Heterogeneous Peer Effects and Rank Concerns: Theory and Evidence

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Abstract

Much evidence exists of heterogeneous and non-linear ability peer effects in test scores. However, little is known about the mechanisms that generate them and whether this evidence can be used to improve the organization of classrooms. This paper is the first to study student rank concerns as a mechanism behind ability peer effects. First, it uses a theoretical model where students care about their achievement relative to that of their peers to derive predictions on the shape of peer effects. Second, it proposes a new method to identify heterogeneous and non-linear peer effects. Third, it tests the theoretical predictions in a novel empirical setting that uses the Chilean 2010 earthquake as a natural experiment. The results indicate that rank concerns generate peer effects among Chilean 8th graders. An important implication is that educators can exploit the incentives generated by academic competition when choosing classroom assignment rules.

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