International Journal of Social Ecology and Sustainable Development
Volume 13 • Issue 1

Financial Inclusion Through Financial Literacy:
Evidence, Policies, and Practices

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ABSTRACT

Financial literacy is a means to tackle the problem of financial exclusion. It is a combination of awareness, skills, knowledge, attitude, and behaviors necessary to make sound financial decisions and achieve financial wellbeing. The objective of this study is to analyze current policy, practices, and evidence on financial literacy. The study has been carried out on the basis of review of literature and secondary data collected from a range of sources. It is found that the Government of India, RBI, and other regulatory bodies are running financial literacy campaigns through diverse mediums. Financial literacy centers (FLCs) are contributing for enhancement of financial literacy. However, they need to be strengthened by enhancing resources. Inclusion of financial education in school and college curriculum has also been recommended. Scope of the study is limited to Ghaziabad district of Uttar Pradesh in India. The study might be valuable for policymakers in enhancing financial inclusion.

KEYWORDS

Commercial Banks, Financial Capability, Financial Education, Financial Inclusion, Financial Literacy, Financial Literacy and Credit Counseling, Ghaziabad, Policies

INTRODUCTION

Financial exclusion is a global problem; estimates show that around one-third of the world population does not have a formal bank account. According to World Bank data, although the number of people with a formal bank account has increased from 61 percent in 2014 to 67 percent in 2017, but more than 80 percent of the current increase is made up of such bank accounts which have been inactive for over the past year. In terms of active accounts, the portion of the banked raised from 52 percent to 53 percent(World Bank, 2018) where the term 'banked' means a person having a formal bank account. Assess to formal financial system is important as it provides significant financial services to households and business enterprise which include safe savings and range of risk/return trade-off services- it helps buildup of financial assets which can provide a cushion against unforeseen events; by way of credit and insurance it helps in absorption of shocks due to unanticipated circumstances; it reduces dependence on informal financial resources such as pawn shops, moneylenders or informal groups relating to savings and credit associations; it facilitates payment between different parties and makes them safer to a cash transaction. The formal financial system also mobilizes savings into formal system which benefits the whole economy.

Financial inclusion is a multi-dimensional concept, as it focuses on not just access to better and affordable financial products and services, but also better usage of those products and services

DOI: 10.4018/IJSESD.2022010102 *Corresponding Author

(Mani, 2018). Herein lies the challenge- better access and better products are of no worth without better usage. Increased availability does not automatically translate into effective use. Effective use is held back due to asymmetries of information between inexperienced-consumers and powerful-financial-institutions. The imbalance exists as the consumers feel uninformed to take decisions about sophisticated financial products and services. This imbalance often brings negative outcomes due to ignorant consumer decisions or institutional abuses.

Financial literacy is a means to tackle this imbalance and help consumers develop the skills to understand, compare and select the best products as per their requirement. It empowers the consumers to protect their rights in case of conflicting situations. Organisation for Economic Co-operation and Development (OECD) highlighted several direct and indirect benefits of financial literacy for unbanked: improved understanding of formal financial products and services; better understanding of risk and returns related to financial products; reduced cost of information and money transfer; high household savings into formal financial products and protection against unfair practices (OECD, 2005).

Financial literacy is defined as a combination of awareness, knowledge, skills, attitude and behaviours necessary to make sound financial decisions and ultimately achieve individual financial wellbeing (Atkinson & Messy, 2012). It is often confused with financial education albeit financial education is a tool to achieve financial literacy. Financial education is the process of creating knowledge, skills and attitude to become financially literate. Introduction to good money practices related to earnings, borrowing, spending, saving, and investing is the basic premise of financial education. Financial education might have different meaning to different people- in the already banked sections of society, financial education might mean knowledge of tax rules, insurance requirement and credit cards, while for unbanked sections it is more about basic concepts of safe saving, budgeting and wise borrowing. The aim of financial education is to achieve financial literacy which is the ability to make informed judgements and take effective actions regarding current and future use and management of money.

Financial literacy is not an absolute state but it is continuous process of learning and responding effectively to changing financial requirements as per age, family, income and economic conditions. Financial literacy targets behavioural changes towards more effective management of scarce financial resources. Its strength lies in its possibility to be relevant to anyone and everyone, from a poor person who juggles money due to irregular, insufficient income and unpredictable expenditures, to the saver who tries to compare different choices of financial products for his retirement savings. Though it is relevant for everyone, it is more relevant for emerging economies like India due to its strong relationship with financial inclusion. Financial inclusion through financial literacy plays a significant role in poverty alleviation and uplift of weaker sections of society. In India the levels of financial literacy are meagre. As per Standard & Poor's Global Financial Literacy Survey, the percentage of financially literate adults in India is less than 25 percent (Klapper, Lusardi, & Oudheusden, Financial Literacy Around the World: Insights from the Standard and Poor's ratings services global financial literacy survey, 2014). The government of India, recognizing the need for financial literacy has taken many initiatives for its enhancement.

In accordance with this, the objective of this study is to analyse current evidences on financial literacy and financial inclusion in Ghaziabad district of India. The study also highlights current policy and practices related to financial literacy. The scope of this study is limited to Ghaziabad district of India, as it is part of a funded research project being carried out in the said geographical area.

LITERATURE REVIEW

Financial Education, Financial Literacy and Financial Capability

Cohen and Nelson (2011) discussed three related terms- financial education, financial literacy and financial capability. These three terms are similar yet different as each one is a part of a whole puzzle

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