

**Strategic Framework for Investor Education and Financial Literacy
IOSCO Consultation Report CR/14**

1. Introduction

We fully agree with IOSCO that the need for investor and financial education has never been greater than today. Therefore, we are very pleased that IOSCO has decided to expand further its activities in this area by creating a new Committee (C8) with a mandate to conduct policy work on retail investor education and financial literacy. We strongly believe that securities regulators are in a unique position to take on an important role in developing investor education initiatives. The fact that investor education forms a key component of the overall objective of investor protection and that securities regulators play a pivotal role in the design of investor protection measures, constitute a further reason why securities regulators and IOSCO should intensify their contribution in the area of investor education. It should be clear, however, that investor education initiatives shouldn't aim at ensuring that everyone understands in detail all the investment and risk management techniques that are being used to develop and manage investment products. Whilst these techniques may appear complex, their main goal in the case of highly regulated products like UCITS is to achieve a clear investment strategy and a limited level of risk. What is essential is that investors understand the proposed strategy and risk and determine if they suit his/her needs.

Before commenting on each section of the Paper, we would like to draw IOSCO and C8's attention to a report on investor education that EFAMA published in March 2014 to push investor education to the top of the public-policy agenda. This report, which is available from the EFAMA websiteⁱ, provides an overview of the existing work on financial literacy by collating wide-ranging, independent analysis, including from Gary Tidwell from IOSCO. It sets out a list of best practice guidelines to support the development of investor education initiatives in the financial sector (see Appendix). It also presents a number of illustrative initiatives that are already being undertaken by EFAMA members – trade associations and corporate members – across Europe in order to promote investor education.

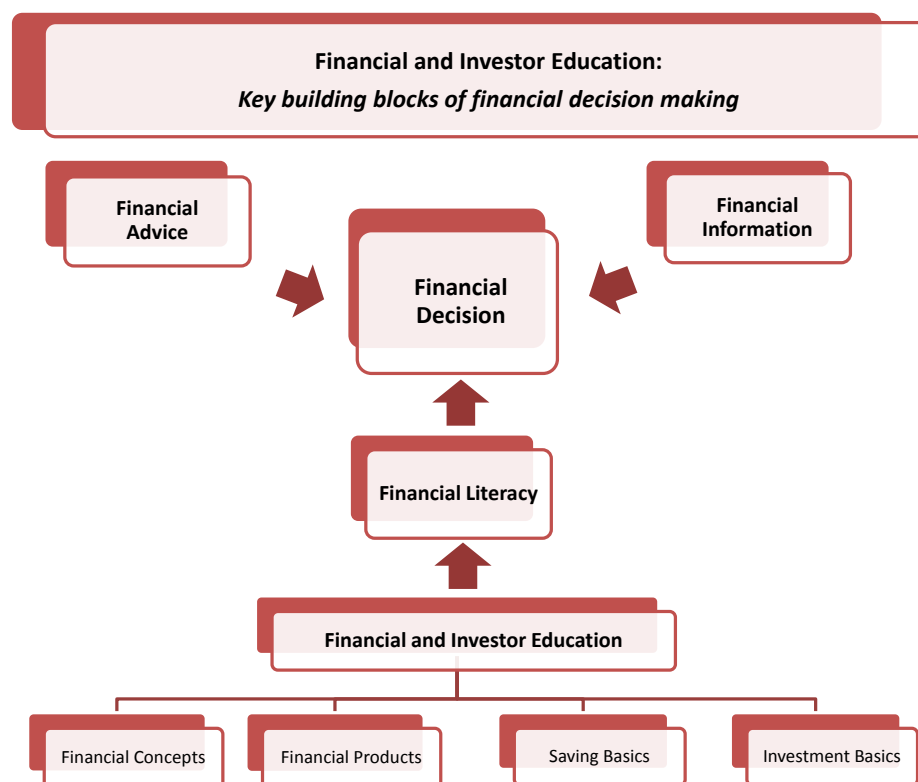
We are also pleased to announce that EFAMA will become a member of the International Forum for Investor Education (IFIE), to help IFIE establish a firm presence in Europe, to complement IFIE chapters in the Americas, the MENA countries and Asia. We hope, of course, that we will be able to collaborate with IOSCO and C8 on some of the new initiatives that will be taken in the context of the Strategic Framework for Investor Education and Financial Literacy.

2. Background

Financial literacy and investor protection

We fully agree that *“investor education is a key strategy for enhancing investor protection”*. It is an important consideration to keep in mind when considering the effectiveness of the numerous

consumer protection measures that have been taken in many countries in response to the financial crisis to strengthen the quality of financial information and advice provided to consumers. Indeed, we believe that this type of measures may be ineffective if consumers do not have the basic knowledge required to understand financial products, concepts and risks. As suggested in the figure below, financial and investor education should be a complement to measures aiming to ensure the appropriate provision of financial information and advice to consumers. From this perspective, it is clear that investor education and financial literacy programs should be viewed as an essential additional tool available to securities regulators in supporting regulation and supervision.



Source: EFAMA's Report on Investor Education (March 2014)

Investor education, financial literacy and financial education

We agree that the terms "investor education" and "financial literacy" should be defined. Generally speaking, we agree with the distinction made in the Consultation Report. In addition, it would be useful to distinguish between the terms "investor education" and "financial education", which tend to be used interchangeably.

One way of thinking is to relate financial education to the learning and improvement of skills and knowledge of financial concepts and products which are essential to the day-to-day management of personal finances, and provides individuals with the ability to understand financial matters that they are likely to come across in everyday life. In this perspective, financial education focusses on basic concepts such as inflation, interest rates and risk diversification, basic financial products such as bank accounts, mortgages, stocks, bonds and investment funds, and basic aspects of financial planning such as saving, debt management and insurance.

Investor education, on the other hand, refers to the learning and improvement of skills and knowledge that people need to know for making sound investment decisions, selecting among different savings products, and planning for retirement. Investor education allows an informed decision to be taken when buying, selling or managing investment products. In this area where a majority of people have to manage their savings and plan for their retirement income, investor education programs are very important to improve the well-being of people by contributing to better saving and investment decisions, as well as overall economic welfare by fostering efficiencies in the financial industry.

Benefits of investor education and financial literacy

It is useful to highlight four important reasons why financial education is critical for individuals and the economy as whole:

- **Financial education strengthens investor protection.** The efforts undertaken to strengthen financial information and financial advice will only have their full effect if they go hand in hand with policies to improve the level of literacy of individuals. A well-educated investor will ask critical questions of his or her adviser, leading to higher levels of investor protection, more sound advice and ultimately, financial results that have a better chance of being well-matched to the investor's goals.
- **Financial education improves investment behaviour.** European citizens, for example, remain mostly risk averse. Consequently, they tend to misallocate their savings towards non-risky and short-term products. It is therefore necessary to educate the end investors so that they better understand the notion of risk and return.
- **Financial education develops retirement savings and promotes long-term investing.** Many people lack the level of financial education required to decide how much they should save to prepare for retirement. As individuals in Europe, for example, are increasingly responsible for making their own arrangements for retirement income, an important policy goal of financial education initiatives has to be to explain to citizens why they should save more for retirement. Achieving progress in this direction not only would help people in securing the future adequacy of their retirement income, but it would also increase the volume of savings available for long-term investments in the real economy.
- **Education as a means to restore confidence:** one of the goals of investor education initiatives is to bring the investor to such a level of knowledge and understanding that he will be in a position to entrust his advisor with total confidence. Confidence is the key concept for financial stability and a smooth functioning of financial markets as well as the economy at large.

3. Role of IOSCO in investor education and financial literacy

We fully agree that IOSCO is well positioned to play a key role in the development and delivery of investor education and financial literacy programs, for the reasons outlined in the Consultation Paper.

We also fully agree that securities regulators can take on key leadership roles in specific areas of investor education in the context of national and local strategies for investor education. It could even be argued that securities regulators should encourage their governments to establish National Strategies for Financial Education, if they have not already done so. *“The rationale for the development of such strategy is multi-fold and especially rests on the need for adapted, consistent, coordinated and effective action to boost financial literacy while avoiding duplication of resources.”ⁱⁱ*

4. Global focus on investor education and financial literacy

It is encouraging that a number of global organizations and networks are committed to promote investor education and financial literacy. And it is good news that the G20 Leaders have endorsed the High-Level Principles on National Strategies for Financial education developed by the OECD and its International Network on Financial Education (INFE).

Given the number of stakeholders involved, it is important to ensure efficient coordination between global organizations and avoid duplication of efforts. We believe that IOSCO and C8 could take an initiative to this end. The IFIE/IOSCO global investor education conferences show that there are cooperation possibilities between global organizations.

We also believe that C8 should aim at engaging directly with organizations within the financial services industry that are involved on investor education initiatives. In this context, it cannot be overemphasized that the asset management industry is very pro-active when it comes to investor education and financial literacy. Our industry has made important efforts, sometimes but not always under pressure from the authorities, to increase transparency in the investment market for retail investors in order to help individuals to make sensible investment decisions. The agreement on a common EU standard for a Key Investor Information Document is a good example. The publication of our report on investor education guidelines provide another illustration. Consequently, C8 shouldn't hesitate to engage with the asset management industry and take into considerations all the initiatives taken or to be taken.

5. Role of research in investor education and financial literacy

We agree that the role of research in investor education and financial literacy is very important. We also believe that it would be useful to distinguish between both fields of research, for the following reasons.

Research in financial literacy is essential because policymakers need reliable indicators about the level of financial illiteracy to establish financial and investor education programs, and secondly, because those indicators are very important to evaluate the effectiveness of these programs and, therefore, whether policies should be adapted.

Research in investor education, on the other hand, should focus on financial decision-making, particularly to try to better understanding how individuals behave when they must take an investment decisions and what role financial information and financial advice play in their decisions.

In our view, IOSCO and C8 have a more important role to play in research in investor education, as this field of research may reach useful conclusions on how consumer protection rules should be designed to be effective given the various reasons that explain why people tend to make poor financial decisions. From this perspective, IOSCO should consider promoting this type of research and empirical testing (including in the area of behavioral economics and finance).

We also feel that C8 should be pragmatic in its approach in order to develop programs and initiatives that can be evaluated according to some methodology to get a view on their impact and to collect suggestions to make them more relevant and as effective as possible. As mentioned in the paper, empirical testing for example is also a topic for research.

6. C8's strategic approach to investor education and financial literacy

Generally speaking, we concur with the initial areas of focus (investment knowledge and understanding, financial skills and competence, and program design, delivery and measurement).

With a view to assisting C8, we would like to offer comments on three aspects.

- The potential areas for C8's work are very broad. It is unlikely that all areas will be taken up in the foreseeable future, unless significant resources can be mobilized to this effect. We would therefore encourage C8 to determine where it can make a difference to the objective of more and/or better retail investor education and financial literacy, and to set realistic goals and identify specific actions.
- We believe that C8 should have the ambition to play an important role in the area of long-term saving and retirement savings. The increasingly important role played by defined-contribution plans imposes on individuals a greater personal responsibility to save, invest, and de-cumulate retirement assets sensibly. Therefore, given the important role that complementary retirement savings will take in the future in securing the future adequacy of pensions, C8 could take concrete initiatives aimed at helping people adopting a future retirement income goal and saving behavior in line with this goal.
- Whilst agreeing that retail investors should have a "healthy sense of skepticism", we find it equally important that retail investors understand the benefits of investing for the long term. There is also a need to find the right balance between the initiatives that will aim at protecting investors against the dangers of investing (such as the risks, fees, fraud, mis-selling, etc.) and those that will encourage people to invest for the long term, for instance by disseminating positive information about the benefits of long-term investment and the safeguards that ensure that an investment can be considered as sufficiently prudent (such as risk diversification, risk management, asset custody, etc.).

- We suggest that C8 pays a close attention to the reality of the investment and distribution process from the perspective of a retail investor. We think that a mapping of all actors and their principal role would help in identifying where the critical points are located, who is concerned and how they could be addressed. Such an exercise should identify the specific challenges associated with the different distribution channels, including internet.
- Finally, we believe that C8 should also take a close look at the role played by very many different channels through which individuals are being informed about investment decisions and products, in particular the press, teachers and professors. These “information intermediaries” could also be targeted by ad-hoc investor education and financial literacy programs.

7. Current practices of C8 members for investor education and financial literacy programs

We are encouraged by the number and scope of initiatives are being taken at the national level. We also find it interesting to see how C8 has regrouped the different initiatives within seven types of practices. We have followed the same logic by arranging our guidelines for investor education initiatives around four themes (context, content, delivery and evaluation), as explained below.

In order to be more specific though, we would like to provide our views on Practices 6 and 7.

Collaborate or partner with other relevant organizations

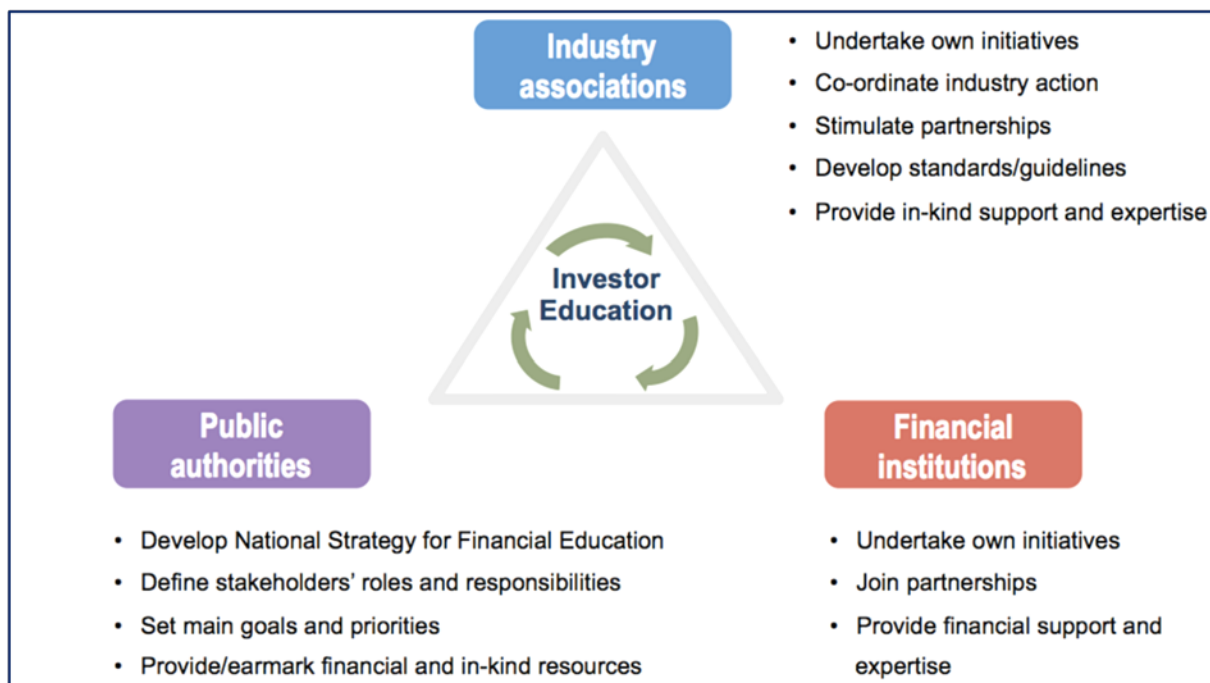
There is no doubt that partnerships with relevant stakeholders in the financial services industry, including industry associations, professional bodies, intermediaries, financial institutions and other market participants, can contribute to strengthen the capacity of investor education initiatives to make a true difference in the community.

As a matter of fact, we feel that the proximity of the industry to both investors and securities regulators would justify regrouping within a specific practice all the investor education initiatives taken by organizations in the financial sector at large. The knowledge that could be gathered and shared in this specific area could be very useful to improve the quality of industry driven investor education initiatives. If we need any proof of this, we would stress that it is the concrete initiatives undertaken by professional associations and firms in the asset management industry to promote financial education that formed the primary material that allowed EFAMA to define detailed guidelines for getting the most out of investor education initiatives.

Consider national strategies

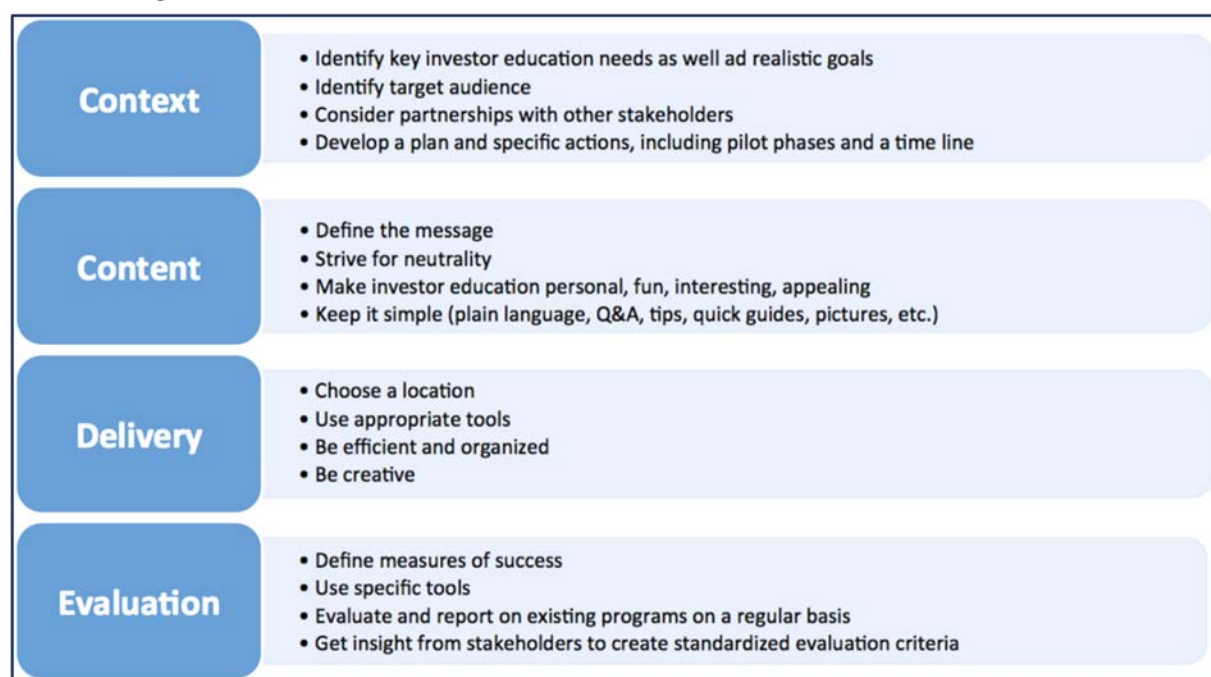
In our view, national strategies for financial education represent a most effective way of adopting a holistic approach to financial education and investor education. In taking the lead in developing strategies for financial education, public authorities, including national and regional governments, securities regulators, and ministries of education and finance, should collaborate with other relevant organizations to create synergies by pooling scarce financial and human resources and coordinating investor education initiatives. In this context, the authorities should not hesitate to seek the support of industry associations, which are well placed to encourage their members – financial institutions

and other market participants – to play a role in the development and delivery of investor education and financial literacy programs. As suggested in the figure below, this type of partnership between the authorities and the financial industry is likely to result in a positive dynamic in the efforts undertaken to improve the level of financial literacy of individuals.



Appendix -- EFAMA's Guidelines for Investor Education Initiatives

Drawing on the initiatives undertaken by ten professional associations and seven investment managers to promote financial education, EFAMA has defined detailed guidelines for maximizing the impact of industry driven investor education initiatives. These guidelines, which are summarized in the next Figure, provide a template to encourage, inspire and support the development of investor education initiatives by organizations in the investment management industry and the financial sector at large.



There are three guidelines which it is particularly useful to focus on to highlight the specific contribution of fund managers in the area of investor education.

➤ Identify the target audience

There are two main target groups for investor education initiatives in the fund and asset management industry: private individuals (end-investors, children, students, employers, pre-retirees, retirees, etc.) and financial intermediaries who can spread financial knowledge to end-investors (company staff, fund distributors, financial advisers, teachers, journalists, etc.). Whereas the first group represents the traditional target audience of investor education initiatives, the actions to ensure intermediaries have an appropriate level of financial knowledge themselves, in order to promote financial literacy and enable potential investors to make better-informed investment decisions, are also very important. It is indeed an effective way for fund managers who are not in regular contact with end investors, to contribute to improved investor education.

The industry can also contribute to investor education by targeting three other categories of stakeholders: the public authorities to convince them of the importance of investor education to gain financial and political support for investor education-related initiatives, the journalists to raise awareness about the role they can play in the area of investor education, and the educators and

other communicators to train teachers and trainers to pass on to their students and specific audiences key investor education principles.

➤ **Define the message**

Investor education messages should either focus on core or general concepts that are fundamental to investor education or on aspects specifically relating to a specific product. Either way, the message must relate to the needs of the consumer and be communicated in a familiar register.

When focusing on core concepts and messages, the initiatives can aim at reaching the following goals:

- Advising consumers about how they should approach an investment decision to act as an educated and informed consumer (“ask questions”, “be critical”, “be engaged”, etc.)
- Developing the knowledge, skills and attitudes every child and young person should have in relation to money
- Educating investors about basic financial concepts, saving and investing, saving for retirement and pensions, bond and equity essentials, sustainable and responsible investment, asset allocation, risk and return, fees, counterparty risk, etc.

Investor education initiatives can also provide specific information about products, such as for investment funds the different types and characteristics of assets funds may invest in. They can also focus on the advantages of investing in the products, e.g. for investment funds: safeguards, collective investment, risk spreading and asset diversification, costs, transparency, liquidity, risk management, etc.

➤ **Strive for neutrality**

Investor education content that does not promote specific products or brands will inspire more engagement and trust from investors. Depending on the context, the focus should be completely neutral vis-à-vis all types of providers (insurers, banks, asset managers) or contribute to enhance people’s knowledge about certain categories of products. This means that not only investor education initiatives promoted by securities regulators should be “*fair and unbiased*”, but also industry driven investor education initiatives.

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ⁱ See <http://www.efama.org/Lists/Topics/form/Displtem.aspx?ID=47>.

ⁱⁱ Quote from the preface written by Flore-Anne Messy (Principal Administrator, Financial Education & Global Relations, OECD) for the EFAMA Report on Investor Education.

