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A Financial Epidemic: How Financial Literacy Affects College Students' Financial Management Practices and the Debt Crisis in America

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A Financial Epidemic: How Financial Literacy Affects College Students' Financial Management Practices and the Debt Crisis in America

By

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Introduction

As a young adult with a young family, I have been forced to evaluate my financial literacy. Major life decisions such as attending a university, getting married, having children, and buying a house all require a significant amount of financial knowledge and preparation. How these major life events are navigated will influence the rest of one's financial life, for better or for worse. However, as I reached each life event, I realized that I was ill prepared to make these decisions; I did not have enough understanding and financial education to be able to make sound and intelligent long-term financial decisions. As I observed my peers around me, it was clear that I was not alone. It seemed that friends or acquaintances all around me were taking out student loans and car loans, signing leases, or utilizing credit cards without having ever been taught how these actions could affect their long term financial success. I was struck with the realization that my generation's financial literacy was most likely pretty low, especially when compared to the vast amount of major financial decisions that we are expected to make between 18-25 years old. I began listening as friends described taking out student loans to pay for TVs, always keeping a balance on their credit card so as to improve their credit score, and other unwise financial decisions. Time after time, I asked myself the question, "Do people really not know that is a bad idea?" Thus, this investigation was born. I want to investigate how prepared my peers are for walking into these major life events by gauging their financial literacy. My hope is that if there is a lack of financial literacy among my peers, we can address the issue and seek a solution to ensure better preparedness and financial readiness for the future.

The Problem

In the United States, debt levels are rising significantly (NerdWallet). In addition, there is a lack of fundamental knowledge in, and a lack of motivation for, implementing good financial management practices. Some common, yet effective, financial management practices include saving, budgeting, investing, and paying bills on time. Some mistakes many make in regards to finances are using a credit card recklessly, accruing unnecessary interest payments, obtaining unnecessary loans, and not having an emergency fund. There are many varieties of debt, but the most common types of debt are credit card debt, mortgages, car loans, and student loans. Unfortunately, a vast majority of Americans are financially illiterate when it comes to financial management practices as they relate to debt. This can be a result of a lack of parental guidance during formative years, a lack of understanding of the financial world, or simply not caring to learn basic financial principles. Regardless, the level of debt for households is getting out of control. Through research, it is evident that there is a correlation between good financial management practices and less appropriate debt levels. The purpose of this study is to investigate young adults', specifically college students', level of financial literacy. Because of the rising debt levels and significant lack of understanding of finances, I want to use the results to help educate households on responsible financial management, and thus reduce household debt significantly.

Financial Management

In the world in which we live, it is very important to not only have money, but to take care of that money as well. Without money, we as a society could not survive. There are many great financial management practices one can institute into daily routines to responsibly take care of one's money and provide for a better future. The following are the main financial management practices that will be the focus of this study.

Saving. Saving is one of the most important financial management practices. It is very difficult to live life based only on the amount of money one has in his/her possession at any given time. Most of the lofty goals Americans have in life involve big financial purchases. Buying a house, getting a car, having families, and traveling are just a few examples of common goals in life, but accomplishing these things is much more difficult without saving. Although saving appears to be inconvenient because it lessens the current available spending money, having those extra funds set aside for future plans or unexpected catastrophes is exponentially beneficial. Savings is important because one can never know what he/she is going to need money for in the future. A little bit of inconvenience in the moment is better than a lot of inconvenience later.

Budgeting. Budgeting is another immensely beneficial financial management practice. Budgeting is planning out how income gets allocated. Having a budget helps one to monitor spending more closely and to only spend what is needed for certain categories. A budget acts as an accountability partner of sorts. Consider an individual with a monthly income of $1,000. Without a budget, it would be easy to spend a majority of that income on food, activities, clothes, or adventures, leaving little left for necessary bills because one could just continuously spend without realizing how quickly the income is getting used up. However, with a budget, one could set aside $400 for rent, $200 for other bills, $200 for food, and have $200 left over for clothes, activities, and miscellaneous expenses. Creating and, more importantly, adhering to a budget will increase one's awareness of spending patterns and help to minimize excessive or unnecessary spending.

Investing. Investing is a financial management tool that can greatly increase one's financial assets and portfolio. While investing can seem daunting because of the apparent volatility of the financial market, there are many options available that are not very dangerous. There are often opportunities available through employers to invest into a 401k-retirement account. Also, financial institutions have IRAs and CDs that are easy for the average risk-averse individual to safely invest in. Investing is an underrated tool to make money and to save money for retirement, future children's education, and more.

Paying bills. Paying bills is another key financial management practice. However, it is not only important that one pays his/her bills at some point, but rather that one pays them on time and in full. Everyone knows that bills need to be paid, but many do not care to pay them on time or in the full amount when the bill comes. By waiting to pay those bills, one accrues interest each day that the bill is not paid. Interest adds up quickly, which makes the overall cost of the item(s) purchased much larger than the initial cost should have been. In addition, not paying bills inevitably hurts an individual's credit score, which makes it more difficult to obtain credit in the future.

As you have read, there are many very beneficial financial management practices one can put into place in order to manage money responsibly. However, there are many misconceptions and mistakes that are made when it comes to money. Two financial concepts that can potentially cause financial harm are the use of credit cards and the absence of an emergency fund.

Credit cards. Credit cards, while helpful at times, are one of the most dangerous tools in the financial industry. Credit cards give users the illusion that they are spending “free money” without consequence, when in reality the user is borrowing someone else’s money with a very high interest rate. Credit card interest rates are most commonly around 18 percent. Users don’t usually comprehend that for every $1,000 they borrow, they have to pay an additional $180 (assuming an 18 percent interest rate) if the bill is not paid in full when the bill is first issued. This interest accrues even more interest as long as the bill is not paid in full. Ultimately, one can end up paying significantly more than what the original item was worth. Many get into serious trouble with credit cards because they do not understand how credit cards actually work. In addition, many think that in order to improve credit scores, one must always keep a balance on a credit card. All this does is accumulate interest on the bill and he/she ends up paying significantly more than the initial purchase was worth. This creates a spiraling debt cycle that is hard to escape. Excess spending with credit cards can be disastrous.

Absence of an emergency fund. An emergency fund is a set amount of money (three to six months’ wages) in case of emergencies, such as unexpected medical issues, loss of job, car accident, etc. Many people do not save money and keep it aside for events such as these, which leaves them vulnerable to extreme hardship when something unexpected happens. Having an emergency fund is a helpful tool to have a monetary back up plan and to be at peace financially in times of crisis.

We have discussed several basic financial management principles. While it is extremely important to save, budget, and to manage one's money responsibly, the biggest issue arises when debt creeps into one's financial situation. While some families may not be able to invest, have the best saving or budgeting system, or maintain an emergency fund, simply refraining from falling into debt can allow them to experience a successful financial life. Alternatively, families can save, budget, and have an emergency fund, but if they are also accruing debt and not paying that debt off in a timely manner, those positive financial management practices become fruitless. Debt is an increasingly dangerous and suffocating financial monster that grips families all across America.

Types of Debt

As a result of several negative financial management practices, many find themselves in extreme debt. People do not want to find themselves in debt, but in this day and age it is almost inevitable in order to survive. While being in debt and owing someone (a person, institution, the government, etc.) money is never ideal, some forms of debt are not as detrimental to one's financial situation as others.

Unsecured debt. Unsecured debt is any debt that does not require assets to be leveraged as collateral for the debt (Friedline and Freeman). The most common form of unsecured debt is credit card debt. Credit card debt is usually accumulated from excess spending on items that may or may not be necessities to live and survive. There are some cases, such as crises, that require the use of credit cards. As previously mentioned, when these cases arise, the bills should be paid as quickly as possible. Consistently running a balance on a credit card when it is not a requirement for survival or for making it through a temporary difficult season is harmful to one's financial wellbeing. Because unsecured debt does not provide the lender with collateral in case the debt cannot be repaid, interest rates are very high. This puts the borrower in an even worse position because the cost of borrowing increases as the interest rate increases. As a result, the borrower is required to pay much more for borrowing that money to offset the risk to the lender.

Secured debt. Secured debt is debt that is backed (or secured) by existing assets. This lessens the risk for the lender, which will most likely decrease the interest rate on the debt. Forms of secured debt are investments that increase a person's personal assets and equity. A common example of secured debt is a mortgage loan. A loan (debt) is taken out by the borrower from the lending institution to purchase the house or property. One of the terms of the loan is that if the loan cannot be repaid according to the terms, the lending institution can repossess the house or property. The property acts as collateral for the loan. Secured debt entails less risk than unsecured debt, which is why it can be beneficial to one's financial wellbeing when used correctly.

Car loans. Car loans are a type of debt that can be both unsecured or secured debt, depending on how they are issued. If a borrower gets a three-year car loan and works hard to pay it off as quickly as possible, then that is secured debt because the borrower obtains an asset (the car). Most likely, by the time the car loan is paid off, the car will still have value. However, if the borrower obtains a seven-year loan on a car, this is unsecured debt. It is unwise to get a substantially long loan on a vehicle because of how quickly vehicles depreciate. Over seven years, by the time the loan is paid off, it is likely that the borrower paid more in principal and interest than the car was even worth once it is completely owned by the borrower.

Student loans. While student loans are not considered secured, they are still a potentially beneficial resource when they are used in the correct way. Student loans are debt that is taken out as an investment for a degree in higher education. It is imperative to understand that while taking out student loans allows the borrower to obtain a postsecondary education, which is beneficial, student loans can be very dangerous. Student loans are the second highest source of debt for households in the United States (Oxford Analytica). As with mortgage loans, student loans to attend a postsecondary college or university are substantial in size. However, the loans allow for the borrower to obtain a higher education, which increases the value of the borrower in the workplace. A(n) undergraduate, graduate, or doctorate degree increases the student's personal equity because it makes the student more attractive to potential employers, and it usually increases the student's personal wellbeing, knowledge, and understanding of the world.

There are a few stipulations to student loans, however, when it comes to present-day application. In theory, student loans are beneficial because they add value to the student. However, in practicality, the levels of debt and marketability of the student for the workplace are causing problems in the current financial market. Student loans now surpass credit cards as the second highest form of debt for an individual (Grant, Anglin). It is rapidly becoming an issue for many Americans. Because of the American Dream, most Americans grow up learning about the need for higher education in order to get a well-paying job. However, this Dream mostly refers to four-year institutions. There is a general stigma that community colleges and trade schools do not meet the standards and expectations that employers look for, even if those forms of education are perfectly adequate for the field of choice. This stigma and pressure to fulfill the American Dream presents a dilemma in many young adults. Students leave high school and automatically attend a four-year institution even though they may not be able to afford it or even need to attend it for their desired career path. Thus, these students are pressured into assuming thousands of dollars in debt in order to pay for the higher education.

In present day America, there are over 45 million student loan borrowers (Gitlen). Total outstanding student loan debt is as high as $1.45 trillion and counting. The average number of college graduates with student loan debt is 60 percent, and the average debt per borrower is $27,975 (Gitlen). As of late 2016, 36 percent of 18-24 year olds have student loan debt, with a median of $10,000 owed, and over 40 percent of 25-34 year olds have student loan debt, with a median of $14,000 owed (Huddleston). Student loan debt has risen from $346 billion in quarter 4 of 2004 to $996 billion in quarter 4 of 2012 (Federal Reserve Bank of New York, 2013). As one can see, the amount of student loan debt is rapidly rising. This is attributed to rising costs of tuition, fees, etc., as well as the increasing numbers of students taking out student loans (Edmiston, Brooks, and Shepelwich).

Unfortunately, a college degree does not mean as much today as it did a few decades ago. Because collegiate markets are flooded with students, there are many more students with degrees than there are jobs available. Having a bachelor's degree is not as impressive anymore since so many people have them. As a result, thousands of indebted graduates cannot get well-paying jobs, and therefore cannot pay off their student loans in the same manner in which they were planning. Also, because student loans are not absolved in bankruptcy cases, those with student loan debt are burdened by it for years and years (Grant, Anglin). This leads to a significant issue: there are more individuals with student loan debt and fewer jobs available, which means less ability to pay off those loans. As a result, the student loan debt level is sure to continue to rise.

Overall, it is evident that fewer and fewer people are practicing good and beneficial financial management. Some have not learned how, and others choose not to in order to live a specific lifestyle that they desire. Either way, the rising debt levels for the average American is evidence that there is a significant problem that needs to be addressed.

History of Debt

Debt and credit have been around for thousands of years (Mudd). They are not recent phenomena in our world. However, the use of credit cards is a relatively new method of payment. Credit cards and debit cards "serve as a payment device in lieu of cash or checks" (Durkin). The credit card first emerged in the United States in 1946 at Flatbush National Bank of Brooklyn. It was the "first bank credit card between bank customers and merchants" (Hardekopf). In 1950, the first widely used credit card was created by Frank McNamara to be used at restaurants, called the Diner's Club charge card (Hardekopf). This sparked the credit industry in the United States. In 1958, American Express created a card specifically for "travel and entertainment expenses." The following year, revolving credit (the idea that the user does not have to pay the entire balance at the end of the cycle) was instituted. Then in 1966, Bank of America created the first "general purpose" credit card, the BankAmericard, which later became Visa in

1976. “In 1966, a national credit card issuing system was created when credit-issuing banks joined together to make the InterBank Card Association. This became MasterCard,” (Hardekopf). Because of the emergence of Visa and MasterCard, the credit card industry skyrocketed. Over the course of a few decades, credit booklets (booklets that listed the specific institutions at which credit cards could be used) morphed into cardboard credit cards, which then morphed into plastic credit cards (Mudd, Hardekopf). Magnetic strips were added in the 1970s, which allowed for credit cards to become part of the “electronic information age” (Mudd).

As a result of the ease and convenience of credit cards, and especially the revolving feature, debt started to creep into the lives of American families. “In 1970, just over one-fifth of all families owed a balance on a credit card after making their most recent card payment... By 1998, the fraction was just over two-fifths” (Durkin). In the month before a 1970 survey, 37 percent of bank-type cardholders had an outstanding balance on their account, whereas 55 percent had an outstanding balance in the month before a 1998 survey. Through the emergence of credit cards, both retailer cards and bank-type general-purpose cards, revolving debt has become more prominent for many American consumers.

The extreme rise of debt in the past few decades can be attributed to multiple things. Credit cards emerged in the 1950s and quickly became a part of the average American’s life by the 1970s (Hardekopf, Mudd, Durkin). However, with this extreme take off, the level of financial literacy did not match. The culture switched from just getting by in the 1930s and early 1940s to having an active spending lifestyle in the 1970s and 1980s. People began to charge these purchases on credit cards and run up balances (Durkin). The combination of widespread use of credit cards and lack of understanding (financial illiteracy) began the rise of debt in America.

Credit cards are not the only reason for rising household debt. During World War II, women entered the workforce in dramatic numbers while most of the men were off to fight (Coleman). Once the soldiers got back from war, many women refused to leave the workforce and go back to being a housewife and/or stay-at-home-mom. In addition, because of the advocacy for women, people of color, and other minorities during the Civil Rights Movement in the 1960s, many more people began to enroll in higher education (US Department of Education, Schofer and Meyer). Americans that would not have normally thought they could have careers because of systemic cultural norms were finally able to dream. Universities and colleges were the logical next step in starting a career because they offered professional training and expertise in one's field of choice. As a result, student loans emerged as the next avenue for debt. Whereas colleges were mainly attended by men at the beginning of the 20th century, by 1979 women had become the majority on college campuses (Center for Education Statistics and Snyder). In addition, the number of bachelor's degrees conferred from 1960 to 1970 nearly doubled (approximately 400,000 to 800,000 respectively) as younger adults sought higher education (Center for Education Statistics and Snyder). Because so many young adults finally found it possible to pursue higher education, student loans were a necessary means to an end. As a result, student loans joined credit cards in the average American's household debt.

The emergence of the ease of debt in America has left a lasting impact on the average American to this day. As of December 9, 2015, the average household has

$15,355 in credit card debt, $165,892 in mortgage debt, $26,530 in auto loans, and $47,712 in student loans (NerdWallet). The Survey of Consumer Finances found in 2001 that “11 percent of all families in the United States had debt-payment-to-income ratios greater than 40 percent” (Hilgert, Hogarth, and Beverly). In a study done measuring the correlation between the use of debit cards, credit cards, or no cards at all and household debt, it was found that household debt was the highest for households who use both debit cards and credit cards ($16,721), followed by using just credit cards ($13,657) (Lee, Abdul-Rahman, and Kim). The increasing levels of debt in the United States is staggering. These levels of debt cannot be managed in the long run. Countless students and adults have the weight of student loan debt on their shoulders, while many cannot get a sufficient job to help pay for those bills for years, if ever.

Importance of Financial Management

Since this study will be focusing on college students, it is pertinent to discuss how these students were raised and taught in regards to finances. Financial illiteracy in young adults is becoming the norm in this upcoming generation of adults. This can be assumed to be one of the reasons for rising debt and fewer amounts of people monitoring their finances. Studies show that instituting good financial management practices from a young age can produce confidence with money and correct financial management practices into adulthood.

Unsurprisingly, parents have the most influence when it comes to socializing their children (Kim and Chatterjee). As a result, how parents portray financial management in front of their kids and what parents teach their kids about finance can influence children's financial practices in the future. According to a 2013 study, "a higher percentage of respondents with savings accounts, or who had learned about helping others with money from their parents, had financial assets and were less worried about their financial situation" (Kim and Chatterjee). In addition, respondents whose parents monitored their financial decisions and habits were more likely to be good stewards of their money. Alternatively, a high proportion of respondents whose parents controlled their financial decisions as children did not have complete responsibility of their own finances (Kim and Chatterjee). This can cause a problem if parents coddle their children too much and do not teach financial independence. Children that become young adults will not have the skills to properly take care of their own money once they are on their own. In addition, it was found that by 19 years of age, "almost one third of individuals carry credit card balances" (Kim and Chatterjee). If young adults are beginning the downward slope of credit card usage and debt at 19 years old, it is likely that financial instability will be a prominent issue in the future.

Because of the significant role that parents play in their children's financial readiness, parents themselves must first be financially literate in order to provide their children with the proper knowledge and skills. In 1979, the U.S. Bureau of Labor Statistics began a survey of over 12,000 men and women ages 14-22 ("NLSY79"). The survey has been repeated over the years, with the most recent data, including a financial literacy section, being retrieved in 2012. In 2012, the respondents' ages ranged from 47-56, which is likely (or at least very close to) the ages of most current young adults or college students' parents. This study found some interesting information regarding the financial wellbeing of the parents that are influencing current young adults and college students. NLSY79 found that 52 percent of respondents have or owe money on a credit card account. The combined balance still owed on all of the credit card accounts after the most recent payment averaged $5,546.77. This illustrates the commonality of the modern American household to consistently have some form of credit card debt. A balance of over $5,000 is a significant amount of money; it is much higher than if an individual or couple used a credit card for convenience or because of an unexpected need. Such a high balance indicates a cycle of debt that accrues and never gets paid off.

A positive finding in the survey was that by ages 47-56, only 8.4 percent of respondents still had student loan debt. However, of those that still had student loan debt to pay, the mean amount still owed was $23,245.46. This financial burden almost 30 years after graduation (assuming a graduation age of 22) is troublesome because it likely inhibits these adults' abilities to invest or save for retirement, their own children's education, or an emergency fund. The survey found that 64 percent of respondents did not have an emergency fund (three month's expenses) set aside. These statistics present a worrisome concept: parents that are not financially literate enough to make responsible and consistent financial choices for themselves are likely passing on these same habits and mindsets surrounding finances to their children. Thus continues the financial illiteracy cycle.

In a separate study, it was found that financial literacy tests of high school seniors were continuously dropping between 1997-2002 (Hilgert, Hogarth, and Beverly). If that trend has continued, financial literacy levels among current high school and college students may be dangerously low. As evidenced above, parents have a great influence in the future financial wellbeing of their children. It is imperative to teach children and young adults how to properly manage finances, save, and budget in order to succeed in adulthood.

Across the board, there is a dramatic lack of knowledge and understanding of saving, credit, interest, investments, and long-term contracts (such as mortgages, car loans, student loans, etc.). Countless Americans lack fundamental knowledge of and skills with numbers, inflation, bonds, stocks, mutual funds, interest, and other economic principles (Lusardi). In addition, because of the culture of luxury spending, many do not think long term and save for retirement, children's college education, or even unexpected emergencies (Lusardi). This lack of saving has become a cultural characteristic since the mid-1980s, when the savings rate began to decline significantly and has now been around zero for years (Lusardi).

In one study, researchers found that both investment and saving were the least frequent financial management practices (Dew and Xiao). Saving is seen as an inconvenience. The money that one could save could be easily used to buy that new video game or go out to eat one more time. It seems that many do not understand the importance of saving. Many who even have savings accounts do not save regularly (Hilgert, Hogarth, and Beverly). While saving and investing are more long-term financial management practices, there is still a lack of everyday management practices. Rather than implementing structured and physical budgets that can be seen and used, many choose to use mental or short-term budgets (Hilgert, Hogarth, and Beverly). It is obvious that there is a lack of knowledge and a lack of motivation to implement and consistently utilize good financial management practices.

Through countless studies, it is clear that those with good financial management practices have less debt. In a study measuring the financial management practices of couples that believed they had great marriages, there were three overall themes that the researchers concluded as a result of the study. First, typically one spouse handled the day-to-day finances. Second, the couples had little to no debt. Finally, the couples usually lived within their means (Skogrand, Johnson, Horrocks, and DeFrain). While it is great that the couples believed they had great marriages, it is interesting to note the financial management practices that these couples put into place to achieve these three themes, specifically that they had little to no debt. The common practices that were evident throughout the study were: paying bills, keeping track of spending, using a budget, paying cash for vehicles, using credit cards only for convenience, paying the bill in full each month, saving, frugality, investing, and not allowing themselves to go into or stay in debt (Skogrand, Johnson, Horrocks, and DeFrain). These are all sound financial management practices that can be associated with the fact that the couples had little to no debt. In a separate study, researchers found that saving and investing were negatively associated with debt (Dew and Xiao). This means that respondents who saved and/or invested had less debt, and those that did not save or invest had more debt.

Financial Literacy

As the evidence has shown, financial management plays a large role in the amount of debt an individual accumulates. It is obvious that to decrease the debt problem, people must make smarter financial decisions. However, it is not that simple. To have sound financial management practices, one must first have financial literacy. Financial literacy has been defined in many ways (Percy and Arnott-Hill). Looking at many proposed definitions, the commonly held idea is that financial literacy is one's knowledge of basic financial concepts and the ability to use this knowledge to make apt financial decisions in everyday life. Financial literacy has been widely studied over the past few decades. Throughout research, it is evident that financial literacy is a key component in making important financial decisions (Percy and Arnott-Hill, Lusardi and Mitchell (2014), Lusardi and Tufano (2009)). Lusardi and Tufano (2009) found that only around one-third of the population understands basic financial concepts such as compound interest and credit cards. In addition, the President's Advisory Council on Financial Literacy found that "far too many Americans do not have the basic financial skills necessary to develop and maintain a budget, to understand credit, to understand investment vehicles, or to take advantage of our banking system" (PACFL 2008).

With the exorbitant amount of financial decisions young adults and adults must make, this lack of financial literacy is a problem. Young adults that are fresh out of high school must make decisions regarding student loans, bank accounts, credit cards, and how to survive as financially independent individuals. Likewise, adults must continually make decisions in regards to budgeting, investments, retirement plans, savings, and more. With such a comprehensive list of important financial decisions (many of which have long lasting effects), it is imperative to have the knowledge and confidence to make beneficial decisions for one's future. However, as the research has shown, the vast majority of Americans do not have such knowledge or competency in making these decisions. Moreover, there are many who are making important financial decisions without proper education or training. As a result, this financial illiteracy translates into poor decisions and negative financial outcomes, such as the rising debt problem that suffocates so many Americans today.

Data Results

The purpose of this study is to evaluate the financial literacy of college students in order to more accurately identify the root problem of the financial management issue in our current culture, and to hopefully propose a solution based on those findings. Appendix A contains a proposed survey to send out to college students at universities looking to gauge their students' financial literacy.

The survey is broken up into three sections: background, financial knowledge, and financial management practices. The background section simply identifies the respondents' age and grade level. The financial knowledge section seeks to gauge how prepared students are when it comes to finance upon entering a university. Questions ask about past financial courses taken, parental involvement in financial education, and familiarity with financial concepts such as compound interest, revolving credit, and loan repayment. The financial management practices section seeks to identify the current financial practices of the respondents. Questions revolve around bank accounts, budgeting, saving, spending habits, credit cards, student and other loans, and common components within a loan. This survey would help to identify areas of concern that need improvement. It would provide the university administering the survey the information needed to understand where and how it can seek to better the financial capacity and literacy of its students.

In 2016, LendEDU sent out a similar survey to the one mentioned above to "455 undergraduate and graduate students. In total, each student answered 25 unique questions related to personal finance and managing money" (Rathmanner). Their findings reveal an interesting and disturbing trend amongst college students. When it comes to knowledge of basic financial concepts, 43 percent could not name one major difference between a credit card and a debit card, 23 percent could not name one major difference between a checking account and a savings account, and 68 percent did not know what a 401k or IRA is used for. When it comes to saving, 58 percent of students did not save each month, 43 percent did not track monthly spending at all, 82 percent saved 30 percent or less of their monthly income, and 81 percent did not have an emergency fund. When it comes to financial education, 30 percent of students had not been taught how to manage money by their parents, 51 percent had never received personal finance education in high school, and 45 percent had never taken a college personal finance course and were not planning on taking one. It is evident that there is a dramatic lack of understanding of basic financial concepts, which is translating into poor financial management. In this same study, 59 percent of students rated themselves a "C" or worse when it comes to managing finances and money, while 25 percent said alcohol or drugs were their biggest monthly expense (Rathmanner).

Between February 22, 2018 and March 7, 2018, LendEDU administered another survey to 850 Generation Z student loan borrowers, between the ages of 18 and 23, currently attending a four-year college or university on their knowledge of student loans (Brown). The survey found some disturbing results, considering the fact that all respondents were student loan borrowers themselves. Only 22.82 percent of respondents could identify what FAFSA stands for. As it pertains to the terms of student loans, 28.82 percent could identify the correct current interest rate, 36.35 percent knew the repayment term, and 36.24 percent and 26 percent could correctly identify whether or not interest accumulates during deferment for unsubsidized and subsidized loans respectively. The majority, 52.94 percent, of respondents believed that they would be helped by federal student loan forgiveness programs after graduation, which according to Brown only happens to maybe 3 percent of student loan borrowers. Lastly, 32.24 percent had never looked at their student loan accounts. These statistics are troublesome. If 60 percent of college graduates are taking out student loans, yet they aren't knowledgeable about the terms and conditions of those loans, it is no wonder there is such a debt crisis for the average American. I believe the poor financial management practices and financial illiteracy of college students can be attributed to the lack of proper financial education that would help prepare these students.

Solution

Since we know that financial literacy is so important to our financial management practices and therefore debt issue, it would appear that the solution to this problem would be simple: make financially illiterate people financially literate. However, this simple proposal is much more complex. The majority of research surrounding financial literacy in the past few decades has supported the fact that financial literacy is the problem. However, fewer researchers have delved into how to fix the problem. Current researchers have been investigating the effectiveness of financial education. Lusardi and Mitchell (2014) investigated many experiments and researchers who were seeking to find a correlation between financial literacy education (high school and college classes, seminars, job training) and financial behavior (saving regularly, budgeting, investing, etc.). They found that, of the minimal research currently available, there were flaws in the experiments and data collected. Some experiments involve short "quick fix" seminars that do not account for the extensive need for comprehensive understanding of finance. Also, they found that few experiments had a test group and a placebo group, which makes it difficult to assume causality. In addition, Percy and Arnott-Hill found that there is inconsistency in the financial literacy education research. While some experiments suggest that financial education produced positive financial behavioral changes, others found no correlation at all (Percy and Arnott-Hill). Thus, it is difficult at this point with current research to definitively say that there is a causality and effectiveness between financial literacy education and financial behavior.

While there is not sufficient research and evidence surrounding the effectiveness of financial education at this current point in time, I believe that is where our solution to this epidemic begins. Simply put, Americans cannot be expected to take care of their money if they are not taught how. While the "right way" to go about educating students on finances has yet to be determined, I propose that personal finance courses in high school and college should be required rather than stand as possible electives. As of 2018, only one-third of k-12 schools require graduates to have taken a personal finance course ("Survey of the States and the Progression of Economic Education"). Personal finance courses should teach students how to budget, save, invest, utilize a bank account, and other basic financial management practices. In addition, these courses should explain how credit cards work, the loan process, including terms and agreements, and – most importantly – why these financial management tools and concepts are so important. These financial concepts can have lasting effects on students' lives, yet few truly understand their importance. If having designated courses can help bring awareness to students of these concepts, hopefully many would begin to make sound financial decisions in their every day lives, which would hopefully lead to a more promising financial culture.

In addition to mandatory financial education courses in high school and college, I think it is imperative that parents take a much more active role in teaching their children about finances. A current problem with this solution is that modern parents themselves do not understand these concepts. We as a society need to make financial literacy a priority to our current adults, so that they can then transfer that information to their children. There are several options to better educate our adults. Some of these options include: financial classes in the workplace, workshops ran by financial institutions, and convenient and easy to understand websites to serve as resources for those unable to go to a class. Hopefully through such endeavors, current adults can be better equipped to make intelligent financial decisions and to pass down that knowledge to the next generation. At such a young age, students begin making financial decisions that will follow them for the rest of their lives. It is imperative that they have the tools and knowledge readily available to them in order to make the best financial decisions that they can.

Conclusion

It is obvious that the current American financial culture is headed down a dangerous path. Basic financial management practices such as saving, budgeting, and investing are not as common knowledge as they should be. Even if individuals understand these basic concepts, few seem to actually put them into consistent practice in their every day lives. In addition, debt levels are continuously on the rise with the use of credit cards and the taking out of loans. Student loans have risen to the second highest debt group for the average American, yet studies have shown that there is a lack of understanding about the terms and conditions of said loans. Overall, financial literacy amongst Americans is surprisingly low. The strong correlation between proper financial management practices and debt level emphasizes the importance that people understand how to properly manage their finances. The problem and solution are the same: financial literacy. People do not understand finance, so they get themselves into trouble with poor management practices and debt. The solution is to educate the young adults of the upcoming generation with financial preparedness. By supplying students with the tools and knowledge necessary to make sound financial decisions, the debt crisis in America could begin to dwindle. As a result, American financial culture could improve drastically for generations to come.

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Appendix A:

Financial Literacy Survey for College Students

Background

Age: _________

Class: Freshman ______ Transfer Student _____ Senior _____

Financial Knowledge

Have you taken a personal finance, economics, or similar course? YES/NO

If so, which classes have you taken? And when did you take the course? ______________________

How did your parent(s) talk with you about or prepare you for money management? ________________

What is your experience with money management education up to this point? _____________

Do you understand how compound interest works? YES/NO

If yes, solve the following question: If you put $100 into a savings account that offers 2% interest, how much money will you have at the end of the year if you don't touch the $100? __________________

Do you know what revolving credit means? YES/NO

Do you know how receiving a loan and loan repayment works? YES/NO

Financial Management Practices

Do you have a bank account? YES/NO

If yes, Checking Account? YES/NO Savings Account? YES/NO

Do you budget your income regularly? YES/NO

If yes, do you adhere to that budget on a consistent basis? YES/NO

Do you save your income regularly? YES/NO

What percentage of your monthly income do you spend on Entertainment? Monthly Expenses? Savings? (3 separate questions)

A. 0-25%
B. 25-50%
C. 50-75%
D. 75-100%

Do you currently have a credit card? YES/NO

If so, how many? ___________________

Do you currently have an outstanding balance on a credit card? YES/NO

If so, what is your approximate running balance? __________________

Have you taken out student loans? YES/NO

Do you have or have you ever had other loans besides student loans? YES/NO

If so, what kind(s)? ________________________

If you have ever taken out a loan, did you understand the terms, conditions, and responsibilities of the loan? YES/NO

What does APR stand for?

A. Approximate Payment Rate
B. Annual Percentage Rate
C. Annual Payment Required

What is the definition of APR?

A. The stated or given interest rate for the loan
B. The actual interest rate paid for the loan, accounting for compound interest
C. The total amount of interest paid on the loan

What statement best represents the maturity of a loan?

A. The total time it takes to pay off the loan
B. How long it has been since the loan was created
C. The age of the borrower taking out the loan

What is an amortization table for a loan?

A. Display of the payment breakdown of principal over the life of the loan
B. Display of the payment breakdown of interest over the life of the loan
C. Display of the payment breakdown of principal and interest over the life of the loan

What are some ways that you could have been better prepared for making financial decisions? _________

Would you be interested in taking a course helping to lay out basic financial concepts for money management? ___________