

Vidzeme University of Applied
Sciences



Improving Financial Literacy at School: a Way to Ensure Retirement Well-being

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Florence 2015

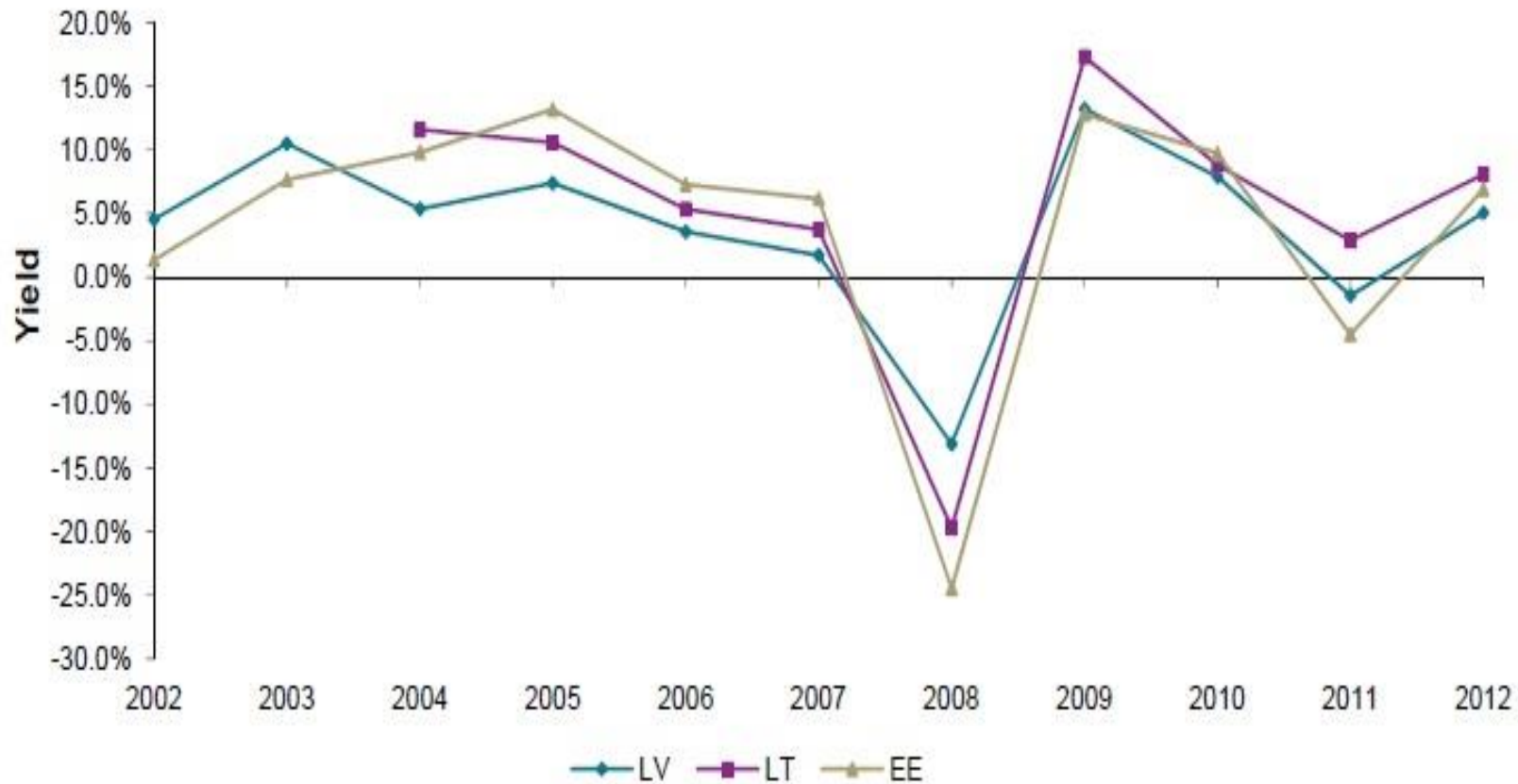
Do knowledge matter?

- One of the roots of the global financial crisis was that the sellers of financial products often had a better idea of their riskiness than did the buyers
- Chairman of the U.S. Securities and Exchange Commission:
 - more than 50 percent of Americans did not know the difference between a stock and a bond
 - individuals are generally badly informed about complex pension products. Many do not understand basic concepts in finance
 - distributional implications: the worst-informed people are disproportionately among the least well off → inappropriate products being sold to ill-informed consumers

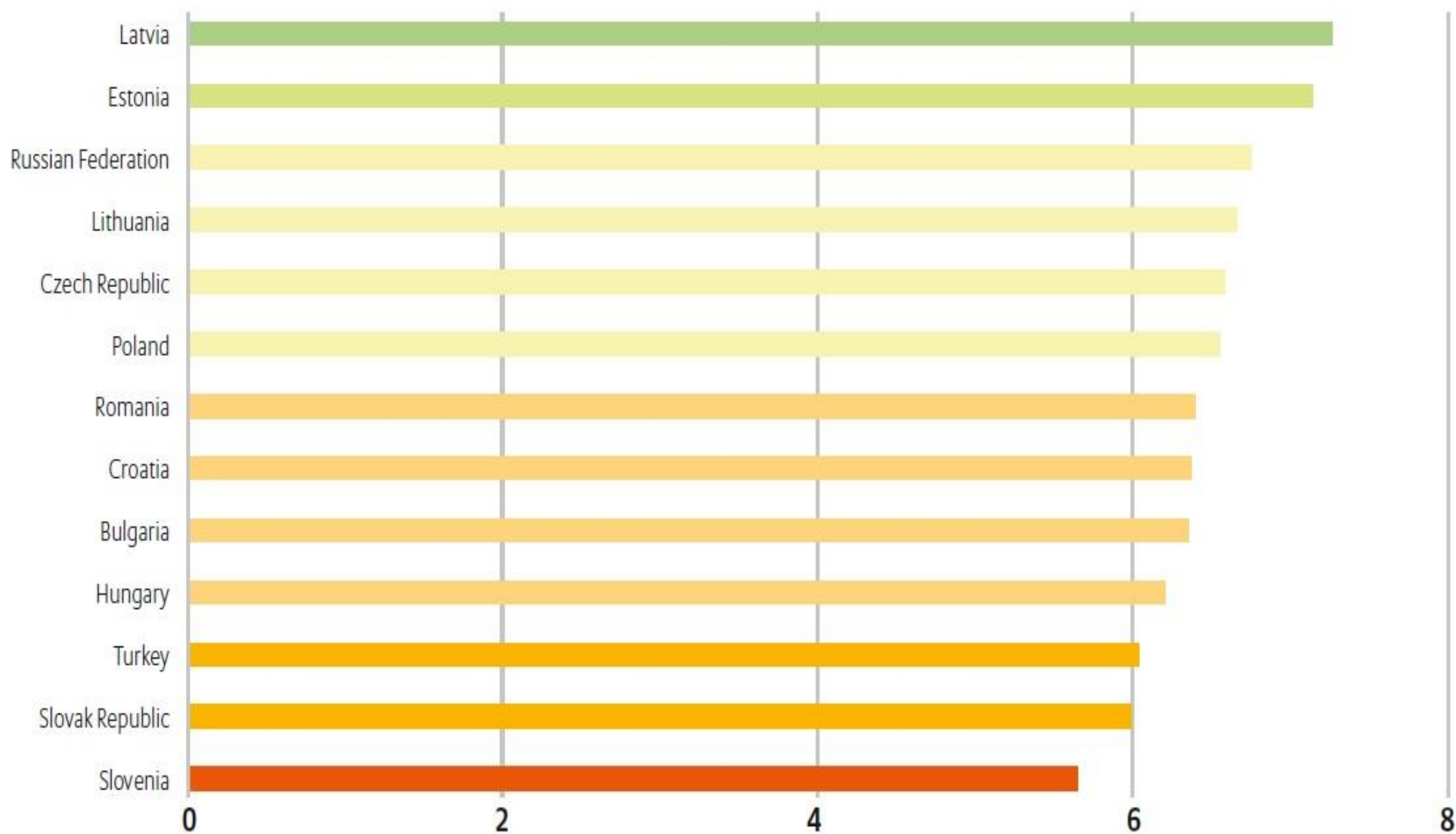
Pension system in Latvia

- On of the first countries to introduce notional defined contribution multi-pillar pension scheme
- Three tier pension system
 - State funded pension scheme (SFPS) → «money makes money»
 - Total value of assets : ~2,202 bn. € (9% of GDP)
- Number of participants (02.06.2015.): 1 240 231
- 1st pension pillar: 15% (2016 – 14%)
- 2nd pension pillar: 5% (2016 – 6%)
- 20 pension plans:
 - 8 active plans (up to 50% of investments in shares);
 - 4 balanced plans (up to 25% of investments in shares);
 - 8 conservative plans (investments in shares are not allowed);
- Performance (1 year): from 2.21 % till 11.42 %

Crisis impact on the 2nd pension level (Baltic States)



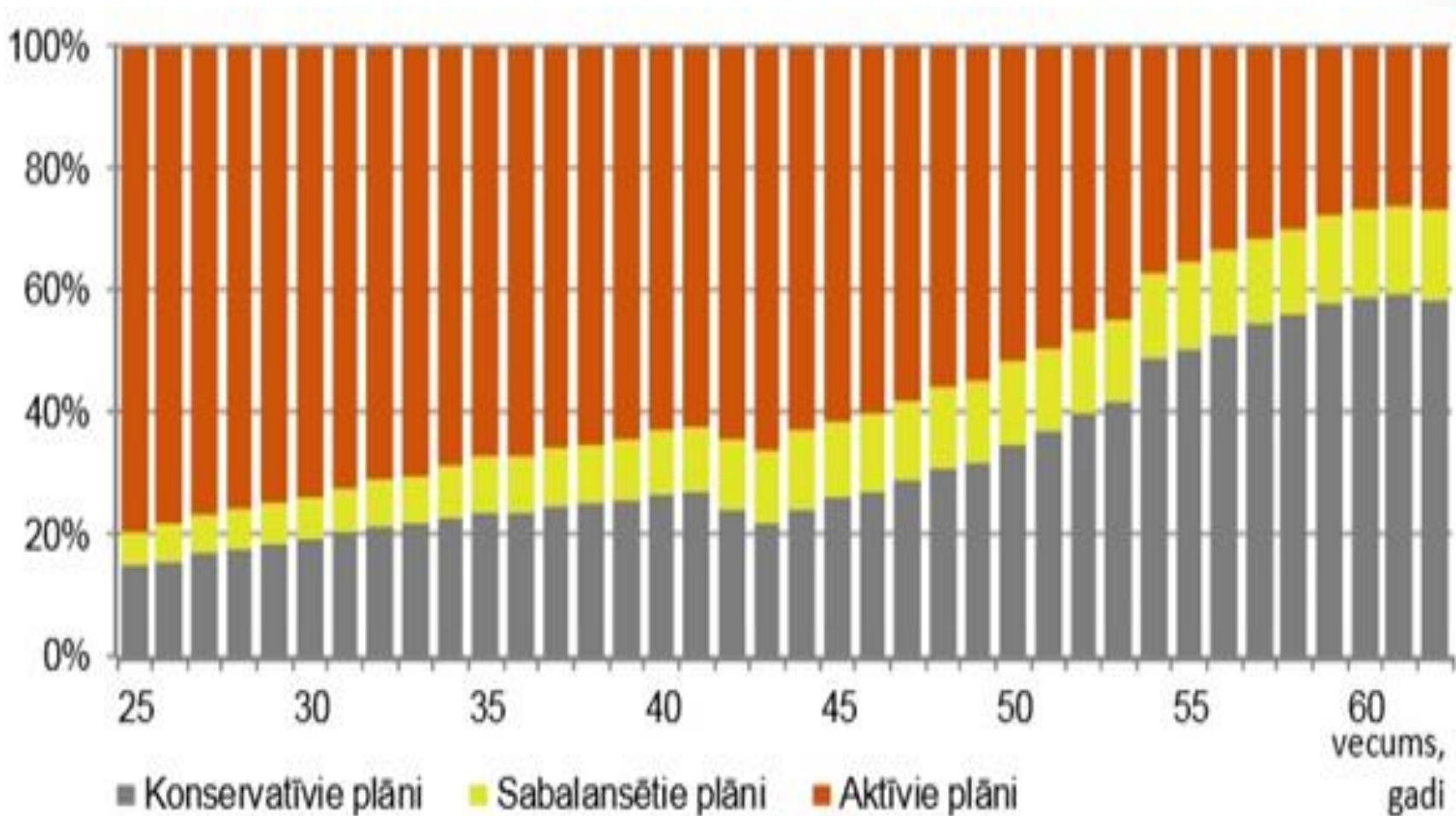
Pension Sustainability Index 2014: Central and Eastern European Countries



* Scale from 1 – 10: 10 minor need for reforms, 1 high need for reforms

Source: Allianz Asset Management, International Pensions

Number of participants (%) in various pension plans



Pension fund administration costs and their impact on pension savings

Administration costs (from the total value of assets)	Impact on pension savings
0,05%	2%
0,15%	5%
0,25%	8%
0,50%	15%
0,75%	22%
1,00%	28%
1,50%	39%

Financial literacy (OECD)

- a combination of knowledge and skills necessary to be aware of and effectively manage personal finances, make informed choice of financial services and their use, ultimately ensuring private financial stability and sustainability.
- financially educated people have knowledge of finances and economics and they are capable of using it for enhancement of their future wellbeing and financial growth, in order to achieve individual financial objectives.

Is there a financially literate society in Latvia?

- Shift of responsibility from state to individual → financially literate society as a precondition for SFPS to be successful;
- 2014 first nationwide financial literacy survey in Latvia:
 - Overall score: 20,6 of 99
 - Worst indicator: pensions(-0,5)
 - 75% are not sure they will have sufficient pension income
 - 82% will completely rely on pension
 - 75% do not follow-up the performance of their pension plan
 - 42% change pension plan under influence of commercials or bank employees
- No guaranteed return rate → since 2015 a performance based administration rate

Promotion of financial literacy at school

- Advantages:
 - Possible to reach out to the widest possible auditorium from various backgrounds;
 - Have not developed particular behavioural patterns (dealing with financial services).
- In Latvia at high school currently “Economics” is an optional subject at high school → less than 40% learn it;
- At secondary school part of the Social Sciences (along with ethics, health education, civics);
- Teachers lack time to discuss personal budgeting and other finance related aspects
- 73% believe that the financial knowledge gained at school is insufficient

Promotion of financial literacy at school I

- Only 10% of parents and 6% of pupils think, that economics is the most important subject at school:
 - Do not understand, where the knowledge gained can be practically used;
 - Methods applied to teach this subject do not meet the needs and expectations of the students;
 - Parents did not have it at school → a bias, that one can successfully carry out their everyday financial activities without applying any specific skills

A way forward

- National financial literacy strategy for the period from 2014 to 2020:
 - need for improvement of financial literacy;
 - «Economics» must become a mandatory subject;
 - Change the curricula, which is overloaded and includes many topics which has no or very limited connection with everyday financial issues;
 - Decentralize the examination process;
 - Additional training for teachers → more active involvement of asset management companies

Alternatives

- «Choose not to choose» or make inappropriate decisions → may not be able to multiply their savings effectively or even lose pension capital;
- Implementation of the National financial literacy strategy → time consuming, unknown results in future
- Alternative solution → life-cycle investment strategies
 - To minimize risks caused by poorly made investment decisions;
 - To allocate greater resources in pension funds with higher risk level → in long term more profitable, higher human capital;
 - Gradually move the pension capital to safer financial instruments → pension capital is at greater risk before retirement age.

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