# Raising Capital from Single-Family Offices: Considerations for Financial Firms

An extensive study of the evolving relationship between the single-family office and investment management sectors.

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Rothstein Kass

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Originally created as investment tools for the ultra-wealthy, private equity funds and hedge funds have thrived by maintaining investment focus even as they continually adapt to meet the needs of an evolving investor base. Over the past decade, inflows of institutional capital have propelled the alternative investment community across new thresholds for assets under management and supported recovery following the market meltdown and ensuing economic crisis. It is hardly surprising that alternative products hold growing appeal, particularly to pension funds seeking talented investment managers to help them overcome deep funding shortfalls. Through our proprietary research, Rothstein Kass was among the first to document the trend toward the “institutionalization” of the alternative investment industry.

The perspective gained through our award-winning work with the alternative investment community has offered Rothstein Kass exceptional insight into the fundamental, but sometimes subtle, changes that are occurring within the space. From our vantage point, it is clear that institutionalization is not defined strictly by capital sourcing, but represents a lasting change to how managers must approach the business to create a framework for sustainable performance. The push for greater transparency has been driven by demand, as investors have increasingly looked beyond performance in considering allocations. Again, institutional investors have led the charge. High-net-worth individuals and families are also becoming more sophisticated in their investment approach.

Pensions, endowments and other institutional investors typically have the resources required to thoroughly screen managers to ensure alignment with long-term objectives and build diversified portfolios. High-net-worth individuals must be more targeted in their assessments, even as they are presented with a greater range of investment options than ever before, from both new funds, ETFs and alternative investment replication funds. With so many aspects of their long-term planning tied to their investment portfolios, more high-net-worth families are finding that single-family offices represent the ideal structure for implementing a cohesive wealth management strategy. As a result, the Executive Director is wielding greater influence over investment allocations, and often acts as a gatekeeper to the vast pools of investment capital the family is seeking to deploy. Our latest survey of investment managers finds that they are recognizing the potential of the family office sector and are increasingly seeking to source capital from the sector. Family offices share many characteristics with pension fund investors, and these similarities are actually serving to reinforce the trend toward the institutionalization of the industry. Most importantly, they share an imperative to allocate to managers that maintain the right mix of investment management and operational staff to promote and maintain institutional-quality best practices.

Our “Raising Capital from Single-Family Offices” report draws on the insights and experiences of our Private Equity Practice and Family Office Group, as well as Forbes Insights and Forbes Private Capital Group, to shed light on the relationship between family offices and the investment community. We hope that you will find the following report thought-provoking and insightful, and encourage you to contact us to discuss our findings.

Sincerely,

Thomas Angell

Tom Angell
Principal-in-Charge of the Private Equity Practice
Rothstein Kass

## Key Themes

- Single-family offices are increasingly appealing sources of capital for investment managers and investment bankers.

- Because single-family offices manage the financial and personal affairs of an individual wealthy family and offer an array of expertise, the Executive Director function is critical.

- Our research indicates that roughly 85% of single-family offices currently invest in hedge funds, and nearly half invest in private equity vehicles. A sizeable majority expect to increase allocations to alternative products in 2011.

- With competition for investment dollars expected to further intensify, investment managers and investment bankers are adopting a consultative approach, encompassing single-family office investment orientation, objectives and "professional ecosystems."

## Research

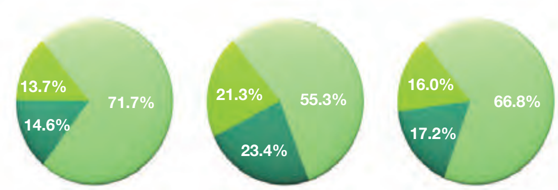
In the first quarter of 2011, we surveyed the Executive Directors of 151 single-family offices on an array of topics. To be included in this sample, the single-family offices had to have hedge fund or private equity investments. Where applicable, we have also referenced a number of prior research initiatives to provide a more complete picture of the sector.

### The Appeal of Single-Family Offices

Over the past five years, our research has indicated that family offices are increasingly appealing sources of capital to hedge funds, private equity funds and investment banks. Our surveys of these communities have suggested that there are three critical forces driving this emerging trend. Quite simply, single-family offices typically represent vast pools of wealth seeking investment return. As demand for integrated wealth management services has increased, the rapid proliferation of the family office model has deepened the sector's resources. Finally, single-family offices tend to have long-term investment horizons that make their assets "sticky," helping to promote fund stability.

Rothstein Kass' "2011 Hedge Fund Outlook," featuring the results of our annual survey of hedge fund managers, for example, found that nearly 70% believe that family offices will be an important source of new capital in 2011 (Exhibit 1). Hedge funds reporting assets under management (AUM) below $500 million (70%) were more likely to see family offices as an important source of funds, when compared to hedge funds with $500 million or more in AUM (55%).

**Exhibit 1: Family offices will be an important source of new capital in 2011**




| | <$500M | $500M+ | Weighted Average |
|---|---|---|---|
| Agree | 71.7% | 55.3% | 66.8% |
| Disagree | 14.6% | 23.4% | 17.2% |
| No opinion/don't know | 13.7% | 21.3% | 16.0% |

N = 313 hedge fund managers

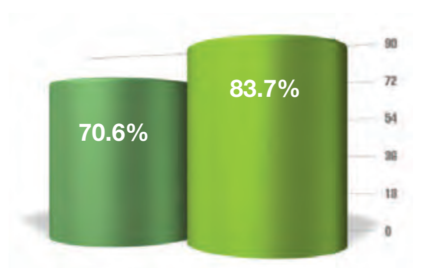
Source: 2011 Hedge Fund Outlook: A Brighter Day

**"Interest in sourcing capital from the family office sector is generally increasing, but is especially strong among emerging hedge fund managers. In the short-term, the financial crisis has created a preference among institutional investors toward allocations to larger, established hedge funds. As a result, many larger funds are disproportionately benefiting from asset flows from pension funds seeking to overcome funding shortfalls through greater allocations to the alternative investment industry," said Rick Flynn, a Principal and Head of the Family Office Group at Rothstein Kass. "Renewed interest from seed capital operations has helped to balance the scale, but competition for funds is furious. Many smaller funds believe allocations from the family office sector will complement more traditional fundraising efforts."**

Alternative investment industry interest in raising capital from family offices is not limited to the hedge fund community. In a 2008 survey of private equity managers, 71% reported that single-family offices would be a significant source of new capital (Exhibit 2). Two years later, nearly 85% of managers believed this would be the case.

**"The rich diversity of the private equity sector provides investors considering allocations with a nearly limitless range of options and strategies. However, the sheer number of funds in operation has produced consistently intense competition for assets. As a result, private equity firms have become adept at differentiating their funds through the implementation of niche strategies. The ability to clearly communicate their value propositions to investment audiences that they have developed will serve these firms well as they increasingly target single-family offices as significant sources of new capital," said Tom Angell, Principal-in-Charge of the Private Equity Practice at Rothstein Kass.**

**Exhibit 2:**
Single-family offices are significant sources of capital for private equity funds

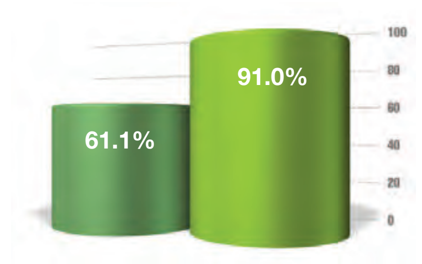



| | |
|---|---|
| 2008 | 70.6% \| (N = 126) |
| 2010 | 83.7% \| (N = 147) |

In addition to hedge funds and private equity funds, we have observed that middle-market investment banks are also increasingly looking to single-family offices as important sources of new investment capital (Exhibit 3). In fact, from 2007 to 2009, the relative proportion of middle-market investment bankers looking to raise money from single-family offices jumped about 50%.

**"In recent months, there have been a number of transactions underwritten by investment banks that have included substantial financing from individual investors through the family office structure. Activity to date has been concentrated in the real estate sector, but early successes are fueling interest across industry segmentations. We've seen increasing interest in direct investment from clients ranging from athletes and entertainers to entrepreneurs," said Mark Hutchison, a Principal in the Family Office Group at Rothstein Kass. "The family office model is effectively positioned to assist in both sourcing investment opportunities and evaluating the risks in the context of broader financial and lifestyle objectives. Many are relying on their deep networks of relationships to forge informal alliances with investment banks that have recognized the benefits of working with the family office sector."**

**Exhibit 3:**
Single-family offices are significant sources of middle-market investing




| | |
|---|---|
| 2007 | 61.1% \| (N = 180) |
| 2009 | 91.0% \| (N = 156) |

From our research, it's evident that a growing number of investment professionals are considering single-family offices attractive sources of capital. Individual imperatives are as diverse as the alternative investment community itself. However, as noted, there are three unifying themes:

- Single-family offices have significant assets to invest.
- More and more single-family offices are being established.
- Single-family offices tend to have long-term investment horizons.

Our research provides greater insight into these motivations.

**Single-family offices have significant assets to invest.** The most overwhelming reason behind growing interest in sourcing assets from single-family offices is also the most basic. Single-family offices oversee allocations of sizeable pools of investment capital. In our most comprehensive and largest study of family offices, conducted in 2009, we found that the mean number of investable assets of 298 single-family offices was $236.4 million (Exhibit 4). With the median reported at $127.9 million.

In 2011, the mean investable assets of this sample of single-family offices have grown to more than US$400 million (Exhibit 5). Median investable assets approached $240 million. It is also notable that in 2011, single-family offices surveyed were directing meaningfully more investable assets than the sample of single-family offices in our previous study (see The Family Office: Advising the Financial Elite, 2010).

The higher levels of investable assets revealed in our 2011 survey of single-family offices are in part due to improvement in the financial market over the past few years. In addition, our 2011 research was restricted to single-family offices investing directly in hedge funds or private equity funds. And, there are more and more single-family offices exceeding US$1 billion in investable assets.

**"As the family office sector has emerged as a viable source of capital, many investment managers have become more active in their approach to sourcing these assets. This has greatly expanded the range of investment options available to family office advisors. Based on their in-depth knowledge of family planning objectives, single-family offices are well-equipped to assess the complexity, investment horizon, and risk profiles of available opportunities to make informed decisions regarding allocations," said Bruce H. Rogers, Chief Brand Officer and Managing Director at Forbes Insights. "For investment managers, greater across-the-board interest in the family office sector will promote intense competition for capital. Those that adopt a consultative approach to interactions with the sector will be the most successful in fund-raising efforts."**

**Exhibit 4:**
Investable assets of single-family offices 2009


| | |
|---|---|
| Mean | US$236.4 |
| Median | US$127.9 |

N = 298 single-family offices
Source: The Family Office: Advising the Financial Elite (2010)

**Exhibit 5:**
Investable assets of single-family offices 2011


| | |
|---|---|
| Mean | US$415.7 |
| Median | US$239.5 |

N = 151 single-family offices

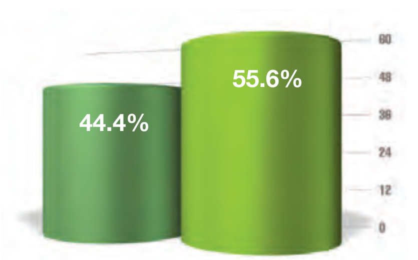
Another factor in the amount of investable assets under management at single-family offices is the official primary location of the structure. The majority of the single-family offices surveyed are based outside of the U.S. We have regularly found that non-U.S. based single-family offices control greater wealth in relation to their U.S. counterparts (see The Family Office: Advising the Financial Elite, 2010).

As super-rich families across the globe increasingly favor a family office model, the amount of money these structures will oversee and manage will logically multiply. Anecdotal evidence based on consulting with the high-net-worth populations has suggested self-made super-rich individuals are more intent on establishing family offices, and that there has been a steady increase in the amount of investable assets these individuals report at inception.

In this sample, a slight majority of the single-family offices were non-U.S. (Exhibit 6). This means that their "official" domicile is outside the United States. However, many of these single-family offices maintain operations in multiple locations.

**"Though there are subtleties dictated by geography, the appeal of the family office seems to be universal. In fact, the model is thought to be even better established overseas, particularly in Europe, where single-family offices have often served wealthy families across several generations. At this stage, the sector's growth in the U.S. is outpacing international expansion. At the same time, globalization trends have compelled some family office providers to pursue strategic alliances with foreign entities to create 'outpost' family office operations," said Mr. Flynn.**

**Exhibit 6:**
Official location of the single-family office




| | |
|---|---|
| US | 44.4% |
| Non-US | 55.6% |

N = 151 single-family offices

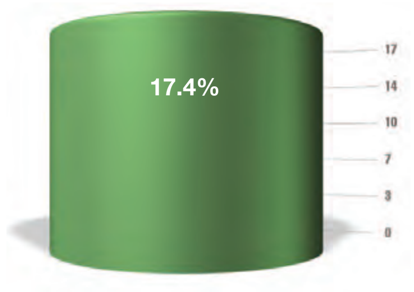
More and more single-family offices are being established. Protecting the privacy of their high-net-worth clients is of paramount importance to the family office provider, frequently driven by the client's own desire to preserve anonymity. Moreover, single-family offices are not typically registered as advisors with regulatory agencies, making it difficult to determine precisely how many single-family offices are currently in existence. The rapid pace of proliferation and the varying notions of what services a family office operation should encompass have also made it more challenging to get a true measure of the sector's scope.

Still, there are many signs indicating exponential growth in both the number and wealth of single-family offices, including statistics regarding latent interest in family office formation. For example, in a study of 108 jet owners, we found that only 8.3% presently have established single-family office operations. However, of those that do not, nearly 20% reported that they are very interested in establishing a single-family office (Exhibit 7).

Just how many of the super-rich actually follow through on their desire to create a family office will be known only in hindsight. Still, our experience with these communities suggests that the considerable interest reported will translate into a meaningful increase in family office launches in coming years, greatly increasing total assets under management by the sector.

**"The influence of single-family offices is rising on both an individual advisor and aggregate basis. Sector assets under management have continued to grow, with the pace of proliferation intensifying in the years following the global market crisis. During that period, we observed a short-term retreat from investment markets, as many wealthy families experienced declining net worth that contributed to liquidity concerns. Over the longer term, this market volatility has served to illuminate the benefits of a more comprehensive approach to wealth management strategies. Because they typically treat investment management, lifestyle and estate planning functions as interrelated aspects of a unified plan, the single-family office model has become even more popular since the crisis," said Cheryl B. Rogers, Senior Vice President at Forbes Private Capital Partners.**

**Exhibit 7:**
Jet owners very interested in establishing a single-family office




Very interested 17.4%

N = 99 jet owners | Source: The Family Office: Advising the Financial Elite (2010)

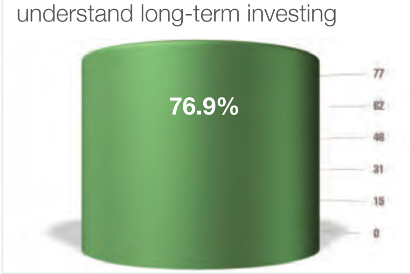
Single-family offices tend to have long-term investment horizons. Another attractive attribute of the sector is that most single-family offices tend to have multi-year investment horizons. As one Chief Investment Officer overseeing more than $1 billion in assets for a wealthy family noted, he often evaluates potential allocations not in terms of years or even decades. Instead, for him and many others in his position, investment management is a multi-generational concern.

This approach is attractive to most alternative investment managers, but is especially appealing to middle-market investment bankers (Exhibit 8). In 2009, of 156 middle-market investment bankers that identified single-family offices as key sources of new funding for deals, more than three-quarters also said that their long-term investment orientation was a critical reason to look to the sector for capital.

Investors with a long-term time horizon represent what is commonly called "sticky money." For hedge funds and private equity firms, maintaining a stable investor base diminishes concerns that market fluctuations will drive redemptions. Even so, investment managers and investment bankers alike are well-served by maintaining an open and ongoing dialogue with family office investors to ensure ongoing alignment of objectives and risk tolerances.

**"For many investors, the years preceding the market meltdown produced a period of steady investment returns that obscured the focus on long-term planning. During that time, essentially all money appeared to be sticky. This came to a crashing halt in 2008, of course, as many hedge funds were forced to contend with a spate of withdrawals from high-net-worth families liquidating positions to address short-term financing challenges," said Howard Altman, Co-CEO and Principal-in-Charge of the Rothstein Kass Financial Services Group. "As conditions have normalized, it's fair to speculate that some of these investors might now regret the decision to reduce allocations to alternatives products. That comes as little consolation to fund managers that were forced to liquidate during the worst of the crisis. In the aftermath, the industry has responded by renewing its focus on alignment of interest with investors. Investors, too, have become more thorough in their due diligence processes, placing a greater emphasize on factors like general partner investment and operational best practices at fund complexes."**

**Exhibit 8:**
Strongly believe single-family offices understand long-term investing




Long-term investors 76.9%

N =156 middle-market investment bankers (2009)

**What is a Single-Family Office?**
Quantifying investment management interest in raising capital from single-family offices has again proven to be easier than characterizing the sector's participants. Even after identifying some of the key motivations for investment managers and investment bankers in sourcing capital from single-family offices, definitional challenges remain. Some operations are essentially functioning as single-family offices without applying that designation. Others are branded as family office structures, but function as a traditional investment advisory firm. For example, one industrialist we spoke with insisted that he did not employ a family office model. More extensive polling indicated that within his corporation, however, he maintains a subsidiary that performs and operates just like a single-family office structure. While he does not define this subsidiary as a single-family office, it meets all the criteria of a single-family office we use to define one.

The lack of consensus surrounding family office characteristics is indicative of the range of approaches applied. For our research purposes, we rely on the most concise and encompassing definition of a single-family office available—an organizational structure that manages the financial and personal affairs of one wealthy family. Within this framework, there's extensive disparity when it comes to the array of services and expertise single-family offices provide their clients. Consequently, the universe of single-family offices tends to be more heterogeneous than homogeneous.

With that disclaimer, broadly speaking, single-family offices provide two principal categories of expertise—wealth management and support services (Exhibit 9). Under the heading of wealth management resides investment management, advanced planning and pri-

**Exhibit 9:** The array of family office services

| Wealth Management | Support Services |
|---|---|
| **Investment Management**<br>**Traditional Asset Management**<br>■ Asset allocation<br>■ Manager selection<br>■ In-house investments<br><br>**Alternative Investments**<br>■ Hedge funds<br>■ Private equity<br><br>**Advanced Planning**<br>Estate planning<br>Asset protection planning<br>Wealth enhancement strategies<br><br>**Private Investment Banking**<br>Buying and selling interests in businesses and other assets<br><br>**Capital Raising**<br>■ Sourcing bank loans<br>■ Sourcing investors | **Administrative**<br>Data aggregation<br>Bill paying<br>Tax preparation or coordination<br>Acting as the day-to-day CFO<br><br>**Lifestyle**<br>Family security<br>Concierge services<br>Medical concierge<br>Philanthropic advisory<br>Formal family education<br>Managing fine art/collectibles<br>Property management<br><br>Source: The Family Office: Advising the Financial Elite (2010) |

vate investment banking. Support services typically include, but are not limited to, administrative and lifestyle services.

**"Within the U.S. investment advisory market, widespread aspiration to be associated with the family office phenomenon has contributed to disparate notions of precisely what the model should entail. By combining wealth management and support services under the auspices a single-family office, high-net-worth families have gained a greater appreciation of how alternative investment allocations can dovetail with advanced planning functions from philanthropic activities to asset protection strategies, helping wealthy families preserve their legacies and effectively structure generational wealth transfer," said Mr. Flynn.**

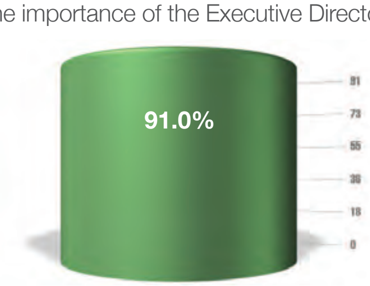
Single-family offices often amass impressive collections of talented professionals with a broad array of professional expertise. At the center of the advisory team sits an individual responsible for maintaining plan cohesion to ensure the success of the venture. In most cases, this role is performed by the Executive Director. In addition to oversight responsibility for day-to-day operations, Executive Directors often play a crucial role in the investment management process, serving as a gatekeeper to the family relationship. As a result, when it comes to raising capital from single-family offices, investment managers and investment bankers must be cognizant that the Executive Director will help to elect allocations, either directly, or in conjunction with family office investment professionals, such as the Chief Investment Officer.

Given their scope of influence, it is not surprising that more than nine out of ten Executive Directors of single-family offices report that they are critical to the effectiveness of the operation and success of the family office (Exhibit 10).

As more of the very wealthy establish single-family offices and as existing single-family offices seek to upgrade their capabilities and performance, competition for Executive Directors is likely to further intensify. This has allowed Executive Directors to be very selective in evaluating positions and long-term career options. In working with single-family offices on the compensation of Executive Directors and other key personnel, we're finding both the Executive Directors and the wealthy families are increasingly willing to adopt a participatory approach to compensation. By exploring more creative payment models and innovative versions of deferred compensation, wealthy families are able to offer greater total compensation to Executive Directors – provided that they deliver.

**"The benefits of adopting a unified approach to wealth management have become more broadly apparent, leading to growing demand for family office support services. More than ever before, wealthy families rely on family offices to provide insight into a range of non-investment initiatives, including bill paying, personal security and even adoptions. Many single-family offices were originally structured around the investment management functions and have maintained that focus by outsourcing ancillary functions to third-party service providers," said Mr. Flynn. "As a steward of the family brand, the Executive Director acts as the quarterback, making sure all team members are working toward a common goal and reconciling conflicting objectives."**

**Exhibit 10:**
The importance of the Executive Director




| | |
|---|---|
| Critical to the effectiveness of the single-family office | 91.0% |

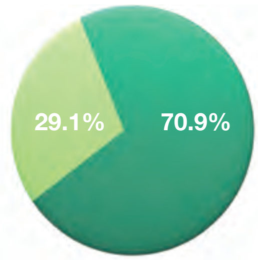
N = 298 single-family offices | Source: The Family Office: Advising the Financial Elite (2010)

**Investment Preferences in 2011**
Over the years studying family offices, we have developed a number of different segmentation criteria. One very powerful segmentation model is based on psychographics and distinguishes between family offices that are Wealth Creators and those that are Wealth Preservers.

Wealth Creators are charged with enhancing or increasing the fortunes of the underlying family. In contrast, Wealth Preservers are focused on ensuring the safeguarding of the underlying family's wealth. In this study the greater majority of the single-family offices can be classified as Wealth Creators (Exhibit 11).

**"Many single-family offices pursue investment diversification strategies that blend aspects of both wealth creation and wealth preservation. However, most are clearly weighted toward one overarching philosophy that is often dictated by individual family circumstances. The good news for both populations is that growing interest from institutional investors has dramatically increased the range of investment options offered by the alternative investment community. At this stage the industry is sufficiently diverse to offer suitable investment options for investors of nearly all risk tolerances. Wealthy clients nearing retirement, for example, are more likely to pursue a wealth preservation strategy to guard against fluctuations that would negatively impact their lifestyle or restrict the generational transfer of wealth. They tend to gravitate toward alternative products that offer annuity-like returns or hedge more aggressive positions," said Ms. Rogers.**

**Exhibit 11:**
Segmenting the single-family offices

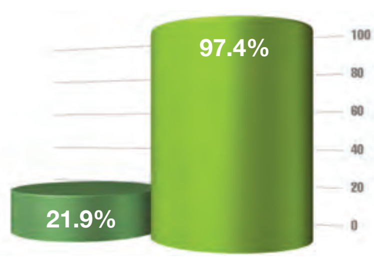



| | |
|---|---|
| Wealth Creators | 70.9% |
| Wealth Preservers | 29.1% |

N = 151 single-family offices

When it comes to managing the family's investable wealth, nearly all these single-family offices are using outside money managers and related professionals (Exhibit 12). At the same time 22% have also developed internal capabilities to manage money. From these statistics, it is clear that single-family offices are almost universally relying on external investment professionals even as almost a quarter of them are selectively managing portions of their portfolios in-house.

**Exhibit 12:**
Internal vs. external investment management



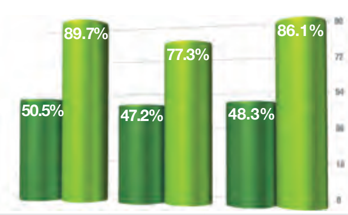

| | |
|---|---|
| Internal | 21.9% |
| External | 97.4% |

N = 151 single-family offices

For these single-family offices, hedge funds have a very strong appeal with a little more than 85% using these investment vehicles (Exhibit 13). About half of the single-family offices are investing in private equity either through funds or directly. Wealth Creators are proportionately more inclined to place assets into hedge funds and private equity.

**"A sizeable majority of the firms participating in our research reported that they are geared toward wealth creation, with many high-net-worth families seeking to recoup wealth eroded during recent periods of market weakness. These investors tend to be relatively less risk averse than those pursuing wealth preservation strategies. However, they are similar in that the success of the investment management functions greatly impacts outside interests from charitable activity to family spending. Building a skilled family office team will help these investors to confidently pursue these objectives in accordance with established risk tolerances, rather than chase returns," said Mr. Rogers.**

**Exhibit 13:**
Current use of alternatives




| | Wealth Creators | Wealth Preservers | Weighted Average |
|---|---|---|---|
| Private equity | 50.5% | 47.2% | 48.3% |
| Hedge funds | 89.7% | 77.3% | 86.1% |

N = 151 single-family offices

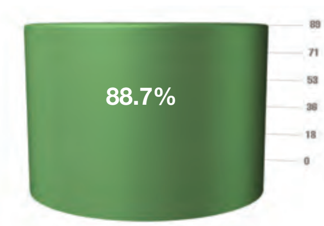
Looking ahead, nearly nine out of ten of the single-family offices anticipate placing additional monies into hedge funds (Exhibit 14). This is much more the case among Wealth Creators compared to Wealth Preservers (Exhibit 15).

Almost 70% of the single-family offices surveyed are inclined to put money into private equity in 2011 (Exhibit 16).

Again, this is more the case with Wealth Creators compared to Wealth Preservers (Exhibit 17).

**"Perhaps due in part to the fact that our research was restricted to single-family offices reporting alternative investment positions, participants reported exceptionally strong intent to increase allocations to alternative products in the months ahead. Because these family offices have often directly benefited from the quick and ongoing recovery in the alternative investment space, it was not overly surprising that they would now be considering greater concentrations. It's reasonable to expect that single-family offices with no past alternative investment sector experience will be somewhat less likely to consider allocations," said Ms. Rogers. "Anecdotally, single-family offices with prior alternative investment exposure were also more likely to maintain investment focus during the crisis, as hedge fund and private equity investment mitigated downside loss in relation to broader markets."**

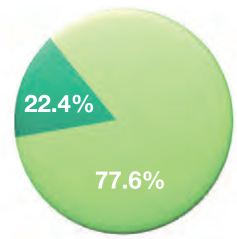
**Exhibit 14:**
Highly likely to place additional monies into hedge funds in 2011




| | |
|---|---|
| Highly likely | 88.7% |

N = 151 single-family offices

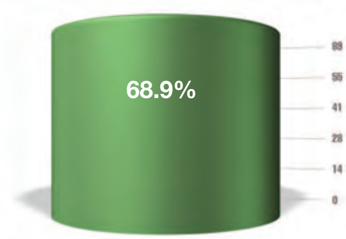
**Exhibit 15:**
Highly likely to place additional monies into hedge funds by segment




| | |
|---|---|
| Wealth Creators | 77.6% |
| Wealth Preservers | 22.4% |

N = 134 single-family offices

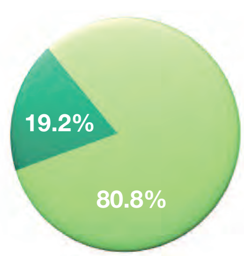
**Exhibit 16:**
Highly likely to place additional monies into private equity in 2011




| | |
|---|---|
| Highly likely | 68.9% |

N = 151 single-family offices

**Exhibit 17:**
Highly likely to place additional monies into private equity by segment




| | |
|---|---|
| Wealth Creators | 80.8% |
| Wealth Preservers | 19.2% |

N = 104 single-family offices

For those single-family offices inclined to increase allocations to hedge funds, long/short equity is currently the most appealing strategy (Exhibit 18). This is followed by distressed investing and then, arbitrage. Beyond these areas, there is no apparent consensus as to the most attractive options. Instead, single-family offices seem to be interested in more than one hedge fund style and that there's a dispersion of interest among the various styles.

**"Even during the peak of market volatility, hedge funds functioned as intended, losing less, on average than industry benchmarks. Still, the fact that the sector failed to generate positive returns came as a surprise to some investors who had become accustomed to the outsized returns generated during the preceding period of sustained economic growth. As capital returns to the alternative investment industry, many single-family offices continue to incorporate these products as critical elements of their wealth preservation strategies. However, it's clear from our research that steady improvement in the global economy has created opportunity that has most single-family offices focused on wealth creation. Hedge funds were among the largest beneficiaries of short-term equity market recovery, and single-family offices report that they will increase allocations to long/short equity funds in the months ahead. They are also indicating greater interest in distressed investment strategies, another area poised to offer strong returns in the near- to intermediate-term," said Mr. Altman.**

**Exhibit 18:**
Hedge fund strategy preferences

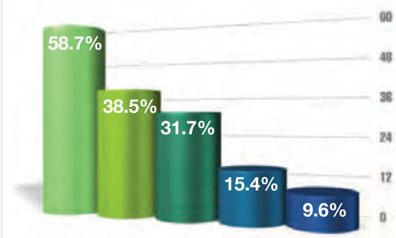
| | |
|---|---|
| Long/short equity | 53.0% |
| Distressed | 48.5% |
| Arbitrage | 32.8% |
| Managed futures | 25.4% |
| Sector | 23.9% |
| Global macro | 24.6% |
| Emerging markets | 20.9% |
| Infrastructure | 19.4% |
| Event driven | 19.4% |
| Market neutral | 14.9% |

N = 134 single-family offices

When it comes to what types of private equity investments, the single-family offices are most interested in "established companies" (Exhibit 19). The next most attractive type of private equity investment is mezzanine financing followed by second-round financing. Only about 15% of the single-family offices interested in private equity investing are interested in start-ups and fewer still are interested in management buy-outs. All in all, when it comes to private equity, the tendency in this sample of single-family offices is to gravitate to less risky private equity investments.

**"The decline in private equity transactional activity was not caused by a lack of attractive investment opportunities, but rather, was a result of market factors, including less favorable terms for investment capital and disagreement with acquisition targets regarding underlying asset values," said Mr. Angell. "As consistent with the industry profile, private equity firms continue to exhibit a strong preference for investment in established businesses, and are increasingly finding opportunity among the middle market business community."**

**Exhibit 19:**
Private equity preferences




| | |
|---|---|
| Established companies | 58.7% |
| Mezzanine financing | 38.5% |
| Second-round financing | 31.7% |
| Start-ups | 15.4% |
| Management buy-outs | 9.6% |

N = 104 single-family offices

### Caveat

When considering the investment preferences of rapidly evolving industries such as the single-family office sector, it is important to remember that survey research essentially provides a snapshot of prevailing trends. Investor preferences are often influenced by investment decision-making processes at the single-family office, which takes into account the amount of authority the Executive Director and/or the Chief Investment Officer wield.

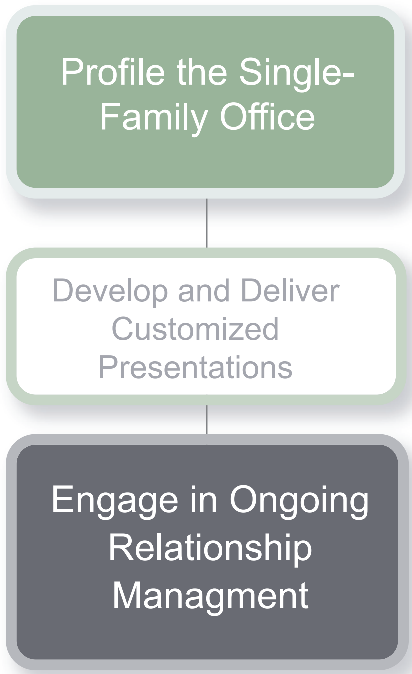
### A Consultative Approach

Bearing in mind the trends in the family office world, it's apparent that investment professionals of all shades and stripes will increasingly be considering, if not actively looking for, investors among the ranks of the single-family offices. As the attractiveness of single-family offices as investors grows arithmetically, the competition for their investment dollars will probably grow geometrically. This will mean that investment managers and investment bankers need to be highly consultative if they are to succeed in generating capital flows from single-family offices.

The consultative approach, in this environment, encompasses three basic components (Exhibit 20). Central to this approach is profiling the single-family offices to understand: (1) their investment orientation, (2) the roles, responsibilities and professional objectives of the Executive Directors, and (3) the professional ecosystem of each single-family office. Being consultative also entails creating customized explanations of offerings as well as continuously managing the relationship.

The consultative approach is interactive and ongoing. Based upon the insights developed in profiling the single-family office, the investment managers or investment bankers can construct customized explanations of their offerings and develop a framework for the continuous management of the relationship. The most effective financial firms will perpetually adjust their profiles of single-family offices, modifying their presentations and consistently reevaluating the needs and objectives of their investors.

**Exhibit 20:**
Being consultative




When it comes to the consultative process, we regularly find the greatest weakness among financial firms is in their profiling. At this stage, only a very few investment managers and investment bankers are essentially just pitching product. The conventional and pervasive approach of investment managers and investment bankers targeting single-family office assets is to offer a generic pitch focusing on their own capabilities. While the quality of the offering may be exceptional, it's often not enough. The first step in developing a consultative approach is profiling, a process we will address in greater detail.

The Profiling Process. In assessing single-family offices there are a number of areas that investment managers and investment bankers need to consider. Three of the most important ones are:

- Discerning the investment orientation of the single-family office.
- Identifying the roles, responsibilities and professional objectives of the Executive Director.
- Mapping out the professional ecosystem of the single-family office.

Discerning the investment orientation of the single-family office. To both determine the viability of their offerings as well as know how to position said offerings, investment managers and investment banks must develop an understanding of the investment orientation of the single-family offices. Some of the questions that should be addressed during this phase include:

- Is the single-family office a Wealth Creator or a Wealth Preserver?
- What experience does the single-family office have with various types of investment?
- How are investment decisions made at the single-family office?

What so very few investment professionals understand is that if a single-family office's investment orientation is not aligned with the investment products offered, investment bankers and/or investment managers should move on. It's highly unlikely that the investment managers or investment bankers will convince the Executive Directors and Chief Investment Officers at the single-family offices to alter strategies that were developed with the high-net-worth family's long-term objectives in mind, especially if these strategies have been successful.

Recognize the roles, responsibilities and professional objectives of the Executive Director. We noted that the Executive Director is regularly a linchpin professional at the single-family office. The Executive Director is often the gatekeeper to investment managers and investment bankers and determines which ones will be granted access to the family's investment capital. Even among single-family offices that employ a Chief Investment Officer and/or in-house investment analysts, the Executive Director can be very influential.

Since the Executive Director regularly plays such a central role in the single-family office, really developing a deep understanding of his or her responsibilities is crucial. Over the course of the relationship, being cognizant of the interplay between the Executive Director and the wealthy family is also essential.

Having awareness of the professional objectives of the Executive Director is a simple concept, but proves to be very meaningful. This includes gaining an understanding of the Executive Director's personal background as well as how he or she came to run the office. This provides insights as to the level of expertise in various areas and offers insight regarding where ancillary investment education is appropriate.

Map out the professional ecosystem of the single-family office. As we pointed out earlier,  no one knows precisely how many single-family offices are currently in operation. Erudite estimates put the number between a few thousand to as many as ten thousand. However, as noted there is consensus that more are on the way.

With the universe of single-family offices still relatively small, the tendency is for the universe of preferred service providers catering to this sector to also be somewhat limited. Rothstein Kass, for example, is increasingly the vendor of choice for single-family offices that choose to outsource various administrative and tax reporting functions as well as advanced planning services. Prince & Associates, meanwhile, is constantly on the short list for various advisory services to single-family offices, from compensation to best practices, including consulting on the optimal ways to launch and structure family offices.

This has created a tight-knit community of services providers, where the professionals working with single-family offices tend to know the major players well. Furthermore, these professionals also are often quite familiar with each other. More often than not, we are dealing with a scant few degrees of separation.

In profiling single-family offices, investment managers and investment bankers benefit greatly by understanding the professional ecosystems catering to this universe. However, it's not enough to "know" the professionals. What is tremendously more effective is to literally map out the ecosystem. The depth of this mapping process can vary from a simple identification of involved professionals to a detailed multi-layered approach with "influence valances" attached.

The breath and depth of a profile is generally a function of trust and time – two variables that are highly correlated. Nevertheless, if the objective is to move beyond a potential sale or even a single sale, then profiling is a requirement. The profiling process, when adroitly managed, provides a holistic understanding of the single-family office that, in turn, results in success even when the smart decision is to move on.

Having profiled a single-family office, investment managers and investment bankers are able to develop highly customized explanations of their offerings. They are also better positioned to most effectively manage ongoing relationships with single-family offices.

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