The Effect of Social Pressure on Individuals' Financial Decisions in Central Malawi

Researchers:

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Sector(s): Finance

Location: Malawi

Sample: 315 farmers in 158 agricultural clubs

Target group: Farmers

Outcome of interest: Savings/deposits

Intervention type: Social networks

Research Papers: The Effect of Social Pressure on Expenditures in Malawi

Partner organization(s): University of Michigan - Rackham Graduate School

Poor farmers in Malawi tend to spend most of their income soon after receiving it, meaning they lack the funds needed to purchase inputs for the next planting season. One reason for this could be that farmers feel pressure from their social networks to share excess cash. Researchers introduced public and private lotteries to test whether social norms about sharing income explain the tendency to spend income rapidly. Receiving prize money in a public setting induced individuals to spend one-third more of their money in the first week than they would have had they received the money in private.

Policy issue

For many farmers, income is concentrated at harvest time and spent soon after. This means there is often not enough cash left to purchase agricultural inputs, like fertilizer or seeds, for the next planting season. One reason farmers do this may be because they value present spending more than they value future spending, a characteristic economists call time-inconsistent preferences. Another explanation may be that farmers face demands from their family, friends, or others in their social network to share financial resources. To avoid social pressure to share resources, individuals may spend harvest income quickly to demonstrate to their networks that their household needs the income. This could reduce the household's ability to reserve some harvest income for future expenses or respond to unanticipated shocks, such as an illness or natural disaster. Farmers might be able to save more if their networks had less information about when and how much they earned. However, there is little evidence about how public knowledge of individuals' resources influences their spending decisions.

Context of the evaluation

Malawi is among the poorest countries in Sub-Saharan Africa. The majority of its population lives in rural areas and ninety percent of the labor force is engaged in agriculture.[1], Smallholder farmers grow both food for their household and cash crops, including tobacco, maize, and cotton.[2], Since many smallholder farmers spend harvest income shortly after receiving it, they may have little cash left and must then rely on loans to purchase farm inputs like fertilizer and seeds. For instance, only 18 percent of farmers who received loans to grow the cash crop paprika reported saving money to use for the next season's inputs. In 2007,

Cheetah Paprika Limited, an agribusiness that offers extension services including field training and inputs to smallholder paprika farmers through a contract farmer program, formed agricultural clubs in central Malawi. Each of these clubs included about ten smallholder farmers and allowed farmers to receive additional extension services and take out group loans from the Malawi Rural Finance Corporation.[3] When members assembled for club meetings in May 2008, researchers introduced public and private lotteries in each club to study the effect of social pressure to share income on farmers' spending decisions.



Farmers harvesting crops in Malawi.

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Details of the intervention

Researchers partnered with Cheetah Paprika Limited to conduct a randomized evaluation examining the effect of social pressure to share income on farmers' spending decisions by varying whether income from large cash prizes was received in a public or private setting. In May 2008, each of the 158 agricultural clubs held two lotteries to distribute prize money:

- *Public lottery*: The lottery winner was announced and prize money distributed in front of the entire club. All club members present knew there was a lottery, who won the lottery, and the value of the prize.
- *Private lottery*: Lottery results were communicated privately and only to the winner. The winner was assured that no one else in the community knew about the private lottery.

Winners of all 316 lotteries received MK2,500 (US$17.86, roughly equivalent to one-tenth of average annual per capita income in Malawi).

Baseline and endline surveys were conducted in May and August 2008, respectively. These surveys gathered data on assets, savings, and the recent harvest, as well as information on winners' anticipated and actual prize money use.

Results and policy lessons

Researchers found that public lottery winners spent 35 percent more of their winnings within the first week of receiving it than those who won private lotteries, who spent MK985. Within a week of the lottery, public winners spent more on people outside of their households than private winners. Though winners of public lotteries gave away more money immediately than winners of private lotteries, they gave less in subsequent months. Public lottery winners also spent somewhat more on themselves, their households, and durable goods immediately after the lottery than private winners. This suggests that public lottery winners might spend their earnings more rapidly in order to avoid the obligation to share income.

After three months, the difference between total spending by public and private winners disappeared. Public lottery winners ultimately spent approximately the same amount on themselves, and there was no difference between the two groups in the amount of money given to people outside of their household. In this context, publicy receiving money affected when winners spent or shared their money, but not how much they spent or shared.

Jesscia Goldberg, "The Lesser of Two Evils: The Roles of Social Pressure and Impatience in Consumption Decisions." Working Paper, December 2011.

1. CIA. "World Factbook: Malawi." Accessed 19 February 2015.
2. FAO. "Country Pasture/Forage Resource Profile: Malawi." Accessed 19 February 2015.
3. Agricultural club members also participated in a study about loan repayment incentives as a part of the Biometric and Financial Innovations in Rural Malawi project. Read the evaluation summary.