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A Theoretical Study of Financial Literacy with Financial Analysis

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Abstract

The purpose of this paper is to analyse a fast-developing collection of economic research on financial literacy. We begin with a review of theoretical research that portrays financial knowledge as a sort of human capital investment. Indigenizing financial information has significant ramifications for welfare and programmes aimed at improving financial literacy in the general population. Then, using data from recent surveys, we determine how much (or how little) people know about money and identify the population segments with the least financial knowledge.

Keywords: *Financial Analysis, Activity, Profitability, Liquidity*

Introduction

In something like an international financial system characterized by persistent unpredictability, firms are challenged with adverse economic conditions. Companies are constantly exposed to changing environmental conditions as well as persistent pressure from rivals who attempt to enhance the performance of their commodities and operations on a continuous basis in order to stand out from the competition. This knowledge has a detrimental impact on the overall effectiveness of the firm in question.

The following are the components of financial literacy:

Financial Knowledge: Insight and knowledge of economic concepts and systems. People with financial expertise can better understand financial concepts and procedures, as well as apply what they have learned to solve financial challenges (Denis & Osobov, 2008; Ahmad, 2020). It is the ability to manage money in a variety of ways, including keeping track of day-

to-day financial concerns in the market and making the best decisions for "financial literate" people's requirements.

Financial Skills: Using economic knowledge to make decisions in the real world (analyzes, evaluations, choices). It is the capacity to apply information and understanding to solve a financial problem and turn it into a benefit and opportunity to one's advantage.

Financial Attitudes: Motivation and willingness to apply financial knowledge and abilities in a variety of scenarios. Individual characteristics that manifest as tendencies toward a financial practice or behaviour are referred to as tendencies. They demonstrate a person's proclivity or probability to engage in a particular action.

Financial Behaviour: Activity on the financial market in various scenarios.

Financial Literacy: Financial knowledge and understanding about the financial concepts and procedures as well as the use of this understanding to solve financial problems.

Financial Skills: The ability to use knowledge and understanding to manage an expected or an unpredictable situation in order to solve a financial problem and convert it to a benefit and opportunity to one’s advantage.

The purpose of this paper is to analyse a fast-developing collection of economic research on financial literacy. We begin with a review of theoretical research that portrays financial knowledge as a sort of human capital investment. Indigenizing financial information has significant ramifications for welfare and programs aimed at improving financial literacy in the general population. Then, using data from recent surveys, we determine how much (or how little) people know about money and identify the population segments with the least financial knowledge.

The impact of financial literacy on economic decision-making in India and internationally is then investigated. While the research is still in its early stages, judgments concerning the causes and implications of financial illiteracy, as well as what works to close the gaps, can be reached. A concluding section discusses what further research needs to be done for scholars to better inform theoretical and empirical models, as well as public policy.

Illiterate persons are fully barred from financial institutions' products and services during the limited financial access stages. The second stage is the extension of financial access, in which financial literacy acts as a moderating element. The teaching of critical financial information to the uneducated in rural parts of the country is aided by socioeconomic status. After attaining adequate financial knowledge pertaining to financial operations and programs, such persons would be included in the financial ensures that an organization (Kania, 2005). Finally, the premise of increasing rural financial involvement benefits domestic development, as well as the country's economy in general, has a positive influence on the development of microfinance activities (Sana, Poddar & Paul, 2020; Sahela et al., 2021). Individuals with at minimum a way to make money or income should be included in the financial systems.

Relevance of the Study

Throughout in the relatively limited access phases, uneducated people are completely excluded from financial institution goods and services. The second step involves broadening financial access, with financial knowledge serving as a moderating factor. The teaching of critical financial information to the uneducated in rural regions is aided by financial literacy. After attaining adequate financial awareness linked to financial features and facilities, such persons are included on the financial inclusion group. Eventually, the premise of increasing micro - finance involvement benefits the rural economy, and the country's broader economy does have a positive influence on the development of rural finance. All individuals having a source of revenue or revenue will indeed be accounted for in the monetary institutions.

Objective of the Study

The purpose of the article would be to provide rudimentary understanding concerning ex-post economic information and, as a necessary consequence, to monitor the appropriateness of a business concern in aspects of activity, liquidity, profitability, and indebtedness in addition to exploring internal strengths on which the entrepreneurial particular topic could perhaps make decisions based. It also seeks to spot defects and threats that might lead to problems, and then makes it clear ways to improve the based on the financial assessment methodology for the company issue based on the results.

Research Methodology

The study focused on the theoretical concept of financial literacy. So, collected kind of conceptual theory from secondary sources like books, journal and website etc.

Financial Analysis

The cornerstone of a company's economic performance analysis is a financial situation analysis, which generally leads to key areas and results including overall effectiveness, reliability, manufacturing capacity optimization, supplementary management, and so on. The financial study revealed a company's flaws and strengths, acts as a "fitness" clinical instrument and provides crucial information to management and investors.

Cost benefit analysis is defined as a method of assessing a company's financial management in which data is graded, aggregated, and compared to one another. Furthermore, the connections between them are assessed in order to establish a causal relationship between the data and its progression. This increases the explanatory capability of data processing as well as its informative value. As a consequence, it focuses on determining difficulties, strengths, weaknesses, and, most importantly, the value capabilities of the firm. The financial analysis supplies us with data that helps us to make judgments about something like a company's general administration and financial situation.

The examination of the company's financial state is declared by the system of financial indicators, which must be in order and organised to reflect all of the essential components of the financial position. As a result, financial ratio indicators are used to depict the situation. The ratio indicators allow for a comparison of the business to other businesses or industry

indicators. The total of the ratio indicators we'll show can be viewed as the sum of representative indicators. In particular, they will be the most extensively used indicators of financial status features. However, hundreds of indications are utilised in conjunction with the practical application, and it is impossible to list them all.

Indeed, the use of a variety of basic indicators that may be related to the objectives depending on various areas of management oversight and the financial wellbeing of the firm has shown to be beneficial. Debt, liquidity, profitability, activity, capital market indicators, and so on are examples of these types of indicators. Based on the objectives outlined in this piece, we'll look through the profitability and liquidity ratio indicators in further depth (Adil, Zafar & Yaseen, 2011; Jahan & Alrajawy, 2020).

Literature Review and Discussion

Activity Ratio

Activity ratios are a type of financial statistic that is used to evaluate a company's operational effectiveness. The term can refer to a number of different ratios that determine how efficiently a company spends its money and assets. Activity ratios are crucial in a horizontal statement analysis for analysing how a firm's performance is trending over time or how it compares to its competitors in similar business research. Operating efficiency ratios or turnover ratios are other names for them.

The following constitute the three varieties of activity proportions:

1. Working Capital: The gap separating current assets and current liabilities is described as working capital, generally recognized as operational capital. Working capital is a measure of a company's capacity to pay current immediate liabilities. Working capital must be favorable; nonetheless, working capital must not be unduly large to prevent tying network bandwidth that may be used somewhere.

Working capital is made up of three fundamental precepts:

1. Receivables
2. Inventory
3. Payables

Receivables: A company's ability to manage credit sales and convert account receivables into cash is measured by its accounts receivable turnover.

Revenue / Average Receivables = Receivables Turnover

A high receivables turnover indicates that a firm can swiftly convert its receivables into cash, whereas a low receivables turnover indicates that a company cannot convert its receivables as quickly as it should (Svensson & Thorén, 2015; Vivekanandam, 2020).

The amount of days it takes to convert credit sales into cash is measured by Days of Sales Outstanding (DSO).

Number of Days in Period / Receivables Turnover = Days of Sales Outstanding

Inventory: Inventory turnover is a metric that indicates how well a firm can manage its inventory.

Inventory Turnover = Average Inventory / Cost of Goods Sold

A low inventory turnover ratio indicates that inventory is moving too slowly and is causing capital to be tied up. A corporation with a high inventory turnover ratio, on the other hand, can move goods quickly; but, if the inventory turnover is too high, it might result in shortages and lost revenues.

The number of days it takes to sell an inventory balance is measured by Days of Inventory on Hand (DOH).

Number of Days in Period / Inventory Turnover = Days of Inventory on Hand

Payables: The amount of time it takes a corporation to pay off its accounts due to creditors is referred to as payables turnover.

Cost of Goods Sold / Average Payables = Payables Turnover

Low payables turnover might signal either liberal credit conditions or a company's incapacity to pay its creditors. A high payables turnover might signal that a firm is paying creditors too quickly or that it can benefit from early payment reductions.

The number of days it takes to pay off creditors is measured by Days of Payables Outstanding (DPO).

Number of Days in Period / Payables Turnover = Days of Payables Outstanding

Cash Conversion Cycle

The cash conversion cycle, as previously stated, is an important indicator for measuring how effectively a firm can turn its inventories into cash. Companies seek to reduce their cash conversion cycle as much as feasible so that they may get cash from inventory sales as soon as possible (Hellström & Inagambaev, 2012; Milic & Bhaumik, 2021). The statistic measures how effectively a company's working capital and operating assets are used.

DSO + DIH – DPO = Cash Conversion Cycle

Fixed Assets

Fixed assets are quasi assets that are physical long-term assets that seem to be non-operating, which means they are not utilised in a corporation's day-to-day operations. Fixed assets such as furniture, machinery, cars, buildings, and land are examples of fixed assets that are expected to provide an economic benefit in the future.

Fixed Assets are assets that cannot be changed. The efficiency with which a corporation uses its fixed assets is measured by turnover. A high ratio suggests that a company's Capital Expenditures (CapEx) may need to be increased, while a low ratio implies that too much capital is locked up in fixed assets.

Revenue / Average Net Fixed Assets = Fixed Asset Turnover

Total Assets

All operational and non-operating assets included on a company's balance sheet are referred to as total assets (current and long-term). Entire asset turnover is a metric that measures how efficiently a company utilises its total assets.

A high ratio indicates that a company is either extremely efficient with its overall assets or has a small number of assets, to begin with. A low ratio indicates that assets are tying up too much money and are not being used to produce revenue effectively.

Assets in Total Revenue / Average Total Assets = Turnover

Profitability Ratio

Profitability is the most important factor for any company. Profitability ratios are one of the most commonly utilised financial ratio analysis methods. They're utilised to calculate the company's bottom line for its executives and its return on equity for its shareholders. Measures of profitability are crucial to both managers and shareholders of businesses. In order to drive the firm in the right direction, management needs to have a gauge of profitability. If a company's stock has been purchased by outside investors, the company's management must demonstrate profitability to those equity investors (Rehman & Takumi, 2012).

Profitability ratios, as stated and shown below, show a company's total efficiency in utilising its assets and performance at the end of each quarter or year. Profitability ratios are divided into two categories: margin ratios and return ratios. 1 Margin ratios show a company's capacity to transform sales dollars into profits at various levels of assessment. Ratios that illustrate returns are used to assess a company's overall efficiency in generating returns for its shareholders. Let's look at the several forms of profitability ratios.

Figure 1: Several Forms of Profitability Ratios

Liquidity Ratio

A liquidity ratio is a financial metric for determining a company's ability to satisfy short-term borrowing obligations. The statistic is used to see if a company's current assets, also known as liquid assets, are sufficient to pay its current liabilities.

The three most often used liquidity ratios are the current ratio, quick ratio, and cash ratio. The quantity of current obligations is put in the denominator of each liquidity the numerator is the quantity of liquid assets, whereas the denominator is the amount of liquid assets.

Because of the nature of the ratio, which places assets on top and liabilities on the bottom, ratios above 1.0 are preferred. A current asset-to-current-liability ratio of one implies that a company's current assets are adequate to cover all of its current obligations. A ratio of less than one (for example, 0.75) shows that a company is now unable to pay its obligations.

A ratio larger than one (e.g., 2.0) shows that a company can meet its current obligations. In fact, a ratio of 2.0 suggests that a company's current obligations are likely to be covered twice as much as its current assets. They can cover their current liabilities three times more if the ratio is 3.0, and so on.

Types of Liquidity Ratios

Current Assets / Current Liabilities = Current Ratio

The current ratio is the simplest of the liquidity ratios to calculate and analyse. Everyone can see the current assets and current liabilities line items on a company's balance sheet right away. Divide current assets by current liabilities to get the current ratio.

Quick Ratio: (Cash + Accounts Receivables + Marketable Securities) / Current Liabilities = Quick Ratio

When it comes to determining liquidity, the fast ratio is more severe than the current ratio. The numerator of both is current assets, while the denominator is current liabilities.

In contrast, the fast ratio just looks at specific current assets. Among the most liquid assets assessed are cash, accounts receivables, and marketable securities. Because current assets are less liquid, such as inventories and prepaid costs, they are omitted. As a result, the quick ratio provides a better gauge of a company's ability to satisfy short-term obligations.

Cash Ratio: (Cash + Marketable Securities) / Current Liabilities = Cash Ratio

The liquidity test is pushed even farther by the cash ratio. This ratio only takes into account a company's most liquid assets, such as cash and marketable securities. They are the assets that a company may employ to meet short-term obligations the fastest.

Depending on how rigorous the liquidity rules are, the current ratio, fast ratio, and cash ratio can be characterised as easy, medium, or hard.

Conclusion

Financial analysis is a crucial instrument to enhance the decision-making of various stakeholder groups in the current chaotic competitive climate. It also gives a picture or feedback on the overall state of the company issue and its progress, as well as the state of individual operation sections. This research can uncover the aspects that have had the most impact on the company issue and have resulted in unfavourable outcomes.

Using financial-economic analysis prediction models, the firm subject can forecast its future development and the potential of bankruptcy.

One of the advantages of this piece is the financial-economic study focused on the firm subject's ratio indicators of activity, profitability, liquidity, and indebtedness. The relevant methods for reducing vulnerabilities revealed through the financial analysis presented in this article are based on real-world experience with the business issue.

Conflict of Interest

The authors declared that they have no conflict of interest.

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