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Exponential growth bias and financial literacy

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Abstract

The tendency to underestimate the future value of a variable growing at a constant rate, an example of exponential growth bias, has been linked to household financial decision-making. We show that exponential growth bias and standard measures of financial literacy are negatively correlated in a representative sample of Swedish adults. Since financial literacy is linked to household decision-making, our results indicate that examining the relationship between exponential growth bias and household finance without adequate controls for financial literacy may generate biased results.

Keywords:

exponential growth bias

financial literacy

household finance

survey data

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Notes

Note: The views expressed here are the views of the authors in their capacity as researchers and do not represent the views of the Swedish Ministry of Finance.

¹ 'Suppose you invest 100 SEK and the interest rate is 7% per year. If you don't withdraw any money, how much money do you have in this account after 30 years?'

² We elicit exponential growth bias in a slightly different way from Stango and Zinman ([2009](#)). They construct their measure indirectly based on two questions, while we use the result of one question that directly measures the bias. This may explain why such a high fraction of their sample, 98%, is in this range.

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