

FINANCIAL LITERACY AND RETIREMENT PLANNING IN CANADA

CIRANO note based on a report written by de David Boisclair, Annamaria Lusardi, Pierre-Carl Michaud, September 2014

Financial literacy and Canadians' capacity to plan for retirement is of primary importance for the policy debate over pension system reform in Canada. In this paper, we draw on internationally comparable survey evidence on financial literacy and retirement planning in Canada to investigate how financially literate Canadians are and who does plan for retirement. The Canadian case is important for many reasons. For decades, Canada has had some of the lowest levels of poverty among seniors. But important transformations in the way we provide financial security in retirement are taking place and it is unclear whether this could threaten this achievement. The capacity of Canadians to save on their own relies in part on whether they have sufficient financial literacy. The survey was conducted over the Internet between May 17 and May 31, 2012, in both French and English, using a national panel run by *Innovative Research*. Respondents were drawn from nationally representative samples and were offered a chance to win CA\$1,000. Data were weighted to ensure the sample was representative of the Canadian population. A total of 6,911 Canadians were interviewed.

We find that 42 percent of respondents are able to correctly answer three simple questions measuring knowledge of interest compounding, inflation, and risk diversification. This is consistent with evidence from other countries, and Canadians perform relatively well in comparison to Americans but worse than individuals in other countries, such as Germany. Only 30 percent of American respondents correctly answered the same questions while 53 percent of German respondents did so.

Among Canadian respondents, the young and the old, women, minorities, and those with lower educational attainment do worse, a pattern that has been consistently found in other countries as well.

It is also lower in Quebec and Atlantic provinces and, in particular, low among those speaking French in Quebec. Respondents on the coasts (British Columbia and Atlantic) did worse on risk diversification. Overall, respondents from Ontario and the Prairies performed best, while those from the Atlantic provinces did the worst. The picture is somewhat different when looking at the results according to language (i.e., whether the survey was taken in French or English).¹⁴ French respondents in Quebec do worse than English respondents in Quebec. French respondents in the rest of Canada do better than French respondents in Quebec and even than English respondents in Quebec and the rest of Canada, apart from the question on risk diversification.

Financial literacy increases with education, but even among those with high levels of education, for example college-educated respondents, only 60 percent could answer all three questions correctly.

Retirement planning is strongly associated with financial literacy; those who responded correctly to all three financial literacy questions are 10 percentage points more likely to have retirement savings. This result has been found in many countries and the estimates in Canada are similar to those of other countries. This is relevant in the Canadian context because of the relatively low level of financial literacy, even among the more fortunate Canadians (i.e., those with higher education and income), who may need to rely more and more on voluntary savings programs to fund their accustomed level of consumption in retirement.

The full study is available on CIRANO's Website at:

<http://www.cirano.qc.ca/pdf/publication/2014s-35.pdf>