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Financial Literacy: Role in Economic Empowerment

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Financial literacy refers to an individual's ability to make informed financial decisions by understanding relevant information regarding income, expenses, savings, investments, debt, insurance, retirement planning, and financial risk. In the modern economy, financial literacy is no longer merely a matter of personal financial management; it has become a crucial component of financial inclusion, social welfare, and economic development. In India, the usage of financial services has increased significantly due to the expansion of banking facilities, the Pradhan Mantri Jan Dhan Yojana, digital payments, UPI, online banking, and various government financial schemes. However, the availability of financial services and the ability to use them effectively are two distinct matters.

Keywords: Financial literacy, financial inclusion, savings, investment, digital payment, financial education, India

Introduction

In today's changing economic environment, every individual faces numerous financial challenges, such as effective income planning, expense control, savings, investment, debt management, insurance, and retirement planning. A wide range of bank accounts, loans, insurance products, mutual funds, shares, pension schemes, and digital financial services are available in the market. Financial knowledge and decision-making capabilities are essential to utilize these facilities effectively.

Financial literacy entails understanding financial concepts and applying that knowledge to actual financial decisions. Within the OECD/INFE framework, financial literacy is considered in terms of financial knowledge, financial attitudes, and financial behavior. The RBI's financial literacy survey also takes into account concepts such as the time value of money, interest, compound interest, inflation, risk and return, and diversification.

India has made significant progress towards financial inclusion. According to the World Bank's Global Findex 2021, 78 percent of adults in India held a financial account; this figure stood at 35 percent in 2011. However, it was also observed that approximately 35 percent of accounts in India were inactive in 2021. Therefore, while opening an account marks the first stage of financial inclusion, ensuring its proper and active usage remains the next critical challenge. A lack of financial literacy can lead individuals to take on unsuitable loans, incur unnecessary expenses, save inadequately, or lose money in high-risk investments due to a lack of knowledge. India's National Strategy for Financial Education highlights the need for specialized financial education for rural citizens, women, low-income groups, senior citizens, and individuals with limited educational qualifications. Consequently, the study of financial literacy should not be confined merely to an individual's financial status; it is essential to examine its relationship with financial inclusion, digital financial services, and socio-economic development.

Research Objectives

The primary objectives of this research are as follows:

1. To explain the concept and importance of financial literacy.
2. To examine the relationship between financial literacy and financial inclusion.
3. To study the opportunities and challenges for financial literacy arising from digital financial services.
4. To suggest measures for enhancing financial literacy.

Concept of Financial Literacy

“Financial literacy refers to the ability to understand how to earn, manage, save, and wisely invest money.”

“financial literacy is the capacity to comprehend financial knowledge, financial attitudes, and financial behavior.”

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An RBI survey assessed financial literacy by considering all three components: knowledge, attitude, and behavior.

Status of Financial Inclusion in India

According to the World Bank's Global Findex 2021, there has been a significant increase in the availability of financial accounts in India over the past decade. The proportion of account holders among the adult population rose from 35% in 2011 to 78% in 2021. A significant increase in access to financial accounts has been observed in India between 2011 and 2021. World Bank analysis indicates that financial inclusion initiatives, such as the Pradhan Mantri Jan Dhan Yojana launched after 2014, played a crucial role in this growth.

Digital Financial Transactions and Financial Literacy

Digital technology has brought about major changes in financial transactions in India. According to the World Bank's Global Findex 2021 report, 35 percent of adults in India made digital payments using their accounts in 2021.

In developing economies, this figure stood at 57 percent. In India, a 13-percentage-point gap was observed in digital payment usage between men and women. Digital payment usage was also lower in rural areas compared to urban areas. As digital transactions increase, knowledge of digital literacy and cyber security has become essential alongside financial literacy. Consumers need to be aware of how to protect themselves against risks such as OTPs, PINs, passwords, fake links, phishing, fraudulent investment schemes, and online scams.

Financial Literacy and Savings

Saving is the fundamental step towards financial stability. Regular saving provides the financial support needed to meet future requirements, such as emergency expenses, medical costs, education, home construction, or retirement. A financially literate person strives to maintain a balance between income and expenditure. Habits such as creating a monthly budget, distinguishing between essential and non-essential expenses, and regularly saving a portion of one's income contribute to greater financial stability.

Financial Literacy and Investment

Understanding the relationship between returns and risk is crucial in investment. Investing in a scheme solely in the hope of high returns can be risky. Financial literacy enables individuals to evaluate various investment options based on risk, tenure, liquidity, and expected returns. Diversification—the principle of not putting all one's money in a single place—is fundamental. Financial literacy also allows individuals to appropriately distinguish between saving and investing based on their financial goals.

Women and Financial Literacy

Increasing women's participation in financial decision-making is vital for their economic empowerment. According to the World Bank's Global Findex 2021, the gender gap in financial account ownership in India had nearly vanished; however,

women's participation in digital payments remained lower than that of men. Therefore, beyond merely providing bank accounts, it is essential to offer women hands-on training regarding digital transactions, savings, insurance, loans, investments, and government financial schemes.

Financial Literacy in Rural Areas

Financial literacy faces specific challenges in rural India. Factors such as low income, limited access to financial institutions, restricted use of digital tools, lack of information, and reliance on informal financial transactions underscore the heightened need for financial education. The National Strategy for Financial Education (NSFE) by the NCFE highlights the need to focus specifically on rural India and emphasizes the requirement for greater financial education for individuals with lower levels of education and those over the age of 50.

Various initiatives are implemented by institutions such as RBI, SEBI, IRDAI, PFRDA, and NCFE to enhance financial literacy in India. NCFE is a Section 8 not-for-profit organization established through the joint initiative of RBI, SEBI, IRDAI, and PFRDA. The National Strategy for Financial Education 2020-25 outlines a '5 C' approach:

- Content – Appropriate financial education material.
- Capacity – Enhancing the capacity of financial educators.
- Community – Financial education through community engagement.
- Communication – Effective communication and public awareness.
- Collaboration – Cooperation among various institutions.

4. Key Challenges Facing Financial Literacy

Financial literacy should not be viewed merely as a training program within the financial sector; instead, it needs to be integrated with school education, higher education, skill development, women's empowerment, rural development, and digital inclusion. To take financial inclusion in India to the next level, the primary objective should shift from simply 'having an account' to the 'safe, active, and informed use of the account.' The key challenges facing financial literacy in India are outlined below.

Limited Reach of Financial Education in Rural and Remote Areas

This is a major challenge for financial inclusion in India. The spread of financial education in rural and remote areas is limited due to factors such as a lack of general literacy, geographical barriers, traditional mindsets, apprehension regarding digital technology, and a lack of information about various government insurance schemes, pension plans, and subsidies.

Rising Use of Digital Financial Services and Associated Cyber Risks

This is a crucial and pivotal issue in today's fast-paced digital era. Over the past few years, there has been a massive revolution in digital transactions, both in India and globally. UPI and mobile wallets

have made cashless transactions easily accessible. Services such as checking account balances, transferring funds, and opening fixed deposits (FDs) are now available 24/7 without the need to visit a bank branch. The use of digital payments has surged significantly for e-commerce, utility bill payments (electricity and water), mobile recharges, and ticket bookings.

However, alongside the growth of digital facilities, the incidence of financial fraud and cybercrimes has risen at an equally rapid pace. Cybercriminals are devising novel methods to defraud people, such as posing as bank officials or government employees to solicit confidential information through phishing (sending fake links) or vishing (making fraudulent calls). They lure customers into revealing sensitive details like bank passwords, UPI PINs, or One-Time Passwords (OTPs). They also steal data and money by creating fake websites that closely resemble legitimate banking sites or by launching unauthorized loan apps. Additionally, incidents where criminals hijack banking transactions by obtaining a duplicate of the customer's SIM card without their knowledge are also on the rise.

Gender Gap in Digital Financial Inclusion

The gender gap in digital financial inclusion is a major challenge in today's digital era. Despite the rapid spread of technology and digital banking, a significant disparity exists between men and women regarding the usage of these services. In many developing countries, fewer women own smartphones compared to men; furthermore, men often exercise greater control over access to internet data. Women frequently lack adequate education on how to use smartphones, conduct digital transactions, and ensure online security. In some societies, women lack the freedom to make financial decisions, with household financial matters handled exclusively by men. They often do not possess the necessary documentation—such as Aadhaar cards, PAN cards, or personal SIM cards—required to open bank accounts or use digital wallets. Additionally, fears regarding cyber fraud, online misconduct, and privacy breaches often deter women from engaging in digital transactions.

Increasing Complexity of Financial Products

The increasing complexity of financial products is a critical issue in the modern economy. Rapidly evolving technology and diverse consumer needs have led to immense complexity within the financial sector. Banks and financial institutions have moved beyond traditional deposits and loans to introduce innovative products such as derivatives, mutual funds, and structured products. Developments like digital banking, algorithmic trading, cryptocurrency, and block chain technology have rendered financial transactions and products increasingly technical and complex. Moreover, the interconnection of global markets means that international events directly influence local financial products.

Dissemination of Incorrect or Misleading Financial Information

The spread of incorrect or misleading financial information is a serious offense and a financial risk in modern times. Such information spreads rapidly via social media, digital platforms, and messaging apps, causing significant losses to ordinary investors. Examples include spreading fake news or rumors on social media to inflate the share prices of weak or fraudulent companies. When the general public buys these shares and the price rises, the perpetrators sell their holdings for a profit, leaving ordinary investors stranded. Schemes promising to "double your money in a month" or offering "100% guaranteed returns" are also promoted. So-called 'experts' who lack authorization from SEBI or other government bodies—advise people to purchase specific stocks or crypto currencies.

Trust in Financial Institutions and Consumer Protection

Trust in financial institutions and consumer protection form the backbone of any country's economic system. If consumers lack confidence in banks, insurance companies, and other financial institutions, economic stability can be jeopardized. Failures or scams involving banks and Non-Banking Financial Companies (NBFCs) erode public trust in the system. Hidden charges are frequently levied on loans or investment schemes. Consumers are often misled because terms and conditions are drafted in complex language. The failure to safeguard personal and financial data—and the subsequent sale of such data to other companies—is a major cause for concern.

Financial Education and Actual Financial Behavior

A significant gap is often observed between financial education and actual financial behavior. Knowing how to manage money (education) and how one actually handles it (behavior) are two distinct matters. In economics, this disparity is referred to as the 'Knowledge-Action Gap' or 'Behavioral Bias.' Often, even when people understand the financial implications, they make decisions driven by fear, greed, or the desire for instant gratification when actually purchasing or investing. Expensive items are bought—often at the cost of financial loss—simply to display social status or to emulate others. Despite knowing the importance of creating a budget, paying insurance premiums, or planning for retirement, people often procrastinate on taking actual action. The multitude of market options (such as shares, mutual funds, and various insurance schemes) leads to confusion, causing people to make poor decisions or take no action at all. Credit cards and digital wallets have made spending money extremely easy, which often disrupts budgetary planning.

Measures to Enhance Financial Literacy

The following measures can be effective in enhancing financial literacy:

- Making basic financial education mandatory in school and college curricula.
- Expanding financial education programs in local languages within rural areas.

- Providing financial training through women's self-help groups.
- Imparting training on cybersecurity alongside digital payment education.
- Making information regarding banking, insurance, loans, and investments available in simple, accessible language.
- Implementing dedicated financial education programs for farmers, laborers, the self-employed, and small-scale entrepreneurs.
- Raising public awareness regarding protection against financial fraud.
- Regularly evaluating the impact of financial literacy programs.
- Fostering collaboration among local NGOs, banks, educational institutions, and government departments.

Conclusion

Financial literacy is crucial for an individual's financial security and the country's economic development. India has made significant strides in financial inclusion. According to the World Bank's Global Findex 2021, 78 percent of adults in India held a financial account, compared to 35 percent in 2011. However, it was also observed that 35 percent of these accounts remained inactive. This highlights the distinction between merely providing financial facilities and ensuring their proper and regular usage. Financial literacy enables individuals to make informed decisions regarding income planning, expense control, savings, investments, debt management, and risk mitigation. With the expansion of the digital economy, the importance of digital and cyber literacy has grown alongside financial literacy.

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Conflicts of interest

The authors declare that there are no conflicts of interest regarding the publication of this paper.

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