

A Preliminary Evaluation of Financial Literacy in Malaysia

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ABSTRACT

Malaysians have been adversely affected by the greatly increased cost of living in the last decade. The majority of them are feeling as if they are not able to cope with the current standard of living relative to the level of income they are generating. Many have been forced to work two jobs and it is not surprising that these challenges have made them desperate and susceptible to financial fraud and falling victims to financial scams. Economic challenges have impacted the way Malaysians save, spend, manage risks and invest in order to preserve their normal daily livelihood. Among the factors for this are the lack of understanding of how best to manage their finances and financial literacy. This research aims to reveal the financial literacy of Malaysians with information regarding financial understanding, knowledge, and skills that respondents possess. It applies a quantitative study method with a self-administered questionnaire to obtain relevant data from a sample of 2000 respondents across a wide selection of: i) public sector employees; ii) private sector employees; iii) FELDA/rural area residents; and iv) youth in institutions of higher learning. Findings reveal that the majority of Malaysians believe that expenses can be higher than income and possess inadequate understanding of risks and investment.

Keywords: Cash Flow, Credit, Financial Literacy, Savings and Investment

Malaysia was adversely affected by the Global Financial Crisis in 2008 but recovered rapidly, posting growth rates averaging 5.7% since 2010. Nevertheless, the Economic Planning Unit reported

recently that the average income per person in Malaysia has fallen by as much as 15% from US\$10,345 in 2013 to US\$8,821 in 2016 (Economic Planning Unit, 2016). Furthermore, the

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increasing cost of living experienced by Malaysians in recent years has made individuals and families more frugal in their spending. At the same time, all these challenges have made Malaysian more desperate and prone to making imprudent financial decisions, with a number resorting to seeking quick and easy ways to make money. Malaysians generally lack clear understanding of financial risk and return, resulting in their not being able to make rational financial decisions. Many Malaysians are still susceptible to financial fraud, falling victim to financial scams.

A 2015 Bank Negara Malaysia (BNM) survey on financial literacy showed that three out of four Malaysians found it difficult to raise even RM1,000 for an emergency (Bank Negara Malaysia, 2015). Further, less than a quarter had any kind of investment. The survey also showed that a majority of Malaysians tended to spend for instant gratification instead of planning for the long term. This can be seen where only 40% of Malaysians considered themselves financially ready for retirement, despite the steadily increasing life expectancy of Malaysians. The findings also showed that the majority of the over 3,000 Malaysians surveyed did not have a proper budget plan nor practised financial discipline to manage their spending and debt (The Malay Mail online, November 2015).

All this underscores the crucial need for financial education to encourage consumers to be financially savvy in

managing their finances, plan for the future and manage risks associated with financial matters. Individuals ought to be able to engage themselves in comprehensive and thorough financial planning either via self-management or by appointing a qualified financial planning practitioner. Nevertheless, personal financial planning is found to be very much still in the infant stage in Malaysia (Mansor, Hong, Abu, & Shaari, 2015) and Malaysians have been generally found not taking ownership of their own financial affairs (Citi, 2008). Though they are aware of the importance of personal financial planning, many remain lacking in a thorough understanding of the significance of personal financial planning and of the numerous benefits that may be derived from such planning (Citi, 2008). This study intends to determine the financial literacy of the respondents in terms of cash and credit management, savings and investment as well as financial institutions.

LITERATURE REVIEW

The increasing cost of living among Malaysians in present times has made individuals and households more conscious of their financial management. Economic challenges have made an impact on how Malaysians spend, save, invest and manage risks in order to protect their standard of living, especially for the long term. The current higher level of consumer indebtedness and increasing focus on individual responsibility for financial planning

indicate that there is a growing need for better financial management understanding among Malaysians. Thus, there is an ever increasing need for them to properly manage their finances.

In an effort to continuously implement effective consumer education, BNM conducted a survey to measure the level of financial capability of Malaysian consumers (BNM, 2015). The survey found that the level of financial capability is still low, thus affecting the financial situation of individuals and households. The effects of financial incapability do not only result in the financial problems of individuals, households and consumers as a whole but also lead to greater levels of stress and financial exclusion (Taylor, 2009; Lenton & Mosely, 2008). Financial incapability among Malaysians is also due to lack of knowledge and skills, thus leading to lower financial well-being.

One of the reasons for personal financial problems is financial illiteracy faced by individuals and households (Lusardi & Tufano, 2009). Apart from that, the combination of financial problems such as high debt, low income, and low level of financial literacy may adversely affect the financial well-being of individuals and households. Income uncertainty, rising petrol prices and physical pain for instance, have a more drastic influence on well-being. In recent times, with increasing public knowledge supporting public confidence, there is a higher rate of participation in

capital market activities, which is central to capital market development and assists Malaysians in becoming more financially prudent and savvy.

Investors with sufficient information and knowledge about the financial market generally make rational asset allocation decisions to expand their financial welfare in both the short and long term (Hamada, Sherris, & Hoek, 2006). Financial education creates an awareness of stock, mutual fund, bond and investment alternatives among consumers and it has positive relationship towards household income and wealth (Guiso & Jappelli, 2004). Financial literacy enables individuals to understand the importance of saving money for retirement and to earn income during their retirement period. As investors invest in financial assets and generate return, they are able to increase future wealth. At such a time when they are unable to work and earn regular income, the income generated from invested financial assets serve as substitutes and would alleviate the problem of old age poverty (Lusardi & Mitchell, 2008; Hilgert, Hogarth & Beverly 2003; Bernheim, Garrett & Maki, 2001). This is supported by Rooij, Lusardi, and Alessie (2007) who found that knowledge about financial markets will increase a household's financial market participation and lack of understanding of economics and finance is a significant deterrent to investment.



It was found that improvement in financial literacy leads to a positive impact on the individual's personal livelihood. People with a high level of financial knowledge are reported to have less stress and less financial disputes among their families (Taft, Hosein, & Mehrizi, 2013). Fox, Bartholomae and Lee (2005) agreed that people who grow up in a family with higher financial knowledge reported better financial well-being and productivity. Financial literacy helps individuals and households to meet their financial goals and secure their financial well-being in terms of social inclusion (Securities & Investment Commission, 2011). Thus, financial literacy not only increases knowledge of money matters but also helps and empowers consumers to make better financial decisions that lead to greater financial well-being (Sabri & Zakaria, 2015).

The need for more knowledge about different aspects of financial planning services has been highlighted by scholars of many disciplines, and calls for more in-depth studies of this practice have been put forward. Findings show that the important aspects of financial planning services have been previously neglected. The characteristics of gender are shown to have importance both for consumers and planning perceptions of the different aspects of the core elements of financial planning services. Research has revealed that individual consumer characteristics affect consumer risk assessment (Harris,

Jenkins, & Glaser, 2006; Weber, Blais, & Betz, 2002); investment behaviour (Hira, Sabri & Loibl, 2013; Hira & Loibl, 2008; Sundén & Surette, 1998); and the decision to engage advisers (West, 2012). It is therefore vital to have some preliminary understanding of financial literacy in order to tailor the necessary financial education programme.

METHODOLOGY

This study engages the approach of quantitative analysis where a purposive sampling technique is conducted to select the sample throughout Malaysia. Self-administrative survey questionnaires were distributed to a sample that covered a wide section of the population. The sample was separated into four categories: i) public sector employees; ii) private sector employees; iii) FELDA/rural area residents; iv) youth in institutions of higher learning. These four categories are noted to have the representation of the population for the results to be generalized. According to the sampling size calculation by Krejcie & Morgan (1970), for a population which is equal to or greater than 1,000,000, the required sample size is about 1,500 with confidence interval of 95% and margin of error of 2.5%. This study collected relevant information from a total of 2,000 respondents in order to compensate for incomplete and unusable responses.

All questions in the questionnaire were developed in close-ended form

by providing possible choices of answers. This method could prevent bias and allow the data to be analyzed in the most appropriate way. Data was collected from April to August 2017. A pilot study was conducted among forty respondents to check the suitability of research instruments in a preliminary small-scale study. This assisted the researchers to decide on the most appropriate approach to conduct such a large-scale research project and to ensure the appropriateness of the proposed methods and instruments. Some instruments were revised and the instructions clarified after the pilot study due to respondents' problems in understanding them. This enhanced the reliability and accuracy of the questionnaire.

The questionnaires requested the respondents' demographic and socio-economic information in terms of age, gender, ethnicity, family size, financial status and income adequacy. The respondents' financial literacy was measured by testing their financial knowledge with questions developed by Sabri, MacDonald, Hira and Masud (2010) based on the Malaysian context. As for the measurement of financial literacy, the survey provided questions in eight areas including cash flow management, credit management, savings and investment, retirement planning, risk management, Shariah-compliant

products, estate planning and financial institutions. The data was then compiled according to the respondents' correct or incorrect answers.

DEMOGRAPHICS AND SOCIO-ECONOMICS

The information on demographics and socio-economic characteristics is shown in Table 1. The sample comprised 55.3 per cent married individuals and 44.7 per cent who were still single. In terms of gender, a larger percentage (54%) of respondents was female. This is consistent with the national overall population averages. The study is also representative in terms of ethnicity where 64% of the sample was Malay, 27.9% Chinese, 5.9% Indians and 2.2% of other ethnicities. The majority of the respondents (57%) had a monthly income of less than RM3,000, which put them in the B40 category. Respondents with a monthly income of between RM3,000 to RM4,999 comprised 25.5% and those earning between RM7,000 to RM8,999 comprised 3.3% and last but not least, those with income of above RM9,000 comprised only 4.8%. The highest percentage of respondents were in the age group of between 20 to 29 years (31.7%), followed by 30 to 39 years (24.70%) and more than 50 years (18.4%). Respondents in the range of 40 to 49 years of age and those aged less than 20 years comprised 15.3% and 9.9 respectively.

Table 1: Demographics and Socio-Economic Characteristics

Characteristics	N (%)
Gender	
Female	1080 (54.0)
Male	920 (46.0)
Marital Status	
Married	1106 (55.3)
Single	894 (44.7)
Ethnicity	
Malay	1280 (64.0)
Chinese	558 (27.9)
Indian	118 (5.9)
Other	44 (2.2)
Income (RM)	
< 3000	1140 (57.0)
3000 - 4999	510 (25.5)
5000 - 6999	188 (9.4)
7000 - 8999	66 (3.3)
> 9000	96 (4.8)
Age (years)	
< 20	198 (9.9)
20 - 29	634 (31.7)
30 - 39	494 (24.7)
40 - 49	306 (15.3)
> 50	368 (18.4)
Household Size (no. of persons)	
< 4	900 (45.0)
5 - 6	696 (34.8)
> 7	404 (20.2)
Asset to Debt Ratio	
Asset value < Debt	1050 (52.5)
Asset value = Debt	440 (22.0)
Asset value > Debt	510 (25.5)
Income Adequacy	
Enough & able to save money	338 (16.9)
Enough for most of things	472 (23.6)
Enough for basic needs	944 (47.2)
Not sufficient	246 (12.3)

In addition, 45% of the respondents had a household size of less than four persons, 34.8% were those in households of between five to six persons and only 20.2% were in households comprising more than seven persons. This is very much reflective of the national household size distribution, which stands at 4.13 persons. Slightly more than half of the respondents (52.5%) had a very low asset to debt ratio. There is definitely a need for more information and guidance in financial readiness for this group of relatively younger respondents. Almost half of the respondents (47.2%) had income that was only sufficient for basic needs. With depressed real wage growth, the data provides an indication that the respondents were just able to meet day-to-day expenses with only 16.9% having enough to live comfortably with some savings. A worrying total of 12.3% of the respondents indicated that they did not have sufficient income for living expenses.

Parallel with this study's objective in identifying the status of the financial literacy of the respondents, they were provided with eight domains to evaluate

their financial knowledge and ability to manage their finances. The information was captured and the findings are discussed in the next section.

FINDINGS

A set of general questions was provided to indicate overall financial literacy and this is shown in Table 2. As for the findings on credit management, it is comforting to note that 81.4% of the respondents knew that credit card holders cannot spend without limit. Nevertheless, 18.6% believed that they could spend an unlimited amount with their credit card. Meanwhile, 21.9% of the respondents misunderstood that the longer the repayment period, the lower the overall loan cost. This is a worrying finding and some action must be taken to rectify the misconception. The majority (61.2%) did not understand that debt cannot be inherited from a legal standpoint. In addition, 81.3% understood the function of Central Credit Reference Information System (CCRIS), indicating that the Central Bank has been successful in explaining the functions of CCRIS. However, more can still be done as 18.7% of the

Table 2: Percentages of Respondents with Correct Answer in Financial Literacy

STATEMENT	CORRECTLY ANSWERED (%)	WRONGLY ANSWERED (%)
CREDIT MANAGEMENT		
Credit card holders can spend without limit.	1628 (81.4)	372 (18.6)
The longer the repayment period, the lower the cost of the overall loan.	1562 (78.1)	438 (21.9)
Debt cannot be inherited.	776 (38.8)	1224 (61.2)
Central Credit Reference Information System (CCRIS) is a credit bureau that collects, processes, stores and creates credit information.	1626 (81.3)	374 (18.7)

Table 2: Percentages of Respondents with Correct Answer in relation to Financial Literacy

STATEMENT	CORRECTLY ANSWERED (%)	WRONGLY ANSWERED (%)
CASH FLOW MANAGEMENT		
Sometimes, expenses can be higher than income.	326 (16.3)	1674 (83.7)
A shopping list helps us to control our expenses.	1869 (93.5)	131 (6.5)
One needs to save before spending.	1853 (92.7)	147 (7.3)
SAVINGS AND INVESTMENTS		
All types of investments are profitable and low risk.	1630 (81.5)	370 (18.5)
All investments in Malaysia are legal.	1485 (74.3)	515 (25.7)
An individual needs to save a minimum of 10% for emergency purposes.	1773 (88.7)	227 (11.3)
RETIREMENT PLANNING		
One can depend on EPF savings for living after retirement.	1124 (56.2)	876 (43.8)
If my retirement fund is insufficient, I will continue working.	1622 (81.1)	378 (18.9)
Private Retirement Scheme is only for Government employees.	1548 (77.4)	452 (22.6)
We can depend on our children after retirement.	1689 (84.5)	311 (15.5)
RISK MANAGEMENT		
If I can afford to bear the risk, I don't have to buy insurance.	861 (43.1)	1139 (57.0)
All types of risk can be insured.	1196 (59.8)	804 (40.2)
SHARIAH-COMPLIANT FINANCIAL PRODUCTS		
Shariah products are only available for Muslims.	1241 (62.1)	759 (38.0)
Shariah products are free from risk.	1229 (61.5)	771 (38.6)
Everyone can buy insurance / Takaful whenever they wish to do so.	565 (28.3)	1435 (71.8)
Shariah products generate reasonable returns similar to conventional products.	1337 (66.9)	663 (33.2)
ESTATE PLANNING		
I can distribute all my assets through my Will.	1636 (81.8)	364 (18.2)
Wills cannot be modified once written.	736 (36.8)	1264 (63.2)
Only if I have assets, I will write a Will.	956 (47.8)	1044 (52.2)
My Will can include EPF and insurance savings nominees.	466 (23.3)	1534 (76.7)
UNDERSTANDING FINANCIAL INSTITUTIONS		
Credit Counselling and Debt Management Agency (AKPK) offers financial loans.	1115 (55.8)	885 (44.3)
Bank Negara Malaysia's role is only to print currency	1502 (75.1)	498 (24.9)
Bursa Malaysia is a stock exchange operator and offers a complete range of services covering trading, clearing, depository and settlement.	1548 (77.4)	452 (22.6)
Securities Commission Malaysia ensures proper conduct of market institutions and licensed individuals.	1680 (84.0)	320 (16.0)

respondents were unaware of CCRIS, its role and functions.

It is surprising that almost 83.7% of the respondents allowed expenses to be sometimes higher than income in their general management of cash flows. The results reveal that respondents felt that it is all right to overspend, revealing a worrying trend among Malaysians. Only 16.3% of the respondents actually understood that expenses cannot be higher than income. Fortunately, the majority of them (93.5%) agreed that a shopping list helps to control expenses and one need to save before spending.

It is disturbing to note that 18.5% were of the opinion that all investments in Malaysia are profitable and low risk. In addition, 25.7% of the respondents believed that all investments in Malaysia are legal and only 74.3% of the population was aware that not all investments are legal. As participants of investment instruments, they must be vigilant to various measures that may be used by unscrupulous platforms/channels that may entice them to channel their funds into illegal investment. This thinking must be corrected to help ensure that Malaysians are able to differentiate between legal and non-legal investments. It is essential that the concept of saving for emergencies is instilled into the 11.4% of respondents who did not see the need for a 10% buffer fund as an allocation for emergency events.

With regard to the retirement planning domain of financial literacy,

the study reveals that only 56.2% of the respondents knew that they could not depend on their Employees Provident Fund (EPF) savings for living after retirement. The majority (81.1%) were aware that they would need to continue working if their retirement fund was insufficient. Alarming, 43.8% of the respondents believed that they could depend on their EPF savings for their living expenses after retirement. However, this belief in the adequacy of EPF savings to meet retirement needs contradicts the findings of a study to determine the adequacy of retirement income delivered by Alaudin, Ismail and Isa (2017). In addition, according to the EPF, as reported by The Star in October 2017, more than two-thirds (68%) of EPF members aged 54 had less than RM50,000 in EPF savings. With the household poverty line income at RM930 monthly, RM50,000 in savings will only last 4½ years. 70% of members who withdraw their funds at age 55 used up their savings in less than a decade after retirement. Most EPF savings are therefore not sufficient to enable retirees to stay out of poverty after retirement.

Another worrying trend is that 22.6% of the respondents were of the view that the Private Retirement Scheme (PRS) is only open to government employees. As such, the Private Pension Administrator (PPA) would need to do much more to educate Malaysians on the PRS. Whilst pointing this out, it must also be noted that the majority of the respondents (77.4%) were aware the PRS is for all.



While Malaysians are generally known to be attentive to the need to take care of the elderly, the majority (84.5%) knew that having their own financial retirement plan is essential.

More than half of the respondents (57%) were illiterate in risk management as they did not understand the need to buy insurance. For them, insurance was a “nice to have” instead of a “need to have” on their list of priorities. Only 59.8% of respondents agreed that not all types of risks can be insured.

Many were unaware that insurance/takaful companies perform risk analysis and implement holistic risk measuring approaches before agreeing to insure an individual and 71.8% of the respondents believed that they could purchase an insurance/takaful policy at any point in their lifetime. While 38% of the respondents were unaware that Shariah-compliant financial products are not limited only to Muslims, the majority (62%) were aware that Malaysians of all religious backgrounds can purchase these products, as the essence of Islamic finance is the concept of inclusiveness. With Malaysia leading in the Islamic financial front and the increasing growth of Islamic financial institutions, the general populace is aware that Shariah-compliant financial products are able to generate reasonable returns. This is as 66.9% of the respondents were aware of this. In terms of knowledge of Shariah-compliant financial products, the majority of the respondents were illiterate in terms of Islamic products

as more than 60% answered correctly for 3 out of the 4 items in this domain. Finally, it is alarming to find 38.5% of respondents believed that Shariah-compliant financial products are 100% risk-free.

As for estate planning, about one-third of the respondents (36.8%) was unaware that Wills can be modified after they have been written. There remains a misconception among the respondents of the need and purpose of a Will as 52.2% of the respondents answered that one can only write a Will if one has assets. A surprising 47.8% did not know that they could also assist their loved ones by writing a Will even if they do not have assets. The respondents did not understand that nominees cannot be included in one's Will as only 76.7% were unaware that a Will cannot supersede a nomination.

With regard to knowledge of financial institutions in Malaysia, only 55.8% of the respondents in this study were aware of the role of AKPK. 44.2% of respondents thought that AKPK's role is to offer financial assistance to support an individual in times of financial distress. Nonetheless, the respondents were aware of the roles of Bank Negara Malaysia, Bursa Malaysia and Securities Commission Malaysia, with more than half responding correctly. This reflects that the respondents did have knowledge of Malaysia's financial institutions and their respective roles and functions. However, it is also essential to note that 24.9% of the respondents thought that

Bank Negara Malaysia's role is only to print currency to ensure an adequate supply in the market. Despite the assumptions of many that the majority of rural residents may be unaware of the roles of the Securities Commission; this study reveals that 84% of the respondents were aware of the existence and role of the SC.

CONCLUSION

The findings in the section on financial literacy show that more than 80% believed that expenses can sometimes be higher than income; and they could depend on their EPF savings to meet living needs after retirement (43.8%), and that they did not need insurance if they could afford the risk (43.0%). An important and surprising finding is that a large proportion (44.2%) of them believed that AKPK offers financial loans.

Financial knowledge regarding cash flow management revealed that 83.7% of the respondents had expenses higher than income. In addition, 61.2% believed that debt can be inherited. This shows that there is definitely a knowledge gap credit management is concerned. It is also alarming to learn that more than a quarter of respondents had the idea that all investments in Malaysia are legal. Finally, 43.8% of the respondents said they could depend on EPF for their living expenses after retirement. Several other concerns were revealed as the respondents were not fully aware of the differences between conventional and

Islamic financial products. The overall findings signify that the respondents were not fully equipped with sufficient financial knowledge to make informed decisions regarding their financial affairs.

With regard to financial literacy and education, it is vital that the values of financial sustainability are disseminated so that Malaysians understand that one's income must always be able to cover expenses and one must never live beyond one's means. Malaysians must be educated to control their credit card spending, save for rainy days and unexpected incidents, and have enough insurance to cover unforeseen circumstances. Malaysians should also be educated on retirement planning as well as on estate planning for their golden years and beyond. Some basic understanding of the types of financial institutions and their functions is definitely necessary so that one knows where to seek assistance when the need arises. Most importantly, a basic understanding of risks and investment is vital in order not to fall prey to unscrupulous investment schemes.

RECOMMENDATIONS

Continuous financial education for the public to create awareness of the importance of setting financial goals and taking the necessary actions to achieve their financial goals is vital for Malaysians. Other than that, the development of financial literacy



programmes tailored to meet the differing needs of the various segments of society is highly encouraged. The training format should be kept simple and relevant to the participants' day-to-day lives. Emphasis should be on learning by doing and linking to the benefits, and knowing how to use available financial products and services. In addition, financial education should be made mandatory in continuous professional development and personal growth programmes in the public and private sectors.

There is still a lack of financial understanding in differentiating between legal investments and scam schemes in Malaysia with quite a number falling into these traps. The undesirable result of this is that one out of four investors has the potential to enter into a 'get-rich-fast' scheme. Hence, our recommendation is for the SC to aggressively interact with the general public to educate them on the real nature of investment as compared to potential scams. Intermediaries such as MFPC can be appointed as ambassadors to bridge the information and knowledge gap on behalf of the SC. Besides that, on-the-job training should be provided to enhance skills and ensure relevant personnel perceived to be financial planners i.e. AKPK Counsellors and Wealth Managers are professionally certified. At the least, they should be made to acquire Registered Financial Planner or Shariah RFP qualification so as to promote

financial planning and provide quality and appropriate advice to the public.

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