PRIVATE CLIENT SERVICES

FAMILY & GENERATIONAL WEALTH

JANUARY 2021

BDO

FAMILY & GENERATIONAL WEALTH

NEW VALUES, LEGACY AND RISK

With the economy under strain and social justice in the spotlight, social attitudes to wealth are changing. The next generation is also more socially conscious and values-driven, so wealth creation must be handled more delicately than ever before, while environmental, social and governance (ESG) considerations form a key pillar of private client investment strategies.

"Millennials have an attitude to wealth that borders on the uncomfortable."

The traditional bar-bell approach, with philanthropy acting as a counterbalance for wealth creation activities, has evolved. The goal is now to align wealth creation with the same values that drive the family's philanthropy.

In many sectors we are seeing the onset of economic recession leading to the exacerbation of trends that were pre-existing. Economic ill-health simply serves to throw these issues into sharper contrast. So, too, with wealth.

Culturally divergent approaches to wealth have always been visible, to greater or lesser degrees, with one philanthropy expert observing that, traditionally, there has been "an admiration of wealth creation in the US, where wealth is trumpeted more than in Europe, where things are more discreet". We must add to this cultural nuance an acknowledgement that new generations today view, and react to, wealth in different ways.

One social impact adviser describes millennial attitudes to wealth as "bordering on the uncomfortable" and there is increasingly a desire to engage with wealth in a different way. "Next gen wants to hold business and previous generations to a standard of embedding values into actions," they explain. Authenticity of approach is vital, and the next generation wants people to "walk the walk in their for-profit decision-making".

A huge, standardising force in this generational shift is the combined impact of globalisation, technology and social media.

The next generation of wealth owners may not know what an internet-less world looks like. The results are varied and numerous but include a greater awareness of what is going on elsewhere in the world.

For the wealthy, this can create both introspective thoughts about their own role in society as well as feelings of guilt about the wealth gap. "Next generation guilt draws them to beneficiary-led solutions," says the social impact adviser. "They take an entrepreneurial approach and see wealth as a tool, not an identity."

"A good reputation can take years to build but can be lost overnight."

This sentiment shift creates challenges for both current and future wealth owners, and impacts everything from investment portfolios and reputation, through to legacy and succession planning.

"The wealthy are conscious of giving back and not just taking – they understand the social importance of that," adds a wealth manager. There is a key balance to be struck involving reputation and perception management.

The media serves as a daily reminder of how quickly this can go off-kilter if it is not carefully managed.

"You don't want to be vilified by the press," says one UK lawyer, while a fintech data intelligence consultant identifies private clients' top two concerns as governance and reputational risk. "A good reputation can take years to build but can be lost overnight," they note.

FAMILY & GENERATIONAL WEALTH

QUESTIONS LINGER OVER ESG AND IMPACT

With wealth inequality now a routine part of public discourse amid economic, health and social crises, the question of whether there is an onus on the wealthy to 'do good' in the world is a common one. Philanthropy has been the primary vehicle for achieving this, but there is increasingly a view that social impact should be more directly tied to wealth creation and preservation itself.

Social impact comes in many forms, and the private client community is well-placed to deliver maximum impact, given the resources at its disposal and its dominance of investment markets. Rocket-boosters have been placed behind the ESG movement, with one wealth management professional noting that ESG offerings are now a staple part of the investment landscape, rather than a "small tributary off the main river". "It's like going to a restaurant these days and seeing vegan options appearing on menus where you wouldn't expect to see them."

Climate change and the environment, where the visible impact is clearer to see, have been joined by a renewed interest in governance issues, for instance in the wake of multinational fast-fashion retailers being found to fall short of ethical standards around working practices despite having positive ESG ratings.

Such instances of potential inconsistency have prompted initiatives to define disclosure standards (such as the Task Force on Climate Related Financial Disclosures). The surge in popularity of green finance has also led to the International Organisation of Securities Commissions formulating a framework to harmonise rules and guidance on disclosing sustainability risks. ESG as a focus area is here to stay.

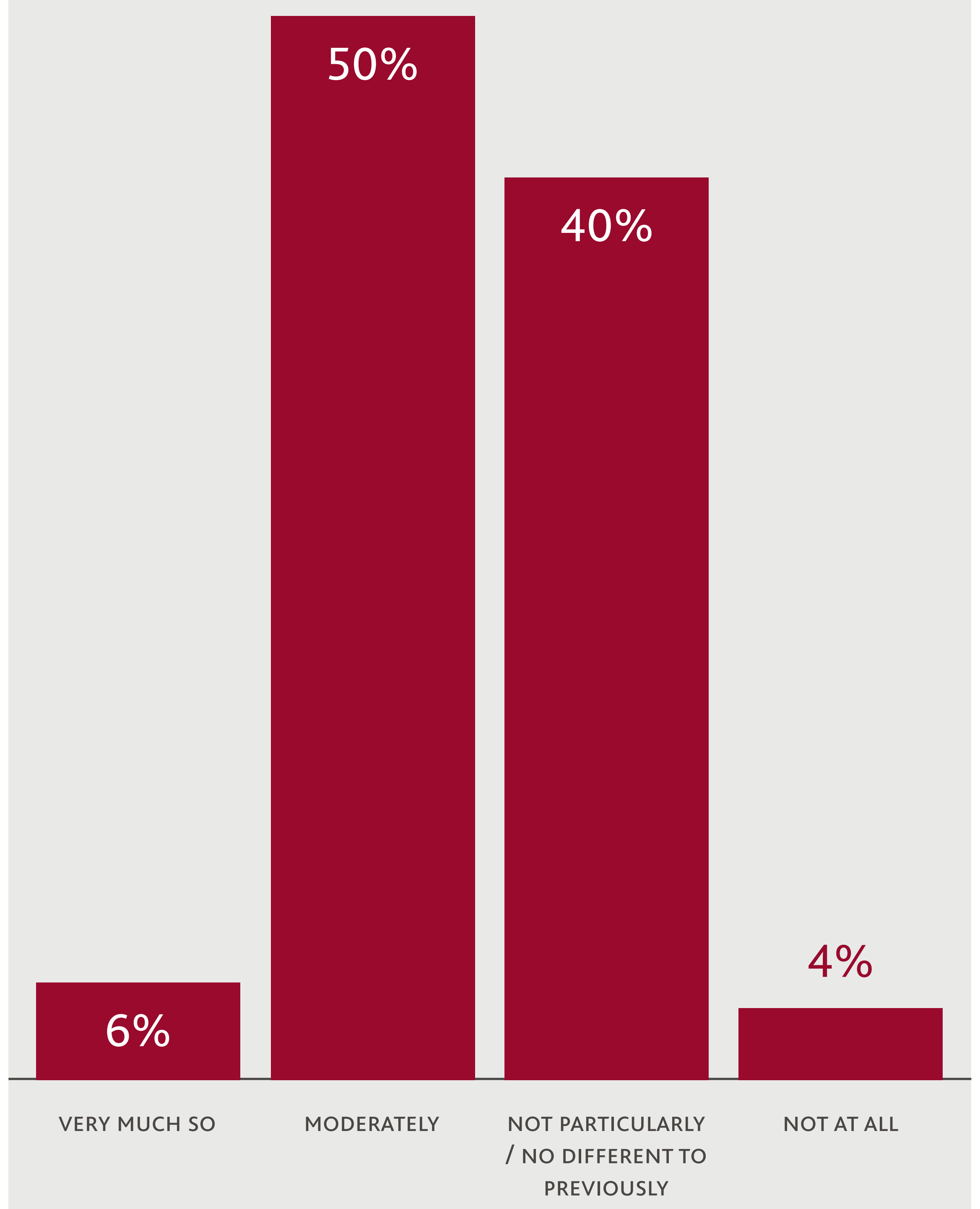
However, our data shows that scepticism remains among private clients, with 56% agreeing that ESG-related action matches rhetoric, while 44% believe a gap remains (Graphic 8).

The forward trajectory, though, is undeniable, as evidenced by providers continuing to launch and refine ESG funds. "It takes a great deal of effort and money to launch new funds," says one banking executive. "Firms don't do it for a laugh or because it's a passing trend."

Investor appetite may initially have been driven by next generation attitudes, but there is a growing realisation that this is not only a beneficial way of investing for 'good', but also a sensible part of portfolio diversification. "There's a place in any portfolio for sustainable and responsible investing," says a corporate administration and family office solutions specialist.

GRAPHIC 8:

TO WHAT EXTENT IS RHETORIC AROUND THE IMPORTANCE OF ETHICAL INVESTING TYPICALLY MATCHED BY CONCRETE ACTION AND INVESTMENT? RESPONDENTS CHOSE ONE ANSWER.



Beyond diversification, investment performance is also an attracting force. "Many are willing to see a sacrifice in financials for perceived social return," says a social impact adviser. But as the market for impact and social investment grows, returns "are at or near market levels".

As education around this area improves, the movement towards a values-driven existence, where social and financial return are linked to the same set of values, will continue apace.

As risk and reward become clearer – and performance is better tested over time – investors will not be able to ignore the opportunity. "It's a great investment option when you look at long-term performance, and does some good at the same time; that's a pretty compelling proposition," says one investment management professional.

FAMILY & GENERATIONAL WEALTH

PHILANTHROPY TRANSFORMED?

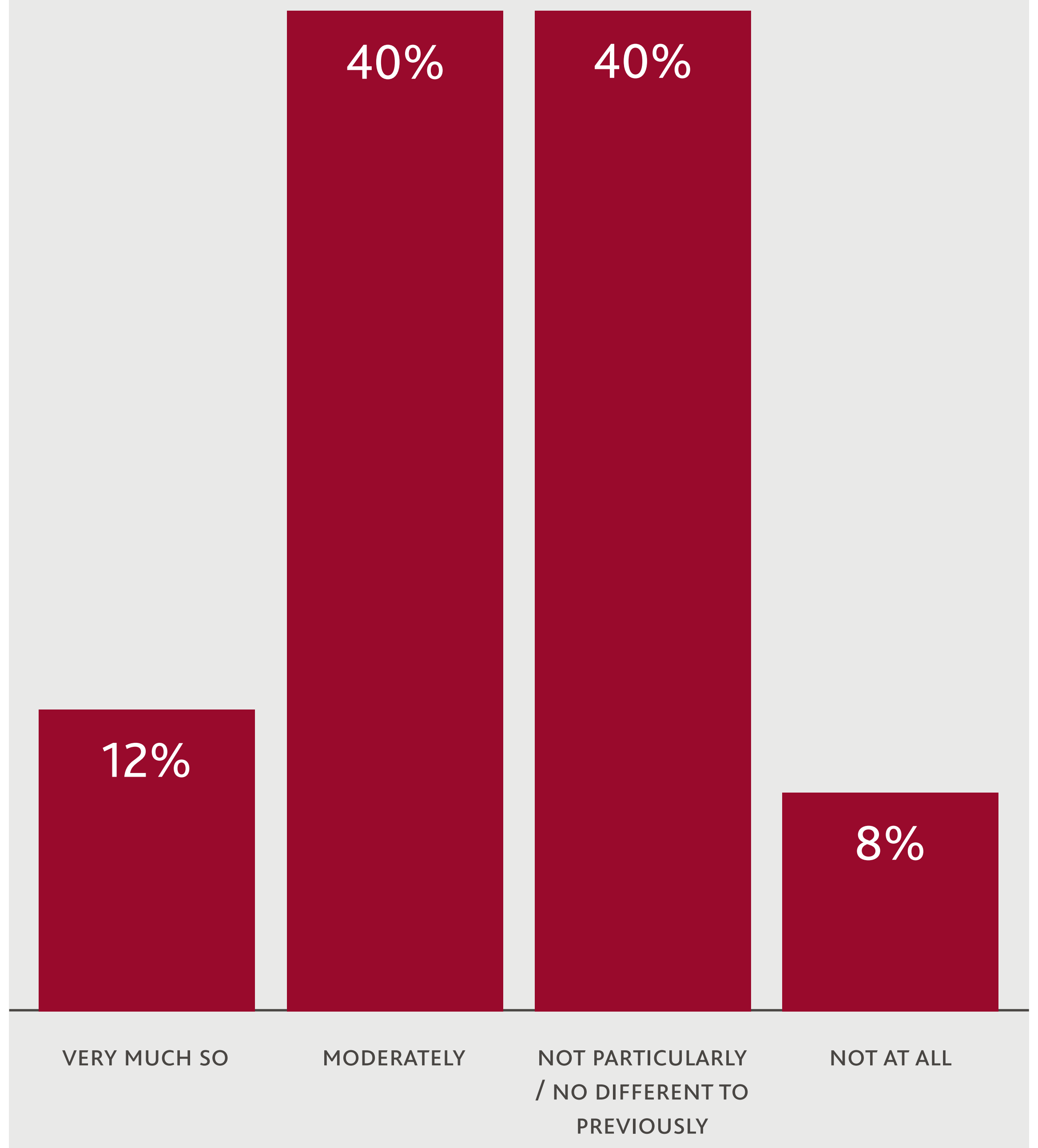
Alongside moves to better reconcile financial performance and social benefit through ESG investing, there remains a role for distinct philanthropic efforts. Whether through charitable giving, establishing foundations, or setting up donor advised funds that integrate with existing wealth management plans, wealth owners have a number of tools through which to pursue philanthropy. Again, inter-generational forces come into play.

If sceptics previously regarded charitable giving as a cathartic act, they now see a far more engaged approach motivated by not only the theoretical notion of 'doing good', but by achieving tangible impact. "It's no longer a once-a-year cheque to one particular organisation" says one financial planner who has worked in multiple jurisdictions including Switzerland and the UK. "The next generation is more hands-on, whether through fundraising, sitting on boards or being actively involved in the businesses themselves."

Next generation interest in philanthropy is unsurprising. It can be a good method for financial engagement and education, by putting the focus on people, rather than on money. Philanthropy can "bring humanity to wealth" notes one consultant.

GRAPHIC 9:

HAS COVID-19 HEIGHTENED SOCIAL PRESSURE ON WEALTHY INDIVIDUALS TO ENGAGE MORE IN ETHICAL AND PHILANTHROPIC INVESTMENT ACTIVITIES THAT DELIVER SOCIAL BENEFIT OUTCOMES? RESPONDENTS CHOSE ONE ANSWER.



As with transparency, however, philanthropy may be a double-edged sword. With a spotlight on the wealth gap, people are both aware of, and angry about, wealth inequality. In some instances, public opinion takes over and there can be "a negative perception that the uber-wealthy are dictating policy via philanthropy," says one philanthropy consultant. This may leave philanthropists in a "no-win situation" and is a reminder that while the focus is rightly on outcome and impact, not on optics, a role may remain for reputation management.

Crises often breed surges in philanthropy and this is evident on a worldwide scale with COVID-19. Philanthropy has already seen activity targeted at helping communities and health systems cope with the immediate threat of coronavirus, while the sector will also play a vital role in mitigating some of the longer-term economic fallout.

Our research shows no clear consensus on COVID-19 heightening social pressure on wealthy individuals to engage in philanthropy, with only 12.4% saying the virus 'very much' heightened pressure to give more (Graphic 9). A majority (80%) combined to say social pressure was 'moderately' heightened (39.6%) or 'no different to previously' (40%).

However, research from Candid and the Center for Disaster Philanthropy shows around $12 billion worth of philanthropic giving in the first half of 2020, outstripping donations made for any other disaster on record, so it is happening regardless of any perceived 'pressure'. BDO UK's recent publication, PrivateView on Philanthropy, takes a closer look at philanthropy in times of uncertainty, particularly this year.

Reassuringly, and as has been seen with the adoption of certain technological solutions mid-pandemic, crisis-mode administration and reduced bureaucracy has kicked in. This reduction in red tape means the lag time between pledge and impact is shortened. While some due diligence processes and governance frameworks will return, or be retrofitted, this streamlined approach should continue post-pandemic. The appetite is there; process must not serve as an off-putting factor.

FAMILY & GENERATIONAL WEALTH

THE IMPACT ON LEGACY

The values-driven investment approach as an accompaniment to distinct philanthropic giving is a prime example of how the character traits of the next generation tend to lead their approach when it comes to wealth management.

Our research shows this also has implications for legacy and succession planning discussions, with 48% saying that changing (next gen-driven) attitudes to social responsibility and philanthropy are driving new attitudes to legacy among wealthy families (Graphic 10).

Younger generations' desire to positively impact the world started the departure from status quo legacy thinking focused on accumulating and preserving wealth, and current socio-economic conditions have accelerated this trend.

Our research shows that, even where next generation is not the driving force for change, attitudes to legacy are still shifting. Graphic 10 indicates that more than two-thirds (69.2%) say this stems from the need to diversify investment portfolios amidst economic uncertainty.

Another intergenerational trend is that individuality is more frequently triumphing over traditionalism.

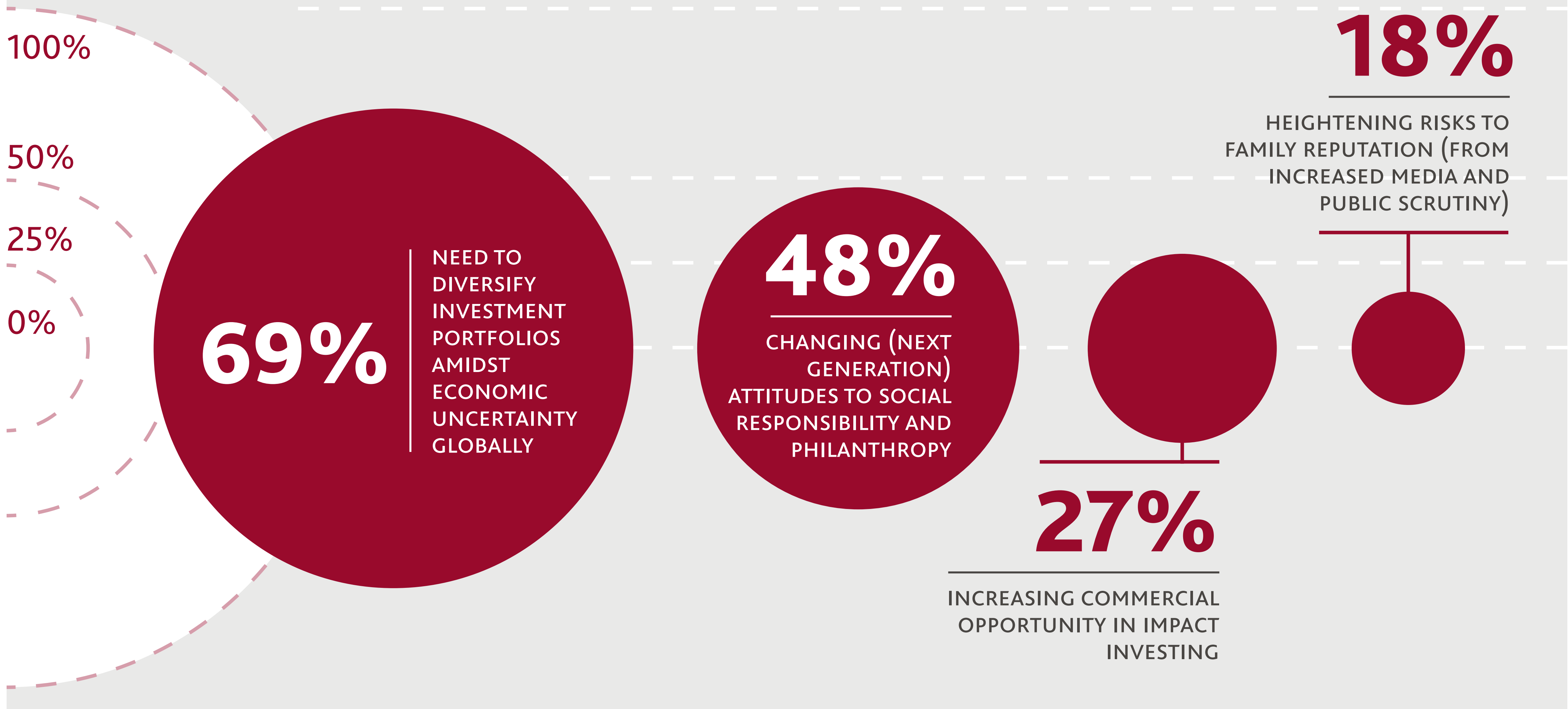
New values dictate the route forward that the next generation is forging, and diversification away from the inherited business or asset portfolio is far more common as a result. This is impacting the traditional structure of many family offices. “The current private client structure is siloed. Millennials hate hierarchy; they ask questions to challenge authority,” says one impact investment specialist, who believes this is because “they have seen authorities let them down”.

Fundamentally, the markers of success have changed. Impact sits alongside, and in some cases above, profit in the pecking order. Next generation often “see failure as an opportunity to learn, whereas the traditional private client landscape does not tolerate failure,” adds an impact investment consultant. A ‘succeed at all costs’ mentality is no longer lauded and celebrated, instead being replaced by a willingness to learn through falling short.

Incumbent wealth owners should understand the motivations of the next generation, and acknowledge that passing on wealth may need to be done completely and alongside the relinquishment of strategy oversight, even if this means successors risk potentially undoing the work of the generation(s) before them.

GRAPHIC 10:

WHAT FACTORS ARE DRIVING NEW AND CHANGING ATTITUDES TO LEGACY AMONG HNWI FAMILIES?
RESPONDENTS CHOSE A MAXIMUM OF TWO ANSWERS.



As one family office adviser observes, “even if next gen hits the buffers, they will have learnt something along the way”.

FAMILY & GENERATIONAL WEALTH

THE SUCCESSION PLANNING STRUGGLE

A vital element of private client considerations, succession planning frequently stalls due to intergenerational differences or administration anxiety. The reasons for this are complex, and often human and interpersonal in nature.

Our research reinforces conventional wisdom by showing that succession planning is a top three priority for wealth owners for the coming 12 months, but in spite of this it can still fall down. Family dynamics play a crucial role, and disputes can arise from anywhere – but more often than not, from a failure to communicate and manage expectations. People don't plan to fail, but they fail to plan.

Delaying decision-making is a tempting and easy default option, evidenced by 53.2% of respondents identifying 'lack of time and a tendency to put things off' as a common cause for failing to plan sufficiently (Graphic 11), but in some cases lack of planning itself creates disputes further down the track. Issues rarely resolve themselves and small differences now can become huge ones further down the line.

ED VAN DE VIJVER | Senior Manager, Family Business Services & Mediator specialising in conflict mediation in Family Businesses | BDO Netherlands

From a psychological perspective – and as our research shows – it can often be difficult for family members to discuss themes that simultaneously impact business and personal. Restraint and conflict-avoiding behaviour are common.

Talking about sensitive issues that could lead to conflict risks upsetting the balance, and unconsciously people steer away from it. However, this can have the opposite effect. Avoiding the issue means that communication suffers, and most conflicts are founded on the fact that people do not understand each other.

Education systems rarely teach people to talk about feelings or emotions, and this can provide barriers to success among businesses. Those that are embedded in the family's complexity may find it difficult to extricate themselves from this tension in order to make sound decisions.

That's where an adviser who has intimate knowledge of the family and business, but who ultimately sits outside the core system, can add real value. Bringing perspective, focus and instilling a systemic approach is a task that requires not only technical know-how but, crucially, 'soft' social skills."

Highest ranked among the factors hindering succession planning was another issue of intergenerational tension: the reluctance of the wealth owner to relinquish control. Any parent-child relationship can be a tough one to manage, and wealth can be a complicating factor. "Regular people have kids; wealthy people have heirs," says one family office specialist. "It's worth remembering that distinction."

Timing is key and concerns are not unfounded, with one consultant acknowledging that wealth has the potential to "stymie hunger, kill a part of the soul and distract from education". Wealth owner desires to avoid impeding the personal development of the next generation must be balanced with an appreciation that there may never be a 'perfect moment' to have difficult conversations around finance – shown by 47.2% listing 'reluctance to discuss wealth with family members' as a key failing, with a further 23.2% pointing to 'lack of knowledge on how to communicate around succession planning' (Graphic 11).

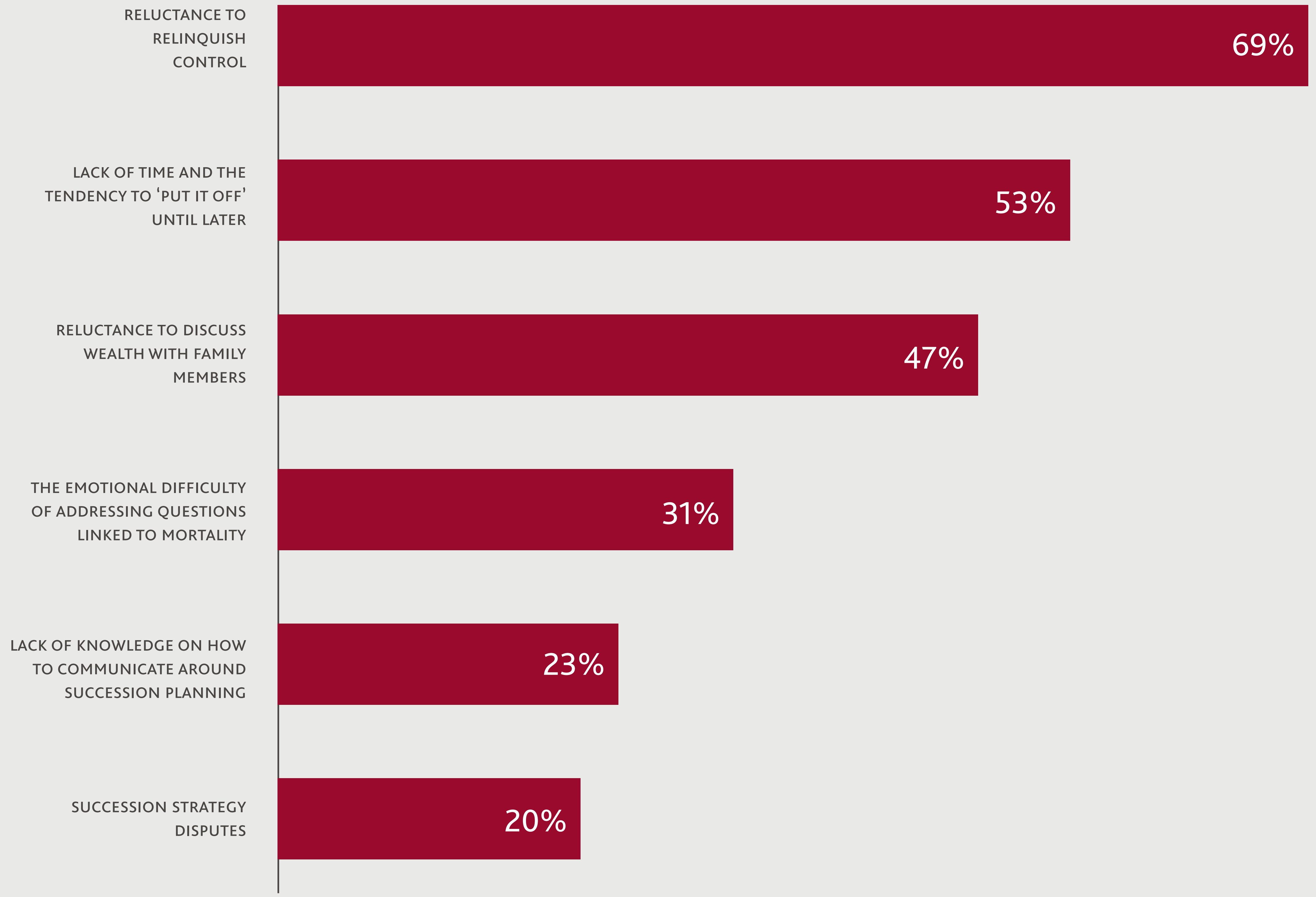
FAMILY & GENERATIONAL WEALTH

THE SUCCESSION PLANNING STRUGGLE

> *"Regular people have kids; wealthy people have heirs – it's worth remembering that distinction."*

GRAPHIC 11:

WHAT IS THE MOST COMMON REASON THAT WEALTHY INDIVIDUALS FAIL TO SUCCESSION PLAN (SUFFICIENTLY)? RESPONDENTS CHOSE A MAXIMUM OF THREE ANSWERS.



FAMILY & GENERATIONAL WEALTH

THE SUCCESSION PLANNING STRUGGLE

This shows that the prospect of having tough conversations is exacerbated by uncertainty as to how those conversations should be executed, so the challenge lies both in principle and practicality. The best advisers will act as mediating – and sometimes therapeutic – forces in facilitating discussions and then implementing plans.

Families need to understand what concerns really relate to, and then how these can be addressed. Setting an age to inherit can be arbitrary and prescriptive. What suits your family? If concerns are understood as early as possible, there are a wide range of steps a family could take to address them, such as implementing an educational programme to prepare the heirs for their new roles.

While 'disputes around succession strategy' is listed by 20.4%, the transfer of wealth is still predominantly a personalities problem, not a process problem – as one lawyer says of disputes: "they tend to be driven by family dynamics and emotion, not by structures".

Generational shifts in society make planning even harder and disputes can be more common "because next gen doesn't obey without question anymore," notes one Singaporean legal adviser.

CATHERINE GRUM | Head of Family Office Services | BDO UK

The most significant generational transfer of wealth the world has ever seen is now underway and the next generation are not passive recipients. With technology, social media and a strong sense of purpose, they are more emboldened to ask questions. They want to understand what has gone before, their full range of options and then create their own path forward. We can then expect a generation who are much more connected to and empowered by their wealth and who take a more holistic approach to their legacy, one that is about values as much as it is about money. Succession is not instantaneous but typically happens over a period of years during which intergenerational cooperation will be critical to success. The landscape is increasingly complex and those families who have properly prepared their heirs for ownership will reap the rewards during this process. There are likely to be bumps in the road however as the rising generation's views and expectations are not the same as the current generation. Effective governance will therefore be increasingly important for those families who wish to continue in some form of shared enterprise. Understanding who makes decisions, how to access information and establishing effective channels of communication will be particularly key. Without these, they may simply vote with their feet and choose the path of independence.

"The prospect of having tough conversations is exacerbated by uncertainty as to how those conversations should be executed, so the challenge lies both in principle and practicality."

A lot of focus is directed at the next generation, but control rests with the seniors and they need to be ready to move on. Supporting their personal transition can help to unblock the process.

Ultimately, both parties must come together and engage. "If the patriarch or matriarch plans in a black box and then goes under the Number 9 bus – or the private jet equivalent – that leaves the next generation outside the loop," says a UK lawyer.

Successful families have a lot going on and complexity only increases over time. Family governance provides an organisational structure to collaborate and make decisions effectively.

"Nobody puts the roof on without building the foundations first," says a family office adviser and former banker who has worked in the US, Europe and the Middle East. The best advisers will be confident and trusted enough to facilitate such discussions and ensure that the next generation – the future decision-makers – are involved in foundation-building, even where their intentions and desires may depart from that of the current wealth owner.

2021 OUTLOOK:

FROM CAREFUL ADJUSTMENTS TO DECISIVE ACTION

While our research reveals the scale and extent of the change that 2020 has thrust upon the world of private clients, it also shows that the fundamental principles wealth owners live by are being adapted, rather than replaced.

Our findings indicate that the appropriate initial response to radical reset is careful adjustment, not knee-jerk reaction. This culture of adaptability and measured response is not new, but its application is. Diversification and opportunity-spotting in reaction to outside events and forces has always been part of sensible wealth management. It is now applied to all aspects of wealth owners' lives.

At the same time, the events of 2020 were unprecedented, so wealth owners remain alive to the need for further change. We have discussed how continued success will rely on thoughtful decision-making that is responsive to change while staying true to the principles that underpin a longer-term outlook.

2021 OUTLOOK:

FROM CAREFUL ADJUSTMENTS TO DECISIVE ACTION

We expect the demand for family offices to continue to grow, as 2020 has given families an opportune moment to take a step back, rethink, plan and start to put in place their succession arrangements. The family office completes the puzzle by providing the basic fundamentals required for this planning phase and set succession planning on a sustainable footing.

But as the themes we have tackled continue to flex throughout the coming year, re-evaluation of priorities will continue to occur. More radical alterations may be warranted as certain trends become permanently embedded while others are shown to be temporary and are duly swept aside.

So, how will our four pillars stack up in 2021?

Transparency will continue quickly. The resolve of national authorities will surely increase, and the tolerance of non-compliance will fall, as recession deepens and governments seek funds to pay for COVID-related policies that have supported the economy in the short-term. Policymakers will keep a watchful eye on the wealthy as they seek to strike a balance between the goal of stimulating the economy and the risk of driving investment away if the taxation 'stick' is wielded too forcefully.

COVID-related restrictions are already impacting **relocation** strategies, and will continue to do so, but at some point cross-border activity and movement will return more fully. We are seeing individuals wanting to return to their "home" country where that country has COVID-19 largely under control. This is in turn leading to a surge in demand for property rentals and purchases in some jurisdictions. Wealth owners should assess (and are already assessing) their priorities and options now in order to act swiftly when the time comes.

We should not ignore the potential for a global pandemic to accelerate **inter-generational change**, both due to modified mind-sets and the mortality implications of COVID-19. Right now, it is impossible to imagine a world without COVID-19 but, even in its absence, new social norms and a focus on ESG serve as accelerating forces. The role of the current wealth holders will increase as they actively plan to pass on their wealth and educate the next generation. The only constant is change – but what positive forces can we expect to see within wealthy families, as the 'react' phase ends and the 'resilience' and 'realise' phase begins?

So, too, for the **adviser of the future**. As wealth owners (and wealth itself) change, they bring with them new expectations. However, while everything else around us changes, client satisfaction must not. One thing that is certain is that business as usual no longer exists. Private client advisers must remain alive to shifting needs as the private client landscape and the wider world evolve.

For now, the pursuit of stability remains the order of the day. As the fallout from 2020 continues to crystallise, and with the aid of additional clarity, wealth owners will be able to turn measured responses into more meaningful, longer-term action plans.

This report is the first instalment of a multi-year initiative designed to track and monitor sentiment within, and directed towards, the private wealth community, as well as analysing wealth-holder attitudes and strategies year-on-year. If you would like to discuss this year's findings, or take part in next year's research, get in touch with us – just search '**BDO World of Private Clients**', or contact your local adviser opposite.

Read our full report to see the wider analysis of our four themes.

KEY CONTACTS

JEFF KANE
CHAIR OF GLOBAL PRIVATE CLIENT STRATEGY GROUP | BDO USA

WENDY WALTON
HEAD OF GLOBAL PRIVATE CLIENT SERVICES | BDO UK

DEBORAH GRAYSTONE
LEADER OF GLOBAL PRIVATE CLIENT STRATEGY GROUP, AMERICAS | BDO CANADA

TAMARA PETERS VAN NEIJENHOF
LEADER OF GLOBAL PRIVATE CLIENT STRATEGY GROUP, EUROPE | BDO NETHERLANDS

MARK POLLOCK
LEADER OF GLOBAL PRIVATE CLIENT STRATEGY GROUP, ASIA-PACIFIC | BDO AUSTRALIA

BRAD NORRIS
ASSOCIATE DIRECTOR, GLOBAL PRIVATE CLIENT STRATEGY GROUP | BDO UK

VICTORIA BAK
BUSINESS DEVELOPMENT & MARKETING MANAGER, GLOBAL PRIVATE CLIENT STRATEGY GROUP | BDO UK

42009881