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Choice Overload

Australians coping with financial decisions

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The opinions presented and conclusions drawn in this paper remain the responsibility of its author.

Summary

Choice and risk in personal finances

Extensive choice is usually regarded as a positive thing for consumers, and it often is. Yet there are circumstances where more choice is actually detrimental to consumer welfare. In the realm of personal finances, people are often presented with choices that they would prefer not to make, or prefer someone else to make on their behalf. This paper considers the circumstances in which ‘choice overload’ can occur, and discusses possible solutions.

Chapter 1 describes the ‘information deficit’ that many consumers now face, and discusses the implications of greater choice for financial decision-making.

Over recent decades, many Australians have taken on additional financial risks – the result of a more ‘flexible’ labour market, a user-pays health system and, importantly, increasing self-reliance in retirement provision. At the same time, Australia has become a nation of share-owners, with many people relying on the ups and downs of the market for their future livelihoods.

Chapter 2 describes the changing risk profile of Australian households, along with the vision of the ‘ownership society’ celebrated by the advocates of economic liberalisation.

There is a large body of research showing that inadequate levels of financial literacy prevent many people from making sensible and informed financial choices. As a result, many people behave in ways that are not ‘rational’ in an economic sense. There is persuasive economic evidence that the effect of such behaviour is often to the detriment of consumer wealth and wellbeing.

Chapter 3 summarises the existing research on financial literacy and ‘irrational’ financial behaviour.

Key findings

This research set out to discover how Australians are coping with complicated financial decisions, through a series of six focus groups and a nationally representative survey of 1,002 people. The findings are presented in Chapters 4 and 5.

The survey results show that many Australians are uneasy about the increasing complexity of financial decision-making:

- 42 per cent of respondents agreed that *when I need to make a financial decision, I often find there is too much choice*, while only 18 per cent disagreed;
- 46 per cent agreed that *financial investments are too complicated to understand properly*, while only 20 per cent disagreed;
- 44 per cent of respondents agreed that *superannuation is too complicated to understand properly*, compared with just 26 per cent who disagreed;

- around a quarter of survey respondents (23 per cent) said they were not confident in their long-term financial future; and
- women, young people, people on lower-incomes and people with less formal education were less likely to be confident in their financial future;
- Major risks worrying participants included job loss, ill health or injury, and property or share market fluctuations.

Focus group participants generally agreed that financial decisions are becoming more difficult as financial markets grow more complex.

- While many were positive about the notion of choice *per se*, some people, and particularly older people and those on lower incomes, are sceptical about extensive choice in their personal finances. Among people over 30, there is also hesitation about the benefits of deregulation and market liberalisation in the financial sector.
- Many young people, on the other hand, appear to regard greater choice and competition as inherently good.

Focus group feedback uncovered a range of approaches to financial decision-making that could be described as ‘irrational’. These included:

- a lack of planning;
- excessive reliance on advertising for information;
- non-systematic ways of making decisions;
- not endeavouring to understand the necessary information, and
- not having, or seeking out, the right information.

The research results confirm just how common ‘irrational’ approaches to personal finances are.

- Around half of survey respondents (52 per cent) reported not spending ‘the right amount of time’ making financial decisions, with some people spending too little time and some spending too much.
- Many focus group participants reported procrastinating in some way over their financial affairs.
- One in three survey respondents (32 per cent) agreed that they often put off financial decisions until later.

Many people support increased efforts to boost financial literacy by making financial information and education available and comprehensible. In addition, there is community support for new initiatives to encourage a savings-oriented ‘culture’, with a widespread perception (particularly among older people) that the present generation

of young people have not been properly taught to save because of the easy availability of credit and consumer-oriented advertising. Focus group findings also revealed community support for:

- independent mechanisms that allow people to compare financial products simply and independently;
- the dissemination of information outside an internet setting (particularly for older people and others who have trouble accessing the internet); and
- practical financial education and advice that takes place outside the context of the profit-based financial adviser/client relationship.

Conclusions

Implications for government

The standard policy response to the shortfall in financial literacy, both in Australia and overseas, has been to address the ‘information asymmetry’ problem by providing financial information to consumers in a variety of ways. Chapter 6 argues that such an approach places the onus of responsibility for dealing with a changing financial environment squarely on the consumer, and neglects the fundamental responsibilities that governments and financial institutions have to present consumers with choices that they understand and value. Government policy in the area of consumer policy should be based on the following priorities:

- improving basic literacy and numeracy at the population level and among particular target groups;
- ensuring that consumers can *choose not to choose*, where appropriate – both in the financial sector and in other areas of activity where greater choice can be shown to have detrimental consequences;
- looking beyond market-based solutions to remedy low rates of financial literacy;
- formally evaluating the success of financial literacy programs in bringing about positive behaviour change in consumer finances; and
- changing the regulatory environment to facilitate better communication between financial providers and their customers.

Implications for business

The way that financial providers have operated in the past has contributed to a widespread mistrust of the financial sector by ordinary Australians. To build community trust and to foster a mutually beneficial relationships between consumers and financial institutions, the following principles should be adopted:

- financial products should be advertised and promoted in ways that contribute to, rather than undermine, broader public understanding of financial concepts and imperatives;
- over the long term, financial advisers should use fair and transparent methods of remuneration that are not tied to the sale of any product; and
- financial providers should compete for retail customers on the basis of optimum simplicity.

Implications for individuals

Consumers are now expected to have the motivation and capacity to improve their financial knowledge. However, it is the responsibility of governments and businesses to ensure that their information matches people's capacity to understand it. In certain respects, government and business have not been fulfilling their end of the bargain.

Citizens should monitor their governments, through the democratic process, to ensure that:

- a regulatory environment is established in which more straightforward financial choices are possible;
- independent information is easily available and comprehensible; and
- the needs of people who struggle with financial decision-making are addressed.

Consumers should also monitor financial providers, and withhold their patronage if necessary, to ensure that:

- they actually understand the nature of any financial risks they are undertaking, rather than just receiving the relevant legal documents; and
- businesses refrain from exploiting emotional triggers (such as anxiety about retirement) to sell them financial products and services they do not need.

Above all, people should not blame themselves if they cannot understand a financial concept, or if they struggle to make sense of a financial document. They are not alone.

1. Good choice and bad choice

1.1 Choice in economics

In the ordinary course of our lives we make all manner of decisions. These range from the trivial and inconsequential, like which breakfast cereal to buy, to important judgments that will affect the rest of our lives, like which career to pursue. Modern society presents us with an increasing number of choices in almost every facet of our lives. Indeed, one of the defining characteristics of the globalised economy is the range of choices available to ordinary consumers.

Choice is usually regarded as inherently good. Common wisdom has it that people like choice, and that governments and businesses contribute to social wellbeing by facilitating greater choice. At the individual level there is much evidence to support this view. Choice has been shown to enhance people's sense of self-determination and motivation to perform tasks, while the increased sense of control associated with choosing leads to improved psychological and even physical health. Choice can also help people to be more positive about the decisions they have made (Botti and Iyengar 2006).

Consumer choice is at the heart of mainstream economic thought. Rational choice theory, for example, assumes that individuals have well-defined and consistent preferences, and will act in ways that maximise their own 'utility'. It also assumes that people have access to enough information to enable them to properly assess the costs and benefits of each option, so that the right choices can be made (Frank *et al* 2007). Or, if the right information is not immediately available, then it is possible to assess the costs associated with acquiring that information, at which point an 'informed' judgement can be made about whether to seek out further information. When the costs and benefits of all these options (including finding more information) have been weighed up, the outcome will, according to rational choice theory, maximise individual wellbeing. Increasing the amount of options allows every individual to express his or her preferences more exactly, and this enhances collective welfare. By this argument, more choice automatically translates into greater overall utility (Schwartz 2000; Botti and Iyengar 2006; Frank *et al* 2007).

Of course, it is difficult or impossible to determine what competing factors coalesce in the minds of individuals as they form their preferences. Rather than examining how people assess different options, economists rely on the theory of *revealed preference*, the idea that people's actions – usually in the form of their purchasing decisions – are the true test of their needs and wants. Revealed preference provides a guarantee that the choices people make are always in their best interests, and that collective choices are in the best interests of society generally. But it also relies on a circular logic, in assuming that people always understand completely what choices reflect their best interests. Challenging the notion of revealed preference, there is persuasive evidence that people often make choices based on emotional factors rather than a strictly rational appraisal of costs and benefits.

1.2 Detrimental choice

Contrary to the dominant economic theory, some economists and other social scientists argue that choosing is not always a positive experience, and that people often make choices that are not in their individual or collective interests. Over recent years, psychologists have been investigating the circumstances in which choice can be detrimental. In a classic experiment, two groups of supermarket shoppers were given a different number of jam products to sample. The first group was given six options, while the second group had 24 to choose from. After tasting the jams, nearly 30 per cent of those who were given the limited range of options ended up purchasing some jam. By contrast, a mere 3 per cent of those who were given the extensive-choice option actually made a purchase (Iyengar and Lepper 2000). Similar experiments were also conducted with students choosing which essay topics to write on and consumers choosing which chocolates to eat. In each case, the results clearly showed that in particular settings too much choice can be overwhelming, and can affect people's subsequent satisfaction with the decisions they end up making (Iyengar and Lepper 2000). As the authors of the study conclude, these findings 'provide compelling evidence that the provision of extensive choices, although initially appealing to choice-makers, may nonetheless undermine choosers' subsequent satisfaction and motivation' (Iyengar and Lepper 2000, p. 1003).

While choice gives us more control over our lives, too much choice can provide the mere *illusion* of control. There is evidence that when faced with a difficult choice – for example, where there is no clear preference for one option over another – people often opt to make no choice at all, or prefer others to make the choice for them. Alternatively, because they regard themselves as being in control, they tend to blame themselves for making the wrong choice (Iyengar and Lepper 2000; Schwartz 2000; Botti and Iyengar 2006; Dhar 1997).

As the extent of choice grows in many facets of modern life – and particularly in the marketplace – it can become increasingly difficult for people to properly assess each option. Abundant choice creates what psychologist Barry Schwartz calls 'a seemingly intractable information problem', in which the 'cost of thinking' is simply too high. In such situations, he argues, 'rather than even try, people may disengage, choosing almost arbitrarily to get the process over with' (Schwartz 2000, p. 84). This is not the standard model of human behaviour as assumed by most economists, but it does appear to provide a more accurate description of how people respond when faced with overwhelming choice.

Clearly, choice is not the uniformly positive attribute advocated by economic theory and celebrated in popular culture. Instead, choice can be good, bad or neither, depending on the context. *Good choice* is the kind which gives people more control over their lives and circumstances, while *bad choice* has a detrimental impact on wellbeing. More specifically, good choice is where there is sufficient information and people have clear preferences (what to have for lunch, for example). Bad choice is where people are poorly informed (such as which medical treatment to opt for), where the 'cost of thinking' is prohibitive (such as which company's shares represent the best value), or where there is no clear preference for one or another (such as which brand of detergent to purchase) (Sunstein and Thaler 2003).

As well as distinguishing good choice from bad choice, we can differentiate between situations where a person relies on their own *subjective* preferences to make a decision, and situations where there is one option that is *objectively* superior to its alternatives, regardless of personal preference. For example, we might say that choosing an item of clothing is a personal choice, and one that is (usually) based on subjective criteria. Generally speaking, no one item of clothing is objectively ‘better’ than others (although many people might agree in their opinion of a particular item). By contrast, choosing which natural gas supplier to use is likely to be based on the price of gas rather than any personal preference. In this case, it is reasonable to say that one gas supplier is objectively better than another, in that they sell their gas more cheaply (assuming that the quality of their customer service is similar). Of course, these two categories of choice – the subjective and the objective – can overlap, and much marketing and advertising activity is designed to turn seemingly objective choices, like mobile phone plans or cleaning products, into subjective ones. However, there are categories of goods and services that more clearly fit into one category or the other.

1.3 Choice in personal finances

Most decisions about personal finances – that is, decisions about savings, investments, retirement planning, insurance and other financial products and services – fit the objective choice model, or involve some degree of objective choice. It is reasonable to say that one savings product is ‘better’ than another because it earns more interest, or that one insurance policy is superior to another (on comparable terms) because it is cheaper. It is the ‘right’ decision to choose an investment product which will maximise returns, and the ‘wrong’ decision to opt for a product with lower returns. Although financial providers often rely on subjective or emotional triggers to advertise and promote their products, orthodox economic theory assumes that people make decisions about financial products according to objective rather than subjective criteria. However, conversations with ordinary Australians, reported in Chapter 4, reveal that emotional factors, such as trust in particular institutions or brand recognition, have a disproportionate influence on financial behaviour.

In order to make the ‘right’ choice, consumers of financial products need the right information. This is not necessarily a problem for very knowledgeable consumers, who are able to understand the implications of each option. For other consumers, however, the cost of acquiring and interpreting this information – the ‘cost of thinking’ – is very high. This could be as a result of insufficient education or problems with numeracy, or it could simply be through lack of experience. Faced with a decision they are not qualified to make, people often end up making *no choice at all* – even when this is the worst option available. Many of the people consulted for this research admitted to being so overwhelmed by the range of choices available that they ended up taking no action whatsoever. According to psychologists, ‘the more choosers perceive their choice-making task to necessitate expert information, the more they may be inclined not to choose, and further, they many even surrender the choice to someone else’ (Iyengar and Lepper 2000, p. 1004).¹

¹ This tendency is borne out by the growth in the financial advice sector, which has taken place at the same time as the range of options available to retail investors has grown.

Even more significantly, people look for shortcuts when they are forced to make decisions for which they have no clear preference or where the cost of acquiring information is high. They apply what psychologists call a *heuristic*: a rule or short-cut that allows them to solve complex problems even with incomplete information. One heuristic that is particularly relevant in the realm of personal finances is *doing what other people do* (otherwise known as ‘social proof’), while another is *doing what informed people do* (that, is relying on perceived authority) (Cialdini 1993; Sunstein and Thaler 2003). For instance, someone who is deciding on a superannuation investment portfolio might ask their colleagues which portfolio option they chose, even if their colleagues are no more qualified to make such a decision. Alternatively, they might rely on the default plan, because they assume that the default has been put in place as a sensible compromise. However, these approaches will not always yield the best financial outcome for each person.

In fact, as Chapter 3 will make clear, people often make decisions about their finances – and other matters – that are not in their best interests or are otherwise not prudent. According to Sunstein and Thaler:

Research by psychologists and economists over the past three decades has raised questions about the rationality of many judgements and decisions that individuals make. People ... use heuristics that can lead them to make systematic blunders, exhibit preference reversals (that is, they prefer A to B and B to A), suffer from problems of self-control, and make different choices depending on the framing of the problem (Sunstein and Thaler 2003, p. 1168).

This is a very different account of how people make choices from that advocated by orthodox economics. While ‘irrational’ decision-making may not be a problem for many of the insignificant choices we make in everyday life, it can have huge ramifications for our personal finances. The consequences of some financial decisions are only felt many years later, by which time a poor choice will be too late to rectify. Further, some people may never realise that they have made the ‘wrong’ decision, because they are unaware of what alternatives there are. Despite this, the range of financial options available to consumers and the knowledge required to assess them continues to grow. With virtually every Australian worker now compelled to choose a superannuation fund, complicated decisions about finances and investments are now everyone’s responsibility. The assumption behind these trends is that people generally like more choice, and in particular prefer more choice in the context of their finances. Yet, as recent empirical research has shown, ‘posing choices in this way ... is to pretend that Australians understand and like the financial sector’ (Pixley 2007, p. 302). Our research sheds serious doubt on the proposition that Australians prefer greater choice in their financial affairs.

1.4 The information deficit

Financial products differ to other goods and services available to consumers in certain crucial respects. Individuals purchase financial products infrequently, so it is difficult for them to apply the lessons of experience in making sensible choices. More importantly, the value of a financial product is often not clear at the time it is purchased, becoming apparent only some years later. For this reason, it can be hard for ordinary consumers to verify the accuracy of any information about the product. This places them in a vulnerable position with respect to financial providers, who

have the wherewithal to accurately predict their likely future liabilities. Given the peculiar nature of financial products, then, consumers automatically face a considerable information deficit.

Exacerbating the situation is the fact that much of the information currently available to consumers, both on individual financial products and on general financial issues, can be extremely bewildering. This was acknowledged by the Australian Government's Consumer and Financial Literacy Taskforce in its 2004 report, *Australian Consumers and Money* (Consumer and Financial Literacy Taskforce 2004). The Taskforce noted that consumers 'have a number of common problems with information and advice', including:

not knowing what information is available or appropriate for their needs, being overwhelmed and confused by different information, not trusting the information, not understanding the jargon and terminology in the information and advice received, not feeling the information is relevant to their needs and lifestyle (particularly the case with young consumers) [and] understanding the information but not being able to act on it in any meaningful way (Consumer and Financial Literacy Taskforce 2004, p. 46).

According to the Taskforce, when information becomes too confusing, 'consumers tend to resort to easier and more trusted sources of information such as the media, friends and relatives' (Consumer and Financial Literacy Taskforce 2004, p. xiv). This means that common misconceptions are perpetuated.

Together, these factors create a major discrepancy between the information and knowledge available to financial providers and institutional investors on the one hand and, on the other hand, 'ordinary' or retail consumers of financial products and services. Consumers can find it much more difficult to assess various types of risk – including market risk, institutional risk and inflation risk – due to the inherent complexities of financial decision-making. Under orthodox economic theory, such 'information asymmetry' is actually a form of market failure. In other words, markets in which some participants possess important information while others do not tend to generate inefficient outcomes (Frank *et al* 2007).

This paper considers how ordinary Australians are coping with a surfeit of choice in their personal finances. Chapter 2 shows how the financial risks that individuals and households face have been changing, and how this has been justified under the guise of 'personal responsibility'. Chapter 3 presents evidence that many people do not possess the knowledge or skills to make rational financial decisions. Chapter 4 reports the findings of a series of focus groups held with Australians about personal finances, while Chapter 5 presents the findings of a national survey on financial issues. Chapter 6 summarises the findings of our empirical research and explores the implications for policy-makers.

2. The brave new world of personal finances

2.1 Changing risks

Australians are now richer than they have ever been. Between 1994 and 2005, real per capita incomes rose by an average of 3.0 per cent per year (ABS 2006a). By 2007, the average before-tax income of someone working full time had reached \$55,068 (ABS 2007). Though many Australians continue to struggle in meeting basic living costs, many more enjoy very comfortable lifestyles. Yet despite affluence now being 'mainstream', many people remain worried about their financial situation. According to a recent major survey of Australian social attitudes, just under half the population (45 per cent) say that they 'worry a lot' about their financial future, while only 28 per cent said they do not worry (Pixley 2007, p. 292).

There is another trend that has taken place alongside the prosperity boom, and that helps explain the disconnect between positive macroeconomic statistics and the pessimism of many ordinary people about their finances. Over recent decades, there have been fundamental changes in the financial risks that individuals and households face. In the wake of reforms designed to bring 'flexibility' to the labour market, job losses and career changes are now more common. The erosion of universal health care has meant that medical costs are often borne by individuals and their families, who can face large out-of-pocket expenses. Since the introduction of compulsory employer superannuation contributions in 1992, most employees have their own retirement savings account whose value is determined solely by the market. Additional saving for retirement (or for a rainy day) often takes the form of shares or other complex investments. As a result, retirement incomes are determined not by a considered appraisal of what standard of living is adequate and realistic – as the age pension was designed to do – but by what workers can earn and the performance of financial markets over the period of investment. High levels of household debt, much of which can be traced to soaring property prices, mean that many families can no longer fall back on their 'personal safety net' – i.e. savings and other liquid assets – in times of need (including increases in interest rates). With the livelihoods of ordinary people exposed to the ups and downs of the market in these various ways, many individuals and households are bearing significant levels of financial risk. One commentator has described similar trends in the United States as 'the great risk shift' (Hacker 2006).

2.2 Personal responsibility

Changes in the risks that Australians face have occurred alongside, and are partly a result of, powerful economic forces that have been set in train in recent decades by governments across the developed world. These policies, often referred to collectively as 'neo-liberalism', were characterised by a focus on market-based arrangements in service provision, the privatisation of government-owned assets and the relaxing of state controls over financial services, telecommunications and other important areas of the economy. In pressing for these changes, proponents of neo-liberalism argue that the private sector is more efficient than governments in providing goods and services, and that the economy as a whole would benefit from increased competition through lower prices and better quality (Hayek 1976).

While these trends are distinct from the simultaneous shift in financial risk from government and business to individuals and households, they share a common philosophy: the idea that each member of society is responsible for themselves. If they makes good choices, they will be rewarded. If their choices are poor, then they will need to deal with the consequences. The role of government in providing a comprehensive safety net – in pooling risk across the population – is therefore kept to a minimum, since this (according to supporters of neo-liberalism) would encourage too many people to ‘work the system’ (or, in economic parlance, present a ‘moral hazard’). Privatisation, deregulation and the individualisation of financial responsibility has as its ultimate goal what has been called the ‘ownership society’. The Cato Institute, a libertarian think tank based in Washington, D.C., explains that the ownership society:

values responsibility, liberty and property. Individuals are empowered by freeing them from dependence on government handouts and making them owners instead, in control of their own lives and destinies. In the ownership society, patients control their own health care, parents control their own children’s education, and workers control their retirement savings (quoted in Hacker 2006, p. 37).

‘Ownership’ is often equated with ‘share-ownership’ by its advocates. In 1998, Prime Minister John Howard declared: ‘It’s my goal to make Australia the greatest share-owning democracy in the world and I think that is an aspiration that many Australians share’ (quoted in Donoghue *et al* 2003, p. 62). This kind of thinking has also been embraced by the Australian Labor Party. In 2003, Opposition Leader Mark Latham declared:

The workers have had a taste of economic ownership and not surprisingly, they want more. Not the cars and refrigerators that their parents aspired to but real economic assets: shares, investments, business and skills....And they expect an alert and modernised ALP to help them on their way (quoted in Johnson 2003, p. 18).

Following the demutualisation and privatisation of several high-profile corporate institutions – AMP, NRMA and Telstra in particular – the share ownership ‘revolution’ has largely come to pass in Australia: direct ownership of shares grew from 9 per cent in 1980 to a staggering 44 per cent by 2004 (Pixley 2007, p. 286). Yet many of these ‘ordinary’ investors remain relatively unaware of basic financial imperatives and practices. Only 8 per cent of Australians regard themselves as having ‘a lot of knowledge of how the share market works’, according to the Australian Survey of Social Attitudes (Pixley 2007, p. 291). Of more concern, many people own shares in just one or two companies, meaning that they are exposed to the much greater risks associated with an undiversified or unbalanced portfolio. Though nobody invests in order to lose money, professional investors (including institutions) expect to incur some losses, whereas undiversified investors can be wiped out by a single downturn (Pixley 2007, p. 288).

On the pretext of encouraging greater personal responsibility, ordinary people are now asked to make complicated decisions that in the past would have been made by bureaucrats, entrepreneurs or bankers. ‘Mum and Dad’ investors are now forced to come to terms with complex financial concepts and make sophisticated decisions that

will ultimately affect their future standard of living. Indeed, a government review in the United Kingdom concluded that ‘competitive forces in the long-term savings industry actually drive towards greater complexity, not simplicity, of products’ (quoted by House of Commons Treasury Committee 2004, p. 35). The rise in discretionary incomes, the liberalisation of financial markets, and government messages about the need to provide for one’s own retirement have resulted in what Randy Martin has called ‘the financialisation of daily life’, which ‘asks people from all walks of life to accept risks into their homes that were hitherto the province of professionals. Without significant capital, people are asked to think like capitalists’ (Martin 2006, p. 12). In Australia, as Pixley observes, ‘the idea that one can control one’s financial future has become increasingly normalised’ (Pixley 2007, p. 288). The rise of ‘popular’ media formats for reporting on finance and investment – including newspaper liftouts, news segments and even prime-time television programs – attests to how far these developments have pervaded Australian society.

The ownership society and the policies which underpin it represent a marked departure from the social contract that was put in place in Australia after the Second World War, and under the New Deal in the United States. In the ownership society, decent working conditions, adequate health care and unemployment insurance all become the responsibility of individuals in the marketplace rather than government. Jacob Hacker paints a picture of what daily life would be like in a society where personal responsibility is taken to its extreme:

Picture our liberated worker. A hardworking professional, he takes time each morning to check the level of his IRA², rebalance the portfolio in his 401(k),³ see if his medical spending is depleting his Health Savings Account, and make sure the Education Savings Account he set up for his kids is accumulating enough for sixteen or more years of private schooling for his twin daughters. If he were to lose his job, he would draw on his Temporary Unemployment Savings Account – which, of course, he’s diligently contributed to, knowing full well the risks that all professionals face in today’s hyperdynamic, free-agent economy (Hacker 2007, p. 59).

In times of plenty, an increased personal stake in one’s financial fortunes can mean additional benefits for some. During an economic downturn, however, or when misfortune strikes (say in the form of illness or job loss), individuals who have not made provision can be severely penalised. The real personal risks associated with the ownership society can be seen in the number of US citizens who remain without health insurance: 15.8 per cent of the US population, or 47 million people (DeNavas-Walt *et al* 2007, p. 18).⁴ As well, the failure to address the US social security deficit has left a \$44 trillion gap in the ‘generational accounts’, to be remedied through ‘personal savings accounts’ rather than substantial government investment (Bernasek 2003).

In Australia, the situation is not yet so severe. Yet the increased responsibilities and risks that ordinary Australians now bear mean that the stakes in financial decision-

² Individual Retirement Account.

³ A 401(k) plan is an employer-sponsored retirement savings account established under section 401(k) of the United States Internal Revenue Code. In providing a tax concession for retirement savings, 401(k) plans share some features with (voluntary) superannuation in Australia.

⁴ Based on 2006 figures (the most recent).

making are ever growing. At the same time, there is evidence that many people do not value their new role, and in fact resent it. The Australian Survey of Social Attitudes found that ‘despite 20 years of policies designed to devolve responsibility for individual financial futures from the state pension system to individuals, active and risky financial activity remains an unpopular choice for improving people’s wealth’ (Pixley 2007, p. 292) – a finding borne out by the results of focus group discussions convened for this research (see Chapter 4).

2.3 Reforms to financial services

An inquiry into Australia’s financial system, completed in 1997, found that regulation of the sector was ‘piecemeal and varied’, and that the different legal frameworks in operation imposed ‘differing levels of disclosure in relation to the various products’ (Department of Finance and Administration 2001, S. 1.3, 2.31). The inquiry regarded this as ‘inefficient’, because it made it ‘very difficult for consumers to compare different, but functionally similar, financial products’ (Department of Finance and Administration 2001, S. 1.3, 2.31). The *Financial Services Reform Act 2001* (Cth) (FSRA) implemented many of the inquiry’s recommendations, including the call for ‘consistent and comparable financial product disclosure’ across the various parts of the financial system (Department of Finance and Administration 2001, 1.4). The FSRA was intended to ‘give consumers a more consistent framework of consumer protection in which to make their financial decisions’ by applying ‘consistent disclosure requirements to all financial products’ (Department of Finance and Administration 2001, 1.5, 2.33).

Under the FSRA, financial providers are required to provide the following whenever a financial product is offered: a Financial Services Guide (setting out the terms and basis of the service), a Statement of Advice (setting out the basis of advice, where this is provided, as well as the amount and source of any commissions or other remuneration they receive from product providers), and a Product Disclosure Statement (providing the essential details about the product) (ASIC 2007). Reforms to the financial sector also resulted in heavy regulation of financial advisers and their disclosure requirements, fundamentally changing the nature of the relationship between adviser and client (Pearson 2006).

One of the key arguments behind the 2001 reforms was to redress the ‘information asymmetry’ that many retail investors face in making complex financial decisions (Pearson 2006). However, consumers are now ‘unable to comprehend and make use of the elaborate information disclosed to them’ (Pearson 2006, p. 100). Despite support from the financial sector for the intent behind the FSRA, implementation of the reforms turned out to be ‘expensive’, ‘challenging’, ‘complex’ and ‘burdensome’ for industry (Association of Superannuation Funds of Australia 2004). A huge ‘compliance industry’ has grown in response to the FSRA regulations (Pearson 2006). Providers have argued that ‘lengthy and complex documents will not be read and be of little use to investors’, and objected to the way in which the reforms were administered by the Australian Securities and Investments Commission (ASIC) (Association of Superannuation Funds of Australia 2004).

Historically, it had been the practice of many financial providers to make short, user-friendly documents, sometimes of a general or educational nature, available to their customers. Under the new regulatory regime, however, risk-averse corporations are

more reluctant to provide concise information resources as they did in the past, instead just producing the standard documents. The Parliamentary Secretary to the Treasurer, Christopher Pearce, was quoted in 2005 as acknowledging that ‘the end result of FSR has been that the disclosure documents themselves are designed more to manage the liability of the service provider, rather than to inform the consumer’ (quoted in Pearson, p. 123). In response to concerns about the effect of the FSRA, legislative amendments designed to mitigate the complexity of the disclosure requirements were passed in 2003 and 2005 (ASIC 2007).

Despite this, many Australians still regard the documentation they receive from financial providers as overly complex and find it difficult to make meaningful comparisons between financial products, as Chapter 4 reveals. Chapter 3 considers what capacity people have to make sensible financial decisions, and what policies are in place to address shortfalls in financial understanding.

3. Understanding and behaviour in personal finances

The first two chapters of this paper have described broad changes in the environment in which ordinary people make financial decisions. With increased competition among financial providers, there is unprecedented choice in the realm of personal finances. The changing nature of financial risk means that the stakes are higher for many people. This chapter considers whether ordinary people are able to deal with the challenges of financial choice, by presenting existing evidence on how well financial concepts are understood and how people actually manage their finances. An integrated discussion of the focus group and survey findings can be found in Chapter 6.

3.1 Research on financial literacy

Functional literacy

Some level of basic literacy and numeracy is required for people to manage their financial affairs properly. Recent research on adult literacy in Australia, conducted as part of an international study by the Organisation for Economic Cooperation and Development (OECD) and published by the Australian Bureau of Statistics (ABS), found that many people are functionally illiterate. The study explored different aspects of adult literacy, including *prose literacy* ('the ability to understand and use information from various kinds of narrative texts, including texts from newspapers, magazines and brochures'), *document literacy* ('the knowledge and skills required to locate and use information contained in various formats including job applications, payroll forms, transportation schedules, maps, tables and charts') and *numeracy* ('the knowledge and skills required to effectively manage and respond to the mathematical demands of diverse situations') (ABS 2006b, p. 4). In each area, literacy levels are divided into five 'skill levels', with Level 1 being the lowest and Level 5 the highest. For the purposes of analysis, Level 3 is regarded as the 'minimum required for individuals to meet the complex demands of everyday life and work in the emerging knowledge-based economy' (ABS 2006b, p. 5). In other words, individuals placed at Levels 1 or 2 are functionally illiterate.

The research results indicate that 17 per cent of Australians are at Level 1 on the prose literacy scale, 18 per cent are at Level 1 on the document literacy scale, and 22 per cent are at Level 1 on the numeracy scale. In other words, around one in five Australians are within the lowest category for these key aspects of functional literacy (ABS 2006b, p. 16-8). If the official definition of functional literacy is used, the figures are much higher: 46 per cent of Australians are functionally illiterate on the prose scale, and 47 per cent on the document scale. More than half of Australians (53 per cent) are also functionally innumerate, using this definition – suggesting that a great many people will struggle to interpret financial information. There are also particular population groups with lower rates of functional literacy, including young adults (16-19 year olds) and older people (55 and older), the less educated and people on lower incomes (ABS 2006b, p. 7-9). Compared with the other (developed) countries involved in the study, Australia ranks in the middle, with Norway and Switzerland having the highest levels of functional literacy (ABS 2006b, p. 8).

Defining financial literacy

Around the world, there has been widespread recognition that many people do not possess the skills and knowledge they need to make sensible financial decisions. This has led to a great deal of research into financial literacy and the factors that lead to poor financial decision-making.

Before describing the results of this research, it is worth considering what financial literacy actually is. This threefold definition, derived from the work of the United States Federal Reserve, is a useful one: (1) ‘being knowledgeable, educated, and informed’ about ‘managing money and assets, banking, investments, credit, insurance and taxes’; (2) ‘understanding the basic concepts underlying the management of money and assets’, such as ‘the time value of money in investments and the pooling of risks in insurance’; and (3) ‘using that knowledge and understanding to plan and implement financial decisions’ (Hogarth 2002, pp. 15-6).

The third criterion is crucial, since it refers to how people translate their knowledge into action. How well they are able to do this depends on both the *cognitive* elements of financial literacy (e.g. do they understand the relevant financial concepts?) and the *psychological* elements (e.g. do they enjoy making financial decisions or find it unpleasant?). The psychological elements of financial decision-making include thought processes with an emotional dimension: confidence, procrastination, fear of old age, and even boredom. Any discussion of financial literacy would be incomplete without addressing its psychological dimensions, since these can override rational or cognitive considerations.

Types of research

Because financial literacy is multifaceted, there are different ways that it can be assessed. A common way is simply to ask people how well they understand financial concepts, for example in the form of a survey. This approach can be valuable in determining how people *feel* about financial issues, but self-reported responses can be influenced by a respondent’s attitudes towards particular aspects of money and finance, and do not necessarily provide an accurate indication of their conceptual understanding of finance. Testing knowledge, on the other hand, can involve presenting people with fact-based questions to which there are objectively true and false answers. Such ‘quiz-style’ techniques allow researchers to develop a better picture of where the real shortfalls in conceptual understanding are. It also lets them compare people’s *actual* knowledge with their *self-perceived* knowledge – for instance to work out whether their level of confidence actually reflects their decision-making abilities.

Another way to assess financial competence is to look at actual *behaviour*. This approach is particularly suited to the financial sector, where accurate records of transactions allow patterns of behaviour to be inferred. This kind of research has contributed much to the emerging field of behavioural economics, discussed later in this Chapter.

Financial literacy in Australia

A number of studies into financial literacy have been carried out in Australia in recent years. The first major population-wide study was ANZ Bank's 2002 survey research on *Adult Financial Literacy, Personal Debt and Financial Difficulty*, which was followed up with a similar survey in 2005 (ANZ 2005).⁵ This research included 'quiz'-style questions designed to test financial knowledge and competency (including basic numeracy), as well as questions about attitudes to financial issues. The authors of the 2005 report concluded that 'Australian society is financially literate, but ... certain groups have challenges that need to be addressed, and certain financial skills, services and products are not as well understood or utilised as they should ideally be' (ANZ 2005, p. 2). Evidence for such an encouraging overall assessment included the high level of 'banking inclusion' in Australia compared with other countries;⁶ the fact the great majority felt 'well informed' when making financial decisions; that knowledge of electronic payment methods had risen over time; and that respondents had a good basic understanding of superannuation (ANZ 2005, p. 2).

Despite these apparently positive results, the ANZ research also uncovered a range of problems. It found that certain population groups tend to have quite poor financial literacy – including people with less education, people who are not in work, people on lower household incomes (less than \$20,000 per year), single people, and both young adults (18-24 years) and older people (over 70 years). Further, although 'the population as a whole had reasonably good mathematical skills', the bottom 20 per cent of respondents scored particularly badly on questions testing basic numeracy, with half of these people being 'unable to calculate 50 per cent of \$1,400'. Other results pointed to real problems with financial literacy across the Australian population. When asked about an investment advertised as having 'a return well above market rates at no risk', 47 per cent of survey participants said they would invest in such a scheme. Around a third of respondents who indicated having an investment of some kind 'did not understand that good investments can have short-term fluctuations'. Sixty per cent 'did not recognise that an adviser who works only for fees was more likely to offer impartial advice than advisers who work for commissions'. The research findings also suggested that many people have not taken adequate steps to ensure they can meet their income aspirations in retirement (although awareness of the need to do so appeared to be improving). Only 54 per cent of those with superannuation 'were aware that it is taxed at a lower rate than other investments'. Taken together, these results indicated that many Australians experience problems understanding important financial concepts and imperatives, and that their financial situation could suffer as a result (ANZ 2005, pp. 2-6).

In recognition of the need to improve financial literacy, the Australian Government established a Consumer and Financial Literacy Taskforce (hereafter known as the 'Government Taskforce') in 2004. The Taskforce recommended that a national financial literacy body be created, and that ongoing research be conducted into the factors affecting consumers' financial decision-making (Consumer and Financial Literacy Taskforce 2004). The first major research report by the new Financial

⁵ The 2005 survey was based on a sample of 3,500 adult Australians and carried out by AC Nielson (ANZ 2005).

⁶ In this context, 'banking inclusion' means to hold an everyday bank account.

Literacy Foundation, *Financial Literacy: Australians Understanding Money*, was released in August 2007.⁷ It found that many Australians are confident with ‘everyday management issues like dealing with credit, budgeting, saving and managing debt’, but find it harder to deal with ‘more complex issues like investing and ensuring enough money for retirement’ (Financial Literacy Foundation 2007, p. vii).⁸ The study uncovered evidence that imprudent financial practices are widespread. For example, 66 per cent of survey respondents ‘would not consider both risk and return when choosing an investment’, while 21 per cent said they would ‘use debt to buy things they can’t afford’. One in five people (22 per cent) said they do not spend a lot of time thinking about financial information before making a financial decision (Financial Literacy Foundation 2007, pp. viii-ix).

Much of the Financial Literacy Foundation’s research addressed the *psychological* dimensions of money management. According to its survey results, fully 48 per cent of Australian adults say that ‘dealing with money is stressful and overwhelming’, while 31 per cent say that ‘dealing with money is boring’. Meanwhile, 40 per cent of adults say that thinking about their long-term financial future makes them ‘uncomfortable’ (Financial Literacy Foundation 2007, pp. 41-6). As the authors of the report observe, the survey revealed ‘a range of money attitudes and beliefs that are inimical to people investing the time and effort required in taking the steps to improve their money skills and behaviour.’ These included ‘stress and discomfort, boredom and disinterest, and personal relevance and procrastination’ (Financial Literacy Foundation 2007, p. xii). The report provides a useful account of the interplay between different psychological characteristics and people’s actual financial behaviour:

Where people are confident in their ability but exhibit behaviour that could not be characterised as financially literate, there may be attitudes or beliefs at play which impede either awareness of the need to learn, or the progression from awareness to learning and action. For these people, a perceived lack of relevance or importance, rather than technical ability, appears to be a more significant factor in determining outcomes (Financial Literacy Foundation 2007, p. 39).

The Financial Literacy Foundation’s research supports the notion that financial behaviour is as much the result of psychological disposition as conceptual understanding. Those who seek to improve financial practices therefore need to address individual motivations as well as shortfalls in understanding. While there is evidence to suggest that increasing understanding itself increases motivation and interest in money matters (Ameriks *et al* 2003; Lusardi and Mitchell 2006), attention also needs to be paid to the individual factors which influence people to learn more about personal finances and act on that knowledge. The Financial Literacy Foundation acknowledges that ‘a key consideration to emerge’ from its research is ‘the practicalities of building pathways to effective consumer engagement with money issues – of putting appropriate emphasis on motivation in design and delivery

⁷ The research was based on a survey of 7,000 Australians aged between 18 and 75 and 553 Australians between 12 and 17 (Financial Literacy Foundation 2007).

⁸ Forthcoming research from the Australia Institute will explore community attitudes to consumer spending, debt and corporate lending practices.

strategies by promoting the personal relevance of money management’ (Financial Literacy Foundation 2007, p. xii).

The Financial Literacy Foundation’s research also included valuable insights into financial literacy and behaviour among young people and women. An additional survey of people aged between 12 and 17 years allowed the responses of young people to be compared to the larger survey of adults. The proportion of young people agreeing that they ‘have the ability to deal with credit cards’ was almost half that of adult respondents (83 per cent compared with 44 per cent). Reflecting a wider lack of awareness about the importance of risk and return, 61 per cent of young people said they would not consider return and 77 per cent said they would not consider risk when choosing an investment. Overall, the research report observes that ‘young people are less confident than adults when it comes to managing money’, although they are ‘reasonably well informed about good money habits, even if they don’t always put them into practice’ (Financial Literacy Foundation 2007, p. 57). However, in its report the Foundation does not address whether young people of different ages are less proficient or diligent than they ‘should’ be in order to make everyday financial decisions.

Some interesting differences between women and men emerged from the Financial Literacy Foundation’s Research. Women reported managing their everyday expenses better than men, but were less confident about more complex and longer-term financial issues like investing and retirement planning – although many women hope to learn more about such matters (Financial Literacy Foundation 2008a). Generally speaking, women are less engaged with financial issues, being more likely than men to ‘find money stressful, uncomfortable or boring and less likely to feel in control of their financial situation’ (Financial Literacy Foundation 2008a, p. 5). Another recent report on women’s attitudes to money was produced by WIRE, and was based on qualitative research with more than 300 women. It found that women tend to think about money based on their own life experiences, and that it is often significant life changes – like job loss, divorce or death – which prompt learning and initiative among women. The study found that women are ‘generally fearful about money’, and feel ‘overwhelmed’ and ‘embarrassed’ by gaps in their knowledge of financial matters, and that ‘feelings of hopelessness, shame and inadequacy ran deep across all socio-economic groups’ (WIRE 2007, p. 5). The research also found that the language and style of financial specialists is a major barrier for women, and that many participants were ‘wary, distrustful and reluctant to engage these types of professionals unless they were highly recommended by someone they trusted’ (WIRE 2007, p. 6). These lessons also applied to information about financial products, which can ‘often alienate women’ (WIRE 2007, p. 6).

In 2006, Reconciliation Australia released the results of community consultations on the topic of money management with Indigenous people (Urbis Keys Young 2006). This project involved qualitative research with 133 community participants and 17 service providers, and found that areas of need include ‘skills such as budgeting, managing debt and exercising consumer rights’, along with advice and counselling on financial issues. The report describes cultural barriers to Indigenous people using the services of financial providers, as well as significant geographical barriers to access for those living in remote areas. Research with Indigenous community members found distinctive patterns in the way they managed their money. These included

focussing on 'immediate monetary needs' rather than saving; incurring 'significant debt by the time they focus on money management'; not fully understanding the role of a credit history or the true cost of credit; not comparing different products in order to choose the most appropriate; being unaware of their consumer rights; and being 'uncomfortable questioning banks about issues or problems' (Urbis Keys Young 2006, p. ii). In addition, the research also indicated that Indigenous people can 'have some difficulty in understanding communications from financial institutions, especially written communication'; some research participants believed that 'financial institutions do not understand, or take any interest in, how Indigenous people live'. The research found that some Indigenous people do not fully appreciate how different terms can affect loan repayments and the total cost of loans (Urbis Keys Young 2006, p. iii). Although no direct comparisons were made between the financial practices of Indigenous and non-Indigenous people, these consultations revealed how Indigenous people often struggle with basic financial knowledge and skills.

Another important study into how the broader Australian population feels about financial issues was conducted as part of the Australian Survey of Social Attitudes in 2005, which included questions framed around share ownership and investment risk. While survey results revealed poor (self-rated) knowledge of the workings of basic financial institutions like the Reserve Bank of Australia and the Australian Stock Exchange, of even more interest were findings on how people respond to financial decisions at an emotional level. Almost half of survey participants (45 per cent) agreed that they 'worry a lot' about their financial future, while only 28 per cent disagreed. Women were more likely than men to be worried about their financial future, and people renting their home were more likely to be worried than people who owned their own home. Around a third of the survey sample (30 per cent) agreed that they were 'willing to take on risks or loans for shares and investment property to improve [their] wealth', while half (49 per cent) disagreed. Men were more willing to take such risks, as were people on higher incomes (especially households earning over \$100,000) and older people. Thirty-four per cent agreed that they 'enjoy having a wide range of choices to search constantly for the best financial gains', while 18 per cent disagreed, with a large proportion (48 per cent) remaining neutral. People on lower incomes were less likely to enjoy financial choice, as were women (Pixley 2007, pp. 290-6) and older people. According to the study's author, these 'attitudinal patterns ... suggest that most Australians are not willing to take financial risks and debts to buy shares and investment property, especially on a continuous basis. Low income and older people resoundingly reject such strategies' (Pixley 2007, p. 300).

International research

Of course, problems with financial literacy are not restricted to this country. Studies conducted in the US, the UK, Japan, Korea and other developed nations have shown that shortfalls in both understanding and motivation contribute to poor financial outcomes. The OECD published a major study of financial literacy and financial education at the international level in 2005. Its report, *Improving Financial Literacy: Analysis of Issues and Policies*, included a review of financial literacy surveys across twelve nations. The results showed that 'many consumers have little knowledge about common financial products and lack information on such basic financial issues as the relationship between risk and return'. Financial literacy is particularly low for certain population groups, including 'the less-educated, those at the lower end of the income

distribution, and minorities' (OECD 2005, p.45). Consumers in various countries encountered difficulties finding and interpreting information on financial products, with a British survey finding that the information that people ultimately receive 'is acquired by luck or chance or hazard, for example, by picking up a pamphlet at the bank or having a chance talk with a bank employee' (OECD 2005, p.45). When people seek advice from a financial specialist, they tend to 'accept without question' what is recommended, rather than checking the adviser's bona fides or asking sensible questions (OECD 2005, p.46).

Another important finding of the OECD review was that consumers tend to be *over-confident* in their own financial competency: that is, survey participants 'often feel they know more about financial matters than is actually the case' (OECD 2005, p.46). Over-confidence can prevent people from seeking out information they really need and from taking steps to improve their general financial understanding. The OECD's findings are supported by the results of a German study, which found that while 80 per cent of survey respondents were 'confident in their understanding of financial issues', only 42 per cent could correctly answer survey questions on those issues (Lusardi and Mitchell 2006, p. 8).

3.2 Irrational financial behaviour: the evidence

Behavioural economics is a relatively recent field of study which seeks to integrate the lessons of psychology with an economic account of human behaviour. In orthodox economic theory (described in Chapter 1), human beings are strictly rational creatures who make choices by carefully assessing the costs and benefits of each option. As a result, 'virtually all the behaviour studied by cognitive and social psychologists is either ignored or ruled out' (Mullainathan and Thaler 2000, p. 2). Behavioural economics provides an account of decision-making that conveys the many ways in which choices deviate from the rational model.

Behavioural economics owes much to the work of Daniel Kahneman and Amos Tversky, whose Nobel Prize-winning 'prospect theory' describes how people in the real world make choices when faced with uncertainty. So called 'anomalies' in economic decision-making include the *endowment effect*, 'the fact that people often demand much more to give up an object than they are willing to pay for it'; *status quo bias*, 'a preference for the current state' over apparently better options, and *loss aversion*, the tendency to think that losses 'loom larger than improvements or gains' (Kahneman *et al* 1991, pp. 194, 199). Without providing a full explanation of prospect theory or other decision-making models, it is sufficient to say that the ways in which real-world decisions do not comply with quantifiably 'rational' predictions are many and diverse.

There are different ways that behavioural economists can study how people make judgements in the real world. The first is to gather pre-existing data (say on certain types of financial transactions) from which they can make inferences. For example, Iyengar, Jiang and Huberman (2003) have examined the effects of greater and lesser choice on the uptake of opt-in retirement savings accounts in US workplaces, known as 401(k) plans. By analysing employee data, they found that participation in 401(k) plans is noticeably higher *where fewer options are presented to employees*. The researchers speculate that 'perhaps in attempting to provide employees with a generous number of 401(k) options, employers may actually intimidate rather than

induce employees to invest in personal retirement plans' (Iyengar *et al* 2003, p. 10-1). This study provides strong evidence that in particular situations, too much choice for financial decision-makers can in fact impede their welfare rather than enhance it.

A second option open to behavioural economists (and psychologists with an interest in financial behaviour) is to conduct controlled experiments. Shlomo Bernatzi and Richard H. Thaler have conducted numerous experiments which undermine the proposition that people always make rational decisions about their finances. In one example, participants were asked to decide between various options in which identical information was presented in different forms. The results showed that people tend to invest more in stocks if they are shown long-term rather than short-term rates of return. The researchers conclude that 'the manner in which the information is provided will influence the choices [that people] make' (Bernatzi and Thaler 1999, p. 380). In another experiment, participants were asked to pick between their pre-existing portfolio choices and the median choice, based on the expected distribution of financial outcomes. The majority actually selected the median option rather than preferring the choices they had already made. Discussing the findings, Bernatzi and Thaler observe that 'most participants simply do not have the skills and/or information available to pick portfolios that line up with their risk attitudes' (Bernatzi and Thaler 2002, p. 1595). In fact, experimental results indicated that ordinary people investing for their retirement could end up reducing their 'expected utility' (i.e. their savings) by as much as 37 per cent as a result of such biases in decision-making. The authors conclude that their participants' choices 'are not rational according to standard economic criteria' (Bernatzi and Thaler 2002, p. 1610).

A third way that behavioural economics can study real-world behaviour is to use empirical data as the basis for economic modelling. Such models can then be extrapolated to glean more general rules governing the way decisions are made. The endowment effect, status quo bias and loss aversion are good examples of general rules that have been developed from empirical observations.

Some of the most valuable lessons of behavioural economics relate to how *time* can affect decision-making. Time is particularly important in the context of personal finances, since today's actions can have a major impact on financial outcomes many years from now. Some have argued that *procrastination* is an important factor in explaining apparently non-rational choices. They have used the notion of 'hyperbolic discounting' to convey how people tend to place much greater value on the present and the immediate future than the longer-term future – even taking into account standard approaches to time discounting (otherwise as 'exponential discounting') (Laibson 1997). As O'Donoghue and Rabin explain, 'procrastination follows as a natural consequence of "present-biased" preferences ... in which people discount delays in gratification more severely in the short term than in the long term' (O'Donoghue and Rabin 1998, p. 2). They conclude that 'people will tend to keep their retirement savings in their existing investment plan even when it is not optimal because they never got around to switching' (O'Donoghue and Rabin 1998, p. 25). Others argue that there is a great deal of power in inertia: 'Even a trivial action, such as filling in some form and returning it, can leave room for failures due to memory lapses, sloth and procrastination' (Sunstein and Thaler 2003, p. 1181). This kind of description is much closer to a common understanding of how everyday financial decisions are made than is the rational-choice model advocated by orthodox

economists. It is also backed up by focus group participants' accounts of their own behaviour, discussed in Chapter 4.

Another way to characterise seemingly inexplicable behavioural patterns is through the notion of *self-control*. The standard 'life-cycle model' of consumption predicts that people will smooth their expenditure out over the course of their lives to reach some degree of equilibrium. The life-cycle model is not borne out in the real world, where it has been shown that levels of consumption tend to track income; that is, people tend to spend more when their incomes are higher and less when their incomes are lower. In other words, people usually do not possess the self-control or foresight to manage their consumption in strictly rational fashion. It has been argued that lack of self-control explains the fact that 'virtually all savings done by Americans is accomplished in vehicles that support "forced savings"', such as home mortgages and retirement saving schemes (Mullainathan and Thaler 2000, p. 9). Indeed, as Avner Offer has shown, much of the developed world has surprisingly low rates of household saving. The main English-speaking countries (the US, the UK, Canada and Australia) have in fact 'relied increasingly on society, by means of commitment technologies, to do their saving for them' (Offer 2006, p. 66).

Interestingly, people often realise that they lack the self-control to act prudently all the time, so they take measures to 'impose' control on themselves. For example, observers have noted that people distinguish, in ways that are not always rational, between 'categories' of money destined for different purposes – even though money is usually completely fungible (that is, one dollar is the same as any other dollar). Richard Thaler has termed this phenomenon 'mental accounting', and has documented how people place their (present and future) money into different categories, even when this jeopardises their overall financial situation. Here is an example:

'Mr and Mrs J have saved \$15,000 toward their dream vacation home. They hope to buy the home in five years. The money earns 10% in a money market account. They just bought a new car for \$11,000 which they financed with a three-year car loan at 15%' (Thaler 1985, p. 199).

In this instance, as Thaler points out, 'the violation of fungibility (at obvious economic costs) is caused by the household's appreciation for their own self-control problems' (Thaler 1985, p. 200). This kind of situation should be familiar to many readers, though it stands outside the rational model of human behaviour.

Another interesting insight from behavioural economics relates to overconfidence, which as we have seen is actually a contributor to poor financial literacy at the population level. Overconfidence helps explain a puzzling characteristic of financial markets – that millions and millions of shares are traded every day, both by institutional and individual investors, even in the absence of trustworthy information about their respective value. Taken together, these many trades impose sizeable transaction costs, and many investors end up losing money. In a rationally efficient market, there would be very little trading (because the information available would not be enough to prompt it), and certainly not the volume that is witnessed every day. Overconfidence means that investors continue to trade even without the right information (Mullainathan and Thaler 2000).

Research from Sweden has examined the effects of advertising on the investment decisions that people make. Most advertising for mutual funds is of the ‘non-informative’ kind; that is, it provides little objective information about the quality of the investment. However, such advertising has been shown to have a considerable impact on the portfolio choices that investors make (Cronqvist 2003). As the author of this study concludes:

Rather than informing individual investors, eliminating behavioural biases that individual investors might have, fund advertising seems to play on and exacerbate such biases. And, rather than steering investors towards better portfolio choices, fund advertising sometimes leads people astray (Cronqvist 2003, p. 28).

Even more worrying is the finding that women and young people, who rated themselves as less knowledgeable about such decisions, were actually the most susceptible to the influence of such advertising. One of the clear implications of this research is that ‘the market, through fund advertising, will likely not solve the problem of lack of investor knowledge in the general public’ (Cronqvist 2003, p. 31).

There is of course also evidence from outside the field of behavioural economics indicating that consumers often make irrational financial choices. The Government Taskforce found that ‘a good proportion of Australian households and small businesses are underinsured or not properly insured’ – up to 40 per cent by industry estimates (Consumer and Financial Literacy Taskforce 2004, p. 27-8). Research by ASIC on *Consumer Decision Making at Retirement* found that ‘the vast majority of people thought little about their superannuation until retirement or retrenchment was imminent’ (ASIC 2004, p. 2). ‘Mum and Dad’ share-owners often hold stock in only one or two companies, despite the need to diversify if investment risk is to be properly mitigated (Botti and Iyengar 2006).

The extent to which people are being ‘scammed’, or lured into risky or simply dubious investment schemes, is a telling measure of how well the population is able to make rational financial decisions. The Australian Institute of Criminology (AIC) uses a simple system to classify scams: *advanced fee schemes* (‘pretending to sell something you do not have while taking money in advance’); *non-delivery and defective products and services* (‘supplying goods or services of a lower quality than ... paid for, or failing to supply ... at all’); *unsolicited or unwanted goods* (‘persuading consumers to buy something they do not really want through oppressive or deceptive marketing techniques’); and *identity fraud* (‘gaining money, goods, services or other benefits, or the avoidance of obligations through the use of a fabricated, manipulated, or stolen/assumed identity’) (Smith 2007, p. 1). In its 2007 Report on consumer scams in Australia, the AIC’s chief criminologist admitted that ‘only limited data are available on the nature and extent of consumer fraud victimisation’, but nonetheless claimed that ‘large numbers of consumers are targeted by fraudsters each year’ (Smith, 2007, p. 9). Beyond outright ‘scams’ is the grey area of high-risk investments. In 2005, ASIC undertook extensive surveillance of ‘high yield debentures’ and discovered that ‘more vulnerable investors, especially retirees, have been the target of these riskier investments.’ Such high-risk investments have been linked to ‘aggressive or misleading advertising, poor disclosure about property developments, related-party transactions, and bad and doubtful debts’ (ASIC 2005).

3.3 Government investment in financial literacy

Over recent years policy-makers around the world have come to recognise what the body of research clearly indicates: that many people struggle with basic financial concepts, and that consumers do not always act in their own financial interests. One of the standard policy responses centres on the need to improve levels of financial literacy, both at the population level and among specific target groups. The European Commissioner for Internal Market and Services, for example, has said that:

People who understand their financial circumstances, and the options or advice available to them, are more likely to make sensible choices and make adequate provision for the future. They are less likely to have purchased products that they don't need, be tied into services that they don't understand, or take on risks that have the potential to drive them towards insolvency (McCreevy 2007, p.2).

In similar fashion, the managing director of the International Monetary Fund has argued that the 'implications of the shift in the location of risk is that individuals need to take more responsibility for managing financial risks themselves. Therefore, they need to be educated consumers for financial information' (de Rato 2007, p. 3).

The Australian Government has responded to the financial literacy shortfall with a number of initiatives. Most significantly, it established the Financial Literacy Foundation in 2005. The Foundation conducts public awareness campaigns in the media, works with schools to promote the use of financial education in curricula, conducts research into financial literacy, encourages financial education in the workplace, and – because there is already a wide range of non-government activity in this area – has established a database of financial literacy resources available in Australia. In 2006, the Foundation launched a website (www.understandingmoney.gov.au) which 'offers a wide range of financial literacy information for people who want to find out more about managing their money', and includes a budget planner, a financial health check information about saving, investing, superannuation, debt, education expenses and even buying a mobile phone (Financial Literacy Foundation 2008b). The Foundation also played a major role in having financial literacy integrated into the curriculum for all Australian schools from 2008 onwards, and has worked to support teachers in the delivery of financial literacy education (Financial Literacy Foundation 2008c).

The Australian Government's Financial Information Service, run through Centrelink since the late 1990s, is an education and information facility available to all Australians. It runs seminars on various financial issues (most of which focus on planning for retirement), and also provides information and advice in one-on-one sessions (Centrelink 2008). According to Centrelink's annual report, in 2006/7 the Financial Information Service's officers fielded around 200,000 phone calls, conducted 80,000 'interviews', and held 7,000 hours of 'outreach' (i.e. seminars) for more than 100,000 participants (Centrelink 2007, p. 59).

The work of the Department of Families, Housing, Community Services and Indigenous Affairs includes a number of initiatives relevant to financial literacy. It

funds the National Information Centre on Retirement Investments, ‘a free, independent, confidential service that aims to improve the level and quality of investment information provided to people who are investing or facing redundancy’ (National Information Centre on Retirement Investments 2008). It also oversees Commonwealth Financial Counselling, which funds community organisations and local government ‘to provide free financial counselling services to people who are experiencing personal financial difficulties’ (FAHCSIA 2008).

Another online initiative of the Australian Government is www.privatehealth.gov.au, its recently launched website designed to help people compare private health insurance providers and policies. As well as providing general background information about private health insurance in Australia, the website allows visitors to access one page statements on different policies, to view a comprehensive list of insurers, and to check if particular private hospitals are covered by different insurers. This website arose from research that found that many Australians are confused about private health insurance and would benefit from ‘independent advice for consumers on private health insurance and information that would assist in comparing products’ (Blue Moon 2006, p. 3).

ASIC, the Australian Prudential Regulation Authority (APRA) and the Australian Competition and Consumer Commission (ACCC) all undertake activity to keep the public informed about high-risk investments and financial scams. The foremost consumer-oriented initiative in this regard is SCAMwatch, a program run by the ACCC. Its purpose is ‘to provide information to consumers and small business about how to recognise, avoid and report scams’. To this end, the ACCC also works alongside ‘state and territory fair trading agencies to promote awareness in the community’ (ACCC 2008). ASIC, which administers consumer protection regulation in the financial services sector, has a website dedicated to providing information to help consumers understand the financial system and protect themselves against scams (www.asic.gov.au/fido/fido.nsf).

These programs are all Australian Government initiatives. There are a great many other programs, run by state/territory governments, the private sector and community groups, aimed at improving financial literacy across various target groups. In fact, in 2004 the Taskforce identified more than 100 organisations delivering over 700 consumer and financial literacy programs (Consumer and Financial Literacy Taskforce 2004, p.49). Despite the growth in popularity of financial education, it is not clear that simply providing information and education is the only policy approach available to mitigate the impact of poor financial decision-making. To properly respond to ‘non-rational’ financial behaviour requires more than information and education – however successfully this might be delivered. Chapters 4 and 5 present the feedback of ordinary Australians about financial decision-making, based on the results of focus group and survey research. In Chapter 6, these policy implications are considered in more detail.

4. Talking about finances

This report has so far described the broad context in which Australians are asked to make financial decisions, and presented existing evidence on how well they are able to make such decisions. In this Chapter, we explore the findings of a series of focus groups held with ordinary Australians about financial decision-making. In Chapter 5, the results of a nationwide survey about financial issues are reported.

4.1 Focus group methodology

Six groups were carried out, each of which included between seven and nine participants, selected by an independent professional recruitment firm. The groups were held in Wollongong, Canberra and Adelaide in late September and early October 2007.

In order to represent a broad cross-section of society, the six groups were comprised of between seven and nine participants in specific age and income categories, with each group including a mix of genders. Two groups were held with people 18-29, 30-49, and 50-70 respectively. Within each age range, one group was with people of below-average incomes, while the second group was with people of above-average incomes.⁹

The groups ran for 90 minutes each, and were based on a structured discussion guide (reproduced in Appendix A). Topics covered included: participants' general feelings about their finances; the time it takes to gather and interpret information in order to make a financial decision; the nature of that information; the amount of choice they have in making financial decisions; mortgages and loans; retirement and superannuation; investments; and private health insurance.

Some of the topics of group discussion, while valuable and interesting, were not directly relevant to the present study. Additional focus group findings relating to superannuation and corporate lending practices will be reported in separate Australia Institute publications.

⁹ Among the two groups with younger people (18-29), a mix of people still living at home (i.e. with their parents) and living independently was recruited, so that the different financial circumstances that young people face was adequately represented. In each of the four groups with people aged 30-49 and 50-70, there were at least two couples (or four participants) in attendance; this was done in order to observe the dynamic among partners and in acknowledgement that financial decisions are often made jointly. The two older groups (50-70) included people who were working, semi-retired and fully retired, so as to take into account the financial implications of these different situations. Average income was determined in different ways for different groups. Groups 1 and 2 (18-29) were split according to median *personal* income, while the rest of the groups (30-49 and 50-70) were split according to median *household* income. The figures used were based on the results of Wave 5 of the Household Income, Labour Dynamics in Australia (HILDA) Survey. Further details on the specifications of each group are provided in Appendix B.

Table 1 Focus group breakdown

Group	Age range	Income range	Other specifications
1	18-29 (younger)	Lower	Mix of people living at home and living independently
2	18-29 (younger)	Higher	Mix of people living at home and living independently
3	30-49 (middle aged)	Lower	At least two couples
4	30-49 (middle aged)	Higher	At least two couples
5	50-70 (older)	Lower	At least two couples Mix of workers, semi-retired and fully retired
6	50-70 (older)	Higher	At least two couples Mix of workers, semi-retired and fully retired

4.2 Financial trends

Choice and complexity

There was virtually unanimous agreement among all focus group participants regarding the complexity of many of the financial products and services currently available to ordinary consumers. There was also a general consensus that personal finances are becoming increasingly complicated over time, and are likely to keep doing so in the future. A number of people recounted experiences about investigating a financial product only to find the range of choice to be bewildering. Many participants, and particularly people over 30, bemoaned this state of affairs.

It's just day-to-day things, like mobile phone contracts or your electricity. What sort of a genius can work out which of these five or six options is the best one? (50-70, Adelaide, higher income)

It's very overwhelming. (30-49, Wollongong, lower income)

You might have the best intentions, but you sit down with it all and never get through it all. So you need to come back to it again and again. (30-49, Wollongong, lower income)

Even our credit union had seven or eight different types of home loan. And I'm thinking, 'I just want to buy the bloody house'. (50-70, Adelaide, higher income)

While many people were positive about the notion of choice *per se* – particularly in encouraging healthy competition between providers – some did not approve of extensive choice in specific areas of finance, such as superannuation or home loans, because they believed that people making such decisions are not always fully informed about all their options or the consequences of their choices. The growing

complexity of financial decisions made these participants ambivalent about the benefits of choice in their financial affairs.

It's a good thing to have choice, but you need clarity. (18-29, Sydney, higher income)

I get confused by the number of soap powders in the supermarket. You don't know which one is actually better. It's like that with financial products too. (50-70, Adelaide, lower income).

Other participants, meanwhile, were quite positive about greater choice in financial matters, regarding it as a positive development even where it brings more complexity. These people pointed to the benefits of competition and associated gains for consumers, such as lower prices, the ability to tailor products to individual circumstances, and alternative scenarios involving market domination.

More choice means cheaper products. (50-70, Adelaide, lower income)

Our needs are all different. There are so many different individuals with different circumstances. I don't know how you could simplify it, given where we're at in society. (50-70, Adelaide, higher income)

It's fair to have to make these decisions, because if we didn't make them who would make them for us? (30-49, Canberra, higher income)

Generally speaking, it was older and lower-income participants who were more hesitant about greater choice in personal finances, while the younger and higher-income groups were more positive about the current situation and the benefits of choice. Younger participants (18-29) in particular appeared to regard greater choice as intrinsically good, whereas people over 30 were more sceptical about its benefits.

It's just life. It's good that we have so many choices. (18-29, Sydney, higher income)

The more choice you have, the more you excel. If you make the effort to go through all the options, then you should come out on top. (18-29, Sydney, higher income)

Many people recalled receiving information of a financial nature that was so difficult to interpret that they suspected financial organisations often *set out* to confuse their customers. While it was acknowledged that there are legal constraints on what information needs to be disclosed, participants felt that in many cases nothing is done to make relevant information apparent to consumers.

They put in all this legal jargon [into financial documents]. It's a way of getting people not to read it. (50-70, Adelaide, lower income)

I have to read it over six times before I can understand it. It's like lawyer-speak. (50-70, Adelaide, higher income)

The banks never make it explicit exactly what they're going to do. When there's an interest rate rise, they call it something obscure like a rate adjustment'. (30-49, Canberra, higher income)

Banks set out to cover themselves. And if that means sending you 12 pages of documents you'll never read, that's what they'll do. (30-49, Canberra, higher income)

There was a common perception that financial products are often essentially the same across different providers, at least at some basic level. Fees, charges and returns may be calculated and presented in different ways, but when compared properly there is little difference between them. Some participants believed that financial institutions deliberately make their products difficult to compare with the competition.

They're all subtly different for marketing purposes. (30-49, Wollongong, lower income)

Their method is to present costs and prices in a deliberately complicated way, so the average bloke has Buckley's of working it out. (50-70, Adelaide, higher income)

Some older participants pointed out that it is sometimes difficult or impossible to work out whether the right choice has been made in the context of financial products and services. For these participants, the notion of choice was a troublesome one in the context of financial products.

You may not live long enough to work out whether your choice is better. (50-70, Adelaide, lower income)

As noted in Chapter 1, whereas other goods and services are purchased and consumed over a relatively short time frame, it can take many years to ascertain the true rate of return or cost of some financial products. Interestingly, it was older participants which drew attention to this issue, while younger people did not mention it – despite the fact that it is precisely young people who need to make decisions which can have ramifications much later in their lives.

A number of people commented that the level of understanding required to be successful in 'playing the share market' was daunting, and most participants (including most share-owners) admitted that they had neither the time nor the inclination to acquire such knowledge.

I gave up trying to work out the stockmarket. It's just too complicated. (50-70, Adelaide, higher income)

People don't really understand what they're getting. You wonder what else you think you understand but don't know all the intricacies and permutations. (50-70, Adelaide, higher income)

Investing in the stockmarket – it's serious gambling. (50-70, Adelaide, higher income)

I tried options trading once. It's complicated. I did it for something different. I went to a seminar and got a bit excited, and then I lost quite a bit of money and thought, 'This is just gambling', so that was the end of that. (30-49, Canberra, higher income)

I have shares. But it's a long-term thing. You buy them and then hold onto them. That way you're not subject to the movements of the market from day to day. (50-70, Adelaide, higher income)

There was unanimous agreement on how complicated health insurance policies can be and how difficult it is to understand the various options available. Participants reported spending a great deal of time trying to interpret the available information when they wanted to join a health fund or change providers. In fact, the complexity of the information appeared to influence the basic decision about whether or not to have health insurance.

I couldn't make any sense of the information about the various health funds. (50-70, Adelaide, lower income)

Health insurance is a bloody minefield. (50-70, Adelaide, higher income)

You'll get some of this, and a bit of that, and less of that other thing, and you've got to work it out for yourself. In the end you just have to make a decision. (50-70, Adelaide, higher income)

People don't know what they're covered for until they sign in to have something done. You ask most people what their excess is and they have absolutely no idea. (30-49, Canberra, higher income)

It's really complicated comparing health funds. And they're not really straight up about what you're getting. (30-49, Canberra, higher income)

I was going to join a health fund, but then it was so complicated that I just shelved it and never did. (30-49, Canberra, higher income)

Deregulation

When asked which factors have contributed to growing choice and complexity in financial products and services, most participants cited the deregulation and liberalisation of the financial sector which has taken place in recent decades. In particular, the over-30 groups agreed that deregulation has opened up markets and made the current state of affairs possible. People under 30, meanwhile, appeared to consider the present situation as normal and a natural reflection of the modern world, and did not seem to regard any alternatives as conceivable.

Among the over-30s, deregulation was said to have both positive and negative consequences, although most people appeared to be hesitant about its overall benefits. Some participants were wary of limiting the options available to consumers in the financial marketplace.

If we only had one bank or insurance company, what would it be like? We would probably be worse off. (30-49, Canberra, higher income)

As soon as you limit choice beyond a certain degree, you can create problems.
(30-49, Canberra, higher income)

Despite these comments, most people in the older (30+) groups believed that some degree of increased regulation was desirable, particularly in protecting consumers from risky operators who might otherwise take advantage of credulous investors.

There should be a standard set of rules and regulations for all financial products. Then we'd all know we're covered. (50-70, Adelaide, lower income)

Choice is good, but legislation and training should be severe, so that the people providing the choice are doing the right thing. People can put a shingle out anywhere nowadays. (50-70, Adelaide, higher income)

There was a very widespread view that deregulation has created a set of circumstances that cannot be reversed, with one person likening the situation to 'unscrambling an omelette'. It was also said that deregulation has removed much of the power governments might have in managing the financial sector. 'How do they control it?' asked one participant. 'They don't.' Some people expressed reservations about government attempting to 're-regulate' finance, which could (by their estimation) make matters even more complicated and confusing for ordinary people. There appeared to be little knowledge of statutory bodies set up to oversee the financial services sector, such as ASIC or APRA.

4.3 Personal finances

Non-rational factors in financial decision-making

In order to see what factors, besides objective criteria like value or financial return, play a role in influencing financial decisions, focus group participants were asked to imagine a hypothetical scenario in which they needed to make a choice between several financial products which all had the same features, or whose features were indiscernible from one another. They were then asked how they would go about choosing the right product or provider.

Participants in most groups acknowledged having been in just such a situation at some point, and having been frustrated at the lack of real choice that they were presented with. 'It's just a flip of the coin', said one person. There was also speculation that some financial providers deliberately present their products so as to make comparison difficult.

Nevertheless, there were many factors which were said to contribute to financial choices, beyond purely rational or objective considerations. Many people ask friends or family for advice, with family being particularly important for younger people in making financial decisions. Perceptions of the institution in question are also very influential, with people becoming more risk-averse as they get older and more likely to question the financial stability of an organisation.

I talk to my friends a lot. I trust them more than someone across a counter.
(30-49, Wollongong, lower income)

I tend to go to the large companies because I know them. (30-49, Wollongong, lower income)

You don't want the fly-by-night dodgy-brothers insurance company. (50-70, Adelaide, lower income)

Participants also reported making decisions based on previous experience, such as receiving good or bad customer service from a particular organisation or having read something about it in the media.

One bad experience is all it takes to go somewhere else. That's because there's so much choice out there nowadays. (50-70, Adelaide, higher income)

Advertising and branding was said to have a major influence on the way people make financial decisions. Certain participants acknowledged being strongly influenced by advertising, such as for a particular organisation or product type. Some argued that advertising has a major affect on how other people make decisions, but did not believe that this necessarily extended to their own choices. Those who found it difficult to distinguish between one product (or provider) and another said they might go with the name or logo they knew from the media.

When everything else is the same I go with the logo I like. A logo is a visual representation of what they stand for. So if it's really modern I would go with them. It's an implied association. (30-49, Canberra, higher income)

This comment is an excellent example of the way that marketing and advertising can influence consumers in ways that are seemingly irrational. As noted in Chapter 3, 'non-informative' advertising has been shown to have a negative effect on the quality of financial choices – particularly where the people exposed to such material have relatively little financial knowledge to begin with.

The various non-rational or subjective factors that play a role in financial behaviour appear to come into play in different ways at different stages of life. Generally speaking, younger people reported being influenced by a financial company's advertising and branding, as well as personal recommendations made by family and friends. Older people, meanwhile, were concerned about the financial situation of the company in question, any personal experiences with that company, and the convenience of using its products (such as 'being able to pay at the post office', or bundling with other products).

How age and gender affect attitudes

There were noticeable differences in the attitudes of men and women within and across the various age groups. Generally speaking, younger women (18-29) appeared to be more in control of their finances and more knowledgeable about financial issues than younger men. Younger women were also more cognisant of the need to plan for retirement and to start on a saving trajectory early in life. Younger men, meanwhile, seemed unconcerned about their financial future, believing retirement to be so far off as to be not worth thinking about at their stage of life. Some younger men also believed that their financial future would be largely secured through their compulsory employer-based superannuation. Such clear gender differences at this stage of life

may be explained by the different assumptions that men and women make about what their working patterns are likely to be as they get older, with women making early provision for time out of the workforce (or in part time work) to accommodate childbearing and child care.

Middle-aged women (30-49), on the other hand, appeared to be less interested in financial issues and more willing to let their male partners take charge of financial decisions, though with their input and consent. Some middle-aged men apparently found financial issues inherently interesting (e.g. reading the investment sections of newspapers, and even dabbling with complicated financial instruments ‘just for something different’). Others liked to stay on top of their finances because they had to. Of course, there were exceptions to this pattern, with some women taking a strong interest in their finances. However, the difference between younger women and middle-aged women remained apparent in this regard.

Among older research participants, meanwhile, interest in and knowledge of financial issues appeared to be comparatively even across the genders, with men and women equally concerned about their financial future and the practical dimensions of funding their retirement. Some women were concerned that they had missed out on the benefits of superannuation, not only through additional years out of the workforce (to raise a family) but also because early superannuation schemes were not offered to many women, who comprised much of the casual and part-time workforce.

Perceptions of risk

In Chapter 2, it was argued that many of the financial risks that were previously borne by governments are shifting to individuals and households. Focus group participants were asked which financial risks they faced, and which of these worried them. Participants over 30 nominated more risks, and appeared to be more concerned about those risks, than those under 30 (who had little to say in this regard).

For middle-aged participants (30-49), perceived risks had much to do with the property market. Rising interest rates were a big concern, since these have a direct impact on everyday outgoings. As well, house price fluctuations were said to affect the value of an investment in ways that were not always predictable. Perhaps most concerning was the prospect of job loss and the impact that would have on people’s capacity to make mortgage repayments. It was generally agreed that unemployment benefits would not come close to covering mortgage repayments, and that people would generally end up losing their home if they could not find another job quickly. Participants also agreed that social security no longer even covers other everyday expenses, like food, transport and healthcare costs. Given this situation, income protection was said to be very important, particularly as employment becomes less secure, with the Coalition Government’s WorkChoices legislation leading some (particularly the lower-income participants) to express concern about how secure their jobs were, even in a strong labour market.

Years ago people felt safe. Nowadays we could be wiped out at any moment.
(30-49, Wollongong, lower income)

This feedback reflects evidence that incomes are growing more volatile, even as prosperity grows (see Chapter 2).

Older participants (50-70) were worried about a different set of financial risks. Health was perhaps the biggest concern, with many people worried about how illness or injury (whether their own, their partner's or even another family member's) might affect their financial situation. The potential costs associated with health problems were said to be greater than in the past, and ordinary people's capacity to absorb such costs had declined now that they needed to fund their own retirement.

My concern is when my health fails and I can't work anymore. (50-70, Adelaide, higher income)

Another risk nominated by older participants was volatility in financial markets, including stock market fluctuations. With most people's superannuation invested in share-based funds, movements in the share market inevitably have an impact on rates of return and their eventual retirement income. Even with such risks spread across different stocks and markets, people were still said to be exposed to national and international financial trends, with direct implications for their livelihoods in retirement.

The stockmarket collapse in 2001 affected my savings. I never recovered it all. (50-70, Adelaide, lower income)

I'm concerned that there will be a turn in the market. I'm thinking about pulling my money out so a crash doesn't affect it. (50-70, Adelaide, lower income)

In addition, participants in most groups (particularly the over-30s) thought that the hazards to ordinary people associated with market fluctuations and company collapse had grown as a result of increased deregulation and the commercialisation of public and mutual assets.

Many of the people involved in the focus group research admitted that they did not understand all the ins and outs of the financial system, and that they often went with companies or products that they were already familiar with to some degree. In this sense, they were consciously *risk-averse*; that is, they were hesitant about losing whatever capital they had already accumulated, and were unwilling to take risks with an unfamiliar product or provider. The following comment was typical:

You get scared about losing something, so you don't do anything you're not sure about. (30-49, Wollongong, lower income)

These kinds of comments reflect academic research suggesting that, generally speaking, individuals (as opposed to institutional or corporate investors) are heavily risk-averse, more so than is strictly rational in an economic sense (see Chapter 3). Loss-aversion appeared to be at its strongest among older participants, who were more keenly aware of the failure of certain large finance companies in recent years, and were very wary of losing their retirement savings. These people were content to do business with very well-known institutions (such as the big four banks), even if it meant getting a lower return on their investments or paying a slightly higher interest rate.

The exception to this was a handful of people who reported ‘dabbling’ in more complex investments, including the share market and even options trading. While they were obviously keen to make money out of such investments, most said they had decided to do so ‘just for something different’. These people tended to be on higher incomes, and to have enough money not tied up in other investments or expenses to ‘play with’. Indeed, the share market was described by some people as a ‘game’, or alternatively as ‘gambling’, where an intricate understanding of ‘how to play’ is paramount to being successful. Some people appeared to be more interested in ‘playing the game’ than investing sensibly or with regard to the longer term – so long as they didn’t lose too much money in the process.

Several people remarked that it was difficult to tell which decisions were more risky and which less, with the financial sector constantly coming up with new products and marketing techniques.

If you invest wisely there’s not too much of a risk. But it’s hard to know what’s wise. (30-49, Wollongong, lower income)

Each group was asked what rates of return might indicate a safe investment or a risky investment. Estimates of safe rates of return ranged from 5 to 15 per cent, while for risky investments it was between 10 and 25 per cent (a risky rate of return was commonly thought to be ‘anything above credit card interest rates’). Given the extreme variability in responses to this question, there is clearly no common understanding of current market rates and how they indicate the degree of risk involved in relative terms. Moreover, most younger people (18-29) appeared to have a limited understanding of the tradeoff between risk and return. Instead, the notion that one can shop around for the best rate of return, independently of risk, was widespread.

Procrastination

As discussed in Chapter 3, government and academic research has shown that procrastination is a common feature of many people’s behaviour in a financial context. When asked about ‘unfinished business’ – that is, what financial matters they should have taken care of but had not – many participants mentioned the need to rollover multiple superannuation accounts into the one fund. There was a common view that having multiple accounts means that super savings will inevitably dwindle through high fees and charges, particularly in the case of corporate (i.e. non-industry) funds. Although regarded as important – because their retirement incomes ultimately depend on prudent decisions about their super – it appeared that rolling over super was just not enough of a priority to bother with, particularly among younger people, who had not yet taken action to consolidate super accounts from multiple jobs (although the need to roll over super was also a common feature among participants aged 30-49). With a mobile labour force and frequent career change in modern Australia, the need to consolidate multiple super accounts is widespread.

The process of super consolidation was also regarded as a major hassle, requiring contact with multiple organisations, the filling out of many forms and a great deal of time. Those younger people who had rolled over their super into the one fund had usually done so on their employer’s behest or because they were given straightforward forms to do so. Some young people likened rolling over their super to doing their tax return: it had such a low priority that they had just not got round to it.

It's just apathy. I'll get around to it eventually. (18-29, Parramatta, lower income)

It all comes down to laziness. (18-29, Sydney, higher income)

It's like the dentist - you just keep putting it off. (18-29, Sydney, higher income)

Another common piece of 'unfinished business' is salary sacrifice. Many people seemed to be generally aware that there may be financial benefits associated with sacrificing a portion of their salary, but had not yet done anything about it. Some hoped to get professional advice (e.g. through their tax accountant) before doing so, while for others it was not yet enough of a priority to act on.

Some older participants, particularly those above 50, said they thought they should be doing 'something better' with their money than they are currently doing. Thoughts about what this might mean were rather vague for most of these people; it appeared that research and investigation was required before they could work out exactly how their money could be put to better use. It appeared that actually doing this kind of research – to satisfy themselves that they are not squandering better returns on their retirement savings - was in fact these people's 'unfinished business'.

I wake up during the night thinking, 'I should do this or that'. (50-70, Adelaide, higher income)

Opportunities come up, and if you don't grasp them you don't get the benefits. (50-70, Adelaide, higher income)

Generally speaking, people in the lower-income groups reported procrastinating more than those in the higher-income groups. These people felt less in control of and less satisfied with their financial affairs, yet had taken fewer steps to redress the situation.

4.4 Planning for the future

Saving

There was much discussion among focus group participants about retirement and superannuation, topics which are addressed in depth a little later in this section. However, there were also comments on the various approaches that people adopt to help them save (rather than the purpose to which their savings might be put).

There were clear patterns in the way that people of different ages save money. Young people (18-29) had very distinctive approaches to saving, often involving parents – who in many cases were also those who initiated a savings program and encouraged them to stick to it. For young people, the emphasis was on putting the money out of the reach of temptation.

I put savings in a tin and give it to my mum. (18-29, Sydney, lower income)

I even had a sign in my wardrobe telling me to save, so I had enough money for my trip overseas. (18-29, Sydney, higher income)

I just hand my money over to the folks, and they save it for me. (18-29, Sydney, higher income)

These kinds of approaches to saving reflect research from behavioural economics showing that people often adopt personal strategies to impose self-control on themselves (see Chapter 3).

Many middle-aged people (30-49) reported putting income they would otherwise have saved into their mortgage, to reduce the length of the mortgage and the amount of interest they need to pay. Most older people (50-70) were keenly aware of the need to save for retirement, and many had taken some action to improve their saving habits. Some people regretted not having done so earlier, with current saving or investment plans described as ‘damage control’. Most people in this age group (aside from those who had already retired) reported putting as much money as they could afford into superannuation, with a few people investing in shares, managed funds or property. Those older participants who had already retired (either partly or fully) made note of the need to alter their lifestyle to take account of a lower income. While they had anticipated such changes, they pointed to the added discipline required to ensure their retirement savings were put to good use.

It’s always been hard to save, but I can’t go out shopping at all now that I’m semi-retired. But I really don’t want to have to go back to work. It’s the end of the road now. (50-70, Adelaide, lower income)

Retirement and superannuation

Retirement was a major area of discussion for all groups, and a great deal of feedback on superannuation and the financial aspects of retirement was collected.¹⁰ Naturally enough, people in the older age bracket (50-70) had the most to say, although many of those under 50 had already begun to worry about retirement (without necessarily doing anything about it).

The majority of older participants had either taken steps to improve their financial situation in retirement (by for instance making additional payments into their superannuation), or were keenly aware that they needed to do so; retirement was commonly said to have ‘snuck up on them’. Despite being aware of the need to plan, save and invest, and also being familiar with basic financial concepts and principles, most people appeared to be unsure of how to go about structuring their retirement incomes, at least until the time when a decision needs to be made. In other words, they had avoided making hard decisions about their superannuation or their retirement lifestyle until they absolutely needed to do so. It was often at this point that people consulted a financial adviser.

Until we got to the stage when we needed to do something I couldn’t grasp it all – it was too far away. Until it was almost upon us. (50-70, Adelaide, lower income)

Until you get there, retirement is too far in the future. It’s a hypothetical. (50-70, Adelaide, lower income)

¹⁰ An extended discussion of community attitudes to superannuation will appear in a future Australia Institute publication.

Many older participants conceded they should have been planning and saving much earlier to ensure that their aspirations for retirement were properly met; this applied as much in the higher-income as in the lower-income group. Yet older participants also completely understood why many people only take action at a late stage, and remembered how as young people they themselves had thought little about their long-term financial future. In other words, they recognised such behaviour as ‘irrational’ but still regarded it as completely normal. For their part, young people also seemed to regard it as normal that they would do little planning for retirement until middle age.

When I was 25 I wanted to have money in my pocket. (50-70, Adelaide, lower income)

I didn't think about retirement when I was young. Even now I don't think enough about it. (50-70, Adelaide, lower income)

I'd rather the money now than when I'm 60. (18-29, Parramatta, lower income)

Some older participants suggested that some portion of future tax cuts be paid into super to strengthen retirement incomes. They regarded this as being of just as much benefit for young people as for those approaching retirement age (and perhaps even more), because young people don't (and, by their estimation, shouldn't be expected to) consider their financial needs in retirement at such an early stage. ‘Otherwise they just don't think about it’, said one older person.

Nevertheless, younger people still regard superannuation as important, and are glad for compulsory employer contributions. They simply see it as too far away to consider in detail at their stage of life, and regard their incomes or their super balance as too small to matter for the moment. This appeared to be the case for participants in both the lower- and higher-income groups, although lower-income people under 30 appeared to be *even less* interested in their super than higher-income young people. In addition, younger women were more aware of their super situation and the need to think about retirement than young men. This reflects a greater level of engagement with financial issues generally on the part of young women. Only a small number of younger participants had made any voluntary contributions to their superannuation, and in each case the decision to do so had been suggested or encouraged by their parents.

Meanwhile, people in the middle-aged groups (30-49) were for the most part much more concerned with paying off their mortgage and meeting everyday expenses than saving for retirement. Once the mortgage had been acquitted, they said, they would think about their financial situation in retirement.

I don't care about my super at this point. I just want to get the house paid off and put the kids through school. (30-49, Canberra, higher income)

Indeed, most older participants reported having the same mindset in their middle years; for these people, too, it was the mortgage barrier which prevented them from thinking properly about retirement until a later stage in their lives. Such thinking exemplified the notion of ‘mental accounting’ (discussed in Chapter 3), whereby people put money intended for different purposes into different mental categories.

Despite being more focussed on their day-to-day finances, a number of middle-aged participants appeared to be quite worried about their retirement situation. They generally thought they should be doing more to save (and especially contributing more to their super on a voluntary basis), but lower-income participants in particular didn't understand how they could do so.

It's too late when you get close to retirement. (30-49, Wollongong, lower income)

I'm scared – I want more in my retirement. But you think, 'what can I do?' (30-49, Wollongong, lower income)

Higher-income participants were more relaxed about their retirement expectations. Although they had not necessarily worked out how much they would need to fund their desired lifestyle, they were quite confident about their financial prospects.

Five years before retirement I'll go and see a financial adviser and ask what I should do. (30-49, Canberra, higher income)

I know 40 year olds who are putting lots of extra money into their super every week. I look at them and think, 'I should be doing that'. (30-49, Canberra, higher income)

I put away ten per cent of everything, because I think every little bit counts. I know people who haven't done that, and now it's too late. But I don't know why I chose ten per cent – it just seemed a good figure. (30-49, Canberra, higher income)

I want lots of money when I retire. I want to do lots of stuff. (30-49, Canberra, higher income)

Higher-income participants over 30 appeared to be much more likely than their lower-income counterparts to pay attention to their super statements, and generally to be aware of what was happening with their super fund. Not surprisingly, those on higher incomes were also more likely to be making additional or voluntary payments (perhaps contributing to increased interest in their superannuation).

4.5 Coping with choice

Financial advice

Participants were asked whether they had ever sought financial advice and how helpful the advice was. Many people – including those who had not actually consulted a financial adviser – were quick to point out that financial advisers do not necessarily provide independent advice, given their commission structure or other incentives to recommend one or another product. There was therefore a great deal of suspicion about whether any advice received could be genuinely trusted.

So many places that are selling a product represent themselves as something else, like providing free financial advice. (30-49, Wollongong, lower income)

[Financial advisers] have a vested interest. They're not independent. (30-49, Wollongong, lower income)

At financial seminars, they're often trying to sell a product. They give you general advice, then they sell their product to you. (50-70, Adelaide, lower income)

Given this situation, there was some concern about how to choose a good financial adviser. It was said to be important to know which advisers are suitably independent, as well as which ones are appropriately qualified. There was a great deal of uncertainty as to how ordinary people might go about making these kinds of judgements.

There's nowhere to go to get good advice. (30-49, Wollongong, lower income)

Some of these advisers have done a six hour course in the back of a taxi. (50-70, Adelaide, higher income)

Despite these hesitations, financial advice was said to be essential at certain times, and especially in the lead-up to retirement, when decisions about the most appropriate income stream need to be made. Given the (increasing) complexity of the financial sector and financial products, most people who had looked into their retirement finances acknowledged that they would need some help from an adviser.

There's too much black magic and smoke and mirrors when it comes to finances. Financial advisers know all the loopholes – that's why we need them. (50-70, Adelaide, higher income)

It's only when you sit down one-on-one with a financial adviser that it all fits into place. (50-70, Adelaide, lower income)

Financial education and information

Focus group participants were asked about the best ways of responding to the increasing complexity of personal financial arrangements and the shortfall in financial understanding in the community. Most supported financial education to give ordinary people the knowledge and skills to make informed decisions about their finances. There was widespread agreement that funding and delivering this is an appropriate role for government to play, particularly in the context of all the selective messages and 'info-marketing' that characterises the financial sector's communication with everyday consumers. In addition to 'technical' information about different kinds of products and the like, it was said to be important that financial education promote a more savings-oriented culture to counteract advertising aimed at getting young people to spend more.¹¹

Governments might not have a role in saying how much debt people can take on, but they do have a role in education, and in creating the right culture. My kids wouldn't know how to save for something – that concept would be foreign to them. But it's not foreign to me. So it's something I've been taught. I don't

¹¹ Community attitudes to lending practices and consumer borrowing will be considered in a forthcoming publication from the Australia Institute.

see why there can't be government initiatives that educate people about these things and help create the culture. (30-49, Canberra, higher income)

There were a number of suggestions as to how financial education funded by government might be delivered. These included human-interest television shows that are designed to be engaging, and use actual examples with real families; shying away from information materials that look too 'serious'; starting at the 'basics', so as to be accessible to people with real financial literacy problems; one-on-one or personal interaction, so that participants can talk about their own situation in concrete terms; an independent financial advice line (with nobody being aware that Centrelink currently provides such a service); and workplace information sessions, to discuss issues like superannuation.

In addition, participants raised the idea of independent mechanisms that allow people to compare financial products properly. A very small number of participants were aware that these are already available in the area of private health insurance (in the form of the Australian Government's new website www.privatehealth.gov.au), while more people knew of the standard comparison rate that can be used to assess the true cost of a loan. There was support for extending the idea of simple, independent comparison (under government aegis) to a wide range of financial products and services, including financial advice, superannuation funds, credit cards and even mobile phone contracts. This was said to be a very good way of getting people to act on decisions that they have been putting off.

If it was spelt out clearly how much you are losing by choosing a particular super fund, then I would probably get off my arse and do something about it. (18-29, Sydney, higher income)

It would be good if there was a government website that just compared all the super funds, so you knew which ones are good. (18-29, Sydney, higher income)

With financial products there's no authority that says: 'This is the best one'. You have to do all that work yourself. Whereas it would be good if the government could step in and tell you which one's the best in simple terms. (30-49, Canberra, higher income)

There were also a number of comments and suggestions about financial education and information specifically for older people. For people approaching retirement, there is a need for practical guidance that goes beyond general advice and addresses individual circumstances. At the moment, the only method of getting such guidance is through a financial advisor, which (as we have seen) is a source of concern for many people. Older people did not necessarily have a problem consulting an adviser; they simply wished to be assured that they were getting the best advice free of undue commercial influences. There is a relatively low level of awareness of the different kinds of fee structures (including one-off fee-for-service) in operation across the financial planning sector. As well, there was support for practical education that takes place outside the context of the profit-based adviser/client relationship.

The issue of how to disseminate information and educational resources is highly relevant for older people who, in general terms, do not have the same capacity to

access online content as younger people. In fact, some older participants noted that having enormous amounts of information available online is irrelevant for those without computer skills. Given that much of the awareness-raising activity of the Australian Government's Financial Literacy Foundation is internet-based, such feedback is highly pertinent. Indeed, the comments of many older people who had reached the point of grappling with retirement income streams indicate that personal (and preferably one-on-one) interaction is the most helpful way to make the necessary decisions.

5. Survey findings

To test attitudes to personal finances across the Australian population, an online survey was conducted with a nationally representative sample of 1,002 respondents over the age of 18. The survey questionnaire is reproduced in Appendix C.

An integrated discussion of the focus group and survey findings can be found in Chapter 6.

5.1 Survey methodology and sample characteristics

The sample was drawn from an online panel of ‘pre-recruited’ respondents, and was designed to be nationally representative by gender, age, income and state/territory.¹² Demographic breakdowns of the survey sample can be found in Appendix D.

The sample included a good mix of respondents with various financial characteristics. Around a third (34 per cent) owned shares, one-fifth (20 per cent) had managed fund investments, and a quarter (24 per cent) had made voluntary superannuation contributions in the previous 12 months.

5.2 Self-assessment of personal finances

Past, present and future

Survey respondents were asked three questions relating to their financial past, present and future respectively. These were:

- *How well do you think you have managed your financial affairs over the last few years? Please answer on a scale of 1 (not at all well) to 5 (very well).*
- *How would you rate your current understanding of finances and investments? Please answer on a scale of 1 (poor) to 5 (excellent).*
- *How confident are you about your long-term financial future? Please answer on a scale of 1 (not at all confident) to 5 (very confident).*

¹² Online sampling is increasingly being used by market and social researchers as an alternative to telephone sampling, as landline penetration declines and household internet access rates rise. The growth in popularity of online survey techniques means that there are now a number of high quality panel providers operating in Australia. The panel used to source respondents for this survey was the Valued Opinions panel, which is owned and managed by the Australian arm of Research Now. It is a research-only panel (i.e. panel lists are not used to carry out any non-research activities, such as marketing) recruited from a wide variety of sources, to avoid any bias associated with limited-source recruitment. The panel recruitment strategy is designed to ensure that a good mix of panel members is captured across each state and across the age, gender and income spectrums. The panel is managed in a manner which complies with the draft ESOMAR (European Society for Opinion and Marketing Research, the global industry body for market research practitioners and organisations) guidelines for online panels. Panel members are individually rewarded for their participation in a survey at a level that helps to ensure reliable levels of response and considered answers to the questions, but not so high as to attract ‘professional’ respondents. In the case of this survey, the incentive for participation was \$1.50 per respondent. A series of checks was run on survey data to safeguard against invalid completes – for example respondents completing the survey in less time than it would take to give considered responses to each question.

Their responses are summarised in Table 2.

Table 2 Respondent self-rating of financial past, present and future

	n	%
Managed financial affairs well in the past	504	50%
Did not manage financial affairs well in the past	187	19%
Neutral/not sure	311	31%
Good current understanding of finances and investments	428	43%
Limited understanding of finances and investments	198	20%
Neutral/not sure	376	38%
Confident in long-term financial future	462	46%
Not confident in long-term financial future	232	23%
Neutral/not sure	308	31%
Total	1,002	100%

Half the survey sample (50 per cent) indicated they had managed their financial affairs well (responding with a 4 or 5), with a quarter (25 per cent) saying they had done it very well (responding with a 5). Around 19 per cent said they had not managed their financial affairs well (with a 1 or 2), while 9 per cent said they had not managed them at all well (1). A further third (31 per cent) remained neutral or were not sure.

Forty-three percent said their understanding of finances and investments was good, with 10 per cent calling it excellent. Twenty per cent said their understanding of finance and investments was not good; 7 per cent of these said it was not at all good. A further 38 per cent remained neutral on this question or said they were not sure.

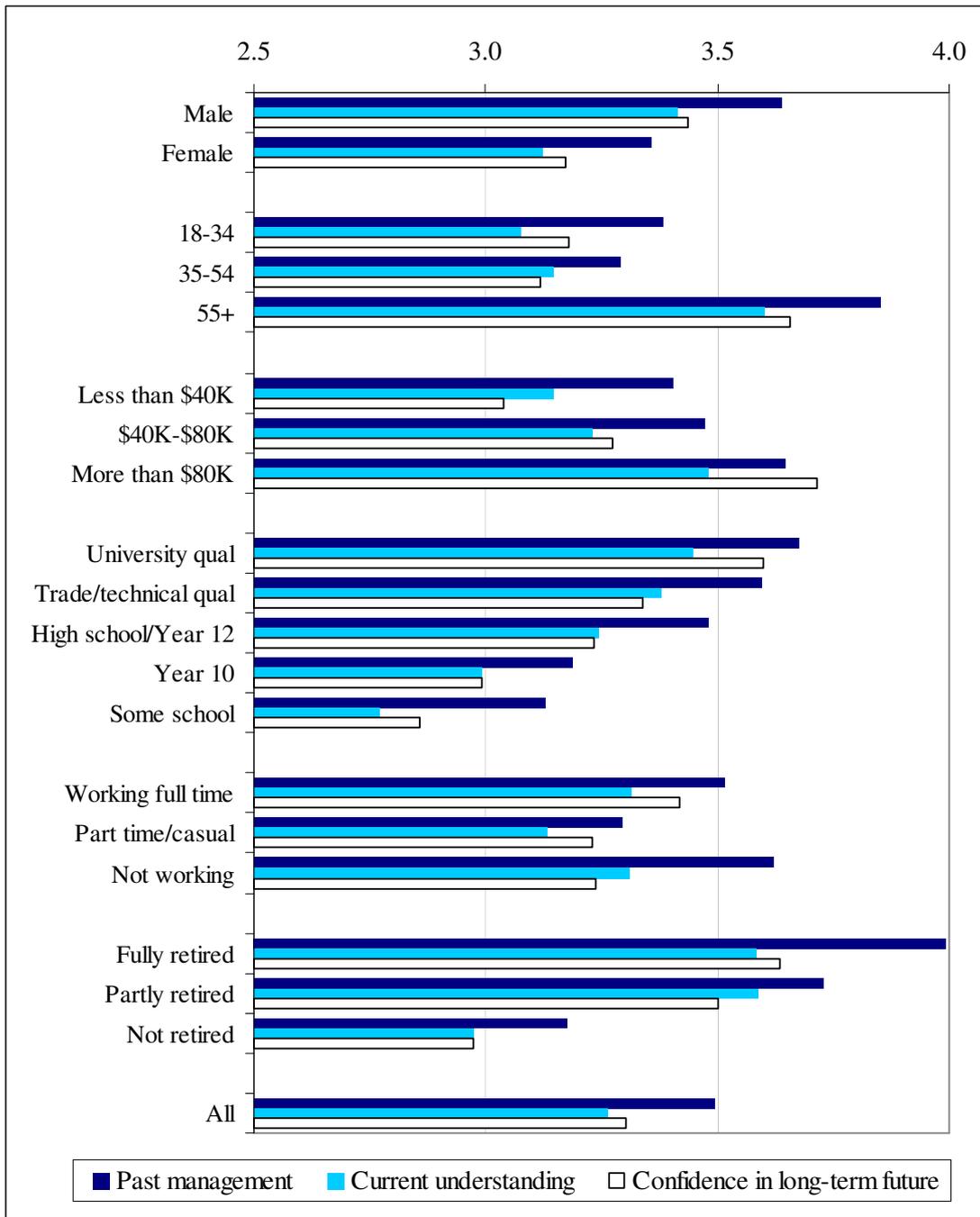
Just under half (46 per cent) indicated they were confident about their long-term financial future; 17 per cent said they were very confident. Twenty-three per cent said they were not confident, with 10 per cent saying they were not at all confident. A further 31 per cent remained neutral on this question or said they were unsure.

Figure 1 provides the mean scores for these three questions by gender, age, household income, highest level of education, working status and retirement status. It shows that:

- men rated their past financial management, current understanding of finances and investments and confidence in the financial future higher than women;
- people over 55 years rated these aspects of their financial past, present and future higher than those under 55;
- people on higher incomes rated these aspects of their financial past, present and future higher than those on lower incomes;

- ratings of past financial management, current understanding of finances and investments and confidence in the financial future each increased with higher levels of education; and
- full-time workers were more confident in their long-term financial future than casual/part time workers or non-workers.

Figure 1 Self-rating of past financial management/understanding of finances and investments/confidence in long-term financial future



* Base=1,002. Respondents were asked to respond on a scale of 1 to 5, where 1 was 'not at all well/poor/not at all confident' and 5 was 'very well/excellent/very confident'. The figures presented are mean scores for each respondent category.

Responses to the three questions reported above (on respondents' financial past, present and future) have been used to divide the survey sample into discrete segments for the purposes of further analysis. The resulting segments are:

- those who have managed their finances *well* or *not well*;
- those with a *good understanding* of finances and investments or a *limited understanding*; and
- those who are *confident* in their long-term financial future and those who are *not confident*.

Additional findings based on these segments of the survey sample are reported later in this Chapter.

5.3 Attitudes to financial issues

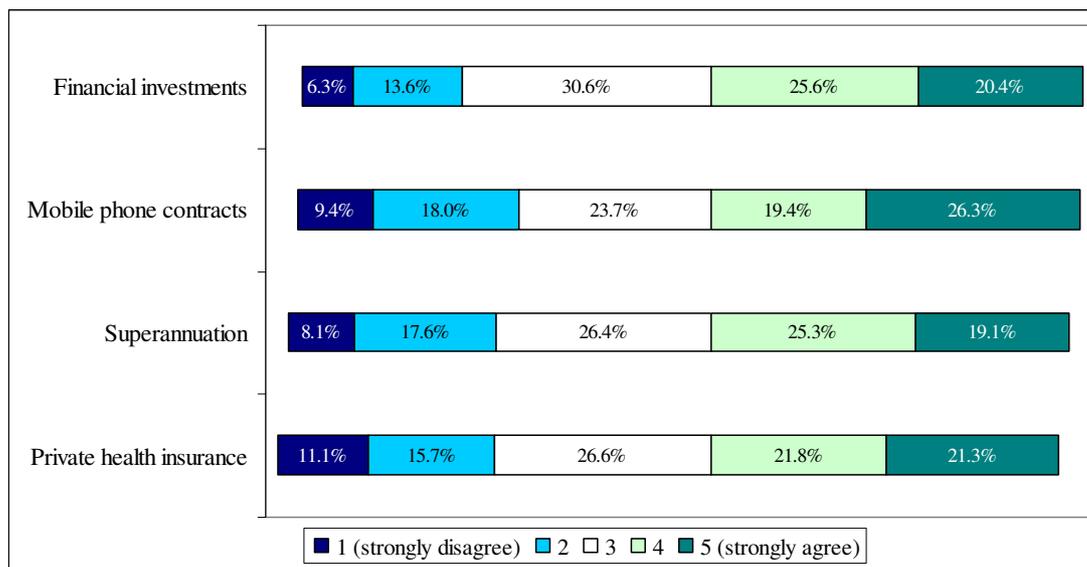
Survey respondents were asked to indicate whether they agreed or disagreed with a series of attitudinal statements about financial issues, using a scale of 1 (strongly disagree) to 5 (strongly agree). The statements were:

- *I think that superannuation is too complicated to understand properly;*
- *I think that financial investments are too complicated to understand properly;*
- *I think that mobile phone contracts are too complicated to understand properly;*
- *I think that private health insurance is too complicated to understand properly;*
- *When I need to make a financial decision, I often find there is too much choice; and*
- *When I need to do something about my finances, I often put it off until later.*

Complexity

The survey results indicated strong levels of agreement that financial decisions are overly complex. As Figure 2 shows, almost half the survey sample agreed that financial investments (46 per cent), mobile phone contracts (46 per cent), superannuation (44 per cent) and private health insurance (43 per cent) are too complicated to understand properly, while much lower numbers disagreed (20 per cent for financial investments, 27 per cent for mobile phone contracts, 26 per cent for superannuation and 27 per cent for private health insurance). By this evidence, mobile phone contracts are seen as even more complicated than superannuation or private health insurance – although financial investments are regarded as more complicated than all of these.

Figure 2 ‘I think that financial investments/mobile phone contracts/superannuation/private health insurance is/are too complicated to understand properly’

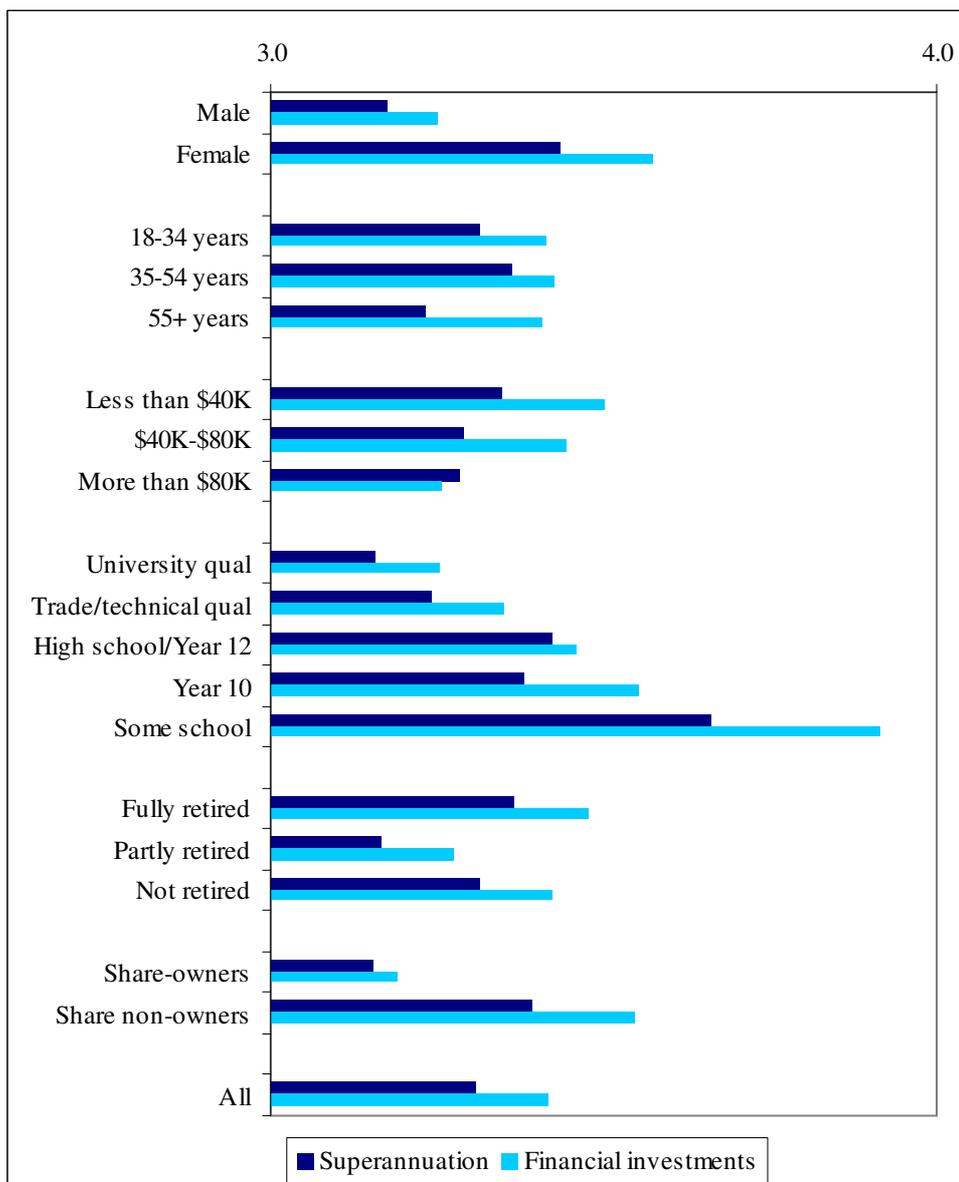


* Base=1,002.

Figure 3 presents mean agreement scores for the statements ‘I think *superannuation* is too complicated to understand properly’ and ‘I think *financial investments* are too complicated to understand properly’ by a range of respondent characteristics. It shows that:

- overall, respondents regarded superannuation as only slightly less confusing than financial investments;
- confusion about superannuation and financial investments is much higher for people with less education;
- women found both superannuation and investments more confusing than men did;
- of all age groups, it was 35-54 year olds that found *superannuation* most confusing; however, *financial investments* appear to be equally confusing across the age spectrum;
- partly retired people – i.e. those on the cusp of full retirement – were more confused about superannuation and financial investments than both retired people and those who were not retired;
- share owners were less confused than non-owners; and
- people who did not own shares were particularly confused about financial investments.

Figure 3 ‘I think that superannuation is/financial investments is/are too complicated to understand properly’*



* Base=1,002. Mean scores presented are calculated from responses on a scale of 1 to 5, where 1 is strongly disagree and 5 is strongly agree.

When asked to respond to the statement ‘I think private health insurance is too complicated to understand properly’, people without private health insurance indicated being much more confused than those who were insured. This could indicate that confusion plays a role in the decision whether or not to take out private health insurance.¹³

¹³ Because lower incomes are associated with poorer understanding of financial concepts, this result could also reflect the fact that low-income earners are less likely to have private health insurance.

Decision-making

Fully 42 per cent of respondents agreed with the statement ‘When I need to make a financial decision, I often find there is too much choice’, while only 18 per cent disagreed. Those who indicated having a limited understanding of finances (at the question ‘How would you rate your current understanding of finances and investments?’) were much more likely to agree with this statement (with a mean agreement score of 3.6, as against 3.2 for those who indicated they had a good understanding of finances). As well, people who reported spending *too little time* on financial decisions (also reported above) were more likely to agree that there is too much choice than those who said they spent *too much time* on financial decisions.

Finally, survey respondents were asked how much they agreed or disagreed with the statement ‘When I need to do something about my finances, I often put it off until later’. Around a third (32 per cent) agreed, while another third (37 per cent) disagreed; the remainder (31 per cent) remained neutral or were unsure. Judging by responses to this statement, people aged between 35 and 54 are greater procrastinators (with a mean agreement score of 3.3) than those between 18 and 34 (3.2) or people older than 55 (2.7). Those living in households with a total income less than \$80,000 per annum reported procrastinating more than people in higher income households. Meanwhile, retired people tended to procrastinate less than others.

People who said they spend *too little time* making financial decisions were much more likely to agree that they put off making such decisions than those who said they spent *too much time* (with a mean agreement score of 3.7, as against 2.7). In other words, it is not that people who spend too little time on their finances make *hasty* decisions; rather, they postpone decisions to a later date.

Respondents who said their understanding of finances and investments was limited tended to procrastinate more than those who said they had a good understanding (3.7 compared to 2.6). As well, people who said they had managed their finances well in the past were less likely to procrastinate than those who had not managed them well (3.9 compared to 2.6).

5.4 Financial behaviour

Time spent on financial decisions

Respondents were asked how much time they spend making financial decisions, on a scale of 1 to 5, with 1 being ‘much less than I should’ and 5 being ‘much more than I should’. Around a quarter (28 per cent) said they spent less time than they should (answering 1 or 2), while another quarter (24 per cent) said they spent more than they should (responding with 4 or 5). A further 45 per cent remained neutral (answering 3), while 3 per cent were unsure. Put another way, a little over half the survey sample (52 per cent) said they were not spending the right amount of time making financial decisions.

Share ownership

Respondents who reported owning shares (34 per cent of the survey sample) were asked how they had acquired them. As Table 4 shows, most (67 per cent) had bought

their shares, although significant numbers had received them as a result of demutualisation or corporate restructure (31 per cent), through an employer (17 per cent), or as a gift (11 per cent). Overall, one in three share owners (33 per cent) had not actually bought their shares, but had acquired them some other way.

Table 3 How share owners acquired their shares (n=337)

	n	%*
Bought them	224	66%
Received them as a result of demutualisation or corporate restructure	103	31%
Received them through an employer	58	17%
Given them (e.g. by a family member)	36	11%
Not sure	2	1%
Total	337	100%

*Because respondents could make more than one response to this question, percentages add up to more than 100%.

Different types of share owners rated themselves very differently on their financial understanding and confidence in the future. Table 5 shows that people who bought shares were much more likely to say they had a good understanding of finances and investments than people who had acquired their shares some other way (62 per cent compared to 46 per cent). Those who had bought shares were also much more confident in their long-term financial future than those who had received shares in some other way (67 per cent versus 47 per cent). Nevertheless, both kinds of share owners ('bought' and 'acquired') rated their understanding of finances and their confidence in the future higher than people who owned no shares.

Table 4 Understanding and confidence among different kinds of share owners*

	Bought shares	Acquired shares**	No shares	All
Good understanding of finances and investments	62%	46%	36%	43%
Not good understanding of finances and investments	10%	12%	25%	20%
Neutral/not sure	29%	42%	40%	38%
Confident in long-term financial future	67%	47%	39%	46%
Not confident in long-term financial future	12%	18%	28%	23%
Neutral/not sure	21%	35%	33%	31%
Total	100%	100%	100%	100%

* Base=1,002

** Refers to respondents who owned shares but had not bought them or did not know how they had acquired them.

6. Conclusions and policy implications

6.1 Research findings

Extensive choice is usually regarded as a positive thing for consumers, and it often is. Yet there are circumstances where more choice is actually detrimental to consumer welfare. Choices are more difficult where people have no clear preference for one option over another, or where they lack the specialist expertise to make an informed decision. In the realm of personal finances, people are often presented with choices that they would prefer not to make, or prefer someone else to make on their behalf. As well, financial decisions commonly involve considerable ‘information asymmetry’ between financial institutions and their retail customers. In other words, institutions know much more about the risks involved in various financial decisions than most ordinary people.

Over recent decades, many Australians have taken on additional financial risks – the result of a more ‘flexible’ labour market, a user-pays health system and, importantly, increasing self-reliance in retirement provision. As well, Australia has become a nation of share-owners, with many people relying on the ups and downs of the market for their future livelihoods. Taken together, these trends mean that ordinary people increasingly need to come to terms with sophisticated financial concepts if they are to make sensible decisions about their financial future. This research set out to discover how Australians are coping with such decisions, through a series of six focus groups and a nationally representative survey of 1,002 people.

Survey results show that many Australians are uneasy about the increasing complexity of financial decision-making. Fully 42 per cent of respondents agreed that *when I need to make a financial decision, I often find there is too much choice*, while only 18 per cent disagreed. Almost half (46 per cent) agreed that *financial investments are too complicated to understand properly*, while only 20 per cent disagreed. Similarly, 44 per cent of respondents agreed that *superannuation is too complicated to understand properly*, compared with just 26 per cent who disagreed. Similar results were obtained with regard to *private health insurance* and *mobile phone contracts*.

Focus group participants generally agreed that financial decisions are becoming more difficult as financial markets grow more complex. While many were positive about the notion of choice *per se*, some people, and particularly older people and those on lower incomes, are sceptical about extensive choice in their personal finances. Among people over 30, there is also hesitation about the benefits of deregulation and market liberalisation in the financial sector. Many young people, on the other hand, appear to regard greater choice and competition as inherently good.

Despite being a nation of share-owners, survey results indicate that as many as one-third of Australians who own shares (33 per cent) did not actually buy their shares, instead receiving them as a result of a corporate restructure, through their employer, or as a gift – that is, not by choice. People who had not actually bought their shares rated their understanding of finances and investments lower than other share-owners, and were also less confident in their financial future.

There is a large body of research (both in Australia and overseas) showing that inadequate levels of financial literacy prevent many people from making sensible and informed financial choices. Alarming, at least one in five Australians is functionally innumerate, while a similar proportion is functionally illiterate. As a result, many people behave in ways that are detrimental to their own financial welfare. Unfortunately, there is persuasive economic evidence that the aggregate effect of 'irrational' economic behaviour is to the substantial detriment of consumer wealth and wellbeing.

Focus group feedback uncovered a range of approaches to financial decision-making that could be described as 'irrational'. These included lack of planning, excessive reliance on advertising for information, non-systematic ways of making decisions, not endeavouring to understand the necessary information, and not having or seeking out the right information. Around half of survey respondents (52 per cent) said they were not spending the right amount of time making financial decisions, with some people spending too little time and some spending too much.

One in five survey respondents (19 per cent) said that they had not managed their financial affairs well in the past, while a similar proportion (20 per cent) said they did not have a good understanding of finances and investments. People with lower levels of education, women and young people were more likely to report having such problems. These findings reinforce existing research showing that women, lower-income households, those with less formal education and Indigenous people face particular challenges with financial literacy.

Prior research has shown that some of the most important factors contributing to financial behaviour are *psychological* rather than *cognitive* – resulting in 'irrational' attitudes like procrastination, disinterest and overconfidence. Our research results confirm just how common such attitudes are. Many focus group participants reported procrastinating in some way over their financial affairs: one in three survey respondents (32 per cent) agreed that they often put off financial decisions until later.

Interestingly, focus group findings suggest that younger women are generally more in control of their finances and more knowledgeable about financial issues than younger men. Younger women are also more cognisant of the need to plan for retirement and to start on a saving trajectory early in life. Many younger men, by contrast, seem unconcerned about their financial future, believing retirement to be so far off as to be not worth thinking about at their stage of life. Among older people, the gender pattern is reversed, with many middle-aged and older women struggling with financial decision-making.

The focus group findings corroborated more general observations about the changing risk profile of Australian households. Major risks worrying participants included job loss, ill health or injury, and (property or share) market fluctuations. Around a quarter of survey respondents (23 per cent) said they were not confident in their long-term financial future. Women, young people, people on lower-incomes and with lower levels of education reported being less confident in their financial future than other respondents.

Focus group participants expressed a great deal of suspicion regarding financial advisors, with many people questioning their independence. Despite these hesitations,

financial advice is understood to be essential at certain times, especially in the lead-up to retirement. Given the increasing complexity of the financial sector, most people who had looked into their retirement finances acknowledged that they would need some help from an adviser.

In addition, there is community support for new initiatives to encourage a savings-oriented ‘culture’, with a widespread perception (particularly among older people) that the present generation of young people have not been properly taught to save because of the easy availability of credit and consumer-oriented advertising. Focus group findings also revealed community backing for independent mechanisms that allow people to compare financial products simply and independently; for the dissemination of information outside an internet setting (particularly for older people and others who have trouble accessing the internet); and for practical financial education that takes place outside the context of the profit-based financial adviser/client relationship.

Our research findings indicate that many people support increased efforts to boost financial literacy by making financial information and education available and accessible. However, there is very little awareness of current government initiatives designed to improve financial literacy, or of government bodies charged with regulating the financial sector.

While our research findings are interesting in themselves, they also have significant implications for governments, for businesses, and for individuals.

6.2 Implications for government

While ‘non-rational’ decision-making may not be a problem for many of the insignificant choices that people make in the course of their everyday lives, it can have huge ramifications for personal finances. The consequences of some financial decisions are only felt many years later, by which time a poor choice will be too late to rectify. Despite this, the range of financial options available to consumers and the knowledge required to assess them continue to grow. With almost every Australian worker now compelled to choose a superannuation fund, and major tax incentives in place to encourage the uptake of private health insurance, complicated financial decisions are now everyone’s responsibility. The assumption behind these trends is that people generally like more choice, yet our research findings indicate that many Australians have doubts about the benefits of greater choice in their financial affairs.

Policy-makers should recognise that extensive choice is not always helpful, and that its benefits flow in different ways to different groups. For some people greater choice can actually undermine wellbeing, by instigating confusion and anxiety and undermining confidence. Governments should therefore try to design policies that allow people to *choose not to choose*, where possible. For example, research has shown that ‘opt-out’ provisions are much more successful than ‘opt-in’ schemes in generating consumer participation in savings schemes and other important initiatives. This principle should inform government policy in consumer finances, and also in other areas of activity where greater choice can be shown to have detrimental consequences.

Governments also need to acknowledge that the increasing complexity of financial affairs actually excludes many people from participating in the ‘ownership society’ championed by mainstream politics. If the economic opportunities that the market presents are to be made truly accessible, then steps need to be taken to reduce the complexities involved. Among other things, this means requiring that the financial sector take steps to lower the ‘psychic costs’ of understanding and interpreting information pertaining to their products and services.

A very straightforward way to improve financial literacy is to concentrate on improving basic literacy and numeracy. OECD statistics show that at least 22 per cent of Australians are functionally innumerate. Increased, targeted and sustained investment in public education is likely to result in improved financial understanding and better financial decisions, particularly for the present generation of young people.

The standard policy response to the shortfall in financial literacy, both in Australia and overseas, has been to address the ‘information asymmetry’ problem by educating consumers so that they can make more informed financial decisions. Such an approach places the onus of responsibility for dealing with a changing financial environment squarely on the consumer, and neglects the fundamental responsibilities that governments and financial institutions have to present consumers with choices that they understand and value.

There is little empirical evidence that government investment in financial literacy actually results in better decision-making by consumers, even though policy-makers assert that one leads to the other. While there has been a great deal of research into financial understanding among ordinary Australians, no formal evaluation of the success of government-funded financial literacy initiatives in bringing about behavioural change has been carried out. This would appear to be a priority for any government looking to address the deficit in consumer understanding with evidence-based policy. One important benchmark for evaluation is the number of people falling victim to scams or excessively risky investment schemes – information that is not readily available at present, despite the laudable work of various government agencies in protection consumers against scams.

People consulted for this research strongly agreed that simpler and more accessible information about financial issues would assist them in making better decisions. However, in its recent research report, the Australian Government’s own Financial Literacy Foundation concluded:

Simply providing comprehensive and well intentioned education resources will not be adequate. There is no shortage of quality resources available already to consumers with an active interest in building their money skills. The challenge is to promote engagement and motivation to those who, for reasons of disinterest in the issue, lack of perceived relevance, stress or the other obstacles identified in this survey, are not currently seeking to build their money skills (Financial Literacy Foundation 2007, p. xii).

In other words, policy-makers need to recognise the basic psychological disposition with which many people approach their finances (and other decisions). Information needs to be tailored for different audiences and competencies, in order to actually

engage these audiences in ways which lead to improvements in their financial wellbeing.

Many of the educational resources designed to improve financial understanding are available online. In fact, much of the awareness-raising activity of the Australian Government's Financial Literacy Foundation is internet-based (www.understandingmoney.gov.au). However, some of those people who are most likely to need help with their finances – including older people, the less educated and people on lower incomes – also tend to have more trouble accessing the internet.

Indeed, this research revealed a strong preference for one-on-one interaction that is directed to the specific financial problems of individuals, rather than group education or 'general' information that cannot be directly applied to individual circumstances. While this kind of guidance is readily available from commercial financial advisers, widespread community mistrust means that many people are reluctant to seek the help of a financial adviser and only do so as a last resort. Currently, government-funded financial *advice* – as opposed to financial *information and education* – is available only to people with 'financial difficulties' (for instance through the Commonwealth Financial Counselling Program).

With this in mind, governments should consider ways to make personal financial advice more widely available to people who do not wish to use the services of a commercial financial adviser. For example, a telephone-based advice service could be established, like Centrelink's Financial Information Service but with the ability to provide financial advice specific to individual circumstances on a liability-free basis. Callers would be entitled to (say) a five-minute phone consultation, after which the details of registered financial advisers (perhaps accredited to ensure their fee structures are appropriate) would be provided if the caller wants more information. (A means test could also be applied to determine which clients may be entitled to additional financial advice free of charge.) Such a service would cater to the many members of the community who wish to clarify relatively simple financial matters in order to take action, and would therefore address the very common problem of procrastination in financial decision-making.

Although intended to protect consumers, reform to the financial sector in 2001 has placed unnecessary burdens on financial providers and their customers by requiring full disclosure of every aspect of a financial service. The documents that providers must produce are onerous to prepare, since they need to address every contingency associated with a given product or service. More importantly, they are bewildering for consumers, and most people pay them little or no attention. In other words, this form of information disclosure actually undermines consumer understanding – both of general financial concepts and in relation to particular transactions. In these important respects, the regulations governing financial disclosure are detrimental to consumer welfare. An inquiry into the impact of the *Financial Services Reform Act 2001* (Cth) on both providers (including financial advisers) and consumers would allow policy-makers to identify which elements make a positive contribution to consumer protection and which make unnecessary demands on providers and consumers. Interestingly, our research indicates that most Australians are unaware that the complex nature of the information they receive about financial products derives from the 2001 reforms; many people tend to blame 'the banks' for the confusing nature of the information they receive.

One of the strong findings of this research is the need for simple, reliable information that allows people to compare financial products of a similar nature. Currently consumers find it very difficult to find such information, and many believe that financial providers deliberately set out to make meaningful comparison difficult. The Australian Government has already taken some steps in this area with its new private health insurance website (www.privatehealth.gov.au), which includes one-page statements on all policies offered by Australian health insurers. To compare investment or superannuation products, however, consumers must gather information from multiple sources, refer to privately-operated sources of information (such as Infochoice), or else ask a financial adviser. There is therefore an opportunity for the Australian Government to collate concise, standardised information on investment and superannuation products and make this available in a form similar to its private health insurance website (although also made available in offline form to take account of the needs of groups with lower levels of internet access). Under such an arrangement, providers would need to answer certain mandated questions in accordance with a template document, to be developed by government. This approach would have the added benefit of allowing policy-makers to monitor the level of complexity in the retail financial sector through a centralised collection point. If this was deemed to be excessive, action could be taken to restrict the range of financial products and services available to retail customers.

The worst way to deal with poor financial literacy would be to leave it to market forces to address the ‘information asymmetry’ between consumers and financial providers. Market-based solutions would inevitably be based on advertising of a largely uninformative nature. Such advertising has been shown to play on pre-existing biases and result in objectively worse financial decisions. Governments should consider ways to restrict the marketing and promotion of retail financial products and services where these activities provide little in the way of helpful information to consumers and instead seek to exploit emotional triggers.

In summary, the following policy suggestions are proposed.

- The Australian Government should establish an inquiry into the results of recent reforms to the financial services sector, with particular regard to information disclosure, the complexity of retail financial products and the needs of groups that have difficulties with financial decision-making.
- The Australian Government should collate standardised information on investment and superannuation products, based on the www.privatehealth.gov.au model but also allowing for offline methods of dissemination.
- The Australian Government should formally evaluate the success of recent initiatives in the area of financial literacy in bringing about positive behaviour change and better outcomes for consumers.
- To strengthen financial literacy at the population level, governments should focus on basic literacy and numeracy.
- Governments should address the information needs of groups that tend to have more difficulty accessing internet-based resources and groups that struggle

with financial decision-making – including women, older people, people with lower levels of education and Indigenous people.

- Governments should consider ways to make personal financial advice more widely available to people who do not wish to use the services of a commercial financial adviser, perhaps through a telephone-based service.
- Governments should consider restricting the advertising and promotion of financial products and services where these activities do not contribute to consumer understanding.

6.3 Implications for business

Ordinary people are now asked to make complicated decisions that in the past would have been made by bureaucrats, entrepreneurs or bankers. Increasing numbers of consumers are looking to make financial investments, even as the financial sector grows more complex. ‘Mum and Dad’ investors are now forced to come to terms with difficult financial concepts and make sophisticated decisions that will ultimately affect their future standard of living. While people generally value choice for its own sake, many are coming to question the benefits of extensive (and sometimes overwhelming) choice in their financial affairs. Over recent years some business and marketing experts have begun to grasp the fact that consumers do not value greater choice in all situations and actually appreciate choice being restricted to a manageable level (Johnson 2004). The wider business community, and especially the financial sector, needs to grasp these lessons and apply them to their own practices.

Competition between financial providers and products has tended to increase, rather than moderate, the complexities of financial products and the level of sophistication required of retail customers. Our research findings suggest that there is significant opportunity for businesses to compete with each other on the basis of optimum *simplicity*. While this might already be recognised on a conceptual level, it has yet to translate into a wider pattern of good practice across the financial sector. Nevertheless, the work of some public-sector superannuation funds is said to be a good example of how to provide consumers with clear and simple choices.

The use of emotional techniques in advertising and marketing financial products is common and clearly effective. However, advertising that relies solely on such techniques, without providing any helpful information or guidance to consumers, is misleading and manipulative, and contributes to the widespread public perception that financial providers act in their own rather than the community’s interests. Businesses should therefore endeavour to promote their products in ways that contribute to, rather than undermine, broader public understanding of financial concepts and imperatives.

Our research findings indicate that many people do not read the written material they receive from financial providers, or if they read it they do not necessarily understand it. Businesses therefore need to do more than meet their legal obligations in providing the standard documentation. Supplying information without regard to how people will use and interpret it can result in stress and bewilderment for consumers. Businesses should invest the time and money in properly explaining their products – and general financial concepts – in ways that allow customers to make decisions about product types, providers and even whether to make any financial commitment at all. In order

to be effective, profound changes in corporate culture, centred on customer welfare and understanding, may be needed. Over time, such changes will benefit the bottom line through increased levels of community trust and better customer loyalty.

Given the growing complexity of financial decision-making, people often need expert advice. Financial advisers, particularly those associated with particular institutions or providers, are widely perceived as acting in their own rather than their clients' interests. This perception is reinforced by the knowledge that many advisers operate on a commission rather than a fee-for-service basis, despite reforms to the sector in 2001 which were in part intended to address this issue. Community perceptions therefore constitute a major barrier in developing a trusting relationship between ordinary Australians and the financial sector. This can only change as the result of concerted and long-term effort by business to foster trust in financial providers and professionals. If the financial advice sector proves incapable of reforming its practices on a voluntary basis, it may eventually be subject to further regulation.

6.4 Implications for individuals

Most people have to make a range of financial decisions over the course of their lives. Some of these choices are rewarding, bringing peace of mind and future prosperity. But some can be bewildering, particularly as financial products become more complicated and harder to understand. Consumers are now expected to make decisions that in years past would have required specialist expertise. Nevertheless, it is only with the consent of ordinary Australians that the 'ownership society' has come to pass.

In recent years policy-makers have come to recognise that many people struggle with financial decisions. Their standard response has been to promote financial literacy through financial education and awareness-raising. The assumption behind these initiatives is that consumers have the motivation and capacity to improve their financial knowledge.

However, government and business have not been fulfilling their end of the bargain. It is the responsibility of governments to ensure that information given to consumers is not misleading or manipulative, to maintain a regulatory environment in which more straightforward choices are possible, to make independent information readily accessible, and to address the needs of people who tend to struggle with financial decision making. It is the responsibility of businesses to refrain from exploiting emotional triggers (such as anxiety about retirement) to sell consumers financial products and services they do not need, and to ensure that customers actually understand the nature of any financial risks they are undertaking – beyond any legal obligations regarding full disclosure. In these areas, government and business need to be held to account. People can use the democratic process to ensure that governments meet their responsibilities, and they can withdraw their patronage from businesses that do not meet theirs.

Of course, consumers should always pay attention to the source of any financial information they receive, and try not to be unduly influenced by advertising of an emotive nature. They should also endeavour to have sufficient financial understanding that they are able to ask the right questions of an expert. But individuals should not blame themselves if they cannot understand a financial concept, or if they struggle to

make sense of a document produced by a financial institution. In the end, it is the responsibility of governments and businesses to ensure that their information matches people's capacity to understand it.

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Appendix A – Focus group discussion guide

Preamble

- Welcome to group
- Introduction to moderator and the Australia Institute, an independent non-profit research centre based in Canberra
- Reassure confidentiality
- Mobile phones off
- Talk one at a time, lots of questions to get through
- Location of toilets
- Food and drink

Introduction to topic

Tonight I'd like to talk to you about *finances*. I'm not going to ask any detailed questions about your own personal affairs, but rather how you *feel* about various kinds of financial decisions you need to make from time to time.

By *finances* I mean a broad range of things like everyday banking, home mortgages and other loans, insurance, investments and superannuation.

Before we start, let's go around the room and introduce ourselves.

General feelings about finances

- Generally speaking, how would you describe your financial affairs? (No need to give specifics)
- Are you *up to date* with your financial affairs? Are there things that you haven't done that you should have done? Why haven't you done them? What will it take for you to do so?
- Do your finances make you feel *anxious* or *worried*? What things?
- Do you find financial matters *interesting* or *boring*, or a little bit of both? Which bits are interesting and which bits are boring? (Does your partner feel the same way or differently?)
- Do you find financial matters *confusing* or *unclear*? Which particular aspects? What experiences have you had which brought you to that view?
- What kinds of *financial risks* do you think you currently bear? (eg health problems, unemployment, retirement, unexpected events) Do you feel in control of those risks? Are you anxious about them?

Time

- Thinking about the last financial decision you had to make – don't tell me what it is - how much time did you spend *getting the right information* to make that decision? How much time do you think you should have spent?
- How much time did you spend *reading and understanding the information*? How much time do you think you should have spent?
- How much time did you spend *actually making the decision and acting on it* once you had read all the information? How much time do you think you should have spent?
- Were you happy with your eventual decision? Why?
- Do you spend *time at work* getting information or making decisions about your finances? How much time? Do you think your employer would be happy that you do this?

Information

- Do you pay attention to the money-related *documents* you receive in the mail? For example:
 - Bank statements
 - Super statements
 - Health insurance documents
 - Product disclosure statements (for financial products like bank accounts, credit cards or insurance policies)
- Do you understand the *language* used in financial documents? Do you think it's important to understand it, or does it not matter too much? Why do you say that?
- When you don't understand something, do you discuss it with anyone? Who would you usually ask?
- Have you ever sought *professional advice* about your finances, say from a *financial planner* or an *accountant*? [Note: not talking about taxation] Why did you do this? Was it helpful?
- Are you interested in improving your understanding of financial matters? Have you ever done anything to gain more knowledge? What was that?
- What do you think would be the *best way for you to learn more*? Would this realistically be worthwhile for you? Do you think you would act on your newfound knowledge? How so?

Choice

- When it comes to financial matters like super or personal investments, do you like to have *lots of choices* between different kinds of products or providers? Or would you like your choice to be *limited to a few options*? Why?
- Do you think there is more choice in financial matters nowadays compared with ten years ago? Is that a good thing or a bad thing? Why?
- Do you think there is enough choice or too much choice nowadays, or about the right amount?

- Imagine you need to make a decision about your finances. You look at the information, but you can't find any real difference between them (eg same interest rate, return, risk etc). How would you make the decision? What factors would you consider?

Mortgages and Loans

- Have you taken out a mortgage (or other loan) or refinanced your mortgage in the last five years? How easy or difficult did you find this process?
- Did you compare different products and providers to make the best choice for you? How well were you able to understand the differences between them? How many did you compare?
- Do you think you fully understood the risks involved when you took out the loan? (eg security for the loan, rising interest rates, fluctuations in property values, job loss)

Retirement and superannuation

- Do you pay attention to your superannuation, or do you just let your employer pay super into your account without thinking much about it? (Do you know *how much* is in your super fund? How often do you check the balance?)
- Two years ago the Government changed the law so each of us could nominate a super fund, rather than have our employers choose them. Did anyone *change* their fund as a result? Why? Did others *investigate* but leave things as they were? Why?
- Are you *comfortable* thinking about your financial future and how you'll make ends meet in retirement, or does that make you feel *uncomfortable*? Why might that be?
- How important is it to be *financially self-reliant* in your retirement? Do you think you will be? Have you done anything about it?
- Do you think the government should have a role in 'forcing' people to be self-reliant – for example through compulsory superannuation? Or should it be up to each individual how they save for retirement?
- Have you made voluntary contributions to your superannuation? Was this a large or a small amount? Why did you put that money into superannuation and not another kind of investment?
- [For those who have made voluntary super contributions] Was this a way of 'forcing' yourself to save – to know that you'd be penalised if you accessed the money? Did it help having it sitting in a separate account?
- Do you manage your own super fund, rather than having a corporate or industry super fund? Why did you decide to do this? What do you think are the advantages and disadvantages?
- If you needed to make a decision about which super fund to join, how many options (i.e. *providers*) would you like to have? How many options would be *too many*?
- If you needed to make a decision about your investment portfolio within your super fund, how many options would you like to have (ie *risk vs return, diversity, type of investment*)? How many options would be *too many*?

Investment

- Are you saving money for the future? What are you saving for?
- [If saving for the future] What do you do with the money you save? Why is that?
- Apart from your mortgage and super, do you have any investments? What kinds? Why did you decide to take out those investments?
- Did you consider other alternatives before you decided on that investment? What other alternatives?
- Who did you talk to about it? What advice and information did you take into account?
- Are you satisfied with the decision you eventually took? Why?
- What rate or return do you think would indicate a *safe* investment? What interest rate would indicate a *risky* investment?

Health insurance

- Do you have private health insurance? Why did you originally take out health insurance?
- Thinking back to when you last joined or switched health funds, how easy or hard did you find this? Could you compare the different options well enough?
- Do you think the benefits of having private health insurance make up for the need to choose the best option for you and your family? Or would you rather you were automatically covered through the public system?
- If you or a family member suffered a serious illness or injury, how well do you think you would cope financially? What problems might you face?

Conclusion

- Are there other financial issues that we haven't discussed that confuse you or worry you?
- Do you think that it's okay that people are expected to make complex decisions about finances? What could financial institutions do about it? What could governments do? What could ordinary people do?

Appendix B – Focus group specifications

Topic	Expectations for the future
Number of groups	6
Participants	Recruit 9 for 7/8
Gender	Mixed
SES	3 x lower, 3 x higher (see below)
Age	2 x 18-29, 2 x 30-49, 2 x 50-70 (see below)
Lower SES (18-29)	<i>Personal</i> income before tax <i>below</i> \$30,000 per annum
Higher SES (18-29)	<i>Personal</i> income before tax <i>above</i> \$30,000 per annum
Lower SES (30-49)	<i>Household</i> income before tax <i>below</i> \$70,000 per annum
Higher SES (30-49)	<i>Household</i> income before tax <i>above</i> \$70,000 per annum
Lower SES (50-70)	<i>Household</i> income before tax <i>below</i> \$60,000 per annum
Higher SES (50-70)	<i>Household</i> income before tax <i>above</i> \$60,000 per annum

Group breakdown

	Lower SES	Higher SES
18-29	Group 1: Sydney West 6pm Monday 22/10	Group 2: North Sydney 6pm Tuesday 23/10
30-49	Group 3: Wollongong 6pm Tuesday 30/10	Group 4: Canberra 6pm Thursday 1/11
50-70	Group 5: Adelaide 6pm Tuesday 7/11	Group 6: Adelaide 6pm Wednesday 8/11

Additional specifications

- Groups 1 and 2 must include people still living at home (at least 3) and people who have moved out of home (at least 3)
- All participants in groups 1,2, 3 and 4 must work in a paid job for at least 7 hours per week OR live with a partner who works in a paid job for at least 7 hours per week
- Groups 3,4,5 and 6 must include at least 4 participants who attend with their partner (i.e. 2 couples per group)
- In groups 5 and 6 a good mix of fully retired, semi-retired and non-retired people is desirable.
- In each group a range of ages and genders is required.

Venue details

Sydney West venue	Focal Point group rooms 93 Wigram Street, Harris Park
North Sydney venue	The Chatroom Facility Level 1, 431 Miller St, Cammeray
Canberra venue	Fellows Room University House Australian National University, Canberra city
Wollongong venue	Corrimal RSL 168 Princes Hwy, Corrimal
Adelaide venue	Robyn Kunko Market Research 7 Hill Court Black Forest SA

Appendix C – Survey questionnaire

The questions used in the online survey are reproduced below. In addition to these questions, respondents were asked basic demographic questions about their age, gender, state/territory, household income, highest level of education, working status, retirement status and housing tenure type.

The following questions are about your **finances**. There are no detailed questions of a personal nature, and this survey is not for a bank or financial institution.

Please note that your answers are **completely anonymous** and will only be used for research purposes.

By **finances** we are referring to:

- **Bank accounts**
- **Mortgages** and other loans
- **Insurance**, including health insurance
- **Superannuation**, including employer super and any voluntary super
- Any **investments** you might have.

Q1. How well do you think you have managed your financial affairs over the last few years? Please answer on a scale of 1 to 5:

- Very well – 5
- Not at all well – 1
- Not sure/not applicable/I don't manage my financial affairs

Q2. How would you rate your current understanding of finances and investments? Please answer on a scale of 1 to 5:

- Excellent – 5
- Poor – 1
- Not sure/not applicable

Q3. How confident are you about your long-term financial future? Please answer on a scale of 1 to 5:

- Very confident - 5
- Not at all confident – 1
- Not sure/not applicable

Q4. Generally speaking, how much time do you spend making financial decisions?
Please answer on a scale of 1 to 5:

- Much more than I should - 5
- Much less than I should – 1
- Not sure/not applicable

Q5. Please indicate your level of agreement with the following statements (Scale of 1 to 5 where 1 is disagree strongly and 5 is agree strongly). [Note: randomise]

- I think that **Superannuation** is too complicated to understand properly
- I think that **Financial investments** are too complicated to understand properly
- I think that **Mobile phone contracts** are too complicated to understand properly
- I think that **Private health insurance** is too complicated to understand properly
- When I need to make a financial decision, I often find there is too much choice
- When I need to do something about my finances, I often put it off until later

Q6. In the past 12 months, have you made any **voluntary** contributions to your superannuation (i.e. beyond what your employer was required to contribute)?

- Yes
- No
- Not sure

Q7. Do you or your partner currently own any shares? (Note: do **not** include any managed investments you may have)

- Yes
- No – skip to QF11
- Not sure – skip to QF11

Q8. How did you (or your partner) acquire those shares? Please select all that apply.
[note: multiple response]

- Bought them
- Received them as a result of demutualisation or corporate restructure
- Given them (e.g. by a family member)
- Received them through an employer
- Not sure

Q9. Do you or your partner currently have any managed investments (also known as managed funds or mutual funds)?

- Yes
- No
- Not sure

Q10. Do you have private health insurance?

- Yes
- No
- Not sure

Appendix D – Survey sample characteristics

Table D1 sets out the features of the survey sample according to gender, age, household income (before tax) and state/territory. Each of these characteristics was subject to quotas to ensure that the sample accurately reflected the broader Australian population. The table also includes information on respondents' highest level of education, working status and retirement status

Table D1 Demographic breakdown of survey sample

	n	%
Male	487	49%
Female	515	51%
18-24 years	155	15%
25-34 years	172	17%
35-44 years	194	19%
45-54 years	178	18%
55-64 years	166	17%
65 years or older	137	14%
Less than \$20,000	112	11%
\$20,000 - \$39,999	249	25%
\$40,000 - \$59,999	210	21%
\$60,000 - \$79,999	181	18%
\$80,000 - \$99,999	140	14%
\$100,000 or more	110	11%
NSW	323	32%
Vic	248	25%
Qld	203	20%
Tas	15	1%
SA	86	9%
WA	101	10%
NT	8	1%
ACT	18	2%
University qualification	271	27%
Trade/technical qualification	267	27%
High school/Year 12 certificate	240	24%
Year 10 certificate	144	14%
Some high school/primary school	75	7%
None of these	5	<1%
Working full time	371	37%
Working part time/casually	269	27%
Not working	362	36%
Fully retired	170	27%
Partly retired	97	15%
Not retired	364	58%
Total	1,002	100%

Table D2 shows the characteristics of the survey sample in relation to various financial criteria, including working status, retirement status, share ownership, managed fund investments, voluntary contribution to superannuation and private health insurance.

Table D2 Financial characteristics of survey sample

	n	%
Share owners	337	34%
Share non-owners	665	66%
Managed fund investors	196	20%
Managed fund non-investors	806	80%
Voluntary super contributions	243	24%
No voluntary super contributions	759	76%
Private health insurance	487	49%
No private health insurance	515	51%
Total	1,002	100.0%



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