

# Maryland GFOA Spring 2018 Conference

## Alternative Investments for Pension Funds

April 27, 2018

# Speaker Bio

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- ▶ Brad Atkins is Co-Founder, Managing Director and Chief Executive Officer at Franklin Park, and a member of the firm's Investment Committee.
- ▶ At Franklin Park, Brad is actively involved with clients on portfolio planning, construction and management matters. He also is responsible for leading the analysis and evaluation of private market investment opportunities, monitoring clients' portfolios and conducting industry research.
- ▶ Prior to Franklin Park, Brad worked with Hamilton Lane and Fleet Bank. He is a CFA Charterholder and a member of the CFA Institute. Brad received an M.B.A. in Accounting and a B.A. in Finance from American University.

# About Franklin Park

## Private markets expertise

- Private equity, private debt and venture capital
- Funds and co-investments

## \$12.2 Billion

Assets under advisement

## 25 Funds

Commingled and separate account funds

## 15 years

Firm history

## 18 Institutional Clients

Public and private pensions, endowments, foundations, health systems and labor unions

## 3 Offices

Global presence

## 26 Professionals

Stable and seasoned team

## 100% Employee-Owned

Economically-aligned team



# Private Market Asset Classes

PRIVATE EQUITY		PRIVATE DEBT		REAL ASSETS	
Corporate Finance Equity	Venture Capital	Corporate Finance Debt	Alternative Credit	Infrastructure	Natural Resources
Buyout	Early Stage	Direct Lending	Hybrid Securities	Power	Conventional Energy
Acquiring controlling ownership in a business and creating synergies or growth to enhance enterprise valuation	Investing equity capital in young businesses creating new technologies, products, or services, with enterprise value growth potential	Investing in senior debt securities that typically provide a floating rate cash yield	Investing in hybrid debt and equity securities that typically provide both a cash yield and equity upside	Greenfield, development, and acquisitions of power plants, storage and transmission networks	Investing in companies in the business of oil and gas upstream production, and midstream storage and transportation
Growth Equity	Late/Expansion Stage	Mezzanine	Asset-Backed Securities	Multi-Sector	Clean Energy
Investing in high growth companies to refinance the balance sheet or raise capital used for expansion or acquisitions	Investing expansion capital in small, revenue-generating, but not necessarily profitable, high growth companies	Investing in subordinated debt securities that typically provide a high fixed rate cash yield	Investing in securities backed by royalties, revenue interests, securitized assets, commercial aircraft, equipment leases, patents and other esoteric assets	Greenfield, development, and acquisitions of transportation, energy, ports, maritime and other infrastructure assets	Investing in companies in the business of clean energy generation, renewable fuels, storage and efficiency
Turnaround		Distressed Debt	Opportunistic Credit		
Acquiring and turning around the operational performance of underperforming businesses or assets		Rescue financing or acquiring corporate debt trading at distressed prices with the goal of leading or influencing the balance sheet restructuring	Flexible strategies that opportunistically invest across various assets and securities based on perceived mispricing, dislocation, inefficiencies, or out-of-favor industries		

# Overview of Private Debt Strategies

Private debt encompasses a broad array of strategies investing in illiquid, current income-generating assets and securities.

	Direct Lending	Mezzanine Debt	Special Assets	Distressed Debt	Structured Capital
	<ul style="list-style-type: none"> <li>Lending senior debt capital to mature, profitable companies</li> <li>The loans are senior in the capital structure, typically with a first-lien on pledged collateral</li> <li>The loans earn interest through a combination of a floating base rate (typically LIBOR), plus a "spread" over the base rate that reflects the issuer's credit risk</li> </ul>	<ul style="list-style-type: none"> <li>Lending junior debt capital to mature, profitable companies</li> <li>Traditionally fixed rate, unsecured securities, but also includes floating rate, second-lien, and unitranche debt</li> <li>Investments are typically structured to provide meaningful current income, and upside potential in the form of discounts, warrants or common stock</li> </ul>	<ul style="list-style-type: none"> <li>Acquiring illiquid, cash generating assets and asset backed securities</li> <li>Strategies include royalties, portfolio transactions backed by senior securities, non-performing loans, securitized assets, commercial aircraft, equipment leases, and patents</li> </ul>	<ul style="list-style-type: none"> <li>Lending to or acquiring the debt of companies facing operational or financial distress</li> <li>Strategies include rescue lending, buying debt securities in the secondary market at discount to par value, accumulating debt positions with goal of participating in balance sheet restructuring or converting to equity</li> </ul>	<ul style="list-style-type: none"> <li>Financing to small and mid-sized companies structured with combination of debt and preferred equity</li> <li>Interest payments typically include cash and payment in-kind</li> <li>A meaningful portion of return comes from equity upside, captured through a combination of warrants and conversion rights</li> </ul>
Key Merits	<ul style="list-style-type: none"> <li>Stable source of current income</li> </ul>	<ul style="list-style-type: none"> <li>Stable source of current income</li> </ul>	<ul style="list-style-type: none"> <li>Less efficient market</li> </ul>	<ul style="list-style-type: none"> <li>Potential for high returns during distress cycles</li> </ul>	<ul style="list-style-type: none"> <li>Inefficient market</li> <li>Opportunity for manager value-add</li> </ul>
Key Risks	<ul style="list-style-type: none"> <li>Efficient market</li> <li>Often reliant on fund level leverage</li> </ul>	<ul style="list-style-type: none"> <li>More efficient market</li> <li>Increasingly crowded out by second lien and unitranche</li> </ul>	<ul style="list-style-type: none"> <li>Manager selection is key</li> </ul>	<ul style="list-style-type: none"> <li>High variability in returns</li> <li>Highly reliant on distress cycle</li> </ul>	<ul style="list-style-type: none"> <li>Manager selection is key</li> </ul>
Target Net IRR	<ul style="list-style-type: none"> <li>Mid to high single digits (if unlevered)</li> <li>High single digits to low teens (if levered)</li> </ul>	<ul style="list-style-type: none"> <li>Low teens</li> </ul>	<ul style="list-style-type: none"> <li>Mid to high teens</li> </ul>	<ul style="list-style-type: none"> <li>Mid to high teens</li> </ul>	<ul style="list-style-type: none"> <li>High teens</li> </ul>

# Rationale for Private Debt Allocation

High absolute return potential

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Attractive risk-adjusted returns

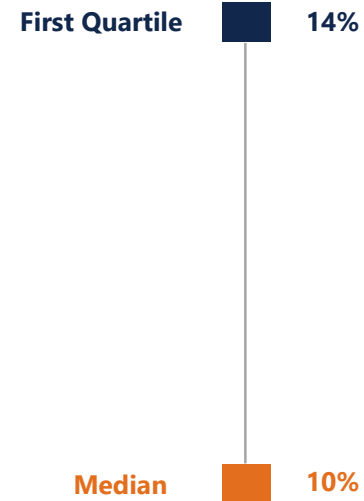
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Current income

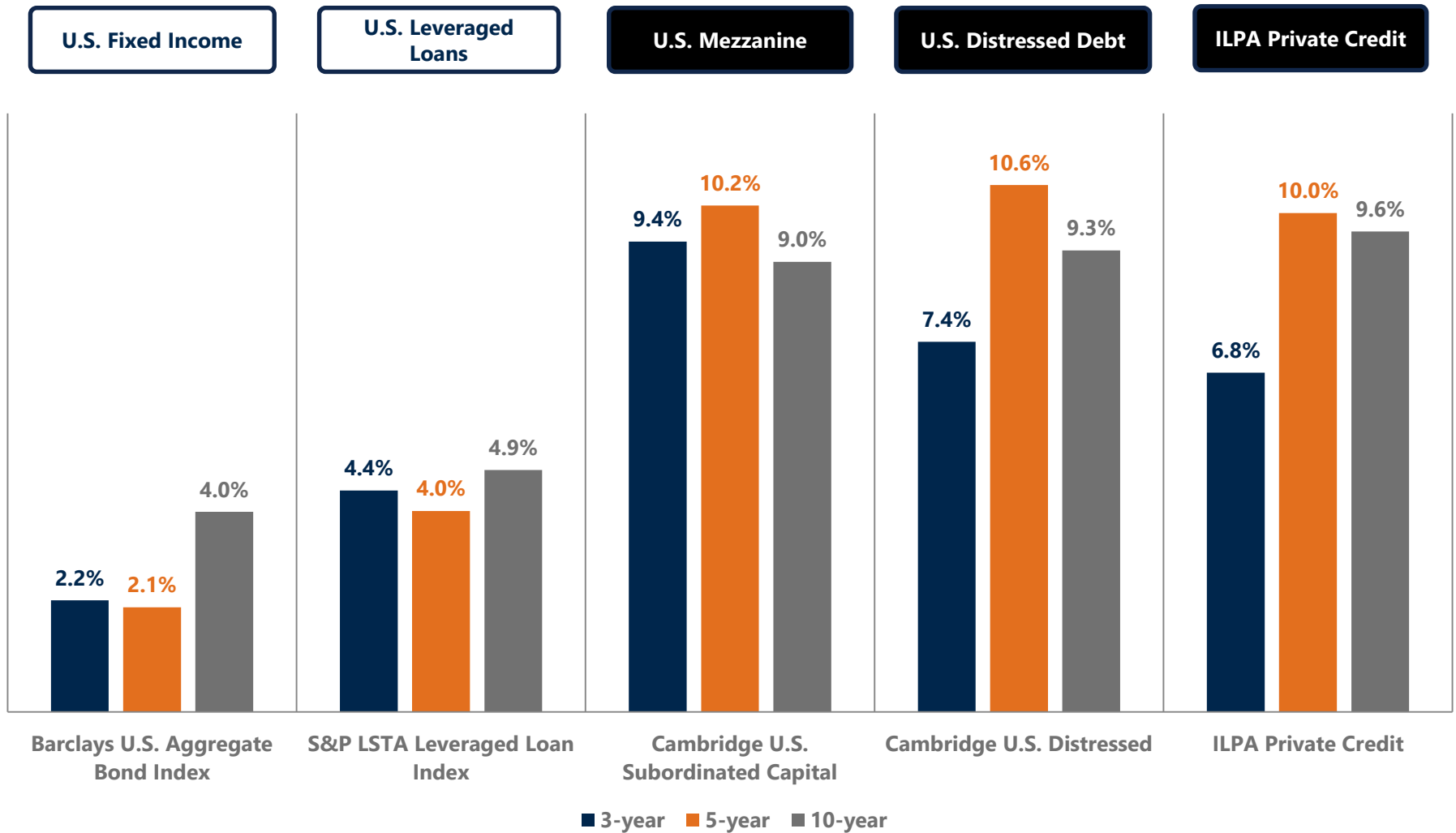
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Shallower J-curve than private equity

Aggregate Net Returns for Private Debt Funds raised between 2004-2013 (Source: Preqin)



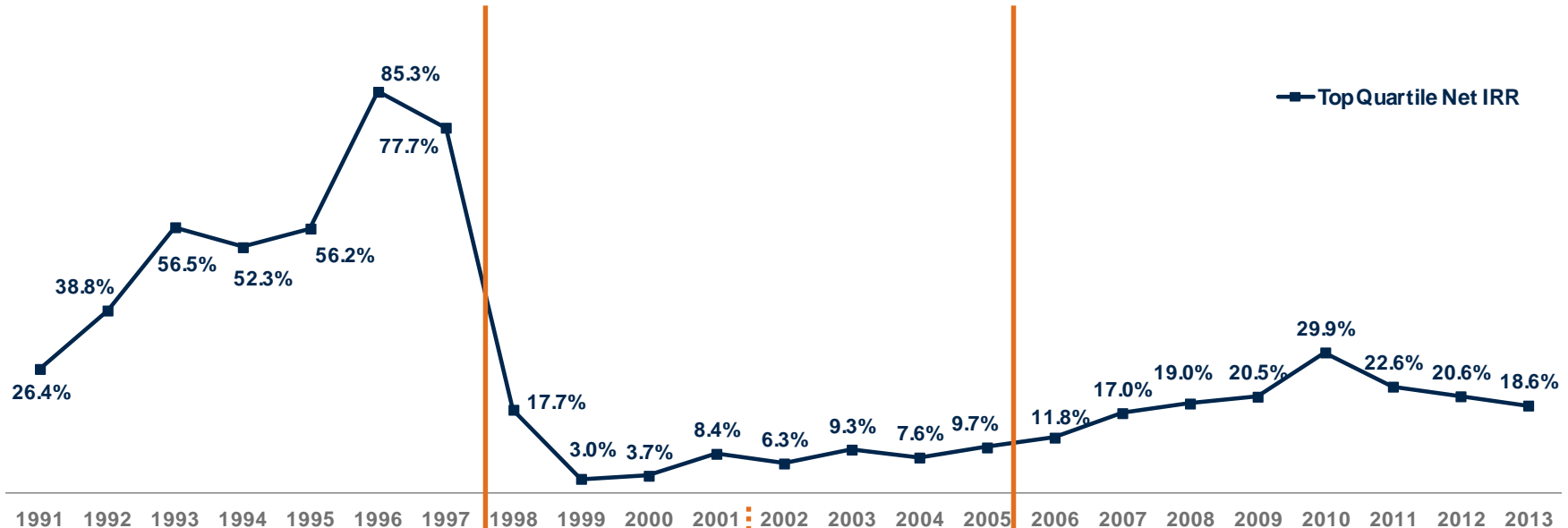
# Public vs. Private Debt Horizon Returns



Source: Cambridge Associates, Bloomberg, ILPA As of September 30, 2017.

# Venture Capital Vintage Returns

▶ Performance for top quartile venture funds has been solid since 2007



## Internet 1.0

- \$89b raised
- \$99b invested
- High double digit IRRs

## Bubble

- \$224b raised
- \$308b invested
- Single digit IRRs

## Aftermath

- \$62b raised
- \$147b invested
- Single digit IRRs

## Internet 2.0

- \$172b raised
- \$378b invested
- Double digit IRRs



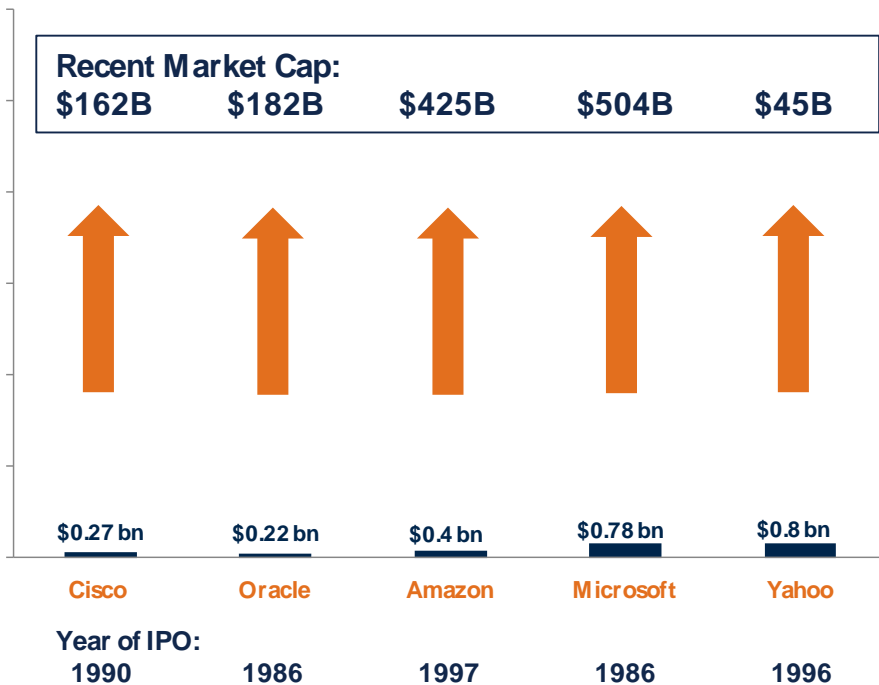
Source: Cambridge Associates.



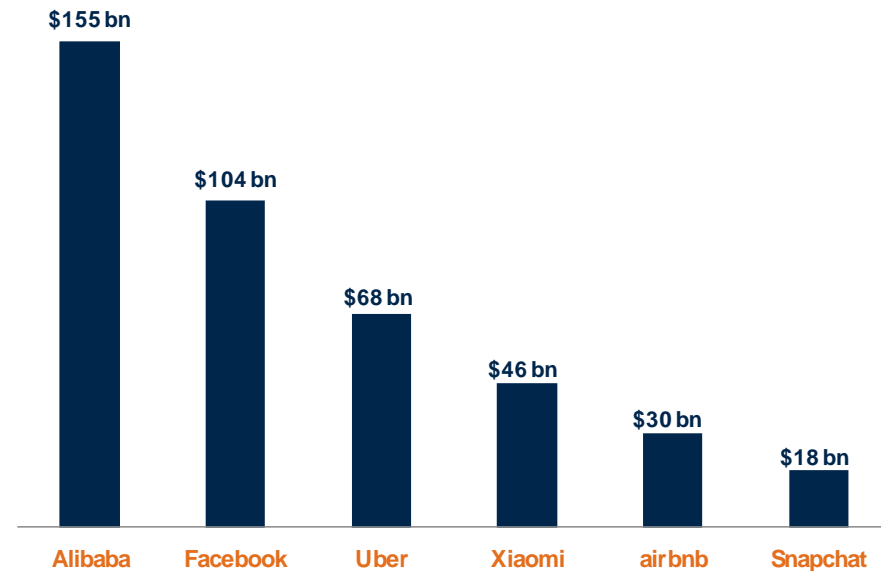
# Value Creation: Public v. Private Markets

▶ Significant value for technology companies today is produced in the private markets

1990s: Most Value Created in Public Market

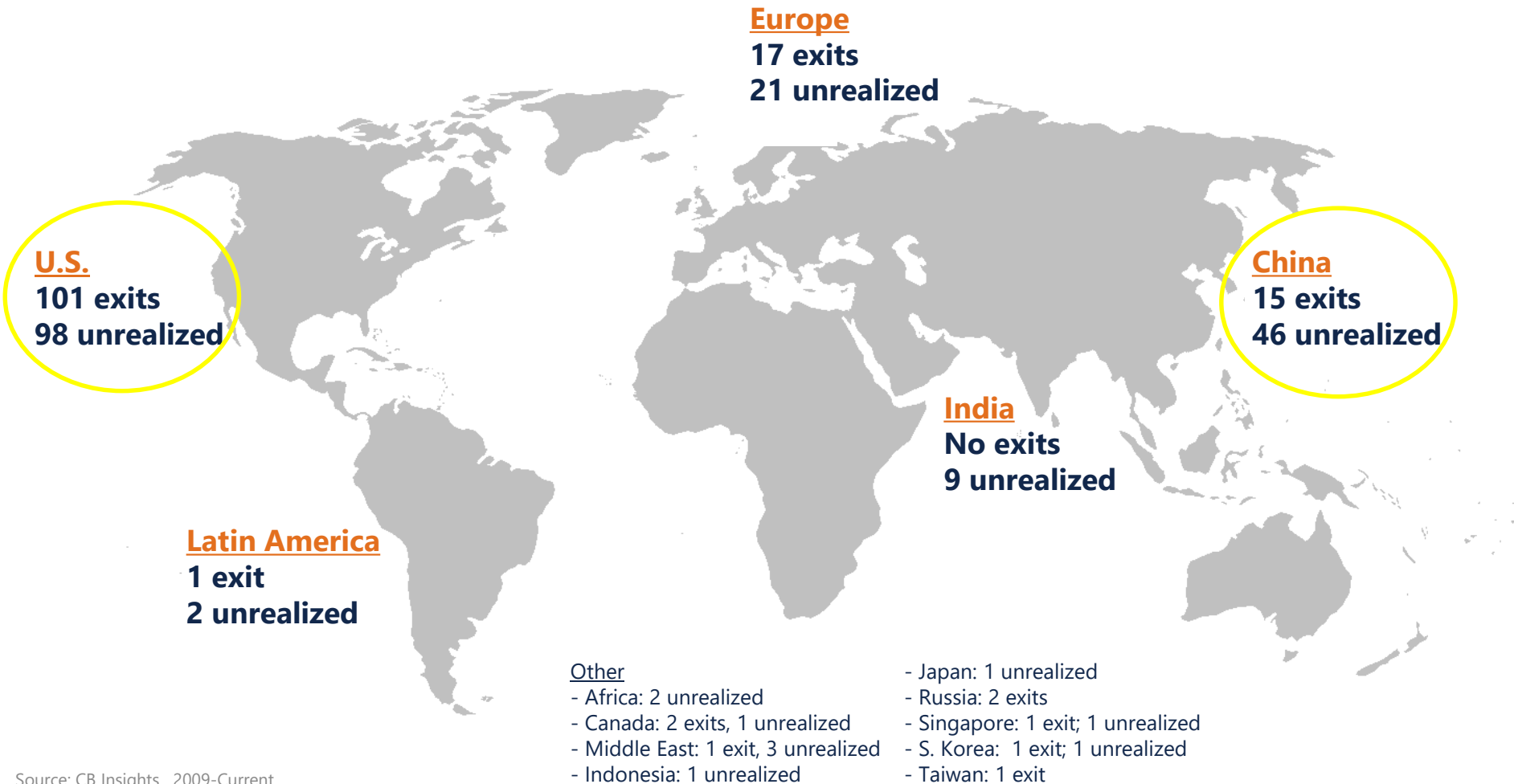


Today: Most Value Created in Private Market



# Venture “Unicorns” By Geography

▶ The U.S. and China account for the vast majority of “unicorns”



Source: CB Insights. 2009-Current.

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# Audience Questions