

## Press Release 39/2016

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### Strong financial literacy could lead to more self-employment

The probability that a person is self-employed also depends on how much financial literacy they have. A new study by the Halle Institute for Economic Research (IWH) – Member of the Leibniz Association recently confirmed this correlation.

The economic development of a country depends on many factors, particularly the entrepreneurial activities of its citizens. When a company is founded, it is also usually accompanied by the generation of income, innovation, jobs, research and development – provided that the company can successfully sustain itself on the market. The failure of a company in contrast is often associated with lack of planning, under-capitalization or financial difficulties, miscalculation of risks, financial mismanagement, overly rapid growth or “over expansion.” However, financial literacy can counteract this because it leads to better decisions – for example, when it comes to financing and investment issues. IWH researchers Aida Ćumurović and Walter Hyll have examined whether thorough financial literacy also promotes self-employment. Their analysis linked existing research on the effects of financial literacy on budgetary decisions to examinations of characteristics possessed by entrepreneurs. As past studies suggest, strong financial literacy is accompanied by higher investment income, more favourable credit terms and better retirement planning.

To measure financial literacy, the researchers adopted data from SAVE (Sparen und Altersvorsorge in Deutschland) [Savings and Retirement Financing in Germany] at the Munich Center for the Economics of Aging. These data included a survey of 2,222 people on financial issues: Three questions concerned basic knowledge, and eight others concerned advanced knowledge in finance. After distinguishing between various occupations, the data showed that the self-employed performed significantly better than the unemployed and people employed in other ways. Even when other factors such as age, education, risk appetite, cognitive ability and parental character traits were taken into account, the results did not change. An attempt was also made to incorporate a reverse effect of financial literacy on self-employment in the calculations. The researchers’ econometric findings thereby showed that greater financial literacy led to greater self-employment. Since financial literacy is teachable, entrepreneurial activities can be supported by incorporating financial education into the educational curricula – if people decide that this is politically desirable.

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