Scaling-up formal risk management instruments like weather insurance requires an inquiry into the causes of low take-up rates among agricultural households. Measuring financial literacy and evaluating its impact on financial behaviour poses formidable challenges, as it is often closely correlated with confounding factors, such as liquidity constraints and indebtedness, which affect risk-management decisions. This study attempts to establish a causal measure of the impact of financial literacy on risk-management behaviour by testing a financial literacy module on weather risk hedging with villagers in Gujarat, India.

Researchers from Harvard Business School, IGIDR, and Wharton School conducted a field experiment in which rainfall insurance, a financial derivative for managing rainfall risk in agriculture, where pay-outs are linked to the amount of rainfall measured at a designated station, was offered to 600 farmers in India. A customized financial literacy and insurance education module communicating the need for personal financial management and formal hedging of yield risks was offered to randomly selected farmers. The effect of the financial literacy training and six marketing treatments are evaluated using a randomized control trial. The study provides some of the first evidence that financial education can influence financial behaviour. Results also reveal extremely low financial awareness, cognitive limitations, and poor comprehension of rainfall insurance among the farmers being studied.