Swiss Financial Services in 2030

Wealth Management

Winning transformation strategies for a decade of major change

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Executive summary

Swiss wealth management (WM) has a long, proud tradition and has demonstrated overwhelming long-term success. The recent past, however, has been more challenging, as Swiss private banks (PBs) face regulatory obstacles to offshore banking and corresponding pressure on margins. Profitability levels have been below expectations despite a decade-long bull market, and potential growth opportunities in the traditional offshore business now seem limited.

Looking towards the next decade, these underlying challenges remain and new drivers of change will shape the WM industry of the future. New competitors are on the cusp of disrupting the industry with entirely new offerings, catering to the needs of a new generation of WM clients, as millennials enter their prime earning years. Hyper-customised products will become increasingly common, enabled by IT as a differentiator and the growth of platform-based services (such as SaaS, PaaS, cloud, etc.). The competitive advantage of Switzerland as a banking hub could therefore decline, making modernisation of the sector's business models and of the regulatory regime, including Swiss bank secrecy, imperative as a catalyst to spur innovation and efficiency.

We have identified five winning transformation strategies as 'no-regret moves' for forward-looking PBs that will set them up for success in the future – irrespective of the overall direction of the WM industry:

1

Build ecosystems and explore M&A

- Focus relentlessly on providing a differentiated value proposition, also by partnering in or establishing own ecosystems
- Explore M&A opportunities to strengthen your core offering and build scale

2

Develop innovative ways to engage with clients and prospects

- Analyse and leverage bank and third party data to further enhance the client experience
- Upgrade digital marketing capabilities to better reach prospects through targeted campaigns
- Empower Relationship Managers by providing integrated tools, analytical insights and streamlined ways of working

3

Focus on innovation and R&D

- Significantly invest in digital innovations to counter threats from new competitors (e.g., co-browsing, advanced advisory and personal finance management features)
- Hyper-customise products and solutions powered by data and automation

4

Leverage cloud services

- Leverage cloud technology to improve agility, lower costs, drive innovation, and benefit from industry-specific solutions
- Shift spending paradigm from CapEx to OpEx

5

Contribute to setting the global 'platinum standard' for secrecy and privacy in digital WM

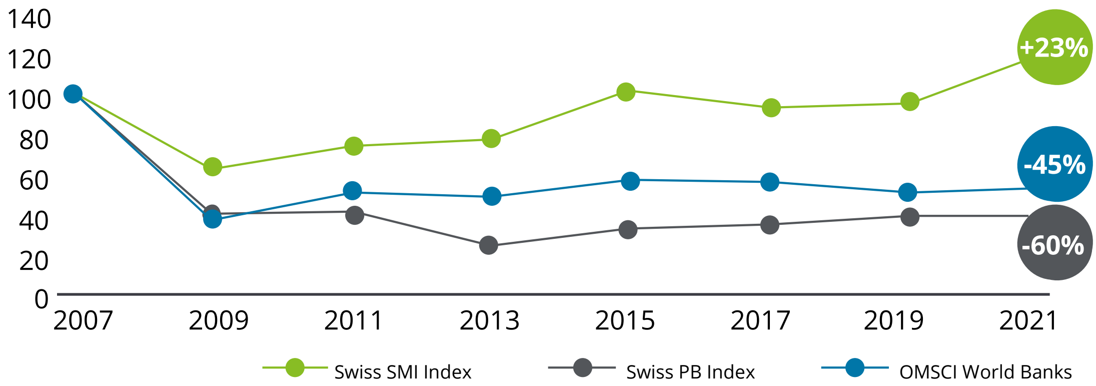
- Engage with policy-makers to review and modernise Swiss bank secrecy as a catalyst for innovation and efficiency
- As a result, leverage digital innovations and cloud technologies while safeguarding clients' privacy

Swiss wealth management today

Swiss private banks (PBs) have delivered sub-par performance over the past decade, often leading to shareholder value destruction. Future success will depend even more on challenging the status quo with bold solutions.

Swiss WM has a long and proud tradition of long-term success. The recent past, however, has been more challenging. The financial performance of Swiss PBs has been lacklustre overall. The long-term positive correlation between PBs' performance and broader stock market performance has been broken. Indeed, Swiss PB stocks have significantly underperformed the Swiss Market Index (SMI) since the financial crisis (Chart 1).

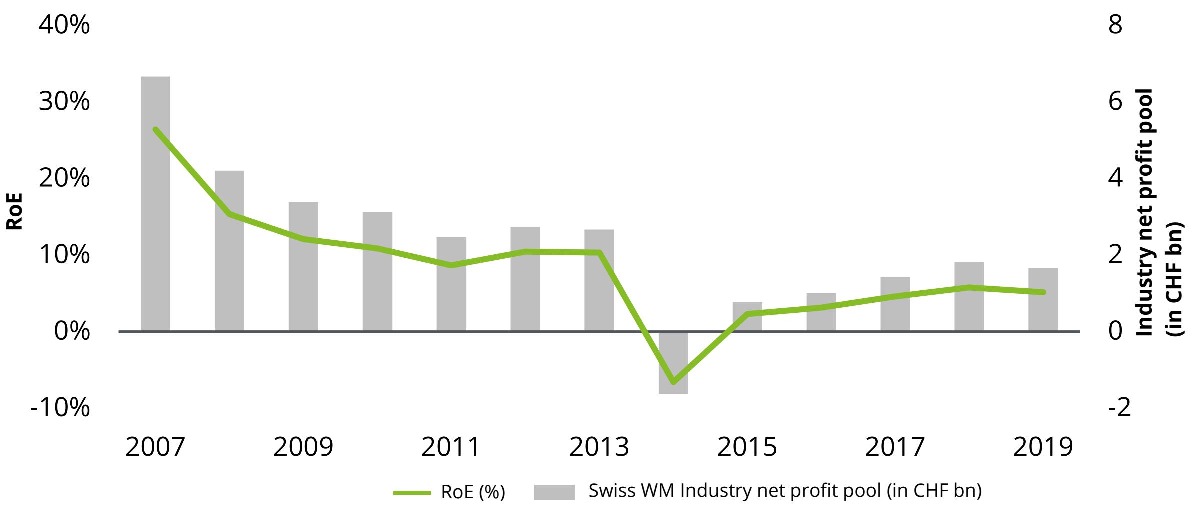
Chart 1. Price performance of Swiss banks since 2007



Source: Capital IQ
Note: Swiss PB Index includes Credit Suisse, UBS, EFG, Vontobel, LLB, VP Bank and Julius Baer

The return on equity has been declining substantially since 2007, to around 5 per cent today, with returns that are significantly below PBs' cost of capital, which is typically ranging between 7-12% depending on the size and profile of the bank (Chart 2).

Chart 2. Swiss WM industry net profit pool and RoE evolution since 2007



Source: SNB, Deloitte analysis
Note: Sample comprising listed banks, foreign-owned banks and PBs and excluding the two large universal banks UBS and CS. The substantial negative dip in industry profits in 2014 was primarily caused by foreign-owned banks.

We believe there are two key root causes behind this lacklustre performance:

Firstly, PBs have struggled to contain the structural fee and margin erosion in a WM industry that is increasingly characterised by tax transparency. Traditional high revenue-generating products and services, such as discretionary mandates, have lost ground to more cost-efficient products and services (e.g., passive solutions or lower-value advisory services). Overall, clients have become significantly more cost-sensitive and ready to switch to more cost-attractive products or competitors.

Secondly, increasing regulation has negatively impacted the ease of doing business for PBs. For example, new cross-border rules have complicated the onboarding of international clients. Most Swiss PBs have reduced the number of target markets in the past years and some, in particular those with limited international onshore locations, have shifted their focus to Swiss-domiciled high net worth individuals (HNWI) – a highly competitive market with limited growth. This development has contributed to a stagnation of offshore client assets (with some offshore clients repatriating their assets) and is now restricting the scope and ability of Swiss PBs to attract new assets.

Swiss PBs have responded with attempts to cut their cost base, mostly through headcount reductions (a decline of 18 per cent from 2007 to 2019) and increased automation, upgraded technology, and modernisation of the operating model.

Overall their efforts have had limited success, as cost/income ratios have increased from below 57 per cent on average in 2007 to 82 per cent on average in 2019. Most importantly, Swiss PBs have been hampered by increased compliance requirements, by their personnel-intensive individualised client service model, and by negative external factors such as the persistent strength of the Swiss Franc and negative interest rates, as well as ever more demanding clients. Swiss PBs will need to embrace major change to reclaim their proud heritage and generate value for shareholders.

Major change drivers in the 2020s

Change is coming to the WM industry. Client demands, increased competition, cost pressures and technology are already driving transformation. These trends will put unprecedented pressure on PBs, but generate new opportunities as well.

We observe a number of trends bringing fundamental change to the WM industry across six key dimensions:

Dimension	Major trends observed
Markets & competitors	• Newcomers (e.g. Big Tech, FinTech and NeoBanks) disrupt the industry with entirely new offerings • Growth of ecosystem models (driven by PSD2 regulation) leading to new value propositions with growing importance for intermediaries, e.g. scalable value-added platforms with multi-custody and multi-manager capabilities • Active M&A strategies from leading players to grow and leverage the advantage of scale
Clients & society	• New client profiles, as millennials are entering their prime earning years • Rising importance of digital interfaces vs. trust-based human interactions – digital marketing key to reach prospects online and generate leads • Wealth increasingly not just defined through money, but through a holistic set of values and social impact
Products & services	• High focus on sustainable and socially responsible investments • Growth of hyper-customised products, private market investments (incl. tokenisation), sophisticated tax services (e.g. tax efficiency fees), and other value-added services (e.g., wealth planning) • Realignment of fees versus true value created for clients
Talent & culture	• Strong competition for talent with Big Tech due to new job profiles – PBs need to redefine their role in society to attract talent again (i.e., sustainable finance) • Role of RM expanding towards orchestrator across broader service categories (e.g., wealth planner)
Platform & technology	• New mindset of leveraging IT as differentiator and innovator, both as orchestrator of different services and driver of customer experience • With growth of cloud services (e.g. SaaS, PaaS), PBs will become more infrastructure-light • Growing importance of deep learning, AI, and data analytics driving customisation
Regulators & governments	• Comparative advantage of Switzerland as an offshore banking hub needs concerted effort to defend – potential ease in cross-border data regulation to enable innovation and efficiency • Globalisation on the retreat, stronger regionalisation, with wealthy individuals further leveraging their ability to move wealth between jurisdictions • Global peak in new regulatory interventions has likely been reached, but we expect higher transparency requirements in investments; regulatory compliance risk is on the rise, with regulators and governments on the hunt

In light of these anticipated industry shifts, PBs need to adequately prepare and define where they want to play and how they intend to win. In sum, we recommend winning PBs define their strategy based on their key beliefs, refine their strategy through stress testing against alternative scenarios, and identify contingent strategies that can be implemented once there is clarity about the direction of the WM industry.

Deloitte recommends a proven five-step process for PBs to develop a future-proof strategy:

Define a shared view of the long-term direction of the WM industry

Determine what the business needs to look like in order to succeed

Stress test where-to-play and how-to-win choices

Identify two to three tangible initiatives that have the greatest potential to fulfil the bank’s long-term ambitions

Ensure a critical mass of resources and clear measures of success for each key initiative

Winning transformation strategies

PBs find themselves confronted by significant transformation needs. We have identified five winning transformation strategies that should play a key role in future-proofing industry leaders.

In light of the major industry shifts described above, PBs face significant transformation needs. We have identified five winning transformation strategies as 'no-regret moves' for forward-looking PBs that will set them up for success in the future – irrespective of the overall direction of the WM industry.

1 Build ecosystems and explore M&A

As many WM products and services have become somewhat commoditised over the years (e.g., stock market transactions, basic investment management), clients nowadays expect more value and clear differentiation from their PBs. Therefore, PBs need to broaden their offering to differentiate it and make it compelling. However, as no single player can be best-in-class in everything, it would not make sense to build and offer all such value-added services in-house. Instead, each PB needs to determine which part of its value chain is truly a differentiating factor and should be delivered in-house, what can be delivered by cooperating with ecosystem partners, and what might better be provided by others. In sum: PBs need to carefully evaluate their desired role in an ecosystem and how they want to configure it.

In addition to partnering in ecosystems, PBs may explore using M&A to strengthen their core offering and build scale. Doing so will make it more likely that PBs can be either at the centre of an ecosystem or a key contributor to it (as opposed to being smaller niche players with blurred profiles that often end up in less prominent roles in ecosystems). We believe attractive consolidation opportunities will arise in the coming years. Bold ideas for PBs to reposition their value chain could be the following:

- Focus on alpha creation and consider downsizing or selling parts of the current plain vanilla investment management capabilities
- Consider M&A or partnerships with large Asian/LatAm PBs, PB divisions of universal banks or insurance companies
- Build or acquire wealth planning and wealth structuring capabilities
- Consider bold strategic partnerships in IT and Operations to enable a cost-efficient back office utility (e.g., in AML/KYC).

2 Develop innovative ways to engage with clients and prospects

The challenge for the WM industry is to remain client-centric in an increasingly digital banking environment. With many prospects arguably spending the majority of their work time and often even leisure time online, PBs will need to upgrade their digital marketing capabilities in order to better reach prospects through targeted campaigns.

In addition to further personalising their client experience, PBs will need to systematically analyse and leverage the breadth and depth of client data already available to them. One idea is that PBs could enhance their existing client connectivity based on personal relationships with analytics-driven propositions, and partner with entirely new industries and sectors, such as luxury platforms.

Lastly, client advisory, arguably the core human element in the WM life cycle, might also be digitally enhanced. Future-proof relationship managers will be able to serve a community of clients both in the digital and in the non-digital area to build a differentiated individual brand. PBs should therefore empower their relationship managers to provide hybrid advice, combining the best of human and machine elements, by providing integrated tools, analytical insights and streamlined ways of working.

3 Focus on innovation and R&D

Compared to other industries, banking in general and WM in particular are lagging behind when it comes to innovation. The 2019 EU Industrial R&D Investment Scoreboard, published annually by the European Commission, lists the EU's 1,000 largest R&D spending companies. It includes only 24 banks (i.e., just 2.4 per cent of the 1,000 companies). None of these banks is a pure PB, and only 9 banks are listed among the top 100 R&D spending companies. This is particularly worrying at a time when the WM industry is being significantly disrupted by new technology. PBs should aim to confront and overcome this digital challenge by investing in digital innovations (e.g., co-browsing). We believe PBs in Switzerland, given their position in a leading WM hub, should be at the forefront of such innovation efforts.

4 Leverage cloud services

As a result of often postponed IT investment decisions, the IT landscape of many PBs nowadays consists of legacy systems that require high maintenance effort and costs. However, many PBs still seem reluctant to fully leverage and integrate cloud services as part of their 'business as usual'. Instead, maintenance of the existing systems still seems to be choice of many PBs, which reduces their agility and ability to innovate.

Cloud-enabled organisations typically move away from a 'do-it-yourself' mentality towards embracing external providers with scalable, flexible, fast and cost-efficient services. The benefits delivered by leveraging cloud services may be significant for a PB, though this depends on its level of cloud maturity. Cloud services can reduce an organisation's IT costs by enabling the transfer of non-core services and infrastructure to the cloud. As an example, PBs can replace or upgrade existing non-core applications (e.g., Enterprise Resource Planning or Customer Relationship Management) and may rationalise and streamline parts of their infrastructure by migrating it to the cloud. In addition, cloud services typically enable faster time-to-market and increased scalability, for example by automating processes and moving them to the cloud. Lastly, leveraging cloud services may truly transform a PB and foster innovation and value chain optimisation, such as accelerated integration of innovative services and products or by fully integrating 'bricks and clicks' into a true omni-channel offering.

Overall, cloud technology enables PBs to improve their agility, drive innovation, leverage industry-specific solutions and shift their spending paradigm from CapEx to OpEx.

5 Contribute to setting the global 'platinum standard' for secrecy and privacy in digital WM

Due to the nature of their business and in light of recent investor protection regulations, PBs are required to have a deep understanding of their clients. The WM industry as a whole is expected to adhere to the highest global standards of diligence in combatting financial crime, terrorist financing and tax fraud. Therefore PBs must actively investigate confidential client information. Multinational treaties and initiatives around tax transparency, avoidance of aggressive tax planning, transparency in regards to shareholder and beneficial ownership, and the respective information gathering and reporting requirements create a situation, where PBs become holders or 'controllers' of significant private and confidential information about their clients. PBs' increasing duty to collect and analyse information about their clients partly contradicts the growing importance of privacy regulations. The EU GDPR, the Swiss FDPA revision, and the famous 'Schrems' decision are examples of a push to protect client data. Not surprisingly, Swiss PBs have often been on the conservative side when evaluating digital innovations or opportunities around cloud technology and, as a consequence, offshoring client data.

Maintaining compliance with all regulations and making full use of digital innovations, while safeguarding clients' privacy and personal data, will therefore be crucial to the success of the Swiss WM industry going forward. Combined with the traditional safety and stability of the Swiss government and economy, this holistic approach may have the potential to become a truly unique selling proposition, namely the global 'platinum standard' for secrecy and privacy in digital WM.

In order to achieve this ambition, PBs will require specific and reliable standards for leveraging digital innovations and cloud technologies while safeguarding clients' privacy and personal data. Switzerland's current regulatory framework, where every PB has to find its own way through complex regulations, may jeopardise this significant opportunity for the Swiss WM industry. Deloitte proposes to initiate a review and simplify the secrecy and privacy regulatory standards with the relevant stakeholders, such as supervisory bodies, auditors, industry associations, and other experts.

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