

Networks and Social Capital in Peruvian Shantytowns

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Abstract:

Does social capital embedded in a networks facilitate informal transactions? We estimate a model of network-based trust using observational and experimental data from Peruvian shantytowns and obtain three main results. (1) Networks matter: the ability to borrow from a direct as opposed to an indirect friend is equivalent to a 5 percentage point change in the interest rate. (2) Both direct and indirect network connections increase the likelihood of informal loans. (3) This network effect is primarily driven by strong ties where the parties spend much time together. Taken together, these results suggest that dense networks and bonding social capital are important for informal transactions. 2

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