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THE PROMISING ROLE OF FINANCIAL LITERACY & FINANCIAL PLANNING

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Abstract:

Economic and financial reforms have given the general people more discretionary income and those who are not part of the official financial system, on the other hand, must be educated about banking. Those who are not part of the formal financial system need to be educated about banking. The financially excluded would benefit from financial literacy since it would enable them to comprehend the benefits and pathways to formal financial system. This study emphasises the relevance of financial literacy as well as research prospects in this field.

Keywords: *Financial Literacy, Financial Planning, Financial Inclusion.*

Introduction:

Give a man a fish and you'll take care of his one meal, but teach him how to fish and you'll take care of the rest of his life. It is not enough for an individual to earn a living; he must also make informed and sensible judgments about what to do with the money once it hits his hands in order to advance economically. Failure to use money wisely leads to rising debt, the abuse of credit facilities, and, in the long run, a slowing of economic progress. Financial literacy, on the other hand, promotes a higher standard of life and a sense of optimism about the future. It aids in smart financial planning - asset accumulation, school funding, and retirement planning – all of which contribute to the growth of the economy.

Making financial decisions can be challenging. For people who aren't familiar with finance, comparing savings or borrowing choices with varied interest rates and term structures can be difficult—and even the most knowledgeable person may need to use calculators or spreadsheets to make genuinely informed judgments. Many households, however, are unaware of these issues and receive little aid in making these decisions. Customers may not obtain relevant feedback on the worth of the financial product they have acquired, unlike when visiting a restaurant or purchasing a certain car, making the standard learning process much more challenging.

As a result, financial literacy—the ability to comprehend financial data and make informed personal finance decisions—is gaining traction in both established and emerging nations as a potentially crucial factor of household well-being.

Literature Review

Fox *et.al.* (2005) in their research paper titled, "*Building a case for financial education*", highlighted the scope and significance of financial education in immense in case of general livelihood and they aimed at improving Americans' financial literacy level. America has seen many financial literacy programs which have through information , advice and encouragement assisted people who wish to reduce their debt level, save emergency funds, save for home, education or for retirement. The most important problem that these programs have witnessed is to prove that they make a difference to the financially literate lives in a positive way. Further the paper concluded that many financial literacy programs fail to have an effective evaluation system which in the long run reduces the impact of such programs. Hence we should develop an effective, evaluative and supportive financial literacy mechanism which understands the real problems of different sections of the society.

Bumcrot, Lin and Lusardi (2011) revealed wide variation in financial literacy across United States (US) measured through financial literacy index constructed by them. Most of the variation was due to differences in the demographic makeup of the states; however, only few states had either higher or lower levels of financial literacy than explained by demographics alone. In addition, significant relationship between financial literacy of a state and that state's poverty level was found.

Financial literacy is an important but often ignored skill that is vital for young people **Jayaraman & Jambunathan (2018)**. This study measured financial literacy levels among high school students in India and found low levels of performance on standard measures of financial literacy. Study showed the levels of financial literacy in India were found to be lower than those in developed countries. The result of the study shows that students, despite having high levels of numeracy, were unable to transfer that knowledge to do financial computations. Researcher hopes this study contribute to raising awareness of financial literacy in India and help in policy making that brings financial literacy programs to the masses. This will prevent people from making bad decisions that will impact the economy, environment, and social well-being of the community in a rapidly growing country like India.

The upshot from this study, despite being from an Indian sample, also provides valuable information for policy makers and educators in similar developing countries around the world.

Setyowati *et.al.* (2018) in the work titled, "*Islamic financial literacy and personal financial planning: A socio-demographic study"* shows that the level of Islamic financial literacy in Solo society is 64.66 percent, however, as OJK found in 2016, the inclusion of Islamic finance in Central Java is only 13 percent. Islamic financial literacy is found to have an effect on financial management planning. A person with a good level of Islamic financial literacy tends to be better at managing finances and the level of Islamic financial literacy is also found to have an effect on the choice of Islamic investment. With Islamic financial literacy anyone will prefer to invest their assets in accordance with Islamic principle. Based on the research, the author expected that the government can continue to provide financial education to the public so that people will not get caught up in illegal and scam investments.

Poongodi & Gowri (2016) in their paper named, *"The financial Literacy and saving /investment behaviour among Indian women, with special reference to Erode City"*. The study analysed the gap between financial literacy and savings/investment among the working women. A small sample of 100 respondents was chosen to participate in the study. The method was used of convenient sampling and only voluntary women were included in the study. The results revealed that the women of the sample were highly educated and moderately fallen in the pay ranges between Rs.15, 000-20,000 per month. The women were aware towards traditional saving/investment avenues, but they had actively diverted their savings to invest from traditional avenues to the modern technically risky capital market operations such as investment in mutual funds, shares, debentures and public or private bonds. Moreover women found not to have restricted their savings in gold and silver rather focussed on investment in real estates and arts and passions. This shows the positive growth sign of liberalisation and women participation in household and national savings/investment.

Most of the studies on financial literacy have been confined to the developed economy context, and investigations into vulnerable farming communities in developing countries have hitherto been neglected. **Gaurav & Singh (2012)** have provided a framework for empirically estimating the relationship between financial literacy and cognitive ability on the one hand and their association with farmers' education on the other. We believe this is an important methodological contribution to the literature on farmer behaviour in the developing world.

Ranjani & Chpora (2011) conducted a study to find financial awareness of working women of Mumbai city by taking sample of 225 women from the age group of 21 to 55 years, with the help of questionnaire primary data was collected by considering various alternatives such as financial awareness, preference for various investment avenues, perception towards investments, Self assessment as an investor, perception regarding riskier investments. Findings of research exploded that respondents accepted that they don't have expertise in financial knowledge. Majority of respondents show assertive attitude towards investing their money. Female respondents preferred such investment options with low risk and high liquidity and even for retirement planning too.

In this article **Krishnakumare *et.al.* (2019)** after going through various studies related to financial literacy, it has been observed that financial literacy has been of paramount interest to various researchers, organizations and economies since last two decades. Various studies have been conducted focusing on the different dimensions of financial literacy and also to assess the impact of different individual's socio-demographic factors on their financial literacy level and it has been generally revealed that there exists a significant relationship between them. The researcher further include that studies were done so as to understand the influence of various factors influencing financial literacy because understanding the factors that contribute or weaken the acquirement of financial literacy could help in making policy interventions to enhance their financial well-being.

Tirupati (2016) In his study trying to make an attempt in understanding the level of financial literacy in urban India, especially of the Bohra Community in the Mumbai Metropolitan Region by collecting 200 samples randomly and presented them with questionnaire. The study concluded as female, single, less educated, sole earning member in the family and not possessing sufficient amount of income.

What Does Financial Literacy Mean?

Financial literacy is the capacity to use information and skills to successfully manage financial resources over the course of a lifetime. Financial literacy is the process through which people obtain a better awareness of their financial condition and learn how to improve it over time by developing financial habits such as saving, budgeting, and planning, and so making better financial decisions.

In India, what do we mean by financial literacy, education, and knowledge?

The primary goal of the Central Government, Regulatory Authorities, and Financial Institutions in India, where the majority of the poor earn less than $2 per day1, is to include the poor and marginalised in the financial system by providing them with low-cost banking and other financial products and services. As a result, while the process of financial inclusion has begun, the supplemental process of financial literacy (Figure 1) has yet to receive the attention it deserves. Spreading financial awareness across India's length and breadth would require regulatory authorities, stock exchanges, and financial institutions to join forces and make joint implementation efforts; however, this is not happening. Much needs to be done to make the average person financially secure and empower him financially for the rest of his life; this cannot be accomplished alone through financial inclusion; it must also include financial literacy, awareness, and information sharing.

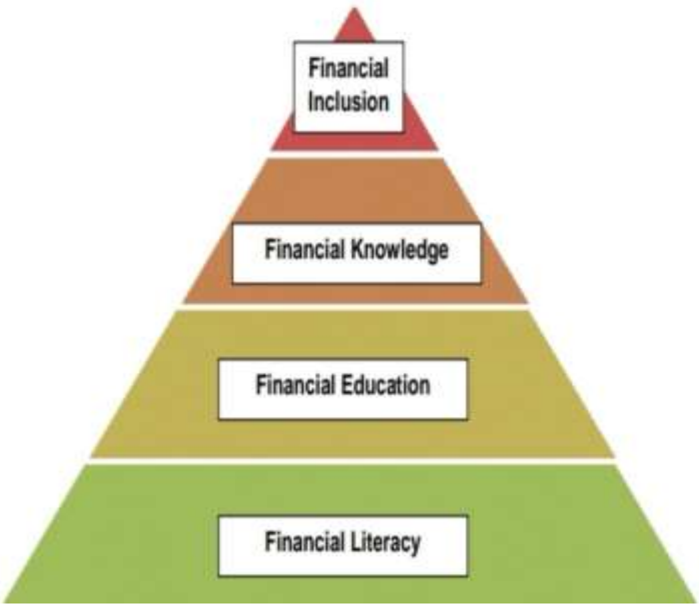


Figure 1- Financial Empowerment Pyramid

Financial Education: Is It Necessary for Different Segments?

Although the importance of financial education cannot be denied, the requirement for different segments of the population differs. It's crucial for the people who have historically been underserved by our banking system. This group is particularly susceptible to the traps set by local money lenders, and they frequently fall prey to them due to a lack of fundamental education, with financial education coming second. Even in the most educated stratum of society, there is a lack of basic financial intelligence. When the economy is healthy, most people's personal financial well-being improves, and collective wealth creation strengthens the economy. Households with a solid financial position consume more and are more willing to make large expenditures. They are also able to put more money into the banking system and are better prepared to use credit to create small domestic companies and cottage industries, which provide jobs and income to tens of thousands of people. This results in a flow of funds and a lot of economic activity, which helps to support the economy's growth and fortification.

Consequences of a Lack of Financial Education

Limited financial market involvement is one of the most obvious implications of low financial literacy. Households that are unfamiliar with the inner workings of a bank, for example, are unlikely to open one, preferring instead to keep cash at home or invest in other forms of value (such as gold), which may provide unappealing returns. For someone with poor financial literacy, refusing to participate in financial markets may be the best option: if she chooses the wrong savings product at a bank, for example, she may end up with an illiquid instrument with high withdrawal costs. A borrower who is unable to fully comprehend the terms of a loan may over-borrow, putting herself at risk of missing a payment and paying significant fines.

The Financial Market is confronted with the following issues:

- Right requires incorrect remedies.
- An excessive reliance on one's own wisdom.
- The instrument's complexity and jargon.
- Smart agents, consultants, and PR have an impact.

Such unethical practises, however, have a significant impact on financial institutions. Established financial institutions value long-term relationships with customers and believe that short-term solutions are ineffective in achieving long-term growth for both the customer and the institution. As a result, financial institutions place a premium on educating customers about the complexities of financial instruments and the market. As a result, it is critical to raise financial literacy among customers by persuading them that they require financial education in order to gain control of their financial situation, improve spending habits, increase savings/investments for future needs, such as children's higher education, ensure prudent use of credit facilities, and contribute to the economy's growth and stability.

Financial literacy has an impact on saving and investing decisions

Because agriculture employs a major portion of the population in many developing nations, such communities are particularly exposed to income shocks caused by weather risk and price volatility in the goods they produce. As a result, home savings can be crucial in allowing households to regulate consumption while also supporting longer-term investments in human and physical capital. While there is a dearth of research linking financial literacy to household savings decisions in underdeveloped nations, there is a plethora of research in wealthy ones.

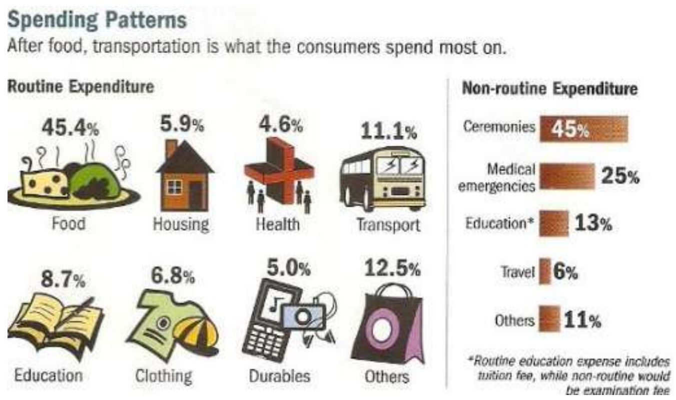
The capacity to comprehend the degree of various investments can have a significant impact on a person's financial well-being. Inflation risk can be significant, and financial literacy is essential to understand which assets offer inflation protection. Similarly, a nuanced understanding of how the value of several assets links with one another can assist households in effectively diversifying risk.

What is India's Income, Savings, and Spending Pattern?

It's a huge undertaking to figure out how Indians earn, save, and spend their money. **Dr. Rajesh Shukla,** head of **NCAER-CMCR**, has done just that in his book *"How India Earns, Saves, and Spends".* The research looks into the relationship between urbanisation and consumption and how they affect the economy. It's worth looking into the findings of the study on personal finance.

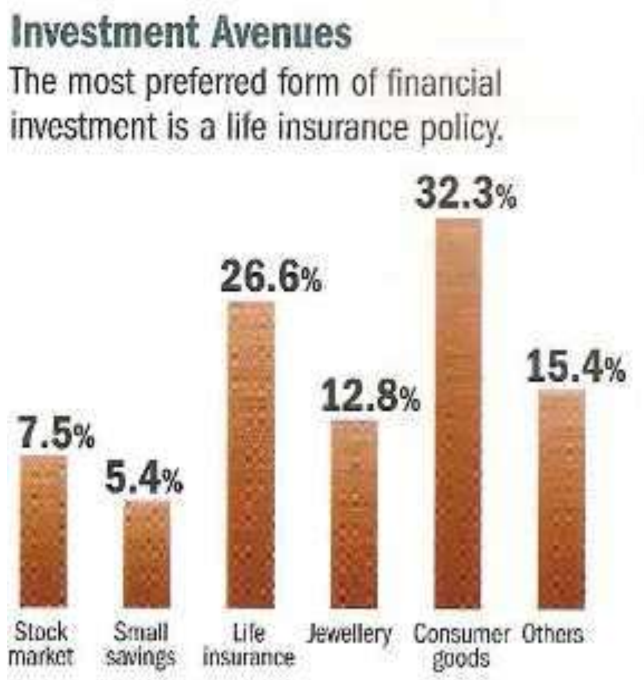
Patterns of Spending:

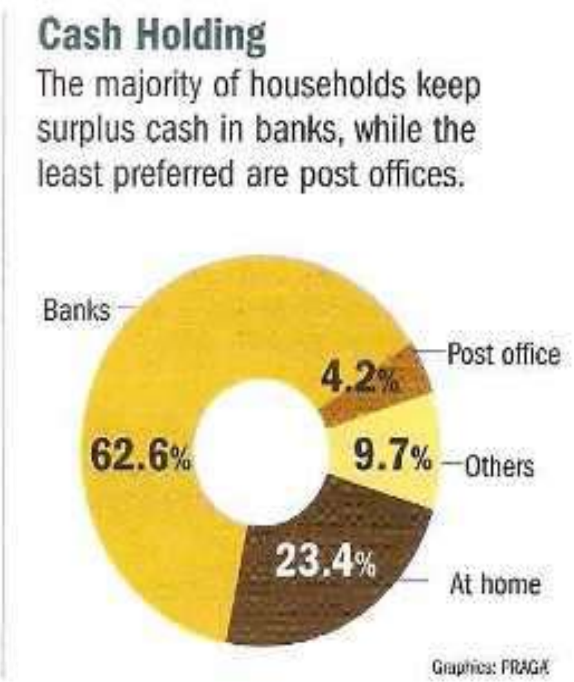
According to the report, urban Indians spend roughly 45% of their income on food. With 11% and 8.7%, respectively, transportation and education finish in second and third place. Ceremonies receive a significant reduction in non-routine spending, while medical emergencies come in second. That is why investors should prioritise planning to cut down on spending on food and transportation, as well as saving for an emergency fund — these are the three most common areas where money is spent. Food, transportation, and education are non-discretionary expenses that cannot be avoided, thus good budgeting is necessary to limit the outlay.



Investment Avenues:

According to the research, the majority of Indians still prefer to invest in life insurance coverage (around 26.6%). This is most likely why practically every investor has a life insurance policy in place. That's unfortunate since it implies most of us are combining investments with insurance, which is designed to protect us. With 13%, jewellery is a distant second. Equity investment is at a low of 7.5 percent, indicating that investors are unaware of the benefits of equity. This isn't one of the best investment strategies. Around 63 percent of investors retain cash in banks, while 23 percent keep it at home! Money sitting in a bank is a waste since it is being eaten away by the inflation monster. This equates to a loss of money! To obtain better returns, investors can put their money into debt funds.





Source: How India Earns, Saves and Spends by "The Wealth Wisher"

When it comes to saving money, the urban consumer puts money aside first for emergencies and subsequently for retirement. Saving for their children's education is also high on their priority list. In my opinion, the saving pattern is excellent. It appears to be the ideal blend for the average Indian. The priorities appear to be correct, although they may be better.

Indians are good savers, but not so good investors:

People in India do not plan for the long term future and avoid investing in long-term instruments, according to a recent nationwide survey of over 60,000 households conducted by the **National Council of Applied Economic Research (NCAER)** in New Delhi and **Max New York Life**. They do, however, save for long-term goals such as emergencies, education, and old age. It indicates that this phenomenon is not limited to poor or middle-class households, but also affects wealthy ones. The following are the findings of the survey:

1. The majority of Indians prefer to maintain 65 percent of their savings in liquid assets such as bank or post office deposits and cash at home, while investing just 23% in physical assets such as real estate and gold and only 12% in financial instruments. 51 percent of Indians place their money in banks to ensure a solid return on their earnings, while 36% of households prefer to retain cash on hand.
2. Postal savings and other guaranteed-return schemes and programmes account for a small percentage of total savings. Only 5% of families invest at post offices, whereas 2% buy insurance and 0.5 percent engage in shares.
3. Despite the fact that life insurance is one of the most popular financial tools (approximately 78 percent of households are aware of it), only 24% of households have a policy.
4. It implies that Indian households have a high propensity of saving. While household income is a significant determinant in determining savings patterns, variations in savings behaviour are also determined by education and occupation. According to the report, 83 percent of the households polled saved for an emergency, with children's education coming in second (81 percent). While just 69 percent of households set away money for retirement, 63 percent set aside money for future expenses such as weddings, births, and other social events.
5. According to the report, over 47% of households saved to purchase or build a home, while a comparable amount saved to enhance or expand their business. Only 22% of

households set aside money to buy consumer goods, while 18% set aside money for presents, donations, or pilgrimages.

6. According to the poll, incentive to save and the necessity to satisfy old-age requirements are the two key factors driving increased savings as people get older.
7. The study also reveals a direct relationship between education and savings by showing that households headed by grads had the highest amount of savings in both absolute and percentage terms.
8. The survey demonstrates that while saving is a good habit, the method of saving is insufficient, as only a small portion of total savings is deposited in a government account, which is insufficient to carry out various plans efficiently.
9. In the event of a loss of income due to an unforeseen catastrophe such as the death or incapacity of the primary earner, the poll finds that 96% of households would be unable to survive for more than a year on their present savings. The majority of individuals polled, on the other hand, expressed optimism about their financial situation. They were unaware of the more effective routes for long-term investing due to a lack of awareness of their financial preparedness for income loss.

Financial Literacy's Emerging Role

Financial literacy refers to the ability to grow, monitor, and effectively employ financial resources to improve one's own, families, and business's well-being and economic security. Many nations, both developing as well as developed, have initiated financial education or financial literacy programmes for their citizens, recognizing the need of financial education. The OECD has published "Recommendations on Principles and Good Practices for Financial Education and Awareness," which is available at the following link:

i. Governments and all stakeholders should support financial education that is neutral, fair, and well-coordinated.
ii. Financial education should begin in school so that people can begin learning about money as soon as feasible.
iii. Financial education ought to be an element of effective financial institution governance, with a focus on accountability and responsibility.
iv. Financial education should be distinguished from commercial advice, and financial institution employees should be subjected to code of conduct.
v. Financial institutions should be urged to ensure that clients read and comprehend

information, particularly when it comes to long-term commitments or financial services with potentially major financial ramifications; small print and cryptic documents should be avoided.

vi. Important life-planning factors, such as basic savings, debt, insurance, and pensions, should be emphasised in financial education programmes.

vii. Programs should be geared at increasing financial capacity, aimed at specific groups, and as individualised as feasible.

viii. Future retirees should be informed about the importance of evaluating the financial viability of their current public and private pension plans.

ix. High-risk concerns for financial customers (such as fraud) should be promoted through national campaigns, specific websites, free information services, and warning systems.

India's current state of financial literacy

The importance of financial literacy has increased as a result of the global economic crisis. Many countries defaulted on loan payments around the world, and hundreds of thousands of ordinary people experienced serious financial difficulties. Many people in India, too, encountered huge difficulties and hurdles in their financial lives after taking on debts or making poor financial judgments during the boom time. As a result, Financial Literacy is no longer a choice. Therefore the government is forming the **Financial Stability and Development Council (FSDC)**, which will focus on financial literacy and inclusiveness. Only a few organisations in India are now engaged in the issue of financial literacy. The following are some of them:

1. **Reserve Bank of India (RBI)** - The Reserve Bank of India (RBI) is quite engaged in the area of financial literacy in India. The Reserve Bank of India has created money and banking cartoons that may be downloaded for free at *www.rbi.org.in*/Financial Education. The RBI's major focus is still on financial inclusion, and one of the areas where it is attempting to raise awareness is financial literacy. The Reserve Bank of India has instructed public and private banks to promote financial inclusion aggressively while ignoring financial literacy. As a result, the RBI has a lot of work to do to make financial literacy and education a mass movement in India.
2. **ICAI, ICSI, and ICWAI** - These organisations have their own financial education and investor awareness initiatives, and they also receive funding from the MCA and other government ministries. Rather than initiatives for the wider public, these institutions

are concentrating on raising investor knowledge within the middle class and their own member groups.

3. **MCA (IEPF) -** The Investor Education and Protection Fund (IEPF) is a programme run by the Ministry of Corporate Affairs to raise financial and investor knowledge. MCA, on the other hand, is mostly focused on adult programmes, such as investor awareness camps.
4. **SEBI -** Many stock market investor associations are registered with SEBI. SEBI's National Institute of Securities Markets (NISM) department runs investor education programmes.
5. **Stock exchanges -** The NSE, BSE, MCX, and others all have investor awareness programmes and publish articles and propaganda on a regular basis. These groups are primarily concerned with encouraging public participation in the stock markets, rather than with financial literacy.

Financial literacy research opportunities

Financial literacy is critical for avoiding and resolving financial issues, as well as enjoying a prosperous, healthy, and happy life. As a result, financial literacy has emerged as a popular research topic, with the emphasis expected to shift toward the implementation and evaluation of strategies to improve the financial literacy levels of specific cohorts of people who have been identified as lacking in financial knowledge and skill. Furthermore, the large number of people with little financial literacy poses a severe threat to both nations' economic well-being and individuals' personal well-being. As a result, research is essential to define relevant and accurate criteria for continuous financial literacy measurement. Continued technological improvements, as well as requirements for saving, borrowing, investing, retirement, medical, and insurance coverage, will give more push for financial literacy study.

Conclusion

Financial literacy is becoming increasingly vital for the nation's economic future, and it is critical that it be directly linked to financial behaviour, and hence financial success and sustainable development. This has yet to be accomplished in a financial literacy study. Another topic of research is establishing which aspects of financial literacy are most and least important for financial success and sustainability. Numerous studies show that personal financial knowledge and abilities are largely learned through 'trial and error,' but no study has looked at what types of financial experiences and qualities have the most impact on an individual's personal financial literacy or competence. Another focus of research is on acquiring detailed information of financial experience and attributes, which may prove to be major influencing variables in modelling financial literacy in general populations.

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