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FINANCIAL LITERACY, INDIVIDUAL SAVING REGULARITY AND RISK TOLERANCE

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ABSTRACT

Financial literacy is a combination of knowledge, skill, behavior, and awareness, necessary to take well-balanced financial decisions leading to financial well-being. It has an influence on financial risk tolerance and saving behavior of the individual. Higher the level of financial literacy, more are individuals tolerant towards financial risks and more positive is their attitude towards saving. The study tries to find out the level of financial literacy amongst residents of Muscat, Oman and also whether there is any relationship between financial literacy and saving behavior. The research method in this study used is quantitative in nature. Data was analysed using Statistical Package of Social Sciences (SPSS). Techniques like Correlation, T-test and Anova are used for analysis and the data has been interpreted accordingly. It is observed from the findings that there is a significant relationship between financial literacy and risk tolerance.

KEYWORDS

Oman, financial literacy, risk tolerance, saving behavior.

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INTRODUCTION

Current evolutions in the financial markets, availability of a wide array of financial products and services have made it necessary for people to be more knowledgeable and proficient in managing their finances. Financial literacy helps individuals to manage their finances in an efficient and wise way leading to better investment and saving patterns, budgeting, insurance and tax planning and retirement plans. A good saving behavior protects both household and the nation's economy against financial crisis and downfall. Financial literacy creates awareness about financial markets and leads to positive attitude towards financial risk tolerance. The interdependent relationship between financial literacy, saving regularity and risk tolerance can neither be underestimated nor ignored. The study measures financial literacy and examines how demographic factors can influence literacy levels? It also examines saving regularity, risk tolerance and its relationship with financial literacy among residents in Muscat, Sultanate of Oman. The current study contributes to the knowledge of financial literacy, saving regularity, risk tolerance and their interrelationship in Muscat, Sultanate of Oman. In the following section, an overview of previous studies is provided.

LITERATURE REVIEW

Literature related to financial literacy, saving behavior and the relationship between financial literacy, saving behavior and risk tolerance were examined from 2000 to 2016. Databases such as EBSCO, SSRN e-library database and Google scholar were searched for peer reviewed scholarly research publications.

FINANCIAL LITERACY

The Organization for Economic Cooperation and Development (OECD, 2005) defines financial literacy as 'A combination of awareness, knowledge, skill, attitude and behavior necessary to make sound financial decisions and ultimately make personnel financial wellbeing.' Financial literacy is the ability to make informed judgments and to take effective decisions regarding the use and management of money (ANZ, 2008). Servon and Kaestner (2008) define financial literacy as "a person's ability to understand and make use of financial concepts". In the current study financial literacy is defined as a combination of financial knowledge and its application to financial decision making.

A number of researchers reported low levels of financial literacy. Lusardi and Mitchell in 2007 found out that only 18% of the respondents in the Health and Retirement Survey (HRS) could calculate compound interest. According to Klapper & Panos in 2011, 36% of the respondents of their sample selected could calculate compound interest or answer about inflation. Lusardi and Tufano in their another study in 2008 reported that only 7% recognized the time value money. As pointed out by Lusardi (2008), this sort of lack of knowledge has serious repercussion for retirement planning, the design of retirement plans and financial education programs.

Lusardi, A. & Mitchell, O.S. (2011) in their study "Financial Literacy and Planning: Implications for Retirement Wellbeing" examined financial literacy in Germany. The study examined the link of causality between financial literacy and retirement planning and developed an instrumental variables strategy by use of regional variation in the financial knowledge of peers. They used ordinary least square regression and found out that women who lived in East Germany lacked the knowledge and basic financial concepts. It was also found that there is no significant difference in retirement planning between age group and no longer differences in education. Tendency to plan for retirement increased with income. Result of this study showed positive impact of financial knowledge on retirement planning. Delafrooz & Paim, (2011) analyzed the relationship of savings behavior and financial problems with financial literacy, financial stress and financial management practices in their study "Determinants of Saving Behavior and Financial Problem among employees in Malaysia." They used structural equation model to examine the degree to which financial literacy, financial management practices and financial stress influenced financial problems and saving behavior. From the results of

their study it can be concluded that financial literacy and financial management practices contributed significantly to the prediction of savings behavior. It was found out that financial management practices had the most positive influence for savings behavior. Based on the findings they have concluded that workplace financial education programs could improve workers' financial problem by reducing financial stress.

Beckman (2013) in his study on "Financial literacy and household savings in Romania" used internationally comparable measures of financial literacy and analyzed relationship of financial literacy and household saving in Romania. He found out those individuals who were financially literate and with regard to inflation were more likely to invest in pension funds and save using more than one interest bearing saving instrument. His study showed positive relationship between financial literacy and saving behavior.

Klapper & Panos, (2011) in their study "Financial Literacy and Retirement Planning: The Russian Case" found out that financial literacy is significantly and positively related to retirement planning using private pension funds and schemes. Based on their study they found out that residents in rural areas are much more contingent on the public provision and invest less in private schemes and savings. And hence based on the results of their study they have suggested a clear policy implication: along with encouraging the availability of private retirement plans and financial products, efforts to improve financial literacy can be critical to the expansion in the use of such schemes.

SAVING REGULARITY

In economic contexts, saving is defined as the residual income after deducting current consumption over a certain period of time (Browning & Lusard, 1996). In the psychological context saving is referred to the process of not spending money for current period in order to be used in future (Warneryd, 1999). Thus, saving behavior is the combination of perceptions of future needs, a saving decision and a saving action. Keynesian Economics defines saving as "the amount left over when the cost of a person's consumer expenditure is subtracted from the amount of disposable income he earns in a given period." The current study defines saving regularity as the frequency with which an individual is able to save.

RISK TOLERANCE

Within the domain of financial decision making, financial risk tolerance is generally defined as the maximum amount of uncertainty someone is willing to accept when making a financial decision (Grable & Joo, 2004). Irwin (1993) defines financial risk tolerance as "the willingness to engage in a financial behavior in which the outcomes are uncertain with the possibility of an identifiable loss". In the current study, Financial Risk tolerance is degree of risks the investor is ready to accept for when an investment decision made.

RELATIONSHIP BETWEEN FINANCIAL LITERACY, SAVING REGULARITY AND RISK TOLERANCE

Previous studies show that financial literacy has a direct impact on saving and risk tolerance behavior of the people. Higher level of financial literacy has positive impact on saving behavior and it leads better planning, as they have more knowledge on financial concepts. Moreover, It is said that a high level of financial literacy have positive attitude to financial risk tolerance. The following section summarizes key research findings on the relation between financial literacy, saving regularity and risk tolerance.

Literature review highlights the significance of financial literacy and its measurement. It is also vital to evaluate the background factors like gender, nationality, income level that affect the financial literacy.

OBJECTIVES OF THE STUDY

The study seeks to measure financial literacy among the citizens in Muscat. It also tries to examine if literacy levels differ by gender, nationality, occupation, education, income level and work experience. It also studies the relationship between financial literacy, risk tolerance and saving regularity.

1. To measure the level of financial literacy among people residing in Muscat, Sultanate of Oman.
2. To identify the background factors affecting financial literacy of citizens of Muscat.
3. To study the influence of financial literacy on risk tolerance and saving behavior of individuals

It is thus **HYPOTHESIZED** that:

H_{A1}: There is a significant relationship between financial literacy (Measured as sum of basic financial literacy and advanced financial literacy) and background factors (gender, nationality, occupation, education, income level and work experience).

H_{A2}: There is a significant relationship between financial literacy (Measured as sum of basic financial literacy and advanced financial literacy) and saving regularity.

H_{A3}: There is a significant relationship between financial literacy (Measured as sum of basic financial literacy and advanced financial literacy) and risk tolerance.

RESEARCH METHODOLOGY

The study uses a quantitative and descriptive research design. Financial literacy was measured through a questionnaire designed by Lusardi (2008). The questionnaire consists of three parts. The first part measures basic literacy, second part measures advanced literacy and the third part collects information on economic and demographic profile of the respondents. Three multiple-choice questions on Percentage, Interest rate and Inflation rate calculations measured Basic Financial literacy. Advanced financial literacy was measured through ten multiple-choice questions on Functions of stock market, relation between bond price and interest rates, riskiness of assets and compound interest rate calculations. One point was awarded to a correct answer and there was no negative marking. The questionnaire was e mailed as a google docs file to hundred participants out of which 85 completed, usable questionnaires were received. 63.5% of the respondents were male, 58.8% were expatriates and 57.6% were in the age group of 20-25 years.

DATA ANALYSIS AND RESULTS

Financial Literacy Level

Financial literacy was measured as sum of basic and advanced literacy. The maximum attainable score for basic financial literacy was 3 and for advanced financial literacy was 10. Results show that respondents scored 2.1 out of a maximum of 3 points on basic financial literacy. The score on advanced financial literacy was 6.35 out of a maximum attainable score of 10. The overall literacy score was 8.45 out of a maximum attainable score of 13.

TABLE 1: FINANCIAL LITERACY LEVEL OF RESPONDENTS

	Mean	Standard Deviation
Basic Financial Literacy	2.10	0.96
Advance Financial Literacy	6.35	2.64
Financial Literacy	8.45	3.6

Source: SPSS Output

It was observed that 42.9% of the respondents scored the maximum attainable score on basic financial literacy and 32.1% scored 2 out of 3. Thus, it can be inferred that the respondents are aware about simple percentage, inflation rate and interest rate calculations.

TABLE 2: BASIC FINANCIAL LITERACY LEVEL OF RESPONDENTS

Score	Frequency	Percent
0	7	8.3
1	14	16.7
2	27	32.1
3	36	42.9

Source: SPSS Output

From the following table it can be observed that 39% of the respondents scored 5 or less on advanced financial literacy. 24.7% of the respondents scored 9 and 10 out of the maximum attainable score of 10.

TABLE 3: ADVANCED FINANCIAL LITERACY LEVEL OF RESPONDENTS

Score	Frequency	Percent
0	1	1.2
1	1	1.2
2	4	4.9
3	5	6.1
4	14	17.1
5	7	8.5
6	11	13.4
7	8	9.8
8	10	12.2
9	6	7.3
10	15	18.3

Source: SPSS Output

BACKGROUND FACTORS AND FINANCIAL LITERACY

The study tried to understand the role of demographic and economic factors on financial literacy. It was found that mean of total financial literacy of male respondents is 8.84 and female respondents is 7.8. Whereas the Basic financial literacy for male respondents is 2.04 and female respondents is 2.19. And the advanced financial literacy was 6.80 and 5.61 respectively. Financial literacy among the Expatriates found to be more comparing to Omanis. The mean of total financial literacy among Expatriate is 9.35 and Omanis is found to be 7.23.

TABLE 4: FINANCIAL LITERACY SCORES BASED ON GENDER AND NATIONALITY

	Male	Female	t	Sig	Omani	Expatriates	t	Sig
Basic Financial Literacy	2.04	2.19	-0.71	0.48	2.13	2.10	0.133	.05
Advance Financial Literacy	6.80	5.61	2.09	0.05	5.10	7.25	-3.63	.000
Financial Literacy	8.84	7.8	1.61	0.11	7.23	9.35	-2.79	.004

Source: SPSS Output

Results of the *t* test show that there is no statistically significant difference in the financial literacy levels of male and female respondents. However, a statistically significant difference is reported in the financial literacy levels of Omani and expatriate respondents *t* (83) = -2.79, *p* = .004.

TABLE 5: FINANCIAL LITERACY SCORES OF RESPONDENTS BASED ON EMPLOYMENT STATUS

	Unemployed	Employed	Self-Employed
Basic Financial Literacy	2.06	2.19	2.25
Advance Financial Literacy	6.56	5.38	3.50
Financial Literacy	8.61	7.57	5.75

Source: SPSS Output

The above table presents scores of respondents on basic and advanced financial literacy based on their occupation. It was found that the mean of total financial literacy among students is 8.61.

TABLE 6: ONE-WAY ANALYSIS OF VARIANCE OF FINANCIAL LITERACY BY OCCUPATION

	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	17.434	12	1.453	1.298	.240
Within Groups	76.122	68	1.119		
Total	93.556	80			

Source: SPSS Output

To analyze the role of occupation on financial literacy, ANOVA was performed using occupation category as an independent variable and financial literacy as the dependent variable. There was no statistically significant difference, as presented in the above Table 6, between occupation and financial literacy.

FINANCIAL LITERACY, RISK TOLERANCE AND SAVING REGULARITY

Pearson Correlation was computed to test the relationship between financial literacy, risk Tolerance and saving regularity among people residing in Oman. A statistically significant relationship was reported between Financial Literacy and risk tolerance ($r = 0.269$, $p = 0.013$). However, no statistically significant relation was reported between financial literacy and saving regularity.

CONCLUSION

The purpose of this study was to measure the financial literacy levels among citizens in Oman. The questionnaire designed by Lusardi (2008) was adopted to measure basic and advanced financial literacy. The study found that the basic literacy score was 70%, advanced literacy score was 63.5% and advanced literacy score was 65%. Thus, awareness of functions of stock market, relation between bond price and interest rates, riskiness of assets and compound interest rate calculations needs to be created. By improving the literacy rates, the Sultanate can increase investment and the returns.

Secondly, the study intended to identify the background factors affecting financial literacy of citizens of Muscat. The study reported no significant difference between male and female citizens. However a significant difference was reported between Omani and expatriate. Financial literacy levels of Omani nationals were lower than expatriates. Financial education and training programs has to be imparted in Omani schools and colleges.

Thirdly, the study tried to study the influence of financial literacy on risk tolerance and saving behavior of individuals. A statistically significant relation was reported between financial literacy and risk tolerance and no significant relation was reported between financial literacy and saving behavior.

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