Kristi Kuechler

Managing Director, Investor Market, Family Office Exchange

Kristi Kuechler is managing director of the investor market for the Family Office Exchange (FOX), a 29-year-old organization that provides education and networking for 380 single-family offices. FOX members oversee investable wealth of more than $500 million, on average. Kuechler opened FOX's West Coast office in San Francisco, where she is based. She recently corresponded with *MMG* about family office investment trends.

"THE MAJORITY OF THE FOX MEMBERS THAT WE WORK WITH ARE SOURCING DIRECT INVESTMENTS THEMSELVES THROUGH THEIR PERSONAL NETWORKS, AND NOT THROUGH GPs."

Q What shifts are you seeing in how families approach investing?

A An important distinction between family offices and institutional investors is that at some point in the history of most families, the family created a successful operating business. Given the entrepreneurial nature of business-owning families, it is logical that they may want to jumpstart the wealth-creation engine that helped them become wealthy.

We have seen significant growth of interest in—and execution of—direct investments in operating businesses, real estate and venture capital by FOX families. Families have always been operators in individual sectors—they knew their space better than anyone else. Ten or 15 years ago, families would more typically look at buying another operating business in the sector that they knew well, essentially the family's "alpha." They rarely looked for deals outside of the sector in which their wealth was originally generated. Now there seems to be a reconsideration of the investment strategy that many families pursued in the past, which was more of a "manager of managers" approach. Families are reawakening their interest in directly investing in operating businesses, whether as lead or co-investor.

While some family offices are co-investing alongside private equity general partners, the majority of the FOX members that we work with are sourcing direct investments themselves through their personal networks, and not through GPs.

Q What other drivers are leading family offices to invest directly in operating companies?

A There are both financial and nonfinancial reasons that families take this approach. They're of course looking for a strong return: FOX members expect their direct investments to generate a 14 percent return. In contrast with investing through a private equity fund, going direct allows families to take advantage of a longer time horizon. Some family investors are also looking to avoid paying the management fees and carried interest to private equity funds, and going direct allows them to disintermediate the general partner and avoid those fees.

Owning an operating company is viewed by some families as an investment from which they can draw more personal satisfaction, through hands-on involvement rather than a purely "paper portfolio." It might also

MORE ONLINE
Find more interviews at *middlemarketgrowth.org.*

be an opportunity to get a member of the family's younger generation involved with running a business and encourage entrepreneurialism. And finally, some families, especially those driven by the younger generation, may be attracted to investing directly in a company with a mission of social or environmental impact.

Q What types of direct investments are family offices pursuing?

A The majority of family office direct investments are in real estate, but 47 percent invest directly in operating companies. Of that group, family offices held an average of 15 direct investments and entered an average of two new deals in 2017.

There's a pretty strong interest in early-stage and midmarket growth equity. Our data show family offices target $500,000 to $1.5 million for venture investments and larger sums for middle-market investments.

Q What are the top challenges associated with direct investing for family offices?

A While appetite is strong, families face several important challenges in making direct investments. One truism among family offices is that most are fairly under-resourced: They are asked to do a great deal for the family, often with fairly small staffs. Family offices recognize that sourcing and due diligence are significant impediments to finding strong direct investment opportunities, as are current high deal prices and valuations.

Another challenge is that many of the families that have been investing directly in operating businesses (outside of the sector where they sourced their wealth) have done so in the last decade and therefore have a fairly cycle-dependent perspective.

Lastly, the interest in direct investing is upending many of the more traditional ways that families have approached asset allocation. As direct investments do not fit well in a more conventional "top-down" portfolio approach, families appear to be less focused on developing a risk framework within their private portfolios. //