

**Remarks by  
Sheila C. Bair Chairman,  
Federal Deposit Insurance Corporation  
Before  
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Good afternoon and thank you Courtney for that warm introduction. As you noted, I am passionate about the topic of personal savings, and I look forward to discussing my views with you today. It is an honor to join the distinguished roster of speakers who have addressed the City Club of Cleveland. Presidents Bush and Clinton, Archbishop Tutu, Ambassadors, Senators and Representatives — these are certainly hard acts to follow! And it is a pleasure to visit your beautiful city — the Forest City, as first described by Alexis de Tocqueville in *Democracy in America*. Your Olmsted-inspired parks, your many architectural treasures -- all help explain why Cleveland has been ranked by the Economist magazine and others as one of the most livable cities in the United States.

From its darkest days of economic crises, culminating in the default of 1978, Cleveland has worked hard to emerge as a model for economic revitalization and renaissance. The city has successfully transformed itself from a heavy dependence on manufacturing to a much more diversified set of industries. "C-town" is now known as the "comeback city" and has become a leader in areas such as health care and biotechnology. Clevelanders know what it is like to deal with financial adversity and understand the importance of having a cushion of savings to fall back on during hard times. This is one of the reasons why I am pleased to talk with you today about ways we might further promote personal savings on a national level during "Cleveland Saves Week" and the first ever "America Saves Week."

### **A Lost Savings Culture**

As a nation, we are not doing a very good job of saving these days. Last year, U.S. personal savings amounted to a negative \$92 billion. That is, Americans spent \$92 billion more than they took in as disposable income. That result, a savings rate of negative 1.2 percent, marked the second consecutive year of "dis-saving" by American households.

American savings habits do not compare favorably to other developed nations. Many European industrialized countries are approaching 15 year savings highs. In France, Germany, and Italy, savings rates exceed 10 percent.

It should be recognized that U.S. savings data does not reflect growth in the value of family assets such as people's homes or the increases in stock market investments. In addition, spending on education — historically one of the best investments a person can make — counts as consumption, not savings, as is the case in some European

countries where measures of savings are considerably higher. None-the-less, the trend of decreased saving is pronounced and troubling.

The American transition from a savings culture to a consumption culture has been relatively recent. Indeed, 2005 was the first year since the U.S. began collecting these data some 60 years ago that the savings rate plummeted into negative territory. Historically, the U.S. savings rate has averaged a healthy 7 percent.

This phenomenon is puzzling, since we are, in many ways, descendants of a generation of savers. We all probably have stories we could tell of the cash-only financial habits of our depression era parents and grandparents that seem antiquated today. My own parents shunned debt. In fact, "Thou Shalt Not Borrow" was their eleventh commandment. They were more than willing to forgo goods and services until they had saved enough to pay for them in cash. They simply did not want the burden of debt hanging over their heads.

What has happened to America's savings culture? Economists have various theories.

One theory is that long periods of economic prosperity have reduced families' perceptions about the need for precautionary savings. It has been over 25 years since we experienced a severe economic downturn, and even the troubled 1970's were nothing compared to the hardships of the Great Depression.

This theory may explain reduced savings among middle and upper income families who have never experienced severe and prolonged economic distress. However, it does not resonate in explaining the lack of savings among lower income families. For these families, the growing wage gap — combined with increasing housing, health and education costs — have made economic hardship a way of life. They have not shared in the economic good times. For them, economic conditions have stretched family budgets and made it much more difficult to save.

Another theory is that wider access to credit products by families of all income levels has dampened the perceived need for precautionary savings. Consumers' ability to tap into borrowing sources such as credit cards or other short-term loans may be enabling spending that was once available only with funds set aside for "rainy days." Indeed, the explosion in consumer credit usage during the past decade suggests most people seem more willing to borrow than save.

Because of their financial capacity, middle and upper class families are more likely to have access to reasonably-priced short-term credit, compared to lower income families. For lower income families confronting an unexpected emergency or a budget shortfall, their only options may be high-cost credit products, such as fee-based overdraft protection or payday loans. Research by the Consumer Federation of America shows that people without savings are six times more likely to use such products. The burden of paying back these expensive loans further impedes the ability of lower income families to save by putting additional demands on already strained family budgets. This

can have the effect of locking lower income families into a vicious cycle of debt that provides few exits to financial wealth building and economic independence.

All of these theories suggest that the evaporation of our savings culture has many roots. As Chairman of the FDIC, I can't do much about job creation, income distribution, rising health care costs or access to quality education. But I, along with other financial regulators and policy makers, can exercise leadership in trying to make sure the nation's financial system works for all Americans and serves as a vehicle for building savings, not stripping wealth.

## **An Inclusive Financial System**

I am conservative and a bit old-fashioned in my political thinking as well as my economic philosophy. I believe in limited government, free markets, and most importantly, the opportunity for people to work hard and get ahead. I also believe the government needs to set rules so that the markets work for everyone. Our financial system should be responsive to individuals' desire for economic progress. It should facilitate ascension to greater income and wealth building, not serve as a slippery slope to economic decline.

A financial system that expands access to financial ownership and empowerment fosters a culture of entrepreneurship and hope, strengthens families, and lifts the fortunes of our nation. A financial system which blocks access to financial ownership, fosters a culture of despair and lethargy, imposes stress on families, and causes people to lose faith in the American dream.

It seems to me that our current financial system is not working as well as it could for low-and-middle income families. Instead of helping them save, for all too many people, it may be pulling them deeper into debt. Instead of providing access to reasonably priced basic financial services, it may create needless barriers for families or perverse incentives for financial institutions.

What can we do to make our financial system work better for low-and-middle income Americans? There are no magic bullets, but there are some areas where banks and regulators can intensify our efforts to make the system work better for all. I would like to highlight a few of those today. But first, let me address the threshold need for financial education to help more people master the basics of saving and wealth accumulation.

## **The Importance of Financial Education**

You should not have to be a financial wiz to understand our financial system, but there are certain core principles that need to be mastered. Central to these is the principle of compound interest and understanding that interest compounding on savings accounts will grow exponentially, while unfortunately, interest compounding on unpaid debts will do the same. Compound interest is fundamental to understanding why it is important to save for the long term, and pay off debts as soon as you can.

For many years, I have been writing for children on financial matters. Several years ago, former Secretary of the Treasury Paul O'Neill and I jointly authored an article for Highlights Magazine for Children which discussed the magic of compounding. To illustrate the principle, we suggested to our young readers that they offer to let their parents reduce their weekly allowances to a dime, with the understanding that they would pay 10 percent compound interest each week. Yes, since publication of that article, I have had more than one complaint from parents who quickly found these compounding interest payments overwhelming. In fact, over the course of 24 months, this scheme would result in an allowance of \$2,071 a week. Just as we were trying to teach kids something instructive about interest bearing financial products with this little exercise, I think we taught their parents something useful as well. This is an added benefit of children's financial education — the material frequently reaches parents in a simplified, non-intimidating format and they end up learning something too.

Many schools have begun integrating financial education into their curriculum and I applaud these initiatives. There is no shortage of "real world" financial tasks which can be woven into math problems. Balancing a check book, calculating credit card debt, or projecting savings account balances at compounded interest rates are good examples. The integration of finance into math makes the math more relevant to kids, and also strengthens their core financial skills.

I am also a big fan of school based banking programs, and I am happy to see that many banks in Ohio offer such programs. They can help kids start an early savings habit, and learn something about banks at the same time. Such programs can also expose "unbanked" parents to the benefits of having a bank account. This is particularly true among immigrant communities where parents may confront language barriers or be unfamiliar with or distrustful of banking institutions.

I was a volunteer coordinator of the school banking program at my kids' elementary school in Western Massachusetts. Yes, you may think it curious that I liked spending my Wednesday mornings counting coins and filling out deposit slips. But as a parent, and a financial policy maker, I derived tremendous enjoyment out of seeing these youngsters come to our school bank each week with their treasured savings. They took such great pride in seeing their money grow with each deposit. I knew those regular savers already had a leg up in ultimately understanding how to make the financial system work for them.

Parents can also do a lot to instill good savings habits in their children. At our house, we give our kids a base amount, with a little extra which automatically goes into savings. Our first grader receives a dollar and a quarter each week, the quarter immediately gets deposited in her piggy bank. We call it "speed saving" and find that with kids, as well as adults, savings comes easier if it is done automatically. We also use a clear container for her piggy bank so she can see her coins pile up. After her savings have accumulated for awhile, we deposit the money in — of course — a savings account at an FDIC-insured bank.

As I mentioned, kids are not the only ones who need financial education. It is a fact that most grown-ups do too. The FDIC has long recognized the importance of financial education in promoting economic inclusion. Low income families, in particular, need reliable information about how to manage their financial affairs. The FDIC's award winning financial education curriculum, Money Smart, has been the cornerstone of the FDIC's efforts. Since its inception in 2001, Money Smart has been offered through over 1,000 organizations to over 660,000 individuals. Available free of charge and in six languages, it has helped countless consumers develop money-management skills and learn how to use banking services effectively.

## **The Role of Banks**

Let me now turn to the role of banks and their regulators. Banks provide the gateway to the financial system. Expanding access to banking services expands access to economic empowerment. For those consumers trying to climb the economic ladder, banks form the first rung.

Why are so many consumers unbanked? Why do so many turn to higher cost non-banks for financial services? I think part of the answer may lie with the regulatory community and the types of incentives we provide. Let me provide some background.

In the 1970s, Congress passed a law called the Community Reinvestment Act or CRA. Its purpose was to ensure that banks were making every effort to serve the credit needs of their communities, particularly low and moderate income neighborhoods. When CRA was enacted, there was a severe shortage of credit available to low and moderate income neighborhoods and all too frequent examples of racial redlining and discrimination. The CRA was passed to address those problems, and I think the law has achieved tremendous good. However, with so much emphasis on credit over the years, there has been too little focus on the need for banks to offer reasonably priced, basic financial services - such as check cashing, money orders, and most importantly, savings accounts - to their lower income customers.

At the FDIC, we've started to explore CRA incentives. Specifically, I want to explore how we can enhance incentives for banks that offer products that build wealth. Last December, we proposed giving banks CRA credit if they provided low cost alternatives to high-cost payday loans which can strip wealth through high, recurring fees. And the FDIC has formed a new advisory committee — the Advisory Committee on Economic Inclusion (ComE-IN) to explore in detail, among other things, the kinds of incentives regulators currently provide to banks, and specifically, whether we can do more to encourage savings products.

To their credit, banks, on their own, are already doing many good things. The 15 banks partnering with the Cleveland Saves program are offering no or low balance savings accounts to help lower income consumers at no expense. They've also initiated the Roll Your Change week which I understand has generated over 2,500 deposits and over

\$200,000 in savings. Here are some other ideas I'd like to propose to banks as they work with their communities to facilitate savings:

First, given that we are midway into tax season, I'd suggest that banks involve themselves in the IRS Volunteer Income Tax Assistance program, or VITA. This program provides free tax-preparation services for low and moderate income taxpayers. It provides participating banks with opportunities to open up new bank accounts for these taxpayers to facilitate direct deposit of tax refunds. What's more, under a recent change in the law, taxpayers can split their refunds into three accounts instead of one, allowing some portion of those refunds to go into savings. And, back to the incentives for banks, their participation in this program can result in favorable CRA credit.

Second, banks should take a look at offering Individual Development Accounts or IDAs. First introduced in 1996, IDAs provide matched savings for lower income families who are building toward the purchase of an asset, most frequently, a home, a small business, or college education. Ohio currently permits IDAs with matching features, which can be provided through government or private sources. Banks usually act as depositories for the matching funds as well as provide and service the accounts. Sometimes, they also provide the matching funds.

Third, banks should start a savings deposit program at their local schools. Those young savers may eventually become bank customers --- their parents too.

Fourth, I encourage banks to look at ways to pair reasonably priced short-term loan products with savings vehicles. As I mentioned earlier, lower income families may have few good alternatives when faced with a financial shortfall. I believe banks can provide sensible alternatives to products such as payday loans in a way that helps families manage their short term credit needs and build a savings cushion for emergencies.

Consider this successful example of a credit union in North Carolina, which is operating a highly profitable small loan program that is also generating a significant amount of deposit funding. Here is how it works. The credit union offers a line of credit of up to \$500 linked to the customer's checking account. Each time the customer draws on the line of credit, five percent of the loan proceeds are automatically deposited into a savings account. This product was developed after the credit union noticed the sizable number of its members using payday lenders. It is now used by 40,000 customers and has produced \$10 million in savings in just two years.

I would encourage banks to look at the guidance the FDIC issued in December on small dollar lending as well as a template we developed for such a program with a savings feature. After all, payday loan customers are already bank customers. Banks are well positioned to offer small dollar loans at greatly reduced costs and help their customers build savings in the process. I believe this is a win-win solution.

Fifth, banks should take an active role in the debate over our nation's savings policy. Banks have a lot to offer in this process, and a lot to gain in returning America to a

nation of savers. For example, there have been proposals at both the Congressional and the state level to create Children's Savings Accounts, which would be seeded by the government and matched by contributions from parents. Many other countries have developed Children's Savings Accounts, the most noteworthy being the program adopted in Britain. What a wonderful way to start out life – creating a savings account at birth that can then be used when entering the world as an adult.

## **Conclusion**

As you can tell, I AM passionate about savings and I thank you for the opportunity to share my thoughts on ways to promote greater savings and wealth accumulation in American society. This is not an easy task. No doubt, the U.S. is a consumption driven culture and economy. But, as a banking regulator, I am committed to finding ways to encourage household savings and affordable credit alternatives. Congratulations, Cleveland, on doing your part through Cleveland Saves Week. I hope the rest of America follows your example.

And now, I will be happy to take your questions.

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