# UBS *Investor Watch*

Analyzing investor sentiment and behavior

2Q 2013

## *The 'new normal' is here to stay*

### Top insights:

1. Investors have redefined risk
2. Personal debt characterized as "good debt" and "bad debt"
3. Older investors are willing to endure tax increases to reduce future debt burden
4. Long-term care remains a greater concern than retirement, with a focus on self-reliance
5. Lack of long-term care planning suggests a potential crisis

UBS

## The permanently pragmatic investor

After the financial crisis of 2008, there was much discussion about the "new normal"—a more reasoned and grounded approach among American investors. While few questioned that investor outlook and mindset had changed in the short-term, many wondered how long this would last, particularly as investors historically displayed tendencies toward amnesia—being "forgetful" about their losses when markets rebounded. However, based on the latest top 5 insights from *UBS Investor Watch*, it appears that the "new normal" is here to stay.

Even as they see the economy and their own financial situations improving, investors remain focused on achieving financial goals within the context of avoiding risk. The industry has historically defined risk using terms like volatility, standard deviation and other jargon. But, investors of all ages define risk as permanent portfolio losses. This redefinition of risk results in comfort with their current asset allocation, often including a considerable cash buffer. And when investors think about borrowing—and they *are* borrowing—it's for longer-term "investments" like a home or education, not for living beyond their means.

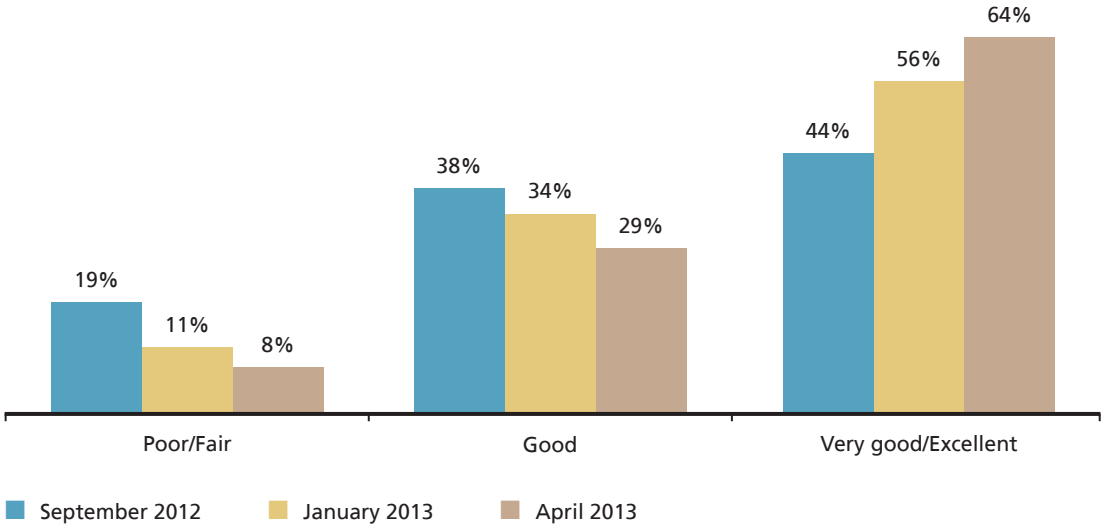
With this more pragmatic mindset, investors value planning ahead, and feel highly prepared for key goals like retirement and protecting against some catastrophes with "rainy day" savings and life insurance. Still, a potential crisis looms—long-term care. This remains a significantly greater concern than retirement. However, long-term care planning is severely lacking, and this challenge to investors is exacerbated by rising healthcare costs and an increased life expectancy.

1

### Investors focus on avoiding risk, even as their optimism grows

As the financial markets continue their recovery, highlighted by the S&P 500 and the Dow Jones Industrial Average recently reaching record highs, investors feel much better about their finances. Nearly two-thirds (64%) of investors say their financial situation is "excellent" or "very good," up considerably from six months ago (44%). The majority (52%) feel their finances are better than a year ago, up significantly from 40% in January.

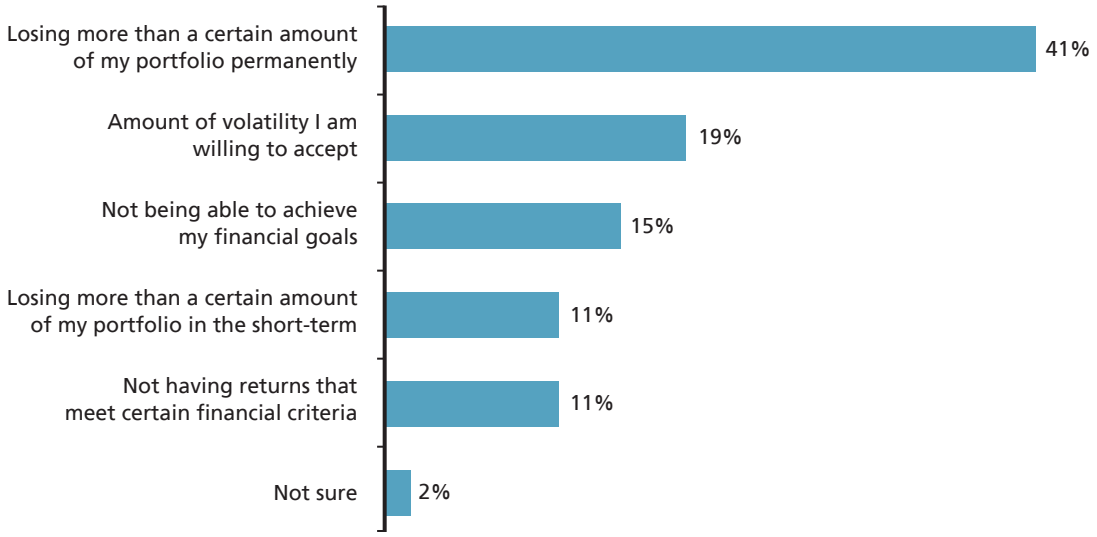
**View of personal financial situation**
**Question:** *"How do you feel about your overall financial situation today?"*



Investors' economic outlook has also improved, primarily in the short-term. Nearly half of investors (47%) have an optimistic outlook for the economy over the next 12 months, notably higher than their outlook just three months ago (32%). Market performance is likely driving this improved short-term outlook, as only 23% are highly concerned about financial markets, compared with 33% in January.

While investors' finances have improved, they are not making any changes to their portfolios. When markets expand, investors tend to become more aggressive. But there has been a deep residual impact from the financial crisis and the market volatility of recent years, and they have settled into a more deliberate approach, founded on avoiding risk. Investors now define "risk" as **permanent** portfolio losses and their risk tolerance remains conservative or moderate rather than aggressive. Surprisingly, investors of all ages define risk as permanent portfolio losses.

**Risk=Permanent loss**
**Question:** *"When you think about risk in your investment portfolio, what does risk primarily mean to you?"*



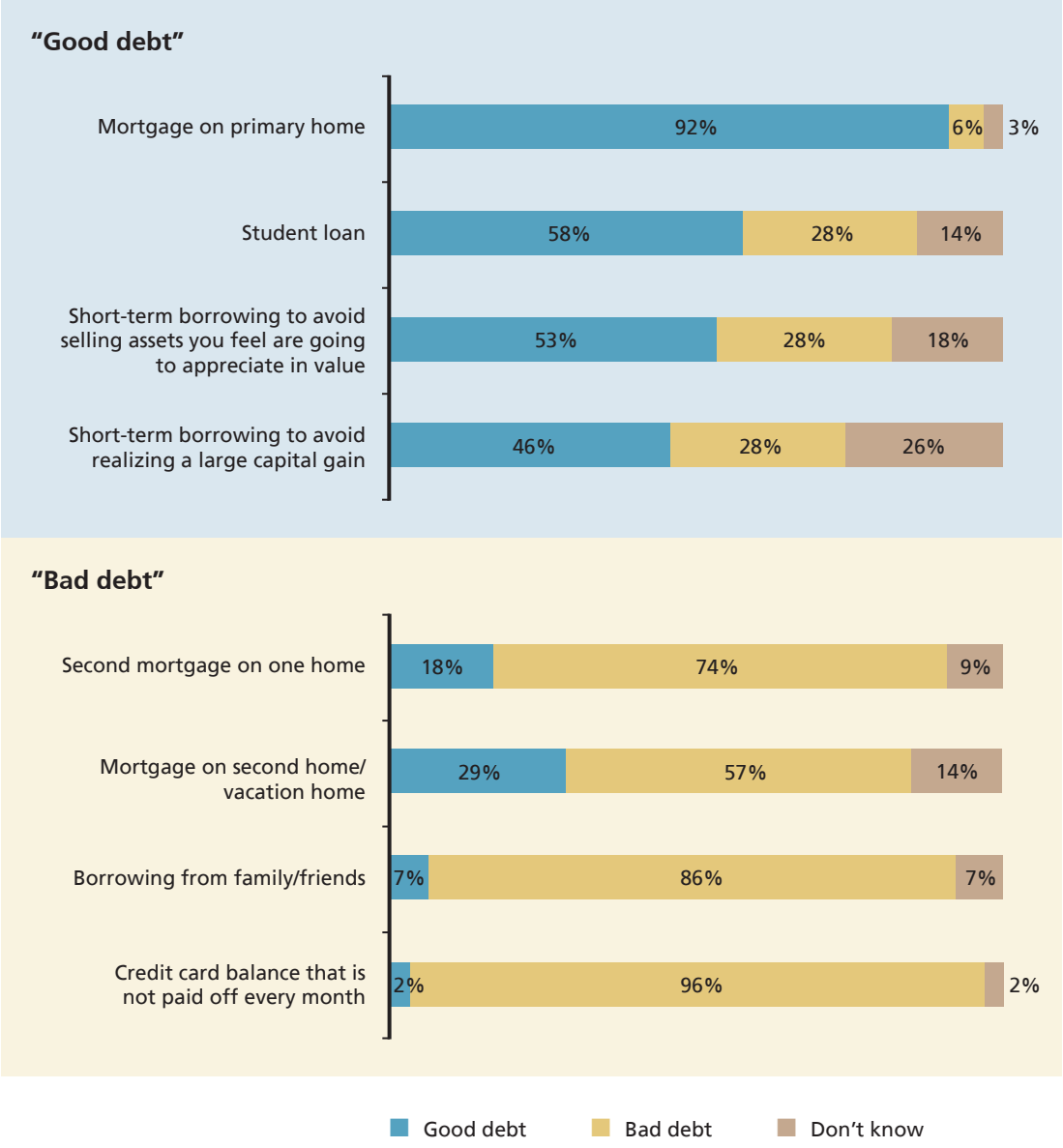

With investors remaining more concerned about avoiding losses (70%) than missing out on market gains (30%), this translates into taking an investment approach that is no longer about beating the market. Only 14% aim to outperform the market. In addition, most investors feel they are holding the right levels of cash (66%), and few say they plan to reduce the cash they have. In fact, investors' average allocation of cash has held steady around 20% for the past three years.

2

## Redefining the role of personal debt: "good debt" versus "bad debt"

While some investors have become more averse to borrowing (29%), most investors remain pragmatic in their views on personal borrowing—believing there is "good debt" and "bad debt." "Good debt" equates to making a sound investment in the future. This includes some of the most frequent borrowing activities—a mortgage on your primary home and student loans, but also short-term borrowing to avoid selling an asset you expect to appreciate at a higher yield or to avoid realizing a large capital gain. "Bad debt" involves taking risk, living beyond one's means or borrowing for luxuries. This includes not paying off your credit card balance, borrowing from friends/family, having a second mortgage on your home and even having a mortgage on a second home.

**Good debt versus bad debt**
**Question:** *"Which of the following would you consider to be good debt versus bad debt?"*



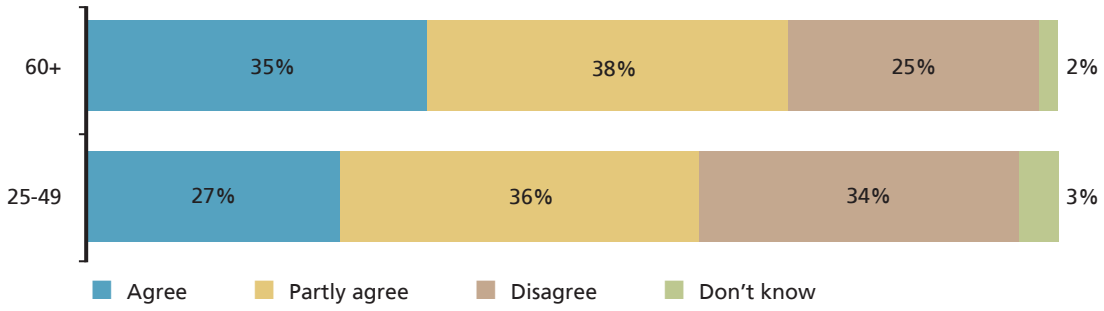
3

## Older investors are so concerned about the national debt burden on future generations, they are willing to endure additional tax increases

Reflecting their pragmatic view for handling their own finances, most investors recognize that tax increases were, and continue to be, needed in conjunction with spending cuts. Seven in 10 investors feel the tax increases in the "fiscal cliff" deal were about right or should have been higher, and 6 in 10 expect there will eventually be more tax increases to help address the national debt issue.

Older investors are more willing to pay additional taxes to reduce the debt burden for future generations (35% agree while 25% disagree). These investors are most likely to feel taxes should have been increased more than they were in the fiscal cliff deal (35% compared with 22% among those under 50). A combination of feeling responsible for leaving the country in a better place and being less impacted by recent tax policy changes are likely drivers of this perspective.

**Willingness to pay more taxes**
**Question:** *"Please indicate to what extent you agree or disagree with the following statement: I am willing to pay more in taxes if it means helping to avoid placing an undue burden on future generations."*




Investors overall have low confidence that Washington will be able to achieve meaningful debt reduction. The political environment in Washington remains their top concern (73% highly concerned), and the size of the national debt is also a big worry (60% highly concerned). Eager for spending cuts, investors are not overly worried about the sequester. Only 27% are highly concerned about its impact, and nearly half think the automatic budget cuts are either a good thing or "better than nothing because government spending is out of control."

The one area where investors are highly concerned about the sequester is that government will continue to make short-term deals instead of agreeing to a "grand bargain" (70% highly concerned) that more comprehensively addresses the debt issue.

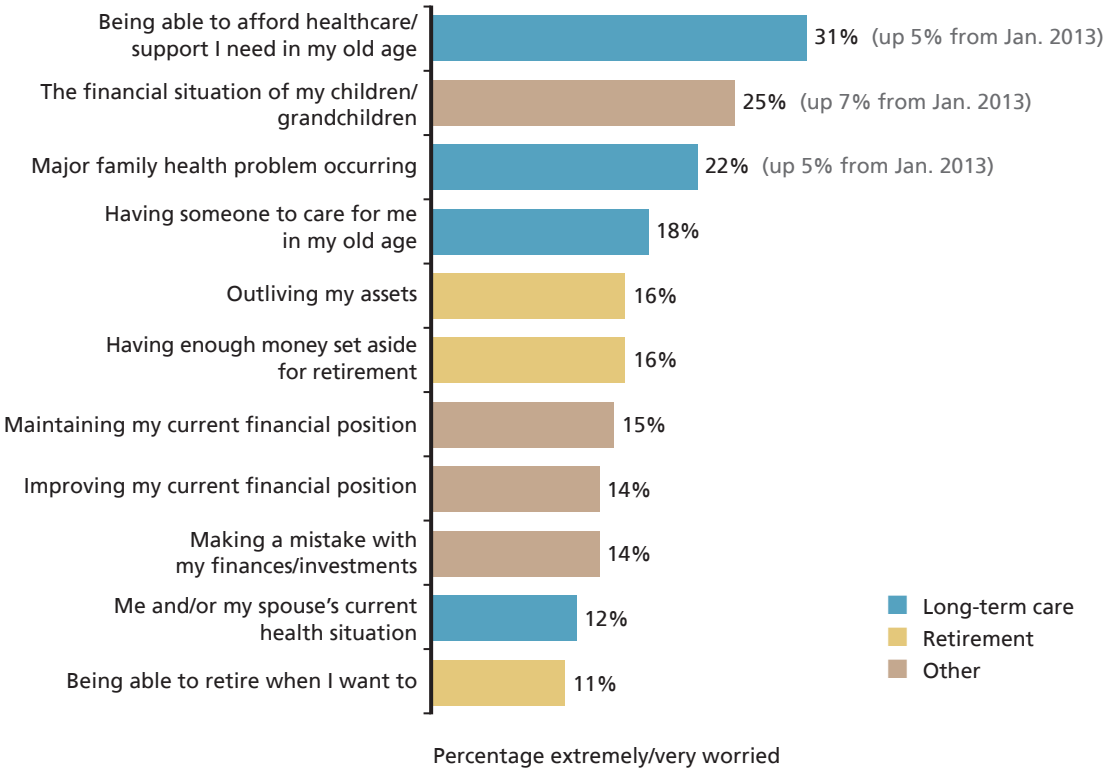
4

**Investors' biggest personal concern is long-term care—significantly greater than retirement—and maintaining self-reliance as they age is critical**

Being able to afford the healthcare and support investors need in their old age remains their top personal concern (31%, up from 26% in January). As we found in our January 2013 *Investor Watch*, long-term care concerns easily trump retirement worries, as only 16% are highly concerned about having enough money set aside for retirement. Additionally, rising healthcare costs are investors' second biggest economic concern (64% highly concerned).

**Top personal finance concerns**

**Question:** *"How worried are you about each of the following regarding your personal finances?"*




In thinking about how they want to age, most investors are focused on maintaining self-reliance as much as possible and for as long as possible; 44% indicate remaining self-reliant will be most important to them as they age, followed by 38% who are focused on preserving their quality of life.

Two-thirds of investors would prefer to remain in their own homes, with only 3% wishing to move in with family. And if they need assistance with daily living activities, most would prefer this support come from a professional health aide rather than a loved one—although they would like their loved ones nearby.

5

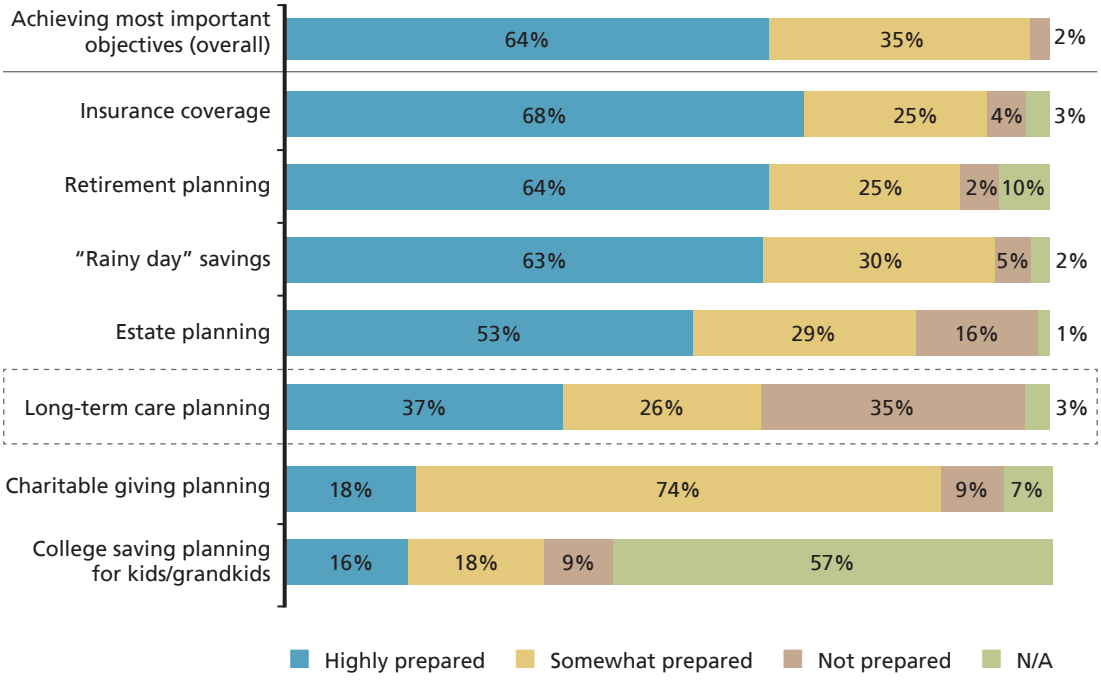
## But investors aren't preparing for long-term care issues

As reported in the January 2013 *Investor Watch*, investors believe in the value of financial planning, and those who consistently follow a plan feel much more confident in their ability to achieve their goals. And most investors feel highly prepared regarding most of their important financial needs and goals.

However, when it comes to planning for long-term care needs, only 37% feel highly prepared. In contrast, 64% feel highly prepared in their retirement planning, followed closely by other important objectives including insurance coverage, "rainy day" savings and estate planning.

This helps explain why investors are more concerned about long-term care than retirement: they know this topic is increasingly important as people live longer and healthcare costs continue to rise—but many have not yet planned for it. Long-term care could be a looming crisis and a challenge many will need to face.

**Preparation for most important objectives**
**Question:** *"How well prepared do you feel for each of the following?"*



# *A closer look: 'New normal' tougher on younger and female investors*

## Age effects

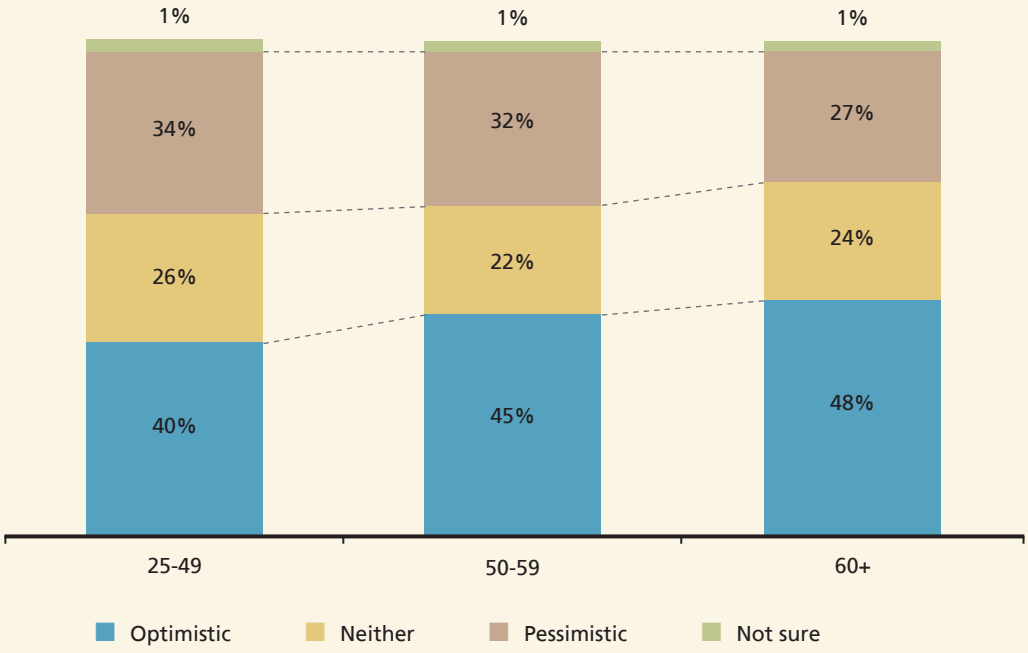
**Younger investors face greater challenges than their parents in preparing for retirement and aging**

Investors under 50 face several challenges their parents did not:

- Fewer pension plans to help provide income during retirement
- Experienced financial crisis and associated investment losses (and in some cases, job losses) during their peak earning years
- Potential for reduced entitlement benefits (Social Security, Medicare) by the time they retire
- Longer life expectancy to finance, with healthcare costs rising quickly

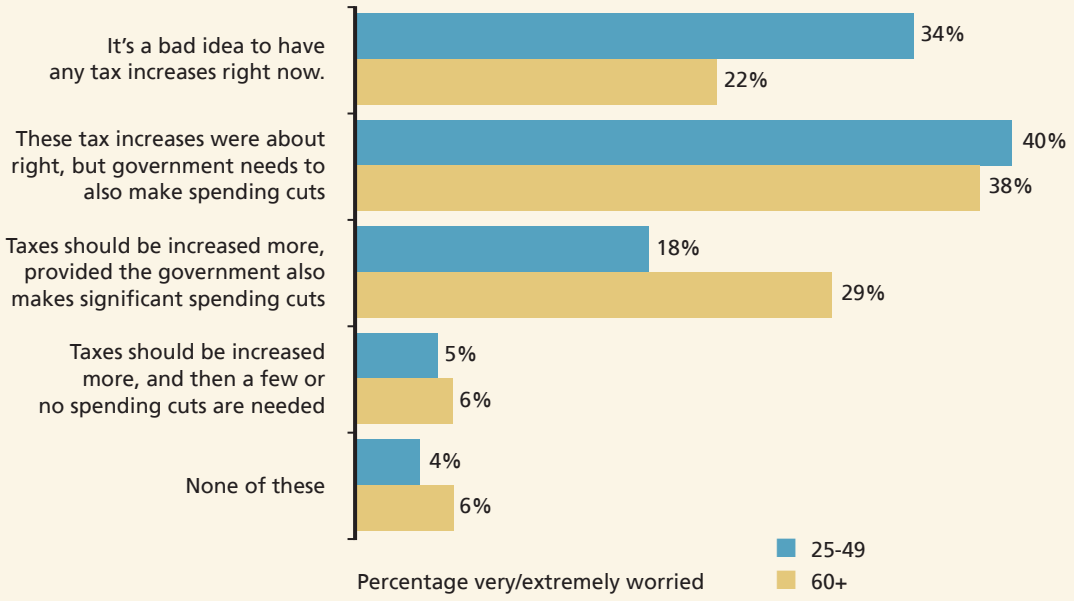
Against this backdrop, it's not surprising that younger investors are less optimistic about the recovery of the economy and more worried about the financial markets. Investors under 50 are less optimistic about the short-term economic outlook (40%, compared with 49% among those over 60) and are less likely to believe the U.S. economy is strengthening (32%, compared with 43%). Additionally, they are more worried about financial markets, continuing market volatility and real estate prices.

**Short-term economic outlook by age**
**Question:** *"How would you describe your outlook on the U.S. economy for the next 12 months?"*



Younger investors also feel the impact of the recent tax policy changes and are more worried about future tax increases. Nearly half (47%) of those ages 25-49 have felt the impact on their paycheck, and these investors are much more likely to believe it was a bad idea to raise taxes right now. Additionally, 51% are highly concerned about more tax increases compared with only 39% among investors over 60.

**Views on recent changes to tax policy**
**Question:** *"Please indicate to what extent you agree or disagree with each of the following statements relating to taxes."*




And as one would expect, younger investors are the least prepared for dealing with healthcare issues after retirement. They are much less knowledgeable about topics like Medicare and long-term care, and are the least prepared in terms of long-term care planning (22% highly prepared, compared with 34% not prepared). While these issues may not be immediate for these younger investors, being able to afford the healthcare and support they need in their old age remains the top personal concern for this age group (32% highly concerned).

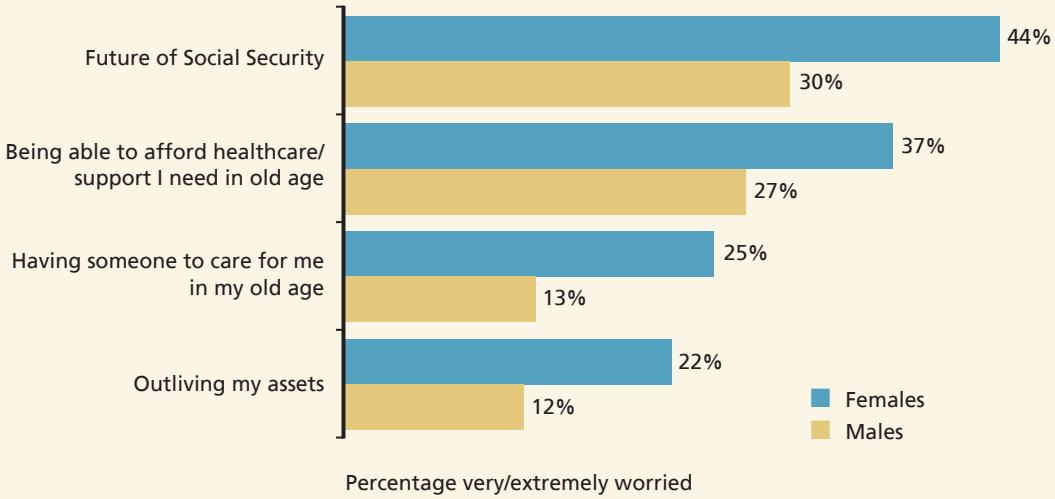
# Gender gaps

**Longevity creates unique challenges for female investors**

Issues relating to long-term care and even retirement are particularly pronounced for women. Women live on average five years longer than men (81 versus 76), and 40% of all women 65 and over live alone.* So women likely will need their assets to cover them for more years in retirement, and they are more likely to be on their own during those later years. Given these facts, it's not surprising that women are more concerned about long-term care and their finances in general during this period. Specifically, they are more concerned about the future of Social Security, being able to afford long-term care, having someone to care for them in their old age and outliving their assets.

**Concerns about aging by gender**

**Questions:** *"How worried are you about each of the following relating to your personal finances?" "How worried are you about each of the following in terms of potential impact on your financial goals or objectives?"*




Accordingly, women also see how the effects of the sequester and the current budget discussions could impact their finances as they age. Women are more worried about the effects of the sequester overall (32% highly concerned, compared with 23% of men) and are more likely to view it negatively (54%, compared with 46% of men). In particular, women are considerably more worried about the sequester's automatic cuts to Medicare and other non-defense programs, possible changes to Medicare and Social Security, and a potential negative impact on their ability to achieve their goals.

In particular, women are more concerned about each of the following related to the sequester:

- Automatic cuts to Medicare and other non-defense programs (55%, compared with 41% of men)
- Changes to Medicare (55%, compared with 44% of men)
- Changes to Social Security (54%, compared with 40% of men)
- Negative impact on my ability to reach goals (30%, compared with 22% of men)

*2010 U.S. Census Bureau.

**About the survey:** UBS Wealth Management Americas surveys U.S. investors on a quarterly basis to keep a pulse on their needs, goals and concerns. After identifying several emerging trends in the survey data, UBS decided in 2012 to create the *UBS Investor Watch* to track, analyze and report the sentiment of affluent and high net worth investors.

*UBS Investor Watch* surveys cover a variety of topics, including:
- Overall financial sentiment
- Economic outlook and concerns
- Personal goals and concerns
- Timely topics, such as impact of the sequester and the "fiscal cliff" agreement

For this third edition of *UBS Investor Watch*, 2,611 U.S. investors responded to our survey from March 19–25, 2013. Investors surveyed have at least $250,000 in investable assets; half have at least $1 million in investable assets. The survey included:
- Investors ages 25-90
- 1,584 men and 1,027 women
- 434 UBS clients

## Looking ahead: 5 things we're tracking

1. How do budget talks and any agreements reached in Washington impact investor outlook?
2. How well do investor asset allocations match up with their risk tolerance?
3. How are different generations within families financially supporting each other?
4. Are investors planning appropriately for financial support provided to their extended families?
5. What does long-term care mean for different age groups?

*The next* UBS Investor Watch *will be released in 3Q 2013 with the results of the 5 things we're tracking.*

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