Breaking new ground

The family office industry is an environment ripe for myth building. Offices operate below the radar, stay out of the limelight and are wary about sharing too much information. In this 12-page section, *Michael Finnigan* unpicks some of the industry's commonly held beliefs debunked by the inaugural *Global Family Office Report*

One of the most enduring family office myths is that no one office is alike. The industry's most common phrase, 'once you've seen one family office, you've seen one family office', speaks to their distinct nature. Yet the inaugural UBS and Campden Wealth *Global Family Office Report 2014* has cast doubt on this conventionally held wisdom, finding that family offices have more in common than originally thought. This research snapshot is designed to give an overview of the report's key points for offices from the regions, North America, Europe, Asia-Pacific and developing economies (DEVEC). It will also overturn a few myths along the way.

Based on the surveys of 205 principals, beneficiaries and executives, the *Global Family Office Report 2014* is the largest family office study ever committed to paper. The sample size ranges across 40 different countries and included offices that manage more than $180 billion (€144 billion) in global assets in total.

Philip Higson, vice chairman at UBS's global family office group, says that the large number of respondents is one reason why the global study has debunked so many long-held family office myths.

"Before the study I had the perception that family offices were relatively similar, but I've been absolutely amazed at how similar they are by geography. The range of variants is really quite small, whether you take the cost-line item or asset allocation strategy," he says.

Higson says the most surprising revelation was that large family offices were not able to demonstrate economies of scale whatsoever, which he speculates is because they are forced to spend on additional services. He said the negative effect of close owner involvement on performance was also surprising (see Comment on page 11).

"There is a feeling that the owner is meddling with the investment committee, which would cause them to have a little bit of a flip-flop in terms of how the team goes about asset allocation. This is because family members make the mistake of believing entrepreneurial success can translate to investment success," he cautions.

Other findings from the report suggest there is a high degree of co-investment between family offices around the globe, with almost four-fifths participating in office-to-office deals. These deals averaged around $76 million annually for syndicated deals, and $119 million for private equity deals.

The report also revealed that environmental, social and corporate governance issues were not prevalent in family offices' investment strategy, but did

Before the study I had the perception that family offices were relatively similar, but I've been absolutely amazed at how similar they are by geography

Above: Philip Higson, vice chairman at UBS's global family office group

GLOBAL FAMILY OFFICE STUDY 2014

Average assets under management (2013)
$890 million

Return on investment (2013)
9%

Respondents from
40
different countries

Wealth under management
$180 billion

have an impact on asset allocation. Family offices that considered these governance issues when choosing investments were least likely to underperform.

Higson says that there are three things that family office executives should take away from the report if they hope to better serve their employers.

"Firstly, there needs to be an improvement in communication. The report shows that there is a divergence between how much services cost and how much family members value the service. This means that family office executives have failed to communicate the cost benefit of the said line item," he says.

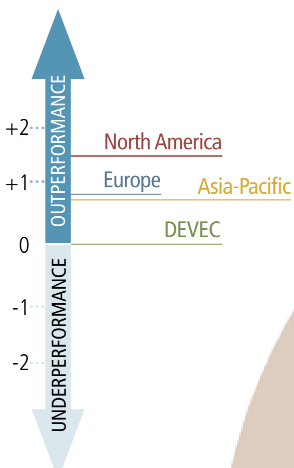
"Secondly, what is it that the family thinks costs a lot or values highly? These are family professional services. They actually cost less to implement but are highly valued by the family. Things like managing cars or boats, or bill paying services.

"The last key finding is how poorly family reputation management is handled. Direct reputation management is not particularly high on the radar screen of the services provided, but it is very high on the radar screen of what families want. The repercussions of a drunken night in a bar can last the next 50 years."

The *Global Family Office Report 2014* also predicts that investment strategy, along with the points raised by Higson, will become increasingly important to family offices over the next 10 years. FO

GLOBAL OVERVIEW

OVERALL INVESTMENT PERFORMANCE (LAST 12 MONTHS), BY REGION



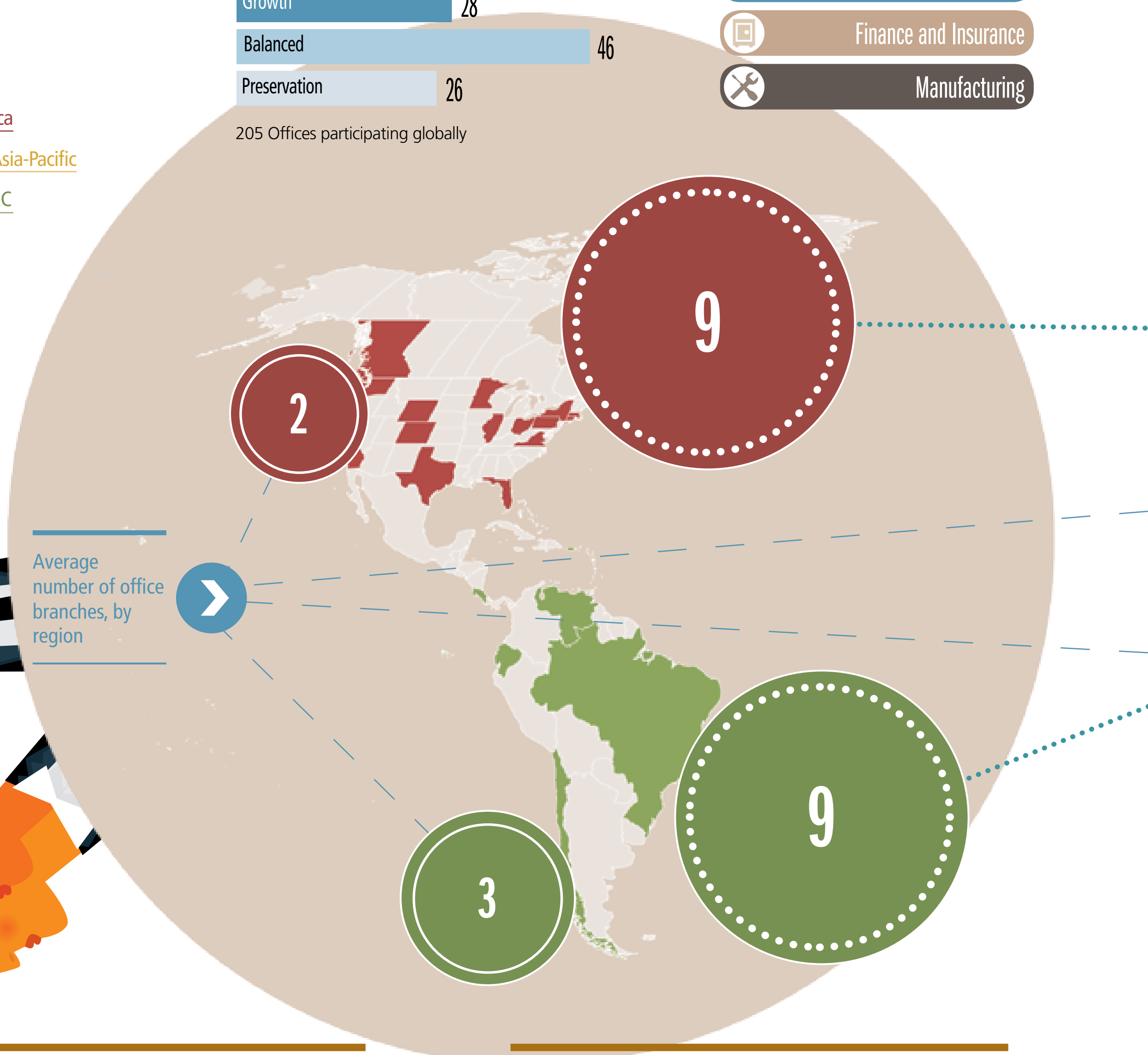
GLOBAL INVESTMENT STRATEGIES, IN %

Growth	28
Balanced	46
Preservation	26

205 Offices participating globally

KEY INDUSTRIES

- Real Estate and Rental & Leasing
- Finance and Insurance
- Manufacturing



AVERAGE COSTS OF OPERATING THE FAMILY OFFICE IN BASIS POINTS (OF AUM)

60 Mode

80 Median

86 Mean

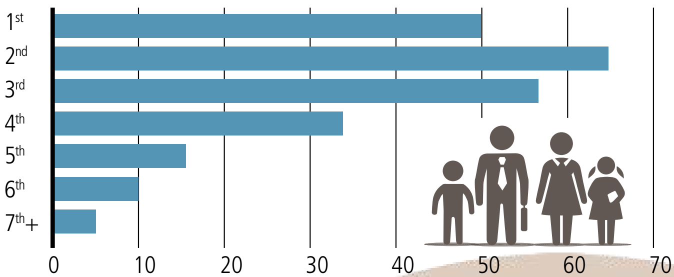
Source: Global Family Office Report 2014

GLOBAL FAST FACTS

9% Average FO portfolio return in 2013

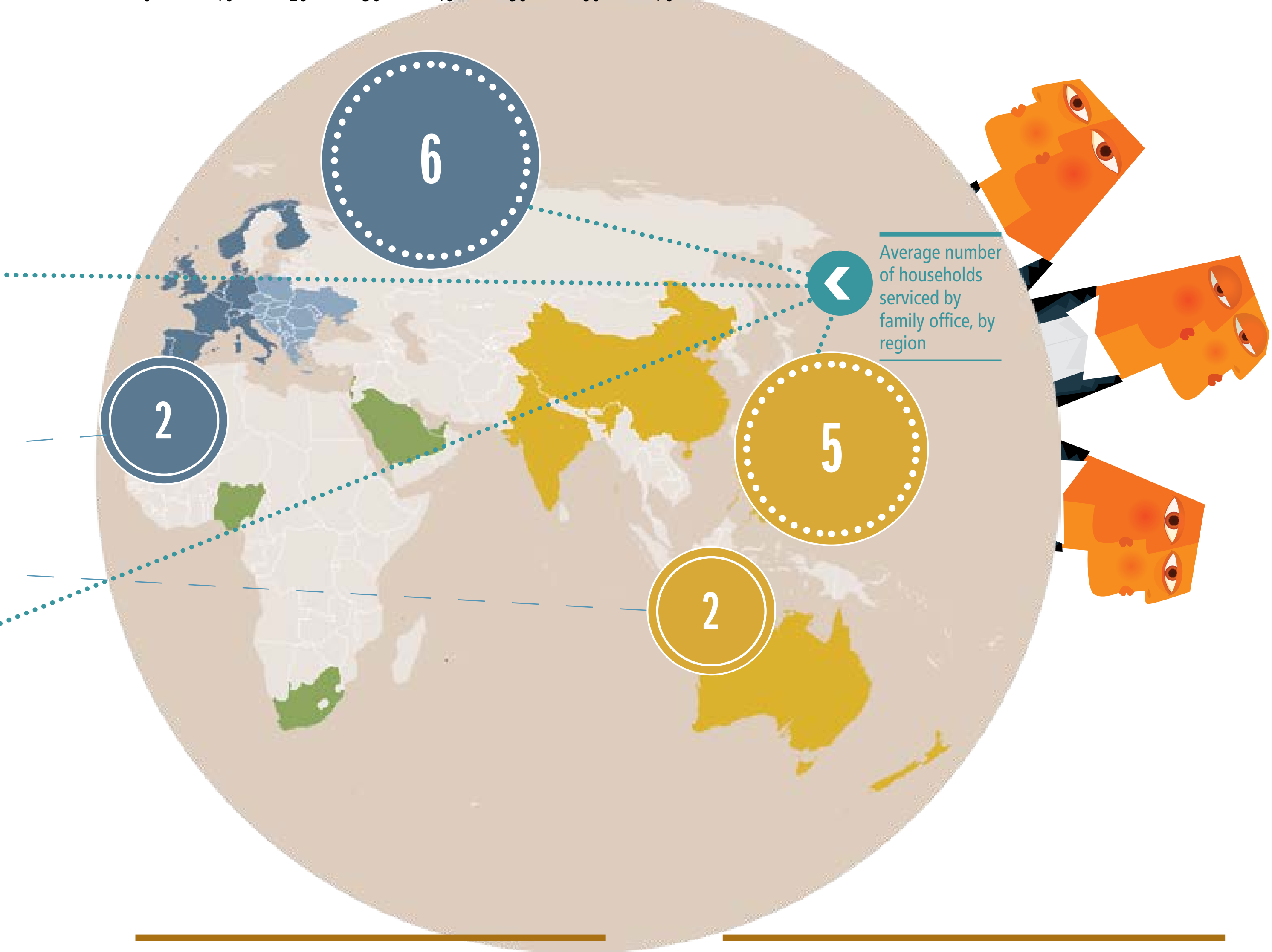
80% of FOs collaborate with one another on investments

GENERATION CURRENTLY SERVICED BY FAMILY OFFICE, IN %



AVERAGE YEAR FOUNDED

1995	1994	2001	1999
Europe	North America	Asia-Pacific	DEVEC



PROPORTION OF FAMILY OFFICES FORMED AFTER THE MILLENNIUM

52%	57%	76%	65%
Europe	North America	Asia-Pacific	DEVEC

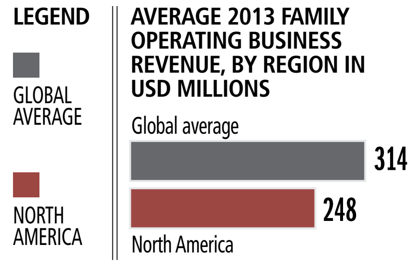
PERCENTAGE OF BUSINESS-OWNING FAMILIES PER REGION

65%	52%	71%	81%
Europe	North America	Asia-Pacific	DEVEC

NORTH AMERICA

Going it alone

Family offices in North America are not collaborating on investments as much as originally thought. Why is the world's largest wealth market cool on the concept, when it's so popular in other parts of the globe?



The popular belief that family offices in North America regularly invest together has been challenged by the *Global Family Office Report 2014*, finding instead that they are the least likely to co-invest.

According to the report, 61% of family offices in North America co-invested together in 2013, while in European offices this figure sat at 86%.

Almost half of North American family offices said they had never taken part in syndicated deals facilitated by banks, while two-thirds of family offices in Asia-Pacific reported high engagement in these types of deals.

Daniel Goldstein, senior managing director at Manchester Capital Management, a North American family office, hears from some families that they believe co-investment is a sign of inexperience.

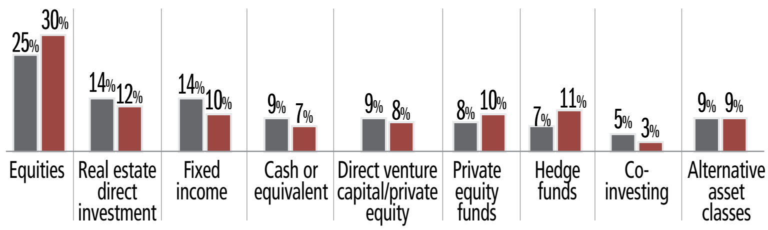
PERFORMANCE

Of all offices worldwide, North American offices were most likely to outperform their 2013 investment benchmarks, and no office in the region reported underperformance. Office outperformance is strongly linked to the adoption of growth strategies. North American offices allocate significant portions of overall portfolios to developed-market equities, followed by direct investment in real estate, and attribute a tenth of overall allocations to hedge funds. Private equity funds constitute a higher allocation in North American offices than in global counterparts.

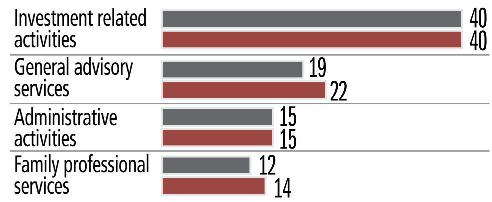
MANAGEMENT

Portfolio horizons in North American offices are among the longest worldwide: over three in 10 offices gear their portfolios toward horizons of more than 10 years. The region also has the lowest proportion of offices investing for less than three years. The trend toward co-investing – whether office-to-office or through a syndicated deal facilitated by investment banks – requires offices to conduct due diligence, research and monitor deal flows in-house, much like family offices in Asia-Pacific.

TYPICAL INVESTMENT PORTFOLIO (10 MOST LIKELY ASSET CLASSES), BY REGION



AVERAGE BASIS POINTS OF AUM COST ALLOCATED PER SERVICE AREA, BY REGION



Many family offices in North America are doing direct deals, but many are keeping it under the radar. Actively investing families do not want others to ride on their coat tails.

Daniel Goldstein, Manchester Capital Management

"Many family offices in North America are doing direct deals, but many are keeping it under the radar. Actively investing families do not want others to ride on their coat tails. There may be a bit of naiveté among some European families who hope to attach themselves onto deals from more experienced families."

Goldstein questions why a family office would co-invest if it already had good deal flow and capital. "Why would you trust that somebody else is not just cherry picking and offloading their most risky deals?"

Goldstein, who has worked on both sides of the Atlantic, says an added concern is that family offices often don't have a robust legal framework to assist when deals go wrong.

"Co-investment sounds great when everything goes well and suffers when deals go bad. The last thing you want is to just have a handshake and be sent on your way," he says.

Worldwide, legal services are the least likely to be provided in-house, the report found, embedded in just 6% of family offices. In the last year, the number of family offices in North America using in-house legal services has almost halved, from 9% to 5%.

Goldstein says family office structures in North America will undergo sweeping changes when Millennials, those born between the 1980s and 2000s, assume control.

"Family offices are going to be leaner and more focused on achieving societal gains while looking for financial gains. They will change constructs of what they do and the way they deploy capital," he says.

The *Global Family Office Report 2014* found that North American offices were most likely to outperform against their benchmarks, whether the goal was wealth preservation or capital growth.

COST AND STRUCTURE

Offices in the region have an average cost of 91 basis points, of which 40 basis points are allocated to investment-related activities (in line with the global average). North American offices are surpassed in the proportion of costs they allocate to investments only by Asia-Pacific offices. Such a difference in costs is attributed, largely, to the maturity of the regional office environment and, consequently, professional staff, as well as the pursuit of more costly, sophisticated investment vehicles, such as hedge funds.

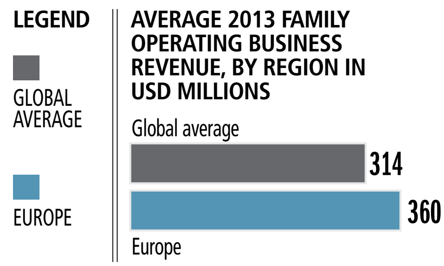
FAMILY EXPECTATIONS

North American family offices are focused on governance, as many principals reach retirement. While many family offices in the region have already adopted formalised governance structures (ahead of other regions), the remainder are preparing now for transition, whether successors are family members or non-family executives. Increasingly, families are looking towards impact investing to fulfil their desires to give back to society, while still meeting investment targets.

EUROPE

Too much of a good thing

European family offices are less likely to manage philanthropy projects than their global counterparts. What impact is this having on their charitable giving and engagement of the next generation?



Family offices in Europe are far less interested in managing family philanthropy than originally thought, with more than one-third (36%) not involved in the practice at all, according to the *Global Family Office Study 2014*. This is proportionally higher than any other region.

Despite this, European family offices have the highest volume of assets dedicated to philanthropy. If their volume of giving is the highest, why do offices not undertake their management?

Campden Wealth's head of research, Andrew Porter, says the Continent's history of state support, which has long promoted the welfare and cultural good of its citizenry, could be one reason why family offices take a backseat on philanthropy.

"State responsibility in Europe, expressed through both health and education initiatives, as well as a legacy of state patronage for the arts, has

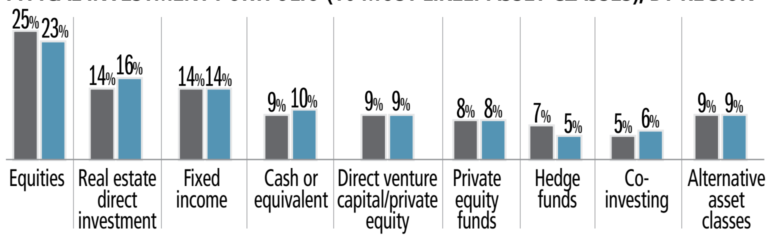
PERFORMANCE

European family offices mirror the Global Family Office Report average findings with improved confidence and a clear willingness to accept more risk in their portfolios. Traditionally, European offices have a bias towards the preservation of capital, resulting in the pursuit of more conservative investment strategies, relative to offices domiciled outside of Europe. However, as highlighted in the 2013 European Family Office survey, offices in this region last year began implementing more pro-growth asset allocations. Subsequently, European family offices have benefited from strong performance from equities, private equity and direct investments in 2013.

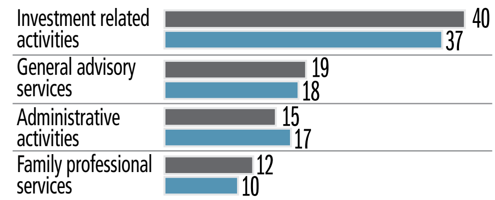
MANAGEMENT

Family offices in the region typically manage longer-term assets, such as real estate, private equity and direct investments, in-house. There seems to be a trend toward insourcing investment services, while technical, legal and tax-related services are increasingly outsourced. Shorter-term assets, hedging instruments and derivatives, which require a high degree of monitoring and execution expertise, are managed via investment and private banks. Portfolios with exotic financial instruments are typically outsourced to asset managers.

TYPICAL INVESTMENT PORTFOLIO (10 MOST LIKELY ASSET CLASSES), BY REGION



AVERAGE BASIS POINTS OF AUM COST ALLOCATED PER SERVICE AREA, BY REGION



State responsibility in Europe, expressed through both health and education initiatives, as well as a legacy of state patronage for the arts, has effectively put charity at the back of many entrepreneurs' minds.

Andrew Porter, Campden Research

effectively put charity at the back of many entrepreneurs' minds," he says.

"This may have created a second-order effect on family offices, causing them to place less importance on philanthropy. Unfortunately, European family offices seeking to promote family legacy place less emphasis on social capital."

Porter says there could also be a perception in Europe that wealth is better spent donating directly to an experienced charity.

Despite a high proportion of family offices having no involvement in philanthropy, one-third had endowments of at least $10 million, with many focusing on the healthcare and education sectors.

Family offices listed the benefits of philanthropy as family legacy and fostering family union. Porter adds that many family offices use philanthropic causes to engage the next generation. That, however, did not stop family offices worldwide from ranking charity as their lowest priority.

Porter predicts family offices will professionalise their philanthropic function in the future as the next generation seek to develop better ways of measuring impact.

The *Global Family Office Study 2014* concludes that philanthropy plays an important role in family legacy – not only because of the social good it provides, but also because it serves as a catalyst for succession.

Porter says two additional, emerging trends to track among Europe's family offices are data security and reputation management. "It remains to be seen whether family offices will evolve to manage aspects of risk beyond an office's traditional investment-focused remit. Considering how privacy, data security and reputation function as core components of family legacy and social capital, it would be surprising if offices do not adapt to manage this remit."

COST AND STRUCTURE

Direct family office costs are slightly lower in Europe than the global average of 86 basis points per annum. Lower costs are a function of the larger average portfolio size of USD900 million and total assets of USD1.5 billion per family office. Investment style also contributes to running the typical European family office at lower marginal cost, because they have a higher proportion of 'conservative mandates' which tend to be cheaper to manage than growth mandates.

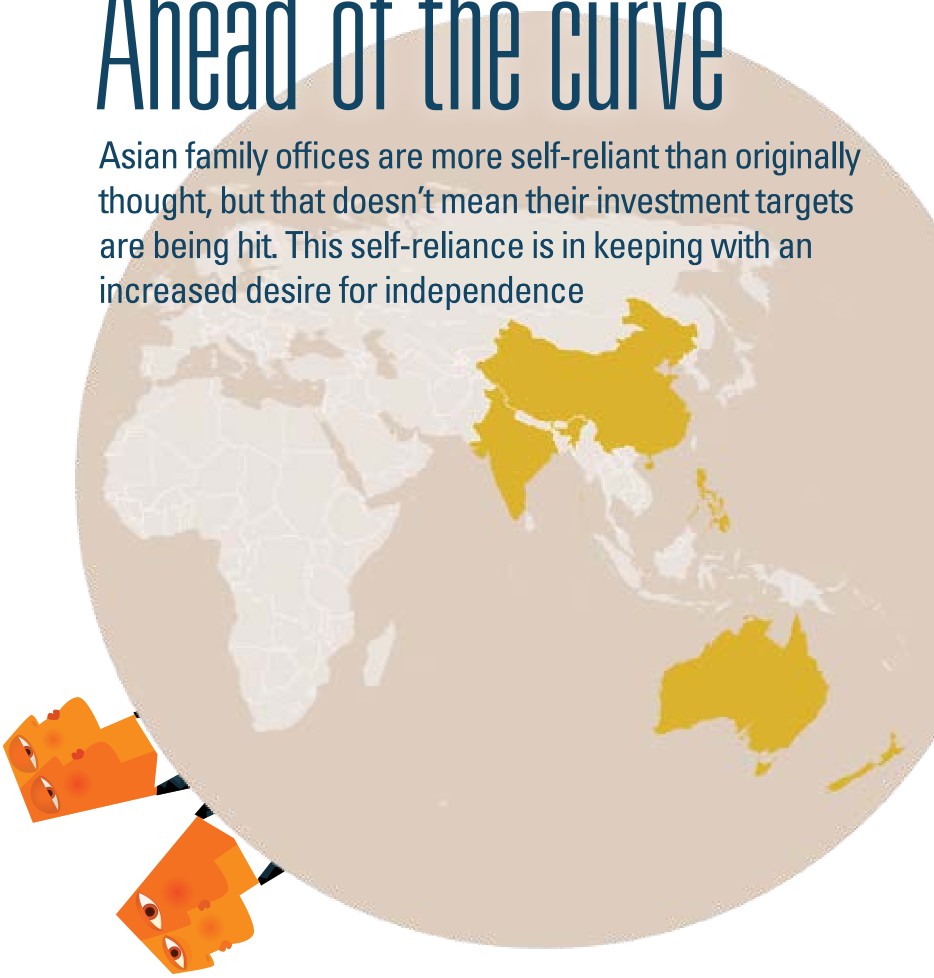
FAMILY EXPECTATIONS

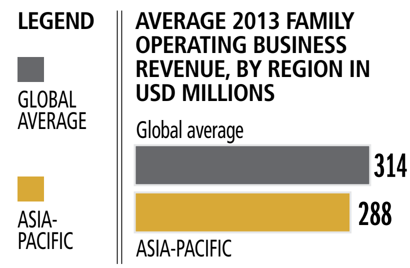
Families expect strategic asset allocation, asset implementation, risk management and structuring/tax planning expertise. Cost effectiveness is not just a given; it must be proven. The European environment is highly regulated and, in some worst-case scenarios, boundaries are defined by litigation. Therefore, family offices will likely have legal as well as accounting and investment expertise.

ASIA-PACIFIC

Ahead of the curve

Asian family offices are more self-reliant than originally thought, but that doesn't mean their investment targets are being hit. This self-reliance is in keeping with an increased desire for independence





The *Global Family Office Report 2014* has challenged a long held stereotype that family offices in Asia-Pacific rely heavily on external service providers for core functions. In fact, it has found that Asian offices spend roughly 20% less than those in Europe and North America.

According to the report, family offices in Asia-Pacific spend 46% of their total budget on external services, while those in North America and Europe spend between 63% and 70%, respectively.

Simon Foster, chief financial officer at the TY Danjuma Family Office, which manages the financial assets of the eponymous Nigerian shipping magnate, found the results unsurprising.

"Why are family offices in Asia-Pacific not big outsourcers? It comes down to wealth generation more than anything. Most business owners in the region developed their wealth fairly recently and as a result are highly entrepreneurial.

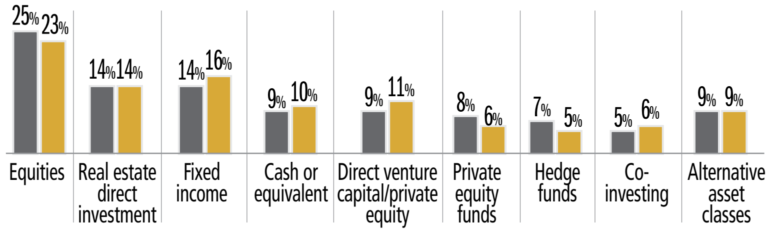
PERFORMANCE

Offices in Asia-Pacific are outperformed by their counterparts in North America and Europe, despite the concentration of offices pursuing growth strategies in 2013. A number of offices reported underperforming relative to their investment benchmark, a first in three years of Campden Wealth research on Asia-Pacific family offices. This performance was attributed mostly to significant allocations of cash (comprising a tenth of the typical office portfolio, on par with Europe and marginally higher than the global average for developing market equity and fixed income), coupled with an emphasis on longer-term, direct private equity investments.

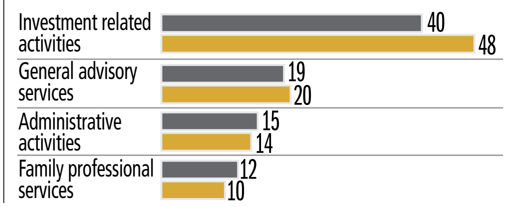
MANAGEMENT

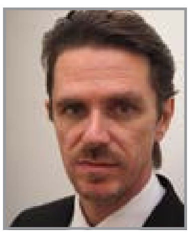
Offices in Asia-Pacific retain some of the shortest horizons globally, with two-thirds of all Asia-Pacific offices retaining portfolio horizons of less than five years. Even more significantly, only 10% of offices have an investment horizon of more than 10 years. Offices in this region display noticeably higher degrees of in-house management of all aspects of an office's investment services, as well as the study's highest degree of employee time dedicated to investment-related tasks.

TYPICAL INVESTMENT PORTFOLIO (10 MOST LIKELY ASSET CLASSES), BY REGION



AVERAGE BASIS POINTS OF AUM COST ALLOCATED PER SERVICE AREA, BY REGION





Most business owners in the region developed their wealth fairly recently and as a result are highly entrepreneurial. This means they like to have a hands-on approach

Simon Foster, TY Danjuma Family Office

This means they like to have a hands-on approach," he says.

The report found that families in Asia-Pacific have the highest degree of involvement in their family offices, particularly in strategic or planning roles. The only area where family office owners took a backseat was with tax and regulatory issues, which are handled by specialists.

Foster, who has been chief financial officer of three independent family offices, says that, despite the report's scope, family offices in the region still remain somewhat of a mystery.

"There are many chief financial officers that run successful trading companies and at the same time manage personal assets for the family members. All too often these individuals are too wrapped up in the operating business to realise that they have become a family office," he says.

Family offices with a high degree of family involvement were the most likely to pursue growth strategies and also the most likely to underperform. The results from the global study represent for the first time in three years of UBS and Campden Wealth research that Asia-Pacific family offices did not hit their investment targets. Asia-Pacific family offices returned 8% on their investment portfolio, compared to a global average of 9%.

The report also found philanthropic giving increased by 10% over the previous year. Foster thinks this trend will continue. He also believes family offices in the region will become increasingly transparent and professionalised. The impact of the global financial crisis has caused family offices to become more independent and less reliant on banks, he concludes.

"It is interesting that family office regulation is set to increase. Nowadays, just because you call yourself something else does not mean that regulators are going to ignore you. I think that holds true across the board."

COST AND STRUCTURE

At 92 basis points, Asia-Pacific offices have, on average, the highest total operating costs. Asia-Pacific stands as the only region where offices allocate over half of their total budget to investment services. While a portion of these expenditures is attributable to the popularity of growth strategies, even those offices pursuing conservative strategies spend more on investments, compared to their global counterparts. As the family office environment matures – accompanied by improvements in service provider offering and costs – offices in the region should expect cost efficiencies to improve.

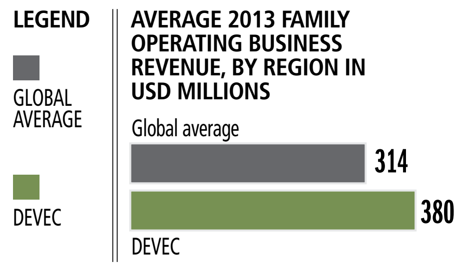
FAMILY EXPECTATIONS

Succession and governance stand as critical challenges for the evolution of the Asia-Pacific family office model and environment. Performance is expected to remain a priority, but governance models must evolve to keep pace with offices globally, evolving to ensure structures support multi-generational wealth management. High degrees of beneficiary involvement, close family networks and adviser relationships are critical as families prepare for transition in an environment where discussions of succession are stigmatised.

DEVEC

More bang for your buck

Family offices in developing regions are the most cost efficient in the industry, with governance and investments on par with their Western peers. Is this attributable to operational efficiency or how offices interact with family businesses?



The family offices of Africa, Latin America and the Middle East have the lowest operating costs in the industry, according to the *Global Family Office Report 2014*, challenging the conventional wisdom that they are costly and underdeveloped.

Despite this, many have governance structures and investment services on par with older offices in Europe and North America, with which they have far more in common than originally thought.

The report suggests that a family office in the developing market regions, managing a portfolio of $200 million, will spend around $1 million on operating costs each year. A family office in North America or Europe will spend nearly double this.

Walid S Chiniara, head of private client services at Deloitte & Touche, has served family offices for more than 15 years. He says offices in the region are cost effective because they are often intertwined with

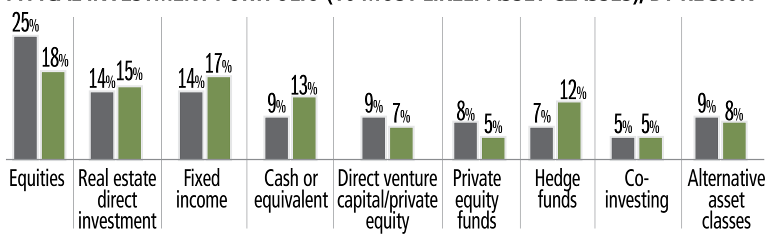
PERFORMANCE

Family offices in developing economies faced some challenges in 2013. Economic growth was generally sub-par, with asset markets under pressure amid local currency weakness. As a result, family offices from Africa, Latin America, and the Middle East, that had significant exposure to local bond and equity markets, had relatively low returns, compared with counterparts holding higher allocations of developed market assets. Based on the study's asset allocation data, it is estimated that portfolios in these regions would, on average, have produced less than 5% nominal returns in 2013. However, given significant non-liquid investments in real estate and sizeable operating companies, actual results may differ considerably from 'portfolio only' returns.

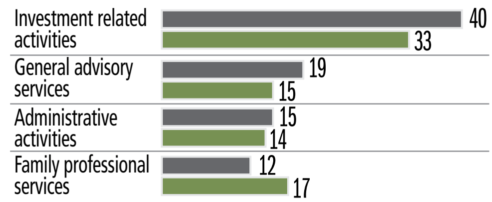
MANAGEMENT

These offices have the shortest overall portfolio horizons, perhaps attributable to local geopolitical and market instability. The scope of management is highly likely to intersect with a family-owned operating company (over 80% of DEVEC family offices covered in the survey had operating companies). Investment services managed by these offices also include the 'usual' components, such as liquidity management, investment portfolios, real estate, direct investments and private equity. Although portfolios have significant home bias, these offices display near-identical functions and processes to the wider population of offices in the global survey.

TYPICAL INVESTMENT PORTFOLIO (10 MOST LIKELY ASSET CLASSES), BY REGION



AVERAGE BASIS POINTS OF AUM COST ALLOCATED PER SERVICE AREA, BY REGION



Most business families are now conscious of the need to introduce a level of governance separate from the family business. [...] The new generation of next-gens are rising and about to enter the market. They are educated, sophisticated, and highly ambitious.

Walid S Chiniara, Deloitte & Touche

the family's operating businesses and can share costs.

"Most businesses operate either in the retail or construction industry and therefore generally pour profits back into their businesses. As a result, few have gone the extra step and set up an independent structure that manages investments related to the business," he says.

Those family businesses that do establish fully-fledged family offices, Chiniara says, are often criticised by industry veterans because they are perceived as passion projects. He says they typically have no more than two members of staff.

Chiniara added that family offices are cost effective not only because the number of employees is small, but because they rely on existing relationships with third parties in order to reduce outsourcing costs.

Other results from the study suggest that developing regions are increasingly becoming home to international family offices that are looking to take advantage of investment opportunities in emerging markets.

Chiniara says that family offices in the Middle East are on the verge of a transformation, suggesting that the next generation is likely to professionalise the industry. He says the family office industry in developing countries will look markedly different by 2025.

"Most business families are now conscious of the need to introduce a level of governance separate from the family business. They are also conscious of the need to consolidate their wealth. The new generation of next-gens are rising and about to enter the market. They are educated, sophisticated, and highly ambitious," he says.

The *Global Family Office Report 2014* concludes that further research needs to be conducted into the cost efficiencies of offices in developing regions, suggesting that the area is little understood so far.

COST AND STRUCTURE

Direct family office costs were almost 10% lower than the global average, which can be attributed to a relatively smaller proportion of 'investment services' in total costs. Family offices in the region were the most sensitive to costs from third parties. Additionally, these family offices tend to support more households, which could drive more (costly) complexity. Many offices in this region benefit from the proximity of the family office to the operating business, both in areas such as administrative and operational costs, as well as investment-related efficiencies (networks, diligence and deal flow).

FAMILY EXPECTATIONS

Families expect to manage their wealth with significant involvement of family members and where the operating company, treasury function and investment portfolios tend to be intertwined. Successful entrepreneurs will typically have assets in multiple countries beyond their home base and therefore they require and expect family office services that can cope with both local and global expertise.