



Clarity on Transformation in Private Banking

Partnering for growth

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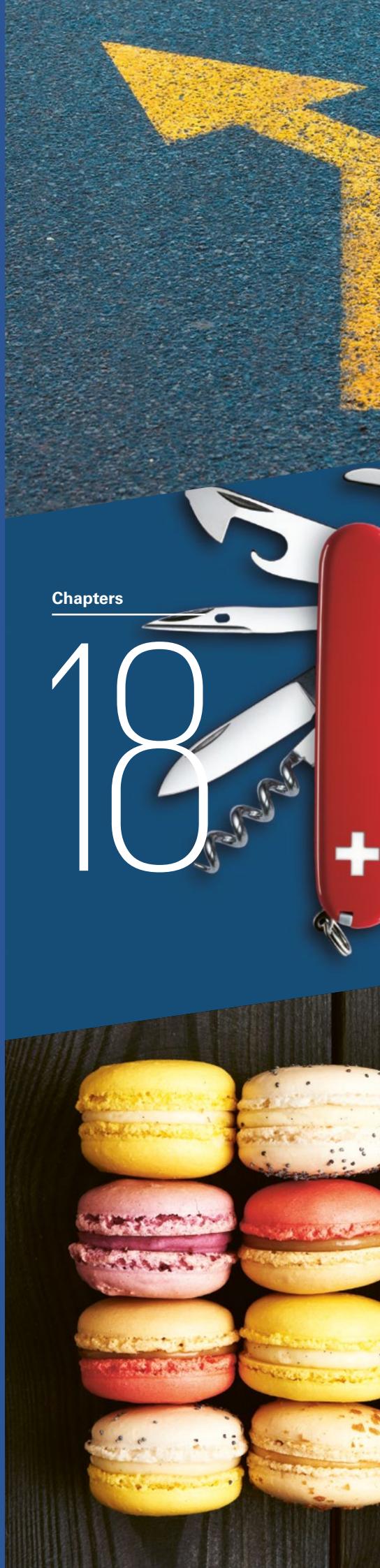


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Clarity on Transformation in Private Banking Partnering for growth

A white paper by KPMG AG Switzerland,

in cooperation with the Business Engineering Institute – Competence Center Sourcing (CC Sourcing), the Institute of Information Management at the University of St.Gallen (HSG) and the University of Leipzig.

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Building competitive advantage through collaboration

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Swiss private banking is progressively entering a new phase. Whilst regulatory-driven changes are still high on the agenda, there is an increasing focus on commercially-driven transformation. Growth is becoming again a key topic for banks.

In this report, we look at the future of Swiss private banking through the lens of such commercially-driven transformation. Our statement is that in order to survive, Swiss private banks need to rethink their businesses. This implies prioritizing their core differentiating strengths, while looking for collaborative solutions with high-quality partners capable of delivering more effectively the bank's non-core activities. Such a combination will maximize value-add for both clients and banks themselves.

There are many ways to approach such strategic partnerships. We strongly believe that holistic ecosystems with a high degree of closeness among partners – referred to as an "US" approach – allow the fostering of sustainable growth.

Thanks to technology and other factors, there are more opportunities to build such ecosystems today than at any time in the past. However, the complexity to do so should not be underestimated either.

Those banks that are willing to take up the challenge stand a very good chance, in our opinion, of finding the way forward.

We hope you find our insights in this paper interesting, and we would be delighted to discuss further these topics and their possible implications for your organization with you.

**Philipp Rickert and Christian Hintermann,
KPMG Switzerland**

Paradigm shift



Although regulatory-driven change is a prerequisite to operate, long-term sustainability will come from commercially-driven transformation. Banks are now at an inflection point between these two change drivers.



Identifying Unique Selling Points (USPs)

Future growth will only come from an in-depth understanding of what really matters for the client and being able to deliver accordingly or beyond. Therefore, it is necessary for banks to clearly identify, focus on and leverage their USPs, while continuously placing the client at the center of the reflection.



From integration to disaggregation

Strategy is about knowing what to do as well as knowing what not to do. Value maximization therefore comes from a refocus on key USPs combined with a strategic disaggregation of the banking value chain for lower client value-add and non-core activities.



Rationality versus emotionality

Although doubts, uncertainties and worries are common when considering radical change such as outsourcing and the like, banking executives can overcome emotional obstacles by following a systematized approach based on facts and rationality.





Think holistically and systematically, think "US"

A systematic assessment of both the business and operating models allows the most suitable disaggregation models to be selected, thereby unleashing the full potential of strategic partnerships, the so-called "US" approach.



Path to competitive advantage

Through effective collaboration with various partners capable of adding more value in performing non-core activities, banks will progressively build true ecosystems. Such ecosystems have the potential of maximizing client benefits, as well as fueling a sustainable competitive advantage going forward.

Key recommendations



GETTING GROWTH BACK ON TOP OF THE STRATEGIC AGENDA

- Swiss private banks have to ask themselves difficult questions:
 - Can we afford the status quo?
 - Should we exit the market?
 - Alternatively, how can we transform to grow?
- Whilst regulatory-driven changes remain very important, private banking C-level executives who decide to stay have to continue to increase their focus on commercial development to reignite growth, as some large competitors are already moving fast on these topics.
- Senior management has to allocate significant efforts to commercially-driven transformation. In turn, this will require banks to develop or acquire specific expertise, while reinforcing their client-centric stance.

GIVING CLIENTS WHAT REALLY MATTERS TO THEM

- Whilst many Swiss private banks have historically delivered the full array of services themselves, it is time to re-concentrate on what brings tangible value to the client. We recommend board members and executives conduct a thorough analysis to identify the real USPs of their organization. They have to determine what differentiates them in the competitive arena and, most importantly, what clearly matters to their clients.
- Banks should then reinforce and develop further these strengths or core assets to maximize client value-add and satisfaction.
- For those non-core activities identified when assessing the end-to-end value chain, private banks should objectively evaluate tactical ("THEM") or strategic ("US") collaboration alternatives to have these services delivered more effectively and/or efficiently.



DEVELOPING AN ECOSYSTEM FOR SUCCESS

- Since cooperation generally entails a high level of complexity, board members and executives can typically face uncertainties and doubts. To overcome such psychological challenges, they have to use a structured and fact-based framework to support the sourcing decision-making process.
- Banking management should holistically assess each building block of the business and operating models to identify partnering opportunities.
- Sourcing, partnerships and the like carry particular risks of their own (e.g. strategy, selection, implementation, people, or management risks). Banks need to develop careful mitigation strategies.
- Achieving the expected ROI of cooperation requires specific transformation expertise in order to properly manage implementation as well as new managerial skills to sustain the effectiveness of partnerships in the long run.
- Private banks should aim at progressively developing multiple cooperative interactions, hereby building true ecosystems, which in turn will typically generate more value to partners and clients than the sum of their parts.



BUILDING A SUSTAINABLE COMPETITIVE ADVANTAGE

- Senior executives have to be aware that multiple partnerships based on trust, reinforced by contracts, as well as possible operational links are particularly difficult to replicate, thereby generating a true competitive advantage.
- In order to maintain the competitive advantage gained by developing an ecosystem, private banks should aim at continuously broadening and deepening the extent and quality of the collaboration with partners.



SWISS PRIVATE BANKS AT THE CROSSROADS



Swiss private banks have had a difficult decade. The financial crisis, the end of banking secrecy and the tsunami of new regulations has heavily impacted their profitability and challenged their business models. Today, many Swiss private banks find themselves at a crossroads. It has become evident that those who want to stay in the market will have to transform. This implies asking difficult questions about themselves, facing the emotional and organizational challenges of change, and being open to - sometimes radical - new ways of thinking.

After the fall: Swiss private banking in a post-crisis world

The last ten years have been a difficult time for Swiss private banks.

First, there was the financial crisis, which damaged trust in banks generally. Wealthy clients of Swiss private banks – many of whom lost a great deal of money in the downturn – no longer believed in their bankers' wisdom, foresight and expertise. Then came the cross-border tax issue, sounding the death knell for bank-client confidentiality and with it the promise of complete discretion.

However, of all the challenges of the last decade, the tsunami of new regulatory requirements has probably been the hardest. New cross-border regulations, MiFID, and the like have driven up the cost and complexity of doing business. FATCA, RUBIK, the Department of Justice Swiss Bank Program and tax amnesties have made tax compliance even more difficult. Banks have had to react on a number of fronts. This has diverted private banks from core banking, revenue-generating activities.

Despite the fact that their business models have been fundamentally challenged, over the past decade, many banks have not been able to make all the necessary transformations, with resources solely absorbed by regulatory-driven transformation.

RIGHTING THE SHIP

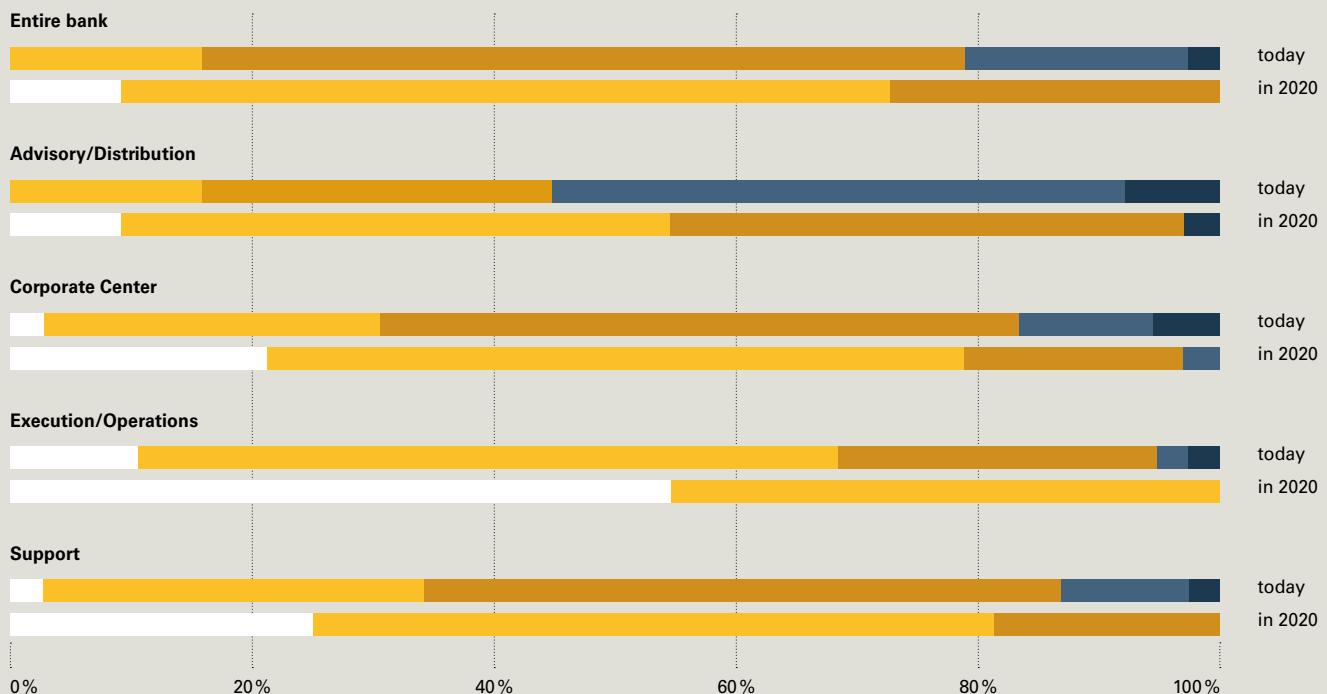
Under intense compliance scrutiny for the first time, Swiss private banks combed their client books looking for tax and other issues. Those clients who wanted were helped to become compliant, others were no longer serviced. However, as many banks learned, cleaning up the client book did not always fix the legacy issues. Banks therefore had to develop risk mitigation strategies as well. All of this cost money, whether in terms of staff, systems, legal fees, litigation provisions or – in some cases – fines.

Banks also started time-consuming and expensive projects to meet new legal requirements. They adjusted operating models, standardizing and automating where possible, to satisfy new compliance rules. Though much was accomplished, many hurdles remain. For one, - although less intense - the regulatory pressure continues. New rules – including Automatic Exchange of Information (AEoI) and FIDLEG – will mean additional painful adjustments. Regulation has also put constraints on the cross-border business model, making it difficult to attract new offshore clients.

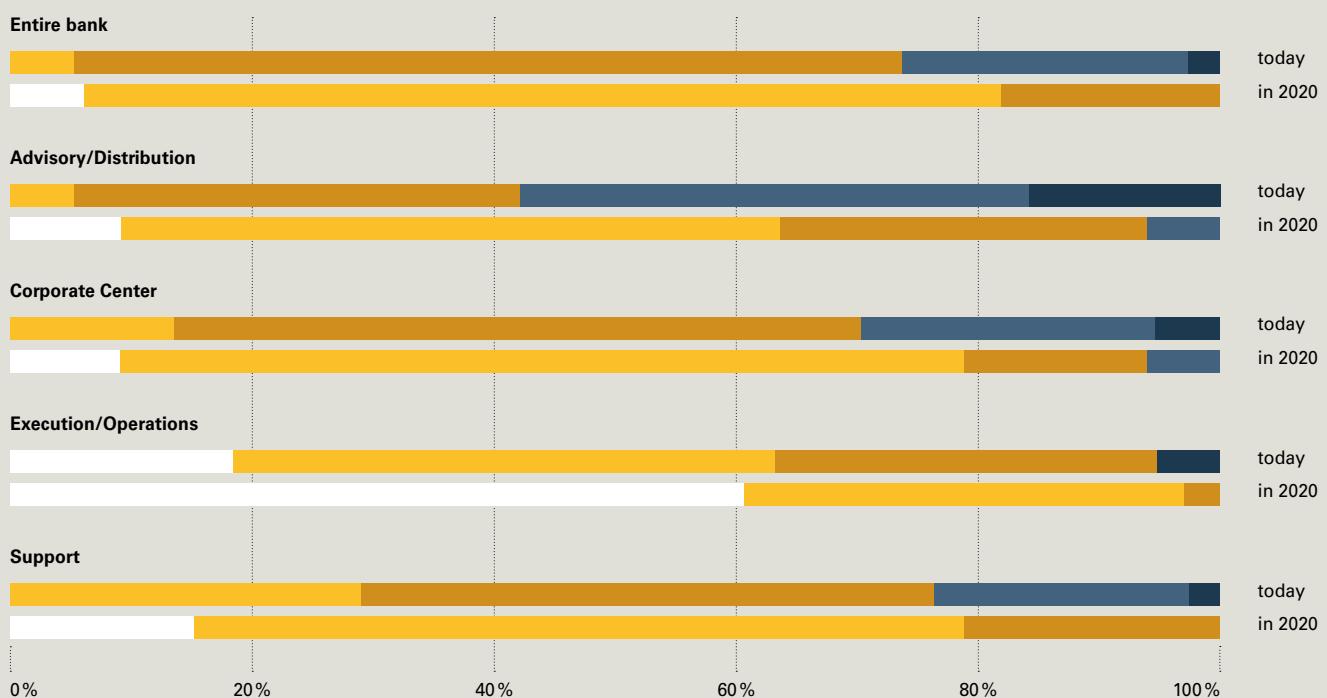
Under current circumstance, it is no wonder the profitability of Swiss private banks has been under intense pressure. That is driving a quest for operational excellence to seek more cost-effective and efficient ways of working. Whether through cost-cutting and optimization programs, industrialization efforts to boost efficiency and productivity, the rethinking of operating models, value chains and collaboration strategies, or efforts to reduce operational risk, banks are looking closely at all aspects of their operations. Technology will likely play a key role here.

In late 2015, KPMG conducted a series of interviews as well as an e-survey involving key Swiss private banking actors regarding industrialization, standardization, automation, and collaboration in the Swiss private banking sector. Respondents stressed the importance of such topics, saying they expected an increasing number of collaborations and partnerships in both the front and in operations. They also saw a need to continue on that path in the future if they are to catch up with costs and quality. By 2020, many therefore expect a considerable increase in outsourcing agreements.

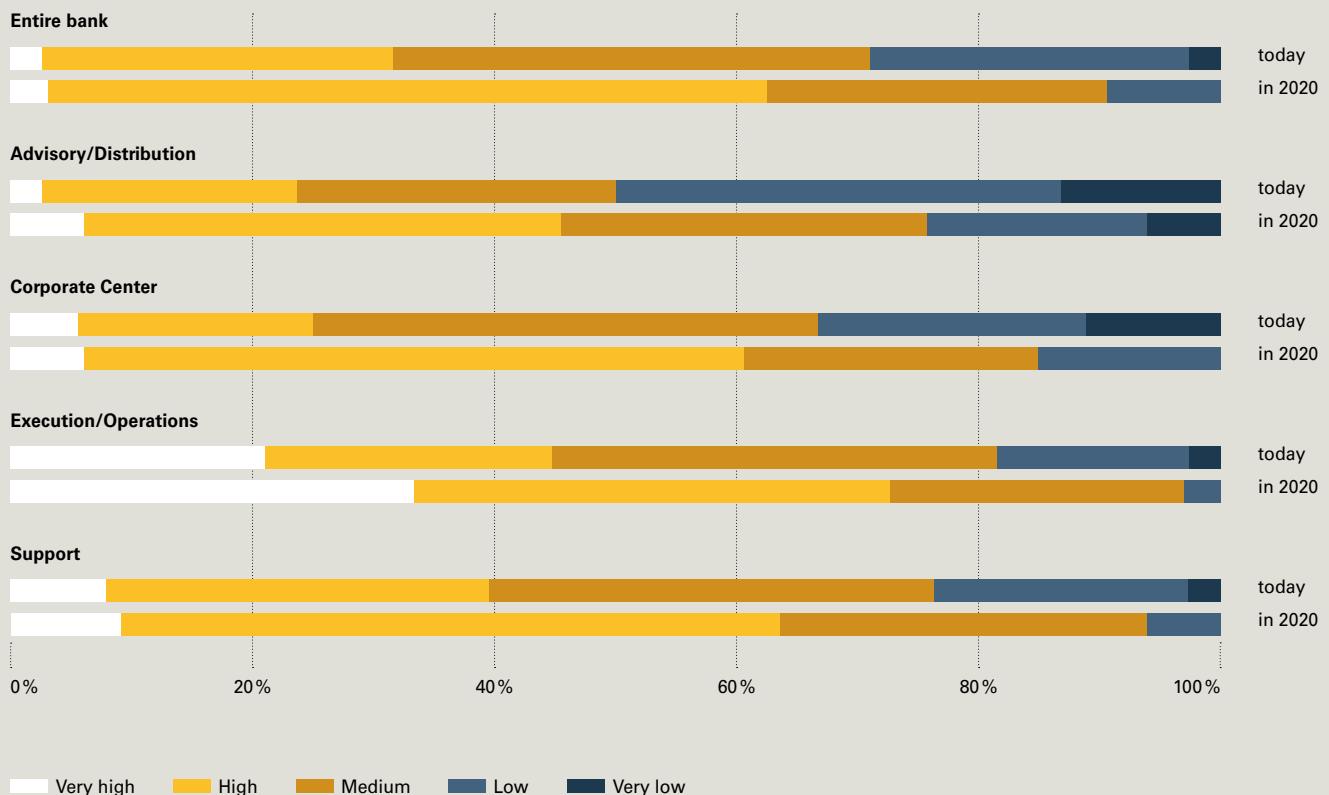
Level of standardization – today and in 2020



Level of automation – today and in 2020

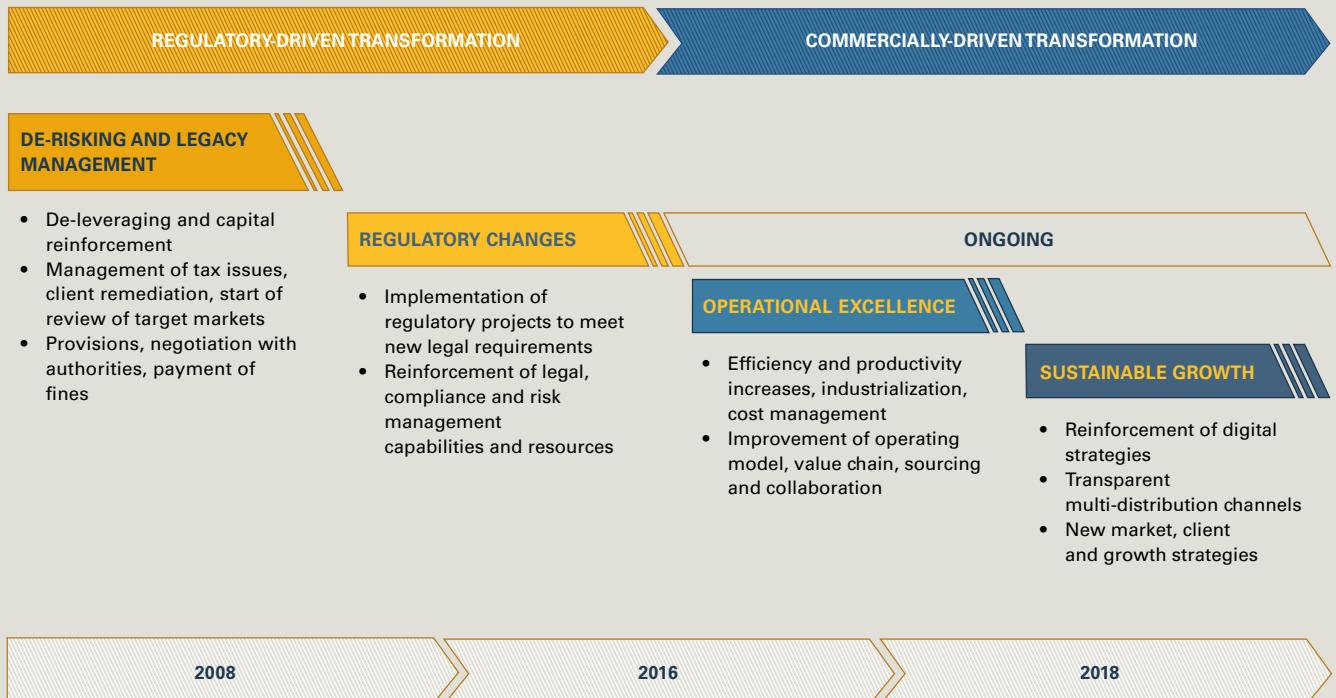


Level of collaboration – today and in 2020



In our e-survey, respondents said they expected an increase in industrialization projects with an emphasis on standardization, automation and collaboration.

Sector evolution



The Swiss private banking sector is facing a progressive paradigm shift.

DESTINATION: GROWTH

Nevertheless, this is only the beginning. Going forward, Swiss private banks will need to move from reaction to action. Everything can and should be on the table, from distribution channels and market strategies to client segments, value propositions and better use of emerging technology. Here the current FinTech revolution could provide an excellent opportunity. Thanks to the explosion of technology firms working on new solutions for financial services, they will have many more options to access innovative capabilities in a cost-effective way. However, technology can only go so far. Banks that want to find new ways of generating revenue and growth must above all refocus on clients and sales.

This being said, although regulatory-driven transformation remains high on the agenda, we consider the peak to be probably behind us. Private banks are progressively refocusing on core revenue-generating activities – commercially-driven transformation - to generate growth. This move from regulatory-driven to commercially-driven transformation is significant. We think it marks the beginning of a new phase of the post-crisis recovery in Swiss private banking.

At the crossroads: Strategic options for Swiss private banks

Swiss private banks today are clearly standing at a crossroads. For some the road stops here. Those institutions solely focused on legacy issues, regulatory-driven transformation or cost cutting - with limited ability to attract new clients and insufficient resources to invest in growth - are likely to fall by the wayside. As we pointed out in our publication "Clarity on Performance of Swiss private banks 2015," this fate may await some 30% of existing Swiss private banks over the next few years. In the 2016 version of the same publication, we noted that in 2015 10% of Swiss private banks had indeed sold out or closed their doors.

In such a difficult context, it is essential that boards of directors and senior management set clear objectives. Without clarity of purpose, serious questions will be raised about a bank's ability to survive. The key questions management must ask are:

- Does the bank have a future in Swiss private banking?
- Does the bank want to stay as it is?
- Can the bank afford to stay as it is?
- Alternatively, how should it change?
- Can transformation bring renewal and growth, and if so, how?

Once these questions have been answered, it will be decision-time.

More precisely, we see three possible strategic ways forward for Swiss private banks. These need not be mutually exclusive. Indeed, we expect banks will end up choosing a mix of the different possibilities we outline below, for example selling client books in some areas while transforming the remainder of the business, or exiting certain markets but increasing activities in others.

Swiss private banks have a mix of options for the future based on three scenario directions: status quo, exit and/or transform.

• **Status quo scenario: an option only for the few.** Banks can of course decide to do nothing at all – meaning no transformation, no changes to strategy, business or operating model. For those few who have found their niche already, perhaps by focusing on specific market segments, this could potentially be an option. Some of the larger institutions – those that have pursued a strategy of acquisitions and now benefit from economies of scale – may also find it possible and desirable to bide their time. For the vast majority, however, we think that clinging to the status quo will not be a viable path.

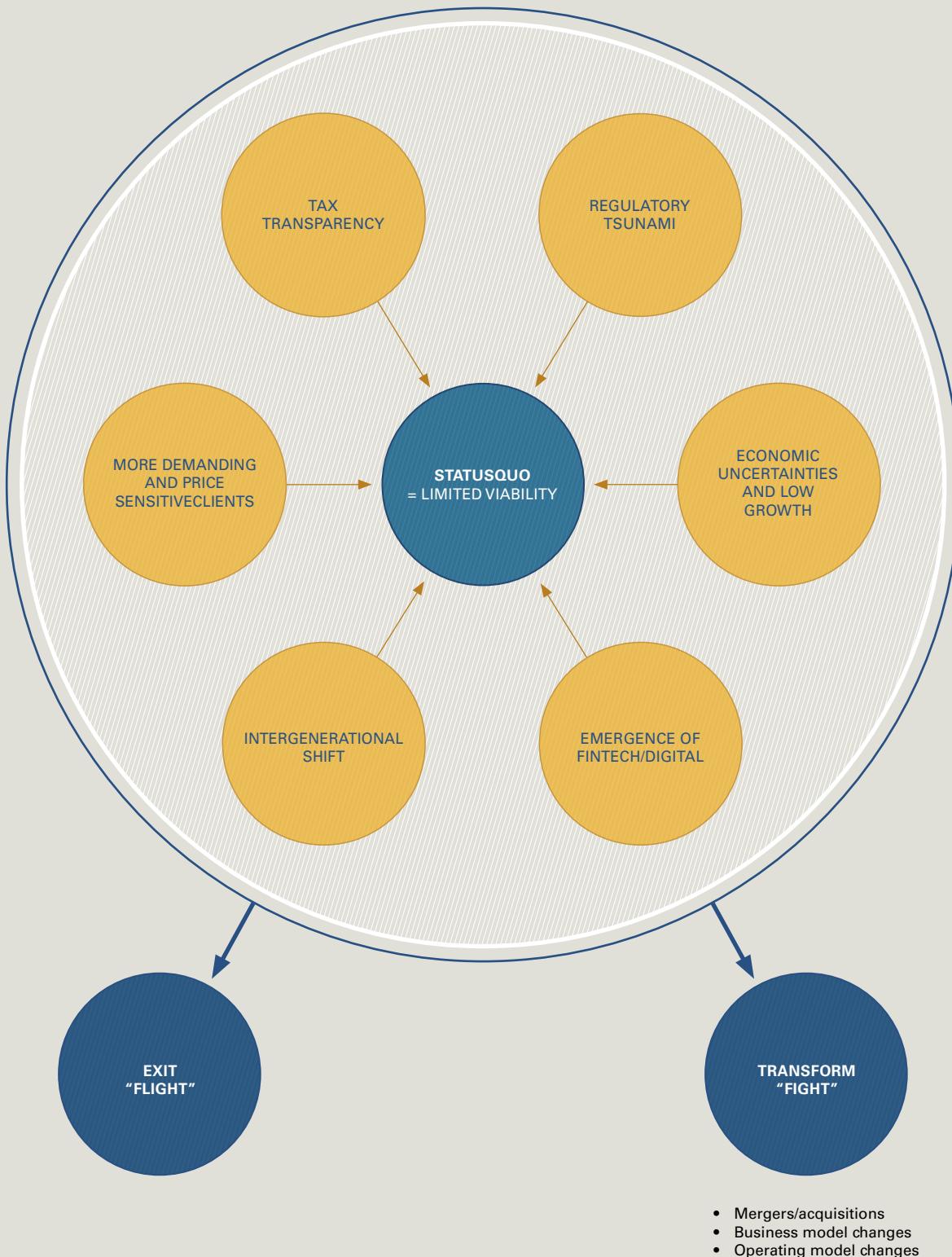
• **Exit scenario ("Flight"): fleeing the Swiss market.**

They say discretion is the better part of valor. Choosing to leave the market or get out of the business may be the most sensible strategy for a number of banks. A lack of sufficient scale, no clear strategy or insufficient funds for financing expansion could all drive such a decision, as could the lack of the right in-house staff or non-compliance with new cross-border regulations.

• **Transformation scenario ("Fight"): building a new future in the Swiss market.**

Those banks who have decided to transform will have to rethink their overall strategy and adapt their organizations. For most, this will in turn mean a radical rethinking of their approaches to becoming truly innovative both on the business and operations side. Here, technology will be key in driving innovation and change. We think the current FinTech revolution could have a significant impact in this regard. While it is too early to say exactly how, we believe FinTech will offer private banks the chance to leverage new digital technologies, innovate, and transform their businesses in ways that were not possible in the past. These opportunities, however, need to be understood, and then fully exploited in a timely manner.

Strategic options



We believe those banks that see a future for themselves and want to go down the path of sustainable growth must at a minimum:

- Understand their own strengths.
- Know the markets they want to target (and those they want to avoid).
- Have a clear strategy, client segmentation and service offering.
- Return to the truly client-centric approach that had characterized Swiss private banks in the past.

GROWTH THROUGH TRANSFORMATION

As we have been arguing, the watchword for Swiss private banks who chose to “Fight” is transformation. For many banks, this will likely entail a combination of organic and inorganic strategies.

On the one hand, banks willing to stay in the market will notably continue to grow through transactions.

Mergers and acquisitions:

In terms of inorganic transformations, banks willing to stay in the market may be interested in buying books of clients from other institutions (asset deals) or even buying banking structures (acquisitions). Alternatively, they can also decide to merge with another private bank (mergers of equals).

On the other hand, organic growth will come from two sources.

Changes to the business model:

- Clients.
- Revenue-generation.
- Value proposition (markets/products/pricing) aspects.

Changes to the operating model:

- Operational excellence.
- Cost optimization.
- Process reengineering.
- Taking advantage of IT/technological developments.

In the mirror: The personal challenge of managing change

Any successful organization needs good leadership. In times of transformation, it needs it even more.

We believe the human challenge of managing change should not be underestimated. As the experience of managers in other industries that have undergone radical transformation has shown, the psychological strains can be immense. However, this is often because managers are not sufficiently prepared. By being aware of what lies ahead, board members and C-level executives may have an easier time recognizing, and mastering, these personal trials. That will only help them as they work to overcome the challenges facing their organization.

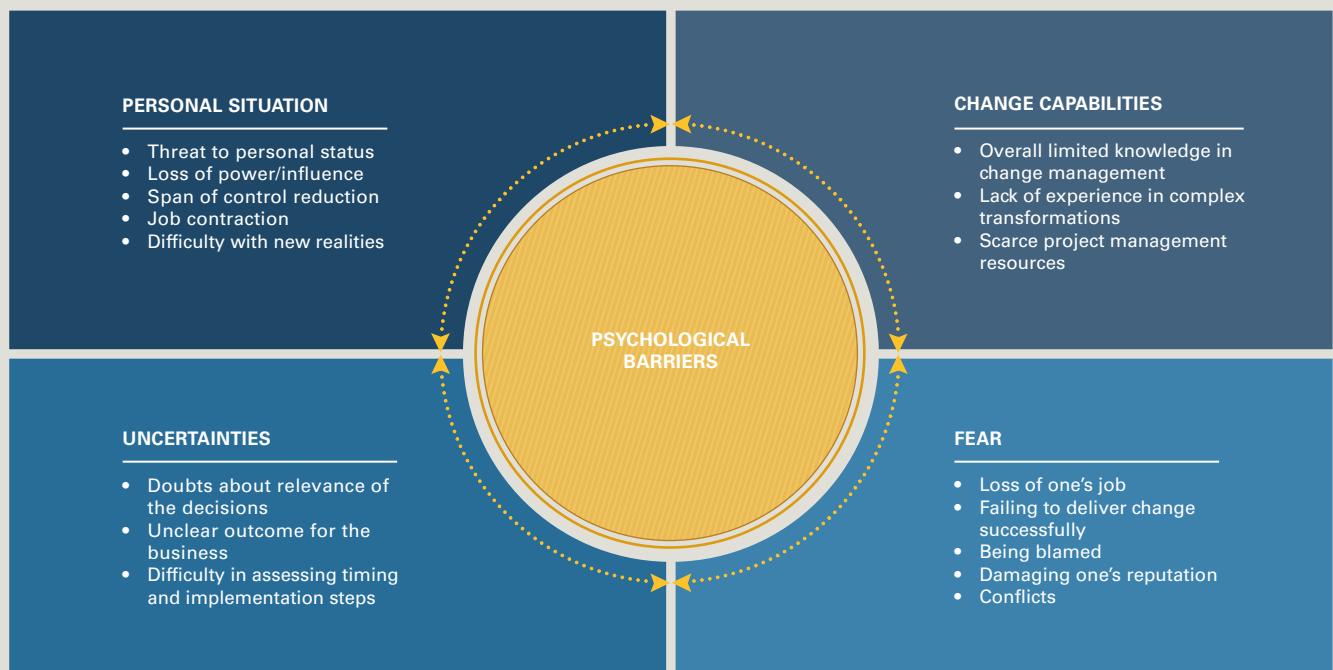
WHEN THE SEA GIVES WAY...

Complex transformational change is particularly challenging in industries with a long history of stability before their particular crisis hits. This is understandable. Managers who know how to hold the helm steady in calm seas (a talent of its own, and never as easy as it looks), may find themselves taken by surprise when the waters become choppy.

This can lead to stress and any number of difficult emotions. Managers may worry, for instance, about such things as whether they have the right change management skills or enough experience in large-scale transformation. They may be concerned about whether their staff is sufficiently experienced to implement transformation plans. They can worry about the project management discipline within their companies, their own ability to lead an organization through change or their capacity to communicate effectively and get buy-in from employees.

Managers have been known to feel threatened by transformational situations as well, whether at the loss of personal status, of influence in the organization, of control, of reputation or of face. Managers can also enter a state of denial about the need for change, resisting the new realities. There can be fear and doubt as well: fear of losing a job, of failure, of conflict; doubts about whether a given decision was right or not, about timing, implementation, methodology.

Typical psychological barriers observed in other sectors



As witnessed in other industries, leaders and managers often face inner psychological barriers when dealing with complex change.

...BUILD BRIDGES

The good news is that these fears and doubts can be countered. The best way to be effective in complex transformational decision-making is to remain rational: tangible facts and broad-based support throughout the organization can be safe havens in the storm of change.

Clear support and sponsoring from top management can help set a calm, serious tone, helping motivate teams for the job ahead. Honest, timely communication which informs and reassures will help not only keep staff on the same page, but also help bind people more closely to the vision and goals of the project. If with these and other measures an organization facing radical change can successfully develop a motivating and change-friendly corporate culture, the seeds will be sown for success.

Managers can also rely on any number of metrics to help them navigate change, from key market, industry and

business figures, or performance indicators to the insights and voices of their clients. Such objective facts and outside feedback can help C-level executives overcome their emotions to make effective, information-based decisions.

Transformation can no doubt be a disruptive and harrowing experience. Managers need not fight their emotions. However, by recognizing them, and relying on objective criteria and their innate skills, they can ensure that their emotions do not get in the way.

From this perspective, method and discipline can help as well. A fact-based decision-making framework, such as the one we outline in the next chapter, reduces uncertainty and increases predictability of the change process. It can also help optimally identify the pros and cons of strategic options.



THE POWER OF "US"



In the past, Swiss private banks relied on a limited number of unique selling points (USPs) and an integrated model. Today, facing more complexity due to weakened banking secrecy, more demanding clients, tightening regulations and costs on the rise, banks have to change their approach. We will argue below that they require a systematic, objective self-assessment followed by a refocus on core strengths and disaggregation of the value chain. By building holistic, high-performing ecosystems - based on "US" thinking - Swiss private banks can help foster the organic growth they need.

All together now: How building true ecosystems can help Swiss private banks master today's challenges

Previously in this paper we have discussed the difficult situation Swiss private banks find themselves in, and the strategic decisions they will have to make when considering their way forward. Along with having the option of seeking expansion through M&A, we argue that those banks that choose to stay in the market will need to pursue organic growth. In this chapter, we discuss two of the key factors we feel will be essential to a successful organic growth strategy: a focus on core strengths and the development of high-performing, strategic external ecosystems.

KNOW THYSELF

Historically Swiss private banks leveraged a limited number of USPs. While they touted Swissness in general and Swiss banking expertise specifically, the chief (and sometimes sole) USP for many had been banking secrecy. With the weakening, if not outright dismantling, of Swiss banking secrecy since 2008, this is no longer an option.

In the meantime, the clients of Swiss private banks have become much more sensitive to and keen on price and quality, as well as more demanding and less loyal. This has translated into higher turnover and asset attrition in many institutions.

Under these circumstances, we believe Swiss private banks will have to change how they run their businesses. In the past banks have traditionally used fully integrated models. Such an approach is no longer sustainable.

This is true both for reasons of cost and quality. Banking has become a complex, technologically sophisticated enterprise. It is very difficult for any organization to master all the components of a modern bank value chain, let alone smaller operators. Instead, we consider today's Swiss private banks have to identify those areas where they can truly make a difference – their key USPs – and then relentlessly refocus their activities around them.

As Swiss private banks examine their value chains, they will typically end up with a limited number of key USPs as well as a list of non-core activities that do not add value. It is here that they will have to look for external support.

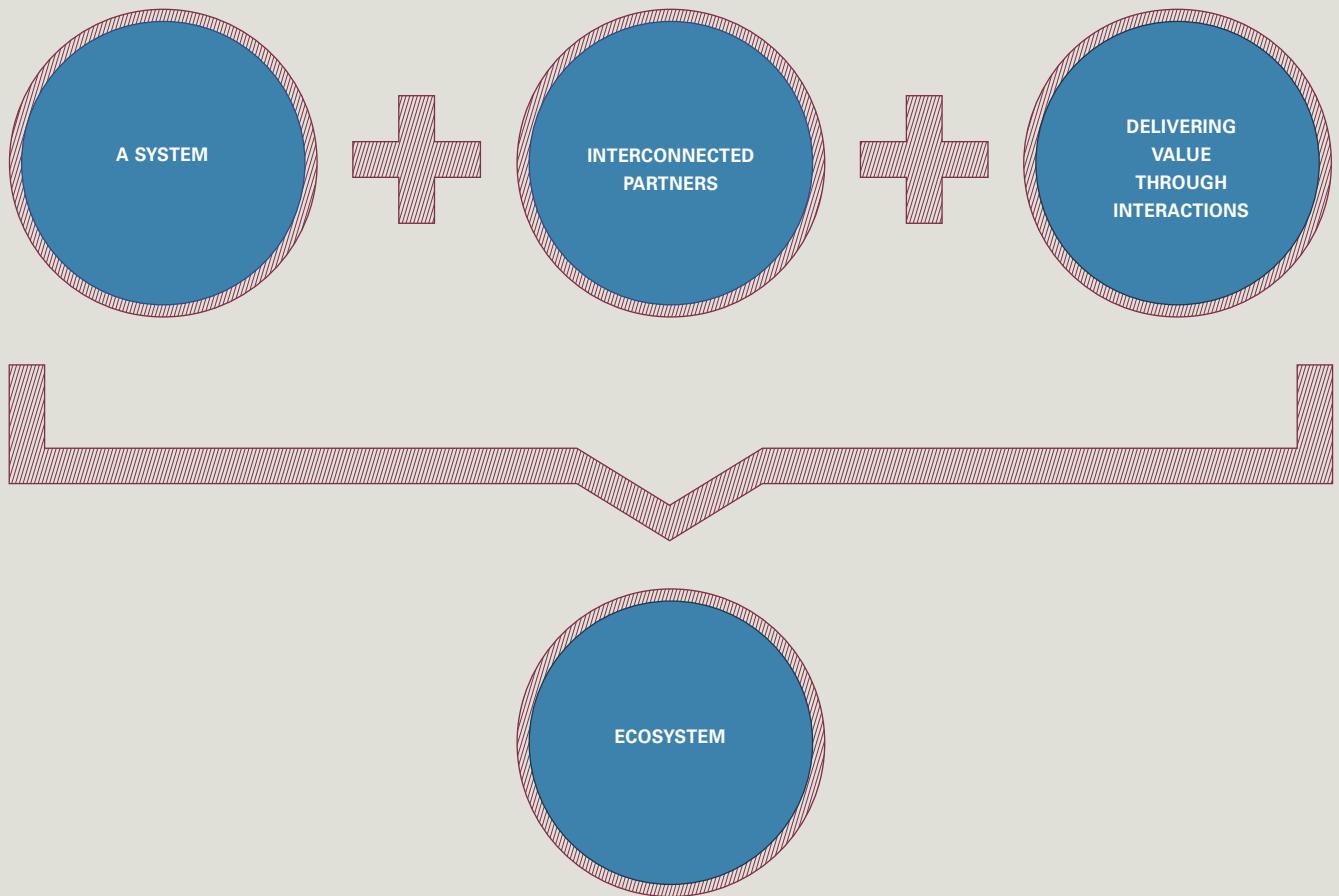
Doing so will involve a disaggregation of the value chain of the kind we have already witnessed in other industries, for example, automotive.

The good news is that Swiss private banks are, by and large, aware of the issue. In our survey interviews, respondents indicated a wide range of factors they could see driving such industrialization efforts. Unsurprisingly, the primary factors all revolved around cost pressure and efficiency considerations. Respondents also said that being compliant with regulatory requirements would be an essential component of any industrialization process.

Furthermore, Swiss private banks will have more options in searching for external support than before. Today we see an increasing number of actors in the market that can perform many of these non-core activities more effectively, in terms of quality, performance and risk management, or more efficiently, in terms of speed or cost, than banks can. Working with such partners will not only deliver further value for their clients. It will also free banks to refocus on their strengths.

Hence, we are convinced that the development of strategic partnerships, with an eye to strategic outsourcing, will become increasingly important in the Swiss private banking sector. As banks spread their non-core activities across multiple actors, allocating each to the best performer, the result will be the genesis of "ecosystems" of partners for each bank. Banks will then need to manage these ecosystems in a holistic fashion.

Ecosystem definition – a system composed of interconnected partners delivering value through their adaptive/flexible/agile interactions



An ecosystem typically delivers more value than the sum of its parts.

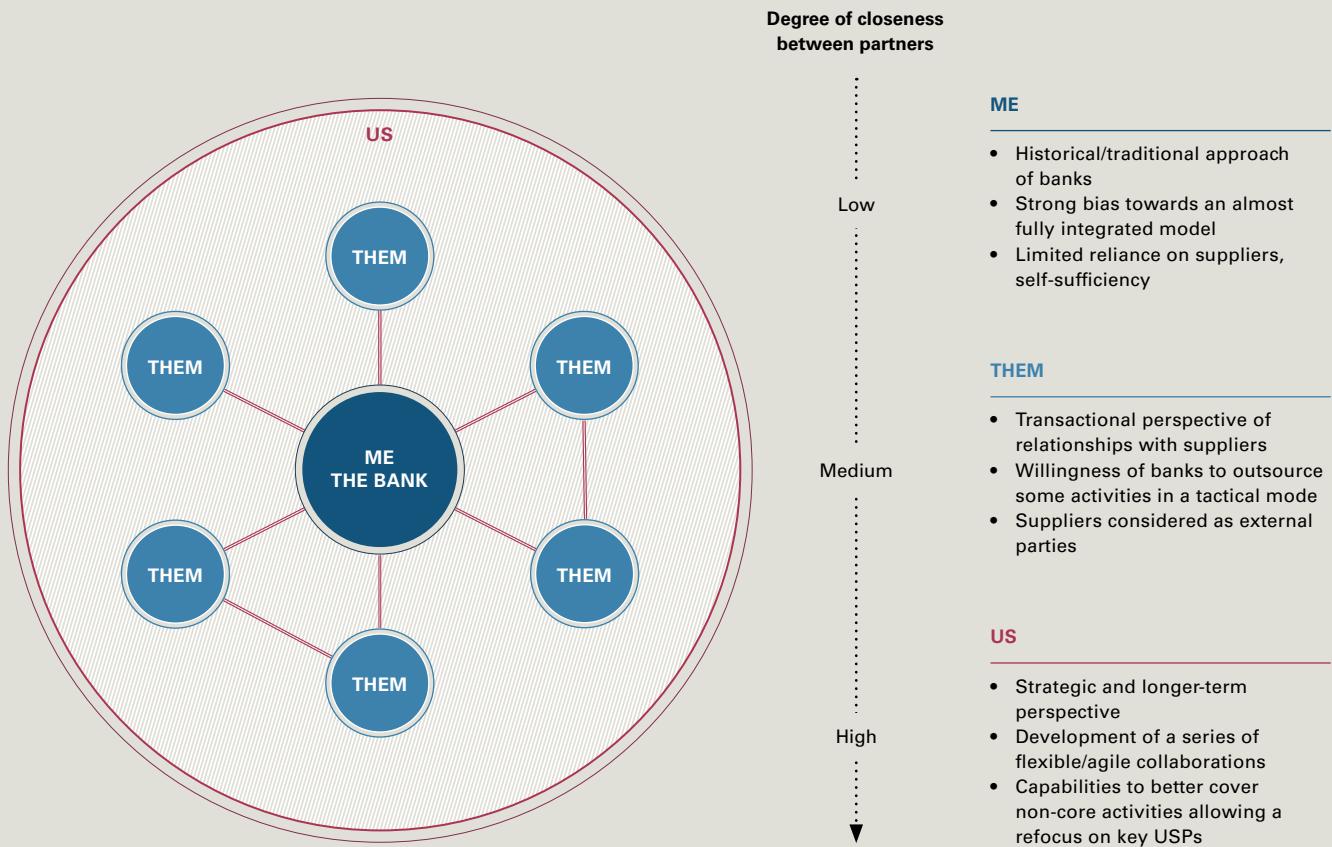
KNOW THY ECOSYSTEM

A key way to ensure ecosystems are successful is to understand them. Here banks will find that their clients may be ahead of the curve. In our digitalizing world, consumers no longer look for isolated products but consider their provider's whole network and ability to address holistically their needs. Amazon's business model is the classic example of the power of modern ecosystem thinking. Amazon today does not just sell books over the Internet, but with its marketplace and new technologies like Alexa permeates the client's daily life.

Whether apparent as provider or less so as an assistant (when customers for example use Amazon's platform to purchase from its partner network), customers are in constant contact with Amazon along their purchasing journey.

Banks with the right platform can play a similar role as provider and assistant in the financial lives of their clients. Building an ecosystem with interconnected external partners can enable banks to provide more value and a greater offering to clients through adaptive, flexible and agile interactions.

Degree of closeness between partners



Out of the three degrees of closeness, a comprehensive "US" approach often delivers the best results.

THREE DEGREES OF CLOSENESS BETWEEN PARTNERS

We see three "degrees of closeness" in the strategic partnership space, which we have defined in the following terms:

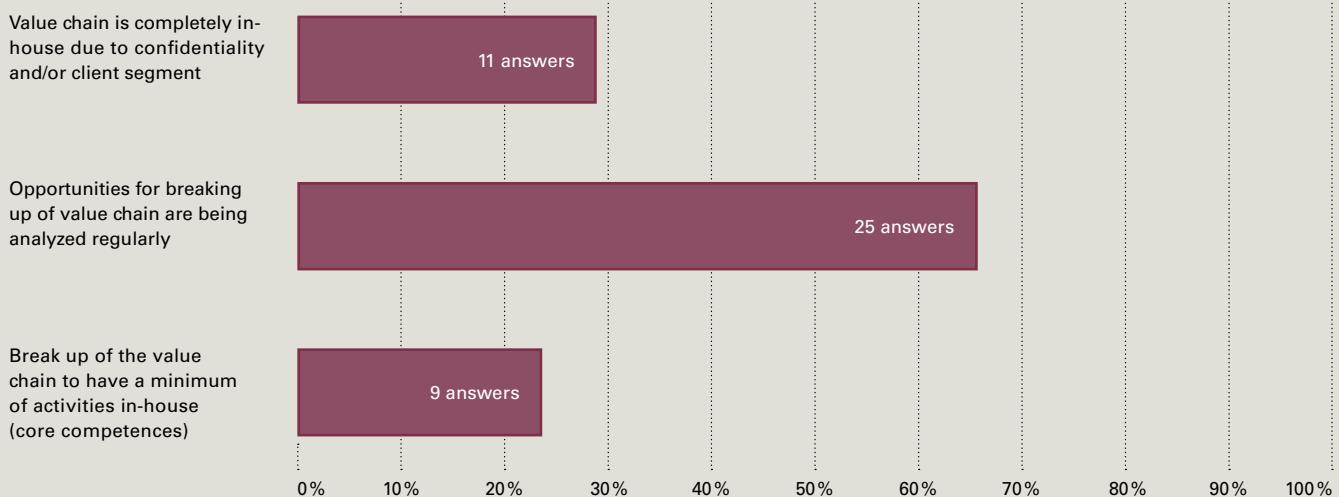
- **ME:** a low degree of closeness, corresponding to the traditional fully integrated model of banks, with some minor services perhaps bought in from suppliers.
- **ME and THEM:** a medium degree of closeness in which banks are open to outsourcing some of their activities in a transaction-type tactical mode.
- **US:** a high degree of closeness in which banks adopt a more strategic and longer-term perspective and look to develop a series of flexible and agile collaborations with a group of highly capable external partners.

The "US" approach is typically characteristic of an ecosystem view.

During the decades leading up to the millennium, the "ME" approach had been the norm. Over the past 10 to 15 years, private banks have increasingly turned to external suppliers, and since 2008, the "ME and THEM" approach has been the clear trend. Yet it remains more tactical than strategic – banks still do not take a holistic view of their supplier ecosystem. We believe this should change.

Evaluate current level of industrialization – How is your bank set up with respect to the value chain?

Answer (more than one answer possible)



In our survey, respondents confirmed there are still private banks with a fully integrated value chain. Nonetheless, there is growing appetite for industrialization and value chain disaggregation. Few executives, however, mentioned that they were looking at a refocus on core competences with the rest to be outsourced.

In our opinion, only the "US" approach will deliver superior long-term results. This means those private banks that understand the need to go beyond the tactical transaction-type perspective and adopt a stronger strategic angle will be at an advantage.

Doing so requires:

- Taking a longer-term view.
- Focusing on partnership and collaboration, as opposed to the more limited transaction view.
- Truly understanding the need to develop an ecosystem of strategic partners, one that also includes the end client and his or her entourage (i.e. family, business), and knowing how to maximize it in order to add value for all parties involved.

Before it is possible, however, to take such a strategic view of the ecosystem, banks will have to identify the "proprietary assets" that make up their specific USPs. These will almost certainly be key activities directly related to clients or having a strong impact on the client relationship – typically the more "human" areas such as relationship management, sales and advisory.

We think fruitful areas for Swiss private bank USPs could include:

- Quality of the client experience.
- Perception of the bank's brand.
- Trust and confidence clients have in the bank.
- Bank's responsiveness and reliability.
- Quality of its service, including perceived Swissness.
- Quality and skill of its relationship management teams.
- Quality of its advisory services.
- Its ability to differentiate in terms of the performance and suitability of the products and services it offers to clients.
- Effectiveness of the bank's distribution channels (including digital channels).
- Bank's ability to employ new technologies with effectiveness.
- Quality of the bank's overall ecosystem.

THE ROAD TO SUSTAINABLE GROWTH

Since a partnership ecosystem is expected to become a key success factor for sustainable growth, understanding the value of such strategic sourcing partnerships, whether short-term, long-term or permanent, is of primary importance.

Will this mix of key USPs plus strategic sourcing be enough to ensure growth over time? Of course not. Ultimately, any transformational journey has to be related to client value-add and not purely internal considerations.

However, it will help on many fronts. A focus on key USPs is necessary to attract the new clients private banks will need to survive, while retaining the clients they already have. In addition, the optimization of the partnership ecosystem – in other words, adopting the “US” approach – will contribute to further maximize value add for these clients.

Unfortunately, as was clear from our interviews and the e-survey, for the present at least, the “US” stance remains underdeveloped in the sector. Few banks are really taking a holistic view of their network of suppliers or trying to optimize it strategically with a long-term horizon.

Looking at the responses in more detail, a majority of respondents did say they are looking at opportunities for breaking up the value chain, generally by outsourcing technical functions (i.e. IT, back office). This corresponds to the “THEM” approach we have outlined. A significant number of respondents said that, for various reasons, they were keeping all client activities in-house – while a smaller number were considering breaking up the value chain with an eye to only keeping core functions in-house. Generally, there was no clear overall strategy on how to develop an ecosystem as a whole, the prerequisite for an “US” approach.

Best foot forward: Transformational methodology to develop effective ecosystems

Shifting to an ecosystem model will not be a straightforward process. There is still a natural tendency to consider suppliers from a transaction perspective rather than a strategic one. Along with talent, skill and conviction, we think a successful transition will therefore require a robust transformational methodology.

Furthermore, banks should be aware of how modern ecosystems function. Technology and digitalization can change the dynamics that have been in play in traditional ecosystems familiar to us from the physical world of collaborative partnerships. A virtual environment can alter the basic rules of an ecosystem, the time horizon of its partnerships, their success factors as well as the way parties behave. Private banks need to monitor new emerging digital trends and breakthrough technologies in order to detect their possible disruptive impacts on ecosystems and to understand how these ecosystems will evolve.

HONEST APPRAISAL

As leaders know, any strategic transformative development typically requires the following:

- A holistic top-down view of the business, market and competitive arena.
- An in-depth analysis of the situation.
- A strong reliance on facts as opposed to gut feeling and intuition.
- Clarity regarding strategic alternatives and options available to the business.
- An objective decision-making process focused on value creation.

Key ingredients for strategic development



A systematic, objective, fact-based approach is a key ingredient for effective strategic transformative development.

All these skills will be integral parts of the systematic approach private banking executives will need to employ if they want to identify the most suitable options for collaboration and partnership across their value chains.

RATIONAL EXUBERANCE

While speed and agility are essential in any transformation activity, senior executives typically face psychological barriers when considering complex or radical changes to their organizations, as we discussed above. Uncertainty about their decisions or a perceived lack of knowledge or change capabilities are common.

This can be more so in private banking, which has been a stable industry for centuries and where transformation management, at least until now, has not been a core skill.

This must change. The development of strategic sourcing programs can be a complex, risky and difficult undertaking. Emotions such as discomfort and fear, while understandable, will only be hurdles, as will delaying decisions. The Swiss private banking industry needs to improve its transformational managerial skills in a methodical, process-oriented way.

We believe the use of a structured framework can help by decreasing emotionality and reducing psychological barriers. A decision-making process based on a systematic decision-tree can help C-level managers develop the positive reflexes required to make complex transformational choices with increased agility, traction and effectiveness.

A SYSTEMATIZED APPROACH

Such a decision-making framework should have the following characteristics.

For one, it will need to provide a methodical way of assessing the value chain of a private bank, including by:

- Identifying key proprietary assets/USPs.
- Identifying non-core activities.
- Objectively evaluating tactical ("ME and THEM") or strategic ("US") sourcing alternatives for those non-core activities.

Furthermore, such an analytical process should cover the entire value chain (i.e business and operating models), allowing for an assessment of the key building blocks within each area.

Finally, the underlying key principle should be the maximization of value creation (incl. client satisfaction, higher quality, reduced costs, lower risks, and evolving needs of clients).

With these considerations in mind, KPMG has developed a framework to help C-level executives reflect on their USPs and strategic sourcing options. This approach focuses on the following dimensions:

• Business building blocks:

1. Propositions and brands.
2. Clients.

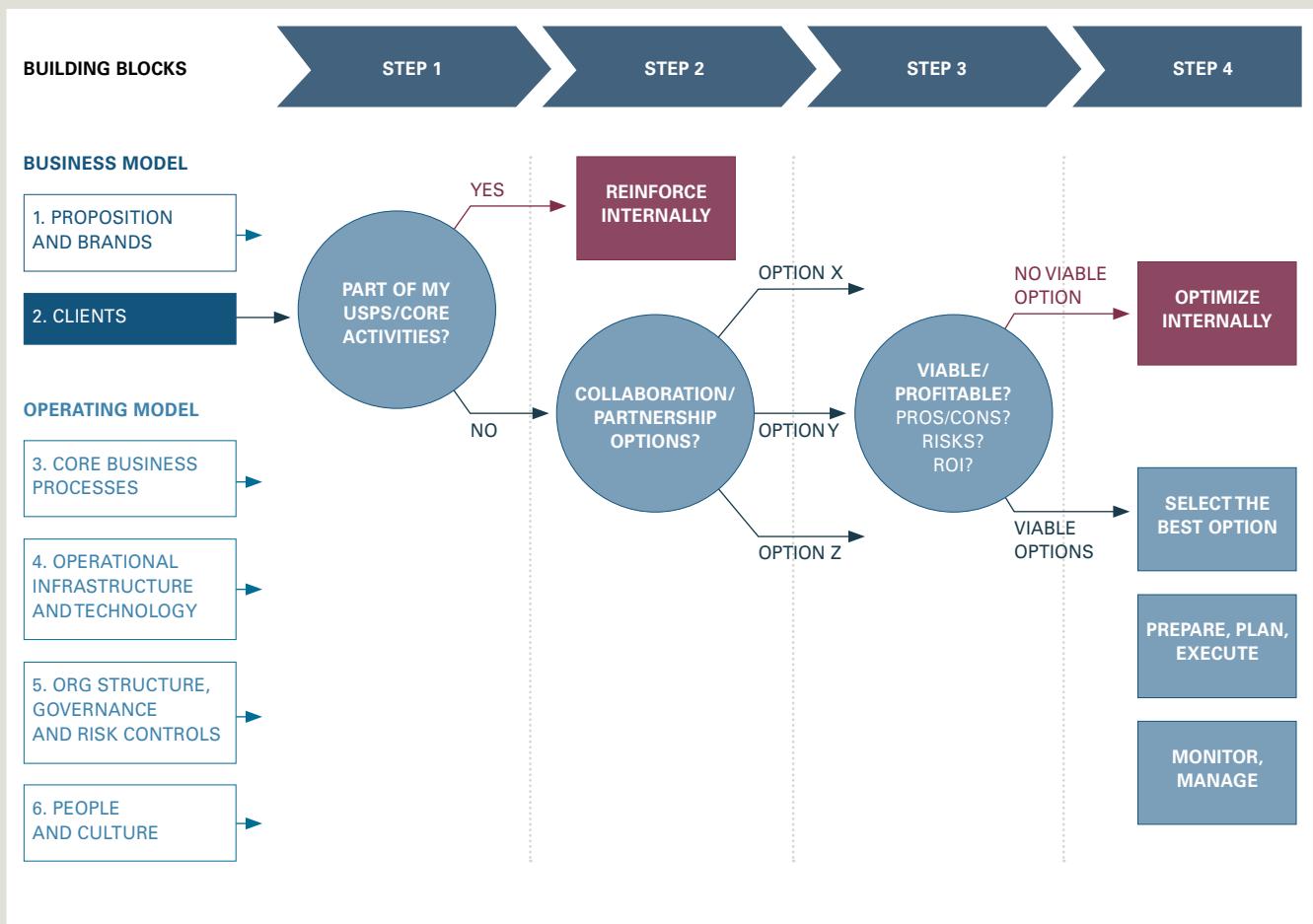
• Operating building blocks:

3. Core business processes.
4. Operational infrastructure and technology.
5. Organizational structure, governance and risk controls.
6. People and culture.

For each building block, executives need to ask – and answer – a series of questions as they build their decision-tree. These include:

- Firstly, is this element part of my USP/proprietary assets, key strengths, core activities or a differentiating factor? If yes, how should I leverage it to increase its differentiating influence? In addition, how can I maximize its ability to generate value for end clients?
- Secondly, is this element part of my commodity assets or non-core activities that brings limited added value to the client or my bank? If yes, what are my collaborative "US" options regarding this activity while maximizing client value-add? Are there non-technological options? Are there FinTech/digitally based options? What should I do to develop a win-win situation between the client and my bank?
- For each proprietary and non-proprietary alternative: How can the alternative best be implemented? How do I manage the risks involved?
- What are the regulatory requirements or constraints, if any?

Decision-tree to assess collaborative options



C-level executives will benefit from a structured decision-making framework to assess systematically and holistically collaboration potential across the value chain.

Building an effective ecosystem will no doubt remain a challenge for many banks, and on many levels. However, if they can overcome the psychological and methodological hurdles, we believe such ecosystems will provide fertile ground upon which Swiss private banks can grow.



THE MANY FACES OF COLLABORATION



Swiss private banks will need to understand the pros and cons of the different collaboration models, from sharing to full outsourcing. They also should not shy away from evaluating all the building blocks of their business and operating models for potential partnerships. Building the ecosystem requires careful management of the risks and complexity of transformation. Those who are successful can expect to enjoy a competitive advantage.

Nuts and bolts: The practicalities of collaboration

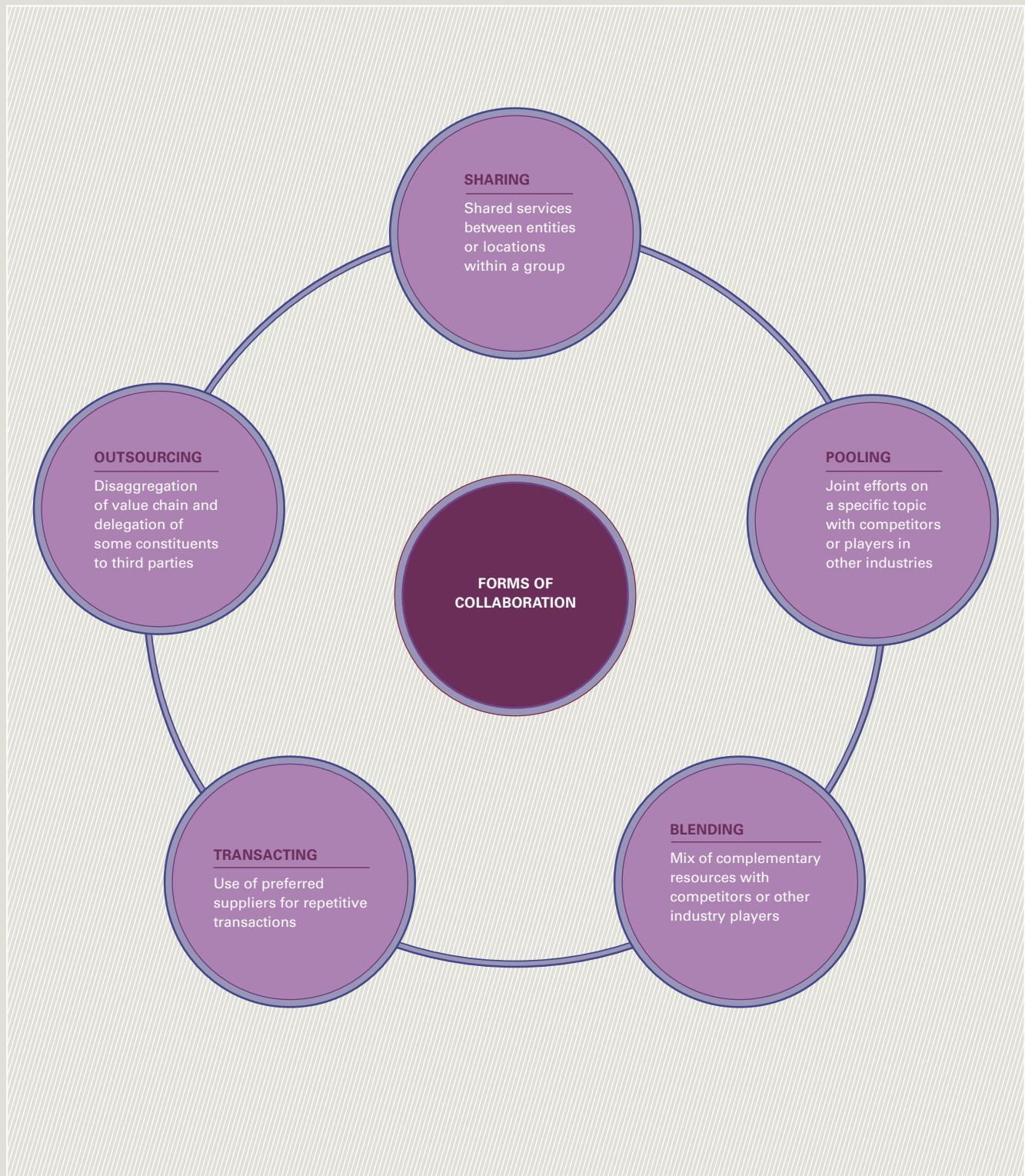
WAYS OF WORKING

Our main message so far has been one of collaboration. In practice, there are many different ways for organizations to work together. We see the following collaboration scenarios for Swiss private banks.

- **Sharing.** A large bank builds an internal shared-services hub in a low-cost country to service several of its entities in different locations. In such a case, the collaboration takes place mainly within the group.
- **Pooling.** In this scenario, two banks choose to join efforts on a specific topic. Pooling can occur between companies in different sectors as well as between direct competitors. Objectives are generally to mutualize costs and/or achieve economies of scale.
- **Blending.** In a blending scenario, two banks decide to mix complementary resources together, for example, by means of a joint venture.
- **Transacting with a preferred supplier.** Here a bank chooses the same supplier for highly repetitive transactions over a long period of time.
- **Outsourcing.** When outsourcing, a bank disaggregates part of its value chain and delegates the management of some of the chain to third parties.

Each form of collaboration outlined above can result in a different form of partnership between the parties. In all cases, however, trust, quality and mutual commitment will be key success factors determining the ability of the parties to establish truly successful partnerships, whether for short-term, specific case needs or for the long term. In such ecosystems, it is important to ensure that the client is well integrated. As ecosystem participants, banks may also want to consider to what extent they would like to not just receive services, but also offer them.

Different forms of collaboration



Collaboration can take various forms.

ACTIVITIES ELIGIBLE FOR PARTNERSHIP

So far, in this paper, we have outlined the challenges facing Swiss private banks, and we have provided our opinion that a move to an “US” approach, based on a focus on core strengths and development of a true ecosystem of strategic cooperation and partnerships with external suppliers, represents one of the most promising paths towards organic growth.

In this final chapter, we bring a more practical perspective to our study. We analyze the key building blocks of bank business and operating models, and assess some practical partnership and collaboration options, delving into the nuts and bolts of the options we think Swiss private banks have in terms of developing their capabilities. Then, each option can be analyzed, on a case-by-case basis, in the decision-tree framework developed in the previous chapter.

Activities eligible for partnership

BUSINESS MODEL BUILDING BLOCKS

1. PROPOSITION AND BRANDS

- Products
- Active advisory
- Robo-advisory
- Discretionary portfolio management
- Investment research
- Brand, marketing and communication

2. CLIENTS

- Client data analytics
- Segmentation and targeting
- Digital customer experience
- Distribution
- Customer feedback

OPERATING MODEL BUILDING BLOCKS

3. CORE BUSINESS PROCESSES

- Back office
- Payments, blockchain
- Cash/treasury management
- Securities operations
- Robotic Process Automation
- R&D, innovation

4. OPERATIONAL INFRASTRUCTURE AND TECHNOLOGY

- IT
- Finance processes
- Procurement management
- Help desks/call centers
- Travel arrangement
- Client reception, property management, internal restaurants, logistics, archiving

5. ORGANIZATIONAL STRUCTURE, GOVERNANCE AND RISK CONTROLS

- Legal advice
- Risk predictive analytics, stress-testing, portfolio monitoring
- Credit risk assessment, AML, KYC
- Fraud analytics
- Risk reporting
- Regulatory transformation

6. PEOPLE AND CULTURE

- Recruitment
- Compensation and benefits
- Training and development

Both the business and operating models of a private bank offer several collaboration options that can be analyzed in the decision-tree framework.

While banks today have many opportunities to build fruitful collaborative partnerships with other parties on both the business and operating model level if they want to maximize the strategic utility and overall value-add of their partnerships, then they must holistically manage the ecosystems that they create.

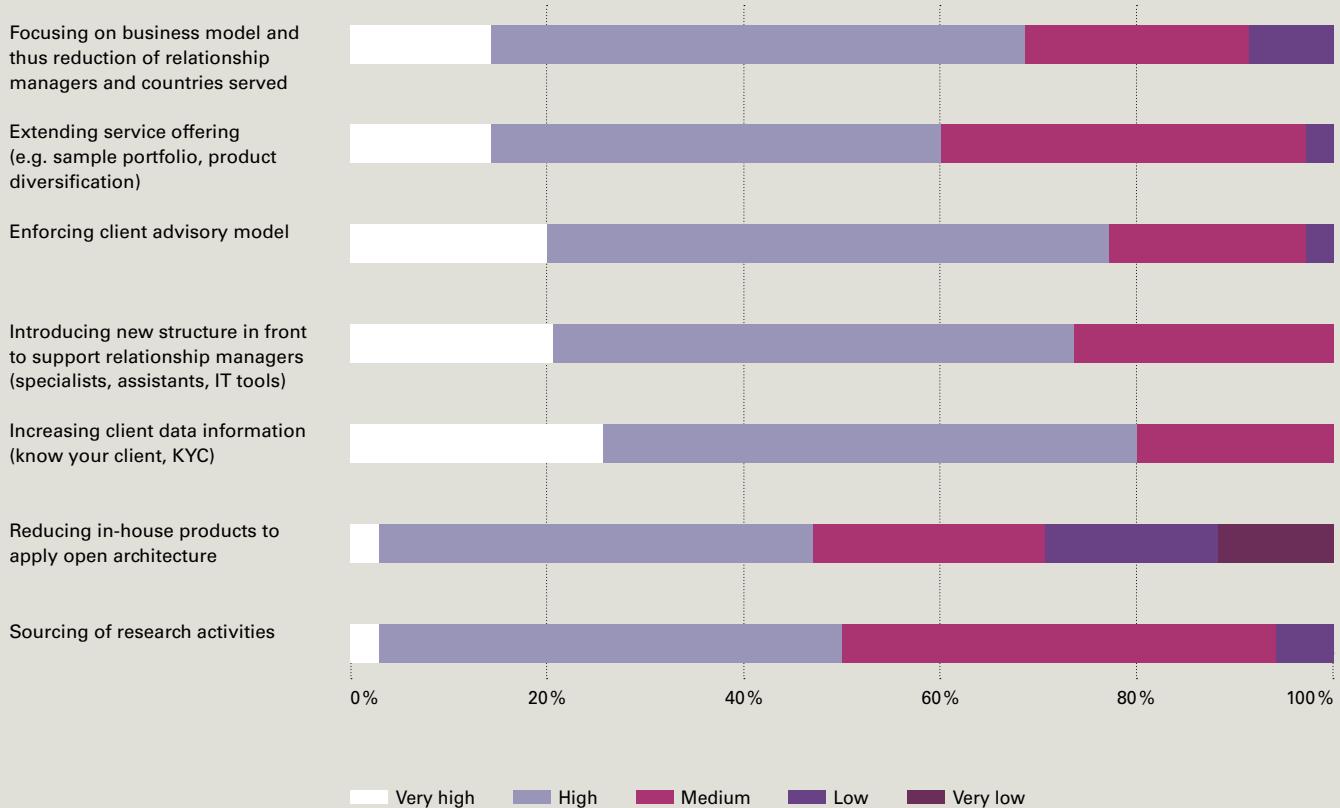
Business Model building blocks: A new approach to business

1. PROPOSITION AND BRANDS

Products and services

Over the years, the open architecture approach has expanded to cover a broad range of products and services. It has since become a significant trend within the industry, and still represents an excellent means of building further strategic partnerships between financial services companies.

How do you consider the need for major investments in the following areas?



Swiss private banks are generally aware of the need to invest in transformation. In our survey, Swiss private bank executives identified products and services, advisory, front office structure or client data as key investment areas for the business model.

In dealing with their future challenges, we believe Swiss private banks need to build on this development, becoming more holistic and systematic in the way they assess their product and service USPs. This includes clearly focusing on their areas of weakness and relentlessly working towards replacing average quality propositions with best-in-class offerings from the market.

Along with standard products like credit cards, investment funds or derivatives, we think candidates for collaboration or delegation to third parties could potentially include the following service areas:

- **Active advisory.** While it may seem counterintuitive to delegate such a key, client-oriented service to a third party, some banks simply do not have the critical mass to offer effective investment advisory services. This is increasingly the case today as financial markets continue to grow, globalize and become exponentially more complex. There are providers in the market that combine a deep expertise in the advisory space with the ability to offer on-demand services to other banking institutions. Working with such partners can help banks improve the quality of their offering and so improve the client experience and client outcomes.
- **Robo-advisory.** From a more digital standpoint, we note that robo-advisory services are playing an increasingly important role in wealth management - either as fully automated solutions, or as a tool to support human advisors. Private banks with no existing capabilities in this technology already have a broad range of partners they could potentially collaborate with today, and new providers are constantly coming to market. We see different ways for Swiss private banks to approach a robo-advisory offering. One option is to invest in an established specialist or help incubate a startup looking to develop this type of product, either alone or jointly with a partner.

This has the advantage of allowing for a tailored solution, but does present selection risk, particularly in the case of a startup with no proven track record. Another option is to work with a traditional private bank or e-private bank that either has existing robo-advisory capabilities or that would be interested in entering into a collaboration to build a new solution from scratch (an approach often referred to as coopetition). Finally, a bank can choose a traditional outsourcing solution from a robo-advisory provider.

- **Discretionary portfolio management.** In the same vein, centralized portfolio management may also be an eligible candidate for a strategic partnership, especially when considering the high maintenance cost of such services. The need has perhaps become more pressing given the fact that few banks have been able to demonstrate a consistent ability to outperform the market, much less turn any such outperformance into a USP.
- **Investment research.** Many small and midsize private banks presently rely on a so-called "secondary" research approach, using "primary" research published by global financial institutions to support them in producing their in-house investment analysis. As with discretionary portfolio management above, if we compare the market performance of such secondary opinions against the costs required to deliver them, we find full delegation of this activity to be justified in many cases.

Marketing and brand

Along with the core activities mentioned above, we think brand management is an area in which private banks could profit from the services of outside specialists. Today, and with a few exceptions, small and mid-size Swiss private banks do not engage in a proactive and systematic management of their brands, nor take responsibility for their strategic brand positioning in the market.

We think they should, as the quality of the brand can affect client perception. Managed well, a brand can support not only the broader marketing mix, but also acquisition of new clients.

Brand management, however, requires specialist expertise, generally in partnership with marketing agencies. Related areas, such as advertising, client marketing, communications or publications management, can also support a bank's USPs in the minds of clients and prospects. These services can be obtained from agencies and other suppliers as well, though banks would do well to systematically assess both the companies and their offerings.

2. CLIENTS

Data

Historically, private banks – limited by their digital capabilities, as well as regulatory and security constraints – have not leveraged the full potential of their client data. We think the time has come for them to consider doing so.

The amount of client data available to private banks is growing by leaps and bounds. This includes demographic, communications-related, behavioral and financial data. While much can be learned from such information, managing today's data volumes is a challenge.

For this reason private banks may consider partnerships with external "customer analytics" specialists. This can help on a number of fronts:

- **More comprehensive client segmentation strategy.**

Today, private banks typically use a combination of geographical market and assets under management metrics to perform client segmentation. Customer analytics partners can help them develop a more comprehensive segmentation strategy in a number of ways. Such partners can assist in aggregating and mining structured and unstructured data sets to get a more comprehensive overview of clients. This can result in deeper insights into client wallet share and relationship penetration.

Leveraging the client insights embedded in customer data can help banks to personalize the client experience across multiple channels, and tailor their communications.

- **Improved cost and sales effectiveness.** By potentially outsourcing the analysis and maintenance of customer data, banks can also bring down costs – an important consideration given today's skyrocketing data volumes. In addition, customer analytics partners can help relationship managers to identify more relevant or suitable products and services for clients. This can help them tailor pricing strategies to specific client segments. It can also help in providing more personalized advisory service as well as better anticipating changes in client behavior.

While the allure of data mining is quite high, there are implementation challenges. Banks face strategic and control constraints around keeping proprietary data in-house. They also face regulatory constraints, including rules on client data protection and banking secrecy. Finally, there are operational challenges. Among these are the ability to anonymize data, to extract and consolidate data from different sources and to truly derive value from the data.

Distribution channels

Along with generating more data, our digitalizing world is also providing new channels with which to interact with clients. Overall, we are seeing a growing appetite among private banking clients for sophisticated digital interactions with their banks. Preferred channels include e-banking, social media, videoconferencing, instant messaging, and co-browsing (which entails having someone from a call center or other support service share a browser with a client, typically to answer questions or help solve a problem). Some client segments are particularly keen on the use of digital media. Millennials, for example, and clients from the Asia Pacific region both display a strong preference for online interactions.

We therefore believe that private banks should enhance their digital capabilities in order to be able to communicate with their clients on their own terms, and so enhance the overall client experience. To do so, banks can consider collaborating with different types of partners. These might include:

- **Mainstream web platforms.** Working with mainstream web platforms can help strengthen relationships with clients and prospects, offering tailored services and leveraging the innovative capacity of these platforms.
- **Specialized web platforms.** Banks can leverage specialized web platforms to build investment and related forums targeting High-Net-Worth and Ultra-High-Net-Worth Individuals with tailored content.

In either case, banks will need to vet solution providers carefully, making sure they find a partner able to build the solution best suited to their needs, while meeting the stringent security, confidentiality and compliance requirements inherent to the private banking environment.

While digital channels are the wave of the future, and will take an increasingly important place in how banks interact with clients, traditional client interaction remains fully effective in Swiss private banking.

One particularly strong channel that private banks should consider strengthening is that of their partnerships with external asset managers (EAMs) and single-/multi-family offices.

Depending on the model, private banks typically provide the following services to EAMs and family offices:

- Custodian and transaction management services.
- General products and services.
- Investment research.
- Execution desks.

In a trusted “US” relationship, private banks could work with EAMs and family offices to improve their overall marketing and sales strategies. Fruitful areas of collaboration might include customer segmentation, customer targeting and the overall value proposition. By working together in this way, it should be possible to strengthen the business of both parties.

Client experience and feedback

Finally, most private banks today do not have well-evolved capabilities in terms of monitoring and then optimizing the client experience and strengthening client satisfaction levels. This is another area where we believe Swiss private banks can improve their skills, and so support their businesses.

Such strategic marketing activities require very specific expertise, and in general should not be fully conducted in-house. Private banks should instead consider the services of dedicated customer feedback specialists, in order to benefit from their knowledge, experience and capabilities. Banks can collaborate with such providers for expertise in such topics as best practice in conducting surveys, data and semantic analysis or alerting and reporting, among others. For example, customer feedback specialists typically provide the following support:

- **Feedback.** They can help capture client feedback, including via word-of-mouth, across multiple channels, various journeys and along the whole client lifecycle.
- **Analytics.** They can help banks analyze what really matters for clients and use predictive modelling techniques to measure the potential effects of any remediation measures the bank may be considering.
- **Insights.** Customer feedback specialists can leverage the insights found in the “Voice of the Customer” (VoC) and help spread these throughout the bank, again to support the remediation actions that have been decided upon.

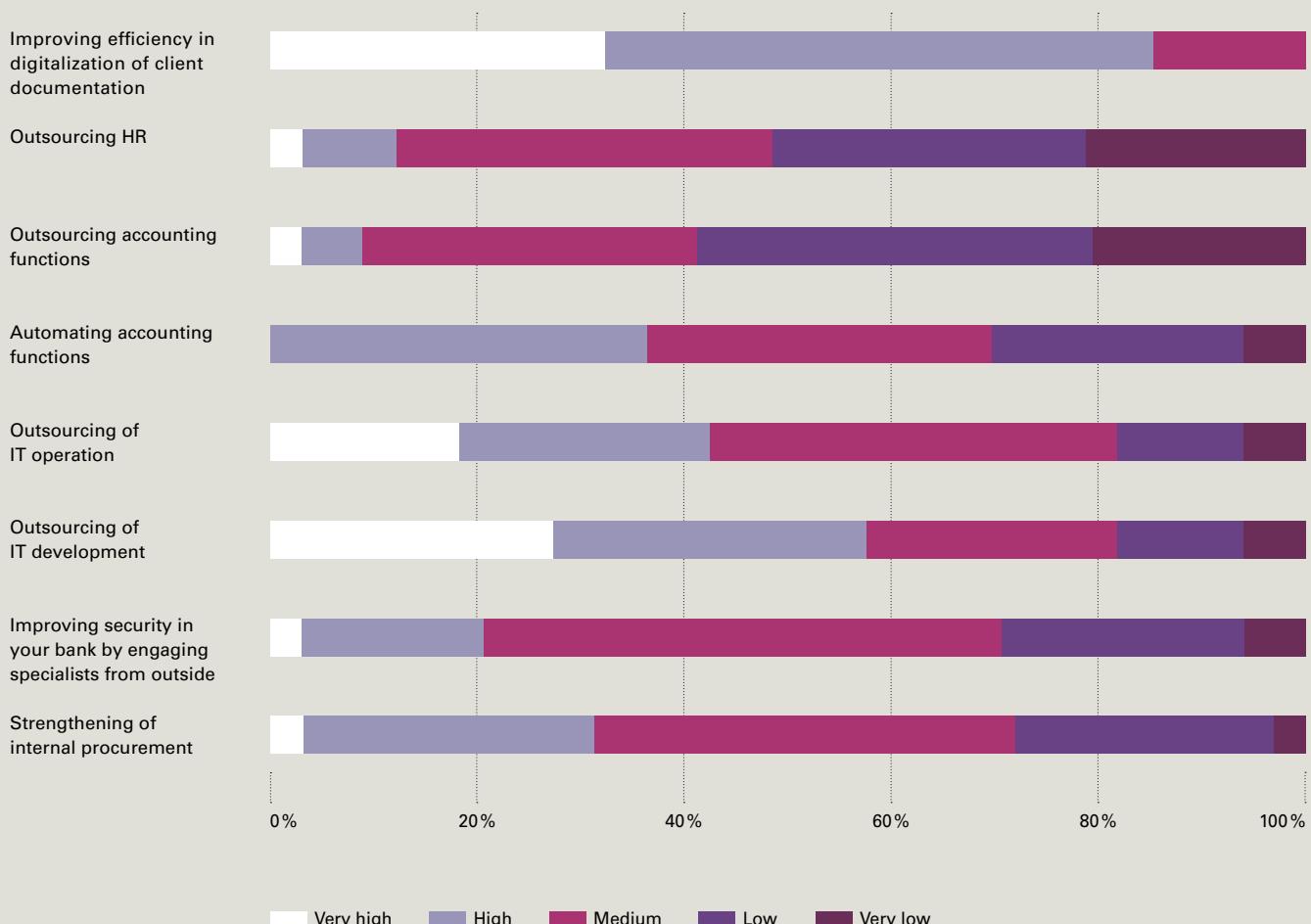
While these are all very desirable ends, in order for a partnership with a customer feedback specialist to bear fruit, private banks must be willing to share not only their data, but their intimate understanding of their High-Net-Worth and Ultra-High-Net-Worth clients as well.

Operating Model building blocks: Rebuilding the engine at Swiss private banks

Above we looked at some of the options Swiss private banks can consider to reinforce their business models, and why we think an increased emphasis on collaboration and partnerships will be key for Swiss private banks in their quest for growth.

In this section, we take a look at Swiss private banks' operating models, where we believe a similar dynamic is at play. Here too, private banks have many opportunities to profit from the skill and expertise of specialists, and to add best-in-class capabilities from different providers into their ecosystems. This is another area where the "US" approach can be a powerful means for banks to meet their challenges.

How do you consider the need for major investments in the area of "Support"?



In our survey, respondents identified outsourcing of IT, outsourcing of back office or digitalization as key investment areas for the operating model.

3. CORE BUSINESS PROCESSES

Processes

We think opportunities for cooperation and partnership abound in almost all parts of a private bank's operations, starting with its core processes. Among the areas where such collaboration could be most fruitful are:

- **Payments.** In our current era of rampant digitalization of almost all industries, payments in financial services is getting attention from a broad range of FinTech companies. These are offering new, streamlined, often more client-friendly and cost-effective approaches to the payments process. There are also significant developments happening at the infrastructure level, the rise of the blockchain being perhaps the most noteworthy. With its ability to enable fast, inexpensive and secure payments in a collaborative environment without the need of specialist intermediaries, the blockchain has the potential to be one of the most disruptive technological advances the industry has seen in a long time.
- **Cash/treasury management.** Cash and treasury management is a necessary but also often costly service, particularly when operating on a stand-alone basis. We think private banks could earn higher returns by transferring this activity, if offered, to a third-party bank or asset manager with deeper expertise and capabilities in this area.
- **Securities operations.** Middle and back office management of securities offers a wide range of possibilities regarding collaboration and the establishment of partnerships. Many large- to mid-sized banks have recourse to centralized intra-group shared services (i.e. custody services, brokerage, compliance monitoring, dealing desks and valuation). Specialized actors also propose such services enabling banks to adapt efficiently to variations in volumes, benefit from more advantageous pricing and significantly broaden their offering. Given the heightened complexity surrounding products and markets as well as the ensuing regulations, partnering with specialists enables to best service clients in a cost-effective manner.
- **Risk and compliance.** As we go into in more detail below, the cost of risk and compliance in the financial industry is skyrocketing, threatening to overwhelm the capabilities of many small to mid-sized banks. Here too, partnerships with specialists offer a potentially cost-effective way to increase safety while bringing down costs.

Automation and robotics

Similarly, alongside moving processes out to third parties in order to enhance capabilities, Swiss private banks can consider instead trying to automate fully some of their in-house processes and so drive efficiency and cost savings. Current developments in FinTech specifically, as well as in the broader technological realm, are leading to major advances in automation that could open up radical new possibilities.

In this context, Robotic Process Automation (RPA) in particular is expected to be a major source of disruption to banking processes. To take advantage of it, Swiss private banks can consider strategic partnerships with technology suppliers and consultants. We believe that over the next few years such partnerships will in fact become a key focus for many banks.

4. OPERATIONAL INFRASTRUCTURE AND TECHNOLOGY

IT and Operations

IT and Operations have traditionally represented a major portion of a typical bank's cost base. We see three possible paths to driving these technical costs down:

- **Incremental change to current operating model.** Banks can choose to improve the efficiency and effectiveness of their current operating and technological framework by optimizing certain elements of it. This could include efforts to simplify processes, reorganize approaches or change working methodologies, as well as to upgrade existing IT systems.
- **More radical change to disrupt the current operating model:**
 - Private banks operating within a larger group might consider the setup of shared service hubs where costs can be mutualized and where they can take advantage of countries and jurisdictions with low labor costs (near- or offshoring). Such collaboration typically occurs within groups, as the various legal entities can derive benefit from the economies of scale and access to cheaper resources.
 - Finally, banks can consider a partial or even full outsourcing of their back office and IT functions to an external partner.

Other support functions

Along with back office and IT activities, other support functions can be outsourced or centralized into a shared-services center as well. This is typically true for the following:

- Finance functions (i.e. accounting).
- Procurement management.
- Help desks or call centers, either client-facing or for internal staff.
- Travel arrangement services.

Moreover, other more peripheral and non-core activities that are good candidates for outsourcing by private banks could include property management, maintenance and cleaning, client reception, security, internal restaurant, logistics or archiving. This can lead to added advantages in terms of cost reduction and process flexibility while providing equal or even improved service quality.

While we believe outsourcing is generally a good choice for the back office and IT functions of many banks, Swiss private banks could also choose a different route by considering the creation of a common but separate company to provide operational services across a number of Swiss financial institutions. This could take the form of a cooperative agreement between competitors to build a shared-service solution that meets a common need across the group.

Such a strategic partnership between banks could lead to significant cost reductions through mutualization of costs across a very large base.

5. ORGANIZATIONAL STRUCTURE, GOVERNANCE AND RISK CONTROLS

Risk and compliance

The cost of compliance, legal and risk management functions has risen sharply in the private banking industry over the past 10 to 15 years. As a result, building strong capabilities in these areas today is both challenging and a very expensive enterprise. At the same time, these specialist capabilities are necessary if banks want to meet current and adapt to future regulatory requirements.

In these areas, size and scalability are critical to mutualizing cost, industrializing processes and developing broader expertise. Both also enhance the power of data analytics, notably by leveraging the potential of big data. Here too Swiss private banks could consider a number of collaboration options:

- **FinTech Partnerships.** For data-intensive risk processes, such as credit risk assessments, anti-money laundering and Know Your Customer (KYC) procedures, portfolio monitoring, risk-predictive analytics and stress testing, banks could consider partnering with FinTech companies. This would have the advantage of allowing them to leverage all available data and get strong, unbiased, statistic-based risk approaches without the need for heavy IT investment.
- **Intra-group service centers.** Larger banks could consider building intra-group service centers for legal, compliance and risk activities that are not too specific to local regulatory conditions. This could include second-level control, credit risk assessment, and fraud analytics.
- **Centers of expertise.** Banks could consider partnering with competitors to create local industry focus groups or even collaborative centers of expertise to share knowledge and experience and exchange ideas on complex topics around regulatory transformation, for example Automatic Exchange of Information.
- **Risk management outsourcing.** Banks could look at outsourcing some of their risk management tasks to providers specialized in risk management services. This could encompass everything from risk calculation to risk reporting. When completely outsourcing risk management, private banks must however keep in mind that they remain responsible and liable for their legal, compliance and risk functions. They therefore need to put in place a very robust control framework with these suppliers in order to ensure the quality and effectiveness of the outsourced risk activities.

6. PEOPLE AND CULTURE

Human Resources

Another area in which Swiss private banks could consider options in terms of outsourcing is human resources (HR) management. We are already seeing this happening, with some banks beginning to partner with their preferred recruitment agencies. Along with using such agencies as pure external suppliers, banks and agencies create operating model interrelationships as well. For example, some banks presently have in-house recruitment specialists from their preferred agency working directly with their internal HR teams.

Banks can also reap the benefits of economies of scale by outsourcing compensation and benefits management to specialist firms. They may also consider transferring the management of their training and development programs to specialist training companies that can develop, organize as well as deliver the trainings. Such specialist providers can also help banks optimize the career paths of key employees and help develop talent throughout the organization.

Outsourcing: An art that requires science

Of the choices above, outsourcing the key building blocks of the operating model generally offers much higher potential for cost reduction than internal optimizations.

Other typical benefits include:

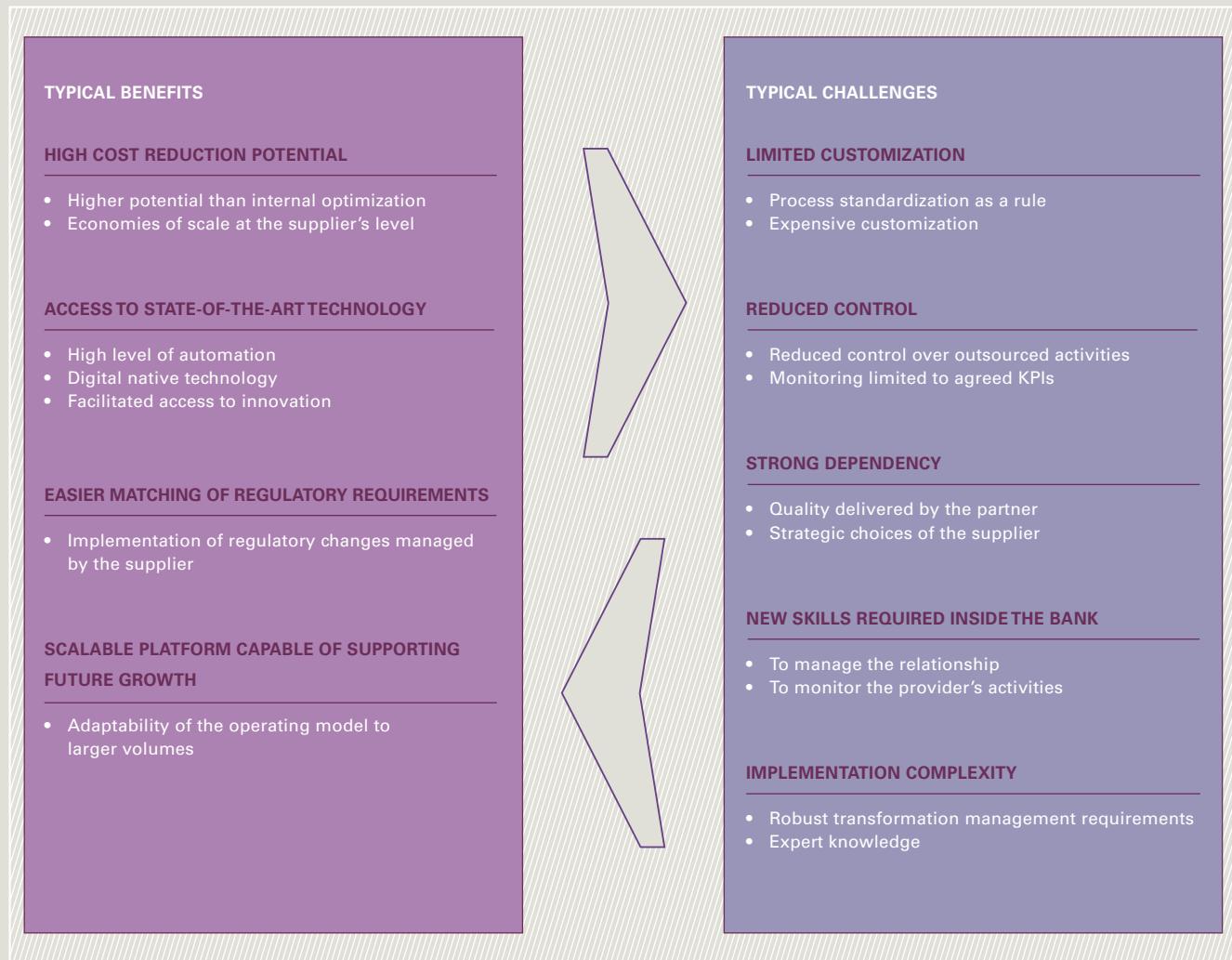
- Access to state-of-the art technology.
- Facilitated access to innovation.
- Easier matching to regulatory requirements.
- More efficient means to achieve a scalable platform capable of supporting future growth.

That said, outsourcing has its shortcomings as well.

Among those, banks need to keep in mind:

- **Process standardization.** In outsourcing, banks are generally forced to standardize in line with the supplier's processes, not use their own.
- **Reduced control.** Outsourcing naturally results in the bank losing or living with reduced control over its processes.
- **Dependency.** In outsourcing scenarios, banks become strongly dependent on the capabilities of their partner. Such dependency includes not only the overall quality of the service delivered. In outsourcing, any number of strategic technological decisions also become dependent on the provider. These can include when to upgrade, what technology to employ, and whether the provider wishes to put in the effort to remain cutting edge. Banks are also dependent on the provider's willingness and ability to invest in the future of its platform, and so have the capacity to adequately support the portfolios of banking clients in the future as well as to adapt to regulatory changes in a timely manner or offer additional services.
- **Skills.** Working with and monitoring the activities of an outsourcing provider is generally not part of the skillset of banks with no outsourcing experience. These skills need to be developed.
- **Implementation complexity.** Implementing a partial or especially a full outsourcing solution can be a major challenge. As we look at in more detail below, it requires robust transformation management skills and expert knowledge.

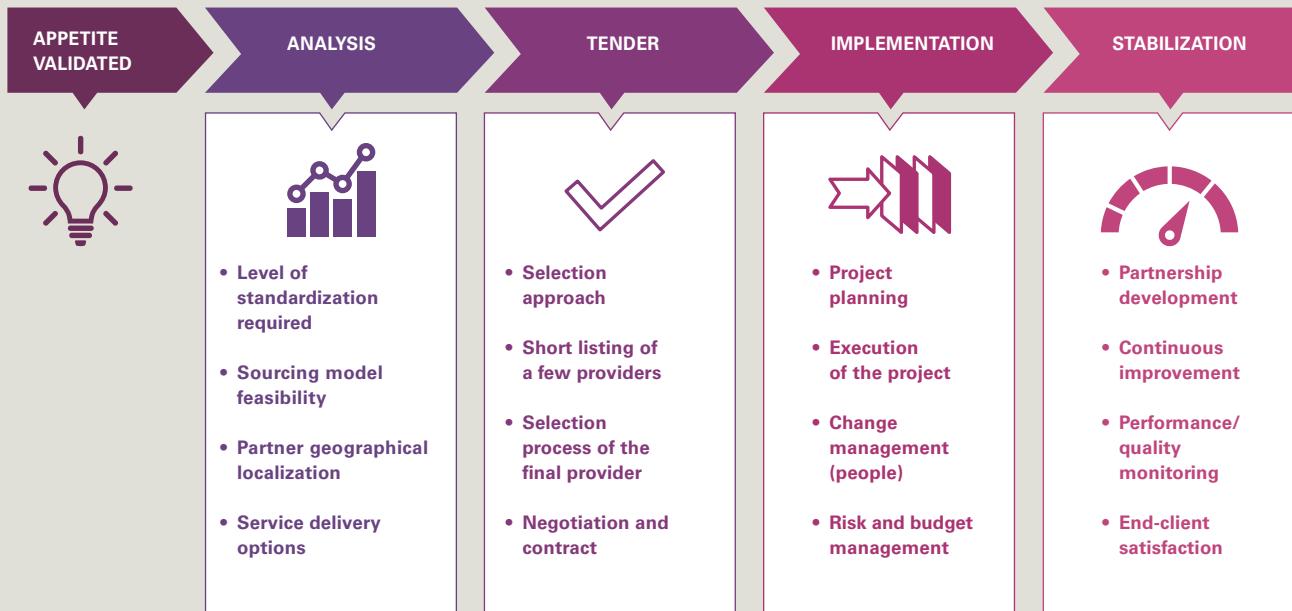
Outsourcing: benefits/shortcomings



Outsourcing has many benefits, but banks must be aware of the challenges as well.

When it comes to making sourcing strategy decisions, we have observed a number of different trends among private banks. These are often correlated with specific characteristics of the bank.

Outsourcing: Methodical and systematic process for a successful execution



By following a systematic process, banks can greatly improve the chances of successfully implementing an outsourcing project.

For example, the size of the bank can play a role. Larger private banks tend to operate their own service centers for their IT and back office functions, including near- and offshoring. These banks generally leverage the potential offered by their parent group. Medium-sized banks, in contrast, tend to focus on outsourcing their applications with an application service provider (ASP). Smaller private banks typically outsource both their back office operations and IT applications, using the services of a full business process outsourcing provider (BPO), which generally includes ASP in its offering.

The maturity of the bank plays a role as well. More mature institutions, with strong experience in outsourcing agreements, tend to source their services from several different providers, an approach commonly referred to as multi-sourcing. These banks can be said to have already started building an ecosystem of partners.

Once a bank has assessed its appetite for outsourcing and validated its approach internally, it needs to turn to execution. Success requires a methodical and systematic process. Important steps include:

- **Analysis.** The bank should conduct a detailed analysis of its situation and needs. This should include defining the level of standardization, assessing the feasibility of the sourcing model, geographical preferences for potential partners, examining service delivery options and considering a selection approach.
- **Tender.** The bank should then conduct a tender process. This should include a short list of two to three providers, leading to an objective selection based on the bank's specific requirements as well as its operating and business models.
- **Implementation.** Main execution challenges include the people and change management efforts along with the development of a quality working relationship with the provider.
- **Stabilization.** Once the outsourcing solution has been delivered and is live, the performance and benefits must be regularly measured. Continuous improvement efforts need to be implemented as well.

The considerations outlined in the section above hold true by analogy for most of the forms of collaboration.

Being sure: Dealing with the typical risks in cooperation and partnerships

Up to now, we have been discussing the general need for Swiss private banks to consider collaboration and outsourcing arrangements in their attempts to deal with today's difficult environment, and we have been outlining the relative merits of different approaches.

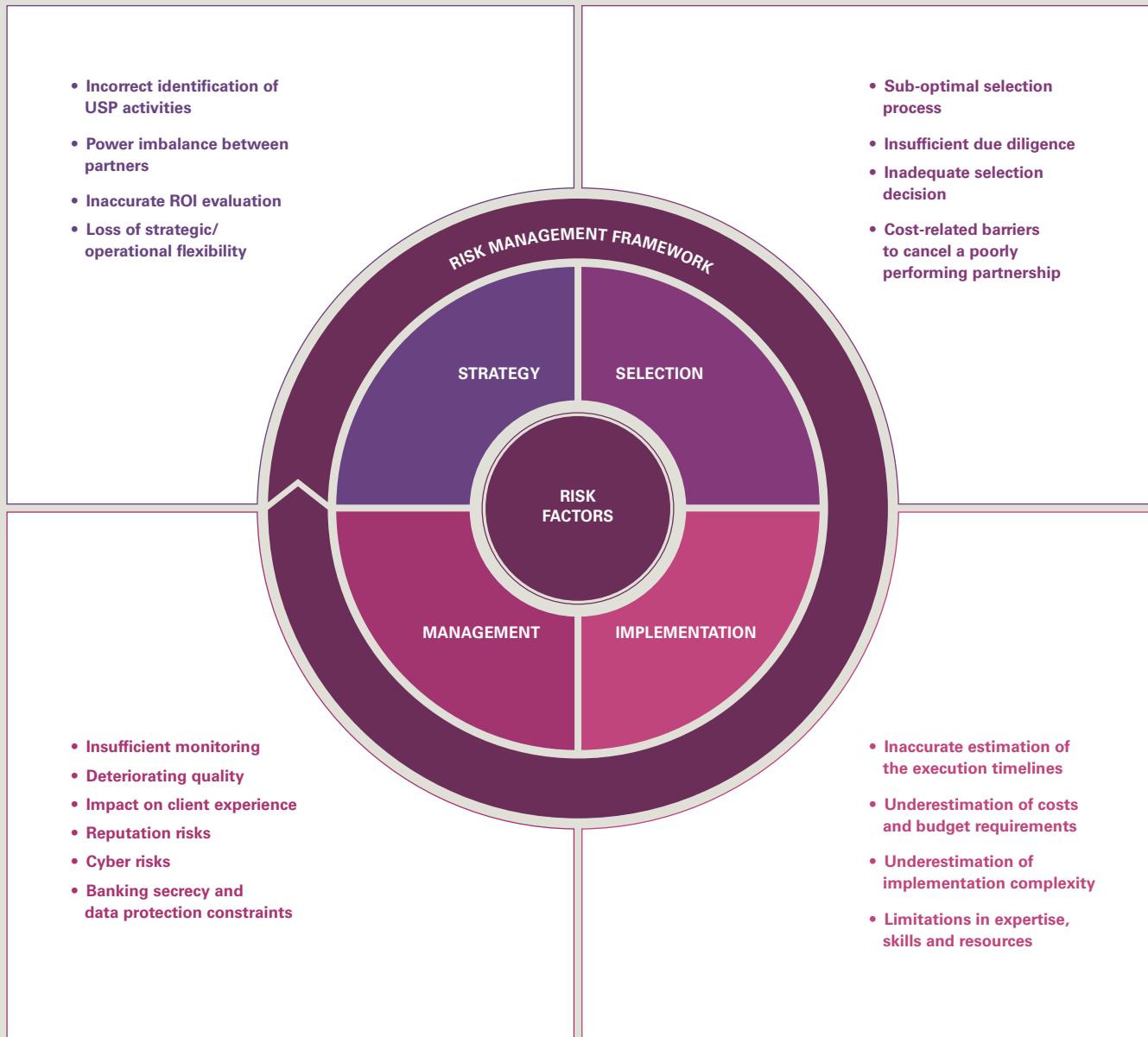
While we firmly believe that such approaches will play a key role for this industry, we are also aware that there are a number of risks involved. For any private bank wishing to pursue a collaboration or outsourcing strategy, these risks need to be taken into account. The major areas of concern include:

- **Strategy risks.** There are a number of strategic pitfalls private banks should consider. For one, they must be sure they have identified the correct non-USP activities, and are not abandoning any activities that could help them differentiate themselves in the market. Similarly, it is important to avoid partnerships which are poorly balanced, and in which a clear win/win situation cannot be immediately identified. It is also important not to make any mistakes when calculating the return on investment (ROI) to be expected from a cooperation or partnership project. Finally, the cooperation or partnership project should not result in a loss of any fundamental strategic or operational flexibility for the bank that could affect the bank's ability to make future strategic moves, or which might drastically curtail its future options.
- **Selection risks.** There are a number of risks involved in the process of selecting the right partner. Chief of these is employing an ineffective selection process overall, for example by being unaware of how such processes are best run or by underestimating what resources they require. As in any partnership, insufficient due diligence is a risk, and banks should ensure that their due diligence processes are sufficient to adequately evaluate all aspects of a potential partner, and so avoid unpleasant surprises. Even given the best efforts, there is always the risk of making a wrong decision. In private banking in particular, where client experience, trust and reputation play such a crucial role, wrong decisions can be costly. Banks must therefore take particular care to make the right choice from the beginning. This is even more crucial considering the potentially high cost of cancelling a cooperation agreement once it has been enacted.

• **Implementation risks.** When it comes to implementation, banks have several risks that they need to consider as well. While speed is often of the essence, setting unrealistic project execution timelines can be counterproductive in the end, adding unwarranted pressure on teams to produce results, and unrealistic expectations among project stakeholders. Another mistake that needs to be avoided is insufficiently estimating costs and therefore underfunding the project. Overly aggressive timelines and insufficient budgets are often related to another implementation risk: that of underestimating the true complexity of the implementation process. Last but not least, and a key risk underpinning all the others, is the risk of not having access to sufficient in-house expertise and resources of the type that are capable of delivering the necessary change.

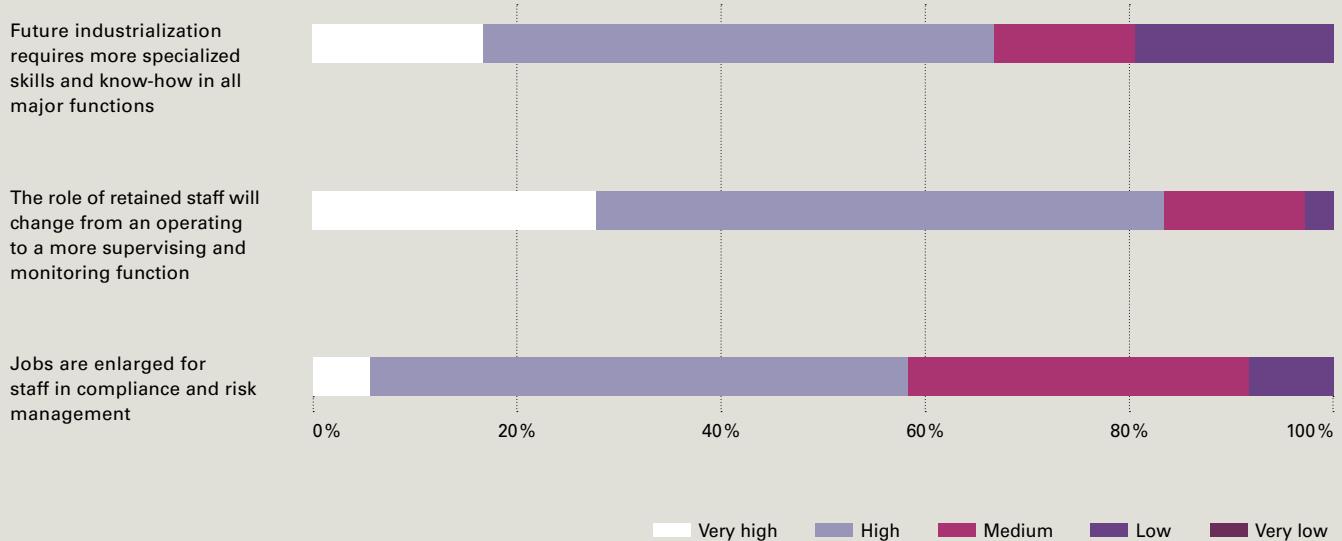
• **Management risks.** Finally, there are a number of risks involved in managing such cooperation and partnership arrangements once implemented. A key risk is failing to monitor the partnership on an ongoing basis, or not being sufficiently focused on continuously improving it. Such arrangements are never of the "fire and forget" variety, and instead need constant attention. Issues can also arise if there is insufficient clarity on the quality criteria that are expected to be met by the parties to the agreement. This risk can be mitigated to an extent by service level agreements (SLAs) that contain service debit/credit systems, thereby helping to reduce quality issues and encourage service over performance. If a partner in the agreement does not live up to its obligations, or delivers poor quality, banks run the risk of a deteriorating client experience and consequent damage to client perception of the bank and to the bank's overall reputation. In private banking, such reputational damage can easily lead to asset attrition, negative word of mouth, litigation and ultimately financial loss. Poorly balanced cooperation and partnership agreements are a risk as well, if they lead to the increasing self-interest of one party at the expense of the other, a so-called win/lose scenario. In today's digital age, cyber risk is also a growing concern. Cyber risks are particularly acute for private banks, where client confidentiality still plays a key role, and where strict banking secrecy and data protection laws are in force.

Typical risks in cooperations and partnerships



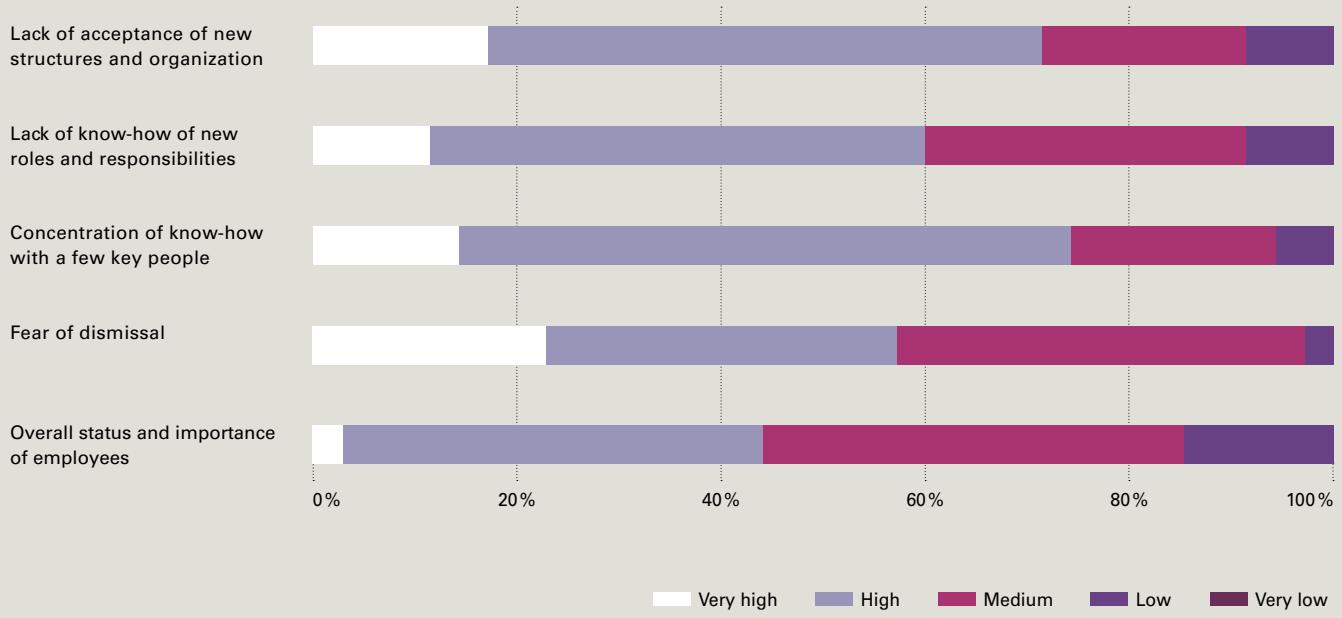
Collaboration comes with specific risks that need to be considered and actively managed.

How much do you agree with the following statements about roles and job profiles change caused by industrialization?



Private banking executives recognized, in our survey, that industrialization efforts require specific skills.

How do you evaluate the cultural risks associated with industrialization?



In our survey, executives confirmed industrialization efforts (incl. value chain disaggregation) would typically also require overcoming cultural as well as psychological barriers.

Going pro: Professionalism and expertise in transformation projects

Our look at risk above was not meant to be only a theoretical exercise. Over the past several years, we have been closely watching developments in the Swiss private banking market, and have observed some concerning developments.

Banks that have been considering large-scale cooperation and/or partnerships often underestimate the complexity of the transformation task ahead of them. Typically, such large-scale transformation projects take up to two years to complete. The negotiation phase on its own can last many months. Unrealistic expectations or lack of understanding of the realities has in several cases already led to concrete execution issues, including delays, budget overruns and disappointing return on investment (ROI) results.

To mitigate execution failure, we believe that banks need to employ a professional transformation process. That means ensuring they have access to state-of-the-art change capabilities. For any large-scale transformation effort, this will require expertise, rigor, the right methodology and a multi-disciplinary approach encompassing expertise across the strategic, legal, business, operational and technological dimensions.

We also think that banks need to be skilled in moving from strategy to execution mode. Just having a good idea, or even a good plan, is not enough. It must be acted upon in an effective way. Only by adopting a disciplined approach to transformation, can banks mitigate transformation risks, and increase their probabilities of success.

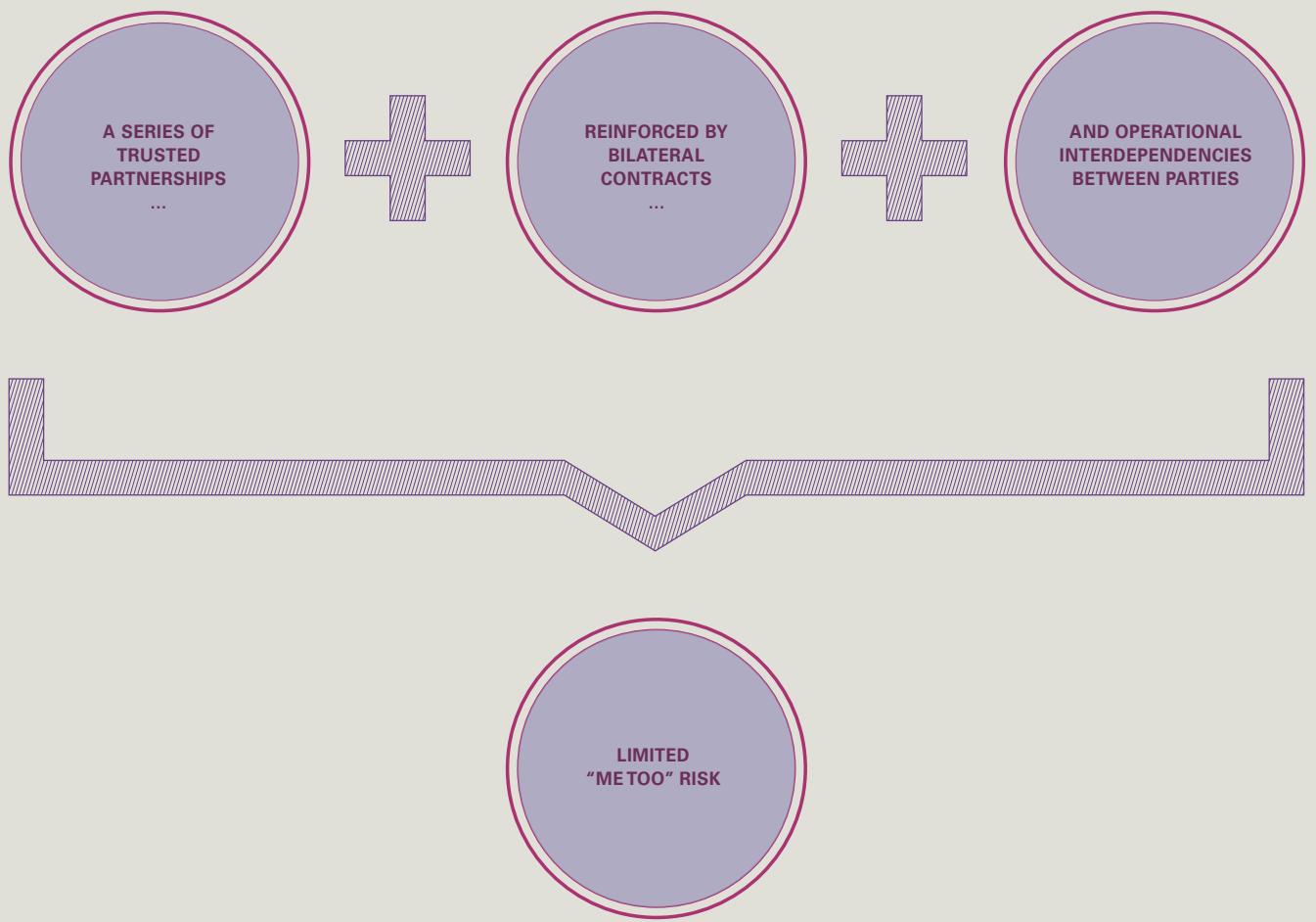
Summing up: Employing an "US" approach for sustainable competitive advantage

To conclude, we are convinced that adopting an "US" strategy and developing a robust ecosystem will lead to a model for banks that truly adds value for end clients.

Such an ecosystem can therefore become an important source of competitive advantage for those banks that can successfully build and make use of such ecosystems.

A series of partnerships based on mutual trust, reinforced by bilateral contracts that benefit all parties involved, and if possible encouraging operational interdependencies between the parties, can become a powerful advantage. Arrangements of this kind will also be difficult, if not impossible, for competitors to replicate, therefore mitigating "me too" risks from rivals.

Ecosystem and competitive advantage



Developing effective ecosystems will contribute building a sustainable competitive advantage for Swiss private banks.

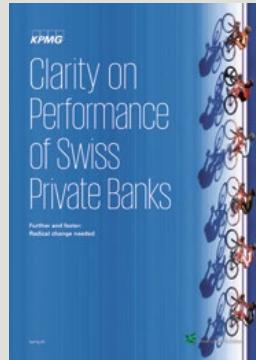
For these reasons, we think developing such ecosystems should be a priority for those Swiss private banks that are seeking to remain in the market and to grow.

By helping banks to develop a sustainable competitive edge over the long run, well-thought-out and effectively run ecosystems represent a promising path forward.

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