The Digitalization Dilemma: Do Private Banks push the right buttons?

Why wealthy clients leave their relationship manager – and whether current digitalization efforts will help tackling "pain points" that trigger such behavior

The Private Banking world continuously faces massive changes in both client behavior and technological trends.

Clients undergo generational shifts: Millennials – the generation that entered the labor market around the year 2000 – are standing in line for inheriting massive amounts of wealth already today and even more over the coming years, as well as will form about half of global workforce in the next couple of years. Already now, about 40-50% of affluent / HNW clients are using tech in banking. But tech-savviness of the millennial cluster is even higher, as is the complexity of their requirements, preferences, social consciences and goals for Private Banks (PB), Relationship Managers (RM) or Financial Advisors (FA) to cope with. Additionally, client loyalty is generally perceived to diminish as options for doing banking increase substantially.

Technology undergoes disruptive shifts: Digital trends and innovations create significant pressure and force private banks to adjust their business models. Standardization, digitalization and opening of interfaces foster trends to disaggregate the value chain. Further trends like robo-advisory, automation, or robotics alter the way clients experience and use banking services.

As **clients are Private Banks' by far most important asset they should be at the center of all undertakings** (strategy, processes, and activities). Everything needs be done to serve the client as best as possible, i.e. focus on what is really of relevance for the client and repeatedly exceed his expectations. This raises the important question whether current clients are actually satisfied with their relationship as trends tend to emerge to either leave / change Private Banks and Wealth Manager (current clients) and search for potential new provider (new and potential clients).

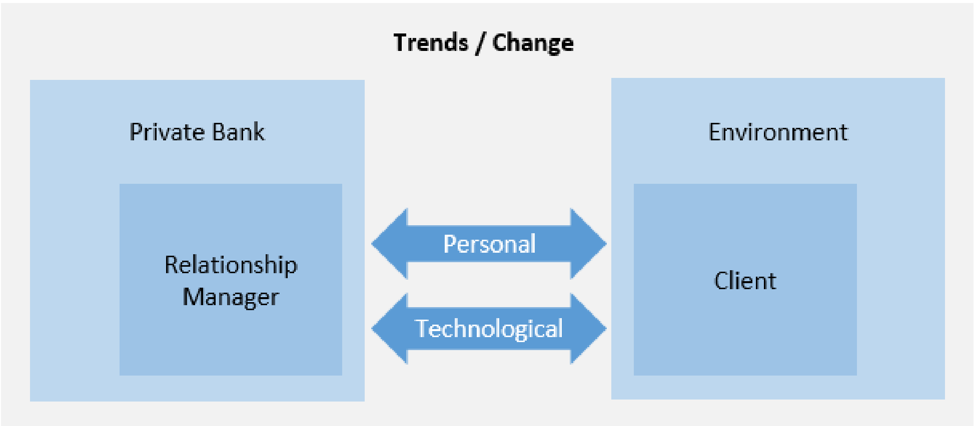

Figure 1: Areas of interdependence in Private Banking client relations

General concept of client satisfaction

The general concept of client satisfaction states that there is a causal relationship between relevant components clients require to be delivered upon – constituting service quality – the level of satisfaction based on clients' expectations, client loyalty and eventually client value in monetary terms. Though this concept might apply more to existing client relationships, its predictive power can also be expanded to prospects. Below the concept's four key building blocks are briefly described.

<u>Relevant factors for private banking clients</u>:

- Expertise / Competence: Competent & fair; professional attitude; extra effort

- Delivery: Promised outcome
- Offering: Comprehensive, cooperation partner & network to provide range of services
- Information: Accurate & comprehensive (repeatedly & consistently)
- Punctuality / Proactiveness: Immediate dealing with topics / requests
- Transparency: Diligent information about business practices, fees, potential conflicts of interest

Client satisfaction

Repeatedly positive experiences – higher than expectations – lead to client satisfaction. Importantly, only relevant needs are considered – the more relevant and valuable a service factor is perceived, the more satisfaction comes with it.

Client loyalty

Loyalty in this context is broadly defined as allegiance or devotion to a private bank. Loyalty can be based on typically long-standing trust, but can also be based on other things.

Client value

Within a relationship, monetary client value can be increased through more frequent use of more valuable and thus more expensive services and products, less defection thus providing a steady flow of income, or broadened client relationship by e.g. including relatives.

A simple model illustrates this interdependence:

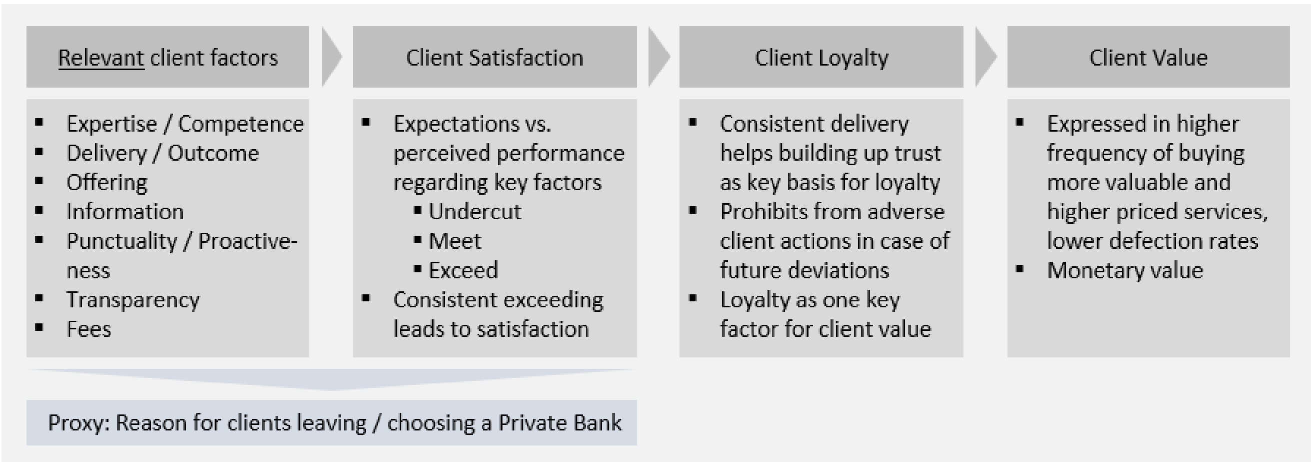

Figure 2: Client satisfaction model

Do Private Banks' efforts match clients' needs? - Applying a meta-analysis to discover

With the two major forces "clients" and "technology" joining, the question comes up inevitably whether Private Banks sufficiently deal with the issue of catering for relevant client needs, wishes and requirements in their efforts to embark on digitization and business transformation measures. To find answers, a simple yet effective 2-step analysis is applied:

Step 1: A brief meta-analysis of online available sources has been done, covering retail, affluent, (U)HNWI and institutional clients of Private Banks and Wealth Managers in various countries (with slight focus on the United States). The underlying studies have been conducted respectively published in 2014-18*. Two factors – acting as proxy for the concept of "satisfaction" – have been applied:

1. Reasons for wealthy clients **leaving** their Private Bank / Relationship Manager / Financial Advisor
2. Reasons for wealthy clients **choosing** a Private Bank / Relationship Manager / Financial Advisor

Step 2: Brief summary of currently undertaken measures applying the wide range of digitalization efforts to Private Banking business model.

Figure 3 displays the consolidated results of the analysis (“pain / gain points” in descending order):

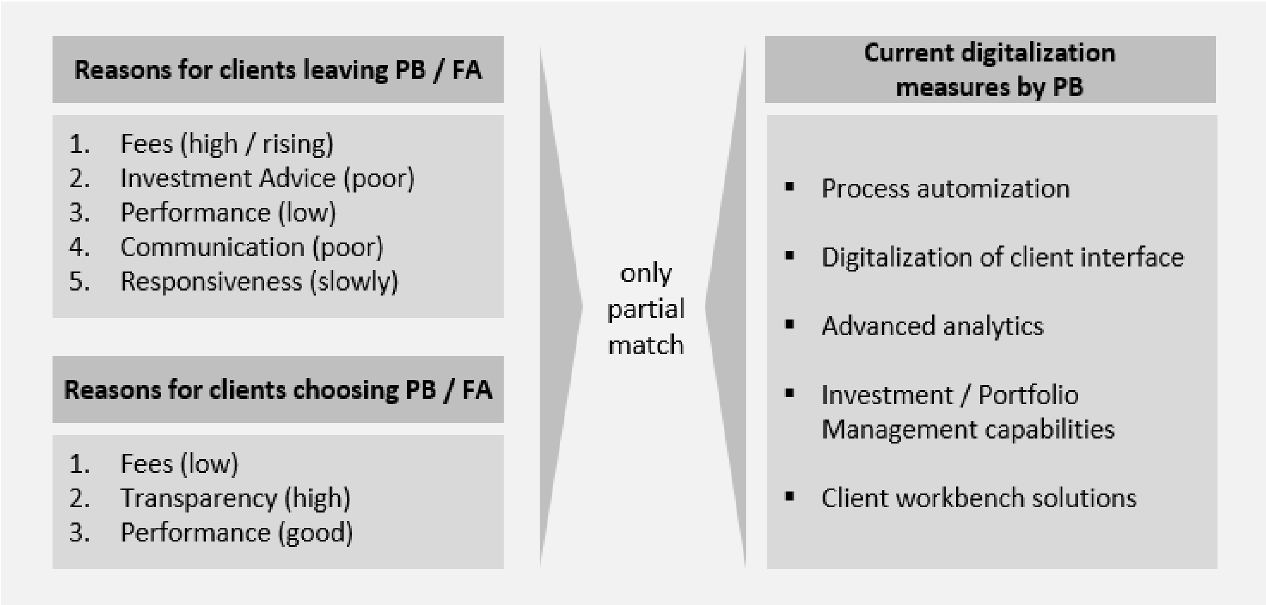

Figure 3: Customer needs and satisfaction level vs. measures deployed by Private Banks

Key findings regarding reasons to leave / choose Private Banks

Fees show strongest evidence in terms of relevance (while being lowest in terms of numbers of mentioning). They are a **key trigger of both leaving** (when high or rising) **and choosing**, thus underlining their importance for wealthy clients – even if this clientele is regarded to be less price sensitive than e.g. retail clients. Price, however, is the only visible attribute in a client relationship.

Investment advice (i.e. personal life goals included in investment strategy, understanding client risk tolerance, providing good ideas & advice) is **one of the key factors** (mentioned 2nd most) in Private Banking. **Repeated poor advice will lead to client defection.** An RM being able to properly gauge client’s tolerance for risk is crucial for a good relationship as the key objective of wealthy clients often times is wealth preservation. Additionally, losing money weighs about 3-5 times higher than gaining (based on behavioral theory) and thus should be prevented for.

Performance (i.e. covering both investment performance & track record) is another crucial factor. Performance is triggering **both leaving** (if poor) and **choosing** (if good) Private Banks or Relationship Managers. Performance is interlinked with investment advice as good advice should c.p. lead to better and more consistent outcome.

Communication (i.e. regular and proactive client communication) also constitutes a very important aspect of satisfaction if exceeded. **Failure to regularly communicate triggers defection.**

Responsiveness (i.e. prompt & quick response via phone or mail) represents the **item most mentioned** which makes failure of being responsive the key factor for (U)HNWI client defection.

Transparency (i.e. covering information towards clients, transparency regarding fees, regulatory issues, offering) is low on numbers of entries but constitutes a trigger of **both leaving** and **choosing** Private Banks or Relationship Managers.

As an **interim result**, the vast majority of “pain points” is in fact **communication-related** respectively performed by the RM or the FA. **Almost all factors are internally controllable**, with the partial exception of investment performance, as this to a high degree is depending from unpredictable market behavior that can only be partially limited by e.g. risk management processes.

Key findings regarding current digitalization measures by Private Banks

In general, Private Banking and Wealth Management are still among the least developed sectors with regard to digitization and digitalization. However, they are ramping up their efforts to cope with the given challenges by – slowly but surely – embracing technological features. This is not yet fully done based on a consistently derived strategy but mostly via implementing various, partly unconnected digital initiatives. These measures cover several areas:

<u>Process automization</u>

Process automization mainly represents optimizing existing business processes via digitization and is a classical approach for incumbent industry players ("doing the same things better"). Key objectives are: increasing efficiency as well as reducing costs and process risks. Those optimizations have more internal impact rather than directly targeting client-related topics. Process automization undertaken these days mainly focuses on two fields:

Robotics Process Automization (RPA) in combination with **Optical / Intelligent Character Recognition** (OCR/ICR) systems enable organization to intelligently identifying, analyzing, integrating, and exploiting formerly unstructured or even physical data, leading to efficiency gains by automating simple and repetitive tasks**.** However, as this generally is applied to back- & middle-office-related processes, client experience is only marginally improved.

Moving on to activities with higher client exposure, the **onboarding / account opening processes** – as one of the first steps during a "customer journey" – come into play. Those are widely regarded as having both optimization potential and customer impact. Admittedly, fast, client-oriented processes do have value – however, it thoroughly needs to be discussed whether the reduction of onboarding time for clients is a relevant factor given that in a Private Banking context both parties enter in a long-lasting relationship that might end up spanning decades. **Would a (prospective) client really refrain from becoming part of a century-lasting private banking franchise only because the onboarding process lasts a couple of days?**

- ⇨ **Effect** on **client-relevant factors unclear**

<u>Advanced Analytics</u>

In an ever-changing, almost unpredictable world, advanced analytics – a set of technology, tools and applications supporting to analyze huge amounts of data and to predict future outcome such as Big Data, Artificial Intelligence, Machine Learning, and Predictive Analysis – are on the rise across all industries, including Private Banking.

Analytic capabilities using valuable, relevant information (qualitative & quantitative) become mission critical for better understanding and predicting client needs, requirements, behavioral patterns etc. to eventually come up with more suitable, tailored and individualized offering proposals. As clients in general tend to share more personal information in return of more tailored and personal advice / offering, the pool of valuable information becomes even more valuable.

Insights from advanced analytics are **highly beneficial for two digitization measures**:

- For **Portfolio Management** by generating new insights through client profiles which are enriched with external data (e.g. from social networks) to be in sync with clients' life events and promote specific services, or creating true 360 degree client profiles by combining internal and external data
- **For Investment Advice** through providing algorithmic advisory in order to find suitable tailored investment opportunities and ideas as well as monitoring several levers risk for client portfolios (i.e. investment risk) as well with regard to the client itself (i.e. defection risk based on predictive analysis)

⇨ **Indirect positive effect** on **internal measures "Portfolio Management capabilities" and "Investment Advice capabilities"**

Portfolio Management capabilities

Portfolio management activities – representing one of the core services of Private Banks – also leave room for further optimization in various ways. Currently Private Banks are starting to embrace the implementation of algorithm-based services that **provide automated and customized portfolio management services** ("robo-advisors"). More suited for younger client groups and used as entry-level Wealth Management service, that transformational approach can be treated as a complementary yet important service for wealthy clients.

Even if a robo-advisor on its own does not tackle any of the given pain points, the underlying approach of providing unbiased portfolio advice for mandate solutions **and better align clients' customized portfolios with their respective risk appetites and financial objectives** for sure does, as it also holds for online analytics and (almost) real-time online portfolio reporting. Meaningful real-time data supporting portfolio simulation and subsequently performance covering tactical and strategic asset allocation changes might substantially help clients plan changes to their portfolios on a tested basis.

⇨ **Indirect positive effect** on **client-relevant factor "Performance"**

Investment Advice capabilities (client workbench solutions)

The optimization of advisory platforms (i.e. client advisor workbenches or workplaces) is underway. Those digital platforms integrate many capabilities and applications required for a Relationship Manager to **serve clients holistically** and help to come up with structured, compliant, objective and risk-aligned proposals.

They enable the RM to be able to share a number of recommendations and opportunities, completely personalized to the client, which the he/she can then review immediately: Not product, but target (life goals) oriented and thus providing for an holistic wealth management approach covering all relevant areas of client's needs.

Additionally, proper systems providing investment advice and being integrated in both customer portal as well as CRM system, and using Business Intelligence capacities will **considerably support the RM to communicate with the client** in a meaningful, proactive and fast way. In combination with digital transaction capabilities (especially for wealthy Self-directed (SD) clients) this set-up significantly supports in tackling two major pain points.

⇨ **Direct positive effect** on **client-relevant factor "Investment Advice"**
⇨ **Indirect positive effect** on **client-relevant factor "Communication"**

Digitalization of client interface

Multichannel online banking capabilities enable clients to interact with their RMs with a convenient "anytime / anywhere" approach, utilizing the full range of digital channels (online, mobile, social platforms etc.). Although already broadly implemented by Private Banks – and thus rather constituting a "hygiene factor" than a competitive advantage – those interfaces **do not yet present the state-of-the-art in terms of functionalities:** Features are often limited (information rather than transaction), as is the offering (limited to basic services). Enrichment of featured services needs to be tackled in the next phases in order to increase value of service quality and foster client engagement.

⇨ **Effect** on **client-relevant factors unclear**

Figure 4 summarizes the findings regarding pain points and measures generally undertaken in the Private Banking sector:

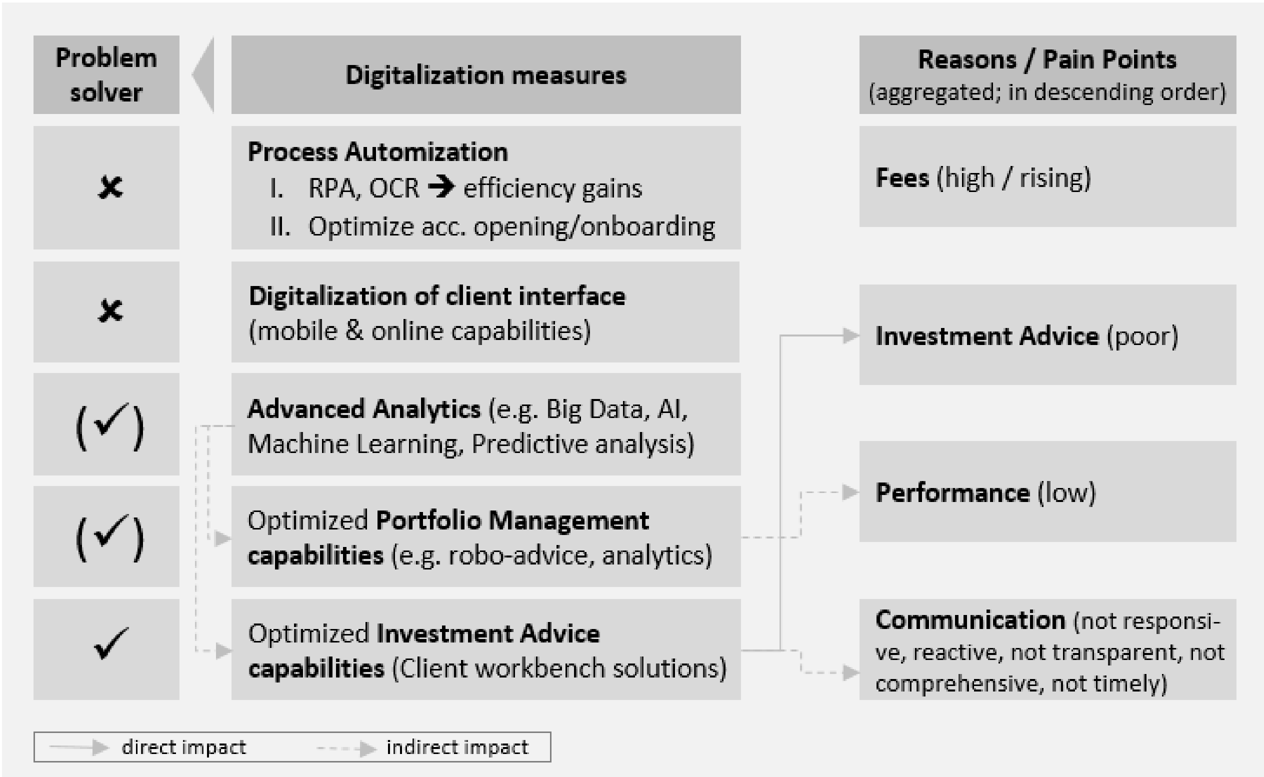

Figure 4: Potential of current digitalization measures to relieve client "pain points"

Conclusion and challenges

The vast **majority** of relevant **defective measures is related to personal communication** between RM and client and thus – due to their very nature – **cannot directly be tackled** by commonplace digitization measures. However, such efforts act as an important facilitator. **But the linchpin of all innovations should always be the client, his needs and his holistic profile.**

What is as relevant as being at the technological forefront is being at the "personal front row" by comprehensively and thoroughly empowering the Relationship Manager or Financial Advisor to fill his role as the clients' first and most important contact person – be it as sparring partner, go-to-guy, advisor, or even friend. Therefore, structured **training and education aiming at increasing relationship-strengthening and people-handling capabilities** and skill sets are mission-critical for optimizing the human resource factor. Additionally, the subsequent qualification of Relationship Managers to accept and finally embrace digital tools and their respective value add while dealing with clients will constitute a future success factor in Private Banking.

RMs also undergo significant generational shifts in the upcoming years as younger people will follow – those newcomers will be more aligned to the new generation of wealthy clients in terms of background, values, shared interests and mind set – high focus on emotional and personal fit. This might potentially move the needle closer towards the **concept of "RM evaluation" to facilitate a better personal fit between the RM and the potential client** – finally improving the odds of a successful upcoming relationship and thus creating mutual benefit.

Outlook

Over time, reasons for clients' defection or choice of banking providers will probably change according to the trends in industry, society, environment and technology. However, (U)HNWI clients are used to pay for professional service to support them achieving their (non-)financial goals and dealing with their complex issues – and will most probably continue to do so. Additionally, wealthy clients value resource and people that are better in their respective jobs than they are themselves. Therefore, **relationship ("face-to-face") stays relevant but will be complemented by cutting-edge technology, further leading to an already anticipated "high-tech – high touch" approach.** As the bar has been raised considerably by client-centric companies (e.g. Amazon), digital functions and interfaces are expected – not providing them will be considered a "no-go" and imposes threat to lose relevance as provider.

The key question a Private Bank needs to address – with regards to all measures undertaken – will always be: What is the relevance for (current and especially potential) clients, and will they value the services, process etc. that will be re-designed?

* Studies can be provided upon request

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