How financial markets and services can better support economic growth

23 June 2015

On the 13th of July 2016, the European Parliamentary Financial Services Forum welcomed **Vice-President Valdis Dombrovskis**, Commissioner for the Euro and Social Dialogue, to discuss the key issue of the role of financial education, as well as the challenges ahead.

This event was co-chaired by **Burkhard Balz MEP** and **Brian Hayes MEP**.

Burkhard Balz
(Chairing MEP)

In a complex and rapidly evolving finan-cial world, financial education is a key element to ensure that people acquire the financial knowledge they will need to take good and responsible financial decisions all along their life. The event sought to address the role of financial education in consumer empowerment and protection, thus contributing to a more healthy and sustain-able economy. It explored the contribution of the financial industry in this area - from improving the transparency of products and the quality of the information provided to clients, to the creation of financial education programs.

Brian Hayes
(Chairing MEP)

EUROPEAN COMMISSION

Keynote address by Vice-President Valdis Dombrovskis, Commissioner for the Euro and Social Dialogue

Valdis Dombrovskis
(European Commission)

First of all, thank you for inviting me to this forum to discuss the role of financial education in the Internal Market. The invitation is particularly timely, as in three days' time I will take on the responsibility for Finan-cial Stability, Financial Services and the Capital Markets Union. I will take over from my trusted colleague Johnathan Hill, whom I thank very much for his professionalism and commitment over the past two years.

As I said in the ECON committee last week, I see it as the main role and responsibility of the financial sector to:

- finance the real economy;
- support investment; and
- sustain Europe's social market economy.

That's how we can support financing for start-ups and SMEs. That's how we can help people to manage their finances effectively, save for education or retirement, or insure themselves against ill-health.

To do so we need a balanced regulatory system to ensure citizens are offered safe financial products that meet their needs.

And it requires that citizens have the information and skills to make the right choice among those products. It will be part of my new portfolio to ensure that the financial services regulatory framework takes into account the needs and interests of consumers and retail investors and about proposing any necessary measures to make financial services work better for citizens.

So it's a great pleasure to be here and to have the chance to talk about financial education.

Retail Financial Services Green Paper

I want to follow up on the important initiatives which Johnathan Hill and this Commission have already brought forward.

The Green Paper on Retail Financial Services is one of them.

At the moment, less than 3% of consumer financial services are sold across European borders. But now, with the possibilities that digital innovation brings, we have a great opportunity to link up our markets better in Europe. That would mean that consumers can shop for the product that is right for them, businesses can offer services to customers wherever they are, and when Europeans move abroad they can take the products with them that are essential for their financial security with them.

We had a good response from industry to our consultation. We are still working on the responses but some clear themes have emerged.

Firstly, it’s clear that the provision of services across borders is complicated by the need to check customer identity. There are security requirements, which we should not weaken. But as services go digital, we need to build on ways to identify customers safely at a distance, like existing e-ID and e-signature schemes.

The next theme is that innovation in fin tech offers great opportunities. Europe needs to be part of this innovation and we need to make sure it works for consumers. We can learn from each other about what works best, including new approaches to regulation.

We're looking at ways we can make consumers aware of hidden costs so that they can make better choices, and, despite the wide-ranging legislation of recent years, it will be important to understand whether there are any gaps in our laws where suppliers don't treat consumers fairly.

But of course we want businesses to make the most of these opportunities too, to widen choice and competition. So we're learning from the consultation what’s holding them back from supplying services cross-border - often it's a lack of information about consumers in other Member States. One of the most difficult problems that we're going to have to work on is how to give businesses and consumers the assurance that if they offer or buy a service cross-border they'll be able to get redress.

Financial Education

Coming to Financial Education - the topic of today's forum discussion. The financial environment is increasingly complex and there is a frightening array of products on the market. We need to complement our efforts to develop the retail financial services market by finding ways to empower consumers to take the right decisions. The European Commission is paying particular attention to financial education, which we believe can contribute to restoring consumer confidence in financial markets - in particular following the crisis. Consumers need to be in a position to choose the products most suited to their needs to be able to identify any potential risks.

However, education remains a competence of the Member States. The Commission closely follows the development of national schemes for financial education and is providing support and patronage to a number of projects implemented by public or non-profit organisations. I would like to highlight our role through some concrete examples of how we do this:

In the recent Mortgage Credit Directive, the need to provide financial education has been addressed by obliging Member States to promote measures supporting the education of consumers in relation to responsible borrowing and debt management.

Also, in 2014 the Commission completed a 2-year pilot project where a number of non-profit organisations (such as consumer organisations, debt advice agencies) in all Member States were trained to provide financial advice to consumers. In total, approximately 500 advisors were trained.

And, over the past three years, the Commission carried out a broad information campaign in selected Member States – first in Ireland, Malta, Spain and Cyprus and then in Austria and Czech Republic – to inform consumers aged between 18 and 35 years about their rights, when they take out credit, under the Consumer Credit Directive.

With the further development of digitalisation and technological innovation, we are likely to see new opportunities arising to facilitate access to information. I am thinking in particular about comparison tools or websites, or possibly the provision of low-priced on-line advice. We are looking into these opportunities in the context of the Capital Markets Union and the Green Paper on Retail Financial Services. We will give further consideration to how potential initiatives, such as supporting the development of comparison tools, facilitating the exit from products or monitoring disclosure requirements in a digital environment, might contribute to enhancing consumer empowerment and trust in retail financial services.

Nevertheless financial education should not be perceived as a substitute for solid legal protections and responsible behaviour of financial services providers. On the contrary, it needs to be seen as a complement to EU legislation – such as the rules that regulate the requirements on transparency and disclosure of information for consumers in different sectors of financial services, and such as other conduct of business rules to protect consumers against unfair business practices.

To conclude, we don't at the moment have a fully efficient single market for consumer financial services. There are many excellent products in Europe's individual domestic markets. But only a small minority of consumer financial products are sold across borders. Fees vary drastically from one country to the next, and so does the quality of services. The right information often isn't available to consumers who want to shop across borders, and they do not feel sufficiently empowered to do so. But today, in an era of digitalisation, we have an opportunity to think again about this whole area and overcome some of the traditional barriers imposed by bricks and mortar.

The responses to our consultations are clear. Consumers want to have the option to buy products across borders. They want to know what products are available beyond their domestic market. And they want to be able to buy products they understand, from companies that are upfront about what they're selling and what they're charging. These are simple, clear demands to which I intend to respond once we have completed our analysis and decided where action is needed.

ASSET MANAGEMENT

Report from Andrea Beltratti, Chairman of Eurizon Capital and member of the Board of Directors of the European Fund and Asset Management Association (EFAMA)

Andrea Beltratti
(Eurizon Capital)

Financial education can be improved at two different levels, through organization of events in schools and outside of schools. Schools are a great opportunities to talk about financial education because it is easy to find a large number of students there. The problem is, young students are not today's decision-makers. They should not be neglected because by helping them better understand financial education we can achieve important results for the long run.

However we should also be concerned with the short run and with improving knowledge of today's savers and investors. Therefore the second level that should be regarded as crucial is the involvement of adults. It is much harder to do that but there are several ways to try. One way is based on the relevance of schools and students. An excellent way to motivate adults is through students: students going home and discussing with their parents and relatives what they have learnt in class is the best way to create a family discussion and increase the attention of adults. Follow-up activities can then be organized in class involving both students and parents. Another way to move forward is by organizing events in firms, for example discussing private pensions. However, these possibilities still leave a large number of people not exposed to financial education, and we need to think hard in trying to connect with them.

In my opinion, financial education is a perfect example of a partnership between the public sector and the private sector. The two sectors are fully complementary. The private financial sector has the knowledge that is necessary to set up good financial education programs. The public sector may contribute to that, and also oversight the activities and the material produced by the private sector. In such a way, we can reduce skepticism about the role of the private sector, that according to some commentators regard financial education just like another marketing tool that is used in order to promote own products and services. If the learning materials produced by the private sector are monitored by the public sector, then skepticism can be reduced. Italy is in my opinion a good example of active involvement of the private sector.

The Italian banking Association has set up a foundation devoted to financial education, and over time the foundation has developed teaching tools that have been used in many schools around Italy. Bank specialists participate in meetings in school for short courses of less than 10 hours. Teachers are involved with students, and the level of satisfaction has been high. Unfortunately, Italy is lagging in terms of approving a general national strategy, that is instead present in other European countries.

A national strategy is of fundamental importance to allow for a better coordination of public and private operations, and to build up a stock of training material that can be approved by the public sector and used by everybody in schools and other events. The OECD has recently shown that there is no unique and best corporate governance model to put together the private and the public sectors in a national strategy, so hopefully the Italian specificities will find some common ground in the near future.

Finally, I would like to stress the role of technology. The use of the Internet has opened a wealth of opportunities in terms of finding information, even though perhaps the availability of too much information is confusing people. One could wonder for example why the Internet is increasingly popular but the level of financial education does not seem to rise in the last few years. Perhaps digitalization by itself is not sufficient. Perhaps it is important to mix the Internet with human intervention and with the organization of events, as I have mentioned initially. Plus, in several countries, among which Italy, the Internet has a lower penetration. And in general, there are some segments of the population that are not proficient at using computers, for example mature people.

We cannot then hope that technology by itself will solve the problem of financial education. It is another tool, a very important one, that we need to exploit, ideally in the context of the cooperation between the public sector and the private sector and within the framework of a national strategy. Technology opens the way for a more creative use of financial education. Rather than boring classes, it is nowadays possible to spread financial education in a fun way, for example through educational video-games. These games are very costly to produce, and this is one more reason for a careful use of the few available resources.

BANKING

Report from Wim Mijs, Chief Executive Officer of the European Banking Federation (EBF)

Wim Mijs
(EBF)

Two out of three adult Europeans do not know how to properly calculate interest on a loan. More than 4 out of 5 Europeans buy financial products without shopping around and without asking for advice. And among 15-year olds in most European countries, financial literacy scores are significantly below those of youngsters in China and Australia.

Research published through the OECD in recent years makes it clear that we in Europe face a brutal need to improve financial education. Looking ahead, the challenge becomes even more daunting. Digital trends make the concept of money increasingly virtual, much less tangible, especially for young people. Spending money thus becomes even more complex, although there are some examples where managing a budget becomes easier thanks to digital tools that illustrate the consequences of certain choices.

Financial choices that our younger generations need to make are far more challenging that those faced by past generations. What's more, they will live longer, making it even harder for pension systems to deliver on their ambitions. If they want to secure a sound financial future, financial planning is required at a much earlier stage in their lives.

It is clear that financial literacy has become an essential life skill for the 21st century, crucial to living and thriving in the modern economy. Financial education can help boost these literacy levels. In the end it is the same as with sex education. If you do not do it properly then accidents will happen.

The EBF - together with the national banking associations of Europe - established the European Money Week (EMW) in 2014. The EMW aims to raise public awareness on financial literacy and to improve financial education for students from elementary and secondary schools. The week consists of a series of events in the participating countries and at a European level. Ultimately, the objective is to improve the level of financial education in Europe.

INSURANCE

Report from Paolo Marini, Global Head Customer Management CLP of Zurich Insurance Company

Paolo Marini
(Zurich Insurance Company)

Financial knowledge is essential for individuals to make informed decisions with long-term consequences for their well-being, however good planning doesn't come naturally: scientific evidence exists of a bias towards the short-term.

The risk is that broader societal issues result from the aggregation of poor individual decisions.

The savings gap faced by aging societies is in part the consequence of less than optimal decision-making against a backdrop of strained public resources. Protection gaps are now looming as an additional societal issue.

Zurich is particularly concerned about the deficits between what a household can receive from all public or private source and their actual need, in the event of the main breadwinner's disability or premature death.

We define these as "Income Protection Gaps" and they can have devastating consequences which should be addressed by individuals, families, employers as well as governments.

People who are able to plan ahead and manage their finances are more likely to be better prepared for ill-health, the loss of a job, retirement or the need for long term care.

Financial education is therefore a critical component of consumer protection against more dangers than just abusive industry practices.

For the general population, the focus of education should be on basic skills, such as numeracy, and fundamental products that students will need when they leave education, such as bank accounts or home insurance.

However, financial literacy alone is not enough. When it comes to insurance, it is extremely important that people understand the relevance of various products to their lives.

Reaching end users is crucial because products like pensions and income protection only gain real relevance in adult life rather than youth. In addition, the ability to make sound decisions decreases with age while our self-confidence increases at the same time thus multiplying the chances of ill-judgement.

The importance of relevance - as opposed to pure literacy - is confirmed by a recent survey we undertook with the Smith School at the University of Oxford. Over 11,000 people in several countries including Germany, UK, Switzerland, Spain and Italy were questioned on factors such as awareness, risk perception, trust, willingness to buy coverage and the impact of different actions by policy makers and employers.

One of the most interesting findings is that personal experience of critical situations, whether first- or second-hand, is a fundamental driver of the demand for insurance.

Conversely, when the poll tested for financial literacy and education levels neither were clearly correlated to insurance coverage.

Zurich believes that the financial services industry, together with employers and the public sector, has an important role to play in developing financial competencies. We indeed strive to help customers and communities make good financial decisions by adopting very concrete and pragmatic approaches:

- partnering in thought leadership initiatives with reputable organizations such as the World Economic Forum, the University of Oxford or the Atlantic Council and making knowledge freely available via different channels (the press, social media, our own website...);
- engaging with corporate customers to benefit their staff as in a recent initiative with Nestlé about the implications, financial or otherwise, of road safety, particularly in emerging markets.

Today, digitalisation is a transformational opportunity for the insurance industry and has the potential to greatly expand consumers' knowledge of financial services and the relevance of these to their lives. It allows to engage with customers at key moments (the purchase of a home, the setting up of a family, the birth of a child...) by using tailored material that is relevant, interactive, flexible, mobile, game-like and user-friendly.

In the UK, the “Picture This” tool of our FutureYou business has innovated retirement planning. By selecting images representing personal preferences, the tool determines a person's more likely lifestyle once work is over: adventuring around the world, learning new skills, spending time with friends, devoting oneself to charity.... The second stage suggests how to get there depending on current age, retirement date, current income and existing savings.

OECD

Report from Flore-Anne Messy, Head of the Financial Affairs Division of the OECD

Flore-Anne Messy (OECD)

Individuals are increasingly responsible for financial decisions such as making their own arrangements for retirement income or covering (at least partially) some important health care costs, as well as identifying and managing a number of risks inherent to complex financial products and a more challenging economic and financial environment. At the same time, **financial access is improving** around the world and is especially high in most EU countries. Yet, OECD research and other national studies have consistently shown that many consumers and entrepreneurs, especially those in vulnerable situations, are still ill-equipped to take on such responsibilities and often fail to make appropriate decisions.

Improving levels of financial literacy through tailored financial education and awareness initiatives and strategies is essential to enable individuals and micro/small businesses to make sound financial decisions and improve their future financial wellbeing. In this respect, (and as recognised by G20 Leaders since 2010), financial education is an **important complement to robust financial consumer protection and financial inclusion** measures designed to promote financial stability, sustainable economic growth and more inclusive societies. As a testament to the importance of financial education, a good number (16, more than half) of EU member states have already embarked in the development of national strategies for financial education following the **OECD/International Network on Financial Education (INFE) High-level Principles on National Strategies for Financial Education** endorsed by G20 Leaders in 2012.

To be effective financial education should start early and ideally in schools to provide children and youth with basic skills and habits which can be built on through experience, information, training and advice as adults. In this respect, **financial education is a life-long process** which should be reinforced in adulthood prioritising populations at risk or in high demand (including MSMEs, women, migrants). In delivering financial education special attention should be paid to the evolving needs of the target audience including those brought about by the increased digitalisation of the financial system. Digital solutions should also be harnessed to provide tailored, timely and innovative to develop financial competence and help consumers control and plan their finances.

All stakeholders can effectively contribute to financial education efforts. Public authorities should certainly take the lead in defining objectives and establishing an adequate national policy framework. But **private financial institutions** can also play an important role in supporting the implementation of suitable financial education initiatives especially relying on their expertise on these issues, direct access to consumers and investors, appetite and resources. However, **potential conflicts of interest** with their commercial activities have to be effectively identified, monitored and addressed as needed (see OECD/INFE guidelines for private and not-for-profit stakeholders in financial education).

The **OECD Governments officially recognised the importance of financial literacy in 2002 with the launch of a unique and comprehensive project**. In 2008, the project was further enhanced through the creation of an **International Network on Financial Education (INFE)**. The INFE has high-level membership from over 240 public institutions - including central banks, ministries of finance and ministries of education - in over 110 countries and most EU countries. The INFE Technical Committee meets twice a year (and at least once in Europe) to share country experiences and discuss the strategic direction outputs, building on unique data collection, policy analysis and dedicated research.

The EU could further support these global efforts by promoting the development of national strategies and effective practices in Europe possibly through dedicated **initiatives and events developed in partnership with the OECD/INFE** (as is currently happening in Asia, Eurasia and Latin America)**.** These could include awareness raising activities, as well as direct support to countries which wish to improve financial literacy across their population, and dedicated research aimed at strengthening the impact of financial education initiatives.

PENSION FUNDS

Report from Matti Leppälä, Chief Executive Officer of PensionsEurope and Chair of the pension stakeholder group of the European Insurance and Occupational Pensions Authority

Matti Leppälä (PensionsEurope)

Financial education is important for people to understand the need to prepare for retirement, empower them to make informed decisions in the pension savings market and help decrease the current high number European citizens who do not have workplace pensions. As a result of demographic change public pay-as-you-go pensions will deteriorate and more funded private pensions are needed. The current market conditions are leading to a shift from Defined Benefit plans to Defined Contribution plans thus meaning that there will be more individual risks to manage. Previously peoples experience was that they had no choice or personal responsibility for the pension outcome and with the changing pensions landscape they are faced with increasing choice and risk. Pensions are becoming more like consumer products. The borderline between occupational and personal pensions is becoming increasingly unclear.

Financial literacy is important but should not be overestimated. Life is full of complexities with which people have to and will cope, but often without optimal outcomes. Also in pensions the key is better design of pensions and especially of default options as in practice most opt for the default.

Financial education can improve the understanding of financial services and the ability to make right decisions**.** It can also raise awareness on the need to save for retirement. However, financial education does not directly mean better outcomes, as it does not improve financial literacy fast enough in relation to rapidly changing environment (economic cycles, labour market changes etc.). The impact of education is limited because even if people have financial knowledge they are not always able to use it in practice (procrastination, limited choice in the pension system, tendency for defaults; e.g. a study in Denmark showed that only 15% of individuals are "active savers" while 85% always stick to defaults and thus prefer passive choice).

Improvements in financial education can be made at European level even though education is a competence of the Member States. Pension providers should play an important part as well. For success the involvement of all stakeholders is essential. There is not an ideal frame to provide education. Financial education should be broad and not limited to certain kinds of categories but also adapted to the target group.

PensionsEurope believes that pension **design** is key for:

- Compensating for the low impact of financial education.
- Pension's adequacy (adapted to needs and interests of members and beneficiaries). When it comes to annuities, providers are more likely to be more equipped than individuals to manage longevity risks (life expectancy mitigation).
- Framing the decision making process in order to avoid choice overload.

Benefits of “auto features” such as auto enrolment, default options, defined architecture of choice.

FINANCIAL SERVICES USERS

Report from Christophe Nijdam, Secretary General of Finance Watch


Christopher Nijdam (Finance Watch)

Objectives of financial education

We should point out that in the narrative of causes for the current crisis, blame has shifted slowly but surely from the industry (i.e. sub-prime lending) to governments (i.e. budgetary overspending) and finally to citizens (i.e. financial illiteracy).

There is now a tendency to promote financial literacy as an alternative solution to financial regulation and industry accountability on behaviour, ethics and conduct risk. This tweaking of the narrative is pernicious as it implies that it is consumers’ and citizens’ own fault if they were mis-sold financial products. Financial literacy is indeed critical – but not sufficient - to avoid high levels of debt and excessive fees for financial products, access to credit and saving for retirement. But there is no causal chain that leads from financial education to higher financial literacy, better financial behaviour, and then to improved financial outcomes. In fact, surveys in the US have shown that consumers who took finance classes were no better at taking financial decisions than those who had not.

The question we should ask ourselves is what do we want to achieve with financial education? Do we want to live in a society where ordinary citizens are left to navigate one by one through an ever-changing number of financial products armed only with a little financial education and the principle of “caveat emptor”? Or do we want a slightly friendlier and safer environment for citizens to meet their financial needs?

Furthermore, many consumers do not want to make their own financial decisions, either because they find the issues too complex or because they fear the consequences of choosing the wrong option. The move towards Defined Contribution pensions from Defined Benefit pensions is a good example of that: why would an ordinary citizen feel comfortable choosing between different pension plans in a Defined Contribution scheme when investment professionals have failed to manage the challenges of Defined Benefit schemes? Is transferring that risk to individual citizens through Defined Contribution plans a responsible answer?

Priority attention to consumers

Education should be tailored to consumers’ daily experience and needs. E.g. for students it could be saving money for holidays, mobile phone or college fees, while for SMEs it could relate to credit or insurance, or how to buy investment products, etc. But we should be realistic about the benefits. Consumer enthusiasm for learning about finance is rather limited: when a free online financial literacy course was offered to struggling credit card borrowers, only 0.4% logged on to the website and just 0.03% completed the course. Those who choose to be educated about finance may be those who are already interested and relatively well-informed about it. And even if the course is taken, financial education appears to increase confidence without improving ability, leading to even worse decisions.

European strategy

Due to the different situations in member states, financial education should remain a national competence. What could be harmonized at EU level is information for consumers about their protections and rights. The EU can run general campaigns and support national initiatives and consumer centres on the subject.

Role of the financial industry

The industry has substantial resources with which it can outmanoeuvre financial education. When public education campaigns blasted warnings about predatory mortgages, lenders of every stripe quickly adapted their marketing to proclaim their trustworthiness. Financial services firms engage in lots of marketing, because it does work. Given the ubiquity of advertising, effective education would need to reach people at the point of financial decision-making.

Digitalisation as an opportunity

There are certainly opportunities, for example with Millennials who are much more tech-savvy than previous generations. Consumers can now more easily reach information, compare it, educate themselves from multiple sources and receive advice when they want. However the promotion of financial education through the use of technology should be based on three principles:

- first, to effectively use computers, mobile phones and the Internet;
- second, they need to understand the content they have received through digital means;
- and lastly, apply it to the best of their knowledge and capacity.

Digitalisation does allow financial information to be democratized: information is often the difference between getting a ‘lemon’ of a deal or a favourable one. By enabling connections, technology can also bridge geographical differences.

We should promote consumer centres and governmental organizations where the consumer may ask questions and get unbiased information. For instance, in the US, there is an interactive online tool called -Ask CFPB (consumerfinance.gov/askcfpb/) – the Consumer Financial Protection Bureau - which gives consumers real-time “when you need it” answers to more than 1,000 questions about financial products and services including credit cards, mortgages, student loans, bank accounts, credit reports, payday loans, and debt collection.

Providing a clear and functional regulatory framework on digitalisation, for instance to avoid the increased risk of mis-selling, is essential.

Alternative tools

Basic financial education will empower citizens but is not enough to protect them. The industry must simplify its offering of basic financial services and limit the transfer of a broad range of financial risks to consumers. Financial education should not be used as an alibi by the industry to do “business as usual”, and it should not be tainted by ideology that contains an industry bias.

Wrong financial decisions can have a much bigger lifetime impact than in other fields on our families and our children, so it is even more important to ban toxic products and have a product approval agency before certain products are brought to market. We don’t need financial products with bells and whistles, we need plain vanilla products and transparency to promote real comparability and real competition. Affordable and independent advice is also key.

Basic financial education programs would need to decide what lessons to teach against a background in which we lack technical and normative consensus on what constitutes correct financial behaviour. For example, saving and investing for retirement these days requires predictions in areas where experts routinely disagree, such as the returns that can reasonably be expected on various investments over various future time periods. Like most financial decisions, selecting investments also requires trade-offs between risk and return that present a normative question: how much financial risk should an individual or household take on? Financial education cannot be effective if it sidesteps these issues.

Financial decisions require an assessment of the probabilities, timing, and costs of a host of misfortunes, from job loss to health problems, to which some consumers respond with either denial or over-optimism. The consequences of financial choices made today will often not be known or felt for many years, but in making decisions people often place too little weight on delayed or uncertain outcomes, although at widely varying discount rates. Education programs need to reflect this as well.