№1, 2020

Thought
Leadership.

Becoming a Digital Wealth Leader

Steps to a Successful Transformation

additiv

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Executive summary

- **Now is the time for digital action** – Although financial institutions have been talking about digitizing wealth management for several years, this has now become a strategic priority if they want to be able to show net revenue growth going forward. While the requirements of clients are relatively straightforward, digital solutions will change the way wealth managers meet these needs. This makes it critical for industry players to be able to prove their value-add via a level of automation they haven't been able to achieve before.

- **Respond to evolving client needs** – Given that the expectations of the next generation of clients are driven by their experiences with online retail offerings, wealth management providers need to deliver far greater levels of digital proficiency. Availability anytime, anywhere, as well as speed, ease of use, transparency and seamless omni-channel services and fair pricing are key success factors in today's landscape.

- **Augment the role of client advisors** – Client advisors will continue to play an important role in managing the overall client relationship in this new world of wealth management, combining the human touch with technology as an enabler to offer more customized and relevant solutions directly to individual clients. The digitization journey therefore needs to start by optimizing the processes of the most effective and productive client advisors – with the dual goal of improving time-to-market and customer experience. Wealth management firms also need to reduce the administrative workload of advisors by giving clients more control and functionality to be self-directed.

- **Turn higher value-add into more revenue** – Once wealth management firms have implemented both internal and external efficiency measures, client advisors will be able to focus more time on maintaining close client contact. In turn, this should lead to more frequent discussions about other potential solutions that create greater revenue streams.

- **Get prepared to go digital** – The success of digital transformation in wealth management is only possible if firms are 'ready' for it. Being prepared starts internally with a top-down process that crafts the 'digital vision'. From here, suitable business and operational models are defined and formulated into the digital strategy.

Section 1

The common approaches to digital today

The wealth management industry is faced with challenges such as intense competition, fee compression, low or negative interest rates, stricter regulations and evolving customer needs. As a result, cost-income ratios have increased for many financial institutions as high as 80%.

Necessity is the mother of invention.

In a slow revenue growth environment, banks have to rethink their strategy. In order to control the bottom line, banks have to cut their expenses. The only way to do this effectively is to swap labour with technology. For the first time technology is ready and clients are ready for technology.

Boosting bank ROE by integrating innovation initiatives

However, it has proven difficult for banks to innovate in ways that deliver «at scale» impact. By «at scale» we mean delivering significant growth in the form of new processes, products, services, experiences and business models. According to McKinsey research, currently 56 percent of banks globally are not generating their cost of equity (COE), with global banking ROE at 10.5 percent in 2018, hovering around its long-term average. For European banks to generate their COE they would need to lift revenue by 15 percent or reduce costs by 20 to 25 percent. So, despite all the activity noted above, very few banks are effectively using innovation to elevate their performance.

Source: McKinsey, July 2019

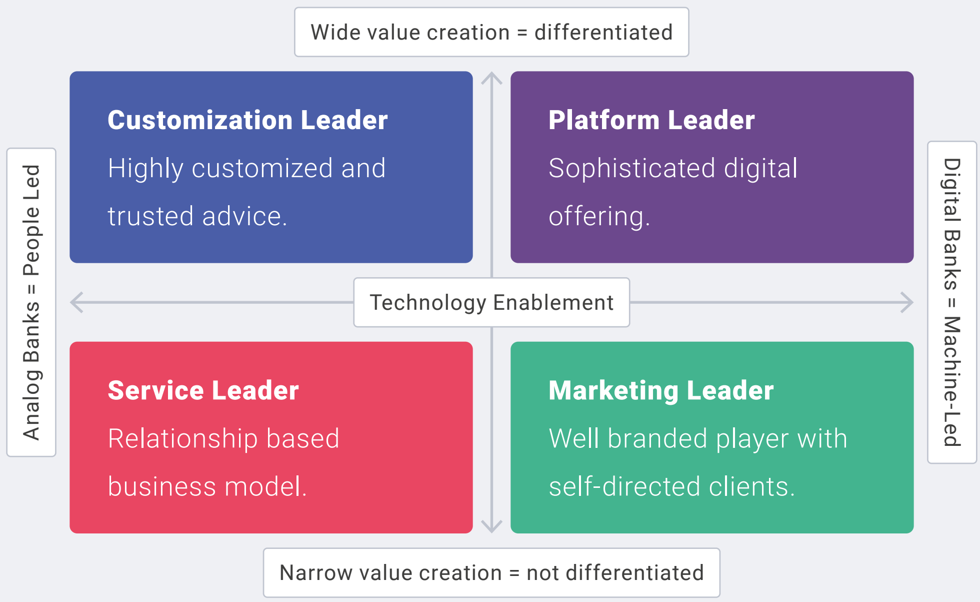
Although the digitization of the wealth management industry is not a new development, many financial institutions are realizing only now that they must address this topic with high priority to show again a net revenue growth in the future. Automation goes together with standardisation. Services and solutions which are highly customised are commercially not interesting for digitization although nowadays software systems are allowing deviations within a given process.

A clear strategic positioning in terms of value creation (narrow versus wide service offering) and the level of automation (machine versus people led) is of outmost importance. We are distinguishing between 4 main strategic scenarios.

The right positioning is crucial for success.

Customization leaders

- These financial institutions have a sizable private banking business.
- A differentiated, advisor-based offering is used to cover the wide-ranging needs of clients.
- Technology is typically used to automate back-office processes and make the valuable front-office staff more efficient. There is also a strong trend towards increasing the self-service offering for selected products.
- These firms adopt a dual – or "hybrid" – approach, where the advisor remains a key part of the offering but has better tools to work with to execute end-to-end processes for the client and spend more time on services where more of a personal interaction is needed.



Source: additiv Analysis, combined with Gartner publications July 2018

Service leaders

- These firms tend to be smaller private banks and wealth managers.
- The value proposition is mostly relationship driven – based on a good, reliable service but the offering is fairly narrow and limited.
- Given changing client behaviour and expectations, there is increasing price pressure, plus the higher regulatory burdens create challenges for this type of niche.
- To maintain a profitable and growing business by controlling costs and extending the offering, joint ventures and mergers and acquisitions are one option. These firms can only remain independent if they introduce a superior hybrid digital offering.

Platform leaders

- These organisations are typically the leading banks, both regionally and globally. They cover all client segments and are full-service in terms of their product range.
- It is common for these firms to be platform leaders within a country, region or even globally – requiring huge IT investments to stay up-to-date and position themselves for future growth.
- These banks tend to have very sizeable in-house IT departments to maintain what has probably grown into a very complex legacy core banking system.
- Given that time-to-market is a key way for these firms to differentiate their offering, a potentially effective route is to collaborate with specialist fintechs. These partners are not only faster and nimbler; but the cost is far less that an in-house IT team.
- Although this might seem a risky strategy, the advantages include the development of specific internal processes, customized front ends and tailored services.

Are Super Apps like Grab, Kojek, Alipay etc. disrupters?

Marketing leaders

- This group of firms represents a new type of wealth management provider: a company, or Super App, with an existing digital channel that has a large number of existing users, which leverages its platform to introduce financial services and products to these existing clients.
- They lack specific expertise in wealth management, so they start more simply by offering payment systems and e-wallets.
- The next step, to offer selected banking services that are heavily regulated, involves partnering with an established fintech and/or large financial institution to provide an end-to-end wealth management offering.
- The experienced PR and marketing arm of these disruptors is typically strong enough to attract clients despite the range of the wealth offering, at least initially.

How banks can react to big tech's entry into financial services

Here we talk about how banks might think about a potential massive advance of big tech players (e.g., Google, Amazon, Tencent, as well as their more local equivalents) into financial services. Banks have been under pressure from these firms for some time. However, there's a strong chance that this pressure will intensify as big tech firms increasingly leverage their strong consumer franchises and digital expertise to compete with banks.

Big techs have not yet taken significant market share outside China in financial services and tend to avoid regulated markets; and when they do look to enter banking, they usually start by partnering with banks. Consider big tech's approach as disintermediation rather than direct entry into the regulated domain of financial services, or of their focus on the most capital-light and digitizable areas of business that are closest to their core. Take Amazon's foray into small business lending, Apple's entry into payments and consumer finance, or Facebook's announced launch of Libra, a cryptocurrency.

It is imperative that banks respond to this potential now, as once big tech firms achieve scale it will become near impossible to compete on price, or with their ability to offer a distinctive client experience that builds consumer loyalty and trust. Ultimately, if not resisted, the tech attack will destroy the financial services industry's margins—by taking some themselves and returning the rest to consumers.

For banks of all sizes, the first imperative is to understand the threat of big tech incursion, and the new competitive landscape, build an objective assessment of your own capabilities and market strengths, and develop a plan of response. It is important for banks to act on all these fronts if they wish to maintain their position in the face of a big tech move into financial services.

Source: McKinsey, November 2019

Section 2

What clients want

The requirements of wealth management clients are relatively straight forward. Interesting is how these needs have been covered in the past and how they will be covered in an environment with higher automation and digitization.

The five main requirements when developing any type of offering to wealth mangagement clients

1	2	3	4	5
Trust	Privacy	Service	Performance	Pricing

Pre-requisite for any business.

Trust

This is fundamental to every business relationship. In banking this is primarily a counterparty risk consideration, so without trust, onboarding new business or partners can be very cumbersome, or even not feasible. This gives sizeable and established players a competitive advantage, and explains why most challenger banks, Super Apps and B2C fintechs use the traditional financial institutions for custody services.

Privacy

Although bank secrecy no longer has the same meaning following changes in legislation, exchange of information rules and other initiatives to create a more transparent world, it is crucial for clients that their financial information is kept private and confidential. Especially in emerging markets where the concentration of wealth but as well the potential criminal energy is much higher!

Service

Wealth management is a service business, with success closely correlated with the level and standards of care that an institution provides for customers. While traditionally this has been achieved by personal interaction with an advisor, the last few years has seen the definition broadened to include a seamless digital journey, available 24/7. A financial institution must review the quality of the interaction with its client independently from the channel that delivers it.

Performance

Many wealth management clients consider performance to be more important than anything else, creating the driver for choosing which firm to maintain a relationship with. In reality, however, it is difficult to measure performance – private clients often think in absolute terms, yet performance is relative to a benchmark. With a multi-asset portfolio in particular, it is difficult to define what the right benchmark should be and, further, there needs to be consideration over how much risk exists in the portfolio, and how this impacts the performance relative to the chosen benchmark. Nevertheless, every firm must aim to produce alpha, both within a clearly defined discretionary mandate and via an actively managed fund.

Pricing

Clients tend to be very price sensitive for most products and services. This is because it is difficult for an advisor to demonstrate correlation between good advice and performance. Further, there is intense competition within the industry. Firms must pay a lot of attention to how they price their offering, also with consideration to factors like transparency, reliability, simplicity and alignment of interests.

Customization through technology

There is no doubt that client advisors will continue to play an important role within all types of wealth management propositions in managing the overall client relationship. However, technology will play an ever-more critical role as an enabler for wealth management firms to offer highly customized solutions directly to clients at lower marginal costs. Helping to fuel this further, the automated analysis of structured and unstructured client data will allow banks to increasingly personalise the solutions according to specific client needs.

How to drive growth in Wealth Management?

It is important to clarify that digitization doesn't mean standardization. To the contrary, it is about engaging clients on a personal level and delivering additional, tailored products and services.

Grow your customer base

- New client segments are targetable (e.g. young, tech savvy, highly busy)
- Activate unserved and underserved clients (e.g. mass affluent)
- Introduce a new product offering (tailored for self-service)
- Attract price sensitive clients (through price segmentation)

Grow your profitability

- Higher business volume correlates with more revenues
- Increased activity level of your clients is leading to higher revenues
- Marginal costs are close to zero (no additional costs for next transaction)
- Higher efficiency of your front staff (higher load, focus, lower admin)

Engage your clients

- Higher loyality through increased client touch points
- Transparency and client satisfaction are closely correlated
- Push customized news and information to your clients
- An omni-channel client experience is considered the gold standard

Meet the needs of your clients

- Service availability 24/7 from everywhere
- Clients are expecting intuitive design, ease of use and real-time
- Clients are used to speed and convencience of online retail
- Clients demand choice in how to deal with service providers

Get a deeper insight into your clients

- End-to-end processes are allowing to collect new client data
- Use this data to understand, innovate and engage your clients
- Spotting trends in client behaviour are allowing to kick-off new marketing initiatives

Risk Management is a crucial success factor.

Reduce your risks

- Automated end-to-end processes are allowing the dedection of fraud
- Client Identification (CI), Know your Client (KYC) and Anti Money Laundering (AML) can be controlled independent from human element
- Cyberattacks are demanding advanced authentication methods

It is worth emphasising two of the key advantages for banks:

1. Increasing revenue via higher activity levels in terms of transaction volumes for existing clients, which only incurs marginal additional cost.
2. Attracting new client segments, especially next-generation clients that have to be approached and on-boarded at an early stage. (In private banking, the average client remains with an institution for about 12 years, meaning the bank must replace around 8% of its clients every single year to maintain its asset base in a stagnating stock market environment.)

Section 4

Winning next-generation and new middle class

In more developed and established wealth management markets, such as Europe, clients tend to be older. The median client age is roughly 60 years old. Further, until recent years, most of these clients had relatively straightforward needs, especially with regards to any offshore banking. This has led to next-generation clients often being neglected, with their needs not generally considered.

As a result, there has been minimal attention paid to the various behavioural differences between the generations. For example, while the first-generation wealthy typically seek more personal attention, their children are looking for greater efficiency, fairer pricing and outperformance.

Digitalization allows to lower profitability threshold

Over 10M High-net-worth	**Special Solutions**	– Personal advice seeking – Institutional product needs – High price sensitivity
0.5M to 10M Middle class	**Wealth Management-as-a-Service**	– Digital Hybrid approach – Looking for added value – Accumulation of wealth
Up to 0.5M Retail	**Wealth Inclusion**	– Digital Self-service – Seeking for access – Simple, easy & affordable

Source: additiv Analysis, January 2020

Further we are observing a shifting landscape and mindset in all the emerging markets. There is a rising middle class of young professional who have embedded online services in their daily life. The expectations are driven by their experiences with online retail channels.

Five predictions for the future of wealth management

Evolution brings change, and the wealth management industry is certainly not an exception. Technology is empowering clients now more than ever, and the millennial generation is beginning to grow and mature financially. The business model of the future is changing.

PwC, for example, found that 47% of ultra-high net worth individuals regularly use Facebook. And, according to Deutsche Bank, “More than 33 percent of all new banking business with customers between the ages of 16 and 39 is conducted fully on the Web.” Clients of the future have different goals and preferences.

As baby boomers age and millennials inherit assets, we’ll see quite possibly the largest generational wealth transfer in human history. While the client base is getting younger, financial advisors and wealth managers are not. A recent study conducted by Ernst & Young identified that only 22% of wealth managers today are under the age of 40. Moreover, only 40% of aging financial advisors say they have a concrete succession plan in place for their client base after they retire. Attracting future talent for the next generation of financial advisors is certainly on our to-do list.

The age gap also means somewhat of a disconnect between clients and their advisors. As Gen Xers and millennials turn toward apps and robo-advisors, the industry will be forced to embrace the digital transformation to help bridge the divide. Adjusting to the clients of the future won’t involve merely tweaking a website, creating an app or offering increased investment options. As technology changes the way firms and clients interact, the firms that will succeed will be those that combine a digital approach with overall integration and a client-centric model. Technologies like robo-advisors will work alongside – not in place of – the next generation of wealth managers, who will be tasked with tomorrow’s digitally-enabled client base.

Source: Forbes, May 2018

Section 5

The 3-phase model

Unfortunately, there is no "one size fits all" solution. The key success drivers of the actual business model have to be analysed very carefully before a digital journey can be defined.

Listen carefully to your clients!

If you don't have a viable sourcing channel for new clients today, it is a wrong assumption that a digital journey will solve this problem. On the other hand, if you are gifted with a high number of existing clients, ideally using already some digital services, it is very likely that an additional digital offer will receive great acceptance. Further we don't recommend to change the distribution channel drastically. If your clients are used to a high service level and to personal interaction with an advisor it is the right approach to introduce a digital journey gradually with the support of the client advisor.

3 Phases of Digitization in Wealth Management

1	2	3
Internal Efficiency Your valuable client-facing advisors are operating highly efficient.	**External Efficiency** Offer an extended self-service channel with great user experience.	**Value Proposition** Provide addtitional services based on digitalisation.

Source: additiv Analysis, January 2020

Phase 1: Internal Efficiency

The digitization process within a financial institution doesn't have to be started directly at the client front. It makes often sense to start internally and optimize the processes around your most valuable client-facing advisors, thereby improving time to market and customer experience. Greater efficiency with your advisors will correlate closely with your top line and keeps their motivation level high. The advisor requires easy access to all relevant client information to reduce the meeting preparation time and driving a successful dialogue with the client with a high closing probability. The installation of end-to-end processes are minimizing the post meeting workload.

Phase 2: External Efficiency

To reduce the workload of your advisors further, an increasing number of tasks need to involve the client directly and give him the control over initiating the process. This is clearly a sensitive topic and has to be done carefully. For payment services this is already a widely accepted standard. A gradual introduction of new digital journeys supported from the client adviser within a hybrid model promises highest chance for success. Crucial for training purposes is that the frontend of the advisor and the client is the same.

Digitalization at the client front always starts with monitoring!

Account and portfolio reporting is a very time consuming task for every client advisor. A 24/7 available mobile client cockpit with state-of-the art login security features and seamless user experience should be an easy sell to a client and is rapidly becoming an expected feature from a client perspective. It can still be a differentiator to the competition if done really well and the client uses the cockpit on a regular basis.
Once a client is digitally on-boarded and he is using the client cockpit frequently the step to introduce a real product offering via this channel is straightforward. A first step could be to provide a cash management offering in several currencies. Again, this has to be intuitive and simple. From their advisory extensions to single securities like ETFs, funds, equities etc. are a logical next offering step. Important is only that the client is receiving the right guidance within this process. A proven approach is to work with example portfolios in different risk categories which are customizable. Client risk profiling is either already done during the on-boarding process or could be done at this stage.

Beside a pure advisory based offering it is of course recommendable to introduce as well a discretionary offering with a higher recurring revenue potential. This could be either simple in the sense of offering an in-house discretionary mandate per risk profile or offering really a multi mandate approach with different strategies from internal and/or external providers. Using highly branded partners could stimulate sales. The portfolio management for these mandates can be done either the “classic” way or with fully automated algorithm based portfolio optimisation engines with rebalancing features. In case you like to set the minimum investment amount low, there is no choice than having a highly automated and scalable solution in place with very low marginal costs. Besides having an attractive product offering in place, pricing has to be considered very carefully. With a lower service level, client’s willingness to pay higher fees is decreasing significantly.

If there is not a price difference between self-service and an advisor led sales process, the client's motivation won't be sufficient high to go through the difficulties to understand and feel comfortable with a pure digital journey. In any case pricing has to be clear and fully transparent. For a very homogenous offer – also in terms of client size - you might even want to consider a subscription based pricing model and not only the classical volume based fee model. As low marginal costs are applying, volume is the key commercial success driver.

Phase 3: Value Proposition

After increasing the internal efficiency of your advisors and the involvement of your clients in the process, you might want to consider to use the power of digitisation as well to extend your existing value proposition.

Ready for Growth!

Your advisors should have now some free capacities and the basic needs of your clients are covered. In order to keep client proximity high, more complex client solutions with an additional revenue potential can be introduced. As an example: if you like to increase the share of wallet with your existing clients you would aim to introduce services like financial planning, asset structuring for the next generation, access to "real" assets, overlay risk management and global custody solutions – just to mention a few. We are recommending to cover these topics within a hybrid approach.

To summarize the ambition in this final step of digitization is to become the client's main point of contact for all finance related topics. The smart interaction between self-service digital channels and the client advisor should allow every client to define himself his sweet spot. It is clearly not identical for a technical savvy millennial and a "Baby Boomer" who is standing shortly before his retirement.

Section 6

How to transform Your organization

Digital transformation is only successful if digital readiness is prepared very diligently. This must start internally within a top-down process. From the digital vision a suitable business and operational model must be defined with leads to the digital strategy of a financial institution.

Internal Transformation

The implementation of such a strategy requires strong internal support. Management and employees must understand and buy-in to the strategy. As the change is in many cases fundamental, this can be a lengthy and cumbersome process. Many employees must leave their comfort zone and adapt their working processes to the new reality. Often this goes together with the fear to lose the job or not having the necessary qualifications.

The RM is the key interface.

Especially at the interface between the client and the financial institution it is extremely important that the new strategy and offering is transported the right way to the client. Typically for bigger clients this is the personal advisor with a long-term trusted relationship. If interests are not aligned it will be very difficult to enforce new processes and to launch successfully a digital service offering for the client. A simple solution could be to attribute all revenues from a client, independent from the used channel, to the client advisor. If a client advisor is realizing that the digital journey helps him to be more efficient and to achieve his targets faster, he will adapt very timely.

Factors of Digital Readiness

Digital Readiness has to be carefully orchestrated to be successful. Every short cut will put the final success at the client front at risk.

Internal Transformation

1 Digital Pre-Requisites
- Vision & Mission
- Business Model
- Operating Model
- Digital Strategy

2 Digital Enablers
- Digital DNA
- Organisation & Governance
- IT Infrastructure
- Digital Intelligence

External Transformation

3 Digital Offering Management
- Omni-Channel Customer Journey
- Omni-Channel Products & Pricing
- Omni-Channel Performance Management

4 Digital Leverage
- Digital Branding
- Digital Marketing
- Social Engagement

5 Digital Experience
- Customer Self-Service Offering
- Front Staff Capabilities
- Customer – Bank – Interaction
- Content Management

Source: additiv Analysis, October 2019

External Transformation

Once the internal transformation is on track, the firm must articulate the message to existing and potential clients. Yet just having new technology or an omni-channel solution is no guarantee of success – instead, it requires the right combination of good services and products, with a great client experience, at a competitive price.

Self-service vs. hybrid?

Firms must carefully decide which offerings will be self-service, which will be possibly hybrid, and which will be advisor-only. Further, it is advisable to introduce different self-service journeys gradually.

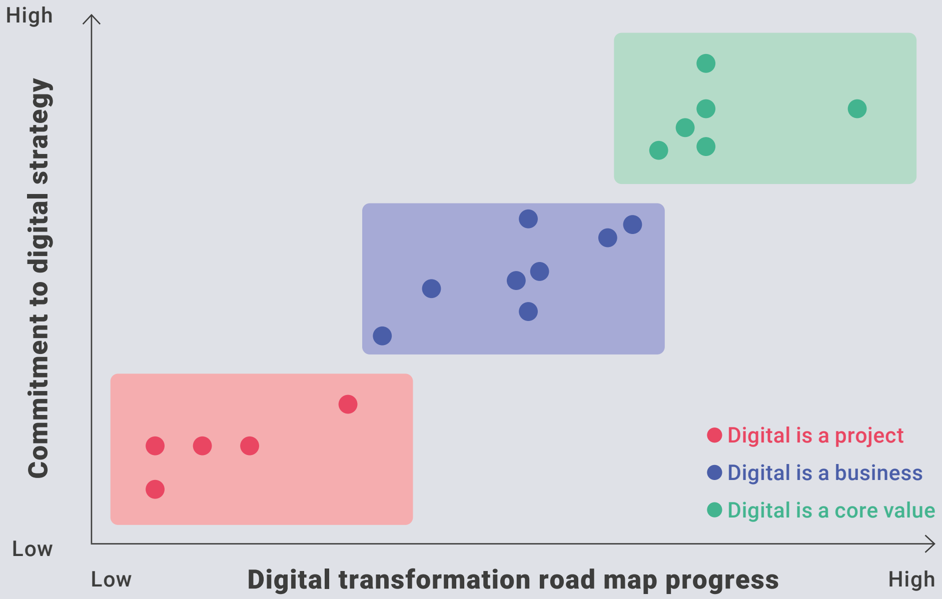
It is difficult to assess the digital readiness of existing clients, so organisations need to be patient and prepared for this. A financial stimulus is potentially an effective approach to motivate, or convince, clients to start using a self-service offering.

In such cases, the institution might implement a penalty system that charges higher fees to clients who continue to transact and interact with their advisors in traditional, non-digital ways. While this approach is only advisable in limited cases which rely on behavioural change to drive the shift towards self-service, banks cannot underestimate the importance to their bottom line of efficiency gains and/or increases in transaction volume.

For new clients, a well-planned communication and PR strategy is essential, given the challenges of acquiring new individual clients as well as targeting new client segments. Targeted campaigns are required via traditional channels and social media, with the messaging tailored for the specific client segment.

Banks want to become digital banking leaders

For most incumbant banks this is a very gradual process. From project status until it is a real business can take years. This makes it even more important for banks to start this transformation process now very timely.



Source: A.T. Kearney analysis , July 2019

Section 8

Closing Remarks

Digital readiness from clients is increasing in today's world very rapidly. Client behavioural patterns we see today in online retail will find their way into financial service industry. For payment services and pure brokerage this development has taken place already to a very large extend.

The question is why this has not happened yet in the wealth management business? The answer is probably simple, except for some big US players the digital offering for wealth management services has not met the high expectations of these clients yet. Traditional wealth managers were simply to reluctant to change their business models and defining the right IT strategy to move away from their IT legacy system. On the other hand, Super App providers are missing the know-how and required licenses to move very quickly with a superior solution. It will be interesting to see what will be stronger in the future – expertise in wealth management or the digital access to the mass affluent population. To be successful both elements are crucial and must be covered. A key element on the scales will be trust. Wealth management is not a transactional business – it is a long-term relationship between two parties.

Asset under digital Mangement will grow at least 3 to 4% p.a.!

But there is no crystal ball needed to predict that this will change now quickly. There is an increasing demand from a growing affluent population. The technical solutions are now available in the market and financial institutions globally have started to develop omni channel client journey's. It might still take a while before an affordable access to superior wealth management solutions is the new standard. But we are not speaking decades – we are speaking a few years!

Five things private banks should do today

Setting the right priorities in a multi-dimensional environment will be a key success factor. Constant adaption and transformation has to become the standard.

Strategic discipline
Winning ambition and clear choices

Partner in the ecosystem
Value, mind-set and technology

Focus on experience
Moments of truth and data aswell as insights

Empower your RMs
Entrepreneruial tools and analytics

Increase adaptability
Agile mission teams

Source: Monitor Deloitte, July 2019

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