

WEALTH MANAGEMENT



BY CHRIS WRIGHT

Private wealth clients in Asia are facing intense market volatility and uncertainty for the second time in three years. The bad news is that almost all investment classes—global and local equities, debt, property and commodities—everywhere from the U.S. to Europe and Asia face a deeply unclear and likely negative future. The good news is that, compared to the global financial crisis of 2008, clients are much better prepared this time around.

“There is a very marked contrast between what we’re seeing this time and what we went through in 2008 with private clients,” says Arjuna Mahendran, managing director and head of investment strategy at HSBC. “At the retail end of the market, they are going through the same experience as 2008: huge redemptions, forced selling and a general state of panic. But high-net-worth clients are different. Because a lot of them used derivative instruments in 2008 and got burned, they learned their lessons and have de-leveraged.” That leaves them less exposed this time, with more liquid investments and lower risk. “Most of them are looking at this as a guarded opportunity to pick things up fairly cheaply.”

Amid the turmoil of today’s market, there are other longer-term trends at work in Asia’s private banking sector. Many of them stem from a key theme in Asia: The first generation, which has amassed wealth over the course of their working lives, are now wondering how—or if—they should transfer the management of that wealth over to the next generation. The effects of this trend are numerous. Among them is an increasing sense of professionalism

in the way people manage wealth, such as via corporate structures, family offices, more diversified portfolios and a greater use of financial advice.

Another is an increased interest in estate planning, from straightforward wills and probate to training younger generations about wealth management. Finally, there is a more hands-on approach to philanthropy, often among the newly wealthy.

One thing’s for sure: Asia is becoming a true engine of wealth-generation and, as a result, an important focus for wealth management. In October, Merrill Lynch Global Wealth Management and Cap Gemini released their closely watched Asia Pacific Wealth Report, which revealed that Asia had overtaken Europe as the world’s second-largest market of high-net-worth individuals, measured both by population and combined wealth. Tracking such impressive growth, it’s only a matter of time before it overtakes North America for the top spot. One week later, the Credit Suisse Research Institute released its Global Wealth Report, showing that Asia Pacific accounts for 36% of all global wealth-creation since 2000, and 54% since January 2010.

In this changing environment, there is strong demand for tailored, individual wealth-management advice that does more than push a product. “The first question should not be: ‘Do you need life insurance or a trust structure?’” says Hugues Delcourt, CEO for private banking for Asia at ABN Amro. “It should be: ‘What are your goals, your objectives, your constraints? What do you want to achieve?’ Then we can start talking about solutions.”

INVESTMENT

Avoiding the Traps and Seizing the Opportunities



Asian private banking clients are approaching today's market volatility with caution. But bankers say there is still a willingness to engage in markets and take a long-term view.

"Those with a strong opinion on a company or sector are seeing an opportunity to enter, in a gradual fashion," says HSBC's Arjuna Mahendran. "But they don't throw all their eggs in one basket."

It's largely a safety-first environment. "With falling macro momentum and an expectation of choppy markets, UBS has recommended clients to position more defensively for quite some time," says Alexander Kobler, head of Investment Products & Services, Asia Pacific, UBS Wealth Management.

"High-dividend and high-yield stocks are an ideal way to gain defensive equity exposure, with the security of a stable income stream in demand from investors right now." He favors rebalancing cyclical exposure toward defensive sectors such as telecoms, healthcare and consumer staples, and focusing on companies with stable earnings, solid balance sheets and high dividends. "In addition, hedge funds can benefit in this environment," Kobler adds. "Given the current market volatility as well as the speed and magnitude of directional changes, we prefer trading strategies within the hedge funds space."

One particular challenge in this economic environment is determining where the safe havens are for investment. In

some ways, the answer is simple: "The best safe haven is to be properly diversified," says ABN Amro's Delcourt. "Yes, have a little bit of your wealth in gold or treasury notes, but putting everything there? That would not be very wise. In these difficult times we ought to come back to the real fundamentals: risk profile, investment horizons and diversification."

But it's also arguable that safe havens have never been harder to find. "Safety is very costly nowadays, be it in terms of close-to-zero returns or high costs of protection strategies," notes Kobler.

Throughout this year, the answer has typically been gold, but even that fell dramatically in October, albeit from all-time highs. "Our advice is that gold



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Some felt gold had simply become too highly valued to be a sensible investment anyway. Speaking just before the major price decline, Lee Boon Keng of Julius Baer said gold was “somewhat overplayed” as a safe haven. “Gold and other precious metals are no longer safe havens but speculated commodities.

pared to the Swiss franc and Japanese yen, gold does not have a central bank that tries to prevent further appreciation. Thus, the metal can be viewed as the purest-play hedge against prevailing sovereign and currency risks.” Corrections in the gold price simply provide good opportunities to enter, he adds.

Currencies With Resilience

In terms of currencies, two in Asia stand out: the Singapore dollar and the Chinese RMB. The Singapore dollar is expected to benefit from the fact that the Swiss franc, the traditional safe haven currency, has now been capped against the euro. “We are telling our clients that amidst all these uncertainties, we need to focus on the things that are the least uncertain,” says Lee. “One is that after the Swiss National Bank fixes the Swiss franc, we will see the establishment of a replacement as a safe-haven currency, and that is likely to be the Singapore dollar. The make-up of the economy is fairly similar, both have the rule of law, they are key financial centers and have similarly high governance standards. That is going to make the Singapore dollar a very attractive currency to have over the course of the next couple of years.” What to do with the Singapore dollar is a different question: Lee advises clients to look at high-yielding Singapore stocks, including real estate investment trusts (REITs).

The RMB is a different story. While still not fully convertible, it is becoming an increasingly internationalized currency, with the so-called dim sum bond market thriving (with a few dips and glitches) in Hong Kong, and RMB bank accounts appearing both there and increasingly in Singapore. “Our clients have been building positions in RMB,” says Mahendran. Lee at Julius Baer argues that problems in Europe and the U.S. will prompt China to increase the speed of the internationalization of the currency, which ought to mean that it will appreciate steadily; over time, as investment products for offshore RMB develop, they are likely to prove extremely popular with overseas clients. Julius Baer itself is launching a China equity fund and has combined with Singapore’s DBS to create a product investing in dim sum bonds. Additionally, a host of mutual funds for offshore RMB have sprung up over the last 18 months, including big asset management names such as HSBC, UBS, Schrodgers, Barclays

Capital, Singapore's Fullerton Asset Management, and—soon—BlackRock.

One problem with assessing a client's risk tolerance is that it's one thing to explain a possible decline but another entirely to experience it. "Risk tolerance is not a discussion that takes 20 minutes and then you fill out the forms," says Delcourt. "It's very different to say to a client: 'Can you take a 20% decrease in your portfolio?' and then the decrease actually happens. Nobody likes losing money, but when you are confronted with the reality of losing 20% of your portfolio, you may realize there were a few things you were hoping to do and can't do anymore." A proper understanding of a client's true risk appetite is key.

That said, the dangers for private

wealth clients do not seem so acute this time. "2008 basically pointed out the perils of leverage and derivatives; those were considered the two most toxic elements," says Mahendran. "So everything else is considered relatively safe." Within that, clearly emerging markets appear to have the better economic prospects, so advisers tend to suggest allocations to Asia on both the debt and equity side. While Asian equities tend to be popular with those in the developed world, Asian debt has remained more resilient. "Asian debt in general is managing this volatility quite well," says Mahendran. "Spreads haven't widened as much as in 2008."

Hedge funds, he says, are out of favor since they have not performed well; long-only funds are fine, but clients have

a greater need to understand exactly how they operate. "The client wants to understand intrinsically what a long-only fund is investing in, rather than plunging in."

Yet, no matter how bad the markets, investors must do something. "You can't remain uninvested when Asia is running at historically high levels of inflation," says Mahendran. "In Singapore inflation is running at 9.5%. Clients realize they can't just keep their money in cash; they've got to make their assets work for them to keep pace with inflation so they don't lose the value of their wealth in real terms."

Kobler agrees: "The time will come over the next months where the higher risks will also be rewarded with higher returns." Timing is everything.



FAMILY OFFICES AND ESTATE PLANNING

Keeping It in the Family

In recent years, many banks, such as UBS, Credit Suisse and Citi, have launched dedicated family office business units; others, whether or not they have separate units, report an increase in the amount of business in this segment. It's no surprise: family wealth drives Asia.

In October, Credit Suisse launched a comprehensive study of family-owned companies. Everyone knows the heavyweights—the Mittals, the Tatas, the Samsungs, the members of Li Ka-Shing's family—but across Asia's ten major markets there are in fact more than 3,500 family-owned companies with a market capitalization of more than \$50 million. Of these, 1,279 of them have a market cap greater than \$500 million. All told, family businesses account for 34% of Asian nominal GDP and 32% of market capitalization, but in some markets that figure is far higher: for example, it is 83.2% of the Philippines market cap, and over 50% in both Singapore and South Korea.

"An interesting difference compared to Europe is that these are businesses that are relatively young," says Nannette Hechler-Fayd'herbe, head of global financial markets research for private banking at Credit Suisse. "38% of them were listed after 2000. Many of them are first-generation led, whereas in Europe there have usually been several generations. They are at the early stage of their life cycle compared to their peers in Europe." That in turn means more family office investment structures. "As family businesses grow and create wealth for the family, there is a movement toward a more professional investment approach as well. It goes hand in hand."

Naturally, this is closely linked to the succession theme. "Succession from one generation to the next will accelerate over the next decade," says Agnes Au-Yeung,

head of Family Wealth Advisory, HSBC Private Bank. "The new generation of family offices will have to adapt to the needs and values of the baby-boomer entrepreneurs, who cherish new ideas and values, and who are concerned about continuity and leaving a legacy."

Amy Lo, head of Ultra-High Net Worth for Asia Pacific at UBS Wealth Management, agrees: "One of the main reasons for the growing interest in family offices is generational transition," she says. "While



we see many family businesses being successfully handed over to the younger generation, some families decide to divest and continue the legacy in the form of investing in philanthropic activities thus transforming from a business family into a wealth management family, while staying entrepreneurial and continuing to look for new opportunities."

But it's not an area where many people appear satisfied with what they've done. A recent UBS Family Advisory study surveying 120 ultra-high-net-worth families globally found that 76% were concerned with protecting their wealth, but only 25% considered the way in which they approached the issue to be sufficient.

"Thirty-two percent said that lack of know-how was the biggest show-stopper in putting a structured approach to family wealth protection in place," says Lo. Good estate planning, she says, should both the senior and junior generations "in a dialogue about the core values of the family and what the family wants to achieve in the long run. Many families make the mistake of limiting their efforts to the legal structuring, while missing the point of the true reason of such a structure. Successful legacy building involves a clear long-term family strategy and thought-through governance system," which might include the drafting of a family constitution or the creation of a family council, she adds.

A Matter of Structure

A large part of family office advice is structural. "For those who want to get started, we help them with the structure and definition of governance," says Marcel Kreis, head of private banking for Asia Pacific at Credit Suisse. "That is crucial to the success of the operation. We discuss issues of legacy and asset protection, help them with the formulation of investment policy if that's required, and provide any financial services they need." Kreis's colleague, Hans-Ulrich Meister, CEO for global private banking, adds: "All over the world, with family offices, you have to push them on succession. If succession is not timely, you can lose everything you built up in the last 30 to 40 years. It is such an important part, especially in companies that might need years to prepare for a successful transition."

Naturally, investment advice is crucial, too. Banks report that with more formal structures, risk management becomes more sophisticated and time horizons for investment tend to grow—perhaps allowing people to invest in illiquid asset classes like infrastructure, which improve

diversification. That said, many family offices did lose a lot in the financial crisis from illiquid alternative investments. “From these lessons many families have started to define risk buckets,” says Au-Yeung. “They may set aside a bucket as a nest egg or a start-over-again fund, while managing another bucket with a higher risk level or a thematic focus so that the combined buckets meet the aggregate needs of the family.”

For banks, this is a growing business, as more and more institutions broaden from a traditional focus on investment management to a far more well-rounded sense of partnership with family wealth. “I look at the relationship manager as being a conductor, being able to play with a number of musicians,” says ABN Amro’s Delcourt at. “An orchestra without a conductor plays a cacophony. A conductor without musicians doesn’t entertain his audience. I believe in a private bank that is a partner to our clients—not only to advise on whether an investment should or should not be made, but to structure wealth in a way to achieve their objectives.

“The private banking model of the recent past in Asia was much more transaction-oriented,” he adds. “It still is, to a large extent. We ought to move to a more client service-based approach, and wealth structuring is a fundamental part of that advisory scope we need to provide.”

Family office structures can take a variety of forms, “ranging from a trusted assistant to a virtual family office managed by an ex-senior banker, and in more mature cases to an entity with an independent legal status and staffed by well-qualified professionals,” says Au-Yeung. Such professionals can be in high demand: Credit Suisse’s most significant private banking hire this year was Bernard Fung, who formerly managed the wealth of the U.K.’s Sainsbury family.

UBS’s Lo points out three separate types of family offices: First are the ultra-high-net-worth families in Hong Kong and Singapore that are sophisticated and have reached a natural point where it makes sense to separate business interests from financial assets. These use investment specialists who coordinate the sourcing and screening of investment opportunities. Then there are clients in China and India. “They are quickly picking up in terms

of professionalizing their wealth management and are very active in enhancing their knowledge as well as seeking ways of adapting the Western family office concept to their business-driven, high-growth environment,” says Lo.

“One of the main challenges for ultra-high-net-worth families in these countries is that most of the family wealth is tied to a family business. In such a situation, the first critical step in creating a family office usually lies in diversifying this concentration risk and adopting an asset-allocation approach to managing their wealth for the long term.” And the third group is European family offices establishing a presence in Asia in order to be in a better position to gain suitable exposure to the Asian growth story, typically through a Hong Kong or Singapore hub.

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HSBC Private Bank

Serving Family Clients

It can be a tricky market to service. “In our experience, single-family office clients require a much higher level of service and attention,” says Au-Yeung. HSBC services them through its HSBC Private Wealth Solutions business, which manages over US\$100 billion of these assets worldwide. “Family members can be quite hands-on, especially with investment decisions.”

And, of course, there is a common challenge for those in the family office business: “Our advisers need to continually validate our objectivity to client families. To assure their independence, our advisers are not incentivized by product sales nor measured by asset gathering.” And advice has to be customized—it’s not a

one-size-fits-all sort of market. According to Lo, “Due to the highly personal nature of the work, we have found that most families prefer to set up their own bespoke family office with a combination of their own trusted employees—who often have served the family business for many years—and external experts with specialist skills.” These include lawyers, accountants and tax advisors as well as investment professionals.

All this said, the family office industry is still in its infancy. “The family office is a relatively new concept, with many still studying, comparing, developing and evolving their models,” says Au-Yeung, who adds that family offices in Asia typically follow a U.S.- and European-style pattern. She says more and more families are using this approach, but says it is unclear how widespread they will become. “The definition is vague, and family offices tend to be very private,” she says. “We expect families to lean toward single-family offices as they prefer their affairs to be managed internally and separately from other wealthy families.”

Another common theme of family wealth management is the impact on the family itself. “As an administrative center supporting the family’s governance structure, the family office provides a unique platform to improve and promote communication and harmony among family members.” Perhaps this is one reason why multi-family office structures are relatively rare in Asia. But they do have some merit. “Rising costs, a difficult investment climate and a desire for a breadth of services tend to drive families to partner with larger multi-family offices,” says Au-Yeung. Lo says multi-family offices serve the needs of at most six or seven families; this sort of model is more common than third-party-owned commercial service providers branded as family offices (“multi-client family offices,” as Lo calls them), which can serve as many as 50 families—a model that is common in the U.S.

Overall, Asia is riding on a wave of new wealth generation and embracing a future full of possibility. Says Delcourt: “Europe has a tendency to look at tomorrow as a zone of risk. Asia has a tendency to look at tomorrow as a zone of opportunity.”

PHILANTHROPY

Philanthropy Turns Professional

Like family office structures, philanthropy is gaining momentum in Asia. “There are increased expectations of transparency and accountability, and evidence of social impact,” says Cynthia D’Anjou-Brown, senior philanthropy and governance advisor, HSBC Private Bank, which manages more than US\$1 billion in assets and handled US\$50 million of donations on behalf of clients in 2010. She says the definition of what constitutes philanthropy is broadening, from informal charity to structured grant-making to investments with social value. The young generation is having an impact here. “There appears to be a high engagement of donors at a younger age and a trend toward working with family members,” she says.

Philanthropy in Asia differs from the rest of the world in some crucial ways. For example, education plays a dominant role in giving programs. A recent study by UBS and INSEAD found that education is likely to account for 35% of giving in Asia in 2011; the next biggest cause—poverty alleviation—accounts for just 12%. “These are strong cultural roots that support education, tied to Confucian, Hindu and other Asian traditions,” says Jenny Santi of UBS Philanthropy Services. Many who have risen from poverty recall either their lack of education or being the first in their family to receive it. “One of the most deep-seated reflections they have is that they were deprived of a high-quality education, so they want to give back in that sector; or they recall that the only reason they were successful was because somebody gave them a handout and made a difference in their lives,” she says.

Other banks echo this: D’Anjou-Brown says nearly half of the donations HSBC administered on behalf of charitable trusts and foundations in Hong Kong between July 2010 and June 2011 were allocated to educational projects, com-

pared to one-fifth for social services and one-tenth for health and medical services. One can argue that the Asian cultural emphasis on family has an effect on the way people give. “In Asia the older dominant religions, the social structure of the clan and collectivism breed a culture of caring for the large extended family and community,” says D’Anjou-Brown.

The recent UBS study revealed that giving is chiefly domestic, although D’Anjou-Brown says there is a trend toward giving internationally—what she calls “diaspora giving.” In particular, she sees a growth in donations to mainland China.



As with estate planning, much of the important advice given around philanthropy is structural: choosing the legal entity for giving and ensuring it is properly set up in terms of succession, flexibility, tax advantages, liability, privacy and compliance. “A charitable trust or foundation managed by a professional or corporation trustee is an excellent choice because it provides better succession arrangements and needs not rely solely on individual directors, as in the case of a company,” says D’Anjou-Brown. It is vital to be clear on what a donor wants to achieve and how to measure it. Measurable results are an important focus in Asian giving.

The rise of governance also has an impact on philanthropy. CSR Asia, a

social enterprise that works to promote corporate social responsibility (CSR) across the Asia Pacific region, says that 87% of family businesses participate in CSR activities, though only 53% have a policy and 39% have clear CSR goals and targets.

Many banks report an increasing insistence on direct involvement in charitable initiatives. “Rather than ‘I donate so much to such-and-such an organization,’ people want to be able to help advise on a philanthropic project and get involved,” says Delcourt. “It’s not just about a financial return, but for people to get their own return—to see that what they do has a positive influence and a multiplying factor. We continue to support a number of institutions that are applying the private equity way of thinking to philanthropy.”

Growing Toward the Future

The Asia of today is a hotbed of wealth creation and private banking: It is certainly on track to become the number one market in the world based on a number of metrics, from total wealth to the total number of millionaires. Serving that wealth creates both a challenge and an opportunity. The coming years will be characterized by an increasing professional approach to wealth management, a growing appreciation of the need to make the transition between generations as seamless as possible, and investment that increasingly focuses on homegrown opportunity across Asia. ■

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