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# Family Offices Exert More Control In Direct Deals

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While family offices are known for making co-investments with private equity firms, a rising number are cutting out the middleman and management fees.

“In the past, family offices tended to invest more passively with managers and they lost a lot of money due to the financial crisis of 2008,” said Irwin Latner, a partner in the Corporate and Securities Practice Group with Pepper Hamilton, which specializes in counseling family offices.

But now family offices are becoming a key player in both direct and early-stage investing.

“There is a place for fund managers even within the portfolio of a $10 billion single-family office, but the market is going more direct as family offices start to pool their resources, share due diligence resources, formalize their family office operations and hire away staff from fund managers to serve them full time,” said Richard Wilson, CEO of a $500 million single-family office and author of "The Single Family Office: Creating, Operating, & Managing Investments of a Single Family Office."

As a result, many of them are taking a more activist investment approach in private deals.

“Early-stage investments refer to those made with hedge funds or private equity funds at launch or when they are small in size,” Latner told *Private Wealth*.

Family offices accounted for 19 percent of investments in an average private equity or hedge fund within its first six months of operation, according to Deutsche Bank’s 13th Annual Alternative Investments Survey.

Family offices are particularly active in smaller-sized deals, according to recent data. They globally invest 13 percent in $5 million to $10 million deals that are either direct or co-investments, 12 percent in $25 million to $200 million deals, 15 percent in deals worth $10 million to $25 million and 46 percent in $500,000 to $5 million direct or co-investment deals, according to Family Office Club data.

The trend indicates that family offices are becoming more sophisticated. As a result, emerging fund managers and lower middle market companies now have more access to capital necessary to grow their businesses.

"The actual family members who created the wealth are often well known and respected in their own industries and have great depth of experience, which is a strategic value beyond just writing a check," Wilson said. "If you can leverage their reputation, contacts and knowledge, the family office could not only be someone willing to invest, but also a driver to really lift you up to another level of success in running your investment fund or company."

The Hamburg Family Office in Germany, for example, shifted from using managers to investing themselves by launching eight private equity funds through their own regulated Alternative Investment Fund Manager (AIFM) to complete secondary investments and co-investments focused on middle-market companies.

"We already had some shipping, trading and investment banking expertise in the family, so combining that with our relationships with a variety of banking and fund managers resulted in successfully recruiting a private equity team," said Roderich Widenmann, managing partner with the HFO Hamburg Family Office in Hamburg.

The HFO funds are a subsidiary of the Hamburg Family Office, which is a melting pot of four family lines, some of whose bloodlines trace back to European royalty.

"The French line of our family are of Huguenot origin," Widenmann said. "The Hamburg line of our family were in the German shipping business and in the 17th century the Jewish family line joined us."

Because lower middle market companies are often neglected by larger banks and brokerage firms and have more trouble sourcing capital, family office money is a welcome relief.

"Our investments benefit lower middle market companies because we're financing some of the debt through the deals we do and the access to capital has never been better for entrepreneurs," said David Dunn, president and founder of Kingsbridge Wealth Management, an advisory firm that caters to ultra-high-net-worth family offices.

In turn, when family offices make direct investments, they avoid the fees charged by fund vehicles and have more control over which companies receive their capital.

"Once the investment is made, family offices have more transparency into company performance as a direct investor than as a fund investor," said Bronwyn Bailey, vice president of research with Private Equity Growth Capital Council (PEGCC).

Matchmaking services and online platforms cater to family offices, where issuers market information about companies and their capital raise as well as deal flow and networking opportunities.

"Most of the opportunities we see are niche related and not large scale, which benefits smaller managers because there's so much money in these big pools chasing so few good ideas that they all throw money at the same concepts," Dunn said. "We see good returns in smaller deals."