



Three threats to retirement security in time of crisis

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The George Washington University School of Business and GFLEC
Italian Financial Education Committee

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Three threats

- 1 > **Financial illiteracy**
- 2 > **Financial fragility**
- 3 > **Lack of retirement planning**

Topic 1

A number:

1/3

To get started

1/3

- People who know the basics of personal finance
- This is true both in the US and around the world
- It is also related to knowledge about risk

Financial literacy: the ABC of personal finance

The Big Three

1. "Suppose you had \$100 in a savings account and the interest rate was 2% per year. After 5 years, how much do you think you would have in the account if you left the money to grow?"

- More than \$102**
- Exactly \$102**
- Less than \$102**
- Don't know**
- Refuse to answer**

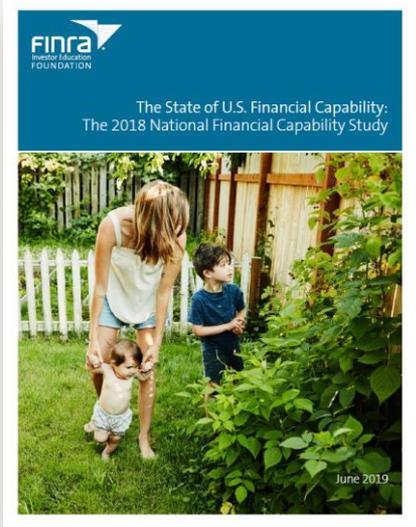
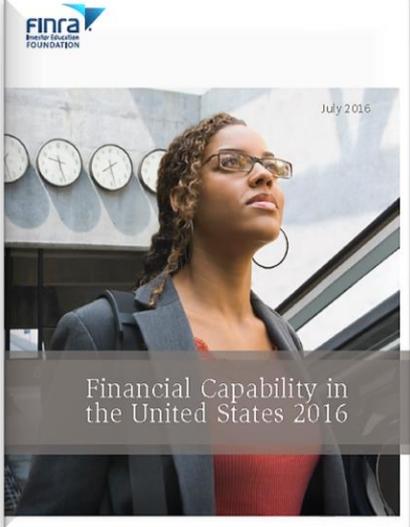
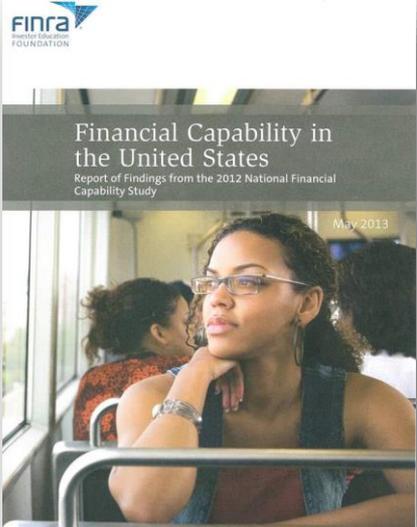
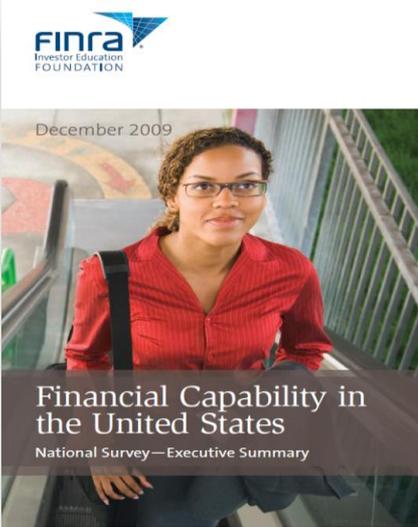
2. "Imagine that the interest rate on your savings account was 1% per year and inflation was 2% per year. After 1 year, with the money in this account, would you be able to buy..."

- More than today**
- Exactly the same as today**
- Less than today**
- Don't know**
- Refuse to answer**

3. "Do you think the following statement is true or false? *Buying a single company stock usually provides a safer return than a stock mutual fund.*"

- True**
- False**
- Don't know**
- Refuse to answer**

Collecting data: The US National Financial Capability Study (NFCS), from 2009 to 2018



Financial Literacy around the World (FLat World)

Evidence from 15 countries:

- ❖ USA
- ❖ The Netherlands
- ❖ Germany
- ❖ Italy
- ❖ Russia
- ❖ Sweden
- ❖ New Zealand
- ❖ Japan
- ❖ Australia
- ❖ France
- ❖ Switzerland
- ❖ Romania
- ❖ Chile
- ❖ Canada
- ❖ Finland



How much do Americans know?

Distribution of responses across the U.S. population
(2009 National Financial Capability Study)

	Responses			
	<i>Correct</i>	<i>Incorrect</i>	<i>DK</i>	<i>Refuse</i>
Interest rate	65%	21%	13%	1%
Inflation	64%	20%	14%	2%
Risk diversif.	52%	13%	34%	1%

NB: Only about 1/3 correctly answer all 3 questions. About 1/3 do not know about risk.

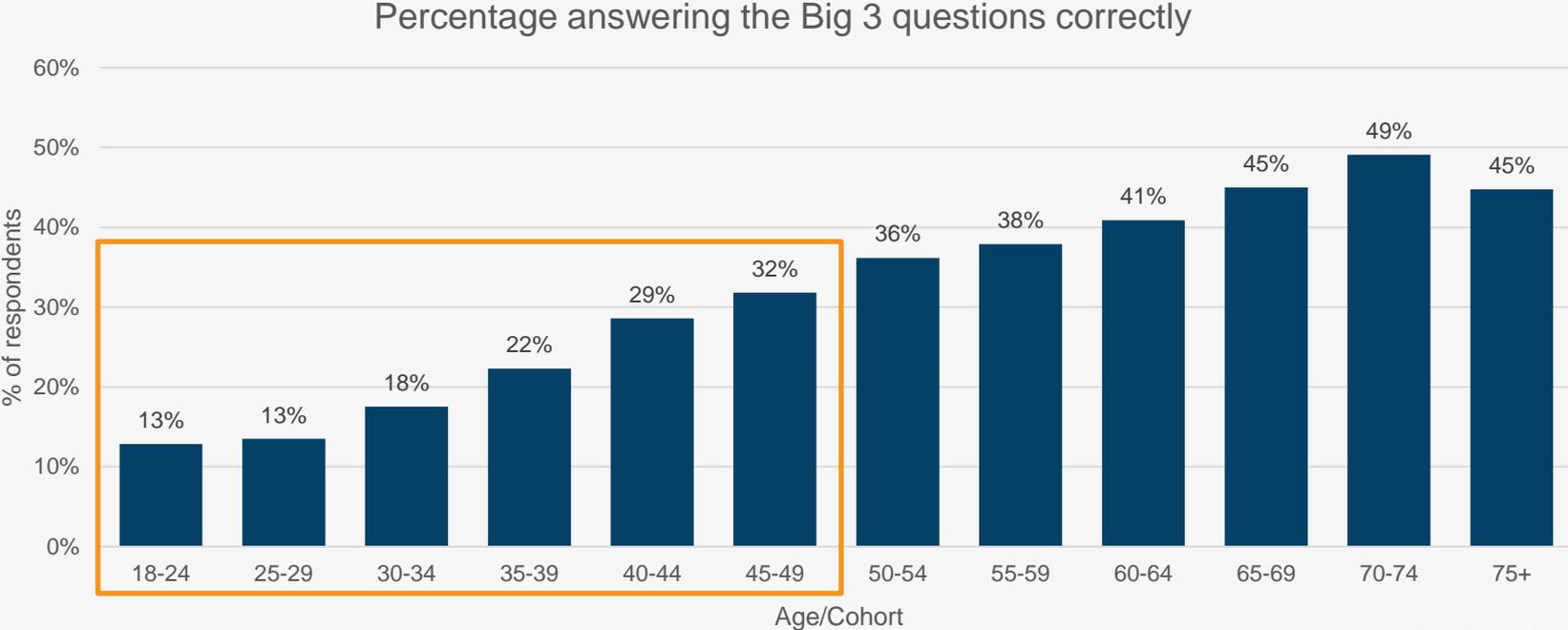
How much do Germans know?

Distribution of responses across the German population
(2009 SAVE)

	Responses		
	<i>Correct</i>	<i>Incorrect</i>	<i>DK</i>
Interest rate	82%	7%	11%
Inflation	78%	5%	17%
Risk diversif.	62%	6%	32%

NB: About half (53%) correctly answer all 3 questions; 72% got the first two questions right. **About 1/3** do not know about risk.

Financial literacy increases slowly with age/cohort (2018 NFCS)



Source: US 2018 NFCS

About 1/3 of Americans know these 3 basic concepts by age 50 even though many financial decisions are made well before that age

The S&P Global FinLit Survey

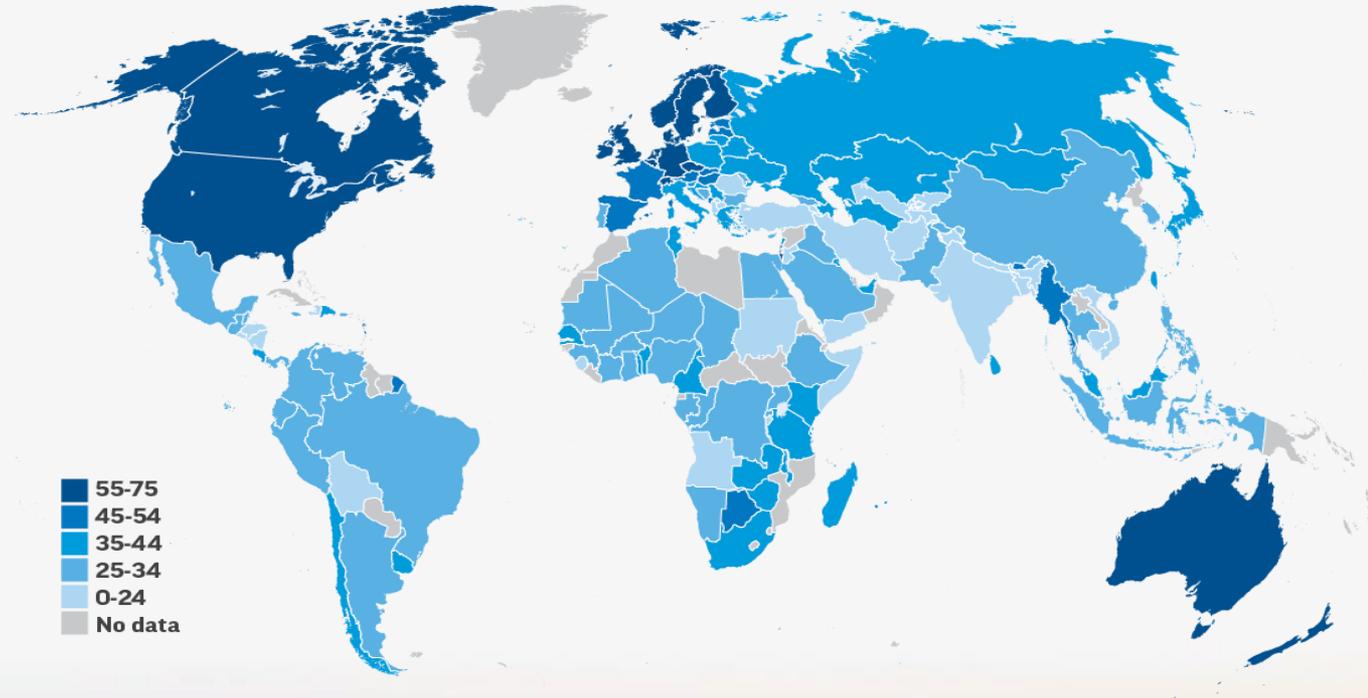
- The largest, most comprehensive, global measure of financial literacy
- Interviewed more than 150,000 adults age 15+ in more than 140 countries
- The measure has to be applicable to every country, irrespective of economic structure and financial market development
- The survey covers four topics:
 - Numeracy
 - Interest compounding
 - Inflation
 - Risk diversification



Being financially literate:
Able to answer 3 out of these 4 topics correctly

Financial Literacy Across the Globe

% of financially literate adults

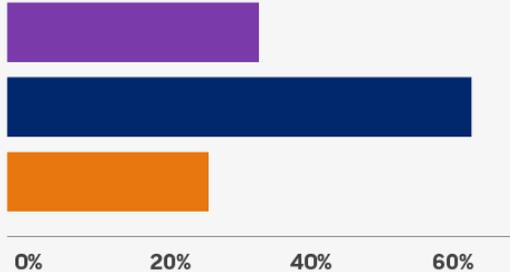


Only 1 in 3 adults worldwide responded correctly to three out of four topics

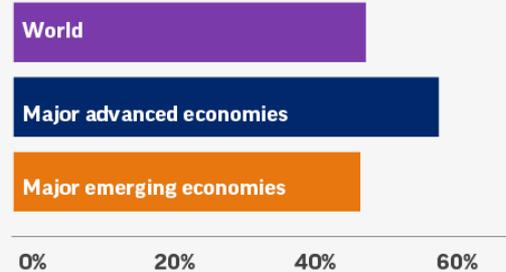
Financial literacy by topic

% of adults answering correctly

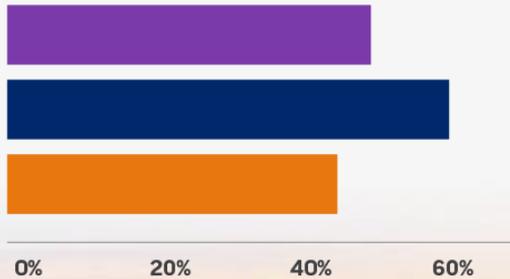
RISK DIVERSIFICATION



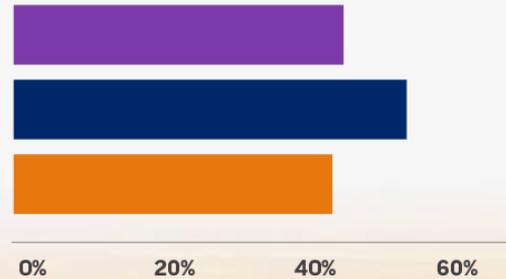
NUMERACY (INTEREST)



INFLATION



COMPOUND INTEREST



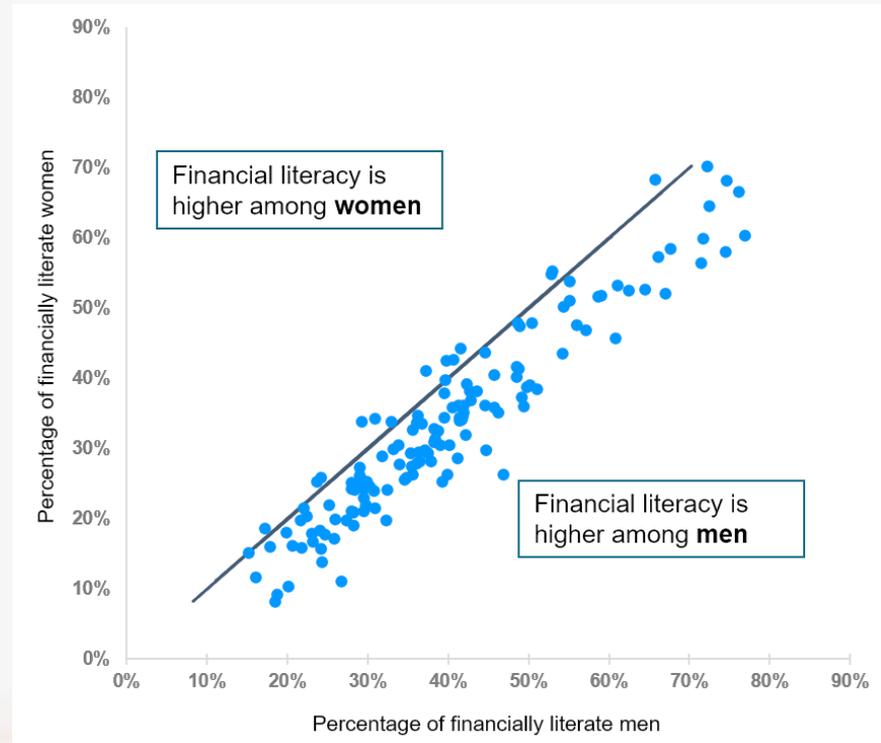
Inflation and simple interest/numeracy is what people know most across countries.

Risk diversification is what people know the least.

Source: S&P Global Finlit

Gender gap in financial literacy around the world

In most economies around the world, men have a better understanding of basic financial concepts than women



Source: Global FinLit Survey

Topic 2

Financial fragility: Can people handle shocks?

Financial fragility

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.

From Lusardi and Tufano, BPEA, 2011

Measure of financial fragility

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.



People with these responses are classified as financially fragile

From Lusardi and Tufano, BPEA, 2011

Financial fragility: What this measure does

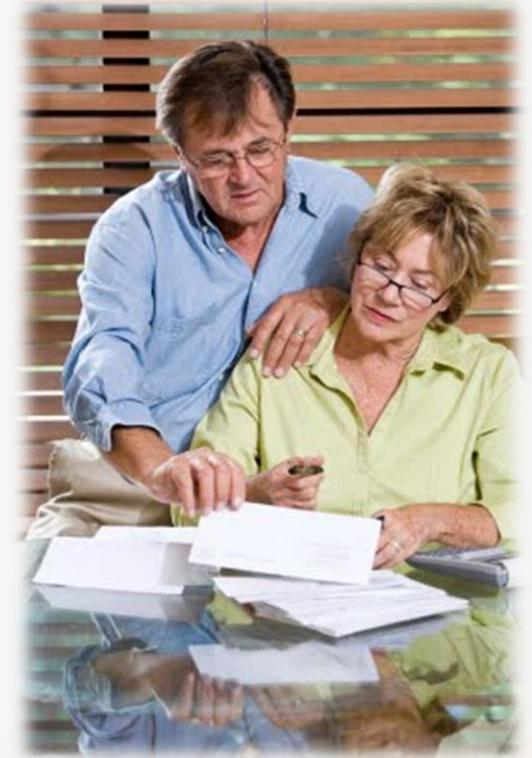
**Is a symptom
of lack of
assets**

**Indicates lack
of borrowing
capacity of highly
leveraged
households**



Financial Fragility in the United States – 2018 NFCS

	Fragility
	<i>Probably or certainly could not come up with \$2,000 in a month</i>
US Adults	31%



Many Americans are financially fragile (2018 NFCS data)

Millennials (age 18-35)

- 35% of Millennials are financially fragile



Women

- 36% of American women are financially fragile vs. 25% of men

Financial Fragility in Europe

Policy Contribution
Issue n°15 | July 2020

The financial fragility of European households in the time of COVID-19

Maria Demertzis, Marta Domínguez-Jiménez
and Annamaria Lusardi

Executive summary

MARIA DEMERTZIS (maria.demertzis@bruegel.org) is Deputy Director of Bruegel

MARTA DOMÍNGUEZ-JIMÉNEZ (marta.dominguez@bruegel.org) is a Research Assistant at Bruegel

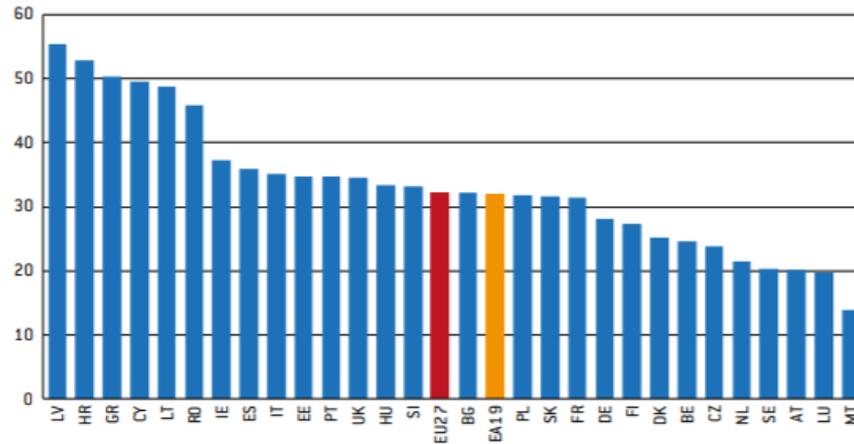
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- **THE CONCEPT OF** household financial fragility emerged in the United States after the 2007-2008 financial crisis. It grew out of the need to understand whether households' lack of capacity to face shocks could itself become a source of financial instability, in addition to risks to the stability of banks and the greater financial system. The concept goes beyond assessing the level of assets and encompasses the state of household balance sheets, including indebtedness. It relies also on individual perceptions of the ability to rely on families and friends and other methods to deal with shocks, though such aspects are less easy to measure and rely frequently on self-assessments.
- **IN THE WAKE OF** COVID-19, we ask how well-prepared households were in the European Union (including the United Kingdom) to handle an unexpected expense. Two years before the pandemic hit, a substantial share of EU households reported that they would be unable to handle unexpected expenses. In some EU countries, many households had savings equivalent to just a few weeks of basic consumption.
- **WE FIND THAT** one in three EU households is unable to meet an unexpected shock during regular times, let alone during a pandemic. COVID-19-related support measures put in place across the EU are intended to provide economic help to those households where members have lost jobs or face a severe reduction in income. However, in a number of countries where one in two households was already fragile - typically countries that are already economically weaker - state help is likely to be smaller and shorter-lived. Policies that increase financial resilience in structural ways will become necessary in the future.

Financial Fragility in Europe

In Figure 1, we plot the share of households that self-reports being unable to deal with an unexpected required expense. The data refers to 2018, a period of growth (albeit moderate) among European countries but, importantly for this exercise, not a period of specific financial stress.

Figure 1: Household inability to meet an unexpected required expense, all households, percentage shares, 2018



Source: Eurostat, EU-SILC. Notes: EU27 displays the average of all EU member states after January 2020 [those exhibited except the UK]. EA19 is the euro-area average.

Topic 3

Retirement planning: are people preparing for the future?

Retirement planning

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

- Yes
- No
- Don't know
- Prefer not to say

Retirement planning (cont.)

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

- Yes
- No
- Don't know
- Prefer not to say



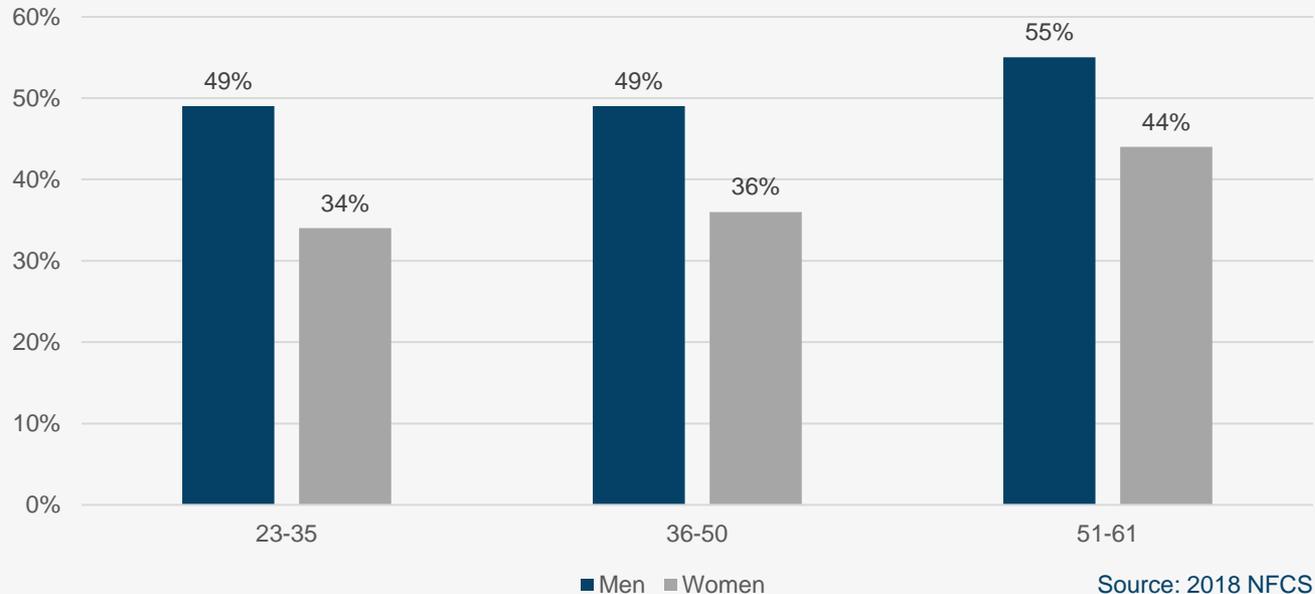
People with this response are classified as planners

Retirement Planning in the United States (2018 NFCS)

	Retirement Planning
	<i>Has tried to figure out how much they need to save for retirement</i>
US Adults	41%



Retirement planning by age and gender (2018 NFCS data)



- Retirement planning slightly increases over the life-cycle
- Women are less likely to plan than men

The link with financial literacy



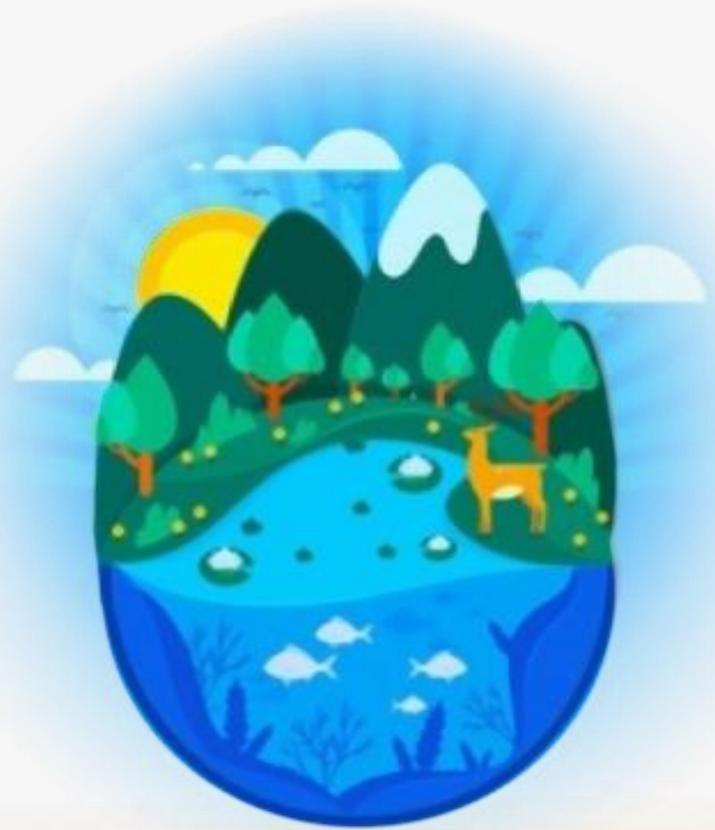
Who is able to answer the “Big 3” questions:

- is less likely to be financially fragile
- more likely to plan for retirement

Building an ecosystem

We need many components

- Financial literacy is an essential one
- It is the foundation (like water)
- We need to refocus after the crisis





A way forward: Using evidence to build programs and advise policy

Building the pump to spread the water (finlit)

This research has inspired our current work: Add financial literacy to any programs

- Financial literacy levels are low
 - Need to improve knowledge of the ABCs of personal finance
- People do not plan for the future
 - Financial education programs that help people make financial decisions
- The young are an important target and can use time in their favor
 - Start in school and also programs in the workplace, in particular for Millennials
- Programs targeted to women

Given widespread financial illiteracy

Need for large and scalable programs

- Financial education in school
- Financial wellness programs in the workplace
- Financial education in the community (libraries, museums, theaters, other places where people go to learn)

Personal finance course at the George Washington University

- Personal Finance courses for undergraduate and graduate students
- Extensive coverage of risk and risk management
- Paying attention to gender differences in financial literacy
- Paying attention to behavioral biases
- Material available for free on our website



Financial education in the workplace

Set-up:

- Design of a low-cost, easily-replicable financial education program called «Five Steps to Planning Success»
- Covering five basic financial planning concepts that relate to retirement
- Delivery models: written narratives and online videos
- Evaluation: control and treated groups using online survey (Rand ALP)

Program:

- Targeted to young workers
- Covered concepts that people know the least, for example risk, in a simple story



Short video about risk: don't put all your eggs in one basket



Assessed effectiveness of different methods of teaching using
Rand American Life Panel (ALP)

Advice for public policy : Toward a new ecosystem

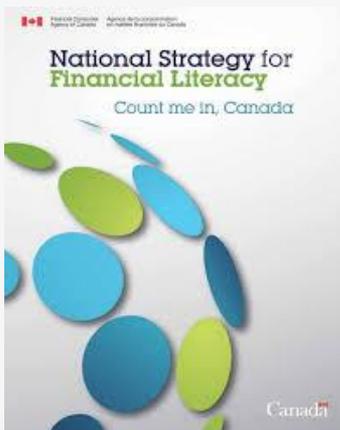
Building a financial resilient society

- Policy makers should focus on well-being
- Add financial literacy among indicators of well-being
- Toward a more inclusive society



Policy work: National strategies for financial literacy

About 70 countries have done or are doing a national strategy for financial literacy



Policy work: Italy



*Annamaria Lusardi Appointed
Director of Italy's New Financial
Education Committee*

This appointment supports GFLEC's vision of promoting the development of a financially literate world.

In July 2017, I was appointed by Italy's Minister of Economy and Finance as director of the new Financial Education Committee

The Committee is in charge of designing the national strategy and implementation program for financial literacy

Follow our work on www.Quellocheconta.gov.it

Public policy: A quote from the first President of the U.S

“Knowledge is in every country the surest basis of public happiness.”

President George Washington

Concluding remarks

Financial literacy is like **reading** and **writing: it is an essential skill to thrive in the 21st century**

- It is very important to be financially literate as early as possible
- Financial literacy is a stepping stone for retirement security and financial well-being

Looking ahead

Short definition of financial literacy: **A vision for the future**

The question is: **Which future do we want to build?**



Thank you!