LIPMAN BURGON & PARTNERS
PRIVATE OFFICE

Wealth Strategy
Family offices: the advantages of partnering with investment experts

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Entrepreneurial success and rising asset prices have catalysed significant wealth creation for many Australian individuals and families. As a result, there has been continued growth in the establishment of Family Offices as families seek a more structured approach to capital growth following liquidity events, and preserve wealth for the next generation.

Paul Burgon
Managing Partner

This growth has occurred alongside a broader maturing in the way Family Offices are managed. An industry has developed to serve Family Offices and offer outsourced expertise, from investment and wealth management to personal and cyber security and travel concierge services.

Family Offices come in varying sizes, as do the advisers who serve them. Increased competition, technological change, and an increasing desire for niche investment opportunities are changing how family offices work with wealth advisors.

For investment management, it's becoming increasingly important to look at the best ways to build or manage the multi-asset portfolios that can deliver optimal outcomes for Family Offices. Therein, there are advantages of outsourcing this to independent advisers with access to a broad range of investment opportunities and expertise.

In this paper, we explore the critical issues facing Family Offices as they decide whether to manage their investment portfolio in-house or outsource it to an external partner.

Establishing a family office

Family Offices are often formed once a family accumulates, or realises, $100 million or more in managed assets. That could be for reasons including a transition from a high-net-worth individual via an intergenerational wealth transfer, the realisation of the sale of a business or through a divorce. Family Offices are an extension of the family and bring several generations together around stated goals and values.

These offices are designed to help families leverage assets and preserve wealth and bring together legal and accounting support and investment management services. Before the decision to set up a Family Office, multiple professional partners are often providing advice, but not always in a coordinated way.

Increasingly, and with more funds at stake, the way Family Offices manage their capital has taken on a more institutional approach. And while some Family Offices choose to manage their own investments, many will hire a Chief Investment Officer to work inside the business. Depending on the size of the Family Office, the Chief Investment Officer will either have recruited an internal team, work closely with an external wealth adviser, or both.

"The primary purpose of family offices is to protect and grow wealth," says Edward Jewell-Tait, Board Advisor at Lipman Burgon & Partners. "If the wealth has come from a previous generation, then often they are set up to preserve a family legacy for future generations."

"An investment adviser adds value by providing a disciplined, unbiased and rigorous approach to investment opportunities using an agreed framework," Jewell-Tait adds. "Family values, intergenerational wealth goals and philanthropic views are all important components of this framework."

Inhouse staff versus external advisers

Family Offices must decide which services they want to focus on in-house rather than outsourcing to a third party. Historically, Family Offices in Australia have tended to bring most services in-house out of necessity or fear of giving up control over the service delivery, potential conflicts of interest, or the release of personal and financial information.

However, this approach comes at a high cost from a managerial time, complexity, scalability, and expense perspective. As a result, demand for independent services is growing, and there remain few independent wealth management firms with genuine family multi-office capabilities.

Globally, successful family offices use a value-add and core competency approach to decide which functions should be handled in-house to manage their personal and financial affairs, according to Citi Private Capital Group.[1] Whether to outsource services or resource an in-house function can be evaluated based on these criteria, among others:

Size of portfolio

Portfolio objectives including ESG investing or philanthropic activity

Access to investment talent with appropriate skills

Nature of the Family Office structure

The desire for a passive versus active role in portfolio management

Privacy and security of information across parties

Costs associated with investment management

According to Lipman Burgon & Partners Managing Partner, Paul Burgon, for a Family Office managing under $500 million of investable assets, it's potentially financially efficient to outsource the management of investments rather than pay wages for several internal staff to provide a similar function.

"To really get a very effective Family Office function, you need around three-to-five people, and you need to be able to offer them career progression opportunities. You also want to have enough funds under advice to access and originate varied investment offerings, and that can be hard to do under $500m."

"It's also salient to consider that for some Family Offices, attracting talented CIOs can be challenging unless they are large and well-resourced enough to fund a full investment function and provide career growth opportunities," says Paul Burgon.

"It's tough to build, and retain, a quality CIO function when a Family Office isn't managing a a substantial portfolio of assets," he says, adding that often broadly experienced, semi-retired advisers may take on these in-house roles and partner with their own network of advisers.

1 https://www.privatebank.citibank.com/ivc/docs/OrgDesign_Leadership_GovInsights_FamilyOffices.pdf

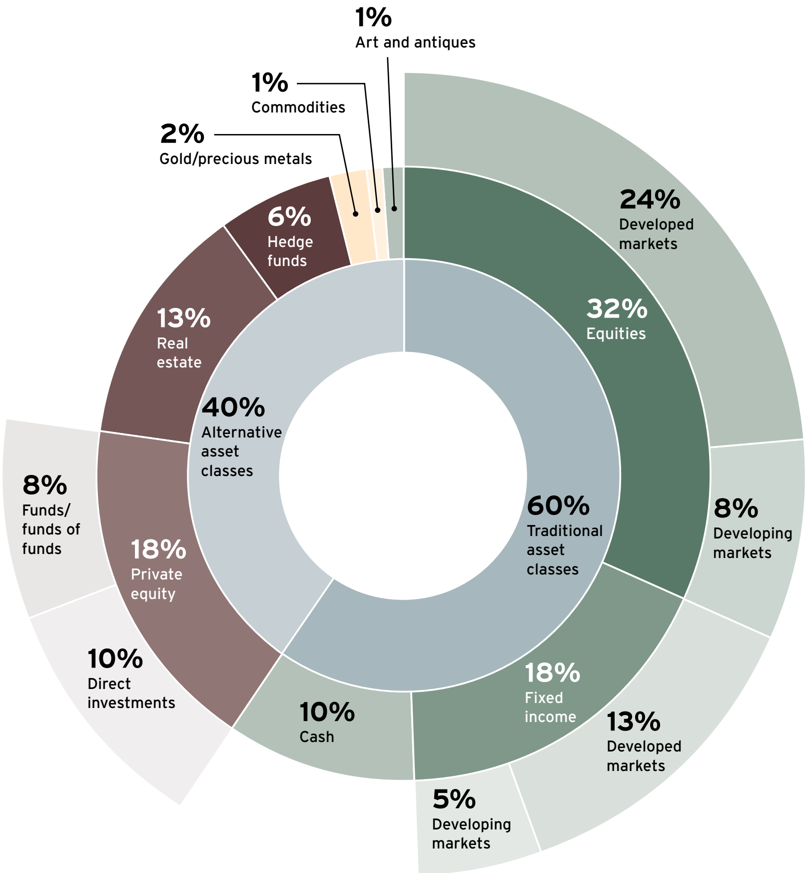
ADVANTAGES OF OUTSOURCING	ADVANTAGES OF IN-HOUSE
• Access to leading investment talent with multi-asset portfolio management expertise • Independence and discipline in setting and governing investment strategies • Resources to filter all investment opportunities in line with objectives • Capabilities to assess specialist investment opportunities • Understanding of evolving ESG and responsible investing frameworks • Efficiencies when compared to running larger internal investment teams	• Higher degree of control over investment processes • Greater privacy and security of financial information • More oversight of day-to-day CIO function

Investment management considerations

Investment management in a Family Office requires time and commitment. A range of factors influence a decision on how best to manage the investment.

Family Offices whose wealth hasn't been acquired from direct investing may have limited experience and need to be wary of the challenges. Building, executing, and managing a successful investment portfolio is a specialist skill and benefits from multi-asset portfolio management expertise. According to recent research undertaken by UBS, the strategic asset allocation of Family Office globally is diverse and having the skills to navigate many and varied asset classes will be crucial to maximising returns.

FAMILY OFFICE STRATEGIC ASSET ALLOCATION IN 2020

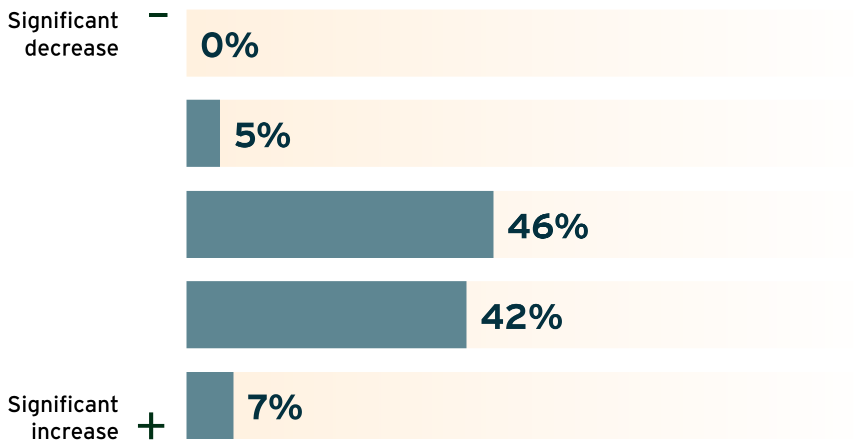


Multi-asset experience matters, says Paul Burgon, because every investment a Family Office evaluates needs to have a place within an overall investment portfolio. He says it's not uncommon to see Family Office portfolios where it's difficult to see what particular role individual investments are playing in the portfolio, as often this hasn't been considered.

"You can have a lot more discipline around how investments are looked at, selected and assessed if you outsource investment management," Paul says. "An investment adviser can act as a gatekeeper when family offices are approached because they can assess opportunities based on a set of agreed criteria and whether they fit in overall portfolio plan and structure."

This is particularly true for direct and private investing and allocations to alternatives, an area growing in popularity for Family Offices, as shown by a recent global survey undertaken by BlackRock. In addition, the option to access advisers from large institutions and investment banks is available. Still, these can come with allegiances to certain product suites and don't always offer a genuinely independent assessment of all investment opportunities.

EXPECTED ALLOCATION TO ALTERNATIVES AMONG FAMILY OFFICES IN NEXT 5-10 YEARS



Source: BlackRock Global Family Office Survey, August 2020

Aside from due diligence and portfolio building skills an independent investment adviser provides, there is a very important role to play in reporting across holdings in the portfolio and the safe custody of assets. Family Offices can require sophisticated financial reporting capabilities to report on on-platform and off-platform assets, and often across multiple asset managers.

Choosing an investment management firm

When choosing a CIO or investment advisor to manage the investment philosophy and objectives for the family, Family Offices need to define the type of investment professional that is right for them.

Families need to be mindful of a mismatch between the principal's expectations for the portfolio and the ability of the CIO or external adviser to meet those expectations.

Paul Burgon suggests considering the following:

Does the firm have pure independence in terms of the products and solutions they're going to bring?

Do they also have the capability to assess and provide advice on investments across all asset classes, and not just those approved by their investment team?

Do they have the capability to provide due diligence and advice on all the investments you may wish to consider?

Do they have a capability to articulate a clear evidence-based investment philosophy tailored to the family's requirements and a framework that can be implemented that enables every asset considered to have a place in the portfolio?

And what is becoming increasingly important is whether they can understand public and private markets, because more family office investment capital is being allocated to the private equity, venture capital and alternative investment markets.

Finally, it's imperative to ask if there is a strong connection and alignment with the values of the advisory firm you intend to engage as the relationship may last through multiple generations.

Lipman Burgon's approach to portfolio management

Paul Burgon further explains that running a truly multi-asset investment portfolio requires a specific skill set and the ability to conduct analysis across asset classes and understand portfolio management.

Lipman Burgon & Partners utilises the Total Portfolio Approach (TPA) to asset allocation favoured by large superannuation and sovereign wealth funds. Unlike traditional strategies that combine asset classes with low or negative correlations, TPA takes a more flexible approach, where every investment decision is based on its own risk and return merits and influence over total portfolio objectives.

This differs from Strategic Asset Allocation (SAA), which relies on asset class benchmarks and often suggests a 60/40 balanced portfolio of equities and fixed income as a classic defensive position.

TPA is a more flexible and holistic approach to portfolio construction. It enables portfolio diversification through the risk factors of each investment rather than through the batching of asset classes to target weightings. It also allows for today's more complex investment environment, with alternatives and private investing playing a much more significant role and interest rates at record lows, leaving government bonds and cash barely investable.

Lipman Burgon has invested in its own research capability over the past decade and values having dedicated research professionals in-house, alongside financial advisers and relationship managers. The firm has sought out professionals with institutional credentials from top global institutions to bring these credentials to Family Offices.

"You really need an institutional capability to drill down on potential portfolio risk factors and ensure you have proper diversification," says Paul Burgon. "It's important when you're looking to outsource investment management that you understand an adviser's processes and their due diligence and governance capabilities."

Ensuring deep alignment

From the outset, our advisers spend time understanding our Family Office clients' investment objectives both from a risk and return perspective but also how interest, passions and family values are expressed within the portfolio.

Typically, the portfolio will be used to assist in securing and building multigenerational wealth, and it may have an impact or ESG values overlay or other investment philosophies such as alternative energy or medical research.

Edward Jewell-Tait says family offices have unique needs, which are not easily met in an initial meeting. He adds that the quality of advisory services has significantly improved in Australia in recent years. "Using advisors is a big leap of faith, Edward says. "You've got to trust them and understand that they are behind you."

So, rising asset prices and the realisation of entrepreneurial success continue to support significant wealth creation. More wealthy families that are beneficiaries of these trends are establishing Family Offices to take a more unified and disciplined approach to investment management.

However, there are a range of considerations whether a Family Office decides to have an in-house CIO or outsource that function. Having the expertise to originate and evaluate multi-asset portfolio opportunities, the visibility over the portfolio holdings, and crucially, the objectivity to make investment decisions that truly align with the family's values and principles, can be crucial determinants of performance and success.

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