Interim Research Report

Research on KII Disclosures for UCITS Products

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By
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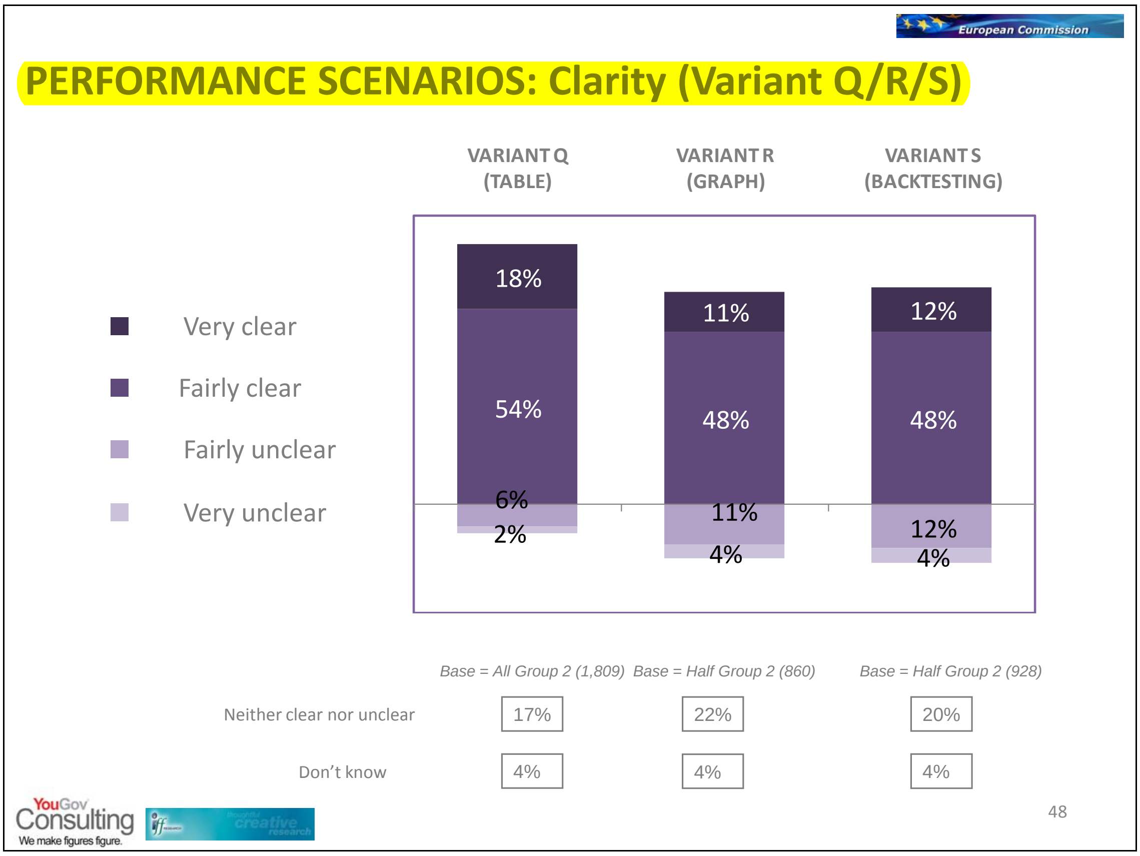
Clarity of variants

6.5 The three performance scenarios were tested for clarity with respondents. Based on a scale of *very clear, fairly clear, fairly unclear, very unclear and neither clear nor unclear*, respondents were asked how clear they found the description of performance possibilities in each variant. The following chart presents the results of these lines of questioning.

Figure .: Perceived clarity of performance scenario variants



6.1 Variant Q (the tabular presentation) obtained significantly higher ratings for clarity than either of the other two graph-based variants with 72% stating that they felt that it was very or fairly clear. Variant R and S obtained equal ratings with 60% of respondents stating that they were very or fairly clear.

6.2 As mentioned earlier this ‘test’ should not necessarily be interpreted as an absolute measure of clarity to respondents (since their actual understanding often runs counter to the clarity rating that they provide) but it does instead demonstrate a basic level of ability to engage with the material. A high proportion stating that they find the variant fairly or very unclear indicates a high proportion who draw a conclusion that the information is going to be difficult to understand and hence are discouraged from looking at it in detail. In the cases of variants R and S, one in six investors found the variant very or fairly unclear.

6.3 Across all three variants investors in Ireland gave significantly higher than average clarity ratings (76% stated that variant Q was very or fairly clear, 71% for variant R and 70% for variant S). Those in Sweden on the other hand gave significantly lower than average clarity ratings for all 3 performance scenario ratings (59% stated that variant Q was very or fairly clear, 40% for variant R and 36% for variant S). In all member states the pattern is broadly the same with variant Q obtaining considerably higher ratings than the other two variants (and the ratings for variants R and S being broadly the same). The difference between ratings for the tabular variant Q compared with the graph variants R and S is particularly marked in Sweden where overall ratings are lower than average.

6.4 As perhaps would be expected, ratings for perceived clarity are lower for all 3 variants among those who assess their financial sophistication to be ‘low’. For variant Q, three-quarters of those with medium or high sophistication considered the variant to be very or fairly clear compared with 65% of those with low sophistication. For both variants R and S, three in five of those with medium or high sophistication considered the variants to be very or fairly clear compared with only half of those with low sophistication. Hence while their perceptions of clarity are lower across the board, consumers with lower financial sophistication still perceive variant Q to be considerably clearer than either variant R or S.

Table .: Perceived clarity of variants by financial sophistication

Column percentages

	VARIANT Q				**VARIANT R**				**VARIANT S**			
	Financial sophistication				**Financial sophistication**				**Financial sophistication**			
	Total	**High**	**Med**	**Low**	**Total**	**High**	**Med**	**Low**	**Total**	**High**	**Med**	**Low**
	%	%	%	%	%	%	**%**	**%**	%	%	%	%
Very clear	17	26	17	14	11	15	**11**	**9**	11	20	11	8
Fairly clear	54	50	58	51	48	47	**52**	**42**	48	41	53	45
Neither clear nor unclear	17	11	16	21	22	17	**22**	**26**	20	20	18	24
Fairly unclear	6	7	5	7	11	13	10	13	12	10	12	12
Very unclear	2	1	2	2	4	3	3	6	4	5	3	6
Don’t know/not stated	4	4	3	5	4	4	2	5	4	5	2	5
CLEAR	72	76	75	65	59	62	62	51	60	60	64	53
UNCLEAR	8	8	7	9	15	16	13	19	16	15	15	18
Base: All Group 2	*1809*	*323*	*1001*	*429*	*1809*	*323*	*1001*	*429*	*1809*	*323*	*1001*	*429*

6.5 In the case of all three variants, those who described their attitude to risk tended to be slightly less likely to find the presentation very or fairly clear while those with at least a degree level qualification were slightly more likely to find the treatment clear than those with lower levels of educational achievement.

Aspects of variants not understood

6.6 As with other elements of disclosure, respondents were asked whether there were any aspects of each of the variants that they did not understand. Three-quarters of investors stated that there was nothing in variant Q that they did not understand. Only 11% stated that there were aspects that they did not understand and a further 16% stated that they were unsure whether there was anything that they did not understand. Respondents in Spain and in Hungary were the most likely to state that there was nothing that they did not understand (85% and 81% respectively). Those in Sweden were least likely to state there was nothing that they did not understand (52%) but the difference to other member states is mostly in the proportion stating that they were unsure whether there was anything that they did not understand (32%) rather than those actively stating that there were aspects they did not understand (16%).

6.7 The aspects that individuals were most likely to mention that they did not understand were the technical terms for which no definition was provided (2% of consumers) and the meaning of 'probability' and how it had been calculated (2%).

6.8 One in six (15%) stated that there were aspects of variant R that they did not understand and 17% stated that they were unsure if there was anything that they did not understand. The proportion identifying aspects that they did not understand was again significantly higher in Sweden (20%) but broadly comparable across all other member states. The proportion of Swedish respondents stating that they were unsure whether there were any aspects that they did not understand was also considerably higher than average (39%).

6.9 The aspects of variant R that individuals were most likely to state that they did not understand were the graphs (4%) and again the technical terms for which there was no definition provided (3%). Furthermore 2% of respondents stated that they did not understand most or all of the variant.

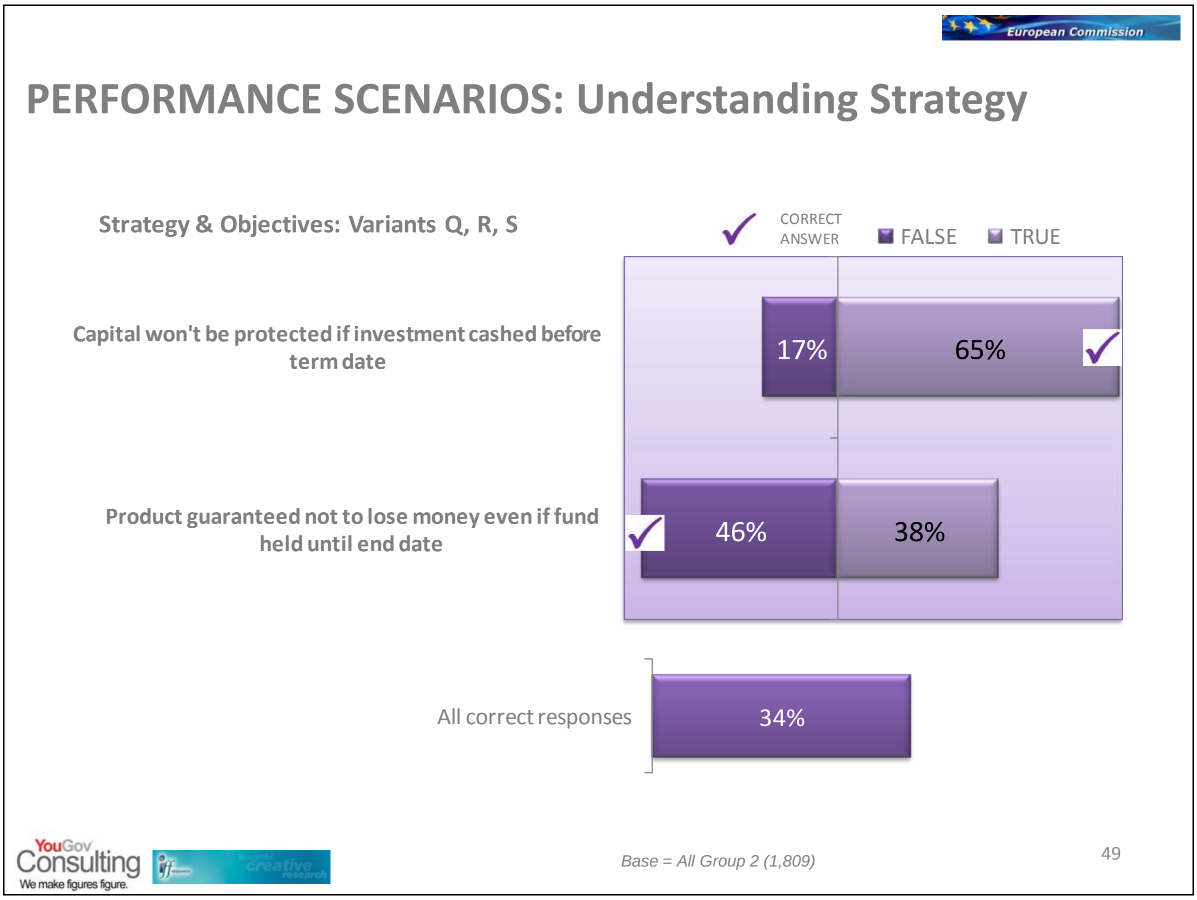
6.10 The proportion stating that there were aspects of variant S that they did not understand (17%) was comparable with that for variant R as was the proportion stating that there were unsure whether there is anything that they did not understand (16%). Again the proportion stating that there was anything that they did not understand was higher in Sweden (23% with a further 37% stating that they were unsure). The proportion of investors identifying that there were aspects that they did not understand was lower for this variant in Germany (11%).

6.11 Again the actual aspects of the variant that respondents stated that they were unable to understand were similar; 5% stated that the graph was unclear, 3% commented on the lack of definitions for financial terms and 2% stated that they were unclear about the calculations of probability. A further 2% stated that all or most of the variant was unclear to them.

Understanding of strategy and objectives of structured fund

6.12 As mentioned earlier, respondents viewing the performance scenario variants were asked to read a description of the strategy and objectives of the fund prior to answering questions about the individual variants. They were asked to respond to a couple of true/false statements which tested their understanding of the overall strategy and objectives of the fund. These were only asked once in conjunction with the performance scenario variant that they were asked to view first. The responses to these two statements are shown in the figure below.

Figure .: Understanding of strategy and objectives of structured fund



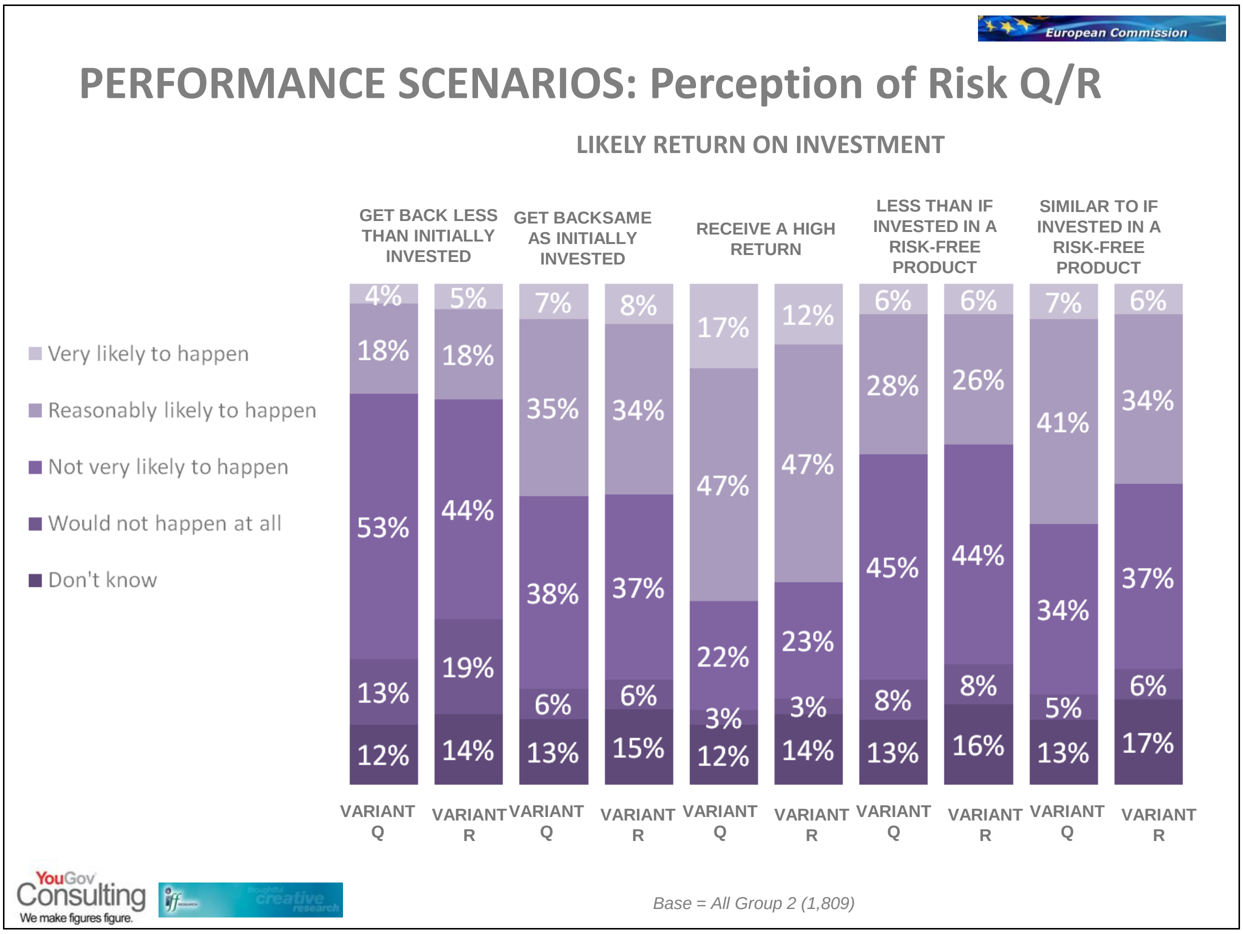
6.13 As the figure demonstrates, there was a general understanding of the fact that there was no capital protection unless the fund was held until the end date (65% answered this question correctly) but in keeping with earlier findings in connection with comprehension of the strategy and objectives of simple funds, there was a relatively widespread misunderstanding about capital guarantees (only 46% of respondents correctly identified the second statement as being false). Overall only a third of respondents answered both statements correctly. It is worth bearing in mind that this level of misunderstanding is the backdrop to interpretation of all the performance scenario variants.

6.14 The proportion answering both statements correctly is significantly higher than average in Germany , Hungary and Ireland (45%, 40% and 47% respectively) but significantly lower than average in Poland, Sweden and Spain (26%, 22% and 19%). For the most part these differences are driven by differing proportions answering the second statement (about capital guarantee) correctly although those in Hungary were also more likely to answer the first statement (about cashing in before the term date) correctly and those in Sweden were less likely to do so.

Perceptions of risk: Variants Q and R

6.15 When viewing variants Q and R (the table and graphical variants), respondents were asked some questions designed to assess how the presentation of the data impacted on their perception of the associated risk. Respondents were asked to state how likely a series of scenarios were to happen. The results of these questions are shown in the figure below.

Figure .: Perception of risk



6.16 As the figure demonstrates, the perceived likelihood of each of these scenarios taking place does not vary significantly between the two variants. The only significant differences are that when respondents view Variant Q they are slightly more likely to feel that they would be 'very likely' to receive a high return on their investment and slightly more likely to feel that they would be 'reasonably likely' to receive a return that was similar to that they would receive from investing in a risk-free product. It would seem that the fact that Variant Q specifically shows the probability of the latter scenario (at 22%) makes respondents more likely to consider this as a possibility. Variant Q does not spell out the probability of a 'high return'. The closest that it comes to this is showing the probability of getting back more than the risk free rate (at 40%); it is interesting that this appears to give investors greater confidence in the product than the graphs that show the performance of the fund under different scenarios with no weight of likelihood attached to them.

6.17 The tables below show the variations in the perception of risk for both Variant Q and Variant R.

Table .: Perceptions of variant Q by member state and level of financial sophistication

Column percentages

			Member State							Financial Sophistication		
		Total	**D**	**IRL**	**S**	**E**	**I**	**H**	**PL**	**High**	**Med**	**Low**
		%	%	%	%	%	%	%	%	%	%	%
You would get back less money than originally invested	Would not happen / not very likely	65	74	56	57	68	49	**86**	62	60	66	68
	Reasonably / very likely	22	14	33	16	27	35	8	25	26	24	17
You would get back more or less the same amount that you invested with no return on your investment	Would not happen / not very likely	44	46	40	32	46	24	**73**	43	38	45	48
	Reasonably / very likely	42	41	48	41	48	59	22	43	47	44	36
You would receive a high return on your investment	Would not happen / not very likely	24	26	23	33	27	20	20	20	25	24	24
	Reasonably / very likely	64	64	69	40	67	63	**75**	68	62	67	61
You would receive less than if you had invested in a risk-free product	Would not happen / not very likely	52	51	45	46	50	49	**70**	52	46	55	53
	Reasonably / very likely	35	38	45	25	44	34	25	35	40	35	31
You would receive a similar rate of return to if you had invested in a risk-free product	Would not happen / not very likely	39	42	33	32	40	35	56	31	39	39	40
	Reasonably / very likely	48	47	**58**	40	54	49	40	53	46	52	43
Base: All group 2		*1809*	*256*	*243*	*256*	*255*	*249*	*295*	*255*	*323*	*1001*	*429*

Table .: Perceptions of variant R by member state and level of financial sophistication

Column percentages

			Member State							Financial Sophistication		
		Total	**D**	**IRL**	**S**	**E**	**I**	**H**	**PL**	**High**	**Med**	**Low**
		%	%	%	%	%	%	%	%	%	%	%
You would get back less money than originally invested	Would not happen / not very likely	63	71	54	50	66	53	**81**	63	58	65	64
	Reasonably / very likely	23	16	36	21	27	30	10	24	27	24	18
You would get back more or less the same amount that you invested with no return on your investment	Would not happen / not very likely	44	46	36	36	44	30	**67**	42	37	45	47
	Reasonably / very likely	42	37	51	36	48	53	25	44	46	43	36
You would receive a high return on your investment	Would not happen / not very likely	26	31	23	36	27	21	22	23	29	26	25
	Reasonably / very likely	59	55	65	35	66	62	**68**	64	55	63	58
You would receive less than if you had invested in a risk-free product	Would not happen / not very likely	52	55	44	43	51	49	**69**	53	45	55	53
	Reasonably / very likely	32	31	43	27	39	30	23	31	38	32	27
You would receive a similar rate of return to if you had invested in a risk-free product	Would not happen / not very likely	43	46	35	36	49	40	**57**	36	39	45	41
	Reasonably / very likely	40	36	49	32	43	39	36	44	43	40	39
Base: All group 2		*1809*	*256*	*243*	*256*	*255*	*249*	*295*	*255*	*323*	*1001*	*429*

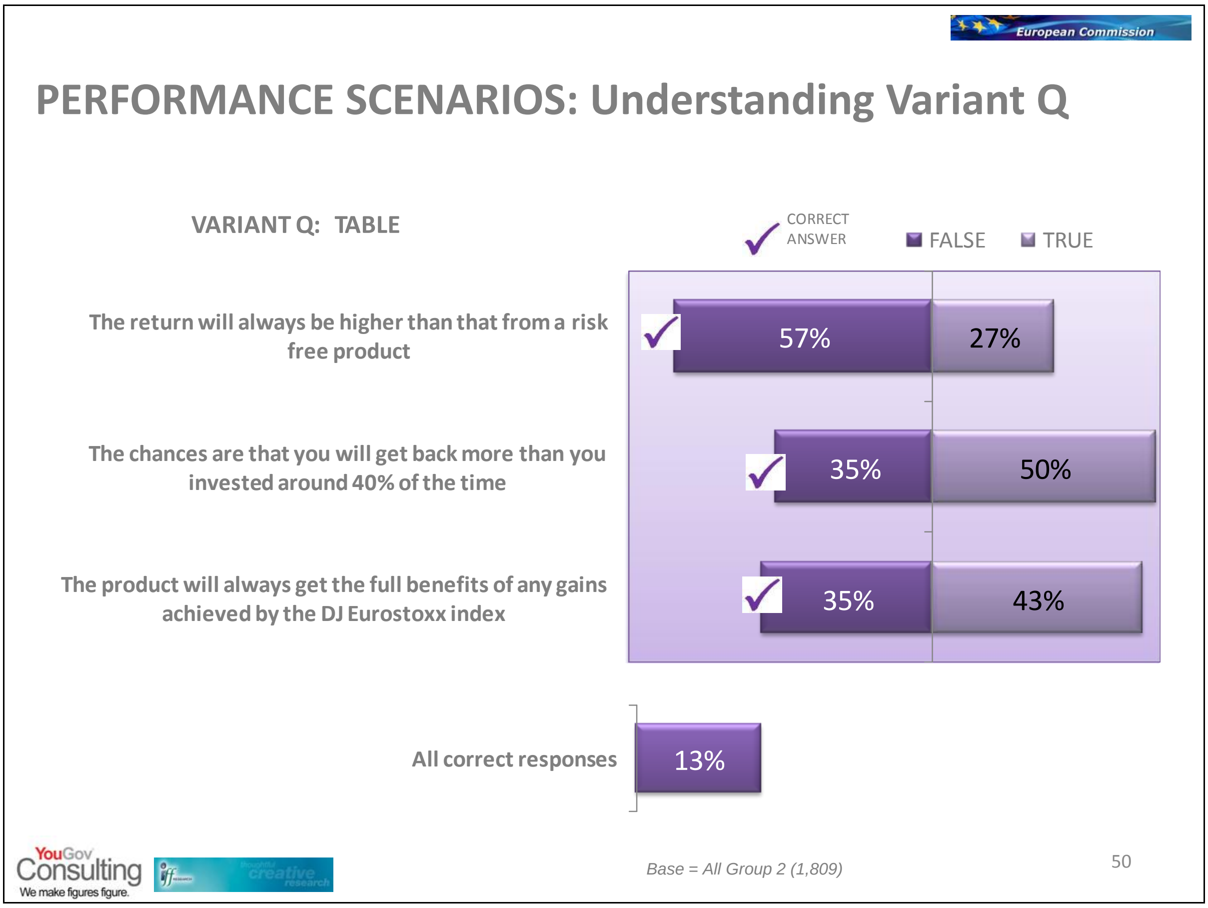
6.18 Investors in Hungary vary most from average for both variants, being more likely than investors in other member states to feel that the fund would give them a low probability of getting back less money than they originally invested, no return on their investment or that they would receive less than if they had invested in a risk-free product. For both variants Hungarian investors were also more likely to feel they had a good or reasonable chance of receiving a high return on their investment.

6.19 There was little differentiation by financial sophistication for either variant Q or R.

Understanding of Variant Q

6.20 To test understanding of Variant Q, respondents were asked whether a series of 3 statements about the fund were true or false. The responses to these are shown in the figure below.

Figure .: Understanding of Variant Q (Table)



6.21 For the first of these statements '*The return will always be higher than from a risk free product*', investors were more likely to select the correct answer (false) than the incorrect one; just over half of respondents (57%) stated that this statement was false. This indicates that the tabular variant does a reasonable job of conveying that there are scenarios under which individuals could receive a return that would be lower than for a risk free product (although the proportion who felt that this was not the case was substantial at 27%).

6.22 For both of the other two statements, respondents were more likely to select the incorrect answer than the correct one (with greater proportions believing the statements to be true than false).

6.23 It seems likely that those respondents believing it to be true that *'the chances are that you will get back more than you invested around 40% of the time'* are simply reading the figure from the bottom row of the table in Variant Q i.e. the likelihood of getting back more than they would have got from investing in 'risk-free' products rather than adding together the figures from the bottom two rows (i.e. including the probability of getting back more than they invested but about the same as investing in a 'risk-free' product). The correct probability for receiving more than initially invested is 62% hence interpreting this probability as 40% is a considerable misinterpretation of the risk profile of the product.

6.24 With regard to the third statement – *'the product will always get the full benefits of any gains made by the DJ Eurostoxx index'* – the information to answer this statement is implicit in the descriptions of scenarios that could lead to each of the outcomes listed in the table but it is not stated explicitly. The fact that 43% of respondents failed to indentify the correct response to this question indicates a widespread fundamental misunderstanding of the operation of the fund that the tabular variant has not been able to address.

6.25 Only 13% of respondents were able to identify the correct answer to all 3 statements and over a quarter (29%) got all 3 incorrect. It is also worth noting that in the region of one in five respondents were unable to provide a response to each of the statements which demonstrates the difficulty that some investors had in engaging with the material at all.

6.26 As the table below demonstrates, there were some variations in the understanding of Variant Q by both member state and by level of financial sophistication. Differences that are statistically different from the total sample are shown in bold text.

Table .: Understanding of Variant Q by member state and financial sophistication

			Member State							Financial Sophistication		
		Total	**D**	**H**	**IRL**	**I**	**PL**	**E**	**S**	**High**	**Med**	**Low**
		%	%	%	%	%	%	%	%	%	%	%
The return will always be higher than from a risk free product	Correct	57	62	**64**	60	**50**	**45**	57	57	57	58	52
	Incorrect	27	**21**	29	26	30	**34**	**35**	**11**	28	27	27
The chances are that you will get back more than you invested about 40% of the time	Correct	35	28	28	26	27	33	50	**55**	**43**	35	30
	Incorrect	49	**58**	**63**	**61**	53	52	**41**	**15**	**42**	**52**	51
The product will always get the full benefits of any gains achieved by the Eurostoxx index	Correct	35	**22**	**52**	36	**40**	32	**29**	**29**	37	36	32
	Incorrect	43	**54**	**34**	47	38	46	**61**	**20**	41	**46**	**38**
ALL CORRECT RESPONSES		13	**8**	16	12	**7**	10	15	**25**	**19**	12	11
Base: All Group 2		*1809*	*256*	*295*	*243*	*249*	*255*	*255*	*256*	*323*	*1001*	*429*

6.27 Respondents in Sweden demonstrated the highest levels of understanding of Variant Q with a quarter identifying the correct answers to all 3 statements. The proportion of respondents answering correctly in Hungary were also higher than average for two of the statements (and by 17 percentage points in the case of the statement about receiving full benefits of any gains in the index) but overall the proportion getting all 3 statements correct was broadly in line with the average.

6.28 Differences in understanding by financial sophistication are only really evident for the statement about the probability of receiving more than invested which those with a high level of sophistication are significantly more likely to answer correctly (although even in this group respondents are equally as likely to answer incorrectly as correctly). The differences in responses to this question are reflected in the proportion answering all 3 statements correctly (19% of those with high sophistication compared with 12% of those with medium sophistication and 11% of those with lower financial sophistication).

6.29 The table below analyses the relationship between perceived clarity of Variant Q and the likelihood to score well on the 'understanding test'.

Table .: Perceived clarity of Variant Q by number of correct responses to understanding statements

Column percentages

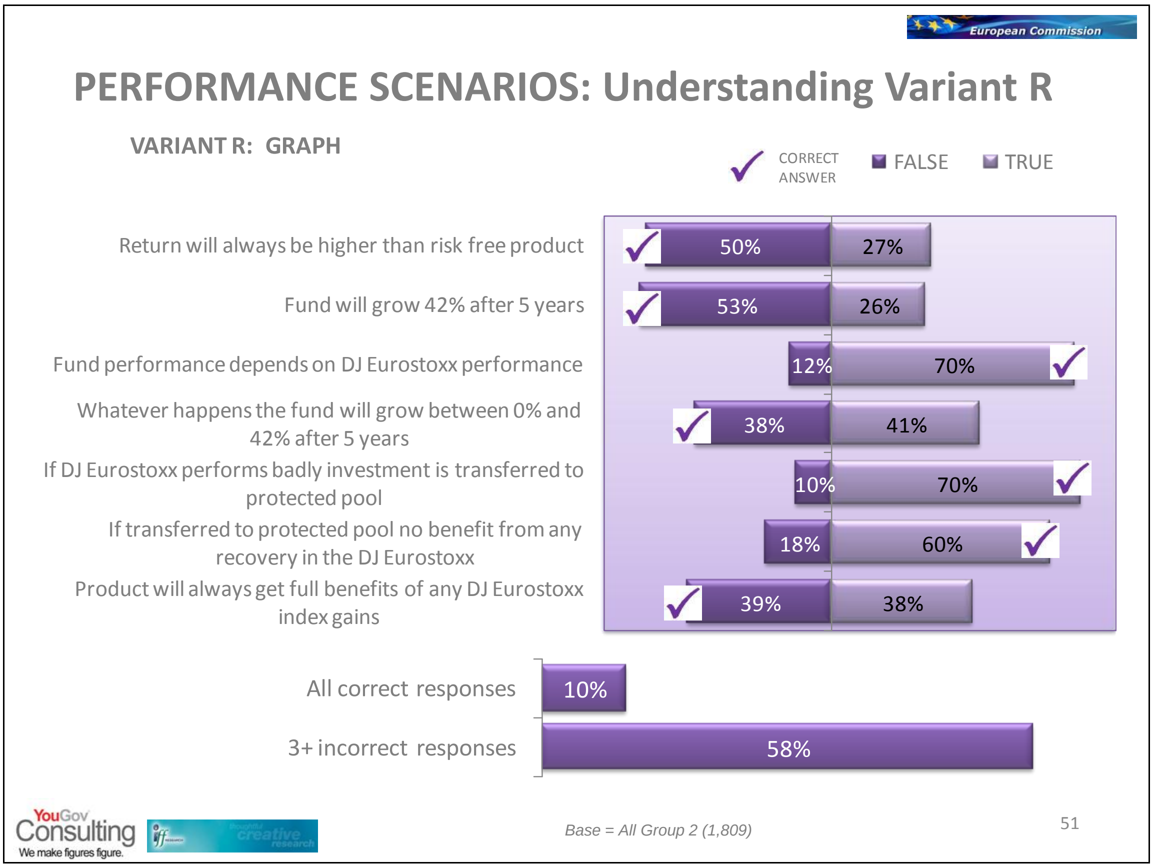
		Perceived clarity of objectives			
	Total	**Very clear**	**Fairly clear**	**Neither clear nor unclear / Don't know**	**Very or Fairly Unclear**
	%	%	%	%	%
No correct responses	29	15	25	46	33
1 correct response	30	30	32	27	29
2 correct responses	28	**35**	29	22	25
3 correct responses	13	21	14	5	13
Base: All group 2	*1809*	*315*	*979*	*372*	*141*

6.30 How clear investors felt variant Q to be was correlated with their understanding of the variant. As well as those who found it unclear being more likely to give no correct response (33% cf. 29% total) and those who found it clear being more likely to give all correct responses (21% cf. 13% total), investors who found variant Q very clear were more likely than those who found it fairly clear to give three correct responses to the understanding statements (21% cf. 14%).

Understanding of Variant R

6.31 As with Variant Q, respondents were asked to respond to a series of true/false statements after viewing Variant R. The responses given are shown in the figure below.

Figure .: Understanding of Variant R (Graph)



6.32 For the majority of statements, the proportion answering the statement correctly was greater than the proportion answering incorrectly. The two exceptions to this were for the statements:

- *"Whatever happens the fund will grow between 0% and 42% after 5 years';*
- *"The product will always get the full benefits of any gains achieved by the DJ Eurostoxx index"*

6.33 Two fifths of respondents believed (incorrectly) that the first statement is correct (while 38% correctly responded that it was incorrect). It seems likely that those that answered incorrectly are interpreting the two graphs as spelling out minimum and maximum returns (since the first shows a scenario where 0% growth is achieved and the second a scenario where 42% growth is achieved). It is obviously a concern that a relatively large proportion of investors interpret this variant as laying out the two extreme possibilities for fund growth. In this particular case this means that two-fifths of respondents interpret the variant as implying that they would not receive less than they originally invested under any circumstance.

6.34 Responses to the statement *'the fund will grow 42% after 5 years'* indicate that around a quarter of investors overlooked the first graph altogether and simply interpreted the second to be forecasting the growth of the fund to be 42%. The growth achieved under the second scenario presented (i.e. 42%) is marked in text on the graph and it is possible that this encourages readers to focus on this figure. Confusion over possible capital returns is also evident from responses to the statement *'return will always be higher than for a risk free product'* (a quarter of respondents – 27% - felt this statement was correct). Responses to this statement are very similar to those given for the same statement in relation to variant Q.

6.35 The fact that understanding that the product will not always get the full benefits of any gains achieved by the index was so mixed is perhaps surprising given that the first graph in the variant demonstrates a scenario where this is the case (because the capital protection has been triggered). The fact that two fifths of respondents (38%) answered this statement incorrectly indicates that a sizeable minority are unable to comprehend the core 'message' of the individual graphs. In fact the responses given to this statement for Variant R are very similar to those for the same statement given for Variant Q indicating that the addition of the graphs does not greatly improve understanding over the tabular format in which this issue is not explicitly covered.

6.36 The responses to the statement about benefitting fully from any gains achieved by the index appear slightly out of kilter with those for the statement *'If transferred to the protected pool you will not benefit from any recovery in the DJ Eurostoxx'* (60% of respondents indentified that this statement was correct and only 18% felt that it was incorrect). This second statement almost appears in the text above the scenario 1 graph and it would appear that there are a group of respondents who are able to pick out this text (and hence give the correct answer to the statement *''If transferred to the protected pool you will not benefit from any recovery in the DJ Eurostoxx'* but not actual understand its **meaning** well enough to be able to answer the other statement correctly.

6.37 Aside from confusion over these issues, the variant appears to successfully convey some elements of the mechanics of the fund i.e.;

- That fund performance depends on DJ Eurostoxx performance (70% of respondents identified that this was correct and only 12% felt it was incorrect);
- That if the DJ Eurostoxx performs badly then investment is transferred into the protected pool (70% identified that this was correct and only 10% felt it was incorrect)

6.38 Overall 10% of respondents answered all 7 statements correctly and 13% answered all statements incorrectly. As with Variant Q, in the case of each statement around one fifth of respondents were unable to provide an answer again demonstrating that this information relating to structured funds was difficult for respondents to engage with.

6.39 As the table below demonstrates, there were some variations in the understanding of Variant R by both member state and by level of financial sophistication. Differences that are statistically different from the total sample are shown in bold text.

Table .: Understanding of Variant R by member state and financial sophistication

Column percentages

			Member State							Financial Sophistication		
		Total	**D**	**H**	**IRL**	**I**	**PL**	**E**	**S**	**High**	**Med**	**Low**
		%	%	%	%	%	%	%	%	%	%	%
The return will always be higher than that from a risk free product	Correct	50	55	**63**	54	46	**44**	**42**	46	51	50	50
	Incorrect	27	23	28	26	27	28	**43**	**16**	29	**29**	**23**
The fund will grow by 42% after 5 years	Correct	53	**60**	**58**	53	54	**46**	**46**	50	57	54	**47**
	Incorrect	25	**16**	27	26	23	**32**	**37**	**14**	25	25	27
The performance of the fund depends on how the DJ Eurostoxx performs	Correct	70	**76**	74	**76**	**63**	69	**77**	**53**	71	73	64
	Incorrect	12	**7**	14	11	15	11	13	10	12	12	11
Whatever happens the fund will grow between 0% and 42% after 5 years	Correct	38	36	34	**47**	33	**50**	35	33	42	39	35
	Incorrect	41	44	**54**	**35**	42	**32**	**48**	**29**	38	**44**	40
If the DJ Eurostoxx performs badly your investment is transferred into the protected pool	Correct	70	71	**83**	72	**61**	75	68	**55**	70	70	70
	Incorrect	10	9	7	10	13	7	**18**	8	12	11	**8**
If transferred to the protected pool you will not benefit from any recovery in the DJ Eurostoxx	Correct	59	58	**70**	65	54	62	57	**47**	60	61	57
	Incorrect	18	15	18	17	21	18	**26**	**10**	19	19	17
The product will always get the full benefits of any gains achieved by the DJ Eurostoxx index	Correct	39	34	**57**	42	42	39	**19**	34	39	39	38
	Incorrect	38	42	**27**	38	32	38	**67**	25	40	40	33
ALL CORRECT RESPONSES		10	13	13	16	9	9	**3**	11	**13**	10	9
4+ CORRECT RESPONSES		57	59	**71**	62	56	61	44	47	56	59	55
Base: All Group 2		*1809*	*256*	*295*	*243*	*249*	*255*	*255*	*256*	*323*	*1001*	*429*

6.40 The proportion able to answer all statements correctly was low in all member states (although it is particularly low in Spain where only 3% were able to achieve this). Respondents in Hungary generally performed better than average (with 71% answering at least 4 statements correctly. Among Hungarian respondents, the proportion answering correctly is significantly above the average for the majority of statements. The exception to this is the statement *'whatever happens the fund will grow between 0% and 42% after 5 years'* that Hungarian respondents were significantly more likely to answer incorrectly (i.e. that this statement was true).

6.41 With most statements there are slight differences by self-assessed level of financial sophistication with those believing their level of sophistication to be high generally being more likely to answer the statements correctly. This difference is most marked for the statement *'the fund will grow 42% after 5 years'* which 57% of those with a high level of sophistication answer correctly compared with 54% considering that they have a medium level of sophistication and 47% of those with low sophistication.

6.42 The table below analyses the relationship between perceived clarity of Variant R and the likelihood to score well on the 'understanding test'

Table .: Perceived clarity of Variant R by number of correct responses to understanding statements

Column percentages

		Perceived clarity of objectives			
	Total	**Very clear**	**Fairly clear**	**Neither clear nor unclear / Don't know**	**Very or Fairly Unclear**
	%	%	%	%	%
No correct responses	13	1	5	26	26
1 correct response	5	2	4	6	6
2 correct responses	9	10	9	10	9
3 correct responses	16	18	16	14	14
4 correct responses	15	13	16	15	13
5 correct responses	17	14	19	16	14
6 correct responses	15	22	17	10	13
7 correct responses	10	20	13	4	6
Base: All group 2	*1809*	*196*	*864*	*466*	*280*

6.43 As well as those investors who found the variant clear being more likely to show understanding by getting correct answers, those who found variant R very clear were more likely to get all responses correct than those who found it fairly clear (20% cf. 13%).

6.44 Respondents viewing Variant R were asked what information they felt that the variant displayed. The table below shows the responses to this question at overall level, by member state and by financial sophistication. The question was pre-coded i.e. a set of possible answers were shown to respondents.

Table .: Information perceived to be shown on Variant R

Column percentages

		Member State							Financial Sophistication		
	Total	**D**	**H**	**IRL**	**I**	**PL**	**E**	**S**	**High**	**Med**	**Low**
	%	%	%	%	%	%	%	%	%	%	%
The impact of different investment conditions upon the performance of the fund	42	48	**51**	48	35	42	33	38	43	43	42
How the fund may perform in the future	39	**49**	37	41	31	36	38	39	37	41	36
The past performance of the fund over a number of years	20	22	22	**28**	14	11	18	22	21	19	20
How the fund will perform in the future	16	14	14	16	17	13	**22**	14	16	17	13
How other similar funds have performed in the past	12	11	9	**20**	12	7	16	10	14	12	10
Something else (WRITE IN)	1	*	2	2	1	*	-	-	2	1	*
Don't Know	13	13	7	7	14	12	9	27	13	9	17
Not stated	*	*	-	-	*	*	*	-	*	*	*
Any correct response	65	70	**72**	70	57	67	63	**55**	62	68	64
Correct responses only	48	49	54	43	49	**59**	42	**37**	46	50	46
Base: All Group 2	*1809*	*256*	*295*	*243*	*249*	*255*	*255*	*256*	*323*	*1001*	*429*

6.45 Either of the top two answers shown in the table above is correct i.e. that the variant shows *'the impact of different investment conditions upon the performance of the fund'* and therefore *'how the fund may perform in future'.* Each of these responses was selected by around two fifths of respondents. The other responses were selected by a much smaller proportion of respondents but they indicate considerable misunderstanding among this group. A fifth believed that the variant was showing them past performance of the fund, one in six believed that the variant was showing them how the fund **will** perform in the future (i.e. forecasting performance) and one in eight believed that it was showing them how other similar funds had performed in the past.

6.46 In total, two thirds of respondents selected at least one of the correct answers indicating that the majority understood the purpose of the variant. However some of those who selected a correct answer also selected an incorrect one as well. Overall half of respondents selected ***only*** a correct answer to the question.

6.47 The proportion selecting only a correct response was significantly higher in Poland (59%) and significantly lower in average in Spain. The proportion correctly identifying the purpose of the variant did not vary substantially by level of financial sophistication.

Understanding of Variant S

6.48 As with the other variants, respondents were asked to respond to a series of true/false statements after viewing Variant S. The responses given are shown in the figure below.

6.49 For the first of these statements *'The return will always be higher than that from a risk free product'*, the proportion answering correctly (that this statement is false) is slightly lower than for Variant Q (the tabular variant) but broadly in line with that for Variant R. A sizeable minority (31%) believed that the fund was guaranteed to deliver a return above the risk free rate.

6.50 The second statement *'The highest return you can get from this investment is around 8%'* was generally answered well with the proportion selecting the correct answer (53%) considerably higher than those selecting the incorrect response (19%). Those respondents believing this statement to be correct are probably reading the simulated figure for the last data point shown on the graph (January 08). It is encouraging that the majority of respondents did not make this mistake however we can not tell from responses to this statement whether some respondents drew a similar conclusion about the highest and lowest levels of performance showing representing the full range of possible performance scenarios (as it appears that a reasonable proportion did from the graphs shown in Variant R).

6.51 Again with the third statement *'You are more likely to do better than the risk free rate than worse than the risk free rate'* the proportion of correct responses (61%) was considerably higher than the proportion of incorrect ones (16%). It is worth noting that readers do not necessarily have to interpret the graph to answer this statement correctly since the figures for the proportion of occasions when backtesting demonstrates that the fund would have achieved certain levels of return is summarised in a table at the bottom of the variant (in a similar format as is used for Variant Q).

6.52 As the table below demonstrates, there were some variations in the understanding of the backtesting variant by both member state and by level of financial sophistication. Differences that are statistically different from the total sample are shown in bold text.

Table .: Understanding of Variant S by member state and financial sophistication

			Member State							Financial Sophistication		
		Total	**D**	**H**	**IRL**	**I**	**PL**	**E**	**S**	**High**	**Med**	**Low**
		%	%	%	%	%	%	%	%	%	%	%
The return will always be higher than that from a risk free product (true)	Correct	49	52	**58**	53	46	**40**	45	46	52	50	45
	Incorrect	31	29	31	28	34	36	**41**	**18**	31	32	30
The highest return you can get from this investment is around 8% (true)	Correct	53	53	**68**	52	53	52	48	**41**	53	55	51
	Incorrect	19	17	**11**	22	21	20	**32**	**10**	24	19	15
You are more likely to do better than the risk free rate than worse than the risk free rate (true)	Correct	61	59	**77**	56	61	58	64	**48**	60	61	63
	Incorrect	16	16	**10**	18	20	20	19	**11**	19	17	13
ALL CORRECT RESPONSES		23	24	**37**	23	21	**17**	**17**	23	27	24	21
Base: All Group 2		*1809*	*256*	*295*	*243*	*249*	*255*	*255*	*256*	*323*	*1001*	*429*

6.53 As with the other performance scenario variants, respondents in Hungary generally demonstrated a better understanding of the backtesting variant (37% answered all 3 statements correctly). Again reflecting patterns seen earlier, levels of comprehension were lower than average in Spain. For this particular variant, levels of comprehension were also lower than average in Poland.

6.54 There were no clear cut patterns by level of financial sophistication for this variant.

6.55 The table below analyses the relationship between perceived clarity of Variant S and the likelihood to score well on the 'understanding test' .

Table .: Perceived clarity of Variant S by number of correct responses to understanding statements

Column percentages

		Perceived clarity of objectives			
	Total	**Very clear**	**Fairly clear**	**Neither clear nor unclear / Don't know**	**Very or Fairly Unclear**
	%	%	%	%	%
No correct responses	18	8	9	34	27
1 correct response	25	30	27	20	26
2 correct responses	34	28	39	28	30
3 correct responses	23	34	26	18	17
Base: All group 2	*1809*	*208*	*870*	*440*	*289*

6.56 As seen elsewhere, those who found the variant unclear were most likely to have least understanding as shown by giving no correct responses to the statements (27% unclear cf. 18% total). Those who found variant S very clear were more likely than those who found it fairly clear to give all three correct responses (34% cf. 26%).

6.57 For variant S, respondents were asked a direct question about what information they felt that the variant displayed. The table below shows the responses to this question at overall level, by member state and by financial sophistication. The question was pre-coded i.e. a set of possible answers were shown to respondents.

Table .: Information perceived to be shown on Variant S

Column percentages

		Member State							Financial Sophistication		
	Total	**D**	**H**	**IRL**	**I**	**PL**	**E**	**S**	**High**	**Med**	**Low**
	%	%	%	%	%	%	%	%	%	%	%
How the fund would have performed if it had been launched at different dates in the past based on the performance of the indices that it is linked to	47	59	**60**	43	37	37	48	39	46	47	48
The past performance of the fund over a number of years	40	39	39	**51**	34	46	36	35	44	41	35
How similar funds have performed in the past	16	11	13	23	19	13	**24**	8	15	16	17
Something else (WRITE IN)	1	-	-	2	3	1	*	*	1	1	1
Don't know	14	12	9	10	16	11	9	33	13	12	19
Not stated	*	*	-	*	-	-	*	-	-	*	*
Correct response only	33	39	**43**	24	31	32	36	27	31	35	33
Base: All Group 2	*1809*	*256*	*295*	*243*	*249*	*255*	*255*	*256*	*323*	*1001*	*429*

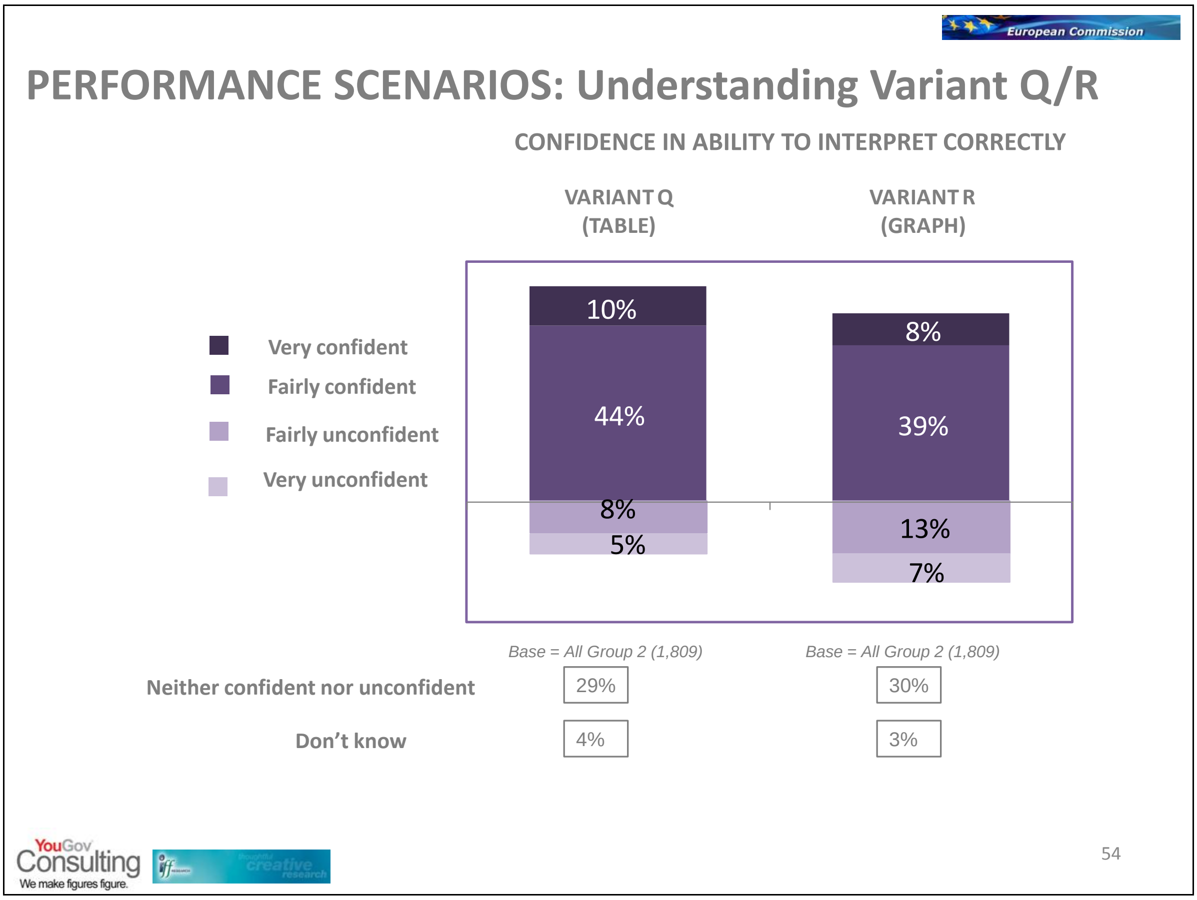
6.58 The first answer option shown in the table above is the correct response (i.e. that the variant shows simulated performance on how the fund would have performed if it had been launched in the past). It is encouraging that this response was the one most commonly given (selected by 47%). However, the other responses demonstrate considerable misunderstanding of the purpose of the variant. The considerable scope for misinterpretation of this variant is demonstrated by the fact that 40% of respondents felt that the variant showed actual past performance of the fund (twice as many as interpreted Variant R to show information about past performance). It seems likely that this material misunderstanding of the information shown could have a considerable impact on the conclusions that investors draw from the information.

6.59 It is worth noting that some of those respondents who selected the correct response to this question also selected an incorrect one as well. It is only a third of respondents who ***only*** selected the correct response. This rises to 43% of respondents in Hungary but falls to only a quarter in Ireland. In no member state did the majority of respondents answer this question correctly.

Confidence in ability to interpret variants

6.60 For variants Q and R, respondents were asked how confident they felt in their ability to interpret the variants correctly. They were asked to state whether they felt *very confident, fairly confident, neither confident nor unconfident, fairly unconfident or very unconfident.* The stated levels of confidence are shown in the figure below:

Figure .: Confidence in interpreting variants Q and R



6.61 As the figure shows, respondents were slightly more confident in their ability to interpret the probabilities table in Variant Q then they were in their ability to interpret the graphs in Variant R correctly. Just over half of respondents were very or fairly confident in their ability to interpret Variant Q correctly (55%) while only 47% were able to interpret Variant R correctly. Conversely a fifth of respondents felt that they were not confident in interpreting the graphs in Variant R compared with 13% for Variant Q. As seen with the clarity ratings, quite large proportions of respondents answered neither confident or unconfident for both variants indicating a lack of engagement with the material.

6.62 The tables below show the variation in levels of confidence by member state and level of financial sophistication.

Table .: Confidence in ability to interpret Variant Q

Column percentages

		Member State							Financial Sophistication		
	Total	**D**	**H**	**IRL**	**I**	**PL**	**E**	**S**	**High**	**Med**	**Low**
	%	%	%	%	%	%	%	%	%	%	%
Very confident	10	10	15	15	6	6	11	9	21	9	7
Fairly confident	44	49	43	54	44	30	54	37	41	49	37
Neither confident or unconfident	29	21	33	19	33	44	25	23	23	30	31
Fairly unconfident	8	13	6	7	8	8	5	11	7	7	13
Very unconfident	5	4	2	2	4	9	2	9	4	3	8
Don't know	4	2	1	2	5	3	2	11	4	2	5
CONFIDENT	55	59	58	**69**	50	36	65	46	**62**	58	44
UNCONFIDENT	13	17	8	9	12	17	7	**20**	11	10	21
Base: All Group 2	*1809*	*256*	*295*	*243*	*249*	*255*	*255*	*256*	*323*	*1001*	*429*

Table .: Confidence in ability to interpret Variant R

Column percentages

		Member State							Financial Sophistication		
	Total	**D**	**H**	**IRL**	**I**	**PL**	**E**	**S**	**High**	**Med**	**Low**
	%	%	%	%	%	%	%	%	%	%	%
Very confident	8	8	12	11	6	5	11	3	17	7	4
Fairly confident	38	43	40	52	43	20	44	29	46	42	29
Neither confident or unconfident	30	22	33	26	29	47	28	24	21	31	35
Fairly unconfident	13	17	8	6	11	15	11	23	8	13	17
Very unconfident	7	7	6	3	8	9	4	13	5	5	11
Don't know	3	3	1	2	3	4	2	7	3	2	4
CONFIDENT	47	51	51	**63**	49	24	55	32	**63**	49	33
UNCONFIDENT	20	23	15	9	18	24	15	**37**	13	18	28
Base: All Group 2	*1809*	*256*	*295*	*243*	*249*	*255*	*255*	*256*	*323*	*1001*	*429*

6.63 In the case of both variants, investors in Ireland demonstrated the highest confidence levels (69% were very or fairly confident in their ability to interpret Variant Q and 63% were very or fairly confident in their ability to interpret Variant R). By member state, confidence levels were lowest among Swedish respondents (20% were not confident in their ability to interpret Variant Q and 37% were not confident in their ability to interpret Variant R).

6.64 For both Variants, levels of confidence varied considerably by levels of financial sophistication. The difference was less marked for Variant Q with 62% of those with high sophistication stating that they were confident and 44% of those with low financial sophistication and no significant difference in levels of confidence between those with high and medium financial sophistication. In the case of variant R, there was a difference of 30 percentage points between the proportion of those with high financial sophistication who felt confident and the corresponding proportion of those with low financial sophistication. For this variant there is a significant difference between the level of confidence expressed by those with high sophistication and those with mid-level sophistication (63% confident compared with 49%). Hence those considering themselves to have a high-level of sophistication are equally likely to feel confident in interpreting either variant but all other investors are considerably more likely to be confident in their ability to interpret the tabular Variant Q.

6.65 Stated levels of confidence in interpreting variants should not necessarily be interpreted in isolation as a way of determining which perform 'better'. It is possible that high levels of confidence in interpreting a variant could be viewed negatively if they are accompanied with low levels of understanding (i.e. if the variant instilled a false confidence in consumers that might lead to them making bad decisions by placing too much weight on information that had misunderstood). Hence it is useful to look at the relationship between confidence in a variant and responses to the understanding questions looked at earlier in this chapter. The table below looks at the number of true/false statements about Variant Q answered correctly by stated confidence in interpreting the variant.

Table .: Confidence in ability to interpret Variant Q by number of correct responses to understanding statements

Column percentages

	Confidence in ability to compare					
	Total	**Very confident**	**Fairly confident**	**Neither confident or unconfident**	**Fairly unconfident**	**Very unconfident**
	%	%	%	%	%	
No correct responses	29	16	22	30	35	48
1 correct response	30	27	31	33	32	22
2 correct responses	28	31	32	27	23	18
3 correct responses	12	26	15	9	10	12
Base: All Group 2	*1809*	*187*	*801*	*518*	*149*	*82*

6.66 As the table demonstrates there is a strong (although not perfect) correlation between confidence in the ability to interpret variant Q and levels of understanding of the variant. Almost half of those who stated that they were very unconfident gave no correct responses to the understanding questions compared with only one in six of those who stated that they were very confident. This reflects the fact that a large proportion of this group (around half) answered 'don't know' for each statement. For all 3 statements, the higher the level of confidence the greater the proportion giving a correct answer although the level of variation differs between the 3 statements:

- In the case of the statement *'The return will always be higher than from a risk free product'* the proportion answering correctly (i.e. that the statement is incorrect) varies from 75% of those who were very confident in interpreting the variant to 37% of those who were very unconfident;

- For *'The chances are that you will get back more than you invested about 40% of the time'*, the proportion giving the correct answer (i.e. false) varies from 45% of those who were very confident to 33% of those who were very unconfident;
- For *'the product will always get the full benefits of any gains achieved by the Eurostoxx Index'*, the proportion giving the correct answer (i.e. false) varies from 46% of those who were very confident to 26% of those who were very unconfident;

6.67 The table below displays the corresponding analysis for Variant R.

Table .: Confidence in ability to interpret Variant R by number of correct responses to understanding statements

Column percentages

	Confidence in ability to compare					
	Total	**Very confident**	**Fairly confident**	**Neither confident or unconfident**	**Fairly unconfident**	**Very unconfident**
	%	%	%	%	%	
No correct responses	13	2	4	10	17	46
1 correct response	5	1	4	6	5	4
2 correct responses	9	11	9	10	11	10
3 correct responses	16	18	17	15	16	13
4 correct responses	15	11	13	20	15	14
5 correct responses	17	10	20	18	16	10
6 correct responses	15	27	17	15	13	3
7 correct responses	10	19	16	6	6	1
Base: All Group 2	*1809*	*403*	*1702*	*1020*	*449*	*147*

6.68 Again there is a clear relationship between confidence in interpreting Variant R and levels of understanding of the variant. Just under half (46%) of those who were very confident answered 6 or 7 statements correctly compared with only 19% of those who were fairly unconfident and 4% of those who were very unconfident.

6.69 The relationship between confidence in interpretation and understanding is evident for each of the 7 statements. As for Variant Q, a large proportion of those who were very unconfident answered don't know at each question (between half and two-thirds). Some of the largest differences in the proportions answering correctly by levels of understanding were for the statements *'If the DJ Eurostoxx performs badly your investment is transferred into the protected pool' and 'If transferred to the protected pool you will not benefit from any recovery in the DJ Eurostoxx index.*

6.70 When asked directly about what information Variant R portrayed, 59% of those who were very confident selected **only** one of the correct responses (*'The impact of different investment conditions upon the performance of the fund' or 'how the fund may perform in the future')* compared with 53% of those who were fairly confident, 47% of those who were fairly unconfident and 24% of those who were very unconfident.

Qualitative findings

6.71 The qualitative research examined two of the three variants tested in the quantitative stage. Variants Q (table) and R (graphs) were selected to investigate the extent to which investors understand these two different ways of presenting information. The hypothesis from the quantitative survey that Q (table) was easier to understand than R (graphs) was also investigated during the qualitative work.

6.72 The third variant used in the quantitative stage, Variant S (backtesting) was not included in the qualitative testing as the quantitative findings showed that around a third of respondents found this variant confusing – the highest of the three variants. There were also some key misunderstandings of what it was showing, e.g. 40% thought it was the past performance of the fund. Whilst not being conclusive evidence to reject this option completely it would appear that there are better ways of showing this type of information (at least from the consumer view) and that time and resource was better spent on refining the other variants.

UNDERSTANDING OF VARIANT Q (TABLE)

6.73 Around two thirds of investors / potential investors felt that the fund described in variant Q was low risk:

“For the conservative, security orientated investor” **Germany**

“Made for those who don’t have a big financial ability” **Italy**

6.74 A few of these explicitly stated that they felt it was low risk because there was a safety mechanism which would be triggered if the DJ EuroStoxx performed badly and this would limit losses.

6.75 However around one third (particularly likely to be Irish and least likely to be Swedish) felt that the fund was medium to high risk:

“Someone who is willing to take a big chance with his money” **Ireland**

6.76 To some extent the perception of the risk associated with the fund depends on each respondent’s attitude to and tolerance of investment risk, but given the capital protection mechanism the fund in question is certainly not very high risk and this fact does not seem to have been understood by all investors.

6.77 Investors were asked how likely they thought the fund was to perform well or badly

6.78 Individuals defined performing well in a variety of ways: the largest group of just under a third felt that the fund would have performed well if it made more than if they had invested in risk-free products (40% probability). There was only the odd mention of defining good performance either as making the same or more than risk-free products (40% + 22% = 62% probability) or as not losing money (40% + 22% + 37.2% = 99.2% probability).

6.79 In terms of performing badly, the largest group (around a quarter of investors) felt that this would be mean getting back less than they originally invested (0.8% probability) whilst fewer felt it would mean getting back less than if they had invested in risk-free products (37.2% + 0.8% = 38% probability) or getting back only about the same as if they had invested in risk-free products (0.8% + 37.2% + 22% = 60%).

6.80 In estimating the likelihood of both good and bad performance only around one third gave an answer which they had clearly pulled off the table or worked out from it (i.e. by adding two figures together) whilst two thirds gave other answers. Investors from Poland, Spain and particularly Italy were most likely to have given figures which were not directly taken from the table.

6.81 Some of this latter group may have rounded up figures before adding them, have added up the wrong cells or simply not be very good at adding figures together; there are also certainly a few who did not use the table at all but instead made their own estimates based on the text and/or personal experience. The majority not being able (or willing) to use the table in the way it was intended probably indicates a need for it to be modified.

UNDERSTANDING OF VARIANT R (GRAPHS)

6.82 Variant R contains two graphs which illustrate the effect of different scenarios upon potential fund performance. Investors were asked questions of both graphs in variant R in order to check whether they were able to interpret them correctly.

6.83 The first graph shows an example where capital protection is triggered. Around three quarters of investors were able to correctly identify what each line on this graph meant and investors in Spain, Germany and Sweden were particularly likely to be able to do this. However it is important to note that some simply read the key of the graph to identify individual lines without this enabling them to unlock the overall meaning of the graph.

6.84 Around one quarter of investors were not able to identify all the lines on the graph and investors in Italy were particularly likely to fall into this category. Most of the misunderstanding centred around the line indicating the dynamic pool, with investors not being able to understand why it stopped at January 2009:

> *"I don't know why the yellow line stops or why the overall fund value goes down"* **Sweden**

6.85 As the aim of the graph is to show how the capital protection and the transfer of funds from the dynamic to protected pool works, that this is the greatest cause of misunderstanding is a concern.

6.86 To further test understanding of the first graph, investors were asked if they invested €100 what the value of the fund would be by January 2013. Over two thirds got this correct, with investors in Sweden and Germany doing particularly well. It should be noted however that not all investors got this information through looking at the graph – several mentioned that they would get back '€100 minus fees' which is explicitly stated in the text above the graph.

6.87 Of those who were not able to arrive at the correct figure almost half were looking at the wrong line and thinking that the DJ Eurostoxx or the value of protected pool was in fact the fund value, the remainder were largely unable to give any answer. Investors in Italy, Spain and Ireland were particularly likely to give an incorrect answer.

6.88 The same question ('If you invested €100 what would the value of the fund be by January 2013?) was asked of investors when they were looking at the second graph – an example with capital gain. The proportions of correct and incorrect answers were very similar to those for the first graph with over two thirds giving a correct answer and investors in Italy, Spain and Ireland most likely to be incorrect. Of those answering incorrectly almost half were looking at the correct line but not being able to interpret it very accurately and not looking at the text on the graph saying 'final performance of the fund is 42%', the remainder were largely unable to give an answer.

CLARITY

6.89 Despite the less than total understanding of variant Q (table), three quarters of investors did feel it was clear, with those in Italy finding it clearest and the Irish finding it least clear.

6.90 The third column entitled 'examples of when this would apply' was the source of confusion for several of those who found the variant unclear as it was seen to be too complicated and include too much information:

> *"The third column would take a bit of reading and it's not simple"* **Ireland**

6.91 The balance of how much information to give is a delicate one as many wanted more explanation of some kind: there was the odd mention of wanting to know how the probability was calculated and how much you might stand to lose or gain, however the things individuals wanted to know were largely disparate and no conclusions can be drawn from them. One suggestion for improvement that did stand out was the idea of presenting the information from the table in the form of a pie chart – although only specifically mentioned by a few the idea of a visual was widely welcomed and may make it easier for investors to realise the effect of adding up various cells / segments / outcomes.

6.92 Turning to variant R (graphs), around three quarters of investors claimed to find this clear. Swedish and Spanish investors were most likely to find it clear whilst Irish investors were least likely to.

6.93 Despite the similar proportion of investors claiming to find variants Q and R clear, comments made about the clarity of the graphs were sometimes less than emphatic:

> *"It's clear when you make the effort"* **Sweden**

6.94 In addition to this, criticisms of variant R were more consistent and not the collection of disparate individual concerns which variant Q provoked. Variant R was felt to be too confusing and to require too much time and effort from the reader:

> *"It's a hotch potch of shading and dotted lines – doesn't mean anything to me"* **Germany**
>
> *"You have to invest some time in trying to figure it out"* **Ireland**
>
> *"It's just too much like hard work"* **Ireland**
>
> *"Made me switch off straight away…too complex for me…if you'd sent me that in the post I'd chuck it straight in the bin"* **Germany**

6.95 Few improvements were suggested but some wanted to see the effect of charges reflected in the graphs and some felt they needed more explanation (including more about when the capital protection mechanism is triggered):

> *"I would like to have more of what you find in the graphs explained in the text"* **Sweden**

PREFERENCE

6.96 There was no consensus from investors as to whether variant Q (table) or variant R (graphs) was most useful – equal proportions chose each with a small number wanting a combination of the two.

6.97 When individuals were explaining why they had chosen one variant or another it was clear that for many their choice had been based on whether they personally found it easier to interpret graphs or numbers and text:

6.98 Therefore, those who preferred variant Q (table) commented:

"It's clearer… when it comes to graphs, lines and figures I don't understand it" **Ireland**

"It puts in words what you have to interpret from the other one" **Germany**

6.99 Whilst those who preferred variant R (graphs) felt:

"It's always easier to relate to a graph than a table" **Ireland**

"People don't read, they look at the graphics" **Italy**

6.100 How different investors like to receive information was the key factor for many in their preference rather than how clear or comprehensible each variant was in its own right i.e. for those who like graphs a slightly confusing graph is better than a clear table whilst for those who are unwilling to engage with graphs any kind of table will be more effective.

6.101 This indicates that those who suggest the need for combining the two approaches may have a point as this would ensure that the information could be understood by all, no matter how their brain works.

6.102 It was also felt by those who suggested a combined approach that the two variants showed different things, with only variant Q mentioning probabilities:

"Q is the likelihood and R explains more how it works" **Sweden**

6.103 For Phase 2 of this research it may be worth testing a variant of Q shown as a pie chart as this would show probabilities in the form of percentage and have accompanying text yet also provide a visual for those who find this more engaging.

7 Likely engagement with disclosure material

7.1 As well as specific views on the variants concerning charges, risk and performance scenarios, the qualitative research sought to investigate at a general level whether individuals felt they would be likely to engage with the information if purchasing an investment.

7.2 Over a third of those who had investments (as opposed to planning one only) had been disappointed with investment products they had taken out in the past and this was more likely to be the case in Hungary, Germany and Ireland. There were a variety of reasons for this disappointment including those who felt they did not have enough information available at the time of purchase:

"Later on some interesting details were coming up and they changed my mind completely" **Hungary**

7.3 There were mentions of insufficient information on charges and what companies would be invested in and for some a lack of complete information led them to make an investment at the wrong time or be penalized for withdrawing early. Investors were split between those who felt that they had been misled when taking out the investment and those who felt it was their own fault for not looking into the investment thoroughly enough. Those who have had a previous bad experience due to a lack of complete information are likely to be more motivated to engage with information they are given about investments in the future.

7.4 Over half of the investors had received information of a similar type to the variants tested in this research when looking at investments in the past and this was particularly the case in Germany and Sweden whilst those in Poland were least likely to have received such information. Not everybody valued written information:

"I would have discussed this sort of thing rather than reading it over" **Ireland**

7.5 However, of those who had received such information in the past, the vast majority did find it useful.

7.6 In terms of the key features that individuals want to know about when thinking of investing, risk (including both the chance of making a profit and the chance of making a loss) was mentioned by a large majority with several pointing out that this is crucial as the whole aim of the investment is to make money. Around half of the investors and potential investors felt charges were of key importance to communicate (all charges, including transaction costs) and this was especially the case in Germany, Poland and Ireland. Around one in five particularly wanted to know the time horizon for the investment, i.e. whether it was a short, medium or long-term investment, and a handful were interested in whether a product would be investing in ethical markets and companies. Although few specifically mentioned the past performance of funds as being of key importance, it was mentioned when investors were considering variants in more detail. It is likely that past performance was not mentioned upfront because it is important only in helping investors to assess risk rather than in and of itself.

7.7 To sum up, indications are that individuals do find information such as that tested in this research to be useful and they are likely to engage with it. The vast majority felt the optimum time to be given such information was at the beginning of the decision making process where the information would have the most impact and value. Although a few investors would only need this level of detail when comparing shortlisted products, most felt that they would need the information as soon as they began considering an investment in order to draw up a shortlist and make the right choice:

"Right at the beginning so you're able to compare the right thing" **Germany**

8 Conclusions and Recommendations for Phase 2 Testing

8.1 Our principle objective for phase one was to set out clear recommendations for phase two of the project, providing guidance for the CESR working group on how to optimise communication of the key messages to consumers. Our interpretation of the evidence is based on the relative effectiveness of the individual disclosure variants that we tested. This means it is difficult at this stage to draw conclusions as to how an improved version of these variants would work as a single document where the different elements of a UCITS fund can be presented together and messages can be reinforced across different sections of the document to improve clarity and enhance understanding. We have taken each variant and drawn conclusions and made recommendations accordingly.

Strategy and Objectives

8.2 A single variant for strategy and objectives was tested and hence we cannot make a judgement about relative effectiveness. However, it is clear from the evidence that the mocked-up variant demonstrated an acceptable level of clarity. In relation, to the fund's strategy there appears to be a relationship between clarity and understanding: those who felt the document was clear demonstrated a better understanding of the main messages. While some respondents requested more information to help make an informed decision, such as more details about the Index, we feel this would detract from the key messages and that there are other ways outside of the main document for communicating this information. The following are the key recommendations that we believe would help improve the strategy and objectives section:

- ➢ This is a key section which sets the overall context for the document. Using detailed technical terms at the outset does not facilitate engagement and works against overall comprehension. We would recommend making this section as simple as possible, and avoid complex financial terms. We recommend reviewing the language used in the variant to make it as simple as possible. In particular, an improved variant should seek to deliver higher levels of understanding regarding investing in bonds and changes in the value of the fund relative to the markets in which it is invested.
- ➢ While increasing the length of this section of the document would be counter-productive, there is evidence of misunderstanding of the basic operation of investment products in relation to capital protection and it would be worth considering the inclusion of some form of simple health warning somewhere in the KII document.

Past Performance

8.3 The key issues to consider for the past performance section are the pros and cons of displaying 5-year versus 10-year time periods and comparisons of investors understanding of fund performance relative to a selected Index. Respondents generally stated that the variants tested were clear; however, their responses to questions that tested their understanding contradict this perceived clarity. Respondents were generally able to determine overall performance of the fund in comparison to the index that was used (MSCI EM), but stumbled in determining specific levels of fund growth. Additionally, respondents had difficulty comparing past performance, in side-by-side comparisons, when the 'yearly growth rate' scales had differing calibrations. The following are the key recommendations that we believe would help improve the past performance section:

- ➢ Display past performance over a 10-year period: there is a clear preference among respondents to display past performance over a period longer than five years. The longer timeframe potentially provides the investor with more information. However, it should be made clear that past performance should be used as a guide and not a guarantee of future performance, as many respondents seem to believe

- Clarify the purpose of the MSCI EM: a bare majority understood that the MSCI EM is used a comparison to the fund one may purchase, a number saw it as a gauge of outperformance compared to the fund or an indicator of the fund's performance. It is possible that some form of shading effect giving the MSCI-EM data less prominence that the fund itself may help to reduce this latter issue.
- Clarify any differences between scales used for 'yearly growth rate': while it is difficult to harmonise the scales across all funds due to differing levels of growth, some explanation is required to avoid misinterpretation in comparing funds. This could perhaps be achieved by the addition of 'data labels' to the bars in the comment.

Charges

8.4 The key issues to consider for the charges section are whether there is added value of an illustration of charges section and the pros and cons of providing information on charges/fees using percentage or monetary amounts. While respondents there was no discernable difference in respondents ability to 'calculate' charges/fees using each of the three methods tested (simple narrative, percentage figures in text and currency figures in a table), there was a clear preference for the illustration of charges that provided guidance using currency figures:

The following are the key recommendations that we believe would help improve the charges section:

- Display charges/fees using an illustration of charges in monetary amounts: respondents clearly preferred this version citing clarity, easier comparison and depth of information compared to the other versions tested
- Clarify the method of calculation: while respondents feel that charges/fees expressed in currency were easier to understand, there was difficulty in actually interpreting the table in terms of charges/fees as a percentage of the investment. Additionally, it may be necessary to include any other pertinent charges/fees such as transaction costs
- Investigate what further could be done to emphasise that the table only shows an illustration that would apply under certain growth conditions. It may be worth explicitly saying that the charges would differ if levels of growth were different.
- Display charges/fees in native currency: respondents show a clear preference for seeing charges/fee in their native currency (although it is a minority who state that they would not be able to use the information at all unless it was in their own currency).

Risk

8.5 The key consideration in relation to the risk section relate to the effectiveness of a pure narrative description of risk versus an approach that incorporates a synthetic indicator alongside a narrative description. Each variant was tested against a high risk/reward fund and a low risk/reward fund. The following are the key recommendations that we believe would help improve the risk section:

- The quantitative evidence suggests that a narrative indicator leads to marginal gains in consumer understanding of risk and reward, but this needs to be weighed against a stronger consumer preference for a presentation in the form of a synthetic indicator. The qualitative evidence lends further support for improvements to be made to a narrative indicator which includes some form of graphical communication.
- On balance, our recommendations lean towards an improved version of a synthetic information as an effective communication tool for consumers. The benefits of an improved synthetic indicator are a better balanced communication of the balance of risk and reward. A pure narrative indicator appears to be more heavily focused on risks alone.

- We recommend that an improved synthetic indicator should not over-simplify key messages in relation to risk and reward and that the right balance needs to be struck between providing the amount of information required for an investor to make an informed decision. The text needs to make clear that class 1 funds are not guarantees and it is particularly important to communicate this to less experienced investors. We would also advocate reviewing the scales for the synthetic indicator and giving some consideration towards more explanation of the scale.
- That said, it does appear that the preference is based on a 'first impression' type basis and there is some evidence that consumers become less convinced of the value of an indicator when they start to think about how ratings are arrived at. It is possible that another visual display of risk could achieve a similar level of engagement with the material while achieving the same level of understanding.
- It is also worth noting that much of consumers stated preference for the indicator is based on the perceived ease of comparing funds using this scale. If reality meant that the vast majority of funds achieved a rating somewhere in the middle of the scale then some of this value would be lost.

Performance Scenarios

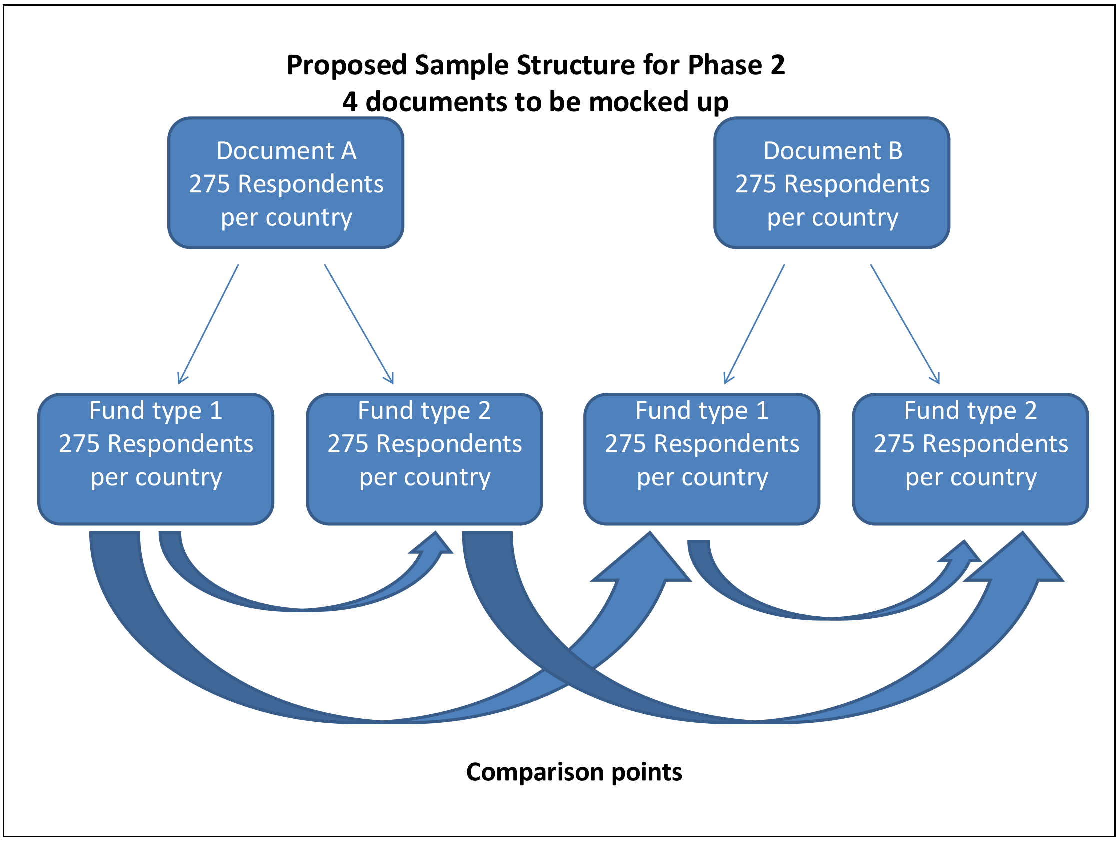
8.6 Performance scenarios relate to a particular form of communicating risk and reward for structured funds. The key considerations for performance scenarios concern the relative effectiveness of communicating risk through i) a table showing the likelihood of achieving different rates of return; ii) graphs to show the possible return of the fund under favourable and less favourable conditions; and iii) a graph displaying backtesting data showing how the fund would have performed under historic market conditions. The following are the key recommendations that we believe would help improve the performance scenarios section:

- On the test of clarity the evidence strongly supports the use of a table. Investors suggest this form of communication could be improved by defining technical terms and explaining probability in more detail. In relation to comprehension, improvements need to be made to the wording of messages about product guarantees which are set out in the initial strategy section. These are poorly understood by investors.
- In terms of understanding, a graph displaying back testing data was broadly misunderstood and we do not feel this approach facilitates consumer comprehension. The key issue concern the table showing different rates of return versus graphs to show possible returns under different conditions. On the basis of the qualitative research, our recommendations lean towards an improved tabular version for communicating risk and reward information for structured funds. However, given that there are mixed consumer preferences for both tabular and graphical formats, we suggest developing a variant taking the existing table but with the information presented as a pie chart. This improvement would show probabilities in the form of a percentage and have accompanying text yet also provide a visual for those who find this more engaging.

Stage two methodology

8.7 The final set of recommendations relate to the design of the quantitative research for phase two, where we recommend the following plan.

Figure .: Proposed approach for Phase 2



8.8 We recommend testing mocked up documents for two contrasting fund types. The fund types will need to be agreed but at this stage, we do not see a forum to test structured funds. We also recommend that documents should be mocked up for each fund type for two contrasting presentations. One document would be a “traditional” document which reflects the recommendations based in this report. The second document would be more innovative and would be based around further enhancement undertaking by the CESR working group. The details for each document will require further discussion before final agreement can be reached, but the broad principle should be that each document is broadly contrasting and reflects the evidence gathered at stage one.