

# Financial Literacy: The Indian Story

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*Financial literacy is of utmost importance for any country's economic growth. Financial education is a crying need and a two way process; where financial education is taught and in turn we learn what 'Real India' is. The research paper attempts to look at the Indian Economy as an Emerging Global Superpower. Financial inclusion is the focal point of the paper which can prove to be the guiding star for the overall economic development for the nation. The general objective of the study is to capture the position of the Financial Sector in India, which includes the Banking Sector, Capital Markets and Insurance Sector as well as the role of financial literacy in developing these sectors. Throwing light on the Indian financial perspective through the eyes of emerging economies, we have used both quantitative and qualitative data sources to draw our conclusion. To support our findings we have referred to reliable agencies like the World Bank, International Monetary Fund, PricewaterhouseCoopers, RBI and Deloitte, thus enriching the data and analysis. The primary research was an attempt to understand the investment pattern and ideology of different groups of people. The results of the survey indicated that the levels of financial literacy in the area were very low. In the end, the paper suggests solutions that would help to chart out the roadmap for the Indian economy. The paper differentiates itself from the past papers by providing statistical data to prove the data collected. The target audience has been carefully chosen and primarily includes the semi urban and rural youth to understand their levels of financial literacy.*

## 1. Introduction

A country that uses only 2.4% of the world's land and yet is home to 17.5% of the world's population, India is the world's most populous democracy. India has a legacy of colonial stagnation and economic backwardness; however, in 1947 when India gained independence, the aim of the leaders was not only to do away with the vagaries of poverty, but also to turn India into a vibrant and self-reliant global economy.

Since the beginning of the economic reforms in 1991, India has seen a systematic transition from being a closed-door economy to an open economy. These reforms have had a far-reaching impact and have helped India unleash its enormous growth potential. Today, the Indian economy is characterized by a liberalized foreign investment and trade policy. India has now developed into a trillion dollar economy with a largely self-sufficient agricultural sector, a diversified industrial base and a stable financial and service sector.

Among the growing economies in the world, India ranks second only to China. The Economic Survey of India pegged the growth rate for 2011-2012 at 6.9% with a population growth rate of 1.6%. This implies that the world would thrive on India's copious human resource.

The objective of this research paper was to identify the two pillars of the economy, financial literacy and financial inclusion, and further analyse the current scenario of the sector thereof. The financial sector is vast and is diverse with all its externalities, thus understanding the sector was the first objective of this paper. Keeping in light the financial conditions prevailing in the economy, the objective of the paper then shifts towards financial literacy. The aim of the

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primary research was to understand the level of financial awareness and the perspective of the common people about the available financial instruments.

The turbulence being faced by the economies across the world, including India, has called for a new wave of reforms to reverse the worsening economic climate of the country. This paper is aimed at analysing and assessing the current scenario of the Financial Sector, providing recommendations, giving a direction, and providing changes that can be implemented to modify the existing policies, propelling India to become the next super power keeping in mind the undervalued importance of financial literacy.

The specific objectives of the paper are as follows:

- Understanding financial literacy levels
- Studying challenges faced by each sector
- Highlighting growth prospects

Throwing light on the Indian financial perspective through the eyes of emerging economies is the central focus of the research, as the country has vast resources and potential with a major advantage of highly skilled professional workforce pitching the country to be now recognized as one of the fastest growing economies of the world.

The research paper flows from understanding the importance of financial literacy in section 3. Then moves on to current scenario of the three main sectors of the finance industry in the section 4 and follows sub-sections namely, Banking, Capital markets and Insurance sector. With the complete understanding of the market in the backdrop, the primary research objectives and analysis are brought to light in Section 5. The paper concludes with appropriate recommendations and inputs by the author in section 6.

## **2. Review of Literature**

Several books, reports and articles were used, of which some of them have been referred below:

“The What, Why and How of Financial Literacy”(February, 2013) by K. C.Chakrabarty, Deputy Governor of the Reserve Bank of India, addressed a few key issues relating to financial literacy in a country like India. The paper highlights the importance of financial literacy, the target audience for financial literacy and the key suggestions to improve the levels of literacy for the growth and development of the nation. Keeping the content of the paper in mind, it lacks empirical evidences or surveys and focuses more on the theoretical aspects.

The report, “Financial Literacy among Working Young in Urban India” (2013), by Sobhesh Kumar Agarwalla, Samir K. Barua, Joshy Jacob, Jayanth R. Varma(IIM-A), presents an investigation of a study on the influence of various socio-demographic factors on different dimensions of financial literacy, among the working young in urban India. The study also investigates the relationship between the dimensions of financial literacy. Adding to the growing empirical understanding of financial literacy across countries, the study provides an analytical basis for enunciating policy to enhance financial literacy of the youth in India.

“National Strategy for Financial Education” (2012), published by the RBI, is an important paper reviewed for this study considering the reliability of the source. The paper traces the

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evolution of the concept of financial literacy. It understands the importance of developing a national strategy for financial literacy in the country. The paper suggests the inclusion of finance and analysis in the curriculum of the schools and colleges through a variety of subjects. It has undertaken an international survey on financial literacy in a number of countries, but most of these countries are not bountiful in population. Thus it makes the scope of the study limited, as it does not focus on a country like India, which has a huge population that would become the future human capital of the country.

A PricewaterhouseCoopers report, “Destination India – Banking Opportunities” (2010), establishes that India is an attractive business destination with a focused approach on the Banking sector. As per the report, outlook for the banking sector is stable and promising. Some reforms can boost growth in the banking sector.

“World Economic Outlook”(2014), a report by the International Monetary Fund (IMF), reviews the economic developments world over and states possible future projections with regard to the World Economy. The report feels that global economic recovery will continue to be uncertain and global economic growth will decline further.

“India 2020” by APJ Abdul Kalam (published in 1998) explores how India can be among the top 5 economic powers by the year 2020. Future projects are based on past trends of growth and development, which serve as basis for developing growth models.

### **3. Importance of Financial Literacy in India**

The financial system of a country plays a key role in the growth and development of a nation. India suffers from low retail participation, primarily due to lack of financial literacy among the masses. In the agenda of financial literacy, it has rightly been said, "Financial literacy needs to be embedded in our way of life. Everyone who earns an income is a potential saver, every saver is a potential investor and every investor ought to be financially literate." Indians are suffering from financial diseases like underinsurance, debt trap, insufficient retirement funds and low return on investment – all of which is caused due to financial illiteracy. The consumers need to be financially literate to be able to understand the financial world and make well-informed decisions that will be profitable. When comparing and evaluating financial products, the consumer should be well aware of the basic terms of financial markets and the latest trends to manage their savings.

The innovations and growing complexity of financial products is adding enormous pressure and responsibility on the shoulders of financial investors, offering the consumers a myriad financial products and services, rendering the masses unaware of the stockpile of financial services at their disposal.

As the financial markets become more sophisticated and widen their scope, financial education is becoming imperative to ensure the smooth functioning of the financial market. The need for financial literacy in a country like India is because of:

#### **3.1 Increase in the Life Expectancy, Changes in Pension Agreement and Transfer of Risk**

The improvement in healthcare services has increased life expectancy in India, resulting in a longer time spent in retirement. The result is a greater need of financial planning, expanded insurance and provision of expanded healthcare related expenses for unpredictable eventualities. The defined benefit plans are speedily being replaced by defined contribution

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pension plans, shifting the burden on the working class to save for their financial security after retirement. Also most of the workers are unaware of the risks they are facing due to lack of knowledge and skills to face these risks.

### **3.2 Increase in an Individual's Responsibility**

The nuclear family structure in the cities makes an individual take a number of decisions related to savings, spending, investments etc. They also have to make provisions for health issues and securing their child's future through systematic investment plans.

### **3.3 Financial Product and Service Innovation**

Deregulation and liberalization have resulted in new financial products that are tailored to meet the specific market needs, providing consumers with more choices to park their savings. To tap the benefits of these products, understanding of the new financial products is crucial on part of the consumers.

### **3.4 Multifaceted Features of Financial Products**

The growing complexity of newer financial products confuses today's individuals who are not even able to understand the basic financial concepts. Also, a wide variety of choices offering a range of benefits makes the investment decisions complex thus leading to delay in decision making.

### **3.5 Technological Changes and Market Innovations**

The development in technology has transformed the functioning of the markets making transactions speedier. Financial literacy will empower the consumers and employees to take correct decisions and also understand and predict market situations.

Thus to understand the importance of financial literacy it is vital to first understand the different sectors that bind the Indian financial system. The research paper is emphasizing the awareness on the basis of the primary research and different observations in the said sectors.

The different vital sectors are:

- Banking sector
- Capital markets
- Insurance Sector

## **4. Vital Sectors of the Indian financial system**

### **4.1 Banking Sector**

In Third World Countries, including India, with high degree of rural population, an institution is necessary at the central level for looking into the financial needs of the poor at the grass root level. Since independence, the mainstream banks have been unable to reach to the majority of the unbanked population in the country. For this, we need institutions that can reach this untapped population. Currently, just one out of two Indians have a savings account and only one in seven have access to bank credit. There is also a huge disparity in the access to

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credit where the six largest cities in the country have 10% of bank branches, while the bottom 50 districts have merely 2% of branches. Thus to cater to the need of the masses, micro finance institutes have expanded their reach to 30 million clients in rural areas in a matter of 5-7 years.

The banking sector is emerging as one of the strongest drivers of the Indian Economy. The Indian Banking Industry stands at a massive valuation of USD 1.22 trillion (April 2012). Today, the banking industry is at the crossroads of an invisible revolution, and the future prosperity and stability of the Indian Economy will heavily depend on the performance of the Indian Banking Industry.

The banking sector in India is a regulated form of finance. Most educated and uneducated people still trust the simplest form of bank deposits over other forms of market mechanisms. The primary research indicated a staggering 36.5% of the population still believe that Fixed Deposit is the best form of investment. Even though maximum population surveyed did not have knowledge of the intricate financial systems of the economy, 69.5% of the surveyed people had their own bank accounts. But this penetration does not bring along literacy, as maximum surveyors still lacked basic information on the interest rates received.

Financial inclusion is needed to extend financial services to the large hitherto, marginalized population, i.e., the people who are unable to meet all their requirements of livelihood of the country to unlock its growth potential. The country will be able to achieve their target of financial inclusion only when there is maximum financial literacy in the country.

### **4.2 Capital Markets**

Expansion of Indian economy in the last few years attracted Foreign Institutional Investments (FIIs) and led to increased merchant banking activities in the country. Indian Capital Market remains one of the most resilient markets globally and is poised to be one of the top most destinations for domestic and global businesses to grow and invest in. India has attracted nearly four-fifth of the entire FDI inflow in the South Asian region, which highlights investors' confidence in India's future growth story.

According to the Deloitte Report 2012, India's performance has remained quite stable with good performance in complex areas including financial markets, business sophistication and innovation. Easing of monetary policy has resulted in increased liquidity which will drive the market upwards.

As per the primary survey, more than 40% considered equity markets to be a gamble. A significant 48% of the population surveyed didn't understand the complexities of the market, leaving less than 10% of the respondents to trust the equity markets as a form of investment. Another surprising response was that of the mutual fund investment, where around 55% of the respondents did not have any knowledge about this form of investment option available to them. This proved the lack of knowledge and the inability to trust the capital markets.

Even with a diverse and fast expanding capital base, the capital markets fails to reach out to the common man. The primary research conducted showed that nearly 50% of the surveyed audience did not believe in the concept of investments in these markets and the rest considered it to be a gamble, and thus refrained from investments here. This proved the lack of comprehension amongst the common man about the capital market.

## 4.3 Insurance Sector

The Indian markets have become even more attractive for global insurance majors due to the fact that markets of developed economies are now saturated. The propensity for insurance products is now increasing within the rural consumers. It has been indicated by a research that rural consumers are now willing to spend anything between Rs. 2100 to Rs. 3500 as insurance premium yearly. The majority of the population especially in rural areas is uninsured mainly due to lack of awareness. Thus they can become the target market for these insurance companies. The health insurance sector is also a potential market that must be tapped by the insurance companies.

With more than 90% of the population without insurance cover, India shows a great potential in the insurance sector. Also with an increase in the FDI limit from 26% to 49% from September 2012 by the government, there would be more foreign players in the picture, ensuring a better insurance industry in the near future with maximum population under the umbrella of insurance.

With growing competition in the insurance industry, the people have a variety of policy options to choose from. When surveyed, the primary research indicated that around 54.6% of the surveyed population had an insurance policy, but were unaware of the array of options available to them. The remaining 35.4% who didn't have a policy are the potential target market for the insurance sector. Among the surveyed population who had a policy, around 65% were unaware about the procedures and new developments in the insurance industry. The surveyed population believed in the conventional policy options, but they were apprehensive of new ventures. This indicates a need for financial literacy. The insurance industry has the scope to penetrate to the smallest of areas and the weakest section of society. Thus reforms in financial literacy will help in the penetration of the insurance sector.

## 5. Primary Research

### 5.1 Primary Research on Financial Literacy

Pegging India to be the next emerging economy requires maximum financial literacy. The main objective of the primary research after recognizing its importance is to determine the level of financial literacy in the country. Majority of the Indian population are not financially literate hampering the economic growth. According to the survey, more than 60% of the consumers are not aware of the services they can avail of or where their money could be better invested.

### 5.2 Objective

The basic objective of the primary research was to determine the financial literacy of Mumbai and Thane district by conducting a survey which would serve as a basis for detailed study of the financial literacy of the economy as a whole. One of the other objectives was to find the number of people who are educated about MFIs and SHGs services available to them, understand the investment pattern and the ideology of different groups of people. The survey conducted also aimed at getting to know the mindset of the consumers in case of saving and spending power.

## 5.3 Target Audience

An appropriate representation of the economy needs to have an opinion of all groups of people. For this, the target audience in the primary research had to be a range of people. It included students from the age of 18 to 25, as well as uneducated youth. Working population was surveyed to understand their investment pattern and unemployed were surveyed to read the mindset with respect to savings and purchasing power. Unskilled labor was surveyed to understand their awareness of financial services. Senior citizens were also approached to see the level to which they are aware of new services and are able to avail of these services. The sample was chosen carefully to represent the entire target audience and focused on absorbing minute details about their literacy levels. Though all the different segments were given due importance, the financial literacy levels of the students and the youth was of utmost significance as this is the population which will majorly represent the average Indian population in the near future. At the same time, the investing and trading activities of the retired and elderly population reflects on their mindset and attitude towards taking risks and eventually also builds a positive impression on the youth for understanding and engaging themselves into trading activities.

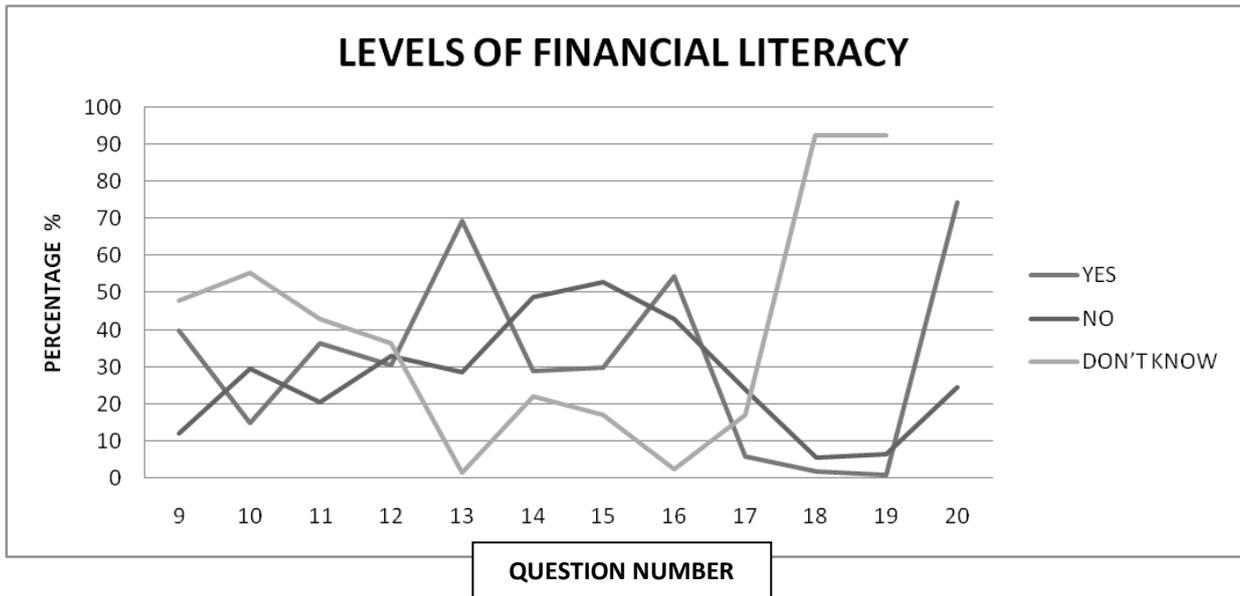
## 5.4 Methodology

The basis of the primary research was the survey method, where a sample was selected as a representation of the entire economy. In this case the sample area was Mumbai and Thane district; which included Vasai, Virar, Thane city, Nalasopara, Mira Road, Dahisar, Bhayander, Naigaon, as well as Dombivali and Kalyan. A basic interview schedule of 20 questions was prepared and data was collected by surveying the people of the places (as stated).

Through this survey, conducted over a month, information was gathered from 202 individuals which included auto drivers, roadside hawkers, retailers and small scale entrepreneurs, watchmen, employees in tertiary and service sector, students, senior citizens and house wives. As seen in earlier reports, even though a primary research was conducted, it was inadequate to reflect the levels of financial literacy in the semi urban areas especially where the population is assumed to have some level of knowledge. Also, the previous papers have chosen countries like Netherlands, Australia and New Zealand, which are not an appropriate representation when compared to a country like India that has a copious population, unlike these countries. The 202 individuals were from different walks of life and represented diverse social and economic backgrounds. Not only were their answers recorded, but the questions were explained and translated into the languages which suited them. A face-to-face interaction gave an opportunity to gauge their facial expressions and attitude towards the whole procedure.

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Figure 1: Levels of Financial Literacy



## 5.5 Data Analysis

The above figure is a graphical representation of the primary research. The survey conducted had three options as their answers. If a person answers 'option A', it means that the person is aware of the particular financial aspect; whereas if the answer selected was 'option B', the person was considered as financial illiterate. A third option 'C' was given for those who would be confused of the asked question. As per this particular format of research, the financial literacy levels prevalent in the area were assessed. It was noticed that although 58.5% of the surveyed population do not have a household budget, they do take into consideration their ability to afford a particular product before they buy it and also that a vast majority of people prefer to save their money rather than spend it. A large number of people are against the belief that "Money is there to be spent," which reflects the psychology of the Indian population to save money.

Although 69.5% of the surveyed people do have bank accounts, only a diminutive 29% of these people know the rate of interest they receive on their account and even fewer know the services and the benefits they can avail of as account holders. 54.5% of the population, which is a substantial part of the surveyed people, does have insurance policies; but having said that, several are unaware of the various types of policies being offered by companies today. Further, the research showed that only 6% knew about trading on the stock market, mutual funds, microfinance institutions, self-help groups, etc., and about 70% were not aware of the concepts and procedures of trading on stock markets, mutual funds. It was observed that most people refrained from investment of any kind either because they were unaware of how to invest their money in a profitable and safe manner or they simply felt that it was too risky an option for them to undertake. Conversely, when asked if they would attend a financial literacy program, 74.5% of the surveyed people said they would definitely do so as it would be of great help to them. 40% considered stock market to be a gamble and 55.5% were uninformed of the existence of mutual funds. A deplorable 49% did not have the basic knowledge of the interest rates received on their accounts. More so, 92.5% were unacquainted of MFI and SHG benefits that were available to their advantage.

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This primary research helped in determining that the people of the surveyed area were oblivious to even the existence of certain benefits that financial knowledge could bring to them. The positive outcome was the fact that the people were eager to learn and know more about better management of their finances. Thus, the aims of a financial literacy survey were met with.

### 6. Recommendations

From the research it was evident that the levels of financial literacy in the area were very low. This is something that must be addressed rapidly. The country envisions providing every Indian individual with an electronic bank account by January 2016. The researcher suggests that:

- It is suggested that schools should consider including financial literacy in their curriculum and also encourage their students to participate in financial literacy contests. For these, bodies like SEBI, BSE, NSE, etc. should sponsor business and economics festivals in colleges to improve financial literacy. These programs will evaluate and certify students on day-to-day money management, based on their understanding of key concepts including financial and economic terms, principles of savings and budgeting, banking, taxation and stock markets, prudent investment avenues, basic accountancy and entrepreneurial skills.
- Understanding the importance of opportunity cost is another suggestion to improve the levels of financial literacy.
- A fund should be created from which the Government can organize financial literacy programs on a nationwide scale.
- A project needs to be launched on increasing market player's initiatives for financial education. For this, the commercial banks need to initiate various measures for creating awareness through financial literacy and counselling centres and rural self-employment training institutes. Thus absorbing a large segment of financially illiterate and excluded segments of prospective customers.
- There is already the Investor Education and Protection Fund (IEPF) of BSE in which 1 rupee of every transaction that takes place on a stock exchange is directed to the financial literacy fund. There is a need to increase the share of money from each transaction that will increase the availability of funds for organizing more seminars and creating financial literacy.
- A comprehensive strategy involving urban as well as rural households should be implemented with joint efforts of Government and private players.
- Funds from all bank accounts that have been dormant for more than three years should be transferred into the fund for financial literacy.
- With increasing interest in this area of learning, there is an extraordinary opportunity to develop a national strategy to improve the economic and financial capability of Indians.
- To seep the efforts to the grass root level, the delivery channels for financial education can be summed through school curriculum, social marketing, resource persons, adult education, self-help groups, microfinance institutes, helpline and other channels.

## 7. Conclusion

India has a savings to GDP ratio of 33% which is the highest in the world. India is the nation of savers and investors; additionally, more than 52% of the population is below 25 years of age, which creates a need for developing a population which is financially literate. Moreover, 85% of the household savings is parked in fixed deposit. In India, household savings in shares, including mutual funds is around 7%. In the US, 50% of household savings are in mutual funds and shares. This is one of the factors for low household net worth in India. Markets like Hong Kong, Korea and Taiwan, have retail participation that is much stronger than foreign investors.

In India, it is the reverse where the share of retail investors is miniscule in listed companies, while FIIs hold sway on how markets move. A strong retail base helps lessen wild volatility in the stock markets. Indians are more risk averse than their global counter-parts. As mentioned by Deepak Parekh, Chairman HDFC Ltd., "I believe the problem is more to do with a lack of awareness of the equity markets." In India, 73% of farmer households have no access to formal credit and 45% of the adult population of India has not accessed financial services from formal financial institutions.

In an era of accelerating GDP and rising per capita growth, financial literacy has become more critical than ever before so that we all reap the tangible benefits of the nation's economic prosperity. Financial inclusion has been quite high on the governmental agenda, given its emphasis on widening the Banking & Financial services network across the country.

In conclusion, financial literacy is the ultimate pillar of a strong financial system. Financial literacy and financial education should be on the agendas of educators, businesses, government agencies, policy makers, NGOs and the issues should be dealt with policy reforms at the national level. Thus, it is important to achieve highest possible financial literacy in the country as its benefits are not restricted to an individual or family, but to the society and the macro economy as a whole.

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## Appendix

### Questionnaire

Please fill the details given below. The data collected will be used purely for academic purpose.

1) Name of the Respondent: \_\_\_\_\_

2) Age: \_\_\_\_\_

3) Marital Status: \_\_\_\_\_

4) Who is responsible for day-to-day decision about money in your household?

a) You b) Parents c) Spouse d) Any other family member

5) Does your house have a budget?

a) Yes b) No c) Don't Know

6) Before you buy something do you carefully consider whether you can afford it?

a) Yes b) No c) Don't Know

7) Do you find it more satisfying to spend money than to save it for a long time?

a) Yes b) No c) Don't know

8) Do you agree that money is there to be spent?

a) Yes b) No c) Don't Know

9) Do you feel Equity Markets are like gambling?

a) Yes b) No c) Don't know

10) Do you feel Mutual Funds are safe investments as we have a fund manager to manage the money?

a) Yes b) No c) Don't know

11) Do you agree that Fixed Deposit is the best investment come what may?

a) Yes b) No c) Don't know

12) Do you believe the main aim of any investment is to double your money?

a) Yes b) No c) Don't know

13) Do you have a bank account? Which one?

a) Yes b) No c) Don't know

14) Do you know the interest rate on your bank account?

a) Yes b) No c) Don't know

15) Do you keep a note of your income and/or expenditures? (Tick the appropriate code)

a) No, I am not able to keep track of my expenditures and income

b) Yes, I have a broad idea of my expenditures and earnings

c) Yes, I keep a written record of important expenses and earnings

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16) Do you have an insurance policy?

a) Yes b) No c) Don't know

17) Do you have a DMAT Account? Do you trade on the stock exchange?

a) Yes b) No c) Don't know

18) Are you aware of MFI's? Have you ever availed their services?

a) Yes b) No c) Don't know

19) Are you aware of any SHG's? Are they approachable?

a) Yes b) No c) Don't know

20) Would you like to attend a Financial Literacy Program?

a) Yes b) No c) Don't know