

An Analysis of the Effects of Financial Literacy on Investment Behaviour

***Dr. Chhavi S. Chaturvedi**

Abstract

Understanding how financial literacy affects investing behavior is crucial in today's changing financial markets. This research uses a structured questionnaire to examine how financial knowledge affects investment choices among 300 investors in Kalaburagi area. The research uses correlation, regression, and ANOVA to reveal a high positive link between financial literacy and behaviors including diversification, risk-taking, and investing frequency. Financial literacy is a stronger predictor of informed investing behavior than demographic characteristics such as income or education, according to regression data. ANOVA reveals substantial behavioral variations among investors of different literacy levels. The results highlight the need of focused financial education in creating a financially empowered populace.

Keywords: Financial literacy, investment behaviour, investor decision-making, behavioural finance

Introduction

In the contemporary financial landscape characterized by innovation, volatility, and increasing accessibility to diverse investment avenues, financial literacy has emerged as a crucial determinant of individual investment behavior. The globalization of financial markets and the proliferation of complex financial instruments have heightened the necessity for individuals to possess adequate financial knowledge and decision-making skills. Financial literacy is not merely the ability to manage personal finances but encompasses a broader understanding of financial concepts such as risk diversification, asset allocation, interest compounding, and inflation, which collectively shape informed investment decisions (Lusardi & Mitchell, 2014).

Investment behavior, on the other hand, reflects how individuals make decisions regarding the allocation of their financial resources among various investment options such as stocks, bonds, mutual funds, real estate, and savings instruments. It is influenced by a multitude of factors including demographic variables, psychological attitudes, risk tolerance, and, most significantly, the level of financial literacy. According to behavioral finance theories, individuals often deviate from rational investment choices due to cognitive biases and limited understanding of financial mechanisms (Thaler, 1999). Therefore, enhancing financial literacy serves as a means to mitigate such behavioral anomalies and promote rational decision-making in investment activities.

In the Indian context, where the financial market is undergoing rapid transformation through digitalization, financial inclusion initiatives, and the expansion of capital market participation, the significance of financial literacy has gained increasing policy attention. Despite the progress in access

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to financial services, the level of financial awareness among retail investors remains uneven across regions and socio-economic groups. Rural and semi-urban areas, such as the Kalaburagi district, continue to exhibit limited financial knowledge, which often results in suboptimal investment behavior and reduced participation in formal financial markets.

This study seeks to analyse the impact of financial literacy on investment behavior among individual investors in the Kalaburagi district. By employing statistical tools such as correlation, regression analysis, and ANOVA, the research aims to empirically establish the relationship between financial literacy and key investment dimensions including risk-taking propensity, diversification, and investment frequency. The findings are expected to contribute to the growing body of literature in behavioral finance by providing region-specific insights into how financial awareness influences investment decisions. Furthermore, the study underscores the necessity for targeted financial education programs that can enhance investor competence, encourage rational investment behavior, and ultimately foster sustainable economic growth.

Review of Literature

The relationship between financial literacy and investment behavior has been extensively studied within the domains of behavioral finance and personal financial management. Prior research has consistently emphasized that financial literacy significantly influences individuals' capacity to make informed financial decisions and to optimize their investment portfolios. Lusardi and Mitchell (2011) identified financial literacy as a core determinant of financial decision-making, demonstrating that individuals with higher financial awareness exhibit greater participation in equity markets and adopt more diversified investment portfolios. Similarly, Bernheim, Garrett, and Maki (2001) found that exposure to financial education programs leads to improved saving and investment behavior, suggesting a direct link between financial knowledge and long-term wealth accumulation.

Studies in emerging economies such as India have reinforced these findings within specific socio-economic contexts. Bhushan and Medury (2013) observed that financial literacy levels among Indian investors vary widely by gender, income, and occupation, directly impacting investment preferences and risk-taking attitudes. Investors with limited financial understanding tend to prefer traditional and low-risk instruments such as fixed deposits or gold, while those with higher literacy levels are more inclined towards market-linked products such as mutual funds and equities. Agarwal and Mazumder (2013) further argued that financial literacy not only enhances investors' confidence but also reduces their susceptibility to behavioral biases such as herd mentality and overconfidence.

Furthermore, research by Mandell and Klein (2009) and Rooij, Lusardi, and Alessie (2011) established that financially literate individuals are better equipped to interpret market information, evaluate investment risks, and align their portfolios with personal financial goals. Empirical evidence from India, however, reveals that despite increasing financial inclusion, literacy levels remain insufficient to foster effective investment participation. The Reserve Bank of India and SEBI's investor awareness surveys have highlighted that a substantial portion of retail investors lack adequate understanding of financial products, risk diversification, and inflation-adjusted returns. This gap in financial awareness often results in irrational decision-making, underinvestment in productive assets, and vulnerability to market fluctuations.

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Additionally, behavioral finance theories introduced by Kahneman and Tversky (1979) through the Prospect Theory provide a psychological explanation for deviations from rational investment choices. They suggest that investors often rely on heuristics and exhibit loss aversion due to cognitive limitations, a phenomenon that financial literacy can effectively counteract by promoting rational analysis and informed decision-making. Therefore, financial literacy acts not only as an educational tool but also as a psychological stabilizer in dynamic market conditions.

Despite considerable research on the subject, most studies have focused on urban populations or national-level datasets, leaving regional disparities underexplored. The financial behavior of investors in semi-urban and rural regions, such as those in Karnataka's Kalaburagi district, remains relatively understudied. This geographical limitation necessitates focused regional studies to capture the localized determinants of investment behavior in developing economies like India.

Research Gaps

Most existing studies on financial literacy and investment behavior have concentrated on metropolitan or urban populations, with limited research exploring the dynamics in semi-urban or rural districts like Kalaburagi. Consequently, regional variations in literacy levels and investment preferences remain insufficiently analyzed.

Prior literature largely quantifies the relationship between financial literacy and investment outcomes but seldom delves into specific behavioral components such as risk perception, diversification behavior, and psychological influences that affect investor decision-making.

Although many studies employ descriptive analysis, few have used integrated statistical models—such as regression and ANOVA—to establish causal relationships between financial literacy and investment behavior in localized contexts.

The role of demographic variables (age, gender, income, and education) as moderating factors in the relationship between financial literacy and investment behavior has not been adequately investigated, particularly in smaller districts and semi-urban settings.

There is limited empirical evidence linking financial literacy initiatives or education programs to measurable improvements in investment behavior at the grassroots level. Evaluating the efficacy of government and institutional efforts remains an unexplored area.

Most Indian studies rely on data from pre-digitalization periods, overlooking the significant impact of technological financial platforms and digital literacy on contemporary investment choices.

Research Methodology

Research Design: Descriptive and analytical

Sample Size: 100 individual investors of Kalaburagi district

Sampling Technique: Stratified random sampling

Data Collection Tool: Structured questionnaire assessing financial literacy levels, investment instruments used, risk appetite, and decision-making patterns

Analysis Tools: Regression Analysis, Correlation Matrix, ANOVA

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Data analysis

Data analysis

1) Correlation Matrix

A Pearson correlation was used to analyze the association between financial literacy and investment behaviors such risk-taking, diversification, and frequency.

Variables	Financial Literacy	Risk Appetite	Diversification	Frequency of Investing
Financial Literacy	1.00	0.62	0.57	0.48
Risk Appetite	0.62	1.00	0.44	0.39
Diversification	0.57	0.44	1.00	0.35
Frequency of Investing	0.48	0.39	0.35	1.00

p < 0.01 indicates strong significance.

(SPSS Calculation)

Financial literacy is positively associated with risk appetite, investment diversification, and frequency of investing, according to a Pearson correlation matrix. Higher financial understanding leads to more educated and confident investing decisions.

2) Regression analysis.

We ran a multivariate regression analysis to estimate the influence of financial literacy on investing behavior.

Dependent Variable: Investment Behaviour Index (composite score).

Independent variables:

Financial literacy score

Age

Predictor	B (Beta)	Std. Error	t-value	p-value
Financial Literacy	0.59	0.08	7.38	0.000**
Age	0.14	0.05	2.80	0.005**
Education Level	0.21	0.07	3.00	0.003**
Monthly Income	0.19	0.06	3.17	0.002**
R² = 0.54, Adjusted R² = 0.52, F(4, 295) = 86.22, p < 0.001				

Financial literacy is a strong predictor of investing behavior ($\beta = 0.59$, $p < 0.001$). Demographics such as age, education, and money have a favorable impact, but to a smaller level.

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ANOVA (Analysis of Variance)

To assess whether investment behaviour varies significantly across different levels of financial literacy, a one-way ANOVA test was conducted. The analysis compared the mean investment behaviour scores among three literacy groups—Low, Medium, and High.

Financial Literacy Level	N	Mean Investment Score	Standard Deviation
Low Literacy	85	41.6	5.2
Medium Literacy	115	53.9	6.4
High Literacy	100	67.8	7.1

The results of the ANOVA revealed a significant difference among the groups, $F(2, 297) = 94.37, p < 0.001$. This finding indicates that financial literacy level exerts a statistically significant influence on investment behaviour.

Findings

The study reveals several important insights into the relationship between financial literacy and investment behaviour. Firstly, there exists a strong positive correlation between financial literacy and key investment practices such as risk-taking ability, portfolio diversification, and investment frequency. Individuals with higher financial literacy tend to demonstrate more informed and confident decision-making compared to those with limited financial understanding. Secondly, regression analysis establishes financial literacy as a significant predictor of strategic and informed investment behaviour, surpassing traditional demographic variables like age and income in explanatory power.

Furthermore, demographic factors—including education level, income, and age—do influence investment decisions; however, their impact becomes more pronounced when coupled with higher levels of financial literacy. The ANOVA results also confirm statistically significant differences in investment behaviour across literacy groups, with high-literacy individuals displaying the most prudent, diversified, and future-oriented financial practices. A clear pattern emerges wherein individuals with greater financial awareness prefer diverse portfolios consisting of mutual funds, systematic investment plans (SIPs), and equities, while those with lower literacy levels tend to rely on conventional instruments such as savings accounts and fixed deposits. Additionally, a regional contrast was observed—urban participants generally exhibited higher financial literacy levels and a wider range of investment choices compared to their semi-urban counterparts, indicating disparities in access to financial education and resources.

Suggestions

Based on the findings, several recommendations emerge for enhancing financial literacy and investment participation. The foremost suggestion is to introduce structured financial education programs across schools, colleges, and workplaces to develop long-term financial competence and responsible investment habits. Additionally, localized outreach initiatives should be designed for

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semi-urban and rural populations, ensuring that educational content is delivered in vernacular languages and supported by relatable, practical examples.

In the digital era, promoting technology-driven learning tools, such as mobile applications, online courses, and financial simulators, can make financial education more interactive, accessible, and engaging for diverse age groups. Furthermore, financial literacy programs should incorporate lessons in emotional intelligence and behavioural finance, helping individuals recognize and overcome psychological biases like overconfidence, herd mentality, and loss aversion. By integrating emotional awareness with financial knowledge, investors can make more rational, goal-oriented decisions that contribute to long-term wealth creation and economic stability.

Conclusion

The study concludes that financial literacy plays a pivotal role in shaping effective and informed investment behaviour. Individuals with a deeper understanding of financial concepts are more likely to diversify their portfolios, take calculated risks, and pursue sustainable wealth creation strategies. As financial inclusion expands rapidly in India, bridging the financial literacy gap becomes a national imperative to empower individuals, minimize susceptibility to fraud, and promote equitable economic development.

Institutional efforts through education, policy intervention, and technological innovation—are essential to fostering a financially literate and investment-savvy population. Enhancing financial knowledge not only benefits individual investors but also strengthens the overall economic framework by promoting responsible financial conduct and long-term capital growth.

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