"Our objective is realistic," says one expert on financial literacy, but can initiatives really change behaviors?

By Rhea Wessel

Financial literacy—or the lack of it—among the general population affects every investment adviser as well as every citizen. Discussions about the problem can cause emotions to surge, given the wide variety of policy and nonpolicy prescriptions that are proposed to tackle it.

Though people may spar about how to reach the goal of a financially capable society, few argue that individuals would not benefit from a deeper understanding of money matters, such as mortgage contracts, inflation, and risk diversification.

Some authorities, including the Organisation for Economic Co-operation and Development (OECD), believe that a poor understanding of financial concepts and poor financial decision making played a significant role in the U.S. subprime mortgage crisis. From this point of view, financial illiteracy is an urgent matter that affects the stability of the entire financial system.

A perfect storm is brewing, the reasoning goes. Individuals must increasingly take charge of their long-term financial security because of the shift from defined-benefit plans to defined-contribution programs and the growing challenge of unfunded government retirement schemes. Financial products are ever more complex and opaque, and people have unprecedented access to credit, which provides an incentive to consume rather than save.

Efforts are being made to put financial illiteracy on the international policy agenda, along with other slow-moving phenomena that can have drastic consequences over the long term but are easy to ignore in the short term. Dealing with financial illiteracy goes beyond official responses. Some people in the financial industry believe they have a responsibility to help improve financial education and outreach programs as part of efforts to rebuild the trust lost during the financial crisis.

Changing behavior, however, may prove even harder than providing education. Research shows that even a high level of financial literacy is no guarantee of a positive economic outcome or a populace that can take care of itself financially. It's a bit like going on a diet. You may know all about diets and how to diet successfully, but knowing about diets and successfully going on a diet are two very different things.

Still, raising education levels is a first step to affecting behavior, according to Annamaria Lusardi, professor of accountancy at the George Washington University School of Business and academic director of the university's Global Center for Financial Literacy. "We have found a strong link between financial literacy and the capacity to plan for retirement, to have a cushion of wealth, and to make decisions that are now more commonplace than before," she says. "Financial knowledge is very, very strongly related to financial behavior."

SCOPE AND SCALE

Financial literacy must first be defined if it is to be measured. In an inaugural 1997 study, Jump$tart, a Washington, DC–based national coalition of organizations working to improve financial literacy among the young (from prekindergarten through college age), defined financial literacy as "the ability to use knowledge and skills to manage one's financial resources effectively for lifetime financial security." Today, however, the term "financial literacy" has been expanded to include knowledge of financial products and concepts, as well as the basic numeracy and mathematics needed to apply concepts to financial activities and financial planning.

No matter where the line is drawn between financial literacy and illiteracy, it is important to acknowledge that a lack of understanding about basic concepts is not limited to low-income or undereducated consumers. Among U.S.-based investors, the 2009 National Financial Capability Study showed that a majority of people with household income of more than $150,000 failed to answer five basic questions about financial concepts correctly, according to analysis published in a National Bureau of Economic

Research working paper released in September 2012 ("Financial Literacy, Financial Education and Economic Outcomes" by Justine C. Hastings, Brigitte C. Madrian, and William L. Skimmyhorn). Advisers to wealthy and educated people know it all too well: Having a high net worth does not necessarily translate into having a high level of understanding about financial concepts.

Nor is the problem limited to specific countries. An international study co-authored by Lusardi and Olivia Mitchell concluded that financial literacy is very low around the world, regardless of the level of financial market development in a country. The survey also showed that women tend to know less than men about financial matters and that older people tend to have lower levels of financial knowledge than the younger generations, suggesting these groups may be vulnerable.

For Robert Holzmann, director of the RH Institute for Economic Policy Analyses in Vienna and an expert on international financial literacy, the important point is not quantitative measures of knowledge but the baseline behavior individuals actually need to make sound financial decisions on their own—because behavior

Financial Literacy Initiatives from CFA Institute Societies

The Bay Area Financial Education Foundation (BAFEF), established as a public nonprofit by members of the CFA Society San Francisco, supports proven financial literacy programs in the areas of finance, investment, and entrepreneurship. Support is given through volunteers, event participation, and funding, according to Ted Jablonski, president of the foundation and a wealth manager in the Bay Area.

Jablonski explained that the foundation's goal is to help people sort through the thousands of education programs available and identify the programs that have a strong track record for making the intended impact.

"The foundation board looked for scalable, proven programs in our area of interest," says Jablonski. "Then we went through due diligence to select a list of partners."

BAFEF selected five public and private partners for its financial literacy program, including the *Wall Street Journal Classroom Edition*, which provides students with access to daily financial news and related study materials, and the SIFMA Foundation's "Stock Market Game," in which teams of students invest a hypothetical portfolio of $100,000.

"When we started our program in 2007, it was a 'feel good' moment and we wanted to give something back," says Jablonski. "But after the crisis, public confidence in large institutions was really low. Now, I think it's critical for our profession to engage in financial education and to find a place where we can offer support to rebuild trust."

PITTSBURGH

CFA Society Pittsburgh began a financial literacy project in 2011 on the initiative of Christopher Pretsch, CFA, a managing director of Staley Capital Advisers and a former board member of the society.

Pretsch, who still runs the financial literacy committee, had noticed frequently that regardless of age or education level, many of his clients lacked basic financial savvy. In addition, he saw how easy it was for companies to mis-sell products or sell bad financial products.

"One of the reasons companies get away with this is because people don't know how to differentiate," he says. "They don't know how to tell a good financial product from a bad financial product. I felt there was a real need for people to learn about this stuff. I felt like CFA Institute and [CFA Society Pittsburgh], because we are unbiased and aren't trying to sell anything, would be a good vehicle for us to get out there in front of the public and educate people."

The committee, which now has 10 people involved, gives lectures on basic financial principles to youngsters, often at schools, and has a backlog of requests to do the same for adults in the Pittsburgh area.

In the opinion of Pretsch, one of the problems in the investing world today is that there is too much information. "You've got all these websites, you've got CNBC all day long," he says. "I try to remind people that CNBC's business is not to teach you about the market or inform you. Their business is to sell commercials. All the stuff in between the commercials is just filler to keep you engaged. They have 14 hours to fill. They have to keep talking about this stuff. It makes people want to trade more than they should, to buy stocks more than they should. It pulls people in too many different directions."

Pretsch sees over and over again how individual investors will do the exact opposite of what they should in times of market panic. "If we can educate people about hysteria and how to resist it," he says, "it makes our jobs as advisers easier because we don't have to deal with clients who are trying to sell stocks when they should be buying and the other way around."

In the end, it comes down to this for Pretsch: "A better-educated investor makes a better client."

determines financial outcomes, regardless of socioeconomic status or knowledge level.

"What's interesting is the outcome of financial education," says Holzmann, who also advises a Russia-supported and World Bank–led research program on financial literacy and education. "That makes the important question, How should people behave to be considered financially capable?"

Researchers have identified five traits that make a person financially "capable": the ability to (1) control or record daily spending, (2) budget or live within one's means, (3) plan or prepare and save for future knowns and unknowns, (4) choose or select between alternative financial products, and (5) get help or know where to go for help. Empirical, international studies are ongoing to compare these traits among people of different demographics, such as high income, low income, country of residence, and so forth.

The impact of financial advisers is also part of the equation. "What comes out from the literature is that good independent financial advice and asking people good questions about their plans and money can be more valuable than generic financial education," says Holzmann.

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But even with good advisory services, individual investors still must be able to understand the advice in order to benefit. "People need the skills to understand what a financial adviser will tell them," says Flore-Anne Messy, senior expert on financial education and executive secretary of INFE at the OECD in Paris. "There is a lot of responsibility on the financial advisers to understand the context and provide people with impartial information. A financial adviser can contribute in a small way to financial education by helping people to make good decisions and have a better understanding of what is at stake."

FINANCIAL EDUCATION INITIATIVES

A plethora of institutions have undertaken the challenge of changing financial behaviors. Government agencies, companies, nongovernmental organizations (NGOs), and concerned individuals are using a variety of ways—some more creative than others—to make an impact.

The OECD's International Network on Financial Education (INFE) provides a policy forum for exchanging views and experiences on financial education. The network, which works with 106 countries and 230 public institutions, has compiled an extensive repository of studies on the subject and holds conferences around the world as part of efforts to develop indicators and define best practices for financial education.

Messy works with partners to develop methodologies for measuring the financial literacy of a population, including attitudes and behaviors. In cases where the goal is to change behavior (not simply to inform or raise awareness), the network recommends starting early with education initiatives in schools and combining those efforts with regulation and advice.

The program's goal is to help people develop savvy, informed habits for their personal finances. "Our objective is realistic," says Messy. "We know that not everyone can become, will become, or should become a sophisticated investor."

EDUTAINMENT

Some efforts to promote financial literacy have experimented with "edutainment," or behavior-oriented content that has a "fun factor." One notable example is a soap opera in South Africa. The project, conducted by South Africa's National Debt Mediation Association (NDMA) and supported with design and evaluation by the World Bank, developed financial-capability themes for a soap opera called *Scandal!* The storylines included a woman overspending and spiraling into debt. After she confesses her situation to a friend, comes clean with her husband, and gets advice from a debt counselor, the character begins to take control of her spending.

Multiple plot elements, introduced over six weeks, touched on getting into debt and breaking the debt cycle. The effect on knowledge and behavior was measured by, for example, monitoring calls to the debt counseling hotline. “The results are encouraging since they show significant improvement in content-specific financial knowledge,” says Holzmann, who served as a senior adviser on the project.

Another creative approach comes from activist Johnny Deas, founder of the Great Ideas Edutainment Foundation. Through a program called “Financial Literacy Music,” he uses his MBA background and training as a financial planner to rap about a variety of financial concepts, from understanding defined-contribution and defined-benefit plans to dollar-cost averaging.

Many experts, including Messy and Madrian, see games as a particularly effective tool for teaching money principles because games allow one to fail within a protected environment. The experience of failure then provides an incentive to improve. A report by the not-for-profit Doorway to Dreams Fund (D2D) describes financial entertainment as a paradigm shift away from traditional financial education, which is typically lecture based and often is perceived as boring. Instead, financial entertainment tries to make financial education engaging, fun, and interactive, and it links education to action by embedding offers and opportunities for real-world choices directly into the games.

THE IDEA IS TO LINK SAVING WITH SUSPENSE, FUN, AND POSSIBILITY INSTEAD OF SELF-DENIAL AND DEFERRED GRATIFICATION.

The SIFMA Foundation’s “Stock Market Game,” for example, has received particularly high marks for its ability to engage players (usually young people) in a real-life simulation of stock investing. It allows participants to see a direct connection between their choices and their account balances as teams invest a hypothetical portfolio of $100,000. The game also gets competitive instincts flowing because teams compete and results are easily comparable.

Boston-based D2D calls itself an “idea lab” for developing products, services, and public policies that promote financial security for low- and moderate-income people. Funded by the Ford Foundation and the W.K. Kellogg Foundation, among others, and chaired by Peter Tufano, dean of the Saïd Business School at the University of Oxford, the organization focuses on behavior-affecting programs to promote saving and learning. It has led efforts to introduce “prize-linked savings” to the U.S. market—products that reward saving with chances to win cash prizes. “The idea is to link saving with suspense, fun, and possibility instead of self-denial and deferred gratification,” says Timothy Flacke, executive director of D2D.

Financial games are a big part of what D2D does. It has developed a number of games to teach financial principles that are designed for the mass market and are available for free on its website. At the start of its work in financial games, D2D realized that the problem was not a lack of available information. “We concluded that the problem is not on the supply side; it’s on the demand side,” says Flacke.

D2D set out to increase demand for financial learning through games that have the potential to teach and attract a large audience. “The number of people who are sufficiently motivated to seek out financial education is not very large; the number of people who are willing to try out something because it looks fun is much larger,” says Flacke.

D2D has pulled together a library of so-called casual games based on themes from popular culture that have wide appeal and are easy to play. One advantage of games is that learning is not passive. Instead, players practice deciding how much to charge to the credit card or debit card or how much to defer for retirement. Games also can help people overcome trepidation associated with the topic of saving and investing.

“If it’s a good game, you get engrossed in the puzzle solving. The anxiety you feel about the topic ebbs away, and there’s a window when you can help people learn both information and skills and increase self-confidence because they are solving the puzzle,” says Flacke. In addition, the games can include a nudge to actually take action, something D2D is focused on right now.

Recently, D2D worked with Staples to help the office-supply company increase the take-up of its retirement plan among employees. D2D embedded into the "Bite Club"—a vampire-themed financial education game—a link that allows Staples employees to go directly to the website of the Staples retirement vendor, and it customized the game for the Staples plan. "Staples did some really creative marketing that looked nothing like a traditional 401(k) enrollment kit," says Flacke.

Flacke sees financial education games as an ideal tool, given the small cost of making electronic ones available online. But he is careful to distinguish between financial education games and online tools, such as retirement or insurance calculators. Often, tools are presented as games, but they lack the game-play elements that make games fun.

EMPLOYER PROGRAMS

Staples' use of a financial game to promote employee participation in the company's retirement plan is part of a larger trend. Increasingly, employers are offering more financial training, conducting campaigns, holding learning competitions, and making online study materials available, among other methods. According to a study titled "Personal Finance and the Rush to Competence: Financial Literacy Education in the U.S.," commissioned by the now-defunct Fannie Mae Foundation, companies have started education programs to increase participation in (and contribution to) retirement plans, to comply with related regulations, and to avoid potential liability for investment losses. Examples in the U.S. include the forestry products company Weyerhaeuser, the logistics provider UPS, and Staples.

The U.S. military also offers personal finance courses. A study of the impact of a mandatory course the U.S. Army provided for enlisted soldiers found that attending the class doubled participation in and contributions to a retirement savings plan. The army course is one of the most significant cases of a program improving financial outcomes that has been documented in the literature, according to one of the study's co-authors, Brigitte Madrian, Aetna Professor of Public Policy and Corporate Management at the Harvard Kennedy School of Government. "The good news is if you structure a financial literacy program well, you can have impact," says Madrian.

CFA Institute and Investor Education

The investor education effort at CFA Institute shares information via various channels and media, including its blog *Enterprising Investor* (blogs.cfainstitute.org/investor). "I am passionate about financial education because when investors are well informed, they require transparency and make better investment decisions," says Robert Stammers, CFA, director of investor education. "This leads us to a more equitable and efficient market and a chance for investors to receive a fair return."

For more effort about investor education initiatives and offerings, contact robert.stammers@cfainstitute.org.

FOR THE ULTIMATE BENEFIT OF SOCIETY

Some CFA Institute member societies have begun their own initiatives in their local communities, such as the outreach programs by CFA Society Pittsburgh and the Bay Area Financial Education Foundation (BAFEF), which was started by the CFA Society of San Francisco (see sidebar on page 32).

CFA Institute also reaches out to those who aren't in the financial services industry through the investor education effort directed by Robert Stammers, CFA. In his view, investor education can improve markets. Well-informed investors will demand transparency and make markets more equitable and efficient.

But achieving large-scale transformation depends on small changes in behavior for individual people. "Financial education doesn't mean making people become little Warren Buffetts or little financial wizards," says Lusardi. "It's about equipping people to be in charge of their own financial lives."

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