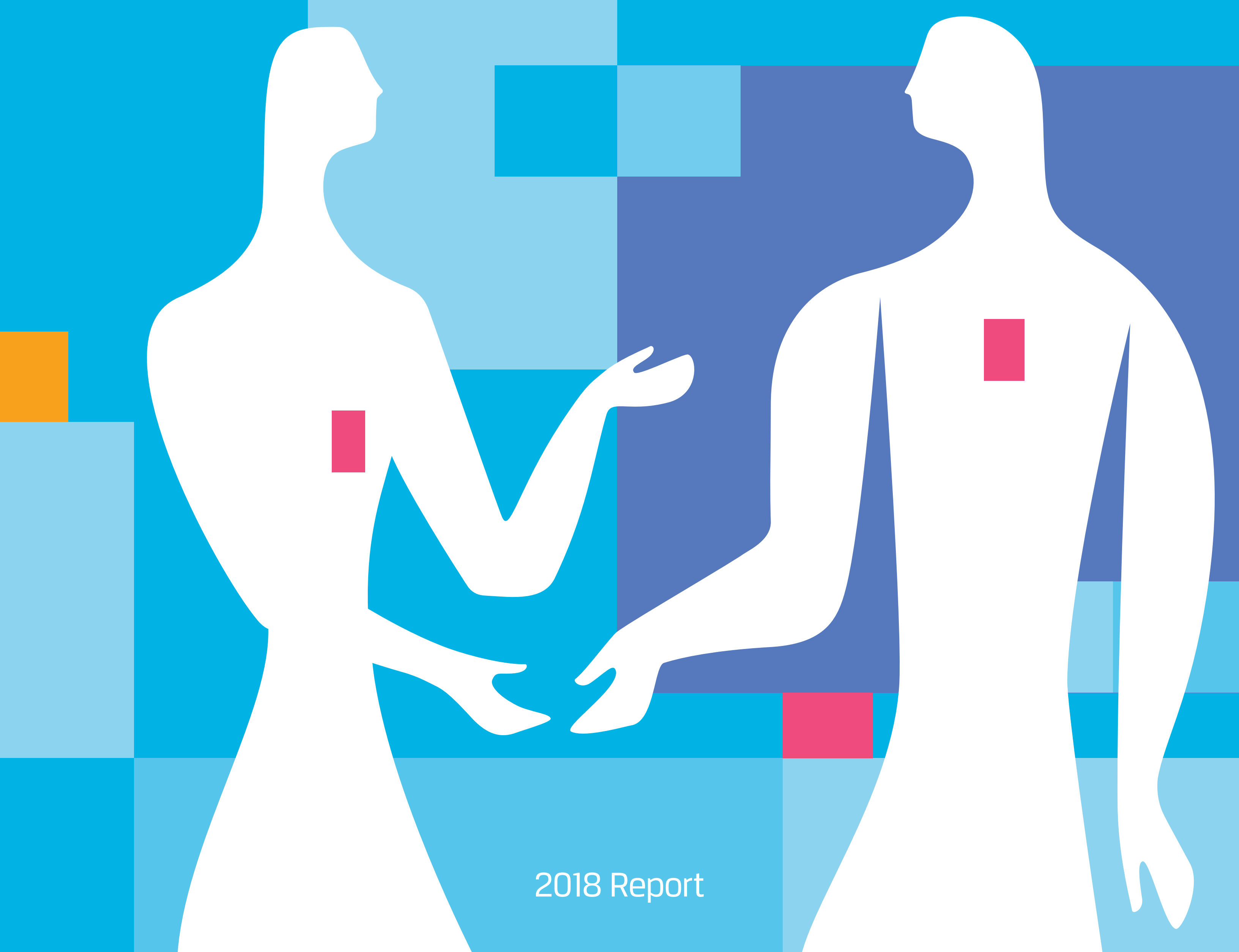
CFA Institute®
Future of Finance

THE NEXT GENERATION OF TRUST

A Global Survey on the State of Investor Trust



2018 Report

A NEW ERA OF INVESTOR TRUST

Investor expectations are changing. We studied these through the lens of trust in producing our third investor trust study. Ten years after the global financial crisis, we are seeing encouraging trends. While the 2018 Edelman Trust Barometer shows that trust in institutions is very low among the general population and the reputation of finance keeps it ranked relatively low among industries, the better-informed population—who are actual participants in the markets—have a more favorable view.

Our survey data, gathered by Greenwich Associates, finds that trust levels among investors—institutional asset owners and retail—have risen since 2016, but it is not all good news. With higher trust comes higher expectations, and among retail investors, the gap between what investors want and what we as an industry are delivering has widened. Just as we have seen polarization of trust across many industries, the investment industry must strive to relate effectively to individual investors and provide high service levels to them. We know this is possible since institutional investors report very high satisfaction with their asset managers.

Finance is democratizing—there is a transition to a state where finance is available to everyone. In this democratization process, we find some interesting opportunities for the investment industry in technology. Investors of every age are using technology more, and the smart use of technology increases their trust in the investment professionals with whom they work.

Demographically, we see significant shifts in the attitudes toward investing, with younger investors reporting higher trust levels and satisfaction in the financial industry. Thus, a pressing question is: Can the industry retain this level of trust as the increasingly influential millennials age?

Finally, we analyze the components of investor trust through the CFA Institute trust equation and offer recommendations for the industry to increase trust in terms of credibility and professionalism. While investment performance cannot be guaranteed, the other actions essential to building trust are very much within the industry's control. In an industry where revenues are now driven more by client retention than client acquisition, the bottom line value of trust should not be underestimated as a competitive advantage.

We hope you find the research that follows useful, as you seek to serve your clients effectively and navigate the next generation of investor trust.

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President & CEO

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Survey respondents

3,127 retail investors from 12 markets, 25+ years old, with investable assets of at least US$100,000

829 institutional investors, with assets under management of at least US$50 million

The Next Generation of Investor Trust

The nature of trust can be difficult to assess and quantify, but everyone knows we need trust to make society work. Nowhere is this more evident than in the world of finance, where well-functioning markets are necessary to create value, and in investment services, where experts work to safeguard and grow the financial wealth of their clients. In this—the third CFA Institute investor trust study—we analyze trends in investor trust and provide recommendations for investment practitioners on how to improve trust with clients. We find that the nature of trust is changing because of a new generation of investors and a new generation of investing technologies.

Key Themes

I. Trust in Financial Services Industry: Reputation versus Realities

While investor trust overall in financial services is only slightly higher, there are many positive signs regarding actual client experiences. Reputational issues for the industry remain, but there are ways investment professionals are effectively building and maintaining trust with clients.

II. The Bottom Line Value of Trust through the Client Life Cycle

Clients consistently rank trust as the biggest differentiator in hiring an investment adviser. Trust also contributes to whether a client will refer others or expand the relationship with additional mandates. Underperformance is the primary reason clients leave, but understanding client goals and fears are ways to build trust and weather uncertainty.

III. Technology Enhances Investor Trust but Does Not Replace the Need for Humans

Investors of all ages and regions want more technology applied to investing, and trust in technology is generally high. Effective use of technology increases trust in a financial adviser or firm, and blockchain holds potential for more trust in the system. For advice, however, people are much more trusted, and robo-advisers are the least trusted segment of the industry.

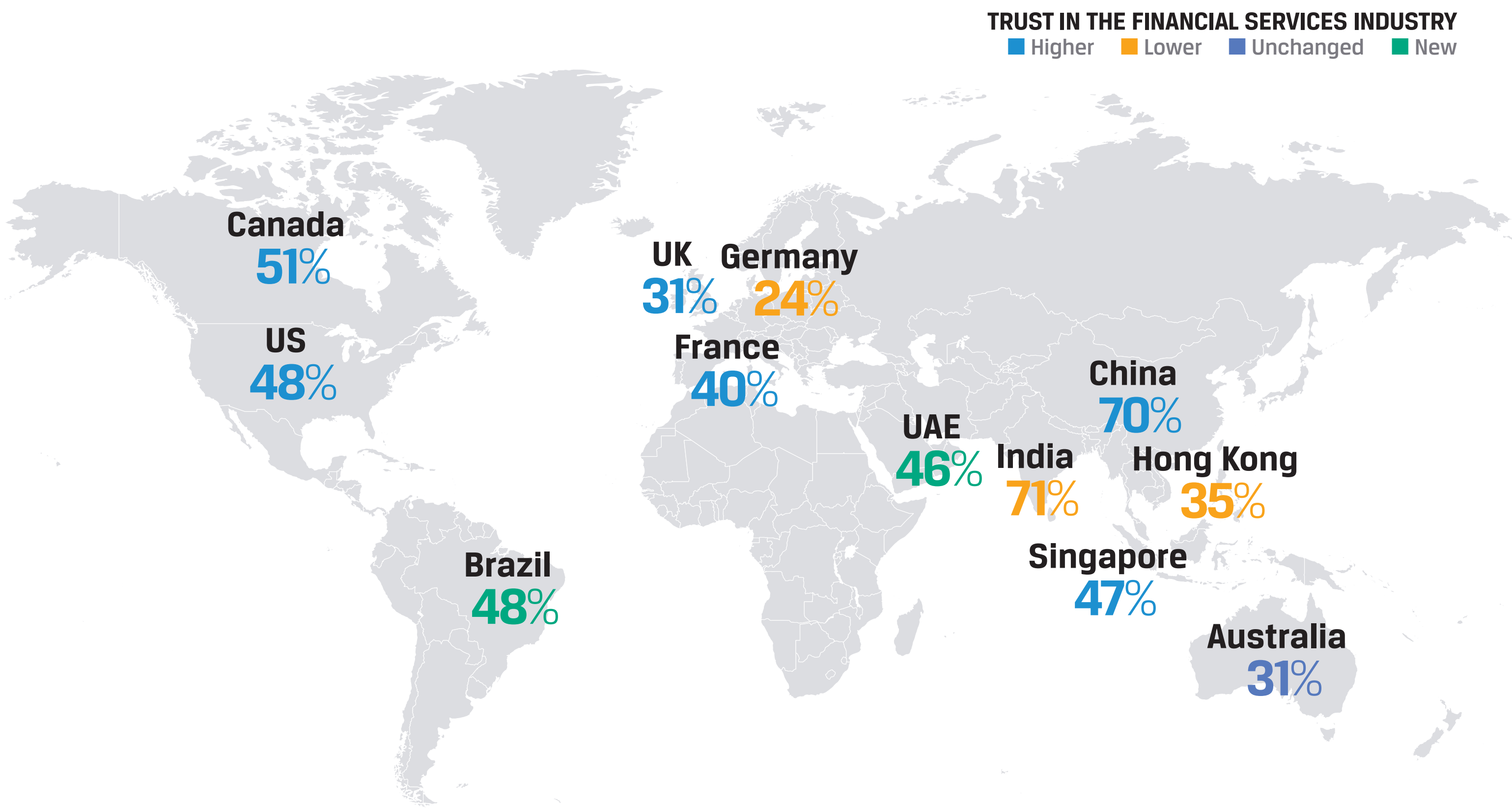
IV. The Trust Equation: Credibility and Professionalism

The trust equation gives investment professionals tools to build trust. Credibility is composed of easily observed factors such as track record, brand, credentials, and use of a code of conduct, and these are highly valued. Professionalism is more difficult to assess but is essential to trust, focusing on factors such as competency and values.

A STRONG FOUNDATION: TRUST IN THE SYSTEM OVERALL

Following the global financial crisis, there was a severe loss of confidence in the financial system overall, but ten years later, we find this is not the case among investors. Nearly two-thirds of institutional investors believe the financial system is appropriately regulated, and only 10% of retail investors disagree with the statement: "I have a fair opportunity to profit by investing in financial markets."

I. Trust in the Financial Services Industry: Reputation versus Realities

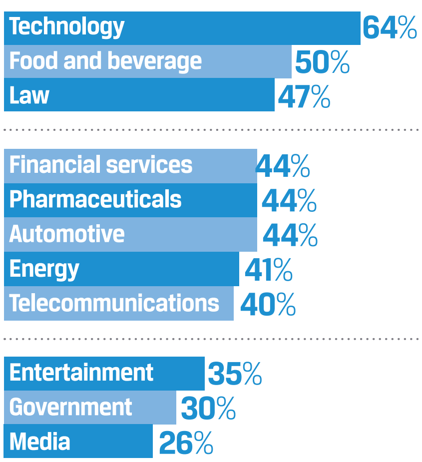


When we began our studies on investor trust five years ago, we knew that the reputation of the financial services industry was lackluster, but we hypothesized that its reputation was better among those who knew it best: investors.

This was not the case in 2013, when investors and the public alike were negative about the industry. Today, however, we see much greater distinctions between the *general view* of trust of financial services and the *personal view* of trust related to actual experiences.[1]

The *Edelman Trust Barometer* shows that trust in financial services has been rising in recent years, though among the public it remains stubbornly low versus other industries.[2] Among retail investors, there are three tiers of trust, and we find that financial services has moved into the middle tier—likely helped in part by recent strong market returns. Meanwhile, industries like the media and government are becoming actively distrusted, at levels double the distrust of financial services (about 40% vs. 20%, respectively). Technology continues to be the most trusted industry by a wide margin—a fact that represents an opportunity for financial services.

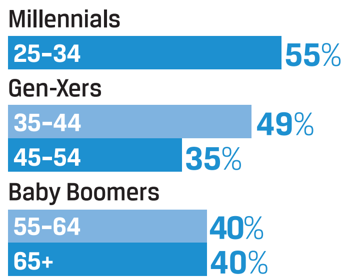
2018 RETAIL INVESTOR TRUST BY INDUSTRY



This year we focus on "high conviction trust," and this narrower definition of trust indicates the trust that is strong enough for investment firms to leverage for more profitable relationships.[3] We find that **44%** of retail investors trust financial services, while **35%** are neutral, and **21%** are distrusting of the industry. When compared to 2016, we find that financial services and the auto industry increased their trust ranking, while telecommunications and entertainment fell in the rankings. In addition, we now include law and government in the comparison industries. Trust is not given uniformly among markets or age groups. Trust levels were higher in most markets, but levels ranged from **24%** in Germany to **71%** in India.

Younger investors are more trusting of financial services than older investors are. This raises the question about whether trust is diminished over time and if the industry can find ways to maintain trust levels through the investor life cycle.

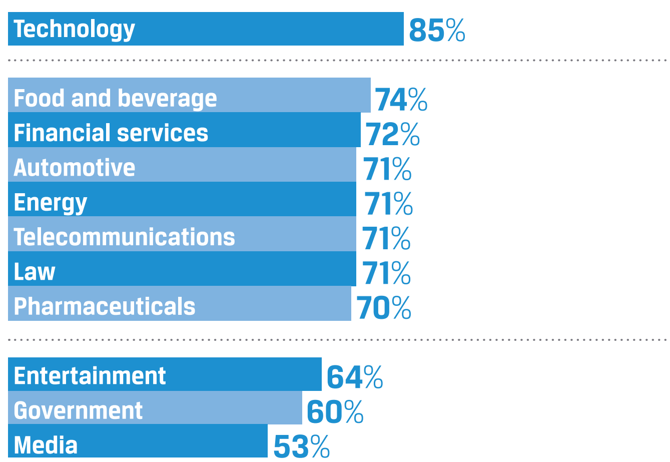
TRUST IN FINANCIAL SERVICES BY AGE



Institutional Investors Have Greater Trust in All Industries

Institutional investors are much more trusting of all industries than retail investors, and do not differentiate significantly among them. Like retail investors, however, they trust technology most and entertainment, government, and media least.

INSTITUTIONAL INVESTOR TRUST BY INDUSTRY



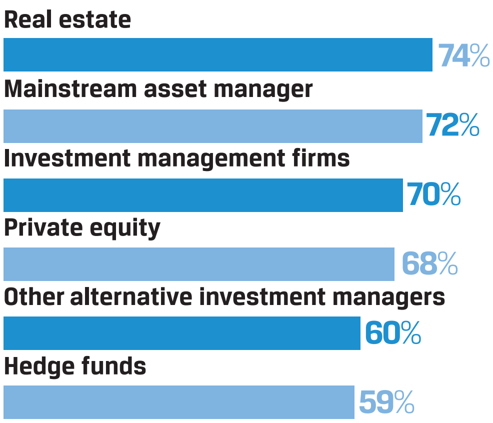
Within industry sub-sectors, **70%** of institutional investors trust investment management firms, though that trust varies among areas of investment management, with real estate trusted most and hedge funds the least.

1 For more discussion on the nature of trust, see Rachel Botsman, *Who Can You Trust?* (New York: Public Affairs, 2017).

2 Edelman, *2018 Edelman Trust Barometer* (New York, NY: Edelman, 2018).

3 In prior years, we considered trust as 6–9 on a 9-point scale. We now count 4 and 5 on a 5-point scale, which is similar to 7–9 on the old scale. This conversion has very little impact on the relative rankings of industries but eliminates about 20% of respondents who answered with "weak trust."

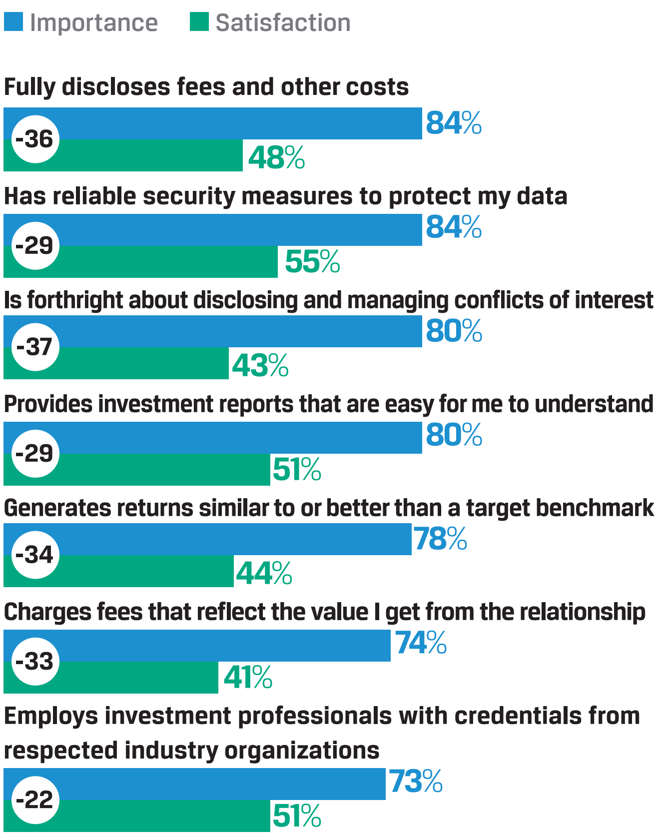
INSTITUTIONAL INVESTOR TRUST WITHIN FINANCIAL SERVICES



What Investors Want

Moving from the high-level indicators of industry trust, we asked respondents about seven specific actions investment firms could take to build trust. These were rated as very important in our 2016 study,[4] and this year expectations were even higher among retail investors. Meanwhile, satisfaction levels remained stable, leading to widening gaps of 20–30+ percentage points. The biggest gaps were related to disclosures, specifically about fees and conflicts of interest.

RETAIL INVESTOR EXPECTATIONS



Institutional investors' expectations were also high, but they are much more satisfied with their managers, likely because of higher service levels given their asset base. The most important factor to institutional investors is data security.

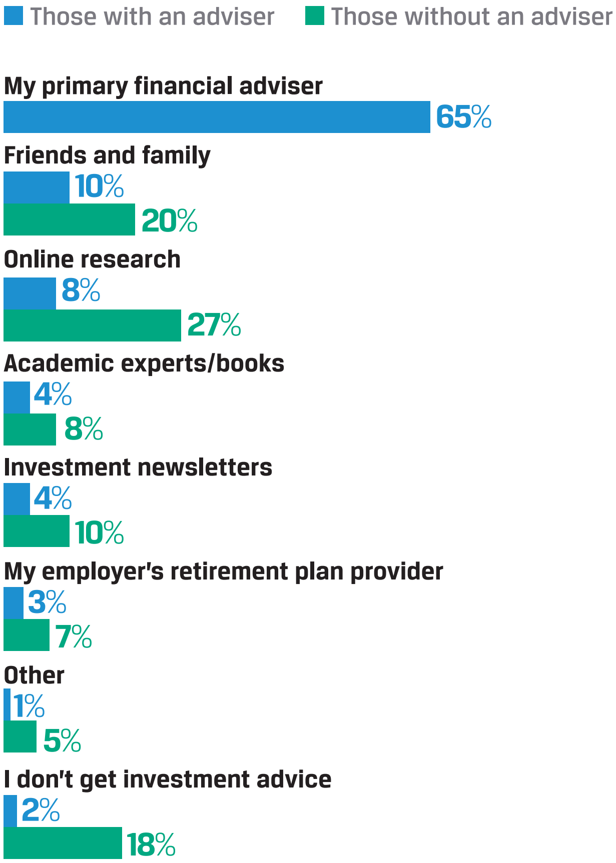
INSTITUTIONAL INVESTOR EXPECTATIONS

Client Experiences

Given the large divide in responses from retail and institutional investors, we looked more specifically at retail investors that have financial advisers, which represented just over half of the respondent base. First, we asked about their most trusted source of investment advice. Only 65% said that their adviser is their most trusted source of advice. The rest responded similarly to those without an adviser, who rely on online research, friends and family, and investment newsletters. In Asia, a much larger number of investors with an adviser rely on these alternate sources. Overall, nearly one-fifth of those without an adviser say they get no investment advice.

4 CFA Institute, *From Trust to Loyalty: A Global Survey of What Investors Want* (Charlottesville, VA: CFA Institute, 2016).

MOST TRUSTED SOURCE OF INVESTMENT ADVICE



When we looked at trust factors related to the actual client experiences, the results were positive. Most retail investors feel that their advisers are accessible, transparent, and fair. Eighty-three percent reported their advisers are accessible, although lower responses in Hong Kong and Singapore may be why they use alternative advice sources. Those whose advisers were more accessible were also more likely to trust the industry overall (54% vs. 30% trust levels).

In terms of transparency, most retail investors said their adviser was very or somewhat transparent around fees, market events, and other items, though less than half thought their adviser was very transparent around conflicts of interest. Regarding fees, 72% thought the fees they paid were fair, 10% thought they were unfair, and 18% were unsure.

DEFINITIONS

Trust

Trust from an end investor is the *dependency on a service provider in a situation of risk over a prolonged period.*

Trust in investment firms is far more complex and tacit than trust for almost any other product providers.

The importance of trust grows with risk and term of engagement.

In the investment industry, trust and value are interconnected.

For the end investor, value will relate to perceptions of outcome relative to expectations (*not* performance versus benchmarks).

Value and trust are shaped by building credibility and demonstrating professionalism.

Credibility

Credibility is reasonably tangible with objective features, which can be broken down into three parts:

Credentials: end investors need some assurance that their investment professional or organization is accredited to provide the service needed for success. Examples for an organization include regulations or a voluntary code like the CFA Institute Asset Manager Code, and the CFA® designation for investment professionals.

Track record: demonstration of value and trust proposition. It must be demonstrated that this individual or organization is able to add value and deserves trust; this includes performance track records and other factors relevant to the value proposition.

Brand: what the organization represents through its image, values, and capabilities, and how it lives up to this picture.

Professionalism

Professionalism, in contrast, is more tacit and has subjective elements:

Competency: the mix of competency attributes needed for an investment role varies; you can specify certain ever-critical skills and experiences (e.g., subject matter knowledge and problem solving), but each role has an additional contextual set.

Values: strong ethics and client-centric focus, such as empathy and loyalty in putting clients first, are the values needed by an investment professional or organization for trust to be granted.

II. Trust through the Client Life Cycle

Trust is an important factor when clients decide on a firm or adviser to hire, and it is an indicator of the health and term of the relationship—both for potential to expand it, or the risk of losing it.

Hiring

In each of our trust studies, retail respondents have consistently and overwhelmingly (by a 2-to-1 margin) chosen trustworthiness over investment performance as the top attribute when selecting a financial adviser. Trustworthiness is also a top attribute for institutional investors when selecting an investment manager, though they focus equally on ability to achieve high returns.

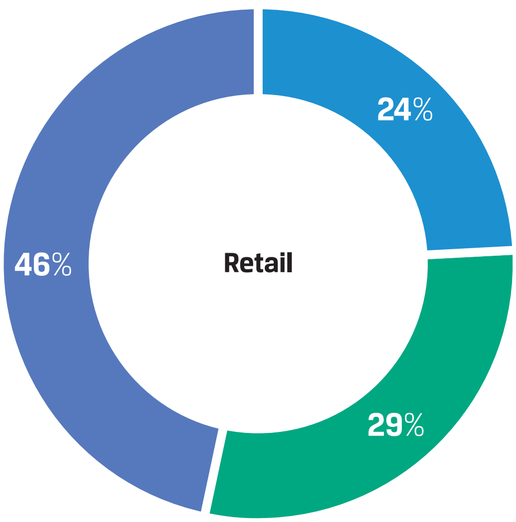
MOST IMPORTANT ATTRIBUTE WHEN HIRING FINANCIAL ADVISER/ASSET MANAGER

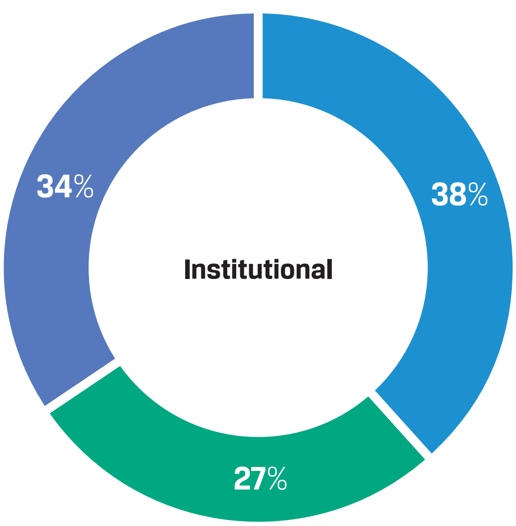
Maintaining Trust

How well trust is maintained within a professional relationship may depend on whether trust is earned or given. In some markets, trust is commonly assumed while in others it must be earned once or continuously over time. One-quarter of retail investors globally said they tend to grant trust from the outset, about one-quarter need initial proof of trustworthiness and then will give the benefit of the doubt, and about half say their trust must be constantly earned and maintained. Institutional investors are more likely to initially grant trust, though they typically have rigorous selection processes.

HOW DO YOU DETERMINE WHEN A PERSON OR BUSINESS IS TRUSTWORTHY?

- I assume they are trustworthy unless they prove otherwise
- Once they demonstrate they can be trusted, I will give them the benefit of the doubt going forward
- My trust must be constantly earned and maintained over time

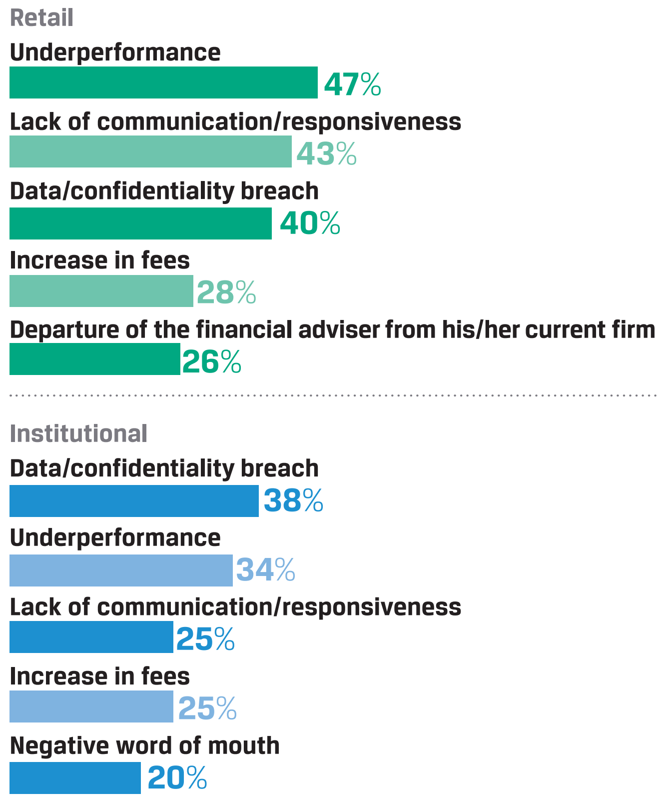




Retaining Clients

Trust maintenance must be connected to meeting client expectations, and for retail investors globally, the common reasons they leave their advisers are underperformance and a lack of communication or responsiveness. This means investment performance is more important for retaining clients than in getting new ones. A data or confidentiality breach is another significant reason retail investors give for leaving (40%), and for institutional investors, it has now outpaced underperformance as the top reason to leave an asset manager.

TOP 5 REASONS TO LEAVE AN INVESTMENT MANAGER



Expanding Relationships

Trust can also pay off in extending the relationship because two-thirds of institutional investors are planning to add to their manager lineups in the next one to three years, and the majority of these say they would prefer to work with a manager with which they already have a relationship. In addition, among retail investors, there is a correlation between those who trust finance and those who are likely to recommend their financial adviser.

Trust and Uncertainty

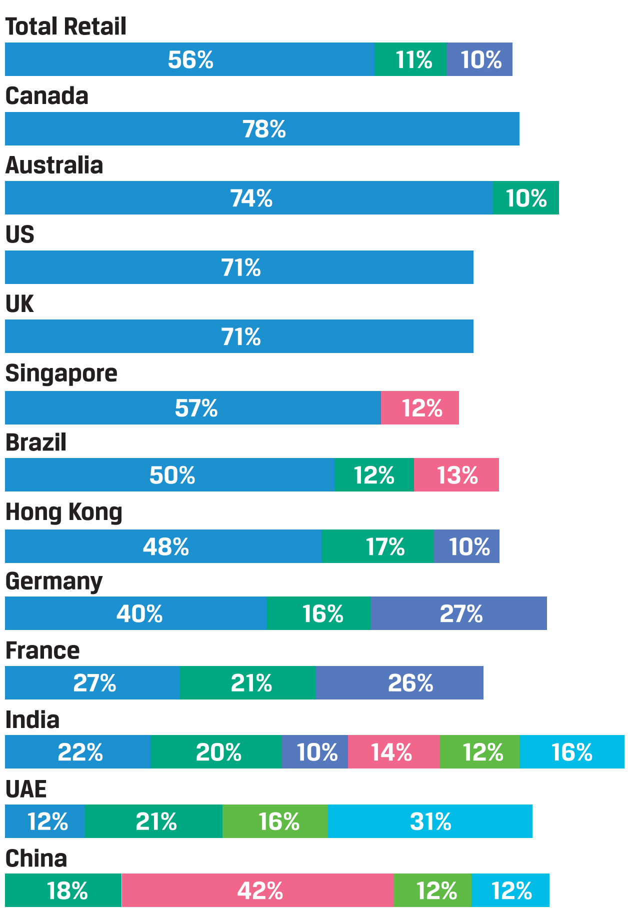
Uncertainty is a necessary ingredient to test trust, and with market uncertainty, those in financial services have plenty of opportunity to demonstrate trustworthiness. Investment professionals can proactively build trust by understanding the two primary motivations of clients: their goals and fears.[5]

Investment Goals

Investment goals can vary significantly by age group or geography. Retail investors in more developed markets are focused on reaching retirement, while in other markets, investors are investing to consume or to maintain financial security. It is important that the adviser defines investment success in the same way the client does.

RETAIL INVESTOR GOALS (ITEMS RANKED #1 BY 10% OR MORE OF RESPONDENTS)

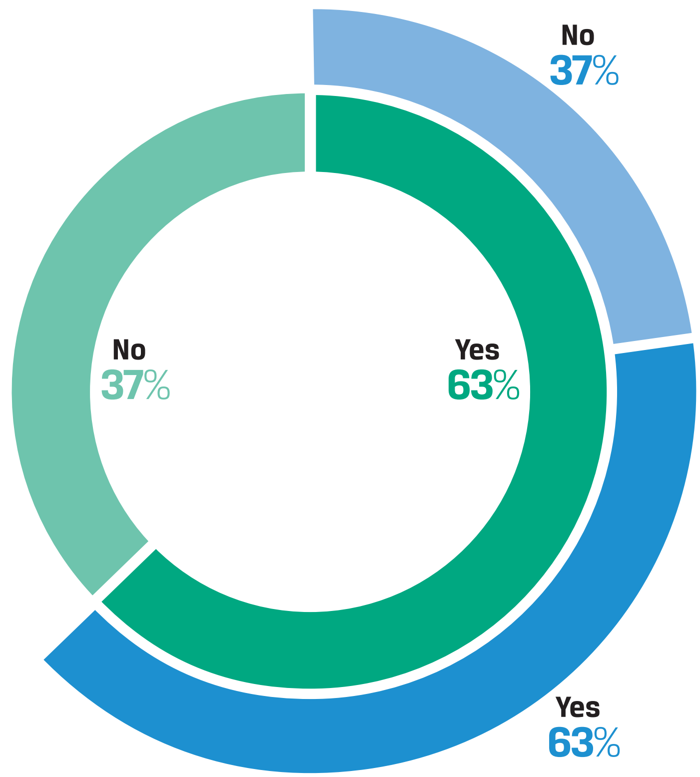
Retirement
Saving for large purchase (i.e. house, car)
Emergency funds
Beneficiaries/Estate Planning
Education savings
Saving to start a business



By understanding client goals better, firms have an opportunity to provide increased customization and personalization of products and services. This is in demand: the majority of retail investors responded they are interested in more personalized products and of these, a majority would be willing to pay more for them. This is consistent with the Parallel Worlds scenario of *Future State of the Investment Profession*, in which investment firms can provide greater value through customization.[6]

RETAIL INVESTOR INTEREST IN PERSONALIZED PRODUCTS

Interest in more personalized products
Willing to pay more for personalized products



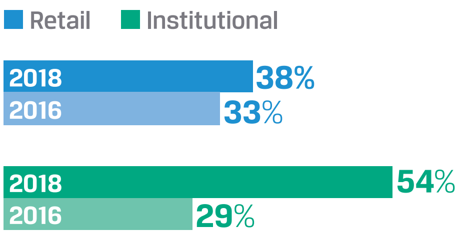
5 See State Street and CFA Institute, *Discovering Phi: Motivation as the Hidden Variable of Performance* (Boston, MA: State Street, 2016).
6 CFA Institute, *Future State of the Investment Profession* (Charlottesville, VA: CFA Institute, 2017).

Investment Fears

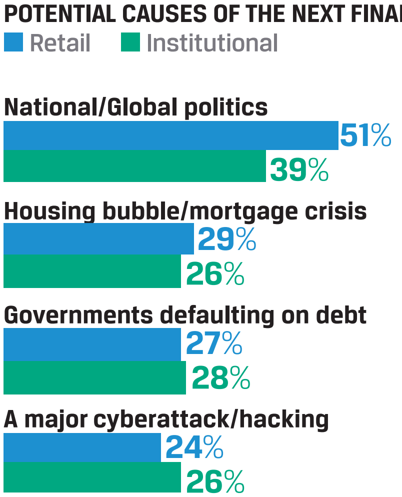
Retail investor fears are also related to their goals; thus, many have concerns about retirement-related issues, either a financial crisis that reduces the value of their retirement portfolio, or living past their wealth. Investors of all ages have similar concerns, although younger investors are also worried about missing out on investment opportunities.

These fears are not decades away either, as nearly **40%** of retail investors globally fear another financial crisis within the next three years. In the last two years, the expectation of a financial crisis has increased in all markets surveyed except India and France. The largest increases are in the US, the UK, and Hong Kong. Younger investors are also more concerned about an impending crisis in the next three years, with **48%** of investors age 24–34 deeming it very or extremely likely.

INVESTORS WHO BELIEVE A FINANCIAL CRISIS IN THE NEXT 1–3 YEARS IS LIKELY OR VERY LIKELY

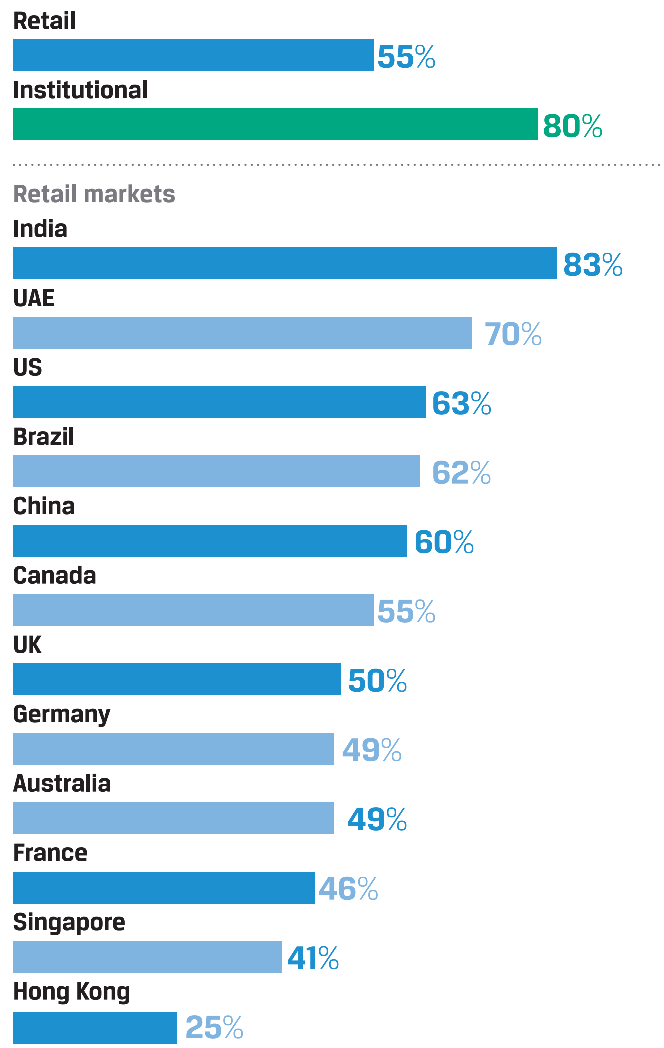


POTENTIAL CAUSES OF THE NEXT FINANCIAL CRISIS



Although the fear of a crisis is high, the good news is most retail and institutional investors think their advisers or asset managers are well positioned and prepared to meet the challenges a financial crisis may bring. An interesting element is whether the client holds the investment firm accountable during a crisis. Institutional investors seem to be more inclined to blame their investment firm, as **32%** said they would re-evaluate their investment firm based on performance through the crisis. Only **17%** of retail investors would re-evaluate their firm, which is down from **27%** in 2016.

INVESTORS WHO THINK THEIR INVESTMENT FIRM(S) ARE VERY WELL PREPARED OR WELL PREPARED FOR A FINANCIAL CRISIS

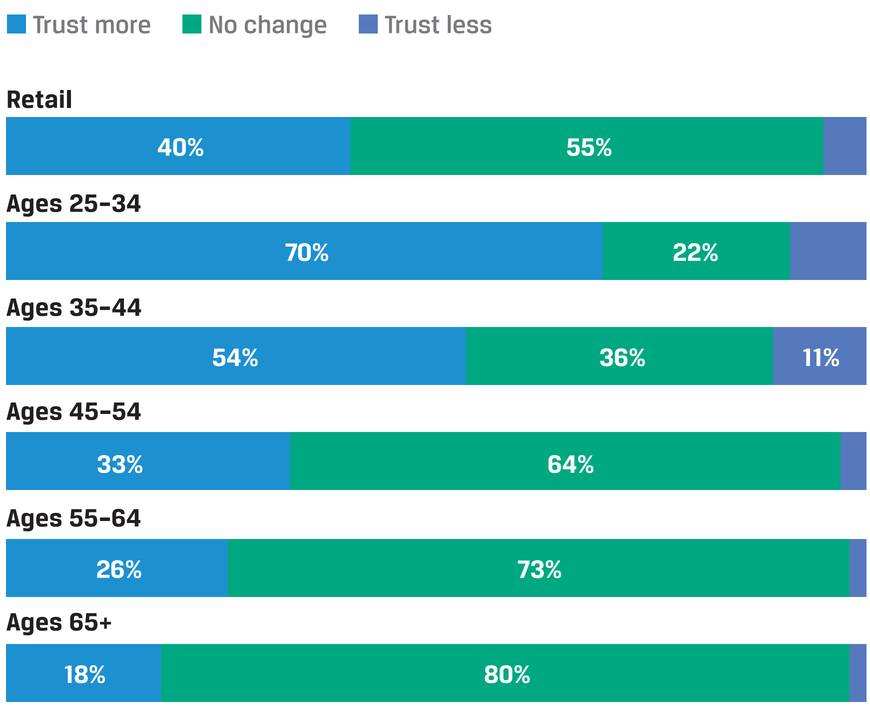


III. How Technology Impacts Investor Trust

Technology itself does not augment trust, but it can facilitate it. Technology enables professionals to provide investors with valuable information and services, in an efficient and consistent way, which can influence trust.

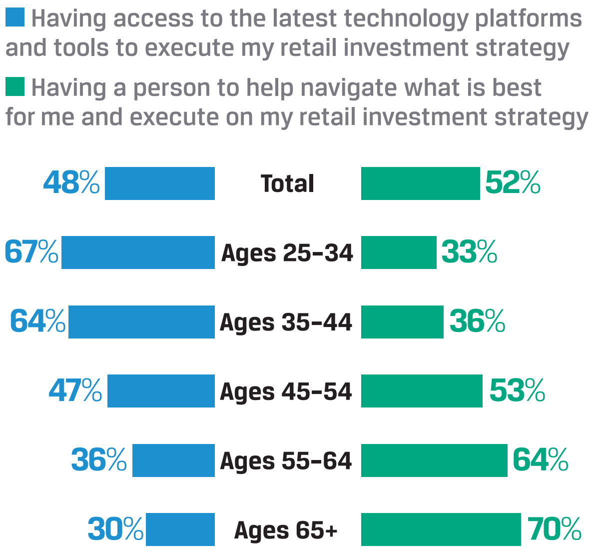
The survey suggests a strong link between use of technology by financial advisers and increases in trust, and this is especially true among younger investors.

HOW HAS THE INCREASED USE OF TECHNOLOGY IN FINANCIAL SERVICES CHANGED YOUR RELATIONSHIP WITH YOUR ADVISER?



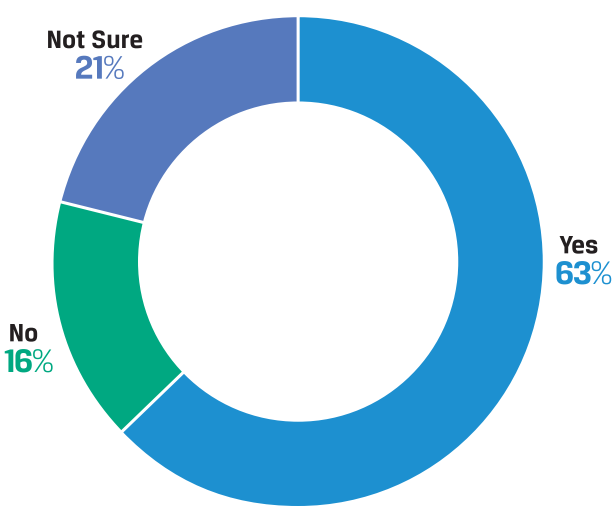
While technology facilitates trust most with younger investors, investors of every age are increasing their use of technology over time. Nearly half of all retail investors say that in three years, it will be more important to have tech tools to execute their own strategy than to have a person to help. In our 2016 survey, only China and India had a strong preference for platforms over people, but now seven of the twelve markets prefer tech. Those who still prefer humans include the US, Canada, UK, Australia, and Germany.

IN THREE YEARS, WHICH OF THE FOLLOWING DO YOU THINK WILL BE MORE IMPORTANT TO YOU?



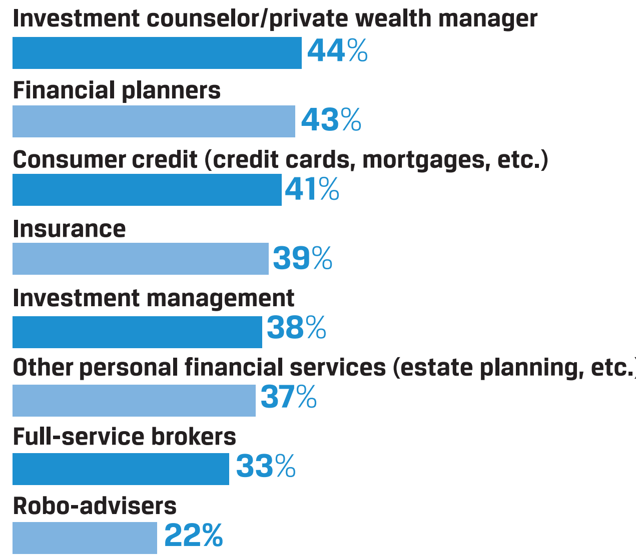
Developments like blockchain could accelerate the pace of change, and through a distributed transparent ledger, trust in the system could be strengthened by reducing reliance on counterparty organizations. Indeed, a majority of institutional investors think blockchain has this potential to increase trust in markets.

DOES BLOCKCHAIN HAVE POTENTIAL TO INCREASE TRUST IN INSTITUTIONAL INVESTORS?



There are two disadvantages to tech, however. The first is that technology is not yet trusted to give advice. Globally, 72% of retail investors say they are more likely to trust a recommendation from a human than from a robo-adviser. The subsectors within financial services that provide clients with more personal familiarity, such as financial planners, are more trusted, while robo-advisers are trusted least.

PERSONALIZED SUBSECTORS MORE TRUSTED BY RETAIL INVESTORS



The second challenge is cybersecurity. Some high publicity data breaches at US companies like Equifax and Target have created awareness of the issue, and while the tech sector continues to be highly trusted, a misstep around security has serious consequences. Investor expectations surrounding cybersecurity are high, and significant satisfaction gaps remain regarding the ability of advisers and asset managers to protect data consistently.

IV. The Trust Equation

In *Future State of the Investment Profession*[7], CFA Institute introduced a trust equation to outline some of the components of trust. In the equation, trust and value are a function of both credibility and professionalism.

Credibility, which is dependent on track record and experience, provides investors with confidence that the investment professional or organization is professionally accredited to provide the required service successfully. Credibility factors are relatively straightforward to assess and include reputation, brand, and credentials.

Professionalism is more subjective and much harder to assess. Professionalism factors include competency and subject matter knowledge, and values such as putting clients' interests first, empathy, and demonstrating a fiduciary mindset.

Credibility

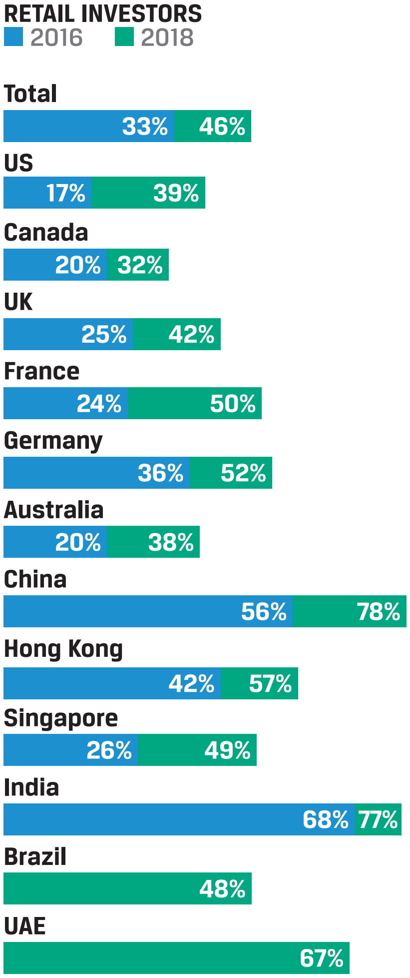
Credibility can be demonstrated and earned, but it can also be assigned by a trustworthy source. When asked to rank attributes needed in making a decision to hire a financial adviser, more retail investors globally chose *Recommended by someone I trust* (**18%**) than *Ability to achieve high returns* (**17%**).

Brand

Brand is also becoming a more important method of establishing credibility, and is increasingly a proxy for trust. As the investment industry gets more concentrated, there are dominant brands, and these firms will have an edge on trust. Brand, while it works as a shorthand for trust, may also be a weak substitute for strong personal relationships, as globally **46%** of retail investors say when considering an investment firm, a trusted brand is more important than "people I can count on."

7 CFA Institute, *Future State of the Investment Profession* (Charlottesville, VA: CFA Institute, 2017).

IMPORTANCE OF INVESTMENT FIRM BRAND TO RETAIL INVESTORS

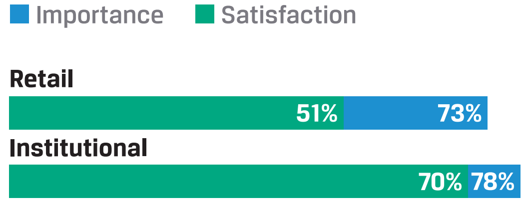


A more fundamental gauge of reputation and credibility for younger investors, brand is more than just advertising; it encompasses how people perceive and feel about a person or business. This makes relationship building more valuable, including community outreach, corporate social responsibility programs, and other types of philanthropy. In fact, **44%** of retail investors globally responded they would be more trusting of an adviser or firm that worked as a philanthropic partner for community efforts. Philanthropy as a trust enhancer was more important for some markets, specifically for **85%** of investors in China and **83%** of those in India. This was also the case for younger investors as reported by **68%** of retail investors from the ages of 24–34 and **62%** of those 35–44 years old.

Credentialing

Other methods of building credibility can lead to greater trust. Credentialing of professionals helps to increase confidence in a person's or a firm's ability to provide valuable services, so it is not surprising that having highly credentialed staff is important to **73%** of retail investors and **78%** of institutional investors. Similarly, **64%** of global retail investors said they would have greater trust in an investment firm that adheres to a voluntary code of conduct for the industry.

CREDENTIAL IMPORTANCE VERSUS SATISFACTION GAP



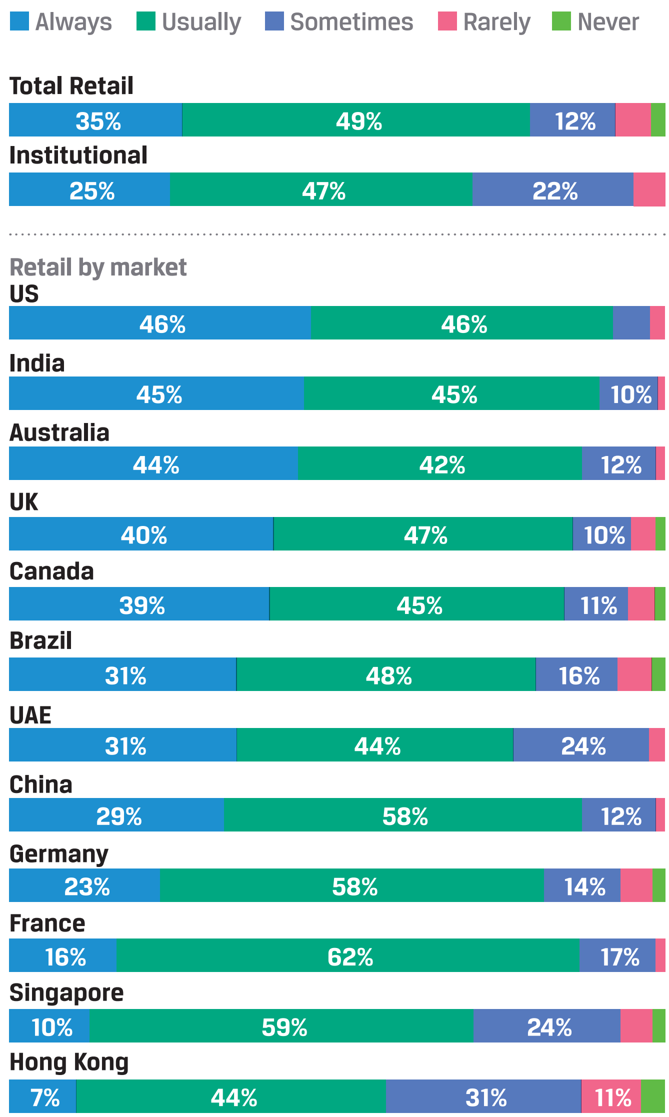
Professionalism

Professionalism encompasses values and competence.

Values

When considering hiring an adviser or firm, investors rated the values of *Trusted to act in my best interest* and *Commitment to ethical conduct* as a combined **40%** (institutional), and **49%** (retail investors). Given the importance of alignment of interests, it is concerning that only one-third of retail investors and a quarter of institutional investors think their investment adviser or firm consistently puts their interests first.

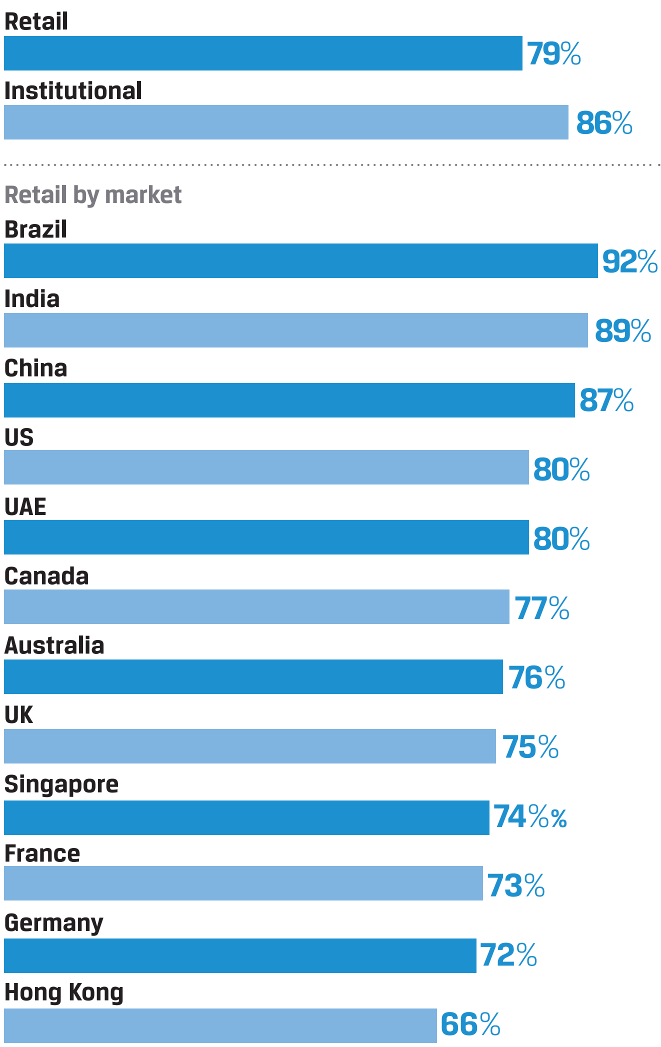
DOES YOUR INVESTMENT FIRM PUT YOUR INTERESTS FIRST?



Competency

Of course, values are not enough without the competency to accomplish the investment goals. When we asked institutional investors to rank attributes in terms of the competence of an asset manager, the most often selected was *Long-term track record* (**23%**). Continuing education is also an indicator of development and competency. In every market, a majority of retail investors agreed they would trust their adviser more if the investment staff performed continuous professional development.

TRUST MORE IF INVESTMENT STAFF DOES CONTINUOUS PROFESSIONAL DEVELOPMENT



8 Steps to Increasing Credibility and Professionalism

Credibility

1. Maintain strong brand identity and follow through on brand promises
2. Employ professionals with credentials from respected industry organizations
3. Stay focused on building a long-term track record to demonstrate competence
4. Adopt a code of conduct to reinforce your firm's commitment to ethics

Professionalism

5. Improve transparency and clarity regarding fees, security, and conflicts of interest
6. Use clear language to demonstrate that client interests come first
7. Showcase your ongoing professional development to improve investment knowledge
8. Demonstrate your dedication to the values that clients hold dear

Conclusion

The investment industry is competitive and changing quickly, but investor trust remains a foundational element for success. The good news is that actions and tools exist to increase trust. By knowing investors' goals and fears, investment professionals can serve them better and provide more customized products and solutions. Firms can address the components of the trust equation—credibility and professionalism—and they should use technology to enhance trust. In turn, these actions will create a more professional industry—one that is worthy of greater trust from current and future investors and that has the capacity to build greater wealth and well-being as a result.

ABOUT THE SURVEY

The Next Generation of Trust data collection was conducted by research firm Greenwich Associates and consisted of a 15-minute online survey conducted in November and December 2017.

The survey sampled 3,127 retail investors 25+ years old and with investable assets of at least US$100,000 in the US, Canada, Brazil, UK, France, Germany, UAE, Australia, India, Singapore, China, and Hong Kong. It also sampled 829 institutional investors with assets of US$50 million or more in these markets. The margin of error for total retail investors is ± 1.9%; the margin of error for total institutional investors is ± 2.1% at a 95% confidence level. CFA Institute encourages you to share the survey and related data available at **nextgentrust.cfainstitute.org.**

ABOUT US

CFA Institute is the global association of investment professionals that sets the standard for professional excellence and credentials. The organization is a champion for ethical behavior in investment markets and a respected source of knowledge in the global financial community. The end goal: to create an environment where investors' interests come first, markets function at their best, and economies grow. There are more than 150,000 CFA® charterholders worldwide in 165+ countries and territories. CFA Institute has eight offices worldwide and there are 151 local member societies.

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