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Private Banking M&A Newsletter

Asian strategic considerations for Swiss private banks

Deloitte Interview: Mohit Mehrotra, Partner, Deloitte Singapore

At the moment, there is in Switzerland a lot of debate about the potential loss of competitiveness of the Swiss market place against other wealth centres, and especially Singapore. What are your views on this evolution?

We see access to local and global financial markets, strong economic fundamentals, political stability and quality of life as among the key factors in Singapore's favour to become the world's leading wealth management hub. Recent feedback from the industry suggests an average 20% growth per annum of private banks' assets under management in Singapore, in line with the rising wealth in Asia; meanwhile, Switzerland is forecast to experience AuM growth per annum in the mid-single-digit area between now and 2017. We have also found that although the financial services sector is larger in Hong Kong, it has not been able to keep up with Singapore as a wealth management hub. Leaving aside the economic fundamentals, we have found that High Net Worth Individuals (HNWIs) still remain concerned about placing their assets in China, where the rule of law is perceived as less developed.

We believe the challenges private banking businesses face today are much greater than those in the past. The combination of global economic and political instability, higher market volatility and uncertainty, increasing regulatory pressure and rapid strategic evolutions engenders higher complexity and numerous obstacles on the road to engage the 2020 client. In this disruptive environment, new risks emerge in relation to strategy, regulation and compliance, clients' investments, reputation and Information Technology (IT). Therefore we believe the future of selected international wealth management centres will also significantly depend on the ability to adapt to these rising challenges.

As an example, this regulatory compliance burden will particularly challenge profitability here in Asia, where the private banks are still struggling to build momentum towards more discretionary management, and thus tend to experience higher cost-income ratios on average - around 85-90% according to the latest market studies and based on Deloitte observations - than their Swiss counterparts, who have mostly already built up economies of scale and built strong client relationships through several generations of service and average cost-income ratios of 70-75%. The Singapore government has been trying to be pro-active to support the industry through these issues, whilst ensuring stability to the Singapore economy. We believe that the growing pains for private banks operating in Singapore will allow them to strengthen their franchises and allow them to flourish over time.

Could you tell us what you see as the current strategic focus for private banks in the local South East Asian market?

We see a lot of appetite for SME entrepreneurs and business-owner clients, as client wealth in the region is often first generational and entrepreneurial. Over the years, domestic and regional Asian banks have focused on growing their SME lending portfolios and consequently developed relationships with business owners and entrepreneurs. These banks are well placed to capture more share of wallet as they have been aggressively expanding their Affluent/ High Net Worth banking value propositions in light of growing economic prosperity and affluence within the region.

While customer relationships developed by these domestic banks over time could be a potential barrier to entry for international private banks looking to tap into the market, we see the potential lack of quality relationship managers and product specialists within such banks as a potential hurdle. The domestic players may not be able to serve more sophisticated client needs, especially those with exposure to the global private banks.
We see the talent pool of established Swiss or international private banks as a key competitive advantage in the market, especially as the customer base is maturing and becoming more familiar with the private banking experience. The battle for talent is expected to get a lot fiercer and private banks will need to ensure that there is a strong focus on hiring, training and retaining the best talent to serve their clients.

What do you see as the key drivers for private banking M&A in the region?

Singapore and the Asia Pacific region are experiencing rising levels of affluence, and consequently rapidly growing as hub for wealth management services. Swiss and international private banks have been entering Asia in droves in search of AuM. However, smaller scale players have found that insufficient AuM leads to higher costs, as well as challenges in marketing, client servicing and retention of human capital. Specificities of the less-mature private banking Asian client base are an additional constraining factor for profitability generation for new entrants.

We have also observed that there is a scarcity of experienced relationship managers; coupled with the personalized nature of private banking and the relationship-centric Asian business climate, we have a situation where it may be difficult for some private banking business to grow organically to a breakeven or profitable level within a feasible amount of time. For such businesses, it may make sense to divest, acquire or otherwise merge with other wealth managers in order to generate scale and achieve sustainability. This is likely to further drive M&A in the Asia Pacific wealth management market. We are already seeing a few small players seeking to exit the market due to cost pressures, as well as selected international banks. Bank of America sold its international wealth management business to Julius Bär in 2012; DBS acquired SocGen's Asian business in 2014 and the international arm of Coutts, RBS's private bank is also presently for sale. These are candidates for M&A for incumbents who intend to stay the course and build their Asian franchises.

At the larger end of the scale, we do not see many M&A opportunities as most profitable banks believe that there is significant potential in the Asian market, and are more likely to increase investment rather than exit. Local Asian banks sometimes invest in their private banking operations through partnerships with established western players, who can bring value-adding private banking expertise which can be lacking in-house, and in order to accelerate market penetration and retain HNW customers.

Case Study of Lombard Odier’s strategic agreement with Thai-based Kasikornbank

Transaction background

After the lifting of the country’s secrecy laws removed local wealth managers’ longstanding competitive advantage, Swiss banks have increasingly looked overseas for growth. Being one of the fastest-growing private banking markets since the global financial crisis, Asia has therefore become a prime target for the industry.

According to UBS’s Wealth-X survey, while the world’s billionaires collectively increased their wealth by 12 per cent in the past 12 months, 30 per cent of that growth came from Asia. Specifically, over the past five years, the HNWI market in Thailand has increased 12.7% per annum, significantly higher than the Asian average over the same period of 9.5%.

However, despite the attractive market potential of the area, international private banks with traditional offshore focus face difficulties in raising their market share. This is explained by the fact that two-thirds of the Asian wealth is generated onshore and this market is still dominated by local banks.

Transaction structure

Lombard Odier has entered a strategic agreement with Kasikornbank in order to expand the scope of its activities in Asia and satisfy the Thai bank’s private clients’ need for global investment solutions and complete wealth management expertise, with products at home and abroad.

According to the agreement, Lombard Odier will manage global investment funds on behalf of Kasikornbank's private clients in return for a management fee. On the other hand, the Thai bank will receive advisory training for its relationship managers and financial advisors (see Figure 1). Under a separate arrangement, Lombard Odier will also act as an exclusive offshore custodian bank for Kasikornbank clients.

This partnership between Switzerland’s oldest private bank and Kasikornbank is similar to other deals Lombard Odier has recently entered in Japan, Australia and South Korea. Those agreements have given the Swiss bank access to attractive domestic markets with fast-growing HNWI market share most wealth in the Asia-Pacific region is held.

Strategic objectives

Through this agreement, Lombard Odier is willing to strengthen its activities in Asia and extend its reach into Southeast Asia for the first time. Through the local client base of the Kasikornbank, the Swiss private bank aims at expanding its networks in the area. In this way, the firm can go into local markets without increasing its costs.

On the other hand, Kasikornbank is willing to improve its private banking business using Lombard Odier’s international service standards tailored to the HNWI customer segment. Kasikornbank’s employees will also strongly benefits from the in-depth training provided by Lombard Odier’s professionals.

Snapshot of Kasikornbank

Kasikornbank Public Limited, formerly known as the Thai Farmers Bank, is one of the leading universal banking groups in Thailand. Kasikornbank was established in 1945 and has been listed on the Stock Exchange of Thailand since 1976. It operates more than 1’000 branches and sub-offices across Thailand and runs overseas offices in China, Japan and Burma. As of September 2014, the bank had THB2.4trn ($73.6bn) in assets and is the 4th largest commercial bank in Thailand. The company employs 20’700 people.

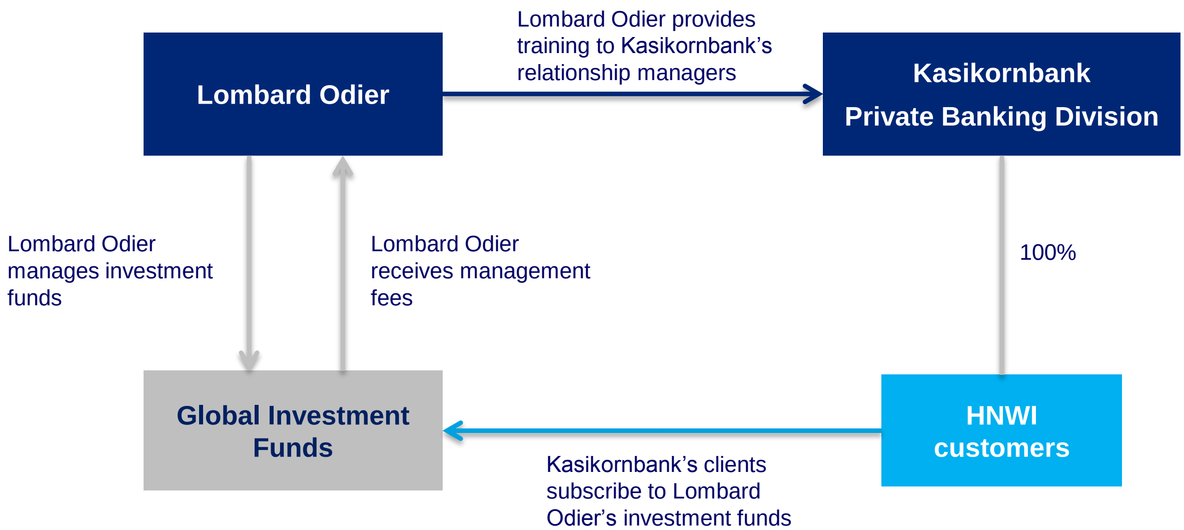

Figure 1: Agreement Structure

Deloitte has advised Kasikornbank on selected aspects of the agreement. For additional information on this transaction please contact Mohit Mehrotra, Partner of Deloitte in Singapore.

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