



REMITTANCES, BANCARIZATION AND THE DEMAND FOR INSURING SCHEMES

Dorothee Crayen - University of Tübingen

Christa Hainz - Ifo Institute for Economic Research,
Munich

**Christiane Ströh de Martínez - Free University of
Berlin**

Dakar, 4th November 2009

CONTENT

1. Introduction
2. Risk management strategies of low-income population
3. Usage patterns of financial services in South Africa
4. Hypothesis and related results
5. Summary and reflections

1. INTRODUCTION

...ACCESS TO RISK MANAGEMENT STRATEGIES ARE IMPORTANT FOR SUSTAINED POVERTY REDUCTION

- Lack of comprehensive or mandatory social security systems in many developing countries
- Exposure to risk is often higher for poor/ low-income households
- Low and fluctuating income streams make risk coping difficult for low-income population
- The way out of/ into poverty can be seen as a zig-zag route
- Households use different and interrelated strategies for dealing with risk

OUR RESEARCH

- FinScope™ surveys from South Africa as a unique and data base, providing representative information on
 - Usage of formal and informal financial instruments
 - Preferences regarding risk management strategies
 - Sources and level of income, including remittances
- In South Africa, funeral insurances are one of the mostly used financial instruments
- We explore the effect of various types of financial arrangements on demand for insurance/ insuring

2. RISK MANAGEMENT STRATEGIES OF LOW-INCOME POPULATION

LOW-INCOME HOUSEHOLDS OFTEN USE COMBINED STRATEGIES FOR MANAGING RISK

First stage mechanisms

- Ex-ante arrangements for influencing the exposure to risk before it occurs
 - Conservative production decisions
 - Diversifying income sources

Second stage mechanisms

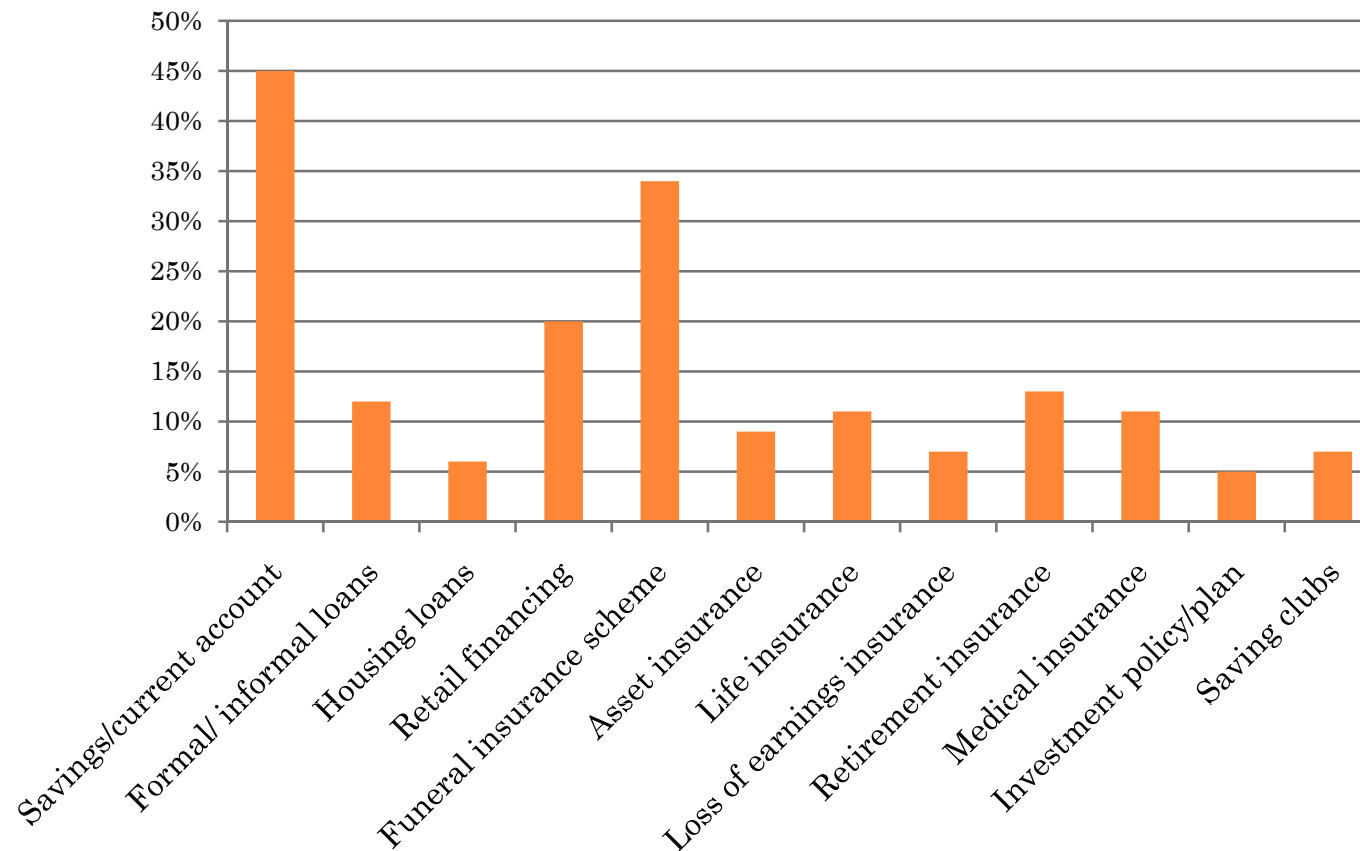
- Ex-ante mechanisms for dealing with damage
 - Saving
 - Formal and informal insurance schemes
- Ex-post mechanisms for coping with the damage
 - Borrowing
 - Receiving remittances
 - Lower consumption level
 - Higher labour level

EX-ANTE AND EX-POST MECHANISMS FOR DEALING WITH DAMAGE CAN ALSO BE SUBSTITUTES

- Besides combined strategies, ex-ante and ex-post mechanisms can be substitutes
- Remittances can also act like insurance and influence other risk coping strategies
 - Income effect: providing additional income for purchasing insurances
 - Substitution effect: acting as an insurance
- Financial function of insuring can be fulfilled not only by insurances products

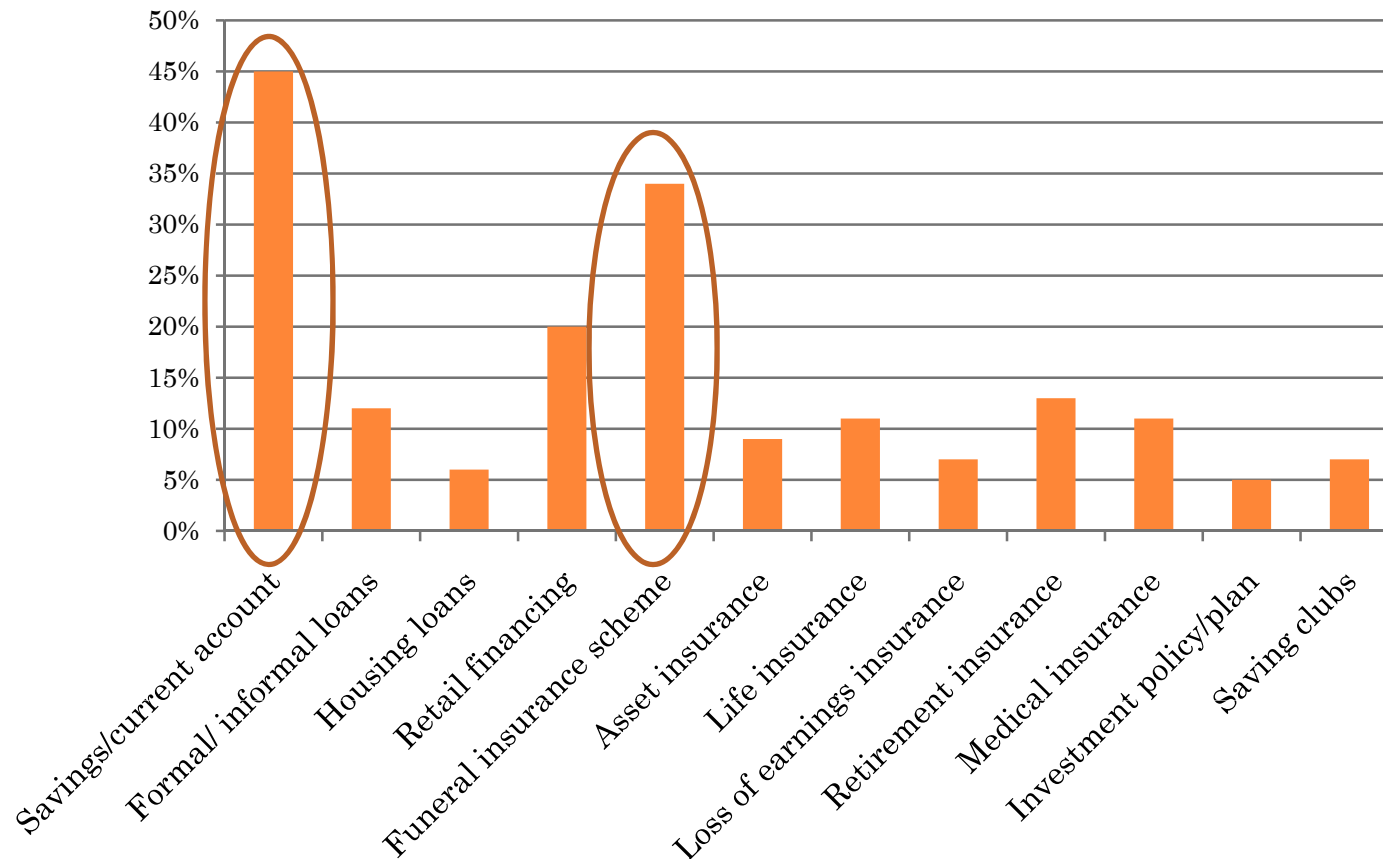
3. USAGE PATTERNS OF FINANCIAL SERVICES IN SOUTH AFRICA

USAGE OF DIFFERENT TYPES OF FINANCIAL INSTRUMENTS IN SOUTH AFRICA



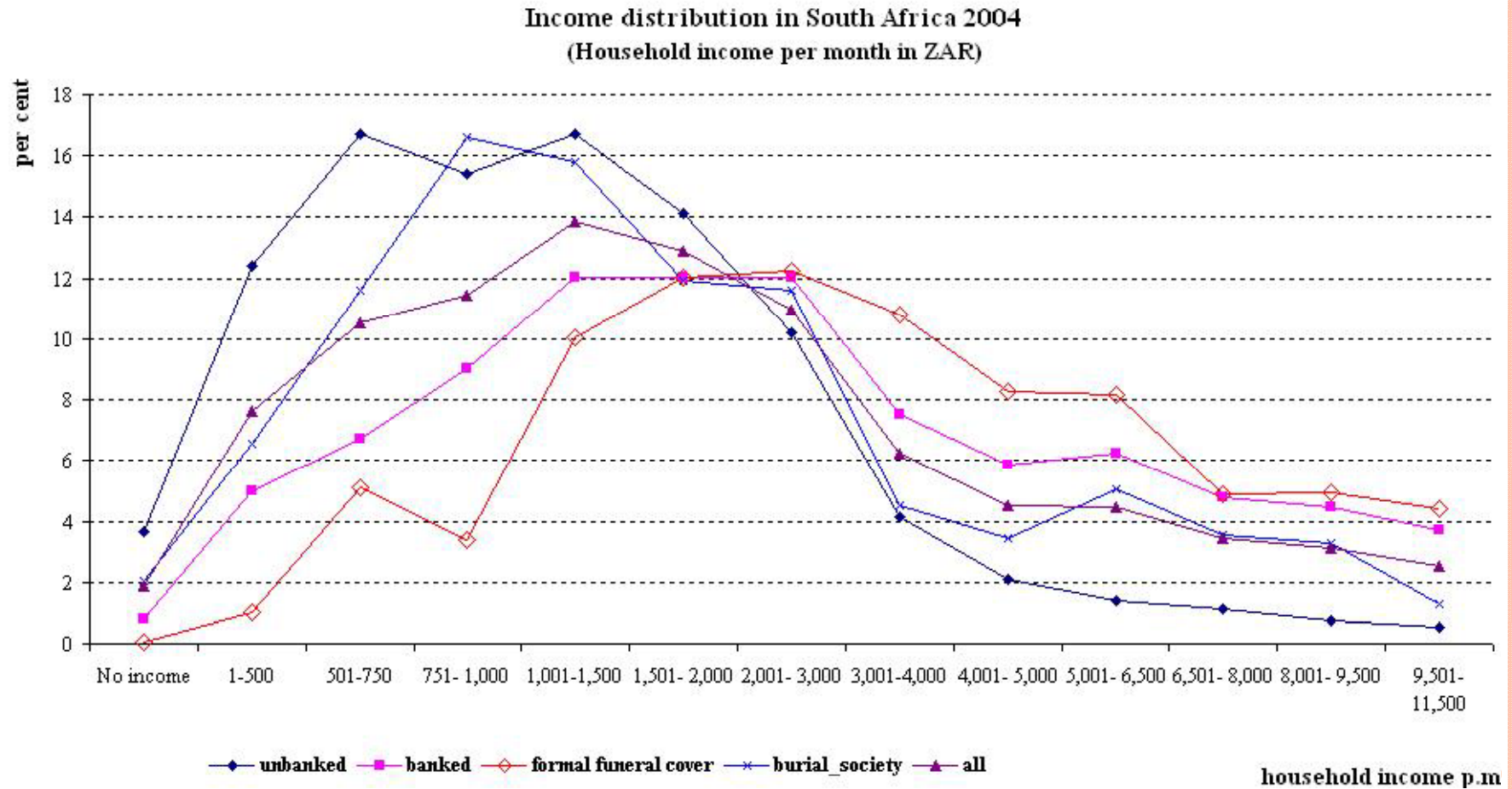
Source: Own elaboration on Finscope data (2004)

USAGE OF DIFFERENT TYPES OF FINANCIAL INSTRUMENTS IN SOUTH AFRICA



Source: Own elaboration on Finscope data (2004)

INCOME DISTRIBUTION BY BANKING STATUS AND FUNERAL COVER (IN %)

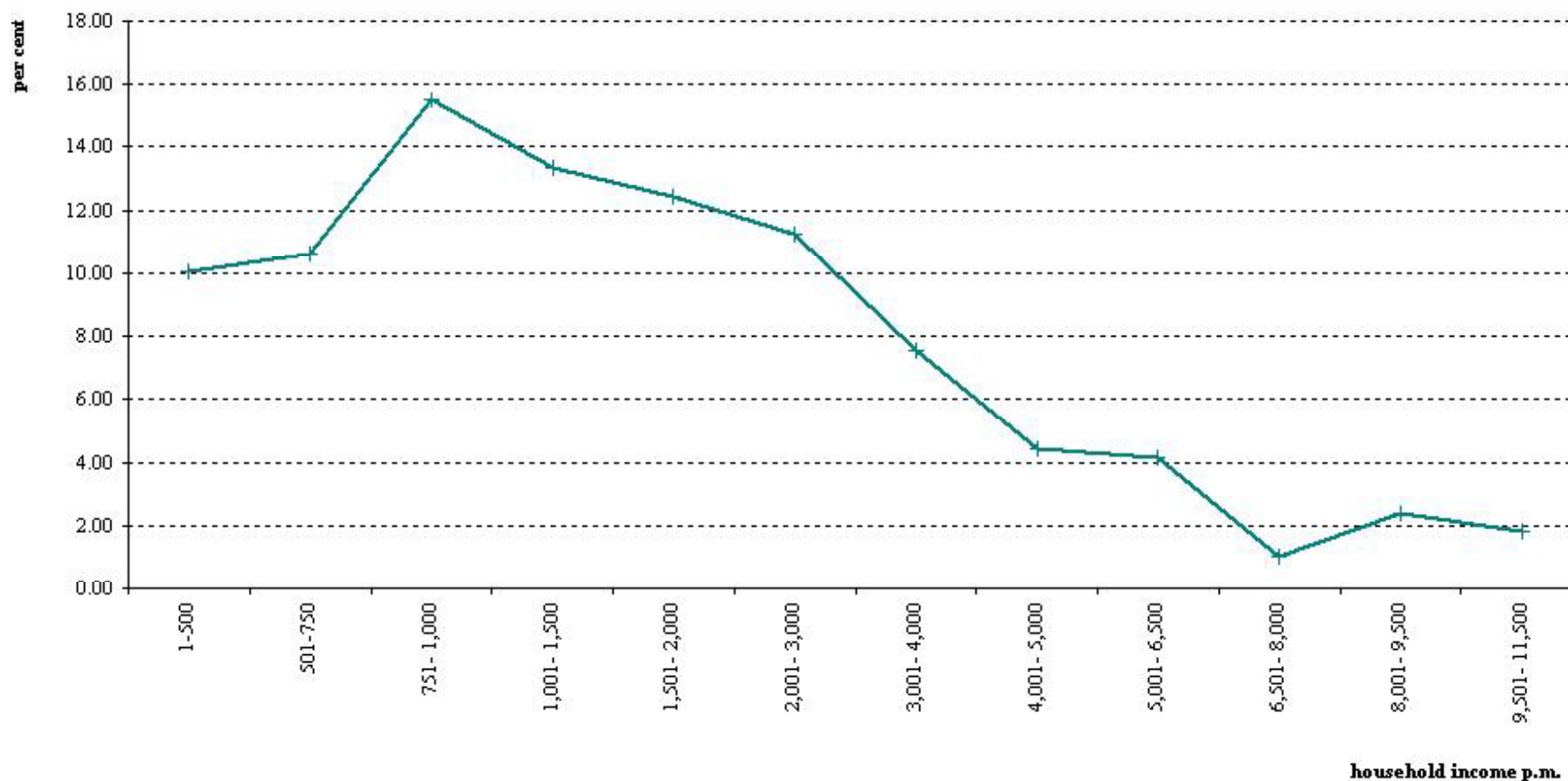


Source: Own elaboration on Finscope data (2004)

Note: The income categories above 11,500 ZAR per month contain less than 1 per cent of the sample

REMITTANCES AS SOURCE OF INCOME BY MONTHLY HOUSEHOLD INCOME (IN%)

Share of respondents receiving remittances by income group (in per cent)
(Household income per month in ZAR)



Source: Own elaboration on Finscope data (2004)

Note: The income categories above 11,500 ZAR per month contain less than 1 per cent of the sample

EVIDENCE FROM FINANCIAL DIARIES

(IN-DEPTH STUDY WITH LOW-INCOME HOUSEHOLDS,
SAMPLE IS NOT REPRESENTATIVE)

- Average of 17 different financial instruments (informal & formal) used
- 75% of respondents held one, more than 50% two funeral covers → spending 3% of monthly income
- Payouts from funeral cover/ burial society have to be complemented by remittances, contributions by relatives, savings or loans
- Burial societies offer additional moral and practical support

4. HYPOTHESIS AND RELATED RESULTS

REGRESSION FRAMEWORK IN BRIEF

- Probability of having a formal funeral cover/ burial society membership modelled as a maximum-likelihood logit function
 - of both individual and household characteristics
 - and income, banking and risk coping information
- Separate regressions for the formal and the informal arrangements were run (alternative dependent variables)
- All models estimated using sampling weights as provided by FinMark Trust
- Robust standard errors reported to account for heteroskedasticity

INCOME EFFECT POSITIVE FOR POSSESSING FORMAL FUNERAL COVER?

Hypothesis 1: A household is more likely to possess formal funeral cover if its income is higher.

Results:

- Household income increases the demand for formal insurance
- Effect decreases with higher levels of income
- Considering only households with highest incomes, effect is still stronger
- Higher education level also increases probability for having formal funeral cover

(Please confer our paper for detailed regression result tables)

SUBSTITUTION EFFECT DOMINATES INCOME EFFECT FOR REMITTANCES?

Hypothesis 2: A household is less likely to possess formal funeral cover if its receives remittances.

Results:

- Remittances receiving household are less likely to have a formal funeral cover
- Substitution effect dominates in all specifications, even if no control for income is included
- Education also enhances the propensity of buying formal funeral cover in remittances receiving household

OTHER (INFORMAL) COPING MECHANISMS USED AS SUBSTITUTES TO FORMAL FUNERAL COVER?

Hypothesis 3: A household is less likely to possess formal funeral cover if it intends to take an informal loan to smooth an income shock.

Results:

- Respondents inclined to deal with occurrences with informal loan are less likely to have a formal funeral cover (even more if risk perception is considered)
- Respondents inclined to use insurances are more likely to have formal funeral cover
- Perceptions on high household-related risk increase the probability of holding formal funeral cover.

DOES BANCARIZATION STATUS MATTER? AND WHAT ABOUT THE PROBABILITY OF MEMBERSHIP IN BURIAL SOCIETIES?

Hypothesis 4: A household is more likely to possess formal funeral cover but not to join a burial society if it regularly interacts with a bank.

Results:

- Being banked increases the probability of having a formal funeral cover three times more than joining a burial society
- Income effect is much weaker for burial society than for formal funeral cover (not significant if controlled for familiarity with banking system)
- No systematic influence of education for joining a burial society
- Receiving remittances does not influence the decision on joining a burial society

5. SUMMARY AND CONCLUSIONS

SUMMARIZING RESULTS

1. Remittances acts as substitute for formal insurance
2. Other risk management strategies also act as substitutes (informal loan – funeral cover)
3. Insurance character of remittances does not interact with the membership in a burial society - different decision criteria
4. Banking status matters for formal financial services

REFLECTING ON RESULTS

- Importance and variety of financial instruments for managing risk and dealing with damage
 - Many microfinance providers still lack to offer specific and differentiated risk management services
- Combinations of formal and informal financial arrangements are used by low-income populations (also for insuring)
 - Informal arrangements and should be considered for designing tailor-made microfinance services and products
- The decision taking for acquiring a formal or informal insurance mechanism differs fundamentally
 - In the case of insurances arrangements, trust and non-monetary services might play an important role
 - Formal insurance providers should focus on their reliability

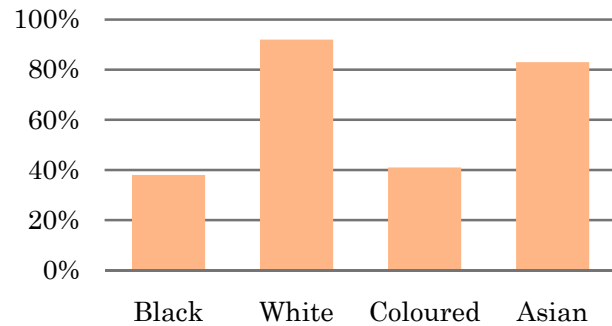
THANK YOU VERY MUCH FOR YOUR ATTENTION
AND LOOKING FORWARD TO YOUR COMMENTS!!

CHRISTIANE STRÖH DE MARTÍNEZ
FREE UNIVERSITY OF BERLIN
CHRISTIANE.STROEH@GMX.DE

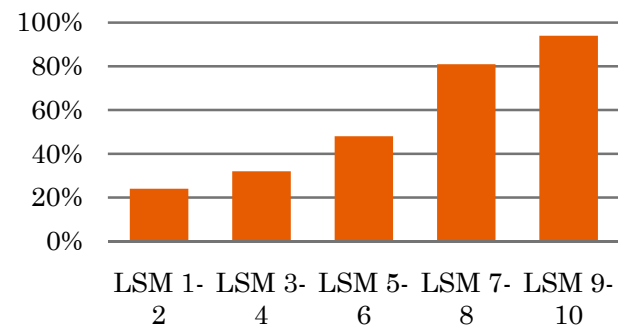
FURTHER MATERIALS FOR THE
PRESENTATION (IF NEEDED)

BANCARIZATION STATUS BY POPULATION PROFILE

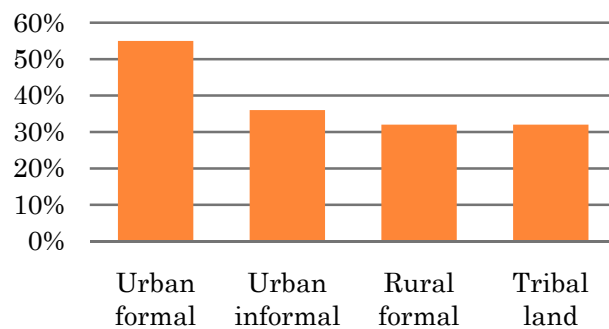
Bancarization status by race



Bancarization status by LSM



Bancarization status by area



Source: Own elaboration on Finscope data (2004)