Analyzing the Impact of Financial Resilience on the Lives of Individuals and Household Post Covid-19 in Indian Economy

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Abstract

Purpose: Economic crisis is a global phenomenon. When the crisis hits, many people are affected. This paper is an attempt to analyze the impact of financial resilience on the lives of individuals and households. In this study we analyze what are common financial shocks that individuals can face and how they tend to cope with this and our recommendations.

Methodology: Literature review and comparative study of consumption and consumer credit across diverse market.

Main Findings: The intensity of the economic crisis may vary from one person to another, depending on the individual financial resilience. Some households are less resilient to financial shocks than others. This may be because they have low levels of savings, have limited access to affordable credit, already hold high levels of debt or lack the skills required to manage household budgets.

Implications: Financial resilience is difficult to estimate because it is a dynamic concept – the ability to recover quickly from an income or expenditure shock. Savings are in anticipation to the challenges face which might hinder the achievement of financial goals, hence there is a scope for new saving/investment products which are more comprehensive in nature.

Novelty: We over a period have witnessed that there is a social support to the society during economic crisis but what is required is organization resilience rather than developing personal capabilities. The resilience should go beyond financial vulnerabilities and encompass mental stability, emotional wellbeing, education attainment etc.

INTRODUCTION

The world is changing rapidly. Information and communication technology are changing the society. Social media and social networking play a great role in influencing political reform, business trends, teenagers' behavior and family relationships. While there are debates on the good and bad sides of the changes, two main concerns are on the rising rate of unemployment including job security, income inequality and debts, and changes to the social integrations. History has shown the relationship between economic turbulence and mental health. (Berkman et al., 2000)

While reports have shown the important roles of social support to the society during economic crisis. (Gilli et al., 2013), it is not of less important for a person to be resilience to face the challenges. However, research in financial resilience shows more focus is emphasized on the organizational resilience, rather than personal capability to cope with economic changes (Torstensson etal., 2014). Similarly, financial literacy has been a subject of investigation in many studies. However, most studies focus the subject as either from the education perspective, (Fernendes etal., 2014) a descriptive study (Almenberg & Dreber, 2015) or how it relates to retirement plan (Boisclair etal., 2017).

As financial literacy is the essence of being financially knowledgeable, how it determines financial resilience is the topic of interest. Therefore, it is of the interest of the researchers to examine the factors influencing the individual financial resilience in coping with the changes.

Household financial shocks can result from loss of employment, reduction in hours of work, ill health of a family member, relationship breakdown, the loss of a partner, damage to household possessions because of flooding or fire, an unexpected large expense, such as a car or home repair bill, the replacement of domestic appliances or an increase in debt interest rates. To cope with these shocks, households need access to sufficient liquid assets or emergency savings, or be able to borrow from financial institutions, wider family, or friends. For those without sufficient liquid assets or emergency savings to cover a financial shock, the effects on financial well-being will be longer lasting as any amount borrowed will have to be repaid along with any interest incurred and borrowing from family and friends can put a strain on these relationships. Paying back any incurred debts will result in a fall in living standards over the period in which repayments are made, with some unable to return to the standard of living they enjoyed prior to the shock.

Interest in financial resilience goes beyond the importance of assessing households' financial vulnerabilities, as financial resilience is associated with several other important outcomes such as emotional well-being, educational attainment, family stability, reliance on the State, and because the effects can extend beyond the direct impact on family members to wider society. In the short-term, financial hardship has an immediate and direct effect on households' consumption and

their ability to cover the cost of basic needs such as the cost of housing, food, utilities, transport, clothing, and essential consumables. This can force families to turn to social security, extended family and friends, food banks, charities, and financial markets/lenders (formal and informal) to cover the costs of these essentials. In the longer-term, increasing levels of debt are problematic for several reasons; including the fact that concentration of liabilities in some types of households is very important for the stability of the financial system (Murtin & d'Ercole, 2017).

OVERVIEW OF LITERATURE

We review the existing evidence on financial resilience, including evidence on which households are least likely to be resilient in the face of income and expenditure shocks and on what factors are related to greater financial resilience, particularly those which may be addressed through policy levers. The review includes evidence on the role assets, financial literacy and capability and household debts.

Previous research has suggested that households need a savings reserve equivalent to the value of three months' expenses or three months' income, but this goal has been found to be well out of the reach of many low- and moderate-income households. (Collins, 2017)

Although access to emergency savings is only one aspect of financial resilience, the accumulation of savings is a good indicator of households' financial well-being and their ability to cope with financial shocks without having to resort to substantial borrowing.

We know from published evidence that households vary in their ability to save, and the largest determining factor is their income relative to meeting basic expenditure needs and other financial commitments (for example, debt repayments), but even holding these factors constant, saving and holding liquid forms of assets vary across households. Part of this is due to difference between households' financial literacy and financial capability, but some may be due to other factors including cultural differences in saving propensity.

Several researchers have attempted to operationalize the concepts of financial literacy and financial capability and these studies help us to understand the role they play in determining households' financial well-being across countries. Some evidence shows that higher financial literacy and capability is associated with a greater propensity to save and to achieve higher rates of return on these savings. However, there is concern that rates of financial capability and financial literacy are low. Research has found that many people are poor at keeping track of their finances, poor at planning ahead, making ends meet, choosing financial products and staying informed and that these indicators of financial capability are not correlated with income. (Atkinson etal., 2006)

The most reported motive for saving in all countries was precautionary (to build up a financial reserve to protect against adverse future shocks. The second most reported motive was saving for retirement. Statistical analysis of saving motives across households found a strong life-cycle pattern with saving for retirement peaking in the middle part of the lifecycle. The precautionary saving motive also varied across households; lower in the oldest age group (71+ years) and the unemployed, and relatively high in higher educated households, higher income, and higher wealth households. This research also assessed the role of institutions across countries in affecting the saving motives. The existence and generosity of public pension provision was found to decrease the motive for households to save for retirement, not surprisingly the results suggest a substitution effect between public and private pension savings with the payment of taxation effectively operating as a form of saving. In addition, precautionary saving was also significantly and negatively related to average income taxes, again demonstrating how the public insurance mechanism acts as a substitute for private insurance or leaves little excess to save. They also include a country level measure for financial literacy and found that this was significantly positively related to propensity for precautionary saving. (Blanc etal., 2015)

Less than 10 per cent (8.2%) of households reported that they had been turned down or discouraged from asking for a loan. Around one-quarter (23%) reported that they did not have a credit card or credit line, and nearly half (44%) of households had low assets, which the researchers identify as a factor limiting access to credit. Some households were more likely to be credit constrained than others: households where the head was female, young, divorced, self-employed or unemployed; larger households; lower income and lower wealth households.

In the same research, around 1 in 10 (11%) households reported that their expenses exceeded their income over the last 12 months; this was most likely to be the case among households with female, young or divorced household heads. Most households in this situation reported that they coped by using past savings (55%), followed by using a credit card or overdraft facility (22%) or assistance from relatives/friends (22%), and 13 per cent left bills unpaid.

The relationship between household debt and financial resilience needs to be understood from two perspectives. On the one hand, access to affordable credit is an important element of financial resilience and can be a key to households' ability to cope with financial shocks. Holding debt in this context can be seen as evidence of a positive coping mechanism. On the other hand, holding high levels of debt reduces these households' resilience to future financial shocks. In addition, overly indebted households may have ended up in this position for a variety of reasons, including poor financial management and low financial literacy, and these households will struggle to cope with any further shocks.

In the prelude to the 2007-08 global financial crisis, household debt levels increased rapidly in many economies, fueled in part by easy access to credit and rising property prices that meant buying property through mortgages required taking out larger loans. (Ynesta & De Queljoe, 2017).

There is no agreed standard measure for financial resilience and so we find a variety of measures used in the literature. Although the concept of financial resilience is dynamic, capturing the ability to recover quickly from financial shocks, in practice this is very difficult to operationalize as it requires high quality longitudinal data that follows households' financial circumstances as they experience shocks, and tracks their circumstances for some time after. Although assessing which households are financially resilient using longitudinal data is usually not feasible, cross-sectional measures can provide informative indicators of financial resilience.

Measures of financial resilience extend beyond assessments of financial flows, such as income, to include information on financial stocks such as liquid savings and assets, financial debts and can include access to affordable credit, ability to borrow from family and friends, assessments of financial capability and financial competence. In the literature a variety of indicator variables have been used to assess financial resilience.

These include

- *The value of savings and liquid financial assets* that could be drawn on in times of need. Common measures include measuring savings and liquid financial assets in terms of ratios of monthly income. For example, a measure of how many months a household could meet expenditure needs by drawing down on existing savings if income fell to zero, with typical values set at three or six months.
- *Subjective assessments of the ability to cope with financial shocks.* Survey evidence is often used to collect information directly from individuals about whether they believe that they could cope with an unexpected large expenditure, and how they would cope.
- *Measures of financial literacy.* Survey evidence covering financial management and planning skills and financial knowledge has been used to derive measures of financial literacy.
- *Measures of financial capability.* Survey evidence has been used to combine measures of skills and knowledge with behavior and attitudinal information to derive measures of financial capability.
- *Measures which look at the opposite of resilience* capturing aspects of financial distress or financial difficulty. For example, financial debt to income ratios, credit to income ratios, financial assets to debt ratios, debt overburden and over indebtedness measures.

RESEARCH OBJECTIVES

In many countries house price inflation not only led to an increase in the size of loans required to enter the property market but increases in the value of housing assets fueled increases in consumption and consumer credit. (Campbell & Cocco, 2007)

For what purposes do people borrow?

One common purpose is to buy land or a home, the largest financial investment that many people make in their life. In 2017, 27 percent of adults in high-income economies reported having an outstanding housing loan from a bank or another type of financial institution. In contrast, that share was typically less than 10 percent in developing economies. Even among high-income economies there is much variation in the share of adults with a formal housing loan. While about half of adults in the Netherlands, Norway, and Sweden reported having one, 10 percent or less did so in Chile, Greece, Latvia, and Uruguay. The 2017 Global Findex survey asked whether people had borrowed money in the past 12 months for health or medical purposes or to start, operate, or expand a business. (Global Findex Survey, 2017)

This could have been money borrowed from any source, including a financial institution, a savings club, and family or friends. In developing economies 11 percent of adults reported having borrowed in the past year for health or medical purposes. Among this group, 79 percent reported having borrowed only from family or friends or from other informal sources. Borrowing to start, operate, or expand a business was reported by 7 percent of adults in developing economies overall.

Data Analysis and Interpretation on Housing market and prices

With the phased unlocking of the economy and various measures to aid revival, the Indian real estate market appears to be emerging from COVID- 19-induced disruptions. The housing market is gradually rebalancing and recovering from the trough into which it had plunged in Q1: 2020-21. New units launched and residential units sold across the top eight cities reflected clear recoveries in Q2:2020-21 and in Q3 so far, relative to the previous quarter.

House Launches and Sales

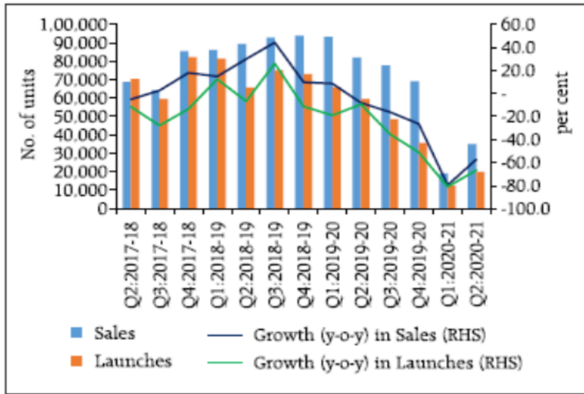

Figure 1: House launch & sales

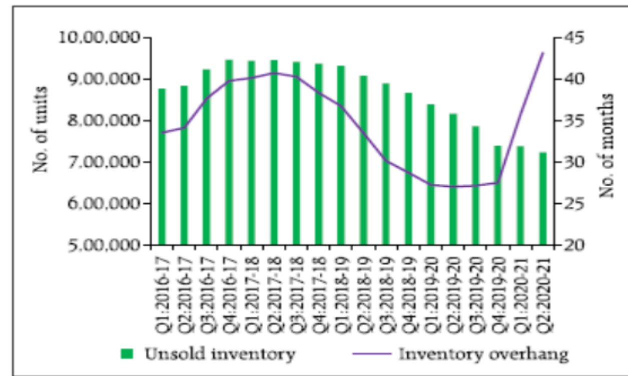

Figure 2: Unsold inventory & inventory overhang

The uptick in sales in Q2:2020-21 resulted in a decline in unsold inventory, though the inventory overhang (i.e., average number of months required to sell unsold houses) increased sharply in the wake of the pandemic.

Unsold Inventory and Inventory Overhang

Under-construction units constituted about 70 per cent of the sales in Q2:20-21 and 81 per cent of the unsold inventory. Sluggish sales have restrained developers from increasing prices in major cities. (RBI, 2021)

Price Growth Trends in Key Housing Markets

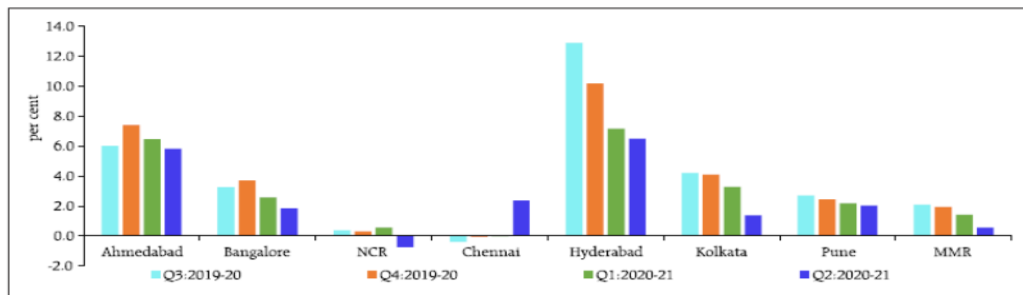

Figure 3: Price Growth Trends in Key Housing Markets

DISCUSSION

Financial inclusion is not an end but a means to an end— when people have a safe place to save money as well as access to credit when needed, they are better able to manage financial risk.

Shocks and Stressors for financial resilience

Majority all households experience multiple shocks and stressors throughout our lifetime. The shocks are categorized in illness/injury, family death, livestock loss, poor harvest and "other." The category "other" usually referred to unexpected expenses, sometimes due to unexpected or expected events. Examples include expenses related to the sale of a plot of land, a roof collapsing, a divorce in the family, burglary of the restaurant of a co-wife's child, death of someone outside their family, old debt, a credit group, home repair, bicycle repair, agricultural activities, weddings, baptisms, children's clothing purchases and holiday celebrations. (Gash & Gray, 2016)

Most Common Shocks Experienced

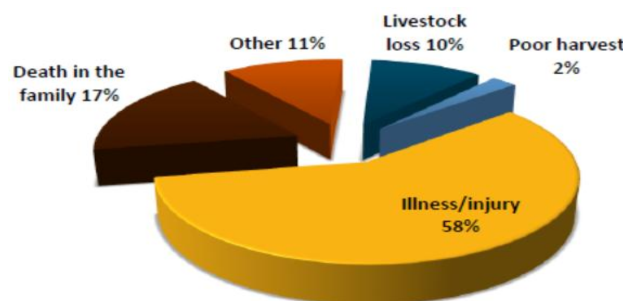

Figure 4: Financial shocks

Coping Mechanisms

The most common coping mechanisms utilized were use of personal savings, followed by reducing food consumption, selling grain, and selling livestock etc. Savings proved to be both the most used coping mechanism overall and the most commonly used mechanism for each individual type of shock. Reducing food consumption is also most-common coping mechanism. Financial services, both formal and informal, played a significant role in managing shocks. (Gray etal., 2014)

Use of Coping Mechanisms

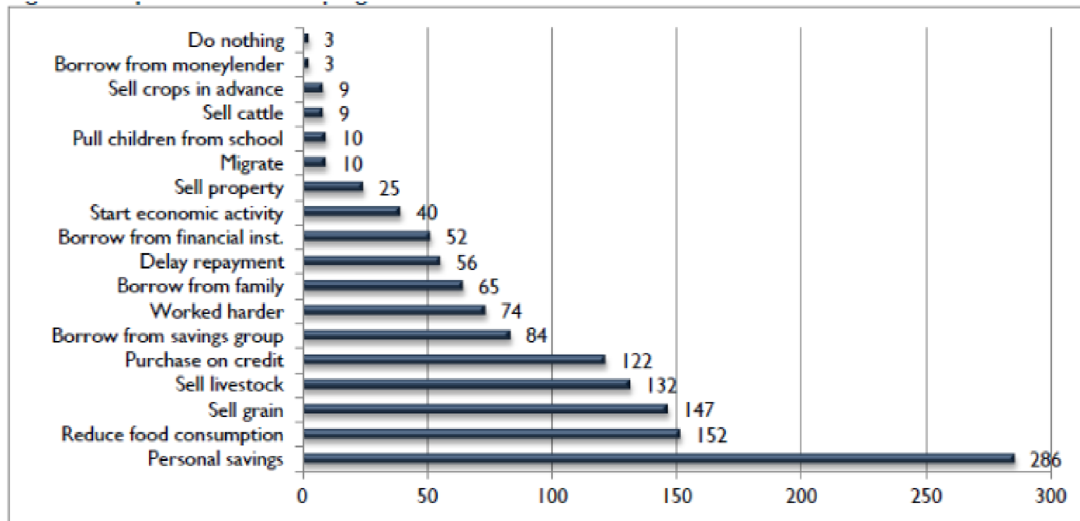

Figure 5: Coping Mechanism

CONCLUSION AND RECOMMENDATIONS

Features that matter most for coping with shocks are timeliness of pay out and availability of the product.

People react differently to a crisis than they would when they can anticipate costs or make investments meant to generate income. The design features from this study are similar to, and complement, those found in both the Human-Centered Design Customer Insights (Seltzer etal., 2014) and Portfolios of the Poor (Collins etal., 2009).

Develop more products and mechanisms that help households increase their savings.

Self-perceived resilient households were more likely to report saving relatively higher amounts *consistently*. Savings was highly relied upon for responding to shocks. There are several ways to help people save for both general expenses as well as earmarked ones—household commitment savings products, agricultural commitment savings, savings groups, and savings groups that save for health. (Brune etal., 2015, Dupas & Robinson, 2013)

Develop financial products for specific shocks.

Products or services that earmark funds or set aside funds for quick access to cover anticipated expenses such as funeral costs—especially family death, which was very common—would be highly useful. (Chandler, 2014)

Financial services can and should play a role in households build resilience. But building resilience should be treated as an intentional goal. Clients need financial and nonfinancial services that help them mitigate risk, lessen the severity of tradeoffs, and avoid long-term adverse developmental consequences.

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