



## **Second thoughts on the Baer-UBS deal: not so transformational after all**

07/09/2005 by: Ian Orton

The dust is beginning to settle after the announcement that Zurich-based Julius Baer is to acquire the SBC Wealth Management division of UBS for SwFr 5.6 billion. And slowly, but surely, the realisation is beginning to sink in that the outcome of the deal may not be quite as clear cut as first thought, especially from a Julius Baer perspective.

This will not worry UBS. Not only does the deal enable UBS to dispose of assets that were becoming increasingly peripheral to its wealth management ambitions, but it looks as if it will get a handsome price for doing so. This includes a stake in the enlarged Julius Baer.

Let's look at the situation from a Julius Baer perspective. At first glance the deal appears to provide Julius Baer with increased scale in terms of client base and assets under management, a new management team and, through GAM, the prospect of tapping new product and geographical markets.

The reality may turn out differently, however. True, Julius Baer has acquired additional assets, especially in private banking. But these are mainly Swiss assets lodged at three relatively small private banks.

The suspicion is that these are mainly tied up with "old money" clients and not likely to grow fast. Indeed, growth, or the lack of it, may have provided the catalyst for UBS to seek a new owner for the banks.

More to the point, Baer does not appear to have been very successful in retaining existing clients' private banking assets in recent years. Indeed, it has hemorrhaged assets. Buying-in assets may be a good, if rather expensive way of staunching the flow. But will it be any more successful retaining assets in the future? As usual time will tell.

Of course it could be contended that Julius Baer's new management team is much better equipped to deal with the problems at the private banking division. This has experienced an outflow of assets and a higher cost income ratio than many of its peers.

In Alex Widmer, its “new” head of private banking, Baer appears to have the right man from the job. At Credit Suisse, where he was also head of private banking, Mr Widmer faced a similar problem, which he dealt with very successfully. Under his watch Credit Suisse’s cost-income ratio fell.

But there are potential problems. Until the announcement of the deal, Mr Widmer was set to assume the role of chief executive at the beginning of 2006, following the retirement of Walter Knabenhans. This will now not take place as Baer has decided to appoint Johannes de Gier, who comes with the UBS acquisitions, as chief executive. This effectively means demotions for both Mr Widmer and Thomas Meier, who arrived from Deutsche Bank as head of private banking, earlier this year.

Assuming that Mr Widmer stays the course, how will he improve Baer’s private banking efficiency ratios? In theory this can be achieved by either reducing costs, increasing income, or a combination of both.

Baer has attempted to reduce costs, with a degree of success. The feeling is, however, that it has tended to go for the easy options or 'low hanging fruit', although the UBS could generate further cost savings. Around 10 percent of the workforce may go as a consequence to share facilities and processes.

The scope for increasing revenue, especially within Switzerland, also looks problematic given the outflow of assets at private banking. Indeed, staunching the outflow of private client assets may provide a more telling test of the new management team's abilities than new asset growth, especially in the immediate short-term.

The acquisition of GAM, and the utilisation of its products and skills within the private banking division could make a difference. Except of course this will not happen. Under the terms of the deal GAM will retain effective operational autonomy. In other words it will be business as usual at the asset management firm established by Gilbert de Botton.

Foreign expansion could provide a possible solution to the conundrum. But as both UBS and Credit Suisse have shown, however, foreign expansion can be very expensive, especially in the short term.

Baer has made no secret of its desire to expand and it has made a number of initiatives in this respect. It intends to establish an onshore branch network in Germany, has hired a team in Argentina and is looking to make hires in Brazil and Uruguay. The firm also has ambitions in Eastern Europe and the Middle East.

Nonetheless, there is a paradoxical element about these developments. The firm decided to withdraw from the US private banking market because it lacked “scale”. But what type of scale

does it require to generate meaningful returns from entering completely new markets? It is hard to imagine that the acquisition of SBC Wealth Management will make much difference in this respect, although its constituent private banks have started to recruit teams to target Eastern Europe and Latin America.

And so we come to GAM. According to a number of industry experts *TheWealthNET* spoke to, GAM was increasingly perceived as UBS' "problem child." Not only did it insist on maintaining autonomy. Worse, it competed directly against its parent.

Moreover, given its size, the resources it could employ and the increasing use of open architecture, it wasn't as if UBS could not manage without its fund management subsidiary. On the surface there were few synergies between the two firms. It almost had to go. And in Julius Baer, UBS found a buyer willing to pay a good price.

Will GAM do anything to advance Baer's international ambitions. At first sight the answer would almost certainly be "yes." Once again, however, all may not be as it seems. The reality is that the GAM purchase may just reinforce the increasingly "Swiss" nature of Julius Baer.

"People in the UK perceive GAM as having a very international clientele," an industry veteran told *TheWealthNET*. "Analyse its client list and you will find that it has a significant Swiss and central European bias. By purchasing GAM, Julius Baer just reinforces its Swiss credentials."

The "new" Baer asset management division certainly has a distinct GAM tinge with David Solo, a former UBS high-flyer and chief executive of GAM, holding the reins. Roman von Ah, who appears to have done a very good job since arriving in 2004 as head of asset management, is relegated to the relative anonymity of head of Julius Baer Funds and segregated products.

The upside to all this is that GAM may become a more integrated component of Julius Baer than it was ever at UBS. And this could generate good results on the investment management front. But don't bet on it.

So, in summary it appears that the deal might not turn out to be as pivotal as initially thought, at least from a Baer perspective. It certainly marks a new phase of consolidation within the Swiss banking sector. And it should mean that a substantial segment of the market remains under Swiss ownership for some time to come. 'I think claims about the transformational aspect of the deal may have been overstated,' concluded our industry veteran. 'If anything it transforms Julius Baer into a much purer Swiss play.'

The reality is, as a number of industry experts, such as **Millenium Associates' Ray Soudah**, and Jeremy Charles of CSTIM have

pointed out, the main beneficiary of the deal is probably UBS.

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