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GENERATION PRIVATE – GLOBAL FAMILY OFFICE INSIGHTS

The following article summarises the results from the BlackRock Global Family Office Survey Report. The BlackRock Global Family Office Survey Report combines data aggregated from an extensive survey completed by 185 Family Offices globally as well as 20 in depth interviews with 20 Family Offices.

All Family Offices (FO's) are unique and this is reflected in how they have responded to the COVID crisis. The survey and the in-depth interviews conducted by BlackRock have identified three key themes.

Firstly, FO portfolios have proved resilient during this period of uncertainty but there are growing concerns, particularly around geographical diversification, equity valuations, liquidity needs and the spectre of inflation.

Second, alternatives continue to be a key focus for clients seeking diversification and to potentially enhance returns and finally, whilst extensive adoption is still limited, FOs are increasingly exploring sustainable investment strategies. There is a recognition that there may not be a need to sacrifice financial returns in order to do good and there is greater interest and pressure from the next generation of family members to better reflect their values.

Executive summary

01 Market outlook: resilience in the face of uncertainty

The survey indicated that despite a challenging economic outlook, few FOs felt the need for material change to their portfolio. Many FOs cited their long-term investment horizon and high allocations to alternatives as the driver of this.

However, FOs have growing concerns particularly around diversification, equity valuations, liquidity needs and the spectre of inflation. The BlackRock Investment Institute argue that the nature of the crisis and its long-term implications warrant a review of asset allocations.

02 Asset allocation: the growing importance of alternatives

Despite challenges, private equity remains the alternative investment of choice. Private debt, real estate and infrastructure are all seen as capable of generating long-term yields. Hedge funds appear to be enjoying a resurgence as many recognise that they could be well placed to profit from a more volatile and dispersed environment.

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03 Sustainable investing: from interest to action

80% of FOs are engaged in some form of sustainable investing and the trend looks set to continue. This is driven by the values of the next generation of family members alongside heightened public awareness. The survey indicated that FOs believe that sustainable products no longer require compromising investment returns. However, addressing the remaining hurdles of education and the absence of common impact measurement methodologies could lead to more widespread integration.

Detail

01 Market outlook: resilience in the face of uncertainty

In uncertain markets, FOs have been relatively unflustered, with only 23% anticipating making material portfolio changes. Their outlook is cautious to marginally negative. Many FOs indicated that their portfolios have proven resilient during recent turbulence but their concerns over portfolio diversification are growing and new challenges have arisen. Given the need to diversify portfolios and access economic growth beyond core markets, FOs stated they will place greater emphasis on geographical diversification and particularly China going forward.

It is believed that even investors with long-term investment horizons would benefit from reviewing their strategic asset allocation to ensure it takes account of a different macro environment emerging in the new normal and a higher degree of uncertainty in future estimates of asset class returns.

So, what was keeping them up at night? Four key themes were clear from the survey and the interviews:

1. Portfolio diversification
2. Liquidity management
3. Global equity market valuations
4. Inflation

Portfolio diversification

Importantly, China is seen by 85% of FOs as an investment opportunity that is distinct from the rest of Asia. Chinese equities, both onshore and offshore, are equally appealing to investors. FOs generally lack in-house investment expertise in Chinese assets and therefore seek partners with on the ground resources.

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The volatility of Chinese equities has decreased over the last few decades and the asset class is more independent and less correlated than other equity markets. However, it is important to note, Chinese equities remain more volatile and higher risk then other developed markets. It was also believed Chinese government bonds offer diversification benefits as they move independently of other developed market government bonds.

Liquidity management

Several FOs are prioritising liquidity from a more forward-looking perspective. Some view this environment as a chance to be opportunistic, seeking to capitalise on anticipated volatility.

Global equity market valuations

The strong relative performance of many technology companies' year-to date has been underpinned by strong and accelerating fundamentals as the Covid-19 pandemic has augmented consumer and enterprise adoption of various technologies. It was believed these changes in demand and behaviour are likely to be persistent over the longer term, which should be supportive of sustained growth for the technology sector going forward.

Inflation

The interviews revealed FO's are paying more attention to inflation hedging assets including gold, inflation linked bonds and real assets such as real estate and infrastructure.

In order to build resilience and ballast into portfolios, it was favourable to tilt away from nominal government bonds, as the return outlook is less attractive.

02 Asset allocation: the growing importance of alternatives

Given their long-term investment horizon, FOs actively look to exploit the illiquidity and other risk premium provided by alternative asset classes. Private equity and private debt are key areas of focus for FOs, with many looking to increase their allocations, driven by the perceived attractiveness of the current entry point in dislocated markets. Many FOs noted they are focusing once more on hedge fund strategies as they contemplate their risk adjusted returns in more volatile market conditions.

The survey highlighted that FOs are seeking to increase their exposure to alternatives. Private equity and debt are the most favoured areas, but many see interesting opportunities across the full spectrum of alternative asset classes, indicating a more diversified approach going forward.

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Private equity

The survey data showed it is most common for FOs to allocate 10-25% of their portfolio to private equity. 55% of FOs reported they expect to grow their exposure to this asset class. Private equity investing has challenges and risks. FOs remain unhappy with the fees and are increasingly concerned about correlations with other asset classes. 35% noted a concern with managing capital calls in an uncertain environment with heightened liquidity needs.

Private debt

Private debt was the second most popular asset class, with 40% stipulated this would be a future focus for them. Many stated they are seeking enhanced yields and alternatives to public fixed income allocations. In terms of strategies, there continues to be a clear preference for direct lending (74%), but given the current climate, this is now closely followed by distressed and special situations (58%).

Hedge funds

FOs are once again paying close attention to hedge funds. The survey indicated that recent market turmoil and the expectation of sustained volatility in the medium term has re-invigorated hedge fund appeal.

Real estate

Real estate is characteristically a stable component of most FO portfolios, representing on average 10-25% of their overall portfolio. Many cite the tangible nature of the asset class as well as a steady income stream and portfolio diversification as key attractive characteristics.

Infrastructure

Infrastructure currently represents a relatively modest component of FO portfolios with 56% of those investing having an exposure of 5% or less.

03 Sustainable investing: from interest to action

80% of FOs are now interested and engaging in some form of sustainable investment. FOs are not driven by financial profit alone. Values and legacy also matter. The next generation of family members are driving acceleration of this trend. The need to compromise on performance is no longer perceived to be reality or a constraint. There has been a lot of noise about FOs and their natural fit with sustainable investing. The survey revealed that much of that interest is now translating into action. This seems due to both generational pressure and increasing public awareness.

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Incorporating ESG data and insights within investment processes or portfolio design can lead to improved outcomes for FOs. Increasingly there is acknowledgement that there may not need to be a trade-off between returns and core values.

Whilst sustainable investment flows are in their early stages, it is believed the full consequences of a shift to sustainable investing are not yet fully appreciated or priced into markets and a return advantage can be gained during what we envisage to be a lengthy transition. It is thought that, on balance, FO sustainable investing has moved beyond mere intent, and many will continue to focus on sustainable investing going forward.