

Central European Wealth

December 2007

Prospects for continuing growth in 2008?

We're not sure who first called them the "Lynx" economies, but the economies of central and eastern Europe have generated very high rates of HNW growth since 8 states joined the EU in 2004 and 2 joined in 2007. In that time, the increase in HNW numbers and assets have been driven by high levels of GDP growth, the free availability of credit, development of the local real estate and, most importantly, liberalisation of their previously restricted local markets.

The individuals who have benefited most from the opportunities have been professionals (esp. lawyers and accountants), property developers and the owners of medium sized local businesses. In our research into the HNW sector in these countries, it has become clear that the free availability of local credit is one of the most important catalyst of HNW growth.

The question we have been asked on numerous occasions in recent month is whether the credit and liquidity crisis in the world banking sector will adversely impact the economies of central and eastern Europe (CEE), and slow the growth of HNW wealth.

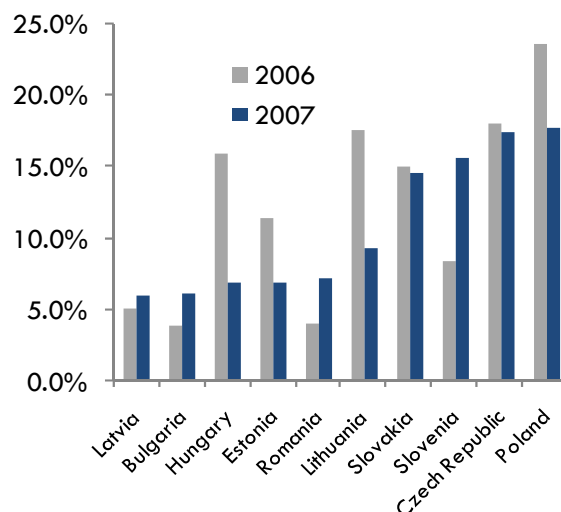
The consensus view is that the underlying prospects for regional growth remain positive into 2008/9. However, although the drivers of individual wealth also remain positive over the next 18-24 months, the outlook for HNW growth is less certain.

At the margin, any significant reduction in the supply of credit to the small/medium corporate sector or for property development will adversely influence the growth of HNW wealth.

Highlights

- HNW growth is dependent on the continuing supply of credit to property development/construction and the small/medium corporate sector.
- HNW growth rates in 2007 are generally lower than in 2006, with a slowdown seen in the second half of 2007.
- Poland, the Czech Republic, Slovenia and Slovakia will show the highest growth rate in HNW individuals in the CEE sector.
- HNW growth in the Baltic states has fallen back to pre-2005 levels.
- Consumption of wealth by HNW individuals is high and is one driver for the high level of HNW cash deposits.

Figure 1 - HNW Growth 2006/7



For this analysis we have re-visited our assumptions on GDP growth, GDP per capita, inflation, employment, taxation, salary levels, property values, construction activity, local stock-market performance and business confidence for each of the 10 countries in the region, to give an up-to-date measure of growth in HNW numbers.

We have also re-assessed our analysis of the relative attractiveness of the wealth market in each of the countries. In particular, we have re-examined the barriers to entry, the ratio of "Self directed" to "Dependent" investors, relative risk appetite and propensity of HNWI to take up wealth management products and services.

Figure 2 below shows a plot of the revised assessment of each CEE country for market attractiveness and HNW growth in relation to the same measures for an average of the 27 EU states. The significant difference between this analysis and our previous assessment in 2005 is that there is now a clear dichotomy between the "best" and the "worst" countries — at least from a wealth management perspective.

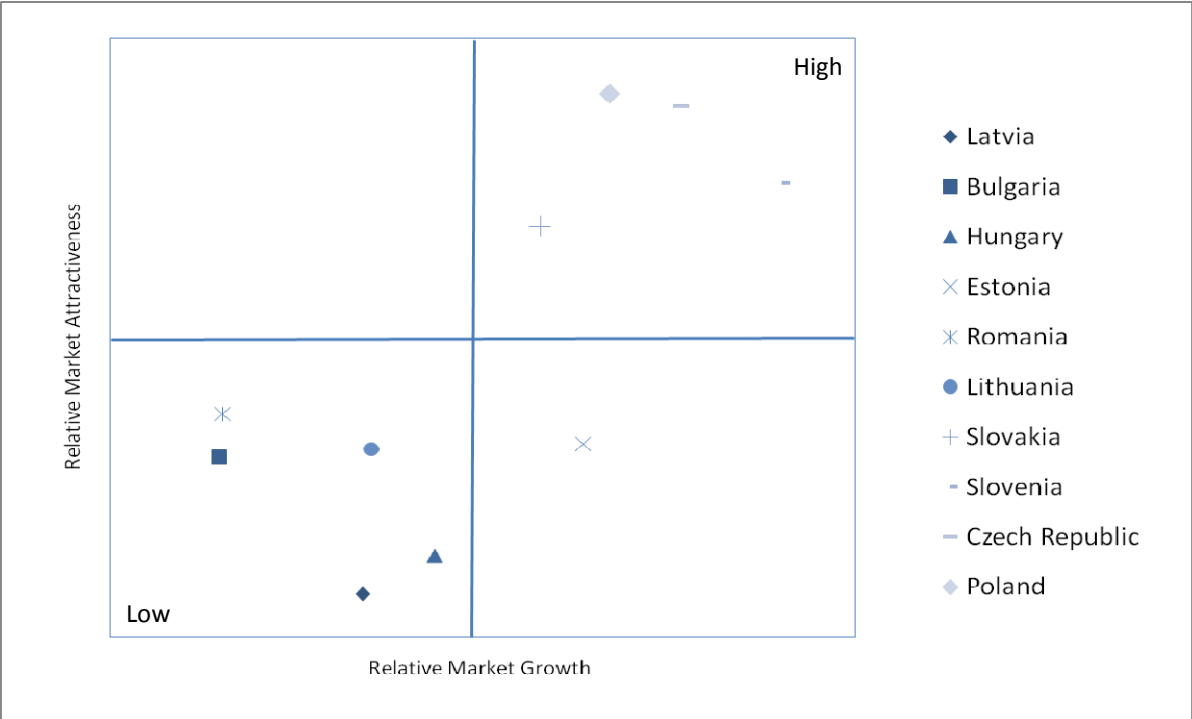
Poland, the Czech Republic, Slovakia and Slovenia are the countries with high rates of

HNW growth and structurally attractive wealth management markets. In contrast, the Baltic states of **Latvia** and **Lithuania** are likely to see GDP growth in 2007/8 at over twice the EU average, but the rate of HNW growth in these countries has slowed and is now at 2004/5 levels. The wealth management markets in these countries are weak.

Although the HNW segment in **Estonia** is expected to grow at a faster rate than its Baltic neighbours, market attractiveness is no higher. GDP in both **Bulgaria** and **Romania** is forecast to grow at around 3 times EU average, but net HNW growth is relatively low as consumption of wealth continues to outpace the rate of HNW investment.

The most difficult country to assess is **Hungary**. The austerity measures introduced by the current government, a weak currency, highly volatile stock market, very high public sector debt and GDP at a third of its neighbours point to an economy in transition. In the short term HNW growth will be low and the wealth management market is relatively unattractive. However, there are sufficient indicators to suggest that the wealth sector in Hungary will grow in line with its' closer neighbours.

Figure 2 - Relative market growth & attractiveness v EU 27 average



About MDRC

MDRC (Market-Dynamics Research & Consulting Ltd) is a business 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.

We focus on catalysing strategic change and value creation in financial services. MDRC helps deliver success for shareholders, employees and customers through product development, process change and strategy formation.

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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