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INSIGHTS FROM CFA SOCIETY SINGAPORE

Who should investors ultimately trust to protect their interests?

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LAST year, CFA Institute issued its biennial global report on trust. In that survey, only 36 per cent of investors had trust in the Singapore financial sector, down from 47 per cent two years earlier. This alarming fall prompted us to delve deeper into the data released by the global body for investment management professionals.

We held focus group discussions and interviews with retail investors as well as dialogues and presentations with financial institutions in a bid to uncover reasons for the slide in trust levels. This culminated in a trust report specific to the Singapore market.

In the recently released report, *Trust in Singapore's Financial Services Industry – Are We At Rock Bottom Yet? Where Next?*, we believe investors' faith in capital markets is influenced by a wide array of factors. Chief among them is returns, unsurprisingly so, especially when it comes to safer or blue-chip risk assets such as bonds widely followed or held by institutional investors. Real estate investment trusts (Reits) were another perceived safe haven, offering stable yields in a low interest environment.

Yet, incidences of significant capital loss in these so-called blue-chip risk assets have occurred and have consequently eroded trust in the financial sector.

Variety is the spice of life, some say. Yet, the smorgasbord of financial products on display can be bewildering for many, and trust can easily get lost here. Soon, special purpose acquisition vehicles (SPACs) will join the spread of financial products. While cognisant that SPACs will provide firms with another avenue to raise capital and draw attention to our capital markets, less sophisticated investors might want to be picky here.

In a consultation paper response to the Singapore Exchange in April, we wrote: "it is difficult even for seasoned investors to figure out the dilutive nature of the terms of SPACs. Issuers may consider providing illustrations on how dilution may occur under different redemption scenarios – say, at 10, 25, or 50 per cent – or a combination of redemptions and private investment in public equity deals, and under other terms, such as forward purchase agreement or side deals. The disclosure should explain how that dilution may impact post-merger returns. We are concerned that boilerplate disclosures would only confuse rather than inform investors".

While SPACs will not be deemed as blue-chip risk assets, we are cognisant that investor trust levels will take another hit if there is any high profile blow-up in this segment. We believe that market development of SPACs should be balanced with investor protection and good corporate governance. Without such balance, there is potential for poor investor experience souring not just future SPAC issuances, but investors' faith in capital markets as a whole.

Ultimately, investors should count on themselves. There is no better person or organisation than investors themselves to protect their own interests. The best way to do so is through financial literacy. Being financially literate is as important, if not more so, as a robust regime of rules and regulations, or a reliance on the ethical behaviour of financial professionals.

Educate yourself

There are still investors who do little research, if at all, to understand investment products before committing a sizeable amount into a financial product or risk asset. Some take positions based on rumours, hear-say, or on a whim. Insufficient research may be due to time constraints imposed by work and family schedules.

Some others are beneficiaries of sizeable inheritances or are successful entrepreneurs, but this does not mean that they have the requisite financial literacy to understand the bewildering array of financial products.

Many do not fully understand how the products can be affected by extreme events; or they fail to examine the fees levied, despite financial advisers' willingness to spend time on a thorough explanation.

Taking positions without adequate understanding and research is a recipe for disaster, and advisers and financial experts have repeatedly warned investors against doing so. Scams and misrepresentations aside, investors must realise that the blame falls squarely on their shoulders for investments gone awry.

When investors have advisers from different financial institutions, there is a natural tendency to compare performance between advisers. However, many do not realise that some facets of comparison are spurious. PHOTO: PIXABAY

Other benefits of financial literacy

In our view, investors have the ability to differentiate the quality of advisers (despite not having work experience in the financial sector). An educated investor is also better able to understand, differentiate, and assess the different product offerings including complex products to suit their unique circumstances and needs.

Yet, when investors have advisers from different financial institutions, which is not uncommon, there is a natural tendency to compare performance between advisers. However, many do not realise that some facets of comparison are spurious.

For example, advice on an equity fund should not be compared to advice on a high-yield unrated corporate bond, as the risk and return profile is different. It is more meaningful to compare advice on two equity funds with similar characteristics.

Similarly, a developed country play has different characteristics from a developing market risk asset, and they should not be put next to each other for comparison purposes. Improving one's understanding of finance enables one to ask the right questions for clarification, comparison and further understanding of products.

Other important benefits include an understanding of the difference in responsibilities of financial professionals. In a fiduciary relationship, the adviser has to look into the aspects of suitability and not just explain the features of the product. An adviser in a fiduciary relationship should not propose a high-return, high-risk product to a client who does not have an understanding of complex products or the ability to take on such risks. Lower-risk products may be deemed be suitable. This duty of examining suitability does not apply to sales personnel who is merely tasked to explain the products thoroughly. Investors should be cognisant of these differences.

There are many avenues to gain financial literacy, from materials at the public libraries and courses, to webinars and online materials. These resources are comprehensive and cater for various learning styles.

In short, the best way to protect oneself is through financial literacy. There is simply no excuse not to get educated with diverse offerings in Singapore.

The article is adapted from the recently released trust report: *Trust in Singapore's Financial Services Industry – Are we at Rock Bottom yet? Where Next?*

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