



FINANCIAL KNOWLEDGE: OBJECTIVE REALITIES AND SUBJECTIVE PERCEPTIONS

Jibin Antony

Research Scholar

Department of Commerce

St. Berchmans Autonomous College, Changanacherry, Kerala, India.

Abstract: *The purpose of this study is to identify whether objective financial knowledge has an effect on subjective financial knowledge. This study used data obtained from multi stage random sample of individuals in Kerala, India (N=300). Results of one way –between subjects ANOVA and Post hoc (LSD) test shows that, effect of objective financial knowledge on subjective financial knowledge is significant. Specifically, higher the objective financial knowledge of individuals, higher will be their subjective financial knowledge and vice versa.*

Index Terms: Financial knowledge, Objective financial knowledge, Subjective financial knowledge.

1. INTRODUCTION

‘Financial knowledge’ has been duly discussed these days because of its practical implications. Evidence shows that, individuals who are financially savvy are more likely to exhibit sound financial behavior that ultimately contributes financial satisfaction (Ali, Rahman & Bakar, 2015; Hilgert, Hogarth & Beverly, 2003; Joo & Grable, 2004; Xiao, Sorhaindo & Garman, 2006). Financial knowledge refers to the understanding about financial concepts and products. Individuals can achieve this through formal education, practical experience, consultation with experts etc., Lusardi & Mitchell (2008) suggests three components for measuring financial knowledge - basic numeracy for the calculation of interest rates, awareness about inflation and risk diversification. Financial knowledge can be categorized in to objective financial knowledge and subjective financial knowledge. Objective financial knowledge is the actual financial knowledge measured by the financial literacy questions and subjective financial knowledge is the self assessed financial knowledge measured by asking the individuals to self assess their financial knowledge. Hadar, Sood & Fox (2013) states that, objective financial knowledge indicates the individual’s ability in financial practices. On the other hand, subjective financial knowledge shows the confidence in the ability for financial decision making.

To engage with financial issues or to take better financial decisions, individuals need to have sound financial knowledge (Robb & Woodyard, 2011). Bernheim (1998), found that, poor financial knowledge acts as a constraint in sound saving habits. Individuals with lack of financial knowledge, may engage in high cost method of borrowing (Lusardi & Tufano, 2015). Researchers (Asaad, 2015 and Parker, Bruin, Yoong & Willis, 2012) shows that, both objective and subjective financial knowledge shares distinctly to the financial behavior of individuals. In the words of Xiao, Ahn, Serido & Shim (2014), compared to the objective knowledge, subjective knowledge has strong impact on composite financial behaviors and each specific financial behavior. Lusardi & Mitchell (2007) stated that, objective financial knowledge is positively associated with individual’s financial behavior. Generally there is a mismatch between individual’s objective financial knowledge and subjective financial knowledge. That means, between the actual financial knowledge and self assessed financial knowledge. Even though, the actual financial knowledge is low, sometimes individuals overestimate it (Lusardi, 2011). Similarly individuals with high objective financial knowledge often under estimate it. Woodyard & Robb (2016) used the measure of financial sophistication by considering individuals’ perception and objective reality in financial knowledge (subjective knowledge and objective knowledge) which reveals the overconfident (low objective - high subjective) or underconfident (high objective - low subjective) individuals. Nonetheless, there is a possibility that objective realities have an effect on subjective perception. Individuals having high objective knowledge can enhance their confidence which in turn reflects his subjective assessment. On that ground, following hypothesis was proposed.

Ha: Effect of objective financial knowledge on subjective financial knowledge is significant.

2. METHODOLOGY

2.1 Participants and Procedure

The population of this study consists individuals in Kerala, India who are aged 25 and above. By adopting multi stage random sampling, 300 respondents were interviewed and their responses were obtained. This 300 consists 57 percent males and 43 percent females. Nearly half of the respondents belong to the age group of 36 - 50 years.

2.2 Measurement of Variables

2.2.1 Objective financial knowledge

Objective financial knowledge of individuals was measured by administering a quiz. It consists ten true- false questions regarding interest rate, inflation, savings & investment, credit usage, budgeting, risk diversification, insurance etc., The correct answer for each question is given a score of one. Scores ranging from zero to ten were taken for analysis. The distribution of scores for different levels of objective financial knowledge is depicted below.

Score	Level of objective financial knowledge
0 – 4	Low
5 -7	Moderate
8 -10	High

2.2.2 Subjective financial knowledge

Subjective financial knowledge of individuals was measured by seven point - one item scale. Respondents were asked “how would you assess your overall financial knowledge?” Responses ranged from 1 to 7 with higher numbers indicating greater level of financial knowledge.

2.3 Data Analysis

The statistical tool - one way between subjects ANOVA was conducted to test the hypothesis. Post- Hoc (LSD) test was used for identifying the significance of difference among the mean scores.

3. RESULTS

Table: 1
Scores for subjective financial knowledge based on objective financial knowledge

Objective financial knowledge	Subjective financial knowledge			
	Mean	Std. Deviation	Minimum	Maximum
Low	2.75	1.391	1	7
Moderate	4.08	1.473	1	7
High	4.78	1.201	1	7
Total	4.26	1.477	1	7

Source: Primary survey

Table 1 shows that, objective financial knowledge has an effect on subjective financial knowledge as there exist difference in the mean scores for subjective financial knowledge among various levels of objective financial knowledge. In order to check whether this effect is significant or not, following hypothesis was proposed.

Ha: Effect of objective financial knowledge on subjective financial knowledge is significant.

Table: 2
Subjective financial knowledge based on objective financial knowledge - ANOVA

Source of variance	Sum of Squares	Df	Mean Square	F	Sig.
Between groups	114.649	2	57.325	31.672	.000
Within groups	537.547	297	1.810		
Total	652.197	299			

Source: Primary survey

A one – way between subjects ANOVA was conducted to compare the effect of objective financial knowledge on subjective financial knowledge in low, moderate and high levels. There was a significant effect of level of objective financial knowledge on subjective financial knowledge at the $p < .05$ level for the three categories [$F(2,297) = 31.672, p = .000$].

Table: 3
Significance of mean difference in subjective financial knowledge between various levels of objective financial knowledge

Objective financial knowledge (I)	Objective financial knowledge (J)	Mean difference (I-J)	Significance
Low	Moderate	-1.335*	.000
	High	-2.033*	.000
Moderate	High	-.698*	.000

Source: Primary survey

* The mean difference is significant at the 0.05 level.

Post hoc comparisons using the LSD test indicated that, the mean score for low level of objective financial knowledge ($M = 2.75, SD = 1.391$) was significantly different than moderate ($M = 4.08, SD = 1.473$) and high ($M = 4.78, SD = 1.201$) levels of objective financial knowledge. Similarly high level of objective financial knowledge was significantly different than moderate level. Taken together, these results suggest that, objective financial knowledge really do have an effect on subjective financial knowledge. Specifically, the results suggest that, individuals who are financially savvy, exhibits, higher subjective financial knowledge. That is, subjective perceptions are influenced by objective realities.

4. DISCUSSION AND CONCLUSION

The study conducted among individuals in Kerala, India reveals that objective financial knowledge of individuals has an effect on their subjective financial knowledge. That means, higher the objective financial knowledge, higher will be subjective financial knowledge and vice versa. The findings supports that subjective perceptions of individuals are influenced by objective realities. Prior studies (Asaad, 2015 and Parker et al., 2012) shows that, financial behavior is influenced by both objective and subjective financial knowledge. The current study reveals that there is an inter relationship between objective and subjective financial knowledge. ie., individuals who are financially savvy, exhibits higher levels of subjective financial knowledge. Existing literature (Xiao et al., 2014) states that, compared to objective financial knowledge subjective financial knowledge has strong impact on financial behavior of individuals. It should be noted that, current research clearly specifies, higher objective financial knowledge creates confidence in the mind of individuals about their awareness regarding financial concepts which in turn help them to take sound financial decisions and to engage in sound financial practices. The findings have implications for financial educators and policy makers. Financial education programs should focus on providing more objective financial knowledge, because individuals with high objective financial knowledge exhibits high subjective financial knowledge that ultimately leads to sound financial behavior.

Limitation should be acknowledged. It is only a cross sectional study. Longitudinal studies may give more clear evidence in the relationship between variables.

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