ENSURING A GOOD FIT

Clients of tomorrow might look quite different from the clients of yesterday, so private wealth firms need to develop strategies to make sure their value proposition fits their target market. Simon Hoyle reports.

The number of high-net-worth individuals (HNWIs) in Australia grew strongly in the past 12 months. New insights from CoreData's Private Bank Intelligence Unit (PBIU) suggest the rate was 11 per cent, well above the recent trend of 7 per cent a year, and that there are now just more than 200,000 people classified as high-net-worth – that is, with $1 million or more of investable assets.

For the past three to four years, a

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significant proportion of the HNWI segment has held its money in cash. The PBIU research has detected signs of movement out of cash and into other assets, principally Australian equities – and this was even before the Reserve Bank of Australia (RBA) cut its target cash rate to 2.75 per cent in May.

CoreData founder and principal Andrew Inwood says it's also clear that individuals who retained the services of a good private wealth adviser – and followed their advice – have done substantially better than those who either abandoned their adviser or didn't have an adviser to start with. PBIU figures suggest that individuals who followed advice tended to remain invested in equities – while those around them were flocking to cash – and may be as much as 40 per cent better off today as a result.

Success in private wealth management will stem from first of all finding the clients that fit the firm's value proposition – and where those clients come from tomorrow may be different from where they came from yesterday – and then having a very clear idea of what role the firm plays in a client's financial life.

"We need to step back and ask ourselves: Are we a facilitator or are we an adviser?" says Nigel Stewart, executive chairman of Stewart Partners.

"I will never ever allow myself, nor any of the advisers in our firm, to be put in the position of being a facilitator. We have fired clients – we fired a major client last year because we refused to liquidate their investments. We said it was dumb. It was stupid. [We said] no. We gave them 30 days' notice and closed down the account. They actually did go to cash. And we all know what markets have done over the last, probably, 18 months."

What a client *should* do and what a client *wants to* do are not always the same thing. A well-rounded value proposition might have to cover both.

"It's not all utilitarian," says the head of Macquarie Private Bank, Jay O'Neil.

"It could be emotional. It could be expressive. And isn't my job to help my client uncover the trade-off between those benefits and find a way to help them accumulate wealth over a long time in a way that's optimal?

"Or is it my place to say, 'I have a view, and if you're not aligned with my view you can't be my client'. Those are two different business models."

The client has to fit the business model, says Elissa Crowther-Pal, head of wealth services at BT Financial Group.

If a firm has clients that are "such controllers, are so self-directed, aren't a really good fit in your model, I would absolutely say that you should fire them. Completely", Crowther-Pal says.

"Especially when you're running such a passionate, boutique type of operation where your value proposition is so strong," she says.

"It almost doesn't fit. So I think there is a role for facilitators; it's just it could be very different to what you look like."

The managing director and Sydney market manager for UBS Wealth Management, Sean Cochran, says one approach is to set up a core-and-satellite structure, where the core is the long-term strategic element "and then a separate satellite, where it's a bit more emotional, a bit more opportunistic".

"You could use that to move somebody where otherwise they wouldn't move," Cochran says.

"If you go to somebody who's largely opportunistic, and that's all they do, the idea that you switch them to a strategic model that has control of tactical shifts and

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Adrian Hondros
Commonwealth Private

Sean Cochran
UBS Wealth Management

Elissa Crowther-Pal
BT Financial Group

Chris Selby
Deutsche Bank

instrument selection – they're not going to do it overnight. The adviser might not either."

Cochran says the adviser can then encourage the client to move increasingly towards the long-term, strategic model.

"You can be how they effect that change, I think," he says.

Culling existing clients if they do not fit the private wealth business model sends a strong message, says Adrian Hondros, executive general manager of Commonwealth Private Bank.

"And it's not just about that client and that adviser. It actually gets well known across the organisation, which is more powerful than just saying it. Actually showing people what you mean is far more powerful than just saying it."

Ultimately, for the long-term benefit of both parties, the private wealth firm and its clients should be a good match, and the firm should be profitable. However, it might be appropriate to run it at break-even, if it serves as a mechanism to introduce clients to other parts of a larger financial institution.

"In all the information we can find, private wealth is not a profitable business in many ways for a global firm – for a big firm," says Chris Selby, managing director of private wealth management at Deutsche Bank.

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CLEAR TRENDS

- The number of rich in Australia – that is, people with more than $1 million to invest – is growing strongly. The natural rate of growth is about 7 per cent a year, but in the past 12 months it has grown at 11 per cent to just more than 200,000.
- Money is moving out of cash and into other things, firstly low-risk Australian equities.
- All around the world the return expectations of high-net-worth individuals have collapsed. In Australia, the number has been around 10 per cent a year – any return above 10 per cent was considered good; and any return below 10 per cent was considered bad. That number is falling and it's now closer to 7 or 8 per cent.
- People who stayed with their private wealth offer are now substantially better off than those who didn't, because people who stayed tended to remain invested in equities. The wealth gap between these two groups is so big now – about 40 per cent – that it is very unlikely it will ever be caught up.

Source: CoreData/Private Bank Intelligence Unit (PBIU)

"So you've really got to do something differently. This is just raw numbers, but if I can make the equivalent of 500 basis points on a strategic transaction with a client, [or] I can possibly carry him as a private client for 20, 35 basis points, or whatever, and do custody, what is the better decision?

"We're always going to take the approach of focusing on the corporate opportunity. Because our business is half-owned, effectively, by the investment bank, so I care probably as much for the investment bank's objective in this transaction as I do on the private side.

"At the end of the day you can go on and on and on, but if you're not going to make any money you have a failed model, long term.

"We've done the numbers and we're still doing them...and it's like seven to one. Every dollar that we take from a client generally results in $7 in value to the bank, across the bank. It's a huge ratio. It shows you how much [value] gets generated if you're intimately entwined."

Cost and value have to be clear, and there is a point at which cost can become an issue and "the big families will choose to disintermediate", says Keith Betty, an executive director of GGBwealthcare.

"I think some are prepared to pay a little

bit more because the value of their time is more important to them, or they really don't feel like they've got the expertise, or they've given up from a desire point of view and they don't mind paying a little bit more to spend more time on the boat or whatever the case may be," he says.

"But I think if you've got someone who's really focused and applying their attention, my sense of it is the minute you introduce the classic tiered-cost scale, I'm not sure that you'll get traction off that."

Outsourcing plays a pivotal role in how GGBwealthcare structures its offer to wealthy families, Betty says.

"To try and position yourself as the cardiothoracic [specialist] of every single possible topic is just impossible," he says.

"At the very best you can be a GP, and you can direct, and you might have some cardiothoracic expertise in a particular area. So I think our business is absolutely built around [holding] the family tight at the centre, and then you can 'conduct' [the orchestra], I think was the term you used.

"But I think you are a source of comfort and continuity, because you're a principal and you are going to be around in seven years' time when they're looking to do their transaction; you actually still are there."

Continuity of relationship between the client and the private wealth management firm is paramount in building long-term relationships, says Crowther-Pal.

"We know that whole transition of private bankers or your key relationship person is a critical piece of continuity," she says.

"I think in the US they do a much better job of making it a career where you're there for a much longer time. I know at Wells Fargo and a lot of the other firms, you're there for 30 to 40 years and you have your same relationships, so families and generations have that continuity. Here it's very, very different."

And continuity means there's a much better chance of attracting multiple generations of clients.

Hondros says that going back a few years, "it was all about transition to retirement. All about it".

"Now it's about the transition of these equity holdings and these tens or hundreds of thousands of businesses around the country that are worth everything from a couple of million to hundreds of millions, or more. And so there's a massive range in there. But I think it is the great challenge for us in the next 20 or 30 years."

Stewart says integral to the intergenerational transfer of wealth is the rise of philanthropy.

"What I'm seeing with many of our clients is the kids are very successful partners in legal firms, they're surgeons. They're earning a million, 1.5 million a year as QCs. They're not interested in their parents' wealth transfer of several million dollars. They're thinking of bypassing that through to charity now to see the benefits of helping people in need in the community.

"And that's where I feel that we as advisers can act as that catalyst. We can sow the seed of encouraging them to give to the community. That's what we should be doing, and whenever we go through a discovery meeting it's non-negotiable as far as all the advisers are concerned not to go down some of these pathways, particularly through philanthropy, because these very wealthy people, if they haven't developed a philanthropic policy, they should be, and the adviser should be the lead on that."

But "we're still in that learning journey there on the philanthropy side, aren't we?" Crowther-Pal says.

"It feels like for some of our clients they're only just considering it now. It's just coming into their consciousness.

"Yet it's such a wonderful way of encouraging family contribution and getting families together." ■