CFA Institute

GLOBAL MARKET SENTIMENT SURVEY 2013

EXECUTIVE SUMMARY

CFA Institute's annual global market sentiment survey reveals members' cautious optimism about the future of the financial markets in 2013, tempered by their concern that the underlying problems that contributed to the worldwide economic crisis and the decline in the integrity of the markets have not yet been solved. As experienced participants within the global financial services industry, the opinions expressed in this report are a strong reflection of the views of highly educated, ethical practitioners with unique insights into the opportunities and risks of the financial markets.

When asked whether they believe the global economy will expand, contract, or stay roughly the same over the coming year, 40% of members answered that the economy will expand; 20% believe the global economy will contract. The outlook is still guarded, which is understandable given the ongoing European sovereign debt crisis, an expected slowing of economic growth in China, and the pending fiscal cliff in the United States. But the outlook is clearly more optimistic than last year, when only 34% said the global economy would expand and nearly as many (29%) said the global economy would contract. Members' outlook on other short-term issues, such as employment opportunities for financial professionals, has also improved slightly over the past year. Further, 50% of those surveyed expect equities to outperform all asset classes, while only about 41% thought that a year ago.

Despite the cautious optimism regarding short-term issues, longer-term issues—the ones that helped bring about the financial crisis whose effects are still being felt—must be addressed for continued positive progress for improvements in economic health and market integrity. In particular, 56% of members identified a continuing lack of ethical culture within financial firms as the major factor contributing to the current lack of trust in the finance industry, and two-thirds said that a culture of ethics and integrity within firms needs to be reestablished. The primary problems are not the physical failures of the market or government actions but the culture of firms within the financial industry.

ABOUT THIS SURVEY

The CFA Institute Global Market Sentiment Survey was created to seek input from CFA Institute members and gather feedback on market sentiment, performance, and market integrity issues in 2013, and to further our mission of promoting ethical and trustworthy investment markets.

METHODOLOGY

An online survey was conducted from 30 October to 13 November 2012. All CFA Institute members globally (115,096) were invited to participate in the survey; 6,783 responded, for an overall response rate of 6% and a margin of error of ±1.2%. In addition to analysis and reporting at the global, regional, and advanced vs. developing economies level, 22 countries are also included in this report.

ABOUT CFA INSTITUTE

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. CFA Institute has more than 110,000 members in 138 countries and territories, including over 103,000 CFA charterholders, and 138 member societies. For more information, visit **www.cfainstitute.org**.

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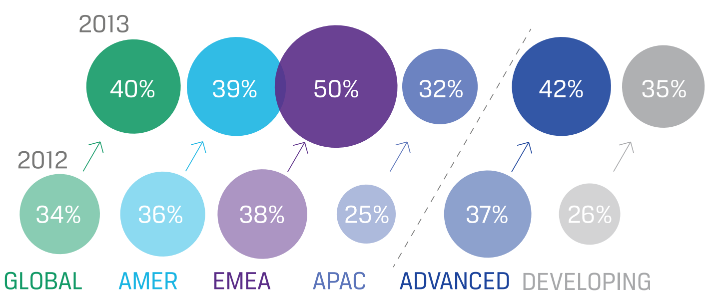
INVESTMENT PROFESSIONALS INCREASINGLY OPTIMISTIC ON GLOBAL ECONOMIC GROWTH

Advanced economies are especially optimistic on global economic expansion in 2013, despite the continued worldwide impact of the European sovereign debt crisis

Most members think the global economy will expand or stay the same in 2013, with a higher proportion of members expecting the global economy to expand this year (40%) compared with those who predicted as much last year (34%) *(fig. 1)*. Although developing economies tend to be more optimistic about local economic growth, a higher proportion of members in advanced economies (42%) compared with the proportion of members in developing economies (35%) think global economic expansion will happen in 2013. France is most optimistic regarding global economic growth (61% of members in France think it will expand), whereas only 21% of members in China expect the global economy to expand in the coming year.

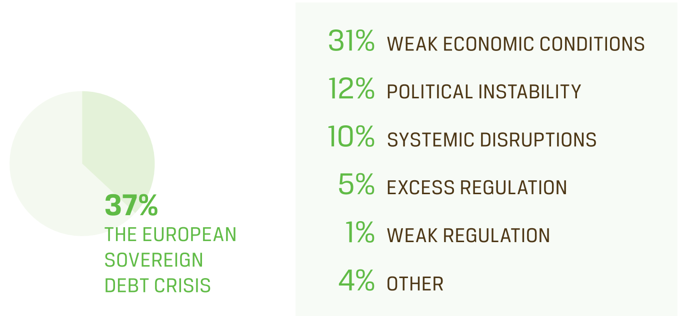
(fig. 1)
Percent of members expecting the global economy to expand



The biggest risks to global capital markets in 2013 that members expressed concern about are the European sovereign debt crisis (37%) and weak economic conditions (31%) *(fig. 2)*.

Although members in most countries in Europe think the European sovereign debt crisis will be the biggest risk to their local markets in 2013, they are less concerned about its impact on the global economy (44% versus 34%). Members in Brazil (59%) and the United Arab Emirates (54%) are more concerned about the risk associated with the European sovereign debt crisis's impact on global capital markets than about its impact on their local economies. China expresses more concern about risks associated with weak economic conditions (48%) than risks associated with the European sovereign debt crisis (28%).

(fig. 2)
Biggest risks to global capital markets in 2013



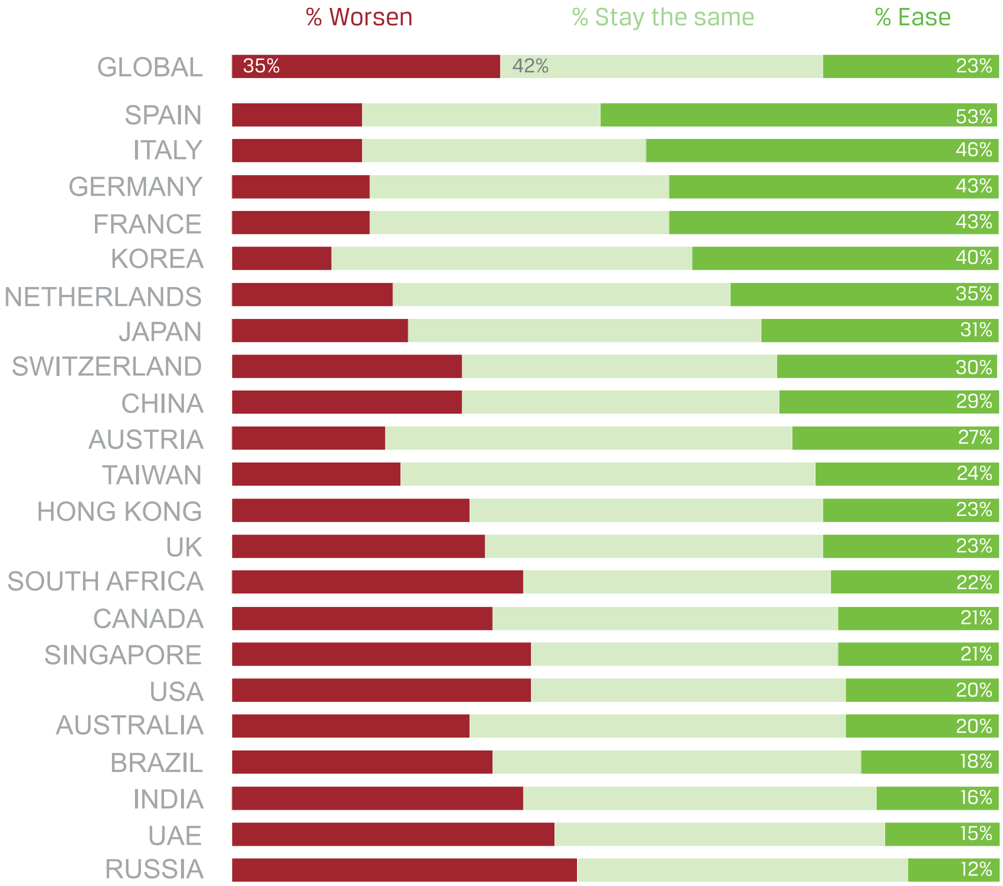
Given the prominence of the European sovereign debt crisis as a risk factor, it follows that members think that an increased focus on resolving or easing this crisis will have the biggest positive impact on global capital markets in 2013 (36%). Other actions members think could have a positive impact include:

- increased growth rates among emerging economies (26%)
- increased focus on solutions to create more jobs (20%)

Members are divided on whether they think the European sovereign debt crisis will ease (23%), worsen (35%), or stay the same (42%) in 2013. The countries with the highest proportion of members who are optimistic about the crisis easing in the coming year are Spain (53%), Italy (46%), Germany (43%), and France (43%). The countries least optimistic, with high proportions of members indicating they think the crisis will worsen, are Russia (45%), the United Arab Emirates (41%), the United States and Singapore (both at 39%), and South Africa (38%) *(fig. 3)*.

"Problems abound but progress is being made"
- Canada

(fig. 3)
Expectation of European sovereign debt crisis in 2013



Members in Europe are more likely to think an increased focus on resolving the European sovereign debt crisis will have the biggest positive impact. Members in South Africa, India, and Brazil think increased growth rates among emerging economies will have the biggest impact (37%, 35%, and 33%, respectively). Taiwan is the only country with the highest proportion of members picking an increased focus on solutions to create more jobs (33%) as the factor that will have the biggest impact.

THE FUTURE LOOKS BRIGHTER FOR LOCAL ECONOMIC GROWTH, UNLESS YOU'RE IN EUROPE

The biggest concerns for local markets include weak economic conditions in advanced economies, political instability in developing economies, and the European sovereign debt crisis in Europe

Members believe that the biggest risks to local markets in 2013 will be:

- *weak economic conditions (38%),*
- *political instability (18%), and*
- *the European sovereign debt crisis (17%).*

Just under half of members globally (45%) think their local economies will expand in 2013 (up slightly from 42% in 2012), but members in developing economies are markedly more optimistic than those in advanced economies (56% versus 43%, respectively). Members in Brazil, the United Arab Emirates, and India are especially optimistic about local economic growth; 87%, 73% and 69%, respectively, expect their local economies to expand in 2013 *(fig. 4)*. In stark contrast, only 28% of respondents in Europe expect their local economies to expand in 2013, which can largely be attributed to the European sovereign debt crisis (44% of European members see the crisis as the biggest risk to their local markets in 2013 compared with only 17% globally). Among European countries, members in Germany are most optimistic, with 42% expecting their economy to expand.

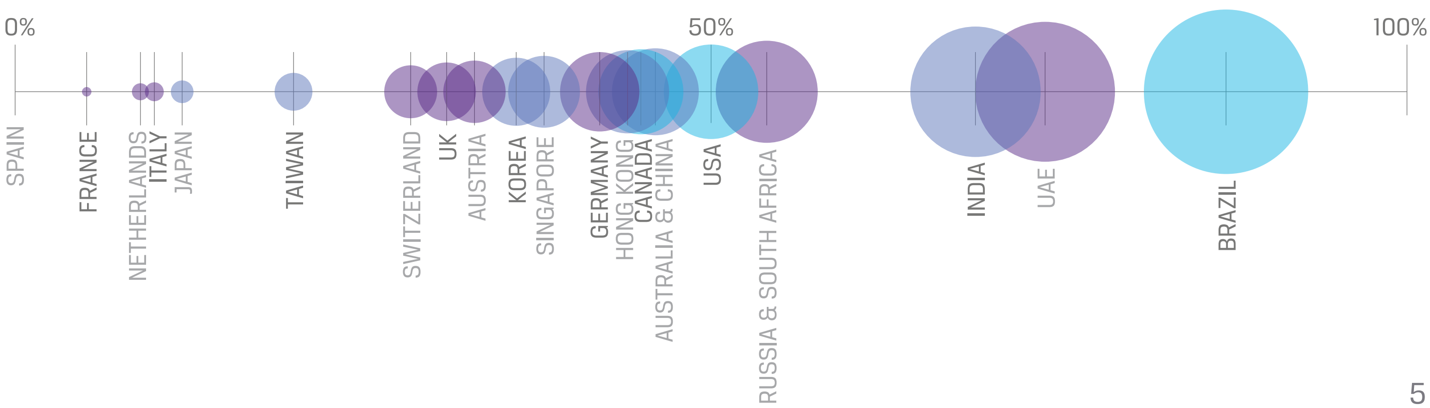
Members in advanced economies (40%) are more concerned with weak economic conditions than those in developing economies (25%) *(fig. 5)*. Members in Taiwan (75%), Canada (51%), and Australia (48%) are most concerned *(fig. 6)*, a result that contrasts surprisingly with the economic stability ratings forecast for these countries by the Economist Intelligence Unit, which do not show current threats to these economies.

A higher proportion of members in developing economies (37%) than in advanced economies (14%) believe that political instability is the biggest risk to their local markets *(fig. 5)*. Developing economies, almost by definition, are less likely to worry about weak economic conditions because they are less likely than advanced economies to have relied on strong economic conditions in the past. Among all countries, South Africa (65%) and India (60%) have the highest proportion of members concerned about political instability, followed by Italy (47%) and Japan (43%) *(fig. 6)*. In the United States, the recently concluded presidential election campaign and gridlock in Congress have contributed to significant delays in the implementation of financial reform under the Dodd–Frank Act. In a globally connected economy, however, economic weakness in advanced economies can negatively affect developing economies, particularly those where political instability, such as the Arab Spring revolutions, has existed for some time already. Similarly, political instability, like the gridlock over the U.S. budget, can send ripples throughout the economic ecosystem.

> *"I feel local markets are closely coupled with global markets. Local markets however will be able to attract capital from overseas which will fuel growth in equity markets. However the key to sustained growth will depend on the will power of the government to bring out transparency, enforcement of regulations and reducing income disparity amongst the rich and the poor."*
>
> *- India*

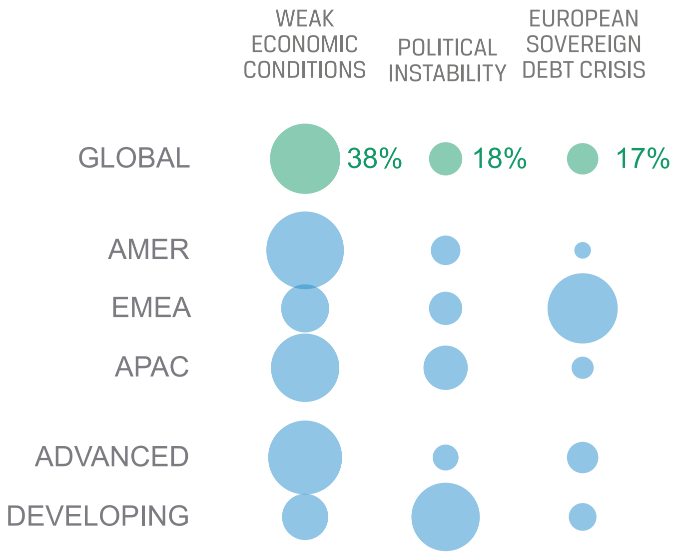
(fig. 4)

Percent of members expecting their local economy to expand in 2013

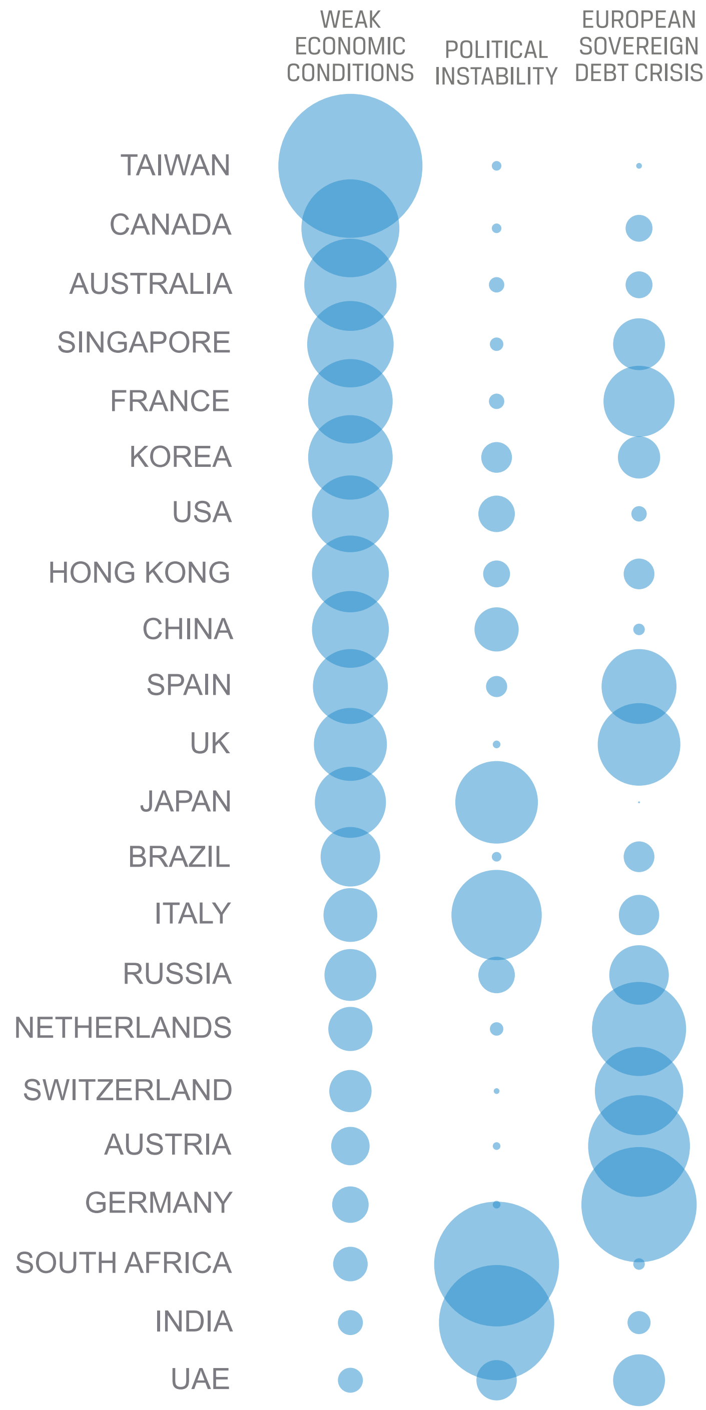


As would be expected, a significantly higher proportion of members in Europe (44%)— than in the Americas and Asia Pacific (9% and 12%, respectively)—are concerned about the risks to their local markets associated with the European sovereign debt crisis in 2013. The worsening of this crisis, which increases the likelihood of a partial breakup of the eurozone with disastrous consequences, has made clear the necessity of bold action by EU leaders to tame it. A separate **CFA Institute survey of European members** in January 2012 found that members believe that the common issuance of eurobonds could help alleviate the debt crisis, but only as part of a package of structural reforms, fiscal integration, and a strong common governance framework. The majority of those surveyed also believe that issuance of long-term eurobonds is neither feasible nor desirable without further EU financial, fiscal, and monetary integration, mainly because of the risk of moral hazard.

(fig. 5)
Percent of members indicating the following as the biggest risk to their local market in 2013



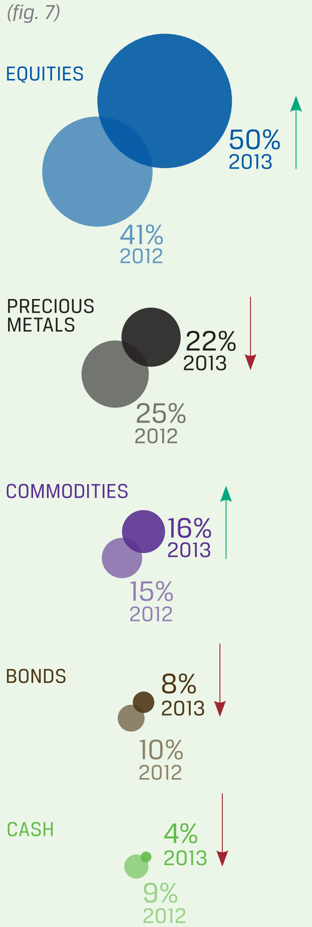
(fig. 6)
Percent of members indicating the following as the biggest risk to their local market in 2013, by country



Equities expected to provide the highest return

Half of members globally think equities will provide the highest expected total return in 2013, up from 41% in 2012 *(fig. 7)*. The increase in the proportion selecting equities as the top performer is most pronounced in Asia Pacific, with an increase of 11 percentage points from last year's survey (41% versus 30%). The asset class with the most significant decrease is cash, down 5 percentage points from 2012.

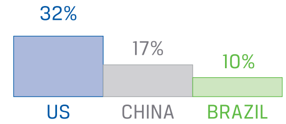
(fig. 7)



United States, China, and Brazil to provide the best investment opportunity

According to the Financial Times, the economy of Brazil is set for one of its weakest annual performances in a decade, adding to economic slowdown in other emerging markets, including China, where growth slipped to 7.4% in the third quarter of 2012. Nevertheless, members identified the United States, China, and Brazil as the three equity markets they expect to provide the best investment opportunity in 2013 *(fig. 8)*.

(fig. 8)
Proportion of members indicating the following equity markets will provide the best investment opportunity in 2013



Employment opportunities for investment professionals expected to remain stable

Members expect employment opportunities for investment professionals to stay about the same in the coming year, which is consistent with the results of last year's survey. Additionally, 49% of members think employment opportunities for investment professionals in their local markets will stay the same, 17% think they will increase, and 33% think they will decrease; 58% of members in Europe expect employment opportunities for investment professionals in their local markets to decrease in 2013. Members in developing economies are more positive about increasing employment opportunities than those in advanced economies (28% indicating an expected increase versus 15%, respectively). Members in India (44%), the United Arab Emirates (36%), and Brazil (36%) are the most optimistic about employment opportunities for investment professionals in the coming year *(fig. 9)*.

(fig. 9)
Expectation of employment opportunities for investment professionals in your local market in 2013

TO RESTORE INTEGRITY TO THE GLOBAL CAPITAL MARKETS, CHANGE MUST COME FROM WITHIN

Investment professionals are cautiously optimistic about the global economy in 2013, but ethical culture within financial firms needs to be addressed to solve systemic problems that led to fiscal crisis

Although conflicting evidence suggests that financial markets may finally be stabilizing after four years of turmoil, members globally agree that:

- *the current level of integrity of global capital markets is poor;*
- *the low level of integrity is unlikely to change in the coming year;*
- *investors overwhelmingly lack trust and confidence in the finance industry.*

The economic crisis and the damage it inflicted to the confidence of investors in the integrity of the global capital markets have led to widespread calls, particularly in the United States and Europe, for increased regulatory scrutiny, tighter enforcement of existing laws/regulations, and new forms of regulation in the financial markets, including:

- *the massive overhaul of United States financial regulation proposed under the Dodd Frank Act;*
- *proposed reform by the U.K.'s new Financial Conduct Authority in response to the LIBOR scandal;*
- *the introduction of the EU's biggest-ever program for financial services reforms, which consists of more than 30 new reforms focused on improving financial market effectiveness, integrity, and transparency and includes new rules on short selling, credit default swaps, and derivatives;*
- *new FINRA regulations to improve market transparency and integrity.*

98% acknowledge a current lack of trust in the finance industry

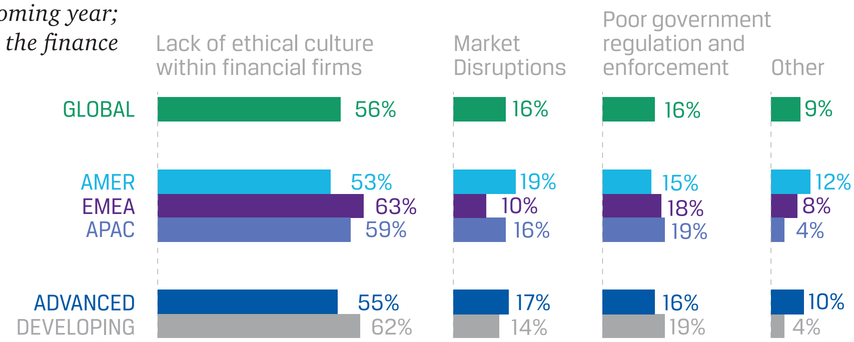
80% of members rated the integrity of global capital markets in 2012 a 3 or less *(Scale: Poor (1) to Excellent (5))*

67% think the integrity of global capital markets will be about the same in 2013 as 2012

CFA Institute members, however, are not placing blame primarily on poor government regulation and enforcement and don't see improvements in this area as having the biggest positive impact on global capital markets. Rather, over half (56%) cited a lack of ethical culture within financial firms as the factor that has contributed the most to the low level of industry trust. Because the problem stems from within firms, members said, change must also start there *(fig. 10)*.

(fig.10)

The factor members think has contributed the most to the current lack of trust in the finance industry



When asked to prescribe a firm-level action to improve investor trust and confidence, members indicated that change must come from the top, with 40% saying that the most-needed action is for top management and executives to establish and encourage an improved ethical culture. Recent high-profile ethical failures ranging from poor risk management oversight and resume padding to excessive compensation and self-dealing have demonstrated that ethical misbehavior can start at the top. Leading financial institutions all have codes of conduct that should foster ethical conduct, but it takes active leadership to make this promise a reality. CFA Institute is committed to helping make this happen by calling for, among other things, a new paradigm of **"Visionary" Board Leadership** that embodies the management and foresight necessary to break through the short-term noise in the markets and ensure that public companies are led and governed for the long-term benefit of all market participants and stakeholders.

> *"Adopt a higher purpose mission than executive compensation and/or stock price."*
>
> *- Canada*

"Ethics is an ongoing project to help restore trust in the financial industry. We need to improve financial professionals' sense of self-control, construct related culture for the whole industry and companies globally, and set a serious penalty system for any illegal and unethical activities." *- China*

The most-needed firm-level action, according to 26% of members is increased adherence to ethical codes and standards. CFA Institute believes that a good place to start is with its **Asset Manager Code of Professional Conduct**, the global standard of conduct for investment managers to affirm their commitment to ethical principles that put client interests first. A higher proportion of members in advanced economies (42%) compared with the proportion in developing economies (34%) think improved culture is the most-needed reform, whereas a higher proportion of those in developing economies (35%) compared with the proportion in advanced economies (24%) think increased adherence to codes and standards is most needed *(fig. 11)*.

(fig. 11)

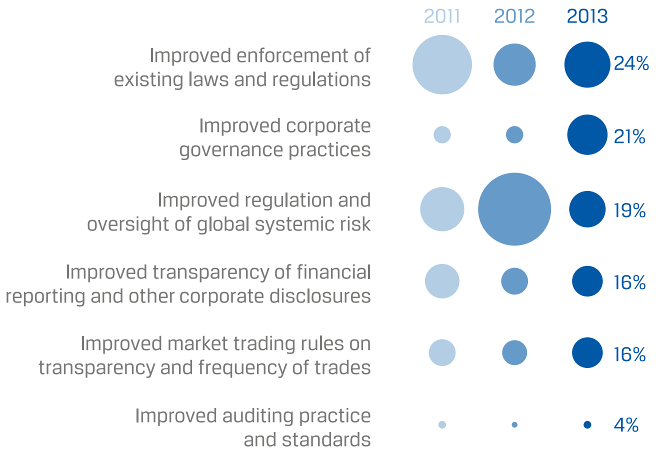
Firm-level action most needed to help improve investor trust and confidence

This desire for leadership and change reflects members' concerns that, as a result of the financial crisis, the social contract that should exist between financial professionals and those they serve has been damaged, if not broken. John Rogers, CFA, president and CEO of CFA Institute, has said that the resulting "social cost" can be seen in the savings gap suffered by many older Americans, many of whom can no longer look forward to experiencing a "dignified retirement." This loss of trust directly correlates with the current defensive mindset of investors: They are seeking "safe haven" investments rather than investing for the long term.

Members responding to the survey did not dismiss the need for action at the industry or regulatory level, but their focus on the most-needed action in the coming year has changed. On last year's survey, the most-needed regulatory/industry action selected by the highest proportion of members (38%) was improved regulation and oversight of global systemic risk; this year, only 19% responded that way. In fact, members this year do not seem to favor any one regulatory action as the most needed, although slightly more respondents called for improved enforcement of existing laws and regulations and improved market trading rules on transparency and frequency of trades compared with last year. This change reflects the trend toward larger volumes of equity market transactions taking place away from public exchanges through internalization and so-called dark pools. The seeming lack of consensus could suggest that members think a combination may be necessary, without any single solution being sufficient *(fig. 12)*.

(fig. 12)

Regulatory/industry actions most needed to improve investor trust and market integrity



Looking ahead to 2013, members see no improvement likely in the integrity of global capital markets, with 67%—up from 56% last year expecting levels to stay the same as last year. As one member in the United Kingdom said, "It is impossible to be optimistic that any of the many problems with the industry and capital markets will be solved. Regulators today focus on the easy wins to be gotten from prosecuting small insider traders and harassing firms over breaches of the thicket of rules they have created to justify their existence." In their local markets, 29% of members (up significantly from 13% last year) said that the most serious ethical issue in the coming year is likely to be mis-selling of products by financial advisers *(fig. 13)*.

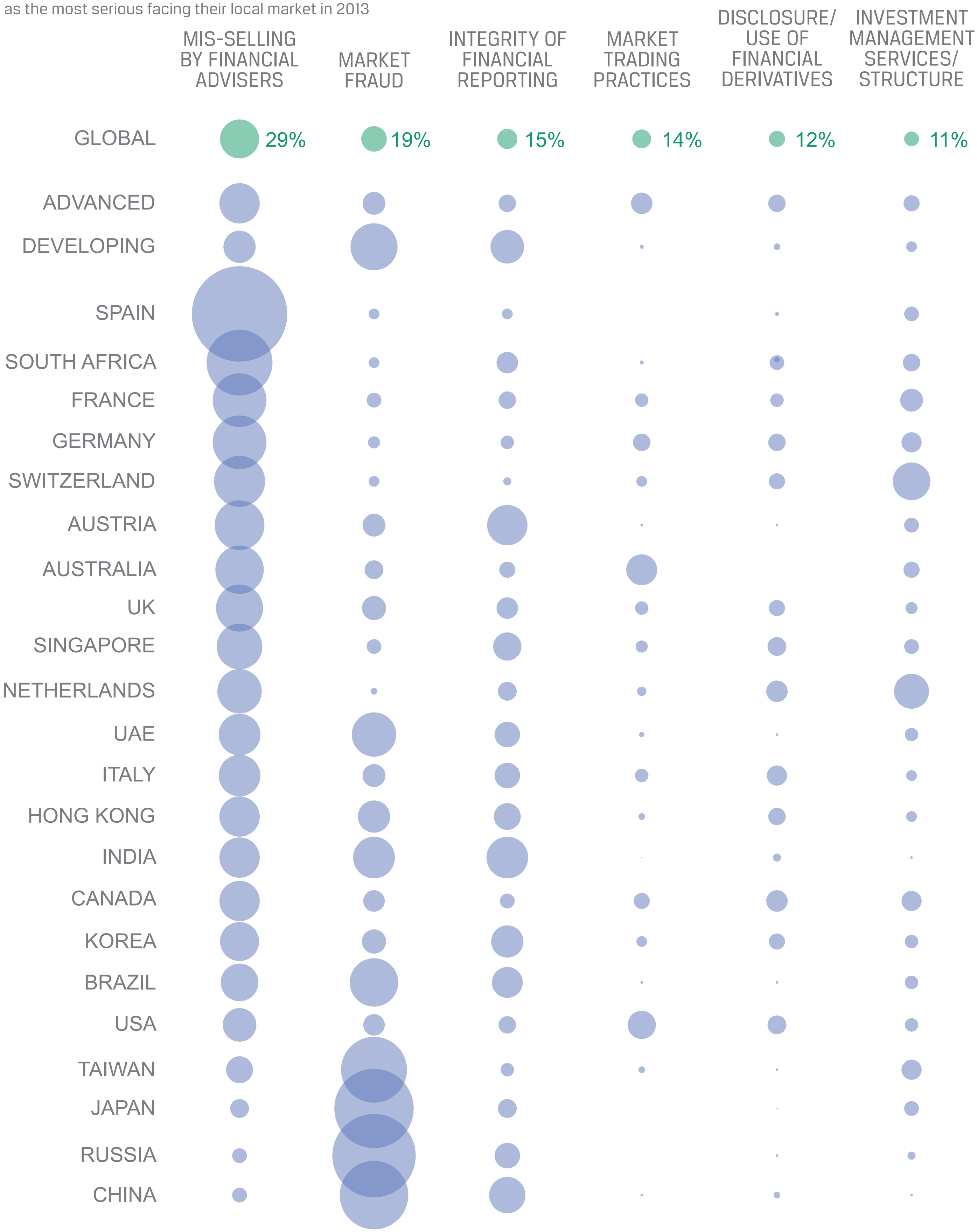
With regard to global markets, however, members are less threatened by mis-selling. Instead, members think the most serious ethical issues facing global markets in the coming year will be derivatives (23%)—the misuse of which was a primary contributor to the financial crisis—and the honesty/integrity of financial reporting (21%, up from 12% last year).

These are disappointing results, indeed. When advisers fail to act in the best interest of their clients, whether by pushing an unsuitable product to obtain a commission or failing to provide advice tailored to the client's specific needs, it directly undermines the basis of trust between client and adviser. CFA Institute members recognize that honoring their fiduciary responsibility is at the heart of restoring the integrity of the system, and this year, they are more concerned about this issue.

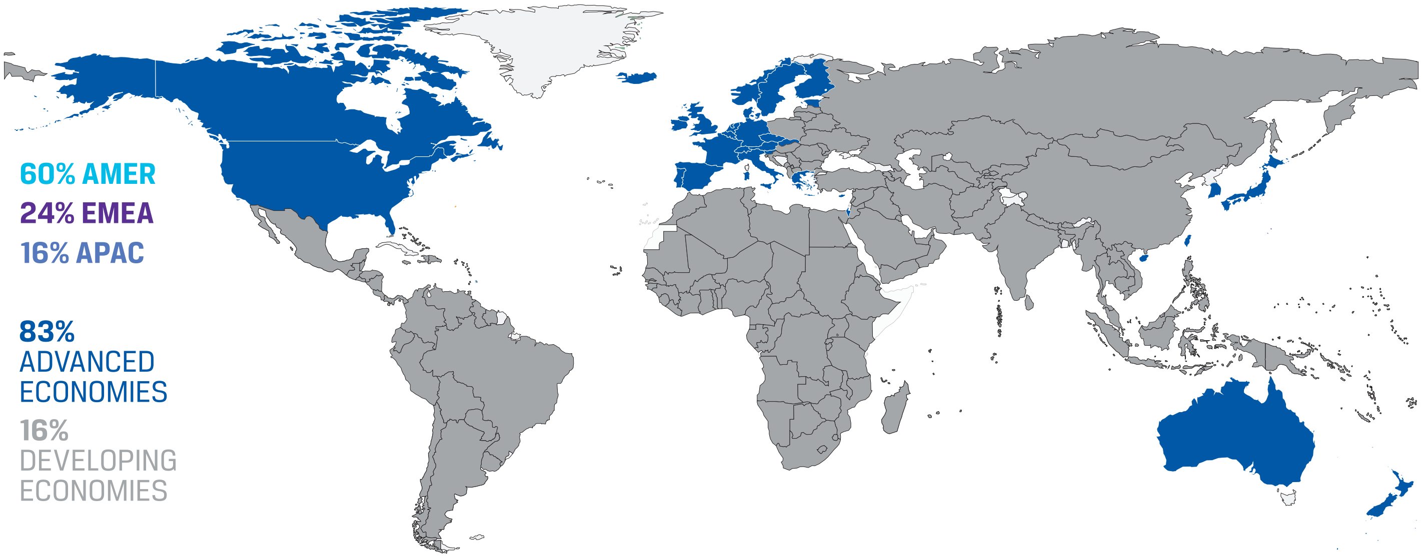
Other ethical issues members view as having the most serious impact on their local markets in the coming year are market fraud (insider trading), lack of honesty and integrity in financial reporting, and such controversial practices as trading in dark pools and high frequency trading, although the seriousness of each issue varies widely by market. For example, 71% of members in Spain say the most serious issue is mis-selling of products by financial advisers compared with only 11% of members in China. Comparing advanced economies with developing economies, we see broad divergence about which ethical issue is the most serious. Although both identify mis-selling of products by financial advisers as serious (30% and 24%, respectively), advanced economies are more concerned than developing economies about derivatives (13% versus 5%) and market trading practices (16% versus 3%). Conversely, developing economies are more concerned than advanced economies about market fraud (35% versus 17%) and financial reporting (25% versus 13%) *(fig. 13)*.

What does this all mean for the profession? Industry participants must come together and make trust and integrity just as important as performance and analytics, beginning with steps taken at the firm level and complemented by effective enforcement of industry regulation. CFA Institute has identified three "pillars" industry firms need to focus on to restore investors' trust and get them back to meeting their investment goals: (1) better education for investment professionals and investors, (2) stronger industry-wide ethical practices (a key element of CFA Institute's mandate), and (3) tougher enforcement of the rules by industry regulators.

(fig. 13)
Percent of members ranking the following ethical issues as the most serious facing their local market in 2013



RESPONDENT PROFILE



60% AMER
24% EMEA
16% APAC

83% ADVANCED ECONOMIES
16% DEVELOPING ECONOMIES

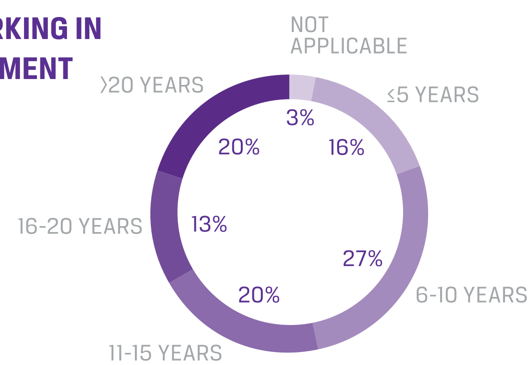
TOP COUNTRIES

UNITED STATES	3042
CANADA	839
UNITED KINGDOM	309
SWITZERLAND	205
HONG KONG	192
CHINA	175
GERMANY	174
AUSTRALIA	135
INDIA	115
SOUTH AFRICA	107
SINGAPORE	98
JAPAN	72
BRAZIL	64
FRANCE	64
KOREA	55
ITALY	53
RUSSIA	53
UNITED ARAB EMIRATES	50
AUSTRIA	46
NETHERLANDS	45
TAIWAN	42
SPAIN	38

ADVANCED - Advanced Economies: *Countries classified as "advanced" in this report are based on the Human Development Index (HDI), a tool developed by the United Nations to measure and rank countries' levels of social and economic development.*

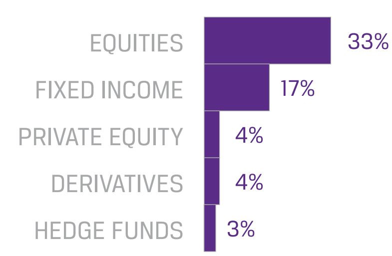
DEVELOPING - Developing Economies: *Countries classified as "developing" in this report are based on a classification system that considers per capita income level, export diversification and degree of integration into the global financial system.*

YEARS WORKING IN THE INVESTMENT INDUSTRY



PRIMARY INVESTMENT PRACTICE

Top 5



JOB FUNCTION

Top 6