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Financial education for investors

Ladies and Gentlemen,

I do commend IFIE (the International Forum for Investor Education) and IOSCO for having jointly organised this conference on Investor Education. Financial education will indeed be one of the major challenges in the years to come. Be it in emerging or developed countries, all retail investors need to have an appropriate level of understanding of the financial environment they live in, in order to take decisions that are suitable to their situation in terms of risk performance and return.

As early as 2005, the OECD published a series of noteworthy recommendations on the topic of financial education. The European Commission and the European Parliament have also been addressing this issue. In April 2007, the Commission published its Green Paper on retail financial services and the

Parliament adopted a report on financial services policy on 11 July 2007. They agree that more needs to be done to promote a high standard of financial education and have asked member states to assume their responsibilities. The Commission has also said it is willing to prepare guidelines and encourage the exchange of best practices.

The movement is, therefore, underway. The IFIE has already launched a compelling project to review the various strategies and programmes that exist in this field. The project, which covers only 11 countries for the time being, must continue.

But things are moving quickly. An increasing number of countries are launching programmes and taking initiatives in the field of financial education. I am quite sure that, after this conference, the initiatives taken by the UK, Italy, Hungary, the Netherlands and Ireland will all be talked about. I am equally sure that Paris-based Institute for Public Financial Education will also figure prominently among the initiatives taken in France.

In 2004, a working group set up by the AMF, detected a significant need in this area. According to a survey conducted by TNS Sofres in December of that year, French people are largely unaware of financial issues, as shown by some examples:

three out of four French people admit that they know little about finance;

more than one in two consider that they are not sufficiently qualified to choose financial products;

more than two-thirds of the population find the world of investments complex.

The findings of the working group resulted in the formation of the Institute for Public Financial Education (IEFP) in April 2006.

The IEFP is a not-for-profit organisation made up of representatives from the public sector, such as the AMF, the Banque de France and the Ministry of Education; private

partners, including professionals, investor representatives, consumer associations and trade unions; and members of civil society, including journalists, researchers and magistrates. We thought it essential for all these stakeholders to joint forces in a effort to help the French acquire the basic financial knowledge they so clearly lack.

- Why? And why now? What has changed that affects the populations of France, Britain and India alike? And what are the factors in Europe and elsewhere that justify an effort in this field now?

Financial education is important for reasons that are both deep-seated and long-lasting.

For the most part, savings and investment are still determined by people's life cycles and income. But the growing use of financial services throughout our lifetimes, in particular in order to fund our retirements, and the interdependence between

investment and debt – for example, when buying a house – are increasingly common features of modern life.

The various types of savings and investment are changing too. Just a few decades ago, in some European countries, savers had the choice between a limited selection of products that differed only in terms of rates of return and investment horizons. Today, savings are increasingly invested in financial assets such as securities and collective investment schemes. What distinguishes these products from each other is their risk/return profile. Products are more complex and ever more sophisticated. Moreover, this is a significant trend that must guide the action of regulators, since risk is being transferred to the saver. The Caveat emptor principle is nonsense if the emptor is unable to make a proper judgement.

Current events have also demonstrated why financial education must become one of our top priorities. In addition to the need for more transparent information and improved safeguards to

protect ill-informed consumers, the subprime mortgage crisis has illustrated why ordinary people need to acquire the basics that will enable them to understand the whys and wherefores and, thus, to avoid further crises in future. Current events also provide an opportunity to think hard about our pensions. Over and above an inevitable reform of contributory schemes, we must also make an effort to educate consumers as a whole so that they become familiar with funded pension products.

- In view of what I have just said, what targets should countries set themselves for their financial education programmes?

The programmes and the underlying concepts reflect a degree of diversity in points of view. We do not feel that this is simply a matter of focussing on information about financial products. Clear, understandable and fair information is obviously essential. A good deal of progress can still be made in this area, and we are working on it. But this will not be enough, particularly since

products change quickly and innovation creates plenty of new ones. Nor should we seek to turn everyone into a professional investor specialising in finance and its increasingly sophisticated workings. The challenge lies elsewhere. We need to provide genuine education in every sense of the term. As the admirable definition of education given by UNESCO many years ago states, it is a matter of "*Learning to know, Learning to live together, Learning to do, Learning to be*".

The main target that we must set for education is to help savers to take their own decisions on savings and investments, to help them to take budgetary and financial dimensions into consideration as they go through life. We must strengthen their capacity to assess the products and services on offer and to decide which products best suit their projects and needs. We aim to improve consumers' understanding and their ability to make the right choices, to strengthen their "market power" and their capacity to make the most of competition, which does not depend solely on economic structures. To achieve this, we

need to know where the right information can be found and what are the right selection criteria for our individual situations. It comes as no surprise that French consumers rarely make comparisons between the financial products on offer and that they do not bring competition into play when making investments. This behaviour stems from their lack of self-confidence in financial matters.

The problems are different in emerging countries where the savings rate is generally very high but where dire poverty still exists. Countries like the United States or the United Kingdom are different again, with high levels of household debt and low saving rates. In countries like France, debt levels are not especially high on the whole and the average saving rate remains elevated, even if it is on the decrease. The main question is how do individuals take on financial risks? For savers who do not limit themselves to savings accounts or investments with guaranteed returns, diversification appears to

be insufficient and there is a strong trend towards procyclical behaviour. This exposes households to inefficient investment of their savings and a potentially unfavourable risk/return profile. This is not a good thing for individual savers, who suffer from underperforming long-term investments, or for key economic balances, since it raises the issue of how to finance growth.

Some people doubt whether financial education can strengthen the ability of consumers and bring about behavioural changes. According to this view, education will always be one step behind complex developments and financial innovation. And behavioural biases mean that, when it comes to money, we are, and always will be, not entirely rational. We are fully aware of all these issues, but I repeat that we should not attempt to transform everyone into a professional financier. While education is not enough to solve every problem, it can help to improve our sense of judgement and encourage more rational behaviour.

We also need to mention the sometimes poor image of finance and the financial markets. This image is all the more harmful given that an innovative and competitive financial sector can make a significant contribution to the growth and employment that governments are so keen to achieve. Against this backdrop, financial education must help people to better understand the workings and the benefits of finance. It must educate consumers in the financial economy.

- What are the priorities and guidelines for financial education?

A review of the programmes and initiatives that have already been taken reveals a broad swathe of differing methods and organisations. The positions and the roles of the public sector (regulators and governments), professional associations or financial institutions differ according to national culture and history. There is plenty of room for the efforts and the

contributions made by all stakeholders and there is no single model, apart from the need for cooperation and synergy.

For example, in France, the savings banks, family affairs associations and the public sector have organised educational programmes in personal finance for certain constituencies.

Basic education programmes in stock market investing, developed by Euronext, have been taken over by the French federation of investment clubs. In addition, the banking industry association has opened a consumer-oriented website. But, in view of the scale of the problem, these initiatives are far from sufficient.

Any and all activities to promote public financial education should be supported by all kinds of organisations and associations, they must be editorially independent and must not aim to make a profit. In this way, they will remain neutral and objective.

The programmes that will be developed must meet the need for information by developing educational tools accessible to the greatest number. Web-based platforms and interactive tools that can be easily updated are an obvious solution, without forgetting hardcopy materials, forums, conferences, conventions and television programmes.

The initiatives must be suited to anyone who wants to understand financial issues or improve their financial culture. This affects every one of us, throughout our lives. Nevertheless, our priority must remain action for young people, their parents and educators, employees and economically active people, who are concerned mainly about how to finance their pensions, and consumers who, as customers of financial institutions, want to understand what is on offer and to be able to talk about it.

- I would like to make some comments on these three top-priority targets.

Let's start with young people. Obviously, it is essential that they acquire the basics of a financial culture and the wherewithal to manage their own finances as early as possible.

An introduction to money matters and personal finance should clearly be taught in school. We are already living in a world where we need to understand and command the basic financial tools used to build our private and professional futures. Our children will need to understand these tools better than us. We must make the effort to convince everyone that this is necessary. In many ways, there are more opportunities available now than a few years ago. For example, the "common core of knowledge" promoted by the European Union provides for the acquisition of knowledge and skills by students. This presupposes an understanding of the concepts of personal finance: notions of budgets and risk must be understood, just like the history of trade and currencies or the concepts of interest rates and percentages.

While it is clear that financial education will never be included in school curricula as a subject in its own right, it must be introduced into other subjects, such as mathematics or history and especially economics or management.

Education about pensions is a primary goal, especially for employees and all economically active persons. There is no need for lengthy arguments. In some parts of the world, the population is getting older. By 2050, this trend will have become widely entrenched, and painful reforms will be necessary.

First we have to explain why it is necessary to save for one's retirement in a national context where there is broad agreement that pay-as-you-go is the backbone of the pension system.

Surveys conducted all over the world show that a significant majority of people are concerned about their pension, that they have no idea about their future income and that they are

worried that it will not be enough. But less than half of the survey participants are saving or plan to save for their retirement.

An effort must be made to explain the specifics of long-term savings. All too often, financial investments for retirement are classified in the following order: buying your house, investing in savings passbooks and then life insurance. Few savers invest in equities with a view to funding their retirement.

Financial education must attempt to convey a number of important messages on the risk/return profile and the correlation between good returns, risk mitigation and the investment horizon. Once consumers are better educated, they will be able to put pressure on the financial sector to obtain simple products that meet their needs.

In addition to the educational documents that are made available on specialised sites, we should also think about

initiatives that will help promote financial education in the workplace, with a focus on workplace savings schemes. In every respect the workplace seems to be the right place, and the timing is right. Employees who work in companies with profit sharing schemes and incentive schemes are faced with difficult choices. Should they simply invest in a savings fund? And in which fund should they invest their profit sharing income?

In the relationship between consumers and financial organisations, informing, advising and educating consumers are one and the same thing. Improvements must be made in every one of these fields. I think that we should highlight a number of initiatives that have been taken in Europe. The implementation of the Markets in Financial Instruments Directive (MiFID) should pave the way for progress in terms of information about products and the quality of advice provided by professional consultants.

MiFID also strengthens obligations in terms of information and advice. A set of precise rules will apply to general information for customers, the required quality of all information and the time when the information is supplied.

Information of any kind must not promote the advantages of a product without explaining in a very clear manner all the associated risks. The information must be understandable for the average investor in the category for which the product is intended. But the actual improvements for consumers will be limited if they themselves are not well informed about financial products and processes.

The directive also strengthens and expands the obligation to provide advice. An intermediary will be required to assess customers and potential customers in order to make sure that the financial services and instruments on offer are suitable. To do this, the intermediary must obtain certain information before the service is provided.

This obligation applies not only to requests for advice from customers, but also to all "active" individual sales made further to a personal approach by the salesperson. On the other hand, it does not apply to execution-only of a buy order placed at the behest of the customer. At most, this gives rise only to a duty to alert the customer if the order does not match his financial experience and skills.

These measures obviously demand a dialogue between the customer and the advisor cum salesman. Customers must answer as exactly and precisely as possible all questions asked by the advisor about their financial situation (disposable income, saving capacity, liquid assets, financial portfolio and, where appropriate, real estate assets). Customers must also respond to questions about their investment projects, giving details about their precautionary saving or project funding, investment horizons, and preferences with regard to risks or security.

If the customer fails to reply or replies too vaguely, the intermediary can and must refrain from making recommendations. In this case, savers are entitled only to the execution of a buy order, placed at their own initiative and for which they are wholly responsible.

Savers must be capable of clearly expressing their projects and, beforehand, properly managing their budget. So their financial education must be improved. In the short term, they need clear and understandable information about the existing system and the new resources that will be available, but also about their new responsibilities.

Closing remarks

Financial education is a long-term project. Financial education aims to raise the level of general understanding of this discipline and to teach everyone "the three Rs" (reading, writing and arithmetics) in the field of finance. The first step consists in increasing awareness of this pressing need and of the scale of resources that must be deployed. Then we have to get down to work. I am a natural optimist. Politicians, professionals, the general public and consumers are all becoming increasingly aware of this need. But we must continue our efforts if we are to progress further. We must continue to insist on the fact that financial education does not replace regulation, but exists alongside regulation. By the way, the more educated the investors, the less burdensome regulation! I prefer to have my cake and eat it too, rather than choosing between them.