

## ► Policy Brief

# Role of Financial and Economic Literacy in Improving Youth Entrepreneurship

## Background

Financial literacy is a combination of awareness, knowledge, skills and behaviors that a potential entrepreneur should have in order to make effective financial decisions to start, run and grow their business. Potential entrepreneurs need a variety of skills including: skills in developing long-term financial strategy and business prospects; skills to understand financial instruments and changes in economic conditions; as well as financial management skills, people skills and sector-specific skills. Successful growth and development of an enterprise depend on both demand and supply side factors.

Understanding financial competencies that the entrepreneurs need is the first step towards developing financial literacy at a higher level.

This policy brief has been prepared incorporating insights from the policy dialogue held in Colombo on the 20<sup>th</sup> of January 2023, under the theme of “**Role of Financial and Economic Literacy in Improving Youth Entrepreneurship**”. This was the fourth of a series of policy dialogues organized by the [Ceylon Chamber of Commerce](#) in association with the [Central Bank of Sri Lanka](#), under the aegis of the [South Asia Leadership in Entrepreneurship](#) (SALE) Program.

The SALE Program is implemented in Sri Lanka and Nepal, by the [International Labour Organization](#), with the financial assistance of the United States Department of State. The main objective of SALE is to promote youth entrepreneurship, by facilitating a change in the entrepreneurial ecosystem and encouraging youth transition into the entrepreneurial world.

## Financial and Economic Literacy in Sri Lanka

The [Financial Literacy Survey](#) conducted by the Central Bank of Sri Lanka (CBSL) in 2021, reported that 57.9% of the adults are financially literate, whereas 93% of Sri Lankans can understand printed text. The gender gap in the financial literacy rates of males and females was 5.9%. The survey findings reveal that young adults are more financially literate than the elderly population. Individuals who use digital finance services and devices exhibit higher levels of financial literacy.

Besides financial literacy, economic literacy is another important concept, which could have a large impact on the behavior and performance of an entrepreneur and eventually impact the country's economy as a whole. Financial and economic education enables entrepreneurs to access and engage with financial services in an effective way.

The [National Financial Inclusion Strategy \(NFIS\)](#), led by the CBSL in collaboration with multiple entities, is aiming to promote financial inclusion in the country. An important initiative under NFIS is to develop a roadmap for financial literacy and capacity building with the collaboration of licensed banks, ministries and agencies. The objective is to empower Sri Lankans to greater financial inclusion with financial skills and knowledge.

## Topics Explored

Against this backdrop, the policy dialogue explored the following sub-topics:

1. Financial Education for all
2. Space for Practice/Skill
3. Enhancing Consumer Protection and Security
4. Transforming from informality to formality
5. Institutional capacity building to enhance knowledge of entrepreneurs
6. Innovation in financial markets
7. Community-based awareness for Entrepreneurial Culture

## Macro Issues and Concerns

### Micro, Small and Medium Enterprises

The MSME sector makes a significant contribution to the economy, by way of a major source of employment and output. MSMEs' strengths are multidimensional, especially the ability to expand value chains, increasing competition, encouraging innovative ideas and embracing technological advancements. Smaller businesses are more flexible and able to overcome challenges, thus improve economic resilience and entrepreneurial skills in human capital.

During the COVID-19 period and consequent economic crisis, many MSMEs faced difficulties in accessing formal financial systems, new technologies and global and local value chains.

## **Financial Literacy**

A considerable proportion of people do not have a good understanding of financial instruments and regulations, owing to the lack of education and training on financial and economic literacy and discipline. This is worsen by the complex terminology being used in standard materials and also in translations into local languages.

Even in entrepreneurship skills development programs, financial literacy has not been considered as a major component, though there is a high focus on providing training on product development, certification and marketing.

A majority of female entrepreneurs have home-based businesses, and they often lack skills and knowledge of financial concepts, such as budgeting and profit management, and they have less access to understanding the financial and economic systems and support schemes.

## **Financial Record Keeping**

Sri Lankan's are deemed to lack the appetite to record daily transactions. Especially, youth entrepreneurs lack financial discipline and do not maintain the financial records. Although financial record keeping is taught in Accountancy, from secondary schools to university level, the traditional teaching approach lacks "learning by doing" methods that make students understand the practicality.

Importance of maintaining accurate records as to entail legitimacy to the business and operations and also to provide evidence in applying for a bank loan is often disregarded.

A main challenge identified in Sri Lanka was focusing only on traditional methods of utilising financial/ numerical skills, which needs to explore how such knowledge can be applied in businesses.

## **Institutional Coordination**

The multiplicity of public and private institutions involved in entrepreneurship development and complexity in their overlapping mandates, make it rather difficult to coordinate and synergize. Absence of a systematic information base of ecosystem players and what they deliver creates numerous overlapping as well as unattended pockets in serving the potential enterprises and aspiring entrepreneurs. Identifying the specific requirements of such enterprises and individuals, including the need of strengthening their financial and economic literacy would require developing a centralized knowledge hub.

## **Community-based engagement**

Lack of mechanisms to make the general public financially literate and community-based organizations be engaged in such awareness creation hinders creating an entrepreneurial culture and also allows space for non-compliance with business

laws and regulations, whereby result in consequent implications that can even hamper business continuity.

Many entrepreneurship training programs do not contain follow-up and continued assistance until the start-ups become resilient and well established, whereas the forum found the untapped opportunity of capacitating the community-based organizations to devise such post-training support systems.

### **Consumer Protection and Security**

Numerous financial frauds and scams are taking place due to lapses in financial laws and regulations as well as in enforcement and creating public awareness, which adversely affects to the vulnerable groups such as youth, women, rural and lower or lower-middle income groups.

The dialogue observed the inadequacy of laws on credit side, whereas many laws and regulations are introduced to control taking deposits from people. This creates ample space for the financial institutions as well as non-regulated market players to operate various financial schemes.

Imposing laws and regulations alone would not resolve the present multifactorial challenges, including the irresponsible behaviour of people who are willingly involve in unauthorised financial schemes, seeking 'quick gains' and eventually trap in scams.

Many Sri Lankan migrant workers often get victimised by the financial scams and black-market schemes in transferring and investing their earnings, primarily due to the lack of financial literacy and in absence of social protection schemes for them.

On the other side, conservative and rigid foreign exchange regulations obstruct inflow of remittances and earnings of foreign trade such as IT-BPO services, which promotes non-formal means of remittances and even retaining such FOREX earnings in other countries. Most of tech-savvy youth who start online businesses find difficulties of receiving their income due to FOREX restrictions, causing severe discouragement.

### **Informality**

According to [Annual Labour Force Survey](#) (2021), informal sector accounted for 58.4% of total employment. Considering the informal employment in formal sector as well, the total informality increases to 67.5% of total employment. Informal employment was the highest in Agriculture sector (91.8%). Further, 70.9% of employed males and 60.7% of employed females were in informal employment. Most importantly, 92.4% of "Own Account Workers", who primarily represent the entrepreneurs of MSMEs, are in informality (neither having business registration nor accounts keeping practices).

Non-compliance with the registration of business for Employment Provident Fund or in Department of Inland Revenue, and also avoiding the 'burden of bookkeeping', are mainly due to the 'culture of enjoying flexibility in informality', which increases the vulnerability and limitations in growth.

In addition, the complexities in the registration and reporting processes and bureaucratic inefficiencies make the entrepreneurs less motivated to transform their MSMEs from informality to formal businesses.

### **Innovation in Financial Markets**

Innovations in both businesses and financial markets are severely lacking the commercialization, with proper profit generating business models. On one hand, adopting FinTech solutions by financial institutions is at a very slow pace, owing to institutional inefficiencies.

Complexities in prevailing procedures and formats in financial operations, from opening a bank account to apply for a business loan, critically discourage the young aspiring entrepreneurs.

In addition, most of the officials engaged in appraising business proposals are lacking with capacity to assess tech-based business proposals, whereby even the young entrepreneurs who are with innovative business ideas face challenges in showing credit worthiness to secure funding assistance from banks.

Furthermore, Sri Lanka is still lacking with regulatory and facilitatory space for alternative financial methods such as Crowd funding, Venture capitalism and Angel Investments, which reduces the trusted options for financial assistance.

On the other hand, a heavy cultural dependency on cash transactions is still evident in MSME sector, due to convenience, precarious nature of businesses, and also to avoid taxes and obligations. This makes low appetite to record daily transactions, which is essential in developing trust and connectivity with the banking system.

Despite the monetary policies introduced to promote new start-ups through progressive funding schemes, most of the financial institutions still maintain precautionary measures of requiring collateral for loans. This disconnect between the policy-making and actual practice, result in less achievement of expected outcomes of such schemes.

Lack of consistency in public policy formulation, implementation and periodic monitoring of progress are very lacking in current context. Hence, progressive review of national policies and regulations to ensure their relevance and pragmatism is essential.

## Recommendations

### Education Programs

Most countries have introduced financial education into general, higher and vocational education curricular, inclusive of aspects such as economic & business models; investment, finance and wealth management; understanding realistic returns; cost-benefit analyses; and risk mitigation. Adopting the same in Sri Lanka will ensure the youth with exposure to financial concepts, thereby improve the overall financial literacy.

The dialogue noted that the CBSL and National Institute of Education have taken initiatives to include such financial concepts into school curricula, under the education reforms. It was highlighted the necessity of training of teachers and financial educators on teaching financial literacy and capacitating them to update their knowledge through appropriate sources (such as CBSL periodic reports).

It is also important to disseminate the financial education to the public, specially to the entrepreneurs and youth aspirants, to prevent them victimised by the emerging financial scams and frauds. Thus, the dialogue proposed to release a “Financial Information Support Manual” for young entrepreneurs, that will cover all essential concepts and provide details on where they can find further information. It was also proposed to

disseminate such information through a “National Digital Platform”, which can play a vital role in educating the general public, with the aid of social media and influencers/ celebrity-type entrepreneurs.

The financial education should have: inclusivity (serving in all local languages, and covering persons with disabilities); simplified vocabulary (that the general public can understand); new technologies and user-friendly teaching methods (such as gamification); practical approaches (learning by doing methods); support for trials (to gain experience); and focus on promoting entrepreneurial mindset.

Financial and economic literacy enable entrepreneurs to utilize formal financial channels and also to make more rational financial decisions, which would be the building blocks of improving and sustaining financial stability in Sri Lanka.

### Encouraging Savings at Home

Enhanced finance literacy will encourage savings and financial discipline from household level to corporate businesses. Persistent promotion of the positive habit of saving and inculcating the financial knowledge among children and youth will eventually transform the country's finance cultural and the entrepreneurship ecosystem.

### **Fast Tracking Initiatives in the Pipeline**

There are many progressive initiatives held up in pipeline, such as credit guarantee scheme, shared e-KYC (online Know Your Customer) and bio metric ID. Fast tracking the implementation of these can help improve ease of doing business.

Many modern technologies, such as QR codes, are not popularized due to the legal, technological and administrative barriers in operationalizing. Identifying and rectifying such bottlenecks can help entrepreneurs leveraging such technologies.

More dynamic and pragmatic foreign exchange (FOREX) regulations are needed to encourage the entrepreneurs to bring in their earnings. Digitalizing the financial transaction tracking systems would support enhance the external trade more efficiently.

Developing regulatory space for alternative sources of funding: such as green funding, angel investment, crowd funding, etc. and educating the youth and other stakeholders of such sources would ease the burden on banking system, and also accelerate the economic recovery.

### **Creating awareness on SDGs and ESG**

“Forms of sustainable finance have grown rapidly in recent years, as a growing number of institutional investors and funds now incorporate various

Environmental, Social and Governance (ESG) investing approaches. This growth has been spurred by shifts in demand from across the finance ecosystem, driven both by the search for better long-term financial value, and a pursuit of better alignment with values” [\(OECD\)](#). Creating awareness on Sustainable Development Goals (SDGs) and ESG funding sources can help entrepreneurs develop innovative solutions to secure a good pitch with investors.

### **Capacity Building of Public Officials**

Many public officials, including the financial regulators and bankers, often lack with the technical knowledge on areas such as FinTech. The gap in digital literacy between the youth and such officials creates severe obstacles in catering to the aspirations of the youth entrepreneurs. The dialogue proposed developing institutional capacity building programs, to order to introduce modern technologies and systems to the public institutions dealing with youth and enterprise development. The proposed ‘National Digital Platform’ can act as a ‘knowledge hub’ for both youth entrepreneurs and public officials to update their financial competencies.

The dialogue also highlighted the need of developing a common ‘business support platform’ that coordinates various agencies, including the public, private, community-based and youth-led

organizations. Such platform should have regulatory space to support trials, and assistance to promote business resilience.

Developing a “Finance Index” for Sri Lanka, with specific consideration to country perspectives, recognizing both strengths and areas to improve, along with adequate measurement indicators of financial literacy will help the government in assessing the financial health of the country’s economy.

The policy dialogue observed the possibility of optimizing the Development Officers and extension officers in public sector to reach the grassroots. Educating them and building capacity can help mobilize these officers to improve financial competencies of the youth. These public officers can also be optimized to enforce the regulations on curbing financial frauds.

The dialogue also insisted on introducing a regulatory mechanism for the investment advisory services. It was also noted the necessity of developing country-specific indicators to measure the financial literacy and trends.

### **Bridging Gender Disparities**

The policy dialogue highlighted the importance of policy support to enhance financial and economic literacy among young females and to encourage their participation in technological education,

vocational training, innovation and entrepreneurship.

It was also advised to identify the financial literacy as a skill that should be required by all personnel, including both men and women. Pragmatic approaches to improve such skills, specially among vulnerable groups, such as youth and women, are desirable.

MSMEs help address common challenges such as gender disparities in the economy by improving female labour force participation, effective use of underutilized natural resources and diversifying economic activity across sectors and regions. Thus, capacitating the females engaged in MSMEs, by way of financial education and awareness creation, would help them in improving their businesses.

Females are often lacking with the ability to commercialize their innovative products/services, primarily due to the difficulties they face in developing viable business models, due to difficulties they face in accessing guidance and training. The Community-based organizations can be capacitated and optimized to undertake the motivation, guidance and referral of young females for financial education and entrepreneurship training; conducting post-training follow-ups; and also for introducing mentoring services for emerging entrepreneurs.

## **Collaboration between Agencies**

Establishing a common hub, not just within government agencies but also with private sector organisations can allow easier knowledge sharing and improve ease of doing business for entrepreneurs. Collaborating and linking together with government and academic institutions, private sector and non-government organisations can provide the synergy needed between such stakeholders. Improving the inter-institutional and intra-institutional communication networks are vital in such collaboration.

As the first move, a dynamic macroeconomic model may be developed, bridging gaps between the academia, industry, policy makers and community-based organizations to support entrepreneurs. Secondly, a centralized knowledge hub may be introduced, catering to different requirements of the youth entrepreneurs. Thirdly, a common National Digital Platform can be built that coordinates with various agencies including the youth organizations.

Collaborating with grassroot level organizations and mobilising the religious and cultural institutions can build trust, since it is easier to impact people through such institutions. Such linkage will help youth to explore avenues for entrepreneurial skills development and business start-up.

## **Build Bankability and Digitizing Operations**

Financial transactions and record keeping, which needs to be transformed into more innovative, digitalised and simplified applications that can be applied in day-to-day businesses and also more user-friendly approaches to attract youth.

Digitalizing transactions will make it easy for entrepreneurs to retrieve the “transactions history”. This will help them in proving their credit worthiness and in building bankability.

Many open-source software tools being used by the new generation entrepreneurs to help digitize operations. Collating of these open-source software and publicize as the Standard Operating Procedures (SOP) will make the emerging entrepreneurs aware of and leverage on those software applications.

The considerable disconnect between policy-making and actual practice, in respect of providing special funding packages to emerging entrepreneurs, needs to be resolved. Creating a help desk/hotline to support youth entrepreneurship with guidance on accessing such special funding schemes and also to gain more guidance related to financial management.

