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Culture and financial literacy: Evidence from a within-country language border

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ABSTRACT

We study the effect of culture on financial literacy by comparing secondary-school students along the German–French language border within Switzerland. We find that students in the French-speaking region have a lower level of financial literacy than students in the German-speaking region. The difference in financial literacy across the language groups is stronger for native students and monolingual students than for immigrant students and bilingual students. This supports the hypothesis that embedded cultural differences rather than unobserved heterogeneity in schooling are driving the effect. A mediation analysis suggests that the cultural divide in financial literacy is related to systematic differences in financial socialisation across the language groups. Students in the German speaking region are more likely to receive pocket money at an early age, and are more likely to have independent access to a bank account than students in the French speaking region.

1. Introduction

A growing body of research documents that financial literacy is associated with better personal financial decision making. Individuals with a higher level of financial literacy perform better in retirement planning (Lusardi and Mitchell, 2007; van Rooij et al., 2012), are less prone to overindebtedness (Lusardi and Tufano, 2015) and participate more often in financial markets (van Rooij et al., 2011) with better diversified portfolios (Gaudecker, 2015). Financial literacy is also related to higher yields on deposit accounts (Deuflhard et al., 2018) and a higher propensity to withdraw deposits from distressed banks (Brown et al., 2017).

Theory models the accumulation of financial literacy as an endogenous human capital choice (Lusardi et al., 2017; Jappelli and Padula, 2013), but is largely silent about heterogeneity in the initial stock, i.e. the level of financial literacy when entering the labour market. Recent empirical work focusses on the analysis of financial education interventions for the youth and adults (see Fernandes et al. (2014), Miller et al. (2015) and Kaiser and Menkhoff (2017) for meta-studies on financial education programs). But again, there is little empirical work analysing heterogeneity in the initial level of financial literacy which is very likely to influence the impact of financial education initiatives.

In this paper we study the effect of culture on the initial stock of financial literacy among the youth. Following Guisoet al. (2006), we define culture as the set of beliefs, norms and preferences that are shared among the members

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of a social group. From an economics perspective, culture may thus affect financial knowledge and decision making through systematic variation in time or risk preferences (Falk et al., 2018) or variation in social norms regarding the incurrence and repayment of debt as well as informal insurance for households in financial distress (Lindbeck, 1997). From a psychological perspective, culture may further influence financial knowledge and decision making through differences in financial socialisation or attitudes towards money (Yamauchi and Templer, 1982). Lusardi et al. (2010) document substantial differences in financial literacy among the youth in the US by ethnicity and race. This raises the question of how cultural background may influence initial financial literacy levels. Race and ethnicity are, however, often correlated with differences in socio-economic background making it difficult to identify the effect of cultural background on financial literacy.

Our aim in this paper is twofold: First, we examine the magnitude of differences in financial literacy among the youth across well-defined cultural groups. Second, we examine to what extent these differences may be accounted for by systematic variations in different dimensions of culture, i.e. preferences, financial socialisation, norms or money attitudes across these groups.

We study the impact of culture on financial literacy at the French-German language border within Switzerland. Two institutional features make this setting ideal to study questions related to culture. First, the language border allows cultural differences in preferences, norms and attitudes to coexist over time within a small geographic area.[1] Second, the language border runs through cantons, the first administrative division of Switzerland. Since most laws and policies are set either at the federal or cantonal level, there is no major change in institutions or policies at the language border within cantons. This setting allows to mitigate the two-way interaction between culture and institutions (Alesina and Giuliano, 2015). Further, there are no geographic barriers and the transport system is fully integrated across the language border. Consequently, economic conditions that potentially influence financial literacy hardly change at the language border. Importantly, we do not study the influence of language per se on financial literacy. In contrast to the recently formulated linguistic-savings hypothesis (Chen, 2013) which focuses on the one-dimensional influence of language on patience, we use language as a proxy for a broader range of cultural differences. The language border in our setting allowed for the historical persistence of cultural heterogeneity within a narrow region and we exploit it mainly for purpose of identification.

We study survey responses of 649 secondary-school students who are located in a narrow geographic region along the language border within the Swiss canton of Fribourg. Besides measures of financial literacy, our survey captures detailed information on economic preferences, financial socialisation, norms and attitudes towards money and consumption, as well as the socio-economic background. Our subjects are on average 15 years old and in their final year of compulsory schooling. The survey covers students from all educational levels.[2] Moreover, the survey covers students which are differentially embedded in local culture on either side of the language border. We can compare native students and in particular those with a single mother tongue to bilingual native students and students with an immigrant background.

Our survey population allows us to study the initial level of financial literacy at an age relevant for future financial decision making. First, the youth in our sample have already been strongly exposed to cultural influences in their parental home, from family and friends as well as at school. However, as they are all still subject to mandatory schooling, their level of financial literacy is less influenced by endogenous education, labour market and financial decisions than this would be in an adult population. Second, the majority of the students in our sample are very likely to make significant independent financial decisions within a year of the survey. In particular, two-thirds of the surveyed students plan to continue their education with an apprenticeship which will provide them with a first salary. Thus we measure financial literacy at an age when independent financial decision making is looming.

We document substantial differences in financial literacy between the two cultural groups. Responding to ten questions on financial literacy, German-speaking students scored on average 1.3 points (23%) higher than French-speaking students. Moreover, assessing their own understanding of financial matters on a five-point scale, German-speaking students scored on average 0.6 points (again 23%) higher than French-speaking students. We find that differences between the language groups are particularly strong among Swiss nationals with a monolingual family background while they are weaker among students with a bilingual family background or students with an immigration background. This supports our conjecture that locally embedded culture influences financial literacy and suggests that the observed differences are not driven by unobserved heterogeneity in schooling across the language border.

In line with previous evidence we document that - at the individual level - financial literacy is strongly correlated with financial socialisation (receiving pocket money at an early age, independent access to a bank account) and time preferences (patience). We further document a substantial difference in financial socialisation between the two cultural groups, but find no significant difference in time preferences. In a formal mediation analysis, financial socialisation, thus emerges as the strongest mediator of financial literacy between the two cultural groups.

Our findings contribute to two main strands of literature: First, we contribute to the recent literature on the determinants of financial literacy. Financial literacy among adults has been modelled as an endogenous choice (Jappelli and Padula, 2013; Lusardi et al., 2017) in which the inherent stock of financial literacy, expected lifetime income as well as time and risk preferences influence the investment in acquiring financial literacy. In line with these predictions, Meier and Sprenger (2013) show

[1] The differences in norms and preferences are for example observed in the voting behaviour. There is a clear cut in support for example for work-time regulations (Eugster, et al., 2017) or left-of-centre referenda (Eugster and Parchet, 2018).

[2] The Swiss school system has on secondary level (13–16 years old) three levels with increasing academic difficulty. Students are assigned after the 6th grade based on their academic performance to a class on basic, medium or high level.