Factors influencing decisions to undertake financial savings

Background Information

The concept of saving does not provide itself to a concise definition leading to diverse definitions put forward by various researchers and economists in the economic literature. In the macroeconomics literature, it is considered as disposal income less consumption. Issahaku (2011) contended that saving goes beyond the proportion of disposable income that is not spent and that, spending on durable goods such as furniture, home accessories, appliances, computer, equipment and accessories, automobiles among others are ways of saving too. Andrea and Francisco (1998) also pointed out that investment in human capital such as medical products, apparatus and equipment, professional health services, health insurance and so forth are forms of saving. Nonetheless, the short coming of this view is that it conceals the clear distinction between expenditure and saving because several of the human capital components mentioned are more or less current expenditure items. This study seeks to consider saving as deposits in savings accounts which are done with banks, microfinance institutions, susu groups and other saving avenues (Schultz, 2005). This definition is in line with the definition put forth by the 2013/2014 Ghana Living Standard Survey (GLSS 6) report as the setting aside of unspent income in a bank or a non-bank financial institution or in other forms of arrangement such as pension plans and some insurance products. The reason for this definition is that, it is through these saving window that financial institutions get to increase their credit standing and promote investment.

Notwithstanding the lack of a common definition for the concept saving, it is an important macroeconomic variable to be studied under the purview of the economic arena of an individual as well as household level. Saving according classical economist like Adam Smith, David Ricardo and J. S. Mill is an important determinant of economic growth. For the individual or household, savings serves as a cushion against future unforeseen and uncertain circumstances of life while for a country's economy as a whole, it leads to higher economic growth. For Rao (1980), saving constitute the basis for capital formation and capital formation constitute a major determinant of economic growth. Unlike developed economies where income is generated at a higher rate which encourages more saving thereby translating into more capital formation, developing economies like that of Ghana where income standard is almost uncertain coupled with low rate of financial inclusion of the various sectors of the economy, it will be appropriate to pay more attention to the patterns and determinants of saving in the economy. On average East Asia saves more than 30 percent of gross national disposable income (GNDI) while Sub-Saharan Africa saves less than 15 percent. Regional differences have been rising: over the past three decades, saving rates have doubled in East Asia and stagnated in Sub-Saharan Africa and in Latin America and the Caribbean (Loayza et al., 2000). By a hike in aggregate saving, the social value of saving can exceed its private value in many developing countries.

National savings of every economy can be broadly categorized into three saving type namely the household sector saving, private sector saving and finally the private sector saving. Public savings is the saving done by government such as state, local and federal government while private savings is the saving done by corporate business, institutions and organisations. Household sector savings is the saving done by families and individuals. Among these three savings type, the household sector savings is said to contribute a larger share to the total domestic savings of the economy (Rehman *et al.* , 2011). Household sector savings is of utmost importance to the capital formation of every economy in that, the sector engages in substantial financial and non-financial investment and make possible both private and public investment by transferring accumulated savings. The Ghanaian household sector savings is made up of savings from urban households and that of rural households. Rural household sector is vital to the Ghanaian economy not only because of its potential in generating employment and income, rather, because of the limit set by this sector to the growth of some other sectors. Hence the growth of the aggregate economy is enormously dependent on the amount of savings emanating from this sector and how they are transferred into the hands of the enterprising investors.

Ghana’s quest to mobilizing enough domestic resource through financial savings for capital formation which will eventually manifest itself in economic growth is believed to have begun when the country embarked on a comprehensive financial sector reform. Preceding this era, the country’s financial system was shallow , fragmented and almost at the verge of collapsing as a result of excessive state control and weak institutional framework leading to lower rate of financial savings. Many were the significant strides made in the economy during the reform which was mainly driven by liberalization policies such as interest rate deregulation and credit allocation, improved regulatory and supervisory frameworks especially in the financial sector. All these were geared towards enhancing banking intermediation that would improve financial savings mobilization. Despite these significant strides made, it is worth noting that most of the expansions in the financial sector were only concentrated in the urban areas at the expense of the rural societies (Osei-Assibey and Baah-Boateng, 2012).

In recent times, the economy has witness a considerable increase in the number of both foreign and local financial institutions with the licenced Micro Finance Institutions leading with a total of 409 as at July 2014. Rural/Community Banks follows with 137 and finally, 58 Non-Bank Financial Institutions. (Data source: Bank of Ghana Website). Despite these significant increase in the number of financial institutions, the 2005/2006 and 2013/2014 Ghana Living Standards Survey (GLSS 5 and 6) reports have revealed that rural areas have higher percentages(78% and 78. 5%) of households that do not owns a bank account or undertake financial savings as compared to that of urban households(61% and 53. 6%) respectively. This leaves us with mind boggling questions such as; what factors at all are responsible for these high percentages of rural households without savings account? What are the factors that influences the decision by rural households/individuals to hold bank account or undertake financial savings? Do the operations of financial intuitions actually play a role in influencing the decision by rural households to hold bank accounts or/undertake financial savings? These questions and many other more are begging for answers. It is against this backdrop that the study seeks to investigate the factors that determines the decision by Ghanaian rural households to undertake financial savings or hold bank account. The hypothesis to be tested is whether operations of financial institutions actually play a significant role in the decision-to- save by rural households in Ghana.

For the purpose of this study, it must be emphasized that " saving" refers to an individual having a bank account or is financially contributing to a loan/savings scheme in any of the financial institutions (i. e. banks, microfinance institutions, susu groups and other saving avenues).

Problem Statement:

It is now widely understood that saving has great potential impact. This insight is grounded in evidence that the poor do save in cash and in-kind—whether as a way to build assets, manage household cash flow, or effectively cope with risk. However, much of their savings remain informal and outside of the financial system (The SEEP Network 2013). Savings makes it possible for combating or meeting any emergency accrued by the individuals or the households or any corporate agencies. Saving is more often meant for meeting contingencies but sometimes it also acts as a form of investment. People are sometimes not inclined towards saving and the very reason for this, is the lack of awareness.

Given the proliferation of financial intuitions (both locally and foreign owned) in recent times, one will expect that the percentage of households (particularly rural households) that undertake financial saving or/ holds bank account will be higher or at least match the increase in the number of financial institutions. Rather, the opposite is what is being observed. According to the 2005/2006 and 2013/2014 Ghana Living Standards Survey (GLSS 5 and 6) reports, rural areas have higher percentages(78% and 78.

5%) of households that do not owns a bank account or undertake financial savings as against that of urban households(61% and 53. 6%). This reflects a worrying phenomenon and leaves us with mind boggling question such as; what factors are accounting for these high percentages of rural households without savings account? What are the factors that influences the decision by rural households to hold bank account or/undertake financial savings? Do the operations of financial intuitions actually play a role in influencing the decision by rural households to hold bank account or/undertake financial savings? This is where the study becomes relevant in providing answers to the above mentioned mind boggling questions. Aggregate saving in any economy is dependent on a number of variables. For effective economic planning, the planners should have an idea regarding the capacity of saving of different groups of people and the method by which saving can be improved. To advocate for financial saving, there is a need to know about the saving motives of the individuals. An understanding of the saving preferences also helps in calculating the saving instruments which can efficiently arouse saving.

Objectives of the Study:

The study seeks to investigate the factors influencing the decision to undertake financial saving in rural Ghana.

1. 3. 1 *Specific objectives* : The above objective of the study will be achieved by;

- Analysing rural households' attitude towards financial savings

- Examining whether the operations of financial institutions such as proximity to financial institution and the extent of flexibility in opening accounts significantly play a role in influencing the decision by rural households to save.

Research Questions:

Some of the questions that this study is seeking to answer are;

- What are the factors that influence the decision by rural households to undertake financial saving or/ hold bank accounts?
- Among the factors, which of them significantly influence the decision-to-save?
- Do the operations of financial institutions such proximity to financial institution and the extent of flexibility in opening accounts have significant bearing on the decision by rural dwellers to save?

Significance/Justification of the Study:

Recounting the saving potential of rural households, Meyer (1985) provided some reasons in support of the saving potentials of rural households and these are; *1) rural households save automatically between harvests, and/or sell a portion of their crops to pay off debts or to expand consumption; 2) rural households are heterogeneous - rich and poor; rich households can always save over long and/or short periods while poor households can save only over short periods; and 3) more modern farming methods allow farmers to increase income and, therefore, savings* . It appears the intervention measures (such as interest rate deregulation and the liberalization of financial sector) which has resulted in the upspring of a number of financial institutions and establishment of Rural/Community Banks put forward by

Ghana to take the maximum advantage of the saving potentials of the rural households is not yielding its intended objectives as indicated by the 2005/2006 and 2013/2014 Ghana Living Standard Survey (5 and 6) reports. It is just appropriate that more time and resources are spent in studying and paying more attention to the savings decisions of rural households so as to take advantage of their saving potential if the objective of mobilizing enough financial resources for capital formation is to be achieved as a country. This is what the study stands to furnish us with.

Also, many are the studies that have been found in the literature to exist on saving prior to (Mills and Ricardo 1884) through Harrod and Domar’s postulation about the essence of savings on economic growth to date. These studies rather focus on the determinants of the amount or rate of savings (Issahaku, 2011; Alma and Richard, 1988), macro level analysis (Gupta, 1970; Khan et al., 1992 ;) and description of savings behaviours using descriptive statistics (Komla, 2012) leaving out the quantitative analysis as gap in the literature. In the Ghanaian context, studies done on the determinants of saving of rural households using a micro level approach have mostly been skewed toward a specific rural area, on gender basis or a group of rural areas in Ghana such as Issahaku, (2011); Munin et al. (2013); Komla, (2012), Oduro et al. (2012) etc. This study takes a micro level approach and a nationwide analyses of the determinants of financial saving decision of rural households in Ghana by employing quantitative and descriptive statistics.

This study again gives an insight into the correlation between the decision to save by individuals in the rural areas and the operations of financial institutions. Financial institutions such as banks and other non-bank financial institutions also stand to benefit from the findings of this research as the findings will make them aware of opportunities to provide rural communities in the Ghana with accessible savings outlets which will enable these businesses to make profit. Finally, the current study will add to the existing literatures on financial savings and shall be a reference material for future study.

Methodology:

The study is focused on using secondary data from the Ghana Statistical Services on the Ghana Living Standard Survey 6(GLSS 6). This is because it captures well most of the variables of interest such as age, marital status, educational status of household heads family size, income dependency rate etc. The study takes a look at two analysis i. e. descriptive analysis and quantitative analysis.

The quantitative analysis takes a look at the determinants of the decision to hold bank account/undertake financial savings by rural households (being binary in nature) with the other independent variables carried out by adopting the model employed by Munin et al (2013) with some modifications.

Organization of Study:

The study is organized into six chapters including the present one. The second chapter of the study covers an overview of financial saving in general, the importance of rural financial savings to an economy especially the economy of Ghana etc. The third chapter includes related theories of saving, views on the savings potentials of rural households and studies conducted on the saving behaviour both rural and urban households in Ghana and other countries . The fourth chapter presents the methods used in this study and the source of the data used. The fifth chapter includes the empirical estimation and discussion of the results generated. The sixth and last chapter includes the summary, recommendations and conclusion.