Leading a race to the top in Asian private banking

Bassam Salem of Citi Private Bank is unfazed at the wave of industry consolidation and competition leading to a scramble among many institutions for AUM. His is a clear proposition focusing on clients of a scale where the bank's core capabilities add real value.

With a cost-income ratio of 56% – and falling – Bassam Salem is right to be quietly content with the success of his business model. "People measure success differently," says the chief executive officer of Citi Private Bank in Asia Pacific, who is also a 35-year veteran of the industry. "I look at both revenues and expenses, which is the cost-income ratio."

As a result, he has been able to spearhead the profitability the institution enjoys today by maintaining a clear focus on UHNW clients with a minimum of US$10 million in assets. The same cannot be said for many of his competitors, which have looked – often mistakenly – to adapt their offering to try to capture as big a share as possible of Asia's growing population of emerging affluent and HNW individuals.

With banking secrecy gone, and a repricing of the market, many European private banks, Swiss ones in particular, have rushed to Asia to attempt to breathe life into what has become a challenged model at home. But they have found it difficult to live up to the expectations, based on projections they and their consultants have made.

Citi Private Bank, on the other hand, doesn't have to convince anyone of its value proposition. As one of the longest-established players in the UHNW space in Asia, Salem doesn't face quite the same uncertainty and pressure as many of his counterparts.

NOT A NUMBERS GAME

It has been compelling for many private banks to try to provide a broader range of products and services to appeal to the lower tiers of Asia's wealthy.

With more and more clients questioning whether they want to bank in Zurich or Geneva, or in Paris, Milan, or Frankfurt, for example, and consultants talking up growth in Asia, the ever-larger pool of US$1 million-plus individuals has attracted interest from institutions traditionally focused higher up the wealth pyramid.

BASSAM SALEM
Citi Private Bank

Yet they typically find a massive imbalance. "Based on some misleading information, a lot of banks believe the 'El Dorado' is in Asia, so they come here, only to find high costs, high expenses, high rents, high salaries and highly-regulated markets," explains Salem. "And they don't find the clients that they were promised."

For example, in reality the definition of HNW refers to a net worth of US$1 million. "Anyone who has bought any property in Hong Kong or Singapore is potentially a millionaire," explains Salem. "But are they a target client? Are they bankable? No, and no."

The Asian private banking opportunity gets further misrepresented because the statistics include HNW individuals in local markets such as Indonesia, India, China, Taiwan and so forth. Yet most models revolve around an offshore model in Hong Kong and Singapore.

is just a starting point in order to open an account.

For those so-called private banks which continue to open accounts for individuals with US$1 million in net worth, this is effectively US$100,000 in 1980s US dollar terms. "These clients are clearly not a target for private banking," adds Salem.

MODELS MADE FOR ASIA

The focus on account minimums underscores the importance for private banks of having a model that suits the clients that the institution is targeting and is geared up to service.

"The right business model is the one that addresses the needs of the client in Asia; the real target market client," says Salem, adding that this should drive the strategic direction that every chief executive officer takes for his or her Asian operations.

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Further, US$1 million today doesn't go nearly as far as it did in 1981, when Salem joined the private banking industry in the first place.

"If you take the 1980 US dollar and adjust it for today, accounting for inflation and the depreciation in the value of the currency, it is around US$10 million, which is where we at Citi Private Bank start," says Salem. And this really

In his view, many private banks simply import a business model into Asia that doesn't really correspond to what the clients in this region want or need.

In China, for instance, many clients have made their money by listing their company in Hong Kong and the only asset they have is their company, so they give the bank their shares as collateral and look for capital market solutions. However, when a Swiss bank, which prefers a diversified portfolio approach, discusses this with the credit officer in Zurich or Geneva, there is little appetite to lend.

Further, most Asian clients don't engage asset management and discretionary portfolios in the same way as many European private banks are geared up to provide.

"While nearly 50% of our investment revenue comes from managed investment, it is very different from plain-vanilla managed portfolios," says Salem. "We do a lot of private equity, real estate and hedge funds, which is what Asian clients want, but not what many [European banks] do."

An example of the type of real estate deals Citi Private Bank executes for and with its clients are single-property funds. "We did one for instance in New York in Manhattan, at 432 Park Avenue, where we financed the tallest residential building in New York," explains Salem. "Every time [with such deals] we raise US$100 million to US$200 million only from Asian clients."

The cost for private banks of not paying enough attention to cost-income ratios and requirements of Asia's wealthiest is often head office deciding to exit the market – witness the sales of Merrill Lynch's international wealth management business to Julius Baer, Societe Generale's Asian private banking operations to DBS, BSI Bank's business to Brazilian investment bank Grupo BTG Pactual, and Coutts' international business to Union Bancaire Privée.

GROWTH DRIVERS

In acknowledging the challenges for his counterparts, Salem is very focused on where growth for his own business will come from: China and India from a geographic perspective; and managed investments in terms of solutions.

"Our growth in China and India is in the range of 45% to 50% per year," says Salem. "These are great markets for us, and these places are where we have been investing."

For its managed investment offering, at just under 50% of the bank's overall investment revenue in Asia, Citi Private Bank bucks the trend in a region where people say clients in Asia don't give discretionary mandates or invest in managed portfolios.

To overcome the restrictions and subsequent reputational risks that cross-border regulations create for private banks in Asia, Salem opts for setting up a managed portfolio.

"When clients have signed on to a series of discretionary portfolios, all their transactions are executed by the portfolio manager, so the risk for the business is much lower and we get annuity revenue," he explains. "We don't have to call and sell a new idea every time."

This business model at Citi Private Bank is a combination of segregated portfolios managed by Citi Investment Management, and alternative investments such as private equity, real estate and hedge funds, typically run by third-party asset managers.

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Salem's strategy to grow in these areas and geographies is inter-connected, linked to the fact that the bank's business model is largely cross border, based on the licenses it has in Hong Kong and Singapore. The only exception is India, where it is present onshore, in Mumbai, Delhi and Bangalore.

"If the client is in Hong Kong or Singapore, then we can do lending, banking, asset management and capital markets," he explains.

"When the bankers go and meet with clients in Jakarta, Beijing, Shanghai, Taipei, Bangkok or Manila, for example, we cannot sell them any securities."

For the types of clients that Citi banks at the US$10 million-plus level, they appreciate the greater transparency offered by segregated portfolios in comparison with mutual funds.

"Since the financial crisis in 2008, they like to see what is inside their portfolio," says Salem.

"With a mutual fund, the manager will show you the top 10 holdings, but these might only represent 20% or 30% of the total portfolio. For a segregated

Citi Private Bank's broad range of clients

Entrepreneurs and business owners *– the bank is a partner to technology and real estate entrepreneurs, principals of venture capital, private equity and hedge fund firms, and other successful business owners.*

Corporate executives *– the bank works with owners and executives of both publicly-traded and privately-held companies, helping them grow and preserve their personal wealth. This includes planning before, during and after a liquidity event, and structuring a wealth plan that suits individual situations.*

Family offices *– with over 850 family office relationships, Citi Private Bank's Global Family Office team know that every family office is as unique as the families that they serve.*

Law firms and attorneys *– the bank's Law Firm Group serves as one of the premier advisers to the legal profession, committed to serving the financial management needs of some of the world's top law firms, their partners and associates, and with experience in the complex investment, banking and cash flow requirements of law firms and legal professionals.*

Next generation *– the bank's Next Generation team focuses on providing programmes, tools and resources to the children of its clients. It creates networking environments in which young adults can meet their peers, connect through a shared experience and gain access to a global NextGen community – a network that spans 35 countries and dates back to 2002.*

portfolio managed by a third-party, the entire list of securities is made available, consolidated by stock, sector and manager," he explains.

Also, he adds, clients want proximity. "They want to speak to their portfolio manager, and if they buy a mutual fund and there is a crisis, the first person a fund manager would talk to is his largest institutional investors, not a retail client," says Salem. "When clients have their own portfolio managers based in the region, they have that proximity."

THE LURE OF LOCAL MARKETS

Similar to his counterparts at many private banks, Salem has been focused in recent years on exiting all the hubs where his predominantly offshore business model wasn't making much financial sense. In doing so, he was able to reduce the bank's cost-income ratio from 84% to 56% today.

So for him to go back onshore, in any market across the region, the venture needs to be money making.

Inevitably, he has China in his sights.

"The big elephant in the room is China," says Salem. "If you were to go onshore you would want to go to China. The challenge is the regulation means that to conduct private banking activities over and above the banking license that Citibank has, we need a brokerage license, a trust license to do asset management, and we can only own a maximum of 35% of these."

Given his priority on profitability, he doesn't subscribe to a wait-and-see approach in such developing markets.

Instead, the day China opens up, which may come soon based on the pace of the reform agenda, Salem will be ready to make his move. He is confident that he can take advantage of the potential quickly, via the existing Citibank presence across the country.

In the meantime, he has carved out a good business capitalising on China's wealthy off-shoring their assets.

"It is a big business," says Salem. "We only deal with entrepreneurs, who typically list their companies offshore, in Hong Kong."

They look to borrow against the stock in Hong Kong to do one of a few things, he explains.

For instance, they might buy stocks in Hong Kong, because they like to reinvest in their local market so look for the capability to trade and use leverage.

Or, they want to buy a "trophy" property somewhere like London, New York or San Francisco, either commercial or residential, and need financing help.

Or, they create a discretionary part of their overall portfolio to achieve a certain amount of diversification.

By concentrating to date on the top end of the China market, Salem says the bank has been successful enough in making the Citi name well known, that he doesn't rule out the possibility of going onshore at some point.

GETTING THE BALANCE RIGHT

Ultimately, Salem's four stakeholders determine his strategy, and he must keep each of them happy.

One of these comprise his shareholders, which want to see a profitable business. "They are not in the business of throwing money into a venture on the expectation that in 10 years' time they will make money; they want to make money today," he explains.

A second group are the regulators, which give the bank a license to operate – and can just as easily take that away. Given the massive consumer bank presence Citi has in most countries in Asia, the private banking arm cannot flirt with the regulation at all.

A third set of stakeholders are the bank's clients. "I have to give them competitive pricing, product and services," he says.

The fourth group are his colleagues in the private bank.

His commitments to them are to provide a working environment they enjoy, attractive remuneration, and opportunities to learn and grow.

To make his model work, Salem is happy to be part of the same business as the investment bank.

"In 10 years' time, I bet you [my main private banking competitors] will have the business model that we have today, but in 10 years' time we will be way ahead and we will be doing a different kind of private banking," he says.

This isn't because he likes change for the sake of it, but because the model will evolve in line with the market, as well as the demands of his clients.

"When other CEOs think about how to make money, they just need to listen to their clients and offer them what they need, not what the bank has to sell," explains Salem. "If they do this, they will be profitable." ■