THE ROLE OF FINANCIAL EDUCATION IN DEVELOPING THE FINANCIAL SERVICES MARKET

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Abstract

Considering the current complexity of financial markets and of financial instruments and services, financial education is part of population's financial literacy and it ranks as paramount factor in the complex for the financial markets development.

Key words: *savings, investments, financial education, financial literacy*

1. INTRODUCTION

Just like investing in various investment instruments, savings are deferred expenses for present consumption or directing monetary resources that are available for shorter or longer period. Individuals invest their resources in financial and non-financial instruments, they open deposit accounts in banks or keep their money cash.

Nevertheless, in view of savers and investors, objectives could be different. Individuals strive for improving their prosperity and the prosperity of their families in a future period or for creating prerequisites for maintaining particular standard of living in the cases of circumstances that result in losing employment or non-employment incomes /because of loss of workability due to disease or retirement age, unemployment/. Starting own business or educational costs also suggest having savings or investments in financial instruments with positive return. The lack or insufficiency of resources in the deposit accounts or in securities or in real estates could precondition the need of bank loans for covering the abovementioned costs. Numerous statistical indicators are being implemented for measuring savings rate of the population (Atkinson and Messy, 2012), but one of the most frequently implemented ones is the proportion of net savings of a particular household/disposable income (http://data.oecd.org).

2. THE INDIVIDUALS PARTICIPATION-FACTOR INFLUENCING THE FINANCIAL MARKETS

From macroeconomic perspective people are net supplier of resources, consequently their savings in banks or their investments could have significant impact on the economy of a particular country. For example, households' savings in the pattern of deposits make up banks' deposit base that in turn could issue loans to enterprises in view of extending and developing their business via investments in real assets. Investing resources in financial instruments – subject matter of primary supply and issued by commercial entities, are all "channels" for funding their business in the pattern of raised capital /in the case of issued bonds/ or in the pattern of fixed capital /in the case of issued shares/. This way economic growth is provided with incentives; furthermore, this is done in the long run. Let us not forget the circumstance that present consumption should not be drastically limited in view of savings and investments, since it contributes for the growth of gross domestic product in the short run. On the grounds of these economic theses, the particular political decisions are to be made in order to combine the incentives of present consumption with the promotion of long-term savings and investments of individuals and households.

Research works by numerous authors on the determinants of private savings in developed and developing countries (Bailliu § Reisen 1998, Booth, Grimmond § Stroombergen 2000, Barrell § Davis 2007, Lewis § Messy 2012, Suppakitjarak § Krishnamra 2015) outline the following factors that impact savings rate variation:

- ✓ The scope of social security network.
- ✓ Economic stability and trust in the financial system;
- ✓ Incomes level and growth rate per capita;
- ✓ Interest rate and inflation level;
- ✓ The implemented measures for consumer protection via regulation and supervision.
- ✓ Access to loans;
- ✓ Population age structure;
- ✓ The impact of financial crisis and trust in financial institutions

Additionally, all these factors impact financial markets' development. Broadly speaking, the latter include markets of financial products and services offered by bank, as well as by non-bank financial institutions.

Individuals' participation at the financial markets impacts these markets in the following basic directions:

- ✓ The demand for traditional financial products and the creation of new ones are promoted;
- ✓ The requirements for disclosing key information undergo changes considering individual investors' needs for making reasoned investment decisions;
- ✓ Competition at the financial markets is provided with incentives and this has favourable impact on investors' costs;
- ✓ Complexity increases when financial products and services are being offered by particular institutional investors;
- ✓ Financial markets' regulation is being directed in view of investors' need of protection in the general context of the consumer protection concept in a particular country.

If we are to review the indicators that characterize financial markets' development, we are to find out that implementing prudency in its capacity of regulatory principle in the case of institutional investors does not limit but is leading principle in the case of voluntary saving patterns. The trends of gradual transfer to risk-based supervision means change in the supervision activity concept where to the actors at the financial markets it is of paramount importance to reasonably define their investment decisions and "decipher" market signals. In the modern market economy individuals' responsibility is increasing considering their financial well-being in the long run, including after retirement. Intrinsically inherent feature of the risk-based supervision is disclosing information about investments and the risks related to them, which is sufficient for the purposes of making investment decision. Nevertheless, the absence of basic financial knowledge does not provide the individuals with the opportunity to participate at the financial markets, be it directly or indirectly or via institutional investors with the clear understanding of their actions and the resulting consequences.

3. MAKING WELL-INFORMED INVESTMENT DECISION

Despite economic crises, financial markets cover ever increasing portion of the population and its assets. Financial markets' important characteristic is about trading mechanisms getting more complicated, as well as the investment instruments created by professionals getting more complicated and accompanied by the particular services on offer. The distribution channels for the types of savings and investment products are getting more complicated as well. Financial institutions are more diversified and this is in effect about the investment opportunities offered by them, correspondingly the related costs and risks are getting diversified too. All these require knowledge not only of instruments, but of the costs and risks related to them when making well-informed investment decision.

Financial literacy predefines individuals' investment behaviour. Investment risk, correspondingly the one somehow related to individuals' prosperity is borne by themselves, and this increases their responsibility and the need to have "culture" backed by knowledge, in view of their personal protection against these risks. For example, we observe the trend in the pension and health insurance globally, where risk is being transferred to insureds via changing the insurance model or via transfer from privately governed pension schemes based on defined benefit pension plans to privately governed pension programmes based on defined contribution plans.

On one hand, the development of information technologies in our modern world provides ever increasing number of people with the opportunity for accessing financial services not only in the country, but abroad. Additionally, technological innovations increase the risks to which consumers could be exposed considering prospective fraud because of the difficulties related to adequately regulating these non-traditional distribution channels.

The abovementioned circumstances objectively predefine the information asymmetry between the financial markets' actors and those that provide financial products and services, furthermore, about some financial instruments /for example the innovative and structural products/ we do not have sufficient information and the ways of selling them are not transparent enough. The long-term consequences of the ineffective management of individuals and their households' resources could unfavourably impact the macroeconomic development, the individuals and their families, and if scale covers significant part of the population – this could necessitate adequate social policy measures. Consequently, limiting information asymmetry is of paramount importance for the prosperity of households and country's economy in general. It includes but is not limited to the regulatory framework. The latest financial-economic crisis clearly showed that underestimating the credit market risks could have significant long-term consequences for the individual and institutional investors.

Financial literacy is not just about individual's financial education, since the manner of implementing it is as important for the effective management of individuals' investments as education. Financial education is part of financial literacy and basis for the practical implementation of information about financial markets, products and services. Financial education is not a one-time process, in whose frameworks you get basic theoretic-methodological knowledge of financial markets and financial products and services. After assimilating the basic knowledge, the individual should extend his or her knowledge while getting to know the methodological and practical aspects of investment:

- ✓ Investor's rights and obligations;
- ✓ Scope of the available information – prospectuses for public securities offering, rules on the pension funds' operations, general terms and conditions of insurance companies, tariffs for bank interests etc.;
- ✓ Rules on trading at the regulated and non-regulated markets;
- ✓ Variety of insurance and security products;
- ✓ Costs incurred when investing in various financial products;
- ✓ Risks inherent to the individual financial instruments;
- ✓ Reputation of those that offer financial products and services;
- ✓ Tax preferences;
- ✓ Regulation and supervision in view of protecting investors and affiliates;
- ✓ Product standardization etc.

Making informed investment decision is predefined by investor's appetite for risk, the stage of his or her life cycle, the practical skills obtained by him or her when it comes to investing. All these factors predefine individual's investment behaviour and the financial decisions that are reasonable from his or her point of view. Hence awareness, knowledge, skills and attitudes of investors define their financial literacy and their behaviour at the financial markets in order to achieve individual's financial

prosperity thanks to making the right investment solutions (Atkinson§ Messy 2012, Lewis § Messy 2012). However, in view of the various types of instruments used for saving purposes one needs different level of financial educational knowledge and skills. The absence of financial literacy could hinder bank savings or investments in securities, hence planning the improvement of individuals' prosperity.

Of course, if savings and investment were so easy, there would be no institutional investors and investment intermediaries. Investing with the use of financial intermediation does not exclude the cases where individuals have basic financial knowledge of sufficient scope and depth for making informed decisions on the grounds of key information and the related documentation about the most popular financial transactions before making the investment decision. Basic financial knowledge is the understanding of essence and significance of investments' diversification and distinguishing risk among the basic financial instruments. In the long-term aspect one should know the basic features of capital pension insurance, especially when it comes to implementing pension funds' organization, where the risk profile of investing pension assets corresponds to insured's age.

The specific characteristics of pension insurance result from numerous circumstances. Firstly, because of its paramount public importance. Pension insurance covers the prevailing part of population and the implementation of pension reforms necessitates public's understanding in view of political consensus. Capital insurance is long-term and often making choice is a one-time act (you cannot learn because of your own experience). Pension products and services significantly differ from the other financial products that are repeatedly bought. Pension savings are part of individual's wealth and they are being planned at the time of starting his occupational activity. The errors that were made when planning the pension programme impact the retirement and cannot be corrected. Pension system is undergoing continuous reforms because of the effect of demographic factors, the condition of the traditional "pay as you go" system etc. This means that every new generation could not fully or partially rely on the experience of the previous generations. Reforming the pension system models and establishing additional capital pension funds on the basis of defined contributions not only provides the opportunity for making individual choice, but also directs investment risk towards individuals. The actors in the pension funds are required to have knowledge of the characteristics of the various pension schemes and products, of the opportunities to participate in portfolio of different risk profile, of the manner of pension calculation, of the rights and obligations under the schemes etc.

The research works about the financial literacy of Bulgarian population being part of international comparative analysis shows that around 25% of the people are financial illiterates (made as part of an international benchmarking project FINAncial Literacy STimulation funded by the European Commission (Kamenov, 2010)

The questionnaire results indisputably show the alarming absence of financial "culture", which suggests active actions under suitable programmes and policies for improving literacy in the financial area. Bearing in mind the circumstance that financial literacy initiatives in the non-bank financial sector in Bulgaria are relatively new (Program, Financial Supervision Commission, 2012), positive changes are not expected to happen in the immediate future. Education is key to the implementation of the Europe 2020 strategy.

4. CONCLUSIONS

Financial education is a necessary prerequisite for limiting and overcoming as much as possible the information asymmetry, especially in the field of investments. Financial literacy impacts the development of financial markets and the way in which people are willing to avoid risk. The usual manner includes bank deposits/ which are ineffective for the purposes of individual saving in the long term because of their lower historical return compared to the return rate of shares and bonds/, investment in housing /from savings or via mortgage loan/, creating asset portfolio. This of course depends on the income group to which the individual or his household belongs.

Financial education improvement starts from the educational system, it undergoes development thanks to the information being provided via different communication channels – web pages, media, holding seminars, meetings with the potential investors, throughout the process of purchase and sale of financial instruments etc.

In order to overcome information asymmetry, the problems related to financial markets and products complexity and other factors that hinder financial markets' development it is important to improve population's financial education and it should serve as basis for continuously enriching individuals' financial literacy. Combining this process with adequate regulation and supervision will result in positive impact not only on financial markets' development but on public and private finance.

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