



Lifecycle effects on consumer financial product portfolios in South Africa: An exploratory analysis of four ethnic groups

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ARTICLE INFO

Article history:

Received 11 February 2011

Received in revised form 12 September 2011

Accepted 15 September 2011

Available online 19 September 2011

JEL classification:

C49

F39

PsycINFO classification:

2240

3900

Keywords:

Consumer psychology

Saving behavior

International finance

ABSTRACT

This paper assesses ownership of 16 financial products by households in different lifecycle stages amongst four ethnic groups (Africans, Coloureds, Asians, and Whites) in South Africa. The lifecycle hypothesis indicates younger households should own more debt-related financial products, whereas households in intermediate lifecycle stages should own more financial products to accumulate assets; both these claims are disconfirmed for all groups. However, White households in intermediate household stages own more financial products than younger and older households, consistent with previously reported lifecycle findings in Western countries. Consistent with the literature on innovation adoption we find that younger, affluent and highly educated households amongst the other three ethnic groups tend to own more financial products than older Africans, Coloureds and Asians. These results indicate that innovation adoption literature may better describe financial product ownership in developing countries than the lifecycle hypothesis.

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1. Introduction

Consumer financial product portfolios are combinations in which individuals own products such as checking accounts, saving accounts, loans and investment products. Such product portfolios have received considerable attention in the extant literature (e.g., Gunnarson & Wahlund, 1997; Kamakura, Ramaswami, & Srivastava, 1991; Stafford, Kasulis, & Lusch, 1982). This is because combinations in which products are owned can be useful for gaining insight into household's financial strategies (Gunnarson & Wahlund, 1997), for detecting consumers that are interested in specific financial products (Kamakura et al., 1991; Paas & Molenaar, 2005) and for assessing the priorities that consumers have for owning various financial products (Paas, 1998; Stafford et al., 1982).

In this paper we assess applicability of the lifecycle hypothesis and findings from the literature on the adoption of innovative products and services for explaining financial product ownership in a country with a developing economy, South Africa. The lifecycle hypothesis has been the prominent theory in explaining borrowing and saving behavior of consumers. However, the lifecycle hypothesis has traditionally been applied to explain financial behavior in Western countries

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(Browning & Lusardi, 1996; Wärneryd, 1999), which we define as Northern America, Western Europe, Australia and New Zealand. It remains unclear whether the lifecycle hypothesis applies outside Western countries. In the theoretical section of this paper, Section 2, we propose that literature on innovation adoption may also explain financial product ownership outside Western countries, as financial products in newly emerging economies can be considered as innovations for most consumers (Roos et al., 2005; Steenkamp & Burgess, 2002). Note that we provide one of the few studies of consumer financial behavior outside Western countries (cf. Davies, Easaw, & Ghoshray, 2009; Roos et al., 2005). Researching the relevance of theories, which were developed on data from Western countries only, in newly emerging economies not only provides insights into the generalizability of such theories but also knowledge about the conditions in which such theories apply or not (Burgess & Steenkamp, 2006).

In an empirical study, we analyze a data set of 18,965 respondents from the four main ethnic groups in South Africa: Africans, Coloureds, Asians, and Whites - we use the generally accepted terms for these ethnic groups in South Africa, according to the South African Bureau of Statistics; www.statssa.gov.za, see also Steenkamp and Burgess (2002). The data indicate, for each respondent, ownership of seven products used for borrowing purposes, such as loans and mortgages, and nine products for saving or investing, such as savings accounts and stocks. Using data on age, marital status, and parental status, we define the lifecycle stages in line with Murphy and Staples's (1979) lifecycle operationalization, with necessary adjustments to describe the South African context. We then apply the lifecycle phase of each respondent to predict household financial product portfolios among Africans, Coloureds, Asians, and Whites according to a segmentation technique, latent class analysis (LCA; Fernandez-Blanco, Orea, & Prieto-Rodriguez, 2009; Oppewal, Paas, Crouch, & Huybers, 2010; Wedel & Kamakura, 2000). In our application, the LCA technique simultaneously segments households on the basis of their financial product portfolios and estimates the effects of household lifecycle phase and ethnic group membership on the likelihood for financial product portfolios to occur. On the basis of our findings, we consider the applicability of the lifecycle hypothesis in developing economies or, alternatively, the findings from the innovation adoption literature that are discussed below.

Accordingly, in Section 2, we discuss the lifecycle hypothesis and its applicability in South Africa. In Section 2 we also discuss relevance of findings from the innovation adoption literature for financial product ownership in South Africa. In Section 3 we introduce our data set, describe the revised lifecycle coding that we apply, and discuss the conducted LCA analysis. Section 4 contains the results of this analysis, including the household financial product portfolios we found and the effects of lifecycle stage, ethnic group, educational level, and income on the occurrence of these product portfolios. We conclude with a discussion and implications of our findings, in Section 5.

2. Household lifecycle phase and financial product ownership in South Africa

2.1. The lifecycle hypothesis in South Africa

The lifecycle hypothesis (Modigliani & Brumberg, 1954) and the related permanent income hypothesis (Friedman, 1957) have been prominent theories for describing, explaining, and predicting financial behavior (Browning & Lusardi, 1996; Wärneryd, 1999). Their basic assumption indicates that households avoid income fluctuations across their lifetimes to sustain a constant consumption pattern. As a result, young households should have debts, households in intermediate lifecycle phases save and invest to pay off debts and build a reserve for their old age, and older households tend to spend assets that they accumulated earlier in life (Browning & Lusardi, 1996; Wärneryd, 1999).

Various studies in Western countries show that the variables that constitute the lifecycle hypothesis, such as age, marital status, and having children, all influence the household's financial product portfolio (e.g., Gunnarson & Wahlund, 1997; Paas, Bijmolt, & Vermunt, 2007; Soutar & Cornish-Ward, 1997; Stanley, Ford, & Richards, 1985; Tin, 2000). Households in the intermediate lifecycle stages own financial products for saving or investing purposes, which is in line with the lifecycle hypothesis (Browning & Lusardi, 1996; Wärneryd, 1999). Findings with regard to debts indicate that products such as loans and mortgages are more prominent among younger households (Gunnarson & Wahlund, 1997; Stanley et al., 1985). Furthermore, households in intermediate lifecycle phases own more financial products than others, i.e., they are financially the most active groups (Gunnarson & Wahlund, 1997; Paas et al., 2007; Soutar & Cornish-Ward, 1997).

It remains unclear whether the findings regarding financial product ownership across different lifecycle phases also apply to non-Western countries. Theories developed using only data from Western countries do not necessarily apply in newly emerging markets (Burgess & Steenkamp, 2006; Steenkamp, 2005. Deaton (1989) and Gersovitz (1988) suggest several reasons the lifecycle affects may differ. First, in developing countries, households usually are indecomposable units that survive beyond the individual members, implying that financial decisions occur at the household level rather than the individual level. Saving for retirement becomes less relevant under such circumstances, because children will take care of the elderly members of a family. Second, households in developing countries have lower and less certain incomes, so it may be very difficult, if not impossible, for them to save. Third, borrowing constraints may be stronger for low-income households in developing nations, and thus, borrowing also becomes more difficult if not completely impossible. Fourth, savings may serve as a buffer against uncertain and unpredictable events, instead of for inter-temporal consumption smoothing.

The conditions in developing countries that lead to a questionable applicability of the lifecycle hypothesis apply most strongly to Africans and least to Whites in South Africa (Nga, 2007). The ethnic groups in South Africa have different incomes,

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