Rethinking wealth management from a production perspective: an ethnomethodological inquiry into increasing perceived added value

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Abstract

The trusted relationship, at the core of wealth management, has been damaged. The financial crisis and the end of the Swiss banking secrecy have left the Swiss private banking sector with a new challenge: how to regain their disillusioned customer's faith. The time has come to reconsider what the client needs in terms of service in order to re-establish long term loyalty between banks and their clients. Using ethnomethodology as our research tool, we have been able to study the tacit knowledge involved in this relationship, as opposed to articulated and codified explicit knowledge. Having interviewed eighty people, half of which are wealth managers, half of which are clients, we were able to study this tacit knowledge leading to loyalty in private banking. A first series of semi-directed interviews has shown that the main salient attributes are more emotional (i.e. trust) than functional (i.e. portfolio performance). In a second series of semi-directed interviews, we focused on the way wealth managers "diagnose" the risk appetite of their clients. In this second phase we notice that the risk appetite diagnosis process is not well understood by clients and thus does not generate sufficient perceived value for them. Consequently, we can question whether the business model of private banks is sustainable.

Submitted to The Oxford School of Hospitality Management; The 6th International Conference on Services Management; Managing services across continents 23-25 June 2013 Cyprus.

Objective

A majority of Swiss private banks have recently announced in the press their wish to externalise their back-office operations in order to cut costs. What they don't realise is that they might also lose some potential perceived value attributes, also key to customer loyalty (Chowney and Fragnière, 2012). In a context where banks are rethinking their ways of functioning, this paper aims to assess how this can be done from a production perspective. As such, the business model of a private bank can be described as follows: on the front office side, a wealth manager adopting an artisanal approach is in charge of establishing the risk profile of their clients whereas on the back office side, a fully industrialised

process handles operations and fund management issues (Dubosson and Fragnière, 2009). Our main research question addresses whether it's enough for a wealth manager to solely focus on the diagnosis of a risk profile for the client as well as reporting tasks. As a subtopic, we explore the possibility for the wealth manager to recuperate some activities of the back office that are today not designed to provide perceived value for the clients (Shostack, 1987).

The Swiss private banking sector needs to be reinvented following the disappearance of Banking Secrecy. As we're currently working with specialists in the field, we aim to provide them with elements of service design which are typically not explored within traditional financial approaches.

This paper is organized as follows. In the next section, a brief literature review presents the main findings of service science related to our topic. Then, the methodology section explains the two ethnographic surveys that were conducted to collect the data that is analyzed in the results section. We finally conclude this paper with a discussion and a set of specific propositions.

Literature review

Service science is an emerging academic field that attempts to better address the particularities of service production. This section presents some important findings that will help the reader to understand the important role that ethnomethodology plays in service science (Fragnière et al. 2012).
The raw material of service production is known to be knowledge. In service science, we make the distinction between explicit and tacit knowledge. Whereas explicit knowledge can be articulated, codified and readily transmitted to others, tacit knowledge, based essentially on know-how and experience, cannot.

In working toward the notion of "service management" that takes a holistic view of the client's overall satisfaction with the delivery of a service and seeks to adjust all organisational functions to the pursuit of this goal, Grönroos (1993) illuminates the need for service science as a way to fully understand the

nature and value of coproduction. In today's growing service economy, it is essential for service providers in both the private and public sectors to understand the important roles that creativity, empathy and implicit knowledge play in service coproduction in order to meet the demand for highly customised, expertise-dependent service experiences (Spohrer et al. 2007). These factors are even more linked to the business basis for strong service design when considering the notion that there is a strong relationship between customer satisfaction and "willingness to pay" (Homburg et al. 2005).

Methodology/Approach

Ethnomethodology is used in order to reveal belief systems and social codes that are typically associated with a wealth management experience. To do so, we held an initial series of semi-directed interviews with wealth managers and clients to understand the key elements of the wealth management service experience and related perceived value attributes (Fandos Roig and Sanchez Garcia, 2006). We then held a second series of semi-directed interviews with the aim of looking at how the wealth manager "produces" their client's risk profile assessment.

Why ethnomethodology:

Because most services rely on human factors such as expertise, implicit knowledge, empathy, and other immeasurable qualities, most quantitative modelling techniques are insufficient for studying and evaluating the current state of a service environment. Ethnomethodology provides a useful tool for studying the contexts, behaviours, and activities that compose a given service environment, and for gathering the information and insights necessary for suggesting iterative improvements (Makino et al. 2009). In his article "Ethnomethodology's program", Harold Garfinkel (2002, p.124) defines ethnomethodology as follows: "Ethnomethodology's fundamental phenomenon and its standing technical preoccupation in its studies is to find, collect, specify, and make instructably observable the local endogenous production and natural accountability of immortal familiar society's most ordinary organisational things in the world, and to provide for them both and simultaneously, as objects, and procedurally, as alternate methods".

Saunders et al. (2007) state: “its purpose is to describe and explain the social world that the research subjects inhabit in the way in which they would describe and explain it. It is a very appropriate strategy in business, if the researcher wishes to gain insights about a particular context and better understand and interpret it from the perspectives of those involved”. This approach is well suited for understanding the underlying constituents of loyalty in a specific area such as private banking.

Semi-structured interviews were used in two distinct phases. The first phase of interviews was held out between 2009 and 2011. The second phase of interviews was held out between 2012 and 2013. The questions are “mirror questions” meaning the same question could be addressed at the same time to a wealth manager and a client, bearing minimal modifications in the way they were posed.

The semi-structured interviews (see for instance Combessie, 1999 and Fenneteau, 2002) were designed to provide respondents with enough freedom to discuss and share their experiences with the analyst, who would then either redirect the interview to explore additional patterns, or conduct further interviews (Gavard-Perret et al., 2008).

The analyst first met the respondents, and asked for a few details such as their age, professional situation (in the case of clients). The first series of interviews, held between 2009 and 2011 (60 in total) were based on the following questions:

“What are the elements that allow you to feel comfortable with your wealth manager?”
This question was designed to identify the key elements that actually allow for the client to feel comfortable with their wealth manager.

“What accounts for you staying with your Wealth manager?”
This questions purpose was to identify, beyond the actual initiation of the relationship, what the wealth manager would have to closely monitor in order to maintain a loyal relationship.

The remaining thirty respondents, all wealth managers, were asked, amongst others, the following question:

"Are you more of a craftsman or a link in the banking chain?"

This question was asked to seek out just how industrialized or not wealth management is. We wanted to observe the flexibility a wealth manager has as to how they will conduct their service in relation to, on one hand their bank, and on the other, their client.

The second series of interviews, held between 2012 and 2013 (26 in total), were based on the following questions:

"How do you approach the issue of investment risk with your customers and how do you estimate it?"

This question was addressed to wealth managers in order to find out in which ways the subject of investment risk was approached. We asked the same question to the clients to get their perspective on when and how this question is treated.

"When diagnosing, defining the risk profile of your clients, what personal freedom do you have in relation to the investment policy of your institution?"

This question relates to the wealth manager functioning more or less in an industrialised way in relation to the investment policy of their bank. The more freedom they have, the more they are considered to be artisans.

"How do you verify your client's knowledge on the subject of risk?"

This questions purpose is to investigate the differences amongst banks in verifying their client's knowledge in terms of risk.

"How do you manage the risk of non-performance in relation to the targets set by the investor (your clients)?"

We wished to find out here who or what the blame was aimed at. A similar question was addressed to the clients:

"If your portfolio is not performing relative to your targets, who would you consider to be most responsible: yourself, your wealth manager, his team, the economy… and why?"

"Do you know the inherent risks linked to your investment structure (portfolio), and can you describe them?"

Finally, we wanted to check if the client is well instructed by their wealth manager about the risks that are related to their financial investment.

After having presented the semi-directed interview questions, we're now going to see in what ways the first series of semi-directed interviews has shown that the main salient attributes are more emotional (i.e. trust) than functional (i.e. portfolio performance) and why the risk appetite diagnosis process is not well understood by clients and thus does not generate sufficient perceived value for them.

Major findings

Our research shows that emotional aspects of service matter more to clients than financial performance aspects. However, we also find that by only doing the risk assessment profile too little problem resolution is taking place, therefore reducing the potential of perceived value.

To simplify the analysis, we have used a selection of questions from the interviews as the main outline of our research, all illustrated with quotes from the respondents. We first present the phase one findings, based on the interviews held out between 2009 and 2011, we then move on to the phase two interviews, held out between 2012 and 2013.

Phase I research findings:

A typical meeting between a wealth manager and his or her client

The survey results show that during the casual conversation that takes place shortly after the wealth manager and the client meet, generally covering topics such as family, health, personal interests and business, it is crucial that the wealth manager evaluate what his or her client's needs are whilst also installing a climate of trust. This assessment must evolve throughout the meetings to meet the client's ever evolving needs.

Senior wealth manager: "the customer profile changes over time. If the client presents a certain profile at age forty-five, this profile will not be the same when he or she retires aged sixty-five. Expectations and appetite for risk will evolve over the years".

The survey results also show, almost unanimously, that for the wealth manager the first meeting with a new client is the most important. It will determine whether the client will entrust his money with them and whether they will bond.

Beyond the performance of the portfolio, what stands out in a significant manner here is the "feeling" a client will get for their wealth manager. This feeling is based on a sense of trust and common understanding.

Important elements allowing for the client to feel at ease

The elements allowing for a client to feel at ease are many. For the client to feel comfortable, the essential component is, again, trust. The survey contains recurrent answers such as the respect of the clients' privacy, always dealing with the same person rather than a replacement colleague, good portfolio performance, accessibility of the manger, professionalism of manager and the advantage of the manager being a friend of the family. These elements all contribute positively to the client feeling at ease, and therefore trusting their wealth manager. The elements that stood out though, through the emphasis put on them by the respondents were: the depth of communication with the wealth manager and their sincerity. The language used by the manager must be understandable, that is to say commensurate to the size of the client's portfolio as well as the ability and will to understand. The client does not generally appreciate an incomprehensible or condescending language, potentially leading to a lack of trust. If the manager makes proposals that are not in line with the expectations of

the client, the trusted relationship will be lost. To feel at ease, the client must feel that the manager is there to provide information that will enable them to make optimal decisions in terms of their financial strategy.

Client, Entrepreneur, 65 years old: When I meet with my wealth manager, he presents me with a report on my current financial situation. He speaks in manner really adapting to my own logic; to my personal way of understanding, because it is important for me to understand the situation. This person knows me very well and is able to reassure me on the preservation of the level of quality of life for my family and myself"

The form of communication depends on the client's profile and his or her expectations.

Wealth manager: "with customers from the entrepreneurial, liberal segments, my objective is to challenge them, they love it. However for some of the private clients segment, we tend to act more as slaves because they need to be pampered".

In conclusion, the most important elements that came from this question are the language of the wealth manager and his or her sincerity. Having established what allows a client to feel at ease, we then looked at what would insure a client's loyalty to their wealth manager.

Components underwriting a client's loyalty to his or her wealth manager in the long term

Three main constituents of loyalty emerged here from our survey: rapport, performance and the bank.

In terms of rapport, time plays the most important role here. Established trust is difficult to replace because it is built over several years. Rapport and trust are the key elements that maintain a longstanding relationship between the client and his or her wealth manager. It's like with a doctor; you no longer need to repeatedly explain things and the client benefits from the fact that the person in front of them knows them well.

Client, 40 years old, entrepreneur: "I have no wish whatsoever to start all over again with someone else and have to tell them all about my life".

Client, 36 years old, marketing director: "There is a real quality of service because of our longstanding relationship. I'm not treated like just another customer".

These clients, benefiting from long-term relationships with their wealth managers, will tend to stay loyal to their banker, rather than their bank.

Client: "I'm bound to my wealth manager. If he changes banks, I'll follow him"

For a relatively smaller portion of respondents, although trust and friendship are established, their main priority is the financial performance of the portfolio. This client profile is willing to change banks or banker immediately if unsatisfied at this level. So this client remains as long as he or she is satisfied with level of portfolio performance.

Client: "I tend to not stay long with any wealth manager, or more precisely with a well-defined investment strategy, therefore I am not dependent on a particular wealth manager and can change when need be".

Client: "Even if I have a good friendship with my wealth manager, if a different bank satisfies me more, I'll leave my wealth manager whilst remaining good friends".

For a minority of interviewees, the bank is primordial and has the greatest influence on the long-lasting relationship. These clients give consideration to the reputation of the bank. Even so, this relationship changes naturally in time in favor of the wealth manager, due to their tacit knowledge being highly valued by the client.

Wealth Manager: "I would say that initially there is an 80%-20% in favor of the bank for these clients, and that as time passes and the relationship develops, the ratio evens-out".

As a general rule, the higher the loyalty between a wealth manager and his or her bank is, the lower the loyalty between this wealth manager and their clientele, and the lower the loyalty between the bank and the wealth manager, the higher the loyalty between the wealth manager and the clients.

Whether the wealth manager considers him or herself more a craftsman or a link in a banking production line

This question allows us to assess the actual capacity of individual wealth managers inside the private banking industry to actually change things. A craftsman would feel relatively more independent than someone considering themselves to be more of a link in a banking "production line", simply executing orders from their hierarchy and following protocol. The answers depended on the financial institution the wealth manager worked for, their years of experience and the amount of money they were dealing with. Generally, the more years of experience a wealth manager gains, the more one becomes independent.

Wealth manager: "It goes without saying that the environment in which everyone works is going to affect their way of handling things. I mean, if one is in a family business, managers tend to behave more like a friend than a manager, the reverse is also true because in the bigger, more "industrial banks", the managers all have a similar mode of conduct which somehow prevents them from fully opening to their customers".

Wealth manager: "We must not forget that we are dealing with people's money, which has a particularly emotional side. Banks offer all more or less the same products; the service will make the difference."

A manager working at Credit Suisse for example will feel more like a link in an industrial chain because of the importance of the infrastructure behind them.

*The first set of interviews brings us to the following conclusion: i*n terms of performance perceived by the client, the wealth managers' service delivery primes over that of financial gain. This means that, in terms of being loyal to one's bank, a majority of clients favour the relationship they have with their wealth manager over the performance of their financial assets. Swiss banks have to compete on the basis of quality of service, but it's not the financial aspect, but the social experience that they need to focus on.

"We must not forget that we are dealing with people's money, which has a particularly emotional side. Banks offer all more or less the same products; the service will make the difference. " (Wealth manager).

Having found through our research that emotional aspects of service matter more to clients than financial performance aspects. We now go on to find out how by only doing the risk assessment profile, too little problem resolution is taking place, therefore reducing the potential of perceived value.

<u>Phase II research findings:</u>

How the issue of investment risk is approached, experienced and estimated

In response to the question "Could you describe briefly and in chronological order a typical meeting with your client? The Wealth manager answered *"of course we try to assess whether we have met the customer's expectations in terms of performance and risk"* and further on, in response to the question "How do you approach the issue of investment risk with your customers and how do you estimate it?" The manager said *"... we try to understand what the expectations are to assess whether the client understands the concept of risk"*. When then asked by the interviewee *"how do you feel?"* This same manager said, *"we have a written form that is filled in with the customer and that is added to the client's file for legal reasons ... "*. We notice that the vocabulary used by the banker suggests an attempt to define the risk profile, an estimate (including a certain error margin); whereas the legal paper added to his file suggests something quite specific. There is a clear dissonance between these two parts of the same risk assessment method.

In response to the question "How do you approach the issue of investment risk with your customers and how do you estimate it?" the wealth manager replied:" *Our basic advice to the client is to never invest in something they cannot control."* Later, in response to the question "How do you manage the risk of non-performance in relation to the targets set by the investor?" The same wealth manager replied: *"It's difficult to answer ... in the case of Madoff, for example, we can't control a speculative bubble, you cannot control it."* Uncertainty is present in the mind of the client. But his perception of

the uncertainty of the risk at the time of the interview will affect his risk profile. The exchange between the client and his banker, this informal exchange, has influence that one can more or less control whilst defining the risk profile. There is a certain margin allowing space for human error.

Wealth Manager: "In terms of risk estimation, the bank provides us with forms to guide us if we have no idea of customer profile ... this can be helpful, but with the experience and knowledge *in behavioral finance, one knows pretty quickly who our customer is and what he expects of us".* From one bank(er) to another, different procedures are applied, more or less rigorously, to complete one same task: produce value for the client through fully understanding his or her needs and making sure they are fully knowledgeable on what their risk assessment means.

We see here that, based on the intricate uncertainty that comes with financial investment, only an attempt to fully assess the client's profile is achieved. This results in too little problem resolution taking place during the risk assessment, the ultimate affect occasioning the reduction of potential perceived value.

Conclusions

Our research shows that emotional aspects of service matter more to clients than financial performance aspects. However, we also find that by only doing the risk assessment profile too little problem resolution is taking place, therefore reducing the potential of perceived value. Consequently, the only way to get wealth management back on track is through the wealth manager who has to regain control over the majority of the service process and activities (e.g. investment allocation, risk management, back office operations) that tend to rely nowadays on hidden labour division. Practically, this would mean a return to artisanship rather than industrialisation over the full wealth management service process.

A crucial point that emerges from our research is that once the clients' trust is considered acquired the banker retreats slightly, not paying as much attention to the client as before a trusted relationship was

established. This is confirmed with remarks relating to the question of a typical meeting between a banker and the client and the importance of the first meeting. This first meeting is crucial in establishing a relationship between the bank and its clientele, the problem being that the initial quality of the service is hard to maintain without "invading" the customer's time and wishes, even though the need for more proximity is still felt. Maybe the key to resolving the problem is finding ways to do this without repeating the first meeting ritual but still conveying this same level of attention in other ways.

Another important point that emerges is the responsibility in the case of non-performance in relation to the targets set by the investor. It appears that if all investors were to take full responsibility, from the very start of the investment process, co-production would be significantly increased and therefore "added perceived value" furthermore. Even if this seems at first to be paradoxical, because the client would play a more proactive role in the management of his portfolio, he would naturally increase his own visibility on what the banking service really does provide to its customers. This is obviously not a solution for everyone. But this stresses the following question: is investing a solution for everyone? Is it normal that everyone should assume that with a certain amount of money it should naturally increase in value? Without any effort on their behalf? It seems to be a given that money simply makes more money.

The problem lies in the fact that banks are not going to acquire clients if they tell them right from the start that if they could guarantee substantial financial increases, they wouldn't necessarily be employed in banks, but doing something else with their systematically and successfully acquired fortunes. On the other hand, clients are not going to understand, let alone accept, the fact that banks can lose part of their wealth. So we reach a natural "compromise" which consists of creating a "fog of confusion" around the service that they are offering to the client. If we turn this fog of confusion into a concrete, dynamic situation where the client must take on a proactive role, then at the very least we will get closer to a more responsible, realistic and sustainable situation.

Having used an ethnomethodological basis in order to develop this proposition, a further validation, using a quantitative survey is deemed necessary. In the case where this proposition turns out to be verified, there would be an urgent need for wealth management to focus their attention on elements of tacit knowledge that convey trust and loyalty. If the quality of the relationship is to be the real differentiator of the future, then financial institutions need to arm their relationship managers with relevant skills, tools and training so that they can fully meet the needs of their clients. This is well illustrated by the following verbatim:

"The social aspect of the relationship is very important, wealth managers can't afford to be financial product selling machines" (Senior wealth manager)

Implications

We can question whether the current business model for private banks is sustainable in the sense where our findings suggest that, rather than attempting to optimize financial products in terms of yield and risk, other ways should be explored. Ways that take into account the concept of perceived added-value in relation to elements of trust, the ability to understand and define financial objectives and the risk appetite of the client based on know-how.

Target audience

The Swiss private banking sector needs to be reinvented following the disappearance of Banking Secrecy. As we're currently working with specialists in the field, we aim to provide them with elements of service design which are typically not explored within traditional financial approaches.

Acknowledgements

We wish to thank the participants having followed the Masters in Luxury Management at the HEG between 2009 and 2013.

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