GFG CAPITAL
A FAMILY OFFICE

VIEWS FROM THE BRICK

REIMAGINING ROI

Return on investment. What is it? Well, it's pretty simple really; you put capital in and you get something in return. But what if it didn't have to stop there? In fact, what if we told you that there was an investment approach that let you judge your investments by much more than the four or five digits on your account statement? Conscious investing is nothing new, but it's seldom talked about. We think that's all about to change in a very big way. So, since you're here, let's reimagine ROI.

WHAT IS A CONSCIOUS INVESTMENT MINDSET?

Traditionally, investors have sat down with their respective advisors (or on their own) and have tried to navigate the investment process of building a portfolio that makes sense for them. The investment policy checks all the boxes: risk profile, return objectives, time horizon, liquidity needs, etc. But there's one part of the process that can help align what you concern yourself with in your everyday life with your investment portfolio. Those unique characteristics that make you *you*, can make their way into your portfolio. On top of your portfolio being a more direct reflection of yourself and values, it could end up being set up for potentially better risk adjusted returns as time unfolds. Research shows that this conversation is becoming more and more common among high net worth individuals and families across the globe, making it an undeniable tsunami of change ready to hit Wall Street. The Global Sustainable Investment Alliance notes that at the end of 2015, more than $22.8T globally was invested in Environmental Social and Governance mandates (ESG). That was a 25% increase from 2014[1]. UBS has reported that family offices have seen steady increases in demand for these conscious investments[2]. And these concerns and conversations being initiated by the end investors have gotten the attention of corporations across the globe as well; impacting how they approach their operations day in and day out.

SOURCE:[1] Data provided by the 216 Global Sustainable Investment Review. [2] UBS 2016 Family Office Report.

EVERYTHING IS CONNECTED...

So once you've subscribed to the conscious investment mindset, where does the economic value come in? Well let's break it down with a quick illustration. Pretend you're a CEO in today's business environment, you have no shortage of issues on your plate. As consumers continue to push the better business practice renaissance forward, you are going to think twice about being on the wrong side of history. Enter: cost of capital. Anyone who's taken an introductory level business class might remember this, but here's a refresher: the cost of capital can be defined as the cost of funds used to finance a business, generally made up between equity and debt issued in a company's capital structure. When determining if your company should be taking on a new project, a discount rate is placed on future cash flows anticipated throughout the life of said project. Now, if your company is not virtuous in nature, investors will command a greater required rate of return from your firm. This consensus view on your firm by the Street will soon enough make its way into your company's boardroom. Therefore, through your analysis process of a particular project, the costs of funding projects will continue to increase, decreasing the potential profitability for the firm and, in return, your investors. All of this stems from those initial steps of investors' portfolio construction process of aligning their investments with their values. And are corporations taking notice? Yup. The University of Oxford has conducted studies on this matter in particular. Their results have shown that 90% of the 200 studies analyzed conclude that adhering to ESG practices reduced the cost of capital for their firms. [3]

GOING BEYOND IRR

Once you've determined you want your investments to be a reflection of your values and that better business practices can lead to greater risk mitigation, what are you trying to accomplish beyond your own IRR? Great question. There are several measuring sticks that have been acknowledged on a global level that help us track the tangible progress we can make towards a more responsible, inclusive and sustainable global economy such as Principals for Responsible Investments (PRI), B-Corp Certification and the United Nations Sustainable Development Goals (UN SDGs) to name a few. As consumers, we have shown increasing likelihood of aligning ourselves with companies that acknowledge and align themselves with these standards. Global consumers surveyed state that they hold the same standard to their personal lives: 84% say they seek out responsible products whenever possible[4]. As global citizens we've voiced our demand for these standards to be common practice. And as investors, we can use these same standards to measure our impact. Many asset managers will use the UN SDGs as justification and key performance indicators (KPI) for their underlying security selection. Some of these goals that investors can help achieve within their portfolio include: responsible consumption and production, climate action, affordable clean energy, no poverty, and gender equality (there are 17 SDGs).

While these measurements are popular within the public markets and commonly referred to in ESG, SRI and thematic investment mandates, there's also the option on the far end of the spectrum: impact investing. Impact investing can help investors identify and carry exposures to very specific themes, projects and regions they identify with. Much like traditional alternative investments (oxymoron?) impact investing generally requires some kind of liquidity sacrifice. These investments differ from their public market counterparts in the sense that they often times carry a double bottom line mindset of social impact along with economic return.

SOURCE:[3] From Stockholder to Stakeholder, 2015. [4] 2015 Cone Communications/Ebiquity Global CSR Study.

Not to be confused with philanthropy, these are still investments that carry potential for personal economical return.

TSUNAMI WARNING

Let's reiterate something before we continue. A conscious investment mindset is something that the investor must choose to carry within their portfolio. What we've discussed so far are options an investor should be made aware of when deciding how they want their portfolio to look and feel, and what they can potentially accomplish as an outcome of it. The conscious investment mindset is a blend of subjective points of view and objective facts based on trends and financial performance. We certainly acknowledge an investor's ability to construct a portfolio and not pay these factors any attention. But there is one thing left that all investors should at least be aware of. This is your official tsunami warning. Generational shifts are some of the most powerful forces within our known universe. Each generation seems to carry signature characteristics that have defined them throughout history. Millennials have been the largest generation in the world since the year 2000, and will be until the year 2040 according to the US Census Bureau [5]. To this point they (we) have not been given the opportunity to shape the world we live in. But the transfer of wealth is about to provide an unstoppable wave to provide momentum for this demonstration. Over the next 30 years, $30 trillion in financial assets will pass from baby boomers to their heirs in North American alone. At its peak, from 2031 to 2045, 10% of total wealth in the United States will be changing hands every five years [6]. So if you have a portfolio exposed to such powerful forces of nature, why not try to at least understand who these investors are? If you've never met a millennial, here's a quick profile.

- 58% of millennial classify themselves as entrepreneurs
- 92% are contributing their skills to a company they feel is making a difference in the world
- Millennials are 1/3 more likely to seek employment opportunities aligned with their values
- They are twice as likely to purchase a good based on social or environmental impact
- Millennials are twice as likely to choose an investment fund that specifically uses social or environmental practices as a way to create a value differentiation
- 7/10 have said that investment decisions are a way to express their social, political an environmental values
- Today, millennials account for 11% of high net worth individuals in the United States

And don't look now, but these characteristics are already impacting family portfolios. The UBS Global Family Office report shows that two thirds of families with children born after 1980 will see an uptick in impact investing requests. Another study shows that, in 2016, more than one in five professionally managed dollars in the United States were allocated to some form of socially responsible mandates [7].

Ready or not, here they come.

-p&t

SOURCE: [5] Bloomberg. [6] Accenture Great Wealth Transfer. [7] Morgan Stanley Institute for Sustainable Investing.

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