# EARNING INVESTORS' TRUST AMID MARKET UNCERTAINTY

By Rhodri Preece

**The coronavirus crisis is placing severe pressures on public health, people's livelihoods and the functioning of economies as businesses adjust to simultaneous demand and supply shocks. The speed at which the developments unfold, along with uncertainty surrounding the timeframe and the severity of the economic impact, have made it hard for investors to price assets. As a result, markets are undergoing turbulence as prices adjust to unfolding developments, testing investors' confidence. How can financial firms and professionals build trust during times of crisis and beyond?**

During this time of heightened volatility, the need for trust in the institutions and advisers that act on behalf of investors, as well as the financial system in which they operate, becomes starkly apparent. Simply put, sound investment decision making is predicated on trust – it is the bedrock on which financial relationships and transactions occur. Having a trusted firm or adviser can help investors navigate through the uncertainty of this crisis and weather the economic storm.

In a new CFA Institute study, Earning Investors Trust, we analyse the dimensions of trust at the system, industry, and firm level. Trust is a multi-layered concept; it is dependent on information (the basis for decisions), innovation (the ability to meet investors' needs), and influence (the extent to which investors can exert control).

The study is built on a survey of 3,525 retail investors and 921 institutional investors across 15 different geographic markets. Importantly, half of retail investors and more than two-thirds of institutional investors surveyed believed their investment firms are well prepared or very well prepared to manage through a financial crisis. Investors with a trusted relationship with the firms and advisers that act on their behalf are much better equipped to navigate the market disruption.

At the system level, the proportion of respondents globally who expressed a high or very high level of trust in the financial services industry was 65% among institutional investors and 46% among retail investors, both of which were down slightly on 2018 levels.

Photo: Archive CFA Institute

Rhodri Preece

## CV

Rhodri Preece, CFA, is Senior Head of Industry Research for CFA Institute. He is responsible for building and maintaining the global research function at CFA Institute, including leading the planning, coordination, and creation of research content across CFA Institute research platforms, which include the Future of Finance, the CFA Institute Research Foundation, the Financial Analysts Journal, and the Enterprising Investor blog. Preece formerly served as Head of Capital Markets Policy EMEA at CFA Institute, where he was responsible for leading capital markets policy activities in the Europe, Middle East, and Africa region. Preece is a former Member (2014-2018) of the Group of Economic Advisers of the European Securities and Markets Authority (ESMA) Committee on Economic and Markets Analysis. Prior to joining CFA Institute, Preece was a Manager at PricewaterhouseCoopers LLP, where he specialized in investment funds.

However, there is a significant difference in trust levels among retail investors with and without an adviser; those with an adviser had much higher trust levels in financial services (57%) than those without an adviser (33%).

Trust levels in financial services also stand in contrast to the levels of trust among retail investors in the technology sector (60%) and in medicine (68%). Trust is hard-earned and easily lost, and it is clear that the financial industry has some way to go before it can earn the level of trust enjoyed by the medical profession.

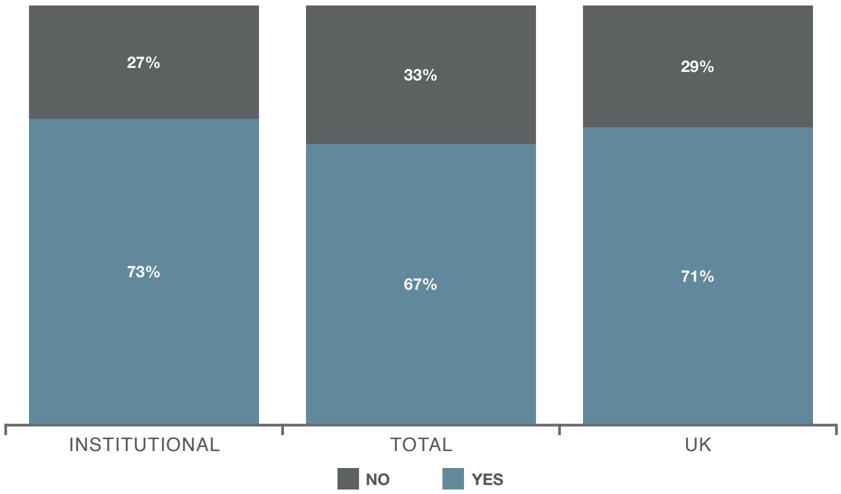
Among institutional investors, specifically defined benefit pension plan sponsors and state or government pension sponsors, 47% of respondents thought it was likely or very likely that their fund would need to adjust benefits downwards in the next 10 years (in contrast, only 11% thought this was unlikely).

In the United Kingdom, 60% of eligible beneficiaries expressed confidence that state-sponsored retirement benefits will pay out as promised, compared with 35% who did not have trust in state-sponsored retirement benefits. The results in the UK compare slightly less favourably than at the global level. Overall, these findings suggest that, as pensions systems come under increased strain from market dislocations and lower-for-longer interest rates, the investment industry may be accruing a deferred trust deficit on its collective balance sheet. In time, the industry will have to adjust to manage a potential markdown in goodwill.

At the investment industry level, we found that innovation and technology can have a significant bearing on the level of trust among investors. Approximately two-thirds of institutional investors and nearly half of retail investors with an adviser trust their investment firm more because of the increased use of technology.

However, investors still overwhelmingly trust advice from a person over advice from a machine, a view expressed by more than three quarters of UK retail investors.

**Figure 1: Would you be willing to give up some return for an investment strategy that meets your values-based objectives?**




Source: CFA Institute, Earning Investors Trust, 2020

Nevertheless, having access to the latest investment technology is increasingly expected to matter to investors in the coming three years.

At the firm level, trust among investors is shaped by their desire for influence and control over investment strategies and products. Fees remain an important criterion in this regard (to the extent that fees are known in advance, whereas investment outcomes are not), and 65% of institutional investors surveyed responded that they have renegotiated manager fees in the last year.

Demand for more customized investment solutions also reflects the desire for greater influence and control, and ESG (Environmental, Social, and Governance) products and strategies continue to grow. Institutional investors believe that ESG investing has increased trust in the industry.

*Institutional investors believe that ESG investing has increased trust in the industry.*

Our survey also showed that 73% of institutional investors and 67% of retail investors would be willing to give up some return in exchange for meeting their values objective.

Each of the dimensions of trust will be put under strain in the current market environment. To retain trust in this climate, investment firms and professionals should focus on the enduring elements of trust. These include maintaining credibility through building a track record, obtaining credentials, adhering to industry standards, and strengthening professionalism by continually improving knowledge, skills and abilities, combined with an ethical, client-centric professional orientation. Taken together, these elements can create value for investors and engender stronger client relationships that will endure market cycles. «

**This article was written by Rhodri Preece, CFA, Senior Head of Industry Research for CFA Institute.**