

Risk Attitudes and Job Contact Networks: Theory and Simulation

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Abstract

A substantial theoretical and empirical literature demonstrates the important role that risk attitudes can and do play in determining labor market outcomes. Studies have connected risk preference to, for example, labor market entry and occupational choice, entrepreneurial activity, investment in education or the setting of reservation wages. To the best of our knowledge, however, the impact of risk attitudes on investment in job contact networks has been unexplored. This is unfortunate, as one important way to insure against unemployment is by using connections to acquire information about job opportunities. Extending recent theory by Galeotti and Merlino (2010), we show that more risk-averse individuals develop networks with a greater number of connections, and that this can have significant impact on employment and wage outcomes. We provide a Monte Carlo analysis that highlights empirical challenges associated with drawing inference with respect to the model's parameters. Empirical research on the endogenous formation of job contact networks promises to shed new light on sources of wage gaps and other forms of inequality, while at the same time providing new approaches to addressing discrimination and related sources of inefficiency.