How much can asset portfolios of rural households benefit from formal financial services?

Discussion

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Central idea, key contribution

- Measurement of household portfolio in developing countries is extremely hard.
- Peering into the asset composition of poor households important for several reasons:
  1. Role of access to financial services.
  2. Extent of under-diversification
  3. Potential contribution of risk-mitigating strategies
- What the authors do: At the same levels of risk, what would be the returns to the household **had they purchased specific financial products?**
- Key contribution: Stylised facts, quantify gains from financial assets in a representative household's portfolio in India.

Stylised facts about a household portfolio

- Is housing an asset for a low-income household, or is it a "consumption" asset?
  Roof over one's head regardless of labour income is risk mitigating?
- Jewellery is hardly ever sold. It is used as an underlying for a loan. What about existing loans?
- What about access to informal sources of finance: We know a lot about the household's assets so far, but the liabilities are not explored.
  Important to know what fraction of assets can be pledged, for instance.
- Is education investment or expenditure? A provocative thought:
  Education is an investment if social structure expects children to take care of parents in the old age - a crude pension scheme?
- A well thought through categorisation is a great contribution to Indian household finance discourse.

Mitigating labour income risk

Table 4: Stylised Asset Portfolios

Asset category	**Agriculture-Only**	**Labour-Only**	**Salaried-Agriculture**	**Business-Agriculture**	**Labour-Agriculture**
Electronics	7,000	7,000	7,000	7,000	7,000
House	99,000	63,000	225,000	225,000	99,000
Vehicle	1,250	1,250	-	-	1,250
Consumption assets (total)	*107,250*	*71,250*	*232,000*	*232,000*	*107,250*
Agricultural-equipment	2,500	-	5,500	5,500	2,000
Investment	-	-	-	-	-
Jewellery	110,400	66,240	64,384	96,576	66,240
Land	200,000	-	130,000	140,000	120,000
Livestock	20,000	300	25,000	25,000	20,300
Shop	-	-	-	-	-
Investment assets (total)	*332,900*	*66,540*	*224,884*	*267,076*	*208,540*
Investment assets (as % of all assets)	*75.63%*	*48.29%*	*49.22%*	*53.51%*	*66.04%*
All assets (Total)	**440,150**	**137,790**	**456,884**	**499,076**	**315,790**

The hypothetical portfolio

- Livestock insurance, rainfall insurance, a suite of products such as ETFs, government securities
- Households don't always pick risk-mitigating products. This is the "ideal" world.
- Claim: Salaried-Agriculture portfolio witnesses reduction in risk, and increase in returns
- Show paired t-test of differences in mean before and after introduction of financial assets.

Policy implications

- Implications in the paper do not flow from the study.
- Two part assumption, untested, to imply policy suggestion:
  1. Only hindrance for the hypothetical portfolio from being realised is access to finance.
  2. All households trust financial institutions with their money.
- Normative vs. positive statements

A few suggestions

- Self-reported income information notoriously bad
  Compare income distribution with existing survey information from this region
- Are these portfolios constructed **before** the investor is offered products by this financial service provider? If not, very important to do so.
- Small, medium and large households. Return variation across income size of households: How does risk mitigation help across the income distribution?
- Ideal setting for this study: Study the household's returns before and after the financial services provider started providing services. More ideal would be to randomly roll out access with a baseline and post rollout survey with the data provider!