

# REPORT

GLOBAL WEALTH 2012

## The Battle to Regain Strength



THE BOSTON CONSULTING GROUP

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GLOBAL WEALTH 2012

# THE BATTLE TO REGAIN STRENGTH

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# INTRODUCTION

**T**HE GLOBAL WEALTH-MANAGEMENT INDUSTRY is at a crossroads of sorts. While mature markets are experiencing either slow or negative growth, developing markets are riding a wave of very strong momentum. These broad trends are likely to continue, even if equity markets rebound in the coming years. The question is one of direction: should established players in the “old world” look eastward or southward for fresh opportunities, or should they adopt new strategies and business models in an effort to capture untapped potential at home? Should institutions in the “new world” concentrate solely on their own burgeoning regions, or should they also try to compete with entrenched institutions abroad? The jury will likely be out on such questions for quite a while.

In the meantime, wealth managers must continue to find ways to raise their performance in a climate of volatile equity and bond markets, increasingly demanding clients, and ever-watchful regulatory agencies. Especially in mature markets, the lingering impact of the 2008–2009 financial crisis has led to laser-like scrutiny along with tough measures to increase transparency in all areas of the investment world.

In *The Battle to Regain Strength*, BCG’s twelfth annual report on the global wealth-management industry, we explore the current size of the market, the present dynamics of offshore banking, the performance levels of leading institutions in a wide range of categories, the emergence of alternative business models, and key trends that all players must adapt to. Our aim is to present a clear and comprehensive snapshot of today’s wealth-management industry, as well as to provide thought-provoking discussion of issues that will affect all types of wealth managers as they strive to grow in the coming years.

# MARKET SIZING

## A YEAR OF MODEST GAINS

**G**LOBAL PRIVATE FINANCIAL WEALTH grew by 1.9 percent in 2011 to reach a total of \$122.8 trillion.<sup>1</sup> (See Exhibit 1.) The rise was considerably weaker than in either 2009 or 2010—when global wealth grew by 9.6 percent and 6.8 percent, respectively—owing largely to overall economic uncertainty and struggling equity markets in major developed economies.

### Global Overview

The evolution of private wealth varied considerably by region in 2011, highlighting the difference in how the year's economic turbulence affected the developed and developing worlds. North America, Western Europe, and Japan all lost private wealth, while the rapidly developing markets in Asia-Pacific and Latin America sustained the double-digit growth that they have experienced in recent years.

The Middle East and Africa continued to grow but at a more moderate rate than in previous years, owing particularly to political instability in the region. North America remained the wealthiest region globally, followed by Western Europe and the Asia-Pacific (ex Japan) region.

Overall, global growth in private wealth is clearly being driven by rapidly developing economies in the “new world,” not by the “old world” of traditional, mature ones. (See

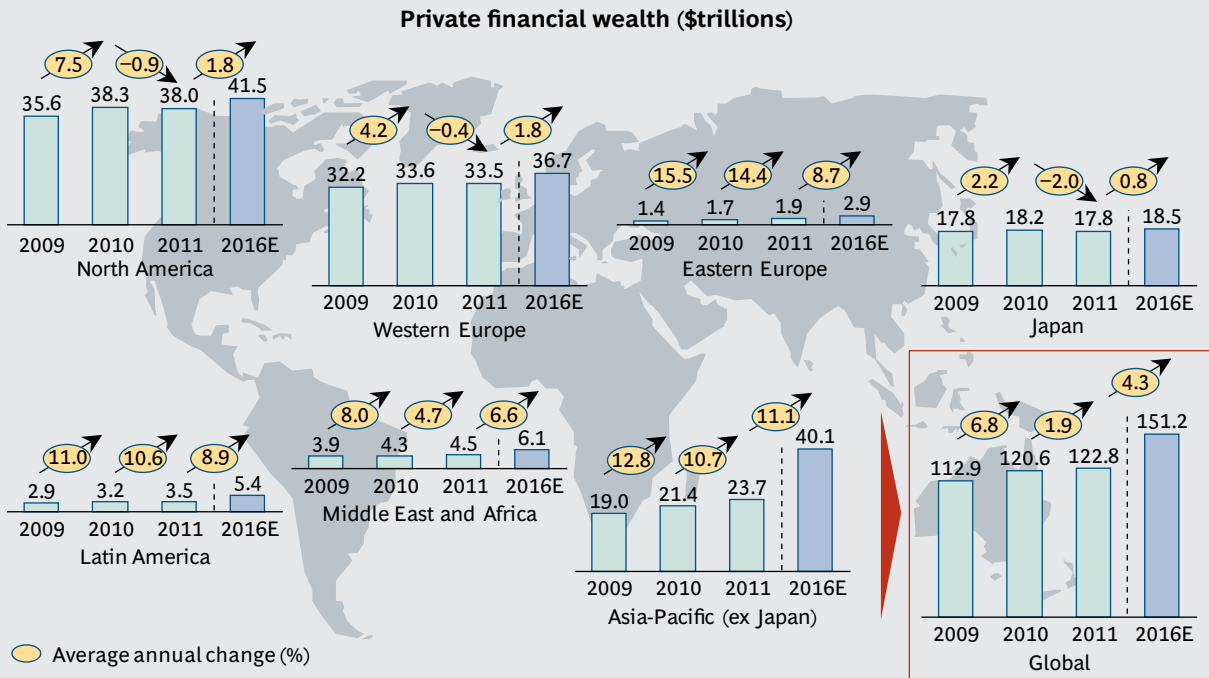
Exhibit 2.) In the BRIC countries, for example, where nominal GDP growth was 15.5 percent on a weighted-average basis, wealth increased by 18.5 percent in 2011.<sup>2</sup>

Equity markets suffered across most of the world in 2011, with positive showings in only a few countries. Europe's equity markets were hurt the most, with Greece's falling by a staggering 52 percent. In the Middle East, Egypt's stock market declined by an almost-as-steep 49 percent.

Globally, the amount of private wealth held in equities declined by 3.4 percent, driven by both negative market performance and asset reallocation.<sup>3</sup> Wealth held in bonds (corporate and government) grew by 3.3 percent, and wealth held in cash and deposits rose by 5.2 percent. The overall asset mix changed somewhat from year-end 2010, although the share of wealth held in equities lost only about 2 percentage points to cash and deposits and still represented about 33 percent of global private wealth at the end of 2011 (versus 35 percent in 2010).

In terms of household segments, the highest growth rate was in the ultra-high-net-worth (UHNW) segment (households with more than \$100 million in wealth), which saw its wealth rise by 3.6 percent—compared with average growth of 1.7 percent across all other segments.

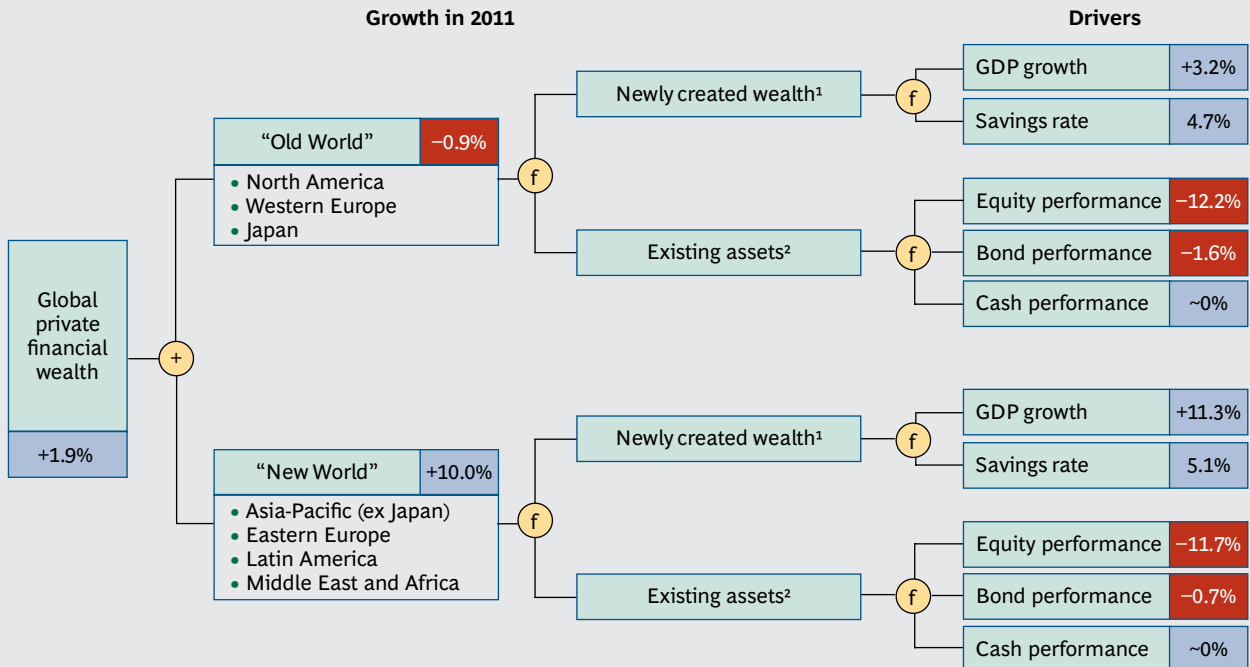
## EXHIBIT 1 | The Growth of Global Wealth Slowed in 2011



Source: BCG Global Wealth Market-Sizing Database, 2012.

Note: Private financial wealth numbers for all years were converted to U.S. dollars at year-end 2011 exchange rates to exclude the effect of currency fluctuations. Percentage changes and global totals of private financial wealth are based on complete (not rounded) numbers. Calculations for 2009 and 2010 are based on the same methodology used for the 2011 calculations. Global wealth is measured by financial wealth across all private households. Countries included in each region can be found in the report.

## EXHIBIT 2 | The “New World” Drove the Modest Growth in Global Wealth



Source: BCG Global Wealth Market-Sizing Database, 2012.

Note: All growth rates are nominal, including GDP growth rates. Performance averages are unweighted and reflect domestic market development.

<sup>1</sup>New private financial wealth, generated primarily through income.

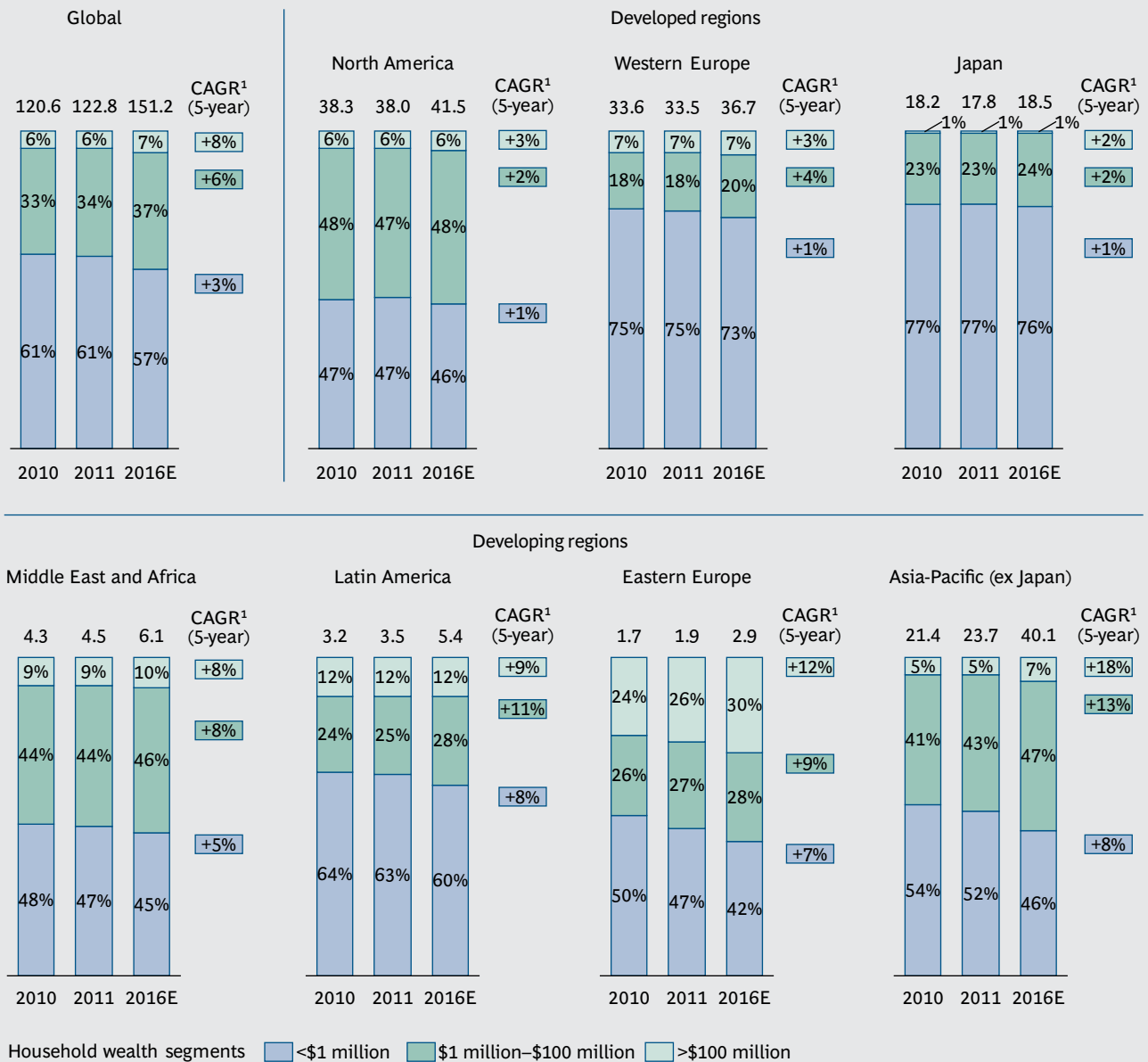
<sup>2</sup>Growth in asset value.

Looking ahead, private wealth is expected to post a compound annual growth rate (CAGR) of 4 to 5 percent over the next five years to reach more than \$150 trillion by the end of 2016. Equities will be the fastest-growing asset class, with a projected CAGR of 4.9 percent. By year-end 2016, the share of global wealth held in equities should be 34.0 percent

cent of the total, still below the precrisis share of 38.5 percent. In addition, over the next five years, the total amount of wealth held by all clients with more than \$1 million in wealth should show a CAGR of around 6 percent annually—driven mainly by an increasing number of households in this segment in Asia-Pacific. (See Exhibit 3.) Average

### EXHIBIT 3 | UHNW Households Will Post the Strongest Growth over the Next Five Years

Private financial wealth by region (\$trillions) and share of wealth by household segment



Source: BCG Global Wealth Market-Sizing Database, 2012.

Note: Private financial wealth numbers for all years were converted to U.S. dollars at year-end 2011 exchange rates. Growth rates and totals of private financial wealth are based on complete (not rounded) numbers; segment wealth percentages may not sum to 100 because of rounding. Countries included in each region can be found in the report.

<sup>1</sup>Compound annual growth rates (CAGRs) are calculated from year-end 2011 through 2016.



wealth for these households is expected to increase just marginally, however. Globally, the UHNW household segment will continue to grow the fastest over the next five years, with a projected CAGR of 8 percent. By contrast, we should see a CAGR of 3 percent in segments below the \$1 million mark.

## Regional Variation

The growth of private wealth varied widely across all regions in 2011.

**North America.**<sup>4</sup> Private wealth in North America declined by 0.9 percent in 2011 to \$38.0 trillion. The UHNW household segment was hit particularly hard, losing 2.4 percent of its wealth. Overall, the amount of wealth held in equities and bonds decreased by 3.6 percent and 2.1 percent, respectively. The share held in cash and deposits grew by 3.5 percent.

A near default on U.S. government debt, combined with the euro debt crisis, made 2011 an unpleasant year for the U.S. economy. These events, along with the downgrade of the nation's credit rating, led to significant investor uncertainty, with the S&P 500 ending the year basically unchanged from 2010. However, stock markets both in the United States and in other developed countries are expected to gradually recover, driven partly by the assumed future stabilization in the euro zone—painful as that may be. North American wealth is projected to post a CAGR of 1.8 percent over the next five years to reach \$41.5 trillion by the end of 2016.

**Western Europe.**<sup>5</sup> Although Western Europe did not suffer as much as North America, the euro debt crisis took its toll, and private wealth declined by 0.4 percent to \$33.5 trillion. The region remained the second wealthiest worldwide. The amount of Western European wealth invested in equities fell by a steep 7.1 percent—owing to weak performance in Western European markets and continued asset reallocation—with the amount held in bonds rising more sharply than in previous years at 3.2 percent, and cash and deposits increasing by 2.2 percent. Equities lost a 2.1 percentage point share and constituted 28.5 percent of Western

European private financial wealth at the end of 2011.

Extreme levels of both government and private debt, as well as the threat of bankruptcy faced by several European Union countries, led to double-digit stock-market declines in some of the region's largest economies—Germany and France—as well as in Greece, Italy, Spain, and Portugal. Owing mainly to repatriations, offshore wealth declined by 2.2 percent, reducing its share of total Western European private wealth to 7.6 percent. Wealth in Western Europe is projected to show a CAGR of 1.8 percent and to reach \$36.7 trillion by the end of 2016, driven by moderate equity-market recoveries in the largest economies.

**Asia-Pacific (ex Japan).**<sup>6</sup> Private wealth in Asia-Pacific (ex Japan) increased by 10.7 percent in 2011 to \$23.7 trillion, enabling the region to widen its gap with Japan as the third-wealthiest area globally. The strongest growth was in the higher wealth bands, with the share of total wealth held by households with more than \$1 million in wealth increasing to 48 percent. The amount of wealth held in equities grew by 4.1 percent, a far weaker performance than the average annual growth of 17.7 percent witnessed over the previous five years. But wealth held in bonds rose sharply by 17.5 percent, and cash and deposits increased by 13.4 percent.

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## The euro debt crisis took its toll on private wealth.

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Despite relatively poor stock-market performance in many large Asia-Pacific countries, notably India and China, strong GDP growth driven primarily by high levels of government and private consumption led to new wealth generation. Wealth in the region is expected to continue growing at a double-digit rate, with a projected CAGR of 11.1 percent, reaching \$40.1 trillion by the end of 2016, at which time it will have slightly overtaken Western and Eastern Europe (combined). These gains should be driven largely by sustained strong GDP

growth in China and India and overall stronger stock-market performance.

**Japan.** Private wealth in Japan decreased by 2.0 percent in 2011 to \$17.8 trillion. The value of wealth held in equities fell by 7.6 percent, while amounts held in bonds as well as in cash and deposits remained virtually flat. Drivers of the overall decline included the lingering effects of the March 2011 earthquake and tsunami—and the subsequent Fukushima nuclear accident—as well as poor stock-market performance resulting from general economic instability. Nonetheless, Japan is expected to overcome these challenges over the next five years. Private wealth is projected to post a CAGR of 0.8 percent to reach \$18.5 trillion by the end of 2016, recovering to pre-Fukushima levels.

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## Many households crossed the millionaire threshold in developing economies.

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**Eastern Europe.**<sup>7</sup> Russia, with GDP growth well above that of most mature economies, was the primary driver of the 2011 increase in Eastern European wealth, which rose by 14.4 percent to \$1.9 trillion. Each of the three asset classes grew by roughly 14 percent.

Eastern European wealth is forecast to grow significantly faster than Western European wealth—at a CAGR of about 8.7 percent over the next five years—reaching \$2.9 trillion by the end of 2016, with the bulk (\$2.0 trillion) held in Russia. These gains will be driven largely by Russia's status as the world's largest oil producer and its continuing GDP momentum. The UHNW household segment is forecast to show the strongest growth, with wealth rising annually by 12 percent through 2016.

**Middle East and Africa.**<sup>8</sup> Middle Eastern and African stock markets suffered from the political instability caused by the uprisings across the Arab world in 2011. Still, the region's private wealth grew by 4.7 percent to \$4.5 trillion in 2011, driven by high savings

rates and strong double-digit GDP growth in oil-rich countries such as Saudi Arabia and Kuwait. Although the amount of wealth held in equities decreased by 2.6 percent, the amount held in bonds rose by 13.3 percent and cash and deposits grew by 5.1 percent. Wealth in the UHNW household segment posted the strongest growth, at 9.0 percent, driven by government programs that benefit large family conglomerates. Private wealth in the region is projected to show a CAGR of 6.6 percent to reach \$6.1 trillion in 2016, largely as a result of continued strong GDP expansion in oil-rich countries.

**Latin America.**<sup>9</sup> Latin American private wealth grew by 10.6 percent in 2011 to \$3.5 trillion, driven primarily by strong GDP growth in Brazil and Mexico. Latin American stock markets were less affected by global economic uncertainty than those in many other economies, with regional wealth held in equities rising by 2.8 percent. Wealth held in bonds soared by 16.6 percent, and cash and deposits rose by 9.2 percent. Private wealth in Latin America is projected to post a CAGR of 8.9 percent over the next five years to reach \$5.4 trillion by the end of 2016—more than double the amount of wealth held in the region in 2006 but still remaining relatively small compared with Asia-Pacific. Particularly in Brazil and Mexico, onshore offerings are becoming more sophisticated as international players enter the market.

## Millionaires

Although the number of millionaire households decreased by a combined 182,000 in the United States and Japan in 2011, globally the number grew by 175,000 as many households crossed the millionaire threshold in developing economies, particularly China and India. The total number of millionaire households reached 12.6 million by the end of 2011, making up about 0.9 percent of the households in our sample (comprising 63 markets representing more than 98 percent of global GDP). The United States still had the largest number of millionaire households (5.1 million), followed by Japan (1.6 million) and China (1.4 million). (See Exhibit 4.) China's number of millionaires should continue to grow strongly, driven by the large number

## EXHIBIT 4 | The United States, Japan, and China Have the Most Millionaires

		Millionaire households				Ultra-high-net-worth (UHNW) households (more than \$100 million in private financial wealth)				
		Number of millionaire households (thousands)		Proportion of millionaire households (%)		Number of UHNW households			Number of UHNW households per 100,000 households	
		2010	2011	2011		2010	2011	2011		
1	U.S.	5,263	5,134	Singapore	17.1	U.S.	2,989	2,928	Switzerland	11
2	Japan	1,640	1,587	Qatar	14.3	U.K.	1,125	1,125	Singapore	10
3	China	1,239	1,432	Kuwait	11.8	Germany	807	807	Austria	8
4	U.K.	411	411	Switzerland	9.5	Russia	607	686	Norway	7
5	Germany	320	345	Hong Kong	8.8	China	538	648	Hong Kong	7
6	Switzerland	317	322	UAE	5.0	France	480	470	Kuwait	6
7	Italy	274	270	U.S.	4.3	Taiwan	369	375	Qatar	6
8	Taiwan	247	246	Israel	3.6	Switzerland	366	366	Taiwan	5
9	Hong Kong	209	212	Taiwan	3.2	Turkey	318	344	U.K.	4
10	France	199	200	Bahrain	3.2	Italy	319	333	Netherlands	4
11	Singapore	165	188	Japan	2.9	Austria	301	301	UAE	4
12	Canada	175	185	Belgium	2.9	Netherlands	291	279	Belgium	4
13	India	134	162	Oman	2.5	India	241	278	Israel	4
14	Netherlands	157	152	Ireland	2.2	Canada	252	257	Sweden	3
15	Spain	147	139	Netherlands	2.1	Australia	228	228	Denmark	3

Sources: BCG Global Wealth Market-Sizing Database, 2012.

Note: UAE is United Arab Emirates. The 2010 rankings are determined on the basis of year-end 2011 exchange rates.

of initial public offerings (IPOs) expected in the country as well as by new wealth generated mainly by entrepreneurs.

The highest density of millionaire households in 2011 was in Singapore—where more than 17 percent of all households have private wealth of \$1 million or higher—followed by Qatar (14.3 percent), Kuwait (11.8 percent), and Switzerland (9.5 percent). The United States had the largest number of both UHNW and billionaire households in 2011 at 2,928 and 363, respectively. Relative to population size, however, Switzerland had the highest number of UHNW households, and Hong Kong was the leader in the number of billionaires—driven partly in both countries by the immigration of billionaire families.

UHNW households held \$7.1 trillion, or 5.8 percent of global private wealth, in 2011, a 3.6 percent increase over 2010. At a projected CAGR of about 8 percent over the next five years, UHNW households should hold \$10.3 trillion, or 6.8 percent of global wealth, by the end of 2016.

### NOTES

1. Private financial wealth includes cash and deposits, money market funds, listed securities held directly or indirectly through managed investments, and other onshore and offshore assets. It excludes investors' own businesses, residences, or luxury goods. Global wealth reflects total financial assets across all households. Unless stated otherwise, wealth figures and percentage changes are based on local totals converted to U.S. dollars at year-end 2011 exchange rates for all years in order to exclude the effect of fluctuating exchange rates.
2. GDP data are from Economist Intelligence Unit.
3. This chapter looks at three asset classes: equities, bonds, and cash and deposits. Managed funds are distributed across these three asset classes on a country-by-country basis.
4. United States and Canada.
5. Germany, France, United Kingdom, Ireland, Italy, Spain, Portugal, Switzerland, Austria, Netherlands, Belgium, Norway, Sweden, Finland, Denmark, and Greece.
6. Taiwan, China, Australia, South Korea, Hong Kong, India, Singapore, Indonesia, Thailand, Malaysia, New Zealand, Philippines, and Pakistan.
7. Russia, Poland, Czech Republic, Hungary, and Slovakia.
8. Saudi Arabia, United Arab Emirates, Israel, Turkey, South Africa, Kuwait, Iran, Egypt, Algeria, Qatar, Oman, Morocco, Lebanon, Bahrain, Tunisia, Syria, Yemen, and Jordan.
9. Mexico, Brazil, Venezuela, Colombia, Argentina, Chile, Peru, and Uruguay.

# OFFSHORE WEALTH

## A CHALLENGED DOMAIN

**B**ECAUSE WEALTH MANAGEMENT CLIENTS will always seek diversification, broad private-banking capabilities, specialized expertise, high-quality service, discretion, and domiciles with relatively high levels of economic and political stability, there will always be a need for offshore banking. In 2011, offshore wealth—defined as assets booked in a country where the investor has no legal residence or tax domicile—increased to \$7.8 trillion, up 2.7 percent from 2010. The increase was driven partly by a flight to safe havens by investors in politically unstable countries and partly by inflows from UHNW families based in rapidly developing economies.

### Greater Scrutiny

Despite ongoing client needs and interest, however, offshore wealth management as an industry remains under intense and increasing pressure owing to greater regulatory scrutiny—particularly from tax authorities in the United States and Western Europe. Simply put, in difficult fiscal times such as these, governments need funds—and cracking down on perceived “tax havens” is one way of obtaining them.

Of the major offshore banking centers, Switzerland has received the most attention from foreign tax authorities. It is still the largest center, with about \$2.1 trillion in offshore

wealth booked in Swiss-domiciled banks in 2011—although it experienced stagnant growth compared with 2010 as funds flowing in from the “new world” just offset those flowing out from the “old world.” (See Exhibit 5.) In addition, Switzerland has already established new transparency and withholding-tax agreements with the United States and Germany, and related discussions with Belgium, France, Italy, the United Kingdom, and other countries are in progress. These initiatives—aimed at greater transparency, the disclosure and regularization of legacy assets, and the adoption of withholding taxes on investment income—have altered the Swiss landscape, somewhat increasing the attractiveness of other offshore centers.

Although the single biggest pool of private financial wealth booked offshore in Switzerland still comes from Western European clients, this wealth declined by 2.2 percent in 2011 and will likely continue to erode. Another traditional offshore center, Luxembourg, has experienced a decline in wealth owing to its high exposure to Western European investors. In both Switzerland and Luxembourg, client assets originating in North America have dwindled to an almost negligible amount.

Obviously, in regions where concerns over issues such as tax fraud and tax evasion are less pronounced, regulatory scrutiny is con-

## EXHIBIT 5 | Switzerland Remains the Largest Offshore Center, but Its Lure Is Being Challenged

Private financial wealth held in offshore centers, 2011 (\$trillions)

Origin of offshore wealth	Destination of offshore wealth								Regional total
	Switzerland	United Kingdom	Channel Islands and Dublin	Luxembourg	Caribbean and Panama	Hong Kong and Singapore	United States <sup>1</sup>	Other <sup>2</sup>	
North America	· 0.04	○ 0.12	○ 0.11		○ 0.39	· 0.05	· 0.00	· 0.02	0.7 →
Western Europe	○ 0.93	○ 0.15	○ 0.51	○ 0.36	○ 0.13	○ 0.14	○ 0.12	○ 0.22	2.6 ↘
Eastern Europe	○ 0.09	· 0.05	· 0.04	· 0.03	· 0.03			· 0.03	0.3 →
Asia-Pacific	○ 0.23	○ 0.26	○ 0.14	· 0.06	○ 0.16	○ 0.76	○ 0.20	· 0.10	1.9 ↗
Latin America	○ 0.25	· 0.03	· 0.03	· 0.01	○ 0.25		○ 0.24	· 0.05	0.9 →
Middle East and Africa	○ 0.56	○ 0.33	○ 0.21	· 0.04	· 0.06	· 0.06	· 0.04	○ 0.22	1.5 ↗
Booking center total	2.1 →	0.9 ↗	1.0 ↘	0.5 ↘	1.0 ↗	1.0 ↗	0.6 ↘	0.6 ↘	7.8 →

→ = Change in 2011

Source: BCG Global Wealth Market-Sizing Database, 2012.

Note: Discrepancies in totals reflect rounding.

<sup>1</sup>Predominantly Miami and New York.

<sup>2</sup>Includes Dubai and Monaco.

siderably less onerous. Indeed, offshore centers such as Hong Kong and Singapore, whose clients come mainly from Asia-Pacific and the Middle East—rather than from the United States and Western Europe—have been much less affected by the calls for greater transparency and tax rigor in the industry. For example, governments in the Middle East do not take issue with residents booking financial assets in offshore hubs such as Switzerland, the United Kingdom, and Singapore.

### Imperatives for New Offshore Growth

The key question for traditional offshore centers and for the banks that operate in them is simply this: Where will growth come from in the future? In Switzerland, for example, asset inflows from investors in neighboring countries will certainly decline. Through 2016, we expect Western European assets booked in Switzerland to decrease substantially because of new, stricter taxation agreements. That said, Switzerland will continue to be the larg-

est offshore financial center in the near future, benefiting from asset inflows that originate in high-growth regions such as Latin America, Eastern Europe, the Middle East, and Africa. Nevertheless, if recent growth rates remain constant, it is possible that Singapore and Hong Kong combined will surpass Switzerland as an offshore booking center in terms of size in the next 15 to 20 years.

Overall, regulatory tightening will mean that the amount of assets flowing to all offshore centers from investors in markets where tax regimes are becoming ever stricter will decline—owing to supplementary tax payments, penalties, repatriation, increased consumption, and the elimination of small accounts. At the same time, client assets flowing offshore from the “new world,” especially countries with underdeveloped private-banking industries, will continue to grow. Clearly, offshore centers with a favorable client-domicile mix will have a structural advantage—particularly Singapore and Hong Kong, which are attracting offshore wealth originating in high-

growth countries. Roughly 75 percent of assets booked offshore in Hong Kong and Singapore are from Asia-Pacific.

What does this new landscape really mean for wealth managers? First, it is clear that the “one size fits all” business model is dead. In the future, wealth managers will need tailored offerings and distinctive advice and service models for each client domicile. Individual relationship managers (RMs) will no longer be able to serve clients from a large number of domiciles because regulatory compliance will become more complex and coun-

try-specific—making it impossible to master the distinct requirements of many different client domiciles. Due diligence on new assets with regard to the source of wealth and its tax status will by necessity have to become more rigorous. As an overarching consequence, many wealth managers will essentially have to reinvent themselves, rethinking their strategies and operating models for each target market. They will have to customize and focus their offerings to meet each client’s specific needs with regard to products, services, tax reporting, and preferred booking centers.

# WEALTH MANAGER BENCHMARKING

A FIGHT FOR PROFITABILITY

**T**O UNDERSTAND HOW WEALTH managers fared in 2011, BCG benchmarked the performance of more than 130 institutions—either private banks or wealth management units of large universal-banking groups—in Europe, Asia-Pacific, North America, and Latin America. Overall, wealth managers faced considerable difficulties in their efforts to bolster growth in assets under management (AuM) and revenues amid a highly uncertain market environment. That said, some cost-reduction efforts have started to show a positive impact on wealth managers' bottom lines.

Globally, the asset bases of the wealth managers in our sample remained flat in 2011, compared with a gain of 11 percent in 2010. The principal reason for the lack of growth was the deterioration in market values, which was not offset by net new inflows. Still, there was wide variation in how wealth managers fared across regions and performance categories. (See Exhibit 6.) Among the results are the highlights below:

- AuM decreased in Europe for both offshore and onshore institutions. Economic instability, demonstrated by euro zone challenges and negative market performance, led clients to shift wealth into real (nonfinancial) assets and to deleverage in order to reduce their exposure.
- The rate of net new asset (NNA) generation—which measures the difference between asset inflows and outflows in comparison with the asset base at the beginning of the period—increased to 4 percent in 2011 from only 2 percent in 2010 for European offshore institutions, and to 10 percent from 7 percent in Asia-Pacific—owing partly to new wealth creation but also to improved front-office capabilities, more-proactive RMs, and an increased focus on client retention.
- Global revenues were virtually stagnant in 2011, rising by just 1 percent. Global return on assets (ROA) increased slightly but was still significantly below historical levels. Broadly, wealth managers were able to increase their level of trading activities and shift somewhat to higher-margin products.
- Cost-to-income ratios (CIRs) varied across regions in 2011, from 68 percent in Latin America and 80 percent in Asia-Pacific to 65 percent for European onshore players and 76 percent for European offshore players—in all cases representing an increase over the previous year.
- Revenue and cost challenges resulted in a slight decrease in profitability in most regions in 2011. For example, for European offshore players as well as Latin

## EXHIBIT 6 | There Was Wide Variation in How Wealth Managers Fared Across Regions and Performance Categories



Source: BCG Wealth-Manager Performance Database, 2010 through 2012.

Note: This analysis was based in Swiss francs for European offshore institutions, in euros for European onshore institutions, and in U.S. dollars for all other institutions. CAL is client assets and liabilities. CAL per RM and revenue per RM are in U.S. dollars for all institutions; averages are weighted by CAL; figures for 2009 and 2010 may deviate from previous reports because the sample size has increased.

<sup>1</sup>Offshore institutions included primarily private banks from Switzerland.

<sup>2</sup>Relative to year-end 2010 AuM.

<sup>3</sup>Revenues divided by yearly average client assets and liabilities.

<sup>4</sup>Cost-to-income ratios of European onshore institutions are likely to be understated because large banks often do not fully allocate costs to their private-banking operations.

<sup>5</sup>Revenues less total costs from private banking, divided by average CAL.



American institutions, pretax profit margins of 23 basis points reflected a deterioration from the previous year. Pretax profit margins for North American brokers improved from 10 basis points to 14 basis points—largely because of cost reductions.

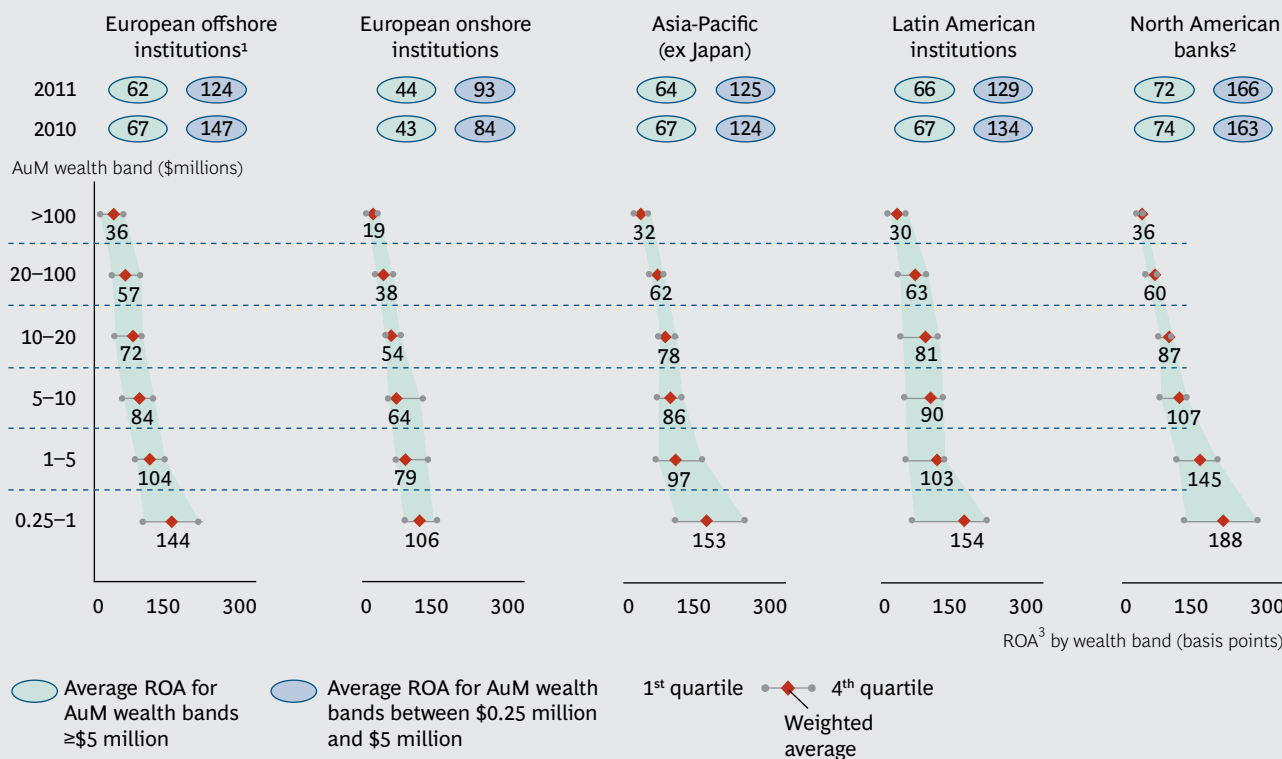
- ROA for European onshore banks and North American brokers rose by 2 basis points and 1 basis point, respectively. However, ROA declined in Latin America (from 83 basis points in 2010 to 68 basis points in 2011) and Asia-Pacific (from 69 basis points to 65 basis points), as well as among North American banks (from 92 basis points to 90 basis points) and European offshore banks (from 95 basis points to 94 basis points).
- ROA also varied considerably across AuM wealth bands, being highly dependent on service models, pricing, and client seg-

mentation. (See Exhibit 7.) ROA declined in all wealth bands among European offshore banks, but the dip was especially strong in the \$0.25 million to \$1 million segment (144 basis points in 2011 versus 172 basis points in 2010). By contrast, European onshore banks managed to increase ROA in most segments. In all regions, banks barely managed to increase ROA for wealth bands above \$20 million, reflecting the strong negotiating power of these client segments. Particularly in the UHNW band, ROA shrank in almost all regions, with only North American banks showing a slight increase (2 basis points).

Our benchmarking also revealed other dynamics concerning products, front-office excellence, and costs.

**Products.** In 2011, most institutions in our sample managed to keep their share of discretionary mandates relatively stable, with

### EXHIBIT 7 | Achieving High ROA Depends on Service Model, Pricing, and Segment Approach



Source: BCG Wealth Manager Performance Database, 2011 and 2012.

Note: This analysis was based in U.S. dollars; averages were weighted by client assets and liabilities.

<sup>1</sup>Offshore institutions included primarily private banks from Switzerland.

<sup>2</sup>North American brokers are not part of this analysis because of the difference in business model.

<sup>3</sup>Revenues divided by average client assets and liabilities.

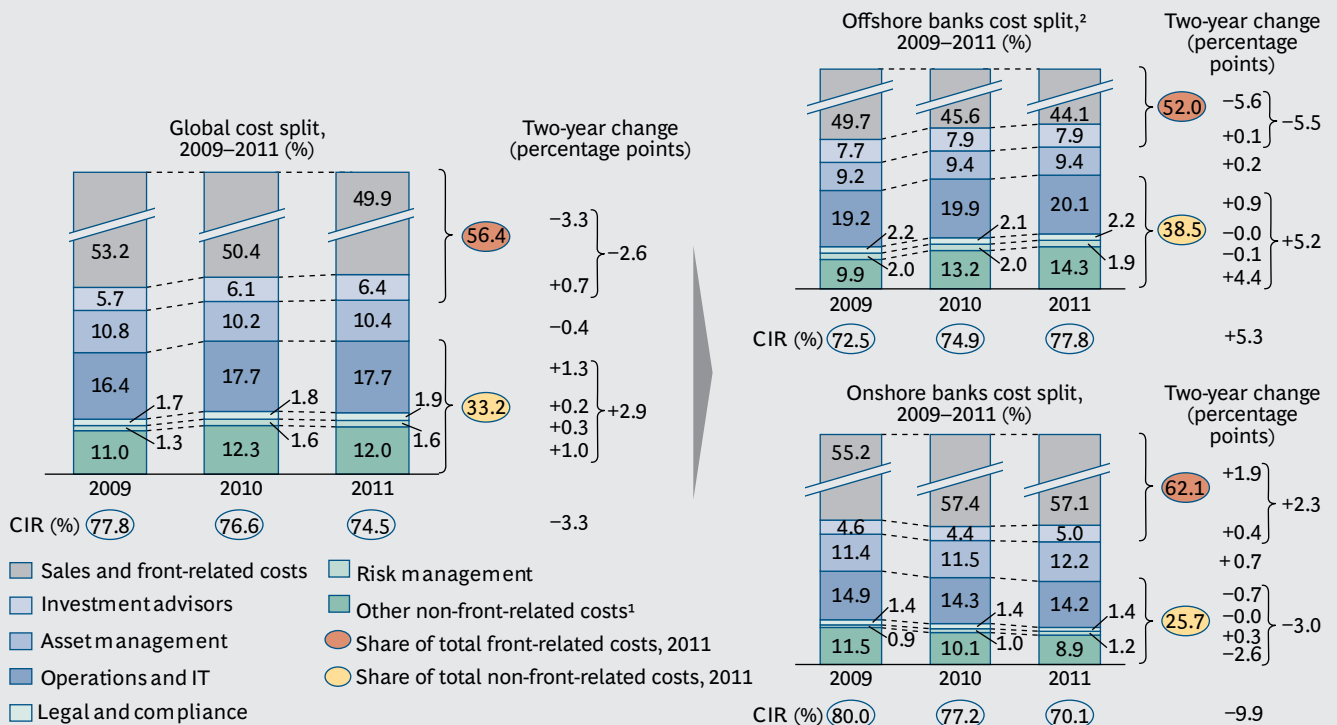
a slight decrease to 21 percent (from 24 percent in 2010). Yet there was wide variation by region, driven by differences among business models. European offshore banks were able to slightly increase their share of discretionary mandates (from 15 percent to 16 percent), while Asia-Pacific banks saw a decline to 4 percent, down from 6 percent the previous year. Nevertheless, discretionary mandates remain an opportunity for Asian banks that use the right business model and that, for example, are not acting only as brokers.

Clients generally continued to allocate their assets in a conservative manner: 23 percent in cash and deposits, 21 percent in direct bonds, and 25 percent in direct equities. Allocations to managed funds increased to 21 percent (up from 18 percent in 2010) and alternative and other investments together made up 10 percent. Loans as a percentage of AuM were at 13 percent, up from 9 percent in 2010.

**Front-Office Excellence.** Globally, the size of total client portfolios per RM increased to a weighted average of \$266 million in 2011, with especially positive trends in Latin America and Asia-Pacific. One reason for the increase was a reduction in RM head counts (as banks weeded out poor performers), leading to the streamlining and consolidation of client portfolios. Also, sales force initiatives aimed at achieving a more rigorous, efficient, and performance-oriented approach were effective for some banks. Many institutions have increasingly aligned RM capabilities with higher client expectations about investment advice. Consequently, weighted-average revenue per RM increased slightly to \$2.2 million, up from \$2.1 million in 2010.

**Costs.** Overall, the share of costs related to the front office has gradually decreased over the past few years as wealth managers have invested more in areas such as operations and IT. (See Exhibit 8.) Additionally, tighter regulations and greater transparency require-

### EXHIBIT 8 | CIRs for Offshore Banks Have Increased Because of Higher Non-Front-Office Costs



Source: BCG Wealth Manager Performance Database, 2012.

Note: This analysis was based in U.S. dollars; averages were weighted by client assets and liabilities. CIR = cost-to-income ratio. Numbers may not add up to 100 because of rounding.

<sup>1</sup>Includes accounting, finance, and control; human resources; communications and marketing; and other central functions.

<sup>2</sup>Includes institutions from Switzerland, Andorra, Singapore, Hong Kong, and Latin America.

ments have resulted in a slightly higher share of legal, compliance, and risk management costs.

Offshore private banks' front-office costs as a share of total costs were significantly lower than at onshore institutions in 2011—52.0 percent versus 62.1 percent—mainly attributable to a more passive service model with regard to managing client relationships. However, non-front-office (corporate center) costs have gradually risen owing to more-complex transactions and higher legal, compliance, and risk-management expenses, leading to higher CIRs. For onshore private banks, corporate-center costs have shown a downward trend, with cost-reduction programs and outsourcing starting to pay off.

For a number of European offshore banks, booking centers were also a significant cost driver. In our sample, these banks did business in an average of four booking centers, with some players present in as many as 13 centers. However, with 82 percent of AuM (on average) booked at one key center, the remaining centers were often below critical mass, suggesting that a leaner structure would be beneficial. Banks need to consider the value of each booking center in terms of meeting client needs.

# ALTERNATIVE BUSINESS MODELS

## NEW PRESSURES ON WEALTH MANAGERS

**O**VER THE PAST SEVERAL years, a handful of wealth management business models outside the mainstream have taken advantage of the disruption caused by the financial crisis and the willingness of clients to consider new alternatives. Traditional wealth managers should aim not only to defend their turf but also to profit from evolving client preferences by adapting their own business models—incorporating different elements from those of unconventional competitors and making sure that they keep their finger on the pulse of what their clients want. (See the sidebar “Client Discovery Never Ends.”)

Each of the three alternative business models described below is exerting pressure on established wealth managers, albeit to varying degrees.

**External Asset Managers (EAMs).** Also known as independent financial advisors or registered investment advisors, these players were in a prime position following the crisis to capture clients who had become disenchanted with private banks. And although their influence varies widely by market, they have gained momentum overall. The EAM value proposition revolves around personal relationships backed by customized, independent advice.

EAMs represent about 20 percent of the wealth management market in the United

Kingdom, 13 percent in Switzerland, and less than 5 percent in the United States. In most other developed countries, they account for under 3 percent of the market—and even less in Asia and Latin America, although the business is developing rapidly. EAMs compete with private banks, but they also depend on them for custody and transaction services as well as for certain products and reporting tasks. In parallel, although some private banks view EAMs strictly as a threat, others see them as a platform or sales channel for their own products and services that can boost operational leverage.

But EAMs are under increasing pressure, too. For example, the regulatory changes taking place are likely to be more abrupt for EAMs—especially if they become subject to banking regulation laws in their markets. In addition, models of remuneration between banks and EAMs are under scrutiny, as are retrocessions (payments from product suppliers). Still, EAMs seem well positioned to continue challenging traditional wealth managers.

EAMs argue that they are more dedicated to the client and better able to provide unbiased advice (their retrocession deals notwithstanding). Moreover, successful relationship managers often opt to become EAMs, viewing that role as having fewer restrictions and better income potential.

## CLIENT DISCOVERY NEVER ENDS

In such times as these, when many investors are more risk-averse and price-sensitive—and increasingly demanding of those who manage their money—it is more critical than ever for wealth managers to know exactly what their clients want and need. A recent BCG survey of high-net-worth (HNW) and ultra-high-net-worth (UHNW) individuals revealed some key insights.

First, although patterns of what clients in these segments seek are largely consistent globally, there are some general differences between those in Asian emerging markets and those in mature, Western markets. For example, Asian HNW clients are generally younger, and are still focused on wealth accumulation as opposed to wealth preservation. They also tend to be entrepreneurs who are comfortable with a high number of trades and transactions, and who want to have substantial input when investment decisions are being made by the bank or relationship manager (RM).

By contrast, our survey showed that their Western counterparts have, to a greater extent, gained their wealth either as senior company executives or through inheritance (often involving multigenerational wealth). Despite these variations, however, there are general trends in what HNW and UHNW clients expect in four domains: private banks (overall), specific relationship managers, channels and interfaces, and product offerings.

**Bank Selection.** According to our survey, the most important criteria in choosing a wealth manager are referrals from friends and family, brand reputation, and product offering. The key reasons for switching providers are price (*vis-à-vis* the level of investment performance), overall poor returns, and poor reporting quality in terms of accuracy, depth, user-friendliness, and customization. In Asia, where the loyalty of clients to RMs tends to be greater than in Europe, clients often follow when their RMs

move to another bank. On average, a strong-performing RM is able to move 15 to 20 percent of his or her client book to the new bank within 18 months. Moreover, in Asia, security, stability, secrecy (for offshore services), and seamless banking services were highlighted in our survey as crucial, allowing for some variation among markets as to which qualities are most important.

**Relationship Managers.** Clients in all regions expect reliability, trustworthiness, and full transparency from their RMs. Another key factor is product knowledge and, naturally, the quality of overall investment advice. Since the RM is often the only person to have face-to-face contact with the client, RMs should always be approachable through multiple channels. The personal touch in private banking continues to be paramount.

**Channels and Interfaces.** Other than RM contact, online banking is the most important channel for HNW clients in the lower wealth segments, whereas a bank's call center and potential social-media presence appear less significant. Overall, Asian UHNW clients are more technology driven, generally speaking, than their Western counterparts.

**Products.** Our survey showed that clients seek wealth management institutions that can provide in-house discretionary and advisory mandates, financial and estate planning, and credit finance. Most other traditional wealth-management products are typically part of the overall offering, but are not differentiators for the average HNW or UHNW client, and do not have to be offered in-house. For some clients, the availability of basic banking products is still important.

For established wealth managers, there are now two options: compete against EAMs by offering more tailored advice and better service, or view them as attractive business-to-business clients and find better ways of collaboration. In order to field a compelling offering for EAMs, wealth managers need to improve reporting capabilities as well as their own online and IT platforms. They also need to provide EAMs with a comprehensive range of products and services. These can include tax and legal support to help EAMs comply with new regulations; market-specific product offerings to help EAMs enhance their client books; and alternative pricing models to aid EAMs in providing the transparency that clients increasingly demand. By courting EAMs with a dedicated offering, traditional wealth managers can effectively create a new distribution channel for their own products and services.

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Clients continue to show a growing affinity for managing their own wealth online.

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**Family Offices.** As the name suggests, this business model is dedicated solely to serving the needs of one (or potentially several) families—a growing niche given the complexity and breadth of some family fortunes. Family offices are most developed in the United States and Europe—where a total of about 10,000 offices manage more than \$5 trillion in assets—as well as in the Middle East. More recently, family offices have begun to appear in Asia.

In a study conducted by BCG, 80 percent of UHNW families said that their main goal was wealth appreciation. Most have their wealth spread across multiple jurisdictions, which often leads to complex legal structures and complicated tax situations. Overall, UHNW families want a highly professional and sophisticated wealth manager with access to a wide range of investment opportunities and an ability to potentially advise several generations. Moreover, these clients often have multiple private-banking relationships, and

their large asset bases allow them to negotiate favorable terms with each one. At the same time, UHNW clients need consolidated reporting across all assets and banking relationships, as well as holistic risk assessment and independent advice. The ability to provide comprehensive service is the key differentiating factor for family offices—and the main reason why they are growing.

The resulting imperative for traditional wealth managers operating in the UHNW segment—few of which have built true family-office capabilities—is to further develop their offerings. To provide a compelling alternative to family offices, wealth managers must ensure that they can provide dedicated, tailored service based on a holistic view of the client’s wealth. To deliver rapid responses to client requests, a team approach—along with crisp execution and strong reporting capabilities—is critical. Investment advice should cover company affairs (M&A and capital transactions), succession planning, mediation of family conflicts, and philanthropy. Family offices, too, can be a potential business-to-business client for wealth managers.

**Online Wealth Managers.** In the past, online wealth managers were basically online brokers, focusing solely on executing transactions. Today, these players have begun offering online advice, research, portfolio management, and investment products. They can cover every step of the advisory process—from assessing risk profiles and generating model portfolios to implementing a defined asset allocation and providing reports. Their offerings are becoming more user-friendly, and clients continue to show a growing affinity for managing their own wealth online.

For now, online approaches are being embraced mainly by clients in lower-wealth household segments, as well as by those who are self-directed or technology-savvy. Still, the need for online wealth management is expected to grow across all wealth bands. The value proposition of online wealth managers centers around 24-7 access and the client’s ability to maintain complete control over his or her investments, with no intermediaries. In addition, online wealth managers usually

have a competitive edge in pricing, which their clients can use to negotiate better deals with traditional private banks.

The key for traditional wealth managers is to significantly improve the integration of their online channels into their overall offerings in a way that enables delivery of a unique and seamless client experience. Several mainstream wealth managers have already taken

meaningful steps in this direction. One has created a separately branded online platform that allows clients to invest in discretionary-mandate-like investments. Another has made virtually every element of its traditional advisory process available online. However, some smaller, more traditional private banks have largely overlooked the importance of this channel and may be missing opportunities.

# TRENDS SHAPING THE INDUSTRY

## A CALL TO ACTION

**T**HE LANDSCAPE IN WEALTH management will change fundamentally over the next ten years as competitive dynamics, regulatory oversight, client behavior, and technology continue to evolve. A broad set of trends is already in motion. Only players that adapt to these trends—particularly the trends outlined below—and seize the opportunities that they present will be able to thrive and achieve leading competitive positions.

**Emerging markets will fuel the growth of global wealth.** In India and China, for example, private wealth is projected to increase at CAGRs of 19 percent and 15 percent, respectively, from year-end 2011 through 2016—significantly faster than the global forecast of about 4 to 5 percent annually. China alone will account for 35 percent (about \$10.1 trillion) of the overall increase in global wealth over this period, while India will account for 10 percent (about \$2.7 trillion).

Both the vibrant growth of wealth and increasing client sophistication in emerging markets are likely to foster the development of onshore investment opportunities and new wealth-management sectors. Growth will occur in local domestic business (onshore) as well as in cross-border business (offshore), with onshore business growing at higher rates but also being more complicated and expensive to enter. Yet traditional wealth managers will still have a difficult time capturing the

opportunity unless they are among the few that are already well positioned in these markets. Indeed, emerging markets are still very diverse in terms of their nature, size, and maturity levels. Some, such as Brazil, are already characterized by clear and transparent regulation, highly developed capital markets, and savvy private-banking clients.

Wealth managers, if they hope to succeed in emerging markets, must first define their strategies, operating models, and ambition levels. They also need to consider the following realities:

- Building a business in emerging markets requires patience and persistence—and potentially several years of investment until breakeven points are reached.
- Business models must be customized to each market and differentiated from those of local players, especially regarding product mix and sales models.
- Given that the underlying economics are different in emerging markets, businesses and ambition levels need to be linked to product usage, trading behavior, and price levels.
- Finding and keeping local talent is a key success factor. This is a particular challenge for foreign banks that need to



position themselves as strong employers of choice.

**The economics of wealth managers will continue to be strained.** Growth will be constrained by tighter regulations, stricter compliance requirements, and greater interest in nonfinancial investments. Revenue margins will be compressed by stronger competition from disruptive business models, increased product commoditization, limited trading activity, and a slow recovery of demand for complex products. Margins will also be affected by rising costs, new infrastructure requirements (driven by regulation), and the scarcity of top talent. More broadly, wealth managers will need to contend with lower profit margins in combination with higher regulatory scrutiny. At the same time, they should continue to protect their revenue streams by working on high-value and higher-margin solutions.

**Clients will become more sophisticated and more self-directed regarding plain vanilla products and services.** We expect HNW and UHNW individuals to increasingly use alternative channels—especially online and mobile channels—to access market information and execute simple transactions. They will continue to prefer personal interactions with experienced advisors when it comes to portfolio reviews, product selection, and holistic advice. All client segments will become more discerning, demanding tailored advice and solutions based on a comprehensive view of their financial needs. Wealth managers must therefore strengthen their capacity to provide highly customized solutions, differentiating themselves from the offerings of retail banks and online brokers. It will also be important to cluster clients according to their needs, permitting a more cost-efficient service model.

**Products will become simpler and more modular.** More flexible, transparent, and modular products will gain prominence as investors seek simple solutions (involving minimal complexity) to increasingly sophisticated problems. Developing such products will require some innovative thinking on the part of wealth managers, but it is thinking that clients will appreciate and be willing to pay for.

**Pricing will become more transparent and closely linked to service models.** In response primarily to regulatory changes but also to changes in client behavior, wealth managers must continue to make prices, fees, and commissions more transparent. In an effort to boost margins and ensure that clients feel they are getting “value for money,” they must also draw a sharper distinction between high- and low-cost offerings. Some will give clients more of a say in determining their own mix of services, and therefore their fees. Pricing, in general, will become a pivotal lever for improving a wealth manager’s economics and bolstering client acquisition and retention. Wealth managers will also have to disclose retrocession payments in some markets (such as Australia and the Netherlands).

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**More flexible, transparent, and modular products will gain prominence.**

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**Risk management capabilities are critical.** Given tighter regulations and a higher profile in the mainstream media, players must reinvigorate risk management. This initiative is not just about avoiding risk incidents and issues with regulators, but also about taking the client experience to the next level. Stricter internal guidelines often lead to more time-consuming processes and higher costs. Overall, the right behaviors with regard to risk management must be strongly embedded in front-office sales and client-service personnel—bringing value to the client while also protecting the bank from operational and reputational risk.

**Multichannel capabilities and social-media presence should be developed further.** Although online wealth managers and community banks will not be major competitors for traditional wealth managers in the foreseeable future, the trend toward online services, increased channel integration, and greater use of social media in banking will have an impact—creating more transparency and setting standards for convenience and

accessibility. Established wealth managers must stay aware of these trends, take them seriously, and use them to their own advantage by developing multichannel capabilities further, striving for deeper channel integration, and ensuring the delivery of a flawless client experience at all touch points. They should also figure out how to embed a social-media presence into their overall strategy.

**Advanced technology and infrastructure will become more essential.** Wealth managers must enhance their IT capabilities in order to keep up with client expectations. For example, in order to provide personalized interactions, product selections, and reporting, they will need an up-to-date, easily accessible client data base or CRM (customer relationship management) system. To provide a consistent and seamless experience across multiple channels, they will need a fully integrated technology platform that has modular applications. To provide tailored products, they will have to develop a more modular product architecture. We expect a breaking-up of the value chain leading to, for example, an increase in outsourcing to third parties—especially for IT and operations.

**O**N the one hand, the markedly slower growth in global wealth in 2011 could be a harbinger of even tougher times to come—a signal that sluggish growth in developed markets will not be offset by strong expansion in developing ones, and that macroeconomic challenges will weigh down both the creation of new wealth and the appreciation of old. On the other hand, the modest growth in 2011 could be attributable to a combination of factors such as flat or declining equity markets in many regions, euro zone worries, and the lingering effects of the 2008–2009 financial crisis—and be seen as a signal that a rebound is due.

We do see a general recovery in equity markets as likely. But wealth managers will still need to continue their cost-cutting and pricing initiatives, refocus on client discovery, master the ever-shifting regulatory environment, bolster risk management, and find ways to use alternative business models to their advantage. Only those wealth managers that take action, as opposed to adopting a wait-and-see attitude, will be in a position to thrive regardless of which direction the markets ultimately take.

# FOR FURTHER READING

The Boston Consulting Group has published other reports and articles that may be of interest to senior financial executives. Recent examples include those listed here.

**Tough Decisions and New Directions: Global Capital Markets 2012**

A Report by The Boston Consulting Group, April 2012

**Customer-Centricity in Retail Banking**

A Focus by The Boston Consulting Group, March 2012

**Digital Insurance: Charting a Course to Best-in-Class Capabilities**

An article by The Boston Consulting Group, February 2012

**A New Virtuous Cycle for Banks: Linking Social Media, Big Data, and Signal Advantage**

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**Operational Excellence in Retail Banking: Raising Performance in Turbulent Times**

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**Facing New Realities in Global Banking: Risk Report 2011**

A report by The Boston Consulting Group, December 2011

**Wealth Markets in China: Seeking the Opportunity to Lead—China Wealth 2011**

A report by The Boston Consulting Group and China Construction Bank, December 2011

**Global Aging: How Companies Can Adapt to the New Reality**

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**Building on Success: Global Asset Management 2011**

A report by The Boston Consulting Group, July 2011

**Shaping a New Tomorrow: Global Wealth 2011**

A report by The Boston Consulting Group, May 2011

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