Families play a significant role in the economies of Asia. Understanding their goals as business owners and investors is vital to building productive, long-term relationships. To efficiently capitalize on this dynamic, the private equity industry must consider the role of families in Asia in a holistic manner.

In two concurrent research projects, INSEAD’s Global Private Equity Initiative (GPEI) explores the main opportunities for interaction between private equity and regional families: industry investment in family businesses as partners for growth and family investment in the private equity asset class as LPs or via direct and co-investments.

Partners for Growth: Family businesses often benefit from an infusion of “smart money”, i.e. capital and expertise from growth equity funds. This is particularly prevalent in emerging Asia, where the Emerging Markets Private Equity Association (EMPEA) notes that growth capital investments accounted for 72% of private equity transactions and 54% of private equity invested capital in emerging Asia between 2009 and 2013. Getting this dynamic right is particularly important in South Asia, where family businesses account for 80% of economic output in India and Indonesia, 70% in Singapore, and 60% in Taiwan.

The private equity industry must
be mindful of the unique characteristics of a family business when considering a partnership with family businesses in the region. In many instances the goals of a family may extend beyond pure value maximization of its business, as the business may provide employment for family members and contribute to a family’s legacy and standing in the community. In addition the business might represent only a portion of a family’s wealth leading to situations in which the family will fully rationally prioritize their wider commercial interests over the specific interests of one individual business. In addition, the oftentimes personal loyalty of employees to the family and omnipresent role of the family at all layers of the business must be recognized, with final decision-making authority on a wide range of topics – from business-critical to the mundane – often resting with the family.

However, these family dynamics cut both ways, as insular decision-making and risk aversion can mitigate the business’s ability to capitalize on opportunities. Private equity’s partnership with a family business can thus infuse both the capital and know-how to tap new growth and professionalize an operation.

Private Equity Investors: Asian families are playing a growing role in global private equity. Data points underscore the opportunity for private equity funds to source LP capital from the region: the Ultra High-net-worth individuals population with assets in excess of $100 million increased 116% between 2003 and 2013 to 10,740, and roughly 40% of the publicly-traded family businesses in Asia were listed since 2000. GPEI’s interviews with more than 25 regional family offices have revealed that as families employ a more institutionalized approach to wealth management – increasingly via a family office structure – their ability and tendency to allocate to alternative asset classes increases. Private equity funds have been a direct beneficiary of this trend, as families become more comfortable with long-term capital commitments to the industry and increasingly look to diversify their portfolios in particular via allocations to developed market managers.

In addition to their historic direct investing through family businesses, families in Asia are partnering with private equity funds in co-investment opportunities in the region’s growth businesses. Established families can generate significant deal flow from their personal networks, and can provide private equity investors increased access to deals in a region that often lacks financial intermediation. According to a 2013 UBS/ Campden survey of family offices, allocations to direct private equity investments jumped from 4% of portfolio assets in 2012 to 15% in 2013. As our research revealed, this is often a function of the youth of many large regional family businesses and family offices relative to their developed market peers, with first and second generation wealth creators exhibiting strong entrepreneurial spirits and a higher willingness to take on risk. This risk is however balanced by a strong preference for investments in sectors and geographies in which a family has close ties and deep experience, often via its commercial business interests, bringing the topic of private equity and families full circle.

As private equity players refine their strategies for the Asian market, understanding the goals and priorities of families in a holistic manner will benefit both their fundraising and investment activity.