

# Reply to the Comment on “Testing Efficient Risk Sharing with Heterogeneous Risk Preferences”

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Aditya Shrinivas and Marcel Fafchamps correctly pointed out that, in Table 3 of the published paper, we misreported the outcome of the test of efficient risk sharing that does not account for heterogeneity in risk preferences. The correct outcome is reported in Table 1 at the end of this note.

As we pointed out in the published version of the paper, the results of the efficiency test under homogenous risk preferences were not new. They were meant to confirm results presented in previous papers (Townsend (1994) and Morduch (2004)). Table 1 documents that, if heterogeneity in risk preferences is not accounted for, efficient risk sharing is rejected at the village level for all three villages, which is the same outcome described in the published version of the paper, and is consistent with the results reported in Townsend (1994). In the published paper, we mistakenly reported that, if heterogeneity in risk preferences is not accounted for, efficient risk sharing is rejected at the caste level for all castes. The correct outcome is that, without accounting for heterogeneity in risk preferences, efficient risk sharing is rejected in Aurepalle for two of the six castes, in Shirapur for two of the three castes, and in Kanzara for one of the four castes. The correct estimates still provide evidence that, if one ignores heterogeneity in risk preferences, efficient risk sharing is rejected

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for many castes. As we discuss in footnote 23 of the published paper, the rejection of efficient risk sharing at the caste level using the standard test that does not account for heterogeneity in risk preferences was not a new result of our paper. Similar results had already been reported using the same data in a paper by Morduch (2004) (see Table 3 in Morduch's paper), where he concludes that efficient risk sharing is rejected at the caste level.

Lastly, we want to point out that, as mentioned in the comment by Shrinivas and Fafchamps, the misreporting of the results in Table 3 occurred during the revision for re-submission of the paper. In the original submission, the results of Table 3 were correctly reported. Also, the Editor and Referees that dealt with our paper had no concern with the outcome of the standard test and made no request about that test when the original submission was reviewed. This can be verified by requesting the Editor's letter and the Referees' reports.

We would like to thank Aditya Shrinivas and Marcel Fafchamps for pointing out the mistake.

## References

- Behrman, Jere R. 1988. "Intrahousehold Allocation of Nutrients in Rural India: Are Boys Favored? Do Parents Exhibit Inequality Aversion?" *Oxford Economic Papers* 40 (1): 32–54 (March).
- Morduch, Jonathan. 2004. "Consumption Smoothing Across Space: Testing Theories of Risk-Sharing in the ICRISAT Study Region of South India." *In: Dercon, S., (Ed.), Insurance Against Poverty. Oxford University Press, Oxford.*
- Townsend, Robert M. 1994. "Risk and Insurance in Village India." *Econometrica* 62 (3): 539–591 (May).

Table 1: Standard Test of Efficient Risk Sharing

	Coefficient on Non-labor Income	Standard Errors	Number of Observations
<b>Aurepalle</b>			
<b>All Households</b>	0.015**	0.004	3635
<b>By caste</b>			
Caste Score=7.5	-0.084	0.147	589
Caste Score=18.75	-0.021	0.131	238
Caste Score=30	0.025	0.021	595
Caste Score=55	0.030**	0.012	944
Caste Score=86.25	0.006*	0.003	595
Caste Score=97.5	-0.001	0.004	238
<b>Shirapur</b>			
<b>All Households</b>	0.006**	0.003	3243
<b>By caste</b>			
Caste Score=5	0.478**	0.097	423
Caste Score=23.75	0.010**	0.004	818
Caste Score=72.5	0.004	0.003	1576
<b>Kanzara</b>			
<b>All Households</b>	0.011**	0.004	3677
Caste Score=11.25	0.008	0.013	611
Caste Score=55	0.031**	0.013	1376
Caste Score=76.25	0.004	0.006	321
Caste Score=91.25	0.005	0.006	738

The sample period corresponds to 1975-1985 for Aurepalle and to 1975-1984 for Shirapur and Kanzara. Household expenditure is the sum of expenditure on non-durable consumption and expenditure on leisure. The caste ranking corresponds to the one considered in (Behrman 1988). (\*\*) and (\*) indicate that the coefficient is significant, respectively, at the 5 and 10 percent level.