DUE DILIGENCE – WHAT IS IT AND WHY IS IT IMPORTANT TO MY FAMILY?

Due diligence is the industry term used to describe the myriad of activities associated with evaluating an investment proposal or manager. The fundamental goal of a due diligence process is to identify discrete risks and opportunities of an investment offering, fund or manager in advance investment. Biltmore Family Office (BFO) searches for investment managers that will drive return out of a special investment edge, a market inefficiency, and/or a temporary mispricing. These managers are hard to find, and frequently, even harder to assess. We've written this piece to shed light on the our approach to manager assessment.

DUE DILIGENCE AT BILTMORE FAMILY OFFICE – A DISCIPLINED PROCESS

We believe that manager due diligence is best designed as a clearly defined and disciplined multi-step process that takes at least three to six months to complete. Our BFO process is designed into four key steps: initial manager sourcing and screening, deep dive due diligence, grading, integrity checks and once we're invested ongoing monitoring.

Sourcing and Screening (Level I)

- Idea generation: Conferences, Network, Inbound Inquiries
- Conference call with manager
- Broad understanding of strategy
- High level performance & risk reviews
- Network cross-referencing
- Research team approval

Deep Due Diligence (Level II)

- Extensive document request
- In-depth qualitative review
- Quantitative performance analysis
- Compliance policy review
- Operations review
- Site visit
- Exhaustive work product reviews
- Evaluate investment terms

Manager Grading (Level III)

- Weighted multi-factor risk score
- Risks classification across five categories:

1. Execution
2. Business
3. Integrity
4. Portfolio
5. Strategy

- Research Team review
- Investment Advisory review

Integrity Checks (Level IV)

- LexisNexis background checks
- References: Colleagues & Clients
- Service provider calls

MANAGER SOURCING AND SCREENING

Once we identify an investible opportunity, we seek out a broad array of investment managers focused on that given opportunity. Simply sourcing managers according to track record or pedigree does not assure successful returns. We are introduced to managers from a variety of resources: referrals from fellow family offices, existing fund managers, independent research services, conferences, and frequently from our client families.

DEEP DIVE DUE DILIGENCE , INTEGRITY CHECKS AND GRADING

In addition to running an investment strategy, an investment manager also runs a business. We seek to allocate to investment firms with the talent to excel at both investments and internal operations. Our process is designed to provide an in depth review not only of the investment offering but also a thorough operational assessment of the investment manager.

Rather than a formulaic, check the box process, we focus on answering questions we really want to know:

- Is the manager skilled or lucky?
- Does the manager have a special edge?
- Are we likely to get paid sufficiently for our risk?
- Does the management do what it says?

Ultimately we ask over 60 questions about the manager. We interview portfolio managers, analysts and business professionals, review legal documents, letters, and marketing materials, and we perform quantitative analyses on the fund. Each question represents a discrete risk. The risks are categorized and graded into five broad categories:

1. **Execution risk** - the risk of investment returns not delivering according to expectations
2. **Business risk** - the operational risk inherent in running a business
3. **Integrity risk** - the conflicts of interest between the manager and the investors
4. **Portfolio risk** - the controllable risks within an investment strategy
5. **Strategy risk** - the uncontrollable risks within an investment strategy

We grade the responses to each risk metric from excellent (5) to poor (1). Imbedded into the process is our series of integrity checks. At the outset, we look for a trusted source to "vouch" for the integrity of the manager. Typically, this come from a fellow investor. As part of grading on each manager, we perform LexisNexis background checks, 3rd party servicer interviews, personal reference checks, and social media checks. Once a manager is through the process we have a thorough 360 degree view of all of the potential risks and returns within an investment.

MONITORING DUE DILIGENCE

Making an investment with a manager is not the end of our due diligence, rather it is one part of the process that will continue over the course of our investment. The ongoing monitoring of an investment manager's strategy, personnel, or opportunity can offer early signs of performance challenges. As part of our BFO monitoring process, we conduct three quarterly conference calls and one annual on site assessment. We believe that the decision to move away from a manager is just as important as the original decision to invest.

SUMMARY

Given the number of investment options available to your family, an established and repeatable due diligence process is critical. The importance of this process cannot be overstated as the range of returns across fund managers is wide and the chance to make mistakes is varied. It is easy to be seduced by the manager's pedigree or exclusivity. It is difficult to differentiate marketing expertise from investment expertise. We require protection from chasing investment returns. We require experience to avoid missing operational or regulatory concerns. Above all, we need a consistent, repeatable process to achieve these goals. At Biltmore Family Office, our due diligence process is central to providing the best investment expertise to all of our families.

BILTMORE FAMILY OFFICE
A FAMILY OFFICE FOUNDED BY LIKE-MINDED FAMILIES

BFO is an SEC registered advisor founded by families to solve for their real-life wealth challenges:

INVESTMENTS
ESTATE PLANNIG
TAX PLANNING
GOVERNANCE
FIDUCIARY
RISK MANAGEMENT

As time passed, other similar families joined to access independent wealth advice in a boutique, intimate setting. Joining Biltmore, they became more than clients. They became part of the cultural fabric that makes Biltmore different.

Some call it a multi-family office. We call it a COLLABORATIVE FAMILY OFFICE.

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