OLIVER WYMAN

Financial Services

Finding wealth in commercial banking

MARSH MERCER KROLL
GUY CARPENTER OLIVER WYMAN

Introduction

The current environment is not an easy one in which to be growing either a commercial banking or a wealth management business. Hence, management focus needs to shift towards tactical opportunities that can be quickly realised and that provide a real competitive advantage. For universal banks with commercial banking (CB) and wealth management (WM) capabilities, there can be a very significant opportunity in bringing these closer together in order to pursue WM business with business owners and executive clients. Across Europe, these two segments account for more than two thirds of new high net worth (HNW) wealth created, but universal banks are capturing less than a third of this new business.

A recent European survey led by Oliver Wyman highlighted strong interest in the business owner and executive opportunity. Many banks have already put in place a number of initiatives including installing closer co-operation between CB and WM, and introducing cross-sell incentives to CB relationship managers. So far, results have been positive, but many banks feel that they could and should be getting more. In particular, a number of common issues have arisen:

- Few CB relationship managers are comfortable talking to clients about wealth and are nervous about opening their relationships up to WM
- "Lost in the forest" – there are so many CB relationships that it is difficult to know where to start targeting clients with WM products
- CB clients are too small today for WM to be interested, particularly when the prospect of a significant wealth generating event (e.g. company IPO or sale) seems to be far off in the future
- Clients are already being covered by a competitor

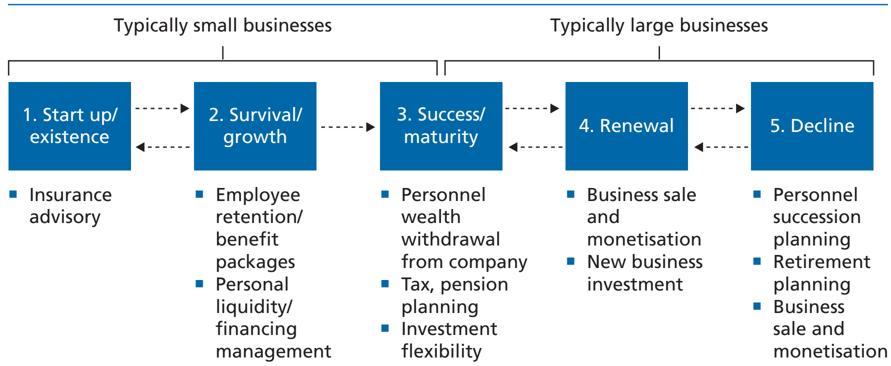
It is not difficult to understand why these issues exist and addressing them can be a challenge. However, from our recent observations, there are two levers that can be particularly effective.

Lever 1: Tailoring the proposition and targeting effort

Business owners' wealth needs are often far from simple and are more difficult to serve than other types of wealth clients. Personal wealth is heavily interlinked with company wealth and can be highly volatile over time. As a result, the standard "let us manage your assets" wealth proposition is rarely the right solution or appealing to business owners. Standard segmentation frameworks based on assets do not work, either. Business owners reward loyalty and relationships; they are unlikely to award a wealth management mandate to a private banker to whom they are introduced after a company sale or similar event. On the other hand, wealth management cannot cover every potential client, or their productivity and economics will suffer.

A potential answer to this challenge is to use a life-cycle segmentation framework. A simplified version is shown in Exhibit 1 and highlights how needs develop at different stages in a typical business life-cycle.

Exhibit 1: Life-cycle segmentation framework



The framework helps to explain the challenge of covering business owner's wealth needs. The net worth of a business will grow substantially between stages 2 and 3 in the life-cycle but it is not until after stage 3 that the business owner can withdraw significant wealth from the business. Between stages 2 and 3, a business owner may be becoming wealthy on paper but has limited free assets and often complex liquidity needs. The client needs a wealth relationship at this stage but not in the traditional sense. Even when personal free assets are built up, the client is likely to want flexibility to re-invest, as the business moves into stage 4. Only really at stage 5 will the client have substantial assets that can be locked away for long term investment and then gifted on to the next generation.

Predictive factors (e.g. firm age, size, turnover, growth, financing structure, etc.) can be used to determine a firm's (and thus its owner's) position and trajectory on a life-cycle segmentation framework. This helps to estimate each client's "wallet profile" both today and tomorrow and then:

- Tailor the proposition:
  - Create differentiated product, pricing and service levels for different wallet profiles to start building a wealth relationship from the beginning, not just once the traditional HNW threshold is reached
  - Focus on solutions tailored to business owner needs: e.g. providing flexible investment/liquidity solutions, optimising corporate vs. personal tax, providing legal and accounting support, etc.
  - Broaden the offering to include employee benefits (e.g. corporate pension) and key executive products as well
- Target scarce resources:
  - Position the best wealth relationship managers to go after the largest, untapped client opportunities
  - Identify new clients that CB and WM should pursue together
  - Provide strategic coverage for high potential but currently small "wallet" clients
  - Design light coverage for smaller "wallet" clients (e.g. electronic channels, group marketing, etc.)

Lever 2: Getting the operating model right

Getting the right operating model is an essential part of ensuring an effective client proposition and targeting of resources. There are a number of different operating models that we observe but these can broadly be categorised into two types – "aligned", where CB and WM form a working partnership and "integrated", where WM coverage and expertise is located within CB. The key aspects of these two models are highlighted in Exhibit 2.

Exhibit 2: Wealth – commercial banking cross-over operating models

	"Aligned"	"Integrated"
Organisation:	Separate: co-operation between units	Joint: WM unit within CB
Branding:	No brand distinction	Distinct: "executive and entrepreneur" brand
Client coverage:	Referrals from CB RMs	Joint teams
Client segmentation:	AuM	Needs based
Accounting:	Separate P/L	Integrated

The "aligned" model reflects where many banks already are or what they are putting in place. The focus of the model is getting both sides to work together and targeting the typical "easy" cross-sell opportunities. Success efforts have delivered conversion rates in the 10-15% region when combined with effective client targeting. Although there have proven to be some difficulties – to date – in creating an effective aligned model, we think there is still ample room for improvement. Adaptations to segmentation and incentive systems form the basis for extracting more value from the "aligned" model. In addition, central MI/intelligence as well as more systematic referral processes, and careful product development and sales process design are also promising optimisation levers. Internally, personal relationship build programmes (between CB and WM) are required to ensure that both units contribute actively to a joint franchise.

There are clear benefits from moving to an "integrated" model (i.e. better conversion rates lifting to 15-25%). The model is more effective with more difficult-to-reach clients who either do not neatly fit into the standard WM client segmentation or require a more dedicated relationship effort before they will open up. It enables the development of more specific client propositions and gives more control over resource targeting. However, the cost implications of moving towards an "integrated" model are not insignificant and need to be carefully addressed. Forming a joint WM unit within the CB, merging coverage teams and pushing two P&L accounts into one, giving local managers – with oversight over both CB and WM teams – responsibility for performance, are non-trivial exercises. Hence, the "integrated" model is clearly the more expensive model in terms of resources required which needs to be considered vs. the potential opportunity.

Conclusion

We estimate that for many European banks, the size of getting a "fair share" in wealth management relative to the size of their commercial lending business is up to €25-50 MM p.a. in new revenue over a five year time horizon. This should be a top 2009 growth initiative in a market that is otherwise limited in large growth opportunities right now. But to ensure success, a clear and well thought strategy is required so that the client proposition, resource allocation and the operating model is the right one given the size and nature of the commercial banking franchise. To develop such a strategy, a structured approach should be taken based on the following cornerstones:

1. Comprehensive review of current CB/WM proposition
2. Analysis of client segmentation and value contributions
3. Determination of "fair share" uplift potential and business case build
4. Implementation planning (including profitability-oriented resource allocation and choice of "right" operating model)

In summary, we believe that now is the right time for universal banks to initiate a joint CB/WM strategy process.

OLIVER WYMAN

Oliver Wyman is an international management consulting firm that combines deep industry knowledge with specialised expertise in strategy, operations, risk management, organisational transformation, and leadership development.

For more information please contact the marketing department by email at marketing.fs@oliverwyman.com or by phone at one of the following locations:

EMEA	North America	Asia Pacific
+44 20 7333 8333	+1 212 541 8100	+65 6510 9700

MMC MARSH MERCER KROLL
GUY CARPENTER OLIVER WYMAN