Crossfire: 'Building financial capabilities should be product-linked and not focused on personal money management'

KATHLEEN STACK and JENNEFER SEBSTAD

In this issue's Crossfire, *Kathleen Stack and Jennefer Sebstad debate whether a product-linked approach is the best way to deliver financial education.*

Dear Jennefer

Given our close work together on the Steering Committee for the Global Financial Education Project, it is a bit odd to be on opposite sides of this debate about the best way to deliver financial education. This is especially the case because we both agree on the power of financial education to make a difference in the well-being of clients and the performance of financial institutions.

But, I do not agree that the product-linked approach is the best way to deliver financial education. In this model, financial institutions teach financial education in relation to a particular product offering. This is popular among some these days because of the belief that the approach creates a stronger business case for financial education. So, if you educate clients about a particular loan product, the reasoning goes, they are more likely to use it. That is, education about financial products will increase product uptake and use, and the resulting increase in revenues to the institution will have a positive effect on its bottom line. This approach misses an important purpose of financial education which is to provide people with the basic skills for personal financial management to make informed decisions about managing their money and good choices about the full array of informal and formal financial options available to them.

The product-linked approach seems focused primarily on formal financial institutions. Furthermore, it looks like marketing to me. It teaches about financial services with a specific focus on the features of products offered by the financial institution. The goal is to promote the product to the existing or potential client. The product promotion approach may result in a client using a financial product that she doesn't need or that is inappropriate for her. It can be a conflict of interest for the institution and go against the principles of client protection.

And, is it true financial education? The ultimate goal of financial education should be to build consumers' financial capability to plan for and manage their own changing financial requirements to meet both their long- and short-terms goals. Otherwise they will scramble

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endlessly to keep up with day-to-day requirements, problems, and crises. Equipped first with financial goals and objectives, a better understanding of their own financial management needs, and knowledge about formal and informal financial services options, consumers can make the best use of education about specific products and services. They will know how to ask questions about these products and services and make informed decisions about the ones that best meet their requirements.

Financial education should teach the full array of financial management skills for consumers including budgeting and saving, how to manage debt, access insurance, manage remittances, use agents, and how to use bank services, including agent- and electronic banking where available. It should also teach consumers to know their rights and responsibilities as financial services customers.

If financial education starts with a formal financial institution that wants to sell a particular product, how will consumers learn about all the different products that may be available in the market place? How will they be able to judge whether a loan product from the financial institution delivering the education is better than a loan product available from a different institution? And, how will they decide what is the right product for them given their financial goals and financial management requirements? Perhaps they need to save more rather than use a loan. Perhaps they need insurance. Product-linked financial education likely will not provide enough information for clients to know all their choices.

If financial education is product-linked, what happens to the vast majority of people who do not have access to formal financial services? For example, in 2011, only 14.3 per cent of the population of eight countries in the West African Economic and Monetary Union had access to financial services (CGAP, 2013). With a product-linked approach this population will be excluded from financial education.

Although the jury is still out on the effectiveness of financial education, there is widespread interest in the developed and developing world alike for increasing access to financial education to build financial capability for adults and children. A product-linked approach will limit not only the numbers and types of beneficiaries of financial education, but the breadth of financial knowledge and skills that can empower people to improve the financial well-being of themselves and their families.

Kathleen

Dear Kathleen

While we both agree on the power of financial education to improve the lives of people and the performance of financial institutions, at long last we've found something we disagree about – delivery. You've argued against linking financial education to specific formal financial products because: 1) financial institutions are only interested in marketing their products, even if they may not be the best product for the client; and 2) there is a conflict of interest between product promotion and financial education because financial education should be about helping people make informed choices about a broad range of financial services, not just a particular product.

I would take a different angle in looking at the merits of linking financial education to products.

First, there are very few financial education programmes at all, and you have to start somewhere. While financial service providers don't have to be the only delivery platform, why not use microfinance and other institutions reaching large numbers of the poor as a platform for financial education, especially if such education is in line with both their social and financial performance objectives? This is an efficient and cost effective way to target large numbers of low-income people at a 'teachable moment'. Financial service providers are going to spend money to market their products anyway, why not spend it on educational marketing, a way that benefits clients more than a flashy TV commercial or promotional event? Embedding the principles of good financial management into marketing messages is a cost-effective approach for reaching large numbers and for repeating simple messages – two things with potential for impact. Also, financial education is a great way to get banks closer to their clients, to learn about their financial lives, and their financial service needs and opportunities.

Second, product-linked financial education provides an immediate opportunity for people to apply what they learn through financial education. Financial education in tandem with adopting a new or improved financial product, provides the perfect opportunity to put new knowledge or skills into practice. One could argue there is more efficiency and potential for impact for this kind of financial education and it can be tailored to the particular product. Here, I agree that we should look beyond just credit and loans to a broader range of products including savings, insurance, and remittances. Designing financial education around the challenges of building financial assets (through savings), managing risk (through insurance), and making the best use of irregular or lumpy sources of income (through remittances) is what people need – and this is all product linked! Understanding not just the immediate use of financial products, but the financial goals of clients and how these products can be used effectively to better achieve these goals is what financial education should be all about. I guess I'm arguing that using a range of financial products and services as the entry point, not just the end point, for financial education would seem to make good sense.

Third, I would argue that the sum is greater than the parts in linking financial education to products. For example, if someone learns how to do a simple budget projection, to figure out how to set aside money for a loan repayment, they have learned how to calculate their total income, expenditures, and balances – fundamental principles of money management they can apply well beyond the product in question.

Fourth, with regard to reaching people outside the formal banking system with financial education, perhaps we can think more broadly and creatively about other types of products and services that they *do* use, as market actors. For example, even if people are unbanked, they will use health products and services – health clinics and pharmacies could be another entry point for financial education. Many rural people use agricultural inputs and services – input distributors, retailers, and agents selling these products and services (yes, often on credit!) could be additional entry points for financial education. The arguments made above about the virtues of product-linked financial education can be extended to a broad range of products and services that poor people use – and manage money around – every day.

I think we are on the same page about money management as fundamental to the lives of people, the challenges of money management, and the potential for good financial education at the right time to improve financial well-being. I would argue against restricting delivery channels on the basis of other commercial interests – we might be losing some of our best opportunities to improve people's lives. A little bit of knowledge and experience can go a long way, even if it's product linked!

Jennefer

Dear Jennefer

You say that: 1) we might as well embed financial education in MFI marketing approaches because it provides a 'teachable moment', is cost effective and can reach scale; 2) using financial products and services as the entry point provides an immediate opportunity to put new knowledge and skills into practice; and 3) unbanked people can be reached by encouraging non-bank commercial players to link financial education to their products and services.

Clearly, some financial institutions now provide general financial education and do it well. These institutions are committed to social performance and are client-centred. They learn about clients' financial requirements and provide basic financial management training to help them plan for the future, manage and increase their assets, and make long- and short-term financial decisions. Many of these institutions consider financial education not primarily as marketing, but as a means to contribute to the financial well-being of their clients.

Don't underestimate the dangers of the conflict of interest that arises when education and marketing are commingled. Education helps clients know what choices they have and make decisions on a full range of product offerings from a variety of sources; marketing promotes a narrow range of products from one financial institution. The result of commingling is that the client may be guided toward a choice that is not right for her. This goes against the principles of client protection and institutional social performance management objectives. Business motivations and the best interests of the clients can collide resulting in unfair treatment of clients and over-indebtedness situations, to name a few.

You argue that financial education 'embedded into marketing messages is a cost-effective approach for reaching large numbers and for repeating simple messages, two things with potential for impact'. But, given that lowering costs will drive institutional decisions, it is likely that financial messages through marketing will result in more awareness-raising than behaviour change. Consider the goals of financial institutions. Incentives drive performance, and a marketing agent delivering financial education is more likely to be held accountable for sales than for the suitability of the education. The measure of his success will be how many new accounts were opened or the percentage increase in savings or loans rather than a measure of whether the client can do a budget projection, pay for her children's education or have less financial stress in her life. Not so long ago, banks and mortgage brokers in the United States educated consumers about how to get a low-cost mortgage to buy their dream home. We know how that ended up!

You point out that product-linked financial education provides a 'teachable moment' at a time when there is an immediate opportunity to apply what has been learned. However, relevant financial education involves more than a short-term decision to use a particular financial product. Financial education, done well, can build confidence to address a range of intertwined financial management issues, such as how to manage over-indebtedness, save for a child's education, or prepare for old age. It can lead to good life decisions, including choosing the financial products and services that are best suited to lifecycle goals and events long into the future. Financial education should strengthen the client's management of financial resources – both formal and informal – to address day-to-day financial concerns or plan ahead for health emergencies, food shortages or devastation from floods or hurricanes, for example. These decisions are extremely relevant.

And I would be cautious about assuming that product-linked financial education is the least expensive route. First, it may require more customization than generic financial education, resulting in higher costs for curriculum design and training. Second, the more specifically tailored to a product, the less scalable the education will be.

I like your creative thinking about getting to unbanked populations by linking financial education with other commercial products. But the dominant motivation will still be to sell the products, rather than to build true financial capability that empowers clients to make important life decisions.

Product-linked financial education still leaves out critical populations. There are now 7 million savings groups members and this number is projected to reach 50 million by 2020. This is not to mention the tens of thousands of other grassroots organizations and community associations that reach underserved populations. As these groups and their members mature and require more diverse financial services, they need to learn about the various types of financial institutions and products they have to choose from. NGOs or government programmes can provide financial education to and through these groups, while commercial entities may not reach them at all.

Finally, we must also consider other populations. Youth make up 60 per cent of the population in the developing world. The vast majority do not have access to financial services. Some say financial education is as important a subject as maths and should be integrated into the school curriculum. Financial education for niche populations, such as sex workers and prisoners, that are not regularly served by formal financial service providers, has already proved highly successful.

You might say that working outside of commercial product delivery is costly and unsustainable. But financial education is a public good, and when delivered only through a commercial approach is too limiting. One might argue that it is the most important educational topic after health. It can mean the difference between having the resources to survive a health threat or natural disaster, or succumbing to it. It can be offered effectively through governments, schools, and NGOs as well as financial services providers of all kinds. And to reduce costs, we are developing new and very promising ways of delivering low-cost financial education through e-learning and mobile applications for cell phones that will revolutionize access.

Jennefer, I think we both recognize that diverse channels of financial education delivery are necessary. My point is that a narrow product-linked approach will be more successful for product sales than for inculcating good financial management practices among a range of populations over the long term.

Kathleen

Dear Kathleen

In debating the pros and cons of financial education linked to products versus a broader approach focused on personal money management, I think there is a lot of overlap in our objective of improving financial capabilities, but less agreement on the motives of different actors and route to getting there. In the context of this debate, I think it is important to keep in mind that a key objective in our field is financial inclusion for the 2.6 billion working age people throughout the world who still do not have access to quality financial products and services that can improve their lives. Financial inclusion requires building a stable financial system, deepening the reach of the financial sector to the poor, improving access to quality financial services for the poor, and building the capability of clients to use them. Financial inclusion will not be achieved unless someone, somewhere is selling quality products and clients know how to use them to their best advantage. You suggest that commingling product marketing and financial education subverts the aims of financial education because the motive of financial service providers is selling products. An important part of financial inclusion is selling products, but combining financial education with product sales adds value to financial inclusion by providing clients with knowledge about the terms, conditions, and obligations of specific products, how to navigate delivery channels, and the pitfalls and/or benefits of use. This type of education is equally beneficial to clients and to financial service providers – more informed clients, improved trust between clients and providers, and better designed products that support the longer-term well-being, sustainability, and profitability of the institution.

There is still a long way to go in building stable financial systems that reach the poor and support broad-based economic growth. Product-linked financial education can promote a virtuous circle: the process of designing and delivering product-linked financial education can help financial institutions reach out, understand, and serve poor clients with appropriate products; appropriate products and services will help to stabilize and improve the financial performance of financial institutions; improved access to quality financial services will reinforce financial capabilities; improved financial capabilities will increase the demand for quality financial services; increased demand will strengthen and expand the market. Linking financial education to specific products can support this process much more quickly than more generalized financial education. From the perspective of financial inclusion, product-linked financial education will result in more immediate and more sustained benefits to the poor.

To the extent that staff and agents are involved, product-linked financial education brings other benefits. By training front-line staff who are often financially illiterate, institutions can also ensure a consistency in financial education and product messaging within and across institutions.

I also think we should not underestimate the ability of clients to discern unscrupulous practices of financial service providers. Many clients have a healthy amount of caution in dealing with financial service providers: the result of the negative experiences of others. Institutions with a longer-term view increasingly recognize the importance and challenges of building and maintaining trust with clients – how long it takes to build trust, and how quickly it can be lost through unprincipled or irresponsible practices. Providing useful financial education in combination with products will help to build trust and client loyalty, which is so important for building a stable financial sector that serves the needs of low-income clients.

Jennefer

Reference

CGAP (2013) 'Deepening financial inclusion in West Africa' [blog], CGAP <www.cgap.org/blog/deepening-financial-inclusion-west-africa> [accessed 8 August 2013].