

# Family Office Trends in Alternative Investing

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# How Many Folks Believe that we will See a Recession by the End of 2020?

More Bull or Soon Bear

?



# Family Offices are Saving for a Rainy Day!

## General Family Office Investment Trends<sup>1</sup>

55%

of family offices believe we will enter a recession by 2020

45%

of family offices are re-aligning their investment strategies to mitigate risk

42%

of family offices are increasing their cash reserves

42%

of family offices are re-aligning investment strategy to capitalize on opportunistic events

22%

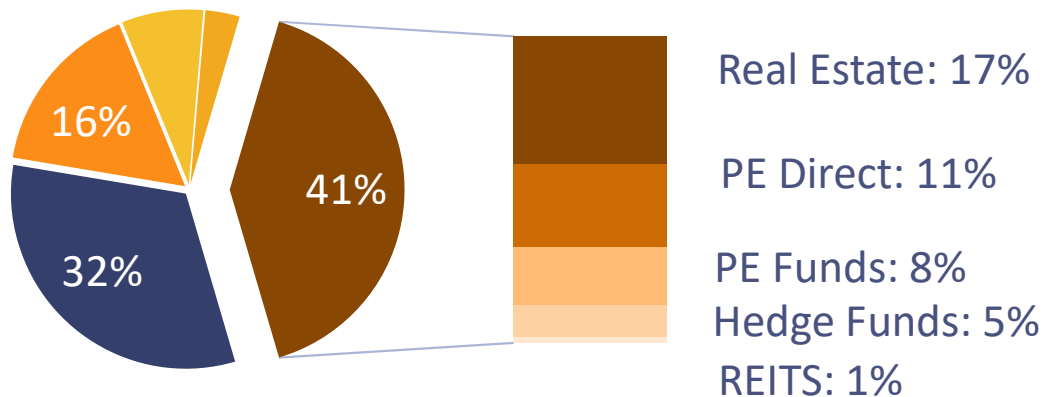
of family offices are reducing leverage



<sup>1</sup>UBS Global Family Office Report 2019

# Family Offices' Largest Allocation is to Alternative Investments

## Current Strategic Asset Allocation<sup>1</sup>



- Alternatives
- Equities
- Bonds
- Cash or Equivalent
- Commodities

## Alternative Investment Outlook<sup>2</sup>

2023 global AUM to \$14tn  
(+59% vs. 2017)

Investments expected to grow at a  
CAGR of 8%

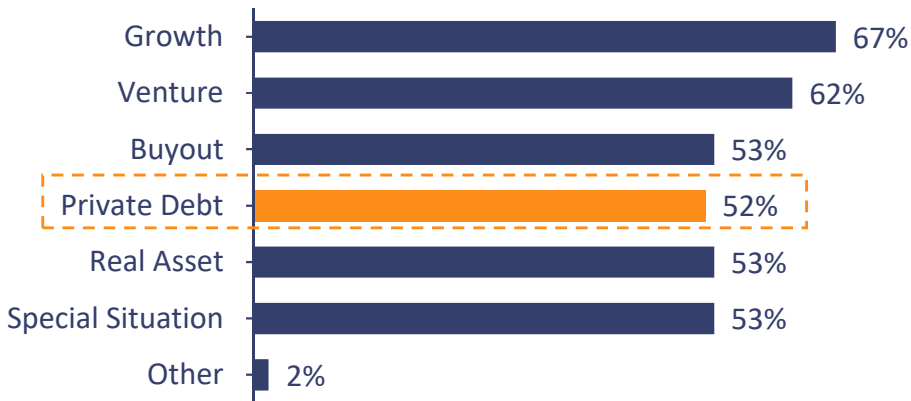
84% of investors plan to increase  
allocation to alternatives in the  
next 5 years.

Source:  
1. UBS Global Family Office Report 2019  
2. Preqin-Future of Alternatives Report, October 2018

# Family Offices Are Investing in Private Debt

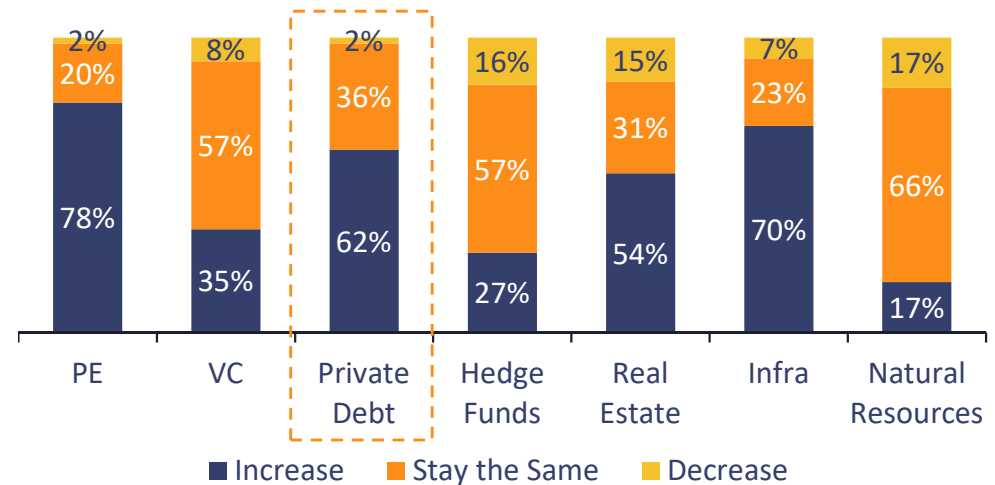
## FO Private Equity Investment Proportion

Proportion of Family Offices that are Involved in the Following Types of Private Equity Investments in North America<sup>1</sup>:



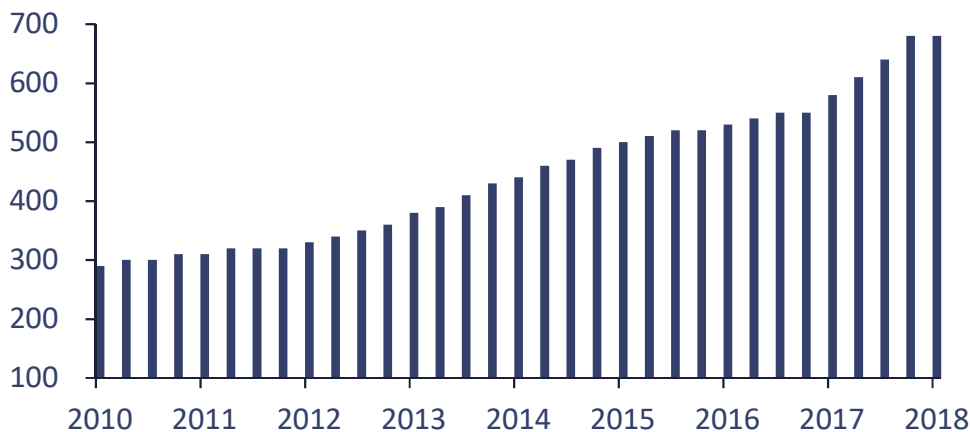
## Anticipated Changes in Capital Allocation

Investors' Projected Change in Allocations Over the Next 5 Years<sup>2</sup>:



## Private Debt Market has More Than Doubled in Under a Decade

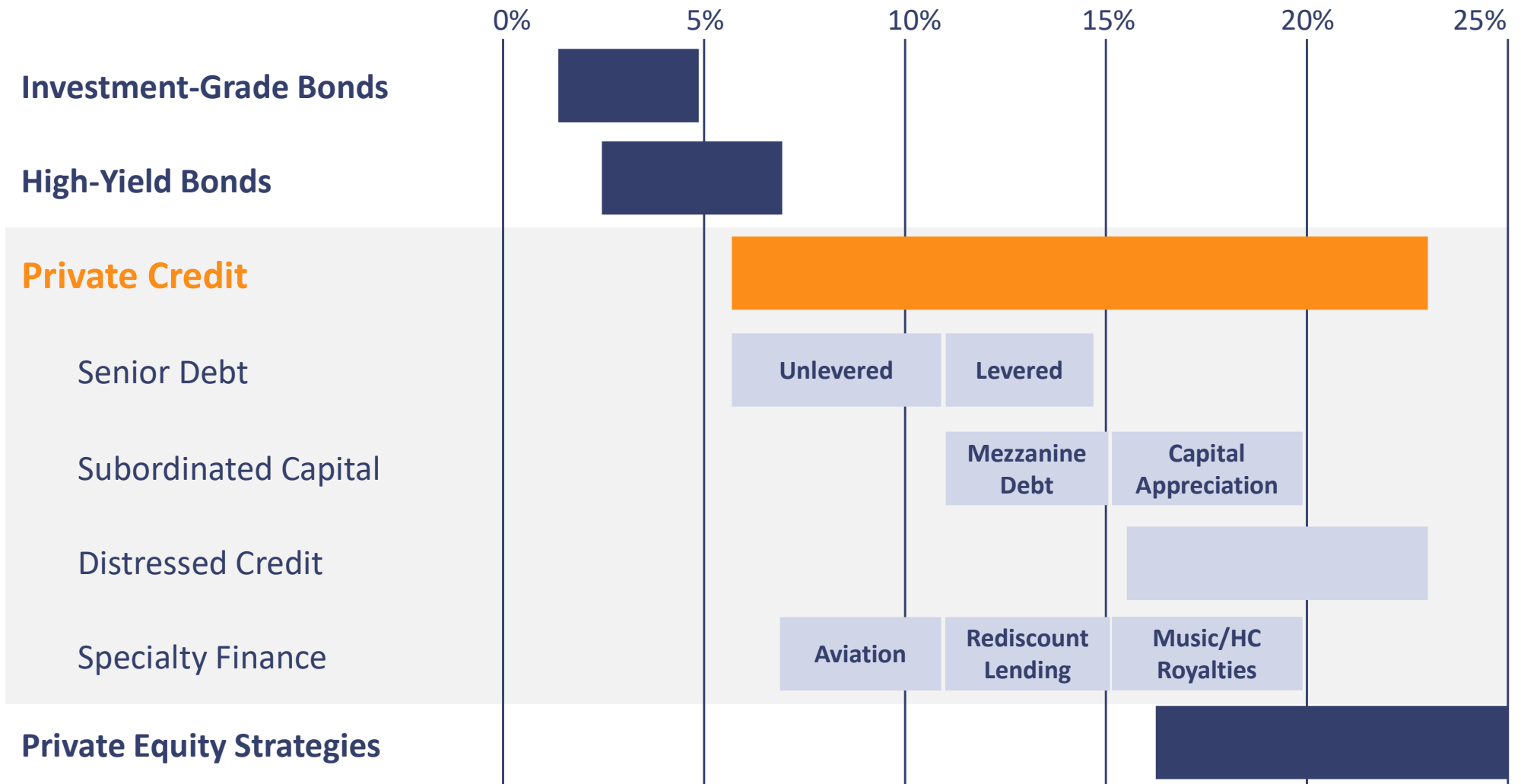
Value of Private Debt Deals Outstanding (\$bn)<sup>3</sup>



- The Private Debt market has swelled from about \$300bn in 2010 to about \$700bn by the end of 2018.
- Fundraising topped \$100bn for the fourth consecutive year in 2018.
- Demand is attributed to falling returns on offer from more mainstream parts of the debt market, and the desire to diversify into new asset classes that are less correlated to the undulations of stocks and bonds.
- Private debt provides diversification, offers high absolute returns, offers returns with low correlation to other asset classes, reduces volatility, generates reliable income and offers an inflation hedge.

# Private Credit is a Sub-Class of Private Debt

## Return Spectrum: Private Credit vs Liquid Credit and Private Equity Strategies<sup>1</sup>



Source:  
1. Cambridge Associates - Private Credit Strategies, 2017

# Are We in a Bubble for Private Debt?

## Risks of Investing in Private Debt

- **Investment Risk**
  - Fund specific – what are the underlying investments that they hold?
- **Liquidity Risk**
  - Investment sector – what asset class do they invest into and what premium do they receive versus their liquid benchmark?
- **Market Risk**
  - How can the macro economic forces impact the actual underlying investments, the overall strategy sector, and private debt space in general?
  - This “Triple threat” can be easily overlooked and a significant negative market event is starting to be viewed as the potential prick that could pop what some view as a bubble in the wider more correlated segments of the Private Debt markets.

# Focus on Non-correlation - Specialty Finance Investing

## Overview

- Targets one niche industry requiring manager specialization.
- These tend to be self-liquidating, not relying on refinancing for exit.
- Specialty finance investments are backed by an asset that has residual value such as a receivable, a rail car, a plane etc.

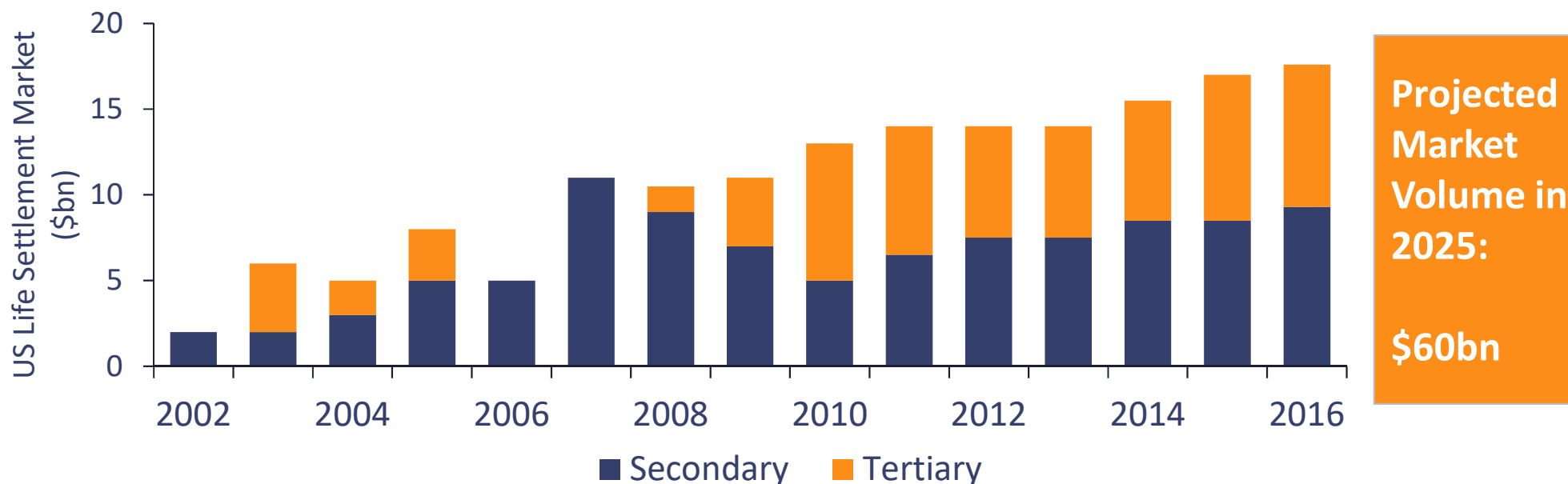
## Niche/Specialty Finance Strategies

- **Aviation** - Real-asset investment structure backed by commercial aircraft which offers long term, contracted revenues. Airlines typically lease the aircraft for a period of around 7-12 years.
- **Rediscount Lending** - Lending to companies that are in turn originating loans to small-and-medium enterprises and individuals.
- **Music/Health Care Royalties** - Investment in royalties or future expected cash streams on a movie, piece of music, drug product prescription.
- **Life Settlements** - Investment in life insurance policies. It is non-correlated and offers low standard deviation with attractive risk adjusted returns.
- **Catastrophe Bonds** - Risk-linked securities structured as floating-rate principal-at-risk notes, with maturities of three to five years.
- **Trade Finance** - Facilitates cross border transfer of goods. Assists exporters and importers to cover any liquidity gap within their trade cycle.



# The Life Settlement Market is Large and Growing

## Life Settlement Market Development



## Life Settlements - Key Investment Characteristics

- Excellent Risk-Adjusted Returns
- Reliably Projected Performance
- Proven Track Record
- Low Volatility
- Minimal Market Correlation

# Life Settlement Investment Risk Overview

## Longevity Risk

The risk that insureds live longer than expected

Mitigation steps involve use of independent medical underwriters, balancing fund life expectancy with opportunistic investments, and updating LE curves periodically.

## Liquidity Risk

The risk that the fund can't pay premiums or meet redemptions

Mitigation steps include maintaining cash reserves, initiating sales in the tertiary market and maintaining ability to "Gate" the Fund.

## Market Rate Risk

The risk that the discount rate used to value policies changes in an adverse way

Mitigation steps seek portfolio diversification, and suggest employing capital at more attractive rates than the average market discount rate

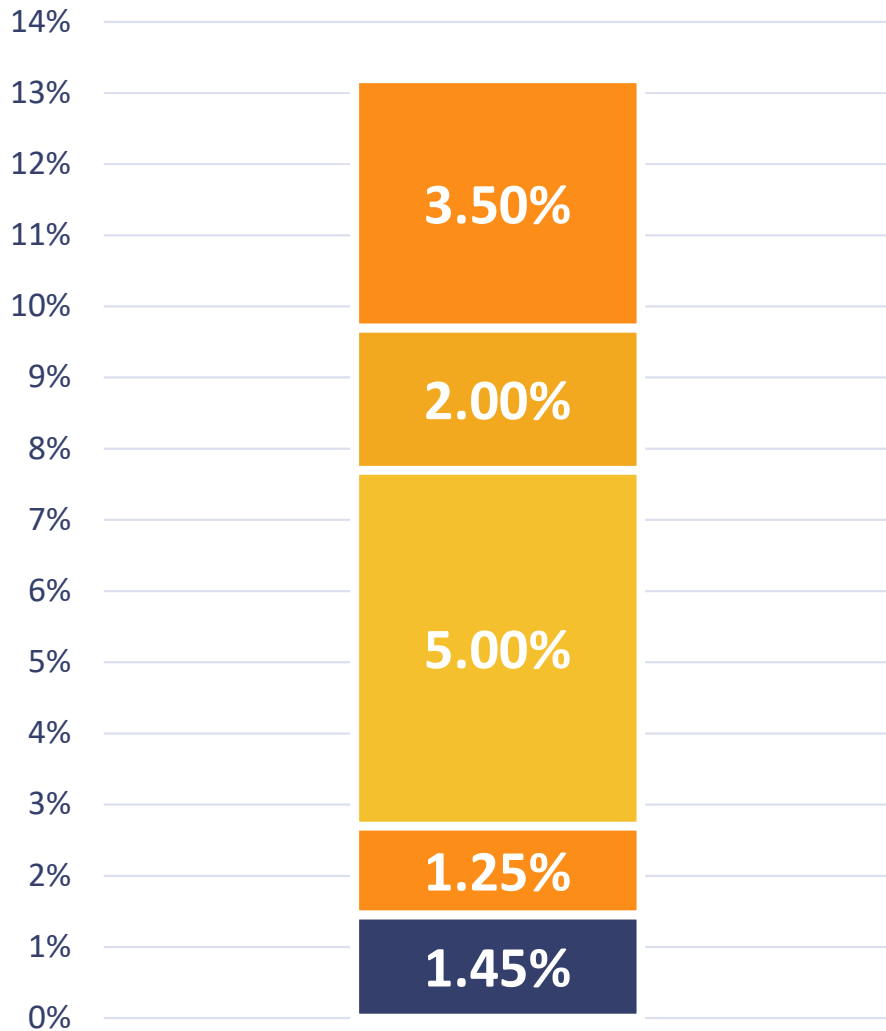
## Carrier Risk

The risk that the insurance carrier defaults, goes out of business, or changes premiums

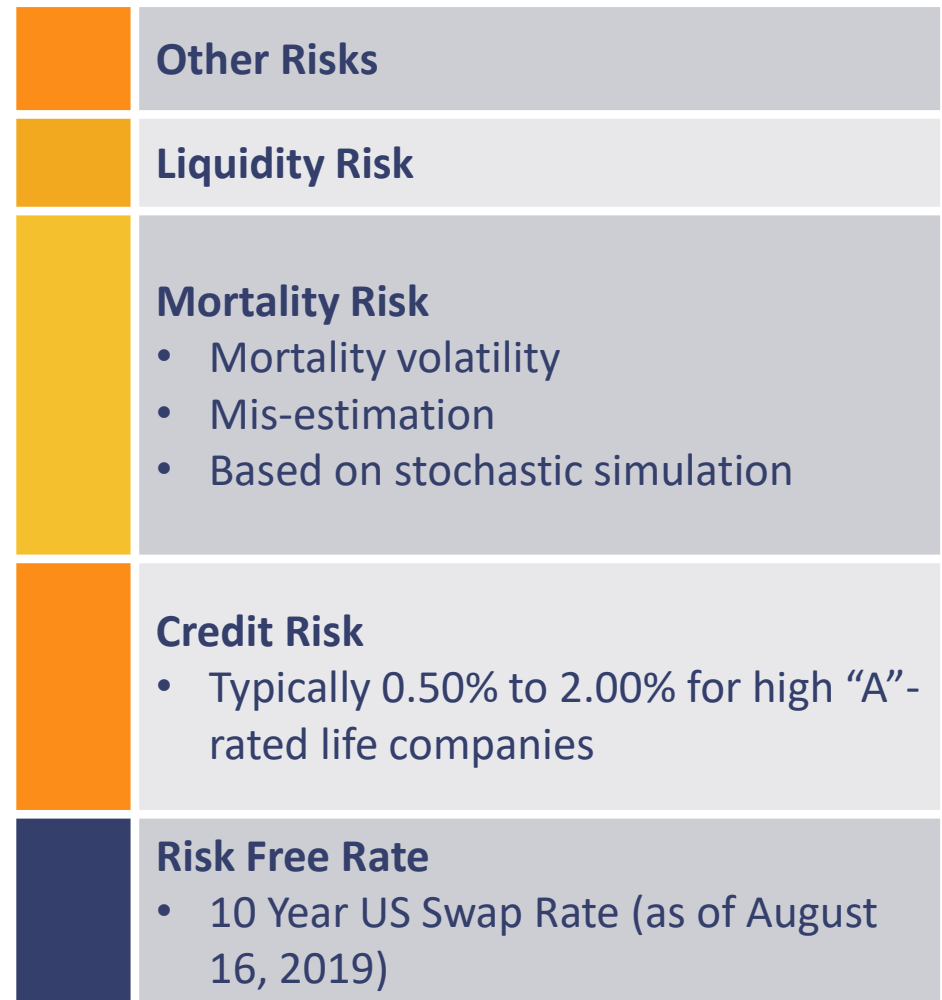
Mitigation steps recommend diversifying investment among carriers.

# Understanding Life Settlement Asset-Level Returns

Example Policy IRR = 13.20%

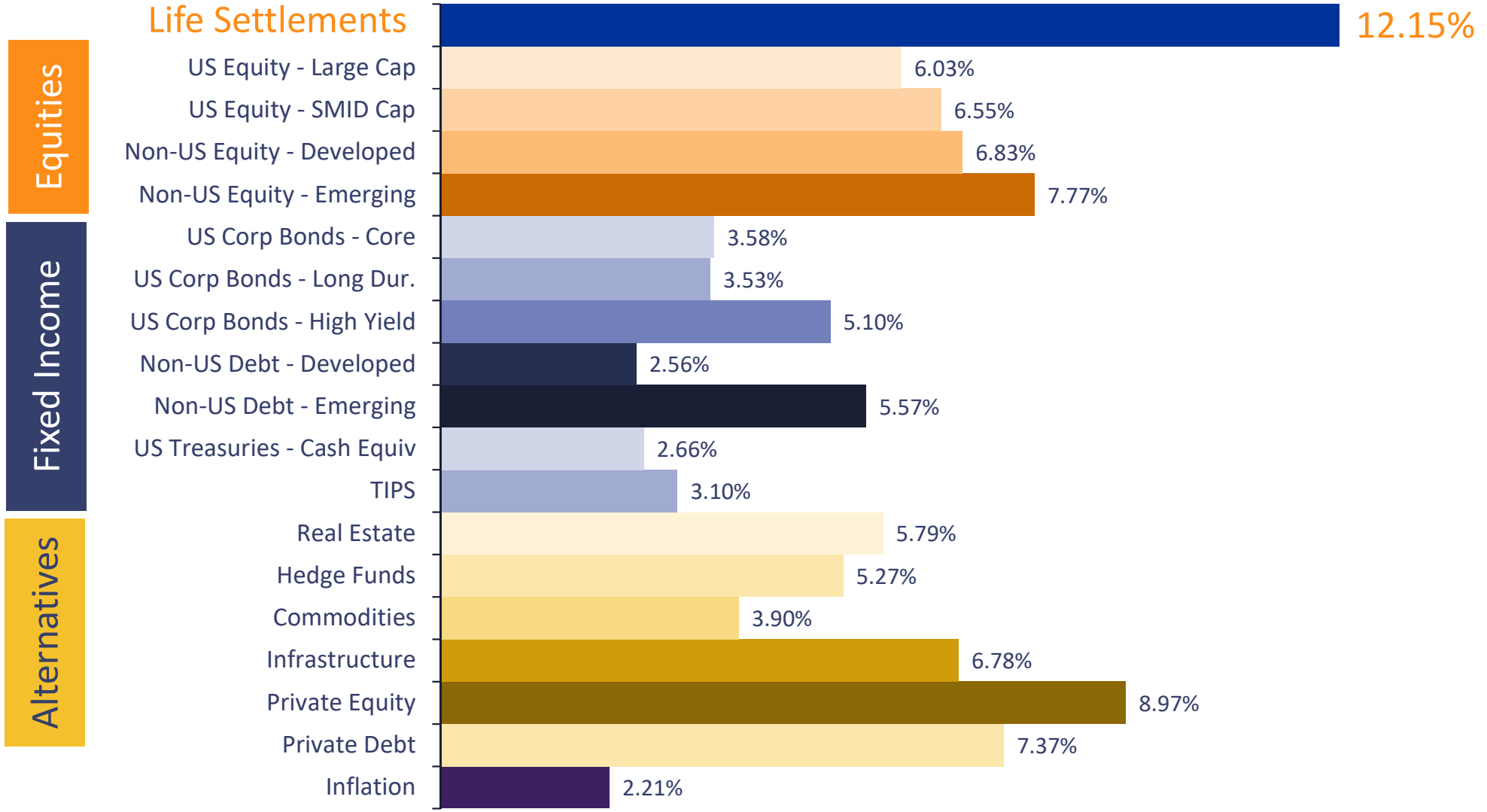


## Components of Asset-Level Returns



# Investor Return Expectations Over the Next Decade

Average Annualized Expected Returns – 10-Year Horizon<sup>1</sup>



Source:

1. Survey of Capital Markets Assumptions 2019 Edition, Horizon Actuarial Services, LLC; Life Settlements average annual return from June 2009 to June 2019, Life Equity LLC.

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