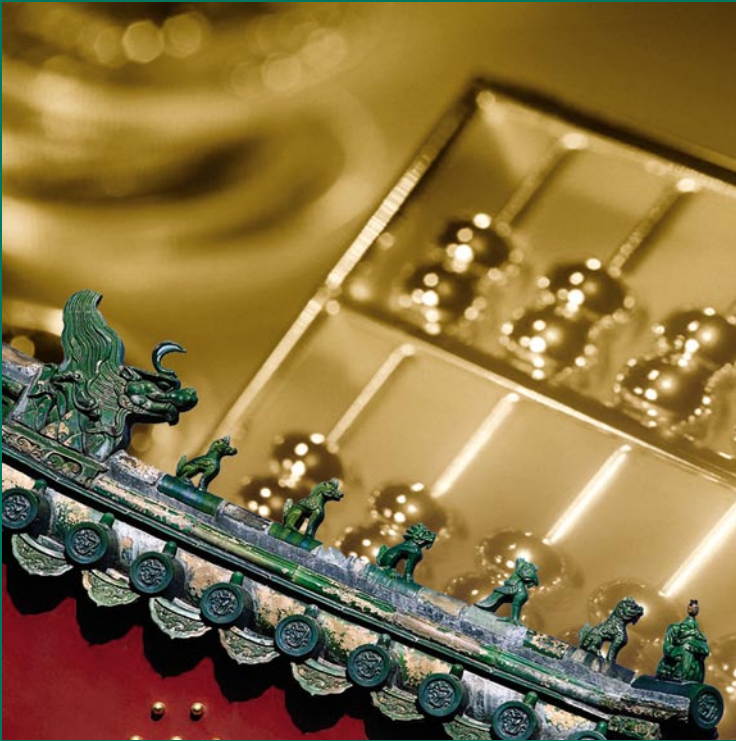


FOCUS

# Wealth Markets in China

Serving the Rising Wealth



THE BOSTON CONSULTING GROUP

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# Wealth Markets in China

Serving the Rising Wealth

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October 2007

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# BCG Financial Services In China

**T**he Boston Consulting Group (BCG) is pleased to present this report which constitutes the most recent in a series of publications produced on the dynamics of China's financial services industry, and the implications for local and overseas players.

BCG is a general management consulting firm that is a global leader in business strategy and that has helped companies in every major industry and market achieve competitive advantage by developing and implementing winning strategies. Founded in 1963, the firm now operates 66 offices in 38 countries.

BCG started operations in China over 25 years ago, with projects for multinational companies entering the country. Soon afterwards, BCG began serving Chinese enterprises and Government entities. In 1993, BCG opened its first office in China—located in Shanghai—well ahead of other major international management consulting firms.

Financial Services has been a cornerstone of BCG's business portfolio in China for many years. BCG serves a select number of leading foreign multinational and domestic Chinese clients in the banking, insurance and securities sectors. In particular, the firm has assisted, and continues to advise, several large state-owned banks in their wide-ranging reform and privatization efforts.

Cooperation with these and other clients typically start from enterprise-wide strategic themes such as understanding customer needs by segment, corporate and business strategy, and competitive differentiation. Subsequently, BCG teams, assisted by a global network of experts and advisers, have also been instrumental in helping our clients build deep professional capabilities in key areas such as capital strategy, risk management, information technology, marketing, and sales force effectiveness.

Consequently, BCG China sees itself as a bridge between Chinese and foreign business cultures and practices. BCG leadership firmly believes that success in China requires a deep understanding of both business perspectives and the ability to meld them into a unique way of doing business in China.



# FOREWORD

**I**n recent years, the global wealth management industry has continued to experience very strong growth and has been a strong focus for many global banks. The Boston Consulting Group (BCG) estimates that worldwide wealth measured as the household financial assets under management (AuM) grew by a very healthy 7.5 percent last year to reach US\$97.9 trillion. This marked the fifth consecutive year of expanding wealth. When wealth was measured in local currencies, Asia Pacific excluding Japan, had the strongest gains in wealth AuM in 2006 at 12.8 percent.

Wealth management customers, be they merely affluent or extremely affluent, represent one of the most attractive individual customer segments for many banks. Indeed, BCG benchmarking surveys of retail banks show that the average private banking customer can be ten times more profitable than an average mass market retail customer.

In recent years, Chinese banks have been paying increasing attention to the wealth management market, to the importance of attracting and retaining these highly valuable customers, and to the profit potential that wealth management offers. Most Chinese banks offer premium banking services (to customers with more than RMB 500,000 in AuM) and several have launched private banking offerings for clients with more than RMB 5 million or USD 1 million in assets. In addition, foreign banks increasingly are turning their focus to tap opportunities with wealthy Chinese clients, utilizing both onshore and offshore private banking models.

In this special supplement to our report “Tapping Human Assets to Sustain Growth: Global Wealth 2007,” we provide an update to the Chinese wealth management market, covering:

- The growing importance of China’s wealth markets
- Understanding the nature of Chinese wealth
- Private banking models for China
- Key elements for building a leading wealth management business in China



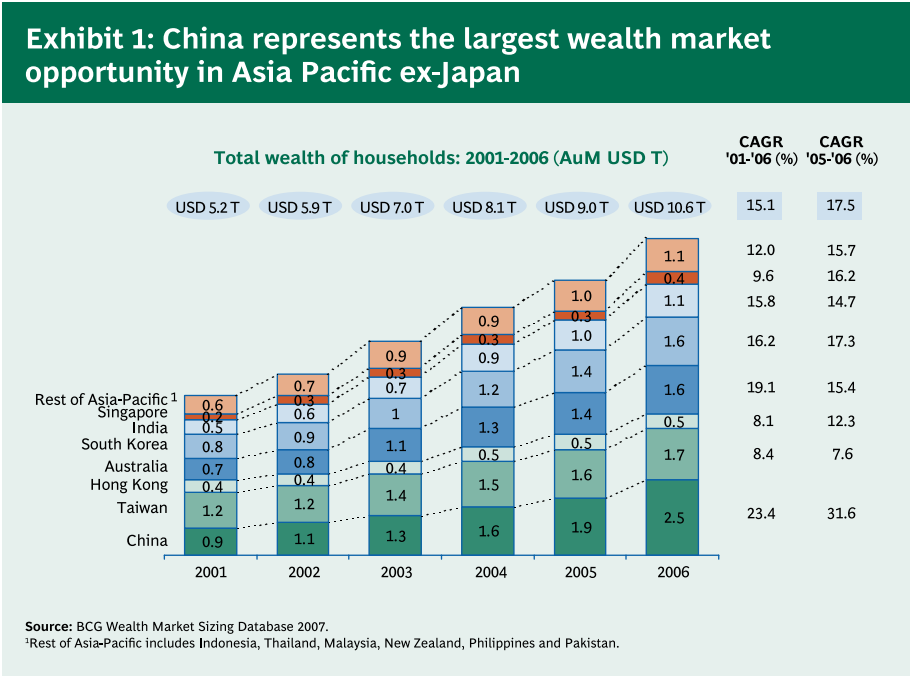
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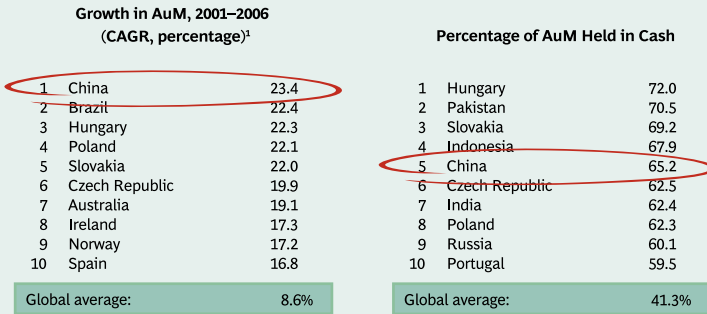
# The Growing Importance of China's Wealth Markets

The wealth management industry in China is still nascent but is already quite sizeable and continues to hold enormous potential. Today, China represents the largest market in Asia excluding Japan, with households owning about US\$2.5 trillion in financial wealth. Indeed, the Greater China region—comprising of China, Hong Kong and Taiwan markets—is now home to 45% of the wealth in Asia excluding Japan. (See Exhibit 1.)

Chinese wealth has experienced extremely strong growth, at 23.4% CAGR over the past five years (against a very healthy global average of 8.6%), and in the past year alone, BCG research estimates Chinese wealth has grown at a staggering 31.6%. This is despite Chinese households holding a very high percentage of their wealth in conservative investments (primarily cash), though this is declining—see later. (See Exhibit 2.)



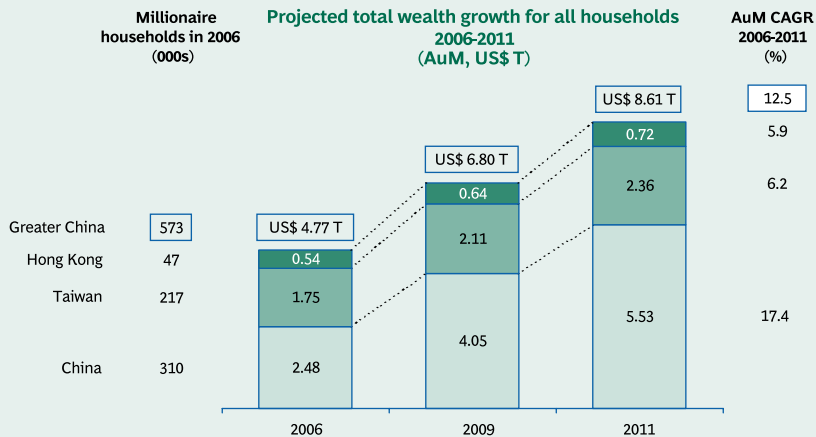
## Exhibit 2: Over the past 5 years, China has led global growth in AuM despite conservative asset allocations



Source: BCG Global Wealth Market Sizing Database 2007.

<sup>1</sup>The compound annual growth rate was calculated by measuring growth in U.S. dollars.

## Exhibit 3: Strong growth in wealth is expected to continue in the Greater China market



Source: BCG wealth market sizing database 2007.

Continued growth in the Chinese market is expected to be supported by ongoing strong growth in the Chinese economy, liberalizing market conditions, and strong asset returns among all segments of the wealth management market. BCG projects annual household financial asset growth in China of around 17.4 percent over the next several years, resulting in AuM reaching an estimated US\$5.5 tril-

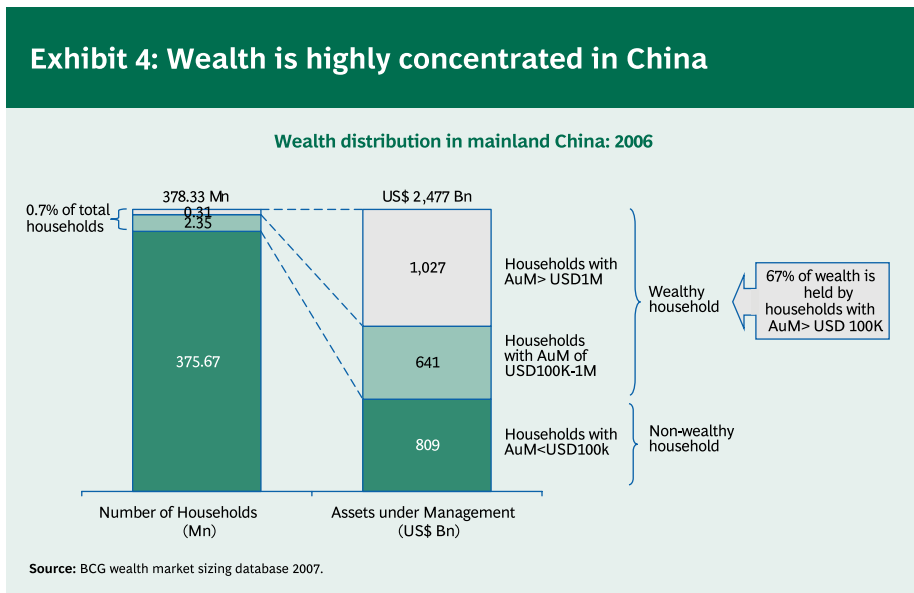
lion by 2011. Indeed, the Greater China region as a market is expected to reach a very sizeable US\$8.6 trillion in AuM by 2011. (See Exhibit 3.)

BCG estimates that the number of millionaire households in Asia excluding Japan grew to just over 1 million households in 2006, with 573,000 or 56% of these high net worth households located across the Greater China region. Consequently, China and Greater China are becoming increasingly important to international private banks as they seek growth outside of their home markets.

Wealth in China is highly concentrated. BCG research indicates that less than one percent of households in China hold more than 67 percent of the nation’s personal wealth. Even amongst these individuals, the richest 0.1 percent of the nation (with financial assets of more than US\$1 million) control approximately 41.4 percent of China’s wealth. (See Exhibit 4.)

Over time, we have observed that the rich are getting even wealthier. Since 2001, households with AuM greater than US\$5 million have steadily grown their share of the nation’s wealth from a 13.3 percent to account for a 20.1 percent, as both the wealth of each established wealthy household has grown rapidly and the ranks of established wealthy households have grown also from a mere 14,000 in 2001 to more than 48,000 in 2006. (See Exhibit 5.)

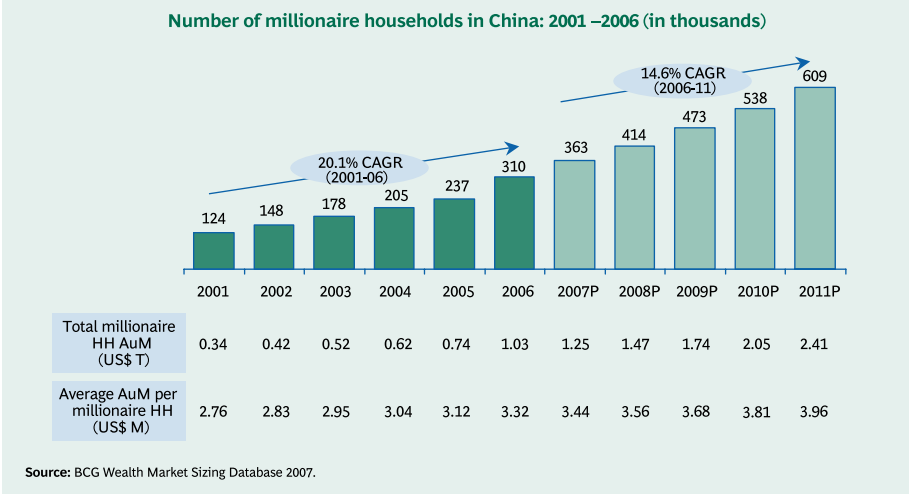
Indeed, more generally, we have seen a rapid rise in the number of millionaires in China over the past five years to 310,000 at 20% CAGR, placing China fifth in the world terms of the largest number of millionaires, ahead of many of the



## Exhibit 5: Over time, the rich are getting wealthier



## Exhibit 6: The rise of the millionaires in China



world's developed countries and only behind the US, Japan, United Kingdom and Germany. Over the next five years, propelled by the continued rapid expansion of the Chinese economy, BCG estimates that the number of Chinese millionaires could reach 609,000 by 2011. (See Exhibit 6.)

# Understanding the Nature of Chinese Wealth

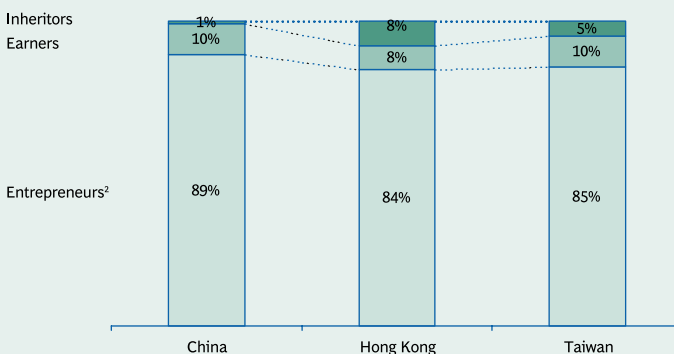
The nature of wealthy customers in China is quite different from those in the United States and Europe. To understand the nature of Chinese clients, it is firstly very important to understand the source of wealth. Much of the wealth in China has been created in the course of the rapid economic expansion of the past two decades. The wealthy in China comprise of primarily entrepreneurs that have made their money from high growth industries such as real estate, manufacturing, retailing, and information technology—sectors that have experienced strong growth and supported the nation’s economic expansion. By contrast, wealth in the United States and Europe comprises a mix of old, inherited money, and new, entrepreneurial assets.

BCG estimates that some 90% of Chinese high net worth individuals are entrepreneurs; indeed, most are first generation entrepreneurs where even more skewed entrepreneurial behaviour and preferences appear to be prevalent. (See Exhibit 7.)

## Exhibit 7: Entrepreneurs dominate private clients

Understanding of their behaviour is critical to offer the right value proposition

Estimated source of wealth for HNW individuals<sup>1</sup> of selected countries (2005)

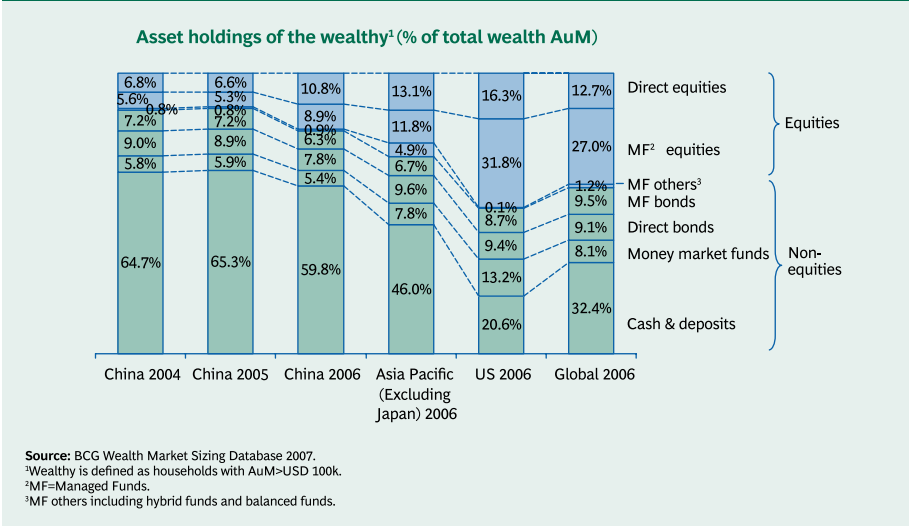


Sources: Government statistics; literature research; BCG analysis.

<sup>1</sup>With AuM of USD 1M or above.

<sup>2</sup>Includes inheritors who are entrepreneurs.

## Exhibit 8: Wealthy Chinese households trust cash



Given the entrepreneurial background of many Chinese high net worth individuals (HNWIs), we observe several important characteristics and analyze their key traits along several dimensions.

- “Bi-polar asset allocation”.** A typical wealth portfolio in China is structured quite differently from those in mature markets. We see that portfolios of Chinese HNWIs tend to highly bi-polar. Firstly, they hold significant levels of cash to provide security—though this has declined in recent years. This type of portfolio structure is common to other parts of Asia as well, where a significant part of the wealth in the rest of Asia non-Japan is held by ethnic Chinese households with potentially similar ways of thinking. Secondly, wealthy customers in China also are highly speculative and have a high tolerance for risk—likely a trait from their entrepreneurial backgrounds. They often pursue higher-risk investments and in their private banking portfolios, they tend to buy significant volumes of higher risk financial market trades (e.g., FX derivatives). (See Exhibit 8.)
- “Participators at heart”.** In BCG’s *Taking the Client’s Perspective: Global Wealth 2006* report, we discussed three types of private client investors: Self-directors (who manage the assets themselves), Participators (who rely on good investment advice and actively gets involved in the investment decisions) and Delegates (who rely heavily on banks and asset managers to make decisions on their investments). Given many Chinese HNWIs are first generation entrepre-

neurs who have built their own companies from scratch, they are used to being in control and making decisions. They want to be involved in the investment process. Many have a strong belief that they are capable of generating good returns and enjoy the experience of evaluating and making speculative investments.

- **“Traditional preference for direct investments”**. Many Chinese HNWI have traditionally felt more comfortable with investments in physical assets such as real estate or businesses, or in a transaction-related project such as investing in land relating to the creation of a new industrial or retail park, or increasingly, as Chinese equity markets have performed well recently, directly into the stock market. This is often considered to stem from the traditional highly entrepreneurial nature of Chinese wealth. A major challenge for private banks is to persuade HNWIs of the value of diversifying pools of wealth into different types of investment, with perhaps more complex structures around the investment or more diversity of underlying assets.
- **“Strong concerns over privacy”**. Chinese HNWIs generally do not like to disclose their wealth, either for fear of investigation over the source of their wealth (regardless of whether there are grey issues or not), or for concerns over attracting public attention to their wealth. Consequently, in selecting their private banks, they can be quite careful about approaches to banking security and client privacy, from how they are introduced to their relationship managers to the reputation of their private bank, from the domicile of their accounts to how they access their accounts.
- **“Multiple private banks are the norm”**. It is very common to find Chinese HNWIs using many different private banks to serve them, regardless of whether it is in onshore or offshore banking. Client discovery interviews tell us that onshore, HNWI clients are often keen to maintain privacy and discretion about the size of their wealth, and seek to spread their assets across a number of different banks. Offshore, the drivers are somewhat different. In offshore markets, HNWI clients are eager to gain new investment ideas that are brought to them by multiple relationships and like to maintain several banks to ensure competitive pricing for the many financial market trades they conduct.
- **“Emerging sophistication in private banking”**. Private banking is still a very new concept in China. Firstly, the onshore market has been traditionally limited by close regulation and product offerings have been constrained; and whilst the offshore market has been served as an opportunity, it is still relatively underdeveloped. Secondly, many Chinese HNWIs have yet still to experience entrusting wealth to a third party to manage. As we described above, many HNWI clients tend to be highly participative in the management of their

wealth, yet another indicator of the continued need to build trust. Thirdly, we observe many Chinese HNWI's are demanding in their target returns yet can also demand guarantees on their principal.

Given these characteristics, wealth managers need to consider how to configure their traditional business models to better serve the rapidly growing segment of wealthy Chinese entrepreneurs, which require differing client advisory approaches, service models, product offerings, organization set-up and economic models. We will discuss this further later in this report.



# Private Banking Models for China

**R**egulations play an important role in determining what private banking offerings are currently available to Chinese clients. Today, we observe there to be three broad private banking models that can be used to serve the Chinese market:

- Onshore private banking
- Onshore securities offerings
- Offshore private banking

**Onshore Private Banking.** Firstly, many Chinese banks and increasing numbers of foreign banks are launching and developing onshore private banking operations. Typically, these are traditional onshore banking operations with a focus on providing wealth management services to HNWI clients with enhanced service levels and differentiated branding from premium banking services. Product offerings have been limited to enhanced ‘retail-like’ products (due to regulation), though banks increasingly have been able to offer alternative investments in the form of retail structured products and investment trust vehicles, and the emergence of the Qualified Domestic Institutional Investor (QDII) program promises new overseas potential.

Wealth management products and services offered by Chinese banks are still relatively unsophisticated. Today’s offerings are still characterized typically as more “hardware” than “software”. Chinese banks have established luxurious wealth management centers across the major cities in China and launched new customer offerings based on the overall value of their local relationships. However, these superior facilities are not complemented by tailored products, service levels, and advisory expertise that are common in international markets. Current wealth management offerings from Chinese banks are very much a “one-for-all” solution rather than “differentiated” models. Wealth management centers do not offer tailored customer service models to meet the different needs of the various wealth segments.

One of the biggest challenges for most Chinese banks in setting up private banking operations remains an organizational issue. Chinese banks tend to be orga-

nized around geographic or product business units, and decisions are often made with limited coordination with other parts of the organization. Wealth management is a highly client-oriented industry, where clients expect special serving and customized offerings. Whilst a bank may set up a dedicated private banking business unit to handle high net worth clients, it is often difficult to encourage other geographic or products groups to either transfer their best clients or to provide support for products outside the mainstream offerings.

In the meantime, foreign banks have been busy launching their own onshore private banking operations. Given the strict regulations and slow licensing process to setting up new branches—each outlet requires a separate approval—the retail banking market is likely to be slow to materialize for foreign banks. But wealth management is a market that foreign banks can access more easily than the mass retail market: high-net-worth customers can be served from just a few outlets in any city; a select few and highly attractive customers can be targeted in focused districts; capital requirements and investments are lower; existing know-how, systems and experience can be leveraged against the local competition. Whilst products remain closely regulated, we are seeing onshore foreign banks begin to gain traction with HNWIs.

Despite these challenges, we expect the Chinese banks to respond to this likely onslaught of foreign competition—and to exploit their own advantages in the very rich Chinese wealth market. First, they do have strong, existing customer franchises that are rich in high net worth customers, although they will have to work hard to overcome organizational constraints and tap these highly valued clients. Second, Chinese banks have an extensive service network that could enhance accessibility and convenience for customers. Third, we expect Chinese banks to leverage their deeper understanding of the Chinese market and customer needs—at least until the foreign players catch up. Finally, Chinese banks have many relationship managers that have strong connections with local customers and whom they can train and develop into private bankers.

**Onshore Securities Firms.** A second potential onshore model is to serve high net worth clients through onshore securities firms. These firms can conduct securities brokerage, underwrite new securities issues, provide asset management services to clients and trade on their own proprietary books. Whilst the range of onshore securities remains quite limited, these onshore securities firms could be used to develop a private banking business. Institutions seeking to develop an onshore private banking business in China could look to leverage the research and broking capabilities from the securities business; the investment banking client relationships; and the licensing potential of a securities firm to build up an investment-led private banking business.

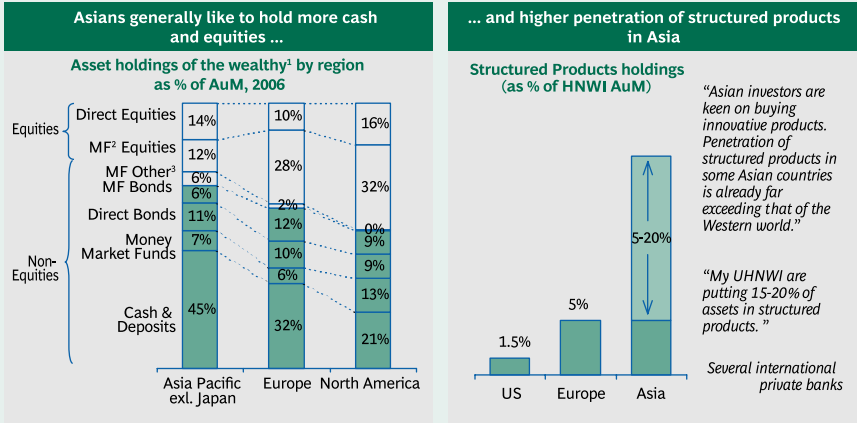
The only foreign securities joint ventures approved so far have been with Goldman Sachs (GaoHua) and UBS (Beijing Securities). Since these joint ventures were approved (and at the time of this publication going to press), the China Securities Regulatory Commission (CSRC) has stopped approval of foreign securities joint ventures in China. Nonetheless, we would expect that should this restriction be lifted and given the potential of the securities licensing, we would expect more foreign banks to seek securities joint ventures in China and to leverage them to develop their onshore Chinese private banking operations.

**Offshore Private Banking.** Finally, international private banks have used traditional offshore private banking centres, where regulatory constraints are significantly easier to manage, to serve Chinese wealth held outside of China. As is typical with offshore models, clients focus on longer-term wealth advice: almost exclusively on investment-related products, tax advantages, safe haven, discretion and security. (In onshore models, there is usually a more balanced and complete view of a client's financial situation: across investment products, liquidity management, credit lines, pensions, life insurance, and tax efficiency).

Relationship Managers (RMs) are typically based in Hong Kong or Singapore, and booking can happen pretty in much any offshore centre worldwide. Increasingly, we observe a growing shift to Hong Kong-based RMs to serve the rising tide of wealth created in the Chinese economic boom, given geographic proximity and the ease of access of Chinese entrepreneurs to visit Hong Kong. These RMs may be of different Chinese provincial ethnicity, as clients prefer to deal with someone able to speak their home dialect and from their own local culture. Similarly, there are many numbers of RMs based in Hong Kong who serve overseas Chinese entrepreneurs, who make their wealth in China and manage it offshore.

Typical products tend to be quite different to the traditional European private banking discretionary offerings. Reflecting on the highly bi-polar nature of asset allocation of many Chinese wealthy clients, both capital markets trades (such as FX derivatives) and structured products are prevalent. On the one hand, capital markets trades satisfy the desire to be participative in their investment approach; on the other, structured products enable private banks to target and offer alternatives to the large allocations to cash holdings. (*See Exhibit 9.*) With their participative investment approach, many Chinese clients like their RMs to bring interesting trading ideas to them and to participate in the decision-making of what to invest in.

## Exhibit 9: Right products have to be developed—cash and structured products tend to be popular



Sources: BCG Wealth Market Sizing Database 2007; Industry interviews; BCG experience.

<sup>1</sup>Wealthy is defined as households with AuM>US\$100k.

<sup>2</sup>MF = Managed Funds.

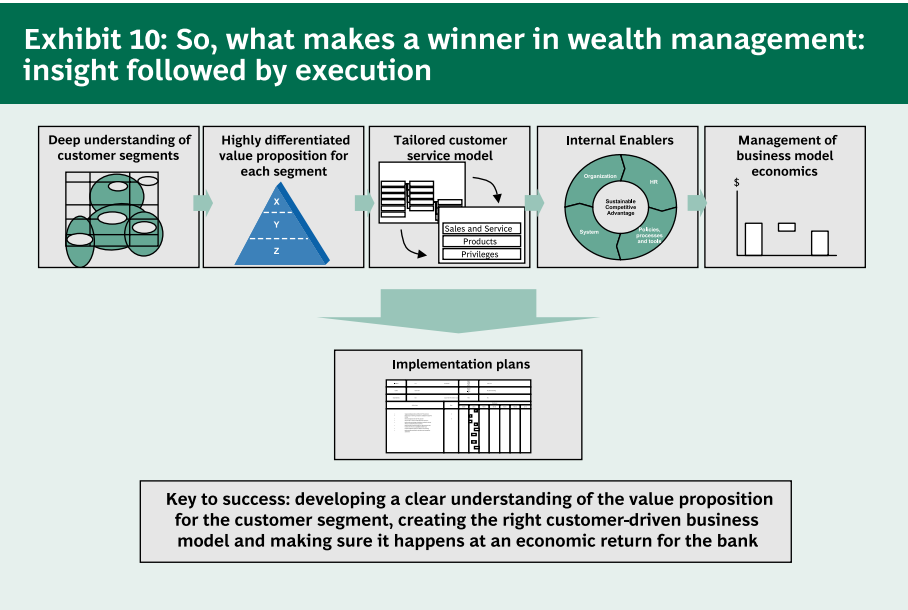
<sup>3</sup>MF Other include hybrid funds and balanced funds.

# Key Elements for Building a Leading Wealth Management Business in China

In BCG's experience, five key elements are critical for building a leading wealth management business:

1. Deep understanding of the nature and needs of customer segments
2. Highly differentiated value propositions for serving each segment
3. Tailored customer service models to deliver on the value propositions
4. Internal enablers: organization; HR; policies, processes and tools; systems
5. Management of the business-model economics

In this section, we will explain what is required in each element. (See Exhibit 10.)



# 1. Deep Understanding of the Nature and Needs of Customer Segments

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The key to any successful wealth management business is to understand the nature of customers and their needs, in order to build business models that appeal to different customer segments. For example, a bank might build an offering targeting “discerning higher income professionals” that would approach marketing, branding, and customer service quite differently than a model focused on “older, conservative, business-owner customers”.

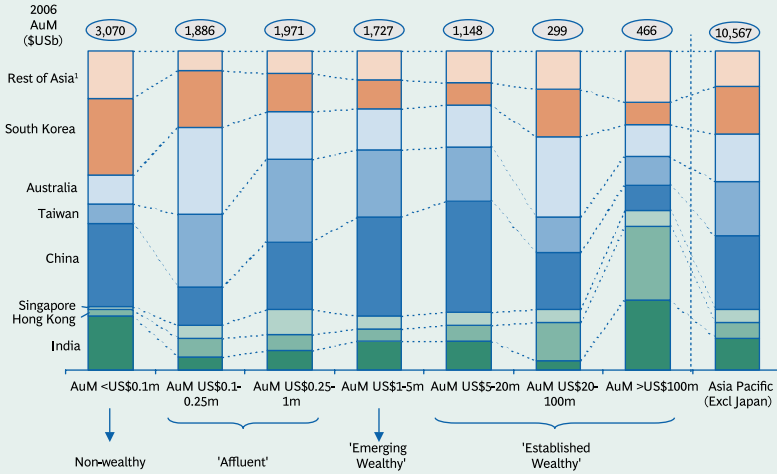
It is necessary to segment customers into different groups based on amount of AuM and their individual profiles; to size each segment; and to create a deep understanding of customer needs (in terms of products, services, branding, customer management, channels for interaction, and their overall risk-return profiles). Further, it is important to understand how competitors are positioned in pursuing these segments, and to develop approaches to identify, attract and retain target customers.

Leading banks in wealth management find that customer segments can vary substantially by country, both in terms of the definition of each segment (e.g. the minimum level of assets for qualification) as well as in receptiveness to various marketing and branding approaches. For example, one leading international bank focuses on promoting the sophistication and safety of its investment offerings in developed markets such as Singapore, whereas in an emerging market such as Thailand, it plays on highly-personalized service.

In its global research, BCG generally distinguishes among several different segments of wealthy investors (in U.S. dollar terms): mass affluent investors, or those with AuM of US\$100,000 to US\$1 million; emerging wealthy investors, or those with AuM of US\$1 million to US\$5 million; and established wealthy investors, or those with AuM of more than US\$5 million. Investors with AuM below US\$100,000 are considered retail customers. Clearly, these definitions of wealth can vary by market and such is the case in China.

Indeed, geographic markets for wealth management vary dramatically in importance across these different segments. In particular, we observe that for private banks targeting the US\$1-5 million and US\$5-20 million AuM client segments, China tends to dominate; whereas, in the US\$100 million segment, Hong Kong and India are important. So clearly, for private banks with service models geared for these US\$1-5 million and US\$5-20 million wealth segments, it will be very important to carefully consider how to approach the Chinese market. (*See Exhibit 11.*)

## Exhibit 11: China dominates the \$1-5m and \$5-20m client segments; Hong Kong has the largest population of ultra HNWI

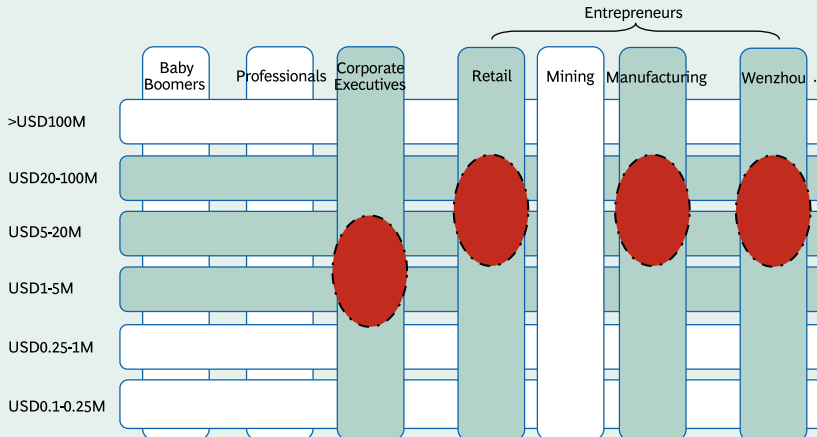


Source: BCG Wealth Market Sizing Database 2007.

<sup>1</sup>Rest of Asia excludes Japan but includes Indonesia, Thailand, Malaysia, New Zealand, Philippines and Pakistan.

## Exhibit 12: Develop segment-specific client strategies

### Illustrative segmentation

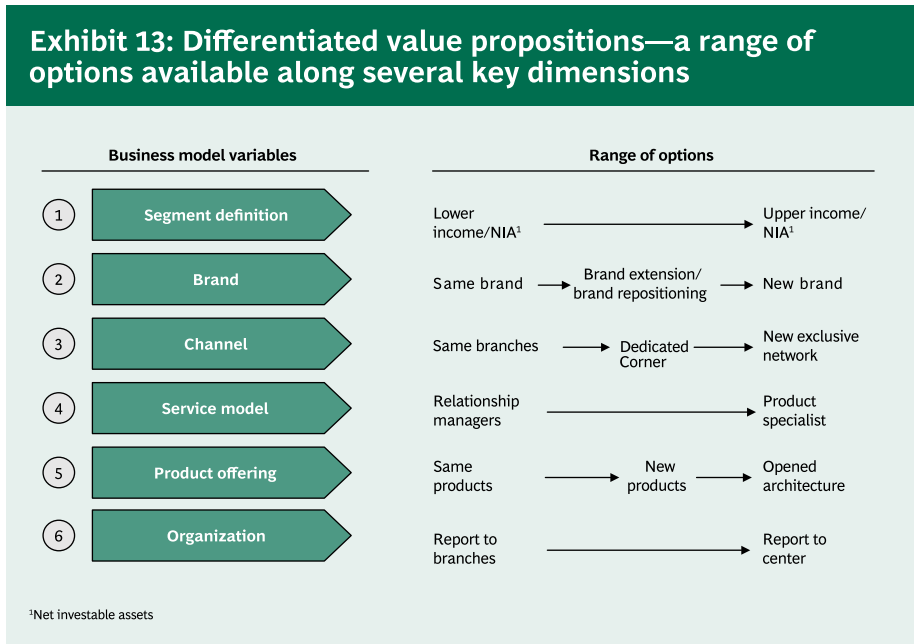


BCG suggests segment specific client strategies. (See Exhibit 12.) A client segmentation framework might cover wealth bands, demographics and source of wealth. Indeed, for the large entrepreneur segments, we might also consider which industries have been growing most quickly and which are the sources of highest wealth creation, what high net worth clients in each of these industries are seeking in terms of advice, products and services, and even how might their preferences vary by their home locality.

## 2. Highly Differentiated Value Propositions for Serving Each Segment

The next step is to create a highly differentiated value proposition to serve each customer segment, leveraging the insights from Step 1. This involves making explicit choices about what to offer based on what customers want and value. (See Exhibit 13.)

For offshore private banking, there is a plethora of products that can be offered, though as described earlier, there appears to be a preference for offerings that satisfy the bi-polar nature of Chinese asset allocation.



For onshore private banking, there are clear constraints on which products banks in China can offer. Products such as offshore investments, IPO investments, and hedge funds—that are typically offered by international wealth managers—are not yet available in China. However, there are opportunities to develop a range of tailored products specifically for wealth management customers, and many of these are not yet common. Such products typically fall into three categories: financial, advisory, and lifestyle. For example:

- Tailored financial products might include specialist trust vehicles, private equity and co-investment funds, and all-in-one insurance programs (together with partners)
- Advisory products might include wealth education, one-stop financial advisory services, and discretionary wealth management plans
- Lifestyle benefits might include privileges at exclusive clubs using corporate memberships obtained by the bank, emergency assistance services, and 24/7 Concierge Services for entertainment and leisure activities

### 3. Tailored Customer Service Models to Deliver on the Value Propositions

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Critical to being able to deliver on value propositions is translating them into specific customer requirements and into the methods by which the bank operates its wealth management service offerings. (*See Exhibit 14.*)

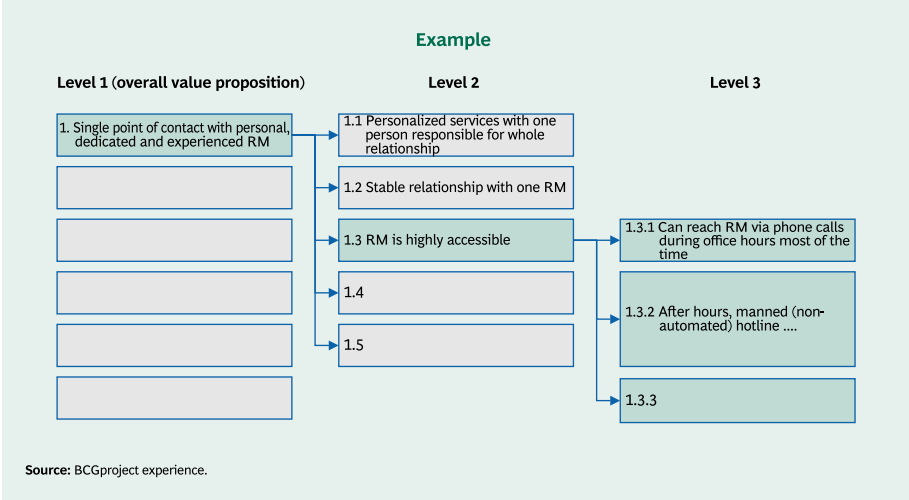
Such a service model needs to be carefully set up so that it is consistent among all staff and locations; is repeatable and sustainable over time; and provides a customer experience in line with the overall brand of the wealth management offering. In China, one often observes products and services that differ greatly and do little to reinforce the VIP nature of the wealth management business.

### 4. Internal Enablers: Organization; HR; Policies, Processes and Tools; Systems

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Successful execution of the new wealth management business requires realignment and changes to enabling platforms. There are four key areas that require attention to make a wealth business work: organization, HR, systems; policies, processes and tools.

## Exhibit 14: Cascade high-level value proposition into specific customer requirements



- Organization.** To enable a strong focus on wealthy customers, it is critical to work out how the management of VIP customers will be coordinated across branches and business units. This is particularly complex in China, where organizations are large and many banks have historically had geographic- and product-oriented organizations. Often, we see banks that need to realign the reporting lines of relationship managers and set up separate and dedicated acquisition teams for private banking. Such steps lead to far more formalized accountability for managing these very important wealthy customers than can be found in the traditional retail bank. Often, there may be internal client ownership issues to address.
- HR.** There are many elements of human resources that can greatly improve the effectiveness of wealth management teams, such as: recruitment, training, performance management, compensation, career management, and retention. In our discussions with Chinese banks, the top issue cited in this area is that the industry talent pool is weak, making it very difficult to recruit and retain experienced relationship managers (RMs). Many banks seek to poach good RMs from other institutions.

However, given the potential size and growth of the wealth management industry, poaching will only drive up the cost of RMs for the future. Therefore, we would encourage banks to invest in training their own talent pools and to make the development of wealth management expertise part of their institutional capability. BCG has helped several international private banks set up

training academies, particularly in Asia where growth is high. These initiatives have yielded considerable success.

- **Policies, processes and tools.** Managing wealthy customers is quite different from managing mass market retail clients. It is critical that brand perception is reinforced by the overall customer experience, as this will be the factor that builds the long term sustainability of any wealth business. Key areas to look at include: developing improved RM sales processes, a holistic client wealth advisory process, creating an emphasis in service differentiation in RMs' planning and tracking activities, adopting a formal tracking process for the management of wealthy accounts, and developing a systematic process for account allocations. Further, banks need to have well-defined approaches for migrating customers from one segment to another, as today's top mass affluent customers are often tomorrow's wealthy VIPs.
- **Systems.** Today, many Chinese banks' customer information management systems are inadequate for wealth management. Typically, these systems need to be able to capture a broad range of relevant customer attributes, far beyond merely product-related data; enable the analysis of customer behavior and preferences; and identify wealthy customers and place them into differentiated customer support segments. Further, platforms to support wealthy customers must be able to provide a holistic picture of the customer's entire relationship with the bank across all products and channels. These systems need to be complemented by integrated sales, service and self-service delivery platforms that allow convenient and efficient access by RMs and clients alike.

## 5. Management of the Business-model Economics

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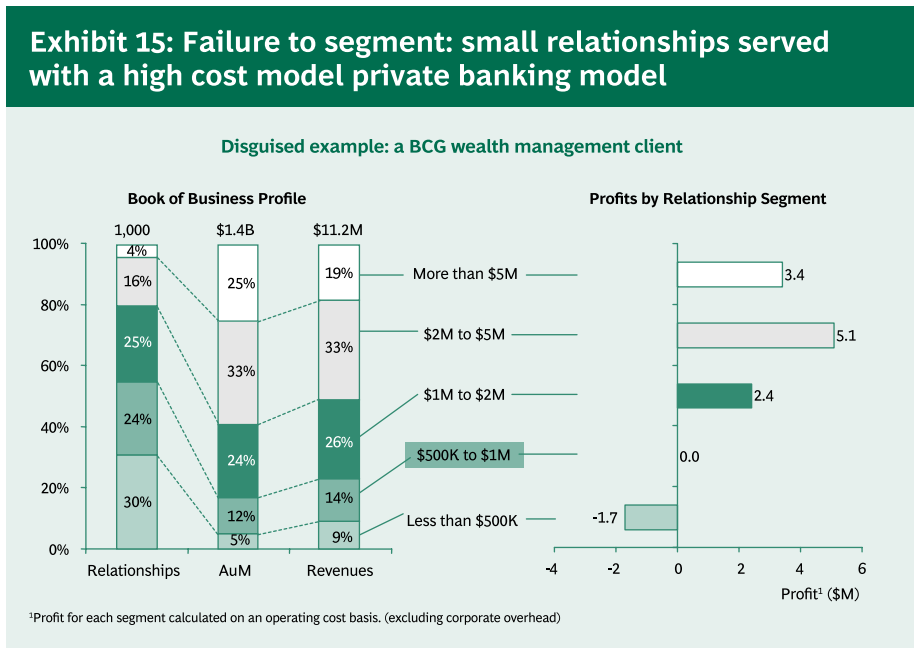
Finally, in any business, and even more so in wealth management, superior management of the economics is critical. Additional products and services always come at a cost. Although it is much more expensive to serve wealthy customers, banks can reap the rewards of much larger and more complex relationships, all of which should translate to higher bottom-line profitability—but only if the economics are carefully managed.

In China, this is vitally important as most banks are used to serving only mass market retail customers and expect the economics to be similar. Talented and experienced relationship managers demand higher compensation. Priority and higher-service banking require new processes and additional overhead. More complex products require more sophisticated capabilities and investments. Integrated views of customer relationships require investments in new or modified systems. And so on.

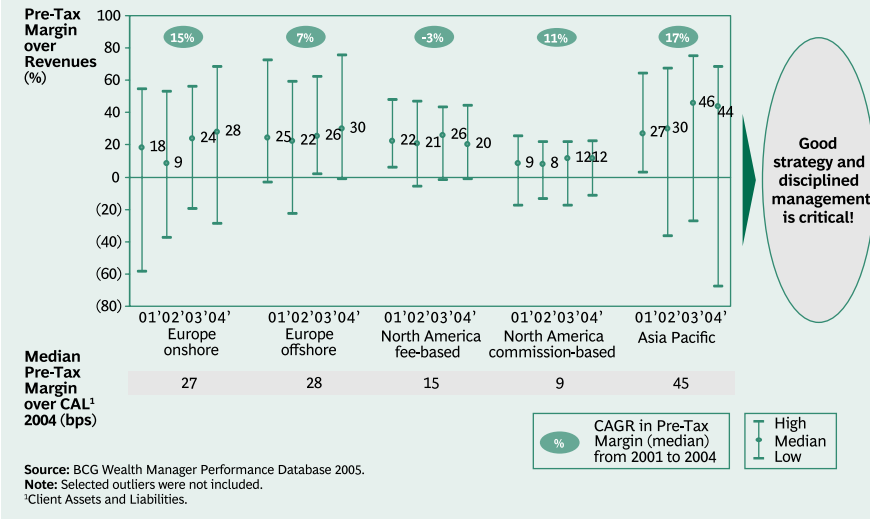
Serving customers with an inappropriate business model for that segment almost certainly will be unsuccessful and/or unprofitable, as either the cost of providing the higher service level will not be fully recouped in the revenues that can be generated. Or, customers with higher levels of wealth will feel under-served and move to competitors. For example, at one wealth-management institution, the organization was serving small clients with a high net worth model. Consequently, some 30% of all clients were unprofitable and a further 24% made no money for the institution. (See Exhibit 15.)

Over the past five years, BCG has benchmarked the wealth management businesses of approximately 100 financial institutions across the world. We have observed that all regions and all types of business models can be profitable, although wide variations exist across competitors. (See Exhibit 16.) Good management of the economics is critical. Some key success factors include:

- ensuring careful customer segmentation and tailoring the value propositions and business models to these segments
- maintaining discipline on how you serve customers, including not allowing accounts smaller than your minimum balances and being vigilant on prices
- controlling costs tightly—almost all top performers have low-cost manufacturing and operations and can reinvest the savings in driving sales and marketing



## Exhibit 16: All regions and business models can be profitable —but wide variations exist across banks



- being disciplined in managing RMs, evaluating their performances regularly, and paying for real revenues delivered

In summary, it is possible to make money with different business models, value propositions, and targeted customer segments. The key is to make sure that one is clear about which segments to pursue, what the unique competitive advantages might be, and how to align all aspects of the business with strategic goals.

The rising wealth in China is creating many opportunities for Chinese and international banks to prosper in serving high net worth clients. The next several years will be certainly an exciting period. Whether institutions will succeed or not depends on many factors, but most importantly, the critical driver will be whether they develop the right business models with the right economics to serve their target segments.



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