



WORLD WEALTH REPORT 2012



RBC Wealth Management

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Preface

Capgemini and **RBC Wealth Management** are pleased to present the *2012 World Wealth Report (WWR)*, which offers insights into the size, composition, geographic distribution, and investing behavior of the world's population of high net worth individuals (HNWIs)—those with US\$1 million or more¹ at their disposal for investing. The report also outlines the state of macroeconomic conditions and other factors that drive wealth creation to illustrate the conditions in which HNWIs were making investment decisions in 2011.

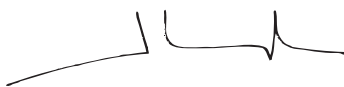
In 2011, our analysis shows, there was about the same number of HNWIs in the world as there had been in 2010. However, HNWIs' aggregate investable wealth, as measured by asset values, declined for the second time in four years. A look at economic and market conditions in 2011 shows the reasons were many, but uncertainty over the ongoing Eurozone debt crisis was clearly a critical factor.

While investors had expected a bumpy road to global economic recovery, the Eurozone crisis especially unsettled investors by increasing market volatility, and helping to slow global economic growth. And more than that, the Eurozone crisis offered a sharp illustration of the longer-term dilemma many debt-strapped countries face: how to juggle seemingly inconsistent imperatives such as austerity and growth. The economic and market uncertainty sent many investors to the sidelines in 2011, or at least to lower-risk investments like U.S. Treasuries, which are typically sought for their ability to preserve capital.

The Eurozone crisis also took its toll on Asia-Pacific. The weakened state of Europe's developed economies reduced demand for Asia-Pacific goods, prompting that region's economic growth to slow tangibly. Still, the number of HNWIs in Asia-Pacific increased slightly in 2011, while the number in North America declined. As a result, Asia-Pacific became home to slightly more HNWIs than any other region for the first time—though North America still accounted for the largest regional share of HNWI wealth.

For wealth management firms and advisors, the volatility in 2011 provided yet another challenge to their business models. Many firms will now need to determine how to leverage intelligently the scalable components of their overall operations, while delivering expertise and a resonant client-advisor proposition. Above all, firms will need to build and maintain robust client-advisor relationships that will help to drive client satisfaction and business growth even when market conditions are challenging.

Until next year,



Jean Lassignardie
Global Head of Sales and Marketing,
Global Financial Services
Capgemini



George Lewis
Group Head
RBC Wealth Management

¹ Investable wealth does not include the value of personal assets and property such as primary residences, collectibles, consumables, and consumer durables



A Message from



RBC Wealth Management

RBC Wealth Management is proud to bring you the *2012 World Wealth Report* with Capgemini. This inaugural collaboration leverages our mutual expertise and global resources to continue producing what we believe to be the global benchmark in wealth management thought leadership.

Through this unique partnership, we have been able to examine the key drivers of wealth creation and the global trends impacting high net worth individuals (HNWIs). The report provides you with unparalleled insight into HNWI behavior and the global state of wealth.

This year's results reinforce our existing focus on thinking globally and acting locally. As our clients' trusted advisors and guardians of their wealth, we need to leverage our global expertise to understand each region individually, and continue to provide expertise that will help our clients preserve and grow their valuable assets. At RBC Wealth Management, we know that each HNWI has a unique set of needs and priorities, and it is our strength, stability, and personalized approach that will allow us to help our clients flourish, wherever they are in the world.

This year's spotlight on how wealth management firms look to scalable business models to drive profitable growth and bolster client relationships also has significant resonance for RBC Wealth Management as we continue to execute our strategy for global growth.

The Royal Bank of Canada is a symbol of Canadian heritage and a pillar of the financial services industry worldwide. We believe that the strength of our business, our global expertise, and our commitment to integrity in serving clients across the globe for over 100 years are what set us apart. We look forward to leveraging this expertise and our global network to investigate HNWI and wealth management industry trends through the World Wealth Report.

We trust you will find value in this report, and, in the years to come, we look forward to continuing to further build our partnership with Capgemini.

A handwritten signature in black ink, appearing to read 'George Lewis', with a horizontal line underneath.

George Lewis
Group Head, RBC Wealth Management

World's Population of HNWIs: Number Edged Up in 2011, but Aggregate Investable Wealth Declined

- **The world's population of high net worth individuals (HNWIs) was little changed in size at 11.0 million in 2011, but HNWIs' aggregate investable wealth as measured by asset values slid 1.7% to US\$42.0 trillion.** The overall decline in investable wealth largely reflected the disproportionate impact of losses among higher wealth brackets,² in which investors are often more likely to be invested in less liquid and more risky assets.
- **Asia-Pacific is now home to slightly more HNWIs than any other region, though North American HNWIs still account for the largest regional share of HNWI wealth.** The number of Asia-Pacific HNWIs hit 3.37 million in 2011, compared to 3.35 million in North America, and 3.17 million in Europe. In terms of assets, HNWIs' investable wealth totaled US\$11.4 trillion in North America, down 2.3% from 2010, and was US\$10.7 trillion in Asia-Pacific, down 1.1%. Among Europe's HNWIs, wealth was down 1.1% in 2011 at US\$10.1 trillion. In Latin America, HNWI wealth declined 2.9%, though the HNWI population grew modestly, by 5.4%.
- **India and Hong Kong topped the list of countries losing HNWIs in 2011.** Equity-market capitalization plunged in India in 2011, wiping out asset values and levels of investable wealth. This helped to reduce the size of the country's HNWI population by 18.0%. A similar stock-market decline in Hong Kong (where HNWIs are traditionally highly exposed to equities) helped to reduce that HNWI population by 17.4%.
- **The bulk of the world's HNWI population remains concentrated in the U.S., Japan, and Germany.** Together, the three countries accounted for 53.3% of the world's HNWIs in 2011, up slightly from 53.1% in 2010. Beyond the top three, there was little change in the geographic distribution of the world's HNWIs, though the loss of HNWIs in India was enough to push it from the Top 12, and it was replaced by South Korea.

ASIA-PACIFIC'S HNWI SEGMENT BECAME THE WORLD'S LARGEST IN 2011

After witnessing robust growth of 8.3% in 2010 and 17.1% in 2009, global HNWI population grew marginally by 0.8% to 11.0 million in 2011 (see Figure 1). Most of this growth can be attributed to HNWIs in the \$1-5 million wealth band which grew 1.1% and represents 90% of the global HNWI population. HNWIs' aggregate investable wealth, as measured by asset values, declined 1.7%—the second drop in the last four years (see Figure 2). Investable wealth had gained 9.7% and 18.9% respectively in 2010 and 2009, when there had been a significant rebound from the hefty crisis-related losses of 2008. In 2011, however, global HNWI investable wealth contracted to US\$42.0 trillion amid high volatility in global markets and challenging macroeconomic conditions.

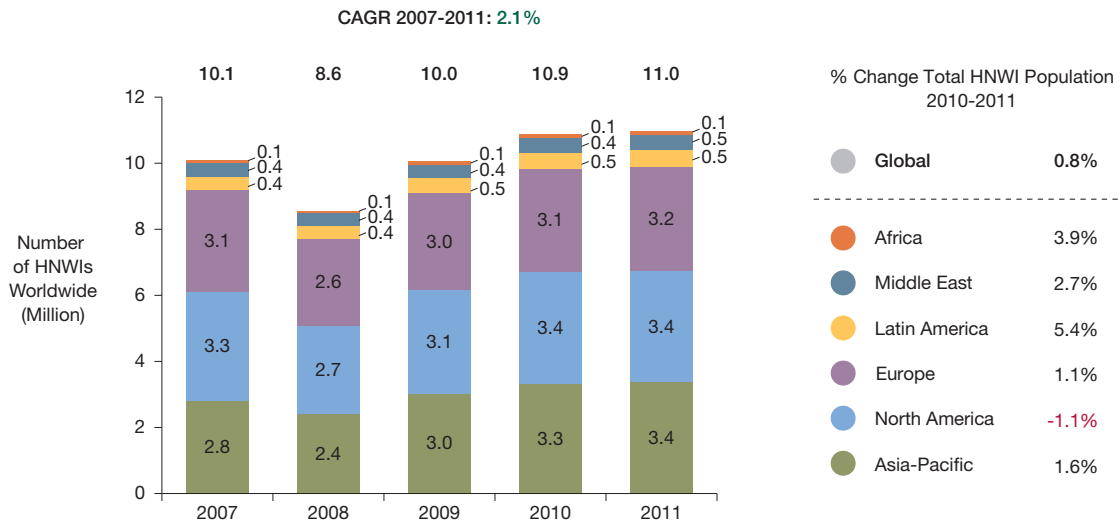
The number of HNWIs in Asia-Pacific rose 1.6% to 3.37 million individuals in 2011, surpassing North America for the first time. However, North America's 3.35 million HNWIs still accounted for the largest regional share of HNWI investable wealth—at US\$11.4 trillion—though that was down 2.3% from 2010.

The investable wealth of Asia-Pacific HNWIs also declined, but by a lesser amount (1.1%) to total US\$10.7 trillion. The number of HNWIs in Europe rose by 1.1% to 3.17 million, due to the growing number of HNWIs in key markets such as Russia, the Netherlands, and Switzerland. However, the aggregate wealth of European HNWIs declined 1.1% to US\$10.1 trillion, as Eurozone jitters made HNWIs there more cautious and risk-averse in their investing strategies. In the Middle East, the size of the HNWI population rose 2.7% to 0.45 million, and wealth edged up 0.7% to US\$1.7 trillion.

² HNWIs are defined as those with US\$1 million or more at their disposal for investing, but for the purposes of our analysis, we also separate HNWIs into three discrete wealth bands: those with US\$1 million to US\$5 million in investable assets (so-called "millionaires next door"); those with US\$5 million to US\$30 million (so-called "mid-tier millionaires") and those with US\$30 million or more ("Ultra-HNWIs")

FIGURE 1. HNWI Population, 2007 – 2011 (by Region)

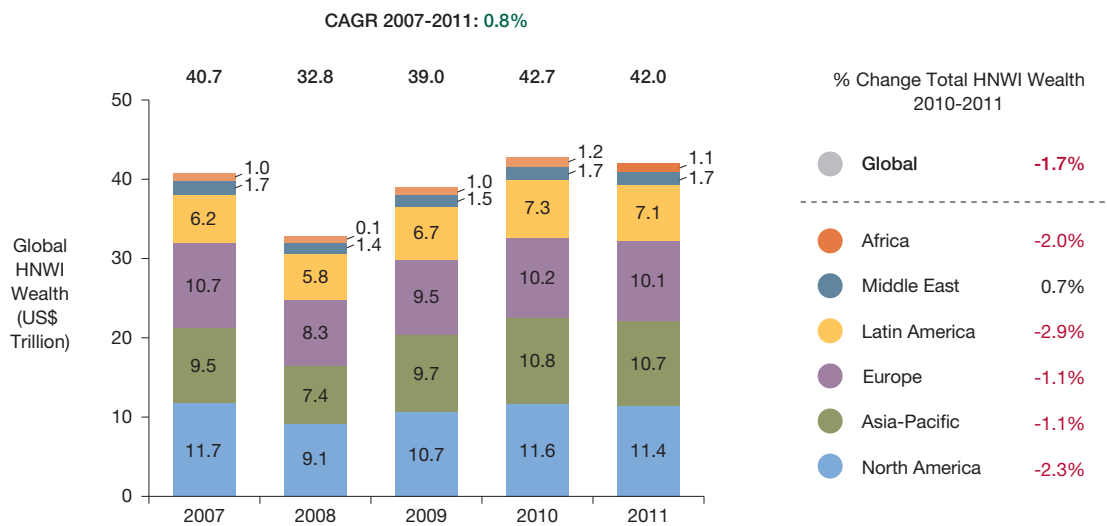
(Million)



Note: Chart numbers and quoted percentages may not add up due to rounding
 Source: Capgemini Lorenz Curve Analysis, 2012

FIGURE 2. HNWI Wealth Distribution, 2007 – 2011 (by Region)

(US\$ Trillion)



Note: Chart numbers and quoted percentages may not add up due to rounding
 Source: Capgemini Lorenz Curve Analysis, 2012

The U.S., Japan, and Germany together accounted for 53.3% of the world's HNWI population in 2011 (see Figure 3), up slightly from 53.1% in 2010. However, the share held by those three has been eroding very gradually (it was 54.7% in 2006) as the HNWI populations of emerging and developing markets, especially those in Asia-Pacific, continue to grow faster than those of developed markets.

In 2011, losses in key Asia-Pacific markets such as Hong Kong and India restrained the pace of growth in that region's HNWI population growth, but the world's HNWI population is still likely to continue fragmenting across the globe over time. In 2011, though, there was little change in that global distribution, except that India dropped out of the Top 12 and was replaced by South Korea. Indian equity-market capitalization dropped 33.4% in 2011, after a gain of 24.9% in 2010. That decline, and domestic factors such as increasing budget/fiscal deficit, contributed to a significant drop in India's HNWI population.

Aggregate Decline in Investable HNWI Wealth in 2011 Reflected Losses among the Higher Wealth Bands

The aggregate decline in investable HNWI wealth in 2011, despite the growing number of HNWIs, reflected the disproportionate impact of performance in the upper wealth bands, which experienced larger-than-average losses in both numbers and wealth.

The global population of Ultra-HNWIs declined 2.5% to 100k in 2011, and their wealth declined by 4.9%, after gaining 11.5% in 2010. The number of mid-tier millionaires declined 1.0% to 970k, and their wealth by 1.2%. These two segments account for just 9.7% of the global HNWI population, but 56.9% of its investable wealth. Investors in these upper wealth bands are more likely to have committed at least some of their investments to higher-risk and/or less-liquid assets such as hedge funds, private equity, or commercial real estate. There is potential for greater returns in such assets, but they can also be hard to divest at a palatable price in a viable time frame, so many such investments remained in UHNW portfolios, losing value quickly in the type of volatile markets seen in 2011.

In Latin America, this UHNWI effect had an even greater impact, because ultra-wealthy individuals actually dominate the small HNWI population, numbering just 500k in that region. The Latin American HNWI segment had proved quite resilient at the height of the crisis (the number of HNWIs shrank just 0.7% in 2008 versus a global drop of 14.9%) and the HNWI population has grown modestly since, gaining 8.3%, 6.2%, and 5.4% in 2008, 2009, and 2010.

But in the case of Latin America, a considerable amount of HNWI wealth stems from domestic business holdings, rooted in the region's natural resources. As a result, while HNWI investable wealth declined in 2008 at the height of the crisis, it then rose from US\$5.8 trillion at the end of 2008 to US\$7.3 trillion by the end of 2010, amid strong demand for agricultural products and metals, especially from fast-developing nations such as China and India. In 2011, when demand for many raw materials faltered, it helped to undermine Latin American HNWI wealth, which declined 2.9% to US\$7.1 trillion.

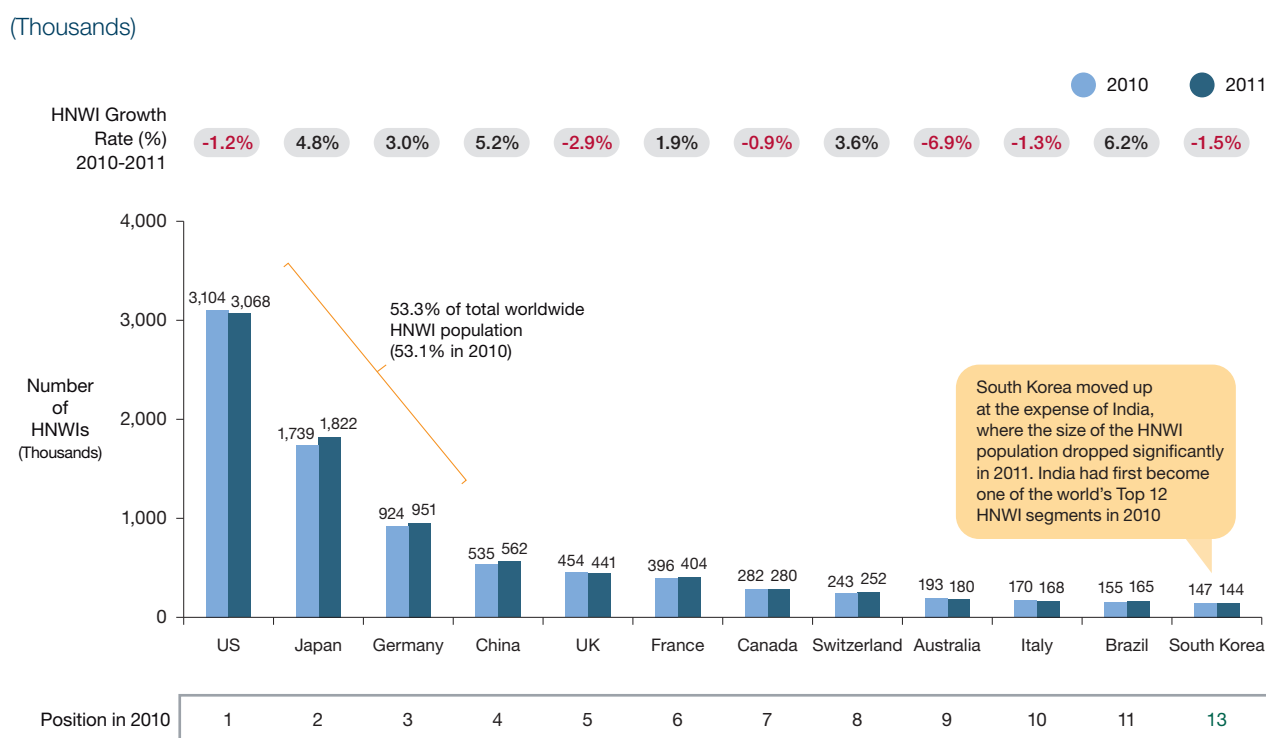
Various Pockets of Growth Emerged in HNWI Ranks beyond Asia-Pacific

Still, some of Latin America bucked the downward trend in 2011. For example, the HNWI population grew 6.2% in Brazil, where gross national income (GNI), national savings, real estate, and other metrics were all positive. And there were several other notable examples in 2011 of HNWI population growth—even beyond Asia-Pacific excluding Japan, which has in recent years been responsible for the greatest year-on-year additions to global HNWI ranks.

Ireland saw a 16.8% rise in its HNWI population as the country's economy showed renewed signs of growth after proactive austerity measures by the government. Equity-market capitalization also surged there, by about 80%, following steep crisis-related losses in prior years.

Thailand was one of the Asia-Pacific countries in which the HNWI population grew in 2011 (by 12.8%) on significant gains in real estate, a solid GNI performance, and only a 3.3% decline in equity-market capitalization (far less than many markets in the world).

FIGURE 3. Largest HNWI Populations, 2011 (by Country)



Note: Percentage growth rates will not match column totals due to rounding
 Source: Capgemini Lorenz Curve Analysis, 2012

Hong Kong and India Featured among the Countries Losing the Most HNWIs in 2011

While many countries witnessed a decline in their HNWI ranks in 2011, India and Hong Kong were the worst hit. India suffered a slump in its equity-market capitalization and its currency in 2011 as a lack of faith in the political process and the slow pace of domestic reforms disappointed investors. The sharp decline in these asset values helped to reduce the size of the country's HNWI population by 18.0%. In Hong Kong, stock-market capitalization also dropped—by 16.7% in 2011 after a gain of 17.6% in 2010—as Eurozone

concerns weighed on the outlook for growth. In the process, the country's HNWI population shrank by 17.4%.

Also hard hit in 2011 were the HNWI populations of Singapore and Poland, which both suffered the direct effects of the Eurozone crisis. Singapore saw a drop in exports, and Poland in foreign investment, and both lost equity-market capitalization. In the process, the number of HNWIs declined 7.8% in Singapore and 7.3% in Poland.

Drivers of Wealth: Investors Focused on Safety in 2011 As Economic Uncertainty Weighed on Sentiment

The road to a global economic recovery proved to be bumpy in 2011, and while many investors had expected it, the impact on investor sentiment was palpable. Economic uncertainty directly increased market volatility, and HNW and other investors adjusted their portfolios to protect capital. As a result, fixed income was the best-performing asset class in 2011, with the price of long-term U.S. Treasuries reaching historic highs, while many equities and commodities ended lower.

Among the key developments in the global economic and investment landscape in 2011:

- **The Eurozone debt crisis was the single largest concern for investors**, but there were plenty of other events around the world to undermine sentiment. The U.S. saw an historic downgrade of its sovereign-debt rating; the Middle East experienced continued civil unrest and regime change, which kept oil prices elevated throughout the year; Asia-Pacific suffered the effects of rising inflation, declining exports, and natural disasters. Many countries around the world also have faced political dysfunction, and unusual market volatility ensued across markets, leaving investors to stretch for yields.
- **Global gross domestic product (GDP) grew at an annual real rate of 2.7%, a slower pace than the 4.1% rate registered in 2010.**³ This was largely due to weaker demand from Western Europe, as well as a spike in oil prices, the Japanese earthquake, and political dysfunction across the globe. Real GDP growth slowed to 6.5% in Asia-Pacific excluding Japan from 8.3% in 2010, to 1.8% from 3.0% in North America, and to 1.7% from 2.2% in Western Europe. Still, the vast majority of individual economies expanded in 2011, and the developing economies of Sub-Saharan Africa and Eastern Europe grew well, 4.5% and 3.8% respectively, to extend substantial gains posted in 2010.
- **Global equity market capitalization slid 18.7%** as many of the world's equity markets ceded gains made in 2010. U.S. Treasuries rallied, with the Dow Jones CBOT Treasury Index rising 12.2%, amid robust demand from risk-shy investors. Gold, long sought as a safe haven, showed another gain for the year, but other tangible assets such as real estate saw weaker demand and lower prices.

Looking ahead, global GDP growth is expected to further slow to 2.2% in 2012 as spillover effects from the Eurozone crisis continue to dampen growth rates, and as fiscal drags mount. By 2013, however, more policy initiatives are likely to have materialized to control debt contagion and spur growth, helping push world GDP expansion up to a forecast 2.9%, and sending growth in China and India back up to a forecast 8.5% and 8.0%, respectively. The political environment is also likely to have a tangible impact on global economies in 2012, with contests for political leadership in many nations—most notably in China, Russia, France, and the U.S., which collectively account for around 40% of world GDP.

HNW investors, meanwhile, need to prepare themselves for ongoing market volatility, and the possibility of extended periods of bimodal investment outcomes, with returns likely to be extremely positive or extremely negative rather than normally distributed.

EVENTS AROUND THE GLOBE UNSETTLED ECONOMIES AND MARKETS IN 2011

As many had expected, the post-crisis road to global economic recovery was a bumpy one in 2011, made worse by the fact that different types of economic and political hotspots continued to flare in many areas of the world (see Figure 4). Uncertainty prevailed as to when the worst would be over, and how investors could safely position themselves in the meantime.

³ Unless otherwise specified, all macroeconomic data and projections are based on Economist Intelligence Unit Regional and Country Reports from March, April, and May 2012

The following were among the key regional developments that unsettled markets and investors in 2011:

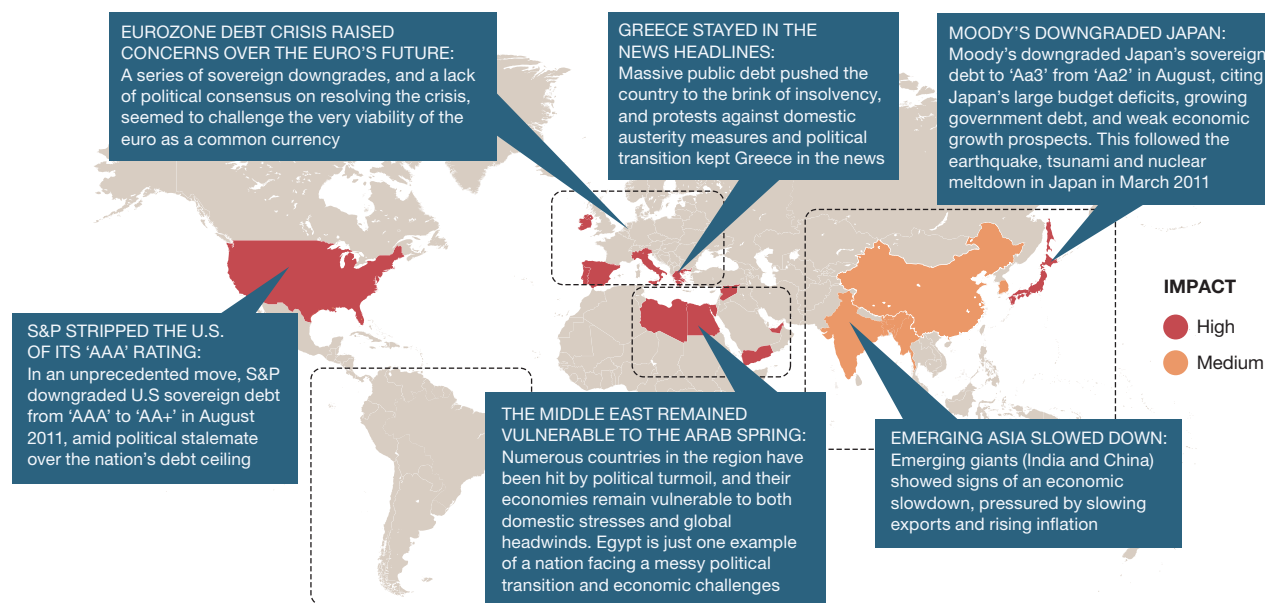
- In **Europe**, numerous sovereign-debt ratings were downgraded, and concerns grew over the very future of the Eurozone. Greece, for one, remained firmly in the headlines, as its failure to deal with massive public-debt levels pushed the country to the brink of insolvency, and civil protests flared against the country's domestic austerity measures.
- In **North America**, Standard & Poor's Corp. took the unprecedented step of stripping the U.S. of its 'AAA' sovereign debt rating, citing the political stalemate over the nation's debt ceiling.
- The **Middle East** remained vulnerable to protests and demonstrations after the so-called 'Arab Spring' unleashed a wave of revolution in December 2010 that has since wrought unrest and regime change across many Arab states. Geopolitical tension in the region has helped to keep oil prices high, despite the slowdown in global economic growth.

- **Asia-Pacific** nations were negatively impacted by the effects of rising inflation, declining exports, and catastrophic events, like Japan's massive earthquake. The key economies of China and India downshifted in their role as growth engines for the world economy.

These economic and political dynamics translated into high volatility in many markets, including equities, commodities, and currencies.

The flight to safety among investors also put a premium on dividend-yielding blue-chip stocks, which significantly outperformed their riskier small-cap counterparts. European stock markets declined broadly, and highly liquid Asia-Pacific markets, such as South Korea and Singapore, proved susceptible to outflows of "hot" money seeking short-term returns. Even the stock markets of major Latin American economies, where macroeconomic fundamentals remained strong, could not buck the global decline.

FIGURE 4. Major Events That Unsettled Markets in 2011 and Q1 2012



Source: Capgemini Analysis, 2012

These widespread losses in equities proved to be a stark contrast to 2010, when many stock markets had rallied. At that time, equities had seemed to be an attractive investment option while crisis-related turmoil was subsiding and the Eurozone debt crisis had yet to fully flare. In 2011, however, it became clear that few equity markets could escape the fallout as the Eurozone effects radiated across the globe. In fact, 2011 was arguably the year that disproved any notion that emerging markets had become self-sufficient enough to somehow decouple themselves from whatever economic and financial woes might beleaguer the world's largest developed economies.

EUROZONE DEBT CRISIS HAD FAR-REACHING EFFECTS IN 2011

While there was no shortage of global hotspots in 2011, it was the Eurozone crisis—or, rather, the seeming lack of consensus on how to resolve that crisis—that proved to be the single most unsettling force for the global economy.

The major focus has centered on the demise of the so-called “PIIGS” (Portugal, Ireland, Italy, Greece, and Spain), which are juggling especially high levels of public debt along with hefty budget deficits (see Figure 5). But these countries are certainly not alone in their economic dilemma, and investors have feared that their predicament is just the tip of the iceberg for the Eurozone and beyond.

The EU invoked a bailout facility (European Financial Stabilization Mechanism) that provided relatively prompt relief to Greece, Ireland, and Portugal between late-2010 and mid-2011. But Greece needed a second round of funding in 2011, and Eurozone leaders insisted that Greece first negotiate a write-down of its privately held debt. Those negotiations took months, before a deal was finally reached in February 2012, allowing Greece a 53.5% debt write-off from private debt-holders.

Still, even if those write-offs are executed in totality, and the second bailout proceeds as planned, Greece must still find a way to cover its remaining debts. Despite reams of austerity measures taken so far, the Greek government still spends far more than it receives in taxes, so must enforce even more tax hikes and spending cuts to try to cover its budgetary shortfall—potentially worsening its existing recession.

Investors fear dynamics such as these across several vulnerable Eurozone countries have the potential to turn the sovereign-debt crisis into another full-blown economic and banking crisis. There are already signs that the region's banks have reduced loans to businesses and consumers while they shore up their capital to guard

against sovereign-debt exposure. Such action has prompted the European Central Bank (ECB) to provide liquidity at low interest rates in hopes of avoiding a resultant credit crunch.

Some observers even fear the Eurozone itself could disintegrate as its member governments continue to haggle over how best to restore fiscal balance to the region, limit the possibility of debt contagion, and protect the health of the European banking system. The collapse of the Eurozone seems unlikely given the significant political will that has been required to establish and expand this unified economic area, but it is not entirely inconceivable, and the uncertainty has unnerved investors.

The Eurozone is already littered with political casualties of the crisis, and by March 2012, the economic spotlight was turning to Spain, which has said it will miss its budget targets for the second half of 2012. Its austerity to date has already spurred a recession given the region's extensive decline in domestic demand and the related drop in Spain's exports.

These are the types of developments investors will continue to watch closely in 2012 as they search for signs of systemic stress in the Eurozone. To date, EU governments and regulators have made tangible progress in recapitalizing the region's banks, but investors will remain nervous until there is substantial progress in achieving greater budget discipline, economic growth, and a deeper fiscal union in the Eurozone as a whole.

WORLD GDP GROWTH SLOWED IN 2011 AS THE EUROZONE CRISIS TOOK ITS TOLL

The world economy grew at an annual real rate of 2.7% in 2011, a slower pace than the 4.1% rate registered in 2010⁴, mostly due to weaker demand from Western Europe, the natural disasters in Japan, high oil prices, and elevated risk aversion. Weaker demand from developed nations translated into slower growth in certain export-driven emerging economies in Asia-Pacific and Latin America (see Figure 6), though the developing economies of Africa and Eastern Europe performed well.

Overall, Asia-Pacific excluding Japan led global economic growth as expected, with real GDP expanding 6.5%—though that was down from growth of 8.3% in 2010. Regional powerhouses India and China both experienced a slowdown, partly due to the effects of persistent domestic inflationary pressures, and in China's case to the tempering of prior credit excesses.

⁴ Unless otherwise specified, all macroeconomic data and projections are based on Economist Intelligence Unit Regional and Country Reports from March, April, and May 2012

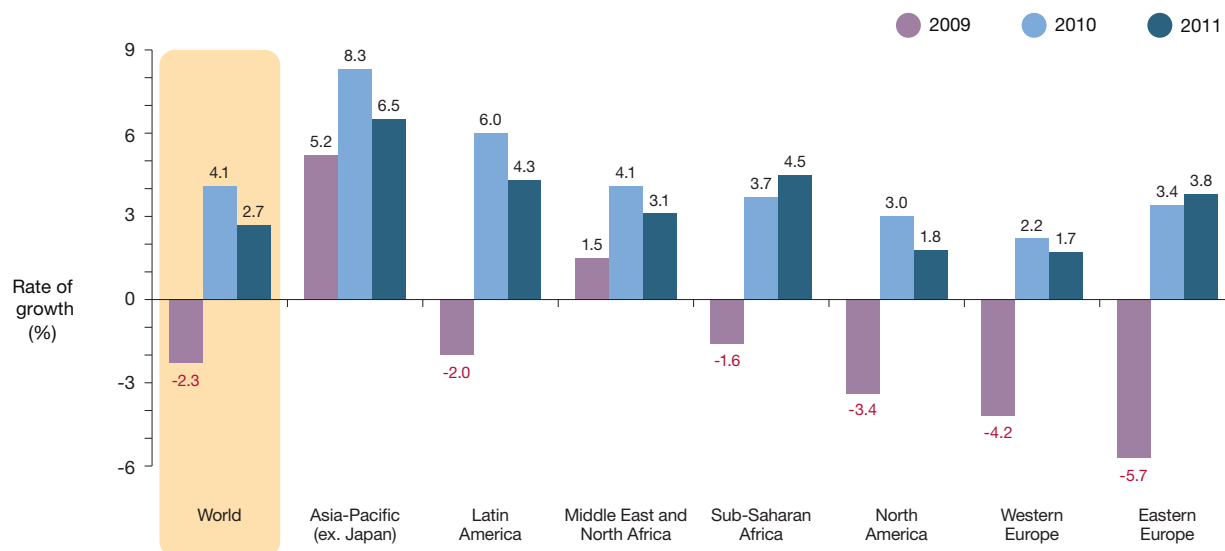
FIGURE 5. Total Public Debt and Budget Balance As a Percentage of GDP, Select Countries, 2011

| Americas | Public Debt/GDP | Budget Balance/GDP | Europe | Public Debt/GDP | Budget Balance/GDP | Rest of the World | Public Debt/GDP | Budget Balance/GDP |
|-----------|-----------------|--------------------|-------------|-----------------|--------------------|-------------------|-----------------|--------------------|
| U.S. | 98.5% | -9.6% | Portugal | 106.8% | -4.0% | Japan | 229.8% | -10.1% |
| Canada | 85.0% | -4.5% | Ireland | 105.0% | -9.9% | Singapore | 100.8% | 7.3% |
| Brazil | 66.2% | -2.6% | Italy | 120.1% | -3.9% | India | 68.1% | -8.7% |
| Argentina | 44.2% | -3.3% | Greece | 160.8% | -9.2% | Thailand | 41.7% | -1.9% |
| Mexico | 43.8% | -3.4% | Spain | 68.5% | -8.5% | New Zealand | 37.0% | -6.5% |
| Columbia | 34.7% | -2.1% | Belgium | 98.5% | -4.2% | South Korea | 34.1% | 2.3% |
| Peru | 21.6% | 1.9% | France | 86.3% | -5.3% | China | 25.8% | -1.2% |
| Chile | 9.9% | 1.2% | Germany | 81.5% | -1.0% | Indonesia | 25.0% | -1.6% |
| | | | U.K. | 75.1% | -8.7% | Australia | 22.9% | -4.3% |
| | | | Switzerland | 48.6% | 0.4% | Saudi Arabia | 7.5% | 15.2% |

Note: Public debt constitutes total domestic, external, and IMF debt owned by the central government of a country as per IMF tallies; Budget balance represents general government receipts minus general government outlays, with positive figures denoting budget surplus and negative denoting budget deficit
Source: Capgemini Analysis, 2012; International Monetary Fund (IMF), May 2012

FIGURE 6. Real GDP Growth Rates, World and Select Regions, 2009 – 2011

(%)



Note: Aggregate real GDP growth rates are based on GDP weights calculated by the Economist Intelligence Unit
Source: Capgemini Analysis, 2012, Economist Intelligence Unit, March 2012

Few economies actually contracted in 2011, but Japan's GDP shrank by 0.4% as the country dealt with the after-effects of the massive earthquake and tsunami that ravaged the country's northeastern coast in March 2011, killing nearly 20,000 people, and causing a critical leak of nuclear radiation. In August 2011, Moody's Investor Services downgraded the nation's sovereign rating to 'Aa3,' saying Japan would find it difficult to reduce its huge debt, given the disaster and the prospects for weak economic growth.

The rate of growth also fell dramatically in Singapore as manufacturing demand from Europe dropped, and the effects of floods in Thailand disrupted the supply of components to Singapore's manufacturing plants. Still, the slowdown put Singapore's GDP growth at a much more sustainable level of 4.8% in 2011, compared to a surging rate of 14.5% in 2010 (which had followed a significant GDP contraction in 2009).

National Savings Increased in Proportion to World GDP As Developed Economies Saved More

In 2011, national savings⁵ increased in many regions, and edged up to 22.7% globally from 22.2% in 2010, suggesting more money was available for investing. The rate continues to be highest in Asia-Pacific excluding Japan (34.1%) given the traditional focus on prudent savings there, and lowest in North America (11.2%).

National savings as a percentage of GDP increased in all G7 economies except Japan in 2011, suggesting global imbalances could be marginally lower in 2012 and 2013 as these major economies are saving more. However, household savings declined in many developed economies, including the U.S. and U.K., due to ongoing macroeconomic problems such as high unemployment and weak economic growth. Household savings rose in Japan (to 7.3% of disposable household income from 6.2% in 2010), because private consumption fell sharply after the earthquake.

National savings as a percentage of GDP decreased in some key emerging markets, including Brazil and South Africa where significant local currency depreciation tangibly reduced purchasing power. As a result, national savings declined slightly in both the Latin America and Sub-Saharan Africa regions. National savings also declined in Russia (to 24.7% of GDP in 2011 from 25.4% in 2010), due to renewed expansion of consumer credit, which boosted private consumption.

Globally, Private and Government Consumption Both Rose Slightly

Global public spending edged up 1.1% in 2011, primarily driven by government expenditure in areas like infrastructure development in emerging nations. Mature economies still account for the largest outright share of total spending by governments globally (US\$3.2 trillion in Western Europe and US\$2.9 trillion in North America in 2011). However, aggregate public spending is not increasing in developed economies, because few can afford to increase further their already massive sovereign-debt levels. The emerging economies of Asia-Pacific and Latin America continued to increase public spending modestly in 2011 to support their economies in the currently challenging global economic environment.

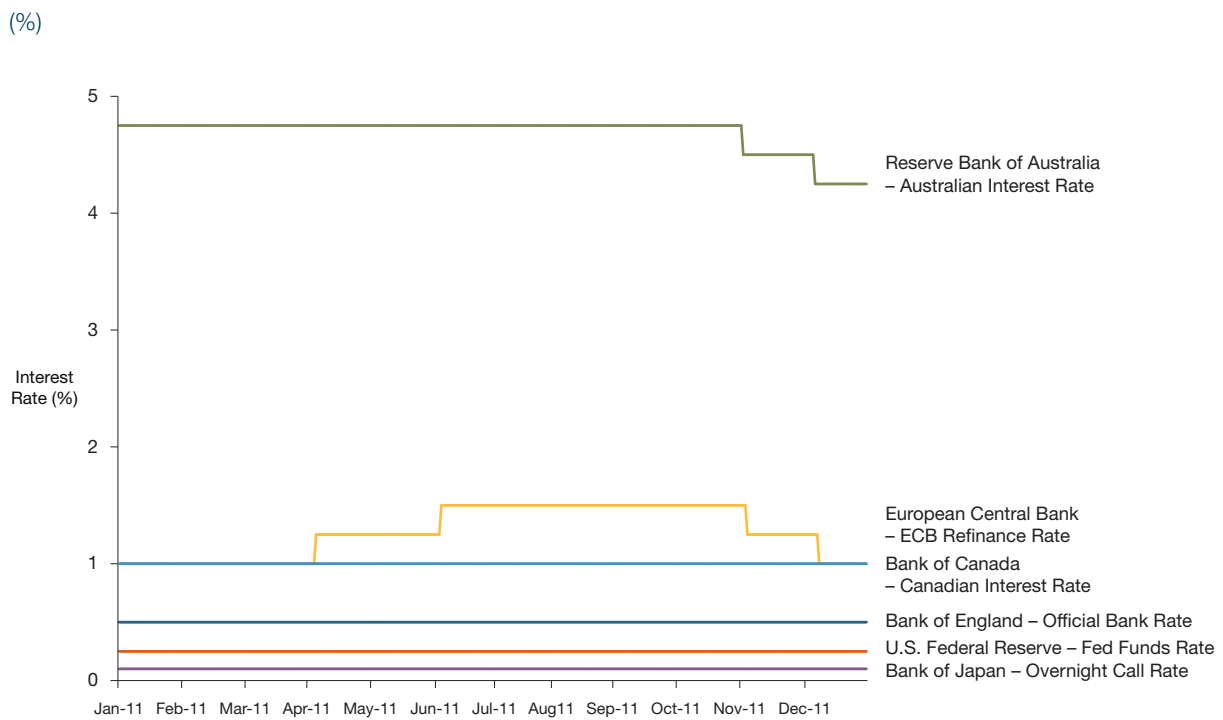
Global real private consumption also rose 2.3% in 2011, to US\$30.7 trillion from US\$30.0 trillion in 2010, largely because personal spending rose in many emerging economies, despite the threat to global economic growth from the Eurozone debt crisis. Asia-Pacific excluding Japan again saw the strongest gain in personal consumption, but the 6.1% increase in 2011 was not much higher than the 5.1% gain in Latin America. Consumer spending in Latin America has been rising steadily, and will probably continue to do so, as the region's expanding middle class remains eager to spend its growing wealth. However, Latin America still has a far smaller outright level of personal consumption than Asia-Pacific excluding Japan (US\$2.2 trillion vs. US\$4.6 trillion, respectively, in 2011).

U.S. real personal consumption also rose and showed an annual increase of 2.2% for 2011, after a gain of 2.0% in 2010. However, the growth in real personal spending is expected to slow to 1.3% in 2012 as the economy recovers only slowly, and unemployment remains high.

The level of real private consumption in Western Europe was unchanged in 2011, at US\$8.6 trillion, and personal spending is expected to decelerate to 0.5% in 2012 after consumer confidence dropped sharply in the second half of 2011, as the region continued to battle the effects of the Eurozone crisis.

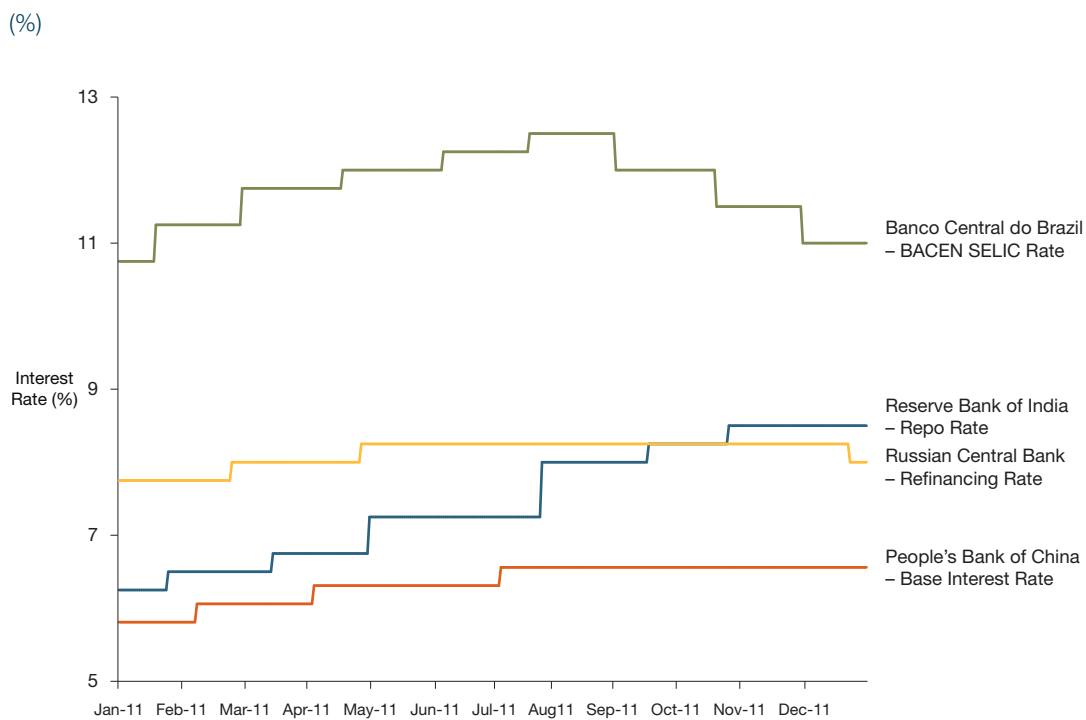
⁵ National savings is equal to real GDP minus the combined total of real public and private consumption

FIGURE 7. Key Global Interest Rates, Select Developed Economies, 2011



Source: Capgemini Analysis, 2012; <http://www.global-rates.com/interest-rates/central-banks/central-banks.aspx>, accessed January 4, 2012

FIGURE 8. Key Global Interest Rates, Select Emerging Economies, 2011



Source: Capgemini Analysis, 2012; <http://www.global-rates.com/interest-rates/central-banks/central-banks.aspx>, accessed January 4, 2012

Slow Economic Growth Kept Interest Rates Low in Many Developed Economies

Central banks kept interest rates low in many countries in 2011, and especially in developed nations facing weak growth rates (see Figure 7). India and China raised benchmark interest rates, however, to combat inflationary pressures in their domestic economies (see Figure 8).

GLOBAL JITTERS IN 2011 UNDERMINED MANY OF THE KEY ASSET CLASSES THAT DRIVE WEALTH

Uncertainty dominated investor psychology in 2011, so many investors stuck to safe-haven assets to protect capital. The best-performing asset class was fixed income, while commodities broadly underperformed, and many tangible investments lost value, including real estate and silver. Many equity markets also declined, after a rebound in 2010. Signs of recovery were seen in Q1 2012 when investors demonstrated stronger risk appetites, and concerns about the Eurozone subsided somewhat. The outlook for equity markets remains cautiously optimistic overall for 2012, and especially for Latin America and Asia-Pacific.

Global Equity Market Capitalization Dropped in 2011, Ceding Ground Made Up in 2010

Global equity market capitalization ended the year at US\$43.1 trillion, down 18.7% from US\$53.0 trillion a year earlier, and well below the high of US\$61.5 trillion seen in 2007 before the global economic and financial crisis (see Figure 9).⁶

Around the world, equity-market prices ceded many of the gains made in 2010 as the Eurozone sovereign-debt crisis persisted and fears of contagion grew, prompting widespread market corrections. Volatility in global equities also spiked, and hit 1.6 in November 2011. That level was far below the highs seen at the height of the financial crisis, but was beyond levels seen during other market crashes, including those tied to the Russian financial crisis in 2008 and the bursting of the dotcom bubble in 2001 (see Figure 10).

Europe experienced double-digit declines in many benchmark equity indices in 2011 with investors shifting to safer holdings as the sovereign debt crisis raised fears about growth prospects and even the viability of the common currency. In Italy, where the ratio of government debt to GDP was more than 118%, the MSCI Italy index fell 26.4%. The specter of a sovereign default by Greece

drove the MSCI Greece index down by 63.7%, while worries about the exposure of French banks to the troubled Eurozone nations, and the ability of the French government to retain its 'AAA' credit rating, drove the MSCI France Index down 20.9%. The adverse sovereign-debt situation even had a bearing on investor sentiment in fundamentally strong nations such as Germany, and the MSCI Germany Index fell by 20.7% in 2011. As Q1 2012 proceeded, however, the intensity of a European crisis abated enough to reduce funding costs, taking some of the pressure off banks. The focus by Italy's technocratic government on promoting economic reforms, the ECB's 3-year liquidity offerings, and Greece's success in obtaining a second bailout and debt write-down all helped to allay pessimism, but concerns are likely to persist—and flare at times—as Europe continues to battle the effects of fiscal retrenchment on growth.

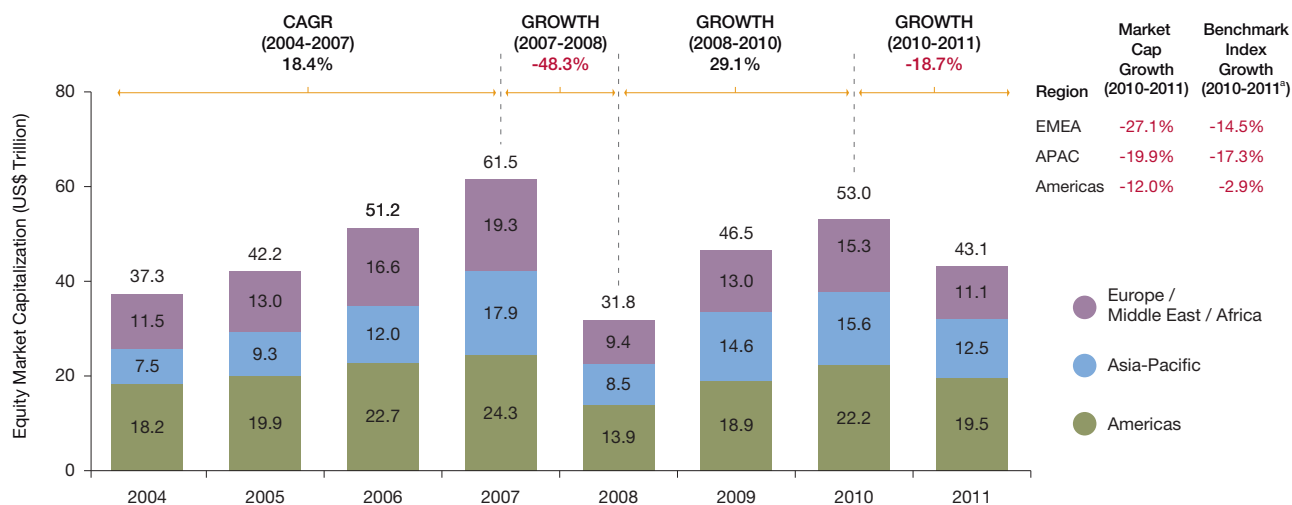
U.S. equities performed quite well in early-2011, amid signs of recovery in the U.S. economy and in corporate profits and cash balances. Investors were also cheered that U.S. firms were relatively unscathed by the global supply-chain crunch induced by the Japanese earthquake, and the impact of increased oil prices due to civil unrest in the Middle East and North Africa. By May, however, the market was deteriorating as the European debt crisis dragged on, and uncertainty persisted over the U.S. debt ceiling. U.S. equities took another hit after S&P downgraded U.S. sovereign debt in August. For the year, investors remained risk-averse overall, and favored dividend-paying companies and multinational blue chips. As a result, the Dow Jones Industrial Average gained 4.7% in 2011, roundly outperforming the Russell 2000 index of small-cap stocks, which fell 7.2%. Going forward, the outlook for the U.S. equities market remains cautiously optimistic, with the housing and employment pictures beginning to improve, and signs the U.S. will escape a double-dip recession.

Asian equity markets tumbled, dashing widespread hopes that the emerging markets could somehow decouple themselves from weakness in developed economies. The MSCI China Index, which tracks the Chinese equity market, dropped 19.7% in 2011 as fears grew that Asia's export-driven markets would suffer the effects of declining consumer demand from the U.S. and Europe, and China's restrictive monetary policy would choke growth. Concerns about an economic slowdown subsided considerably, however, after Chinese policymakers exploited a period of falling inflation to deliver monetary stimulus to the local housing and debt markets. The MSCI India index was the worst-

⁶ Capgemini analysis

FIGURE 9. Equity Market Capitalization, 2004 – 2011 (by Region)

(US\$ Trillion)

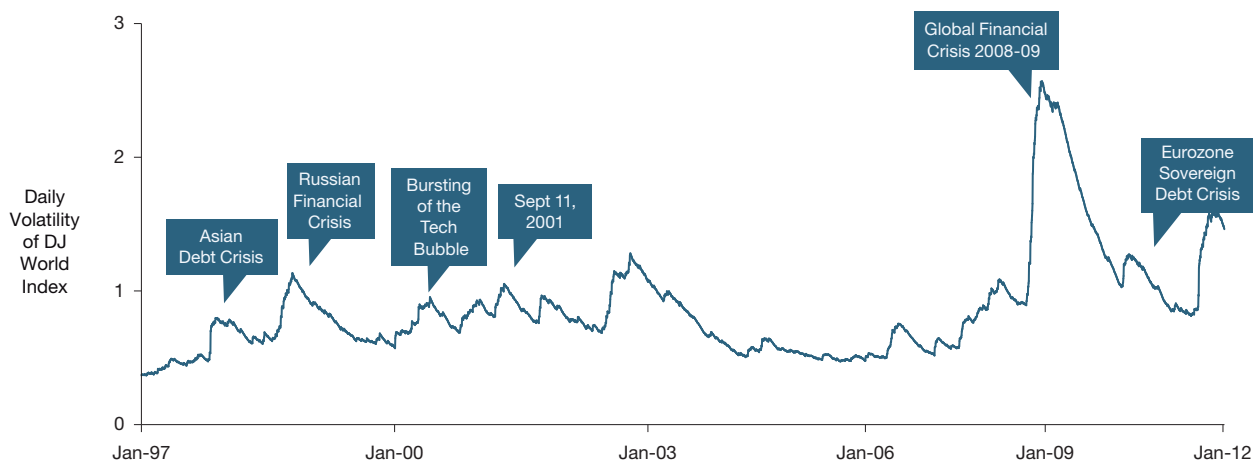


* Benchmark indices are MSCI AC Americas, MSCI AC Asia Pacific, and MSCI AC Europe
 Source: Capgemini Analysis, 2012; World Federation of Exchanges, January 2012

performing country index in Asia-Pacific in 2011, sliding 37.3% as myriad factors, including persistent inflation, rising debt levels, policy paralysis, and infrastructure bottlenecks shook investor confidence in the Indian growth story. Several of the region’s more liquid markets,

and especially those with high levels of foreign equity ownership, such as South Korea and Taiwan, also suffered outflows of “hot” money as investors sought to exploit or anticipate short-term profit opportunities and interest-rate/currency differentials by moving their money

FIGURE 10. Daily Volatility of Dow Jones World Index, January 1997 – January 2012



Source: Capgemini Analysis, 2012, Dow Jones World (W1) Index – Daily close values from January 1, 1997 to January 31, 2012

from one market to another. Worst hit by this phenomenon were the MSCI Taiwan index, which declined by 22.8% in 2011, and the MSCI Korea index, which declined by 12.8%.

Equity markets also tumbled in the **emerging economies of Latin America**, undermined by the developed-economy ailments that affected all equity markets. However, market performance in the region also remains highly dependent on local politico-economic dynamics. For example, in Brazil, investors remained concerned about the prospects of an overheating economy due to high spending by the government and high interest rates (the central bank raised interest rates to 12.5% in July 2011).

Still, the underlying macroeconomic performance of most Latin American economies remained strong as these countries profited from high prices for mineral and agricultural exports, which boosted their foreign currency reserves. Financial institutions also remained well-capitalized, thanks to conservative banking traditions. Nevertheless, since Latin American economies benefit from foreign capital inflows and elevated commodity prices, they are also vulnerable to the debt woes of Europe and to slowing growth in markets such as China. As a result, the MSCI EM Latin America indicative index dropped 21.6%. The outlook for 2012 is strong, though, with the Latin American equity markets expected to perform well.

Long-Term Bond Prices Rallied As Investors Shied from Risk

The Dow Jones CBOT Treasury Index rose by 12.2% in 2011, and the Dow Jones Corporate Bond Index rose by 3.3%, amid robust demand from risk-averse investors. Governments, financial institutions, and consumers have all been deleveraging since the financial crisis, and the drag on economic growth is palpable. At such times, bonds tend to perform better than other assets such as stocks, and that was certainly the case in 2011.

Long-term U.S. Treasuries generated a 29.9% return in 2011, including price gains and interest payments,⁷ vastly outperforming the 7.8% return on the Barclays Capital Aggregate Bond Index, a broad bond-market benchmark. Sovereign debt concerns in the Eurozone led to a flight to safety in favor of U.S. Treasuries in 2011, and since there was a lack of safe alternate investments, that strong demand endured even after S&P

downgraded U.S. debt. As a result, prices of U.S. Treasuries had risen significantly by the end of the year, resulting in lower yields.

In the Eurozone, yields on government debt remained elevated throughout the year, reflecting the heightened credit-default risk. By the end of 2011, Switzerland, Japan, and Germany were among the few nations in the world to have lower yields on their 10-year bonds than those on U.S. 10-years.

While there is always underlying demand for fixed income securities, the bull run in many government bonds cannot continue. Prices simply cannot go much higher with yields already so low—despite stimulative efforts by central bankers. Investors could find it difficult, then, to capture capital gains beyond inflation, except in certain strata of bonds, such as investment-grade corporate and high-yield offerings, which continue to provide strong opportunities for growth.

Real Estate Markets Fell As Demand Languished

The Dow Jones Select REIT Index fell 2.4% in 2011 as the slow pace of the global economic recovery, growing sovereign debt-concerns, weak consumer confidence, and high unemployment continued to weigh on the real estate market. The combination of low borrowing costs and lower home prices have boosted housing affordability, but in most developed economies, there is too little domestic demand to drive a sustained revival.

The hotel segment was the worst-performing category of real estate in 2011 (down 14.8%), but the industrial segment was also down 4.0%, and all types of real estate declined significantly during the third quarter after S&P downgraded U.S. debt, and Greece teetered on the edge of a sovereign-debt default.

The U.S. housing market continues to suffer the effects of tight credit conditions, buyer hesitation, and an overhang of inventory, but it was starting to show signs of life in early-2012, and could finally be bottoming out. Japan, hit by the earthquake in March, saw the yield on its real-estate market drop by an annualized 22.6% in 2011, leaving no end in sight to the country's two-decade-long property slump. Within Europe, the French and Swiss housing markets remained relatively resilient, with average inflation-adjusted home prices in Q3 2011 up 4.4% and 3.3%, respectively, from a year earlier. However, most other European markets remained mired in negative

⁷ Based on returns from the Barclays Capital Long-Term U.S. Treasury Index, which includes all publicly issued U.S. Treasury securities that have a remaining maturity of 10 or more years, are rated investment grade, and have US\$250 million or more of outstanding face value

territory. In Asia-Pacific, housing activity also downshifted; even in Australia, where house prices were quite resilient in 2010, average inflation-adjusted home prices were down 5.7% from a year earlier in Q3 2011. However, there were some notable exceptions to the bearishness in Asia-Pacific real estate, namely India, Singapore, and Thailand.

Robust Demand for Cash/Deposits Kept Yields Low

U.S. T-bill yields hit rock-bottom in 2011, with investors willing to accept negative real yields in return for safety. Yields on U.S. Treasuries with maturities of 5 years or less plunged below 1% in the second half of 2011, due in part to a pledge by the Federal Reserve to keep the short-term federal funds rate near zero until mid-2013. Demand remained strong even after S&P downgraded U.S. debt in August. If the economic situation in Europe does not improve significantly, yields could remain near Q4 2011 lows for some time.

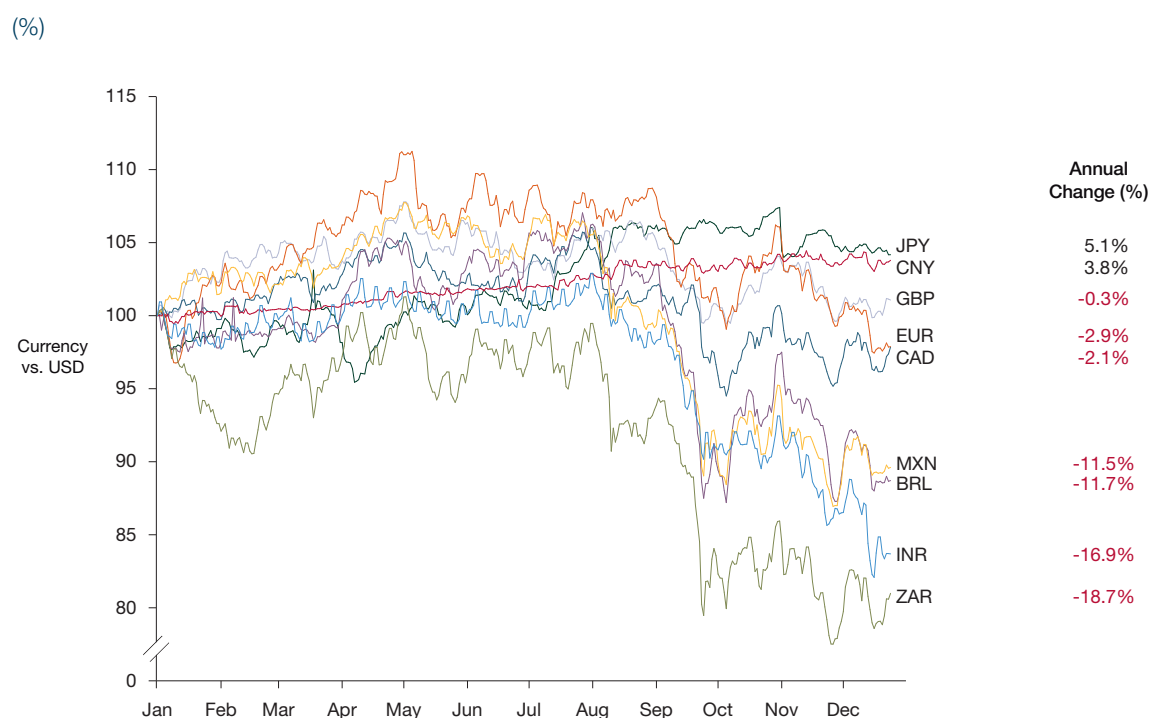
Performance of Other Investments Was Mixed

The global performance of other investments, such as currencies, commodities, and hedge funds, was mixed in 2011 amid the ebb and flow of macroeconomic trends and volatility.

Vacillations in currency markets were driven, for instance, by global economic developments and uncertainty, but emerging-market currencies depreciated significantly against the U.S. dollar, especially in the second half of the year. This largely reflected moves by banks and corporations based in developed economies to liquidate emerging-market assets to repatriate funds and bolster their balance sheets.

Among the hardest hit currencies were the South African rand and the Indian National rupee, which depreciated by 18.7% and 16.9%, respectively, against the U.S. dollar in 2011 (See Figure 11). Against most major developed-market currencies, the U.S. dollar finished within about 3% of where it started the year.

FIGURE 11. Change in Value of Select Currencies Against US Dollar, 2011



Note: (Re-based 1/1/2011 = 100); GBP: British Pound; ZAR: South African Rand; BRL: Brazilian Real; MXN: Mexican Peso; CAD: Canadian Dollar; EUR: Euro; CNY: Chinese Yuan; JPY: Japanese Yen; INR: Indian Rupee

Source: Capgemini Analysis, 2012; www.oanda.com, accessed January 6, 2012

Gold prices rose 10.1% in 2011, extending their bull run to 11 years amid safe-haven demand, triggered by turmoil in the Middle East and the ongoing European debt crisis. During the year, gold prices had spiked in August on S&P's unprecedented downgrade of U.S. debt, before correcting somewhat as the U.S. dollar rose and some leveraged investors liquidated gold assets to secure cash.

Among other commodities:

- Silver hit a new high (of US\$48.3 per ounce) in April 2011, extending strong gains made in 2010, but corrected over the rest of the year to post a decline of 10% for the year as a whole. Speculative traders and individual retail investors were key drivers behind both the rise and fall of silver during the year.
- Signs of a global economic slowdown reduced demand and prices for natural gas, but geopolitical tensions in the Middle East led to a rise in oil prices. Crude prices may rise further in 2012, as Mideast tensions remain, including the standoff surrounding Iran's nuclear ambitions, and persistent turmoil in Syria. US oil production has been rising steadily as prices have risen, however, and that increased output could alleviate a little of the upward price pressure.
- Prices of agricultural commodities such as corn and wheat began the year on a strong note after rising significantly in 2010 on expectations of shortages. Corn prices continued to soar during 2011 due to a combination of poor weather affecting U.S. output, rising Chinese demand, and demand from ethanol producers. Wheat prices ultimately declined, however, due to bumper harvests.

On the whole, commodity prices are expected to follow global cues and may decline in the short-term, especially if the slowdown in China's economy is sustained.

Hedge funds turned in a negative performance in 2011, after two consecutive years of positive growth. On average, hedge funds lost 5.0% in value in 2011,⁸ mostly due to the market volatility that was largely precipitated by the European debt crisis. Global hedge-fund industry assets topped US\$2 trillion for the first time at the end of Q2 2011⁹, surpassing the pre-crisis peak hit in early-2008, before turning lower for the remainder of the year.

On the back of lackluster economic fundamentals, especially in the Eurozone, the Dow Jones Credit Suisse Hedge Fund Index fell 2.5% for the year, and more than 75% of emerging markets funds posted losses, most markedly those focused on India. At the same time, directional funds were unable to either benefit from upside momentum or control losses during downward market trends. Hedge funds of funds, the notable exception, performed decently in 2011, and the outlook for such funds in 2012 remains fairly optimistic.

OUTLOOK: UNCERTAINTY IS LIKELY TO PLAGUE GLOBAL MARKETS AND ECONOMIES FOR THE NEAR-TERM

Global GDP expansion is expected to slow to 2.2% in 2012 (see Figure 12) as spillover effects from the Eurozone crisis continue to dampen growth rates, including those in emerging markets, where exports have been lower due to weak demand from Europe. Global GDP growth is expected to rebound to 2.9% in 2013, as more policy initiatives materialize to control debt contagion and spur growth. If there is a risk to this, however, it is from persistent fiscal drags and ongoing deleveraging.

In fact, uncertainty will still be a hallmark of economic and market conditions in the year or so ahead, and the Eurozone remains a critical challenge to the world economy. Investors want to see the Eurozone plot a viable route to deficit-reduction, but also want assurance that austerity measures will not stifle growth, especially since demand from Europe remains critical to the expansion of export-driven emerging economies such as Brazil and China. Even if the Eurozone situation stabilizes, the ability of individual economies to rebound and grow will depend heavily on the extent to which governments manage the confluence of challenges they face—including the inflation threat in some faster-growing emerging markets and the crippling deficits in many of the world's developed economies.

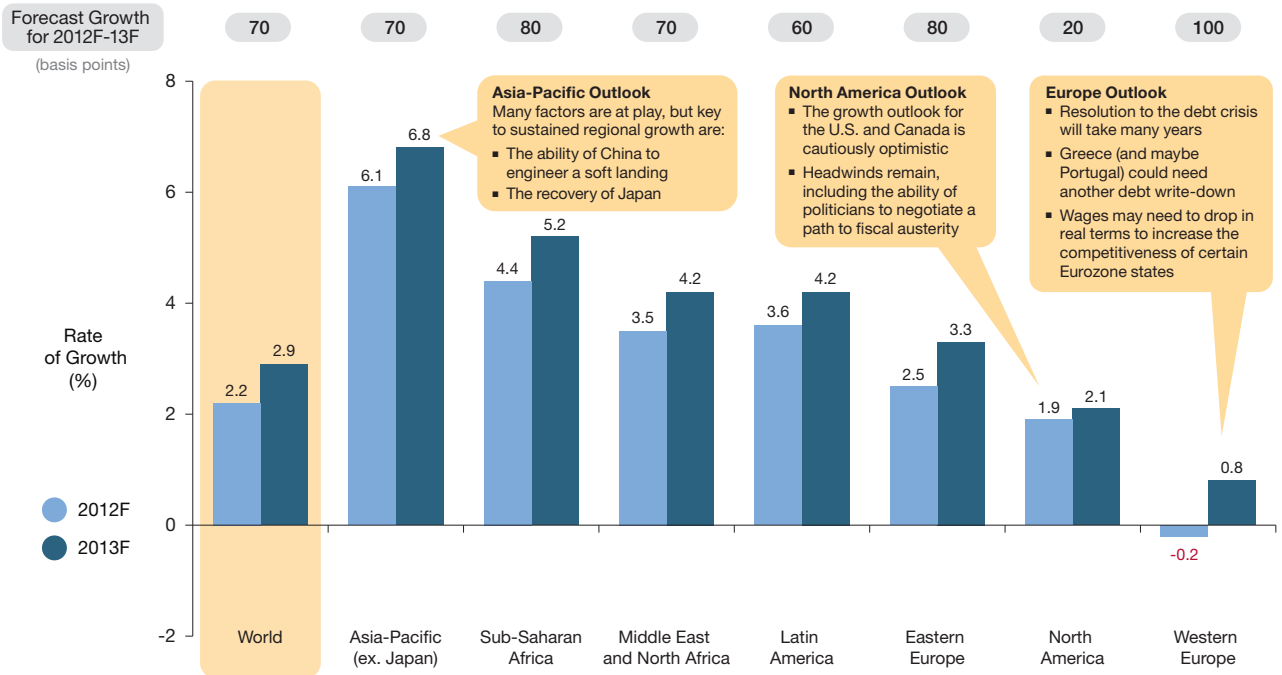
Politics is also likely to have a tangible impact on global economies in 2012. Many nations have undergone or will undergo a contest for their political leadership in 2012 (see Figure 13)—most notably China, Russia, France, and the U.S, which collectively account for around 40% of world GDP.

⁸ As measured by the Hedge Fund Research Inc. (HRFI) Fund Weighted Composite Index

⁹ HRFI: http://www.hedgefundresearch.com/pdf/pr_20120119.pdf

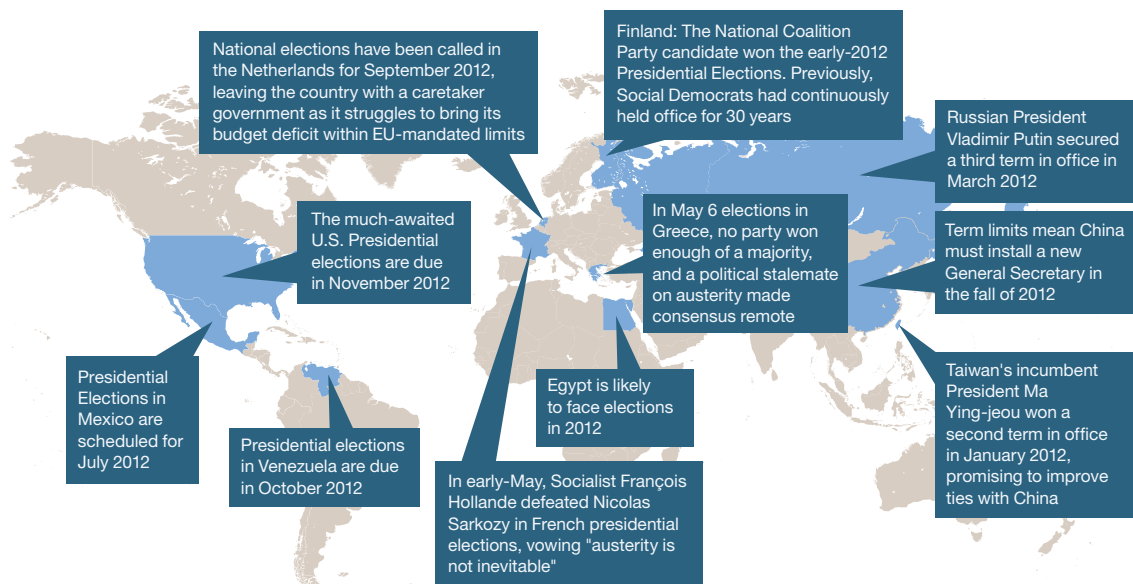
FIGURE 12. Outlook For Real GDP Growth Rates, World and Select Regions, 2012F – 2013F

(%)



Note: 100 basis points equals 1 percentage point; Aggregate real GDP growth rates are based on GDP weights calculated by the EIU
 Source: Capgemini Analysis, 2012; Economist Intelligence Unit, May 2012 'Global Economic Prospects May 2012,' The World Bank, May 2012

FIGURE 13. List of Nations That Have or Will Undergo National Elections in 2012



Source: Capgemini Analysis, 2012; Leadership elections and selections in 2012, The Economist

The following are among key regional considerations for investors in 2012-13:

- **Europe:** The deteriorating quality of sovereign debt is still hurting European banks, and European governments are struggling to juggle the need for austerity and growth. Uncertainty has rattled investors, who want clear signals that Eurozone countries have the political will to negotiate solutions that can guide individual member countries back to health, and preserve the viability of the Euro as a common currency. The liquidity situation in the Eurozone also needs monitoring, and wages may need to drop in real terms to increase the competitiveness of the region. That said, investors also need to understand there is no panacea for Europe's problems, which could take years to resolve, and could feature additional debt write-downs for the likes of Greece and Portugal.
- **U.S.:** Economic data suggest the U.S. economy is recovering, albeit slowly. Corporate revenues are also showing signs of health, while companies are keeping inventories low and costs in check. The result is likely to be greater investor interest in equities, and a move away from U.S. Treasury securities—especially since the Federal Reserve has pledged to keep interest rates near zero for some time. Moreover, a fiscal cliff looms at the end of 2012 that requires a remedy, or U.S. economic prospects will drastically dim. Politics could also be a major issue for U.S. investors since political stability is a key prerequisite for client trust in financial markets. Presidential campaigning ahead of the November 2012 general election has already revealed drastic differences between Republicans and Democrats over how to revive the U.S. economy. And arguably more important than the victor, is whether politicians will find a way to cooperate after the elections to address the near-term economic threat and the long-term need for fiscal austerity. Another economic concern is the housing market, which remains a drag on the recovery, despite low interest rates and signs the market may have bottomed.
- **Asia-Pacific:** Investors remain cautious about the prospects for Asia-Pacific economies, but there is underlying optimism that policymakers will be able to maintain high growth rates without being overrun by inflation. In the first half of 2011, the People's Bank of China battled inflation by pushing the bank reserve requirement ratio up to a record high of 21.5%, but as

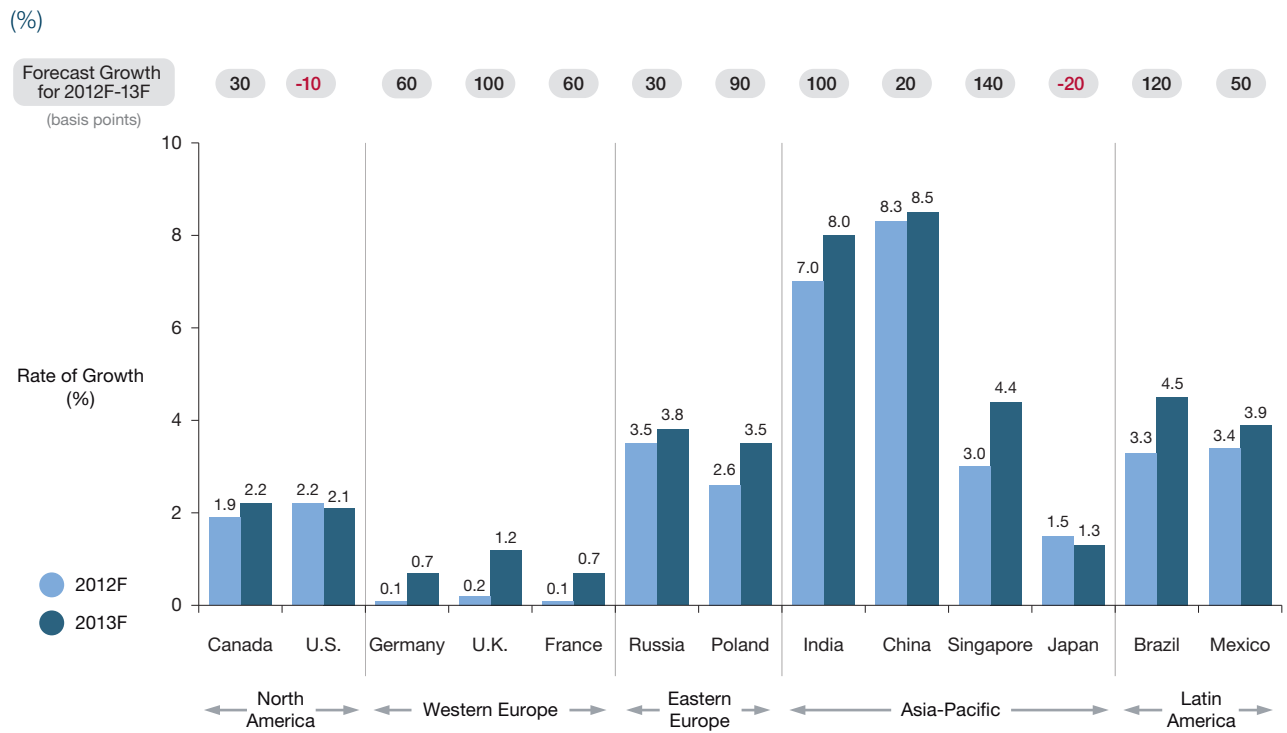
inflation started to slow, Beijing embarked on a path of monetary easing, cutting 0.5 percentage point from the ratio in November 2011 and then again in February 2012. Elsewhere in the region, markets such as South Korea and Taiwan, from which foreign investors have fled in droves, could be the first to benefit when investors regain their appetite for risk. The prospects for the region as a whole, however, depend most heavily on whether China can engineer a soft landing, and the mature economy of Japan can recover from a challenging 2011.

- **Latin America:** The region's major economies are perceived to be on solid footing, and are expected to post healthy growth in 2012, largely because high prices for mineral and agricultural exports in recent years have boosted foreign-currency reserves, and conservative banking rules have left institutions well-capitalized. Still, benchmark equity indices such as Brazil's IBOVESPA are unlikely to recoup all their recent losses in 2012, especially if investors fear weakness in Europe could result in lower investment inflows and less demand for the region's agricultural exports. The region's prospects will be helped by recent initiatives to improve government transparency and civil liberties, which contribute to market confidence. Also, central banks in many Latin American countries have focused on keeping inflation low, and many have recently abandoned soft exchange-rate pegs, opting for floating exchange-rate regimes.

By 2013, many countries are expected to be showing healthier growth rates. However, those rates will still be very modest in developed nations, which still face a vicious cycle of high debt, austerity measures, and low investment in infrastructure. GDP growth in China is expected to be back up at 8.5% in 2013, while growth in India hits 8.0% (See Figure 14).

Notably, trade among emerging markets is likely to be an important source of growth for those economies as they seek to lessen their reliance on developed markets. Intra-emerging-market trade has already grown at a rapid pace in recent years, and is expected to accelerate in the near future. To facilitate such trade, the development banks of Brazil, Russia, India, China, and South Africa (BRICS) signed two pacts in early-2012 meant to provide credit facilities in local currency and enable easier confirmation of multilateral letters of credit.

FIGURE 14. Outlook For Real GDP Growth Rates, Select Countries, 2012F – 2013F



Note: 100 basis points equals 1 percentage point
 Source: Capgemini Analysis, 2012; Economist Intelligence Unit, May 2012

Investments of Passion Attracted Interest As Substitute Investments in 2011, Especially Among Emerging-Market HNWI's

The value of Investments of Passion (IoP), including Art, Jewelry and Memorabilia, does not count toward our calculations of HNWI investable wealth, but it is clear that many HNWI's choose to devote considerable sums to many types of pursuits and collectibles. While these investments are not strictly an alternative to financial assets, the global economic and financial crisis has certainly led many HNWI's to view these holdings as an important component of their overall investment strategy.

In 2011, young HNWI's from emerging markets showed themselves to be an especially powerful force behind many of the classes of IoP, and especially those that are seen as solid investments likely to appreciate in value over time and/or offer a low correlation to mainstream financial instruments.

In early 2012, the European Fine Art Foundation (TEFAF) reported that China (including Hong Kong) has overtaken the U.S. as the world's largest market for art and antiques.¹⁰ China's share of the global art market, according to the TEFAF report, rose from 23% in 2010 to 30% in 2011, pushing the U.S. into second place, with 29%. The U.K., which had already been overtaken by China in 2010, remained third, with a 22% market share. "The dominance of the Chinese market," says the report "has been driven by expanding wealth, strong domestic supply and the investive drive of Chinese art buyers."

Emerging-market buyers have also increasingly shown themselves to favor indigenous works, and items that represent their own cultural heritage. This preference has helped to drive up regional indices, including the World Traditional Chinese Works of Art Index, which rose 20.6% in 2011, and the Latin American Art Index-NY, which rose 16.0%.¹¹

The growth in buying interest from emerging markets HNWI's has also led to the creation of specialized funds. For example, independent advisory firm Artvest¹² values the Art funds industry at US\$700 million to US\$750 million globally, with Asian funds accounting for approximately one third of that total.

¹⁰ "The International Art Market in 2011: Observations on the Art Trade over 25 Years," commissioned by TEFAF Maastricht, published March 16th, 2012

¹¹ Both indices are part of the Mei Moses Family of Art Indices; <http://www.artasanasset.com/>

¹² <http://artvest.com/>

OUTLOOK FOR MANY INVESTMENTS OF PASSION IS UPBEAT AFTER BUYING INTEREST IN 2011

IoP return on investment is difficult to gauge, not least because investors are heavily motivated by intangibles such as aesthetic appeal. As a result, it is difficult to say how much investable HNWI wealth will find its way into IoP, but buying interest is expected to remain strong in many classes as investors look to diversify their holdings—especially while strong returns on financial products are difficult to secure.

The outlook for Art remains upbeat, for instance, although experts report that buying interest was selective in 2011. For instance, Christie's November 2011 sale of Impressionist and Modern Art in New York yielded only US\$140 million against presale estimates of US\$210 million-300 million, and 38% of the lots failed to find a buyer. By contrast, in the same month and city, Christie's Post-War and Contemporary auction yielded sales of more than 33 works for more than US\$1 million, and only 10% of lots went unsold.

Luxury Collectibles, Coins, Diamonds, and Gems/Jewelry were other categories that rose in value in 2011, while the estimates regarding Fine Wine and Sports Investments were more bearish.

Prices in the luxury car market, a key component of the Luxury Collectibles segment (which also includes boats, jets, etc.), has also showed divergent trends. For example, the HAGI Top Index, which measures rare historical auto values, rose by 13.9% in January-November 2011, far outperforming the S&P Global 1200 index of equities, which declined 7.7% during that period. The Hagerty

Ferrari Index rose 22% in 2011, putting it 138% higher than its value five years earlier. By contrast, the Hagerty Price Guide's Index of British Cars has fallen 7% since 2008.

Diamonds outperformed again in 2011, providing more evidence that HNWIs and other investors are opting for tangible assets during economic uncertainty. The price of diamonds surged nearly 30% in the January-July period, before easing to end 2011 up 20% from a year earlier. The price run-up was fueled by increased demand from China and elsewhere in Asia-Pacific, while production remained flat.

HNWIs continue to buy into professional sports, but data suggest the purely financial return on such investments was weak in 2011. For example, the STOXX Global Grand Prix Index fell 19.4% between January 2011 and January 2012, during which time the STOXX Global 1800 index fell 6.7%¹³. Still, the index returned an annualized 60.9% in the three years to January 2012, while the STOXX Global 1800 index grew 39.1%. By contrast, the STOXX Europe Football Index, which covers exchange-listed soccer clubs in Europe, fell by 38.2% between January 2011 and January 2012. Given the prevailing economic uncertainty, sports indices such as these are likely to under-perform for some time.

Among other collectibles (e.g., Wine, Antiques, Coins, Memorabilia), the Fine Wine market remained mostly bearish during 2011. The Live-Ex Fine Wine 50 Index, which tracks the 10 most recent Bordeaux vintages, declined by 10.1%. However, the Live-Ex Fine Wine 500 Index (which also includes New World wines) jumped 10% during 2011, reflecting the shift away from French wine as the dominant taste.

¹³ The STOXX Global Grand Prix Index tracks the performance of major players in the Formula 1 industry, including engine manufacturers, tire suppliers, and oil and fuel suppliers participating in Formula 1, as well as title sponsors

Wealth Management Firms Look to Scalable Business Models to Drive Profitable AuM Growth and Bolster Client-Advisor Relationships

- **While wealth management has fundamental strengths as a business, costs have risen faster than the growth in revenues in recent years, so the imperative for wealth management firms now is to chart a course to profitable AuM growth, while bolstering the client-advisor relationships that are the lynchpin of their business.**
- **Challenges other than costs are also converging to reshape the wealth management industry.** Firms have a degree of control over some of these developments, such as diminished client and advisor loyalty, but less control over more systemic and structural trends, including the post-crisis backlash against the financial services industry, rising competition, greater regulatory scrutiny, heightened market volatility, and increasing diversity in the world's HNWI population.
- **Many firms will need to rethink their business models to deal effectively with the new industry landscape, and overcome constraints imposed by previous decisions and assumptions.** In the process, firms will need to re-focus on core competencies, shore up client trust, bolster client-advisor relationships, improve client-segmentation models, and analyze new market opportunities through the prism of changed external realities. This will also require senior management to be focused and proactive, yet flexible, in steering the firm's re-orientation, which is likely to include numerous other imperatives, from executing digital-technology strategies to managing an ageing advisor workforce.
- **Firms that can identify, leverage, and embed scalability levers in their business models** will be better able to drive client AuM growth at relatively lower cost, while maintaining high levels of client satisfaction. Different firms will prioritize different scalability levers, depending on factors such as core competencies and overall business strategy, but critical for most will be levers around client segmentation and true scalability-driven acquisitions.

ELEVATED COST-TO-INCOME RATIO TOPS LIST OF FUNDAMENTAL CHALLENGES TO WEALTH MANAGEMENT BUSINESS MODELS TODAY

Wealth management is an inherently attractive business, largely because it is a stable generator of cash, and requires relatively little capital. Its client and asset bases also seem to expand naturally and continually, given rising levels of global prosperity. For some firms, wealth management can also be an important “door-opener” to other business lines (such as investment banking¹⁴). And the client pool is seen as relatively resilient, because HNWI's have deeper pockets and access to more sophisticated and timely advice than the average investor, so they are theoretically armed better to ride out market fluctuations.

That said, these favorable dynamics have yet to fully deliver the benefits many firms have envisaged. For example, while capital requirements are relatively low in wealth management, the recent returns on equity are also low—estimated to be in the single digits globally. Also, firms have found it harder than expected to achieve and leverage scale in their operations, as evidenced in recent years by the pull-out of large firms from sub-scale operations, especially in emerging markets.

These setbacks are also a reflection, though, of the challenging operating conditions. Widespread and significant changes are under way in the wealth management industry. These shifts include the post-crisis tendency of investors to opt for products that minimize risk and preserve capital, and the persistent weakness in economic growth in mature markets. Slow growth has kept interest rates low in many markets as governments seek to offset the effects of the global slowdown. Regulation has also become more stringent, making risk management

¹⁴ See World Wealth Report 2011 Spotlight, “Wealth Management Firms Can Leverage Enterprise Value to Better Address HNWI's' Complex Post-Crisis Needs”

even more complex, and potentially jeopardizing the future of certain revenue streams for some financial services firms.

As these forces coalesce, many wealth management business models are buckling under the pressure, unable to adapt quickly or effectively enough to position firms for sustained success.

The issue of profitable AuM growth is a critical case in point. Industry estimates suggest that while total AuM has grown since 2008 (after a significant decline that year), the costs associated with managing those assets have risen faster than the growth in income. The cost-to-income ratio of the global wealth management industry stood at 79.8% in 2010, up from 63.7% in 2007¹⁵ (see Figure 15), reflecting a consistently rising cost trend. And that trend is clearly exacerbated by the inability of firms to generate significant fees when interest rates are low and investors are favoring capital-preservation products. To improve overall profitability, then, firms need to find new and sustainable ways to control and reduce their costs while growing AuM.

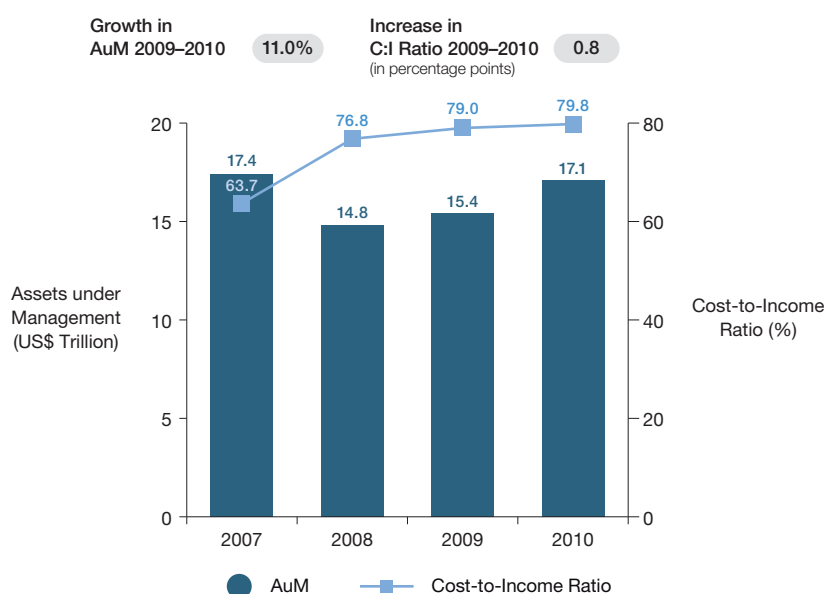
Gains in total AuM at some firms also reflect another industry trend—bringing brokerage and insurance businesses under the wealth management brand umbrella. These strategies aim to provide a more comprehensive and holistic proposition for clients, but have pooled AuM

without necessarily rationalizing the underlying costs. Similarly, private banking now offers many mainstream retail banking products, such as time deposits, which boost industry AuM but rarely generate much margin.

And even as profit margins are being eroded, rising levels of advisor remuneration make it expensive to acquire and retain successful advisors (who, of course, are key to bringing in and managing clients and assets). Other costs are also high, with expensive real estate locations, and high technology and regulatory compliance costs all taking their toll on the bottom line.

While many firms face rising cost-to-income ratios, they must also manage numerous other forces at play. For instance, both client trust and advisor loyalty have been undermined by the financial crisis and its effects. HNWI's faith in advisors and firms is slowly being restored,¹⁶ but trust and confidence in regulatory bodies and institutions remains shaken, especially as politicians and governments prevaricate over tax and other market-related policies. And client trust in advisors and firms remains fragile, as it depends so heavily on investment performance—and performance is far from assured in the currently challenging and volatile macroeconomic and market conditions. Advisors could also be in danger of defecting in current conditions given there is high demand for successful advisors.

FIGURE 15. Assets under Management (AuM) and Cost-to-Income (C:I) Ratio, 2007 – 2010



Source: Capgemini Analysis, 2012; The Scorpio Partnership Private Banking Benchmark, 2009 and 2011

¹⁵ The Scorpio Partnership Private Banking Benchmark, 2009 and 2011

¹⁶ See World Wealth Report 2011 Spotlight, "Wealth Management Firms Can Leverage Enterprise Value to Better Address HNWI's Complex Post-Crisis Needs"

The good news is that firms have some degree of control over how they address AuM, client, and advisor issues. More difficult to tackle are the systemic and structural transformational trends in the wealth management landscape, especially in the post-crisis years.

First of all, wealth management firms are operating amid a widespread public backlash against the entire financial services industry. The loudest criticism centers on taxpayer-funded bailouts, and industry practices such as perceived conflicts of interest and executive bonuses. Still, all firms have to work harder to drive client and advisor loyalty amid perceptions that the financial industry puts profits before clients.

This backlash has been coupled with greater regulatory oversight and scrutiny. The aim of regulators has been to reduce systemic risk, and protect individual investors. The result for firms, however, has been higher costs—in the form of both increased compliance and indirect economic effects. For example, some regulatory measures have affected funding costs, and some are even targeting business models. The U.K.'s Retail Distribution Review, for one, is designed to improve transparency and reduce fees, but essentially shifts the industry income structure from a primarily commission-based approach to a more fee-based approach.

At the same time, the markets themselves have been highly volatile since the financial crisis, and uncertain economic and political conditions have complicated investor strategies even more. With heightened volatility even in traditional safe-haven investments such as gold, and a high level of correlation between asset classes, it has become especially difficult since the crisis for wealth management firms to develop effective diversification strategies, and provide appropriate holistic wealth management advice to HNW clients.

Even before the financial crisis, however, financial markets had started to display far shorter cycles than had been typical before the year 2000 (see Figure 16). This suggests wealth management firms must be able—as the rule, and not the exception—to guide their clients successfully through more periods of higher volatility, and short, unpredictable bull and bear cycles. This could be a particular challenge for firms that have built business models directly tied to market performance (especially in commission-based systems). These models assume up-cycles will occur consistently, thus providing firms with an extended period in which to accumulate the trust

of HNW clients, along with greater incomes, when times are good. Firms now need to adjust to a 'new normal' in which they must find ways to add value to the client relationship even when market conditions are persistently difficult.

The challenges just described show how the convergence of shifts in the economic and business environment are affecting the fundamental economics of wealth management. But these are not the only changes affecting individual firms and the industry as a whole.

For one thing, corporate structure and brand reputation can help or hinder any wealth management business today. For instance, scandals or financial losses incurred by any part of an integrated financial services firm can reflect badly on the reputation of a wealth management business. In an integrated firm, senior management may also become distracted from the wealth-management business by problems in other areas of the firm.

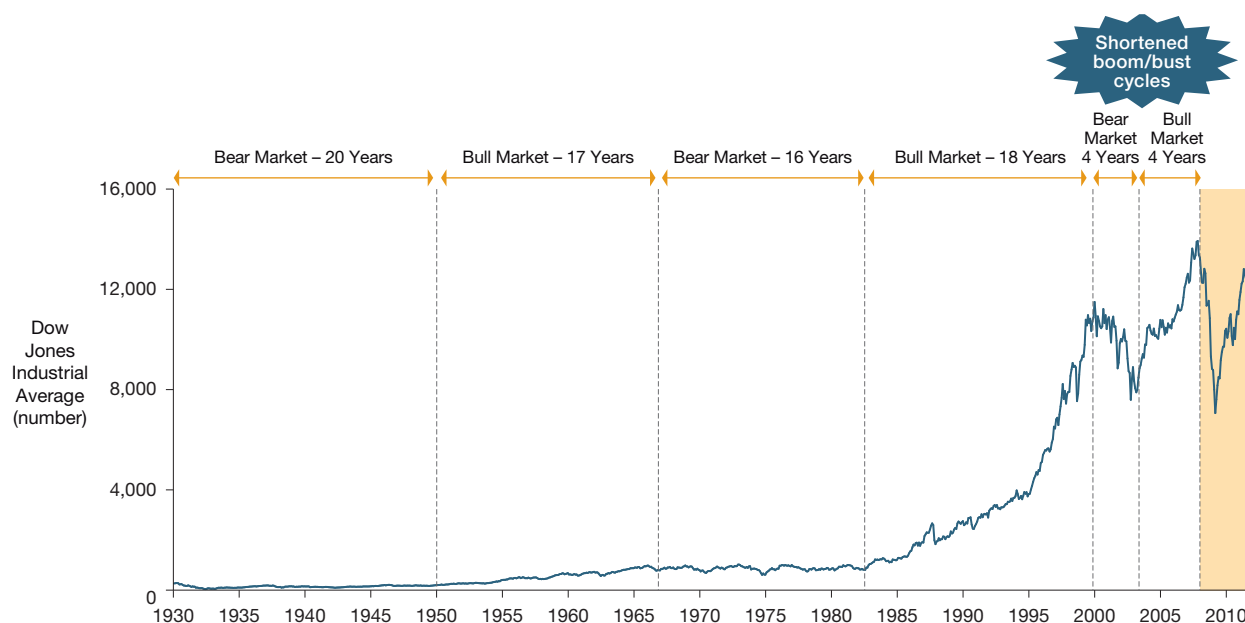
Parental structure can also influence the types of products a wealth management firm makes available to its clients. For example, a wealth management firm with investment bank ownership might favor more institutional products (the parent's specialty). A retail bank legacy might produce a greater focus on products linked to the parent's retail banking offerings.

The wealth management industry as a whole is also facing both consolidation and new competition, as players jockey to capture relatively dependable, fee-based revenue streams. These revenues offer a critical boost to pre-tax margins, which have been declining gradually for the past few years, though they have been more resilient and dependable in wealth management than in activities such as investment banking.¹⁷ Each player also needs enough AuM to operate profitably, and it can be especially difficult for new entrants to accumulate adequate AuM when they are often battling large and established incumbents, and less-than-friendly regulatory environments.

In emerging markets, it is especially critical for firms to make a reliable assessment of how much AuM is really targetable, given the stiff competition, and the fact that many of the assets are in illiquid or unmanaged pools. And increasing wallet share creates yet another imperative for firms: understanding the cultural and behavioral specifics of each market in which they operate.

¹⁷ See World Wealth Report 2011 Spotlight, "Wealth Management Firms Can Leverage Enterprise Value to Better Address HNWIs' Complex Post-Crisis Needs"

FIGURE 16. History of Bull and Bear Markets in the U.S., 1930 – 2012



Source: Capgemini Analysis, 2012; Yahoo Finance, 2012

The world's population of HNWIs is increasingly diverse, and firms can no longer hope to simply take a business model that works in one market and replicate it in another. Rather, firms have to make deliberate adjustments to their business models to achieve sustained success in multiple locations. This means choosing which processes, products, and services to standardize across the firm, and which are differentiators that need to be customized to individual market requirements—even if it increases operational costs and complexity.

FIRMS NEED TO FIND RELEVANT WAYS TO MODERNIZE LEGACY BUSINESS MODELS

Today's wealth management business models reflect strategic decisions of the past, operational decisions of the present, and the ongoing evolution in markets. The net effect, though, is that many firms have little flexibility to adapt to changing business conditions quickly or effectively enough. Next-generation business models will need to overcome that weakness.

Firms May Need to Rethink Prior Strategic Decisions

In looking for ways to improve future performance, many firms will need to look first at how to undo the impact of prior strategic decisions. Those effects include:

- Diluted brand proposition.** Many firms, pursuing ambitious growth targets, moved away from core competencies in the recent past, and ended up diluting service levels and brand value. Ironically, this is a problem firms have faced many times over the last few decades as they have sought to adapt to changing market conditions. So yet again, they will now need to re-focus on core competencies to drive client satisfaction, and must consider other approaches, such as adopting an open architecture, to provide clients with access to non-core services.
- Fragile client trust.** Many firms focused excessively on investment performance in the past, without tightening risk management practices, especially in the ebullient pre-crisis years. As the financial crisis unfolded, it quickly became clear this strategy had contributed to the contagion in markets, compounding losses for

clients, confounding regulators, and causing the widely publicized demise of counterparties and firms. The fallout weakened client trust, and reduced the commitment (and wallet share) of clients. If firms are to grow the AuM of existing clients, and attract client referrals, they will need to work on reinforcing client trust and making it less vulnerable to market cycles. This will also bolster the ability of firms to attract net new money, which is critical to growing revenues while keeping costs low.

- **Diminished client-advisor interaction.** In the past, many firms urged advisors to expand their client lists, assuming that more clients would mean more profits. In reality, when advisors focus aggressively on bringing in new clients, they invariably reduce the time spent with existing clients—possibly to a point where clients become dissatisfied or mistrustful. Firms will need to discern and maintain the optimum level of client-advisor face time (an amount that will differ by client), especially as they seek to develop an integrated channel strategy.
- **Inadequate focus by top management on key issues.** At many firms, a number of issues have detracted from the focus of top management on key business issues. Some firms have been distracted from long-term strategy by short-term investment and other metrics. Others have increasingly hired executives from segments other than wealth management, where the key strategic issues may be very different. To chart and pursue a course to sustainable growth, firms will need a stable and experienced top management team, which understands the fundamental changes under way in the industry, and who can execute the kind of operating decisions needed to succeed in a margin-squeezed environment.
- **Vulnerability to an ageing advisor workforce.** While the average age of HNWI is getting younger, the same cannot be said of advisors. Older, successful advisors play a crucial role in maintaining and growing the existing client base, and grooming young advisors. However, if these tenured advisors favor advisory methods (and technology) that do not resonate with younger HNWI, important client needs could go unmet. Firms will therefore need to map advisors to the appropriate category of clients to ensure the relationships are well-matched, and perhaps develop a younger advisor workforce for younger HNWI to relate to.

Key Operating Practices, Including Client Segmentation and Digital Strategies, May Also Need to Be Refreshed

Certain legacy operating assumptions have also made it hard for firms to adapt to new market dynamics. A prime example is how client segmentation has remained heavily based on assets—for instance classifying clients as “mass affluent,” “wealthy,” or “ultra-wealthy,” depending on their assets.¹⁸

Segmentation based purely on assets yields sub-optimal results in both product positioning and client service, so firms will need to be more sophisticated in their approaches, taking account of the growing number of factors that shape client aspirations and needs—from age, gender, and location to risk appetite, source of wealth, product preferences, return expectations, and investment objectives.

Segmentation strategies will also need to take a more comprehensive accounting of HNWI assets, including assets held at other institutions, to provide firms with a more thorough understanding of the overall needs of their clients. Without this kind of holistic view, firms could inadvertently be under-serving high-potential HNWI. This is especially true for retail banking-wealth management strategies, but applies equally to the wealth management industry as a whole.

More-relevant segmentation approaches, in helping firms to better understand client investment behavior and biases, can help to improve client experience, optimize channel marketing, service positioning and sales efforts, and rationalize costs.

Firms have also been slow to implement comprehensive digital-transformation strategies, despite rising demand from both clients and advisors, who want more freedom to transact, interact, collaborate, and access information in different ways.

Many firms could be more aggressively pursuing digital adoption and transformation, but there are hurdles in terms of initiating and executing such strategies, and managing their governance. Management inertia, security and privacy concerns, and the lack of a proven business case can all stump digital transformation at the planning stage. Execution can be undermined by a lack of skills, IT complexity, and inadequate data/information management. Firms may also be unprepared to manage the impact on job responsibilities when activities are automated and information is widely accessible.

¹⁸ For the purposes of our analysis, we separate the HNWI segment into three discrete wealth bands: those with US\$1 million to US\$5 million in investable assets (so-called “millionaires next door”); those with US\$5 million to US\$30 million (so-called “mid-tier millionaires”) and those with US\$30 million or more (“Ultra-HNWI”)

The governance of digital transformation can also be a problem if there is no real transformative vision, or there is ineffective (or non-existent) coordination across organizational boundaries, business units, functions, or processes.

Firms May Also Have to Re-Think Legacy Assumptions in Sizing New Opportunities

In today's operating environment, wealth management firms will also need to consider carefully whether to target "buzz" markets, which are expected to be the drivers of future HNWI growth. If investable-wealth levels prove to be less than expected, it will be difficult for multiple players to survive.

The experience of some firms in Asia-Pacific may offer important lessons learned. In an effort to garner more AuM, and strengthen their industry positions, many wealth management firms have attempted to expand into key Asia-Pacific markets in recent years, lured by rapid economic growth. However, levels of real investable wealth have often proved to be smaller than expected, and insufficient to sustain multiple global wealth management firms, let alone to power growth.

Some global players have already begun to sell off operations in these smaller markets. Instead, they are focusing on markets in which they can better utilize organizational capabilities so as to add more client and shareholder value. These firms are essentially conceding their attempts to build scalable business models were incompatible with prevailing market conditions or their own DNA. However, it is important to note that other firms may still be able to thrive in these markets (and perhaps acquire disposed assets) by leveraging different competencies and business models.

SCALABILITY IS KEY AS WEALTH MANAGEMENT BUSINESS MODELS EVOLVE, BUT HURDLES EXIST

Given the challenges facing the wealth management industry, many firms are now grappling with how best to achieve revenue growth from new markets or products without adding incremental resources and costs—and while avoiding service degradation during expansion. This type of scalability is likely to be the earmark of 'next-generation' business models, because it better positions firms to navigate the changing landscape profitably, and offers more flexibility to manage whatever is the next industry shift.

In fact, a well-defined scalable business model can reinforce a virtuous circle of brand building and expansion, providing an important competitive edge to wealth management firms as they identify and pursue growth opportunities. But scalability offers benefits, and presents challenges, at different business levels. For instance:

■ At the wealth management firm level:

- **Business agility** can be enhanced by speeding go-to-market strategies, facilitating market entry/expansion, and ensuring greater responsiveness to other changes in the market environment. This can serve as a competitive differentiator.
- The **profit equation** is improved as fixed costs are kept in check while variable costs increase at a slower pace than the value added (at least over the medium term once investment returns begin). In short, firms can serve more clients, or the same number of clients in more ways, at lower incremental cost. However, it is also a reality for most firms that costs have long grown in lockstep with revenue and asset bases, and many will struggle to make substantive changes to that paradigm.
- **Regulatory hurdles** to expansion may be spotted sooner, allowing firms to take proactive steps to ensure compliance. But scalability may also expose firms to regulatory risk. For instance, attempts to centralize the design of products, or standardize products and processes across regions, may inadvertently create non-compliance. Restoring compliance, or creating regional-specific exceptions to the rules, may ultimately be more costly than a less scalable approach.
- **Client and employee engagement** can get a boost from scalability, which allows more clients and advisors (and other stakeholders) to be closely engaged in the firm's processes and culture, helping to drive their engagement in the brand.
- **Scale economies** are an obvious and much-touted benefit of scalability, but at least one route—acquisition—may not always deliver hoped-for dividends. This is because scalability is not about absolute size, but about the ability to generate returns at a lower incremental cost. Too often, acquisitions end up merging businesses that are not complementary, so process complexity actually increases, and firms struggle to rationalize in a cost-effective way.

▪ **At the distribution level:**

- **Client satisfaction** can certainly be improved through scalability, as systems and processes can be deployed appropriately to maintain high service levels during expansion, even without additional resources.
- **Advisor satisfaction** can also be improved—by streamlining processes and technology to optimize advisor time, while providing clearer direction on the firm’s value proposition.
- However, the **underlying business proposition** is inherently relationship-based and personalized, so it is difficult to standardize in any meaningful way. In fact, standardization attempts could directly counter the increased demand by clients for customized solutions related to their specific requirements.

Ultimately, then, it will probably be difficult for wealth management firms to achieve scalability across the entire wealth management value chain (as illustrated in Figure 17), but firms can still selectively scale up specific activities related to acquiring, retaining, and servicing clients—while employing other tools to improve the proposition in areas that cannot be easily scaled.

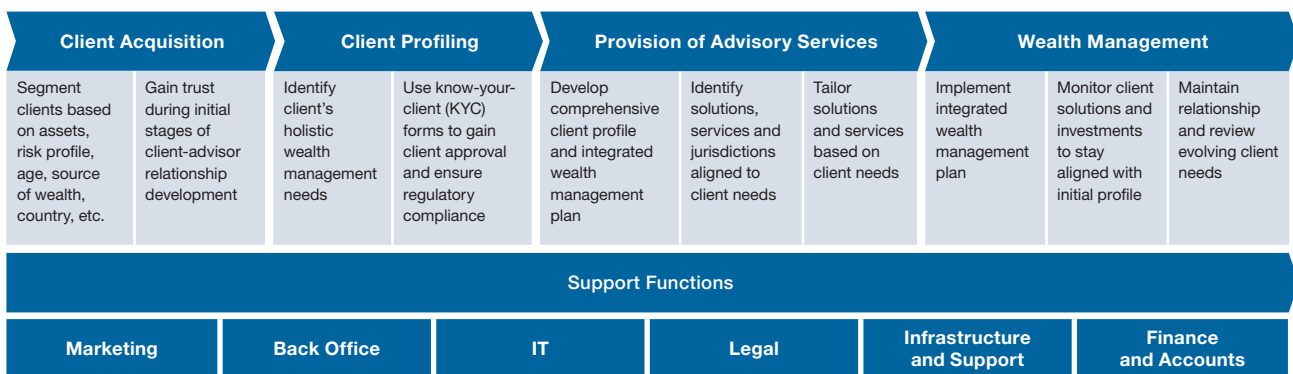
Client Acquisition and Profiling Epitomize the Challenges of Scalability

In general, scalability is much more difficult to achieve in activities related to client acquisition and profiling than in advisory services or wealth management. The nature of the advisory relationship creates a significant challenge in these two activities, as it is difficult to secure client trust in general, let alone on an accelerated basis.

Indeed, the trust required to acquire clients can only be built through multiple interactions that prove to the client that the advisor understands their needs, and can develop and execute a customized wealth management strategy that reflects their priorities. Many of these interactions take place even before the HNW client has committed to the advisor relationship, so the effort is very much a long-term commitment to loyalty from the perspective of both the advisor and the client.

Technology can facilitate the means, speed, and frequency of communications between advisor and client (and thus improve advisor productivity), but it cannot improve the substance of those interactions, or otherwise replace “face time” spent building client relationships.

FIGURE 17. Wealth Management Value Chain



Source: Capgemini Analysis, 2012

As a result, the role of technology-led scalability in client acquisition is likely to be focused most on standardizing advisors' non-core and administrative activities so as to minimize the amount of client-relationship time lost by advisors, and speed their administrative response times.

Client profiling is another area in which scalability is challenging, since the business proposition must recognize a wide range of investing behaviors and cultural preferences to cater to different geographies. These disparities defy standardization, making it difficult for firms to build packaged wealth management solutions that can be successfully leveraged globally.

For example, HNWI in developed economies in Europe and North America have generally become more conservative in current uncertain macroeconomic conditions. Capital preservation is a top priority for these HNWI, while those in Latin America and Asia-Pacific excluding Japan are more likely to consider a relatively higher-risk investment if the potential rewards are high. Tradition also helps to drive different cultural investing norms, such that gold (in the form of jewelry) has long been an asset class of choice for many in Asia-Pacific, while Sharia products (which adhere to Islamic banking principles) are critical in many Middle Eastern markets, and Art and other collectibles remain a popular asset class among European HNWI.

Given the need for customization and the desire for scale, wealth management firms will need to create an effective client segmentation model by identifying the critical elements for each market. Then they can customize their operating practices to cater to various segments. In this way, selective scalability, enabled by technology, can create value for both the firm and the client.

THE WAY FORWARD: LEVERAGING TECHNOLOGY TO ACHIEVE SELECTIVE SCALABILITY

The hurdles to scalability are far lower in providing advisory and wealth management services than in client acquisition and profiling, so wealth management firms will get most value from leveraging technology to achieve scalability in these areas of the value chain. The benefits of scalability in these areas largely relate to automation, and the expanded reach of expertise. Some firms may also have highly developed asset management capabilities that can be used as a foundation and lead-in for building scale.

On the advisory side, firms can be highly effective by creating back-end teams, specialized in financial planning, asset allocation, estate planning, etc., to create customized plans for clients, based on advisor input on the client's profile, segment, aspirations, and so on.

Similarly, firms can leverage technology in executing wealth management activities, without using any high-value advisor time, once the client's integrated wealth management plan has been designed and agreed. Straight-through processing systems can provide prompt notification to clients of trade execution, position, and portfolio updates, etc., preserving advisor time for strategic conversations.

Leading firms are already experimenting with embedding scalability into business models, using process- and strategy-based levers, as well as advisor- and client-based initiatives. The impact of technology-enabled solutions differs by lever, however, making some more critical to success than others.

Multi-Dimensional Client Segmentation Models and Scalability-Driven Acquisition Approaches Are the Most Critical of the Process- and Strategy-Based Levers

Firms will need to focus on core competencies, granular segmentation, and higher automation to drive scalability in wealth management, but most critical (see Figure 18) are: 1) adopting an effective, multi-dimensional HNW client segmentation model based on criteria such as asset size, risk appetite, behaviors, and financial/investment needs and goals, and 2) a more nuanced approach to acquisitions.

The current asset-based approach to segmenting clients yields sub-optimal results, because it does not take account of key drivers of investing behavior, such as risk appetite, and financial aspirations. Using a more multi-dimensional approach, firms will be better positioned to customize their offerings, pitch strategy, and provide touch-points, according to the client's segment. This is likely to generate a higher return on effort, more productive use of advisor time, and higher relationship-conversion and client-acquisition rates—potentially at lower cost.

It will also be critical for firms to view keenly any acquisitions designed to drive scale, since only complementary acquisitions will actually deliver growth while containing incremental costs. It may also be preferable for some firms to opt for acquiring another firm's wealth management team (a "lift-out"), rather than undertaking a fully fledged corporate acquisition.

Other scalability levers offer significant potential, notably optimizing processes by automating back-end operations. Several back-office activities, such as those involving regulatory filings, client reporting, and management information systems, are repetitive and can easily be automated. This will help to optimize cost structures by reducing manpower expenses. Additional benefits include eliminating human error and, most importantly, ensuring timely regulatory compliance. However, it is also important to make sure the outputs are truly standardized as exceptions-handling is time-consuming and costly.

Other process- and strategy-based scalability levers also have potential, including a deliberate focus on markets/operations that can deliver scale for profitability. However, wealth management firms will need to conduct a thorough cost-benefit assessment to identify the point at which the scale of different geographies and operations essentially becomes unprofitable. (This is likely to depend, in part, on the maturity of the prevailing financial system.)

Similarly, firms will need to focus on core business (maximizing the time, energy, and resources devoted to client advisory services), and decide when the business is sub-scale for certain activities. Firms will also need to identify when and how to outsource discrete activities, such as asset management, or repetitive processes that can be more effectively and efficiently handled by a specialist vendor. For some firms, outsourcing will preserve expert resources for core activities, and help to drive cost optimization, though firms with the requisite expertise and AuM may be able to build scale by keeping asset management activities in-house.

Implementing a well-functioning enterprise-wide customer relationship management (CRM) system can also help to ease the flow of information among stakeholders, facilitating quick and efficient decision-making and improved service at the distribution level. However, it is important for the business and technology teams to agree on the usability and functionality of the CRM system at the earliest (design) stage, to ensure the buy-in, success, and ultimate applicability of such initiatives.







Notably, while the client segmentation and acquisition levers are the most widely applicable and critical, each of these scalability initiatives has considerable potential to deliver benefits, especially if firms can combine them to rationalize processes while improving customer experience.

Pooling Product Specialists and Creating Advisor Teams May Be the Most Important Advisor-Based Scalability Levers

There are also several advisor-based initiatives available to wealth management firms hoping to embed scalability in their business models, but the highest priorities are likely to be pooling product specialists and creating advisor teams (see Figure 19).

Pools of product specialists can be responsible for maintaining a knowledge base of various investment products to suit the diverse needs of HNWI's across all client segments. These teams become a central source of knowledge for all advisors, and thus enhance advisor effectiveness and client satisfaction. For the firm, these teams provide another way to share expert resources more efficiently (and cost-effectively). Advisors are more productive, as they have more time to concentrate on core advisory activities. Clients are kept happy, and may even be better served, as they have access (via their advisor) to a wealth of specialized knowledge.

FIGURE 18. Process- and Strategy-Based Scalability Levers

| Lever | Critical/Related Success Factors | Criticality |
|--|--|---|
| Adopting an effective HNW client segmentation model based on asset size, risk appetite, and financial/investment needs | <ul style="list-style-type: none"> Front-office segmentation on servicing needs requires an ability to drive service development in back office Strong data management capabilities required |  |
| 'Scalability-led' focus on acquisitions | <ul style="list-style-type: none"> Acquisitions may yield increased scalability and returns when complementary 'Lift-outs' (acquiring a team) can be beneficial |  |
| Optimizing processes through automation of back-end operations (such as regulatory filings, client reporting, and MIS) | <ul style="list-style-type: none"> Standardized outputs are important as handling exceptions can be a time-consuming and costly activity |  |
| Focusing on markets/operations with potential scale for profitability (and exiting other markets/operations) | <ul style="list-style-type: none"> Firms can look at countries with developed financial systems for relative cost advantages Markets with complementary features are important |  |
| Choosing 'open-architecture' or 'managed-architecture' platform for scalable growth (depending on firm DNA) | <ul style="list-style-type: none"> Large AUM size is needed to support 'managed-architecture' where asset management is done in-house |  |
| Implement leading enterprise-wide customer relationship management systems (CRM) | <ul style="list-style-type: none"> Business and technology teams need to agree on the usability and functionality of the CRM system, and co-design for success and future relevance |  |




 Negligible
  Low
  Medium
  High
  Very High

Source: Capgemini Analysis, 2012

Other team-based models can pull together and leverage advisors of differing experience levels. Most current models assign HNW clients a single, experienced advisor (often because HNW clients demand it), but this approach puts a premium on experienced advisors, and makes it hard for firms to utilize less-experienced advisors. The team approach can help firms to utilize and groom less experienced advisors, without undermining the quality of service to clients.

A more marginal but nevertheless possible source of scalability involves utilizing professional expertise (or vendors) to implement a robust hiring and training plan for new advisors. This approach can help firms to build the technical and "soft" skills needed to engage effectively with potential HNW clients. This training could also occur through mentoring in the team-based environment, but firms could reduce manpower expenses if they use outside specialists and vendors to find and properly train new (and less expensive) hires.

FIGURE 19. Advisor-Based Scalability Levers

| Lever | Critical/Related Success Factors | Criticality |
|--|--|---|
| Maximizing advisor effectiveness through sophisticated central product specialist teams | <ul style="list-style-type: none"> Smooth flow of information and strong co-ordination between advisors and product teams Team capability and multi-market expertise |  |
| Creating advisor teams that include a healthy mix of experience to cater to client needs while grooming new talent | <ul style="list-style-type: none"> An effective mentoring plan with well-defined roles is necessary to truly prepare young advisors |  |
| Utilizing professional expertise (or vendors) to implement a robust hiring and training plan for new advisors | <ul style="list-style-type: none"> Situation-based case studies designed by successful advisors can also be useful for training purposes |  |

 Negligible
  Low
  Medium
  High
  Very High

Source: Capgemini Analysis, 2012

Options Exist for Pulling Client-Based Scalability Levers

While client acquisition and profiling activities are difficult to scale, there are certain client-based levers that firms can pull to increase the number of HNW clients they serve, at lower costs (see Figure 20).

For example, ‘virtual advisors’ and self-driven investment portals can leverage evolving Internet and mobile channels, meeting demand from clients for greater choice in touch-points and digital interaction. Some leading firms have already started to use virtual advisor platforms, either online or in branches, or through multiple channels to overcome the shortage of experienced advisors. Virtual advisor platforms can enhance collaboration, improve client experience, and help firms to optimize costs and improve productivity.

Similarly, self-driven investment portals both improve client experience and reduce costs. Client demand is strong for real-time insight into portfolio balances and wealth. Some clients also prefer greater control over portfolio management, and Internet-based applications can provide a way for them to feel greater control over their assets, and avoid any sense that certain products are being pushed on them. For firms, self-driven investment portals can help to reduce staffing expenses and free up valuable advisor time.



Importantly, though, several such levers are complementary and inter-dependent. For example, the success of virtual advisors requires the firm to have a sophisticated underlying approach to segmentation. Choosing and combining levers for maximum effect will therefore require firms to evaluate the efficacy of levers given their own DNA and scalability strategies.

Whatever the Scalability Strategy, Strong Client-Advisor Relationships Stay Front and Center

Even as wealth management firms try to pursue selective scalability in growth, their focus remains firmly fixed on establishing and maintaining a robust client-advisor relationship. Some examples:

- One leading global wealth management firm opted for selective growth, using advanced client segmentation.** One leading firm had successful operations in many regions, but was hoping to tap into the future growth potential of the Asia-Pacific HNW population and its wealth. Recognizing the vast differences in behavioral/cultural issues in different markets, and their differing levels of wealth, the firm charted a selective growth strategy using advanced client-segmentation techniques to decide which markets to enter. The firm also opted to strengthen its presence in emerging offshore banking centers such as Singapore (critical gateways to Asia-Pacific investments) to position the firm better to meet the future needs of clients and serve them profitably.
- A leading financial services firm in North America built a strong advisor workforce to penetrate the wealth management market.** Wanting to establish a market presence, the firm critically analyzed available data, and identified the importance of a loyal advisor force to sustained firm profitability and client retention. The firm meticulously built its advisor base, understanding the long-term nature of the process, and despite a short-term hit to profitability.
- One leading pure-play wealth management firm wanted to grow its business by luring successful advisors from other firms.** The CEO of the firm (with more than US\$100 billion AuM) was adamant that many of the industry’s top-notch advisors were

FIGURE 20. Client-Based Scalability Levers

| Lever | Critical/Related Success Factors | Criticality |
|---|---|---|
| Increasing client satisfaction by creating ‘virtual advisors’ to leverage evolving Internet and mobile channels | <ul style="list-style-type: none"> Capabilities to create the right connection with HNWIs (based on their preferences and value) are crucial to ensure success of virtual advisors |  |
| Implementing self-driven investment portals to capture non-managed client assets | <ul style="list-style-type: none"> Portals with complete research, execution, and reporting capabilities can help attract new clients |  |

 Negligible
  Low
  Medium
  High
  Very High

Source: Capgemini Analysis, 2012

dissatisfied because they lacked the freedom to make independent decisions. The firm therefore attracted advisors from other firms by making them directly and completely responsible for their client relationships, with the help of centralized back-office support, which managed activities that were important but non-core for an advisory role, such as such as compliance administration.

Some Firms Are Scaling Back to Refocus On Core Markets

Other wealth management firms, acknowledging a lack of scale, are ceding some markets in order to refocus their resources on markets they consider to be core. Some examples include:

- **One large bank with Asia-Pacific aspirations focused instead on leveraging its home-country dominance.**

The firm realized it could not successfully enter multiple countries at the same time, or effectively serve all client segments. Nor could it compete against the slew of competitors, as an increasing number of players sought to tap into the growing population of HNWIs in Asia-Pacific. Instead, the bank focused on building a strong client base with roots and relationships in its home country. The firm also specifically targeted corporate employees and entrepreneurs, who would also appreciate the firm's robust banking offering. The firm also acquired advisors with cultural knowledge of its home region to make clients feel more comfortable in their interactions.

- **One leading wealth management firm focused on Asia-Pacific opted for an independent asset management role.** As the financial crisis unfolded, the firm realized that HNW clients were suddenly skeptical of proprietary products, and favored third-party products—and wanted to be able to choose custodians for investment purposes. The firm also recognized that the independent (external) asset management model was new to many Asia-Pacific clients (though well-tested in mature financial markets). The firm therefore developed a wealth model that allows its clients to choose products and services from other banks and asset management firms via an open architecture platform, while providing clients with a simple fee-based cost model built on a holistic advisory relationship.

- **One leading global financial services firm cut back operations in markets that lacked scale.** At one time, this firm had expanded to establish operations across multiple countries, but the strategy diluted the firm's strategic focus on core operational areas, and led to its operating in many unprofitable businesses. Under regulatory pressure to raise capital ratios and under shareholder pressure to improve profitability, the bank opted to exit more than 15 countries where it lacked scalability in its offerings. The decision will help the bank to reduce costs and meet capital adequacy standards. The firm even exited private banking in larger economies such as Japan so as to focus on high-growth markets when solidifying its Asia-Pacific footprint.

CONCLUSION

A range of firm-specific and industry-wide trends are converging to undermine the profitability of wealth management operations today. When combined, these trends are clearly creating stress on wealth management business models. For instance, firms are faced with market volatility and gun-shy investors, so need to create products that appropriately cater to client needs and risk profiles, while generating margins.

Similarly, given increasingly competitive conditions, firms have to decide when and how to pursue selective growth strategies or prepare for consolidation—at the same time that increased regulation may be creating new hurdles to profitable entry/expansion in some markets, especially perhaps for smaller players.

Scalability—growing AuM at lower incremental cost, not simply expanding in outright size—will be an important lever of sustained profitable growth for many firms. To leverage scalability, however, firms cannot just tighten their belts. Rather, they will need to reassess many of the costs they once considered to be fixed or “sunk,” and explore new options for rationalization. In short, firms need to find ways to recover revenues needlessly lost to costs, thereby reducing their cost-to-income ratios, and ultimately boosting profitable AuM.

For firms to plot their growth strategies, and evaluate the potential for leveraging scalability in that growth, they must first assess their starting point.

Broadly speaking, by assessing the current state of their operations, firms could characterize themselves in one of the following four ways:

- The **“blank slate” firm** is operating successfully in its home market, but considering how to expand. It will need to perform a gap analysis on available vs. required skill sets to excel in target markets, and identify how its core strengths (which also drive brand value) can be leveraged. By leveraging whatever in their DNA made them successful at home to effectively target clients in new markets, these firms can decide whether and how to offer non-core services (e.g., via joint ventures, partnerships), and identify ways in which technology can help to embed scalability in that existing model. These firms have significant potential to get scalability right the first time, assuming they have the requisite capabilities and commitment.
- The **“limited success expander”** has spread beyond its home market, but has been only partially successful. This type of firm will need to ascertain what constrained its success. Common issues include excessive competition for meager asset pools, lack of a sophisticated client segmentation model, and inadequate use of digital tools to improve client experience and advisor productivity. Such firms will need to consider how behavioral and cultural issues vary by market, and whether those differences are properly accounted for in the firm’s value proposition. They may also need to fortify client-advisor relationships. To embed scalability, these firms will need to identify how technology can help target and exploit synergies between operations across regions, and evaluate whether acquisitions have been (and could be) complementary enough to deliver the desired benefits.
- The **“successful expander”** is already reaping rewards from profitable operations in multiple regions. In the process, it will have been exposed to myriad challenges, from evolving regulations to market-specific dynamics such as norms in cultural and investing behavior. To continue growing profitably and maintain existing dominant market positions, these firms will need to analyze exactly what has driven their success, and how they managed to expand without incurring undue

additional costs. They will need to keep rationalizing costs and activities by, for example, leveraging digital tools as widely as possible to enhance client experience. These firms will also need to stay ahead of ongoing regulatory and other market trends that could change the economics of their business—a capability they have probably employed in prior expansion initiatives.

- The **“re-focuser”** is not using scalability primarily to facilitate their growth agenda. Rather, they see scalability as a way to be more responsive to market conditions, even if business is contracting. The challenge for these firms will be to preserve core operations and minimize costs “stranded” in operations that have been de-scaled. One example of a “re-focuser” might be a “limited success expander” that is in a contraction phase. Such a firm could undertake scalability-related investments while contracting, thereby becoming more like a “blank slate firm” when it ultimately pursues growth opportunities at some point in the future.

Whatever the starting point, the path to next-generation business models essentially begins with identifying the effects of legacy business models, and re-focusing on core competencies to expand the business. But the end-game—achieving a robust scalable business model that also reinforces client-advisor relationships—will involve systematic decisions and precise execution.

To identify and prioritize scalability levers, firms will need to decide which processes and activities need to be centralized or decentralized, what types of products and solutions are crucial to growth and whether they need to be centrally and/or consistently designed, whether the technology is in place to leverage the chosen scalability levers and support strategic business priorities, and whether stakeholders (across business, technology, and operations teams) are aligned—and senior management is committed—to leveraging scalability initiatives to achieve profitable AuM growth.

And all the while, firms will need to remain focused on whether their decisions will bolster the satisfaction and loyalty of both clients and advisors.

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Appendix A:

METHODOLOGY

The WWR analysis is rooted in a market-sizing model that evaluates the size and growth of investable wealth in different regions using Lorenz curve methodology. For the 2012 WWR, which evaluates the HNWI segment in 2011, our model covered 71 countries, which together accounted for more than 98% of global GNI and 99% of world stock-market capitalization.

Our methodology involves three steps. We estimate total wealth by country, using national account statistics from recognized sources such as the International Monetary Fund and the World Bank to identify the total amount of national savings in each year. These are summed over time to arrive at total accumulated country wealth. As this captures financial assets at book value, the final figures are adjusted based on world stock indexes to reflect the market value of the equity portion of HNWI wealth.

We then estimate the distribution of wealth across the adult population in each country, based on formulized relationships between wealth and income. Data on income distribution is provided by the World Bank, the Economist Intelligence Unit and countries' national statistics. We use the resulting Lorenz curves to distribute wealth across the adult population in each country.

To quantify investable wealth as a proportion of total wealth, we use statistics from countries with available data to calculate their financial wealth figures, and extrapolate these findings to the rest of the world. We iterate our macroeconomic model each year to account for additional domestic economic factors that influence wealth creation. We also work with colleagues and partners around the globe to best account for the impact of domestic, fiscal and monetary policies over time on HNWI investable-wealth generation.

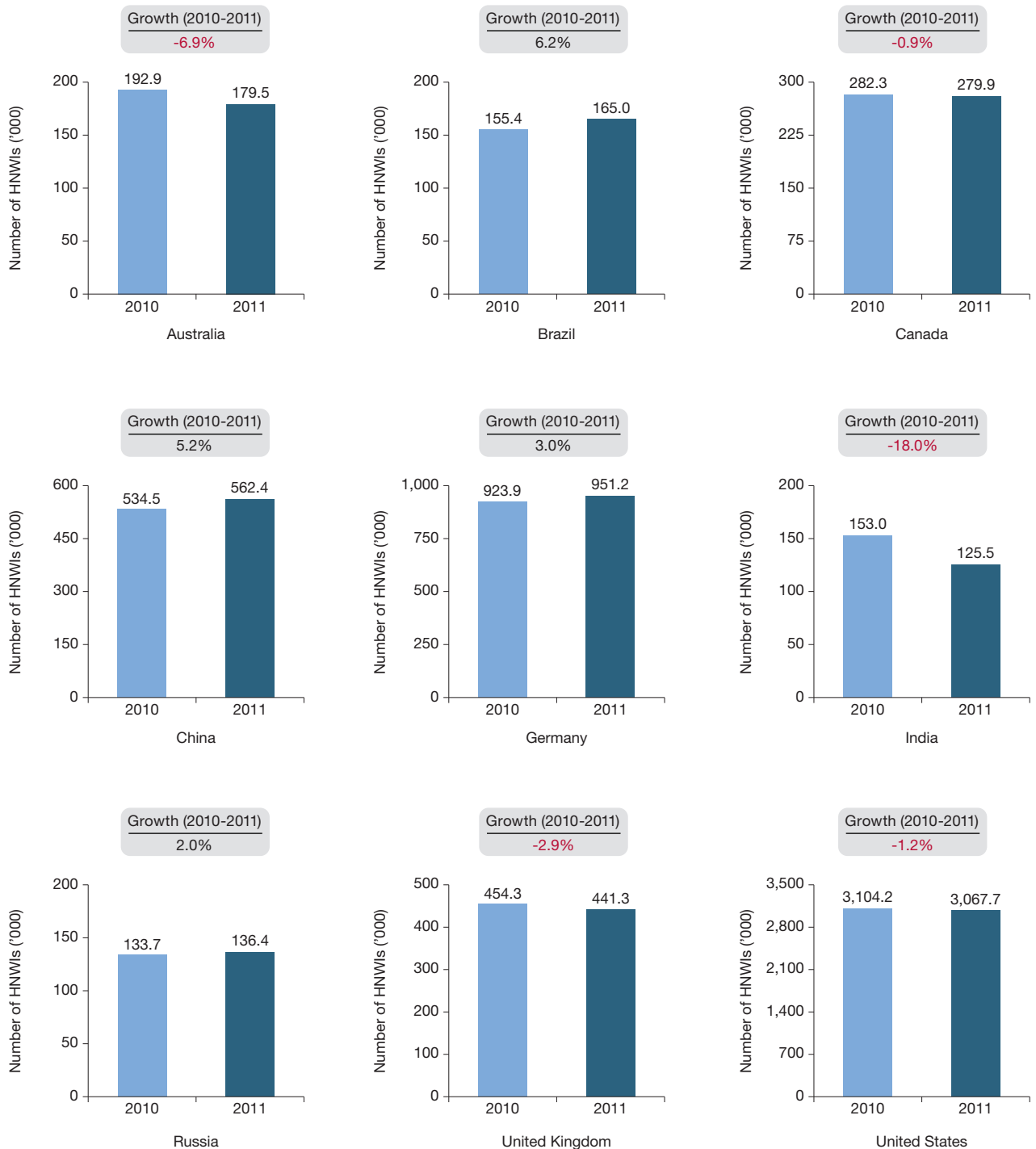
Our investable-wealth figures include the value of private-equity holdings stated at book value, as well as all forms of publicly quoted equities, bonds, funds and cash deposits. The figures exclude collectibles, consumables, consumer durables and real estate used for primary residences. Offshore investments are theoretically accounted for, but only insofar as countries are able to make accurate estimates of relative flows of property and investment in and out of their jurisdictions. We account for undeclared savings.

Given exchange rate fluctuations over recent years, especially with respect to the U.S. dollar, we assess the impact of currency fluctuations on our results. From our analysis, we conclude that our methodology is robust and exchange rate fluctuations do not have a significant impact on the findings.

The information contained herein was obtained from various sources; we do not guarantee its accuracy or completeness nor the accuracy or completeness of the analysis relating thereto. This research report is for general circulation and is provided for general information only; any party relying on the contents hereof does so at its own risk.

Appendix B:

HNWI POPULATIONS, SELECT COUNTRIES, 2010-2011



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