

Exploring the Investment Behavior of Minorities in America

This fact sheet provides a cultural perspective about the investment behavior of racial/ethnic minorities in America. The topics discussed range from minorities' financial socialization, including parental involvement in their financial education and their sense of financial security during childhood, to their learning preferences, risk tolerance levels. The facts discussed here suggest that financial education programs for minority adults would be best suited if they were tailored to the needs of each specific audience.

The study "Gender Differences in Investment Behavior" (Hira and Loibl, 2006) identified a number of significant environmental and personal factors that influence investment behavior in America. This study paid particular attention to the investment actions, attitudes, motivations, needs, and wants of women in high-income households (for more information about women investors, see "Examining the Investment Behavior of High-Income Women in America," "Comparing Search Strategies for Investment Information in America," "Strengthening Investor Confidence of High-Income Women in America," and "Promoting Investment Involvement among High-Income Women in America"). However, the study also revealed useful knowledge about the investment behavior of minorities in America. It began to answer questions about racial/ethnic minorities' financial socialization, sources of investment information, risk tolerance levels, and confidence in their investment abilities. This fact sheet summarizes those findings and discusses their implications for financial educators.

Methods

In the fall and winter of 2005 and 2006, the Iowa State University Center for Survey Statistics and Methodology conducted a telephone survey of a representative sample of high-income investors in the United States. In all, 911 telephone interviews were completed, producing a twenty-two percent response rate. Each phone interview lasted an average of twenty-two minutes.

About twenty-three percent of the interviews were conducted with members of three minority groups, with roughly equal numbers of African American (7.46%), Asian (7.57%), and Hispanic (7.57%) respondents. Fifteen respondents refused to specify their race or reported a mixture of minority backgrounds. Data analysis of their responses revealed knowledge about high-income minorities' investment behavior in America, beginning with their responses about financial socialization. For more information regarding the methods and design of this study, see the fact sheet titled "Studying the Investment Behavior of Women & Men in America."

Financial socialization

In minorities' responses about their financial socialization, each group of minorities—African American, Asian, and Hispanic—identified their parents as the main source of their financial knowledge. Additionally, each group identified their parents as having influenced both the way they handle money and their attitudes about saving, although a slightly larger proportion of African Americans than other minorities indicated that their parents discussed money-handling, while more Asians reported that their parents discussed the importance of saving money for the future.

Among African Americans, the person reported as having the greatest influence on an investor's financial socialization was the mother. In contrast, whites, more than any other group, identified their fathers as the person who influenced them. Hispanics and African Americans were more likely than whites or Asians to identify an "other adult" as the person who most influenced their approach to handling money.

Part of financial socialization is a person's sense of financial security during childhood. The majority of Asians and whites in this study indicated that while growing up, they felt their family's financial situation was either secure or very secure. On the other hand, fewer than half of African Americans or Hispanics felt similar levels of financial security during childhood.

Finally, a person's financial socialization may influence how investment decisions are made in each household. Many respondents such as one-third among African Americans and Asians and one-fourth among Hispanics and whites—made investment decisions alone.

However, a majority of respondents made investment decisions jointly with their spouse. A very small proportion of respondents in this study involved other adults in investment decision-making, and this proportion was highest among Hispanics and whites.

Investors may begin their financial socialization as children at home, but one's financial education rarely ends there. Investors use various sources of information and prefer to learn about investments in specific ways. The next section discusses minorities' preferences in these areas.

Information sources

There are several informational sources available for those who want to learn about investing, including financial advisors, the internet, the workplace, and other people. Likewise, there are different ways that people can learn—for example, they can attend seminars or do their own research about investments. Each of these appeared in minorities' responses to the survey questions.

Of all the survey respondents, a larger proportion of whites used financial advisors as sources of investment information. This number was followed by African Americans. In contrast, a much smaller proportion of Asians or Hispanics were using financial advisors in this capacity.

The workplace was identified as a source of investment information only by a very small proportion of the respondents (slightly over 10% of African Americans, Asians, and whites, and 7% of Hispanics). However, friends seemed to play an important role in providing investment information for African Americans and Hispanics, and for a somewhat smaller proportion of Asians and whites.

Other potential sources of investment information (radio, classes/workshops, investment clubs) were only identified by approximately five percent of the respondents in this study. A majority of the respondents in each group indicated that they prefer to do their own research—they want to know the details regarding investment issues they investigate. Some, however, prefer to attend seminars. African Americans and Asians were more likely to fall into this group than Hispanics or whites.

Another area addressed in the telephone survey was investors' risk tolerance levels.

Risk Tolerance Level

Risk tolerance is the acceptable amount of risk an individual investor is willing to undertake. While risk tolerance is only an individual preference, large deviations of risk preference between social groups of people (e.g., race, education) can lead to different portfolio returns and wealth inequalities. High-risk investors are more likely to be invested

in annuities, corporate bonds, and stocks than CDs, money market accounts, and cash (e.g., savings accounts and money market funds).

In this study, African Americans, Asians, and whites all report an equivalent proportion of high-risk thresholds, whereas a much smaller proportion of Hispanics are willing to take high financial risks. However, the results did not reveal any discernable differences in risk tolerance level and asset ownership among the four high-income and high net worth racial/ethnic groups.

While not always the case, one's risk tolerance level may be closely related to one's investor confidence, which is discussed below.

Investor confidence

To analyze ethnic/racial differences in investor confidence, we used three indicators of investment confidence: confidence in investment ability, level of concern about investment outcomes, and confidence in investment knowledge.

In this study, Asians appear to be most confident in their ability to invest, followed by Hispanics. However, while Asians were the most confident in investment abilities, they were also more worried about the investment outcomes than any other group. The proportion of confident investors was lowest among African Americans and whites.

More Asians than any other group also indicated that they were confident in their investment knowledge. The differences in the proportions of those who indicated confidence in investment knowledge among the various ethnic/racial groups of investors were not significant, but there does seem to be a relationship between respondents' confidence in their investment knowledge and confidence in their ability to invest.

Another area that aids in determining investor confidence is that of investors' confidence in their ability to invest for the future (retirement), discussed below.

Retirement confidence

In this study, minority investors' retirement confidence was measured by three factors: their level of retirement contributions, their having clear ideas about the financial needs of retirement, and their confidence in having adequate finances during retirement.

Results show that a majority of the respondents in each group had IRA and Keogh accounts and were making maximum contributions to their employer-provided retirement accounts. However, Asians were more likely to maximize retirement contributions than investors in the other three groups (African Americans, Hispanics, and whites).

Over half of the respondents in each of the four groups felt that they were well-prepared for their retirement; they were confident that they would have adequate financial resources during the retirement period. However, when compared to other ethnic and racial groups, whites were less likely to express high confidence in their preparation for retirement.

The study's results do not reject the notion that minorities have different confidence levels, but they do suggest that racial and ethnic differences are not significant among high-income and high net worth households.

Discussion and implications

In many ways, racial and ethnic groups are more similar than different in investment epistemology and investment decision making. Findings of this study indicate the financial socialization is relatively the same amongst racial groups. However, the execution and tools used by individuals who make financial decisions and gather important information tend to differ by race.

Parents are a primary financial socialization agent for children, even though much of what is transferred from parent to child is non purposive; hence, it is vital that parents become more aware of the influence of their own family of origin on their present attitudes, standards, motives, and behaviors so that the transference of these things becomes more intentional. Our findings suggest that the delivery method chosen varies for adults according to their cultural, socioeconomic, demographic, and life-cycle characteristics. As such, adult programs may be more effective if they are tailored to reach specific audiences. This concept is discussed in two other fact sheets in this series, "Strengthening Investor Confidence of High-Income Women in America" and "Promoting Investment Involvement among High-Income Women in America," although those consider women rather than racial or ethnic minorities. However, the principles of the educational and marketing concepts addressed in each fact sheet remain the same, and are therefore relevant to minority high-income investors as well. For more information about investment behavior in America, see the fact sheets titled "Studying the Investment Behavior of High-Income Women in America," "Examining the Investment Behavior of High-Income Women in America," and "Comparing Search Strategies for Investment Information in America."

References

Hira, T. and Loibl, C. (2006). Gender differences in investment behavior.
<<http://www.nasdfoundation.org/resources.asp>>.