

OECD-US Treasury International Conference on Financial Education

**VOLUME I - Keynote addresses, interventions
and main policy recommendations**

OECD-US Treasury International Conference on Financial Education

**Taking Financial Literacy to the Next Level:
*Important Challenges and Promising Solutions***

PROCEEDINGS

In order to further advance the policy dialogue on financial education, the OECD and the US Treasury co-organised a high-level International Conference on Financial Education, on 7-8 May 2008, in Washington D.C. This successful and particularly well attended global event, and the resulting publications, are an integral part of the OECD Project on Financial Education.

The first volume of the proceedings provides a selection of main speeches delivered and papers presented at the conference. The rich analysis in these papers, and the sharing of experience and good practices of senior governmental and private experts makes this publication a valuable reference tool.

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and main policy recommendations**

VOLUME I



U.S. Treasury
Department



Washington, DC, USA

May 7-8, 2008

OECD-US TREASURY

INTERNATIONAL CONFERENCE ON FINANCIAL EDUCATION

Taking Financial Literacy to the Next Level: Important Challenges and Promising Solutions

Washington D.C.

7-8 May 2008

PROCEEDINGS

VOLUME I

Keynote Addresses, Interventions and Main Policy Recommendations

FOREWORD

On May 7-8, 2008, the U.S. Treasury Department and the Organization for Economic Co-operation and Development (OECD) co-organized a two-day high-level International Conference on Financial Education in Washington, DC. It generated a multinational dialogue on recent developments, innovative methods, and successful tactics for improving financial literacy.

The culmination of this conference was the result of OECD's ongoing financial education project which started in 2003 and was built on three main pillars: the elaboration of analytical and comparative research reports; the development of international principles and good practices; and the promotion of enhanced international awareness, cooperation and policy dialogue on financial education¹.

Through this partnership between the Treasury Department and OECD, the Treasury Department accomplished one of its calls to action outlined in its national strategy entitled, *Taking Ownership of the Future: The National Strategy for Financial Literacy*², which was issued in 2006 by the U.S. 20-agency Financial Literacy and Education Commission.

Participants included over 200 leaders from governments, universities, businesses, non-profits and international organizations that, in total, represented 43 countries. Through a far-reaching programme, these international high-level policy and decision makers and practitioners shared their approaches, experiences and best practices on most topical and challenging financial education issues including:

- Creating and implementing national financial education strategies
- New realities of retirement savings
- Enhancing awareness of risks transferred to individuals
- Credit challenges and opportunities resulting from the mortgage problems
- Developing and delivering youth financial literacy programs
- Increasing financial access for underserved groups
- Identifying efficient practical tools and innovative techniques to implement financial education programs

In his opening address at the conference, the OECD Deputy Secretary-General, Mr. Pier Carlo Padoan stressed that "Financial education is not just for investors. It is just as important, if not more so, for the average family trying to balance its budget and save for their children's education and the parents' retirement." He touched upon upcoming challenges for financial education and concluded by noting that financial education should be considered as a complement to, rather than a substitute for, proper financial market regulation and supervision.

¹ For further information, on this project, see the foreword of volume II and the OECD International Gateway for Financial Education (www.financial-education.org)

² For more information about the U.S. National Strategy, see www.mymoney.gov.

The Secretary of the Treasury Department Henry M. Paulson, Jr. in closing the conference stated that as the world has become more connected and financial products have become more complex, there is an even greater need for financial education. He also said “people everywhere want to know how to wisely spend, save and invest their money. They want to build a more secure and prosperous future for themselves and for their families.”

Among the keynote speakers and moderators of the conference, Dan Iannicola, Jr., Treasury Deputy Assistant Secretary for Financial Education and Executive Director of the President's Advisory Council on Financial Literacy, emphasized that in spite of nations' unique economic characteristics, they share a number of common problems when their populations lack needed financial skills. He said a goal of the conference was to bring countries together to look for common solutions to these problems. André Laboul, head of OECD's Financial Affairs Division, also stressed the need to develop a new culture of financial responsibility and help citizens become financially educated. He said that in a world where financial risks are increasingly transferred to households, financial education has become an essential policy tool.

This volume provides the details of the conference sessions and panel including the main keynote addresses and summary of interventions of speakers as well as specific policy conclusions of moderators for each session³.

The OECD and the Treasury Department would like to especially thank the Organization of American States and its staff for hosting the event. They are also grateful to all the speakers and moderators for their valuable contributions to the success of this conference.

The views expressed here are the sole responsibility of their authors and do not necessarily reflect those of the OECD Committee on Financial Markets, Insurance and Private Pensions Committee and Working Party on Private Pensions, the Secretariat, the Member or non-Member countries. The publication has been prepared by the OECD Financial Affairs Division with the collaboration of the Treasury Department's Office of Financial Education.



Dan Iannicola
Treasury Deputy Assistant Secretary
for Financial Education and
Executive Director of the President's Advisory Council
on Financial Literacy



André Laboul
Head of the Financial Affairs Division
OECD

³ PowerPoint presentations and papers included in this publication as well as bios of moderators and speakers are available on the OECD Conference webpage www.oecd.org/daf/financialeducation. The conference was transmitted live by the OAS, with the support of the Young Americas Business Trust, and can be viewed through their videos on demand service at www.oas.org.

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OPENING ADDRESS

“IMPORTANCE OF FINANCIAL EDUCATION”

by Mr. Pier Carlo Padoan, OECD Deputy Secretary-General

Introduced by Dan Iannicola, Jr., Treasury Deputy Assistant Secretary for Financial Education and Executive Director of the President's Advisory Council on Financial Literacy, United States

Introduction

I'm sure all of you noticed the increasing new buzz around Financial Education. The Economist was recently referring to this as the “global crusade which is under way to teach personal finance to the masses”.

Like never before, researchers, public authorities, community groups, industry associations and international organizations, are developing financial education initiatives and want to understand how people can become “financially literate”, or in other words, have the knowledge, understanding, skills and competence to deal with everyday financial matters and make the right choices for their needs.

Looking at the variety of organisations represented here today, we have a great demonstration of the expertise, knowhow and commitment that is being put towards this goal of informing and protecting financial consumers.

Areas of Concern

Why have so many stakeholders started paying so much attention to the issue of financial education and literacy? You will all have your personal answers to that, but for the organization I represent, the OECD, financial literacy and awareness clearly promotes economic growth and well being, by expanding the quality of available financial services, and by enhancing the ability of individuals to more effectively use these services for their best interest.

But why is this goal so difficult to reach? There are, in my view, three broad areas of concern that call for enhanced financial education:

1. There is a rapid and growing sophistication of financial markets, as a result of deregulation, globalisation and technological progress in the financial marketplace. Consumers are now faced with a variety of complex financial instruments offering a large range of options. And in some cases, as underlined by the recent market turmoil, it may take years before the quality of the products can be assessed.

2. At the same time, risks have been increasingly transferred to households. Households now assume more of the responsibility and risk for financial decisions, especially in the areas of credit and retirement savings. For example, the shift in the pensions field to defined contribution schemes means

a transfer both investment and longevity risks to individuals, who may not have the knowledge to deal with these risks.

3. Rapid developments in several emerging economies have resulted in the explosion of financial products (like credit cards) being offered to a vast number of “new consumers”, many of whom have only limited experience with formal financial systems.

OECD Response

In response to these concerns, 5 years ago the OECD launched a major international programme on financial education. The programme is composed of 3 main components:

The first facet is analytical: A key milestone of the programme was the publication, in 2005, of *Improving Financial Literacy: Analysis of issues and policies*. That was the first major international study addressing the issue of financial education. This study analyses financial literacy surveys in OECD member countries; highlights the economic, demographic and policy changes that make financial education increasingly important; describes the different types of financial education programmes currently being offered in OECD countries; and endeavours to evaluate their effectiveness. It also recommends actions that policymakers can take to improve financial education and awareness.

The second objective of the programme is related to the first one and concerns the development of international guidelines and good practices.

- The 2005 study was accompanied by the OECD Council’s Recommendation on Principles and Good Practices for Financial Education and Awareness. The aim of the Recommendation is to help policymakers design and implement effective financial education programmes. The Principles include suggestions:
 - on how governments can increase public awareness of financial issues,
 - on how financial institutions can provide objective information on financial products,
 - the role of employers in the provision of financial information,
 - what the providers of retirement savings products need to consider in determining the content and delivery of financial education programmes.
- In June 2006 the G8 finance ministers welcomed the ongoing work of the OECD on its Financial Education Project, and called for further development of financial literacy guidelines based on best practices.
- In response, the OECD developed and recently adopted financial education guidelines and good practices in the pensions and insurance sectors.
- In light of the recent developments in the mortgage and credit markets, the OECD is analysing policy issues related to financial education in the area of credit, and this will likely result in the development of further guidelines for that sector.

The third component of the programme relates to promoting international cooperation on financial education. When establishing the programme, OECD governments recommended that the

Organization become an international forum to exchange information on recent national experiences in financial education.

- We achieve this goal through the organization of high level conferences like the one you are attending today, which has been prepared jointly with the Department of the US Treasury; The OECD has organised similar events in India, Russia, and Turkey. We will hold a Global Forum on financial education in Jakarta in October of this year, in co-operation with the Indonesian government.
- To further promote international cooperation, we recently created the International Network on Financial Education, which held its first meeting yesterday in the margins of this conference. The purpose of the Network is to bring together high-level public officials from OECD and non-OECD countries to discuss issues, new developments, experiences and programmes related to financial education. The Network will also allow governmental experts to exchange views on good practices and contribute to the development of OECD guidelines and principles in the area of financial education.
- We have also set up the International Gateway for Financial Education, accessible at www.financial-education.org. The Gateway will serve as an international clearinghouse for financial education and good practices around the globe.

But Financial Education is only one of the Pillars of Adequate Financial Policy Action

Since the OECD issued its Recommendation on Principles and Good Practices for Financial Education and Awareness, a number of governments have developed wide ranging financial education policy approaches. We have also been impressed with the innovative financial education initiatives that have been developed by NGOs, the private sector and by small community groups.

These initiatives are important. At the same time, financial regulation is also an essential component of consumer protection. While financial education can help individuals understand the information that is disclosed to them, policy makers and regulators are certainly expected to provide a framework of protection and supervision, for example to make certain complex products “off-limits” to retail consumers or investors or to ensure that information on products is communicated in plain and understandable language.

Financial education should also be developed hand in hand with improving access to financial markets and services. This access concerns not only populations in developing economies but a significant number of consumers in OECD-member countries – very often minorities or low income groups who do not have access to the banking system. Access to effective, efficient financial services is also a particular issue for international migrants.

Conclusion – Challenges Ahead

We still have much to do and learn about financial education programmes and how to improve them.

First, it is important to increase consumer awareness of the necessity for financial education and to make it accessible. Financial education is not just for investors. It is just as important, if not more so, for the average family trying to balance its budget and save for their children’s education and the parents’ retirement. More needs to be learned about the financial education needs of consumers at various stages in their lives and how financial education programmes can be designed to best address

these needs. We need to better understand how consumers prefer to receive information on financial issues and on how financial education can be best delivered to consumers busy with jobs and families. We should also understand the limitations of financial education programmes and the behavioural factors like inertia or passive behaviour which reduce the effectiveness of financial education and need to be complemented by other mechanisms.

Another challenge is to deepen our knowledge about the role that different institutions can effectively play in educating for financial literacy. Schools certainly need to incorporate financial education into curricula. And we need to better define the roles and responsibilities that can be taken by financial institutions to advance individuals' financial awareness and access to financial services.

To better understand the needs of consumers and the roles of institutions will require objective analysis of which programmes are effective. Evaluation is key to being able confidently to identify good practices.

We hope the discussion at this International Conference on Financial Education will illuminate some of these issues and facilitate the exchange of views and sharing of experience in the area of financial education and awareness.

SESSION I- NATIONAL STRATEGIES: CREATION AND IMPLEMENTATION

Chair: André Laboul, Head of Financial Affairs Division, OECD

A- Chris Pond, Director of Financial Capability, FSA, **United Kingdom**

B- Paul Clitheroe, Chair, Financial Literacy Foundation, **Australia**

C- Diana Crossan, Retirement Commissioner, **New Zealand**

D- Dan Iannicola, Jr., Treasury Deputy Assistant Secretary for Financial Education and Executive Director of the President's Advisory Council on Financial Literacy, **United States**

Policy Conclusions of the Chair

- While local financial education initiatives are very important, it is essential to promote financial education and awareness at the national level in order to stimulate a wider culture of financial education, motivate the whole population and coordinate all the efforts;
- Governments should take actual commitments to promote financial education, including through adequate resources;
- Public/private partnership is essential;
- All national channels should be used: TV, internet, newspapers, brochures; financial education at school is also key for the success of financial education strategies;
- Improved information is useful but not sufficient: population has to change its behavior; to reach a wide audience is one thing, but to change consumer's attitude is another;
- The national, regional and local programmes should be systematically assessed. This calls for an international methodology that the OECD will develop.

A- FSA UK, Financial Capability Strategy

Chris Pond, Director of Financial Capability, FSA, United Kingdom

The FSA is the main statutory regulator for the UK financial services industry. We were established by parliament and are accountable to the Treasury, but are operationally independent of Government and funded solely by the industry we regulate. In total we regulate some 29,000 firms, from global investment banks to very small businesses, and around 165,000 individuals. And we set the standards that they must meet and can take action against firms if they fail to meet these standards.

The Financial Services and Markets Act sets our four statutory objectives; one being 'promoting public understanding of the financial system'. Our development and leadership of the National Strategy for Financial Capability sets out to meet this objective. It is a core part of the FSA's work as improving people's financial capability will contribute to more effective and efficient retail markets.

To inform this work we commissioned a survey, publishing the results in '*Financial Capability in the UK: Establishing a Baseline*' in March 2006. This was the largest ever conducted into personal finance – a rigorous large-scale study to set a baseline against which we can measure progress. We define financial capability as being able to: manage your money, keep track of your finances, plan ahead, make informed decisions about financial products, and stay up to date about financial matters. Over 5,300 in-depth interviews were conducted to serve as a representative of the UK population. Interviews covered people's understanding, attitudes and behaviour to personal finance. This extensive study has been critical in quantifying 'the problem' and in earning space on Government's own policy agenda and buy in from industry. It has also enabled us to target our intervention where it is needed most. We will repeat this every 4 to 5 years.

It revealed the extent to which the UK's financial capability needs to be improved: Too few people plan ahead, too few understand financial products or shop around, and the under 40 age group is far less financially capable than their elders, whilst needing to take far greater responsibility for financial decisions than previous generations. An additional challenge is posed by a changing financial climate, making the area of personal finance particularly daunting for consumers.

The Survey identified groups of people that could benefit from increased levels of financial capability. However, improving financial capability requires large-scale behavioural change over many years. And there are no silver bullets. We need to reach people in a sustained and engaging way through a variety of channels. In some cases, it is clearly appropriate to communicate direct with consumers. But early pilot work showed to reach many of our target groups we must work with the intermediaries that have existing lines of communication with them. Partnership working is therefore central to the National Strategy. We aim to join the expertise and resources of financial services regulator and providers with government, voluntary services, consumer groups and media. We work with existing trusted intermediaries who could, or may already be, working with the consumers we are trying to reach. Our work is designed to complement and work alongside or extend existing initiatives. And we have developed tools and resources to help them, and are implementing our projects with intermediaries and in close partnership with other external organisations.

A programme was developed to reach 10 million people in five years, achieving 'better informed, educated and more confident citizens, able to take greater responsibility for the financial affairs and play a more active role in the market for financial services.' £90 million has been committed by the FSA over the period to 2011 to take this forward. The programme covers:

- In Schools - *Learning Money Matters* delivers teacher support initiatives in England, along with initiatives in Wales, Scotland and Northern Ireland;
- In Further Education - Working with colleges to embed personal financial education in the curriculum through our *Money for LiFE* approach and resources;
- In Higher Education - Providing our *Money Doctors* toolkit to advisers working with students in UK universities;
- For young adults not in education, employment or training ('NEET') – Delivering *Young People and Money* training courses to youth professionals;
- For new and expectant parents - Providing *Parent's Guide to Money* folders;
- In the workplace - Providing *Making the Most of Your Money* materials and seminars to employees across the UK.
- Information direct to consumers via our Moneymadeclear website and free printed guides, providing clear, impartial information to help consumers to make informed decisions about their money.
- Website visitors can make use of our *Financial Healthcheck* and *Debt Test* online tools and comparative tables.
- Working with a number of non-profit sectors to reach people facing financial exclusion, through our *Partnership Development* work. We are working with national bodies so that projects can be rolled-out nationally. The current sectors include cancer support, offenders and prisoners, and those with mental health problems.

'Financial Capability: The Government's Long-Term Approach' published last year set out that everyone in the UK should have access to financial education and advice. It requested the Thoresen Review of Generic Financial Advice, which has now set out a blue-print for a national Money Guidance service for all people in the UK. The FSA has been asked to take forward a two-year 'pathfinder' project to establish the next steps for turning the blue-print into reality.

For more information please visit:

http://www.fsa.gov.uk/financial_capability/

<http://www.moneymadeclear.fsa.gov.uk>

<http://www.whataboutmoney.info>

B- Australia's National Financial Literacy Strategy

Paul Clitheroe, Chairman, Financial Literacy Foundation Advisory Board

Overview

In February 2004, the previous Australian Government established the Consumer and Financial Literacy Taskforce “to develop a national plan to equip Australians with the skills to make important financial decisions over the course of their life”⁴ In August 2004, the Taskforce issued preliminary recommendations to Government on ways to build the capacity of Australian consumers to more effectively manage their money, including that the Foundation be established to take forward a national strategy for improving consumer and financial literacy.

In response to the Taskforce's recommendations, the Financial Literacy Foundation (the Foundation) was established in June 2005 as a division of the Australian Treasury to give all Australians the opportunity to increase their financial knowledge and better manage their money. The Foundation's remit was to deliver a national financial literacy strategy to:

- establish a centralised clearinghouse for consumer and financial literacy education and information resources;
- incorporate education benchmarks and standards in schools;
- foster industry, government and community collaboration; and
- undertake a national consumer and financial literacy information program.

Delivering The National Strategy

The Foundation works to build the capacity of all Australians to better understand and manage financial risk and take advantage of increased competition and choice in Australia's finance sector. It successfully delivered the national strategy over the period to end 2007 and continues to build on those achievements through two broad streams of work:

- Addressing attitudinal and behavioural barriers through awareness-raising – a whole-of-population approach to raising awareness of financial literacy and its benefits, and encouraging people to engage with information and resources through the *Understanding Money* campaign, website and handbook; and
- Addressing structural barriers through education and training initiatives designed to sustain long-term generational improvements in financial literacy by creating opportunities for Australians of all ages to learn more about money – at school, through vocational and higher education, in the workplace and in the community.

Addressing attitudinal and behavioural barriers

The Foundation is working to address attitudinal barriers that prevent people from engaging with money issues in two ways:

⁴ Election 2004 Policy, *Super for All and Understanding Money*, p. 11.

- Providing consumers with easy access to trusted, reliable, independent and easy to understand information, resources and strategies for managing their money better; and
- Conducting research to assist in identifying and addressing the attitudinal and behavioural barriers to improved financial literacy.

Public information campaigns

The Foundation has delivered two *Understanding Money* information campaigns: one that ran between July and December 2006; and a second that ran between August and October 2007.

The aim of the campaigns was to raise consumer awareness of financial literacy and its benefits, and encourage people to engage with financial literacy information and resources to find out more about how to make the most of their money.

The 2006 campaign consisted of advertisements (television, print, radio, online and outdoor), supported by the *Understanding Money* website and handbook, all of which were very well received. The campaign struck a chord with many people, who said that the campaign had relevance for them and motivated them to get started, with the help of the website and handbook.

The website had over 300,000 visits during the campaign, with the Budget Planner and Financial Health Check being the most popular parts. During the campaign, *Understanding Money* was one of the most popular websites on the Australian Government portal.

The handbook was also popular, with over 600,000 sent to individuals and organisations throughout Australia during the campaign. Bulk orders came from schools, counselling services, government departments, accountants and financial planners, credit unions, employment services providers, health services and a range of other organisations and businesses.

The campaign messages were designed to be positive, encouraging, easily accessible and relevant to everyone. Some of the campaign messages were:

A few simple things done regularly can make a real difference, so put yourself in charge.

- Whether you have a little or a lot, it's easier than you think to take control.
- By understanding money better, you can get more of what you want without losing control.
- It helps if you start early.
- Understanding money helps answer those tricky questions, and now is the right time to ask them.

Feedback suggested that the campaign messages were right – that doing a few simple things, like a budget, is a great way to get started. It also suggested that people saw the advertisements and took up the call to action, engaging very actively and taking the first basic steps to managing their money better.

The 2006 *Understanding Money* media campaign was extended by an advertorial campaign in the print and electronic media, and on the internet, between August and October 2007. There was a

positive response to the campaign both in terms of people's reaction to the messages and content and in traffic to the website, which had more than 122,000 visits in the 8 weeks advertorial period.

Website

The *Understanding Money* website:

- Was designed from scratch to meet specific objectives, ie. those identified through the *Understanding Money* campaign research, and as a result, is easy to navigate, easy to understand and internally consistent in terms of style and language;
- has two key audiences: consumers, and educators and trainers, who are addressed through different parts of the site;
- deals exclusively with a comprehensive range of financial literacy issues;
- is well-established and highly regarded as trusted, reliable and independent;
- promotes access to and use of quality education materials; and
- has achieved considerable success in a relatively short period, indicating that the Foundation's approach to delivering effective website design and content has responded to previously unmet demand.

The website was initially conceived as having a "clearinghouse" function to connect consumers with existing financial literacy information and resources. However, it was developed as one of three calls to action for the *Understanding Money* media campaign (visit the website, order a handbook, attend a seminar). Through this process, the underlying concept for the website developed considerably, with the clearinghouse function now being delivered more strategically and with considerably greater effect.

Research conducted in the context of developing the 2006 *Understanding Money* campaign found that consumers did not want assistance in accessing existing financial literacy resources, but easy access to trusted, reliable and independent information to help them manage their money better. Moreover, the information needed to be appealing and easy to understand to overcome the barriers to engagement, such as boredom, dismissiveness (it's not important), lack of time or lack of confidence, ie. consumer feedback was that they needed to be motivated to engage with financial literacy information and resources.

Rather than being a simple link between consumers and financial literacy resources which, without taking these issues into account may have been not only detrimental to advancing financial literacy, but detrimental to people's level of engagement and financial outcomes, the website was developed to be consistent with the campaign's whole-of-population approach and messages:

- inclusive – we all know what it's like, but whether you have a little or a lot, it's never too early or too late to take control of your money;
- engaging – understanding money doesn't have to be boring, difficult or complex;
- enabling and supportive – a few simple steps can make a big difference;

- motivating – by understanding money better, you can get more of what you want; and
- empowering – so put yourself in charge: control your money so it doesn't control you.

As a result, the website provides consumers with:

- access to trusted, reliable, independent information on a range of financial literacy topics and issues in an appealing and easy to understand way; and
- links to other trusted, reliable and independent sources of financial literacy information, rather than duplicating the information provided on those sites, consistent with the original clearinghouse concept.

The responsiveness of the website to identified consumer needs and concerns has been a significant factor in its success, such that it has become a well-established financial literacy resource in its own right, rather than a temporary adjunct to a media campaign, providing an ongoing service to consumers in response to previously unmet demand.

Consumer interest in the site has grown steadily since it was launched in 2006. In financial year 2006-07, the site had almost 570,000 visits. At the time of writing, visits are expected to reach 590,000 in 2007-08. Outside the peak periods of activity prompted by the information campaigns, traffic continues to grow month by month. For example, between January and April 2008, visits were up 40% on the same period in 2007. Traffic analysis shows the most popular content is the practical tools and articles with practical advice on budgeting and saving. There is a steady flow of return visitors and the average visitor spends eight or nine minutes on the site reading three or four articles or using one or more of the tools.

The website will be developed further in the future to further engage consumers and strengthen the Foundation's role in driving long-term improvements in financial literacy. Current plans include:

- developing a "My Financial Plan" space, with interactive tools to encourage people to use the website on a regular basis; and
- improving the site's information architecture and search functionality to make it easier for consumers to explore the full range of content available.

These developments are intended to establish the framework within which the website can develop consistently over the coming years, in a way that optimises its useability, responsiveness, appeal and value in providing consumers with the information, tools and resources they need to manage their money better.

Handbook

The Foundation has also achieved considerable success with the *Understanding Money* handbook, a companion resource to the website for people who do not have internet access, with about 988,000 distributed to end April 2008.

As with the website, the handbook was developed in the context of the 2006 *Understanding Money* campaign, but it has become a resource in its own right with demand extending well beyond the campaign period. Consistent with its position of not duplicating existing resources, the Foundation had not planned to produce such a resource. However, it was produced to be consistent with the

campaign's whole-of-population approach and messages, and against expectations, proved to be popular. Again this indicates that a Foundation resource was responding to previously unmet consumer demand.

In addition to orders placed via the website and by telephone, the handbook has been distributed:

- through Commonwealth government agencies and other distribution partners such as CPA Australia;
- to families with young children through 9,550 childcare centres in March 2007;
- to industry bodies, such as superannuation funds, for distribution to members and in the context of in-house training programs;
- to various community organisations working with low income, disadvantaged and marginalised Australians; and
- to many retirement villages and seniors' organisations.

The handbook is also available in Arabic, Chinese, Greek, Italian, Korean, Spanish and Vietnamese.

Research

The Foundation's primary research response to identifying and addressing the attitudinal and behavioural barriers to improved financial literacy has been the survey of Australians' attitudes, behaviours and beliefs about using and managing money, the findings of which have been published in the report *Financial literacy – Australians understanding money*.

The report represents a unique contribution to the body of international financial literacy research, as well as to research on financial literacy in Australia. Its unique qualities stem from:

- the sample size – 7,500 Australians;
- the age range – 12 to 75 year olds (reflecting the Foundation's commitment to financial literacy education through school-based learning);
- the comprehensive range of money management issues covered – 13 issues from budgeting, saving, managing debt and dealing with credit, to avoiding scams and protecting money, and investing, understanding financial language and ensuring enough money for retirement; and
- the focus – people's ability, understanding and behaviour in regard to using and managing money, as well as the attitudes and beliefs which act as barriers to engaging with and learning about better money management.

The survey was designed to complement other Australian surveys that aim to provide an objective measure of competency in financial matters, and contribute to a broader understanding of financial literacy in Australia by examining respondents' self-assessed ability, understanding, attitudes and behaviour in regard to using and managing money.

The findings of the research are important in terms of developing financial literacy initiatives which respond to consumers' self-identified needs, for example:

- people are less confident in their ability and more willing to learn about more complex issues that they encounter less frequently, such as investing, understanding financial language and ensuring enough money for retirement, suggesting a need for more targeted financial literacy responses;
- people do not always have good money habits, even when they say they have the ability to manage money well (for example, 22% of people say they don't save), suggesting a need to reinforce basic financial literacy messages;
- young people have completely different needs to the adult population: their confidence is lower across the board, reflecting their relative lack of experience, but they have uniformly higher levels of recognition of the importance of learning more about managing money better and they like learning at school; and
- it is not sufficient to provide consumers with access to financial literacy information, tools and resources: they must be motivated to overcome the attitudinal and behavioural barriers to engaging with and learning about managing money better.

In addition to informing its own work, the Foundation has a responsibility, consistent with its national leadership role, to share the findings of the research so that service providers and resource developers in other settings are also building their understanding of where their efforts can be focussed to optimise results, and what barriers they need to address in motivating consumers to engage with and learn about managing money better. Consistent with the breadth and depth of the research, the findings also have broad application across a range of stakeholder groups. As a result, they have been widely received with interest and enthusiasm, to the extent that some groups have decided not to pursue their own research projects, but to draw upon the wealth of valuable and unique information to be found in the Foundation's research⁵.

Addressing structural barriers

The Foundation's work in the education sector has focussed on addressing key structural barriers to improved financial literacy. The essential elements are:

- *National, systemic reform* – The Foundation has focussed on promoting national, systemic reform in the education system that will benefit all students.
- *National Consumer and Financial Literacy Framework* – In 2005, the Foundation worked with Australia's eight state and territory education systems, the Catholic and Independent education sector, the national Department of Education, Science and Training and state and territory departments of fair trading to develop the *National Consumer and Financial Literacy Framework* (the Framework). Through this nationally agreed Framework, Australian school students will start to receive financial literacy education in their compulsory years at school from 2008. The Framework provides guidance to states and territories in the development of their curricula and sets out a consistent national approach to

⁵ For further information, see www.understandingmoney.gov.au/report/. See also *current priorities* for information regarding the Financial literacy – women understanding money report.

integrate financial literacy across the curriculum in the compulsory years of schooling from Kindergarten to Year 10. It builds levels of knowledge and understanding, competence, enterprise and responsibility that will provide students with a sound basis for making financial decisions as adults⁶.

- *Professional development of teachers* –The 2005 agreement to the Framework did not, of itself, guarantee the delivery of financial literacy education in schools: it was recognised that teachers would require support in acquiring the knowledge and skills to deliver effective financial literacy education; and schools would require assistance in delivering professional development opportunities.

In 2006, the Foundation, with the support of all Directors-General of Education and the Catholic and Independent school systems, initiated development of a National Consumer and Financial Literacy Professional Learning Strategy (the Professional Learning Strategy) to provide guidance and support to all education systems in the delivery of professional development opportunities to teachers. The Professional Learning Strategy was completed and agreed in late 2007. The Strategy aims to develop in teachers the knowledge, understanding, skills and values they need to deliver consumer and financial literacy in schools.

In June 2008 the Professional Learning Strategy will move into the implementation phase, with teachers across Australia being trained to deliver consumer and financial literacy to their students through the compulsory years of schooling.

Professional learning will be supported by a Professional Learning Package designed to illustrate innovative ways of integrating consumer and financial literacy through real life contexts into core curriculum areas. The package contains support materials for teachers and a website⁷, scheduled to be live in June 2008.

Finally, in accordance with its general approach to partnerships, the Foundation is scoping the potential for promoting system-wide and school-based partnerships with parents, community and business as a means of ensuring the sustainability of financial literacy in the curriculum.

- *Promotion of quality education materials* – Consistent with its approach to promoting national, systemic reform in the delivery of financial literacy education, the Foundation promotes the use of quality materials and, rather than producing education resources, it supports the development of a competitive market for quality resources. As part of this, the Foundation has developed education and training pages on the *Understanding Money* website that are unique in providing educators, trainers and other professionals with efficient access to a trusted source of education materials assured to meet specified quality standards.

The pages function as a filter to promote efficiency in linking providers with those materials. They are not intended to provide access to the entire market of financial literacy education materials, which is of variable quality.

⁶ For further information about the framework visit www.mceetya.edu.au/mceetya/default.asp?id=14429.

⁷ <http://www.financialliteracy.edu.au>

Collaboration and partnerships

In addition to the Australian Government and state/territory government bodies that have a role to play in advancing financial literacy in Australia, many other participants are private sector or community bodies. The Foundation's role in promoting efficiency in the market of financial literacy services and resources is to encourage and facilitate collaboration and partnerships and, where appropriate, fill information gaps.

This collaborative approach does not mean that partners agree or are contracted to deliver the Foundation's financial literacy initiatives on its behalf, or that these initiatives would be implemented, progressed or continue to be provided successfully without the Foundation's involvement. The Foundation's resources are fully engaged in ensuring that its initiatives are delivered and in light of the Foundation's relatively small size, strategic engagement is essential to ensuring that maximum impact is achieved relative to available resources.

To this end, the Foundation's approach to collaboration and partnerships exists on several levels, key examples of which are as follows:

- Working collaboratively for mutually beneficial outcomes
 - Developing the *Understanding Money* website and handbook with the assistance of government and industry organisations, including: Abacus (Association of Australian Credit Unions and Mutual Building Societies); Association of Superannuation Funds of Australia; Australian Bankers Association; Australian Securities and Investments Commission; Centrelink; Department of Families, Housing, Community Services and Indigenous Affairs; Financial Services Institute of Australia; Insolvency and Trustee Service of Australia; Insurance Council of Australia; Investment and Financial Services Association; National Insurance Brokers Association; Australian Stock Exchange; CPA Australia; Financial Planning Association of Australia; and the Institute of Chartered Accountants in Australia.
 - Establishing the Educators and Trainers Network to assist educators, human resource professionals and resource developers to provide quality financial literacy education and training. The primary functions of the Network are to promote the development and use of quality education materials, give exposure to innovative financial literacy programs and create an interactive community of practice, rather than to promote Foundation initiatives. Therefore, while the Network has around 700 members, membership is voluntary and generally of direct interest and benefit to professionals in the financial literacy education field. The Network newsletter is also available to a wider audience on the *Understanding Money* website.
 - Publishing the *Understanding Money Update*, an electronic newsletter that provides information to government, industry, education and community sector stakeholders on how the Foundation is tracking in its priority areas and encourage information sharing and collaboration. There are just over 200 subscribers to the *Update*, and again, subscription is voluntary and relevant to individuals and organisations with a direct interest in financial literacy. The *Update* is also available to a wider audience on the *Understanding Money* website.
- Advancing financial literacy through national agendas

- Initiating, leading and coordinating work with government, Catholic and Independent school sectors, and the Department of Education, Employment and Workplace Relations in delivering the National Consumer and Financial Literacy Framework and the National Professional Learning Strategy.
- Developing national and strategic responses to advancing financial literacy
 - Initiating work with the Curriculum Corporation and Innovation and Business Skills Australia, the Industry Skills Council for the business and financial services sector, in assessing materials in accordance with the Foundation’s *Essential Elements Financial Literacy Assessment Guidelines*.
 - Developing and evaluating a pilot program with the Master Builders Association (MBA) to introduce financial literacy training to cadets, apprentices and the MBA membership nationally.
 - Working directly with Australian Technical Colleges to build financial literacy into Years 11 and 12 curriculum.
- Responding to identified needs
 - Developing case studies on workplace financial literacy with ANZ, Australia Post, Commonwealth Bank of Australia, Flight Centre, QIC, Unilever Super and Westpac. The case studies were the basis for the *Understanding money: Financial literacy in the workplace* booklet and website pages produced and published by the Foundation to assist employers interested in providing financial literacy education to employees. There has been strong demand for the booklet from businesses, industry associations and community groups.
 - Working with providers of Indigenous financial literacy programs and resources to develop good practice guidelines, *Understanding money: Good practice in developing financial literacy initiatives with Indigenous Australians*. The National Indigenous Money Management Agenda identified the need for good practice principles as part of a suite of actions required to improve Indigenous Australians’ financial literacy and access to banking and financial services. The booklet, which lists good practice principles for Indigenous financial literacy and key programs and resources, was written and produced by the Foundation to encourage consideration and discussion about implementing money management initiatives with Indigenous Australians, and provide guidance to people and organisations that are delivering financial literacy initiatives with Indigenous Australians. The guidelines have been well-received, with demand coming from a range of government, private sector and community organisations working to advance the financial literacy of Indigenous Australians.
 - Indigenous Australians will also have the opportunity to learn about financial literacy through the school system. The National Professional Learning Strategy to support financial literacy teaching in schools will take into account the needs of teachers in remote areas, particularly the Northern Territory.⁸

⁸ The Foundation’s initiatives with Indigenous Australians are part of Treasury’s *Reconciliation Action Plan*. Reconciliation Action Plans are an initiative of Reconciliation Australia. Reconciliation Australia has invited

- Responding to the identified financial literacy needs of women.
- Collaborating with providers of Government publications, such as *News for Seniors*, *VetAffairs* and *Defence Family Matters* to produce articles that raise awareness of financial literacy and its benefits. The Foundation has provided a number of articles for publication.
- Sharing research findings
 - Publishing the *Financial Literacy Resources Australia* database (September 2007), a centralised listing of financial literacy programs and resources available in Australia, compiled by the Foundation as a resource for service deliverers and resource developers, researchers and others with a direct interest in advancing financial literacy education. The database will help inform the development of new financial literacy programs and resources by identifying gaps and overlaps, and facilitate collaboration between organisations that want to use or develop programs and resources. It will be particularly useful for organisations that have limited resources to search for programs and resources available, or that are new to the financial literacy field. These include multicultural organisations seeking resources in languages other than English, and community groups that provide seminars and financial counselling services.
 - Publishing *Financial literacy – Australians understanding money* (September 2007), a major research report on the Foundation’s survey of 7,500 Australians aged 12 to 75 and our attitudes to money: how confident we are and how we behave when it comes to managing our money. The report will be of assistance to financial literacy education service providers and resource developers in focussing financial literacy initiatives effectively to stimulate positive change.
 - Publishing *Financial literacy – Women understanding money* (April 2008), which builds on *Financial literacy – Australians understanding money* by examining the findings for women in greater details. See **Current Priorities** below.

Current Priorities

Current priorities for the Foundation are:

- **National Professional Learning Strategy:** The Strategy will support implementation of the National Consumer and Financial Literacy Framework by providing professional learning opportunities for teachers in 2008. Through the Framework, all government, Catholic and Independent schools sectors have agreed to financial literacy education for Kindergarten to Year 10 students from 2008 onwards. The Strategy is scheduled to be launched on 3 June 2008.
- **Financial literacy resource for women:** The Foundation responded to a recommendation of the House of Representatives Standing Committee on Economics, Finance and Public

Australian governments, businesses, peak bodies, non-government, Indigenous and community organisations to develop and pursue individual Reconciliation Action Plans. The overarching objective of all Reconciliation Action Plans is to close the 17-year life expectancy gap between Indigenous and non-Indigenous children by addressing the key areas of housing, health, education, training, employment, and relationships, respect and rights.

Administration that it work with the Office for Women to target programs to improve the financial literacy of women under the age of 40 with respect to superannuation. The *Women understanding money* financial literacy resource was launched on 3 April 2008. It is available on the *Understanding Money* website.

- **Financial literacy - Women understanding money report:** The Foundation also launched the *Financial literacy - Women understanding money* report on 3 April 2008. This report builds on the findings of its 2007 research report, *Financial literacy – Australians understanding money*, by examining the responses of 4,138 women aged 18 to 75 in relation to their self-assessed ability, understanding, attitudes and behaviour when it comes to using and managing money. The report complements the women’s financial literacy resource, with clear links between the findings and the superannuation focus of the resource. The report is available on the *Understanding Money* website.
- **Workplace financial literacy strategy:** Over the first half of 2008, the Foundation will develop a strategy to encourage and facilitate workplace financial literacy initiatives by supporting both employers and employees in accessing quality learning opportunities and resources that meet their needs.
- **Further education strategy:** Over the first half of 2008, the Foundation is developing a multi-tiered strategy for promoting financial literacy programs through universities including pilot projects and incorporation of the Framework in teacher training education courses.

Advisory Board

The Foundation’s Advisory Board provides independent and strategic guidance on financial literacy issues. Members are appointed in their own right, rather than as representatives of particular organisations. Current membership is:

Paul Clitheroe – Chair (Executive Director, ipac securities)

Jeremy Duffield (Managing Director, Vanguard Australia)

Craig Dunn (CEO, AMP)

Linda Elkins (Managing Director, Russell Superannuation)

Elaine Henry (CEO, Smith Family)

Peter Kell (CEO, Choice)

Kerrie Kelly (Executive Director, Insurance Council of Australia)

Margaret Kilby (Financial counsellor and financial educator)

John McFarlane (former CEO, ANZ)

Further Information

For further information about the Foundation and the *Understanding Money* initiative, visit <http://www.understandingmoney.gov.au>

C- New Zealand Gets Sorted on Financial Education

Diana Crossan, Retirement Commission, New Zealand

New Zealand in context

The population of New Zealand is just over 4 million. Population similar to Ireland, Singapore and Los Angeles. Area of New Zealand equivalent to the United Kingdom, Italy and Japan.

Retirement Commission in context

How did the Retirement Commission come about and why the focus on financial education? In the 1990s New Zealand had just two pillars regarding retirement income – those of private provision and public provision:

There was no government supported saving: no tax breaks or other government incentives. The New Zealand Government decided that if there were no incentives, they had to support people in making their own financial decisions therefore financial education was needed. So in 1993 the Todd Task Force was set up. The Task Force recommended that a Retirement Commission be established and this is where we began ...

Initially the Retirement Commission focussed on retirement and the life stages leading up to retirement. This information was available to the public in the form of printed brochures. In 2001, the decision was made to move from print material to a website – Sorted.org.nz

Sorted.org.nz

We've had over four and a half million visitors to the award-winning website. The number of visitors totals more than the population of New Zealand. To date, 14 million calculations have been made over 32 different calculators – mortgage calculators, savings calculators, budget calculators. It's consistently in the Top 5 government websites in New Zealand

But Sorted is not just a website ...

We have complementary printed material that reflects the content of Sorted: brochures which:

- can be ordered through the website
- are distributed through direct mail campaigns
- available from places, for example Citizens Advice Bureaux and libraries

We run an annual television series with an average audience of 10% of the population per episode. It's the best free independent financial website in the world. Even though we know it's the best website in the world we still need to promote it.

You won't understand the accents but I want to show you two advertisements: one for children - we have a good section on Sorted for kids; one in which we used texting to get New Zealanders involved. Two television ads:

Adult Financial Knowledge Survey

The first survey was in 2005. This was a public/private partnership with a New Zealand bank helping to fund it. The survey at a glance:

- Data weighted to population by age, by gender, and by ethnicity
- Booster samples of Maori and Pacific people to ensure statistically significant results for these groups
- Survey questions ranged from whether there are interest-free days on credit cards, to the definition of 'equity' and 'net worth'.

The survey will take place every 4 years. Survey has highlighted need for financial education in New Zealand. This led to a move to develop a national strategy.

National Strategy for Financial Literacy

Timeline for the National Strategy for Financial Literacy:

- 2000-2005 Growing activities throughout country leading to tipping point.
- 2005-2006 National survey
- 2007 Development and launch of the draft strategy (including international research). This was an example of trying something differently. We pulled together a group of people - individuals and organisations across the public, private and voluntary sectors.
- March 2008 Submission process
- May 2008 Final copy
- Ongoing Annual Review via advisory group and Retirement Commission reporting to Parliament

New Zealand National Strategy for Financial Literacy

- Reaching people
 - Flexibility & timeliness
 - Cultural fit
 - Impartial & empowering
 - User-friendly & plain language
 - Financial Literacy is a life skill
- Extending delivery

- New Zealand Curriculum - eg in schools we have developed a Personal Financial Education Framework for Yrs1 to 10 students (5 to 16 year olds) and are moving towards embedding it into the Curriculum. We've also carried out a Children's Knowledge Survey.
- Professional development & resources for teachers
- Community partnerships
- Workplace partnerships
- Pacific peoples – tailoring & cultural fit
- Māori – reaching whānau
- Sharing what works Research – what works long-term
 - Evaluation framework & guidance
 - Linking people & resources
 - Database of financial education providers – to become interactive
 - Financial Knowledge Survey 2009

So in summary and to give you a taste of home ...

Summary

Retirement Commission

- Financial Education: 5 years to 95 years.
- “Sorted” materials

Adult Financial Knowledge Survey

- 4-yearly
- Monitoring changes in financial knowledge over time

National Strategy for Financial Literacy

- Public/Private
- “New Zealand Inc”

D- Taking Ownership of the Future: The National Strategy for Financial Literacy

Dan Iannicola, Jr., Treasury Deputy Assistant Secretary for Financial Education and Executive Director of the President's Advisory Council on Financial Literacy, United States

Today's increasingly-complex financial services market offers consumers a vast array of products, services, and providers to choose from to meet their financial needs. While this degree of choice provides consumers with a great number of options, it also requires that they be equipped with the information, knowledge, and skills to evaluate the options and identify those that best suit their needs and circumstances. This is especially the case for populations that have traditionally been underserved by our financial system. Financial education is also essential to help consumers understand how to prevent becoming involved in transactions that are financially destructive, how to avoid becoming victims of fraud, and how to exercise their consumer protection rights. Financial literacy can empower consumers to be better shoppers, allowing them to obtain goods and services at lower cost. This optimizes their household budgets, providing more opportunity to consume and save or invest. In addition, comprehensive education can help provide individuals with the financial knowledge necessary to create household budgets, initiate savings plans, manage debt, and make strategic investment decisions for their retirement or their children's education. Having these basic financial planning skills can help families to meet their near-term obligations and to maximize their longer-term financial well-being.

In 2003, Congress established the Financial Literacy and Education Commission (Commission) through the passage of the Financial Literacy and Education Improvement Act under Title V of the Fair and Accurate Credit Transactions Act of 2003 (P.L. 108-159). Congress designated the U.S. Department of Treasury's Office of Financial Education to lend its expertise and provide primary support to the Commission, which is chaired by the Secretary of the U.S. Department of the Treasury. In addition to the Department of the Treasury, the following Federal agencies are represented on the Commission: the Federal banking agencies (as defined in section 3 of the Federal Deposit Insurance Act)—Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of Thrift Supervision—the National Credit Union Administration, the Securities and Exchange Commission, each of the Departments of Education, Agriculture, Defense, Health and Human Services, Housing and Urban Development, Labor, and Veteran Affairs, the Federal Trade Commission, the General Services Administration, the Small Business Administration, the Social Security Administration, the Commodity Futures Trading Commission, and the Office of Personnel Management.

Congress charged the Commission to "improve the financial literacy and education of persons in the United States through the development of a national strategy to promote financial literacy and education".

In April 2006, the national strategy, entitled *Taking Ownership of the Future: The National Strategy for Financial Literacy* (National Strategy) was released. It examines a variety of topics – such as homeownership, credit management, retirement savings, multicultural populations – and describes the challenges and the solutions to each. Since 2004, the Commission has reviewed it annually and has made changes and recommendations as outlined in the statute.

Title V, Section 514 of the Fair and Accurate Credit Transactions Act of 2003 states that the National Strategy "shall provide for participation by state and local governments and private, nonprofit, and public institutions in the creation and implementation of such strategy". This mandate recognizes that both the private sector and the public sector are essential to improving financial

literacy in America. In adherence to this mandate, the Commission sought input from financial education providers and examined resources of the Federal government, state/local governments, non-profit organizations, academia, and the private sector. The development process is outlined below.

National Strategy Goals:

To make it easier to access and use helpful financial education information at the time it is needed, in a format most useful to the intended recipient.

To help consumers identify reliable and unbiased sources of information and equip them with the skills needed to evaluate the quality of information to use in choosing the products and services that are best suited for their needs and circumstances.

The Development Process:

Request for public comment. On August 2004, the Commission issued a notice in the *Federal Register* with a request for comments on the National Strategy. In response to that notice, more than 150 comments were received from private citizens, non-profit organizations, academia, Federal/state agencies, and others.

Commission held six sector-specific public meetings. The Commission conducted six sector-specific public meetings to gather more information from respondents to the August *Federal Register* Notice. These meetings were held in various locations in Washington, D.C. Many of the elements in the National Strategy are thoughts voiced by participants in those meetings.

Commission formed a working group. The Commission convened a working group of 13 Commission agencies to provide input into the National Strategy, drafted by the U.S. Department of the Treasury. Working group representatives met in several occasions to discuss internal timelines and the general structure of the document.

Content. The Treasury Department considered a variety of the non-governmental programs that it learned about in one of the following ways:

The programs were cited by a respondent to the *Federal Register* notice which requested public comment on financial education resources for the National Strategy. Or,

In response to outreach by the Treasury Department to promote a broad sampling of programs which were recommended by organizations.

Additionally, other non-governmental programs that are included in the National Strategy were found by the U.S. Department of the Treasury to contain at least six out of the following eight elements, which were developed by the U.S. Department of Treasury's Office of Financial Education in 2003:

1. The program content focuses on basic savings, credit management, home ownership and/or retirement planning.
2. The program content is tailored to its target audience, taking into account its language, culture, age and experience.

3. The program is offered through a local distribution channel that makes effective use of community resources and contacts.

4. The program follows up with participants to reinforce the message and ensure that participants are able to apply the skills taught.

5. The program establishes specific goals and uses performance measures to track progress toward meeting those goals.

6. The program demonstrates a positive impact on participants' attitudes, knowledge or behavior through testing, surveys or other objective evaluation.

7. The program can be easily replicated on a local, regional or national basis so as to have broad impact and sustainability.

8. The program is built to last as evidenced by factors such as continuing financial support, legislation backing or integration into an established course of instruction.

The purpose of including these non-governmental programs was to give specific, concrete examples of financial education efforts that specifically illustrate the issues discussed in each of the thirteen chapters.

Additionally, the Commission concluded that an effective national strategy must encompass four crucial areas, set forth below.

1. Building public awareness of available resources. Improved financial literacy among all Americans requires an increased public awareness of the issues, as well as the many state, local and national resources that are available for financial education. One theme that emerged from the Commission's sector-specific meetings was the realization that the Federal government must make its financial literacy resources more easily available. This is important in order to better leverage existing financial education resources and avoid overlap or duplication.

2. Developing tailored, targeted materials and dissemination strategies. Fortunately, a large variety of excellent financial education materials do exist. The MyMoney.gov, a Web site created by the Commission, catalogs a great deal of neutral, unbiased information aimed at educating consumers so that they can obtain materials that can assist them in making informed financial decisions. Rather than creating new teaching materials, these existing materials and resources can be tailored for particular audiences and distributed through those organizations and dissemination channels that are most trusted within individual communities.

Improving the financial literacy of Americans is not an action that occurs through a "one-size-fits-all" approach. People learn in many different ways, and many of us benefit from hearing and seeing educational messages repeated in many different ways on different occasions. Effective financial literacy and educational efforts require materials that are clearly understood by the intended audience. Tailored, targeted resources are important to reaching key demographics, including unbanked populations, multi-cultural and multi-lingual communities, geographically-remote communities, and consumers with special needs.

3. Tapping into public-private and private-private partnerships. Improving the nation's financial literacy is not a task that can be undertaken solely by the Federal government. To the contrary, the majority of financial education and skills-building activities are those currently led by non-federal

government and private-sector organizations. Community involvement can greatly enhance the effectiveness of collaborative resource development and dissemination efforts. Public-private and private-private partnerships therefore play an important role in equipping consumers with needed financial skills. Successful partnerships can efficiently reach key audiences with high-quality, unbiased information. These partnerships can highlight the local successes of financial literacy efforts and boost local enrollment in and access to education programs. Partnerships are valuable components to any public awareness effort initiated by the Commission, and they are a key part of the National Strategy to improve financial literacy.

4. Research and Evaluation of Financial Education Programs. While many excellent financial education efforts are ongoing throughout the nation, a theme repeatedly sounded in public comment letters and during the Commission's sector-specific meetings is that a systematic evaluation method of financial literacy programs does not exist. A broad and deep base of research on financial education will assist policy makers, as well as public and private sector providers of financial education, improve the effectiveness of their work on financial literacy. While some good research has been conducted, more can be done. From research comes a shared body of knowledge on how to best inform and educate different and varied constituencies on financial education topics. Such research is essential in developing and replicating programs that are proven to achieve results and to ensure the efficient use of resources.

Ideally, financial education programs would strive to incorporate findings from academic research that utilize both qualitative and quantitative measures to assess the effectiveness of financial education programs. For consumers, these data will offer confidence about programs that work; for educators, the data will offer guidelines for developing evidence-based, quality materials; and for funders of financial education, research provides assurance of the optimization of resources.

Launch. Before the launch, the Commission enlisted the support of elected officials, business leaders, non-profit organizations, the education community, and local community leaders to assist in the promotion and distribution of the National Strategy. Subsequently, the Commission conducted a series of rollout activities which were designed to promote the National Strategy in key markets. The rollout plan was designed to address the topics in the National Strategy while visiting diverse markets throughout the United States. All the activities were open press.

Implementation. As part of the National Strategy, Treasury's Office of Financial Education partnered with other Federal agencies to increase financial literacy by implementing the following initiatives:

- Hosting a series of conferences with other Commission-member agencies.
- Convening a series of roundtables addressing different ethnic populations and topics.
- Conducting a credit literacy media campaign to educate consumers.
- Raising discussions on integrating financial education into school curriculum and enhancing teacher training programs.
- Convening an international dialogue on financial education to discuss recent developments and successful strategies for improving financial literacy.

Conclusion

The United States is not the only country in the world to be engaged in a serious analysis of the financial literacy and educational needs of its citizens. Virtually every other nation faces the same challenge to increase the financial knowledge and skill set of citizens to enable them to make better financial decisions and avoid fraud.

Through the implementation of the National Strategy, the U.S. Department of the Treasury along with the Commission are working to improve financial literacy levels in the United States. Reaching the goal of a financially educated population will take time; therefore it is important to continue a dialog with other nations in an effort to learn from their efforts.

SESSION II- DIVERSE APPROACHES

Chair: Ursula Menke, Commissioner, Financial Consumer Agency of Canada, Canada

A- Jeanne Hogarth, Manager for the Consumer Education and Research Section, Division of Consumer and Community Affairs, Federal Reserve Board, **United States**

B- Annamaria Lusardi, Professor, Dartmouth College/Harvard Business School, **United States**

C- Alison O'Connell, OECD Consultant on Methodology to Evaluate Financial Education Programs, **New Zealand**

Policy Conclusions of the Chair

- Governments need to work with private and voluntary sectors to provide better information to consumers so that consumer can make informed decisions.
- We need to look at financial education programs from a micro level as well as at a macro level. On a micro level, how effective is the program versus the objectives of the program? In order to ensure effectiveness, evaluation of financial literacy programs is essential to improving program delivery and increasing consumer financial literacy knowledge levels. Such evaluation programs must be robust.
- At the macro level, how well does it fit in with government policy?

Ursula Menke, Introductory Remarks

- The conference led off with a big-picture look at financial literacy, its relevance and some of the broad strategies that have been created to address it. In this session, we're shining the spotlight on specific tools – from the leading-edge to the tried-and-true – that have been used to help financial consumers make informed decisions.
- What techniques are available? Which have proven to be successful? And how are regulators and governments delivering on their commitments?
- Arguably, when it comes to elevating financial acumen, our jobs are tougher than ever. On the one hand, we have the most sophisticated technologies at our fingertips, making the delivery of information much easier than in the past. Yet reaching, engaging and educating people remains a Herculean task.
- How do regulators and educators keep pace with financial innovation and change, which has been unfolding at a dizzying pace, to ensure the learning resources we deliver reflect the current marketplace?
- Another issue is accessibility. How can we make sure information is accessible to all groups and crafted in plain language.
- Plus, there's the added challenge of trying to make financial messaging resonate with consumers – who are as diverse as the financial products and services available to them. How do we present content in ways that will grab and maintain the attention of each target audience, from tech-savvy youth to time-strapped professionals to the elderly?
- In my view, we shouldn't be naïve about the fact that financial discourse isn't exactly riveting for most people. It's a multi-channel, multi-media, fast-paced world, and there are lots of voices competing for the citizen's attention. People are constantly inundated by offers for products to buy, worthy causes to support, or ways to change their behaviour for the better. There are only so many minutes in the day, and getting on the radar is a challenge.
- So how do we help consumers to a higher level of knowledge and comfort on money and financial matters? How do we get people interested in sound financial decision-making and understanding the consequences of poor financial choices?
- These important themes will underlie the discussion.
- In the context of Canada, advancing the financial capability of Canadians is a major priority for government. In fact, the Financial Consumer Agency of Canada was created in 2001 with that vital mission in mind. Over the years, we've developed a growing family of tools – tip sheets and brochures, forums and outreach events, and more.
- Building on this foundation, we recently launched a major strategy, supported by government funding, which will see us multiply our financial literacy efforts. A cornerstone of our approach is nation-wide cooperation and partnership-building, particularly with existing successful programs.

- As an example, we've teamed up with British Columbia, Canada's westernmost province, to develop a Financial Life Skills program. It's modeled on an award-winning curriculum that the province has used since 2004 to help students prepare for the financial world they'll face when they leave high school. We're adapting the program for use across the country, and will be delivering it online in the coming school year.
- Good partnerships like this can have tremendous impact. I believe it's vital for regulators to act in a collaborative way with the various organizations that support the same goals and have direct dealings with consumers at the grass-roots level. Community agencies, for instance, are uniquely placed to reach and respond to the hardest-to-serve and most disadvantaged groups of citizens, those who are likely most at risk when it comes to financial capability.
- Important too is that we share and pool our expertise with other regulators and experts in the field to become even more effective. This symposium is one important channel for us to do just that.

A- Jeanne Hogarth, Manager for the Consumer Education and Research Section, Division of Consumer and Community Affairs, Federal Reserve Board, United States⁹

The Federal Reserve is the central bank of the United States and a financial regulator. The Federal Reserve writes the regulations, including consumer protection regulations. In the U.S., because the Federal Reserve writes the consumer protection regulations, it also provides consumer education and outreach.

Regulators have long used disclosure as a tool for getting key financial information into consumers' hands. The goal for this presentation is to discuss some of the strengths and limitations of disclosures as a tool.

There are tremendous market changes and market complexity facing consumers today and as a tool, disclosures have to reflect what is going on in the marketplace and what consumers need to know about these changes. This discussion will focus on the credit card disclosures being developed by the Federal Reserve. It should also be noted that the U.S. credit card market may be very different than it is in other countries, and thus it is difficult to generalize the U.S. disclosure strategy to other markets.

The U.S. has a robust credit reporting system. Credit card companies may access credit reports to examine how risky a consumer is, and rather than denying credit to the consumer, they may offer credit at a higher price. The result is a system of risk-based pricing and issues of subprime, or less than prime, pricing in our credit card markets. In addition, in the U.S., credit reports can be used by insurance companies in their pricing and by prospective employers during the hiring process.

The Federal Reserve Board's disclosure strategy takes into account not only interest rate adjustments but also fees. Fees have become an important revenue stream for credit card companies and consumers have additional information about fees that they have to process in making credit decisions. Interest rates and balance calculations are intertwined; there are different balance calculation methods that credit card companies use and consumers need to be aware of.

Payment allocation is another issue for consumer disclosures. In the U.S., a consumer can have one interest rate for purchases of goods and services, a different one for balance transfers, and a third for cash advances. When an individual makes a credit card payment, the question becomes which one of those debts is the payment applied to?

Disclosure does not happen in a vacuum. Special attention must be given to the political structure and the Congressional priorities in the United States at the time; for example, subprime and predatory lending, credit card practices, and strengthening consumer protection are all on the minds of Congress. In the spirit of strengthening consumer protection, the Federal Reserve Board has proposed some substantive rules and prohibitions and will be using those as a complement to disclosure. It should be noted that disclosure is an important tool, but it is not the only tool.

What does this mean for regulators? Disclosures must be designed to be effective, easy to understand, useful, neutral, and comparable. This requires a combination of layout and language. For disclosures to be effective, consumers have to be exposed to them, pay attention to them, comprehend them, and understand them. Consumers have to remember and use this information in decision-making.

⁹ This summary has been extracted from the transcript of the OECD-US Treasury International Conference on Financial Education, and reviewed by the author.

Since 1995, the Federal Reserve Board has used consumer testing to help develop disclosures. Hearing from “real” consumers helps improve the effectiveness of disclosures. Over the years, the Board has used focus groups, one-on-one testing and interviews, and quantitative validation via consumer surveys.

In designing disclosures, the Board is guided by the key question, “What do we want consumers to do?”. In the action steps for credit card disclosures, the objective is to have consumers pay their bills on time, to make more than the minimum payment, and to avoid unnecessary fees. In solicitations for new credit cards, consumers should be able to compare credit card offers, to understand the multiple interest rates that they were facing on their credit cards, and to understand the fee structure.

The Federal Reserve has tested and proscribed a standard format as part of its disclosure scheme with the primary objective of getting consumers to pay their bills on time. The scheme advises credit card companies put the key information in the upper right-hand corner of disclosure documents; specifically, the payment date and the time that it's due, information about a late payment warning and the consequence of not paying the bill on time.

The Federal Reserve is also creating a minimum payment calculator on its website that will be launched at the end of 2008 where consumers can go online and inquire, "If my bill is X and my interest rate is Y, how long will that take me to pay off my credit card bill if I only make minimum payments?". The objective is to have consumers avoid unnecessary fees by highlighting the fees that consumers are paying on the bill.

In addition, the Federal Reserve’s proposed disclosure scheme requires that the fees on the bill be itemized and consumers be presented with a year-to-date total. Research by John Driscoll, a Federal Reserve economist, Sumit Agarwal from the Chicago Reserve Bank and David Laibson from Harvard, shows that consumers who pay a late fee or an avoidable fee in month one are only 40 percent as likely to pay another late fee in month two. Further, there is a learning effect by paying a late fee and this learning effect tends to dissipate over a period of nine months.

Another objective of the Federal Reserve is to make consumers aware of changes on their bill. In a simulated testing situation, we found that consumers only attend to the bill and disregard handouts that are mailed along with the bill. Hence, the scheme requires disclosure information be presented on the middle of the front page of their bill, where important changes to the account terms are highlighted.

With respect to solicitations, consumers should be able to compare offers, understand interest rates, and understand fee structures. The goal is to have consumers be able to compare information across standardized boxes, with special attention attributed to multiple interest rates: for goods and services, balance transfers, cash advances and penalties.

The Fed has proposed a new rule that will have credit card companies allocate payments in a way that is favorable to consumers. That means that credit card companies have to allocate payments to either the highest interest balance first, prorate the payment across the different types of balances, or make equal payments across the types of balances that consumers have. The new rule is that fees (1) substantively cannot be more than 50 percent of the credit limit and (2) if they are more than 50 percent of the credit limit, only 25 percent can be billed in the first month and the balance has to be prorated across the remaining 11 months.

The Federal Reserve also has proposed that credit card companies to place the Federal Reserve website on credit card solicitations. The objective is to connect consumers with more information than

can be put into a disclosure. Linking consumers to other relevant information is a good complement to disclosure statements.

In addition to effective disclosures, consumers also need education, access to counseling, coaching, and advice. Additional areas of interest include taking into account different audiences (i.e., youth and adults), different topics (i.e., credit, savings and general money management), and stages of behavior change – as some consumers are just becoming aware of their financial issues and preparing to make changes and take action. Finally, different learning styles need to be taken into account; for example audio learners, visual learners, and kinesthetic learners. The combination of information through disclosures, education, and access to personalized advice can go a long way toward helping consumers become financially secure.

B- Increasing the Effectiveness of Financial Education in the Workplace

Annamaria Lusardi¹⁰, Professor, Dartmouth College/Harvard Business School, United States

More than ever before, individuals are in charge of their own financial security after retirement. With the shift from defined benefit to defined contribution pension plans that has occurred over the past twenty years, individuals increasingly have to decide how much to save and how to allocate their pension wealth. The necessary decisions are daunting and are made more difficult by the increased complexity of financial instruments; investors have to deal with a vast array of new and sophisticated financial products. Saving decisions now require not only that individuals be informed about their pensions, but also that they be knowledgeable about finance and economics.

Yet, there is mounting evidence that people are unfamiliar with even the most basic economic concepts. Throughout the book I edited last year and in many papers I have written in collaboration with other researchers, evidence is shown of widespread financial illiteracy in the United States. Older workers display little knowledge of the power of interest compounding, the effects of inflation, and the workings of risk diversification.¹¹ Even among individuals in their prime earning years, such as Early Baby Boomers, who were 51–56 years old in 2004, there is evidence of low numeracy and limited understanding of interest compounding. Knowledge of more advanced financial concepts, such as the difference between bonds and stocks, the workings of mutual funds, and basic asset pricing is even scarcer. These findings are not only widespread, but are particularly severe among specific demographic groups, such as women, those with low education and low income, and African-Americans and Hispanics.¹² Individuals also display low *debt literacy*; only a little more than one-third of respondents in a representative sample of the U.S. population can figure out how quickly debt can grow when borrowing at an interest rate of 20 percent. Similarly, only 36 percent know how to eliminate credit card debt by making small payments over time, and a meager 7 percent are able to correctly pick the more advantageous method of payment out of two options.¹³ Finally, many individuals participating in customized surveys report that not having enough knowledge about finance/investing represents one of the most difficult elements of their saving decisions. Consistent with this fact, many individuals consider themselves simple investors.¹⁴

Lack of information about pensions—one of the critical components of retirement wealth—is also widespread. When comparing workers’ and employers’ reports about pensions, Gustman, Steinmeier, and Tabatabai (2008) find that close to half of older workers were not able to correctly identify their pension plan type. Workers misreport their pension plan type because they do not understand their pensions well, and today’s workers need—at minimum—an adequate level of

¹⁰ Annamaria Lusardi is professor of Economics at Dartmouth College and visiting scholar at Harvard Business School. Part of this article draws from the book she edited, “Overcoming the saving slump: How to increase the effectiveness of financial education and saving programs” (University of Chicago Press), and the article “Household saving behavior: The role of financial literacy, information and financial education programs,” written for the conference and conference volume “Implications of Behavioral Economics for Economic Policy” (Federal Reserve Bank of Boston, September 27–28, 2007). She would like to thank participants to the U.S. International Conference on Financial Education, Washington, D.C., for their comments and Harvard Business School for its hospitality while writing this paper.

¹¹ See Lusardi and Mitchell (2006).

¹² For more detail, see Lusardi and Mitchell (2007a, 2008, 2008b) and Lusardi (2007).

¹³ See Lusardi and Tufano (2008).

¹⁴ See Lusardi, Keller, and Keller (2008)

understanding of pensions in order to be sure of funding them properly. Knowledge about Social Security is also scanty. As was noted in the Employee Benefit Research Institute report describing the findings from the 2007 Retirement Confidence Survey, even though it has been 24 years since legislation was passed that increased in increments the normal retirement age for Social Security, and despite 8 years of annual mailings of individual benefit statements from the Social Security Administration, only 18 percent of workers know the correct age at which they will be entitled to full Social Security benefits. Consistent with evidence of lack of information about major components of retirement wealth, research shows that many workers do not plan for retirement, even when they are only 5 to 10 years away from it. Lack of planning is not only widespread among older generations, but it is also present among current Baby Boomers.¹⁵

Lack of information and lack of financial literacy provide fertile ground for financial errors. Left to their own devices, employees may choose to invest their pension wealth in either too-conservative or too-aggressive assets. An analysis of portfolio allocation from a large sample of investors offers compelling evidence that portfolio allocation can be improved upon.¹⁶ Moreover, those who display low literacy are more likely to have problems with debt, are less likely to participate in the stock market, and less likely to plan for retirement.¹⁷ Those who do not plan, arrive at retirement with much less wealth than those who do plan.¹⁸

Financial education

Most large firms, particularly those with defined contribution pension plans, offer some form of financial or investment education program. The evidence on the effectiveness of these programs is, so far, rather mixed.¹⁹ There is evidence of some positive effect of financial education on savings and pensions, but the type of education seems to matter. For example, Bernheim and Garrett (2003) find that programs that rely on print media (newsletters, plan descriptions, etc.) have generally no effect on pension participation or contributions, even though the quality of financial information does matter (Clark and Schieber, 1998). Only a few studies find that those who attend a retirement seminar are much more likely to save and contribute to pensions.²⁰ Clearly, those who attend seminars are not necessarily a random group of workers. Because attendance is voluntary, it is likely that those who attend have a proclivity to save, and it is hard to disentangle whether it is seminars, per se, or simply the characteristics of seminar attendees that explain the higher savings of attendees that are shown in the empirical estimates. However, Bernheim and Garrett (2003) argue that seminars are often remedial, i.e., offered in firms where workers do little or no saving. In their work, they find that the effect of seminars is concentrated in the first two quartiles of wealth and decreases or disappears at higher values of wealth holdings, a finding difficult to rationalize simply by appealing to tastes for saving.

Lusardi (2004) uses data from the Health and Retirement Study and confirms the findings of Bernheim and Garrett (2003). Consistent with the fact that seminars are remedial, she finds that the effect of seminars is particularly strong for those at the bottom of the wealth distribution and for those

¹⁵ See Lusardi (1999, 2007) and Lusardi and Beeler (2007)

¹⁶ See Mottola and Utkus (2008).

¹⁷ See Lusardi and Tufano (2008), van Rooij, Lusardi, and Alessie (2007), and Lusardi and Mitchell (2006).

¹⁸ See Lusardi and Mitchell (2007a).

¹⁹ See Lusardi (2004) and Lusardi and Mitchell (2007b) for a review of the effectiveness of financial education programs.

²⁰ See Bernheim and Garrett (2003) and Lusardi (2004).

with low education. Estimated effects are sizable for the least wealthy, for whom attending seminars appears to increase financial wealth (a measure of retirement savings that excludes housing and business equity) by approximately 18 percent. Note also that seminars affect not only private wealth but also measures of wealth that include pensions and Social Security wealth, perhaps because seminars provide information about pensions and encourage workers to participate and contribute. This can be important because, as mentioned before, workers are often uninformed about their pensions. Additionally, seminars affect accumulation by changing not only how much people save but also how they invest their portfolios; for example, those who have attended seminars are more likely to hold stocks. Analysis by education groups confirms that those with low education and lower wealth respond to retirement seminars by purchasing more stocks, while there is no comparable effect of seminars on those with high education.²¹

While these studies were able to single out the effects of financial education, one should also note that a only small fraction of workers ever attend retirement seminars or work at firms that offer such seminars. Thus, many workers are left untouched by such initiatives.

Other papers find rather modest effects of education programs. Duflo and Saez (2003, 2004) investigate the effects of exposing employees of a large not-for-profit institution to a benefit fair. This study is notable for its rigorous methodology; a randomly chosen group of employees was given a monetary incentive (\$20) to attend a benefit fair, and their behavior was compared with that of a similar group in which individuals were not offered any incentives to attend the fair. This methodology overcomes the problem mentioned before that those who attend education programs may already be inclined to save. Findings from this study show that incentives to attend greatly increase participation in the fair. Those who were provided with a monetary incentive were more than five times as likely to attend than other employees. Interestingly, even those who were not offered an incentive but were in departments with employees who did receive such an incentive were three times as likely to attend, indicating that peer effects are at work in these types of decisions. After attending the fair, individuals who received an incentive to participate were significantly more likely to start contributing to a Tax Deferred Account retirement plan. However, the same was shown to be true for those individuals who did not receive the financial incentive but who worked in departments where other employees received an incentive, again suggesting that people may be highly influenced by the behavior of those around them.

In a series of papers, Clark and D'Ambrosio (2008) examined the effects of seminars offered by TIAA-CREF at a variety of institutions. The objective of the seminars was to provide financial information that would assist individuals in the retirement planning process. The authors' empirical analysis is based on information obtained via three surveys: participants completed a first survey prior to the start of the seminar, a second survey at the end of the seminar, and a third survey several months later. Respondents were asked whether they had changed their retirement age goals or revised their desired level of retirement income after the seminar.

After attending the seminar, several participants stated they intended to change their retirement goals and many revised their desired level of retirement income. Thus, the information provided in the seminars did have some effect on behavior. However, it was only a minority of participants who were affected by the seminars. Just 12 percent of seminar attendees reported changes in retirement age goals, and approximately 30 percent reported changes in retirement income goals. Moreover, intentions did not translate into actions. When interviewed several months later, many of those who had intended to make changes had not yet implemented them. Another conclusion of the study was

²¹ See Lusardi (2005).

that the effect of the seminar was rather different among demographic groups. For example, the study highlights rather pronounced gender differences in saving behavior. Before attending the seminars, women displayed less confidence in their ability to attain their retirement goals than men. But women were substantially more likely than men to increase their expected retirement age and to alter their retirement goals. Thus, evaluating the effects of seminars on the whole population of participants may understate its impact on specific groups.

It is not surprising that one retirement seminar does little to change behavior. Few surveys on the topic provide information on the number of seminars offered or the number that participants attended, but it seems that participants often attend only once or a handful of times (Clark and D'Ambrosio, 2008). But widespread financial illiteracy cannot be "cured" by a one-time benefit fair or a single seminar on financial economics. This is not because financial education is ineffective, but because these programs are too small with respect to the size of the problem they are trying to address. Evidence from financial education sessions offered in programs aimed to promote Individual Development Accounts (IDAs), which are subsidized savings accounts targeted at the poor, show that multiple education sessions are effective in stimulating saving (Schreiner and Sherraden, 2007).

Increasing the effectiveness of financial education programs

The evaluation of the programs implemented so far suggests that exposing workers to information or education sessions may be insufficient to stimulate behavior. As I have highlighted in most of my papers, saving is a complex decision and requires knowledge well beyond what most employees seem to possess. One way to help people save is to find ways to simplify saving decisions. This is the strategy analyzed by Choi, Laibson, and Madrian (2006). They study the effect of Quick Enrollment, a program that gives workers the option of enrolling in the employer-provided saving plan by opting into a preset default contribution rate and asset allocation. Unlike default options, where workers are automatically enrolled into a pensions plan, in this program workers have the choice to enroll or not, but the decision is much simplified as they do not have to decide at which rate to contribute or how to allocate their pension assets.

When new hires were exposed to the Quick Enrollment program, participation rates in 401(k) plans tripled, going from 5 percent to 19 percent in the first month of enrollment. When the program was offered to previously hired nonparticipants, participation increased by 10 to 20 percentage points. These are large increases, particularly if one considers that the preset default contribution rate was not particularly advantageous: the contribution rate in the most successful program was set at only 2 percent, with 50 percent of assets allocated to money market mutual funds and 50 percent allocated to a balanced fund. Moreover, Quick Enrollment is particularly popular among African-Americans and lower income workers who, as the research mentioned before shows, are less likely to be financially literate. Thus, changes in pension design can have a significant impact on participation. Most importantly, programs such as this can be implemented at a low cost.

The finding, noted earlier, that people have difficulty following through on planned actions further suggests that education alone may not be sufficient to influence behavior. Rather, it is important to give consumers the tools to change their behaviors. Another approach intended to simplify the decision to save and, in addition, help employees make an active choice is the one designed by Lusardi, Keller, and Keller (2008). They devised a planning aid to be distributed to new hires during employee orientation. The planning aid displays several critical features. First, it breaks down the process of enrollment in supplementary pensions into several small steps, describing to participants what they need to do to be able to enroll in a plan online. Moreover, it provides several pieces of information to help overcome identified barriers to saving, such as describing the low minimum amount of income employees can contribute (in addition to the maximum) and indicating

the default fund that the employer has chosen for them (a life-cycle fund). Finally, the planning aid contains pictures and messages designed to motivate participants to save.

The planning aid was designed after thorough data collection. The researchers devised a survey asking explicitly about barriers to saving, sources of financial advice, level of financial knowledge, and attractive features of a pension plan. Moreover, they conducted focus groups and in-depth interviews (with both employees and human resources administrators) to shed more light on the impediments to saving of employees at this institution. These data collection methods, which are common in the field of marketing, are well suited to capturing the wide heterogeneity that exists among individuals facing saving decisions. Even though the sample in this study is small, and hardly representative of the U.S. population, it displays findings that are consistent with the evidence described above. For example, many employees in this study stated that they consult only family and friends when making saving decisions. Close to 40 percent stated that they do not have enough knowledge about finance/investing, and close to 20 percent stated that they do not know where to start. Similar to the findings of Clark and D'Ambrosio (2008) and Choi, Laibson, and Madrian (2006), women were found to be more reactive to the saving program. The program was very successful; contribution rates to supplementary retirement accounts tripled after the introduction of the customized planning aid.

The planning aid was further supplemented with new methods of providing information and advice to employees. Given the evidence reported in previous studies of the importance of “peer effects” on saving and low levels of numeracy among employees, particularly among women and those with low income, videos were made available to employees. These videos provided testimonials of how other employees in the same institution overcame barriers to saving. They also provided implicit suggestions on how to save and how to invest retirement wealth. The targeted groups were women and low-income employees, and only employees in these two groups were shown in the videos.²²

This program highlights several important considerations. First, while economic incentives, such as employer matches or tax advantages may be useful, they do not exhaust the methods that can be employed to encourage people to save. In fact, given the identified lack of information and financial knowledge among the general population, there may exist other, more cost-effective, programs that can induce people to save. Second, employees are more prone to decision-making at specific times. As discussed before, many people do not plan for retirement even at an advanced age, and it may be very important to exploit “teachable moments”. For example, the start of a new job induces people to think about saving. Thus, it may be particularly beneficial to target initiatives to employees who are newly hired, as this is the group that is the most open to changes, since they are already in the process of making decisions regarding saving and retirement planning. Third, to be effective, programs have to recognize the many differences that exist among individuals, not only in terms of preferences and economic circumstances, but also in the level of knowledge, financial sophistication, and ability to carry through with plans. In other words, relying on “one-size-fits-all” principles can lead to rather ineffective programs. Note that a planning aid can work in conjunction with other saving mechanisms. In other words, a planning aid can supplement rather than substitute for existing (or new) initiatives to promote saving. Combined with other initiatives, planning aids can significantly enhance employees’ retirement security. Finally, this is not only an effective initiative but also one that is low-cost.

While the mixed evidence on financial education programs has led some to question whether it is worth offering these programs, the evidence gathered in this article shows that it is possible to increase

²² The videos are available on the following web site: http://www.dartmouth.edu/~hrs/benefits/saving_for_retirement.html

the effectiveness of financial education programs. The problems are many and the challenges are daunting, but programs can be designed to change saving behavior. We have a wealth of information to rely on, as we are increasingly understanding the variables at play in providing and promoting effective saving and financial education programs. That information should make effective financial education and improved saving increasingly possible as we move further into a very different pension landscape and a financial world of increased individual responsibility for financial well-being.

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C- Evaluating the Effectiveness of Financial Education Programmes

Alison O’Connell, OECD Consultant on Methodology to Evaluate Financial Education Programs, New Zealand (*See Report in Volume II*)

Policy makers in many countries are giving more attention to ‘financial literacy’ or ‘financial capability’. Funding for financial education programmes from governments and other agencies is increasing. The value for money of these programmes is likely to be increasingly questioned, so the need to evaluate the effectiveness of financial education will increase.

This paper reviews what is being done around the world to measure the effectiveness of many different types of financial education. It takes a broad sweep through academic and policy-related literature world-wide, focusing on those countries where reports on financial education have been prominent.

The paper finds that relatively little evaluation is currently taking place, and the evaluations made so far show mixed and inconclusive results. It is not clear whether this is a consequence of poor evaluation methods or poor programme design, or, that financial education works patchily. But it does mean that a positive impact from financial education has not been unambiguously proven; nor has a clear picture emerged of how effective different types of financial education could be.

Evaluation of financial education is inherently difficult, and the impact of any one programme can probably never be fully isolated. Nevertheless, this paper suggests that evaluating the effectiveness of financial education can and should be improved.

The paper begins to develop an approach to do this, including a Financial Education Evaluation (FEE) Framework which can be tailored for any programme in any country. This paper also suggests guidelines for governments and other public authorities to lead the way towards better evaluation of the benefits, costs and value for money of financial education.

GUEST SPEAKER

Martin J. Gruenberg, Vice Chairman, Federal Deposit Insurance Corporation and Chair of the Executive Council and President of the International Association of Deposit Insurers²³

Good afternoon and thank you André for that kind introduction. I would like to congratulate both André Laboul from the OECD and Dan Iannicola from the US Treasury for hosting this conference. There is a growing understanding that financial education is critical, to enhance the ability of individuals to manage their affairs successfully and as a vehicle for economic opportunity. It is a means for effective consumer protection, a critical component for financial stability – a dimension that is perhaps less appreciated. As a member of the Board of a deposit insurance agency, financial stability is, in a sense our first mission as far as the agency is concerned. A critical element for an effective deposit insurance system is to maintain financial stability and public confidence, and the basis for financial stability is financial education and financial literacy.

Financial literacy initiatives have been one of the highest priorities of the Federal Deposit Insurance Corporation (FDIC), particularly in the context of expanding access to mainstream financial institutions to the general population in the United States. Financial stability and its relationship to financial education and awareness is a critical element of the FDIC's mission. Recent developments on the international scene have underscored this and will be very important going forward as we try to deal with the international financial turmoil that we are experiencing today in financial markets.

The starting point of international awareness and sensitivity to this issue is linked to the recent events in the United Kingdom (UK), specifically concerning one of its large mortgage lenders, an institution called Northern Rock. It should be noted at the outset that whatever lessons the UK has learned, the United States learned in the 1980s when it had a large crisis in its savings and loan industry. The savings and loan crisis resulted in the failure of nearly 1,000 insured thrift institutions and the collapse of the deposit insurer for those institutions at a very large cost to taxpayers. The UK experience is mild in comparison, yet it has served to attract greater international attention – in no way suggesting that the US has any greater wisdom. Yet, the UK experience with Northern Rock was instructive.

Northern Rock was the fifth largest mortgage lender in the UK. It had assets of about 100 billion pounds, about 200 billion dollars, and because of its mortgage exposures, it had significant vulnerabilities. There was discussion among the UK authorities about whether to intervene and how. The public became aware of the problems of the institution, and because of the fears by the public about the potential failure of the institution, the institution experienced something that the UK really had not seen in over 100 years. There was a run on the bank.

Photographs at the FDIC from our Great Depression in the 1930s depict people lined up around failed institutions trying to get their money. That is what happened in the case of Northern Rock. People were lined up around the block trying to get their money out of the institution and part of the reason was an inadequate system of deposit insurance. The UK authorities had a system under which only the first 2,000 pounds of deposits were insured at 100 percent. From 2,000 pounds to 35,000, those deposits were covered only 90 percent. For example, if a depositor in that institution had 10,000 pounds in the bank, the first 2,000 were covered but the next 8,000 were only insured for 90 percent, which means that 800 pounds or \$1,600 were at risk if that institution should fail.

²³ This summary has been extracted from the transcript of the OECD-US Treasury International Conference on Financial Education and reviewed by the author.

In addition, the UK system had a very slow payout in the event of failure. It could take six months or more for a depositor to get their money to the extent that it was insured. It was that inadequate system, most observers believe, that at least contributed to the public reaction to the rumors about the institution. It is also recognized that among the shortcomings of the system was a lack of effort to inform the public generally, even about the existence of the system, much less than the specifics of its coverage. Now, the coverage itself was perhaps inadequate but if depositors did not even know the system exists, it is even more problematic.

The UK authorities presented with this crisis of public confidence in this institution went from a system of extremely limited coverage, to insuring all deposits at 100 percent in order to calm down the public. In addition, in an effort to stabilize the situation, the UK authorities provided \$50 billion of direct loans to try to assist the institution. When that support proved inadequate, the UK authorities had to take over the institution; today, the UK authorities own the institution and are managing it.

In a sense, Northern Rock was a worst-case scenario, at least in part prompted by what the authorities now recognize as an inadequate system of deposit insurance. The UK authorities are now moving quite forcefully to develop and adopt a series of reforms to strengthen the system, including expanded coverage, reliable funding, a system of prompt corrective action, and an aggressive effort to communicate and educate the public about their system of deposit insurance. In addition, UK reforms include establishing an independent bankruptcy authority to be able to close a failing institution and dispose of its assets or arrange its sale, which is not possible under current law.

In summary, a public that does not understand or is poorly informed is a public more susceptible to loss of confidence and to financial panic. The objective of international initiatives to improve financial education and literacy, in addition to individual empowerment, consumer protection and economic opportunity, is financial stability. The UK experience led directly to a very promising opportunity internationally in deposit insurance and it relates directly to public education and awareness.

In response to the general international financial turmoil that we are seeing in the financial markets today, the G7 finance ministers formed a working group of an organization based at the BIS in Basel, Switzerland. It is called the Financial Stability Forum and is made up of finance ministers and central bankers. Further, the G7 finance ministers asked this working group to develop a set of proposals to respond to recent developments.

Among the issues that this working group focused on -- in significant part because of this UK experience -- was deposit insurance. The International Association of Deposit Insurers (IADI) met with the working group and discussed what they might do. It was suggested that the working group consider in its report recommending and emphasizing the importance of effective deposit insurance systems to financial stability and recommending the development of an international set of core principles that countries could use as a guidepost for developing effective national systems of deposit insurance. The working group was quite responsive to that suggestion and invited the IADI to submit a draft set of core principles to the working group. Among the 20 core principles submitted to this international working group of the Financial Stability Forum, the most important was public awareness:

In order for a deposit insurance system to be effective, it is essential that the public be informed about the benefits and limitations of the deposit insurance system. The characteristics of the deposit insurance system should be publicized regularly to maintain and strengthen public confidence. All deposit insurers should promote public awareness about the deposit insurance system on an ongoing basis. The major goals of the public awareness program are for the deposit insurer to accomplish its

public policy objectives and enhance the effectiveness of the deposit insurance system through public education to promote the stability of the financial system. The objectives of the public awareness program should be clearly set out and consistent with the public policy objectives and mandate of a deposit insurer.

Recently, at a meeting of the G7 Ministers here in Washington, the Working Group released its final report. The final report has a section on deposit insurance where it recommends that authorities review and where necessary strengthen deposit insurance arrangements:

Events during the recent turmoil have illustrated the importance of effective depositor compensation arrangements in giving depositors confidence, thereby reducing the likelihood of a run on the bank and in supporting confidence in the financial system as a whole. Explicit and limited coverage deposit insurance system clarifies the authority's obligations to depositors, limits the uncertainty that arises from the scope of discretionary decisions, can promote public confidence, helps to contain the costs of resolving failed institutions and can provide countries with an orderly process for dealing with bank failures. To be credible and to minimize moral hazard, deposit insurance systems must be properly designed, well implemented and understood by the public.

The section of the final report on deposit insurance also recommends the development of an international set of core principles incorporating these ideas and references the draft core principles that the Association submitted. This is an important development as it elevates the international discussion on financial stability, both the importance of deposit insurance systems -- which was not as widely appreciated internationally until recent events. It also underscores the importance of public awareness -- and education for maintaining financial stability.

An important lesson of these recent developments is that a mission was not clear before, as well as the broader mission of improved financial education, improved financial literacy, public awareness and understanding of how the financial system works. Northern Rock was a powerful lesson and serves as an impetus to efforts to strengthen international cooperation with respect to financial education, elevate its priorities at the national level and around the world, and be a vehicle not only to individual opportunity and empowerment, but also to financial stability.

The FDIC is concerned about the issue of financial literacy and the broader issue of economic inclusion and expanding access to mainstream financial institutions to everybody in this country. The FDIC understands that perhaps the most important vehicle for accessing economic opportunity and self-improvement is access to credit that is appropriate to the financial situation of the individual and that is provided on a responsible basis. Gaining access to the financial mainstream is a challenge for millions of people in the United States and is a major issue internationally as well.

Financial literacy has been a longstanding priority of the FDIC. The FDIC has a widely recognized program -- MoneySmart. This financial education program was initially developed in 2001 to help bring low and moderate-income adults into the mainstream banking system and help them understand banking services, improve their money management skills, and build financial confidence. The MoneySmart curriculum is provided free of charge and it is now available in several languages, including Spanish, Chinese, Korean, Vietnamese and Russian. To reach as broad an audience as possible, the FDIC has collaborated with federal, state and local governments, national non-profit organizations, financial institutions, bank trade associations, and both community and consumer-based organizations. The FDIC has also initiated a MoneySmart for young adults program, which is designed to appeal to young people by using activities and examples that are age appropriate and relevant. Further, the FDIC has established relationships with public school systems around the country in an effort to disseminate the program.

In addition, the FDIC has conducted studies to try to evaluate the impact of financial education on the people who go through the MoneySmart program. A number of studies have shown that financial education efforts can foster positive changes in behaviors and better equip people to make appropriate financial decisions. Last year, the FDIC completed a multi-year study designed to measure the effectiveness of financial literacy training; specifically, training using the MoneySmart curriculum. The findings suggest that MoneySmart financial education training covering the basics of checking, saving, budgeting and credit, can positively change consumer behavior and improve financial confidence.

The FDIC appears to be getting tangible results from the MoneySmart program. Program participants have been shown to be more likely to open deposit accounts, save money in mainstream deposit accounts, use and adhere to a budget and have increased confidence in their financial abilities, as compared to non-participants. In addition, the FDIC has developed a national effort to expand access to insured financial institutions in the United States, identifying nine communities in different regions. In each of those communities, the FDIC has organized coalitions of local financial institutions, state and local public leaders, community organizations and academics, to identify the local challenges that inhibit people from gaining access to mainstream financial institutions and to develop local strategies to respond to them. This initiative is called the Alliance for Economic Inclusion. It has been operating for over a year now and will be expanded to additional communities around the country.

The response to the Alliance for Economic Inclusion in these communities has been very positive both from financial institutions and from local leaders. The Alliance's goals include expanding access to mainstream financial institutions so people do not have to rely on fringe financial institutions: the check cashers, the payday lenders, and the sub-prime mortgage lenders who offer higher cost financial services (often with far less responsible terms and subject to less stringent consumer protection regulations). As well, the Alliance provides meaningful access to insured financial institutions so that people can get affordable credit on responsible terms -- a critical challenge for this country and a major priority for the FDIC.

Finally, there is an important need for information in the United States on access to the banking system; specifically, who is unbanked or under-banked in the US. In this regard, the FDIC is now undertaking a national survey and is in the process of developing another. The first is a survey of over 1,300 financial institutions around the United States asking them what they do to expand access to their institutions to people who today either do not have an account or under-utilize the opportunities that insured financial institutions provide. This survey is pursuant to a congressional mandate from Congress that was contained in legislation recently passed.

In the second survey, the FDIC is working with the US Census Bureau to conduct the first national census survey of the unbanked in the United States. The FDIC hopes to launch the survey in January of next year. The survey aims to be a way to identify reliably -- on a national basis and regionally by state -- who is unbanked, why are they unbanked and what are their obstacles to gaining access to the financial mainstream. The FDIC hopes this survey will provide critical information that can serve as the basis of effective policy responses to this issue.

In closing, the issue of financial education in access to credit is an issue of international dimension that affects all countries in the world, developed countries and emerging markets. There is a great deal to be learned by exchanging experience and interacting with one another. It is an issue that should be raised in priority both at the national and the international level.

SESSION III- RETIREMENT SAVINGS: NEW REALITIES FOR CONSUMERS

Chair: Mr. D. Swarup, Chairman, Pension Fund Regulatory and Development Authority, India

A- Nicolas Blancher, Deputy Division Chief, Monetary and Capital Markets Department, **IMF**

B- Ambrogio Rinaldi, Chair of the Working Party on Private Pensions, OECD, and Director COVIP, Pension Funds Supervision Commission, **Italy**

C- Annika Sundén, Research Associate at the Center for Retirement Research at Boston College, Chief of the Research Unit at the Swedish Social Insurance Agency and OECD Consultant

D- Jeffrey Dominitz, Senior Economist, RAND, **United States**

Policy Conclusions of the Chair

- Financial education can make a big difference in the quality of life that individuals can afford and benefit the consumers of all ages and income levels.
- Low financial literacy levels often lead to a situation where savings are done primarily for meeting short and medium-term goals or for emergencies rather than for retirement income security.
- Financial education should complement not substitute financial prudential regulation and consumer protection.
- Defined Contribution plans require employees to not only bear investment risk but also to make financial decisions for which they are poorly prepared; thus the need for financial education.
- Insufficient long-term savings or asset misallocations as well as risk and uncertainties affecting ageing related liabilities represent potentially major challenges.
- Adequately designed and targeted financial education programs should aim to equip the individual to ask informed questions and understand potential outcomes.
- Automatic enrolment in pension plans with appropriate default mechanisms and opt out procedure should be encouraged.
- Public authorities should introduce regulatory and tax regimes that improve long-term household savings.
- Innovative market instruments are needed to facilitate the management of aging related risks for pension funds and insurance companies.
- Pension reforms around the world will increase individuals' need for information about pension plans as well as the need for general financial literacy. An important tool for information about

pensions is the annual statement. The example of ‘Swedish Orange Envelop’ was commended in this regard.

- Internet services could be an important tool to provide more comprehensive, individualized and relevant pension information services in the future.
- Disclosure norms for fees and expenses to plan fiduciaries and participants as well as to the regulator should be improved.
- Dedicated investors education and protection funds should be created through appropriate legislation.

Mr. D. Swarup, Introductory Remarks

OECD has conducted extensive work on financial education relating to pensions over the last several years, which culminated in 2008 with the adoption of OECD's recommendations on good practices for financial education relating to private pensions. These recommendations provide useful guidance and directions to policy makers, financial institutions and the general society to improve literacy and capability regarding pension and retirement issues.

Speakers before me have already brought out the felt need for improving financial education and literacy levels. All of us will agree that financial education can make a big difference in the quality of life that individuals can afford and benefit the consumers of all ages and income levels; provide individuals with basic tools for budgeting, help them to acquire the habit of savings with a view to ensuring that they enjoy a dignified and independent life after retirement.

Financial education is even more important for retirement savings and pensions as these are unique products with exceptionally long-term contracts covering all segments of the population, especially those with low general education levels and low income levels. This segment of the population has a particularly low risk-tolerance levels.

There is a worldwide trend of shifting from Defined Benefit and Defined Contribution plans involving individual choice; financial literacy assumes great significance in this regard.

India has one of the highest household saving rates in the world; however, financial savings rate is tiny with most of the household wealth allocated in non-financial assets.

Low financial literacy levels in India have led to a situation where savings are done primarily for meeting short and medium-term goals or anticipated emergencies rather than for old age income security.

Less than 5% of the earning population is preparing for retirement; more than 50% have not even thought of savings for retirement.

However, once the concept of new pension system (NPS) was introduced to the working population at large, there was great enthusiasm for savings for retirement. About 110 million people would like to join NPS immediately and start defined contribution to a regulated voluntary pension plan.

The expected first year contribution corpus is likely to be around US D 14 billion; by 2020, it is estimated to be over USD 300 billion.

A survey in India indicates that while rates of interest and risk factors are important, other factors also play a very significant role in individual financial decisions such as saving capacities and income levels, ability of evaluating product choices and performance, service providers and regulators, tax incentives as well as ease of market access.

The survey also reveals that there is a significant co-relation between general education levels and financial behaviour of individuals.

Financial literacy and education will, therefore, have to keep the above consideration in view while designing the financial education programmes.

Meanwhile, initiatives have been taken to provide adequate funds for financial literacy by creating dedicated investors education and protection funds through legislation.

Forums like this will be of immense help in arriving at the most effective and efficient way to concretize the future steps for spreading the message of savings and financial literacy.

A- Risk Transfer to Households and Long-Term Savings Challenge

Nicolas Blancher, Deputy Division Chief, Monetary and Capital Markets Department, IMF

As part of ongoing efforts to better understand the various challenges associated with macroeconomic and financial stability, the IMF has focused in recent years on the transfer or risk across financial systems. In a series of issues of its flagship publications, the Global Financial Stability Report, the IMF has analyzed such a flow of risks and the ability of various sub-sectors to manage them. While the condition or resiliency of systemically important institutions, most often banks, remains central to financial stability assessments, the analysis highlighted important changes in the flow of risks among a broader range of market participants, often as a result of policies intended to strengthen the financial resilience of a particular sub-sector. Sometimes, the flow of risk has been redirected to less monitored or measured sectors, like the household sector. This in turn has raised questions as to the potential magnitude of such risk transfer, the capacity of households to manage these risks, and related challenges for households and policymakers going forward. Such questions feature increasingly high on the policy agenda in a growing number of countries.

This paper aims to highlight some key challenges in these areas, including by describing the household sector changing risk profile, potential roles for government in helping to raise both public awareness of these challenges and household financial literacy, and roles for financial innovation and market solutions. While much of the material provided below derives from discussions with policymakers, regulators and market participants in G10 countries, its is and will likely be increasingly relevant to a broader set of countries.

1. Risk transfer to the household sector

Changing risk profile

A number of changes are having a material impact on the financial risk profile of the household sector. Households face additional risks as a result of adjustments in public benefits, which require households to provide a larger share of pension income from their own savings than in the past. In addition, risks traditionally managed by pension plans or financial institutions are flowing more directly to the household sector. For example, in many countries, the shares of insurance products in the form of unit-linked contracts and of defined contribution (as opposed to defined benefit) pension plans are growing, leading to a transfer of investment risks to individuals. Over time, reductions in public healthcare benefits can also be expected, as healthcare costs are rising in excess of inflation and are adding to budgetary pressures in many countries.

In effect, households have always been the ultimate holders of systemic risks and exposures (e.g., as shareholders, depositors, employees or taxpayers), even as these risks were traditionally intermediated in various ways by governments or private institutions. However, the above structural changes illustrate that going forward, households will becoming more directly exposed to a variety of financial risks than in the past, and responsible for managing them.

Such risks are numerous, reflecting the complexity of long-term savings challenges associated with the need to meet old-age liabilities. They consist in some combination of market risks (i.e., interest rate, equity and credit), inflation risk (e.g., reflecting benefit indexation), investment planning and reinvestment risk, and longevity risk (especially as public and private annuity income streams are reduced or eliminated). Indeed, the general uncertainties over investment returns and risks are

magnified over a long-term horizon, increasing the potential costs of systematic resource misallocations. Finally, the growing complexity and variety of retail products available also renders savings and investment decisions more difficult.

Households' risk management capacity

While households need to manage larger and more complex risks, most available survey information show a substantial lack of knowledge of households' own arrangements for retirement savings. For instance, in the Netherlands, 65 percent of households are unable to provide an estimate of their pension income upon retirement. In the U.K., 44 percent of the population reported a basic knowledge of pensions in 2004, down from 53 percent in 2000. In the U.S., 47 percent of workers who have not saved at all are confident that they will have enough for retirement. Many employees may also count on employer-provided benefits that are increasingly unavailable.

More broadly, experience suggests that households generally do not take a comprehensive approach to their long-term savings strategy, are slow to adjust their asset allocation as needed, and underestimate required level of savings and risks. In many countries, for example, a large share of household financial wealth remains invested in short-term savings vehicles, such as money market funds or even just bank deposits. Such asset allocation only preserves savings against inflation, and does not allow household to build sufficient financial wealth to meet expected retirement income needs. Such a "long-term investment underperformance risk" is likely to have increasingly visible impact, but is still often ignored.

Overall, the growing disconnect between the increased responsibility of households in making key long-term investment decisions for their old-age needs, and their limited capacity to manage the complex risks associated with such a responsibility, seems likely to grow further in the future. This highlights that taking action to address the adverse consequences of poor household financial literacy has become all the more urgent.

2. Raising public awareness

A first important step in addressing the above challenges is to raise household awareness. While reforms to reduce the role of the state in providing pension and other benefits have been accompanied by actions aimed at informing households about the implications of such reforms, the public debate on long-term savings obligations and risks for households is often still nascent, pointing to the need for further initiatives.

In the U.K., the authorities have been particularly active in communicating to the public with regard to these challenges. In 2004, the Pensions Commission Report reviewed the adequacy of private pension saving and issued a candid warning that many households are significantly undersaving. This report attracted wide publicity in the media and triggered a relatively broad-based public debate on long-term retirement and pension challenges. In Sweden, a comprehensive information campaign accompanied the introduction of a new public pension system a few years ago, and subsequent surveys showed that it had had a material impact on participants' understanding of the system.

Innovative ways to assess and communicate on the above challenges also include the design and development of forward-looking measures to assess the impact of changes in pension and welfare systems on households' wealth and income. The National Retirement Index (NRI) recently introduced in the United States is a good example of how complex risks associated with retirement saving can be presented relatively simply. The NRI identifies the population cohorts (by age and income) most "at

risk” of being unable to maintain their expected standard of living in retirement, and gauges the sensitivity of these exposures to changes in key parameters (such as the retirement age). Another example is the methodology developed by the Sveriges Riksbank to assess households’ financial margin relative to anticipated future obligations. This methodology also addresses future constraints and risks across income categories, taking into account potential benefit adjustments or economic shocks (e.g., a rise in interest costs and/or a decline in income).

3. Information versus education

Experience shows that greater availability of financial information cannot substitute for greater household financial literacy. Indeed, households often make limited use of such information when it is easily accessible, and increased disclosure of financial information to consumers does not necessarily result in improved financial management. Furthermore, the existence of a potential trade off between disclosure and transparency is confirmed by behavioral studies that have shown that an excess of information and choice (e.g., with regard to portfolio investment options) may tend to reduce the capacity of individuals to actually take financial decisions.

Public sector initiatives

Governments have an important role to play, and even interest in promoting financial education. Indeed, if financial literacy shortcomings are left unaddressed, governments may come under pressure to intervene directly in support of the household sector, either in the form of added public expenditure, re-regulation of certain products or services, or even to deal with waves of litigation.

An obvious role for governments is to strengthen basic financial education programs at school, and such efforts are underway in some countries. Broader government involvement in providing and/or coordinating financial education efforts has also been observed in many countries. In the United States, the Treasury established in 2002 an Office of Financial Education to coordinate the financial education efforts of other federal bodies, and more generally to identify and promote access to financial education tools. In the United Kingdom, the Financial Services Authority plays a key coordinating role and has developed proposals on improving financial capabilities across the full range of consumers’ life stages and financial decisions (e.g., schools, young adults, the workplace, families, retirement).

Another, relatively “low cost” role for governments is to support the development of data and tools required to identify population segments most at risk (e.g., see above). It is often difficult to obtain consistent data on both financial and nonfinancial balance sheet items for the household sector over an extended period of time. Even among those countries with relatively better aggregate data, timely panel data covering households of different age and income groups is limited.

Financial education objectives and programs

As noted, long-term saving for retirement involves complex decisions that are very challenging for most households. Key aspects to consider include: how much to save; uncertainties over ageing-related risks and long-term returns; the need to monitor and possibly adjust savings strategies; choosing between the variety of products available; how to structure pay-outs during retirement. Accordingly, the purpose of financial education should not be to define a single approach to saving and investment, but rather to equip individuals to ask informed questions and to understand the potential outcomes of their financial decisions.

The design of financial education programs has been the subject of increasing international attention in recent years. The OECD, in particular, launched a Financial Education Project in 2003 to review education programs across countries, and developed on this basis a set of good practices. Key issues to consider relate in particular to the focus of financial education programs (home ownership, savings, debt management, etc), the identification of target audiences, and the selection of most appropriate delivery channels. For example, while basic financial education is best provided in schools, long-term planning is needed for the middle aged, and consideration of payout strategies is likely to become a key focus during later working life.

Importantly, governments and the private sector have comparative advantages in the delivery of financial education. While, as noted, governments can promote financial education at school, the private sector may be better positioned to consider individuals' financial situations and concerns at various ages, and to provide tailored financial education and advice. In Japan, for example, investor education is often done by banks, taking advantage of their strong relationship with depositors, and using their branch offices to conduct seminars about new products. In the United States, employers often organize seminars to help employees evaluate their financial needs and investment options –and there is evidence that such seminars have a material impact on employee financial behavior (e.g., participation in 401(k) plans).

4. Private sector and financial innovation

Government incentives

In addition to their role in delivering financial education programs, governments can introduce frameworks and incentives to encourage more adequate long-term household savings and related market solutions. A simple and stable tax environment, for example, is likely to facilitate advanced planning and helps to overcome households' general inertia or risk aversion. While empirical evidence is mixed on whether tax incentives help raise overall household savings, they seem to play a positive in encouraging more stable and longer-term savings.

By supporting market solutions for better risk management by pension funds and insurance companies, governments may also help to increase the availability of various retail products for households. For example, interest has grown in recent years in the development of longevity instruments which may help life insurance companies to better manage longevity risk, and in turn to provide annuity products more easily to households. It is not clear today that governments should assume larger longevity risk exposures by issuing longevity bonds, especially in countries where the government is already heavily exposed to longevity risk through existing public pension liabilities. However, financial innovation may allow governments to play a catalytic role for the development of such markets and instruments in the future, for example by assuming only extreme longevity risk (the "toxic tail" risks) in a transitory and relatively cost-effective way.

Governments may also improve the incentives for financial advisers to better support the needs of households. The provision of quality financial advice should progress with that of financial education and many financial institutions have realized that it is also in their interest to help households better manage financial risks, and to provide sound advice when it comes to financial decisions and their implications. However, appropriateness of advice may be an issue, as financial advice is often or transaction based, and risks being focused on selling financial products. Greater transparency of commission and fee structures may thus be one priority action in this area.

New investment products for households

While financial institutions increasingly recognize the demand for better household risk management tools, financial innovation has allowed for a rapid development of savings and investment products and services for households in recent years. In particular:

- Life-cycle funds address changing risk profiles of individuals as they age by automatically adjusting asset allocations to a more conservative profile (i.e., increasing fixed-income investments). While such products still represent a relatively small portion of the overall market for retirement savings, they have expanded in the United States, Japan, and Europe in recent years, including sometimes as “default options” under self-directed pension plans.
- Structured products offer a variety of risk/return profiles, including capital or performance guarantees, and have become increasingly popular in Asia and continental Europe since the equity market downturn in 2000–02 and in response to the prolonged low interest rate environment. However, certain products such as equity-linked and structured credit notes may raise consumer protection issues given the complexity of their underlying exposures and risks.
- Mutual funds and index products may meet long-term investment needs, and are more widely used by households. Rapid innovations in the mutual fund industry in recent years has led to low cost investment alternatives (e.g., Exchange Traded Funds), facilitating access to a wide range of asset classes with greater diversification and liquidity benefits.
- Annuities allow households to manage longevity risk, which is a critical risk associated with retirement savings. Indeed, certain countries have imposed partial annuitization of defined contribution pensions at a certain age (e.g., at least 75 percent of pension savings at age 75 in the United Kingdom). As noted, however, the development of deeper annuity markets depends significantly on the ability of annuity providers to hedge longevity risk.

Households and housing wealth

Housing assets play a special role as they generally represent households’ main asset and are viewed as an attractive long-term investment, including for retirement. However, the ability to rely on housing as a source of savings or investment depends in part on the liquidity of the housing and mortgage markets. In this regard, the U.S., Dutch and U.K. markets have seen the largest development of home equity credit lines and reverse mortgages, which offer additional flexibility for households to convert part of their home equity into disposable income. Home equity lines of credit are a form of revolving credit in which the borrower’s home serves as collateral. Similarly, reverse mortgages may offer a variety of cash flow profiles structured in a way similar to an annuity. Their use, however, has been relatively limited to date, including because such products contain risks similar to an annuity, combined with risks related to preserving the value of the house and eventually selling the property (i.e., price movements and liquidity).

5. Wrap up

In many countries, the growing flow and dispersion of risk has led the household sector to act more as a “shock absorber of last resort.” In this context, while financial education shortcomings are not new, they become more important as households are expected to manage more directly their financial affairs. Households must learn how to manage the newly-acquired risks, and policymakers need to help them to improve on their financial education, and to obtain quality advice and products

necessary to manage their financial affairs. Improving financial education is a process that will ultimately take decades, but public awareness can be increased now, and many welcome initiatives have recently been taken in this regard.

More broadly, household financial literacy should arguably be seen as an important aspect of financial stability considerations. Policies aiming to improve the financial stability of systemically or otherwise important institutions need to also take into account the potential public sector costs related to household shortfalls in long-term saving and investment. As noted above, addressing this risk supposes that governments take a long-term, strategic view to their possible role as “insurer of last resort,” to facilitating the development of markets and market solutions, or to re-regulate institutional behavior in order to achieve a desirable sharing of long-term risks.

B- Financial Education and Pensions

Ambrogio Rinaldi, Chair, OECD Working Party on Private Pensions, Central Director, COVIP, Italy

1. Introduction

Financial education is an increasingly hot topic, in many countries and international fora, and this conference is going to reinforce the current momentum. Indeed, both the organizers of the conference, the US Treasury and the OECD, have been very sensitive to the topic for quite a long time. Both of them were early movers in the field, taking initiative as early as 2003; and both soon devoted specific attention to the area of pensions.

In particular, when in 2005 the OECD Council approved its "*Recommendation on principles and good practices for financial education and awareness*" – an important international standard-setting document – it also instructed the relevant groups within the OECD to conduct further analysis and identify good practices in relation to pensions. The OECD Working Party on Private Pensions (WPPP) produced soon a comprehensive background report and, in 2006, drafted a document containing good practices for financial education relating to private pensions. A few weeks ago, in late March 2008, the document was formally approved by the Council as the "*OECD Recommendation on good practices for financial education relating to private pensions*".²⁴

As chairperson of the WPPP, it is my duty to briefly describe the OECD Recommendation. Taking stock of behavioural economics, I will then take this opportunity to discuss the efficacy and the limits of financial education related to pensions, and I will highlight the need to put it in a wider context, taking an integrated and consistent approach that considers education together with information and disclosure to plan members, and –more in general– financial and pensions regulation and policy. In other words, education efforts relating to pensions are to be seen as necessary, but not sufficient to ensure informed choices and adequate income in retirement: other policy tools are also needed and, above all, a well-designed integrated policy approach has to be pursued.

Before all that, let me spend a few words underlining the relevance of the topic.

2. Why is financial education so important for pensions?

Increasingly so, individuals are asked to take decisions regarding their own pensions. Indeed, a significant shifting of risk and responsibility has been occurring from the public domain and from employers to individuals, as a result of shrinking public pensions, and of the shift from defined benefit to defined contribution schemes in supplementary private pensions.

Unfortunately, decisions regarding pensions are not easy. Pension products are very long term and complex, requiring not only knowledge, but also planning skills, as well as the willingness to plan.

The very nature of the decision process is tricky: past experience is of little help. Individual learning-by-doing, useful to consumers in many instances, can hardly be used in pensions, because decisions in this field are typically non-recurrent. And individuals cannot learn from the experience of their parents as well, because the retirement environment has been changing so much.

²⁴ The background report and the Recommendation are both made available in the OECD (2008), Publication "*Improving Financial Education and Awareness in Insurance and Private Pensions*".

The social relevance of pensions has also to be underlined. Pension reforms increasingly require that private pension plans are addressed to the entire working population, and therefore also to low-income workers, that are more likely to lack the necessary basic literacy and capability to make informed choices. The more so, pension reforms should be well understood by the public at large, in order to enhance the consensus and make them politically acceptable.

All these factors highlight the special role that financial education has to play in the field of pensions, a role that probably is more difficult than in the case of most other financial issues and products. Indeed, we might even speak of "retirement education", in order to emphasize the peculiarity that education should have in the field of pensions.

3. The OECD Recommendation

Let me briefly present the OECD Recommendation on financial education related to pensions. It is composed of three parts.

The first part defines the general framework and the objectives of financial education in relation to retirement. Financial education related to pensions is encouraged, either as part of a wider education effort, or through specific programmes. Its objectives include the promotion of the understanding of the changing retirement environment, of the need to save more for retirement, and of retirement schemes and products. Financial education should be taken into account within the pension regulatory framework (i.e. regulation on the provision of information) and should be seen as a tool to enhance personal well-being, social and economic growth through efficient and transparent competitive markets for pension products. It is noted that education does not substitute but rather complements prudential regulation and consumer protection, and that financial education can promote market efficiency and symmetrical information between pension providers and consumers.

The second part of the recommendation focuses on the roles and responsibilities of the main stakeholders in the pension environment: the governments and the other public authorities, the social partners such as trade unions and employers' associations, the individual employers sponsoring the plans, the pension funds and the other pension providers (notably the financial institutions). For each of these stakeholders, the main actions that could contribute to financial education are indicated, with an approach inspired to comparative advantage.

The recommendation has a third part devoted to encouraging the assessment of education needs and the measurement of the level of financial literacy of the population and of more vulnerable groups, as well as the assessment of measures and programmes aimed at enhancing financial capability related to pensions.

This final part also mentions mechanisms and tools that may complement financial education efforts. In particular, the recommendation encourages the automatic enrolment in pension plans with appropriate default mechanisms and opt-out procedures, and promotes various tools – including financial calculators – for estimating retirement income needs and saving requirements. Finally, it is recommended to make available financial education in relation to pensions through a large variety of sources, including broad media coverage, in order to increase the awareness of pension issues in the public at large.

4. Efficacy and limits of financial education

While the OECD Recommendation strongly encourages efforts to enhance financial literacy and capability in relation to pension planning, it is also well aware of the limits of financial education if it is used as a "solo" tool to ensure adequate choices and economic well-being in retirement.

This is consistent with a growing body of behavioural economics literature, referred mainly to the US, showing that financial literacy has a strong explicative effect in increasing saving and improving retirement planning, and also that financial education does indeed improve individuals' ability to take sensible choices regarding their pensions. Many papers by Annamaria Lusardi (and her co-authors) argue in this sense²⁵. However, the same body of literature shows the limits of financial education and suggests to complement it with other policy tools.

For example, as mentioned in the background OECD report, Choi et al.²⁶ study the savings behaviour of holders of 401(k) pension plans in the US, and assess the impact of financial education as well as of many plan features, including automatic enrolment, employer matching provisions, and investment options. They identify a key behavioural principle: plan members are likely to follow "*the path of least resistance*". In other words, they will often do what is the easiest, which usually is doing nothing, and are therefore prone to take passive decisions, accepting the default options that are set for them.

Along similar lines, Thaler and Benartzi²⁷ have suggested to fight employees' inertia and procrastination, and increase their saving through the programme called "*Save More Tomorrow*": at any point in time, workers are offered to commit to increase their savings not immediately but later, for example when they will get pay increases. As documented, in the companies where it was adopted the program has been quite effective. In other papers, the same two authors argue that the value or investors' autonomy in relation to retirement is quite limited, as they are not able to make consistent choices; moreover, the investors' choices are very sensitive to the "frame" of options offered, suggesting again a large scope for influencing choice through appropriate option design.

Mac Farland and al.²⁸ emphasize the heterogeneous saving behaviour across workers, identifying several groups by cluster analysis: the "successful planners", but also those that are stressed by financial matters and those that are plainly uninterested in the future at all. This analysis suggests that any policy aimed at improving decision making for retirement must consider that "*one size does not fit all*", and therefore that different solutions should be designed for different target groups, as financial education may be fit and effective for some but not for others.

²⁵ See for example Lusardi, Annamaria (2004): "*Savings and the Effectiveness of Financial Education*", in *Pension design and Structure: New lessons from Behavioural Finance*, edited by Olivia Mitchell and Stephen Utkus, Oxford University Press.

²⁶ See Choi, James et al. (2001): "*Defined Contribution Pensions: Plan Rules, Participant Decisions and the Path of Least Resistance*", Pension Research Council Working Paper, The Wharton School, University of Pennsylvania.

²⁷ See Thaler, Richard and Benartzi, Shlomo (2001): "*Save More Tomorrow: Using Behavioral Economics to Increase Employee Saving*", Working Paper, Graduate School of Business, University of Chicago.

²⁸ See Mac Farland, Donna et al. (2003) "*Money Attitudes and Retirement Plan Design: one size does not fit all*", Pension Research Council Working Paper, The Wharton School, University of Pennsylvania.

5. The use of other tools to complement financial education

The need to consider financial education in a wider context, together with other policy tools that may be used in order to ensure the workers' financial well-being in retirement, is evident not only from the stream of literature mentioned in the previous section.

In a recent paper considering the international trends in the provision of information to members of defined contribution pension plans²⁹, a conceptual framework is offered in which the provision of such information, together with financial education, is put in relation with other policy instruments, such as regulation limiting individual choice, product standardization, prudential regulation, cost caps, advice, and default options.

The paper highlights the strong complementary relationship between information and education: in general, information to pension plan members is only useful to the extent that they are able to make use of it. While basic and simple-to-understand information should be considered good in any case, detailed and sophisticated information is likely to be useful only if members are endowed with the literacy needed to understand, interpret, and make use of it.

On the other hand, when financial literacy is poor, the provision of detailed information is likely to be ineffective or even harmful. In this case, other regulatory instruments may play a replacing role, limiting the complexity of the decisions to be taken by members.

According to this framework, regulation limiting individual choice - in principle inefficient as it limits the opportunities available - may instead be seen as welfare-improving, radically reducing decision costs and overcoming the difficulty of empowering members to take their own decisions. Therefore, a "paternalistic" rationale may be found for a set of policies such as mandatory membership, limitations to shop around for different providers, restrictions to the number and range of investment options.

Along the same lines, any regulation or practice that simplifies the decision-making process may also be seen as welfare-improving. Standardization of pension products, of their risk/return profiles or their fee structure, is an other example. This regulatory approach is typical of systems that are based on personal pension plans, provided by a range of financial firms, and usually offered directly to individuals (though in some cases an employer, and employee representatives, are involved in the selection of the sponsored plan). In these cases, emphasis is placed upon product comparability, and competition between providers. The interaction of these factors with the need for information (and education) to be offered to members is complex: product standardization can be seen as an information (and education) substitute, reducing complexity and easing comparison, making choices simpler; but in order to make competition work effectively and foster market discipline, information and education are essential complementary ingredients.

The case of default options is also especially interesting. They may be seen as an effective way to convey information and education, in the form of an authoritative advice. Indeed, providing a default option signals the choice that should best suit workers in "normal" conditions, and for the majority of them may act as an efficient "substitute" for the processing of complex information and the provision of education and advice. However, default options do not remove the need to offer information on all

²⁹ See Rinaldi, Ambrogio and Giacomel, Elisabetta (2008), *The Information to Members of DC Pension Plans: Conceptual Framework and International Trends*, Working Papers, International Organization of Pension Supervisors.

other options available; for if they wish, members should always be able to check whether other options are better suited to their specific needs and preferences.

In conclusion, in order to favour the financial well-being in retirement many tools are available along with financial education. Their optimal mix will depend on specific circumstances: however, it should be considered anyway that financial education is bound to be effective especially in the long term, and therefore it is likely that in the immediate other tools – especially those simplifying individual choice – will also have to be put at work.

6. The need for an integrated policy approach

The previous section highlighted the need to put financial education related to pensions in a wider context. Let me finally emphasize that a well-designed integrated policy approach has to be pursued, that considers education together with information and disclosure to plan members, and –more in general– financial and pension regulation and policy.

As a significant example, such an approach is particularly needed in the design of nation-wide automatic enrolment. Programs of this kind have been recently launched in New Zealand and in Italy, and are scheduled for the near future in the UK. In the softer form of incentivating employers to offer such plans, policies favouring automatic enrolment have been put forward recently also in the US.

These plans are based on an interesting philosophy, that stands in the middle between the paternalistic approach that traditionally characterized many public pension schemes (as well as defined benefit private pension plans) and the extreme libertarian approach that often characterizes member-directed pension systems based on individual accounts and defined contributions.

In these plans, substantial information and education efforts are anyway requested, as in principle freedom of choice is preserved and therefore workers have to be put in condition to make their own choices if they decide to do so.³⁰ However, the risk of relying too much on the decision-making capability of workers is moderated by the paternalistic component, accomplished through the system of default options, that play a twofold crucial role: setting choices for those that are unable and/or unwilling to choose; and –as noted before– providing to all workers information and advice about the option that is most likely to be the best for them.

Paternalism may be provided uniformly nation-wide by national public policy, or it can be left to employers, trade unions, or other "intermediate" bodies, with an approach consistent with the "subsidiarity" principle. In both cases, it is very important that consistency is ensured between the default options and the information and education efforts.

For example, if financial education aims at encouraging saving for retirement, it is sensible that the default option provides for a sufficient level of contribution of the employee and –where possible– for a matching contribution of the employer. The more so, if financial education explains the positive

³⁰ It is interesting to mention a recent paper (Willis, Lauren (2008), "*Against Financial Literacy Education*", mimeo, Loyola Law School, Los Angeles), where financial education is seen as controversial or even wasteful. This paper appears to be based on a philosophy that is strongly sceptical on the role that individual responsibility may play in the design of a welfare system. For example, it is argued that "*consumers generally do not serve as their own doctors and lawyers and for reasons of efficient division of labor alone, they should not serve as their own financial experts*". Let me note that recent trends in the design of welfare systems encourage a better awareness and a larger responsibility of individuals also in health-care matters.

relationship between risk and expected return, and rationalizes the opportunity to take advantage of the "risk premium" of investing in stocks in the long investment horizon typical of pension products, it is sensible that default options are designed in a life-cycle fashion, allowing the share of stocks to automatically decrease as a worker gets older³¹.

In conclusion, the messages conveyed through the different policy tools have to be consistent, in order to be mutually reinforcing and to succeed in improving financial literacy and capability, as well as confidence in the implementation of public policy in the pension field. The experience earned through the actual implementation of the nation-wide automatic enrolment programs will be particularly instructive for the development of good practices also in the field of financial education.

³¹ It may be noted that such an overall consistency of the policy approach has not been achieved in Italy, in the case of the automatic enrolment program recently implemented: this may help explain its only partial success.

C- Pension Information: The Annual Statement at a Glance (*see report in Vol. II*)

Lena Larsson, Annika Sundén and Ole Settergren, OECD Consultant

Public and occupational pensions are the major sources of income for most workers during retirement. How much income workers will have in retirement depends on a range of decisions—from how much to work and save to when to retire. Recent trends in pension reform around the world are likely to increase individuals' need for information about pension plans as well as the need for general financial literacy. Furthermore because of the increased financial pressures caused by aging populations, pension reforms often result in a reduction in replacement rates hence increasing the need for individuals to save for their own retirement.

An important tool for information about pensions is the annual statement. This paper discusses the challenges for pension information and describes national pension information in twelve OECD countries. The Swedish Orange Envelope is taken as a starting point for the analysis. The results show:

- Personal pension statements are being introduced across OECD countries to provide information on pension benefits. Personal statements are often introduced in connection with pension reform and are regarded as an important tool in communication about the new pension system.
- Statements are typically mailed to participants annually; most countries also provide additional information on their websites. In particular, the web sites give participants the option to do their own projections and receive additional information about the pension system.
- The information goals are similar across countries: to provide information on contributions to the system and expected benefits. An important information objective is to trigger participants to think about retirement, consider how their life choices affect benefits and make informed choices about if additional savings are required for an adequate retirement income.
- Most pension statements include information on contributions and some countries provide information on participants' earning records. The Orange Envelope provides detailed information on individual accounts much like a bank account.
- The projection of benefits and how expected benefits vary with retirement age is one of the most important sections of the personal pension statement in order to plan for retirement. Some countries only provide projections for participants approaching retirement. By definition, the projection is uncertain for young individuals; however it provides useful information for thinking and planning for retirement. The risk of only providing projections for individuals close to retirement is the information needed to make savings decisions comes too late.
- In Germany and the United States, the pension statement is used to provide system-level information about the financial status of the pension system. The U.S. statement warns participants that benefit cuts or tax increases are necessary and that such changes are will affect retirement income.
- Several countries have evaluated their pension information. However, additional research is needed to show the effectiveness of pension information.

- Both the usefulness and “understandability” of pension statements from public schemes is significantly reduced in countries where workers receive pension benefits from several sources.
- Internet services promise to be the most important tool to providing more comprehensive, individualized and thus relevant pension information services in the future. The development of such services is a difficult endeavor. They involve public, private and often social partners and are often both legally and technically challenging.

D- Research Findings on the New Realities of Retirement Savings

Jeff Dominitz, Based on joint work with Angela Hung and Joanne Yoong RAND Corporation

Over the past few decades, risks associated with providing for financial security in retirement have increasingly shifted from employers to employees as employer-provided pensions have shifted from defined-benefit (DB) to defined-contribution (DC) plans in the United States. According to calculations based on the Survey of Consumer Finances, among those workers reporting any pension coverage in 1983, 12% reported having a DC plan only, 26% reported both a DC and DB plan, and 62% reported having a DB plan only. By 2004, fully 80% of covered workers reported having a DC plan (63% DC only, 17% both) (Munnell and Sunden, 2006). DC plans require employees not only to bear investment risk but also to make financial decisions for which they may be poorly prepared. The growth of individual retirement accounts outside of employer-sponsored plans raises similar concerns.

Recent work in behavioral finance suggests that investors do not make optimal investment decisions in their DC plans. Mottola and Utkus (forthcoming) examine data from nearly 2.9 million 401(k) participants in a sample of Vanguard investors and find that only about 45 percent of investors are constructing portfolios with equity allocations that may be consistent with expert advice. Other research has found that investors tend to use heuristics or simple decision rules to make their allocation decisions (e.g., Benartzi and Thaler, 2001; Madrian and Shea, 2001). In response to concerns about these behaviors, key provisions of the Pension Protection Act of 2006 are intended to remove impediments to DC plan participation and diversification and to the provision of financial advice about investing for retirement.

Recent litigation and congressional inquiries have focused attention on 401(k) plan fees: what fees are charged, who receives these fees, and what plan fiduciaries and participants know about the levels of these fees and their impact on financial returns (U.S. Government Accountability Office, 2006). The U. S. Department of Labor, which maintains regulatory oversight, is engaged in ongoing efforts to improve the disclosure of fees and expenses to plan fiduciaries and participants, as well as to the regulator. It is unclear how improved disclosure will ultimately impact investor behavior and outcomes.

Researchers at RAND are actively engaged in studies of financial decision making for retirement, addressing such questions as:

- What kinds of choices do individuals make?
- What do they know about the choices they face?
- Where do they get information and advice?
- What information and advice are they given?

Much of this research utilizes data from the RAND American Life Panel, an ongoing national survey administered via the Internet. The remainder of this essay discusses illustrative findings from the literature and from research at RAND.

Individual Decision Making in Defined-Contribution Plans

Employees who are eligible to participate in DC plans face important questions about how much money to put into retirement accounts and how to invest that money. Standard investment advice, as

well as findings from academic research, calls for individuals to save more. Some of the academic research has even led to the design and implementation of mechanisms intended to encourage savings, such as Save More Tomorrow™ (Thaler and Benartzi, 2004) and Quick Enrollment™ (Choi, Laibson, and Madrian, 2006a).

As for how to invest those savings, standard investment advice calls for individuals to reduce the allocation to risky assets with age, or, more precisely, as the investment horizon shortens. Canner et al. (1997), for example, cite a rule of thumb stock allocation percentage of 100 minus age. More generally, so-called life-cycle funds decrease the share in equities as the investor ages. These funds have become increasingly popular investment vehicles in the United States and were included among the qualified default investment alternatives associated with the Pension Protection Act.

The increasing popularity of life-cycle funds and associated investment strategies runs counter to a key finding by Samuelson (1969) that the portfolio allocation should be invariant to the investment horizon. Samuelson (1994) discusses several exceptions to this result, as do Bodie et al. (1992), Jagannathan and Kocherlakota (1996), and Ameriks and Zeldes (2004). For example, one must account for human capital wealth when assessing the allocation of total wealth, in which case age variation of the optimal financial wealth allocation depends crucially on the variation of labor market earnings with financial market returns. Standard investment advice, however, tends to ignore these aspects of prospective labor market earnings, focusing instead on risk tolerance, investment horizon, and, perhaps, the extent of background risks, such as labor income risk.

Recent work in behavioral finance suggests that, whatever their preferences, expectations, and background risks, investors do not make optimal investment decisions in their DC plans. Instead, investors tend to use heuristics or simple decision rules to make their initial allocation decisions. Madrian and Shea (2001), for example, examine 401(k) allocation behavior by a group of employees from a Fortune 500 company. They find that an individual's allocation of regular contributions to a 401(k) plan is sensitive to enrollment default options.

A related example of apparently suboptimal decision making is the preponderance of the "*1/n rule*" documented by Benartzi and Thaler (2001). These authors find that investor allocation decisions are heavily dependent upon the choices offered to them. Roughly speaking, if they are offered n choices, then they tend to allocate $1/n$ of their investment to each of the choices offered, independently of the risk characteristics of the investment opportunities. Huberman and Jiang (2006) find that investors follow the $1/n$ rule, but the n used in the denominator is not the number of fund choices available. Instead, they find that most investors equally allocate their 401(k) contributions across a subset of funds.

Other evidence indicates that retirement portfolios are rarely adjusted. The overwhelming majority of individuals engage in no rebalancing of 401(k) portfolios in any year (e.g., Agnew et al., 2003; Samuelson and Zeckhauser, 1988). Even where the introduction of Internet access was found to greatly increase trading activity, most participants were inactive over a three-year period of study that immediately preceded the stock market collapse of 2000 (Choi et al., 2002).

Dominitz and Hung (2006) assess the welfare implications of alternative retirement plan investment options given that households may not invest according to optimal portfolio choice theory but may instead use simple decision rules. Their approach is similar in spirit to Calvet et al. (2006), who assess the welfare costs of household investment "mistakes" in Sweden, focusing on underdiversification of risky assets and nonparticipation in risky asset markets. These authors recognize that the expected benefits of participation must be assessed based on some notion of how households will actually behave once they choose to participate.

Poterba et al. (2006) use simulations based on historical returns in the United States to assess the outcomes of a number of investment strategies. They find that the welfare implications of various investment strategies are very sensitive to assumptions on preferences, wealth held outside of retirement plans, asset returns, and expense ratios. The role of expense ratios is particularly relevant when one considers the benefits of life-cycle funds, which tend to carry higher ratios. Much work remains to be done to assess the benefits of such passively managed but high-fee accounts in a second-best world where plan participants seem to systematically make investment mistakes.

The Impact of Fees and Expenses on Investment Behavior

A few academic studies have focused attention on how fees and expenses affect the decisions of individual investors. Barber et al. (2005) analyze mutual fund flows and find that fund purchase decisions are sensitive to salient fees, such as front-end loads and brokerage commissions. In contrast, purchases are insensitive or perhaps positively related to expense ratios. A positive relationship could be explained by the impact of marketing, the costs of which may be included in the expenses.

Wilcox (2003) conducted experiments to assess how mutual fund and investor attributes affect choices among mutual funds. He finds that individuals tend to avoid loads, overweighting their negative impact relative to management fees. This finding is actually stronger among highly educated and wealthy individuals. Moreover, members of these two groups are also found to overemphasize the importance of past performance relative to fees. Choi et al. (2006b) address similar questions with their experiments on the impact of mutual fund fees. They also find that individuals tend to place too little emphasis on fees and too much emphasis on past performance. While these studies indicate that individuals do not make optimal decisions, they provide little guidance about how to present fee information in a way to improve decision making.

In a study that was inspired by the design of Choi et al. and the findings of other researchers, Dominitz, Hung, and Yoong (2008) report the results of experiments administered to members of the RAND American Life Panel (ALP). This analysis sheds light on the question of how mutual fund investors respond to variation in fees in a hypothetical scenario in which fees should be obvious to the investor. In this experiment, respondents tend not to minimize expected fees and are more averse to back-end load fees than to front-end loads. The trade-off between expense ratios and loads is found to be somewhat sensitive to the expected holding period in a manner consistent with expected-wealth maximization, but investors may tend to be too averse to loads. Differences in measured financial literacy predict differences in behavior, with lower rates of literacy among women accounting for differences in choice behavior by gender.

It is difficult to understand how fees and expenses impact behavior without knowing what individuals actually know about these costs outside of experimental settings. According to conventional wisdom, individual investors tend to know little about the fees and expenses that they directly or indirectly pay. Survey evidence seems to bear this out. For instance, a 1995 survey conducted on behalf of the Office of the Comptroller of the Currency and the Securities and Exchange Commission (SEC) found that few investors could provide estimates of mutual fund fees that they face (Alexander et al., 1997). Over 80% of 401(k) plan participants in a 2007 AARP study reported that they do not know how much they pay in fees and expenses associated with their own plan (AARP, 2007). Findings from ALP surveys conducted over the past year are in line with previous results, leaving open questions about how to provide information about fees that participants will effectively utilize.

Financial Advice

Interactions between individual investors and financial advisors have changed considerably over the past few decades as financial service providers have expanded their range of services and individuals have taken on greater responsibility for retirement savings. A recent RAND study for the SEC uncovered considerable investor confusion about their financial service providers, including investment advisers and broker-dealers (Hung et al., 2008). This report also highlights the stated desire among investors for financial advising, especially with respect to retirement planning.

The Pension Protection Act enhances the ability of firms to facilitate the provision of investment advice by granting exemptions from prohibited transactions rules if the investment advice is provided under an “eligible investment advice arrangement.” Mottola and Utkus (forthcoming) suggest that advice programs could benefit a meaningful group of participants and that the added service costs should be compared to the potentially large gains in expected returns and diversification. However, while evidence suggests that employee-investors want this advice, it is unclear about how they will implement the advice they are given (Helman et al., 2007). While some behavior such as trading activity in 401(k) plans has been found to be correlated with advice (Agnew, 2006), a causal relationship has not been well-established in the literature.

The potential expansion in investment advising also raises questions about the quality of advice being given. Bodie (2003) evaluates a wide range of investment advice provided to individuals in participant-directed retirement plans by financial service firms and investment advisory services. He finds much of the advice to be inappropriate.

Conclusions

Over the past few decades, risks associated with providing for financial security in retirement have increasingly shifted from employers to employees, with changes in employers’ offerings of DB versus DC plans. DC plans require employees to bear investment risk in addition to the risk associated with longevity—that is, the length of time for which retirement funds will be needed. The two kinds of plans also carry different implications for the retirement benefits available to a surviving spouse upon a worker’s death. Overwhelming evidence indicates that many individuals are ill-equipped to successfully face this new reality. These individuals often seem to recognize the own state of confusion and their need for useful advice.

To address these concerns, the U.S. Congress passed and the President signed the Pension Protection Act. Key provisions of the PPA are intended to help Americans who save for retirement through DC plans by, for example, removing impediments to DC plan participation and diversification and to the provision of financial advice about investing for retirement. Substantial challenges remain, however, as policy makers and practitioners attempt to translate these well-intended legislative and regulatory actions into effective interventions.

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SESSION IV- RISK AWARENESS: ENHANCING EDUCATION AND PROTECTION OF HOUSEHOLDS ON LARGE-SCALE RISKS

Chair: Manuel Aguilera-Verdusco, Chair of the Comisión Nacional de Seguros y Fianzas CNSF, Mexico, Chair of the OECD Insurance and Private Pensions Committee

A- Dr. Rebekah Green, Risk RED, OECD Consultant

B- Dr. Erwann Michel-Kerjan, Managing Director, Wharton School Risk Center, University of Pennsylvania, Chairman of the OECD High-Level Advisory Board on the Financial Management of Large-Scale Catastrophes, **United States**

C- Katsuo Matshushita, General Manager of the International Department, General Insurance Association of Japan, **Japan**

D- Semih Yüccemen, Professor and Director, Earthquake Engineering Research Centre, Member of Management Board, Turkish Catastrophe Insurance Pool, **Turkey**

Policy Conclusions of the Chair

- In general, large-scale risk awareness and risk education policies should be based on the personalization of risk and should emphasize on effective risk reduction strategies. It is important to build in these policies a sense of self-efficacy, encouraging community participation.
- It is not enough to provide the population with information about the main risks they are exposed to. It is necessary to incorporate specific long term mitigation measures as well as the appropriate incentives for the adoption of risk reduction strategies.
- Effective and efficient risk awareness policies and strategies imply a close collaboration between the public, private and civil sectors.
- The government may play a key complementary role in implementing risk reduction strategies, through tax incentives, compulsory insurance schemes and as reinsurer of last resort, where applicable.
- Nevertheless, government participation should be consistent over time and should imply a long term commitment, especially in those large-scale disaster financial management systems.

A- Stocktaking Report and Policy Recommendations on Risk Awareness and Education on Natural Catastrophes (*see report in Vol. II*)

Dr. Rebekah Green, Risk RED, OECD Consultant

In recent decades the scale and cost of natural catastrophes has steadily increased. Much of this increase has resulted from human activity. As such, many countries recognize that public awareness and education on natural catastrophe risk must be enhanced.

The OECD commissioned a stocktaking of selected country efforts to raise public awareness and education of the impact of natural hazards and to enhance awareness and education regarding risk mitigation measures, including financial coverage and protection. This stocktaking covered the public, education, private and civic sectors of 11 selected OECD and 2 emerging economy countries: Canada, Iceland, Italy, Japan, Mexico, New Zealand, Portugal, Spain, Turkey, the United Kingdom, the United States, China and India.

The stocktaking looked at efforts in the public, education, private, and civic sectors as well as cross-sectoral partnerships and international efforts within each country. The primary focus was on national level programs, campaigns, and educational material aimed at increasing awareness of large scale natural hazards and pre-event risk reduction measures, including strategies for financial loss-sharing and risk transfer. The stocktaking effort was achieved primarily through interviews with key personnel in each country, review of scholarly articles, and an assessment of material available on the internet.

The stocktaking found that all of the countries surveyed had some risk awareness and preparedness information that is distributed or made available to the general public by civil defence or other ministries. Some insurance companies and consortiums are directly targeting the public with mass marketing campaigns and information dissemination. There are also examples of large corporations providing or funding risk reduction education for the general public and their employees. Within the growing global awareness of the importance of community risk reduction, international and national civic organizations have also recently begun to include risk reduction education as part of their strategies.

Despite the presence of risk awareness and risk reduction education in assessed countries, there remains significant scope for enhancement. Many government-sponsored and civil society programs continue to put heavy emphasis on emergency response and citizen response-preparedness. While important, this focus often fails to emphasize the individual and collective actions that can be taken prior to a disaster and may even promote a sense of public helplessness. As evidenced in this stocktaking, a re-direction of focus from response to preparedness, risk reduction and financial protection is occurring, although the change is slow.

Awareness and education efforts in all sectors could be improved by promoting land use planning, building codes, and insurance schemes as a means of minimizing or spreading risk. Furthermore, most countries assessed do not include risk awareness or risk reduction education as a fully-integrated part of school education. Innovative school programs were most often implemented in an ad hoc and voluntary way, reducing their impact. Within the private sector, insurance and financial education programs may benefit clients by including or further emphasizing risk awareness and natural catastrophe insurance education in their on-going public education programs.

This stocktaking represents a thorough, initial overview of large-scale efforts in the countries selected and is a solid basis from which to evaluate the current state of risk awareness and risk

reduction education. It suggests that promoting awareness and education of natural catastrophe risks and, in particular, risk reduction measures can encourage voluntary risk reduction activities, including such key measures as safe construction, retrofitting and household preparedness. As part of a broad national risk reduction strategy, it can also strengthen public support for compulsory risk reduction measures such as land use planning, building codes, environmental stewardship and insurance schemes.

B- Reducing Human and Financial Vulnerability to Large-Scale Disasters: Is Risk Awareness (Really) Enough? -- The Individual Behavior Puzzle

Dr. Erwann Michel-Kerjan³², Managing Director, Wharton School Risk Center, University of Pennsylvania, Chairman of the OECD High-Level Advisory Board on the Financial Management of Large Scale Catastrophes, United-States

Outline

Setting the Stage: A New Era of Catastrophes

What's Happening? The Question of Attribution

I Know, But Don't Act: The Individual Behavior Puzzle

Bold Initiatives: OECD's Leadership on Financial Management of Large-Scale Catastrophes

Prelude

Not very long ago, disasters were considered to be low probability events because they did not occur often. That assumption was very reassuring for many: the expected losses of these disasters (understand here, the potential loss associated with a disaster is multiplied by the probability of that event occurring) was often relatively low. Given this, many individuals and leaders would focus their limited resources and time on day-to-day activities with much more certain payoff, rather than on protecting against improbable events.

But in the first few years of the 21st century, the world has faced a string of catastrophes of a totally new dimension: the September 11, 2001 (9/11) terrorist attacks that forever changed international security; a major blackout in August 2003 which deprived electricity to over 50 million North Americans in just a few seconds, then a similar episode in Italy a few days later. 2003 was also one of the hottest summers on record in Europe: the European heat wave killed over 35,000, creating major health crises in several countries; the two following years, seven hurricanes hit the U.S. within a 15 month period. These are but a few examples in OECD countries.

And catastrophes are often even more destructive when they occur in poor or developing countries. Just look back the past five years. The December 2004 tsunami was responsible for the deaths of nearly 300,000 people, the major earthquake in the Sichuan province in China in May 2008 killed nearly 50,000, just a few weeks after a major cyclone killed over 100,000 in Myanmar.

In fact, there has not been a 6-month period in the past few years without a major crisis that simultaneously affected several countries or industry sectors. Two elements are important to consider

³² The Wharton Business School, University of Pennsylvania (USA) and Ecole Polytechnique, Paris (France). Partial support for this paper was provided by the Managing and Financing Extreme Events Project of the Wharton Risk Management and Decision Processes Center and The Chair on Sustainable Development of the Ecole Polytechnique. I would like to thank Tim Bishop, Neil Doherty, Robert Hartwig, Martin Grace, Claude Henry, Dwight Jaffee, Robert Klein, Paul Kleindorfer, Carolyn Kousky, Howard Kunreuther, André Laboul, Patrick Lagadec, Alberto Monti, and Mark Pauly for numerous discussions on these issues. Contact: ErwannMK@wharton.upenn.edu

here. First, media coverage is much more developed today than it was 20 years ago; as a result, any disaster that occurs on another continent is reported live on TV and radio for the entire world to see. In other words, we are all closer to more disasters. Second, and certainly even more important, the globalization of social and economic activities worldwide has created interdependencies. This is not new of course, but the world has reached a degree of interconnectivity that is unprecedented in history. As former Prime Minister Tony Blair put it, “interdependence is the defining element of the 21st century”.³³ As a result, a disaster that occurs 5,000 miles away from you is more likely to affect you tomorrow via ripple effects on different industries and countries.³⁴

Despite these two elements – increased media coverage and interdependency –, the severity of these recent events also demonstrates that the world is changing, and that we have entered a new era. It is now far from clear that we should continue to associate these extreme events with a low probability of occurrence.

1. Setting the Stage: A New Era of Catastrophes

Over the past few years, the losses from natural disasters have expanded dramatically in many developed and developing countries. In countries that benefit from warning systems and effective mitigation programs, consequences are often much lower than in emerging economies that are deprived of such capacity. In Southeast Asia, the December 2004 tsunami surprised everyone and in just a few hours killed more than 280,000 people located on the coastal areas. Mitigation measures were almost non-existent.

But even in a country like the United States, which has extensive experience with natural catastrophes, the 2004 and 2005 hurricane seasons demonstrated the lack of adequate loss reduction measures and emergency preparedness capacity to deal with truly large-scale natural disasters. Katrina killed 1,300 people and forced 1.5 million people to evacuate the affected area – a historical record for the country. Economic damages are estimated in the range of US\$150 to \$200 billion. The three hurricanes (Katrina, Rita and Wilma) that made landfall in the U.S. during 2005 generated nearly \$65 billion in private insurance payments and another \$20 billion by the Federal National Flood Insurance Program for flood damage – another historical record. Federal relief to the victims of these catastrophes and for local reconstruction is estimated to be over \$125 billion – yet another historical record. The 2005 hurricane season, which followed the four major hurricanes that hit Florida in 2004, has demonstrated a new scale of destruction.

Between 1970 and 2004, storms and floods were responsible for over **90 percent** of the total economic costs of extreme weather-related events worldwide. Storms (*hurricanes* in the U.S. region, *typhoons* in Asia and *windstorms* in Europe) contributed to over 75 percent of insured losses. In constant prices (2004), insured losses from weather-related events averaged \$3 billion annually between 1970 and 1990 and then increased significantly to \$16 billion annually between 1990 and 2004 (ABI, 2005).³⁵ In 2005, 99.7 percent of all catastrophic losses worldwide were due to weather-related events (Mills and Lecomte, 2006)³⁶.

³³ *Global Risks 2008*. Report by the World Economic Forum, with Marsh McLennan, Swiss Re, The Wharton School Risk Center and Zurich. Davos, January 2008. Available online.

³⁴ Michel-Kerjan, E. (2008), “Toward A New Risk Architecture: The Question of Catastrophe Risk Calculus”, *Social Research*, Volume 75, No. 3.

³⁵ Association of British Insurers (ABI) (2005), “Financial Risks of Climate Change,” June 2005.

³⁶ Mills, E. and E. Lecomte (2006), “From Risk To Opportunity: How Insurers Can Proactively and Profitably Manage Climate Change,” *Ceres*, August 2006.

These recent catastrophic events are actually part of a trend that has been observed over the past 20 years. The figures are telling: Twenty of the most costly catastrophes to the insurance industry in the world over the past 37 years (1970-2007) occurred after 1987 (in 2007 prices corrected for inflation). Furthermore, of these 20 catastrophes, half of them (10) occurred since 2001 (bolded in Table 1), 9 of them in the United States.³⁷

On the value creation side, with this wider variance in the level of risk, new business opportunities have emerged. For instance, catastrophe bonds (cat bonds), which are financial instruments transferring catastrophe exposure to investors on the financial markets, quickly developed in the aftermath of the 2005 hurricane season in the U.S. (Lewis, 2007).³⁸ In 2006, twenty cat bonds were issued (\$4.7 billion issued and \$8.7 billion capital outstanding), compared with eleven in 2005 (\$2.1 billion issued and \$2.9 outstanding), the previous record. In 2007, the total value of cat bonds issued for natural disasters alone was \$7.1 billion; 27 transactions were completed, a new record compared with the 10 transactions closed in 2005 (Michel-Kerjan and Morlaye, 2008).³⁹

Table 1. The 20 Most Costly Insured Catastrophes in the World, 1970-2007⁴⁰

U.S.\$ Billion (indexed to 2007)	Event	Victims (Dead or missing)	Year	Area of Primary Damage
46.3	Hurricane Katrina	1,836	2005	USA, Gulf of Mexico, et al.
35.5	9/11 Attacks	3,025	2001	USA
23.7	Hurricane Andrew	43	1992	USA, Bahamas
19.6	Northridge Earthquake	61	1994	USA
14.1	Hurricane Ivan	124	2004	USA, Caribbean, et al.
13.3	Hurricane Wilma	35	2005	USA, Gulf of Mexico, et al.
10.7	Hurricane Rita	34	2005	USA, Gulf of Mexico, et al.
8.8	Hurricane Charley	24	2004	USA, Caribbean, et al.
8.6	Typhoon Mireille	51	1991	Japan

³⁷ A series of detailed analyses of the natural disaster insurance and mitigation markets in the United States is provided in Kunreuther and Michel-Kerjan (in press), *At War with the Weather. Managing Large-Scale Risks in a New Era of Catastrophes*, MIT Press, Cambridge, MA.

³⁸ Lewis, M. (2007), "In Nature's Casino," *The New York Times Magazine*, August 26.

³⁹ Michel-Kerjan, E. and F. Morlaye (2008), "Extreme Events, Global Warming, and Insurance-Linked Securities: How to Trigger the 'Tipping Point,'" *Geneva Papers on Risk and Insurance*, 33(1): 153-176.

⁴⁰ This table excludes payments for flood by the National Flood Insurance Program in the U.S.; e.g., \$17.3 billion in 2005 as a result of Hurricanes Katrina and Rita.

7.6	Hurricane Hugo	71	1989	Puerto Rico, USA, et al.
7.4	Winterstorm Daria	95	1990	France, UK, et al.
7.2	Winterstorm Lothar	110	1999	France, Switzerland, et al.
6.1	Winterstorm Kyrill	54	2007	Germany, UK, NL, France
5.7	Storms and floods	22	1987	France, UK, et al.
5.6	Hurricane Frances	38	2004	USA, Bahamas
5.0	Winterstorm Vivian	64	1990	Western/Central Europe
5.0	Typhoon Bart	26	1999	Japan
4.5	Hurricane Georges	600	1998	USA, Caribbean
4.2	Tropical Storm Alison	41	2001	USA
4.2	Hurricane Jeanne	3,034	2004	USA, Caribbean, et al.

Sources: Data from Swiss Re and Insurance Information Institute

2. What's happening? The Question of Attribution

It is important for decision makers to better understand the key drivers of this new loss dimension. Given space limitations here I shall mainly focus on one question: *What role have socio-economic factors played in the increase in the level and variability of these losses?* Another important question (which I will not discuss here) is *How is a change in climate likely to affect the number and severity of catastrophes in the future?*⁴¹

There are at least two principal socio-economic factors that directly influence the level of economic losses due to catastrophic events: *degree of urbanization* and *value at risk*. In 1950, approximately 30 percent of the world's population lived in cities. In 2000, about 50 percent of the world's population (6 billion) resided in urban areas. Projections by the United Nations show that by 2025, that figure will have increased to 60 percent based on a world population estimate of 8.3 billion people.

In hazard-prone areas, this urbanization and increase of population translates into greater concentration of exposure and hence a higher likelihood of catastrophic losses from disasters in the future. In the U.S. in 2003, 53 percent of the nation's population, or 153 million people, lived in the 673 U.S. coastal counties, an increase of 33 million people since 1980, according to the National Oceanic Atmospheric Administration—yet coastal counties, excluding Alaska, account for only 17

⁴¹ Kunreuther, H. and E. Michel-Kerjan (2007), "Climate Change, Insurability of Large-scale Risks and the Emerging Liability Challenge," *Penn Law Review*, Vol. 155, No. 6, June 2007, pp. 1795-1842.

percent of U.S. land area. And the nation's coastal population is expected to increase by more than 12 million by 2015 (Crossett, et. al., 2004).⁴²

The development of Florida highlights this point. According to the U.S. Bureau of the Census, the population of Florida has increased significantly over the past 50 years: 2.8 million inhabitants in 1950, 6.8 million in 1970, 13 million in 1990, and a projected 19.3 million population in 2010 (almost a 700 percent increase since 1950), increasing the likelihood of severe economic and insured losses.

Insurance density is another critical socio-economic factor to consider when evaluating the evolution of insured loss due to weather-related catastrophes. According to a study undertaken by Munich Re (2000)⁴³ Florida has a high density of insurance coverage, with most houses covered against windstorm losses and about one-third insured against floods under the National Flood Insurance Program (NFIP).⁴⁴ In 2008, the modeling firm AIR Worldwide estimated that nearly 80 percent of insured property assets in Florida are located near the coasts, the high-risk area of the state as shown in Figure 1. This represents more than \$2.4 trillion of insured exposure located in coastal areas (commercial and residential exposure) (see Figure 2). Given the growing concentration of exposure on the Gulf Coast, another hurricane like Katrina hitting the Gulf Coast is likely to inflict significant property damage unless strong mitigation measures are put in place.⁴⁵

In order to better understand this new vulnerability, we can compare the total direct economic cost of the major hurricanes in the U.S. in the past century, adjusted for [inflation](#), population and [wealth normalization](#), by estimating what each of these hurricanes would have cost had they hit today. This exercise has been done in several studies. The most recent one by Pielke et al. (2008) normalizes to the year 2005 mainland U.S. hurricane damage for the period 1900–2005.⁴⁶ Table 2 provides estimates for the top 20 most costly hurricanes assuming they had occurred in 2005. The authors propose two ways to normalize these losses, each of which gives a cost estimate. We provide the range of costs between these two estimates, along with the year the hurricane occurred, the states that were the most seriously affected and the hurricane category on the Saffir-Simpson scale. The data reveals that the hurricane that hit Miami in 1926 would have been almost twice as costly as Hurricane Katrina

⁴² Crossett, K.M., T.J. Culliton, P.C. Wiley, and T.R. Goodspeed (2004), “*Population Trends Along the Coastal United States: 1980-2008*,” National Oceanic and Atmospheric Administration, NOAA's National Ocean Service, Special Projects: Silver Spring, MD. This proportion varies depending on the definition of “costal counties” one considers; for instance, taking a more restrictive definition (i.e. any county that has a coastline bordering the open ocean or associated sheltered water bodies or a county that contains V zones (as defined by the US National Flood Insurance Program), one finds that the proportion of population living in such counties is 30%). M. Crowell, S. Edelman, K. Coulton and S. McAfee (2007), “How many People Live in Coastal Areas?”, *Journal of Costal Research*, 23 (5), iii-vi. In any even this proportion is significant and growing.

⁴³ Munich Re (2000), “Topics 2000. Natural Catastrophes – The Current Position,” Special millennium issue.

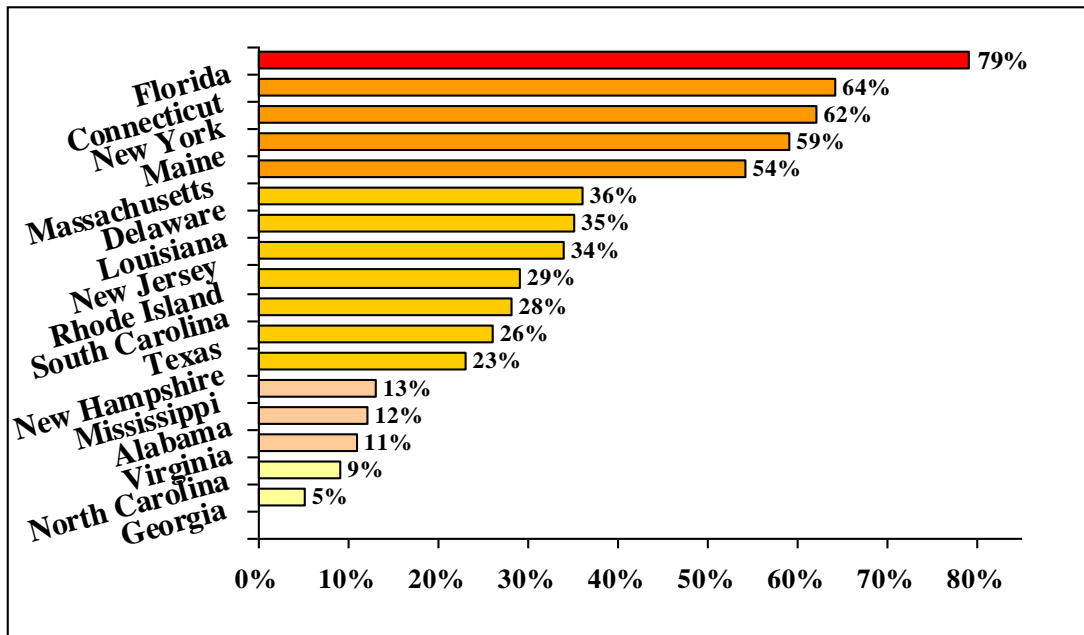
⁴⁴ The NFIP is a federal insurance program created in 1968. Insurers play the role of intermediaries between the policyholders and the federal government. Following Hurricane Katrina, the program had to borrow \$20 billion from the federal government in 2006 to meet its claims. Congress is considering modifying the program substantially. For a more detailed discussion of recent operation of the NFIP, see Michel-Kerjan, E. and C. Kousky (2008), “Come Rain or Shine: Evidence on Flood Insurance Purchases in Florida”, Working paper, The Wharton School of the University of Pennsylvania and Kennedy School of Government, Harvard University, February 2008.

⁴⁵ For additional data on the economic impact of future catastrophic hurricanes, see Financial Services Roundtable (2007), *Blue Ribbon Commission on Mega-Catastrophes Comprehensive Report*, Chapter 2 (2007).

⁴⁶ Pielke, R. Jr, J. Gratz, C. Landsea, D. Collins, M. Saunders, and R. Musulin (2008), “Normalized Hurricane Damage in the United States: 1900–2005”, *Natural Hazard Review*, February 2008.

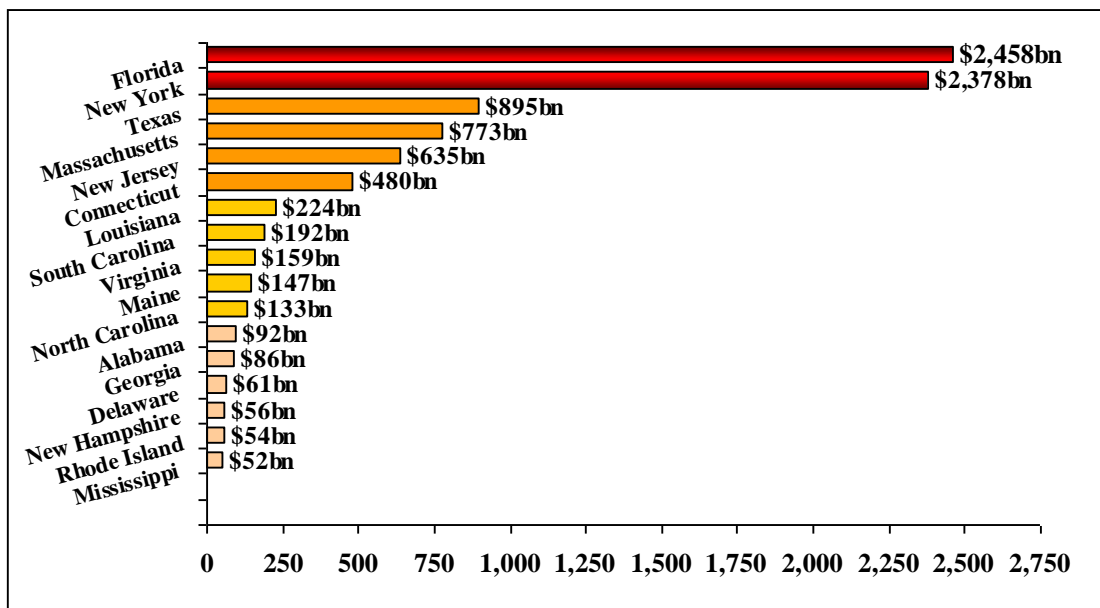
had it occurred in 2005, and the Galveston hurricane of 1900 would have had total direct economic costs as great as those from Katrina. This means that independent of any possible change in weather patterns, we are very likely to see even more devastating disasters in the coming years because of the ongoing growth in values in risk-prone areas.

Figure 1. Insured Coastal Exposure as a Percentage of Statewide Insured Exposure as of December 2007 (Residential and Commercial Properties)



Source: Data from AIR Worldwide Corporation

Figure 2. Total Value of Insured Coastal Exposure as of December 2007 (in \$ billion; residential and commercial properties)



Source: Data from AIR Worldwide Corporation

**Table 2. Top 20 Hurricane Scenarios (1900-2005)
Ranked Using 2005 Inflation, Population, and Wealth Normalization**

Rank	Hurricane	Year	Category	Cost range (\$ billion) in 2005
1	Miami (Southeast FL/MS/AL)	1926	4	140-157
2	Katrina (LA/MS)	2005	3	81
3	North Texas (Galveston)	1900	4	72-78
4	North Texas (Galveston)	1915	4	57-62
5	Andrew (Southeast FL and LA)	1992	5-3	54-60
6	New England (CT/MA/NY/RI)	1938	3	37-39
7	Southwest Florida	1944	3	35-39
8	Lake Okeechobee (Southeast)	1928	4	32-34
9	Donna (FL-NC/NY)	1960	4-3	29-32
10	Camille (MS/Southeast LA/VA)	1969	5	21-24
11	Betsy (Southeast FL and LA)	1965	3	21-23
12	Wilma	2005	3	21
13	Agnes (FL/CT/NY)	1972	1	17-18
14	Diane (NC)	1955	1	17
15	4 (Southeast FL/LA/AL/MS)	1947	4-3	15-17
16	Hazel (SC/NC)	1954	4	16-23
17	Charley (Southwest FL)	2004	4	16
18	Carol (CT/NY/RI)	1954	3	15-16
19	Hugo (SC)	1989	4	15-16
20	Ivan (Northwest FL/AL)	2004	3	15

Sources: Data from Pielke et al. (2008)

Given the potential for truly extreme events, the importance of public awareness and education of risks for the effective management of large-scale disasters has to be recognized. In that spirit, the OECD has recently commissioned a “stocktaking” of selected countries’ efforts to raise public awareness and education about the impact of natural hazards and to enhance awareness and education regarding risk mitigation measures, including financial coverage. The survey covered the public, educational, private and civic sectors of 11 selected OECD countries (Canada, Iceland, Italy, Japan, Mexico, New Zealand, Portugal, Turkey, United Kingdom, United States and Spain) as well as the two largest emerging economies outside the OECD, namely China and India.

Conclusions from this exercise are enlightening. The authors conclude: “All of the countries surveyed had some risk awareness and preparedness information that is distributed or made available to the general public by civil defence or other ministries. Memorials and museums located at past disaster sites, hazard resistant construction seminars and materials, and mock evacuations and disaster drills were also present in many countries. Some countries have risk education in their national curriculum, while others have developed voluntary programs for risk awareness and risk reduction education in the schools. Some insurance companies and consortiums are directly targeting the public with mass marketing campaigns and information dissemination. There are also examples of large corporations providing or funding risk reduction education for the general public and their employees. Within the growing global awareness of the importance of community risk reduction, the International

Federation of Red Cross and Red Crescent Societies and many national civic organizations have also recently begun to include risk reduction education as part of their strategies. The United Nations, through its International Strategy for Disaster Reduction (UNISDR), has been active in internationally promoting better awareness and education of disaster risks and especially disaster risk reduction strategies. International efforts have focused on increasing awareness of national governments and policy makers regarding the risks facing their country and the ways they can reduce catastrophic losses.

Despite the presence of risk awareness and risk reduction education in many countries, there remains significant scope for enhancement. Many government-sponsored and civil society programs continue to put heavy emphasis on emergency response and citizen response-preparedness. While important, this focus often fails to emphasize the individual and collective actions that can be taken prior to a disaster and may even promote a sense of public helplessness. As evidenced in this stocktaking, a re-direction of focus from response to preparedness, risk reduction and financial protection is occurring, although the change is often slow.” (Green and Petal, 2008).⁴⁷

3. I Know, But Don't Act: The Individual Behavior Puzzle

One of the well-know challenges here is that although catastrophes are becoming more frequent, this does not necessarily mean that catastrophes will strike every year, nor that everyone will be hit. For instance, after two consecutive years of historic wind and flood losses in 2004 and 2005, and despite forecasts of higher-than-normal hurricane activity for the 2006 and 2007 seasons, the only hurricane to make landfall in the U.S. since 2005 was a Category 1 hurricane. Bearing in mind that this OECD/U.S. Treasury conference focuses on financial education, and that this paper was prepared for a session on risk awareness, it is important to elaborate on how such high variability from one year to the next affects the behavior of residents in these high-risk areas.

Here I would argue that the conventional wisdom might be false: one often makes the simplifying assumption that if people knew there were at risk, they would immediately act to protect their family and assets. Recent analyses estimated that if effective mitigation measures were in place for each house in the state of Florida, the cost of a 100-year hurricane would decrease by more than 50 percent.⁴⁸ Rationality would call people living in hazard-prone areas and to undertake proper risk reduction measures to make their house more resistant to future extreme events and to buy adequate insurance coverage. Unfortunately, evidence shows that this is far from the case.

Prior to a disaster, many individuals perceive its likelihood to be sufficiently low that they believe, “It will not happen to me” and are reluctant to incur upfront cash expenditures to reduce future losses. As a result, they do not voluntarily invest in protective measures, such as strengthening their houses or buying insurance. It is only after the disaster occurs that these same individuals claim they would like to have undertaken these actions; this behavior was termed the *natural disaster syndrome* (Kunreuther, 1996, 2006).⁴⁹ Hence the area is highly vulnerable and unprepared should a severe hurricane or other natural disaster occur. The magnitude of the destruction following a

⁴⁷ R. Green and M. Petal (2008), “Stocktaking Report and Policy Recommendations on Risk Awareness and Education on Natural Catastrophes”, report to the OECD, Direction of Financial Affairs, Paris: OECD.

⁴⁸ Kunreuther, H. and E. Michel-Kerjan (in press), *At War with the Weather. Managing Large-Scale Risks in a New Era of Catastrophes*, MIT Press., Cambridge, MA.

⁴⁹ Kunreuther, H.. (1996), “Mitigating disaster losses through insurance,” *Journal of Risk and Uncertainty* 12: 171-187; Kunreuther, Howard (2006), “Disaster Mitigation and Insurance: Learning from Katrina,” *The Annals of the American Academy of Political and Social Science*, 604: 208-227.

catastrophe often leads public sector agencies to provide disaster relief to victims even if the government claimed prior to the event it had no intention of doing so. This combination of underinvestment in protection prior to the event leading to large disaster losses, together with the general taxpayer financing some of the recovery can be critiqued on both efficiency and equity grounds.

There is extensive evidence that residents in hazard-prone areas do not undertake loss prevention measures voluntarily even though they are fully aware of the risk. A 1974 survey of more than 1,000 California homeowners in earthquake-prone areas revealed that only 12 percent of the respondents had adopted any protective measures (Kunreuther et al. 1978).⁵⁰ Fifteen years later, there was little change despite the increased public awareness of the earthquake hazard. In a 1989 survey of 3,500 homeowners in four California counties at risk from earthquakes, only 5 to 9 percent of the respondents in these areas reported adopting any loss reduction measures (Palm et al. 1990).⁵¹ Burby et al. (1988) and Laska (1991) have found a similar reluctance by residents in flood-prone areas to invest in mitigation measures.⁵²

The 2004 and 2005 hurricane seasons in the United States offer additional compelling evidence of the aforementioned natural disaster syndrome. In fact, one would think that after four major hurricanes hit Florida in 2004, residents in coastal areas would be fully aware of the risk they are exposed to. Yet the following year, the Department of Housing and Urban Development (HUD) reported that 41 percent of homes damaged by the 2005 hurricanes were uninsured or underinsured. Of the 60,196 owner-occupied homes with severe wind damage from these hurricanes, 23,000 (more than one-third) did not have insurance against wind loss (GAO, 2007).⁵³

Even more telling is that even after the devastating 2005 hurricane season, a large number of residents had still not invested in relatively inexpensive loss reduction measures with respect to their property, nor had they undertaken emergency preparedness measures. A survey of 1,100 adults living along the Atlantic and Gulf Coasts undertaken in May 2006—nine months after hurricane Katrina and just a month before the beginning of what was predicted to be very intense 2006 hurricane season—revealed that 83 percent of the responders had taken **no** steps to fortify their home, 68 percent had no hurricane survival kit and 60 percent had no family disaster plan (Goodnough, 2006).⁵⁴

While some might argue that these residents are illogical, one should also make clear that this is likely to be the case again and again unless we recognize that risk awareness does not necessarily imply action. Solving this individual behavior puzzle is thus critical if one wants to develop public policies and private sector strategies that effectively reduce the burden of future large-scale disasters. In Kunreuther, Meyer and Michel-Kerjan (2008), we provide a systematic analysis of the more likely factors that influence the decision of residents in high-risk areas, to adopt or *not* adopt risk reduction measures even though they clearly understand they are exposed. We find that the most important ones

⁵⁰ Kunreuther, H. et al. (1978), *Disaster Insurance Protection: Public Policy Lessons*. New York: John Wiley and Sons.

⁵¹ Palm, R., M. Hodgson, R.D. Blanchard and D. Lyons. (1990), *Earthquake Insurance in California: Environmental Policy and Individual Decision Making*. Boulder, CO: Westview Press.

⁵² Burby, R.J., S.J. Bollens, E.J. Kaiser, D. Mullan and J.R. Sheaffer. (1988), *Cities Under Water: A Comparative Evaluation of Ten Cities' Efforts to Manage Floodplain Land Use*. Boulder, CO: Institute of Behavioral Science, University of Colorado; Laska, S.B. (1991), *Floodproof Retrofitting: Homeowner Self-Protective Behavior*. Boulder, CO: Institute of Behavioral Science, University of Colorado.

⁵³ U.S. Government Accountability Office (GAO) (2007), *Natural Disasters: Public Policy Options for Changing the Federal Role in Natural Catastrophe Insurance*, Washington, DC: GAO, November, p. 25.

⁵⁴ Goodnough, A. (2006). "As Hurricane Season Looms, State Aim to Scare," *The New York Times*, May 31.

include budgeting heuristics, biases in temporal planning, underweighting the future, underestimation of risk due to excessive optimism, mistrust of experts' estimates, affective forecasting errors, failure to learn from past experience, social norms, expectation for federal relief ex post at no cost ex ante, and lack of incentive for elected official to ask too much from their constituencies before a disaster, among others.⁵⁵

Further work needs to be done to evaluate how these different elements play a role and how we can better measure them. With this it will be possible for governments and leading companies in and outside the OECD-area not only to develop more effective risk awareness policy but some that effectively induce people and countries to better prepare for the new era of large-scale risks and catastrophes we have entered. Time has come for governments to act, not merely to react. Work that is currently being undertaken by the OECD High Level Advisory Board on Financial Management of Large-Scale Catastrophes (see below) concludes that emphasis should also be placed on the relevance of education concerning available disaster risk financing, risk-sharing, and risk transfer tools, such as insurance. Promoting a better understanding and knowledge of the financial management of costs associated with disaster events should, indeed, be recognized as a priority in this area. In particular, disaster insurance, if correctly priced, and linked to actionable measures by policyholders, can provide not only coverage against damage – permitting more rapid economic and social recovery – but also signals to individuals as to the hazards they face, as well as financial incentives to encourage investment in cost-effective mitigation measures to reduce vulnerability, thereby contributing to the risk communication and education efforts.

Effective disaster risk communication and education strategies require an in-depth knowledge and understanding of:

- (1) the key features of the relevant natural hazards and disaster risks;
- (2) the behaviour and perception changes that the strategy is aimed at inducing in the target audiences (e.g., the type of risk reduction measures that can be adopted at different levels of government and society); and,
- (3) the most appropriate tools and methods to convey the information, and to educate stakeholders and induce action.

Risk awareness and risk reduction education initiatives should be integrated into broader national or international disaster risk management strategies. Risk awareness and risk reduction programs and policies should be scaled to the level of country exposures and vulnerability, and be aligned with the geographical distribution of risks. Promoting a culture of safety requires long-term sustained strategic planning by governments and must be based on a strong commitment of all institutional actors. Higher levels of government should be the source of innovation and lead the process, but local governments, communities, businesses and individuals are the driving force of implementation. Ongoing monitoring and evaluation of awareness and education efforts are essential to assure accountability and transparency, and increase public confidence in the outcomes.

⁵⁵ Kunreuther, H., R. Meyer and E. Michel-Kerjan (2008), “Strategies for Better Protection against Catastrophic Risks”, in E. Shaffir (ed), *Behavioral Foundations of Policy*, Princeton University Press.

10 Principles to Address Catastrophe Risk Awareness More Effectively⁵⁶

1. Natural hazard awareness and disaster risk reduction education are a *foundation and prerequisite* for effective catastrophic risk management strategies at country and regional levels.
2. Risk awareness and risk reduction education priorities should be *risk-based*, tailored to the hazards of the region and the particular vulnerabilities and capacities of those exposed to risk. Resources, if limited, should be focussed on raising awareness and improving knowledge of risk mitigation and financial protection tools for the risks that are most likely to cause significant human, physical and financial losses.
3. *Hazard mapping* and *risk assessments* provide the basis for elaborating risk awareness and risk reduction education strategies and for informing their content. Consistent methods for the collection and dissemination of *data on physical damages and economic losses* from natural hazards will support risk assessments, encourage a better understanding of the benefits and costs of risk reduction strategies, and may support the development of risk financing, risk-sharing and risk transfer tools, such as insurance, reinsurance and capital market instruments.
4. Natural hazard awareness and disaster risk education efforts should aim at encouraging *voluntary risk reduction activities*, building support for a shift in disaster management and enhancing public acceptance of any necessary compulsory measures.
5. *Disaster risk transfer and financing mechanisms* can provide a mechanism for enhancing risk awareness and risk reduction education. Risk-based disaster insurance, if correctly priced, and linked to actionable measures by policyholders, can provide not only coverage against damage, but also signals to individuals as to the hazards they face, as well as financial incentives to encourage investment in cost-effective mitigation measures.
6. *Appropriate risk communication techniques* should be adopted to reach the targeted audiences and induce the desired changes in behaviour and perception. Information on natural hazard exposures to the general public should be accompanied with practical illustrations of the actions that can be taken to reduce risk and the expected benefits of such actions.
7. Clear and consistent messages to all interested parties concerning the *allocation of expected disaster costs and disaster prevention responsibilities* can promote a shared understanding of roles and responsibilities and stimulate individual and collective actions to reduce vulnerability and exposure to the risk of physical and financial losses from natural hazards.
8. Risk reduction strategies should be *specific and realistic for local conditions*.

⁵⁶ Sources: Work under revision - OECD, *Policy Handbook on Natural Hazard Awareness and Disaster Risk Reduction Education*, OECD High Level Advisory Board on Financial Management of Large-Scale Catastrophes, Paris.

9. Promoting a culture of safety requires a *long-term and sustained strategy* by governments and must be based on a strong commitment of all institutional actors. To ensure continuity and sustainability, risk awareness and risk reduction education efforts should become part of a broader cross-sectoral strategy for disaster risk reduction.
10. *Continuous monitoring* and *periodic evaluations* of awareness and education efforts assure accountability and transparency, and increase public confidence in the outcomes.

4. Bold Initiative: OECD's Leadership on the Financial Management of Large-Scale Catastrophes

With the accelerating rhythm and growing scale of natural and man-made disasters and the related impact of climate change we have witnessed in the past few years, it is critical for leading international organizations like the OECD and national bodies such as the U.S. Treasury to be a source of knowledge and strategic thinking for top decision makers. Because of increasing interdependencies across countries, economies and industries, which result from globalization of social and economic activities worldwide, disasters are likely to have even more ripple effects beyond national frontiers in the near future.

What new financial instruments and markets can be developed to create value, while at the same time reducing the impact of future disasters? Are governments in developed and emerging countries adopting efficient strategies to manage the increasing financial burden of catastrophes? Are they allocating sufficient energy and resources to address this issue? What are the roles and responsibilities of key stakeholders in the public and private sectors in the management of disaster risks and costs? And more importantly perhaps, how do we assure that stakeholders with very different agendas and priorities can work together towards a common goal?

To address these issues and develop sound policies, the OECD Secretary General Angel Gurría launched a bold initiative in 2006: the creation of an International Network on the Financial Management of Large-Scale Catastrophes. Under the guidance of a High-Level Advisory Board comprised of leading experts across several OECD countries, the Network promotes the exchange of information and experiences among policymakers, industry, and academia in OECD and non-member countries. I believe the creation of this innovative group to advise top decision makers is a very concrete step toward reducing human and financial vulnerability to large-scale disasters.⁵⁷

⁵⁷ More information about this initiative can be found on the web at: www.oecd.org/daf/fin/catrisk.

C- Katsuo Matsushita, General Manager, General Insurance Association of Japan

Rapid economic growth envisaged in emerging and developing countries is causing an accumulation of peak risks and population growth in urban areas. In developed countries, increased frequency of natural catastrophes is causing devastating economic and social damage. The implication of these realities for the general insurance industry is; we need an efficient system to transfer and spread these risks to the international market in a commercially viable way. However, given the magnitude and increased frequency of large-scale risks, we definitely need more harmonized and collaborative measures beyond conventional methods expected from stand-alone insurance services.

Outline:

The Necessity of a Comprehensive Policy

Backstop for Natural Catastrophes in Japan

Risk Awareness Promotion by the GIAJ

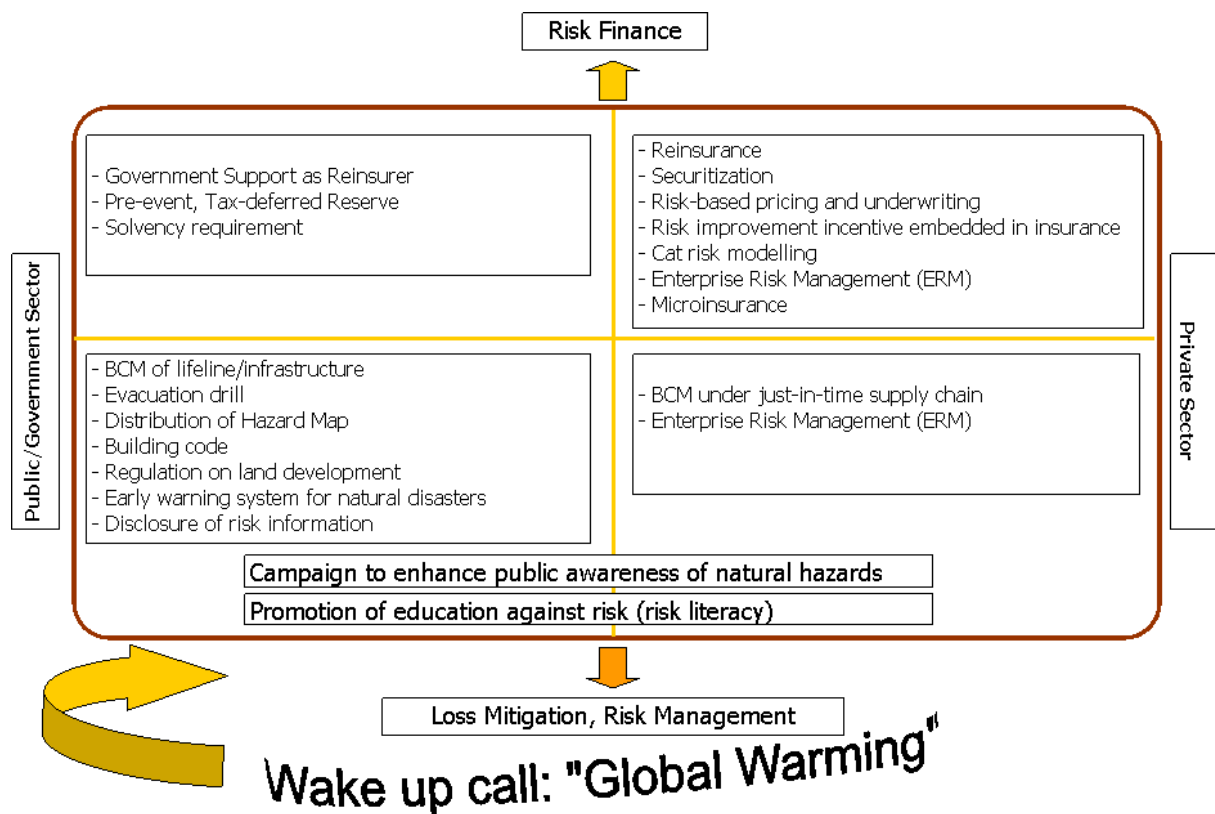
Discover and Learn from Community Wisdom

Linkage of Disaster Prevention and Environmental Preservation

Conclusion

The presentation will start by highlighting the importance of a Comprehensive Policy Framework in order to deal with large-scale risks, with a focus on effective collaborative measures.

The chart below presents the various measures of how to cope with catastrophe risks. They range from measures to be taken up by the private sector to those taken up by the public sector, and from loss prevention/mitigation before the occurrence of disaster to risk finance and post-disaster financial aid.



It is widely recognized that when it comes to disaster prevention, no stand-alone measure can bring any meaningful solution to society and the community. What we need is a coalition of action plans and well-coordinated implementation of these plans. For example, collaboration between:

- Risk finance and loss mitigation/risk management
- Government agencies in charge of land use planning and another government agency in charge of insurance supervision
- Insurers and community/NGOs
- Private sector and public sector towards, for example, institutionalization of the reinsurance pool and tax incentives for catastrophe reserves
- Insurance market and capital market
- Micro-insurance and insurance/reinsurance market
- Prevention of ecosystem degradation and prevention of catastrophes such as landslides and floods.

We need a comprehensive policy framework where we shall pay attention to (1) pre-event prevention, (2) risk financing and (3) financial aid in the event of a disaster with careful evaluation of resource allocation. Resource allocation is, ultimately, an allocation of public funds, including tax incentives. We should seriously study how to allocate public funds among these three measures.

An effective tax incentive is one of the most important public fund allocations. The following is a viable example of incentives.

- Tax policies to promote the building of disaster resilient houses.
- Tax incentives to provide pre-event cat-reserves in the insurance and reinsurance sectors.
- Allowing deductions in premiums from taxable income as an incentive to increase take out ratio of insurance cover. Now moving on to the second point, **Backstop for Natural Catastrophe**. Let me explain to you how the insurance scheme, under partnership with the government, is working towards the sustainability of society, using Japan as an example, a nation very prone to natural catastrophe risks such as typhoons and earthquakes (EQ).

Now moving on to the second point, **Backstop for Natural Catastrophe**. Let me explain to you how the insurance scheme, under partnership with the government, is working towards the sustainability of society, using Japan as an example, a nation very prone to natural catastrophe risks such as typhoons and earthquakes (EQ).

We have three kinds of EQ coverage available, but in conjunction with main fire insurance policies.

- (1) EQ insurance cover for residential houses with reinsurance support from the government under the Law Concerning Earthquake Insurance.
- (2) EQ insurance on industrial or commercial risks written in the extended coverage endorsement. These risks are partly retained by primary insurers and the rest will be reinsured with the international reinsurance market or capital market through ILS (insurance linked securities).
- (3) EQ fire expense coverage for consolation payment for fire insurance policyholders. This coverage is provided as built-in coverage in the main fire insurance policy.

Due to the efforts of the government, municipalities and insurance industry, take out ratio of EQ cover by household (the ratio of policyholders who purchased EQ cover attached to their main fire insurance policy) increased from 33.5% in 2001 to 41.7 % in 2006. This ratio varies from prefecture to prefecture with nearly 70% as the highest and 26% as the lowest. The tax system of allowing deductions of premiums, with a maximum of 50,000 yen, from taxable income has been working effectively to support this positive trend.

As illustrated in the following chart, the government participates in the scheme as a reinsurer of the last resort. The current formation of the EQ insurance scheme for residential risks has a maximum limit of 5,500 billion yen (55 billion US Dollars) and in a three layer structure.

The first layer, which is up to 110 billion yen, private insurers are liable for 100%. The second layer, over 110 billion yen up to 1,730 billion yen, the government is liable for 50% and private insurers are liable for 50%. The third layer, from 1,730 billion yen up to 5,500 billion yen, the government is liable for 95% and the private sector for 5%.

EQ risks on industrial/commercial building, wind-storms, floods and other accumulated perils are managed by reinsurance and insurers' retention. To maintain the financial resilience and flexibility of the insurance carrier, the retained portion is protected by the pre-event, tax-deferred catastrophe reserve.

Let me explain how this reserve has been working in Japan to maintain the financial resilience of insurers. The Japanese islands were hit by ten typhoon landfalls in the year 2004 with J YEN 745 billion (USD 7.1 billion) of insured losses, equivalent to 11 % of the total net tangible assets of our industry.

Despite this magnitude of insured losses, rating agencies such as S&P and Moody's instantly declared that they would maintain the AA rating that was then assigned to major Japanese general insurers.

This is because they clearly understood that insurers' financial resilience would be maintained by the release of catastrophe reserves. In fact, insurers paid claims to their insured and dividends to shareholders as usual that year. Partly due to this reserve system, there have been almost no insurance availability and affordability issues in Japan. The role of this reserve has been great in maintaining insurers' solvency and in bringing benefits to consumers and business customers.

Now let me move on to the third topic, **Risk Awareness Promotion by the GIAJ**. The GIAJ has been conducting various activities to improve risk awareness and risk literacy among various sectors of society. These activities were referred to in the stocktaking report on Risk Awareness and Education on Natural Catastrophes prepared for the Insurance and Private Pensions Committee of the OECD.

As part of the initiatives, we assign staff and send them to school to give lectures to students. We also publish series of booklets, CD-ROMs etc. We have continued to donate fire engines and ambulances to municipalities around the nation. From 1952 to the present day, the number of fire engines stands at more than 2600. From 1971 to the present, the total number of ambulances donated is around 1,600.

Let me explain the three activities in a bit more in detail. They are (1) Earthquake Disaster Prevention Forum, (2) Exploration for Disaster Prevention and (3) Compilation of Hazard Maps.

Earthquake Disaster Prevention Forum:

The GIAJ organizes an educational event inviting more than 100 local radio presenters from all over the nation. In the first part of the event, the experience of a big earthquake, smoke from fires, fire fighting etc. is simulated for the presenters. Then they are given lectures and learn the importance of disaster preparedness, tips to mitigate damage caused by disasters, and EQ insurance, etc. The GIAJ asks the radio presenters to pass their messages on to their listeners about their experiences, the lessons learned in the forum, and the importance of raising risk awareness and disaster preparedness.

(Note) To experience big quakes artificially, there is a quake simulation machine, which is carried on a truck. Major Fire Departments usually have such trucks for educational purposes. Such trucks visit schools and communities and give people an opportunity to experience big quakes.

Exploration for Disaster Prevention:

The GIAJ and Nippon Volunteer Network Active in Disaster, NPO in Kobe, jointly developed this program in 2003. The program is designed for elementary school students. Children can enjoy learning about disaster prevention and risks in daily life. Why do we support and promote this program? The reasons are;

- Useful for raising children's awareness and knowledge of disaster prevention. This could also influence parents, and local communities through children's activities.
- Encourage closer ties in communities and interaction between people of different age groups.
- Simple and inexpensive.
- The program can be tailored according to participants.

“Exploration for Disaster Prevention” is designed to guide children to gradually discover the importance of disaster prevention, while having fun.

Children explore their towns and communities and find facilities related to disaster and crime prevention, such as fire stations, police departments, hospitals, fire hydrants, etc. Children then collate their experiences in a disaster prevention map and make presentations of their findings before the class.

Since 2004, the GIAJ has been co-hosting, jointly with UNESCO and other parties, a “Disaster Prevention Map Contest”. Every year more than 200 schools/community groups (1,000 maps) have participated in the contest.

Compilation of Hazard Maps:

The GIAJ has been conducting studies and research into the making of hazard maps. In 2002 and 2005, the GIAJ digitally compiled all the hazard maps produced by different municipalities in Japan into a CD-ROM, and distributed it to all municipalities in Japan, free of charge.

Through such activities, the GIAJ hopes to facilitate the production of hazard maps and ultimately, limit the property, economic and human loss. As a result of such ongoing endeavors, the Japanese government revised the Flood Prevention Law in 2005 and made it the mandatory obligation

of every local government to prepare and distribute a hazard map to every household in the community.

(Note) A hazard map shows areas where certain natural hazards such as floods, landslides, eruptions, tidal waves, high tides, etc., could occur. It also shows evacuation sites, allowing for safer evacuation of citizens in case of natural disasters.

The fourth talking point is **Discover and Learn from Community Wisdom**.

In the international conference and seminar on natural catastrophe risks, we tend to speak to transfer experience, practice and know-how from developed jurisdiction to developing jurisdiction. However, from our experience, I would like to emphasize that community based initiatives and activities are equally important. So, let me say; Encourage local initiative to enhance risk awareness and let's discover community wisdom, hidden wisdom.

One example is the lessons learned from "Inamura no Hi", a Japanese story from around 200 years ago. The literal meaning of "Inamura no Hi" is putting fire on rice sheaves, the most precious harvest of village farmers. The village chief observed, from a hill top, an early sign of a tsunami attacking his village. He sent a warning message to the villagers who were busy preparing their autumn harvest festival near a beach (and could not recognize the symptom of the tsunami) by putting fire on rice sheaves. Noticing the fire, all the villagers ran up the hill to ask their chief, shouting "Are you crazy? Why put fire on our important harvest?" They thought he must have been crazy under any normal situation, but the villagers soon realized that his decision and action saved the lives of all the villagers.

This story has been passed from generation to generation through school books, short dramas or even in animation to teach about the early signs of a tsunami and how to evacuate from danger. The government of Japan extended financial support to the translation of the animation into English and seven Asian languages for wider distribution mainly in Asia⁵⁸.

The last talking point is **Linkage of Disaster Prevention and Environmental Preservation**.

It is a widely supported and shared belief that global warming, climate change and increased frequency of natural catastrophes are interrelated. We, in the general insurance industry in Japan, have a motto; Let us start from where we can.

As an example, our member companies are promoting and volunteering for various reforestation projects in East Asia, Southeast Asia and Pacific regions. In the case of mangroves, they absorb CO2 and also provide protection against tidal waves and storms.

In conclusion, let me summarize my message to you as follows;

- 1. A comprehensive policy framework is a must for a sustainable society and economy.
- 2. The insurance industry must keep moving forward and continue its efforts to enhance public awareness on catastrophe risk through all possible programs and avenues, e.g. community, schools, media, etc.

⁵⁸ You can retrieve it from the following website:

http://www.adrc.or.jp/publications/inamura/materials/english_inamura.pdf

- 3. The important role of government: tax incentives for earthquake, wind or fire resistant buildings, tax deductions for catastrophe risk insurance premiums and pre-event, tax-deferred catastrophe reserves of insurers.
- 4. Role of government as the reinsurer of the last resort, when appropriate, and partnership between government and private sector. Ultimately, appropriate sharing of risk and burden among policyholders, insurers, reinsurers, and public institutions is required.
- 5. Energize potentials of communities through utilizing local wisdom and initiatives.
- 6. Let's start from where we can: sustaining a linkage between risk awareness, disaster prevention and preservation of the ecosystem.

D- Turkish Catastrophe Insurance Pool (TCIP): Contributions to Risk Awareness

Semih Yüçemen, Professor and Director, Earthquake Engineering Research Centre, Member of Management Board, Turkish Catastrophe Insurance Pool, Turkey

1. Introduction

Turkish Catastrophe Insurance Pool (TCIP) is a non-profit public entity affiliated with the Ministry of State, to whom the Under-secretariat of Treasury reports. TCIP was established by the Decree Law 587 (Date: 27.12.1999) pertaining to the compulsory earthquake insurance. According to the decree law, earthquake insurance was made compulsory for all registered residential buildings within the municipality boundaries.

In Turkey, the State used to have a legal obligation (Disaster Law, No. 7269) to fund the costs of reconstructing buildings after an earthquake. This responsibility of the State brought an unplanned burden on the national economy and on the already limited central budget in the case of catastrophic seismic events. The two major earthquakes in Turkey on 17 August and 12 November 1999 both occurred in or near urban settlements and caused widespread destruction of the building stock. Immediately after these two extremely destructive earthquakes the Government of Turkey has decided to enforce the earthquake insurance on a nationwide basis through the Turkish Catastrophe Insurance Pool (TCIP). TCIP was established under the supervision of Under-secretariat of Treasury to offer such insurance at affordable premiums. The original aim of TCIP was to provide a multi-peril coverage, but currently it provides only compulsory earthquake insurance coverage.

The idea of a nation-wide obligatory earthquake insurance enforcement was first put forward in 1978 by the Ministry of Reconstruction and Settlement. Although the main aim was to reduce government's fiscal exposure, it was also intended to encourage risk mitigation and safer construction practices. To achieve these purposes all registered residential dwellings that are located within municipality boundaries are required to have the compulsory earthquake insurance coverage. Initially funded by the World Bank, TCIP was founded on August 2000 and the TCIP program became effective since then. (The delay in the risk awareness at the government level caused 22 years of delay in the implementation of this insurance scheme). With its 2.7 million policy count as of April 2008, Turkish Catastrophe Insurance Pool has the potential to become the largest earthquake insurance company in the world.

In the first part of the paper background information on TCIP is presented considering those who may not be too familiar with TCIP and the obligatory earthquake insurance scheme. In this first part, objectives foreseen in establishing the Pool and its organizational structure are also presented. Then the contributions of TCIP to the risk awareness of public are discussed, the major problems encountered since its foundation are summarized and a number of comments based on past experience are presented.

2. Background Information

2.1 Basic Properties of the Compulsory Earthquake Insurance Scheme

In general terms, the compulsory earthquake insurance is an insurance product oriented towards dwellings within the boundaries of municipalities. This coverage is a compulsory insurance, for which the guarantee is provided by TCIP but the marketing authority is given to the 25 authorized insurance companies and their 14 000 agencies. Only material damage to the buildings is covered since the subject matter of insurance is specified as the building in the policy. Any damage to persons and

contents is not covered. The period of circulation of the compulsory earthquake insurance is one year. The policies must be renewed prior to its expiry every year.

Compulsory earthquake insurance has to be bought for those dwellings and their independent sections as listed below:

- (i) Dwellings constructed on real estate registered at the Land Registry Office and subject to private ownership;
- (ii) Independent sections situated within these buildings and used as workplace, office or with similar purposes;
- (iii) Dwellings either constructed by the State due to natural disasters or built with the credit provided by the government.

Private dwellings located in villages, public buildings, buildings entirely used for commercial and industrial purposes and buildings under construction are left outside the scope of the scheme.

The amount of annual premium shows variations in relation to the size of dwelling, type of construction (steel/reinforced concrete, masonry and others) and the seismic zone (five zones) and ranges from 0.44‰ to 5.5‰. For a dwelling of 100 m² the annual premium ranges from \$25 to \$120 [1]. A deductible of 2% is imposed in order to avoid minor claims and reduce administrative costs.

The insurance premiums increase every year according to the increase in the construction costs, but they are kept at affordable levels. If the dwelling sum insured exceeds the TCIP limit, then the insured can ask for a homeowner's policy through the private insurance companies in excess of the current TCIP policy. The land value is not included under the "sum insured".

Twenty-five insurance companies and their 14,000 agents can access the central database through the web and produce TCIP policies on a real-time online basis. However, nine insurance companies incorporated policy production unit into their main application by using real-time data transferring function of the TCIP system [2]. A disaster recovery center is established in Ankara as a backup and to provide the same non-stop service if needed. All the software and hardware are owned by the TCIP.

It is to be noted that since the State does not provide any funds, TCIP has to pay claims through its own funds. On the other hand, TCIP's funds cannot be used for any purpose other than insurance, either by any other authority or by TCIP itself. The collected premiums are deposited into accounts in order to get yield. The guidelines for depositing the funds of the Pool give priority to safety and liquidity.

The claims are generally paid within a month. Statistical data showing some of the details of the compulsory earthquake insurance as of 19 March 2008 are given in Table 1. The overall penetration rate is about 21% if the whole building stock is considered. However, if only the eligible building stock is considered (i.e. those buildings that are registered at the cadastral records) a more realistic rate will be obtained as 35%-40%. The penetration rates for different geographical regions closely follow the income level of the people living in these regions.

Table 1 Statistical information on the implementation of the compulsory earthquake insurance as of 19 March 2008

Total Number of Policies	2.711.045
Penetration Rate (%)	21 %
Total Coverage (YTL)	US\$ 105.5 billion
Average Coverage (YTL)	US\$ 38 900
Average Premium (YTL)	US\$ 73
Renewal Rate (%)	36 %
Total Number of Claim Files (since 2000)	9 939
Total Claims Paid (since 2000) (YTL)	US\$ 15.2 million

2.2 Objectives

The primary objectives foreseen in the establishment of TCIP can be summarized as follows:

- (i) To provide insurance coverage for all of the dwellings within the scope of the TCIP policies against earthquake risk in return for an affordable premium;
- (ii) To ensure risk sharing within the country and also to distribute the financial liabilities caused by earthquakes on to the international reinsurance markets;
- (iii) To mitigate the possible financial burdens on the government due to earthquakes (especially construction of new dwellings after a catastrophe);
- (iv) To utilize the insurance system as a means to encourage the construction of earthquake-resistant structures;
- (v) To ensure the accumulation of long term reserves to finance the future earthquake losses;
- (vi) To contribute to the development of insurance consciousness and risk awareness in the public.

2.3 Organizational Structure

TCIP can be considered as a public-private partnership. TCIP is supervised by the Under-secretariat of Treasury, which forms the public side of this partnership. The Under-secretariat develops and maintains a regulatory framework and is responsible for overseeing the program, auditing of all operations and accounts of TCIP.

The other partner (private sector), called Pool Management Company, performs the administrative duties. The wide range of activities of the pool manager consist of co-coordinating the sale processes, settling of accounts, getting the necessary reinsurance protection, settling of claims regardless of which insurance company or agent issued the policy and indemnifying the insured, maintaining the non-stop service of the IT system, performing public relations and managing funds of the Pool [2]. This operational management duty has been contracted out to the leading reinsurance companies in Turkey for periods of 5 years. Milli Reinsurance Company has carried out this duty for

the first 5 years, and Eureko Insurance Company since 8 August 2005, after a selection process. By engaging the private sector in the process of administration, the bureaucratic burdens are minimized.

The overall management of TCIP is performed by the TCIP Board of Directors, which is the only body of TCIP. Setting principles of all operational work and deciding for expenditures including reinsurance, marketing and public relations expenses are among the duties of the Board. The Board is composed of the following seven members: Representative of the Prime Ministry, representative of the Under-secretariat of Treasury, representative of the Ministry of Public Works and Settlement, representative of the Capital Markets Board, representative of the Association of the Insurance and Reinsurance Companies of Turkey, operational manager and an earthquake scientist.

3. Major Problems

The fundamental problem that TCIP has faced in the last couple of years is the lack of interest and support from the State, although it is the State who has established TCIP. Until recently, the government has provided complete coverage for the losses of the public due to earthquakes to a large extent. Currently, there is still a long term loaning system to compensate the losses of owner occupied dwellings or offices. This is an important barrier that prevents the increase in the penetration rate, in spite of the fact that the system was established as an obligatory insurance scheme, by a temporary governmental decree. There is no mechanism for the enforcement of the compulsory earthquake insurance. For the realization of its full effect, the parliament should approve the follow up “Earthquake Insurance Law”, making the earthquake insurance compulsory also in reality. To date the parliament has not passed this legislation which has been waiting there for almost two years.

TCIP was subjected to the coverage of the Turkish Public Procurement Law towards the end of 2004. The Law brought a number of restrictions on the expenditures of the Pool. Accordingly, during the period 2005-2007 it was not possible to carry out effective advertising and public relations campaigns for the promotion of the compulsory earthquake insurance. It was only after two years of intensive effort that TCIP was exempted from this Law, by the end of 2007.

Although the current penetration rate of 21% is much higher than those attained in most of the other countries and the 5% penetration rate in Turkey prior to the establishment of TCIP, it is still not as high as desired. The rate of renewal is about 36% as of 19 March, 2008, and needs to be improved substantially.

The main factors which cause the penetration rate to remain below the desired level are identified as follows:

- (i) A fatalistic mentality in society and the habit of expecting the State to provide everything.
- (ii) A low level of income and the wrong impression that the earthquake insurance premium is expensive.
- (iii) The cultural awareness of insurance has not reached to a sufficient level in Turkey and obtaining insurance is not a high priority in the daily lives of people. Parallel to this general characteristic, the awareness of public with respect to TCIP and the compulsory earthquake insurance is not very high.
- (iv) Lack of trust in TCIP with respect to the compensation of losses after an earthquake.

- (v) There are no legal penalties or fines for the enforcement of the “compulsory” earthquake insurance;
- (vi) The governments follow a populist trend by displaying their willingness to provide post disaster aid to homeowners by themselves. This destroys the homeowners’ incentive to participate in the program. Instead, the State may subsidize the earthquake insurance premium for the low-income section of the population, which would be the rational policy.
- (vii) Insufficient advertisement and public relations campaigns due to the barriers created by the Turkish Public Procurement Law.

4. Contributions of Tcip to the Risk Awareness of the Public

Contributions to the development of insurance consciousness and improvement of risk awareness in the public were among the secondary objectives considered in the establishment of TCIP. The compulsory earthquake insurance scheme became available as of September, 2000. Prior to this date, earthquake insurance in Turkey has been mostly provided as an allied peril to the fire and engineering policies. The penetration rate has been quite low, especially for residential buildings (5% at that time). Within a year after the inception of TCIP the number of compulsory insurance policies sold reached 2.4 million, corresponding to approximately a 20% penetration rate. In the last couple of years, in spite of the adverse attitude of the Government and no legal enforcement, the penetration rate was kept slightly above this level (2.7 million as of 19.03.2008 corresponding to a penetration rate of 21%). This can be attributed to the following contributions of TCIP to risk awareness of the public with respect to earthquake hazard.

(i) The decision that only property covered by insurance will be eligible to receive compensation was a very significant reform, considering the traditional practice and realities in Turkey. TCIP was aimed to be the only source of funding for the earthquake losses in residential buildings. This had a very effective impact on the public. The compulsory earthquake insurance implementation not only contributed to the development of insurance consciousness in the public, but also forced them to become aware of the earthquake risk in the geographical region that they are living in.

(ii) The payment that the Pool Management Company receives is proportional to the insurance policies sold. Therefore, the Company conducts very intensive advertising and public relations campaigns to promote the sale of earthquake insurance policies. These campaigns include mainly:

a) Every week a regular television program is broadcasted on a national TV channel providing information on the compulsory earthquake insurance and TCIP and also answering questions asked by the audience.

b) Commercials are displayed on various TV channels and newspapers.

c) Periodic trips are organized to different cities, especially to those where seismic hazard is high. In these trips the local authorities are contacted and their cooperation is obtained. Elementary and high schools are visited, seminars are given on the general aspects of earthquakes, brochures, CDs and seismic zoning maps of Turkey are distributed. Also live programs are arranged on local TV’s and radio channels. News on such visits take place in the local newspapers and especially children show a great interest in such activities.

d) On the web page of TCIP (www.dask.gov.tr), besides information on the compulsory earthquake insurance, general information on earthquakes as well as information on disaster

preparedness and reduction are presented. Real-time information is displayed on earthquakes that are occurring within the boundaries of Turkey over an interactive map on the web page. On the same interactive map, the seismic zones are shown and people can easily learn the level of seismic hazard in the region they are living in by just clicking on that region on this map.

Although the actual aim of the Pool Management Company in carrying out these activities is commercial, still these activities improve the awareness of the public with respect to seismic risk and also serve for the development of insurance culture. It is to be noted that all of these activities are funded by TCIP. The advertisements taking place on national television constitute the major part of such expenses. However, generally the media employ reduced rates since the mission of TCIP is considered as a public service.

5. Future Actions and their Expected Impact on Risk Awareness

TCIP is proved to be a well designed public-private partnership due to its satisfactory performance over the past eight years. A number of initiatives are still being undertaken for the betterment of the system in various aspects. The major initiative is to develop strategies to increase the penetration rate. As soon as TCIP was exempted from the Turkish Public Procurement Law, a contract was signed with one of the well known public relations companies and an action plan was designed. In accordance with this action plan a public opinion survey was conducted in 18 cities by interviewing 2268 persons, of whom 475 were present customers, 1525 potential customers, 200 agency representatives, 38 academicians and 30 media workers. The most significant findings of the survey were:

- (i) Peoples' awareness of TCIP and its product (i.e. obligatory earthquake insurance) was not as high as expected.
- (ii) People have the impression that the earthquake insurance premiums would be high in view of the premiums charged for car insurance.
- (iii) There is a lack of trust in TCIP with respect to the compensation of losses after an earthquake.

Taking the results of this public opinion survey as the main input, public relations strategies are being developed and new advertising campaigns are designed in order to upgrade the risk awareness of the public and overcome these adverse effects, which are hindering the increase in penetration and renewal rates.

Up to date TCIP has been involved in small to moderate-sized earthquakes. The number of claims to be filed following a major earthquake, like the one in Istanbul, is estimated to be around 400,000 which undoubtedly would create an enormous burden on TCIP [2]. For this reason, an emergency action plan involving various scenarios is prepared with the supervision of experts in this field and work is still being carried out for the improvement and satisfactory implementation of this plan. The scenarios considered range from the situation in which the current workforce would be adequate to the most serious one in which many other loss adjusters, engineers, claim handlers and other professionals would be needed.

Due to the reluctance of the government to pass the "Earthquake Insurance Law" through the approval of the parliament, other mechanisms are tried to enforce earthquake insurance. Currently homeowners have to present their insurance policy to the Land Registry Office whenever they have to carry out an operation concerning the building subject to obligatory earthquake insurance coverage. A

similar plan, obliging homeowners to present their insurance policy when opening an account for such services as water, natural gas, electricity and telecommunications is under consideration for creating additional checkpoints. These types of checkpoints will also activate the risk awareness of individuals.

Besides these initiatives, two major policies are under consideration for future realization. These are as follows:

(i) Allocation of a modest portion of the annual income of the Pool to mitigation investments. Examples of these are: risk avoidance and reduction projects, revisions in land use planning, retrofitting of public and private buildings.

(ii) The use of earthquake insurance as a tool for the enforcement of earthquake resistant provisions of the Seismic Code [3]. In two recent studies conducted by Yucemen [4] and Deniz and Yucemen [5] significantly higher (two to three times more) insurance premium rates were calculated for buildings for which the Code requirements are violated, compared to the ones which comply with the requirements of the Seismic Code. This fact strongly suggests that compliance with the Code should be an important factor in determining the earthquake insurance rates. In other words, different rates should be charged for buildings depending on their degree of compliance with the Code. It is also believed that enforcement of such criterion, will not only encourage the implementation of the code requirements with respect to the earthquake resistant design provisions, but will also create a control mechanism. For this purpose, insurance premiums should be graduated taking into consideration the “seismic resistance quality” of the buildings. In other words, lower premiums should be charged for buildings that comply with the requirements of the Seismic Code. Such a rating procedure will shift the attention of individuals from global to local risk awareness.

6. Concluding Comments

Based on the past eight years of experience the following comments can be made with respect to TCIP:

- (i) TCIP is proved to be a well-designed public-private partnership due to its satisfactory performance over the past eight years. By engaging the private sector in the process of administration, the bureaucratic burdens are minimized.
- (ii) Formation of a very large pool independent of the national budget and therefore largely free of the molest of political decision makers is among the major benefits of the system.
- (iii) TCIP has all the main components and the potential for substituting for the government, in compensating post disaster losses in residential buildings through an insurance program.
- (iv) Within the context of Turkish experience, it is observed that pooling natural catastrophe risks increases the penetration rates significantly if it is made mandatory (with affordable rates) and improves risk awareness of the public. The current penetration rate of 21% is quite high compared to some other countries like India, Philippines, Iran, China, Romania and Bulgaria, where the penetration rates are all less than 5%. Furthermore, pooling natural catastrophe risks enforces standard wordings, conditions and tariffs and establishes a single risk transfer solution for a whole region or a country, yielding usually low administrative expenses.
- (v) In terms of program characteristics, TCIP can be a role model for countries with similar exposures and economic conditions for the mitigation of financial burdens on local

authorities as well as stimulating the risk awareness of the public. However, alternative models can be considered for other countries with respect to spatial extent (one or many countries) and organizational structure (public-private partnership or a purely private organization).

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GUEST SPEAKER

James Flaherty, Minister of Finance, Canada

Good morning.

I am delighted to be here to discuss financial literacy and its growing importance in an ever-changing world of financial services.

As you know, we are in a period of economic uncertainty. The global economy is slowing and we are seeing increased volatility in our financial markets. Clearly, some of the flaws of our financial system have bubbled to the surface. We are today witnessing the consequences of a lack of disclosure and awareness. There are many causes to the financial turmoil, and improved financial literacy is certainly one aspect. Something that is an obvious benefit to society—the ability of citizens to own their own home—has through improper disclosure and complex investments led to global financial turmoil.

This forum is certainly topical. It is taking place less than a month after the G7 Ministers unanimously endorsed the report of the Financial Stability Forum. This report sets out timely and expert recommendations on enhancing transparency and valuation and strengthening the role of credit rating agencies. The report was central to a meeting I held last week with the CEOs of Canada's largest banks. I called on the bankers to implement the Financial Stability Forum's recommendations immediately. We agreed to meet again before the summer to review our progress.

The recent market volatility underscores the importance of investors understanding exactly what they are buying. Greater transparency is an essential part of ensuring that happens. So, too, is financial literacy.

We are living in a highly competitive global financial marketplace. Technology is generating ever-increasing market activity, allowing international investors in search of the best returns to find them not in hours, minutes or seconds, but in fractions of a second. The range of financial products on the market is rapidly expanding, and the complexity of such products can make it difficult for the average investor to fully understand the risks, fees and potential returns. The fact remains, financial turmoil or no financial turmoil, Canada and indeed the world are players in the global marketplace. Individuals are investing like never before.

Understanding the basics is crucial. Financial literacy is essential for people from all walks of life:

- The worker who is setting up a bank account and trying to determine the best way to reach his goals;
- The family trying to make ends meet while saving for a first home;
- The investor who fails to understand the risks, returns or the benefits of compound interest; and

- The senior who, in a world of Internet banking and ATMs, is susceptible to financial scams and fraud.

Whether it's a sophisticated investment or a simple savings account, today's financial world cries out for improved financial literacy.

Today I would like to take a few minutes to highlight what Canada is doing on this front.

Financial Literacy-The Basics

Financial literacy is something that, for too long, we neglected or have simply taken for granted. We all know the benefit of a quality education. Governments around the world make substantial investments in education. We make the effort to nurture our future scientists, engineers and skilled tradespeople. Yet financial literacy is seldom a core component of our curriculum. The irony should not be lost on anyone in this room. We are graduating people who can design and build complex buildings and bridges, but cannot effectively manage their personal finances. Financial literacy is an essential skill that should be developed early in life. After all, a country's financial success is ultimately the sum of the financial success of all its households. Our youth now have more exposure to financial dealings than ever before. They have bank accounts, chequebooks, debit cards, credit cards and online banking. Many have student loans, cell phone contracts and perhaps the beginning of an investment portfolio.

The world of finance is continually evolving and people need to keep up. Without the ability to understand and pay for their lifestyle, they could wind up spending well beyond their means and drowning in a sea of debt. By focusing on financial literacy, we can provide people with the knowledge to help keep their heads above water.

When it comes to buying a house, for example, being financially literate means you may not have all the answers, but at the very least you know what questions to ask:

- What kind of mortgage can I get?
- What are my repayment options?
- What are the fees and taxes?
- How can I lower my payments?
- Can I *really* afford this?

Asking the right questions means understanding the true cost of borrowing. It means knowing that the initial years of mortgage payments go towards servicing the debt, not paying down the principal.

As they struggle to support a family, citizens with a low financial capability could end up at a competitive disadvantage, unknowingly paying higher costs for basic banking transactions and short-term credit. They may face increased exposure to unregulated financial options, and make themselves vulnerable to uninsured risks. This is particularly true in a world where holding multiple jobs over the course of a career is expected, and self-employment is becoming more common. Conversely, effective financial information and increased financial literacy can result in better consumer choices, a larger and more dynamic market for financial sector services, and greater participation in capital markets. It can translate into higher savings levels and decreasing indebtedness. In study after study the evidence is clear: the more you know financially, the more likely you are to save over the long term.

Savings Choices for Canadians

Canada is a saving nation. This has been the result of some innovative savings programs introduced over the years. In the 1950s the federal government introduced the Registered Retirement Savings Plan to support life after work. Today, over 55 per cent of Canadian households own RRSPs. We have established a Registered Education Savings Plan to help Canadians save for post-secondary education. Today, over 42 per cent of children aged 5 to 9 have RESP savings.

One of my proudest achievements as Finance Minister was the introduction of the Registered Disability Savings Plan. Our government realized that parents of children with severe disabilities face financial hardships that can, at times, be overwhelming. They naturally worry about how they will take care of their children and prepare for their future. With a structure similar to a Registered Education Savings Plan, the RDSP will help ensure the long-term financial security of Canadians with severe disabilities. I expect this program to be up and running by December of this year.

In this year's budget, our government did something that hadn't been done in Canada before. We introduced a new and innovative personal savings plan: the Tax-Free Savings Account. This account will be similar to savings accounts in the U.S. and the U.K. It is a flexible, registered, general-purpose account that will allow Canadians to watch their savings grow, tax-free. It will provide Canadians with a powerful incentive to save for everything from a new car to a new home.

Under the account all investment income, including capital gains, will be exempt from any tax, even when withdrawn. Canadians will be able to withdraw from the account at any time and they will be able to save for anything they want, without restriction.

We believe that, within the next 15 to 20 years, over 90 per cent of Canadian individuals will hold all of their financial assets in tax-efficient savings vehicles, either through existing tax-deferred plans or the new savings account.

Financial Markets

To be able to save and invest with confidence, you need a financial system with integrity. Fortunately for Canada, just as our strong economic fundamentals, balanced budgets and tax relief have helped us deal with global challenges, so too have the traditional strengths of our financial system. For one thing, Canadian financial institutions have a low exposure to the subprime market. They have not invested heavily in securities backed by U.S. subprime mortgages. Moreover, Canada's subprime market represents less than 3 per cent of outstanding mortgages. Our housing market remains sound and has not experienced the same stresses as in the United States. Canada's financial sector is considered one of the most highly developed and sophisticated in the world. According to the IMF's recent Financial Sector Assessment Program Update, Canada's financial system is resilient and capable of weathering substantial financial stresses.

As I mentioned previously, the majority of Canadians are saving. More than half of all Canadians have Registered Retirement Savings Plans. And we expect that number to grow with the introduction of the Tax-Free Savings Account.

According to another recent national survey:

- 96 per cent of all Canadians hold a bank account;
- 46 per cent used the Internet to do at least some of their everyday banking; and

- Only 7 per cent have used a storefront cheque-cashing service.

Improved Financial Literacy

All of this suggests that Canadians have a good, basic understanding of their financial choices. Still, the financial world today is far from basic, which means more must be done to strengthen the nation's overall financial literacy. Canada has continued to strengthen the framework overseeing the financial sector. Our focus has been to provide the best consumer protection environment possible, one where there is competition, where information is disclosed, and where consumers are able to make informed choices. One of the best ways to foster competition in financial services in Canada is through our statutory, five-year review of our financial institutions legislation. In our last review completed in 2007, we further promoted competition through the simplification of the entry framework for foreign financial institutions. The review also included measures to permit credit unions and caisses populaires greater flexibility to expand their business. We're also making sure that regulation continues to be updated to better reflect a modern, innovative economy. This is why, in my 2007 budget, I released a separate plan intended to create a Canadian advantage in global capital markets.

Our global capital markets plan has four key building blocks:

1. Improving investor information by promoting financial literacy;
2. Strengthening market integrity by enhancing investor protection;
3. Creating greater opportunity for business and investors by pursuing free trade in securities with the United States and other Group of Seven (G7) countries; and
4. Enhancing regulatory efficiency by creating a Common Securities Regulator that is principles-based, proportionate, and tailored to the unique makeup of Canada's capital markets.

Principles-based regulations are also critical to ensure our financial sector is capable of constantly introducing new products and services. To this end, we will be moving forward with final principles-based regulations on principal protected notes this spring. These notes guarantee the invested principal and offer returns linked to returns on an underlying investment product, which can range from a relatively straightforward basket of equities to less transparent investments such as hedge funds.

When these notes were first introduced by Canada's financial institutions the Government instituted detailed, rules-based regulations. But as these products grew more varied and complex, it became clear that the old disclosure rules were no longer adequate.

Financial Literacy

To make the most of our financial services sector, people need to be informed. They need to be financially literate. Knowledge is power, as they say. One of the primary ways we are increasing financial literacy is by building on the success of the Financial Consumer Agency of Canada. The Agency was created in 2001 to ensure that financial institutions adhere to consumer protection policies.

The Financial Consumer Agency develops financial education material on a wide range of financial products and services. It conducts numerous activities to educate consumers and create awareness of financial issues.

The Agency released findings recently on Canadians' knowledge on debit cards showing that, while Canadians use their debit cards frequently and for a wide range of transactions, more information is needed about consumers' liability for fraudulent use of debit cards. The Agency also updated its publication summarizing the fees and features of more than 200 credit cards available in Canada. This is valuable information that will benefit consumers.

Savvy consumers have also turned to the Internet. Traffic on the Financial Consumer Agency's website has grown steadily to 1.5 million visits in 2006-07. The same year, the Agency distributed more than 770,000 publications and fielded more than 32,000 calls, e-mails and letters from consumers.

Part of this public interest is the result of innovative features such as a web-based mortgage calculator. It quickly determines mortgage payments and the potential savings resulting from prepayments. The Financial Consumer Agency also provides online tools that help consumers shop around for the credit card and banking package that best meets their needs.

It is important that the Financial Consumer Agency continues providing in-depth, non-commercial comparisons of the various products available on the market. It is also critical that it goes further to make consumers more knowledgeable about the products themselves.

That's why our capital markets plan highlighted the need for the Agency to expand its efforts in sharing information with its partners across the country. It also highlighted the need to educate consumers about the growing inventory of financial products and services in a way that is simple and straightforward.

In our two most recent budgets we've allocated the funding necessary to enhance financial literacy. Budget 2007 provided funding over two years for the Financial Consumer Agency to create educational materials, for young Canadians in particular, and to better share this information with governments and private sector partners.

In this year's budget we further emphasized the Agency's role in promoting financial literacy by allocating additional, ongoing funding.

There are a number of initiatives now underway in Canada to strengthen financial literacy:

- An agreement with the British Columbia Securities Commission to adapt its high school financial literacy program into a Canada-wide web-based version;
- A pilot course to help teach young Canadians the basics of financial literacy;
- A financial literacy web portal to help support financial literacy programs; and
- Numerous partnerships with non-profit organizations to share information and good ideas.

Through increased funding, the Financial Consumer Agency of Canada is making continued progress in reaching out to Canadians and helping them better inform themselves. Our government strongly supports this, and is demonstrating that it is ready to invest the time and money necessary to make their efforts a success.

In fact, this September I plan to attend an important conference sponsored by the Agency that will bring together key players in Canada's financial literacy community to discuss areas where consumer education is currently working and gaps that need to be filled.

Along with this conference, our government is conducting key research in financial literacy, including a national survey measuring the financial capability of Canadians. This research will supply much-needed data on improving the country's financial knowledge, and identify the areas where greater effort is needed. Clearly, we are making progress. This survey, the upcoming financial literacy conference and the Financial Consumer Agency's ongoing work will make a real difference. It will provide people with the ability to make more informed financial decisions. This is in the best interests of all Canadians.

Conclusion

Now I've gone on for almost as long as it seems. I would like to conclude with a few final thoughts.

Since our nation's very beginnings, Canadians have worked hard to build a country with a growing economy and a solid financial foundation.

Those that came before us would have been astounded at the modern conveniences of today: the financial products and services that enable people to afford the necessities and luxuries early in life and eliminate years-and, in many cases, decades-of simply doing without.

Of course, if they were still here today, they would also cast a very sceptical eye on some of the behaviours that played a part in the current financial turmoil.

I'm sure they would tell us, quite rightly, of the dangers of making a promise you're not sure you can keep, and in investing in something you know little or nothing about.

Again, the best decision is an informed decision. Especially in the fast-paced global market we now live in.

It's time to get serious about financial literacy.

We must ensure our children and grandchildren understand our markets and our financial products and services. Our collective prosperity depends on financial sectors society can trust, and rules that are fair and can be followed.

I commend the OECD and the U.S. Treasury for the hard work in making this week's conference a reality. Your timing is impeccable, and the results of your knowledge-building efforts will have a value everyone can understand.

Thank you.

SESSION V- CREDIT: CHALLENGES AND OPPORTUNITIES

Chair: Thomas Wieser, Director General for Economic Policy and Financial Markets, Federal Ministry of Finance, Austria, Chair of the OECD Committee on Financial Markets

A- Bruno Levesque, Principal Administrator Financial Education, **OECD**

B- Mary O’Dea, Consumer Director, Irish Financial Regulator, **Ireland**

C- Faith Schwartz, Executive Director, HOPE Now Alliance, **United States**

D- Jane Nash, Head of Government and Regulatory Affairs ANZ, **Australia**

E- Pete Crear, Chief Executive Officer, World Council of Credit Unions

Policy Conclusions of the Chair

- Facilitating access to credit plays a crucial role in development, but needs to be flanked by adequate policies
- Financial education is not a panacea, as financial problems for credit users stem from numerous sources
- Policy makers need to be aware that financial education is a cross cutting issue of importance for consumer protection, financial market stability and other important policy areas. Benefits from financial education will be mutual to credit providers and users.
- Policies need to increasingly not only focus on credit providers and users, but on intermediaries
- Frameworks for disclosure should focus on being easily understood, and focused
- Audited responsible lending practices appear to be a best practice for the sector, e.g. as unsolicited products and unsolicited changes to products (often through cold selling) are one of the main risks to consumers
- Cost comparisons of products and between institutions need to be facilitated, and costs, risks and benefits of products should be made easily understandable
- Cooperation between the industry and NGOs on financial education in the areas of prevention and resolution will be beneficial to both sides.

A- OECD's draft good practices on financial education and awareness relating to credit

Bruno Levesque, Principal Administrator Financial Education, OECD

OECD Financial Education Project

Responding to the concerns of member governments, the OECD launched a comprehensive, high-level project on financial education in 2003. This project has produced a large number of concrete outcomes in three main areas: international cooperation, analysis and standard setting.

International cooperation. The OECD is providing an international forum in which to exchange information on recent national experiences in financial education using a three-prong strategy.

First, the OECD holds high-level international events and global forums on financial education, which allow key financial education stakeholders to engage in a dialogue on financial education in the international arena, to share experiences, and to discuss best practices, including OECD's international principles and good practices. Such events have so far been held in India, Russia, and Turkey, and we are glad to have contributed to the current conference, organized jointly by the US Treasury and the OECD. The next OECD international conference on financial education will be held in Indonesia in October 2008.

Second, the OECD has recently established the International Network on Financial Education, which brings together high-level public officials from more than 50 OECD and non-OECD countries to discuss issues, new developments, experiences, and programs related to financial education. The network allows government experts to exchange good practices and to discuss international OECD guidelines and principles in the area of financial education and awareness before they become publicly available. The first meeting of the Network was held in the margins of this conference, and the next one will be held in October 2008 in Indonesia

Finally, an important new component of the OECD strategy is the International Gateway for Financial Education, www.financial-education.org, which was launched in 2008. The gateway serves as an international clearinghouse for financial education programs and issues around the globe and as a platform for the exchange of information, including on emerging good practices.

Analysis. A key milestone of the OECD project is the publication, in 2005, of the first major study on financial education at the international level, entitled *Improving Financial Literacy: Analysis of Issues and Policies*. The Organisation has since then developed analytical papers and methodologies on a wide range of issues related to financial literacy; the current analytical work focuses on financial education in selected sectors (credit and pensions), locations (schools, workplace) institutions (financial intermediaries). It also addresses the more fundamental issues related to risk transfer to households, as well as new methodologies to assess financial education and literacy.

Standard setting. In 2005, the OECD Council formulated its first international *Recommendation on Principles and Good Practices for Financial Education and Awareness*. These principles address the role of government, financial institutions, employers and the design of financial education programmes. With the support of the G8 Finance Ministers who called on the OECD in 2006 for “*further development of financial literacy guidelines based on best practices*”, as well as the OECD Council's invitation to identify further good practices, the OECD confirmed its international leadership on development of guidelines and standards in financial education. In 2008, this work included two new OECD recommendations on financial education in pensions and insurance, while

current work, developed by various OECD Committees and hundreds of governmental delegates, focuses on the development of international guidelines and good practices in the area of credit.

OECD Credit Project

Background

Why has the issue of credit been identified as a priority area for OECD's financial education project? In recent years across OECD countries, governments, financial institutions and others concerned about social welfare have become increasingly worried about the growing levels of debt taken on by consumers. Increased mortgage borrowing and the misuse of credit cards have resulted in excess indebtedness, and a rise in credit delinquencies, insolvencies and personal bankruptcies. Moreover, the emergence of alternative banking products and predatory lending are posing serious consumer protection concerns. Yet the abilities of consumers to use credit effectively and manage their money successfully are fundamental skills. Failure to develop debt management skills can cause consumers to suffer, at best, financial distress and, at worst, major crises, which can have severe consequences and lead to significant losses for financial institutions (as creditors). Despite this risk, there seems to be a persisting lack of tools and resources available to ensure that consumers have the essential financial knowledge and skills needed to manage personal credit and prevent excess-indebtedness or repair bad credit.

There have been a number of recent developments in the markets that call for enhanced financial education programmes and initiatives aimed at strengthening consumer knowledge and awareness in the area of credit:

The changing importance of credit use: the rise of household credit in OECD countries has been fast, and data on household total debt, household debt as a percentage of disposable income and mortgage loans as a percentage of household debt show worrisome levels of consumer indebtedness as a direct effect of credit expansion in a large number of OECD countries and non-OECD economies.

Flexible regulation based on disclosure: Despite regulatory frameworks in place to govern disclosure of credit information, consumers seem overwhelmed by the complexity and quantity of information. Even sophisticated consumers show weak understanding of their credit agreement, low awareness of their rights and responsibilities, and little shopping around for the best credit terms and conditions.

New credit users: there has been, in recent years, a sustained increase in the number of new credit users, both in emerging markets and developed economies. A large number of consumers newly exposed to credit most often do not understand the terms and conditions of the credit products they are using, have not shopped around to compare options and do not know how and where to get neutral advice and information.

New credit players: brokers and other intermediaries are now playing a much more active role in distributing credit products to consumers (such as residential mortgages). The growing presence of intermediaries in credit markets poses new challenges for consumer protection and awareness.

New credit products: parallel credit markets are rapidly developing outside traditional (or mainstream) financial institution infrastructures and regulatory frameworks, to serve the more vulnerable consumers who do not have access to common credit options. Consumers have been increasingly using these alternative credit products despite their high cost and often prohibitive terms and conditions.

Confidence and market dysfunctions: The recent sub-prime mortgage lending crisis has raised a number of questions related to the information provision and disclosure, one of which concerns the ability of consumers to understand sufficiently the nature of the financial products that they are buying into.

Analytical report

In order to pursue its work around the development of financial education guidelines and good practices, and particularly to address financial education and literacy concerns related to credit, the OECD has begun an analysis on a large range of credit-related issues affecting consumers of financial services. The first step has been to commission a consultant report⁵⁹ to identify the main contemporary areas of concerns linked to consumers' use of credit, and to provide some directions for the development of OECD's financial education good practices in this area.

The paper, developed by Fortin and Prefontaine, examines some emerging issues regarding consumer protection and information in four OECD countries: Australia, Canada, the United Kingdom and the United States. These four countries have much in common yet develop their own specific experience. By comparing their recent experience, the consultants identify some questions of emerging importance.

To realize this goal, they first analyze the extent of credit use. Because residential mortgages represent the main source of household debt, the authors link the trends in total indebtedness to the housing booms and busts. They identify securitization has an important new feature of mortgage funding. They also look at the causes for the growing importance of revolving credit and show that a large part seems to be due to a substitution from non revolving credit. Nevertheless, total indebtedness seems to translate into a growing financial stress as personal insolvencies are on the rise.

The authors also look more closely at two important issues in the mortgage market that have implications for credit availability of higher risk borrowers, that is, the growing presence of securitization and that of mortgage brokers. They explain how the incentives of market participants are modified because the mortgage market generated more up-front incomes to lenders and brokers. This has led to a reduced pricing of risk. They also identify some 'areas of concern', such as the regulation of mortgage brokers, the adequate pricing of risk and the cost of credit disclosure in mortgage loans in the US. Finally, they explore if the subprime crisis can be linked to a failure in consumer protection.

Finally the report defines alternative banking, the nature of the operations on this alternative market and compares the extent of alternative banking in the different countries. Then the authors look at challenges in regulating alternative banking, and conclude with the challenges posed by credit counselling agencies and credit reporting.

The four main conclusions of the report can be summarized as follows:

1. Based on the recent developments in the mortgage market the authors identify a number consumer protection implications linked to securitization: 1. Securitization made adequate risk pricing difficult, so that credit become easily available to high risk borrowers. 2. Securitization reduced the lenders' incentive to scrutinize loan applications, as loans are sold rapidly. 3. Securitization facilitates the distribution of mortgage by non-deposit taking institutions, reducing the effectiveness of consumer protection achieved through bank regulation. 4. In

⁵⁹ See consultant Report by Mario Fortin in Vol. II.

parallel, mortgage distribution by brokers poses a new agency problem for consumer protection.

2. A second area of concern is the growing dependence of low-income and low-educated households on alternative banking. Being blocked from mainstream banking, these vulnerable consumers are operating with less protection, pay more for credit and, more generally, for basic financial services.
3. A third area relates to credit counselling agencies. The authors show how the industry has developed with a growing presence of agencies that are increasingly interested in making profit by negotiating debt management plans for which they receive a fair-share for lenders. Given the growing financial stress, the authors identify this as an urgent issue for consumer protection.
4. Finally, the report indicates that credit reporting and credit scoring are increasingly used to give or refuse access to credit. In this context, it becomes important to look to the conduct of the agencies that collect the financial information and calculate the credit scores. It is also of growing importance that consumers be aware of the information in their credit report and be able to protect the accuracy and privacy of this information.

OECD's Draft Good Practices

This report has been very useful in allowing the OECD to identify good practices. The work is meant to cover general good practices applying to any credit product, with some special tentative considerations given to mortgage products and issues. The good practices provide guidelines on the roles and responsibilities of the main stakeholders (governments, market players, social and business partners) in enhancing public awareness and capability on credit issues. The good practices also provide directions on the design of programmes and initiatives aimed at raising awareness and strengthening education on credit issues.

The good practices have been submitted to the CMF and IPPC, as well as the members of the recently created International Network on Financial Education, for input. The good practices should be finalised by the end of 2008.

B- Mary O’Dea, Consumer Director, Irish Financial Regulator, Ireland

The following presentation looks at some of the issues that have faced the Irish Financial Regulator in terms of Consumer Protection and Education and how they are linked together.

The strategy within the Irish Financial Regulator is always consumer led; the Regulator talks to and consults with consumers, holds consumer focus groups and issues consumer surveys. As part of the education programme, the Irish Financial Regulator also goes out to schools and talks to kids about what financial issues are relevant to them.

As the topic of Ms O’Dea’s presentation was credit, she wished to share with the participants what the Irish Financial Regulator has been doing for consumers to better prepare them for the opportunities and challenges presented by credit and also to outline their approach to education. The Irish Financial Regulator has officially adopted the OECDs definition of financial education. It is defined as a process by which consumers improve their understanding of financial issues, through information, instruction and objective advice. As a result, consumers develop the skills and confidence, which is a very important part, to become more aware of financial risks and opportunities. Therefore, consumers can make informed choices and better decisions, know where to go for help and to take other effective actions to improve their financial well-being.

However for adults, education is a choice. It needs to complement the Consumer Protection and regulatory work the Financial Regulator does and is not a substitute for it. Providing education is also expensive and resource intensive. As a result, the Regulator needs to demonstrate the outcomes from spending these resources. Most regulators do not have a competence in education. It is vitally important to get educational professionals involved from an early stage as they have the necessary expertise. It is also vital that the importance of financial education is fully appreciated by the education sector.

Leading on from this is how financial education fits into a wider consumer protection framework. The key consumer protection role is the “prudential supervision for a safe market”. It is sometimes hard to explain why protecting companies in terms of solvency is good for consumers. However, the recent turmoil in the credit market has provided the perfect opportunity to do so. The second pillar is the “conduct of business for a fair market”, while the third pillar is “informed consumers for informed decisions” - how the Regulator informs consumers and raises education levels.

With regards to the Consumer Protection Code and the provision of credit, a statutory Consumer Protection Code was introduced in Ireland in July 2007. As the Irish Financial Regulator is a single regulator, the Code covers banks, insurance companies, brokers and other retail financial services providers. It will also cover sub-prime lenders in the next couple of months. Lending provisions in the Consumer Protection Code include;

- “know your customer” and suitability requirements applied to all areas of credit – making affordability a key factor in the granting of credit. When a consumer is getting a loan, the institution must be able to demonstrate that the product is suitable for that customer and must keep a record of this suitability so that the regulator can check.
- a ban on unsolicited, pre-approved credit and unsolicited increases in credit card limits. Before this was introduced, on credit cards alone, over 42,000 notices a month were going out to consumers saying, “we hereby increase your credit card limit”. Now, the consumer must initiate contact and must apply directly to the bank for an increase;

- statutory disclosure notices for mortgage and debt consolidation advertising. Consumers are inclined to wrap up their mortgages. Institutions now need to give the new cost of credit, so as to enable consumers to compare their old situation with their new situation and know how much the extra credit is costing them;
- a requirement to give important information “in a way that seeks to inform.”;
- that arrears handling procedures must be in place; and
- that complaints handling procedures must be in place.

The challenges facing the Irish Financial Regulator in the regulation of credit are first and foremost in striking the right balance;

- stakeholder expectations – while certain stakeholders may be calling for caps on interest rates, it may not be the answer;
- if consumers want credit - refusing credit often offends even if that refusal may be in a consumer’s best interest;
- avoiding a rush to unregulated lending – when one introduces unnecessary rules for the regulated sector, it can provide an incentive for the unregulated to act illegally.

The role of regulated firms in helping consumers to meet the challenges and opportunities afforded by credit include compliance with the Code and other legislation, plus minimum competency requirements for advisors. When someone is selling a financial product, they should understand what they are selling and can better explain the product to their customers, and finally, firms have unparalleled access to consumers at the point of purchase, and are, therefore, best placed to inform and advise them.

Financial education can also help consumers meet the challenges and opportunities afforded by credit. To become financially capable, basic budgeting and money management skills are key – especially for avoiding debt problems. Consumers need skills in planning ahead and having a broad understanding of financial products can help achieve personal goals in the future. In relation to what knowledge should consumers have when buying credit, the following are vitally important;

- the cost and how it compares to alternatives. Consumers should have know about the terms, the repayment amounts, frequency etc;
- in particular, in relation to credit, the key features of the agreement and what they mean;
- the terms and conditions, which poses a challenge for regulators as people often don’t have time to read them and are not interested; and
- credit records and the consequences of not making repayments. Many Irish people are not aware they have a credit record and are entitled to access it. The Irish Financial Regulator, however, ran a campaign in relation to this issue and has a fact sheet available for people.

With regards to financial education in Ireland, the Irish Financial Regulator has a statutory role in “raising awareness among consumers of the costs, risks and benefits of financial products and services”. This in turn allows us to have a budget to work effectively on these issues. The National

Steering Group on Financial Education, (which Mary O’Dea chairs), comprises of key stakeholders in the area of financial education, within which the Regulator progresses its work. A separate agency called Money Advice and Budgeting Service (MABS) is also active in this area. It provides debt-counselling services and negotiates with lenders on behalf of those who have serious debt problems. These three strands help the Irish Financial Regulator meet the elements of the OECD definition of information, instruction and generic advice. Finally, the Financial Regulator has just finished its first Financial Capability Research Study on consumers in Ireland and will have the results shortly.

Concerning raising awareness of the costs, risks and benefits of credit, the Financial Regulator has a public information service comprising of a suite of publications on financial products. Credit publications include guides on mortgages, personal loans, credit cards and your credit record. The features on the personal finance website for consumers, itsyourmoney.ie, include information on credit products, cost comparisons of personal loans and credit cards, tools such as budget planner and loan / mortgage calculators. The use of the calculators is one of the site’s most popular tools. The Financial Regulator also has a number of channels for consumers to contact them and ask questions or seek advice. There is a personal finance help-line and an Information Centre in Dublin city.

The Irish Financial Regulator also has a role in advocating and setting standards for financial education via the National Steering Group. As a result, a competency framework has been drawn up. It sets out to establish what is a financially capable person at all different ages and levels. A sample of the competency framework, in relation to credit, is outlined below:

Areas of Learning	Foundation knowledge, skills and concepts	Researching and evaluating information and advice	Coping with problems and the unexpected	Social and personal issues about finance
Broad Learning Outcomes	Budget for daily spending	Critically evaluate and compare information	Plan for changes in their personal circumstances	Analyse their own financial needs and wants
Levels Leading to Specific Learning Outcomes	<ul style="list-style-type: none"> • Understand the basic types of borrowing • Manage an appropriate level of debt • Plan to absorb rising interest rates • Understand the consequence of defaulting 	<ul style="list-style-type: none"> • Access Information provided by firms and other sources. • Compare costs and benefits • Compare how different forms of credit affect the ownership of assets 	<ul style="list-style-type: none"> • Prepare for a loss in income • Anticipate and plan for growing expenditure • Understand the options for dealing with debt problems. 	<ul style="list-style-type: none"> • Prioritise needs over wants • Explain life events that lead to the need for planning.

Finally, one of the journeys the Irish Financial Regulator went through is finding out what it is that people feel comfortable talking about with regards to financial education? The key thing the “On the Bus” advertising campaign highlighted is “come to us”. The ad dramatically increased public awareness of the Financial Regulator and it captures the public imagination with different amateur remakes of the ad on youtube. In the end, the Regulator can be authoritative when it wants to be and consumer friendly when it needs to be and the ad helped the Financial Regulator tune into and connect with its target audiences.

C- HOPE NOW: Connectivity, Clarity and Education

Faith Schwartz, Executive Director, HOPE Now Alliance, United States⁶⁰

In the context of the housing event, the U.S. has been experiencing an asset bubble; specifically, the U.S. is coming off a double-digit annual appreciation in housing. In the last several years, there has been the introduction of complex and exotic loan instruments, certainly in the subprime market. This is thought to be the 228 and 327 hybrid arms that carry adjustable rate mortgage shock and that are different from what have traditionally been the prime mortgage instruments.

In addition, the U.S. has instruments that are called the option ARMs that are generally a prime product, specifically a prime credit product that has a negative amortization if the full payment is not made by the borrower. The U.S. also has interest-only types of products that were meeting the affordability issues regarding the double-digit housing appreciation and the lack of affordability in key markets. The securitization and risk transference to multiple investors has made this problem in the housing crisis more complex due to dealing with several different investors that are backing the loans. In addition, there has been housing depreciation. The U.S. has leveraged borrowers across the spectrum and in the last number of years, not only the subprime cash out refinance, but also a cash out refinance throughout the whole housing market where people were tapping into the growth in their home appreciation over a number of years.

The U.S. is experiencing gas and food pricing increases. There has been a lot of borrower optimism over the last decade in which consumers were buying more house than they could afford. However, all the players involved were too exuberant, not only the consumers.

In October of 2007, Secretary Paulson and the Secretary of the U.S. Department of Housing and Urban Development (HUD) gathered together lenders, investors, nonprofit housing counselors, and industry trade organizations throughout the country to represent housing market participants and ask them to come together and help solve the problem. The solution they were seeking was how to help minimize foreclosures and find a way to keep people in their homes. This process was a culmination of many meetings with all the participants. After interviewing many people, the recommendation from the government was to get together as an industry and start solving the problem today in every way they can.

One of the primary objectives of the representatives of the housing market was to find a way to effectively communicate with the borrower. Traditional loan servicers who service the mortgage debt service on behalf of investors are used to collecting payments and very few borrowers who are in trouble are in touch with their lender or servicer.

Borrowers can be educated about alternatives to foreclosure and new ways of working with lenders, servicers, and third party housing counselors can be created so that a third party can be trusted on behalf of the borrowers.

Hope Now is an alliance among all these different parties and it brings together people who often did not talk to each other on a daily basis, but disparate interests have become very much aligned. Keeping people in their houses is good for everyone, the banks, the regional economy, the global economy, and certainly for the borrowers. The advantage of using the housing counselors is a very important component of this effort.

⁶⁰ This summary has been extracted from the transcript of the OECD-US Treasury International Conference on Financial Education and reviewed by the author.

One out of two people that have traditionally gone to foreclosure never talk to their lender. Typically, this is even after lenders have made numerous attempts to talk to the borrower, for example phone calls, door knockers, and letters being sent out to the home. Yet, the borrower still does not communicate with the lender. Key themes that have arisen out of the crisis have been to reach borrowers in need, counsel homeowners in need, and assist homeowners in need. These themes are the backbone of this effort and certainly improving communication is central to the issue.

When soliciting members for Hope Now, all the major servicers in the market were asked to participate, because they are the ones needed to execute and innovate in order to avoid foreclosures. Hope Now comprised approximately 90 plus percent of the subprime market securities and balance sheet loans and a vast majority of the prime market. The investors that are part of Hope Now are Fannie Mae, HUD, Freddie Mac, the trade organizations, and the American Securitization Forum who have offered tremendous guidance to the market to work through the complex securitization issues with regard to the foreclosure problem and how to avoid further foreclosures. Also included is the bond market organization otherwise known as SIFMA. Insurance companies are involved because they are in a loss position for foreclosed loans as well and are present in part of these conversations and committee structures.

Hope Now is also working with nonprofits and the leadership of the nonprofits has come from NeighborWorks America and the Homeownership Preservation Foundation. Hope Now has added the entire HUD housing counselor intermediaries who provide grassroots counseling on the ground in which face-to-face counselors meet with the borrowers on a regular basis. This has been an unprecedented effort, as it brings together investors who are not used to talking about housing counseling. There is also the issue of servicers who were not really the original lenders who made these loans -- some are and some are not. People have been very engaged at the most executive levels in this effort.

Hope Now has established free counseling for borrowers through a public domain, a hotline that was in existence, it is called 888-995-HOPE. Members of Congress have advertised the hotline by sending it out to their constituencies, promoting the hotline as an important tool that any borrower in trouble can call. Ten housing counseling intermediaries that belong to the Hope Now foundation run the hotline and 450 housing counselors back the hotline. For the first half of the year, the loan servicers who are part of the Hope Now alliance paid for the hotline. The hotline also gets other funding from the government and other sources, but this funding is minimal. The government appropriated \$180 million for all housing counseling that was distributed through Neighborworks America, and the hotline received some of that funding. The hotline receives over 4,500 calls a day from borrowers in distress and has provided counseling to 200,000 homeowners to date.

The Hope Now website⁶¹ provides information on data that has been collected and various types of work going on under Hope Now.

Hope Now has identified a gap by the people who are talking to borrowers on the ground who are not getting service by their lender or servicer: a better job needs to be done in working with the counselors who are with borrowers face-to-face or on the hotline. To address this need, every servicer agreed to establish an 800 number, a fax and an email, with a port of entry, so there is a warm handoff or information sharing at the borrower level. This communication is essential, as one out of two loans goes to foreclosure without any conversation with the servicer. In fact, Freddie Mac just released an

⁶¹ HopeNow.com

updated study, the Roper study, in which 58 percent of the borrowers said, “I’m not going to talk to my lender because they can’t do anything for me.”

However, the earlier in the process a borrower begins talking to the lender or the servicer, the more alternatives there are and the penalties, fees, and lack of payment only add to the problem if it is not early enough in the process for intervention. Every servicer needs to make a commitment to share all of their data with Hope Now, of which a report in aggregate is created and that report is available on the Hope Now website. The data comprises all of the lender’s foreclosures, the foreclosure starts that they have created and all of the repayment plans and modifications taken to avoid foreclosure. The report provides a comprehensive loss mitigation view of what is going on in the mortgage market across all sectors. It may be the largest database of loss mitigation of the mortgage market, which is helpful in informing the policy debate and the regulatory debate over these issues.

Some of the issues are often technical and difficult. For example, if it were easy to freeze all the rates and keep everyone in their homes, it would be done. There are some mechanisms in place in which it is possible to freeze rates if a borrower has the willingness and capacity to repay. The American Securitization Forum, a New-York-based trade association that is comprised of those investors who own the securities, has come to terms with a way to stop foreclosures and stop ARMs from sliding into foreclosures by those who are experiencing payment shock. It is not as material today because interest rates are currently low. LIBOR, which is much of the index for subprime loans, is also quite low again; it is over 300 basis points lower than where it started in December. Therefore, there is no additional payment shock to those ARMs. The American Securitization Forum has provided an avenue of how rates can be frozen if there is hardship and those loans could go into default.

The issue becomes further complicated by the fact that the following also need to be considered: mortgage-based securities of Fannie Mae and Freddie Mac, FHA loans through HUD, balance sheet loans, and option ARMs. In addition, there are a vast majority of securitized loans through different instruments and different investor contracts, and many regulatory and accounting issues associated with stopping foreclosures. As well, there are issues relating to how to efficiently work with and maintain effective communication with the borrower. In spite of this complexity, there has been a large amount of progress made.

Servicers have agreed to develop with counselors a standard intake form of what information is needed regarding the borrower before the hardship determination can be made. If the borrower is unable to make payments, it is essential to identify the borrower’s income and expenses and to identify a debt plan and a management plan. This has all been part of the Hope Now Alliance effort.

In addition, direct mail is sent to borrowers to raise awareness of the Hope Now branding and to get people to respond if they are not responding to their servicers. About 250,000 letters a month get mailed. Direct mail is sent at 60-days late or more to borrowers who have not been in contact with their servicer. It is the most at-risk borrowers who will indeed go to foreclosure if there is no contact.

Direct mail has garnered approximately a 20 percent response rate. Generally, these respondents have been bombarded with efforts prior to this but have not responded to their servicer. Hope Now is encouraged by these results. There are about a million and a half loans with letters out, and 20 percent of that is a form of loss mitigation.

Hope Now also has worked with NeighborWorks America on funding an ad council campaign and it has spent a couple of years raising media awareness to encourage borrowers to contact their lenders.

Hope Now helps to facilitate third-party housing counselors. It holds home ownership forums across the country in the hardest hit areas and partners with local government, city and national government, as well as the Federal Reserve and others to host events where lenders attend. Housing counselors are there and anyone can get help for free. These events have been a great success. Recently in Foxborough Massachusetts, a suburb of Boston, the event had 2176 homeowners attend.

The Hotline serves a greater volume of borrowers, as more than 4,500 calls are received a day. The counseling hotline is open 24 hours, 7 days a week, and it has Spanish and English. Some of the intermediaries also have other languages that they can support. In addition, Hope Now has been mailing out letters and in the first quarter alone, 500,000 loans have avoided foreclosure due to these concerted efforts; specifically in the form of modification or repayment plans. For example, a short-term repayment plan might be drawn up to handle temporary unemployment. Hope Now has been working hard on measuring results since July, and the data is showing that since July, 2 million loans have avoided foreclosure.

Another model that Hope Now is trying to put in the market, is fee for service agreement with investors to participate in foreclosure prevention counseling. Fannie Mae and Freddie Mac have already agreed to participate. Hope Now is working with the American Securitization Forum to get a model in the market soon so that servicers, counselors, and investors have a better framework going forward.

Hope Now's tour has been very successful and is continuing to think of ways to be more impactful going forward. Hope Now's objective is to get better practices in the market, principals, and establish a base for lender servicers. In addition, a central objective of Hope Now is to create a model in the market that is workable through any kind of housing crisis, and when not in the face of a crisis, to be better prepared.

There are certainly interests aligned in this process and the leadership from all sections and sectors of the economy and housing market who come together and really put in their good faith and effort has been inspiring. It is definitely making a difference. Foreclosure starts in the United States are startling, yet less than half of those ever go to foreclosure. A couple of months ago, that was about 35 percent. It is higher now, but it is still well under 50 percent. Hope Now is endeavoring to find a way to get ahead of that statistic, to turn the corner, stop houses from going into foreclosure, increase borrower communication so that there is willingness and capacity to repay and strengthen communication and service levels at the lender's institutions.

Certainly financial literacy is a key issue and it is essential that it be delivered in a scalable way. Financial literacy is a central issue with consumers who leverage and try to get a house that is bigger than what they could afford, or who need to cash out in order to pay their bills. Hope Now supports all efforts towards financial literacy with the outcome being more homeowners stay in their home.

The Federal Reserve has done an extraordinary job along with the other bank regulators on the guidance that has been provided to the market, on practices and on risk layering. Much of the crisis centers on risk being layered across the mortgage market and its shift in the last few years. The final rule of the Federal Reserve will be far reaching and transformative with respect to what is originated in residential mortgages going forward. Hope Now understands that this rule will be much more limiting on risk layering, the extent of the advertising broker involvement and the food chain of the origination – this is a great step forward on minimizing risks. However, financial literacy and education will be an important component as well.

D- ANZ's Approach to Responsible Lending

Jane Nash, Head of Government and Regulatory Affairs ANZ, Australia

1. Context

Debt levels of Australian households have risen strongly since the mid 1990s under circumstances of 17 years of strong economic growth, 30 year lows in unemployment levels, real wages growth and low interest rates. Australia is currently in a rising interest rate environment and while increases in interest rates, combined with other rises in cost of living expenses have put some households under pressure, overall consumer credit quality in the banking sector remains sound.

The strong increase in household debt levels has raised questions about lending standards and the marketing practices of lenders. To make a contribution to the debate, to inform responses by governments and regulators and improve its own business practices, ANZ commissioned AC Nielsen to undertake research into why some people with borrowings and credit experience financial difficulty. This research forms part of ANZ's broader commitment to researching financial literacy, contributing to public discussion and delivering innovative financial education initiatives and programs for our staff, customers and the wider community⁶².

2. Financial Difficulty Research

In 2005 ANZ commissioned AC Nielsen to undertake research into why some people with borrowings experience financial difficulty. The focus was on the two percent of the adult population in Australia that another quantitative survey⁶³ had shown had borrowings and "felt out of control with their finances".

The researchers took a qualitative approach to examining financial difficulty, interviewing around 160 people, some individually in interviews of one to one and half hours duration and some in small groups of six to eight people. During the interviews and group sessions, the researchers explored how people with borrowings came to be in financial difficulty, their experience of financial difficulty and where the person had recovered from financial difficulty, their journey to recovery. The definition of financial difficulty was broad: it ranged from people who had not necessarily defaulted yet felt uncomfortable with the amount of money they owed, to people who had experienced bankruptcy and severe financial hardship.

2.1 Causes of Financial Difficulty

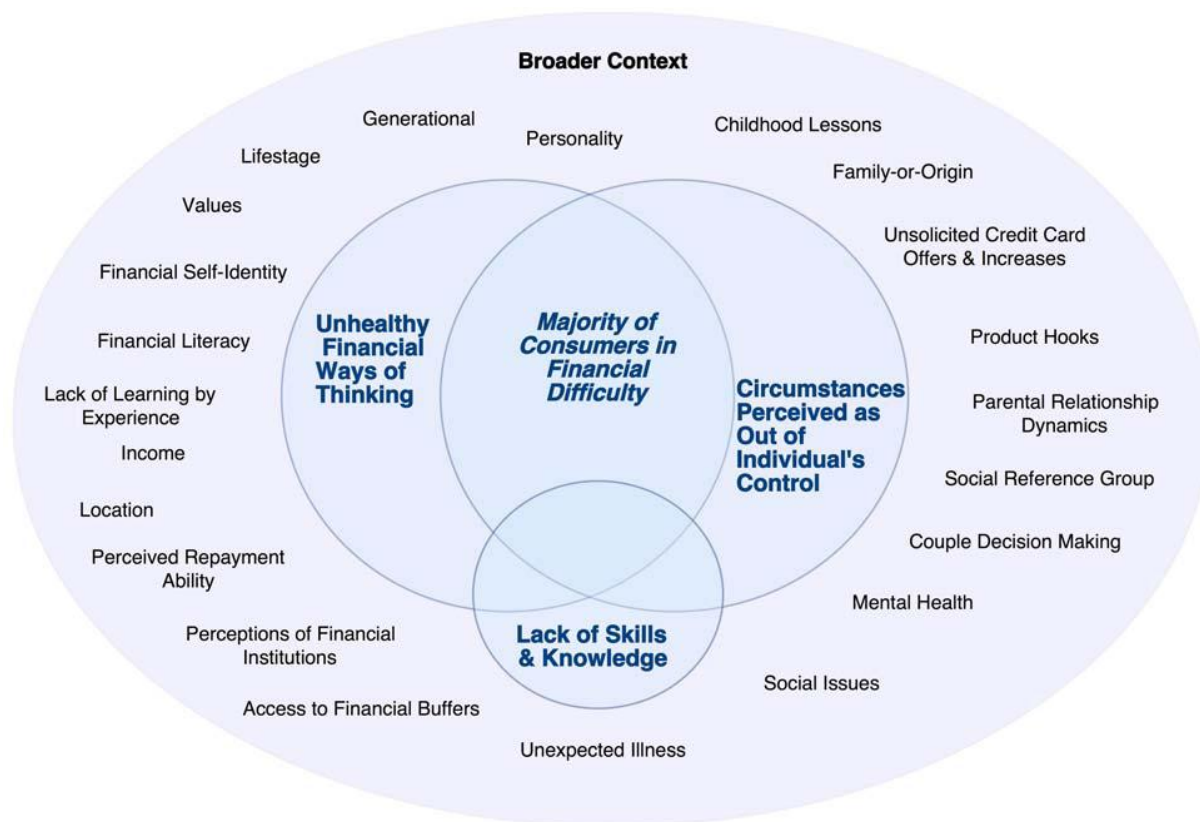
The research revealed quite a complex picture with multiple factors responsible for an individual experiencing financial difficulty in the majority of cases.

In most cases, financial difficulty resulted from a combination of unforeseen circumstances perceived as outside an individual's control, what the researchers termed "unhealthy financial ways of thinking" and to a lesser extent, lack of financial skills and knowledge. In addition, there are many influences acting on these three factors, including individual, social, family, circumstantial, lender and product variables. This is illustrated schematically in Figure 1.

⁶² ANZ commissioned Australia's first national Survey of Adult Financial Literacy, conducted by Roy Morgan Research and published in 2003 and in 2004 published research by Chant Link into financial exclusion in Australia

⁶³ ANZ Survey of Adult Financial Literacy in Australia, 2005, conducted by AC Nielsen

Figure 1: Factors Leading to Financial Difficulty



Unforeseen circumstances included job loss, ill health and relationship breakdown, all of which led to income loss and/or increased expenses. People involved in the study also displayed a number of ways of thinking about their finances that guided their actions and behaviours and which had a negative impact on their finances. It is these ways of thinking that are termed 'unhealthy' and they included:

- 'living for today' – focusing on the present not the future and the consequences of today's spending;
- 'financial disengagement' – no interest in managing finances, either current or future, so no monitoring and no taking responsibility for spending;
- 'aspirational' – spending to 'keep up with the Joneses';
- 'emotional enhancement' – spending to feel better;
- 'ownership of credit' – over time developing an attitude of 'it's my money' as opposed to credit that needs to be repaid; and
- 'credit as supplementary income' – 'I need more to live': to supplement a low income, to replace a loss in income or for those with higher incomes to support a 'lifestyle'.

For a full discussion of the factors leading to financial difficulty see the research report *Understanding Personal Debt and Financial Difficulty in Australia*, November 2005, by AC Nielsen⁶⁴.

2.2 Role of Financial Literacy

Low levels of financial literacy were identified as a contributing factor rather than a primary cause in most cases. In many instances it appeared that the individuals had a reasonable level of financial literacy and knew what they should have done. However, they did not apply that knowledge, it was “dormant” and they appeared to suffer from ‘over confidence’ in that they did not believe that things would go wrong and they would experience difficulty. The challenge for financial educators with this group is to have them activate and use their dormant knowledge and skills.

In a small number of cases, low levels of financial literacy appeared to be the primary reason for an individual’s financial difficulty. This group included people who had run small businesses that had failed and elderly people whose skills and knowledge did not adequately equip them for today’s more complex financial world. The challenge for financial educators with this group is to lift their financial literacy levels.

2.3 Role of Lenders

For the majority of people in this study – reflective of the two per cent of the population who had borrowings and felt out of control - lenders could be seen as indirectly influencing an individual’s path to financial difficulty. For example, the majority of people in this study with credit cards had received unsolicited credit limit increase offers and around half had accepted them. Acceptance in many cases occurred where there were pre-existing ‘unhealthy ways of thinking’ and the offer provided the opportunity to access credit. Acceptance was also underpinned by a perception that ‘it must be okay’ because the lender had sent it out, coinciding with a behaviour of not reading the parameters of the offer. Once in financial difficulty, a small number of people felt powerless to negotiate with lenders, and said they received little understanding and flexibility from lenders overall. Experience of financial difficulty also tended to coincide with reduced or no choice about where people could borrow, forcing people to borrow from fringe lenders rather than from mainstream lenders. Loans from fringe lenders tend to be high cost and can compound the borrower’s financial situation.

The challenge here is for lenders to market their products responsibly and to be responsive and appropriately flexible in dealing with customers who show signs of financial hardship.

2.4 Role of Financial Counsellors

In addition to identification of factors leading to financial difficulty, the study documents the experience and significant impacts on individuals of falling into financial difficulty, and also, on the positive side, outlines some of the ways that financial difficulty can be overcome.

The experience of financial difficulty and its emotional impact and the ways people respond to it indicate that the consequences of falling into financial difficulty can be very severe, causing individuals considerable hardship, stress and unhappiness. However, the study also identifies a variety of pathways that some people have been able to follow to overcome their difficulties. In particular, it is clear that financial counsellors can play a powerful and positive role in assisting individuals to address the financial difficulties and hardships that they face.

64. The research report is available at <http://www.anz.com/aus/aboutanz/Community/Programs/FinSurvey2005.asp#causes>

3. ANZ's Response

ANZ has responded to findings from its surveys of financial literacy in Australia, the financial difficulty research and discussions with financial counsellors and others, both through changes to the way it does business and with programs it runs in partnership with community organisations.

3.1 Responsible Lending

3.1.1 Responsible Lending Promises

In 2005 ANZ was the first Australian bank to introduce responsible lending promises. The promises are part of a 'Customer Charter', which sets out benchmarks for service to personal and small business customers. Performance against these benchmarks is reviewed annually by an external auditor and the results are published.

Under these promises ANZ credit card customers will not receive an unsolicited credit limit increase offer if they:

- Have repeatedly been overdue in making repayments or only made minimum payments in the previous six months;
- Have an ANZ account receiving Government benefits.

As a result of these promises, the pool of customers who would have otherwise received a credit limit increase offer reduced by around 11 per cent.

Other promises made about responsible lending are to:

- Provide information about easy and efficient ways to reduce your credit card limit;
- Ensure the minimum monthly credit card repayment does not fall below 2% of the outstanding balance, unless the customer:
 - is in financial difficulty and we are assisting with reduced repayments;
 - has accepted a special offer where for a specified period either no interest or a concessional interest rate is charged and no repayment is required;
- With any credit card limit increase offer:
 - outline how much the minimum monthly repayment would increase if the offer were accepted;
 - recommend the offer be rejected if personal circumstances have changed;
 - Include information about how to request a lower offer;
- Explain in clear and simple terms how interest on a credit card or loan is calculated and charged, what fees may apply and when, and the consequences of late credit payment;
- Respond within 48 hours to customers who have contacted us by telephone, and within five days to customers who have contacted us by letter, to advise us of financial hardship. We may also refer a customer to an accredited financial counselor.

3.1.2 Tools, Information and Products

In addition to responsible lending promises, ANZ offers on-line tools and information to assist customers to manage their credit cards. For example, a credit card payoff calculator allows customers to work out how much they need to repay on their credit card balance each month to clear their debt within a specified timeframe. Information about how credit cards work and about how to responsibly manage a credit card is available on-line. On the product side, a credit card that rewards repayment rather than spending with loyalty points was introduced in 2007.

3.2 Improved Approach to Assisting Customers in Financial Difficulty

Even with responsible lending practices it is inevitable that some customers will experience financial difficulty, often due to circumstances outside of their control. With input from financial counsellors, ANZ is refining the way it interacts with customers in financial hardship and also piloting an early assistance program for credit card customers.

A refined approach to financial hardship involves:

- Building staff capacity to approach customers proactively and offer assistance in a way that is respectful and sensitive;
- Establishing an organisation-wide definition of hardship that is based on a customer's ability to pay rather than the causes of hardship; and
- Taking a customer's word in good faith rather than seeking proof of hardship.

In June 2007 ANZ commenced a pilot to contact credit card customers who may be showing early signs of financial difficulty. For the pilot, we chose customers who were close to or had exceeded their credit limit, even though they may not have missed payments. The intention is to offer assistance to those customers at an early stage before their situation becomes unmanageable. Customers contacted were offered options of temporary fee waivers or reduced minimum monthly payments to help them stabilise their finances with the objective of avoiding serious credit problems. ANZ is continuing to monitor the accounts of customers who took up these offers to see whether the early intervention has made a difference to default rates.

3.3 Building Money Management Capabilities

An adult learning program called MoneyMinded was funded by ANZ and developed by educators. MoneyMinded is unbranded and has been used by community partner organisations and financial counsellors to build the money management skills and capabilities of 50,000 people to date. ANZ needs to take a responsible approach to lending and we also believe that it is important that our customers have the skills and capabilities they need to make sound decisions about money.

The ability to save and having a savings buffer are also important for keeping people out of financial difficulty. Saver Plus is a matched savings program funded by ANZ and run in partnership with the Brotherhood of St Laurence. The program is delivered through community partner organisations.

Program participants must be working, be on relatively low incomes and save for a purpose related to education. ANZ matches every dollar saved by participants up to \$1000. The aim of the

program is to teach money management and savings skills and for participants to establish a long-term savings habit.

RMIT University has assessed Saver Plus as being effective in influencing savings behaviour – the latest longitudinal snapshot of participants who were involved up to 3 years ago prepared by RMIT indicates that 70% of them have maintained or increased their levels of personal saving since their involvement in the program, and attribute this in some part to Saver Plus.

In recognition of the need of the most vulnerable in the community for ‘fair and safe’ credit, ANZ is piloting Progress Loans with the Brotherhood of St Laurence. These are small amount loans of up to \$3000 to people on low incomes to assist with paying for essential household items such as white goods. ANZ is working with the Brotherhood to understand the best way of scaling up the program and will be conducting further market research and a formal evaluation of the program.

E. Financial Education Equals Financial Empowerment

Pete Crear, President & Chief Executive Officer, World Council of Credit Unions

I'm always pleased to speak on behalf of the world's credit unions because, when it comes to financial education, we have a good story to tell. In fact, many of us involved in financial education in developed countries can learn a lot from those who live in the townships, villages and rural provinces and states in Latin America, Africa and other developing areas and who are struggling to reach financial success.

In order to do that, let me first introduce you to the World Council of Credit Unions so you can better understand who we are and what we do. Firstly, World Council is a trade association for credit union systems serving individual credit union movements worldwide, including systems from the United States, Canada, Australia, Ireland, as well as others around the globe. We're guided by an international board of directors from those countries mentioned, as well as Brazil, the Caribbean, New Zealand, Peru and Poland

Secondly, and more relevant to the topic of financial education, perhaps, is our role as a credit union development agency for countries with more pressing financial and social needs than ours. We currently have projects in 19 countries worldwide, including places like Afghanistan, Kenya and Sri Lanka, where our field staff often have to work in the shadows of civil unrest and conflict. Our mission goes beyond the role of microfinance lender to empower individuals and communities through more comprehensive financial services programs, opening the door to eventual wealth accumulation through a balanced approach to guiding personal financial growth.

We have active financial education and instruction programs as part of our efforts in Mexico, Peru and Ecuador, where we address not only management of funds, but also proper application of those funds through the entire crop and product production and distribution system, referred to as value-chain management. Financial education also plays a role in much of what we do elsewhere, a critical factor considering the crying needs in many developing nations.

By some estimates, more than half the world's population – some 3 billion people – live on less than one dollar a day with little or no ready access to formal savings and credit services. World Council's goal, as much as possible, is to raise that economic standard and, wherever possible, improve the quality of life for the people we serve.

Much of our effort focuses on supporting financial education through credit union systems to the credit unions themselves and the members they serve. Our ongoing efforts include programs that provide financial services to people in developing countries, which allow individuals to start their own very small businesses so they can support their families and educate their children. In the best possible cases, that support also helps create businesses large enough to enable these micro-entrepreneurs to eventually employ other family and community members so that they, too, can develop greater financial independence and become part of the credit union system.

For us, that last part is a very important distinction, and one I can't emphasize enough. In the U.S., we're seeing a growing number of articles in the press criticizing micro-lenders for doing the right things for the wrong reasons and with even worse results. Providing micro-loans to many people in developing countries is an absolute necessity and a first step in helping many pull themselves out of poverty.

However, providing such loans without offering overall financial education can create false expectations among recipients, who may think that the funds are a “gift,” not a loan to be repaid. Credit given without the proper education can put people who can’t possibly earn enough to pay back even the smallest loans into a position of eventual default, leading to even worse financial problems. And credit without education creates the impression that, no matter how noble the micro-lenders’ intentions are, micro-loans may simply be another source of interest revenue for the lender. That’s because, too often, interest income ends up being the only “plus” that comes from many such loans.

The opportunity for credit, especially among people without proper collateral, comes accompanied by critical responsibilities. It is World Council’s position that financial education, especially for people who have never before had access to credit and may never have before participated in a formal financial services system, is the single most important aspect governing financial success. No credit should be given without the accompanying education in its proper use and repayment obligation.

Frankly, that wouldn’t be bad advice for a lot of U.S. lenders either, especially when it comes to marketing to youthful borrowers, many of whom also have never had access to credit nor fully participated in a formal financial system. I’m sure the alarming lack of financial education in U.S. schools causes many of us to fear that things will get worse before they get better. In terms of helping our constituency, however, World Council has taken distinct steps toward improving education, both of lenders and borrowers in countries for whom credit is new and its proper management critical to continued economic growth.

Part of our role worldwide is to provide draft policy to credit union systems and work with regulators to assure that credit unions develop the proper safeguards and accounting practices to operate with safety and soundness on behalf of their members. We welcome strong credit union-specific regulations as a way to support the systems and institutions in the countries we reach, enabling them to more effectively serve their members. Earlier this year World Council issued Model Regulations for Credit Unions, a companion volume to the earlier Model Law for Credit Unions, both of which are compendiums of recommended guidelines for suggested legislation and operational procedures for credit unions worldwide.

Among those guidelines you’ll find provisions for proper credit practices, which we believe are vital to effective credit union management and loan administration in service to members. We took a step further a few months ago, drafting a set of International Credit Union Consumer Protection Principles, which we have submitted to our members worldwide for comment.

The final principles will be posted to the World Council web site with free access to anyone who needs them. The draft is available for our field staff to share with credit unions, systems and government bodies in the countries in which they’re working. They’re also available for your review.

Experienced financial industry executives will recognize many if not all of the 9 principles we have highlighted in our draft. From a credit union standpoint, they are all designed to be member-friendly while preserving the lending institution’s enforcement capabilities. In the U.S., several of these standards are required by law and should surprise few of us here.

However, this is not the case in emerging countries, many of which have no legislation governing credit because, until recently, credit was not available to most citizens. Sample guidelines like those shown on the screen behind me may be considered luxury, not law in many countries where micro-financers have begun to make loans. It’s the World Council’s position that, as much as possible, such

lending must be governed by ethical, if not legal principles, and we're happy to share those principles we've developed with countries and in situations where none currently exist.

Let me especially draw your attention to Principle Number 8, because it speaks directly to the purpose of this panel and, indeed, this entire conference.

Principle Number 8 – Provide Education on Thrift and Wise Use of Credit – is one of the cornerstones of our International Operating Principles. Like other proposed credit union guidelines, this one speaks directly to the goal of member service, of performing functions in ways that benefit credit union members directly through financial education. As you see it even suggests aligning with and funding consumer advocacy groups to provide the best possible financial educations to borrowers and savers.

These 9 standards - and Number 8 in particular - may at first seem a little extreme. But please keep in mind what I said earlier about supporting strong regulatory oversight for the credit unions themselves. We believe with the right kind of guidance, credit unions in developing countries can accomplish their goals and even thrive in service to their members. That same need for guidance, in this case in the form of consumer education, will help the members stay out of harm's way and may even allow them to eventually thrive as well.

The more members understand about personal financial management, the more likely they are to maximize the opportunities safely and to good result. Financial guidelines are tools that, when properly used, yield positive results. That's true for members, for the credit unions that support them, and for the systems that enable those credit unions to operate safely. And it's clear to me that operating on behalf of educated members can be equally beneficial to the financial institution.

One of World Council's larger, more successful members is known most simply by the name SICREDI and represents 135 member credit unions throughout Brazil. What's remarkable about this organization is that, in world where growth among many financial institutions is stagnant, SICREDI members have grown their membership base by an average of 15 percent per year and their assets by 30 percent per year for the past five years. Those member institutions have managed that growth not by relaxing credit standards and casting their nets to encompass riskier business, but by working closely with members and taking action based both the borrowing needs and the repayment capabilities those individuals exhibit.

SICREDI member institutions grant credit based on their members' capacity to repay, a policy that is beneficial to borrowers by keeping them out of harm's way. The credit unions understand which borrowers represent higher risk and respond according by not furthering that risk nor deepening their debt beyond their capacity to repay. What's more, the financial education is ongoing, not only among youth members, but adult borrowers as well. Credit counseling takes the place of debt advisement, reducing delinquencies before they happen while at the same time building portfolio strengths by satisfying member needs.

In the end, the numbers make the case for financial education among SICREDI members and borrowers. From December 2002 through December 2007, SICREDI's member institutions have grown their loan portfolios at an average rate of 30 percent per year. During that time, the organization's aggregate portfolio grew from \$1.2 billion in loans to \$5.5 billion, with a default rate well below Brazil's market average. Member-friendly terms, including competitive rates and no pre-payment penalties, has helped drive that growth, and ongoing financial education made business safer and more profitable for SICREDI members than for other forms of financial institutions.

SICREDI's success, like that of many of World Council's other members, proves the power financial education has in serving members, while still protecting them and the institutions from unmanageable debt. At the very least, it demonstrates how successful a well-managed system can be when member education and service is taken into account.

The importance of credit, particularly as relates to developing countries, can never be underplayed. But it's only through a more comprehensive approach that includes savings mobilization efforts and financial education for both borrowers and savers that we can expect any such enterprise to thrive.

Financial education is the true source of financial empowerment. How well we oversee and administer that education, especially when it comes to managing credit, should really be considered the benchmark of our success.

SESSION VI- TOOLS II

*Chair: **Dan Iannicola, Jr.**, Treasury Deputy Assistant Secretary for Financial Education and Executive Director of the President's Advisory Council on Financial Literacy, **United States***

A- Daniel Kosicki, Policy Officer, DG Internal Market and Services, **European Commission**

B- Marcin Polak, Education Now Foundation, **Poland**

C- Kathleen M. Floyd, Executive Director, The Stock Market Game, **United States**

Policy Conclusions of the Chair

- Financial education practitioners should use innovative means of communication to promote their programs such as interactive delivery methods, viral media, and mobile phones among others. Electronic tools must be engaging and relevant to attract and retain users, and content must be of high-quality.
- Having strong electronic tools like websites is not enough. Since people who need these tools the most generally do not seek them out, financial education practitioners should utilize human channels of distribution such as teachers, community organizations, service providers and mass media.
- Expenditures on financial education technology should be evaluated as investments. This approach requires demonstrating the increases in impact and effectiveness that come with the likely upfront increase in costs for the technology. Additionally, as funding is often limited, financial education practitioners should leverage resources by partnering with other organizations.
- Financial education practitioners may also look at innovative methods of delivery that have succeeded in other fields such as those in the health field as it appeared that there are similarities between personal finance and health issues. By looking at other fields, practitioners may obtain ideas about how to use technology to bring financial education to the public in different formats.

A- Financial education initiatives of the European Commission

Daniel Kosicki, Policy Officer, DG Internal Market and Services, European Commission

The EC Competence

Financial education has become a very important issue in last years, especially in the context of the surge in financial innovation, growing complexity of financial products and the recent financial turmoil. Numerous international surveys have demonstrated consumers' poor grasp of financial matters, including in the European Union. The European Commission has recognised that enhancing consumers' understanding of financial issues is a crucial condition for the creation of the Single Financial Market. Increased financial literacy empowers consumers to make informed decisions about purchasing financial products and enables consumers to benefit from the opportunities created by the integration of financial services markets in the European Union.

The European Union has only a subsidiary role in the field of education. One of the main objectives of the EU, as stated in the Treaty establishing the European Community, is the creation of an internal market characterised by the abolition of obstacles to the free movement of goods, persons, services and capital between the Member States (Art. 3). The European Commission policy in the area of financial education activities is principally derived from this objective. However, the Treaty also refers to consumer protection, requiring the Commission to aim at a high level of protection when drafting new legislative proposals (Art. 95) and to education, encouraging the Member States to cooperate in providing high quality education and the Community to support and supplement the Member States' action (Art. 149). In addition, the Treaty specifies that a high level of consumer protection be achieved, among other things, by protecting the economic interests of consumers and promoting their right to information and education (Art. 153).

The EC Policy Documents

The importance of financial education was for the first time acknowledged by the European Commission in the White Paper *Financial Services Policy 2005–2010*⁶⁵, outlining the policy agenda of the current Commission. It was confirmed in the Green Paper *Retail Financial Services*⁶⁶ issued in May 2007, specifying the plans for supporting integration of retail financial markets in the EU. The importance of financial education was also acknowledged in the Commission's strategy paper '*A Single Market for 21st Century Europe*' launched in November 2007, whose aim is to improve the delivery of the benefits of financial market integration to the EU's citizens.

On 18 December 2007, the Commission issued a communication entitled '*Financial Education*', which underlines the Commission's support for the provision of financial education and outlines its position and plans in this area. The Communication sets out the economic, societal and personal benefits of increased financial literacy and gives an overview of the provision of financial education in the EU. The Commission sees its role in this area as raising awareness of the need to raise consumers' level of financial education, encouraging and promoting the provision of high-quality financial education in the EU, and providing some practical facilitating tools to help achieve these goals.

The Communication presents some basic principles to guide providers of financial education, based on existing best practices and taking into account the diversity of approaches to develop a

⁶⁵ COM (2005) 629 final.

⁶⁶ COM (2007) 226.

successful financial education strategy. According to the principles, financial education programmes should be accessible and actively promoted among citizens at all stages of life, beginning at primary school. In full respect of the Member States' exclusive prerogatives in the field of education, the Commission encourages national authorities to give consideration to including financial education in school curricula. Furthermore, it is essential that financial education, especially the schemes by private providers, be supplied in a fair, transparent and unbiased manner. The principles highlight the importance of national co-ordination between stakeholders, which facilitates sharing of experience and helps rationalise resources. An element of regular evaluation should also be incorporated into financial education schemes.

Finally, the Communication announces four practical initiatives aimed at promoting and facilitating the provision of financial education in the European Union. These initiatives are currently being implemented.

The EC Initiatives

Creation of a pan-European network of financial education practitioners

The main objective of the newly established Commission's Expert Group on Financial Education (EGFE) will be to share best practice and experience in the field of financial education. The group will serve as a platform for public and private providers of financial education to exchange information on high-quality financial education schemes and research running in the EU. The group will also promote contacts among the Commission, public authorities, financial services providers, consumer organisations and other stakeholders involved in the delivery of financial literacy to consumers.

As their second task, experts will advise the Commission on various issues in relation to financial education in the EU, in particular on how the principles for the provision of high-quality financial education schemes, contained in the Communication should be implemented. This non-binding advice will assist the Commission in proper implementation of the policy presented in the Communication on financial education. The members of the group will be presenting, analyzing and discussing examples of different approaches and methods of financial education teaching with the aim of verifying whether they are in line with the principles and guidelines included in the Communication. In addition, the members of the group will assist the Commission in identifying any legal, regulatory, administrative and other obstacles to the provision of financial education and provide advice to the Commission on how the identified obstacles should be addressed. Finally, the group will contribute to an evaluation of the initiatives included in the Communication on Financial Education.

The group will be composed of a maximum of 25 high level experts with practical experience and competence in the area of financial education. The members of the group will represent various backgrounds including Member State authorities, academic institutions, financial services providers, consumer organisations and other groups where appropriate. They will act in a personal capacity and be required to advise the Commission independently of any external influence. A call for applications for participation in the group was open from 14 May until 13 June 2008. The first bi-annual meeting is foreseen for the autumn 2008.

Development of an on-line database of financial education schemes and research in the EU

The Commission believes that wide reach is crucial to the success of financial education programmes. Therefore, one of the Commission's initiatives is development of an EU-wide database of financial education schemes and research aimed at disseminating information on financial education programmes across the EU. This dynamic, fully searchable "reference library" to financial education

initiatives and research in EU Member States will provide references to projects with regard to their geographical base, subject matter covered, the target audience, the method of delivery used and the contact details of the providers. It will include information about the schemes offered by both public and private providers. The database will be publicly accessible and available on Europa website. Its content will be updated on a regular basis.

Granting the Commission's patronage to selected events promoting financial education

The Commission presumes that awareness-raising events ought to take place as close to the target audience as possible, at a local, regional or national level. At the same time, debates involving various stakeholders are crucial to achieve clear definition of roles, facilitate sharing of experiences and prioritise resources. For this reason, the Commission wants to provide sponsorship to Member States and private actors in the organisation of national/regional conferences and other events, which give visibility and impetus to the issue of financial education. Private and public actors are encouraged to launch financial education programmes as well as nationwide conferences and forums for exchange of best practices and experiences in the field of financial education.

The Commission envisages honorary support for such events and initiatives by providing official patronage and offering the Commission emblem, a message of support and, if possible, participation of a Commission representative. Since there is no specific EU funding programme for financial education, currently the Commission cannot offer financial support.

Elaboration of a new module of the Dolceta website to offer support materials for teaching financial matters at schools.

'Dolceta' stands for 'Development of On-Line Consumer Education Tools for Adults'. The European Commission has been developing it since 2004. The project is contracted out to EUCEN (European Universities Continuing Education Network), which is an international non-profit association registered in Belgium and operating for almost 20 years. It has more than 200 members in 43 countries across Europe and beyond, mostly universities, but also other higher education institutions and, national networks for lifelong learning.

Dolceta goes beyond simple provision of general information and includes learning exercises and interactive material with the content being translated and adapted to the specifics of each EU Member State. The tool is tailored to consumers and professionals in all Member States. In 2006, two Dolceta modules – "Consumer Rights" and "Financial Services" – became publicly available. Five new, additional modules are currently under development: "Food and Product Safety" (to be completed by end 2008), "Consumer Education – Teacher Corner" (to be completed by end 2008), "Liberalised Services of General Interest" (to be completed by end 2009), "Sustainable Consumption" (to be completed by end 2009) and "Financial Literacy – Tools for Teachers" (to be completed by early 2010).

Dolceta Module 2: Financial Services

The aim of the Dolceta "Financial Services" module⁶⁷ is to give consumers the necessary competences to compare financial products and services in the market place and to make informed purchasing decisions. All information and examples are adapted for to each country's specific conditions in terms of legal and regulatory systems, market structures and existing institutions. The materials focus on practical issues and on common consumer problems.

⁶⁷ The module can be viewed at www.dolceta.eu

The module includes sixty-seven interactive training sessions grouped in six courses according to the six main themes: consumer credit, mortgages, running a bank account, means of payment, savings & investments. Using another criterion, the courses are broken down into three levels of complexity. Level 1 covers the basics to familiarise users with financial services. Level 2 is equivalent to a middle ground level and covers slightly more complex areas. Level 3 deals with even more complex issues and requires, therefore, a sound knowledge of financial services. A user can choose to follow the training sessions either in relation to a topic of interest or by following a path through a particular level.

In each session theoretical knowledge presented is accompanied by numerous examples, exercises, quizzes and FAQs. In addition, the site contains a comprehensive glossary of various financial terms. For those users who would like to deepen their knowledge in certain areas - links to other relevant websites are included.

Dolceta Module 7: Financial Literacy – Tools for Teachers

The Commission has just launched the work on the new Dolceta module in the area of financial services, entitled "Financial Literacy – Tools for Teachers". The new module will consist of lesson plans to help teachers include financial literacy issues in their teaching programmes.

It is important to emphasise that Dolceta is offered on a purely voluntary basis. Dolceta materials are designed to provide for an option for individual consideration by teachers. They may complement other materials, tools and schemes in use. The concerns of the national authorities in some Member States on potential overlapping of Dolceta materials with similar materials developed at the national level have already proven to constitute a non-negligible challenge to the development of the project.

The content

The objective of the module "Financial Literacy – Tools for Teachers" is to enhance young consumers' understanding of how personal finances function and help develop good habits from a young age to avoid problems in adult life stages. The ambition of the module should be to provide pupils and students with the competence to:

- Identify their own needs in relation to particular financial topics;
- "Shop around" and compare different offers;
- Find and use appropriate and reliable information to perform simple transactions;
- Predict the positive and negative consequences of different decisions and actions.

The financial literacy module is targeted towards teachers of primary and secondary school pupils. Apart from lesson plans, it will also include interactive tools, such as games, stories, quizzes, to help deliver education on financial issues in a lively and stimulating way that will be engaging for children and young people. These materials should be available in both online and printable versions.

The lesson plans should fit in easily in various subjects in the existing curricula; for example, maths, history, economics, citizenship and entrepreneurship. The set of subjects will depend on the curriculum of the particular Member State. Several lesson plans will be offered for each identified subject.

The lesson plans will be grouped according to the main areas of personal finance, such as making payments, saving and investing, and taking out loans. The list of topics covered in Module 2 – Financial Services will serve as a basis for the content of Module 7. It will be complemented by some topics particularly relevant to children (e.g. history and basic concepts of money) and young people (e.g. on-line banking, student loans, saving in investment funds). The lesson plans will also be broken down in three levels according to the age group of pupils / students: kids, younger teens, older teens.

The core of the module will be common across the EU. The country specific materials will be developed by national teams of experts to meet the different needs of students in various Member States and to allow programmes to be developed in a way that best complements existing national curricula. Like other Dolceta modules, "Financial Literacy – Tools for Teachers" will be translated into all official Community languages.

The process

The EUCEN is responsible for the overall management of the project, supported by its partners: the EAEA and UCL/Media Animations. Representatives of the Commission are involved in monitoring of the execution of the contract.

EUCEN organises the work on the project by forming the Expert and Design Teams and the National Development Teams:

- The Expert Team works on the core content as well as guidelines for exercises and interactive aspects of the new module. It consists of experts in adult pedagogy, on-line learning, and a wide range of consumer issues including financial services. These experts will also be part of the National Development Teams.
- The Design Team works on the web design and IT aspects of the new module. It consists of IT specialists.
- The National Development Teams will consist of EUCEN members coming from all 27 EU Member States. They will undertake the production of the national versions of the new module.

The EAEA (European Association for the Education of Adults) will be responsible for module testing with adult learners and their tutors and for writing of the teachers/trainers guides in all the official languages of the EU. The EAEA has 114 members in 41 countries and its members are almost all national associations for adult education.

The Université catholique de Louvain (UCL) with their partner Media Animations will provide the software and technical support to all the national teams developing this module.

The module is scheduled for launching in April 2010.

Conclusion

In the context of the growing complexity of financial products and rising individual needs, financial education is high on the EU agenda. In full respect of the Member States' exclusive prerogatives in the field of education, the Commission sees its role in this area mainly as: raising awareness of the need to raise consumers' level of financial education, promoting the provision of high-quality financial education in the EU and providing practical facilitating tools to help achieve

these goals. The four practical initiatives, which are being currently implemented by the Commission: pan-European network of financial education practitioners, on-line database of financial education schemes and research, granting Commission's patronage to selected events promoting financial education and elaboration of a new module of the Dolceta website to offer support materials for teaching financial matters at schools, should help achieve these goals.

B- The Edutainment in Action

Marcin Polak, Education Now Foundation, Poland

Introduction

Being active in economic and financial education for the past six years, I have delivered personal finance knowledge to different target groups in many ways, including workshops, seminars, booklets, school programs, essay competitions, electronic games, short movies, podcasts, multimedia presentations, internet sites, and edutainment. This report focuses on the latter – edutainment. It is still not a very popular tool for financial education and this is why financial education strategies used in Poland can serve as an example of how a tool such as edutainment can be used as an effective financial education channel to transfer financial knowledge to consumers.

According to Wikipedia's definition, Edutainment (also educational entertainment or entertainment-education) is a form of entertainment designed to educate as well as to amuse. Edutainment typically seeks to instruct an audience by embedding lessons in some familiar form of entertainment: television programs, computer and video games, films, music, websites, multimedia software, etc. Successful edutainment is unique in the fact that learning becomes fun and teachers can educate an audience in a manner which is both engaging and amusing.

There are many examples of edutainment programs that have resulted in social or educational change; some of these include: *The Archers (UK)*, *The Sesame Street (USA)*, and *Blue's Clues (USA)*. Another form of edutainment tools includes health education programs (e.g., *Soul City* in the Republic of South Africa) which successfully changed peoples' opinions and behaviours all over the world. Financial education is similar to health education in that personal finance knowledge is as important as personal health. Hence, the planning of edutainment campaigns for financial education may take into consideration the methods applied by the health organizations in their campaigns to promote health issues.

Learning in Change

Another reason for choosing edutainment tools for financial education is the need for innovation; because of rapid developments in information and communication technologies, a new world of learning has emerged. With its interactive, collaborative and social networking tools, it is often not effective to continue the methods of education that were popular in the 20th Century. Financial educators must develop new methods of communication and education, as the education process in the 21st Century requires a change of approach and use of a variety of tools. Web 2.0 (blogs, wikis, social networking, etc.) and e-Learning do influence the development of collaborative and informal learning worldwide, and as a result of that a new learner requires new approaches.

Table 1. A new world of learning

Old world	New world
Audience	
Single channel	Multichannel
Staff	Customers/partners/public
Single task	Multitask
Insular thinkers	Global thinkers
Deep knowledge	Broad knowledge
Clear	Ambiguous
Individual	Community
Learning	
Event	Process
Long life content	Perishable content
One-off	Continuous
Formal	Informal
Training led	Business led
Training	Performance
Produce and consume	Search and retrieve
Quality	Quantity
Learning design	
Trainers	Consultants
One size	Personalised
Fixed	Scalable
Fixed choice	Menu options
Content	Access
Full solutions	Small chunks

see: Global Watch Mission Report: Beyond e-Learning, 2006

Being 21st Century educators, we must think not only about the quality of the teaching/learning process but also about proper communication channels to deliver personal finance knowledge, adding a new dimension of effectiveness. For education to be effective, innovative techniques should be adopted such as the development and use of education tools that are popular: blogs, podcasts, videocasts, multimedia presentations, interactive internet sites and various mass media including television series. New perspectives on learning offer fantastic opportunities to deliver financial education to people in many popular channels; including: YouTube, iTunes, Scribd, Slideshare, Digg, Facebook, Mobile Phones, and Digital TV programs.

According to various surveys, informal education is 80-90% of all learning processes today. Lifelong learning requires that most learning activities take place informally throughout one's life. This applies to personal finance education too. In the 21st century, the learner creates his own educational environment, and the educator must be ready to deliver information in as many ways as possible.

Modern digital devices including mass media, Internet and social networking tools are natural learning environments for many people and must be carefully considered when planning educational

activities. In addition, edutainment programs are a way of delivering knowledge to people in a truly interactive manner, which engages many channels and tools in a new learning landscape.

Engage Mass Media

Surveys in many countries confirm that people want to learn economics and finance from mass media or new media. The reason being that most people have easy access to mass media channels, use them on a daily basis and it does not require much effort on their part. Therefore, if an audience of millions is considered in an educational effort, the attention should be turned to mass media channels. This does not mean that including economic experts in various programs would be an effective strategy, as people usually do not like talking heads in the television or radio programs -- they usually look for entertainment. People like to be educated in an original and easy way.

In the mass media channels, financial education and entertainment could be easily combined. It is possible to offer entertaining programs and, at the same time, spread financial knowledge to viewers or listeners. All depends on the form of communication and an original idea for the program.

Involving mass media in financial education offers great opportunity to promote effective and responsible behaviour, positive attitudes that are useful methods for managing most common daily financial challenges. It offers a variety of forms where financial education topics can be included or hidden in the storylines. Educators should not hesitate to use all possible channels of communication, traditional (television, radio, press) and modern (Internet, internet tv, mobile phones) for that purpose. When making a decision to run a mass media educational project, it is always good to think big.

Why Edutainment?

The essence of edutainment is a combination of education and entertainment - in other words it is "learning through playing". Further, the purpose of edutainment is always education. A form of entertainment only facilitates and makes the process more attractive for learners, and sometimes it helps producers to hide the educational message within the context of the program too.

Edutainment is a tool that serves for implementing a strategy for a social change. It can be used in many educational initiatives – helping to promote healthy lifestyles, develop ecological attitudes or increase responsible behaviour in personal finance.

It is highly effective tool that promotes particular knowledge and skills. There are many evaluation reports worldwide that confirm edutainment programs facilitate and develop the education process and in the end, result in real social change -- especially when an improvement is desired by the target group (e.g. the lack of knowledge on how to manage one's own credit expenses).

While planning an edutainment project it is always good to involve mass media; specifically, the major one at the centre of the action and others supporting the main channel. It is recommended to use many tools in the project too. There are several reasons for multi-channel and multimedia approach:

- People learn in unique ways over different periods of time. It is important to present information differently so that people can absorb it;
- People learn by observing others and by the consequences of their own behaviours. By using a variety of different media, actions can be presented from different points of view, yet still contain the same message.

- Individuals prefer some media channels over others. Hence, providing the opportunity to learn the message in a variety of ways increases the probability that the individual will learn.
- Learning is most effective when people can learn at their own pace – different channels offer a different pace of learning so that people can choose the one they prefer.

Financial Education Edutainment Experience

Edutainment as a tool for economic and financial education worldwide was incorporated into the strategy of economic education of the National Bank of Poland (NBP) in 2005. Since then, there have been several complex Edutainment programs run from 2005-2007, with many positive results in both the range of programs and effectiveness of the education process. The following four cases illustrate this method in action:

GOLD FOR THE BOLD – POLES & MONEY 2006

A 120 minute long dynamic television show was run on Sunday evening in the TVN – the most popular private television in Poland (February 2006). The program was based on a format used by the Dutch TV producers for nationwide television shows. Viewers had the opportunity to test their knowledge on money and personal finance issues by participating in the financial knowledge test online, through a specially dedicated web page or by filling in the test form (distributed through largest Polish daily) while watching the TV program.

The test of financial knowledge was tailored to the average viewer and to make it more attractive, each of the 30 questions was illustrated by film material from famous Polish comedies or cabaret scenes (all had an economic context inside). That was a crucial approach in order to attract people's attention.

To organize the show, a large professional film studio was rearranged to host a selected group of 100 people, media celebrities and organizers. The group in the studio was divided into four teams which had to compete in order to win the financial prize of 25 000 Polish zlotys. To further attract viewers, each team was lead by two popular TVN celebrity stars.

There were several fields of economics chosen as test areas, among them: money and monetary policy or personal finance (savings and investment). The test questions were programmed not only to deliver knowledge, but also to offer entertainment and fun for viewers, while at the same time directing people's attention to important personal finance issues.

The test competition was not only in the studio but also online. For the online competitors the main prize was a car sponsored by a car company.

The results of the show were as follows: 8 Million viewers of the main TV show, 250.000 people visited the program website and 102.000 completed the test online during the broadcast.

The program also attracted significant attention in the supporting mass media: radio programs focusing on personal finance issues recorded up to 750.000 listeners, 800.000 copies of the test form were distributed in the popular TV Program weekly, another 10 educational articles were published in the main Polish daily Gazeta Wyborcza and one of the most important weeklies Wprost.

In addition, a special set of financial test materials was sent to 2500 high schools, which includes a game-like scenario for a single lesson on personal finance. Students were able to solve a similar test

in the classroom. Close to 53.000 students completed that test within a couple of days following the TV show.

The effectiveness of this form of education in the Gold for the Bold was evaluated in a specially designed survey. In the adult population, the average increase of knowledge was 5.6 % (after watching) and in a repeated test in a fortnight, it was 3 %. Within the younger population, the increase of knowledge was much higher - up to 10.1%.

THE MOTEL HALFWAY

Another interesting form of edutainment is the radio novel. In November 2006, a new radio novel The Motel Halfway was launched on the Polish Public Radio Program 1. The first season was 30 episodes long (once a week). Basing this idea on a popular UK radio novel The Archers, this novel focused on microentrepreneurs, a small group of people running a small motel in the countryside.

As well, other media accompanied the main channel in this educational effort. This time it was a popular daily tabloid Super Express, and one of the largest Polish internet portals Wirtualna Polska, which hosted the programs official web page (www.motel.wp.pl).

There were famous Polish actors who agreed to read the parts of the program's characters. Scenarios, prepared under the supervision of the National Bank of Poland staff, included many real-life situations where the program characters had to find a solution to problems in their business activity, management of the budget (personal and corporate) and savings or investments issues.

The program was very successful. Over 1 Million listeners a week followed the adventures of the Motel staff, which resulted in a decision to continue the Motel for a second season beginning in December 2007.

The aim of the novel was not to teach entrepreneurship, but to make people think about being entrepreneurial in everyday life and manage their finances better. As each episode lasted up to 23 minutes, it was a good opportunity to include many crucial financial issues in the storyline.

The effectiveness of this form of education in the Motel Halfway was assessed in a specially designed survey. The increase of knowledge among adults amounted to 21.5% after listening to Motel Halfway episodes (and in a fortnight, without listening to episodes: 29.3%); among young people it was 9.7% and 19.3% accordingly.

THE WALLET PORTRAIT

The Wallet Portrait was a three and a half week long educational TV campaign on personal finance education launched within the Christmas to New Year's Day period (2006/2007). It was broadcast on four channels of the most popular private TVN station. By choosing this period, organizers focused on "unpopular" topics near Christmas time – savings and responsible financial attitudes, or in other words responsible spending.

To get the attention of viewers, short "eduvertisements" were produced. These were composed of six short interviews with popular media celebrities, explaining why (and how) they try to save during that particular time. Each interview was up to 90 seconds and viewers could easily discover that even celebrities often have similar problems.

The discussion in the edvertisements was a very practical one. It concentrated on issues that are common for most of us; for example: What is better, a credit card or money in the wallet?, the benefits of taking care of the home budget, how to save and invest and which type of credit is best for buying a flat.

These six edvertisements were broadcast 266 times on four channels of the TVN. People loved that form of education. An estimated 10.5 million people watched at least 3 episodes.

The effectiveness of this form of education was assessed in a specially designed survey. The increase of knowledge among adults was 13.9% after watching episodes (and in another survey in a fortnight, without watching episodes again, it was 11.8%). Among young people the results were 18.6% and 19.8% accordingly.

WHAT? EDUCATIONAL FILM PORTAL

The most innovative form of education introduced was the educational film portal on the internet, called What? The idea was to develop a form of viral marketing to promote economic and financial education issues among internet users. There were 60 short films produced (up to 3 minutes long), each presenting a story with an economic context in an everyday-life situation, of which many focused on financial issues. The portal engaged other forms of communication, like blogs and an internet forum as well.

All films were designed for OFF film production rather than for typical reports or novels. Each film had a unique story depicting the impact of good or bad decisions on people's everyday life.

The portal was very popular – it was visited by over 4.5 million Internet users within 6 months. An average of 120 000 users viewed each film.

The effectiveness of this form of education was assessed in a specially designed survey. The increase of knowledge among adults was 17.5% after watching films (and in another survey in a fortnight, without watching the episodes again, it was 21.8%). Among young people, it was 15.3% and 17.4% accordingly.

Summing Up

New methods of learning influence the way knowledge and skills are delivered to learners. Imagine a process in which the most important lifetime education can take place out of schools and incorporate different forms of informal education. Financial education must be included in that scheme.

As financial knowledge is a major life skill, Edutainment is an effective method of delivering that knowledge to a large audience. It offers an attractive form of learning and when using multi-channel communication, it enables people to learn the message from different channels.

Polish Edutainment programs of the National Bank of Poland confirmed that edutainment is an effective tool for economic and financial education and when properly implemented it offers a significant increase in knowledge within a target population.

C- Kathleen M. Floyd, Executive Director, The Stock Market Game, United States

On behalf of the Stock Market Game Program and the SIFMA Foundation for Investor Education (SIFMA Foundation)⁶⁸, we were honored to be included in the OECD/US Treasury International Conference on Financial Education held in Washington, D.C., May 2008. Every nation's strength is fundamentally based in the cumulative knowledge of its people. We believe it is imperative that the knowledge include an understanding of the economy and the role of the capital markets, particularly as individuals will increasingly bear more direct responsibility for building and managing their own retirement funds. Given these challenges, The SIFMA Foundation believes that practical, hands-on programs help bridge the gap between classroom learning and the real world.

The SIFMA Foundation's primary educational program for students, The Stock Market Game™ program (SMG), takes place in classrooms under the supervision of a program-trained teacher. Students in grades 4-12 are given a hypothetical portfolio of \$100,000, which they manage through online stock and mutual fund selection, sales and purchase. SMG teams of three to five students compete on a regional, statewide, or national basis. Since 1977, the SMG has given educators a way to improve the learning experience in thousands of classrooms. Teachers have successfully used SMG to enliven core academic subjects - including math, social studies, and language arts - and research has shown there's no better way to teach the importance of long-term saving and investing. The program is growing rapidly and is currently used by more than 20,000 teachers annually, has served more than 11 million students since inception, and reached more than 740,000 students in the 2007-2008 school year.

It is very easy to understand why the students get excited over the program. It combines two of their favorite things, computer technology and learning about money. Gaming and fun are part of our essential learning tools for the students. They relate well to this medium. They understand technology. This is evident by the exponential growth the program has experienced. In the past three years the program has more than doubled and during the 2007-2008 school year there were more than 185,000 student portfolios.

In the United States, teachers tell us that one of the challenges they face most often is how to use a program like the SMG and other financial literacy programs in a way that meets the state educational standards required by our legislation, the No Child Left Behind (NCLB) Act⁶⁹. An increased emphasis on academic standards, makes it more difficult to implement programs (financial literacy or otherwise) that are not directly correlated to the standards they are required to teach. And to make it more difficult, each of the 50 states has their own academic standards. The teachers we speak with often believe financial literacy is important, but feel they have to make a choice between ensuring that students meet the standards for their subject matter and teaching a financial literacy program. If that is the choice, standards invariably win.

At the SIFMA Foundation we are convinced that financial literacy programs must be engaging for students, but they also need to be integrated within a teacher's curriculum. Teachers shouldn't have to choose between teaching their subject matter and teaching students about how to manage their money. One of the most attractive aspects of our lesson plans for teachers is that they are tied to both national and state academic standards. We have taken the step of matching each of our lesson plans to

⁶⁸ The SIFMA Foundation for Investor Education, an affiliate of the Securities Industry and Financial Markets Association, is a charitable, educational not-for-profit (501-c-3) organization dedicated to advocating financial education.

⁶⁹ See PL 107-110, the No Child Left Behind Act of 2001, Title I, Part A, Sec. 1111

the academic standards of all 50 states. Teachers tell us that correlating our lesson plans to standards in math, social studies, economics, business, and language arts has helped them successfully implement our program in the classroom. It allows teachers the time to teach the fundamentals of saving and investing while reinforcing lessons in the aforementioned subject matters. We believe that linking financial literacy programs and curricula to standards can help overcome one of the most serious barriers financial literacy programs face in terms of access to the classroom.

Additionally, the SIFMA Foundation pursues other classroom strategies in terms of helping teachers implement a meaningful and educational financial education. Our national essay contest, InvestWrite, is an integral part of the Stock Market Game and serves as its culminating activity. It gives students real-world scenarios and asks them to apply classroom learning about long-term saving and investing to their essays and demonstrate a fundamental understanding of essential investing concepts, such as risk, diversification, and the time value of money.

At the SIFMA Foundation we are also strong advocates of researching financial education. Every two years since 1998, the US Jump\$tart Coalition for Personal Financial Literacy conducts a personal financial literacy survey. All six surveys have shown that high school students involved in a stock market game perform better on the test than those who don't. The data also show that college students who participated in a stock market game while in high school performed better than those that did not participate. Similarly, the 2008 Nation's Report on Economics conducted by the National Assessment of Education Progress found that high school students who participated in a stock market game scored 8 points higher on the economics test than the average and 10 points higher than students that did not participate.

This raises, we believe, an interesting question to be answered and also we believe a gap to be filled. What is the level of financial literacy among America's teachers? We believe our program raises the level of student financial literacy because the program is sound, but also, we believe, because many teachers report to us that they began teaching the program because they wanted to learn more about investing. There also teachers we know of that are already financially savvy having worked in the financial services or other industries where they obtained financial knowledge they use in the classroom. Can this self-selection and motivation of SMG teachers be part of the reason our students score higher on personal financial literacy and economics tests? Do we need to raise the level of financial literacy among America's teachers? These are questions we would like to see answered.

We are anxiously anticipating the results of a FINRA-sponsored study of the Stock Market Game. The evaluation will assess the impact of The Stock Market Game program on students' academic achievement in mathematics and investment knowledge as well as on teachers' investment practice. The study will take place over the coming school year and we look forward to sharing the results.

In conclusion, what we have learned over the past 30 years indicates four important points:

- 1) Not only students but teachers need financial literacy knowledge.
- 2) Integrating the financial literacy into other "academic classes" makes it easier for the teacher to "buy in." In fact our mission states, The Stock Market Game is a comprehensive, engaging, real world program that advances student academic achievement in the core disciplines (language arts, math, social studies) and enhances understanding of investing concepts among learners of all ages.

- 3) Gaming and fun are essential learning tools for students – they love money and learning how to grow their money.
- 4) The use of technology makes it exciting for the students.

For more information on the Stock Market Game can be found on our website at www.stockmarketgame.org.

**SESSION VII - YOUTH FINANCIAL LITERACY:
DEVELOPMENT, DELIVERY AND EXECUTION OF PROGRAMS**

Chair: Erik Pointillart, Chair of the Institut pour l'Éducation Financière and General Director Caisse d'Épargne, France

A- Shaun Mundy, Former Head of Financial Capability Department, Financial Services Authority, **United Kingdom** and OECD Consultant

B- Koid Swee Lian, Consumer and Market Conduct, Director, Bank Negara, **Malaysia**

C- Dara Duguay, Director of Citi's Office of Financial Education, Citigroup, **United States**

D- Roy Thomasson, Chief Executive Officer, Young American Business Trust, **Organization of American States**

E- Klaus Wertenbroch, Professor of Marketing, **INSEAD**

Policy Conclusions of the Chair

Youth financial education's critical importance, especially at school, leads to both a rapid growth in the number of countries concerned with the financial education of its young population, and an increase in the scope of dedicated financial education programmes.

Some suggestions stand out from the practices presented during the conference session on Youth Financial Literacy and from the recommendations of the OECD Research Report on *Financial Education Programmes in Schools*⁷⁰:

- Governments and policy makers in education must be aware of the importance of the matter.
- Existing programmes are often designed for students younger than 17 years of age. It is indeed a good thing to educate students about financial matters as early as possible, including primary school. But it is equally desirable to develop financial education programmes aimed at university students and vocational training.
- These programmes should be continuous, progressive, coherent and comprehensive, even if pressure on curriculum makes it difficult to add financial literacy as a new standalone subject.
- The methods should be adapted and attractive. An active pedagogy, widely based on real life situations would be very useful.
- Teachers should be aware and trained in personal financial education.

⁷⁰ See Proceedings Vol. II

- Cooperation between the educational and the financial systems is desirable. It can be beneficial if it is clearly elaborated on non-commercial bases. In any case, teachers should be engaged in the process.
- Youth financial education should provide knowledge and skills. It should also contribute to more effective and responsible personal finance behaviours.

Erik Pointillart, Introductory Remarks

The French Institute for Public Financial Education contends that financial education will be one of the major challenges in the years to come and specifically for young people. The objective is not to make a financial specialist out of each young adult, rather to bridge the gap between knowledge and the skills that young people need to know.

In some countries, surveys indicate that the financial literacy levels of young people are deteriorating. In France last year, a “young people and financial matters” survey was conducted of 15-20 year old people. This survey showed that the majority of the young people surveyed believe that they have control of money matters and that they are well prepared to act on concrete issues like budgeting or contacting their bank. However, the survey results showed that their knowledge is largely inadequate on matters like saving, pensions, insurance and so on. In fact, they are scared about taking credit. The economic and financial world is very unfamiliar to them. In addition, youth report that their parents have the essential role of teaching and counseling them in money matters. These results are not very encouraging.

In fact, according to another survey of the French adult population, 73% report that they believe that they are under-skilled in savings and investment. Becoming aware of this handicap was not only important for the population surveyed, but also provided an impetus for the financial industry and for the national economy to act.

In France, money remains a sort of taboo. For example, to say how much you earn is impolite. Similarly, it is inappropriate to say that one has money to invest. Parents do not often teach their children about money matters; perhaps even less often than family conversations about sex education. Therefore, there is much work to be done in France.

The not-for-profit organization, the Institute for Public Financial Education, has been created two years ago under the request of the French Securities Regulator (l’Autorité des Marchés Financiers). From the beginning, young people have been one of the three priority targets identified.

One of the Institute for Public Financial Education’s primary objectives is to provide financial education to youth within the school system. In this regard, there is still much progress to be made. In France, it is difficult to introduce financial education as a specific academic discipline, as the school curriculum is already overloaded. One strategy is to initially promote teaching financial literacy within other disciplines at school like mathematics, history, economics, civic instruction and even literature. A second possibility could be organizing finance-related conferences inside schools, but outside of the compulsory schedule.

A second objective of the Institute is to address not only education for students but also education for teachers who often ill-equipped to handle financial education questions. The Institute is working with teachers to design and produce educational materials; as well as organize conferences for training and sensitizing teachers to the importance of financial education. To address this need, the Institute has opened a special space for teachers on its website.

The Institute for Public Financial Education’s website also includes spaces for young people: one for kids and another for teenagers, with games, special information, etc. Further, the Institute is also cooperating with a book publisher to create a small book (“vos enfants et l’argent”, “yours kids and money”) to help parents teach their children about money matters.

However, the best way to reach people at large and especially young people is television. An important step in providing financial education to young people would be having a television program on financial education. It would allow the Institute to succeed in attracting attention and increasing interest in financial education.

To conclude, the exchange of international financial education experiences is particularly useful in informing the development of financial education initiatives in France.

A- Financial Education Programmes in Schools: Analysis of Selected Current Programmes and Literature; and Draft Recommendations for Best Practices (*See Report in Vol. II*)

Shaun Mundy, Former Head of Financial Capability Department, Financial Services Authority, and OECD Consultant, United Kingdom

This preliminary report, on financial education programmes in schools and other educational establishments, forms part of the OECD's Financial Education Project. The report reviews financial education programmes aimed at students in selected OECD and non-OECD member countries. The focus is mainly on programmes aimed at schoolchildren, since the great majority of programmes intended for students are for those of school age.

The overall picture is one of rapid growth in both the number and range of financial education initiatives. But the picture is patchy, both between countries and within countries.

There is a wide variety of programmes in existence, many of which have been launched relatively recently. Many of the programmes are innovative and have been carefully designed so that their target audience will find them engaging. While many of these programmes have characteristics which are particular to the country in question, there is nevertheless clear potential for those who are looking to develop new financial education programmes to adopt ideas from existing ones – whether from their own country or overseas. The report refers to websites, and to other sources of programmes, on which policy makers and other stakeholders may wish to draw.

The report also reviews the available research on the effectiveness of financial education initiatives aimed at students. There is, at least as yet, a lack of unambiguous research to demonstrate the effectiveness of financial education programmes for students. Not surprisingly, the focus to date in many countries has been on the development of new programmes, rather than on commissioning research. The report recommends that a broad range of research is undertaken to establish the most effective ways of providing financial education, both to assist policy makers to decide how best to focus resources in the future and to help convince educationalists that, within what are often crowded curricula, space should be found for personal finance education.

The report sets out a number of further recommendations for increasing the delivery of, and the effectiveness of, the provision of financial education to students.

There are lessons that can be drawn from those countries which have made greatest progress in delivering effective financial education programmes which can help to overcome these challenges. Among other things:

- financial education can be integrated into more established subjects (such as mathematics and citizenship) as well as, or instead of, being delivered as a separate subject;
- teachers can be helped, through training and the provision of tried and tested materials and lesson plans, to become competent and confident in the delivery of financial education;
- there is a wealth of attractive materials lesson plans and other support which teachers can draw on;
- there are a number of research results which, together with feedback from educational professionals and students, point to particular ways to deliver financial education effectively.

Drawing on the main findings of this initial survey of financial education programmes in educational establishments, the OECD intends to launch in 2009-2010 a more extensive stock-take exercise covering all OECD countries and selected non-members countries. This broader exercise would enable the development of a more comprehensive report on financial education programmes in educational establishments across a wide range of countries.

B- Youth Financial Literacy: Development, Delivery and Execution of Programmes

Koid Swee Lian, Consumer and Market Conduct, Director, Bank Negara, Malaysia

Introduction

Financial consumers can effectively participate in the economy if they are properly informed and have the requisite knowledge and skills. Enhancing the levels of financial literacy is being accorded high priority in many countries, including Malaysia due to the current environment of rapid change in technology, product innovation, deregulation and greater competition that have dramatically transformed the financial system. This new environment has created a greater need for consumers to be equipped with financial knowledge and skills to make sound financial decisions and to promote consumer activism to drive competition, improve efficiency and performance of financial institutions as well as enhance the potential for the economy to prosper.

Enhancing financial capability – the Malaysian approach

Bank Negara Malaysia (the Bank) has embarked on the following three-pronged approach to enhance the financial capability of consumers:

1. Developing and disseminating educational materials on financial products and services through booklets and websites;

2. Promoting financial education to students in collaboration with the Ministry of Education and financial institutions; and

3. Conducting financial educational outreach programmes to various target groups, including university students, through strategic partnerships with other organisations.

1. Developing and disseminating educational materials

To raise the financial capability of consumers to enable them to make informed and confident decisions on financial matters, the Bank initiated consumer education programmes for adults, including young adults, known as *bankinginfo* and *insuranceinfo* in 2003. These programmes are intended to:

- Promote greater understanding of, and more informed decision making on, financial products and services; and
- Enable consumers to have greater access to reliable information, thus be able to take greater responsibility for and management of their financial matters.

Scope of the Consumer Education Programme

Under the programme, consumers are educated on a wide range of issues to equip them with the necessary knowledge and skills to manage their financial matters effectively. The components of the programme are tailored to the level of understanding of each target group. These include knowledge and skills on:

- Planning - Saving and budgeting;

- Spending - Buying tips and comparative shopping;
- Financial products - Features of financial products and services (banking, Islamic banking, insurance and takaful), risks and liabilities involved, salient terms and conditions as well as rights and responsibilities as a financial consumer;
- Credit and debt - Borrowing and debt management, and rights and responsibilities as borrowers and guarantors;
- Risk management - Basic insurance and insurance planning; and
- Market awareness - Avenues for redress, illegal schemes, currency related matters, role and functions of financial players and credit bureaus.

2. Promoting financial education to students

To inculcate responsible money management habits and provide early exposure to students on financial matters, the Bank has embarked on financial education programmes in schools in collaboration with the Ministry of Education and financial institutions since 1997. The savings campaign, which was launched in 1996 to nurture Malaysians to be financially savvy, provides the foundation for a financial education programme for students in Malaysia. The programme is designed to inculcate savings habits and create awareness amongst students on the importance of smart financial management and planning. The specific initiatives undertaken to promote financial literacy to students include:

(i) School Adoption Programme (SAP)

The SAP is a collaborative effort between the Bank, the Ministry of Education and financial institutions aimed at raising the awareness of students on the importance of financial management. Under the SAP, which was introduced in 1997, each school is adopted by a financial institution. Financial institutions conduct activities related to banking, insurance and basic financial knowledge, apart from providing an opportunity for students to experience having a bank account. Since its introduction in 1997, more than 7,000 schools nationwide have been adopted by financial institutions.

(ii) Student Financial Club (SFC)

SFC, which was implemented in 1999, provides a platform for schools to organise financial education activities as part of the school co-curriculum activities. Currently, more than 2,000 schools under the SAP have formed SFCs. The SFCs serve as an effective focal point for financial institutions' outreach activities at schools by leveraging on the clubs' activities to increase the interest of students in financial matters. Students who join the club engage in money and finance related activities through workshops, quizzes, contests, games, knowledge-sharing sessions and visits to financial institutions.

(iii) Lesson plans and workshops for teachers

- To assist teachers in conducting SFC activities, lesson plans for teachers with outline modules and activities on financial education that can be conducted during SFC meetings have been developed and distributed to all schools.
- A series of workshops had been organised for teachers. The teachers were provided with fundamental knowledge on personal financial management and the effective approach to

disseminate financial literacy to students. Since 2000, a total of 65 workshops had been conducted and more than 6,238 teachers had benefited from these workshops.

- For the financial education offered through the co-curriculum activities, the modules for secondary school students (13 – 17 years old) are as follows:
 - Setting financial goals and budgeting;
 - Financial management (including consequences of personal financial decisions) and saving and investment (use of financial tools, risk and return of investment); and
 - Effects of inflation, the need to manage credit prudently and the concept of insurance.

In relation to the above topics, the following aspects of financial education are generally included:

(a) Financial knowledge and understanding

Developing the financial understanding of students enables them to have the requisite skills needed to deal with everyday financial issues, as well as to help them to make informed decisions on spending and saving their pocket money.

(b) Financial skills and competence

This would enable students to apply knowledge and understanding of financial matters in managing financial situations effectively and efficiently.

(c) Financial responsibility

This would enable students to appreciate how financial decisions can affect an individual, their family and community.

(iv) Workshops for students

- Workshops for students (primarily for members of SFCs) have been conducted since 2002. To date, a total of 24 workshops involving 5,860 students have been organised:
 - To provide exposure to students in managing and planning their personal finances through the use of the pocket money book;
 - To provide them with exposure on the fundamentals of investment and consumer rights;
 - To educate students on the importance of basic financial management; and
 - To develop students' leadership qualities by providing them with information on how to manage the school financial club.

(v) ***Pocket money book***

The pocket money book which was introduced in 1998, is a learning tool developed by the Bank to educate and assist students to manage their pocket money and to take control of their personal finances at an early age. The book contains money and finance related articles, exercises and games. To date, a total of 5.9 million books have been distributed to students throughout Malaysia.

(vi) ***Financial education website 'Duitsaku.com'***

In line with the development of information technology and the growing usage of computers among the younger population, the Bank in collaboration with the Ministry of Education, has created an interactive financial education website in October 2004, to enhance financial literacy among students. Students can participate in interactive financial games, contests, quizzes, financial calculations and other activities related to personal financial management. Currently, the website has attracted more than 85,000 members.

3. Conducting financial educational outreach programmes

The Bank in collaboration with smart partners, undertakes outreach programmes to provide information to various target groups including university and college students, with the aim of creating responsible Malaysians who can manage their finances wisely. The key messages conveyed during these outreach programmes include:

- Wise money management (why and how);
- Benefits and importance of saving from a young age; and
- Consumer responsibility for their own actions and decisions.

The main aspects of financial planning highlighted during the seminars/workshops for undergraduates were on personal money management especially on managing education loans for higher learning, banking and insurance issues particularly on loans, guarantors, credit cards, motor and life insurance, issues on investments including illegal get-rich-quick schemes.

Beginning in 2007, students aged 17 attending the compulsory National Service Programme are taught various aspects of financial management such as budgeting, managing spending by making smart financial choices and banking information to enable them to have a better appreciation of money management. Annually, a total of 120,000 students are involved in the National Service Programme.

Financial education for undergraduates

For institutions of higher learning, the Credit Counselling and Debt Management Agency, which is a subsidiary of the Bank, is collaborating with the public universities to incorporate the subject of 'Personal Finance' into the curriculum. Once introduced, financial education with emphasis in personal finance will be provided as a mandatory subject to undergraduates from the age of 20 to 24 years old, with the aim of preparing graduates to face the challenges of managing their finances wisely at the start of their careers.

The Malaysian Financial Planning Council (MFPC) jointly with Permodalan Nasional Berhad (PNB), which is a government-owned investment holding company, have been taking a major role in promoting financial planning among undergraduates. Over the next two years, MFPC and PNB will be jointly organising financial planning workshops for 10,000 undergraduates at 26 universities. Apart from raising the awareness of undergraduates on the importance of financial planning, the workshops will also introduce undergraduates to the important concepts and skills in personal financial planning. In addition, the 'Fundamentals of Financial Planning' will also be offered as one of the elective papers for undergraduates in 26 universities in Malaysia.

Strategies to promote youth financial literacy

Some of the challenges in promoting financial literacy to youth include the integration of financial education into the school curriculum, identifying the most effective means of engaging youth in financial education, the availability of effective educational materials as well as the ability of the teachers to deliver the relevant information to youth. In Malaysia, the financial education modules which are delivered in an interactive manner with the aim to actively involve students, through group-work and simulation of real life situations proved to be effective. It is a way of keeping students interested and enables them to see first-hand the benefits of financial education programme, which are applicable to their everyday life. In this way, they are more likely to retain and use the information acquired through these programmes.

The effective promoting financial education programmes is also dependent on the school policy, outlook and capabilities of the school, and whether the programme is regarded as a priority by the school. Although the involvement of financial institutions in financial education programmes is part of their corporate and social responsibilities, it is a challenge to encourage financial institutions to play a more significant role in this area. In this regard, collaboration between Bank Negara Malaysia and financial institutions is enhanced with the setting up of the School Adoption Programme Working Group comprising financial institutions which are active in the SAP initiatives.

The emerging best practices in enhancing financial literacy clearly suggest that an integrated and coordinated delivery of financial literacy initiatives is needed to address the issues related to financial literacy. This requires a comprehensive approach involving the regulators, relevant Government ministries, educators, financial institutions and community-based organizations to work collaboratively to equip the youth with the necessary skills and confidence in managing their personal financial matters effectively. In this regard, Bank Negara Malaysia has established the Financial Education Working Committee and formed strategic alliances with other quasi-governmental agencies such as the Credit Counselling and Debt Management Agency, Financial Mediation Bureau and the Malaysia Deposit Insurance Corporation. The Working Committee serves as a platform to coordinate financial education initiatives and facilitate the more efficient allocation of resources between the agencies in achieving the mutual goal of promoting financial literacy to Malaysians.

C- Citi Financial Education Program

Dara Duguay, Director of Citi's Office of Financial Education, Citigroup, United States

Our History

For more than a century, Citi has helped customers and clients access, build, and manage assets.

Our Commitment

US\$200 million over ten years to support financial education programs and organizations around the world and we established the Citi Office of Financial Education to lead our efforts. Through our commitment, Citi will touch the lives of millions of people by supporting financial education that will help them achieve their dreams.

Our Belief

Knowledge is your greatest asset. We support financial education because it helps people understand how to use financial resources, and in the process, raises the quality of life for individuals, families, and institutions and strengthens communities around the world. Financial education is a natural extension of the work we do every day and a major focus of our effort to make a difference in the communities where we live and work.

Our Focus

Personal: helping people save, invest, borrow, and spend wisely, and manage debt responsibly;

Small Business: helping entrepreneurs save, invest, and secure financing to better manage their capital and grow their businesses;

Institutional: supporting programs that assist governments, academic and financial institutions, and nonprofit organizations to promote knowledge and sound management of economics, markets, and financial systems.

Our Reach

In 2007, Citi and the Citi Foundation provided nearly US\$36 million to support financial education programs and activities that reached millions of people in 65 countries. As one of the world's largest financial services companies, we're in a unique position to make a difference. We have over 300,000 employees with an extraordinary record of community involvement and volunteerism. Citi also has a global initiative designed to encourage our employees around the world to devote time to support financial education and other charitable causes. Under this initiative, employees are able to take a day off each year to volunteer for a nonprofit organization.

Our Web site

Citi's Financial Education web site features information on our financial education programs, upcoming activities, and resources, including Citi's Financial Education Curriculum. It is available at <http://financialeducation.citi.com>.

Highlighted International Programs

Mexico:

Jóvenes Emprendedores (Young Entrepreneurs)

Program that consists of training, coaching, and counseling young people so they can create their own companies. This is the fourth year of the program, achieving the participation of 600 high school students, organized in 51 companies. The program lasts 17 weeks.

Key success factors:

- The participation of volunteers this year amounted to 102 volunteers.
- The program is coordinated jointly with Impulsa, Junior Achievement México.
- The participation of two public schools and one private school, as beneficiaries.
- Specialized training by areas, with the participation of GF Banamex directors.
- The participation coordination of the young people made by Impulsa (invitation, training, counseling, and application of result assessment instruments).
- The participation coordination of volunteers performed by EF Banamex (invitation, training, counseling, and application of result assessment instruments).

Bancos en Acción (Banks in Action)

Program that consists of an electronic simulator that enables the young high school students nationwide to make decisions and learn how the banking system works.

For the fourth year in a row, Mexico will participate in the contest Bancos en Acción, as the venue for the Latin American contest. Likewise, it will be performed in three stages this year; the first at a regional level, the second at a domestic level, and the third one in Latin America.

The participation of more than 300 youngsters in the national contest is expected.

Key success factors.

- As it is an electronic simulator, nationwide coverage is possible.
- The recurrent participation of the volunteers in this program.
- Attain the participation of all the GF Banamex Divisions nationwide.
- Innovation in teaching materials that complement the information and formation of the young participants.

Financiero por un Día (Banker for One Day)

A Program in which a senior school student spends a full working day beside a member of GF Banamex direction, giving him the opportunity to approach the working environment. We have

conducted this program successfully for three years in a row, with the participation of approximately 100 students and directors. It was also replicated, for the first time, in one Mexican state: Jalisco.

Key success factors:

- The invitation made to Directors by the GF Banamex General Director.
- Prior awareness creation on the participants about the relevance for these young people to gain experience about their future in the labor field.
- The impact that the institutional image has on these youngsters.

Foro Internacional de Emprendedores 2008/ (2008 International Entrepreneurs Forum)

A one-week encounter organized by Impulsa, Junior Achievement México, where we have participated for the fourth year in a row with the *Banamex Day*, offering talks, workshops, board games, and educational activities associated with personal and business finance, and with entrepreneurship-related topics.

Success factors:

- The continuity of the Banamex Day.
- The design of the game Decisiones de pe\$o.
- Around 200 scholarships for children of collaborators.
- 50 % of sons of collaborators attend for a second or third time.
- The participation of senior directors of the GF Banamex, acting as voluntary lecturers and workshop participants.
- The extensive invitation.

Certified on-line tutors for the course: "Personal Finance: your Money, your Work, and your Property".

Students of the Administration and Finance Division (DAF) of the Tecnológico de Monterrey have been trained and certified as on-line tutors of the course "Personal Finance: your Money, your Work, and your Property", in order to provide on-line counseling to people of low-income communities nationwide. Nowadays there are thirty students of the DAF, of which 18 are acting as tutors of approximately 100 people of communities that participate in the Instituto Tecnológico y de Estudios Superiores de Monterrey's (ITESM) Learning Community Centers.

Key success factors:

- By being an on-line course, nationwide coverage is possible.
- The design of the on-line training and certification model.
- Alliance with a prestigious academic institution, having high impact technological infrastructure.
- Strengthen the social commitment of young students.

Maicitos (Little Corn)

It is a program offered by the Institutional Relations area to children of collaborators and customers of GF Banamex. EF Banamex participates for the third year in a row with a budget workshop. It trains approximately 100 young people every year.

Key success factors:

- Create awareness on young people about the importance of financial planning and about budget use.
- The design of practical activities that allow them to apply what they learn in a creative way.

Train the trainers as museum guides.

From the design of the itinerant exhibit “El Ábaco para Saber más de la Cuenta”, and from other mobile interactive shows, EF Banamex has trained young people who work as museum guides in Mexico City and in different states of the Mexican Republic, such as Mexico City, Nuevo León, Chiapas, Coahuila, and Sinaloa, among others. We have trained more than 100 youngsters on the importance of savings and on other associated financial education topics.

Key success factors:

- The direct contact with partners in several Mexican states, representing the public, private and social sectors, as well as with the Regional and Divisional Directions of GF Banamex.
- The training given by EF Banamex, that makes it possible for the exhibition to be shown throughout the country.

In all the programs, the **follow up and assessment** consist of:

- At the end of the program, a qualitative assessment instrument is applied.
- Records of the quantitative impact of the participants is maintained (volunteers and beneficiaries).
- The youngsters and volunteers are followed up closely throughout the program to identify areas of opportunities.

Asia Pacific:

Agent Penny

1. Youth Financial Literacy program Development

a. Briefly describe the international program.

Agent Penny is a financial literacy initiative targeted specifically at upper primary students aged 10-12 years. Using an illustrated comic book and drama, the program provides an innovative and fun-filled way to teach children the values of savings, budgeting and how to be a smart consumer.

The Adventures of Agent Penny” program was developed with a view to becoming a flexible module with universal appeal, one that is easily transferable and adapted to suit the needs of the

countries where Citibank has a presence. Its main objective is to make financial education interesting and engaging to children, regardless of nationality or language.

In Asia Pacific, Agent Penny is implemented in five countries:

- Singapore, China, Hong Kong in partnership with the Learning Society⁷¹
- Malaysia, in partnership with the Malaysian Invention & Design Society (MINDS)
- Indonesia, in partnership with the Yayasan Mitra Mandiri (Self-Reliance Partner Foundation)

2. Education & Delivery

What delivery methods have been proven to be successful?

- **Manga-style illustrated comic book:** to date three Agent Penny comic books have been developed and distributed to primary school students
- **30 minutes drama:** based on stories from the books that depict scenarios which focus on themes such as savings, budgeting and ways to be a smart consumer. A theatre group usually develops the drama skits. In the case of Malaysia, the students perform the skits themselves, with support from their teachers. Each performance is also usually followed by a time for questions.
- **A resource kit:** which contains teaching tools such as games, quizzes, exercises and activity plans, is offered to teachers to reinforce the concepts and financial management highlighted in the book. In addition, teachers and students have access to an interactive website that hosts online resources and tools

3. Evaluation

a. What performance measure does this program use to evaluate effectiveness?

- No standard evaluation process in place across all countries.
- After the skit performance, the theatre group and/or teachers ask a series of questions to test students' understanding of basic money concepts and values introduced through the skit.
- In Singapore, a sample of students are also given a basic questionnaire to determine their response and learning related to the skit and the comic book focusing on money management, understanding the importance of saving and spending wisely. In addition to the basic questionnaire, an evaluation of the effectiveness of the program was conducted by the National Institute of Education in 2007, using student and teacher interviews and focus group discussions. The evaluation looked at students' experience managing money and other financial matters and their feedback on Agent Penny.

⁷¹ www.learningsociety.org.sg.

Making Cents

1. Youth Financial Literacy program Development

a. Briefly describe the international program.

MakingCents is a financial education program that provides teaching resources, linked to the school curriculum for students in primary school (aged 6-12). Supporting elements of the program include teacher professional development, a program for parents (targeting low socio-economic communities) and a website with resources for parents and teachers.

MakingCents is the main component of the Finance First project, an initiative of Citi Australia, in partnership with YWCA New South Wales and funded by the Citi Foundation.

2. Education & Delivery

What delivery methods have been proven to be successful?

- Teacher professional development is delivered in cooperation with the relevant Department of Education in each State in Australia
- All teaching resources are downloadable from the MakingCents website
- The MakingCents for Parents program is delivered by Department of Education representatives in schools

3. Evaluation

a. What performance measure does this program use to evaluate effectiveness?

- Teacher attendance at professional development training sessions - over 3,000 teachers have received training to date
- Downloads of materials from the MakingCents website- in one year there were in excess of 56,000 downloads of materials
- Research evaluations: In 2007, Professor Christine Halse from the Centre of Education Research at the University of Western Sydney conducted an evaluation of the MakingCents program. The evaluation measured the appropriateness of the resources and materials, including the MakingCents website, for primary school children, their parents, teachers and specialist trainers.

Additional Information

1) Citi Australia Financial Education Fact Sheet February 2008

MakingCents

Starting financial education from an early age is the key to setting good foundations for the future. MakingCents is a personal financial resource for primary school teachers and includes teaching resources, teacher professional development and a complementary program for parents.

The MakingCents program aims to ensure children learn at an early age the fundamentals of financial management, the difference between needs and wants and the importance of saving and minimising debt.

The MakingCents program not only aims to help students, but also encourages families to support their children's learning at home through a complementary program for parents. The MakingCents for Parents program provides information and practical ideas parents can introduce at home to expand their children's school knowledge and experience.

The MakingCents website⁷² has tips, hints and resources for parents and teachers to reinforce financial education.

MakingCents is a unique program in that materials have been matched to curricula of each state and territory. The MakingCents program has been delivered to over 3000 teachers across Australia through a teacher professional development program. Teachers report a very positive response from their students in their classrooms and highlight how important this learning is for the younger age group.

2) Summary of Christine Halse's Presentation on the Making Cents for Parents program at the 2007 Citi-FT Financial Education Summit⁷³

The primary objectives of the Citi funded project, 'Engaging and transforming communities: The Finance First Project (2007) conducted by the Centre for Educational Research, University of Western Sydney, Australia, were two fold. First and foremost, it aimed to empower individuals and communities by supporting social change and developing a critical consciousness of financial literacy, and secondly it aimed to strengthen their capacity to manage money more effectively.

In order to achieve its objective the program content included budgeting, developing short and long term goals, managing expenses, creating awareness about financial tool and credit and debt management.

The structure of the program was designed to be interactive. A fictional family - the Pratchet Family - was created, and participants were encouraged to build their financial problem into this family. The pedagogy of the program involved questioning for critical reflection, small group discussion, active participation, 'easy to understand' information and encouraged action at home.

Overall, the aim of the project was to support social change and develop a critical consciousness of financial literacy.

Key Challenges

The key challenge of the program was how to ensure continuity and make it a self-sustaining. There were four principles for sustainable financial literacy – communication, collaborative learning, constructing a social mode and developing resilience through research.

⁷² <http://www.makingcents.com.au>

⁷³ <http://www.financialeducationsummit.org/programme.php>.

Learning points

The Finance First project provided three critical learning points:

Lesson 1: Know your participants

Professor Halse stressed that the traditional models of consumer behaviour do not apply in some communities. Moreover, it was important that the content of the program was flexible in order to meet the needs of the participants. According to her, the primary reason that women participated in this program was because it provided a social network for their financial and emotional needs. It is also important to treat the course structure as a framework and not a blueprint. Thus timing, duration, modes of delivery were modified in order to execute an effective program

Lesson 2: The value of social outcomes

Parent's knowledge and understanding led to increased self-esteem and confidence, which in turn builds family resilience and well being leading to community membership and participation.

Lesson 3: High quality trainers are the key to success

Successful trainers were flexible and adaptable, with vast knowledge about the social and cultural fabric of their particular community. They would also have the cultural capital and skill in facilitating access to local support resources.

D- Roy Thomasson, Chief Executive Officer, Young American Business Trust, Organization of American States

Financial education – including broader aspects of economic education – is a fundamental survival skill for young people of the 21st Century. Rapid globalization with its inter-dependent trade, worldwide emphasis on entrepreneurship, and increasing pressures for national competitiveness, make these skills essential to surviving and thriving in this changed environment.

For the almost 70% of the population of the Americas under age 35, understanding to manage their resources, how economies work, how to be entrepreneurial, will largely determine whether their future offers possibilities for overcoming the traditional challenges of poverty and unemployment. Governments and the private sector both recognize that increasing the relevance of education to work and to skills in demand in the marketplace is necessary for broad based economic and social development.

The Young Americas Business Trust is a private sector initiative that works to support the work of the General Secretariat of the Organization of American States, particularly in the creation of employment opportunities for young people through entrepreneurship. Over the past ten years, we have learned that business skills training and access to resources is not sufficient to prepare young people to the challenges of starting and managing a business. Also needed are the entrepreneurial spirit that comes from personal development as well as leadership, business social responsibility, financial education, and technology.

Our program emphasize engaging young people in experiential learning to reinforce academic lessons, provide opportunities to apply lessons learned in the community and market place, and to enable them to readily see the application of principles. These are not exactly new ideas, but what we have found is entrepreneurship is more of a process than a project. An integrated program offers additional benefits of follow-up, links to on-going related training, and ways to continue to maintain the young person's interest in learning.

YABT's entry into financial education began with the realization that the current push to expand microcredit, though very much needed, could lead to an emphasis on borrowing rather than saving or managing money. For entrepreneurs, as it is with individuals and families, this can create a distorted approach and perspective that would be detrimental to their long-term business survival and success.

With pilot funding provided by the Permanent Mission of Canada to the OAS, YABT developed and pilot tested a basic introductory curriculum in the English-speaking Caribbean. This training has been integrated into our experience-based Business Labs training that provides an introductory entrepreneurial experience to young people in business startup. It is now part of a wider curriculum that includes business social responsibility, financial education, personal and leadership skills, and follow-up resource centers.

We have also learned that it is not sufficient to simply translate materials from one language and culture to another, based on the obvious fact that young people in different countries live in different realities. For example, credit cards and internet banking may be appropriate for some, it may not be for others and it would be a mistake to broadly apply materials and content without recognizing this. And technology needs to be a key component to attract the interest of young people. However, technology alone is not enough and a blended approach that combines technology with human contact works best to maintain their motivation over time.

At the same time, the focus should not be entirely on school materials and curricula as this misses the large numbers of out of school young people and those who may not be “youth” since they are in their thirties. Quite simply, financial education should not be limited to young people but part of life-long learning. The recent financial mortgage debacles in the US demonstrate there is still very much a need for this among the adult population, too. This needs to be a crosscutting issue that is integrated into education and workforce training at all levels.

Finally, there has been substantial recognition of the benefits of financial education by the banking community, particularly larger institutions – since in large part this directly affects their customers, or in the case of young persons, their potential customers. Greater engagement among smaller banks, credit and microcredit programs, business education programs, and employers is necessary to realize the potential for positive impact that financial education offers. In the end, everyone benefits from financial education.

E- What Youth Financial Literacy Needs to Solve: Undersaving, Overspending, and the Role of Self-Control Strategies

Klaus Wertenbroch, Professor of Marketing, INSEAD

Youth financial literacy programs have to solve two fundamental problems in young consumers' financial decision making—undersaving and overspending. This paper presents a short overview of research into some of the key causes of these two problems. The research is drawn from behavioral economics, finance, and marketing. The data come from laboratory and field experiments with mostly young adult participants in the U.S. and in Asia.

Undersaving is caused both by procrastination and by overspending on consumption. Procrastination, which is, not getting started with a savings plan, is a self-control problem. I briefly review empirical findings that show how consumers and financial institutions can mitigate this self-control problem. Overspending is caused by the availability of (easy) credit but can itself also be a self-control problem. Accordingly, I also briefly review some empirical findings that show that consumer credit boosts spending to an extent that consumers themselves find problematic; they strategically try to mitigate their spending by not financing hedonic consumption. The research suggests strategies consumers can use to mitigate excessive spending.

The featured strategies against undersaving and overconsumption should constitute important components of financial education at all ages but especially as part of youth financial literacy programs. The fact that the research reviewed here shows that some consumers are applying these strategies voluntarily and by themselves suggests that policy makers ought to be able to provide enabling conditions to consumers without necessarily enforcing the use of these strategies. However, the primary purpose of this paper is not to provide empirical evidence of how policy makers can enhance financial literacy but rather to provide an overview of research into some of the fundamental causes of dysfunctional behavior in the realm of consumer finance.

Undersaving and Procrastination

A key cause of undersaving is procrastination. Consumers all too often shy away from gathering information and deciding on how to invest for their retirement or other long-term savings goals because they have to incur some (relatively) small transaction (or psychic) costs (e.g., information acquisition, getting advice, deciding among investment funds) to get started with a savings plan. It is these small but concrete costs that seem to outweigh the more abstract long-term benefits of reaching the savings goal (Trope and Liberman 2003). So everyday, consumers postpone the start of their savings or investment plan until tomorrow (e.g., Thaler and Benartzi 2004).

Procrastination and Time-Inconsistent Preferences. Such procrastination in the face of small immediate costs even though there are much larger long-term benefits has long puzzled economists and policy makers. Behavioral scientists, on the other hand, are quite familiar with this phenomenon. They describe it in terms of hyperbolic (as opposed to constant) discounting of the future—someone who discounts future events hyperbolically drastically discounts any events that are not immediate (Ainslie 1975; Laibson 1997). In other words, immediate payoffs take on a disproportionate importance in driving decisions and consumer choices. For example, someone who discounts the future hyperbolically might prefer to receive \$11 in 366 days for sure rather than \$10 in 365 days (implying a daily discount rate of less than 10%), yet they might also prefer to receive \$10 today rather than \$11 tomorrow (implying a daily discount rate of more than 10%). In other words, his or her preference reverses depending on how far in the future the two payoffs will occur, a time-inconsistent preference. More generally, such hyperbolic discounting leads to non-normative, non-rational behavior

and causes people to give in to the temptation to smoke, take drugs, overeat, overdrink, have unprotected sex, not clean up their room, delay doing their homework, watch TV, or gamble away their life's savings—along with all kinds of other dysfunctional behaviors (Loewenstein, Read, and Baumeister 2003). One such dysfunctional behavior is procrastinating with getting started with a savings strategy.

Only in the last decade have behavioral scientists begun to explore empirically whether and how consumers might try to mitigate their own self-control problems (DellaVigna and Malmendier 2006; Wertenbroch 1998). A popular self-control strategy is precommitment—much like Ulysses who had himself bound to the mast of his ship to allow himself to hear the Sirens sing without wrecking his ship on their shores, consumers are said to impose constraints on their own future freedom of choice at a time when they are not yet tempted. For example, smokers often buy their cigarettes in single packs rather than in cartons of 10 packs to make it more difficult for themselves to smoke later on when they run out of cigarettes and might be tempted to smoke more (Wertenbroch 2003).

Procrastination and Self-Imposed Deadlines. How might consumers exercise self-control by precommitment in the face of temptation to procrastinate with their savings plan? Companies, governments, schools, and other organizations often impose deadlines with penalties on their members to motivate them not to procrastinate. These deadlines impose extra costs on putting off a task (O'Donoghue and Rabin 1999a). However, when there are no such external deadlines, are people sophisticated enough to strategically impose costly deadlines on themselves (O'Donoghue and Rabin 1999b)?

In response to that question, research by Ariely and Wertenbroch (2002) provides direct evidence of the self-imposition of costly deadlines. In one of their experiments, for instance, these authors offered a group of undergraduate students at M.I.T. and Harvard University a chance to self-impose deadlines for handing in each of three term papers in a 14 week-long course. The students had a choice of committing to when to hand in these papers during the semester as long as all papers were completed by week 14. However, if the students missed any of the three deadlines, the instructor would impose a penalty of one percent of their grade for each day of delay. A significant majority of students (39 out of 51) chose deadlines throughout the entire semester as opposed to at the last possible moment, thus unnecessarily imposing the risk of incurring penalties upon themselves, making themselves potentially worse off. Why might these students have made this 'irrational' choice?

In a world without the temptation and impulse to procrastinate, such behavior seems uncalled for. Standard economic theory would suggest that the optimal deadline for each of the three papers would have been at the end of the semester in week 14. A rational decision maker with time-consistent preferences would not self-impose constraints on his or her own behavior. Nevertheless, if people procrastinate and if they are aware of that, self-imposing costly deadlines as a tool to bind them seems eminently reasonable. In fact, Ariely and Wertenbroch (2002) found that those students who spaced their self-imposed deadlines evenly throughout the semester handed in better term papers than those who did not. Overall, these findings show that people are sophisticated enough to understand the value of binding themselves to overcome their temptation to procrastinate, despite strong normative reasons for setting deadlines as late as possible. The data clearly show that procrastination is a real behavioral problem, but they also show that some consumers are sophisticated enough to take advantage of precommitment devices—deadlines in this case—to overcome their temptation to procrastinate.

An Application to Savings. Recent field research by Ashraf, Karlan, and Yin (2006) explored the use of precommitment devices to mitigate procrastination directly in a savings context. The authors worked with a bank in the Philippines to offer a random sample of their customers the opportunity to precommit to saving—by allowing them to withdraw money from a specially designated savings

account only once a specific savings goal or a specific date had been reached. Of 710 randomly chosen banking customers, 202 voluntarily signed up for such a “commitment account” even though they restricted their own flexibility by doing so. After 12 months, the average savings balance in these commitment accounts was 81 percent higher than the average balance in otherwise identical (but unconstrained) savings accounts held by those customers who had not signed up for a commitment account. This research suggests that offering consumers precommitment devices in a savings context can lead to massive improvements in savings rates. Similar to Ariely and Wertenbroch’s (2002) research on self-imposed deadlines to mitigate procrastination, these findings also suggest that a large number of consumers will recognize the value of precommitment devices on their own, without being coaxed or forced into adopting them.

Overspending and Consumer Credit

Shefrin and Thaler’s (1988) “behavioral life cycle” hypothesis suggests that people’s propensity to spend on current consumption increases with the liquidity of their available funds. Accordingly, researchers have argued that the use of consumer credit and financing tools (e.g., in the form of credit cards) boosts consumer spending because consumer credit temporarily lifts liquidity constraints (e.g., Gross and Souleles 2002). Such enhanced spending is problematic because it implies a reallocation of consumption from the future to the present as the liquidity boost from financing does not affect the consumer’s real budget constraint—having a credit card doesn’t make you any richer. That may be why retailers often provide extended credit terms to furnish consumers with enough liquidity to enable purchases that they might otherwise not make because of budget constraints. Similarly, credit card companies and banks that state a particular credit limit for their customers often seem to raise the limit without telling their customers when they have breached that limit.

Is there controlled experimental evidence that consumer financing enhances spending as would be expected if the provision of credit removes liquidity constraints? In one particularly dramatic experimental test, Prelec and Simester (2001) showed that paying by credit card yields much higher willingness to pay for a given purchase than paying cash. They sold their research participants tickets to see a National Basketball Association (NBA) regular season game between the Boston Celtics and the Miami Heat and solicited participants’ willingness to pay for a ticket. One group of participants paid cash, whereas another paid by credit card. Random assignment of participants to these two conditions ensured that there were no systematic differences between the participants in the two conditions. The authors also ensured that there were no liquidity constraints in the cash condition by providing access to an ATM to get access to additional cash if needed. They found a massive credit card premium—in one study, for instance, consumers in the cash condition were willing to pay \$28.51 for a ticket, whereas consumers in the credit card condition were willing to pay \$60.64 for a ticket, a premium of 113% caused by the availability of consumer credit.

Consumer Credit as a Self-Control Problem. Prelec and Simester’s (2001) findings on the effects of payment mechanisms demonstrate that consumer credit enhances spending. This has been linked to several possible reasons. For example, research by Soman (2001) shows that consumers do not immediately realize the full budgetary impact of making a credit card payment. That is because they do not properly encode an expense when paying by credit card and do not immediately book it against their objective budget constraint. Soman and Cheema (2002) show that consumers use the size of their available credit limit as an indicator of their future earnings potential, leading them to interpret their credit line as indicative of their objective budget constraint, even though the relationship between credit limits and future earnings is highly uncertain.

Although these findings are suggestive of problematic spending behavior, they do not show whether and when the temporary liquidity boost that consumer credit provides induces overspending

and overconsumption in excess of consumers' real (lifetime) budget constraints. After all, consumers might take the effect of consumer credit on their current spending into account when making future spending decisions; they might simply be reallocating consumption from the future to the present. On the other hand, real world observations such as the pervasiveness of consumer debt, coupled with the ease with which one can obtain consumer loans, the negative savings rate in the U.S., the record number of personal bankruptcies in the U.S., and the current mortgage crisis in the U.S. all seem to suggest that consumers borrow too much. Can we demonstrate that consumer credit tempts consumers into making purchases they would otherwise not make, given their lifetime constraint? In other words, can we show that borrowing leads consumers to overspend and overconsume? Do consumers use self-control strategies to protect themselves from giving in to their own impulses to overconsume?

Initial evidence comes from Wertenbroch, Soman, and Nunes (2001). These authors argue that relaxing liquidity constraints on purchasing (e.g., by providing consumer credit in addition to consumers' real purchasing power) is likely to lead to overspending on, and therefore overconsumption of, more tempting hedonic products (e.g., luxury or fashion goods) than of less tempting utilitarian goods (see Dhar and Wertenbroch 2000). Are consumers sophisticated enough to recognize that they have such a self-control problem (i.e., are they aware of a need for self-control; O'Donoghue and Rabin 1999b)? If so, they should avoid going into debt for hedonic purchases in an attempt to control their hedonic consumption. Wertenbroch et al.'s (2001) findings from several experiments in the U.S. and from consumer panel field data in Hong Kong show that consumers with a stronger need for self-control prefer not to finance hedonic consumption but pay cash instead or, alternatively, that they self-impose stricter payment terms when financing hedonic consumption. For example, U.S. respondents in a hypothetical scenario study were more likely to prefer a shorter but more expensive car loan to a longer less expensive one (measured as the net present value of the loan payments) when they were considering the purchase of a hedonic car rather than a utilitarian car. It is this willingness to pay a premium for limiting their own liquidity that implies that consumers are strategically trying to exercise self-control. It is important to note that such debt aversion suggests that consumers are aware and worried that they would otherwise risk overspending and overconsuming (i.e., without self-rationing their own liquidity).

Overspending and Mental Budgeting. In addition to the binding constraints imposed by debt aversion, consumers also set (economically) non-binding limits on their spending behavior by imposing mental budgets (Heath and Soll 1996; Thaler 1985, 1999). Mental budgeting entails an allocation of expenditures to specific spending categories such as entertainment such that each category has a spending limit, much like budgets used in organizations to limit expenditures. For example, you may have a \$100 budget for entertainment expenses every week. Once you have spent that money, you will then not go to see a movie, instead postponing it until next week. Unlike the deliberate avoidance of consumer financing described above, a precommitment device that imposes actual constraints on overspending, mental budgeting does not entail the automatic imposition of a penalty or of a binding constraint. This is because tracking expenditures against a budget is a malleable process that requires that expenditures are first noticed ("booked") and then assigned to the proper account ("posted"). Booking requires attention and memory, posting requires similarity judgments and categorization processes (Heath and Soll 1996), all of which make mental budgeting flexible and subject to 'fudging' (Cheema and Soman 2006). For example, if you really cannot resist going to the movie theater, you might re-categorize paying for the movie ticket as a social expense, booking it to a social budget (i.e., money available for social activities) if you decide to go and see the movie with a friend. Nonetheless, mental budgeting is a useful self-control device in that it allows consumers to partition and ration their financial resources, whose real constraints may otherwise not be salient enough to prevent excessive spending on tempting consumption categories.

Conclusion

The findings reviewed here—from self-imposition of deadlines to voluntary participation in commitment savings plans to avoidance of consumer credit for hedonic purchases—all provide evidence that a significant number of consumers are aware of their self-control problems, which O’Donoghue and Rabin (1999b) have termed ‘sophistication.’ Consumers will recognize and adopt strategies that firms and other interested institutions may offer to help them solve, or at least limit, these self-control problems, consistent with what Thaler and Sunstein (2008) have called nudging—designing choice environments in a way that allows consumers to overcome their temptation to overspend and undersave (e.g., by offering employees to precommit today to use part of next year’s raise to invest in their retirement; Thaler and Benartzi 2004). This, in turn, suggests that consumers who are perhaps less aware of their self-control problems (naïfs in O’Donoghue and Rabin’s 1999b terminology) should be taught the value of precommitment strategies early on to avoid undersaving and of overspending. This is especially important in light of research by Mischel and colleagues (e.g., Mischel et al. 1989) that has provided dramatic illustrations of how good habits established in childhood can lead to improvement on various indicators of success in later life. In a famous set of studies, Mischel tested the extent to which children were able to resist the temptation to eat marshmallows that were placed in front of them. Children who had developed simple strategies to resist that temptation (e.g., for example by distracting themselves and by not looking at the marshmallows) exhibited significant advantages in later life over those who had not (e.g., in SAT scores, social and cognitive competence, absence of drug use, and educational attainment). In summary, teaching children and young adults precommitment strategies and behavioral rules such as the ones discussed here in the context of financial decision-making should go a long way toward improving financial literacy.

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SESSION VIII- UNDERSERVED GROUPS:

GREATER FINANCIAL ACCESS THROUGH EDUCATION

Chair: Christopher F. Egan, U.S. Ambassador to the OECD

A- John Bryant, Founder, Chairman and CEO of Operation Hope, Vice-Chairman, **U.S. President's Advisory Council on Financial Literacy, United States**

B- Olivia Davids, Head of Consumer Education, Financial Services Board, **South Africa**

C- Guillermo Zamarripa, Head of the Banking, Securities and Savings Unit of the Ministry of Finance and Public Credit of Mexico, **Mexico**

D- Susan L. Rutledge, Regional Coordinator on Corporate Governance and Financial Consumer Protection, **World Bank Programs**

Policy Conclusions of the Chair

Unbanked individuals and families are found both in the developed and developing world. They are typically low income, minorities, young, less educated and live in rural areas. Access to financial services is an important means of reducing poverty and financial literacy helps break the cycle of poverty.

- Specialized financial institutions and low cost/standardized deposit products to ease access to financial tools can be developed;
- Importance of transparency and appropriate disclosure of financial information;
- Education -- particularly targeted at young individuals through media, school, non-school environments -- at “teachable moments”;
- Increasing importance of consumer protection;
- Countries are encouraged to consider a national policy on financial education and inclusion.

A- John Bryant, Founder, Chairman and CEO of Operation Hope, Vice-Chairman, U.S. President's Advisory Council on Financial Literacy, United States

Operation HOPE now operates throughout the U.S. (51 under-served communities) and South Africa, and is the nation's leading urban delivery system for financial literacy and economic empowerment to and for the under-served nationwide in the U.S.

Programs

Operation HOPE operates exclusively in under-served communities both domestically and internationally, and maintains five major program portfolios; namely (1) Banking on Our Future (youth financial literacy), (2) HOPE Centers (financial literacy to economic empowerment for all), (3) HOPE Coalition America (emergency economic disaster preparedness, response and recovery), and (4) HOPE Advisors (consultants and advisors).

Banking on Our Future (BOOF) is an award winning financial literacy program which has won both the Oprah Winfrey "Use Your Life" Award and the U.S. Treasury Department John Sherman Award for Excellence in Financial Education. BOOF has educated more than 280,000 low-wealth youth in financial literacy, in more than 1,200 schools, and with the help of more than 6,000 HOPE Corps volunteers. BOOF will soon be complimented with an additional segment on dignity, which we believe to be the "real wealth," and a young person's first HOPE Starter Savings (Bank) Account.

Banking on Our Future, South Africa (BOOF, SA) was launched in June, 2007, and has already educated more 2,000 youth and recruited 120 HOPE Corps volunteers in South Africa. In South Africa we have added a course in dignity as well as a course in entrepreneurship, as there are not enough jobs to go around in South Africa, thus the need to create self-employment projects and entrepreneurs in local communities.

We have found that financial literacy curriculum is less than the main issue impacting low-wealth and poor communities, but rather a sense of being more "poor (in spirit) than broke (financially)." Additionally, the distribution system in low-wealth and poor communities is either dysfunctional or non-existent, thus our focus on creating a reliable and consistent financial literacy-to-empowerment delivery system in these communities. Additionally, we have focused on recruiting and mobilizing a network of professionals as community volunteers, called HOPE Corps members, who bring the curriculum to life by teaching young people financial literacy through the prism of their own stories and individual life experiences.

This has the added benefit of not only teaching financial literacy and what we call the "language of Money," placing this information into the DNA of young people at the very earliest age, but also opening their minds to the magic of free enterprise and capitalism (for them), combined with the power of education, as a way out of poverty. Furthermore, the HOPE Corps members become mentors of sorts, reminding young people of what they can do, and who they can be when they grow up.

Our 5-year goal (2012) is also our challenge; to educate 5 million low-wealth youth in financial literacy, to recruit 25,000 professionals and others as HOPE Corps members, to fund \$1 billion in new home ownership and small business ownership, and to spark a new global movement around "silver rights," or making capitalism and free enterprise relevant to the poor. To make capitalism and free enterprise finally work for the poor.

The work of HOPE, and specifically BOOF and BOOF SA, is rigorously assessed and evaluated annually by independent agents.

HOPE Global Initiatives has also helped launch Global Dignity (www.globaldignity.org), co-founded by John Hope Bryant, Professor Pekka Himanen of Finland and HRH Crown Prince Haakon of Norway, which conducts Dignity Days around the world and its “A Course in Dignity” curriculum has been incorporated into much of the BOOF and BOOF SA course work.

*Note: in the urban, inner-cities of the U.S. the high-school drop-out rate often reaches alarming levels of more than 50%. We here at HOPE are convinced that young people are dropping out of school because they don’t believe that education is relevant to their futures. The way to make education relevant, we believe, is to show a young person how to succeed in life, and even to get rich, legally and with their dignity intact.

Partnerships⁷⁴

HOPE partners with more than 400 private sector partners with more than \$7 trillion in assets (U.S.), along with 2,000 non-profit and school partners, and more than 100 government partners, on a non-partisan basis.

Partners in South Africa include Citi, a global HOPE partner, the Nelson Mandela Children’s Fund, IFC of the World Bank, Standard Bank, Deutsche Bank of South Africa, CIDA University, the South African government and many others from government, community and the private sector.

People

HOPE is all about its people; from our partners (outlined above) to our 100 full-time employees, to our 6,000 HOPE Corps volunteers. The HOPE people make all the difference in the work we do.

Policy

Inspired in part by the work of HOPE, as well as by the ongoing work conducted by the U.S. Treasury Department Office of Financial Education, U.S. President George W. Bush signed a historic Executive Order on January 22, 2008, making financial literacy the policy of the federal government. Furthermore, the President created the U.S. President’s Advisory Council on Financial Literacy, which is chaired by financial guru Charles Schwab, its vice chairman is John Hope Bryant, chairman and founder of Operation HOPE, and is administered by the U.S. Treasury Office of Financial Education.

⁷⁴ For a complete list of HOPE partners please visit www.operationhope.org.

B- Implementation of the Consumer Education Strategy: Underserved/Vulnerable Groups

Olivia Davids, Head of Consumer Education, Financial Services Board, South Africa

1. The Financial Services Board

1.1 The Financial Services Board Act and Amendment

The FSB is a regulator established in terms of the Financial Services Board Act, (Act 97 of 1990) to oversee the non-banking financial services in South Africa, in the public interest. Industries supervised include insurance, collective investment schemes, financial advisers and intermediaries, capital markets and retirement funds. The FSB is also responsible for monitoring and addressing matters relating to market conduct.

Section 3 of the Act as amended in 2000, places a statutory responsibility on the FSB to *promote programmes and initiatives by financial services institutions and bodies representing the financial services industry to inform and educate users and potential users of financial products and services.*

1.2 Consumer Education Strategy

Together with full participation by financial sector bodies and other interested parties, the FSB coordinated the development of a consumer education strategy. The long-term goal of the strategy is *for all South Africans to manage their personal and family financial affairs soundly. Irresponsible financial services providers are not supported but reported.*

The strategy has three components:

- To educate consumers about effective saving and debt management
- To impart knowledge to consumers of what products and services are available and which might be applicable to their circumstances
- To ensure that consumers have a cautious approach to purchasing financial products and a knowledge of their rights and responsibilities and recourse in this regard

1.3 Measurement of Success

Measurement of success of projects is of great importance to ensure accountability and also to ensure that consumers have indeed benefited from the programme. The FSB is currently undertaking research to determine what the best ways to measure the success of various delivery methodologies would be.

1.4 Implementation

The implementation of the current strategy has not been as successful as had been hoped. Although the FSB will be entering its 5th year of partnership with the short-term insurance industry to educate consumers, more work needs to be done to bring more industry bodies on board.

However, the FSB's consumer education strategy which was approved in 2001 is currently under review. We want to pay more attention to coordination to minimise duplication of effort in terms of programming and to maximise the use of scarce financial resources.

2. Underserved groups

In South Africa, 19 million people or 63% of the adult population fall within the lowest income groups, 94% of them are Black, while 79% of them earn incomes of less than about USD 121 per month. Sixty-eight (68%) percent are unbanked, while 95% are not insured (either long or short-term), 38% have funeral or burial insurance and only 8% have formal insurance. Only 8% of this market has a compulsory retirement savings product (but this could be an understatement).

3. Challenges

The FSB's consumer education programme takes place on two fronts, namely, at the community level as well as in the formal education sector. The following are some challenges that need to be addressed in both sectors in order to provide effective consumer education programmes for low income consumers:

- Low levels of education and skills
- The use of risky informal savings methods
- Squandering money on “get-rich-quick schemes”
- Living in isolated rural communities with limited infrastructure
- Lack of access to financial services such as banks, insurance, among others
- Lack of knowledge about financial products and services
- Not complaining, not knowing how and where to complain
- Borrowing from micro lenders at exorbitant interest rates
- Patronising unregistered business
- Teachers not sufficiently equipped with the knowledge and materials to teach financial consumer education according to the curriculum

4. Best practices for enhancing financial capability

This section is limited to a listing of practices that have worked in South Africa for educating low income consumers. It should also be noted that success resulting from the practices listed below is not defined in terms of in-depth research but on the basis of on site responses from programme participants, workshop facilitators, funding partners, key community representatives and service providers. As mentioned earlier, the FSB is about to embark on research into the measurement of success so that we can have more substantial and reliable information.

- Best to use a multifaceted approach with messages being repeated via a variety of formats such as face-to-face interaction together with media awareness
- Absolutely no marketing
- Limited branding
- Mother tongue presentation/facilitation of education as well as translated materials; use plain, clearly understood language
- Take the education to the people with road shows, outside broadcasts at shopping malls, taxi ranks, key organisations such as the House of Traditional Leaders, the Council of Churches,

educate those waiting in queues at social grant pay points (pensioners and child grant recipients), work with employee assistance programmes, school leavers, persons with disabilities, participate at careers fairs and exhibitions

- Train service organisations such as advice office staff, the police
- Work with national and provincial departments of education to provide content and to assist with developing lesson plans and teaching posters for teachers to use in the classroom
- Always include an assessment component in each project
- Make use of accredited service providers or take great care in selecting them
- Conduct an informal audit of projects to ensure that all project conditions are met

5. Innovative products

Although the FSB does not regulate products or product standards, but since we are discussing access issues in relation to low income consumers, it would be worth mentioning some efforts by the financial sector to introduce affordable products targeted at consumers in this group. Efforts in this regard were largely brought about by industry commitment to the Financial Sector Charter.

5.1 The Financial Sector Charter

The Financial Sector Charter was signed in South Africa in October 2003 by major players in the financial sector including banks, insurance companies, brokers and exchanges. The purpose of the Charter was to set in motion the implementation of initiatives aimed at meeting documented product service and empowerment targets such as, for example, targets for the achievement of effective access to banking, insurance and investment services for underserved consumers. As a matter of interest, another commitment by the financial sector bodies through the Charter was to spend 0.2% of after tax profits on financial consumer education.

5.2 Access products

5.2.1. Mzansi bank account

The Mzansi bank account was launched in 2004 as a means of extending banking services and products to low income people. Bank branches were built into containers and mini automatic teller machines were employed in the rural areas and townships in order to make this product more accessible. All that is required to open this low-cost account is a valid identity document. Transactions are limited to deposits, withdrawals, transfers (anywhere in South Africa) and debit card payments. No management fees are charged and one free cash deposit per month is allowed. These accounts are available at major banks as well as at the Post Bank (post office).

The Finscope 2006 survey results indicate that the growth in the banked population in South Africa has been fuelled by the increased use of Mzansi accounts. The fact that 81% of those surveyed are using the Mzansi account mostly for withdrawals, could point to the possibility that more awareness about product features may be needed.

5.2.2. Mzansi Short-term insurance standards

These are standards that have been developed by the short-term insurance industry to apply to products targeted at low income consumers and in keeping with the Financial Sector Charter

requirements of affordability and accessibility. These are no-frills policies aimed at providing cover for the household structure, household goods and personal effects against specific risks such as fire, lightning, explosions, storms, floods, impact and theft. Consumers are encouraged to shop around and check with various dealers as the products bearing the Mzansi stamp of approval are available under different names.

Some examples of distribution models are:

- The provision of limited advice such as in the sale of a product through a “tick-box” method which minimises reliance on intermediaries or brokers who have been accredited under the Financial Advisory and Intermediary Services Act. This kind of distribution involves no advice to the consumer but can involve some basic explanation of product features. Intermediaries who give financial advice must be registered with the FAIS Department of the FSB. An example would be the sale of insurance through a retail sales store in which case the product is not actively sold by the staff of the store but rather is sold just as any other commodity is sold in the store.

While this model may work for selling a product that is already “made” such as the funeral insurance market in South Africa, it is difficult to use this method to sell products to consumers with which they are not familiar such as cell phone insurance. Selling unfamiliar products requires intensive effort to inform and advise in order to “make the market”.

- The second model was used to sell an unfamiliar product, namely, household structure and contents insurance to the low-income market. This involved active selling by sales people or “runners” that are not accredited under the FAIS legislation and therefore are not allowed to give advice. The runners would provide information on the product and as soon as the client became interested in the product, the runners would refer the prospective client to a registered broker who would provide advice. This model was discontinued because of the high turnover of runners.
- A third model, an airtime distribution model, which has also been discontinued, was used to sell a funeral insurance product which was packaged in a cell phone starter pack. It was the client’s responsibility to ask for the funeral insurance product in the cell phone airtime vendor’s store and no advice was provided to the client.
- Other models that are still being tested include entering into a partnership with a group of people, for example, a church group to distribute a short-term insurance product through the group structures and accompanied by financial consumer education. Another model planned for the near future uses a referral concept to reach an ever growing pool of linked people. Another new model soon to be introduced will involve a partnership between an insurance company and a cell phone banking company to distribute both insurance and banking products as well as enabling ease of premium payment.

5.2.3. Zimele Long-term insurance standards

The long-term insurance industry launched its Zimele (a Zulu word meaning “stand on your own”) standards in February 2007. These standards aim to give low income consumers access to life insurance. The first set of Zimele branded products are funeral policies. In order to make these products truly accessible and in keeping with Charter requirements, the industry would have to identify and use new distribution channels to ensure profitability of the low income market because these products would have smaller profit margins.

Some distribution mechanisms include direct marketing, face-to-face advice, and traditional broker networks.

There have been recent reports about a number of challenges being encountered with the sale of these funeral policies. Consumers in the low income categories tend to prefer informal funeral products such as those available through burial societies and funeral parlours even though these product sources can be more expensive. Finmark Trust, in a recent report indicated that the Zimele standards and associated products are not visible in the community for which they were intended. Long-term insurance companies are not branding their low-income insurance products with the Zimele brand. In addition, insurance brokers are not pushing Zimele products because of the small commissions involved.

5.2.4. The Fundisa Fund

The Fundisa fund was developed by the collective investment industry to meet the Charter requirements of access and affordability. It is a savings vehicle for the education of students at Further Education and Training colleges (similar to community colleges in Canada) and universities and is based on the Canadian Education and Savings Grant model as introduced by the government of Canada in 1998.

The Fundisa Fund enables parents, family or friends to contribute to the costs of further education for a child. The investor receives a 25% bonus as an incentive for making the savings. Investors may access their savings at any time, like a normal unit trust. However, if they do this, they will forfeit the proportionate amount of the bonus. When the student is ready to study further, the money is deposited directly to the chosen institution. The bonus has been made possible by the Department of Education and donations from leading collective investment companies. This Fund can be initiated at the major banks as well as the post bank.

In terms of distribution, the investor must have a bank transaction account in order to open a Fundisa Fund account. Face-to-face promotions are conducted in bank branches situated in townships and all distribution mechanisms are supported by a call centre. Multilingual brochures have been produced and the industry body that developed this product has a multilingual Fundisa Fund website. Presentations in communities in addition to the development of audiovisual promotional material are in process.

Fundisa was launched in November 2007. To date take up has been slow, but there is a steady increase in the number of accounts being opened.

Since the introduction of all these access products and distribution models has been recent, there are opportunities for continuous improvements in all aspects of making affordable products accessible to low income consumers.

6. Role of Stakeholders

Stakeholders can be effective partners in the education of consumers by bringing their various mandates, expert knowledge, and logistical mechanisms among others, into play. They can be helpful as members of task teams to provide input into strategy development, materials development, programme planning, project implementation and management or they may simply wish to donate funds toward the implementation of a particular project.

7. Conclusion

In order to make financial education available on the required scale, serious financial and other commitments from all role players are necessary. All indicators point to the need for widespread, sustained, successful, long-term, focused, coordinated, tailor-made educational programmes coupled with longitudinal impact assessment research. Consideration should also be given to the education of businesses that market financial services and products in order to increase their understanding of issues impacting on consumers

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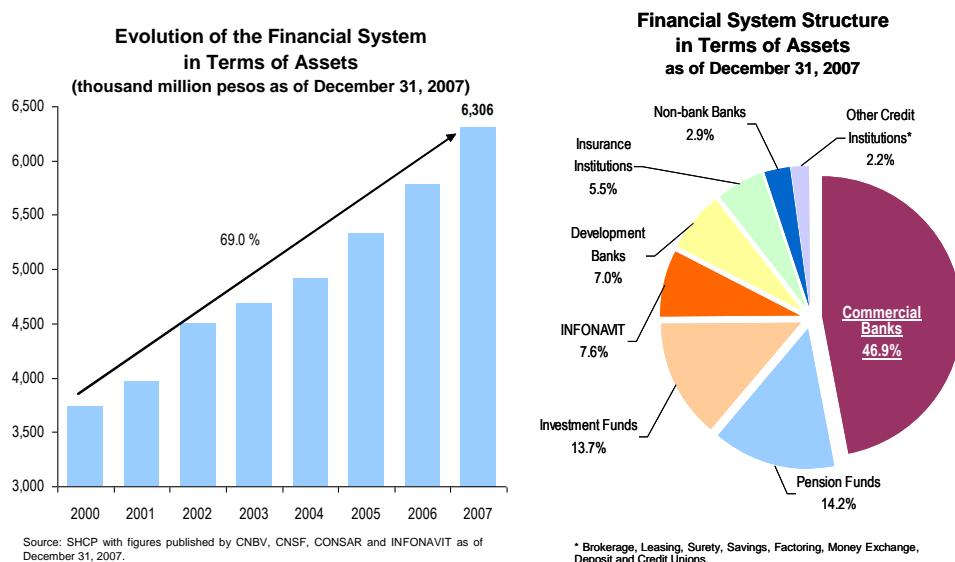
C- Greater Financial Access through Education

Guillermo Zamarripa, Head of the Banking, Securities and Savings Unit of the Ministry of Finance and Public Credit of Mexico, Mexico

Financial system

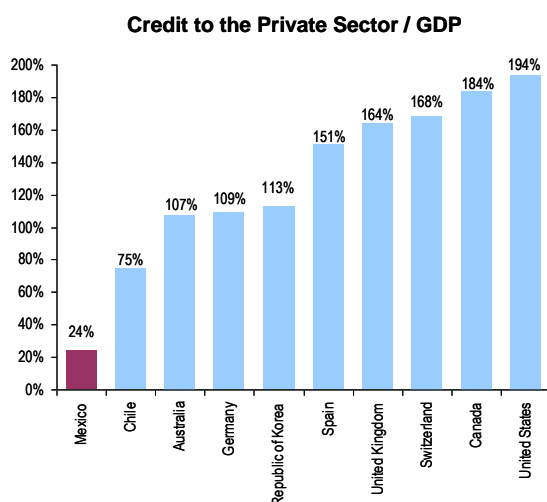
The Mexican financial system has grown 69% in real terms during the last 7 years. This was strongly propelled by the competition in different market segments, particularly the banking system which held, at year-end 2007, 46.9% of the total assets of the system.

During this period, the structure of the system experienced changes and in the forthcoming years, it is expected to continue changing. Within the credit segment, players such as the “Sofoles” (non-bank banks), have found their specific niche and become effective competitors to reach underserved sectors of the population. In this sense, at the end of 2007 the market share of Sofoles, in terms of total assets, went up to 2.9%.



With respect to financing to the private sector as a percentage of the GDP, this ratio increased 7.3 percentage points from 2000 to 2007, from 16.9% to 24.2%. In this context, the most active intermediaries in granting financing to the private sector were the commercial banks which accumulated real growth from 2000 to 2007 totalling 124.7% growth. The debt (bond) corporate market which provided financing for enterprises and cumulated, in the same period, experienced growth in real terms of 161.4%.

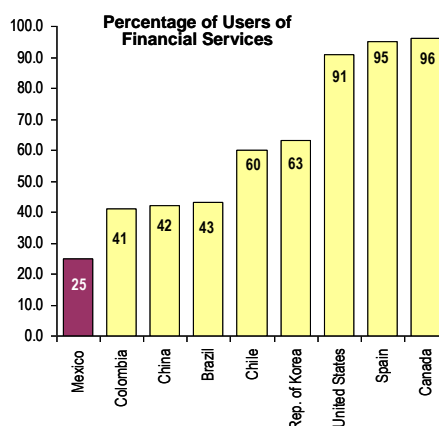
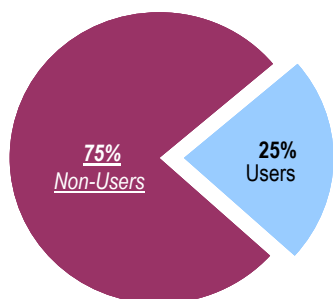
Nevertheless, this growth in financing to the private sector is low when compared to other countries and to their level of financing as a percentage of GDP. Taking for example, Republic of Korea or Chile, financing to the private sector with respect to their GDP, the ratio is 113% and 75%, respectively, while Mexico's is barely 24%.



Source: SHCP with figures published by CNBV, Banxico, INEGI and World Bank; A new database on Financial Development and Structure; Thorsten Beck, Asli Demirgüç-Kunt and Ross Eric Levine. Figures of Mexico as at December 31, 2007. Figures from other countries as at December 31, 2006.

Access to financial services in Mexico

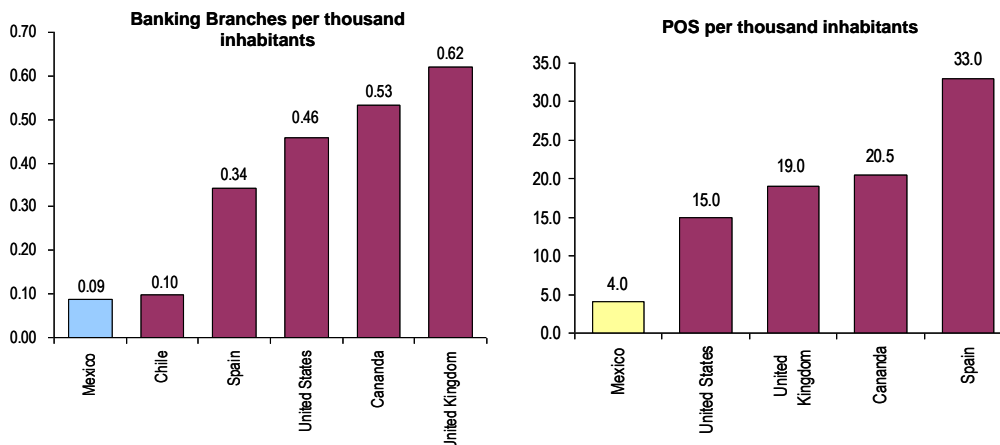
According to a World Bank publication (*Finance for All?*⁷⁵), only 25% of the population in Mexico has access to financial services, measured as the percentage of the adult population with access to an account with a financial intermediary. When compared at the international level, the access in Mexico to the financial market is low⁷⁶.



The level of financing as a proportion of the GDP is related to the access to the market and the availability of financial services to the population. In this sense, the access to financial services in terms of infrastructure in Mexico is also behind other economies. While countries such as Spain have 0.34 banking branches per thousand inhabitants, the figure for Mexico is 0.09. In these same meanings, in terms of point of sale terminals (POS) per thousand inhabitants, the figure for Mexico is one fifth that for Canada.

⁷⁵ Finance for All? Policies and Pitfalls in expanding Access. A World Bank policy research report.

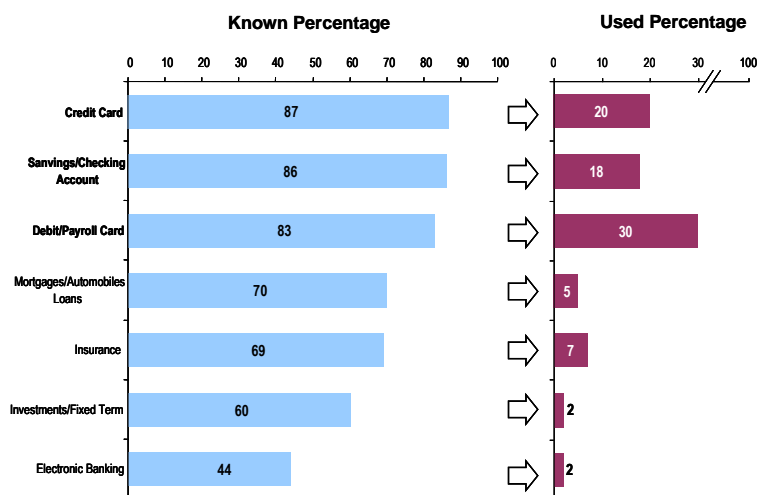
⁷⁶ It is worth mentioning that most of the underserved population is located in the lower income levels, lower education levels and lives in rural communities.



Source: Banco de México data as of December 31, 2007; Asociación de Bancos e Instituciones Financieras de Chile; Banco de España data as of June 30, 2007. United Kingdom, United States and Canada (CONDUSEF), data as of March 2006. Population data: INEGI and World Bank.

Demand for financial services

In this respect, the financial authorities conducted survey research on financial services among the population and reported a series of conclusions on the demand for financial services. Based on the results, it was concluded that on average, 85% of the population has heard about credit cards, saving / checking accounts and debit / payroll cards, nevertheless, only 22.7% on average, has used these products.



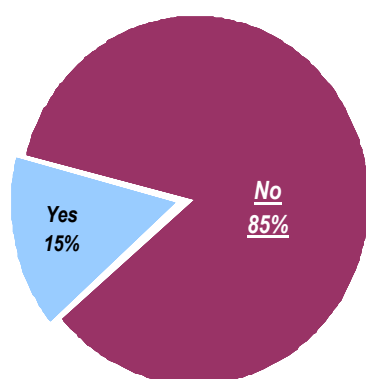
On the other hand, the underserved sector has traditionally found a way to obtain financing, from family and friends to moneylenders, which sometimes are expensive and unsafe. Other sources are neighbors and employer thrifts, among the most important. In this sense, the survey revealed that informal financing provided 75% of the loans during the last 12 months and that 18.2% of individuals assume that informal saving communities are the only way to save.

Savings	%
Informal savings community ("tanda")	26
Cash at home	22
Grant a loan	11
Family, neighborhood or community savings group	5
A family member takes care	5

Financing	%
Family & Friends	81
Employer thrifts	10
Neighbors	2
Moneylenders	1
Others	3

The survey also revealed the population's attitude towards financial services that limit access to the financial system. Among others, the survey answers could be provided in the absence of available resources and lack of information.

Are you interested in having any product/service with a financial institution?



Source: Primera encuesta sobre cultura financiera en México. Banamex-UNAM.

What is the reason you are not interested?	%
"Do not have money"	22
"Interest rates are high"	12
"Do not feel like / Not interested"	11
"Do not need"	7
"I do not have a job"	5
"They ask for too many requisites"	3

Note: Most frequent mentioned reasons were only included, the sum does not add up to 1000%.

Although there is an unsatisfied demand for financial services, it could also be concluded from the survey that there is a large portion of the population that is not interested in services from financial intermediaries. In this sense, the negative perception of the surveyed individuals could be related to lack of knowledge on financial services.

Benefits of increased access

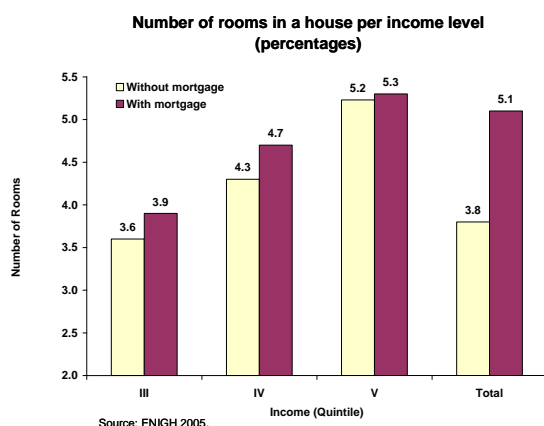
One of the main objectives of the financial authorities in Mexico is to promote the use of formal financial services given the correlation between the household's access to these services and their higher living standards. Empirical evidence reveals that on average, those households with access to a credit card loan have a greater level of benefits than those without access.

Differences between households holding a credit card loan

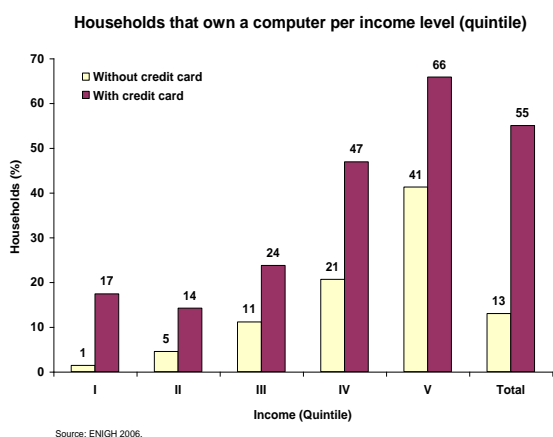
	Without	With
Households that own a car (%)	21.8	65.0
Households with internet (%)	4.3	30.5
Households with cable tv (%)	15.3	54.4
Households with cellular phones (%)	42.3	85.7
Households with a telephone line (%)	45.4	83.4

Source: ENIGH 2006

For instance, the proportion of households owning a car and having access to a credit card loan is almost 3 times greater than those households owning a car but without access to a credit card loan. In addition, other statistics confirm that access to financial services includes benefits correlated to quality of life, such as the size of the house and the presence of household appliances.



There may be circumstantial benefits of having access to financial services.: For example, those individuals who have access to financing would be enabled to buy a computer, which in turn could be used to access the internet.



The potential benefits for the population are based on the capacity of the authorities and financial intermediaries to provide formal access to the system to new users, thus reducing the percentage of underserved individuals.

In this sense, financial authorities are required to provide the individuals with an adequate environment for saving their income for future retirement, contracting a loan to finance their personal projects, basic protection from external risks and adequate disclosure on consumer credit obligations. This in turn, will contribute to guarantee the soundness of the financial system and to encourage competition within the system.

Actions addressed to increase financial access

Given the low level of access to financial services, the authorities have worked on different aspects to enhance the regulatory framework and foster access to individuals. The aim is to expand the

coverage of financial services throughout the population and to enforce clear and legible information be made available to consumers. These efforts could be classified as follows:

a) Actions to increase access.

With the aim to promote the entrance of new participants into the market and foster competition, on December 2007, Congress approved a number of reforms to the Credit Institutions Law including the regulation of specialized or limited licensed banks. These institutions would be required to comply with specific regulation in accordance to the activities performed.

In addition, in June 2007 the Congress approved a law that requires banks to offer a cost-standardized deposit account, exempted from opening, cash withdrawals or consultation fees. This product is intended to facilitate access for the low-income segments of the population.

b) Actions to provide increased consumer protection standards.

In June 2007, reforms were published in the Official Gazette to the law regulating transparency in the offering of financial services. Such reform is intended to promote greater consumer competence through the disclosure of comparable information among the different financing alternatives. It also strengthens the faculties of the *Condusef*, the national agency for financial user's protection.

c) Actions to enhance financial education.

In this respect, the authorities launched the National Strategy for Financial Culture, which seeks to develop among the population training on financial tools required to improve their decision making abilities while searching for financial services alternatives. The objective of the National Strategy is to increase the ratio of financing to the private sector as a percentage of the GDP to 40% by 2012.

Some aspects of the National Strategy on Financial Education, which the Mexican authorities will undertake in the future with the aim to increase financial inclusion, include:

- a) A nationwide media campaign for financial education;
- b) Promotion of the *Condusef*;
- c) Introduction of financial education textbooks at elementary schools;
- d) Financial literacy programs in the work place; and
- e) Workshops for financial educators.

Conclusion

The Mexican financial system has grown 69% in real terms during the last 7 years. Despite this growth, when compared to other countries and their financing as a percentage of GDP, Mexico is much below other countries with similar GDP per capita. Furthermore, in terms of infrastructure, such as banking branches, POS or electronic payment services, Mexico differs greatly from other economies.

From the observed situation, characterized by the low access to financial services, the authorities have identified the need to establish complimentary policies focused on reducing the lack of financial education on the overall population.

To overcome this situation and encourage a higher standard of living for the population, the authorities have implemented different actions in order to communicate and educate the population on financial services. In addition, the authorities have amended the regulatory environment required to provide enhanced access to the financial market.

Furthermore, the authorities have launched the National Strategy for Financial Education, which encompasses different activities to increase financial education and provide greater consumer access to the Mexican financial market.

D- Consumer protection and financial education in developing countries: Reaching underserved communities

Susan L. Rutledge, Regional Coordinator on Corporate Governance and Financial Consumer Protection, World Bank Programs

Financial markets can be complex and opaque, giving consumers little opportunity to assess the risks and costs (or returns) of the products being offered.⁷⁷ Consumers need financial services that are transparent and fair. However excessive regulation can drive up prices, inhibit competition and even increase risk levels. Determining the right level of regulation is not always obvious and governments have tended to respond to abuses by over-reacting to events, particularly where wide media coverage is involved. The World Bank Group has been examining the scope for a proactive and measured approach to financial consumer protection.

Work on the ground has demonstrated that it is the poor and other low-income households that are most vulnerable to unethical financial behaviors. Countries should focus on three areas: (1) Customers of financial institutions should receive information that is clear, complete, accurate and comprehensible before they decide to borrow or invest or purchase a financial product. (2) Consumers should have access to recourse mechanisms that are efficient and cost-effective. (3) Consumers should have the right to education that allows them to become financially literate so that they can make informed decisions. The starting point for all countries is financial literacy.

In 2007, the World Bank brought together a team of leading experts in banking, insurance, securities and pension funds to study and share the experience of consumer protection in retail financial markets worldwide. They developed a set of good practices that in turn has provided an analytical tool (or template) to assess a country's approach to financial consumer protection. The first two reviews were conducted for Slovakia and the Czech Republic. Based on earlier work and these reviews, this note highlights some key issues and lessons to be learned.

Financial consumers need protection in both developed and developing economies

Appropriate consumer protection in financial services strengthens the financial sector. Due to the uneven bargaining position individual consumers can find themselves in vis-à-vis financial institutions, effective consumer protection ensures that the borrowers and savers have confidence in the financial system--and are willing to use it. There are numerous examples worldwide where financial sectors have failed to develop because of unfortunate early experiences with weak consumer protection.

Participation of retail consumers benefits the financial system by increasing the liquidity of the system, deepening the sector, and increasing financial intermediation as needed for a modern vibrant economy. It is estimated that 150 million new financial consumers are added to the global economy each year.

Regulatory intervention is needed in consumer protection for five reasons:

- Information may be costly or difficult for an individual consumer to obtain.

⁷⁷ Prepared by Sue Rutledge, Senior Private Sector Development Specialist in the Europe and Central Asia Region of the World Bank (srutledge@worldbank.org). The note is based on reviews on consumer protection in financial services for Slovakia (July 2007) and the Czech Republic (June 2006). Both are available at www.worldbank.org/eca/consumerprotection.

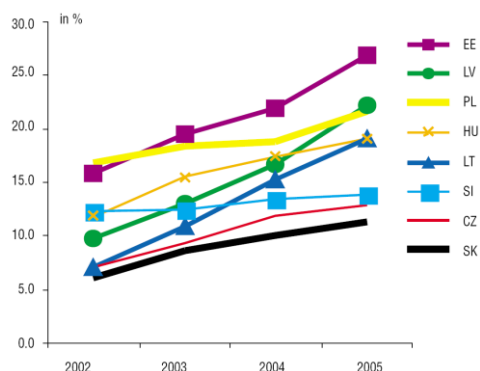
- Complex financial products can be difficult to assess, even when all relevant information is available.
- Consumers fear that financial institutions have an information advantage over them and may take advantage of unsuspecting customers (known as asymmetric information or the “lemon problem.”)
- Low-income consumers may be excluded from acquiring access to the financial system by financial institutions with short time horizons.
- Brokers selling financial products may sell products that have high commissions for the broker but are unsuitable for the customer.

However excessive regulation can bring negative unintended consequences and increase prices for consumers. An appropriate balance between too little and too much regulation is needed.

Growth of household debt has brought new attention to consumer protection

Over the past five years, household borrowings worldwide have grown rapidly. In the emerging economies of central Europe, for example, consumer debt has doubled in relation to national economies (see table.)

Figure 1. Consumer Debt vs. GDP



Source: National Bank of Slovakia using data from the European Central Bank

At the same time, financial institutions have increased the use of foreign currency lending to households. For example, in Poland in 2006 over 60% of all consumer borrowing was in foreign currency, primarily Swiss Francs but also in Japanese Yen.

Recent problems in U.S. housing loans to subprime borrowers (i.e. those with patchy credit histories) have highlighted weak disclosures to borrowers. As of April 2008, estimated losses from subprime lending were over \$500 billion, representing over 4% of U.S. GDP.

The poor are particularly vulnerable to financial abuse

Low-income households are the most vulnerable groups where consumer protection is weak. Increasingly one cannot participate fully in society without being "plugged in" to the financial system through a current account and a credit card. For low-income consumers, financial institutions can make it difficult to acquire these gateway products. Sometimes the requirements of anti-money laundering legislation, if inflexibly administered, can be used to reduce the access of low-income consumers to the financial system.

Low-income households are also more likely to spend more of their income on debt payments than high-income families. In Slovakia, a 2005 household survey found that those without formal employment pay 38% more of their gross household income in loan repayments, including mortgages, than do families where the head of the household has a steady job. Low-income households in Slovakia were also the most likely to borrow from high-cost providers of credit, through credit cards at about 25% p.a. (vs. 12% for bank loans) or short-term installment sale loans at up to 240% p.a.

Regulators should ensure that sales and collection practices are fair--and disclosure is complete

Disclosure of standardized information is a first step in consumer protection. In the Czech Republic, the Consumers' Defense Association complained that when borrowers tried to pay off loans earlier than originally planned, hidden prepayment penalties amounted to 100% of the original amount of the loan.

All financial institutions should be required to provide a standardized *Statement of Key Facts* for consumers at the time of contract signing. For credit products, the key facts could include:

- Annual Percentage Rate (APR),
- Total amount of the credit,
- Amounts of monthly payments,
- Final maturity of the credit or investment,
- Total amount of payments to be made,
- All fees including prepayment and overdue penalty fees,
- Any required deposits or advance payments,
- If the interest rate is variable, the basis on which the calculation is made, and
- If any additional insurance (such as personal mortgage insurance) is required.

Sellers of financial products are often permitted to sell financial products door-to-door or by telephone. While such sales provide convenience for some customers, consumers should be protected from predatory lending and abusive collection practices. A "cooling-off" period of 7-14 days is a useful standard for all financial products sold outside of the offices of financial institutions. Collection agencies should also be limited to defined times of day when they can call.

A larger issue lies with unlicensed and poorly regulated intermediaries. All sellers of financial products should be subject to standards of fitness and propriety (competency and honesty) and be properly qualified, with minimum training depending on the complexity of the products sold. All intermediaries should be registered or licensed. Sellers should also be required to assess the suitability of the product for the consumer who purchases it. Sales of 30-year annuities to the elderly make little sense.

In addition, intermediary markets will only operate to the benefit of consumers when the incentives offered to the intermediaries are aligned with the interests of consumers. Thus volume-driven commission structures militate against quality sales. On the other hand a commission system that rewards good business (measured for example by persistency in insurance contracts) will produce beneficial outcomes for consumers and the market.

Consumers also need to be assured that their financial information is kept private and secure through effective data protection laws. At the same time, financial institutions need accurate information about their customers through efficient credit bureaus and systematic credit scoring systems.

Efficient dispute-resolution systems are needed for small financial claims

Most customer disputes with financial institutions are relatively small at under \$500. Even in countries with honest and efficient courts, such small claims do not warrant the time and expense of litigation. Yet consumer confidence is undermined where no effective system of dispute resolution is in place.

All financial institutions should be obliged to maintain departments to receive customer complaints—and the complaints should be reviewed in the course of annual inspections by the supervisory agency. Furthermore financial institutions should be obliged to have a formal complaints-handling procedure that is made available to consumers. Some countries have also established financial ombudsmen with authority to take decisions on small claims and require corrective action by financial institutions.

In addition, the banking and other associations should develop codes of conduct to establish minimum practices in addressing customer relations. Consumer protection organizations can also play a helpful role in identifying common forms of customer complaints—and assisting low-income borrowers in renegotiating burdensome loan terms and conditions.

Financially literate consumers are best prepared to protect themselves

Consumers who are well-informed and financially-literate are better able to make sound financial decisions for themselves and their families. They are able to increase their financial well-being and ensure economic security in times of financial crisis. They are also able to protect themselves from unscrupulous sellers of financial services and make it difficult for sellers to use unfair or deceptive practices.

Research in the U.S. indicates that in the residential mortgage market, predatory lending generally occurs in the "subprime" market where borrowers with weak access to credit use the collateral in their homes for debt consolidation or other consumer credit purposes. However subprime borrowers often have weak financial literacy. In one U.S. survey, 12% of subprime borrowers were unfamiliar with basic financial concepts such as the definition of "principal" and "interest." One-third also claimed that they were not familiar with the different types of mortgage products available.

U.S. surveys of financial consumers have found that the most effective form of financial education is through the media. In one survey, 71% of all consumers chose television, radio, magazines and newspapers as the preferred way to learn about personal finances. Information brochures and presentations at home were the second best method of acquiring financial expertise.

Other approaches have also been used. For example, in 2005-06 the European Commission funded the development of the DOLCETA program, which provides an online training tool for use by teachers of adult education. In addition in 2006, the Commission funded a study of financial education initiatives throughout the European Union. The objective was to exchange best practice models for improving the access to financial services for those suffering from poverty and social exclusion. Focus was placed on highly-indebted consumers.

Regulatory agencies should play a role in alerting consumers to illegal practices. One useful approach would be to set up a “Consumer Affairs” page on the home page of the regulator’s website. The page could link to consumer and investor alerts, thus making it easy for consumers (and their advocates) to identify possible scams and schemes from unauthorized financial institutions—with regular distribution of press releases to the media.

Financial institutions should be active in educating their customers. Financial counseling prior to signing a mortgage can help to reduce payment delinquencies. In one U.S. survey of 40,000 mortgages conducted between 1993 and 1998, the effect of individual counseling was to reduce the delinquency rate by 34% compared to those who had received no counseling. Classroom training and home study also helped to reduce delinquencies by 26 and 21% respectively.

Specialized institutions can also be established for consumer education and financial literacy. To be effective, a financial education institute should conduct a baseline assessment of the current level of financial literacy, using perhaps methods applied in other countries. Several years later, a follow-up assessment should be conducted to see if the consumer education and financial literacy program is working or if it should be revised to improve its effectiveness and penetration.

One approach would be to use a financial awareness quiz, administered through a consumer survey, to test consumers' understanding of retail financial services. Special consideration should also be given as to how to reach the low-income groups and advise them of their legal rights and institutions available to help them. The institute should also help to set up a national education program through the universities and middle schools to develop programs of financial literacy for students of all ages.

Consumer protection organizations and the media could also play a helpful role. The voluntary consumer protection organizations need to have sufficient expertise and resources to deal with financial sector issues. It may be helpful to encourage one, or several, of the current organizations to specialize in financial issues. In addition, newspaper columns on financial issues should be encouraged. Regular columns on financial matters for consumers can be very useful for the general readership who is generally retail investors and consumers.

In the end, individuals who are literate in financial matters will be empowered consumers and better able to protect their rights.

CONCLUDING REMARKS

Henry M. Paulson, Jr., Secretary of the United States Treasury

Introduced by Carolyn Ervin, Director for Financial and Enterprise Affairs, OECD

Thank you very very much. I am honored to be here. Having sat through a number of conferences myself, I know how eager people are to hear the last speaker of the day. And I think what you are probably most eager for is to hear the end of my remarks.

But despite that, I am very much looking forward to giving them, because it is a very important topic.

And it is my great pleasure to be here, and I want to thank you all for your commitment to financial education. As I look around the room I know some of you very well, as I have worked with you very closely. And I know all of you are very much involved here.

I want to thank the OECD and OAS for your support, and assistance, in preparing for this conference.

I was in Kansas City, Missouri, this morning, and I visited the Treasury Financial Management Service facility there and watched them print the first batch, if you can call almost half a million checks a batch - of economic stimulus checks. This is the first day of mass production of those checks, and the Financial Management Service facilities in Kansas City, Philadelphia, San Francisco and Austin prepared over two million checks alone today.

This is in addition to direct payments that were sent last week, 75 days after President George W. Bush signed the economic stimulus act of 2008, to provide individual payments and business incentives to boost the U.S. economy.

By the end of this summer about 130 million Americans will, either through paper check or direct deposit, receive nearly \$100 billion in economic stimulus payments. These payments along with the business incentives also included in the act will provide a boost to the U.S. economy by the middle of the year. And they will also lead to the creation of half a million jobs this year that wouldn't be created otherwise.

I mention these payments because they coincide with the purpose of this conference. People can decide how best to use their payments, and people everywhere want to know how to wisely spend, save and invest their money. They want to build a more secure and prosperous future for themselves and for their families.

This conference is particularly timely as we work through a difficult economic period. I hope you will return to your countries and your organizations with new ideas about innovative methods and strategies that will improve financial literacy around the world.

People everywhere can certainly benefit from becoming more financially literate. Financial knowledge makes people better informed consumers, and when they understand the terms of a car or a mortgage loan, they are better able to compare the costs and benefits of different products, and they are more likely to make long term decisions and advance their financial goals.

This is a worldwide concern. We want all our citizens to have financial knowledge and we all recognize that in an increasingly connected global economy broader knowledge will bring stronger economies that benefit us all; we are all connected.

And not only is the world becoming more connected, financial products are becoming more complex. And this raises an even greater need for financial education.

President Bush recognizes this. In January of this year he created the President's Advisory Council on Financial Literacy to bring the vital resources and perspectives of the private sector to assist the American people in understanding and addressing financial matters.

The Advisory Council joins the Financial Literacy and Education Commission in this growing effort. Created by Congress in 2003, the Commission is made up of 20 federal agencies, each contributing in its unique way to improving the nation's financial literacy.

Under the President's leadership, this combination of public and private sectors can accomplish great things.

One key area of focus is on our young people, because this is where we have the best chance to make a difference over the long run. The concepts of financial literacy can be taught to young people before they become young adults, and start to need a lot of things. Any parent will tell you it is what is needed and what is wanted that tends to get confused in children's minds. I know, I am seeing it with grandchildren; I need this, or I need that.

What parent has not told their child, money does not grow on trees. The Treasury Department is doing some good work in this area. Earlier this year the Advisory Council recommended that the Treasury launch Money Math, a curriculum for middle school students. These free lesson plans teach the concepts of mathematics, and use relevant personal finance examples.

And rather than having to choose between teaching math or financial topics, teachers can integrate them into the existing curriculum, and teach both at the same time. In just a few months nearly 40,000 people have downloaded these lesson plans.

Our efforts to help young people extend farther. We believe we can reinforce the good work of financial educators by offering teachers and students special recognition, which is always a powerful incentive.

So last week Treasury also launched the National Financial Literacy Challenge, another initiative recommended by the Advisory Council. This online voluntary test of high school students measures personal financial knowledge. In just 10 days more than 10,000 students nationwide took the challenge.

The top scoring students will receive certificates or medals. For the best of the best, the Charles Schwab Foundation is offering college scholarships.

Last week 15 Treasury officials also volunteered for the annual Teach Children to Save Day. This is the fifth year the Treasury has been part of this program. They visited elementary and high schools across the country, and helped teach more than 1,200 kids the difference between a need and a want, and how even they can save money for the future to help pay for college, a bike or a car; or maybe even a Mother's Day gift.

These are but a few examples of the programs we have here in the United States. I know there are similar programs around the world, the Malaysia Central Bank, along with the Malaysia Ministry of Education and the financial institutions, are also reaching out to school children.

Since 1996 Malaysia has had a savings campaign to create both a savings habit at an early age, and an awareness of the importance of smart financial management and planning.

There are financial literacy programs in Poland, in New Zealand, in the United Kingdom, and in many other countries represented here today, programs that rely on school, government and even health care assistance, to find teachable moments for financial education.

This is such important work. I commend you and encourage you to contribute. And I support current OECD efforts in financial education, and especially the development of good practices and guidelines.

The OECD has already developed good practices in insurance and pensions. And these were endorsed by the OECD council this year.

The OECD work is valuable. It should continue and extend into other issues.

I also offer special congratulations to the OECD for launching the international network on financial education earlier this week. Here at Treasury, the Office of Financial Education works to increase awareness of financial literacy issues through public outreach, disseminating voluntary standards for financial education, and providing technical assistance to financial educators, nonprofit organizations, and to state and local governments among others.

Through its events, materials and outreach, the Office has reached hundreds of thousands of people in the United States and abroad.

It also coordinates the efforts of the new President's Advisory Council on Financial Literacy and the Financial Literacy and Education Commission.

Thank you again for coming to this conference, and for participating and sharing your ideas.

I hope you will return home newly invigorated, and full of new plans. I will look forward to learning more about programs in other countries, so that the United States can adapt and adopt the best of what is being done around the world.

Thank you all very much, and congratulations again on a good conference. And enjoy the evening. Thanks.

APPENDIX

**PROGRAMME OF THE OECD/US TREASURY
INTERNATIONAL CONFERENCE ON FINANCIAL EDUCATION**

Taking Financial Literacy To The Next Level: Important Challenges And Promising Solutions

**Washington D.C.
7-8 May 2008**

Day 1

9:00 AM-5:30 PM

Registration 8:30 AM-9:00 AM

9:00 AM

Introductory Remarks

- OECD Deputy Secretary-General, Mr Pier Carlo Padoan

Introduced by Mr. Dan Iannicola, Jr., Deputy Assistant Secretary for Financial Education, **United States**

9:30 AM-11:00 AM

I - National Strategy: Creation and Implementation

Chair: André Laboul, Head of Financial Affairs Division, OECD

- Chris Pond, Director of Financial Capability, FSA, **United Kingdom**

- Dan Iannicola, Jr., Deputy Assistant Secretary for Financial Education, Department of the Treasury, **United States**

- Paul Clitheroe, Chair, Financial Literacy Foundation, **Australia**

- Diana Crossan, Retirement Commissioner, **New Zealand**

Speakers will cover the different types of national strategies that have been created; approaches and objectives; challenges and opportunities; roles of government, private sector and non-profit organizations; and evaluation of impact.

Coffee Break 11:00-11:15 AM

11:15 PM-12:30 PM

II - Tools I: Diverse Approaches

Chair: Ursula Menke, Commissioner, Financial Consumer Agency of Canada, Canada

- Jeanne Hogarth, Manager for the Consumer Education and Research Section, Division of Consumer and Community Affairs, Federal Reserve Board, **United States**

- Annamaria Lusardi, Professor, Dartmouth College/Harvard Business School, **United States**

- Alison O'Connell, **OECD** Consultant on Methodology to Evaluate Financial Education Programs, **New Zealand**

Speakers will address practical techniques to reach people of all ages through a variety of means to support and ensure the efficiency of financial education programs. Each tool presented represents a viable policy option for providers of financial education independent of the issue addressed or whether the provider is from the private or public sector.

Lunch 12:30 PM-2:00 PM

1:30 PM - Guest Speaker

Martin J. Gruenberg, Vice Chairman, Federal Deposit Insurance Corporation and Chair of the Executive Council and President of the International Association of Deposit Insurers

2:00 PM-3:30 PM

III - Retirement Savings: New Realities for Consumers

*Chair: Mr. D. Swarup, Chairman, Pension Fund Regulatory and Development Authority, **India***

- Nicolas Blancher, Deputy Division Chief, Monetary and Capital Markets Department, **IMF**

- Ambrogio Rinaldi, Chair of the Working Party on Private Pensions, **OECD**, and Director COVIP, Pension Funds Supervision Commission, **Italy**

- Annika Sunden, Research Associate at the Center for Retirement Research at Boston College, Chief of the Research Unit at the Swedish Social Insurance Agency and **OECD** Consultant

- Jeffrey Dominitz, Senior Economist, RAND, **United States**

Speakers will cover demographic changes; shrinking welfare budgets; shift from defined benefit to defined contribution plans; challenges in developing long term care markets; strategies for increasing participant enrollment; strategies to promote pension plans among citizens; roles of government & private sector (including employers); and behavioral research.

Coffee Break 3:30 PM-4:00PM

4:00 PM-5:30 PM

IV- Risk Awareness: Enhancing Education and Protection of Households on Large-Scale Risks

*Chair: Manuel Aguilera-Verdusco, Chair of the Comisión Nacional de Seguros y Fianzas CNSF, **Mexico**, Chair of the OECD Insurance and Private Pensions Committee*

- Dr. Rebekah Green, Risk Red, **OECD** Consultant

- Dr. Erwann Michel-Kerjan, Managing Director, Wharton School Risk Center, University of Pennsylvania, Chairman of the OECD High-Level Advisory Board on the Financial Management of Large-Scale Catastrophes, **United States**

- Katsuo Matshushita, General Manager of the International Department, General Insurance Association of Japan, **Japan**

- Semih Yücemem, Professor and Director, Earthquake Engineering Research Centre, Member of Management Board, Turkish Catastrophe Insurance Pool, **Turkey**

Speakers will cover transfer of a large variety of risks to individuals; particular issues related to large-scale risks; challenges of and strategies for promoting risk awareness; roles of compulsory insurance and new insurance tools (micro insurance); roles of government, private sector and non-profit organizations; and evaluation of impact.

End of Day 1

6:00 PM

Cocktail Reception hosted by the OECD

7:00 PM - Guest Speaker

Ambassador Michael Ian King of Barbados, Chair of the Permanent Council of the Organization of American States

Anna Escobedo Cabral, United States Treasurer

Introduced by Carolyn Ervin, Director, Directorate for Financial and Enterprise Affairs, OECD

Day 2

9:30 AM - 6:15 PM

9:30 AM - *Guest Speaker*

James Flaherty, Minister of Finance, Canada

10:00AM-11:45 AM

V- Credit: Challenges and Opportunities

Chair: Thomas Wieser, Director General for Economic Policy and Financial Markets, Federal Ministry of Finance, Austria, Chair of the OECD Committee on Financial Markets

- Bruno Levesque, Principal Administrator Financial Education, **OECD**
- Mary O’Dea, Consumer Director, Irish Financial Regulator, **Ireland**
- Faith Schwartz, Executive Director, HOPE Now Alliance, **United States**
- Jane Nash, Head of Government and Regulatory Affairs ANZ, **Australia**
- Pete Crear, Chief Executive Officer, **World Council of Credit Unions**

Speakers will cover the role of financial education in the credit granting process. More specifically, speakers will identify some best practices in this area and discuss the role of specific stakeholders, such as the governments, financial institutions, counseling and credit reporting agencies. Finally, this session will address the recent subprime credit crisis in respect of its financial education component.

Coffee Break 11:45 AM-12:00 Noon

12:00 AM-1:15 PM

VI - Tools II

Chair: Dan Iannicola, Jr., Deputy Assistant Secretary for Financial Education, United States

- Daniel Kosicki, Policy Officer, DG Internal Market and Services, **European Commission**
- Marcin Polak, Education Now Foundation, **Poland**
- Kathleen M. Floyd, Executive Director, The Stock Market Game, **United States**

Speakers will address practical techniques to reach people of all ages through electronic and innovative means. Each tool presented will represent a viable policy option for providers of financial education independent of the issue addressed or whether the provider is from the private or public sector.

Lunch 1:15 PM-2:15 PM

2:15 PM-4:00 PM

VII - Youth Financial Literacy: Development, Delivery and Execution of Programs

Chair : Erik Pointillart, Chair of the Institut pour l'Éducation Financière and General Director Caisse d'Épargne, France

- Shaun Mundy, Former Head of Financial Capability Department, Financial Services Authority, and OECD Consultant, **United Kingdom**
- Koid Swee Lian, Consumer and Market Conduct, Director, Bank Negara, **Malaysia**
- Dara Duguay, Director of Citi's Office of Financial Education, Citigroup, **United States**
- Roy Thomasson, Chief Executive Officer, Young American Business Trust, **Organization of American States**
- Klaus Wertenbroch, Professor of Marketing, **INSEAD**

Speakers will cover youth financial literacy levels; ways to ensure higher level of literacy and capability; role of school programs and challenges to getting financial education into the school system; tactics to get around these challenges; role of other tools such as teaching techniques - experiential learning- and strategies for building effective motivation and student engagement; the roles of government, private sector, partnerships, and non-profit organizations; and research.

Coffee Break 4:00 PM-4:15 PM 4:15 PM-5:45 PM

VIII - Underserved Groups: Greater Financial Access through Education

Chair: Christopher F. Egan, U.S. Ambassador to the OECD

- John Bryant, Founder, Chairman and CEO of Operation Hope, Vice-Chairman, U.S. President's Advisory Council on Financial Literacy, **United States**
- Olivia Davids, Head of Consumer Education, Financial Services Board, **South Africa**
- Guillermo Zamarripa, Head of the Banking, Securities and Savings Unit of the Ministry of Finance and Public Credit of Mexico, **Mexico**
- Susan L. Rutledge, Regional Coordinator on Corporate Governance and Financial Consumer Protection, **World Bank** Programs

Speakers will cover challenges in enhancing financial capability of most vulnerable groups and unbanked; innovating products; tying financial education to asset building programs; effective delivery strategies; role of government, the private sector, non-profit organizations, and local networks; and evaluation and results.

5:45 PM-6:15 PM

IX - Wrap Up Session

- Secretary of the United States Treasury, Henry M. Paulson, Jr

Introduced by Carolyn Ervin, Director for Financial and Enterprise Affairs, **OECD**

Background Material

Publications

US Treasury Department (2006), *Taking Ownership of the Future: The National Strategy for Financial Literacy*

OECD (2005), *Improving Financial Literacy: Analysis of Issues and Policies*

OECD (2008), *Financial Education and Awareness on Insurance and Private Pensions*

Instruments

OECD Recommendation on Principles and Good Practices for Financial Education and Awareness, 2005

OECD Recommendation on Good Practices for Financial Education relating to Private Pensions, 2008

OECD Recommendation on Good Practices for Enhanced Risk Awareness and Education on Insurance Issues, 2008

Material

OECD consultant reports, (2008)

OECD International Gateway for Financial Education (www.financial-education.org)