The Federal Reserve Board

Remarks by Vice Chairman Roger W. Ferguson, Jr.

Before the National Council on Economic Education, Washington, D.C.
May 13, 2002

Reflections on Financial Literacy

I am delighted to welcome the National Council on Economic Education and the Minneapolis Federal Reserve Bank to Washington. I want to commend your partnership and the important discussion you have organized for tomorrow. I also want to commend both institutions for their excellent leadership. In Gary Stern, President of the Minneapolis Fed and Chair of the NCEE, you have one of the most thoughtful, committed, and capable public servants I know. Gary is also one of the world's best economic educators and is deeply committed to making economic and financial education a priority in this country. I decided to take advantage of your presence tonight to speak about the benefits of economic and financial education and about why such education matters to the Federal Reserve. I also want to spend a few moments examining the importance of focus and clarity in our goals and expectations.

The Benefits of Education
I know that I could speak for much longer than you care to listen about why the understanding of economics and finance is crucial for individuals in a market economy. Knowledgeable and astute consumers promote competition among providers, which benefits us all. Personal financial security enhances individual well-being. Increasing national savings allows us to invest more productively for tomorrow. And, at a more fundamental level, our social fabric and national image are intimately connected to our material aspirations. The United States cannot be the land of opportunity unless all of our citizens have both the tools and the ability to use them to improve their lives and livelihoods.

As you may know, I have been trained both as a lawyer and an economist. I think the point can fairly be made that the most critical underpinnings of our society are the Constitution and our market structures. From my perspective, however, the education that we provide our citizens about the rule of law differs dramatically from what we provide about the functioning of markets. By the time I graduated from junior high school I had read the Constitution; not until much later did I study how prices are set in a market economy. This imbalance can and will be addressed by your work and that of many others. Fortunately, as my Federal Reserve Board colleague Ned Gramlich pointed out recently, changes in our financial system--including the increasing complexity and diversity of product offerings--have created consumer demand for improved education.

The Work of the Federal Reserve
The Federal Reserve has a special interest in economic and financial education and has for many years conducted teacher training and worked with partners like NCEE, Jump Start, and others to encourage programs aimed particularly at students, educators, and consumers. In part, these activities arise from the role the Federal Reserve plays in implementing the nation's consumer-protection laws. In part, they arise from the effective roles the Reserve

Banks play in their Districts as good public citizens. And, in part, they arise from the knowledge that our mandate to promote economic growth and stable prices requires public understanding and approval of the policies we implement.

Many Federal Reserve educational programs date from the period in which the Fed's efforts to fight inflation inspired an intense political and economic debate about monetary policy. The institution rightly joined in the debate and, among other things, decided to develop a nationwide public information program to increase the understanding of the functions, responsibilities, and policies of the Federal Reserve System. The designers of the program had the modest goal of offering information to the public so as to provide "a fair and sound basis" for judging the System's work, which seems quite modest by today's standard of "hype" and "hard sell."

Today, Reserve Banks and the Board continue to offer products and support to teachers and others who want to understand the Fed as an institution, but we also work very hard in the fields of consumer education and financial literacy training. For example, the Federal Reserve System is an active partner in the "America Saves" program developed by the Consumer Federation of America. The project was piloted in Cleveland, with the Cleveland Federal Reserve Bank being an active partner. In Chicago, the Federal Reserve Bank recently spearheaded a coalition of financial institutions and community partners to host an entire week of events to encourage financial education, connecting consumers directly to important resources in their community. The Philadelphia Fed is working with community groups and bankers to target financial literacy for adults. The Dallas Fed has developed a workbook on building wealth that banks are using with their customers and nonprofit organizations are using with their members. Currently, staff members from public information and community affairs offices throughout the System are working together to highlight the importance of financial education, increase consumer awareness of local educational opportunities, and encourage research into the most effective educational approaches to educating the public. I am very proud of the System's commitment to economic and financial education and of the support we provide to educators like you.

Let me make one additional point about the Fed's interest in economic and financial education. As Chairman Greenspan has said, "educated consumers are simply less vulnerable to fraud and abuse." And when millions of educated consumers make good personal financial choices, our economy is strengthened in fundamental ways. A strong and flexible economy means that resources are directed to the areas of greatest need, productivity and innovation are supported, and the ability to withstand shocks is enhanced.

Goals and Expectations

As policymakers and educators who believe deeply in the power and effectiveness of economic education, we must be clear about our goals and expectations. Such clarity helps us allocate our resources appropriately, target the areas of greatest need, and ensure a sustainable commitment to the most-effective educational initiatives.

Let me make a point that is self-evident. We certainly expect that economic and financial literacy can keep people from making uninformed decisions. But it cannot keep them from making bad decisions. Additionally, education will not always overcome circumstances. Unemployment happens to even the most financially literate, as do medical emergencies. Thus, though successful financial education programs will help individuals minimize or avoid the worst consequences of financial setbacks, education will not necessarily reduce the frequency of financial emergencies.

Also, education will not overcome human nature. Procrastination, for example, can heavily affect financial outcomes, and education may not overcome the tendency to put off financial changes. In a study of defined contribution plans by James Choi and others, one-third of self-reported undersavers said they intended to increase their savings rate in the next few months, but almost none actually made a change in their 401(k) savings rate. This finding amply demonstrates the value of bringing a variety of disciplines to bear in creating effective programs. Clearly, neoclassical economics, with its strong assumptions about rational decisionmaking, provides a helpful theoretical framework, but we will also need to rely on other models and frameworks to help us better understand how people process information and make decisions. The work of economists such as Richard Thaler on the benefits of "low-willpower" techniques to increase savings is an example in this regard.

Education is not likely to work if presented in a one-size-fits-all package, and it often works best when employed in conjunction with other targeted initiatives. This is particularly true for low- and moderate-income consumers. Research at the Board by Jeanne Hogarth and Chris Anguelov using data from the 1998 Survey of Consumer Finances indicates that 60 to 70 percent of households at the poverty level can be classified as current or usual savers. This finding should encourage those who are focusing their educational programs on the importance of savings because it reinforces the view that almost all households are able to accumulate assets. But as the researchers note, education is only one variable affecting savings. Income, age, assets, access to health insurance, and a host of other variables are at work. Education is important, but so are things like a steady job, good health, an economy growing at a sustainable rate, and the availability of tailored financial products to enhance financial well-being.

Sometimes our efforts will prove frustrating or appear to be failing, and in these cases we need to do everything we can to understand the failure and learn from it. Recently, the Jump-Start Coalition for Personal Financial Literacy released results of its third study of financial literacy among high-school students. Surprisingly, despite the increasing availability of literacy programs, the results indicated a declining level of understanding of basic financial concepts among surveyed high-school seniors. Such findings make the case for more research into desired competencies, learning styles and preferences, and program effectiveness.

Finally, we know that education will not be successful in an environment in which credibility and trust are lacking or in situations in which the self-interest of the educator are undisclosed. Transparency is as critical in the education market as it is in others.

Conclusion

In sum, I believe that increased education about how our markets function, about economic and financial concepts, and about ways to build financial security is crucial to our individual and national well-being. At the same time that we encourage interest and participation in educational programs, we also need to be clear about our goals and expectations. We must continuously encourage research to identify programs that work, and we must use what we learn to develop improved approaches.

Return to top

2002 Speeches

Last update: May 13, 2002, 8:00 PM