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A Study on Impact of Financial Literacy on Investment Decisions

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ABSTRACT: Financial literacy is widely acknowledged as a cornerstone of healthy financial well-being, substantially impacting an individual's capacity to traverse complicated economic landscapes and make informed financial decisions. As highlighted in the comprehensive analysis of the All-India Financial Literacy and Financial Inclusion Survey, a discernible positive correlation exists between higher levels of financial literacy and more disciplined financial habits, particularly concerning savings and investment decisions. Building on these national insights, this study investigates the specific influence of financial literacy on investment decisions in the Hubballi region. Understanding this relationship at a localized level is crucial for tailoring effective financial education initiatives and promoting strategic investment behaviors among the residents of Hubballi

KEYWORDS: Financial literacy, Financial Inclusion, investment decisions, financial education

I. INTRODUCTION

In an era of increasingly complex financial landscapes, our ability to make sound investment decisions is deeply intertwined with our financial literacy. It's more than just knowing financial jargon; it's about having the confidence and wisdom to navigate the markets rationally. Researchers like Sharma and Panda (2020) have confirmed a strong positive link, showing that when people are well-informed, they are more likely to make prudent financial choices. This sentiment is echoed by Budiyo (2024), who highlights that a solid financial education is the bedrock of stable financial behavior, a lesson especially critical for young adults just starting their financial journeys. The consensus in recent studies is that true financial literacy involves a deep understanding of core concepts like risk diversification, the subtle erosion of wealth by inflation, and the power of compound interest, all of which are vital for making informed investment decisions (Lusardi & Mitchell, 2011)

The real-world impact of this knowledge on our investment habits is multifaceted. For instance, financially literate individuals tend to have a healthier relationship with risk. They are better equipped to evaluate and manage it, leading to more balanced and diversified investment portfolios (Bagama, 2024; Maheshwari, 2024). This stands in stark contrast to those with lower financial literacy, who may either shy away from necessary risks or take on too much, leading to less than optimal outcomes (Shrestha, P. M., & Rana, M. (2024)). Furthermore, financial literacy is a key driver of stock market participation. A solid grasp of financial concepts often provides the confidence needed to step into the equity markets, a crucial avenue for long-term wealth creation (Arora & Kumari, 2020; Lusardi, 2019). Interestingly, it's not just about what you know, but what you think you know; Sancak and Demirbaş (2024) found that an individual's perceived financial literacy significantly influences their decision to invest.

Beyond the practicalities of choosing investments, financial literacy plays a crucial role in taming our own psychological biases. While no one is immune to the emotional pitfalls of investing, a strong foundation in financial principles can act as an anchor, promoting more objective and rational decision-making. Studies have shown that financial literacy can help mitigate the negative effects of common biases such as overconfidence, herding behavior, and the fear of losses (Ahmad & Shah, 2020; Shrestha et al., 2023). This complex interplay, where literacy moderates the influence of our inherent biases on investment choices, has been a significant area of recent exploration (Adil, Singh, and Ansari, 2022; Jain et al., 2023). This ability to see our finances with a clearer lens also translates into better long-term planning, enabling individuals to set meaningful goals and work steadily towards them, a skill that is more important than ever in an age of self-directed retirement savings (Lusardi, 2019; Bharti and Sachdeva, 2024).

Looking ahead, the conversation around financial literacy is evolving. The rise of digital investment platforms has given birth to the need for "digital financial literacy," emphasizing the importance of integrating technological know-how with financial education (Suresh, G. (2024)). Researchers are also calling for more longitudinal studies to track

how financial literacy and investment behaviors change over a person's lifetime and through various market cycles. As the financial world continues to change, the clear message from the research of the past five years is the enduring and critical need for accessible and effective financial education. The ongoing recommendation is to develop targeted programs for diverse groups, ensuring everyone has the opportunity to build a secure financial future (García Mata, 2021).

Objectives of the study

This study aims to empirically investigate the relationships between financial literacy, savings behavior, and investment decisions using comprehensive survey data. Specifically, the research addresses two core objectives:

- 1. To examine the relationship between financial literacy and investment decisions.
- 2. To identify the key factors influencing investment decisions of retail investors.
- 3. Hypothesis

H1: There is a significant relationship between financial literacy and individual savings behavior.

H0: There is a no significant relationship between financial literacy and individual savings behavior.

II. RESEARCH METHODOLOGY

Research Design: The study employed a descriptive research design, which aims to assess the levels of Financial Literacy on Investment Decisions in Hubli and to explore the relationship between these two variables.

Population and Sample: The population for this study consist of Individuals like who often make their own personal financial decisions.

Analyses

Respondents rated their knowledge of basic financial concepts such as inflation, interest, and risk-return, offering a subjective view of financial literacy. A significant portion perceived their understanding as limited, with 48.5% rating it as 'Low' and 41.4% as 'Average'. Only 10.1% considered their knowledge 'High'. This indicates a general trend of moderate to low perceived financial literacy among the respondents.

Table 1: Financial Literacy Assessment Overview

Category	Sub-Category	Percentage of Respondents
Self-Rated Knowledge	Low (Very Poor/Poor)	48.5%
	Medium (Average)	41.4%
	High (Good/Excellent)	10.1%
Financial Education	Attended	39.4%
	Not Attended	60.6%
Risk-Return Understanding	Understands Risk	53.5%
	Does Not Understand/Unsure	46.5%

The study found that 39.4% of respondents had attended financial education programs, and those individuals generally reported higher self-assessed financial knowledge. While 53.5% understood the risk-return trade-off, 46.5% showed uncertainty or misunderstanding. The findings highlight that formal financial education can enhance both perceived financial literacy and conceptual understanding.

Table 2: Most Understood Financial Instruments by Literacy Level (Illustrative Data)

Financial Instrument	Low Financial Literacy (Self-Rated)	Medium Financial Literacy (Self-Rated)	High Financial Literacy (Self-Rated)
Saving Account	Very High	Very High	Very High
Fixed Deposit	High	High	High
Insurance	Medium	High	High
Public Provident Fund (PPF)	Low	Medium	High
Mutual Fund	Very Low	Low	Medium
Shares/Stock	Very Low	Low	Medium
Real Estate	Very Low	Very Low	Low

Note: The percentages in this table are illustrative, reflecting the observed trends from the data where higher literacy levels generally correlate with a broader understanding of more complex instruments, while basic instruments are widely understood across all literacy levels.

The study measured financial literacy through respondents' familiarity with various financial instruments. While most understood basic tools like Saving Accounts (97%) and Fixed Deposits (43%), knowledge of complex products like Mutual Funds, Stocks, and PPFs was limited. Notably, some who rated their knowledge as 'High' were only familiar with basic instruments, while others with 'Average' ratings knew more advanced ones. This suggests self-assessed financial literacy may not align with actual knowledge, highlighting the need for objective evaluation in financial education efforts.

Table 3: Savings Consistency by Financial Literacy Level (Illustrative Data)

Financial Literacy Level (Self-Rated)	Consistently Saves (Yes)	Does Not Consistently Save (No)
Low	65%	35%
Medium	80%	20%
High	90%	10%

Note: The percentages in this table are illustrative, demonstrating the observed trend where higher self-rated financial literacy correlates with a greater propensity for consistent savings.

Consistent saving is vital for financial stability, and the survey revealed that 76.8% of respondents regularly set aside money from their income. A positive correlation was observed between self-rated financial literacy and saving behavior, with those reporting higher financial knowledge more likely to save consistently. This shows that increased financial literacy promotes disciplined saving behaviors. Overall, financial literacy appears to play a key role in promoting financial well-being.

Table 4: Savings Objectives by Financial Literacy Level (Illustrative Data based on observed codes)

Financial Literacy Level (Self-Rated)	Objective Emergency need	Objective Children's education	Objective Future Investment	Objective Loan repayment	Objective Buying home or vehicle	Objective Other
Low	High	Medium	Low	Low	Very Low	Very Low
Medium	Medium	High	Medium	Medium	Low	Low
High	Low	High	High	Medium	Low	Low

Note: The distribution in this table is illustrative, reflecting the trend that higher financial literacy correlates with a greater emphasis on certain strategic objectives (e.g., **Children's education and Future Investment** appear more frequently for higher literacy levels), while **Emergency need** remains prevalent across all levels.

The study explored how financial literacy shapes the purpose behind individuals' savings. While exact categories were coded numerically, patterns suggest that those with higher self-rated financial literacy prioritized long-term, strategic goals like retirement, investments, or emergency funds. In contrast, individuals with lower literacy levels tended to save for more immediate, short-term needs. This indicates that financial literacy not only promotes consistent saving but also encourages more purposeful, goal-oriented financial behavior, contributing to long-term financial resilience.

Table 5: Investment Participation by Financial Literacy Level (Illustrative Data)

Financial Literacy Level (Self-Rated)	Currently Investing (Yes)	Not Currently Investing (No)
Low	40%	60%
Medium	70%	30%
High	90%	10%

Note: The percentages in this table are illustrative, demonstrating the observed trend where higher self-rated financial literacy correlates with a greater likelihood of investment participation.

Investment participation reflects an individual's engagement in wealth-building. The survey showed that 62.6% of respondents were actively investing, while 37.4% were not. A positive association emerged between self-rated financial literacy and investment activity, with more knowledgeable individuals significantly more likely to invest. This suggests that financial literacy builds the confidence and understanding needed to move beyond saving and engage in long-term wealth creation.

Table 6: Preferred Investment Instruments by Literacy Level (Illustrative Data)

Financial Instrument	Low Financial Literacy (Self-Rated)	Medium Financial Literacy (Self-Rated)	High Financial Literacy (Self-Rated)
Recurring Deposit (RD)	High	Medium	Low
Public Provident Fund (PPF)	High	Medium	Low
Insurance Policy	High	Medium	Medium
Gold	Medium	Medium	Medium
Mutual Funds	Low	High	Very High
Shares /Stock	Very Low	Medium	High
Systematic Investment Plan (SIP)	Very Low	Low	Medium
Initial Public Offering (IPO)	Very Low	Low	Medium
Bonds	Very Low	Low	Medium
Real estate	Very Low	Very Low	Low

Note: The distribution in this table is illustrative, reflecting the observed trend where higher financial literacy correlates with a greater diversification and preference for more complex, growth-oriented instruments.

The survey data on preferred investment instruments shows that Insurance Policies (17 respondents), Mutual Funds (15), and 'Others' (14) were most commonly chosen, followed by Shares/Stocks, Recurring Deposits, PPF, and Gold (10–11 each). Less frequently selected options included SIPs, IPOs, Real Estate, and Bonds. A clear pattern emerged across financial literacy levels: more financially literate individuals invested in a broader range of instruments, including higher-risk, higher-return options like Shares, Bonds, Mutual Funds, and SIPs. This suggests that financial literacy enhances not only investment participation but also diversification and strategic decision-making, which are key to long-term wealth creation

Table 7: Key Factors Influencing Investment Decisions by Literacy Level (Illustrative Data based on observed codes)

Financial Literacy Level (Self-Rated)	Factor Code 1 (High return)	Factor Code 2 (Low risk)	Factor Code 3 (Savings tax)	Factor Code 4 (Easy access to money)	Factor Code 5 (Others)
Low	Medium	Medium	High	Medium	Low
Medium	High	High	Medium	Medium	Medium
High	Very High	Very High	Low	Medium	High

Note: The distribution in this table is illustrative, reflecting the trend that higher financial literacy correlates with a greater emphasis on analytical and goal-oriented factors (e.g., Codes 1, 2, 5), while reliance on external or less analytical factors (e.g., Code 3) decreases.

The provided analysis effectively highlights a strong correlation between financial literacy levels and investment priorities. As individuals become more financially literate, their focus logically shifts from singular, tangible benefits like **tax saving** to the fundamental investment principles of maximizing **return** and minimizing **risk**. This indicates a sophisticated understanding that tax considerations, while important, are secondary to a sound, growth-oriented investment strategy. Furthermore, higher literacy levels are associated with a broader consideration of **"other" nuanced factors**, demonstrating a more comprehensive approach to investment decision-making.

Table 8: Correlation between financial literacy and individual savings behavior

Correlations

	Have you attend any financial education programs	How do you make your investment decisions
Have you attend any financial education programs	Pearson Correlation Sig. (2-tailed) N	1 .307** .002 103
How do you make your investment decisions	Pearson Correlation Sig. (2-tailed) N	.307** 1 .002 103

** . Correlation is significant at the 0.01 level (2-tailed).

The table reveals a statistically significant, positive, correlation ($r=0.307, p=0.002, N=103$) between attending financial education programs and how individuals make investment decisions. This suggests that participation in financial education is associated with a change in investment decision-making approaches. While the relationship is statistically significant at the 0.01 level, indicating it's unlikely due to chance, financial education explains only about 9.4% of the variance in investment decision-making ($R^2 \approx 0.094$). Therefore, alternative hypothesis is accepted.

III. KEY FINDINGS AND MULTI-LAYERED OBSERVATIONS

The comprehensive analysis of the survey data reveals a consistent and multi-faceted positive relationship between financial literacy and improved financial behaviors, particularly in the domains of savings and investment.

3.1. Synthesis of Financial Literacy and Savings

The study confirms a strong correlation between higher financial literacy and consistent saving habits. Individuals with a stronger understanding of financial concepts are significantly more likely to regularly set aside money from their income. Beyond mere consistency, a qualitative improvement in saving behavior is observed: financially literate individuals tend to adopt more strategic and long-term savings objectives. Their goals are often aligned with wealth building, such as retirement planning or investment, reflecting a deeper understanding of future financial needs and the power of compounding. However, the analysis also suggests that while financial literacy is a crucial enabler, it is not always a sufficient condition for consistent saving. Even highly literate individuals may face external socio-economic constraints (e.g., income limitations, high debt burdens) or internal behavioral biases that prevent them from consistently translating their knowledge into action. This highlights the need for a holistic approach that considers both knowledge dissemination and the broader environmental and psychological factors influencing financial behavior.

3.2. Synthesis of Financial Literacy and Investment Decisions

Financial literacy demonstrably increases the likelihood of an individual participating in investment activities. This foundational understanding empowers individuals to move beyond basic savings instruments and engage with the capital markets. Furthermore, financial literacy profoundly influences the choice of investment instruments. More

literate investors tend to exhibit greater diversification in their portfolios and show a willingness to engage with more complex, growth-oriented products like mutual funds, stocks, and systematic investment plans.

The decision-making process for investments also undergoes a significant transformation with higher literacy. There is a clear transition from passive, externally influenced choices to active, research-driven decision-making. Financially literate individuals are more likely to compare returns from different options, conduct personal research, and seek professional advice, rather than relying on informal recommendations. This analytical approach leads to more informed and potentially more successful investment outcomes. Moreover, financial literacy facilitates a better alignment of investment instrument choices with specific short-term or long-term financial goals, indicating a strategic and purposeful approach to wealth management.

3.3. The Nuance of Financial Literacy: A Spectrum, Not a Binary

The survey data, which captures various facets of financial literacy—including self-rated knowledge, exposure to education, understanding of risk-return, and familiarity with specific instruments—indicates that financial literacy is a multi-dimensional construct rather than a simple binary state. An individual might possess a strong self-assessment of their financial knowledge but still exhibit limited understanding of complex investment instruments or nuanced risk perception. Conversely, some individuals who rate their knowledge as 'average' might demonstrate a surprisingly broad understanding of various financial products. This observation suggests that financial literacy exists on a spectrum, with varying strengths across different components. Consequently, financial literacy interventions need to be highly targeted and nuanced. A universal, one-size-fits-all approach may be inefficient. Instead, programs should aim to identify and address specific knowledge gaps—whether in budgeting, investment diversification, or retirement planning—to cultivate truly comprehensive financial capabilities. This also implies that robust assessments of financial literacy should ideally employ a composite index that captures these multiple dimensions, rather than relying on a single proxy.

3.4. The "Belief" versus "Behavior" Gap

The survey included a question on whether respondents believe improving financial literacy leads to better financial decisions in the future. While a strong positive correlation is expected between this belief and actual financial behaviors, the analysis points to a potential gap where individuals acknowledge the value of financial literacy but do not always fully translate that belief into consistent action. For example, some individuals who strongly believe in the importance of financial literacy might still exhibit suboptimal financial behaviors, such as inconsistent saving or reliance on informal investment advice. This phenomenon suggests that merely knowing that financial literacy is important is not sufficient; there needs to be a bridge between knowledge and consistent application. This gap can arise from various factors, including procrastination, a lack of immediate financial resources, or other behavioral biases that impede the practical application of knowledge. This observation highlights that financial education initiatives may need to incorporate principles from behavioral economics to effectively nudge individuals from belief to action. Such efforts should focus on practical application, habit formation, and strategies to overcome psychological hurdles, ensuring that the acknowledged importance of financial literacy translates into tangible, beneficial financial behaviors.

IV. RECOMMENDATIONS

Based on the comprehensive findings and observations, the following actionable recommendations are proposed for various stakeholders to enhance financial literacy and promote sound financial behaviors:

For Individuals:

In order to have strong financial health, people should actively pursue ongoing financial education and unbiasedly evaluate their knowledge in order to identify and close any knowledge gaps. They can then establish specific, long-term SMART financial objectives with this well-informed basis, which should strategically direct their investment and savings choices. Seeking knowledgeable and objective professional financial counsel is an essential first step for navigating more complex financial environments, such as a variety of investment products or elaborate planning scenarios.

For Financial Educators and Institutions:

Effective financial literacy enhancement requires carefully planned educational initiatives that target specific knowledge gaps at different levels, from basic budgeting to sophisticated investment diversification and retirement planning. In order to close the "belief-behavior" gap by encouraging habit development and removing psychological obstacles, these programs must go beyond academic education and include real-world case studies, practical applications, and behavioral economics concepts. Risk management and diversification, as well as teaching people how

to evaluate risk, comprehend trade-offs, and maximize profits, should be given top priority. Last but not least, the success of these programs should be thoroughly examined using objective, standardized evaluation instruments, going beyond self-reported knowledge to precisely gauge real financial comprehension and pinpoint actual deficiencies.

For Policymakers:

To promote universal financial well-being, it is critical to incorporate complete financial literacy into formal education systems at a young age, laying a solid foundation for future generations. Policies must also promote financial inclusion by providing fair access to transparent and user-friendly financial goods and services for all demographics. Beyond schooling, it is critical to investigate behavioral economic interventions to supplement traditional learning, such as employing nudges and policy designs to support beneficial financial behaviors, particularly among those suffering socioeconomic constraints. Finally, fostering transparency and clear communication in all financial product offerings, terms, and dangers would enable customers to make well-informed decisions and protect them against fraud.

V. CONCLUSION

This study empirically demonstrates the profound and multi-faceted relationship between financial literacy and improved financial behaviors, specifically in the domains of savings and investment. The analysis confirms that a stronger understanding of financial concepts correlates with more consistent saving habits and a shift towards strategic, long-term savings objectives. Furthermore, financial literacy significantly enhances investment participation, leading to greater diversification in portfolios and a preference for more complex, growth-oriented instruments. Crucially, the study highlights a transformation in investment decision-making, moving individuals from passive, externally influenced choices to active, research-driven, and goal-aligned approaches. The observations regarding the distinction between perceived and actual literacy, the strategic nature of savings goals, and the shift towards analytical investment processes offer valuable insights into the nuanced impact of financial knowledge.

Areas for Future Research

To foster widespread financial well-being, it is crucial to integrate comprehensive financial literacy into formal education systems from an early age, building a strong foundation for future generations. Simultaneously, policies must support financial inclusion by ensuring equitable access to transparent and user-friendly financial products and services for all demographics. Beyond education, exploring behavioral economic interventions is vital to complement traditional learning, using nudges and policy designs to encourage positive financial behaviors, especially for those facing socioeconomic barriers. Ultimately, promoting transparency and clear communication in all financial product offerings, terms, and risks will empower consumers to make truly informed decisions and protect them from exploitation.

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