



On the costs of financial illiteracy and how to take care of your personal finances

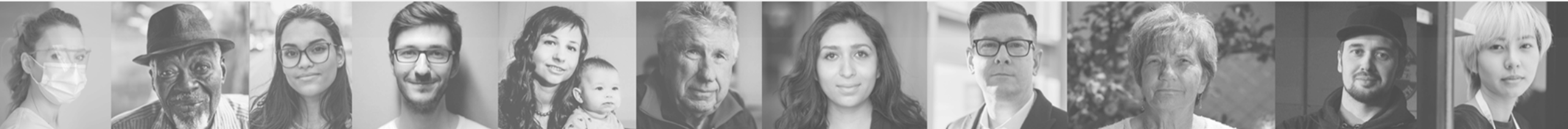
Annamaria Lusardi

The George Washington University, and Global Financial Literacy Excellence Center (GFLEC)
December 1st, 2021



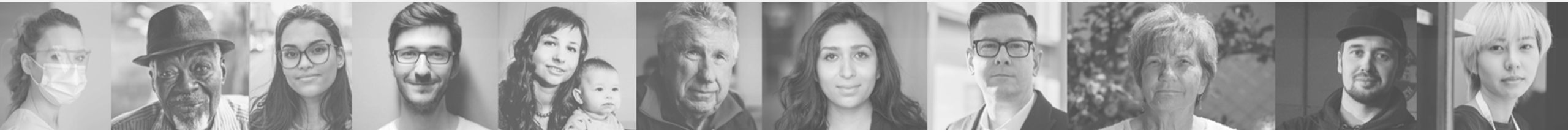
What we will discuss today

- Financial literacy research
- How research can guide policy and programs
- What we can learn for our personal finances



A number to get started

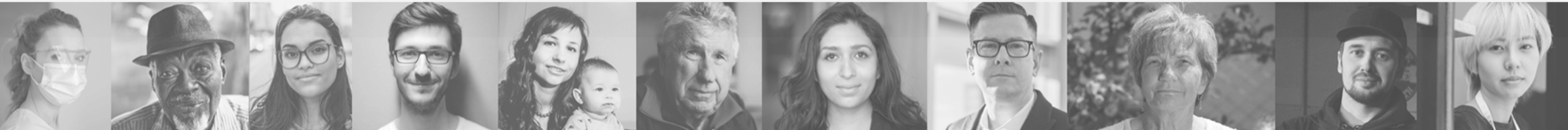
1/3



A number to get started

1/3

- Proportion of people in the US who know the ABCs of personal finance before age 50
- Proportion of people who are financially literate around the world
- Proportion of people who were financially fragile before the pandemic started



Financial literacy: The ABCs of personal financial

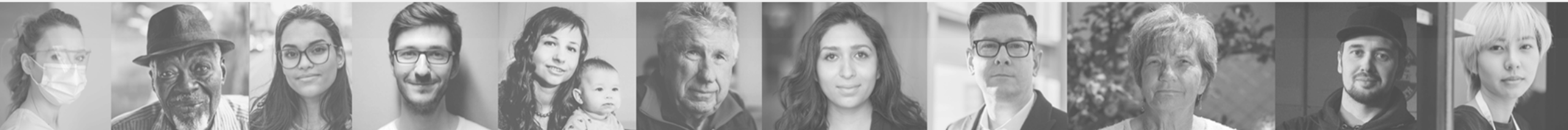
The Big 3

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?”
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...”
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.*”

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

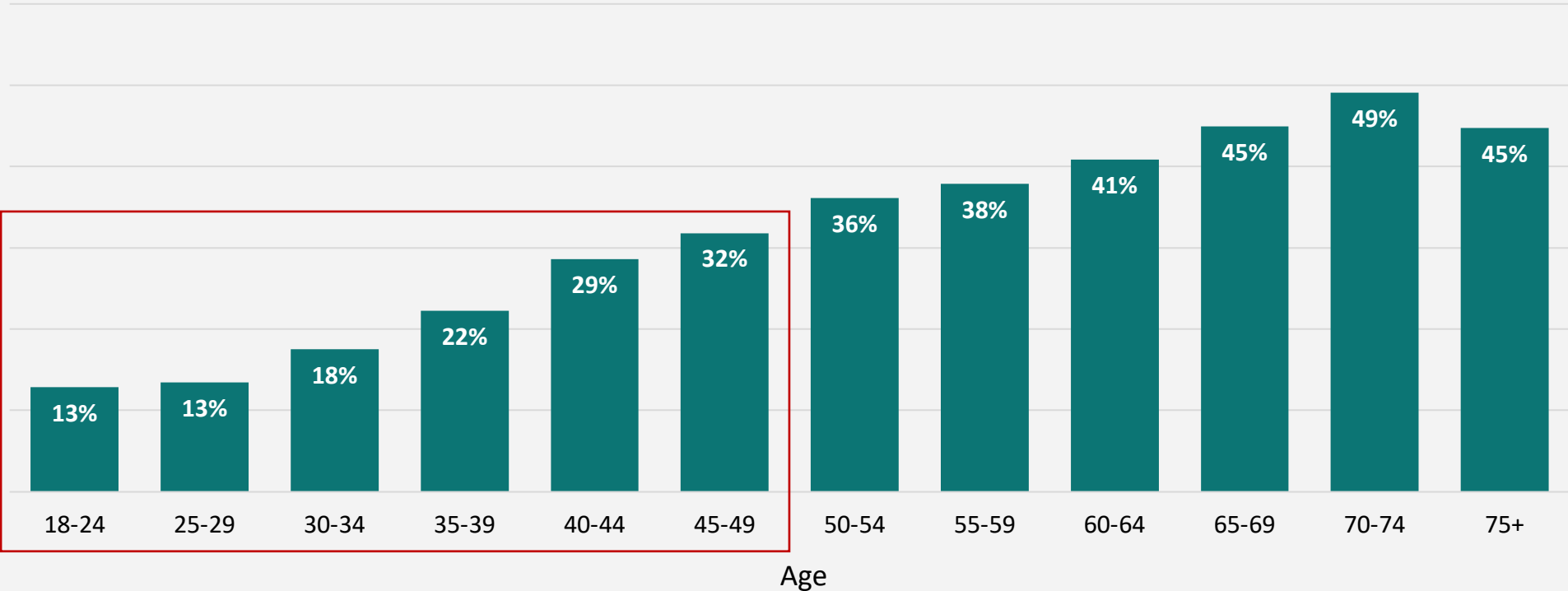
- More than today
- Exactly the same as today
- Less than today
- Don't know
- Refuse to answer

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



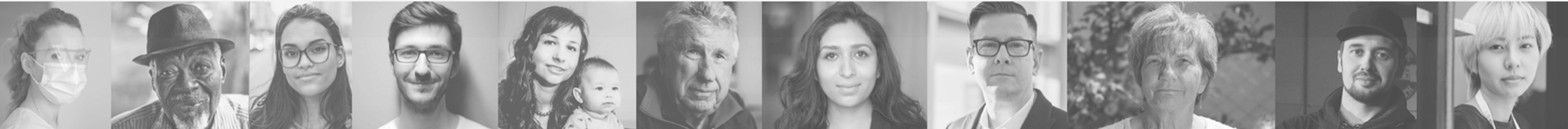
Financial literacy in America, by age

Percentage answering the Big 3 questions correctly



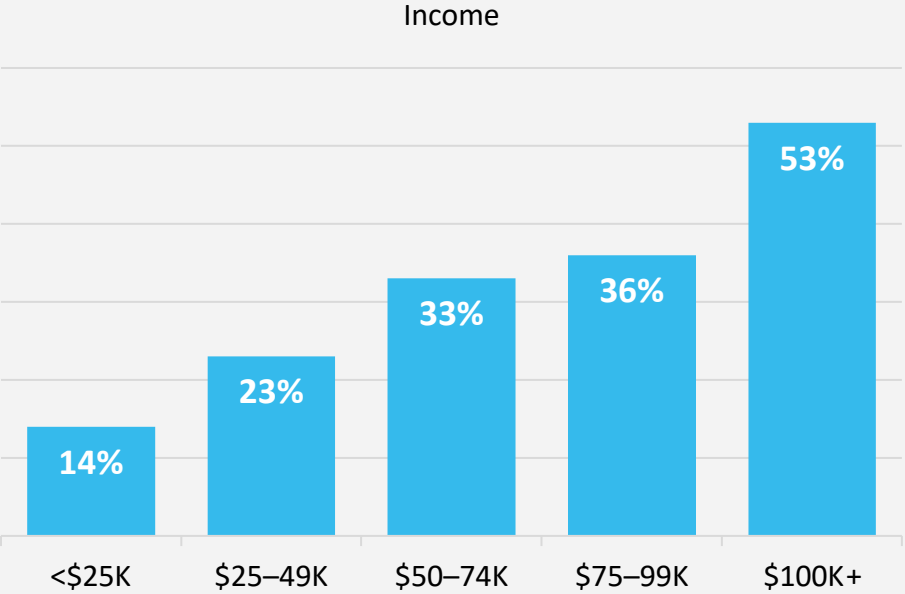
1/3 of Americans know these 3 basic concepts **by age 50**, even though many financial decisions are made well before that age.

Source: 2018 NFCS

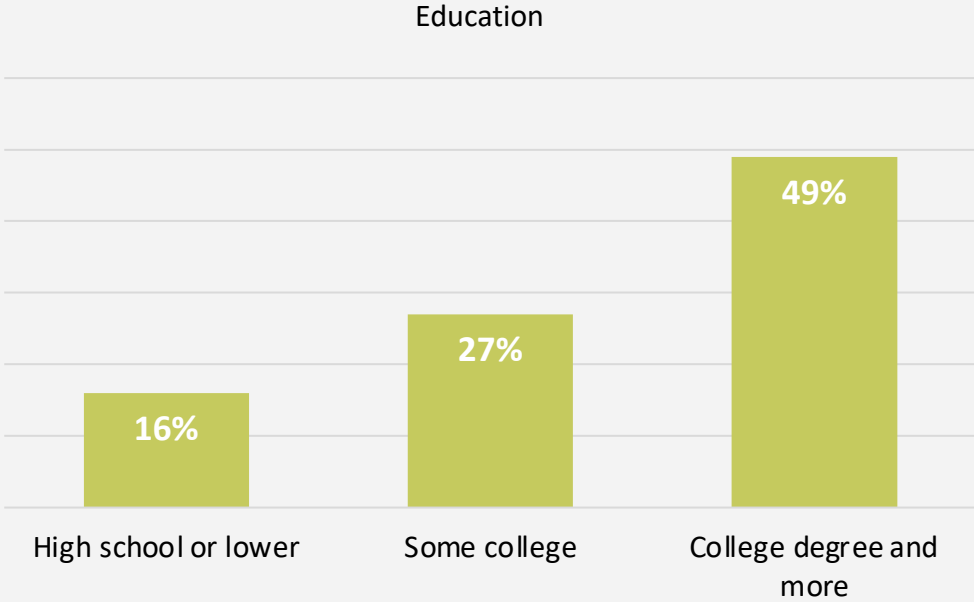


Financial literacy by income and education

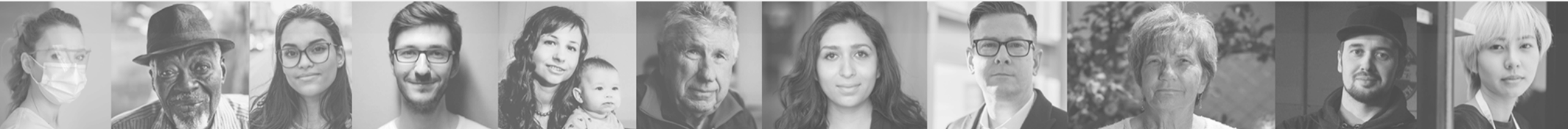
Financial literacy increases with **income...**



... and it increases with **education.**



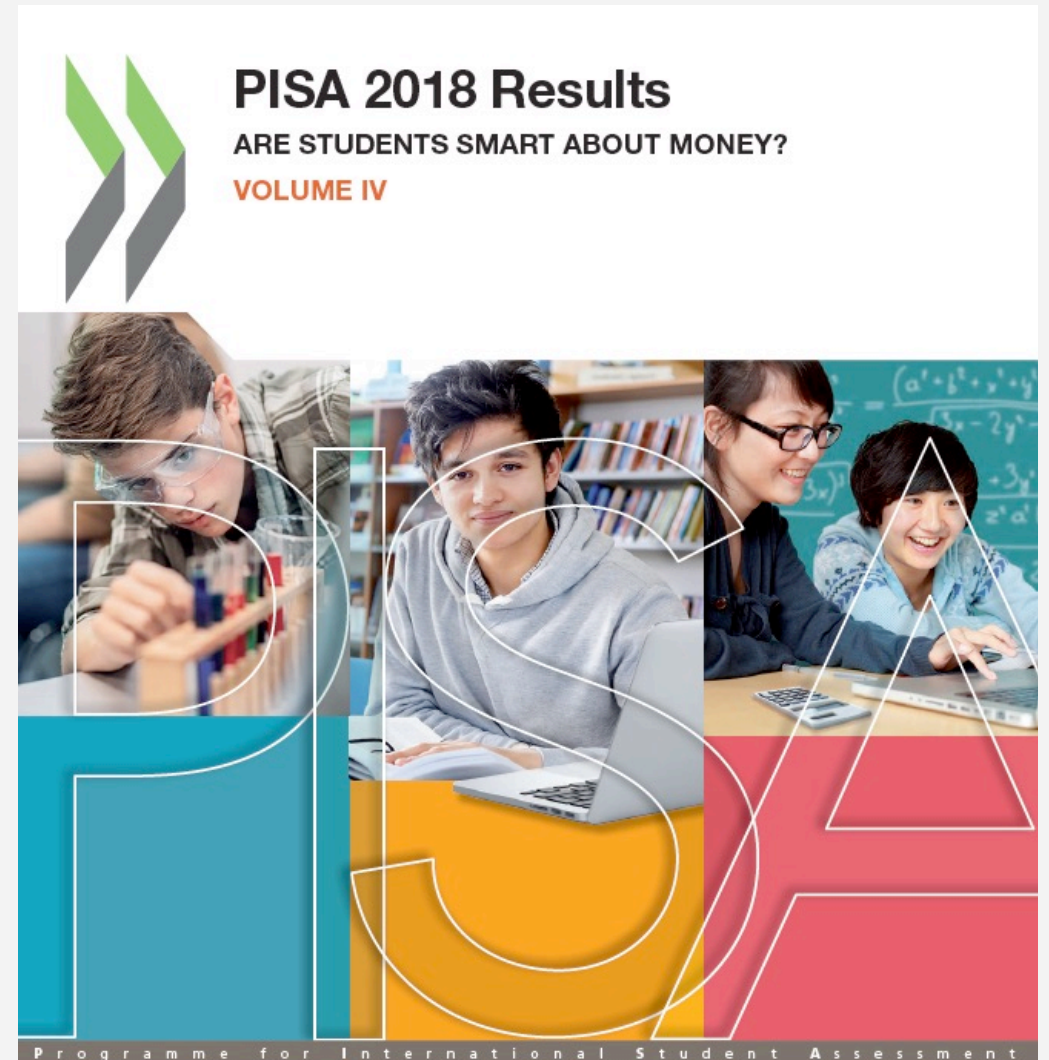
Source: 2018 NFCS



Financial literacy among 15-year-old


Every three years since 2000, the **OECD Programme for International Student Assessment (PISA)** has assessed the extent to which students near the end of their compulsory education have acquired the knowledge and skills needed to fully participate in society.

Financial literacy was added in 2012.



2018 PISA financial literacy scale

Average scores of 15-year-old students on the PISA financial literacy scale, by education system: 2018

Education system	Average score
OECD average	505
Estonia	547 ▲
Finland	537 ▲
Canada	532 ▲
Poland	520 ▲
Australia	511
 United States	506
Portugal	505
Latvia	501
Lithuania	498
<i>Russian Federation</i>	495 ▼

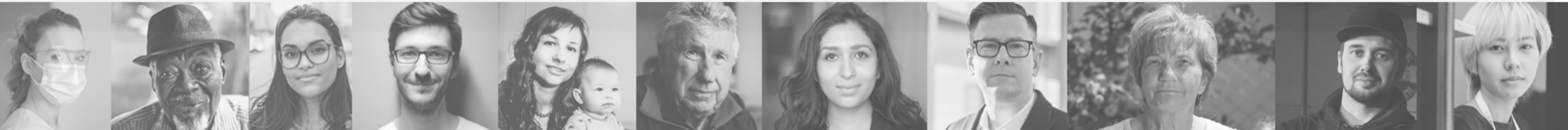
Education system	Average score
Spain	492 ▼
Slovak Republic	481 ▼
Italy	476 ▼
Chile	451 ▼
<i>Serbia</i>	444 ▼
<i>Bulgaria</i> ¹	432 ▼
<i>Brazil</i> ¹	420 ▼
<i>Peru</i> ¹	411 ▼
<i>Georgia</i>	403 ▼
<i>Indonesia</i>	388 ▼

- ▲ Average score is higher than U.S. average score at the .05 level of statistical significance.
▼ Average score is lower than U.S. average score at the .05 level of statistical significance.

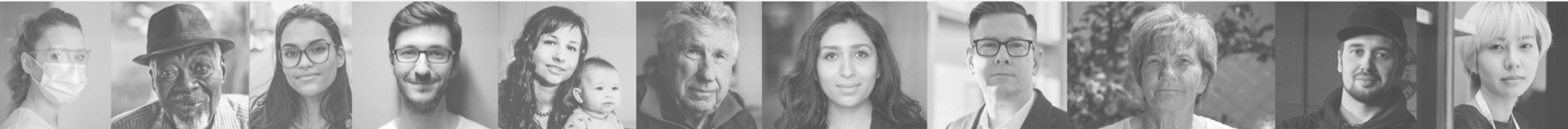
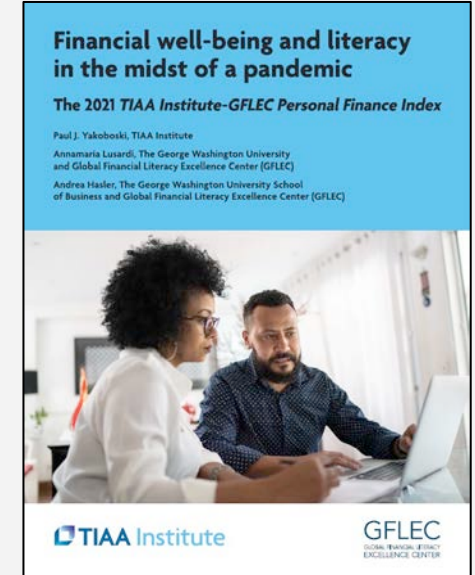
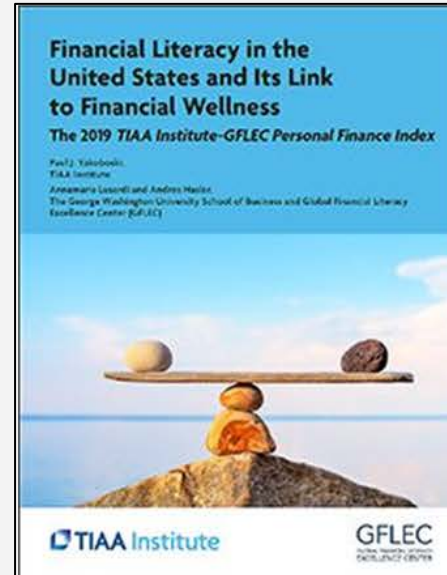
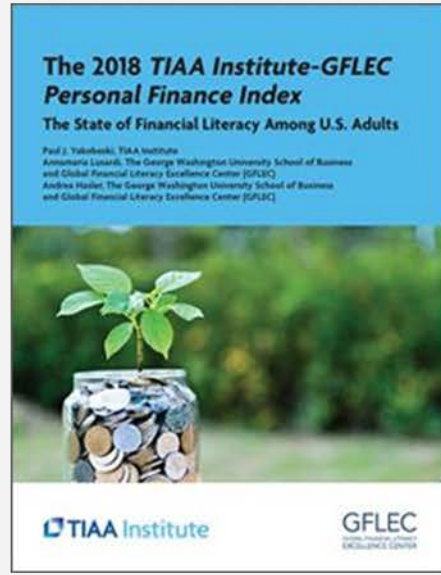
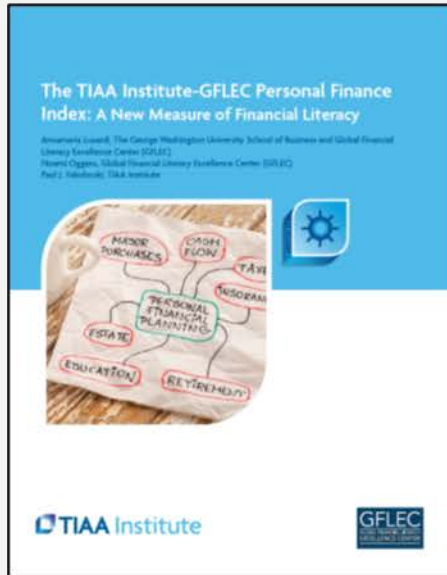
Who is less financially literate?

- Students from families with low income and educational attainment
- Those who do not have books at home
- Students of color

Differences in financial literacy start early.

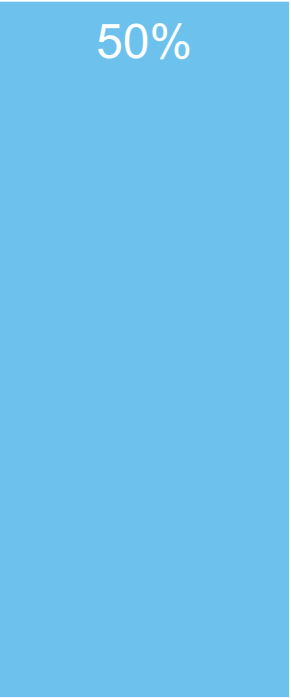


Measuring personal finance knowledge with 28 questions: The P-Fin Index

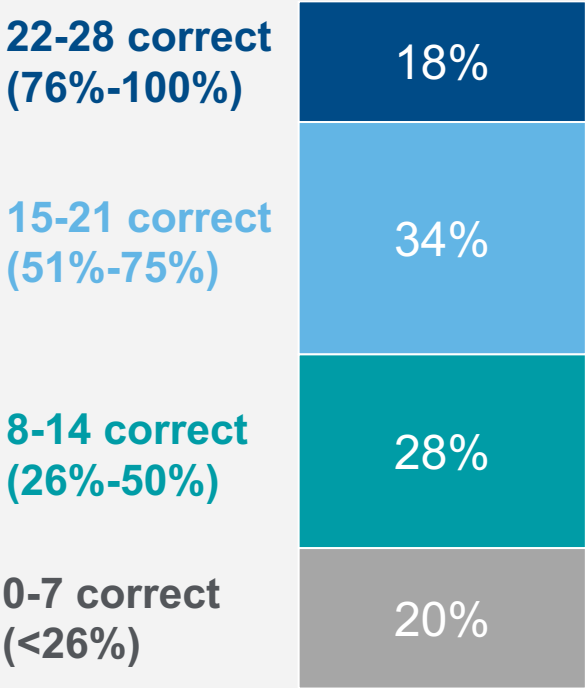


Financial literacy in America: A failing grade

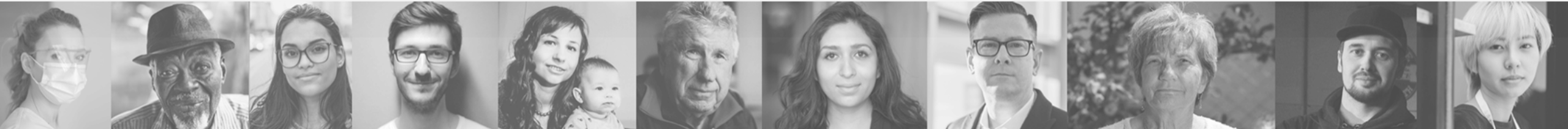
% of P-Fin Index questions answered correctly



Distribution of correct answers to P-Fin Index questions



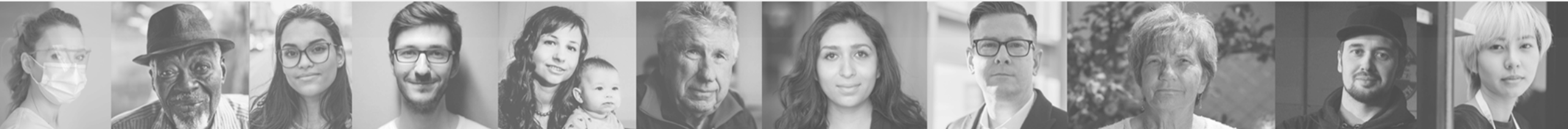
Source: TIAA Institute-GFLEC Personal Finance Index (2021).



Who is less financially literate?

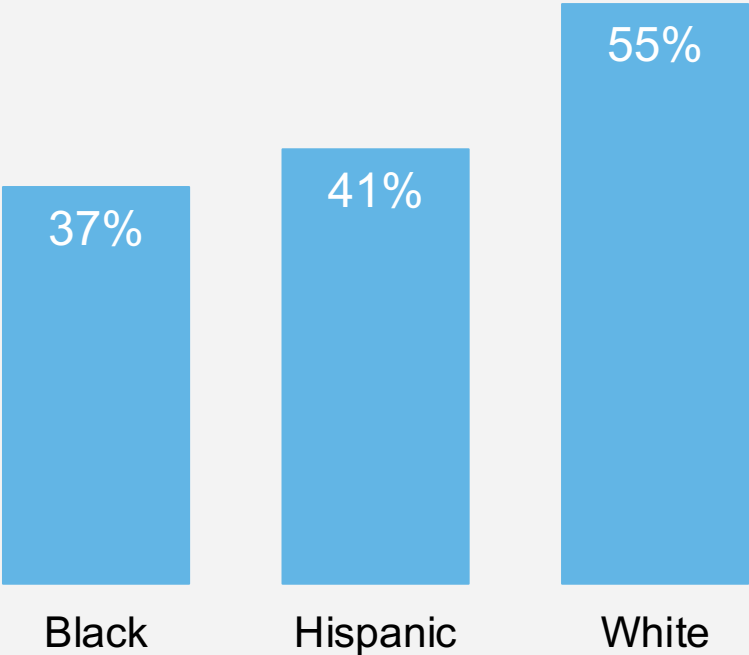
- Individuals with low income and educational attainment
- Women and African Americans and Hispanics
- The young

Differences in financial illiteracy have been growing over time.

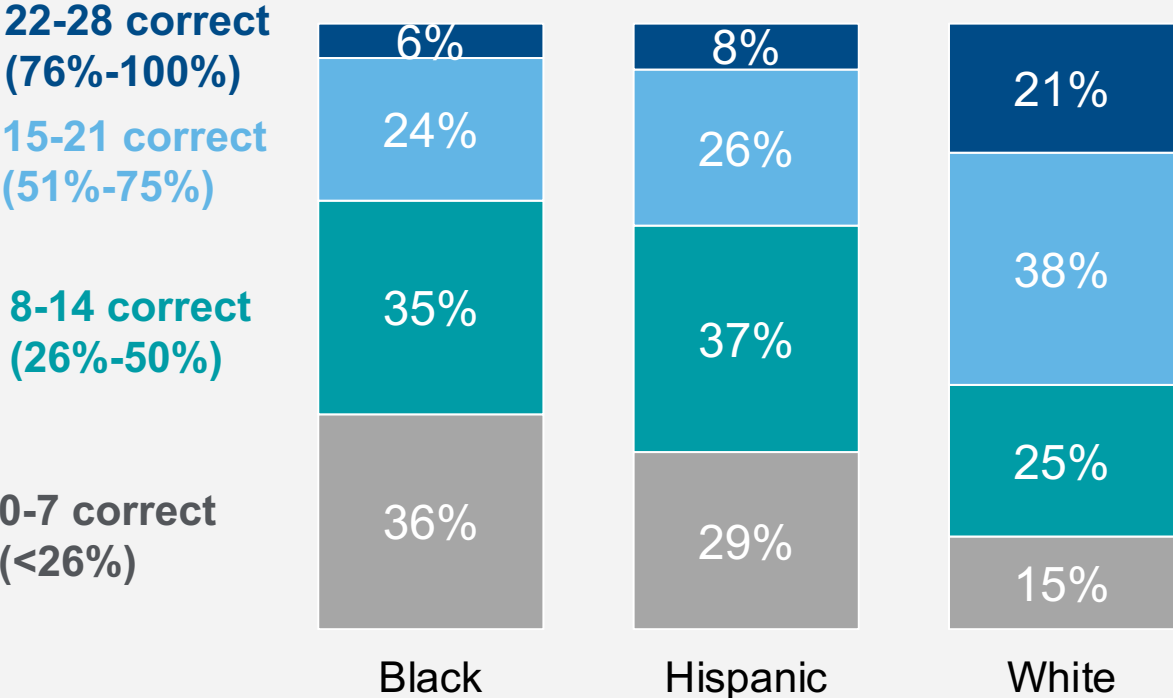


Demographic variation: Racial/ethnic groups

% of P-Fin Index questions answered correctly

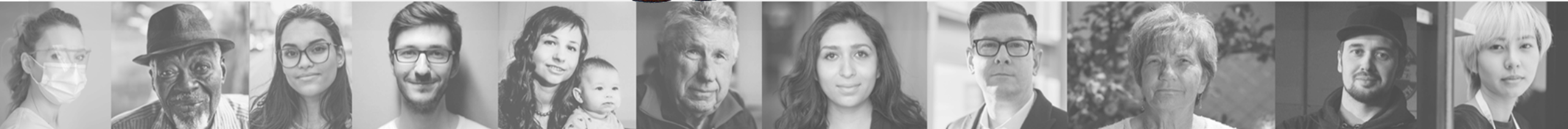


Distribution of correct answers to P-Fin Index questions



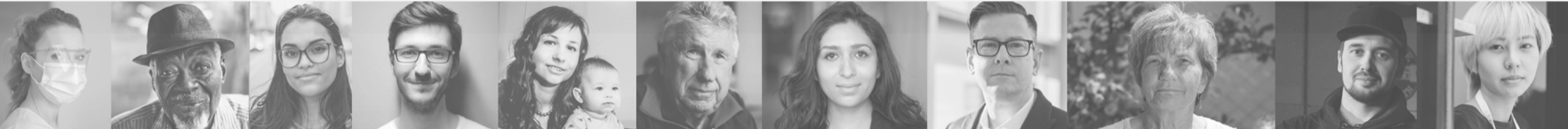
Source: TIAA Institute-GFLEC Personal Finance Index (2021).

The costs of financial illiteracy



Financial fragility in America

Long lines at the food banks at the start of the pandemic!



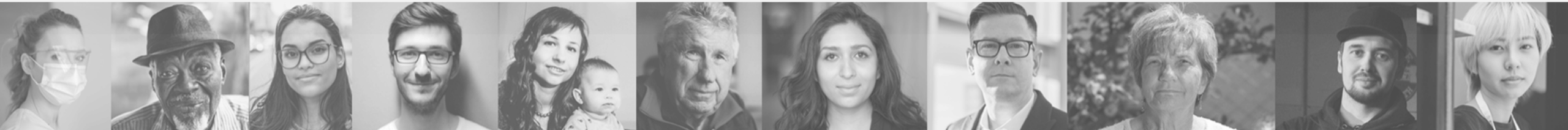
Measuring financial fragility

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

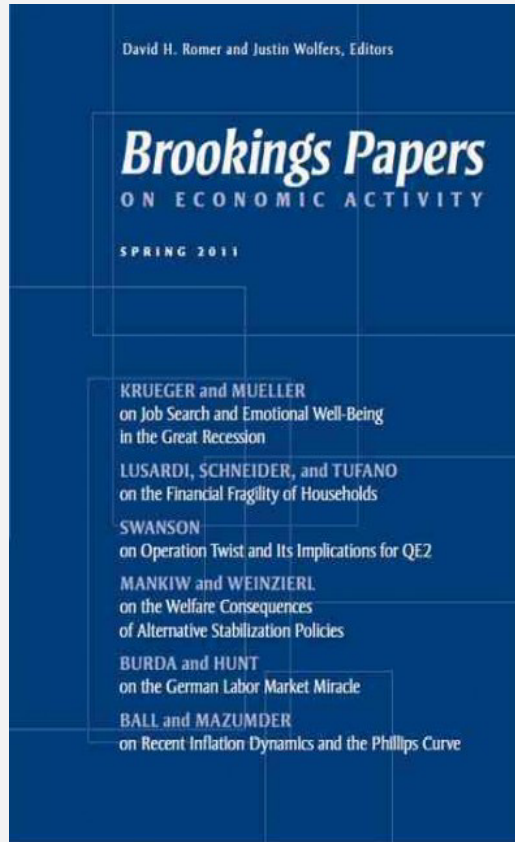
- I am certain I could come up with the full \$2,000.
- I could probably come up with \$2,000.
- I could probably not come up with \$2,000.
- I am certain I could not come up with \$2,000.
- Don't know.
- Prefer not to say.



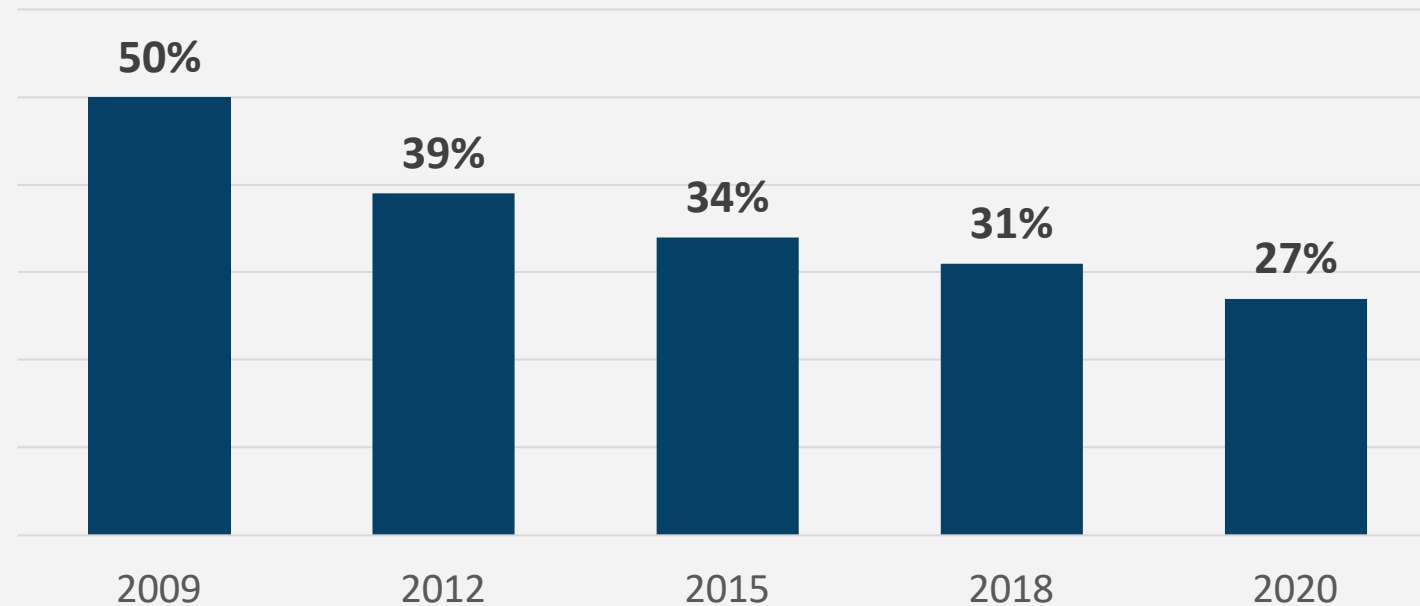
People with these responses are classified as financially fragile.



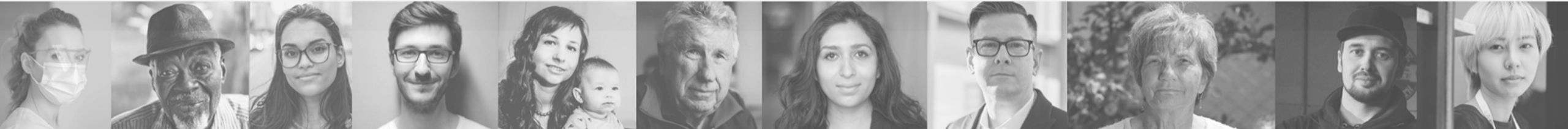
Financial fragility in America before the pandemic



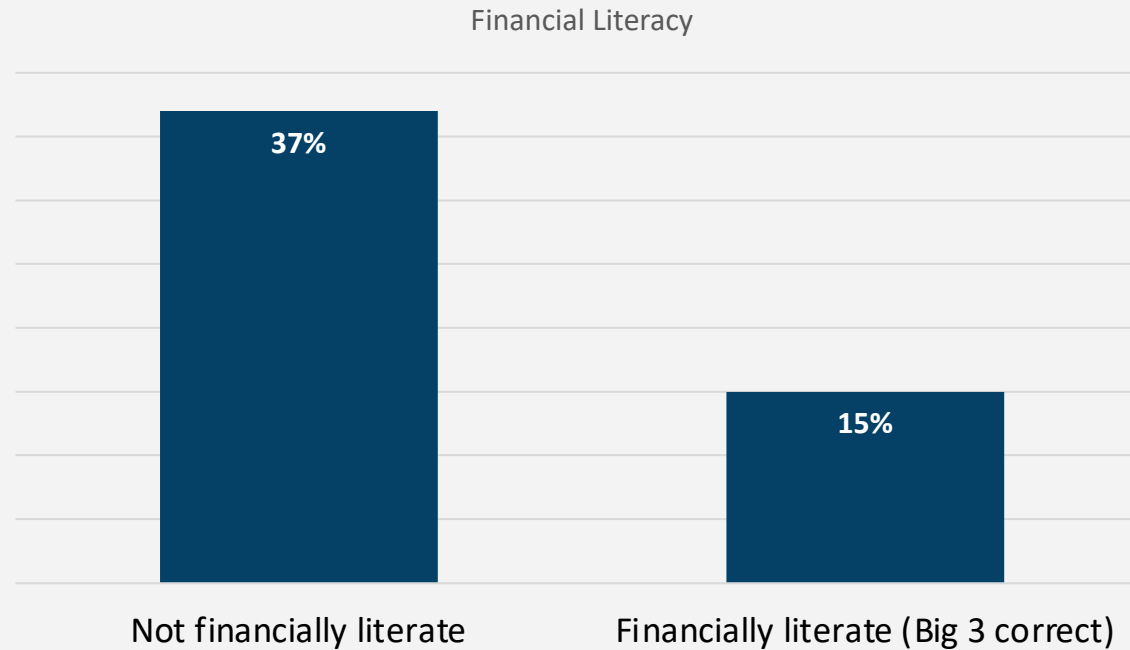
Financial Fragility Over Time



Source: 2009 TNS data, 2012, 2015 and 2018 NFCS data, and 2020 P-Fin data

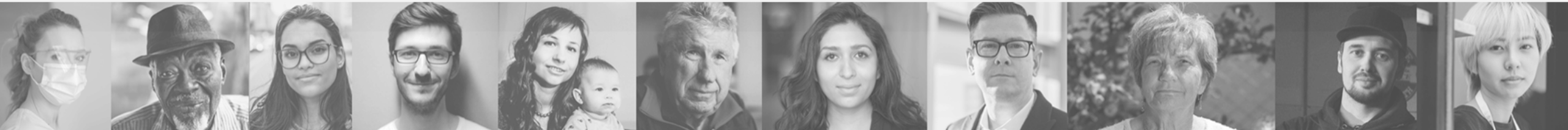


Financial literacy matters for financial fragility



Among those who are **NOT** financially literate, 37% could not come up with \$2,000 within 30 days.

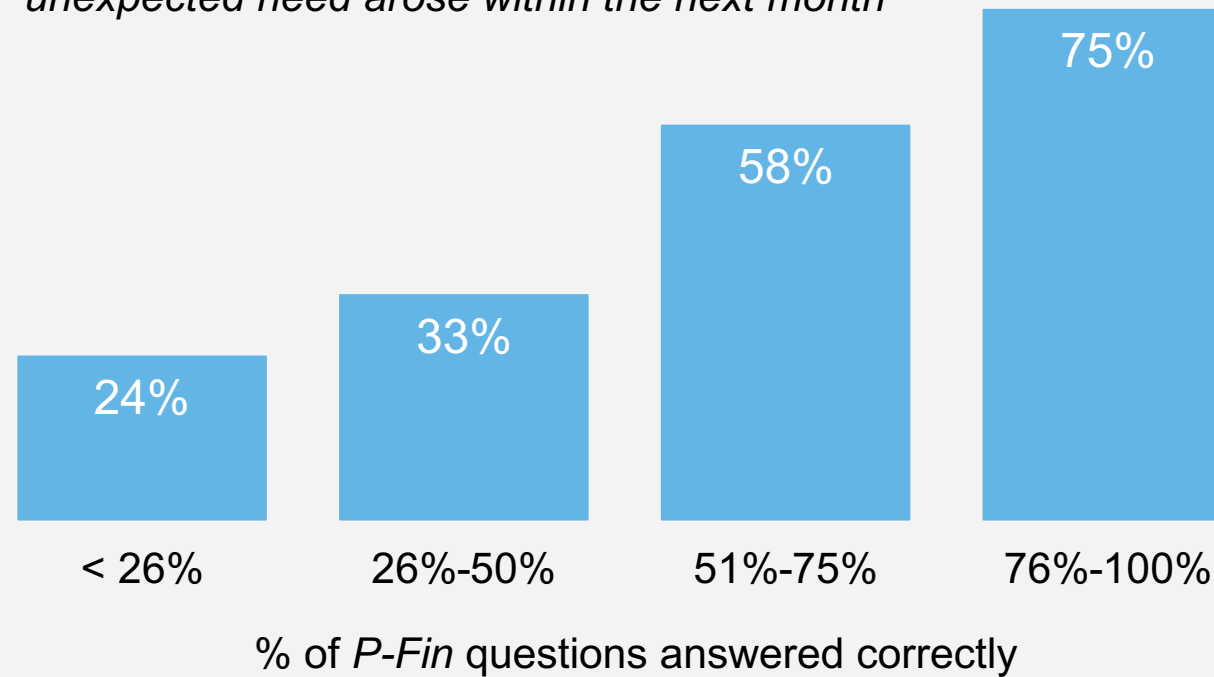
Source: 2018 NFCS



Strong negative correlation between financial literacy and financial fragility

% who could certainly come up with \$2,000 if an unexpected need arose within the next month

Those with greater financial literacy are less likely to be financially fragile.

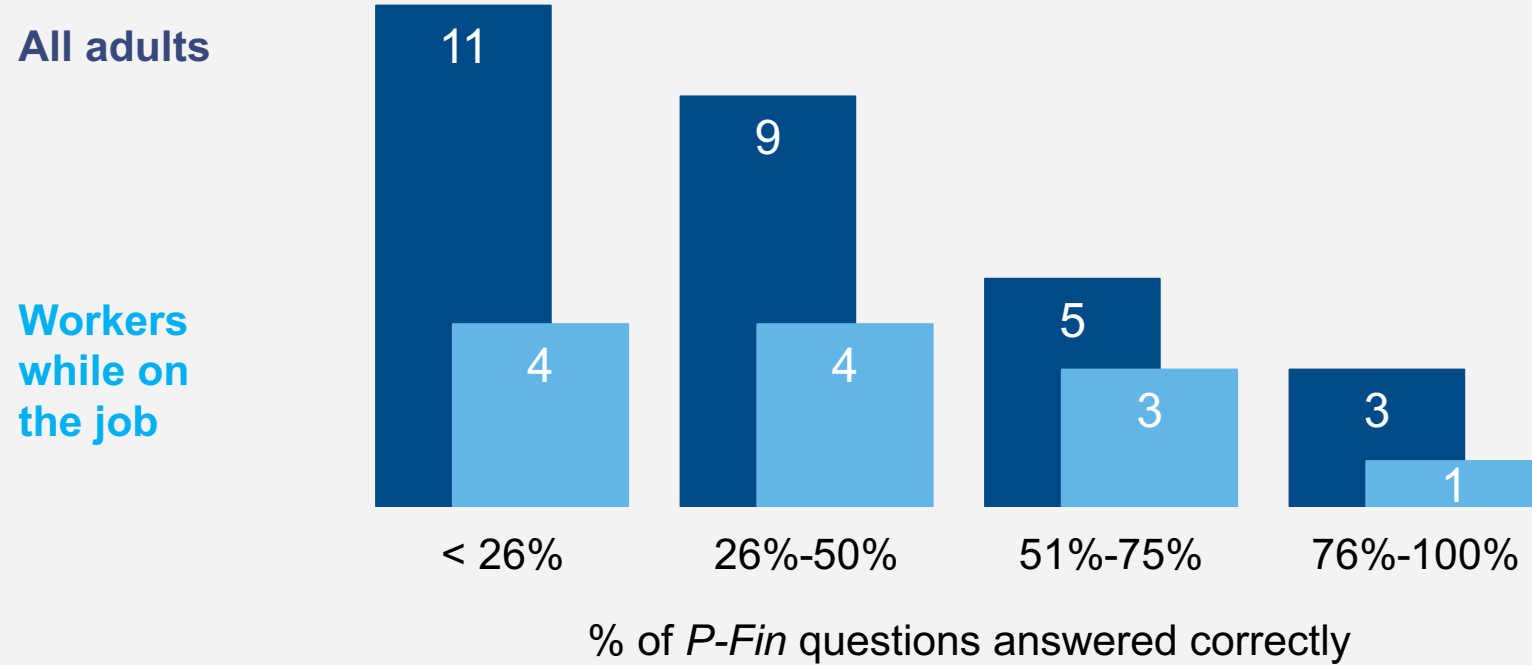


Source: TIAA Institute-
GFLEC Personal Finance
Index (2021).



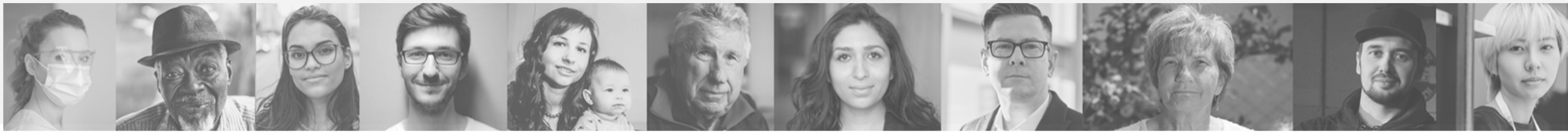
A simple measure of the cost of financial illiteracy

Average hours per week spent thinking about and dealing with issues and problems related to personal finances



People spend an average of 7 hours per week thinking about and dealing with financial issues and problems. An average of 3 hours per week occur at work.

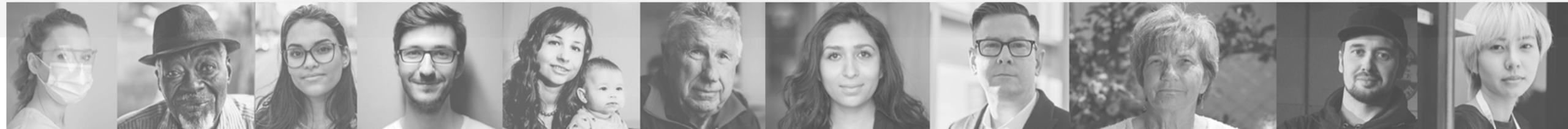
Source: TIAA Institute-GFLEC Personal Finance Index (2021).



Translating research into action

We need large and scalable programs

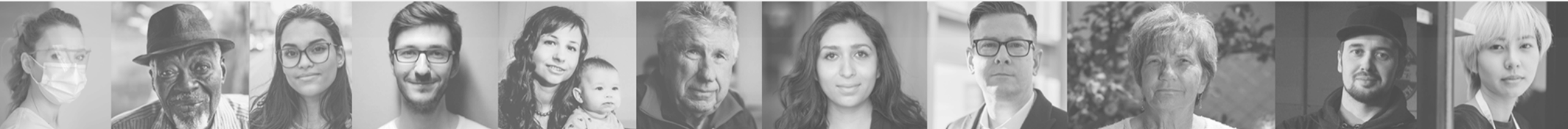
- Financial education in school
- Financial wellness programs in the workplace
- Financial education in the community (libraries, museums, theaters, churches, town halls, or other places where people go to learn)



GFLEC initiative: Fast Lane for finedu in high schools

- Provides research-based guidance and support for (1) students, (2) teachers, (3) school administrators, (4) parents/guardians, (5) policy makers, and (6) community members
- A resource center with tailored toolkits
- Making sure young people are on the fast lane to financial prosperity

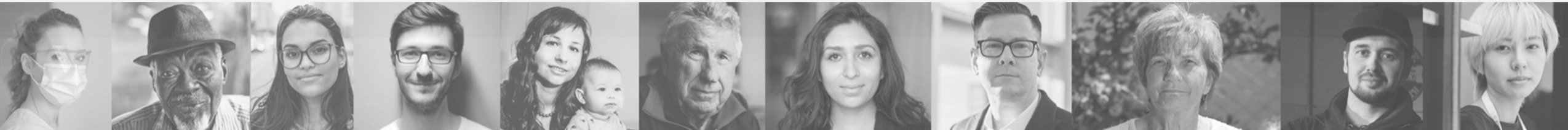
fastlane-education.org



Personal finance course at GW since 2012

- Personal Finance courses for undergraduate and graduate students
- Based on our data and research
- Takes into account the large differences across students based on their demographic background
- Material available for free on our website:

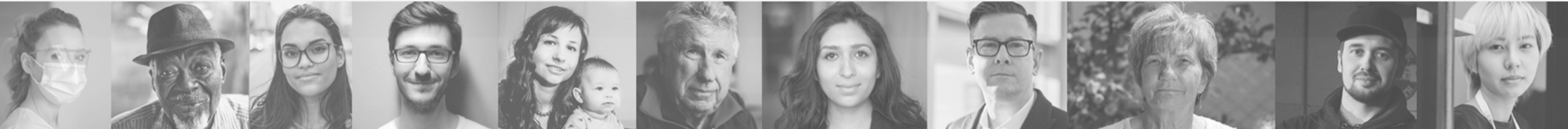
<https://gflec.org/education/personal-finance-course/>



Suggestions for personal finance

Five steps to financial freedom

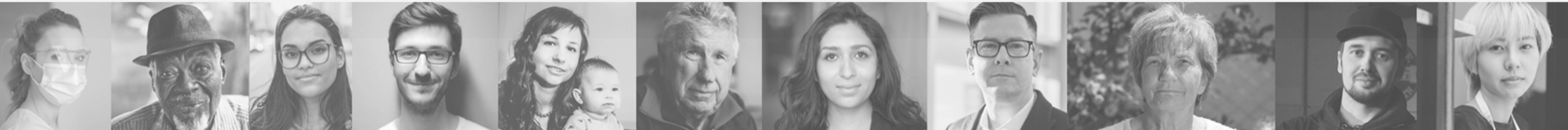
- Take care of your finances
- Build a good credit score (it's your personal finance GPA)
- Build and keep a buffer stock of savings
- Make good use of time
- Invest in education and in financial markets



Take care of your finances

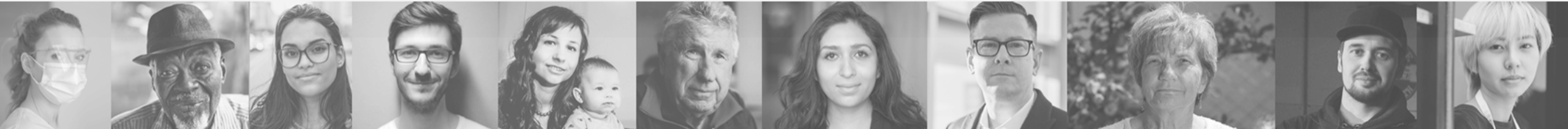
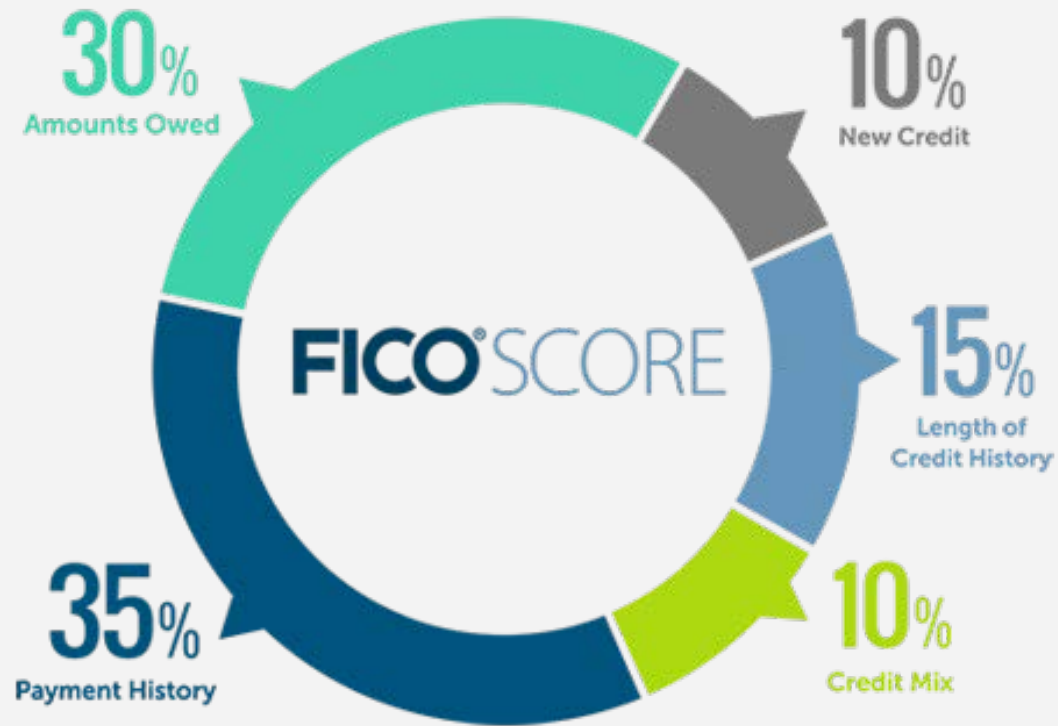
How:

- Dedicate time each week to your personal finances, even 10-15 min will do
- Keep track of expenses
- Read about this topic; improve your financial literacy



Build a good credit score

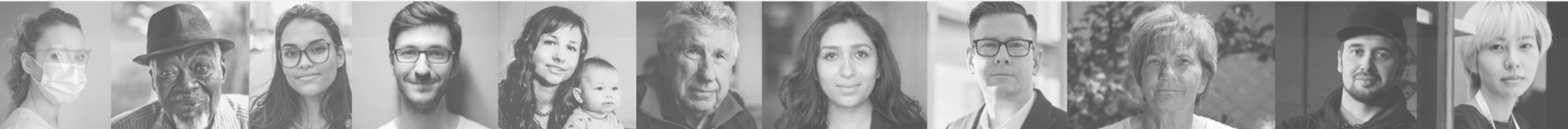
Build a credit history and keep track of your score, it will save you a lot



Build and keep a buffer stock of savings

It is very important to have emergency savings

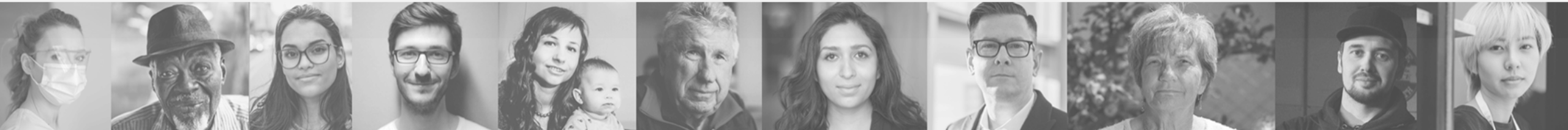
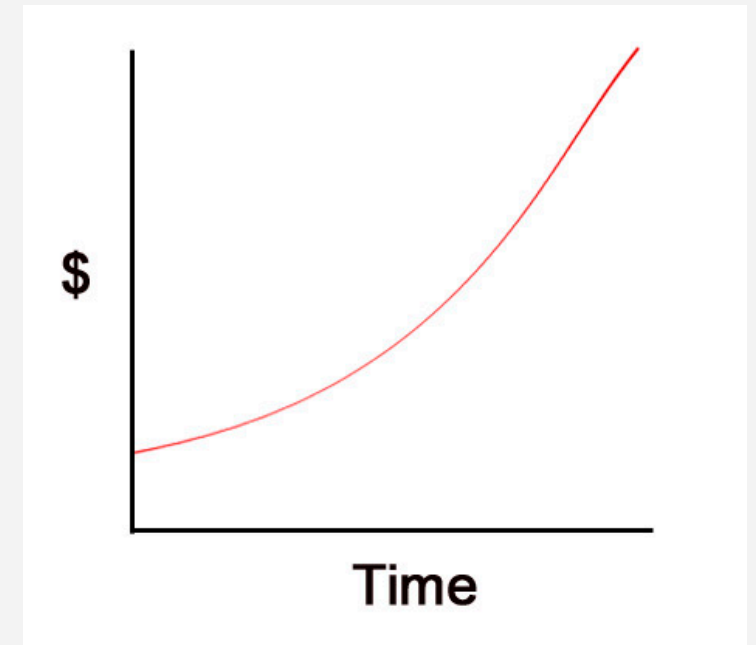
- Save small amounts regularly
- Rebuild the stock if you spend it out
- Avoid using debt or credit cards to deal with shocks
- Having \$2000 can go a long way to prevent financial stress



Make good use of time

All young people have a great resource: time

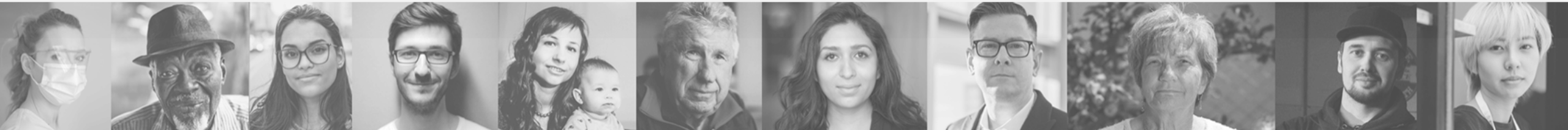
- Start saving as soon as possible
- Save consistently over time
- With long horizons in front of you, you can take risk



Invest in education and financial markets

Invest in your talents and in financial knowledge

- Education has a good return, particularly in certain fields
- Many jobs of the future have not been invented; invest in skills that make you adaptable to changes
- Interest rates are low or zero: Grow your wealth by investing in the stock market; diversified index funds are what academics recommend



What is financial literacy

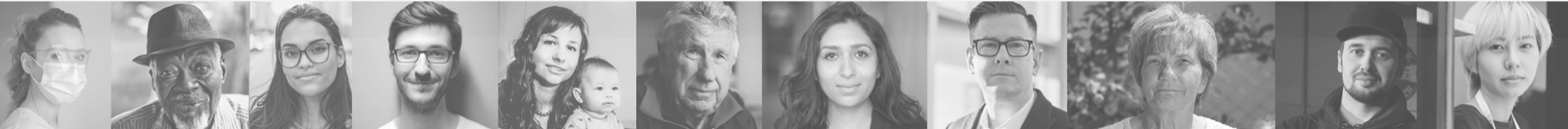
Financial literacy is like water in an ecosystem

- One of many ingredients needed for one's financial life to flourish
- It is an essential component (i.e., the foundation), but people do not have enough of it



Living well

- Just as we ensure access to clean water to protect quality of life, we must provide people with the resources and skills needed to be more financially resilient, more financially secure, and less worried about their future.





Thank You!

More info at www.gflec.org. For any questions, you can reach me at alusardi@gwu.edu

