Savings: Short vs Long Term Savings
Insights from behavioral economics and the informal sector

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The Big Picture: An Aging World
Old-age dependency index, 1980-2050

Global status of retirement savings

- <1 in 4 saving for old age
- <20% of elderly (60+) receiving benefits
- Pension coverage: Luxury

What's in the literature?

- Extensive research on retirement savings in the United States
- Extensive research on short- and medium-term savings in the developing world
- Research gap on long-term savings in the developing world... why?
Which pre-retirement individuals age 25 and over should be saving for retirement?

1. Everyone!
2. Everyone not borrowing at more than 10% APR
3. Everyone not living in a three-generation household
4. Everyone not borrowing at more than 10% APR

AND not living in a three-generation household
Is long-term savings the optimal financial behavior for low-income individuals?
Consider: where does the money come from?

• Other savings:
  • Risk, interest rate, terms difference?

• Lower consumption:
  • Shifting over time / type

• Debt:
  • At what interest rate?

• Lower long-term investment:
  • Education, health, enterprise, agriculture
Maximizing returns on investment for the poor

Education?

• Indonesia: increase of ~0.19 years of education → 2.7% higher wages (Duflo 2000)

Debt repayment?

• Global average microcredit interest rate was 35% in 2008 (CGAP)

Investment in an enterprise or farm?

• Often high real returns for micro firms (Sri Lanka: 5.7% per month, de Mel et al 2007)
Paths forward
First: Ask what are the barriers to long-term saving?

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Karlan, Ratan and Zinman, 2014
Commitment mechanisms

Save More Tomorrow (SMaRT) in the United States

- Default individuals who make automatic payroll deductions into a retirement increase contribution rates at regular intervals, unless individual opts out
- Pilot increased retirement contributions from 3.5 percent of salary to 13.6
- Now offered by more than half of large employers in US

Thaler and Benartzi, 2004
Subsidies and automated savings: Where does the money come from?

Three Denmark tests
1. Test #1: Tax subsidy reduced
   - Active savers (15%): total savings stayed the same. Merely shifted $ across savings
   - Passive savers (85%): did not shift anything
2. Test #2 & #3:
   - When retirement savings is automated
     - To increase via job change: total savings increases
     - To increase via regulatory change: total savings increases
     - i.e., when automated, no re-shuffling occurs
3. Punchline:
   - Subsidies through tax system may NOT change behavior
   - Careful about automated changes: is this optimal for everyone?

Chetty et al, 2013
How can we replicate these mechanisms in developing countries?
Audience Poll #2
Uganda Supersavers program

• Problem: Families report not enough money to pay for school supplies, tests, etc.
• Grades 5, 6 & 7, weekly deposits into savings “box” in class
• Deposits then put into a bank account
• Beginning of term, a fair held to sell school supplies

    KEY TEST: At fair, students receive CASH or VOUCHER from account

    One worked. One did not.

    LET’S VOTE

Karlan and Linden, 2016
Uganda Supersavers Program

1. The CASH treatment arm worked, and not the VOUCHER treatment.

2. The VOUCHER treatment arm worked, and not the CASH treatment.
Linkages with mobile money

Using defaults to counter present bias in Afghanistan

- Automatic payroll deduction up to 10% of salary into secondary mobile money account (short-term savings account)

- Tested impact of default status (in at 5% or out) and matching incentive (0-50%) on savings

- Default enrollment increased contributions and generated new savings

- Roughly equivalent to a 50% employer match

Blumenstock et al., 2016
Linkages with remittances

- Important source of income for many households, leveraging social and family networks
- Source of regular digital transactions for those in a cash economy
- Linking savings to remittance transfers may overcome obvious informal sector challenge
Thank you