Barriers to Household Risk Management: Evidence from India

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Abstract

Why do many households remain exposed to large exogenous sources of non-systematic income risk? We use a series of randomized field experiments in rural India to test the importance of price and non-price factors in the adoption of an innovative rainfall insurance product. Demand is significantly price sensitive, but widespread take-up would not be achieved even if the product offered a payout ratio comparable to U.S. insurance contracts. We present evidence suggesting that lack of trust, liquidity constraints and limited salience are significant non-price frictions that constrain demand. We suggest contract design improvements to mitigate these frictions.

JEL: G22, C93, O16, D14, G11, G20.

Key Words: Insurance, Household Finance, Trust, Liquidity Constraints, Financial Literacy, Economic Development.

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