Financial Literacy: A Necessary Tool for Improving Financial Inclusion in India

Channaveerayya Hiremath
Phd Scholar
Central University of Karnataka
Department of Commerce
channuhiremath94@gmail.com

Shivakumar Deene
Assistant Professor
Central University of Karnataka
Department of Commerce

Abstract

Effective Financial Inclusion is pivotal for the inclusive development of the country and also it aids in alleviating extreme poverty and boosting shared prosperity. There are both demand-driven and supply-driven requirements for the effective implementation of financial inclusion. Financial inclusion is primarily a supply-driven approach, and numerous initiatives have been adopted. Financial literacy is a demand-side strategy that helps the individual in entering the country's formal financial system. The study traces the relationship between financial literacy and financial inclusion in India. The research is based entirely on secondary data from a survey performed by the National Center for Financial Education in 2013 and 2019. It is a descriptive statistics-based study i.e., correlation analysis. The findings of the analysis are that financial inclusion and financial literacy are positively correlated. Financial literacy has a significant impact on financial inclusion.

Keywords: *Financial Inclusion, Inclusive Development, Demand-Driven, Supply-Driven, Financial Literacy.*

Theoretical Background

Effective financial inclusion is pivotal for the inclusive development of the country. It aids in the preparedness to attain Sustainable Development Goals (SDGs). Seven of the 17 Sustainable Development Goals have been identified as being achievable by financial inclusion, it is worth noting that financial inclusion helps in alleviating extreme poverty and boosting shared prosperity (World Bank, 2020). The Global Findex Report (2017) has stated that 80 percent of Indians are having a bank account. But for effective implementation of the financial inclusion goals require both demand-driven and supply-driven approaches. Merely opening a bank account does not satisfy the main goals of financial inclusion. As stated by the world bank databases (2017) around 48 percent of bank accounts are currently inactive in India. India holds the first position with the highest number of inactive accounts in the world. 84 percent of accounts have done only a single transaction in the previous two years (Ministry of Finance, India). Despite several measures, only about 40 per cent of India's small and marginal farmers have access to formal finance (Reserve Bank of India,2019).

Since its independence, the Government of India has taken initiatives for the effective implication of financial inclusion among people i.e., the nationalization of Life Insurance Companies in 1956, the

Nationalization of Banks in 1969 and 1980, the establishment of Regional Rural Banks in 1975, and National bank for Agriculture and Rural Development (NABARD) 1982, and Mandatory Priority Sector Lending, the introduction of No-frills account, connecting the Self-Help Group (SHG) to the banks, Introduction of Lead Bank Scheme and Banking Correspondents (BC). In 2015 The Government of India introduced the world’s largest financial inclusion program i.e., Pradhan Mantri Jan Dhan Yojana[1] 2014 (PMJDY 2014), and the Government has given permission for the establishment of Payment Banks and Small Finance Banks 2015. (RBI 2019 and NSFI 2019). Traditionally, it is observed that new bank branches have been established in rural and remote areas. However, financial inclusion is considered as more than just opening bank branches in underprivileged areas and providing formal financial services across the country (Kale & Chobe, 2016).

Effective Financial inclusion has a leading role in the overall development of the country. It is inversely linked to the household's risk of being poor, and the future possibility of poverty in the future (Koomson et al., 2020). Financial inclusion is positively related to people’s income earning potential (The Global Findex Database 2017). There are three main components of financial inclusion i.e., Access, Usage, and Quality (GPFI, 2013). Access means that people can easily access financial products and services. The main focus of all financial inclusion programs is the component of accessibility. The other two components i.e., usage and Quality, are given less importance in the Indian context. Due to the lack of these three facilities nearly half of bank accounts in India are inactive or non-operational. People in India are also less aware of various financial products and services. So, there's an urgent need for financial literacy because it primarily focuses on the use and accessibility of financial products and services.

It is worth mentioning that there are two foremost initiatives toward financial inclusion i.e., Demand-driven and Supply-driven. The Government of India has initiated both Demand and Supply sided programs to attain the goals of Financial inclusion. The research related to financial inclusion is giving more focus on Supply-sided initiatives. These studies have major limitations because they have failed to incorporate demand-side initiatives (Mukhopadhyay, 2016). So, the main focus of our study is the supply-side initiative i.e., Financial Literacy.

Financial Literacy

“A combination of awareness, knowledge, skill, attitude, and behavior necessary to make sound financial decisions and ultimately achieve individual financial wellbeing” (Atkinson and Messy, 2012). Financial literacy has an effect on various factors such as poverty reduction, financial well-being, debt management, etc. Financial literacy is very pivotal in the present time because of the introduction of complex sophisticated financial products by financial institutions, most importantly, understanding mobile banking, internet banking, debit and credit card, mutual fund, stocks…etc. Financial literacy not only helps people to understand financial products it also helps in generating proper knowledge, awareness, and the right skill to use financial products securely. A study in Nigeria stated that financial literacy helps people in determining their saving patterns in formal and informal financial institutions (Adetunji & David-West, 2019). With the implementation of Liberalization, Privatization, and Globalization (LPG) in India in 1991, vast changes have taken place in the financial sector. The NDA Government of India has implemented ….. program to make the country cashless in….. The digitalization of the Banking sector requires knowledge of the people regarding the use of financial products and services (OECD, NFIE 2013),

According to a Standard and Poor survey (2017), more than 75 percent of Indian adults do not adequately understand basic financial concepts. Only 27 percent of people of India are financially literate (NCFE 2019).

[1] Pradhan Mantri Jan Dhan Yojana

72 percent of Indians are illiterate to save or invest their money in order to reach financial independence. (Scripbox, 2019). Real estate and other tangible assets account for 84 percent of the average Indian household's wealth (RBI, 2017). So financial literacy merely it's not just knowledge, it's a combination of Awareness, Knowledge, Skill, Attitude, and Behavior, (OECD 2013). It helps a person to get included in the financial system because financial literacy gives, knowledge about various products and services. Financial literacy creates awareness and also teaches a person proper skills to use it. So financial literacy is the backbone of achieving the goal of financial inclusion in the context of India (Khan et al., 2022a).

The linkage between Financial Literacy and Financial Inclusion

Financial literacy helps to understand the reasons for high transaction costs, uncertainty, asymmetric information, or a lack of physical access and thus helps in financial inclusion. (Grohmann et al., 2018). A study in the MSME (Full form) sector of Indonesia has shown that financial literacy has a direct impact on financial inclusion. (Bire et al., 2019). The findings of the study in Nigeria based on Survey data of over 2000 respondents stated that financial literacy has a considerable impact on savings patterns with both formal and informal financial institutions (Adetunji & David-West, 2019). Based on the data from the rural population in Bangladesh, it is observed that having a good understanding of various financial services factors has an important impact on getting financial access. The different national and international organizations also have considered financial literacy as an important component of financial inclusion (Hasan et al., 2021). Financial literacy aids in the implementation of financial inclusion by providing information on accessible basic financial services and enabling financial stability and self-sufficiency without requiring a large amount of public or private funds (Ozili, 2020). It has a strong influence on investment decisions.(Iram et al., 2021) and financially literate people participate more in the stock market and they are able to hold a diversified portfolio (Clark et al., 2017). Financial literacy has a substantial impact on saving patterns, investment decisions, and maintaining a well-diversified portfolio, as evidenced by the aforementioned research. It also assists people in learning about various financial institution offerings. As a result, financial literacy may be stated to assist people in participating in various financial services and gaining access to the financial system.

Objectives

In this paper, efforts are made to examine the relationship between financial literacy and financial inclusion in India. Two major survey data from the National Center for Financial Education are considered; as it is clear from the literature review that financial literacy aids people in financial inclusion, data from NCFE 2013 and 2019 are used to determine, whether is there any correlation between financial literacy and financial inclusion.

Methodology

The research is based entirely on secondary data from a survey performed by the National Center for Financial Education. There are two Survey Reports, one from 2013 and the other from 2019. Both years are considered in the study. The association between financial literacy and financial inclusion has primarily been tested through statistical correlation. For analysis, standard graphs and tables were used, as well as Microsoft Excel and IMB SPSS software for calculation reasons. Because the survey was done across India and the results were compared to macro-level data, the study area was expanded to include the entire country.

Results And Interpretation

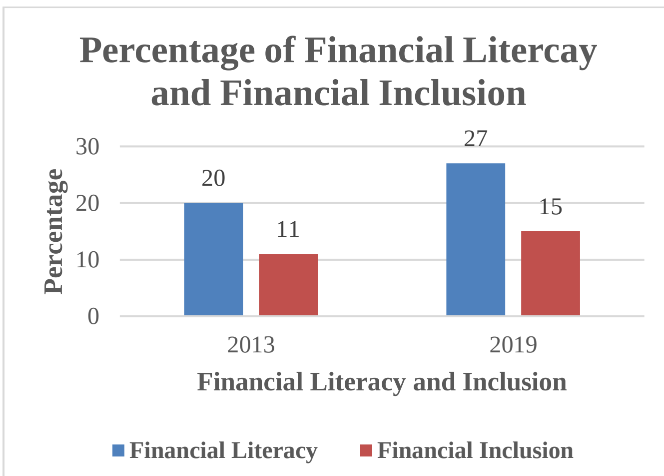
For the present study, the data is taken from the survey conducted by the national centre for financial education held in two years, 2013 and 2019. Mainly paper focused on verifying whether financial literacy is having a correlation and effect on financial inclusion in India. That In this study, three types of data have been considered to compare financial literacy and its effect on Financial Inclusion, 1) Overall Financial Literacy and Financial Inclusion in India in 2013 and 2019. 2) Age-Wise Financial Literacy and Financial Inclusion in India in 2013 and 2019. 3) Occupation Wise Financial Literacy and Financial Inclusion in India in 2013 and 2019. The correlation between these data has been checked through the SPSS software and the results are interpreted.

A. **Overall Financial Literacy and Financial Inclusion in India in 2013 and 2019**

Table 1: Representing Overall Financial Literacy and Financial Inclusion of India (Unit= Percentage)

Year	Financial literacy	Financial Inclusion
2013	20	11
2019	27	15

Source: National Centre for Financial Education 2013 and 2019



Source: National Centre for Financial Education 2013 and 2019

As evident from the above table, financial literacy and financial inclusion are significantly correlated i.e., as the financial literacy of people increases the financial inclusion also increases. In 2013, the Overall financial literacy of India was 20 percent and financial inclusion was 11 percent. Financial literacy increased to 27 percent in 2019, whereas, financial inclusion was also showing an increasing trend i.e., 15 percent. It indicates that the increased rate of financial literacy is 7 percent whereas 4 percent from 2013 to 2019. It is worth noting that the increased rate of financial inclusion compared to financial literacy is less. So, for effective financial inclusion in India, there should be an effective financial literacy program and policies. Financial Literacy helps in the demand-side strategy of financial inclusion. It is evident from the literature that financial literacy is the backbone of financial inclusion (Khan et al., 2022b). Especially financial literacy helps rural people to access financial services that lead to poverty reduction and boost prosperity in the century (Hasan et al., 2021). Financial literacy also has a significant relationship with financial behavior (Fernandes et al., 2014). One who receives financial literacy training is more likely to have a bank account, and more likely to save and get financial assistance (Koomson et al., 2020a). Financial literacy, race, and economic self-sufficiencies are significant predictors of economic empowerment (Postmus et al., 2013). And raising financial literacy helps in social inclusion and enhances the well-being of the community (Ramakrishnan, n.d,2011). It leads to the economic well-being of the people.

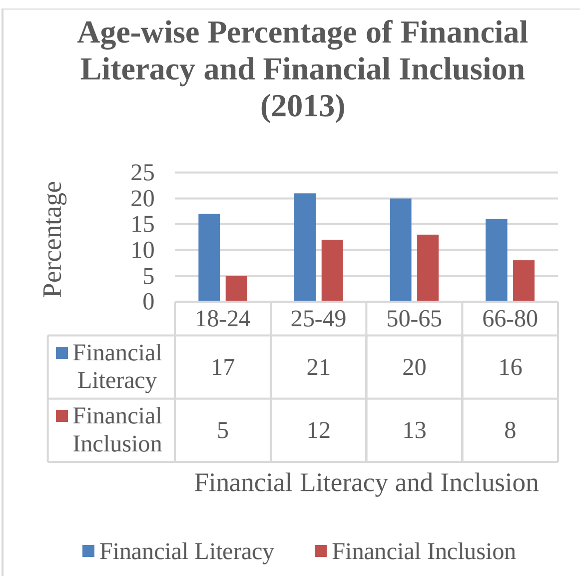
The findings of the study from the national center for financial education survey state that financial literacy helps people to get included in the financial system of the country and also indirectly helps to reduce poverty in the country and boosts the prosperity, and also helps in overcoming the problem of over-indebtedness (Kurowski, 2021).

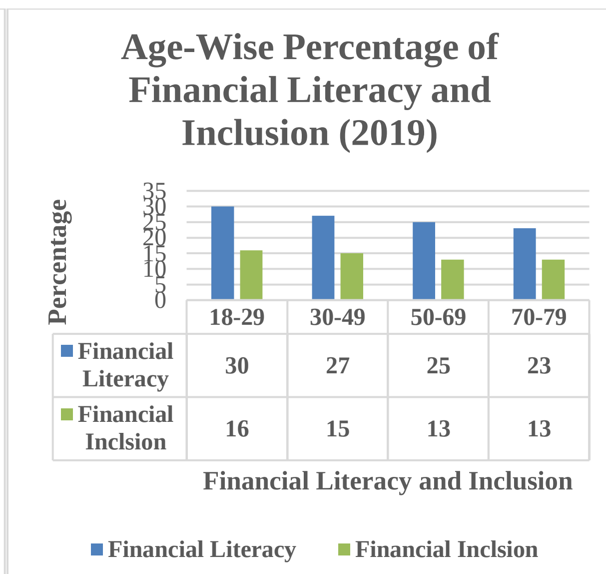
A. Age-Wise Financial Literacy and Financial Inclusion in India in 2013 and 2019

In this Section, financial literacy of various age groups and its effect on financial inclusion is measured based on correlation analysis. The below table and graphs explain the exact correlation between these two variables.

Table 2 and Graph 1: Age-Wise Financial Literacy and Financial Inclusion

2013 **2019**





Source: National Centre for Financial Education 2013 and 2019

2013 ***2019***

Correlations

		FL	FI
FL	Pearson Correlation	1	.833
	Sig. (2-tailed)		.167
	N	4	4
FI	Pearson Correlation	.833	1
	Sig. (2-tailed)	.167	
	N	4	4

Correlations

		FL	FI
FL	Pearson Correlation	1	.949
	Sig. (2-tailed)		.051
	N	4	4
FI	Pearson Correlation	.949	1
	Sig. (2-tailed)	.051	
	N	4	4

The above table and graph show the percentage of people who are financially literate and financially included by age. Although the age ranges for the two surveys were different, both tables show that financial literacy and financial inclusion are highly associated. In 2013, there was an 83.33 percent positive association between age-based financial literacy and financial inclusion, and in 2019, there was a 94.88 percent positive correlation. As shown in the table, from 2013 to 2019, there has been a steady improvement in financial literacy among individuals of various ages, and as a result, financial inclusion among people has increased in 2019. The lower the financial literacy, the lower the financial inclusion. It's also worth noting that the age group with the highest financial literacy has the highest financial inclusion. As a result, financial literacy and financial inclusion are highly connected with age.

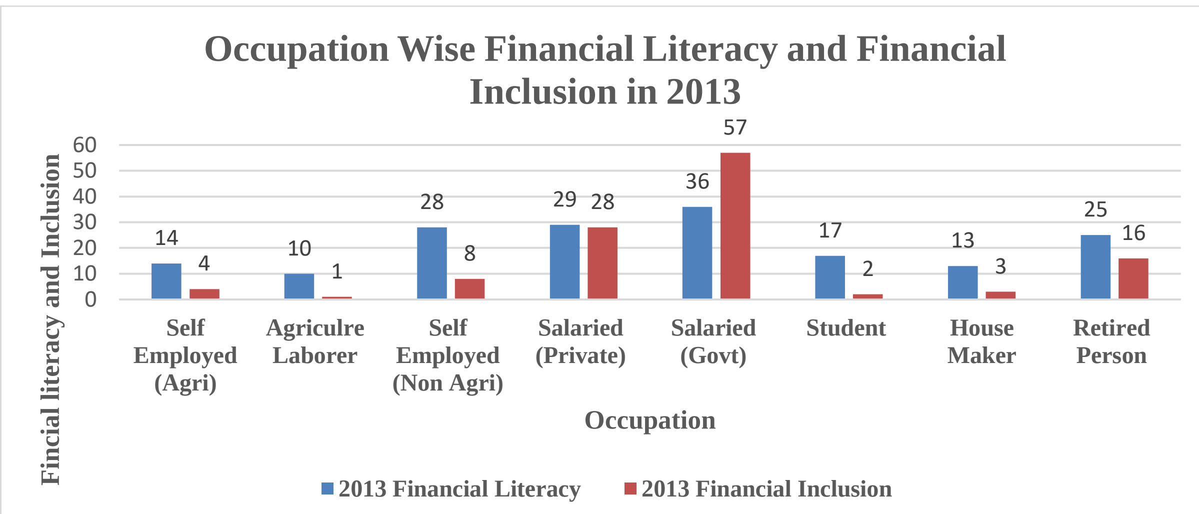
B. Occupation Wise Financial Literacy and Financial Inclusion in India in 2013 and 2019

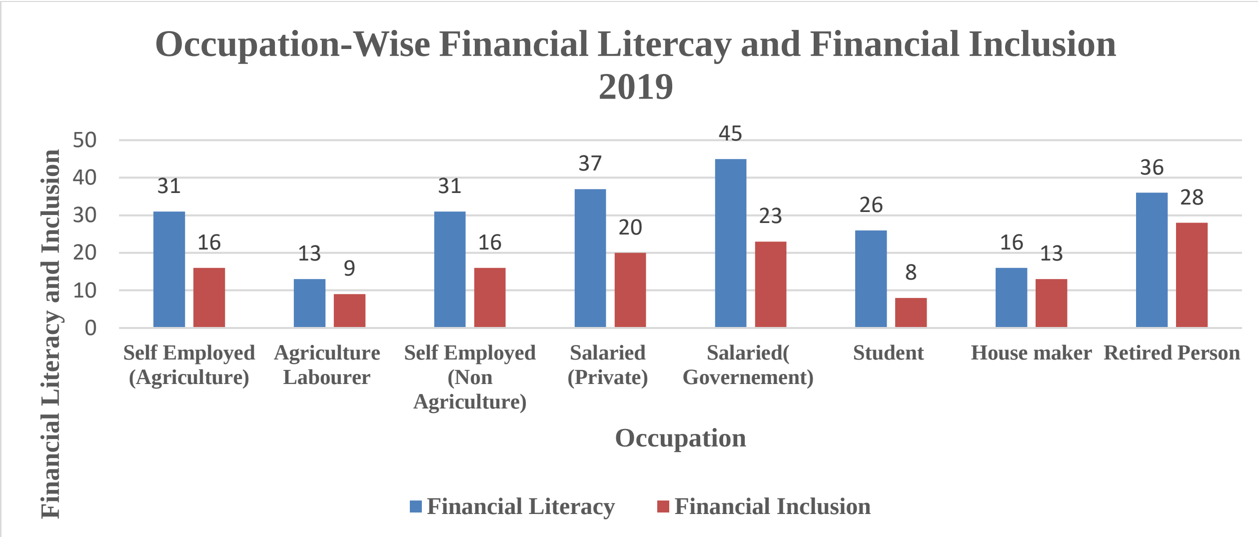
In this section, a comparison of occupation-based financial literacy and financial inclusion is made. Various occupations were considered, such as self-employed, agriculture labor, government employee, and private employee, and their level of financial literacy and financial inclusion were taken and the correlation between them was measured. Below are the facts and computations.

Table 3 and Graph 2: Occupation wise financial literacy and Financial Inclusion (Unit= Percentage)

Occupation	2013		2019	
	Financial Literacy	Financial Inclusion	Financial Literacy	Financial Inclusion
Self-Employed (Agri)	14	4	31	16
Agriculture Labourer	10	1	13	9
Self Employed (Non-Agri)	28	8	31	16
Salaried (Private)	29	28	37	20
Salaried (Govt)	**36**	**57**	**45**	**23**
Student	17	2	26	8
House Maker	13	3	16	13
Retired Person	**25**	**16**	**36**	**28**

Source: National Centre for Financial Education (2013 and 2019)





Source: National Centre for Financial Education

2013

Correlations

		FL	FI
FL	Pearson Correlation	1	.852**
	Sig. (2-tailed)		.007
	N	8	8
FI	Pearson Correlation	.852**	1
	Sig. (2-tailed)	.007	
	N	8	8

2019

Correlations

		FL	FI
FL	Pearson Correlation	1	.778*
	Sig. (2-tailed)		.023
	N	8	8
FI	Pearson Correlation	.778*	1
	Sig. (2-tailed)	.023	
	N	8	8

In this table, various occupations are listed along with their financial literacy and financial inclusion percentages. There is a positive correlation between financial literacy and financial inclusion in this analysis as well; in 2019, there is a 77 per cent positive correlation between occupation-based financial literacy and financial inclusion, and in 2013, there is an 85 percent positive correlation. Government personnel has the highest financial literacy and financial inclusion in both years, followed by private employees. One clear observation is that salaried people have more financial literacy and financial inclusion, whereas agricultural labor has the least financial literacy and thus the least financial inclusion in that category. Another observation is that retired people, despite having less financial literacy than other professions, have more financial inclusion in 2019. This is due to various policy schemes that were introduced to them like a pension plan, retirement plan, investment plan…etc. but when it comes to the

ISBN: 978-93-83302-57-4

working class, we can say that occupation-wise financial literacy is making an influence on the financial inclusion rate.

Conclusion

After analyzing the impact of financial literacy on financial inclusion, it's worth noting that the two are strongly correlated. For effective analysis, this study traces three variables: overall financial literacy and financial inclusion, age-based financial literacy, and financial inclusion, and finally occupation-based financial literacy and financial inclusion. Financial literacy is positively correlated to the financial inclusion rates in India in all three categories i.e., in 2019, there is a 94.88 percent correlation between age and financial literacy, and a 77 percent correlation between occupation and financial literacy in India. Other findings of the study include the fact that former agricultural laborers and self-employed people have lower financial literacy, and thus have a lower financial inclusion rate. So, efforts have been needed to improve the level of financial literacy among laborers and farmers, and self-employed people to increase the financial inclusion rate. According to the World Bank's development indicators collection 2020, 41.49 percent of the population accounts for agriculture employment. So it's very pivotal to enhance their financial literacy among them as it helps people to get into the financial system. The Reserve bank of India and other government regulators are putting efforts to increase financial literacy among the Indian population but still, there is more strategic initiatives are required to enhance people's financial literacy, most importantly for the rural population as nearly half of the population lives in rural India.

References

Adetunji, O. M., & David-West, O. (2019). The Relative Impact of Income and Financial Literacy on Financial Inclusion in Nigeria. Journal of International Development, 31(4), 312–335. https://doi.org/10.1002/jid.3407

Bire, A. R., Sauw, H. M., & Maria, -. (2019). The effect of financial literacy towards financial inclusion through financial training. International Journal of Social Sciences and Humanities, 3(1), 186–192. https://doi.org/10.29332/ijssh.v3n1.280

Clark, R., Lusardi, A., & Mitchell, O. S. (2017). Financial knowledge and 401(k) investment performance: A case study. Journal of Pension Economics and Finance, 16(3), 324–347. https://doi.org/10.1017/S1474747215000384

Fernandes, D., Lynch, J. G., & Netemeyer, R. G. (2014). Financial literacy, financial education, and downstream financial behaviors. Management Science, 60(8), 1861–1883. https://doi.org/10.1287/mnsc.2013.1849

Grohmann, A., Klühs, T., & Menkhoff, L. (2018). Does financial literacy improve financial inclusion? Cross country evidence. World Development, 111, 84–96. https://doi.org/10.1016/j.worlddev.2018.06.020

Hasan, M., Le, T., & Hoque, A. (2021). How does financial literacy impact on inclusive finance? Financial Innovation, 7(1). https://doi.org/10.1186/s40854-021-00259-9

Iram, T., Bilal, A. R., & Latif, S. (2021). Is Awareness That Powerful? Women's Financial Literacy Support to Prospects Behaviour in Prudent Decision-making. Global Business Review. https://doi.org/10.1177/0972150921996185

Kale, B. S., & Chobe, C. N. (2016). 18 | PARIPEX-INDIAN JOURNAL OF RESEARCH v Financial Inclusion in India-A Look. http://www.affairscloud.com/what-is-financial-inclusion-importance-in-india/

Khan, F., Siddiqui, M. A., & Imtiaz, S. (2022a). Role of financial literacy in achieving financial inclusion: A review, synthesis and research agenda. In Cogent Business and Management (Vol. 9, Issue 1). Cogent OA. https://doi.org/10.1080/23311975.2022.2034236

Khan, F., Siddiqui, M. A., & Imtiaz, S. (2022b). Role of financial literacy in achieving financial inclusion: A review, synthesis and research agenda. In Cogent Business and Management (Vol. 9, Issue 1). Cogent OA. https://doi.org/10.1080/23311975.2022.2034236

Koomson, I., Villano, R. A., & Hadley, D. (2020a). Intensifying financial inclusion through the provision of financial literacy training: a gendered perspective. Applied Economics, 52(4), 375–387. https://doi.org/10.1080/00036846.2019.1645943

Koomson, I., Villano, R. A., & Hadley, D. (2020b). Effect of Financial Inclusion on Poverty and Vulnerability to Poverty: Evidence Using a Multidimensional Measure of Financial Inclusion. Social Indicators Research, 149(2), 613–639. https://doi.org/10.1007/s11205-019-02263-0

Kurowski, Ł. (2021). Household's overindebtedness during the covid-19 crisis: The role of debt and financial literacy. Risks, 9(4). https://doi.org/10.3390/risks9040062

Mukhopadhyay, J. P. (n.d.). Financial Inclusion in India A Demand-side Approach. https://about.jstor.org/terms

Postmus, J. L., Plummer, S. B., McMahon, S., & Zurlo, K. A. (2013). Financial Literacy: Building Economic Empowerment with Survivors of Violence. Journal of Family and Economic Issues, 34(3), 275–284. https://doi.org/10.1007/s10834-012-9330-3

Ramakrishnan, R. (n.d.). Swabhiman-Inclusive Growth and Beyond 2 nd & 3 rd June, Mumbai India (i) Title of submission: Financial Literacy-The Demand Side of Financial Inclusion.

The Global Findex Database 2017 Measuring Financial Inclusion and the Fintech Revolution. (2017)