Global Financial Crisis Survey Report 7th September 2009

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Overview

From December 2008 to July 2009, FinaMetrica surveyed advisers and their clients regarding the impact of the Global Financial Crisis (GFC).

The preliminary analysis confirms some accepted wisdom but also reveals some surprises, three of which are:

- Clients appear to have an unrealistic expectation that their adviser can protect them from the vagaries of the market,
- Given the market's relatively recent history, advisers appear to have been too surprised by the market falls.
- Incontrovertible evidence of the stability of risk tolerance which, though not a surprise to us, does disprove accepted wisdom. However, this may provide an opportunity for the wider advisory community as explained in the report.

The survey sought information about:

- the extent to which the market falls were within clients' and advisers' ranges of expectations,
- the effects on clients' finances and the achievement of goals,
- clients' and advisers' current perceptions of market risk and the economic climate,
- clients' investment intentions, and
- the impact of market falls on risk tolerance.

The data collected, stripped of adviser and client names, will now be made available to our panel of academic researchers for detailed analysis.

Data Collection

FinaMetrica subscribers were asked to participate,

- by completing the Adviser Survey (Appendix A), and
- by asking their clients to complete the Client Survey (Appendix B) and to redo their FinaMetrica Risk Profiles.

We readily acknowledge that the very fact of the GFC, which presented a once-in-a-lifetime research opportunity, made it a difficult time for advisers to be asking more of clients.

We are very appreciative of those advisers who did participate. To encourage participation we offered ten US$100 Amazon gift vouchers dawn by lottery with each adviser having one 'ticket' per client completing the survey. The winners have been notified.

Overall, 174 advisers and 445 clients participated, as follows

Advisers

Country	Number	Percentage
AUS	30	17%
CAN	5	3%
NZ	6	3%
UK	49	20%
US	81	47%
Other	3	2%
Total	174	100%

Clients

Country	Number	Percentage
AUS	97	22%
CAN	4	1%
NZ	10	2%
UK	83	19%
US	227	51%
Other	24	5%
Total	445	100%

Detailed summaries of the data are set out in Appendices C (advisers) and D (clients).

On a month-by-month basis, client data was collected as follows,

December	January	February	March	April	May	June	July	Total
23	38	73	109	121	59	10	12	445

We were able to match 432 client surveys with an adviser and 368 with a current risk profile, and of these 368 we were able to find a previous risk profile for 251.

In a separate analysis of our complete database, we were able to find two risk profiles for 8,163 clients and three risk profiles for 730 clients.

Initial Analysis

Global Financial Crisis

The current crisis has had a global impact but the impact on markets has differed from country. However the difference has been one of degree rather than order of magnitude as can be seen in Figs 1 and 2. The charts in Fig1 and Fig 2 have been prepared from these indices.

Australia:	AFR - XAO All Ordinaries
Canada:	S&P/TSX Composite Total Return
New Zealand:	NZSX 50 Benchmark Index
United Kingdom:	UK FT-Actuaries All-Share Total Return Index
United States:	S&P 500 Total Return

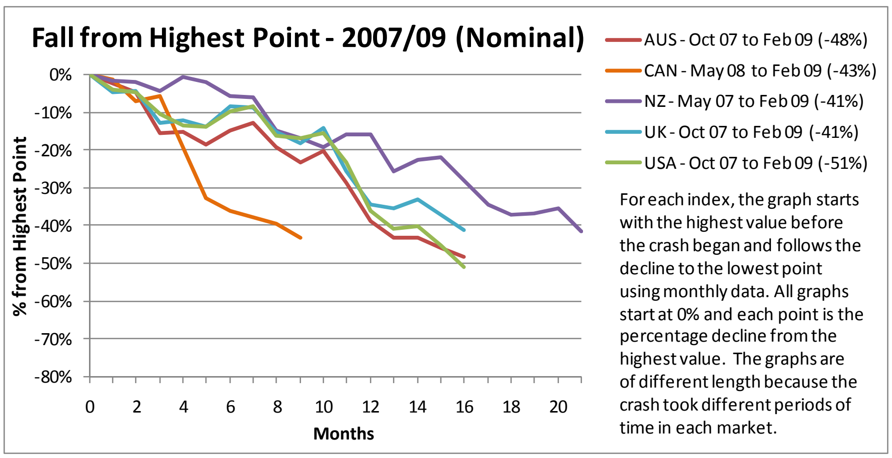

Fig 1

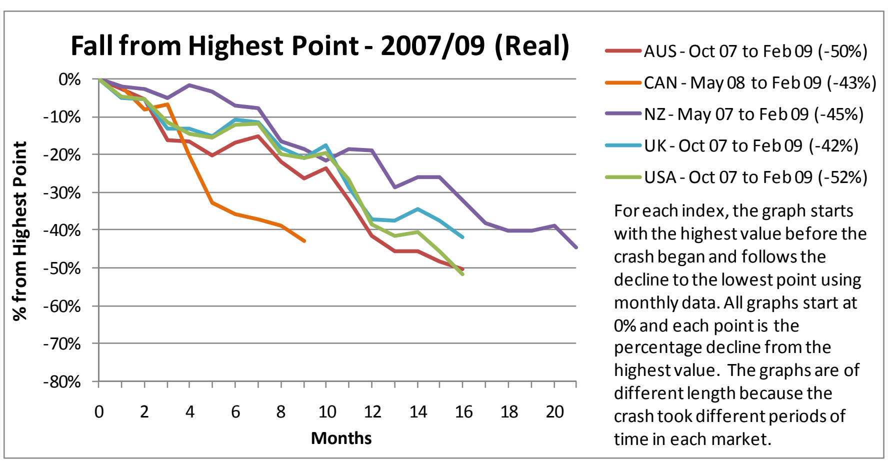

Fig 2

Despite the similarities in the size of market falls, we did notice some differences in mood from country to country as we visited the US and the UK and in feedback from our subscribers.

The mood in the US was the gloomiest by far. Many Americans' confidence had been severely dented by the demise (or near demise) of many iconic corporations and the collapse of the housing market; and many felt betrayed by Wall Street as executives continued to pocket huge bonuses while investors' lifetime savings disappeared.

Surprisingly though, the mood in Australia was not far behind despite the relative health of our economy, our government solvency, the strength of our banks and only a mild, by comparison, fall in the housing market. Perhaps this was due to the fact that we had escaped the dot com crash and the Asian crisis and had not seen a severe market fall since 1987, so this fall was almost completely unexpected by those who drew their market understanding from the past 20 years.

The UK appeared to us to be the least gloomy, though certainly having more to be gloomy about than Australia. It may be that this is a reflection of British stoicism.

Survey Data

Clients

To date our analysis has been of single variables. We will do some simple multiple variable analyses which we will report on in due course. However, the 'heavy duty' multivariate analysis will be done by our panel of academic researchers.

Some interesting information has emerged.

There can be no doubt that the GFC has had been bad news for clients, Fig 3.

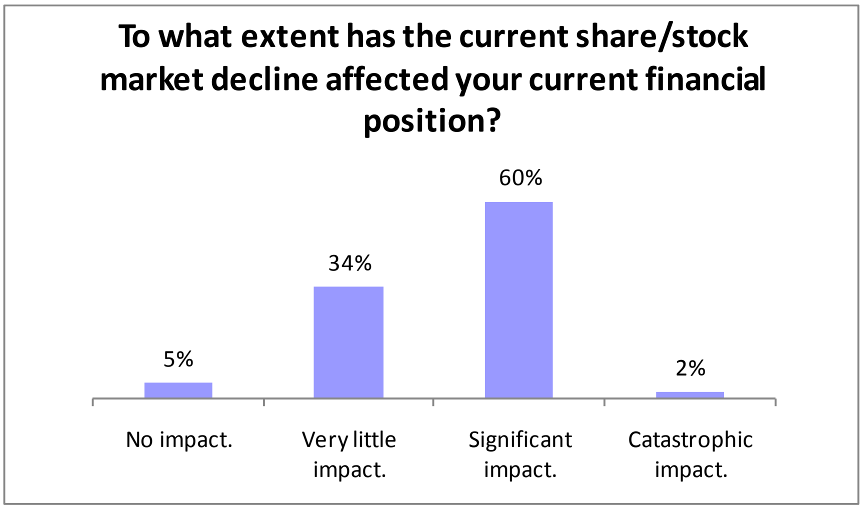

Fig 3

Clients were also surprised by what happened to their investments, Fig 4.

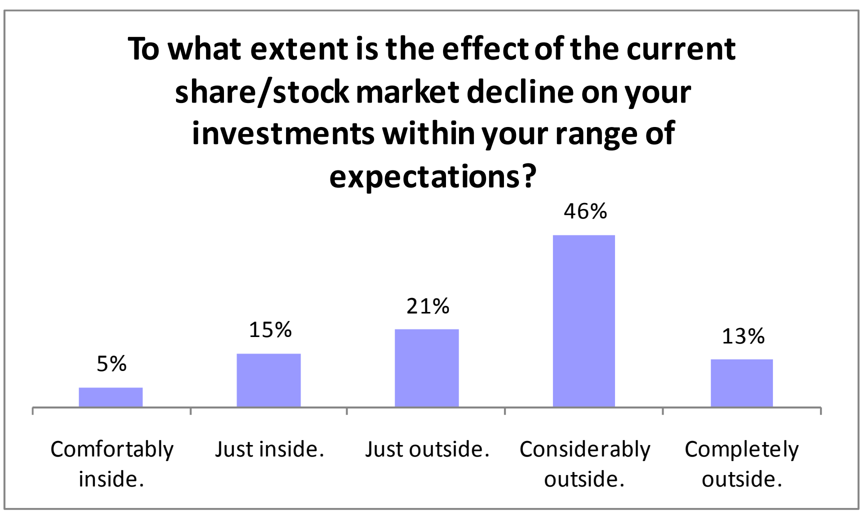

Fig 4

Interestingly, clients seem less surprised by what happened in markets, Fig 5.

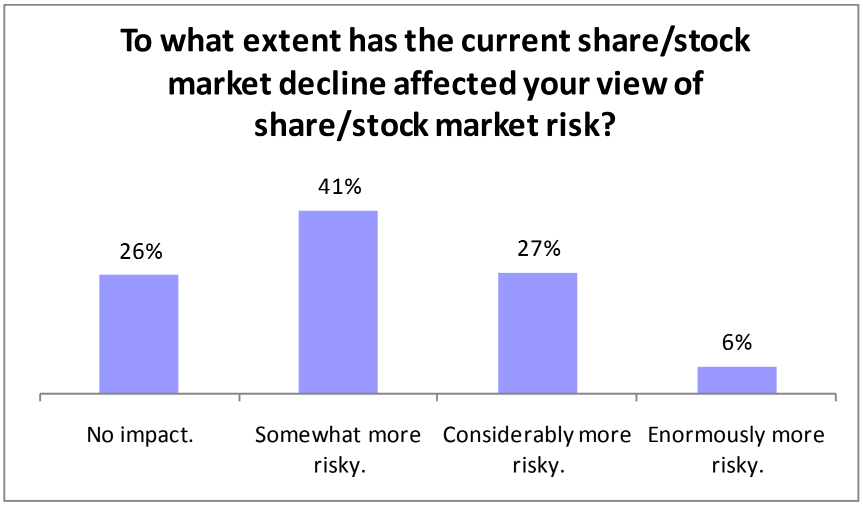

Fig 5

While the wording of the two questions in Figs 4 and 5 does differ, for 59% the effect on their investments was at least considerably outside their expectations, whereas only 33% believe the share market is at least considerably more risky than they had thought. This suggests that clients were expecting their advisers to protect them from the vagaries of the share market somehow. It is a reminder to advisers to be careful about how they describe their value offering to clients. Even so, no matter how careful advisers are some clients will want to believe that their adviser offers special protection.

Not surprisingly, clients' ability to achieve their long term goals have been affected, Fig 6.

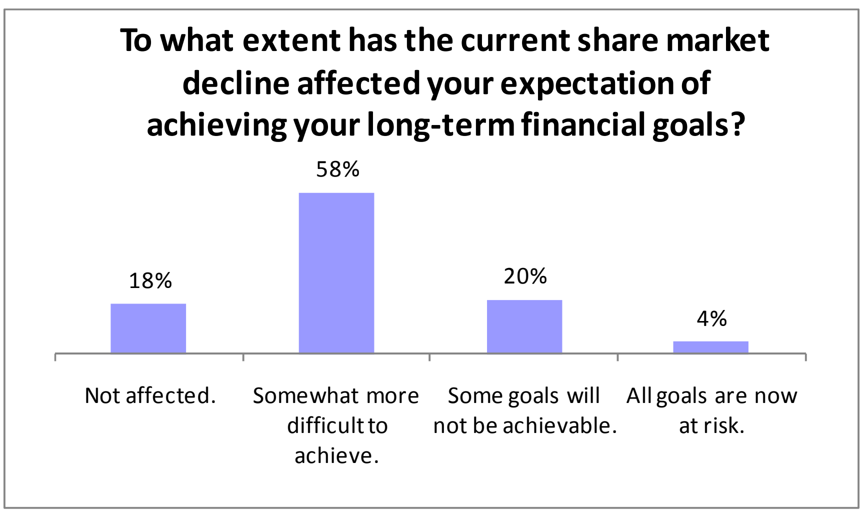

Fig 6

However the picture could have been bleaker than it is. Given the magnitude of market falls, the fact that for 76% of clients their long term goals are, at worst, only somewhat more difficult to achieve reflects well on the quality of advice they received.

Perhaps this might explain the lack of panic evident in their intentions, Fig 7.

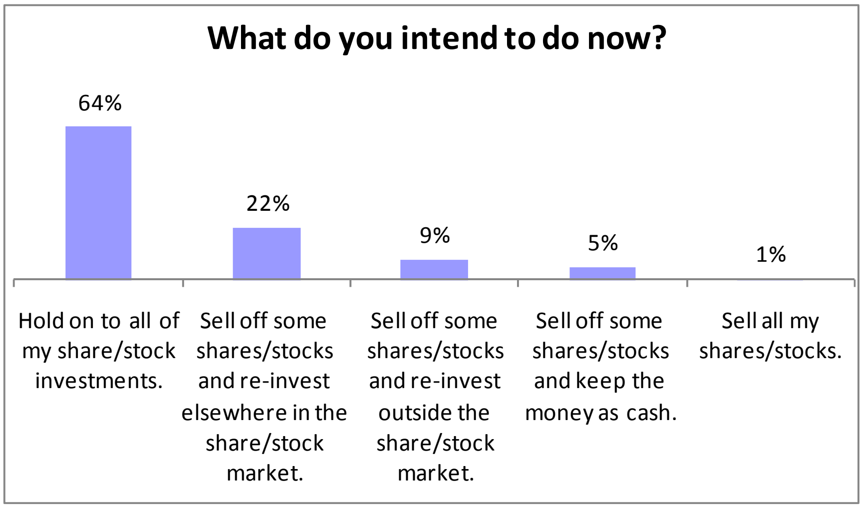

Fig 7

Fortunately, for many, their fears about our economic future have not eventuated to date, Fig 8.

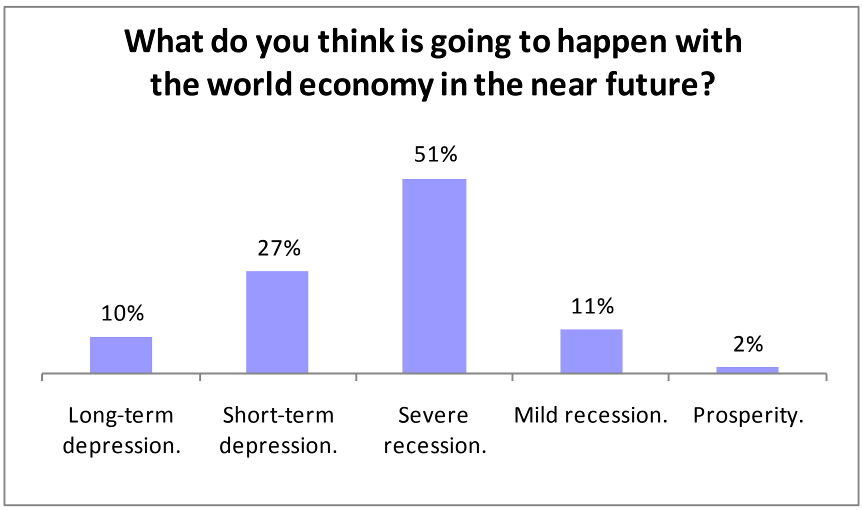

Fig 8

Overall, as can be seen in the detailed summaries of adviser and client responses set out in Appendices C and D, the consistency between Australia, the UK and the US[1] is quite high to the 'naked eye'. However, it does appear that UK clients feel less gloomy than their US or AUS counterparts.

The academic analysis may reveal underlying by-country patterns and will also be able to consider cross correlations between clients' responses and advisers' responses.

Where we have a risk profile and demographic for a surveyed client, and particularly where we have a previous risk profile and demographic data, there will be a myriad of multivariate analysis possibilities. Relationships between survey answers, risk tolerance scores, risk tolerance question answers and demographic variables can all be explored.

Perhaps the most interesting analysis will be of changes that occurred over the seven months. Markets had already fallen substantially by the start of December 2008 and continued falling for the next three months before turning around in March 2009. Comparisons between responses in December 2008 to February 2009 and responses in March to June 2009 could be very informative.

[1] There is sufficient data to make by-country comparisons for these three countries but not the others, see Appendix D.

Advisers

Participating advisers typically had around 15 years experience and overall their clients were not yet retired.

Some advisers were quite surprised by the magnitude of the market decline, Fig 9.

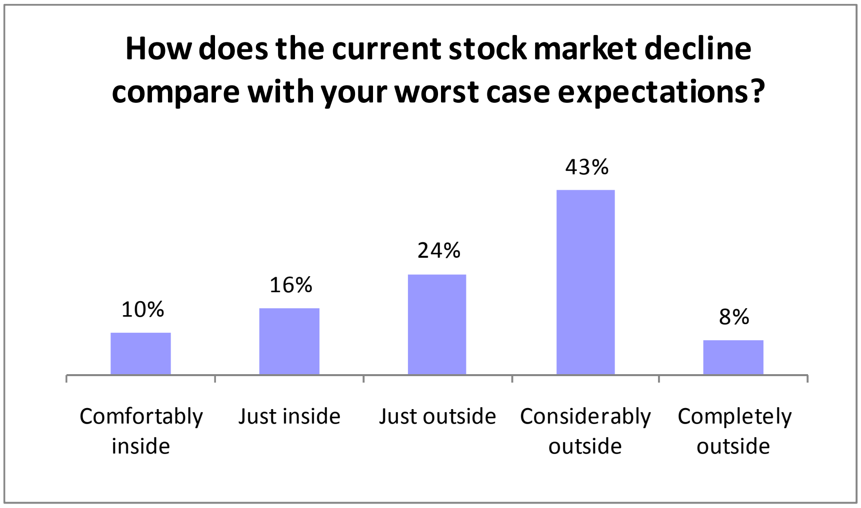

Fig 9

This in itself was somewhat surprising. All countries had experienced a substantial fall in 1973/74, Fig 10.

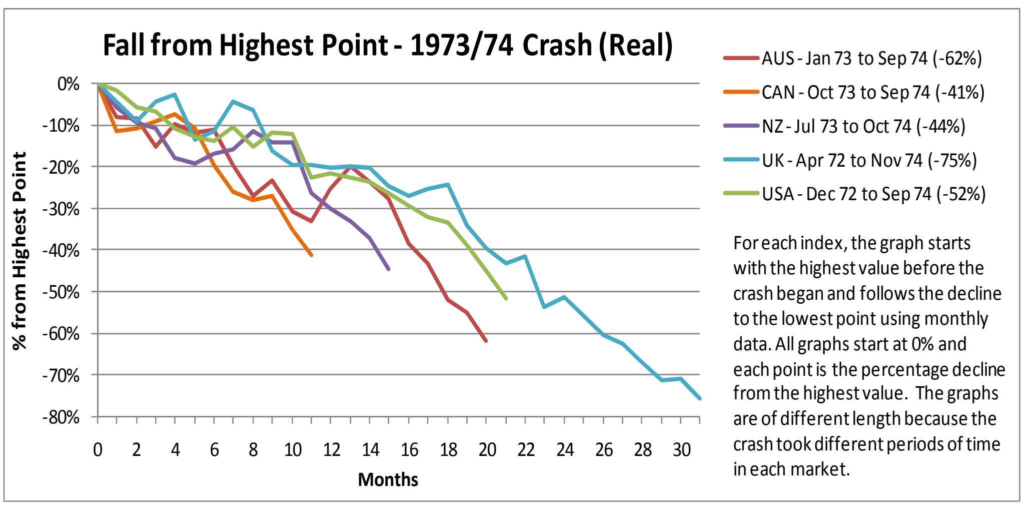

Fig 10

Comparing the falls in Fig 10 with those in Fig 2, shows that current falls are comparable except for the UK where the 1973/74 fall was much worse. Additionally, most markets experienced severe falls in 2000/02.

With regard to their clients' financial goals we asked a very similar question to the one we asked clients, Fig 11.

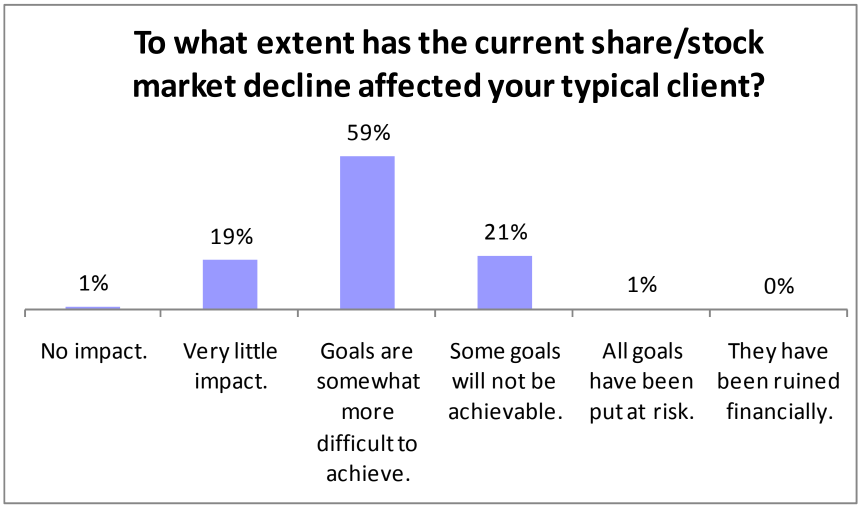

Fig 11

Clearly the answers here very closely match the clients' answers, see Fig 6, indicating that advisers were very much in tune with their clients' thinking. Again, the picture is quite positive overall with 79% believing that goals will be no more than somewhat more difficult to achieve (versus 76% from the client surveys.)

Test/Retest Data

The analysis of test/re-test data from the GFC provides the most convincing evidence of the stability of risk tolerance. Here test scores for individuals were compared. The first test was done between 1st July 2003 and 31st December 2007 (inclusive) and the second test after 31st July 2008. The longest period between test and retest was 71 months and the shortest was 9 months. The results are shown in Fig 12's scatter diagram. The y-value for each point is the first test score and the x-value is the second test score.

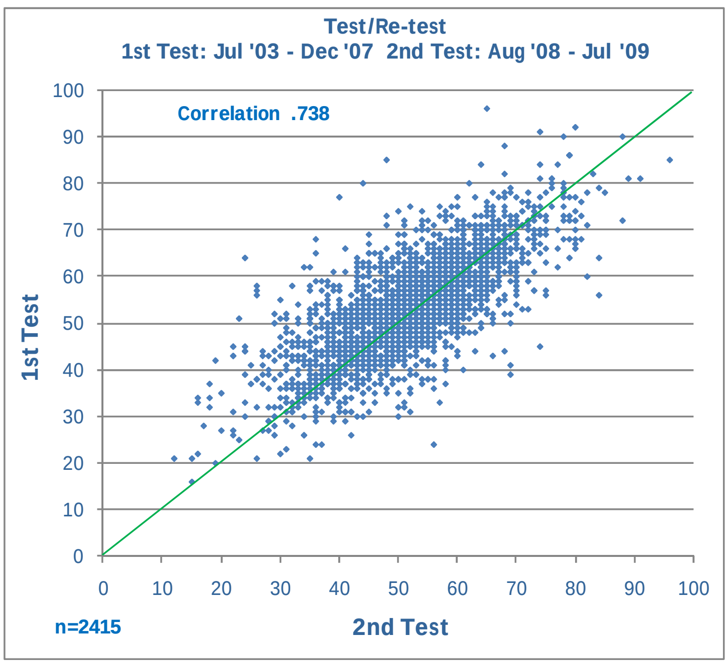

Fig 12

We see a small overall decline by, on average, -1.9 points. This is less than one-third of the standard deviation of 10 points, and so would not have a significant practical impact. Also note that some clients' risk tolerance scores have increased. However, there is an overall fall and it is worth considering possible explanations.

Major life events have been known to cause permanent psychological change. For some clients the crisis might have been a catastrophic life event and their scores might have decreased dramatically, bringing the average down.

Also, there might have effectively been a change in how some of the questions asked in the questionnaire were understood. The perceived riskiness of the answer options given for questions involving share market investment is likely to have increased with the result that the client would now choose a lower option leading to a lower score.

Or, there might be something else entirely. We are hopeful that our academic researchers will be able to analyse risk tolerance scores, answers to specific questions in our risk tolerance test and the demographic data we gather with each test.

This finding of stable risk tolerance will pose some challenges for the wider advisory community where the accepted wisdom is that risk tolerance collapses in a bear market. However, it may also provide an opportunity.

There is no argument that behaviour changes in a bear market. But this is not because risk tolerance has collapsed, rather it is because of an increase in perceived risk, as per Fig 5.

It is quite possible that some clients are perceiving markets to be much more risky than they actually are (just as two years ago they perceived markets to be much less risky than they actually were) and, as a result, may have 'frozen'. Re-educating clients about actual risk may help them to move forward which would be to the clients' benefit and so a significant value-add for their advisers.

Summary

To our knowledge this is a unique survey. We would again like to thank the advisers who participated and their clients. The preliminary analysis discussed above confirmed some accepted wisdom but also revealed some surprises, three of which were:

- Clients appear to have an unrealistic expectation that their adviser can protect them from the vagaries of the market,
- Given the market's relatively recent history, advisers appear to have been more surprised by the market falls than one would expect.
- The stability of risk tolerance, which though not a surprise to us, does disprove the accepted wisdom that risk tolerance collapses in a bear market but may provide an opportunity for advisers.

Geoff Davey
October 2009

Appendices

Appendix A – Adviser Survey

1. How long have you been an adviser?

- a Less than 5 years.
- b 5 to 10 years.
- c 11 to 20 years.
- d 21 to 30 years.
- e Greater than 30 years.

2. Who is your typical client?

- a Accumulator – focussed on building net wealth.
- b Pre-Retiree – focussed on pending retirement.
- c Partial Retiree – retired from full-time work but working part-time.
- d Retiree – no longer working.
- e Other. Please describe …

3. How does the current share market decline compare with your worst case expectations?

- a Comfortably inside.
- b Just inside.
- c Just outside.
- d Considerably outside.
- e Completely outside.

4. To what extent has the current share market decline affected your typical client?

- a No impact.
- b Very little impact.
- c Their financial goals are going to be somewhat more difficult to achieve.
- d Some of their financial goals will not be achievable.
- e All their major financial goals have been put at risk and will be very difficult to achieve.
- f They have been ruined financially.

5. To what extent has the current share market decline affected your view of share market risk?

- a No impact.
- b Very little impact.
- c I now believe that the share market is somewhat more risky than I had thought.
- d I now believe that the share market is considerably more risky than I had thought.
- e I now believe that the share market is enormously more risky than I had thought.

FinaMetrica produces and updates a version of its Risk and Return Guide and Charts (R&R) for each market in which we operate. The R&R provides advisers with unique educational material that, amongst other things, illustrates the historical pattern of returns with particular emphasis on declines. In particular, it includes data on the 1973/74 crash (which is comparable in magnitude with the current crash.) We are keen to know how useful the R&R has been in preparing your clients for the current share market decline.

6. To what extent did you use FinaMetrica's Risk and Return Guide and Charts with your clients?

- a Never.
- b Occasionally.
- c Often.
- d Always.

7. To what extent has the Risk and Return Guide and Charts been useful in preparing your clients for the possibility that their portfolios would have declined as they have?

- a Did not use the Risk and Return Guide and Charts.
- b The Risk and Return Guide and Charts were not useful.
- c The Risk and Return Guide and Charts have been somewhat useful.
- d The Risk and Return Guide and Charts have been extremely useful.

Appendix B – Client Survey

Most people will not have had all of their investments in shares during the current market decline. Rather they will have had diversified portfolios which, in addition to shares, will have included several other asset classes such as cash, fixed interest and property, so as to spread the risk. Hence, for most, only some of the current share market decline will be reflected in their investments as a whole.

1. To what extent is the effect of the current share market decline on your investments within your range of expectations?

- a Comfortably inside.
- b Just inside.
- c Just outside.
- d Considerably outside.
- e Completely outside.

2. To what extent has the current share market decline affected your current financial position?

- a No impact.
- b Very little impact.
- c Significant impact.
- d Catastrophic impact.

3. To what extent has the current share market decline affected your expectation of achieving your long-term financial goals?

- a My long-term financial goals are not affected.
- b My long-term financial goals are going to be somewhat more difficult to achieve.
- c Some of my long-term financial goals will not be achievable.
- d All my long-term financial goals have been put at risk and will be very difficult to achieve.

4. To what extent has the current share market decline affected your view of share market risk?

- a No impact.
- b I now believe that the share market is somewhat more risky than I had thought.
- c I now believe that the share market is considerably more risky than I had thought.
- d I now believe that the share market is enormously more risky than I had thought.

5. To what extent has the current crisis in the overall financial system affected your view of the risk in the overall financial system?

- a No impact.
- b I now believe that the overall financial system is somewhat more risky than I had thought.
- c I now believe that the overall financial system is considerably more risky than I had thought.
- d I now believe that the overall financial system is enormously more risky than I had thought.

6. What do you intend to do now?

- a Hold on to all of my share investments in their current accounts.
- b Sell off some shares and re-invest the proceeds elsewhere in the share market.
- c Sell off some shares and re-invest outside the share market.
- d Sell off some shares and keep the money as cash.
- e Sell all my shares and get out of the share market entirely.

7. What do you think is going to happen with the world economy in the near future?

- a Long-term depression.
- b Short-term depression.
- c Severe recession.
- d Mild recession.
- e Prosperity.

Appendix C – Results Summary: Adviser

SUMMARY* - Advisers	All	AUS	CAN#	NZ#	UK	US	Other#
No of Respondents to Survey	174	30	5	6	49	81	3
		17%	3%	3%	28%	47%	2%
How long have you been an adviser?							
Less than 5 years.	9%	10%	0%	0%	8%	10%	0%
5 to 10 years.	18%	20%	40%	17%	10%	21%	33%
11 to 20 years.	35%	40%	0%	17%	35%	36%	67%
21 to 30 years.	28%	23%	60%	67%	33%	22%	0%
Greater than 30 years.	10%	7%	0%	0%	14%	11%	0%
Avg.^	3.1	3.0	3.2	3.5	3.3	3.0	2.7
Who is your typical client?							
Accumulator – focussed on building net wealth.	20%	10%	20%	0%	24%	21%	67%
Pre-Retiree – focussed on pending retirement.	40%	40%	40%	50%	33%	43%	33%
Partial Retiree – retired from full-time work but working part-time.	7%	10%	0%	17%	4%	7%	0%
Retiree – no longer working.	22%	30%	20%	17%	27%	19%	0%
Other. Please describe …	11%	10%	20%	17%	12%	10%	0%
Avg.	2.6	2.9	2.8	3.0	2.7	2.5	1.3
How does the current share/stock market decline compare with your worst case expectations?							
Comfortably inside	10%	0%	20%	0%	18%	6%	67%
Just inside	16%	3%	20%	33%	29%	11%	0%
Just outside	24%	27%	20%	50%	29%	17%	33%
Considerably outside	43%	70%	40%	17%	24%	48%	0%
Completely outside	8%	0%	0%	0%	0%	17%	0%
Avg.	3.2	3.7	2.8	2.8	2.6	3.6	1.7
To what extent has the current share/stock market decline affected your typical client?							
No impact.	1%	0%	0%	0%	2%	1%	0%
Very little impact.	19%	17%	20%	33%	24%	14%	67%
Their financial goals are going to be somewhat more difficult to achieve.	59%	67%	40%	50%	61%	57%	33%
Some of their financial goals will not be achievable.	21%	17%	40%	17%	12%	27%	0%
All their major financial goals have been put at risk and will be very difficult to achieve.	1%	0%	0%	0%	0%	1%	0%
They have been ruined financially.	0%	0%	0%	0%	0%	0%	0%
Avg.	3.0	3.0	3.2	2.8	2.8	3.1	2.3
To what extent has the current share/stock market decline affected your view of stock market risk?							
No impact.	10%	17%	20%	17%	12%	6%	0%
Very little impact.	43%	43%	0%	67%	63%	30%	100%
I now believe that the share/stock market is somewhat more risky than I had thought.	39%	40%	40%	17%	22%	52%	0%
I now believe that the share/stock market is considerably more risky than I had thought.	6%	0%	20%	0%	2%	11%	0%
I now believe that the share/stock market is enormously more risky than I had thought.	1%	0%	20%	0%	0%	1%	0%
Avg.	2.4	2.2	3.2	2.0	2.1	2.7	2.0
To what extent did you use FinaMetrica's Risk and Return Guide and Charts with your clients?							
Never.	34%	27%	20%	17%	27%	43%	67%
Occasionally.	24%	30%	40%	0%	22%	22%	33%
Often.	18%	10%	40%	33%	24%	15%	0%
Always.	24%	33%	0%	50%	27%	20%	0%
Avg.	2.3	2.5	2.2	3.2	2.5	2.1	1.3
To what extent has the Risk and Return Guide and Charts been useful in preparing your clients for the possibility that their portfolios would have declined as they have?							
Did not use the Risk and Return Guide and Charts.	43%	30%	20%	33%	41%	51%	67%
The Risk and Return Guide and Charts were not useful.**	6%	10%	0%	0%	3%	8%	0%
The Risk and Return Guide and Charts have been somewhat useful.**	64%	67%	50%	100%	52%	68%	100%
The Risk and Return Guide and Charts have been extremely useful.**	30%	24%	50%	0%	45%	25%	0%
Avg.	2.2	2.1	2.5	2.0	2.4	2.2	2.0

* The wording of some answer options has been précised for layout purposes.
** Results are based on people who have used the charts only.
# The sample size sizes for CAN, NZ and Other are too small for meaningful analysis.
^ The average (Avg) is calculated by numbering each of the answer options and then multiplying that number by the percentage who chose that option and summing the results. The Avg provides a basic, by-country comparison of answers.

Appendix D – Results Summary: Clients

SUMMARY* - Clients	All	AUS	CAN#	NZ#	UK	US	Other#
No of Respondents to Survey	445	97	4	10	83	227	24
	100%	22%	1%	2%	19%	51%	5%
To what extent is the effect of the current share/stock market decline on your investments within your range of expectations?							
Comfortably inside.	5%	6%	50%	10%	4%	4%	13%
Just inside.	15%	7%	0%	30%	24%	12%	33%
Just outside.	21%	23%	50%	10%	28%	18%	21%
Considerably outside.	46%	46%	0%	50%	37%	52%	29%
Completely outside.	13%	18%	0%	0%	7%	15%	4%
Avg.^	3.5	3.6	2.0	3.0	3.2	3.6	2.8
To what extent has the current share/stock market decline affected your current financial position?							
No impact.	5%	4%	0%	0%	6%	4%	13%
Very little impact.	34%	24%	50%	50%	49%	30%	50%
Significant impact.	60%	68%	50%	50%	45%	65%	33%
Catastrophic impact.	2%	4%	0%	0%	0%	2%	4%
Avg.	2.6	2.7	2.5	2.5	2.4	2.6	2.3
To what extent has the current share market decline affected your expectation of achieving your long-term financial goals?							
My long-term financial goals are not affected.	18%	18%	25%	10%	17%	18%	29%
My long-term financial goals are going to be somewhat more difficult to achieve.	58%	55%	75%	80%	65%	56%	58%
Some of my long-term financial goals will not be achievable.	20%	22%	0%	10%	17%	22%	8%
All my long-term financial goals are now at risk and will be very difficult to achieve.	4%	6%	0%	0%	1%	5%	4%
Avg.	2.1	2.2	1.8	2.0	2.0	2.1	1.9
To what extent has the current share/stock market decline affected your view of share/stock market risk?							
No impact.	26%	28%	75%	40%	29%	22%	33%
I now believe that the share/stock market is somewhat more risky.	41%	45%	0%	30%	43%	39%	38%
I now believe that the share/stock market is considerably more risky.	27%	23%	0%	30%	23%	32%	17%
I now believe that the share/stock market is enormously more risky.	6%	4%	25%	0%	5%	7%	13%
Avg.	2.1	2.0	1.8	1.9	2.0	2.2	2.1
To what extent has the current crisis in the overall financial system affected your view of the risk in the overall financial system?							
No impact.	15%	20%	50%	20%	16%	11%	17%
I now believe that the overall financial system is somewhat more risky.	35%	41%	0%	50%	34%	33%	38%
I now believe that the overall financial system is considerably more risky.	38%	30%	25%	30%	40%	44%	25%
I now believe that the overall financial system is enormously more risky.	12%	9%	25%	0%	11%	12%	21%
Avg.	2.5	2.3	2.3	2.1	2.5	2.6	2.5
What do you intend to do now?							
Hold on to all of my share/stock investments in their current accounts.	64%	55%	75%	80%	75%	63%	54%
Sell off some shares/stocks and re-invest elsewhere in the share/stock market.	22%	34%	25%	10%	18%	19%	21%
Sell off some shares/stocks and re-invest outside the share/stock market.	9%	3%	0%	0%	6%	12%	13%
Sell off some shares/stocks and keep the money as cash.	5%	8%	0%	0%	1%	5%	13%
Sell all my shares/stocks and get out of the share/stock market entirely.	1%	0%	0%	10%	0%	1%	0%
Avg.	1.6	1.6	1.3	1.5	1.3	1.6	1.8
What do you think is going to happen with the world economy in the near future?							
Long-term depression.	10%	7%	25%	20%	17%	7%	8%
Short-term depression.	27%	21%	0%	40%	31%	26%	42%
Severe recession.	51%	56%	50%	20%	47%	53%	33%
Mild recession.	11%	16%	25%	20%	5%	11%	13%
Prosperity.	2%	0%	0%	0%	0%	3%	4%
Avg.	2.7	2.8	2.8	2.4	2.4	2.8	2.6

* The wording of some answer options has been précised for layout purposes.
# The sample size sizes for CAN, NZ and Other are too small for meaningful analysis.
^ The average (Avg) is calculated by numbering each of the answer options and then multiplying that number by the percentage who chose that option and summing the results. The Avg provides a basic, by-country comparison of answers.