

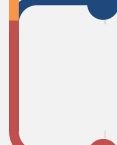
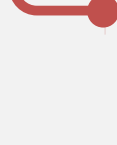


**Level III
of the
CFA® Program**

Private Markets

THE PRIVATE WEALTH MANAGEMENT INDUSTRY

Learning Outcome Statements

-  **LOS** : Discuss the typical **business models** of private wealth management service providers and their segment-based strategies.
-  **LOS** : Discuss typical **fee, revenue, and compensation** structures prevalent in the private wealth management industry.
-  **LOS** : Discuss how various **advisers, consultants, and professionals** support private wealth managers and their clients.
-  **LOS** : Describe and evaluate **regulatory and compliance considerations** influencing the private wealth management industry.

Introduction

- **Private Wealth Management** serves wealthy clients needing comprehensive financial advice.
- **Services** extend beyond investments to include tax, legal, philanthropy, and estate planning.
- Firms often **collaborate** with lawyers, tax specialists, and other professionals for holistic management.



Brief History of the Private Wealth Management Industry



Ancient Civilizations: Early wealth management practices.

Post-WWII: Global expansion of private banks, rise of offshore financial centers.



Late 20th Century: Growth driven by globalization and emerging markets.

2008 Financial Crisis: Led to regulatory reforms like Dodd-Frank and MiFID II.



Swiss Banking Secrecy: Major reforms post-2008, aligned with global transparency norms.

Current Trends: Emphasis on transparency, compliance, and comprehensive services.

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Typical Business Models of Private Wealth Management



Universal Banks: Offer a **wide range of financial services**, including wealth management, under one brand.

Private Banks: Independent entities focusing solely on wealth management for **high-net-worth clients**.

Local Banks and Trusts: Provide region-specific **wealth management** and retail banking services.

Investment Banks: Serve **ultra-high-net-worth** individuals with specialized services like mergers and acquisitions.

Digital and Direct Banks: Use **digital platforms** to offer low-cost, automated investment advice.

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Typical Business Models of Private Wealth Management



Brokerage Firms: Facilitate **market transactions** and provide investment management at competitive fees.

Asset Managers: Focus on managing investments through **dedicated funds**, not full wealth management services.

Independent Advisers: Operate **autonomously**, offering personalized advice without product ties.

Family Offices: Manage **comprehensive financial needs** for single or multiple wealthy families.

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Segment-Based Strategies



Retail Segment: Focuses on **savings accounts** and inexpensive investment solutions.



Affluent Segment: Offers basic financial planning and **digital tools** for investment management.



High Net Worth (HNW): Provides customized **investment solutions** and **wealth-transfer assistance**.



Ultra-High Net Worth (UHNW): Delivers **highly personalized services** with a diverse asset mix, involving senior management.

LOS : Discuss the typical business models of private wealth management service providers and their segment-based strategies.

Offshore vs. Onshore Services

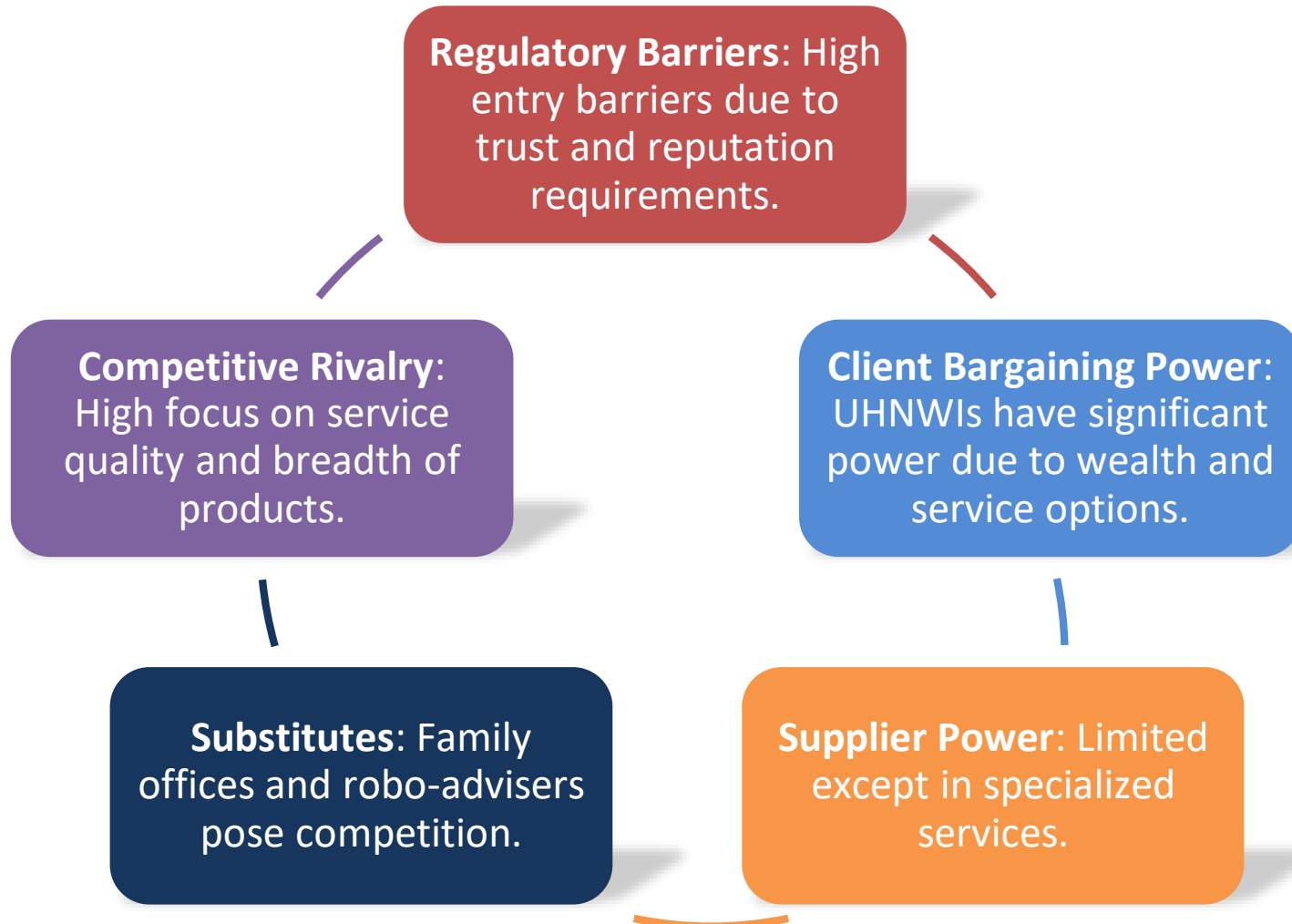


Popular Offshore Financial Centers

- **Onshore Services:** Provided within the client's country of residence, complying with local tax regulations.
- **Offshore Services:** Offered in foreign jurisdictions for benefits like tax incentives and political stability.
- Clients may choose offshore for **legal advantages** and **diverse investment opportunities**.

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Competitive and Strategic Drivers



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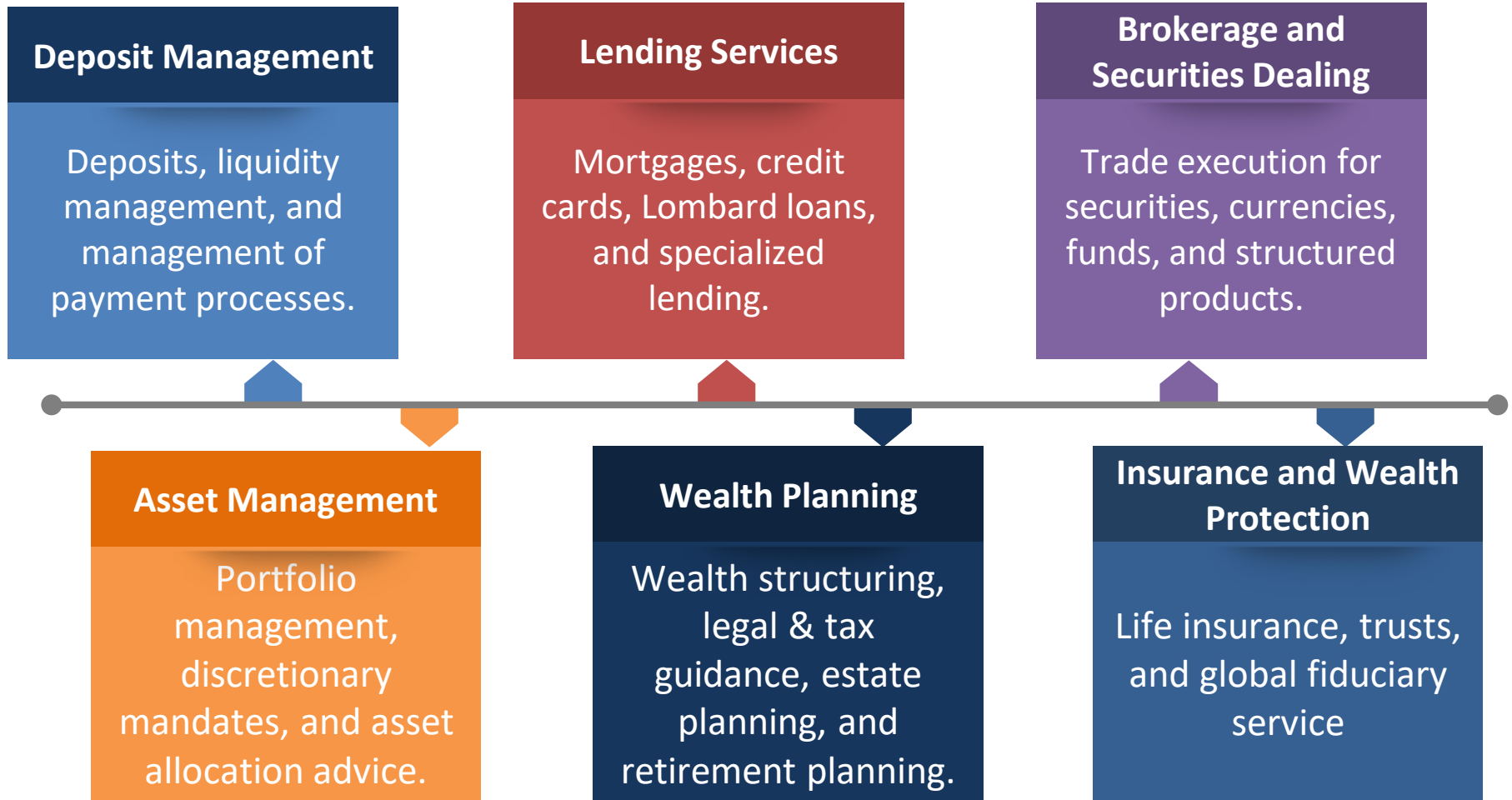
Strategies for Competitive Advantage

- **Cost Leadership:** Focuses on economies of scale and operational efficiency for broad market appeal.
- **Differentiation:** Offers unique, valued services for higher margins, targeting HNWIs.
- **Focus/Niche:** Targets specific segments with highly personalized services, often at premium prices.



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Key Services in Private Wealth Management



LOS : Discuss typical fee, revenue, and compensation structures prevalent in the private wealth management industry.

Fee Structures in Private Wealth Management

- ◆ **Asset-based fees:** Calculated as a percentage of the client's assets under management (**AUM**), typically invoiced quarterly.
- ◆ **Transaction-based fees:** Charges per transaction, applied to trades involving securities, funds, and structured products.
- ◆ **Interest and margin-based fees:** Associated with lending programs, applied to **negative cash balances, mortgages, and securities lending**.
- ◆ **Service and maintenance:** Fixed charges related to account upkeep, such as **administrative fees** and charges for **payments and transfers**.
- ◆ **Additional fees:** May include **accounting, taxation, legal support, and technological support fees**.



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Revenue Structures in Private Wealth Management

Revenue Structures

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graph TD; A[Revenue Structures] --- B[Recurring revenues: Originate from portfolio management activities, custody, and regular service-related activities.]; A --- C[Fixed revenues: Service fees charged periodically.]; A --- D[Non-recurring revenues: Arise from life events (e.g., death, divorce, sale of business) or special projects.]; A --- E[Variable revenues: Transaction/AUM-based fees, varying with client activity and asset levels.];
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External Drivers Impacting Revenues

Global Capital Markets

Increased connectivity and **sensitivity to macroeconomic and geopolitical** developments affect market valuations and revenue stability.

Private Markets Investments

Growing use of private equity, real estate, and venture capital provides diversification and return premiums but **introduces liquidity challenges**.

Technology Adoption

Robo-advisors and low-cost trading platforms can reduce client costs but may also lower industry revenues; however, they can attract new small investors.

ESG Awareness

Environmental, social, and governance factors are **increasingly integrated into services** but can compress net revenue if costs can't be transferred to clients.

Regulatory Changes

Initiatives like the **Retail Distribution Review (RDR)** and **Financial Advice Market Review (FAMR)** in the UK emphasize fee transparency, potentially reducing revenues.

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Internal Drivers Impacting Revenues

Client Portfolio Returns

Higher returns on client portfolios increase assets under management (AUM) and revenue.

Fee Increases

Firms can raise fees, especially with unique or differentiated products, though it's challenging in a **competitive market**.

New Client Acquisition

Attracting new clients and growing net assets **boosts firm revenue**.

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Internal Drivers Impacting Revenues

Client Retention

Focusing on client satisfaction and retention minimizes revenue losses.

Net New Money (NNM)

Focuses on **bringing in new client assets**.

Net New Business Volume (NNBV)

Measures the volume of **new business across new and existing clients**.

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Compensation Structures in Private Wealth Management



Fixed Remuneration: Base salary determined by role, experience, and firm-specific factors.



Variable Remuneration: Includes annual bonuses, often tied to individual, team, and firm performance.



Long-Term Incentives: Equity or stock ownership in the firm, typically with vesting periods.



Fringe Benefits: Includes insurance packages, retirement perks, and access to exclusive training programs.

LOS : Discuss how various advisers, consultants, and professionals support private wealth managers and their clients.

Role of Legal Experts in Private Wealth Management

Estate planning: Lawyers specialize in estate planning, trusts, and wills to ensure efficient asset transfer and legal protection.

Conflict mediation: They mediate family disputes and provide legal solutions during conflicts.

Regulatory compliance: Ensure compliance with local and international laws, protecting client interests in complex jurisdictions.

Legal documentation: Draft and review legal documents to secure asset ownership and facilitate transactions.



Example: The Rockefeller Trust

The Rockefeller family used a complex trust structure to preserve wealth across generations, **minimizing estate taxes and ensuring philanthropic endeavors continued**. Legal experts were crucial in setting up and maintaining this structure to adapt to changing laws.

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Role of Tax Advisers and Accountants

Tax planning: Develop strategies for income splitting, charitable giving, and investment in tax-efficient vehicles.

Compliance: Ensure accurate and timely tax filings to avoid penalties.

Financial records: Maintain financial records for budgeting, forecasting, and compliance.

Complex tax structures: Advise on family limited partnerships, investment companies, and offshore trusts for tax efficiency.



Example: Apple, Inc.

Apple has over the years used tax advisers to establish an international structure, **channeling profits through countries with favorable tax laws**, significantly reducing the company's tax burden. This allowed more funds to be **reinvested in innovation and growth**.

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Role of Custodians

Asset safekeeping: Ensure the safekeeping and segregation of client assets.

Transaction verification: Verify and record transactions post-settlement for compliance.

Performance analytics: Provide real-time analytics for portfolio assessment and strategy formulation.

Global expertise: Navigate diverse regulatory frameworks for seamless operation.



Example: Northern Trust

Northern Trust acts as a custodian for **numerous high-net-worth individuals** and institutions, providing **secure storage and management of diverse assets**, including art collections, real estate, and digital assets.