THE WALL STREET JOURNAL.

https://www.wsj.com/articles/the-new-force-on-wall-street-family-offices-1488991396

MARKETS

New Force on Wall Street: The 'Family Office'

Clans with nine-figure fortunes are increasingly investing through unregulated firms known as family offices, impinging on the business of investment banking and private equity

Ross Perot Jr.'s Circle T Ranch outside Dallas. Family-office networks such as one set up by Perot Investments are springing up to help families strike private-equity-style deals and discuss investing strategies. *PHOTO: HILLWOOD*

By **ANUPREETA DAS** and **JULIET CHUNG**
March 8, 2017 11:43 a.m. ET

On a warm October day in 2014, envoys from 15 of America's wealthiest families gathered at Circle T, Ross Perot Jr.'s 2,500-acre ranch outside Dallas. Skeet-shooting was on the agenda, but the real purpose of the two-day retreat was for the families to get acquainted and eventually team up to pursue investments.

From that exclusive gathering, attended by people investing the fortunes of Michael Bloomberg, George Soros and other billionaires, sprang a broader network of 150 families that have since participated in more than 10 deals together, including acquisitions.

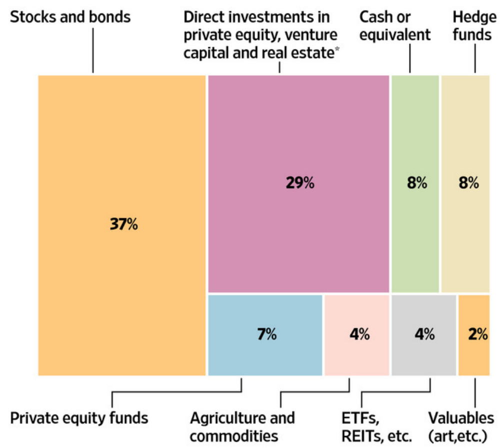
Such transactions traditionally were the province of big companies or private-equity firms. But a disruptive force has emerged on Wall Street: the family office. These entities, set up to manage the fortunes of the wealthy, and able to operate under the radar, are making their presence felt with their growing numbers, fat wallets and hunger for deals.

"We're all just starting to recognize that we should be a more important part of the investment world than we historically have been as a group," said Kenny Springfield, an executive at Perot Investments, which handles the multibillion-dollar Perot fortune and hosted the Dallas get-together.

Wealthy families have always found ways to protect and build their money, and the savvier among them have pursued their own business deals, from acquiring farmland to seeding hedge funds to buying companies. Today their ranks are ballooning, and many, put off by the high fees and sometimes weak performances of Wall Street money managers, are shifting to investments they can pursue directly through family offices.

Model Portfolio

What the average global family office portfolio looks like.



Note: Due to rounding, totals may not add up to 100%. *Includes co-investments.
Source: UBS/Campden Wealth Global Family Office Report 2016

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The offices are alternately linking up with buyout firms and competing against those firms to do acquisitions. They are providing financing to startups. They are buying distressed debt, real estate and esoteric insurance products. They are lending to companies and occasionally going into battle with companies as activist shareholders.

To do so, family offices are poaching talent from Wall Street. Among such hires, Thomas Pritzker, the billionaire chairman of Hyatt Hotels Corp., in 2015 recruited Joseph Gleberman, a senior banker in Goldman Sachs Group Inc.'s private-equity division, to help run his family office.

On Tuesday, Mr. Pritzker's family office and two other wealthy investors agreed to buy Hargray Communications Group Inc., a Hilton Head Island, S.C.-based cable operator, from private equity firm Quadrangle Capital Partners. The group, which includes the family firms of Arkansas banker Warren Stephens and Jim Davis, a co-founder of staffing company Allegis Group Inc., will pay $700 million in cash, according to people familiar with the matter.

“Family offices are becoming more institutional in their approach,” said Chuck Stutenroth of U.S. Bank's Ascent Private Capital Management unit, which works with family offices. He calls them “insti-viduals.”

For clans with at least $250 million in assets to invest, family offices have become the preferred vehicle through which to put their money to work, because they afford complete control and near-secrecy. They don't have to register with federal regulators as long as they limit their investment advice to descendants of a common ancestor within 10 generations, plus others such as key employees, adopted children and former spouses. Names of most family offices don't include the family's name.

Hedge-fund manager William Ackman and Google co-founder Sergey Brin have family offices. Billionaire brothers Charles and David Koch last year started one, named 1888 Management LLC, to manage a small portion of their estimated $86 billion in combined net worth. Oprah Winfrey has OW Management LLC.

“Everybody wealthy seems to want to have their family office,” said David Rubenstein, co-founder of private-equity giant Carlyle Group LP, on an investor call last year. Mr. Rubenstein, who once paid $21 million for a copy of the Magna Carta, is considering one for his own family, people familiar with the matter said.

The wealthiest families are commanding fresh attention from investment banks such as Morgan Stanley and J.P. Morgan Chase & Co., which in recent years have appointed senior bankers to cover family offices. Families' appetite for investing directly into companies rather than through funds has pushed private-equity firms to invite them to be minority deal partners. Family offices have also been among those pushing hedge funds, in which they are big investors, to reduce fees.

Tracking the number of family offices isn't easy, since they don't have to register. A

David Rubenstein, co-founder of private-equity firm Carlyle Group. *PHOTO: DAVID PAUL MORRIS/BLOOMBERG NEWS*

study by accounting firm EY said there are more than 10,000 globally, about half set up in the past 15 years. Robert Casey, senior managing director of research at Chicago-based consultancy Family Wealth Alliance LLC, has estimated the U.S. has 3,000 family offices with more than $1.2 trillion in assets.

The offices proliferate partly because of a surge in global wealth in recent decades, traceable in part to high levels of merger activity and initial public offerings. The number of billionaires in the world rose 6.4% in 2015 to a record 2,473, according to data provider Wealth-X. It says their collective wealth reached nearly $7.7 trillion.

"It used to take 100 years to make $100 million, but that process has been sped up" by entrepreneurs in Wall Street, Silicon Valley and elsewhere, said Dominic Samuelson, chief executive of Campden Wealth Ltd., which connects wealthy families with one another.

How the Ultra-Wealthy Invest

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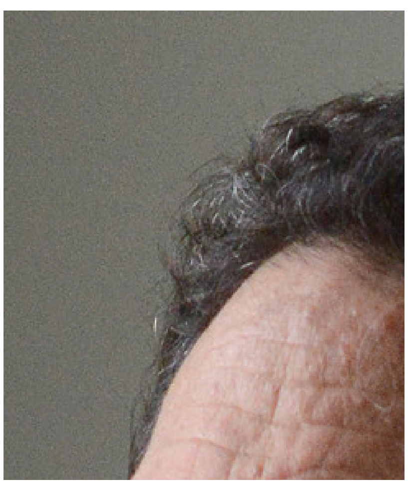
Family offices, private investment firms for the wealthy, are emerging as a disruptive force on Wall Street. They control an estimated $4 trillion.



Campden's research shows family offices hold assets of more than $4 trillion. That approaches the cumulative $5.7 trillion of private-equity firms and hedge funds, as estimated by data provider Preqin, though there is overlap because family offices sometimes invest in private-equity and hedge funds.

Carol Bernick's family wealth stems from hair-care company Alberto Culver Co., built by her father. Ms. Bernick said her family created an office in 2002 to manage assets outside of their stake in Alberto Culver. It had no formal name and just one employee.

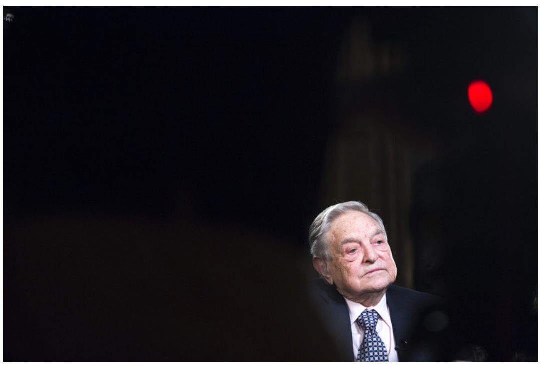
Four years later, Alberto Culver spun off a beauty-supply business, adding to the family's cash hoard, and then in 2011 Alberto Culver was sold to Unilever PLC for $3.7 billion. Assets of the family office, given the name of Polished Nickel Capital Management LLC, swelled. It now has 14 employees and invests in companies alongside other families and private-equity firms. Ms. Bernick is its CEO.

Since 2011, roughly three dozen hedge funds have converted into family offices after returning their clients' money, according to a Wall Street Journal tally. Soros Fund Management was among them. Mr. Soros cited increasing regulation as one reason. U.S. regulators require hedge-fund firms with more than $150 million in assets to disclose their strategies and how much they manage.

Energy trader John Arnold turned his focus to his family office and to philanthropy in 2012 after closing his hedge fund, Centaurus Energy Master Fund. Six months ago, his family office invested alongside a Goldman Sachs unit and some pension funds in Bass Pro Shops' $4.5 billion buyout of outdoor-sports gear seller Cabela's Inc. The deal is yet to close.

"Where can we capture outsize returns and protect our capital? The only way to do that is in the private world," said Allen Gibson, who oversees investments for Mr. Arnold's family office. Mr. Gibson said he invests most of the multibillion-dollar fortune in direct deals designed not to perform in lockstep with the stock market.

Family-office networks such as the one set up by Perot Investments are springing up to help families strike private-equity-style "club deals" and discuss investing strategies. The Perot group consists mostly of families with at least $1 billion, including the family offices of Messrs. Bloomberg and Soros, people familiar with the matter said. Perot family office executives said they hatched the idea after having to pass on a deal that needed more cash than they were willing to put up.



George Soros converted his hedge-fund firm, Soros Fund Management, to a family office in 2011. *PHOTO: JASON ALDEN/BLOOMBERG NEWS*

Family offices are "as quiet as you possibly could find, and they're writing extremely large checks," said Ward McNally, a great-great grandson of Andrew McNally, who co-founded atlas publisher Rand McNally in 1856.

The McNallys set up a family office after Rand McNally was sold in 1997 to private equity. In 2008, Mr. McNally established a new firm, McNally Capital LLC, that uses funds from his family and from a network of roughly 800 families globally to invest in companies together. Mr. McNally says he met with about 300 families last year, and every single one was interested in doing direct deals.

When private-equity firm BC Partners closed a $2 billion deal in November to buy several dozen data centers from CenturyLink Inc., its partners included Longview Asset Management. Longview is a family office for Chicago's Crown family, whose estimated $7 billion fortune comes partly from a stake in General Dynamics Corp.

In another deal, Hillspire LLC, a family office that manages more than $5 billion for Eric Schmidt, the chairman of Google parent Alphabet Inc., bought a fifth of hedge fund D.E. Shaw Group in 2014 for about $500 million.

Family-backed investors own all or part of luxury brands such as Jimmy Choo and Four Seasons Holdings Inc. and trendy consumer ones such as the parent of packaged coconut-water company Vita Coco.

Revealing their ownership is rare, but some family offices have drawn attention to themselves by launching activist campaigns.

In May, the family office of David Bonderman, a founding partner of private equity firm TPG Capital, criticized the management of Sorrento Therapeutics Inc., a cancer-drug company in which the family office owned a stake. Wildcat Capital Management LLC urged Sorrento's board to make a variety of changes that included firing the CEO. Soon after, Sorrento hired advisers to explore "strategic alternatives."

Goldman Sachs bankers last year started paying more attention to family offices after

The family office of former hedge-fund manager John Arnold pursues direct investments. *PHOTO: MICHAEL STRAVATO FOR THE WALL STREET JOURNAL*

realizing they were losing out on merger deals involving such offices. Starting with a list of 750 potential targets, they whittled the number to 27 families they thought had the interest and wherewithal to buy companies outright.

“We treat these family offices the same way we treat [buyout firms such as] Bain or Advent,” said Alison Mass, co-head of an investment-banking group at Goldman Sachs.

Among families Wall Street is eyeing are Quadrant Capital Advisors, a $14 billion New York firm that invests on behalf of Colombia’s Santo Domingo family and Fremont Group, which invests the construction-related wealth of the Bechtel family, bankers say.

Buyout firms Blackstone Group LP and KKR & Co. have executives who woo families with specialized investing opportunities. Some private-equity shops offer funds that invest for longer than the usual private-equity time frame, and co-investing options.

KKR co-CEOs Henry Kravis and George Roberts asked every employee to come up with five wealthy families the firm could tap for business as the firm looked to kick-start its effort. KKR now counts several hundred wealthy families as clients, up from virtually none in 2010, said Jim Burns, who leads its individual-investor business.

“It’s an ocean of wealth,” Mr. Burns said.