Thoughts of Rural Development through Developing Financial Skills

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Abstract

The issue of financial literacy is of greater concern in developed countries than the developing nations. Financial literacy gained far more importance after the financial distresses and become the pre-requisite with the objective to avoid financial crisis by attaining financial stability. In recent years, financial literacy has gained the attention of a wide range of major banking companies, government agencies, grass-roots consumer and community interest groups, and other organizations. Interested groups, including policymakers, are concerned that consumers residing in rural India lack a working knowledge of financial concepts and do not have the tools they need to make decisions most advantageous to their economic well-being. Such financial literacy deficiencies can affect an individual's or family's day-to-day money management and ability to save for long-term goals such as buying a home, seeking higher education, or financing retirement of rural people. Ineffective money management can also result in behaviours that make consumers vulnerable to severe financial crisis. This paper tries to explore all those major concepts and measures which can be extremely helpful in the developing not only the rural living of standard but also the mindset of common people. We can also see the extensive literature in this area which will be ultimately helpful for knowing the current phenomenon. Success in expansion of financial awareness as a part of financial literacy among individuals ensures the prevalence of financial well being and much required financial inclusion. Apex regulatory bodies in India are trying to achieve utmost level of financial inclusion. It cannot be attained without the basic requirement of Financial awareness and Literacy among common individuals.

Key Words: Financial Awareness, Financial Literacy, Rural Economic Development, Financial Inclusion, Demographic Factors.

Introduction

The financial crisis has highlighted the need for strengthened national and global financial regulation and supervision, including in the area of financial consumer protection. We should not forget that, at the epicentre of the crisis – the subprime mortgage sector in the United States – insufficient levels of financial literacy were among the major aggravating factors. If there is any consolation to be drawn from this debacle, it is that the importance and profile of financial education has been raised decisively around the world. In his Speech, Mr. Richard Boucher, OECD Deputy Secretary General, at the occasion of the RBI-OECD Workshop, stated, “Financial education could play an important role in enabling the most vulnerable segments of the population to use legitimate and well-governed financial services. The Organisation (OECD), therefore, concentrates its activities on the analysis and promotion of efficient programmes that are tailored to improve the financial skills and knowledge of the most vulnerable groups. Such programmes should promote their awareness of available financial services and enable them to make appropriate use and choice of these services.”

Financial Literacy enhances the ability to effectively monitoring of financial resources for
developing the economic security of a person. Financial stability of economy is based on these terms and currently it is necessary for developing and developed country. Currently most of countries are adopting various programmes for financial education. India is having large population, growing economy with national focus on inclusive growth and an urgent requirement to develop a vibrant and stable financial system. The Reserve bank of India, which is the central bank, has been actively participating in the field of eradicating financial literacy and maintains financial stability in the country. RBI has developed various strategies and adopted programmes to develop a smooth process of financial literacy. It is being just a start, it needs to be more popularized and implemented in the basic requirements of common individuals.

Thoughts of Financial Inclusion and Financial Literacy

In order to achieve the status of a developed economy, financial inclusion is one of the rudimentary requirements. It means that every individual should be provided with the financial services. Financial inclusion enables improved and better sustainable economic and social development of the country. It helps in the empowerment of the underprivileged, poor and women of the society with the mission of making them self-sufficient and well informed to take better financial decisions. Financial inclusion takes into account the participation of vulnerable groups such as weaker sections of the society and low income groups, based on the extent of their access to financial services such as savings and payment account, credit insurance, pensions etc. Also the objective of financial inclusion exercise is easy availability of financial services which allows maximum investment in business opportunities, education, save for retirement, insurance against risks, etc. by the rural individuals and firms.

According to the Planning Commission (2009), “Financial inclusion refers to universal access to a wide range of financial services at a reasonable cost. These include not only banking products but also other financial services such as insurance and equity products.” The household access to financial services includes access to contingency planning, credit and wealth creation. Access to contingency planning would help for future savings such as retirement savings, buffer savings and insurable contingencies and access to credit includes emergency loans, housing loans and consumption loans. On the other hand, access to wealth creation includes savings and investment based on household's level of financial literacy and risk perception.

Financial inclusion is one side of the coin. The other side is known as Financial Literacy. Organisation for Economic Co-operation & Development (OECD) identifies the term Financial Literacy as “A combination of awareness, knowledge, skill, attitude and behaviour necessary to make sound financial decisions and ultimately achieve individual financial wellbeing.” Financial literacy enables people to make the best use of financial products and services and invest without waste or incurring unnecessary costs (Capuano & Ramsay, 2011). Financial illiteracy is thought to be associated with the spiralling debt problem impacting people with ‘buy now, pay later’ credit mentality (Hall, 2008). Indeed, research shows that individuals with higher levels of financial literacy tend to have higher disposable incomes and a greater capacity to 'spend, save and invest' (Garman, 1997). With more disposable income and greater capacity to save and invest, financially literate people tend to have more financial products and are more productive investors (Cole & Fernando, 2008). From a survey of Dutch households, van Rooij et al. (2011) find that people with higher levels of financial literacy are significantly more likely to participate in the stock market. Lusardi, Michaud and Mitchell (2013) also identify differential wealth outcomes due to differences in the levels of financial knowledge that individuals possess. As financially literate consumers will be more
confident when making decisions about finance, their financial wellbeing is more likely to be enhanced. In addition to the benefits identified for individuals, financial literacy is important to economic and financial stability for a number of reasons. Financially literate investors can create a more competitive, innovative, safe, stable, accessible, disciplined and liquid financial system and markets” (Capuano & Ramsay, 2011). They are also less likely to react to market conditions in unpredictable ways and more likely to take appropriate steps to manage their risks. All of these factors will lead to a more efficient financial services sector and potentially less costly financial regulatory and supervisory requirements (OECD, 2012).

There comes also the name of the term 'Financial Capability'. Financial capability is a broader concept, encompassing people's knowledge and skills to understand their own financial circumstances, along with the motivation to take action. Financially capable consumers plan ahead, find and use information, know when to seek advice and can understand and act on this advice, leading to greater participation in the financial services market (Treasury, 2007). Financial literacy will undoubtedly make people more capable of managing their finances. It is unclear, however, whether it will reduce financial vulnerability in low-income households if institutional barriers to beneficial financial products are not also addressed. The concept of financial capability includes financial literacy but also addresses these institutional barriers facing low-income households. So, we can conclude that financial capability is achieved when people are more financially literate and the government is termed successful in prevailing financial inclusion throughout the economy.

**Rural Development Challenges and Opportunities**

With the progress of the Indian economy, especially when the focus is on the achievement of sustainable development, there must be an attempt to include maximum number of participation from all the sections of the society. But the lack of awareness and financial literacy among the rural population of the country is hindering the growth of the economy as majority of the population does not have access to formal credit. This is a serious issue for the economic progress of the country. In order to overcome such barriers, the banking sector emerged with some technological innovations such as automated teller machines (ATM), credit and debit cards, internet banking, etc. Though introduction of such banking technologies brought a change in the urban society, a majority of the rural population is still unaware of these changes and is excluded from formal banking (Singh et al., 2014). The results from the PISA 2012 assessment, which was conducted at a time when many of the 65 participating countries and economies were grappling with the effects of the crisis, reveal wide differences in education outcomes, both within and across countries.

People absorb from their environment what they have the opportunity to observe and experience. When parents lack financial knowledge, when they do not talk to their children about household finances, or when the media showers the public with messages to borrow and consume, it is
unlikely that economic socialization leads to optimal financial decision-making. Clearly, to choose wisely from the variety of products and providers available, consumers must have the financial knowledge to navigate today's increasingly complex financial services marketplace. Consumers with the necessary skills to make informed financial decisions about purchasing a home, financing an education or their retirement, or starting a business will almost certainly be economically better off than those lacking those vital skills. Policymakers, practitioners, and financial institutions have responded with growing numbers of financial literacy programs. To cite one example, a study by NCAER and Max New York Life has shown that in India, around 60 per cent of labourers surveyed stored cash at home, while borrowing from moneylenders at high interest rates; a pattern of saving money that is bound to aggravate financial vulnerability of these labourers.

Commercial banks generally view the financial inclusion model as social service and not a profitable proposition that increases their customer base or the deposits. As per the RBI directives, the process of reaching out to any area by the bank with population greater than 2,000 becomes another barrier as such low numbers combined with minimal 8-10 transactions in kiosks and 30-40 transactions in Ultra Small Branches (USBs) per day makes this model non-profitable for the banks. An additional cap on the value of transactions not exceeding Rs. 10,000 and amount of liquidity maintained at these branches to be not more than Rs. 10,000 makes the model less scalable (Singh et al., 2014). World Bank data suggest that only 50% of adults globally had an account at a formal financial institution in 2011 (Demirgüç-Kunt & Klapper, 2012).

Lack of information and guidance regarding practices of savings and credit result in taking wrong financial decisions; this stands in the way of empowerment. Wise financial practices and right financial decision-making go hand in hand. To achieve this, increased information dissemination, knowledge sharing and promoting the practice of financial planning for the SHG members is important. Financial literacy modules that are easy and comprehensible as the one described in the study would be effective tools to lead women towards economic independence (Bijli, 2012). NSSO data reveal that in India, 45.9 million farmer households in the country (51.4%), out of a total of 89.3 million households do not access credit, either from institutional or non-institutional sources. Further, despite the vast network of bank branches, only 27% of total farm households are indebted to formal sources (of which one-third also borrow from informal sources). Farm households not accessing credit from formal sources as a proportion to total farm households is especially high at 95.91%, 81.26% and 77.59% in the North Eastern, Eastern and Central Regions respectively. Thus, apart from the fact that exclusion in general is large, it also varies widely across regions, social groups and asset holdings. The poorer the group, the greater is the exclusion (Report of the committee on financial inclusion, 2008).

There is a cost involved in this massive exercise of extending financial services to hitherto excluded segments of population. Such costs may come down over a period of time with the resultant business expansion. However, in the initial stages some funding support is required for promotional and developmental initiatives that will lead to better credit absorption capacity among the poor and vulnerable sections and for application of technology for facilitating the mandated levels of inclusion. The Committee has, therefore, proposed the constitution of two funds with NABARD – the Financial Inclusion Promotion & Development Fund and the Financial Inclusion Technology Fund with an initial corpus of Rs. 500 crore each to be contributed in equal proportion by Government of India / RBI / NABARD. This recommendation has already been accepted by Government of India.

Financial Skills as a Development Tool

Since the majority of the rural population is still not included in the inclusive growth, the concept of
financial inclusion becomes a challenge for the Indian economy. Since 2005, many concerted measures are initiated by the Reserve Bank of India and Government of India in favour of financial inclusion but the impact of these did not yield satisfactory results. The aim should be to focus on utilizing the existing resources such as Mobile phones, Banking Technologies, India Post Office, Fair Price Shops and Business Correspondents thereby making it more efficient and user friendly for the interest of the rural population as well as the formal sector.

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| Financial Stability |

Equipping citizens with the skills necessary to achieve their full potential, participate in an increasingly interconnected global economy, and ultimately convert better jobs into better lives is a central preoccupation of policy makers around the world (PISA Results: Students and Money, 2012). Research has demonstrated the importance of financial literacy as one of the key life skills for sound financial decision-making. Despite the vast availability of educational resources, young adults were consistently found to have low levels of financial education and financial capability. Of particular concern is that many of these young people do not have adequate money skills to manage their freedom during university time, which may contribute to suboptimal financial behaviours. This study surveyed university students by assessing their financial literacy and perception of the financial education they received in school. Illiteracy across different domains of financial topics was evident. Results also indicate that majority of respondents viewed that high school has not taught them financial knowledge that will prepare them for adult life. Accordingly, it is proposed that graduate skills development in higher education should be broadened to incorporate financial literacy to help university students to navigate the financial maze.

There have been rising global interest in financial literacy as a core life skill due to considerable changes in the landscape for the management of individual and household wealth (OECD, 2012). One of the most noticeable changes is that individuals are increasingly facing a wider range of complex financial products and services and for a longer period of time.

Greater financial literacy can also be an important component to efforts to increase saving rates and lending to the poorest and most vulnerable consumers. Financial literacy substantially increases the demand for banking services, but only among those with low initial levels of financial literacy and low levels of education. Financial literacy appears to also be linked to economic and social development (Singh, 2014). In order to have the ability to act and be
financially capable, people require knowledge and skills to manage their personal and household finances. All other things equal, people who have greater knowledge and understanding about finances and possess financial management skills are more likely to make good financial decisions. As a nationally representative study finds, financial knowledge is associated with positive financial practices (Hilgert et al., 2003).

Efforts to strengthen financial capability in low-income households can build on these time-honoured financial survival strategies. Financial information, education, and training can improve people's knowledge and skills. However, families also need access to quality financial products. Low-income households cannot address the deficiencies of mainstream and alternative financial services industries alone. Policy and regulatory changes are required to build financial capability in low-income households. It is possible to nurture increased financial inclusion without a large increase in aggregate credit. For low-income populations, for example, the most pressing financial needs may consist in having reliable savings and payment instruments rather than credit (Hawkins (2011), World Bank (2008)).

We can see what Mr. K. C. Chakrabarty, former Deputy Governor of RBI, quoted at the stakeholders' workshop on “Financial literacy”, organized jointly by the UNDP, NABARD and MicroSave, “Financial Literacy forms a triad, which is necessary for ensuring financial stability. Not only do the three have a bearing on financial stability, they also have a strong interplay among each other, with each having a vital impact on the other. Thus, financial literacy has significant relevance for financial inclusion and consumer protection. Without financial literacy, we cannot expect to make major headway in either financial inclusion or consumer protection.” Access to formal financial services is increasing in many economies worldwide. This special feature has outlined various ways in which increasing financial inclusion affects central bank policies intended to maintain monetary and financial stability (Mehrotra & James Yetman, 2015).

The global financial crisis has brought the need for financial inclusion into greater focus worldwide as it is believed that widespread incidence of financial exclusion was one of the factors that precipitated the financial crisis. While spread of financial inclusion is recognized through formal financial institutions such as banks, credit unions, post offices or microfinance institutions, the approach of keeping some/all of these entities as a part of the core or as support players, varies from country to country. Besides, it is important to note that the defining principles of financial inclusion, coverage, role and responsibilities of institutions and measurement / monitoring requirements have been evolving over the years. In Indian context, apex bodies like RBI, SEBI and others have taken many initiatives which have been remarkably successful to attain the concentration of consumers or common individuals so as to ensure their financial welfare. Still, there is far more development needed in this area, especially the rural population. Once, the rural people are as conscious and skilled as the people in urban & metro cities, they will be able to manage their finances in sophisticated manner; eventually contributing in the economy by their savings etc.

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