

“Analysis of Financial Literacy Metrics on the Efficiency of Investment Decision-Making among Individual Investors”

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Abstract

In this paper, we examine the reasons why many individual investors fail to convert financial knowledge into sound investment choices using three specific literacy metrics: budgeting knowledge, saving behavior, and investment knowledge, and how each influences the quality of an investor's decisions. Our research design is descriptive and explanatory, relying on a quantitative approach: approximately 130 respondents, whose financial literacy levels are measured using a structured Likert-scale questionnaire, and secondary data from existing journals and studies that test the relationship of financial literacy to decision-making efficiency, and identify the most salient behavioral and demographic factors. We will examine these relationships using descriptive statistics, correlation, regression, and factor analysis. We anticipate the data will show what previous work has indicated—that investors with higher levels of financial literacy make more rational, confident, and effective decisions.

Keyword: Financial Literacy, Investment Decision Making, Budgeting, Saving Behavior, Investment Knowledge, Behavioural Finance, Retail Investors

1.Introduction

Over the last three decades, financial literacy has gone from being an afterthought in economic policy to a cornerstone of personal economic security, with research in developed economies linking basic numeracy and financial understanding to retirement planning and savings behavior, and with both researchers and policymakers realizing that as global financial markets were liberalized in the 1990s and

2000s, and as investment instruments became more and more complex, financial literacy was not simply an optional extra but a gateway to economic participation itself.[1]

In India, this change took root in the 1990s with the opening up of financial markets and the growing retail participation in equity and mutual fund markets. The global financial crisis of 2008 was a wake-up call to the international community that widespread financial illiteracy was a contributing factor to poor household financial decisions, over-leveraging, and susceptibility to mis-selling, prompting international bodies such as the OECD to develop standard frameworks for assessing financial literacy that encompass financial knowledge, financial behavior, and financial attitude as interrelated dimensions.[2]

Given the digitization of financial services, proliferation of trading applications, and capital markets opening up to first-time retail investors, the need for financial literacy has only increased, with a particularly significant increase in individual investors in India in recent years, especially through digital onboarding, financial influencers, and easier demat account access, without a concomitant increase in financial literacy, which is leading to a fear about the quality and efficiency of investment decisions being made by first-time and existing investors.[3]

The present study aims to fill this gap by empirically exploring the level of financial literacy among individual investors, investigating its relationship to investment decision-making, and isolating the relative contribution of its constituent components in order to discover the most influential factors on investment decisions.[4]

2. Review of Literature

Vishwakarma (2026). The study explains that knowledge of financial concepts such as risk and return, diversification, inflation, savings, and interest rates enables investors to make informed and rational financial decisions. It emphasizes that financially literate individuals are more confident in selecting suitable investment avenues, managing risks, and planning long-term financial goals. The paper further identifies that lack of financial knowledge often leads to poor investment choices and financial insecurity. Based on secondary data collected from journals and previous research studies, the study concludes that financial literacy positively influences investment behavior, wealth creation, and financial stability, while also recommending promotion financial education programs to enhance investor awareness and decision-making efficiency.[1]

Rahmiyati and Somodiharjo (2025) : This paper examine the influence of financial literacy, investment decision-making, risk tolerance, and behavioral biases on individual investment performance using a quantitative approach. Using a quantitative research approach, the study collected data from 200 respondents through a structured questionnaire and analyzed the results using Structural Equation Modeling–Partial Least Squares (SEM-PLS). The study finds that financial literacy has a significant positive effect on investment decision efficiency, as financially knowledgeable investors are more capable of evaluating risks, diversifying portfolios, and making informed choices. Investment decision-making ability emerges as a key determinant of performance, while risk tolerance acts as a supporting factor that enhances the relationship between financial knowledge and outcomes.[2]

Alam et al. (2024) The studied how subjective financial literacy (i.e., an individual's confidence in their financial knowledge) affects investment decisions among individual investors in India. The study found that investors who believe they have good financial knowledge are more confident and active in making investment decisions. It also shows that different aspects of financial literacy, such as understanding financial concepts, market knowledge, and analytical skills, positively influence decision-making. The study highlights that both actual knowledge and perceived knowledge are important for making effective investment decisions. Overall, the research concludes that improving financial literacy and investor confidence can significantly enhance investment

decision efficiency and lead to better financial outcomes.[3]

Cucinelli and Soana (2023) This research paper investigate the relationship between financial literacy, investor preferences, and the choice of financial intermediaries with a focus on sustainable or socially responsible (SR) investments among retail investors in Italy. The findings reveal that individuals with higher levels of financial literacy and stronger orientation toward sustainability are more likely to prefer SR financial intermediaries and make more informed investment choices. Additionally, their investment decisions with long-term sustainability goals. The research concludes that financial literacy not only improves investment decision efficiency but also promotes responsible investment behaviour, contributing to the development of sustainable financial markets.[4]

Shroff et al. (2024) The study found that financial literacy plays an important role in encouraging individuals to participate in financial markets by improving their understanding of financial products and risk-return relationships. It highlights that financially literate investors are more confident and less risk-averse, enabling them to make more informed and efficient investment decisions. The research also shows that while factors such as income and wealth influence investment behavior, financial literacy significantly enhances an individual's ability to evaluate opportunities and manage financial risks. Overall, the study concludes that improving financial literacy can lead to increased participation in financial markets and better investment decision efficiency among individual investors.[5]

Baveja and Verma (2024) The study found that financial literacy plays a crucial role in improving investment decision-making and encouraging participation in the stock market. It highlights that individuals with higher financial knowledge have greater confidence and are more capable of making informed and rational investment choices. The research also identifies that low financial literacy acts as a major barrier to market participation, as investors lack understanding and fear financial risks. Additionally, the study shows that financial literacy influences behavioral factors and reduces vulnerability to financial fraud and poor decision-making. Overall, the study concludes that improving financial literacy is essential for enhancing investment decision efficiency and promoting active participation in financial markets among individual investors.[6]

3. Research Methodology

This study adopts a descriptive and analytical research design to examine the relationship between financial literacy and investment decision-making among individual investors. Primary data is collected through a structured questionnaire administered to individual investors across different age groups, income levels, and investment experience, using a combination of Likert-scale and multiple-choice items to capture financial literacy components such as budgeting, saving behavior, and investment knowledge, alongside indicators of investment decision efficiency (portfolio diversification, risk tolerance, and return satisfaction). [1]

A stratified or convenience sampling method is used to select a representative sample of respondents, and the collected data is analyzed using statistical tools such as correlation and multiple regression analysis to test the proposed hypotheses on the relationship between financial literacy components and investment decision-making outcomes. Reliability of the survey instrument is checked using Cronbach's alpha, and descriptive statistics (mean, standard deviation) are used to profile respondent characteristics before hypothesis testing. This mixed quantitative approach allows the study to move beyond a general assessment of financial literacy and isolate which specific components (budgeting, saving, or investment knowledge) contribute most significantly to efficient investment decisions. [2]

4. Result

Statistic	Value
Multiple R	0.186
R ²	0.0345
Adjusted R ²	0.0270
F (1,128)	4.576
Significance F (p)	0.034

TABLE I. SIMPLE REGRESSION MODEL SUMMARY

These simple linear regression results show a statistically significant positive relationship between financial literacy, or understanding of the fundamental financial concepts of inflation, interest rates, and the risk-return tradeoff, and investors' confidence in their investment decisions, with a beta value of 0.197, t-statistic of 2.139, and p-value of 0.034, which is statistically significant and leads to rejecting the null hypothesis and confirms that financial literacy does impact investment decision-making confidence, as the correlation coefficient from the previous section suggests ($r = 0.186$), but the R^2 of 0.0345 indicates that this single component accounts for only about 3.45% of

the variation in investment confidence, which while statistically significant, suggests that the practical explanatory power is very low, and that other factors such as investment experience, risk appetite, access to financial advice, or behavioral tendencies, among others, likely account for the remaining variance. (According to table value)

Predictor	Coefficient (β)	Std. Error	t-Stat	p-value
Intercept	1.390	0.367	3.782	<0.001
Budgeting Practices	0.247	0.068	3.650	<0.001
Consistent Saving before investing	0.190	0.080	2.385	0.019
Emergency fund creation	0.204	0.073	2.788	0.006

TABLE II. MULTIPLE REGRESSION COEFFICIENTS (DV: INVESTMENT DECISION CONFIDENCE)

The multiple regression results show that the combination of budgeting practices, saving consistently, and creating an emergency fund has a statistically significant positive effect on investors' confidence in their investment decision-making ($F(3,126) = 12.229$, $p < 0.001$), explaining 22.55% of the total variance ($R^2 = 0.226$), which is much higher explanatory power than the single-item financial concept model tested in the last section ($R^2 = 0.035$). Among the three predictors, budgeting practices were the most influential ($\beta = 0.247$, $p < 0.001$), followed by emergency fund creation ($\beta = 0.204$, $p = 0.006$) and consistent saving ($\beta = 0.190$, $p = 0.019$), suggesting that all three saving and budgeting behaviors do contribute meaningfully to investment decision confidence, with budgeting habits having the most impact. This result supports Objective 3, which found that practical financial behaviors (budgeting and saving) explain investment decision-making efficiency.

5. Discussions

The results of this study offer valuable information about the effects of financial literacy on investment decision-making by individual investors. The correlation and simple regression results indicate that knowledge of basic financial concepts (inflation, interest rates, and risk-return tradeoff) are only statistically, but weakly, related to investment decision confidence ($r = 0.19$, $R^2 = 0.0345$, $p = 0.034$) and are thus not a particularly strong factor in driving investment confidence.

On the other hand, the multiple regression results show that when considering all three practical financial behaviors together, there is a significantly stronger and more substantive relationship ($R^2 = 0.2255$, $F(3,126) = 12.229$, $p < 0.001$) such that all three predictors were individually significant: budgeting practices ($\beta = 0.247$, $p < 0.001$), creating an emergency fund ($\beta = 0.204$, $p = 0.006$), and consistent saving behavior ($\beta = 0.190$, $p = 0.019$). This suggests that the behavioral application of financial literacy, not just the conceptual understanding, is related to investment decision-making confidence, and that the strongest practical financial behavior that influences investment decision-making is budgeting practices.

6. Conclusion

In contrast, when budgeting practices, consistent saving behavior, and emergency fund creation were examined together, they explained a substantially larger share of the variance in investment decision confidence ($R^2 = 0.2255$), with budgeting practices emerging as the single strongest predictor. This demonstrates that the behavioral application of financial knowledge — how investors manage, save, and plan their money on a day-to-day basis — matters considerably more than abstract financial concept knowledge in shaping confident and effective investment decisions.

These findings carry practical implications for financial educators, policymakers, and financial service providers. Rather than focusing narrowly on teaching financial theory, literacy initiatives should prioritize building actionable financial habits such as structured budgeting, disciplined saving, and emergency fund planning, particularly among first-time and young retail investors entering markets through digital platforms. Strengthening these behavioral competencies is likely to yield more meaningful improvements in investment decision-making quality than conceptual education alone.

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