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3 Ways Family Offices Can Better Compete in a Deal Process

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By Meghan Daniels

Family offices are the hot new buyers in the lower middle market, but involving them in a deal process is not without headaches. “Many of them will indicate they want deal flow, but when we call them about a deal they’re not very responsive,” says James Cassel, chairman and co-founder of Miami-based investment bank Cassel Salpeter & Co.

There are an estimated 3,000 family offices in the US alone, and about a quarter of them currently invest on a direct basis, according to a 2017 report by financial technology platform iCapital Network. Family offices are also one of the fastest growing classes of buyers on Axial — the number of family offices on the network has doubled in the last 12 months.

Here are three tips for family offices looking to compete more effectively with PE firms and other investors.

1. Communicate.

“If a family office wants to bow out at any point in the process — whether it’s the initial call or when they get the NDA, the teaser, or the deck — there’s nothing wrong with saying, ‘It’s not for us.’ The key is to do it quickly and as soon as possible once the office has reached that conclusion. It’s important to respect everyone’s time,” says Cassel.

Being transparent about how the approval process works is also helpful. In a private equity firm structure, everyone understands that an associate or VP isn’t going to make the final decision on an investment. But in a family office, roles and job titles aren’t so well-established, and it can be harder to know where the buck stops. “Sometimes family offices will tell you one thing in terms of their process, but it turns out that process isn't exactly how it works — for example, you might have a meeting without the key decision-maker there and end up wasting everyone's time," Cassel says.

2. Find your edge.

"In the court of a family office, preservation of wealth is very important," says Cassel. Outbidding PE firms and strategic buyers often isn't a viable option.

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So how can family offices effectively compete? Find sellers who are looking for what you're selling. An owner looking for a relatively passive minority partner with patient capital, for example, may be willing to leave money on the table. Sellers may also trade cash for relationships and industry expertise, especially those that seem likely to lead to valuable partnerships down the line.

Cassel suggests looking at companies in the industry where your family made their money initially and has expertise and knowledge. "Even if you can't buy direct competitors, you may be able to buy suppliers," or other tangentially related businesses. You are also more likely to get so-called proprietary deal flow and get into the process earlier, when you have less of a chance of being outbidded by PE firms. If investing in your industry of speciality isn't an option, consider teaming up with another family who does have knowledge in the space. (For more on how family offices can successfully invest in complex or unfamiliar industries, see sidebar.)

3. Narrow your focus.

Carl Coughlin is partner at Coughlin Capital, a family office based in Corte Madera, CA and St. Louis. When the firm started out in 2007, it was broadly focused on investing in founder-led businesses that didn't have a clear transition plan in place. But that universe was so large that it came to be overwhelming.

"We have since narrowed our focus to logistics and supply chain services," says Coughlin. The firm chose these sub-sectors because of their existing expertise: two of their current entities are within these platforms, and their family business was a freight forwarding company which was eventually rolled up into DHL.

The improvement in deal flow was immediate. “We found that the better we defined what we were looking for, and put that out proactively on our website and on Axial, the better deals we found and the better shot we had at closing them. Once we fine-tuned that message, that’s when really good deals came to our doorstep. We were able to speak the sellers’ language and understand what’s important to them,” says Coughlin.