Abstract

Over one third of college students decide to switch majors; and since students’ beliefs about their expected labor market returns are a determinant of their major choice, shocks to these beliefs likely play a role in their decision to switch majors. For example, sophomore engineering majors at UT Austin were 40% more likely to switch majors during the 2001-01 recession, when the unemployment rate for engineering graduates increased to double that of the average college graduate. However, typical models of major choice are unable to explain this behavior because they assume students’ beliefs follow rational expectations. Hence, engineering students would correctly predict that the unemployment rate would recover by their expected graduation in 2004-05. This paper is the first to explain why students switch majors in response to labor market shocks by more flexibly modeling their beliefs, including how persistent they believe labor market shocks will be. I show that students’ choices are consistent with beliefs that the shock to the unemployment rate is highly persistent, and use simulations to illustrate the impact that beliefs have on students’ welfare. In particular, giving students rational expectations reduces the probability that they switch out of engineering during the recession by 7.5% and increases the expected earnings of sophomore engineering students by $1.35m.

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