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LOOKING FORWARD – RESEARCHER VIEWS

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The growing importance of financial literacy

A new economic landscape

Major changes in many markets and institutions

- **Changes in pensions**
  - More individual and private accounts

- **Changes in labor markets**
  - Divergence in wages – skills are critical

- **Changes in financial markets**
  - Greater complexity
  - More opportunities to borrow & in large amounts
Increase in life expectancy changes everything

- Life expectancy is high, and has kept growing.
- Young people today will need to be able to support themselves for many years.

Source: OECD Factbook 2013: Economic, Environmental and Social Statistics - © OECD 2012
Many questions

Given these changes:

1. How well-equipped are people to deal with this new economic environment?
2. Are there vulnerable groups?
3. Does financial literacy matter?
4. What can be done to promote financial well-being?
A large amount of research on these topics

We can answer some of these questions

1. New data, thanks in particular to OECD-INFE
2. New initiatives and field work
3. Many researchers contributing to the emerging field of financial literacy/personal finance
4. A lot of new findings that are important for policy
OECD-INFE Research Committee

New committee

1. Members are from many countries and bring many different competencies
2. Provide most up-to-date relevant research
3. Provide information and expertise
4. Help looking forward
Topics I will cover in my presentations

Data – Research – Lessons learned

1. Data: PISA
2. Research: Examples of field work
3. Some lessons we have learned so far
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.
This is the first large-scale international study to assess the financial literacy of 15-year-old students.

Financial literacy assessment framework

The framework was the first step in constructing a financial literacy assessment of international scope by providing an articulated plan for developing items, designing the instrument and providing a common language for discussion of financial literacy.
A group of experts was put together by the OECD to design the 2012 module on financial literacy.

They represented many countries and many stakeholders (Treasury departments, central banks, regulators, practitioners, academics).

Experts worked on the assessment for about two years.
“Financial literacy is **knowledge and understanding** of financial concepts and risks, and the **skills, motivation and confidence** to apply such knowledge and understanding in order to make **effective decisions** across a range of financial contexts, **to improve the financial well-being of individuals and society**, and to enable **participation in economic life.**”
18 countries-participated in the 2012 Financial Literacy Assessment (13 are OECD countries).

Australia, Belgium (Flemish Community), Shanghai-China, Colombia, Croatia, Czech Republic, Estonia, France, Israel, Italy, Latvia, New Zealand, Poland, Russia, Slovak Republic, Slovenia, Spain, and the United States.

Data was released on July 9, 2014.
Mean score

Strong performance in financial literacy

Shanghai-China

Flemish Community (Belgium)

Australia

Estonia

New Zealand

Czech Republic

United States

Slovenia

Spain

Croatia

Israel

Slovak Republic

Latvia

Poland

France

Italy

Russian Federation

Low performance in financial literacy

Colombia

Average performance of 15-year-olds in financial literacy
Differences only partially explained by GDP per capita

\[ R^2 = 0.1632 \]

GDP per capita explains only 16% of the country level variation in financial literacy.
Distribution of student performance

<table>
<thead>
<tr>
<th>Financial literacy performance levels</th>
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<tbody>
<tr>
<td>625 and above</td>
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<tr>
<td>550 to &lt;625</td>
</tr>
<tr>
<td>475 to &lt;550</td>
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<tr>
<td>400 to &lt;475</td>
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<tr>
<td>Less than 400 points</td>
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</tbody>
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- **Baseline**
  - L1 15%
  - L2 23%
  - L3 30%
  - L4 22%
  - L5 10%

- **Top performers**
  - OECD average-13
Financial Literacy and Financial Inclusion
Relevance of bank account holding (accounting for socio-demographics)

On average across OECD countries and economies, students who hold a bank account score 21 points higher than students with similar socio-economic status who do not.
There is a lot to learn

- There is so much we can learn from PISA
- A lot of research can be done both within and across countries
- A rich set of information about schools, teachers, parents, etc.
- It is possible to compare data not just across countries but also over time. Data will be collected in 2015, and 2018 is in the planning stage.

Very rich data
New data on financial literacy around the world
The Global Financial Literacy Survey

In 2014, Gallup interviewed 1,000 people per country in more than 140 countries around the world about their level of financial literacy.

The survey covers 4 topics: Numeracy, interest compounding, inflation, and risk.

The data will be released in November 2015.
1 in 3 adults worldwide answered 3 out of 4 topics correctly
Globally, risk is the concept people know the least
Combining data from PISA (math) and Gallup Survey

- Positive relationship between knowledge of the young and the general population
- The young are doing well in some countries
Financial Literacy and Financial Inclusion

Potential to link data at the individual level with other datasets

Well-being measures (Gallup World Poll)

Food security measures (Voices of the Hungry)

Financial inclusion measures (Global Findex)

banked
unbanked
formal credit
no formal credit
formal savings
no formal savings

Financial literacy

Source: GFLS & Global Findex database
Several findings

Findings hold true across countries

- Financial illiteracy is widespread in the population
- Some groups are particularly vulnerable, in particular the young
- Risk diversification is most difficult concept to grasp
- There is a link between financial literacy and financial inclusion
Improving financial literacy among the young

Evidence from adding financial literacy in high school curricula

- Brown, Collins, Schmeiser, and Urban (2014). *State Mandated Financial Education and the Credit Behavior of Young Adults*
  - When exposed to rigorous programs and trained teachers, students do well and are less likely to have problems with debt

- Bruhn, de Souza Leao, Legovini, Marchetti, and Zia (2013). *The Impact of High School Financial Education: Experimental Evidence from Brazil*
  - Financial education had an impact on both students and parents
Field work: Five steps to planning success

Building a more robust pension system starting with the young

- Focused on young workers
  - They are the ones with low financial literacy

- Covered concepts, such as risk diversification
  - This is the concept people know the least

- Kept the message free of economic/finance jargon
  - Research shows it matters, in particular for women

- Teaching using videos and narratives
Short video about risk

Risk diversification = don’t put all your eggs in one basket

http://www.rand.org/labor/centers/financial-literacy.html
We measured whether it worked

- Tested interventions using a set of respondents to an Internet panel
- Baseline questions on risk diversification
- Randomly assigned
  - Intervention group
    - Video only, narrative only, video & narrative
  - Control group
    - No intervention
- Repeated the concept questions
Findings

- After being exposed to videos and narratives, the performance on financial literacy questions (general knowledge and hypothetical choices) improved.
- Video worked best.
- While young were targeted, the intervention affected all age groups.
When financial illiteracy is so widespread, it cannot be cured with very limited interventions

One size does not fit all, we need targeted programs

The young are an ideal group for financial education programs, in particular in school

We need more experimental work so to continue to improve
Conflicting evidence on the effectiveness of financial education?

Learning from meta-analyses

  - Interventions to improve financial literacy explain only 0.1% of the variance in financial behaviors

- What this paper shows is that the dosage we have used in financial education is wrong
  - Programs are very limited (an average of 10 hours)
  - Quality of material and teachers is rarely available
  - Financial knowledge, like every knowledge decays over time, which is good otherwise the data would be suspicious
Final thoughts

- **Financial literacy is like reading and writing**
  - As it was not possible in the past to participate in society without being able to read and write, so it is not possible to thrive in today’s society without being financially literate

- **Building human capital for the 21st century**
  - Everyone deals with finance and finance is sufficiently complex that we cannot leave it to the individual to learn by himself/herself
“Knowledge is in every country the surest basis of public happiness.”

George Washington, First President of the United States (1789–97)
“(Financial) knowledge is in every country the surest basis of public happiness.”

George Washington, First President of the United States (1789–97)
“If you think education is expensive, try ignorance”

Derek Bok, Former President of Harvard (1971-1991)
Contact and further information

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