Title of the Paper – **Role of the financial Literacy in National Growth**

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Abstract –

Financial literacy refers to the understanding and proficiency in a range of skills that empower individuals to make informed decisions regarding their finances. It encompasses the ability to comprehend and utilize various financial tools and systems for managing personal finances effectively. This proficiency enables individuals to achieve financial independence by making sound financial choices based on their circumstances. This paper underscores the significance of financial literacy, which entails the ability to make informed decisions about money management. Financial literacy impacts individual consumers, the financial system, and the broader economy by shaping saving, borrowing, investing, and financial management behaviours. It influences wealth accumulation, income growth, and lifestyle choices. Moreover, financial literacy affects the operations and product offerings of financial institutions, as it guides investment decisions and resource allocation in the economy, impacting its growth rate and stability. Overall, the paper emphasizes the importance of financial literacy across various levels, with a focus on its role in the national growth.

Introduction

Financial Literacy –

a. **Definition / Meaning –**

   The OECD INFE has defined financial literacy as follows: 'A combination of awareness, knowledge, skill, attitude and behaviour necessary to make sound financial decisions and ultimately achieve individual financial wellbeing.' (https://www.oecd.org/finance/financial-education/49319977.pdf)

   Financial literacy, as defined by Noctor et al. (1992), empowers individuals to make informed decisions about money management, reducing susceptibility to financial misguidance (Beal and Delpachitra, 2003). Proficiency in financial principles like planning, interest, and debt management is crucial, as a lack of literacy can lead to poor financial choices and negative consequences. Understanding money management is fundamental for financial stability, aiding in savings, protection, and preparation for life events. In today's complex financial market, consumers must possess the skills to choose suitable options among a variety of products. Financial literacy is key to achieving both short-term and long-term financial goals, providing the tools to navigate the financial landscape effectively and make informed decisions.

b. Importance

Financial literacy knowledge is indispensable for individuals due to its role in facilitating sound financial decision-making and promoting financial well-being, as outlined earlier. Its significance extends beyond the individual level to the broader community and national economy. Financially literate individuals contribute to the economic advancement of their communities and, ultimately, their countries. The following points elaborate on the importance of financial literacy.

i. **Budgeting** –

Creating a budget ahead of time helps curb unnecessary spending and enables more effective management of essential expenses relative to income. This budgeting approach spans daily costs and larger purchases such as durable goods. Daily budgeting helps control impulsive spending, while planning for significant expenses enhances debt management by allocating savings beforehand.

ii. **Goal Setting & Follow-up** –

Financial literacy empowers individuals to turn dreams into financial goals by calculating costs and timeframes, planning savings or investments, minimizing reliance on debt, and monitoring and adjusting plans to meet investment targets.

iii. **Understanding of complexity** –

As societal norms and technology evolve, financial products and services undergo continuous change, resulting in increasing complexity. Traditional offerings are often enhanced with additional features, and digitalization further complicates access and usage. Navigating this dynamic financial landscape has become challenging. However, financial literacy serves as a lifeboat, guiding individuals safely through these complexities.

iv. **Better Selection of Choices** –

Globalization, ongoing digital advancements, and intense market competition drive the rapid expansion of financial products and services. Traditional offerings have evolved significantly, offering a multitude of variations and added value. This diversification has led to a plethora of choices for consumers, with customized financial products becoming increasingly prevalent. As a result, individuals with financial literacy can discern between different offerings and select the most suitable option based on their requirements.

v. **Increased Income** –
Financial stability and wealth accumulation create more income opportunities. Understanding the stock market enables calculated risk-taking and wealth multiplication, moving away from speculative gambling. Investing in productive assets can also generate secondary and tertiary income alongside the primary source.

vi. **Away from Frauds** –
Money naturally captures the interest of many individuals, and this attention can be exploited by fraudsters. They often promote Ponzi schemes with enticing promises of high returns, such as doubling investments quickly. Financial literacy equips people with the ability to discern return calculations and market realities, enabling them to avoid falling for such schemes.

vii. **Risk Management** –
Risk refers to the potential loss of valuable assets, particularly in financial investments and insurance. Personal risk involves various assets like stocks, mutual funds, real estate, or loans. Financial literacy plays a crucial role in managing these risks, educating individuals about essential financial planning for achieving their goals and effectively managing risks to safeguard future interests. It also helps individuals understand the relationship between risk and return.

viii. **Tax Management** –
Tax literacy, a component of financial literacy, pertains to understanding the intricacies and aspects of taxes, along with public awareness of tax-related matters. Effective tax management, achieved through tax planning, involves timely filing of tax returns, adherence to relevant tax regulations and related laws, and avoidance of interest and penalties. Enhanced tax literacy

significantly impacts tax morale, compliance, and consequently, government tax revenue (Cvrlje, 2015).

ix. **Financial Inclusion** –

Financial inclusion offers transparent access to financial services like transactions, savings, credit, and insurance, tailored to individuals and businesses' needs. Research by Paramasivan & Ganeshkumar (2013) stresses the importance of literacy in raising investment awareness, a crucial aspect of financial inclusion. Additionally, Joseph & Varghese (2014) emphasize the need for active utilization of essential financial services. Enhancing financial literacy is thus crucial for more effective financial inclusion.

x. **Retirement Planning** –

Structured retirement planning enables individuals to build sufficient funds for their post-retirement life. This fund supports maintaining their standard of living, covering medical expenses, and financing enjoyable activities like vacations. Individuals who are financially literate prioritize this aspect of financial planning. Research indicates that those with financial literacy tend to plan for retirement in advance (Rooij, Lusardi, Alessie, 2011; Lusardi & Mitchell, 2007).

xi. **Debt Management** –

In today's world, debt financing is easily accessible and attractive, especially with enticing marketing targeting younger consumers. Long-term loans for items like homes and vehicles come with appealing schemes. Research shows that consumers' borrowing habits vary with their financial literacy level (Sevim et al., 2012), with poor financial management being a leading cause of debt issues (Hafidzah et al., 2016). Financial literacy equips individuals with essential skills for managing their finances effectively.

xii. **Self-Reliant** –

Financial literacy empowers self-reliance through wealth accumulation, enabling financial independence. It facilitates saving for retirement and emergencies, fostering independence. Additionally, it equips individuals to make informed and wise financial decisions autonomously.

xiii. **Improved Quality of Life –**

Financial literacy goes beyond theoretical understanding to practical application when making decisions regarding investments, borrowing, and retirement planning (Huston, 2010). Sound financial decisions are essential for enhancing personal finance, as evidenced by the global financial crisis, which underscored the widespread lack of financial knowledge (Singh, 2014; Lusardi & Mitchell, 2014). Research strongly asserts that financial literacy contributes to financial well-being, ultimately enhancing quality of life.

xiv. **Development of Economy –**

Financially literate individuals make informed decisions about money, leading to increased savings at both individual and national levels. They are less susceptible to fraud and Ponzi schemes and their rational behavior positively affects stock market development. Adequate retirement planning eases pressure on government social security schemes. Effective debt management limits defaults, promoting growth of financial institutions. The broader impact of financial literacy on the economy is discussed further in the same chapter.

Literature Review

In their 1992 report commissioned by NatWest Bank, Noctor et al. discussed financial literacy as the capacity to make informed judgments and effective decisions about managing money.

Beal & Delpachitra (2003) surveyed students at Australian universities on financial literacy. While they performed well in basic concepts, applying financial knowledge proved challenging. The authors noted that students studying related subjects tended to fare better. They warned that a lack of financial skills among young students could negatively affect their future financial decisions, impacting not only their personal finances but also the economy as a whole.

Cvrlje (2015) observed that individuals who grasp basic taxation and public expenditure concepts are more capable of managing their finances and understanding potential fiscal policy implications. Conversely, those lacking such understanding and numeracy skills may face challenges such as debt accumulation or failure to fulfill tax obligations.

Paramasivan & Ganeshkumar (2013) found that financial literacy is crucial for increasing investment awareness and plays a vital role in financial inclusion. However, their research suggests that while literacy is important, it alone cannot guarantee high levels of financial inclusion. The availability of bank branches also significantly impacts financial inclusion.

Rooij, Lusardi, and Alessie (2011) found a strong link between financial literacy and household net worth. They suggest that financial literacy aids in wealth accumulation by encouraging stock market investment and proactive retirement planning. Overall, the study highlights the direct and indirect benefits of financial literacy on household wealth.

Objectives

- To understand financial literacy concept.
- To understand about various facets of financial literacy.
- To learn importance of financial literacy.
- To understand role of financial literacy in the national growth.

Analysis and Interpretation

Role of Financial Literacy in National Growth

Financial literacy not only enhances individuals' quality of life but also elevates the quality of financial markets. Educated consumers promote genuine competition and compel service providers to enhance efficiency. The COVID-19 pandemic underscored the importance of financial literacy, with well-informed individuals navigating the crisis more effectively. Financially literate investors diversified their investments and maintained higher rates of investment, while insurance options protected their wealth and minimized medical expenses. Additionally, efficient debt management reduced their liabilities. Overall, financial literacy improves financial services and fosters economic growth and development.

Global Recession and Melt Down affected financial literacy positively. According to the 2011 Teens &Money Survey (*The Charles Schwab 2011 Teens & Money survey was conducted by Koski Research, an independent research firm, on behalf of CharlesSchwab. The nationally-representative online survey polled 1,132 American teens between theages of*

16-18 from February 21 through March 14, 2011, to better understand their views, behavior and knowledge of spending, saving, borrowing, and earning money. The survey, which has a margin of error of plus or minus 2.97% at the 95 percent confidence level, was conducted using the Harris Interactive panel. Details of the survey are available at www.aboutschwab.com/press/research.), 9 out of 10 teens say they were "affected by the recession," and the importance of saving has had a lasting effect.

Just as dropping a rock into a lake creates expanding ripples, so does financial education. Informed consumers make better financial choices, enhancing their economic security and well-being. They're better positioned to secure employment and contribute to a skilled labor pool. Stable families are more engaged in their communities as homeowners and voters, and as involved parents, they support better educational outcomes for their children. This involvement contributes to vibrant communities, fostering economic development. Financial literacy isn't just vital for individual households; it's crucial for communities and societies as a whole. Recognizing this importance, the G8 nations' Finance Ministers' meeting in St. Petersburg in June 2006 underscored the significance of financial education. Informed consumers contribute to economic stability by making sound investments that inject funds into the economy. In emerging economies, financially literate consumers play a crucial role in ensuring the financial sector contributes effectively to real economic growth and poverty reduction. Financial literacy is equally important in more developed economies, helping consumers save enough for retirement while avoiding excessive debt that could lead to bankruptcy and foreclosure.

Impact of financial literacy on economy and national growth

1. Improved financial literacy may lead to more cautious management of household finances, potentially lowering the lending risks faced by banks and other credit providers.
2. Increased financial literacy may prompt consumers to make wiser choices when selecting investments and financial products, encouraging financial institutions to innovate in response to consumer demand, thus enhancing overall financial system efficiency.
3. A financially literate society is likely to exercise stronger market discipline on financial service providers by scrutinizing risks and being more aware of risk-return

trade-offs. This increased scrutiny should lead to more prudent risk management by financial institutions and higher standards of financial service delivery.

4. Well-informed investment decisions, driven by strong financial literacy, may lead to a more efficient allocation of resources over time, potentially reducing economic volatility and promoting financial stability in the long term.
5. Greater financial literacy among consumers improves market discipline on financial institutions, resulting in a more efficient financial system. This enables less stringent regulation and supervision, reducing compliance costs and regulatory distortions.
6. Financial literacy also impacts the efficiency of the financial system, which involves its effectiveness in allocating risk and resources (allocative efficiency), the economic costs of providing financial services (productive efficiency), and its capacity to innovate in response to consumer demand (dynamic efficiency) (Hunter, Orr, and White, 2005).
7. Insufficient financial literacy can lead to poor decision-making, where individuals may fail to understand risks, purchase inappropriate financial products, or overlook beneficial services. While financial advice is available, it may be costly or tied to specific providers.
8. John Tiner, CEO of the UK Financial Services Authority and Financial Capability Steering Group Chair, has stated: “If people know what they want, and how to get it, the market for financial services becomes less one-sided and a lot more efficient. Consumers will demand better, cheaper and more appropriate products and services” (Financial Services Authority 2004:1).
9. Financial literacy influences resource allocation in the economy. When investors are financially literate, they make more discerning investment decisions, considering risks and returns carefully. This leads to higher risk-adjusted returns on investments, potentially increasing long-term economic growth and reducing cyclical volatility.
10. The growth rate of the economy is influenced by various factors beyond financial literacy. Factors such as debt preferences, domestic savings, and the development of capital markets are influenced by demographics, lifestyle choices, and market constraints. Resource allocation is similarly influenced by numerous factors, with financial literacy being just one of them. Nevertheless, it can be convincingly argued that financial literacy does contribute to the long-term growth and stability of the economy.

Insights From the Standard & Poor’s Ratings Services Global Financial Literacy Survey

A worldwide survey was conducted to understand level of financial literacy among the adults across the globe. Nation wide results of the survey highlights the need of financial literacy for the sustainable national growth.

1. Countries having highest financial literacy are having the high rate of household savings too. (e.g. Sweden, Norway, Denmark etc.)
2. Countries with lowest financial literacy level are among the weak economies in the world (Yemen, Afghanistan, Somalia etc.)
3. 19 out of top 20 countries with highest financial literacy knowledge are developed countries.
4. Forbes list of 20 happiest countries in the world features 18 of the highest financially literate countries.
5. Top 10 countries with highest GDP (per capita) are among the top 22 countries of highest financial literacy level. However, only 3 among top 10 countries with highest financial literacy rate could feature in 10 largest economies in the world (by largest GDP)

Conclusion

This paper contends that financial literacy holds significance across various domains. It is crucial in empowering individuals to handle their financial matters and can significantly enhance the stability and effectiveness of the financial system, as well as the overall economic performance.

A lack of public financial knowledge may result in individuals making inappropriate risk-return decisions without fully understanding the risks involved in their everyday financial choices.

Enhanced financial literacy can empower individuals and families, providing them with greater control over their finances and enabling them to make more informed decisions. Strong financial literacy skills will enhance individuals' ability to comprehend and manage financial risks, as well as capitalize on the expanded competition and choices within the finance sector of the economy.

Financial literacy should be integrated into society's mindset, similar to the customary practice of removing shoes before entering places of worship. It serves the broader interests of the nation, and fostering a financially robust country is a joint responsibility involving the government, private sector, and community-based organizations. This endeavor is too vast for any single stakeholder group to tackle alone.

The primary objective is not to cultivate financial experts but rather to empower individuals with adequate knowledge to comprehend financial activities, seek relevant information, feel comfortable asking pertinent questions, and skillfully interpret acquired information.

In today's intricate and ever-evolving economy, having financial literacy is essential for everyone. It enables individuals to make wise choices, prepare for the future, and play a role in their country's progress. The advantages of financial literacy go beyond personal welfare, influencing society by encouraging economic engagement, alleviating poverty, and supporting upward mobility. To ensure India's prosperity and resilience, it's vital to prioritize financial education efforts and provide citizens with the tools needed to manage finances adeptly.

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