

# The Formation of Mutual Insurance Networks within Group Lending

Experimental and Survey Evidence  
from Self-Help Group Program in South India

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## Abstract

In the theoretical and empirical literature on microfinance, a joint liability clause has been treated as exogenous mutual insurance institution within group lending, in which a participant is supposed to be obligated to repay microloans instead of peers who belong to the same group if they are falling into default.

Therefore, few empirical attempts have been made at investigating whether a joint liability clause actually encourages program participants to form mutual insurance networks within same financial groups and what factors determine the network formation. This paper aims to provide empirical evidence of the mechanisms of endogenous formation of mutual insurance networks within group lending in rural South India, by comparing with the formation of pre-existing risk-sharing networks. To do so, I have conducted a household survey that is complete enumeration including 220 households in the single village and a dyadic network survey that consists of 48,180 observations (220 households are multiplied by 219 households) in 2008 and 2011, respectively.

Moreover, network information is combined with the data on social and risk preferences elicited by laboratory experiments conducted in 2011. Two main empirical findings emerge. First, econometric estimations find no evidence that a joint liability clause facilitates more dense insurance networks inside of financial groups than outside of them.

In other words, the person who is on the verge of default is likely to rely on the insurance partner who is in other financial groups.

Thus, a joint liability clause appears to be established in a unit of the entire surveyed village rather than a unit of small financial groups.

Second, while social and geographical proximity are major determinants of the formation of mutual insurance, altruistic motivation (e.g. guilt aversion, shame aversion, and benevolent altruism) and social norms such as noblesse oblige also predict the formation of mutual insurance.

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