

## China: The Wealth Management Agenda

## Rise of the Wealthy

The potential for the wealth management business within China is on the rise. However the geographic spread of the country has created some doubts for service providers, as to whether the 'one model fits all policy' will work in China. Private banking was a restricted market till about 2005-2006 and thus in a relatively less sophisticated market, private banks and wealth management service providers are retaining focus on the urban markets.

China is the second largest wealth management market in Asia with significant wealth creation driven by unprecedented economic growth in recent years. Reports state that in 2007, the number of High-Net-Worth Individuals (HNWIs) in China reached nearly 350,000 in 2006, up almost 8% from 2005. In terms of HNWI wealth in Asia-Pacific, about one-fifth resides in China.

However, the wealth management market in China remains in its infancy, but it can be expected to evolve rapidly, in line with the development and de-regulation of financial markets. The key to growth is dependent on a number of factors but will first be prompted by continued local regulatory relaxation.

The growth figures coming from a low base in an emerging market can often be misleading as every increment can appear substantial. However analysts across all foreign private banks are betting strongly on the local Wealth Management business. There is a strong expectation of robust growth over the coming few years. A majority of the private banks are now expanding wealth management services into Shanghai, Beijing, Shenzhen and Guangzhou which roughly accounts for 60% of China's wealth.

### Wealth Management: The Business Model

Celent defines wealth management as a suite of services and products designed to assist in the accumulation and management of wealth for individuals with at least US\$100,000 in investable assets.

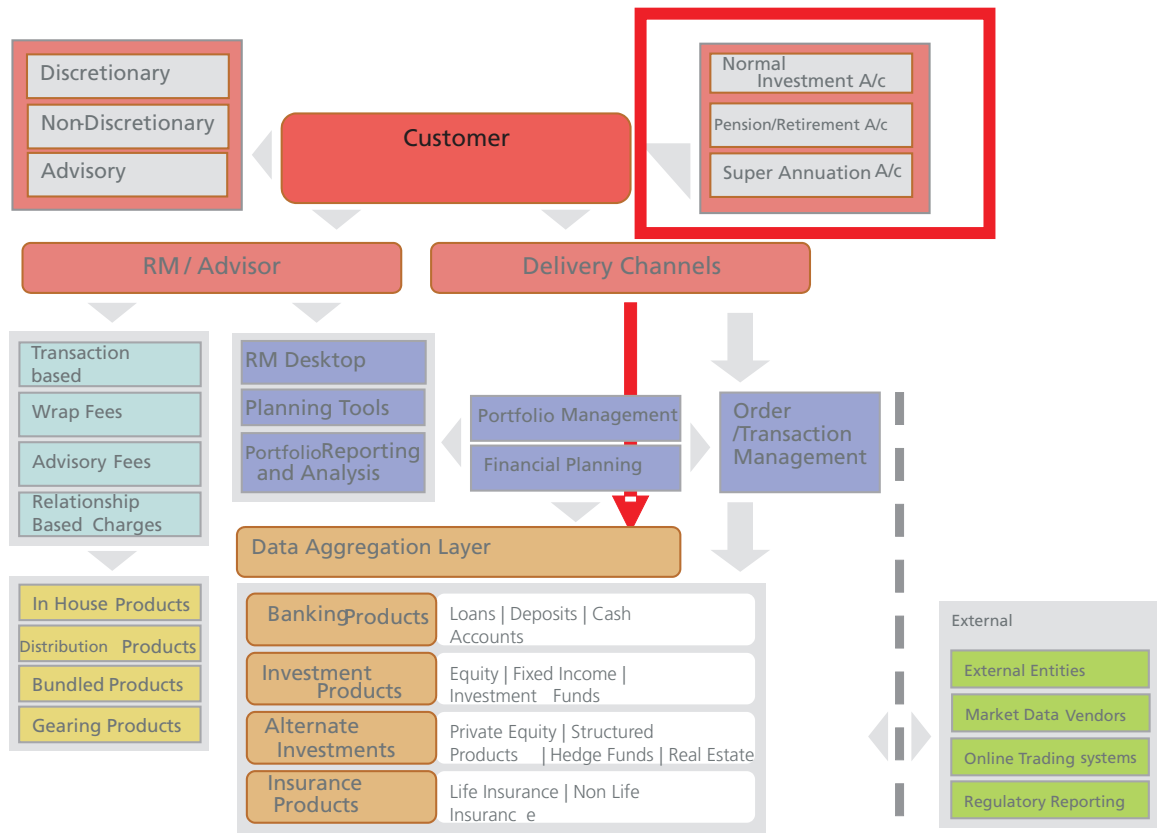
The wealth management marketplace is evolving with the expansion of the affluent client pool and increased competition through mergers, acquisitions and the introduction of non-traditional players. Wealth managers are setting business goals that require innovative technology

solutions to help increase sales, reduce costs, retain current clients and attract new ones. For wealth managers to succeed in this marketplace, they must coordinate their processes around their customers. They need to carefully evaluate and quickly deploy the right technology solutions that are already providing competitive advantage in the market. The considerations to create or strengthen a customer-centric model are complex, but most firms have recognized that long-term success in this competitive market is dependent upon the ability to deliver customer-centric products and services.

### The wealth management service canvas for banks includes:

- ▶ **Delivery channels:** Anywhere & anytime through branch/call center/online/POS/PDA
- ▶ **Personalized services:** Advisory services /relationship managers/financial planning experts to manage accounts and plan financial goals
- ▶ **Investment tools for customers and their financial planners to manage wealth:** Analyze portfolio, rebalance portfolio against model portfolio, portfolio simulation and 'what-if' tools
- ▶ **Product types:** Traditional banking, traditional investment products and alternate investments
- ▶ **Straight Through Processing:** End-to-end transaction processing for investments
- ▶ **Tax planning:** Country-specific tax and social security
- ▶ **One stop financial shop:** Interface with market data vendors/banks/depositories/clearing house/ custodians/brokerage house
- ▶ **Concierge services:** Lifestyle related value added services
- ▶ **Customized views and reports:** Portfolio specific or across portfolios
- ▶ **Consolidated view:** Complete financial picture in one screen
- ▶ **Strict adherence:** Financial regulation, compliance and other country-specific mandates
- ▶ **Secure and trusted environment:** Data storage

## Offerings: componentized view



## The changing landscape

### Dynamics of the mass affluent pie

The markets across the globe have experienced several highs and lows over the years and analysts have recognized and accepted this as a key challenge which would affect the profitability and growth of the private banking and wealth management sector.

While wealth management is essentially a service provided across customer categories, there is an increased focus on the mass affluent and HNW segments where a combination of advisory services, do-it-yourself services, management and customized reporting is required. The ultra HNW segment continues to be serviced by the private banks, while retail banks woo the mass affluent segment with a vast array of products across banking and investment domains, topped with insurance offerings and unique product bundling features.

In a space traditionally dominated by private banks and niche service providers, retail banks have streamed into the space to handle the booming mass affluent segment. Typical model on view is the distribution model with end-to-end services across the banking and investment domains. Banks have identified the key revenue drivers as:

- ▶ Revenue from distribution (3rd party products)
- ▶ Revenue from advisory services
- ▶ Cross sell opportunities to existing banking customers

Product manufacturing and revenue based on assets under management and ROI (Discretionary PMS) would be the way forward for banks.

There are critical challenges in serving the mass affluent segment, depending on the institution. For example, private banks serving the HNW and UHNW market, are scaling up to serve the larger number of clients in the mass affluent segment but have not yet clearly figured out the right technology and process investments to make. While, on the other hand, retail financial institutions have the technology and scale to reach a large number of customers, but are struggling to provide advisory services on a mass scale - so critical for the affluent segment. Wealth management institutions will need to chart the

path to profitably serve the mass affluent segment or must suffer a severe competitive disadvantage.

### Increasing focus on advisory services

Private banking and wealth management customers are turning cautious with their investments and are seeking better service providers. Quality of service, reporting and the quality of investment advice remain some of the important selection criteria for customers. 'Know-all' advisors, offering advice across different product types, suggesting unique product bundling, predicting trends in the local and as well as global markets and suggesting investment protection mechanism are key to the success of wealth management services. With the frequent highs and lows in the markets, there is an apparent disconnect between advisors and customers. Advisors are turning to fact-based analysis and even detailed case studies to bridge the gap.

However, it would be pertinent to note that there is also a growing trend towards do-it-yourself services, where knowledgeable customers are not fully dependent on the advisory services provided by the bank.

To provide such high levels of service, banks are seeking help from systems that offer a holistic view of the customer relationship across assets and liabilities, to tailor appropriate investment solutions.

### Product range and innovation

Banks have realized that product features and the range of products are key differentiators in the fiercely competitive market. Product manufacture is not every bank's cup of tea and the 'gap' in product offering is catered to by distributing products originating from other issuers. While product manufacture is definitely the way forward, distribution income continues to be a key revenue stream.

The investment domain spans across a wide range of products and there is a definite shift from traditional investments in funds, equities and fixed income to alternate investments like structured products, real estate, private equity and hedge funds.

Banks have also realized the benefits of innovation in terms of product bundling and utilizing 'sleeping

assets' of customers. Loan products bundled with insurance, margin lending, self funding instalments to gain geared share exposure and bundling of banking & investment products are some of the interesting products showcased.

Wealth management is new in China and the range of domestic product offerings is limited. Typically, wealthy individuals have a bipolar asset allocation with half of the asset holdings allocated to cash, deposits and money market funds, with the balance invested in equities and bonds. There is growing trend to invest in Structured Deposits with Equity and Currency as the underlying, as the risk appetite of the HNWI is steadily on the rise.

## Key tech trends

### Service Oriented Architecture (SOA)

The wealth management process is dynamic and involves change at a rapid pace, mainly to incorporate new products, new process, regulatory requirements and address ever changing customer demands. Service providers must quickly respond to business changes with agility; leverage existing investments in applications and application infrastructure to address new business requirements; support new channels of interactions with customers, partners, and market data vendors.

Wealth management providers and private banks must focus on open standards for communication with external entities. Service Oriented Architecture and web service standards is and will be the key components of current and future wealth management systems as it will help technology vendors in delivering flexible and cost effective solutions. Wealth management is a complex process and to support this complex process the system needs to embed, incorporate and interface with multiple systems for customer information, market data, transaction data and accounting.

Account aggregation, one of the critical components in the wealth management process will be served well by the 'SOA trend' as it will enable service providers to share, integrate and data mine across multiple systems and entities.

### 'One system' v/s multiple systems

The ideal wealth management system should be able to provide a complete 'front to back'

functionality for all asset classes, product types and related process, Straight through Processing for all transactions, account aggregation and portfolio planning, monitoring and reporting. Wealth management is essentially a complex process which runs across various product types in the investment and banking domains. There are 'one system' vendors and 'niche area' vendors currently servicing the ever increasing technology requirements in this domain.

In recent times there is a growing trend of adoption of the 'one system' approach which offers an integrated platform for traditional banking and wealth management products and processes. Retail banks entrenched, expanding or venturing into the wealth management space are increasingly seeking such integrated platforms to service customers.

The typical 'one system' provides the necessary infrastructure to support various asset classes and provide the bank with a consolidated view of the customer's portfolio across banking and investment products. With a topping of SOA, web service standards and robust work flow engine; it would provide the ideal 'one system' solution for the banks to service their customers. However going by the business domain it caters to, wealth management systems inevitably need to interface with niche area systems and external entities.

The shortcomings of the 'one system' approach in terms of depth of functionality and infrastructure changes which have to be optimally countered across the system. This could entail higher costs and migration related issues.

### Future Trends

In China, the level of sophistication and experience with more complex products is lesser than in advanced markets. However, as the businesses and the numbers of wealthy Chinese grow, expand and mature, there will be a marked change in the product offering, services levels and channels of offering.

The Chinese wealth management market would continue to liberalize, and there will be increased competition from both local and foreign banks in China.

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