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The Financial System and the Financial Literacy Imperative in Developing Countries

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Abstract:

The purpose of this paper is to review the existing state of knowledge of the financial system and its operations in advanced economies and to assess the application of the system to developing countries. The methodological approach consisted mainly of: collecting data from leading texts and peer-reviewed journals on the subject; conducting a content analysis of these secondary sources to gain a deeper insight into the issues; identifying the concepts critical to the functioning of the financial system; and discussing the matter of financial literacy to an emerging economy. The results of the research provided a basis for understanding the components of the financial system, finance and financial decisions, financial statements and financial analysis, the financial planning process and capital budgeting, financial planning, market and industry fluctuations, and financial literacy. It is intended that the results of the study should serve as a sound introduction to the nature of the financial system with the implication that the professional associations in the field of finance and higher education institutions must engage businesses and students in understanding how the financial system works and the imperative for increasing financial literacy. The paper is novel because no similar study for a small island emerging economy in the Caribbean has been published in an accessible academic journal, and the importance of broad based financial literacy is highlighted. The research is limited to the extent that only secondary data sources were explored so the insights from practitioners were not obtained which opens the subject to future research.

Key words: Financial System; Decisions of Firms; Financial Analysis; Financial Planning; Capital Budgeting; Financial Literacy; Emerging Economies.

1. Introduction

The need for this study arises from the vital importance of the ordinary persons in developing countries and emerging economies such as those of the Caribbean region, to obtain a greater understanding of the operation of the financial system (FS) and the requirement to enhance financial literacy as a platform for development. The central purpose of the study is to document the major issues regarding the FS in a form that can be understood by persons at the tertiary level of business education who are expected to relay the concepts to their peers. The research approach is essentially qualitative in that the main focus is on published material collected from leading texts and journals.

There exists a relatively large body of work on the dynamics of the FS which was sourced from leading texts and relevant journals. From an analysis of these sources, the major themes from the literature were identified as covering: the composition of the FS; the functional as opposed to an institutional perspective of the FS; financial institutions and financial innovation; interest rates; types of financial decisions and savings; and financial statements and analyses (Bodie, Meron, and Cleeton, 2009; Muldowney and Sievers, 2007; Ariely, 2010; Ehrhardt and Brigham, 2009; Ogle, 2008). The paper also explores the vital subject of financial planning and the planning process, and the implications for capital budgeting, competitive firms, and market and industry fluctuations (Ehrhardt and Brigham, 2009; Bodie et al., 2009; Truong, Partington, and Peat, 2008; Gitman, 1987; Murray, 1992; Orlando, 2009; Herremans, Issac, and Bays, 2007; Mills, 1995).

The above sources adequately covered the fundamental concepts in the study of the FS and its associated issues, but such sources tended to focus on the advanced economies to the detriment of developing and emerging economies. In particular, the treatment of small island states was deficient and are barely addressed, therefore, this study sought to explore the real world issues that impact emerging countries such as Trinidad and Tobago (TT) classified as a high income developing country by the World Bank. The issues highlighted include: project analysis because of the challenge of selecting development projects in emerging economies; financial decisions and the methods employed by firms; the use of financial leverage; social responsibility of financial firms; and the major matter of financial literacy (Bodied et al., 2009; Ogle, 2012; Worthington, 2013; Mauna and Anise, 2013; Assad, 2015; Nkundabanyanga, Kasozi, Nakluenge and Tauringana, 2014; Kefela, 2011; Lausardi and Mitchell, 20111; and Wise, 2013).

This study is significant for policy making and for encouraging public agencies, business associations, higher education institutions, and financial institutions to collaborate in making opportunities available for increasing financial literacy among the population of emerging economies. The main conclusion is that emerging economies should concentrate on improving financial literacy by mounting broad programs which extend to the main centres of population preferably on a collaborative basis with financial, educational, and relevant public sector agencies.

2. Research Approach

The research on the FS presented in this paper is aimed at acquiring a deeper understanding of the key concepts involved in the FS and the application of those concepts at the operational level. The methodology adopted was a qualitative research approach which was limited to: collection and distillation of relevant literature on the FS from leading business texts, relevant journals obtained from the ABI/Inform database; internet searches on financial keywords; and assessment of the concept of financial literacy in the context of emerging economies and the small island case of TT. The research process, consistent with acknowledged qualitative procedures, was outlined by Cresswell (2009) as involving: the researcher as the key instrument for conducting the research; multiple sources of data obtained from financial texts and peer reviewed journals; a theoretical lens which seeks to identify the social and political context of the issue studied, and represents a holistic account to better reflect the complex picture of the study elements.

3. Overview of the FS

The FS comprises the markets, intermediaries, service firms, and other institutions which make financial decisions on behalf of households, businesses, and governments. Sometimes markets can be described by their location such as the New York Stock Exchange, but most markets are over-the counter markets such as stocks, bonds, and currencies which are facilitated by computer networks linking security dealers and customers. Financial intermediaries such as banks, investment companies, and insurance companies specialize in providing financial services and products such as checking accounts, commercial loans, mortgages, mutual funds, and a range of insurance instruments (Bodie et al., 2009, p. 24). The FS facilitates growth by channeling savings to finance investment projects. In so doing, financial institutions serve to provide money indirectly to borrowers through specialized intermediaries, such as banks, savings-and-loan associations, mutual funds and pension funds; and to provide money to firms or governments directly through financial markets which include the stock market, the bond market, and the money market for short-term securities.

Bodie et al. (2009) described the FS using a functional rather than institutional lens and argued that functions are more stable because they change less over time and vary less across borders. Thus, Bodie et al. identified the six core functions of the FS as providing: ways to transfer economic resources through time, across borders, and among industries and business ventures; ways of managing risk by pooling investor funds which reduces the risk on an individual person or institution; ways of clearing and settling payments to facilitate trade including checking accounts, credit cards and wire transfers; mechanisms for pooling resources and subdividing ownership in various enterprises; price information to help coordinate decentralized decision-making in various sectors; and ways of addressing the incentive problems that arise as a result of asymmetry of information (p. 26).

Financial institutions evolved from mere providers of savings and checking accounts, to the innovation of credit cards which are now universal instruments for personal and corporate transactions. Increasingly, with the wide use of the internet, financial institutions are providing internet banking and other transactions which can be executed across borders through the simple use of a password. Financial innovation, therefore, was facilitated by the use of technology and, as indicated by Bodie et al. (2009), "analysis of consumer preferences and the forces of competition among financial service providers, helps one to make predictions about future changes in the financial system" (p. 36).

Critical to the operation of the FS is the application of interest rates which include: mortgage interest, commercial loan interest, and deposit interest. As indicated by Bodie et al. (2009), interest rates are a function of: the unit of account which refers to the currency or commodity used as the measure; the maturity of a fixed-income instrument which is the length of time for repayment of a loan or payment of a bond; and the default risk which is the risk of non-payment or partial payment on maturity. Risk is an inherent part of the financial system and the challenge faced by financial institutions is the effective management of risk.

Bodie et al. (2009) stated that "the legal and accounting procedures, the organization of trading and clearing facilities, and the regulatory structures that govern the relations among the users" are integral to the financial system (p. 60). Currently, the financial system is regulated by local institutions such as the Security and Exchange Commission and central banks, and international organizations such as the World Bank and International Monetary Fund (IMF). Kopcke (1995) argued that regulations that stabilize financial markets by managing the price of risk in order to foster an appropriate flow of savings and investment, rather than attempting to set absolute standards in order to judge the safety and soundness of intermediaries, best suited an efficient financial system.

4. Understanding Finance and Financial Decisions

Finance, as defined in the literature, is the study of the allocation of scarce resources over time mainly by households and firms. The distinguishing features of financial decision-making are that the costs and benefits of financial decisions are spread out over time and the decision makers do not have advance knowledge. The mechanism for implementing financial decisions is the financial system, defined as the set of markets and other institutions used for financial contracting and the exchange of assets and risks. The financial system includes the markets for stocks, bonds, and other financial instruments; financial intermediaries; and the regulatory bodies that govern all of these institutions (Bodie et al., 2009). A basic tenet of finance is that the ultimate function of the system is to satisfy people's consumption preferences, including all basic necessities of life, such as food, clothing, and shelter. Based on a study of consumer goods companies, Muldowney and Sievers (2007) asserted that finance can be viewed as providing the "innovation insurance" necessary to ensure scarce investment is spent on a portfolio of programs that really drive growth and shareholder value. Further, the finance function should partner with business leaders to inform decisions, provide insight and deliver objective, fact-based advice.

Households face four basic types of financial decisions: consumption and saving; investment; financing; and risk management decisions. The first imperative of families is finding a balance between expenditure and savings because the accumulation of wealth is tied to saving part of the family income. The savings instruments available to families are bank accounts, acquisition of real estate, or a share in a business venture, which together constitute the family assets (Bodie et al., 2009). In some countries there is the phenomenon of forced savings, and Ariely (2010) pointed to Chile where by law, 11 percent of every employee's salary is automatically transferred into a retirement account which is converted into annuities at retirement. In the absence of adequate savings, households very often have no option but to borrow from financial institutions thus incurring liabilities or debt. Lusardi and Mitchell (2011) felt that “the new financial era imposes a much heavier burden on workers and their households to become financially literate to learn how to process economic information and make informed decisions about household finances” (p. 498).

The first decision any firm must make is the choice of business sector in which it wants to operate, which introduces the process of strategic planning. Most firms stick to their core business, but increasingly, firms are branching out into related lines of business for competitive purposes. In TT, the company law views firms as having the same flexibility as individuals with the ability to choose the types of businesses they start, emphasizing the need for strategic planning. In this regard, Silvers (2006) emphasized finance's role in executing strategy which include: helping craft executable strategies that drive shareholder value; converting abstract ideas, such as shareholder value, into tangible, understandable goals; embedding finance capabilities and expertise throughout the company; fostering a disciplined, fact-based approach to decision making; and providing a steady beacon for change and transformation (p. 26).

5. Financial Statements and Analysis

The key financial statements are the balance sheet, income statement, and the cash flow which are supported by explanatory notes to aid in understanding what the figures mean. Bodie et al. (2009) indicated that the balance sheet reflected the firm's position with respect to its assets (current and non-current), and its liabilities such as debt. The balance sheet also shows the level of equity invested in the firm by owners and the extent of retained earnings. The income statement indicates whether the company is making a profit or not and is usually the first statement that attracts attention. The cash flow shows whether the firm is generating enough cash to meet obligations and especially whether receivables are being collected. Bodie et al. point out that it is possible for a company to be showing profits yet run into trouble for a lack of cash.

Financial statements form the basis on which analysts apply certain tools to gauge the performance of companies. Bodie et al. (2009) stated that financial statements serve three key economic functions: provision of information on a firm's past financial performance and current status for the use of owners and creditors; provision of a convenient way for owners and creditors to set performance targets and to impose restrictions on the managers of the firm; and provision of convenient templates for financial planning (p. 72). Ehrhardt and Brigham (2009) posited that "The real value of financial statements lies in the fact that they can be used to predict future earnings, dividends, and free cash flow" (p. 117).

Ratio analysis facilitates comparisons of a firms' performance over time and across companies and indicated that selected ratios are used to measure a firm's performance (Bodie et al., 2009, pp. 84-86). These ratios have traditionally been grouped under five headings: liquidity, asset management, debt management, profitability, and market value. Liquidity ratios show the relationship of a firm's currents assets to its current liabilities which produces its ability to meet maturing debt. The liquidity of a business firm is measured by its ability to meet its short-term cash obligations and, therefore, points to the overall solvency of the firm. The three basic measures of liquidity are: net working capital, the current ratio, and the quick (acid-test) ratio. Asset management ratios include inventory turnover, days sales outstanding, fixed assets turnover, and total assets turnover and together measure how effectively a firm is managing its assets. Debt management ratios comprise the debt ratio, times-interest earned, and EBITDA coverage ratio which provide an insight into the level of debt financing of the firm and the potential for defaulting on debt obligations (Bodie et al., 2009, pp. 83-88; Ehrhardt & Brigham, 2009, p. 138).

Profitability ratios are the most important to a firm because they indicate the long term situation of the business. The main profitability ratios are: net profit margin, return on investment (ROI), and return on equity (ROE). Net profit margin is obtained by dividing net profits after taxes by sales and is the single most critical calculation the firm can make. The ROI measures the return on total assets and is a measure of the effectiveness of management in generating profits, while the ROE indicates to shareholders the return they can earn from their investment in the firm. Market value ratios consist of the price/earnings, price/cash flow, and market book ratios and are used to relate the firm's stock price to its earnings, cash flow, and book value per share. These ratios provide management with an indication of what investors think of the company's past performance and future prospects (Ehrhardt & Brigham, 2009, p. 139).

In applying ratio analysis, Dennis (2006) suggested that liquidity, leverage, profitability, and efficiency ratios be utilized and argued that financial ratios are important tools because they "chart trends in a customer's financial performance, and point to potential problem areas that require additional scrutiny by the credit manager" (p. 62). Ogle (2008) used ratios as scorecards for measuring the relative strengths of a firm and suggested the relevant benchmarks as: net profit before taxes; current and quick ratios; and turnover ratios of accounts receivable, accounts payable, and inventory, all measured in days. Such benchmarks are the key indicators which are applicable to most enterprises including professional services firms.

6. The Financial Planning Process and Capital Budgeting

The financial planning process was described as dynamic comprising a cycle of making plans, plan implementation, and plan revision based on measured results which starts with the firm's strategic plan (Bodie et al., 2009, p. 88). The financial planning process begins with long-run, or strategic financial plans that, in turn, guide the formulation of short-run operating plans and budgets. Gitman (1987) stated that the short-run plans and budgets operationalize, or implement, the firm's long-run strategic objectives. Long-run (strategic) financial plans are orchestrated financial actions and such plans tend to cover periods ranging from two to 10 years. The use of five-year strategic plans, periodically revised in accordance with new information, is common (p. 49).

Generally, firms subject to high degrees of operating uncertainty, relatively short production cycles, or both, tend to use shorter planning horizons. Long-run financial plans take into account the following: proposed fixed-assets outlays; research and development activities; marketing and production development actions; and major sources of finance. Short-run (operating) financial plans are planned financial actions which cover one to two year periods and the key inputs include sales forecast, and other operating and financial data. The outputs include the operating budget, the cash budget, and pro forma financial statements (Gitman, 1987, pp. 149-150).

A financial planning model was elaborated by Ehrhardt and Brigham (2009) as comprising the following actions: projecting financial statements to analyze the effects of the operating plan on projected profits and financial ratios; determining the needs to support a 5-year plan; forecasting the funds to be generated internally and identifying external sources of funding but subject to constraints due to borrowing covenants such as restrictions on the debt ratio, the current ratio, and the coverage ratios; establishing a performance-based management compensation system that rewards employees for creating shareholders wealth; and monitoring operations after plan implementation, identifying the cause of any variances, and taking corrective actions. (p. 402).

The management of working capital is critical to any financial planning model and Bodie et al., (2009) argue that a firm must "minimize the amount of the firm's investment in nonearning assets such as receivables and inventories and maximize the use of "free credit" such as prepayments by customers, accrued wages, and accounts payable" (p. 95). Working capital management is critical to small firms which constantly need to monitor collection of payments, an ongoing challenge for many small businesses.

Capital budgeting is an essential element of financial planning and according to Bodie et al., (2009), "the basic unit of analysis in the capital budgeting process is the individual investment project" which starts "with an idea for increasing shareholder wealth by producing a new product or improving the way an existing product is produced" (p. 171). The process involves analyzing the original concept, collecting information to assess the costs and benefits of implementation, and formulating an implementation strategy. Truong, Partington, and Peat (2008) in a survey of the capital budgeting practices of Australian companies confirmed that net present value (NPV), internal rate of return (IRR), and payback were the most popular evaluation techniques with discounting based on the weighted average cost of capital which is held constant for the life of the project. Verma (2009) in a survey of Indian manufacturing companies found that NPV was favored by large companies, but small companies used the payback method, however the payback period was a supplementary technique irrespective of size. Verma also pointed out that companies needed to account for the risk of unexpected inflation, interest rate risk, commodity price risk, and foreign exchange risk (p.8)

Sensitivity analyses are a proven technique in financial planning, and according to Bodie et al. (2009), "sensitivity analysis in capital budgeting involves testing whether a project remains attractive even if some of the underlying variables turn out to be different from the assumptions" (p. 178). The process involves consideration of alternative scenarios in which income and/or expenses are varied to gauge the impact on net profit. Critical to sensitivity analyses is the calculation of the break-even point which is the point of indifference between accepting and rejecting a project (Bodie et al., 2009, p. 178).

7. Financial Planning and the Competitive Firm

Gitman (1987) suggested that a competitive firm must focus on cash planning and the cash budget or cash forecast is at the heart of this process. A firm expecting a cash surplus needs to plan short-term investments (marketable securities) while a firm anticipating cash shortages must arrange for short-term (notes payable) financing. The cash budget gives the financial planners a clear view of the timing of the firm's expected cash inflows and outflows over a given time period. The most critical component of cash planning for the competitive firm is the sales forecast because this forecast is used to estimate monthly cash flows resulting from projected sales; and production-related, inventory-related, and sales-related outlays. Usually, a combination of these forecasts is used in making the final forecast (Gitman, 1987, pp. 151-152).

Murray (1992) suggested that a firm should create a mission plan and distinguished among the strategic plan, the tactical plan, and the budget. The strategic plan incorporates the projects and activities the firm plans to undertake and informs such decisions as: when to borrow; when to seek equity; market expansion; developing new business ventures; and undertaking large capital expenditure. The tactical plan is normally two to five years duration and is developed quarterly to address a specific need such as cash flow management, or when to commence a capital project. Murray suggests the budget is the cornerstone of financial planning and placing the budget process in a wider framework of a tactical model, makes it possible to expose the shortfalls of budgeting assumptions that are often hidden within the politics of organizational positioning (p. 33). Murray concluded that "When the processes of planning and control become blurred, the plan degenerates from an image of possibilities to a mirror of the anxieties and fears of management itself" (p. 35).

A researcher argued argues that "the budget has become a strategic business plan in itself, analyzed and updated regularly ….. in the form of monthly forecasts and sliced and diced to allow various views into the company's operations, performance, and future direction" (Orlando, 2009, p. 49). The budget has assumed great importance in financial planning in that, according to Orlando, it has become: a cash flow management tool; a forecasting tool; a reporting/disclosure mechanism; the tool for measuring progress; a factor in compensation; and a crystal ball (p. 50). In order to embed the budget planning process within a company, the following actions were recommended: evaluate the process to ensure it is streamlined, simple, and clear; upgrade technology; communicate how the budget supports the achievement of corporate strategy and goals; explain the process, timetable, assumptions, and responsibilities; train and educate; collaborate with all department heads; and follow through by providing tailored reports for managers for monitoring performance (Orlando. 2009, p. 51). The main implication of these decision options is that a competitive firm whose sales are relatively stable can safely take on more debt and incur higher fixed charges, while a firm with less operating leverage is better able to employ financial leverage because of less business risk and less volatile earnings.

8. Market and Industry Fluctuations: Implications for the Firm

Herremans, Isaac, and Bays (2007) advised that among the resources that should be targeted by the firm in situations of market and industry fluctuations are the intellectual capital elements (ICEs) of the firm. The ICEs represent the know-how borne in the minds of an organization's employees as well as processes and relationships. Herremans et al., devised an intellectual capital realization process (ICRP) was devised to identify a firm's ICEs and the critical ICEs were identified as: technical knowledge (41%); marketing (36%); concept formulation (9%); team psychology processes (5%); knowledge management support systems (5%); and communications (4%) (Herremans et al., p. 31).

Firms can make serious financial blunders in their corporate financial planning and seven ways to avoid such mistakes were suggested as: clarify the business plan in view of the complex changing business models; use a cooperative approach involving all business units; manage earnings expectations by choosing a level that can be surpassed; fix the performance measurement system so it delivers the information management needs; slash the detail by focusing on the crucial planning variables; crystallize financial reports by increasing transparency; and use automation effectively by installing the appropriate software (Anonymous, 2004, pp. 12-14).

Critical to the question of market and industry fluctuations is the selection of the planning period and Mills (1995) asserted that the dynamics of competition within the marketplace demand the selection of an appropriate planning period. The reason offered by Mills is that “the further forward the planning period can be projected, the greater its contribution to value and the lower the proportion left to the vagaries of a continuing value calculation” (p. 42). Mills (1995) further stated that strategic thinking should focus on what makes firms different and the relative performance within an industry is a more important source of profit then the industry itself. In this context, Kay (cited in Mills, 1995) identified four types of capabilities in a business: reputation building which allows a firm to charge higher prices or gain larger market share; architecture design which takes account of the relationships among employees (internal architecture), with suppliers and customers (external architecture), and relationships with groups engaged in related activities (networks); innovation as a source of competitive advantage; and strategic assets.

9. Real-World Issues and Financial Literacy in Developing Economies

The critical real-world issues in the area of finance that impact emerging countries are highlighted in this paper as: structure of the FS; project analysis of major development initiatives; financial decisions; social responsibility of firms; and the level of financial literacy among the population. The country of TT is classified by the World Bank as a high income developing country, and in the context of this paper, the FS accounts for approximately 12 per cent of GDP and is of great significance in the economy because of close linkages with the real sector. In terms of the structure of the FS in TT, commercial banks lead with 45 percent of total assets in 2013 followed by insurance companies with 16 percent, occupational pension funds with 13 percent, and with other institutions such as the national security organization (NIB), the Unit Trust Corporation, credit unions, non-bank financial institutions, development banks, and the Deposit Insurance Corporation comprising the remainder of the financial sector assets (CBTT, 2014).

The CBTTs stated mandate is to secure the financial stability and to maintain confidence in, and promote safety and soundness of, the domestic FS. At the operational level, the FS is subject to specific vulnerabilities including: heavy dependence on the energy sector for income and foreign exchange amounting to 85 per cent of export earnings because only limited success in economic diversification has been achieved by 2015; high level of household indebtedness with consumer debt standing at $4 billion in 2013; historically low domestic interest rates which have negatively impacted profitability and asset growth across the financial system; and rising financial interconnectedness in the Caribbean which heightens the risk of contagion and spillovers to its economy and financial sector from regional shocks (CBTT, 2014).The potential risks to the FS of TT are represented graphically in

Table 1 which shows the probability and impact of the key risks ranging from low, moderate, elevated, high, and very high.

Table 1: Key Risks to Financial Stability in TT

RISKS	Probability	Impact
Risk 1: Sharp and Persistent Fall in Energy Prices		
Risk 2: Household Financial Stress and a Correction in House Prices		
Risk 3: A Spike in Long-Term US Interest Rates		
Risk 4: Sovereign Debt Restructuring in the Caribbean		

Low	Moderate	Elevated	High	Very High

Source: CBTT, Economic Stability Report 2014.

The system of project analysis rests on the generation of projected cash flows and an evaluation of their effect on the market value of shareholders' equity. The main technique employed to evaluate streams of cash flows is the NPV in which the cash flows are discounted using a selected rate of interest to account for the time value of funds received at different periods. According to Bodie et al. (2009), the NPV is the expected increase in the wealth of a firm's shareholders, and the general rule is that investment projects are approved when the NPV is positive. Bodie et al. also highlighted the need for taking the impact of inflation into account in projecting cash flows.

Bodie et al. (2009) explained that projects may also be mutually exclusive in that a firm has to choose one project over another, and a practical example is that of a firm which evaluated whether to construct a building for rent or erect a multi-storey parking garage. The mutually exclusive matter was resolved by the decision to build the parking garage with small rental outlets on the first two floors to enhance the viability with parking on four floors above. Bodie et al. (2009) stated that in all cases the project with the higher NPV should be selected, although some companies use IRR which is the rate of discount that that reduces the NPV to zero. This measure is not a suggested measure for mutually exclusive projects because a project's IRR is independent of scale and does not present a comparable situation. In this regard, Ehrhardt and Brigham (2009) noted however, that managers prefer IRR which led to the development of a modified IRR (MIRR) which "involves finding the terminal value of the cash flows, compounded at the firm's cost of capital, and then determining the discount rate that forces the present value of the terminal value to equal the present value of the outflows" (p. 347).

Financial leverage is also a very relevant issue for firms in the real world and three alternative methods available for estimating the NPV of an investment project to take account of financial leverage were outlined as: the adjusted present value (APV) which is equal to the project's unlevered present value (PV) plus the present value of the interest tax shields gained from additional debt financing; the flows to equity (FTE); and the weighted average cost of capital (WACC) which is an estimate of the project's PV by discounting the expected unlevered after tax cash flow and then subtracting the full investment outlay (Bodie et al., 2009, pp. 451-454). The implications for a firm's use of financial leverage are: stockholders can maintain control without increasing their investment; if a firm earns more on investments financed by borrowings, shareholders' returns are increased but risk is also increased; and the higher proportion of owner equity, the lower is the credit risk (Ehrhardt & Brigham, 2009, p.123).

In the real world, financial decisions involve trade-offs, and Bodie et al. (2009) indicated that a firm which is incurring losses and therefore is not liable to pay corporate income taxes, will view a situation of trade-off of tax benefits and costs of financial distress very differently from a firm that is liable for taxes (p. 449). There are five main financing methods employed by firms which Bodie et al. outlined as: loans from friends or relatives; leasing arrangements; issuing common stock; debt with warrants; and factoring receivables. Loans from friends and family and leasing, is a common method used by small and medium enterprises in order to reduce initial capital expenditure. Firms issue common stock usually when making an initial public offering (IPO) or when undertaking a major expansion. Warrants are call options which provide its owners with the right to purchase an issuing company's stock at a fixed price and are attached to a debt issue from firms raising new equity. Factoring involves selling accounts receivable at a discount to a financial institution. The firm receives cash and the factor waits until the receivable is due for collection (Bodie et al., 2009, pp. 450-451).

An issue of increasing relevance to financial institutions and the functioning of the entire financial system especially in emerging countries is social responsibility. Ogola (2012) studied the social responsibility of financial firms in developing countries with a focus on Sub-Saharan Africa. Ogola formulated a list of the main indicators of social responsibility of financial institutions comprising: "low interest on loans; small loans; micro-savings; income equality; marketing equality; geographical equality; and unbiased financial education" (p. 116). These indicators of social responsibility are highly relevant to most developing countries

This paper specifically highlights the issue of financial literacy which has been the subject of considerable research in advanced countries but is an under-research area in developing and emerging countries but is viewed as critical to the overall economic development of any country. There are several definitions of financial literacy but this paper adopts the definition utilized in Australia and cited by Worthington (2013) as "the ability to make informed judgements and to take effective decisions regarding the use and management of money" (p. 230). Worthington reviewed several financial literacy programs in Australia but concluded that efforts to improve financial literacy among the population had proven elusive and can be viewed as largely promotional (pp. 236-237).

Mouna and Anis (2013) addressed the complexity of the interconnection between financial information and the decision making ability of individuals in an organizational setting in Tunisia. The investigation concluded that a low level of understanding of financial matters existed in organizations which pointed to a need for training of persons outside the finance departments. Asaad (2015) viewed financial literacy as linked to financial knowledge and financial confidence which were considered critical to sound decision making (p. 102). The author's assessment was that persons with great knowledge and confidence were likely to make superior financial decisions than persons with low knowledge and confidence which led to the suggestion that educational was vital to instilling confidence in individuals and should be introduce on a broad basis (p.114). This condition was supported by Nkundabanyanga et al., (2014) who argued that persons who were less financially literate encountered greater challenges in "debt management, savings and credit, and are less likely to plan for the future" (p. 346).

In reviewing financial literacy around the world, Lusardi and Mitchell (2011) came to the following conclusions: financial literacy is very low despite the level of market development; sex and age difference exist with women tending to have less knowledge than men; older people are also possess less financial knowledge and are thus more vulnerable; little retirement planning is pursued; people who understand risk diversification are more likely to undertake retirement planning; and that financial literacy is a major determinant of action towards retirement planning (p. 506). In relation to developing countries, Kefela (2011) studied the implications of financial literacy in developing countries and focused on the role of banks in promoting financial literacy which, in turn, would improve access to finance eventually benefitting the banks in addition to the general society (p. 3699). Based on an examination of the situation in Kenya and Uganda, Kefela concluded that financial literacy is important to "the soundness and efficiency of the financial system and to the performance of the economy" (p. 3704).

A novel study was conducted by Wise (2013) who investigated the impact of loan default and involuntary closure in relation to new venture survival and concluded that the lack of financial management can be attributed to the low level of new venture formation and the high failure rate of small and medium enterprises (SMEs) (p. 31). Wise drew the link between an entrepreneur's knowledge of financial statements and the relevance of financial ratios and the frequency with which such financial information was generated, and the repayment of loans and business failure. The availability of financial data pointed to on-time loan repayment and lower business failure of SMEs. The work of Wise (2013) could easily have formed the basis for the financial literacy initiative launched in TT in the same year which tried to avoid the elusiveness trap of mere promotional value pointed by Worthington (2013).

In this respect, the efforts to promote broad-based financial literacy in TT have been restricted to the efforts of the central bank (CBTT) through its financial inclusion and education training institution designated the Financial Inclusion Development Agency (FIDA). This initiative was triggered in March 2013 when the bank signed the Maya Declaration on Financial Inclusion, and became the 100th member of the Alliance for Financial Inclusion. FIDAs main objective is to promote the development of sustainable financial inclusion strategies, financial literacy programs and outreach services premised on the commitment to education as a powerful mechanism for addressing social ills. The CBTT stated position is to pursue its function of empowering citizens of TT through financial management education with an emphasis on the socially disadvantaged. The main driver of the financial literacy initiative is to "close the gap separating the financially excluded or illiterate, and to produce citizens more capable of making sound financial decisions that will enhance their standard of living" (CBTT, 2015). The financial literacy programs are delivered through educational sessions, seminars, and workshops from which participants can earn a certificate or diploma in financial education. This paper proposes that this approach be promoted as a relevant model for financial literacy programmes in small developing countries.

10. Conclusion

The main aim of this paper is to serve as an introduction to the key concepts governing the nature of the FS. The paper targets tertiary level business students who are viewed as the vehicles for transmitting an understanding of the concepts to their peers. Financial matters are viewed as complex by many non-financial persons and its operations defy most people in emerging countries. The study of finance and the impacts of financial decisions are wide ranging and contribute significantly to the wealth and happiness of families and the survival or demise of firms. Because of the increasing complexity of financial systems, both individuals and firms must gain an understanding of: how the system operates; the tools of financial analysis; the concept of NPV; how to construct a financial planning model; the nature of capital budgeting decisions; project analysis and ranking of projects; and the practice of real-world financial decision making. Understanding these issues is indispensable to firm competitiveness.

In the context of the discussion on financial planning, the conclusion is that firms wishing to compete nationally and internationally must adopt a clear system of financial planning with due emphasis on budgeting. Understanding the impacts of leverage on the financial statements is indispensable for all managers operating in a competitive environment. Market and industry fluctuations have become the norm in the globalized business environment; therefore competitive firms must target their resident intellectual capital, planning processes, and overall architecture for sustainable operations.

As a particularly critical issue for developing countries, the need to promote financial literacy is an overwhelming imperative for achieving economic and social progress. The CBTTs initiative at financial inclusion has the potential to act as a model for major business corporations, especially banks, which can execute a similar initiative through their respective associations. In order to strengthen the model and sustain the activity, a collaborative arrangement is vital and will be a powerful example for the 14 member countries of the Caribbean Single Market and Economy which is experiencing delayed implementation of the economic integration promise.

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