Asset Management
Market commentary
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CREDIT SUISSE

Trust – the alpha factor for family-owned companies

March 22, 2022 – **Family-owned companies are the key driver of the economy and have in general performed well over time, something that was not least apparent during the COVID-19 pandemic. According to Gianfranco Iafigliola, a fund manager at Credit Suisse, family-owned companies can represent appealing investments in all stock-market phases for investors with a long-term investment horizon. He believes the reason for this is a crucial but invisible alpha factor: trust. This is particularly relevant in the uncertain current market environment.**

People spent much more time at home than usual during the COVID-19 pandemic. This enforced isolation spawned any number of interesting business ideas in our view, as is clear from the much higher number of company start-ups during this period. Even though only a small proportion of all newly founded companies will succeed in the longer term, we consider family-owned companies and the associated entrepreneurial spirit the key driver of the economy. Family-owned companies are estimated to account for almost two thirds of all global companies, and for some 70% of global GDP1. Time and again, these companies have shown an ability to withstand periods of economic crisis, reinvent themselves, and remain relevant in different market phases in our view. Well-known examples of large family-owned companies include the likes of Hermès, Merck, and L'Oréal.

Family-owned companies outperform the wider equity market

This resilience and dynamism has not gone unnoticed by the investment community. A number of studies show that family-owned companies outperform the wider equity market over the long term. An analysis of family-owned companies published by the Credit Suisse Research Institute puts this performance superiority compared to other companies at 4% since 20062. What's more, this strong track record persisted through the pandemic. Once again, these companies demonstrated that their blend of entrepreneurial spirit, agility, and prudent company management together with a low level of indebtedness enabled them to adapt rapidly to new market parameters in our view. This ability to withstand crises was more important than ever in 2020 and 2021 and was rewarded by the stock market accordingly. Another reason for the outperformance of family-owned companies during the pandemic in our view was their sector focus: family-owned companies are strongly represented in the consumer goods and industrial sectors, but are also positioned for long-term success in the healthcare and IT sectors.

Family-owned companies focus on sustainable profitable growth

Successfully managed family businesses rank among the so-called blue chips of the equity market. With their strong corporate culture, long-term investment horizon, pronounced culture of innovation, and robust balance sheets, family-owned companies typically focus on sustainable profitable growth. Over the last decade, which has been

[1] KPMG (2015). European Family Business Trends, https://assets.kpmg/content/dam/kpmg/pdf/2015/12/european-family-business-trends-2015.pdf
[2] Credit Suisse Research Institute (2020). The Family 1000: Post the Pandemic, https://www.credit-suisse.com/about-us-news/en/articles/media-releases/family-owned-businesses-show-resilience-through-pandemic-202009.html

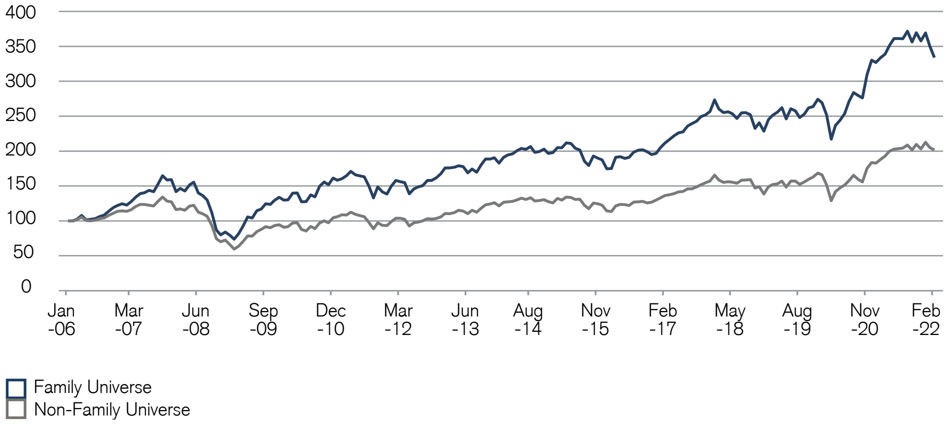
characterized by low interest rates and economic uncertainty, family businesses of this kind have been strongly in demand due to their consistent operating performance. In many cases, this has driven a strong rise in valuations. However, against a backdrop of higher rates of inflation and the likelihood of interest rate hikes on the part of the US central bank (Fed), many of these stocks have come under huge pressure recently.

Research suggests that family-owned companies lag the market at times of strong cyclical recovery and rising interest rates, due to their quality bias. Although Russia's invasion of Ukraine and the consequences for the global economy raise a question mark over the magnitude of the cyclical recovery, inflationary pressures and the associated expectation of rising interest rates remain in place.

Family companies enjoy the trust of investors

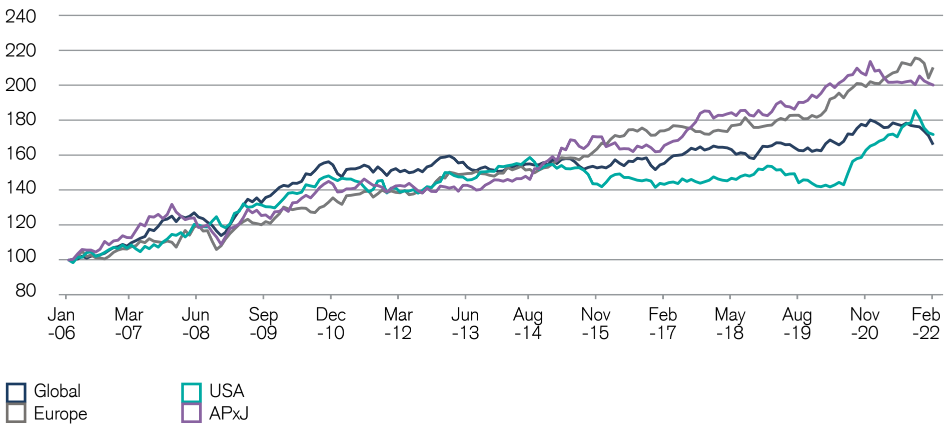
Investing in family-owned companies in phases of rising interest rates is nonetheless worthwhile in our view. We believe the reason for this is their crucial but invisible alpha factor: trust. Thanks to their entrepreneurial loyalty, family-owned companies are more likely to respect the interests of their clients, employees, and business partners, and indeed fulfill their social responsibilities. They are also more likely to reinvest profits in the business. This creates trust, which is the key to their success. Even if the stocks of certain successful family-owned companies are likely to experience valuation corrections in the short or medium term, we believe this is unlikely to damage the trust of investors over the longer term. In summary, participating in the innovative spirit and vision of family-owned companies over the long term and remaining invested in these stocks holds plenty of appeal in our view.

Chart 1: Returns of family-owned vs. non-family-owned companies, weighted by market capitalization and sector-adjusted



Source Credit Suisse Research Institute

Chart 2: Family alpha by region – relative performance of family owned versus non-family-owned companies



Source Credit Suisse Research Institute

Historical performance indications and financial market scenarios are not reliable indicators of future performance.

Further information

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Credit Suisse Asset Management

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