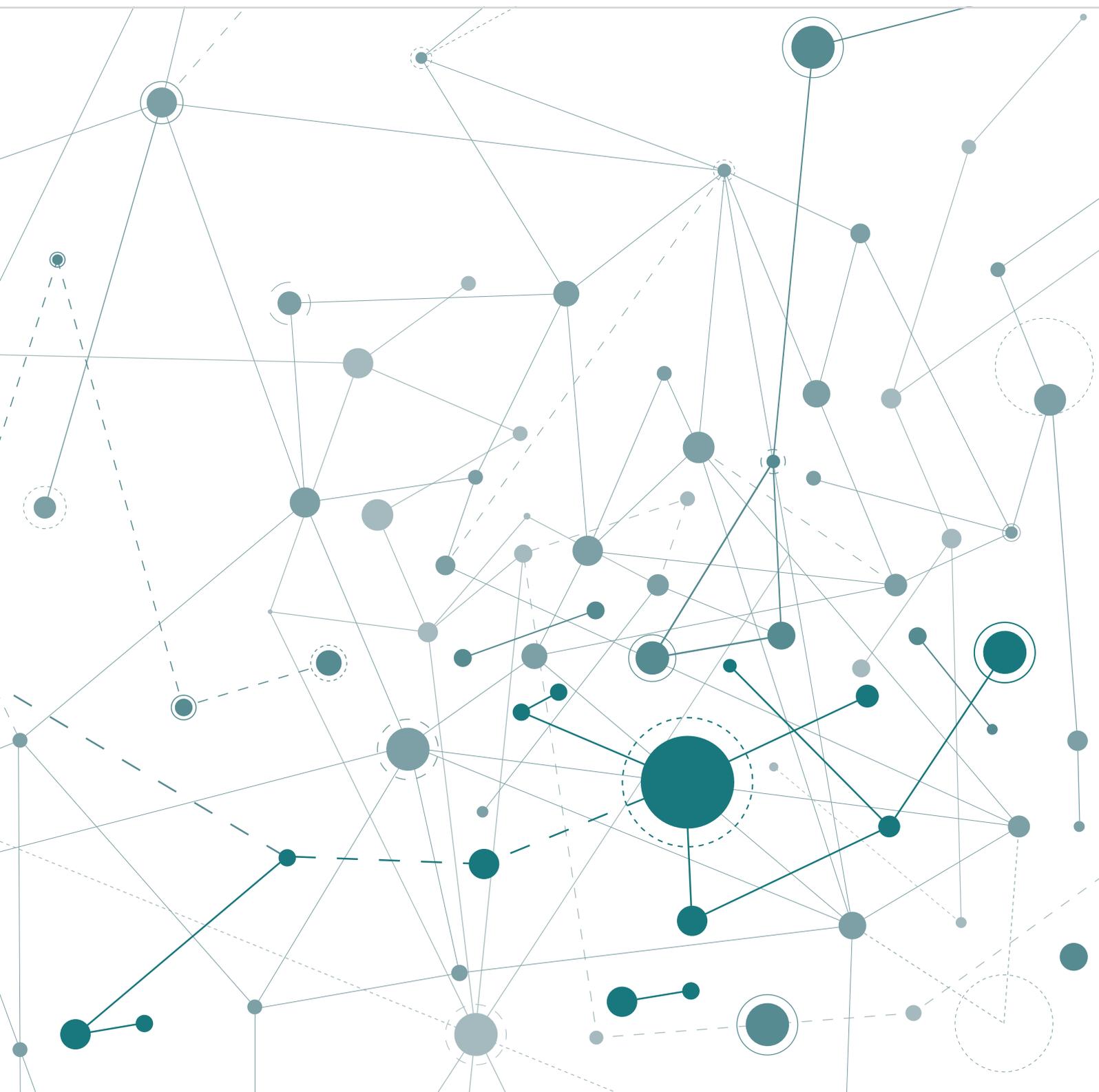


# LGT Private Banking Report 2018

## Key findings

Prof. Teodoro D. Cocca, Department of Finance, Johannes Kepler University Linz

Commissioned by LGT



## LGT Private Banking Report 2018

A survey of the investment behavior of high-net-worth private individuals in Germany, Austria and Switzerland

Commissioned by



**Private  
Banking**

### **Credits**

#### **Publisher**

LGT Group Foundation, Vaduz, [www.lgt.com](http://www.lgt.com)

#### **Author**

Prof. Teodoro D. Cocca, Department of Finance, Johannes Kepler University Linz,  
[www.ibfw.jku.at](http://www.ibfw.jku.at)

#### **Methodological consulting, data analysis and survey coordination**

Jörg Schneider, [js\\_studien+analysen](mailto:js_studien+analysen), Zurich, [js@js-studien-analysen.ch](mailto:js@js-studien-analysen.ch)

#### **Layout**

LGT Marketing & Communications, Vaduz

#### **Printer**

BVD Druck+Verlag AG, Schaan  
Print run 300 copies

© LGT and Prof. Teodoro D. Cocca

## High-net-worth clients caught in a conflict between markets, regulation and digitalization

**The Department of Asset Management at the Johannes Kepler University in Linz was this year commissioned for the fifth time by LGT to research the investment behavior of private banking clients in Germany, Austria and Switzerland. A representative number of high-net-worth investors was surveyed to this end in early 2018 (156 in Switzerland, 104 in Austria and 100 in Germany).**

The survey allows for both an in-depth analysis of the behavioral patterns of private banking clients at a specific point in time, as well as a comparison over the period spanning from 2010 until 2018. The current market cycle, which began in 2009 at the height of the financial crisis, can therefore be tracked over this entire period.

Although markets have developed positively, in particular over the last two years, there is no indication of a euphoric sentiment among the private banking clients surveyed in Germany, Austria and Switzerland: compared to 2016, the average asset allocation has remained largely unchanged. The share of assets invested in equities, which can be an indicator of investors' risk appetite, remains practically the same.

The respondents' subjective perception of the risks associated with various asset classes is also subject to cyclical fluctuations and is influenced by market events as well as the respondents' personal experiences. Similar to asset allocation, however, almost no changes were identified here in comparison to 2016. Their assessment of the risks associated with equities in particular remains constant. Only the subjective risk associated with bonds is seen as being slightly higher. This is noteworthy because according to the traditional classification of asset classes, equities are deemed a risky and bonds a less risky investment. It is possible that the respondents' perceptions reflect a fear of price corrections in the bond segment resulting from a possible end to the low interest rate environment.

### **Domestic equities popular**

Many studies show that investors have a strong "home market orientation". This refers to the tendency of investors to invest their money in domestic stocks. The private banking clients surveyed for this report are no exception to this phenomenon: they also hold a disproportionate amount of domestic equities and systematically categorize the risks associated with these stocks as lower than for foreign equities. This home market orientation is strong in all of the groups surveyed – irrespective of whether investors make investment decisions primarily based on the advice of their relationship manager or they tend to make investment decisions independently. One would expect the portfolios of respondents who primarily rely on the advice of their relationship manager to be more broadly diversified in geographic terms, but this is not the case. Although broad diversification is a proven and important factor for good investment performance, the clients tend to "put all of their eggs in one basket" and focus on equities in their geographic proximity, which are better-known to them and thought to be easier to monitor.

Generally speaking, it can be ascertained that investors are also not targeting broad diversification across different asset classes, or that this is still not taking place. Asset classes such as funds, derivatives and commodities in particular are not widely held. Similar to foreign equities, the respondents categorize hedge funds and private equity as very risky.

This provides a clear overall picture in terms of asset allocation: the large majority of investors continues to limit itself to the three traditional asset classes cash, equities and bonds. Compared to 2016, the level of diversification for a large number of portfolios has actually slightly decreased. Of note is that those respondents who categorize themselves as being particularly risk averse are even less diversified than those who categorize themselves as being prepared to take risks. It would appear that the risk-mitigating effects of portfolio diversification resulting from the fact that returns for the various asset classes are not correlated and can therefore offset each other is hardly taken into consideration.

However, for advisory services, there is one positive effect that can be identified in this area: investors who reach their investment decisions together with their relationship manager better spread their investments across the various asset classes than investors who make the majority of investment decisions independently.

### **Investors cautious**

Although the positive market environment of the last few years has not resulted in investor euphoria, there are nevertheless traces thereof in their attitudes and views. For example, a significant share of respondents is of the opinion that there are no alternatives to equities in the current environment. The share of clients who are of this opinion has risen compared to 2016. At the same time, however, many respondents also feel that equities are currently overvalued. It would appear that investors currently see themselves as faced with an inner conflict and are therefore cautious. This is also reflected in their limited readiness to reduce cash holdings in the future and invest them. Private banking clients do not appear to be adjusting their investment behavior in line with market sentiment during the current investment cycle.

### **Attitude to risk dominates**

Whether private banking clients see themselves as willing to take risks or as risk-averse has a big impact on their preferences and their investment behavior. The data collected clearly substantiate this. For example, a strong correlation exists between individual risk appetite and asset allocation.

Respondents who are willing to take risks have lower cash and bond holdings, but larger equity positions. Individual risk appetite can also explain a number of other differences in investment behavior. It is therefore more than justified that as part of the investment process, banks pay particular attention to a client's attitude toward risk.

However, the data also clearly show that clients' attitudes toward risk are not always in line with their portfolio composition. Around half of the respondents have a clear mismatch between their individual risk appetite and the subjective perception of the level of risk in their portfolio. Both in theory and in practice, a risk-averse investor should have a low-risk portfolio, and an investor who is willing to take risks should have a portfolio with a higher level of risk. In other words, there should be a match between portfolio risk and risk appetite. However, the sample contains numerous risk-averse clients with a high-risk portfolio and vice versa. It would therefore appear that the client risk classification conducted as part of the advisory process does not function optimally.

The mismatch could, however, also be the result of the difference in how risk is perceived by a relationship manager and by a client. As a result of his or her traditional financial training, a relationship manager might categorize the risks associated with bonds as being lower, while the client might have an entirely different perception thereof. Greater attention should therefore be paid to these subjective differences when it comes to assessing risks. One positive aspect in this area is that, compared to the 2016 study, the share of mismatches is substantially lower – particularly for the group of clients who are risk-averse.

#### **Is it possible to beat the market?**

The extent to which it is possible to generate excess returns on the stock market without having to take on additional risk is a question that has been hotly debated for decades, both in theory and in practice. So how do investors view this question?

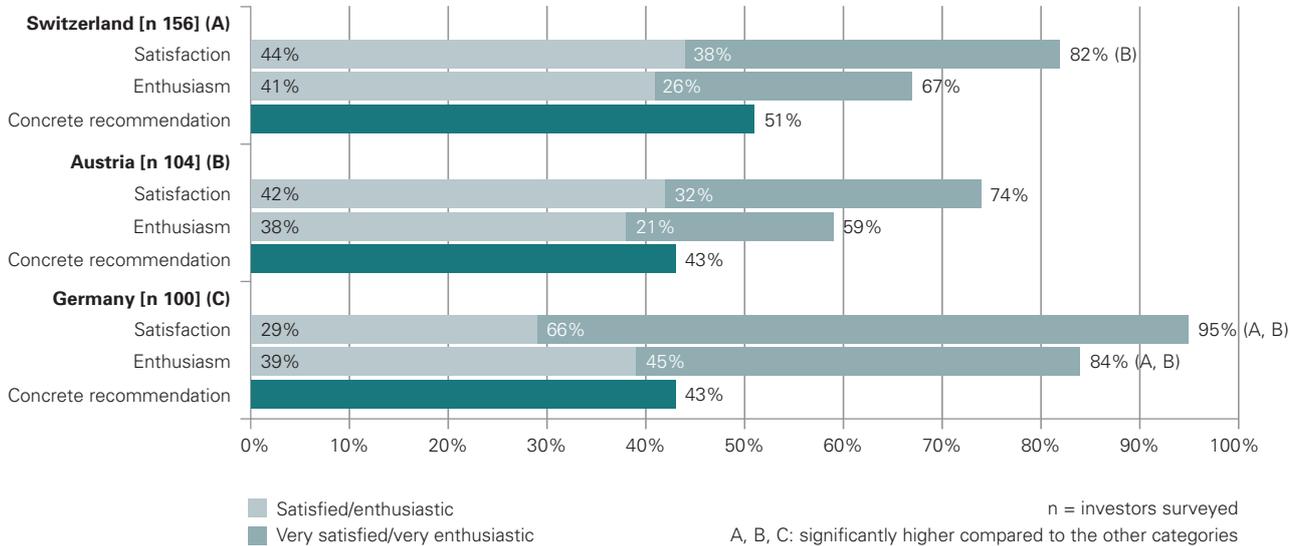
A comparison between the three countries highlights significant differences in this area. While the respondents in Switzerland and Austria believe in market efficiency and are of the opinion that it is not possible to “beat the market”, the German clients tend not to believe in the efficiency of markets. Clients of private banks in particular (and to a lesser extent clients of big banks) are of the opinion that it is possible to generate an excess return vis-à-vis the benchmark (“inefficient market”). Clients with an appetite for risk and respondents whose primary objective is to appreciate their capital are also not overly convinced of efficient markets and therefore assume that it is possible to generate excess returns without additional risk.

#### **Clients satisfied but critical**

The satisfaction levels of private banking clients with their primary bank can be described as good to very good (see Figure 1). Healthy market returns and the recent, positive market sentiment mentioned previously have contributed to this. Compared to the survey conducted in 2016, the levels of satisfaction and enthusiasm remain essentially unchanged for all three countries. The recommendation rate, which is very important in private banking, has generally remained high and constant over the years.

**Figure 1: Satisfaction, enthusiasm and recommendations (country comparison)**

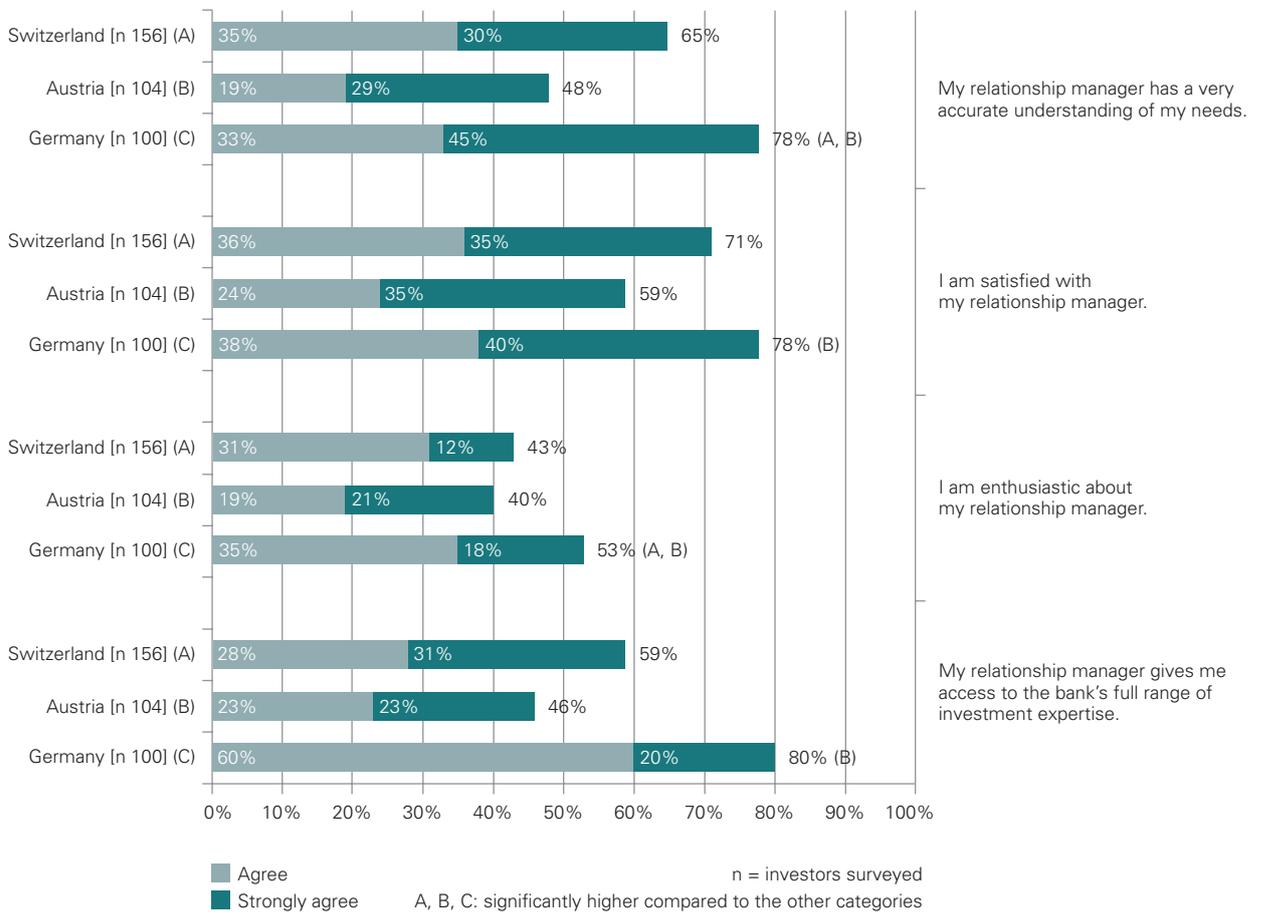
The respondents' general level of satisfaction with their primary bank depicted in this figure reflects the answers "satisfied" to "very satisfied"; enthusiasm, reflects the sum of the answers "enthusiastic" and "very enthusiastic". In order to understand not only sentiment, but to also validate this on the basis of concrete actions, respondents were asked about making concrete recommendations to others as regards their primary bank.



The picture that emerges when asked about the level of satisfaction not with their bank, but their relationship manager, is similarly positive – with minor exceptions. Although less than half of private banking clients are enthusiastic about their relationship manager, the overall assessment of relationship managers is good. The aspects "understands needs" and "access to investment expertise" (see Figure 2) in particular met with a high level of agreement.

**Figure 2: Assessment of relationship manager (country comparison)**

Substantial differences in how relationship managers are assessed can be observed primarily between Austria and Germany. Austrian respondents are significantly less positive with regard to how they categorize their relationship managers in terms of "understands needs" and "access to investment expertise", which also results in significantly lower satisfaction and enthusiasm levels.



However, there nevertheless appears to be latent potential for dissatisfaction concealed behind these results. If more than one-quarter of the clients surveyed are dissatisfied with the bank, relationship manager or both, it means that substantial retention risk exists. A certain amount of skepticism can also be identified among clients based on the fact that around two-thirds of respondents is of the opinion that banks are primarily focused on their own interests and not the interests of the clients. This perception, whether justified or not, is relevant and should be addressed by financial institutions.

Notwithstanding these in part critical assessments, as in the 2016 survey, there is no indication of a further shift away from relationship managers: this trend observed between 2009 and 2013 in the immediate wake of the financial crisis has, at least in Switzerland and Germany, not continued. Clients who are independent and make their own decisions remain a relevant segment. However, contrary to numerous predictions, the majority of clients does not appear to want to act more independently, even after the financial crisis. Instead, they would like to receive even more personal advice in the future. Only a small share of respondents is considering whether a relationship manager will still be needed in the future. The majority of clients wants to continue to reach all investment decisions in consultation with their relationship manager. Clients explicitly desire a greater number of personal advisory discussions. This may seem astounding in the age of digitalization, but ultimately, it is likely an accurate description of the private banking client segment. The average number of respondents' annual interactions with their bank is approximately 16, of which around two in Switzerland, three in Austria and four in Germany are personal discussions. This appears to be too few for these clients.

#### **What is more important: the bank or the relationship manager?**

Close personal contact is key for client loyalty. Loyalty to the relationship manager or the bank is stronger in particular when a client achieves above-average returns with a good price-performance ratio. Further to this, when it comes to client loyalty, loyalty to the bank is ultimately more important than loyalty to the relationship manager in all three countries.

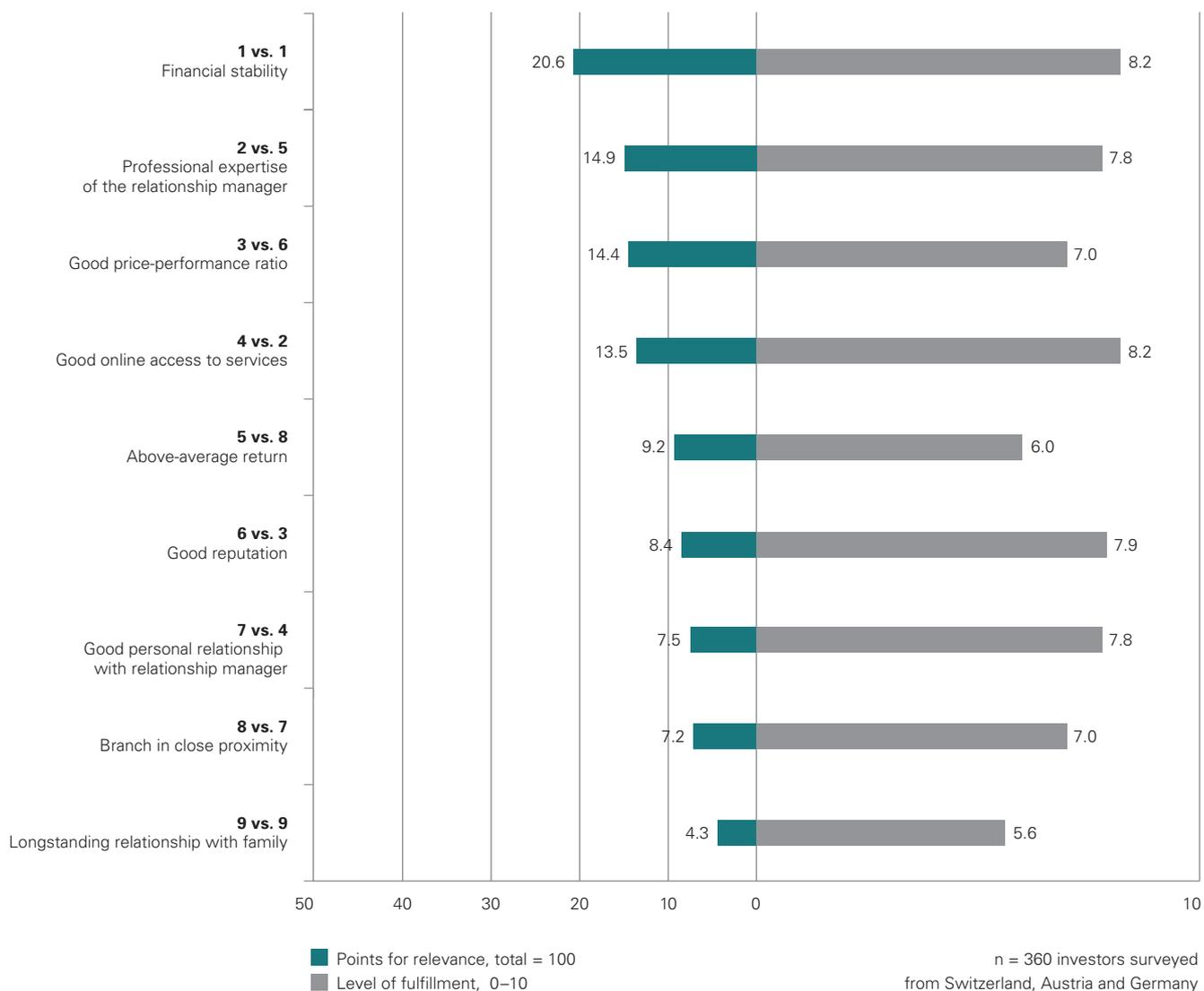
From a client perspective, the financial stability of a bank is the most relevant characteristic when choosing a primary bank for wealth management (see Figure 3). Having a branch in close proximity does not appear to be particularly important. Instead, greater importance is attributed to online access to banking services. This highlights the relevance of technological developments, at least in certain areas.

In order to increase client loyalty, banks should maintain and strengthen the interaction and performance-related aspects that are considered by clients to be of particular relevance.

**Figure 3: Characteristics attributable to banks – relevance ranking and level of fulfillment**

The respondents were asked to allocate 100 points to various characteristics attributable to banks as a means of expressing their personal preferences (a large number of points means that the corresponding characteristic has a high level of relevance). A comparison of the relevance of the characteristic with the level of fulfillment of the criteria in question is provided on the right-hand side of the figure (on a scale of 0 to 10).

**Ranking: Relevance vs. fulfillment**



**Adjustment to new framework conditions**

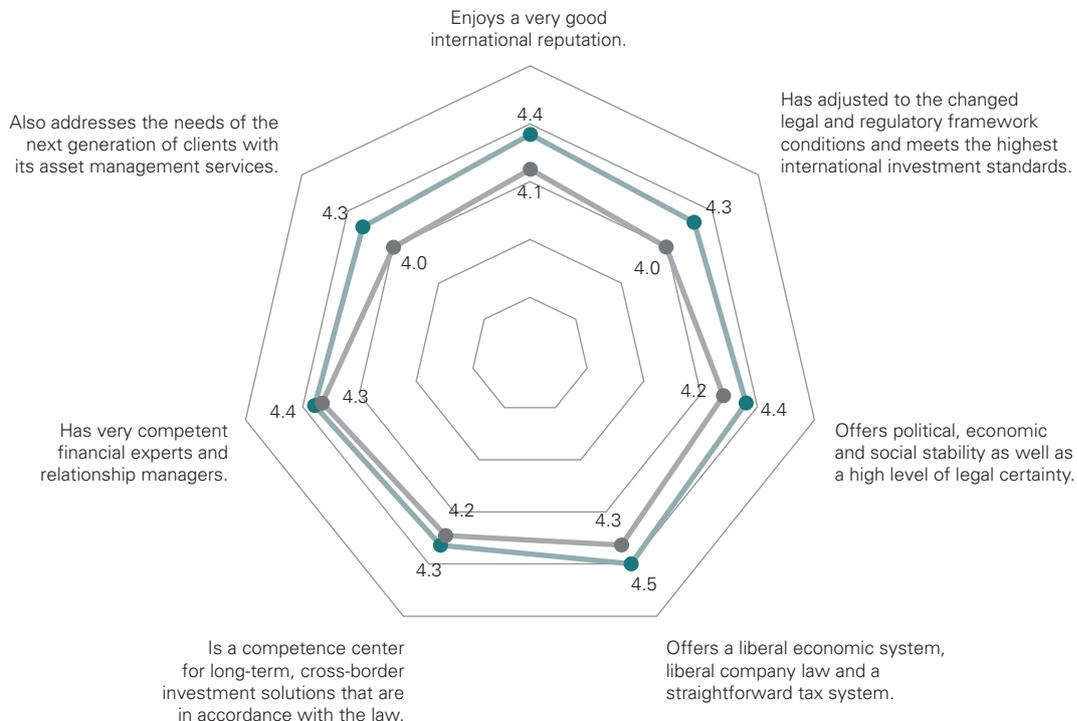
The greater investor protection and stricter banking regulation that have emerged since the financial crisis have had a strong impact on the client business. The legal and regulatory framework conditions for cross-border private banking have also undergone a significant transformation and created a new environment – some of the key drivers behind this are the weakening of bank-client confidentiality as well as the Automatic Exchange of Information (AEOI). Although these issues are being intensely discussed by experts, little systematic information is being collected in terms of how clients perceive them.

The information contained in this study allows for certain statements to be made regarding tendencies in this area: private banking clients generally have mixed feelings about the supposed improvement of investor protection through stricter regulation. However, significant differences can be identified here, particularly in a country comparison: while the majority of German respondents feel they are now more protected, only half of Swiss and a fraction of Austrians share this view. The Swiss are particularly critical of the increased administrative burden arising from this regulation – the German respondents, in contrast, would like to see more regulation.

An assessment of various financial centers also makes it possible to draw conclusions from the survey about which characteristics are currently relevant in cross-border private banking. This assessment confirms the theory that as a result of the harmonization of the regulatory and legal framework conditions for cross-border private banking, competition between the financial centers is now increasingly taking place in terms of the differences that exist in services and expertise. The assessment “Has adjusted to the changed legal and regulatory framework conditions and meets the highest international investment standards.” that German respondents attribute to both the Swiss and Liechtenstein financial centers (see Figure 4) is further confirmation of the financial sector’s transformation. Younger respondents in particular appear to have a high propensity to invest money in neighboring foreign financial centers even under the new framework conditions – a highly relevant finding for these financial centers.

**Figure 4: Comparison of assessments of the Swiss and Liechtenstein financial centers (German respondents)**

The German respondents were asked to rank the Swiss and Liechtenstein financial centers according to various criteria on a scale of 1 (is not consistent with the financial center) to 5 (is very consistent with the financial center). Depicted is the scale range from 2.5 to 5.



- Swiss financial center
- Liechtenstein financial center

n = 100 investors surveyed in Germany

**Rating scale from**

1 = is not consistent with the financial center to 5 = is very consistent with the financial center, scale range depicted 2.5 to 5

### Women more convinced about sustainability

The terms “sustainability” and “sustainable investments” are enjoying increasing popularity with investors, but to some extent still remain unclear. Generally speaking, the term sustainability can be broken down into environmental, social and ethical aspects. Respondents’ consideration for these aspects when making investment decisions is of particular interest.

Significant differences can be identified here in a country comparison. Especially German respondents show a strong affinity for this matter and much more frequently indicate that they have in fact taken sustainability criteria into consideration when making investment decisions.

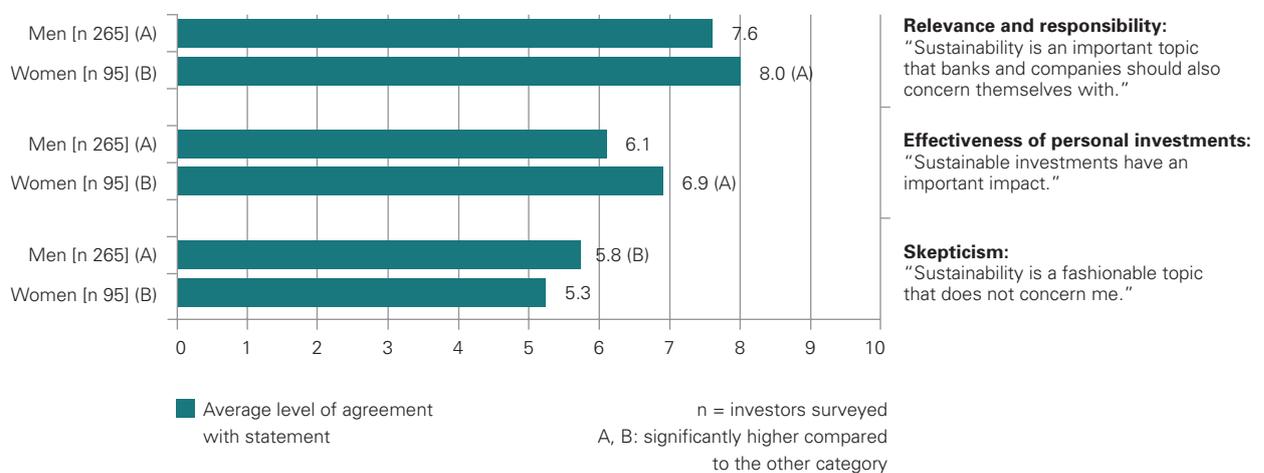
A number of clear convictions can be identified in terms of respondents’ personal attitude toward the issue of sustainability: the most common perception is that sustainability must be viewed as an important topic that banks and companies should also concern themselves with.

A gender comparison shows that women are significantly more often of the opinion that sustainable investments have an important impact (see Figure 5). In contrast, men more often view it as a fashionable topic that is receiving too much attention and is being used by companies only for the purpose of improving their image. They see responsibility for this issue as lying at the political level and not with themselves.

The results of the survey underscore that investors are becoming increasingly aware of sustainable investments. A clearer understanding of the topic and an explanation of concrete sustainability criteria could help to increase the attractiveness of sustainable investments with a view to making these a fixed component of investing in the future.

**Figure 5: Attitudes surrounding the issue of sustainability (gender comparison)**

Using a factor analysis, different statements about sustainability can be clearly grouped into three categories that reflect fundamental positions on the topic. The first category comprises attitudes that can be classified under “Relevance and responsibility”. The second contains views that underscore the “Effectiveness of personal investments”. The third position, “Skepticism”, comprises statements that question the relevance of the topic and one’s personal responsibility in this area.



**Digitalization is advancing**

A dynamic trend can be identified in terms of the utilization of new technological possibilities. The gender and generational differences seen in this area two years ago already appear to be largely dissipating, albeit only for those online offerings that can now be considered standard, for example payment transactions.

The now widespread use of online solutions confirms the need of a clear majority of the private banking clients for convenience as well as interaction with the bank, irrespective of the time or location. The possibility of having a ubiquitous overview of one's investments at all times is important to around half of the respondents. This should in no way be seen as a rejection of the concept of receiving advice from a relationship manager. On the contrary: the data collected clearly underscore that the majority of private banking clients continues to attach great relevance and importance to personal advisory services.

**Risk posed by disruptive clients**

A rapidly diminishing group of clients – those who forgo the use of any technological or digital channels (digital deniers) – stand in contrast to a growing share of clients who exhibit a high affinity for technology. The latter client segment is currently receiving significant attention from the banks' upper echelons for strategic reasons.

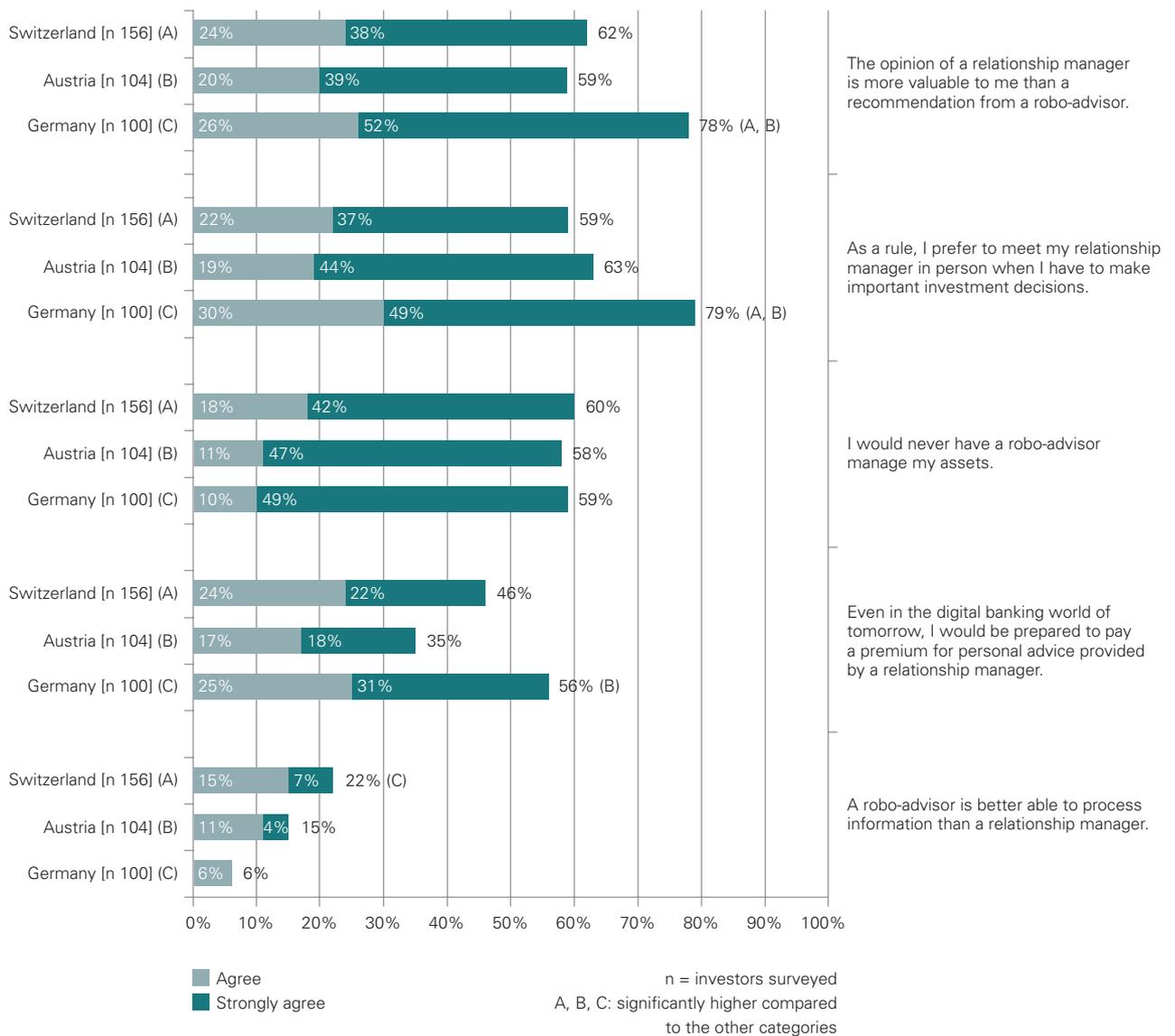
It is necessary to take a closer look at the different ways in which this growing client affinity for technology is manifesting itself in order to gain a clearer and more differentiated picture. For example, the study identifies one client type, the so-called "early tech adopter" (9% of respondents), whose strong affinity for technology and curiosity about new innovations does not automatically translate into a rejection of the bank/relationship manager model. An affinity for technology does not, therefore, necessarily mean a shift away from the bank/relationship manager model for this client segment. A greater threat, however, is the "potential disruptor" client segment (14% of respondents), who in addition to an effective use of technology, are also very skeptical about the bank/relationship manager-centered model. Accordingly, the risk that this group of clients substitutes a traditional private banking relationship with strictly virtual offerings is much higher. The largest share of clients (32%), however, can be classified as "convenience onliners" – in addition to the advantages of online access, they continue to appreciate personal advice from a relationship manager.

### Human or machine?

A clear majority of respondents believes that the opinion of a relationship manager continues to be more valuable than a recommendation from a robo-advisor that offers a completely automated online solution that regularly adjusts a portfolio's asset allocation (see Figure 6). The statement that one would never let one's assets be managed by a robo-advisor also met with a very high level of agreement. Only a minority is convinced that a robo-advisor would be better able to process information than a relationship manager. The challenge for private banking providers is nevertheless the fact that the readiness to pay a premium for personal advice in the future is not particularly high.

**Figure 6: Assessment of robo-advisors versus relationship managers (country comparison)**

Readiness to pay a premium for personal advice in the future is limited. German respondents agree most with this statement, respondents from Austria the least. On the other hand, only a clear minority is convinced that a robo-advisor is better able to process information than a relationship manager: 22% in Switzerland, but only 6% in Germany.



Concerns about conducting online transactions appear to be significantly more widespread than expected, which contributes to a cautious and in certain cases also skeptical attitude among clients. Greater caution when conducting online transactions and concerns about hacker attacks are therefore barriers that banks should take seriously when developing and disseminating digital solutions. Mobile banking is another area that has not gained broad acceptance in this context – at least not with the same momentum as other channels. Social media channels, contrary to many predictions, are also not utilized very much in private banking. Only a small share of respondents indicates that they use social media to foster finance-related relationships. In addition, only a few use these platforms to exchange information with others on economic, financial and investment matters; and an even smaller segment looks for financial experts using these channels.

Despite the increased use of technological possibilities, based on the data collected, the greatest potential for the future lies in a “hybrid, bank-focused model” that combines personal advice with state-of-the-art online services. Private banking providers therefore face the challenge of further developing existing business models by integrating innovative technological solutions in order to further increase convenience for clients. The revolutionary visions of an exclusively machine or robot-dominated investment business do not currently appear to be a model that private banking clients find particularly convincing.

Commissioned by



Private  
Banking

