

## WEALTH &amp; INVESTING

## CFA SINGAPORE INSIGHTS

By CFA Singapore Advocacy Team

# Trust is integral to keep wheels of financial markets turning

Investment professionals can serve their clients better by addressing the key components of credibility and professionalism

**M**OST people would agree that trust is difficult to gain, easily broken and once broken is tough to rebuild. Nowhere is this more evident than in the world of finance and in investment services where trust is integral in keeping the wheels of the markets turning. Following the global financial crisis, there was a severe loss of confidence in the financial system overall (for various reasons such as allegations of mis-selling, collapse of asset prices, closure of firms and bailouts of financial institutions using tax payers' monies), and it has taken years for confidence to be restored.

## What is 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 terms 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). And value and trust are shaped by building credibility and demonstrating professionalism.

## Maintaining trust

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

## 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 clients' two primary motivations: their goals and fears.

## Investment goals

Investment goals can vary significantly by age group or geography. Retail investors in more developed markets like Singapore 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.

## Investment fears

## 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 organisations
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

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

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 many retail investors globally fear another financial crisis is on the horizon and expect their advisers or asset managers to be well positioned and prepared to meet the challenges it may bring. An interesting element is whether the investment firm holds itself accountable during a crisis. With the global spread of Covid-19 virus, perhaps investment managers need to look even more closely at protecting clients' portfolios especially after the stock market blood-bath on March 9.

## Trust equation, a toolkit to build trust

The CFA Institute introduced a trust equation to outline some components of trust. The trust equation can be seen as a tool kit to build trust. In the equation, trust and value are a function of both credibility and professionalism.

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

**Brand:** Brand is also becoming a more important method of establishing credibility, and is increas-

ingly 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.

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.

**Professionalism:** This 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. Professionalism encompasses values and competence.

**Values:** When considering hiring an adviser or firm, investors do rate the values of "trusted to act in my best interest" and "commitment to ethical conduct" as important. Given the importance of alignment of interests, it is important for investors to believe that their investment adviser or firm consistently puts their interests first.

**Competency:** Values are not enough without the competency to accomplish the investment goals – institutional investors tend to place long-term track record as a very important attribute when deciding to hire an asset manager. Continuing education is also an indicator of development and competency. In every market, many retail investors would trust their adviser more if the investment staff performed continuous professional development.

**Credentiaing:** Other methods of building credibility can lead to greater trust. Credentiaing of professionals helps to increase confidence in a person's or a firm's ability to provide valuable services, so having highly credentialed staff is important to retail investors and institutional investors. Similarly, many global retail investors said they would have greater trust in an investment firm that adheres to a voluntary code of conduct for the industry.

## 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. Firms can address the components of the trust equation – credibility and professionalism. 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.

*This article has been adapted from CFA Institute Future of Finance's "The next generation of trust".*

⇒ The writers are CFA Charterholders who volunteer with the Singapore society on advocacy issues with a view towards promoting financial literacy among retail investors and improving overall standards and integrity in the industry. Should you have comments and feedback, do write to the CFA Society Singapore Advocacy Committee: [advocacy@cfasingapore.org](mailto:advocacy@cfasingapore.org)