

A Study of Determinants Influencing Financial Literacy of Individual Investor in India

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Abstract: Investment scenario is changing very fast and financial literacy impacts financial decisions of individual investors. The present study is exploratory in nature and determines the factor that affects financial literacy and how they affect decision making. The sample consist of 649 individual investors to obtain information through structured questionnaire from various parts of India. The result indicated that there are seven most influencing factors of financial literacy that affects investor decision making are: Attitude, Knowledge, Budgeting Habits, liquidity, self analytical skills, Emotional Inclination and Goal Planning. This study will help to determine strategies which will help to improve financial literacy of an individual investors.

I. INTRODUCTION

Financial Literacy is a buzz word today and it plays a vital role in the economies of the world. With the advent of globalization and liberalization, there are variety of complex modern products available in the market. Very few fractions of people in our population have access to them. (Lusardi and Mitchell, 2007). Financial literacy is the education and understanding of various financial products (Source: Investopedia), it lays main focus on personal financial management which is the ability, skill and attitude of a person to manage personal finances on the basis of knowledge about various investment options available in the market. Financial illiteracy is not an issue unique to any one person but it is the reality of masses. It affects everyone: men and women, young and old, across all the racial and socioeconomic lines. It has become imminent to raise the financial literacy level as we cannot ignore this problem anymore. The economic future of India depends on it. We need to impart capacity building to the masses in such a way that an individual becomes capable of making informed financial choices in personal life. Personal financial management connotes to sound analysis on the basis of risks and returns of various investment options before doing any investment. Financial literacy involves broader comprehension of ethical, social, political and environmental dimensions of finance. (Noctor et al, 1992 apud Kempson et al, 2005)

II. CONCEPTUAL FRAMEWORK AND REVIEW OF RELATED LITERATURE

Trivedi and Trivedi, 2014 states that the financial system of country is the sole backbone of its economy. But the financial systems are helpful only when they are utilized and properly distributed among the total population of the country. For the country like India which involves a large number of illiteracy

among the population, it is desired to implement the financial literacy among the uneducated people for any kind of financial product to become successful. Financial literacy can be defined on the basis of OECD (organization of economic cooperation and development) which is an international organization for economic progress and world trade. It depicts that financial literacy is measured with the level of financial knowledge, financial behavior and financial attitude of the overall population.

Athreya and Stilwell, 2009 during 2008, the FLEC (financial literacy and education commission) developed the research priorities in order to study the financial literacy. 'The FLEC Research and Evaluation Working Group determined that it was time to update the 2008 research priorities and to expand these with a set of key research questions. These research priorities are intended to inform the FLEC as a whole, individual member agency and their sub-agencies, other federal government supporters of research, as well as private sector and academic researchers and other research funders. The objective is to address the most important questions facing the field, reduce duplication and overlap in the field, and make best use of limited research dollars. The present report investigates the influence of various socio-demographic factors on different areas of financial literacy in growing India.

Barua, Jacob, Varma and Agarwalla, 2013, states that the financial literacy in the country is influenced by the various factors such as education, income, gender, caste etc, some other factors such as orientation also depicts the verdict of financial literacy which are influenced by the authorities. It can be explained as the orientation factors such as joint family focuses over consultative decision making among the family by the higher authorities. This report derivates on poor financial literacy due to lack of decision making powers and portfolio diversification. Various explanations have been advanced to explain the diversification issue. In this report the main focus is over lack of financial literacy as one potentially important factor.

Guiso, and Jappelli, 2008 states that financial literacy affects from lowest to highest levels in our life such as from households' behavior to education of children. Financial literacy is an understanding of the most basic economic concepts needed to make saving, borrowing and investment decisions and the perception that ordinary investors should have regarding market rules, financial products, financial

organizations and regulations. Financial illiteracy or low of financial literacy leads to lack of healthy financial ways of decision making, lack of necessary financial knowledge and in turn poor financial performance. First item judged in financial literacy is financial knowledge. It measures knowledge of financial products, how to access them, difference in variants offered, interest calculations, understanding about risk and return, time value of money, portfolio investment etc

Varma, 2003, states that as of the literature review, the status of financial literacy in India is not satisfactory, especially in the rural areas. These rural areas of India are affected by malnutrition, unemployment, poor education and poverty. People are unaware of financial services offered to them such as banking services which helps them in saving their valuable assets and providing them return on their savings such as security and interest over their savings. The rural areas have trend of borrowing money from the lenders at high interest rates which is the traditional method in India. The role played by governments and employers in managing investments on behalf of individuals has shrunk significantly in the recent past as a result of changes in the social support structures across the world. This has increased individuals' responsibility in managing their own finances and securing their financial future. In an environment where the range and the complexity of financial products continue to increase, it is imperative that individuals develop nuanced understanding of the world of finance to be able to make choices that are most appropriate to their financial goals and needs. The level of financial literacy among the working young in urban India is similar to the levels that prevail among comparable groups in other countries. The inferences reached by the study on the influence of several socio-demographic variables in the Indian context also confirm inferences reached by studies elsewhere. For example, the influence of family income and gender on various dimensions of financial literacy is similar to the influence recorded in other studies.

III. RESEARCH METHODOLOGY

Questionnaire Development

The self structured questionnaire was built for analysis consisting of various questions related to individuals' financial literacy related to various investments options which individual opts for its personal financial management. The questions helped to identify the level of financial literacy which an individual possess. The target group consists of various individuals who manage their finances from all over India. Finally all information was obtained by 40 item index.

The research developed the criteria that individual possess financial literacy before investing in various alternatives available. Finally all information was obtained by 40 item index. For each item a 7 point scale was developed from "Strongly Disagree" to "Strongly Agree". A questionnaire response was collected from businessman, salaried individuals and self occupied professionals of age groups ranging from above 20 to above 40 years of age from various parts of India.

Hypothesis

As per the prior discussion, the present study accesses in detail the effects of financial literacy of individual customers. Specifically, we examine the effect of literacy on customer in terms of financial changes in industry.

H₁: To determined factors affecting financial literacy of Individual Customers.

Reliability and Validity

The present study was aimed at understanding the impact of various factors of financial literacy on various personal management decisions. For this purpose, 650 respondents were selected from various parts of the country. The sample was divided into four parts i.e. North, East, West and South. The part of data was collected online through Google docs and rest was collected through offline mode. The respondents were screened as individuals who were beyond the age of 20, earning and managing their finances by investing in various investment alternatives. Reliability of was defined with Cronbach alpha which was 0.926 and at 40 items.

Statistical Analysis

Data on financial literacy was first analyzed by factor analysis KMO and Bartlett Test. Bartlett (1938), Bartlett (1951) as factor analysis is a means of examining and describing the internal structures of variables (Lawley and Maxwell, 1926).

For all analysis, authors used SPSS (version 20), setting = 0.05.

IV. RESULTS, FINDING AND ANALYSIS

H₁: To determined factors affecting on financial literacy of Individual Customers.

Factor Analysis

The Kaiser Mayer- Olkin (Table 2) measure of sampling adequacy was 0.948 and the Bartlett tests of sphericity were found to be significant at $p < 0.001$.

Table 1 Showing values of KMO and Bartlett's Test

KMO and Bartlett's Test		
Kaiser-Meyer-Olkin Measure of Sampling Adequacy.	Approx. Chi-Square	.948
		12997.064
Bartlett's Test of Sphericity	Df	780
	Sig.	.000

The Kaiser-Meyer-Olkin Measure of Sampling Adequacy value here .948 and Bartlett's Test of Sphericity were also found to be significant at $P < .001$.

Table 2 Showing Total Variance explained

Component	Total Variance Explained						
	Initial Eigenvalues			Extraction Sums of Squared Loadings			Rotation Sums of Squared Loadings
	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %	Total
1	14.882	37.204	37.204	14.882	37.204	37.204	8.508
2	2.025	5.063	42.267	2.025	5.063	42.267	6.206
3	1.728	4.320	46.587	1.728	4.320	46.587	5.465
4	1.217	3.043	49.630	1.217	3.043	49.630	7.046
5	1.164	2.911	52.540	1.164	2.911	52.540	8.928
6	1.087	2.717	55.257	1.087	2.717	55.257	4.377
7	1.043	2.608	57.865	1.043	2.608	57.865	4.148
8	.979	2.447	60.312				
9	.918	2.295	62.607				
10	.900	2.251	64.857				
11	.818	2.044	66.902				
12	.789	1.972	68.874				
13	.781	1.951	70.825				
14	.711	1.777	72.602				
15	.707	1.767	74.369				
16	.656	1.640	76.010				
17	.625	1.562	77.571				
18	.610	1.524	79.095				
19	.586	1.465	80.560				
20	.559	1.398	81.959				
21	.522	1.304	83.263				
22	.505	1.262	84.525				
23	.479	1.198	85.723				
24	.476	1.189	86.912				
25	.453	1.132	88.044				
26	.431	1.076	89.120				
27	.395	.988	90.108				
28	.383	.958	91.066				
29	.367	.919	91.984				
30	.351	.878	92.863				
31	.346	.865	93.727				
32	.336	.839	94.567				
33	.323	.807	95.374				
34	.314	.785	96.160				
35	.298	.746	96.906				
36	.288	.719	97.625				
37	.273	.683	98.308				
38	.258	.644	98.953				
39	.234	.584	99.537				
40	.185	.463	100.000				

The cumulative total variance values here ranges from 37.204 % to 57.865 % which is moderate and can be further increased to optimize the results.

Table 3 showing 40 items for financial literacy with its mean and standard Deviation

	Mean	Std. Deviation		Mean	Std. Deviation
F1	4.57	1.800	F21	4.70	1.717
F2	4.43	1.883	F22	4.78	1.777
F3	4.92	1.822	F23	5.22	1.693
F4	4.83	1.980	F24	4.92	1.767
F5	5.23	1.721	F25	4.72	1.788
F6	4.80	1.782	F26	4.75	1.708
F7	4.38	1.783	F27	4.88	1.771
F8	5.24	1.727	F28	4.92	1.839
F9	5.33	1.735	F29	5.26	1.708

F10	5.07	1.624	F30	4.73	1.852
F11	4.95	1.850	F31	5.10	1.743
F12	4.57	1.753	F32	5.03	1.736
F13	4.58	1.843	F33	4.69	1.845
F14	5.06	1.775	F34	5.06	1.754
F15	4.19	1.821	F35	4.97	1.725
F16	4.18	1.836	F36	5.03	1.852
F17	4.58	1.891	F37	5.13	1.713
F18	5.41	1.605	F38	5.18	1.672
F19	4.83	1.789	F39	5.14	1.739
F20	4.79	1.741	F40	4.92	1.750

N = 642, Mean total = 195.07, S D total = 70.91, Variables= 40

Analysis

According to the scale used the maximum score to be received is 280 if all the 40 items were rated at 7 point scale. However

the mean score 195.01 indicated that 69% of the constructs are explained by items. It indicates that financial literacy of individuals regarding various investment options or personal financial management tools was good.

Table 4: Showing results of factor analysis

S.No.	Attitude	Knowledge	Budgeting habits	Liquidity	Self Analytical Skill	Emotional Inclination	Goal Oriented
F1		.558					
F2		.643					
F3		.549					
F4	.612						
F5						.698	
F6							.632
F7		.766					
F8		.643					
F9	.698						
F10	.606						
F11						.577	
F12							
F13				.523			
F14	.594						
F15				.743			
F16				.813			
F17				.599			
F18					.615		
F19					.735		
F20					.762		
F21		.571					
F22					.674		
F23					.621		
F24							.581
F25							.632
F26							.524
F27	.574						
F28	.646						
F29	.614						
F30				.623			
F31	.572						
F32	.752						
F33				.581			
F34			.814				
F35			.741				
F36					.686		
F37					.566		
F38			.506				
F39					.623		
F40					.703		

FC1: Attitude

This is the most important factor as inferred by the following figures 37.204% of the total variance is 14.882. The scale reliability for this factor is 0.5. The factors covered here are: time horizon of insurance policies, retirement planning, and investments in FD's and post office deposits. These components require specific attitude for investments as it can be positive or negative. Any increase in financial literacy level of an individual will make their attitude more positive and informed..

FC2: knowledge

This is the second most important factor explaining 42.267% of the total variance is 2.025. The scale reliability for this factor is 0.5. The factors covered here are; health insurance, hospitalization reimbursements and cashless facilities, ULIP's (investment as well as insurance), tax benefits of health insurance and life insurance, liquidity attached to mutual funds etc. Financial literacy is attributed by knowledge about various financial alternatives available.

FC3: Budgeting Habits:

This is the third most important factor explaining 49.630% of the total variance is 1.728. The scale reliability for this factor is 0.5. The factors covered here are; investments in gold as a part of portfolio or coverage against inflation, proper balance should be maintained between debts and equity. Budgeting habits varies from person to person depending upon an individual's financial literacy.

FC4: Liquidity:

This is the fourth most important factor explaining 52.540% of the total variance is 1.217. The scale reliability for this factor is 0.5. The factors covered here are; loan against Personal Provident Funds, PPF withdrawal facilities, fixed deposits regular income schemes, maintaining 3 months' salary as a backup in bank accounts etc. Financial literacy is directly linked with liquidity as when we manage our finances this is one of the crucial factor which affects an individual's financial decision.

FC5: Self Analytical Skill

This is the fifth most important factor explaining 2.911% of the total variance is 1.164. The scale reliability for this factor is 0.5. The factors covered here are: mutual funds bearing high risk and high returns but needs less research, people who have low financial knowledge prefer to invest in mutual funds as they consider it less cumbersome, SIP is considered one of the best option involving least research, housing loan fulfills dream of a house and gives taxation benefits simultaneously without much research and numerical competency, thus numerical and research skills of a person affects their financial decisions remarkably.

FC6: Emotional Inclination

This is the sixth most important factor explaining 55.257% of the total variance is 2.717. The scale reliability for this factor is 0.5. The factors covered here are: fact that insurance should be taken by the bread winner of family as life insurance cover gives financial and moral support to entire family in case of death. Some prefer to invest in gold owing to tradition and culture, also sometimes driven by emotions. Thus, financial literacy is greatly affected by emotional inclinations to protect oneself against various uncertainties which are attached to an individual.

FC7: Goal Oriented

This is the seventh most important factor explaining 57.865% of the total variance is 1.043. The scale reliability for this factor is 0.5 and loadings range from 0.646 to 0.230. The factors covered here are: loan facility against life insurance policies, loan facility on Fixed Deposits, EMI for vehicle loan should be one third of earnings on regular basis. Enhanced financial literacy levels of an individual can lead to better financial goal planning in life.

V. DISCUSSION AND CONCLUSION

The study found out that along Attitude, Knowledge, Budgeting habits, liquidity, self analytical skills, emotional inclination and goal orientation are major determinants emphasized by individual investors. This study will be very helpful to individual investors if they consider these seven factors into consideration. Financial literacy is low in India as it can be seen that the mean of all items ranges from 4.00 to 5.22 and which is far below from 7. So focus should be given on these factors so that financial literacy can be improved.

VI. RESEARCH IMPLICATIONS AND DIRECTIONS OF FUTURE RESEARCH

India is one of the emerging economies in the world so financial literacy should be improved so that economy flourishes. Individual investors should give importance to these factors so that financial literacy increases. They should be given proper financial education so they may not suffer financial shocks and starts adopting changes. Improves financial literacy will lead to strong financial system. As we can see recently the transition which is done in legal tender money of India has created chaos but if people are properly financially literate they would adopt changes in relaxed way as it is good for the country. The chaotic situation in India is a result of poor financial literacy which has created fear in the minds of the people. So, enhancement of financial literacy should be on prior list of the economy for financial well being and sound financial decision making.

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