

**PwC-KWHS Seminar for NonProfit Leaders on Business and Financial Responsibility
December 4, 2014**

State of Affairs: FINRA Financial Capability Study Results

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What is financial capability?

Four main components:

- how people manage their resources
- how they make financial decisions
- the skill sets they use in making decisions
- the search and information elaboration that goes into their choices.

Relevance

Major changes that increase individuals' responsibility for their financial well-being

➤ Changes in the pension landscape

- DC pensions and IRAs

➤ Changes in the labor markets

- Divergence in wages – skills are critical
- One of the most important decisions (invest in education) has to be made early in life

➤ Changes in the financial markets

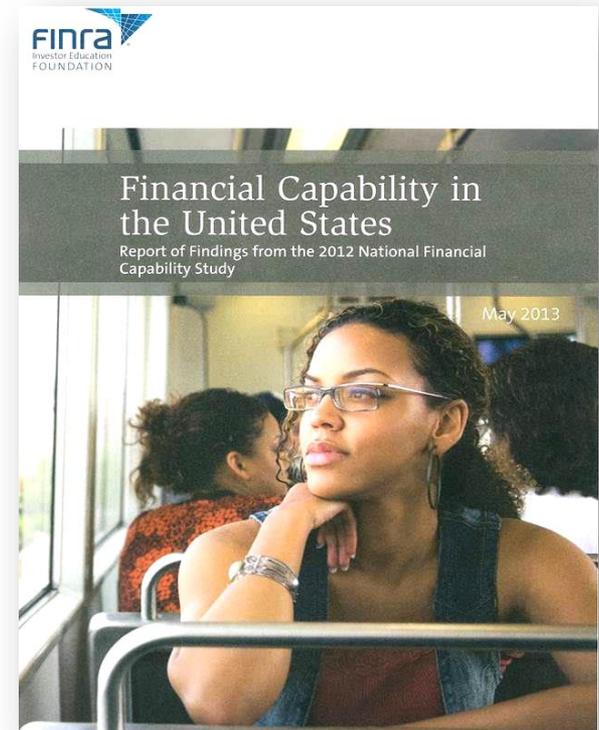
- Increased complexity, many financial products
- More opportunities to borrow and large amounts



2012 National Financial Capability Study (NFCS)

State-by-State Survey: Online survey of more than 25,000 respondents (roughly 500 per state + DC)

- Objective—Benchmark and better understand financial capability in America
- Representative of the US population
- First wave in 2009, second wave in 2012
- GFLEC has been FINRA's academic advisor on the survey



We are currently designing the 2015 wave

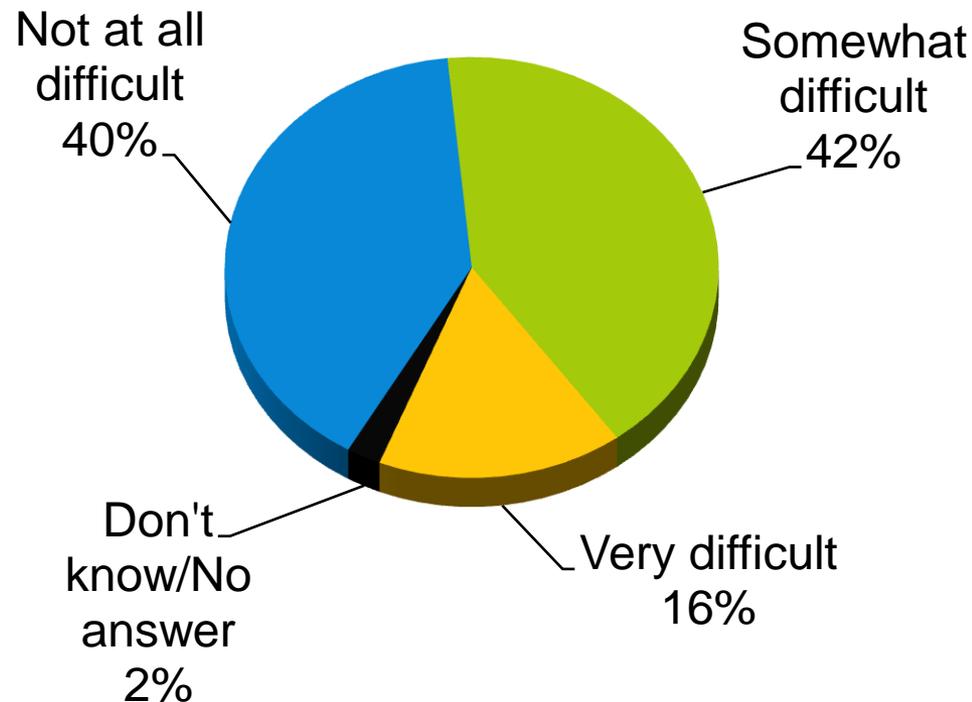
How to measure financial capability?

Four key financial capability components:

1. Making ends meet
2. Managing financial products
3. Planning ahead (short-term and long-term)
4. Financial knowledge and decision-making

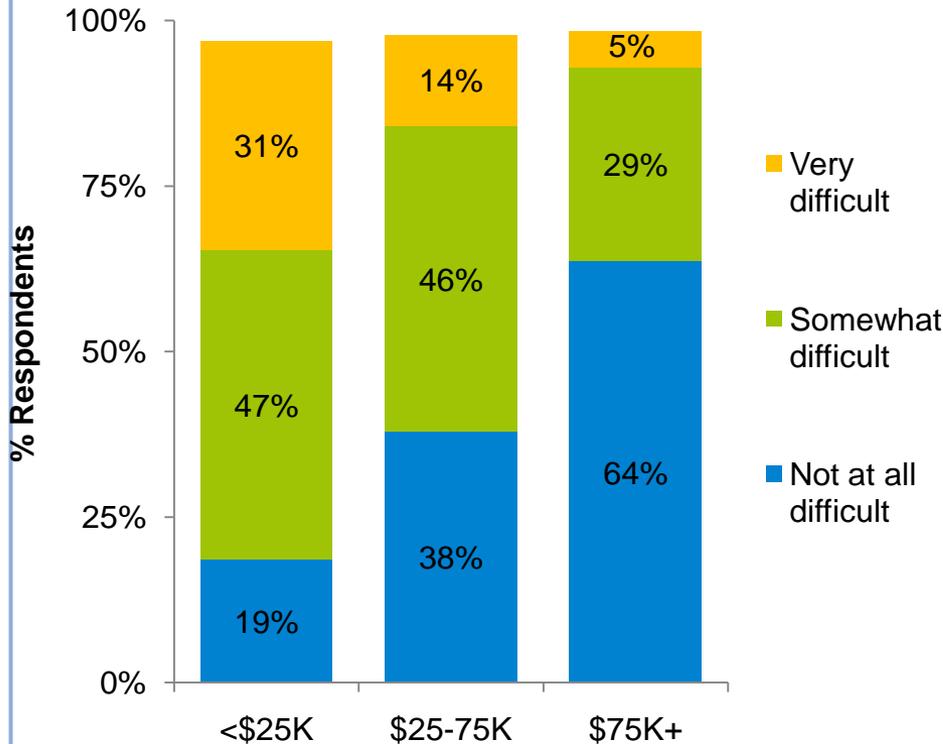
Making ends meet

In a typical month, how difficult is it for you to cover your expenses and pay all your bills?

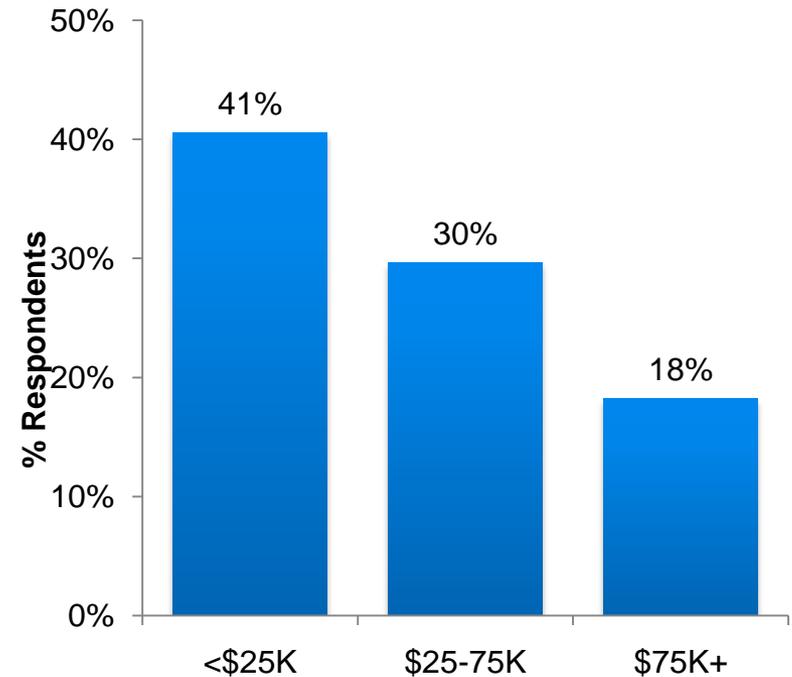


Low Income Households Under Greatest Strain

In a typical month, how difficult is it for you to cover your expenses and pay all your bills?



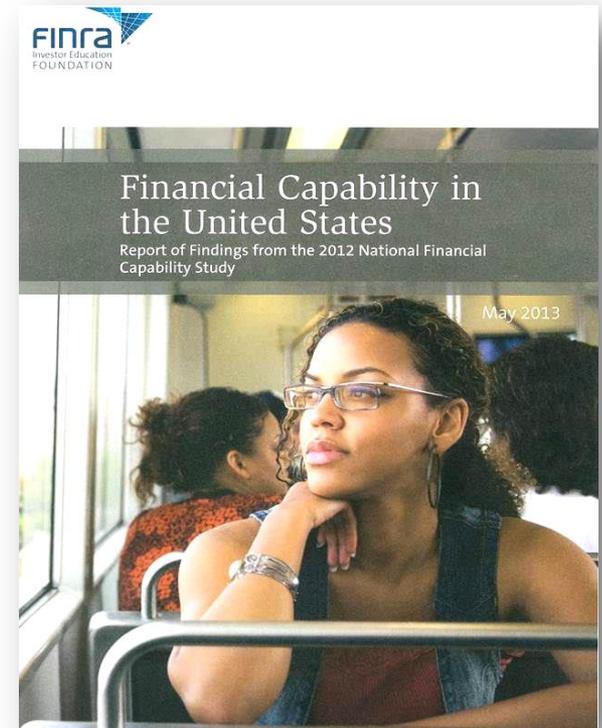
Respondents with unexpected large drop in income in past 12 months



Second component of financial capability

✓ Making ends meet

2. Managing financial products



Assets & investments

<i>Percentage of respondents with:</i>	
Checking accounts	89%
Savings accounts	72%
(% Banked)	(91%)
Any retirement accounts, employer-based or independent	57%
Investments in stocks, bonds, or mutual funds	35%
Home	58%

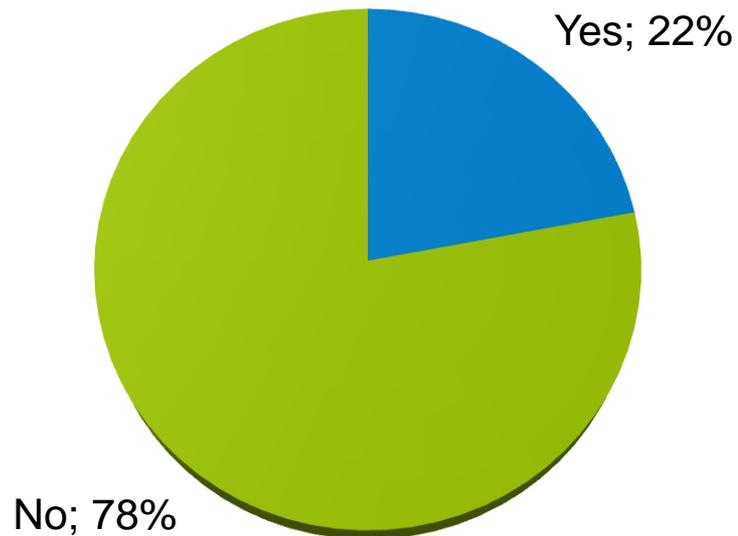
- Need to look also at the liability side of balance sheets
- Many Americans are borrowing on their assets and investments

Let's look closer at some of these assets and investments.

Overdrawing from checking accounts

- 89% of respondents have a checking account
- Many borrow from such account

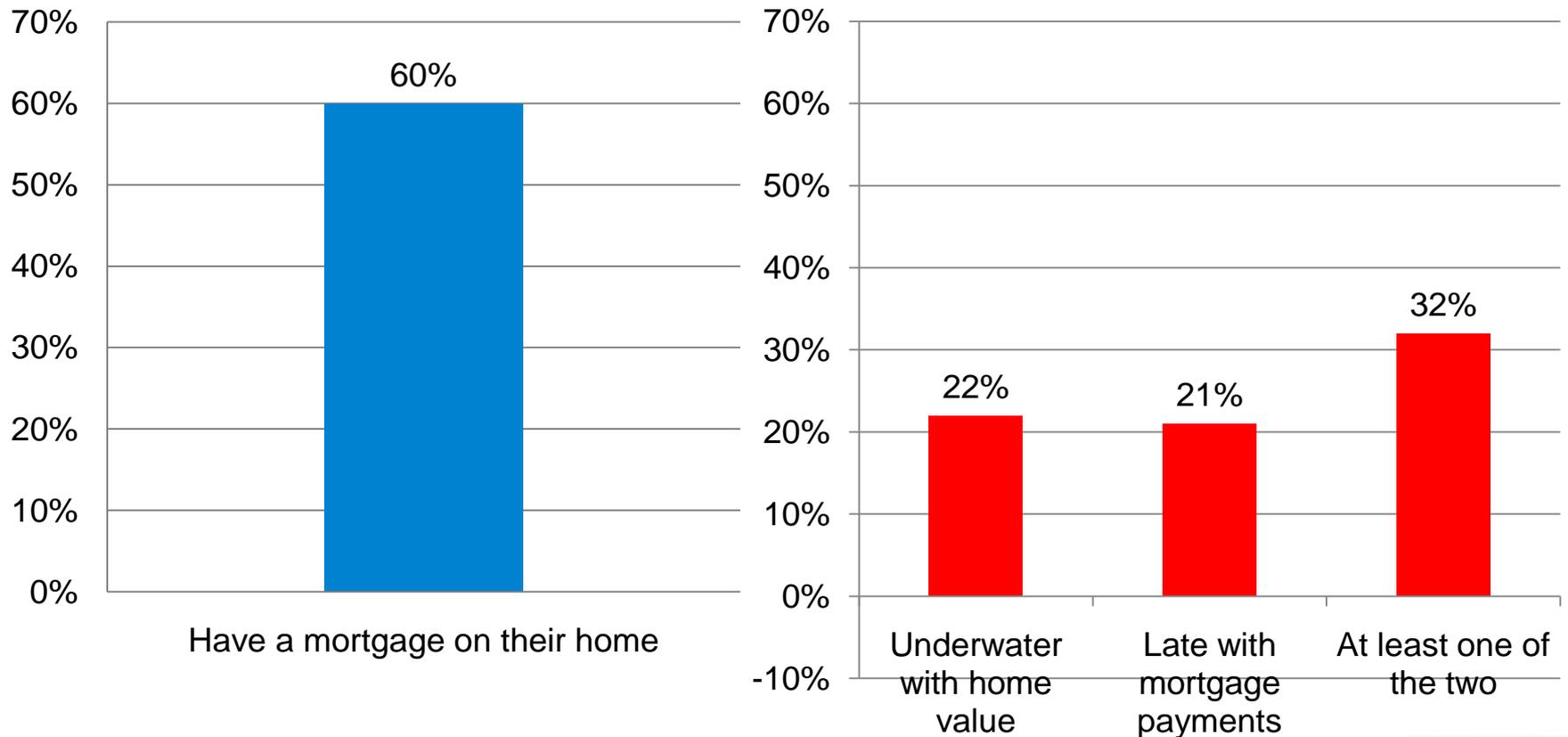
Overdraws from checking account



Note: The statistic relative to overdrawing checking account is conditional on having a checking account.

Borrowing on the home

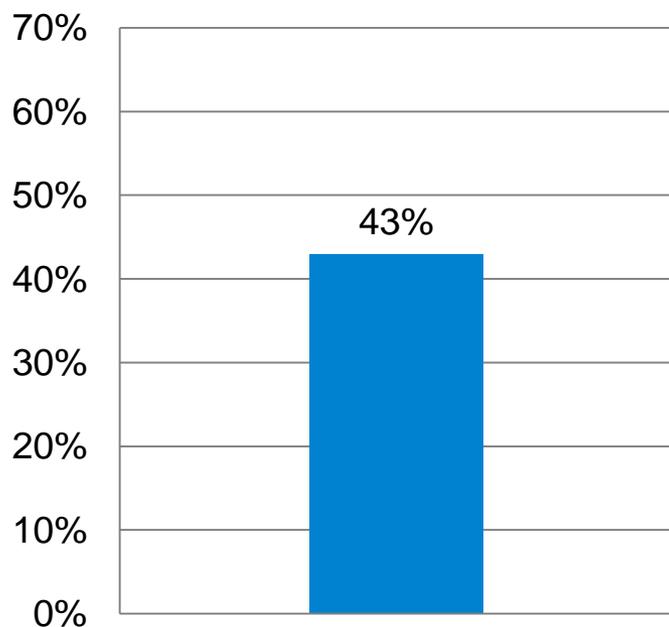
➤ Among 58% of Americans who own their home:



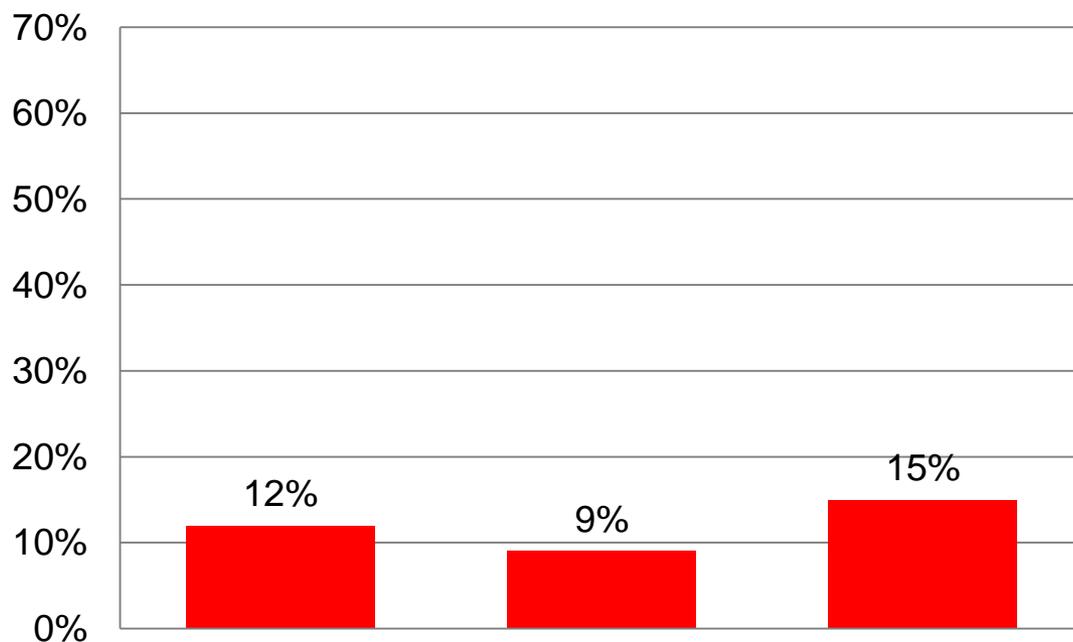
Note: The statistic relative to home mortgages and the statistics displayed in the graph at the right are conditional means.

Tapping retirement accounts

Loans and hardship withdrawals



Respondents with self-directed retirement accounts, employer-based or independent



Took a loan from retirement account

Made a hardship withdrawal

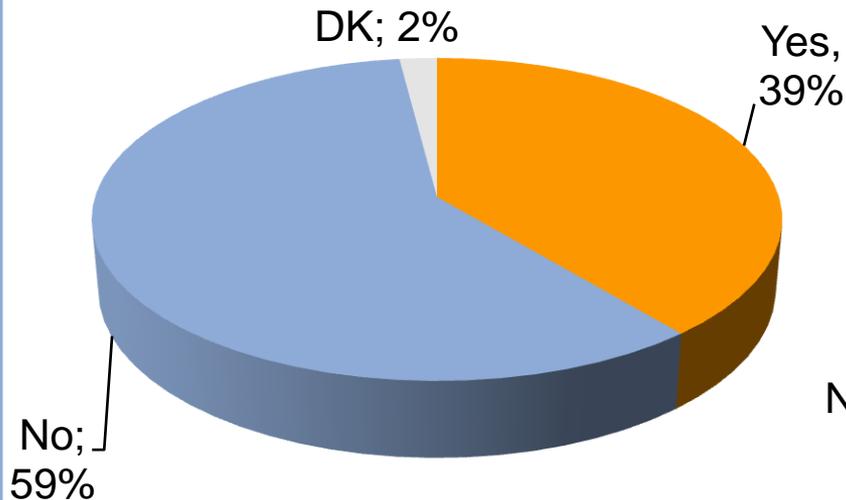
One of the two

Note: The statistics displayed in the graph at the right are conditional means.

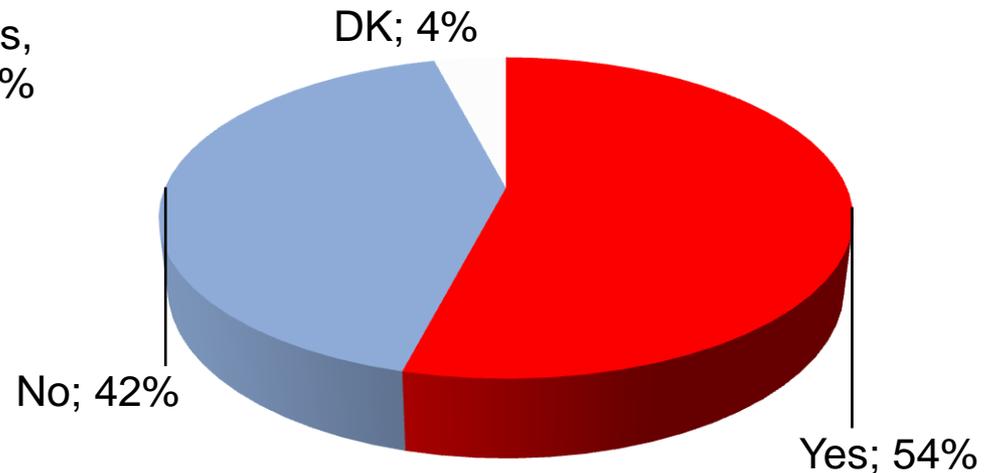
Borrowing for education (Millennials age 23-35)

- 38% of Millennials have a college degree
- Many Millennials are taking on debt to finance their education

Have a student loan



Concerned might not be able to pay off student loan



Note: The statistic relative to ability to repay student loans is conditional on having a student loan.

Millennials and student debt: is it a problem?

Student Loan Debt by Demographic Characteristic

	<i>% with outstanding student loan debt</i>	<i>% concerned about their ability to pay off the student loan</i>
Full sample	39%	54%
Age 23-29	43%	54%
Age 30-35	35%	54%
Male	37%	49%
Female	40%	57%
No undergraduate degree	29%	62%
Have undergraduate degree	55%	47%
Ethnicity - White and Asian	35%	50%
Ethnicity – African American	54%	62%
Income < \$35K	35%	67%
Income \$35K - \$75K	42%	52%
Income >\$75K	42%	34%

Note: Percentages are calculated over the relevant subsamples, i.e., 39 percent of all respondents have outstanding student loan debt, and 54 percent of these respondents are concerned about their ability to pay off the loan.

Short term debt: Credit cards

- 70% of Americans have a credit card, and among them:

In the past 12 months...	Total	18-34	35-54	55+
I always paid credit cards in full	49%	52%	40%	56%
In some months, I paid the minimum payment only	34%	44%	40%	22%
In some months, I was charged a fee for late payment	16%	23%	19%	9%
In some months, I was charged a fee for exceeding my credit line	8%	14%	9%	3%
In some months, I used the cards for a cash advance	11%	17%	12%	7%

41% of cardholders used them in “expensive” ways

High-cost borrowing: Use of Alternative Financial Services (AFS)

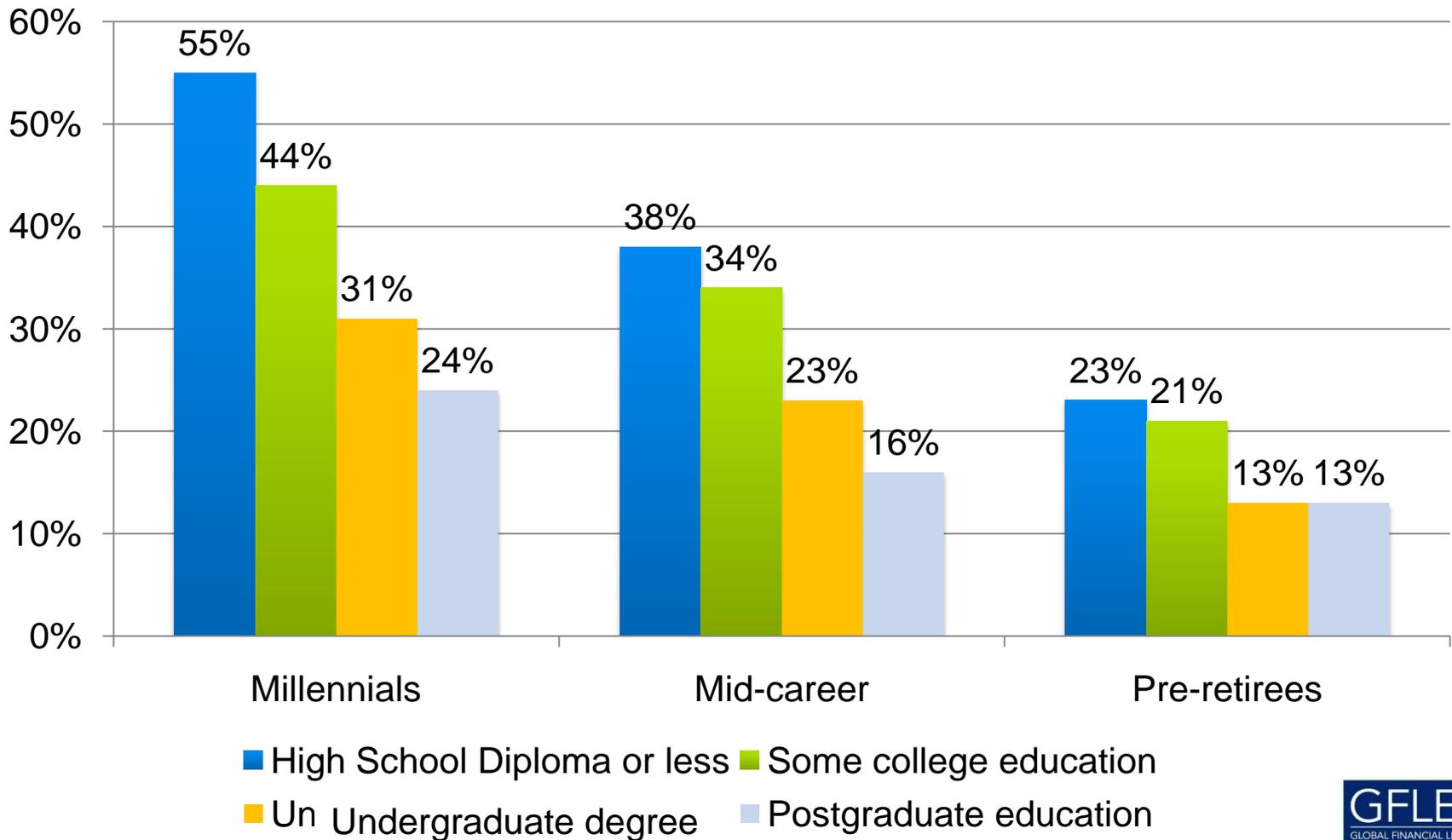
Many Americans use high-cost borrowing—**29%** have used one of these methods in the past 5 years

- ❖ Pay-day loans (14%)
- ❖ Pawn shops (16%)
- ❖ Refund anticipation loans (8%)
- ❖ Auto title loans (10%)
- ❖ Rent-to-own stores (10%)



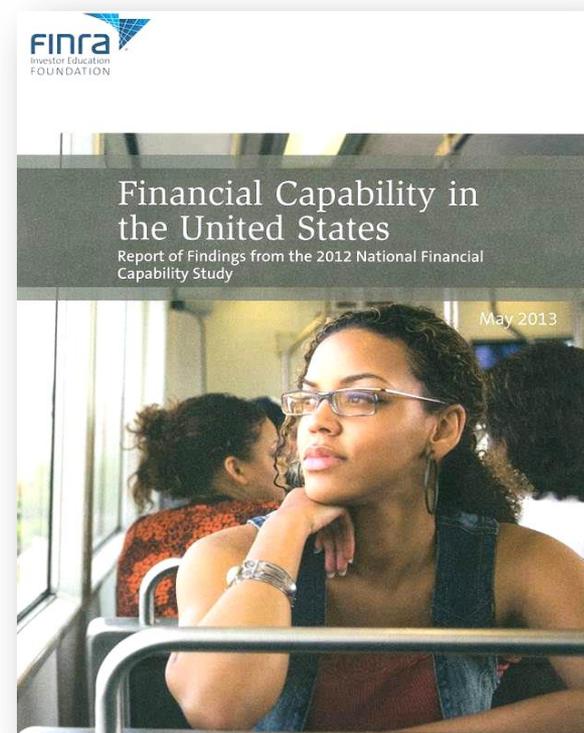
58% of users among the unbanked

AFS use by career stage and by education



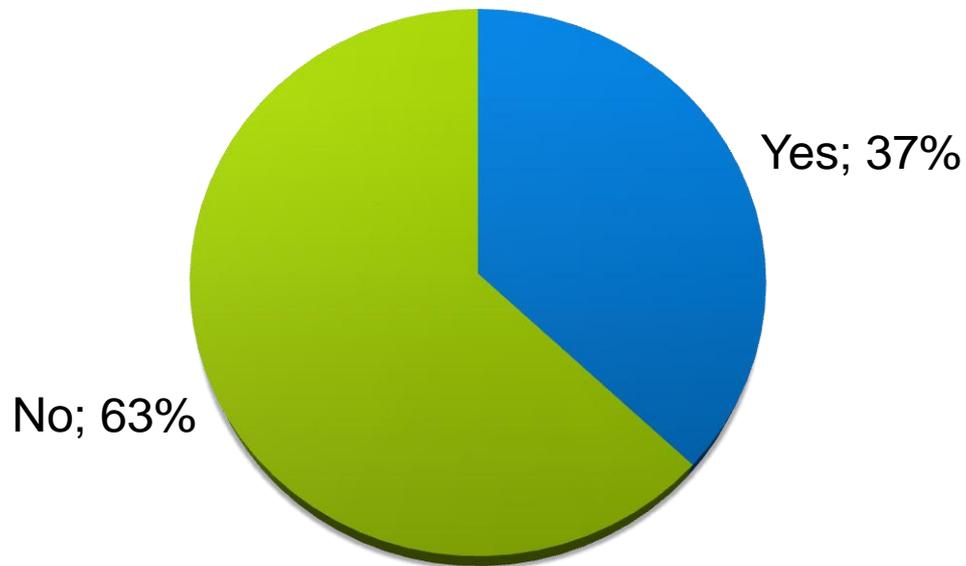
Third component of financial capability

- ✓ Making ends meet
 - ✓ Managing financial products
- ## 3. Planning ahead

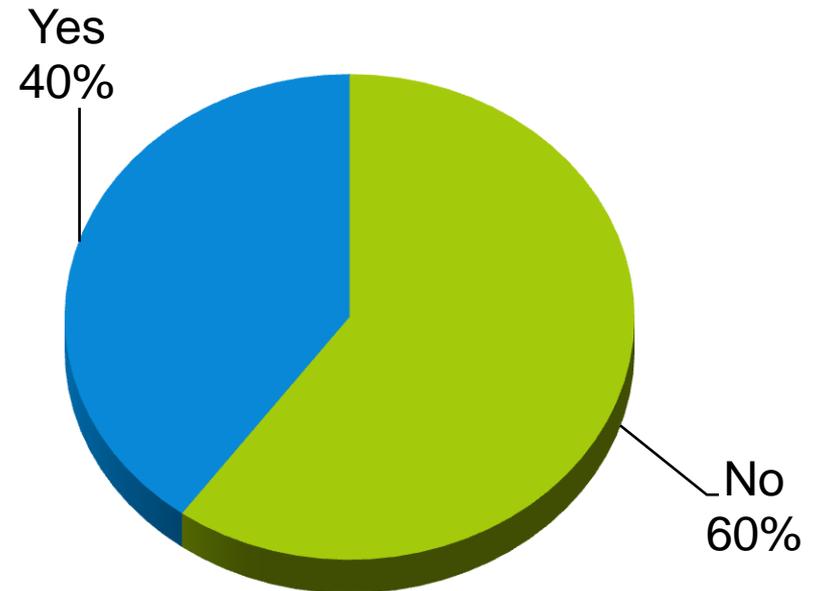


Many Americans don't plan ahead

Have you ever tried to figure out how much you need to save for retirement?

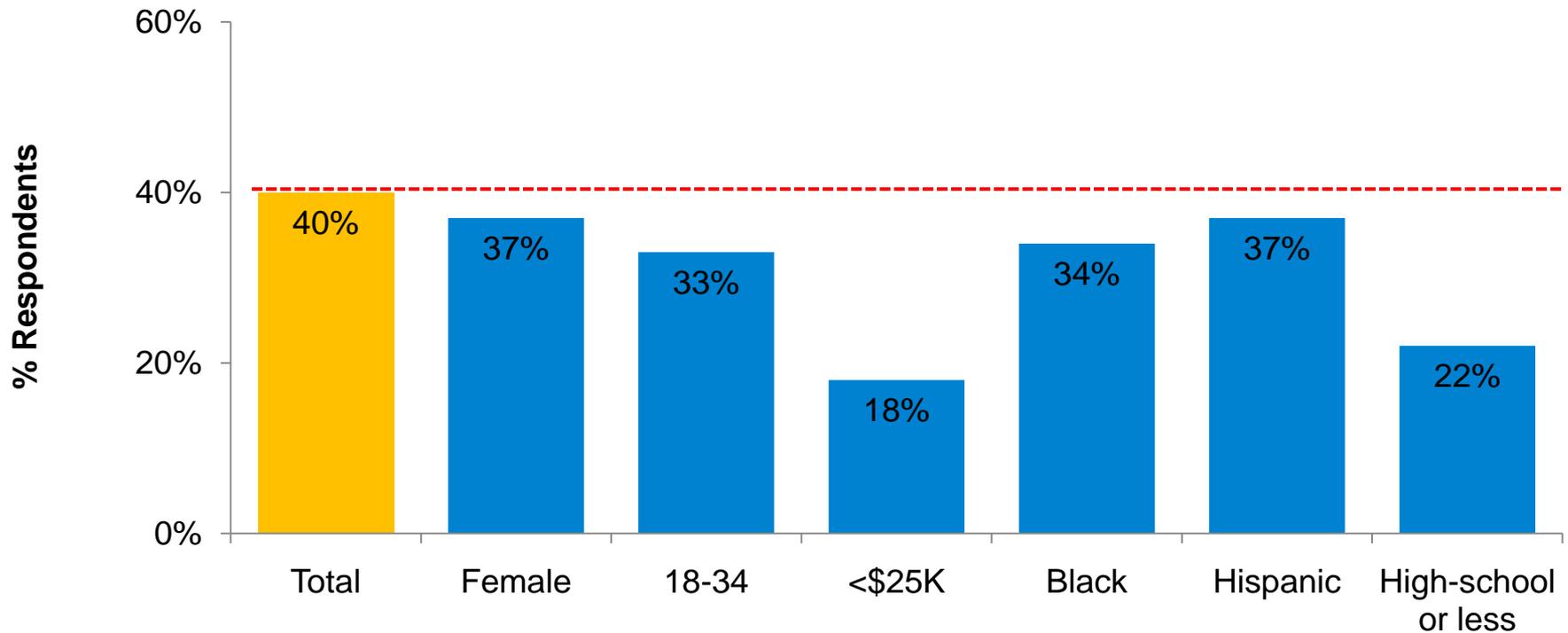


Have you set aside an emergency or rainy day fund?



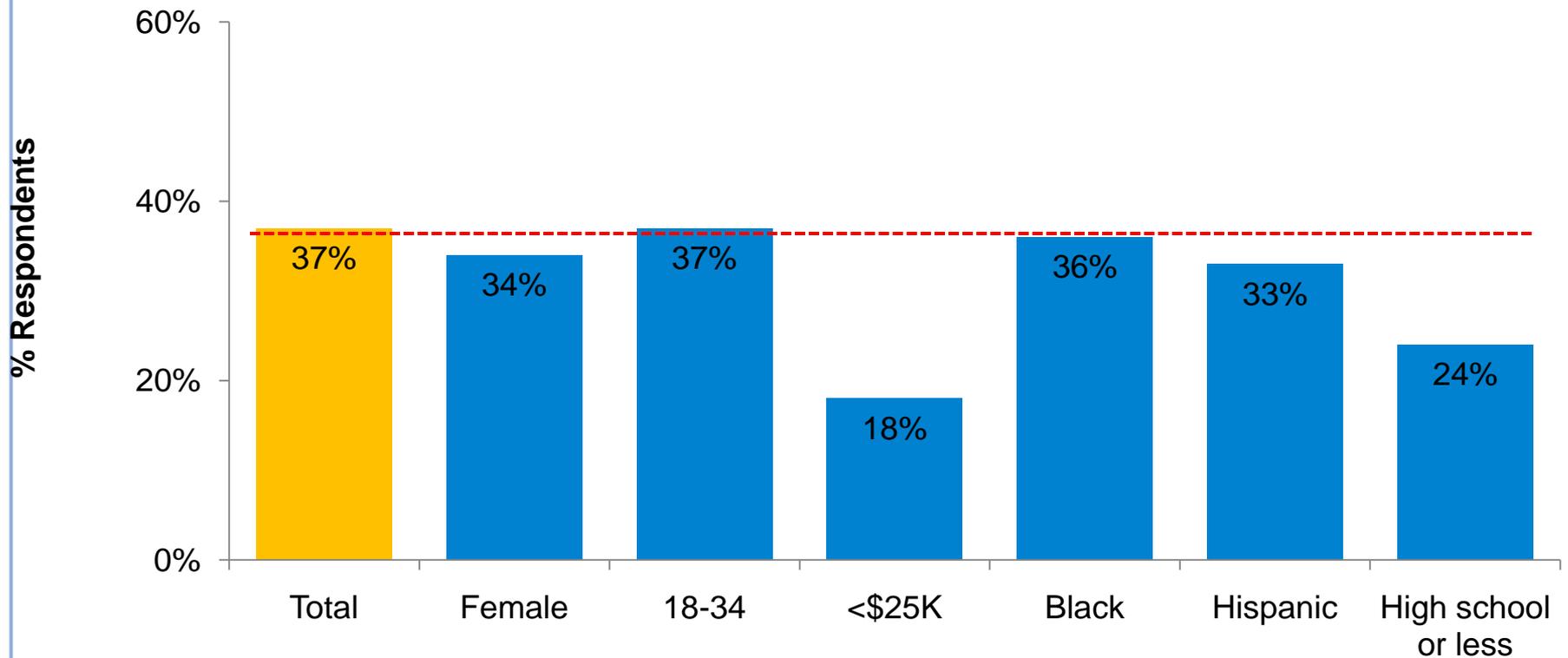
Those most at risk are least prepared for emergencies...

Respondents with emergency or rainy day funds that would cover expenses for 3 months



...And least likely to plan for retirement

Respondents who have tried to figure out how much to save for retirement



Evidence of financial fragility

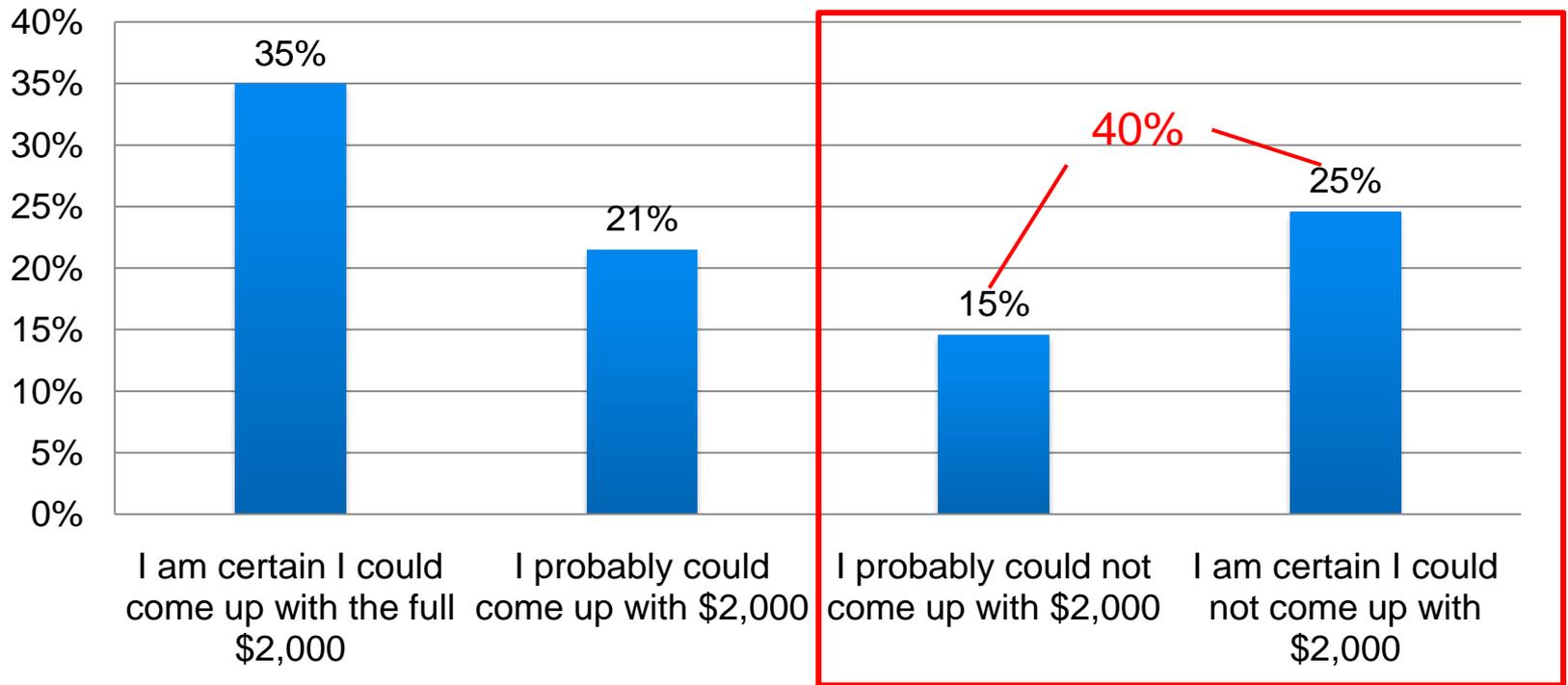
Can people cope with unexpected expenses?

Use a measure of financial fragility developed by Lusardi, Schneider and Tufano (2011):

- How confident are you that you could come up with \$2,000 if an unexpected need arose within the next month?
 - I am certain I could come up with the full \$2,000
 - I could probably come up with \$2,000
 - I could probably not come up with \$2,000
 - I am certain I could not come up with \$2,000
 - Don't know / Prefer not to say

- **The measure captures respondents' ability to cope with mid-size, unexpected income shocks**

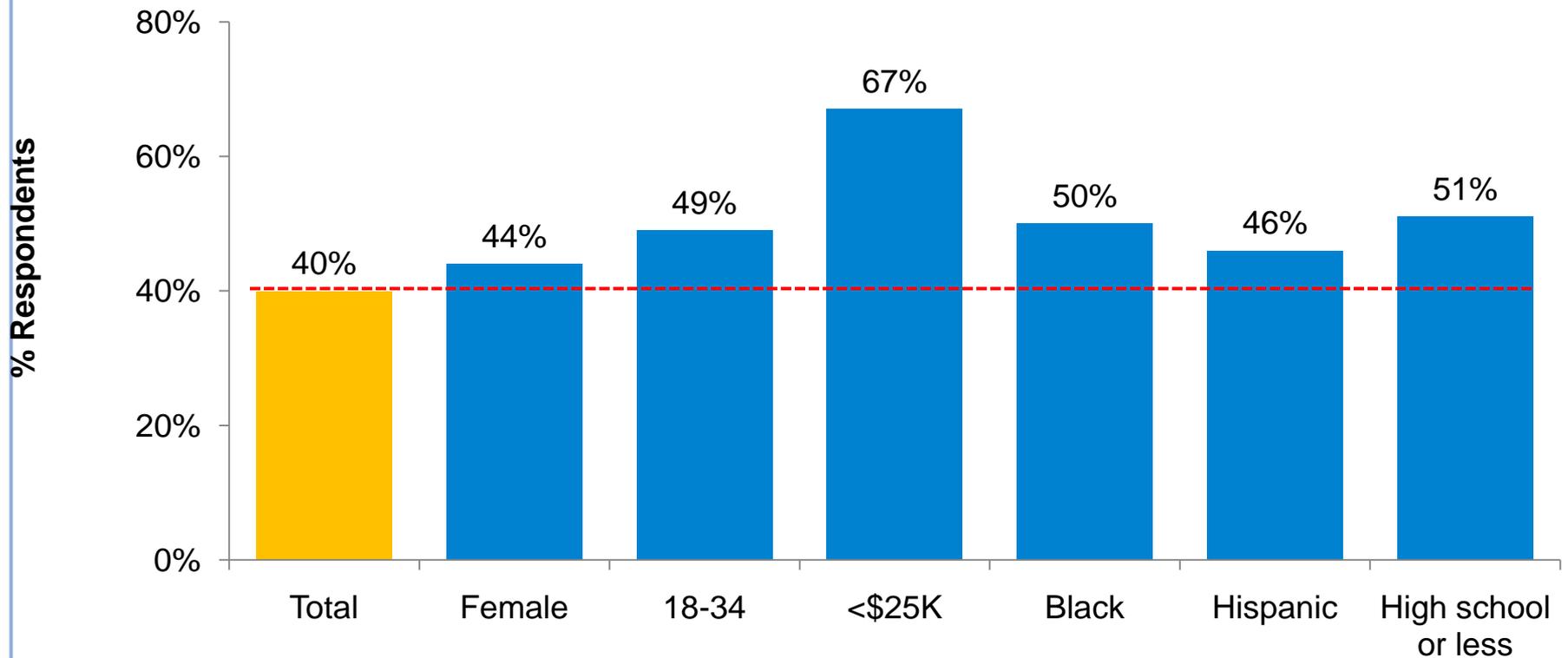
How confident are you that you could come up with \$2,000 if an unexpected need arose within the next month?



Note: The figure reports answers to the question “How confident are you that you could come up with \$2,000 if an unexpected need arose within the next month?” Percentages do not total 100 percent because “do not know” and “prefer not to say” answers are not reported in the figure.

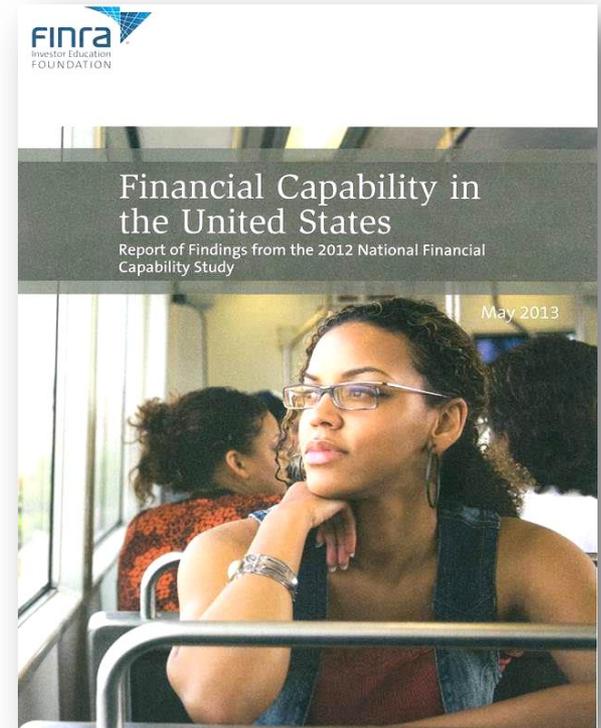
Financial fragility by demographic

Respondents who either certainly or probably cannot come up with \$2,000



Fourth component of financial capability

- ✓ Making ends meet
 - ✓ Planning ahead
 - ✓ Managing financial products
4. Financial knowledge and decision-making



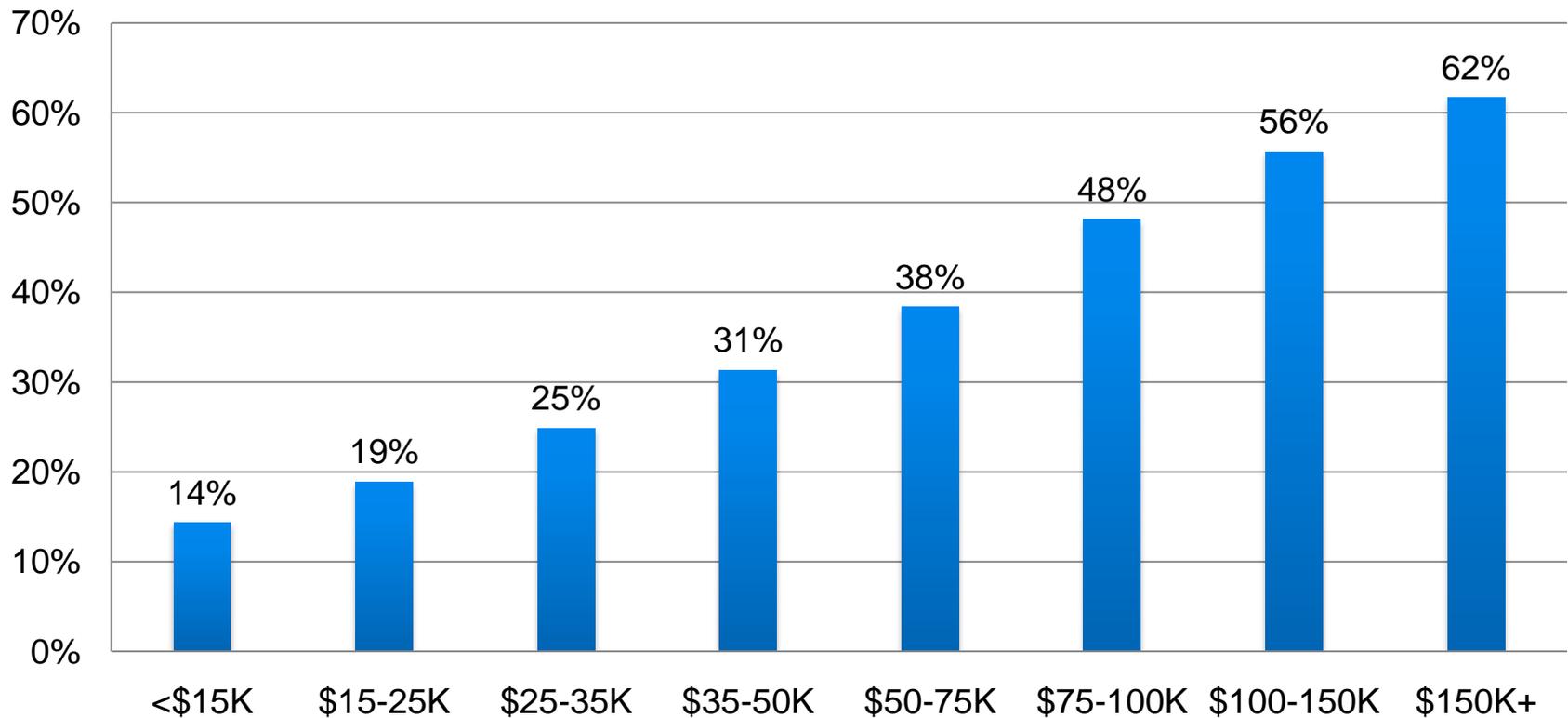
Financial literacy

Answers to five financial literacy questions

	<i>% Correct</i>	<i>% Don't Know</i>
Numeracy question	75%	11%
Inflation question	61%	20%
Risk diversification question	48%	42%
Mortgage question	75%	15%
Bond prices question	28%	37%
Answered the first three questions correctly	34%	-
Answered all five questions correctly	14%	-

Financial literacy across income groups

**Financial literacy by income level in the United States
(3 questions answered correctly)**



Gender differences in financial literacy

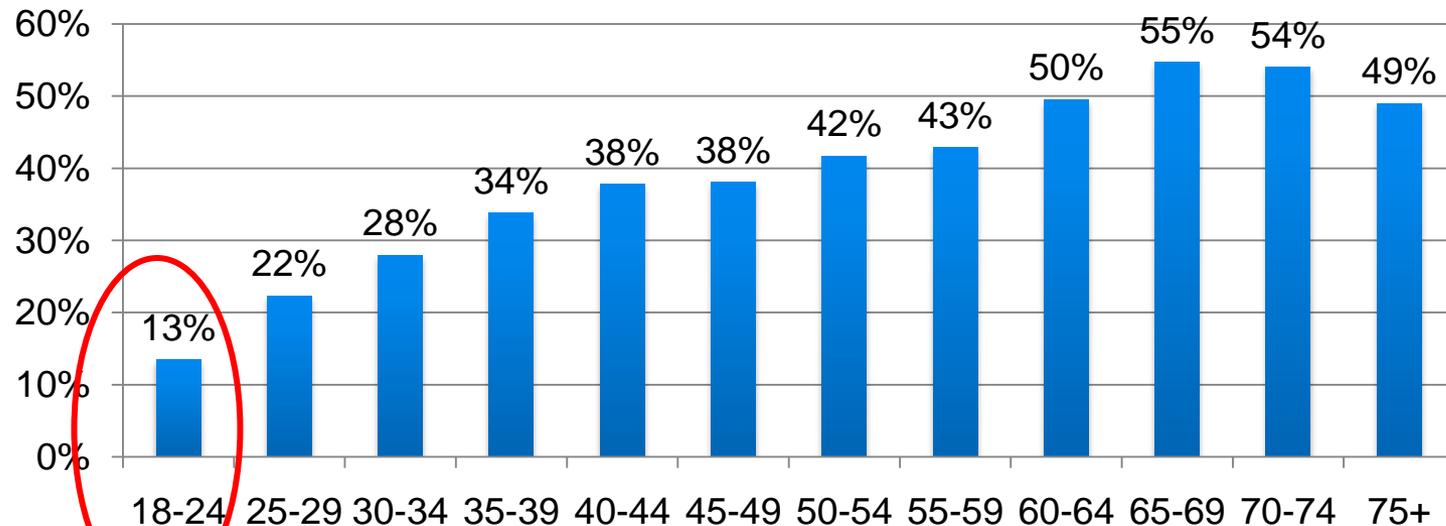
Women and financial literacy

- **Large gender differences in financial literacy**
 - Similar pattern across 13 countries
- **Women answer in the same way**
 - They frequently state they “do not know” the answer
- **Women report lower levels of self-assessed knowledge**
 - A group to target



Financial knowledge among the young

**Financial knowledge by age in the United States
(% answering 3 questions correctly)**



- Compared to other age groups, financial knowledge among the young is very low

From research to applications

Ideal venues for financial education and most scalable

➤ Schools

- Easier to reach the young
- Need to prepare new generations
- Have a basis on which to build



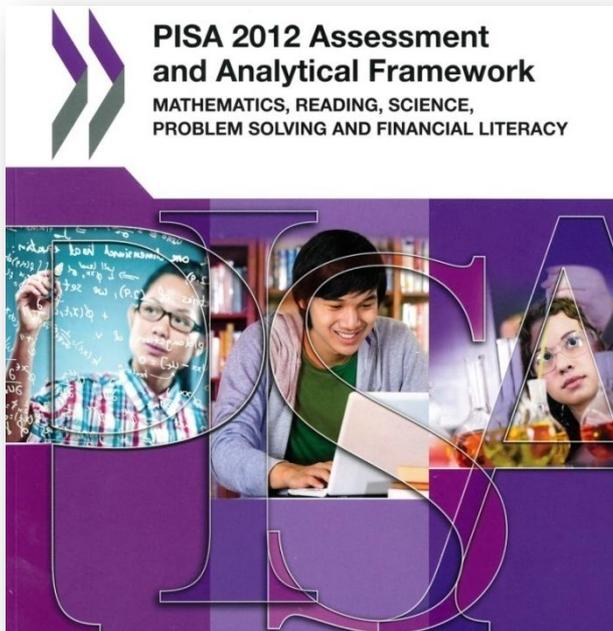
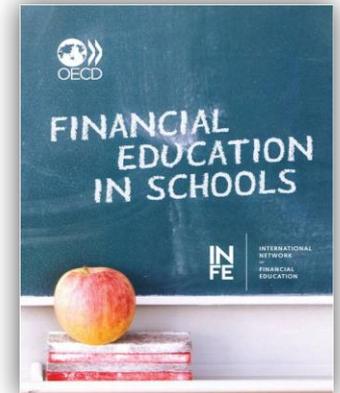
➤ The workplace

- Easier to reach the adults
- Many teachable moments
- Part of benefits and training



OECD's Programme for International Student Assessment (PISA). Financial literacy added in 2012

**Are students well prepared for future challenges?
Can they analyze, reason and communicate effectively?
Do they have the capacity to continue learning throughout life?**



Every three years the OECD Programme for International Student Assessment (PISA) answers these questions and more. It assesses to what extent students near the end of compulsory education have acquired some of the knowledge and skills essential for *full participation in society*.

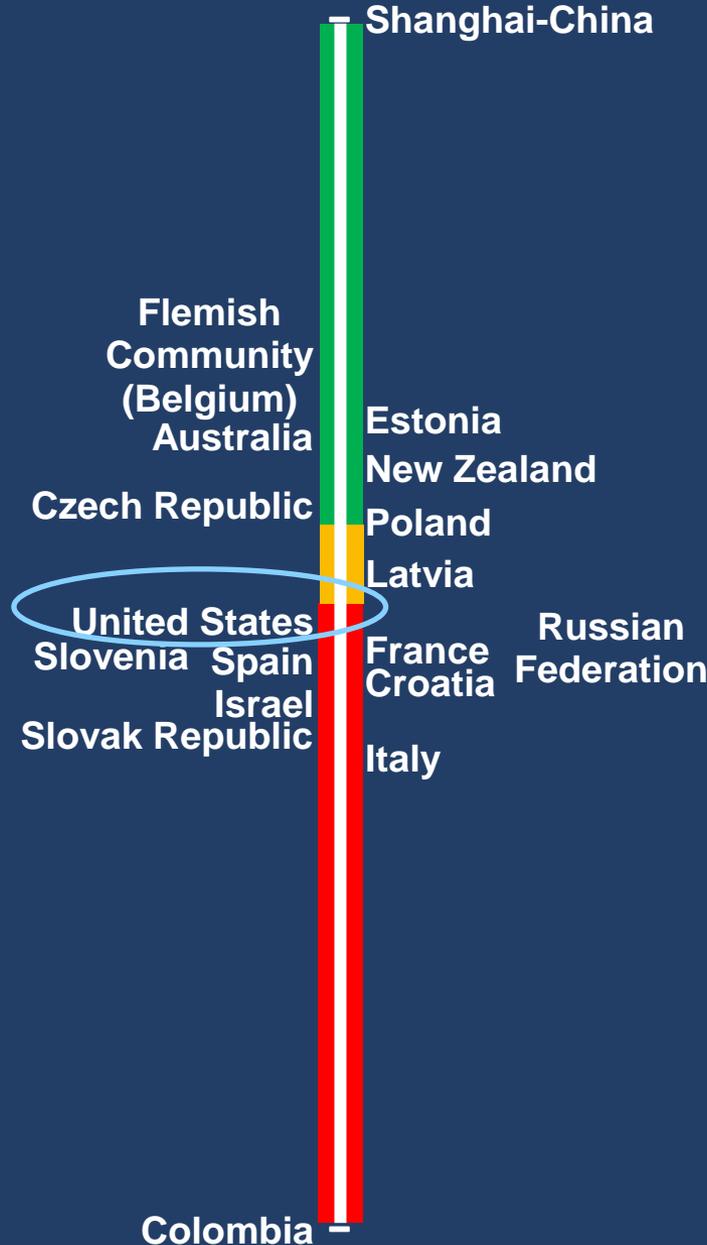
Mean score

605
595
585
575
565
555
545
535
525
515
505
495
485
475
465
455
445
435
425
415
405
395
385
375

Strong performance in financial literacy

Low performance in financial literacy

Average performance of 15-year-olds in financial literacy





 **NYSE**

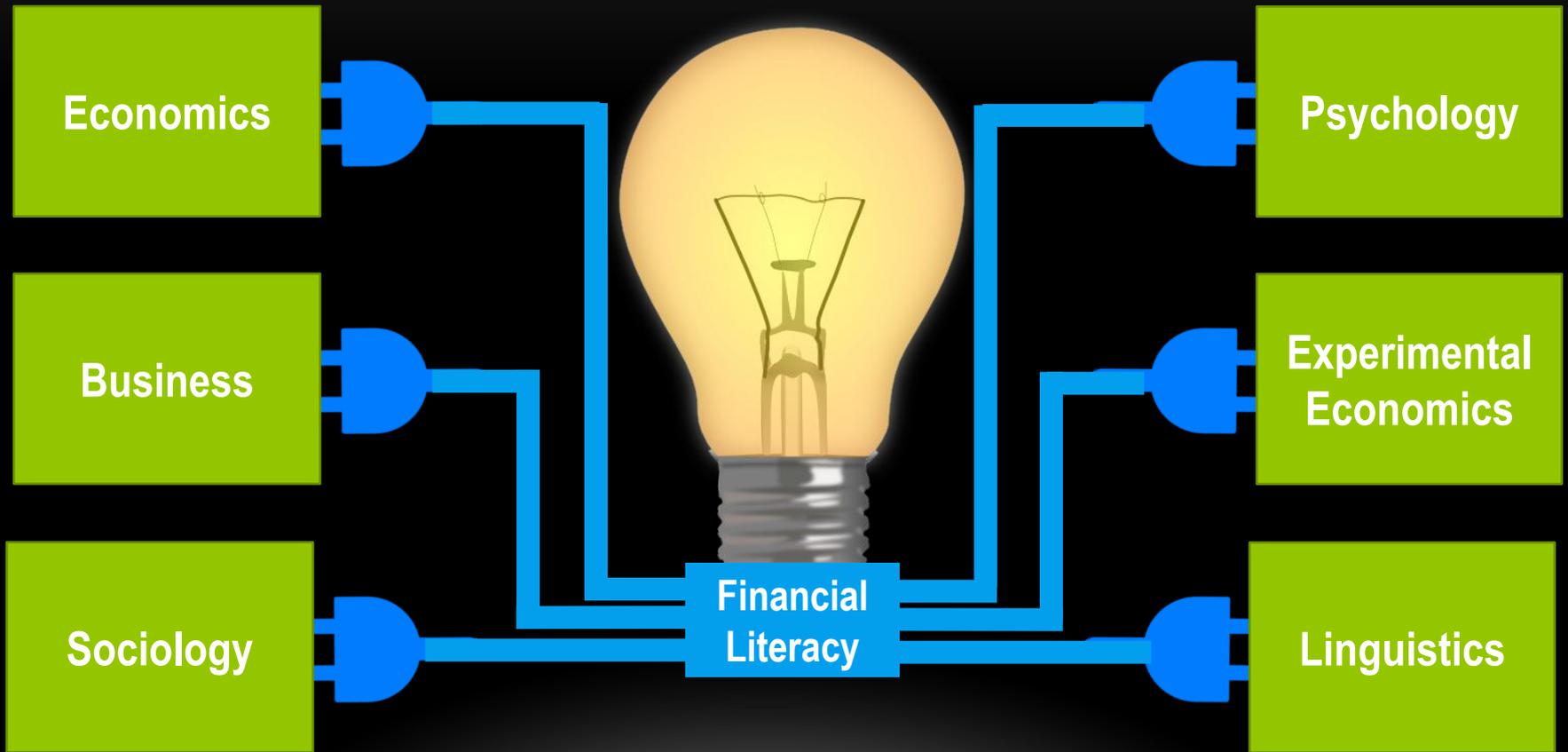


NYSE Workplace Financial Fitness Toolkit

A program for any company

- **Ten steps divided into 3 stages**
Basic, Intermediate, and Advanced
- **Customize the program for employees**
One size does not fit all
- **The Employee Checklist**
Ten guidelines with implementation tips to improve employees' financial fitness

Our approach is multidisciplinary



New initiative: FinLab

➤ **FinLab**

- An innovation lab
- Focus on experimentation
- Focus on financial education programs



➤ **Technology + financial literacy**

- They are complements not substitutes



Summary

The survey provides evidence that:

1. Many Americans are overly indebted and financially fragile
2. Many incur in behaviors that generate fees, interest payments, and other costs
3. The majority of Americans do not plan ahead for life-cycle events and do not insure against unexpected ones
4. Americans are not well equipped to make financial decisions
5. The groups displaying lower financial capability are the young, those with low income, those with low education, and minorities

Thank you

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