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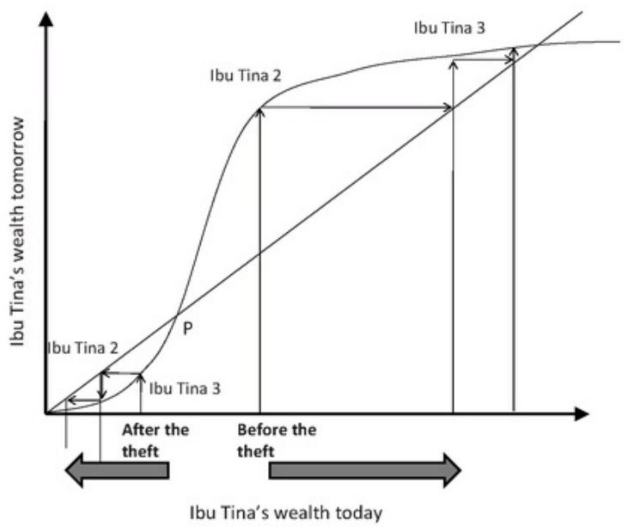
The Hazards of being poor



The reason that poor are hedge-fund managers is that they have to live with uncertainty and risk in their business. Many of poor run small business or farms especially agricultural businesses. However, most of their agricultural lands are not well-irrigated which makes their yields are highly dependent on the weather but when there is a drought or delay of rain, they will face even worse situation. Therefore, half of the year's income might disappeared. Not only income risk that most of them are facing but also some of them are hired as casual workers that get paid day by day but in the end, the income is still not stable. In poor countries, agricultural income is quite varied especially during disasters or food crises. The poorer the country, the greater its variability. For example, in the rich country like the US, their farmers are insured and receive subsidies. So. the are less dependent on the weather unlike poor farmers. Later on, an economic crisis became a human crisis because the poor are far more exposed to the economic instability. All government budget would be cut according to the lower tax rate. The poor also lose their jobs especially a construction jobs because of the less opportunity during the economic crisis then they have to migrate away to seek for the better life but often not a really good choice in the end. According to the interview in india, some of the families that migrate, face with disease and etc. For the poor every year feels like being in a colossal financial crisis because the crisis increase the risk for the poor. The indonesian crisis, their currency lost about 75 percent of its value. The food prices increased 250 percent and the GDP decreased 12 percent but only the government and a fixed incomes earners were affected by the crisis. However, the poor farmers tend to gained more purchasing power. During thailand's financial crisis in 1997, two-thirds of 1,00 people surveyed explained that their income decreased because of the drought. There was only 26 percent of losing employment wasn't from the effect of the crisis. Otherwise, things seemed not to be that worse for poor in every year but still not good for them. The poor always have a worse life than the less poor because they might have to cut some of their essential expenditure such as foods, medicine or even foods. When the relationship between income now and future is s shaped the effect on the poor might be a lot worse than a temporary unhappiness like in the case of Ibu Tina, a business woman. She is able to invest in small amount and she earns back a little. Before the theft, the business was poorly run but still profitable because they still had enough money to buy raw material. Later on, they change to by a ready-made product instead of producing by themselves but she still gain a little but less profit than before. But when they faced with theft that clearly made them fell into the poverty trap zone, they made a little earning and getting poorer and poorer. Therefore, when the relationship between income today and future income is s shaped, they tend to turn from a middle income family to a permanently poor. Some other evidence of being poor that came from the stress and anxiety that may lead to less motivation and depression among the poor. Being stress makes it's harder to focus then the result of worker tend to become less productive. Otherwise , they will be less able to make an economically rational choice.

The Hedge

Similarly to hedge-fund managers, the poor has to diversify a portfolio. But, the difference is that they have to manage the risk exposure instead of financial instrument. What can the poor do to cope with these risks?

1. Working More

When the poor faces the drop of wages, they would react by working more in order to generate more income. However, it would not always be an effective option. For example, drought and increase in input might cause the reduction in wage. Anyway, if poor laborers work more, they would end up competing with each other and drive down the wage even more.

2. Diversified Portfolio

They normally do not rely on sole occupation, but rather multiple occupations. Mostly, men and teenage boys temporary migrate to the city while the rest stay behind at the farm to maintain the farming business.

3. Share Liability

There is a contact between the poor farmers and landlord to share the cost of farming and claim some parts of the output. This could reduce risk exposure for farmers. However, the con is that farmers became inefficient in a way that they put less effort comparing to the land they are entirely entitled to.

4. Helping Each Other Out

Since, most poor people live in neighborhoods have extensive network of people in the area. When some shocks hit specific group of people, those people who are still doing well usually help out in order that they expect that these people will do the same thing in return in reverse situation. For example, they could help out by giving gifts or informal loans. Moreover, the terms of loans are flexible depending the situation they are facing. This networking could reduce the risk exposure to the group.

Insurance

Although poor people face many high risks when it comes to their jobs and health, surprisingly, formal insurance is a rarity in poor communities. Common types of coverage for farmers in developed countries such as health insurance, insurance for bad weather, and insurance for livestock deaths are not typically found in developing countries. Insurance for the poor seems like an untapped market with potential for a large amount of profit but there are numerous problems that arise with providing insurance. These issues are not exclusive to the poor, but they are intensified in poorer communities due to difficulties in regulating and monitoring the insured.

An example of this moral hazard would be people changing their behavior by farming less carefully because they would not have to deal with all of the consequences. Another potential problem is adverse selection. If insurers are not able to separate those who are likely to have a problem and those who just decided to care and join now, they will raise the premium price on everyone. Higher price will makes things worse because those who might actually need the insurance will be driven away. This is why affordable health insurance programs are typically mandatory, so the insurer does not get stuck with only the high-risk individuals. A third problem is straight up fraudulent activity. How do you prevent hospitals from trying to profit off bogus claims or a farmer from claiming his water buffalo died? Different types of risk are of course, easier to insure than others.

Using weather as an example, a farmer can value a policy that pays a fixed amount when the rainfall does not reach a certain level. Insuring catastrophic health problems is simpler than covering outpatient care. However, the bigger issue that still must be solved is selection because insurance companies do not just want ill people signing up. Insurance companies can counter this issue by targeting a large pool of people who come together for similar reasons unrelated to health.

In 2007, SKS Microfinance, India's then largest microfinance institution, introduced a health-insurance program that offered benefits relating to maternity, hospitalization, and accidents. In order to avoid adverse selection, this program was made mandatory for the offered groups. In order to prevent potential fraud, benefits were capped and clients were encouraged to utilize hospitals that SKS had long-term networking agreements with. SKS ran into problems with the initial launch and decided to make the insurance mandatory only at the first renewal because clients rebelled. SKS ultimately started to lose clients and money so it stopped insuring new clients. Problems like these can explain why poor people are not insured.

Another reason why there is low demand for insurance is that government intervention disrupts the market. When certain markets fail, overprovision by international institutions or the government is probably to blame. This is known as the demand-wallah argument. When a major disaster takes place, these institutions step in to assist them leaving no need for actually insurance. However, an argument can be made that governments only intervene when the disaster is catastrophic, not if someone's water buffalo dies.