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Banks

Industry  
**Global Wealth  
Managers**

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**Special Report**

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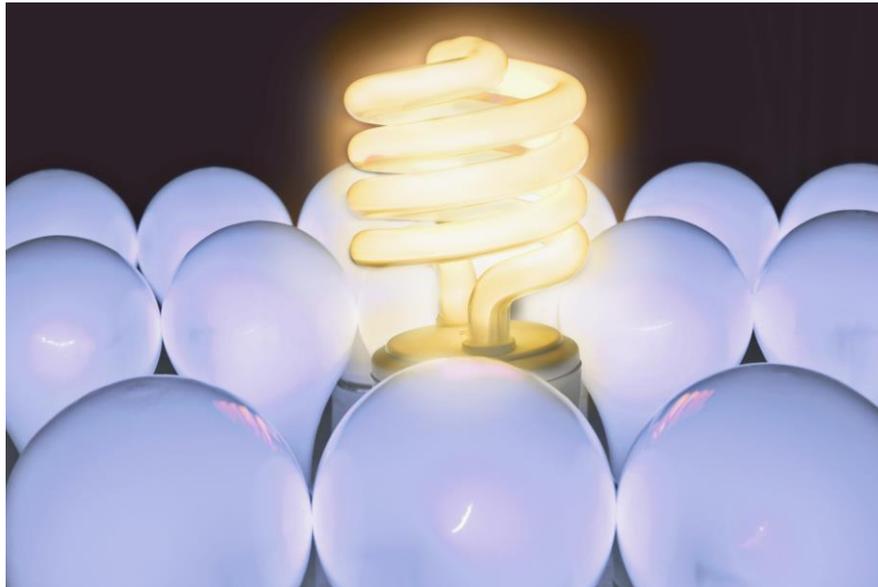
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## Dare to be different

In 2017, Wealth Managers capitalised on strong wealth creation to drive positive operating jaws. But structural headwinds remain: we expect investment returns to be weaker, asset growth to slow, fee pressures to persist and costs to rise. The business remains highly cyclical and concerns are rising in the face of an extended bull market. Wealth managers should pull both tactical and strategic levers to address these challenges and must 'dare to be different'.

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# Messages for the C-suite

Wealth Managers showed strong results in 2017 with global financial wealth growing by 7%, but tail risks continued to grow. Net interest income tailwinds from recent USD rate hikes provided some relief, but fee pressure remains high. Costs must remain a top priority, with the industry continuing to face weak operating jaws and profitability remaining highly sensitive to top-line performance.

In contrast to what we hear from many industry executives, we believe that efforts to diversify revenue streams over the past decade will not provide sufficient protection against revenue declines in the next market downturn. The ability to sustain high levels of mandate penetration during a market downturn will be the single most important driver distinguishing leaders from the rest of the pack.

The valuation gap between Wealth Managers and other bank businesses has narrowed. Wealth Managers must act now to preserve their superior valuations by taking a hard look at their business models. The traditional 'broad waterfront' approach looks increasingly untenable for most.

## Priorities for the C-Suite

### Focus on key competencies

Differentiated value propositions and business models achieve up to double pre-tax margins – Wealth Managers need to sharpen their pencils. What to do:

- Stand out through a differentiated and well-articulated value proposition by focusing on key competencies, e.g., by re-evaluating the physical footprint, re-focusing the delivery model, and / or streamlining the (in-house) product shelf
- Prepare to face off disruptive competitors, e.g., brokers for investment services, by considering own aggregator / platform models or working closely with them as part of a broader Wealth Management ecosystem

### Embrace data analytics to unlock revenue upside of up to 20%

Data analytics has not yet lived up to its potential – Wealth Managers need to overcome challenges to realise the full revenue opportunity. What to do:

- Build the foundation for advanced analytics by enhancing data governance and quality controls; avoid costly re-platforming exercises and instead leverage readily available data aggregation software
- Embrace third-party solutions to close the capability gap; integrating third-party data with own CRM and other client data will allow for accelerated opportunity realisation; third-party data providers and aggregators are often way ahead of banks, e.g., combining hundreds of data sources to identify new leads / improve services to existing clients will become the new norm
- Embed data analytics into the organisational culture and day-to-day business processes, most notably the advisor desktop, to ensure acceptance by users

Adapting talent management to address emerging gaps for ~40% of employee skill profiles must be a CEO priority

Wealth Managers must participate in the war for talent, particularly for highly sought-after data scientists and “hunters” – external partnerships become more important to fully close the skill gaps. What to do:

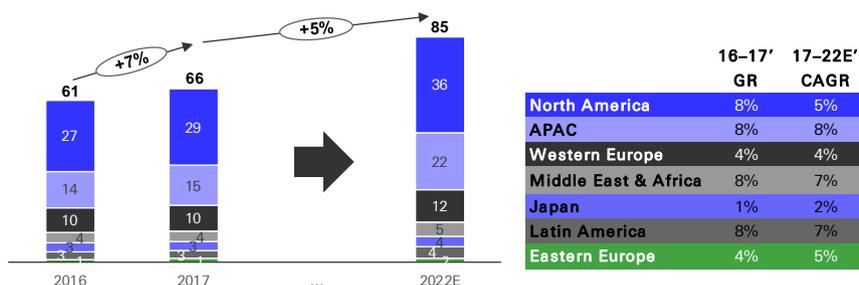
- Treat this as a top 3 CEO priority; firms running this effort out of the HR department will likely fail
- Accelerate learning and training efforts to upgrade existing employees’ skillsets, particularly related to rising data analytics demands
- Sharpen the talent value proposition to accommodate the preferences of new and transforming talent pools, particularly data scientists
- Seek external partnerships to tap into new talent pools beyond financial services to access the required skillsets, particularly for “hunters”

# Joint Executive Summary

## Strong results in 2017, but tail risks continued to grow

Global private financial high-net-worth (HNW) wealth grew by 7% in 2017 to US\$ 66TN – primarily driven by accelerating economic growth and the continuing strong performance of equity markets. North America and Emerging Markets have again seen the strongest growth.

Figure 1: Global private HNW wealth by major region, 2016-2020E, US\$ TN



Source: Oliver Wyman analysis

Note: HNW wealth is measured across households with financial assets greater or equal to US\$ 1 million. Financial assets include investable assets (deposits, equities, bonds, mutual funds and alternatives), excluding assets held in insurance policies, pensions and direct real estate or any other real assets. Numbers for all years were converted to US\$ at the year-end 2017 exchange rates to exclude the effect of currency fluctuations.

We project growth to slow to 5% p.a. over the next five years until 2022; however, with strong regional variation. Indicators pointing towards the end of the more than 30-year fixed income bull market have further intensified. The equity market correction and volatility spike in February 2018 may be an early indicator for the approaching end of the decade-long bull run in equity markets. Net new money (NNM) will be the main driver of wealth growth in our base case over the next five years, representing 55% of global HNW wealth growth.

## New offshore competition for regularised funds is starting to emerge

Recent Emerging Markets tax amnesties have resulted in the regularisation of offshore assets across Latin America, APAC, Eastern Europe, Middle East, and Africa. Many Emerging Markets HNW clients have participated in government tax amnesty programs and other schemes, but significant offshore-to-onshore flows have failed to materialise. Emerging Markets HNW individuals have mostly kept their wealth offshore. As a result, more than US\$ 600BN in offshore assets can now be freely moved between offshore Wealth Managers.

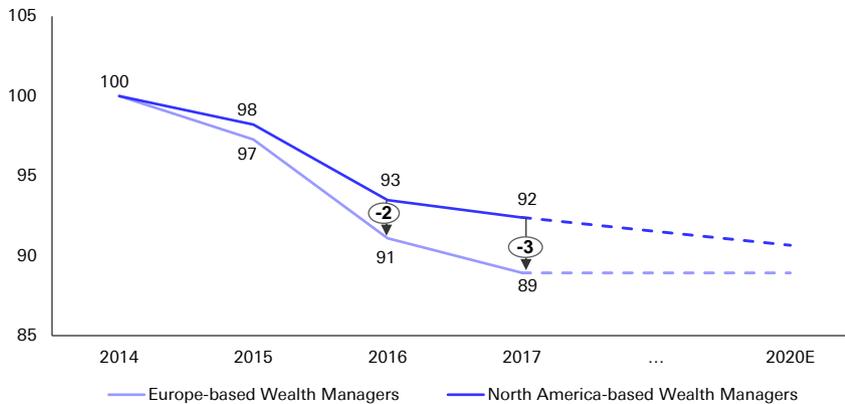
Consolidation of share of wallet represents a significant opportunity for those Wealth Managers with strong offshore propositions and attractive investment offerings. As tax optimisation considerations have lost attractiveness, our primary research shows that access to attractive investment products is turning into the main competitive edge.

## Fees remain under pressure but increasing mandate penetration provides a hedge

Fees remain under pressure. Additional fee transparency, from e.g., MiFID II / MIFIR in Europe, will only result in an accelerated shift towards lower-margin passive products or other sources of cheap beta. The stronger margin compression impact on Europe-based Wealth Managers was caused by a

MiFID II-driven shift to inducement-free products, the impact of regularisation and resulting loss of higher-margin offshore assets as well as stronger growth of the lower margin ultra-high-net-worth (UHNW) segment. However, we believe Europe-based Wealth Managers' fee levels will stabilise on the back of greater mandate penetration, given the attractive margin accretion from brokerage to mandate clients of sometimes more than 50bps.

Figure 2: Fee margin of Europe-based vs. North America-based Wealth Managers, 2014-2020E, %, indexed to 100, sample of leading Wealth Managers



Source: Deutsche Bank Research, Oliver Wyman analysis

We expect fee margins of North American firms to decline further due to a shift into lower-cost models (e.g., full service, hybrid, robo-advisory) through 2020, though pricing will remain mostly stable within the different models. While full implementation of the Department of Labor (DOL) fiduciary rule in its current state seems unlikely, the U.S. Securities and Exchange Commission (SEC) recently issued its own conflict-of-interest proposal that would require brokers to disclose material conflicts of interest and prohibit them from putting their interests before their clients'.

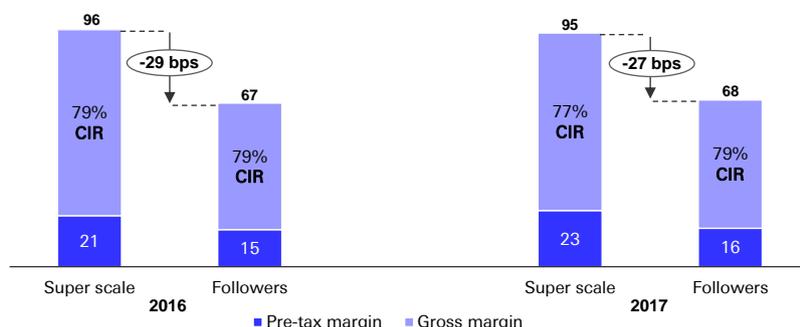
**Strong interest rate tailwinds have driven NII growth but deposit beta is kicking in**

Over the past year, higher net interest income (NII) driven by USD rate increases and increasing loan penetration translated into significant revenue uplift for many Wealth Managers. Looking at forward interest rate curves across USD and EUR, the upward slope suggests further opportunity for rate and NII sensitivity. At the same time, we believe that a large part of the US opportunity is already captured. Following recent rate hikes and similar to the developments during the last US rate cycle starting 2004, we expect a delayed pick up in deposit beta to take effect, i.e., the share of margin upside passed on to clients through pricing. Going forward, we expect Europe-based Wealth Managers to see the largest upside from future rate hikes due to the steeper forward curve and lower deposit betas.

**Cost-income ratios for medium and smaller Wealth Managers remain stubbornly high – regional differences are diminishing**

The profitability gap of super-scale firms vs. smaller firms has widened over the last year. Super-scale Wealth Managers were more successful in managing their costs, driven largely by early successes of automation and digitisation efforts.

Figure 3: Gross and pre-tax margins and cost-income ratios for super-scale vs. medium to small Wealth Managers, 2016-2017, bps



Source: Deutsche Bank Research, Oliver Wyman analysis  
 Note: "Super scale" defined as Wealth Managers with more than US\$ 500BN HNW AuM vs. "Medium to small" defined as Wealth managers with less than US\$ 500BN HNW AuM

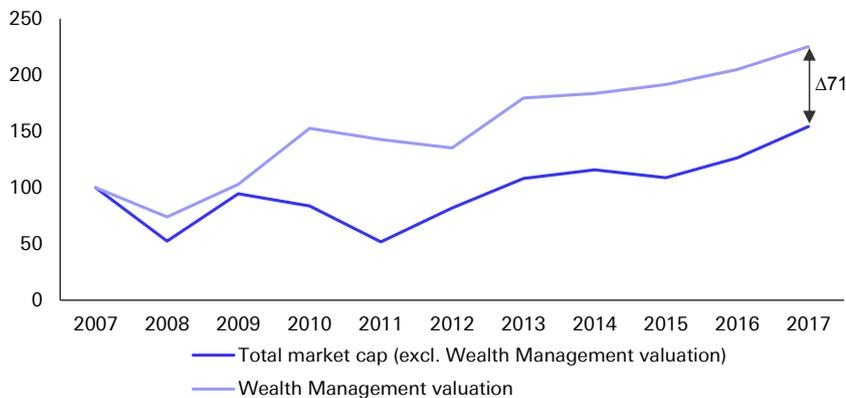
Medium to small Wealth Managers increased gross margins but failed to reduce cost-income ratios – their profitability continues to be highly sensitive to top-line pressures.

Recently, the differences in cost-income ratios between European-based and North America-based Wealth Managers have been diminishing. North America-based firms were able to lower cost-income ratios, while European-based firms have seen increasing cost-income ratios. Following a steady gap of c. 9 %-points in cost-income ratios from 2013 to 2015, cost-income ratios have since converged towards a gap of 1 %-point. This may give North America-based firms an advantage in absorbing profitability pressures in times of a market correction, compared to their European peers.

#### Wealth Management valuation gap vs. other bank businesses continued to narrow in view of structural headwinds

Wealth Management valuations continued to increase in 2017 (+10% YoY) on the back of an overall positive market environment. However, the valuation gap to other bank businesses has continued to narrow, given the structural headwinds the Wealth Management industry is facing: continued revenue pressure and an expected slowdown in Assets under Management (AuM) growth. Wealth Managers' sensitivity to asset levels remains high.

Figure 4: Equity market value development of overall bank vs. Wealth Management unit, 2007-2017, %, indexed to 100, sample of leading Wealth Managers, sum of parts analysis



Source: Deutsche Bank Research, Oliver Wyman analysis

We argue that management teams underestimate the potential effect of a bear market on economics. Instead of only focusing on short-term economics and quarterly results, they should prepare their business models for a potential market downturn.

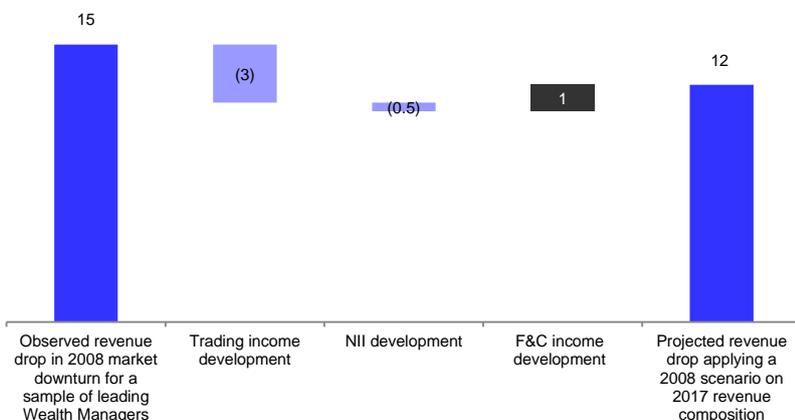
Wealth Managers must act now to preserve their superior valuations and remain a key focus of investor and management attention. Preparing for a market downturn in the short-term can make the difference between future winners and losers.

#### Revenue diversification does not shield top line from a market downturn

Wealth Managers have significantly changed the composition of their revenue streams over the last years. The share of NII rose across the industry on the back of continued strong lending growth. Share of overall revenue from fee income has remained broadly constant, with headwinds from downward fee pressure offset by greater mandate penetration. Greater mandate penetration however, has resulted in an overall decline in trading income share.

The frequently held belief that increased revenue diversification will protect Wealth Managers' top-line in times of stress does not hold in our view. In the short-term, all revenue components are still highly correlated to equity markets. In 2008, Wealth Managers faced AuM drops of c. 20%. Applying a stress scenario similar to the market correction of 2008 to today's industry average revenue composition of Wealth Managers only shows a slight protection of revenues by 3%-points vs. the last crisis. Absent any mitigation measures, we expect a revenue decrease of at least 12% compared to 15% experienced by Wealth Managers during the market downturn in 2008.

Figure 5: Expected revenue decline of Wealth Managers in a market downturn similar to 2008 and expected change of individual revenue components vs. 2008, % of revenues, sample of leading Wealth Managers



Source: Deutsche Bank Research, Oliver Wyman analysis

NII-related sensitivity drivers, in particular loan book composition, can only be influenced by Wealth Managers in the medium-term, but fee- and trading income-related income can be influenced in the short-term – this should be the main focus of attention. Offering capital protection for existing mandate positions and promoting superior investment quality embedded in mandate offerings are two key levers to mitigate mandate outflows. Promoting dynamic asset allocation within the investment guidelines of mandates and highlighting the quality of the overall CIO setup and investment process should further add to client confidence and help avoid emotion-driven trade decisions.

### Sharpening value propositions and mastering new transversal capabilities

Wealth Managers need to look towards more strategic changes to their value propositions and business models, which they have neglected in recent years.

By addressing strategic levers, we believe Wealth Managers can increase revenues by up to 20%, reduce cost-income ratios by more than 10%-points, and close the emerging gap in 40% of their employees’ skill profiles. To achieve this, they need to develop a differentiated value proposition by focusing on key competencies, embrace the revenue potential from data analytics, and transform their workforce strategies.

Figure 6: Strategic priorities for Wealth Managers

Focus on key competencies	Mastering data analytics	Transforming the workforce
Develop differentiated and focused value propositions along key competencies	Overcome data analytics challenges to unlock revenue potential along the entire client life cycle	Adjust talent management strategies to transform workforce
10+%-points Cost-income ratio reduction potential	~20% Revenue upside potential	~40% Change of employee skill profiles

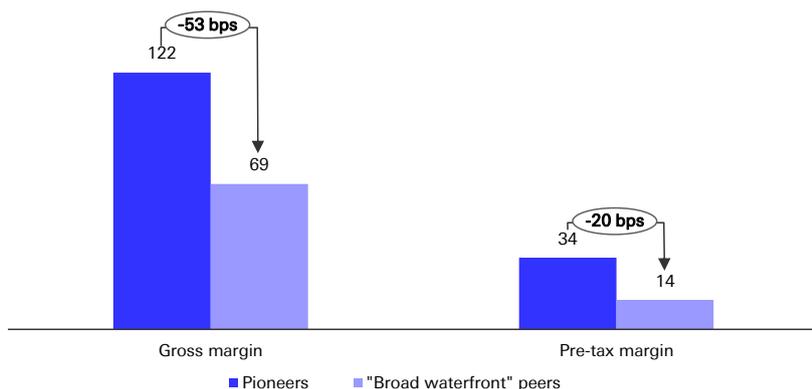
Source: Deutsche Bank Research, Oliver Wyman analysis

### Focus on key competencies

Most Wealth Managers' claim to offer clients a unique value proposition clearly distinguishing them from their competitors. This does not hold up in reality. Comparing leading Wealth Managers' strategies, visions, offerings, global footprint, and marketing materials reveals that the same "unique" value propositions are found across most; a strong client focus, advisory excellence, global reach, and a broad and superior product offering. This "broad waterfront" strategy of "offering everything, everywhere to everyone" is still the standard across most of the industry.

We believe that "broad waterfront" strategies can only be successfully pursued by a select few Wealth Managers, who have the necessary scale to orchestrate a complex geographic, client and product footprint. Most firms pursuing these "broad waterfront" strategies are achieving significantly lower economics compared to those Wealth Managers that have focused their value propositions and aligned their business models accordingly ("pioneers"), e.g., by reducing global footprint, product shelf and / or focusing on specific client segments. For example, Wealth Managers who manage to operate with an integrated platform on a regional level, e.g., Europe, can leverage synergies and reap significantly better economics going forward. Pioneers showcase gross and pre-tax profits that are ~50bps and ~20bps higher than their "broad waterfront" peers and hence also operate at significantly lower-cost-income ratios.

Figure 7: Average gross and pre-tax margin - Pioneers vs. "broad waterfront" peers, 2017, bps, sample of leading Wealth Managers



Source: Deutsche Bank Research, Oliver Wyman analysis

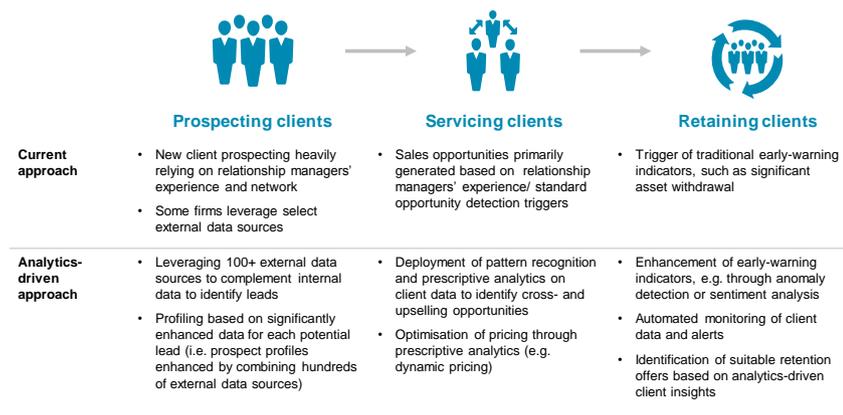
Across industries, within and outside financial services, a prevalence of non-differentiated value propositions has in the past reliably led to the emergence of new disruptive competitors. In recent years, competition from new entrants focusing on a single Wealth Management value chain component has already increased significantly. We see the expansion of intermediary / "broker" business models that have taken a strong foothold across the financial services industry (in particular for mortgages and insurance products) as a key risk to traditional Wealth Managers. Differentiation and continued client access will be critical in order not to be demoted to intermediated component providers. Wealth Managers must actively position themselves as demand aggregators, who own the client relationship and guide clients' buying decisions, for example through holistic financial advice and planning. Demand aggregators could then also move to integrate non-banking products and services that improve the overall client experience.

**Embrace data analytics to unlock revenue upside of up to 20%**

Extracting the full potential of Wealth Managers’ vast amounts of proprietary client data and combining it with external data sources remains a largely untapped value source for the industry. Especially unlocking the opportunity related to the vast amounts of external data remains a critical gap for many. New third-party providers, who start to combine hundreds of data sources to provide new leads / improve services to existing clients, can be a game changer.

The effective use of data analytics can both lead to a greatly improved client experience as well as a significant economic upside for Wealth Managers. Wealth Managers that succeed in fully exploiting data analytics opportunities can expect to achieve a revenue uplift of up to 20%. Revenue upside potential can be unlocked along the entire client lifecycle from improved prospecting and new client acquisition, to servicing existing clients better and improving retention rates.

**Figure 8: Upside levers of data analytics along the client lifecycle (not exhaustive)**



Source: Oliver Wyman analysis

Wealth Managers have started to build out their data analytics capabilities but no firm has fully captured the opportunity so far. Going forward, three key challenges must be addressed.

**Challenge 1: Getting the foundation right**

Most Wealth Managers still face significant gaps with respect to consistent and standardised collection, aggregation, and cleaning of data, frequently amplified by fragmented data storage across legacy IT systems.

Many firms have mistakenly looked at re-platforming to solve the issue, but we believe data aggregation software can help to address data governance-related issues already in the short-term. In the long run, Wealth Managers need to source or develop big data analytics technology capable of processing large amounts of data. The use of Application Programming Interfaces (APIs) offers an opportunity to advance the overall data governance and prepare a data landscape that allows to effectively integrate third-party data analytics point solutions.

### Challenge 2: Balancing internal legacy systems and in-house development with 3rd party solutions

Successfully exploiting the data analytics opportunity requires the identification and integration of external data and tool providers. Wealth Managers face a dual challenge: Identifying suitable partners in a fragmented market of point solutions providers and creating interfaces to integrate external tools and data with their legacy IT systems.

This requires Wealth Managers to establish strong sourcing and partnering capabilities. At the same time, it will be key to select those providers who have managed to create a key competitive edge. While in the past combining 2-5 sources of third-party data sources was typical and industry leading, the barrier has already shifted towards integrating hundreds of data sources.

### Challenge 3: Successfully embedding new capabilities into the day-to-day life of Relationship Managers

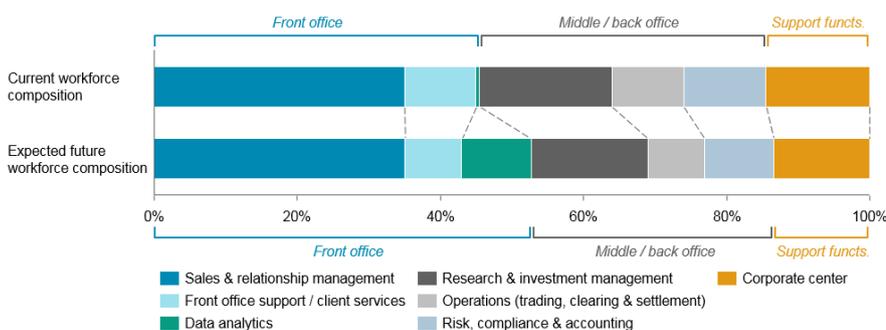
Low user acceptance and utilisation rates, particularly amongst relationship managers, are a key road block to unlocking the full value of existing and future data analytics tools.

Change management is crucial to realise the full potential, focusing on underlying culture, user acceptance, and ease of use. Wealth Managers must cultivate a data-driven culture emphasising accessibility and use of sophisticated analytics by all stakeholders. Management leading by example and revised incentive structures are key to foster acceptance. Future users must be closely involved in the development phase to shape functionality and user friendliness. Insights and recommendations must be seamlessly integrated into advisor workflows, providing a superior user experience. At the same time, pilots to showcase early successes will be key to create a pull effect across the front of the house.

### Adapting talent management to address emerging gaps for ~40% of employee skill profiles must be a CEO priority

We project up to 40% of Wealth Management employee skill profiles to significantly change over the next 5 to 10 years, requiring up- and reskilling along the entire Wealth Management value chain and fundamentally impacting the future workforce composition. At the same time, we expect Wealth Managers' headcount to reduce on the back of automation and externalisation, particularly in middle and back office functions.

Figure 9: Workforce composition of large Wealth Managers, current vs. expected, share of total workforce



Source: Oliver Wyman analysis

To close the emerging skill gaps, Wealth Managers will need to improve their learning and training efforts to upgrade existing employee skillsets. Skill gaps that cannot be closed through reskilling existing employees will have to be addressed through new hires and expanding the partner- and vendor ecosystem. This needs to be treated as a top 3 CEO priority, as the required workforce transformation is of critical importance to future success. Wealth Managers who handle the coordination of the workforce transformation as a simple Human Resources (HR) issue will likely fail.

#### [Wealth Managers must participate in the war for data science talent – external partnerships become more important to fully close skill gaps](#)

The increasing importance of data analytics across industries has led to a spike in demand and recruiting competition for data scientists and engineers. The financial services industry, including Wealth Management, is suffering from low popularity as an employer among this target talent pool. At traditional financial services target universities, the share of graduates joining financial services almost halved to around 25% between 2007 and 2016. At the same time, technology companies have more than tripled their intake to 20% of graduates.

Facing off against technology firms and the broader start-up universe, Wealth Managers need to sharpen their employee value proposition along three dimensions to attract data scientists and engineers: Organisation & culture, talent management, and compensation & incentives. They must establish a culture fostering agile working and innovation practices as well as accounting for different career path preferences, flexible working options, non-monetary incentives, and non-hierarchical reward systems. Gaps, that cannot be closed by hiring new talent directly, will see Wealth Managers seeking new external partnerships to access the required skillsets.

#### [Relationship managers will remain the most significant employee population but access to “hunters” will be the real source of competitive advantage](#)

The advancement of data analytics will reshape activities and skillsets of relationship managers: they will be able to focus their activities on the acquisition of new clients, relationship building, and increasing the share of wallet with existing clients. This shift in activities will widen the divide between the roles of nurturing “farmer” profiles and sales-driven “hunter” profiles.

Wealth Managers will increasingly need to tap into new talent pools beyond financial services to access the required talent, particularly for sought-after “hunter” profiles.

In exploring new talent pools, Wealth Managers must look towards industries that display distinct “hunter”-related characteristics, requiring similar sales-driven employee profiles and involving close interaction with high profile HNW and UHNW clients. Exemplary talent pools Wealth Managers can target include luxury goods sales staff and services, hospitality, and lobbyists.

#### [Wealth Managers need to act now, while markets support superior income and the industry still has its fate in its own hands](#)

With a host of challenges for the industry looming on the horizon, decisive management action is required now to make the necessary business model adjustments to stand out vs. competition. Investments into transversal capabilities of data analytics and workforce management will be a key differentiator to cement future success.

# 1) Strong results in 2017, but tail risks continued to grow

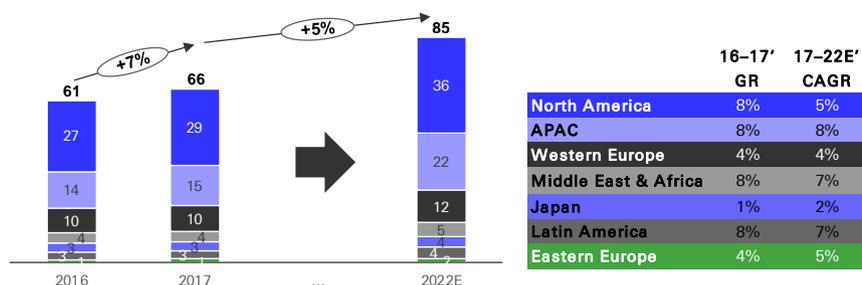
## Global financial wealth continued to grow by 7% but the outlook remains muted as asset growth slows down

Global private financial HNW wealth grew by 7% in 2017 to US\$ 66TN, driven by accelerating economic growth and the continuing strong performance of equity markets. We observe strong regional variation in growth. North America and Emerging Markets have again seen the strongest expansion of HNW wealth, with growth rates in the high single-digits.

North American wealth expansion was primarily driven by market reactions following the US presidential election in November 2016 as well as expectations of deregulation of financial markets and tax cuts. The US tax reform, which came into effect in the beginning of 2018 and significantly reduces corporate tax rates, is expected to have a positive effect on personal HNW wealth growth. The personal savings rate is expected to grow over the next several years as employee earnings grow.

Driven by regional economic growth, APAC and Latin America saw almost double-digit HNW wealth growth in 2017. The Middle East and Africa benefitted from rebounding oil prices. Western Europe's HNW wealth growth continued to face challenges in light of Brexit and Eurozone uncertainties, which will remain in the short- to medium-term. We project Western Europe's HNW wealth market to continue to lose relative weight compared to other regions.

Figure 10: Global private HNW wealth by major region, 2016-2020E, US\$ TN



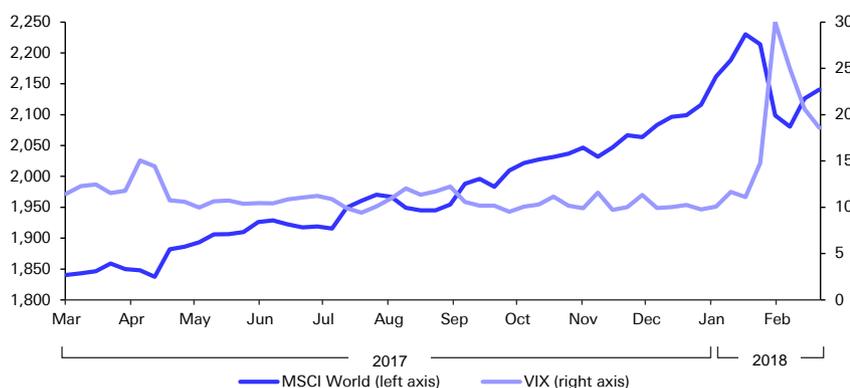
Source: Oliver Wyman analysis  
 Note: HNW wealth is measured across households with financial assets greater or equal to US\$ 1 million. Financial assets include investable assets (deposits, equities, bonds, mutual funds and alternatives), excluding assets held in insurance policies, pensions and direct real estate or any other real assets. Numbers for all years were converted to US\$ at the year-end 2017 exchange rates to exclude the effect of currency fluctuations.

As a more uncertain macro environment lies ahead, we expect global HNW wealth growth to slow to 5% p.a. over the five years until 2022. Emerging Markets are expected to see continued strong HNW wealth growth on the back of strong gross domestic product (GDP) growth. The overall lower HNW wealth growth will primarily be driven by lower asset returns over the next five years.

Indicators pointing towards the end of the more than 30-year fixed income bull market have further intensified. The Federal Reserve is now firmly on a regular hike cycle whilst the European Central Bank is slowly but surely approaching the end of an extraordinary period of quantitative easing and, in recent years, negative rates. We expect rates and yields to continue to structurally increase over the next few years along with short-term volatility. Reissuances will provide higher yields going forward but bond prices will likely decrease.

At the end of January, cyclically adjusted price-to-earnings multiples were at a record high of 34 compared to 29 a year ago and significantly higher than the previous cycle's peak of 27 in autumn 2008. The equity market correction and volatility spike in February 2018 may be an early indication for the approaching end of the decade-long bull market in equity markets.

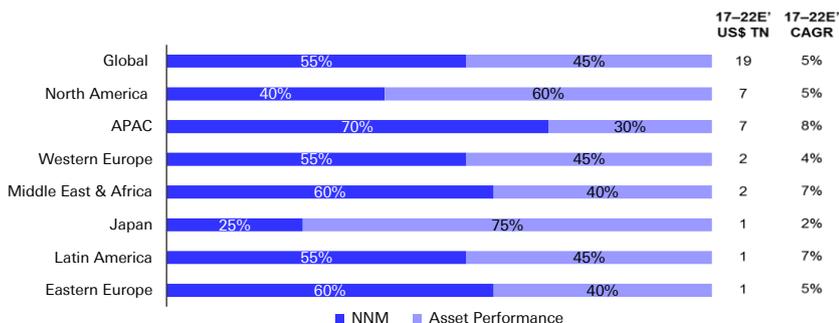
Figure 11: MSCI World and Volatility Index, last twelve months



Source: Bloomberg, Oliver Wyman analysis

The unwinding of this extended period of ultra-loose monetary policy will lead to higher volatility and more regular risk sell-offs. As a result, NNM will be the main driver of wealth growth over the next five years, representing 55% of global HNW wealth growth.

Figure 12: HNW wealth growth composition projections by region, 2017-2022E, %



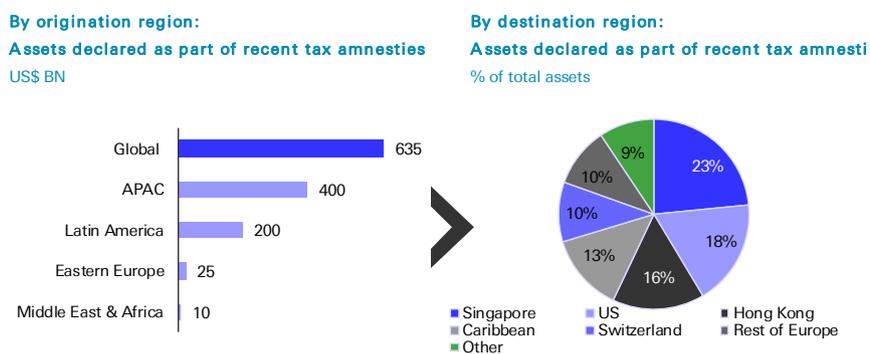
Source: Oliver Wyman analysis

## New offshore competition for regularised funds starts to emerge

In last year's report – "Time to advance and defend" – we argued that the onset of Automatic Exchange of Information (AEOI) paired with the growing trend towards tax amnesties would continue to drive further material regularisation outflows from offshore assets originating in Emerging Markets, i.e., the second regularisation wave.

Recent Emerging Market tax amnesties have resulted in regularisation of offshore assets across Latin America, APAC, Eastern Europe, Middle East, and Africa. As a result, more than US\$ 600BN offshore assets are now in motion.

Figure 13: Offshore assets declared as part of tax amnesties since 2015



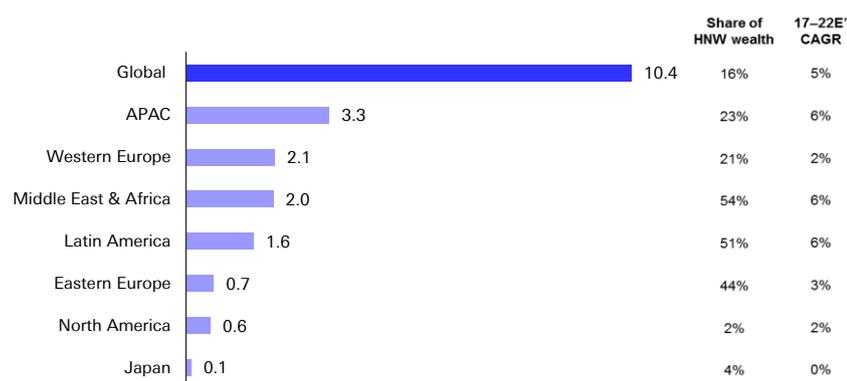
Source: Oliver Wyman analysis

Many clients have participated in government tax amnesty programs and other schemes during this second wave of regularisation but significant offshore-to-onshore flows have failed to materialise – Emerging Markets HNW individuals have mostly kept their wealth offshore.

We believe the bulk of regularisation to be over but with the actual implementation of AEOI taking place in 2018 and 2019, we expect modest further pressure over the next couple of years. Global Wealth Managers have largely completed their portfolio clean-up activities but a smaller Wealth Managers will likely be further impacted by remaining regularisation pressures.

Emerging Markets onshore offerings have evolved, but we expect HNW individuals demand for offshore offerings to remain high, driven by macroeconomic and geopolitical instability, FX fluctuations, better investment opportunities, and sophisticated client needs that cannot be served onshore at present. We anticipate stable offshore wealth growth of 5% p.a. over the next 5 years, which is in line with our overall wealth growth projection.

Figure 14: HNW offshore wealth by origination region, 2017, US\$ TN



Source: Oliver Wyman analysis

We see an emerging opportunity for Wealth Managers in offshore markets. Offshore competition has been revived by the regularisation efforts, as clients can now freely move offshore assets between offshore Wealth Managers. Consolidation of share of wallet represents a significant opportunity for those Wealth Managers with strong offshore propositions and attractive investment offerings. As tax optimisation considerations have lost relative attractiveness, our primary research shows that access to attractive investment products is turning into the main competitive edge. Global Wealth Managers will be able to use their international presence as leverage; regional players can leverage their local presence, expertise and relationships as strong arguments to compete for offshore assets.

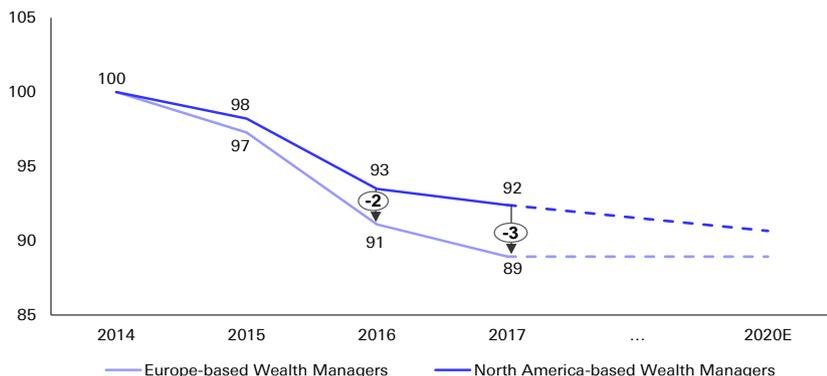
## Rate tailwinds offset continued downward fee pressure

Throughout last year, Wealth Managers could offset continued fee pressure due to increasing rates and growing AuM. Most of the US NII opportunity seems to be over and we anticipate further pressure on fees for North America-based Wealth Managers. For Europe-based Wealth Managers the future looks brighter considering anticipated interest rate hikes and fee pressure levelling off.

### Fees remain under pressure but increasing mandate penetration provides a hedge

Fees continue to remain under pressure - additional fee transparency, e.g., from MiFID II / MIFIR in Europe, will only result in an accelerated shift towards lower-margin passive products or other sources of cheap beta. North America-based firms' fee margins have held up better than their Europe-based peers in the past but we believe European Wealth Managers' fee levels have the worst behind them and will stabilise on the back of greater mandate penetration.

Figure 15: Fee margin of Europe-based vs. North America-based Wealth Managers, 2014-2020E, %, indexed to 100, sample of leading Wealth Managers



Source: Deutsche Bank Research, Oliver Wyman analysis

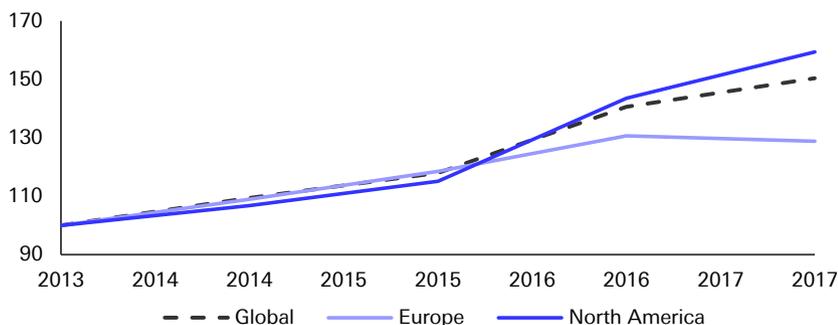
The stronger fee impact on Europe-based Wealth Managers was largely caused by a MiFID II-driven shift to inducement-free products, the impact of regularisation and resulting loss of higher-margin offshore assets, as well as stronger growth of the generally lower margin UHNW segment. We believe European Wealth Managers will stabilise on the back of greater mandate penetration going forward, given the attractive margin accretion from brokerage to mandate clients of sometimes more than 50bps.

We expect fee margins of North American firms to decline due to a shift into lower-cost models (e.g., full service, hybrid, robo-advisory) through 2020, though pricing will remain mostly stable within the different models. While full implementation of the Department of Labor (DOL) fiduciary rule in its current state seems unlikely, the U.S. Securities and Exchange Commission (SEC) recently issued its own conflict-of-interest proposal that would require brokers to disclose material conflicts of interest and prohibit them from putting their interests before their clients'.

**Strong interest rate tailwinds have driven NII but deposit beta is kicking in**

Industry NII has increased significantly on the back of increasing loan penetration and recent US rate hikes, translating into a significant revenue uplift for many Wealth Managers. Looking at two-year forward interest rate curves across USD and EUR, the upward slope continues to suggest further opportunity for rate and NII margin sensitivity.

Figure 16: Development of NII, 2013-2017, %, indexed to 100, sample of leading Wealth Managers



Source: Deutsche Bank Research, Oliver Wyman analysis

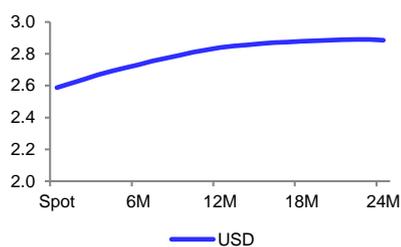
Particularly Wealth Managers based in North America and those with significant USD exposure have benefited from recent rate hikes, but we believe a large part of the US opportunity is already captured. Following recent rate hikes, we expect deposit betas, i.e., the share of margin upside passed on to clients through pricing, to rise.

Data from past US rate hike cycles, the most recent one commencing in 2004, suggests a delay in deposit betas after rate hikes. Deposit betas remained below 20% during the initial 2004 rate hikes, but took off subsequently. By 2006, increases in client rates paid outpaced rate hikes and cumulative deposit betas reached c. 60%.

The current deposit beta development resembles 2004, but deposit beta levels are already higher than in the beginning of the last rate hike cycle. Deposit betas have risen over the last months, with many US-based banks reporting deposit betas approaching 30% and higher. We expect deposit betas of Wealth Managers to exceed these levels going forward, given the increasing focus on upper HNW and quasi-institutional UHNW clients who expect a greater pass-through of rate increases. Considering the increased competition in the US Wealth Management market, we anticipate further strong increases in deposit betas beyond peak levels observed in the past rate hike cycle, limiting the upside to Wealth Managers from future US rate hikes.

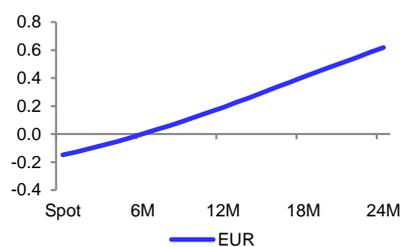
Looking at EUR forward curves, we expect European Wealth Managers to see the largest upside from future rate hikes. Not only because of the steeper EUR forward curve compared to the plateauing USD forward curve, but also due to lower deposit betas in Europe, which implies that a smaller proportion of each rate hike will get passed on to clients.

Figure 17: Forward 2yr curve – USD, %



Source: Bloomberg, Oliver Wyman analysis

Figure 18: Forward 2yr curve – EUR, %

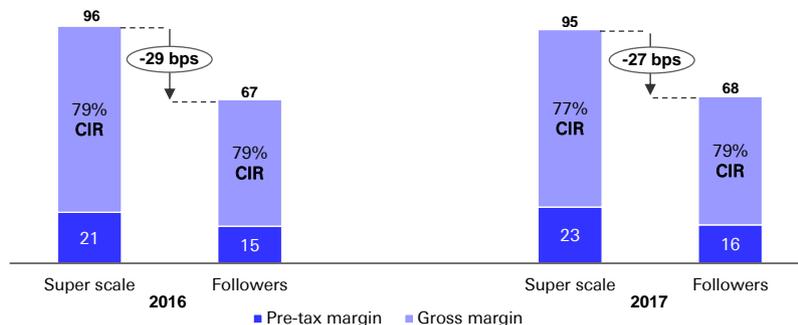


Source: Bloomberg, Oliver Wyman analysis

## Cost-income ratios for medium and smaller Wealth Managers remain stubbornly high – regional differences are diminishing

Improving profitability through ongoing cost reductions remains of critical importance. The profitability gap of “super scale” Wealth Managers vs. medium to small Wealth Managers has widened over the last year. Gross margin differential decreased by 3 bps but the gap in pre-tax profit widened to 7bps on the back of more successful cost management by super scale Wealth Managers, driven largely by early successes of automation and digitisation efforts.

Figure 19: Gross and pre-tax margins and cost-income ratios for super-scale vs. medium to small Wealth Managers, 2016-2017, bps



Source: Deutsche Bank Research, Oliver Wyman analysis  
 Note: “Super scale” defined as Wealth Managers with more than US\$ 500BN HNW AuM vs. “Medium to small” defined as Wealth managers with less than US\$ 500BN HNW AuM

Medium to small Wealth Managers increased gross margins but failed to reduce cost-income ratios mainly due to regulatory response costs. This continued struggle to address their high operating costs means that medium to small Wealth Managers are significantly more sensitive to top line pressures than their larger peers.

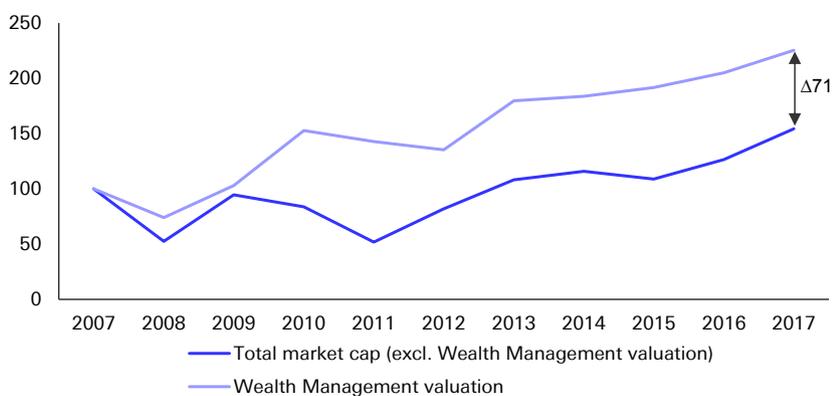
In their attempts to lower costs, Wealth Managers should be sensitive to the trade-off between fixed and variable costs. At ~40% of total costs, the variable cost component (i.e., costs that largely fluctuate with revenues) of North American broker-based business models is usually much higher compared to the traditional, European Private Banking-based model at ~20%. This has given North America-based players more leeway in times of market downturns, but also led to North American firms operating at higher cost-income ratios than their Europe-based peers in good times.

Recently, the differences in cost-income ratios between European-based and North America-based Wealth Managers have been diminishing. North America-based firms were able to lower cost-income ratios, while European-based firms have seen increasing cost-income ratios. Following a steady gap of c. 9 %-points in cost-income ratios from 2013 to 2015, cost-income ratios have since converged towards a gap of 1 %-point. This may give North America-based players an advantage in absorbing profitability pressures in times of a market correction, compared to their European peers.

## Wealth Management valuation gap vs. other bank businesses continued to narrow in view of structural headwinds

Wealth Management valuations continued to increase in 2017 (+10% YoY) on the back of an overall positive market environment. However, the valuation gap to other bank businesses has continued to narrow, given the structural headwinds the Wealth Management industry is facing: continued revenue pressure and an expected slowdown in AuM growth as possible signs of an approaching market downturn. Wealth Managers' sensitivity to asset levels remains high.

Figure 20: Equity market value development of overall bank vs. Wealth Management unit, 2007-2017, %, indexed to 100, sample of leading Wealth Managers, sum of parts analysis



Source: Deutsche Bank Research, Oliver Wyman analysis

We argue that management teams underestimate the potential effect of a bear market on economics. Instead of only focusing on short-term economics and quarterly results, they should prepare their business models for a potential market downturn.

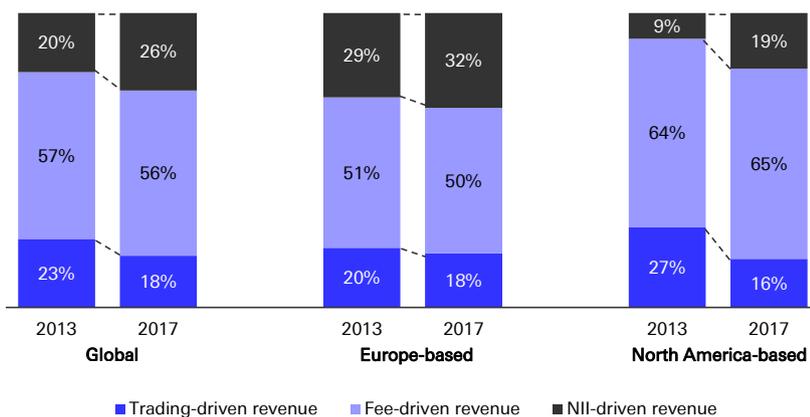
Wealth Managers must act now to preserve their superior valuations and remain a key focus of investor and management attention. Preparing for a market downturn in the short-term can make the difference between future winners and losers.

## 2) Revenue diversification does not shield top line from a market downturn

Wealth Managers have changed the composition of their revenue streams over the past decade, but this will not shield economics from a market downturn

Wealth Managers have significantly changed the composition of their revenue streams over the last years. The share of NII rose across the industry on the back of continued strong lending growth. Particularly North America-based Wealth Managers have effectively doubled NII's share of overall revenue. Share of overall revenue from fee income has remained broadly constant, with headwinds from downward fee pressure offset by greater mandate penetration. Greater mandate penetration however, has resulted in an overall decline in trading income share.

Figure 21: Composition of Wealth Managers' revenues, 2013 vs. 2017, % of revenues, sample of leading Wealth Managers



Source: Deutsche Bank Research, Oliver Wyman analysis

### Overall revenues remain highly sensitive to asset levels

The frequently held belief that increased revenue diversification will protect Wealth Managers' top-line in times of stress does not hold in our view. The increase in NII at the expense of investment income brings limited diversification benefits and the increase of fee income's share in investment income provides only limited protection.

In the short-term, all revenue components are still highly correlated to equity markets. In 2008, Wealth Managers faced AuM drops of c. 20%. Applying a stress scenario similar to the market correction of 2008 to today's industry average revenue composition of Wealth Managers only shows a slight protection of revenues by 3%-points vs. the last crisis. Absent any mitigation measures, we expect a revenue decrease of at least 12% compared to 15% experienced by Wealth Managers during the market downturn in 2008.

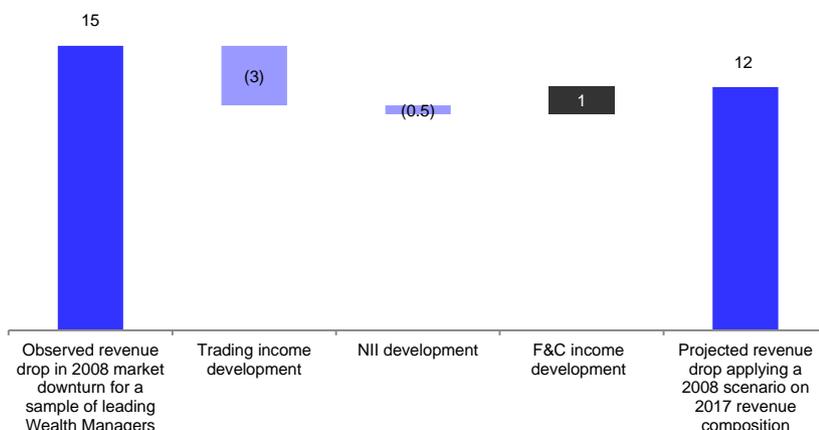
**NII-related sensitivity drivers:** The protection offered by NII growth depends on the loan book composition of the respective Wealth Manager. Lombard loans are significantly more sensitive to market downturns than mortgages. We anticipate a disproportionate revenue hit in times of crisis for Wealth Managers with a high share of Lombard loans. Today's overall loan book composition in the industry is approximately equal to 2007, but a subset of Wealth Managers has disproportionately grown their Lombard book – they will be hit hardest in times of market corrections. During the last market downturn, Wealth Manager's NII was protected by a LIBOR tailwind – we do not expect this to be the case in the next market downturn - which amplifies NII pressure. During the last market downturn, banks became fearful of lending to one another, leading to an increase in the rates they charged each other for short-term loans. Consequently, the share of LIBOR-linked loans led to an increase in NII for Wealth Managers in 2008 and 2009.

**Trading income-related sensitivity drivers:** Historical data shows that increased volatility at the onset of a market downturn will lead to temporarily higher trading income for one or maybe two quarters. Once clients have traded out of their positions and shifted investments into "safer" asset classes, trading income should drop sharply.

**Fee income-related sensitivity drivers:** In a market downturn, fee income will be negatively affected by declining AuM. We further expect the decline in fee income to be amplified by clients getting "cold feet" and shifting their assets out of mandates and into perceived stable and crisis-safe asset classes like cash.

NII-related sensitivity drivers, in particular loan book composition, can only be influenced by Wealth Managers in the medium-term, e.g., through a conscious shift towards mortgages. Fee- and trading income-related income can be influenced in the short-term – this should be the Wealth Managers' main focus of attention.

Figure 22: Expected revenue decline of Wealth Managers in a market downturn similar to 2008 and expected change of individual revenue components vs. 2008, % of revenues, sample of leading Wealth Managers

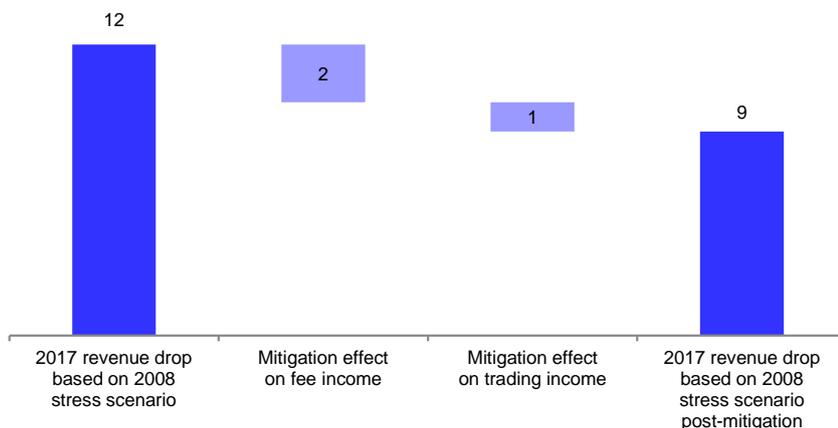


Source: Deutsche Bank Research, Oliver Wyman analysis

## Immediate action is required to mitigate market downturn impacts

We see a number of mitigation measures that can help reduce revenue pressures in a market downturn. Protecting mandate penetration is the single most important driver for Wealth Managers to preserve their economics in a market downturn. ‘Stimulating’ trading activity can have a positive short-term impact which typically fades after 1-2 quarters. We estimate that revenue pressure can be reduced by up to 2%-points by protecting current levels of mandate penetration. Mitigation measures to encourage trading activity of clients can reduce pressure on trading income by up to 1%-point.

Figure 23: Expected effect of mitigation measures on fee income and trading income, % of revenues, sample of leading Wealth Managers



Source: Deutsche Bank Research, Oliver Wyman analysis

To mitigate the expected drop in fee income, it will be key to offer clients protection against negative asset returns. Protection of mandate holdings benefit Wealth Managers twofold: it increases client satisfaction and loyalty

and protects AuM levels. Wealth Managers can offer protection on the mandate principal outstanding for an additional fee, e.g., through index options on equity positions in the mandate.

Secondly, building dynamic asset allocation into mandate investment guidelines and highlighting the quality of the overall CIO setup and investment process should further add to client confidence and help avoid emotion-driven trade decisions in times of market downturn.

In last year's industry report we urged Wealth Managers to rethink their CIO models to more dynamically re-allocate assets. Spotting and communicating tactical investment opportunities to clients faster represents a win-win opportunity. It can simultaneously drive greater client engagement and generate higher client returns. Trading activity can be stimulated and consequently trading income protected.

Although these mitigation measures will not fully negate the revenue pressure, they can meaningfully lessen the impact. Still, Wealth Managers need to look towards more strategic and structural changes in their business model to emerge from a future market downturn well positioned for success.

### 3) Sharpening value propositions and mastering new transversal capabilities

In recent years, Wealth Managers’ have benefitted from a favourable market environment driven by strong asset performance and in many cases an opportunity to expand balance sheets. The majority of Wealth Managers have failed to address critical questions regarding future strategic direction. If these remain unaddressed, the sustainability of the Wealth Managers business models may be challenged. Developing differentiated and focused value propositions along key competencies as well as embracing the full potential of data analytics should be key strategic priorities. To unlock these opportunities, Wealth Managers will have to rethink their workforce strategies. By addressing these strategic levers, we believe Wealth Managers can increase revenues by up to 20%, reduce cost-income ratios by more than 10%-points, and close the emerging gap in 40% of their employees’ skill profiles.

Figure 24: Strategic priorities for Wealth Managers

Focus on key competencies	Mastering data analytics	Transforming the workforce
Develop differentiated and focused value propositions along key competencies	Overcome data analytics challenges to unlock revenue potential along the entire client life cycle	Adjust talent management strategies to transform workforce
10+%-points Cost-income ratio reduction potential	~20% Revenue upside potential	~40% Change of employee skill profiles

Source: Oliver Wyman analysis

#### Focus on key competencies

##### Most Wealth Managers lack a differentiated value proposition

Most Wealth Managers claim to offer clients a unique value proposition, clearly distinguishing them from competitors. Yet this does not hold up in reality. Comparing leading Wealth Managers’ strategies, visions, offerings, geographic footprint, and marketing materials reveals that the same “unique” value propositions are found across most; a strong client focus, advisory excellence, global reach, and a broad and superior product offering.

Figure 25: Key words used in Wealth Managers' communication materials, size according to frequency of occurrence, sample of leading Wealth Managers

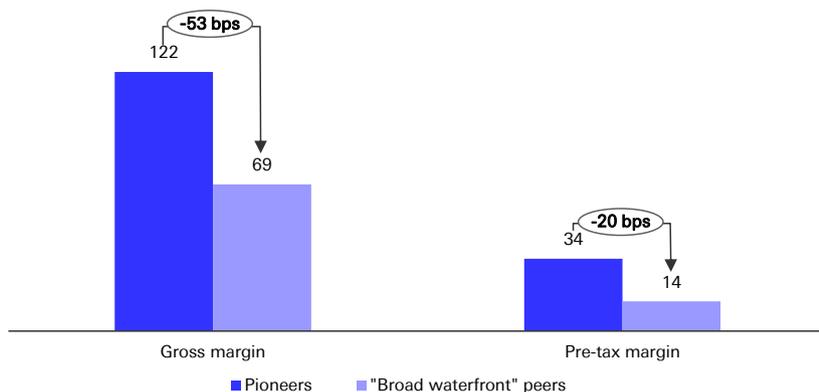


Source: Company information, Oliver Wyman analysis

### Wealth Managers willing to focus on key competencies can unlock superior economics

The “broad waterfront” strategy of “offering everything, everywhere to everyone” is still the standard across most of the industry. We believe that “broad waterfront” strategies can only be successfully pursued by a select few Wealth Managers who have the necessary scale to orchestrate a complex geographic, client and product footprint. Most firms pursuing these “broad waterfront” strategies are achieving significantly lower economics compared to those Wealth Managers that have focused their value propositions and aligned their business models accordingly (“pioneers”), e.g., by reducing global footprint, product shelf and / or focusing on specific client segments. Pioneers showcase gross and pre-tax profits that are ~50bps and ~20bps higher than their “broad waterfront” peers. This translates into a cost-income ratio differential of 7%-points, with pioneers operating at ~72% and “broad waterfront” peers at ~79% cost-income ratios at present.

Figure 26: Average gross and pre-tax profit - Pioneers vs. “broad waterfront” peers, 2017, bps, sample of leading Wealth Managers



Source: Company information, Oliver Wyman analysis

In the past, strong overall asset performance masked the inferior economics associated with a lack of differentiation. Increasing transparency on products and pricing, lower switching costs for clients, as well as rising competition from emerging disruptors are amplifying the pressure. “Broad waterfront” Wealth Managers will need to sharpen their value proposition to improve economics and regain investors’ attention.

### Undifferentiated Wealth Managers face an increased risk of becoming irrelevant

Across industries, within and outside financial services, a prevalence of non-differentiated value propositions has in the past reliably led to the emergence of new disruptive competitors. In recent years, competition from new entrants focusing on a single Wealth Management value chain component has increased significantly

#### **Case study: The rise of mortgage brokers in the UK**

Thirty years ago, the UK mortgage market was dominated by lenders and characterised by a lack of price competition. Basically, lenders jointly pre-agreed prices and captured all profits. Only in the mid-1980s, deregulation caused a change in market structure which intensified competition and cleared the way for mortgage brokers to enter the market.

Three decades later, in 2017, mortgage brokers and intermediaries account for 80% of mortgage distribution in the UK and profits are divided between lenders and brokers. Mortgage brokers have stimulated competition through increased overall price and product transparency for borrowers. Borrowers now have visibility into a much broader and pre-screened product portfolio from which they can select. A clear-cut value proposition paired with increased distribution through digital channels has fuelled and solidified broker success in Europe’s largest mortgage market.

We see the expansion of intermediary / “broker” business models that have taken a strong foothold across the financial services industry (in particular for mortgages and insurance products) as a key risk to traditional Wealth Managers. Brokers have fundamentally shifted revenue and profit pools within the segments they are serving. As brokers increasingly gain a foothold in the Wealth Management industry, initially through high value mortgages, incumbents will face pressure to preserve their economics. Differentiation and continued client access will be key in order not to be demoted to intermediated component providers. Wealth Managers can actively position themselves as demand aggregators, who own the client relationship and guide clients’ buying decisions, for example through holistic financial advice and planning. Demand aggregators could then also move to integrate non-banking products and services that improve the overall client experience. Demand aggregators differentiate by providing an all-encompassing client experience centred on individual needs. They benefit from their large number of client relationships, wide-ranging distribution reach and access to client data, such as credit quality, source of wealth and life cycle stage

### Pioneers have proactively sharpened their value propositions

Recent actions taken by select Wealth Managers can serve as examples of how to successfully sharpen value propositions and streamline the business. This includes, most notably, efforts to narrow the geographic footprint and client segments served. Additional efforts include differentiation of delivery models and rationalisation of product shelves.

When implementing these initiatives, pioneers have seen considerable revenue upside and cost reductions. We argue that focusing on key competencies can unlock cost-income ratio reductions of 10%-points and more. This will exceed the 7%-point cost-income ratio differential previously observed between pioneers and “broad waterfront” peers.

Figure 27: Exemplary actions to focus on key competencies and associated cost-income ratio reduction potential, %-points

 Sharpen global footprint	 Align target clients with delivery model	 Streamline product offering
Streamlining booking centres and physical office footprint  <b>3-6%-point CIR reduction</b>	Raising entry threshold for full-service model  Implementing digital-only access/pooled relationship manager model for clients with lower revenue potential  <b>5-10%-point CIR reduction</b>	Rationalisation of product shelf  <b>2-4%-point CIR reduction</b>

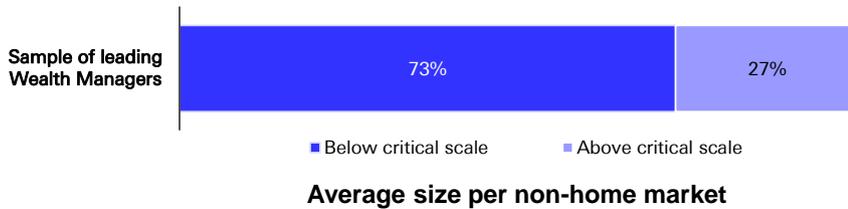
Source: Oliver Wyman analysis

### Streamlining booking centres and physical office footprint – less is more

Wealth Management for core HNW individuals is still a multi-local industry rather than truly global, i.e., firms compete in each national market largely independent of other markets. Geographic footprint rationalisation is a key lever to simplify the business matrix. Wealth Managers have significantly reduced offshore booking centres in recent years but many have been more reluctant to reduce their physical footprint onshore. Most large Wealth Managers still maintain a highly fragmented geographic footprint, often only reaching sufficient scale in their home market and select adjacent markets. Sub-scale operations in other markets have limited positive bottom line impact and are hence often a “luxury” to be able to advertise global reach to their existing client base.

As we noted last year in our report “Time to Advance and Defend”, the mid-term minimum scale to operate a regional booking centre / platform profitably will increase to roughly US\$ 30BN. Even if we lower the threshold to US\$ 20BN to take into account some markets with lower cost to serve at present, our analysis of leading Wealth Managers shows that less than 30% of them reach critical scale in markets outside their home market. Naturally, the exact critical scale required depends on the individual market characteristics, but many Wealth Managers remain far below any economically feasible threshold in multiple markets.

Figure 28: Wealth Managers operating non-home markets at scale or below scale by average AuM per market, % of Wealth Managers, sample of leading Wealth Managers



Source: Deutsche Bank Research, Oliver Wyman analysis  
 Note: "Critical scale" defined as US\$ 20BN per booking centre that is located outside the home market (i.e., "non-home market")

Geographic reach will continue to be a key selling proposition, especially for upper HNW and UHNW clients, but only a few true global champions will be able to operate profitably across markets on a global basis. Wealth Managers who manage to operate with an integrated platform on a regional level, e.g., Europe, can leverage synergies and reap significantly better economics going forward. Most Wealth Managers will need to take well calculated bets to serve only those jurisdictions where they are already at scale or have a high confidence plan to get to critical scale in the short-term.

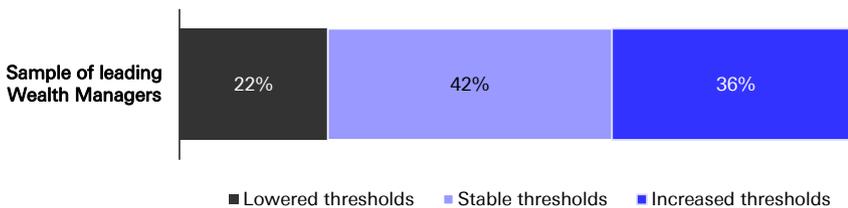
Over the past few years, select Wealth Managers have started initiatives to focus their geographic footprint. Some have reduced their physical footprint by almost half, realising cost-income ratio reductions of 3-6%-points. Other examples include Wealth Managers forging international collaborations to serve clients globally without growing their physical presence.

**Increasing entry thresholds – serving fewer clients better**

We believe narrowing the target client segments served is another lever for Wealth Managers to sharpen their value proposition, albeit still underutilised.

Inflation and an increasing number of HNW and UHNW clients worldwide have significantly increased the client base available to Wealth Managers. Since 2011, only 36% of Wealth Managers have raised their entry thresholds for HNW clients. At the same time, 22% of Wealth Managers have even lowered their entry thresholds

Figure 29: Change in entry thresholds, 2011-2017, % of Wealth Managers



Source: Oliver Wyman analysis

As a result, Wealth Managers are serving an increasingly diverse set of clients across wealth brackets, straining relationship managers' ability to address individual client needs and limiting the ability to reduce costs to serve. This is particularly challenging for Wealth Managers who do not differentiate their delivery model for different client segments but instead employ a one-size-fits-all approach.

A market scan shows a select few Wealth Managers who have doubled their entry threshold for private banking clients. This effectively leads to terminating a significant number of client relationships, often more than 10%, or migrating them to lower end mass affluent service models, with much lower average cost to serve, e.g., through digital delivery models or a higher client-to-relationship manager ratio. Remaining clients are encouraged to consolidate their wallet with a single Wealth Manager to meet the higher entry thresholds, increasing the revenue-generating AuM basis. Successful Wealth Managers have seen their cost-income ratio drop by 5-10%-points due to narrower client focus and a better alignment of their delivery model to client types served. Although a significant number of clients have been exited / migrated to lower tier banking services these Wealth Managers have largely kept their asset base stable.

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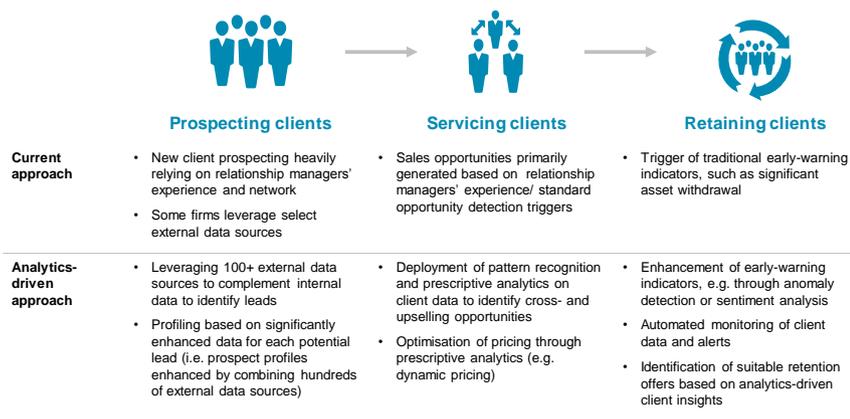
## Embrace data analytics to unlock revenue upside of up to 20%

[Extracting the full value of internal and external data is the most underutilised value source for Wealth Managers today](#)

Extracting the full potential of Wealth Managers' vast amounts of proprietary client data and combining it with external data sources remains a largely untapped value source for the industry. Especially unlocking the opportunity related to the vast amounts of external data remains a critical gap for many. New third-party providers, who start to combine hundreds of data sources to provide new leads / improve services to existing clients, can be a game changer. The effective use of data analytics can lead to a greatly improved client experience as well as significant economic upside for Wealth Managers. New regulatory requirements, such as the Revised Payment Service Directive (PSD2), the General Data Protection Regulation (GDPR), or the Basel Committee on Banking Supervision's standard number 239 (BCBS239), will force the industry to revise their current data management practices. We expect this to accelerate the integration of advanced analytical capabilities.

Wealth Managers that succeed in fully exploiting data analytics opportunities can expect to achieve revenue uplifts of up to 20%. Revenue upside potential can be unlocked along the entire client lifecycle from improved prospecting and new client acquisition, to servicing existing clients better and improving retention rates. Data analytics empowers relationship managers and provides them the insights and decision making tools to enhance their value-add to the client relationship.

Figure 30: Upside levers of data analytics along the client lifecycle (not exhaustive)



Source: Oliver Wyman analysis

### Prospecting clients

Relationship managers rely heavily on their experience and networks when prospecting for new clients. The manual collection of information on prospective clients is a time intensive and cumbersome process. Few are leveraging advanced analytical methods to identify new client opportunities, foregoing the significant potential of existing client and third-party data to improve prospecting. Based on recent client work, we see that leaders in the data analytics field can increase their annual NNM by up to 50% based on targeted acquisition efforts and more successful lead conversion.

Figure 31: Analytics-driven new client prospecting



Source: Oliver Wyman analysis

Advanced data analytics can aggregate and interpret data from a variety of sources, cluster potential leads into groups with similar characteristics and compile profiles of individual prospects. Firms have begun to adopt a more data-driven approach to prospecting new clients. Usually, they are not tapping more than a handful of sources, but we have observed best practice firms leveraging third-party solutions that can combine external sources in the range of hundreds. By incorporating external data sources, relationship managers can identify potential leads way beyond their current sphere of influence.

Wealth Managers seeking to attract new clients can already today easily generate a longlist of potential leads based on data of merchants such as LinkedIn or Crunchbase. In the future, intelligent data analytics tools aggregating a whole host of external data will be able to effectively identify clusters of prospective clients sharing similar characteristics (e.g., CEOs of companies of a certain size owning yachts) or help build detailed profiles of

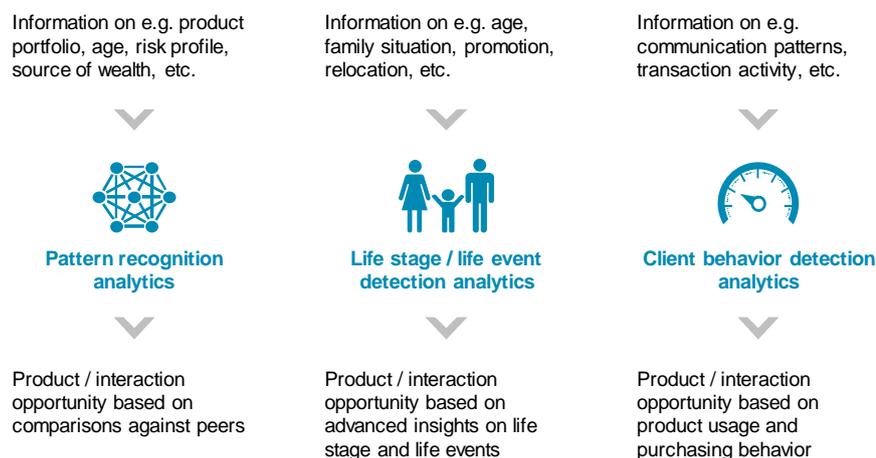
individual leads, and suggest product or service offerings tailored to the specific needs of the group or individual. Wealth Managers can then target select clusters directly through active or passive marketing, e.g., through real-time web advertisements restricted to specific groups only.

### Servicing clients

Many client opportunities today are still generated following a product-centric approach with relationship managers recommending “en vogue” products to a broad group of clients that might be interested. In view of the limited time and the increasing number of investment options, only few Wealth Managers have adopted a client-centric approach offering tailored products based on the specific needs of individual clients. Deploying data analytics when servicing existing clients can help exploit the untapped revenue pools of a more client-centric offering.

Standard in retail banking, the introduction of “Next Best Action”-tools for relationship managers can significantly increase share of wallet. We anticipate three major use cases of data analytics enhancing the servicing of existing clients, particularly by providing impulses for interaction or product recommendations: peer-group pattern recognition analytics, life stage or life event analytics, and client behaviour detection analytics.

Figure 32: Possible applications of analytics to service existing clients



Source: Oliver Wyman analysis

**Pattern recognition analytics:** Prescriptive tools, which use regression models, identify and analyse specific client clusters to uncover cluster-specific patterns. This reveals opportunities to make targeted product recommendations to clients fitting or deviating from the identified pattern. Data analytics may identify that a certain type of client with a shared set of characteristics follows a specific pattern, e.g., male UHNW with a background in financial services shifting from equities into fixed income as signs of a market downturn intensify. This can be used to make targeted recommendations to a different group of clients with a high propensity to follow the moves of the first group.

**Life stage / life event detection analytics:** Information on individual clients’ life stage and life events can be analysed to detect sales opportunities. For instance, information on the client’s family situation can be aggregated to anticipate important life events and provide interaction impulses to the

relationship manager. Data analytics enables Wealth Managers to aggregate and analyse vast amounts of information and gain crucial insights, rather than relying on advisors' intuition and direct client interactions. Accessing social media data, for example, could provide information on the relocation of a client's daughter, who is entering university. This can be used to initiate a conversation on student loans or real estate financing solutions. While the use of social media data is currently under scrutiny, following data privacy concerns, we believe that the opportunity will remain even following new and stricter data privacy and data sharing consent standards. As another example, aggregating information from news and career networks may indicate an increase in available income due to a promotion, which can be used as a trigger to re-evaluate the overall asset allocation.

**Client behaviour detection analytics:** Analytical tools enable Wealth Managers to extract valuable insights from behavioural client data such as transaction activity, the frequency of interactions with the relationship manager, or activity in online accounts or on the website. Predictive models, analysing historical and real-time behavioural data, help to identify patterns that allow Wealth Managers to anticipate clients' next moves. Based on this, relationship managers can proactively initiate client conversations and recommend actions. For instance, a client always contacts their relationship manager the day after their company releases its quarterly earnings report. The Wealth Manager can then proactively initiate contact upon the next release date, giving the client a sense of security and increasing client satisfaction.

**Case study: Amazon's success with data analytics**

Amazon successfully employs advanced analytics to derive personalised product recommendations based on data from previous product purchases, searches, reviews, shopping carts, wish lists, etc. For example, "frequently bought together" recommendations increase average order value from up- and cross-selling. Similarly, Amazon leverages data analytics to optimise its prices based on a variety of real-time factors including the customer's activity on the website, competitor pricing, or the expected profit margin. Product prices are adjusted frequently to capture the customers' maximum willingness to pay. According to expert estimates, the application of advanced analytics allows the company to generate a 30% revenue uplift from product recommendations and a 25% profitability uplift from optimised pricing.

**Retaining clients**

Today, relationship managers largely rely on their instincts or major risk indicators, such as a significant asset withdrawal, to identify clients at risk. Diagnostic and predictive analytics can complement existing risk indicators by deriving yet undetected indicators hidden in behavioural patterns.

Information regarding trading activity, communication behaviours, risk attributes, or service issues of non-retained clients can be analysed to identify common indicators of attrition. Identified irregularities in the behaviour of existing clients are used to predict a client's probability of attrition. This enables the generation of watch lists for relationship managers and triggers alerts for customer dialogue, embedded in the advisor desktop.

Figure 33: Analytics-driven attrition risk monitoring



Source: Oliver Wyman analysis

#### Case study: Churn reduction in Telco

Several examples from the telecommunications industry have demonstrated a possible reduction in churn rates by more than 20% within one year through the development of more sophisticated retention systems based on data analytics.

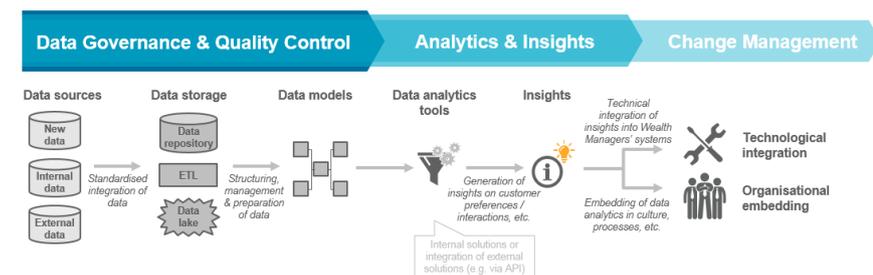
For example, a South European Telco client employed predictive algorithms to identify customers with a high churn likelihood based on e.g., calls to customer service or calls received from competitors. Customers at risk were routed to a retention platform where they were provided with both proactive and reactive retention measures including special offers such as financed handsets, special discounts, or migration offers to more suitable plans. The company used ad-hoc reporting tools to monitor results in real time, including information on e.g., targets, contactability, acceptance, etc. Given its great success, the churn reduction program was subsequently extended to a “Next Best Action”-tool for existing customers.

Across all three use cases along the client life cycle, Wealth Managers can also leverage data analytics to optimise their pricing. Some Wealth Managers have driven efforts to improve their pricing but significant potential remains in employing dynamic product pricing according to individual client’s price sensitivity. Data analytics can help with dynamic loan and deposit pricing. Prescriptive analytics leverage client data and historic transactions to determine the optimal pricing based on, for instance, price sensitivity, product preferences or competitors’ pricing.

#### To date, Wealth Managers are not ready to fully capture the analytics opportunity

Wealth Managers have started to build out their data analytics capabilities but no firm has fully captured the opportunity so far. Success has been limited by several challenges along the data analytics process. These need to be addressed to unlock the full potential of the opportunity.

Figure 34: Data analytics implementation process



Source: Oliver Wyman analysis

### Challenge 1: Getting the foundation right

Data governance and quality control form the basis for insight generating and value creating data analytics. Many Wealth Managers still struggle with getting their data architecture in order, resulting in significant gaps with respect to consistent and standardised collection, aggregation, and cleaning of data. Numerous firms have launched large scale re-platforming programs to harmonise their fragmented data storage across legacy IT systems, but their success in improving agility and generating IT savings has been limited.

A “capture first, sort later” approach to information management has led to the construction of vast data lakes overloaded with excessive amounts of unstructured data in various formats. Data lakes have been regarded as an alternative storage solution to legacy systems – instead, in many cases, they have turned out to be data swamps, not that different from the systems they were meant to replace.

Many firms have mistakenly looked at re-platforming to solve the issue but we believe data aggregation and preparation software can help to improve data hygiene already in the short-term. In the long run, existing technology relying on data warehouses will not suffice. Instead, Wealth Managers need to source or develop big data analytics technology capable of processing large amounts of data in such a way that allows for the deployment of advanced analytics.

The use of messaging protocols such as APIs, virtualisation, and other integration systems offer an opportunity to advance the overall data governance and prepare a data landscape that allows the effective integration of third-party data analytics point solutions (e.g., custodian-supported portals and dashboards for the front office). APIs make it possible for originally proprietary data (e.g., from management information systems, customer relationship management tools, or other internal databases) to be shared with external parties and integrate third-party offerings using the same underlying data pool. This enables Wealth Managers to reduce dependency on complex in-house legacy systems and opens innovative ways of analysing data and delivering added value to clients.

### Challenge 2: Balancing internal legacy systems and in-house development with 3rd party solutions

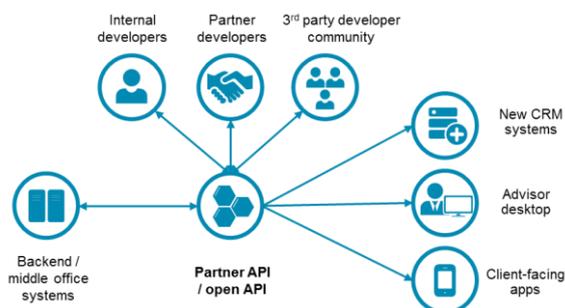
Successfully exploiting the data analytics opportunity requires the selection and integration of external data and tool providers. Wealth Managers face a dual challenge: Identifying the best partners in a fragmented market of point solution providers and creating interfaces to integrate external tools and data with their legacy IT systems.

Having defined the key business applications for analytics, it is important for Wealth Managers to specify the core analytics modules required to successfully roll out applications and pick the most suitable tools for the intended purpose. Developing a framework to seamlessly integrate in-house and best in class third-party vended solutions, such as “Next-Best-Action”- or dynamic-pricing-tools, is essential to accelerate revenue upside generation. This requires Wealth Managers to establish strong sourcing and partnering capabilities.

Moving to API-driven platforms and gaining comfort with partner APIs, Wealth Managers can leverage a broad range of open source and proprietary solutions to enhance their data analytics capabilities. Leveraging an external community for additional data and new application development can extend client reach, improve innovation speed, reduce infrastructure and development costs as well as dependency on legacy systems.

At the same time, it will be key to select those providers who have managed to create a key competitive edge. While in the past combining 2-5 third-party data sources was industry leading, the barrier has already shifted towards integrating hundreds of data sources.

Figure 35: Key API elements (not exhaustive)



Source: Oliver Wyman analysis

### Challenge 3: Successfully embedding new capabilities into the day-to-day life of Relationship Managers

Finally, Wealth Managers must ensure that key operating model requirements, such as governance, talent management, policies, and processes are in place. Low user acceptance and utilisation rates, particularly by relationship managers, are a key road block to unlocking the full value of existing and future data analytics applications. The Wealth Management industry has historically been more hesitant in embracing change compared to other industries.

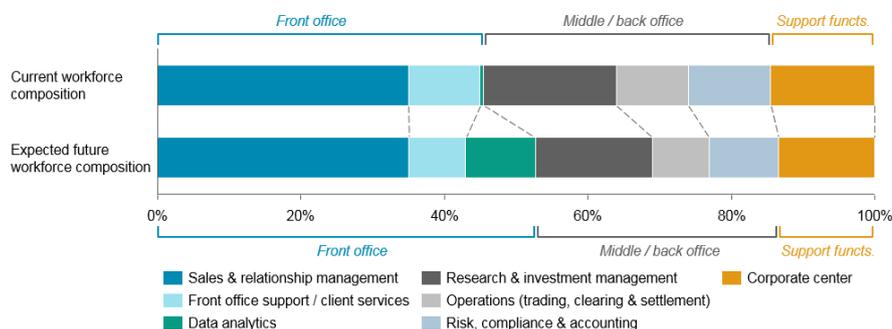
Change management is crucial to realise the full potential, focusing on underlying culture, user acceptance, and ease of use. Wealth Managers must cultivate a data-driven culture emphasising accessibility and use of sophisticated analytics by all stakeholders across the organisation. Management leading by example and revised incentive structures are key to foster acceptance. Future users must be closely involved in the development phase to shape functionality and user friendliness. Insights and recommendations must be seamlessly integrated into advisor workflows, providing a superior user experience. At the same time pilots to showcase early successes will be key to create a pull effect across the front of the house.

## Adapting talent management to address emerging gaps for ~40% of employee skill profiles must be a CEO priority

~40% of Wealth Management employee skill profiles are about to change significantly

We expect the overall composition of the Wealth Management workforce will change significantly, driven by reductions in size and changes in skillsets. The number of data analytics jobs is expected to increase as this skillset increases in importance. The headcount in middle and back office functions will decline, primarily driven by automation. Relationship managers will continue to represent the largest employee population, acting as the face of the Wealth Manager to the client, albeit with an adapted skill profile and a higher demand for sales-driven “hunter” profiles.

Figure 36: Workforce composition of large Wealth Managers, current vs. expected, share of total workforce



Source: Oliver Wyman analysis

We project up to 40% of Wealth Management employee skill profiles to significantly change over the next 5 to 10 years, requiring up- and reskilling along the entire Wealth Management value chain and fundamentally impacting the future workforce composition. Some profiles will see an increasing focus on specific “hard”, or technical skills, such as market / product knowledge, programming or advanced modelling and statistics. Other job profiles – particularly in the front office – will continue to rely on advanced soft skills, such as relationship building and qualitative problem solving. New skillset requirements will also emerge because of the increased importance of data science and analytics. Skill profiles of jobs that face automation will increasingly shift towards supervision activities, only requiring human intervention in case of failure of automated processes, exception handling, or escalations. Routine operations-related jobs will disappear.

Figure 37: Expected change in skill profile along the Wealth Management value chain

New focus activities along the value chain (not exhaustive, in addition to current activities)		Change in skill profile
Front office	Sales & relationship management	<ul style="list-style-type: none"> <li>Utilisation of data analytics tools and resulting insights for prospecting, servicing and retaining clients</li> <li>Collaboration with data scientists to enhance underlying data analytics algorithms</li> <li>Provision of holistic, solutions- and goal-oriented advice instead of product-focused advice</li> </ul> 
	Front office support	<ul style="list-style-type: none"> <li>Supervision of automated support processes and client (self-)servicing</li> <li>Intervention in case of failure of automated processes and mitigation of escalated client inquiries</li> <li>Utilisation of data-driven predictive analytics to anticipate client support needs</li> </ul> 
	Data analytics	<ul style="list-style-type: none"> <li>Integration of external / development and improvement of proprietary state-of-the-art data analytics tools</li> <li>Close collaboration across the value chain to align business divisions' and support services' needs and requirements with development of proprietary data analytics tools</li> </ul> 
Middle / back office	Research & investment management	<ul style="list-style-type: none"> <li>Application of data analytics tools to identify trends and generate investment ideas</li> <li>Execution of algorithm-based portfolio construction, management, and reporting</li> </ul> 
	Operations (trading, clearing & settlement)	<ul style="list-style-type: none"> <li>Supervision of automated trading and payment processes</li> <li>Intervention in case of exceptions or failures of automated processes</li> </ul> 
	Risk, compliance & accounting	<ul style="list-style-type: none"> <li>Supervision of automated risk, compliance &amp; accounting processes</li> <li>Intervention in case of exceptions or failures of automated processes</li> <li>Advising front office support on risk, compliance and accounting issues</li> </ul> 
Support functions	Corporate center	<ul style="list-style-type: none"> <li>Supervision of automated processes (e.g. HR and Finance)</li> <li>Intervention in case of exceptions or failures of automated processes</li> <li>Enhancing automated processes with human overlay / observations</li> </ul> 

○ = Low change in skill profile expected    ● = Significant change in skill profile expected

Source: Oliver Wyman analysis

To close the emerging skill gaps, Wealth Managers will need to improve their learning and training efforts to upgrade existing employee skillsets. Skill gaps that cannot be closed through reskilling of existing employees will have to be addressed through new hires and an expansion of the partner- and vendor ecosystem.

**Case study: AT&T's Workforce 2020**

A recent large-scale workforce retraining initiative by the US telecommunications company AT&T showcases what companies can do to prepare for a skills transformation. The company first defined future skill profiles and identified gaps compared to its current workforce. The number of job profiles was reduced significantly, leading to a much leaner overall workforce structure with broader and more flexible roles. Presented with the new role landscape, employees were then encouraged to take responsibility of identifying their future options and developing their personal re-skilling plan. AT&T provided employees with a range of re-education opportunities through online courses, workshops, certifications, and degree programs, e.g., in computer science.

The initiative, which targeted approximately half of the company's 250,000 FTE, helped AT&T avoid costly replacements of employees in intensifying labour markets. Early successes can already be observed. Within three years, internal sourcing of science and technology jobs increased by more than 20%. Thousands of employees have completed individual courses to enhance their technology skillset and several hundred employees have enrolled in online Master programs. Looking at specific KPIs, it could be observed that within 18 months, product development time was reduced by 40% and time to revenue by more than 30%.

This needs to be treated as a top 3 CEO priority, as the required workforce transformation is of critical importance to future success. Wealth Managers who treat the workforce transformation as a simple HR issue will likely fail.

Going forward, we expect two workforce evolutions to be of standout importance for Wealth Managers: the emergence of data scientists as well as a refined relationship manager role.

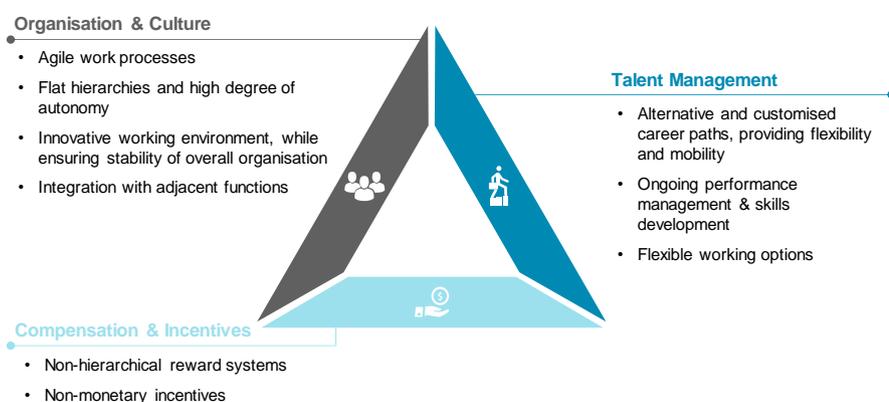
**Wealth Managers must participate in the data science war for talent – external partnerships become more important to fully close skill gaps**

The increasing importance of data analytics across industries has led to a recent spike in demand and recruiting competition for data scientists and engineers. All leading Wealth Managers we assessed are currently actively looking to fill data analytics-related jobs, such as data analysts or data scientists. As the importance of data analytics rises, Wealth Managers need to compete to attract data analysts, scientist, and engineers.

The financial services industry, including Wealth Management, is suffering from low popularity as an employer among this target talent pool. At traditional financial services target universities, the share of graduates joining financial services almost halved to around 25% between 2007 and 2016. At the same time, technology companies have more than tripled their intake to 20% of graduates.

Facing off against technology firms and the broader start-up universe, Wealth Managers need to sharpen their talent value proposition along three dimensions to attract data scientists and engineers: Organisation & culture, talent management, and compensation & incentives. They must establish a culture fostering agile working and innovation by granting a high degree of independence and, at the same time, ensuring close collaboration with adjacent business functions. Wealth Managers must tailor their existing performance management and explore flexible working options to shift away from traditional, management position-oriented careers and instead account for different career path preferences. Compensation and incentive frameworks will need to match these alternative operating structures including less hierarchical reward systems and a wider range of non-monetary incentives.

**Figure 38: Building blocks of a data scientist-focused value proposition**



Source: Oliver Wyman analysis

Gaps, that cannot be closed by hiring new talent directly, will see Wealth Managers seeking new external partnerships to access the required skillsets. As the workforce composition evolves and the Wealth Management value chain becomes more modularised, successful sourcing and collaboration with external partners will emerge as a significant driver of Wealth Managers’

performance. Improved access to external talent pools, including leveraging freelance work, will facilitate and accelerate innovation and allow Wealth Managers to align costs to the business cycle and to better manage employee turnover.

Firms should proactively leverage external talent pools to outsource technology and back office positions, driving leaner organisations and, at the same time, ensuring access to essential skills. Like internal resources, Wealth Managers need to offer an attractive value proposition to external resources, integrating them into the organisation and extending benefits such as learning and training opportunities. This increases loyalty and productivity.

**Relationship managers will remain the most significant employee population but access to “hunters” will be the real source of competitive advantage**

A fundamental transformation of the way Wealth Managers think about their relationship managers is required. Wealth Managers must re-assess their recruitment strategies to ensure access to critical front office skills.

The advancement of data analytics will reshape the activities and skillsets of relationship managers. As time-consuming routine tasks are increasingly automated, relationship managers will have more time to engage with clients. They can focus their activities on the acquisition of new clients, relationship building, and increasing the share of wallet with existing clients. A new mindset is essential to fully embrace the innovation brought about by new analytical capabilities. Problem-solving and personal accountability remain particularly relevant to excel in interactions with increasingly digital-savvy and well-informed clients. Wealth Managers must recognise that these skills will no longer be a “nice to have” but a critical differentiator in bringing value to clients.

The shift in activities will widen the divide between the roles of nurturing “farmer” profiles and sales-driven “hunter” profiles. “Farmers” with strong client management skills remain important to serve clients with an existing high share of wallet and low expected growth. This group of relationship managers will, for instance, leverage analytics-driven insights to enhance their account management efforts, i.e., catering better to the needs of existing clients. “Hunters” are needed to drive new client acquisition or increase the share of wallet with existing clients, thereby generating growth through NNM in times of decreasing asset performance. These relationship managers will deploy data analytics to generate up- and cross-selling opportunities for existing clients and drive NNM by targeting promising new leads with highly-customised recommendations.

In terms of recruiting strategies, Wealth Managers will increasingly need to tap into new talent pools beyond financial services to access the required talent, particularly sought-after “hunter” profiles. As asset performance is expected to decline and NNM becomes the primary source for Wealth Managers’ AuM growth, the demand for scarce “hunter” profiles will increase. Hiring from within the industry will often come at a significant price, driving Wealth Managers towards new sources of talent. Wealth Managers have become significantly more rigorous and selective in their recruiting efforts, burned by past hires based on books that failed to live up to expectations.

**Case Study: Declining relevance of relationship managers' existing client books in the US**

In the US, select high-profile firms have recently exited the protocol for broker recruiting. The industry agreement, which was signed in 2004 between major US financial institutions, had made it easier for brokers to change firms and limited lawsuits against brokers when they left firms. As a result, the industry-wide practice of generating NNM by hiring relationship managers from competitors will face strong headwinds going forward. Wealth Managers will increasingly focus on retaining their current workforce and increasing its productivity instead of large, costly recruiting initiatives. Alternatively, they may explore talent pools in other industries.

In exploring new talent pools, Wealth Managers must look towards industries that display distinct "hunter"-related characteristics, requiring similar sales-driven employee profiles and involving close interaction with high profile HNW and UHNW clients.

Figure 39: Potential "hunter" talent pools



Source: Oliver Wyman analysis

Exemplary talent pools Wealth Managers can target are luxury goods and services, hospitality, and lobbyists. Luxury goods sales staff, e.g., high end jewellery or private planes, often have the client understanding Wealth Managers are looking for and are accustomed to working with a HNW clientele. Hospitality professionals have been engrained with a customer-centric mindset and are familiar with close interactions with HNW clients. Lobbyists can leverage their highly trained communication and persuasion skills in client interactions.

With a host of challenges for the industry looming on the horizon, decisive management action is required now to make the necessary business model adjustments to stand out vs. competition. Investments into transversal capabilities of data analytics and workforce management will be a key differentiator to cement future success.

# Appendix 1

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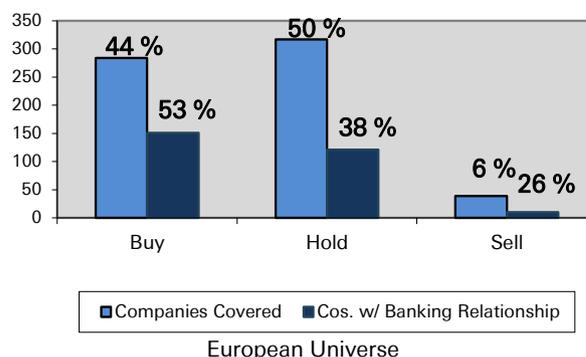
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