PRIVATE BANKING IN EUROPE – Getting Clients & Keeping Them!

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Abstract

The paper examines the features of private banking business in Europe and focuses on the key roles of client segmentation, retention and acquisition. There has been substantial growth in private banking business over the last decade or so as commercial banks have targeted both the 'mass-affluent' and more upmarket high net worth individuals (HNWI's). The combined amount of investable assets at the disposal of these two groups amounts to around Euro 6 trillion and a wide range of banks, investment firms and other operators have focused on devising strategies aimed at grabbing a share of this potentially lucrative market. The private client wealth management industry in Europe remains relatively fragmented although a few major players have emerged and consolidation is an ongoing theme in the sector. Given the commercial opportunities afforded by this business area the increased complexity of clients needs continues to be a critical strategic issue for industry participants. This paper illustrates important themes relating to the wealth management service proposition and focuses on client segmentation, retention and acquisition strategies. Overall we find that private banks will have to adopt a more systematic approach to these areas and in particular also have to pay greater qualitative and quantitative attention to client satisfaction, trust and loyalty issues if their client retention and acquisition strategies are to be a success.

Keywords

Private banking, wealth management, segmentation,

Introduction

Private banking concerns the high-quality provision of a range of financial and related services to wealthy clients, principally individuals and their families. Typically the services on offer combine retail banking products such as payment and account facilities plus a wide range of up-market investment related services.

Market segmentation and the offering of high quality service provision forms the essence of private banking and key components include:

- tailoring services to individual client requirements
- anticipation of client needs
- a long-term relationship orientation
- personal contact
- discretion
- investment performance

The market for private banking services has been targeted by many large banks because of the growing wealth of individuals and the relative profitability of private banking business. The CapGemini Merrill Lynch Wealth Report (2005)[1] highlights various features of the market for high net-worth individuals (HNWI's):

- 8.3 million people globally each hold at least US$1million in financial assets
- HNWI wealth totalled US$30.8 trillion, an 8.2% gain over 2003
- Wealth generation was driven by fast-paced GDP performance and moderate market capitalization growth
- HNWI wealth and population growth in North America outpaced those in Europe for the first time since 2001
- Singapore, South Africa, Hong Kong, and Australia witnessed the highest growth in HNWI numbers
- HNWI financial wealth is expected to reach US$42.2 trillion by 2009, growing at an annual rate of 6.5%.

An important feature of the private banking market relates to client segmentation which will be discussed in more detail later in the paper. The bottom end of the market is referred to as the 'mass affluent' segment – typically individuals who have up to $300,000 of investable assets. The top-end of the market are often referred to as 'ultra HNWIs' with over $50 million in investable assets and in-between lie HNWI's ($300,000 to $5 million) and very high HNWI's ($5 million to $50 million). Note that these definitions are by no means precise and different banks and commentators use various definitions for their own market

[1] CapGemini Merrill Lynch Wealth Report (2005) http://www.merrilllynch.com/media/48237.pdf

segmentation strategies. The level of service and the range of products on offer increases with the wealth of the respective client.

The number of HNWI ‘s tends to fluctuate in line with developments in the economy and global stockmarkets. Since 2001/2 the growth in the number of HNWI’s has been relatively slow in both the US and Europe. For instance, the population in Europe increased at a compound annual rate of 4.3% between 1998 and 2003, while the US growth has been only 1.7% over the same period. As noted by Datamonitor (2005)[2]:

> The worst year for these regions was 2002, when the population of high net worths in Europe fell by 6.7% to 3.3 million and in the US the population fell by a substantial 13.9% to 7.3 million. In the US however, the HNW population had been falling since 2000, while for Europe, this represented the only year of decline during the five year period. 2003 on the other hand has witnessed a great improvement in these markets. Over the course of the year the high net worth population in Europe reached 3.6 million individuals, representing an increase of 8.7% compared to 2002. In the US, the picture was also far more positive, with the high net worth population increasing 16.3% during the year to 8.5 million. (p.8)

There are an estimated 3.5 million European HNWI’s and these are believed to hold an estimated Euro trillion in 2003 (compared with the $7 trillion held by wealthy US individual) as shown in Table 1. You can see from the table that the mass affluent market in Europe (defined as individuals with up to Euro 300,000 in investable assets) constitutes an estimated 25.5 million individuals with a total of just under $3 trillion in assets to invest. It can also be seen that the size of the market has been growing somewhere in the region of 3 to 4% in recent years, and other forecasts suggest that this rate is likely to increase to around 5% up to 2008 leading to HNWI assets growing to just under $5 trillion by 2008. Germany has the largest market, followed by France, UK, Italy and Spain. During the 1990’s the Spanish HNWI market has been growing at the fastest rate.

[2] Global Wealth Predictions 2005 - What’s in Store for Wealth Next Year, Datamonitor, January 2005.

Table 1 Wealth Management Market in Europe, 1998-2003

Individuals (000s)	**1998**	**1999**	**2000**	**2001**	**2002**	**2003**	**CAGR**
HNW	2,898	3,180	3,338	3,523	3,286	3,571	4.3%
MA	21,865	27,595	29,059	26,258	23,828	25,522	3.1%
Total	**24,763**	**30,776**	**32,398**	**29,782**	**27,114**	**29,093**	**3.3%**
Liquid assets (EURbn)	**1998**	**1999**	**2000**	**2001**	**2002**	**2003**	**CAGR**
HNW	2,447	2,777	2,761	2,771	2,653	3,028	4.3%
MA	2,420	2,958	3,170	2,957	2,683	2,930	3.9%
Total	**4,868**	**5,735**	**5,931**	**5,728**	**5,336**	**5,958**	**4.1%**

Countries included under 'Europe': Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Netherlands, Norway, Spain, Sweden, UK

Source: Datamonitor's Global Wealth Model 2004 DATAMONITOR

Notes: MA = mass affluent defined as having investable assets of £30,000 and £200,000. (EUR 50,000 to 300,000).
HNW = high-net worth individuals have investable assets of greater than £200,000 (Euro 300,000)
CAGR = compound annual growth rates

Source: Global Wealth Predictions 2005, Datamonitor, January

A wide range of different banks and other financial institutions offer private banking services to HNWI clients. Table 2 shows a listing of major private banks taken. It can be seen that major Swiss banks such as UBS and Credit Suisse are represented – and this is not surprising as Switzerland is the global capital of offshore private banking business (where HNWIs have there investments managed by banks outside their home country). In addition, other large commercial banks have substantial private banking operations including HSBC, Deutsche Bank and Barclays. The table also shows that the top US investment banks such as JPMorgan, Goldman Sachs and Merrill Lynch also rank highly in private banking as do some lesser known Swiss banks (such as Pictet & Cie and Lombard Odier Darier Hentsch – '*If you have not heard of the latter – you are probably not rich enough to avail of their services!!!!*'). It is important to note that the (mainly commercial and investment banks) shown in Table 1 all deal with HNWI clients whereas it is really only the commercial banks that focus on the mass affluent market – where the latter differentiate services for their upmarket retail banking customers.)

Table 2 Top 25 global private banks by worldwide assets under management, Year end 2003

Rank	Company	Home country	Global AuM (€bn) 2003
1	UBS Wealth Management[1]	Switzerland	858.8
2	Credit Suisse Private Banking	Switzerland	329.2
3	Merrill Lynch Global Private Clients[2]	US	183.8
4	Deutsche Bank Private Wealth Mgt.[1]	Germany	162.0
5	Citigroup Private Bank[3]	US	158.6
6	Barclays Private Clients[4]	UK	155.3
7	HSBC Private Banking Holdings	UK	137.5
8	JP Morgan Private Banking	US	112.2
9	Morgan Stanley Private Wealth Mgt	US	105.7
10	ABN-AMRO Private Clients[5]	Benelux	102.0
11	Pictet & Cie	Switzerland	100.4
12	BNP Paribas Private bank	France	96.0
13	Bank of America Private Bank	US	85.0
14	Northern Trust Personal Financial Services[6]	US	84.8
15	ZKB Private Bank	Switzerland	75.9
16	RBC Global Private Banking[5]	Canada	75.1
17	Lombard Odier Darier Hentsch	Switzerland	74.0
18	Sal. Oppenheim	Germany	61.0
19	US Bancorp - Private Client Group[7]	US	55.5
20	Wachovia Wealth Management	US	52.7
21	Fortis Private Banking	Benelux	50.0
22	Credit Lyonnais Private Banking	France	46.5
23	Société Générale Private Banking	France	45.1
24	National Australia Bank Wealth Mgt.[8]	Australia	43.9
25	Union Bancaire Privée (UBP)	Switzerland	43.2

Notes: 1 Invested assets; 2 Assets in asset priced accounts; 3 Client business volumes under mgmt; 4 Total customer funds; 5 Assets under administration; 6 Managed assets; 7 Assets under custody; 8 Total funds under management.

Source: Datamonitor analysis of company accounts DATAMONITOR

Source: The Wealth Management Super League – Breaking Away from the Pack? Datamonitor, March 2005.

A similar listing of the 'Best Global Private Banks' from a Euromoney Survey (in January 2005) is shown in Table 3 - this is based on a survey of market and other participants. It can be seen that many of the private banks that appear in Table 2 and 3 are similar.

Table 3 Best Global Private Bank (Euromoney Survey, January 2005)

GLOBAL BEST GLOBAL PRIVATE BANK	
1	UBS
2	Citigroup Private Bank
3	Credit Suisse Private Banking
4	HSBC Private Bank
5	JPMorgan Private Bank
6	Goldman Sachs
7	Pictet & Cie
8	Deutsche Bank, Private Wealth Management
9	Merrill Lynch
10	ABN Amro Private Banking
11	Coutts & Co
12	BNP Paribas Private Bank
13	MeesPierson
14	Rothschild
15	Morgan Stanley
16	Société Générale Private Banking
17	ING Private Banking
18	Lombard Odier Darier Hentsch
19	Barclays
20	Union Bancaire Privée
21	Julius Baer
22	Nordea
23	Royal Bank of Canada
24=	Carnegie
24=	LCF Edmond de Rothschild

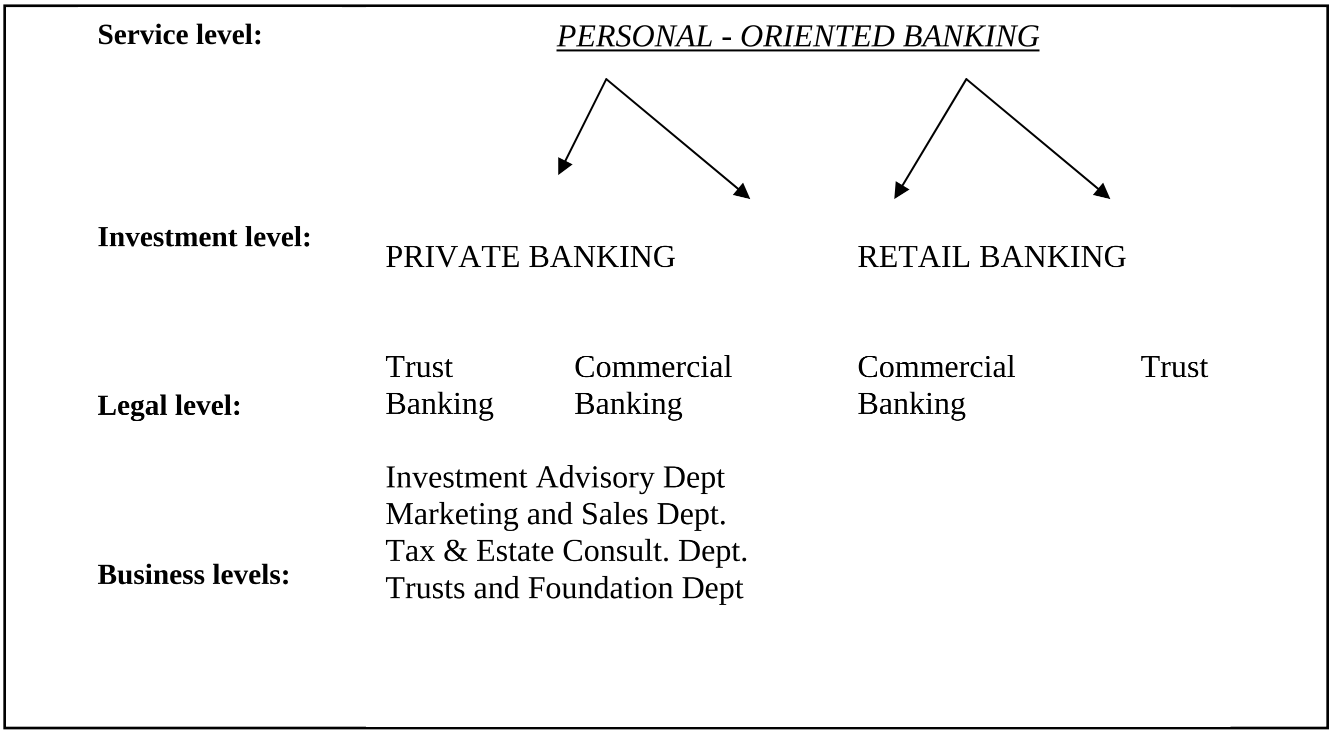
Source: Euromoney (2005) January

A key feature of the industry structure, however, is the general lack of concentration (especially compared with investment banking). For example, it has been estimated that the top 10 private banks in Europe manage around 20% of HNWI wealth, and within a country no player has more than 5% of the domestic private banking market. Note however that in Switzerland, UBS and Credit Suisse are major managers of offshore wealth – Switzerland being the capital of offshore private banking.

2. Relationships among Private Banking Institutions, Services and Clients

A precise definition of what constitutes private banking business is problematic as the product and service offering can vary considerably across national boundaries and also according to clients' needs. For instance, the state of the domestic economy, capital market performance, tax and inheritance laws can all have a strong influence on the types of services demanded by clients. In addition, the organizational structure (e.g. the set-up within a universal bank) of the institution that is offering private banking services can also determines the possible scope of services offered. In Switzerland, for instance, private banking services are provided through traditional private banks (like Pictet) and universal banks (such as UBS and Credit Suisse), whereas in the US and UK both commercial and investment banks are the main operators in the private banking market (although there are of course some specialist private banking firms although their role is as not as prominent as in Switzerland). In recent years various large European banks have emphasized the role of their private banking operations as major strategic units as an attempt to achieve a clearer segmentation of this line of business from other activities. However, there is still no clear cut way of defining the private banking offer for all banks as the products and services combine elements of both commercial banking and investment related business. As a result, the terminology "trust banking", "commercial banking" or "investment banking" are frequently applied to describe the business of private banking activities. Typically private banking forms a part of trust banking (in Japan, for instance, there are stand-alone trust banks that effectively do mass-affluent and HNWI business, and the main city banks all have trust divisions), and in many cases country-specific banking law determines in which division or part of the bank the "private banking" operations are to be located. (See Exhibit 1)

Exhibit 1 Private and Retail Banking Overlaps



In Exhibit 1 it is best to think of "private banking" as organizationally positioned from a market oriented view where this type of business focuses strongly on personal relationships with the clients, in contrast to an institution – oriented structure where the banks' services are not tailored to the needs of an individual person. Obviously, private banking and retail banking both belong to the personal-oriented service level specifically taking care of various customers' needs. While private banking refers to business aimed at high-net-worth individuals, traditional retail banking focuses on offering standardized products and services to a wide range of customers, where individual relationship is of less importance. One can think of mass affluent clients lying on a spectrum somewhere in-between retail and HNWI's.

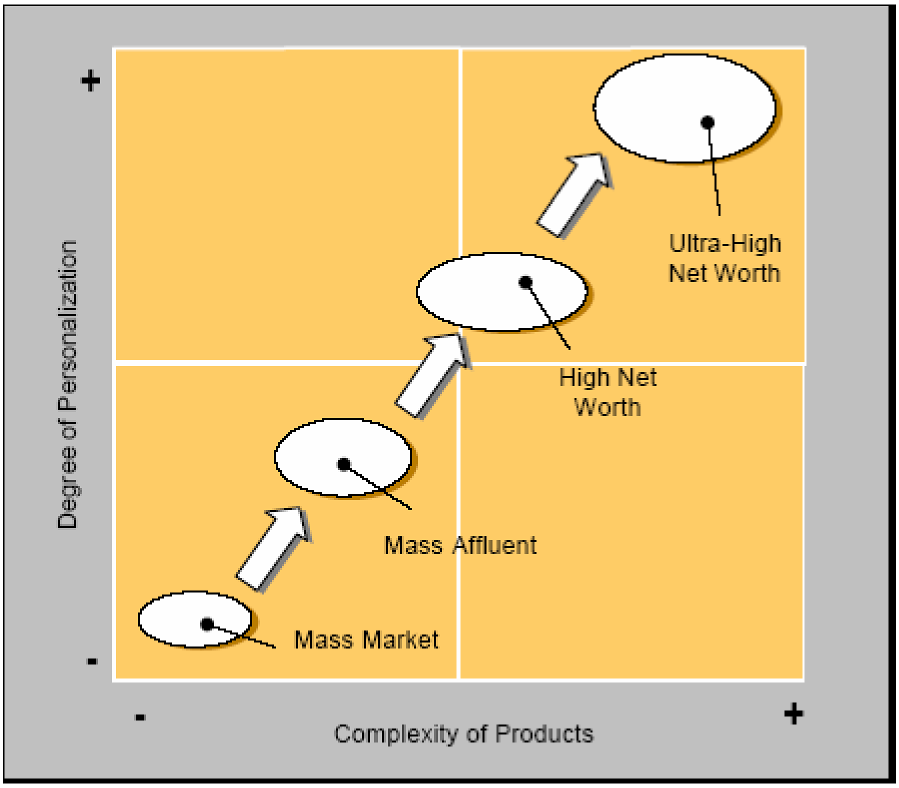
The striking difference between serving retail and private banking relates to the much wider range of products and supplementary services available to the latter, that include: portfolio management, investment advisory services, estate planning, trust services and tax advice. Many of these services tend to be frequently organized in separate departments within a bank. As such, the private banking offering tends to involve a variety of different parts of a bank and for HNWI services there tends to be a blurring of distinction between various banking and investment services and a strong focus on develop 'wealth packages' to meet the needs of clients. Integral to this offering is the client focus of the bank – does it aim mainly at the mass affluent market or focus on various types of HNWI? Closely linked to this is the brand image of the institution[3].

As has already been suggested, private banking business can most easily be distinguished by the wealth or income of clients being served. Traditionally, private banks catered for individuals having more than $1 million in liquid assets. With the growth of mass affluent banking over the last decade or so entry requirements have become more modest although there still remain private banking clients that focus on super wealth HNWI (like Goldman Sachs) where entry requirements are high.[4]

Not surprisingly, depending on the financial institution and entry requirements stipulated, the level and complexity of wealth management services can vary widely (See Exhibit 2). Note also that wealth management products need not only be provided by private banks. They can also be offered by a host of other firms including: universal, commercial and investment banks, trust banks, brokerage companies (e.g. securities firms), "financial boutiques", private banks (i.e. banks with traditional partnership structures), mutual fund companies, "special discounters" and "tailored ateliers", independent asset managers, intermediaries and life insurance companies. Exhibit 2 illustrates the types of firms offering private banking and wealth management services and the clients they typically target.

[3] Taylor, R.: Private Banking Renaissence, 1990, p.X.
[4] Maude, D. Molyneux Ph.: Private banking maximising performance in a competitive market, Euromoney Publications, Great Britain, 1996, p.46.

Exhibit 2 - Complexity and Personalization of Wealth Management Services



Source: Celent Communication, Wealth management market: capturing the hearts and assets of mass affluent Survey, Boston November, 2001, p.9.

Exhibit 3 - Types of private banking providers and their targets

Providers:	Presence		Service		Range		Targets:
	Local	*Global*	*Standardised*	*Personalised*	*Narrow*	*Wide*	
Category I:							
Universal /Commercial banks		X	X			X	Globale clientele
Merchant/investment banks		X	X			X	
Trust banks		x	X		X		
Traditional private banks	X		X			x	
Category II:							
Financial boutiques	X		x		x		HNWI's UHNW's
Ateliers	X			X		X	
Independent asset managers	X			X	x		
Intermediaries	X			X	X		
Category III:							
Mutual fund companies	x		X		X		Affluent
Life insurance companies	X	X	X		X		
Brokerage companies	x		X		X		
Special discounters	x		X		X		

X and x defines a different strength of the item: X means strongly related to the item; x weak relation to the item

Source: Adapted from Svend E., International Private Banking, Zurich, Verlag Paul Haupt, 1997, p.104.

The picture that evolves, therefore, is that private banking (or wealth management) industry is rather fragmented and is subject to intense competition. Traditional private banks vie with arms of commercial banks, investment banks, brokers, insurance companies and so on with a slice of the market. Like in other parts of the banking business, competition has increased putting substantial pressure on private banking participants to focus on managing their costs and revenue streams more effectively. The recent response to these pressures has been a significant degree of acquisition activity on the part of the largest wealth managers. The top Swiss banks, for instance, have acquired a significant number of relatively small, targeted, bolt-on acquisitions, mainly in the Asian markets and other acquisitions in the European onshore market (particularly in Spain)[5]. The consolidation trend is predicted to continue over the next few years.

Another interesting feature of the private banking business is that high net worth clients usually have multiple financial relationships. For example, a HNWI may have a relationship with his or her local retail bank for a simple checking account; with a full service broker for investment management; an insurance agent for life insurance and annuities; and a tax accountant for tax planning. The fact that private clients have multiple relationships means that suppliers of wealth management services are unlikely to have as complete a picture as they would like about their HNWI. This may make it difficult to leverage scale and scope economies from such relationships.

3. Customer Acquisitions and Retention

Client acquisitions, as well as, customer retentions are the main issues facing the wealth management industry today[6]. As the battle for new customers has intensified one resulting trend is that some wealth managers have become increasingly willing to waive their minimum investment thresholds for new customers, as we mentioned above. For example, in the US up to 50 per cent of private clients apparently fall below normally accepted minimum investment thresholds.[7] This situation occurred most noticeably during the late 1990's, when wealth managers sought growth through developing mass affluent market, drawing these clients into private banking services, and lowering their minimum account thresholds in the expectation of being able to cross sell products and services.

The desire to attract new clients in this manner has been justified by the view that that current wealth is not necessarily a good indicator of future wealth. Private client managers could build unprofitable current business with the prospects of these clients perhaps benefiting from inheritance or the sale of a company in the future. In addition, it is a fact that customer referrals from existing clients are one of the key means of client acquisition and some lower net worth clients may be valuable in terms of the customers they can bring in.

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[5] Datamonitor: Global Wealth Predictions 2005, pp.22-23.

[6]In accordance with Mercier Oliver Wyman: European Wealth Management Survey 2004.

[7] Datamonitor: Customer acquisition in wealth management Survey, September, 2002, pp-9.

While some of these reasons may justify taking on lower net worth clients this should be weighed against the potential risks. The widening gap between the wealthiest and least wealthy clients implies a growing range of client needs that might not be well served by a single service proposition. Having said all this, client acquisition and retention is obviously a key feature of private banking business. The private bank obviously has to make a realistic assessment that considers which customer groups are attainable and which are not and the bank has to balance the costs of providing high levels of services and face-to-face contact (associated with HNWI clients) with the lower revenues available from the mass affluent sector.

Targeting the mass affluent segment has been a strategy of many financial intermediaries over the last decade or so. However, the mass affluent sector has already lost some of its allure, with many competitors increasingly moving up the wealth ladder to focus on higher net worth individuals, particularly those that that emphasise a wider range and more personal service. Many institutions found attracting new mass affluent clients was too costly, and they failed to adapt their level of services to reflect the margins achievable, and consequently these clients failed to meet their profitability targets.[8]

But while some private bankers and wealth managers have chosen to go up-market to pursue wealthier clients, there are others, such as Barclays in the UK, that have responded to the difficult mass affluent market conditions by pulling out of this segment altogether and instead have focused on increasing share of wealth management with among existing customers. Adopting such a strategy involves carefully selecting the relevant client segment and services and convincing existing clients of the extra value they will receive from adopting a new (or at least different) wealth management product set. The correct segmentation strategy should aim to ensure that there is a balance between the costs of serving investors likely to generate lower income that are apparent in current operating environment.[9]

Having said this, however, mass affluent clients are an important proportion of many wealth managers client base and a successful model for mass affluent banking should be able to generate good reward for those managers are able to control costs, use technology effectively and manage lower service-level expectations. Wealth managers operating within retail banking groups are particularly well placed to succeed in this sphere by leveraging cross-sales based on their traditional retail operations. In this way they should be able to differentiate products for the mass affluent market and keep a tight control over costs and provide apparently proactive service, using technology.

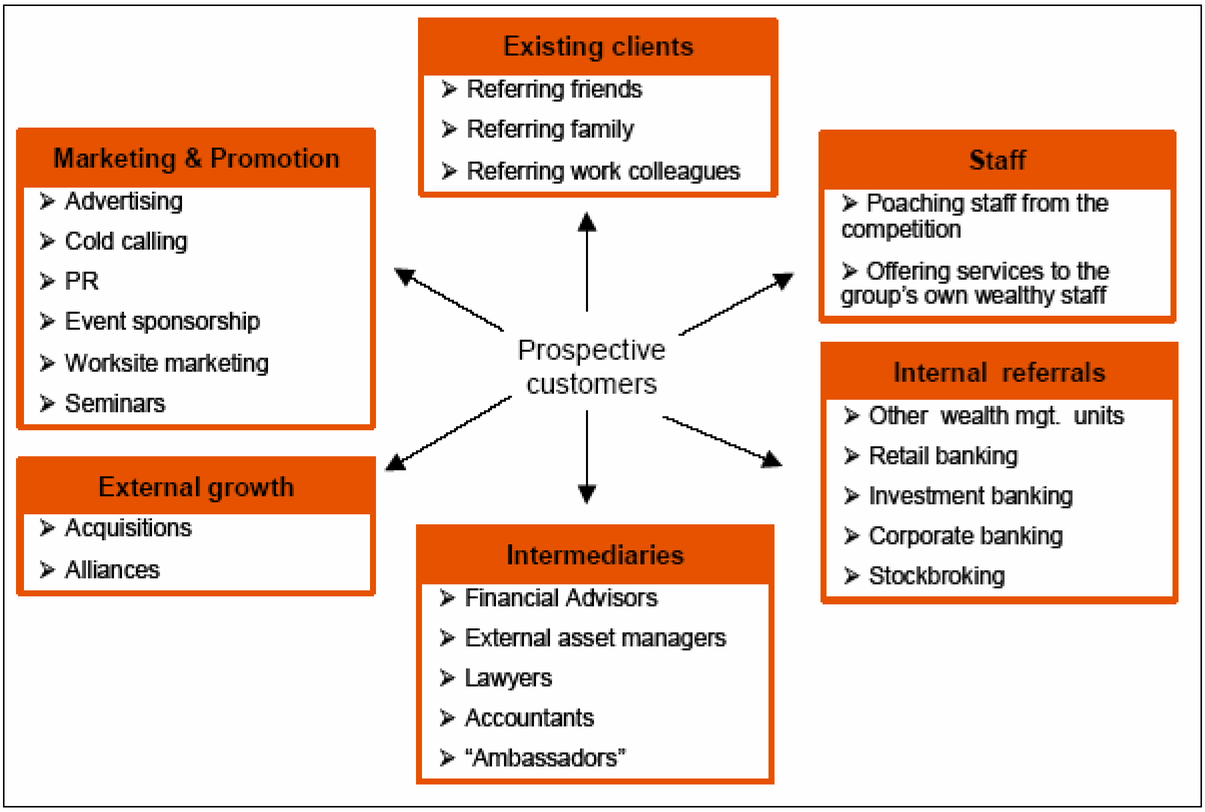
The identification of the mass affluent market was one (obvious) way that banks with large customer bases could develop private banking type activities and therefore generate greater fee and commission income.

[8] See also PriceWaterHouseCoopers: Competing for clients Survey, Spring, 2004, p.6.
[9] Datamonitor: Customer acquisition in wealth management Survey, September, 2002, pp. 10.

However, to a certain extent this involved 'Balkanising' their established customer bases. Wealthy retail clients could be enticed from one part of the bank to another, or cross-sold investment and other services through the branch or traditional channels. By and large, targeting the mass affluent customer has resulted in a restructuring part of traditional retail banking activity but in most cases (as far as we are aware) has not resulted in large-scale acquisitions of new wealth management clients.

In addition to re-segmenting established customer bases there are also a wide variety of other potential sources of prospective customers. The ability attract new clients, of course, depends on the bank's own internal capabilities as well as on various external opportunities. Various sources of prospective clients are illustrated in Exhibit 4.

Exhibit 4 - Sources of Prospective Clients



Source: Datamonitor: Customer acquisition in wealth management Survey, September, 2002, p.11.

Internal acquisition channels relate to the exploitation of the organizational structure including branches, representative offices, affiliates, as well as other business divisions. In the case of universal banks substantial cross-selling potential is available through services that can be provided via the corporate and investment banking divisions to wealth management clients. Having said this, however, there is little empirical evidence to suggest that the potential economies of scope and other cross-selling advantages that purport to be a major feature of universal banking have resulted in noticeable performance gains – especially with respect to the cross-selling of products and services to private banking clients.

A private bank can develop its client acquisition strategy by focusing on both organizational issues as well as placing a greater emphasis on marketing based activity. (See Exhibit 5). The marketing based approach focuses on acquiring clients via selling, promotional and various marketing activities. This approach, however, has been shown to not always be effective by itself in the short run because of difficulties associated with potential client recognition and skepticism associated with a relatively financially sophisticated potential target market. A marketing based approach has to be developed in conjunction with a reorganization of the business organization so that prospective clients can be offered value relevant product and service propositions. Once a successful framework for client acquisition has been identified (easier said than done) private bankers/wealth managers should aim to convert the prospect to client and then develop a strong focus on customer knowledge to innovate its own client propositions.[10]

Customer retention is obvioulsy an essential part of relationship development. The economic value of customer retention is widely recognised. It was found that customer retention has a more positive effect on profits than market share, scale economies and other variables that are commonly associated with competitive advantage.[11] The problem is that once customers are lost, they are difficult to regain.

Financial institutions need to strive to keep defection rates low and retention rates high. A high customer defection rate makes the market attractive to new entrants since it makes easier for new players to acquire customers. Low defection rates increase barriers to entry and make the market less attractive for new entrants.

Exhibit 5 - Sources of Client Acquisition

Organization-based:	Marketing activity-based:
Senior management personal network	Advertising
Branches, representatives offices, affiliates	Direct Marketing
Other divisions, i.e. corporate banking, investment banking	Cold calling
Co operations with complementary companies	Media events
Intermediaries (financial intermediaries, individual with a professional network, individual with a social network)	Sponsored events
Existing clients – word of mouth	Conferences, lectures
	Sales presentations
	Private luncheons
	Cooperation with third-parties, e.g. clubs, organizations
	Internal / external cross selling
	Purchase of addresses / mail shots
	Database marketing
	Internet access
	Franchising / white labeling
	Outsourcing peripheral services

[10] Mercer Oliver Wyman: European Wealth Management Survey 2004.

[11] Reichheld, F.F – Sasser W.E.: Zero Defections: Quality Comes to Services, in Harvard Business Review, Vol. 68, No.5, September/October, pp.105-111.

Source: Adapted from Svend E., International Private Banking, Zurich, Verlag Paul Haupt, 1997, p.124.

While there is strong agreement on the key issue of client retention, in practice it appears that there is too low an emphasis on client retention in the private banking/wealth management industry. According to the PriceWaterhouseCoopers Survey (2005) on private banking operators in Europe, nearly 46% of industry respondents stated that they had no client retention process, and moreover, remarkably few wealth managers even collected and took any action on direct client satisfaction information. Clearly, significant attention should be given to both of these areas by wealth managers if they are to avoid losing clients.[12] So if they want to retain customers they have to develop retention strategies.

One of the difficulties for wealth managers is that while they claim to understand their individual clients' financial needs, preferences and behaviour quite well, they often have no way of tracking these features systematically. So they are not so good at extrapolating the insights of their customers in terms of developing new products and customer propositions aimed at building retention.

A more professional retention – marketing –scheme should help strengthen ties and also help support cross-selling possibilities. But banks need to be able to examine the nature of existing relationships and investigate the possibility of providing services that add value for the client otherwise customers' requests cannot be satisfied and defections are likely to arise.

As customer loyalty declines with the growing presence of a wide array of service providers the issue of client retention becomes increasingly important.[13] To overcome this threat private banks and wealth managers can introduce a simple four-stage plan to foil defectors and boost retention rates.[14] The first step is to measure the current retention rate; then defection motives need to be ascertained; thirdly, an analysis of complaints / customer satisfaction issues need to be analysed and finally, financial institutions should attempt to erect barriers to customer exit. In this way wealth managers should be able to build on client retention helping to ultimately feed through into higher performance.

3.1 Loyalty and the Private Banking Relationship

[12] PriceWaterhouseCoopers: Global Private Banking / Wealth Management Survey, 2005, p.11.
[13] IBM, Wealth and Private Banking – Industry Survey 2003, IBM, London
[14] DeSouza G.: Designing a Customer Retention Plan, in Journal of Business Strategy, March/April, pp.24-31.

As customer loyalty weakens among private clients[15], various industry participants are looking to ways to enhance loyalty – one such response is the increased offering of differentiating lifestyle services. While lifestyle services may provide part of the answer to the loyalty issue they cannot substitute for getting the basics right in terms of understanding client needs, relationship management, investment reporting, product offerings and investment performance.[16]

In order to develop loyalty private banks have to be aware of the distinction between loyalty and trust. The word trust makes us think of how a person feels when he or she puts his/her trust in another one; it is the relaxed yet confident feeling a person or thing one can instil in another. On the other hand, loyalty refers to the precision with which we tend to our matters and keep our promises. The semantic origin of customer loyalty, therefore leads to two different meanings; one refers to a behavioural nature such as that of holding one's promises by making them come true while the other refers to an idealistic/cognitive nature reflected in believing/having faith/feeling sure about someone/something. Therefore, it is be best first to focus attention on client trust before attention is paid to customer loyalty.[17]

Trust has been analysed from several different perspectives (economic, sociological, psychological, and organizational) and this has led to a multidimensional understanding of the word. Therefore, there are many differing definitions of trust. Economists favour a view of trust based on calculations regarding costs and benefits (Williamson 1993). Psychologists commonly focus their attention on individual traits that lead to a trust-based relationship (Williams 1988; Rotter and Tyler 1990). Organizational theorists on the other hand, explore the role of trust in intra- and inter-organizational dynamics (Ring, Van De Ven 1994; Zaheer, Mcevilu, Perrone 1998). Sociologists study how trust can be woven into the network that ties interpersonal relationships between people and institutions (Granovetter 1985; Zucker 1986). For financial firms that wish to develop the trust of their clients a combination of the various aforementioned definitions are most likely to be used or emphasised.

Given that the trust of clients cannot be directly measured one has introduce and recognize those resources where customer's trust comes from. They are represented by a set of important variables such as image, client loyalty and relations created by the bank / institution throughout the years. Every company has its own 'trust resources' that are the result of its past history, which no other company can copy. The very nature of trust resources represents both a competitive and lasting advantage for a company. Trust can therefore be described as the middle link of a chain that foresees customer satisfaction in regards to what the company offers, and looks back on customer loyalty as shown in Exhibit 6.

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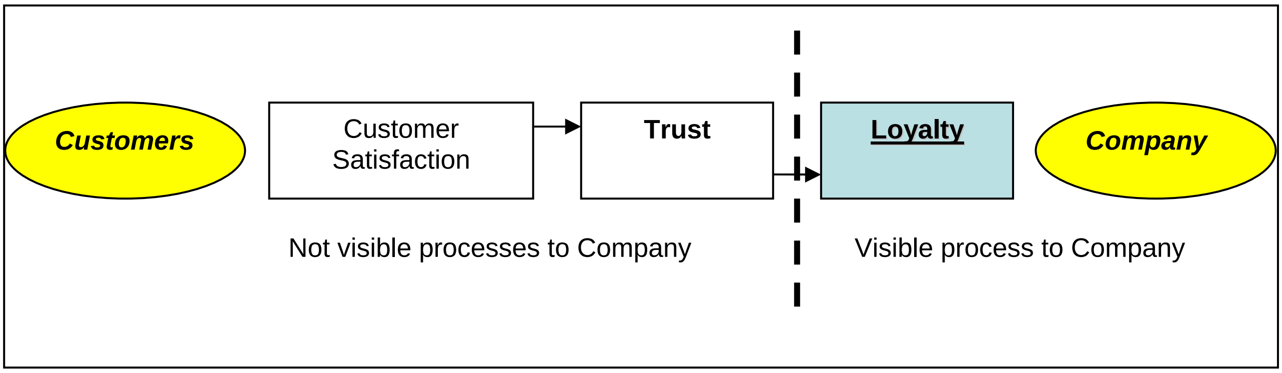
[15] See: IBM, European Wealth and Private Banking Industry Survey, IBM, London, 2005.
[16] On this issue see also: Coyles S – Gokey T. C.:Customer retention is not enough, in The McKinsey Quarterly, n.2., 2002.
[17] See also: Griffin J.: Customer loyalty. How to earn it how to keep it, Jossey-Bass, San Francisco, 2002.

Exhibit 6 - The Chain of Trust



Customer satisfaction engenders trust in the value propositions of a company, which then leads to enhanced loyalty and the perpetuation of the buying process. But as noted in Exhibit 6 customer satisfaction and trust are customer's internal features, so they are not visible to a bank unless it undertakes studies to identify the trust embedded in customer satisfaction assessments of clients.

The link between trust and loyalty then has to be evaluated. Loyalty has two different meanings: first, it can refer to a behavioural nature such as holding one's promises by making them come true, while the second refers to an idealistic/cognitive nature reflected in believing/having faith/feeling sure about someone/something. For client retention purposes (obviously) the latter is the most important. Difficulties in measuring loyalty can arise as bankers typically assume that retention of clients equals loyalty - but there is no clear guarantee that because, say retention rates increase, that the private banking service offering is a reflection of any enhanced faith by clients. For example, clients retention may increase because of greater market uncertainty or volatility, or be confused about the complexity of alternative product offerings and so on.

This turns to be of some importance for managers because it suggests that existing measures of loyalty may be seriously flawed, and thus strategies developed on the strength of such measures may be inadequate. The very term loyalty implies commitment rather than just repetitive behaviour, which suggests that there is a need for a cognitive as well as a behavioural view. This has led many bankers to use various customer satisfaction measures as a proxy indicator of loyalty because it has been assumed that satisfaction affects buying intentions in a positive way. However, research indicates that it is overly simplistic to assume that dissatisfied customers will defect, and that satisfied customers will remain loyal. Indeed, despite being "satisfied" or "very satisfied" many customers still defect. Therefore there are two things to consider: the first is that attitudinal measures of satisfaction are poor predictors or measures of behaviour, and second, it casts some doubt on the concept of 100 per cent loyalty.[18]

When furthering our understanding of the word loyalty in private banking/wealth management industry, we have to face the fact that it is made up of two main assets. There are*:*

1. The image of the bank, as far as trust is concerned, is represented through the esteem, and the familiarity that the customer might summarize by saying: "I can trust my bank"
2. The coherence between bank image and behaviour, from which we may gather what relation exists between promising to place money in the bank and the bank keeping the promise to manage this money in an appropriate manner.

Customer loyalty, thus, is the result of a reciprocal relationship, in which there is some kind of equal exchange of interests; we can infer that in order to ask for/obtain loyalty it is necessary to offer loyalty.

As far as we are aware little work has been undertaken on customer loyalty measures in private banking / wealth management and either:

a. the value of trust; or
b. the value of user satisfaction which includes customer behaviour - his/her experiences with the private bank/wealth manager in terms of service, communication and access.

The former is represented through the ideal aspects of loyalty such as identity and the bank *brand* value. The current situation demonstrates that longstanding brands tend to survive thanks to their prestige; the new ones have not had time to consolidate themselves, while, there are some other brands that can rise in the consumer's mind such as those related to new value propositions proposed by brokers, wealth boutiques and so on.

So far much of what has been discussed focuses on loyalty from a clients perspective but it is important to remember that in bank jargon "loyalty" is often used as a synonym for *cross selling* and *retention*. Bankers generally view the degree of customer loyalty as the extent to which the customer turn to other providers to obtain services. Using this sort of definition the difficulty lies in identifying whether loyalty is an attitudinal or a behavioural measure. Used loosely, as it usually is, the term "loyalty" conjures up various notions of affection, fidelity or commitment[19]. As we have already mentioned, this has led to the use of customer satisfaction as a proxy measure of loyalty because it has been assumed that satisfaction affects buying intentions in a positive way. However, research indicates that it is overly simplistic to assume that

[18] Omarini A.: Customers, retail banks and loyalty schemes, in EfmaGazine (on coming).

[19] McGoldrick and Andre, 1997, p. 74.

dissatisfied customers will defect, and that satisfied customers will remain loyal. Indeed, Reichheld (1994) found that despite being “satisfied” or “very satisfied” many customers still defect.[20] Then the very term loyalty implies commitment rather than just repetitive behaviour, which suggests that there is a need for a cognitive as well as a behavioural interpretation of the meaning of loyalty and more effective measures need to be developed to take this into account.[21]

Developing an affective commitment to both analyzing and promoting client loyalty is key to retention. In order to building loyalty private bankers / wealth managers need to act in an increasingly pro-active manner by investigating such things as: word of mouth recommendations, customer’s purchase intentions, customer’s price insensitivity and complaints (as well as procedures for dissatisfied clients). Once these are effectively analyzed then the private bank can focus on the issues of trust and loyalty.

4. Customer (Re-) Segmentation

The former features neatly lead onto some of the justifications for segmenting the HNWI customer base and the criteria used to differentiate clients. From the bank perspective, segmentation is all about maximizing value from every customer; so customers will pay more if they feel the product offering provides something special to them. This is particularly important in the context of private banking, as essentially the business model is based on the premise of high value clients and tailored services. Private banking clients, of course, have to value the service proposition on offer in both financial and psychic terms.

While a substantial proportion of retail banking and investment services are provided on a transactions basis private banking is relationship orientated. Clients and the wealth management proposition are heteregenous in nature. Despite this fact, clients of a private bank are often lumped together as one client group and do not always receive the tailored services they are promised at the outset of the relationship. True they receive more individual attention, but their relationship manager has to be able to focus on a number of clients (however small) with very different needs and lifestyles. This can result in homogenisation of the product and service delivery mechanism that has the effect of not meeting client’s needs. The following section outlines features of the segmentation strategy of private banks.

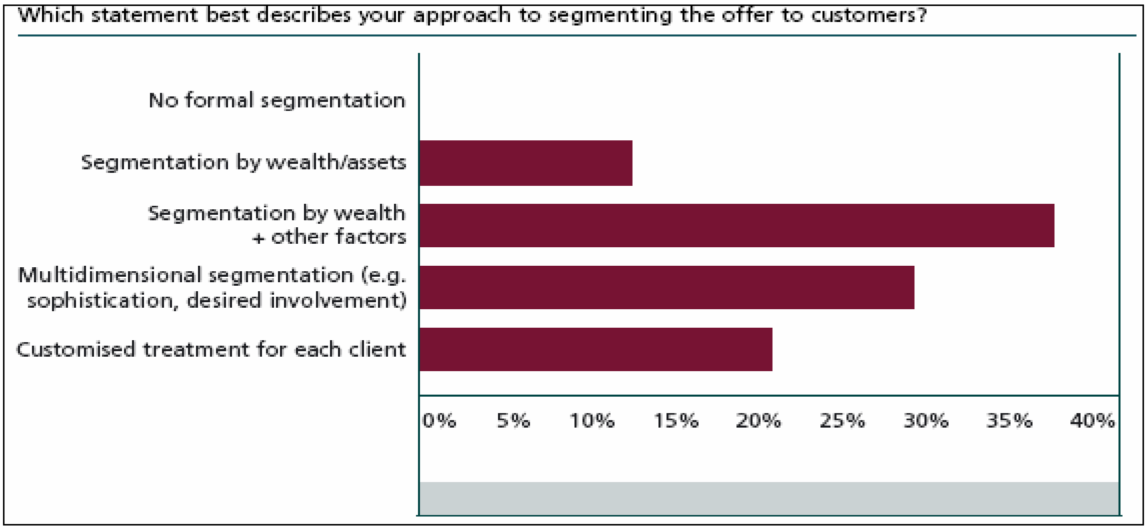
4.1 Ongoing Practices in Segmenting the Customer Base

In most cases wealth management customers are segmented by geography, demographics, wealth, income, asset class holdings and preferences, domicile, and so on.[22] But these criteria are becoming an inadequate

[20] Reichheld, 1994, p.45.
[21] Assael, 1992, p. 89
[22] See Maude, D. – Molyneux Ph.: Private banking maximising performance in a competitive market, Euromoney Publications, Great Britain, 1996, pp.49-51. And PriceWaterhouseCoopers, Global Private Banking/Wealth Management Survey, 2005, p.10; Mercier Oliver Wyman: European Wealth Management Survey 2004, p.19.

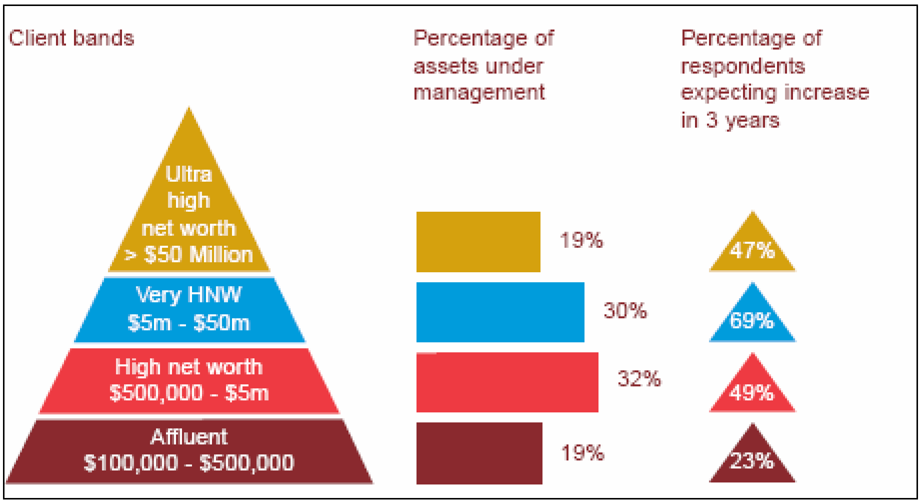
denominator for customers' requirements as indicated in Exhibit 7 where it can be seen that customised segmentation for clients are being developed. However, it is still commonplace for clients and service offerings to be simply segmented on their level of wealth as shown in Exhibit 8.

Exhibit 7 How European Wealth Managers Segment Their Clients



Source: Mercer Oliver Wyman European Wealth Management Survey 2004, page 16.

Exhibit 8 - The Wealth Management Pyramid



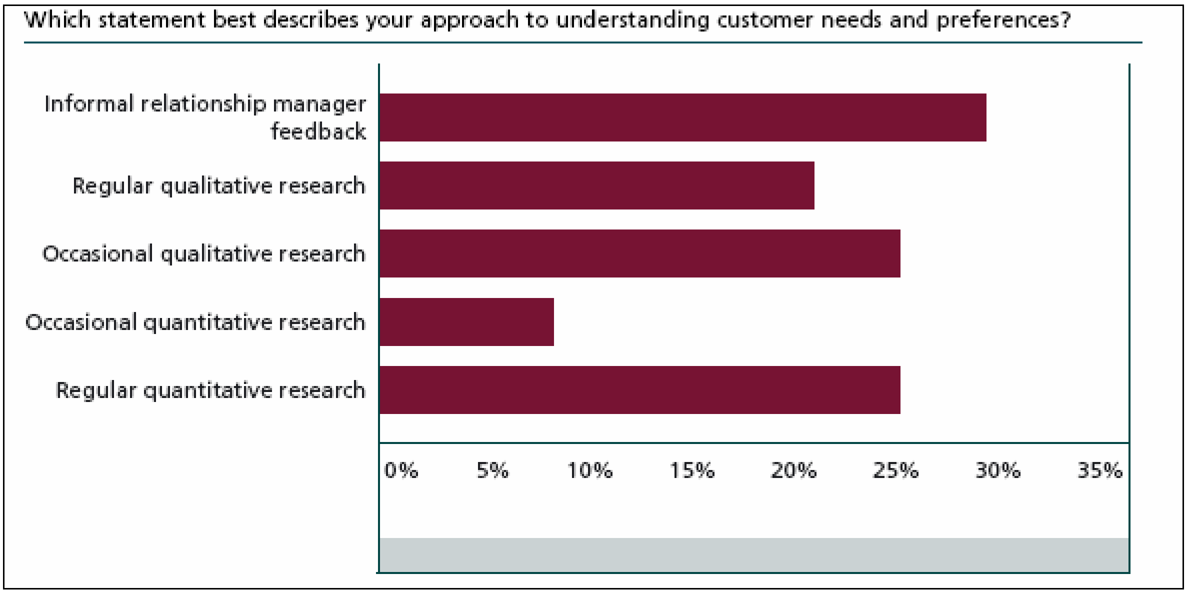
Source: PricewaterhouseCoopers, Global Private Banking / Wealth Management Survey, 2005, p.10

Other widely used segmentation strategies focus on the source of wealth (e.g. inheritance, entrepreneurial activity etc) and the risk preferences of clients. These ongoing practices outline a general lack of sophistication in the client segmentation process. As far as we can gather few wealth mangers analyse individual client relationship profitability, demand elasticity of products and/or regular structured studies aimed at enhancing their client propositions or marketing techniques. A recent report[23] provides further

[23] Mercer Oliver Wyman European Wealth Management Survey 2004, p. 15.

evidence on the limitations of European wealth managers approaches to identifying the needs of their clients. The report found that only one third of respondents to a survey of wealth management firms said they undertook quantitative research into customer needs and preferences: see Exhibit 9.

Exhibit 9 Understanding Client Needs in Wealth Management



Source: Mercer Oliver Wyman European Wealth Management Survey 2004, page 15

Wealth managers do not always make good use of the information they already have about their customers. For example, the Mercer Oliver Wyman survey on European Wealth Management (2005) noted that survey participants said that their customers were more interested in service level, brand, privacy and "peace of mind" than in superior investment performance. But even if this ranking is broadly correct, many wealth managers still continue to sell themselves on their investment offering and performance rather on other valued characteristics of service: so their current marketing is failing to exploit existing insight into customer preferences. This again suggests that much of the industry still works with relatively basic models of clients' needs, such as segmentation by wealth level or risk aversion.

At present, a single segmentation scheme used for both institutional and private clients is based on the concept of ‘clients' professionalism’. A sophisticated client “buys” products and solutions; an unsophisticated client is “sold” products and services. Of course, a wealth manager usually proxies wealth for sophistication but this (obviously) is not necessarily the case. However, there has been a move by some of the larger private client wealth management firms to focus on the ‘buying side’ by bundling in an increasing number of lifestyle and other services – so the customer proposition is becoming a wider concept than the product offering alone. It is a promise to meet the clients' needs; the product is part of that solution, but not, in itself, the complete solution.

For instance, beyond the mechanical details of the service proposition (service intensity, frequency, coverage model and so on), and the asset classes and structure of investment management products, lie new selling opportunities in such underexploited areas as advice, delivery, ancillary services and branding, but also relating to developing new propositions, expanding product and service ranges to include non-traditional offerings such as tax, fine art and “concierge” services. As noted by the Mercer Oliver Wyman (2004) survey the vast majority of private bank / wealth managers - 85% - said they were still looking to grow their product range while the remainder 15% were seeking to shrink their range selectively. The survey also noted that all the approaches implemented in designing customer propositions were largely unscientific. Around a sixth of the survey respondents use only informal procedures to improve their customer offerings. A further two-thirds focus on propositions designed around segments (with or without individual customisation), but the segmentation scheme used is usually very simply based on wealth; and as a consequence the resulting client propositions appears to be no more than weakly differentiated.

3.2 Some New Criteria for Re-segmenting the Client Base

It should be apparent that the existing client segmentation strategies pursued in European private banking / wealth management are simplistic and do not appear to map accurately into client requirements. This is somewhat surprising given that bankers all know that an essential starting point for any financial services provider targeting HNWI’s is to recognize their diversity and the important influences this has on their product/service demands and behaviour.

Of course the diversity of the HNWI population is important at much more than a purely conceptual level. It has to be translated into a range of very different product and service requirements and sometimes wealth managers may not have the appropriate business models to meet exacting demands. Indeed HNWI’s appear to recognize their diverse nature much more than wealth managers. For instance, “Those people who have made money on a one-off opportunity and those that need to be consecutively successful with their investments have very different requirements”.[24] (Quote from an Australian HNWI)

As with any individual, background and situation have a significant impact on attitudes and objectives. This is especially true when it comes to managing financial affairs. Many clients’ requirements are not always born of practical choice, many are also based on individual interests and understanding. Furthermore there is

[24] Datamonitor: Customer Segmentation in Australian Private Banking Survey, March 2005, p.10. And see also: Datamonitor : Customer Segmentation in Singaporean Private Banking Survey, April, 2005.

the issue that complexity of service demands from individuals is often unique and increases with time and affluence. Various affecting the complexity of private client demands include:

1. Life choices. These relate to employment and lifestyle preferences or the undertaking of key life events such as marriage, retirement or divorce. One notable example would be the decision to live abroad, which often adds several complexities to a HNWIs' financial situation in terms of tax and legal status issues.
2. Investment/product choices. The greater the range of different asset classes and product categories into which clients place funds, the more complicated their management will become.
3. Provider choices. These include the quality, type and number of providers selected by HNWI's in arranging and managing their financial affairs. Similarly, the stronger the element of self-direction and control over finances the greater the complexity in handling their financial situation.

These features mainly focus on the financial aspects of client demand while there are other dimensions that need to be taken into some considerations. To finish off we propose a combination of segmentation approaches that we believe should be used by wealth management firms to more accurately identify client needs. These are illustrated in Exhibit 10 and emphasise segmentation strategies based on a combination of factors including:

1. Criteria based on the source of wealth
2. Criteria based on client needs and sophistication
3. Criteria based on the inherent advantages of lifestyle services
4. Criteria based on price sensitivity; and
5. Criteria based on customer value.

Exhibit 10 – New criteria for segmenting HNWI's

Criteria based on	**Description of sub-segments:**	**Advantages:**
Source of wealth	The different segments are identified in terms of different sources of wealth (winning it; earning it; inheriting it …)	This identifies similarities more effectively and is relatively easy information to obtain.
Needs and sophistication	The different segments are identified in terms of services to "non-professional" versus service to "professional" client segments	They have very different requirements so they should need different business models
Inherent advantages of lifestyle issues	Sub segments are identified in terms of value for customers such as trust, access, information …	Lifestyle issues must leverage on the existing segmentation strategies of the private bank to increase customer insight by monitoring the client's use of lifestyle services to glean knowledge of the clients behaviours and commitments in their general lives.
Price sensitivity	While pricing is one of the marketing mix variables it can also be useful to segment the market	Price differentiation can be an effective way of promoting areas of core and non – core competencies by offering different pricing models to different sorts of client. Wealth managers should be aware of the price sensitivity of product offerings.

Customer value	The sub segments are based on assessing the difference among a set of key indicators of value per customer (value of assets, value of liabilities, revenues, number of footings, duration of relationship, age …)	Identifying how value is distributed across the customer base can allow private banks to pinpoint the most attractive segments in targeting prospective clients and help to plan an approach to existing accounts by highlighting the priority areas/means by which it can extract additional value from its current clients.

5. Conclusions

The paper examines the features of private banking business in Europe and focuses on the key roles of client segmentation, retention and acquisition. There has been substantial growth in private banking business over the last decade or so as commercial banks have targeted both the 'mass-affluent' and more upmarket high net worth individuals (HNWI's). The combined amount of investable assets at the disposal of these two groups amounts to around Euro 6 trillion and a wide range of banks, investment firms and other operators have focused on devising strategies aimed at grabbing a share of this potentially lucrative market. The private client wealth management industry in Europe remains relatively fragmented although a few major players have emerged and consolidation is an ongoing theme in the sector. Given the commercial opportunities afforded by this business area the increased complexity of clients needs continues to be a critical strategic issue for industry participants. This paper illustrates important themes relating to the wealth management service proposition and focuses on client segmentation, retention and acquisition strategies. Overall we find that private banks will have to adopt a more systematic approach to these areas and in particular will also have to pay greater qualitative and quantitative attention to client satisfaction, trust and loyalty issues if their client retention and acquisition strategies are to be successful.

The issue of client segmentation is the most important issue for customer retention and acquisition. It will always remain a central theme of private banking and wealth management. In devising new segmentation approaches the question may arise '"where do you stop?" We would ague that, on the whole, the industry norm of using qualitative segmentation approaches based upon levels of wealth does not adequately address the issue of individual needs. There are a number of fundamental needs and sentiments that HNWI's have in common and we believe that these are not being appropriately gauged or addressed by European wealth managers.

Presuming that industry participants develop and use more appropriate client segmentation approaches the next challenge is to develop a business model that can effectively and efficiently meet the diverse demands of clients. There is much talk about 'open architectures' and flexibility in the business model, although it is by no means clear the extent to which such structures are used, especially by the top firms who produce most of their products and services 'in-house'. Various specialist areas such as hedge funds, trust and fiduciary services are often outsourced as are certain lifestyle services. Small firms, of course, are much more dependent on offering third-party services to their clientele. There is also increasing discussion of the major players as ‘producers’ and the smaller operators as ‘distributors’ of wealth management services – note the analogy can apply to different divisions within the same organisation. This distinction is likely to become more polarised in the future.

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