

NEW MEXICO EDUCATIONAL RETIREMENT BOARD

INVESTMENT COMMITTEE

TELEPHONIC/VIRTUAL MEETING

April 16, 2020

1. a. CALL TO ORDER

A meeting of the New Mexico Educational Retirement Board Investment Committee was called to order on this date at 1:00 p.m. via teleconference.

Members Present:

Mr. H. Russell Goff, Chair

Ms. Mary Lou Cameron

Mr. Larry Magid

Members Excused:

None.

Staff Present:

Ms. Jan Goodwin, Executive Director

Mr. Rod Ventura, Deputy Director

Mr. Bob Jacksha, Chief Investment Officer

Mr. Steve Neel, Deputy CIO, Alternative Assets

Mr. Mark Canavan, Real Estate & Real Assets Portfolio Manager

Ms. Susanne Roubidoux, General Counsel

Ms. Kay Chippeaux, Deputy CIO, Public Markets & Credit

Mr. Lawrence Esquibel, Chief Information Officer

Mr. Alan Myers, Operations Manager

Others Present:

Mr. Allan Martin, NEPC

Mr. Sean Gill, NEPC

Mr. Colton Lavin, NEPC

Mr. Kevin Bliss, NEPC

Ms. Noi Spyratos, CBRE Caledon

Mr. Connor Jorgensen, LFC Analyst

Ms. Judith Beatty, Recorder

b. Approval of Agenda

Mr. Magid moved approval of the agenda, as published. Chairman Goff seconded the motion, which passed unanimously.

c. Approval of Minutes: March 19, 2020

Mr. Magid moved approval of the March 19 minutes, as submitted. Chairman Goff seconded the motion, which passed unanimously.

d. Introduction of Guests

Chairman Goff welcomed staff and guests.

2. VISTA CREDIT PARTNERS III – OPPORTUNISTIC CREDIT

[Presenters: Kay Chippeaux and Allan Martin and Colton Lavin, NEPC]

Ms. Chippeaux presented staff's recommendation of a \$100 million commitment to Vista Credit Partners Fund III for the Opportunistic Credit portfolio. She stated that Vista Credit Partners is the credit platform of the private equity group, Vista Equity Partners, and both are focused on enterprise software businesses, data and technology-enabled businesses sectors. Vista Credit has a very high underwriting bar for companies to qualify for financing, a process that seeks to ensure that companies are able to operate and succeed, no matter the economic environment. They are investing mostly in North America and mostly in the first lien position of capital structures. The capital coverage is usually strong with low loan to value, and historically, Vista Credit has very low loss ratios.

Ms. Chippeaux said this is a somewhat esoteric investment manager in an area where the ERB does not have any exposure. She said she was impressed by their solid business plan and underwriting, and since meeting with them in Santa Fe and New York, she is further convinced that they have identified a unique opportunity and are well positioned to execute this strategy.

Ms. Chippeaux said Vista had nothing to disclose in the disclosure documents submitted to the ERB; however, NEPC did disclose that NEPC's director of global research, Neal Sheth, is the brother of Brian Sheth, president of Vista Equity Partners. ERB staff found this interesting but not influential in the decision to pursue this opportunity.

Mr. Martin stated that, because the ERB's portfolio has been conservatively positioned to begin with, it hasn't faced the extreme need to worry greatly about liquidity, and so today it is in a position to take advantage of this bad market to buy access that would have cost more money a while ago. He suggested that nobody knows what the outcome of this virus is going to be, and while most are expecting a v-shaped recovery, others are saying it could be a u-shaped recovery, which could potentially be a depression that could rival the markets in 1929, and where lending people money at the start of that is a concern. NEPC feels, however, that lending is generally a good strategy at this time. He pointed out that the ERB has a very well diversified private debt portfolio, so focusing on some of the niche sectors like software, which is a very fast growing part of the overall economy and therefore less susceptible to a decline, should give the ERB some comfort.

Mr. Lavin discussed NEPC's due diligence, experience and research in Vista Credit Partners, as well as what NEPC likes about Vista's strategy.

Mr. Lavin said NEPC supports staff's recommendation for this investment.

[Ms. Cameron joined the meeting.]

David Flannery, president of Vista Credit Partners, and Cheryl Leahy, vice president of investor relations, joined the meeting and made a presentation.

Mr. Jacksha asked if there are any “problem children” in the Fund II portfolio that have issues and might take time to manage away from Fund III. Mr. Flannery responded that they fortunately have none and are going into this crisis with the Fund II portfolio being in very good shape. He commented that any companies having problems “pre-Covid” would have real problems “post-Covid,” and Vista doesn’t have that. He said they have no companies in the portfolio that have any serious covenant defaults.

Mr. Jacksha asked what they are seeing in terms of pricing on the loans they have been getting since 2019, and how much has that changed in their particular sector. He asked what form of leverage they use.

With respect to pricing, Mr. Flannery responded that they source their deals from different channels, which is an advantage for Vista because they can move between different parts of the market to source the best risk. In 2019, they saw some price compression in a reasonably frothy market, but not every lender is well versed in software companies or knows how to think in those terms, so Vista has an embedded advantage in that.

In terms of leverage, Mr. Flannery responded that they use some CLO bonds-type leverage, all of them non mark-to-market. In Fund III, as they move through this year and part of next year, they would look to do a lower levered CLO, and they also have bilateral lines of credit with JP Morgan and Wells Fargo. He said JP Morgan recently underwrote their platform from a credit perspective.

Ms. Chippeaux asked Mr. Flannery to discuss exit strategies and whether those would change in the current market.

Mr. Flannery responded that there is currently a lot of merger and IPO activity, and that has typically been their exit out of individual loans. He said he thought that would continue, but at a slower pace, so they would hold onto loans for a bit longer. He said he wasn’t concerned about this at all. He said there would be more consolidation happening later this year and next year in their sector, which is how they will be refinanced out, and the equity market would eventually come back, too.

[Mr. Flannery and Ms. Leahy signed off.]

Mr. Jacksha commented that this is a timely investment, because the ERB wants to look for more stable companies because the environment is volatile. In addition, this is an area the ERB doesn’t have much exposure to in the investment portfolio, so this is a good addition.

Ms. Chippeaux said Vista maintains low LTV's in the portfolio and has a very good reputation among software companies. As a firm, they can execute and execute fairly, so this is a very good base for them to continue.

Mr. Magid moved that the Investment Committee approve a commitment of \$100 million to Vista Credit Partners Fund III for the Opportunistic Credit portfolio. The commitment is subject to New Mexico State Law, Educational Retirement Board policies, Educational Retirement Board approval for placement agencies, negotiation of final terms and conditions, and completion of appropriate paperwork. Ms. Cameron seconded the motion, which passed unanimously.

3. BEACH POINT TACTICAL OPPORTUNITIES FUND – OPPORTUNISTIC CREDIT

[Presenters: Kay Chippeaux and Allan Martin and Kevin Bliss, NEPC]

Ms. Chippeaux presented staff's recommendation of a \$75 million commitment to Beach Point Tactical Opportunities Fund for the Opportunistic Credit portfolio. She said this is a new fund with one of the ERB's longest serving managers in this portfolio who has managed a very large slice of that portfolio for many years. Beach Point Tactical Fund is targeting opportunities within distressed debt, special situations, and private equity, and will seek to invest in mid-sized, complex, and out-of-favor US companies. She said the background of the Beach Point investment professionals in bankruptcy and securities law would benefit this fund. The goal of the fund is to provide a more concentrated vehicle for high alpha opportunities with longer investment horizons in generally more complex investments. This will be a new addition to the Beach Point platform, targeting illiquid opportunities with higher target returns than more liquid Beach Point strategies.

Ms. Chippeaux said this fund will fit well into the Opportunistic Credit portfolio, especially in the current market environment and the current expectations from distressed opportunities in the next couple of years.

Mr. Martin stated that there are countless opportunities to invest in distressed debt in the current environment, and this is an opportunity to take advantage of that without having to deal with new managers that the ERB is unfamiliar with. He said NEPC really trusts Beach Point ; they are people that NEPC has worked with before, and they are straightforward, know what they're doing, and have excellent resources.

Mr. Bliss discussed NEPC's research process and details about the investment team. He said the Tactical Fund will seek to raise up to \$300 million and invest in five to ten deals, creating a very concentrated portfolio of their truly best ideas.

Responding to Ms. Cameron, Mr. Bliss said Beach Point will not be investing in private prisons.

Mr. Magid moved that the Investment Committee approve a commitment of \$75 million to Beach Point Tactical Opportunities Fund for the Opportunistic Credit portfolio. The commitment is subject to New Mexico State Law, Educational Retirement Board policies, Educational Retirement Board approval for placement agencies, negotiation of final terms and conditions, and completion of appropriate paperwork. Ms. Cameron seconded the motion, which passed unanimously.

4. STONEPEAK INFRASTRUCTURE FUND IV, L.P. – INFRASTRUCTURE

[Presenters: Mark Canavan and CBRE Caledon consultant Noi Spyrtos]

Mr. Canavan presented staff's recommendation of a \$50 million commitment to Stonepeak Infrastructure Fund IV for the Infrastructure portfolio. Stonepeak was established in 2011 by Michael Dorrell and Trent Vichie as co-founders, who had previously worked as senior executives at Macquarie and Blackstone. Stonepeak has collectively raised \$12.5 billion of capital over three prior funds and has collectively made 23 investments across transportation & logistics, power & utilities, midstream energy, water, and communications infrastructure sectors. Stonepeak is targeting \$10 billion of capital commitments in Fund IV, and will target a gross IRR of 15 percent and net IRR of 12 percent. The fund expects to target equity investments of greater than \$250 million.

Mr. Canavan said the ERB's first investment in Stonepeak was approved in April 2012, and since that time, the ERB's relationship with Stonepeak has demonstrated significant co-investment opportunities in three equity fund commitments and the opportunity to seed an infrastructure debt platform. As of December 31, 2019, Funds I, II and III have returned, respectively, 11.3 percent, 14.4 percent and 26.3 percent IRR after all fees.

Mr. Jacksha commented that Stonepeak is another manager investment staff knows very well and they have done very well for the ERB not only in the fund but also in co-investments. He recommended approval of this investment.

Mr. Magid moved that the Investment Committee approve a commitment of \$50 million to Stonepeak Infrastructure Fund IV, L.P. for the Infrastructure portfolio. The commitment is subject to New Mexico State Law, Educational Retirement Board policies, Educational Retirement Board approval for placement agencies, negotiation of final terms and conditions, and completion of appropriate paperwork. In addition, the Investment Committee grants staff discretion to invest an additional amount, not to exceed \$10 million, in secondary partnership interests offered by other limited partners in Stonepeak Infrastructure Fund IV, L.P. should they become available from time to time. Ms. Cameron seconded the motion, which passed unanimously.

5. ARES ACOF FUND VI, L.P. – PRIVATE EQUITY

[Presenter: Steve Neel]

Mr. Neel presented staff's recommendation of a \$50 million commitment to Ares Management ACOF Fund VI for the Private Equity portfolio. He said this would be the third commitment the ERB has made to Ares ACOF strategy. In 2012, the ERB committed \$40 million to Ares ACOF Fund IV, which is tracking as expected with a net IRR of 10.1 percent and a total value to paid-in capital (TVPI) of 1.6x. In 2017, the ERB also committed \$40 million to Area ACOF Fund IV, which is tracking as expected with a net IRR of 12.8 percent and TVPI of 1.1x. Fund VI will continue its all-weather investment strategy in a \$7.7 billion fund.

Samir Menon and Autumn Learned, representing Blackrock, made a presentation to the committee.

Responding to Ms. Cameron, Mr. Neel said ACOF's focus is on energy, consumer & retail, services & technology, and healthcare sectors, so investment in private prisons would not be included.

Mr. Jacksha stated that he, Mr. Neel, Ms. Chippeaux and Mr. Canavan have talked about the current environment and how they want to work with funds that are investing in distressed opportunities based on the theory that distressed manager can do very well at this time, and this is one fund that is in that category.

Chairman Goff moved that the Investment Committee approve a commitment of \$50 million to Ares Management ACOF Fund VI for the Private Equity portfolio. The commitment is subject to New Mexico State Law, Educational Retirement Board policies, Educational Retirement Board approval for placement agencies, negotiation of final terms and conditions, and completion of appropriate paperwork. In addition, the Investment Committee grants staff discretion to invest an additional amount, not to exceed \$10 million, in secondary partnership interests offered by other limited partners in the Ares Management ACOF Fund VI, should they become available from time to time. Mr. Magid seconded the motion, which passed unanimously.

[break]

6. LIGHTYEAR CAPITAL FUND V, L.P. – PRIVATE EQUITY

[Presenter: Steve Neel]

Mr. Neel presented staff's recommendation of a commitment of \$50 million to Lightyear Capital Fund V for the Private Equity portfolio. This will be the third recommitment for ERB. In 2012, the ERB committed \$40 million to Lightyear Fund III, which has a net IRR of 24.3 percent and a total value to paid-in capital (TVPI) of 2.3x. In 2016, the ERB committed \$50 million to Lightyear Fund IV, which has a net IRR of 12.6 percent and a TVPI of 1.2x. Fund V will continue

its value focused investment strategy in a \$1.1 billion fund. The ERB holds Limited Partner Advisory Committee seats in Funds III and IV.

Mr. Neel noted that the GP has a nexus to New Mexico, embarking on a banking roll-up strategy in the Southwest that includes the Bank of Santa Fe and a bank in the Las Cruces area.

Mr. Neel said Fund III has 11 portfolio companies and Fund IV has nine, and so it is expected that Fund V will have a comparable number, probably in the low double digits.

With regard to strategy, staff would anticipate seeing corporate carve-outs with accretive add-on acquisitions in Fund V, as Lightyear has completed over 20 corporate carve-outs and 90 add-on acquisitions to date. Thematically, the ERB may see portfolio companies that focus on the digitalization of financial services, B2B type companies that may facilitate real-time decision-making, and RIAs or independent broker-dealers, because one of Lightyear's themes is around growth in independent financial advice.

Andrew Farris and Monica Dyches, representing Blackrock, made a presentation to the committee.

Ms. Cameron asked if Blackrock has divested from Core Civic and GEO, two private prison funds.

Mr. Jacksha responded that Blackrock runs a number of index funds, and the ERB uses them as an index fund manager in the EAFE space. He said he would expect they still have those index funds and own those shares because they're in the index. On the private equity side, none of the ERB's private equity funds, including Lightyear, own prison shares and he wouldn't expect any of them to in the future.

Ms. Cameron moved that the Investment Committee approve a commitment of \$50 million to Lightyear Capital Fund V for the Private Equity portfolio. The commitment is subject to New Mexico State Law, Educational Retirement Board policies, Educational Retirement Board approval for placement agencies, negotiation of final terms and conditions, and completion of appropriate paperwork. In addition, the Investment Committee grants staff discretion to invest an additional amount, not to exceed \$10 million, in secondary partnership interests offered by other limited partners in the Lightyear Capital Fund V should they become available from time to time. Mr. Magid seconded the motion, which passed unanimously.

7. BANNER RIDGE DSCO FUND, L.P. – PRIVATE EQUITY

[Presenter: Steve Neel]

Mr. Neel requested approval to approve an additional \$40 million to the Banner Ridge DSCO Fund, which focuses on distressed, special situations and credit. This is a top-off to an

existing commitment made in August 2019, when the ERB committed \$100 million to a secondary focused distressed/special opportunities fund with Banner Ridge, and also committed \$40 million to their DSCO Fund. Both of these funds have very recently called capital, and in light of market conditions as well as Banner Ridge's bias toward distressed, credit, and special opportunities, staff feels it is prudent to ask for a top-off.

Mr. Neel stated that this second part of this request is that the committee approve the next step in the Centers of Excellence Initiative. As the committee is aware, the ERB changed its private equity consulting structure from a single consultant that provided the full scope of private equity services to one focused on multiple service providers with specific domain expertise. A pro forma detailing the cost savings of this new platform was included with his report to the committee. He said the consulting arrangement with Banner Ridge would cost approximately \$100,000 per year, and staff expects one or two commitments per year.

Mr. Neel said the ERB has a longstanding relationship of more than six years with the leadership of Banner Ridge dating back to its tenure at Siguler Guff. The Banner Ridge team will aid ERB staff in underwriting one to two commitments per year in distressed and special situations opportunities in private equity.

Banner Ridge managing partner/cofounder Anthony Cusano discussed his background and market dislocation opportunities that Banner Ridge is focusing on.

Mr. Neel said Mr. Cusano and his team have built a compelling platform, and this is one of the best performing relationships the ERB has had across this platform.

Mr. Magid moved that the Investment Committee approve a commitment of \$40 million to Banner Ridge DSCO Fund for the Private Equity portfolio. The commitment is subject to New Mexico State Law, Educational Retirement Board policies, Educational Retirement Board approval for placement agencies, negotiation of final terms and conditions, and completion of appropriate paperwork. Ms. Cameron seconded the motion, which passed unanimously.

8. ORCHARD LIQUID CREDIT FUND – DIVERSIFYING ASSETS

[Presenter: Steve Neel and NEPC analyst Sean Gill]

Mr. Neel presented staff's recommendation of a \$60 million commitment to Orchard Liquid Credit Fund (OLCF) for the Diversifying Assets portfolio. The ERB has a historic relationship with Orchard Global Asset Management dating back to 2012, when it made a \$200 million commitment to Elegantree. Subsequent commitments were made to Black Forest for \$150 million in 2014, and \$200 million to Taiga in 2017. All of these commitments were made through the ERB's Opportunistic Credit allocation. In 2018, the ERB committed \$40 million to Orchard's Liquid Credit Fund along with \$85 million to Olea Special Opportunities in "Other" Diversifying Assets. In 2019, the ERB added capital to Olea through Private Equity (\$50 million), Diversifying Assets (\$50 million) and Opportunistic Credit (\$50 million) In 2019, the Liquid Credit

Fund returned 7 percent for the calendar year and in March 2020 returned close to 10 percent due to the market volatility.

Mr. Neel discussed the strategy of this fund. He said an attribute of this strategy is that it is in a hedge fund type of structure, giving the ERB almost immediate market exposure after closing. Additionally, the strategy provides for quarterly liquidity. This liquidity, coupled with a tail-risk hedge, provides a good fit for the portfolio. As much of the portfolio in other diversifying assets is in private equity drawdown vehicles that will take a number of years to fully deploy, the ERB will get immediate exposure through the OLCF Fund. In short, this provides an elegant funding bridge for longer-term positions that will take time for the ERB to develop and implement.

Mr. Gill reviewed highlights.

Mr. Neel discussed the management ownership structure of OGAM, which is 100 percent owned by Paul Horvath subject to contractual rights to four firm individuals, and with about 50 percent of the economics flowing down to the team.

Mr. Jacksha added that the ERB intentionally paired OLEA and this fund with the idea that, when the ERB got into a higher volatility environment, the Liquid Credit Fund would provide protection and would do well, and that is what has happened here over the last few months.

Mr. Martin discussed the history of OGAM going back to Orchard Elegantree, when the ERB was an early participant and Orchard was very successful in doing bank recap trades that helped them to develop banking relationships that led to subsequent funds in which the ERB invested. He said NEPC has always objected to the economics in this and suggested they share it more widely, but they have done very well. He added that they haven't changed the key man structures in a way NEPC would have liked.

Mr. Magid moved that the Investment Committee approve a commitment of \$60 million to Orchard Liquid Credit Fund for the Diversifying Assets portfolio. The commitment is subject to New Mexico State Law, Educational Retirement Board policies, Educational Retirement Board approval for placement agencies, negotiation of final terms and conditions, and completion of appropriate paperwork. Ms. Cameron seconded the motion, which passed unanimously.

9. AMENDMENT TO CUSTODY BANK CONTRACT

[Presenter: Alan Myers]

Mr. Myers stated that the ERB's custody bank contract with State Street Bank & Trust expires on June 30, 2020, and staff is requesting a recommendation of approval by the Investment Committee to extend the contract for an additional two years.

Mr. Myers reviewed two amendment changes to the contract, which were reviewed and approved by General Counsel Susanne Roubidoux.

Mr. Myers stated that the ERB's relationship with State Street has not been trouble-free, but staff and State Street have been working together to resolve any and all ongoing issues. Staff's recommendation to extend the contract comes with the intent to continue to work with State Street to resolve current and ongoing issues. The ERB has implemented a Key Performance Indicator process with State Street, so that a failure to perform per the contract will result in a credit to the fees paid to State Street. Staff holds biweekly calls with State Street and is in daily touch, as needed, to ensure that all issues are resolved in a timely manner.

Ms. Cameron asked Mr. Myers if staff feels that issues can be worked out with State Street. Mr. Myers responded that, in the next year, staff will have to decide if it wants to go through the RFP process to contract with another custody bank. He commented that it is a long and grueling process; and unfortunately, what staff has found is that most custody banks are the same, providing "okay" service with issues that have to be dealt with. He added that the ERB has worked with every custody bank out there except one.

Mr. Jacksha said the ERB has worked with Northern Trust, JP Morgan, and now State Street. He commented that no custody bank is perfect, and State Street is providing acceptable service.

Mr. Martin added that it is very expensive to conduct a search and transition, and in the end, the likelihood that the ERB would end up with somebody better is not very high.

Ms. Cameron moved that the Investment Committee recommend the Board approve a two-year extension of the custody bank contract with State Street Bank & Trust Company subject to and contingent upon New Mexico State Law and Educational Retirement Board policies. Mr. Magid seconded the motion, which passed unanimously.

10. OTHER REPORTS AND DISCUSSION

None.

11. NEXT MEETING: THURSDAY, MAY 21, 2020

The meeting was scheduled at 1:00 p.m.

ADJOURN

The meeting adjourned at 4:30 p.m.



H. Russell Goff, Chairman