

## **FINANCIAL ADULTERACY – A LIFELONG LEARNING (LLL) SOCIAL ENGAGEMENT OF THE UNIVERSITY TO THE DEVELOPMENT OF BETTER CITIZENSHIP**

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### **ABSTRACT**

Life is not free. Regardless of living in times of rapid change, everybody still has to provide for their own needs. The lack of seriousness with which money is treated at times in modern society leads many to assume that they will always have sufficient income for the immediate satisfaction of their needs. As is obvious, this cycle is not infinitely reproducible. Investment and progress only take place if there are savings. Preparing for the future requires a degree of sobriety in income management. Savings are fundamental.

No matter how well informed or well qualified citizens are, it is certain that there has been increasing indebtedness in the average modern household; and, indeed, at national and governmental level as well. The search for higher levels of wellbeing has led to behaviours which are inconsistent with a strictly economic logic. It is necessary to recover the basis of a balanced domestic budget in order to secure the future: not only at the expense of forthcoming incomes but also by deferment of consumption options.

There are no lack of financial management disciplines, regulatory bodies and control mechanisms. There is however a need to teach from an early age what is the meaning of money, and its importance for the acquisition of goods and services. Nonetheless, the numbers and modern behaviour do not seem to correspond to these teachings: the choice of credit mechanisms for personal consumption is markedly increasing, even for those with high incomes. It is this certain limited rationality of human behaviour in relation to money that we will deal here under the subject of “financial *adulteracy*”. Therefore, we propose this concept, which is born from the combination of adulterate (to corrupt or modify), and literacy (to understand or to give good use to), and aims to highlight situations in which people (adults) contravene the golden rules of financial management.

A recognition that, in the course of learning, human feelings overcome these rationalities, adulterating the good principles of budget management and savings that should support a future security, was created in 2012 (DL 227/2012) by the Network of Indebted Consumer Support (RACE) under the supervision of the Directorate-General for Consumer Affairs (DGC). The Office for Consumer Indebtedness (GOEC), linked to ISEG – Lisbon School of Economics & Management - University of Lisbon and the University of Aveiro Extrajudicial Consumer Support Office (GEACE-UA) were created, respectively, in October 2006 and October 2013 and are members of this Network since its inception. It is their function to inform, advice and assist consumers, free of charge and confidentially, in the management of their family budget, and support in the renegotiation of their charges / credits. Aware of the underlying problems, both seek to intervene in society by educating and informing citizens around financial literacy issues, helping to create more informed, responsible and active consumers / citizens.

Considering the good practices promoted internationally, in particular by the Organization for Economic Co-operation and Development (OECD), conveyed by RACE, and by GOEC and GEACE-UA, it is intended to assess the application of these practices by all Portuguese consumers, specifically with regard to their relationship with credit, based on the behaviour revealed by the official statistics from the Central Bank of Portugal.

KEYWORDS: finance, adulteracy, debt, saving.

## FRAMEWORK

Life is not free. Looking at Maslow's pyramid of needs, we understand that the satisfaction of most human needs will require the use of economic resources. However, like natural resources, they are neither infinite nor immediately available. They require effort and work. They are the indispensable means that allow access to goods and services, which ensure the survival of people, define their quality of life and promote their well-being.

We live in times of rapid change. Economic, social, scientific and technological knowledge and progress, together with a more globalised world with easier individual travel and distribution of goods, have enabled progress and helped to solve many of the problems associated with subsistence and quality of life.

Nevertheless, one fundamental fact remains: each person still has to provide for their own needs. This is the basis of our reasoning, and why we are not promoting more governmental solutions, at national or supranational level; or emphasizing answers from socioeconomic models; or even analysing the role of international organizations engaged in the search for solutions to such problems. We recognize that such actions are very important and have been vehicles for the development of countries and societies. However, they are often remote from the concrete difficulties experienced by individuals in their real lives. The actions of governments and international organizations, and even the theoretical socioeconomic models, are focused on a larger scale, thinking more about the behaviour of aggregates, populations and economic agents than about the needs of the individual.

Although crisis experiences are not only a characteristic of the modern world, as they have always accompanied the growth of various societies and economies, it is universally recognized that these difficult situations and crises at the macro-economic level trickle down to affect the daily lives of individuals. The recent financial crisis, which is easy to explain but difficult to solve, has forced, in many countries, the intervention of governmental and other regulatory authorities in order to correct situations of fraud and unwise behaviour among financial and credit institutions, curb irresponsibility in product management and financial investments, and even intervene in the management of companies, through the strengthening of corporate governance mechanisms. The result has been greatly increased legislative output; reinforcement of the regulatory and behavioural supervision instruments of financial institutions; control of the actions and decisions of the managers and boards of directors of banks and insurance companies; fraud prevention; and education (information and training) of economic operators, even down to the level of individual households.

Given the cross-pollinating and contaminating effects ensuing from bad decisions on the allocation and use of money, the regulatory and supervisory bodies of the financial system, as well as the political and government agents of the countries, are now more aware of the use of money. Moreover, these types of phenomena are often reflected in the need for external intervention to help to solve the problems of (over)indebtedness – such as the use of such institutions as the International Monetary Fund (IMF) or the European Central Bank

(ECB) – or tax increases, an "almost unique", or at least more "immediate" measure, to respond to private and public deficits and debts.

Awareness of the need for an integrated policy on financial education led to the creation in Portugal, under the responsibility of the National Council of Financial Supervisors (CNSF) [Bank of Portugal, Security Markets Commission (CMVM) and Insurance and Pension Funds Supervisory Authority (ASF)] of the Portuguese National Plan for Financial Education (PNFF) (<https://www.todoscontam.pt/pt-pt>).

The PNFF led by the CNSF has a structure composed of the Coordination Committee responsible for the management of the Plan; the Jury for the "Concurso Todos Contam" (Everybody Counts Contest), a national contest for the best financial education projects to be implemented in schools; and the Monitoring Commission ([www.todoscontam.pt/comissao-de-acompanhamento](http://www.todoscontam.pt/comissao-de-acompanhamento)), with 34 partners, whose functions are "to contribute to the identification of training priorities and needs, to provide means for their implementation, to stimulate financial training projects and to propose methods and means for implementing training initiatives."

It is in the context of a society that is much more technologically advanced and in which citizens actively engage every day that we reflect on the easy attitudes to money and in particular to spending today, with many people and households anticipating and perhaps feeling entitled to higher incomes for the immediate satisfaction of all their needs and wants. It is not unreasonable to want better living conditions, access to desirable goods and services, or a good quality of life that should not have to wait for the next generation, or even for 10 or 20 years, or for their retirement. Our citizens, however, feel entitled to all these things now, not in some future time when they have saved enough money. In fact, credit structures and institutions agree with and encourage this approach. However, for living we need money, but to live better or with better quality, for the majority of people and in more modern societies, this means that we need a lot of / much more money.

As is known, the economic cycle is not infinitely reproducible. Investment and progress will only take place if there are savings. Preparing for the future requires a degree of sobriety in personal, business, and public income management. Savings are therefore fundamental.

## THE PORTUGUESE CONTEXT

No matter how well informed or well qualified our citizens are, individually or as a society, the reality is that increasing indebtedness of households and governments is a common modern phenomenon. The search for higher levels of well-being has motivated behaviours that are inconsistent with a strictly economic logic. It is necessary to return to the basics of a more prudent and balanced domestic budget approach to secure the future: not only curbing income inflation but also in the postponement of consumption options.

Under the theme of *Active Citizenship and Humanity Engagement*, our concern is focused on the households as economic agents. They most directly feel social and economic changes; and it is on their behalf, ostensibly at least, that governments and companies make decisions, either regulating or creating products and services that are aimed at satisfying their needs and improving their quality of life. Since government actions are implemented on a macroscale, far from the concrete needs of individuals, what is the real situation of these households? Chart 1, obtained from Pordata, a database on contemporary Portugal with official statistics, shows the evolution of income, expenditure and savings of Portuguese households over the last two decades:

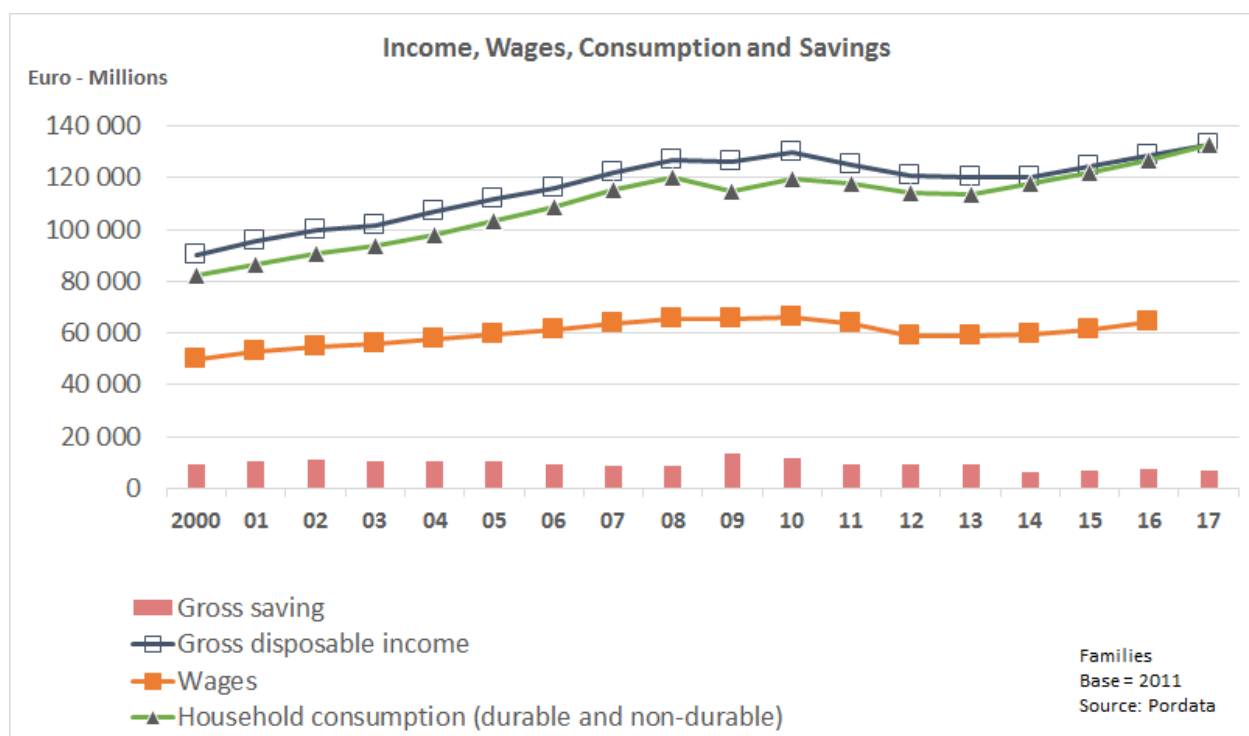


Chart 1 – Income, Wages, Consumption and Savings of Portuguese Households

As can be observed, wages, as a "single" remuneration of the productive factor, are not sufficient nor the only source of income for the levels of consumption of households in Portugal. Chart 2 further shows that consumer spending is even higher than income levels in 2017:

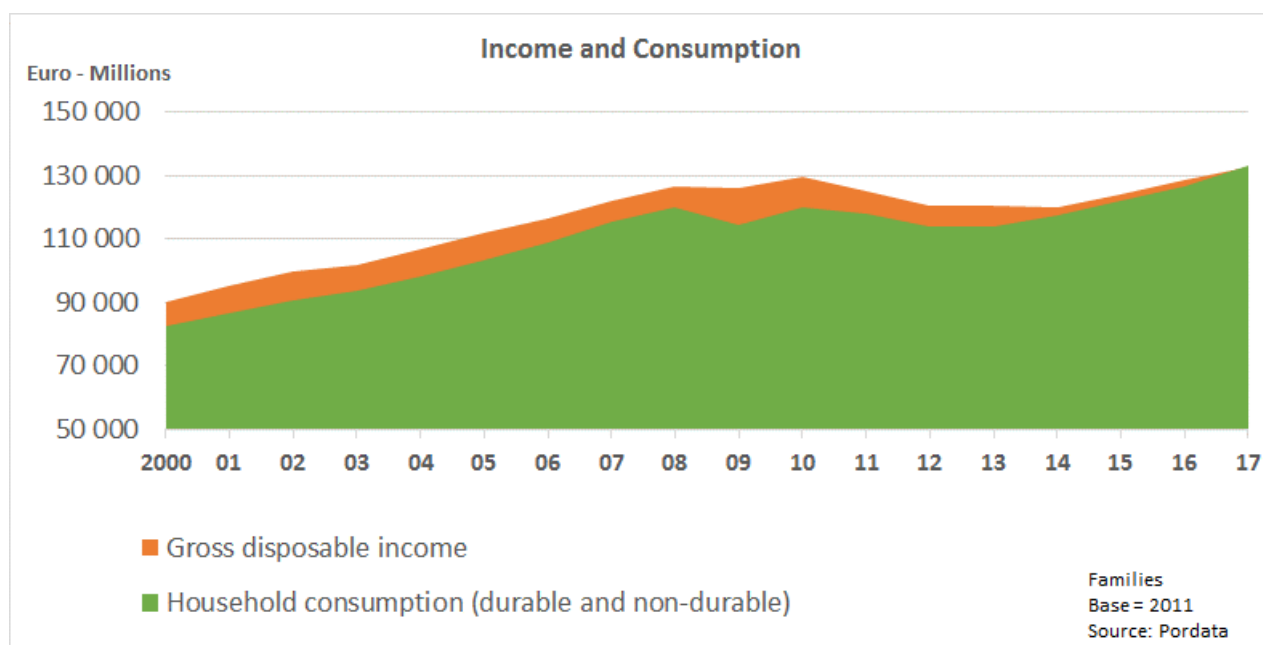


Chart 2 – Income and Consumption of Portuguese Households

Chart 3 shows the evolution, in the same period, of savings rates. The dashed line represents the trend line of the behavior of the savings rates of Portuguese Households from 2000 to 2018.

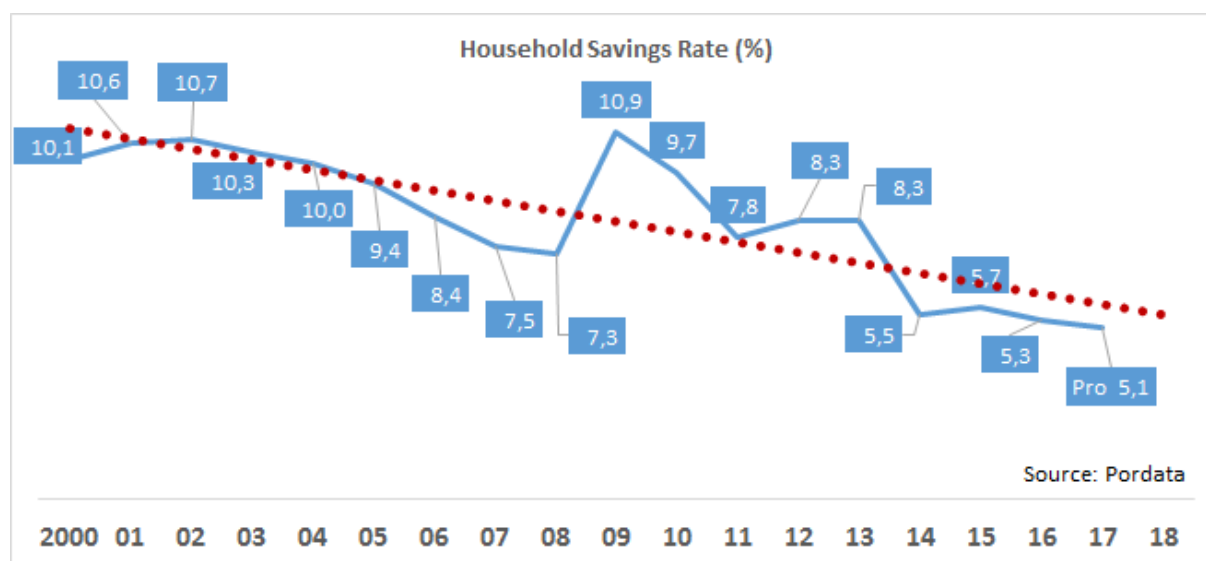


Chart 3 – Savings Rate of Portuguese Households

As can be seen, not only is there a downward trend in the savings efforts of Portuguese households, but currently it accounts for only half the value of the rate recorded in the year 2000. Despite the crisis (2008-2013) generating fear for the future, which temporarily increased the level of savings, the reality is that after the initial shock and nervousness has receded the option for higher levels of consumption has prevailed.

In summary, and as shown in Table 1, yield is multiplied in 2017 by 1.47 compared to 2000, but consumption is multiplied by 1.61.

Year	Income	Consumption	Δ
2000	90 267,90	82 504,90	7 763,00
2017	132 602,80	132 947,40	-344,60

(Base = 2011)  
Source: Pordata

Table 1 – Income and Consumption of Portuguese Households (2000; 2017)

In conclusion, it can be said that a problem that, on average, associates less savings with more credit, and consequently more debt, has been aggravated during this period, and the trend is continuing. Although this is a common framework for many countries and societies, this has prevented a more healthy and harmonious economic growth for Portugal and its citizens.

## FINANCIAL ADULTERACY

It is in thinking about this limited rationality of human conduct in relation to money that the issue of financial "*adulteracy*" will be dealt with here. There is no lack of financial management disciplines, regulators, and control mechanisms. There has been an effort to teach, from the early years, what money means and why it is needed. However, as has been seen, the numbers and behaviours do not seem to correspond to these lessons: the option for using credit mechanisms for personal consumption is markedly increasing, even for those who have high incomes.

The term financial *adulteracy* arises, therefore, from the combination between adulterating (corrupting or modifying) and literacy, and intends to highlight situations in which people (adults) contradict the golden rules of financial management. The use of easy credit, even at higher interest rates and with less compatibility with average individual or household income, exceeds the prudence required when it is necessary to moderate consumption levels.

However, it must be recognized that not all credit is bad. The use of virtuous and conscious credit, associated with certain types of acquisitions such as the purchase of housing, is a driving force of the economy and people's quality of life. The conscious, informed and responsible use of loans, if anchored in rational management of income and savings, is the basis for the development and application of financial literacy.

However, this is not the picture that has characterized the economy of most European countries since 2008/09. The deterioration of economic and financial conditions has exposed numerous situations of household over-indebtedness, associated with a high growth of default in credit agreements, and the decapitalization or even bankruptcy of many institutions of the financial system. Are we facing an individual or institutional problem or both?

The answer to this question is not simple. In the context of market economies in which people made their income application and investment decisions, the processes of choice and prioritization of needs satisfaction are not always accompanied by the economic reality that is (and should be) taught. The easiness with which credit is accessed, the countless credit offers and incentives that the financial institutions advertise, together with the fact that people want to improve their living and comfort levels much faster, tend to make the whole system over-heated. In fact, the system has anchored its growth in fast results and in anticipated profits, but with behaviours that do not respect the real growth of the overall economies, the creation of national wealth or the fundamental rule that consumption should never be higher than income.

It is known that, in principle, open competition systems allow competitive situations that respond better to the satisfaction of human needs, with a more diversified supply, at lower prices and faster. But systems are not perfect and not all decision-making follows the rules of economic and financial prudence. Free choice does not free us from our responsibilities, which is why this is a phenomenon that worries everyone. The problems of information asymmetries between consumers and credit institutions are combined with the disproportion of (in)formation and means in disadvantage of the consumers. There are, in fact, only a few entities of the financial system that follow a "prudent, correct and transparent action at all stages of credit relations with their customers as consumers".

## SOME ANSWERS

A recognition that, in the course of learning, human feelings overcome these rationalities, adulterating the good principles of budgetary management and savings which should support a future security, together with the weaknesses of the financial system, was created in 2012



(Decree-Law No. 227/2012) by the Underfunded Consumer Support Network (RACE) under the supervision of the Directorate-General for Consumer Affairs (DGC).

The Office for Consumer Indebtedness (GOEC), linked to ISEG - Lisbon School of Economics & Management - University of Lisbon and the University of Aveiro Extrajudicial Consumer Support Office (GEACE-UA) were created, respectively, in October 2006 and October 2013 and have been part of this Network since its inception. It is their function to inform, advise and assist consumers, free of charge and confidentially, in the management of their family budget, and support in the renegotiation of their charges / credits.

Aware of the underlying problems, both seek to intervene in society by providing training and information on financial literacy issues, seeking to encourage more informed, responsible and active consumers / citizens. As stated in Decree-Law no. 227/2012, the RACE offices should "inform, advise and monitor consumers who are at risk of default with credit agreements negotiated with a credit institution or that are late with those obligations."

Considering the internationally promoted good practices, notably by the OECD, carried out by RACE, and in particular by GOEC and GEACE-UA, we intend to assess the application of these practices by Portuguese consumers, in particular with regard to their relationship with credit, based on the behaviour revealed by the official statistics, namely *Banco de Portugal*.

In addition to helping and informing consumers about credit and family budget management, and ensuring technical, professional and documented support, these offices also develop important financial education in the communities and territories under their influence.

GOEC and GEACE-UA, as provided for in Decree-Law no. 227/2012, are part of the network to support bank clients in the prevention of non-compliance and in out-of-court settlement of situations of non-compliance with credit agreements.

The out-of-court banking support network is made up of legal persons, either public or private, who, under certain conditions, are recognized by the Directorate-General for Consumer Affairs after obtaining the prior opinion of the Bank of Portugal. They do not act with credit institutions, but adopt conciliation, mediation or arbitration mechanisms with a view to obtain agreements between bank clients and credit institutions. Their activity ceases as soon as they become aware of the existence of legal proceedings related to the credit agreement(s) for which the support was requested. They must respect the principles of independence, impartiality, legality and transparency, and are subject to professional secrecy.

The many cases that we have been following up on in the operation of these two offices are a real sign of the scale of the problems we have been describing and of the need to intervene with consumers and households on these matters. The reasons why people justify their situations of over-indebtedness, default or inability to manage the family budget are very diverse. There is, however, one common fact: they all affect family security, personal and professional stability, and individual and collective well-being.

It is, therefore, with all these contexts that one of the basic propositions of our work is confirmed: the elaboration of a household budget, regardless of its complexity, is fundamental for the adequate management of a household's resources. In addition, there is a real need for people to have free and confidential information, while preserving their privacy, but seeking help and advice, without this being an additional burden on the financial problems they seek to solve.

These offices, linked to two universities, are deeply committed to actions to increase people's awareness of economic changes taking place in society and to reconcile households' needs and desires with the households' budget.

## ACKNOWLEDGEMENTS

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