What Drives Rural Household Savings? Evidence from an Emerging Economy

Keywords: Financial Inclusion, Household Savings, Financial Literacy, Joint liability Groups.

JEL Codes: D14, O16, Q12

Abstract

Household savings provide the resources needed in an economy to fund investment activity in both the public and private sectors. When efficiently inter-mediated through the financial system, savings are channelized for most productive deployment, thereby supporting economic growth and development. Although income and interest rate are considered the two key determinants of household savings, financial inclusion and financial literacy also play a role in influencing the savings behavior of households (Bruhn and Love, 2014).

Understanding the factors that drive or hinder the savings behavior of households is essential to design effective policies to mobilize adequate savings. Even in well- developed financial systems, certain segments of the population may remain excluded from formal financial services (Pais and Sarma, 2018). These aspects of human development fall under the broader concept of *financial inclusion*. Financial inclusion goes beyond having access to and using payment and savings accounts; it also encompasses access to credit, insurance, pension products, and securities markets with- out facing barriers, whether they are related to price or not. It has a direct implication on broader sustainability goals as defined by the United Nations[1]. This inclusion may allow individuals to invest in education, save for retirement, pursue business opportunities, and manage financial risks through formal insurance products (Demirgu¨c¸-Kunt and Singer, 2017; Sahay et al., 2015). Studies have shown that financially included individuals are not always financially literate, and conversely, some financially literate individuals may not be financially included. Empirical research indicates mixed findings. Some studies suggest that financial education leads to increased savings over a person's lifetime (Bernheim et al., 1998; Lusardi, 2003), while others have found no conclusive evidence that financial education im- proves personal financial decisions (Mandell, 2006; O'Connell, 2009). The results are conflicting and hinder policy making. Certainly, policy-level interventions on financial inclusion have been studied in the context of developed countries (Kempson et al., 2004), however, its applicability in emerging economies still needs to be studied in detail.

From an emerging economy perspective, India serves as a crucial test case. With about 65% of the population still residing in the

[1]For more information, please refer: https://www.uncdf.org/

rural area[2] it provides an ideal setting to study aspects of financial inclusion in the larger area of economic development. The Government of India has made significant efforts to reduce poverty, achieving notable success in reducing poverty, yet a substantial portion of its population is classified as poor[3]. In this context, we try to understand the factors that affect savings behavior in India, specifically in the rural context.

Using a large cross-sectional survey conducted by the National Bank for Rural and Agricultural Development (NABARD), the apex body overseeing rural banking in India, we analyze rural household data to identify determinants of household savings as part of the financial inclusion assessment. We essentially ask two pertinent questions:

- What are the determinants that enable household savings?
- Once savings occur, what are the determinants that impact the quantum of savings?

We approach this problem using a double hurdle model where the first hurdle refers to the factors that are responsible for the savings. This allows us to use a logistic regression model. Our model at the first hurdle shows that households led by women save more often compared to men, larger households and reserved category households do more saving and social security measures like insurance and pension support savings.

The second hurdle focuses on the quantum of savings. Using quantile regression, we found that the factors that impact the quantum of savings vary in size and significance across the data set. This verifies the non- linear nature of household savings (Emara and Kasa, 2021). On comparing the first hurdle with the second hurdle, we found that the amount of money saved by men is higher compared to women. This is an interesting finding that highlights the difference in earning potential and psychological tendencies between sexes. Although education of the household may not be responsible for inducing saving, it is responsible for doing higher savings in instances of its occurrence. If one is member of a Self Help Group (SHG) or a cooperative, as per first hurdle, chances of savings go up, but the quantum of savings go down indicating shared risk paradigm.

To verify our findings, we divided the entire dataset on the basis of household type, i.e., agricultural and non- agricultural. In both data sets, we ran the logistic model (for the first hurdle) and quantile regression (for the second hurdle) and found convergence with our larger household findings.

The findings of this analysis make significant contributions to the broader discourse on financial inclusion by providing a nuanced understanding of how socioeconomic, demographic, and asset-based factors influence financial well-being in agricultural and non-agricultural households. This study contributes to the debate on whether financial inclusion policies adequately address the challenges faced by the most vulnerable, particularly in rural environments where income disparities are more pronounced.

[2] For more information, please refer: https://www.indiabudget.gov.in/
[3] For more information, please refer: https://www.niti.gov.in/