SOCIETY

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Why are Minnesota and its neighbors alike?

BY JOHN PHELAN

This article is an adaptation of John Phelan's 2023 report "The X Factor? Social capital and economic well-being: A quantitative analysis."

Minnesota and its neighbors operate a range of different economic policies. Our state imposes some of the highest income taxes in the United States, ranking 43rd on the Tax Foundation's State Business Tax Climate Index for 2019; South Dakota, by contrast, imposes no income tax and ranks 3rd. And yet, both states see similar, high outcomes for the share of the population employed. In 2019, Minnesota ranked 3rd in the United States and South Dakota ranked 5th.

There is, then, something besides state government policy driving these high rates of employment. And, given the statistically significant and positive relationship across states between the employment ratio and a standard measure of economic well-being like median household income, this "something" also plays a role in driving economic well-being. If we want to understand why some states have higher levels of economic well-being than others, it seems important to identify and understand this "something." That is what we do in American Experiment's new report "The X-Factor? Social capital and economic well-being: A quantitative analysis."

The suspect:

Social capital

While much of my time is spent analyzing economic outcomes, economics doesn't operate in a vacuum; cultural, societal, and economic conditions often converge in ways that are difficult to quantify. One day, I saw a report titled "The Geography of Social Capital in America," which contained a map of the United States denoted by each state's level of "social capital." I was struck by the apparent overlap between states with high employment ratios and states with higher levels of social capital. It was more than apparent: Levels of social capital are statistically significantly and positively related to levels of employment. Is social capital that "something"?

What is social capital? Harvard political scientist Robert D. Putnam did more than anyone to popularize the concept with his 2000 book *Bowling Alone: The Collapse and Revival of American Community.* In it, he defined social capital as "connections among individuals — social networks and the norms of reciprocity and trustworthiness that arise from them." Networks and norms, in other words. The academic John Field elaborates: "The more people you know [networks], and the more you share a common outlook with them [norms], the richer you are in social capital."

Why would higher levels of social capital enhance economic well-being? Consider a key ingredient of social capital: trust. People are more likely to do business with people they trust than with people they do not. And, if they do business with people they do not trust, they are likely to do so only at a higher "transaction cost," insisting on reassurances they would not insist on with a person they trust. This is why, for example, a country like Italy, which has relatively low levels of trust for a rich country, sees a higher share of family-owned businesses; these are the only people you can trust. This imposes an economic cost, however. If you are only looking to your family for people to deal with, you are drawing on a much smaller pool and will exclude many qualified people. Indeed, a large body of empirical literature has found that higher levels of social capital in a community are associated with higher levels of employment and a greater ability for entrepreneurs to identify and exploit business opportunities and access financing.

"Networks" are quantitative and neutral, in that they can be put to uses that are either socially beneficial — like the Lions Club — or socially harmful, like the Mafia. Membership of both increases "the [number of] people you know," but while many would argue that membership of the former was a positive for society overall, few would make that argument about membership of the latter.

"Norms" are qualitative and *non*-neutral. While the number of people you know can be either a good thing or a bad thing, socially speaking, *from the point of view of economic well-being* — no moral judgment is made here — some norms are better than others. The economist Oded Galor writes in his recent book *The Journey of Humanity: The Origins of Wealth and Inequality*:

> *Cultural traits — the shared values, norms, beliefs and preferences that prevail in a society and are transmitted across the generations — have often made a significant impact on a society's development process. In particular, aspects of culture that dispose populations towards or away from the maintenance of strong family ties, interpersonal trust, individualism, future*

orientation and investment in human capital have considerable long-term economic implications.

The trial:

Exploring the link between social capital and economic well-being in America

We established a relationship between higher levels of social capital and higher levels of employment. We also established a relationship between higher levels of employment and higher levels of economic well-being, measured by median household income. What, then, is the direct relationship between levels of social capital and levels of median household income?

Our hypothesis is that a higher level of social capital in an area is associated with higher levels of economic well-being. The null hypothesis to be tested is, then, that there is no relationship between levels of social capital and median household income.

First, one must quantify social capital, and that is no easy task. Several attempts have been made at the state level, starting with Putnam in *Bowling Alone*, but these often rely on responses to surveys designed to get the views of the average American, not the average resident of a particular state. More recently, others define social capital rather narrowly, focusing mostly on Putnamesque measures of "cohesiveness" like membership of, yes, bowling centers.

Which brings us back to "The Geography of Social Capital in America," produced by the Social Capital Project, which is run by the Joint Economic Committee of the U.S. Congress. They created an index of social capital at both the state and county level. They have a broad definition:

> *In our understanding of social capital, close and nurturing relationships with other people almost self-evidently provide benefits. Therefore social capital is likely to be "greater" or more productive in families, communities, and organizations with an abundance of close, supportive relationships. Social capital is also likely to be reflected in cooperative activities. These activities may be informal (e.g. conversing or working together with neighbors), or formal (e.g. membership in groups or service on a committee). Some cooperative activities may be formalized in institutions (e.g. governments, schools, news media, corporations), including nonprofit organizations specifically meant to deliver benefits or to represent interests. Social capital is also reflected in trust in other people, confidence in institutions, mutual generosity, high collective efficacy, and low social disorganization. In our view, places where these features of social life come together have "high," or "more," or more productive social capital — features of social life that provide benefits to community and family members. Places with a dearth of these features have "low," or "less," or less productive social capital.*

A large body of empirical literature has found that higher levels of social capital in a community are associated with higher levels of employment and a greater ability for entrepreneurs to identify and exploit business opportunities and access financing.

Even better, the indexes have sub-indices so we can look beneath the relationship between social capital and economic well-being and at the relationship between various *components* of social capital and economic well-being. To test our hypothesis, we use the county-level index, which gives us 2,897 observations.

The four sub-indices — the explanatory (factor/independent) variables in our analysis — are: Family Unity, which comprises "the share of births that are to unwed mothers," "the percentage of children living in families headed by a single parent," and "the percentage of women ages 35-44 who are married (and not separated)"; Community Health, which comprises "non-religious nonprofits per capita," "congregations per capita," and "the informal civil society subindex"; Institutional Health, which comprises "presidential voting rates," "census response rates," and "the confidence subindex"; and Collective Efficacy, which comprises "the violent crime rate."

Our measure of economic well-being — our response (outcome/dependent) variable — is the median

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household income for each county. We also include controls for county size and metropolitan status.

The results of our multiple panel regression measuring the impact of our four explanatory variables — the components of social capital at the county level — and our controls for county size and metropolitan status on levels of median household income show that three of them have both statistically significant and positive relationships: Community Health, Institutional Health, and Family Unity. We can reject the null hypothesis that there is no relationship. Hitherto, results from the research into the relationship between levels of social capital and economic well-being at the macro-level have been, according to Field, "suggestive rather than conclusive." Our results make less suggestive and more conclusive the case that higher levels of social capital are associated with greater economic well-being at the macro-level.

The sentence:

Can policy build social capital?

Having found a statistically significant and positive relationship between levels of social capital and economic well-being, we can ask whether policy can grow social capital with the aim of boosting economic well-being.

There is a great deal of skepticism among social capital scholars on this point. They argue that social capital evolves, it is not created. For Putnam, the development of social capital was unplanned; it is a "by-product of singing groups and soccer clubs."

In addition, are these relationships between components of social capital and economic well-being causal? When we look at Institutional Health, for example, research tends to suggest that people vote in presidential elections at higher rates because they are rich, not that they are rich because they vote at higher rates.

Even where a causal link is clearer, as with Community Health, there is debate about the exact state of social capital in America. In *Bowling Alone*, Putnam famously argued that social capital in the United States was in precipitous decline, pointing to declining rates of membership in voluntary associations, rates of voting, newspaper readership, reciprocal helpfulness, sociability, trust, and trustworthiness while identifying television as the leading cause. Others argued that social capital was not declining, it was simply changing. "Rather than joining groups in our neighborhoods, like bowling leagues" the Organisation for Economic Co-operation and Development writes, "we're now joining groups made up of people who share our beliefs — fighting for environmental protection or gay rights, for instance — rather than our locality. These groups — such as a branch of Greenpeace or Amnesty International — can exist in the 'real' world. But they may also exist only virtually on the Internet, which is arguably creating whole new 'communities' of people who may never physically meet but who share common values and interests."

Our results make less suggestive and more conclusive the case that higher levels of social capital **are associated with greater economic well-being at the macro-level.**

Putnam, in response, argues that this is a poor substitute for older forms of social capital.

For our third statistically significant and positive variable, Family Unity, however, the causal link is clear, and so is the situation in America.

The share of married adults has plummeted ("the percentage of women ages 35-44 who are married" in our sub-indices) and the declines have been greatest among those Americans with lower incomes and those belonging to minority ethnic communities, with the notable exception of Asian Americans. This decline in two-earner households has exerted a downward pressure on household incomes, especially among those Americans who have seen higher rates of "family fragmentation," driving increased rates of income inequality.

More important is the explosion in single parenthood ("the share of births that are to unwed mothers" and "the percentage of children living in families headed by a single parent"). Between 1980 and 2019, the share of children in the United States who lived with married parents fell from 77 percent to 63 percent. More than one in five American children now live in a home with a mother who is neither married nor cohabiting. As economist Melissa S. Kearney writes in her book *The Two-Parent Privilege: How Americans Stopped Getting Married and Started Falling Behind*, single parents have both less time and, on average, less income to devote to their children than married parents, with the result that the children of single parents are more likely to struggle at school and later in life. Again, these declines have been greater among those Americans with lower incomes and those belonging to minority ethnic communities, again with the notable exception of Asian Americans, again contributing to increased income inequality.

Research offers two leading causes. One is a decline in "marriageable men" as the decline of manufacturing employment removes a source of well-paid work for unskilled men making them less appealing as marriage partners. The other is a change in social norms, "away from the maintenance of strong family ties," in Galor's words. What can policy do about either of those?

This decline in a key component of social capital been described as "the biggest problem we have," "the largest or second-largest problem in America," and the "shadow behind all sorts of other problems that people are much more easily conversant about." With new books from prominent social scientists such as Kearney and Richard V. Reeves as well as a forthcoming book by Brad Wilcox, "family fragmentation" — the opposite of Family Unity — is earning much attention. Having been a focus of Center of the American Experiment since its founding in 1990, we are well-placed to contribute. If our new report offers more problems than solutions, that is a vital first step. ★