

FINANCIAL LITERACY AND ITS DETERMINANTS AMONG HOUSEHOLDS IN JIMMA ZONE

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Abstract

Financial literacy becomes a topical issue for academicians and policy makers, both in developed and developing countries. This might be because of the fact that there is low level of financial literacy prevailing across the world. To achieve the objective of the study, a quantitative research design and a cross sectional survey research approach was used. The research focused on the urban area of Jimma Zone by taking a sample of 173 households using multi-stage sampling. The result of multiple regression analysis showed that educational levels of the households have a significant and positive effect on their level of financial literacy. That is, as the educational level of households increase, their financial literacy levels will also increase. But the remaining three predictors i.e. Age; Gender and financial literacy training from microfinance institutions have no significant effect on the financial literacy level of the households.

Keywords: *Financial literacy, households, Jimma Zone*

1. Background of the Study

Financial literacy becomes a topical issue in academics and policy circles, both in developed and developing countries. This is because of the fact that the low level of financial literacy prevailing across the world resulted in suboptimal personal financial decisions having adverse consequences on the individual/households, financial sector and the entire economy. The Organization for Economic Cooperation and Development (OECD) defined financial literacy as,

“[a] combination of awareness, knowledge, skill, attitude and behavior necessary to make sound financial decisions and ultimately achieve individual financial wellbeing.”¹

The desire for enhancing financial literacy has led to financial education interventions in various countries. And studies on the role of financial education interventions both in developed and developing countries provided suggestive evidences. But those studies are not conclusive, whether financial education improved financial literacy and financial behavior of individuals, and in turn enhanced socio economic welfare. Most of the financial education programs are motivated by the results of financial literacy surveys conducted in developed countries (Zu & Xia, 2012). In Ethiopian context, few have been known about the level of financial literacy and its determinants. Hence, policy makers and practitioners in the finance sector might face difficulty of crafting appropriate financial literacy and financial education intervention policy to leverage financial inclusion and its outcomes to the poor.

¹Messy, F. and C. Monticone (2012), “The Status of Financial Education in Africa”, OECD Working Papers on Finance, Insurance and Private Pensions, No. 25, OECD Publishing, available at <http://dx.doi.org/10.1787/5k94cqx90wl-en>

Although it was commonly understood that the poor and low-income people would benefit from the burgeoning access to formal financial services resulted from financial inclusion efforts, lack of financial literacy is found to limit the envisaged outcomes (Center for Financial Inclusion, 2013). Thus, financial literacy/capability intervention is suggested to be part of financial inclusion. The concept of financial inclusion has been shifting from a mere expansion of access to financial service to beneficial use of financial service and sustainable financial outcomes. Contemporary concept of Financial Inclusion is broader and include three integrated elements, namely: (1) improving access to basic financial services, (2) developing suitable products/services to meet the current and potential demand of the disadvantaged groups, and (3) enhancing financial capability of clients to enable beneficial usage of existing and potential products (Center for Financial Inclusion, 2013). The purpose of financial literacy survey in a particular country is to provide input for designing targeted financial education interventions, to address identified lack of knowledge, skill, and attitude relevant to personal financial decision making. This research was aimed at measuring level of financial literacy of households, which are responsible to personal and household financial decisions, on one hand, and identify socio-economic and demographic correlates of financial literacy.

Assessing the level of financial literacy and its socio-demographic correlates in the context of a given country has paramount importance to identify a segment of community with a particular personal financial education need and other policy interventions. Nonetheless, similar efforts in developing and low income countries and specifically in Africa are scantily available. So far as our review efforts were concerned, there are few previous studies on financial literacy, its determinants, and its implication on financial inclusion in Ethiopia. Therefore, further research will add value to the practical and policy relevance of the existing literature. Taking into account the role of financial literacy to financial inclusion, poverty reduction, household wellbeing, financial sector development and stability of the entire economy, it is felt pertinent to examine the level of financial literacy across demographic and socio-economic characteristics of the households.

Though national or regional survey of financial literacy appeared to have a paramount importance, the current study delimits the geographical scope to Jimma Zone of Oromia Regional State, in Ethiopia. The study area is selected as it is appropriate to address community problems where our university is immediately responsible in light of its community based education Philosophy. The issue is less explored in Ethiopia and hence, it would be technically and economically feasible to conduct a study in specific area and scale it up in other areas with similar context to the study area.

2. Theoretical Background and Conceptual Framework

Financial literacy was conceptualized variably on different studies implemented both in developed (Houston, 2010) and developing countries (Fatoki & Oni, 2014) which limits opportunity of comparing findings and draws an overall inference. Thus, it deemed essential to first develop a theoretical framework to facilitate the measurement of financial literacy level and describe across socio economic and demographic characteristics of respondents, pertinent to the objective of the study. Based on review of theoretical literatures and previous studies on measurement of financial literacy, the framework first defines financial literacy construct and its dimensions, then discuss the measurement and interpretation issues in order to enhance the construct validity.

The way financial literacy connived by Microfinance opportunities (2005) as stated below emphasized on the potentials of financial literacy enhancements in improving personal financial decision making.

Financial literacy can be defined as knowledge of financial concepts and the skills and attitudes to translate this knowledge into behaviors that results in good financial outcomes. (Microfinance Opportunities, 2005)

According to Justine et. al. (2012)

As operationalized in the academic literature, financial literacy has taken on a variety of meanings; it has been used to refer to knowledge of financial products (e.g., what is a stock vs. a bond; the difference between a fixed vs. an adjustable rate of mortgage), knowledge of financial concepts (inflation, compounding, diversification, credit scores), having the mathematical skills or numeracy necessary for effective financial decision making, and being engaged in certain activities such as financial planning. The OECD on its recent document intended to measure financial literacy and financial inclusion at a global level, defined financial literacy as:

[a] combination of awareness, knowledge, skill, attitude and behavior necessary to make sound financial decisions and ultimately achieve individual financial wellbeing (Atkinson and Messy, 2012).

The OECD definition, aimed at ensuring standardized study framework, is commonly used on most recent studies, for the fact that it has to incorporate knowledge, skill and attitude components, which is consistent to evaluation and analysis of financial literacy measurement by Houston (2010) that suggested clarity of important aspects of knowledge, skill linked with behavior in personal finance. Financial literacy benefits people to be able to make optimal financial and economic decision including, saving, borrowing, investment as well as proper management of money (Capuano & Ramsey, 2011). Operationalization of the construct selected above shared a common feature in that all identified dimensions of financial literacy that can be linked with financial behavior: confidently using knowledge and skill in management of personal finance. Financial literacy is difficult construct to measure as it comprises different concepts, at times with varied connotation across various studies, not observable and easily measurable. The common approaches across previous studies is to use financial literacy quizzes, which are objective questions, aimed at measuring level of basic financial knowledge: interest, inflation, risk diversification, which are useful in personal financial decisions. The skill components are usually related to numeracy and measured by respondents' ability of computing simple and/or compound interest, and perform division and comparing different borrowing or saving options. Financial awareness is also measured following questions asking whether respondents do know various products/service options available in their respective financial land scape. According to Houston (2010), lack of standardized measurement limits the possibility of comparing financial literacy studies and use overall findings for their intended purpose of devising a financial literacy education policy and programs. Houston (2010) conceptualized the term financial literacy and suggested approaches for the purpose of measuring and interpreting results after a thorough review and analysis of studies that measured financial literacy from 1996 to 2008. He conceptualizes financial literacy to incorporate basics of personal finance that can be categorized under four domains to be measured by multiple items linking financial literacy and financial behavior. Accordingly, financial literacy embraced: (1) basic money management, (2) saving and investment, (3) borrowing, and (4) protection from risk. The Organization for Economic Cooperation and Development (OECD)-International Network on Financial Education (INFE) has also been working to standardize financial literacy measurement techniques to ensure comparative result across different countries to enhance policy relevance of studies. OECD (2009) framework for the development of financial literacy baseline survey pointed out four conceptual areas, showed on broad-range of surveys: (1) day-to-day money management; (2) financial planning; (3) choosing appropriate products and (4) financial knowledge and understandings are domains of financial literacy construct to be considered in survey instruments. The theoretical frameworks for financial literacy are developed in the context of high income and developed countries (Holzman, 2010). Thus, studies in developing countries could not be at ease to direct adoption; rather, Holzman (2010) suggested the need for careful adaption through consideration for unique socio-economic characteristics of developing countries. The proposed study will follow the commonly used and tested conception of financial literacy by OECD (2013) after efforts to tailor the concept in the context of Ethiopia. The unique features of developing countries, such as: informality of the market, poverty, low level of general educational attainment, high risk and lack of risk management mechanisms (Holzman, 2010; Messy and Monticone, 2012).

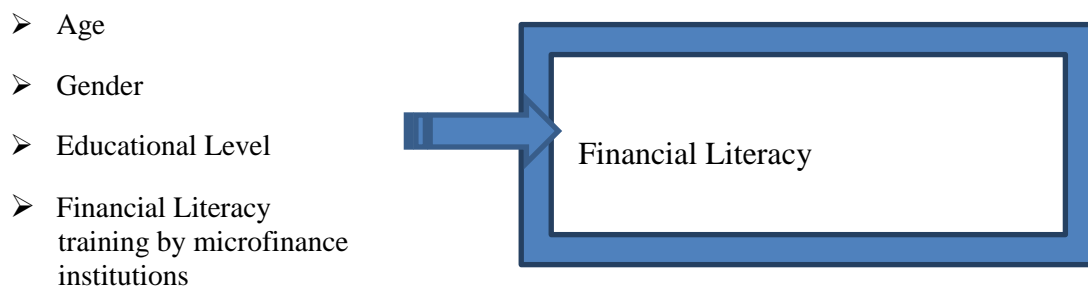


Figure: 1 Conceptual framework of financial literacy and its determinates, adopted and modified from 18th Annual Colloquium of Superannuation Researchers, UNSW, Sydney, Australia, 12-13 July 2010).

3. Research Methodology

The objective of this research was to measure and describe the level of financial literacy and its socio economic and demographic correlates. In addition, the research aimed in identifying groups in the population that requires particular type of financial literacy education intervention. The objective of the study calls for a quantitative research design and a cross sectional survey research approach.

3.1. Sampling Design

The study was conducted on financial literacy and its determinants of the households in Jimma Zone of Oromia regional State, Ethiopia. The research focused on the urban area of Jimma Zone because, there is a difference in financial literacy and financial behavior among rural and urban household operating at a various level of financial decision making scenario. Hence it is better to study both the urban and rural household separately, since the main purpose is to provide an input for designing a targeted financial literacy education. Therefore, the target population of the study was the heads of households in urban area of Jimma Zone. From the target population, a total of 173 sample households have taken using multi-stage sampling technique.

3.2. Method of Data Collection

Data in a survey can be collected using a self-administered or interview administered (face-to-face Interview) questionnaire. An interviewer administered questionnaire is a preferred method in financial literacy survey (OECD, 2009) for the fact that target population may include people with too low level of formal education. The questionnaire used for this study was adopted from OECD/INFE (2015) that is used for measuring financial literacy and financial inclusion. But modification has been made to the context of the study area. Therefore, to achieve the objective of the study; an interview administered questionnaire was used to collect the necessary data from the households. Before starting the field work, data collectors with adequate experience in household survey was recruited and trained. Then collection of data was undertaken by the data collectors under the supervision of investigator and co-investigators.

4. Data Analysis, Presentation and Interpretation

4.1. Demographic Data

Table 4.1.1: Gender of the respondents

	Frequency	Percent	Valid Percent
Male	108	62.4	62.4
Female	65	37.6	37.6
Total	173	100.0	100.0

Source: compiled from questionnaire, 2018

The above table indicated that 62.4% of the respondents were males and 37.6 % were females. Even though the above gender proportion indicates for the household heads, as per the CSA (2007), 50.29% of the total population of Jimma zone represents the male population and the remaining 49.71% was female.

Table 4.2: Age of the respondents

	Frequency	Percent	Valid Percent
20 – 24	5	2.9	2.9

25 – 29	6	3.5	3.5
30 – 34	40	23.1	23.1
35 – 39	78	45.1	45.1
40 – 44	33	19.1	19.1
45 – 49	9	5.2	5.2
50 and above	2	1.2	1.2
Total	173	100.0	100.0

Source: compiled from questionnaire, 2018

The above table 4.2 presents the age of the respondents. From the total respondents, 45.1% of them were found in the age interval of 35-39, 23.1% of the respondents were found in the age interval of 30 – 34 and 19.1% of the respondents were found in the age interval of 40 – 44. This table shows that 87.3% of the respondents fall in the age interval of 30 to 44, whereas 6.4% of the respondents were below the age of 30 and 6.4% were above the age of 44.

Table 4.3: Educational level of the respondents

	Frequency	Percent	Valid Percent
No formal education	13	7.5	7.5
Some primary school	8	4.6	4.6
Complete primary school	9	5.2	5.2
Some secondary school	22	12.7	12.7
Complete secondary school	51	29.5	29.5
Technical/vocational education	4	2.3	2.3
Diploma	36	20.8	20.8
Bachelor Degree	29	16.8	16.8
Masters and above	1	0.6	0.6
Total	173	100.0	100.0

Source: compiled from questionnaire, 2018

Table 4.3 shows the educational status of the respondents. This study was conducted in urban area of Jimma zone. From the total respondents, 29.5% of them have completed secondary school, 20.8% have diploma, 16.8% have first degree, 12.7% have some secondary school, and 7.5% have no formal education, 5.2% have completed primary school, 4.6% have some primary school, 2.3% were certified from technical and vocational education and 0.6% of the respondent have masters and above. From this table, we can understand that most of the respondents have attended formal education.

Table 4.4: Marital status of the respondents

	Frequency	Percent	Valid Percent
Married	137	79.2	79.2
Single	18	10.4	10.4
Widowed	2	1.2	1.2
Divorced	16	9.2	9.2

Total	173	100.0	100.0
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Source: compiled from questionnaire, 2018

Table 4.4 shows the marital status of the respondents. From the total respondents, 79.2% of them were married, 10.4% of the respondents were single, 9.2% of them were divorced and the remaining 1.2% of them was widowed.

Table 4.5: Existence of budget for the household

	Frequency	Percent	Valid Percent
Yes	75	43.4	43.4
No	98	56.6	56.6
Total	173	100.0	100.0

Source: compiled from questionnaire, 2018

The respondents were asked whether the household have a budget or not. For this study, a household budget is used to decide what share of the household income will be used for spending, saving, paying bills or others. The above table indicates that from the total respondents, 56.6% of the respondent said that there is no budget for their household whereas the remaining 43.4% of the respondent responded that there is a budget for their household.

Table 4.6: Respondents ability to cover major expenses

	Frequency	Percent	Valid Percent
Yes	95	54.9	54.9
No	78	45.1	45.1
Total	173	100.0	100.0

Source: compiled from questionnaire, 2018

The respondents were asked if they personally faced a major expense today equivalent to their own monthly income and would be able to pay it without borrowing the money or asking family or friends to help. Based on their response, 54.9% of the respondents said that if they faced major expenses equivalent to their monthly expenses, they have the ability to cover this expenses without borrowing money or asking family or friends for help. This shows that 54.9% of the respondents have saved money at least equivalent to their monthly income. 45.1% of the respondents said that if they faced major expenses equivalent to their monthly income, they don't have the ability to cover this expenses without borrowing money or asking family or friends for help. This shows that those respondents have no saved money or their saving is less than their monthly income.

4.2. Financial Behavior and Attitudes of the respondents

		1	2	3	4	5	Mean	Std. dev.
A	Before I buy something I carefully consider whether I can afford it	148 (85.5)	17 (9.8)	2 (1.2)	5 (2.9)	1 (0.6)	1.23	.668
B	I tend to live for today and let tomorrow take care of itself	1 (0.6)	16 (9.2)	4 (2.3)	77 (44.5)	75 (43.4)	4.21	.917
C	I find it more satisfying to spend money than to save it for the long term	3 (1.7)	41 (23.7)	8 (4.6)	87 (50.3)	34 (19.7)	3.62	1.101

D	I pay my bills on time	70 (40.5)	89 (51.4)	4 (2.3)	10 (5.8)		1.73	.769
E	I am prepared to risk some of my own money when saving or making an investment	29 (16.8)	8 (51.4)	17 (9.8)	36 (20.8)	2 (1.2)	2.38	1.031
F	I keep a close personal watch on my financial affairs	29 (16.8)	111 (64.2)	11 (6.4)	22 (12.7)		2.15	.849
G	I set long term financial goals and strive to achieve them	24 (13.9)	105 (60.7)	7 (4)	36 (20.8)	1 (0.6)	2.34	.978
H	Money is there to be spent	3 (1.7)	49 (28.3)	51 (29.5)	64 (37)	6 (3.5)	3.12	.923
I	My financial situation limits my ability to do the things that are important to me	22 (12.7)	94 (54.3)	3 (1.7)	31 (17.9)	23 (13.3)	2.65	1.284
J	I tend to worry about paying my normal living expenses	9 (5.2)	29 (16.8)	3 (1.7)	72 (41.6)	60 (34.7)	3.84	1.219
K	I have too much debt right now	1 (0.6)	24 (13.9)	4 (2.3)	42 (24.3)	102 (59.0)	4.27	1.074
L	I am satisfied with my present financial situation	10 (5.8)	43 (24.9)	8 (4.6)	71 (41.0)	41 (23.7)	3.52	1.256

Source: compiled from questionnaire, 2018

The financial attitudes of the respondents were evaluated by using likert scale (1=Totally Agree, 2=Agree, 3=Don't Know, 4=Disagree and 5=Totally Disagree) questions. The above table shows the financial attitude and behavior of the respondents. From the total respondents, 95.3% of them carefully consider whether they can afford it or not before they buy something with the mean score of 1.23 and standard deviation of 0.668. Those are respondents who will critically consider their financial ability before going for shopping.

87.9% of the respondents of the respondents were against the idea of tending to live for today and letting tomorrow to take care for itself. Their mean score of 4.21 and standard deviation of 0.917 shows their tendency to the disagreement with the idea of living only for today.

There are individuals who find it more satisfying to spend money than to save it for the long term and have no patience in building up cash balance for the long term. From the total respondents, 25.4% of them were satisfied in spending money today than saving it for the long term. 70% of the respondents were against the idea of being satisfied in spending than saving it for the long term.

In many developing countries specifically in our country, payment of bills on time become a problem especially payment of bills made to the government like tax, water and electric bills. From the total respondents, almost 92% of the respondents described their agreement in paying bills on time. This is also shown with the mean score of 1.73 and standard deviation of 0.769 showing the tendency of the respondents to the agreement of making bill payment on time.

Respondents were asked if they were prepared to risk some of their money when saving or making an investment to evaluate their attitude towards accepting a risk. From the total respondents, 68.2% of them believe that they were prepared to accept a risk when saving or making an investment and those are considered to be risk takers. 22% of the respondents were not ready to accept a risk when saving or making an investment and those respondents can be considered as risk averse.

Financially successful individuals will keep a close personal watch on their financial affairs and controls the incoming and outgoing money appropriately. 81% of the respondents will keep a close personal watch on their financial affairs and the remaining respondents were not. The mean score of 2.15 and standard deviation of 0.849 shows that many respondents have a tendency of agreeing in keeping a close personal watch on their financial affairs.

Most of the time extravagant individuals will say that money is there to be spent. Respondents were asked regarding the extent to which they will agree or disagree to the idea. From the total respondents, 30% of them will agree with the saying "Money is there to be spent". Those respondents were susceptible to financial difficulties as they are ready

to spend if they have money. Whereas 40.5% of the respondents disagree with the saying “Money is there to be spent”. Those respondents were prudent who will spend only for their basic needs.

From the total respondents, 67% of them responded that their financial situation limits their ability to do the things that are important to them. Whereas 31.2% of the respondents disagree with this view and responded that their financial situation will not limits their ability to do the things that are important to them.

Respondents were asked if they are worrying in covering their normal living expenses. From the total respondents, 76.3% of them are not worrying about paying their normal living expenses whereas 22% of the respondents were tend to worry about paying their normal living expenses. 83.3% of the respondents have no too much debt right now and 14.5% of them have too much debt right now.

Finally respondents were asked if they are satisfied with their present financial situation. From the total of them, 30.7% of the respondents confirmed that they are satisfied with their current financial situation. Those respondents might be who are able to manage their financial matters appropriately. Whereas 64.7% of the respondents were not satisfied with their current financial situations.

4.3. Result of Regression Analysis

Model Summary^c

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.476 ^a	.226	.222	1.0007633	
2	.485 ^b	.235	.217	1.0038217	1.650

a. Predictors: (Constant), Educational level

b. Predictors: (Constant), Educational level, Gender, Age, financial training

c. Dependent Variable: Financial literacy Test Score

Under the column labeled R was the values of the multiple correlation coefficients between the predictors (gender, age, educational level and financial literacy training) and the outcome (financial literacy test score). Here we have used hierarchical multiple regression analysis. Under the first model, only educational level was used as a predictor. Under the second model, Gender, Age, Educational level and financial literacy training were used as a predictor. When only educational level is used as a predictor, this is the simple correlation between the level of education and the financial literacy with the correlation coefficient of 0.476. But when the other three predictors were also considered, the correlation coefficient between the predictors and the dependent variable become 0.485 showing the addition of the three predictors (gender, age, educational level and financial literacy training) to have very slight effect on the first model.

The next column gives us a value of R square, which shows a measure of how much of the variability in the outcome (dependent variable) is accounted for by the predictors. For the first model its value is .226, which means that educational level accounts for 22.6% of the variation in the level of financial literacy. However, when the other three predictors are included as well (model 2), this value increases to .235 or 23.5% of the variance in financial literacy level. Therefore, if education accounts for 22.6%, we can tell that gender, age, and financial literacy training account only for additional 0.9%. So, the inclusion of the three new predictors hasn't explained the variation in in financial literacy level.

ANOVA^a

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	50.126	1	50.126	50.050	.000 ^b
	Residual	171.261	171	1.002		
	Total	221.387	172			
2	Regression	52.101	4	13.025	12.926	.000 ^c

Residual	169.287	168	1.008		
Total	221.387	172			

a. Dependent Variable: Financial literacy Test Score

b. Predictors: (Constant), Educational level

c. Predictors: (Constant), Educational level, Gender, financial training, Age

ANOVA tests whether the model is significantly better at predicting the outcome than using the mean as a 'best guess'. Specifically, the F-ratio represents the ratio of the improvement in prediction that results from fitting the model, relative to the inaccuracy that still exists in the model (mean).

The F-ratio is calculated by dividing the average improvement in prediction by the model (MSM) by the average difference between the model and the observed data (MSR). If the improvement due to fitting the regression model is much greater than the inaccuracy within the model then the value of F will be greater than 1 and SPSS calculates the exact probability of obtaining the value of F by chance. For the initial model the F-ratio is 50.050, which is very unlikely to have happened by chance ($p < .001$). For the second model the value of F is 12.926 which is significant at $p < .001$. As it was seen the F ratio is lower for the second model because as we have explained under the model summary, the addition of the three predictors to the first model hasn't explained the variation in the outcome. We can interpret these results as meaning that the initial model significantly improved our ability to predict the outcome variable, but that the new model (with the extra predictors) was not good in explaining variation in the outcome (even though the F-ratio is significant) as compared to the first one.

Coefficients^a

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	4.774	.208		22.934	.000
	Educational level	.259	.037	.476	7.075	.000
2	(Constant)	5.087	.712		7.140	.000
	Educational level	.257	.040	.472	6.445	.000
	Gender	-.131	.159	-.056	-.827	.409
	Age	.044	.076	.041	.575	.566
	financial training program	-.186	.203	-.063	-.913	.362

a. Dependent Variable: Financial literacy Test Score

It is easiest to conceptualize the t-tests as measures of whether the predictor is making a significant contribution to the model. Therefore, if the t-test associated with a b-value is significant (if the value in the column labeled Sig. is less than .05) then the predictor is making a significant contribution to the model. The smaller the value of significance level and the larger t-value, the greater the contribution of that predictor. For this model, educational level is a significant predictor of the financial literacy level (t-value = 6.445 and $p < .001$). Gender, age and financial training from microfinance institutions are insignificant predictor of the level of financial literacy.

The first part of the above table gives us the estimates for these b-values and these values indicate the individual contribution of each predictor to the model. Here the b-values tell us about the relationship between financial literacy and each predictor. If the value is positive we can tell that there is a positive relationship between the predictor and the outcome, whereas a negative coefficient represents a negative relationship. For this data, only the educational level has a positive significant effect ($p < .001$) on the level of financial literacy with the b- value of 0.257. This value indicates that as educational level increases by one unit, financial literacy level increase by 0.257 units. As per this result, the remaining three predictors (age, gender and financial training from microfinance institutions) have no significant effect on the level of financial literacy.

5. Conclusion

To conclude, we can observe that, from the independent variables considered by the study, only the educational level has a positive significant effect ($p < .001$) on the level of financial literacy with the beta value of 0.257. Therefore, educational level of the respondents was proven to have a significant positive effect on the financial literacy level of the respondents. This value shows that as educational level increases by one unit, their financial literacy level increases by 0.257 units. This finding is the same with Behrooz G., (2015); Bhushan P. and Medurey Y., (2013). The remaining three predictors (age, gender and financial training from microfinance institutions) have no significant effect on the level of financial literacy.

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