

Financial Literacy as a Solution for Bank Marketing Myopia

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ARTICLE INFO

Keywords: Financial Literacy,
Banks, Marketing Myopia

Received : 25, April

Revised : 27, Mei

Accepted: 29, June

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ABSTRACT

Profit maximization through offering customer-centric products, sometimes with manipulative approaches, has been the norm for bank strategies. Therefore, some sort of bank marketing myopia rules the financial markets. Yet, these practices have been proven of being self-deteriorating. This research discusses the possibility of both banks and their clients benefiting from a higher degree of financial literacy. Banks would no longer have the need to be myopic, clients will no longer be afraid of getting scammed. A win-win situation is proposed with the use of S&P's global financial literacy survey results and macroeconomic data from the World Bank and IMF's databases.

INTRODUCTION

The liberalization of the financial markets during the last couple of decades throughout the world eased the emergence of novel financial products with the aim of maximizing profits (Campbell, et al., 2011; Gaurav, et al., 2011; Lusardi & Mitchell, 2014; Laeven, et al., 2015). To realize the latter, financial institutions turned their focus to finding innovative marketing strategies to retain their current clients, attract new ones, and upsell their products (Uksumenko, et al., 2017). Yet, the last global financial crisis which lasted for nearly two years (2007-2009) proved these “innovative” strategies to have fooled the consumers as they were rather complex to be understood (Campbell, et al., 2011; Disney & Gathergood, 2013; Lusardi & Mitchell, 2014; Laeven, et al., 2015; Calcagno & Monticone, 2015). Having focused simply on profit maximization rendered the executives of these financial institutions shortsighted with no consideration at all about what’s to come (Laeven, et al., 2015). In other terms, they were nearsighted to the gold cliffs rather than farsighted to the gold mountains, a common phenomenon when marketing myopia takes place. Similarly, the present-biased consumers were happy by benefiting from the ease of access to loans, credits, and other financial services (Campbell, et al., 2011). Consequently, the high level of customer-centric products hurt both parties attesting to Smith, et al. (2010)’s calls for a lesser customer-centricity in the markets than what Levitt (2004), the founder of customer centrism in marketing, calls for. Further research found that being completely customer-centric causes companies to be shortsighted as they see the market from one perspective: the customer’s perspective (Gallo, 2016), which is not enough for the success of the company (Smith, et al., 2010). Hence, both parties are to be blamed for the misfortunes that they endured due to the crises.

Even though a win-win solution is mostly sought for yet hard to reach, financial literacy in this case might be the key to avoiding such malpractices in the future. There has been a lot of research discussing the personal benefits of financial literacy and a consensus has risen on the positive relationship between financial literacy and people’s financial decision-making (Bolton, et al., 2011; Disney & Gathergood, 2013; Lusardi & Mitchell, 2014; Calcagno & Monticone, 2015). For instance, Her Astuti and Trinugroho (2016) found that higher financial literacy increases people’s participation in the formal financial market, Calcagno and Monticone (2015) found that a more financially literate person is less prone to falling into financial biases, and Lusardi and Mitchell (2014) found that a higher financial literacy rate leads to a higher propensity to save money for retirement. Yet, similar research works showing the benefits of financial literacy for business are still underdeveloped in academia. One of the most interesting on-topic works is Yun (2017) who focused on the US and found that making people more financially literate could benefit business entities as well. The number of academic works gets even smaller when the focus turns to financial institutions.

Therefore, this paper's aim is to advocate the importance of financial literacy for financial service providers. It rejects the idea that having financially literate individuals is a threat to the profitability of financial institutions and it discusses the reasons why having financially literate clients is beneficial to them. This paper also calls on financial institutions to invest in their clients' financial literacy with the aim of overcoming banking marketing myopia.

LITERATURE REVIEW

The liberalization of the financial markets during the last couple of decades throughout the world eased the emergence of novel financial products with the aim of maximizing profits (Campbell, et al., 2011; Gaurav, et al., 2011; Lusardi & Mitchell, 2014; Laeven, et al., 2015). To realize the latter, financial institutions turned their focus to finding innovative marketing strategies to retain their current clients, attract new ones, and upsell their products (Uksumenko, et al., 2017). Yet, the last global financial crisis which lasted for nearly two years (2007-2009) proved these "innovative" strategies to have fooled the consumers as they were rather complex to be understood (Campbell, et al., 2011; Disney & Gathergood, 2013; Lusardi & Mitchell, 2014; Laeven, et al., 2015; Calcagno & Monticone, 2015). Having focused simply on profit maximization rendered the executives of these financial institutions shortsighted with no consideration at all about what's to come (Laeven, et al., 2015). In other terms, they were nearsighted to the gold cliffs rather than farsighted to the gold mountains, a common phenomenon when marketing myopia takes place. Similarly, the present-biased consumers were happy by benefiting from the ease of access to loans, credits, and other financial services (Campbell, et al., 2011).

METHODOLOGY

To check this research's claim's validity, I have used Standard and Poor's 2014 Global Financial Literacy Survey's results published in Klapper, Lusardi, and van Oudheusden (2015) and the World Bank's Database primarily focusing on the Global Findex Report and IMF's Financial Access Survey. These datasets contain information on the financial markets of nearly all the countries around the world with either thousands of respondents having been surveyed or data collected from reliable sources (Ozsuca, 2019). After cleaning the data, the total number of included countries amounts to 142 scattered in different parts of the world. The data also focuses solely on 2014 as it's the only year during which global financial literacy data exists. As the main idea of this research is to find enough supporting evidence of financial literacy's benefits to banks, I have used three different sorts of data from the World Bank and IMF to answer it noting that all the data is at the national level. The banks' average return on assets (bank capital to assets ratio) and the percentage of banks' non-performing loans rate to their total gross loans will show the profitability and healthiness of the banking sector. The number of branches and automated teller machines (ATMs) will show the on-field presence of banks and the use of self-banking. Whereas the number of account owners, the number of borrowers from commercial banks, and the number of depositors at commercial banks will show the acceptance of financial institutions and the use of their services by the masses.

In other terms, these factors will show aspects of the financial inclusion (Ozsuca, 2019; Cicchiello, et al., 2021) and their relation to financial literacy. Table 1 shows further detail about the chosen factors.

Table.1 Variables

Abbreviation	Description	Source
FinLit	Financial literacy rates (%)	Klapper, Lusardi, and van Oudheusden (2014)
ROA	Bank capital to assets ratio (%)	IMF's Financial Access Survey
NPL	Banks nonperforming loans to total gross loans (%)	IMF's Financial Access Survey
Branches	Commercial bank branches (per 100,000 adults)	IMF's Financial Access Survey
ATMs	Automated teller machines ATMs (per 100,000 adults)	IMF's Financial Access Survey
Accounts	Account ownership at a financial institution or with a mobile-money-service provider (% of population 15+)	World Bank's Global Findex Database
Borrowers	Borrowers from commercial banks (per 1,000 adults)	IMF's Financial Access Survey
Depositors	Depositors with commercial banks (per 1,000 adults)	IMF's Financial Access Survey

I used JASP, an open-source statistical tool based on IBM SPSS supported by the University of Amsterdam, to run my tests. I have used different statistical methods to check and assess the research claim. I have run a set of different analyses of variance (ANOVA) to check the existence of cross-continental differences in the variables. I have also run simple regressions between financial literacy as the independent variable and the remaining factors as the dependent variables. In addition, "continent" is used as a weighted least square factor to check the validity of the results both internationally and continentally.

RESEARCH RESULT AND DISCUSSION

The primary results show that there's a statistically significant difference in the levels of financial literacy on the continental level. Oceania, represented by two countries, Australia and New Zealand, top the list with 62.5%, whereas Central America has the lowest continental average with 27.67%. Asia, Africa, and South America have similar results, whereas Europe and North America are in the top 3. Table 2 shows the results received from the ANOVA. These results are important for this research because it sheds light on the importance of discussing the research aim both on the international and continental level.

Table.2 ANOVA FinLit by Continents

Continent	Africa	Asia	Central America	Europe	North America	Oceania	South America
FinLit	32.84	32.63	27.67	46.08	52.33	62.50	31.09
p-value <0.001							

Table.2 presents all the results of the different regressions. The first regression between FinLit and ROA reaffirms the fears of the banks. A higher financially literate population is a threat to their profitability. One percent change in people's financial literacy would decrease their ROA by 0.078%. Though, further exploration using the continent as a factor refutes this finding. Even though it remains significant on the international level, the relationship is statistically non-significant in all the continents with p-values being higher than 5%. The discussion of both results is at a 0.05 significance level. Therefore, the existence of a negative relationship between these two factors cannot be ascertained and surely no significant change happens to banks when people's FinLit increases. Using continent as a factor is important here because that allows this research to be taking into consideration the FinLit differences across continents. The other profitability and current standing variable, NPL, shows no statistical relation with FinLit. But when the continent is used as a factor, it shows a statistical relation (negative) with a 1% increase in FinLit decreasing the NPL by 0.2%. The coefficient of determination is also high, with 32.8% of the variation in the NPL being explained by the variation of FinLit.

The existence of banks, whether in the form of branches or ATMs, is also related to people's financial literacy. A one percent increase in people's FinLit resulted in an increase in the existence of both branches and ATMs. This means that higher FinLit increases people's usage of banking services and requires its presence. The increased return to scale of ATMs also shows how more financially literate populations use the ATMs much more frequently which could reduce the total operating costs of in-branch banking. To explore it further, I've checked the trends in the accessibility's two variables. The results are shown in figures 1 and 2. I found that the national demand for in-branch banking in relation to FinLit level reaches to two local maximums. The first one is when 25% of the people are financially literate. Though after a certain time, it grows back to the second maximum when at least 50% of the people are financially literate. This trend is quite interesting as it shows people's financial trends very clearly. In the beginning, people have to go to the bank to create a personal relationship with the bankers, understand the concept, and avoid mistakes in their transactions. Though, after a certain period, they get acquainted and no longer need to do that. With time passing by, they start their involvement with the bank more often as they'd like to get more services, hence causing an increase.

The best scenario is when people start doing most of their banking transactions without the use of a banking representative. Whereas the trend in the ATMs' existence shows a somewhat upward straight line in which the higher the national FinLit level, the higher the number of ATMs.

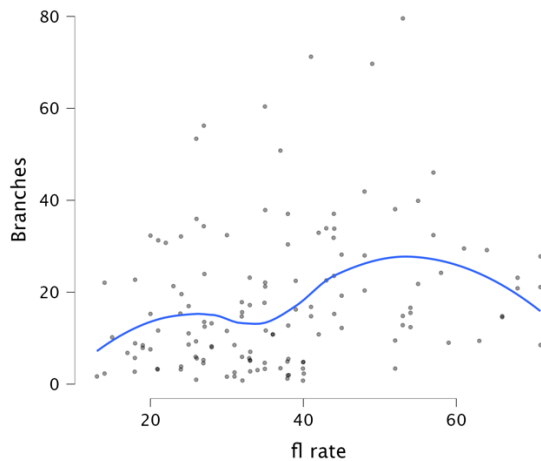


Figure 1: FinLit & Branches

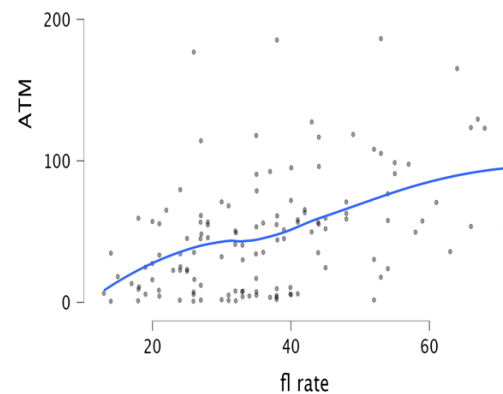


Figure 2: FinLit & ATMs

When it comes to people's use of financial products, all three variables (account ownership, number of borrowers, and number of depositors), are positively correlated with the national FinLit levels. This means that a higher FinLit will lead to an increased number of people holding bank accounts. Likewise, Her Astuti and Trinugroho (2016)'s research on the world's 4th largest country by population, Indonesia, shows the positive effect of an increase in people's financial literacy on their acceptance of financial products. They've focused on the poor people as they form the biggest portion of the unbanked population. A global characteristic for low-income people is also a relatively low financial literacy rate (Her Astuti & Trinugroho, 2016). Their regression line showed that the more a society is financially literate, the more its banking engagement rate is. As per the results of this research, borrowing money from banks also increases with a higher level of FinLit.

Disney and Gathergood (2013) found that households with heads showing low financial literacy rates engage more in high-cost credit than the ones showing high financial literacy rates. For instance, payday loans, which are short-term loans for small amounts of money, reached to 40 Billion US Dollars in 2010 (Campbell, et al., 2011). Noting that most of the people asking for payday loans are financially illiterate, a slight increase in their financial literacy will cause tremendous changes in their behaviors (Disney & Gathergood, 2013; Campbell, et al., 2011). They'll realize the high expenses they were incurring in getting payday loans and shift their main source of financing from the latter to bank loans. Similarly, depositing money in banks is positively related to people's financial savviness. Research shows that the more financially literate a person is, the more will he save money and engage in retirement pensions (Lusardi & Mitchell, 2014). When people save money

through bank-based retirement and saving plans, the deposits in banks will increase which will allow them to invest more and make higher profits. In addition, higher levels of financial literacy mean higher participation rates in the financial markets (Calcagno & Monticone, 2015; Lusardi & Mitchell, 2014), which quite often require people to have deposited money in bank accounts. Even if people have no clue what to invest their money in, there are many sources from which they can get help in making sound investment choices (Calcagno & Monticone, 2015). One of these sources is the use of banking representatives as financial experts, who, according to previous research, are mostly put in confidence by the financially literate and wealthy investors (Calcagno & Monticone, 2015). All these three being the most important factors for the success of a banking business, the increase of people's financial literacy should be taken quite seriously.

Table.3 Regression Results

Dependent Variable	Coefficient	P-Value	R-squared
ROA	-0.078	<0.001	18.5%
ROA (with continent)	-0.059	0.003	23.4%
NPL	-0.069	0.140	2.1%
NPL (with continent)	-0.20	<0.001	32.8%
Branch	0.281	0.004	6.3%
ATM	1.41	<0.001	16.9%
Accounts	1.485	<0.001	45.2%
Borrowers	10.662	<0.001	26.3%
Depositors	17.937	0.003	12.6%

CONCLUSIONS AND RECOMMENDATIONS

Acquiring the highest number of clients and retaining them has been the focus of bank marketing strategies for quite a long time (Uksumenko, et al., 2017). They've created and offered customer-centric products to realize the latter (Gaurav, et al., 2011). Even when they suffered from these practices, they didn't quit their customer-centric product development. One of the solutions for reducing their NPL, for example, was debt consolidation. Merging all the loans a person has into just one assumingly made it easier for the installment to be paid with the monthly payment being minimized (Bolton, et al., 2011). Yet, research and natural experiments showed the latter's inefficacy most of the time noting that the latter was once again a customer-centric solution. This research proposes a new solution for banks to be more competitive, earn more, and have a better standing. I propose the empowerment of people's understanding of financial principles and turning them into confident financial consumers by increasing their financial literacy. A lot of opportunities exist that banks could seize if the people are more financially literate. The inclusivity of the unbanked and underbanked households into the financial markets and people's refraining from

high-cost borrowing are some of these opportunities which banks disregarded till now (Yun, 2017).

Through this research, I find that by increasing people's FinLit, their adoption rates of financial products will increase causing an eventual increase in profits for banks. I also find that banks do not lose money if their clients are more financially literate. The required investments to realize the proposed solution will cost the financial institutions some money for sure. But at the same time, it will increase their profitability rates in the short term and secure their continuation in the long term. In this way, banks will no longer be bound to be financial institutions providing financial products but will reposition themselves as institutions facilitating and accelerating the public's financial decision-making processes. Future research should check the validity of this research's findings on the national level and provide mechanisms that assist banks to form a competitive edge over their competitors.

ADVANCED RESEARCH

Still conducting further research to find out more about Financial Literacy as a Solution for Bank Marketing Myopia.

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