Pricing and monetisation in private banking: New trends in revenue management

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Executive summary

The delicate art of pricing and sales psychology in the world of private banking is in greater focus due to increasing regulation, which is forcing the banks to find ways to ensure compliance in every aspect of their client interface. Hubbis and co-host Simon-Kucher & Partners assembled a group of wealth management experts in a private discussion to analyse the latest trends and anticipate future developments.

The premise for the discussion was that the approach to pricing, monetisation and discounts in the wealth management sector in Asia need addressing in a more professional manner, for sustainable growth and superior service. As the business model migrates ever more towards advisory, rather than the former transactional model, this is ever more important for transparency, business planning and customer satisfaction.

But the transition to advisory revenues in Asia is not an easy one. The struggle around pricing in the wealth management sector in Asia is the continuing focus on transactional revenue as opposed to recurring revenue, which is proving more elusive than many had expected.

However, as Asian clients move onto their second and third generations of wealth management firms hope they might gradually be able to start charging along the lines of their Swiss counterparts, based around advisory fees rather than transaction fees.

The template for the future is in Europe, where there have been great strides forward, especially in that bastion of private banking, Switzerland. Two decades ago banks there knew little or nothing about pricing technology and strategy; today, private banks and other wealth management firms focus considerable effort on pricing structure and transparency within their organisation, as they know how vital it is for revenues and also for customer retention. In fact, pricing transparency has become a key selling point for many of the leading institutions.

Transparency in the Asia region will be ever more essential, partly due to the demands of regulatory reform and inspections. The wealth management industry in Asia has remained too opaque for too long, but with increasing disclosure required for clients and compliance, it is gradually becoming an internal priority for all the players in this industry that they focus on and willingly embrace transparency.

A more level playing field is the hope and expectation for the future, as private bank clients in the region are under pressure to clarify fees at the earliest stage possible and to justify discounting internally and externally. As profitability is under pressure at the banks and other wealth management providers, firms that focus on professionalising their pricing strategies and structures will be better placed to prosper in the future.

Competition will only intensify and accordingly the drive towards monetisation and value pricing will also become more crucial, with innovations and smart pricing strategies central to protecting and predicting margins in the future.

THE PRIVATE, ENTIRELY off-the-record conversation took place in late May, with a wide variety of participants, including private bankers, consultants, asset and wealth management firms, family offices, and others in attendance. The discussion began with a brief introduction from Silvio Struebi, Simon-Kucher partner in Singapore and Jan Engelke, Managing Partner in Switzerland, who set the scene for the discussion.

Struebi explained that Simon-Kucher has 1200 staff in 35 offices globally and that more than 50% of the firm's revenues come from pricing and monetisation projects in all industry types. "When I arrived here in Asia 18 months or so ago," he explained, "I noticed big differences between this region and Europe or Switzerland and was even more convinced that this whole topic of pricing, monetisation and discounts needed addressing in a more professional manner, for sustainable growth and superior service."

Engelke explained that he had worked in this sector for 21 years and for a considerable portion of that time had worked on behalf of a global banking group client. "Banks knew little or nothing about pricing technology and strategy at the start and it has been a great journey, to bring pricing structure and transparency into their organisation. How many discounts were on offer and by whom in their bank? They had no idea at the outset. But we gradually set about a pricing and discount management policy that gives internal transparency and controls and external consistency."

He explained that a core element of the discussion was to convey their messages, but also learn the state of the art, whatever it is, amongst wealth management experts in the region.

Attack vs defence

An ex-banker who is now with a private asset management firm noted that he sees two sides of this coin, one from a banker's perspective and the other from a boutique perspective. "Clearly there are retrocessions and those have not been entirely transparent," he said. "We are 100% full disclosure, and the client, not the bank pays us, so we are effectively pitching against the banks and we highlight their lack of transparency in pricing."

"This is the attacker and defender model in business," added another attendee. "The attacker presents a simple price model, the defender has a more complex one, not so transparent. It is a typical

strategy seen in other industries." The regulators will be driving much of this pressure, effectively taking the role of the attacker. "They are going to tighten the screw dramatically and my view is it will accelerate with the next downturn," added another panel member.

Recurring fees – achievable or a mirage?

There seems little doubt that Asia's regulators will drive the market towards the model adopted in the UK or Switzerland. "At our bank, we are trying to move from the brokerage model into recurring fees, for example trying to introduce a flat fee all-in. We aim for transparency, telling clients exactly what is included. As a generalisation, international clients in this region understand it, while Asian clients struggle with the flat fee concept. Our bankers can set these fees, as they own their profit centre, but they have to get the balance right and to help them we do a lot of data mining to help find the sweet spot. This differs between smaller HNW clients and then on upwards to the ultra-HNW individuals."

Another expert at the discussion noted that in his experience of working previously with a global bank, they had huge pricing flexibility, often being able to discount heavily for one client, while earning that back with another client who was charged top dollar.

"Pricing varies between the big banks and that pricing also includes the cost of providing lending to HNW clients, which is a central element of winning and keeping clients in what is a generally leveraged market," he explained.

"We hear of some absurd, lowball debt pricing amongst our major bank competitors and particularly some of the major regional banks in Asia, based out of Singapore for example."

The search for value pricing

Pricing, said one attendee, is also about finding value. For example, in the car industry metallic paint is a high-cost option, but the extra cost to the producer is minimal compared to solid colours.

"This is value pricing, focusing on not on cost but on the value the client likes to pay, he said. "Accordingly, for our industry there needs to be this balance between the value the client gets and the price he pays. There is great potential in this industry to improve the balance."

Another banker from a major private bank, but not part of a global universal bank, noted that their global business has expended some 30 times in size in the past 10 years through organic and M&A expansion. "There is an incredible amount of innovation going on in Switzerland and a lot of these advances are quickly being brought into Asia but in Zurich, they perceive this region to be very different, they do not expect things to transit so well to this market."

"So," he added, "we have to manage the expectation on how successfully we can implement a good idea in Asia. We are in the process now to also move towards a more advice-led model, we have about 5% in DPM now, relatively small, and a successful advisory business today, but that is mostly remunerating the bank in terms of the transaction base, so it is not really a recurring fee business, it is more process."

Discounting – necessary but totally unstructured… so far

Because of the presence of "treat customers fairly" policies, discounting is now a major issue to address and have to be carefully justified. "If you have clients with similar profiles and they have completely different prices for the same service it can become a problem, so a consistent framework is preferable," commented one expert.

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"Sure, some deals can be at different prices, for example for a client that is bringing more value to the bank, but this must be quantified and assessed internally. The banks have to make more transparent what the clients really pay and show a regulated discount structure. When things change in Asia they change fast, and this is likely the next step."

Another banker tackled the pricing of leverage for clients, noting that if the client borrows and brings good fee revenue to the bank from trading, there is considerable leeway for loan pricing discounts.

"We give good freedom to our team," he explained. "You have to look at the overall profitability of the relationship, but in recent times there is clearly less room for manoeuvre. The key issue for us nowadays is actually analysing how to price products and services, to work out if we actually make money on them. For example, brokerage costs in big, liquid exchanges should be different from the more esoteric, frontier markets. It is a highly complex set of equations to work out where we do and can make money."

"For newer, more complex products, higher pricing is required because there are more operational, legal or whatever processes and costs involved," another participant noted. "Add-on costs and data to assess those need to be carefully mined and handled."

"Then we see that there are plenty of clients who will shun the DPM approach because they are not the wealth planning type of mentality."

A wealth management professional explained that their drive to win more DPM mandates in Asia is at its infancy but progressing acceptably. "We offer a tailor-made service," he said, "but we quickly tell the clients that if they want the best portfolio managers don't come to us, or the private banks because the best are running portfolios elsewhere. We say we are here to provide the best service and customised for any one client, not off-the-peg. We also show them funds they might consider buying if they do not decide to work with us, those funds being closest to their requirements."

"So," he continued, "we say we will monitor our performance for that client against that agreed benchmark. So far, so good, the clients have a benchmark, and also a fall-back position if we underperform. We also downgrade some clients who want things on the cheap, so we have a team to handle them and the RMs can downgrade them but still get revenue attribution."

Mind your client behaviour

Another expert noted that they are focusing heavily on behavioural pricing. "We are investing in this field and collaborating with a well-known research institution," he reported. Behavioural history determines much of their decision-making. But when, for example, dealing with very price sensitive clients, differentiation is actually the only way to take price pressure away. So the response might be: so ok we can take your lower price but in return, there is a lesser level of service."

He also noted that there is a convergence between the role of pricing and sales, especially in Asia. As a result, banks are investing heavily into sales tools that support RMs to discuss and negotiate with the clients in a more structured manner. "Not every RM is an excellent negotiator," he added.

He gave some examples of the tools in use, for example, a RM might have a leaning towards FX or DPM, or other products or services. "But in many cases, they are not good at cross-selling, so we need to incentivise them and encourage them to raise certain topics in meetings or discussions."

Horses for courses

Another banker noted that for some bankers, substantiating the value of their advice comes naturally. However, for bankers from the more product-led institutions, especially those that have a strong retail focus and/or are very brokerage, transactional focused, it is difficult to have that conversation with the clients.

"Then we see that there are plenty of clients who will shun the DPM approach because they are not the wealth planning type of mentality," he observed. "So, we have an active advisory arm that makes a real effort to ensure that the RMs understand how to sell these propositions. More than half the book at our bank is now engaged in active advisory."

He explained in more detail that the active advisory clients under the active advisory proposition are generally quite active, meaning that RMs are in touch at least once a fortnight. "With constant engagement, the stronger the relationship and the more trust you have in each other. We can then bring in other elements of the bank to service those clients, without the RMs feeling as if their rice bowl is being taken away."

A turning point?

"We are going through a huge inflexion point driven by Automatic Exchange of Information, CRS and so forth," remarked one attendee. "A lot of what happened before, for example, between distant clients and Switzerland [banks] was effectively DPM, as the clients did not expect or want to be in touch all the time. But now we are all suddenly

in this environment where how you own your account, how you manage and control it does matter, so any value-add now means a premium cost for solutions."

He gave the example of some Asian clients he had recently signed up, with substantial wealth. "They do not really know what they have; they have structures put in place in the past two decades that are utterly inappropriate today, they have CRS issues, they have no clue what is being reported and to whom. The future, however, is consolidated, and the drive is to reduce the touch points, reduce the information flows, cut back on leakage points, not just for tax planning but for confidentiality. These are Indian families to whom privacy is extremely important."

The holistic approach, digitally-enabled

One banker highlighted the value of data consolidated onto a platform to allow the clients to view their entire positions holistically, and also enabling the RM or bank to consider their situations more insightfully.

"This aids a discussion to help the clients then make informed decisions about what they are actually going to do. The bank becomes their 'honest' adviser and they create a value proposition. Some of the banks are building it into their offerings to the ultra-HNW clients to do aggregation, consolidation, and provide a sort of CIO office to their family office. The objective is trusted adviser status."

But investment is required

While one banker noted that the bank can drill down to each client account to see how much the bank is making from each service or product taken up, there is not yet an automated software system to facilitate that.

"It is important to carefully include all associated costs to work out the true profitability, and that is what banks often lack," he observed. "In our bank, we have good transparency across the P&L across the markets, across the relationship managers, across the client but most of the banks struggle to quantify exactly what is the cost of producing that particular service and therefore what price it should be sold at."

In DPM, for example, the banker maintained that the bank needs to be more differentiated in different client segments and more standardised for the low AUM clients. "We have also introduced what we call the special client desks for those clients below $1 million in AUM; they are serviced by a separate desk and then if they upgrade their AUM they will return to the advisory relationship within the bank again. Differentiation is crucial."

New demands from new generations of wealthy

The discussion turned further towards digitisation. "In Switzerland, we also have a trading platform - white-labelled from a well-known broker - for clients that trade very frequently," a banker reported. "We will bring that into Asia at some stage. Of course, we can offer higher frequency trades at lower prices than the typical private banking client who seldom trades, maybe once a month. The high-frequency clients can then get access to the trading desks, bypassing the RMs. We need to have different offerings, different options for clients really from the typical private banking client."

"Additionally, we need to recognise the changing age groups

of the clients, as we move to the next generations," he added. "The next generation is very much more demanding in terms of how they want to access the bank, digitally I mean, and the banks have to move in that direction."

Leave it to the experts, but do we have them?

In answering a question posed to the group as to who at their banks can or cannot make pricing decisions, one expert replied that he looks at it somewhat differently. "The question for me is do we need a professional pricing for some clients or is it reasonable that every relationship manager or team head or market head is allowed to negotiate prices? In a mid-size organisation of maybe 500 or 1000 people, I doubt that everybody is a good price negotiator."

"In cases where the bank cannot take the prices a RM asks for on behalf of their client, I go personally to them and say 'sorry, we can't do the business at that level. Anecdotally, about maybe a quarter will insist that either you take it or leave it and the rest will say okay, let's try for a while. This works for us as we are relatively small, of course, but perhaps in a major global bank this personal approach is not possible with so many clients out there."

Another perspective was injected when one wealth management advisory expert said that there are so many pricing discussions on products and services, but not enough on costs.

"Why after so many years do banks still not have a digitised onboarding process with efficiencies and the ability to onboard a client within a couple of weeks rather than a couple of months?" he mused. "If there was more focus on cost pricing then I think the cost income ratio would be in better shape. But, for senior management looking at this with a view of perhaps five years, they are going to resist investing heavily in an efficient onboarding process when it is going to sharply affect their bonus for those next five years."

"Too many banks have too much pressure on the RMs to do the wrong thing, to sell the wrong product to the client," he continued. "As we see it from our perspective, the pressure is often too intense on them to meet targets."

The scale is important, noted another expert. "The bigger players have more pricing power because they can walk away from clients, away from deals. The smaller players cannot do that readily."

The discussion turned to the credit cost of leverage for clients and the relationship with the RMs. "One bank I know of would allocate for example 75bp of the total example 200bp spread to the RM, the rest to treasury P&L. We, however, share the entire loan spread with the RMs, but we also charge the RM a cost of capital because every loan has an impact on capital and risk-weighted assets. The better the credit, the lower the cost of capital."

"You are right," interjected another participant, "we all have too short a time horizon, but that is a guilt we all share and is a reality of the modern world."

Pricing – a juggling act to be professionalised

The struggle around pricing in Asia is the focus on transactional revenue as opposed to recurring revenue. "As our Asian clients

move onto their second and third generations of wealth we might gradually be able to start charging along the lines of our Swiss counterparts," one banker observed, "in other words, more for advice as opposed to transactions, but that will take time."

Transparency will be key, partly due to regulatory reform and inspection. "There are many disclosures of monetary benefits that the banks have to provide anyway," another expert added, "but it should also be an internal priority for all the players in this industry that they actually provide the transparency for the benefit of the client and for the bank. RM education is also a key to pricing."

Lines in the sand

The discussion neared a conclusion with further debate about the ability of wealth management advisers to be objective, to focus precisely on the client's needs.

"As an adviser," a participant noted, "it is not about just giving advice that technically speaking works, it is about implementation. If you think something works technically on paper but that on implementation it will implode, a good adviser would say that based on my experience and based on the regulatory environment I advise against it."

A fellow panel member agreed, but wondered whether HNW clients can obtain anything resembling independent advice amidst the proliferation of regulatory directives and supervision and whilst the private banks or advisory firms they work with are also restraining their teams from potentially over-stepping prudent advisory lines in the sand. "Who these days is brave enough to give their clients advice without worrying about the liability?", the panellist wondered. Another expert at the discussion contended that even RMs who work for major private banks - where the compliance teams are increasingly powerful - still have the independence and the flexibility to advise objectively and in depth. "But," he said, "independence is not the key factor here, it is what you can and cannot discuss openly with the client, and where the lines in the sand are that you or your clients do not want to cross. Advisers are ever cagier because of those lines in the sand and the clients can understandably become frustrated and that can then affect their willingness to pay for advice."

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In search of excellence

The debate over the role of IFCs amidst the new standards of global regulation and compliance will continue for many years ahead, as the new directives filter down to affect day to day practices and wealth management psychology.

What the IFCs can do today is listen to the regulators, and to the advisory community and their end clients, and strive ever more strategically and energetically towards transparency and excellence. ■