PRIVATE BANKING

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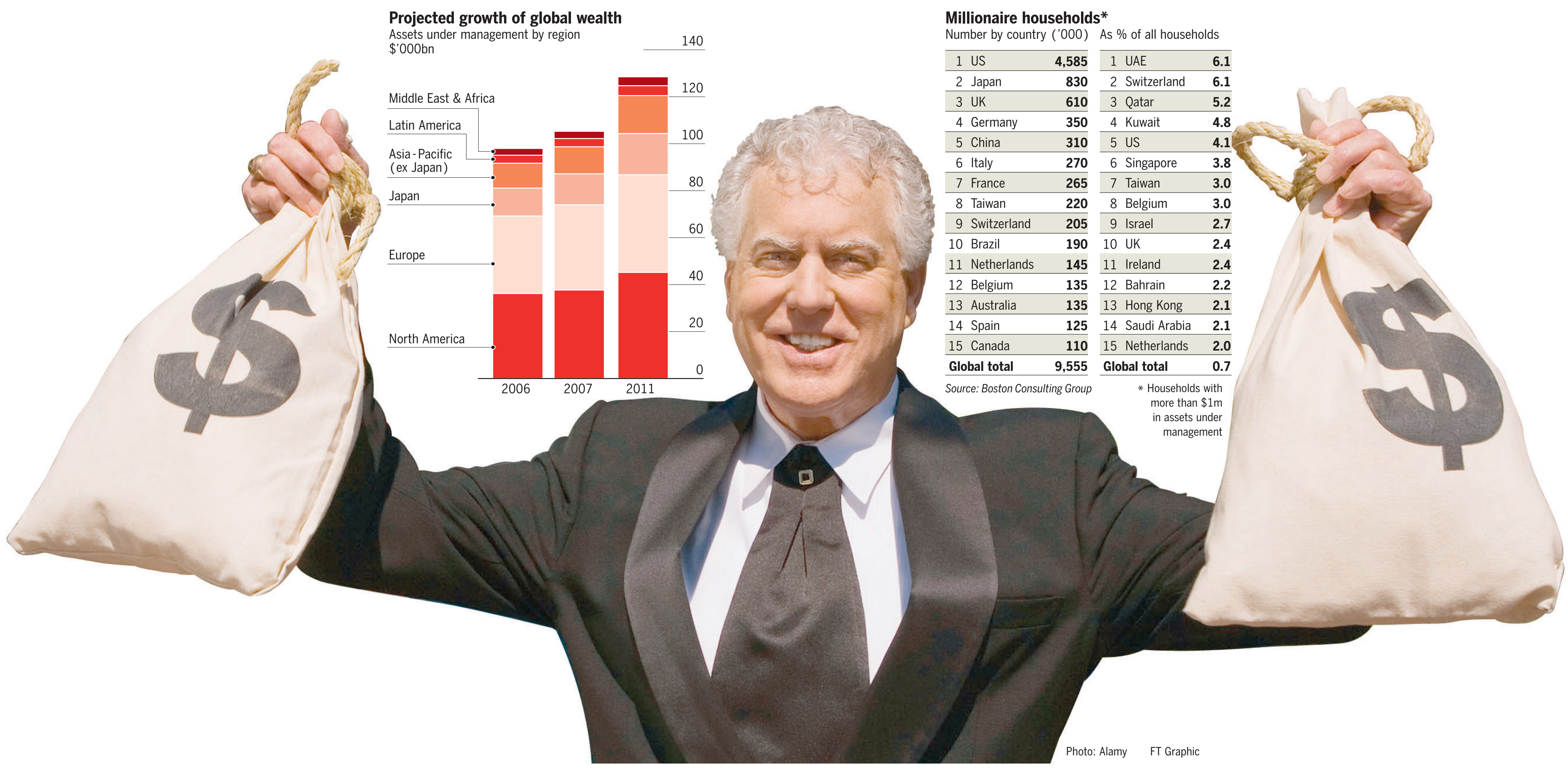

Millionaire households*

Number by country ('000)			As % of all households		
1	US	4,585	1	UAE	6.1
2	Japan	830	2	Switzerland	6.1
3	UK	610	3	Qatar	5.2
4	Germany	350	4	Kuwait	4.8
5	China	310	5	US	4.1
6	Italy	270	6	Singapore	3.8
7	France	265	7	Taiwan	3.0
8	Taiwan	220	8	Belgium	3.0
9	Switzerland	205	9	Israel	2.7
10	Brazil	190	10	UK	2.4
11	Netherlands	145	11	Ireland	2.4
12	Belgium	135	12	Bahrain	2.2
13	Australia	135	13	Hong Kong	2.1
14	Spain	125	14	Saudi Arabia	2.1
15	Canada	110	15	Netherlands	2.0
Global total		**9,555**	**Global total**		**0.7**

Source: Boston Consulting Group

* Households with more than $1m in assets under management

Photo: Alamy FT Graphic

Storms cause ripples in haven of calm

The industry has been affected by the turmoil elsewhere in banking, writes **Peter Thal Larsen**

Private bankers tend to keep a low profile. Yet since the credit squeeze started last year, the business has stood out as a haven of relative calm amid the turmoil in the global credit markets.

As investment banks have suffered heavy losses on complex credit products, the business of looking after wealthy people's money – for long viewed as the dull relative in the financial services family – has appeared increasingly attractive.

"Private banking is living up to its billing as the stable anchor," says Jeremy Marshall, chief executive of Credit Suisse's UK private banking arm.

What is more, the business continues to grow. Despite financial upheaval, the expectation is that the ranks of the very rich will continue to expand.

Oliver Wyman, a consultancy, estimates that the wealth controlled by high net worth individuals – those with investable assets of more than $1m – will grow by 9 per cent a year in the next four years. Although this is slower than the 11 per cent growth rate experienced since 2003, it will still be sufficient to propel the assets of the rich from $50,000bn today to $75,000bn by 2012.

This is not to say that the industry has been unaffected by the crisis. Turmoil in the financial markets has knocked the value of assets managed by private banks, leading to a reduction in management fees. Clients have also responded by buying fewer investment products, and by shifting their assets into cash, both of which are less profitable for private banks.

The uncertainty has made it harder for entrepreneurs to sell their businesses or float them on the stock market, choking off one of the main supplies of new private banking clients. Wealthy people, particularly in Asia, who relied on borrowed money to enhance their investments, have been forced to unwind some bets, further shrinking the assets managed by banks.

"The business has proven it has low volatility but is not immune from the economic environment," says Christian de Juniac, senior partner and managing director at Boston Consulting Group. "I would be surprised if there is a private bank that is currently hitting its revenue targets."

> 'Why should you put your money with an institution that can't manage its own money?'

The credit turmoil has also raised questions about those private banking businesses that are part of large institutions that have suffered heavy losses, such as UBS and Merrill Lynch. Some clients, spooked by what would happen if their wealth manager collapsed, have chosen to shift assets to other institutions. But the greater blow is to the banks' reputation as savvy money managers.

"It is fair to say: why should you put your money with an institution that can't manage its own money?" says Stefan Jaecklin, a partner at Oliver Wyman. "It's very hard to avoid that sort of question because it's fair."

The credit crisis has reopened a debate about the benefits of combining private and investment banking in one institution.

For several years, institutions such as UBS and Credit Suisse have trumpeted the benefits of combining the two, arguing that the businesses could introduce clients to each other while private banking customers would gain access to sophisticated investment products – particularly private equity and hedge funds – not available to others.

These benefits still exist: based on a study of leading institutions, Oliver Wyman estimates that as much as 7 per cent of investment banking revenues come from the private bank.

Chris Meares, global chief executive of HSBC's private banking arm, says commercial banking relationships with smaller, family-owned businesses not covered by large investment banks can also prove valuable.

"Our commercial banking presence is the sweet spot," he says. "The private bank will have close relationships with the owners of these businesses."

The question, however, is whether these benefits are outweighed by the risks that a large investment banking business will run, particularly in its proprietary trading operations.

So far, the main beneficiaries of the crisis appear to be smaller institutions that are not part of large investment banks and are therefore protected from subprime related losses.

This is particularly true at the upper end of the market, where wealthy families are increasingly setting up their own family offices, or relying on the advice of boutique firms that manage the wealth of multiple families.

"As things currently stand the trend is for a shift from big institutions to smaller

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Haven of calm amid turmoil

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ones," says Michael Maslinski, director of Maslinski & Co, a private banking consultancy. "The balance of power is shifting."

Nevertheless, it seems certain that large banks will continue to invest in expanding their private banking arms as they seek exposure to the fastest-growing parts of the financial services industry. The majority of this growth is expected to be in onshore markets as the authorities in the US and Europe continue to crack down on suspected tax evasion in offshore centres such as Liechtenstein.

Larger banks can also differentiate themselves by using their balance sheets to lend to wealthy clients. Though lending has not been a large part of the industry's recent growth, it is becoming more attractive as the credit squeeze makes it harder for the wealthy to find loans, particularly large mortgages or loans to finance the purchase of private jets.

"There is no question that there are opportunities in the market for lending," says Thomas Kalaris, chief executive of Barclays Wealth.

The question is how many institutions will have the patience to make the heavy investments required. Raoul Weil, chairman and chief executive of global wealth management and business banking at UBS, says it can take 10 to 12 years for a new office to mature fully in terms of attracting clients. "Some of our competitors with an investment banking background have different expectations in terms of paybacks," he says. "This business is based on a long-term franchise. Physically that takes longer to build."

This task is made even more complex by the fact that the vast majority of new wealth is expected to emerge from Russia, the Middle East and Asia – markets where the concept of private banking is less well established. As a result, banks are grappling with establishing a presence and with attracting sufficiently experienced relationship managers.

It is also far from clear whether these emerging markets will develop a fully-fledged private banking industry – where clients are charged a percentage of their assets each year – or move towards a US-style brokerage model, where brokers earn fees based on the transactions they make for clients.

For private banks, the former is much more profitable. "It still needs to be proven that high-growth markets such as China or Korea will offer the same attractive margins as the European trusted-adviser model," says Mr Jaecklin.

Nevertheless, given the attractive growth forecasts, it seems certain that the private banking business will attract an increasingly high profile in the next few years. The challenge for private banks will be to prove that – unlike the investment banking binge of recent years – it is possible for the industry to serve both its clients and its shareholders, and not just its employees.

Called to account: large financial services companies such as Citi have suffered heavy writedowns but their capabilities remain unchanged AP

A question for the wealthy

BUSINESS MODELS

Lauren Foster on the pros and cons of institutions' links

Many large financial institutions have in recent years sought to exploit the links between their private banking and investment banking arms. The idea was that a new generation of wealthy clients – entrepreneurs who had built their fortunes in business – wanted sophisticated products and access to expertise in corporate finance and investment banking.

It was a win-win situation – until the big writedowns at the investment banks showed this structure could expose private banks to significant reputational risk.

Now that the credit crisis has shone an unwanted spotlight on many banks, some private banking clients may be wondering: "Am I better off with a small, independent wealth manager or a private bank attached to a global investment bank?"

The answer has less to do with the size of the institution than its culture and capabilities. While the large banks tout the advantages of being global, having big balance sheets, and being able to create sophisticated products, the independent firms – whether small or large – argue that not having an investment banking division allows them to focus on what matters most: wealth management.

Rob Elliott, senior managing director at Bessemer Trust, an independent wealth manager in New York, says his firm is able to offer clients the same products that the big investment banks make available to their private clients, as well as the same services – be it investment management, philanthropy, tax and estate planning or family company advisory services.

"We're a client of those [investment banking] firms," he says. "Their products are available to anybody who wants to invest in them, whether it's structured products, or private equity, or hedge funds or credit. Our clients benefit from our ability to objectively compare the best offerings from Wall Street, without being limited to any one firm's products."

Sherry Barrat, president of personal financial services at Northern Trust, an independent financial services firm that focuses on institutional and family wealth, agrees. She believes that while investment banks produce "some great products and take companies public", there are distinct advantages to not having an investment banking division.

"The flipside when you are not attached to an investment bank is that while we still have access to their products, we don't have the conflicts that some view as inherent to that model," she says. "Our clients do not have to worry about us pushing product . . . there is that 'no-conflict objectivity' that goes with not being an investment bank. That is one of the main reasons we have not gone into that business in our 119 years."

At Northern Trust, which manages about $780bn, private clients comprise 42 per cent of revenues, while institutional clients generate the rest. This, Ms Barrat says, underscores that the firm's focus is on wealth management.

> 'Our clients do not have to worry about us pushing product'

While developing sophisticated products is one part of an investment bank's business, another is helping owners of private businesses float or find buyers.

Mr Elliott brushes aside the notion that private banks attached to investment banks have a built-in advantage in this area.

"We don't execute a transaction, but on a very objective, unbiased . . . basis, sit down with a family business owner and say: 'You've done a great job, you've built this business to $50m – do you want to keep it going? . . . If an exit is the right thing for the family, or a partnering agreement that takes some money off the table, we'll help you get it done'." Bessemer will then help the family identify a suitable investment bank for the work.

By contrast, a large financial services company such as Citi has in-house expertise. Sallie Krawcheck, chairman and chief executive of Citi global wealth management, calls this the "one-stop shopping aspect" of having both divisions under the same roof. "We can help a client look across not just their company needs but their personal needs as well," she says.

But being associated with an investment bank can have its downsides – as the credit market turmoil has shown.

"Some days it doesn't feel as great to be part of a large financial services company as it did a year ago, or two years ago or 10 years ago because, of course, the large banks, ourselves included, have had significant write-offs from the subprime issue and have, as a result, taken a reputation hit," Ms Krawcheck says.

"What doesn't change are the capabilities that we, in a large banking organisation, bring to our clients – be it the global footprint, which clients find to be very, very helpful, or the access to the broad range of products and services that are difficult to replicate in a smaller organisation."

Unlike Citi, JPMorgan Chase was never a significant creator of collateralised debt obligations backed by residential mortgages – a decision that is now paying off for the bank.

"Our clients know us very well as a private bank and a firm, and have confidence in our people and process to vet managers," says Catherine Keating, chief executive of JPMorgan's US private bank. "We have had record inflows for the past five quarters."

She says a big advantage of having an investment banking division is that many of the private bank's clients are the size of institutions and "are every bit as complicated and sometimes more complicated than institutional investors". Having the divisions under the same umbrella allows the wealth management teams to leverage the institutional knowledge honed by the investment banking arm.

"Managing wealth in this decade is much harder than in the previous two," she adds. "You need to be more global; more conscious of volatility and dislocation in the market; and need to move more quickly and tactically. Being part of a large financial services firm gives us insight and access that benefits clients."

PROFILE BESSEMER TRUST

Rob Elliott is rather unusual in the world of private banking. He has spent the past 33 years with one company: New York-based Bessemer Trust, an independent wealth manager that evolved from the family office of Henry Phipps, a partner of Andrew Carnegie in the Carnegie Steel Company.

This sort of stability is rare in an industry where smaller firms are routinely acquired by global financial services firms and staff turnover is high. But what sets Bessemer apart is that it is independent and private – the firm is owned by management and the Phipps family, whose assets comprise $5bn of the $52bn under management.

Mr Elliott, senior managing director, says staff turnover, along with client turnover, is very low. There are 670 staff and 1,900 clients, who include about 80 family-member representatives of the Phipps family.

"We have 140 current or retired CEOs of major corporations, we have had over time the head of every investment bank as a client, we have had three Treasury secretaries and one former President," says Mr Elliott.

The fees are on a sliding scale from 1 per cent on the first $10m to 0.75 per cent on the next $10m and 0.65 per cent on the $30m after that. Mr Elliott says teams of four deal with around 45 clients, which gives the firm "one of the highest client service ratios in the industry".

Bessemer offers the usual array of services: investment management, tax and estate planning, philanthropy, family wealth stewardship, insurance advice and family company advisory services. "If you're a smart client and use us for all those things we become quite inexpensive," he says.

Bessemer – named for the steel-making process that helped build the Phipps fortune – was established in 1907 but it was not until 1975 that it began accepting other wealthy families as clients. Over its 101-year history, its reputation has been untarnished.

"The highest priority for us and the Phipps family is reputation," Mr Elliott says. "We also spend a lot of time taking on the right client – you can say: 'Money is money, right?' Not right. We don't have to take every client."

He says the single biggest issue for new clients is whether the firm will stay private. "They ask: 'Are you going to stay the same?' And the answer to that is yes. We have been approached by virtually every major investment bank in the US, and some from overseas, who have said: 'Why don't you sell to us and you could become part of our global network.' Our answer is always a polite no."

Another question is whether Bessemer is going to grow too quickly. "We could grow much faster if we had $5m minimums," says Mr Elliott. "We really are taking $10m minimums but our average new client is over $35m. Our expected growth rate is about 7 per cent a year in terms of new clients – that's not huge but that's about as much as we can assimilate and do a first-rate job for those clients."

Lauren Foster

Benefiting from flight to quality

INTERVIEW
PIERRE DE WECK

Peter Thal Larsen meets the head of Deutsche Bank's private wealth management arm

The credit crisis has prompted many wealthy individuals to think carefully about the stability of their private banks. While the turmoil has not presented large financial institutions in a good light, the handful that came through the crisis without too much damage are seeing benefits.

Deutsche Bank appears to be one of the beneficiaries. Even though the group fell to an overall first-quarter loss as a result of turmoil in the capital markets, its private banking arm still reported strong growth in net new assets.

"Clearly we're benefiting from a flight to quality and from the fact that Deutsche Bank as an institution has weathered the storm with its strategy and management intact," says Pierre de Weck, global head of Deutsche's private wealth management arm.

Indeed, he is sufficiently confident that he has just increased his target for gathering new assets. Whereas Deutsche was aiming for growth of 8-10 per cent – in line with forecasts for the overall market – Mr de Weck now targets new client assets to expand by more than 10 per cent this year.

The credit crisis has cast a spotlight on Deutsche's wealth management arm, which for long was something of an afterthought as the German bank pursued its goal of building a global investment banking business. That began to change in 2002 when Josef Ackermann, Deutsche's chief executive, hired Mr de Weck to knit together the bank's patchwork of operations around the world.

Deutsche's business is unusual because two-thirds of its assets – around €200bn – are in onshore markets, which are gaining ground at the expense of traditional offshore centres. The bank has onshore operations in Germany, Italy, Spain, Switzerland, the UK and the US. It is also building onshore operations in China, India and Russia.

Mr de Weck, a former executive with Citigroup and UBS, is keen to cultivate entrepreneurs, who account for a substantial proportion of new wealth created for private banks. Apart from exploiting links with its investment banking arm, Deutsche is also using its balance sheet to develop lending relationships with current and potential clients.

Another target is to improve the profitability of Deutsche's private banking business, which generates a margin of about 82 basis points. Mr de Weck hopes to lift that to 90-100 basis points.

Deutsche has also shown a willingness to make small bolt-on acquisitions. Its most recent, in 2006, was Tilney & Co, a small British private bank with more than €10bn under management. Many rival bankers are sceptical about acquisitions, arguing that the risk of losing staff and clients mean few deals justify the purchase price.

Mr de Weck says the Tilney acquisition was necessary to give Deutsche Bank critical mass in the competitive UK market. The bank was also given some comfort on the integration by the fact that Tilney's chief executive, David Campbell, had previously worked for it.

But he remains cautious: "Acquisitions are very difficult and very expensive and you need to achieve substantial growth to justify them," says Mr de Weck. "Client continuity is key to the process and if you cannot achieve that you are better off not proceeding with the acquisition." Indeed, the main thrust of the bank's expansion has been organic: in 2006, it hired 300 additional client relationship managers, and added a further 200 in 2007, taking the total to around 1,800 around the world.

Along with other private banks, Deutsche has not been immune from the turmoil in the capital markets. Falling stock markets have hit the value of its clients' assets, and the dollar's depreciation affected the measurement of non-euro denominated assets. Mr de Weck also acknowledges that the crisis has hit clients' appetite for making new investments, although despite this, Deutsche's private banking arm was able to increase revenues by 9 per cent in the first quarter.

> 'If you have the patience you can build organically in a very successful fashion'

In the longer term, the credit crisis has given banks and investors a new appreciation for their private banking operations, which are now seen as a source of stability and long-term growth while consuming relatively little capital. As a result, Mr de Weck expects the business to become even more competitive as rivals seek to beef up their operations. But, he adds, there are no short cuts.

"The wealth management business is a business where if you have the patience you can build organically in a very successful fashion," he says. "What is built organically is probably more secure."

Pierre de Weck: weathering the storm
Bruno Vincent

The discreet appeal of the multi-family office

SMALLER INSTITUTIONS

Peter Thal Larsen on a challenge to the sector's established order

Over the past few years, most of the trends in financial services have moved in favour of larger forces. The same is true of the private banking business, where institutions such as UBS and Credit Suisse have gathered a growing proportion of the assets of the wealthy.

Yet when it comes to looking after the wealth of very rich families, a number of smaller institutions have emerged to take on the bigger companies.

Many of these institutions, operating from discreet offices in the West End of London or Zurich, have evolved from looking after the money of one or more wealthy families. The assets they control are insignificant when compared with the big private banks. Nevertheless, these institutions – known collectively as multi-family offices – represent a very real challenge to the established order of the private banking business.

Multi-family offices are a response to two powerful trends: first, the desire of wealthy families for access to sophisticated financial advice, unique investment opportunities, and top-notch planning of their tax and legal affairs. Second, the multi-family offices also reflect their clients' desire for independent advice, and suspicion of large institutions.

While the multi-family offices have grown significantly in recent years, the credit crisis has given them a further boost. The turmoil in the credit markets has prompted many families to review their financial affairs.

"For the first time in four years we are seeing potential clients sitting up and saying: 'Are we getting the best service?'" says Gavin Rochussen, chief executive of Fleming Family & Partners, the multi-family office originally set up to manage the wealth of the 150-strong banking family.

At the same time, many wealthy families that previously relied on large private banks have increasingly sought independent advice. "The crisis has definitely moved client perceptions on what is considered to be safe," says Giuseppe Ciucci, chief executive of Stonehage, which started out administering the affairs of wealthy South African families, and has expanded since. "People have realised that independence is worth quite a lot."

> The institutions threaten to lure away some of the largest and most lucrative clients

Multi-family offices represent a significant challenge to private banks, because they threaten to lure away some of the banks' largest and most lucrative clients. And although multi-family offices will often recommend products provided by particular banks, the relationship between the bank and its customer is more at arm's length.

Large private banks argue that the multi-family offices cannot offer clients access to the same suite of investment products, and also risk adding an additional layer of cost. But defenders of the multi-family office model point out that, if they are sufficiently large, they can often gain access to investment products and services on better terms than are available to an individual high net-worth client.

This trend has increased with the introduction of so-called open architecture, where investment advisers recommend a suite of products from a range of providers, and banks sell their products to a range of institutions, with little or no preferential treatment for other parts of the same company.

"In a world where family offices have equal access to all the products the wealthy are asking themselves: why go to a large private bank?" says Christian de Juniac, senior partner and managing director at Boston Consulting Group.

Nevertheless, there are significant differences between individual multi-family offices. Fleming Family & Partners offers trust services as well as its own funds and even advisory services to clients who want corporate finance advice. Stonehage, by contrast, has concentrated more on administration and custody of its clients' assets, as well as planning their tax and legal affairs.

Multi-family offices are not for everyone: though standards vary, most organisations are targeting families with assets of at least $100m. But Paul Ross, chief executive of Arundel Iveagh, the combination of a fund manager and the Guinness brewing dynasty's family office, says the current crisis has given multi-family offices an opportunity to prove their model is better.

He says: "Over the last six months, if a family wanted to set up a family office, or go into a multi-family office with a view that their money will be managed better, this is a very good period to judge."

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Clouds disturb sunny outlook

SWITZERLAND

Haig Simonian on the twin impact of volatile markets and a new threat to bank secrecy

After a wonderful run, two storms are looming for 2008 in Switzerland's private banking sector. While the first – extremely challenging markets – may be transitory, the second – the threat to bank secrecy – looks more permanent.

Volatile, often tumbling, markets have a double impact on banks that depend on wealth management for their livelihoods. Fee income, levied as a percentage of assets under management, falls as assets shrink. And client activity, the second big source of fees, slips as customers – even rich ones – shy away from fickle markets. Add the weakness of the dollar, a significant factor both as an asset class and a reference currency for portfolios, and the downbeat mix becomes complete.

Most big private banks have already hinted that 2008 will be difficult, although few have been explicit. Among the handful that have been concrete, Julius Baer last month prepared analysts for first-half results that would reflect the more trying conditions.

How long the downturn lasts depends on the depth and duration of economic weakness in the US, the world's largest economy. Optimists hope the impact of the housing crisis will be limited, and claim the residential market has hit bottom. They also contend that global growth, still strong, will compensate for transitory problems across the Atlantic.

But for the pessimists the effect of plunging US house prices is still being played out, with rising unemployment and contagion to other categories of credit as the corollaries. Stocks and bonds, inevitably, have been affected, while inflationary tendencies are being stoked.

Strong response: UBS has led the move in recent years to develop onshore networks in key markets Getty Images

Such developments are beyond the control of even Switzerland's private bankers. Amid the uncertainty, most are ploughing on with expanding their networks to tap into so far underexploited pockets of global affluence.

Branch openings in Asia and the Middle East have continued, and have been followed, in some cases, by openings in Russia and eastern Europe. Those eschewing bricks and mortar have been hiring busily, especially fluent Russian speakers, to beef up their Switzer-land-based regional teams.

Sterner cost controls have become another theme in this year's more difficult climate. But here, banks have sometimes found themselves in a bind in trying to decide between investing in new branches or client-facing staff, just as revenues and earnings may be falling. So far, the investment case has proved stronger. But many banks are turning the screw on costs in other parts of their business.

The year has also brought a renewed challenge to bank secrecy. Matters began badly when German prosecutors launched a high-profile campaign against alleged tax dodgers after having acquired stolen data about customers of the trust subsidiary of LGT, Liechtenstein's biggest bank.

Weeks later, a second Liechtenstein bank came unwillingly into the frame as a criminal case opened in Germany into individuals accused of illegally obtaining customer details that had been stolen from Liechtensteinische Landesbank, another of the principality's big banks. Adding piquancy this time, prosecutors have suggested the bank transferred significant amounts to some or all the perpetrators to regain the data, but the whole issue became public before the final tranche was, allegedly, to have been paid.

Initially, Swiss bankers looked on uneasily as their Liechtenstein colleagues gained unwelcome publicity. The Liechtenstein cases, spearheaded by the German authorities, refocused attention on not just the principality, but also Switzerland and Austria, the two other European countries that assure client confidentiality.

In the wake of the revelations, European Union finance ministers, spurred by Germany, are talking about revisiting the deal with Switzerland on taxing foreigners' savings – a pact the Swiss thought had defused the issue for years to come.

Whether the EU will mount an effective challenge is another matter. Some member-states, notably Austria, say they will not budge on bank secrecy – or at least, not until Switzerland and Liechtenstein do.

Then came the bombshell from the US, where, according to the authorities, employees of "a Swiss bank" (known to be UBS) allegedly helped rich citizens evade taxes by setting up elaborate schemes involving offshore companies and Liechtenstein trusts. Investigations were accompanied by the brief detention of UBS's head of offshore private banking for North and South America, who had to remain in the US as a "material witness".

The move could hardly have come at a worse time for Switzerland's biggest bank, slowly recovering from huge losses in the US subprime meltdown and in the throes of a SFr15bn rights issue.

But the adverse attention was not just untimely for UBS, it was also a reminder to all Swiss private banks that the traditional offshore private banking model of administering the undeclared funds of rich foreigners remained under pressure.

Some Swiss bankers have responded robustly, accusing the US – which itself generally refuses to provide client data to foreign countries – and the UK, with its special status areas such as Jersey and Guernsey, of double standards when it comes to bank secrecy and tax evasion.

But for Switzerland, a small country with an extremely large financial services sector in which private banking plays a singular role, the risks of confrontation are impossibly high. Some banks, led by UBS, have in recent years responded to such threats to the traditional private banking model by developing onshore networks in key markets.

The latest events suggest such moves have come not a minute too soon.

PROFILE CLARIDEN LEU

When Credit Suisse announced two years ago it would merge its four independent private banks and a fund manager into a single unit to exploit the opportunities of consolidation, it seemed an astute step.

Cynics joked that Switzerland's second-biggest bank was again mimicking UBS, its bigger rival, which some months earlier had addressed a similar issue by selling its three small private banks and a fund manager to Julius Baer, the Swiss private bank.

With massive wealth management arms of their own, UBS and Credit Suisse were, in their different ways, seeking solutions for their relatively undersized, and independent minded, private banks at a time of rapid market change.

Folding such units into the parent company risked destroying hard-earned value. Opting for flotation, by contrast, heralded future conflicts of interest. So while UBS sold, Credit Suisse consolidated.

Two of its private banks, Leu and Clariden, were sizeable businesses. Leu was one of the most venerable, if less dynamic, names in Swiss banking. Clariden, much younger, was known for profitability and growth. Combining them with Bank Hofmann, BGP Banca di Gestione Patrimoniale and Credit Suisse Fides, three niche forces completing the puzzle, promised big synergies.

Two years later, Clariden Leu, as the combined bank has been called, is seen as a good idea executed badly. Top executives have left, private bankers have quit and the group now appears smaller than the sum of its parts.

"The idea was fine. But there wasn't a strategy about where to go next. Credit Suisse left things completely in limbo, so people left," says one person close to the situation. "They just didn't think it through."

Alex Hoffmann and Bernard Stalder, chairman and chief executive respectively of Clariden, opted for other ventures or semi-retirement. Beat Wittmann, Clariden's head of investment products, took his team to Julius Baer. Two top regional heads also quit, while, at a lower level, a team of eight private bankers moved en masse to Rothschild. Other departures, smaller or less senior, went unnoticed.

Hans Nützi, chief executive of Clariden Leu since last November and previously occupant of the same job at Bank Leu, will have none of it.

He admits Credit Suisse knew there would be casualties. And he concedes the number of departures – or at least the top level ones – exceeded expectations. But Mr Nützi, who has spent more than 30 years at Leu and its predecessors, says appearances have been worse than reality.

"In terms of numbers, we didn't lose more people than expected. And those we lost, we've replaced, in many cases with better alternatives – including whole teams," he maintains.

Mr Nützi, originally entrusted with private banking for the combined group before becoming chief executive on Mr Stalder's surprise departure last year, also points to Clariden Leu's results as evidence of its wellbeing. "In our first year, we achieved better net revenues than the best for all five companies combined, in spite of the difficulties of merging."

Nützi: strong rebuff for critics

He says the figures for 2007, when net revenues rose by 12 per cent to SFr1.76bn and assets under management climbed by SFr5bn to SFr129bn, laid the foundations for growth. Clariden Leu aims to raise assets under management in private banking by 6 per cent a year and boost the amount invested in its funds by 10 per cent annually.

The goal is to build on Clariden's strong Asian and Latin American franchises and Leu's Swiss and west European business. Mr Nützi is concentrating on eastern Europe, the Middle East and Asia to power his plans. But he is also confident about traditional European markets, including Germany.

"Now is not the time to step on the brake. It's just when the going gets tougher that you can cash in on opportunities," he reckons.

Observers remain sceptical. Critics point to a fundamental conflict in Credit Suisse's decision to migrate Clariden Leu to the group information technology platform and standardise procedures. While essential for synergies, such moves eroded entrepreneurial spirit – particularly at Clariden, they say.

Some also note that Clariden Leu's 2007 figures may not be enough to justify Mr Nützi's confidence. The 2007 net profits of SFr626m were no improvement on the previous year's pro forma figure. And net new assets, at SFr2.85bn, were down sharply on 2006.

"Figures for one year just aren't representative in private banking. A bank needs a three- to five-year track record before one can say how it's doing," says one observer.

Mr Nützi disagrees. He describes the 2007 profits as creditable, given the inevitable disruption and costs from the merger. And Clariden Leu can still project itself as independent, while being on Credit Suisse's IT platform.

For Mr Nützi, the pieces are now in place to boost net new money and assets under management. With competition rising and markets becoming much tougher this year, it is up to Clariden Leu to prove it.

Haig Simonian

Time for calm on secrecy

Guest Column
PHILIP MARCOVICI

Recent high-profile tax investigations have given pause to families burdened by the offshore ownership of funds that, contrary to the laws of their home countries, remain undeclared for tax purposes.

These events, however, do not signal any change to a longstanding reality: in today's increasingly transparent world, wealth owners have only two choices. These are to "play by the rules" of their home country or to "get out", giving up taxable residence (and, in some cases, citizenship).

It is, however, high time for the realities to be addressed in a calm, rational way by the holders of such funds and their bankers. And, given the amount of undeclared money held abroad, which some estimate at around $6,000bn, it is also time for governments to make it easier for taxpayers to "come clean".

For many years, countries have been taking steps to obtain tax information from banks and others, whether or not they are in bank secrecy locations. Developments here range from the US Qualified Intermediary rules to the contribution of technology, and the growing ease in which tax authorities can obtain credit card, financial and other information. Co-operation among countries, resulting in wide information sharing, is also a growing focus.

The European Union Savings Directive was designed to capture tax on interest payments made to individuals who reside in a different EU country from where the payment is made. Filled with loopholes, the directive permitted many to avoid the rules. However, the EU has made it clear that the loopholes will be closed and the scope of the directive extended. One can run, but for how long can one hide?

In today's transparent world, wealth owners are badly served by advisers who emphasise bank secrecy as a means of avoiding taxation. It is surprising that Singapore, a model of strategic planning, seems to be falling into the trap of secrecy-based private banking, maintaining a system that attracts Europe's tax evaders fleeing the tightening grip of the EU directive.

Bank secrecy is important and wealth owners have rights to privacy in relation to financial and other affairs. However, bank secrecy can no longer be misused to permit the evasion of tax.

At the moment, the wealth management industry is not doing enough to address the real long-term needs of wealth owners. While a substantial and growing business, in all too many quarters little effort is made to understand the changing international environment within which banks operate and on training and knowledge management.

Wealth owners need to understand that non-compliance with tax laws is simply not an option in today's environment. Breaking the law carries criminal, financial and reputational risks, and all too often these are left to the younger generation to sort out. Given that many advisers and intermediaries are living in the past, great care needs to be taken by wealth owners who obtain advice from those who have a financial interest in enabling assets to continue to be maintained on a non-declared basis.

Wealth owners must become familiar with ways to address issues of undeclared money, including voluntary disclosure, amnesty arrangements and review of statutes of limitations and other relevant rules that can help families to "come clean". Wealth owners are doing their children no favours by not thinking seriously about the future.

A solution to the issue of undeclared funds will need to involve financial institutions and governments working together co-operatively.

First, there needs to be an acceptance that undeclared tax money exists, and that the issue is

'Bank secrecy can no longer be misused to permit the evasion of tax'

Philip Marcovici
Baker & McKenzie

not confined to well-known bank secrecy centres.

Second, the historical reasons, often unrelated to tax issues, why wealth owners are holding undeclared funds need to be acknowledged. Bank secrecy rules in a number of countries were developed to help families protect against expropriation of assets and corruption in their home countries.

While bank secrecy has been abused, many wealth owners deserve a sympathetic approach to regularising undeclared monies. That will require the co-operation of governments and banks and other providers of services to wealth owners.

It is time for a creative approach to resolving a global problem.

Philip Marcovici is chief executive of LawInContext, the interactive knowledge and training venture of Baker & McKenzie. A partner of Baker & McKenzie Zurich, he is also chair of the law firm's global private banking practice group.

Preserving reputation is a paramount concern

RISK MANAGEMENT

Andrea Felsted on how the issues differ from those affecting mainstream banks

Across the financial services industry, the concept of risk is being reassessed.

The turmoil in credit markets has been a reminder that risk can lurk in previously unexpected areas, with credit and liquidity risks, in particular, rising up the agenda.

But according to Stefan Jaecklin, leader of Oliver Wyman's wealth and asset management practice, private banks are concerned with a particular set of risks rather than those preoccupying the mainstream banking sector.

"When you talk to the normal banks, the risk management focus is on solvency and liquidity issues," he says. "That is not really what the wealth managers are worrying about... For them risk management is much more a question around non-financial risks such as reputational damage." This, he says, can come from issues around fraud, lost data, or problems with tax authorities.

Nigel Harman, head of financial risk management at KPMG, agrees that liquidity is not an issue for private banks.

"They have strong and growing funding bases and the issue is where they place them, rather than the other way round," he says. "A number of the larger integrated groups have legitimately used the funding from their private banking operations to fund their investment banking business. That model is under review as a result of the crisis in financial markets," he says.

Indeed, another risk to private banks that are part of bigger groups is that from "business behaviour or failure of the bank in other areas", says Mr Jaecklin.

"When you have a bank group that is a combination of a wealth management business and a corporate investment banking business, the type of risks in the two institutions and what they care about are very different," he says.

Alison Morris, a partner in PwC's wealth management practice, says private banks belonging to groups that have incurred losses in their investment banking arms "need to be quick off the mark to ensure clients understand their assets are still safe".

This underlines one of the the biggest issues for private banks: ensuring that their clients' assets are secure – even in a market meltdown.

The first step in safeguarding clients' assets is understanding their appetite for risk. "The losses that have been seen [in financial markets] over the past few months have brought the whole risk profile to the fore with huge clarity," says Ms Morris.

The next step is designing portfolios that meet these clients' risk appetite. "Ensuring that clients have an asset allocation that matches to their risk tolerance is crucial," says Philip Watson, head of the investment analysis and advice group at Citi Private Bank.

Ms Morris says some clients' risk appetites may be lower as a result of the recent market turmoil, and this will need to be reflected in their portfolios.

"The riskiness of investments has been brought to the public's attention very starkly," she says. "Many clients may now be deciding [their] risk appetite is lower than it may have been 12 months ago. Banks need to react to that and remodel the portfolios to take account of that fact."

She says that if private banks are investing clients' assets in line with their appetite, this should help manage risk. "If they have been investing client portfolios in accordance with the clients' pre-agreed risk category, they ought not to have issues."

Mr Jaecklin says the biggest problems come when clients incur losses on products that they do not understand. "Losses on assets that the clients have understood – that is not a problem. That is part of the business and that is accepted," he says. "The problem is more losses or products that have been sold to private clients that, actually, the clients have not understood."

'Private banks have strong and growing funding bases and the issue is where they place them'

Nigel Harman
KPMG

With more and more clients turning to non-traditional and complex assets, this raises a challenge for private bank risk management.

"In the traditional investment products, the risk management framework, environment and understanding of the risks are relatively well established," says Mr Jaecklin. "Where it becomes tricky is... with the more complicated, complex instruments."

Other factors to mitigate the risks to clients include portfolio construction. Ms Morris at PwC says private banks use sophisticated model portfolios: "A lot of thought goes into them," she says.

Citi's Mr Watson says diversification is key to safeguarding assets. Not only does this mean ensuring that clients' portfolios are adequately diversified by asset class, it also means ensuring that their money is invested in a sufficient number of funds, so that they are not overexposed to the actions of any one fund manager.

"That way, we have a high level of confidence that the client is sufficiently diversified to actively preserve capital and not incur large losses when a single manager does underperform," he says.

To further safeguard clients' assets, it is important that thorough due diligence is carried out on fund managers and capital market structures.

According to KPMG's Mr Harman, some private banks are beginning to apply sophisticated investment banking-style risk management techniques to their clients' underlying portfolios.

"With the turmoil in investment banking, you may ask: 'what is the use of that?' But I think it is right to see that increased sophistication," he says.

"For private banks, it is all part of managing risk by looking after your client's assets as if they were your own."

Staffing worries in Asia – the bald facts

RECRUITMENT

Andrew Wood reports from a region where talented employees are in short supply

Hairdressers come up a lot in conversations with private bankers in Asia about recruitment. The shortage of staff in the region, so the story goes, became so acute in the past year or two that one bank started hiring stylists from upmarket salons to retrain as bankers to the wealthy.

Of course, nobody seems to know which bank it was that actually hired the hairdressers. Whether the story is true or not does not really matter; like the best urban legends, the fact it is repeated so often tells you something about the private fears of private bankers in Asia Pacific.

Part of that fear is about missing some great opportunities.

The region is home to more than a quarter of the world's wealthy individuals, those with at least $1m of investable assets.

Their wealth is growing by 8.5 per cent a year – well above the global average of 6.8 per cent, according to Merrill Lynch and Capgemini estimates. By 2011, their combined riches could total $12,700bn.

Wealth managers, so far, are serving only about a third of Asia's rich people. So the market shows enormous further potential – if only the staff can be found.

PwC, the consultancy, estimates that the demand for private bankers will increase by 57 per cent in the region over the next two years compared with a global rise of 32 per cent.

"At a time when wealth managers have failed to fill almost half of the previous year's recruitment openings, it is difficult to understand how the required rate of expansion will be met," says PwC's Developing A Talent Legacy report, which analysed the results of the consultants' Global Private Banking/Wealth Management Survey 2007.

Managers at 265 institutions in 43 countries were surveyed. They said that finding appropriately qualified staff was the biggest issue they faced, and retaining key employees was next.

Finding staff takes up an enormous amount of time, says Didier von Daeniken, Asia Pacific chief executive officer for Barclays Wealth, the private banking arm of the British lender Barclays.

"It's never easy to build up a team, be it in Asia or in Europe," says Mr von Daeniken, who was hired last year from Credit Suisse to expand Barclay's wealth management business in the region. "You have to create an environment where people realise they will be measured on their merits."

"Recruitment requires a lot of discipline," he says. For every 100 CVs Barclays receives – usually from headhunters – the private bank interviews about 30 people and hires about 10.

"If you take these numbers, and I have interviewed personally 100 people since January, it's a significant effort in terms of resources," he says.

Most of the people he has hired have been private bankers, or corporate bankers looking for a different direction for their careers within finance. "I'm not sure it's a good idea to hire people from outside the industry," says Mr von Daeniken. "There's nothing wrong with it in theory but you have to ask yourself: 'What are our training capabilities?'"

Poaching entire teams is another tactic that has been popular in recent years. For example, Deutsche Bank Private Wealth Management in Hong Kong lured six senior people away from JPMorgan Private Bank in March.

Andrea Benanti, Julius Baer's managing director for North Asia, says that, tactically, team poaching may look like it makes sense: you instantly gain expertise and you deal a body blow to a rival at the same time.

But in fact it has many drawbacks. "I'm not a big fan of it," he says. "We really try to go for quality people. If you hire a team of 15 people as a package deal, what is the chance that all these people will fit and will have what we want? The chances of that are very small."

The danger, Mr Benanti says, is that you might have to fire some of the team members after six months – "and that's not our style".

As for the client relationship managers (CRMs) themselves – the front-line staff who have the day-to-day contact with customers – PwC reports that 90 per cent of them say they have been approached by a rival firm in the last year.

"Whilst this may solve immediate resource shortages, it serves to accelerate CRM salaries, driving up the cost base of the wealth manager, and in the long term is not a sustainable strategy," PwC says.

Pay for relationship managers in Asia doubled between 2004 and 2006, according to Boston Consulting Group. Total average compensation jumped $162,000 a year to $324,000, although much of that increase was in performance-related pay.

But Kaven Leung, chief executive officer for Citi Global Wealth Management Asia Pacific, thinks the wheel is turning in favour of employers again. High wages simply erode margins.

"We don't want to compete on raising the salary," he says. "The challenge is really not about who pays the highest, which was the game in the past few years of exuberance and unbelievable packages. It's much more internal strength and the culture. The brand is also key."

Citigroup says its Asian private banking business has been growing at annual rates of between 15 and 25 per cent. It has spent millions of dollars on its banking "platform", including sophisticated transaction systems, product selection and creation tools and a small army of product and investment specialists.

Few of the smaller, more recent entrants to private banking can match the support that Citi gives to its relationship managers, Mr Leung says. Some of the weaker competitors are already being winnowed out – and that means a wider pool of potential staff to choose from.

"We are seeing consolidation in the industry but I didn't expect it to be so steep. It's a good thing," says Mr Leung. "From my point of view what we are seeing today is natural and may be healthy in the long term." For now, it seems, hairdressers will have to stick to hairdressing.

Hair today, hire tomorrow: a Hong Kong urban legend suggests stylists have retrained as private bankers Alamy

CASE STUDY CREDIT SUISSE

Credit Suisse set itself an ambitious target for its private bank when it announced its 2007 results in March: it would hire an additional 1,000 relationship managers, the key frontline staff who deal with wealthy customers, around the world by the end of 2010. Most of them would be in the Asia Pacific region.

Last year was a good one for Credit Suisse's wealth management business. Pre-tax profits rose 19 per cent to SFr3.86bn, margins improved to 40.3 per cent compared to 39.6 per cent in 2006, and the business attracted SFr50.2bn of net new assets to manage.

"Our strong performance and the turmoil we see in the industry means this is an ideal time for us to acquire great people," says François Monnet, managing director and head of private banking for south-east Asia and Australasia.

"We clearly increased the pace at which we are hiring relationship managers. Of the 320 total in 2007, 70 per cent were added in the second half of the year alone, with a bias towards Asia, the Middle East and Latin America. More than 100 were hired in Asia Pacific."

The private bank now has 390 relationship managers in the Asia Pacific region – 50 per cent more than a year earlier. What is more, Credit Suisse has improved its ability to keep staff once they have been hired. "We achieved 100 per cent relationship manager retention in the region this year," Mr Monnet says.

Credit Suisse says its own in-house business school in Singapore has played a big part in attracting and keeping staff. It has trained more than 4,100 employees since opening in 2005, and in the past year has launched a curriculum to prepare staff for individual relationship manager and private banking roles.

Singapore is turning into a big centre for training private bankers, in line with the government's plans to make the city-state a hub for wealth management for the region. UBS also has a similar school, and Singapore Management University has a master's degree in wealth management.

Among Credit Suisse's other initiatives, it has expanded its "training and onboarding programmes" to cover all new joiners. It has also extended its career development plan to every private banker above a certain grade to focus on talent development, career growth and mobility within the bank.

Additionally, it has launched a relationship manager award to recognise private banking staff's individual achievements.

Andrew Wood

Isn't it interesting how seductive solidity is in times like these?

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Rising high: for wealth creators in China or Hong Kong, Singapore is becoming a viable alternative to Geneva or London AFP

ALTERNATIVE CENTRES

Jane Croft on the rising profile of Singapore, Dubai and Hong Kong

Much has been made of the ambitions of Singapore and Dubai to develop into the new Switzerland of private banking.

Certainly they are located in the right part of the world, where wealth creation is growing fastest. Private wealth in Asia grew 10.5 per cent last year to $8,400bn, according to consultancy Capgemini.

Asian private banking is growing fast because many of the region's new millionaires are ploughing their money into private banking rather than into property.

There are industry estimates that close to $300bn – or around 5 per cent of the world total – of private banking assets are managed in Singapore, compared with Switzerland's $1,700bn. The number of private banks in Singapore has risen from just 20 in 2000 to around 42 and private banking assets have grown from $50bn in 1998 to just over $300bn.

For entrepreneurs generating wealth in China or Hong Kong, Singapore is becoming a viable alternative to the traditional locations of Geneva or London.

Singapore is regarded as stable and secure and has transformed its private banking over the past 10 years. The island state has beefed up account secrecy protection and allowed foreigners who meet minimum wealth requirements to buy land and become permanent residents.

In 2000 it strengthened its banking secrecy laws, which are considered stricter than even those of Switzerland.

Another big attraction is Singapore's new trust laws. Some countries have laws that supersede trusts and wills but in late 2004, Singapore exempted foreigners who set up local trusts from these limitations.

Tjun Tang, partner and managing director at Boston Consulting Group, says the level of money booked in Asia by Asian entrepreneurs has been running at almost three times that booked in Switzerland, so these clients now have a "a very viable alternative in Asia".

"The Singapore private banking laws are modelled on those for Switzerland and the infrastructure is pretty good. Singapore has gone out to create a very strong private bank infrastructure and is known for investing in private banking courses at universities to train private bankers." Mr Tang says.

Indeed as regulators have tightened up in Europe, some suggested this year that centres such as Singapore would be a beneficiary from the Liechtenstein tax evasion investigation.

Daniel Truchi, global head of Société Générale's private banking business, said this year that these events were "sort of like an earthquake for European private banking" as they undermined client confidence, and that the implications would be felt in other European centres such as Switzerland and Luxembourg.

Wealthy clients in the Middle East, India and Iran are increasingly looking to deposit money in Dubai.

Sven-Olaf Vathje, partner and managing director at Boston Consulting Group, says many Middle Eastern clients are keen to invest in regional private equity and real estate.

Private banks have been capitalising on that trend by offering regional investment products to attract clients, cross selling other more traditional private banking services later. They are still booking most of their business through Switzerland rather than Dubai, although that is changing slowly.

"The Old Wealth in the Middle East is still focused on private banking centres like Switzerland and London – up to 40 per cent of wealth is offshore," says Mr Vathje.

"However places like Dubai are growing as a centre, leveraging their proximity to local investment markets. There is an increasing self-confidence, especially among the younger generation, in using a regional financial centre."

Peter Flavel, global head of Standard Chartered private bank, believes the cultural mindset of private banking clients in regions such as Asia is different and clients prefer being able to deal more directly with their relationship managers.

"There has been an explosion in wealth in Asia and the Middle East as well. Once upon a time the wealth found its way to Geneva and London," he says.

Increasingly, he says, the bank is seeing people wanting to invest their money in a private bank in the country where they live. "Asian entrepreneurs who have built their operations up from scratch often want to have greater control in managing money. They may also place it in several places."

At the same time, a client may invest in Singapore and in Geneva to get a choice of banking centres. "This is what they want – different buckets and different flexibility," he says.

"There are differences in clients – the generational wealthy are comfortable with Geneva and know Geneva well. A lot of our second generational wealthy Asian clients want to be close to their relationship managers and see them frequently rather than for a game of golf once a year."

Mr Flavel says Asian entrepreneurs are more likely to take a hands-on approach to managing their money instead of handing a mandate to a wealth manager.

"They are very sophisticated and people are using more sophisticated products and take a view on diversification and risk. Asian entrepreneurs have a different perspective and different needs to Swiss clients."

However, many experienced private bankers do not believe Singapore or centres such as Dubai are seriously challenging Switzerland's pre-eminence as a private banking centre yet.

Chris Meares, global chief executive of HSBC's private bank, says there are several reasons why these centres are growing very fast but will not develop as much as other centres.

"The pool of wealth creation and size of the market has created all three of them. Dubai has Middle Eastern money and Singapore and Hong Kong have been driven by Asian growth and growth in China," he says.

"Certainly not as much wealth will now filter back to Switzerland or London from a private banking perspective as there might have been 25 years ago."

However Mr Meares believes the main problem is a resource issue as there is a smaller pool of private bankers and top quality asset managers in Dubai or Singapore than in centres such as London or Geneva.

> 'There has been an explosion in wealth in Asia and the Middle East as well'

"In Singapore there is a shortage of private bankers. In London and New York you will find the best asset managers.

"What we see at the moment are resource constraints and there is not the same pool of investment bankers and asset managers in Dubai and Singapore, which could hold them back for a while."

Mr Tang at Boston Consulting Group also identifies the shortage of good staff as a serious constraint on the new centres. "Switzerland has such a head start on Singapore and overall assets in Singapore are a quarter of the size of those in Switzerland," he says.

However he also notes that clients in Asia like to talk to relationship managers on a more regular basis.

"The business model is different in Asia. In Europe a lot of people give wealth managers discretionary mandates," says Mr Tang.

"In Asia there are fewer mandates and much more of the business is transactional and therefore there is a higher level of involvement by clients.

"Some clients might have up to a dozen private bank accounts and regularly talk to private bankers just to get ideas."

Golden opportunity: a jewellery shop in Dubai Charlie Bibby