Financial Literacy Alone is Not Enough: How Overconfidence Among Young Indian Retail Investors Creates an Expertise Paradox

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Abstract

The huge growth in young retail investors participating in Indian stock markets due to online trading and other fintech tools has attracted tens of thousands of new young investors to financial markets. Although financial literacy is considered a useful way to aid better investment decisions how it relates to behavioral biases is still debatable. This research examines the relationships between financial literacy, over confidence bias, and irrational investment behavior amongst young Indian investors. Through primary data collection, data were collected from 654 young Indian investors and analyzed using Spearman rank correlation analysis, multiple regression analysis and non-parametric bootstrap mediation analysis in R. Three hypotheses were tested: whether financial literacy affects over-confidence bias, whether over confidence bias affects irrational investment behavior, and whether over-confidence acts as a mediator between financial literacy and irrational investment behavior. The results demonstrate that financial literacy did not have a statistically significant impact on over confidence bias (β=-0.012, p=0.678); however over confidence was a very strong predictor of irrational investment behavior accounting for approximately 51.2 % of its variation (β= 0.575, p<0.001). The mediation analysis confirmed that over confidence does not act as a mediator in the relationship between financial literacy and irrational investment behavior. Therefore these findings support the conclusion that having financial knowledge alone is insufficient to overcome entrenched psychological biases; therefore if financial education programs are going to be effective at improving investment outcomes amongst young investors they must also include components of behavioral awareness.