

# Household Finance Research Initiative

## *Strategy Note*

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### **1. SCOPE OF WORK**

Household finance is an emerging academic discipline at the intersection of economics, finance, development and behavioural studies. We identify with Tufano (2009)'s comprehensive description of the field as “the study of how institutions and provide goods and services to satisfy the financial functions of households, how consumers make financial decisions, and how government action affects the provision of financial services”. This definition underscores our firm belief that individuals and households cannot be meaningfully studied in isolation from the context they operate in, and without understanding their interactions with various socio-economic and institutional actors including informal and formal and informal advisors, providers, and regulators.

Even though an emerging field, household finance leans heavily on a rich academic history in asset pricing, corporate finance and behavioural economics; and additionally, on the studies of poverty, socioeconomic development, financial market development and financial inclusion in developing countries. Thematic reviews of the field (Campbell 2006, Tufano 2009, Guiso and Sodini 2013 and Sane 2016) organize and classify the body of relevant work both by themes and tools. In terms of themes, the research is broadly classified as:

- (a) Analysis of financial statements such as Household Balance sheets, Income and Expense statements and Cashflow statements. These include the study of portfolio composition, asset allocation, home ownership, trends in wealth accumulation and distribution, income dynamics, cashflow volatility and consumption smoothing.
- (b) Analysis of borrowing behaviour including studies on the availability of credit to various household types, terms and features of various product types, consumer attitudes towards debt, use of credit, returns to credit and as well, issues in over-indebtedness.
- (c) Analysis of savings and investment behaviour including attitudes towards risk, available investment choices and barriers to access them, participation in investment markets and risk diversification, return maximization and life-cycle optimality of the overall portfolio for various household types.

(d) Characterization of financial *mistakes* of consumers and *mis-sales* by providers and evidence-based design to prevent consumer harms.

(e) Study the modes of transactions and preferred means of payments for various use cases.

There is a strong motivation to establish household finance as a thriving academic discipline in India. Indian financial inclusion policy has primarily focused on supply-side initiatives, employing either mandates, channel regulations or standardized product design<sup>1</sup> to deliver incremental supply. The design of this approach seems to implicitly assume either that last-mile consumers are homogeneous or that— even if they are heterogenous— there is sufficient capacity among practitioners to understand and respond suitably to consumers' needs and circumstances. In other words, this approach to financial inclusion primarily targets the *level* of supply but does little to alter the characteristics, quality and suitability of supplied services.

However, an emerging body of evidence rejects these assumptions, and calls for a more *consumer-aware* and *consumer-centric* system of policymaking. First, not only do households experience heterogeneous financial needs and institutional interactions, their heterogeneity is dynamic over time and unique to their own experiences (Agarwal et al. 2008, Badarinza et al. 2016, Ramadorai 2017). Second, there is evidence to show that particularly with respect to banking, economically or informationally vulnerable families report unsuccessful purchase and negative experiences more frequently (Das 2013, Mowl 2013, Mowl and Boudot 2014). Even when successful at purchase, vulnerable households are more likely to be aggressively mis-sold (Anagol et al. 2017, Halan et al. 2014, Halan and Sane 2016) or experience distressing outcomes from use (Dattasharma et al. 2016, Prathap and Khaitan 2016). This evidence rejects the hypothesis of sufficient capacity within the average practitioner to suitably design and deliver financial services for typically under-served households.

Through the Household Finance Research Initiative, we hope to significantly amplify the efforts of *all* practitioners and policymakers, and devote intellectual capital to solving critical challenges in the design and delivery of financial services that increase financial access, facilitate socioeconomic mobility and ultimately improve well-being in India.

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<sup>1</sup> Priority sector lending targets and FIP village scheme are examples of mandates; the Lead Bank Scheme, guidelines on urban branch licensing in the Social Banking scheme, Banking Correspondent rules are examples of using channel regulation to deliver financial inclusion; No-frills accounts, Jan Dhan account and overdraft, Suraksha Bima Yojana and Atal Pension Yojana are examples of standardized product design.

## 2. OBJECTIVE

The objective of the Household Finance Research Initiative is to catalyze insightful and rigorous research on household finance that is customer-centric while also relevant and responsive to the Indian policy context and financial landscape.

This specific articulation is deliberate:

- **Catalyze** represents our ambition to rapidly accelerate the development of India-focused household finance research both as an academic discipline and within the policy research community
- **Rigorous** and **Insightful** qualify the research output we wish to generate from this initiative. The research must be conceived to comprehensively address chosen research questions, conducted in accordance with best practices and a high standard of ethical and research integrity and ultimately, the research must deliver a clear and deep understanding of the complex behaviour that drives often paradoxical outcomes.
- **Consumer-centric** reflects a strong orientation of the research towards the needs of— and value to— individuals and households as consumers of financial services, regardless of whether the actual subjects of study are consumers, providers or policymakers.
- **Relevant** and **Responsive** are chosen as a reminder to ensure research insights are synthesized and disseminated in a manner that is timely, cognizant of extant policies, regulations and sectoral developments and importantly, in a format that facilitates positive action<sup>2</sup>.

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<sup>2</sup> We are careful in balancing dual goals, and always retain our strong consumer-orientation while also effectively responding to practitioners' and policymakers' realities. A practitioner/policymaker is **not** our 'customer' or 'client' but rather a potential partner in our vision to deliver high-quality services to all individuals and enterprises.

### 3. THE OPPORTUNITY

Since inception, Dvara Research has been both a consumer and producer of household finance research. As a consumer, we have sought to synthesize findings from academic studies and draw implications and recommendations both internally (for our policy research teams as well as all Dvara group companies) and more widely for all parties in the Indian financial system. As authors, and sometimes grant-makers, we have sought to bridge critical knowledge gaps on emergent issues where targeted studies could significantly enhance the direction and quality of decision-making. From this vantage point, we have been able to develop multiple perspectives on the Household Finance Research Initiative may interact with existing institutional structures and communities to meaningfully improve the design and delivery of financial services.

We identify three broad types of constraints to high-quality research in India today: motive, various dimensions of research capacity and an effective feedback mechanism that loops in *all* consumers of the research.

- ***Motive***

Since household finance is an emerging field, its' scope, theory and methods are often not familiar to—or valued by—even trained researchers. Very few economics/finance departments teach a course or module on household finance and even where research students may be familiar with the topic, identifying relevant and rewarding research questions may be a challenge for individuals.

- ***Research capacity***

As Campbell (2006) notes, two primary constraints for researchers in this field are measurement and models. With respect to the former, measurement requires data that is representative, detailed, disaggregated, accurate and (preferably) longitudinal. With respect to the latter, empirical and/or normative household finance typically attempts to measure compliance or deviance of observed financial behaviour with theoretical models (most notably, the work of Merton). To the extent that these models are not revisited and updated, it constraints not only the development of household finance theory but also empirical work.

Other constraints to the conduct of research are the availability of funding (especially for data collection), establishment of research standards and access to an expert community for intellectual exchange and peer review.

- ***Feedback loop***

Perhaps a unique part of the Initiative’s objective is the emphasis on positive action by practitioners or policymakers and tangible outcomes for consumers. This would only be possible if the Indian household finance research origination process and policy generation process are drawn closer together and are mutually informative from early stages.

We understand that this will not occur if left to chance— academic research is seldom communicated in a format and language that is easily understood and actionable by bureaucrats and executives, while the latter’s decision-making process is often opaque.

For the Household Finance Research Initiative to successfully achieve its’ objective, our actions must simultaneously and effectively relieve all three (or more) constraints. For example, we may make a sizeable fund available as research grants to young Indian researchers, but outcomes from this would be limited if they are not also able to access expert advice and guidance on research methods and best practices. Similarly, we may curate a community of renowned academic experts on this topic, but their efforts may be most impactful only if their research speaks to—and is heard during— contemporary decision-making.

Accordingly, we propose the following types of efforts, targeted at relieving each of the constraints identified. In turn, we expect that the outcomes from these effects will not only have an impact on researchers themselves but also on how the research is used to deliver positive outcomes for low-income consumers. These are detailed in Table 1.

Constraints on research	Proposed types of actions	Expected research outcomes	Potential consumer outcomes
<b>Motive</b>			
Scope and research opportunities unfamiliar to wider research community	Commission systematic/thematic reviews of academic developments in the field  Conduct an annual survey of experts to stay updated  Identify, celebrate and widely disseminate good examples of research and impact	More research on Indian household finance, both in Indian and international universities/research centres	
Challenging to identify relevant and rewarding research questions	Featured interviews with experts developing the field in new directions  Learning from our immersion in the Indian financial sector and policy, publish an annual letter to the research community highlighting opportunities for impact through research	There would be multiple studies (i.e. a body of rigorous work) on relevant topics and this would contribute to an evidence-based debate to inform policymaking	
<b>Research capacity</b>			
Insufficient data to support high-quality empirical research	Create a data catalogue of Indian finance datasets (both household-focused and supply-side)  Curate new datasets including both survey and administrative data for research use Publish questionnaires from featured	A growing catalogue of datasets on household financial behaviour, supporting numerous empirical research studies	

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	studies to encourage standardization and best practices in new data collection. Ensure that questionnaires published through the initiative follow best practices, and ask questions such that insights are tangible and actionable		
Insufficient focus on theory development			
Constraints on research funding, especially in Indian institutions/for mixed methods research	Set up a research grant fund with a regular cycle of 1-2 year grants with the objective to provide bridge evidence gaps on specific themes of interest	More research on Indian household finance, both in Indian and international universities/research centres.  Additional funding could ensure that even where data is a constraint, rigorous qualitative work uncovers insights.	The design on financial products, services and policies begin to incorporate qualitative aspects of consumer experiences
Limited access to experts for mentorship or peer review	Studies funded by the Initiative should mandatorily be shortlisted as well as peer-reviewed by a panel of experts	The quality of research produced under the Initiative/ in India is well-regarded	
Need to clearly establish expected standards (in-line with best practices) for research funded under this Initiative	Conduct research and training workshops for young researchers/students at Indian universities	The quality of research produced under the Initiative/ in India is well-regarded	
Limited publishing opportunities	Create avenues for rigorous discussion and publication such as an online peer-reviewed	More research on Indian household finance, both in Indian and international	

Constraints on research	Proposed types of actions	Expected research outcomes	Potential consumer outcomes
	journal on Indian Household Finance. To begin with, we may think of curating/inviting selected pieces to publish a book on the same theme.	universities/research centres.  The quality of research produced under the Initiative is well-regarded	
<b>Feedback loop</b>			
Research origination, review and dissemination processes may not involve practitioners/policymakers (who are also consumers of research for action)	<i>See “Challenging to identify relevant and rewarding research questions” above</i>	More research on Indian household finance, both in Indian and international universities/research centres.	
Bureaucrats and executives may be unfamiliar with relevant research at the time of their decision-making	Disseminate thematic research bulletins and policy memos  Include relevant research in all practitioner/policy conversations	Household finance research is understood, referenced and used in decision-making.	Product features and policies are proactive in addressing and responding to the needs of excluded segments.  Consumers operate in a financial environment that feels secure, suitable and successful.
Insufficient communication between researchers, practitioners and policymakers			
Few opportunities for early-stage policy assessment			

#### **4. ACTION STRATEGY 2018-2020**

In 2018-2020, the Household Finance Research Initiative should consider the following to establish and widely communicate its' vision, objectives and resources.

1. Conduct a stakeholder analysis/community mapping exercise, develop a theory of change and constitute an advisory board that includes representation from all key stakeholder categories
2. Create outputs that add value to the research community and complement existing high-quality research capacity
  - 2.1. Create a data repository of private/administrative datasets on household finance as well as a navigation guide of the extensive public datasets available in India
  - 2.2. Publish a "State of Indian Household Finance" book that exemplifies the varied use cases for the datasets in the repository, features contributed chapters by researchers and also lists open research questions
  - 2.3. Conduct/commission systematic reviews and thematic reviews
  - 2.4. Conduct unique research on under-studied/under-funded topics that bridge critical knowledge gaps
  - 2.5. Create opportunities for research publication/dissemination including a Household Finance conference
3. Research community outreach and engagement
  - 3.1. Publish an 'agenda-setting' annual letter that reviews developments in the Indian financial sector and highlights priority research questions/opportunities for evidence-based policymaking
  - 3.2. Conduct an annual survey of experts to identify and disseminate new developments in the field including new publications, upcoming researchers, methodological innovations etc.
4. Invest in building research capacity in Indian or India-focused international academic institutions
  - 4.1. Award PhD research grants to selected students of Indian academic institutions conducting high-quality research on topics in Household Finance. Also consider matching them to a research mentor at 2 pre-determined stages of the research for quality review and feedback.

- 4.2. Award conference travel grants to young researchers to present their work at a pre-determined list of premier international conferences
  - 4.3. Award 1-year residential fellowships for PhD/Post doc fellows of premier international institutions for an immersive study on a topic in Indian household finance
5. Practitioner and policymaker outreach
- 5.1. Publish research bulletins on relevant themes of interest to various groups
  - 5.2. Invite practitioners and policymakers to actively engage in research dissemination events
  - 5.3. Interview practitioners/policymakers to understand priority areas where new research could be most impactful

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