Nicholas Barr June 1st, 2023

How can people improve their relationship with money?

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Low financial literacy is widespread and continuing. Many people do not understand simple interest, let alone compound interest or present values, which underpin sensible decisions about pensions. ***Nicholas Barr*** *writes about his work and that of* ***Martin Lewis*** *on financial education and policy design to help people make better financial decisions. While they agree on desired outcomes, they don't always see eye to eye on how to get there.*

Nicholas Barr will be speaking at the event In Conversation with Martin Lewis, Thursday 15 June, 5.00pm to 6.00pm.

An important strand in LSE's DNA is to rattle cages, by being countercultural (supporting tuition fees in higher education) and/or by sticking a spoke in the wheel of government policy (scuppering the then government's proposals for all-singing, all-dancing identity cards). A second strand is the drive to improve the life chances of people from disadvantaged backgrounds. Martin does both.

We met 30 years ago when I was an academic governor and Martin the general secretary of LSE Students' Union. Hot topics at the time were the level of tuition fees for overseas students and the design of the UK student loan system. In tandem with my friend and colleague Iain Crawford (one of Martin's early mentors) I argued that the government's hugely controversial introduction of student loans in 1990 was the right direction, but that the fact that loans were organised like a mortgage or bank overdraft was the wrong design. Iain and I spent 10 years campaigning for student loans with (in the jargon) income-contingent repayments, that is, repayments of *x*% of the graduate's subsequent earnings collected each week or month as a payroll deduction alongside income tax and national insurance contributions. That type of loan was eventually introduced in 1998.

At the time Martin and I agreed about some things, disagreed about others, and had a splendid time kicking ideas around.

Since then Martin has gone on to a wide range of hugely impactful activities, and some of our interests have continued to overlap, in particular financial literacy. Martin's work has included action to improve financial literacy directly, and related work including template letters to reclaim overpaid bank charges, recover compensation for sales by banks of unsuitable financial products, and activity on negative home equity. It's not just talk. Martin has also put his money where his mouth is, working on and paying for 365,000 financial education textbooks to go into every state school (1 for every two pupils) because the government would not fund the project. That work is enormously important. Financial literacy, such as how losing control of credit card spending can spiral or how student loans work should be a standard part of the school curriculum.

My work on financial literacy, as part of my work on pensions, starts from the other end – that it is unrealistic to expect people to make good choices in the face of complexity. In the case of pensions, people face multiple uncertainties. A worker's future needs depend on life expectancy, on the duration of marriage and options after a divorce or death of a partner; on the number, ages and experiences of children; and on medical expenses. And people face further uncertainty over the level and time path of their future earning opportunities.

The evidence is stark that low financial literacy is widespread and continuing. A famous international survey by Lusardi and Mitchell (2014) asked three very basic questions about finance. I'll mention only the first: 'Suppose you had $100 in a savings account and the interest rate was 2 percent per year. After 5 years, how much do you think you would have in the account if you left the money to grow: more than $102; exactly $102; less than $102; do not know; refuse to answer. The other two questions were similarly basic. In the US, only 35% of respondents answered all three questions correctly, in many OECD countries only about 25%.

The truth is that many people do not understand even simple interest, let alone compound interest, let alone present values, which underpin sensible decisions about pensions. Financial education is hugely important, but its potential should not be overestimated. For such reasons, my work on pensions (joint with Peter Diamond) includes designs that do not require people to make complex choices. In particular, in evidence to an Australia inquiry, we argue that if someone wants to make choices about pensions and retirement, the pension system should assist them, but that the system should be designed to work well also for people who make no choice – and making no choice should be an entirely acceptable option.

Martin's work on educating in the basics, providing textbooks and giving active help in claiming entitlements is spot on. So is his work seeking assistance for people with negative home equity and his wider work as founder, funder and chair of the Money and Mental Health Policy Institute charity.

Beyond the basics, however, is the question of how far it is either realistic or desirable to expect financial expertise. It would be interesting to get Martin's views on where to locate the boundary between what is essential and what makes undue demands on time, attention and skills.

Martin's activities have all been driven by two passions: improving policy and helping people to make better financial choices. He has done so in a variety of ways.

First, he seeks to empower individuals by giving them the information they need to make informed choices both directly and by financing gaps in public policy, such as financial textbooks and support with mental health. Thus his web site explains student loans, how to interpret them, whether it's a good idea to repay early, and other topics such as how to reclaim overpaid charges. And over time he has become a major and highly trusted personality. The Martin Lewis Money Show is the biggest current affairs programme in the UK – a bully pulpit for empowering people; and most recently he has become one of the regular hosts of ITV's Good Morning Britain.

Second, he discusses policy design with a wide variety of people to test his ideas.

While he and I fully share progressive objectives (the What) we don't always agree on the details of policy (the How). For example, we have not always agreed whether interest subsidies for student loans are a good idea (my concern is that interest subsidies benefit even the best-off graduates, and I worry that sight is being lost of other, more powerful ways, to help students from poorer backgrounds). At other times, we focus on different aspects. Martin, for example, is concerned that the loan repayment formula may bear too heavily on lower earners. While not underplaying that aspect, my concern has focussed at least as much on the 50% of so of the cohort, mostly from poorer backgrounds, who do not go to university and who receive vastly smaller subsidies for skills development than the 50% who do.

Where we agree is that successive governments have made a shockingly bad job of explaining student loans (see my 2011 blog post on Martin's MoneySaving Expert website), and that whatever changes are made, the arrangement should be described as a graduate tax or graduate contribution, not as a loan.

A third strand in Martin's activity is to bend ministers' and officials' ears to get done what he thinks needs to be done. I am sure that much goes on quietly behind the scenes, but part of his power is that those in government know that he has a powerful voice in multiple media and is not bashful about naming and shaming.

My worry that I might be misremembering or misinterpreting Martin's positions or activities is tempered by the fact of our conversation on 15 June as part of the LSE Festival, at which Martin – of all people – will be robust in stating his position, the next chapter in the dialogue we started those many years ago.

Argumentative, stroppy when necessary, passionate on the side of the underdog and ruthlessly intellectually honest – it's the LSE DNA – what's not to like?

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Notes:

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