FinLit news

SPRING 2013 NEWSLETTER
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Message from the Academic Director, Annamaria Lusardi

Dear Friends and Colleagues,

The Global Center for Financial Literacy at the George Washington School of Business is celebrating its one year anniversary, and Financial Literacy Month seems the perfect time to launch our newsletter and let you know what we've accomplished in the last year as well as what lies ahead for us. We are also excited to unveil our new name: Global Financial Literacy Excellence Center (GFLEC).

In this past year, the Center has grown from being made up of just one person, myself, to being a team of four full-time members and several part-time researchers and consultants. We have hit the ground running by completing several research projects on financial literacy, organizing a global summit, hosting a financial literacy seminar series, and starting a policy perspectives luncheon series. We hope you will enjoy reading about our activities.

We take pride in being part of the movement to raise financial literacy awareness this month and throughout the year. We hope you will continue to join us in these efforts.

Warm regards,
Anna

"Just as it was not possible to live in an industrialized society without basic literacy – the ability to read and write – so it is not possible to live in today's world without being financially literate. Financial literacy is an essential skill for full participation in society."

Annamaria Lusardi, PhD

Featured Research Paper: Optimal Financial Knowledge and Wealth Inequality

In this paper, we explore two questions: (1) What forces shape financial knowledge accumulation over the life cycle? and (2) How much wealth inequality can be attributable to resulting differences in financial knowledge?...

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GFLEC Hosts Global Financial Literacy Summit

When policymakers, scholars, executives, pension experts, analysts and other thought leaders from 40 countries converged at a high-profile summit sponsored by the Global Financial Literacy Excellence Center (GFLEC)....

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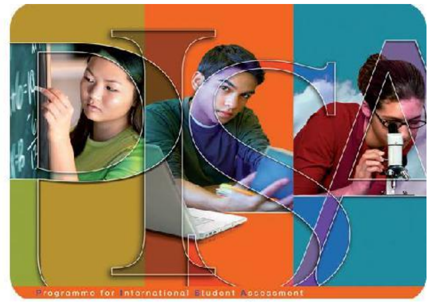

OECD PISA Financial Literacy Assessment

The Programme for International Student Assessment (PISA) aims to evaluate education systems around the world by assessing 15-year-olds' competencies in key subjects: reading, mathematics and science. In 2012, PISA added....

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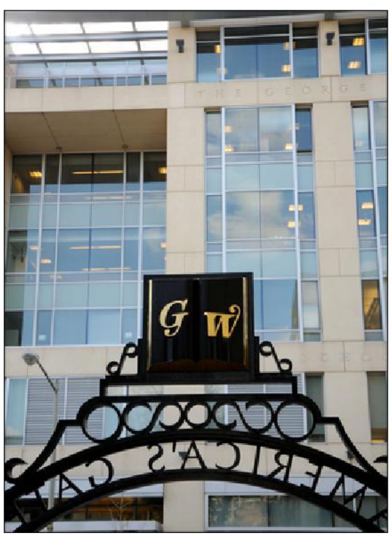
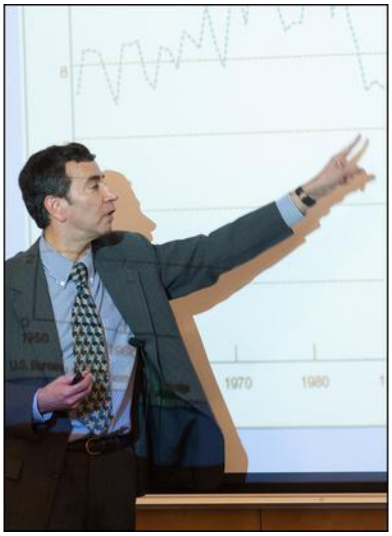
GFLEC Happenings



Chairman Bernanke Lectures at George Washington School of Business

Chairman Ben Bernanke delivered four lectures on the history of the Fed at George Washington School of Business. Together, the lectures made up a course titled "Reflections on the Federal Reserve and its Place in Today's Economy" and provided a firsthand look at the inner-workings of the U.S. central banking system. Chairman Bernanke's first two lectures covered the origins and mission of the Fed and the role and actions of the Fed in the period following WWII. His final two lectures reviewed some of the causes of, and policy responses to, the recent financial crisis, focusing specifically on the actions of the Fed. Director Lusardi was one of the faculty members chosen to lecture in this course.

To watch the lectures, please click here.



FRB & GFLEC Host Financial Literacy Seminar Series

The Financial Literacy Seminar Series (FLSS) is a joint initiative of the Board of Governors of the Federal Reserve System (FRB) and the Global Financial Literacy Excellence Center (GFLEC). The objective of the seminar series is not only to present and discuss financial literacy research but also to provide a forum where academics, practitioners, policymakers, and others can interact and share ideas on this important topic.

Sheldon Garon, Nissan Professor of History and East Asian Studies at Princeton University, provided the Distinguished Financial Literacy Lecture as part of FLSS in the 2012 fall term. Garon presented his new book....

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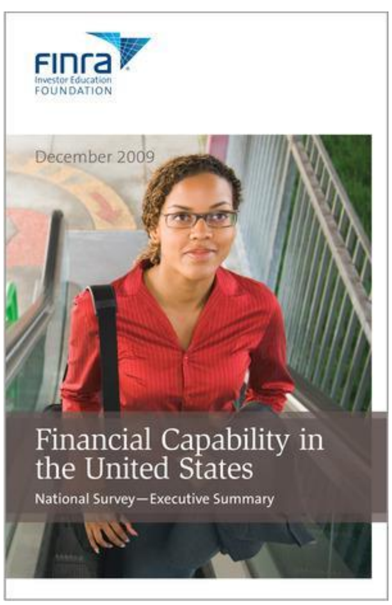
Financial Literacy Policy Perspectives Luncheon Series

The Luncheon Series is another way GFLEC brings together thought leaders to discuss financial literacy. We started the series in November 2012 when Diana Crossan, Commissioner for the New Zealand Commission for Financial Literacy & Retirement Income, visited GFLEC.

Our most recent luncheon was held on April 9, 2013, and featured our visiting scholar, Monica Aparicio Smith, former head of the Colombian Deposit Insurance Corporation (Fogafin). She spoke about her experience with financial literacy policies to representatives from institutions such as the Federal Deposit Insurance Corporation, World Bank, and Consumer Financial Protection Bureau.



FINRA Investor Education Foundation Roundtable Spotlights National Financial Capability Study

When the FINRA Investor Education Foundation scheduled a roundtable meeting in Washington, D.C., in mid-2012, the goal was to discuss findings from the 2009 National Financial Capability Study (NFCS) with researchers, policymakers, and practitioners. The meeting also looked at ways to promote the 2012 NFCS.

The May meeting, hosted by the Global Financial Literacy Excellence Center, drew participants from across the country and fueled substantive discussion on a spectrum of issues, from retirement planning to day-to-day financial management....

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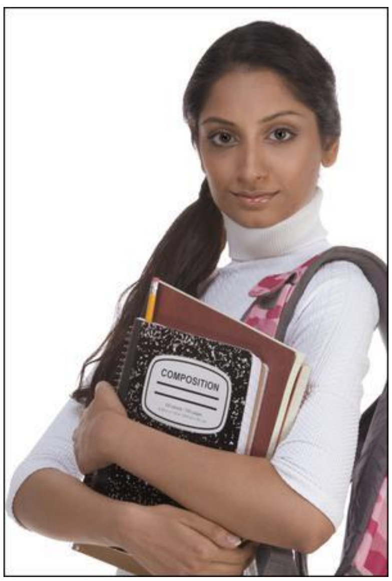
Improving Financial Literacy and Capability: What Works?

At a gathering co-sponsored by the Financial Literacy Center, a joint center of RAND, Dartmouth College and the Wharton School, academics and practitioners in the field of financial literacy came together at George Washington School of Business to report on new research projects.

The discussions touched on a range of issues, from how to measure financial literacy and capability to financial literacy programs at different stages of the life cycle. Participants also discussed financial literacy programs in school, in the workplace, and for vulnerable groups.

The daylong conference, titled “Improving Financial Literacy and Capability: What Works?” covered more than a dozen projects. View videos and presentations from the conference by clicking here.



GFLEC Studies Effectiveness of High School Program

It is one thing to design a financial literacy program for teenagers. It is quite another to design a financial literacy program for teenagers that works— with metrics to prove it.

The Global Financial Literacy Excellence Center (GFLEC) and the Council for Economic Education (CEE), with the support of Bank of America, are aiming for proven effectiveness with their new study, “the Effectiveness of Financial Fitness for Life.”

The study, which hopes to launch in Texas in the summer of 2013, will measure the effectiveness of Financial Fitness for Life (FFFL)

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Credit Unions Discuss How to Promote Good Financial Choices

Credit unions embrace financial literacy as part of their consumer-focused mission and they look for strategies that are effective in today’s quick-changing financial landscape. The “From Financial Literacy to Financial Capability” research colloquium hosted by the Global Financial Literacy Excellence Center brought together researchers and industry experts to discuss ways to promote good financial choices among clients while simultaneously meeting business goals. Filene Research Institute, a nonprofit dedicated to the analysis of issues affecting the future of consumer finance, sponsored the event…….

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Optimal Financial Knowledge and Wealth Inequality
By Annamaria Lusardi, Pierre-Carl Michaud and Olivia S. Mitchell

In this paper, we explore two questions: (1) What forces shape financial knowledge accumulation over the life cycle? and (2) How much wealth inequality can be attributable to resulting differences in financial knowledge? These questions have not been studied in a rich theoretical context including uncertainty, and our analysis can shed light on the important issue of wealth disparities over the life cycle.

We build and calibrate a life cycle model featuring uncertainty in income, capital market returns, and medical expenditures; we also incorporate an endogenous knowledge accumulation process and a sophisticated saving technology. In the model, financial knowledge permits consumers to use sophisticated financial products which can help them raise the return earned on financial assets. Individuals who wish to transfer resources over time by saving will benefit most from financial knowledge. Moreover, because of how the U.S. social insurance system works, better-educated individuals have the most to gain from investing in financial knowledge. As a result, making financial knowledge accumulation endogenous allows for an amplification of differences in accumulated retirement wealth over the life cycle.

We report several important findings. First, our model can explain why many consumers lack knowledge about key aspects of financial markets. Several papers have reported that a large proportion of the population is not financially literate and cannot grasp the concepts of inflation and risk diversification.

Second, we show that some level of financial ignorance may, in fact, be optimal. That is, we explain why consumers may rationally fail to invest in knowledge, since it is expensive to acquire financial knowledge and not everyone will benefit from greater financial sophistication.

Third, our model generates wealth inequality above and beyond what traditional models of saving normally deliver. Thus, it helps account for some of the large differences in wealth reported in the literature by recognizing that individuals do not start their economic lives with full financial knowledge and that knowledge can be acquired endogenously over the life cycle.

Fourth, we show that financial knowledge can be an important public policy lever. For example, reducing the cost of financial knowledge by providing financial education in high school could have potentially large effects on wealth accumulation and welfare. We report that a 25-year-old college graduate would be willing to pay more than half of his initial wealth to boost financial knowledge if this offered an expected permanent increase of 1% in his annual rate of return. Our estimates also suggest that over half of wealth inequality can be attributed to financial knowledge.

"Optimal Financial Knowledge and Wealth Inequality" is part of the working paper series of the National Bureau of Economic Research. It can be accessed here.

OECD PISA Financial Literacy Assessment

The Programme for International Student Assessment (PISA) aims to evaluate education systems around the world by assessing 15-year-olds' competencies in key subjects: reading, mathematics and science. In 2012, PISA added financial literacy to the list of subjects, thus creating the first large-scale global assessment of the financial literacy of young people.

Director Lusardi chaired PISA's Financial Literacy Experts Group. These experts—including regulators as well as people from central banks, Treasury departments, and other institutions in charge of financial literacy—developed a financial literacy framework and used that framework to design a financial literacy assessment.

The Organisation for Economic Co-operation and Development (OECD) launched PISA in 1997. PISA assesses the following:

"Are students well prepared to meet the challenges of the future? Can they analyse, reason and communicate their ideas effectively? Have they found the kinds of interests they can pursue throughout their lives as productive members of the economy and society? The OECD Programme for International Student Assessment (PISA) seeks to answer these questions through the most comprehensive and rigorous international assessment of student knowledge and skills."

The OECD anticipates that younger generations will handle more complex financial products and services than their parents. They are also likely to face more financial risks in adulthood, especially when it comes to savings, retirement planning and health care coverage. Moreover, high school students must decide whether or not to invest in higher education. The decision, which can markedly affect wages and income over one's lifetime, must be considered against the rising costs of a college education.

Comparing levels of financial literacy across countries makes it possible to identify effective national strategies and best practices. Students in 65 countries or regions participated in PISA 2012. Students from 18 of these countries—Australia, Belgium, China, Colombia, Croatia, Czech Republic, Estonia, France, Israel, Italy, Latvia, New Zealand, Poland, Russia, Slovak Republic, Slovenia, Spain and the United States—tackled questions directly related to financial literacy. PISA findings about financial literacy will be released in the spring of 2014.

For more information about PISA Financial Literacy Assessment, please click here.

Center Hosts Global Financial Literacy Summit

Policymakers, scholars, executives, pension experts, financial analysts and other thought leaders from 40 countries converged in Amsterdam in November at a high-profile summit sponsored by the Global Center for Financial Literacy.

The new global economic landscape, marked by changes in pension options, workforce needs and financial markets, has elevated the urgency for financial literacy, Annamaria Lusardi, academic director of the Global Center for Financial Literacy, told summit participants. She added that individuals are required to make more complex financial decisions at each stage of their life, underscoring the lifelong need for financial competency.

"Just as it was not possible to live in an industrialized society without literacy—the ability to read and write—so it is not possible to live in today's world without being financially literate," Lusardi said. "To fully participate in society today, financial literacy is critical."

Participants from all around the world came together at the Global Financial Literacy Summit to present analysis and discuss the state of financial literacy around the world, as well as ways to improve basic financial knowledge.

Italy's minister of Labour, Social Policies and Equal Opportunity, Elsa Fornero, one of the spotlighted presenters at the summit said the level of financial literacy necessary in today's world goes beyond basic knowledge of money matters.

"You need to give people more structure to understand their life cycle. This is perhaps broader than a basic financial education … and it is essential," Fornero said. "It will allow people to make the right decisions."

Fornero said this broadened approach should include efforts like those in Germany, where technical jobs—especially for young citizens—are being encouraged as platforms for economic security.

The gathering, held in conjunction with the WorldPensionSummit 2012, brought together a broad range of speakers, from Chinese and German scholars to government finance officials from the Netherlands and the Czech Republic.

Highlights of the program include:

- Flore-Anne Messy, the senior policy expert at the Organisation for Economic Co-operation and Development (OECD), discussing the need for financial literacy efforts that target women and youth.
- Timothy Flacke, executive director of Boston-based Doorways to Dreams Fund, advocating for the development of engaging and interactive "financial entertainment" that teaches how to manage money.

- Herman Tange, managing director of ING's marketing banking services in the Netherlands, outlining the role that the private sector can play in global financial education.

- Sue Lewis, an independent policy consultant in the financial services arena, presenting financial literacy case studies on the gender gap and on Latin America.

Lusardi said she was thrilled to host the summit. "There will be enormous challenges ahead as individuals around the world will increasingly be required to secure their financial well-being after retirement. We are pleased to provide a forum for solutions," she said.

The next Global Financial Literacy Summit is scheduled for **November 12, 2013**.

Click here to access the videos and PowerPoint presentations from the summit

Fed and Global Center for Financial Literacy Deepen Partnership

As self-directed portfolios replace traditional pension plans, workers determine how much money goes into accounts and how much is taken out. Research by the Federal Reserve has found that the recent economic crisis sparked more withdrawals—but not always by people undergoing financial shocks.

John Sabelhaus, who worked on the research for the Fed, said Congress recognized there might be times when early withdrawals from retirement accounts were needed. That is why the law allows it, albeit with penalties. But Sabelhaus was surprised to see how much those withdrawals have increased.

For every dollar that flowed into the retirement system in 2004, he said, about 30 cents were taken out again. "By 2010, that had risen to nearly 50 cents," Sabelhaus said, characterizing the withdrawals following the most recent recession as "substantial." He said they were especially troubling because they came at a time when both contributions to and returns on retirement accounts were low.

Sabelhaus reported the findings as part of the Financial Literacy Seminar Series, a joint initiative of the Board of Governors of the Federal Reserve System and the Global Center for Financial Literacy at the George Washington School of Business.

Last year the speakers' series, which continues semi-monthly presentations in 2013, brought together academics, practitioners, policymakers and other experts to discuss new findings around financial literacy issues. Speakers included experts from Sallie Mae, the Social Security Administration and several universities.

During a presentation in October, Jason Fichtner, senior research fellow at George Mason University's Mercatus Center, discussed how government "framing"—or presentation of information—could affect at what age Americans tap their Social Security retirement benefits.

Fichtner said there is no one-size-fits-all formula for determining when to take those payments, adding that factors such as spousal benefits and health should be considered.

"Social Security can do a better job or a more complete job with the information it hands out to beneficiaries and potential beneficiaries. I think there are many who don't realize that the decision really impacts them," Fichtner explained. "If they retire in their sixties, they're going to need income for approximately 20 years. Their decision affects how dignified and comfortable those 20 years will be."

Retirement decisions were not the only issue addressed during the series. Sheldon Garon, Nissan Professor of History and East Asian Studies at Princeton University, discussed the savings habits of U.S. residents. Garon wrote the book *Beyond Our Means: Why America Spends While the World Saves.*

“During the 20th century, in particular, Americans began to diverge from the spending and saving habits that we see in the rest of the advanced economies of the time,” Garon said. “As late as 1910, most Americans did not have a savings account or checking account. They were basically unbanked.

“That was very different from what you would have seen in Japan at the time or European countries at the time,” he added.

Garon explained that Americans had greater access to credit than their counterparts overseas. The 1980s deregulation of the American financial industry widened the gap between the United States and the rest of the world.

He said the lending process has improved and is more transparent but much more needs to be done to encourage Americans—especially low-income families—to save more. He said that includes offering savings programs that do not carry onerous fees or minimum balances.

Financial education research was the focus of the presentation by J. Michael Collins, director of the Center for Financial Security at the University of Wisconsin at Madison. He told series participants that too few studies have been done on the subject, adding that the little research currently available indicates that carefully designed educational programs can result in better financial choices.

The seminar series marks a deepening collaboration between the Fed and the George Washington University. In March 2012, Federal Reserve Chairman Ben Bernanke launched a four-part series of talks as part of an undergraduate course at GW’s School of Business. He opened with a presentation on the origins and missions of central banks. Subsequent talks looked at the role and actions of the Federal Reserve in the period after World War II and some of the causes—and the Fed’s responses—to the most recent financial crisis.

View the dates of our spring seminars.

Watch the videos and read the papers from the fall seminars.

FINRA Roundtable Spotlights NFCS

When the FINRA Investor Education Foundation scheduled a roundtable meeting in Washington, D.C., in mid 2012, the goal was to collect input from financial experts, researchers and policymakers as FINRA launched the next round of its National Financial Capability Study.

The May meeting, hosted by the George Washington School of Business, drew participants from across the country and fueled substantive discussion on a spectrum of issues, from retirement planning to whether financial literacy varies from state to state.

The high-profile meeting also looked at ways to promote the 2012 National Financial Capability Study, a survey of Americans' understanding of basic finances.

The national study carries three components: a national survey, a state-by-state analysis and a look at the financial literacy levels of military personnel. It aims to assess and establish a baseline measure of the financial capability of U.S. adults, factoring in various aspects of behavior to determine how individuals manage their resources and make financial decisions.

Because of the country's changing financial landscape, individuals must forecast their own future financial needs, be more involved in ensuring safe retirement and navigate increasingly complex financial markets. In tandem, mortgages and savings and investment products have become more complicated, and the consequences of unsound financial decisions are more severe.

Participants at the roundtable included representatives from the Federal Reserve Board, the U.S. Department of Treasury, The Pew Charitable Trusts, RAND Corp., the FDIC, the Social Security Administration, the U.S. Government Accountability Office, the Urban Institute, the U.S. Securities and Exchange Commission, the National Institute on Aging and more than a dozen universities.

GCFL Studies Effectiveness of High School Program

It is one thing to design a financial literacy program for teenagers. It is quite another to design a financial literacy program for teenagers that works—with metrics to prove it.

The Global Center for Financial Literacy and the Council for Economic Education (CEE), in partnership with Bank of America, are aiming for proven effectiveness with their new project on the "Effectiveness of Financial Fitness for Life."

The $200,000 project, which hopes to launch in 150 Virginia high schools in the summer of 2013, will measure the effectiveness of Financial Fitness for Life (FFFL), a signature program of the CEE. The council is the leading U.S. organization focused on the economic and financial education of students from kindergarten through high school.

Teachers in the study will be trained in the use of FFFL and then tracked to see how well their students perform in comparison with those of teachers without the training.

"We will analyze whether FFFL is an effective classroom tool for teaching personal finance," said Annamaria Lusardi, academic director of the Global Center for Financial Literacy and the study's director.

In 2008, high school seniors across the United States incorrectly answered more than half the questions on a national financial literacy test. A year earlier, 72 percent of 18-year-olds had savings accounts. Today only 58 percent do.

Since its introduction in 2001, FFFL has been used by more than 75,000 teachers, including 30,000 who received professional training on both its content and pedagogy. Anecdotally, FFFL is making a difference in K-12 personal finance education, with teachers giving the curriculum high rankings on the quality of the material and the ease of use. But there has been little research showing how student learning is affected by the program, which addresses key aspects of personal finance, including earning income, spending, saving, borrowing, investing and managing money.

The new study will examine whether FFFL training changes students' and teachers' knowledge of financial concepts as well as teachers' instructional practices. Teacher training will unfold during a three-day conference. Student financial knowledge will be tested before and after the intervention, taking into account CEE's soon-to-be-released national standards in personal finance.

The research team on the project includes MIT econometrician Bruno Ferman.

Lusardi characterized the research as a "starting point," noting that the study examines just one grade level of the four in the FFFL and focuses on just one type of teacher training. "Teachers receive training in FFFL in various forms, each of which would be interesting to study on its own merits in future studies or in comparison to other forms," she added.

Lusardi said it would also be valuable to examine the student performance with an eye on how different types of instructors—business teachers, consumer science educators and others—present personal lessons.

Because of Virginia's socioeconomic and cultural diversity, the study should shed light on the effectiveness of FFFL beyond that state's borders. However, a broader study or a series of studies in other states would offer additional insight. Future research could also compare states with graduation requirements in personal finance to those without in order to identify other factors that influence student achievement.

Credit Unions Play Pivotal Role

Credit unions embrace financial literacy as part of their consumer-focused mission, but they worry that their traditional strategies are not effective on today's quick-changing financial landscape. The "From Financial Literacy to Financial Capability" research colloquium at the George Washington University School of Business brought together researchers and industry experts to discuss how credit unions can promote good financial choices while simultaneously meeting business goals.

The colloquium looked at the difference between financial literacy and financial capability, the consequences of low financial literacy rates, which groups can be most effectively targeted by credit union educational efforts and the best methods by which credit unions can promote financial literacy. The gathering was sponsored by the Filene Research Institute, a nonprofit dedicated to analysis of issues affecting the future of consumer finance.

Lois Kitsch of the National Credit Union Foundation explained that credit unions have invested to provide financial education opportunities. Those investments include hosting retirement fairs, creating teaching tools and pursuing "edu-tainment" opportunities that combine education and entertainment to elevate consumers' understanding of basic financial functions.

She also described "financial reality fairs," which introduce teenagers to the types of decisions they will make in the future. Reality fair participants are assigned a salary then challenged to see if they can pay bills and meet other needs without breaking their budget. For many teens, according to Kitsch, cell phone bills proved to be the eye opener.

In a presentation on psychology—and the factors that influence decision-making—Piyush Tantia and Alex Fiorillo from Harvard University's ideas42 lab discussed ways to make financial literacy training more effective.

They discovered that the way choices are presented can affect behavior. Often, too, consumers have good intentions but don't follow through. Self control, reminders, the ease in making certain choices and other factors all influence financial decisions.

Ron Borzekowski, from the Consumer Financial Protection Bureau, detailed his agency's research as well as the work of the bureau's Office of Financial Education, which is responsible for initiatives aimed at educating consumers to make better-informed financial decisions. The work of the Office of Financial Education touches on virtually all aspects of household finance, from the management of daily transactions to the prudent use of credit products to asset accumulation and taxes.

Annamaria Lusardi, academic director of the Global Center for Financial Literacy, provided colloquium participants with a comprehensive overview of research, including financial literacy differences among demographic groups.

Other presenters at the colloquium included author and *Savvy Money* Education Director Jean Chintzy and Nick Maynard of the Doorways to Dreams (D2D) Fund, which supports social media and innovative video and gaming education to promote financial knowledge.