

Enhancing Financial Capability and Inclusion in the Philippines - A Demand-side Assessment



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Abbreviations and Acronyms

ADB	Asian Development Bank
AML/CFT	Anti-Money Laundering/Combating the Financing of Terrorism
BSP	Bangko Sentral ng Pilipinas
CAPI	Computer-assisted Personal Interview
CCT	Conditional Cash Transfers
EA	Enumeration Area
EAPF	East Asia and Pacific Region
EEC	Étude Économique Conseil
FCPD	Financial Consumer Protection Department
GSMA	GSM Association
IFAS	Inclusive Finance Advocacy Staff
KFS	Key Fact Statements
KYC	Know Your Customer
MFI	Microfinance Institutions
MFS	Mobile Financial Services
NCR	National Capital Region
NFIS	National Financial Inclusion Strategy
NSSLA	Non-Stock Savings and Loan Association
PCA	Principal Component Analysis
PDP	Philippines Development Plan
PHP	Philippine Peso
PPS	Probability Proportional to Size
PSA	Philippines Statistics Authority
PSU	Probability Sampling Unit
WBG	The World Bank Group

Preface

Financial capability, as defined by the World Bank and in this report, is the capacity to act in one's best financial interest, given socioeconomic and environmental conditions. It encompasses knowledge (literacy), attitudes, skills and behavior of consumers with respect to understanding, selecting, and using financial services, and the ability to access financial services that fit their needs (World Bank 2013d).

Financial capability has become a policy priority for policy makers seeking to promote beneficial financial inclusion and to ensure financial stability and functioning financial markets. Today people are required to take increasing responsibility for managing a variety of risks over the life cycle. People who make sound financial decisions and who effectively interact with financial service providers are more likely to achieve their financial goals, hedge against financial and economic risks, improve their household's welfare, and support economic growth. Boosting financial capability has therefore emerged as a policy objective that complements governments' financial inclusion and consumer protection agendas. To this end, policy makers are increasingly using surveys as diagnostic tools to identify financial capability areas that need improvement and vulnerable segments of the population which could be targeted with specific interventions.

In response to a request of the Bangko Sentral ng Pilipinas (BSP) and as part of a broader engagement on enhancing financial consumer protection and education in the Philippines, the World Bank has implemented a financial capability survey. Financial inclusion, financial literacy and consumer protection are important priorities for the BSP and the Philippines government. Consumer protection and education are critical elements in building an inclusive financial system and BSP seeks to identify sustainable methods of delivering financial education through effective partnerships. As the BSP's financial inclusion initiatives are expected to usher in more Filipinos, including the previously marginalized sectors, to access a wide range of financial services from a variety of financial institutions, they need to acquire knowledge and develop skills to enable them to make better financial decisions. The proposed survey constitutes a key diagnostic tool that aims to guide BSP on the models for delivering financial education and to set quantifiable and concrete targets. Moreover, it serves as a baseline against which the effectiveness of future financial capability enhancing programs can be assessed. So far, no financial capability surveys have been conducted in the Philippines and it is one of the very first such experiences in the East Asia and Pacific Region (EAPF).

The key findings and recommendations presented in this report cover 3 main areas: 1. Financial Inclusion, 2. Financial Capability, and 3. Financial Consumer Protection. The remaining chapters are structured as follows. Chapter 1 explores the

financial inclusion landscape in the Philippines. Chapter 2 gives an overview of Filipinos' levels of financial capability, in particular about their financial knowledge, attitudes and behaviors. The last chapter investigates if the products which financially included individuals use are effectively meeting their needs.

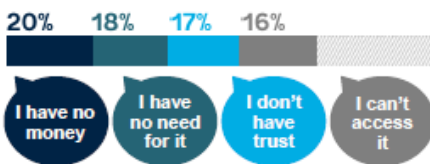
Key Findings

How Financially Included are Filipinos?



41% of surveyed adult Filipinos do not use any formal or commercial financial product.

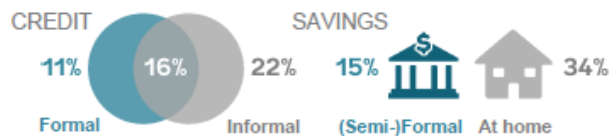
Adults without an account report lack of money, lack of need, lack of trust, and lack of physical access as the main reasons.



82% of those in the top quartile of the income distribution and 66% of women use a formal financial product, compared to 42% in the bottom quartile and 50% of men.



Adult Filipinos either use formal, informal, or a mix of both methods to borrow, and save both formally and at home.



How Financially Capable are Filipinos?

On average, adults were able to answer 3.2 out of 7 financial literacy-related questions correctly.



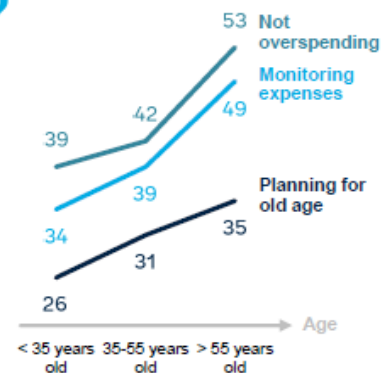
While 77% were able to perform simple divisions, about half of adults knew how to calculate simple interest and inflation, and understood the purpose of insurance.



Respondents scored low in behaviors related to budgeting, but showed strengths in other areas:

- Planning for unexpected expenses (67) ✓
- Achievement orientation (66)
- Farsightedness (64)

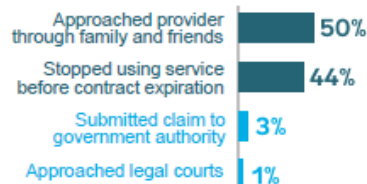
- Inclination to save (46) ✗
- Budgeting (44)
- Living within means (43)
- Refrain from overspending (42)
- Monitor expenses (38)



Overall, financial behavior scores improved with age.

How Financially Protected are Filipinos?

17% of respondents experienced a conflict with a financial service provider in the past 3 years. Of them, only 27% took action to try to solve it.



To redress a dispute, regulators and legal courts were barely sought.



The main three causes for inertia are the perceived lengthy time of proceedings (66%), the view that providers are too powerful (62%) and the lack of trust in the efficiency of authorities (59%).

Summary of Key Recommendations

	Recommendations	Responsible	Term ²
Financial Inclusion	Develop National Financial Inclusion Strategy (NFIS)	BSP	ST/MT
	Continue progress on expanding the physical reach of financial access points	BSP	MT
	Design financial products with an evidence-based approach to satisfied the needs of consumers, particularly the financial excluded population	BSP, Private Sector	LT
Financial Capability	Develop a National Financial Education Strategy	BSP, Department of Finance, industry associations, consumer associations, and relevant other stakeholders	MT
	Consider engaging mass media and edutainment to enhance the financial capability of adults	BSP, Department of Finance, industry associations, consumer associations, and relevant other stakeholders	MT
	Evaluate scope and delivery mode of financial capability-enhancing programs within conditional cash transfer initiatives	BSP, DSWD	MT
	Evaluate the possibilities of using nudges and reminders, default options, as well as smart product designs	BSP, Department of Finance, industry associations, consumer associations, and relevant other stakeholders	MT
	Consider development of a curriculum that integrates financial education as one of the core subjects for school-based financial education programs	BSP, Department of Education	LT
Consumer Protection	Require financial institutions regulated by BSP to meet internal dispute resolution standards set by BSP	BSP	ST
	Use supervisory tools such as mystery shopping to gain insights into why banks' products appear to be less satisfied	BSP	ST
	Consider making external complaint resolution schemes more effective	BSP	LT

² ST, short term, indicates action can be undertaken in 0-6 months. MT, medium term, indicates 6 months-1 year. LT, long term, indicates 1+ years

Executive Summary

Financial Inclusion

Approximately 42 percent of surveyed adults in the Philippines report owning an account at a formal financial institution, a commonly used metric for international comparison. As compared to other lower-middle income economies, the Philippines have a relatively high level of financial inclusion though it does lag behind the average level among East Asian and Pacific economies. This pattern is consistent with the other financial sector indicators for the Philippines as compared to its country peers.

When the definition of financial inclusion is broadened to include a more complete range of financial products, participation in financial sector in the Philippines is broader. Approximately 41 percent of surveyed Filipinos report currently not using some type of formal or commercial financial product, including mobile financial services, loans, pensions, car or building insurance, and money transfer services.

Women in the Philippines are considerably more likely than men to be financially included. Women are sixteen percentage points more likely than men to be financially included, a difference that remains statistically significant even after controlling for income, education, and a range of other individual characteristics. The gender gap in the Philippines differs sharply from trends observed in other countries: according to the 2011 Global Findex survey: 55 percent of men worldwide have an account, compared to 47 percent of women, a gap which grows larger when the sample is restricted to the developing world, and larger still when only those living on less than \$1.25 per day are considered.

There are significant differences across income categories in the use of financial services, a potentially key obstacle to achieving inclusive growth. While 82 percent of those in the top quartile of the income distribution use a formal financial product, just 42 percent of those in the bottom quartile percent report the same. Without the necessary tools to manage their day-to-day finances and make important educational and entrepreneurial investments, the poor in the Philippines are thus limited in their ability to improve their economic well-being and fully reap the benefits of national economic growth.

There is significant variation in financial inclusion across regions and rural/urban lines within the Philippines. Inequality in access to financial services is naturally exacerbated by the archipelago geography of the country, consisting of more than 7,000 islands. While approximately 75 percent of adults living in the National Capital Region (NCR) region report using a formal financial product or service, only about 45 percent of adults in SOCKSARGEN, Zamboanga, and Cagayan do the same.

Mobile financial services (MFS) have found relative success in the Philippines with 17 percent of adults reporting current use of an MFS product. This figure is in line with data from the 2011 Global Findex survey which found that 15 percent of adults reported sending or receiving money via a mobile phone. This sets the Philippines apart from many other developing economies, where mobile financial services (MFS) have struggled to take off. While there is some evidence that mobile financial services have successfully reach otherwise unbanked adults, MFS, like other financial services, are still used disproportionately by the wealthy. Approximately 28 percent of adults in the highest income quartile report currently using a mobile financial service, as compared to 6 percent of those in the lowest income quartile.

Forty-nine percent of Filipinos report some type of borrowing, across a range of formal and informal systems. Eleven percent of adults in the Philippines use exclusively formal credit products (bank loan, microfinance loan, credit card, mortgage, etc.) to borrow while 22 percent of adults meet their borrowing needs relying only on informal source such as a money lender, family member, or friend. Approximately 16 percent of adults blend informal and formal sources of borrowing. The prevalence of informal borrowing is considerably higher than the average in other lower-middle income or East Asian economies (31 percent and 28 percent, respectively). Given that 53 percent of “informal only” borrowers report having an account, it appears that the prevalence of informal borrowing is driven both by ineligibility and lack of physical access.

Fifty-seven percent of Filipinos report some form of saving or risk management behavior, including formal and informal savings, investments, private pensions, or car or building insurance. Thirty-four percent of adults report saving at home, which is consistent with 2011 Findex results that show Filipinos are considerably more likely than adults in other lower-middle income or East Asian economies to save informally, that is, usually neither formal nor semi-formal (e.g. savings groups) mechanisms. Formal or semi-formal saving instruments are reportedly used by 15 percent of the adult population. Sixty-two percent of informal savers have an account, which suggests that the formal financial system is not fully meeting the savings needs

of its clients. Just under half of adults report using neither informal, semi-formal nor formal methods to save.

The most commonly reported obstacles to formal account ownership are lack of enough money to use one – reported by 20 percent of adults without an account – and lack of need for an account – reported by 18 percent. A lack of trust in financial institutions is a significant obstacle for greater financial inclusion in the Philippines. Seventeen percent of unbanked adults report that they do not have an account due to a lack of trust. Other commonly cited barriers – such as distance and documentation – can be directly addressed by public policy. Sixteen percent of unbanked Filipinos are deterred from opening an account due to a lack of physical access.

Recommendations³

There is a need to continue progress on expanding the physical reach of financial access points. Sixteen percent of unbanked adults cite distance as a barrier to financial access. This is of course challenging in a country with over 2,000 inhabited islands. However, with 8.6 access points per 100,000 adults, the Philippines lags behind other economies in the reach of the financial sector, including Indonesia and Malaysia, countries that face similarly challenging geographic obstacles. Many of the existing financial access points in the Philippines – which include commercial banks, thrift banks, rural banks, cooperative banks, ATMs - are concentrated in urban centers. According to BSP, as of end-September 2014, 595 of 1,634 cities and municipalities do not host a single banking office. Agents, ATMs, and microbanking offices (MBOs) should be fully leveraged to expand the reach of the financial sector in a cost-effective and sustainable basis. Improved data on the precise location of all financial access points can help policymakers to develop incentives – including waiving process fees - and help inform investment and operational decisions of the private sector.

Public and private sector actors should take an evidence-based approach to the development of financial products that meet the needs of consumers, particularly those at the bottom of the pyramid. Despite banks' efforts to extend products and services to low-income clients, the survey data indicates a lack of suitable products addressing the needs of large parts of the population. Research should be conducted to understand the effectiveness of microdeposit accounts and associated public awareness

³ It should be noted that the recommendations provided in this report mainly arise from this demand-side assessment and can therefore not be seen as being exhaustive.

campaigns. Approximately ten percent of unbanked respondents report that high costs are a main barrier to formal accounts and an additional ten percent report that documentation requirements are significant obstacles. These findings suggest that the costs associated with these accounts remain prohibitively high for a significant portion of the population or that the availability of microdeposit accounts are not widely known. Restrictions that may disproportionately affect poor adults in accessing and using mobile financial services – such as the prohibition on agents performing account openings – should also be reconsidered.

The achievement of scale through improving availability, product design, and consumer choice for social transfer and remittances payment products can boost financial inclusion. More than fifty percent of 4Ps payments are made over-the-counter while the remaining payments are distributed through somewhat restrictive cash cards. Improvements to the reliability, product choice, recipient financial education, and partner arrangements of these systems could boost demand for other financial services among program recipients. The formal financial system may also be able to further capture the enormous regular transfer of domestic and international remittances. The SMART Padela program and SMART’s partnership with the National Commercial Bank in Saudi Arabia are good models.

To align and unite initiatives pursued by various agencies in the Philippines, there may be merit to put in place a National Financial Inclusion Strategy (NFIS). Such a document can promote a more effective and efficient process to achieve significant improvements in financial inclusion. An NFIS can also be a valuable mechanism for aligning and scaling up initiatives from the public sector, financial and nonfinancial institutions, and other stakeholders. A range of countries have now launched a NFIS, including Malaysia, Indonesia, Tanzania, and Nigeria. A NFIS could also usefully set forth ambitious but achievable quantitative targets for increasing financial inclusion in the Philippines. Well-defined, publicized, and monitored targets can be a powerful tool to translate the ambition of goals into practice outcomes. Tracking progress against targets can provide valuable insights into obstacles and/or opportunities for financial inclusion. Embedding financial inclusion modules into regular household surveys is a critical element of a robust monitoring and evaluation framework for financial inclusion. An effective secretariat empowered and enabled to monitor and measure progress towards increasing financial inclusion is critical for the successful implementation of the NFIS. Going forward, Philippines could build on the earlier data initiatives and leverage expertise available in Inclusive Financial Advocacy Staff at BSP to facilitate NFIS measurement and monitoring.

Financial Capability

Knowledge of basic financial concepts is a significant challenge in the Philippines which is mirrored in the fact that on average, Filipino adults were able to answer less than half (3.2) out of 7 financial literacy-related questions correctly. A more worrisome finding is that around a fifth of the surveyed population did not answer more than one question correctly, while still a significant proportion of respondents, one out of ten adult Filipinos, did not appear to have a sound grasp of any of the basic concepts being tested. One of the most notable knowledge gaps which deserve policy attention is that only around a third of the adult population appears to be comfortable in solving simple numeracy task required to shop around. The working of compound interest seems to be the most difficult to understand and only 29 percent of the sample managed to answer the respective question correctly.

Segments of the population that appear to struggle the most to understand basic financial concepts include adults who did not save as a child, non-household heads, as well as men. Unlike most other countries where women display lower financial knowledge than men, the gender gap identified in the Philippines is in favor of women. For example, female respondents are four percentage points more likely than men to understand the primary purpose of insurance products as a risk management tool.

An international comparison to survey participants in eleven countries shows that although survey participants in the Philippines outperform respondents from eight other countries in their inclination to think about the future, this forward-looking attitude does not translate into sound financial decisions. Specifically, even though only 27 percent of the respondents think that the future will take care of itself, less than a quarter of the surveyed respondents aged 60 and younger do have sufficient provisions in place to cover their expected old age expenses. Nevertheless, a substantial proportion of those without any provisions are either not worried at all or only a bit worried (64 percent) about their long-term financial security. This low score is of particular concern and deserves policy attention given its implications for people's long-term wellbeing.

Two characteristics which are strongly correlated with better scores on financial capability are people's educational attainments and their financial knowledge/literacy levels. Survey participants with higher educational attainment outperform their counterparts with lower education in the areas of choosing financial products, managing their daily finances, and in planning for old age expenses. The

most remarkable gap between highly educated Filipinos and those without any educational attainment can be observed in their ability to live within means. While those with completed tertiary education achieved a living within means score of 51, those with no schooling scored only half as high. Likewise, higher financial literacy is strongly associated with higher scores in several areas, in particular in those related to daily money management and planning for retirement age expenses.

The survey results further suggest that a generational gap exists with the younger generation lagging behind older survey participants, in particular in their ability to manage day-to-day finance and to plan for old age expenses. For instance, while those aged 35 or younger achieved a score of 26 on planning for old age expenses, people between 35 and 55 scored 31, and those 55 and older scored the highest score (35).

Savings habits and preferences formed in early life stay with Filipinos into adulthood and regular use of a broad range of media has profound effects on how they make financial decisions. Those who began savings habits as children display better attitudes towards savings than those who did not save in their childhood. Moreover, respondents who already saved in their childhood tend to outperform their counterpart group who did not form savings habits in early life in the areas of choosing financial products and services, monitoring expenses, and planning for old age expenses. Notably, as compared to those who do not use print, broadcast, and internet media at a regular basis, more active media consumers tend to score higher in almost all assessed financial capability areas, suggesting that any efforts to enhance financial capability in an effective manner should involve a very broad media engagement.

Recommendations

National Financial Education Strategy can be an important organizing framework to scale up and maximize effectiveness of various interventions on financial education in the Philippines. Such an effort at the national level can promote co-operation between relevant stakeholders, avoid duplication of resources, and minimize gaps and overlaps in addressing the challenges identified through this survey. The strategy should outline a set of priority programs to enhance financial capability levels of the overall population and specific subgroups. Priorities could be set based on a number of criteria, including the need, goals, costs and availability of resources. Other essential elements of such a document include the roles and responsibilities of all involved stakeholders, the main groups which shall be targeted, a framework for monitoring and

evaluation, and most importantly the resources for the implementation of the strategy. For more information about the process of developing a NFES see OECD/INFE High Level Principles on NFES.⁴

Use of mass media, and edutainment in particular, can be an effective channel in delivering financial education to adults. The field of behavioral economics has documented a plethora of behavioral biases which can prevent people from translating their intentions into action. For instance, people tend to be biased towards the status quo and to choose the default option. They may also suffer from self-control issues, procrastination, overconfidence, or systematically underestimate the time to complete tasks (Buehler et al. 2002). These behavioral biases may explain why the farsightedness of Filipino adults does not translate into sound long-term decisions-making and why they are more challenged in providing for old age expenses than survey participants in other countries. Recent research has shown that conveying financial messages through innovative ways such as using popular TV soap operas, films, videos or radio programs can be quite effective, not only in improving knowledge but also in altering behavior (Berg and Zia 2013). Edutainment programs are also presumed to be more effective if messages are delivered in an engaging and entertaining manner through appealing stories that stick to memories, and if they are repeated and reinforced over time. For instance, in Kenya, a soap opera with more than six million viewers, 'Makutano Junction', incorporated financial education messages into some of its stories. These messages aim to encourage people to save regularly or to open a bank account, rather than to keep money under a mattress. Other examples of the use of entertainment education for finance are 'Scandal!' in South Africa or 'Mucho Corazon' in Mexico. As with other soap operas, people watch these edutainment dramas because they identify with the characters and enjoy the stories; but in the course of watching the shows, they benefit from the financial capability enhancing messages and ultimately change their behaviors. At the same time some research findings indicate a possible short-lived impact of these interventions (Di Maro et al. 2014). Further review and analysis of experience and exploring options for testing such methods in the Philippines in partnership with private sector and NGOs could help establish information basis for determining the role such methods could play in the broader financial education efforts.

In addition to TV and radio programs, possible channels to specifically reach out to young adults include youth development associations; mobile applications, as well as social media websites which are popular with the youth. For instance, in Malaysia, the Credit Counseling and Debt Management Agency (AKPK) undertakes an initiative known as 'POWER!', which is targeted at young adults and first-time borrowers

⁴ Online available at: http://www.oecd.org/finance/financial-education/OECD_INFE_High_Level_Principles_National_Strategies_Financial_Education_APEC.pdf

and which aims to equip them with practical money and debt management skills, which will help them to become more financially responsible adults.⁵ AKPK also provides briefings, docu-dramas, e-newsletters, a handbook, classroom exercises, and has also created a social media website. In view of the fact that according to this survey around 85 percent of young adults use mobile phones on a regular basis, mobile applications could be another promising outreach channel. A good example of a mobile app is the mobile budget app (Mobile Financial Assistant – maFin) which has been developed for young adults by the polish Financial Supervision Authority. This mobile app is designed to help monitor and analyze personal spending and to facilitate budget planning and which is available free of charge to users of mobile phones and other mobile devices.

Scaling up integration of financial capability programs into existing conditional cash transfer initiatives (CCTs) in the Philippines can help improve long-term financial decisions of vulnerable segments of the population. Around the world CCTs have been shown to affect people’s investments in health and education (see Benhassine et al. 2014). CCTs may also provide an opportunity to take advantage of so called teachable moments which are moments in people’s lives when they are more receptive to receiving information and are consequently more likely to acquire and retain knowledge. The Pantawid Pamilya program in the Philippines with four million beneficiaries may provide a good opportunity for enhancing the ability of beneficiaries and their families to manage their daily finances and to make provisions for old age expenses. BSP in collaboration with the Department for Social Welfare have already introduced financial education elements in this ongoing CCT program. The next steps could involve evaluation of the effectiveness of these efforts in particular in terms of the suitability of learning materials and consistency of delivery.

Over the medium to long-term it is recommended to scale up and mainstream initiatives for school-based financial education programs as the survey results suggest that starting early can have large payoffs. If people form sound habits on how to manage their money from a young age, they are more likely to adhere to them throughout their lives. International evidence on the effectiveness of school-based financial education programs in changing student’s behaviors is mixed. Nevertheless, there are lessons learned from other countries which have implemented such programs. For example, the rigorous evaluation of a large scale school-based financial education program in Brazil showed that such programs are particularly effective when financial education is provided in ways which students find relevant to their lives either currently or in the near future, and if it is interactive (Bruhn et al. 2014). High-quality material or textbooks are therefore required, and teachers need to be well-trained on the content and

⁵ <http://www.akpk.org.my/services/financial-education/power>

techniques. There are a number of websites containing links to teaching resources.⁶ The BSP collaborated with the Department of Education in the development and integration of lessons on financial education in the elementary curriculum.⁷ BSP in partnership with Department of Education may wish to explore a possibility of the development of a curriculum that integrates financial education as one of the core subjects. This would not only ensure that financial education is actually taught, but it will also provide sufficient time for its teaching.

Moreover, it is suggested to go beyond financial capability enhancing programs and evaluate possibilities of the use of nudges and reminders, default options, as well as smart product design. Studies in Bolivia, Peru, and the Philippines show that simple, timely text messages reminding people to save can boost savings rates in line with earlier established goals (Karlan et al. 2010). Since Filipino adults struggle with long-term financial decision making, periodic reminder messages could induce them to attend to the benefits and tasks of saving regularly and putting money aside for old expenses. Another experimental study from the Philippines shows that commitment devices can have a strong and positive effect on people's financial behavior. Specifically, the study shows that individuals who had been offered and used savings accounts without the option of withdrawal for six months, increased their savings by 82 percent more than a control group that was not provided with such an account.

⁶ These include the Australian Securities and Investments Commission (ASIC) MoneySmart Teaching website (which lists a range of educational materials, each of which has been vetted by a quality assurance process); the US Jump\$tart Coalition Clearinghouse and the UK Personal Finance Education Group (PFEG) website. Some resources are available free of charge and others are available for purchase. The Citigroup Financial Education Curriculum contains interactive lessons, facilitator tips and printable lesson plans (which are available in several languages) for use from kindergarten level upwards.

⁷ In May 2013, the Child and Youth Finance International (CYFI), presented the Country Award to the Philippines for having the Most Outstanding National Child and Youth Finance Program. The award was for the collaboration of BSP and Department of Education to implement a financial education program for school children.

Financial Consumer Protection

A substantial proportion – almost one fifth – of the surveyed adult population reports a dispute with a financial service provider in the past three years. The incidence rate of reported disputes with providers of financial services is much higher in the Philippines than in the few countries for which a comparable indicator is available. Three quarters of those who experienced a dispute with a financial service provider did not pursue any actions to resolve it. The survey results suggest that low income segments and retirees are more vulnerable than the rest of the population to having faced a dispute with a financial service provider. High incidence of disputes could also be in part attributed to low levels of financial literacy and lack of understanding of financial products by population.

In terms of actions taken in the event of a dispute few consider formal mechanisms, including those operated by BSP. Most of those who experienced a conflict and took any actions to resolve it, decided to approach the financial service provider through friends and family (50 percent), followed by a significant proportion that simply stopped using their services before contract expiration (44 percent). Only four percent of consumers actually used formal external systems of redress for settling financial disputes they encountered. Major reasons for not trying to solve a dispute include perceived lengthy time of proceedings, the view that financial providers are simply too powerful, as well as lack of trust in the efficiency and lack of awareness of the respective government authorities.

The survey results suggest that despite serving more customers, banks appear to be less likely to cater the needs of their clients as compared to six other types of financial services providers. Specifically, while three quarters of MFI's customers indicated to be satisfied with the product and services they provide, this number compares to only 43 percent among bank clients. A closer look into satisfaction rates among different user segments reveals that men and rural dwellers are compared to their respective counterpart groups not only less likely to participate in the formal financial sector but also less likely to benefit from it if they do.

Recommendations

These findings emphasize the need to complement financial capability enhancing efforts by measures to strengthen the existing financial consumer protection framework, including minimum requirements to meet internal complaints handling

standards set by BSP. In line with the recommendations of the 2014 Philippines Diagnostic Review of Consumer Protection and Financial Literacy⁸, legal or regulatory provisions should require financial institutions regulated by BSP to provide customers with information on internal complaints handling procedures (including contact information and time limits). This information should not only be disclosed in their products' terms and conditions but also be visibly posted in branches and online. In addition, customers should be informed about formal redress systems such as BSP's Financial Consumer Protection Department (FCPD) or legal courts to increase low awareness levels of government agencies which can be approached for help in the event of a dispute with a financial service provider.

It is further recommended that BSP considers making its external complaint resolution scheme more effective, including for example by enhancing FCPD's power to make binding decisions and through awareness campaigns to inform the public about FCPD's role. In light of the fact that around 60 percent of those who reportedly experienced a conflict but did not try to solve it because they think the government agencies do not function properly, it appears to be critical to make formal redress systems more relevant for those clients who experienced a conflict with a financial service provider. Specifically, FCPD may be more effective if given powers for binding decisions. Such reform would require legislative changes and may not be feasible in a short term. Since around 40 percent of those who did not take any actions in the event of a dispute indicated that they lack awareness of the respective government authority, FCPD needs to re-assess its approach to conducting public awareness campaign to inform consumers of their rights and mechanisms for conflict resolution.

Given the high rate of reported conflicts with financial institutions, BSP should analyze consumer complaints statistics submitted by banks and other financial service providers and use this information as inputs to their supervisory and regulatory activities. All financial institutions and banks in particular, should be obliged to share their complaints data with BSP. Based on the analysis of the consumer complaints and inquiries, BSP could propose guidelines, instructions or conduct public awareness campaigns that address the main problems identified in such analysis. For instance, BSP may issue case studies based on real complaints that would explain in plain language particular complaints, how they were dealt with and why. Such case studies might be published on BSP's website, in local newspapers and/or disseminated through different alternative channels including local government structures and

⁸ Online available at: <http://responsiblefinance.worldbank.org/~media/GIAWB/FL/Documents/Diagnostic-Reviews/Philippines-CP-DiagReview-Banking-Volume-I-FINAL.pdf>

communities. In addition, making complaints statistics available to the public could serve as an effective tool to in promoting consumer protection through 'naming and shaming'.

Mystery shopping and focus group discussions with consumers are powerful supervisory tools to be used to gain additional insights into why banks and their products appear to satisfy their clientele less than other type of providers. Mystery shopping can be a very powerful tool to test bank's compliance with specific requirements, and to determine the quality and quantity of information consumers receive or if suitable advice is given. However, to realize the benefits of this supervisory tool, mystery shopping needs to be well structured, the shoppers need to ask the same questions at each provider based on a simple and plausible scenario, and it needs to cover a reasonable sample of providers. Focus group discussions with consumers of bank services are another effective research technique which helps to delineate attitudes, motivations, and opinions of the participants regarding the most important issues and concerns they have with bank services and products.

Background on the Philippines Survey

The financial capability questionnaire used for this survey has been extensively tested in the context of middle- and low- income countries. The survey instrument used is based on a questionnaire developed with support by the Russia Financial Literacy and Education Trust Fund and is tailored to measure financial capability in low- and middle-income countries, although it can also be used in high-income countries. Extensive qualitative research techniques were used to develop this survey instrument, including about 70 focus groups and more than 200 cognitive interviews in eight countries to identify the concepts that are relevant in middle- and low- income settings, and to test and adapt the questions to ensure that they are well understood and meaningful across income and education levels. The instrument is currently used or planned to be used in 14 countries in Latin America, Africa, Middle East and East Asia and the Pacific.

The survey instrument used allows financial capability, financial inclusion, and consumer protection issues to be assessed and measured. Financial capability is measured by knowledge of financial concepts and products, and by attitudes, skills and behavior related to day-to-day money management, planning for the future, choosing financial products and staying informed. In order to jointly analyze financial capability and inclusion, the survey instrument captures information on usage of different kind of financial products and providers. The financial consumer protection section gathers information on incidence of conflicts with financial service providers and levels of satisfaction with financial products offered by different financial institutions. To further customize the survey instrument to the policy priorities of BSP, specific questions have been added to the survey, for example relating to the usage of E-money.

The Philippines survey is representative of the financially active population of the covered regions and comprises a total sample of 3,000 adults. To fulfill the requirement of a scientifically sound survey which allows inferences to the whole universe of financially active adults in the Philippines, probability sampling techniques were used to select a sample of 3,000 adults. With a theoretical nonresponse rate of 25%, the target sample was set at 4,000 households. The most recent 2010 Philippines Census of Population and Housing, kindly provided by the Philippines Statistics Authority (PSA), were used as a sampling frame. In order to prepare the sample frame adequately, some barangays needed to be excluded due to Peace and Order Problems while others had to be excluded because they were the hardest hit by Typhoon Haiyan.⁹ Once the population

⁹ Barangays in which more than 40 percent of families were seriously impacted by the typhoon were excluded from the sampling frame. In total, around 16 percent of the targeted population had to be excluded from the national frame.

size was finalized, the population was divided into strata based on urban/rural criteria. Urban areas of the country were reorganized into the National Capital Region and all other urban locations. Rural areas were regrouped by dominant economic activity of the regions: agriculture, industry or services. Moreover, a housing score was also created per household and then per barangay, corresponding to the average responses to certain housing questions in the 2010 Census.¹⁰ Each barangay was then characterized as belonging to one of the four categories of housing. Finally, both urban and rural barangays were distributed according to the housing score developed, resulting in a total of 20 strata, 8 of which were urban and 12 of which were rural.

The sample was selected through a three stage cluster sampling. The sample was subsequently selected in a three-stage cluster sampling with probability proportional to size (PPS) selection at the first stage, and with barangays being used as the primary sampling unit (PSU). In total 200 PSUs were selected with PPS and the measure of size for each barangay was based on its number of households. Following the first stage selection of barangays, a household listing was conducted in the chosen barangays. In each selected barangay, a sample of 20 households was selected from this list at the second stage, out of which 15 were targeted for surveying and 5 were reserve households for replacement purpose only. Finally, within each selected household, eligible adults either responsible for personal or household finances were randomly drawn by means of the Kish grid. Proper individual weights were calculated and used in the following analysis to adjust for varying probabilities of selection (design weights).

Between February and September 2014, a Canadian survey firm implemented the survey using computer-assisted personal interview methods (CAPI). Étude Économique Conseil (EEC) Canada, a Montreal based survey firm, was hired to conduct the Financial Capability Survey in the Philippines. To ensure highest data quality and avoid common errors associated with paper-and-pencil surveys, an electronic version of the questionnaire including consistency were programmed and the survey was administered from tablet computers. Due to extensive efforts and different strategies used (e.g. training of enumerators on refusal conversion strategies, letters which were in advance to inform respondents about the surveys' objectives, 5 contact attempts, etc.) the total non-response rate was around 12 percent of the total targeted households.

The adult population to which the results of this survey are meant to extrapolate has the following key characteristics which are in line with figures reported in the 2010 Population Census data: Half of the population lives in urban areas, while the remaining 50 percent live in rural environments (see Figure 20 in Appendix A). Slightly

¹⁰ The highest scores reflected barangays that were composed mostly of homeowners, with houses made of concrete/brick/stone walls that did not need repairs, and had roofs made of either iron/aluminum or tile concrete/clay tile. As the housing score decreases, so does the overall average quality of housing.

less than half of the population are male (48 percent, see Figure 22 in Appendix A). Ranking all individuals by their reported household income and dividing them into 4 groups, 22 percent of the population fall in the lowest income segment (less than 8200 PHP per month), 24 percent in the second lowest (between 8201 PHP and 14200 PHP), 25 percent in the second highest (between 14201 PHP and 23600 PHP), and 29 percent in the highest income bracket (more than 23600 PHP, see Figure 21 in Appendix A). Forty-six percent of the population is younger than 35, 39 percent ages from 35 to 55, and 15 percent of the population is older than 55 (see Figure 23 in Appendix A). As compared to many other countries, adult Filipinos have relatively high educational attainments. Twenty nine percent of the population has some or completed tertiary education including college-, master-, and doctorate degrees; 43 percent has some or completed high school or vocational school education; 25 percent has some or completed primary schooling, while only 2 percent of the population has no schooling (see Figure 24 in Appendix A). Less than half of the population is characterized as earning stable income (48 percent), while 52 percent is facing irregular and uncertain income flows (see Figure 25 in Appendix A). The average number of adults per household is 3, whereas an average sized household comprises 5 people. As shown in Figure 26 in Appendix A, 52 percent of the respondents live in households with 4 to 6 members, 24 percent in households comprising 7 or more members.

1. Financial Inclusion

1.1 Introduction

Expanding the breadth and depth of financial inclusion is a policy priority in the Philippines. The Philippines launched a National Strategy for Microfinance in 1997 to broaden access to basic financial services for low income populations. Over the years Philippines supported innovation in financial services to expand access through proportionate KYC requirements, mobile banking, flexibility in branch regulations and a broad range of policies to expand access to financial services for unserved and underserved segments of the economy. In 2011 Bangko Sentral ng Pilipinas (BSP, the central bank) joined many other countries and made a pledge to expand financial inclusion under the Maya Declaration. The commitment reflected BSP's leadership and coordination role with respect to financial inclusion in the Philippines, as well as the institution's priority goals, which include: i) a wide range of financial services that serve different market segments, ii) financial products that are appropriately designed, priced and tailor-fitted to market needs; iii) a wide variety of strong, sound, and duly authorized financial institutions utilizing innovative delivery channels; and iv) an effective interface of bank and non-bank products, delivery channels, technology and innovation to reach the financially excluded. These goals are mirrored in the Philippines Development Plan (PDP) 2011-2016, which envisions an inclusive financial sector that "provides for the evolving needs of its diverse public."

The Philippines has made positive progress towards achieving its financial inclusion priorities in recent years. BSP has established a dedicated office for Inclusive Finance Advocacy as well as a cross-bank group to coordinate financial inclusion initiatives (The Inclusive Finance Steering Committee). Several reforms and initiatives have significantly contributed towards meeting BSP's priority goals. They include i) the establishment of microdeposit accounts, which have removed barriers such as high-balance requirements and dormancy charges; ii), a flexible regulatory approach for mobile financial services, which has facilitated a range of bank-led and telco-led products, and; (iii) approval of a general consumer protection framework to safeguard consumers of financial services from abusive practices. The Philippines was recognized by the Economic Intelligence Unit's 2014 MicroScope report as having the third best enabling environment for financial inclusion worldwide, behind only Peru and Colombia.

BSP recognizes that measuring progress is a critical component of advancing financial inclusion in the Philippines. Though an explicit numeric target for financial inclusion has not been set, BSP has demonstrated its commitment to measuring

progress. IFAS of BSP have launched a number of initiatives in coordination with other stakeholders including (i) the creation of a financial inclusion database; (ii) regular updates on the state of financial inclusion; (iii) preparatory work for a national baseline survey and product catalogues.

The analysis of the financial inclusion module serves to strengthen the understanding of the state of financial inclusion in the Philippines and provide valuable context for interpreting the results on financial capabilities. Collecting survey data from individuals – that is, from the demand side - can provide valuable insight into the usage, value and limitations of existing financial services. Demand-side survey data also facilitates analysis of how patterns of financial inclusion vary across different population segments, and the degree to which different financial behaviors – such as saving, borrowing, and making payments – overlap. The data and analysis presented below can be used to identify priority populations, set national financial inclusion targets, and design reforms and interventions to advance financial inclusion in the Philippines. Finally, the data can provide a baseline survey against which to measure progress of reforms and initiatives. Future rounds of surveys will shed light on the degree to which the financial inclusion landscape is shifting in the Philippines, and to what extent progress is evenly distributed across different population segments and regions.

1.2 Headline measures of financial inclusion

According to this 2014 Financial Capability Survey, approximately 42 percent of the surveyed adults in the Philippines report owning an account at a formal financial institution, a commonly used metric for international comparison. As compared to other lower-middle income economies (World Bank classification), the Philippines has a relatively high level of financial inclusion, although it does lag behind the average level among East Asian and Pacific economies. This pattern is generally in line with the other financial sector indicators for the Philippines as compared to its country peers (Table 1).¹¹

¹¹ According to the 2011 Global Findex survey in the Philippines, 27 percent of adults have a formal account. The difference between the values likely reflects several factors: (i) the fact that some barangays needed to be excluded from the WBG Financial Capability Survey due to Peace and Order Problems while others had to be excluded because they were the hardest hit by Typhoon Haiyan, (ii) a three-year period during which public and private-sector actions have focused on expanding financial inclusion, for example according to supply-side data from BSP, registered e-money accounts increased 34% between 2010 and 2013; (iii) differences in methodologies between the surveys, for example the 2014 Financial Capabilities survey is based on interviews with adults 18 years and older while the Findex includes adults ages 15 and above. When comparing statistics within or across surveys, it is also important to consider margins of error. For example, the 27 percent value in the Findex survey is associated with a margin of error (95%) of +/- 2.6 percentage points, and the 42 percent value in the 2014 Financial Capabilities survey is associated with a margin of error (95%) of +/- 3.3 percentage points.

Table 1. Measures of Financial Inclusion and Development across Economies

	Financial account ownership (% of adults)	Commercial bank branches (per 100,000 adults)	Firms using banks to finance investment (% of firms)	Domestic credit provided by financial sector (% of GDP)	GDP per capita (constant 2005 US\$)
Philippines	42 (FinCap 2013) 27 (Findex 2011)	8.6	33.2 (2009)	51.9	1,581
Malaysia	66	11.3	60.4 (2007)	142.9	6,990
Indonesia	20	10.4	18.2 (2009)	45.6	1,810
Vietnam	21	3.7	49.9 (2009)	108.2	1,029
China	64	7.9	25 (2012)	163.0	3,583
Lower-middle income	28	-	-	66.0	1,260
EAP (developing)	55	-	35	149.7	3,036

Source: Data on formal account ownership is drawn from 2013 Financial Capabilities Survey (Philippines) and 2011 Global Findex (other economies); data on commercial bank branch penetration is drawn from the IMF FAS database (2013); data on firm finance is drawn from Enterprise Survey data (latest available year by country); data on domestic credit to GDP and GDP per capita are drawn from the World Development Indicators (2013).

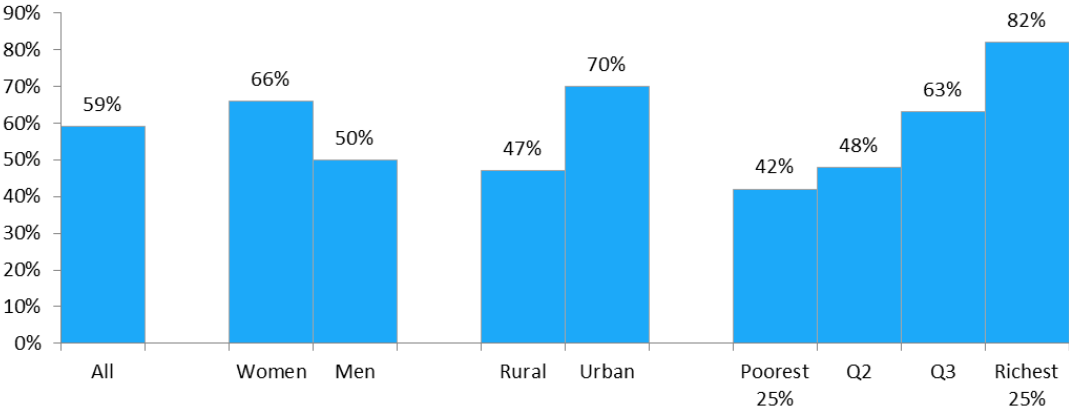
Yet when the definition of financial inclusion is expanded to include a more complete range of financial products, participation in financial sector in the Philippines is broader. Currently, approximately 59 percent of Filipinos reportedly use some type of formal or commercial financial product, including mobile financial services, loans, pensions, insurance, and money transfer services. This definition of financial inclusion will be used throughout the rest of this analysis.

Unlike many countries, women in the Philippines are considerably more likely than men to be financially included. Women are sixteen percentage points more likely than men to be financially included, a difference that remains statistically significant even after controlling for income, education, and a range of other individual characteristics. This is consistent with findings from earlier surveys including the 2011 Global Findex which found that women are fifteen percentage points more likely than men to report owning an account at a formal financial institution (34 percent vs. 29 percent). This gender gap is in contrast to the trend found in most countries: according to the 2011 Global Findex survey: 55 percent of men worldwide have an account, compared to 47 percent of women, a gap which grows larger when the sample is restricted to the developing world, and larger still when only those living on less than \$1.25 per day are considered. However, the “reverse gender gap” finding for the Philippines is consistent with other gender-segregated analyses. According to the World Economic Forum’s 2014 Global Gender Gap Report which measures gender equality in health, education, economy, and politics, the Philippines ranks ninth worldwide, above many developed economies.

There are sharp differences across income categories in the use of financial services, a key obstacle to achieving inclusive growth. While 82 percent of those in

the top quartile of the income distribution use a formal financial product, just 42 percent of those in the bottom quartile percent report the same. Without the necessary tools to manage their day-to-day finances and make important educational and entrepreneurial investments, the poor are limited in their ability to improve their economic well-being, which may hinder progress towards achieving inclusive growth. Simple averages also show variation across education and employment categories and these differences are statistically significant even when controlling for a range of other demographic and socioeconomic characteristics in regression analysis¹² (see table 5 in Appendix B).

Figure 1. Financial Inclusion by Gender, Urban/ Rural, and Income



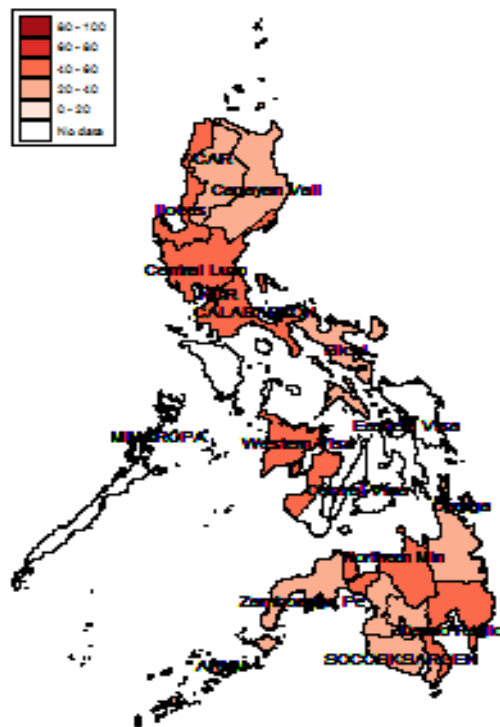
Source: WB Financial Capability Survey, Philippines 2014

There is significant variation in financial inclusion across regions and rural/urban lines within the Philippines. Inequality in access to financial services is naturally exacerbated by the archipelago geography of the country, consisting of more than 7,000 islands. While approximately 75 percent of adults living in the National Capital Region (NCR) region report using a formal financial product or service, only about 45 percent of adults in Soccsksargen, Zamboanga, and Cagayan Valley do the same (Map 1).¹³ More generally, Filipinos living in urban areas are significantly more likely to be financially included: 70 percent of these adults report using a formal financial product compared to 47 percent of their rural counterparts.

¹² The multivariate regression model includes the following control variables: age, gender, education, urban/rural, income, household head status, employment, whether saved as a child, and media consumption.

¹³ Due to relatively low population and therefore low sample sizes, it is not possible to present statistically robust financial inclusion estimates for every region.

Map 1. Financial Inclusion by Region



Source: WB Financial Capability Survey, Philippines 2014

1.3 Money Transfer and Mobile Financial Services

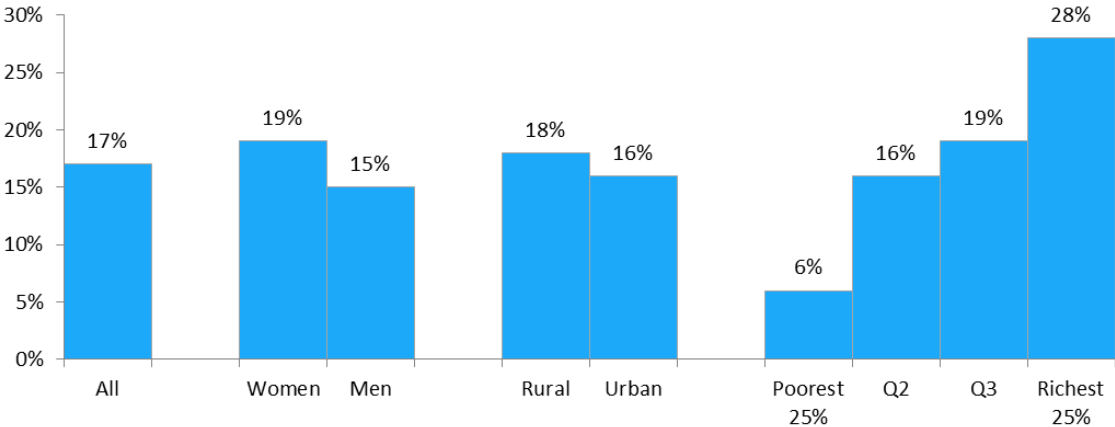
Approximately 23 percent of Filipino adults report that their household has received money or in-kind payments or support from family or friends living elsewhere. Seventeen percent of adults report receiving money from friends of family living elsewhere within the Philippines and 10 percent report receiving money from outside the country. Remittances have long been a crucial component of the Philippines economy. The World Bank estimates that international remittances account for nearly 10 percent of GDP. Ten percent of adults report that money or in-kind payments from family or friends living elsewhere is their main source of income.

Seventeen percent of Filipino adults report using a money transfer service, a category that includes bank linked and stand-alone remittance service providers and mobile-based services. The finding is consistent with results from the 2011 Global Findex survey which showed that 14 percent of adults in the Philippines use a formal financial institution to send money to or receive money from family living elsewhere. Yet, money transfer services are not used equally among different segments of the population: 36 percent of adults in the richest quartile of the income distribution report using money transfer services, but just 5 percent of those in the poorest quartile do. While the poor are equally likely to receive money from family and friends living elsewhere as the rich (21

percent among those in the lowest income quartile vs. 24 percent among those in the highest income quartile), the poor are likely to make more use of informal money transfer mechanism (e.g. bus companies or via relatives) given the high costs of some money transfer services and lack of physical access.

Mobile financial services (MFS) have found relative success in the Philippines with 17 percent of adults reporting current use of an MFS product. This figure is in line with data from the 2011 Global Findex survey which found that 15 percent of adults reported sending or receiving money via a mobile phone. This sets the Philippines apart from many other developing economies, where mobile financial services have struggled to take off.

Figure 2. Use of Mobile Financial Services Urban/ Rural, and Income



Source: WB Financial Capability Survey, Philippines 2014

A key enabler of mobile financial services in the Philippines has been BSP’s willingness to enable non-banks to offer financial services. In 2005, BSP approved a MFS product of GXI, a non-bank, which subsequently registered with BSP as a “remittance agent” and met BSPs requirements for consumer protection, safety and soundness, and AML / CFT issues. This was followed by BSP Circular Number 649, which issued comprehensive guidelines governing the issuance of electronic money and the operations of electronic money issuers. This regulation maintained the ability for non-banks to issue electronic money. A GSMA report notes that in addition to the enabling environment reforms, a high adoption of mobile phones and the ability of early entrants (SMART and Globe) to design strong offerings and align the interests of supporting ecosystems, have been important determinants of the success of mobile financial services in the Philippines. Indeed, the GCASH product – launched in 2004 by telco Globe – and SMART money – launched in 2001 by SMART Communications in partnership with Banco de Oro - have been the dominant market players. The survey does not contain data on the usage of product-specific MFS. Other key enablers include widespread

mobile coverage, SMS literacy, latent demand for financial services, prevalence of international remittances, and an existing network of merchants accepting debit/credit payments, according to a GSMA analysis.

The data does suggest that mobile financial services have, to some degree, been successful in reducing traditional barriers to financial inclusion, including physical access. An equal proportion of adults without a traditional account (e.g. in a bank or other non-e-money account) report using mobile financial services as adults with a traditional account. This may be explained by improved physical access associated with mobile financial services. Approximately 11 percent of rural residents report having a traditional account at a formal financial institution as compared to 33 percent of urban residents. Yet rural residents and urban residents report using mobile financial services at rates that are statistically indistinguishable: 18 percent and 16 percent, respectively.

Mobile financial services, like other financial services, are used disproportionately by the wealthy. Approximately 28 percent of adults in the highest income quartile report currently using a mobile financial service, as compared to 6 percent of those in the lowest income quartile. Broadening the scope of mobile financial services to include savings and credit – as M-Shwari and other products have done in Kenya – may improve the value proposition for lower-income adults. While electronic transfer of social benefits is often considered to be an effective method for increasing adoption of e-money services by the poor, recent research has shown that the use of cash card systems in the Philippines – mainly the 4Ps program - does not necessarily lead to great use of digital financial products.

Table 2. Measures of Mobile Financial Service Penetration across Economies

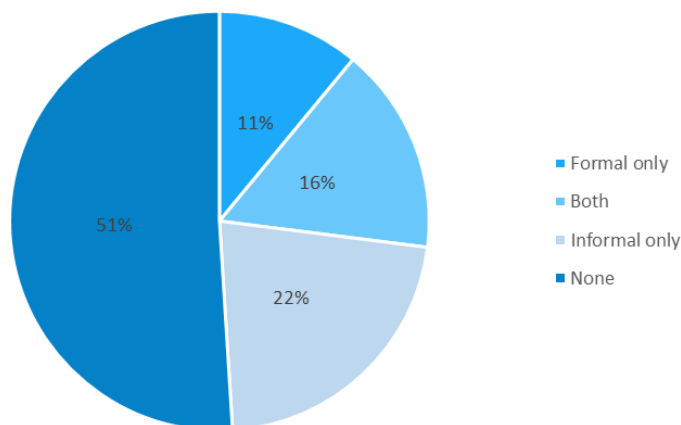
	Use of mobile financial services	Adults living in HH with mobile phone	Formal account ownership (% of adults)	MFS products available (GSMA)
Philippines	17	89	42	2
Malaysia	3	99	66	2
Indonesia	1	84	20	6
Vietnam	7	93	21	1
China	2	97	64	-
Kenya	68	68	42	6
Tanzania	23	63	17	4
All lower-middle income	6	-	28	-
EAP (developing)	2	-	55	-

Source: Data on the use of mobile financial services and formal account ownership is drawn from 2013 Financial Capabilities Survey (Philippines) and 2011 Global Findex (other economies). Data on mobile phone penetration is drawn from the 2013 Gallup World Poll. Data on MFS products available is drawn from the GSMA Mobile Money for the Unbanked Deployment Tracker.

1.4 Credit

Forty-nine percent of Filipinos report some type of borrowing, across a range of formal and informal systems. The prevalence of informal borrowing is considerably higher than the average in other lower-middle income or East Asian economies (31 percent and 28 percent, respectively). Around 11 percent of adults use exclusively formal credit products (bank loan, microfinance loan, credit card, mortgage, etc.) to borrow while and 22 percent of adults meet their borrowing needs relying only on informal source such as a money lender, family member, or friend. Approximately 16 percent of adults blend informal and formal sources of borrowing. Given that 53 percent of “informal only” borrowers report having an account, it appears that the prevalence of informal borrowing is driven both by ineligibility and lack of physical access. Yet the majority of adults – 51 percent – do not report engaging in any borrowing behavior at all. Adults in the poorest quintile are relatively unlikely to borrow, with sixty-six percent of this population segment reporting no borrowing activities at all.

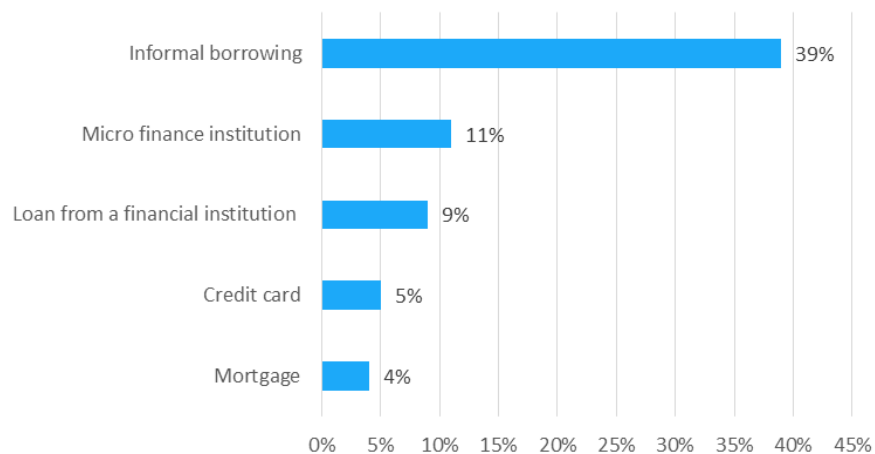
Figure 3. Formal and informal credit



Note: “Formal only” includes adults that report currently using a mortgage product, formal loan from a bank/NSSLA/Cooperative/MFI or credit card, but do not borrow from money lenders or family/friends. “Informal only” includes adults that report borrowing from money lenders or family/friends but do not use a mortgage product, formal loan from a bank/NSSLA/Cooperative/MFI or credit card,

Source: WB Financial Capability Survey, Philippines 2014

Figure 4. Types and sources of borrowing



Source: WB Financial Capability Survey, Philippines 2014

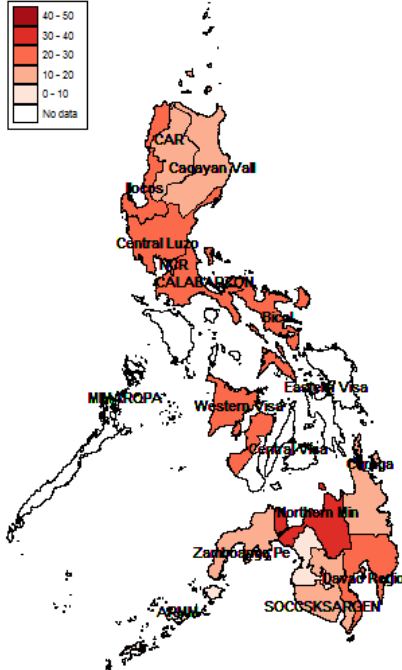
Loans from financial institutions, including microfinance institutions, are the most commonly reported source of formal lending among Filipino adults. Approximately 11 percent of respondents report having a microfinance loan, which translates to approximately 4.8 million adults.¹⁴ These demand-side findings show a larger prevalence of microcredit than is reported in official figures: BSP data shows that the number of microfinance borrowers increased by 191 percent between 2002 and 2012, reaching 1.1 million borrowers. However, official figures do not account for microloans from non-supervised institutions. There are also challenges in measuring specific products from the demand-side as respondents may not be fully aware as to what is considered a microfinance institution. A spatial representation of formal credit usage confirms previous findings that usage of formal financial services is concentrated in populous regions; the map also shows that formal credit on average is less frequently used than informal credit across the Philippines (Map 2, Map 3). Research also highlights that formal credit products for the poor, often disbursed through microfinance institutions, have positive impacts though often through unexpected channels. In a 2011 experiment in the Philippines, researchers found that access to credit led to a decline in the number of business activities and employees in the treatment group relative to controls. However, the results did show that microloans increase the ability of consumers to cope with risk, strengthen community ties, and boost the access to informal credit.¹⁵ Just 5 percent of adults report currently using a credit card. Housing finance remains a relatively

¹⁴ According to the 2010 census, there are 92.34 million people in the Philippines, of which 34 percent are below the age of 15 (according to the World Bank World Development Indicators).

¹⁵ Karlan and Zinam, 2011.

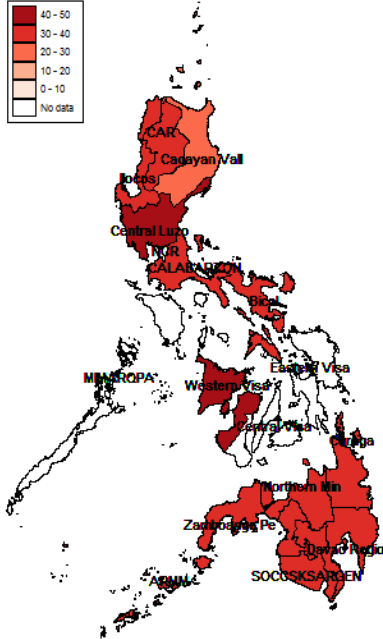
underdeveloped sector in the Philippines with only four percent of adults currently having a mortgage product.

Map 2. Spatial distribution of formal borrowing (% of adults with formal credit)



Source: WB Financial Capability Survey, Philippines 2014

Map 3. Spatial distribution of informal borrowing (% of adults with informal credit)

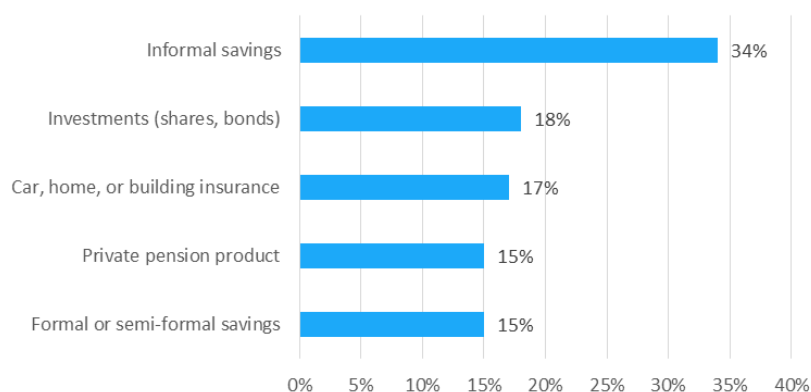


Source: WB Financial Capability Survey, Philippines 2014

1.5 Saving and Risk Management

Fifty-seven percent of Filipinos reported some form of saving or risk management behavior (e.g. insurance). Informal savings (e.g. saving at home) is the most commonly reported behavior, reported by 34 percent of adults. Other activities, such as having investments, private pensions, car or building insurance, or formal / semi-formal saving are each reported by approximately 15 to 20 percent of the adult population. There are significant differences across income categories in the degree to which adults engage in savings or risk management activities. The poor, who arguably are most in need to tools to help protect against income shocks and smooth consumption, are considerably less likely to report savings or risk management activities. Forty-four percent of the poorest 25 percent of adults report some form of saving or risk management behavior, as compared to 76 percent of the richest quartile.

Figure 5. Types and sources of saving and risk management



Source: WB Financial Capability Survey, Philippines 2014

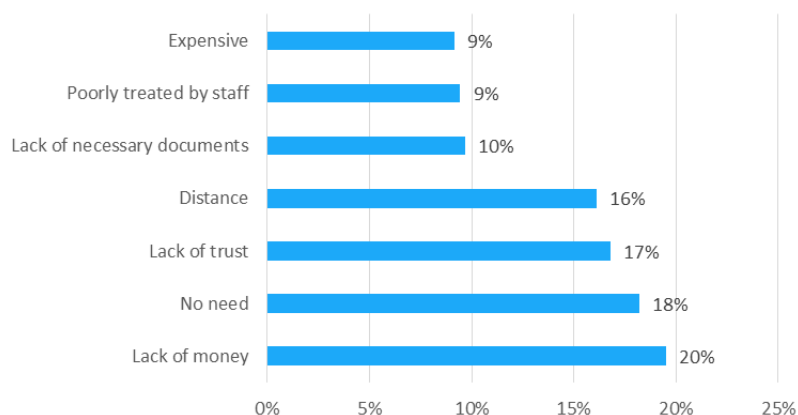
The use of informal financial management and planning techniques is common among Filipino adults. Thirty-four percent of adults report saving at home, which is consistent with 2011 Global Findex results that show Filipinos are considerably more likely than adults in other lower-middle income or East Asian economies to save informally, that is, usually neither formal nor semi-formal (e.g. savings groups) mechanisms. Sixty-two percent of informal savers have an account, which suggests that there is significant scope for financial service providers to mobilize additional savings either through existing customers (those using both) or new customers who are already engaged in regular savings behaviors. Of those with a formal bank, richer adults are in fact more likely than poorer adults to also save informally. Just under half of adults report using neither informal, semi-formal nor formal methods to save. Product design should

also reflect recent research, including experiments conducted in the Philippines that found that accounts with savings reminders can lead to a boost in savings.¹⁶

1.6 The Unbanked and Barriers to Owning a Formal Account

The approximately 39 million adults without an account at a formal financial institution in the Philippines are disproportionately poor, less educated and living in rural areas.¹⁷ Seventy-six percent of the poorest quartile of Filipinos report not currently having an account at a formal financial institution. The same applies for 71 percent of adults living in rural areas. Yet, as stated in the Global Financial Development Report 2014 (World Bank, 2013a), lack of usage of financial products does not necessarily mean lack of access. While some people may have access to financial services at affordable prices and may decide not to use them, others may lack access because of constraints such as excessively high costs, or unavailability of the services due to regulatory barriers or other factors. The Financial Capability Survey asked respondents who do not have a formal account to report why.

Figure 6. Reasons for not having a formal account (% of unbanked Filipinos without an account)



Source: WB Financial Capability Survey, Philippines 2014

The most commonly reported obstacles to formal account ownership are lack of enough money to use one – reported by 20 percent of adults without an account – and lack of need for an account – reported by 18 percent. Perhaps not surprisingly,

¹⁶ Karlan and Zinman, 2010.

¹⁷ Due to the design of the survey, obstacles to financial access are assessed specifically with respect to account ownership and thus this may include adults who do in fact use other formal financial services such as insurance, pensions, or mobile financial services.

respondents who report lacking enough money to use an account are disproportionately poor: 28 percent of unbanked adults in the poorest income quartile report this obstacle, while only 15 percent of those in the richest income quartile do the same. While these answers could suggest voluntary exclusion from the formal financial sector, it does not necessarily imply that these adults are unbankable. Instead, it may reflect a cost-benefit analysis on the part of these adults and demonstrates that many adults perceive banking services to be of little value, not in absolute terms, but for current levels of income and the quality of banking products. This could be because of the nontrivial costs associated with owning a formal account, from explicit costs like minimum balance requirements and withdrawal charges to implicit costs such as transportation costs, but it suggests that, for many adults, formal institutions do not offer sufficiently valuable services for day-to-day transactions or savings, particularly those involving small amounts. The Philippines is not an outlier in this regard: “lack of enough money to use an account” is the most commonly self-reported barrier in 124 of 148 countries, according to 2011 Global Findex data. A significant subset of unbanked adults in the Philippines do, however, explicitly cite the costs associated with a formal account: nine percent of the unbanked report not having an account because they are too expensive (Figure 6). It is notable, however, that this barrier is ranked 7th, perhaps due to the microdeposit accounts that have successfully lowered costs related to dormancy and minimum requirements.

A lack of trust in financial institutions is a significant obstacle for greater financial inclusion in the Philippines. Seventeen percent of unbanked adults report that they do not have an account due to a lack of trust. A lack of trust is positively associated with income: 14 percent of adults without an account in the lowest income quartile report this reason, as compared to 21 percent of unbanked adults in the highest income quartile. Unbanked adults with a tertiary education are also more likely than lesser-education Filipinos to report trust as a barrier. This finding is also linked to another reported obstacle: nine percent of Filipinos without an account report that they are deterred due to poor treatment by bank staff. Variations across income and education level are not significant for this variable.

Other commonly cited barriers – such as distance and documentation – can be directly addressed by public policy. Sixteen percent of unbanked Filipinos are deterred from opening an account due to a lack of physical access. This is of course challenging in a country with over 2,000 inhabited islands. However, with 8.6 access points per 100,000 adults, the Philippines lags behind other economies in the reach of the financial sector, including Indonesia and Malaysia, countries that face similarly challenging geographic obstacles. Many of the existing financial access points in the Philippines are concentrated in urban centers. According to BSP, 604 of 1,634 cities and municipalities do not host a single banking office – though this does represent a decline from 611 in 2012.

2. Financial Capability

Financial Capability is the internal capacity to act in one's best financial interest, given socioeconomic environmental conditions. It therefore encompasses the knowledge, attitudes, skills, and behaviors of consumers with regard to managing their resources and understanding, selecting, and make use of financial services that fit their needs.

2.1 Knowledge of Financial Concepts

There is substantial evidence that lack of financial knowledge and skills contributed to the recent global financial crisis. It is a well-accepted hypothesis that limitations in consumers' ability to fully understand the financial products and risks they had taken on, contributed significantly to the worst financial crises since the great depression (Geradi et al. 2010; Klapper et al. 2012).

Financial knowledge and skills are even more important in an environment where financial products are increasingly complex and being delivered through new distributions channels. Thanks to the launch of mobile banking services such as GCASH and SMART money financial products and services are becoming increasingly available to formerly disconnected segments. While these developments provide benefits, they also bear risks which may be unfamiliar to existing and new customers. To be able to benefit from these new opportunities without being exposed to undue risks, a certain level of financial knowledge and skills is required.

In line with global trends, policy makers in the Philippines recognize the importance of financial knowledge and skills (financial literacy) for peoples' ability to take informed financial decisions and to benefit from the financial services they use. Financial supervisors in 81 economies are currently involved in financial capability enhancing activities according to the WB's 2013 Global Survey on Consumer Protection and Financial Literacy which interviewed regulators involved in financial consumer protection in 114 jurisdictions from all regions. Financial capability and education is an important priority for BSP as it helps to empower people to become effective partners of the BSP as productive economic agents and improves people's lives. To this end, as part of the 'Maya Declaration 2011', BSP has committed to promote financial capability and to ensure that consumers are adequately informed and able to enjoy the full benefits of their financial access. Since 2012, BSP has implemented the BSP economic and Financial Learning Program across the country with the aim to promote greater public awareness

and understanding of key economic and financial issues. This chapter focuses on gaps in financial knowledge that need policy attention as well as vulnerable groups that display limited knowledge and understanding of financial concepts and need to be targeted with tailored programs.

To evaluate respondent's financial knowledge and their basic numeracy skills, 7 questions were added to the 2014 Philippines Financial Capability Survey, covering basic calculus and financial concepts such as simple interest rates, inflation, compound interest, risk diversification, and the main purpose of insurance products. These questions have been asked because they capture financial concepts and skills which are widely considered as being crucial for informed savings and borrowing decisions as well as for being able to mitigate risks more effectively and or to take advantage of investment opportunities. We construct a financial literacy index based on the number of correct responses provided by each survey participant to the seven financial literacy questions. This index ranges from 0 to 7, whereby 0 indicates respondents who struggle the most with correctly answering any of these questions. A score of 7 indicates survey participants with good understanding of fundamental financial concepts and the ability to perform simple mathematical calculations.

Box 1. Financial Literacy Quiz

Question 1 Imagine that five brothers are given a gift of 1,000 PHP. If the brothers have to divide the money equally, how much does each one get?

Question 2 Now, imagine that the five brothers have to wait for one year to get their part of the 1,000PHP and inflation stays at 10%. In one year's time will they be able to buy:

- More with their share of money than they could today
- The same amount
- Less than they could buy today
- It depends on the types of things that they want to buy (do not read out this option)

Question 3 Suppose you put 100 PHP into a savings account with a guaranteed interest rate of 2% per year. You don't make any further payments into this account and you don't withdraw any money. How much would be in the account at the end of the first year, once the interest payment is made?

Question 4 How much would be in the account at the end of five years? Would it be:

- More than 110 PHP
- Exactly 110 PHP
- Less than 110 PHP

- It is impossible to tell from the information given

Question 5 Let's assume that you saw a TV-set of the same model on sales in two different shops. The initial retail price of it was 1,000 PHP. One shop offered a discount of 150 PHP, while the other one offered a 10% discount. Which one is a better bargain, a discount of 1,50 PHP or 10%?

- A discount of 150 PHP
- They are the same
- A 10% discount

Question 6 Which of the following statements best describes the primary purpose of insurance products?

- To accumulate savings
- To protect against risks
- To make payments or send money
- Other

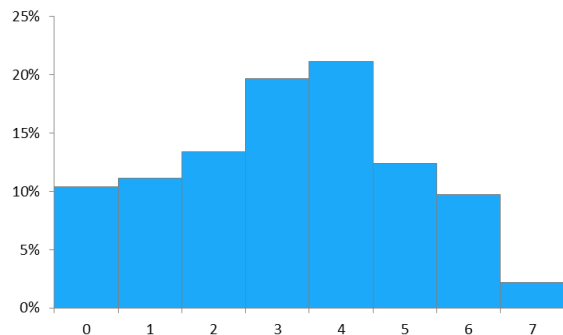
Question 7 Suppose you have money to invest. Is it safer to buy stocks of just one company or to buy stocks of many companies?

- Buy stocks of one company
- Buy stocks of many companies

Source: WB Financial Capability Survey, Philippines 2014

The survey results suggest that on average, Filipino adults were able to answer 3.2 out of 7 financial literacy-related questions correctly. Although, the majority of the population was able to answer between 2 to 5 questions correctly, only a meager proportion of the sample population (10 percent) answered 6 questions correctly and hardly anybody - 2 percent of the respondents - managed to provide correct responses to all 7 questions. A more worrisome finding is that around a fifth of the surveyed population did not answer more than 1 question correctly, while still a significant proportion of respondents, one out of ten adult Filipinos, did not appear to have a sound grasp of any of the basic concepts being tested.

Figure 7. Financial Literacy Overview

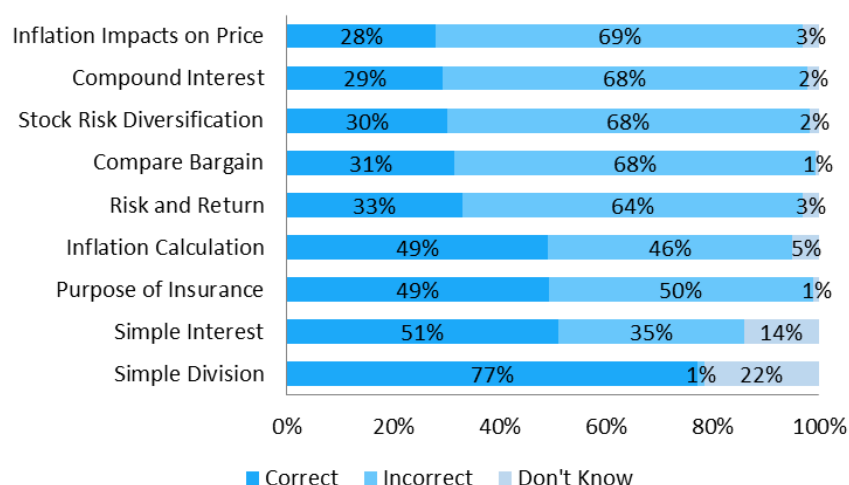


Source: WB Financial Capability Survey, Philippines 2014

A deeper exploration into the type of basic financial concepts known reveals that Filipino adults are most comfortable with performing simple divisions but lack specific knowledge required to make informed savings and borrowing decisions. One of the most notable knowledge gaps which deserve policy attention is that only around a third of the adult population appear to be comfortable in solving simple numeracy tasks needed to shop around and to identify simpler bargains. A similar proportion of the sample has a good grasp of the concept of risk diversification and understands that holding stocks from different companies can usually be associated with less risky returns than holding stocks from a single company. The working of compound interest appears to be the most difficult to understand and only 29 percent of the sample managed to answer the respective question correctly.

The fundamental misunderstanding of the concept of compound interest can have far-reaching consequences in particular for long-term savings and the buildup of wealth as evidence from recent field experiment in China shows. The experiment studied the relationship between the understanding of the nature of compound interest and retirement savings in China using a sample of thousand households. It concludes that households which were randomly assigned to a financial education treatment that emphasized the concept of compound interest increased their pension contribution by roughly 40 percent as compared to a control group which did not receive this training (Changcheng 2012).

Figure 8. Financial Literacy Quiz Overview



Source: WB Financial Capability Survey, Philippines 2014

An international comparison to respondents in 18 countries on key financial literacy measures confirms that financial knowledge and awareness levels are a significant challenge in the Philippines and require immediate policy responses.

Table 3 shows for 19 countries the proportion of adults with good grasp of basic concepts such as inflation, simple and compound interest as well as those who are comfortable with performing simple divisions. As can be seen, respondents in the Philippines perform near the middle of the pack in terms of their understanding of simple and compound interest, while their understanding of the effect inflation has on their savings and their ability to perform simple divisions is lower than in most other countries in the developed and developing world for which comparable indicators are available.

Table 3. Cross-country comparison of different financial literacy scores

Country	Year	Inflation	Simple Interest	Compound Interest	Simple division
Albania	2011	61	40	10	89
Armenia	2010	83	53	18	86
Colombia	2012	69	19	26	86
Czech Rep.	2010	80	60	32	93
Estonia	2010	86	64	31	93
Germany	2010	61	64	47	84
Hungary	2010	78	61	46	96
Ireland	2010	58	76	29	93
Lebanon	2012	69	66	23	88
Malaysia	2010	62	54	30	93

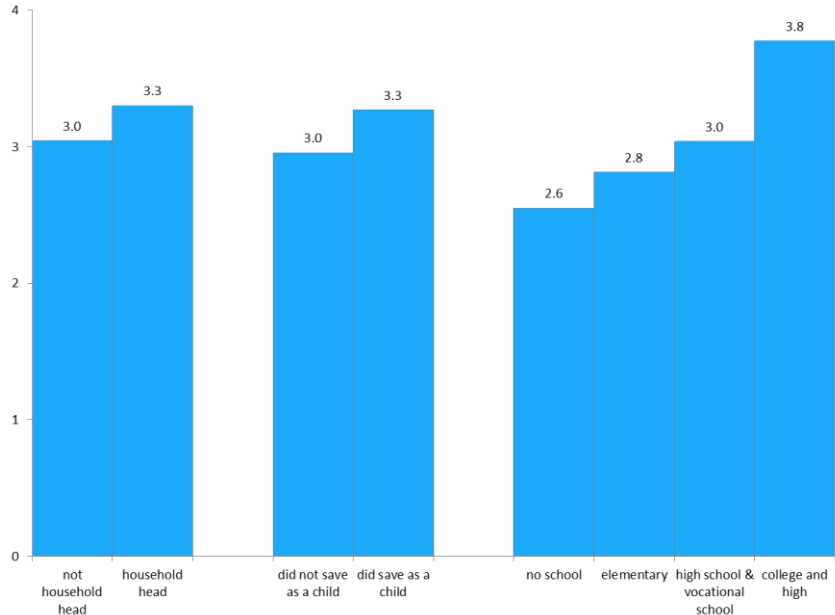
Mexico	2012	55	30	31	80
Mongolia	2012	39	69	58	97
Mozambique	2013	28	78	28	93
Philippines	2014	49	51	29	77
Peru	2010	63	40	14	90
Poland	2010	77	60	27	91
South Africa	2010	49	44	21	79
Turkey	2012	46	28	18	84
Uruguay	2012	82	50	N/A	86

Source: WB Financial Capability Survey, Philippines 2014

Segments of the population that seem to struggle the most to understand basic financial concepts include those adults who did not save as a child, non-household heads, as well as men (see figure 9). Moreover, unlike most other countries where women display lower financial knowledge than men, the gender gap identified in the Philippines is in favor of women: On average, women answered 3.2 questions correctly as compared to men who provided on average 3.1 correct responses to the financial literacy quiz related questions. Although this difference in the average number of correct responses may not look substantial, it masks differences in the distribution of the financial literacy quiz scores men and women achieve. Regression analysis reveals that even after controlling for other demographic and socioeconomic factors men are more likely than women to belong to the group of adults who scored the lowest on the financial literacy quiz (2 or less correct responses) (see table 6 in Appendix B). Delving deeper into the specific concepts women tend to be more knowledgeable about shows that female respondents are four percentage points more likely than men to understand the primary purpose of insurance products as a risk management tool.

In contrast, a better understanding of basic financial concepts is strongly associated with individual characteristics such as completed tertiary education, higher income, and the usage of print, broadcast, and internet media on a regular basis. As may have been expected, those with highest educational attainment and highest incomes provide significantly more correct responses on the financial literacy quiz as compared to their respective counterpart groups with lowest educational attainment and lowest incomes, even after controlling for other factors. Notably, regression analysis reveals significant knowledge gaps between more active media consumers and those who do not use print, broadcast, and internet media on a regular basis (see table 6 in Appendix B). In addition, the survey results suggests that location matters and that those who live in inner city areas achieve significantly higher financial literacy quiz scores as compared to those who live in urban, peri-urban or rural areas.

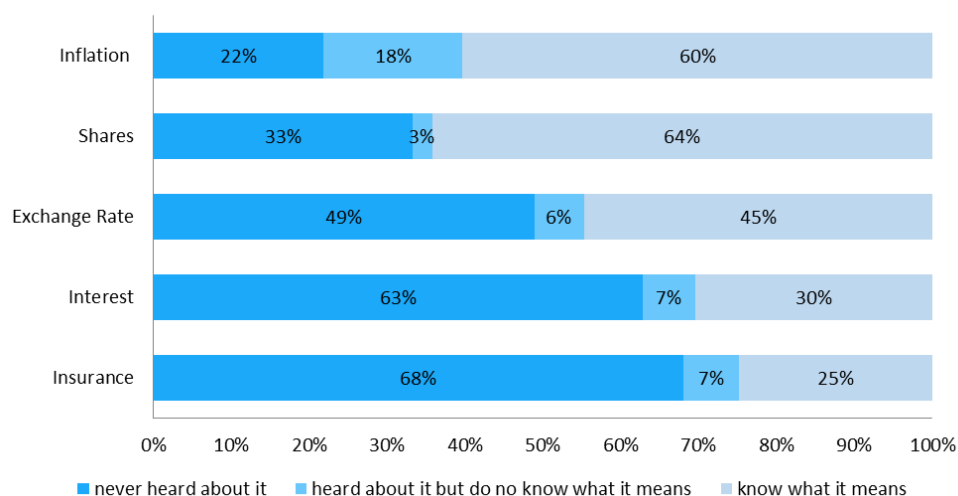
Figure 9. Financial Literacy Average Score by Household Head Status, Saved as a Child



Source: WB Financial Capability Survey, Philippines 2014

Financial knowledge gap identified through the objective financial literacy quiz are largely confirmed through participants’ subjective self-assessment of their levels of awareness and understanding of financial concepts. With the view of comparing objective findings of the financial knowledge quiz with subjective education needs, respondents were also asked to self-assess their understanding of basic terms and concepts such as interest rates, insurance products, exchange rates, and inflation. As shown in figure 10, similar to the findings of the objective financial literacy quiz, awareness of insurance and interest rates is relatively wide-spread. However, only 22 percent of the surveyed population stated that they know what the term inflation means which is much less than the 49 percent of the respondents who answered the inflation quiz question correctly. Looking into the reasons behind this discrepancy the survey results indicate that even among those who answered the inflation quiz question correctly and therefore understand the underlying mechanics of how inflation affects their savings three quarters seem to lack familiarity with the inflation term.

Figure 10. Awareness on Financial Concepts and Products



Source: WB Financial Capability Survey, Philippines 2014

2.2 Financial Behavior and Attitudes

Even if people possess knowledge of basic financial concepts they may struggle to translate it into adequate actions. To identify the role that attitudes play in shaping individuals' financial decisions and to see if and how attitudes translate into financial behavior, the survey contains questions on different aspects (components) of financial capability that include attitudes/motivations and behaviors. This chapter gives an overview of strengths and areas for improvements that surveyed adult Filipinos showed regarding relevant financial behaviors and attitudes.

In the Philippines data set, 10 main components of financial capability can be identified, some of which refer to behaviors, and others to attitudes or motivations. Each financial capability component is measured through a combination of relevant questions. These are identified by using a statistical technique called principal component analysis (PCA). PCA is a data reduction method that finds a small number of linear combinations of those variables that explain most of the variance in the data. The method is used to aggregate the variables that measure different nuances of the same component in order to obtain a single indicator (or score) for that component. Each component score ranges between 0 (lowest score) and 100 (highest score).

The following seven components measure behaviors related to financial capability: budgeting, not overspending, living within means, monitoring expenses, planning for unexpected expenses, making provisions for old age, and choosing products. More specifically, 'budgeting' measures the extent to which people plan how to use their money and whether they adhere to the plan; 'not overspending' assesses whether people

have money left over after buying essentials and if yes, if they refrain from spending it on non-essentials; 'living within means' measures whether adults run short of money after buying essentials and why, their level of borrowing and whether people borrow to buy food or to repay other debt; 'monitoring expenses' measures the ability to track expenses; 'planning for unexpected expenses' indicates whether people could cover an unexpected expense equivalent to a month's income and whether they worry about it; 'planning for old age expenses' indicates whether people have strategies in place that allow them to cover for expenses in old age; and 'choosing products' indicates whether people search for alternatives, check terms and conditions, get information before selecting financial products, and search until they found the best products for their needs. The last score is only calculated for those who have personally chosen a financial product in the past five years.

Three financial capability components refer to underlying attitudes and motivations that influence the way people behave, such as those related to people's farsightedness, their attitude towards savings, and their achievement orientation. In particular, 'farsightedness' measures whether respondents agree or disagree with statements such as 'I live for today', 'The future will take care of itself', 'I only focus on the short term'. The attitude towards savings score on the other hand is based on respondents' agreement or disagreement that statements such as 'I try to save for the future', 'I try to save for emergencies', 'I try to save even if a small amount', and 'I am very disciplined when it comes to managing money', describe them personally. The achievement orientation score assesses whether respondents always look out for opportunities for improving their situation, have many aspirations, and always work hard to be among the best at what they do.

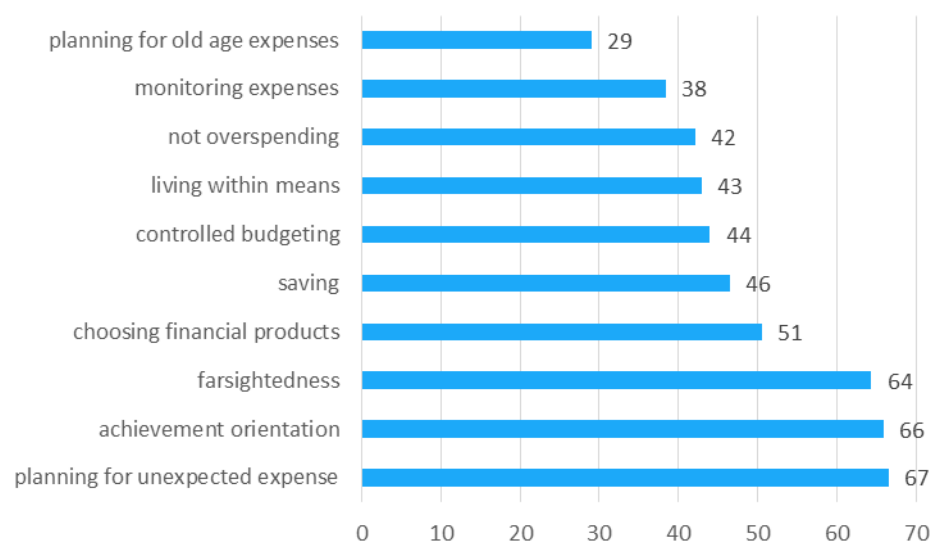
As compared to other aspects of financial capability, Filipino adults show relative strengths in terms of their farsightedness, achievement orientation, as well as their ability to plan for unexpected expenses. According to PCA analysis, Filipino adults are most capable in the area of planning for unexpected expenses where they achieve the highest score (67) of all aspects of financial capability being measured. This high score reflects that fact that around half of the surveyed Filipino adults could reportedly cover an unexpected expense equivalent to one month's income without borrowing. Only 19 percent of them could not cover such expense and have not thought about doing anything to make sure they could cover it. Listing all scores for different aspects of financial capability in increasing order, figure 11 indicates that the second and third highest scores can be found for respondents' achievement orientation (66) and their level of farsightedness (64). Although a significant proportion of adults reported some form of saving (see chapter 1.5), Filipino adults score substantially lower regarding their inclination to save (46), suggesting that average savings amounts may be low. As would

be expected, Filipino adults with lower inclination to save are found to be less likely to hold formal savings.

In contrast, financial behaviors related to day-to-day money management appear to be a major challenge in the Philippines. Figure 11 further shows that Filipino adults struggle with their daily money management, including their ability to budget (44), live within their means (43), refrain from overspending (42), and monitor their expenses (38). More specifically, regarding people's ability to track their expenses, the survey results show that over half of the surveyed respondents either did not know the amount of money they had spent last week or the amount currently available to them. In terms of living within means, the survey results suggest that 20 percent of the survey participants ran short of money due to their overspending. Alarming, 19 percent of those who tend to overspend borrow money regularly in order to cover their food expenses.

By far the lowest score is, however, found for behaviors relating to long-term planning. Despite people's forward-looking attitude and their ability to cope with unexpected income shocks equivalent to one month's income, the lowest overall financial capability score indicates that people's ability to procure for old age expenses is severely constraint. A closer look into the variables based on which this low score has been computed reveals that it reflects the fact that less than a quarter of the surveyed respondents aged 60 and younger do have sufficient provisions in place to cover their expected old age expenses. Moreover, a substantial proportion of those without any provisions are either not worried at all or only a bit worried (64 percent) about their long-term financial security. This low score is of particular concern and deserves policy attention given its implications for people's long-term wellbeing.

Figure 11. Average Financial Capability Scores



Source: WB Financial Capability Survey, Philippines 2014

A comparison to survey participants in eleven countries confirms that Filipino adults tend to be far-sighted, but they are among the most challenged with respect to their daily money management and long-term planning. Table 4 compares the average financial capability scores Filipino adults achieved in eight different areas to the ones of respondents in various countries in which a similar survey has been conducted. As can be seen, survey participants in the Philippines outperform respondents from eight other countries in terms of their inclination to think about the future. However, the cross-country comparison confirms that Filipino respondents display weaker performance in their daily money management and lack far behind survey participants in other countries in their ability to make provisions for their old age expenses.

Table 4. Cross-country comparison of different financial capability scores

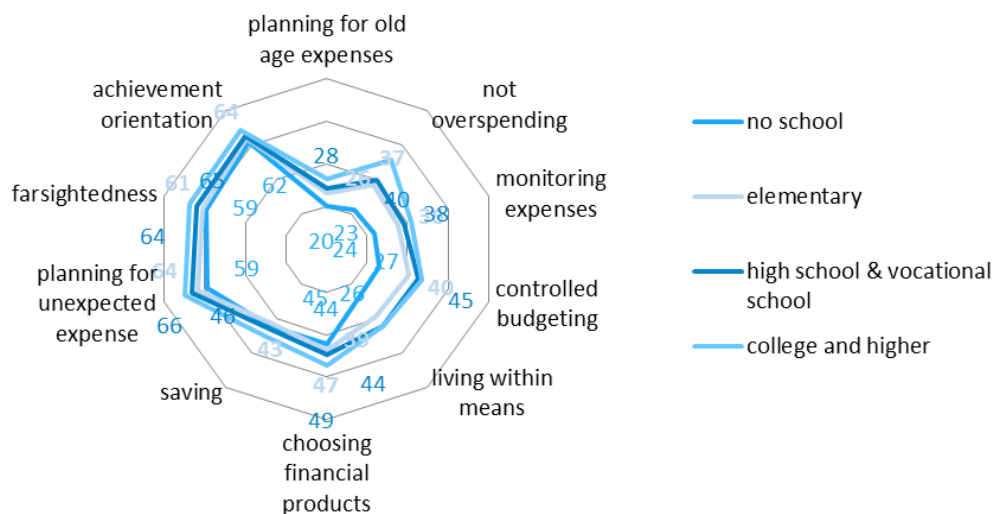
Country	Saving	Far-sightedness	Planning for old age expenses	Choosing financial products
Armenia	46	28	100	59
Colombia	45	37	67	57
Lebanon	40	55	71	63
Mexico	57	35	65	59
Mongolia	62	60	N/A	49
Mozambique	42	40	40	34
Morocco	42	78	6	89
Nigeria	55	N/A	N/A	N/A
Philippines	46	64	29	51
Tajikistan	66	84	N/A	N/A

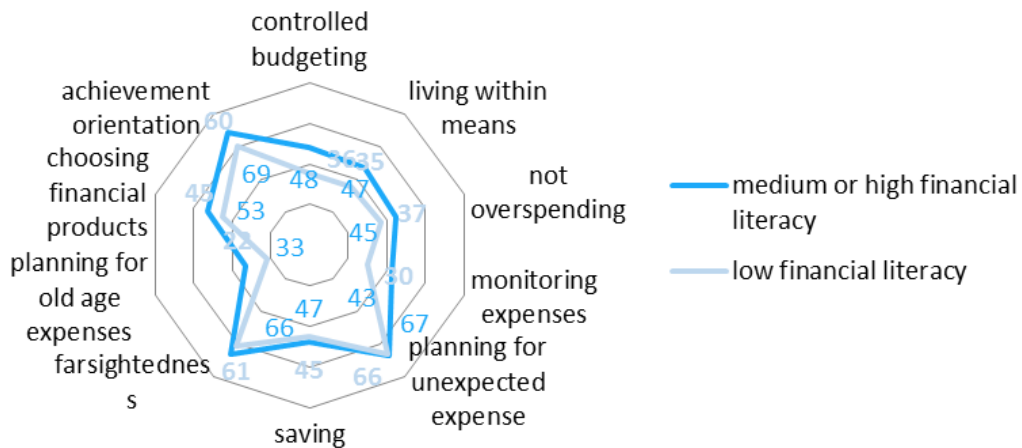
Turkey	30	50	72	52
Uruguay	44	35	60	N/A

Source: WB Financial Capability Survey, Philippines 2014

Two essential personal characteristics which are found to be strongly correlated with better scores in a number of financial capability areas are people’s educational attainments as well as their financial knowledge/literacy levels. Survey participants with higher educational attainment outperform their counterparts with lower education in the areas of choosing financial products, managing their daily finances, and in planning for old age expenses. The most remarkable gap between highly educated Filipinos and those without any educational attainment can be observed in their ability to live within their means. While those with completed tertiary education achieved a living within means score of 51, those with no schooling scored only half as high (23). According to regression analysis (see table 7, table 8 in Appendix B), this difference remains significant even after holding income and other characteristics constant. Likewise, higher financial literacy is strongly associated with higher scores in several areas, in particular in those related to daily money management and planning for retirement age expenses.

Figure 12. Average Financial Capability Scores by education, financial literacy level

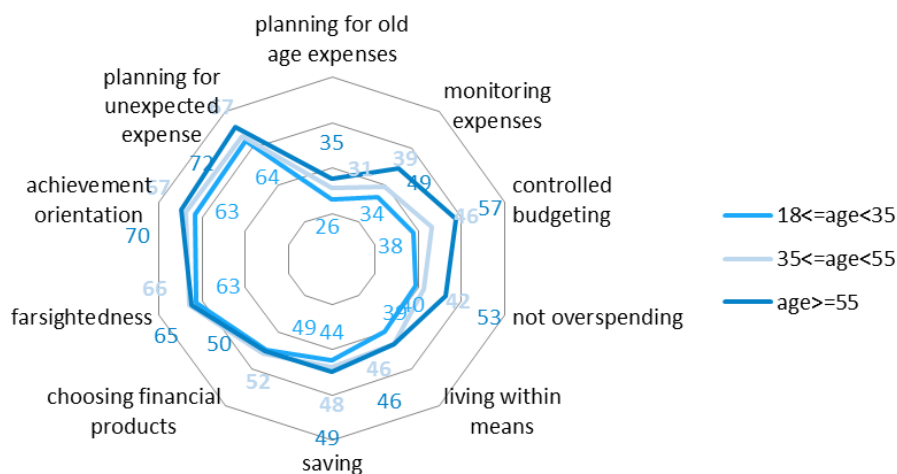




Source: WB Financial Capability Survey, Philippines 2014

The survey results further suggest that a generational gap exists with the younger generation lacking behind older survey participants, in particular in their ability to manage day-to-day finances and to plan for old age expenses. Figure 13 shows that while those aged 35 or younger achieved a score of 26 on planning for old age expenses, people between 35 and 55 scored 31, and those 55 and older scored the highest score (35). With respect to day-to-day money management skills, younger adults struggle more than their older counterpart groups when it comes to monitoring their expenses (34 vs 49), budgeting (38 vs 57), and not overspending (39 vs 53).

Figure 13. Average Financial Capability Scores by age



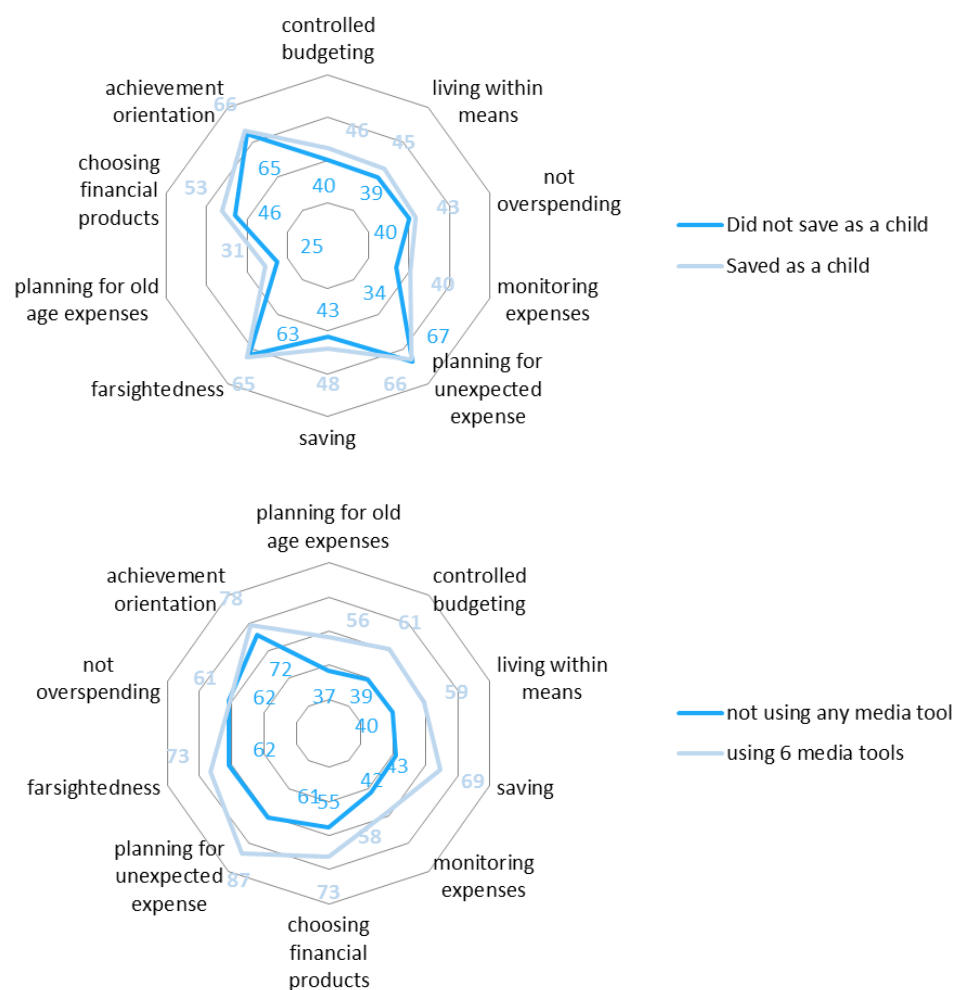
Source: WB Financial Capability Survey, Philippines 2014

Starting early pays off since having saved as a child correlates with higher scores in several financial capability areas. Respondents who already saved in their childhood tend to outperform their counterpart group who did not form savings habits as a child in

the areas of choosing financial products and services, planning for old age expenses, and monitoring expenses. As shown in figure 14, those who began savings habits as children display better attitudes towards savings than those who did not save in their childhood. Regression analysis confirms that these differences remain significant even after controlling for other socio-economic and demographic factors (see table 7, table 8 in Appendix B).

Another pattern which emerges is that regular usage of a broad range of media has huge value. Notably, as compared to those who do not use print, broadcast, and internet media at a regular basis, more active media consumers tend to score higher in almost all assessed financial capability areas, except in the area of refraining from overspending. This result suggests that any efforts to enhance financial capability in an effective manner should involve a very broad media engagement.

Figure 14. Average Financial Capability Scores by child saving behavior, media usage



Source: WB Financial Capability Survey, Philippines 2014

3. Financial Consumer Protection

In addition to peoples' ability to take sound financial decisions, the recent global financial crisis has highlighted the importance of financial consumer protection to protect consumers from abusive sale practices and to level the playing field between providers and consumers of financial services. Financial consumer protection is about ensuring a fair interaction between providers and consumers of financial services. An effective financial consumer protection regime is essential in counterbalancing the inherent disadvantage of financial service consumers vis-à-vis the power, information, and resources of their providers. Without basic protective measures, consumers may find it difficult or costly to obtain sufficient information or adequately understand the financial products that they use.

Effective financial consumer protection frameworks are also critical for instilling trust in the formal financial system and for ensuring that expanded financial sector outreach benefits consumers and the overall economy. A high incidence of conflicts with financial service providers or low levels of satisfaction with financial products used could undermine the trust in the formal financial system. Despite making existing consumers worse off, it can also discourage potential new consumers to enter the market. As indicated in chapter 1.5, this already appears to be the case in the Philippines since seventeen percent of the unbanked population cited lack of trust as main obstacle to formal account ownership.

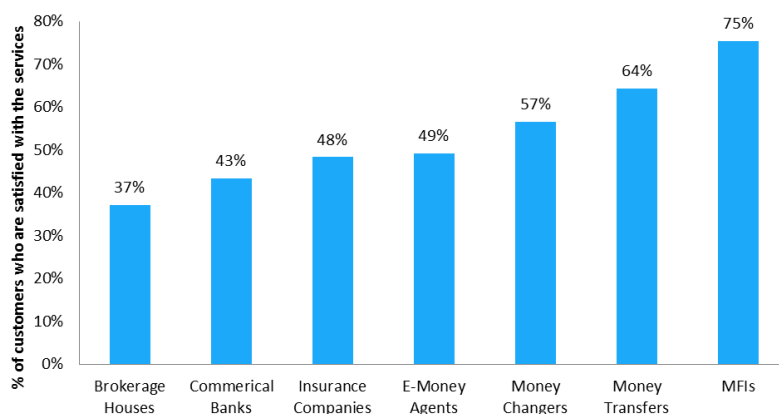
This chapter assesses the effectiveness of the current financial consumer protection regime from a demand-side perspective, with a focus on consumers' satisfaction with financial products and service and consumer redress and dispute resolution. In order to measure whether products that financially included Filipino adults use are effectively meeting their needs, the financial capability survey sought to capture the overall satisfaction of consumers with the eight most common types of providers and their products and services. To examine the effectiveness of existing consumer redress mechanisms, this survey asked users of financial services to share their experiences with current internal and external redress mechanisms, and identified segments of the population that are more likely to have encountered a conflict with a financial service provider in the past three years.

3.1 Financial Consumers' Satisfaction Rates

The survey results suggest that although commercial banks have the highest financial sector outreach, they appear to be less likely to cater the needs of their

customers, as compared to six other types of financial service providers¹⁸. Figure 15 indicates that banks seem to meet the needs of only 43 percent of their client base, a satisfaction rate which is only slightly higher than the 37 percent achieved among brokerage services users. On the other side of the spectrum, MFIs achieved the highest satisfaction rate among their clients (75 percent), followed by money transfers with 64 percent, and money changers with 57 percent. The usage of agents as distributors of e-money has been favored by policy makers in the Philippines given cost and convenience benefits of this distribution model. However, user experience with their services suggests that not all of them meet their clients' needs. Only around 50 percent of those who used their services reported to be satisfied with providers of digital financial services.

Figure 15. Clients' satisfaction with services provided by common types of financial institutions



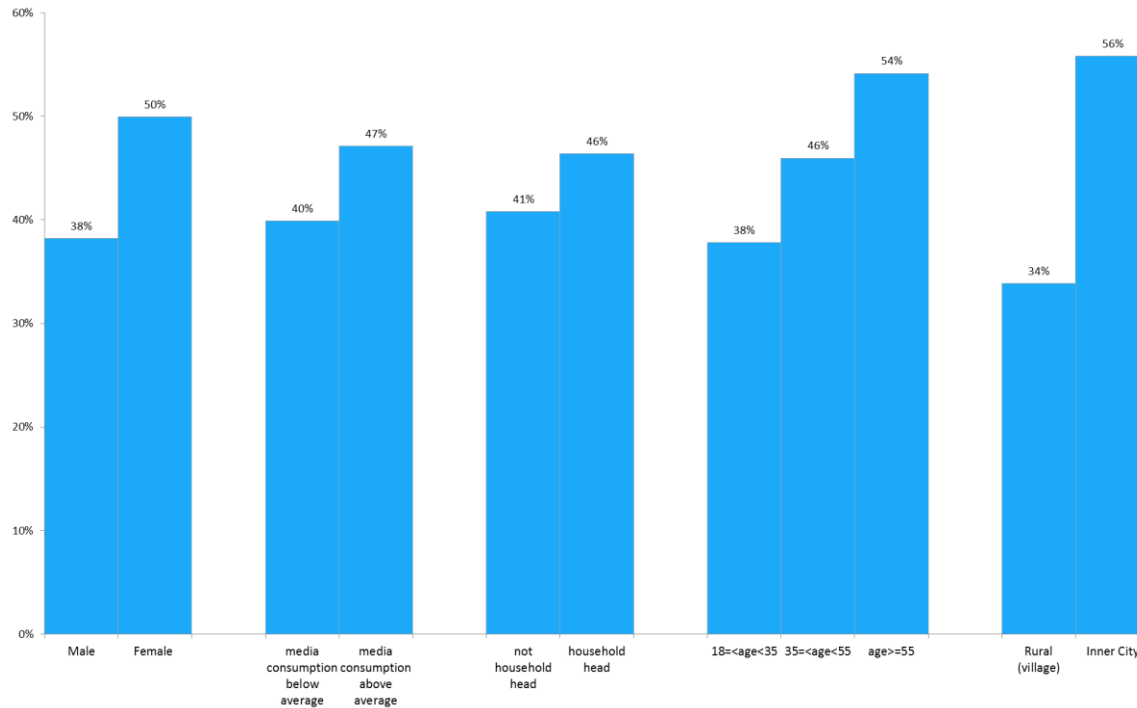
Source: WB Financial Capability Survey, Philippines 2014

A closer look into bank satisfaction rates among different use profiles reveals that banks are less likely to cater the needs of men, young adults, and rural dwellers as compared to their respective counterpart groups. Notably, women in the Philippines are not only more likely than men to be financially included but they are also more likely to benefit from their participation in the formal financial sector. This finding is mirrored in the fact that female Filipinos are 12 percentage points more likely than men to be satisfied with the bank services they used. As illustrated in figure 16, age also plays an important role in explaining differences in bank satisfaction rates. Even larger differences in bank

¹⁸ It has to be noted that satisfaction rates are by nature subjective and the client pool differs between different types of providers. However, this finding holds even if we look at the same pool of customers. For instance, even if we compare holders of bank products who currently use products from other types of providers, bank products still seem to relatively cater their needs less than products from other financial institutions.

satisfaction rates can be observed between urban and rural dwellers suggesting that they are not only less likely to participate in the formal financial sector but also less likely to benefit from it once they do.

Figure 16. Bank’s satisfaction rate by gender, media consumption, household head status, age, and location



Source: WB Financial Capability Survey, Philippines 2014

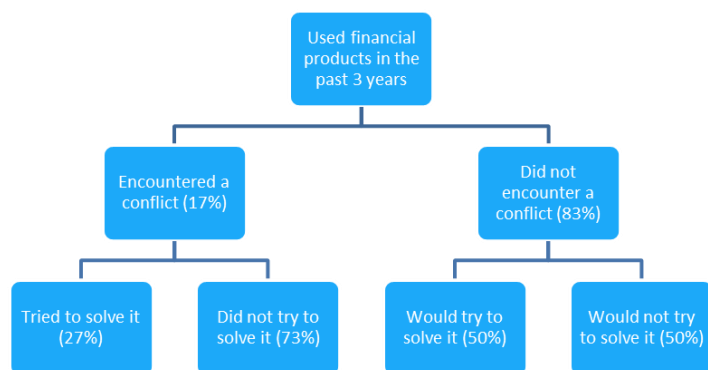
3.2 Dispute Resolution Mechanisms

A big worry is that a substantial proportion – almost a fifth - of the surveyed adult population experienced a dispute with a financial service provider in the past three years, the large majority of which did, however, not pursue any actions to resolve it. The proportion of reported disputes within the past three years in the overall population is relatively higher in the Philippines than in those few countries for which similar survey data is available. For example, a comparable survey in Mozambique revealed that in the past three years 15 percent of the surveyed population encountered a dispute with a financial service provider, while in Mongolia only five percent, and in Tajikistan only one percent of the sample reportedly experienced similar disputes. Figure 17 shows that inertia is the most common response in the event of a dispute and only around a quarter of those who experienced a dispute actually tried to solve it. When asking those who had not experienced a financial service provider conflict in the past three years about actions

they would take in the event of such a dispute, around half of them indicated that they preferred not to take any actions.

Delving deeper into the characteristics of those who encountered a conflict, the survey results suggest that low income populations and retirees are among the groups most vulnerable to having faced a financial dispute. The bottom 25 percent of the income distribution is not only less likely to use formal financial products and services they are also more likely to experience a financial dispute once they participated in the formal financial sector, as compared to the richest 25 percent. While only 16 percent of the richest 25 percent encountered a financial service provider, around a fifth of the bottom of the pyramid stated that they encountered a conflict in the past three years (see figure 17). As compared to the active working force, retirees on the other hand enjoy relatively better usage levels of financial services, they are, however, also more likely to having encountered a financial dispute. Twenty three percent of retired population had experienced such disputes in the last three years, compared to 18 percent for those who were not retired. Regression analysis reveals that these differences are significant even after controlling for other socioeconomic and demographic factors (see table 9 in Appendix B).

Figure 17. Approach to deal with financial service provider conflicts

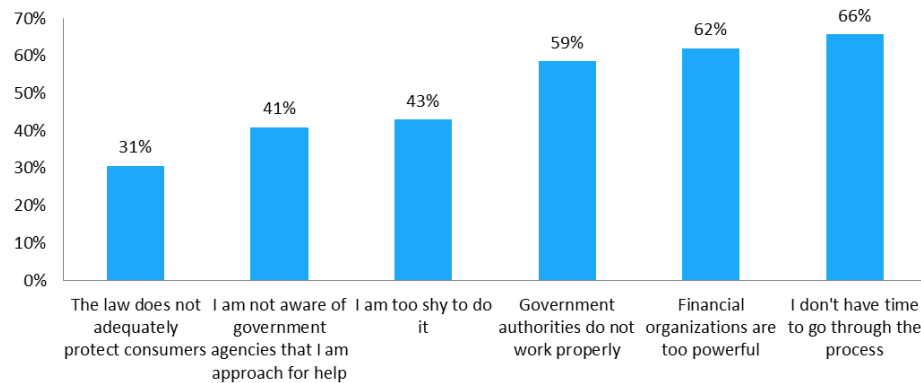


Source: WB Financial Capability Survey, Philippines 2014

Major reasons for not trying to solve a dispute include perceived lengthy time of proceedings, the view that financial providers are simply too powerful, as well as lack of trust in the efficiency of the respective government authorities. While two thirds of the surveyed financial consumers stated that lack of time to go through the process was the main reason for their inertia, 60 percent stated that lack of trust in the effectiveness of government authorities was the main perceived obstacle to taking any actions. Forty three percent indicated that they did not pursue actions to resolve the dispute due to their lack of confidence. Nearly half of those who did not try to solve a conflict stressed that they lack awareness of appropriate government agencies they could approach for help. These findings are consistent with those of the 2014 WB Diagnostic

Review of Consumer Protection in the Banking Sector and suggest the urgent need to require financial institutions at a minimum to resolve complaints within a reasonable timeframe and to raise public awareness about BSP’s FCPD, in particular about its mission of providing a comprehensive external complaints resolution service. In addition, in order to increase overall trust in FCPD’s effectiveness, it requires powers to make binding decisions.

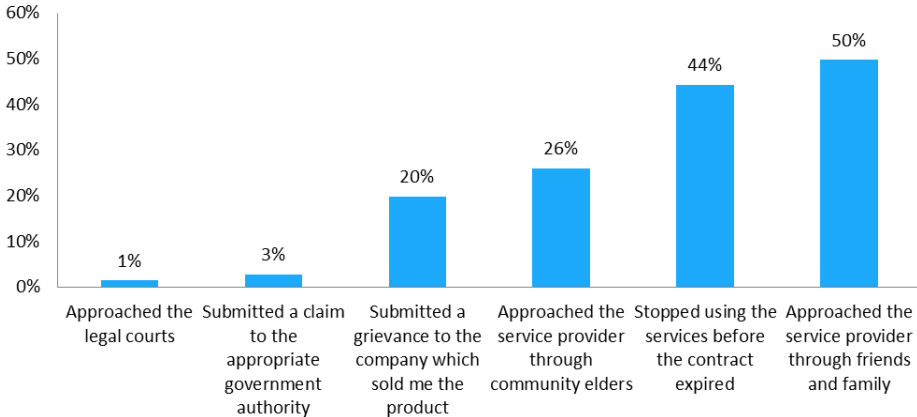
Figure 18. Reasons for not solving conflicts with financial service providers



Source: WB Financial Capability Survey, Philippines 2014

In terms of actions taken in the event of a dispute, external systems of redress such as BSP’s FCPD were barely sought by financial customers who experienced conflicts with financial providers. Most of those who experienced a conflict and took any actions to resolve it, decided to approach the provider through friends and family (50 percent), followed by a significant proportion that simply stopped using their services before contract expiration (44 percent). Besides friends and family members, local power-holders were also frequently sought in the event of a dispute to help those facing the conflict in approaching the service providers (26 percent). Only four percent of consumers actually used formal external systems of redress for settling financial disputes they encountered: three percent submitted a claim to the appropriate government authority including FCPD, while one percent approached the legal courts.

Figure 19. Actions taken to redress conflicts with financial service providers



Source: WB Financial Capability Survey, Philippines 2014

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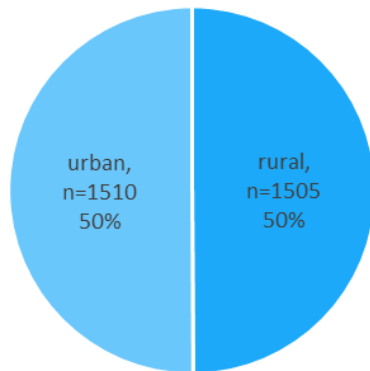
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Appendix

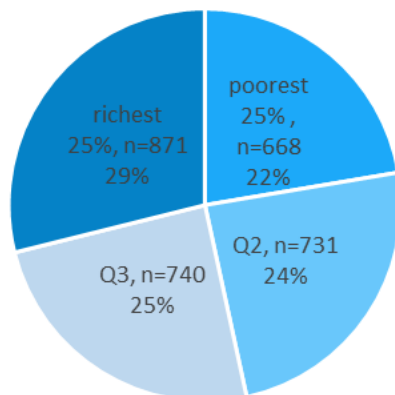
A. Background on the Philippines Financial Survey

Figure 20. Estimated population break-down by urban/rural



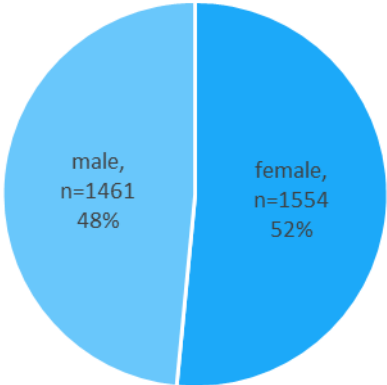
Source: Philippines Financial Capability Survey 2014

Figure 21. Estimated population break-down by different income groups



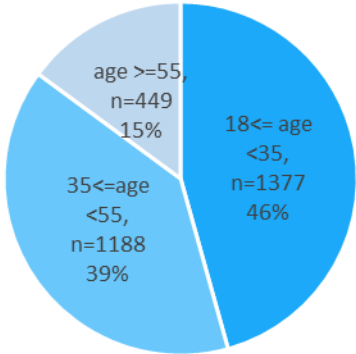
Source: Philippines Financial Capability Survey 2014

Figure 22. Estimated Population Break-down by Male/Female



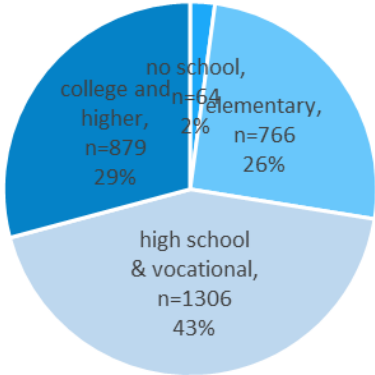
Source: Philippines Financial Capability Survey 2014

Figure 23. Estimated population break-down by age groups



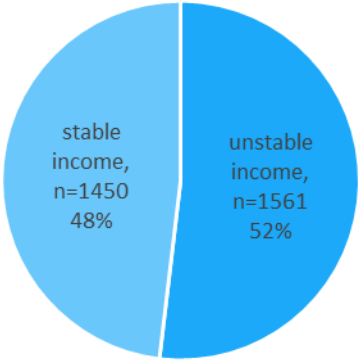
Source: Philippines Financial Capability Survey 2014

Figure 24. Estimated population break-down by education groups



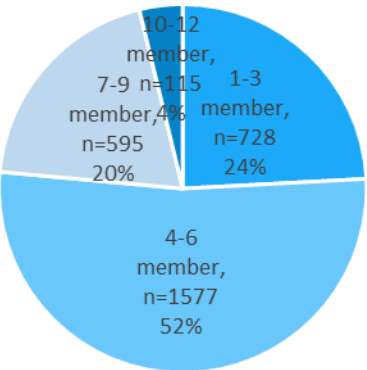
Source: Philippines Financial Capability Survey 2014

Figure 25. Estimated division of stable/unstable income groups



Source: Philippines Financial Capability Survey 2014

Figure 26. Estimated population break-down by household size



Source: Philippines Financial Capability Survey 2014

B. Regression Tables

Chapter 1. Financial Inclusion

Table 5. Financial inclusion by social and demographic factors

Age	0.00*** (0.00)	0.00*** (0.00)	0.00*** (0.00)
Male	-0.18*** (0.02)	-0.18*** (0.02)	-0.20*** (0.03)
Primary school	0.22*** (0.07)	0.24*** (0.07)	0.20** (0.08)
Secondary school	0.28*** (0.07)	0.29*** (0.07)	0.28*** (0.09)
Tertiary school	0.32*** (0.08)	0.33*** (0.08)	0.31*** (0.09)
Read	-0.09 (0.09)	-0.11 (0.09)	-0.14 (0.11)
Head	0.05* (0.03)	0.05* (0.03)	0.06* (0.04)
2nd income quartile	0.07** (0.03)	0.07** (0.03)	0.10*** (0.03)
3rd income quartile	0.22*** (0.03)	0.22*** (0.03)	0.25*** (0.03)
4th income quartile	0.37*** (0.03)	0.36*** (0.03)	0.42*** (0.04)
Unemployed	0.10** (0.05)	0.11** (0.05)	0.10* (0.06)
Formally employed	0.12*** (0.04)	0.11*** (0.04)	0.16*** (0.05)
Informally employed	0.05 (0.04)	0.05 (0.04)	0.08* (0.05)
Self-employed	0.12*** (0.03)	0.12*** (0.03)	0.16*** (0.04)
Retired	0.09 (0.06)	0.09 (0.06)	0.10 (0.09)
Urban	0.16*** (0.02)	0.16*** (0.02)	0.11 (0.08)
Saved as a child		0.03	-0.00

	(0.02)	(0.02)
2 medium used	0.08*	0.06
	(0.05)	(0.05)
3 medium used	0.02	-0.03
	(0.04)	(0.04)
4 medium used	0.08*	0.04
	(0.05)	(0.04)
5 medium used	0.06	-0.00
	(0.05)	(0.05)
6 medium used	0.11	0.08
	(0.07)	(0.07)

Standard error in parentheses *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$

Chapter 2. Financial Capability

Table 6. Financial literacy score by social and demographic factors

Age	8.48e-06 (0.000971)	0.000382 (0.00106)	0.000380 (0.00106)	0.000578 (0.00104)
Male	-0.114*** (0.0298)	-0.0968*** (0.0293)	-0.0952*** (0.0293)	-0.0911*** (0.0296)
Primary school	-0.0323 (0.150)	-0.0556 (0.147)	-0.0596 (0.147)	-0.0300 (0.142)
Secondary school	0.0740 (0.152)	0.0551 (0.150)	0.0498 (0.150)	0.0689 (0.145)
Tertiary school	0.274* (0.153)	0.251* (0.151)	0.245 (0.151)	0.256* (0.146)
Read	0.199 (0.167)	0.210 (0.165)	0.215 (0.167)	0.152 (0.164)
Head	0.184*** (0.0339)	0.177*** (0.0332)	0.175*** (0.0332)	0.166*** (0.0329)
2 nd income quartile		-0.0575* (0.0316)	-0.0566* (0.0319)	-0.0594* (0.0321)
3 rd income quartile		-0.0662* (0.0366)	-0.0665* (0.0367)	-0.0797** (0.0356)
4 th income quartile		-0.0529 (0.0422)	-0.0573 (0.0419)	-0.0735* (0.0401)
Unemployed		-0.104* (0.0629)	-0.104* (0.0630)	-0.106* (0.0616)
Formally employed		0.00679	0.00666	0.0419

	(0.0457)	(0.0455)	(0.0499)
Informal employed	0.112**	0.114**	0.131**
	(0.0485)	(0.0485)	(0.0507)
Self-employed	-0.0204	-0.0201	-0.0231
	(0.0416)	(0.0415)	(0.0411)
Retired	-0.00386	-0.00443	0.0166
	(0.0816)	(0.0813)	(0.0816)
Urban		0.0202	0.0246
		(0.0410)	(0.0379)
2 medium used			0.188***
			(0.0681)
3 medium used			0.167**
			(0.0686)
4 medium used			0.177**
			(0.0685)
5 medium used			0.152**
			(0.0735)
6 medium used			0.402***
			(0.0837)
Household size			0.00182
			(0.00624)
Stable income			-0.0727**
			(0.0300)
Saved as a child			0.115***
			(0.0301)

Standard error in parentheses *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$

Table 7. Financial capabilities by social and demographic factors

VARIABLE S	Budgeting	Living within means	Not overspending	Monitoring expenses	Covering unexpected
Low financial literacy	-6.645***	-7.354***	-2.279	-7.923***	-0.0453
	(2.047)	(1.804)	(2.282)	(2.443)	(1.856)
Age	0.364***	0.130*	0.341***	0.207**	0.177***
	(0.0732)	(0.0702)	(0.0891)	(0.0851)	(0.0672)
Male	-9.681***	-6.387***	-4.124*	-6.632***	0.923
	(2.088)	(1.835)	(2.481)	(2.433)	(2.452)
Primary school	5.113	4.211	7.638	4.177	8.970
	(7.517)	(7.748)	(8.660)	(9.910)	(7.013)
Secondary school	10.54	8.087	9.398	7.293	12.53*
	(7.701)	(7.796)	(8.619)	(9.915)	(6.892)

Tertiary school	9.411	6.718	12.82	9.515	14.35*
	(7.736)	(7.856)	(8.588)	(9.954)	(7.309)
Read	14.46*	12.63	10.53	7.821	-11.34
	(8.110)	(7.881)	(9.845)	(10.12)	(8.699)
Head	7.312***	4.223*	0.846	6.560**	-2.390
	(2.573)	(2.230)	(2.897)	(2.860)	(2.524)
2 nd income quartile	0.483	-1.015	6.237**	-1.011	1.355
	(2.564)	(2.059)	(2.581)	(2.594)	(2.292)
3 rd income quartile	1.188	-0.842	8.942***	-1.484	3.097
	(2.765)	(2.227)	(2.904)	(2.791)	(2.177)
4 th income quartile	14.60***	9.713***	19.59***	9.180**	4.455
	(3.090)	(2.740)	(3.810)	(3.700)	(3.150)
Unemployed	-2.266	-1.284	9.136	-9.586	3.484
	(4.924)	(4.168)	(5.548)	(5.815)	(4.898)
Formally employed	1.802	2.780	9.436**	-2.642	-0.811
	(3.341)	(2.848)	(3.826)	(3.932)	(3.246)
Informal employed	-7.005*	-6.640**	10.18**	-14.15***	6.012
	(4.218)	(3.308)	(4.087)	(4.089)	(3.760)
Self-employed	-0.524	0.670	12.67***	-3.705	0.738
	(3.224)	(2.723)	(3.405)	(3.387)	(2.791)
Retired	6.539	57.06***	14.75**	2.633	1.839
	(5.966)	(6.367)	(7.352)	(7.634)	(5.600)
Urban	-7.262	-7.644	2.435	-8.169	-5.474
	(9.248)	(7.176)	(7.149)	(8.119)	(4.431)
2 medium used	2.645	4.224	-8.357*	4.830	0.679
	(3.865)	(3.328)	(4.715)	(4.641)	(3.721)
3 medium used	-2.360	0.266	-6.266	0.458	6.187
	(3.600)	(3.048)	(4.580)	(4.427)	(3.965)
4 medium used	-3.194	0.987	-7.502	4.003	2.737
	(3.541)	(2.987)	(4.909)	(4.245)	(4.246)
5 medium used	-0.748	0.211	-12.38**	-1.252	6.410
	(3.872)	(3.334)	(5.275)	(4.654)	(4.850)
6 medium used	5.909	10.54**	0.978	18.26***	20.11***
	(6.266)	(5.170)	(7.306)	(6.428)	(5.308)
Household size	0.167	-0.0234	0.672	0.213	-0.484
	(0.432)	(0.341)	(0.542)	(0.491)	(0.418)

Stable income	-4.212*	-4.035**	4.405**	-7.830***	1.046
	(2.224)	(1.873)	(2.212)	(2.475)	(1.906)
Saved as a child	4.070**	4.078**	2.139	4.813**	-2.175
	(1.966)	(1.681)	(2.267)	(2.133)	(1.730)

Standard error in parentheses *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$

Table 8. Financial capabilities by social and demographic factors

VARIABLES	Saving	Farsightedness	Provision for old age	Choosing financial products	Achievement oriented
Low financial literacy	-0.269	-2.146*	-5.835***	-6.829***	-5.672***
	(1.723)	(1.149)	(1.795)	(2.264)	(1.504)
Age	0.0918	0.0603	0.105	0.119	0.109**
	(0.0647)	(0.0523)	(0.0708)	(0.0839)	(0.0479)
Male	-0.810	-0.513	-4.372**	2.761	-0.852
	(1.935)	(1.616)	(1.842)	(2.613)	(1.690)
Primary school	-9.208	6.671	10.66**	9.344	4.023
	(5.756)	(4.609)	(4.817)	(11.16)	(3.621)
Secondary school	-7.470	10.92**	12.10**	11.98	5.664
	(5.935)	(4.740)	(4.871)	(10.96)	(3.560)
Tertiary school	-6.896	14.40***	11.36**	13.28	4.585
	(6.015)	(4.665)	(4.933)	(11.04)	(3.500)
Read	7.963	-7.788	-3.985	-8.095	-4.351
	(6.219)	(5.530)	(5.629)	(10.53)	(4.566)
Head	1.211	-0.113	3.874*	-5.133*	2.259
	(2.431)	(1.559)	(2.273)	(2.823)	(1.725)
2 nd income quartile	8.304***	-2.018	1.264	7.890**	-1.011
	(2.020)	(1.680)	(2.011)	(3.167)	(1.841)
3 rd income quartile	5.247**	-3.905**	-0.779	6.428**	-0.863
	(2.289)	(1.765)	(2.272)	(3.120)	(1.832)
4 th income quartile	6.717**	-5.124**	-2.957	7.857**	0.0942
	(2.861)	(2.052)	(2.357)	(3.361)	(2.071)
Unemployed	-8.092*	-0.0317	-4.932	1.193	-6.158**
	(4.329)	(2.694)	(3.446)	(7.072)	(3.052)
Formally employed	-1.996	0.586	0.717	8.591**	-0.619

Informally employed	(3.221) 0.397	(2.264) 0.325	(2.717) -7.810***	(4.126) 7.168	(2.697) -8.379***
Self-employed	(3.623) 0.225	(2.394) 1.018	(2.711) -5.145**	(5.399) 5.258	(2.710) -5.555***
Retired	(2.747) 1.489	(2.035) -6.881	(2.045) 49.93***	(4.442) 8.097	(2.086) -4.789
Urban	(4.810) -6.538	(4.549) -4.349	(4.355) -4.658	(6.540) -4.181	(3.401) -6.200
2 medium used	(6.891) 2.962	(5.673) 4.120	(10.47) -0.459	(6.988) 0.299	(6.155) -3.440
3 medium used	(2.951) 3.860	(2.561) 1.880	(3.217) -1.208	(4.771) 3.150	(2.656) -4.348
4 medium used	(3.105) 4.291	(2.595) 0.406	(2.985) -0.804	(4.588) 0.992	(2.757) -5.751**
5 medium used	(2.921) 3.258	(2.463) 1.939	(2.950) -0.653	(4.394) 0.302	(2.527) -3.465
6 medium used	(3.354) 22.48***	(2.661) 7.030	(3.600) 18.70***	(5.209) 19.42***	(2.669) 0.561
Household size	(4.801) 0.619	(4.282) 0.0826	(6.224) 0.285	(5.287) -0.435	(4.342) -0.410
Stable income	(0.408) -0.541	(0.275) 4.718***	(0.317) -4.665***	(0.513) 2.086	(0.258) -7.174***
Saved as a child	(1.810) 3.835**	(1.408) -0.0992	(1.624) 3.351**	(2.537) 4.900**	(1.679) 0.796
	(1.468)	(1.195)	(1.656)	(2.227)	(1.426)

Standard error in parentheses *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$

Chapter 3. Consumer Protection

Table 9. Probability of encountering a financial conflict by social and demographic factors

Age	0.00173 (0.00194)	0.00152 (0.00217)	0.00168 (0.00222)	0.00164 (0.00228)
Male	0.0476 (0.0630)	0.0442 (0.0631)	0.0466 (0.0630)	0.0538 (0.0641)

Primary school	0.432 (0.304)	0.475 (0.306)	0.379 (0.314)	0.422 (0.309)
Secondary school	0.422 (0.305)	0.474 (0.307)	0.363 (0.315)	0.402 (0.311)
Tertiary school	0.412 (0.308)	0.476 (0.309)	0.351 (0.321)	0.374 (0.316)
Read	-0.319 (0.308)	-0.344 (0.315)	-0.268 (0.318)	-0.372 (0.317)
Head	0.0591 (0.0645)	0.0285 (0.0671)	0.0264 (0.0692)	0.0153 (0.0719)
2nd income quartile		-0.0428 (0.0846)	-0.0466 (0.0819)	-0.0440 (0.0815)
3rd income quartile		-0.0200 (0.0863)	-0.0411 (0.0811)	-0.0225 (0.0813)
4th income quartile		-0.137 (0.0878)	-0.206** (0.0860)	-0.174** (0.0829)
Unemployed		0.0359 (0.105)	0.0115 (0.106)	0.194* (0.115)
Formally employed		-0.129* (0.0734)	-0.132* (0.0739)	0.0469 (0.0855)
Informally employed		0.0179 (0.146)	-0.0432 (0.144)	-0.0236 (0.143)
Self-employed		-0.0228 (0.126)	-0.0599 (0.128)	0.130 (0.133)
Retired		-0.312*** (0.115)	-0.311*** (0.115)	-0.213* (0.122)
Urban			0.0583 (0.0807)	0.0582 (0.0753)
Armm region			-0.0285 (0.160)	0.0106 (0.157)
Bicol region			-0.0271 (0.153)	-0.0118 (0.157)
Cagayan Valley region			0.0120 (0.141)	-0.0262 (0.153)

Calabarzon region	-0.112 (0.151)	-0.122 (0.145)
CAR region	-0.0231 (0.119)	-0.00749 (0.126)
Caraga region	-0.157 (0.251)	-0.180 (0.217)
Central Luzon region	0.231* (0.130)	0.169 (0.130)
Davao region	0.0704 (0.144)	0.0400 (0.146)
Ilocos region	0.0785 (0.135)	0.0877 (0.138)
NCR region	0.141 (0.138)	0.0765 (0.139)
Northern Mindanao region	0.161 (0.157)	0.147 (0.163)
Soccsksargen region	-0.0754 (0.165)	-0.0643 (0.169)
Western Visayas region	0.241 (0.179)	0.267 (0.182)
1 medium used		-0.359* (0.199)
2 medium used		-0.393** (0.154)
3 medium used		-0.226 (0.152)
4 medium used		-0.266* (0.156)
5 medium used		-0.212 (0.152)
Household size		-0.0151 (0.0140)
Stable income		0.300***

Saved as a child

(0.0711)

0.0398

(0.0638)

*Standard error in parentheses *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$*