



NAVARRA CENTER FOR INTERNATIONAL DEVELOPMENT

Isabel Villamor

Book review:

Portfolios of the Poor:

How the World's Poor Live on \$2 a Day

By Daryl Collins

In the same manner that people read the newspaper from the end to the beginning, the same could be done with this book to increase its interest, as the last chapter of the book reveals the most important fact of the book: not having enough money is only one part of what it means to be poor, but without it, health and education cannot occur. Therefore it is essential to understand how the poor manage their income in order to find better solutions for alleviating poverty.

Portfolios of the Poor, however, start by explaining the research that supports its thesis and how Collins and his group devised it. Several years ago they launched a series of detailed studies to shed light on how families live with so little. Through a series of financial diaries, they analyze not only the balance sheet of these poor households but also their cash flows making it possible for them to reach the conclusions presented in the book.

One of the facts that is more appreciated in the introduction of the book is that from the very beginning Collins criticizes common beliefs and goes straight ahead into his thesis:

“We imagine that with incomes at these impossible levels, the poor can do little more than hand-to-mouth survival. The chances to move from poverty must depend either on international charity or their incorporation into the globalized economy. The hottest public debates in the world of poverty, therefore, are those about aid flows and debt forgiveness and about the virtue and vices of globalization”

He also clarifies the main result of the research in the first pages: Poor people do not consume everything they earn. This interesting finding and the thought that came after it -money management- are a fundamental and well-understood part of poor's everyday life. In addition to this, a second fact is pointed out: these households are frustrated by the poor quality of the instruments that they have access to, which in fact opens a complete new door of:

“New opportunities for philanthropists and governments seeking to create social and economic change and for business seeking to expand the markets”

Collins begins his book clarifying the main characteristics of household incomes, which even though are not as surprising as the conclusions, they are not exactly what the reader expects and therefore allows Collins the opportunity to better understand why the poor behave the way they do.

These families survive thanks in part to financial tools; however, the most common are not the ones celebrated by advocates of microfinance.

In addition to this, the reader also learns that these people's incomes are not just low, but also unpredictable, which helps explain the wide variety of financial instruments that are found in the book. The complex way in which poor manage their unregular cash-flow is to make sure that they have something to eat every day. As the reader knows, or at least expects, the reason for this uncertainty is the fact that jobs are not always permanent, and even if they are the payments may not be regular.

However, it is surprising to see the huge differences that appear between countries. For example, due to the labor laws in South Africa -often criticized for their rigidity- once a household manages to find a waged job, they tend to have a fairly reliable source of income. This and the grants provided by the government may explain the difference in income earning pattern and the number of children at work between this country and the other two presented in the book - India and Bangladesh.

Following the descriptive characteristics of these households' cash-flows, Collins compares the needs and instruments of both wealthy and poor people, which surprisingly are very similar. In both cases the financial activities are based on three facts: managing basics, coping with risk and raising lump sums, and insurance and saving independently on his/her status or income. Where these facts differ is the way and instruments in which they are applied.

Once again Collins amazes the reader when he explains that in developed countries, where households like to have insurance, the poor continuously

suffer on the anxiety that comes from anticipating emergencies and dealing with them when they occur. It is very surprising that even those earning less than 2\$ a day, are investing -or willing to invest- in financial tools specifically designed to protect them against emergencies. The book points out one example in each country which may be transferred to other ones: the state-sponsored insurance for the poor in India, the “pro-poor” private life insurers and credit-life coverage in Bangladesh, and the funeral coverage in South Africa.

Even though the book is more descriptive and focused in telling what is happening in the poor household’s finances, one of its strongest parts is that from time to time it provides good ideas on how the problems can be addressed. For example, Collins explains that:

“There would be substantial demand for cheaper partly coverage the portfolio approach suggest that it is not necessary to solve an entire problem in order to improve the wellbeing of poor communities”

The second financial activity of the poor is their ability to save substantially- something unimaginable for most readers. Collins explains they do so by forming lump sums that they use for the same purposes: life-cycle uses (weddings, funerals, etc.) and broader life-cycle uses (emergencies). What may differ is that they save in a different ways and that financial instruments for saving may have disadvantages for them.

The book perfectly explains the most popular ways of saving: The Saving Up Clubs, Rascals (rotating saving and credit association), lottery Rosa’s, auction rascals, ASCAs (cumulating savings and credit associations) and Mutation, adaptations and evolutions of informal clubs. All of which are really interesting and increasing year after year.

However, in a realistic approach, Collins also explains that these clubs are not always good enough because they are unreliable, mismatched and too short and he provides the different cases in the book. Even more shocking is the fact that the poor pay to save, in informal sectors, an incredibly high rate. Collins, once again, helps the reader to understand that this is because interest rates are more like fees than rates, and for poor people, money and time are not closely associated.

However, the evil image that the reader may have about money lenders ultimately imposing high interest rates is balanced when she/he discovers that money lenders are often as much part of the community as their clients, which makes forgiveness and rescheduling even more likely.

Once again the reader is stunned to find that price is not the main factor, but price itself

adjusts to many other factors. It is not that poor households do not care about price, but they also care about convenience and flexibility and are willing to pay for those features.

Another strong aspect of the book is that it explains everything from the beginning in a clear succinct way. For instance, the reader discovers and understands why poor use informal sources and not banks for their financial issues. Informal transactions have many virtues like the convenience, paperwork is not necessary, and no financial price needs to be paid. However, they also have important drawbacks like unreliability (as poor have to approach several lenders to put together a small sum), lack of privacy (a source of stress and shame), and lack of transparency. As Collins points out:

“We have noted that informal arrangements offer flexibility and convenience but may lack on reliability, privacy and transparency, and rely too heavily on kindness good will and norms of mutual obligation. An important element on reliability rest with the rule -bound agreements, clear expectation on both sides of transactions, and professional relationship-elements essential in formal transactions but mostly rarely in informal ones”

Nevertheless, the portfolios of the poor are more diversified than could be imagined and therefore these household also use formal instruments to meet their financial necessities.

Before the book approaches the third financial tool -borrowing- every reader is informed that the world is paying special attention to the connection between poverty and finance like never before. Over the past decade the idea that poor household are “bankable” has been widely embraced. This change in minds brings a great hope for the households discussed throughout the book.

What surprises the reader most is that even though Grameen bank and microcredits are well-known in developed countries, Bangladesh is the only country in the survey in which the microfinance institution had a large presence. By contrast, both Indian and South Africa’s poor remained unnerved.

Even with this fact there is still place for hope as both countries are actively making efforts to bring microfinance and other financial services to low income households.

In addition to the expansion of microcredits, a second challenge is needed: moving to microfinance from the narrow goal of microcredit as the demand for microcredit extends well beyond the need for just microenterprise credit. The poor households in the book seek loans for a multiple of uses besides business investment as we discover in the financial diaries.

In the fortune at the BOP of Prahalad, the innovation did not come from the nature of the product, but from discovering a way to suit payments

to patterns of household's cash flow. This is what the microfinance sector has to do.

One element of the inflexibility in microfinance is the insistence by some lenders that all loans have to be invested in business. The book provides ideas to solve this inflexibility, to mainly allow penalty-free grace periods when problems hit, to allow borrowers to "top up" these loans partially through repayment schedule (Grameen bank), to offer loan against liquidity assets commonly held by the poor; or to lend against deposits and gold.

An additional point of the book is that the reader discovers the Grammen Bank a few years ago responded to a crisis by discarding old premises and taking new approaches that matched better the irregularities of cash-flows. The poor welcome safe, local, convenient, open-access saving and use it intensively. Garment II was able to serve most of the necessities of the poor, by being able to offer saving, lending, and insurance product that meet their cash-flows needs.

For those readers who may think the book is too academic, the last couple of chapters may be the most interesting ones as they are full of hope and express the more probable path that the microfinance is going to follow.

Bangladesh microfinance industry continues to develop at a rapid pace. Today's short coming can be overcome. Given time, legislator will enact an improved microfinance law and hope that microfinance institutions positioning themselves as providers of integrated money manager systems for poor household. There are reasons for optimism as microfinance is less dependent in political will once there is a suitable legal framework, something that many governments are already offering.

Furthermore they are trying to meet the principles of the financial instruments directly for the needs of the poor: reliability, convenience, flexibility and structure. Collins expresses his optimism in the following way:

"As recently as a decade ago, we might have been accused of wishing for impossible, but recent developments in microfinance, coupled with evidence that poor people are willing to pay for such services, have changed the outlook entirely.

Could it be that financial services will become the first global reliable service that the world's poor enjoy? We hope that the insight described in this book will help to achieve that end."

The reader ultimately ends the book with the idea that not having enough money is bad enough, but not being able to manage whatever money you have is worse. Hopefully this is start to change but the first step to do so should be read this book.

REFERENCES

Sachs, J. (March, 2006). The big push Déjà Vu [Review of the book *The end of Poverty* by W. Esaterly] *Journal of Economic Literature*

Fogel, R. (March, 2006). The great escape [Review of the book *The escape from hunger and premature death* by A. Deaton] *Journal of Economic Literature*

Fischars, S. (March 2006). The International Monetary Fund in a Time of Crisis [Review of *IMF essays from a Time of Crisis* by P. Conway] *Journal of Economic Literature*

Fischars, S. (March 2006). The International Monetary Fund in a Time of Crisis [Review of “IMF essays from a Time of Crisis” by Patrick Conway] *Journal of Economic Literature*

Mackintosh, J. (2010). Small enough to fail [Review of “More money than God: hedge funds and the New Elite” by Sebastian Mallaby] *Financial Times*

Patterson, S. (2010). The long and short of it [Review of *More money than God: hedge funds and the New Elite* by S. Mallaby] *The Wall Street Journal*

Prahalad, C.K. (2009) *The fortune at the bottom of the pyramid: Eradicating poverty through profits*. Revised and updated 5th anniversary edition. Wharton School publishing University of Pennsylvania