70 percent of Americans can't answer 3 basic money questions

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Most Americans don't know the basics when it comes to money.

When economists Annamaria Lusardi and Olivia Mitchell conducted a three-question survey to see how much people really know about compound interest, inflation and stock risk, the results weren't great: Only 30 percent of respondents answered all three questions correctly.

"Financial literacy should not be taken for granted," Lusardi tells Stephen Dubner on a recent Freakonomics podcast. "Actually, if you ask me, we are at a crisis level."

Here are the three survey questions:

Question 1

Suppose you have $100 in a savings account and the interest rate is 2 percent per year. After five years, how much do you think you would have in the account if you left the money to grow?

A. More than $102
B. Exactly $102
C. Less than $102
D. I don't know

The correct answer is A. You'd have $102 after the first year. Over the next four years, interest will grow on that $102, meaning you'll have more than $102. It's a phenomenon known as **compound interest**.

Question 2

Imagine that the interest rate on your savings account is 1 percent per year and inflation is 2 percent per year. After one year, how much would you be able to buy with the money in this account?

A. More than today
B. Exactly the same as today
C. Less than today
D. I don't know

The correct answer is C: Less than today. "If inflation is two percent, prices go up two percent," says Lusardi. "But if you only earned one percent in your saving account, you basically can buy less."

Question 3

Do you think the following statement is true or false: Buying a single company stock usually provides a safer return than a stock mutual fund.

The answer is false. "A single company is a lot riskier than a basket of stocks," says Lusardi. "Don't put all of your eggs in one basket."

That's why experts like Warren Buffett warn against picking individual stocks. When it comes to investing, Buffett recommends low-cost index funds, which are highly diversified and tend to come with low fees.

If you answered all three questions correctly, you're in a distinct minority.

Lusardi and Mitchell note in their report that financial illiteracy is concentrated among certain demographics: "Those facing most challenges are the young and the old, women, African-Americans, Hispanics, the least educated, and those living in rural areas."

Perhaps the survey results are so dismal is because many young people are never taught money basics. Less than half of U.S. states require high school students to take a personal finance class before they graduate.

This lack of education appears to be taking a toll: Half of all Americans have nothing put away for retirement, 35 percent of all adults in the U.S. have only several hundred dollars in their savings accounts and 61 percent report that they don't have enough in an emergency fund to cover six months' worth of expenses.

To boost your financial literacy, check out the smartest things to do with your money in your 30s, a definitive guide to retirement savings accounts and the smartest way to invest your money.