THE ROLE OF FINANCIAL LITERACY IN THE DIVERSIFYING OF HOUSEHOLD SAVINGS INTO FINANCIAL ASSETS AND PHYSICAL ASSETS IN INDIA: AN ASSESSMENT OF LITERATURE

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Abstract

In India, household savings contributed major share to the total gross domestic savings over the period of time. Here, household savings majorly concentrated in the physical assets then the financial assets, lack of knowledge, awareness about the financial products, services and markets can mainly attributed to the low participation of the households in the formal financial markets. present paper largely concentrated on the relationship between financial literacy and diversification of the household savings into thefinancial savings and savings in physical assets. Secondary data of the financial literacy, household savings in India and exiting literature used for this present study.

Key words

Financial literacy, household savings, savings in physical assets, financial savings

1. Introduction

In any economy accurate investment in productive sectors is the key factor to determine economic growth, if there is no sufficient investment in the economy it will lead to low growth rate. Investment in the economy comes majorly from two sources; those are public and private investment; public investment is limited into the few sectors only due to the resource constrains, therefore, private investment is crucial for sustaining economic growth of the country.
Domestic investment is the result of the domestic savings which comes mainly from the household sector.

In any economy,there are two different kinds of households; deficit spending households and surplus spending households respectively.Deficit spending households need funds fortheir consumption expenditure as well as investment expenditure whereas surplus spending households provide funds through their savings, so, here, households act as suppliers of the funds as well as demander of the funds, but there is a need for intermediation between deficit and surplus spending households. The well-developed financial system can facilitate intermediation through financial institutions, financial markets and financial products.

Here, savers can save their funds into physical assets like gold, land, buildings, etc., as well as financial assets like saving deposits, fixed deposits, stocks, bonds, debentures, mutual funds etc..., if savers choose the physical assets for their savings it will not be so useful for the countries investment needs, at the same time savings in financial assets can be converted into the investment in the productive sectors which will result in the country's economic growth.
In India, over a period of time household savings contributed a major share in the total gross domestic savings. In these household savings, financial savings proved to be less preferred over the savings in physical assets.

Thus, there are two main factors that determine savers to prefer savings in physical assets over the financial assets, which are, expected returns and risk associated with their savings and financial literacy respectively.

Present paper largely concentrates on financial literacy and its impact on demand for financial assets, in general, financial literacy can be defined as the understanding of the financial concepts which are basic in nature, financial principles, skills and ability to understand financial products so that one can make financial decisions.

According to the definition given by Organization for Economic Co-operations and development (OECD,2018), financial literacy is, "A combination of awareness, knowledge, skill, attitude and behaviour necessary to make sound financial decisions and ultimately achieve individual financial well-being".

According to Reddy (2006) financial literacy is, "Providing familiarity with and understanding of financial market products, especially rewards and risks, in order to make informed choices." Viewed from this standpoint, financial education primarily relates to personal finance to enable individuals to take effective action to improve overall well-being and avoid distress in matters that are financial.

2. Importance of financial literacy

- In the complex financial system making and managing money is one of the important tasks for each and every individual, financial literacy provides the knowledge of understanding and managing money in a better way. financial literacy makes every household to recognize the importance of the preparing household budget for utilize money optimally and make financial planning for future such as retirement plan.
- Financial literacy leads to positive financial behavior such as timely payment of bills and loan installments, saving before spending, using credit card judiciously, lesser number of litigations etc.
- Financial literate household can understand the financial products, financial services and financial markets, so that, they can channelize their savings into the better options by way of diversifying their investments into various portfolios as result they will get optimum returns with the low risk.
- Financial literates are able to assess the financial risks and financial options, it will make them to take actions for the financial well-being.
- Financial literacy not only useful for individual's financial well-being but also nations financial development, it provides link between households and formal financial system as a result savings in financial assets increases, which can be utilizing for productive purposes.
- The increasing complexity of our financial system makes it clear that strengthening the financial knowledge and skills of the people is critical for the future success and financial stability of our country.

3. Relationship between Financial behaviour and Financial literacy

Financial literacy will help households to understand the complex financial system, so that, they will know how money is made, spent and saved as well as how it can be used to make financial decisions. When households have knowledge about the different alternatives for their savings and investments, they can diversify it in a better way. Extensive literature is also available to support this argument.

There is a positive correlation between financial literacy and retirement planning, savings and wealth accumulation. (Ameriks et al. 2003). Financial literacy is considered to be a prognostic of individuals investment behaviour and outcomes, which also includes stock market participation. (Rooij, et al., 2011, Kimball, et al., 2006).

Households with low level of financial literacy participate less in the formal financial system relative to their more financially literate counterparts (Rooji, et al. 2007, Hogarth et al. 1999). Low financial literacy households acquire fewer assets (Lusardi, et al. 2007).

With the help of the above references it can be concluded that, there is a positive correlation between financial literacy and financial wellbeing of the households. Financial literate households prefer financial assets over the physical assets which means that it will be a good sign forindividuals' financial well-being as well as the nation's well-being. Financial literacy will make the households to understand and assess alternative financial productsthus, it will lead to developing a formal financial system.

4. Level of financial literacy in India

Most surveys show that financial literacy is still poor in India. Over two-thirds of the population is not financially literate, i.e., people lack financial planning basics. The Standard & Poor survey (2014) found that over 76 percent of adults in India did not comprehend financial planning basics.

National Centre for Financial Education carried out baseline survey in India that is, NCFE-Financial Literacy and Inclusion Survey (NCFE-FLIS, 2015) for assessing the state of financial literacy and financial inclusion. The survey report clearly shows that financial literacy is very poor in the country.

Table 1: Status of Indian Financial Literacy

	Percentage of Financial Literacy
India	20
Location-Wise	
Rural	15
Urban	25
Gender-Wise	
Male	23
Female	16
Age-Wise	
18-24	16
25-49	20
50-65	18
66-80	15
Education-Wise	
Illiterate	4
Primary (Up to class V)	11
Upper Primary (class vi-viii)	13
Secondary (class IX-X)	19
Senior Secondary (class XI-XII)	21
Diploma	29
Graduate & Above	35
Income-Wise (Per Annum)	
No Income	14
<10,000	12
INR 10,001-50,000	16
INR 50,001-200,000	27
INR 200,001-500,000	38
>500,001	47

Source: NCFE-Financial Literacy and Inclusion Survey (NCFE-FLIS 2015), India

Table 1. shows the percentages of financial literacy in India and financial literacy in different subgroups, only 20% of Indians are financially literatewhereas, relatively, the urban population (25%) are more financially

literate than the rural population (15%). Male population seems to be having higher financial literacy (23%) compared to the female population (16%). The above table shows that there is a positive correlation between education and financial literacy, the percentage of financial literacy in the illiterate subgroup is very low at 4%, along with level of education, financial literacy has also been increasing. We observe that the income level and financial literacy are also positively correlated.

5. Households savings in India

In India, historically household savings have been a major part in the total gross domestic savings which clearly indicates that household savings play a crucial role in the domestic capital formation, but on the other hand, the Reserve bank of India data revealed that major part of the households savings concentred more on the physical assets rather than the financial assets.

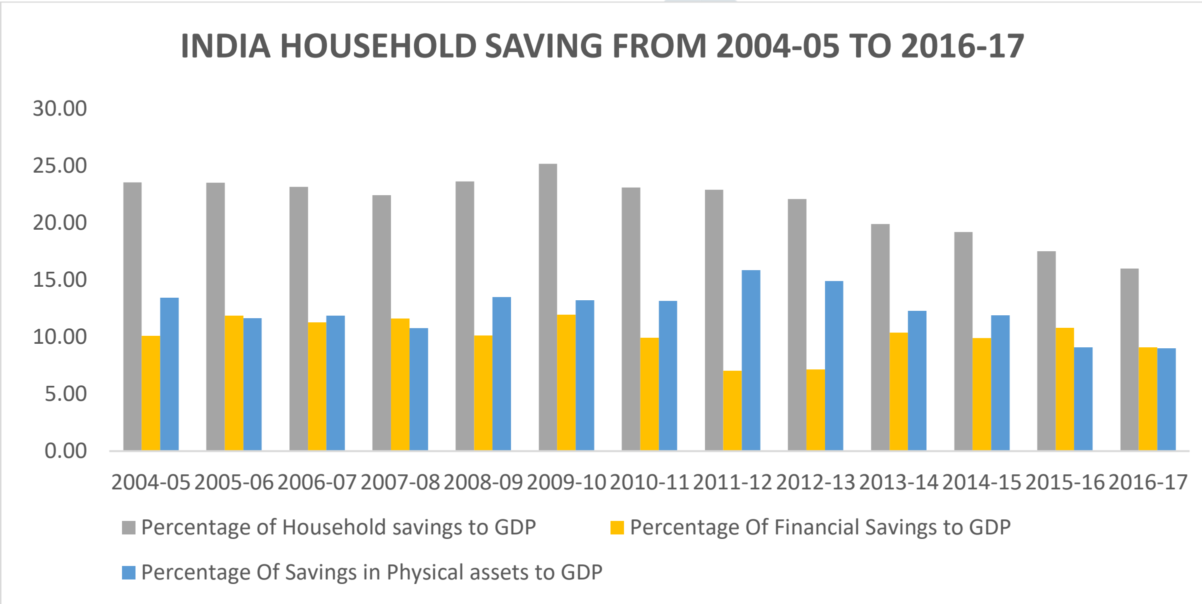

Fig 1: Trends in India Household savings from 2004-05 to 2016-17

Source: Reserve Bank of India Data and CSO Press Note on Quick Estimates of National Income, Consumption Expenditure and Savings, 2013-14 & Advance Estimates of National Income

In Fig. 1, we find that household savings to GDP ratio remained almost constant i.e., 22-23%from the years 2004-05 to2008-09 and slightly increased and stood at 25% in the year 2009-10 and again came down to 22-23% from 2010-11 to 2012-13. Household savings continuously decreased from 2013-14 to 2016-17. In the recent times, 2016-17 recorded lowest household savings percentage to the GDP which is 16%.

From 2004-05 to 2016-17 percentage of savings in physical assets dominated over the percentage of financial savings.

6. Relationship between Financial Literacy and Household savings in India

From Table 1 and Fig 1, we can visualize that in India, financial literacy and savings in financial assets are still very low, over the period of time, savings in physical assets are preferred over the financial savings. The reason for this can be attributed to the lack of financial literacy, which means that people could not understand the concepts related to financial assets which obviously leaded to concentration of savings in physical assets.

7. Suggestions

There is a need of a comprehensive plan to improve financial literacy in India, from primary schooling to post graduationlevel, it has to be included as a part of the curriculum. Apart from that, financial literacy projects must be implemented on a large scale resulting in greater practical knowledge.

In the village level, at lest one organisation has to be established per village which could function as the link between people of the village and the formal financial markets.Encouraging the use of digital platforms such as Android apps and Demat accountsare the best practical ways to improve financial literacy and it can connect people to the formal financial system.

Financial institutions have to take initiatives to improve financial literacy by way of implementing financial education in the concerned areas. Governments in the state level as well as central level need to establish separate institutions to provide financial education to people of all ages.

8. Conclusion

Underdeveloped formal financial system is the main characteristics of the Indian economy; low financial literacy has led to less familiarity of the financial services and financial products which shows that majority of the people are choosing physical assets as a saving option. Physical assets like gold, land and buildings have been the known saving options to the people of India, due to this India is still witnessing low levelsof domestic investment in the productive sectors, thus resulting in the dependence on FDIs and other overseas sources. Making India financially literate is very crucial for the country as well as the individuals well-being.

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