

Taking the Client's Perspective

Global Wealth 2006



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Note to the Reader

The focus of this year's Global Wealth report is twofold: to analyze the development of global wealth markets in 2005 and to discuss the findings from an in-depth analysis of clients' wealth-management needs and investment behaviors. The report is based on three sources. First, we used our own model to estimate the size and growth of major wealth markets around the world. Second, we conducted a client discovery of wealthy investors. This technique uses interviews and analysis to generate insights into client behavior, which can be leveraged to shape strategies and offerings around specific needs and expectations. Third, we drew additional insights from our experience with wealth managers and private banks around the world.

Our client discovery was based on 150 interviews with investors who had assets under management (AuM) of more than \$1 million. (AuM includes listed securities held directly or indirectly through managed investments; cash deposits; money market funds; and onshore and offshore assets. It excludes wealth attributed to investors' own businesses, residences, or luxury goods.) Of the interviewees, 42 percent had AuM between \$1 million and \$5 million, 33 percent had AuM between \$5 million and \$20 million, 12 percent had AuM between \$20 million and \$50 million, and 13 percent had AuM of more than \$50 million. The interviews took place during the first half of 2006 with clients from more than 15 countries.

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Preface

This is the sixth edition of our Global Wealth report. For the most part, previous reports were based on extensive economic benchmarking of leading wealth managers. Last year's report, for example, drew insights from a survey of roughly 100 wealth managers around the world. This year's report focuses on the other side of the wealth management coin: the client.

We believe that success in wealth management depends on a detailed understanding of the client and that optimizing the total client experience—in particular, designing a strategy and an offering on the basis of specific client needs—is a prerequisite for sustained growth. With these imperatives in mind, we set out to understand how investors approach wealth management. Our objective was to identify common needs and expectations, as well as different styles of investing, among wealthy clients.

By taking the wealthy client's perspective, this report provides a basis for private banks and wealth managers to leverage their most valuable asset: the client relationship. Our report focuses on four main topics:

Global Market Sizing. We present historical and projected levels of AuM from 62 countries, representing 96.7 percent of the world's total GDP. Our analysis covers variations in AuM across regions and asset types. It also explores the growth of wealth in the world's most-talked-about emerging markets: Brazil, Russia, India, and China—the so-called BRIC countries.

Millionaire Market Sizing. The report zeroes in on wealth managers' core constituency: clients with more than \$1 million in AuM.

Client Discovery. We drew insights from our interviews with wealthy individuals and families, identifying distinct patterns in how they invest and trade, as well as the factors behind regional differences in investing behavior. We also provide a detailed look at ultra-high-net-worth investors—those with more than \$50 million in AuM.

The Wealth Manager's Perspective. We describe how wealth managers can incorporate a deeper understanding of the client into their strategies, offerings, and plans for growth.

Summary of Key Findings

Global wealth grew by 8 percent in 2005, measured in local currencies.¹ This growth, an improvement over the 6.2 percent increase in 2004, propelled global wealth to a total of \$88.3 trillion. Wealth increased across all regions but at widely varying rates.

- In general, growth in AuM was driven by strong stock markets and was supported by an increasing share of equity in investment portfolios.
- The two wealthiest regions, North America (the United States and Canada) and Europe, were at the extreme ends of AuM growth. North America had the lowest growth, at 4.1 percent, but remained the largest wealth market, with AuM totaling \$33.2 trillion. Europe had the highest growth in AuM, at 13.2 percent, driven mainly by strong stock performances; its AuM totaled \$29.2 trillion.
- Asia-Pacific (excluding Japan) had the second-highest growth in AuM, at 9.7 percent. Growth was led by India (15.9 percent) and China (14.8 percent). Japan's wealth market grew by 5.1 percent—the first solid growth in several years.
- AuM grew by 8.3 percent in the Middle East and Africa, owing mainly to the increasing price of oil and booming investment in infrastructure. AuM grew by 6.7 percent in Latin America (South America, Central America, and Mexico).
- In the BRIC countries, wealth grew at above-average rates. All four countries now rank among the 20 largest wealth markets. China is seventh in total AuM, Brazil is fourteenth, India is nineteenth, and Russia is twentieth.

Worldwide, the number of millionaire households (those with more than \$1 million in AuM), measured in U.S. dollars, reached 7.2 million in 2005. They owned 28.6 percent of global wealth.

- Nearly 41 percent of all millionaire households—almost 3 million—were in the United States. Japan had the second-largest number of such

households—825,000—followed by the United Kingdom, Germany, and France. China, in sixth place, had 250,000 millionaire households.

- The United States claimed most of the cities with large populations of millionaires. The metropolitan area of New York City had the highest number of millionaire households—nearly half a million—followed by Tokyo and Los Angeles. London, including its suburbs, had the largest population of millionaires in Europe but less than half as many as New York City.

An investor's general approach to wealth management provides valuable clues for understanding his or her needs and expectations. Three distinct approaches emerged from our interviews:

- *Self-directors* play an active role in managing their assets. They make all key decisions, relying on the bank and the relationship manager (RM) mostly for execution.
- *Participators* seek investment advice from, and interact frequently with, their RM before deciding how to allocate their assets.
- *Delegators* give their wealth manager wide discretion over their accounts, within defined guidelines. The portfolio's performance is especially important for these investors.

In addition to their overall approach to investing, wealthy clients can be distinguished by their disposition toward risk and trading.

- From a risk perspective, there are two types of wealthy clients: *Wealth accumulators* focus on growing wealth. *Wealth preservers* look to maintain wealth but will target moderate growth if it entails low risk.
- There are two types of trading styles: *Strategists* have a long-term perspective on investing, which leads to less trading activity. *Opportunists* are driven by short-term market developments and have a higher volume of trades.

1. Unless stated otherwise, all growth rates in AuM are measured in local currencies in order to exclude the effects of currency movements.

We have identified seven investment traits common to most wealthy clients in most regions, irrespective of their overall approach to investing.

- Wealthy clients tend to be relatively well versed in financial matters. The Internet helps them stay knowledgeable and involved.
- Most have multiple banking relationships—often to diversify risk but also to tap into a wide range of ideas or specialized services.
- When selecting a financial institution, wealthy clients are guided primarily by referrals or tradition; few conduct an objective search.
- Wealthy clients are very loyal to their private banks or RMs. When they do make a change, it is often to follow their RM to another bank. However, disappointing service or performance can also prompt them to shift AuM among wealth managers.
- Wealthy clients do not see wealth managers as primary providers of additional services, such as legal or tax advice, but they use them to establish trusts and foundations.
- Wealthy clients who are entrepreneurs keep their business and private-banking interests separate, using different banking relationships for each.
- Wealthy clients are generally sensitive to price and will negotiate rates with their banks. Many are concerned about the fairness of pricing rather than the absolute level of fees and charges, and prefer performance-based pricing.

Three factors give rise to regional differences in the investment needs and behaviors of wealthy clients.

- More sophisticated wealth-management markets are associated with greater demand for such services as online banking and with increased price sensitivity, especially for onshore investments.
- Cultural differences can lead to distinct investment behaviors. For example, wealthy clients—especially entrepreneurs—in Asia-Pacific are likely to have a higher tolerance for risk than similar investors in other regions.

- Political, fiscal, and regulatory environments can affect the risk disposition of investors and influence decisions to seek offshore investments.

We also observed important differences in investing behavior among ultra-high-net-worth investors—those with more than \$50 million in AuM.

- The needs of such investors are more complicated because of, among other factors, their international perspective and the complexity of their wealth, which often involves multigenerational family interests.
- Most ultra-high-net-worth investors have adopted a more professional approach to wealth management, usually relying on a small proprietary family office to provide objective advice and comprehensive services.
- They often focus on selecting an asset manager rather than looking for specific investment opportunities and tend to have a greater number of managed accounts than less wealthy clients do.
- Ultra-high-net-worth investors have a larger number of banking relationships and more diverse investment portfolios. In addition, their bargaining power allows them to realize better prices.

Before they build an offering around client needs and behaviors, wealth managers must define a client strategy.

- Because only a few global players can cover the whole spectrum of client needs, private banks must understand what types of clients they have—self-directors, participators, or delegators—and decide what types of clients they want to focus on.
- As part of their client strategy, they should decide how to serve ultra-high-net-worth investors—by focusing on asset management, for example, or by providing comprehensive family-office services.

Client discovery should play an equally important role when wealth managers design a client offering.

- Wealth managers will need to set the right ratio and team structure of RMs for different client types and ensure that the client's characteristics drive the relationship. For example, a self-director will want an RM to focus on execution,

whereas a participator will need an RM to develop an investment strategy and provide proactive, customized advice.

- To build trust, loyalty, and credibility, a wealth manager should complement its offering with third-party products, when appropriate.
- Given the sophistication of wealthy clients, as well as their price sensitivity, wealth managers should offer performance- or service-based pricing models and evaluate pricing options that are more customized.
- Additional services should be offered for specific types of clients. Self-directors, for example, will expect access to comprehensive research and state-of-the-art online functionality.
- Performance reporting is an important part of the offering, as well as an opportunity to improve service, because most wealthy clients want a simpler overview of fees and performance.
- The offering as a whole should reflect the sophistication of the local market, cultural differences, and the political, fiscal, and regulatory environments.

Client discovery also provides valuable lessons for wealth managers that plan for growth.

- Because wealthy clients tend to have multiple banking relationships, wealth managers will need to work hard to win a greater share of wallet. They should continue refining their understanding of their clients and adjusting their offering to meet the most important needs, thereby ensuring that they get the most active and profitable business.
- Given the strong loyalty of wealthy investors, wealth managers should focus on a long-term approach to developing relationships with prospective clients before their competitors target them—for example, by pursuing younger high-potential investors, such as the children or grandchildren of current clients.
- Wealth managers should explore opportunities in markets with the potential for high growth not only in overall wealth but also in the amount of AuM being channeled into private banks. In Asia-Pacific, for example, AuM is pouring into the private-banking system at a much faster rate than the overall growth in AuM in the region, as clients become more sophisticated and gain trust in private banks. Wealth managers may also want to focus on cities with large populations of millionaires, especially when looking for a foothold in BRIC countries.