招商银行 CHINA MERCHANTS BANK | BAIN & COMPANY 贝恩公司

2011 China Private Wealth Report

China's private banking industry: Competition is getting fierce

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Preface: Intentions and expectations for the *2011 China Private Wealth Report*

Two years ago, China Merchants Bank (CMB) and Bain & Company jointly published the *2009 China Private Wealth Report*, providing the first in-depth look at China's private banking sector and customer segmentation within the emerging wealth market. The report used rigorous statistical modeling to measure China's private wealth market and pioneering research into high-net-worth individuals' (HNWIs) investment attitudes, drawing on CMB's private banking customer resources. Back in 2009, the financial crisis and increasing market volatility prompted China's wealthy to reconsider their investment strategies. Many individuals became more risk averse and started seeking professional advice about asset allocation to preserve family wealth. Private bankers took advantage of this significant shift in thinking to discuss portfolio management with China's newly wealthy and gain their trust. As a result, China's private banking industry started to take off.

Much has changed over the past two years. China's HNWIs have become sophisticated investors. They now have a moderate risk profile, expectations for reasonable investment returns and diversified wealth management needs. They also are knowledgeable about wealth management institutions' competitive positions and how best to use their strengths and expertise to enhance their own judgment and ability to invest. With an in-depth understanding of financial products offered by wealth management institutions, they are better able to make a thorough comparison before selecting products and optimizing their asset allocation, helping them to achieve liquidity and revenue targets with full utilization of asset control rights.

In addition, they recognize the worth of value-added services offered by wealth management institutions, and they are assessing them based on the investment requirements of their career, family and lifestyle objectives. HNWIs are increasingly aware of the advantages offered by private wealth management. To obtain a mix of expertise and opportunities, most HNWIs rely on several institutions to manage their investments.

As competition intensifies in China's private banking industry, many financial institutions are rushing to claim a share of the HNWI wealth management market. This influx of players with varied offerings changes the market landscape for HNWI wealth management, which is entering a new stage. With growing brand awareness among Chinese HNWIs, wealth management institutions are now focusing on brand building to differentiate their competitive advantages and enhancing customer loyalty by improving their end-to-end experience. To accomplish that, institutions' top priority is to identify target customers accurately by understanding their needs and then offering targeted products and services.

To follow the ongoing changes in China's private wealth market and HNWIs, CMB has worked closely with Bain. We have tracked shifts in the private wealth market, developed insights into the needs of various customer segments and monitored trends in the evolving private banking sector. This collaborative effort relied on Bain's extensive experience with private banking research, rigorous methodology and effective data analysis tools. It drew on CMB's knowledge of retail banking and high-end customer resources, along with research findings from the *2009 China Private Wealth Report*. The resulting data analysis enabled the creation of a wealth-distribution curve, which estimated the number of Chinese HNWIs and their combined wealth. We developed growth and financial projections for 2011 by comparing the 2008 data. By combining survey information from more than 2,600 HNWIs and interviews with more than 100 experts, relationship managers (RMs) and HNWIs who had access to authoritative secondary data, the report documents important changes over the past two years and developing trends. The 2011 study provides new insights into the investment attitudes and behaviors of Chinese HNWIs as well as their opinions of the private banking sector.

The updated version of the pioneering 2009 private wealth study, based on scientific analysis and large sampling, serves as the authoritative report on high-end private wealth management in mainland China. Once again, the collaboration between Bain, a global consulting firm, and CMB, one of China's premier financial institutions, sets a high bar for China wealth management market research and provides a foundation for the development of China's private banking industry.

Acknowledgments

This report is a joint effort between China Merchants Bank (CMB) and Bain & Company, Inc.

Two years ago, CMB initiated a groundbreaking, high-level analysis of China's wealth market. This report builds on the 2009 findings and advances research into shifts and trends in China's fast-growing private wealth market among HNWIs and the private banking sector. To collect firsthand information, CMB drew on its high-end customer resources and coordinated customer interviews and in-depth surveys with relationship managers. CMB also provided industry expertise, internal data and input on analytical methodologies. As part of the joint effort, CMB's executive team provided important suggestions for revising analytical approaches and refining the recommendations. We would like to thank Mr. Weihua Ma, president of CMB; Mr. Wei Ding, vice president of CMB; Mr. Jianjun Liu, executive vice president of the retail banking group; Mr. Kunde Chen, wealth management director; Ms. Jing Wang, vice general manager of the private banking department; Mr. Yuennan Chen, vice general manager; and other CMB team members, including Mr. Yi Xia, Ms. Yushi Shangguan and Ms. Songxue Li, as well as CMB headquarters' investment research, product, operation and marketing management teams.

In addition to the CMB customer and relationship manager surveys, Bain also interviewed many non-CMB customers and relationship managers. Two years ago, the Bain team built a market-sizing model with innovative methodologies. For the 2011 report, Bain continued the use of these methodologies and refined the classification of assets to reflect accelerated growth in recent years. In addition, Bain conducted detailed data analysis based on the research and survey results, and developed a clear conclusion and supporting arguments. We extend our gratitude to Bain partners, including Dr. Alfred Shang, Mr. Donie Lochan, Mr. Sameer Chishty, Mr. Philippe De Backer and Principal Ms. Jennifer Zeng. We also appreciate the efforts from team members, including Mr. Allen Li, Ms. Helen Deng, Ms. Cynthia Sun, Ms. Claire Lu, Mr. Leon Zhang and Ms. Lily Shao.

We would like to extend our gratitude to each and every customer and relationship manager who has participated in our interviews, as well as CMB employees who facilitated the interviews and the research. They were actively involved in data screening and customer surveys and interviews. They also shared their years of experience in the sector, assisting with market research and input to the Bain team. During the project, many Bain experts and other colleagues also helped with identifying interviewees, data collection, modeling, methodologies and analytical tools. Finally, many thanks to everyone at Bain Greater China, as well as other offices in the world, for their contributions.

We express our sincere gratitude to all those who contributed their valuable time and materials to the team.

Chapter I: 2011 Overview and trends in China's private wealth market

- **China's overall individual investable assets totaled RMB 62 trillion in 2010, a 19 percent increase from 2009.**

- **By the end of 2010, there were 500,000 Chinese HNWIs, with at least RMB 10 million in investable assets. Average investable assets per capita were approximately RMB 30 million. Aggregate investable assets for all HNWIs equaled RMB 15 trillion.**

- **We predict that the number of Chinese HNWIs will rise to 590,000 in 2011—nearly twice as many as in 2008—and their investable assets will reach RMB 18 trillion.**

- **In 2010, 15 provinces/municipalities had more than 10,000 HNWIs, increasing by four since 2008: Tianjin, Hunan, Hubei and Anhui. More than 50 percent of China's wealthy remain clustered in five provinces: Guangdong, Shanghai, Beijing, Zhejiang and Jiangsu.**

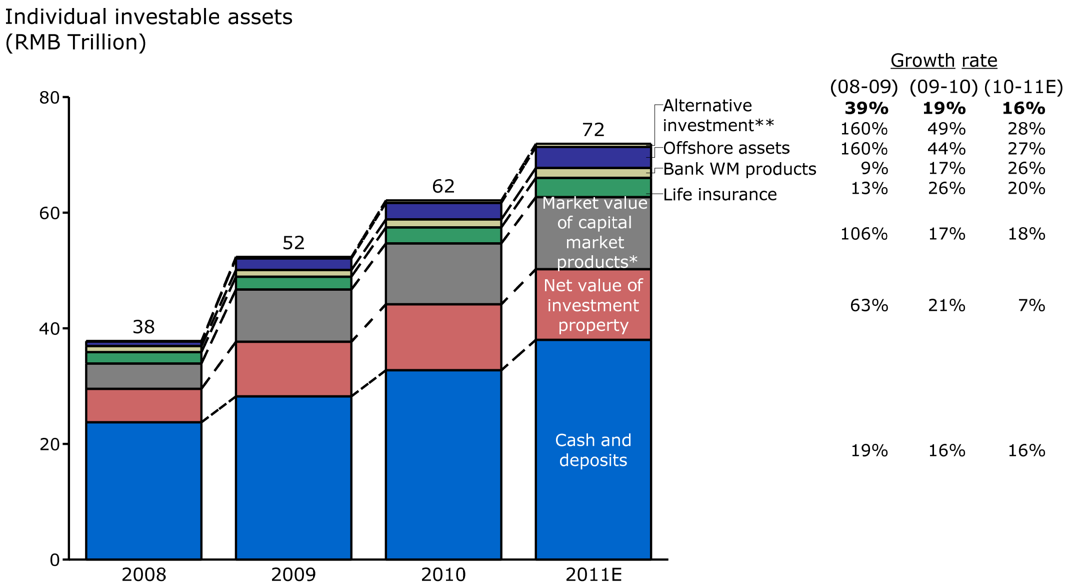
The enormous potential of China's private wealth market[1]

In 2010, China's economy recovered its rapid pace of expansion after the global financial meltdown, with double-digit GDP growth. After plunging share prices in 2008, China's major investment markets bounced back quickly, spurred by the Chinese government's stimulus package of RMB 4 trillion in 2009 and 2010. Stocks and real estate—the two most important markets—experienced the sharpest growth. Meanwhile, we found a sizable shift in Chinese HNWI asset allocation under way. Alternative investment vehicles emerged as a new focus for HNWIs. They include private fund invested in secondary market created through trust companies and real estate trusts, along with overseas investments.

By the end of 2010, the total value of investable assets[2] held by individuals in China in 2010 totaled RMB 62 trillion, a 19 percent increase, year to year. A detailed breakout shows that the market value of capital market products and net investment property values grew at a compounded annual growth rate (CAGR) of 55 percent and 40 percent, respectively, between 2008 and 2010 (see Figure 1). Other alternative investments represented by private equity and private fund invested in secondary market delivered a 100 percent CAGR in the same period, emerging as a popular investment option for HNWIs. Overseas investments, especially in Hong Kong, also won favor with HNWIs, producing a 100 percent CAGR.

[1]This report covers mainland China only, excluding Hong Kong, Macau and Taiwan.
[2]Investable assets are a measurement of the total investable wealth (assets with a secondary market and certain liquidity) of an individual. Investable assets include an individual's financial assets and investable real estate. Financial assets include cash, deposits, stocks (tradable and non-tradable shares of listed companies, hereinafter inclusive), bonds, funds, insurance, bank financing products, overseas investment and other investments (trust, private equity, private fund invested in secondary market, gold, futures and so forth), excluding assets such as owner-occupied real estate, non-listed companies held by non-private equity and consumer durables.

Figure 1: Total individual investable assets in China, 2008–2011

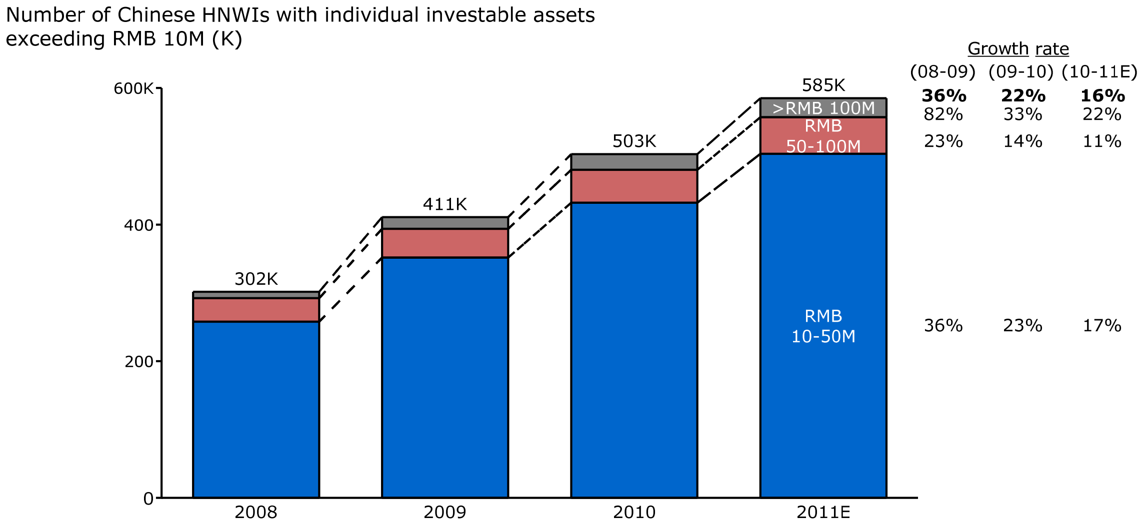


Note: *"Capital market products" include individually held stock, funds, exchange traded funds, open-end funds, bonds and over-the-counter bulletin board; **"alternative investment" includes trust, private funds invested in secondary market, gold and futures held by individuals.
Source: Bain's HNWIs Income-Wealth Distribution Model

The Chinese population of HNWIs continues to increase at a fast pace. In 2010, there were approximately 500,000 HNWIs in China, including more than 20,000 ultra-HNWIs[1] and 70,000 HNWIs with investable assets exceeding RMB 50 million. In one year, 90,000 HNWIs joined the ranks of the newly wealthy, a 22 percent increase since 2009. In terms of total worth, investable assets owned by Chinese HNWIs totaled RMB 15 trillion in 2010, or RMB 30 million per HNWI on average. The wealth owned by ultra-HNWIs totaled RMB 3.4 trillion, increasing from 16 percent of the total assets owned by HNWIs in 2008 to 22 percent (see Figure 2 and Figure 3).

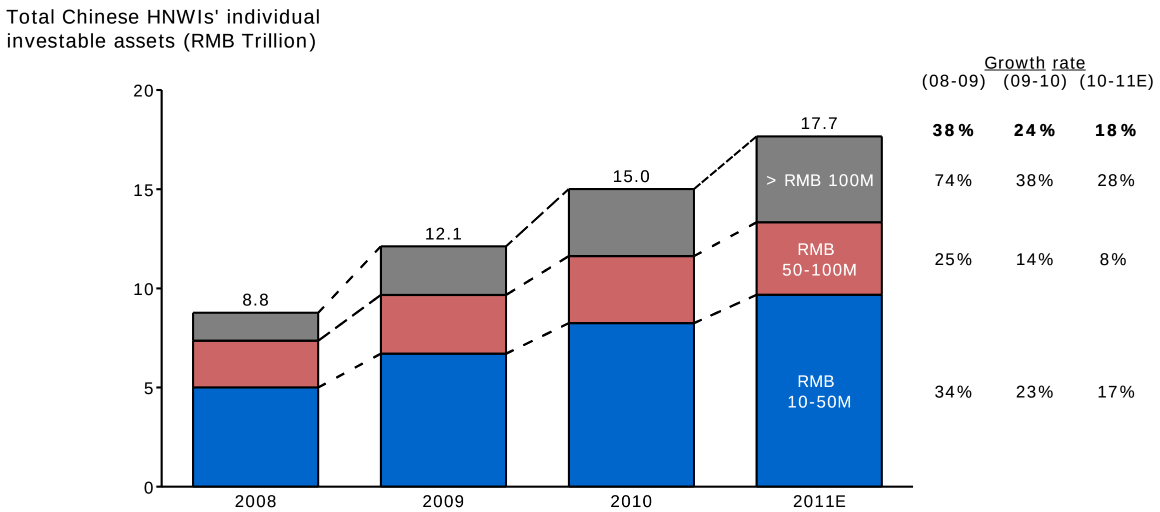
[1]This study defines ultra-HNWIs (ultra-high-net-worth individuals) as those who have at least RMB 100 million in investable assets.

Figure 2: Number and composition of China's HNWIs, 2008–2011



Source: Bain's HNWIs Income-Wealth Distribution Model

Figure 3: Total wealth and distribution of Chinese HNWIs, 2008–2011



Source: Bain's HNWIs Income-Wealth Distribution Model

Surprisingly, the number of HNWIs with incomes of RMB 10 million to RMB 50 million and more than RMB 100 million grew faster than HNWIs in the mid-income range of RMB 50 million to RMB 100 million (see Figure 2). There are two major reasons. First, the heated real estate market allowed a large number of individuals to increase their investable assets quickly, to more than RMB 10 million in 2009–2010, qualifying them as HNWIs. Second, as capital markets regained momentum, many entrepreneurs saw high returns from their successful enterprises—about 500 billionaires alone were created by the emergence of the China growth enterprise market.

Increasingly, HNWIs account for more of the nation's wealth, rising to 24 percent in 2010, up from 23 percent in 2008. We expect the number to reach 25 percent in 2011.

Taking into consideration macroeconomic factors that can affect China's wealth market, we predict that the number of newly wealthy will continue to grow in 2011, reaching about 590,000, which is a 16 percent increase, year to year, and nearly *twice* as many as in 2008. Individual investable assets may hit RMB 72 trillion, up 16 percent since 2010. Total wealth owned by HNWIs could reach RMB 18 trillion, an 18 percent increase, year to year. The doubling in the number of HNWIs in just two years demonstrates the enormous market and growth potential for China's private wealth market (see Figure 2 and Figure 3).

2009–2010 review of the China private wealth market and the outlook for 2011

2009–2010 review

Macro economy: In 2009 and 2010, the Chinese economy entered the final two years of the Chinese government's 11th five-year plan amid continued global economic turbulence. The government revitalized growth with a RMB 4 trillion stimulus package and easier credit. Real GDP increased by 10.3 percent, far exceeding growth targets. At the same time, inflation accelerated, with the consumer price index (CPI) rising by 4.7 percent in Q4 2010 for an annual average of 3.3 percent in 2010.

Cash and deposits: The Chinese government maintained low interest rates and a relaxed monetary policy to counter the impact from global turbulence, including the sluggish US economy and Euro zone debt crisis. In 2010, the government raised the reserve-requirement ratio six times and the deposit/loan benchmark interest rate twice. Even though M2 and new loan growth slowed, both still saw a considerable increase. The M2 currency increased 28 percent in 2009 and 20 percent in 2010, with new loans surging 32 percent and 20 percent, respectively.

Stock market: The stock market rebounded from the financial crisis, with the stock index soaring by 50 percent in two years. The capital market cap also grew with increased IPO financing and an end to the ban on non-tradable shares, as well as the tripling of A-share market capitalization. In addition, the stock market received a boost from the China Growth Enterprise Market, creating about 500 billionaires in one year alone.

Real estate market: China's real estate market has undergone a tremendous boom in the past two years. In the wake of the global recession, the real estate stimulus policy put in place in 2009 spurred high prices and turnover. The boom has doubled real estate market value, which now exceeds RMB 10 trillion, serving as a major accelerator of wealth growth. In the second half of 2010, the Chinese government successfully initiated several policies to control escalating prices.

Between 2008 and 2010, real estate prices and turnover increased 40 percent and 30 percent, respectively.

Private wealth management products and insurance: Bank wealth management products, offering low risk and higher returns than deposits, have gained popularity with investors. In the second half of 2010, growth of wealth management slowed as the Chinese government regulated the cooperation between banks and trust companies. But overall, they've grown over the past two years at a compounded rate of 15 percent annually. Meanwhile, life insurance has maintained steady growth, with a 20 percent CAGR between 2008 and 2010.

Alternative investments: As investment needs diversified and regulatory oversight increased, alternative investments have experienced a growth spurt. Real estate trusts, private fund invested in secondary market, private equity and investments in gold are an investment focus for HNWIs.

- Property trust products: As the real estate market heated up in 2009 and 2010, real estate trusts offered more financing opportunities for enterprises and high-end investors. They were well received by the market. In 2010, the number of real estate trust products increased almost 40 percent, year to year.

- Private fund invested in secondary market: New government policies for asset management products—such as broker collective wealth management, one-to-many funds discretionary accounts and single trusts—have made private fund invested in secondary market a popular investment option for HNWIs, providing both a high return and a high entry threshold. In 2010, the year-end balance was up 30 percent over 2009 for private fund invested in secondary market.

- Gold investment: Intensified inflation in 2010 boosted investor demand for precious metals like gold. Net capital invested in gold surged by about 80 percent compared with 2009.

- Private equity investment products: China's robust economy gave rise to a new generation of high-return private equity investment products, including a surge in new RMB private equity funds. Between 2009 and 2010, private equity investment products increased 30 percent.

Overseas investment: Overseas investment grew rapidly over the past two years, with assets more than doubling, fueled by overseas investment immigration and the rising market value of companies listed overseas. Hong Kong is fast becoming the major repository, home to more than 50 percent of overseas investment assets for mainland investors.

Outlook for 2011

Macro economy: We expect China to sustain solid GDP growth through 2011, guided by proactive fiscal and prudent monetary policies. GDP growth will be primarily fueled by fixed asset investment and consumption. With 2011 marking the first year in the government's 12th five-year plan, we will see tremendous demand for investments in central and western regional infrastructure projects, along with increased investments by local governments throughout the year. China's disposable income per capita now exceeds US$3,700, creating huge potential for domestic consumption. Along with a policy shift focused on raising living standards, personal consumption will experience rapid, sustained growth. We also expect increased net exports as the US economy improves and the European debt crisis eases.

However, expected RMB appreciation will continue to increase production costs for businesses and impact profitability. As a result, export enterprises will lose their competitive advantage. Overall, we predict continued growth for net exports but at a slower pace. Considering macroeconomic factors, we expect China's private wealth market will retain its steady growth.

Cash and deposits: In 2010, the Central Economic Working Conference took steps to curb inflation, shifting from a more lenient to a prudent monetary policy. In 2011, we predict the Chinese government will continue this more prudent approach, implementing a combination of regulatory measures to curb inflation further, including raising the reserve-requirement ratio/benchmark interest rate and controlling the credit rating scale. The increase in cash and deposits is expected to slow in 2011.

Stock market: We anticipate the rebounding stock market will continue surging in 2011 due to three major factors. First, the market scale of tradable shares will keep increasing with the lifting of the ban on non-tradable shares, along with growing IPO financing needs. Second, some real estate investment funds have moved into the stock market. The shift is due to excessive market liquidity from the government's massive economic stimulus policy and loose credit. Though the government's tightening monetary policy will reduce some liquidity, it is a difficult situation to remedy. Finally, inflation may result in lower interest rates on deposits, spurring individuals to invest in the stock market for higher returns and pushing the market index even higher.

Real estate market: New government regulations continue to cool China's heated real estate market. We expect escalating prices will slow in 2011. Tighter credit will constrain financing for real estate business loans and trusts. Meanwhile, higher interest rates will increase costs for real estate developers and buyers, reducing turnover. Also, the new policy places provisional restrictions on property purchases. As a result, we expect a continued decline in turnover and for price increases to slow or even lead to lower prices. We also predict the investment ratio will experience a significant drop. Three factors are at work: higher down payment ratios will result in lower investment leverage; restrictions on multiple property purchases will reduce the number of newly built homes; and real estate investments are diversifying, with funds shifting from direct property purchases to alternative investment channels such as real estate trust funds and investments in overseas property.

Private wealth management products and insurance: With expected interest rate hikes, bank wealth management products are winning more investors. We expect to see continued strong growth in 2011. Wealth management products are more protected from inflationary pressures and they offer a short holding period, lower risks and higher yields. Given China's aging population, life insurance also should maintain steady, fast growth, matching the 2010 growth rate.

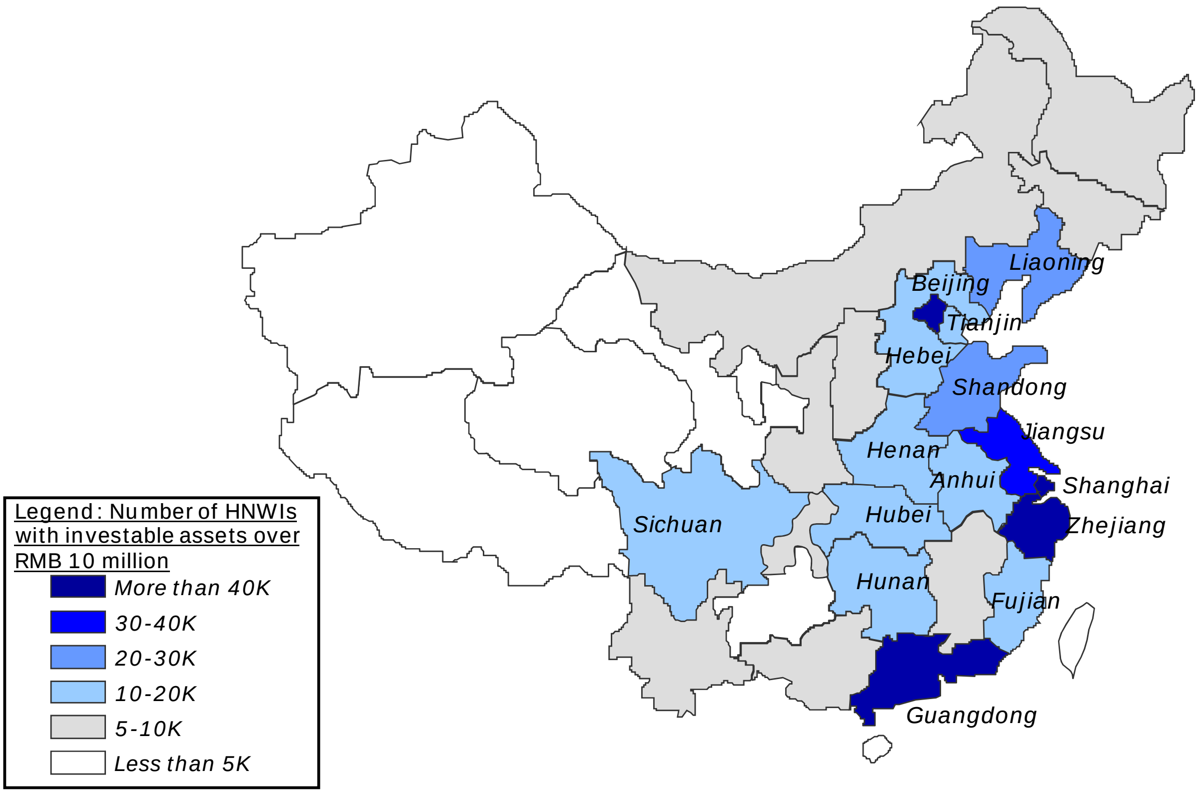
Alternative investment: With their high returns and high entry threshold, alternative investments will remain popular with HNWIs, continuing accelerated growth through 2011. New real estate market regulations will slow investments in real estate trusts. But private fund invested in secondary market and private equity funds will maintain their momentum in 2011. With no sign that inflation is abating, gold investments should increase. The emergence of index futures will lead to a dramatic increase in individual investments, with index investments expected to continue growing rapidly in 2011.

Overseas investment: With HNWIs' increasing need for global asset allocation and investment immigration, overseas investment will continue surging in 2011. We anticipate Hong Kong will maintain the momentum it gained in 2010 as a favored destination. Relaxed government rules governing the qualified domestic institutional investors (QDII) market is expected to experience a modest increase in 2011 as the government relaxes QDII rules and the overseas market rebounds.

Regional distribution of Chinese HNWIs in 2010

By the end of 2010, five provinces and cities had HNWI populations exceeding 30,000: Guangdong, Shanghai, Beijing, Zhejiang and Jiangsu. Ten provinces and cities had HNWI populations between 10,000 and 30,000: Shandong, Liaoning, Sichuan, Fujian, Henan, Hebei, Tianjin, Hunan, Hubei and Anhui. The HNWI populations in other provinces and cities were lower than 10,000. Since 2008, the number of provinces and cities with more than 10,000 HNWIs has increased. The total now is 15, with the addition of Tianjin, Hunan, Hubei and Anhui (see Figure 4).

Figure 4: Regional distribution of Chinese HNWIs in 2010



Source: Bain’s HNWIs Income-Wealth Distribution Model

Top 15 provinces/cities are home to 80 percent of Chinese HNWIs

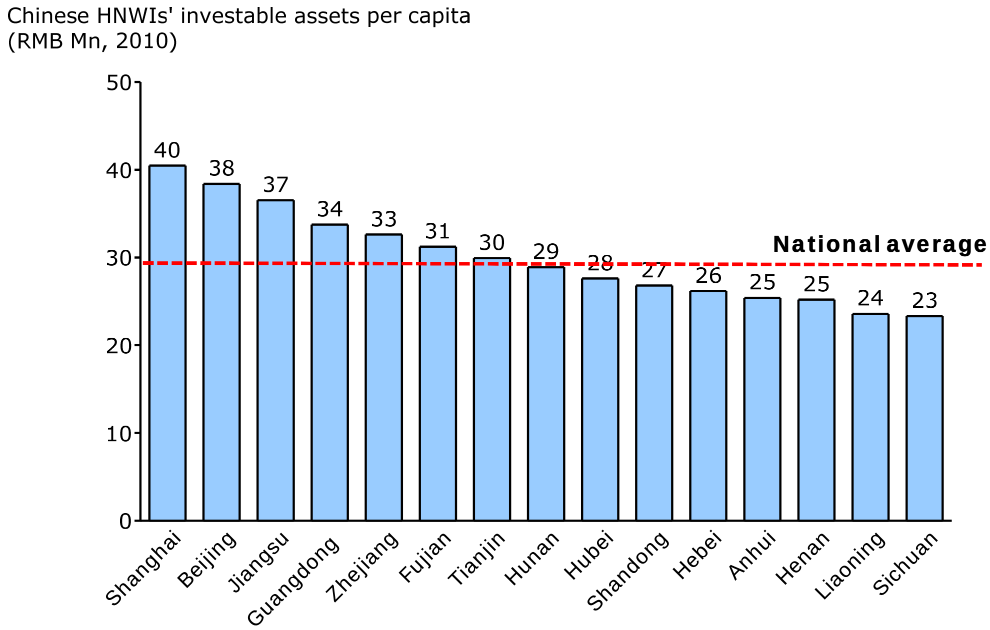
By the end of 2010, a total of 40,000 HNWIs were clustered in 15 provinces and cities, making up 80 percent of the national total. Each province/city had more than 10,000 HNWIs. Fifty percent of China's wealthy population—of 240,000 HNWIs—live in five provinces/cities, with more than 30,000 HNWIs in each province. Guangdong had the largest number of HNWIs, with a population of 70,000 by the end of 2010, 15 percent of China's total HNWIs. Shanghai and Beijing had the second and third largest populations, with 47,000 and 44,000, respectively.

The five provinces and cities with the largest net increases in HNWI populations remained Guangdong, Shanghai, Beijing, Zhejiang and Jiangsu. Guangdong had a net increase of 24,000 HNWIs. Shanghai and Beijing had the second and third largest net increases, 17,000 and 16,000, respectively.

HNWIs in eastern coastal areas had higher average investable assets than those from Bohai Bay and Central/West China

The eastern coastal area had investable assets per capita of more than RMB 30 million for HNWIs: Shanghai, Jiangsu, Guangdong, Zhejiang and Fujian. Shanghai had the highest investable assets per capita—about RMB 40 million. In two other regions, investable assets per capita ranged between RMB 25 million to 30 million: Bohai Bay, comprising Tianjin, Shandong, Hebei and Liaoning; and Central/West China, comprising Hunan, Hubei, Anhui, Henan and Sichuan. We can surmise that China's eastern coastal area has the highest average wealth and the largest HNWI population (see Figure 5).

Figure 5: Comparison of HNWIs' investable assets per capita in 2010



Source: Bain's HNWI Income-Wealth Distribution Model

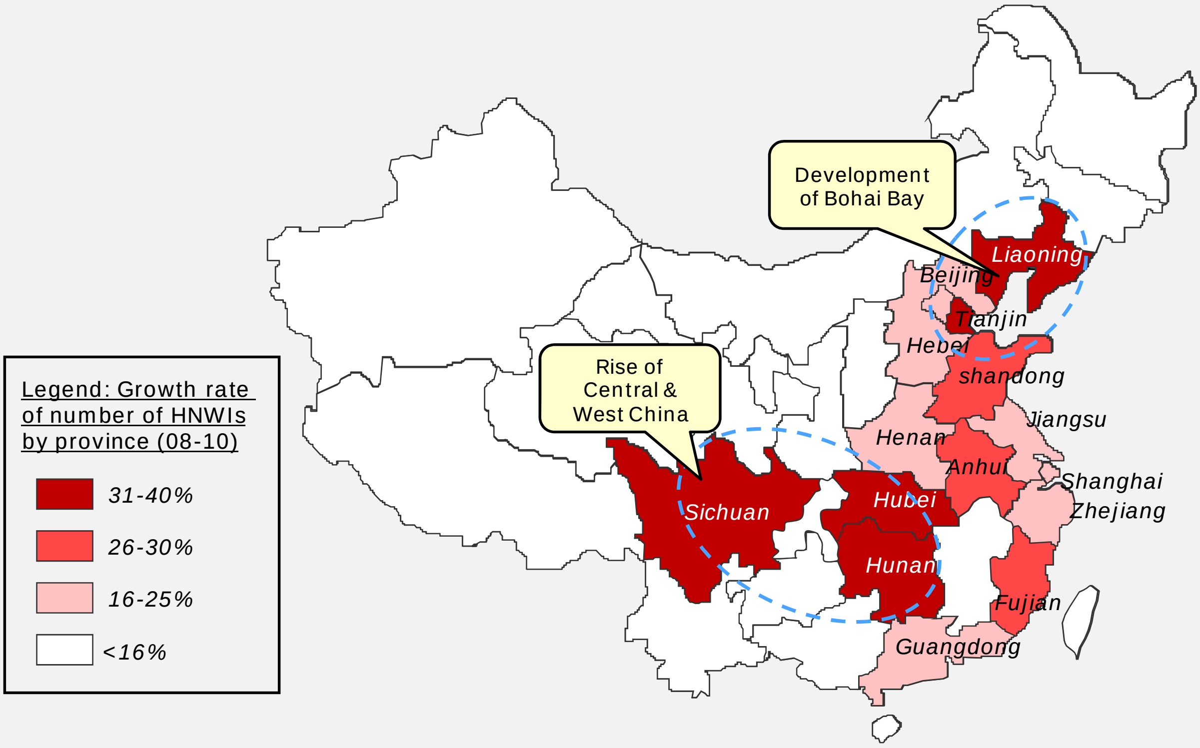
Spotlight I: Growth rates of HNWI populations vary across regions as a result of regional economic policy

There are distinct regional differences in China's private wealth market. While the eastern coastal area has more HNWIs with higher assets per capita, the number of wealthy individuals is growing at a faster rate in Bohai Bay and Central/Western China. These two regions have enormous potential as new growth hubs for China's private wealth market.

Among the 15 provinces and cities with more than 10,000 HNWIs, five experienced a 30 percent increase in their HNWI populations in 2008–2010: Tianjin, Liaoning, Hunan, Sichuan and Hubei. Three provinces and cities saw their HNWI populations grow at an annual rate of 26 percent to 30 percent: Fujian, Shandong and Anhui. In other provinces and cities, HNWI population growth increased 16 percent to 25 percent (see Figure 6).

Our analysis of growth rates found that among the provinces that have more than 10,000 HNWIs, HNWI populations in provinces and cities in Bohai Bay: (Tianjin, Liaoning and Shandong) and in central/western China (Hunan, Sichuan, Hubei and Anhui) increased faster than in eastern coastal area provinces and cities (Shanghai, Jiangsu, Zhejiang and Shandong) with growth rate of greater than 25 percent per year. However, five provinces and municipalities still remain the largest wealth clusters, with increases of 10,000 HNWIs in each area for the period between 2008 and 2010, currently totaling 30,000 HNWIs in each of these provinces/municipalities. In the last two years, more than 40 percent of incremental HNWIs live in the above five provinces and cities. There are almost 50 percent of China's total HNWIs clustered in these five provinces and cities.

Figure 6: Growth rate of Chinese HNWIs in 2008–2010 by region



Source: Bain's HNWI Income-Wealth Distribution Model

Growth rates of HNWI populations varied as a result of regional economic policies. During the 11th five-year plan, Bohai Bay developed steadily with strong government support. The emerging region is one of China's three major development zones, along with the Pearl River Delta and Yangtze River Delta. The Chinese government has issued a series of industry-related policies, focused on Beijing and Tianjin, to foster regional strengths, enable sustained economic growth and optimize the allocation of resources. Our HNWI income and wealth distribution model shows that Tianjin had the fastest-growing HNWI population among the above 15 provinces/cities, demonstrating the impact of economic development policies, including increased capital expenditures and construction in the Binhai New District within Tianjin.

Meanwhile, the central/western region is another focus of economic development, which began in 1999 after the Central Economic Working Conference enacted its western expansion strategy. The strategy makes development in the region a priority, including providing national investments. Recently, the central region received a renewed commitment when the State Council passed a plan to boost development. It calls for significant—and sustained—progress in the area's economic development. Our model found that out of the 15 provinces and cities, Hunan, Sichuan and Hubei are among the top five when we look at strong growth momentum, reflecting the government's development strategy for central and western China.

Chapter II: Chinese HNWIs' investment behaviors, segmentation and selection of wealth management institutions

- **Chinese HNWIs have a more sophisticated investment philosophy, with a preference for moderate risk, more diversified wealth objectives and an increased need for asset allocation and services.**

- **Occupation and size of individual investable assets are two of the most distinct indicators of major differences in risk preferences, wealth objectives and asset allocation.**

- **The major channel for wealth management has shifted to professional wealth management institutions. Brand is the most important criteria for selecting a wealth management institution, followed by expertise and relationship manager services.**

- **Chinese HNWIs are using multiple professional wealth management institutions to manage their investments. However, in the future, they may adopt a different approach, with a primary wealth management provider, supplemented by other institutions.**

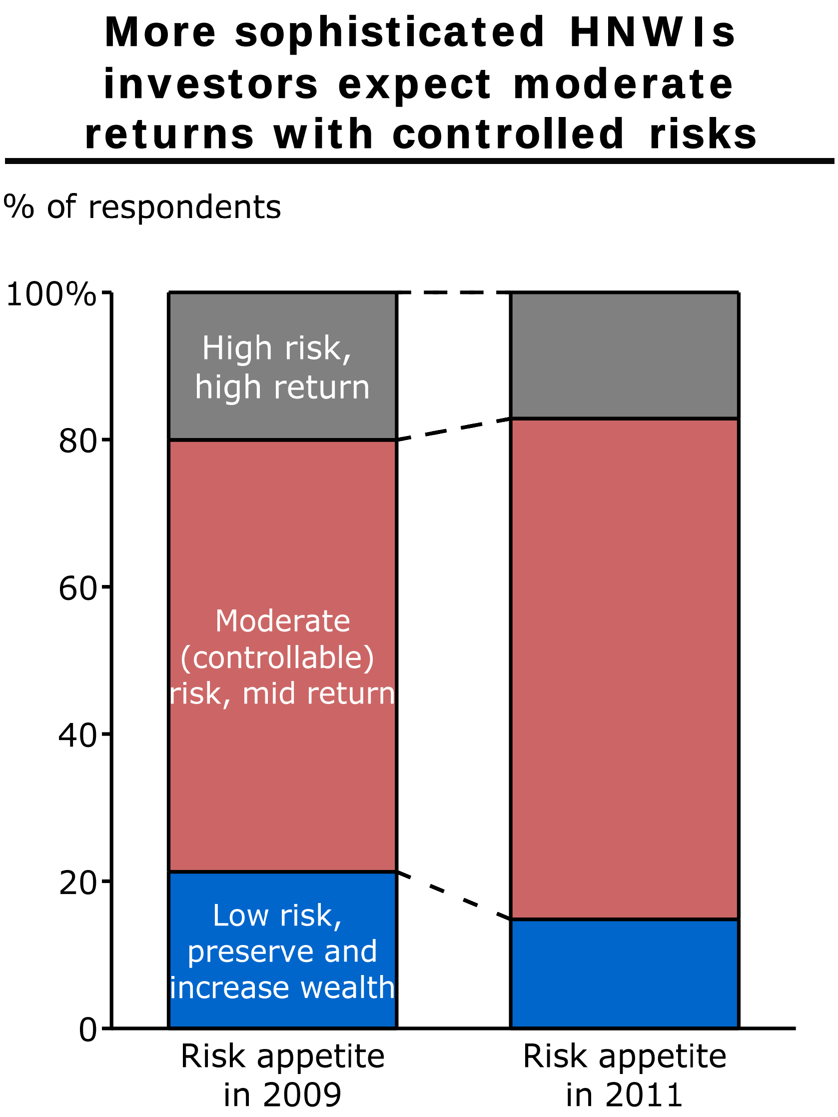
Chinese HNWIs have a more sophisticated investment philosophy, with a preference for moderate risk, more diversified wealth objectives and an increased need for asset allocation and services

After two years of rapid development, China's private wealth market has grown both in the number of HNWIs and the size of their assets. Wealthy investors are more knowledgeable, learning from wealth management institutions and their own experiences. They are less risk averse, diversifying their wealth objectives, and increasingly in need of asset allocation and services.

More Chinese HNWIs are willing to take moderate risks

In the wake of the financial crisis, wealthy Chinese investors have developed a deeper understanding of market risks. Our survey found that about 70 percent of China's HNWIs have investments delivering moderate returns with manageable risks, a significant increase—about 10 percent—since 2009. At the same time, fewer HNWIs expect high returns with high risks or low returns with low risks. Financial volatility taught them the importance of controlling investment risks. HNWIs who pursued high returns while ignoring risks—or failing to understand them—suffered losses. They now tend to select products aligned with their risk tolerance. They also have cut back on high-return/high-risk products. Investors who avoided losses during the financial crisis by shifting to high-liquidity and low-risk products are in a strong position. As the investment market recovers amid rapid economic growth spurred by major government stimulus, these products now offer higher returns with moderate risks (see Figure 7).

Figure 7: Chinese HNWIs' changing risk preferences during 2009–2011

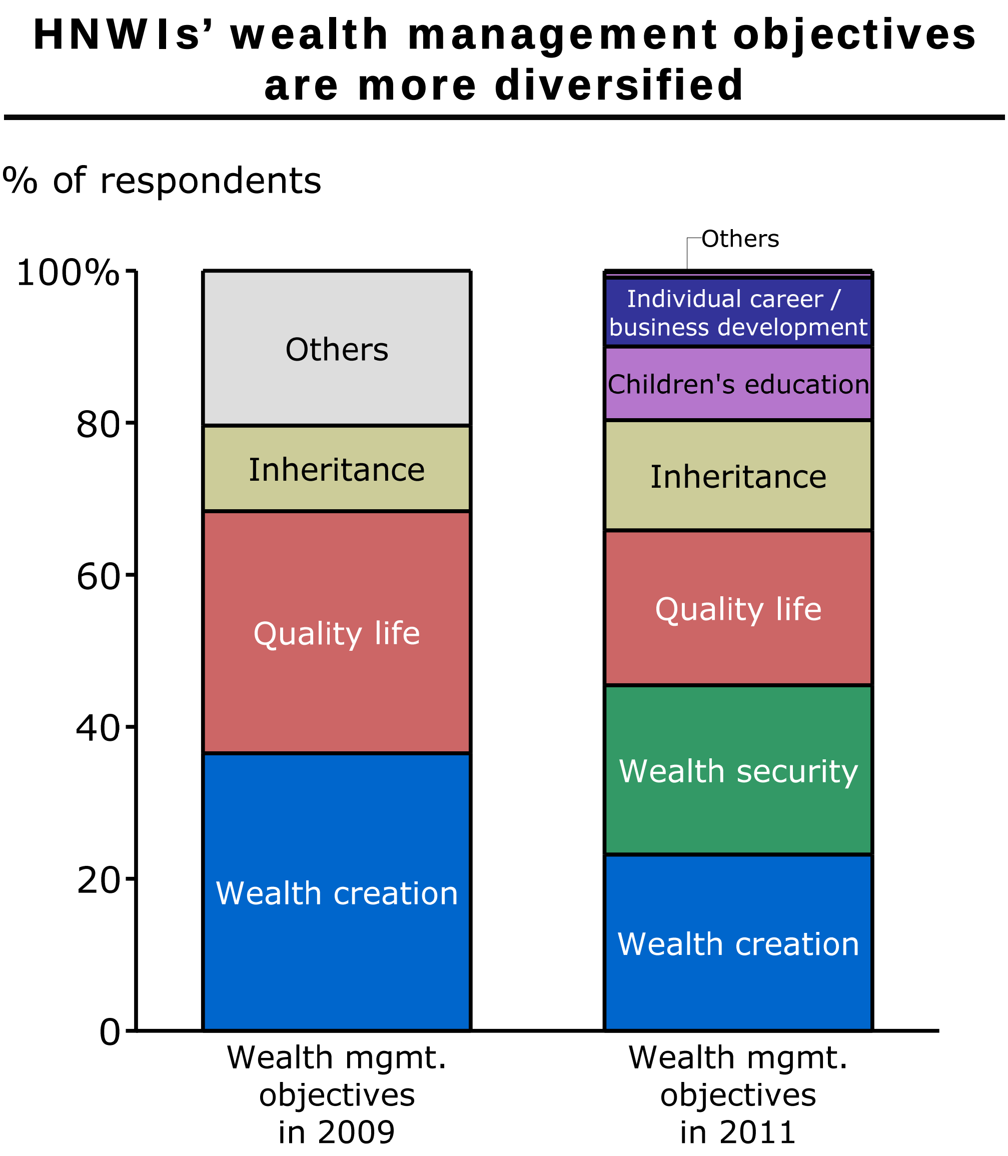


Source: CMB-Bain Chinese HNWIs' survey

More diversified wealth objectives

Two years ago, China's HNWIs had two major wealth objectives: accumulating wealth and improving the quality of their lives. In 2011, wealthy investors have more diversified objectives (see Figure 8).

Figure 8: Chinese HNWIs' diversifying wealth objectives



Source: CMB-Bain Chinese HNWIs' survey

Wealthy Chinese still view wealth creation and an improved quality of life as major investment goals. Each of these objectives was mentioned by more than 20 percent of our survey respondents. Their ambition is rooted in several shared traits. Many Chinese HNWIs are active, under 50 years old, with advancing or advanced careers. Their aggressive pursuit of wealth and career objectives motivates them to create even more wealth. But they are discovering that wealth alone is not enough. They want a high quality of life. Material comforts and social stature no longer are satisfying. Quality means having a satisfying spiritual life. Wealthy Chinese are devoting more attention to supporting charity and social welfare issues. Instead of simply making donations, they want to contribute to society through charity work. They also are cultivating improved manners and taste through travel, photography and collecting artwork and wine. Meanwhile, HNWIs are interested in attending events with other successful individuals where they can exchange ideas and develop rewarding relationships.

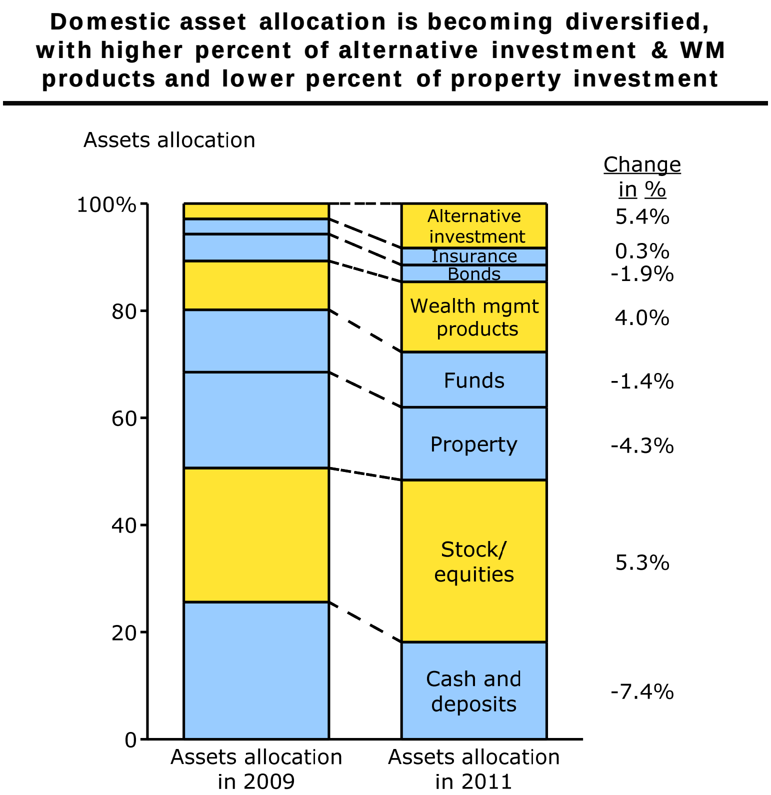
China's wealthy individuals are paying more attention to other wealth objectives:

- **Wealth preservation**: China's booming economy has allowed Chinese HNWIs to amass fortunes. They are proud of the nation's achievements that resulted from the reform and opening-up policy. But with a broader international perspective and better risk awareness, HNWIs are focusing more on ways to preserve their wealth, which impacts their decisions about domestic and foreign asset allocation.
- **Family inheritance planning**: A lasting family fortune is integral to traditional Chinese culture. With their lives and careers maturing, China's first generation of wealthy individuals is starting to think about the need for professional inheritance planning. That is especially true for the small group of China's ultra-wealthy, and older HNWIs already are taking action.
- **Educating children**: Providing children with an excellent education is as important culturally as preserving the family's wealth. In addition, HNWIs hope to give their children more opportunities for wealth management and social networking.
- **Business and career development**: The major objective for many of China's HNWIs, especially entrepreneurs, is to develop their businesses and careers further.

Diversifying needs for assets allocation and services

As HNWI become less risk averse with diversified wealth objectives, they need a comprehensive asset allocation strategy for wealth management. The evolving wealth market and a broader array of investment products give them new options. In early 2009, traditional, less volatile investment instruments—cash and deposits, stocks, property and funds—captured 80 percent of the wealth market. In 2011, the market share for these four asset classes has dropped to about 70 percent. Wealthy Chinese are adding more alternative investments to their portfolios. Investments like private fund invested in secondary market and private equity, representing recent market rushes and bank wealth management products, are taking up a larger share in Chinese HNWIs' assets portfolio, up by 5 percentage points and 4 percentage points, respectively (see Figure 9).

Figure 9: Chinese HNWIs' diversifying asset allocation



Note: Alternative investment include trusts, private equity investment, private fund invested in secondary market, gold and futures held by individuals
Source: CMB-Bain Chinese HNWIs' survey

A breakout of each asset class reveals key trends:

- The fact that cash and deposits declined as percentage of total assets is a significant indicator of diversification. HNWIs are no longer as satisfied with safe, stable investments such as cash. Over the past two years, the percentage of cash and deposits has dropped from 25 percent to about 18 percent, indicating an important shift in HNWIs' outlook about wealth management, private bank offerings and the overall economic environment. China's wealthy have developed more sophisticated wealth management strategies. They are increasingly diversifying their portfolios, employing a broad range of investment instruments to achieve moderate returns with manageable risks. HNWIs are interested in new wealth management products offered by banks and other financial institutions. Banks are launching low-risk products similar to cash and deposits, but yielding higher returns. Finally, massive government credit is resulting in high inflation, making cash and deposits even less attractive as interest rates drop.

- Stocks are recovering. In our 2009 report, the outlook for the stock market was bleak. But over the past two years, the market has experienced considerable appreciation, increasing the value of Chinese HNWIs' stock assets, as well as the percentage of their asset allocations. Some wealthy Chinese foresaw the rebound in 2009 and made investments that increased their share of stock among the total assets.

- The booming real estate market is slowing after prices skyrocketed over the past two years. A series of increasingly strict regulatory policies aimed at cooling the market dramatically curbed investor enthusiasm. Some consumers in our survey confirm that in early 2011 they started unloading some of their property investments. While our survey indicates that more than 90 percent of China's HNWIs plan to reduce or maintain their real estate investments, they want to shift from apartments to other investment vehicles such as real estate trusts and funds. The end result: the amount that HNWIs are investing in property is declining and may decline even more in the future.

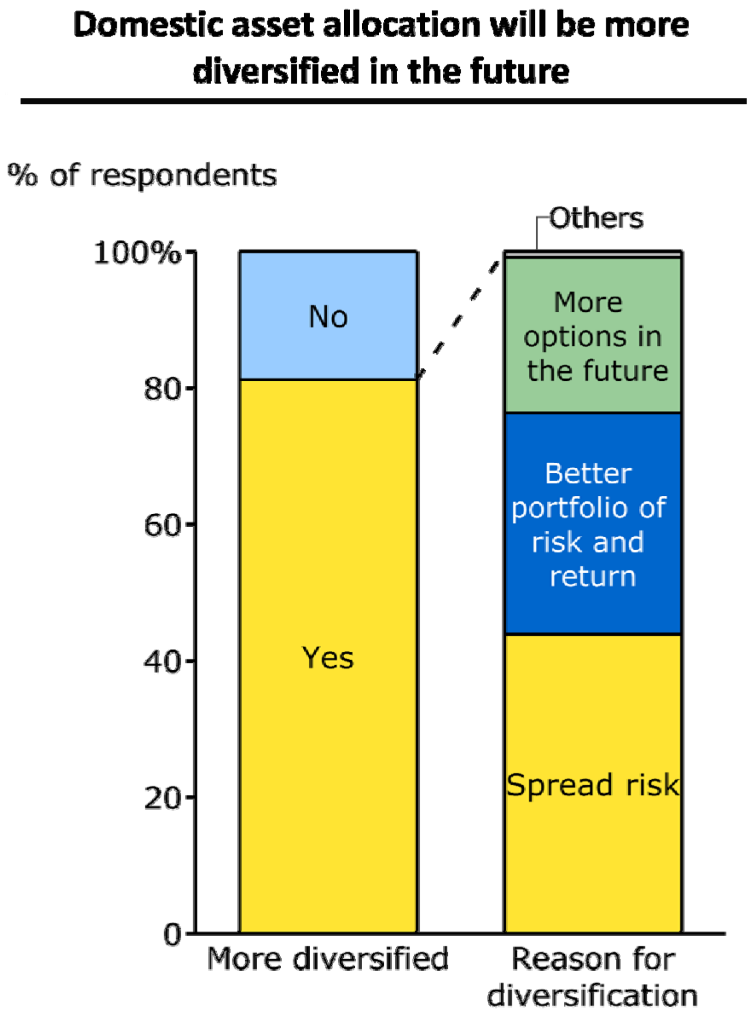
- The share of mutual funds in Chinese HNWIs' portfolios has slightly decreased, largely due to shares divested and the emergence of private fund invested in secondary market, which has higher returns and higher risk.

- Bank wealth management products have experienced rapid growth since they came on the market. The broad selection provides the flexibility for customers' different needs. Products with risks comparable to deposits usually have a better yield, giving them an advantage. With inflation on the rise, wealthy investors also are selecting inflation-pegged products with guaranteed returns. In addition, banks also have launched services that customize products for China's HNWIs. These new bank wealth management products and services are winning an increased share of wealthy individuals' asset allocation, gaining 4 percent in two years. They now are the third largest asset class after cash and deposits and stocks.

- Alternative investments such as private fund invested in secondary market and private equity emerged in recent years as a hot spot for HNWIs diversifying their portfolios. Investments with high risk and relatively high returns can be a critical component in diversified asset allocation. But there is a growing range of alternative investment vehicles. In addition to offerings by commercial banks' private banking services, many financial institutions are developing products designed for China's HNWI customers. The rapid development of these new products stems from relaxed regulations and policies governing funds' dedicated wealth management accounts and wealth management provided by trusts and securities houses.

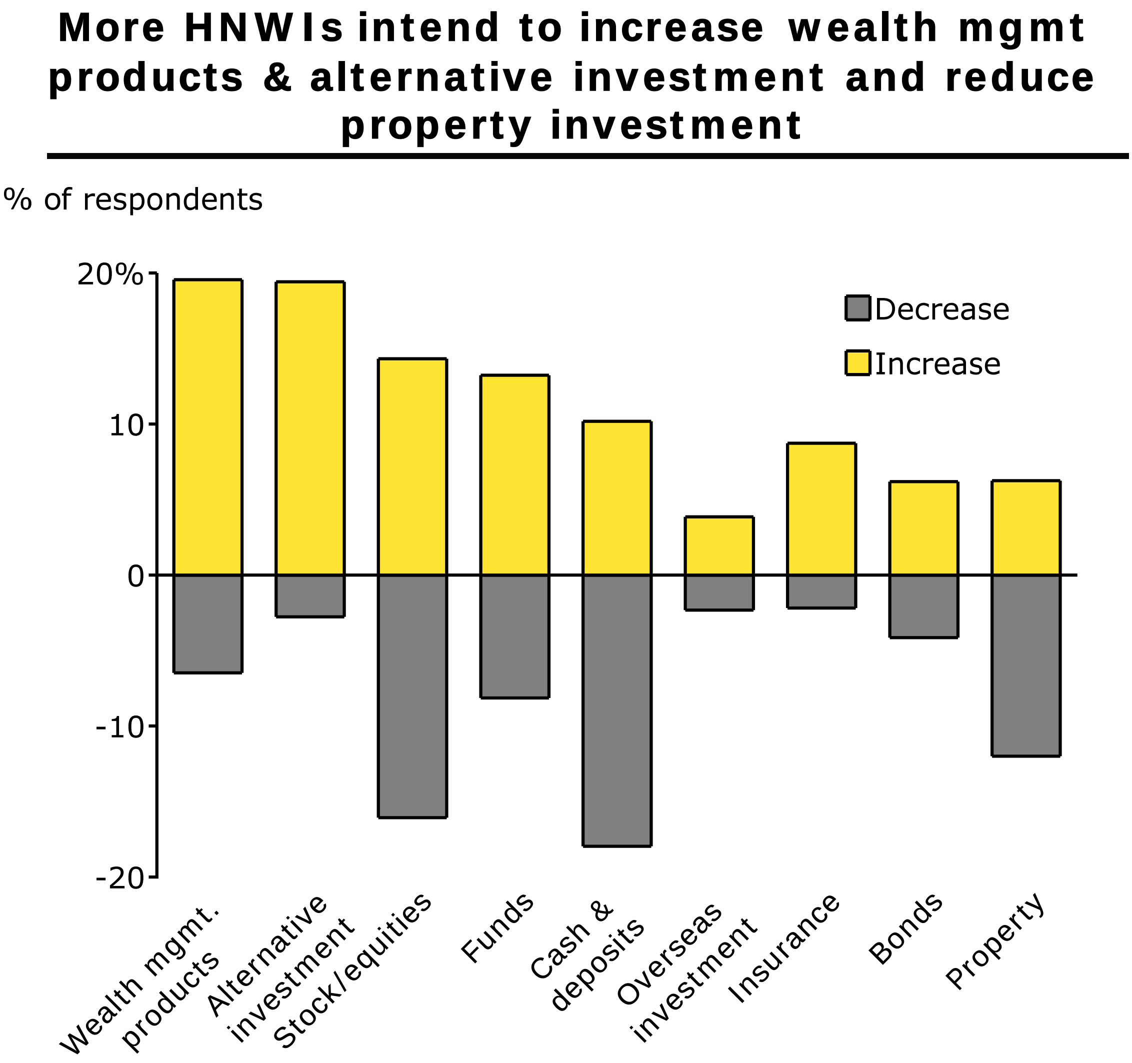
Based on in-depth research and extensive customer interviews, we found that more than 80 percent of survey respondents plan to diversify their asset allocation in the future. The major motivation is to spread the risk. As China's HNWIs develop a more sophisticated understanding, they recognize that the best approach is to avoid putting all their eggs in one basket. They also are less risk averse, making them more willing to develop portfolios that include a range of products delivering strong returns, aligned with their own risk tolerance. And intensifying competition in the fast-growing wealth management market will lead to more investment options with each institution launching products aimed at attracting wealthy customers. The rich array of options will encourage increased diversification of HNWIs' assets (see Figure 10). We expect that bank wealth management products and alternative investments will maintain their momentum. By next year, we anticipate they will be the preferred investment vehicles for China's wealthy (see Figure 11).

Figure 10: Future trends in asset allocation



Source: CMB-Bain Chinese HNWIs' survey

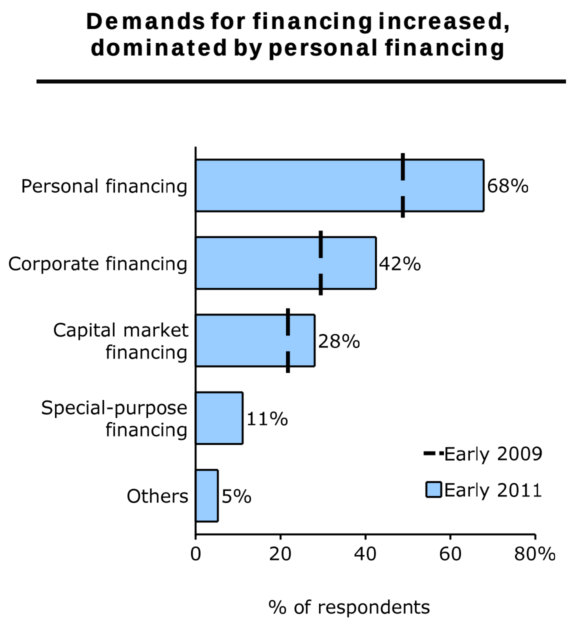
Figure 11: Investment trends by asset class in 2011

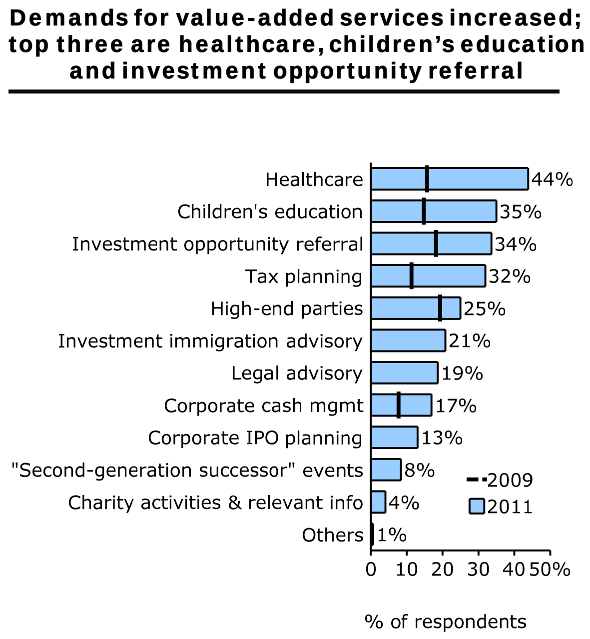


Note: "Alternative investment" includes trust, private equity, private fund invested in secondary market, gold and futures held by individuals
Source: CMB-Bain Chinese HNWIs' survey

As HNWIs diversify their wealth objectives, they need a better understanding of complex financing requirements and other value-added services. Today, wealthy Chinese are more aware of the private banking sector due to the industry's education and promotional campaigns. To meet HNWIs' growing needs, wealth management institutions must fulfill the increased demand for personal financing and other value-added services (see Figure 12).

Figure 12: Chinese HNWIs' needs for financing and value-added services





Source: CMB-Bain Chinese HNWIs' survey

Financing services with the highest demand include personal, business and capital market financing. Our survey found that 70 percent of respondents are looking for personal financing, almost 20 percent higher than in 2009. The finding suggests that more and more Chinese HNWIs are turning to banks or wealth management institutions for their personal financing needs, allowing them to achieve capital turnover and improve their investment leverage. In addition, Chinese HNWI business owners hope wealth management institutions will provide corporate services, especially corporate financing. Demand for such services is required by 40 percent of our respondents, up 10 percent since 2009. Another 30 percent of HNWIs want wealth management institutions to provide capital market financing services, including lending and borrowing from securities companies, to achieve higher investment returns. Demand for capital financing services has risen 5 percent since 2009. Meanwhile, China's ultra-wealthy, with more than RMB 100 million in investable assets, want specialized financing services for large purchases such as yachts and private jets.

Demand also is up since 2009 for value-added services from wealthy management institutions. Services that top HNWIs' list include:

- **Healthcare**: As Chinese HNWIs' devote more attention to improving the quality of their lives, healthcare-related services have the highest demand. Obtaining high-quality medical services is an issue across all segments of society. Many HNWIs we interviewed said they have difficulty booking appointments with experienced doctors. They hope that private banks will use their resources to provide services, such as gaining access to respected physicians.

- **Educational services:** Depending on their children's ages, China's wealthy require different education-related services. The highest demand is for private banks to organize activities targeted at HNWIs and their children, such as family trips and summer camps in remote areas.

- **Investment opportunities:** In addition to wealth management services, HNWIs also want banks to organize events that open the door for other investment opportunities—investment presentations, themed-investment lectures and investment workshops, helping them develop insights into market trends and potential investment opportunities.

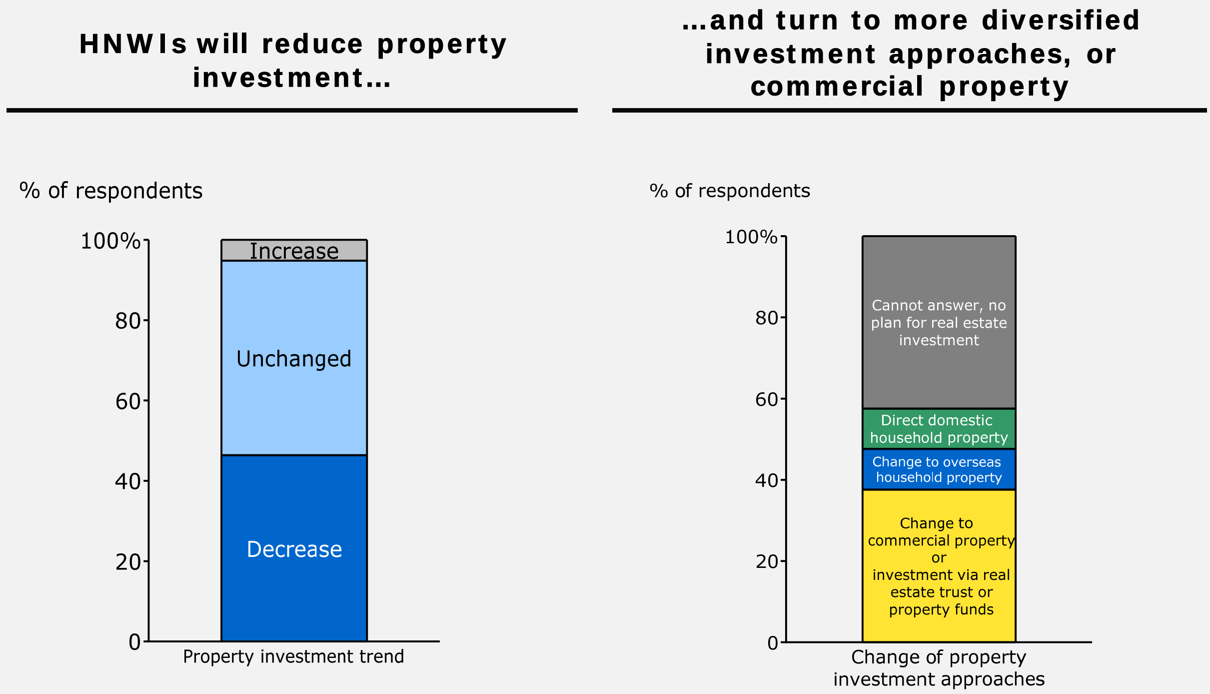
- **High-end business events:** Wealthy business owners view high-end parties as a top value-added service that wealth management institutions could provide. Such events help broaden their knowledge, enable networking and develop friendships.

Spotlight II: HNWIs shifting investments from residential real estate as regulations cool the market

In recent years, the government has enacted real estate market policies aimed at curbing soaring housing prices. The measures include restrictions on purchases and tougher loan requirements. For example, the General Office of the State Council issued a policy known as the "Eleven National Principles" on January 10, 2010. It made it more difficult to purchase a second apartment by requiring a minimum down payment of 40 percent. A year later, on January 26, 2011, even tougher mortgage requirements were adopted in the *Notice of the State Council on Resolutely Curbing the Soaring of Housing Prices in Some Cities*, which raised the down payment minimum to 60 percent for a second apartment. Local governments in Tier 1 and 2 cities supported these policies by developing detailed rules of their own. The areas include Beijing, Shanghai, Tianjin, Qingdao, Nanjing, Chengdu, Nanning, Taiyuan, Guiyang, Harbin, Shijiazhuang and Wuhan.

Within the real estate industry, there's increasing concern about the future. We surveyed more than 300 real estate industry employees in 30 domestic provinces and municipalities. Most respondents believe that real estate investors are less confident and question whether the market will continue growing in 2011. Their belief is confirmed by interviews with HNWIs and relationship managers. They show a fading interest in the residential housing market. Within their portfolios, real estate investments dropped from 17.9 percent of their total asset allocation in early 2009 to 13.7 percent in early 2011. When asked, "Would you decrease the amount you invest in the real estate market (including all investment vehicles) over the next one to two years?" The overwhelming majority—90 percent—of the HNWIs surveyed said they had no plans to increase their property investments. And half said they are gradually reducing capital invested in the real estate market. We also asked, "Would you change your approach to making investments in the real estate market over the next one to two years?" Less than 10 percent of the HNWIs said that purchasing residential housing would remain their primary investment strategy. Almost 40 percent expressed an interest in shifting to commercial property or diversifying their investments through real estate trusts or property funds. The findings document the impact of the government's new controls on the real estate market. China's wealthy are moving away from residential property purchases in favor of commercial real estate and diversified investments (see Figure 13).

Figure 13: Chinese HNWIs' attitudes towards future investments in the real estate market



Source: CMB-Bain Chinese HNWIs' survey

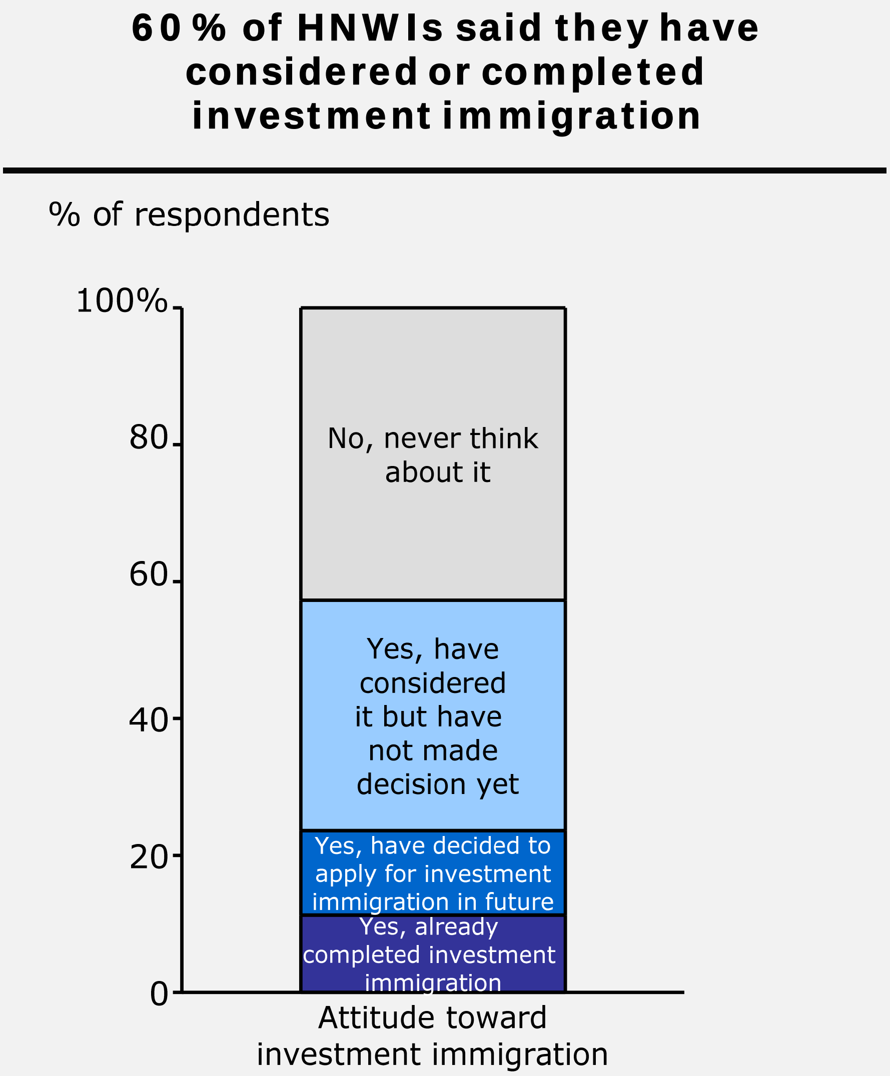
Spotlight III: More Chinese HNWIs pursue investment immigration as their overseas assets increase

Between 2008 and 2010, Chinese individuals with overseas assets experienced rapid growth, with a compounded annual growth rate of 100 percent. Hong Kong is the main destination for their foreign investments, accounting for 50 percent of all Chinese overseas assets and growing at a compounded rate of more than 70 percent from 2008 to 2010. Overseas investing is expected to remain strong in 2011, as more wealthy Chinese pursue international investment opportunities and investment immigration. That is a form of temporary or permanent residency that some countries give to foreign citizens when they create jobs and invest a high sum of money in a less developed region.

China's investment immigrant population is quickly increasing. In the US, the number of Chinese investment immigrants grew at a compounded annual rate of 73 percent over the past five years. Because of the number of investment immigrants, some countries have raised the investment threshold for applicants. For example, in 2010, Canada increased its threshold for minimum net assets from CAD 800,000 to CAD 1.6 million. Australia also raised the personal asset requirement from AUD 250,000 to AUD 500,000 in 2010.

Our survey verified the investment immigration trend. Almost 60 percent of Chinese HNWIs surveyed have either completed investment immigration, applied for investment immigration or are considering it (see Figure 14). Large business owners with more than RMB 100 million in investable assets have a strong interest. Of that group about 27 percent have completed investment immigration, while almost half—47 percent—are considering submitting an application.

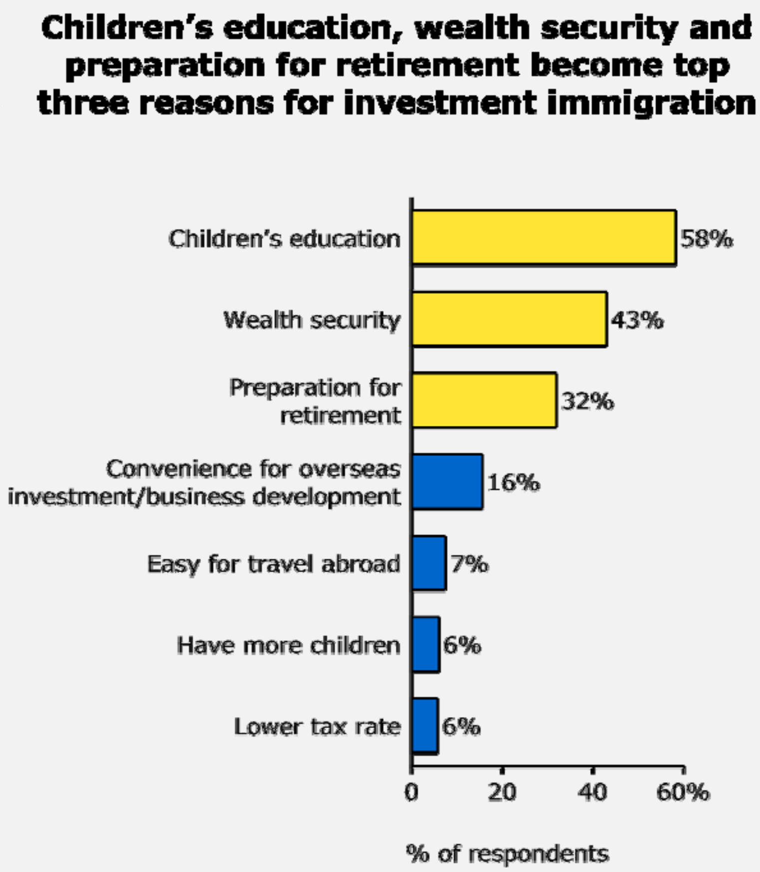
Figure 14: Chinese HNWIs' attitude toward investment immigration



Source: CMB-Bain Chinese HNWIs' survey

Providing for their children's education is the primary reason that China's wealthy will decide to move. Most of the HNWIs we interviewed already have sent their children abroad to study or plan to do so. In fact, the number of overseas Chinese students has been steadily growing at a rate of more than 20 percent, totaling almost 230,000 in 2009. HNWIs also cite wealth security and preparing for retirement as other factors motivating investment immigration (see Figure 15).

Figure 15: Chinese HNWIs' reasons for investment immigration



Source: CMB-Bain Chinese HNWIs' survey

Chinese HNWIs who decide on investment immigration discover they need professional guidance in managing their overseas assets. As their overseas wealth grows, it becomes an important concern. As a portion of their total wealth, HNWIs' overseas assets have increased from 16 percent in 2009 to 19 percent in 2010. The rapid growth creates special asset management requirements. Our survey found that about 45 percent of the Chinese HNWIs who obtained investment immigrant status had difficulty understanding the complex tax requirements for individuals with dual citizenship. Almost 40 percent want help identifying overseas investment products and opportunities, as well as deciding on how best to balance domestic and foreign investments.

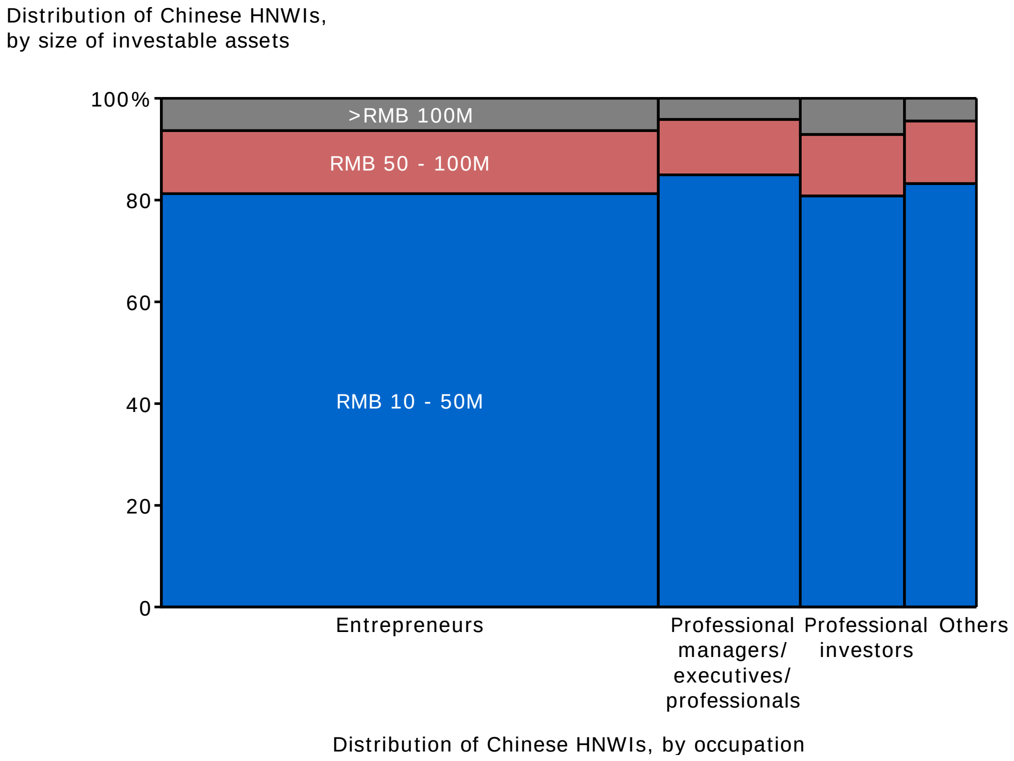
China's HNWI segments demonstrate diversifying risk preferences, wealth objectives and asset allocation behaviors

After two years of accelerated growth, China's HNWI population now tops 500,000. Once again, our report found that their occupations and the value of individual assets have the strongest influence on HNWI behavior. Using this approach, we segmented the HNWI population. China's wealthy population falls into six groups:

- Business owners in the lowest asset band, with assets under RMB 50 million;
- Business owners in the middle asset band, with assets between RMB 50 and 100 million;
- Business owners with assets in the highest asset band, with assets greater than RMB 100 million;
- Professional managers (including corporate executives and professionals);
- Professional investors;
- Others (primarily housewives, retirees, entertainment personalities and sports stars).

Just as in 2009, business owners still make up the overwhelming majority of China's HNWI population, but their numbers have declined from 70 percent to 61 percent. Meanwhile, professional managers, including corporate executives and professionals, are a quickly expanding segment, increasing to 17 percent from 11 percent in 2009. They now are the second largest segment, overtaking professional investors. The specialized investor population is stable, growing at about the same rate—13 percent—as the HNWI population. The smallest segment includes housewives, retirees, entertainment personalities and sports stars. Their share has grown slightly but remains below 10 percent. The majority of Chinese HNWIs have investable assets of RMB 50 million or less. Ultra-wealthy individuals, usually business owners, with more than RMB 100 million in assets still are rare, but they have grown from 3 percent of the HNWI population in 2009 to 6 percent in just one year (see Figure 16).

Figure 16: Chinese HNWIs' segmentation by occupation and size of investable assets



Source: CMB-Bain Chinese HNWIs' survey

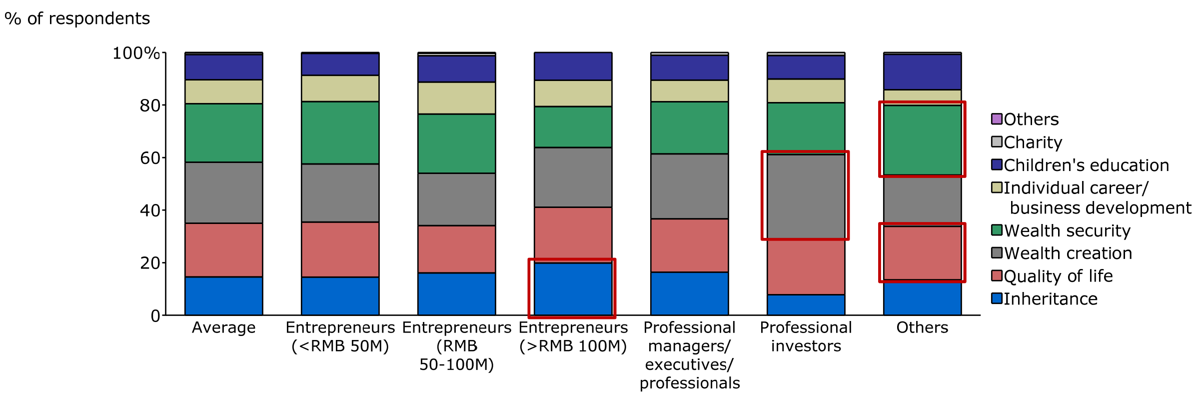
China's first generation of wealthy individuals makes up the vast majority of HNWIs, but a second generation is emerging. They account for less than 1 percent of the total HNWI population and their average asset size is relatively small, limiting their investment decision-making power. Even so, this second generation of wealthy Chinese is an emerging force. They are advocating for public initiatives such as environmental protection, charity work and energy conservation.

HNWIs share certain characteristics. An analysis reveals that they are predominantly male and between 40 and 50 years old. As they age and their businesses grow, they accumulate more wealth. The number of business owners in the mid-asset band who are under 40 has increased since 2009, reflecting how quickly young Chinese entrepreneurs are becoming rich, especially in finance and real estate.

Over the past two years, business owners have advanced their education by earning EMBAs through senior manager training programs and other opportunities. Almost 80 percent now hold bachelor degrees. Professional managers tend to be young—one-third are under 40 years old, well educated, with a two-to-one male to female ratio. They hold more master's degrees than any other segment. Professional investors also are younger and, increasingly, under the age of 40. The last category is dominated by housewives who are between 30 and 49 years old.

The six HNWI segments have different wealth objectives. Aging, wealthy business owners are more focused on inheritance planning, especially those who own large enterprises. The goal of professional investors is creating more wealth. Professional managers and professional investors have more balanced objectives. Retirees and housewives are less interested in wealth creation. They are focused on improving the quality of their lives and ensuring the safety of their wealth (see Figure 17).

Figure 17: Wealth objectives across segments

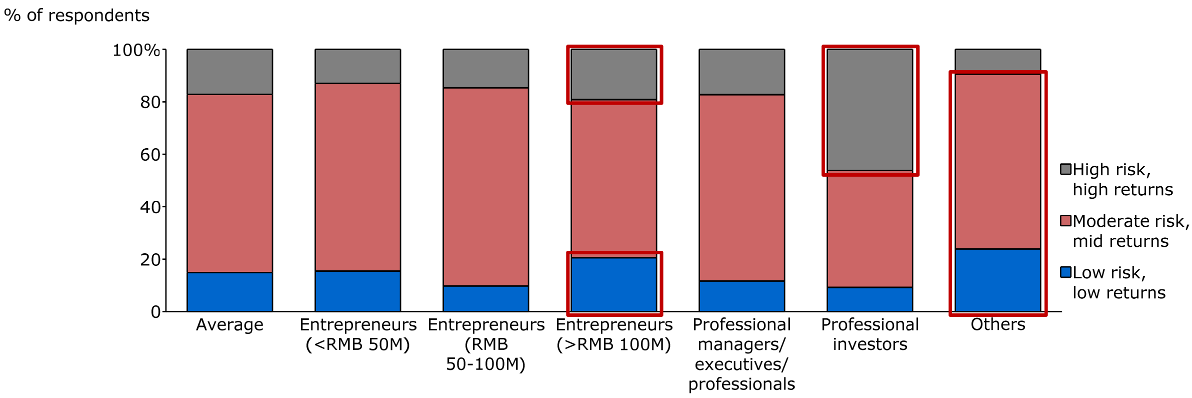


Source: CMB-Bain Chinese HNWIs' survey

Risk preference is also different for each HNWI category. Small and midsize business owners are moderate risk takers. However, risk preferences among large business owners, with more than RMB 100 million in assets, have polarized. One group wants investments with high risk and high returns, while another group has a lower risk tolerance. These are large business owners who have shifted from wealth creation to preserving wealth accumulated by years of hard work.

Professional investors who are accustomed to market volatility have a higher risk tolerance. They have confidence in their ability to target market opportunities, making them comfortable with investing in high-risk equity products. Professional managers are focused on their careers and usually opt for a diversified portfolio with moderate returns and risks. Housewives and retirees are conservative investors who are primarily concerned about preserving their wealth (see Figure 18).

Figure 18: Risk preference across segments

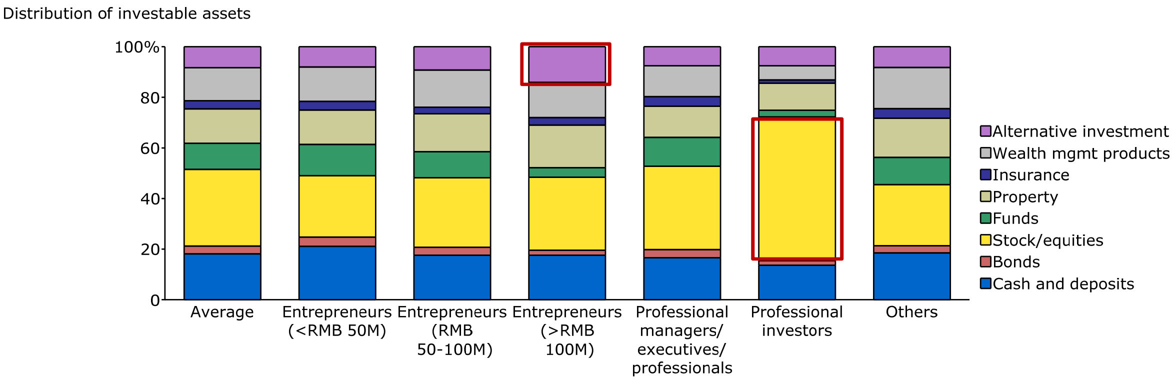


Source: CMB-Bain Chinese HNWIs' survey

As HNWIs develop more risk tolerance and diversify their wealth objectives, it impacts the way they allocate their assets. Since risk preferences and wealth objectives differ within each segment, asset allocation also varies. Business owners tend to invest in high-risk instruments like stocks and alternative investments. There are two reasons. Mid-size and large business owners' capacity for risk increases as their assets grow, making high-risk and high-return products more attractive. Also, business owners often are more confident and have extensive networks that connect them with promising investment opportunities and special investment channels, such as private equity.

Professional investors seek high-risk and high-return investments, putting more than 50 percent of their assets in stocks. Professional managers typically have well-balanced, diversified asset allocation, consistent with their moderate risk tolerance. Stocks make up a slighter higher share of their portfolios, reflecting an optimistic market outlook. Housewives and retirees' portfolios prefer bank wealth management products that offer liquidity and wealth security (see Figure 19).

Figure 19: Asset allocation across segments



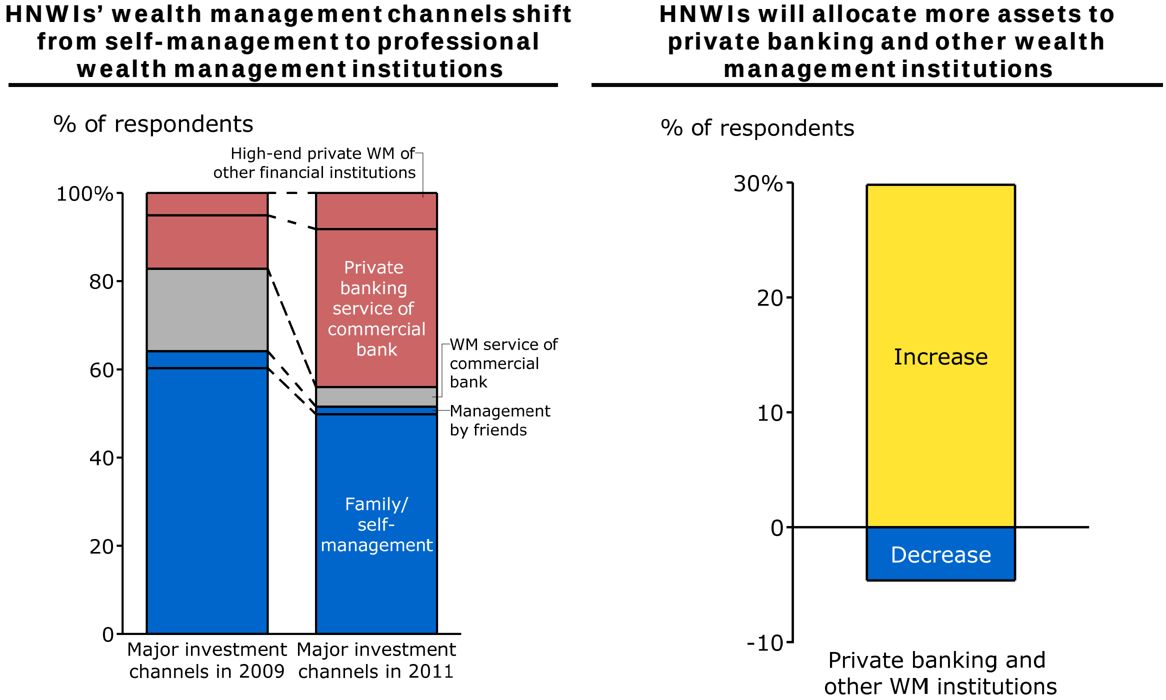
Note: "Alternative investment" includes trust, private fund invested in secondary market, gold and futures held by individuals
Source: CMB-Bain Chinese HNWIs' survey

Chinese HNWIs' wealth management channels are shifting to professional institutions. Brand has become a major selection criterion, followed by expertise and relationship manager services.

When they launched private banking services for wealthy individuals in China in 2007, few HNWIs were familiar with the concept. But the industry's four-year development plan is paying off. Professional wealth management institutions are playing an increasingly important role in managing HNWIs' wealth. Over the past two years, our survey shows that more Chinese HNWIs are shifting from managing their own wealth and are turning to professional wealth management services. Almost 45 percent of wealthy Chinese are entrusting private banks and other wealth management institutions with the majority of their investable assets—almost a 30 percent increase since 2009.

Commercial banks and other financial institutions have successfully raised awareness of their private banking services and high-end wealth management businesses. They are attracting HNWI customers with rich offerings and improved expertise. As wealthy Chinese diversify their wealth objectives and become more risk tolerant, asset allocation is more complex, making it difficult for them to manage their own portfolios effectively. As a result, most HNWIs are relying more on professional wealth management institutions and we expect the trend to continue. In our survey, more than 30 percent of the HNWIs indicated that they plan to move more assets to private banks and other wealth management institutions, making them their major investment channel (see Figure 20).

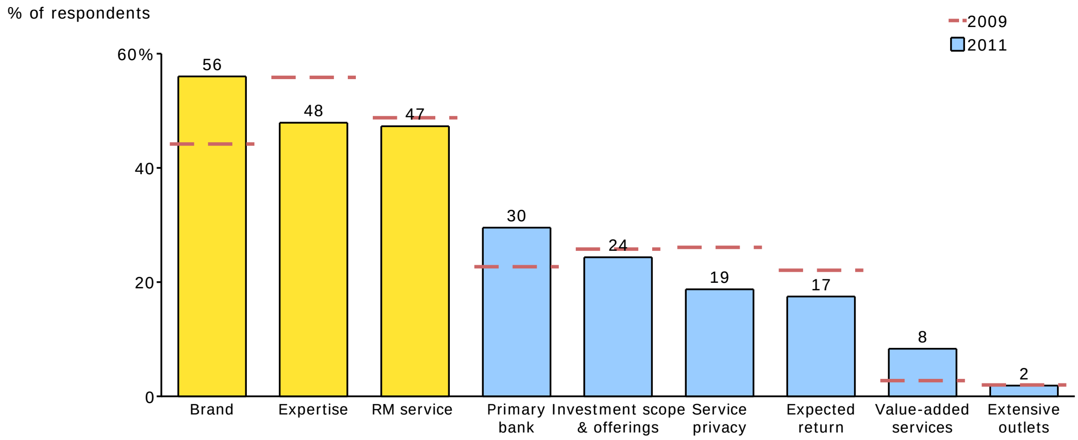
Figure 20: Chinese HNWIs' wealth management channels



Source: CMB-Bain Chinese HNWIs' survey

China's HNWIs are quickly becoming savvy shoppers of wealth management products and services. When selecting wealth management institutions, they continue to use three major criteria: brand, expertise and relationship management services (see Figure 21). Brand is now the major factor, with 56 percent of survey respondents rating brand as the main reason they select wealth management institutions, a 10 percent increase from 2009. The change reflects a growing dependence by wealthy Chinese on their intuitive impressions of a brand as well as years of branding campaigns by wealth management institutions. HNWIs look for wealth management institutions that provide asset allocation services tailored to their needs as well as investment guidance. High-level relationship management services remain another important criterion since it directly impacts a customer's experience. HNWIs expect professional, thoughtful and comprehensive services from reliable relationship managers.

Figure 21: Major criteria for selecting a private bank and wealth management institutions

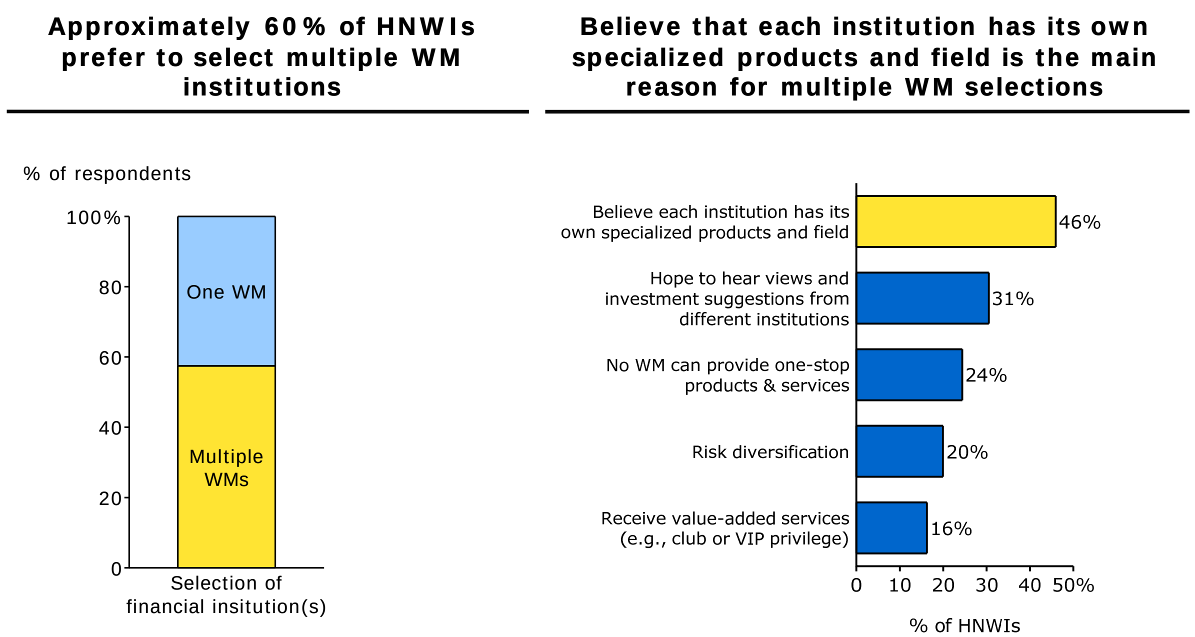


Source: CMB-Bain Chinese HNWIs' survey

Chinese HNWIs are using multiple wealth management institutions; the trend is shifting to one primary provider

Our survey reveals that more than 60 percent of Chinese HNWIs prefer to use multiple financial institutions, with nearly half believing that each institution offers specialized products and services. By using several institutions, some customers say they benefit from different points of view and investment advice, helping them develop an in-depth market analysis. Since China's private wealth market still is evolving, it is difficult for institutions to provide comprehensive one-stop shopping for products and services, given their limited resources and experience as well as regulatory restrictions. Currently, no single institution can meet HNWIs' increasingly complex needs with their diversified wealth objectives and asset allocation requirements. Meanwhile, some customers find that using multiple institutions spreads the risk and gives them access to more value-added services (see Figure 22).

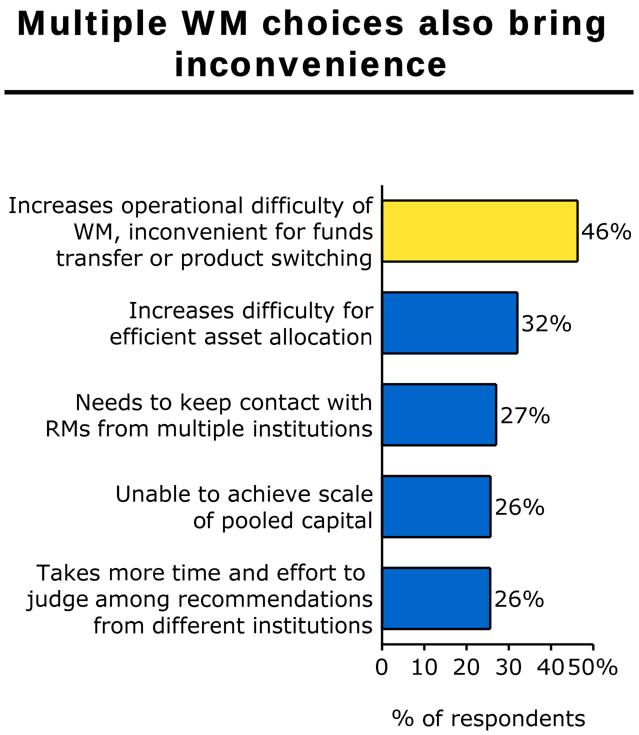
Figure 22: How Chinese HNWIs select wealth management institutions



Source: CMB-Bain Chinese HNWIs' survey

Although most Chinese HNWIs use several institutions for wealth management, it also creates inconvenience. Nearly half of the HNWI customers surveyed found that using multiple institutions increased the difficulty of managing their wealth: 46 percent said the approach made it harder to transfer funds and switch products. For busy executives, it requires too much time to coordinate wealth management needs with various institutions. And 32 percent said that fragmented asset management made it more challenging to develop a comprehensive asset allocation strategy. Another major downside: it reduces the benefits from private banking relationship management. Customers are unable to take advantage of pooled capital and have trouble evaluating investment advice (see Figure 23).

Figure 23: The inconvenience of using multiple institutions for wealth management

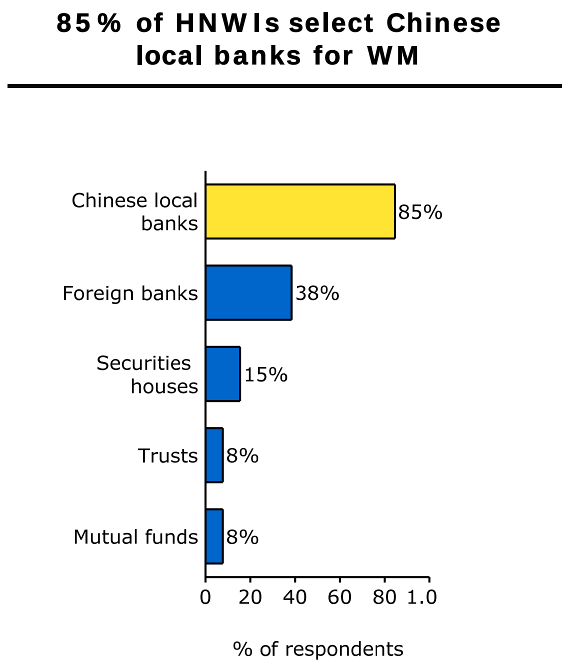


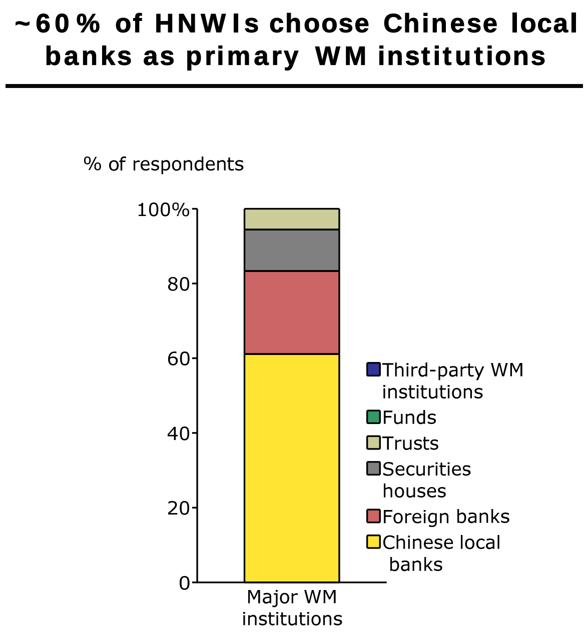
Source: CMB-Bain Chinese HNWIs' survey

As the wealth management market develops and offerings are refined, we expect most HNWIs to adopt a new model: one primary provider, with other institutions providing backup support. Using one main institution has several advantages. It will reduce asset management difficulties; improve communication with relationship managers; enable customized asset allocation and investment guidance; and provide the advantages of scale, resulting in improved products, preferential rates and more comprehensive asset allocation. Even so, we expect wealthy customers to supplement their wealth management periodically by using other institutions, especially when they launch attractive products.

Our survey reveals another key trend: domestic banks now dominate China's private wealth market. Eighty-five percent of HNWIs who use financial institutions for wealth management select domestic banks and among them, 60 percent are using local Chinese banks as their primary wealth management institutions. As domestic banks gain market share, foreign institutions are not growing as rapidly due to both regulatory restrictions and the impact of the financial crisis on their brands and customers' trust. Only about 20 percent of HNWIs surveyed said they would select a foreign private bank. At the same time, professional financial institutions such as securities houses, funds and trusts have rapidly expanded their customer base over the past two years (see Figure 24).

Figure 24: Chinese HNWIs' selection of private banks and high-end wealth management institutions

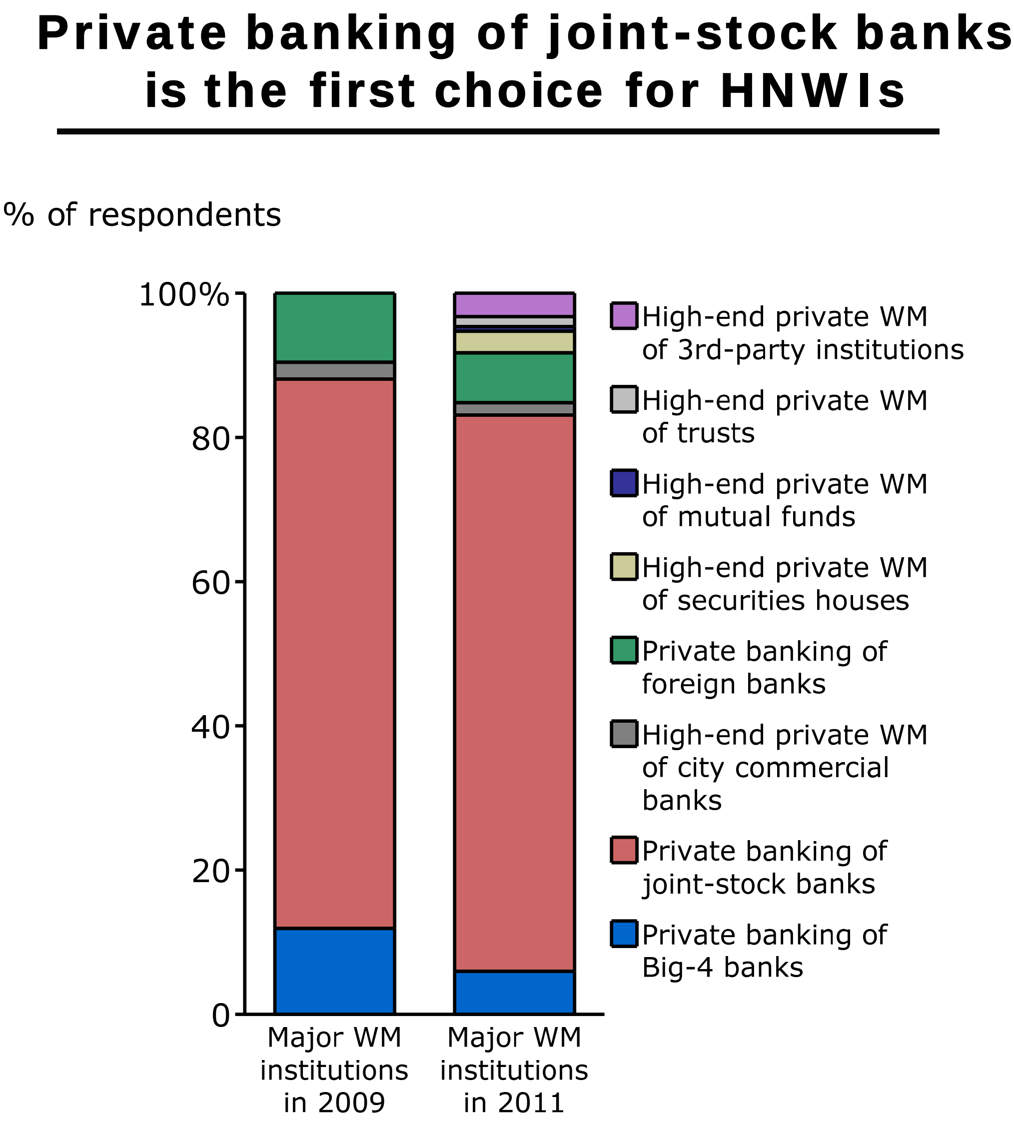




Source: CMB-Bain Chinese HNWIs' survey

In the future, 80 percent of HNWIs still plan to use private banking services provided by joint-stock commercial banks. We expect more wealthy Chinese customers will select securities houses and third-party wealth management institutions for their wealth management business, accounting for 10 percent of the market (see Figure 25).

Figure 25: Chinese HNWIs' private bank and wealth management institution selection trends



Source: CMB-Bain Chinese HNWIs' survey

Chapter III: Competitive landscape for China's private banking sector

- **Various wealth management institutions are entering and competing in China's private banking sector.**

- **Compared with the market's early days in 2009, competition in China's private banking industry is fierce, with the industry entering a new stage.**

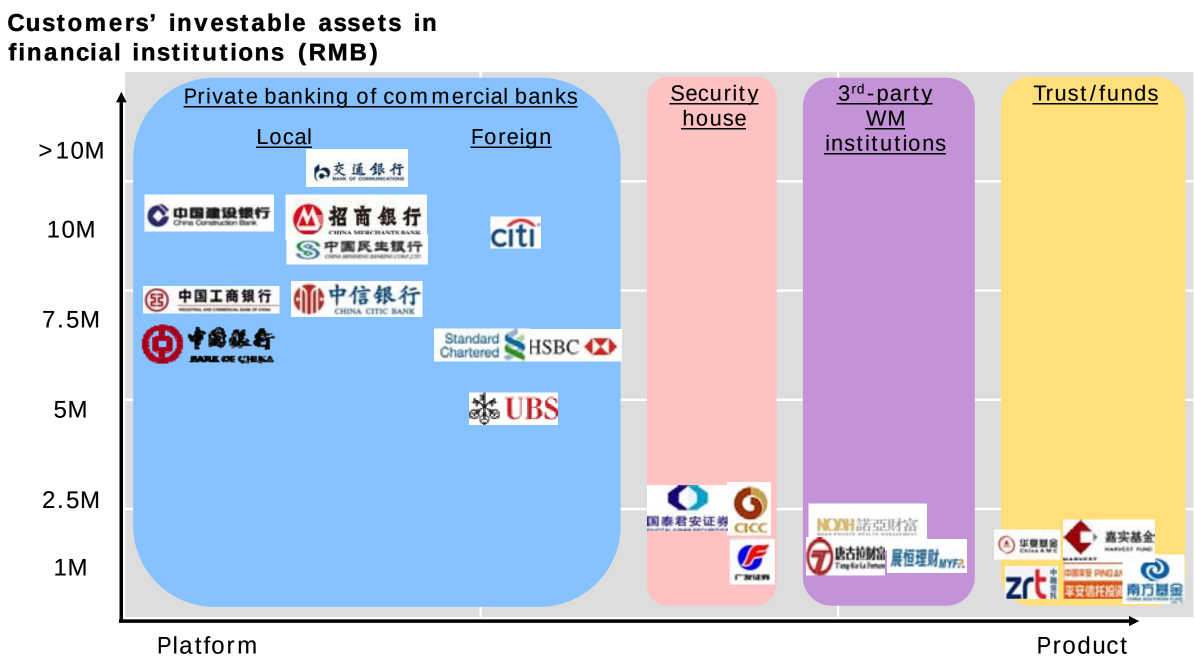
- **Chinese domestic private banks now are the first choice of wealth management customers seeking a diversified portfolio; they have an extensive customer base, wide variety of wealth management products and investment expertise.**

Various wealth management institutions are entering and competing in China's private banking sector

As the ranks of China's HNWIs surge and their needs diversify, wealthy Chinese are increasingly shifting from self-management to relying on professional wealth management. The potential for China's private banking sector is enormous. Financial institutions are entering the market at a rapid pace, creating fierce competition.

The wealth management sector now includes private banks, (domestic and foreign) commercial banks, brokers, third-party wealth management institutions, trusts and funds. The wealth management institutions are classified below based on a threshold of dedicated wealth management services for high-end customers (see Figure 26).

Figure 26: Segmentation of wealth management institutions for HNWIs



Note: Fund management companies also provide discretionary fund management services for individual account larger than RMB 50 million
Sources: Company websites; company annual reports; Bain analysis

The average entry threshold for commercial banks offering private banking is RMB 10 million, or US$1 million. The threshold is lower for product providers, including brokers, third-party wealth management institutions, trusts and funds. The rationale is that they have smaller customer bases and use product sales to acquire customers. By offering dedicated services to a customer willing to invest RMB 2 million to 3 million to purchase their products, the institution raises customer awareness of its brand and services, encouraging them to deposit more funds in their accounts. The four kinds of institutions also focus on different customer segments. For example, brokers' customers have investable assets of more than RMB 10 million as well as ultra-wealthy customers; funds offer one-to-one dedicated services for customers with RMB 50 million in assets, differentiating their services and increasing the loyalty of ultra-HNWIs.

Compared with the market's early days in 2009, competition in China's private banking sector is fierce, with the industry entering a new stage

The competitive landscape for China's private banks is rapidly changing. After two years of intensifying competition, players in China's private banking sector have a better understanding of the market, helping them develop customized Chinese business models. Institutions offer services that vary in scope and quality, creating both advantages and disadvantages that impact their market position, development trends and strategic objectives. As competition heats up among wealth management institutions across all dimensions, the private banking sector is entering a new stage. Overall, commercial banks' private banking businesses dominate the sector.

China's domestic private banks take advantage of their extensive customer base to offer a wide variety of products, but they have limited global and customization capabilities.

Domestic private banks are using their commercial businesses as a wealth management platform, with a nationwide network of customers providing an extensive customer base. It gives China's private banks a competitive edge in building brand awareness and customer trust. In addition to selling their own wealth management products, domestic private banks can sell products from their family of financial institutions, serving as a production platform. Their disadvantages: compared with foreign private banks, they have limited expertise in managing overseas assets and providing customized products and services for ultra-wealthy customers.

As a result, China's domestic private banks are most attractive to HNWIs with wealth objectives that include diversifying assets, safeguarding wealth, creating wealth and preserving capital. Domestic private banks offer these HNWI customers a convenient one-stop service. They can purchase a portfolio offering different products for desired liquidity, risk/return allocation and value-added services to enhance careers and quality of life.

Foreign private banks gain an advantage with global networks offering asset allocation services worldwide; however, there are more restrictions on their RMB transactions.

Foreign private banks' main advantage is their ability to offer global asset allocation services to HNWIs through their worldwide networks. They also have established reputations in private banking. When HNWIs invest overseas, foreign private banks are their first choice. They have strong brand recognition around the globe, with a long corporate track record and expertise in overseas markets, especially when compared with the overseas branches of China's domestic commercial banks. Foreign private banks also are better equipped to customize services for the ultra-wealthy.

Of course, foreign private banks have disadvantages. Government regulations limit development, including multiple restrictions on foreign bank's RMB transactions, curtailing product offerings. In addition, hard-selling relationship managers can leave a negative impression with customers. It's harder for foreign private banks to attract new customers because they lack a nationwide branch network, resulting in a more limited customer base. And the financial crisis impacted the reputation of global brands in contrast to Chinese banks, which remained financially sound.

Foreign private banks are most attractive to HNWIs focused on overseas and global asset allocation. Wealthy Chinese find transactions are easier with foreign banks' worldwide branch network and array of global services, including asset allocation and management, cross-border transactions and help with tax and legal issues.

China's domestic private banks now are the first choice of wealth management customers seeking a diversified portfolio; they have an extensive customer base, a wide variety of wealth management products and investment expertise

Chinese private banks benefit from commercial banks' extensive customer base. The parent companies of most Chinese commercial banks have been active in the Chinese market for decades, developing branch networks and a large customer following in most first- and second-tier cities. These advantages have made it relatively easy for Chinese commercial banks to establish their own private banking centers, acquiring major customers through their retail banking operations. Over the past few years, Chinese private banks have invested heavily in brand building, setting up private banking centers, launching aggressive advertising campaigns and organizing upscale events and activities. The strategy has succeeded in raising HNWIs' brand awareness. Domestic private banks also have benefited from favorable government policies. They have fewer limitations on product offerings compared with foreign banks and other institutions. In addition, by selling products from related financial businesses, domestic private banks can offer products with more variable terms, from one day to 10 years or longer. Our interviews with Chinese HNWIs show that they believe relationship managers from domestic private banks provide more objective and thorough investment recommendations, improving their trust and loyalty. About 85 percent of HNWIs currently using wealth management services selected domestic private banks for wealth management. About 60 percent of those surveyed said local Chinese private banks are their primary wealth management provider. The results show that domestic private banks remain the top choice for most HNWIs.

Customers pursuing diversified wealth management are turning to domestic private banks because of the benefits. They have developed convenient one-stop product and service platforms. Domestic private banks draw on their commercial banking relationship to acquire HNWI customers. And, by combining wealth management services with general services offered by commercial banks, they can offer more convenient and diversified services to HNWIs, better meeting their needs. In the short run, China's domestic private banks will retain their market leadership and strong competitive advantage over other wealth management institutions.

Chapter IV: Implications for China's private banking sector

- **China's HNWI population and total wealth are rapidly increasing, creating enormous potential and a promising future for China's private banking sector.**

- **Wealthy Chinese are more sophisticated wealth management investors, with increasingly diversified needs. The fierce competition in the private banking sector is reshaping the industry as it enters the next phase.**

- **China's domestic private banks have seized the opportunity created by the global financial crisis, becoming the preferred choice for HNWIs customers pursuing diversified wealth management objectives.**

- **Overseas asset management is increasingly important; in the short term, foreign banks will continue their domination of overseas wealth management.**

- **Domestic private banks will increase their competitive advantages by identifying target customer segments, aggressively building brand recognition, improving relationship management expertise, better understanding HNWIs' needs and providing customized products and services.**

China's HNWI population and total wealth are rapidly increasing, creating enormous potential and a promising future for China's private banking sector

After prices fell in 2008, China's investment markets rebounded, achieving rapid growth as a result of a RMB 4 trillion stimulus package in 2009–10. The two most important markets experienced the fastest growth—stocks and real estate. Stock market capitalization soared, reaching a 120 percent growth rate. The market value of capital market products and net value of investment property also grew quickly, at a compounded annual rate of 55 percent and 40 percent, respectively, in 2008–2010. In investment markets, accelerated gains fueled the rapid growth for individual investable assets.

With China's economy recovering, individual investable assets totaled RMB 62 trillion in 2010, up 19 percent over 2009, increasing at a slower rate than in 2009. We expect China's individual investable assets will reach RMB 72 trillion in 2010. In addition, the number of Chinese HNWIs continues to multiply. In 2010, there were 500,000 HNWIs in China, including more than 20,000 ultra-HNWIs with investable assets of RMB 100 million and 70,000 HNWIs with investable assets of more than RMB 50 million.

The booming private banking sector reflects a major shift in the way HNWIs manage their wealth. Instead of self-management, China's wealthy are increasingly using professional institutions. They are much more aware of the specialized services offered by private banks, especially domestic private banks. That shift creates enormous opportunities for the private banking sector's expansion and a promising future.

Wealthy Chinese are more sophisticated wealth management investors, with increasingly diversified needs. The fierce competition in the private banking sector is reshaping the industry as it enters the next phase

Our survey found that Chinese HNWIs' wealth management needs are changing as they diversify their wealth management objectives and look for value-added services. While they still are focused on wealth creation and enhancing their quality of life, HNWIs are placing more importance on other objectives, including wealth security, inheritance and their children's education. As they diversify asset allocation, wealthy investors require a more diverse array of bank wealth management products and alternative investment vehicles, including private equity, trust, private fund invested in secondary market and other popular emerging investment options. Demand for value-added services also is on the rise. Wealthy individuals are turning to wealth management institutions for assistance with their healthcare needs, their children's education and social opportunities that advance their careers and improve quality of life.

HNWIs now are more realistic about risks and returns from investments, with a preference for moderate risks and returns. Their needs also have changed, shifting from simple product referrals to integrated management services across multiple dimensions.

After two years of competition, the players in China's private banking sector have a better understand of wealthy Chinese customers' needs, allowing them to design business models tailored to the Chinese marketplace. Competition is intensifying as more financial institutions rush to capture market share. Commercial banks are rolling out their own private banking services. Another group of financial institutions also has developed dedicated wealth management services for high-end customers. They include security houses, third-party wealth management institutions, trusts and funds. The competition is intense across all dimensions of the marketplace.

All of these changes are reshaping China's private banking industry. Wealth management institutions are drawing on their competitive advantages to win over wealthy investors with more diversified products and flexible services. With increasing demand from customers and suppliers, the HNWI segment of China's private banking sector is surging as the market enters a new phase.

China's domestic private banks have seized the opportunity created by the global financial crisis, becoming the preferred choice of HNWI customers pursuing diversified wealth management objectives

In our *2009 China Private Wealth Report*, we concluded that "Foreign private banks are unable to press their advantages in the short term; Chinese private banks should actively capture and consolidate market share during the two-year window of opportunity." During recent years, Chinese private banks have invested enormous capital and resources in brand building, setting up private banking centers, investing in advertising and organizing upscale events and activities. As a result, HNWIs have increased brand awareness of domestic private banks. Our survey finds that most HNWIs already using wealth management institutions have selected domestic private banks. Over half list Chinese private banks as their primary wealth management provider. We expect this trend will continue, with domestic private banks increasing their share of the HNWI market. By seizing the opportunity created by global economic turbulence, China's private banks have established their leadership in the domestic HNWI wealth management market.

In contrast, foreign private banks are growing at a slower pace due to several restrictions. Regulatory rules limit RMB transactions. They also lack domestic market experience and vehicles like nationwide branch networks to attract wealthy customers. Security houses appeal to high-end customers who want high capital liquidity, since their investment decisions are tied to the stock market's performance. Third-party wealth management institutions still are developing a customer base. They face regulatory uncertainty, making it harder to build their brand and customer trust. Funds and trusts have fewer channels to attract customers. With regulations restricting product offerings, they are positioned in the short term as product suppliers for banks and other wealth management institutions.

In the immediate future, China's domestic private banks will have strong and sustainable competitive advantages over other wealth management institutions. They will continue leading the HNWI wealth management market as the preferred choice of most HNWIs.

Overseas asset management is increasingly important; in the short term, foreign banks will continue their domination of overseas wealth management

Based on our findings, we expect HNWIs' overseas assets to continue surging, reflecting their continued investment diversification. As a percentage of their total assets, overseas assets have increased to about 20 percent from less than 10 percent just two years ago. They include HNWIs' overseas income, overseas equity cash-outs and pledged or liquidated capital still overseas. As more HNWIs pursue investment immigration, the need for overseas asset management services becomes more pressing.

Although wealthy individuals' overseas assets still account for a smaller percentage of the total compared with domestic assets, demand for overseas wealth management is rapidly growing as more HNWIs boost their foreign investments. They are searching for more overseas investment products, investment immigration-related value-added services such as assistance with complicated tax and immigration requirements, cross-border capital allocation and management services.

Foreign banks remain the leading wealth management providers for HNWIs' overseas asset allocation. For now, they have a strong competitive edge over China's domestic wealth management institutions, with a worldwide network of branches, extensive experience in the overseas market, tailor-made services for the ultra-wealthy and proven expertise with global asset allocation services.

We expect Chinese wealth management institutions, especially commercial banks with branches in major global markets, to devote increasing attention to cultivating their overseas asset management business. They should commit the resources required to establish competitive services. China's private banks should begin with the Hong Kong market, which has the largest number of wealthy mainland immigrants, using it to improve their expertise in overseas wealth management. They can use this experience to build a global brand, expand their channels and enhance resources for overseas wealth management.

Domestic private banks will increase their competitive advantages by identifying target customer segments, aggressively building brand recognition, improving relationship management expertise, better understanding HNWIs' needs and providing customized products and services

According to our survey, the top three criteria used by HNWIs to select private banks are brand, expertise and relationship management services. To gain more of a competitive advantage, domestic private banks must aggressively work to build a trusted brand image. They must increase their credibility as trusted wealth management advisers who make objective asset allocation recommendations based on customer needs. To improve the customer experience further, they should offer more targeted HNWI products and value-added services, with enhanced relationship management services and expertise. Domestic private banks also should develop detailed breakouts of HNWI segments to identify high-value customers better. The resulting insights will allow them to build their brand, expertise and wealth management products and services more effectively.

Specific initiatives for China's private banks include investing heavily in brand building, beefing up resources and dedicated wealth management personnel and differentiating themselves with customized products and services for select HNWI customer segments. To boost customer loyalty, Chinese private banks need to polish their reputations as objective investment managers, offering valued products and services for their wealthy clients. They also should establish an experienced technical team to assist customers, reinforcing the bank's expertise with HNWI clients. For improved relationship management services, domestic private banks need to recruit more experienced relationship managers. To attract and retain them, banks have to enhance training, assessments and compensation systems.

Chinese HNWIs continue to use multiple wealth management institutions because they believe there are advantages in working with various investment advisers. But that approach also creates major inconveniences for customers. Increasingly, wealthy Chinese favor a new wealth management model with one primary provider offering integrated services, supported by institutions that serve as backups. The long-term goal for China's private banks is to establish themselves firmly as the leaders in wealth management institutions for HNWIs. To accomplish this in a crowded field of aggressive competitors, domestic private banks must strengthen their financial position by raising the capital in current customers' accounts while acquiring new HNWI clients. Only by building long-term relationships with China's wealthy and improving their loyalty will the nation's private banks capture a larger share of China's rapidly growing wealth management market.

Appendix: Research methodology

The *2011 China Private Wealth Report* primarily focuses on the domestic HNWI market and includes analysis on the number of HNWIs, the size and segmentation of the HNWI group, HNWIs' different investment behaviors, the competitive landscape and implications for China's private banking industry.

We used Bain & Company's HNWI Income-Wealth Distribution Model, as we did for the *2009 China Wealth Report,* to estimate the overall HNWI market in China, as well as the distribution of HNWIs and their investable assets by province. Using the same methodology advanced our study and in-depth research into the major market trends over the past two years. The Distribution Model serves as the cornerstone for both the *2009* and *2011 China Private Wealth Reports,* providing a top-down methodology to estimate the number of HNWIs and the market value of their investable assets. That allows us to avoid the possible under-sampling errors that occur when employing a bottom-up methodology. It ensures that our results are more reliable, comprehensive and predictable.

The model first estimates the overall value of investable assets held by residents, by province. Individual investable assets include cash and deposits, tradable stocks, untradable stocks of listed companies, mutual funds, bonds, investment property, insurance, bank financial products, overseas investments and alternative investments. Investable assets exclude the following items: owner-occupied property, non-listed company held by non-private equity and durable consumer goods. By using the same methodology as in 2009, we were able to perform a detailed analysis and estimate of overseas investments and alternative investments. Overseas investments include individually held overseas deposits, overseas stocks, overseas investment property and QDII. Alternative investments include trust, private equity, private fund invested in secondary market, gold and futures. Data sources include the People's Bank of China, National Bureau of Statistics, National Development and Reform Commission, China Insurance Regulatory Commission, China Banking Regulatory Commission, Shanghai Stock Exchange and the Shenzhen Stock Exchange.

The major output from this model is the calculation of the HNWI Wealth and Income Lorenz Curve, using a statistical methodology. Based on the latest income distribution, inheritance tax and family-owned asset data from the United Nations, tax authorities and central banks of different countries, we calculated the HNWI Lorenz Curves for more than 10 developed and developing countries in Asia, Europe and the United States. We discovered a high correlation between the curve and a country's Gini coefficient, GDP, population and other macroeconomic indexes. By applying this mathematical correlation to China and individual provinces, and by comparing the United Kingdom, United States, Japan and South Korea's recent HNWI Lorenz Curves with CMB clients' asset distribution data, we derived the overall domestic HNWI Lorenz Curve and respective curves by province.

Finally, we used the HNWI Lorenz Curve to allocate the investable assets owned by HNWIs by province and calculated the number of HNWIs by asset level—both at the national and provincial levels—and then calculated the value of investable assets owned by each.

To collect data for the *2011 China Private Wealth Report*, we conducted a thorough survey of 37 major cities in 28 provinces, with more than 2,600 research samples and more than 100 face-to-face interviews. In order to achieve the best representation, we surveyed all of the major economic regions: the Yangtze River Delta, Pearl River Delta, North China, Northeast China, Middle China and Western China. Our interviewees included industry experts as well as RMs from private banks and other financial institutions, private banks' HNWIs' clients and other HNWIs. All clients interviewed meet our criteria for HNWIs with at least RMB 10 million in investable assets.

Following the same CMB–Bain HNWIs research analysis methodology used in 2009, we divided HNWIs into six categories for an in-depth analysis. By comparing the data with the 2009 results, we analyzed changes in HNWIs' investment attitudes and behaviors. In addition, we followed important market trends over the last two years.

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