



Investment Committee Memorandum

HPS Mezzanine Partners 2019, L.P.

Private Credit Asset Class

July 29, 2020

**Investment Recommendation**

SERS’ Investment Office Staff and SERS’ Private Equity Consultant, StepStone Group, recommend that the State Employees’ Retirement System Investment Committee interview HPS Investment Partners, LLC (“HPS”, the “GP” or the “Firm”) at the July 29, 2020 Investment Committee Meeting to consider a potential commitment of up to \$75 million to HPS Mezzanine Partners 2019, L.P. (“Mezz 2019”, “Fund IV” or the “Fund”), subject to the satisfactory completion of legal due diligence.

**Investment Rationale**

Staff identified HPS Mezzanine Partners 2019 as a strong candidate for SERS’ capital commitment as it offers:

- Exposure to an attractive risk-adjusted return profile that seeks to achieve the private credit objective return of 10% net;
- Demonstrated, strong historical net returns;
- Strong relative value, with a positive net alpha against credit benchmarks;
- A stable and experienced team of senior investment professionals;

**Investment Risks**

Staff identified the following potential risks of a commitment to HPS Mezzanine Partners 2019:

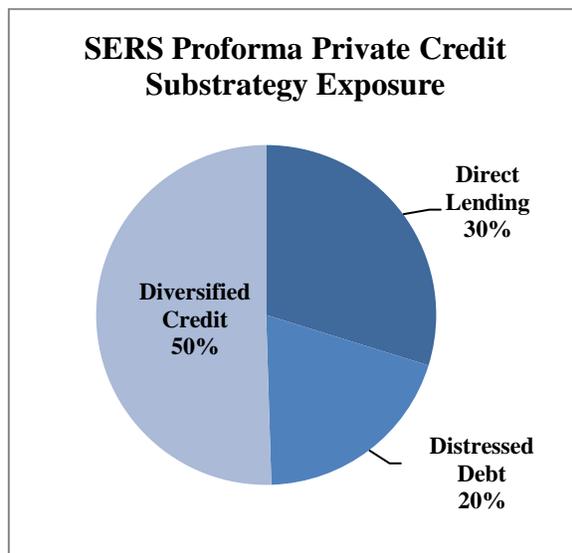
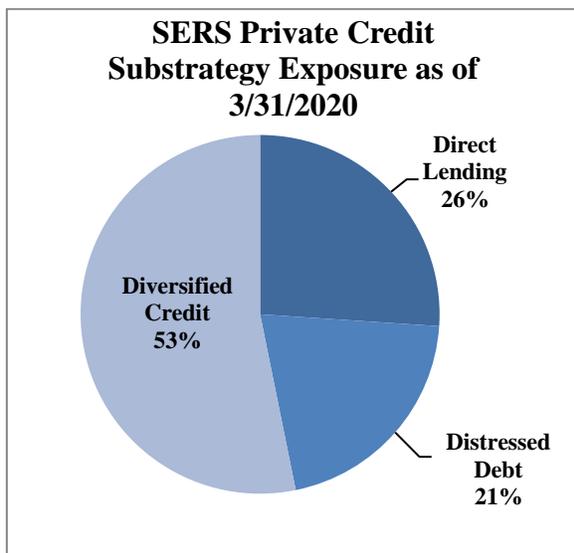
- Higher than expected default and/or lower recovery rates associated with a potentially prolonged recession;
- Team capacity with a fairly large unrealized portfolio;
- Large transactions with covenant-lite structures.

**Portfolio Implications**

A commitment to HPS Mezz 2019 would be a 2020 vintage allocation, in the Private Credit asset class and Direct Lending sub-asset class. As of March 31, 2020, SERS’ market value of Direct Lending investments was 26% of the Private Credit portfolio. This commitment aligns with SERS’ Strategic Investment Plan initiatives of making fewer commitments to top-tier managers.

SERS is targeting this commitment of up to \$75 million, or 25% of the strategic plan pacing 2020 budget for private credit. This commitment also reflects a position size of approx. 5.3% within the Private Credit portfolio

The following two charts show the Private Credit portfolio allocations by sub-strategy as of March 31, 2020 on the left, and a prospective view of the allocation post a commitment to HPS Mezz on the right.



## Sponsor Overview

HPS is a global investment firm focused on credit with \$61 billion in assets under management. Since founding, the Firm has grown to 310 employees, including 120 investment professionals, with a main office in New York and ten additional offices globally. The Firm has both private and public market divisions with various strategies that invest across the capital structure. In private markets, HPS manages \$41 billion in assets, primarily split in half between first lien senior loans and mezzanine investments.

## Investment Strategy

Since inception, HPS's mezzanine strategy has been focused on investing in the North American and European upper middle-market and large-cap segment of the mezzanine market, with average issuer EBITDA between \$75 million and \$400 million.

HPS's mezzanine strategy has the following attributes:

- Focus on the large-cap segment with resilient business models and strong fundamentals;
- Flexible and opportunistic approach to investing;
- Loss mitigation through extensive diligence, diversification and proactive management;

## Management Team

**Scott Kapnick**, *Chief Executive Officer and Governing Partner*. Before founding HPS, Mr. Kapnick was a Management Committee Member, Partner, and Co-Head of Global Investment Banking at Goldman Sachs, positions he held from 2001 to 2006. He also served as Co-Chief Executive Officer of Goldman Sachs International from 2005 to 2006 and spent 12 out of his 21 years at the firm in Europe (London and Frankfurt). Mr. Kapnick was named Partner in 1994. Mr. Kapnick is a graduate of Williams College and holds a combined JD/MBA from the University of Chicago. Mr. Kapnick also studied at the London School of Economics & Political Science.

**Scot French**, *Governing Partner and Portfolio Manager of the HPS Mezzanine Funds*. Prior to joining HPS in 2007, Mr. French spent three years at Citigroup as a Managing Director and Head of Private Investments for Citigroup Global Special Situations, a credit-focused, on-balance sheet proprietary investment fund. Within Citigroup Global Special Situations, Mr. French managed a portfolio of private mezzanine and private equity investments in North America, Europe and Latin America. Prior to joining Citigroup, Mr. French worked in the Investment Banking Division at Goldman Sachs from 1999 to 2004 and in Mergers & Acquisitions at Salomon Brothers Inc. from 1994 to 1999. Mr. French began his career at Price Waterhouse from 1992 to 1994. Mr. French is a graduate of the University of Illinois.

**Mark Albert**, *Managing Director*. Prior to joining HPS in 2016, Mr. Albert was a Managing Director of Crescent Capital Group LP and a member of Crescent's Management Committee. Prior to Crescent, Mr. Albert worked at various Investment Banking firms, including Credit Suisse First Boston, Bear, Stearns & Co. Inc., Donaldson Lufkin & Jenrette, and Drexel Burnham Lambert, where he was responsible for covering Financial Sponsor groups. Mr. Albert holds an AB from Stanford University and an MBA from the University of Chicago.

**Marcus Colwell**, *Managing Director*. Prior to joining HPS in 2010, Mr. Colwell spent three years at Merrill Lynch as Managing Director and as Global Head of Business Selection and Conflicts, reporting to the President's Office. Prior to Merrill Lynch, he worked at Goldman Sachs from 1990 to 2006 in the Investment Banking Division, where he served in various capacities, including Managing Director and acting as General Counsel of the Merger Group, COO of the Americas Merger Group and Head of Business Selection and Conflicts for Investment Banking. From 1987 to 1990, Mr. Colwell was an Associate at Shearman & Sterling. Mr. Colwell holds a BA from Denison University and a JD from the University of Michigan.

**Oliver Feix**, *Managing Director*. Prior to joining HPS in 2008, Mr. Feix was a Vice President at Morgan Stanley and a member of the Leveraged and Acquisition Finance Team, where he focused on originating, executing and distributing leveraged loans and special situation financings. Prior to that, Mr. Feix worked at Deutsche Bank in London, where he

sourced and executed multi-asset portfolio trades as a member of the Transition Management Team within the Global Markets Division. Mr. Feix holds an MSc in Economics from the University of Konstanz.

**Jeffrey Fitts**, *Managing Director*. Prior to joining HPS in 2014, Mr. Fitts spent six years as a Managing Director at Alvarez and Marsal (“A&M”), where he was responsible for the workout, management and ultimate liquidation of Lehman Brothers’ real estate portfolio following Lehman’s Chapter 11 filing. Prior to that, Mr. Fitts worked at GE Capital from 2000 to 2008, where he led workout, portfolio and distressed debt investing groups. From 1988 to 2000, Mr. Fitts worked at Citicorp focusing on real estate and corporate workouts and real estate asset management. Mr. Fitts holds a BS in Finance from the University of Delaware.

**Christopher Gunther**, *Managing Director*. Prior to joining HPS in 2018, Mr. Gunther was a Managing Director at Warburg Pincus, where he served as a senior member of the Fundraising and Investor Relations team. Prior to Warburg Pincus, Mr. Gunther was a Managing Director at Providence Equity Partners, where he served as an investment professional focused on North American TMT and information services companies. Mr. Gunther also served as a fundraising professional across Providence’s private equity and private credit (Benefit Street Partners) platforms. Prior to Providence Equity, Mr. Gunther held various roles in Investment Banking at Salomon Brothers/Salomon Smith Barney in Los Angeles, Hong Kong, and New York. Mr. Gunther holds a BA in Public Policy with Honors from Stanford University.

**Taylor Kushner**, *Managing Director*. Prior to joining HPS in 2017, Mr. Kushner was a Managing Director at TPG Special Situations Partners. Prior to TPG, Mr. Kushner worked at Goldman Sachs and held various roles in the Special Situations Group and Investment Banking Divisions. Mr. Kushner holds a BS in Business Administration from Georgetown University where he graduated Cum Laude.

**Mark Rubenstein**, *Managing Director*. Prior to joining HPS in 2008, Mr. Rubenstein worked as an Associate in the Special Situations Group at Citigroup, where he focused on private mezzanine and private equity investments. Prior to joining Special Situations, Mr. Rubenstein was an Analyst in the Leveraged Finance Group at Citigroup. Mr. Rubenstein holds an HBA from the Richard Ivey School of Business at the University of Western Ontario.

**Ed Tam**, *Managing Director*. Prior to joining HPS in 2008, Mr. Tam spent four years as a Partner at the publicly traded private debt fund, Apollo Investment Corporation, where he focused on sourcing, due diligence and structuring unitranche, mezzanine and equity co-investments. Prior to joining Apollo in 2004, Mr. Tam spent four years at DLJ Investment Partners (“DLJIP”), where he was responsible for sourcing, due diligence and structuring mezzanine and equity co-investments. Prior to joining DLJIP, Mr. Tam spent seven years at Donaldson, Lufkin & Jenrette, where he focused primarily on corporate finance transactions including mergers and acquisitions, debt and equity financings and restructurings. Mr. Tam holds a BS in Operations Research/Industrial Engineering and an MBA in Finance from Cornell University.