

Alan Greenspan: Financial education

Remarks by Mr Alan Greenspan, Chairman of the Board of Governors of the US Federal Reserve System, at the 33rd Annual Legislative Conference of the Congressional Black Caucus, Washington, DC, 26 September 2003.

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I am pleased to be here today to discuss the importance of financial education for consumers. Forty years ago, Dr. Martin Luther King, Jr., challenged this nation to fulfill its promise of freedom and equality for all citizens, to ensure that all Americans are able to participate in day-by-day business without being hampered by debilitating discrimination. In those forty years we have witnessed a great deal of change. However, the momentous goal of ensuring that everyone has access to the benefits of our free and efficient market economy has yet to be achieved and remains as relevant today as it was in August of 1963, when marchers gathered around the Lincoln Memorial. Increasing economic prospects for people in traditionally underserved neighborhoods and granting every individual the opportunity to succeed remains crucial to our national well-being. A strong and effective system of education is one fundamental way to strengthen our economy and raise living standards. And education about personal finance that helps consumers of all ages meet the challenges and demands of our increasingly knowledge-based economy is one important component of such a system.

Trends in Consumer Finances

Today's financial world is highly complex when compared with that of a generation ago. Forty years ago, a simple understanding of how to maintain a checking and savings account at local banks and savings institutions may have been sufficient. Now, consumers must be able to differentiate between a wide range of financial products and services, and providers of those products and services. Previous, less-indebted generations may not have needed a comprehensive understanding of such aspects of credit as the impact of compounding interest and the implications of mismanaging credit accounts. Today, however, the advance of telecommunications technologies and the development of other new technological tools have broadened the availability of credit and other banking services. More generally, these advances mean consumers must be familiar with the role that computers play in the conduct of every traditional financial transaction, from withdrawing funds to borrowing.

Data, both empirical and anecdotal, point to trends in consumer financial conditions that have caused concern among some consumer groups. Household debt has risen appreciably in recent years. While analyses suggest that, overall, the level of debt is being serviced adequately, a record number of nonbusiness bankruptcy filings reveals that many consumers are experiencing significant financial distress.

Regulators, lenders, community leaders, and consumer advocates also continue to be concerned about abusive home mortgage lending practices and other consumer credit practices that target vulnerable populations. Financial education is especially critical in the effort against these deceptive practices. Consumers empowered with the information to make educated financial choices are less susceptible to fraud and less likely to become entangled in financially devastating credit arrangements.

Trends in the Financial Services Industry

Some may believe these trends indicate that market forces have hurt consumers. On the contrary, household and business borrowers have benefited from the technological developments that have enhanced financial services, and their remarkable growth. Computer and telecommunications technologies have lowered the cost and broadened the scope of such services. Consequently, specialized lenders and new financial products tailored to meet very specific market needs have proliferated. At the same time, the development of credit-scoring tools and the securitization of loan pools are opening doors to national credit markets for both consumers and businesses. Deregulation has encouraged competition and innovation by opening the marketplace to the entry of new service providers and the expansion of existing service providers.

Throughout our banking history, markets have adjusted to respond to demand. These structural changes have heightened competition, resulting in lower costs and the emergence of increasingly

diverse and highly specialized organizations. These entities range from banks and brokerage firms that offer their services exclusively through electronic delivery mechanisms to locally based public-private partnerships that provide counseling and financing arrangements to low- and moderate-income families.

The Role of Financial Education

Given the significant changes in the financial marketplace, some consumers may lack sufficient familiarity with the newer financial concepts to make sound decisions. In response, government agencies, major banking companies, grass-roots consumer and community groups, and other organizations have developed a wide variety of financial education programs. Some are tailored to specific products such as credit cards and home equity lines of credit, and others are focused on specific consumers, such as military personnel, college students, or first-time homebuyers. Yet other programs adopt a more comprehensive approach, teaching broad audiences about savings, credit, budgeting, and similar topics. All of these programs are designed to give individuals tools to manage their personal financial affairs and make responsible decisions about products that can improve their economic well-being.

The financial services industry maintains a keen interest in financial education programs and provides significant support. A recent nationwide survey of bank-sponsored financial literacy programs at fourteen of the largest twenty-five banks, as well as other smaller banks, noted a consistent increase in the number of financial institutions that support financial education initiatives. Bankers who responded to a 2003 Consumer Bankers Association survey reported that 98 percent offer financial literacy programs or work with partners that support such efforts. Many bankers participate because they want to be recognized as good corporate citizens; however, many other bankers have realized that their activities may help them reach hard-to-serve markets such as immigrants or people without a relationship with a bank.

Organizations, including some of the Federal Reserve Banks, working at the community level have established Volunteer Income Tax Assistance (VITA) sites, where instructors not only help people with their tax returns, but also teach them how to budget their income, pay their bills, and manage credit. These programs are especially noteworthy since preliminary research reveals a considerable number households that receive tax refunds intend to save them or invest them in education and other wealth-building activities.

Building a Foundation for Financial Education

Children and teenagers should begin learning basic financial skills as early as possible. Indeed, improving basic financial education in elementary and secondary schools can help prevent students from making poor decisions later, when they are young adults, that can take years to overcome. In particular, it has been my experience that competency in mathematics--both in numerical manipulation and in understanding the conceptual foundations--enhances a person's ability to handle the more ambiguous and qualitative relationships that dominate our day-to-day financial decisionmaking. For example, through an understanding of compounding interest, one can appreciate the cumulative benefit of routine saving. Similarly, learning how to conduct research in a library or on the Internet enhances decisionmaking. Focusing on improving fundamental mathematical and problem-solving skills can develop knowledgeable consumers who can take full advantage of the sophisticated financial services offered in an ever-changing marketplace.

While some adults may believe that financial and related mathematical concepts are too complex for younger school children, I was pleased to have an experience that dispels such thinking. In June, I had the opportunity to discuss financial matters with a sixth-grade class that had begun a financial education program sponsored by Operation Hope, a national nonprofit organization. The children's surprisingly precocious questions demonstrated an ability and a desire to learn more about the fundamental principles of money and banking.

This encounter and countless others in classrooms and community centers across the country indicate that, in the long run, better basic education at home and in elementary and secondary schools can provide the foundation for a lifetime of learning. But not all have risen to the level of that sixth-grade class. We need to exert especial effort to improve the skills and earning power of those who appear to be falling behind.

The Federal Reserve has a keen interest in promoting financial education and increasing the visibility of resources for consumers. In May, the Federal Reserve launched a national campaign to highlight the importance of personal financial education and money management to achieving short- and long-term goals such as pursuing higher education, purchasing a home, or starting a business. This initiative includes a public service announcement, a printed brochure, and a dedicated [web site](#) that identifies resources for learning more about financial management products and services.

The Federal Reserve also has a long-standing interest in increasing minority access to credit markets. We study access to mortgage and small business credit for underserved populations and have participated in a pilot program teaching mortgage finance at select community colleges. This innovative program, targeted to minority students in underserved communities, trains individuals for a broad array of career opportunities in mortgage lending.

We also are interested in measuring the effectiveness of financial education programs. Studies evaluating such programs were presented at the [Federal Reserve System's 2003 Community Affairs Research Conference](#). In addition, the Federal Reserve and the Department of Defense are collaborating on a study of the efficacy of personal financial management education provided to members of the military services and their families. This research will provide insights into what financial education interventions prove most effective with specific audiences and will provide valuable guidance for teachers, employers, and other financial education providers and funders.

Building bridges between community organizations, educational institutions, and private businesses is essential to increasing familiarity with new technological and financial tools. And the success of such efforts will bear significantly on how well prepared our society is to meet the challenges of an increasingly knowledge-based economy.

In closing, let us remember that education is the primary means for creating new economic and financial opportunity for everyone. If we are able to boost our investment in people, ideas, and processes, just as we do in machines and technology, consumers and the economy can readily adapt to change, providing ever-rising standards of living for all Americans.