

International Private Banking and the emergence of the Family Office

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The concept and practical delivery of private banking services by international banks has in some ways evolved rapidly over the last three decades, in response to changes in the nature and quantum of wealth generation globally, resulting primarily from economic and demographic changes but also impacted by the policies of governments around the world. The result is a complex picture made up of several different market segments, wider than in the “early days” of the 1970s and also deeper in terms of the product/service/advice mix which banks make available to each of these different segments. The most recent development is the emergence of the family office as an identifiable market segment, to which international banks are now seeking to offer services, primarily through their private banking arms.

The 1980s

Up to the 1970s and the early 1980s, there was a predominance of global wealth in the hands of what is sometimes referred to as “old money”, and private banking, still primarily a Swiss concept at that time, was considered the preserve of the ultra wealthy. As the 1980s progressed, this picture changed. The larger international banks began to seek ways of entering the “private banking” arena, and at the same time began to bring the private banker’s range of wealth management services to a wider audience than before. The expression “HNWI” (high net worth individual) was coined.

In Europe, one characteristic of this initial widening of the approach to private banking was inherited from the “Swiss model”, and this was the central role of the private banker (or account executive, or relationship manager) in the bank’s delivery of services and products to the

client. Clients knew their banker, and had a close relationship with him or her based on trust. The client was usually happy for the banker to suggest appropriate wealth management strategies and to utilise the bank’s proprietary wealth management products to accomplish these.

However, economic and demographic factors were changing rapidly during the decade. These were diverse in nature. In the UK, for example, they included the expansion of wealth ownership associated with the Thatcher government’s policies. The growth in wealth in this decade was across not only the very rich, but the “middle market” as well, and by the time the decade ended, notwithstanding some set backs in the investment markets, a sizeable new tier of wealthy and high earning clients had emerged.

The 1990s

During the 1990s, banks increasingly recognised the importance of this growing middle sector of the market and the potential for it to continue increasing both in terms of customer numbers and of average values for each relationship. The international banks saw their private banking departments as the area that could be extended to address this new segment of the market, at the same time seeking both to offer an increasing range of wealth management products and, in the last years of the decade, also aiming to meet a rapidly emerging set of client requirements for new technology-based service solutions.

“Premium” banking which, in the UK, was particularly led by the leading high street banks was one development responding to the change in the numbers of clients for whom wealth management products might be suitable. Whilst distinguished from the typical retail banking services available to clients previously, it was nonetheless

predominantly product rather than service focused.

Development of the product range made available to this new market was extensive. In addition to core banking elements of higher rate deposits, flexible lending, and securities execution, banks also targeted the wider wealth management requirements of these new customers. Pension planning, insurance needs, discretionary investment services, and other financial planning services were offered either directly, or, in another sign of change, in partnership with qualified intermediaries and financial planners.

At the same time, with technology moving at a very fast pace and clients’ requirements developing as a result, the need arose for banks to be able to offer banking and securities transactions through either a secured service or an Internet-based approach. These communication and technology advances impacted the nature of private banking, with the standards expected for turn-around times for information and transactional processing rising to significantly more demanding levels. High earners and the newer, “entrepreneurially” wealthy were tuned in to this wave of technology and demanded a different style of private banking, combining the one-on-one features of the traditional approach with on-line access to information on a “24/7” basis.

2000 and beyond

So, how is private banking as delivered by international banks shaping up for the first decade of the new century?

One trend that stands out is a growing appreciation among banks of the much wider diversity which now exists in the kinds of person or family who can be prospective private banking clients today. This leads to a need for even more granular market segmentation than in the

past in order to properly understand and then meet the different client needs arising. After the global economic slow down of 2001-2003, back-to-back strength of the world economy in the years from 2004 onwards has led to wealth generation expanding at a very rapid pace indeed in the US, Europe, the Middle East and the Far East. Alongside newer emerging, entrepreneurial wealth, the more traditional old money has also returned to very high growth rates.

A recent Cap Gemini survey indicated that there are now 8.7m people globally holding more than USD1m in financial assets, compared to 4.5m ten years ago. In the concentrated area of individuals whose net wealth exceeds USD30m, numbers now exceed 85,000 worldwide; a 10.2% increase in 2005 alone compared to 8.9% in 2004. Cap Gemini's forecast is for this to continue with high net worth global wealth to reach USD44.6 trillion (USD33.3 trillion in 2006) by 2010 growing at an annual rate of 6%.

This return to very high growth rates in the numbers of the very wealthy in turn has given rise to the need for close consideration of the phenomenon of generational shift. The need for multi-generational planning to allow family wealth to pass effectively to the next generation has of course existed for many years. The differences now are in part to do with the numbers of families whose wealth is of a size where highly detailed and sophisticated planning for the generational shift is warranted. Another difference is in the greater availability of techniques whereby individuals and families can engineer liquidity for their assets through innovative financing arrangements, facilitating the flotation or sale of private family businesses.

The rise of the Family Office

This wider interest over the last five years in the effects and needs arising from generational change among families with very high levels of wealth is one of the factors behind the tremendous increase being seen in the numbers of family offices. The old adage of "shirtsleeves to shirtsleeves" in three generations may be on the change, with the family office concept allowing the family to take more control over generational wealth planning, and enlisting the commitment by family members to preserve the family wealth beyond the third generation.

The family office, an idea originally more prominent in the US (and still developing strongly there, with some reports suggesting there are over 3,000 family offices in the USA), has now become a rapidly growing feature for families in Western Europe, Eastern Europe and the Middle and Far East. As a result, a number of international banks are focusing part of their private banking efforts on this market

segment, including the setting up of departments within their private banking operations exclusively to service the family office client.

Can banks respond to this new market segment successfully?

Those banks which have kept relationship management rather than product at the heart of their approach to their private banking clients will have a head start in building meaningful business relationships with the family office market segment. Moreover, the best positioned are those most experienced in "partnership" solutions, working alongside other trusted advisers with whom the client operates, and demonstrating flexibility in combining their own service offering with solutions outside those they can directly "manufacture" themselves.

Whilst large international banks will be able to participate in the provision of services to family offices, arguably it is the medium and smaller sized banks that will be able to adapt alongside their clients more quickly. Whether among the large or the smaller players, private bankers have to remember the key element in service provision – listening to and really understanding the needs and interests of their clients (in this case, the family office as potentially having additional and, to an extent, distinct needs from the requirements of family members individually). The individualisation of the offering to each individual family office's specific context is paramount.

This focus on customisation of service to provide a specific and tailored outcome, rather than on delivery of product, is a return, of course, to the original approach of traditional private banking organisations. However, whilst the international private banker's offering for the family office is an overall service, which needs to be integrated with the services of the Family office's other providers to create the total solution for the client family, international banks do need to be able to demonstrate a menu of product/ service/advice content which encompasses at least the following key components:

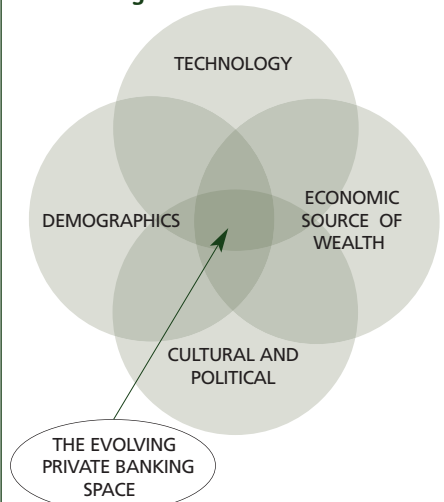
- Flexible deposit products, in a growing range of currencies.
- Short and long term lending solutions, to include property financing solutions and lending against alternative investment products, as well as lifestyle lending.
- Treasury products including hedging and foreign exchange management.
- On-line access to information as the family office and/or individual family members require it.
- Portfolio management advice, though only as an overlay for the family office's in-house management capabilities.
- Fiduciary administration for a range of

asset holding structures, from foundations for charitable giving, through trusts for generational planning, to companies and segregated asset vehicles for asset holding. This extends further to the administration of the clients' own private trust company, and can also lead the private banker into providing support in the area of family governance.

- Custody of international assets across a widening spectrum of investment types.
- Administration of stock exchange listed corporate structures evolved from clients' businesses and asset holding needs.
- An awareness of the family's interests in philanthropy, fine arts and other less standard and arguably non-financial areas, which nonetheless need to be supported by financial planning within a coherent overall wealth management strategy.
- The risk management element, be that specific and insurable or more general in nature and requiring risk control measures and changes in the way services and communications are delivered.

The markets which international banks seek to serve through their private banking businesses have grown in complexity over the last 30 years and will certainly continue to do so, with new geographic areas of the world generating significant family wealth and new products continually being designed which allow wealth management solutions to be accessed by wider audiences. Speed of adaptation will continue to be one of the qualities international private banks most need to possess.

Key Dynamics of three decades of Banking



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