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Why every student needs financial literacy training

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Imagine filling out a job application without knowing how to read or write. Or taking your driver's test without ever having been behind the wheel of a car.

If those are recipes for failure, then so is making a major financial decision without financial literacy training. Yet, young people are routinely called upon to do just that. No wonder thousands of students leave college with significant student loan debt and no clear plan for how to pay it off.

To have a better chance at making smart decisions about money and avoiding some common pitfalls, it would help if young people receive some basic training on the financial decisions that can affect their lives for decades to come.

Unfortunately, financial literacy is not taught in all schools, though students can seek out courses to improve their chances of financial success.

This article shows some of the costs at stake when it comes to financial literacy, and looks at the skill set experts say is necessary to develop habits for a financially secure future. To gain a better understanding of what financial literacy entails, CardRatings talked to two experts in the field:

- Dr. Daad Rizk, Director Penn State's Sokolov-Miller Family Financial & Life Skills Center
- Dr. Joyce Serido, Associate Professor & Extension Specialist at the University of Minnesota's Department of Family Social Science

These experts describe financial literacy as both a set of specific skills and more generally as a mindset.

What's at stake with financial literacy?

Before setting foot on a college campus, many young Americans sign up for student loans that they may be paying off for decades.

It has become routine for people to begin their lives as independent adults with those loan obligations. The Federal Reserve's Survey of Consumer Finances finds that just over one in five U.S. households has education debt, with an average balance owed of \$40,300.

Wouldn't it be nice if students got some education about interest rates, payment schedules and the consequences of falling behind on repayment before they commit to high levels of student loan debt?



If student loan debt becomes a burden that damages a young person's credit, the cost can go beyond just that debt. For example, people with bad credit ratings pay much more for credit cards than people with good credit.

When shopping for credit cards, it is common to see a range of interest rates. For example a card might advertise rates from "13.99% to 23.99%." What does this mean? Well, if a consumer has a well-established history of responsible credit use and a reliable income, they might be eligible for a rate toward the lower end of that range.

In contrast, those with a limited credit history, questionable income or past credit problems could end up with a rate toward the higher end of the range – if they qualify for a credit card at all.

How important is this? To provide an example, CardRatings.com recently looked at five popular credit cards. The average of the lowest rates offered by these five cards was 13.89%. The average of the highest rates was 23.94%.

The difference between those two averages is 10.05%. That means that someone with a weak credit history would typically pay 10.05% more on a credit card balance every year than someone with a strong credit history. On a \$10,000 balance, this means those with bad credit could pay \$1,005 more in interest every year than those with good credit. The problem is, people often run into credit problems before they really know what they're doing. Then, the cost of having poor credit makes it more difficult to improve their financial condition.

Numbers like the amount of student loan debt and the cost of poor credit can seem scary, but young adults shouldn't be afraid of using credit. Instead, they should be empowered to use it correctly. The source of that empowerment is financial literacy.

What is financial literacy?

Financial literacy refers to a basic toolkit for making sound decisions about personal finances. This does not require becoming an economist or an investment expert. It means understanding the choices that consumers are likely to face with common financial products.

Over the course of a lifetime, individuals are likely to borrow money at some point – probably more than once. This may start with a student loan, then by opening a credit card, and later on an auto loan and a mortgage.

Besides borrowing money, it will probably be necessary to open a bank account and save and invest for retirement.

All of these decisions involve financial products that work differently from one another. In all cases, consumers have choices that could make thousands of dollars worth of difference over time. Given what's at stake, it's wise to make those decisions with some background on how these things work, rather just winging it.

Rizk explains "financial literacy is based upon providing individuals sound financial knowledge and skills so that they can make informed financial decisions and take effective actions regarding their personal money management. However, the underlying message is aimed to adjust people's core attitudes and beliefs, so that a change in financial behavior can help them reach a future of financial freedom and security."

In other words, financial literacy is about more than just what you know, but also what you do with that knowledge.

As Serido adds, "It's important to distinguish between the need to learn more about a topic versus how to develop the self-discipline to take action."

While the changes in financial behavior and the self-discipline that these personal finance experts describe come from each individual, financial literacy training can help prompt people to take the right approach. It can help consumers understand which choices work to their advantage, and give them the confidence to insist on the information they need to make sound decisions.

This has never been more important, for reasons Serido describes, "The choices we face are becoming increasingly more complex in today's shifting climate of social and economic change. For example, saving for retirement for this generation entails more of an understanding of long-term investment risks and enrolling in college often means taking on substantial debt before you even decide on a career."

What financial literacy training should include

One way to think about financial literacy is to consider the skills needed for the types of decisions you are likely to face. Rizk describes the necessary toolkit:

"Practical skills include but are not limited to budgeting, debt management, saving and investing and protection of assets. The core competencies include earning, saving, spending, borrowing, and protecting. These five core competencies cover most of the financial topics needed to achieve financial security and freedom."

You could spend a lot of time learning all the ins and outs of the various financial products available through the years. However, it simplifies things somewhat if you view financial literacy training as a systematic approach to making decisions rather than as any specific set of knowledge.

"It may be more helpful to think of financial literacy as an ongoing learning process," advises Serido. "Understand the options available to us and what is important so we can make more informed choices."

Adopting that kind of ongoing learning process should enable you to seek the information needed to make good decisions in each new financial situation you face.

Where can you find financial literacy training?

Entering into your college career can be an excellent time to ramp up your financial literacy game. After all, you may well have choices to make about student loans. A person becomes eligible for a credit card upon turning 18. If you want to buy a car, you may have decisions to make about an auto loan and car insurance.

Don't be intimidated by these decisions. Developmentally, you have reached an age when you can deal with them, if you take the right approach.

"Young adulthood is a crucial time to focus on the importance of money management," notes Serido. "As youth mature, they reinterpret and re-organize their values and beliefs about finances as they prepare for more full-time adult roles and responsibilities. It is the time to take an active interest and to be proactive to learn more about financial services, things like insurance, credit cards, even investing."

As both Rizk and Serido suggest, financial literacy is about both gaining the right knowledge and how you apply that knowledge.

Not all high schools offer personal finance courses, and those that do may offer them as electives. If you have the opportunity to take personal finance coursework in high school, grab it. You may be about to start making important financial decisions, so the timing couldn't be better.

Even if you can't do anything about gaining financial literacy in high school, college gives you an excellent opportunity to learn about personal finance.

Several prominent colleges have whole programs specializing in the subject. The following are just a few examples:

- University of Arizona
- University of California
- University of Central Florida
- Indiana University
- University of Minnesota
- New York University
- Penn State University
- Ohio State University
- University of South Florida
- University of Wisconsin

There are plenty more colleges offering personal finance coursework. You don't have to major in the subject to gain basic competency. Given the importance of these skills throughout life, you might want to make the availability of these courses a factor in your college choice.

Finally, outside of your formal education, there are numerous online sources offering consumers information about financial decisions. Sites like CardRatings.com not only offer details that make it easy to compare different products, but also "how-to" articles that help you use those products wisely.

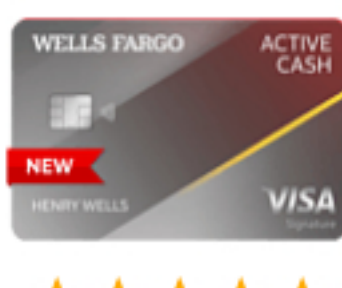
Like knowing how to read or drive, financial literacy is a building-block skill set that can help you succeed in life. The knowledge you need to be financially literate is available both formally through schools and informally through online and other sources.

How you apply this knowledge is up to you, and that's an important part of the equation. For starters though, financial literacy training can give you the tools you'll need to make the right decisions for years to come.

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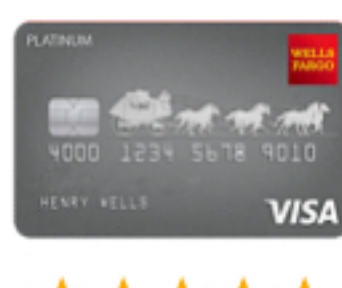
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