

# How the savings cookie crumbles

PK GHOSH / PK ROY / MYTHILI BHUSNURMATH



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Savings is no longer a habit in India. However, risk-taking varies, with the South ahead of even the West in equity investments

Indian households have always accounted for the major share of gross domestic savings. But they seem to have lost the savings habit now. You can blame some of that on consumerism. But what explains the fall in the share of their savings in financial instruments? Received wisdom says persistently high inflation since 2009. Years of negative real returns from a host of financial instruments, especially bank deposits, has seen Indian households react in the only way they can – by turning to physical assets, typically gold.

According to the RBI, household savings declined from 25.2 per cent in 2009-10 to 22.3 per cent in 2011-12. Worse, financial savings by households fell to a paltry eight per cent in 2011-12, down from 12 per cent in 2009-10 and 10.4 per cent in 2010-11 even as savings in physical assets rose to touch 14.3 per cent in 2011-12, up from 13.1 per cent in 2010-11.

But savings in financial instruments are the bedrock of a modern financial system. Corporates seeking to raise both equity and debt and governments looking for ways to fund their deficits need finance. Typically this need is met predominantly by savers willing to hold their savings in the form of financial instruments.

What happens if savers turn their face against financial instruments? In countries like India where households account for the major share of savings, the fallout can be disastrous. Not only are banks starved of lendable funds, the resort to gold import has adverse consequences for our balance of payments.

But are households across the country uniformly disenchanted with all financial assets? Or do certain financial assets find more favour than others? Is there a regional pattern to these preferences? Do factors like literacy, income levels and the rural-urban divide play a role in determining people's choices? Not much information is available regarding the distribution of savings by households at the disaggregated level — state-wise, in terms of income decile, rural-urban divide, and so on.

### **Urban-rural divide**

The NCAER's NISHIE (national survey of household income and expenditure) survey 2010-11 provides some interesting insights. First the rural-urban divide. While the average household income in urban areas is almost twice that in rural areas, the average household investment in financial assets in urban areas is thrice that in rural areas.

Savings in bank deposits are the overwhelming favourite in both rural as well as urban areas, with rural households opting to hold 46.7 per cent of their financial assets in bank deposits and urban households following close behind at 44.6 per cent.

When it comes to the second-most popular form of savings, there is a clear divergence between rural and urban areas with rural households preferring insurance to savings in provident funds, both employee and public provident funds as compared to urban households who seem to prefer the latter.

Insurance is a more complicated product than provident fund. But the apparent contradiction is, perhaps, explained by the medical insurance cover extended under programmes such as the Rashtriya Swasthya Bima Yojna in rural areas, while the larger share of the organised work force in urban areas relative to rural areas explains why PF/PPF are the second-most popular form of savings in urban areas.

A state-wise comparison shows households in Punjab, Haryana and Rajasthan have a strong preference for bank deposits, with over 55 per cent of financial assets being held in bank deposits.

In contrast, households in Kerala and Andhra Pradesh hold less than 30 per cent of their savings in bank deposits. Both states have a strong network of bank branches, so poor access to banks may not be the reason why bank deposits are less favoured. The reason, perhaps, lies in the relatively greater share of household savings going towards self-help groups/chit funds and the stock market; yes even in Left-dominated Kerala!

As against the all-India average of just 2.1 per cent of household savings going to the SHGs/chit funds, households in Kerala invested about a fifth of their financial savings in them while the comparable number for households in Andhra was 9.4 per cent.

Again, households in Andhra and Kerala saved about 6.1 and 5.1 per cent of their total financial savings in the stock market as against all-India average of 2.8 per cent. Another interesting finding is that households in Assam, particularly in rural areas, put about one-fifth of their savings in the post office followed by West Bengal which is 10.8 per cent. It may be due to the non-existence of other financial institutions or more trust in government institutions.

### **Impact of literacy**

Does literacy make a difference to how households allocate their savings among different instruments? It would certainly seem so, with more literate households opting to keep less of their savings in the form of cash.

Surprisingly, this inverse relationship seems more pronounced in rural rather than urban areas. The correlation coefficient is -0.66 in the former compared to -0.45 in the latter.

The correlation with stock market investments is much weaker. Higher literacy levels do not seem to be a factor in motivating people to invest in the stock market; though here again, in a rather counter-intuitive finding, the relationship seemed stronger in rural rather than urban areas.

As might be expected, households in Gujarat are more engaged with the stock market than elsewhere in the country.

The surprise, however, is that Gujarat, known for its entrepreneurial culture, does not top the list of states in terms of the share of household savings in the stock market. It ranks number three, well behind Tamil Nadu and Andhra . Maharashtra, the state that houses the financial capital,

Mumbai, comes even further behind at number five. Contrary to the widespread belief of households in the south being conservative, Tamil Nadu, Andhra and Kerala figure in the list of top five states in terms of the share of household savings both in SHG/chit funds and the stock market.

(The writers are with NCAER)

(This article was published in Business Line, Dated 10/3/2014)