

European High Net Worth 2008

February 2008

The Dimensions of Wealth

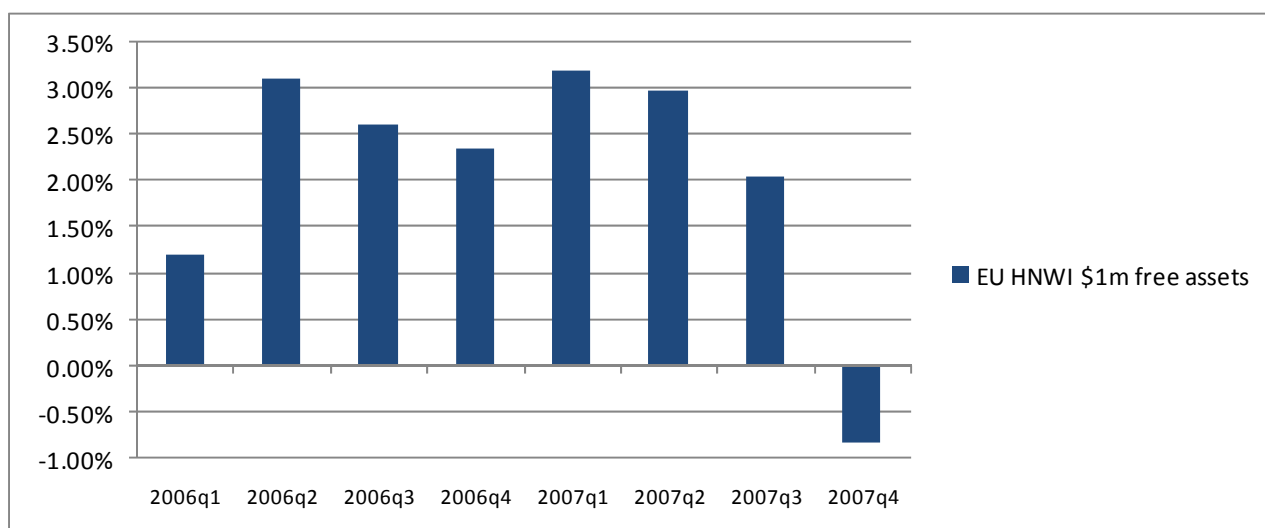
The number of high net worth individuals in the EU grew by 7.41% in 2007 to reach 2,761,300 in January 2008. Although 2007 overall was another year of strong growth in individual wealth across Europe, the sharp decline in asset values seen in the second half of the year put a brake on HNW growth and in the fourth quarter of 2007 the number of EU HNW individuals declined by 0.83% – the first quarterly decline since 2002.

Not all regions of the EU experienced this decline; in the countries of Western Europe (particularly the UK) individual wealth creation had already experienced some slowing and the decline in equity values seen in Q3 and Q4 2007 accelerated this trend, while in the countries of central and eastern Europe individual wealth continued to grow albeit at a slightly slower rate.

Highlights

- The number of high net worth individuals in the EU grew by 7.41% in 2007 to reach 2,761,300 in January 2008.
- Including the non-EU countries of Norway, Russia and the Ukraine increases the European market to 3,055,500.
- The largest HNW segment is in the UK where there are some 570,000 individuals with more than \$1m in investable assets.
- The fastest growing HNW segments are in the Czech Republic, Slovakia and Poland with growth rates of 11.0%, 10.7% and 10.4% p.a. respectively.
- The rate of HNW growth across the EU slowed sharply in the second half of 2007 and was negative in Q4 2007.

Figure 1 - EU HNW Quarterly Growth 2006/7



Western Europe

<i>\$1m equiv in free assets</i>	HNWI 2008 (individuals)	% change	HNWI 2007 (individuals)	% change	HNWI 2006 (individuals)
UK	571200	7.49%	531400	10.71%	480000
Germany	387700	8.48%	357400	9.20%	327300
France	365000	7.07%	340900	8.29%	314800
Italy	312500	6.91%	292300	9.60%	266700
Spain	206500	8.29%	190700	8.72%	175400
Netherlands	136200	7.08%	127200	7.89%	117900
Belgium	109200	6.95%	102100	8.85%	93800
Luxembourg	90500	7.35%	84300	8.91%	77400
Portugal	48100	5.95%	45400	7.84%	42100
Ireland	36500	8.63%	33600	11.63%	30100
Cyprus	1300	8.33%	1200	9.09%	1100
Malta	1200	9.09%	1100	10.00%	1000

20% of the EU's HNWI individuals live in the UK, with most living within commuting distance of London. The steady increase in HNWI numbers in the UK in recent years has been driven by the ready availability of credit (particularly for property development), remarkable increases in domestic property prices, a strong small/medium business sector, relatively benign taxes and corporate regulation and, most importantly, the UK's success in financial services.

The UK's twin "Achilles Heels" however, is this dependency on both the financial services sector and property development for the growth in HNWI individuals. Since 2005 over 55% of HNWI growth has been from these 2 sectors, with an even higher proportion in the £1m+ (\$2m) wealth segment. The fallout from the 2007 "Credit Crunch" has been to reduce to flow of credit for speculative property transactions, to reduce the number of individuals in asset management and investment banking receiving very high bonuses and an absolute reduction in the value financial assets. The consequence has been a fall in HNWI numbers in Q4 2007.

In contrast, the HNWI markets in France and Germany are much more broadly based. HNWI sector growth has come from increases in existing wealth

as well as creation of new wealth. Although there is a significant number of HNWI individuals connected to the financial services in both countries, a far greater proportion of HNWI individuals in both France and Germany are entrepreneurs, business owners or executives. The continued growth of HNWI wealth is closely linked to the success of the medium sized corporate sector; the ready availability of credit is a key driver for the corporate sectors in both countries and the tightening of credit will be a brake on the growth of HNWI individuals. Inherited wealth is significant in France and in the west of Germany, but is relatively low in the former DDR.

HNWI numbers in the Benelux region have grown steadily in recent years, but the growth of HNWI individuals has been driven by increases in the value of existing wealth, rather than the creation of new wealth. In particular:

- The stock of wealthy corporate executives, an important sub-segment of the HNWI market in the region, has gradually declined and is not being replenished,
- Most small/medium enterprise business wealth was created in the 1960s and 1970s and there has been much lower new wealth creation in recent years compared to other countries in the EU.

HNW numbers in Italy grew steadily in 2007 but at a slower pace than in the other large EU economies. The HNW \$1m plus sector is a mix of new wealth and inherited wealth, but conservative investment preferences, restrained property values and a tendency for wealth consumption has constrained the growth of existing wealth. However, despite relatively low national economic growth, wealth creation in the northern region of Italy (Lombardy, Lazio, Emilia Romagna, Veneto and Piedmont) has continued at levels similar to those in other Western European countries.

Spain's impressive economic growth has generated a large number of individuals in the affluent and sub-HNW sectors. Growth in the number of HNW individuals during 2007 has been slightly lower than would be expected from this magnitude of personal wealth generation, but increases in existing assets plus new wealth creation suggests that HNW growth is probably more sustainable than in many EU countries. Unlike many EU countries there was relatively little slowdown in HNW growth in Q4 2007.

Portugal, in contrast, has seen HNW wealth creation at the lower end of the EU15 states. The EU expansion into Eastern Europe has erased Portugal's historic competitive advantage particularly in the manufacturing and agriculture sectors, and the service sector has become Portugal's largest employer. Affluent segment growth was strong in 2007, but the growth of the Portuguese HNW sector in 2007 was driven by increases in existing wealth rather than new growth from entrepreneurial activity.

Ireland's HNW sector has expanded strongly as the Irish economy has flourished with very high rates of GDP growth. Although in 2006 HNW growth in Ireland was the highest in EU15, HNW growth peaked in Q1 2007 and there was a gradual slowdown through the rest of the year. Much of this can be attributed to the decline in the residential property market, which had contributed significantly to the growth of HNW individuals in Ireland. However, the economy is broadly based and entrepreneurial activity remains high, individual wealth creation remains at above the EU average.

Scandinavia

<i>\$1m equiv in free assets</i>	HNWI 2008 (individuals)	% change	HNWI 2007 (individuals)	% change	HNWI 2006 (individuals)
Sweden	80900	7.01%	75600	6.93%	70700
Denmark	57000	5.95%	53800	5.91%	50800
Finland	41900	5.54%	39700	8.77%	36500
Norway	103100	7.17%	96200	7.85%	89200

Despite high levels of personal taxation, the HNW segments in the Scandinavian countries have grown steadily in recent years, although not as fast as the affluent segment in these countries. Strong economic growth, government policies to encourage the development of small and medium businesses and an increased appetite for financial risk has fuelled both the growth of existing portfolios and the creation of new wealth.

Unlike many EU countries, wealth creation in Scandinavia has been broadly based, without an over concentration on property development or the ready availability of inexpensive bank lending, and this suggests that HNW growth is likely to continue in any economic down turn. Only in the ultra HNW segment has growth been significantly slower than the EU norm. A high proportion of the largest investment portfolios are held outside country of domicile; the Channel Islands, Luxembourg and Switzerland being the most popular destinations for Scandinavian wealth.

Central Europe

<i>\$1m equiv in free assets</i>	HNWI 2008 (individuals)	% change	HNWI 2007 (individuals)	% change	HNWI 2006 (individuals)
Poland	77800	10.35%	70500	16.72%	60400
Czech Rep.	26200	11.02%	23600	13.46%	20800
Hungary	21000	7.14%	19600	12.64%	17400
Slovakia	9300	10.71%	8400	12.00%	7500
Bulgaria	6800	4.62%	6500	3.17%	6300
Romania	22600	5.12%	21500	3.86%	20700
Slovenia	5000	6.38%	4700	9.30%	4300

The competitive advantages enjoyed by Central European states since 2004 has transformed these economies and created individual wealth at an unprecedented rate. Although there was some slowdown in the second half of 2007, nevertheless the growth of both the affluent and the HNWI segments in Poland, the Czech Republic and Slovakia continued at a rapid rate. Average personal wealth in these countries remains well below EU15 average, but the rise in property values, booming construction and encouragement of entrepreneurs has created a number of wealth “hotspots” (e.g. Wroclaw in Poland) where the HNWI segment is large and growing. In Hungary, the HNWI sector should grow steadily as the economy recovers from weak GDP growth and relatively high inflation.

Slovenia stands out from the other Central European states. Having adopted the Euro in January 2007 Slovenia has been successful in capitalising on the benefits of the single currency without experiencing too many significant problems. Wealth creation is broadly based, with the afflu-

ent segment (\$250k to \$1m) proportionally larger than other Central European states, but growth in the HNWI sector slowed during the second half of 2007.

In both Romania and Bulgaria there is little “old wealth”; growth in personal wealth is linked very closely to the health of the economies and the degree of entrepreneurial activity over recent years. The accession of both countries to the European Union in January 2007 provided a significant stimulus to wealth creation (as in the A8 states in 2004), and the construction and property sectors in both countries have benefited from increased investment. Retail property has been a major source of new wealth and this looks to continue (providing there is sufficient lending capacity available) and constraints on foreign ownership of land suggests that much of the wealth created will be channeled domestically. However, inflation remains high due to strong domestic demand, high resource utilization and large current account deficits.

The Baltic States

<i>\$1m equiv in free assets</i>	HNWI 2008	% change	HNWI 2007	% change	HNWI 2006
Estonia	2300	4.55%	2200	10.00%	2000
Latvia	4100	5.13%	3900	5.41%	3700
Lithuania	6800	4.62%	6500	14.04%	5700

Despite very high GDP growth in the region in recent years there has been a sharp slowdown in the growth of HNWI individuals in the Baltic states

– although the growth in the number of affluent individuals with between \$250k and \$1m remains buoyant. There is little inherited wealth in these

countries, so growth in personal wealth is linked very closely to the health of the economies in each state and the degree of entrepreneurial activity over recent years. In all three countries, inflation remains high due to strong domestic demand and high resource utilization; the three states are also

plagued by continued major imbalances and large current account deficits. The HNWI sector has been affected by the tightening of credit and there is some evidence of consumption of wealth exceeding wealth creation in the 2nd half of 2007.

Russia and Ukraine

<i>\$1m equiv in free assets</i>	HNWI 2008 (individuals)	% change	HNWI 2007 (individuals)	% change	HNWI 2006 (individuals)
Russia	147400	12.09%	131500	9.58%	120000
Ukraine	43700	7.11%	40800	9.09%	37400

In both Russia and the Ukraine nearly all HWN individuals are first-generation millionaires, the majority being entrepreneurs in both the manufacturing and service sectors of the domestic market. In both countries, wealth creation has accelerated in recent years as structural reforms have successfully started to transform the economies. However, decades of under-investment in both physical and social infrastructure is likely to place real constraints on the pace of future growth of the HNWI segments. Analysis of the sources of HNWI wealth suggests that many in this segment benefited from “quick wins”

at the time of major economic reforms, and that opportunities of the same magnitude have been more difficult (or impossible) to exploit since.

However, Russia’s natural resources provide an exceptional opportunity for the expansion of both the economy in general and individual wealth. In particular the supporting industries (rather than the primary producers and those in State control) are areas where significant wealth has been created and will continue to do so.

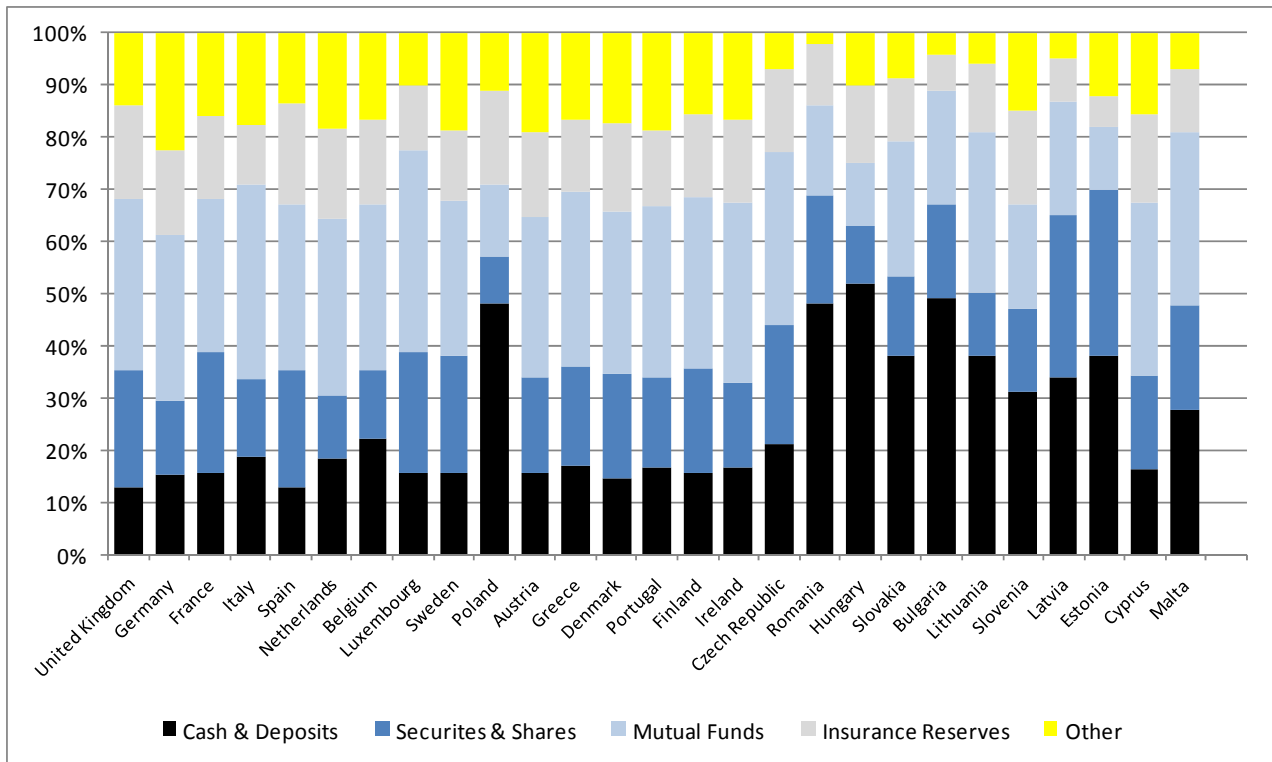
Composition of EU HNWI wealth

As HNWI individuals (and their advisors) learn more about risk and return there is a gradual move from low risk investments (cash and deposits) to higher risk vehicles, and at times of falling investor confidence the process is reversed with the HNWI increasing the proportion of assets held in cash and deposits.

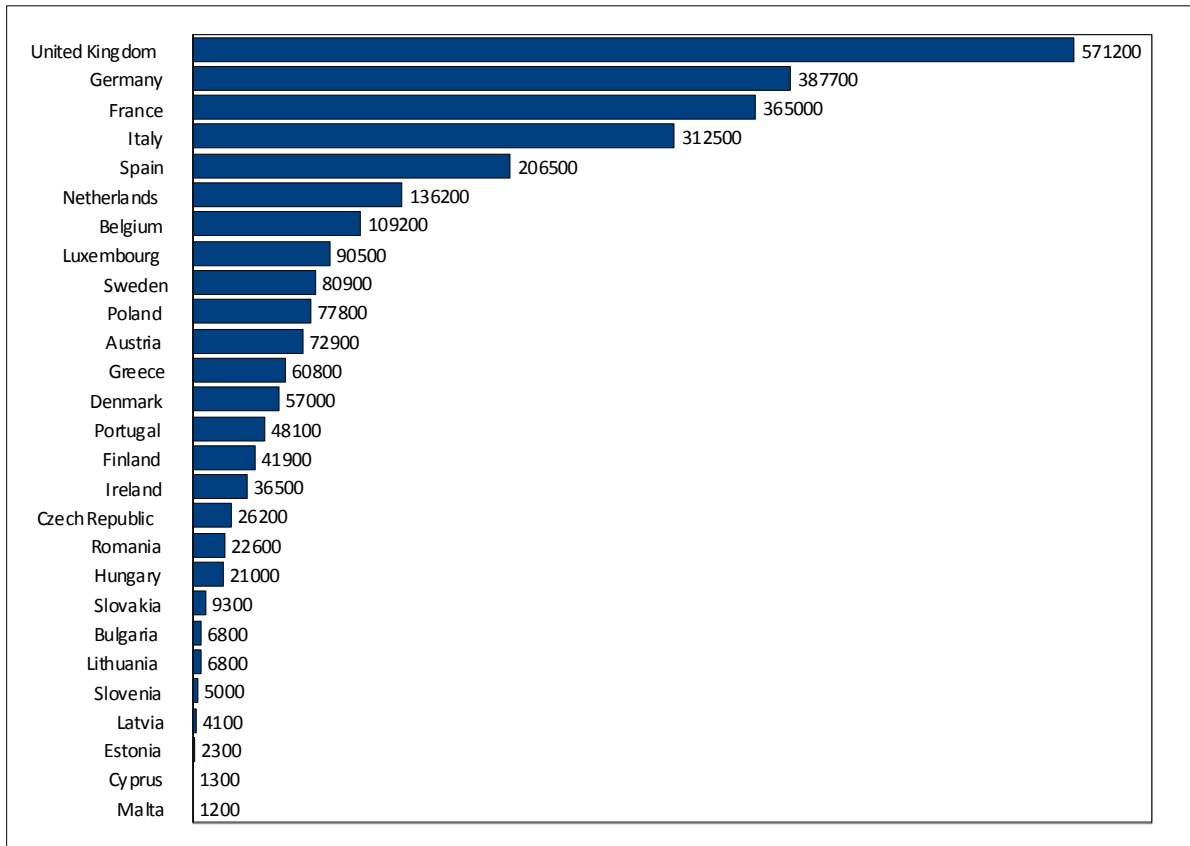
As the Figure 2 below shows at the end of 2007 there is a dichotomy between those countries

where HNWI investors have a balanced approach to risk and those countries where capital preservation is paramount and HNWI preference is for investment in very low risk investments. Although across the EU there has been a move from equity based investments to cash, given the volatility of the equity markets, at the end of 2007 the overall composition of most HNWI portfolios was unchanged from 12 months earlier, but with new funds held back waiting some indication of market stability.

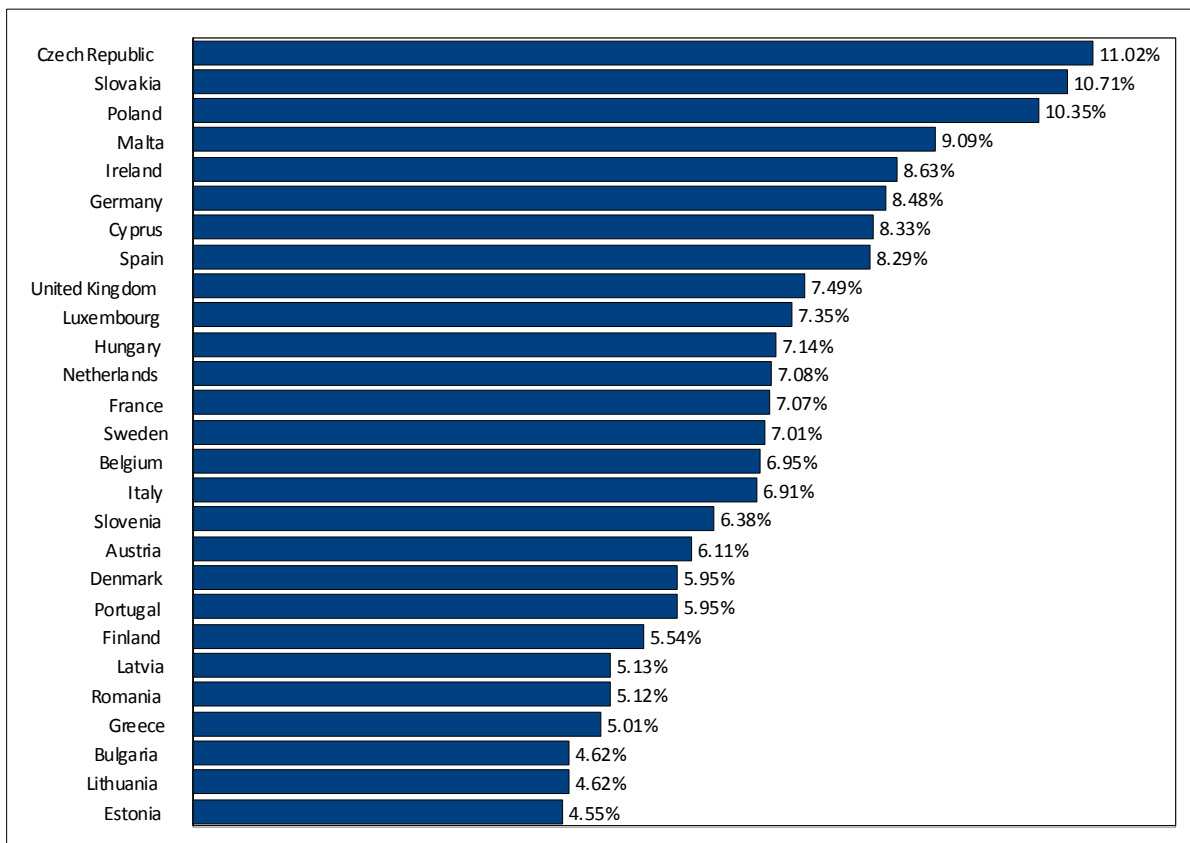
Figure 2 - Composition of EU HNW wealth



Appendix 1 - EU HNW market by size January 2008



Appendix 2 - EU HNW market by 2007 growth rate



About MDRC

MDRC (Market-Dynamics Research & Consulting Ltd) is a management consultancy dedicated to maximising value to its client firms. MDRC delivers high value solutions through small, experienced teams working with clients in the pursuit of innovative solutions. MDRC's core skills are in strategy consulting, marketing and product development, client retention, and strategic research.

MDRC's areas of interest are the high net worth (HNW) markets in Europe, particularly the UK, and the wealth management, private banking, insurance and investment business that seek to serve high net worth individuals. Our clients range in size from the largest US and European Banks, to businesses with fewer than 10 employees. We undertake a wide range of client specific assignments using well-established value based frameworks. The MDRC team provides our clients with cost effective support and assistance in practical strategy formulation and implementation.

To support our work in the EU HNW sector we have developed unique market models, with a knowledge base derived from conversations with many hundreds of high net worth individuals each year. These individuals come from a broad spectrum of behavioural segments, risk appetites and wealth values. We believe that our market model and knowledge base is a very accurate proxy for the total EU wealth market.

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