SPEECH

Stewart: The Growing Importance of Financial Literacy Education

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Jamie B. Stewart, Jr., First Vice President and Chief Operating Officer

Remarks by First Vice President Jamie B. Stewart, Jr. before the New York State Banking Department I would like to begin my comments this afternoon by congratulating the New York State Banking Department for planning this timely and important program. Thank you, Superintendent McCaul, for giving me this opportunity to offer a central banker's perspective on why efforts to improve financial literacy are important.

Most members of the public associate the Federal Reserve with the formulation and implementation of monetary policy, the most visible link between what we do and their daily lives. By adjusting the money supply and the level of short-term interest rates, the Fed strives to make the economy as strong as possible for as long as possible. The Federal Reserve also has responsibility for promoting the safety and soundness of the nation's banking system, working closely with other agencies, such as the New York Banking Department. Less well known to most of the public is the Fed's role in the payments system – to assure the reliability and integrity of all means of payment.

With so many economic and financial connections to the public, it is important to the Fed for individuals to understand what it does and why it does it. Improved knowledge and understanding help to build support for our monetary and supervisory policies; they also help individuals to make better economic and financial decisions on the job, at home and in their community. We consider efforts to improve the public's understanding to be squarely within the mainstream of our work as central bankers.

For half a century, the Bank's series of cartoon-style booklets has been a useful tool in our effort to help the public understand the nation's complex economic and financial environment. The New York Fed also distributes more than a million booklets and thousands of videotapes annually on a wide range of economic and financial topics, and we rack up an average of more than 900 thousand hits on our website each month.

During the 1990s, we greatly expanded our educational outreach efforts by putting in place professional development programs for educators, writing curricula, organizing educational programs and competitions for students, and advising educational organizations on program development. We've been busy.

I have been asked many times why the Federal Reserve devotes so many resources to improving the public's economic and financial literacy. In the few minutes I have with you this afternoon, I would like to discuss four observations that guide our mission.

Observation #1: The financial well being of individuals is linked inextricably to the nation's economic progress.

Throughout the 1980s and 1990s, economic policy makers got frequent reminders that the personal financial well being of most individuals increases when the economy is strong and financial assets are rising in price. The causality runs both ways, however-- the economy and our financial institutions are stronger when more people have jobs, rising incomes and a buildup of wealth. Financially strong households tend to have higher levels of confidence about consumption and are more willing to make the major purchases that advance our economy. In addition, financially successful people inject savings into the banking system; they also are more able to make use of credit to start the small businesses that provide jobs and income to millions of people.

For most people, having a job and earning a paycheck are the keys to personal financial well being and independence from the government's social safety net. Yet being able to earn a paycheck is not the same as being able to make informed and wise judgments about what to do with money once it reaches your hands. It is at that point when the financial literacy and competence of household members are given their first fundamental test. According to numerous surveys, most workers, particularly young ones, fail that test---and the consequences are severe.

One manifestation of this failure is in the growing debt loads and credit difficulties of our citizens. For an individual, failure to use credit wisely can foreclose opportunities and result in future financial distress. For the Fed, systemic breakdowns in the credit process create problems that slow down real economic growth.

With this in mind, my Bank has supported the efforts of JumpStart, Operation Hope and other organizations to promote improvement in overall financial literacy, particularly among young people. In 2000, one of my New York Fed colleagues served as chair of the New York State JumpStart Coalition, which included four dozen organizations concerned with promoting awareness of the benefits and risks of consumer credit and other financial literacy concerns.

#2: Financial literacy among individuals results in more stable communities and a stronger, safer banking system.

Improved financial literacy has been a pathway for millions of individuals and their families to accumulate assets and achieve their financial goals. One positive spillover from that process is greater economic and financial stability in communities. Banks contribute to that stability by providing appropriate credit to entrepreneurs and households, and by financing the construction and renovation of housing. As a regulator, the Federal Reserve helps by monitoring bank's compliance with laws requiring them to offer credit and other banking services legally, fairly and impartially. We enforce these laws vigorously. Meanwhile, financially literate customers help the banking system by buying a wider array of financial services. The result is greater efficiency, lower fees, better services, and a safer, sounder banking system.

We also work with numerous community development organizations dedicated to the physical revitalization of neighborhoods. The Fed, along with many others, informs individuals and groups about how to improve their credit histories, reduce debt and create household budgets. We do this so that they can become homeowners and thereby improve their neighborhoods and their own financial success through home equity appreciation.

#3: Improved financial literacy, particularly early in life, results in a higher standard of living for households over the long term, including retirement.

When you come down to it, the most fundamental reason why people should strive to become more financially literate is to help them to reach their personal financial goals. Whatever the specific goal, the payoff to financial literacy is an improved standard of living and a sense of confidence about the future.

Financially literate individuals are more likely to engage in sound financial planning, even casually, early in life.This enables them to plan for retirement, fund the education of their children and accumulate more assets. From a national perspective, the payoff is large. With the baby boom generation approaching retirement age, the potential dependence of additional millions of senior citizens on social security and other parts of the government's social safety net may pose a very expensive fiscal dilemma for the federal government. Clearly, too many Americans are unprepared to maintain their standard of living in retirement.

#4: Gaining financial literacy is a long-term process that, for most people, requires the assistance of institutions outside the home.

Sadly, too few people understand compound interest, investment strategies, risk assessment, insurance and other basics of money management. Most people don't realize the benefits and the costs of credit or the role that home ownership plays in helping to accumulate wealth.

The roots of the problem are not hard to find. Most people acquire their financial knowledge haphazardly, by trial and error. Numerous surveys reveal that most people growing up do not learn any principles of personal finance systematically from their parents.

Instead, they pick up bits and pieces in school, from the media, and through their business dealings with financial service providers. Often, the information they acquire is misleading or fraught with errors. This message was reinforced in a story in Tuesday's New York Times about a new survey that found that "Adults avoid talking to youngsters about budgeting, saving and giving to charity in much the same way that they recoil from advising them about sex. Their reticence," the survey found, "stems partly from a failure to practice what they preach."

One way to begin to eradicate haphazard learning is through the introduction of financial literacy concepts early in the education of every child. In this context, the Federal Reserve Bank of New York is committed to continuing its program of working to promote financial literacy through the schools. Here are just a few examples of our recent efforts:

- In the last two years we have coordinated a drive to preserve economics as a mandated course in all New York State high schools.
- In 2000, at the request of the Department of Education, New York Fed staff wrote the syllabus from which the State Department of Education is currently writing the economics curriculum to be taught statewide beginning in September 2001.
- New York Fed staff, in collaboration with other organizations, has begun an intensive professional development program for high school economics teachers to prepare them for the new curriculum.

In conclusion the New York Fed is committed to continuing its active involvement in financial literacy. We believe this program is important in our official role as the central bank responsible for the economic well being of people in all communities. We also believe that financial literacy is the right thing to do, because we live and work in New York and want our fellow New Yorkers to lead financially successful lives.

Thank you very much.