

Credit: the Financial Education and Awareness of Credit Users

Bruno Lévesque, Principal Administrator OECD Financial Affairs Division

In recent years across OECD countries, governments, financial institutions and others concerned about social welfare have become increasingly worried about the growing levels of debt taken on by consumers. Increased mortgage borrowing and the misuse of credit cards have resulted in excess indebtedness, and a rise in credit delinquencies, insolvencies and personal bankruptcies. Moreover, the emergence of alternative banking products and predatory lending are posing serious consumer protection concerns. Yet the abilities of consumers to use credit effectively and manage their money successfully are fundamental skills. Failure to develop debt management skills can cause consumers to suffer, at best, financial distress and, at worst, major crises, which can have severe consequences and lead to significant losses for financial institutions (as creditors). Despite this risk, there seems to be a persisting lack of tools and resources available to ensure that consumers have the essential financial knowledge and skills needed to manage personal credit and prevent excess-indebtedness or repair bad credit.

There have been a number of recent developments in the markets that call for enhanced financial education programmes and initiatives aimed at strengthening consumer knowledge and awareness in the area of credit:

- The changing importance of credit use: the rise of household credit in OECD countries has been fast, and data on household total debt, household debt as a percentage of disposable income and mortgage loans as a percentage of household debt show worrisome levels of consumer indebtedness as a direct effect of credit expansion in a large number of OECD countries and non-OECD economies.
- Flexible regulation based on disclosure: Despite regulatory frameworks in place to govern disclosure of credit information, consumers seem overwhelmed by the complexity and quantity of information. Even sophisticated consumers show weak understanding of their credit agreement, low awareness of their rights and responsibilities, and little shopping around for the best credit terms and conditions.
- New credit users: there has been, in recent years, a sustained increase in the number of new credit users, both in emerging markets and developed economies. A large number of consumers newly exposed to credit most often do not understand the terms and conditions of the credit products they are using, have not shopped around to compare options and do not know how and where to get neutral advice and information.
- New credit players: brokers and other intermediaries are now playing a much more active role in distributing credit products to consumers (such as residential mortgages). The growing presence of intermediaries in credit markets poses new challenges for consumer protection and awareness.
- New credit products: parallel credit markets are rapidly developing outside traditional (or mainstream) financial institution infrastructures and regulatory frameworks, to serve the more vulnerable consumers who do not have access to common credit options. Consumers have been increasingly using these alternative credit products despite their high cost and often prohibitive terms and conditions.
- Confidence and market dysfunctions: The recent sub-prime mortgage lending crisis has raised a number of questions related to the information provision and disclosure, one of which concerns the ability of consumers to understand sufficiently the nature of the financial products that they are buying into.

In order to pursue its work around the development of financial education guidelines and good practices, and particularly to address financial education and literacy concerns related to credit, the OECD has begun an analysis on a large range of credit-related issues affecting consumers of financial services. The aim of this analysis is to close some information gaps on major issues and gain a better understanding of the various credit products, regulatory regimes and challenges affecting credit users in various jurisdictions, and to identify innovative initiatives that have been developed to enhance credit users' knowledge, awareness and literacy. As a final outcome of the analysis, and in respect to its mandate to issue guidelines and good practices on financial education, the OECD will develop a set of good practices on financial education and awareness relating to credit products.