Grohmann, Antonia; Wittenberg, Erich

Article
"Many people have inadequate understanding of basic financial concepts": Seven questions to Antonia Grohmann

DIW Economic Bulletin

Provided in Cooperation with:
German Institute for Economic Research (DIW Berlin)

Suggested Citation: Grohmann, Antonia; Wittenberg, Erich (2015) : "Many people have inadequate understanding of basic financial concepts": Seven questions to Antonia Grohmann, DIW Economic Bulletin, ISSN 2192-7219, Deutsches Institut für Wirtschaftsforschung (DIW), Berlin, Vol. 5, Iss. 30/31, pp. 413

This Version is available at:
http://hdl.handle.net/10419/113235

Terms of use:
Documents in EconStor may be saved and copied for your personal and scholarly purposes. You are not to copy documents for public or commercial purposes, to exhibit the documents publicly, to make them publicly available on the internet, or to distribute or otherwise use the documents in public. If the documents have been made available under an Open Content Licence (especially Creative Commons Licence), you may exercise further usage rights as specified in the indicated licence.
SEVEN QUESTIONS TO ANTONIA GROHMANN

»Many people have inadequate understanding of basic financial concepts«

1. Ms. Grohmann, some people make considerably poorer financial decisions than others. Where exactly do these people experience difficulties? Many individuals make poor financial decisions, particularly when it comes to saving for retirement. They don't start planning early enough and consequently don't save enough to provide them with financial security in old age. They underestimate how much money they’ll need when they retire and how long they’ll live and so fail to put sufficient funds aside. Another problem for some people is that they run up too much debt. In terms of financial investments, we see the main type of asset most people invest in is an owner-occupied property or they own stocks in the company they work for, whereas a more diversified portfolio would be more sensible.

2. What are the reasons for poor financial behavior? Many people’s financial literacy is too limited and they have an inadequate understanding of concepts such as interest, inflation, or risk diversification. One reason for this could be poor numeracy skills or that their parents failed to teach them how to manage money at an early age. Poor schooling might be another reason.

3. Which factor has the greatest impact? Our study focuses specifically on childhood variables. This enables us to demonstrate that people whose parents encouraged good financial behavior at a young age are more financially literate and have a better grasp of financial concepts. Our study also shows that a better education generally and studying economics in school have a positive impact on financial behavior.

4. What are the financial literacy levels among the German population? There are certainly people who have an insufficient understanding of basic financial concepts. The problem is that these people are often precisely those who need this knowledge the most, in other words, low-income groups with a limited school education.

5. All German Länder have now integrated financial education into the school curriculum. What impact has this had? In my view, it’s still too early to answer this with 100 percent certainty. It will only become evident when the students whose education included financial studies reach adulthood. Only then will there be any clear findings. However, there are short-term scientific studies on school students which demonstrate that financial education in school improves financial literacy. Yet the studies also show that these school courses have no impact on saving behavior.

6. What form should financial education take in Germany? Studies have shown that teaching simpler concepts or rules of thumb is often more effective than desperately trying to explain how to calculate an interest rate. How to structure these courses and financial education in general definitely requires more research. It certainly makes sense, however, to teach school-age children how to manage their own finances. School is essentially the only place where policy-makers can still reach everyone with relative ease. It’s clearly much more difficult to influence how parents raise their children. Although there are certainly potential ways of drawing parents’ attention to the fact that financial literacy is crucial for their children’s future financial behavior, whether or not they actually do anything about it is quite another question.

1. What is the situation in other countries? Other countries face a similar predicament. On the whole, financial products have become increasingly complex and are difficult to understand. Additionally, social security systems in countries such as the US and also in Europe have been subject to more and more cutbacks. Consequently, the individual is now expected to bear the primary responsibility of putting money aside for their own retirement, for example. In my view, this is a trend that can be observed in many industrialized nations. The financial products available in developing countries, however, are far more straightforward. Nonetheless, financial literacy is still important in these countries to ensure that people know how to manage these products properly.

Interview by Erich Wittenberg