

DRIVING ENTERPRISE VALUE IN THE WEALTH MANAGEMENT MARKET THROUGH TECHNOLOGY OPTIMIZATION



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Executive Summary

Today's market realities require banks to think of new ways to create additional revenue streams to support their business growth objectives. Do these new revenue streams have to be new markets? With the diversity on offer by today's financial institutions, with as varied solutions as wealth management, insurance, mortgages, credit cards, and so forth, is not the answer perhaps already available within the enterprise? The notion of "Enterprise Value" drives the concept of satisfying the client's assorted financial needs by making available the required information and solutions to the client facing personnel of the organization. This capability can only happen, however, through a technology infrastructure that is built to provide such information. Delivering "Enterprise Value" to the client, then, is predicated on a thorough technology optimization to identify and correct limitations in the delivery of information and solutions to the client.

Enterprise Value: A New Paradigm in Driving Client Satisfaction

The Wealth Management industry has, since its inception, been focused primarily on delivering asset management solutions in the pursuit of satisfying clients' needs. This was due, in a large part, to the singular focus of the unit and its insular existence. Measures such as Assets Under Management (AUM) and Net New Money (NNM) are the key performance indicators that most firms use. In addition, a similarly narrow approach is taken when measuring the value of a client to the firm, as assets invested with the financial institution. But is this the appropriate way to look at the opportunity? As a quick definition, "Enterprise Value" is the notion of satisfying the client's financial needs across the full spectrum. By this definition, does an asset management's only view accomplish this, or are their other opportunities being left on the table?

Let us divide the two principal wealth groups as High Net Worth (HNI) and Mass Affluent (MA). For purposes of this dialogue, HNI will be \$5 million and above in investable assets. MA will be \$500,000 to \$5 million in investable assets as this seems to be the measures which most financial

institutions utilize. Ultra High Net Worth (UHNI) are generally categorized as individuals having \$25 million and above in investable assets. For purposes of this discussion, we will group HNI and UHNI together. We recognize they have very different needs and requirements, but we will simplify it for this conversation.

Changing Needs of the Mass Affluent Segment

Let's begin with the MA population. Diagram 1 demonstrates the full breadth of the financial needs of the MA client. It is noteworthy to point out that investments are actually down the priority list as compared to day-to-day budget concerns and healthcare. In addition, this segment is the least risky segment for both lending and insurance products. Their propensity to "move around equity" or more simply to use home equity loans and other such lending products to acquire secondary homes, automobiles or to fund their children's education, also makes them a good target for these other financial institution offerings. So, perhaps, instead of grouping the MA clients by AUM, a better measure may be net worth.

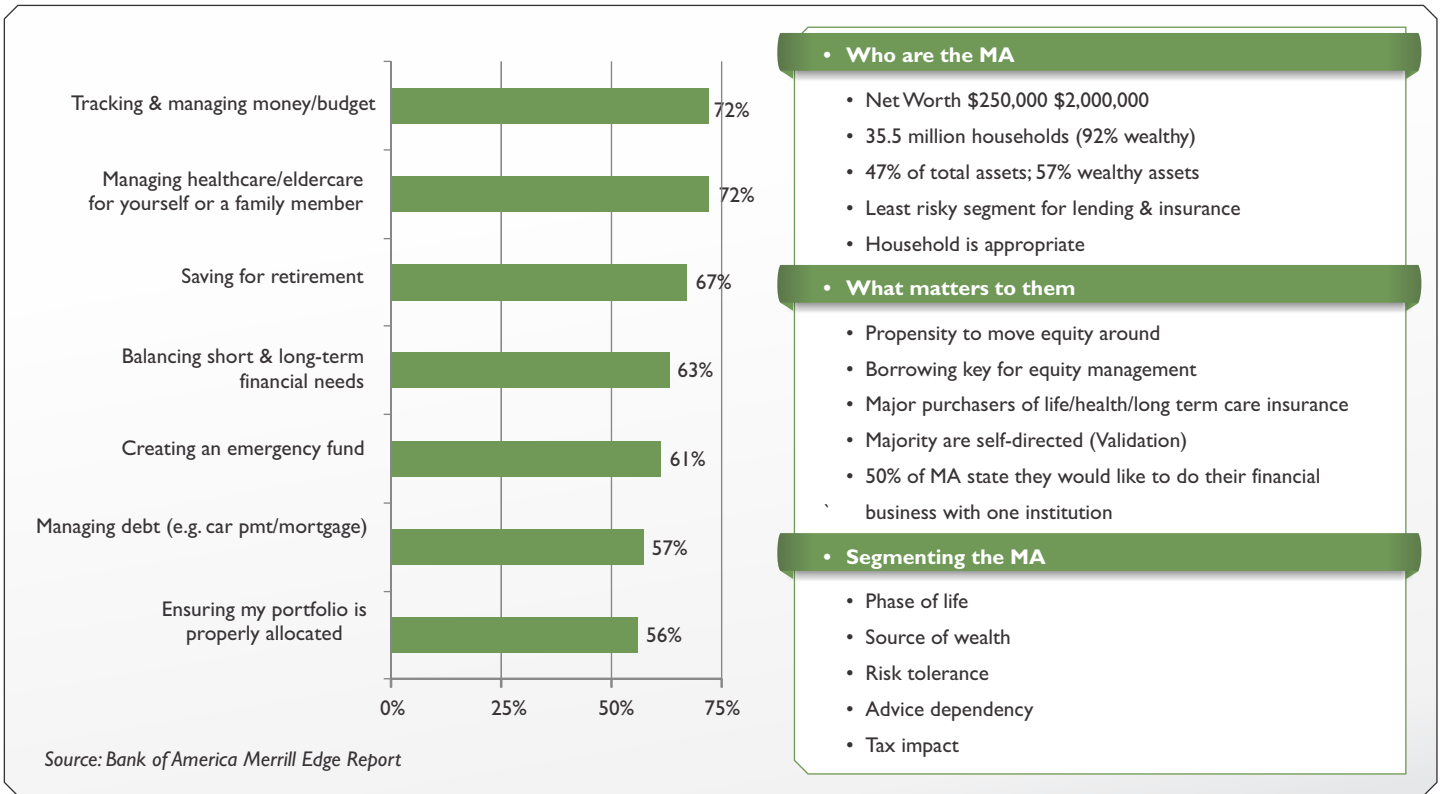


Diagram 1: Financial Priorities of the MA (US)

The reason to define the MA segment becomes even more readily clear in Diagram 2. The MA utilizes all of the products a financial institution has to offer.

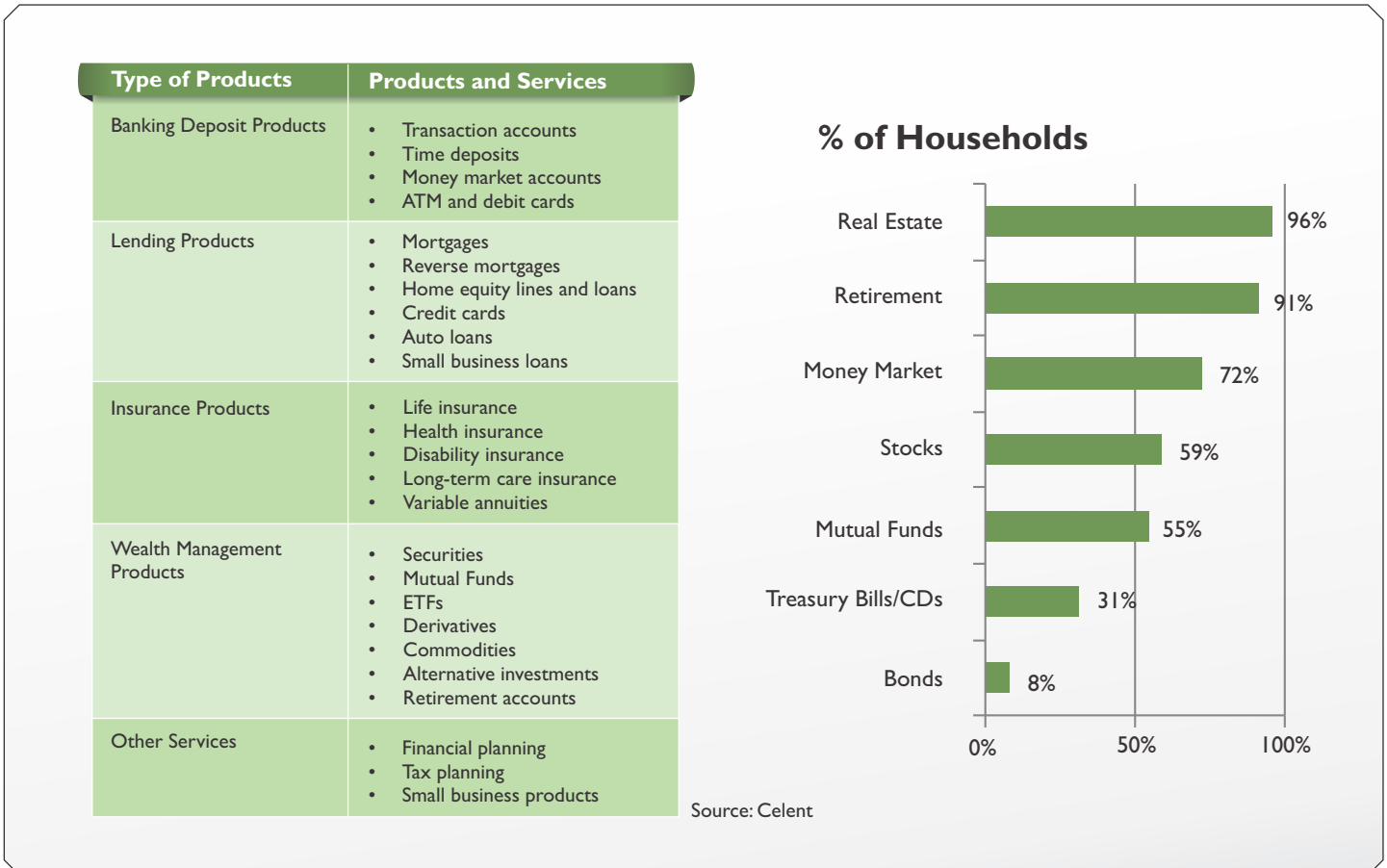


Diagram 2: Products and Services Utilized by the MA Customer (US)

What is even more encouraging is that 50% say that they would utilize just one financial institution for all of their needs if they felt they could find that one. In the Mass Affluent segment in the US as an example, the husband and wife are also more likely to act as a team, with each having their own career (and income) as well as a 401k plan. This then leads to capturing a net worth perspective, so that not only are assets factored in, but also the opportunity to sell insurance, mortgages and other lending and financial institution products.

From an asset management perspective, demographic changes and variations in wealth preferences are quite evident in many studies. In a changed and interlocked world, the wealthy are more willing to expose their assets to global market opportunities. Countries are increasingly adopting capital convertibility making money-flow between markets easier than ever. Though return on investment remains a critical consideration in choosing a wealth services provider, global access, reach and insights into cross border markets are driving competitive advantage. The ability to deal with global scale complexities is also reshaping the wealth management industry structure.

have the same need for insurance or lending products due to their wealth, although they may choose to leverage lending solutions for convenience or business needs. As a result, the wealth management industry has focused on asset management solutions and for the higher end market (UHNI), family office and other bespoke services. That being said, since the 2008 financial crisis, the concept of "Enterprise Value" has crept into the relationship with the HNI client, albeit with a slightly different flavor.

The recent World Wealth Report 2011, from Merrill Lynch and Capgemini, showed the top six priorities of the high net worth client per Diagram 3, and then added two additional: alternate communication channels and succession planning.

To be sure, a quick glance would put these in the category of satisfying needs through an asset management solution, but a deeper understanding is required. As pointed out in the Global Wealth Report, in addition to more transparency of fees and a deeper understanding of the ramifications of the investment programs put in front of them, the HNI client expects alternate investment solutions, previously provided only to

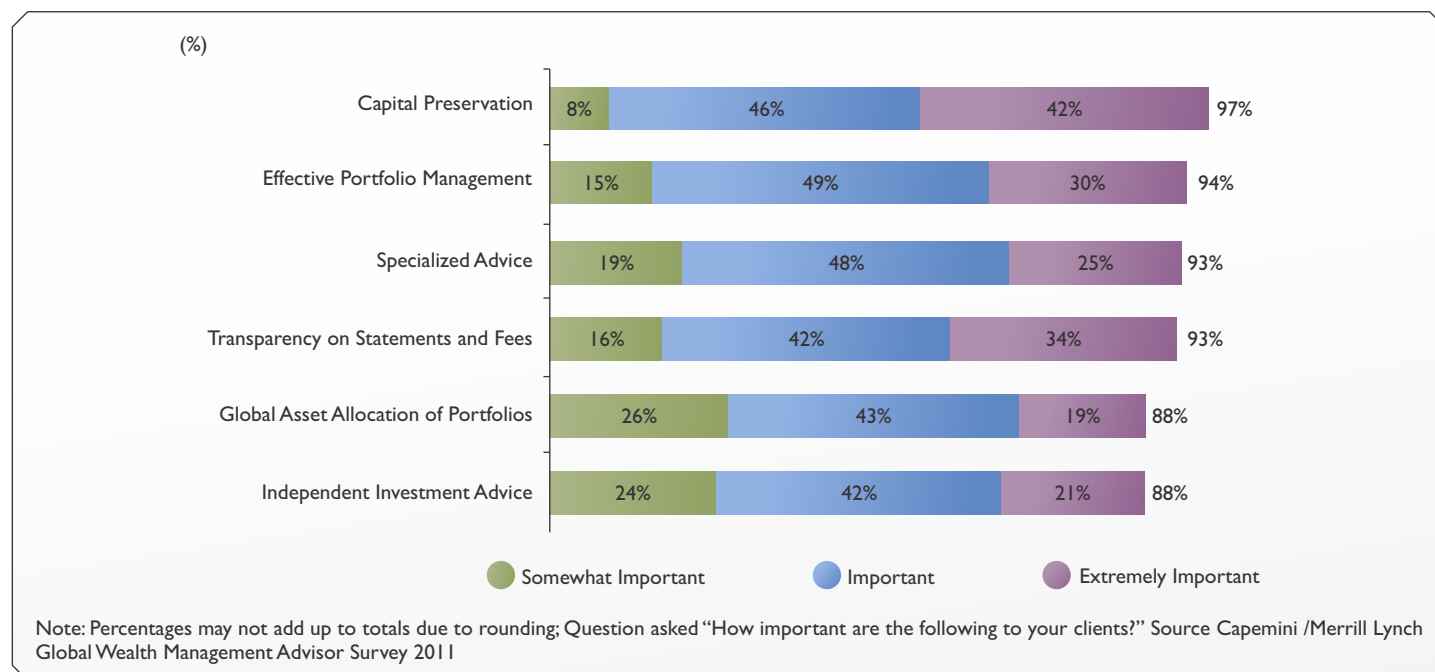


Diagram 3: Top Six Priorities of HNI Clients, 2010

Is It Only about Asset Management for the High Net Worth Client?

The high net worth client follows a slightly different pattern. They do not

institutional clients, like special IPO opportunities, to be availed. In addition, special lending rates for entrepreneurial and other business ventures are sought, as they expect their financial institution to be more of a partner than merely an expense. Finally, they expect the financial institution to meet them in the communication channel that is most

convenient for them (the HNI client), be it face to face or virtual through any number of channels such as in the office/home, Internet, or mobile.

Can we consider HNI as a single homogeneous segment and create products and services based on that assumption? Service providers are increasingly made aware of the fact that within the broader category of HNI, there are various sub segments which bases its decision to invest in an asset class based on different local and global considerations. An individual who builds his or her assets based on the professional job he or she holds may have a very different outlook from the person who is running a small and medium size business. Though this difference exists, what we are seeing in the market place is that the world is increasingly adapting multiple channels for their communication.

Asian Story – Changing the dynamics for global wealth service providers

One such example of the changing dynamics is what is happening in Asia. Gordon Percthold, in his study on changing dynamics of the Asian wealth management industry "A Perspective on Demographics: Income: Needs for Retail Financial Services" notes some of the interesting trends. In the research findings, he documents that the demographic diversity of population across Asia is quite high and makes it difficult to define a common business approach for retail financial services including mass affluence based wealth advisory. This fact is further supported by the study conducted by Accenture and Capco Research Institute. It is interesting to note that over 300 million people in the developing nations characterized by youthful or adult demographics are moving across the economic threshold to become viable consumers for wealth management products and services. Overall it is expected that ongoing economic growth in Asia will further enhance business opportunities for global service providers that build on their core business of finding superior returns on investments for investors and remain focused on effective execution of asset allocation strategies.

However, these shifts in dynamics are posing a different set of questions. Questions pertaining to how to make global systems that address local variances, particularly around regulatory and market practice considerations, are having far reaching implications on IT in managing and supporting the business. Building a standardized platform to provide effectiveness and cost advantage may not necessarily be in line with demographic variances that exist in the Asian markets. Localization of global applications needs to consider the demographic realities required to

build the agile IT infrastructure to support business expansion by global majors. The Asia market is an example of the challenges posed by the current ever changing regulatory environment the wealth management market is facing globally requiring extremely agile IT infrastructure to address local differences.

Importance of Technology in Driving Enterprise Value

The definition of "wallet share" has changed. No longer is it just share of the investable assets wallet, but a share of the financial services wallet. Retail wealth clients are expecting services to be provided both from traditional banking solutions (asset management, lending, insurance, and banking) and now, increasingly, nontraditional or institutional solutions (IPO and other alternative asset management and lending solutions) through a single point of contact. From an asset management product development perspective, what we are increasingly seeing is a shifting preference from return generation to asset preservation and creation. This is a game changing trend which has yet to be deeply understood by the wealth services providers. These types of asset products require a very different business outlook resulting in different thinking for technology adaption to enable this more conservative approach.



Technology clearly has a role to play here. Traditionally, the Chinese walls established in the financial institution, be it due to the functional limitations of the organization or, more likely, the technological limitations of the applications and infrastructure utilized by client facing personnel, have made it virtually impossible for a full grasp of the value of the client to the organization. If a person had investments, bank products (checking and saving accounts), credit cards, and loan products (mortgages, home equity loans and/or auto loans) they were treated like four or more different people to the bank versus a single client. They would get multiple statements; from multiple “advisors” all working at cross purpose within their corner of the world. What’s worse, the incentive plans and technology infrastructure encouraged and solidified this mindset. Little did the financial institution realize that the slightest mistreatment by one of these areas would put at risk all of the other, and likely, more profitable relationships with this client. To the client, it was always one financial institution. “Enterprise Value” now enables the financial institution to recognize what the client has known all along, there is only one client, and he is dealing with only one financial institution.

Process, People, then Technology

Applying technology to the issues blocking a financial institution’s ability to achieve enterprise value is not just about speed. Building technology on unstable or incongruous business processes only delivers bad information faster. Given how long many of the legacy platforms, and underlying business processes have been in place, it is necessary before any technology optimization begins, that an examination of basics: process, people, then technology be completed.

The end goal for the service provider remains the same, i.e. superior service and return in fulfilling the client’s needs. However, the process of doing business has continuously changed reflecting the ever morphing business realities. Client decisions are made not only based on what a wealth advisor has suggested but through external validation of these proposals via social networks. HNIs are increasingly comfortable using social networks to validate an investment idea and often seek free advice from their business associates. It is naive to think that the client will have a single advisor relationship for all of his or her needs. Increasingly, the industry is accepting the fact that it is a multi-advisor scenario for a client to

make the right decisions. The loyalty of the client has to be earned every day in this context.

The business processes must be examined to ensure that they are maximizing along four key considerations: client experience, revenue generation, risk mitigation and cost efficiency. How many steps in the process are there because of the limitations of the current technology? How many Excel spreadsheets or Access databases have been institutionalized to lock down manual processes? How many data sources are there for the same data? Are any correct? Are there ways to build in new revenue opportunities? Before any technology optimization is performed, it is vital to get the underlying business processes right first. After the process is proven to be scalable, efficient and optimized for revenue opportunities while mitigating risk, then figure out operationally, from the front office through to the back office how to apply personnel. Finally, add technology to increase throughput and overall efficiency while mitigating risk.

Client Intimacy vs. Revenue Generation vs. Risk Mitigation vs. Operational Efficiency: Do they have to be Mutually Exclusive?

Traditionally, many people have labeled a project as one of these categories to the exclusion of the others. If there was a secondary benefit, it was more by accident than by design. Organizations would look for technologies to cut costs in the back office, or ways to provide the client facing personnel a new way to provide alternative asset management solutions to their wealth management clients or new technologies that a client can use to become more familiar with products the financial institution has on offer.

Using enterprise value as a guidepost should help drive the four standards in the same direction. Enterprise value is about providing the client what he needs to satisfy his financial service requirements, despite what part of the financial institution it may come from. It drives revenue generation as it redefines the definition of wallet share and broadens it to include solutions traditionally outside of the scope. In order to achieve enterprise value, it will require a new and broader understanding of the client on a

cross-enterprise basis, and so will require a total re-examination of data flow across the firm. This more complete client information should reduce risk and drive processes that can be optimized through a technology optimization program that will drive operational efficiency, but more importantly, enterprise efficiency.

Building a Responsive Technology Landscape via Technology Optimization and Integration

Global wealth management functions can be divided into four important processes – front office, middle office, back office and support functions. Front office focuses primarily on client relationship management and enabling advisory and sales. Middle office functions focus on product and advisory strategies, research, asset allocation and rebalancing of portfolios in addition to investment proposal creation. Back office is built to enable transaction processing, clearing and settlement, custody, reference and other key data handling and client reporting. In addition to these three distinct blocks of the wealth management business, a firm will have support functions such as finance, human resource management and administration. One look at the cost structure of doing business, front office constitutes about 37%, middle office is about 13%, back office is about 32% and 18% will belong to support functions (author's assessment as indicated by diverse research findings).

It is the industry view that inadequate support from back office has been the reason for frequent client churn. From the back office perspective, it is the outcome of inadequate investment and support to the initiatives of modernizing back office IT systems. Even today, the IT landscapes supporting the wealth management business reflects non-standardized applications and a lack of integration and seamless message flows. It is not

surprising that leading service providers often find it difficult to believe some of their own data and information provided by these systems. Often client and their investment data attributes are maintained in different systems and databases, resulting in non-synchronized interest and cash flow calculations, as an example. Manual intervention to reconcile the data has often been the source of inaccuracies. It is difficult to say how much integration the industry has achieved to build Straight Through Processing (STP) from front through the back office. Considering the disperse approach of building different IT infrastructure between front, middle and back office historically, it is difficult to now take a view on how to streamline the IT functions without causing some service level issues to the business.

Historically within the wealth management service providers, IT functions reflected the myopic view of creating non-synchronized structure to support the business. Front office in general has been built on third party applications; while middle is a mix of third party applications and custom built. Back office is primarily created over gradual custom built applications on nonstandard architecture. To respond to new business events and opportunities or regulatory requirements, additional applications were bought or built.

The counter parts of the wealth management service providers, such as investment banks, have adopted smart sourcing as a way to outsource large parts of non-core activities to third parties. The wealth management infrastructure, however, remains largely in house resulting in a significant fixed cost structure. Though this was not a major issue in the boom era of 1995-2005, changed economic realities have started impacting the ability of wealth advisors to gain higher fees for their services. Rapid adaptations of technology by client segments have often left advisors feeling inadequate to service their ever demanding client segment. The reality of a slowdown in NNM flows, lower return product mix due to client wealth safety concerns and increasing pressure on maintaining healthy margins all



are creating new thinking in building IT infrastructure to support the business.

In this context, the reaction of the CIO organization within the enterprise is to go back to the drawing board to re-think IT strategies. In our view, the following questions need to guide the strategy of recreating a blue print for IT

Question 1: How do I regain client trust?: Client trust has two important dimensions – the first one is purely business. It depends on how well a wealth advisor can create above average return on their investment consistently and in a predictable manner. Secondly; how transparent have wealth advisors been in dealing with complex investment advice to their wealthy client segments? IT has significant impact enabling better answers on these dimensions. The first dimension is linked to the firm's ability to convert abundant data flows into meaningful decision creating information. Innovative technologies like Big Data Analytics can synthesize vast amounts of data for true cross enterprise 360 degree client views and portfolio performance analytics creating better client interaction levels. A non-synchronized front, middle and back office is of little help. Since key information resides both internally and externally, new generation wealth advisory service organizations need to build IT structures by questioning fundamental industry building blocks.

The second dimension of the question is all about making accurate information available to wealth advisors on a real time, any place basis. Not having a 360 degree view of all client information is a huge hindrance in effective communication between a wealth advisor and his/her client. Credibility and accuracy of information is the first requirement in establishing client intimacy and needs to be taken into consideration. If the objective is to provide a 360 degree view of a client for the advisor; a siloed approach of front, middle and back office will not help. Though a vertical structure can be retained to some extent, a great degree of importance exists in breaking the barriers. In addition to the data rationalization, alternative communication channels, such as mobile and social media alternatives, are a means to robustly address this need.

Question 2: A CIO organization needs to ask the question how variabilizing the fixed cost structure to support the business can be accomplished without compromising the quality of service to the business? Rebuilding the IT infrastructure to support the business can be based on the 'smart sourcing' principles. An enterprise needs to ask the fundamental

questions on what component does not constitute the core business. If advisory is the core, then providing the ability to gather information can be defined as non-core. Data gathering is an input to the process rather than the outcome. Defining the 'input' and 'outcome' activities across key building blocks can provide greater insight into how 'smart sourcing' strategies can be adapted to variabilize the fixed cost structure in supporting the business. For the wealth management industry, there is significant opportunity to break the barriers, build industry responsive IT structure and enable wealth advisors to provide industry differentiated products and service to their clients. Cloud technology, as a means to drive efficiency, cost reduction and better service levels, should be a consideration when looking to address current infrastructure limitations.

Way Forward

It is difficult to envisage the industry structure remaining the same. The Global Wealth Management Business is facing serious questions about its credibility. Increasing adaptation of self-servicing systems are creating environments of disintermediation within the industry. More than ever, in today's context, a wealth advisor has to justify his reason for existence on an everyday basis.

Building a responsive next generation IT structure to support the day to day existence of a Wealth Advisor can provide much needed competitive differentiation for the service providers.

In conclusion, it is imperative for the industry to re-think their IT strategies. Breaking the barriers, consolidating multiple applications and rationalizing the IT infrastructure are all means of achieving a higher order of customer service and provide above average returns to their investments. It is important to align the IT structure to the "new normal" realities of multi-advisor relations, growing influence of social media resulting in an adaptive and sophisticated customer base asking for more at the same price or less.

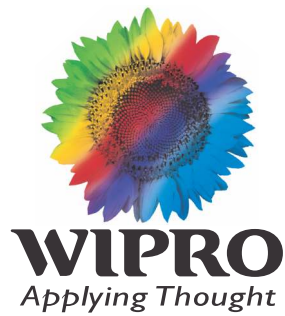
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