BANK OF ENGLAND

Speech

Financial education and the Bank of England

Speech given by

Ben Broadbent, Deputy Governor Monetary Policy

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The views expressed are my own and do not necessarily reflect those of the Bank of England or other members of the Financial Policy Committee or the Monetary Policy Committee.

Welcome

Hello and thank you for asking me along today. These are very important issues and I'm grateful to be able to talk to you. My purpose today is to set out a few things we've been doing at the Bank to help schools with economics education.

Some of this, I should say, is self-interested. Over time, we benefit from having a large and diverse pool of well trained economists who might consider working for us. The same is true of many other institutions. More significantly, public understanding of what the Bank of England is for, and what it does, is very important. It matters because it is the general public that constitute our ultimate and most important stakeholders. Although the public already hold us to account via parliament, it's important that we can explain ourselves, and in turn listen to people's concerns, people, more directly. (I have to concede that, important though they are, not everyone in the country is glued to his or her TV screen watching parliamentary hearings on the most recent monetary policy decisions.)

It matters too because the effectiveness of our policies themselves may actually depend on that understanding. I can give you an example from the area of the Bank's work that I'm most closely involved with, namely monetary policy. The Monetary Policy Committee's primary objective, set by parliament and the government, is to keep price inflation low and stable. Subject to that target, we are also required to support growth and employment (over the longer run, monetary policy will have little impact on these things; over the shorter run it can have important effects). However, the scope for us to do that – for monetary policy to help even out the ups and downs of the economy – is greater if the inflation target is itself understood and credible. And that in turn is more achievable when people understand how we're trying to meet it. One could make similar points about the Bank's newer responsibilities for financial stability.

So it's very important that we explain our role, and our policy decisions, as clearly – and to as wide an audience – as we can. And it was partly these considerations that prompted our new programme of public and educational outreach, launched last year.

However, they weren't the only considerations. In a moment I'll outline what this outreach effort involves. I then want to say something about the importance of personal financial education.

There are two distinct parts to the strategy. One involves visits to secondary schools. Below director level, more than 400 people working at the Bank have volunteered as "Ambassadors", who explain to school pupils what we do and why. People on our policy Committees do the same. It's now rare that, on one of my regular trips around the country to hear from businesses about what's going on in the economy, I don't also make a visit to a local school. In all, we reckon we've talked to 12% of the UK's state secondary schools in the past 18 months alone.

For our part, we very much enjoy these visits. And the feedback has also been good. Central banks are not often associated with the words “positive”, “appreciated” and “inspiring” so you can imagine how invigorated our Ambassadors are when they hear them.

The second strand is a package of online materials – something we’ve named “EconoME” – to help non-specialist teachers of students aged between 11-16 years deliver quality financial education. EconoME comprises three one-hour lessons focussing on financial decision-making and the implications of these decisions on students and the world around them. The resource draws on real-world examples, provided by the Bank of England, which shows how the Bank makes decisions and the practical skills we employ to understand the likely outcomes of those decisions. These examples include the impact of interest rate rises on different agents (such as a bank manager, car manufacturer and consumer) and analysing the cost of a basket of goods to explain how inflation is measured. As part of the resource, EconoME features interactive videos, in which Bank of England staff explain how they deal with these issues in the course of our everyday work. It is designed to help young people understand the economy better and provide them with the analytical skills to make informed decisions.

Take up amongst schools has been both rapid and encouraging with 36% of UK secondary schools having registered for the resources since launch in April 2018. We’re currently designing something similar, and age-appropriate, for primary school children to launch later this year. We will then focus on developing resources to support the GCSE and A level economics syllabus.

Now, the name “EconoME” may or may not grab the attention of your pupils. But I think the content is excellent. And one thing the name should tell you is that these resources are designed for more than learning some economics. They’re also intended to help people with their personal financial decisions.

These personal financial decisions matter. I should emphasise that, from the bird’s eye perspective we take as guardians of overall financial stability, I don’t think overall levels of household debt are a great worry at the moment. Relative to income, household debt is comfortably lower than its levels in the middle of the last decade. Interest payments, defaults and the proportion of households spending a very significant (>40%) proportion of income on servicing debts are all at historical lows. Interest rates would have to rise a lot – certainly by a lot more than financial markets expect – for this to change significantly.

But underneath any aggregate, there are always more concerning stories. According to the Bank/NMG survey 7% of households say they are "very concerned" about their debts, even if they are able to service them. And we know from extensive research that financial worries can be an important contributor to poor mental health. High levels of debt are, for example, associated with anxiety and depression, and studies using changes in local house prices and foreclosures have found that changes in households' financial situation can affect health.[1]

One thing we also know is that people are generally prone to over-concentrate on present, urgent needs, and neglect things that are more important for us over the longer term. Economists are naturally interested in how people trade off the future against the present. In standard models that seek to describe these choices, it is assumed that people discount the future at a constant rate: the extent to which we care more about things one rather than two months from now (say) is the same as between today and a month away.

But on many occasions, and compared with this simple representation, experiments suggest that people focus excessively on the present. It's not just that they generally place higher value on getting something sooner rather than later: people seem to put a particularly high weight on current outcomes. They seem to discount the importance of what comes tomorrow, relative to today, more heavily than they do any two successive days further into the future. This is referred to in the economic jargon as "hyperbolic discounting" and by psychologists as "present bias".

It helps to explain why we often put things off right until the last minute, even if the cost of doing it is much higher by that time. It means it can be advantageous to commit to things that are good for you over the longer term – regular saving, or signing up to a gym programme – but that, when the time comes, you might be tempted to avoid.[2] And it can also explain why people borrow money, and roll over those debts, even at very high interest rates.

This borrowing can take many forms, including foregoing opportunities to reduce the longer-term cost of something. In their recent book "Scarcity", economist Sendhil Mullainathan and psychologist Eldar Shafir give the example of rag collectors in India – people who rely on collecting discarded clothes and selling them on. It is an ardous job with very little reward. But it is, at least, a job that requires very little investment in training or equipment: the only "capital" a rag collector will need is a pushcart, which might sell for $30. Yet, despite saying they'd very much like to own their own, nearly all these rag collectors instead rent their pushcarts, at a cost of $5-$10 a month. They therefore spend in a matter of 3-6 months what it would cost to own the thing outright. This is an enormous, and self-imposed, effective rate of interest – an annual rate of somewhere between 200 and 400 per cent.[3]

[1] Gathergood (2013).
[2] Laibson (1997).
[3] This would cover any depreciation costs, which the owner of the cart would have to bear. But these are likely to be only a small part of the rental cost.

Mullainathan and Shafir document many such examples. And they go further: they claim, supported by the result of interesting experiments, that the tendency to over-weight the present, at the expense of the future, is itself increased by financial stress. The more cash-strapped people feel, the more prone they are to taking decisions that make the situation worse. Financial distress isn't just the partial result of wanting things sooner rather than later: according to Mullainathan and Shafir it can also be the cause of it. The result can be what the authors describe as a "scarcity trap".

I don't think we have the evidence to say that better financial education is enough to escape such a trap. But it surely can't hurt. A recent study using data from the OECD Programme for the International Assessment of Adult Competencies, or PIAAC, found that rates of financial literacy – defined as the ability to answer relatively straightforward financial questions[4] – were lower here than in other advanced economies. According to a recent, UK-specific survey by a private-sector firm, less than half of adults and barely a third of teenagers actually know what an interest rate is. And we also know that the less financially literate tend to face higher debt costs than others and more often face financial distress.[5] If financial education can make any difference at all to these problems we have a duty to try and improve it.

Conclusion

The Bank of England has a direct interest in improving and broadening the teaching of economics. There's an appetite for it. According to a recent poll, three quarters of the public believe economics should be taught in schools.[6] Yet only around a third of schools offer children the option to study economics from the age of 14.[7] We hope our online teaching materials will help fill some of the gap. However, we also hope that our "EconoME" package can help with financial literacy. I think economics is fascinating and very valuable. But you don't need to be an economist to understand the basics of personal finance and their importance for people's lives.

One of the things economists like to focus on is return on investment. For the modest investment the Bank has made to develop EconoME - £80,000 - we hope to reach over 130,000 young people directly by 2020, with a multiplier effect through word of mouth and social media. And we know that our efforts will complement and reinforce those of the PSHE Association, Young Money, Economist Educational Foundation, NowTeach, Speakers for Schools and many other initiatives that are improving mathematical and financial literacy and inspiring students to broaden their horizons.

We know our contribution depends on the support of teachers and influencers. That's why we're so grateful for your help in informing, educating and inspiring your students.

[4] One was along the lines of: if a litre of cola costs £3.15, how much would a third of a litre cost? Around 60% of adults in England and Northern Ireland were able to answer this correctly (see Bhutoria et al, 2018).
[5] Disney and Gathergood (2011).
[6] ING – Economics Network (2017).
[7] Haldane (2017).

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