ANALYSIS OF FINANCIAL LITERACY, KNOWLEDGE AND RISKS OF CREDIT CARD

(CASE STUDY IN STUDENTS OF FACULTY OF ECONOMICS)

BagusShandyNarmaditya

DwiWulandari

Faculty of Economics, UniversitasNegeri Malang

Abstract

This researchis aimed to determine the financial literacy of students of Faculty of Economics in terms of their understanding of the credit card. The results show that two out of ten respondents who knew about the interest rate they paid. The explanation for this research relates to the fact that most credit card bills were paid by their parents and even their credit card applications were approved because of their parent's application, so that they thinkthere is no need to know things like interest rate and others. In addition we found that these students have low financial literacy as only two out of ten students who understand things about basic finances.

Keywords: Financial Literacy, Credit Card, Non-CashPayment, Plastic Cards

Introduction

Financial literacy is the ability to understand how money works, how someone managed to get the money or print it wisely according to the investment program that he knows, how one can manage the money and how to invest and transform it into more money and how people donate money to help others. More specifically, it refers to a set of skills and knowledge that allows an individual to make effective decisions on its investments in order to increase financial resources.

Financial literacy should be a lifeskill that is owned by someone in his life because one purpose of life is becoming prosperous. How one can be prosperous if he is not able manage his finances well.

COPY RIGHT © 2015 Institute of Interdisciplinary Business Research

There are many definitions of financial literacy, as some of them from Chen and Volpe which defines financial literacy as the ability to manage finances. Other definition from Katy, Hudson, and Bush who interpret financial literacy as the ability to understand the financial condition and financial concepts, and to change the appropriate knowledge into behavior. Not much different, The President Advisory Council on Financial Literacy defines financial literacy as the ability to use the knowledge and skills to manage financial resources to prosper.

The definition of financial literacy by Chen and Volpe is looser, systematic and has a greater coverage. The purpose of the coverage is more comprehensive because besides systematic, covers broad areas, namely spending and credit, insurance, and savings and investment also. Explanation of the first field on spending and credit is how people can manage their spending. In the sense that there should be a spending plan or budget is appropriate and how the discipline to do that in according with the budget.

Specifically, it's how people need to make a normal spending plan so they do not slip into the pattern of spending that exceeds targets and the ability to buy. Such as how to buy something that is actually needed or not needed and desired. It is important to note as to avoid themselves from a deficit, due to avoid and prevent this deficit at the heart of healthy spending. As for the credit that is how the credit position correctly. The point is to position credit as a tool that is healthy and not as excess cash to meet various desires. The use of credit is actually intended to meet the needs and to their use should be adjustable to the financial capabilities.

Another domain of financial literacy is insurance. Insurance needs to be owned because of the growing financial uncertainty at this time. Having insurance, whether it's a life, education, health, property, house fire, car or any other insurance will be helpful to cover the losses. The main objective of insurance is to give compensationguarantee. Last domainsare savings and investment. The role of financial literacy is to give an understanding that savings are an important part because it would provide security in the short term consumption. For example when there is an unexpected spending then that's when savings can be a tool to meet consumption. As for investments, financially literate people will be greatly helped because it has knowledge/understanding of the ways that can be done to invest in investment instruments available, including stock. In fact, financial literacy will improve the ability to understand what

COPY RIGHT © 2015 Institute of Interdisciplinary Business Research

is the best way to determine smart attitude in making stock trading decisions in the sense that how to do the analysis or even observe the relevant factors to consider in making stock trading decisions, whether to buy, hold or sell. Not only that, financially literate people also provide insight on how to avoid themselves from investment fraud under the guise of giving high returns. The reason is that financiallyliterate people will be able to understand that it is impossible to get high returns that provide low risk and this is in accordance with the golden rule of investing which is high risk high return.

Based on the benefit if the person has a financial literacy, we conclude that the core or essence that financial literacy will be very helpful in providing deep insight understanding of the rules to manage smart financial, and the chances of achieving financial freedom would be even greater. In other words, financial literacy can be used as one of the tools that need to be improved if people want to have a passive income that exceed active income.

This researchspecifically focus on discussing about the credit card for a survey to prove that the use of debit and credit cards will increase the gross domestic product (GDP) in Indonesia and contribute as much as US $ 983 billion to global GDP over the period 2008-2012. The growing use of electronic payment products such as credit and debit cards accounted for US $ 6.4 billion (Rp 62 trillion) to Indonesia's GDP, according to findings of a study conducted by Visa Moody's Analytics, an independent economic institution.

Studies conducted in 56 countries including Indonesia, which represents 93% of total global GDP, concluded that the use of payment cards can further improve efficiency and provide a significant contribution in promoting economic growth. Globally, electronic payments contribute as much as US $983 billion to GDP in the 56 countries in the period 2008-2012. In the same period, GDP in these countries on average grew by 1.8 %.

With the growing use of cards which accounted for 0.27 percent or US $ 6.4 billion to the GDP of Indonesia, no doubt that electronic payments provide a significant benefit, not to mention the added importance of maintaining the openness of the market to increase competition and innovation in the domestic industry. From this data, we can see that economic growth is one of the positive effects of the use of the card which is certainly closely related to the benefits

COPY RIGHT © 2015 Institute of Interdisciplinary Business Research

offered by electronic payments, such as the security aspect, convenience in transactions without cash, increased efficiency and decreased illegal economic activity.

Increased used of credit and debit cards contribute to economic activity by lowering transaction costs and improve efficiency in the flow of goods and services. The existence of credit and debit cards to help consumers optimize their consumption choices by providing secure access and real time against the money in their accounts or their need for credit. Merchants also benefit from the reduction in cash and checks, which eliminates the risks of the use of cash. In addition, the growth of e-commerce and mobile payment are also supported by a global electronic payment system that allows consumers to make payments with a definite security guarantees.

Electronic payment also helps reduce black markets activity by improving transparency and generate additional tax revenue. Moody's Analytics found that growth of 1 % of the increase in card in 56 countries resulted in an increase in the consumption of 0.056 percent. Seeing the card penetration growth rate and its effect on GDP, Moody's Analytics projects a 0.25% contribution to the growth of consumption and 0.16 % to GDP growth. From 2008 to 2012, the GDP growth rate of only 1.8% per year. Without an increase in the use of the card, the growth amounted to only 1.6 %. Penetration and use of the card gives a boost to the economy by helping to prevent the slowing of growth.

Despite the increased use of credit cards can boost economic growth in the aggregate, we need to realize that a person's inability to manage the use of credit cards has made a lot of problems lately as violence committed by the debt collector or someone who committed suicide because of credit card debt and cannot afford paid or salaried workers one million dollars which turned out to have more than one credit card debts. Necessary understanding of the mechanisms and consequences of using credit cards early before someone incurred debts and even misery. Since 2015 The Central Bank of Indonesia set a limit on the number of credit card ownership by the level of monthly income. For customers with income between 3 million-10 million per month may only have a credit card no more than 2 publishers. Maximum funding ceiling is 3 times the number of average monthly income. As for income above 10 million per month, The Central Bank of Indonesia did not specify in detail how the amount of the credit card can be owned. In

COPY RIGHT © 2015 Institute of Interdisciplinary Business Research

addition, The Central Bank of Indonesia also provides flexibility to the issuing bank to determine the maximum ceiling of each client. Of course, this flexibility does not come out of the corridors of rules that have been made previously by The Central Bank of Indonesia.

METHODS

In this study we wanted to see how big the student's understanding of personal finance in terms of the understanding of the credit card. Respondents were students of the Faculty of Economics who has a credit card. Some of the questions asked and explored in depth such as whether students who use credit cards understand the interest rates on credit card use? Does the student know the penalties faced if late paying the bill? Does the student know the penalty if the limit is not adhered to? What distinguishes the behavior of students in the use of credit cards? Do gender and age of the student influence on their behavior in the use of credit cards? Our survey respondents on average were in the final semester and already getting the course of business, management and finance. The number of men and women are equal, and are in the nearly equal age range

RESULT AND DISCUSSION

We found only about ten people from the end of the semester students at the Faculty of Economics who has a credit card. They all have a credit card registered by the parents of each student. Their ownership of the credit card was not due to personal desires, but rather because the application is made by their parents. This is in contrast to studies conducted in the United States by Ludlum et al (2012) which states that in many campuses in the United States, 70% of undergraduate college students have a credit card even 36 % have two credit cards. The Indonesian credit card users among students is not much, in contrast to debit card users. The study by Sharpe (2009) also states that 66 % of students in the Midwest have a credit card. Students we surveyed stated that they do not often use a credit card, only urgent moments alone. In contrast to research Ludlum et al (2012) which states that half of their respondents use credit cards for immediate interests and 36% use it less than five times a month.Compared with students overseas, students on our campus is not much use of their credit cards, they prefer to

COPY RIGHT © 2015 Institute of Interdisciplinary Business Research

pay in cash when it is to have money in order not to be confused pay the bill. Although almost all states that parents they pay the bills, but they felt shy and uncomfortable when the credit card bill shows that they buy items that are not too important. In addition they all have a debit card that they think is more convenient to use because it directly cut from their bank accounts.

Just as the results of research Ludlum et al (2012), very few are using credit cards to pay for college (in the case of Indonesia, the credit card can be used to withdraw cash and when we asked the respondents had they use the funds withdrawn to pay college, no one is using it), use of credit cards is to pay for purchases most books and lecture purposes. Ludlum et al (2012) stated that the wide use of credit cards is more indicative of the problem of family welfare than the students showed about aspects of their financial literacy.

For the question of whether the students understand the existing interest rates on credit cards, same with research Ludlum et al (2012). Because the interest rate is the cost of the loan, a student who has financial literacy should know the interest rate he should pay (Robb and Sharpe, 2009). In turns out answer to this question is in line with research Ludlum et al (2012). Ludlum find only one of the six students who understand the interest rates they pay. In our study, only two out of ten respondents who knew about the interest rate he paid. The explanation for this relates to the fact that most credit card bills paid by their parents and even their credit card applications get because their parents so that they feel no need to know things like interest rate and others.

In addition we also ask do the students know the penalties faced if late paying the bill? In line with the research Ludlum et al (2012) turned out to be 80% of students who have a credit card do not know this. And whether students know the penalty if the limit is not adhered to? It turns out 80 % of respondents did not know this. If these results are combined, only 20% of the student credit card holders who understand interest rates, late payment penalties and fines if beyond a limit. This indicates that the financial literacy as only two out of ten students who understand things about basic finances.

Chen and Volpe (1998) states that students who take business courses should have a better understanding of basic finances. But the results of this study stated that students who had taken business courses was also lack an understanding of basic finances when viewed from the

COPY RIGHT © 2015 Institute of Interdisciplinary Business Research

side of credit cards. This may be caused by the acquisition of the credit card of the parents, as well as payments made by the parents so that students are less concerned with interest rate and a limit. The process that occurs when a student using a credit card are the parents of these students go to a bank and register a credit card in the name of his son, but the account numbers of parents. After that, the student is given credit card by parents and can use the credit card for the transaction. Transactions that can be used online transactions, offline, as well as cash withdrawals through ATMs. After that report the use of credit cards is usually delivered by the bank to the parent within a specified period. Use of credit cards is very dependent on children who act as business actors. Various risks may arise depending on how the child how to use a credit card.

Gender did not affect the financial literacy and understanding of the credit card. This is in line with the findings Robb and Sharpe (2009) but refused finding that women have a lower financial literacy related to credit cards (Seyedian and Taihyeup, 2011; Lusardi , Mitchell, &Curto, 2010; Borden, et al., 2008; Lusardi and Mitchell, 2005; Jones,2005; Chen and Volpe, 2002). Armstrong and Craven (1993) and Lawrence, et al. (2003) found that female students have more credit cards than students and this is not evident in this study.

CONCLUSION

Although many definitions of financial literacy, student less understand, especially when associated with the knowledge of the credit card (Ludlum and Smith, 2011; Jones, 2005; Warwick and Mansfield, 2000; Chen and Volpe, 1998).

In our study, only two out of ten respondents who knew about the interest rate he paid. The explanation for this relates to the fact that most credit card bills paid by their parents and even their credit card applications get because their parents so that they feel no need to know things like flowers and others. In addition we found the low financial literacy as only two out of ten students who understand things about basic finances. Chen and Volpe (1998) states that students who take business courses should have a better understanding of basic finances. But the results of this study stated that students who had taken business courses was also lack an understanding of basic finances when viewed from the side of credit cards. This may be caused

COPY RIGHT © 2015 Institute of Interdisciplinary Business Research

by the acquisition of the credit card of the parents, as well as payments made by the parents so that students are less concerned with interest rate and a limit.

An understanding of financial literacy in students is primarily concerned with the credit card is still needed because when the increasingly widespread use of these cards, it will be a student incomprehension turned to the future financial life.

COPY RIGHT © 2015 Institute of Interdisciplinary Business Research

REFERENCES

Armstrong, C. J., & Craven, M. J. (1993). Credit card use and payment practices among a sample of college students. Proceedings of 6th Annual Conference of the Association for Financial Counseling and Planning Education: 48-159.

Borden, L. M., Lee, S. A., Serido, J., & Collins, D. (2008). Changing college students' financial knowledge, attitudes, and behavior through seminar participation. Journal of Family Economic Issues, 29(1), 23-40.

Chen, H., & Volpe, R. P. (1998). An analysis of personal financial literacy among college students Financial Services Review, 7(2), 22. Retrieved from http://www2.stetson.edu/fsr/abstracts/vol_7_num2_107.pdf

Chen, H., & Volpe, R. P. (2002). Gender differences in personal financial literacy among college students. Financial Services Review, 11, 289-307.

Jones, J. E. (2005). College students' knowledge and use of credit. Financial Counseling and Planning, 16(2), 9-16

Lawrence, F. C., Christofferson, R. C., Nester, S. E., Moser, E. B., Tucker, J. A., & Lyons, A. C. (2003). Credit card usage of college students: Evidence from Louisiana State University. University of Illinois at UrbanaChampaign, Research Information Sheet #107

Ludlum, M, et al. 2012. Financial Literacy and Credit Cards: A Multi Campus Survey. International Journal of Business and Social Science Vol. 3 No. 7; April 2012

Lusardi, A., & Mitchell, O. S. (2005). Financial literacy and planning: Implications for retirement wellbeing. Michigan Retirement Research Center Research Paper No. WP 2005-108.

Lusardi, A., Mitchell, O. S., &Curto, V. (2010). Financial literacy among the young. 44.2 Journal of Consumer Affairs, 358-380.

Robb, C.A. & Sharpe, D.L. (2009). Effect of personal financial knowledge on college students' credit card behavior. 20.1 J. of Financial Counseling and Planning, 25-43.

Seyedian, M., and Taihyeup, D.Y. (2011). Improving financial literacy of college students: a cross-sectional analysis. 45.1 College Student Union 177-189.

Warwick, J., & Mansfield, P. (2000). Credit card consumers: College students' knowledge and attitude. Journal of Consumer Marketing, 17(7), 617-626

COPY RIGHT © 2015 Institute of Interdisciplinary Business Research