Consumer Federation of America

Mutual Fund Purchase Practices

An Analysis of Survey Results
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Executive Summary

Opinion Research Corporation conducted a survey on behalf of CFA as part of a research project funded by the NASD Investor Education Foundation examining mutual fund purchase practices. The survey reveals a gap between how experts recommend investors go about making mutual fund purchase decisions and how investors describe their actual fund selection practices.[1] Significant differences between expert recommendations and actual practices are found in: the factors investors consider when selecting a mutual fund, the extent to which they research their fund purchases using available written information sources, and the degree of reliance they place on the recommendations of financial services professionals. This gap may have significant implications for the development of investor education materials, both by identifying areas where educators need to do a better job of conveying their message, and by identifying areas where expert recommendations are unrealistic or fail to reflect the environment in which different purchase groups make their fund selections.

Factors Considered

Virtually all financial experts (including regulators, personal finance writers, and investor educators) consider a fund's risks, including the volatility of its past returns, and its expenses to be among the most important factors for investors to consider when selecting a fund. Only a third of current owners considered either costs or volatility to be very important when making

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[1] During the initial stage of this project, CFA conducted an extensive review of investor education materials prepared by regulators, fund companies, investor advocates, and personal finance writers. Materials reviewed included brochures, websites, newspaper and magazine articles, and books. That review indicated there is broad agreement among experts about the key factors investors should consider when investing in mutual funds and how they should go about making those selections.

their most recent mutual fund selection, however, and just four in ten considered risks to be very important. Most investors gave more weight to fund company reputation and the past performance of the fund compared with that of other funds. Those who purchased most of their funds directly were significantly more likely than either workplace purchasers or those who purchased most of their funds through a professional to consider costs important. Those who purchased their funds through a financial services professional were more likely than others to consider the fund's past performance compared with that of other funds as very important.

Extent to which Fund Owners Research their Funds

Experts typically recommend that investors carefully review a fund's prospectus before making a fund purchase. At a minimum, fund investors are advised to consider certain key information contained in briefer summary documents describing funds. In addition, fund investors have extensive information available to them from independent third parties, such as the fund ranking services and newspaper and magazine articles. However, none of these written information sources was viewed as highly influential by most current fund investors. While those who purchased most of their funds directly indicated that they got greater value than others from the prospectus, just over a third of even these direct investors rated the prospectus as highly influential and just over half rated the prospectus as either highly or somewhat influential. Those who purchased funds through a workplace-based retirement plan were least likely to describe written materials as influential. In addition, the vast majority of investors in all three groups indicated that they do not take advantage of the independent, third-party information sources available to them. On the other hand, the survey did not support the conventional wisdom that many investors simply select funds from advertisements. Strong majorities rated fund ads as either not very or not at all influential.

Reliance on Advice

Investors rely heavily on advice when selecting funds, doing less research than experts typically recommend in evaluating the recommendations they receive from financial services professionals. Among those who purchased most of their funds from a financial services professional, nearly three in ten said they relied totally on that professional's recommendation without doing any independent evaluation of the fund. Another 36 percent said they relied a great deal on the professional's recommendation but reviewed some written material about the fund before the purchase. Even among those who purchased most of their funds through a workplace retirement plan, where one-on-one expert advice is often not available, such advice outranked other more commonly available information sources as influential to purchase decisions. Women were significantly more likely than men both to value one-on-one expert advice and to act on that advice without doing any additional research.

Attitudes Toward Mutual Funds

A strong majority of current fund owners have positive attitudes toward funds, even though they realize owning funds carries risks and may not always be profitable. In contrast, those who either owned funds in the past but do not now or who indicate they do not ever expect to own funds have far less positive attitudes toward funds. In particular, they are far less likely to view funds as safe or profitable. Those who do not own funds but expect to do so in the future have attitudes toward funds that are neither as positive as those of current owners nor as negative as those of other non-owners.

Use of the Internet

All survey respondents, including non-investors, were asked about their willingness to use the Internet for various activities if they were to purchase a fund in the future. The survey revealed widespread willingness to use the Internet for several mutual fund purchase-related activities. For example, strong majorities of individuals aged 18 to 54 expressed a willingness to use the Internet to obtain general information about mutual funds and to research individual funds. In addition, a majority of individuals in the youngest three age groups (18-44) expressed a willingness to use the Internet to receive reports and disclosure documents and to use a cost calculator.

However, the survey also revealed a widespread lack of willingness to use the Internet among certain groups and for certain purposes. More than two in ten survey respondents indicated they would not use the Internet at all, including a majority of those 65 and older. Among this oldest group, no more than 24 percent indicated they would use the Internet for any of the specific activities listed. Even among the youngest three groups of survey respondents, significantly fewer were willing to use the Internet to communicate with a financial services professional or to purchase funds than for other purposes. And, among current investors who purchased most of their funds from a financial services professional, fewer than half indicated they would be willing to receive periodic reports or disclosure documents for the funds they own over the Internet, and just over a third indicated they would be willing to use the Internet to communicate with their financial services professional.

Purchase Group Profiles

The survey reveals significant differences among the three purchase groups – workplace purchasers, purchasers through professionals, and direct purchasers – in how they approach the purchase process. Some of these differences have important implications for the design and development of investor education materials. The report includes brief profiles of the three purchase groups. (See pages 18-23.)

Introduction

In September 2005, Opinion Research Corporation conducted a survey of consumer use of mutual fund information sources. The survey was administered to a representative sample of 2,048 adult Americans, including both individuals who currently invest in mutual funds and those who do not. It was conducted for the Consumer Federation of America (CFA) as part of a research project funded by the NASD Investor Education Foundation.[2]

The survey included questions on the factors mutual fund investors consider when selecting funds and the information sources on which they rely in making those selections. In addition, both investors and non-investors were asked about the sources they would be likely to consult for information and advice if they were to make a mutual fund purchase in the near future. The entire sample was also asked about their willingness to use the Internet for various mutual fund purchase-related activities. The following is a summary of key survey findings.

General Characteristics of Mutual Fund Investors

Of the entire sample of 2,048 adult Americans, 43 percent identified themselves as current owners of mutual funds. Another 15 percent indicated that they do not currently own mutual funds but expect to in the future, 12 percent said they had owned mutual funds in the past

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[2] The survey was developed by CFA with extensive input from members of an advisory group assisting the research project. The advisory group included the following members: Don Blandin, President and CEO, Investor Protection Trust; Mercer Bullard, Founder and President, Fund Democracy, Inc.; Denise Voigt Crawford, Texas Securities Commissioner; Timothy Forde, Vice President of Fund Administration, Capital Research and Management Company; John Gannon, Secretary, NASD Investor Education Foundation; Mellody Hobson, President, Ariel Capital Management; William Lutz, Professor of English, Rutgers University; Don Phillips, Managing Director, Morningstar, Inc.; John Rea, Chief Economist (retired), Investment Company Institute; Dallas Salisbury, President and CEO, Employee Benefit Research Institute; and Tom Selman, Senior Vice President, NASD. In addition, Susan Wyderko, then Director of the Securities and Exchange Commission's Office of Investor Education and Assistance, and Susan Nash, Associate Director of the SEC's Division of Investment Management, acted as observers. The advisory group and observers assisted in analysis of initial research on mutual fund investor education materials and disclosure documents, development of the survey instrument, and analysis of survey findings. CFA gratefully acknowledges their contributions. However, participation as an advisory group member or observer does not imply endorsement of the survey report.

but do not currently own mutual funds, and 25 percent said they had never owned mutual funds and do not intend to own funds in the future. Five percent answered "Don't know."

Purchase Method: Workplace-based retirement plans are the most common means of obtaining mutual funds. Among current mutual fund owners, 58 percent had obtained most of their funds through a workplace-based retirement plan, 28 percent had purchased most of their funds through a financial professional such as a broker or financial planner, 8 percent had bought most of their funds either directly from a fund company or through a discount broker or fund supermarket, and 4 percent had inherited most of their funds.

Length of Ownership: Most fund owners have owned funds for a considerable time. Nearly half (48 percent) of all current mutual fund owners said they had owned mutual funds for more than ten years. A little over a quarter (27 percent) of current mutual fund owners said they had owned funds for five to ten years, and one quarter (25 percent) said they had owned funds for five years or less, including just 5 percent who said they had owned funds for two years or less. Those who purchased most of their funds at work were significantly more likely than others to have owned funds for five years or less, while those who purchased most of their funds directly were significantly more likely than others to have owned their funds for ten years or more.

Size of Fund Holdings: Mutual fund owners' household fund holdings are fairly modest in light of the long time many individuals have been investing in funds and the level of assets experts estimate people need to retire comfortably. Over one-third (35 percent) of current fund owners have $25,000 or less invested in funds, and nearly half (48 percent) have $50,000 or less invested in funds.[3] Mutual fund investors' retirement plan fund assets are even more modest. Among those who purchased most of their mutual funds through a workplace-based retirement plan, nearly six in ten (56 percent) indicated they had $50,000 or less in mutual fund retirement plan assets, including 40 percent with $25,000 or less in mutual funds in these accounts.

Table 1: Current Owners' and Workplace Purchasers' Mutual Fund Assets

	$25,000 or less	**$25,000-$50,000**	**$50,000-$100,000**	**$100,000 or more**	**Don't know**
Current owners' household fund assets	35%	13%	14%	20%	18%
Workplace purchasers' retirement plan fund assets	40%	16%	14%	14%	16%

[3] This includes money held both inside and outside workplace-based retirement plan accounts.

Knowledge of Mutual Funds: Approximately two-thirds (66 percent) of current mutual fund owners indicated they know either a great deal or a fair amount about mutual funds.[4] Of these, 14 percent expressed confidence that they know a great deal about mutual funds, and 52 percent said they know a fair amount. On the other hand, only 4 percent said they know nothing about funds. Not surprisingly, those who have never owned funds and never intend to have much lower levels of self-reported knowledge about funds, with nearly half (48 percent) indicating they know nothing about funds. Those who expect to own mutual funds in the future had self-assessed knowledge levels that fell largely in the middle. A third (34 percent) said they know a fair amount about mutual funds, and four in ten (40 percent) said they knew a little about funds.

Table 2: Self-Assessed Knowledge of Mutual Funds

	Great Deal	Fair Amount	Little	Nothing
Current Owners	14%	52%	30%	4%
Past Owners	12%	47%	35%	5%
Future Owners	6%	34%	40%	20%
Never Owners	5%	14%	33%	48%

Conventional wisdom suggests that those who purchase funds through workplace-based retirement plans are significantly less knowledgeable than other mutual fund investors. However, these fund owners expressed confidence in their knowledge that was equivalent to that of those who purchase through financial professionals. Roughly two-thirds of both groups (66 percent of workplace purchasers and 68 percent of those who purchased through a financial services professional) said they knew either a great deal or a fair amount about mutual funds. Those who purchased most of their funds directly expressed the greatest confidence in their fund knowledge, with 77 percent saying they knew either a great deal or a fair amount about funds. Nearly three times as many direct purchasers (33 percent) said they knew a great deal about funds as either workplace purchasers (12 percent) or those who purchased from a financial services professional (13 percent).

General Demographic Characteristics: The survey found significant demographic differences between the various mutual fund ownership categories – i.e., current owners, future owners, past owners, and those who never expect to own mutual funds. For example, current mutual fund owners on average

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[4] The survey did not attempt to assess respondents' actual knowledge levels. It asked only for respondents to assess their own knowledge level. Typically, surveys that have tested investor knowledge have found actual knowledge levels that are significantly lower than self-assessed knowledge.

are older, are better educated, and have higher incomes than future owners. Those who say they never expect to own funds are significantly older than future owners. While their education level is comparable to that of future owners, they are significantly less likely than either current or future owners to be employed full-time, and their mean income is substantially lower than that of the other groups. Past owners are significantly less likely than either current or future fund owners to be employed full-time. They are far more likely than either of these groups to be retired. Their mean income is higher than that of those who never expect to own funds, but lower than that of current owners. They are also slightly older than current owners.

Table 3: Age, Education, and Income by Ownership Category

	Current Owners	Future Owners	Past Owners	Never Owners
Mean Age	46.2	33.2	50.3	48.0
Mean Income	$66,500	$42,900	$47,800	$37,400
% with At Least a Bachelor's Degree	49%	17%	26%	17%

The survey indicates that minorities, particularly African Americans, expect to increase their fund ownership in the future. Most notably, a quarter (25 percent) of those who identify themselves as future owners of mutual funds are African American, compared with just 8 percent of current owners. Similarly, 17 percent of those who identify themselves as future fund owners are Spanish, Hispanic, or Latino, compared with just 8 percent of current owners. While the percentage of future owners who are Spanish, Hispanic, or Latino is comparable to the percentage of those who never expect to own mutual funds who fall within this group, the percentage of future owners who are African American (25 percent) is more than twice as high as the percentage of those who never expect to own funds who are African American (11 percent).

Attitudes toward Mutual Funds

All survey respondents were asked a series of questions about their attitudes toward funds. Specifically, they were asked to rate on a one-to-five scale whether their views toward funds are generally favorable or unfavorable, whether they view funds as safe or risky, whether they view funds as profitable or unprofitable, and whether they view funds as easy or difficult to purchase.

A large majority of current mutual fund owners have positive attitudes toward mutual funds. At the same time, many of these owners express an understanding that there are risks associated with owning mutual funds, including the risk that they will not always be profitable. In contrast, past fund owners and those who never expect to own funds have significantly less positive views of funds. Those who indicated that they expect to own funds in the future have attitudes that fall somewhere in the middle –

not as positive as those of current owners but more positive than those of other non-owners. One exception involves attitudes towards the ease of purchasing funds. Similar percentages of future owners (20 percent) and other non-owners (19 percent) view funds as either very or somewhat difficult to purchase. Only five percent of current owners view funds as very or somewhat difficult to purchase.

Table 4: Attitudes toward Mutual Funds among Owners and Non-Owners

	Current Owners	Past/Never Owners	Future Owners
Favorable/Unfavorable	64/8	27/25	52/16
Safe/Risky	44/10	20/26	38/19
Profitable/Unprofitable	47/9	23/19	43/12
Easy/Difficult to Purchase	72/5	36/19	42/20

Note on Data: The first number in each entry represents the percentage of 4s or 5s for each category. The second number represents the percentage of 1s and 2s.

Among current owners, those who purchased their funds directly from a fund company or through a discount broker or fund supermarket expressed the most positive views toward mutual funds. Nearly seven in ten (68 percent) of these investors had either a somewhat or very positive view of funds, including more than four in ten (42 percent) who had a very positive view. While the survey did not reveal significant differences among purchase groups in perceptions of fund risks or profitability, it did reveal that those who purchase funds through work are significantly less likely to view funds as easy to purchase. Specifically, well under half (44 percent) of those who purchased most of their funds through a workplace-based retirement plan said funds were very easy to purchase, compared with roughly six in ten of both direct purchasers and those who purchased through a financial professional.

Among the general population, including both investors and non-investors, those 65 and older express significantly less positive attitudes toward mutual funds than younger respondents. Only 34 percent of those 65 and older said they view funds either somewhat or very favorably, compared with 48 percent of the entire sample, while nearly a quarter (23 percent) said they view them either somewhat or very unfavorably. They were particularly likely to view funds as risky and unprofitable. This may reflect the fact that this age group is significantly less likely than younger groups to have been introduced to funds through a workplace retirement plan.

Those who rate themselves as knowing either a great deal or a fair amount about mutual funds tend to have the most positive views toward funds. In particular, they are disproportionately likely to regard funds as relatively safe and profitable. While these individuals make up only 47 percent of the total sample, they account for 62 percent of those who rate funds as somewhat or very safe, and 58 percent of those who view funds as somewhat or very profitable. These findings, along with the generally positive attitudes among current owners, seem to indicate that greater familiarity with mutual funds is associated with more positive attitudes.

Factors Investors Consider When Selecting a Fund

A primary goal of the survey is to better understand how mutual fund investors go about making their investment decisions. With that in mind, the survey asked all current owners of mutual funds how significant each of five factors was in their most recent mutual fund purchase decision. Those factors were the fund's risks, the fund's performance compared with that of other funds, the reputation of the fund company or fund manager, the volatility of the fund's past returns, and the fund's expenses. Respondents were asked to rate the importance of each factor to their purchase decision on a five-point scale from not at all important to very important.

Virtually all financial experts consider a fund's risks and its expenses to be among the most important factors for investors to consider when selecting a mutual fund. They typically identify the volatility of a fund's past returns as one of the best measures of risk. But just under a third of current mutual fund investors (32 percent) considered expenses to be very important when making their most recent mutual fund purchase, the same number considered volatility to be very important, and just under four in ten (39 percent) considered the fund's risks very important. Approximately one-third of investors (31 percent) did not consider a fund's risks even somewhat important. More than a third (35 percent) did not consider the volatility of its past returns even somewhat important. And four in ten (41 percent) did not consider a fund's expenses even somewhat important. Investors gave higher priority to the reputation of the fund company or fund manager and to the fund's past performance compared with that of other funds, factors most financial experts consider to be somewhat less important.

The survey also revealed significant differences among the different purchase groups regarding the factors members of those groups considered when selecting a fund. Investors in all three groups gave greatest weight to the reputation of the fund company or fund manager in making their selection, but direct investors gave by far the greatest weight to this factor. Direct purchasers were also significantly more likely than members of other groups to weigh expenses when selecting a fund. Those who purchased most of their funds through a financial services professional were more likely than others to view a fund's past performance compared with that of other funds as very important to their purchase decision.

See Table 5 on the following page for detailed findings.

Table 5: Percentages of Investors who Rated Various Factors as Very or Somewhat Important to their Most Recent Mutual Fund Purchase

	Current Owners	Direct Purchasers	Purchasers through a Professional	Workplace Purchasers
Fund Company Reputation	52/23	72/16	59/21	46/24
Fund Expenses	32/22	50/24	33/22	30/21
Past Performance	41/30	39/41	49/26	38/30
Fund Risks	39/26	46/25	43/31	36/24
Volatility	32/30	30/27	31/30	32/30

Note on Data: The first number in each entry represents the percentage who rated the factor as very influential (5). The second number represents the percentage who rated the factor as somewhat influential (4).

Importance of Advice

Investor advocates and other experts counsel investors to research the funds recommended to them by financial services professionals, on the grounds that some professionals may have conflicts of interest that could bias their recommendations. According to the survey, however, investors typically do little independent research of the funds recommended to them by professionals. Nearly three in ten (28 percent) current mutual fund owners who purchased most of their funds through a financial services professional said they relied totally on that professional's recommendation, without doing any additional research. Another 36 percent said they relied a great deal on the recommendation of the financial services professional, but reviewed some written material about the fund before the purchase. For this latter group, it is impossible, based on the results of this survey, to know for certain what types of material they reviewed. While that written material could include a fund prospectus or Morningstar report, it could also simply consist of marketing material.

Women were more likely than men to say they relied totally on the recommendation of a professional. Nearly one-third (32 percent) of women who purchased through a financial professional said they relied totally on that professional's recommendation, compared with 23 percent of men. Men were more likely to say they relied a great deal on the professional's recommendation. Nearly four in ten men (39 percent) compared with one-third of women (32 percent) said they relied a great deal on the professional's recommendation.

This heavy reliance on expert advice can be seen even among mutual fund owners who purchased most of their funds through a workplace retirement plan. Although many of these investors do not have access to one-on-one expert advice in selecting mutual funds, those who do appear to rely heavily on their recommendations. For example, nearly half (45 percent) of those who purchased most of their funds through a workplace retirement plan said one-on-one advice from an expert that they consulted outside the workplace was either a very influential (22 percent) information source in choosing their workplace mutual fund investments or somewhat influential (23 percent). Slightly fewer said one-on-one advice from an expert consulted at the workplace was either very (20 percent) or somewhat (18 percent) influential. Furthermore, expert advice was either as influential as or more influential than other information sources that are more commonly available, such as written and website materials provided by employers, information sought out by the investor, or information provided in workplace seminars.[5]

Table 6: Percentages of Workplace Purchasers Who View Various Sources of Information as Influential or Not Influential

	Expert away from work	**Expert at work**	**Written material from employer**	**Written material found on own**	**Workshop at Work**	**Friends, Family, Fellow Workers**
Very/Somewhat Influential	22/23	20/18	18/21	14/23	13/17	13/14
Not Very/Not at All Influential	7/22	9/25	12/17	12/24	13/29	17/29

Note on Data: In the first row of entries, the first number represents those who rated the information sources as very influential (5), and the second number represents those who rated the information sources as somewhat influential (4). In the second row of entries, the first number represents those who rated the information sources as not very influential (2), and the second number represents those who rated the information sources as not at all influential (1).

Women's tendency to place greater value on expert advice was evident among those who purchased most of their funds through a workplace-based retirement plan. Nearly half of these women (49 percent) said one-on-one advice from an expert away from work was either very or somewhat influential to their most recent retirement plan mutual fund purchase, compared with just 40 percent of men. More than four in ten women (45 percent) said one-on-one advice from an expert at work was

[5] The term expert in this case does not necessarily refer to a financial services professional, as the term was not defined. It could, for example, refer to a human resources employee. However, the question did refer specifically to one-on-one advice and did distinguish between an expert and friends and colleagues.

either very or somewhat influential, compared with less than a third of men (31 percent). And more than a third of women (35 percent) compared with just a quarter of men (25 percent) said information provided in a workplace seminar was very or somewhat influential. In contrast, men were much more likely to conduct their own research and rely on written and website publications. Four in ten men (41 percent) said information that they found on their own on a website or in a printed publication was very or somewhat influential, compared with less than a third (32 percent) of women.

The less affluent also expressed both a greater reliance on advice and a greater interest in obtaining advice. For example, workplace purchasers with incomes under $50,000 were significantly more likely than those with higher incomes to have been influenced by one-on-one advice from an expert at work or information obtained in a workplace seminar, while those with incomes over $50,000 were more likely to have relied on information on a website or in a printed publication they found on their own. When the entire sample was asked about sources of advice they would be likely to turn to if they were to make a fund purchase in the future, those with incomes between $25,000 and $50,000 were more likely than those with higher incomes to indicate they would definitely turn to each type of financial services professional. This is true, despite the fact that these individuals are less likely to be able to afford the services of such professionals.

Value of Various Written Materials

Experts almost universally recommend that investors carefully review the fund prospectus before purchasing a mutual fund. In addition to the prospectus, mutual fund investors have a variety of written materials available to assist them in selecting mutual funds. These include briefer fund summary documents prepared both by the fund companies and by independent parties, ranking services such as Morningstar and Lipper, and newspaper and magazine articles evaluating funds. In addition, many fund companies advertise widely, often including performance information and fund ratings in the ads.

The survey asked current mutual fund investors who purchased most of their funds how influential each of these documents was in their most recent mutual fund purchase. Supporting the view that mutual fund investors do relatively little research when selecting mutual funds, none of these documents was viewed as highly influential by most current fund investors. On the other hand, the survey did not support the conventional wisdom that many investors simply select funds from advertisements. Strong majorities in all three categories (71-75 percent) said ads were either not very or not at all influential.

As expected, those who purchased funds either directly from the fund company or through a discount broker or fund supermarket indicated the greatest willingness to research funds using available written materials. Over one-third of these investors (37 percent) rated the prospectus as highly influential, and more than half (55 percent) rated it as either somewhat or highly influential. That still leaves more than four in ten (43 percent) of these investors who did not consider the prospectus, the fund's primary disclosure document, even somewhat influential. Direct purchasers also gave much higher ratings than those who purchased through other methods to the independent ranking services, such as Morningstar or

Lipper. Still, only two in ten (19 percent) rated these ranking services as highly influential, and under half (46 percent) rated them as either highly or somewhat influential.

Those who purchased most of their funds through an employer-sponsored retirement plan were least likely to rate written materials as highly influential. None of the documents evaluated in the survey was rated highly influential by more than two in ten workplace purchasers. The prospectus was described as very influential by 19 percent, followed by the brief summary document (16 percent), and ranking services (11 percent). Moreover, more than half of investors who purchased through retirement plans did not consider any of the documents as even somewhat influential. Just over half (52 percent) did not consider the prospectus even somewhat influential. Nearly six in ten (59 percent) did not consider brief summary documents as even somewhat influential. Nearly seven in ten (68 percent) did not consider ranking services even somewhat influential. This makes some sense, given the relatively limited choices most retirement plan investors have available to them. It is also consistent with the preference workplace purchasers expressed on a separate question for advice rather than written documents (See "Importance of Advice" above).

Those who purchased most of their funds through a financial services professional were significantly more likely than the others to rate briefer summary documents highly. Specifically, more than half (55 percent) rated the briefer summary documents as either somewhat or very influential, including nearly one quarter (23 percent) who rated them as very influential. The prospectus was next behind summary documents, rated somewhat or very influential by 44 percent, including 22 percent who rated it as very influential. Less than a third rated any of the other documents as somewhat or very influential.

Table 7: Percentage of Investors in Different Purchase Groups Who Viewed Various Documents as Either Very or Somewhat Influential

	Direct Purchasers	Purchasers through a Professional	Workplace Purchasers
Prospectus	37/18	22/22	19/24
Fund Summary	18/15	23/32	16/23
Ranking Service	19/27	13/17	11/15
Magazine article	12/13	6/15	6/15
Fund ad	4/2	3/3	3/3

Note on Data: In each entry, the first number represents the percentage who rated the document as very influential. The second number represents the percentage who rated the document as somewhat influential.

In addition, the entire survey sample was asked what documents they would consult if they were to purchase a mutual fund and the documents were readily available. The briefer summary document was viewed most favorably, rated as being of great interest by 23 percent and as of some or great interest by

46 percent. The prospectus followed, considered of great interest by 20 percent and of some or great interest by 35 percent. The prospectus's negatives, however, were very high. More than four in ten (41 percent) rated the prospectus as of little or no interest, compared with just 26 percent for the briefer fund summary document. Women were more likely than men to favor the brief summary, and men were more likely than women to favor the full prospectus.

Survey respondents showed particularly little interest in the independent sources of information available to assist them with their fund purchases. Among these categories (ranking services, general information about funds, and magazine or newspaper articles rating funds), only ranking services were viewed as of some or great interest by at least a third of survey respondents (34 percent). Interestingly, this is a significantly higher rating from hypothetical investors than ranking services received from any of the actual fund purchasers except the direct purchasers. (Unlike the previous questions about investors' actual experiences in selecting funds, this survey question is premised on the ready availability of the information sources, which may contribute to the discrepancy.)

The survey also reveals significant differences in attitudes toward these information sources between current owners and those who do not currently own funds but expect to in the future. In particular, future owners expressed far greater enthusiasm than current owners for the briefer fund summary documents. More than a third (35 percent) of future owners rated these documents as being of great interest, and more than six in ten (62 percent) rated them as being of either some or great interest. In contrast, fewer than two in ten current owners (19 percent) rated them of great interest, and just under half (49 percent) rated them as either of some or great interest. Future owners also expressed greater interest in mutual fund ranking services (47 percent rated them as either of great or some interest, compared with 36 percent of current owners), general information about mutual funds (48 percent compared with 28 percent), and newspaper and magazine articles rating funds (43 percent compared with 25 percent). A variety of factors could explain this difference, including perhaps an overly optimistic view among future investors of the amount of research they are likely to be willing to do once it comes time actually to make a fund purchase or a less favorable view of the value of existing written documents among current investors who have actually been exposed to them. However, these results do suggest a possible opening to reach future fund investors with well designed abbreviated disclosure documents as well as easily accessible education materials.

Sources of Advice for Future Purchases

The entire survey sample was asked from whom they would be likely to seek advice if they were to purchase a mutual fund. By far the largest number indicated they would be likely to consult a financial planner, with one-third (33 percent) indicating they definitely would consult a financial planner and another quarter (24 percent) indicating they probably would do so. This is significantly more than indicated they would consult a stockbroker (the second highest ranking source of advice). Just two in ten (19 percent) indicated they definitely would consult a broker, and another 18 percent indicated they probably would do so. Brokers' negatives were also much higher than the negatives for financial planners, with nearly four in ten (38 percent) saying they either definitely or probably wouldn't consult a broker for advice compared with just over two in ten (22 percent) for financial planners. In considering these findings, it is important to keep in mind that investors do not clearly distinguish between brokers and financial planners.

Survey respondents were fairly evenly divided in the likelihood that they would consult brokers, banks or credit union representatives, accountants, and friends and family members (with numbers of those who would definitely or probably consult each group ranging from a high of 37 percent for brokers to a low of 30 percent for friends, family members and coworkers). Far fewer indicated they would be likely to consult an insurance agent, with only 10 percent saying they would definitely do so and 18 percent saying they would either definitely or probably do so. More than half (57 percent) said they either probably or definitely would not consult an insurance agent for advice.

In each category, future owners were more likely than current owners to say they either definitely or probably would consult that particular type of financial services professional. This likely reflects the greater uncertainty that these investors bring to a purchase process they have not yet engaged in. Current owners are more likely to know how they would approach their next purchase than those who have never made such a purchase. Interestingly, the most marked difference between the two groups was seen in their attitude toward consulting a representative of a bank or credit union. More than twice as many future owners (52 percent) as current owners (24 percent) indicated they would either definitely or probably consult a bank or credit union representative when making a mutual fund purchase. The least marked difference between the two groups was seen in their attitude toward financial planners, with 63 percent of current owners and 71 percent of future owners indicating they either definitely or probably would consult a member of this profession.

Reflecting the same value they place on advice that they revealed on other questions, women were more likely than men to indicate they would consult each type of financial services professional, with the exception of insurance agents. The difference was particularly notable with regard to financial planners, where 36 percent of women, compared with 30 percent of men, said they would definitely consult a financial planner for advice.

Use of the Internet

Policymakers are increasingly looking to the Internet to reduce the cost and increase the ease of communicating with investors. Already, an enormous amount of valuable information is available online to assist mutual fund investors in making fund selections. Not only can prospectuses be downloaded, but many fund companies provide on-line fund snapshots that make key information about the fund easily accessible. In addition, fund ranking services and others offer tools for evaluating funds, including calculators that enable investors to compare the costs of various funds. The entire sample of survey respondents was asked about their willingness to use the Internet for various purchase-related activities.

Survey respondents were most interested in using the Internet to obtain general information about funds (59 percent) and to research individual funds (58 percent). Fewer than half of survey respondents expressed a willingness to use the Internet for any of the other suggested activities, including: to receive periodic reports and disclosure documents (49 percent), to use a calculator to compare costs (47 percent), to communicate with a financial services professional (39 percent), or to purchase mutual funds (26 percent). More than two in ten survey respondents (21 percent) said they would not use the Internet at all.

As expected, younger people are significantly more likely than older people to be willing to use the Internet. For example, roughly three-quarters of respondents in the 18-24, 25-34, and 35-44 age groups would plan on using the Internet to obtain general information about mutual funds or to research individual mutual funds. Six in ten (61 percent) of those age 45-54 would do so. In contrast, just 45 percent of those age 55 to 64, would use the Internet for these purposes, and less than a quarter of those age 65 and older would do so.

Younger respondents also express greater willingness than others to use the Internet for purposes beyond research. For example, roughly six in ten survey respondents in the youngest three age groups said they would use the Internet to receive periodic reports and disclosure documents about mutual funds they owned or to use a fund cost calculator. Even among younger respondents, however, only about half or less said they would use the Internet to communicate with a financial services professional, and just over a third said they would use the Internet to purchase mutual funds.

See Table 8 on the following page.

Table 8: Willingness of Different Age Groups to Use the Internet for Various Mutual Fund Purchase-Related Activities

	18-24	25-34	35-44	45-54	55-64	65+
Obtain general info	72%	74%	73%	61%	45%	24%
Research individual funds	77%	69%	71%	62%	45%	22%
Receive reports, documents	57%	61%	62%	50%	36%	21%
Use cost calculator	64%	58%	56%	45%	35%	19%
Communicate with professional	53%	43%	45%	43%	34%	17%
Purchase funds	38%	34%	33%	21%	18%	9%
Would not use	6%	10%	9%	20%	32%	54%

Men were also significantly more willing than women to use the Internet for various mutual fund activities. Just 16 percent of men, compared with 26 percent of women, said they would not use the Internet for any purpose. For each of the activities included in the survey except one, significantly more men than women said they would be willing to use the Internet. The exception was using the Internet to communicate with a financial services professional, where men were only slightly more likely than women to say they would use the Internet for this purpose. Despite men's greater willingness to use the Internet, fewer than half indicated they would be willing to use the Internet to communicate with a financial services professional (40 percent) or to purchase a mutual fund (31 percent), and just over half (53 percent) said they would use the Internet to receive periodic reports and disclosure documents about mutual funds they own.

The question about willingness to use the Internet was asked of all survey respondents. This included those individuals who indicated they had never owned funds and never planned to, a group with the most negative attitudes overall toward use of the Internet. When looked at separately, current owners and future owners expressed significantly greater willingness than the overall population to use the Internet. In particular, current owners expressed greater willingness than the overall population to use the Internet to obtain general information about mutual funds, to research individual funds, and to receive periodic reports and disclosure documents for funds they own. On the other hand, their willingness to use the Internet to use a cost calculator, communicate with a financial services professional, or purchase funds was roughly the same as that of the general population. Those who indicated they expect to own funds in the future, a younger group than current owners, expressed the greatest willingness to use the Internet for mutual fund purchase-related activities. In contrast to other ownership groups, two-thirds of future owners expressed a willingness to use the Internet to compare costs using a cost calculator, nearly two-thirds expressed a willingness to use the Internet to receive periodic reports, and more than half expressed a willingness to use the Internet to communicate with a financial services professional.

Table 9: Willingness to Use the Internet among Current and Future Mutual Fund Owners

	Overall Population	Current Owners	Future Owners
Obtain general info	59%	66%	74%
Research individual funds	58%	65%	74%
Receive reports, documents	49%	56%	63%
Use cost calculator	47%	48%	67%
Communicate with professional	39%	42%	56%
Purchase funds	26%	27%	40%
Would not use	21%	16%	9%

Among the three purchase groups, those who purchased most of their funds through a workplace retirement plan expressed the greatest willingness to use the Internet for at least some purchase-related activities. The vast majority of these investors (87 percent) indicated they would be willing to use the Internet. This may reflect in part the younger age of these investors as well as widespread use of the Internet as the primary tool for managing workplace retirement accounts. Internet use also has high acceptance among the other two purchase groups, with 80 percent of direct investors and 73 percent of those who purchased most of their funds from a financial services professional indicating they would be willing to use the Internet for at least some purposes. However, this willingness does not extend to all uses. Among current investors who purchased most of their funds from a financial services professional, for example, fewer than half (48 percent) indicated they would be willing to receive periodic reports or disclosure documents for the funds they own over the Internet, and just over a third (36 percent) indicated they would be willing to use the Internet to communicate with their financial services professional.

In order to understand which of various demographic factors have the greatest influence on investors' willingness to use the Internet, CFA conducted a tri-variate analysis of the survey findings for current and future fund owners.[6] Factors analyzed included age, income, education, race, and ethnicity. As expected, the analysis showed that age is the biggest variable affecting willingness to use the Internet. In particular, there is a consistent and significant drop-off in willingness to use the Internet after age 65. This is true for each type of use except fund purchase, which has strong negatives across virtually all age groups. The tri-variate analysis also showed a fairly strong association between both education and income and willingness to use the Internet. Race and ethnicity, on the other hand, had no identifiable influence.

Purchase Group Profiles

The survey revealed distinct differences between the three purchase groups in a variety of areas, many of which have been described in the body of the report above. This suggests that different approaches to investor education and information will be needed to communicate effectively with these groups. In order to facilitate thinking about how to develop investor education and information practices targeted at each group, we are including brief profiles of these three purchase groups here. These profiles will largely repeat information scattered throughout the report, but consolidate that information in one place and provide greater detail.

Direct Purchasers: Among current mutual fund owners identified by the survey, eight percent indicated they had purchased most of their mutual funds directly from the fund company or through a discount broker or fund supermarket. These investors are somewhat older (mean age 54.7), wealthier (mean income $70,100), and better educated than other investors (86 percent have at least some college education and 64 percent have at least a bachelor's degree). Half of direct purchasers are employed full time, and more than a third (37 percent) are retired. They are disproportionately male (64 percent). Although they have a high degree of Internet usage (79 percent), it is the lowest of the three purchase groups – perhaps reflecting their somewhat older age. Of those who use the Internet, 75 percent use it at home, 48 percent use it at work, and 44 percent use it both at home and at work.

[6] Current fund owners were divided into two groups for the purpose of this analysis, workplace purchasers and retail purchasers. The latter category included both those who purchased most of their funds directly and those who purchased most of their funds through a financial services professional.

Direct purchasers have, on average, owned mutual funds for longer than members of the other two purchase groups. Nearly three-quarters (72 percent) of direct purchasers have owned funds for more than ten years. Only 10 percent have held funds for less than five years. The mean length of ownership for direct purchasers is 10.3 years. They also have larger fund holdings. A third of direct purchasers have over $100,000 in total household fund holdings. The mean amount of household fund holdings for direct purchasers is $68,500.

Direct purchasers are the most likely of the three groups to view themselves as very knowledgeable about mutual funds. This is not surprising, since confidence in their level of knowledge would make it far more likely that someone would take on the task of selecting mutual funds without the assistance of a financial services professional. A third of direct purchasers rate themselves as very knowledgeable. They have the most favorable attitude toward funds. More than four in ten direct purchasers (42 percent) indicate they have a very favorable view of funds. They are also most likely to indicate that purchasing funds is very easy (63 percent), even though this purchase method requires them to do considerably more work than is typical for either workplace purchasers or those who purchase through a financial services professional.

Direct purchasers are the only group to give fund costs significant weight in their purchase decision. This is logical, since minimizing costs is a primary reason to purchase funds directly. Half of direct investors considered fund costs very important to their last fund purchase decision, and three-quarters (74 percent) considered costs at least somewhat important. That said, direct purchasers gave greater weight to the reputation of the fund company or manager. Nearly three-quarters (72 percent) considered reputation very important. Since fund company reputation, particularly in the direct purchase market, may be based in significant part on low costs, investing based on reputation may have the same effect as investing based on costs. (On the other hand, some investors may interpret investing based on personal finance magazine articles featuring the latest "hot" funds as investing based on reputation.) The survey does not allow us to distinguish between these factors.

Consistent with their other characteristics, direct purchasers are the most likely of the three groups to place significant reliance on written materials to research their fund selections. In particular, they are more likely than members of other groups to consider the fund prospectus and mutual fund ranking services as influential. Just over a third of direct purchasers considered the prospectus to have been very influential in their last fund purchase, and 55 percent considered the prospectus somewhat influential. Nearly half (46 percent) considered the fund ranking services to be at least somewhat influential. Although this represents greater use of these materials than was found in other groups, it still seems to indicate that a significant number of direct purchasers are not doing extensive research of the funds they purchase.

Much of the existing investor education materials appear to have been written with this relatively small group of investors in mind. Certainly, their purchase practices most closely resemble those advocated by many experts. Indeed, the recommendation to reduce costs by investing directly is an explicit message of many investor education materials. Nonetheless, gaps can be seen between how experts recommend investors select funds and how even these direct purchasers go about that process. For example, a significant number of these investors appear to be ignoring the message to carefully review the fund prospectus before purchasing a fund. Nearly half (45 percent) did not consider the prospectus even somewhat influential to their most recent fund purchase. Fund risks join fund costs at the top of the list of factors experts recommend investors consider and understand when selecting a fund. While a large majority (71 percent) considered fund risks at least somewhat important to their most recent fund purchase, fewer than half (46 percent) considered fund risks very important. Many appear to be giving little if any consideration to the volatility of past returns – a factor experts typically equate with fund risk. Only three in ten (30 percent) considered volatility very important, and less than six in ten (58 percent) considered it even somewhat important. They were more likely to be influenced by how a fund performed compared to other funds, a practice experts often warn against. Eighty percent considered past performance at least somewhat important, including 39 percent who considered it very important. This suggests that, even with this group, there is a significant gap between expert recommendations and actual investor practices.

Purchasers through Professionals: Just under three in ten survey respondents (28 percent) indicated that they had purchased most of their funds through a financial services professional, such as a broker or financial planner. In their general demographic characteristics, these investors are similar to direct purchasers but are slightly younger, slightly less wealthy, and somewhat less well educated. The mean age of those who purchase funds through professionals is 51.6. Their mean income is $67,600. More than three-quarters (77 percent) have at least some college education, including 54 percent with at least a bachelor's degree. More than half (52 percent) are employed full-time, and 28 percent are retired. In contrast to direct purchasers, who are disproportionately male, those who purchase through professionals are slightly more likely to be female (53 percent).

Purchasers through professionals have less money, on average, invested in mutual funds than direct purchasers and have not owned funds for as long. Just over half of this group has owned funds for ten years or more (53 percent). The mean length of ownership for purchasers through professionals is 9.1 years. The mean amount they have invested in funds is $57,300. Roughly a quarter (24 percent) has more than $100,000 in total household mutual fund holdings.

A defining difference between direct purchasers and those who purchase through a professional is their confidence in their level of knowledge about mutual funds. Only 13 percent of those who invest through a professional rate themselves as very knowledgeable. They also have a less favorable view of mutual funds. Only 30 percent have a very favorable view of mutual funds.

When purchasing funds, those who purchase through a professional appear to give greater weight than others to how a fund performed in the past compared to other funds – a factor experts often suggest investors should de-emphasize. Nearly half (49 percent) considered past performance very important. However, they were slightly less likely than direct purchasers to consider past performance at least somewhat important. Three-quarters (74 percent) of those who purchased through a professional, compared with 80 percent of direct purchasers, considered past performance at least somewhat important. Those who purchase through a professional gave little weight to fund costs, which in their case include sales charges as well as fund operating expenses. Only a third (33 percent) considered costs very important, and just over half (55 percent) considered costs even somewhat important.

Those who purchase through professionals appear to make little use of written materials when selecting funds. This is consistent with the fact that a majority of these investors indicate that they rely either totally (28 percent) or heavily (36 percent) on the recommendation of their professional when selecting funds. Less than a quarter of these investors rated any of the written materials as very influential to their most recent mutual fund purchase. They were most likely to consider fund summaries as influential, with 23 percent rating a fund summary as very influential and 55 percent rating a summary as at least somewhat influential. Less than half (44 percent) considered the fund prospectus as even somewhat influential, including 22 percent who considered it very influential. This latter finding is not surprising, since those who invest through a financial professional typically do not receive the prospectus until after the sale.

Although a large majority (82 percent) of these investors uses the Internet at home, at work, or both, somewhat fewer (73 percent) indicated they would be willing to use the Internet for at least some mutual fund purchase-related activities. Significantly, fewer than half of these investors (48 percent) indicated they would be willing to use the Internet to receive periodic reports and disclosure documents about mutual funds they own. Even fewer (36 percent) indicated they would be willing to use the Internet to communicate with a financial services professional.

Although roughly three-quarters of retail fund purchasers buy most of their funds through a professional, most existing mutual fund investor education materials do not appear to have been designed with these investors in mind. Logic suggests that individuals who expect to rely heavily or exclusively on the recommendations of a financial professional are unlikely to heed advice to carefully research their funds by reading the prospectus and comparing costs, risks, and investment objectives of various funds recommended. This supposition appears to be borne out both in the purchase practices and preferences described by survey respondents who purchase most of their funds through a professional. Consideration should be given to development of investor education materials that take these investors' attitudes and behavior into account.

Workplace Purchasers: The largest group of current fund holders identified by the survey (58 percent) indicated that they had purchased most of their funds through a workplace-based retirement plan, such as a 401(k) plan. Consistent with the fact that most first-time fund purchases are made through such a plan, these investors are significantly younger (mean age 43.1) than members of the other two groups. Not surprisingly, they are also much more likely to be employed full-time (73 percent) and less likely to be retired (7 percent). Their mean income of $67,300 is comparable to that of those who purchased most of their funds through a financial professional. Their education level is somewhat lower than those of the other two groups, particularly direct purchasers. Seven in ten have at least some college education, including 46 percent with at least a bachelor's degree. Unlike the other two groups, workplace purchasers are fairly equally divided between males (51 percent) and females (49 percent). They have the highest rate of Internet usage (91 percent) among the three purchase groups, and the greatest willingness (87 percent) to use the Internet for at least some mutual fund purchase-related activities.

Consistent with their younger age, these investors tend to have somewhat more modest household mutual fund holdings. The mean value of workplace purchasers' holdings is $47,900. They are significantly more likely than members of other groups to have less than $50,000 in household fund holdings (53 percent) and are significantly less likely to have more than $100,000 in funds (17 percent). They also have owned funds for a shorter period of time on average than members of the other two groups. More than a quarter (28 percent) have owned funds for five years or less, and only 44 percent have owned funds for ten years or more. The mean length of fund ownership for this group is 8.3 years.

Like those who purchase through a professional, these investors have a noticeably less favorable view of funds than direct purchasers. Only 32 percent have a very favorable view of funds. They are also the least likely of the three groups to view funds as easy to purchase, with fewer than half (44 percent) viewing funds as very easy to purchase. Workplace purchasers also resemble those who purchase through professionals in their lower confidence in their fund knowledge. Just 12 percent rate themselves as very knowledgeable about mutual funds. Nearly a third (32 percent) rate themselves as knowing only a little.

Workplace purchasers typically operate within a very different purchase process than that for either of the other two groups. While both direct purchasers and those who purchase through a professional have, at least in theory, thousands of funds to choose among, workplace purchasers typically choose from a fairly limited menu of funds that have been pre-selected by their employer.

It should come as no surprise, then, that the survey findings indicate that they approach the purchase process differently than those who purchase funds in the retail marketplace. In each case except volatility, workplace purchasers were the least likely of the groups to consider any of the factors – cost, risk, reputation, or past performance -- as important to their purchase decision. They were also the least likely to consider any of the written materials as influential on their most recent purchase decision. Not even two in ten workplace purchasers considered any of the documents very influential, and fewer than half considered any of the documents as even somewhat influential. When asked about their most recent purchase through a workplace plan, 48 percent indicated the fund prospectus was at least somewhat influential and 38 percent indicated a fund summary was at least somewhat influential. When asked what types of documents they would be interested in using, fund summaries did somewhat better, with nearly half of workplace purchasers (49 percent) rating these documents as of either great or substantial interest. This suggests that employers who do not already do so might want to consider making or promoting greater use of either the fund snapshots produced by fund companies or the fund summaries prepared by third parties, such as Morningstar or Yahoo!Finance.

Many employers provide a wealth of educational materials and tools to help their employees make their fund selections. The survey findings suggest that employees are not making good use of these materials, that they are not aware of their availability, or that these materials are not serving workplace purchasers as well as they could. Consideration should be given to conducting further research to determine how employees view the educational materials available to them and what could be done to improve them, whether through better design, content, or delivery.

Conclusion

The gap the survey reveals between how experts recommend investors go about making mutual fund purchase decisions and how investors actually do so has important implications both for policy-makers and for investor educators. In some cases, the survey findings may reveal a real failure on the part of investors to take important steps to protect their interests. In these cases, the challenge for investor educators is to figure out how to convey their message more effectively. In other cases, however, the gap between expert recommendations and investor behavior may reveal unrealistic expectations on the part of experts as they develop their education messages, a failure to tailor their messages for different segments of the market, or both. By beginning to explore the nature of the gap between expert recommendations and investor behavior, this survey can help us develop more effective investor education materials and methods that coincide more closely with the real world experiences of mutual fund investors and build on their preferences for receiving information.