Chapter 1

The importance of financial education for youth

This chapter presents the global trends underpinning the rising importance of financial literacy, from improved financial inclusion and innovation to the transfer of (financial) risks to individuals. It then highlights the benefits of financial literacy for individuals, and its positive spillovers on the financial and economic system. The chapter also points to the rationale for a focus on youth and in particular on schools. It notably draws on OECD/INFE surveys, desk research and work developed for the preparation of the OECD PISA Financial Literacy Framework.

The importance of financial literacy for individuals

In recent years, advanced and emerging economies have become increasingly concerned about the level of financial literacy of their citizens. This has stemmed in particular from improved levels of financial inclusion and rising middle classes in emerging economies, as well as wide-ranging developments in the financial marketplace, shrinking public and private support systems, and shifting demographic profiles including the ageing of the population. Concern was also heightened by the financial crisis, with the recognition that lack of financial literacy was one of the factors contributing to bad financial decisions and that these decisions could, in turn, have tremendous negative spill-overs (INFE/OECD, 2009; OECD, 2009a; see also Gerardi, Goette, and Meier, 2010 for empirical analysis of financial literacy and mortgage delinquency).

As a result, financial literacy is now globally acknowledged as an important element of economic and financial stability and development. In 2012 and 2013, G20 leaders notably endorsed the OECD/INFE High-level Principles on National Strategies for Financial Education, recognised the importance of financial education for youth and called for the identification of potential barriers faced by youth in their access to financial products and financial education, and welcomed Progress Reports on Youth and Finance developed by the OECD on financial education and by the World Bank on financial inclusion (G20 Leaders communiqué, 2012; G20 Leaders communiqué, 2013). This attention is justified by a series of tangible trends (OECD, 2005a), which make financial literacy a key life skill for individuals. This includes Asia-Pacific Economic Cooperation Ministers of Finance who recognised "*the importance of financial literacy as a critical life skill in the 21st century that can contribute to individual and families' wellbeing as well as to financial stability in our economies.*" (APEC Policy Statement, August 2012)

The following sections present these trends, highlight the benefits of financial education and the importance of its introduction in schools.

Greater supply of a wide range of financial products and services

In most countries, growing numbers of consumers have now access to a wide range of financial products and services, from a variety of providers and delivered through various channels. Improved levels of financial inclusion in emerging economies, developments in technology and deregulation have resulted in widening access to retail financial products, from current accounts to remittances products, consumer revolving credit and equity portfolios. The products available are also becoming more complex, and individuals are required to make comparisons across a number of factors such as the fees charged, interest rates paid or received, length of contract and exposure to risk. They must also identify appropriate providers and delivery channels from the vast array of possibilities, including community groups, traditional financial institutions, online banks and mobile phone companies.

Increased demand for financial products and services

Economic and technological developments have also brought greater global connectedness and massive changes in communications and financial transactions, as well as in social interactions and consumer behaviour. Such changes have made it more important that individuals be able to interact with financial providers. In particular, consumers often need access to financial services (including banks and other providers

such as Post Offices) in order to make and receive electronic payments like income, remittances and online transactions, as well as to conduct face-to-face transactions in societies where cash and cheques are no longer favoured. Those who cannot access such services often pay more for cash transactions, using informal financial services such as moneylenders or cheque cashers (Kempson, Collard, and Moore, 2005).

Risk shift

In parallel, there has been a widespread transfer of risk from both governments and employers to individuals. Many governments are reducing or have reduced state-supported pensions, and some are reducing healthcare benefits. Defined contribution pension plans are quickly replacing defined benefit pension plans, shifting onto workers the responsibility to save for their own financial security after retirement. Traditional pay-as-you-go (PAYG) pension schemes are supplemented by new schemes in which the individual is subject to both revenue and investment risks. Most surveys show that a majority of workers are unaware of the risks they now have to face, and do not have sufficient knowledge and skill to manage such risks adequately, even if they are aware of them (OECD, 2008). Furthermore, the array of demographic and financial risks that people have to face is increasing: and notably the risks associated with longevity and health, credit, financial markets volatility, as well as unemployment.

Increased individual responsibility

The number of financial decisions that individuals have to make is increasing as a consequence of changes in the market and the economy. For instance, longer life expectancy means individuals need to ensure that they accumulate savings to cover much longer periods of retirement. People also need to assume more responsibility for funding personal or family healthcare needs. Moreover, increasing education costs make it important for parents to plan and invest adequately for their children’s education. Even when individuals use the services of financial intermediaries and advisors, they need to understand what is being offered or advised. The individual is responsible for the financial product he or she decides to purchase, and the individual will face all the consequences of the choice. In addition, the current economic and financial environment can make it even more difficult for individuals to find and remain in a stable and salaried occupation.

All of these trends have transferred the responsibility of major financial decisions to individuals. At the same time, they have both enlarged the options for the majority of the population (including new financial consumers) and increased the level of complexity they face. Against this backdrop, individuals are expected to be sufficiently financially literate and entrepreneurial to take the necessary steps to protect themselves and their relatives and ensure their financial well-being including by coping with unexpected events and/or developing their own source of income.

Benefits of financial literacy

Existing empirical evidence shows that adults in both developed and emerging economies who have been exposed to financial education are subsequently more likely than others to save and plan for retirement (Bernheim, Garrett, and Maki, 2001; Cole, Sampson, and Zia, 2010; Lusardi, 2009). This evidence suggests a link between financial education and outcomes; it indicates that improved levels of financial literacy can lead to positive behavioural change.

Other research, stemming largely from developed countries, and the United States in particular, indicates a number of potential benefits of being financially literate. There is mounting evidence that those with higher financial literacy are better able to manage their money, participate in the stock market and perform better on their portfolio choice, and that they are more likely to choose mutual funds with lower fees (Hastings and Tejeda-Ashton, 2008; Hilgert, Hogarth, and Beverly, 2003; Lusardi and Mitchell, 2008; Lusardi and Mitchell, 2011; Stango and Zinman, 2009; van Rooij, Lusardi, and Alessie, 2011; Yoong, 2011). Moreover, those who have greater financial knowledge are more likely to accumulate higher amounts of wealth (Lusardi and Mitchell, 2011).

Higher levels of financial literacy have been found to be related not only to asset building but also to credit and debt management, with more financially literate individuals opting for less costly mortgages and avoiding high interest payments and additional fees (Gerardi, et al., 2010; Lusardi and Tufano, 2009a, 2009b; Moore, 2003).

In addition to the benefits identified for individuals, financial literacy is important to economic and financial stability for a number of reasons. Financially literate consumers can make more informed decisions and demand higher quality services, which will encourage competition and innovation in the market. They are also less likely to react to market conditions in unpredictable ways, less likely to make unfounded complaints and more likely to take appropriate steps to manage the risks transferred to them. All of these factors will lead to a more efficient financial services sector and potentially less costly financial regulatory and supervisory requirements. They can also ultimately help in reducing government aid (and taxation) aimed at assisting those who have taken unwise financial decisions – or no decision at all.

Financial education for youth and in schools

In this context, the focus on financial education for youth and in schools is not new. As mentioned, financial literacy is increasingly considered to be an essential life skill including by regional and global fora such as G20 and APEC (G20, 2012; APEC 2012). In fact, as early as 2005, the OECD Recommendation advised that "financial education should start at school. People should be educated about financial matters as early as possible in their lives" (OECD, 2005b). Two main reasons underpin this recommendation: the importance of focusing on youth, and the efficiency of providing financial education in schools.

Focus on youth

Owing notably to technological advances, younger generations are likely to be more financially included in their adulthood than older generations and to use financial services to perform a wider array of activities throughout their lives. They will also probably have to bear more financial risks in adulthood than their parents. In particular, they are likely to be responsible for the planning of their own retirement savings and investments, and the coverage of their healthcare needs. They may also have to deal with increasingly sophisticated and innovative financial products, services and markets.

In a growing range of countries, youth have access to financial services from a young age. It is not uncommon for them to have accounts with access to online payment facilities or to use mobile phones (with various payment options) even before they become teenagers. Before leaving school, they may also face decisions about such issues as car insurance, savings products and overdrafts. Furthermore, the development of

appropriate financial skills can also boost entrepreneurship and provide youth with additional tools in case they will experience economic hardship.

Given the complexities of new financial systems and their constant evolution, as well as social welfare systems (and particularly pension systems) and demographic trends, current generations are unlikely to be able to learn from past generations. Youth will have to rely on their own financial literacy[1] including not only knowledge, but more importantly sound competencies and new habits and attitudes to make savvy financial decisions and informed use of professional financial advice where they exist. However, surveys conducted nationally and globally show that young adults display lower levels of financial literacy compared to older generations (Atkinson and Messy, 2012 and Kempson, E., V. Perotti P., K. Scott, 2013).

These new and evolving competencies will thus have to be acquired through an ongoing process throughout individuals' lives. To be effective and lead to behavioural changes, this process has to start early in life (OECD, 2005). In fact, research and surveys conducted in various countries including Australia, the United Kingdom and the United States (see Whitebread and Bingham, 2013, for a review of the literature) show that the development and integration of financial habits and attitudes begin very early and probably before children reach seven years old.

It is also important that youth be financially literate before they engage in major financial transactions and contracts. In many countries, at around the age of 15 to 18, young people (and their parents) face one of their most important financial decisions: that is, whether or not to invest in college or higher education. The gap in wages between college and non-college educated workers has widened in many economies. At the same time, the education costs borne by students and their families have increased, often leading to an excessive reliance on credit (Smithers, 2010; Bradley, 2012; Ratcliffe and McKernan, 2013).

Finally, efforts to improve financial literacy in adulthood through the workplace or other settings can be severely limited by a lack of early exposure to financial education. It is therefore important to provide early opportunities to establish the foundations of financial literacy.

Efficiency of providing financial education in schools

When addressing young people's needs for greater financial competencies, the role of schools is paramount.

Research suggests that there is a link between financial literacy and family economic as well as educational background: those who are more financially literate disproportionately come from highly educated and financially sophisticated families (Lusardi, Mitchell, and Curto, 2010; Atkinson and Messy, 2012). In order to provide equality of opportunity, it is important to offer financial education to those who would not otherwise have access to it. Schools are well positioned to advance financial literacy among all demographic groups (including vulnerable groups such as low income and/or migrants families) within a generation, which will help to break the cycle of generational financial illiteracy. Schools also have the potential to reach out to parents, teachers and to disseminate sound financial habits in the wider community.

Moreover, school provides a relevant context to develop high quality teaching and effective learning. Existing curricula, pedagogical tools and school resources can indeed be harnessed to address youth's needs for financial education. Children in the school

context are also a particularly appropriate audience with the necessary time and ability to learn. The country case studies of effective practices presented in the following chapters as well as the results of impact assessments notably conducted in Brazil (Bruhn, M., et al 2013, forthcoming) demonstrate that the introduction of financial education is effective when delivered in an engaging and consistent way (Lührmann et al., 2012).

Recognising both the importance of financial literacy for youth and the unique potential of school programmes, an increasing number of countries started delivering financial education in schools. OECD/INFE ongoing surveys reveal that over 40 countries have introduced some form of financial education in schools. These initiatives are developed at national, regional and local levels and also include pilot exercises. A shorter but constantly evolving list of countries have introduced financial education as a compulsory subject in schools generally through a cross-curricular approach.

Most countries however highlight that the introduction of financial education in schools is challenging for a series of reasons, including limited political willingness, and commitment; overloaded curricula; insufficient expertise and know how; lack of high quality materials; lack of resources and time; as well as the variety of stakeholders involved.

Against this backdrop, the following Chapter (2) sketches out the experience of countries which have overcome these challenges through strategies to secure the support of government and public authorities, and flexible but consistent approaches to the introduction of financial education into schools. It also highlights tools to support the provision of financial education in schools (including the training of teachers and the development of good pedagogic materials); and to ensure the sustainability of the programmes (including earmarking of resources and evaluation of programmes). Chapter 3 then addresses the content of learning frameworks developed for financial education in schools. Finally, the INFE Guidelines for Financial Education in Schools displayed in Annex A provide policy makers and interested stakeholders with high-level international guidance on the introduction of financial education in schools and guidance on the development of adapted learning frameworks.

Note

1. See Definition of financial literacy for 15 year old students, OECD (2013a), "Financial Literacy Framework": Financial literacy is knowledge and understanding of financial concepts and risks, and the skills, motivation and confidence to apply such knowledge and understanding in order to make effective decisions across a range of financial contexts, to improve the financial well-being of individuals and society, and to enable participation in economic life.

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