THE BOSTON CONSULTING GROUP

Searching for Profitable Growth

GLOBAL WEALTH 2005

BCG | REPORT

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GLOBAL WEALTH 2005

VICTOR AERNI

CHRISTIAN DE JUNIAC

ANDREW DYER

BRUCE M. HOLLEY

SEPTEMBER 2005

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E-mail: bcg-info@bcg.com
Fax: +1 617 973 1339, attention BCG/Permissions
Mail: BCG/Permissions
The Boston Consulting Group, Inc.
Exchange Place
Boston, MA 02109
USA

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Note to the Reader

The focus of this year's report is twofold: first, to present the development of global wealth markets in 2004; and second, to review key levers for growth in the wealth management business. We distinguish among three different segments of investors: *mass affluent investors,* or those with assets under management (AuM) of $100,000 to $1 million; *emerging wealthy investors,* or those with AuM of $1 million to $5 million; and *established wealthy investors,* or those with AuM of more than $5 million. For the purposes of this report, investors with AuM below $100,000 are considered *nonwealthy.*

We have based the report on three main sources. First, we built our own global market-sizing model to estimate the extent of major wealth markets by country and by wealth segment. Second, we conducted an extensive quantitative and qualitative survey of roughly 100 leading wealth managers worldwide. Third, we drew insights from wealth managers' best practices and from our in-depth project work for wealth managers and private bankers.

The results of the quantitative benchmarking of leading wealth managers will be published separately. It has become clear throughout our research that a detailed understanding of clients' needs is a critical issue for growth and retention in the industry. We are therefore planning to focus our 2006 survey on the needs and service experiences of wealth management clients. We invite interested institutions to contact us at GWR2006@bcg.com.

If you would like to discuss your wealth-management business with The Boston Consulting Group, please contact one of the following leaders of BCG's global Financial Services practice:

The Americas

Bruce M. Holley
BCG New York
+1 212 446 2800
holley.bruce@bcg.com

Jorge Becerra
BCG Miami
+1 786 497 8100
becerra.jorge@bcg.com

Willie Burnside
BCG Los Angeles
+1 213 621 2772
burnside.willie@bcg.com

John Garabedian
BCG Chicago
+1 312 993 3300
garabedian.john@bcg.com

Paul Orlander
BCG Toronto
+1 416 955 4200
orlander.paul@bcg.com

Craig Rice
BCG New York
+1 212 446 2800
rice.craig@bcg.com

Europe

Christian de Juniac
BCG London
+44 20 7753 5353
de.juniac.christian@bcg.com

Victor Aerni
BCG Zürich
+41 44 388 86 66
aerni.victor@bcg.com

Stefan Dab
BCG Brussels
+32 2 289 02 02
dab.stefan@bcg.com

Ludger Kübel-Sorger
BCG Frankfurt
+49 69 9 15 02 0
kuebel-sorger.ludger@bcg.com

Huib Kurstjens
BCG Amsterdam
+31 35 548 6800
kurstjens.huib@bcg.com

Andy Maguire
BCG London
+44 20 7753 5353
maguire.andy@bcg.com

Philippe Morel
BCG Paris
+33 1 40 17 10 10
morel.philippe@bcg.com

Asia-Pacific

Andrew Dyer
BCG Sydney
+61 2 9323 5600
dyer.andrew@bcg.com

Giles Brennand
BCG Hong Kong
+852 2506 2111
brennand.giles@bcg.com

Steven Chai
BCG Seoul
+822 399 2500
chai.steven@bcg.com

Julian Durant
BCG Bangkok
+66 2 667 3000
durant.julian@bcg.com

Roman Scott
BCG Singapore
+65 6429 2500
scott.roman@bcg.com

Janmejaya Sinha
BCG Mumbai
+91 22 2283 7451
sinha.janmejaya@bcg.com

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Victor Aerni
Vice President and Director

Christian de Juniac
Senior Vice President and Director

Andrew Dyer
Vice President and Director

Bruce M. Holley
Vice President and Director

Preface

Global wealth-management markets are in constant flux. Currently, revenues appear to be back on a steady growth track, competition is becoming more and more global, new growth markets are emerging, and the significance of offshore banking is decreasing. These trends are changing the competitive landscape and thus influencing the ways in which wealth managers can best improve their businesses and achieve profitable growth.

The Boston Consulting Group is committed to enhancing the understanding both of market dynamics and of the levers available to wealth management institutions in their battle to achieve sustainable competitive advantage. In this, the fifth edition of our Global Wealth report, we focus on four main issues.

Global Market Sizing. We cover the historic and projected level of AuM for 62 countries worldwide, including variations among wealth segments, changes in asset mix, and the resulting implications for wealth managers' revenues. We emphasize regional differences among the North American, European, Asian, and Latin American markets. We have also deepened last year's insights into the Indian and Chinese markets, and highlighted Russia as another key growth market.

Client Discovery. The product and service needs of wealth management clients have evolved significantly—and have done so independently from market dynamics. We analyze these changes and their effect on wealth management institutions.

Business Models. Market dynamics and changes in clients' needs have forced wealth managers to revisit their business models. We discuss possible changes to traditional models as they relate to serving different segments of the wealth management market.

Key Levers. Creating wealth management excellence requires the optimal use of the key levers available to wealth managers. We share insights and best practices gained from our client work in order to determine the most important levers for creating strategic and sustainable competitive advantage.

Summary of Key Findings

Global wealth is back on a solid growth path. After a period of recovery from the losses of previous years, global AuM should grow by roughly 4 percent annually, in U.S. dollar terms, from 2004 through 2009. The specific dynamics of growth, however, will change significantly over the next few years.

- Growth in North America and Europe will come mainly from established wealthy investors, whereas in emerging countries it will come from emerging wealthy investors.
- The share of equity assets globally has stabilized at around 37 percent. Investors will likely focus more on alternative investments to enhance performance.
- China, India, and Russia are currently the most attractive growth markets. Although still small, these markets offer the highest potential because their onshore investment climates are improving significantly.
- European offshore wealth will slowly decrease as international transparency and cross-border taxation of investment income continue to increase.

As markets have rebounded, investors have changed their needs and attitudes. Greater awareness of financial matters and a desire for higher returns will require wealth managers to change their traditional approach to client service.

- Clients are searching for a combination of enhanced investment performance and security. Their asset mixes are changing as conventional portfolios are combined more frequently with alternative investments.
- Increased regulatory complexity and uncertainty about pensions require integrated and long-term wealth solutions.
- Higher fees relative to investment returns have made clients more aware of getting value for their money. Clients are demanding greater transparency on pricing and more value-added services.
- Clients across all regions, being more financially aware, are demanding a higher degree of participation in investment decisions.

The changes in market dynamics and clients' needs have challenged traditional wealth-management business models.

- The trend to move onshore will increase transparency.
- Increasing client awareness and a lack of consolidation have put significant pressure on prices and margins.
- Wealth managers in mature European and North American markets need to focus on retaining clients. Substantial growth in the emerging wealthy segment will occur only in nascent Asian, Eastern European, and Latin American markets.
- The demand for alternative investment products and the introduction of tighter regulation have increased complexity and the cost of providing wealth management services.

Three core business models have emerged in the wealth management landscape.

- Global players are targeting numerous onshore and offshore locations and are building a portfolio of mature high-margin and emerging high-growth markets.
- Medium to large players are focusing on both onshore business and offshore business at home, as well as on some other foreign locations. They will have to concentrate on selected products and markets.
- Small institutions and boutiques are focusing on product and customer niches. For most of these institutions, client relationships are their key asset. Because of their insufficient scale, many will move to a distributor model with product development, operations, and IT being outsourced.

In order to be successful in a world of increasing competition—and resulting margin pressure—

wealth management institutions need to strive for excellence by optimizing all relevant growth and efficiency levers. Our experience in working with leading wealth managers reveals a need to concentrate on specific levers.

- *Pricing.* Standard banking services are under significant price pressure, and wealth management institutions are moving toward less visible pricing. Offering proactive, tailor-made advice remains a high-margin activity, and wealth managers are capitalizing on this. Internally, a lack of pricing discipline and complex discount schemes often prevent wealth management institutions from realizing optimal prices. Best-practice institutions have limited discounts.

- *Small-Client Management.* Most institutions handle clients with AuM below $250,000. These customers are often unprofitable. In order to make these accounts profitable, best-practice wealth managers have increased minimum fees or offered standard product and coverage models.

- *Retention Management.* Most wealth-management institutions experience a high rate of client attrition without understanding the true reasons for it. Best-practice institutions have implemented early warning measures and systematic client feedback to prevent the loss of clients.

- *Relationship Manager Performance.* A key to growth in the existing client base is enhanced cross-selling and up-selling. Raising the performance of relationship managers in the third, fourth, and fifth quintiles has a significant impact on growth. Some wealth-management institutions have already implemented performance programs that measure client contacts and conversions.

The most important growth levers for wealth management institutions are increasing share of wallet and retaining existing clients.

- The quality of a client's experience at a wealth management institution is the foundation of these levers. However, only a few institutions have succeeded in understanding the needs of their clients properly.

- Perfecting the client experience will thus be one of the most important issues for wealth management institutions over the next few years.

Global Market Sizing

Returning to Solid Growth

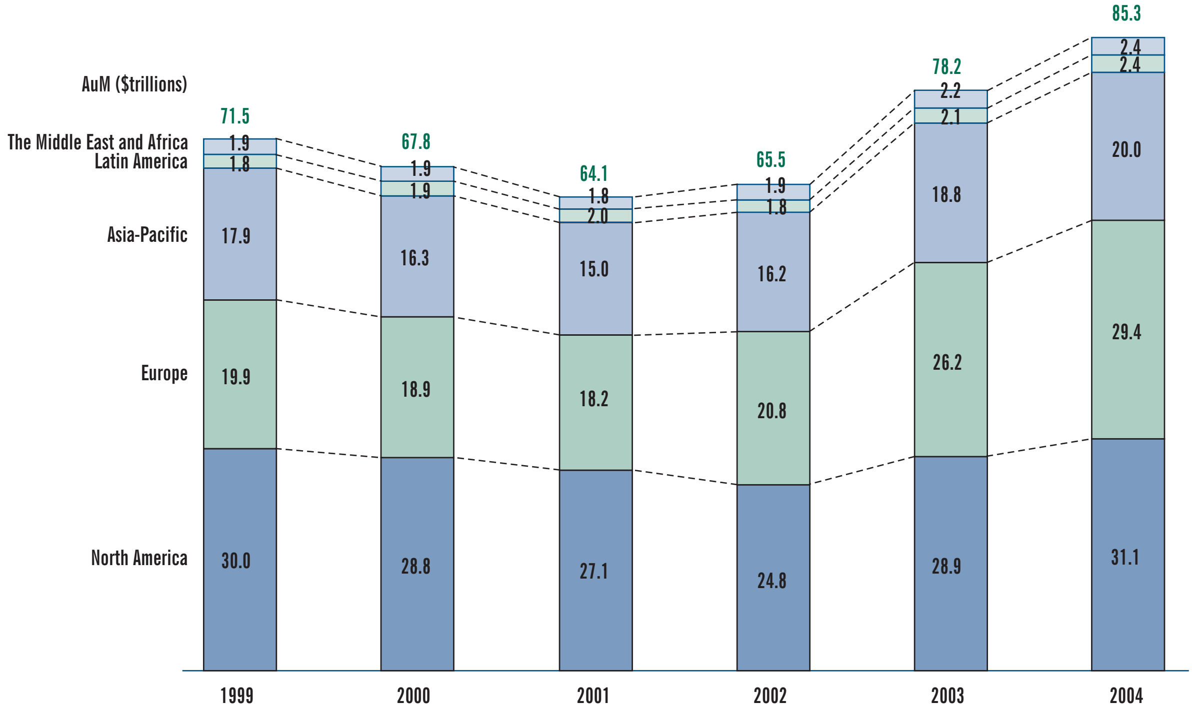
In 2004 the global wealth market grew by 9.4 percent in U.S. dollar terms and by 5.5 percent in local currency terms. (See Exhibit 1.) This represents a return to solid growth after the difficulties of 2000 through 2002 and the recovery of 2003. Latin America, Europe, and the Middle East experienced the highest growth rates in U.S. dollar terms.

Of the total global wealth market of $85.3 trillion in AuM, 7.5 percent is held offshore, primarily in European offshore centers. Europe accounts for roughly 50 percent of global offshore wealth, although this proportion is shrinking and should continue to decrease given rising levels of wealth repatriation and the current shift into property investments. The European Union Savings Tax Directive should have only a marginal impact on the offshore market since client confidentiality remains unaffected by the directive and the tax will amount to just 15 percent in 2005 (and can be partly avoided). Yet increasing international transparency means the viability of offshore business models will gradually come into question. That said, Singapore, for example, is becoming interesting as a regional offshore center because it offers favorable tax conditions—a development that has already led to some offshore wealth moving from Europe and other Asian countries to Singapore.

Between 2003 and 2004, the global asset mix remained fairly stable, with equity assets accounting

EXHIBIT 1

IN 2004 THE GLOBAL WEALTH MARKET GREW BY 9.4 PERCENT



CAGR 1999–2004 (%)	CAGR 2002–2003 (%)	CAGR 2003–2004 (%)
3.6	19.2	9.4

Source: BCG wealth market-sizing database.

Note: Because of a differing methodology in this year's report, some AuM amounts calculated for the years 1999 through 2003 may differ from those published in last year's report. Column totals and percentage changes in AuM are based on complete, not rounded, numbers.

for about 37 percent of total AuM. (See Exhibit 2.) Still, ever since equity markets began to be characterized by a higher degree of uncertainty early in the decade, investors have increasingly been looking for capital protection and alternative investment opportunities. As a result, the demand for structured products and hedge funds has grown significantly. And whereas demand for structured products should continue to rise, demand for hedge funds is likely to decline because of weakening industry performance. Another trend is that managed funds have edged up to about 34 percent of the market, reflecting a movement toward somewhat conservative investment behavior in a more complex capital-market environment.

Looking ahead, we estimate that global AuM will grow on average by roughly 4 percent annually in U.S. dollar terms, or a total of about 23 percent, from 2004 through 2009. (See Exhibit 3.) A continuing recovery in the markets and growing wealth in all investor segments (except the nonwealthy segment) will be the key drivers of growth.

Regional Differences

Because of the strong recovery of equity markets, the North American wealth-management market grew by 7.9 percent in 2004 and exceeded the AuM level of 1999. (See Exhibit 4.) In contrast to the global average, mass affluent clients are the largest North American segment, resulting in a lower concentration of overall wealth. The mass affluent segment also grew at a faster rate than other North American segments in 2004, posting a 12.1 percent increase. (See Exhibit 5.) North American investors hold

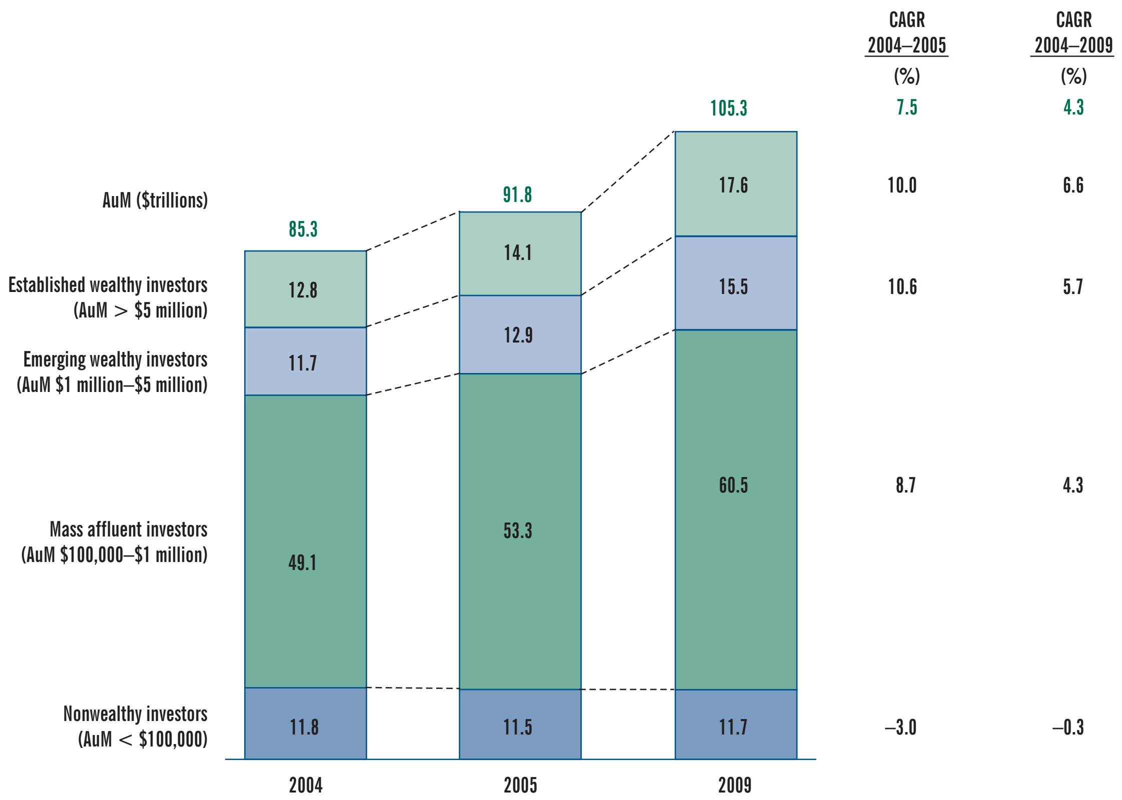
EXHIBIT 2

THE GLOBAL ASSET MIX REMAINED FAIRLY STABLE IN 2004

SOURCE: BCG wealth market-sizing database.
NOTE: Column totals and percentage changes in AuM are based on complete, not rounded, numbers. *Wealthy* is defined as households with AuM greater than $100,000.
[1]Includes hybrid funds and balanced funds.

EXHIBIT 3

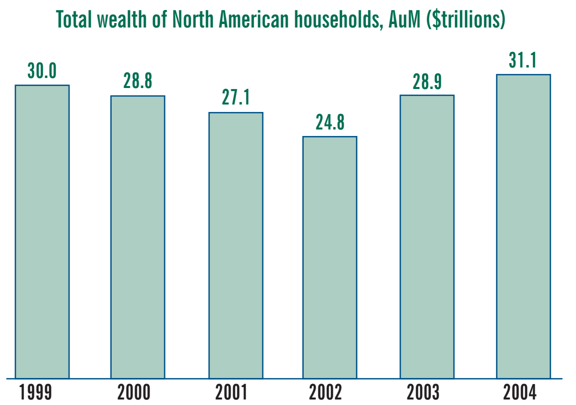
GLOBAL WEALTH IS PROJECTED TO GROW BY ABOUT 23 PERCENT FROM 2004 THROUGH 2009



Source: BCG wealth market-sizing database.
Note: Column totals and percentage changes in AuM are based on complete, not rounded, numbers.

EXHIBIT 4

THE NORTH AMERICAN WEALTH-MANAGEMENT MARKET HAS SURPASSED ITS 1999 LEVEL

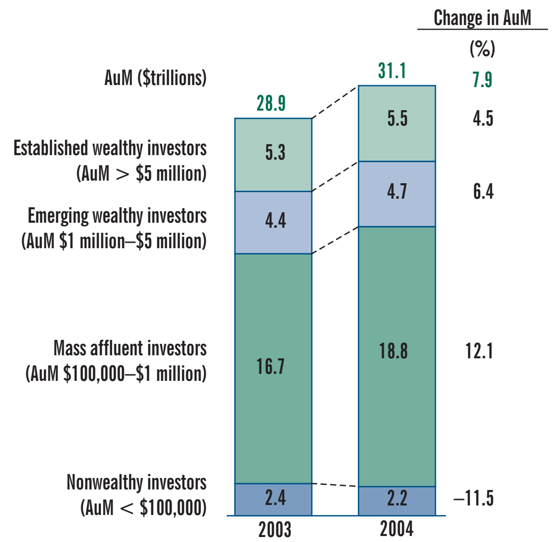


CAGR 1999–2004 (%)	CAGR 2003–2004 (%)
0.7	7.9

Source: BCG wealth market-sizing database.
Note: Column totals and percentage changes in AuM are based on complete, not rounded, numbers.

EXHIBIT 5

IN NORTH AMERICA, THE MASS AFFLUENT SEGMENT SHOWED THE STRONGEST GROWTH



Source: BCG wealth market-sizing database.
Note: Column totals and percentage changes in AuM are based on complete, not rounded, numbers.

about 50 percent of their assets in equities—a much higher share than the global average. Most of these assets are invested in managed funds. We expect the North American wealth market to grow by about 4.1 percent per year from 2004 through 2009, owing mainly to stabilizing market conditions.

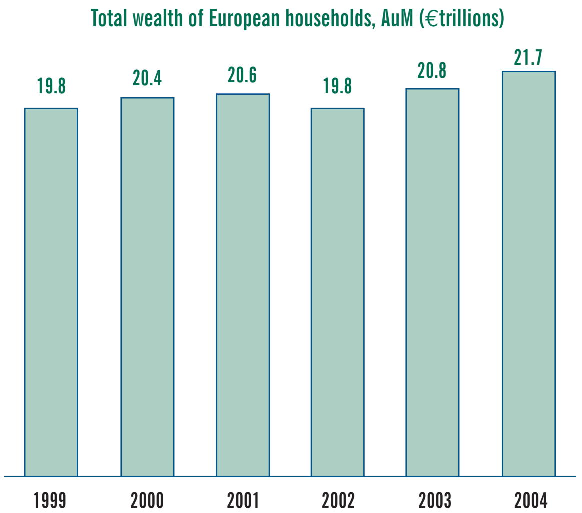
The European wealth-management market grew by 12.4 percent in U.S. dollar terms in 2004 but by only 4.7 percent in local currency terms because of the continuing devaluation of the U.S. dollar over the course of the year. (See Exhibit 6.) Central and Eastern European countries and Switzerland experienced the strongest growth, whereas the United Kingdom, Germany, France, and Italy were the largest markets in absolute terms. Europe's established-wealthy investors experienced the strongest growth, with AuM rising by 11.5 percent in 2004, whereas nonwealthy investors saw their AuM shrink by the same percentage. (See Exhibit 7.) After several years of decline, exposure to equities throughout Europe has stabilized at around 32 percent of assets, although some countries—such as the United Kingdom and Switzerland—have significantly higher shares. The majority of wealth management revenue in Europe is generated both from cash and deposits (43 percent) and from managed funds (41 percent). We expect the European wealth market to grow by about 6 percent per year in local currency terms from 2004 through 2009, with fairly equal growth across all investor segments.

In Asia, wealth markets grew by 11.8 percent in U.S. dollar terms in 2004 and by 7.3 percent in local currency terms, mainly as the result of strong expansion in South Korea, Australia, and Hong Kong. (See Exhibit 8.) China and Taiwan had the highest asset holdings in absolute terms, and wealth was extremely concentrated—with about 2 percent of households holding roughly 70 percent of the wealth. Growth was in the double digits across all investor segments except the nonwealthy segment. (See Exhibit 9.)

There was a slight shift toward more equity exposure in Asia (currently at 28 percent), driven mainly by higher equity shares in mature markets such as Australia, Hong Kong, and Taiwan. Most Asian assets are still held in cash and deposits, which are also the source of most asset-management revenue. Wealth in

EXHIBIT 6

THE EUROPEAN MARKET GREW BY NEARLY 5 PERCENT IN 2004

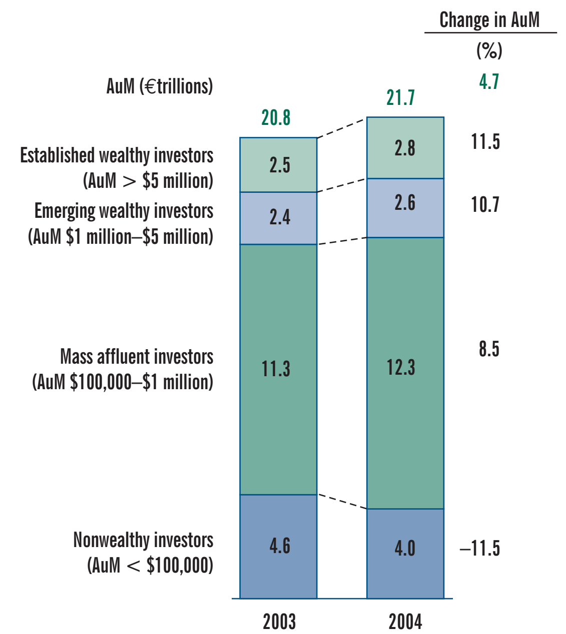


CAGR 1999–2004 (%)	CAGR 2003–2004 (%)
1.9	4.7

Source: BCG wealth market-sizing database.
Note: Column totals and percentage changes in AuM are based on complete, not rounded, numbers. At press time, U.S.$1 equaled €0.81493.

EXHIBIT 7

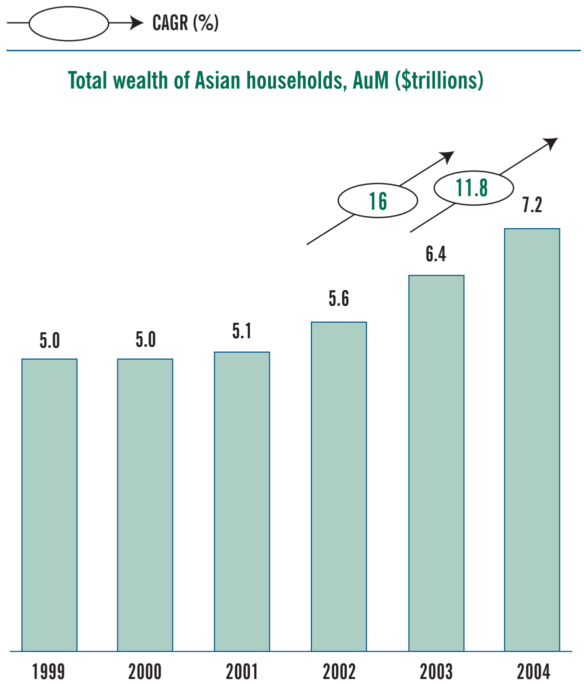
IN EUROPE, THE ESTABLISHED WEALTHY SEGMENT SHOWED THE STRONGEST GROWTH



Source: BCG wealth market-sizing database.
Note: Column totals and percentage changes in AuM are based on complete, not rounded, numbers. At press time, U.S.$1 equaled €0.81493.

EXHIBIT 8

THE ASIAN MARKET GREW BY NEARLY 12 PERCENT IN 2004, BUT GROWTH HAS SLOWED SINCE 2003



CAGR 1999–2004 (%)	CAGR 2003–2004 (%)
7.4	11.8

Source: BCG wealth market-sizing database.
Note: Column totals and percentage changes in AuM are based on complete, not rounded, numbers.

Asia is expected to grow by 6.8 percent from 2004 through 2009, with the established wealthy being the fastest-growing segment.

Latin American wealth markets experienced significant growth in 2004—14.4 percent in U.S. dollar terms and 12 percent in local currency terms—driven mostly by assets in Brazil and Chile. Brazil is by far the largest market, and wealth is as concentrated there as it is in Asia. The established wealthy segment was the largest and fastest growing in Brazil in 2004.

Moreover, although wealthy Latin Americans have historically been active offshore investors, there are notable differences among countries. Wealthy Venezuelans invest roughly 70 percent of their assets offshore, for example, whereas wealthy Chileans invest only 40 percent offshore because of Chile's more highly developed financial markets. Latin America has the lowest equity exposure—only 14 percent in 2004—with 40 percent held in cash and deposits. We estimate that Latin America's wealth-management market will grow by roughly 6 percent per year from 2004 through 2009 because less new wealth is being generated now than in the 1990s.

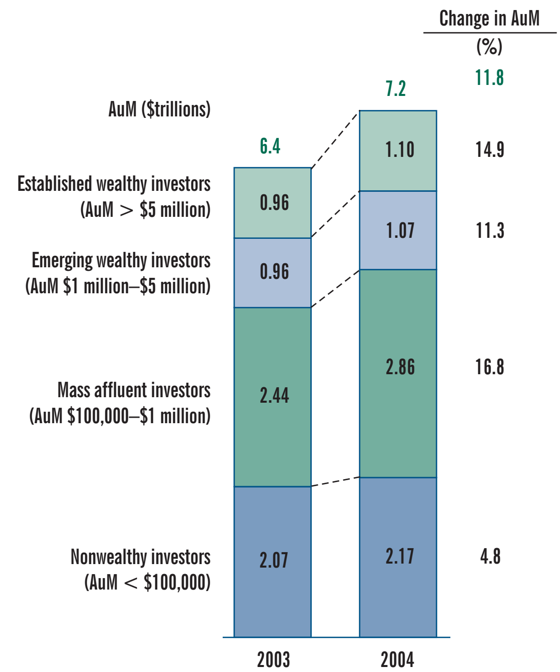
Attractive New Markets

China, India, and Russia may still be small markets, but they will represent the most attractive growth countries in the near future. International wealth-management institutions should focus on these markets in order to provide growth stories for the industry and to diversify their low-growth, high-margin portfolios.

Greater China is a significantly larger wealth market than either India or Russia, but the latter two grew more quickly in 2004. (See Exhibits 10 and 11, page 14.) Looking ahead, the expansion of wealth in Russia is expected to outstrip that in China and

EXHIBIT 9

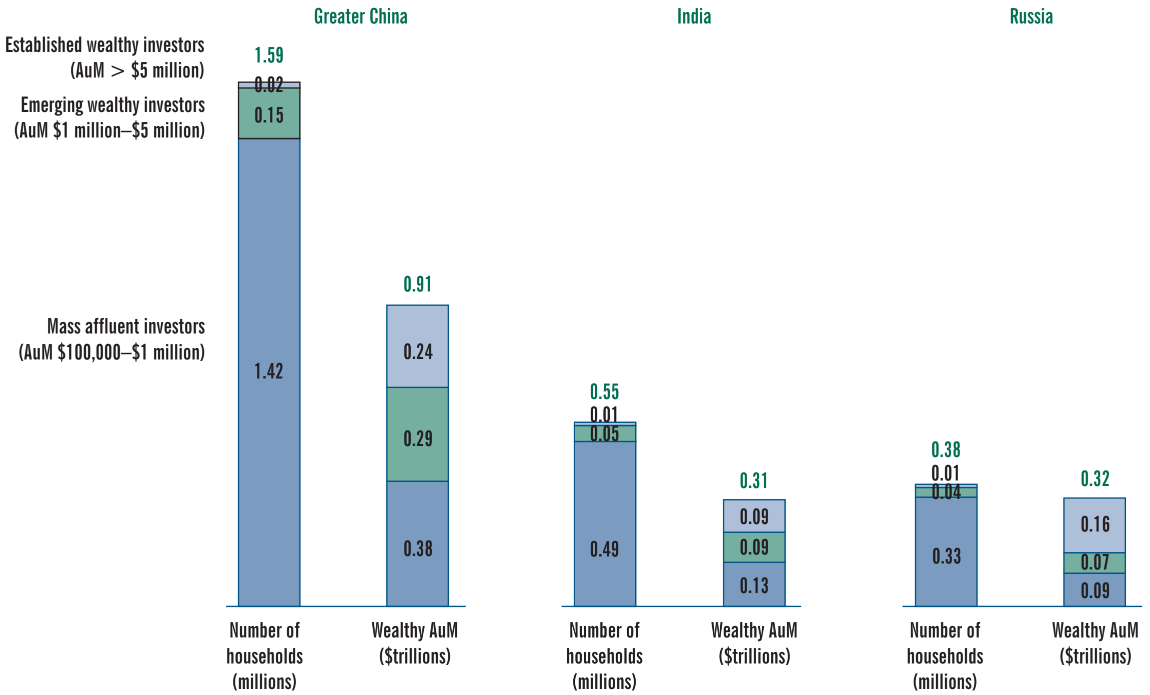
IN ASIA, THE MASS AFFLUENT AND ESTABLISHED WEALTHY SEGMENTS SHOWED THE STRONGEST GROWTH



Source: BCG wealth market-sizing database.
Note: Column totals and percentage changes in AuM are based on complete, not rounded, numbers.

EXHIBIT 10

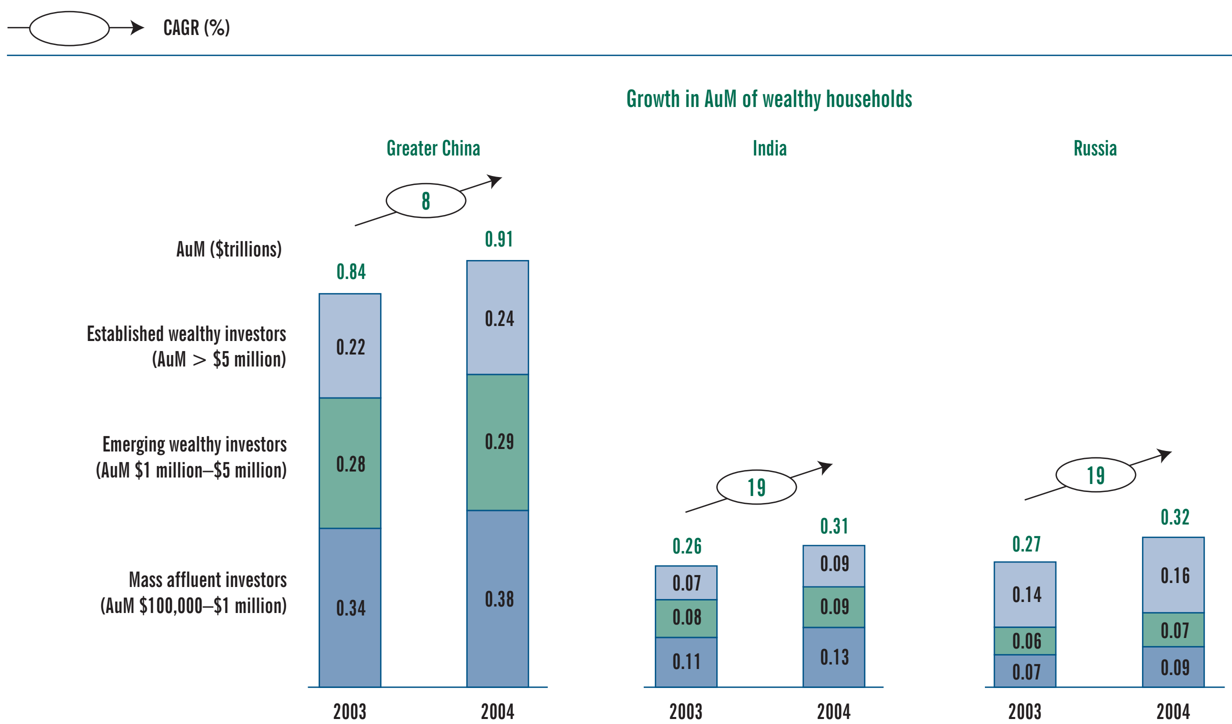
GREATER CHINA IS A SIGNIFICANTLY LARGER WEALTH MARKET THAN INDIA OR RUSSIA



Source: BCG wealth market-sizing database.
Note: Column totals and percentage changes in AuM are based on complete, not rounded, numbers. *Wealthy* is defined as households with AuM greater than $100,000.

EXHIBIT 11

THE INDIAN AND RUSSIAN WEALTH MARKETS GREW FASTER THAN THE CHINESE WEALTH MARKET IN 2004



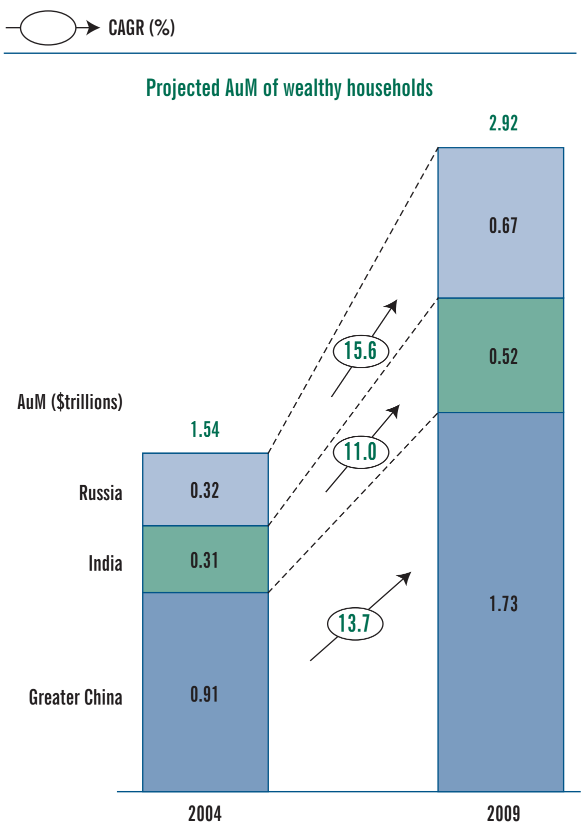
Source: BCG wealth market-sizing database.
Note: Column totals and percentage changes in AuM are based on complete, not rounded, numbers. *Wealthy* is defined as households with AuM greater than $100,000.

India. (See Exhibit 12.) In contrast to global trends, the nonwealthy segment in Russia is growing significantly. Many wealth managers are currently focusing on India and Russia, and keeping China as an option for the medium-term future. Indeed, China's huge export industry, along with many successful IPOs of Chinese companies in Hong Kong and New York, have resulted in a large number of Chinese entrepreneurs becoming wealthy. For foreign wealth managers, China will offer primarily onshore opportunities.

India may possibly offer greater potential than China because wealthy nonresident Indians, who often transfer money back into their home country, are an attractive target group. In addition, the Indian banking market will be fully liberalized by 2009. Several foreign players—such as Citigroup, Goldman Sachs, BNP Paribas, and SG Private Banking—have already established a presence in the country. They are focusing on discretionary portfolio-management services, which local players are still struggling to provide. However, competition will increase as local players broaden their wealth-management capacities.

EXHIBIT 12

THE RUSSIAN WEALTH MARKET SHOULD GROW FASTER THAN THE INDIAN AND CHINESE WEALTH MARKETS



SOURCE: BCG wealth market-sizing database.
NOTE: Column totals and percentage changes in AuM are based on complete, not rounded, numbers. *Wealthy* is defined as households with AuM greater than $100,000.

It is worth noting that a large proportion of Russian wealth is currently held offshore. Political instability, the state of the banking system, a lack of services aimed at long-term wealth preservation, and wealth transfer have compelled many wealthy Russian investors to manage their assets away from home. We believe, however, that the Russian onshore market will grow in the long term as the result of two factors: first, risk-adjusted returns are currently much higher in Russia than they are in Europe as a whole; and second, cash storage will decrease as trust in the domestic banking system gradually improves.

Global wealth managers need a separate strategy for each of these three markets. The Western approach of seeking a balanced asset framework is not applicable in these countries because the typical portfolio structure is different—with a high cash base providing security, and property playing a larger role because it offers more stable returns. For more speculative investing, expected returns are difficult to achieve with the standardized wealth-management products typically offered by global institutions today.

In order to determine an optimal strategy, wealth managers need to address the following key questions about mature markets:

- Which mature markets are the most attractive?
- Where will the highest number of wealthy households emerge in the future?
- Where will margin erosion be the highest?

They also need to address the following questions about new markets:

- How close should new markets be to our core business?
- What is required for competitive advantage in these markets?
- Which types of products and services would be most suitable?

Client Discovery

Addressing Clients' Needs and Enhancing the Client Experience

Historically, private-banking clients have sought secrecy, anonymity, and tax relief. Products have been traditional, with discretionary mandates focusing on international bonds, equities, and money market funds. But the painful experience of the market downturn early in the decade, along with ongoing generational changes, have shifted clients' needs more toward enhanced performance and security, integrated wealth solutions, sound professional advice, and active participation in investment decisions.

Enhanced Performance and Security

Following the equity market struggles that began in 2000, wealthy clients are now seeking both higher returns and a higher degree of capital protection. In particular, demand is growing for innovative structured products that offer both of these benefits. Wealth managers are eager to meet this new demand because structured products yield comparatively high margins. Demand for higher returns will increase even further if capital markets are relatively flat.

Integrated Wealth Solutions

Given the significant transfer of wealth between generations, increasing uncertainty about pensions, and regulatory complexity, wealthy investors now require integrated and life-cycle-oriented solutions. Proactive investment consulting, tailored advice based on individual clients' needs, and expertise in legal and tax matters are becoming essential. Wealth managers have begun to address these needs not only for the established wealthy but also for the mass affluent and emerging wealthy segments. Financial institutions have implemented standard processes and are using specialist know-how to ensure consistency of advice and consideration of all relevant client needs. But wealth managers must go further and focus more on clients' risk profiles and on the integration of investors' long-term financial goals into portfolio structures.

Sound Professional Advice

Current low-to-medium-level returns have made clients more aware of the quality of the counsel they receive from their wealth managers. Investors are also demanding greater transparency of products and prices, higher service levels, and direct accountability regarding investment advice—especially when returns are subpar. Wealth managers are expected to offer an open-architecture environment that includes products from external providers and to present qualified recommendations on the full spectrum of available products. Although a comprehensive in-house product range is no longer required, scrutiny of the products and investment strategies offered by wealth managers has become more meticulous than ever before.

Active Participation in Investment Decisions

Generally speaking, today's investors are far more knowledgeable and financially aware than those of previous generations. They tend to have a greater desire to participate more actively in the investment decisions made by their wealth managers. They also tend to be more price sensitive, particularly to externally visible fees such as those for account administration. As a result of this trend, the overall number of managed mandates will likely decrease. Price sensitivity is at its highest in the mass affluent and established wealthy segments (especially in portfolios valued at more than $8 million).

In order to address clients' needs in a more efficient way, wealth management institutions should consider moving away from segmenting clients solely according to their level of AuM and focus more on segmentation that reflects geography, lifestyle, product-mix usage, and risk tolerance. In our view, in order to become more client focused, wealth managers need to address the following key questions:

- How can clients' needs be systematically identified?
- How can clients' needs be better integrated into the advice process?
- How can increasingly complex demands be met with third-party solutions?
- How can wealth managers react to the continuing convergence of onshore and offshore needs?

Business Models

Finding the Right Focus

Trends in the global wealth-management market and changes in clients' needs have challenged traditional wealth-management business models. For example, the decline in offshore volumes will increase onshore competition and transparency with regard to fees. Yet offshore accounts tend to have higher returns. Wealth management institutions will therefore need to find ways to improve overall investment performance in order to compensate clients for generally lower onshore returns.

Many institutions have recently reviewed their pricing practices. This has largely been a reaction to increased pricing pressure—particularly on standard banking fees—as clients have demanded a greater degree of price transparency. Wealth managers have thus shifted loads from highly visible areas, such as administration fees, to less visible areas, such as structured-product margins or in-house funds. Given that a large number of financial institutions are eager to grow in wealth management markets, pricing pressure is certain to intensify.

Wealth managers will also likely struggle with the increasing complexity of the business and, hence, the cost of providing services. The demand for alternative products will raise product development costs, and new regulations such as the European Union Savings Tax Directive will significantly increase the burden on operations.

In our view, wealth managers in mature markets should focus on client retention because the rich are becoming richer in these regions. By contrast, in such emerging markets as Asia, Eastern Europe, and Latin America, wealth managers need to pay attention primarily to emerging wealthy investors.

These competitive trends have given rise to three basic types of players within the international wealth market: global players, medium to large players, and small players.

Global Players

UBS, Citigroup, HSBC, and Credit Suisse are leading the race for global presence in wealth management. All of these institutions target multiple onshore and offshore markets, mostly through a combination of high-margin mature home territories and selected high-growth regions such as Europe (onshore) and Asia. In high-growth markets, these banks are concentrating on cherry-picking attractive private and corporate clients that currently are not adequately served by domestic institutions.

Generally speaking, global players are pursuing two strategic thrusts: excellence in their home markets and leading positions in attractive overseas markets. At home, they are leaders in fulfilling clients' needs based on a standardized advisory process. Typically, this approach leads to high client retention. In foreign growth markets, they focus on achieving leading positions either through acquisitions or through fast organic growth. UBS, for example, is the largest player for servicing ultrarich families in Germany and has built a leading Asian offshore presence. However, many global players entering foreign markets are currently struggling to adapt their advisory processes to varying cultural needs.

Medium to Large Players

Medium to large players focus on both onshore business and offshore business in their home markets and have a selected geographic presence elsewhere. Examples include BNP Paribas, Société Générale, and Deutsche Bank. These institutions offer onshore wealth-management services in countries where they have a retail-banking presence.

Such institutions benefit from actively managing referrals within the institution and from leveraging their integrated business models. Indeed, most universal banks have retail-, corporate-, and investment-banking divisions in addition to their wealth-management division. Identifying potential clients in their retail base and leveraging untapped potential from corporate- or investment-banking transactions are key growth levers for these banks.

It is worth noting that medium-size wealth-management institutions are in a difficult position.

They do not have the resources to compete with global players such as UBS or HSBC, yet they are too large to focus solely on certain product or customer niches. Consequently, they face severe competition from such new entrants as family offices, hedge funds, and other specialist providers. Finding the right business-model focus, therefore, remains a key challenge for medium-size institutions.

Small Players

Small wealth-management institutions tend to focus on product and customer niches, sometimes combined with a selected international presence. One example is Wegelin & Co., a Swiss boutique specializing in structured products. Increased scale is likely to put pressure on such small players because they will face higher costs, especially for compliance. For example, implementation of the European Union Savings Tax Directive has created an average cost burden of two to three basis points for each individual institution. Our work with wealth managers indicates that in the future smaller institutions are likely to move to a distributor model, concentrating on improving the quality of interactions with customers and creating a detailed understanding of clients' needs.

In order to focus their business models on the right levers and markets, wealth management institutions need to ask themselves the following questions:

- Should we concentrate on onshore and/or offshore business?
- Which products should we offer?
- Which segments should be our primary targets?
- Which are the most attractive markets, given our particular resources and expertise?

Key Levers

Achieving Wealth Management Excellence

In the current low-growth, highly competitive environment, wealth management institutions need to concentrate on operational excellence. Key overall levers include significantly improving revenue generation from both existing and new clients, and tightening cost management. Each of these broad initiatives has several individual sublevers. (See Exhibit 13.)

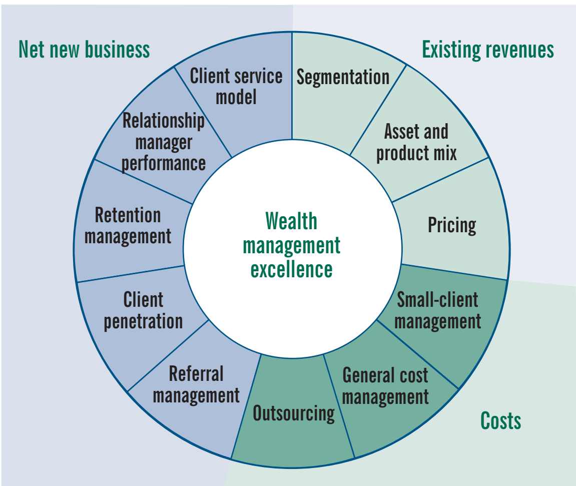
Overall Levers

With regard to enhancing revenue from existing clients, wealth managers need to resolve the conflict between performance and revenue. In other words, although pushing in-house products can maximize revenue, such products often do not generate the highest performance compared with the wide range of products available in the marketplace. In the future, institutions will be forced to focus primarily on performance in order to satisfy this ever-increasing client need. They can generally improve revenue by offering both products that are customized for certain client segments and innovative pricing.

Increasing net new assets must also be a priority. Sustainable net-new-asset growth requires both high retention levels among existing clients and selective growth in new clients. To enhance retention, leading wealth managers are increasingly monitoring client satisfaction and building stronger relationships by selling clients a broader range of products. For new-client acquisition, wealth managers are focusing heavily on referrals. In Europe, for example, approximately 75 percent of wealth management clients are obtained through referrals from existing clients. Our survey indicates that retention management and relationship manager productivity are currently regarded as two of the most important levers for achieving stable growth.

EXHIBIT 13

THERE ARE MANY FACETS OF WEALTH MANAGEMENT EXCELLENCE



SOURCE: BCG analysis.

In order to improve cost efficiency, institutions have focused mainly on general cost management. However, there is significant additional potential for cost reduction in operations, IT, and product outsourcing. Small institutions, in particular, need to consider outsourcing solutions because they lack the scale to comply with increasing investment requirements and complexity.

Over the past few years, wealth managers have focused mainly on improving only selected efficiency and growth levers. Yet our survey shows that over the next few years, financial institutions will have to go much further—particularly in terms of optimizing the following specific sublevers for wealth management excellence—if they are to achieve growth and margin stability.

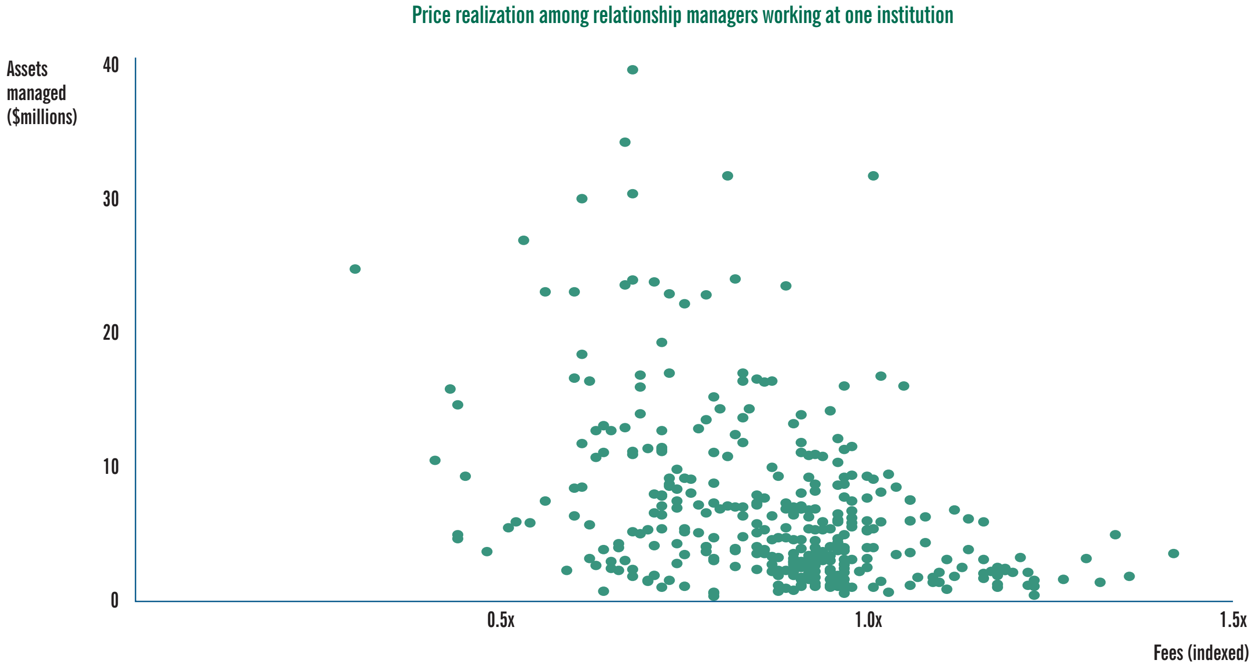
Pricing

Our survey of leading wealth managers reveals that pricing is widely considered to be one of the most important levers for further revenue optimization—and one whose potential has gone largely untapped. Indeed, a 1 percent improvement in price realization typically leads to a 7.7 percent improvement in return on equity. Yet our survey indicates that price realization varies greatly among relationship managers—even within the same wealth-management institution. (See Exhibit 14, page 20.)

The principal reasons for price leakage are an overall lack of discipline and costly discount schemes because relationship managers tend to sell on price, rather than on value, and discounts are not

EXHIBIT 14

A LACK OF PRICING DISCIPLINE HURTS WEALTH MANAGERS



Source: Wealth manager example.

always tied to compensation. What is more, discounts often appear illogical because smaller accounts are typically granted the highest discounts. A clear value proposition is therefore critical for avoiding discount pressure. Moreover, most discount schemes are extremely complicated and difficult to manage. Limited discount classes would ease the management of such schemes considerably. Our survey of wealth managers shows that fees for standard banking services—especially the most visible charges—will likely decrease, whereas individualized, proactive advisory services with custom-made solutions will maintain their high margins.

Best-practice institutions have optimized pricing at both a strategic and a tactical level. At a strategic level, these institutions have repositioned their pricing models according to changes in the competitive landscape. At a tactical level, they have managed to increase price realization throughout all wealth levels. They have also aligned compensation with pricing strategies, set clear expectations for pricing norms, and limited discounts to 5 percent.

When considering pricing optimization, wealth management institutions need to address the following key questions:

- Are all discounts monitored and reported?
- What is the value of our products to different customer segments?
- Are both visible and less visible prices competitive in the marketplace?
- Does our institution have a good understanding of the fixed and variable costs involved in the sales and delivery of services?

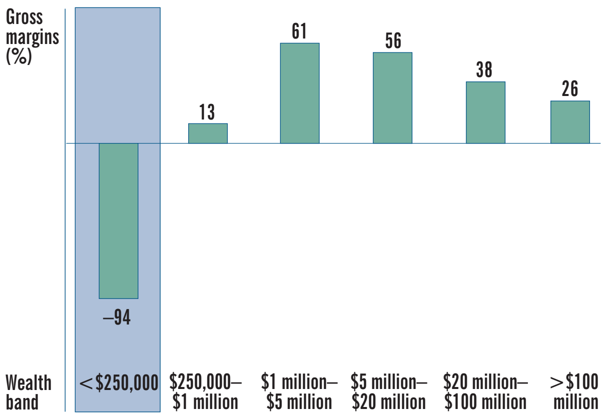
Small-Client Management

The majority of wealth managers have a large number of small mass-affluent accounts that are charged less than the stated minimum fees. Consequently, many small-client accounts tend to lose money for the institution. (See Exhibit 15.)

But some best-practice wealth managers have energized small-client accounts and made them profitable. Some institutions have accomplished this by asking small clients to bring more assets to the table or face being transferred to the retail division. Others have streamlined their business models with call center support, standardized asset-allocation products, and higher minimum account fees—or by having

EXHIBIT 15

SMALL-CLIENT ACCOUNTS TEND TO DELIVER NEGATIVE MARGINS



SOURCE: Wealth manager example.

junior relationship managers service approximately 800 to 1,000 small clients. Moving small clients to standardized solutions has proved to be the most efficient way of raising profitability. (See Exhibit 16.)

In order to improve small-client profitability, wealth managers should address the following questions:

- How can our cost base be reduced without losing the client segment?
- What are the key drivers for smooth client transfer?

Retention Management

In times such as these, when growth is slow and competition is intensifying, retention is crucial for protecting the existing client base. Many wealth-management institutions have implemented the systematic registration and analysis of complaints, although this step is often taken too late to retain dissatisfied clients. In addition, win-back programs are usually extremely expensive.

Clients generally leave, logically enough, because they feel their overall needs are not being adequately considered and believe that the institution's investment performance is unsatisfactory. (See Exhibit 17, page 22.) However, looming client dissatisfaction can be foreseen early if investment performance is weak—particularly with discretionary mandates—or if the account shows low transaction volumes and increasing asset outflows. Proactive relationship management and early warning programs are key instruments for retaining clients that may be at risk. Such programs—in which the performance of client accounts is regularly monitored according to risk profiles—have proved to be very effective.

In order to increase retention, wealth managers should address three basic questions:

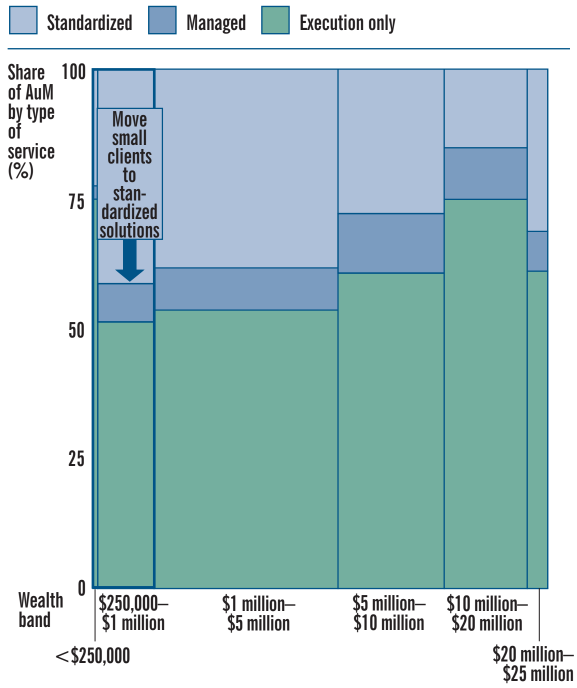
- What are the true reasons for client attrition?
- What are the most effective measures for increasing client retention?
- How can relationship managers get to know their clients better?

Relationship Manager Performance

To date, many initiatives to improve overall performance in wealth management have been back-office oriented—in other words, focused on operations and IT. However, numerous players are turning their attention increasingly to the front office. According to our survey of leading wealth managers, the performance of relationship managers has become a princi-

EXHIBIT 16

MOVING SMALL CLIENTS TO STANDARDIZED SOLUTIONS IMPROVES MARGINS



SOURCE: Wealth manager example.

pal organic growth lever, and competition for high-quality relationship managers has risen dramatically.

The main differentiators among relationship managers are the product mix they offer clients and their level of price realization and asset loading. Asset loading, in particular, is a primary driver of sales force performance. Relationship managers in the top quintile manage ten times the AuM and generate ten times more revenue than those in the lowest quintile. It is therefore critical to raise the average asset loading of relationship managers who languish in the bottom three quintiles up to the level of those in the second quintile.

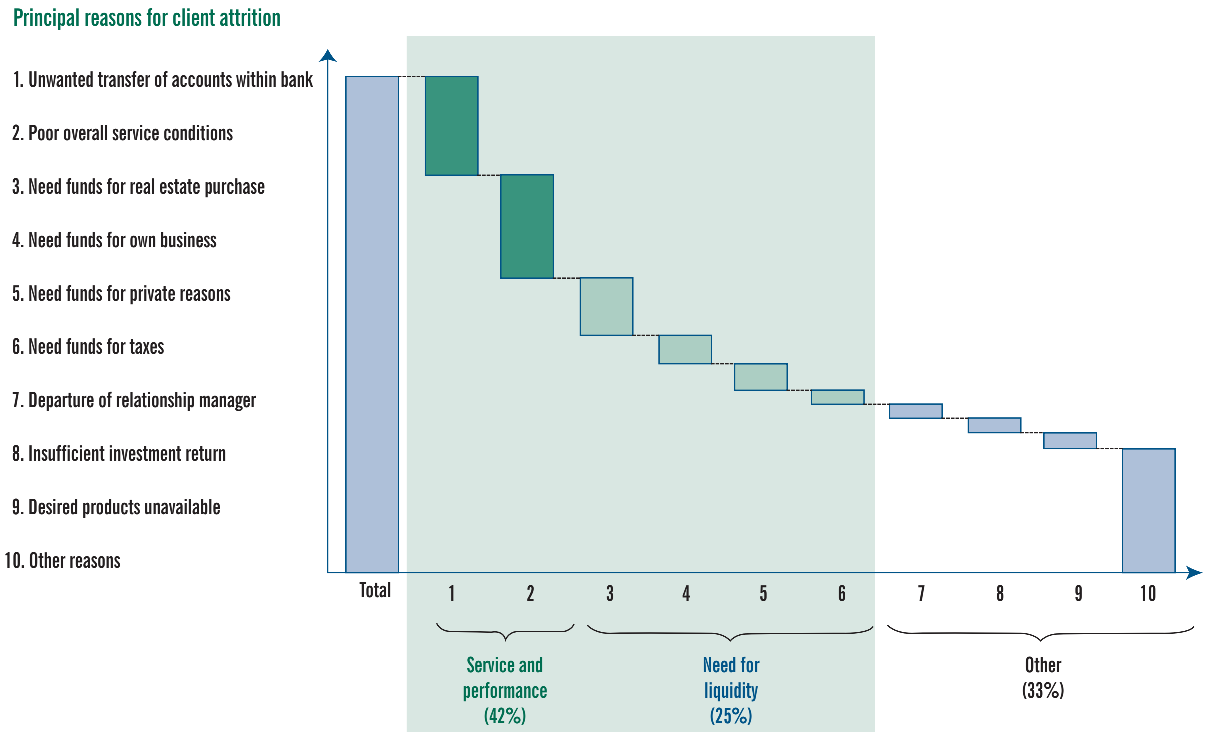
Best-practice wealth managers focus on achieving sales and creating action plans for clients. But in order to guide relationship managers more effectively, institutions need to monitor a broader range of key performance indicators (KPIs) than just net new assets and revenues. Successful institutions tend to focus on additional indicators, such as the number of new contacts, client conversions, and products per client—thereby exposing performance differences among relationship managers. In particular, wealth managers need to analyze net-new-asset performance in a different way, because the highest net producers are not always the best at retaining clients. For client planning, relationship managers need to focus on increasing their penetration of average clients and on systematically selecting and prioritizing target clients so they can then develop and monitor specific action plans. Our survey shows that asset gathering and performance can also be boosted by sharing best practices and by splitting sales forces into "hunters" and "farmers."

Improvement in the performance of relationship managers leads to a significant increase in the penetration of the existing client base. In order to achieve this, wealth management institutions need to address the following questions:

- What are the right KPIs for sales force effectiveness?
- How should teams and relationship manager portfolios be structured to achieve higher performance?
- Which relationship managers should be targeted for performance improvement?

EXHIBIT 17

CLIENTS LEAVE IF THEY FEEL NEGLECTED OR IF INVESTMENT PERFORMANCE IS UNSATISFACTORY



SOURCE: Wealth manager example.

Perfecting the Client Experience

As we have discussed, success in increasing revenues from existing clients and achieving net-new-revenue growth from new clients relies on a detailed understanding of clients' expectations and needs. Addressing these needs more efficiently increases both the retention of existing clients and the gaining of new business.

Although our survey has indicated that some leading wealth managers have focused on addressing clients' needs through a standardized advisory process—thereby ensuring that those needs are dealt with in a systematic way—we have also observed that standardized processes are not enough for institutions to fully understand the range of products and services that wealthy investors want in today's market environment. This is one reason why financial intermediaries are proliferating. Clients that desire integrated and customized solutions use these individuals and institutions as ambassadors vis-à-vis the banks.

In the future, wealth managers will be forced to deepen their understanding of clients' expectations and needs even further. As a result, entire business models may have to be redesigned. Client-focused behavior, which starts with the relationship manager, must be integrated into products and services throughout the whole institution. In order to accomplish this, a systematic approach to assessing and tracking client feedback and satisfaction is required.

Client satisfaction data are currently gathered mainly through relationship managers—and very often only after the client has left. Wealth managers should now make it a high priority to examine the whys and wherefores of client behavior more aggressively. Our benchmarking shows that some institutions have already started to survey clients extensively—a meaningful step that more institutions should take.

As we look ahead to the second half of the decade, it is our view that understanding and optimizing the total client experience will be at a greater premium than ever before in the wealth management marketplace. Those institutions that execute these initiatives the best will be the most advantageously positioned to gain and maintain competitive advantage.

Appendix: Market-Sizing Methodology

We define *wealth* as assets under management (AuM), which includes the net of listed securities, held either directly or indirectly through managed funds, and cash deposits, including life and pension assets. This is the measure of the assets that a typical wealth-management provider can most directly monetize.

We calculated 2004 AuM for larger countries through a review of national accounts and other public records. For smaller countries, we calculated AuM as a proportion of GDP, adjusted for country-specific economic factors.[1]

We then distributed total wealth within each country on the basis of Lorenz curves. These curves were based on a combination of wealth distribution statistics for countries that had available data. For countries without such data, we made estimates on the basis of the wealth distribution patterns of countries with similar income distributions (Gini coefficients) compiled by the World Bank. We further refined wealth distribution using other public sources and BCG proprietary information.

We then used available national statistics to identify different holding patterns for different countries and wealth segments. When such data could not be obtained, we assumed that countries with similar cultures and regulatory environments would have similar asset-holding patterns.

We calculated market movements as the weighted-average capital performance of asset classes held by households in each country, factoring in both domestic and overseas equity and bond holdings.

1. Whenever possible, we used national accounts for past years as well. This approach contrasts with the methodology used in *The Rich Return to Richer Returns: Global Wealth 2004,* where we projected into the past based on market performance estimates. For this reason, some AuM amounts calculated for 1999 through 2003 may differ from those published in last year's report.

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