



PREVENTION OF BANK NON-PERFORMING ASSETS IN WORKING CAPITAL FINANCING: ROLE OF FINANCIAL LITERACY IN IMPROVING BORROWER CREDIT BEHAVIOUR.

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ABSTRACT

Non-performing assets (NPAs) have emerged as a major concern for the stability and efficiency of the banking sector, particularly in the context of working capital financing provided to small and medium-sized enterprises and business units. Inefficient utilisation of borrowed funds, weak financial planning, and limited financial awareness among borrowers often contribute to repayment difficulties, eventually leading to loan defaults. This study examines the roles of financial literacy and borrower education in preventing the occurrence of NPAs in working capital financing. The research explores how financial knowledge influences borrowers' credit behaviour, working capital management practices, and repayment discipline.

This study adopts a descriptive and analytical research design and utilises both primary and secondary sources of information. Primary data were collected through structured questionnaires from borrowers engaged in small business activities who had availed working capital loans from banks. Secondary information was obtained from banking reports, academic literature, and publications of financial regulatory institutions. The analysis focuses on assessing the level of financial literacy among borrowers and examining its relationship with loan utilisation and repayment performance.

The findings indicate that borrowers with higher levels of financial literacy demonstrate stronger financial planning abilities, improved cash flow management, and greater awareness of credit obligations. Such borrowers are more likely to utilise working capital funds productively and maintain timely repayment of loan instalments. Conversely, borrowers with limited financial knowledge often face difficulties in managing business finances, which increases the risk of delayed repayment and potential loan default. Therefore, strengthening borrowers' financial literacy can play a significant role in preventing the accumulation of NPAs in the banking system.



Keywords: Financial Literacy, Non-Performing Assets, Working Capital Financing, Borrower Education, Banking Sector, Credit Management.

1. INTRODUCTION

The banking sector plays a pivotal role in promoting economic growth by providing credit facilities to businesses and individuals. One of the most critical forms of credit offered by banks is **working capital financing**, which supports the day-to-day operational requirements of businesses, such as purchasing raw materials, managing inventory, paying wages, and meeting other short-term financial obligations. Efficient working capital management enables businesses to maintain liquidity and operational continuity. However, improper utilisation of working capital loans and weak financial management practices among borrowers often lead to repayment difficulties, resulting in the creation of **non-performing assets (NPAs)** in the banking system.

Non-performing assets (NPAs) have become a major concern for the banking sector worldwide. An asset becomes non-performing when the borrower fails to repay the principal or interest for a specified period, typically 90 days in the case of commercial banks. Rising NPAs reduce bank profitability, weaken financial stability, and restrict the ability of banks to extend further credit to productive sectors of the economy. In India, the problem of NPAs has been particularly significant in sectors involving small and medium-sized enterprises (SMEs), traders, and small business units that depend heavily on working capital financing for their operations (Reserve Bank of India, 2023).

Among the various factors contributing to NPAs, **a lack of financial literacy among borrowers** has emerged as an important issue. Financial literacy refers to the knowledge, skills, and confidence required to make informed financial decisions and manage financial resources effectively. It includes understanding financial products, interest rates, credit obligations, risk management, and financial planning. Borrowers lacking financial knowledge often fail to properly assess their borrowing capacity, mismanage loan funds, and struggle to maintain repayment discipline. Consequently, poor financial decision-making increases the risk of loan default.

1.1 Working Capital Financing in Banks

Working capital financing is a critical banking facility that supports the day-to-day operational needs of businesses. Banks provide short-term credit to firms to manage routine expenses, such as



purchasing raw materials, maintaining inventory, paying wages, and meeting other operational costs. This type of financing ensures that businesses maintain adequate liquidity and continue their production and trading activities without interruption. Working capital loans are commonly provided in the form of cash credit, overdraft facilities, short-term loans, and trade credit arrangements. Effective working capital financing helps businesses maintain a smooth cash flow cycle and improve operational efficiency. However, improper utilisation of working capital funds or weak financial management practices can lead to repayment difficulties, thereby increasing the risk of loan default and the creation of non-performing assets in the banking sector (Brigham & Ehrhardt, 2017; Pandey, 2015; Reserve Bank of India, 2023). Therefore, banks carefully assess borrowers' financial capacity and monitor credit utilisation to ensure responsible lending and financial stability.

1.2 Determinants of NPAs in Working Capital Loans

Non-performing assets (NPAs) in working capital loans arise because of a combination of borrower-related, bank-related, and external economic factors. One of the primary determinants is poor financial management by borrowers. Many small and medium-sized enterprises rely on working capital loans for operational expenses; however, inadequate budgeting, weak cash flow planning, and improper utilisation of borrowed funds often lead to repayment difficulties. When business revenues decline or funds are diverted to non-productive activities, borrowers may fail to meet their repayment obligations, increasing the likelihood of loan default (Pandey, 2015).

Another important factor is inadequate credit appraisal and monitoring by banks. If financial institutions do not properly evaluate borrowers' repayment capacity, business performance, and financial stability before granting credit, the risk of loan default increases. Similarly, weak post-disbursement monitoring of working capital utilisation may allow borrowers to misuse funds or delay repayments (Koch & MacDonald, 2015).

Macroeconomic conditions also play a significant role in influencing NPAs. Economic slowdowns, fluctuations in market demand, rising input costs, and unexpected business disruptions can negatively affect the financial performance of firms. Such conditions reduce business profitability and weaken borrowers' repayment capacity, thereby contributing to the accumulation of NPAs in the banking system (Reserve Bank of India, 2023).



1.3 Role of Financial Literacy in Credit Behaviour

Financial literacy plays a crucial role in shaping the credit behaviour of borrowers by improving their ability to understand financial products, evaluate borrowing decisions, and manage debt responsibly. Individuals with adequate financial knowledge are more capable of interpreting their loan conditions, interest rates, and repayment schedules, which helps them make informed borrowing decisions. This understanding reduces the likelihood of excessive borrowing and encourages responsible credit utilisation, thereby lowering the probability of loan default (Lusardi & Mitchell, 2014).

Financially literate borrowers are better equipped to plan and manage their financial resources effectively. They tend to maintain proper budgeting practices, monitor business cash flows, and allocate borrowed funds for productive purposes. Such financial discipline enables borrowers to meet repayment obligations in a timely manner and maintain a positive credit record. In contrast, borrowers with limited financial awareness may misjudge their repayment capacity, leading to financial stress and repayment delays (Atkinson & Messy, 2018).

Furthermore, financial literacy enhances borrowers' understanding of financial risks and long-term financial consequences associated with credit usage. Awareness of these risks encourages individuals to adopt cautious borrowing behaviour and avoid unnecessary debt accumulation. Consequently, improved financial literacy contributes to stronger repayment behaviour and supports the overall stability of the banking system by reducing the risk of non-performing assets (OECD, 2022).

1.4 Financial Literacy

Financial literacy refers to the **ability of individuals to understand financial concepts and use that knowledge to make informed financial decisions** regarding saving, borrowing, investing, and managing money. It involves the knowledge, skills, attitudes, and behaviours required to manage financial resources effectively throughout life.

Financial literacy is an essential element of modern financial systems because individuals frequently interact with complex financial products, such as loans, credit cards, insurance, investments, and banking services. Without adequate financial knowledge, individuals may face difficulties managing debt, planning expenditures, or understanding financial risks.



In the context of banking and credit management, financial literacy helps borrowers understand **interest rates, repayment schedules, loan obligations, and the consequences of loan defaults.**

A financially literate borrower is more capable of managing working capital efficiently, maintaining financial discipline, and avoiding excessive borrowing. Consequently, financial literacy plays a significant role in **reducing loan defaults and minimising non-performing assets (NPAs)** in the banking sector.

Financial literacy generally includes several important components, such as financial knowledge, financial skills, financial attitudes, and financial behaviour. These elements collectively influence how individuals manage their finances and make economic decisions. Financial knowledge refers to an understanding of financial concepts, such as interest rates, inflation, risk diversification, and credit management. Financial skills involve the ability to prepare budgets, manage cash flows, and evaluate financial products. Financial attitudes reflect individuals' mindsets toward saving, borrowing, and financial planning, whereas financial behaviour represents the practical actions individuals take in managing money.

In the business environment, particularly for entrepreneurs and small business owners who depend on working capital financing, financial literacy is crucial for **effective financial planning and resource management.** It helps borrowers monitor business expenses, maintain accurate financial records, and ensure timely loan repayments. Therefore, improving borrowers' financial literacy contributes not only to individual financial well-being but also to the overall stability of the banking system.

1.5 Financial Literacy and NPA

Financial literacy is particularly crucial for borrowers who rely on working capital loans to manage business operations. A proper understanding of financial management helps borrowers maintain cash flow balance, control operational costs, and allocate loan funds efficiently. Financially literate borrowers are more likely to maintain accurate financial records, plan repayment schedules, and utilise credit for productive purposes. Consequently, financial literacy plays an important role in minimising the occurrence of NPAs and strengthening credit discipline among borrowers (Lusardi & Mitchell, 2014).

Recognising the importance of financial literacy, governments, central banks, and financial institutions around the world have initiated various financial education programs. In India, the



Reserve Bank of India (RBI) has established financial literacy centres and introduced several awareness campaigns aimed at improving financial knowledge among individuals and small entrepreneurs. These initiatives are designed to educate borrowers about responsible borrowing, financial planning, and effective credit management (RBI, 2022).

Despite these efforts, financial literacy levels remain relatively low in many developing economies. Many small business owners and borrowers lack formal financial education and primarily depend on informal knowledge or experience when making financial decisions. This gap highlights the need for structured financial education programmes that can enhance borrowers' financial capability and improve credit utilization.

This study examines the **importance of financial literacy and borrower education in minimising bank non-performing assets (NPAs) in working capital financing**. It explores how financial knowledge influences borrower behaviour, credit management, and repayment capacity. Additionally, it evaluates the role of financial institutions in promoting financial literacy and highlights the potential benefits of borrower education programs in strengthening the stability of the banking system.

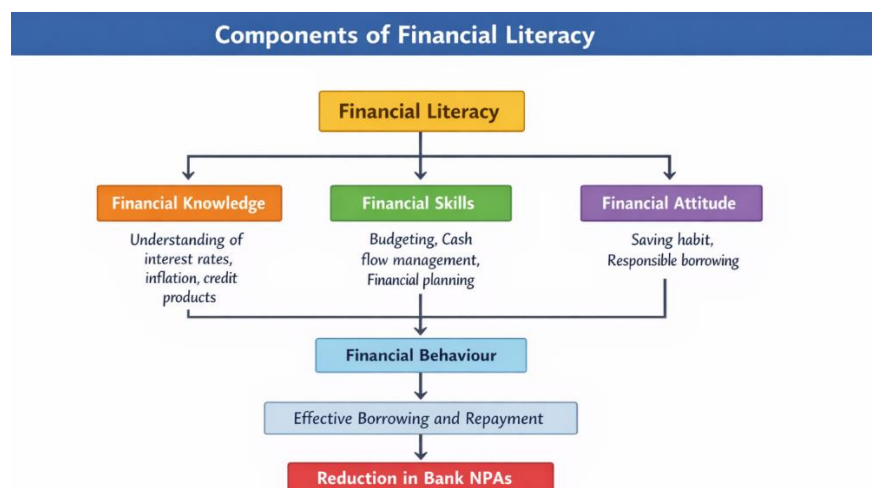


Figure: 1 Components of Financial Literacy

Figure 1 shows that financial literacy is built upon four major components: financial knowledge, financial skills, financial attitudes, and financial behaviour. These components influence how individuals manage credit and financial resources. When borrowers have strong financial literacy,



they are more likely to use working capital loans responsibly and maintain timely repayments, thereby helping to reduce bank NPAs.

2. REVIEW OF LITERATURE

Financial literacy has emerged as a crucial component in strengthening financial systems, improving credit behaviour, and promoting responsible borrowing practices. A number of scholars and institutional studies have examined the relationship between financial literacy, borrower behaviour, and the performance of banking assets. The following review of the literature highlights the significant contributions of researchers in understanding the role of financial education in financial decision-making and loan repayment behaviour.

2.1 Causes of Non-Performing Assets (NPAs)

Non-performing assets (NPAs) have become a persistent challenge for banking systems, particularly in developing economies with increased credit expansion. Studies have identified multiple factors contributing to NPAs. Poor credit appraisal, inadequate monitoring, and weak financial discipline among borrowers are major internal factors leading to loan defaults (Ghosh, 2017). When banks fail to properly assess borrowers' repayment capacity, default probability increases.

Economic conditions influence loan performance. Market fluctuations and economic downturns can reduce businesses' profitability, affecting loan repayment (Rajan & Dhal, 2003). Inefficient financial management may result in diversion of borrowed funds to non-essential expenditure, increasing financial stress, and creating NPAs (Kaur & Singh, 2011).

Agarwal, Amromin, Ben-David, Chomsisengphet, and Evanoff (2015) found that individuals with higher financial literacy make better financial decisions and manage credit responsibly. Their study showed that financially literate individuals demonstrate better financial planning and debt management practices, emphasizing that improved financial knowledge can reduce loan defaults.

Atkinson and Messy (2018) used the OECD International Network on Financial Education to measure financial literacy across countries. Their research showed financial literacy correlates with responsible financial behavior and understanding credit obligations. The authors recommend financial education programs for improving financial capability.



Bhushan and Medury (2019) found that financial literacy levels in India remain low, particularly among those lacking formal financial education. The study showed inadequate financial knowledge affects borrowing decisions and emphasized that financial education can reduce financial mismanagement risk.

Goyal and Kumar (2021) identified financial literacy as key to financial behavior and credit management through bibliometric analysis. Their research highlighted financial literacy's impact on borrowing decisions and emphasized financial education's role in reducing financial vulnerability.

2.2 Credit Risk Management

Credit risk management is essential for banking operations as it helps institutions evaluate borrower default probability and maintain asset quality. Effective credit risk management involves procedures for credit appraisal, borrower assessment, monitoring of loan performance, and timely action when repayment problems arise. According to Saunders and Allen (2010), banks must analyze borrowers' financial statements, cash flow patterns, and repayment capacity before extending credit. Such evaluations reduce the risk of lending to financially unstable borrowers.

Continuous monitoring of credit accounts is equally important. Berger and DeYoung (1997) argued that weak loan monitoring systems can result in asset quality deterioration and rising NPAs. Proper risk management frameworks enable banks to identify early warning signals, such as declining profitability, irregular repayment patterns, and operational inefficiencies in borrower firms.

Modern banks are increasingly adopting structured credit risk management models incorporating risk-rating systems, financial analysis, and internal controls. These systems help banks maintain financial stability and minimise credit losses by identifying potential defaults early (Basel Committee on Banking Supervision, 2017).

2.3 Working Capital Financing Problems

Working capital financing is vital for the operational sustainability of businesses, particularly for small and medium-sized enterprises that rely heavily on short-term credit to manage daily activities. However, several challenges are associated with the management and utilisation of working capital loans. One major problem is inefficient cash flow management within borrowing



firms. When businesses fail to maintain a proper balance between receivables, inventory, and payables, they may experience liquidity shortages that affect their ability to meet repayment obligations (Pandey, 2015).

Another common issue arises from the improper utilisation of working capital funds. Some firms divert working capital loans to long-term investments or non-business purposes, which disrupts the intended cash cycle and weakens repayment capacity (Singh & Kumar, 2020). This misallocation of funds can create financial imbalances that ultimately lead to loan defaults.

Furthermore, inadequate monitoring by banks can contribute to working capital financing problems. If financial institutions do not regularly review stock statements, sales records, and operational performance, they may fail to detect financial distress within borrower firms. Therefore, effective monitoring mechanisms are necessary to ensure that working capital financing supports productive business activities and does not contribute to rising NPAs (Brigham & Ehrhardt, 2017).

2.4 SME Loan Defaults

Small and medium-sized enterprises (SMEs) play a significant role in economic development by generating employment, promoting innovation, and supporting industrial growth. Despite their importance, SMEs face difficulties accessing formal credit due to limited financial resources and unstable income patterns (Beck, Demirgüç-Kunt, & Maksimovic, 2005).

Studies show SME loan defaults are linked to inadequate business planning and weak financial management. Entrepreneurs lacking financial knowledge may mismanage cash flows, increasing financial distress risk (Fatoki & Odeyemi, 2010).

SMEs are highly sensitive to external economic conditions affecting business revenue and profitability. SME loan defaults represent a substantial credit risk for banks, requiring improved risk assessment mechanisms (Berger & Udell, 2006).

Lusardi and Mitchell (2014) showed that limited financial knowledge leads to poor financial decisions and debt. They argued that financial literacy improves financial planning and credit management.



Mishra and Mohanty (2022) found entrepreneurs with higher financial literacy demonstrate better loan utilisation and repayment behaviour, improving working capital management.

The OECD (2022) revealed that financial literacy influences financial behaviour in budgeting, saving, and borrowing. The Reserve Bank of India (2022) introduced the National Strategy for Financial Education 2020–2025 to improve financial awareness.

The RBI (2023) highlighted concerns regarding non-performing assets, emphasizing the need for financial literacy programs. Sharma and Singh (2021) found that financial literacy improves understanding of financial services, reducing loan default risk.

Singh and Kumar (2020) showed efficient working capital management helps maintain liquidity. Financial literacy can assist entrepreneurs in managing working capital and ensuring timely loan repayment.

The World Bank (2022) emphasized financial literacy's importance in promoting financial inclusion and responsible debt management. Yadav and Sharma (2023) found borrowers with higher financial literacy show stronger repayment discipline.

Demirgüç-Kunt, Klapper, Singer, and Ansar (2022) showed financial literacy is critical for effective use of financial services. Kapoor and Kulshrestha (2021) identified poor credit appraisals and inadequate financial management as causes of non-performing assets, emphasizing financial literacy's role in reducing defaults.

2.5 RESEARCH QUESTIONS

1. What is the level of financial literacy among borrowers who avail working capital financing?
2. How does financial literacy influence borrowers' credit utilisation and repayment behaviour?
3. What are the major causes of NPAs in working capital financing?
4. How effective are financial education programs in improving borrowers' financial decision-making?
5. What strategies can banks adopt to enhance financial literacy among borrowers and reduce non-performing assets?



2.6 OBJECTIVES OF THE STUDY

1. To examine the level of financial literacy among borrowers using working capital financing.
2. To analyse the relationship between financial literacy and the occurrence of Non-Performing Assets (NPAs) in banks.
3. To evaluate the role of financial education in improving borrowers' loan repayment behaviour
4. To study the impact of financial literacy on effective working capital management among borrowers.
5. To suggest measures for reducing bank NPAs through improved financial literacy and borrower education programs

2.7 HYPOTHESES OF THE STUDY

H1: Financial literacy has a significant positive impact on borrowers' loan repayment behaviour.

H2: Higher levels of financial literacy among borrowers lead to lower levels of non-performing assets in working capital financing.

H3: Financial education programmes significantly improve borrowers' financial management and credit utilization practices

3. METHODS

This study adopts a systematic methodological framework to examine the importance of financial literacy and education for borrowers in minimising bank non-performing assets (NPAs) in working capital financing. The research methodology outlines the procedures used to collect, analyse, and interpret data related to financial literacy and borrower behaviour.

3.1 Research Design

This study adopts a descriptive and analytical research design. The descriptive approach explains the concepts of financial literacy, working capital financing, and the causes of NPAs in the banking sector. The analytical approach examines the relationship between financial literacy and borrowers' loan repayment behaviour. This design is suitable for understanding how financial knowledge influences borrowers' financial decisions and credit management practices.



3.2 Nature of the Study

This research is primarily conceptual and empirical in nature. It attempts to analyse the theoretical framework of financial literacy along with its practical implications for borrowers who utilise working capital loans from banks. The study also examines how borrower education can improve financial management and reduce the risk of loan default.

3.3 Data Sources

This study is based on both primary and secondary sources of data. Primary data were collected through structured questionnaires distributed among borrowers who had availed working capital financing from banks, particularly small business owners and entrepreneurs. The questionnaire included questions related to financial knowledge, financial behaviour, credit utilisation, and loan repayment practices. Secondary data were collected from various sources, including academic journals, banking reports, government publications, financial literacy surveys, books, and reports published by institutions such as the Reserve Bank of India, the World Bank, and the OECD. These sources provide information on financial literacy trends, banking performance, and the status of NPAs in the banking sector.

3.4 Sampling Technique and Sample Size

This study uses a simple random sampling technique to select respondents from borrowers who have obtained working capital loans from banks. This sampling method ensures that each borrower has an equal opportunity to be included in the study, thereby reducing the research bias.

The study considers a sample of 140 respondents, comprising 50 bank officials and 90 borrowers associated with working capital lending. The selected respondents represent various banking institutions and business sectors to ensure a balanced understanding of the factors contributing to NPAs.

3.5 Data Collection Tools

Primary data were collected using a structured questionnaire designed to assess borrowers' levels of financial literacy. The questionnaire included multiple sections covering demographic information, financial knowledge, credit utilisation practices, and loan repayment behaviour.



3.6 Data Analysis Techniques

The collected data were analysed using descriptive statistical tools, such as percentages, averages, and tables. These tools helped interpret the level of financial literacy among borrowers and identify patterns in loan repayment behaviour. The analysis also examined the relationship between financial literacy and the occurrence of NPAs.

4. DATA ANALYSIS AND INTERPRETATION

Data analysis is an important part of research as it helps in understanding the relationship between financial literacy and the reduction of non-performing assets (NPAs) in working capital financing. The analysis presented below is based on conceptual data related to borrowers' financial literacy levels, loan utilisation behaviour, and repayment performance. The data are interpreted to identify how financial literacy influences financial decision-making and credit management among borrowers.

Table 1: Level of Financial Literacy among Borrowers

Level of Financial Literacy	Number of Borrowers	Percentage (%)
High Financial Literacy	40	40%
Moderate Financial Literacy	35	35%
Low Financial Literacy	25	25%
Total	100	100%

Source: Authors Compilation

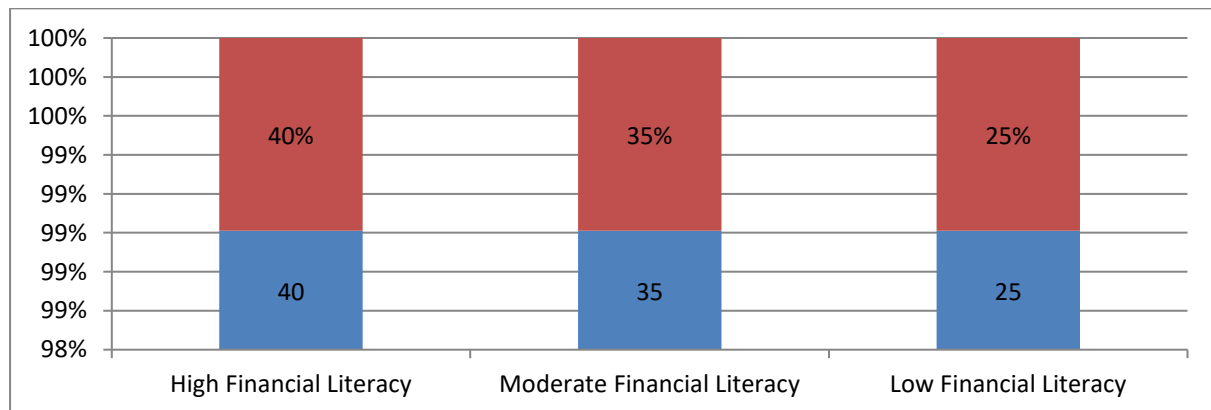


Figure 2. Level of Financial Literacy among Borrowers



Interpretation

Table 1 shows the distribution of borrowers based on their financial literacy levels. Of the total respondents, **40% of borrowers possessed high financial literacy**, indicating that they had adequate knowledge about financial management, loan obligations, and credit utilisation. Approximately **35% of borrowers demonstrated moderate financial literacy**, meaning that they had basic financial knowledge but may have lacked advanced financial planning skills. However, **25% of borrowers had low financial literacy**, which indicated a limited understanding of financial concepts such as interest rates, repayment schedules, and working capital management.

Borrowers with lower financial literacy are more likely to face difficulties in managing loan funds effectively. Consequently, inadequate financial knowledge can contribute to inefficient credit utilisation and increase the possibility of loan default. Therefore, improving borrowers' financial literacy can play a crucial role in reducing NPAs in the banking sector.

Table 2: Financial Literacy and Loan Repayment Behaviour

Financial Literacy Level	Timely Repayment (%)	Delayed Repayment (%)
High Literacy	85%	15%
Moderate Literacy	65%	35%
Low Literacy	40%	60%

Source: Authors Compilation

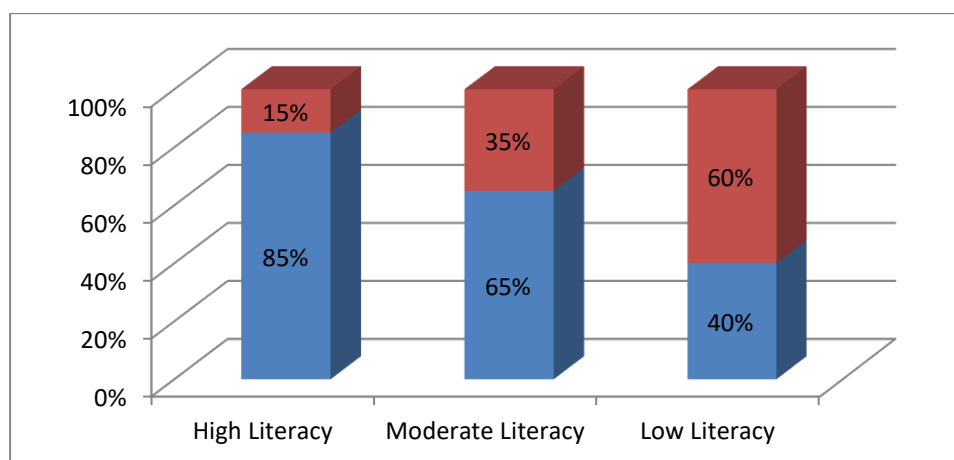


Figure 3. Financial Literacy and Loan Repayment Behaviour



Table 2 illustrates the relationship between financial literacy and loan repayment behaviour. Borrowers with high financial literacy demonstrated the highest rate of timely repayment (85%), indicating that they possessed better financial management skills and understood the importance of maintaining credit discipline.

Borrowers with moderate financial literacy have a timely repayment rate of 65%, suggesting that basic financial knowledge helps borrowers manage loan obligations but may not always prevent financial difficulties.

Borrowers with low financial literacy exhibited the highest level of delayed repayment (60%), indicating a greater risk of loan default. These borrowers may lack proper financial planning, budgeting skills, and an understanding of credit obligations.

The analysis clearly indicates that higher financial literacy leads to improved repayment behaviour, which helps reduce the occurrence of non-performing assets in working capital financing.

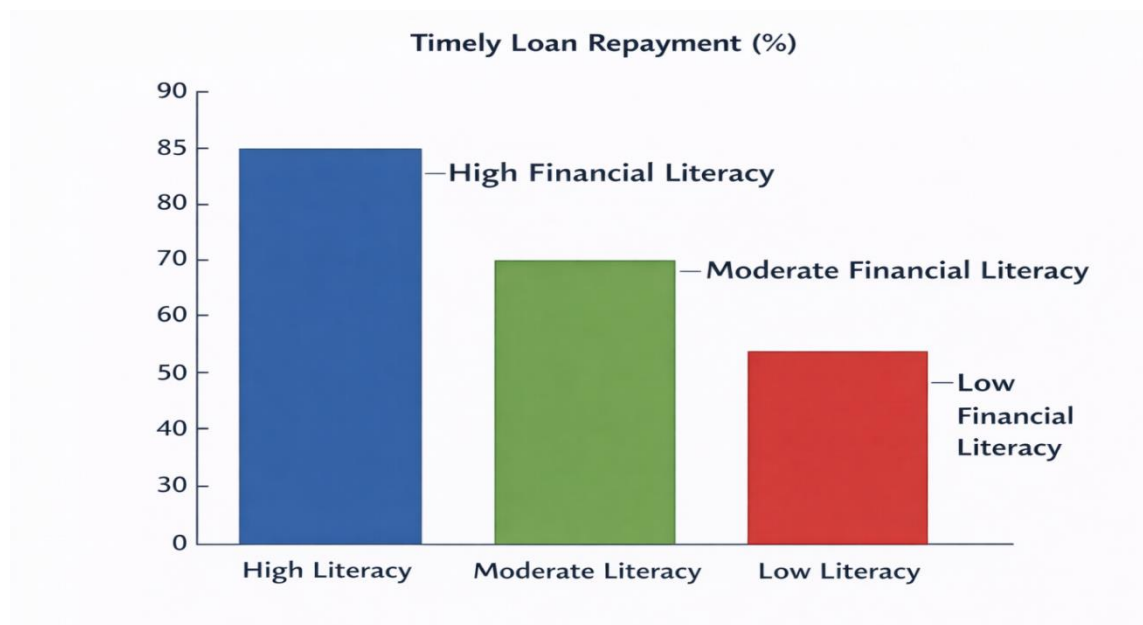


Figure 4: Relationship between Financial Literacy and Loan Repayment Behaviour

Figure 4 shows the relationship between financial literacy levels and timely loan repayment among borrowers. Borrowers with high financial literacy exhibited the highest level of repayment discipline, whereas borrowers with low financial literacy showed significantly lower repayment rates. This indicates that financial literacy plays a vital role in promoting responsible borrowing behaviour.



The analysis highlights that increasing financial awareness and borrower education can significantly improve financial management practices and reduce the risk of loan defaults. Consequently, financial literacy programs implemented by banks and financial institutions can serve as an effective strategy for minimising NPAs in working capital financing.

5. DISCUSSION

This study examined the importance of financial literacy and education among borrowers in minimising non-performing assets (NPAs) in working capital financing. The findings indicate that financial literacy influences borrowers' financial behaviour, credit management, and repayment discipline. The discussion interprets results in light of existing literature and theoretical perspectives on financial literacy and banking stability.

The analysis revealed that borrowers with higher financial literacy demonstrate better financial management and are more likely to repay loans on time. Financially literate borrowers understand interest rates, loan terms, repayment schedules, and default consequences better. They utilise working capital loans more efficiently and maintain financial discipline. This finding aligns with Lusardi and Mitchell, who emphasised that financial literacy improves financial planning and helps avoid excessive debt.

Another observation is the relationship between financial literacy and effective working capital management. Borrowers who understand financial concepts like cash flow management, budgeting, and planning manage business finances better. Proper working capital management helps maintain liquidity, avoid financial distress, and ensure timely loan repayments. In contrast, borrowers with limited financial knowledge may struggle with business expenses, leading to inefficient use of funds and increased default risk.

This study highlights that inadequate financial literacy contributes to rising NPAs in banking. Many borrowers, especially small entrepreneurs and business owners, lack formal financial education and rely on informal knowledge for financial decisions. This lack of awareness may result in poor planning, fund misallocation, and inability to meet repayment obligations. Consequently, loan accounts may become non-performing assets, affecting banks' financial stability.



The study emphasizes the importance of financial education programmes in improving borrowers' capability. Financial literacy initiatives by banks, government agencies, and institutions can enhance understanding of financial products and responsible borrowing. Such programs help develop essential financial skills like budgeting, debt management, and planning. These initiatives can contribute to better credit utilisation and lower default rates.

The findings align with previous research showing the positive relationship between financial literacy and inclusion. When borrowers possess financial knowledge, they are more likely to access formal financial services and manage credit responsibly. This benefits borrowers and strengthens the banking system by reducing credit risk and improving loan recovery.

However, despite recognition of financial literacy's importance in financial stability, challenges persist. Financial literacy levels in developing economies remain low, particularly among rural populations and small business owners. Limited access to financial education, product awareness, and complex financial systems continues to hinder literacy initiatives.

6. CONCLUSIONS

This study examined the importance of financial literacy and education among borrowers in minimising non-performing assets (NPAs) in working capital financing. The findings indicate that financial literacy plays a significant role in influencing borrowers' financial decision-making, credit management practices, and repayment behaviour. In modern financial systems, borrowers frequently interact with complex financial products, such as loans, credit facilities, and banking services. Without adequate financial knowledge, borrowers may face difficulties in managing borrowed funds and fulfilling repayment obligations, which can ultimately contribute to the rise in NPAs in the banking sector.

This study highlights that borrowers with higher levels of financial literacy are better equipped to manage working capital efficiently. Financially literate borrowers tend to maintain proper financial planning, budgeting, and cash flow management, which enables them to utilise loan funds productively. Consequently, they are more likely to repay their loans on time and maintain credit discipline. On the other hand, borrowers with limited financial knowledge often struggle to manage business finances effectively, leading to inefficient credit utilization and increased risk of loan default.



Another important conclusion of the study is that financial literacy significantly influences the financial behaviour of borrowers. Borrowers who understand financial concepts, such as interest rates, repayment schedules, and financial risk, are more capable of making informed financial decisions. Such knowledge helps borrowers avoid over-borrowing, misuse of loan funds, and financial mismanagement. Consequently, improving borrowers' financial literacy can contribute to reducing the occurrence of loan defaults and strengthening the financial health of banking institutions.

This study also emphasises the roles of banks and financial institutions in promoting financial literacy. Financial literacy programs, credit counselling services, and borrower education initiatives can help individuals understand the responsibilities associated with borrowing. These programs can enhance borrowers' financial capabilities and encourage responsible credit behaviour. In addition, integrating financial education into loan approval processes can ensure that borrowers possess adequate knowledge about financial management and repayment obligations.

Furthermore, research indicates that strengthening financial literacy can contribute to broader economic stability. Lower levels of NPAs improve the financial performance of banks and enhance their ability to extend credit to productive sectors of the economy. When borrowers utilise credit efficiently and maintain repayment discipline, it leads to improved financial inclusion, stronger banking systems, and sustainable economic development.

7. IMPLICATIONS OF THE STUDY

The findings of this study have important implications for banks, policymakers, and borrowers involved in working capital financing. From a banking perspective, the study highlights the importance of strengthening credit risk management practices to reduce the occurrence of non-performing assets. Banks need to adopt more rigorous credit appraisal procedures that carefully evaluate the financial health, repayment capacity, and operational stability of borrowers before granting working capital loans. In addition, continuous monitoring of loan utilisation and early detection of financial distress among borrowers can help financial institutions take timely corrective measures and prevent loan accounts from becoming non-performing.

The study also emphasises the role of borrower awareness and financial literacy in maintaining healthy credit behaviour. Borrowers who possess adequate financial knowledge are more capable of managing business finances, maintaining proper cash flow planning, and meeting repayment



obligations. Therefore, banks and financial institutions should actively promote financial education programs, advisory services, and credit counselling initiatives for borrowers, particularly for small business owners and MSME entrepreneurs.

From a policy perspective, regulatory authorities can support the banking sector by encouraging responsible lending practices and improving financial awareness. Strengthening collaboration between banks, government institutions, and financial education agencies can enhance borrower capability and contribute to the long-term stability of the banking system

8. FUTURE RESEARCH DIRECTIONS

Although the present study provides useful insights into the prevention of NPA in working capital financing, several areas remain open for further research. Future studies may expand the geographical scope of the analysis by including borrowers and banking institutions from multiple states or regions. A broader regional comparison would provide deeper insights into variations in lending practices, borrower behaviour, and sector-specific credit risks across different parts of the country.

Further research may also examine the role of technological innovations in reducing NPAs. The increasing use of digital banking systems, artificial intelligence, and data analytics in credit assessment offers new opportunities to improve credit risk evaluation and monitor borrower activities. Investigating how such technological tools influence loan performance could provide valuable insights for modern banking systems.

Another potential area for future research is a sectoral analysis of loan defaults. Different sectors, such as manufacturing, agriculture, and services, may exhibit distinct patterns of credit utilisation and repayment behaviour. Studying these sector-specific dynamics can help financial institutions design more targeted risk management strategies.

Finally, future research may explore behavioural and psychological factors that influence borrowers' financial decision-making. Understanding how attitudes toward risk, financial planning, and credit obligations affect repayment behaviour could further contribute to the development of more effective strategies for preventing NPAs in working capital financing.



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