

Financial Services  
Banking

# Opportunities and Competitive Re-positioning of Luxembourg Private Banking by 2012-2015\*

Developing a recognised centre of excellence for new generation wealthy clients



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# Foreword

In Luxembourg, where the financial sector represents 46% of the country's economic value added<sup>1</sup> and 32%<sup>2</sup> of total fiscal revenues, private banking is a key activity. Private banks manage over EUR 300 Bn<sup>3</sup> (USD 440 Bn) in clients' assets, employ directly and indirectly over 9,200 full-time employees<sup>2</sup> and contribute over EUR 350 Mio to tax revenues<sup>2</sup>. This is an important achievement, but the Luxembourg private banking industry has the potential to be further developed.

In 2006 and 2007, Luxembourg private banks achieved substantial business growth in line with the market. In the quest for continuous growth and a better positioning in the global private banking landscape, Luxembourg private bankers are ambitious and would like to go beyond market growth. The private banking sector is serving a huge potential market of EUR 25 trillion<sup>4</sup> (USD 37 trillion) in assets owned by its "traditional clients", the High Net Worth Individuals (HNWI).

It is a highly competitive market where players are not only looking for growth, but also for more service quality while maintaining reasonable production costs. That is why, within some financial centres, players are aiming at sharing capacities to leverage their competitive position in areas like product development, transaction processing, training, etc.

The private banking sector is undergoing some fundamental changes and failing to adapt now could leave Luxembourg private bankers behind in the years to come. The goal of this report "**Opportunities and Competitive Re-positioning of Luxembourg Private Banking by 2012-2015: Developing a recognised centre of excellence for new generation wealthy clients**" is to provide a sense of purpose shared by all the Luxembourgish stakeholders of the private banking sector and guidance for the development of coherent capacities to sustain the cluster in the long-term. Every stakeholder of the Luxembourg private banking

sector (bankers, specialised services providers, ABBL, public institutions, regulator and government) should see its strategic contribution leveraged from this joint initiative.

In this report, we address the changes in the global private banking landscape; the actual performance of the private banking sector in Luxembourg and opportunities for growth; the vision for a sustainable long-term development; as well as an indicative action plan for growth and leadership of Luxembourg for the horizon of 2012-2015.

The groundwork of the present document consisted of on one hand, market analysis to understand Luxembourg private banking centre's

current positioning and, on the other hand, a series of workshops conducted between August and November 2007 involving private banking business leaders in Luxembourg and key stakeholders. The joint vision was drawn collectively for the re-positioning of the Luxembourg private banking centre and the preliminary conclusions were shared during PwC's Banking Day 2007 and greatly enriched by participants.

We hope that this report will support private bankers and key stakeholders in achieving their growth ambition. We look forward to continuing these discussions in attempt to contribute to the development of the Luxembourg private banking centre.



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<sup>1</sup> As a percentage of Gross Domestic Product (GDP). Source: "Etude d'impact de l'industrie financière sur l'économie luxembourgeoise", CODEPLAFI, 2006 results

<sup>2</sup> Source: "Etude d'impact de l'industrie financière sur l'économie luxembourgeoise", CODEPLAFI, 2006 results

<sup>3</sup> Source: CSSF, 2007

<sup>4</sup> Source: Merrill Lynch/Cap Gemini World Wealth Report 2007

# 1. Changing Business Landscape

## 1.1 Needs and competition are evolving

The traditional private banking business of banks is in constant evolution. Investment performance, added-value services provision such as lifecycle financial planning, inheritance-succession management and estate planning, and improved client relationship are the key trends of this major evolution.

In addition to these important factors impacting the business, three drivers urge private bankers, and especially Luxembourg private bankers, to adapt:

- Clients want a holistic approach, which means essentially that they are looking for an increased link between services to manage their savings, investments and wealth. More importantly, clients coming to Luxembourg today want an international approach to services since they have interests in several jurisdictions;
- Clients want advice. Private banking is no longer simply about delivering products to satisfy the basic needs of creating, preserving and maximising savings and wealth. It is rather about advice to optimise investments (return, tax optimisation, risk diversification) or to transmit wealth to the new generation, which has different needs and behaviours. Private banking is therefore confronted with the necessity to be more proactive in both retaining existing monies and uncovering real needs to service current and future clients more effectively;
- Competition is increasing in different jurisdictions. Homeland private banking is developing rapidly, providing improved services to residents and therefore, retaining the share of the richest individuals. New “International Financial Centres” are steadily developing their offerings to attract the richest with

more international needs. This forces private bankers to clearly differentiate in order to maintain their attractiveness, or to form alliances in order to leverage their competitive advantage.

## 1.2 Target clients are changing

### 1.2.1 The new wave of wealthy individuals

The economic boom of both traditional leading economies and new developed countries brings its share of new HNWI and significant changes in the geographic sources and flows of wealth. The financial wealth growth of HNWI<sup>5</sup> is expected to increase worldwide at an annual rate of 6.8% until 2011 to reach USD 51.6 trillion<sup>6</sup>. By 2050, the E7 economies (Brazil, China, India, Indonesia, Mexico, Russia and Turkey) are expected to be around 25% larger than the current G7 in dollar terms<sup>7</sup>. This means that, in addition to traditional family wealth, a new generation of entrepreneurs springs up from the new wave

of economic globalisation. This provides private bankers with a chance to further expand onshore business worldwide as a result of improved market access.

However, competition to attract clients from emerging markets is already fierce. A recent study<sup>8</sup> analysing a sample of Swiss banks shows that while “old Europe” represents approximately 60% of the stock of assets, it only counts for 40% of net inflows. In contrast, the majority of Swiss banks’ net inflows are coming from emerging markets like Middle East, Eastern Europe, Latin America, and Asia. According to the study, Middle Eastern investors themselves are responsible for 20% to 30% of Swiss banks’ net inflows.

In Europe, Ultra High Net Worth Individuals (UHNWI)<sup>9</sup>, who represent now more than 1/4 of the total wealth invested in private banks, is the most promising category of clients. Their wealth grew by 27% in 2007, compared to a 7% wealth growth in the affluent and wealthy client categories<sup>8</sup>.

<sup>5</sup> Individuals disposing of more than USD 1 Mio in liquid assets

<sup>6</sup> Source: Merrill Lynch/Cap Gemini World Wealth Report 2007

<sup>7</sup> Source: PricewaterhouseCoopers “Banking in 2050: How big will the emerging markets get?”

<sup>8</sup> Source: European Private Banking Survey 2007, McKinsey & Company

<sup>9</sup> Individuals disposing of more than USD 30 Mio in liquid assets

# 1. Changing Business Landscape

## 1.2.2 The retirement of baby-boomers

In addition to the wave of “new generation clients”, retirees and near-retirees represent another potential client segment for private banks given the significant number of baby boomers who are moving into retirement age, the increasing life expectancy, and the consequent intergenerational wealth transfer. Forecasts show that retirees and near-retirees will hold almost 2/3 of all assets by 2010<sup>10</sup>.

This demographical shift will have important consequences for private banks as retirees and near retirees have particular financial needs and investment behaviours. Demand for products and advice focused on income generation and principal protection should therefore increase.

## 1.3 Business model is transforming

The competition amongst financial centres and amongst private banking groups has facilitated the emergence of new and differentiated models to both maintain and develop the client base across borders. In this context, private bankers are more actively looking for complementarities between local and international markets to attract new clients and serve them across geographies.

International wealthy clients’ needs are becoming more complex, placing very strong product and service demands on private banks. Therefore, private banks are increasingly adopting open-product architecture for offering clients the best products available on the market and a broad range of

sophisticated products and services, including non-banking services such as estate and trust management, philanthropy and art investments, or concierge services. This is impacting the current value chain of products and services sourcing, putting an emphasis on possible alliances between specialised actors of the wealth management industry.

In this highly competitive business environment, performance and productivity of key resources are determinant. Recent literature shows that the best performing business models are now more and more based on a mix of high quality financial advisers and efficient technology platforms. However, studies show that the business model of private banks today is still mainly focused on products, not on customers’ needs.

<sup>10</sup> Source: The Asset Management Industry in 2010, McKinsey & Company

## 2. Diagnostic of the Luxembourg Private Banking centre

### 2.1 Current strengths and weaknesses

#### 2.1.1 Luxembourg has a strong client base which is evolving

The Luxembourg private banking centre has a large client base mainly composed of wealthy<sup>11</sup> clients and HNWI<sup>12</sup>, which together account for 68% of the client base and 50% of private banking Assets under Management (AuM)<sup>13</sup>. UHNWI represent only 3% of the client base, but account for almost 20% of AuM.

Luxembourg's clientele is mainly regional as 60%<sup>14</sup> come from neighbouring countries<sup>15</sup>. Compared to other leading private banking centres, Luxembourg has a limited number of clients coming from emerging markets such as the

Middle East, Eastern Europe, and Asia, where wealth is growing at a much faster rate than in traditional markets.

The average account size of private banking clients in Luxembourg is between EUR 500,000 and EUR 1 Mio. Interestingly, new clients who are coming to Luxembourg today are bringing higher amounts of assets as illustrated by the steady increase in the average client account size over the past three years<sup>13</sup>. Luxembourg market experiences show that recent trends in new clients' money inflow is on average between EUR 800,000 and EUR 1 Mio, while current clients' money outflow is on average between EUR 200,000 and EUR 300,000.

Luxembourg is predominantly servicing traditional family wealth<sup>16</sup>, which has been Luxembourg's main clientele for many years. However, Luxembourg private bankers confirm that they are increasingly attracting "new money" clients, such as entrepreneurs and corporate executives.

#### 2.1.2 Luxembourg offers a good product and service range with key differentiation factors

Luxembourg offers a broad range of products and services, as a real "one-stop-shop", which has effectively favoured the increase in wealth managed over the years. Luxembourg offers both traditional, plain vanilla savings products, and sophisticated solutions for creating, maintaining, maximising and transmitting wealth.

Luxembourg has developed solid financial engineering capabilities and know-how in cross-border wealth engineering, asset structuring, fund constitution, and tax optimisation services. Luxembourg benefits today from a broad range of legal structures, which collects 2/3 of Luxembourg's AuM invested by wealthy individuals<sup>14</sup>.

As private banking clients today recognise that a provider cannot offer "best-in-class" solutions for every product and service, Luxembourg entities have embraced the concept of open-product architecture, making use of a wider range of products and services to meet increasingly sophisticated client demands.

<sup>11</sup> Individuals disposing of USD 500,000 - USD 1 Mio in liquid financial assets

<sup>12</sup> Individuals disposing of USD 1 - USD 5 Mio in liquid assets

<sup>13</sup> Source: PricewaterhouseCoopers Global Private Banking and Wealth Management Survey 2007

<sup>14</sup> Source: CSSF, 2007

<sup>15</sup> Belgium, France and Germany

<sup>16</sup> Currently, traditional family wealth accounts for 77% of Luxembourg's client base, whereas "new money" clients account for the remaining 23%; however, the latter is expected to represent 39% of the client base in the next 3 years. Source: PricewaterhouseCoopers Global Private Banking and Wealth Management Survey 2007

## 2. Diagnostic of the Luxembourg Private Banking centre

Areas of improvement for Luxembourg private banks today are to be found in:

- Discretionary portfolio management, which currently accounts for approximately 15% of the wealth managed in Luxembourg. Luxembourg private bankers expect to increase this percentage to 50% in the future<sup>17</sup>;
- Advisory portfolio management with a mandate, which is very limited today despite clients' increasing demand for it;
- Alternative investments, where the offer is not as well developed as it is in competing financial centres<sup>18</sup>.

### 2.1.3 Luxembourg private banking entities are perceived as a centre of excellence within their group<sup>19</sup>

**Luxembourg entities believe for the most part that they are perceived as a centre of excellence in private banking by their group and as a strong contributor to the group's net profit<sup>20</sup>.**

The Luxembourg private banking centre of excellence recognition is the result of several factors:

- Due to their international know-how and exposure, Luxembourg entities are considered as a key contributor to the group's global clients value proposition<sup>20</sup>;
- Thanks to the flexibility, quality of service and experience gained in the investment fund industry in Luxembourg, some private bankers have developed transaction hubs in Luxembourg for servicing other group entities

located in Europe, Middle East and elsewhere;

- As a result of innovation and the flexibility of the legal framework, Luxembourg private bankers have developed recognised vehicles providing the group with flexible, tailor-made and efficient solutions in wealth engineering.

Luxembourg entities are also considered as strong contributors to the group's net profits, encouraging headquarters' support<sup>20</sup>. The Luxembourg average Return on Assets (RoA) is 70 to 80 basis points, which is on average 10% to 15% above headquarters' RoA.

**Nevertheless, only 1/4 of Luxembourg private banking players succeeded in converting this perceived positioning into a European or international responsibility<sup>20</sup>.** Given that Luxembourg positions itself mainly as a regional or European private banking centre of excellence, Luxembourg entities are lacking

group support to develop activities in emerging markets outside Europe, such as Asia, Middle East and South America.

The centre of excellence approach must be further developed by investing more in these crucial areas, and by improving the positioning of Luxembourg entities within the group to overcome the restrictions they currently have with regards to setting their strategic direction to go for new markets.

<sup>17</sup> Source: PricewaterhouseCoopers Global Private Banking and Wealth Management Survey 2007

<sup>18</sup> Some Swiss private banks are investing between 20% and 30% of clients assets in Hedging strategies. Source: Financial Times, 23 April 2007

<sup>19</sup> Group relates to the Banking group to which the Luxembourg entity belongs

<sup>20</sup> Source: PricewaterhouseCoopers Luxembourg Banking Market Challenges and Opportunities Survey, 2006 (Results include only the views of banks having a Private Banking activity in Luxembourg; the sample includes 40 banks)



## 2.1.4 Luxembourg benefits from a favourable environment for private banking development

Luxembourg's legislation regarding the financial sector is being benchmarked by rival private banking centres, which carefully watch at the latest evolutions. According to the Swiss Bankers Association, "Luxembourg has an efficient, innovative and forward-looking regulator. It has always been one of the first countries to put European Union regulations (such as those covering funds or the recent directive on international pension products) into practice while preserving its own sovereignty as far as possible."

The Luxembourg regulator is perceived as highly competent by Luxembourg private bankers<sup>21</sup> and has developed international recognition in other financial centres. Luxembourg private bankers are quite satisfied with the regulator's response time to their requests<sup>21</sup>.

Luxembourg private bankers assert that the wealth management industry has been positively impacted by government legislation over the last three years<sup>21</sup>. The new tax regime, with abolition of personal wealth tax in 2006, has eliminated some of the obstacles in attracting new very wealthy residents.

In addition, Luxembourg offers further advantages for the development of its private banking centre, such as a stable political and economic framework, its European Union membership, client privacy, a high commitment to regulatory compliance, qualified and multilingual staff, and low labour costs<sup>22</sup>.

Finally, Luxembourg offers a highly competitive business environment, ranked 4<sup>th</sup> most competitive country in the world after the US, Singapore and Hong Kong, in terms of government and business efficiencies, infrastructure, and economic performance<sup>23</sup>.

Looking at the key constituents of a successful business, Luxembourg has an interesting profile, but the **cluster** approach is at its start. Therefore, there is room for improvement in areas where collective effort is needed:

- Luxembourg lacks market and business intelligence, as well as research structures dedicated to the wealth management industry;
- Although the Luxembourg private banking centre is well supported, there are still limited promotional activities, tools and data concerning the private banking industry. The promotion of the Luxembourg financial sector has historically focused on the investment funds industry, which has different drivers than the private banking industry;

- Luxembourg is not attracting enough talents to the private banking industry. Today, the demand for Client Relationship Managers (CRMs) in Luxembourg already exceeds supply<sup>24</sup>.
- Luxembourg private bankers are not sufficiently investing in the development of the required private banking skills. Less than half (46%) of Luxembourg entities strongly agree that sufficient resources are allocated to ensure that employees receive the correct level of training to undertake their role at a high standard<sup>21</sup>.

### Cluster

In a cluster a significant part of both the social community and the economic agents work together in economically linked activities, sharing and nurturing a common stock of products and services, technology and organisational knowledge in order to generate superior quality in the market place.

<sup>21</sup> Source: PricewaterhouseCoopers Global Private Banking and Wealth Management Survey 2007

<sup>22</sup> Financial sector labour costs (deflated) in Luxembourg are below EU25 average and countries like UK, Ireland, Netherlands, France or Spain. Source: Eurostat, 2006.

<sup>23</sup> Source: IMD World Competitiveness Yearbook 2007

<sup>24</sup> On average, only 65% of Luxembourg private banks' job openings were filled in 2006. Source: PricewaterhouseCoopers Global Private Banking and Wealth Management Survey 2007

## 2. Diagnostic of the Luxembourg Private Banking centre

### 2.2 Key opportunities for the future

#### 2.2.1 Improve existing and develop new client servicing

On one hand, existing clients are to be served well because they are Luxembourg's primary source of net new money in the future<sup>25</sup>. Luxembourg entities expect both to increase the share of wallet of existing clients in the next three years<sup>26</sup> and use them as key introducer to new clients through referrals<sup>25</sup>. Therefore, better exploiting the existing client base through improved understanding of clients' needs and segmentation should become a major mean for developing long-term client relationships and gaining a share of the wallet. Developing a process to retain key clients at risk and actively measuring client satisfaction

is also extremely important for the development of Luxembourg's client base.

Moreover, given the intergenerational wealth transfer that will occur in the coming years, Luxembourg banks should place special efforts in forging relationships with the younger generation in order to preserve current AuM and develop new money inflow in the years to come.

On the other hand, Luxembourg entities expect an increase of AuM in the HNWI, Very High Net Worth Individuals (VHNWI) and UHNWI segments in the next three years<sup>25</sup>. Targeting HNWI, the most profitable client segment today and tomorrow, along with VHNWI, is a good opportunity for the Luxembourg private banking centre to raise its image in the world's financial sector and differentiate itself from homeland headquarters.

Within the HNWI sector, entrepreneurs and corporate executives are the two client segments offering the greatest potential in Europe over the next five years<sup>27</sup>. Currently, the primary source of new assets for Luxembourg private banks is new wealth coming from entrepreneurs who have sold businesses<sup>25</sup>. This trend will pursue since 46% of Luxembourg family business owners will transfer/sell their activity in the next five years<sup>28</sup>, without mentioning the "Greater Region"<sup>29</sup> where we see similar evolution. Growth of private businesses and highly paid employees, such as corporate executives, are other key sources of new clients for Luxembourg private banks. Thus, Luxembourg private bankers should look at increasingly shifting from old, traditional family wealth to "new money" in order to capture a greater share of these promising segments.

Going beyond the borders and reaching out to new geographical areas in Europe and emerging markets could also be a valuable source of growth for Luxembourg entities. Some Luxembourg private bankers have already succeeded in these areas and others could leverage these successes to think about new ways of contributing to the group's growth.

<sup>25</sup> Source: PricewaterhouseCoopers Global Private Banking and Wealth Management Survey 2007

<sup>26</sup> However, the previous expectations Luxembourg entities had in gaining share of wallet have not been achieved. Source: PricewaterhouseCoopers Global Private Banking and Wealth Management Survey 2005

<sup>27</sup> Source: Datamonitor Wealth Management Market Leaders Survey 2006

<sup>28</sup> Source: Les entreprises familiales luxembourgeoises – Edition 2007, PricewaterhouseCoopers

<sup>29</sup> The Greater Region is one of Europe's largest cross-border zone; it represents an area composed by the Grand Duchy of Luxembourg, the German federal states Saarland and Rheinland-Pfalz, the French region Lorraine and the Belgian region Wallonia.

## 2.2.2 Focus on developing the product and service offer

To develop client loyalty, Luxembourg private banks have to further:

- Develop their range of innovative products (such as art investments or lifestyle services) and structures (such as family offices, trusts and foundations);
- Strengthen the links between asset management, risk management and reporting services, as performance reporting is becoming an important part of the offering as well as an opportunity to improve service and differentiate as most HNWI request a simpler overview of fees and performance<sup>30</sup>, especially when they use multiple banks;

- Develop advantageous synergies between private banking, asset management, investment management and corporate banking activities in an integrated business model for better client servicing. The growing sophistication of private banking needs has prompted private banks worldwide to draw in experts from investment banks and fund management groups who are used to dealing with large institutional clients<sup>31</sup>.

Becoming a true “one-stop-shop private bank” for VHNWI or UHNWI means making efficient links between the various offerings that the bank has in different fields to make sure it captures all the opportunities a client provides, especially when looking at the entrepreneur and international corporate executive segments.

## 2.2.3 Strengthening the Luxembourg private banking centre

The creation of the Private Banking Group Luxembourg in 2007 is the first sign of the need to increasingly work together. Individually, the banks have done a lot for the development of the Luxembourg private banking business, however, now it is time to move forward and use the cluster to achieve economies of scale, develop specialised knowledge and foster continuous innovation. Nowadays, this is key to create and maintain a competitive advantage, increase regional/European recognition and finally improve the global competitiveness of Luxembourg as a key actor in this business. Today there are opportunities in terms of:

- **Leadership.** There is recognition amongst private bankers that somebody has to take on the role of fostering mutual cooperation, knowledge sharing to turn private banking from a fiercely competitive to a closely collaborative environment.

- **Communication.** There is a need today for more regular communication events, interactions or approaches that foster common sense of identity in a business that is by essence very “individualistic”.
- **Coordination.** There is room today to set-up benchmarking task forces, joint research initiatives and a “Think Tank” to sustain the positioning of Luxembourg as a key player in the financial community, within the group and among the client community.

There is today a momentum to create a new culture of collaboration amongst key Luxembourg private bankers to better compete as a unified cluster against other financial centres that are strengthening or developing their capacities in private banking/wealth management.

<sup>30</sup> Source: Morgan Stanley European Investment Research, 2005

<sup>31</sup> Source: Financial Times, July 8<sup>th</sup>, 2007



# 3. Re-positioning the Luxembourg Private Banking centre

There is a strong consensus between private bankers that, in order to remain competitive and be distinctive by 2012-2015, the business model of the Luxembourg private banking centre will need to undergo a substantial transformation.

Luxembourg private bankers must adapt individually to changes caused by new patterns in clients' profiles, behaviours and needs and increased competition, and at the same time improve their ability to act collectively to reinforce the position of Luxembourg as a strongly recognised international private banking centre.

To gain a larger critical mass in terms of assets managed and to develop Luxembourg's key strategic capacities in order to leverage its current competitive advantages, a vision has been developed and key strategic objectives have been agreed amongst the key stakeholders driving the private banking business for the years to come.

## 3.1 Vision 2012-2015

*"If we grow as fast as the market with the small global market share we have today, we will be insignificant tomorrow."*

Participant

*"Luxembourg must focus on HNWI with over EUR 20 Mio in liquid assets to attain critical mass, ensure growth, and differentiate itself from competing private banking centres."*

Participant

With almost 64,000 full-time employees<sup>32</sup> and EUR 23 Bn in revenues<sup>32</sup>, the Luxembourg financial sector makes a key contribution to the overall economy, representing 46% of the country's economic value added<sup>33</sup> and 32% of tax revenues<sup>32</sup>.

The private banking sector is a key pillar of the Luxembourg financial centre: it counts EUR 2.8 Bn in revenues<sup>32</sup>, represents 6% of the country's economic value added<sup>33</sup> with a workforce of over 9,200 direct and indirect full-time employees<sup>32</sup>, and EUR 350 Mio in contribution to tax revenues<sup>32</sup>.

<sup>32</sup> Source: "Etude d'impact de l'industrie financière sur l'économie luxembourgeoise", CODEPLAFI, 2006 results

<sup>33</sup> As a percentage of Gross Domestic Product (GDP). Source: "Etude d'impact de l'industrie financière sur l'économie luxembourgeoise", CODEPLAFI, 2006 results

### 3. Re-positioning the Luxembourg Private Banking centre

#### By 2015, the Luxembourg private banking centre should:

- Reach a market volume of at least EUR 1,000 Bn in AuM, compared with current approximately EUR 300 Bn<sup>34</sup>. The overall Luxembourg economy will benefit from such a growth as contribution to tax revenues should evolve from EUR 350 Mio<sup>35</sup> to EUR 1,150 Mio, and the number of direct and indirect employees should rise from 9,200<sup>35</sup> to 17,000<sup>36</sup>;
- Be a recognised **centre of excellence** in tailor-made **financial engineering** solutions, sustained by a pool of talents and continuous innovation, to offer a superior quality of services to increasingly sophisticated clients;
- Have a good track record with HNWI disposing of at least EUR 20 Mio in liquid assets. These HNWI will be mainly composed of “first generation money” clients, including entrepreneurs and those who have sold businesses, shareholders in private equity and real estate funds, as well as young executives, coming mainly, but not solely, from European countries;
- Have at least 50% of Luxembourg entities with European and/or international responsibility in private banking within the group, either because Luxembourg entities are at the forefront in servicing targeted markets, have become operation hubs or are the product factory to cover specific needs.

#### Centre of excellence

A centre of excellence is defined as “a physical or virtual centre which concentrates know-how in a technical field creating competitive advantages once critical mass is reached. Development tends to be propagated in other local activities, in particular of service and subcontracting. A centre of excellence plays a dynamic role in innovation, has appropriate human resources, knowledge capacity in technology, and benefits from high levels of international visibility”

#### Financial Engineering

Financial Engineering solutions consist of organising and restructuring holdings, relocating an estate or a company, organising financial flows and income (dividends, capital gains, etc.), optimising real estate holdings through specific vehicles like Soparfi, SPF or other trusts, and include services such as domiciliation, the assessment and the implementation of financial planning projects, in particular the formation of ad hoc legal structures for holding transferable assets and financial holdings, and for financing purposes.

<sup>34</sup> Source: CSSF, 2007

<sup>35</sup> Source: “Etude d’impact de l’industrie financière sur l’économie luxembourgeoise”, CODEPLAFI, 2006 results

<sup>36</sup> This evolution considers a 7% annual growth in full-time employees until 2015

## Vision for the Luxembourg Private Banking cluster by 2015



### The vision in key figures

	2006	2012E	2015E	Annual Growth
<b>Private banking AuM</b>	EUR 300 Bn*	EUR 650 Bn	EUR 1,000 Bn	➔ 14%
<b>Revenues</b>	EUR 2,800 Mio**	EUR 6,200 Mio	EUR 9,150 Mio	➔ 14%
<b>Contribution to tax revenues</b>	EUR 350 Mio**	EUR 770 Mio	EUR 1,150 Mio	➔ 14%
<b>Number of CRM's employed (approximate)</b>	1,500***	2,500	3,250	➔ 9%
<b>Number of employees (direct and indirect)</b>	9,200**	14,000	17,000	➔ 7%

\* Source: CSSF, 2007

\*\* Source: "Etude d'impact de l'industrie financière sur l'économie luxembourgeoise", CODEPLAFI, 2006 results

\*\*\* Source: PwC calculations

### 3. Re-positioning the Luxembourg Private Banking centre

#### 3.2 Strategic Building Blocs

*“We must act to capture new target clients; we can not sit and wait for them.”*

Participant

*“Luxembourg has a real willingness to go beyond European borders and has competitive advantages to succeed.”*

Participant

*“Luxembourg must further attract “first generation money” clients.”*

Participant

#### Strategic Building Blocs

- ✓ Increase market and client reach
- ✓ Improve product and service richness
- ✓ Attract talents and develop competencies
- ✓ Build a strong and coherent brand
- ✓ Improve the operating model
- ✓ Invest more and faster in the development of private banking activities

#### 3.2.1 Increase market and client reach

The Luxembourg private banking activity could become significantly stronger within the Luxembourg economy and across the global private banking landscape by increasing AuM to EUR 1,000 Bn by 2015. This would result in an additional direct and indirect workforce of almost 8,000 full-time employees, an additional EUR 800 Mio in contribution to tax revenues, and a more than doubled European share of HNW wealth from approximately 4.3% today to almost 10% in 2015<sup>37</sup>.

To achieve this goal, Luxembourg must ensure a double-digit annual growth of at least 14% until 2015.

This growth is needed to remain competitive vis-à-vis emerging private banking centres such as Singapore, which increased its private banking AuM by approximately 25% in the past two years to reach approximately EUR 175 Bn (USD 250 Bn)<sup>38</sup>, and vis-à-vis Switzerland which is aiming at a 6% annual growth in private banking AuM until 2015<sup>39</sup>, roughly the same growth as of global HNWI's financial wealth<sup>40</sup>, to maintain its leading position as the largest private banking centre worldwide.

This growth is also needed to be on the radar of all the head offices of the main players present in Luxembourg recognising therefore the complementarities between homeland private banking and international private banking.

This growth should partially come from:

- Neighbouring countries, in which annual HNWI's financial wealth growth will be around 5%;
- Other “new” European countries, in which annual HNWI's financial wealth growth will be around 8%;
- Non-European countries, in which annual HNWI's financial wealth growth will be close to 10%.

Going beyond neighbouring countries in emerging wealth markets, where the proportion of UHNWI is higher<sup>41</sup>, is a necessity if Luxembourg private banks want to increasingly attract “first generation money” clients with larger portfolios, a segment new to all players on which past history has no weight and for which competence is highly important.

<sup>37</sup> European HNW financial wealth was estimated at USD 10.1 trillion (EUR 7 trillion) in 2006, with an annual growth of 4.3% until 2011. Source: Merrill Lynch/Cap Gemini World Wealth Report 2007

<sup>38</sup> Source: Wall Street Journal, February 12, 2007

<sup>39</sup> Source: Swiss Banking- Roadmap 2015, Association Suisse des Banquiers

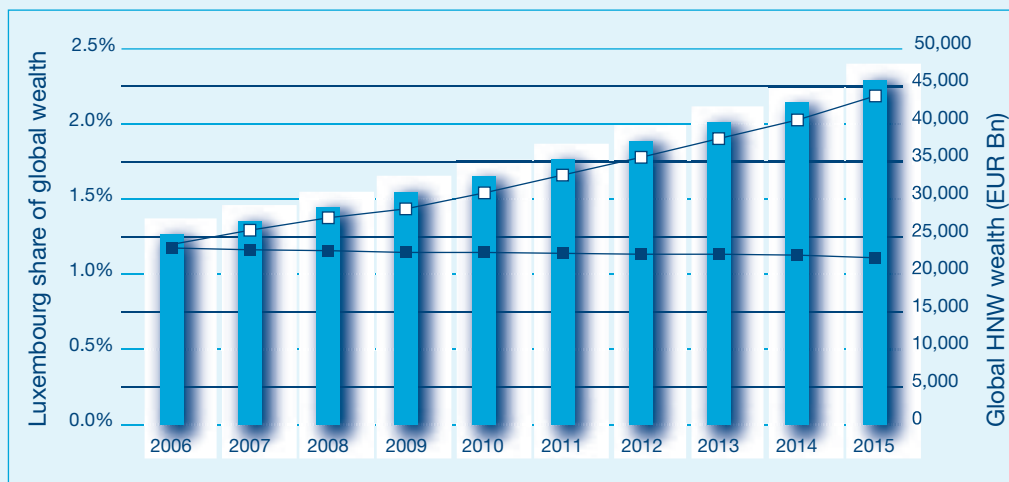
<sup>40</sup> Annual growth rate of HNW financial wealth is estimated at 6.8% until 2011. Source: Merrill Lynch/Cap Gemini World Wealth Report 2007

<sup>41</sup> The proportion of UHNWI is higher in Eastern Europe, Latin America and Middle East, than in “old Europe”. Source: Merrill Lynch/Cap Gemini World Wealth Report 2007



## What would be the consequence if Luxembourg follows market performance?

### Vision and alternative scenario comparison (market share)



□ 14% annual growth    ■ 6% annual growth

Global HNW wealth is expected to grow by 6.8% annually until 2011<sup>42</sup>. Switzerland sets the goal of 6% private banking AuM annual growth until 2015 in order to maintain its leading position as a private banking centre. This is a reasonable goal for Switzerland, however if Luxembourg, given its size, only follows market performance of 6% annual growth, it will only reach AuM of EUR 510 Bn by 2015 and Luxembourg's share of global wealth will be reduced to less than 1%.

### The alternative scenario in key figures

	2006	2012E	2015E	Annual Growth
<b>Private banking AuM</b>	EUR 300 Bn*	EUR 430 Bn	EUR 510 Bn	➔ 6%
<b>Revenues</b>	EUR 2,800 Mio**	EUR 4,000 Mio	EUR 4,750 Mio	➔ 6%
<b>Contribution to tax revenues</b>	EUR 350 Mio**	EUR 500 Mio	EUR 600 Mio	➔ 6%
<b>Number of CRMs employed (approximate)</b>	1,500***	1,900	2,150	➔ 4%
<b>Number of employees (direct and indirect)</b>	9,200**	11,000	12,000	➔ 3%

\* Source: CSSF, 2007

\*\* Source: "Etude d'impact de l'industrie financière sur l'économie luxembourgeoise", CODEPLAFI, 2006 results

\*\*\* Source: PwC calculations

Luxembourg entities would face difficulties in positioning themselves within the group, and the Luxembourg centre of competence would not be developed as strongly as what most Luxembourg participants are aiming at. Therefore, Luxembourg would remain a regional private banking centre.

<sup>42</sup> Source: Merrill Lynch/Cap Gemini World Wealth Report 2007

### 3. Re-positioning the Luxembourg Private Banking centre

#### 3.2.2 Improve product and service richness

*“Luxembourg cannot focus only on portfolio management in the future. Luxembourg entities must find niche activities that differentiate themselves from competing entities.”*

Participant

*“The Luxembourg market is the only one within the EU offering a real cross-border approach, giving the unique possibility to operate as a real European player.”*

Participant

*“Private estate engineering is a key success factor for the Luxembourg private banking centre.”*

Participant

In order to be recognised as a key actor in the private banking landscape, Luxembourg must increase the depth of its services offering to enhance its differentiating factors and position itself clearly on the radar screen of the richest people in the targeted markets.

Luxembourg provides today some of the differentiating means and vehicles for servicing the upper clients segment who have international business interests and lifestyles, seek consistent, high-quality holistic advice and want an integrated and tailor-made financial planning approach.

Luxembourg has also developed a proven expertise in financial engineering solutions tailored to satisfy the specific requirements of clients willing to transmit, restructure, share and preserve their wealth with an international perspective.

But most of the players recognise that more has to be done to both improve the attractiveness of Luxembourg and increase customers' loyalty in order to develop the client base and increase the share of the clients' wallets the Grand Duchy is managing.

Only by continuously and consistently creating distinctive and added-value activities will Luxembourg remain in line with market demands, and position itself as a centre of excellence within the group thereby gaining group responsibilities in private banking, clients' referrals and recognition.

### 3.2.3 Attract talents and develop competencies

*“Competition will be increasingly based on talents: having the right people and adapting their skills to the changing facets of the business. We must search for excellence in order to serve upper-level clients.”*

Participant

*“Luxembourg offers highly value-added jobs in private banking, but we need to further promote such opportunities.”*

Participant

Luxembourg’s private banking growth ambitions will depend on its ability to recruit enough professionals from the wealth management industry. Private bankers expect to increase their CRM base by 9% annually over the next few years<sup>43</sup>.

This means that by 2015 Luxembourg will need at least 1,700 additional CRMs, not to mention other wealth management professionals such as: investment bankers, complex products specialists and experts in tax, estate, trust and property. It will be essential for Luxembourg to attract not only young graduates, but also experienced and recognised CRMs disposing of an average client portfolio above EUR 150 and 170 Mio in AuM, which is the average range in the Luxembourg market. Moreover, in order to maintain superior service while fitting the needs of more sophisticated clients and more complex products and services range, Luxembourg private banks must develop and upgrade its current CRMs’ advisory competencies and skills, mainly through training and higher exposure to the richest clients.

### 3.2.4 Build a strong and coherent brand

*“Why doesn’t Luxembourg put forward its advantages? Switzerland and Singapore do it.”*

Participant

*“The promotion of Luxembourg must also focus on attracting talents. We must promote Luxembourg at social, cultural and fiscal levels.”*

Participant

*“We need to move away from the offshore vision and promote a European and international vision.”*

Participant

Branding will be increasingly critical to the success of private banking in Luxembourg. While referrals from existing clients and cross-referrals from wider organisations will continue to be the main sources of new clients for Luxembourg, brand strength is expected to be the third major contributor to new assets<sup>43</sup>.

Branding will not only be vital to attracting clients and talents, but also to developing the visibility of Luxembourg entities within their groups, which will in turn facilitate the acquisition of European and/or international responsibilities.

To grow in the future, Luxembourg must build a strong and coherent brand to be conveyed consistently outside the country in the “institutional” community, “private” community, and within the group.

<sup>43</sup> Source: PricewaterhouseCoopers Global Private Banking and Wealth Management Survey 2007

### 3. Re-positioning the Luxembourg Private Banking centre

#### 3.2.5 Improve the operating model

*“Luxembourg private banks need to develop their current operating model to face expected growth. That must be achieved in part individually but also collectively by sharing activities.”*

Participant

In the highly competitive business landscape in which the Luxembourg private banks play, it is recognised that they must optimise their operating models to create sustainable value and attain their overall strategic objectives.

This will be achieved through consistent developments to:

- Adapt to the continuous impact of legal and regulatory evolutions;
- Improve the positioning of the Luxembourg private banking centre on the global landscape, and the positioning of Luxembourg entities within the group;
- Enhance innovation capacity to further develop the attractiveness of the Luxembourg private banking centre vis-à-vis European and non-European competitors;
- Align and share IT infrastructures as private banks will need the latest and best technologies available to satisfy information needs and serve sophisticated clients effectively.

#### 3.2.6 Invest more and faster in the development of private banking activities

*“The private banking sector should position itself to benefit from government investment in financial Research & Development.”*

Participant

Luxembourg private bankers and key stakeholders are confident about Luxembourg private banking centre’s capacity for growth, and Luxembourg authorities continue to state their support to the private banking industry.

Nevertheless, a finance plan specific to the development of private banking activities needs to be created to serve as a catalyst for the development of the whole industry, to facilitate the individual groups’ investments and to reinforce the link between the financial sector and the rest of the economy.

Current investments in the private banking industry need also to be reviewed given that the re-positioning of the Luxembourg private banking centre will require larger amounts of investments. Singapore and Dubai are heavily investing in the development of infrastructures and promotion specific to the private banking activity.

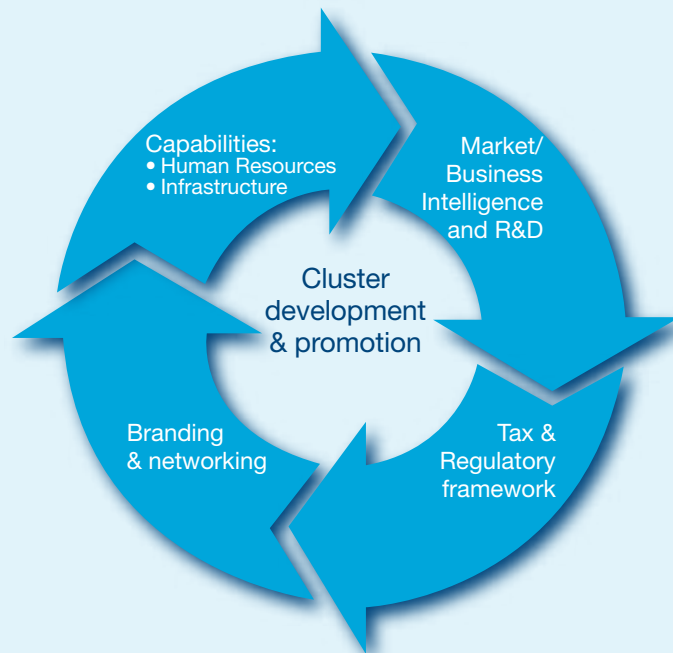
Finally, it is also essential to reduce the timing for investment decisions that are crucial to reinforce Luxembourg competitive advantages in areas such as Research & Development (R&D) and training.

# 4. Indicative Action Plan for 2012-2015

Achieving the targeted growth figures requires adopting an offensive strategy accelerating the development of key activities and key resources of the cluster. This can only be achieved through the collective collaboration of firms and all stakeholders and through reinforced investments.

Five interrelated strategic domains should be developed simultaneously to boost the competitiveness of the Luxembourg private banking centre (as seen in the figure below):

- Cluster development and promotion;
- Capabilities in terms of HR and infrastructure;
- Market/business intelligence and R&D;
- Tax and regulatory framework;
- Branding and networking.



## 4.1 Working together to develop and promote the cluster

*“It is not enough to desire, we need to provide ourselves with the necessary resources. In the coming months, we must come up with a concrete plan to present to the Luxembourg authorities.”*

Participant

*“A real partnership between private banks and authorities will make Luxembourg more competitive in the global financial landscape, resulting in new business.”*

Participant

*“The development of mutual activities represents a good way of reducing costs and sharing experiences.”*

Participant

The Luxembourg private banking cluster, even if it is still young, has encountered significant growth and real success over the last two decades, confirming its competitive

position on the European wealth management landscape. However, besides a few collective and ad-hoc initiatives, this success was mainly achieved through the individual efforts of key players.

The Luxembourg private banking industry should be inspired by the success of the fund industry cluster, which created its official representative body ALFI (Luxembourg Association of Investment Funds) in 1988 to be responsible of the promotion and development of the industry. Today, the ALFI counts almost 1,200 members including 12 associate members, approximately 15 full-time employees and three part-time employees who organise an internationally recognised annual conference on key industry trends. Although, we cannot expect the private banking cluster to develop like the investment funds cluster, because of its specific typology and because the market drivers are not the same, it is important to recognise the need to work together on private banking priorities for the years to come.

## 4. Indicative Action Plan for 2012-2015

One of the main reasons to develop the Luxembourg private banking cluster is the need to share activities in order to more proactively sustain growth, while maintaining costs at a reasonable level. Luxembourg stakeholders should increasingly recognise that they must improve their collaboration in order to be better placed to compete with other financial sectors.

### Collaboration means:

- Sharing recruitment efforts to attract qualified workers. Luxembourg private bankers recognise the need to attract together more high calibre professionals and develop competencies more consistently over a longer period of time in order to build long-term relationships with clients. As wealth management is a people business, human assets can have a particularly strong impact on organic growth. Consequently, attracting the best people to Luxembourg will be crucial for the development of private banking activities;

- Sharing training efforts to develop not only staff and client facing professionals but also managers. The development of accredited training, designed to respond to private banking and wealth management needs, goes hand in hand with Luxembourg's increased focus on quality of services. Effective training to improve CRMs' understanding of tax and regulatory changes, asset management strategies and new products (hedge funds), and client handling methods is certainly a domain on which there is consensus amongst private bankers;
- Sharing market intelligence, research and development infrastructures tailored to cover the needs of the private banking sector. Disposing of figures on the private banking sector is essential for Luxembourg to position itself vis-à-vis competing financial centres. Specific applied research projects dedicated to banking and finance need to be developed to maintain the innovation capacity that is needed to differentiate

Luxembourg from the other financial centres;

- Sharing service centres for managing technology, which is one of the key enablers of growth. Given the additional requirements imposed by rapid growth, increasing client expectations on business responsiveness and quality, and increasing regulatory and fiscal changes, IT management could become a burden for most of the small/medium Luxembourg entities if treated independently.

Based on the workshop discussions, we estimate that a dedicated entity working as an exchange platform and composed of key individuals having specific roles and encouraging mutual cooperation, knowledge sharing and arbitration, must lead the development of the cluster and ensure the implementation and coordination of the actions to reach the vision.

According to the experience gained in other financial services and in other clusters around the world, **we suggest a series of actions to be undertaken in the months to come:**

1. Set-up working groups with regular frequency of meetings, in which all private bankers are represented as well as key stakeholders such as PFS, lawyers, university, regulators and authorities;
2. Define the objectives of each working group. Each member must understand her/his role and each working group must have one strategic objective (HR, market and business intelligence, R&D, tax and regulatory, branding and networking, infrastructure);
3. Define three actions to be implemented, one of which must be implemented in the very short-term (maximum 6 months). Cluster development will need to hold the commitment of stakeholders by generating early

benefits. Therefore, it is important to quickly go through the phase of setting-up a structure in order to start developing business cases for each working group as early as possible;

4. Obtain the resources required in terms of employees and financial means;
5. Launch the cluster with key stakeholders in a dedicated event.

Actively promoting the private banking cluster vis-à-vis Luxembourg authorities and externals is also an important task to ensure their support and commitment. The Private Banking Group Luxembourg would be the most appropriate entity to lead this initiative. But an agreement between all stakeholders on the overall promotion strategies of the Luxembourg private banking centre is needed before launching an international campaign.

## 4.2 Attracting and developing the expertise for serving new target clients

*“Private banking is a real people business for which you need longstanding relations to build trust.”*

Participant

*“Currently, the Luxembourg School of Finance has 12 students, but we will need 1,700 CRMs! We must have a much larger educational program and also attract talents from abroad.”*

Participant

As private banking is a people business, disposing of sufficient and highly skilled human resources is essential. Like competing financial centres, Luxembourg’s private banking growth ambitions will depend on its ability to attract and develop skilled staff. The human capital investment required for growth is significant: approximately 1,700 additional CRMs will be needed by 2015 as well as a significant number of

other professionals from the wealth management industry. In addition, competencies must be aligned to ensure a high level of service quality in servicing more sophisticated needs of the upper client segments and more complex products and services offering.

### 4.2.1 Attracting talents

The availability of skilled personnel is the most important competitive factor across international financial centres today<sup>44</sup>. To gain recognition, Luxembourg must consistently attract in the years to come highly skilled professionals.

We believe that in order to define an effective recruitment strategy, the Luxembourg private banking cluster must conduct a “needs analysis” in order to identify:

- Which competencies are required?
- What is the targeted profile of new recruits in terms of geographical origin, technical and soft skills, spoken languages, professional and educational backgrounds?

- What will be the real number of workers required in each field by 2012-2015?

Developing a promotional campaign specifically designed to attract international wealth management career professionals is crucial to create awareness of the opportunities offered by the Luxembourg private banking market, still unknown even in neighbouring countries.

A strong cooperation between Luxembourg private banks and the promotion agency in charge of developing the Luxembourg financial centre is required to make sure that attracting talents is a key priority, not a secondary goal.

<sup>44</sup> Source: “The Competitive Position of London as a Global Financial Centre”, November 2005

## 4. Indicative Action Plan for 2012-2015

Concrete promotional actions concerning the whole financial sector in Luxembourg should include:

- Organising a collective financial recruitment forum in Luxembourg twice a year, highly promoted abroad to attract recruits. In France for example, a number of recruitment fairs are organised with firms from a given industry;
- Luxembourg firms participating collectively in business schools' recruitment forums abroad in a "Discover Luxembourg Opportunities" stand;
- Developing partnerships between the Luxembourg financial centre and well-known international universities for internship in order to allow students to discover Luxembourg's opportunities. Singapore for example has developed a cooperation agreement with some of the best business schools worldwide, such as the INSEAD, Berkeley and MIT.

Luxembourg private banks will need to expand the geographical scope of their current recruitment strategy in order to respond to the actual market pressure. To facilitate that, the Luxembourg government has recently lifted restrictions on the 8 new EU member countries<sup>45</sup> and a new law should be adopted to facilitate the delivery of work permits for non-Europeans as well. Granting temporary work permits to non-European students attending a Masters Degree in Finance at the University of Luxembourg would also be a short-term beneficial action.

### 4.2.2 Developing competencies

Luxembourg private bankers have recognised the importance of building a more coherent educational system to sustain the business development. The objective of educational and training structures should be three-fold:

- Train young wealth management professionals in order to respond to the needs of the Luxembourg private banking sector;

- Raise the capabilities of Luxembourg's existing talent stock (knowledge of a broad array of financial instruments and skills to deepen client relationships);
- Provide the banking groups that are present in Luxembourg with a training platform on Luxembourg' specific vehicles and achieve international industry recognition. In this sense, it is very important to develop an accredited and internationally recognised label for training.

The IFBL Certified Private Banker, a 180-hours high-level executive programme launched in 2008, as well as the "Private Banking Training Program" to be launched in association with the University of Luxembourg, are good starting initiatives. However, in the workshop discussions with Luxembourg private bankers, there was a consensus that these training structures should be developed on a larger scale in order to respond to the actual and future demand of the wealth management industry.

This could be materialised through the creation of a large offer of financial education programs not only designed to produce a pipeline of well-trained graduates ready to pursue financial careers, but also to upgrade the skills of experienced and senior executives.

Similar training and development initiatives have proved to be a success. In 2003, Singapore launched a wealth management institute with the support of the local authorities, who reimburse students 70% of program fees if they pass the course and get a job in the industry within a year. The Swiss Banking School, in cooperation with four Swiss and one American university, created the first executive MBA program in international wealth management, which includes courses both in Switzerland and in the US.

<sup>45</sup> Estonia, Latvia, Lithuania, Poland, Czech Republic, Slovakia, Hungary, and Slovenia



## 4.3 Building the right tool to anticipate market evolution

*“Knowledge intelligence is needed; for instance a comparative study on international tax frameworks would be highly valuable.”*

Participant

*“Products such as the SIF and SICAR allow an enhanced service approach for niche clients.”*

Participant

### 4.3.1 Developing the knowledge base

Knowledge, encompassing research, is a key success factor of most financial centres. Luxembourg private bankers want to develop three pillars of knowledge:

- **Market and Business Intelligence.** Market and business intelligence consists of acquiring and analysing market information to assess its own positioning and the business

environment that may affect the size and nature of the market in the future. Gathering solid data on the Luxembourg private banking cluster is an important step in understanding its positioning and opportunities and in identifying capability gaps.

We believe that in order to plan the future, Luxembourg must first dispose of significant figures and data on its private banking centre because these will impact the overall cluster and branding strategy.

Therefore, gaining market intelligence is a key priority for the short-term of the cluster. The recently launched CODEPLAFI study is a good start but is not sufficient. We think that the Luxembourg private banking cluster should, in the next 6 months, have a clearer view of the wealth management industry and its best practices. An example of business intelligence subject is the analysis of the economic impact of

recently introduced vehicles (such as the SIF and the SPF, which encountered a great success), in terms of additional revenues, clients, jobs, and service providers. Such results would be beneficial in promoting innovation to Luxembourg’s authorities.

- **Market Watch.** Carrying out regular benchmark analysis on each of Luxembourg’s strategic objectives (HR, market and business intelligence, R&D, tax and regulatory, branding and networking, and infrastructure) vis-à-vis the competing financial centres is essential to maintain Luxembourg’s competitive positioning in the global landscape.

Private bankers have to create a Tax Market Watch, shared between members of the private banking cluster, in order to permanently monitor national and international regulatory and tax frameworks evolution at all levels and leverage on new ideas.

- **Research & Development.** Luxembourg entities plan to continue to differentiate themselves through quality of advice with strong focus on the provision of comprehensive, integrated wealth management planning solutions and product innovation<sup>46</sup>. Innovation adds value to the group and allows the improvement of the Luxembourg entity’s positioning within the group, enabling the acquisition of European and/or international responsibilities. In this context, the mutualisation of research and development structures specific to the private banking sector would be beneficial for the development of activities. Promoting applied research focusing on wealth management is a current practice in competing private banking centres. In 2001, the Swiss National Science Foundation launched the National Centre of Competence in Research with the objective of promoting research focused on the dynamics of wealth creation and redistribution.

<sup>46</sup> Source: PricewaterhouseCoopers Global Private Banking and Wealth Management Survey 2007

## 4. Indicative Action Plan for 2012-2015

In the coming years Luxembourg will have to innovate a lot more than it did in the past. Luxembourg's innovation strategy should rely on three pillars:

- ◆ strengthening the innovation capacity;
- ◆ improving the economic and legal framework for innovation;
- ◆ improving information security and trust management.

### 4.3.2 Defining a structure and achieving commercialisation

Traditional private banking services should be constantly adjusted to the needs of the client, as well as to changes in the regulatory and tax framework. Therefore, research subjects must be defined in close collaboration with the industry.

There are two concrete examples of research subjects needed to be carried out in Luxembourg:

- One relates to the development of new vehicles. We think it is necessary to make an inventory of the wealth management vehicles currently existing in Luxembourg and in the competing financial centres, and then conduct an opportunity and risk analysis to identify which products and services should be developed in Luxembourg;
- The other concerns the development of a prototype for the Luxembourg Philanthropic Foundation defining the characteristics of a fiscal and legal environment adapted to foundations. HNWI are increasingly eager to make donations to charitable entities. In 2006, 9% of HNWI requested philanthropic offerings and allocated as much as 4.6% of their portfolio to such investments, raising a total of USD 27 Bn<sup>47</sup>. This is a potential

opportunity for Luxembourg to develop a service offering and position itself in this segment. The development of this prototype must be done as soon as possible in order to start the discussions phase with the Luxembourg authorities.

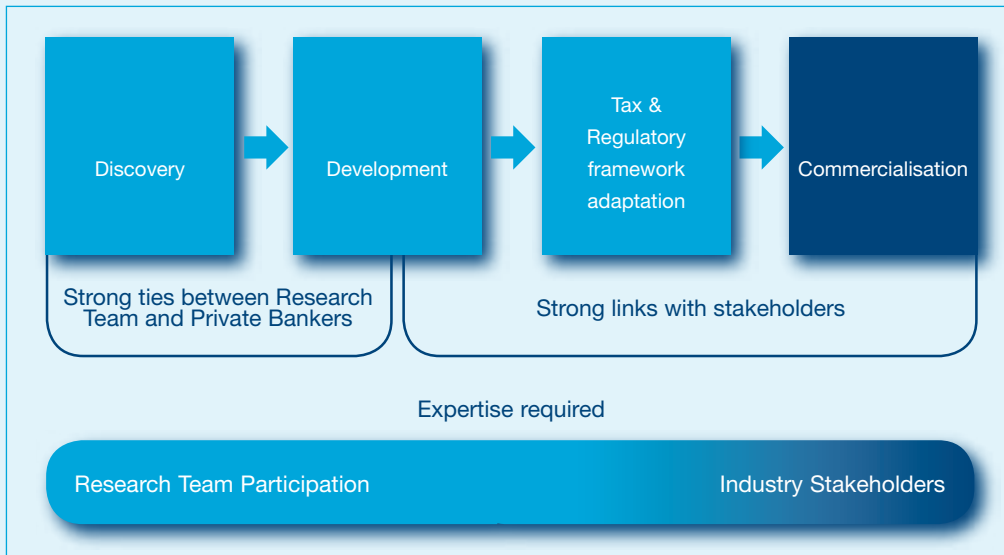
We think that in order to develop sustainable R&D, the Luxembourg private banking cluster must define the structure or the entity in charge of carrying proactive research. It should be a multi-disciplinary, well-adapted structure, in which researchers and the industry collaborate continuously. This structure should attract a few internationally recognised professors in the financial field who will in turn attract students and other professionals.

The University of Luxembourg must be a major partner in this initiative and should dispose of the resources needed to develop such a program. An adjustment of current competencies is required in order to better respond to the needs of the financial industry, and partnerships with foreign universities disposing of a track record should be signed in order to accelerate the development phase. Working with foreign universities could help increasing the Luxembourg financial centre's recognition abroad. As an example, the "Swiss Finance Institute", created in 2006 with the objective of providing the Swiss financial sector with latest applied research in banking and finance, has already signed partnerships with Geneva, Lausanne, Lugano, and Zurich universities.

<sup>47</sup> Source: Merrill Lynch/Cap Gemini World Wealth Report 2007

In addition to the structure, it is essential to create an applied research plan for the development of new vehicles and wealth management theories. The focus should be on reducing the commercialisation period, as the speed with which new products and services are brought to the market is a major barrier to more constructive collaboration between universities and practitioners. Thus, it is essential to operate at a faster pace and transform research into real economic activity, reducing the lag time between discovery and commercialisation of products and services.

### Discovery to Commercialisation – Reducing the lag time



### 4.4 Addressing key tax and regulatory priorities to enhance competitiveness

*“Some tax & regulatory measures would be very beneficial to the Luxembourg private banking centre, such as the development of a philanthropic foundation, and a foundation of private family right or the enlargement of the DTT network.”*

Participant

The regulatory and tax framework has a crucial role to play in the growth of the private banking sector. The government must support the Luxembourg private banking industry by strengthening competitiveness in tax matters and through the enhancement of the legal and regulatory framework while maintaining a level playing field across Europe.

Luxembourg must proactively continue to ensure an optimal tax and regulatory environment for business in order to remain

competitive in the global landscape. As previously said, it is important to carry out a tax market watch to monitor continuously the regulatory and tax frameworks of competing private banking centres.

According to Luxembourg private bankers, today there are four tax and regulatory priority measures aimed at enabling growth in the private banking sector:

- Enlarge the Luxembourg Double Tax Treaty (DTT) network<sup>48</sup> and scope. Currently, Luxembourg has a limited number of DTTs signed (52 in total) compared to other countries<sup>49</sup>, covering income and property taxes only. By increasing the number of partners, Luxembourg would help give legal security to both its residents and business partners. This would also increase visibility on the tax treatment of income. This would be part of a bilateral and multilateral cooperation strategy with a view to eliminating double taxation but also to preventing

<sup>48</sup> Luxembourg DTTs are being negotiated in the following 13 countries: Azerbaijan, Bahrain, Georgia, India, Kazakhstan, Kuwait, Lebanon, Moldova, Montenegro, Serbia, Ukraine, United Arab Emirates and United Kingdom.

<sup>49</sup> France has signed 113 DTTs covering income, property, inheritance, gift taxes, and 13 new agreements are being negotiated. Switzerland has signed 75 DTTs. Belgium has signed 88 DTTs, and 13 new agreements are being negotiated. The UK network counts 113 DTTs.

## 4. Indicative Action Plan for 2012-2015

tax fraud and tax evasion on a global scale. Countries showing potential opportunities for a DTT include, Argentina, Australia, Chile, India, Kuwait, Monaco and Saudi Arabia.

- Improve taxation on exit rights and set-up a favourable tax regime for the transfer of business. This would help attract entrepreneurs to Luxembourg thanks to the absence of any DTT in terms of inheritance or gift taxes. In the meantime, Luxembourg should establish a pay-off system addressing capital gains in the case of transfer upon death. This would allow inheritors to get rid of latent capital gains that could have been rolled over since the set-up of the business, sometimes one or two generations earlier.
- Develop an efficient tax and regulatory environment for the creation of a philanthropic foundation, like in Belgium, Switzerland, the United Kingdom or the US. The use

of a Multi-Donors Trust Fund (MDTF) vehicle would be a professional solution. To achieve such a model, the MDTF must appear as a reference and the commitment of several private banks is required, as well as recognition by the public sector. In return, it would be a window to Luxembourg and the corporate social responsibility of the banking sector.

- Create an efficient tax and legal framework for a foundation of private family rights. This foundation would meet the needs of individuals looking to transfer their estate to relatives and friends or to third parties. Since the estate allocated to the foundation would not be part of the founder's assets, no gift or estate tax would be levied in the hands of the beneficiaries. The foundation could also benefit from simplified accounting requirements. The parties could also remain anonymous if the founders and beneficiaries' names did not have to be made

public. This type of foundation would enable Luxembourg to remain attractive to HNWI and help develop upscale private banking services in Luxembourg. Such a foundation may also help compensate for the absence of bilateral instruments relating to gift and estate taxes.

### 4.5 Strengthening the Luxembourg Private Banking branding

*“If we want to get more international it requires, not only the individual effort of each player, but also the collective effort of the industry.”*

Participant

*“We must promote Luxembourg towards the outside and inside the group. Market intelligence is essential for positioning and promoting Luxembourg in a global environment.”*

Participant

Private banking is an industry that, more than any other sector of financial services, must promote strong up-market brand values to attract and retain valuable wealthy clients<sup>50</sup>. Branding and networking development must result from joint efforts of all private bankers, government bodies and professional associations. The creation of the promotional agency “LuxembourgforFinance”, a private public partnership (PPP) between the Luxembourg government and Profil is a promising start. However, the Luxembourg cluster needs a dedicated team specifically in charge of the promotion of private banking activities, aligned with private bankers' objectives.

<sup>50</sup> Source: Private Banker International, September 2007

#### 4.5.1 Building a brand and identity

The first step in building a valuable brand for the Luxembourg private banking centre is the completion of a dedicated study clarifying:

- Who are the Luxembourg private banking cluster's key target audiences?
- Where are they located? The geographical scope of trade missions must then be adapted accordingly.
- What are Luxembourg's real competitive advantages? How is Luxembourg currently positioned vis-à-vis other private banking centres?
- What are the short and long-term actions required to improve Luxembourg's reputation abroad and within the group?
- What is the budget needed?

#### 4.5.2 Promoting the brand

The second step is promoting Luxembourg's private banking competitive advantages across the different target markets. Although clients and banking groups are starting to recognise that a good range of important private banks are present in Luxembourg, offering a broad product and service range, they can not distinguish Luxembourg's competitive advantages. This is confirmed by the fact that almost half of Luxembourg private bankers are currently focusing on the familiarity stage<sup>51</sup> of their branding strategy to attract new clients.

The promotion of the Luxembourg private banking brand should be delivered through different channels, including public relations, networking, and marketing tools such as a dedicated website, brochures and presentations.

To efficiently promote the Luxembourg private banking cluster the first action could be the creation of a "Why Private Banking in Luxembourg?" brochure, adapted to different target audiences, promoting the attractiveness of Luxembourg for:

- ◆ private clients;
- ◆ young graduates looking for international financial careers and experienced professionals in search of career development;
- ◆ headquarters and group entities;
- ◆ intermediates and other financial centres;
- ◆ service providers.

The second action could be to identify:

- Which are the best networks?
- Who are the best ambassadors of these networks?
- Which ones have the greatest multiplier effect?

This action is essential to optimise the promotion effects in the countries where we see the greatest potential of expansion for the private banks.

#### 4.5.3 Adapting continuously the brand

Best practices show that a brand must continuously be adapted to the changing environment and to new objectives in order to remain relevant. Thus, it is key to regularly reset brand goals and redefine the identity of the Luxembourg private banking cluster.

For that it is important to have people who travel and meet clients in foreign countries to understand how Luxembourg is perceived abroad.

<sup>51</sup> There are four stages of branding: 1. Familiarity, 2. Positioning, 3. Differentiation, 4. Emotional power. Whereas Luxembourg private banks are at the first stage of familiarity, Swiss private banks are on average on the third stage of differentiation. Source: PricewaterhouseCoopers Global Private Banking and Wealth Management Survey 2007

## 4. Indicative Action Plan for 2012-2015

### 4.6 Improving Luxembourg infrastructures as a vector for growth

*“In order to promote Luxembourg to talents, clients, and the group, efforts must be done to develop Luxembourg’s accessibility, leisure and educational infrastructures.”*

Participant

Following the workshop discussions with Luxembourg private bankers, there are two types of infrastructure on which Luxembourg must work in order to facilitate the growth of the private banking sector:

#### 4.6.1 Infrastructure related to the financial sector, and specifically to the private banking industry

It is essential for private bankers to develop infrastructures collectively as a cluster. An example of a service that can be put in place between private bankers to decrease the administrative burden and costs is mutual tax reporting. The creation of an Economic Interest Grouping (EIG)<sup>52</sup> would facilitate the coordination of

the shared tax reporting service. The EIG could centralise information sent by the private bankers for a single client in order to help with synthesising taxable income that has to be reported either in Luxembourg or abroad. Alternatively, the role of the grouping could be limited to the maintenance of a format of tax reporting for each jurisdiction, which would be available to each member. The tax reporting service could use a kind of unique fiscal paper, and this should be the first priority to be proposed to Luxembourg tax authorities.

Disposing of an effective integrated national financial sector value chain is also key. The Swiss financial centre has a strong value chain, benefiting from a system whereby the three stages in a securities transaction – trading, clearing and settlement, and payment – are fully integrated online. Three organisations have been instrumental in the development of the Swiss value chain: the SWX Swiss Exchange (for trading), SIS SegalInter-Settle (for clearing and settlement) and Swiss Interbank

Clearing (for payments). Today, the Swiss value chain not only eliminates risks, but it also enables the banks to transact at low costs.

The same could be applicable in Luxembourg with a clear integration between the Luxembourg stock exchange, a transaction bank dedicated to private banking activities, and all the private banks acting as front office managing their clients. Some partial models exist already and eventually there is a case for a larger and national one.

#### 4.6.2 Infrastructure related to the entire economy

Luxembourg is positioned as the 25<sup>th</sup> most competitive country in the world according to the Global Competitiveness Report 2007-2008<sup>53</sup> conducted by the World Economic Forum. Luxembourg disposes of a good basic infrastructure which is continuously evolving. Examples of recent developments include the creation of a new terminal for the Luxembourg Airport, to be launched in April 2008; the new urban centre being created at Esch-Belval that

should host schools, institutions and offices; and the building of a second European School at Mamer.

However, improving the access to Luxembourg, as well as its cultural and educational (basic, higher and continuous education) infrastructures are important steps to develop the cluster and to attract business, clients, and workers willing to take up new employment opportunities.

As the Zurich private banker Hans J. Baer states, the success of Swiss private banking relies partially on its infrastructure: “Private banking is the full range of services that a client may wish to obtain and this therefore extends way beyond wealth management. Swiss private banking starts at the three international airports in Zurich, Geneva and Basel and continues via the railway stations and luxury hotels of our country right up to the doors of Sprüngli’s cake shop. Swiss private banking encompasses our hospitals, cultural institutions, media, lawyers, shops, schools, universities and, of course, our banks and asset managers”.

<sup>52</sup> An EIG is a vehicle which allows companies or individuals to combine and register a grouping which has a legal personality. Source: Gateway to the European Union.

<sup>53</sup> Competitiveness was measured through 12 factors: institutions, infrastructure, macro economy, health and primary education, higher education and training, goods market efficiency, labor market efficiency, financial market sophistication, technological readiness, market size, business sophistication, and innovation.

## 5. Moving forward with leadership, energy and agility

As presented in the previous chapters, the vision of the expected development and competitive re-positioning of the Luxembourg private banking cluster for the horizon 2012-2015 is challenging but focused on the key issues at stake for the future of the Luxembourg financial centre: war for talents, increased contribution of private banking to the Luxembourg economy, and markets positioning.

Raising the combined AuM to EUR 1,000 Bn will require the proactive mobilisation of all stakeholders – private, institutional, and governmental – in a shared initiative where risks and opportunities must be proactively assumed by all participants.

Even if the global market for wealth management services is very fragmented and has already recognised activity hubs, the pressure fuelled by the new challengers should bring significant changes in the business landscape and affect the competitive positions of private banking centres. In this respect, the recent major investment of the Government of Singapore Investment Corporation in the capital of UBS illustrates this movement of re-architecting the comparative capacities of private banking clusters.

The Luxembourg financial centre, and especially its private banking cluster, is confronted with the practical necessity of moving forward in order to be part of the new phase of growth in AuM and consequently of the international redistribution of wealth management activities. Historically, Luxembourg has moved rapidly as a European member state in the creation of competitive advantages for firms involved in private banking and, ex-post, being proactive has proved to be advantageous for the country. The same logic applies today thanks to this new window of opportunities that is accessible to Luxembourg for the next five years if it moves forward with energy and agility.

Based on the workshops held, the analysis, the shared diagnostics with all stakeholders of the private banking sector of Luxembourg, and the Banking Day conducted with the CEOs of the industry, the implementation of the Action Plan for 2012-2015 should be driven with engagement and clear leadership. The small size of Luxembourg's economy and its institutional configuration provide the country with a strategic advantage over its competitors that are running for the same vision and opportunities for development. However, a lack of engagement and leadership from the Luxembourg private banking cluster could be really counterproductive to the future positioning of its wealth management practice and reputation.

## 5. Moving forward with leadership, energy and agility

Getting to the success implies that:

- The **leadership for the implementation and follow-up of the action plan should be assumed by the industry** and via its representative body, the Private Banking Group Luxembourg (PBGL), which should set-up working groups in close collaboration with the ABBL specialists to move forward on the key projects defined in the action plan. The PBGL should start defining its operational plan for the next two years, including very short-term actions to be put in place in the coming six months to guarantee the build up of a strong momentum for development matching the level of expectations related to the accomplishment of the vision.
- The action of the PBGL should be done in close **partnership with all the other stakeholders involved in the future of the private banking** activity in Luxembourg: the ABBL, the government, the regulator, the university, the Fonds National de la Recherche, other industry associations and all categories of firms and service providers directly related to private banking. **Synergies with the Luxembourg funds management industry via ALFI** should be considered for the enhancement and strengthening of Luxembourg's strategic position in the domain of wealth management.
- The **Luxembourg government**, under the leadership of its Minister of Finance, should on one hand set a **high level committee** of top public civil servants and administrators dedicated to partnership discussions with the representatives of the cluster in relation to the advancement of the projects that will be generated from the action plan. The Luxembourg government should on the other hand, therefore, dedicate specific funds to the development of the private banking cluster.
- In the first semester of 2008 clear and applicable business cases should be developed by the working groups in order to develop a series of projects simultaneously. Isolated actions would not be sufficient to achieve expected growth. At a later stage, a Luxembourg Wealth Management Institute could be created to coordinate all the initiatives around the development of private banking activities: HR development, R&D, competitive intelligence and international wealth management clusters evaluation and benchmarking, and promotion. The Luxembourg Wealth Management Institute would serve as a label for the private banking centre to increase recognition, attract talents, and even train CRMs within the Group as a European training platform.

The first months of 2008 will be decisive in the creation of a continuous momentum for effective action clearly oriented to the future development of private banking in Luxembourg.



# Appendices

# Appendix 1

## List of Acronyms

ABBL	Association des Banques et Banquiers, Luxembourg
ALFI	Association Luxembourgeoise des Fonds d'Investissement
AuM	Assets under Management
CODEPLAFI	Comité pour le Développement de la Place Financière
CRM	Client Relationship Manager
CSSF	Commission de Surveillance du Secteur Financier
DTT	Double Tax Treaty
EIG	Economic Interest Grouping
HNWI	High Net Worth Individuals
MDTF	Multi-Donors Trust Funds
MiFID	Market in Financial Instruments Directive
PBGL	Private Banking Group Luxembourg
PFS	Professionals of the Financial Sector
SEPA	Single Euro Payments Area
SICAR	Société d'Investissement en Capital à Risque
SICAV	Société d'Investissement à Capital Variable
Soparfi	Société de Participation Financière
SPF	Société de Gestion de Patrimoine Familial à Luxembourg
UCITS	Undertaking for Collective Investment in Transferable Securities
UHNWI	Ultra High Net Worth Individuals
VHNWI	Very High Net Worth Individuals

# Appendix 2

## List of Participants to the workshops held on the “Future of Luxembourg Private Banking”

- Association des Banques et Banquiers, Luxembourg (ABBL)
- Banque Degroof Luxembourg S.A.
- Banque et Caisse d’Epargne de l’Etat, Luxembourg
- Banque Privée Edmond de Rothschild Europe
- BNP Paribas Luxembourg
- Crédit Agricole Luxembourg Private Bank
- Credit Suisse (Luxembourg) S.A.
- Dresdner Bank Luxembourg S.A.
- EFG Private Bank (Luxembourg) S.A.
- Fuchs & Associés Finance Luxembourg S.A.
- HSBC Private Bank (Luxembourg) S.A.
- HVB Banque Luxembourg Société Anonyme
- ING Luxembourg S.A.
- Kredietbank S.A. Luxembourgeoise
- Landsbanki Luxembourg S.A.
- Lloyds TSB Bank Plc, Luxembourg branch
- Luxembourg Finance Ministry
- Petercam Luxembourg
- Sal. Oppenheim Luxembourg
- Skandinaviska Enskilda Banken S.A.
- Société Européenne de Banque S.A.
- Société Générale Bank & Trust
- UBI Banca International S.A.
- UBS (Luxembourg) S.A.
- University of Luxembourg
- Victor Buck Services S.A.



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