

Financial Literacy and Its Role in Shaping Personal Investment Decisions in India

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ABSTRACT- The issue of financial literacy is critical in determining the way people in India make personal investment choices. This paper explores the present situation in financial literacy in India, how it connects to investment preferences and policy efforts to enhance financial education. Based on the use of secondary sources and illustrative data, the study demonstrates that increased financial literacy correlates with an increase in the degree of risk-taking, diversification of portfolios, and financial performance. They give policy recommendations that would enhance financial education in India.

KEYWORDS: Financial Literacy, Investment Decisions, India, Financial Inclusion, NCFE

I. INTRODUCTION

Financial literacy has become a vital life skill of the contemporary world, in which individuals have become more and more accountable in the manner in which they manage their financial lives. It involves possession of knowledge, skills and confidence to make informed financial decisions in terms of budgeting, saving, borrowing, investing, and risk management [1]. Financial literacy is especially important in developing economies such as India where the rapid economic growth is accompanied by increased disposable income and financial product innovations. This financial literacy and its resulting skills in effectively applying financial concepts is key to the formation of an individual investment choice, which subsequently determines the amount of household wealth, financial health, and economic stability over the long term [2].

Regardless of the significance, research shows that the financial literacy rates in India are low in comparison to international rates. Financial literacy is not high among Indian adults with a survey by Securities and Exchange Board of India (SEBI) revealing that only 27% of the adult Indians are financially literate with the global average standing at 33 percent [3]. This financial illiteracy restricts the involvement of households in formal investment outlets like equities, mutual funds, insurance, and retirement plans and results in their greater use of traditional or informal investment outlets like gold, real estate, or savings accounts [4]. The trends make it difficult to create wealth, and expose people to financial risks.

Investment choices are complicated and are affected by numerous variables such as risk tolerance, income, cultural beliefs, bias behavior and availability of financial information [5]. Nonetheless, the financial literacy serves as the base through which individuals evaluate these variables and adjust their investment plans to the long-term objectives. An example is that the more financially literate a person is, the more likely he/she would diversify their portfolio, manage risk better and have better financial performance [6]. On the contrary, underperformance in financial literacy is usually related to ineffective financial planning, possibility of fraud, and inefficient investment practices [7].

The problem acquires even more topicality in the Indian context under the pressure of the financial inclusion of the country by such programs as the Pradhan Mantri Jan Dhan Yojana (PMJDY), the development of digital banking and the emergence of fintech platforms [8]. Although such interventions expand access to financial services, insufficient financial literacy can make people unable to harness such opportunities. Financial literacy, as the India dreams of growing to be a 5 trillion economy, is not just an issue that needs to be empowered individually but also a crucial aspect of the economic development that is sustainable.

The purpose of this paper is to find out how financial literacy is related to personal investment decisions in India. It analyses the effects of differing levels of financial literacy, in terms of individual decision-making on a variety of investment instruments and the obstacles that hinder the rational decision-making process. Policy implications are also assessed in the study and appropriate measures to improve financial literacy among Indian households are recommended. In so doing, the paper is able to contribute to the current discussion of the promotion of informed financial behavior, economic vulnerability reduction, and long-term financial resilience.

II. LITERATURE REVIEW

The study by Rajdeep Kumar Raut [9], attempts to investigate the significance of past behaviour and financial literacy in investment decision-making of individual investors and the validity of the theory of planned behaviour in that regard.

P. Parsai et al. [10] examined underscores critical role of financial literacy in the process of the investment decision. People who are better informed in their financial matters

are more likely to make informed decisions in their investments and those who are not informative take risks away. This question is the focus of the Jain et al. [11] study as it discusses whether or not herding and overconfidence bias are the serial mechanisms that mediate the relationship between financial literacy and decision-making of equity investors in the Indian stock market. Primary data was collected using a survey method where 436 individual equity investors in the north Indian region were surveyed. The study has also been modelled using PLS-SEM to assess the serial mediation-based model. Financial literacy was established to possess a significant positive impact on the decision made by individual investors. Madhuri et al. [12] research paper explores the important role of financial literacy in determining individual investment choices. In the world where financial markets are getting more and more complicated, the need to inform people in their investment decisions is more essential than ever before. Nevertheless, most people are not sufficiently financially educated, and this may hinder their capacity to maneuver in the world of investments. The study will focus on the direct effect of financial literacy on different determining factors of investment decision-making.

H. Garg[13] et al. discusses the effect of financial literacy on investment decision making and its importance in the promotion of individual financial well being and economic stability. Financial literacy is the knowledge and skills needed to manage money properly hence having these skills is essential in empowering people to make sound financial decisions. The paper reviews the literature, outlines the themes and gaps in the literature, and suggests measures of treating and increasing financial literacy. N Sharma studied[14] et al. is a comprehensive review of the currently available body of literature by infometric and lexicometric analysis. After this, the study formulates an innovative conceptual model of market microstructure with investment decision, asset development and financial literacy.

S Singh et al. [15] attempts to explore the antecedents of social interaction between Indian retail investor and fund managers in order to comprehend the influence of these antecedent factors. The study will help illuminate the social process that influences investment behavior in the Indian financial market by identifying and analyzing these antecedents.

III. RESEARCH OBJECTIVES

- To assess the level of financial literacy in India and its variation across groups.
- To examine the influence of financial literacy on personal investment behavior.
- To recommend policy measures to improve financial literacy and investment outcomes in India.

IV. METHODOLOGY

This study synthesizes secondary data from national surveys (NCFE/FLIS), government reports, and peer-reviewed studies. An illustrative dataset is used to

visualize how differing literacy levels relate to preferences for safe versus risky assets.

V. ANALYSIS AND FINDINGS

In the below Table 1 presents an illustrative relationship between the level of financial literacy and the investment preferences of individuals. The table categorizes respondents into three groups—low, medium, and high financial literacy—and compares their tendency to prefer safe assets (such as savings accounts, fixed deposits, gold, and government securities) versus risky assets (such as equities, mutual funds, and market-linked instruments).

Table 1: Financial Literacy and Investment Preferences (Illustrative)

Financial Literacy Level	Preference for Safe Assets (%)	Preference for Risky Assets (%)
Low	75	25
Medium	50	50
High	30	70

Source: Illustrative data prepared for this paper (based on trends reported in national studies)

The data indicate that there is a negative correlation between financial literacy and preference to safe assets. Lowly financially literate people are highly risk-averse, as 75 per cent of them prefer low-risk investments, and 25 per cent of people are risk-takers. This action indicates low awareness of financial markets, low confidence and risk-averse behavior that tends to be common among financially less-informed households.

When the financial literacy is raised to the middle level, the distribution becomes a balanced one (50:50) between risky and safe assets. It suggests that those that possess average financial literacy will start diversifying their portfolios and become more accepting of returning-oriented investment options.

Conversely, high financially literate people have a higher preference in risky assets (70 percent) over safe ones (30 percent). This group is more prepared to judge risks, has knowledge of the possibilities of market-based instruments and is more confident in making informed investment choices. Their actions are consistent with the existing theories according to which financial knowledge is associated with better portfolio diversification and rational risk-taking.

In sum, the results highlight the importance of financial literacy to the orientation of investments. Poor literacy breeds conservative monetary behavior, with increased literacy enabling individuals to explore more lucrative investment opportunities thus increasing wealth generation and monetary security in the long-term.

Figure 1 shows the association between the level of financial literacy and investment preferences. The chart divides investors into three levels, low, medium, and high financial literacy, and demonstrates the ratio of investors investing in safe assets and those investing in risky assets.

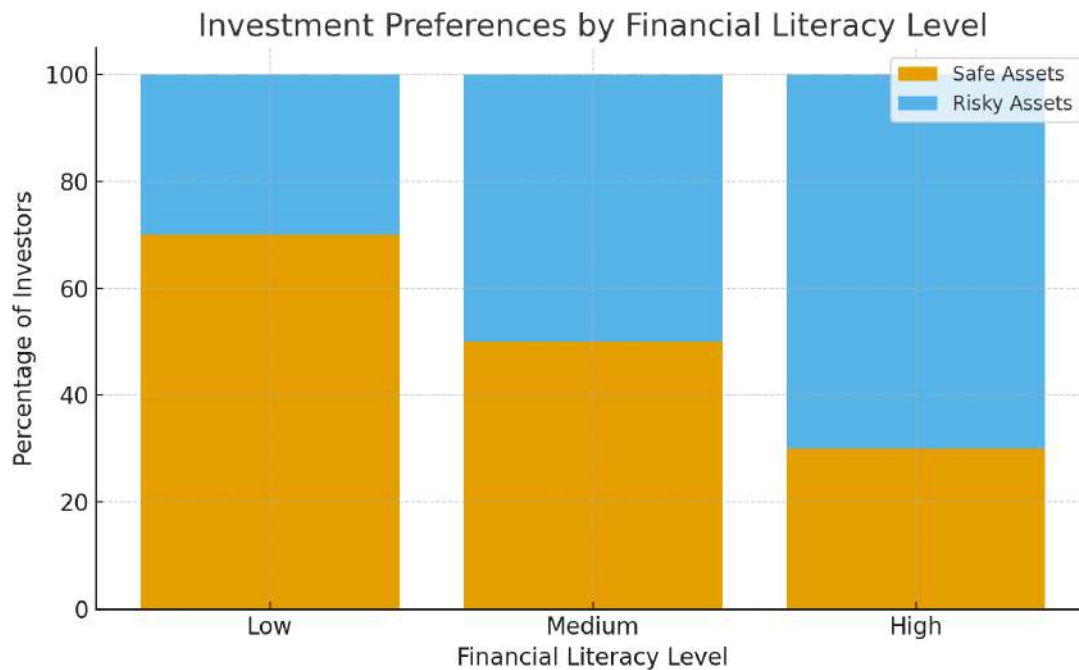


Figure 1: Investment Preferences by Financial Literacy Level (Illustrative)

The figure demonstrates a distinct pattern:

- **Low Financial Literacy:** Most investors (approximately 70-percent) are interested in safe investments, like fixed deposits, savings accounts, and gold, with only 30-percent investing in risky investments. This shows the high-risk aversion as they have very little financial literacy and do not trust themselves to operate complex tools.
- **Medium Financial Literacy:** The moderately knowledgeable investor is more balanced, as they place about half of their portfolio in safe investments and half in risky investments. This shows increasing consciousness on diversification of portfolios and readiness to venture in the field of returns-driven investments.
- **High Financial Literacy:** Financial literate investors show that they tend to take high risk (approximately 70 percent) over low risk (30 percent) assets. This group is also confident in risk assessment, more knowledge of the market dynamics and can diversify effectively to accumulate in the long-term.

In general, Figure 1 supports the idea that financial literacy is one of the determinants of investment behavior. With increased financial literacy, people abandon the traditional investment habits and pursue more risky and sophisticated options that have the potential to offer better returns.

VI. DISCUSSION

The data on the level of basic financial literacy of Indian adults shows that it is only among a minority of the population that basic financial literacy requirements are satisfied, with large interstate and demographic differences. The low literacy is linked to the conservative investment behavior (like preference to fixed deposits, cash and informal savings), whereas high literacy is linked to diversified portfolios and market investments.

Newer policy initiatives such as the National Strategy of Financial Education (NSFE 2020-25), activities of the

National Centre of Financial Education (NCFE) and the Reserve Bank of India (RBI) [3] also seek to enhance access and quality of financial education in the nation.

VII. CONCLUSION AND POLICY RECOMMENDATIONS

In India personal investment decisions are shaped materially by financial literacy. In order to increase investment performance and financial sustainability, the recommendations are the following:

- Incorporate financial education into the school and university curricula and vocational training.
- Improve community outreach (women self-help groups, local NGOs) to access underserved groups.
- Use FinTech and mobile to scale and engage in interactive financial education.
- Review and assess financial literacy initiatives with the help of standardised instruments (e.g., OECD/INFE toolkit).

These measures will be implemented to enhance informed investment decisions and the improvement of the wider Indian economic welfare.

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