CHAPTER 2
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2.1 Introduction:-

Financial literacy is considered to be the most important factor for the better investment. Nowadays its priority is going on increasing. Based on financial literacy few Indian researchers have tried to study the financial literacy and investment inclination. Whereas on investment pattern, investment inclination and instruments used by the investors have studied by the Indian researchers.

2.2 Review of Literature:-

2.2.1 Domestic Scenario:-

Pallavi Seth, G N Patel and K.K. Krishnan. The purpose of this paper is to assess the level of financial literacy among people residing in Delhi and National Capital Region (NCR) who invest in different financial instruments, like Post Office Savings Scheme, Mutual Funds, Life Insurance, Stock market etc. The study indicated that the financial literacy of investors in Delhi and NCR was different for different financial instruments. Around 96% of them have savings account in the banks, as only around 30% had knowledge about National Savings Certificate & Public Provident Fund. While 98 % of the investors knew about Life Insurance, only about 45% preferred Life Insurance as the most effective financial instrument, which would be helpful at the time of contingencies. Around 92 % of the investors knew about Mutual Funds but only 24 % preferred them. Financial literacy is found to be affected by age, income and educational level of the individuals. High-income respondents had high financial literacy than lower income people. The study also revealed that people consider Life Insurance as the most effective financial instrument followed by Fixed Deposits in banks. It has also been found that most of the people relied on telecast in the T.V channels or advertisements put out in the newspapers and magazines to learn about financial products followed by "advice" from friends. But, while investing in share market, around 21% people relied on brokers.

Sumit Agarwal, Gene Amromin, Itzhak Ben-David, Souphala Chomsisengphe and Douglas D. Evanoff. In this study the researchers have report findings about financial literacy and financial planning behavior based on a financial advisory program in India. Researchers have evaluated survey responses to three standard questions previously used to measure financial literacy. The researchers evaluated the financial literacy of a select group of residents in India that participate in an on-line investment service provided by Yogi Financial Advisory Services. The findings on financial literacy are further related to self-report information on respondents' other investment activity.Researchers had find out that the participants are generally financially literate based on their responses to the survey questions. The researcher found a number of relationships between literacy and socioeconomic variables, notably; the probability of getting all the survey questions correct is higher for male respondents, and generally increases with education level and the aggressiveness of the investor.

Researcher has tried to collect the reviews done in domestic scenario. Reviews collected are on financial literacy, financial planning and investment avenues. Reviews help to justify the financial knowledge among investors and how does the investors react on investing in different avenues and the most preferred source of collecting information regarding investment and financial advisors.

2.2.2 International Scenario:-

Noel Capon, Gavan J. Fitzsimons and Rick Weingarten, *(1994)*. The respondents are highly likely to make future mutual fund investments; these are perceived as relatively low risk. Slightly over 60 per cent are in equity investments; and slightly under 40 per cent in fixed income. The predominant investment vehicle is a domestic US mutual fund; only 15 per cent of respondents invest in mutual funds with investment in foreign economies. Two sources of mutual fund purchases dominated for affluent investors – direct or through a broker; only 2.3 per cent of purchases were made from a banking institution. The most important information source overall was mutual fund rankings based on prior performance (4.25), relative importance were recommendations of business associates (2.80) and several forms of advertising: i.e. local newspapers (2.61), magazines (2.40) and national newspapers (2.18).

Neol Capon, Gavan J Fitsimons and Russ Alan Prince, *(1995)*. Had investigated the manner in which consumers make investment decisions for mutual funds. The researcher had found out that published performance rankings and investment performance track record were respectively the most important information source and selection criteria. Only 60.7% know whether their investments were in load or no load funds, no more than 25.0% were familiar with the investment management style any 27.7% were apprised of the domestic/international dimension of their investments.

Haiyan Chen and Ronald P Volpe, *(1998)*. The predictive knowledge among students of personal finance knowledge shows that improving college student's knowledge is important without adequate knowledge they are more likely to make mistakes in the real world. Overall conclusion is that college students are not knowledgeable about personal finance. The lack of education has resulted in serious financial illiteracy found in the American public due to the systematic lack of personal finance education in an education system.

Gordon J. Alexandera, Jonathan D. Jonesb, Peter J. Nigro, *(1998)*. The results show that the typical mutual fund investor surveyed is older, wealthier, and better educated than the average American. The survey results also suggest that more can be done to make mutual fund prospectuses more useful to investors, especially since over 40% of those surveyed stated that they never used the prospectus. Although broker and direct fund company purchasers are relatively more knowledgeable about the costs and risks of mutual fund investments than non-broker and non-direct fund company purchasers, it is likely that investors self-select into the various distribution channels. Ultimately, the goal of better educated investors can only be achieved by a concerted joint effort involving numerous parties, including plan sponsors, brokers, fund companies, and governmental regulatory agencies.

Michael S. Gutter, Jonathan J. Fox and Catherine P. Montalto, *(1999).*The sample for this study is 3,939 households, consisting of households with a Black or White household head and where the gender of the household head is reported. On average, Black households are larger than White households. Only 23% of Black households hold risky assets compared to 46% of White households. Black households report a lower willingness to take financial risks and have a shorter investment horizon compared to White households. A significantly higher proportion of Black households (60%) than White households (42%) report they are not willing to take any risk. The majority of Black households are in the lowest income quartile (57%) compared to less than one third of White households (32%). White households that are willing to take above average financial risk or substantial financial risk are more likely to own risky assets than otherwise similar households that are willing to take only average risk.

Maria Ward Otoo, (1999). This paper examined the relationship between movements in consumer sentiment and stock prices. An increase in stock prices aggregate sentiment because people are wealthier or because they use movements in stock prices as an indicator of future economic activity and potential economic growth.

Peggy D. Dwyer, James H. Gilkeson and John A, *(2001).* The researchers had used data from nearly 2000 mutual fund investors; the researchers found out that women's take less risk than men in their mutual fund investments. The researcher found that the observed difference in risk taking is significantly attenuated when we include a financial investment knowledge control variable in the regression model, suggesting that the gender effect found in previous studies that employ less specific knowledge controls may be biased upward.

Massimo Massa, Andrei Simonov, *(2002).* In their paper researcher came with the finding that investors react to prior gains/losses according to what postulated by the house money effect. Previous gains increase investor risk taking, while previous losses reduced it. Investor choice is mostly driven by the availability of information. Reliance on familiarity with a stock is a cheap way of acquiring information about it that fades away when better and more expensive information is provided.

John E. Grable and Ruth H. Lytton, *(2003).* This theory states that risk and return are positively linked, and that individual investors should determine their asset allocation, at least in part, on the basis of financial risk tolerance. In this study those who reported higher levels of risk tolerance did, indeed, hold more equity assets than others, while those with lower levels of risk tolerance held more fixed income securities and cash.

Alexander Niessen and Stefan Ruenzi, *(2006)* had tried to show that male and female fund managers are not identical. Firstly, women seem to take moderately less risky. Specifically, the researcher found that women take less unsystematic risk and less small firm risk, while overall return risk does not differ systematically. Woman follow significantly less extreme investment styles, as reflected by factor loadings closer to the average fund in their respective segment than those of male managers. Finally, male managers trade more actively, which is reflected in a significantly higher turnover ratio as compared to female managers. Overall, the researchers suggest findings on behavioral differences between male and female managers suggests that investors preferring moderate and stable investment styles should invest in female managed funds, while more daring investors interested in funds that take more active bets should choose male managed funds.

Marten Van Rooji, Annamaria Lusndi and Rob Alessie, *(2007).* In this paper the researcher has shown that lack of understanding of economics and finance is a significant deterrent to stock ownership. The different measures of financial knowledge have employed in their work, all show that lack of literacy payments prevents households from participating in the stock market. The results from this paper are that higher the financial literacy higher is the stock holding among respondents.

Richard Deaves, E. Theodore Veit Bhandari, John Cheney, *(2007)*. The focus of the study was to investigate the impact of the propensity to plan on savings and investment decisions. Planners are careful individuals who seek to understand the investment environment. This encourages them to acquire knowledge and become more sophisticated. Although most of the 236 survey respondents took full advantage of the employer's matching contributions, study found that the depth of participation (pension contributions as a percentage of salary) was positively influenced by a planning mindset. Additionally, such demographic attributes as gender, marital status, age, and salary mattered as well, with the one surprise being that men saved less. The propensity to plan also was shown to be positively correlated with risk tolerance, arguably because planners are more financially sophisticated and understanding of the fact that some risk-taking is appropriate in a pre-retirement portfolio. Risk taking was also shown to be positively associated with income and, somewhat surprisingly, negatively associated with age.

Jeff Domimtz, Angela A hung and Joanne K Yoong, *(2008)*. In their paper the researcher has designed and administrated a pair of mutual fund choice experiments to over 1000 survey respondents who participate in the RAND American Life Panel. Analysis sheds light on the question of how mutual fund investors respond to variation in fees in a hypothetical scenario in which fees should be obvious to the investor. Overall the researcher find out that respondents tends to not to minimize expected fees and are more averse to back end load fees than to front end loads. Differences in measured financial literacy predict differences in behavior, with lower rates of literacy among women accounting for differences in choices behavior by gender. It is also found out that financial literacy mediates individual responses to the presentation of information to enhance decision making.

Catherine C Eckel and Philip J Grossman, (2008). The researcher discovered that men were significantly more risk prone than women in their betting habits. The researcher report that, relative to men, women held a significantly greater share of their account balances in relatively low-risk fixed income investments and a significantly smaller share in higher-risk employer stock. Controlling for factors such as age, education, children, and home ownership, find that single women are significantly more risk averse than single men.

Married men and married women were less risk prone than their single counterparts (i.e., married men were less likely than single men to choose investment choice and married women were less likely than single women to choose investment choice Single women were less risk prone than single men (i.e., less likely to choose investment choice).

Sebastian Muller and Martin Weber, (2010), have assessed financial literacy. Researchers have asked certain questions to assess the effectiveness of the financial literacy. Relationship between financial behaviors of people depends and financial education has been assessed. The results suggest that the level of financial literacy is not related to the performance of the actively managed funds that our participants selected. Less knowledgeable fund customers mainly choose traditional distribution channels, implying that they seek assistance from a financial advisor who has an incentive to recommend actively managed funds. In contrast, fund customers with a higher degree of financial knowledge believe that they have some fund selection ability, more often select their funds independently, and rely more on internet channels, thus avoiding sales commissions.

Warren Bailey, Alok Kumar and David, *(2010)*. Using thousands of brokerage accounts of U.S. individual investors have shown that behavioral factors influence the decisions of individual investors to hold individual stocks as opposed to mutual funds, including passive index funds. Therefore investors with higher income, relatively higher educational level, and greater investment experience are more likely to use mutual funds and benefit from their choices. On the other hand, investors with strong behavioral biases tend to gravitate towards individual stocks and avoid low expense index funds.

Fabian Niebling, Steffen Meyer and Andreas Hackethal. This paper contributes to the growing body of literature on mutual fund purchasing decisions, smart investment decision making and household finance. Investors making smart investments are older, more experienced, wealthier and less overconfident. Investors who act smart and purchase mutual funds by chasing historical performance have more overall investment success.

Jasim Y.Al- Ajmi, The objective of this research is to provide further evidence on the validity of the relationship between a psychometrically derived measure of subjective risk tolerance and responses to questions on six demographic characteristics. To achieve this objective, a survey was used to collect the data. Several statistical procedures were used to investigate the effect of certain investors' socioeconomic factors on investor risk tolerance: sex, education, age, and wealth. The results, after controlling for nationality of the investors, show that, Men are less risk averse than women, Less educated investors are less likely to take risk, The effect of age on risk tolerance is complex in contrast to reports in earlier studies. Wealthy investors are more risk tolerant than the less-wealthy investors.

2.3 Conclusion:-

From the above reviews collected the researcher concludes that financial literacy is one of the important factors while investing in any investment avenue. Having good knowledge about finance and economics is the requirement among investors for the better management of their funds. Therefore knowledge of financial literacy helps in better investment. Fund customers with a higher degree of financial knowledge believe that they have some fund selection ability; more often select their funds independently. Hence, greater the financial literacy better is the investment and higher returns.