International Journal of Education, Modern Management, Applied Science & Social Science (IJEMMASSS)
ISSN : 2581-9925, Impact Factor: 7.150, Volume 06, No. 02(II), April - June, 2024, pp. 223-228

AN EMPIRICAL STUDY ON IMPLICATIONS OF FINANCIAL LITERACY ON FINANCIAL WELL-BEING

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ABSTRACT

The study aimed to assess the level of financial literacy among individuals in Delhi. The implications of financial literacy on financial well-being were analysed. Financial literacy was measured using three dimensions: financial attitude, financial knowledge and financial behaviour. An attempt was also made to identify financial knowledge under/overconfidence. The relationship between various socio-demographic factors with financial literacy and financial well-being was also analysed after investigation. The primary data was collected and analysed using statistical tools such as percentage analysis, t-test, ANOVA, linear multiple regression analysis, and chi-square analysis and finally, a Structural equation model was constructed to understand the impact of financial literacy on financial well-being. The analysis uncovered some significant findings, which are summed up in this paper. Various areas of concern are also identified and suggestions are offered to improve financial literacy and enhance financial well-being.

Keywords: *Financial Literacy, Financial Well-Being, Financial Knowledge, Financial Behaviour, Financial Attitude.*

Introduction

Financial literacy involves knowledge about financial concepts, and the capability to apply it to make informed financial decisions for the financial well-being of the individual. The level of financial literacy of a country serves as a good signal of the country's economic growth and development. It expands the financial system and helps individuals in addressing their day-to-day financial problems. It helps people make better financial choices, in knowing why long-term investments are better and in knowing about complex finance-oriented products & services. It makes consumers aware of their rights and responsibilities as clients of finance-oriented products & services. Thus, financial literacy plays a significant role in today's complex financial environment. It empowers individuals to manage their finances and enhances their skills and knowledge. It ensures that the financial system is inclusive and individual's financial well-being is enhanced. The current study attempts to analyse and understand the level of financial literacy and its implication on financial well-being.

Objectives:

The objectives of the study are:

- To determine the level of financial knowledge among people.
- To access the financial behaviour of people.
- To analyse the financial attitude of people.
- To examine the relationship between financial literacy level and financial well-being of select individuals.
- To study the mediating effects of financial inclusion in the relationship between financial literacy level and financial well-being.

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Review of Literature

According to the paper by Chen and Volpe titled "An Analysis of Personal Financial Literacy Among College Students" in the USA in 1998- The authors explored students' personal financial literacy level and knowledge influence on their financial decisions. Results showed that student's knowledge of finance is low and due to inadequate financial knowledge, their financial decisions also get affected. It was concluded that limited financial education is the main reason behind low financial literacy

According to the paper by Robb and Woodyard titled "Financial Knowledge and Best Practice Behaviour" in the USA in 2011- The authors showed that knowledge of finance has significantly influenced behaviour but alone it is insufficient to influence financial behaviour. Income, financial satisfaction, financial confidence and education also play significant roles in determining best financial behaviour.

According to the paper by Agarwalla titled "A Survey of Financial Literacy among Students, Young Employees and the Retired in India" in India in 2012- The authors evaluated the financial literacy of Indians and found a low level of financial knowledge among Indians. The study revealed that Indians have a limited understanding of personal financial concepts like the impact of inflation on prices, risk diversification, interest, etc. Findings also reported that Indians performed better on behaviour and attitude dimensions. Positive financial behaviour and positive financial attitude offset low financial knowledge and led to an average financial literacy score which is on parity with the results of 13 countries studied by OECD.

According to the paper by Ramos-Hernández titled "Financial Literacy Level on College Students: A Comparative Descriptive Analysis between Colombia and Mexico" in 2020- The authors did a comparative study among college students of Mexico and Columbia and found low levels of financial literacy for both countries. Findings also revealed that students were not aware of various financial topics i.e. diversification of risk, savings and investment options, inflation concepts, and future planning for retirement. Authors emphasised that financial literacy efforts should be directed towards college students as they are in an important stage of their lives i.e. starting to enter into the working stage.

According to the paper by Kim titled "Relationships Among Credit Counseling Clients' Financial Wellbeing, Financial Behaviours, Financial Stressor Events, and Health" in the USA in 2003- The authors' study found financial behaviour as one of the predictors of financial well-being and suggested that the financial well-being of an individual could be enhanced through improved and positive financial behaviour.

According to the paper by Falahati and Paim titled "Gender Differences in Financial Well-Being among College Students" in Malaysia in 2011- The authors conducted a study among Malaysian College students and found a lower level of financial knowledge for female students than male students. The findings also showed that students with previous financial socialisation and higher financial knowledge experience little financial problems which ultimately enhances their well being in finance.

According to the paper by Taft titled "The Relation between Financial Literacy, Financial Well-being and Financial Concerns" in 2013 -The authors conducted a study and evaluated the association between financial literacy and financial well-being among University Professors in Iran using regression analysis. The study found that a unit increment in the financial literacy level leads to a 0.93 unit increment in the well-being of the individual. It promotes individuals' participation in economic activities in the form of savings, investment, asset management, credit management, etc. It enables individuals to assess their financial position, comprehend their economic situation and worry less regarding financial issues which ultimately enhance their financial well-being.

According to the paper by Chu titled "Financial Literacy, Portfolio Choice and Financial Well Being" in China in 2016 - Authors conducted a study among households and found that high financial literacy levels showed good financial outcomes in the form of positive investment return and this contributes to household financial well-being level.

According to the paper by Adam titled "Financial Literacy and Financial Planning: Implication for Financial Well-Being of Retirees" in Ghana in 2017 - The study developed a model studying the relationship between financial literacy, financial behaviour, retirement planning and financial well-being among retirees of Ghana using Partial Least Squares and SEM. The study found a positive association between financial literacy and well-being. It helps people in planning for their retirement and managing their money effectively. This will result in better financial well-being.

Thus, the study focused on promoting financial literacy and retirement planning.

According to the paper by Lee titled "Consumer Financial Well Being: Knowledge is Not Enough" in the USA in 2019- The authors analysed the relationship between financial knowledge and financial well-being and observed increased financial well-being levels of individuals having an understanding of basic financial concepts along with applications. The study also confirmed that to increase financial well-being, individuals should plan to attain future financial goals along with financial knowledge.

Methodology

Individuals aged above 18 from the National Capital Region (NCR) of India were taken randomly to comprise the sample. A convenience sampling technique was used to carry out the present study.

As the population size of individuals in the National Capital Region (NCR) of India is more than 10,00,000, therefore it is planned to take a sample size of 500 individuals from the National Capital Region (NCR) of India in the final sample leaving enough scope to meet the issues of non-response and data cleaning requirements.

- **Primary Data:** A structured questionnaire has been used to collect primary data. 550 questionnaires were distributed offline. Respondents were approached directly. Overall, there were 476 valid responses received from offline mode. Overall, the response rate was approx 95.2%.
- **Secondary Data:** Newspapers, journals, books, RBI website, magazines and other relevant websites have been used to collect secondary data.

Both the data collected were studied and analysed. The total score of each respondent was calculated. The total score of each respondent was further converted into their percentage score and further mean and standard deviation was calculated. The following hypothesis was developed.

The hypothesis of the Study

Hypothesis 1

H_1: Financial knowledge (FK) significantly predicts the financial literacy (FL) level.

Hypothesis 2

H_2: Financial attitude (FA) significantly predicts the financial literacy (FL) level.

Hypothesis 3

H_3: Financial behaviour (FB) significantly predicts the financial literacy (FL) level.

Hypothesis 4

H_4: The financial well-being of select individuals is significantly influenced by financial literacy level.

Results:

- The overall mean score for financial knowledge is 12.76 out of a maximum possible score of 20 and SD is 4.97. It is found that 28% of the respondents have a high level of financial knowledge, 46% have a moderate level of financial knowledge and 26% of them have a low level of financial knowledge.
- The mean score of the respondents for basic financial knowledge is 5.23 out of a maximum possible score of 8 and SD is 2.10. On average, respondents have answered more than 60% of the questions on basic financial knowledge 'correctly'.
- 85.45% of the respondents are aware that credit card holders have a credit limit, whereas only 46% of them are aware that buying goods availing services on credit will reduce their purchasing power in future.
- 79.22% of the respondents are aware of the concept of simple interest, whereas only 64.94% of them are knowledgeable about compounding.
- On average 72% of the respondents have an understanding about inflation and answered the two questions on inflation 'correctly'.
- The mean score of the respondents for advanced financial knowledge was 7.53 out of a maximum possible score of 12 and SD 3.22. On an average respondents have answered a little over 50% of the questions on the advanced financial concept 'correctly'. It is to be noted that a

lesser percentage of respondents are aware of advanced financial concepts compared to basic financial concepts. A greater amount of deviation in the answers given by respondents is found in advanced concepts compared to basic concepts.

- 77% of the respondents are aware of the functions of the stock market and only 68.31%, understand the meaning of a stock.
- 74.55% of the respondents understand the features of a mutual fund whereas only 51.95% are aware of the returns from a mutual fund.
- 65.97% of the respondents know the meaning of bond/debenture. However, just over one-third of the respondents, 35.71% which is a very small percentage, are aware of how bond prices move.
- 52.08% of the respondents are aware of the comparative risk and return of a company stock and a mutual fund and 67.66% are knowledgeable about the risk factor is stocks and bonds/debentures.
- 86.62% of the respondents are well aware that stock prices fluctuate over time and 74.16% of them have an understanding that over a long period (eg) 10 years, stocks of good companies usually give a higher rate of return than saving accounts.
- 70.13% of the respondents seem to be knowledgeable about the concept of diversification.
- 72.34% understand that the longer the duration of the housing loan, the higher the cost of financing it. The analysis reveals that 30% of the respondents have a low or negative financial attitude, 42% have a moderate or neutral financial attitude and 28% have a high or positive financial attitude.
- Respondents' belief in planning is analysed by considering their attitude towards drafting a will, being certain about where money is spent, certainty that investments are safe, and risk-taking attitude to improve one's financial position. The respondents have an average score of 17.36 out of a maximum possible score of 25 for this factor.
- The propensity to save is analysed by considering the attitude of the respondents towards saving money. On average, respondents have a score of 15.36 for this factor out of a maximum possible score of 25.
- Confidence in personal financial management is measured by studying the attitude respondents exhibit in planning and managing their finances, decision-making, understanding various financial services and worrying about meeting normal living expenses. The respondents have a mean score of 27.70 for this factor, out of a maximum possible score of 40.
- 58% of the respondents find it satisfying to save for the long term, 44% of the respondents tend to live for today and let tomorrow take care of itself and only 17% of them agree that money is there to be spent.
- It is found that 26% of the respondents have a good or desirable financial behaviour, 48% of the respondents have a moderate financial behaviour and 26% of them have a poor or undesirable financial behaviour.
- To comment on debt management, the researcher aims to understand how respondents make loan payments, pay for monthly expenses and manage debt. Financial behaviour such as paying bills on time and borrowing to make ends meet also are analysed in this factor. The mean score of the respondents for this factor is 19.23 out of a maximum possible score of 25 and SD is 4.70.
- To understand how respondents monitor personal finance, they are asked if they draft a monthly budget, before buying something if they consider whether they can afford it, if they identify needs and wants separately and do a good job balancing spending and savings. On an average respondents have scored 22.63 out of a maximum possible score of 30 and the SD is 4.61.
- The long-term planning behaviour of the respondents is studied by analysing if respondents have retirement plans, if they have set long-term financial goals and strive to achieve them if they save money for the long term and plan on substantially increasing their income in the long run. Respondents have a mean score of 24.07 out of a maximum possible score of 35 and an SD of 7.04.

- Emergency and risk management behaviour are analyzed by investigating if respondents have set aside emergency funds if their financial situation is such that it would cover their expenses for 3 months in case of emergencies, and if they are adequately covered by health insurance. The mean score of the respondents for this factor is 10.92 out of a maximum possible score of 15 and an SD of 2.87.
- Advice-seeking behaviour of the respondent is analysed by asking respondents if, in the last 2 years, they have asked for advice from a financial professional if they usually talk to friends or peers about money management issues and if they update themselves on various financial issues from sources like TV, Newspaper etc. On average respondents have scored 10.49 out of a maximum possible score of 15 and SD 2.69.
- Around 72% of the respondents have set up an emergency fund, and 62% of them have a backup fund which would cover 3 months' expenses in case of emergencies.
- 59% of the respondents have the habit of drawing up a monthly budget, and 88% of them pay their bills on time always.
- 86.2% of the respondents do consider if they can afford something before buying it whereas a little over half (56.6%) of respondents buy things even if they can't afford it.
- 69.3% of the respondents have set long-term financial goals, 45.8% have started saving money for retirement and 63% are adequately covered by insurance.
- 38% of the respondents have the habit of taking loans to cover their monthly expenses whereas 59% tend to save money each month. 68.7% of the respondents have reported to be keeping a close watch on their financial affairs.

Interlinkages – Financial Knowledge, Financial behaviour, Financial Attitude and Financial Well-being

- A strong association is found between all three dimensions of financial literacy (i.e.) financial knowledge, financial attitude financial behaviour and financial well-being based on the chi-square test.
- It is found that 53% of the respondents with a high level of knowledge have a high level of attitude, 52% of respondents with moderate knowledge have a moderate attitude and 63.30% of respondents with low knowledge have a poor attitude.
- 46% of respondents with high knowledge have good behaviour, 59.6% with moderate knowledge have moderate behaviour and 65.80% with low knowledge have undesirable financial behaviour.
- 61.90% of respondents with a positive attitude have good financial behaviour, 65.5% with a moderate attitude have moderate behaviour and 59% with a negative attitude have undesirable financial behaviour.
- 44.20% of respondents with high knowledge have high financial well-being, 63.80 with moderate knowledge have moderate well-being and 65.30% with low knowledge have low well-being.
- 56.70% of respondents with positive attitudes enjoy good well-being, 64.90% with moderate attitudes have moderate well-being and 55.10% with negative attitudes have low well-being.
- 49.7% of respondents with good behaviour enjoy good well-being, 62.90% with moderate behaviour have moderate well-being and 62.70% with bad behaviour have bad financial well-being.
- Karl Pearson's correlation is greater than zero. It shows that a positive relationship exists between the dimensions of financial literacy i.e. (knowledge, behaviour and attitude) and well-being.

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