INVESTING ACROSS GENERATIONS
Family wealth in the 21st century
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Keeping it in the family

Investment beliefs that reflect the concerns of multi-generational families.

César Pérez Ruiz  
Head of Investments & CIO

According to recent analysis by a US consultancy firm, the median tenure of chief executive officers at large-cap companies in the US has fallen from 7.5 years to five in the space of just four years. The increasing turnover can be seen as both a cause and an effect of short-termism: CEOs of firms with outside shareholders are often under pressure to deliver results every quarter, which can lead to excessive risk-taking, including taking on too much leverage.

“Who pays the bill for the huge debts incurred by covid-19?”

With less pressure from external shareholders, the heads of private family firms are able to think more long term. Such companies are often self-funded. And while we might look sometimes with a jaundiced eye at buy-outs, we certainly like buy-ins, where the owners of family companies express confidence by upping their stake in a business just as bigger corporate investors withdraw. And over the generations, well-established family businesses will have built up a wealth of knowledge, experience and values that each generation absorbs and passes on to the next.

With 215 years of existence, and with an average partner tenure of 21 years, Pictet itself has a lot in common with such multi-generational firms. Consistent with this longevity, the Pictet group has drawn up a series of long-term, multi-asset investment beliefs, which act as guidelines for the investment services we deliver to our family clients.

Among these is the belief that strategic asset allocation is the most important driver of returns over the long run. This, we believe, means standing ready to take a range of diverse and uncorrelated investment decisions rather than concentrating on a small number – in other words, managing portfolios actively. In turn, success in active management means trying to eliminate the noise that comes with information overload and looking at the real thematic drivers of long-term returns. Family owned businesses fit well into many of these themes, whether it be innovation, stability and sustainable finance. Active management also involves ensuring prices reflect long-term fundamentals – something the owners of family wealth should value as it is often a hallmark of their own business success.

One of our core investment beliefs is that active management best serves the interests of our clients, including our family clients. Today, active management also means exploiting the dislocation that has resulted from the coronavirus crisis. Since the financial crisis in 2008, aggressive central bank stimulus has led to tighter correlation within and between asset classes, meaning passive investing has had the wind in its sails. We do not think this will last, given the price distortions and misallocation of capital often associated with enduringly tight correlations. We believe proper price disclosure will come in the wake of the economic uncertainty engendered by the coronavirus. Who pays the bill for the huge debts incurred by covid-19? Will it be bond holders or equity holders? Taxpayers in poor countries or in rich ones? In the huge monetary and fiscal stimulus we are currently seeing lies the roots of widening correlations that active managers will exploit, separating the winners from the losers as volatility and dislocation come to the fore again.

Finally, as stewards of client savings, we want to act responsibly, interacting positively with the investments we select. The families who count among our clients well understand our intent to invest with purpose, which is not the least important of the investment guidelines we follow.
FAMILY BUSINESSES: SECTOR BREAKDOWN WORLDWIDE

Family businesses tend to invest in less capital-intensive industries as well as newer, more innovative segments such as cloud computing and e-commerce.

Source: Pictet Asset Management, 30.06.2020
Family businesses are the backbone of economies throughout developed and emerging markets alike.

Source: Tharawat Magazine, Economic Impact of Family Businesses – A Compilation of Facts, 06.01.2016
Infographics: Valerio Pellegrini

*In purchasing power parity (current international $)
Source: IMF World Economic Outlook, October 2019
The global pandemic has put philanthropy to perhaps its greatest test yet.

Christoph Courth  
Head of Philanthropy

The temptation to start any article these days with ‘it has been an unprecedented year’ is as powerful as it is redundant. I think it is fair to say that we all agree it has been a strange one to say the least. Due to the turmoil that the pandemic has had on all aspects of our global community, it has been a pivotal time for philanthropy, one when the very systems and processes that have supported it have been challenged. And yet this has also been a time when philanthropy has really come into its element.

To paraphrase Aristotle, giving money away is a simple feat, but doing so in a manner that truly achieves sustainable positive change is fraught with challenges. As an advisor to philanthropists, never have I experienced such demand for my help as since March, with the questions I have had to field evolving at a rapid pace. For example, during the early days of the pandemic the focus was on how to get medical supplies to those on the front line in the health service. These questions then morphed into wider concerns about equal access to healthcare and education during a time of lockdowns and remote learning. And more recently around hardship funds, unemployment, homelessness, addiction, domestic violence and those related to our food chains and food systems.

Many have also been reevaluating their own role as philanthropists. Are the systems and requirements they have in place fit for purpose? Are they agile enough? Are they supporting the right causes? Are the expectations, timelines and parameters they attach to their support suitable? Are they really leveraging all the ways they can mobilise their wealth?

This year private capital really has been put to work extremely quickly, with commitments by the global philanthropic community surpassing €10 billion by June, according to Reimagining European Philanthropy (McKinsey). Because of this revaluation, those assets have become more flexible, more patient, less directive and with fewer restrictions. And that is exactly how philanthropic capital performs best, putting ownership in the hands of the experts and organisations working on the front line of the causes we all care about.

“To give away is an easy matter and in any man’s power. But to decide to whom to give it and how large and when, and for what purpose and how, is neither in every man’s power nor an easy matter”  
— Aristotle

Now not only could this year show more wealth being pledged to social and environmental causes than ever before, but resources are being activated with a renewed sense of purpose and dynamism. This can be seen in the growing determination of a rising generation passionate about addressing the ills they see in the world through their businesses, their investments and their philanthropy.

And with a legacy of more than 200 years of social and economic consciousness at Pictet that permeates to the very DNA of the firm and its people, we too continue to focus not just on the ethical way we do business and on the responsible way we invest our clients’ assets, but also on how we help our clients realise their own philanthropic aspirations.
Providing Families with Peace of Mind

Wealth Solutions brings together PWM’s expertise across various facets of wealth management to help provide families with all-round solutions to the complex issues they face.

Stéphanie Lair Crommen
Head of Wealth Solutions

We all know that family wealth dynamics can be complex, especially given the diverse nature of modern families whose members may have differing priorities and are often scattered across several countries. Life events, expected and unexpected and of every sort, throw up a wide range of issues that cause wealth owners sleepless nights. Issues can especially come to a head at times of transition — when it comes to transmitting wealth to children or selling a family business for example.

Pictet Wealth Solutions was created to provide families with a certain peace of mind by treating complex wealth issues under a single roof. This has meant bringing together transnational expertise in areas stretching from wealth planning to family advisory, as well as from credit and private funds to philanthropy services.

Pictet has been around for 215 years, all the time owned and managed by a small number of rotating partners, with the same families represented since its origins. This gives it a certain pedigree when it comes to talking about family wealth, with Pictet’s independence reinforcing the group’s legitimacy and integrity.

A healthy, responsible relationship with families is especially important when dealing with potential conflicts of interest inside families. This is where Wealth Solutions’ family advisory capabilities come in, helping to build a strategic framework for addressing issues such as sharing out financial responsibilities within a family, bringing in outside parties to manage the family business and, most fundamentally, setting out what the family actually wants to achieve.

Wealth Solutions can also foster initiatives — for example in the area of philanthropy — that helps bring families closer together. Ultimately, Wealth Solutions’ ambition is to be there with credible advice and solutions at crucial times for families, accompanying them right through their life journey.

After having built a strategic framework for managing family wealth comes the implementation stage. Is a family office needed? Should a foundation be established? What about a trust? How much control can and should a family have over these structures, and what are the tax and legal implications from one jurisdiction to another? How should a family invest in private assets and how can a family make optimal use of credit facilities to further its aims? Wealth Solutions can call on multiple expertise to help deal with all of these questions, with Pictet’s independence a guarantee that the clients’ interests will always come first.

At Wealth Solutions, we concentrate on various facets of family investment, from the priorities of Family Offices to investing in family businesses and how these businesses address socially responsible investing issues. We also look at the particular issues facing family wealth owners in both Europe and Asia.

The case of Asia is especially interesting. The economic boom in Asia over the past three decades has produced a generation of self-made men and women who now face the kinds of issues surrounding transition that we typically see in Europe. While each country in the region is different, Asian families stand out for the importance they attach to transmitting values and have become increasingly concerned about their impact on the world and the legacy they will leave. It is therefore perhaps not surprising that Pictet, with the same families at its helm for eight generations, holds a special interest for them.

Without promising too much, Wealth Solutions can, perhaps, help these Asian families achieve a similar longevity.
INVESTING IN FAMILY BUSINESSES: FACTORS FOR SUCCESS

Although succession issues call for vigilance, research shows that family businesses consistently deliver superior returns on the back of a long-term focus and continuity. Similar reasons, plus the proverbial ‘skin in the game’ also explain the effectiveness of manager-owned fund companies.

For Alexandre Tavazzi, Head of Pictet Wealth Management (PWM) CIO Office, in an investment environment where short-term thinking is under heavy scrutiny, there is growing appreciation of the enduring qualities of family businesses. Indeed, the single major difference between family businesses, and businesses with a wider ownership base, is time horizon.

“If you are put in charge of a family company, such as Pictet itself, you want to make sure that the company is in good order when it’s transferred from one generation to the next, which means that you tend to be more cautious and think in years and not in quarters.” This is a major contrast with company managers (as opposed to owners) whose aim is to “maximise the company’s value while they are at the head of the company because part of their compensation is determined by stock price and the performance of the business.”

This long-term perspective is linked to shareholder expectations. “If the majority of shareholders is a family, it tends to be OK to wait for the long term-potential to be realised, which is not the case if you are talking about, say, a pension fund. The latter’s mindset is to reach their investment objectives from one year to another and to match their liabilities on the pension funding side – and hence they want to extract as much value as possible from the investment.”

It might be expected that the pool of investable family companies is limited but this is not the case, according to investment funds team leader at PWM, Jean-Marie Gaudichau.

“We reckon there is a large and deep universe of family companies listed worldwide. Family businesses operate in all geographies, market caps and sectors. So, from an investment point of view, there are lots of choices and you can diversify a portfolio of family-owned businesses. That’s the first factor for success.”

For Gaudichau, family businesses in investment terms are synonymous with growth and quality – quality of balance sheet, low leverage, quality of management and the business. “We’re looking for self-funded organic growth and a scalable business model. While family-owned businesses are attractive prospects for investors, getting the most out of them necessitates close analysis and a well calibrated, active approach.”

The nature of family business is such that qualitative factors require particular attention. This centres around governance, in particular succession planning and holding structure.
“Sometimes things aren’t that transparent [with family businesses] due to the lack of board independence so when you invest it’s important to look at ownership, long-term vision, controversies and committees, i.e at succession planning, independence of remuneration, nomination, audit committees and so on. But when you are past two, three, four generations you tend to have well-structured governance,” says Gaudichau. On the other hand, notes Alexandre Tavazzi, the particular skills and qualities that built the company’s success may fade after several generations. Conflicting views may emerge and a lack of cohesion develop among family shareholders and it may be time to go outside the family to ensure continued success. After all, “you can choose your friends, managers – but you cannot choose your family.”

Pictet Wealth Management’s approach to manager selection reflects the same values and mindset as often is found in a family business structure.

Mussie Kidane
Head of Fund and Manager Selection

Pictet Wealth Management’s open architecture model means we try to find the best-fitting products for our clients’ portfolios in line with strategic and tactical asset allocation decisions. When it comes to investing in family businesses, there are two areas where we play an important role. First, we bring access to our approved list of funds, a range of off-the-shelf investment vehicles that meet the needs of our clients. We also analyse the same kind of products from other asset managers.

Second, one of the core principles behind our manager selection process is that we look at the structure of the firm where a fund is managed. All things being equal, we have a preference for owner-operator models. We like institutions where individuals who manage client assets are also involved in the ownership of those institutions; we want them to manage our clients’ assets as if it is their own money. In that way, there is a strong alignment of interests.

This is an approach that is close to the Pictet DNA. One of the reasons clients come to Pictet is because of its particular structure, with the owners running the business (thereby significantly reducing the agency problems that can occur elsewhere). We don’t exclude other business structures but, all things equal, we prefer owner-operator models, which we typically find in boutique asset managers.

Finding the most fitting and best performing managers is a challenge in itself but once we find them it’s also important to have a lasting relationship with them. The worst thing for us is to find and select highly-performing fund managers and see them leave the firm a short time after. The tenure of fund managers who are owners of the businesses that they run tends to be longer, thereby ensuring stability and continuity.

Empirical evidence shows that fund management teams that work together are more productive and effective. For instance, there is a manager we selected 15 years ago (and in which we still invest heavily) that has generated tremendous excess returns for our clients. It’s a private company, not a listed company, and the founder and his team own and run that business. It’s one example that illustrates the stability that this owner-manager model brings.

One of the things that these manager-owned firms place stress on is the governance of the companies they invest in. They put a lot of emphasis on the management team, incentive structure and track record of the CEOs. Many of the firms they invest in also exhibit incentive structures that ensure alignment of interest between company management and investors. Unlike our colleagues on the equities and fixed income research side, we don’t pick securities directly. However, we are careful to choose managers who are keen to translate the alignment of interest requirement that is at the core of Pictet’s owner-operator model into action.
WHY GOOD FAMILY GOVERNANCE MATTERS

Families need to put in place sound governance models to navigate through crises such as the one we are experiencing.

Honora Ducatillon  
Head of Family Advisory

Why should families care about governance?  

Wealthy families, irrespective of where or how big they are, share a common characteristic, which is that their family, ownership and wealth/business interests are intertwined. To start, a family patriarch or matriarch usually cumulates all the roles. But as families grow, different combinations of roles emerge: some family members are owners, others are not (think of in-laws or of younger-generation members for example). Some are involved in managing the family business or wealth, others are not.

Moreover, with each generation, more effort is needed to maintain family ties: family members are raised in different households and may live at opposite sides of the globe; different generations may also have very different views on the road ahead. Governance involves understanding the various (sometimes competing) interests family members have and agreeing
upon boundaries that keep issues manageable. It is also about intentionally nurturing family unity.

Governance also addresses several risk factors which may destroy value, such as nepotism, losing touch with the outside world, sibling rivalry, intergenerational issues, financial disputes and ‘Prince Charles Syndrome’ (a tendency by current family owners to keep the next generation waiting). Failing to recognise these risks could leave families facing similar scenarios to the Lur Saluces family, owner of the prestigious Château d’Yquem in Bordeaux. Some family stakeholders felt left out by the family member in charge of the business and unsatisfied with the dividends they received. This eventually prompted them to sell out to the luxury conglomerate LVMH in 1999, thus ending a family business stretching back to 1593.

How do you help families address these risks?

First, by drawing their attention to the challenges they face. Awareness and education are key to gain support in the family for a governance model. Second, by guiding them through an exploratory journey that alternates individual reflection and collaborative workshops. This approach facilitates the emergence of the different perspectives on the most important wealth issues facing a family.

We start by mapping out a family’s unique DNA: What are the defining moments of its history? What are its core values? What specific skills and interests do family members have? Developing a shared understanding of the family’s history helps members learn from the past and identify its strengths and weaknesses. Discussing values enables them to better understand the motivation behind their behaviour. Recognising the individual passions and capabilities of family members help them realise the role of human capital in crafting a family’s future.

Families then discuss their purpose and mission. This can be an eye-opener. Families may, for example, realise that even if they thought their main aim was to keep the business in the family, their priority at a deeper level is actually to maintain and nurture the family’s identity and unity.

Once families are united around the idea of a mission, of achieving something together, they can see the value of working on a decision-making and governance framework that minimises the risk of conflict. If it appears that there isn’t really a mission shared by all, then families may consider splitting the assets or “pruning the tree” (allowing some of the family members to exit from the shared ownership of assets).

Finally, families determine how to organise themselves to achieve their mission, mapping out the boundaries between their family, wealth and business and deciding which governance bodies they need to nurture unity and decision making (family board, family assembly, family office, etc.)? By defining clear guidelines on access to ownership, employment, and financing, for example, family expectations can be managed. By creating governance bodies, families make sure they “de-personalise” issues and create a fair process which increases the chances that decisions are well accepted. At the end of our series of workshops, we assist them in drafting a family charter covering all the topics addressed.
Is governance only an issue for business-owning families? No, it is also an issue for so-called ‘financial’ families (those who have sold their businesses or inherited financial wealth). As long as a family owns assets together and has a multigenerational vision, then some governance rules are needed. Think, for example, of the clarity needed around issues such as the disposal of a family home or a portfolio of financial investments.

A family that decides to sell its family business and therefore transform the nature and source of its wealth from business to financial assets needs new skills and a completely new organisation – not to mention a renewed family commitment to act together as a group. Some families may decide to professionalise administration of their wealth by setting up their own family office, while others may prefer to delegate part or all wealth management and advisory to external experts.

You have conceived a three-step approach (see diagram) to help develop human capital inside family businesses. How does this translate into practice?

This approach stems from recognition that the family talent pool is a key asset for family businesses. We have developed a process that allows families to set out different ownership roles, the skills needed for these roles, and how family members can develop those skills. The outcome need not be binary. A family could have an external CEO, but still have control of the board. The question simply is how to find an equilibrium between family interests and non-family management.

What are some of the best governance practices you have observed?

Whatever the size, location and origin of family wealth, governance is crucial. In partnership with the Lausanne-based IMD business school, each year we recognise a family business that excels both on the business and family fronts through the Global Family Business Award. Past recipients have shown an ability to achieve the right balance between family and corporate governance, created a platform to facilitate the relationship between families and external managers, set up training programmes to prepare the next generation of family owners, or extended the family system to include people on the grounds of merit.

What role does governance play in dealing with crises?

A sound governance model is key to weathering crises, as complex trade-offs have to be made, sometimes very rapidly; family owners not only care about the financial health of their business, but also about their network of stakeholders, including their employees, partners, suppliers, family members, and communities. Since the outbreak of the covid-19 crisis, many family business owners have been much more involved in their business than they were before the crisis. In such a context, being clear about the respective roles of the owners and managers, and beefing up the level of coordination (but without intruding on each other’s tasks), is of particular importance to ensure enlightened and timely decisions.

How do you deal with the increasing prominence of social and environmental responsibility issues?

As we help families to align around their values and mission, the social and environmental impact of their actions (their businesses, investments, and lifestyle) is increasingly coming to the fore. A vegan millennial sensitive to environmental issues might not be aligned with a family business involved in meat-processing or a family investment portfolio that includes hydrocarbon companies.

Today, families can use numerous ways to mobilise their wealth and businesses for social and environmental impact, through giving, investing and innovating their business model. We help families navigate through the different possible strategies and translate their views into coherent action.

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**A THREE-STEP APPROACH TO DEVELOPING HUMAN CAPITAL INSIDE FAMILY BUSINESSES**

1. **SET THE STAGE**
   Define the ownership roles and the competencies they require

2. **IDENTIFY NEEDS AND PRIORITIES**
   Define which competencies must be developed in your family and in which order of priority

3. **DESIGN PERSONALISED LEARNING PATHS**
   Define how the competencies can be acquired

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Source: Lansberg Gersick, Pictet Wealth Solutions, 2020
Family-owned businesses are incredibly wide-ranging in size. Some are very small, but others are huge multinationals. Yes! Even some of the world’s biggest and best-known companies are family-owned businesses, if you look at how much voting rights the founding family has.

Family businesses are at the heart of the global economy. According to analysts at Family Capital, the 750 top family businesses in the world by revenues generated USD9.1tn in revenues in 2018 and employed 30.5 million staff. In fact, in most countries, family businesses account for 40–60% of all private-sector jobs. And most start-ups (85%) are actually funded by family money.

Successful family businesses generally share a few structural characteristics:

— **ENTREPRENEURSHIP.** Often innovative or disruptive, family businesses invest more resources in research and development (R&D) than others;

— **“SKIN IN THE GAME”.** With most of their wealth and reputation invested in the firm, the interests of family owners and their business are closely aligned;

— **CAREFUL STEWARDSHIP.** Family businesses typically show a strong desire to invest now for the success of the next generation; and

— **LONGER-TERM PERSPECTIVE.** As family owners’ wealth is often tied up in the business, they typically reinvest for growth. Usually with lower gearing ratios than non-family-owned companies, they tend to fund operations more through internal funds than through debt.

**FAMILY BUSINESSES AT THE FOREFRONT OF SUSTAINABILITY**

Family-owned businesses will play a key role in finding and implementing solutions to this century’s global challenges.

Rosa Sangiorgio
Head of Environmental, Social and Governance (ESG)
Do family-owned businesses have a sustainability advantage?

There are as many varieties of a sustainability advantage? Do family-owned businesses have a sustainability advantage? There is as many varieties of a sustainability advantage. My favourite is contained in ‘Our Common Future’, the 1987 report from the United Nations’ World Commission on Environment and Development, which defines as sustainable any “development that meets the needs of the present without compromising the ability of future generations to meet their own needs.”

As such, sustainability concerns companies’ financial, social and environmental risks, obligations and opportunities, often called the ‘triple bottom line’.

Often, depending on the ESG rating provider, family-owned companies score better in sustainability surveys than non-family-owned companies. This is mostly because of better environmental and social scores, whereas they may lag in terms of governance (see chart).

Family businesses may find it easier to deliver sustainable value creation, as their inter-generational perspective allows them to focus on the long term.

Families launching and passing on their business to the following generation have always existed. The world’s oldest existing business is a family-owned Japanese spring resort founded in 705AD called Nishiyama Onsen Keiunkan. It is one of a select group of businesses in existence for over 1,000 years, and united around what is called the Spirit of Shinise (Japanese for established and long-standing company). The Spirit of Shinise has four main purposes:

1. to ensure a sound company resides in a sound society;
2. to create tradition through the continuity of innovation;
3. to maximise customer satisfaction by ensuring employee satisfaction; and
4. to convey the moral value of Shinise to people around the world.

Not far from the concept of sustainability, is it?

The most successful family firms are often those committed to more than just profitability. Not being answerable to shareholders anxious to maximise profits helps. Additionally, their sense of commitment typically includes long-term relationships with a wide circle of stakeholders, including customers, employees, suppliers and the extended community – again, behaviours that fit in well with the basic principles of sustainability.

Another distinctive advantage family businesses enjoy is a shorter chain of command when it comes to making crucial decisions, including resource allocation. This means family-owned companies are often faster and more patient than other companies when it comes to R&D, which gives them a key role in finding solutions to this century’s global challenges.

“The most successful firms are often those committed to more than just profitability”

If the concept of stewardship for future generations comes naturally to many family-owned businesses, these companies are not necessarily “perfect” from a sustainability perspective. Due to their ownership and board structures, some family-owned companies may, for example, score poorly in implementing corporate-governance best practices.

What does this poor governance score mean? In some cases, the so-called ‘best practices’ defined by publicly owned companies’ behaviour may not be appropriate in a family-owned environment. For example, the concentration of ownership is considered a threat in standard frameworks, as there are companies with highly concentrated ownerships and poor transparency that have abused minority shareholder rights. But when looking at the specificities of a family business, the concentration of ownership may become a valuable and defining trait, with visionary family owners being particularly devoted to product and brand quality. Furthermore, these entrepreneurs are dedicated to creating strong and durable businesses. Their strong impact on social and environmental scores is strictly linked to the possibility of leveraging concentrated ownership in decision making. Does this make them unsustainable? Definitely not.

Other governance best practices may be applicable across family- and nonfamily-owned businesses alike. Family-owned companies may also have less diverse management boards or lack the resources to explore best practices and implement change (ie. demand supply-chain information or ask suppliers to do things differently).

Key to ensuring family-business sustainability is establishing the right...
Many family companies tend to prioritise people and the communities in which they work”

Look at one of the US’s biggest carmakers (and one of the world’s most successful family-owned businesses), which partnered with a healthcare company to manufacture ventilators. Similarly, a fifth-generation UK business, known for manufacturing luxury outerwear, moved to produce gowns and scrubs to support frontline medical staff. Or the Danish toy company that launched a website to encourage families to share creativity and play ideas and help children to develop problem-solving skills while they are out of school.

These are just a few examples. Through their efforts, family businesses are strengthening our defences and will play a crucial role in driving the global recovery.

Any family business that wants to make the difference needs to think of sustainability not only as something they might support or engage in, but also as something they influence through their supply chains. According to the IFB Research Foundation, such families also: keep a clear sense of long-term vision for their organisation, balancing long-term objectives and short-term performance; engage publicly in sustainability issues and leverage their position to influence supply chains; develop people capital; and focus on resource efficiency to avoid depletion of resources and ensure materials security.

Corporate governance conditions so that the positive aspects of family ownership are coupled with safeguarding the interests of non-family investors.

Family-owned businesses and covid-19

Every business today is facing the greatest challenge in generations, as the pandemic forces owners to drastically rethink business models, supply chains and working practices.

Family-owned businesses’ long-term perspective, entrepreneurial spirit, agility and guiding sense of purpose, together with the resilience of their leadership teams make them especially well prepared to fight a such crisis, especially as their multi-generation perspective allows them to meet their customers’ changing circumstances through economic cycles.

The covid-19 crisis has produced some great examples of family businesses displaying their experience as innovators to support their governments and communities in need. Some have pivoted their production lines to produce critical medical equipment in short supply, others have found ways to improve the lives of people in lockdown. All these companies tend to prioritise people, from their employees and customers, to their suppliers and the communities in which they work.

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ASIAN FAMILIES PREPARE FOR WEALTH TRANSFER

With significant wealth transition in the coming years, succession planning and legacy issues are steadily moving up families’ list of priorities.

Angie Han
Senior Wealth Planner
David Turysk
Head of Strategic Solutions SEA

A significant majority of listed firms are in family control in South-East Asia. Having amassed wealth during the strong period of growth in the region over the past three decades, leadership in many of these families is now transferring to a younger generation, whose concerns and aspirations may be different from those of their forebearers.

At the same time, with the prospect that Asia will account for 12% of the USD15 trillion of global wealth set to transfer from baby boomers to GenX in the coming years, according to consultancy firm Wealth-X, Asian families are seeking a more structured way of organising the management and transition of family wealth to the next generation, fuelling the growth of family offices in the region. They often receive official encouragement in this regard. For example, the Monetary Authority of Singapore (MAS) has set up a department dedicated to support the creation of family offices. Initiatives include the Family Office Circle, which enables family offices to exchange ideas; deal-making sessions leading up to the Singapore FinTech Festival, which connects tech start-ups with potential investors such as family offices; and a skills map for wealth advisors to navigate Singapore’s growing family-office ecosystem. The MAS has also launched a new fund vehicle called a Variable Capital Company to facilitate inter alia, the structuring of ultra-high net worth wealth.

The growth in family offices seems a logical consequence of rising family wealth in Asia, with Asia home to 758 billionaires in 2019 according to Wealth-X, including 342 in China. While family wealth in Asia, especially in China, may often be of more recent vintage than in Europe or the US, we see family offices being established at a much earlier stage and evolving much faster than elsewhere, assisted by digital and tech advances. Although many Asian families are still in the early stages of the wealth cycle, they are moving through that cycle fast—which means they are on a steep learning curve. This is fuelling a willingness to seek advice and employ outside professionals to manage operations—for example in the realm of IT and global custody as well as legal and financial advice. Within the growing sophistication and professionalisation of wealth management in Asia, family offices are making a significant contribution by centralising and vetting external providers.

As in other regions, ESG and responsible investing are becoming prime concerns among wealthy Asian families. According to studies, Asian families place a particular emphasis on environmental issues when considering impact investments. Whereas philanthropic money in Europe and the US is often directed towards environmental causes such as climate change, Asian families show a preference for helping the less privileged in their midst. (This is understandable: while Asia has the world’s fastest growing ultra-high net worth population, it is also home to nearly half of the world’s poorest people.)

While they are becoming more common, there is still room for family offices in Asia to take on more tasks and responsibilities, engaging with the next generation to facilitate the smooth transition of wealth across generations and to structure philanthropic efforts. As families’ wealth grows in Asia, they are diversifying into new areas such as direct investments and private equity, areas where Pictet Wealth Management has significant expertise, and in which family offices can play a central role. Family offices also have a role to play in developing family governance systems, where there is still much to do in Asia. More broadly, beyond the conventional pursuit of capital growth and concierge services, family office structures can be instrumental in preserving harmony and the legacy of the family across generations.

<table>
<thead>
<tr>
<th>REGION</th>
<th>VHNW</th>
<th>UHNW</th>
<th>UHNW</th>
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<tbody>
<tr>
<td>Region</td>
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<td>USD10-100m</td>
<td>USD100m+</td>
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<tr>
<td>Pacific</td>
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LARGE FAMILY WEALTH AND ENDOWMENTS: INVESTING LONG TERM WITH CONFIDENCE

Understanding goals and possible outcomes helps families steer their financial affairs.

Christophe Donay
Chief Strategist, Head of Asset Allocation & Macroeconomic Research
Kristoffer Jonsson
Senior Investment Manager

So much in life is about balancing the wish to seize opportunities that reflect aspirations and hopes with the need to build up defences to deal with unforeseen risks and threats. This is just as true for long-established family businesses, for whom establishing clear objectives is a cornerstone of good investment governance. Setting clear objectives helps drive growth and innovation while providing a level of safety during challenging periods like wars, natural catastrophes, or the kind of pandemic we have seen this year. Given the exposure to business risk, the custodians of the personal wealth of such families typically aim to maintain a certain minimum wealth level to provide the ‘fortress’ balance sheet needed in an adverse environment. This is where Goals-Based investing (GBI) comes in.

GBI provides a structured approach to addressing the goals of developing the core family business while maintaining a ‘fortress’ balance sheet to weather unexpected business challenges over time.

The origins of GBI go back to the early 1950s. Recognition of the imperfections of human reasoning led to the development of behavioural portfolio theory and mental accounting, with different sub-portfolios aligned to specific goals. Once these goals have been defined, a diversified GBI-type portfolio can be built involving an optimised allocation that extends to private equity and co-investments as well as public equity, fixed income and hedge funds, direct investments as well as cooperation with best-in-class funds/investment managers.

As goals and investment objectives vary widely (see chart), wealth managers need to work with families to define these, balancing risk and return for each goal to ensure families the peace of mind that comes from knowing their financial assets are part of a strong family balance sheet.

Three broad portfolios
With this in mind, families’ financial wealth outside their business can be loosely allocated to three broad portfolios with different goals: the first to preserve capital and provide financial safety in the face of unknowable risks; the second to maintain and grow wealth net of inflation; and the third for more ‘aspirational’ investments.

The size of the first portfolio will depend on how much risk the family is willing to take to avoid slipping below a certain wealth level. The second portfolio can be optimised by investing globally across asset classes. A family portfolio intent on maintaining and growing wealth net of inflation might consider using an asset allocation similar to that for university-style endowments. Indeed, along with incorporating advances in behavioural finance theory, GBI can use the endowment style of investing, which puts investors’ goals at the heart of the investment process.

Endowments are intent on maintaining and growing capital in real terms for current and future generations. Endowments thus can have a lot in common with a family’s long-term wealth objectives; they both seek to maximise risk-adjusted returns from a portfolio of global assets, being long term means they generally have limited liquidity needs and they both can have high tolerance for short-term drawdowns. Endowments are less regulated than other large institutional investors and typically managed by compact investment teams able to leverage third-party expertise in areas such as alternative asset management.

When setting goals it is important to strike the right balance between completeness and complexity, maintaining a limited number of sub-portfolios to reflect the variety of goals and investment objectives, including the needs of the family business, safety, desire to maintain living standards and other aspirational goals.

### SOME EXAMPLES OF INVESTMENT GOALS

<table>
<thead>
<tr>
<th>GOAL</th>
<th>INVESTMENT OBJECTIVE</th>
<th>STRATEGY</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Family Business</td>
<td>Grow and develop</td>
<td>Quality balance sheet</td>
</tr>
<tr>
<td>Safety</td>
<td>Capital Preservation</td>
<td>Conservative Endowment</td>
</tr>
<tr>
<td>Maintain Living Standard</td>
<td>Inflation + tax + living standard</td>
<td>Balanced Endowment</td>
</tr>
<tr>
<td>Aspirations</td>
<td>Enrichment</td>
<td>Concentrated higher risk / reward</td>
</tr>
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Source: PWM AA&MR, PWM Pictet Investment Office
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