APPROVED

WASHINGTON STATE INVESTMENT BOARD
Private Markets Committee Meeting Minutes
April 2, 2015

The Private Markets Committee met in open public session at 9:00 a.m. in the boardroom at the Washington State Investment Board in Olympia, Washington.

Members Present:	George Masten, Chair Kelly Fox Judy Kuschel Treasurer Jim McIntire Richard Muhlebach David Nierenberg Jeff Seely
Members Absent:	Senator Mike Hewitt
Other Board Members Present:	Marcie Frost Bill Longbrake (teleconferenced)
Also Present:	Theresa Whitmarsh, Executive Director Gary Bruebaker, Chief Investment Officer Tom Ruggels, Senior Investment Officer – Private Equity Björn Seebach, Investment Officer – Private Equity Carmen Matsumoto, Investment Officer – Private Equity Gary Holt, Investment Officer – Private Equity Susan Freese, Investment Officer – Tangible Assets John Graves, Assistant Senior Investment Officer – Tangible Assets Steve Draper, Senior Investment Officer – Real Estate Linda Buchanan, Administrative Assistant Mary Lobdell, Assistant Attorney General Tara Blackburn and Michael Augustine, Hamilton Lane Kurt Jaggers, Jennifer Mulloy, and Todd Crockett, TA Associates Robert F. Agostinelli and M. Steven Langman, Rhône Capital Partners Joseph P. Baratta and Michael S. Sotirhos, Blackstone Capital Partners Brent Burnett, Real Asset Portfolio Management Richard Halderman, Teays River Investments Jim Vanderhider, EnerVest Michael Humphrey, Courtland Partners Dan Schulte, Principal Enterprise Capital Holdings

[Names of other individuals attending the meeting are listed in the permanent record.]

Chair Masten called the meeting to order and took roll call.

ADOPTION OF THE JANUARY 8, 2015, MINUTES

> **Mr. Fox moved to adopt the January 8, 2015, minutes. Ms. Kuschel seconded, and the motion carried unanimously.**

PRIVATE EQUITY INVESTMENT RECOMMENDATION – TA XII, L.P.
Mr. Seebach said staff recommends an investment of up to $250 million in TA XII, L.P., consistent with the Board-approved annual plan and the private equity model portfolio. Mr. Seebach noted the WSIB has invested in four prior funds and is on the advisory board. He described the fund's investment strategy, geographic focus, investment team, deal sourcing, portfolio director, and 180-day plans to accelerate portfolio company growth. Mr. Seebach discussed the firm's investment discipline, institutionalized processes, low number of board seats per professional, focus on exits, and liquidity. He further discussed the performance of Fund X, increases in portfolio company pricing, staff changes, the well-established transition process, and the potential impact of a downturn in the market on the portfolio.

[Treasurer McIntire arrived at 9:03 a.m.]

Ms. Blackburn, Hamilton Lane, discussed the fund's fit in the WSIB's private equity portfolio, alignment of interests, generational transition planning, unique investment strategy and fees. Ms. Blackburn said that Hamilton Lane supports the commitment.

The Committee discussed the firm's environmental, social, and governance risks and strategies, prospects of Fund X, and the partner's disciplined investment approach.

Mr. Jaggers, Ms. Mulloy, and Mr. Crockett, TA Associates, introduced themselves. Ms. Mulloy provided an overview of the firm and discussed its mission statement, history, team, portfolio coverage, industry focus, and investment strategy.

Mr. Jaggers discussed the firm's stable organization, growth, industry groups, women in the firm, and compensation methodology.

Mr. Crockett described the firm's origination philosophy, industry expertise, relationships, profitable business models, low use of leverage, diversified portfolio, geographic diversification, 180-day plans, value creation, and its promote-from-within culture.

Discussion ensued regarding the firm's differentiated approach, lessons learned during the downturn, use of industry consultants, investment pace, investment criteria, current market conditions, risk management, and participation in the Women in Investing conference.

Treasurer McIntire moved that the Private Markets Committee recommend the Board invest up to $250 million, plus fees and expenses, in TA XII, L.P., subject to continuing due diligence and final negotiation of terms and conditions. Ms. Kuschel seconded, and the motion carried unanimously.

PRIVATE EQUITY INVESTMENT RECOMMENDATION – RHÔNE PARTNERS V, L.P.

Ms. Matsumoto stated staff recommends an investment of up to €150 million (approximately $165 million at the current exchange rate) in Rhône Partners V, L.P. Ms. Matsumoto reported the fund has a target size of €1.8 billion with a cap of €2.5 billion. If approved, the investment would be a new relationship for the WSIB. The proposed investment is consistent with the Board-approved 2015 private equity annual plan and the private equity model portfolio.

Ms. Matsumoto described the firm's presence in the U.S. and Europe, history, experienced team, performance history, investment strategy, global footprint, competitive advantage, and expertise. She explained that, while the fund will target industries in the chemical, consumer product, general industrial, media, packaging, retail services, and transportation sectors, there is no mandate for any certain percentage in each. Ms. Matsumoto discussed the fund's operational improvements to portfolio companies, lower concentration, and excellent fit in the WSIB's portfolio.

[Mr. Longbrake joined the meeting via teleconference at 10:16 a.m.]

Ms. Blackburn, Hamilton Lane, described the fund's focus on the middle market, low use of leverage, reputation in European family businesses, and complicated process that the firm executes well. She explained that while the strategy carries a little more risk, it has high-level returns and has been top quartile over multiple funds. Ms. Blackburn discussed the firm's well-developed investment platform, team, portfolio diversity, and increased fund size. She said that Hamilton Lane supports the investment.

The Committee discussed the increase in fund size, staff turnover, portfolio companies with big wins or losses, and the size of deals.

Mr. Agostinelli and Mr. Langman, Rhône Capital Partners, introduced themselves. Mr. Agostinelli discussed the firm's history, standards, cohesive unit, transatlantic investments, cross-border culture, and one-firm approach.

Mr. Langman described the firm's investment strategy, geographic focus, global outlook, and relatively small investment team. Mr. Agostinelli spoke to the firm's careful approach to pricing, low use of leverage, and superior internal rate of return. Mr. Langman explained the firm's selection process, complex deal structure, investment opportunities disproportionate returns, and consistent returns. Mr. Agostinelli addressed the firm's investment focus, experience, expertise, and reputation. Mr. Langman discussed the firm's investment professionals, promotion opportunities, cohesive team, and unanimous decision making process. Mr. Agostinelli and Mr. Langman described the firm's revenue model, deal sourcing, portfolio companies, and focus on returning capital.

Discussion ensued regarding lessons learned during the financial crisis, opportunities during market dislocations, diversification, low amortization of principal, and investment discipline.

Treasurer McIntire expressed interest in evaluating the potential benefit of hedging the commitment amount given the current exchange rate for the Euro.

> **Treasurer McIntire moved that the Private Markets Committee recommend the Board invest up to €150 million, plus fees and expenses, in Rhône Partners V L.P., plus fees and expenses, subject to continuing due diligence and final negotiation of terms and conditions. Ms. Kuschel seconded, and the motion carried unanimously.**

[The Committee recessed at 10:29 a.m., and reconvened at 10:42 a.m.]

PRIVATE EQUITY INVESTMENT RECOMMENDATION – BLACKSTONE CAPITAL PARTNERS VII, L.P.

Mr. Holt said staff recommends an investment of up to $500 million in Blackstone Capital Partners VII, L.P. The fund has a target size of $15 billion. Mr. Holt said the firm is thoroughly institutionalized, and he described the firm's 25-year history, impressive performance record, generational transition, strategy, formal operational intervention capability, global footprint, and sister alternative investment businesses. He discussed the firm's organizational changes, team, multiple products, and fund size. Mr. Holt explained the firm has greater accountability and transparency because it is a public company.

The Committee discussed the potential of club deals and the investment's fit in the WSIB's private equity portfolio.

Mr. Augustine, Hamilton Lane, discussed market timing and the fund's sourcing model, deal teams, global approach, investment strategies, disciplined approach, consistent returns across multiple cycles, low risk, strong liquidity, and reputation. He addressed the firm's public structure and the ensuing increased transparency. Mr. Augustine stated that, while the proposed investment does increase the WSIB's exposure to mega buyouts, the overall exposure is still reasonable. He said that Hamilton Lane approves the investment.

Messrs. Baratta and Sotirhos, Blackstone Capital Partners, introduced themselves. Mr. Baratta said Blackstone's private equity business was the firm's longest-standing and most consistently performing strategy. He described the firm's evolution, infrastructure, disciplined investment strategy, sister energy fund, ability to allocate capital to the best deals globally, investment committee, global deal team, homegrown talent with a long tenure, consistent culture, incentive alignment, performance through multiple cycles, lessons learned during the financial crisis, value on unlevered returns, cash flow yield, ability to intervene to change and drive value operationally, recent performance, geographic focus, transaction diversity, functional experts, and average investment size. Mr. Baratta discussed cyclical market opportunities, targeted deal sourcing, structural ability to deploy capital at scale, brand recognition, and management of talent base.

The Committee discussed the firm's energy investments and sector volatility, investments in coal and coal-fired power generation, focus on renewable energy, lack of women in senior positions, participation in club deals, and geographic distribution. Discussion ensued regarding current market conditions concerning private equity.

> **Mr. Fox moved that the Private Markets Committee recommend the Board invest up to $500 million, plus fees and expenses, in Blackstone Capital Partners VII, L.P., subject to continuing due diligence and final negotiation of terms and conditions. Ms. Kuschel seconded, and the motion carried unanimously.**

[The Committee recessed at 11:40 a.m., and reconvened at 12:11 p.m.]

TANGIBLE ASSETS INVESTMENT RECOMMENDATION – TEAYS RIVER INVESTMENTS, LLC

Ms. Freese said staff is recommending an investment of up to $300 million in Teays River Investments LLC. She said Teays is not a fund, but rather a privately-held company and, at the proposed investment level, the WSIB will have representation on its Board. She explained this is an expanded role as compared to that of a traditional fund's Advisory Committee. Ms. Freese highlighted the reasons to consider this investment, which include exceptional leadership, portfolio visibility, a diminished J curve, the permanent capital nature, and portfolio fit. She also said staff believes the proposed investment in protein has attractive fundamentals. Ms. Freese shared the proposed investment is not without its challenges, including determining valuation. The WSIB will invest in Teays at fair market value as determined by the management of Teays and confirmed by an independent third party. She also said the permanent capital nature is a challenge, as the goals and circumstances of the other investors may change over time. This is mitigated by the WSIB's representation on Teays' board. Ms. Freese shared the roster of potential investors in Teays includes a number of large, institutional investors known by the WSIB, and staff is confident that they can work with them.

Discussion ensued regarding the company's organic products and the plan for continued water availability for the grape production in California. Mr. Nierenberg inquired about the investment structure as an operating company and the process by which resources are allocated among the four separate businesses, how decisions are made, and how might decisions be made if contemplating getting into a fifth or sixth company. Ms. Freese responded that Mr. Akers will hold a board seat on behalf of the WSIB, and Mr. Halderman has a good understanding of the resources necessary for each operation. Mr. Bruebaker reiterated that, as a board member, Mr. Akers will be involved in approving annual business plans and budgets, among other things.

Mr. Burnett, Real Asset Portfolio Management, said that Teays has built an exceptional organization. He shared that one of the challenges in agriculture investing is finding a team that can access good deals and has a strategy that is repeatable, and Teays fits both of these. Mr. Burnett explained that Teays has built the institution to be able to continue the strategy, individuals in management come from farming backgrounds, and relationships are very important. He said that what his firm likes about the investment is the portfolio visibility and the opportunity to participate in four strong business segments with the strongest and most diverse customer relationships that are diversified by customer base and operating strategy and complementary to others in the tangible assets portfolio.

He said they reviewed the valuation methodology, and he felt the assumptions utilized are reasonable to the extent the publicly available comparisons are fair. He said the investment structure as an operating company investment has inherent risks; however, pension funds have advantages in a lower cost of capital and long-term time horizon, and this is an opportunity to partner to leverage these advantages. Mr. Burnett said he would expect the proposed structure to improve the net return by 200 to 300 basis points.

Chair Masten announced the Committee would go into executive session to discuss financial and commercial information relating to an investment since public knowledge regarding the discussion would result in loss to the funds managed by the WSIB or would result in private loss to the providers of the information. He said the executive session was expected to last about 15 minutes, at which time the Committee would reconvene in open session.

[The Board went into executive session at 12:25 p.m., and reconvened in open session at 12:40 p.m.]

Mr. Halderman and Mr. Gray, Teays River Investments, introduced themselves and shared that the firm started out as a fund manager, but the business nature is long-term, so the business converted the four segments it is today. Messrs. Halderman and Gray discussed the firm's culture, purpose, strategy, value integration, focus on quality, alignment with partners, strategic objectives, and expansion of end-user value. Mr. Halderman said the WSIB is a great cultural partner and shared the reasons, including its long-term vision, transparency in capital, and ability to partner with the firm in decision-making processes.

He said the company wants to build a long-term focus structure in agriculture to take advantage of market fragmentations, by connecting all pieces together to align capital and reduce volatility. He described the history and relationship of the firm's management team, diversity of staff, and desire to attract the deepest and most advanced talent in the industry.

Discussion ensued regarding the firm's retailer partnerships; contract structure; benefit of scale; products, including organics and GMOs; climate risk, including water issues; technology and information management; common thread between the firm's four businesses and allocation resource decisions relative to the businesses; valuation metrics; vertical integration; transportation; and labor issues.

Mr. Fox asked if staff believed the group to be well-positioned to mitigate the risk factors, to which Ms. Freese and Mr. Burnett responded in the affirmative.

> **Mr. Fox moved that the Private Markets Committee recommend the Board invest up to $300 million, plus fees and expenses, in Teays River Investments, LLC or a related special-purpose vehicle, subject to continuing due diligence and final negotiation of terms and conditions. Ms. Kuschel seconded, and the motion carried unanimously.**

TANGIBLE ASSETS INVESTMENT RECOMMENDATION – ENERVEST ENERGY INSTITUIONAL FUND XIV, L.P.

Mr. Graves said, in evaluating this opportunity, staff focused on gas-related properties and that demand is forecast to increase by 20 percent from today to 2020. He said that drivers of natural gas demand include new gas-burning power plants opening in the U.S., replacing older coal-fired plants, new manufacturing plants opening throughout the U.S. due to lower energy costs, and significant growth in LNG exports and pipelines exporting natural gas to Mexico. Staff reviewed several managers that could provide exposure to natural gas and selected EnerVest as the best fit for the WSIB tangible assets portfolio. EnerVest follows a strategy where it strives to be to be a leading producer in each basin it targets, seeking properties that consist of 50 to 60 percent proved, developed, and producing reserves (PDP), while the reminder consists of proven but undeveloped reserves. Mr. Graves described the structure of EnerVest, the history of its funds, returns in commodity markets, and the current dislocation in U.S. markets. He explained that the tangible assets program looks for the composition of returns to favor income, which EnerVest does, with a target of 8 to 9 percent after the initial J-curve period, and roughly 60 to 70 percent of returns coming from income over the life of the fund. Mr. Graves said there are risks, such as the collapse in commodity prices, which has brought down returns in energy sector markets. EnerVest mitigates this risk through hedging upon acquisition, and they achieve additional returns on the drilling side. He said other risks include potential conflicts in connection with EnerVest's publicly traded MLP, which co-invests occasionally with the fund; however, the MLP targets assets with more mature, stable proven reserves. Mr. Graves explained that this new fund is doing something slightly different with a 5 percent allocation to New Ventures, a higher-risk/higher-reward exploration effort. He shared that staff investigated thoroughly a historical 1992 SEC charge against John Walker but became comfortable that through the proceedings everything that occurred was handled in a highly ethical manner and was as transparent as possible.

Mr. Burnett, Real Asset Portfolio Management, shared some of the risks identified in his firm's evaluation and how they are mitigated, including commodity price fluctuations, mitigated by operational efficiencies, focus on developing dominant positions in the basins in which they are active, creating leverage with service contracts, and hedging activities; operating risk, mitigated by focusing on basins that they understand and showing discipline in by not taking bets on new basins, as well as the reduction of the gross to net fee spread as compared to other private equity type energy investments; potential for conflicts with the MLP, mitigated by the clearly-defined asset targets and staff seat on the Fund's Advisory Committee.

Discussion ensued regarding location of the focus basins, opportunities to acquire assets in a dislocated market at a discount, the commodity price environment, and exit strategy.

Mr. Vanderhider, EnerVest, Ltd., said that EnerVest is the largest firm in the U.S. and has been in the top quartile over a 24-year period. He discussed the key goals for 2015, the seven asset regions in which the firm focuses, assets under management, proved and probable reserves, strategy, operating company model, and seasoned management team. He said the firm has significant depth and ability, and he explained the structure of the company and executive leadership, how the firm creates value, deal sourcing and structuring, operating cycle, the firm's model portfolio and targeted returns, and historical returns.

Mr. Vanderhider said EnerVest is a very active participant in the market, which has exploded in size over the last decade. He shared the expectations for the firm's deal volume based on current market conditions; how EnerVest differentiates itself from the rest of the industry by following a contrarian strategy, with a net effect of being very well positioned in the market; the structure of employee ownership; merits of investing in energy; and the current market opportunities.

> **Mr. Fox moved that the Private Markets Committee recommend the Board invest up to $200 million, plus fees and expenses, in EnerVest Energy Institutional Fund, XIV, L.P., subject to continuing due diligence and final negotiation of terms and conditions. Treasurer McIntire seconded, and the motion carried unanimously.**

REAL ESTATE INVESTMENT RECOMMENDATION – PRINCIPAL ENTERPRISE CAPITAL HOLDINGS LLC

Mr. Draper said staff is recommending a $500 million commitment increase to Principal Enterprise Capital Holdings LLC (PECH) and the transfer to PECH of the WSIB's direct investment in Alere Property Group (Alere) of $200 million as per the annual plan. He stated that Dan Schulte is one of the WSIB's longest-standing investment managers in all asset classes – over 20 years – with 16 years leading PECH, during which time the investment has achieved a 13.4% return. He said this is even more impressive when one considers that the nature of most of what PECH does is relatively less risky than other parts of the real estate portfolio. Mr. Draper said PECH is very consistent with a long-term approach, and shared a recent article regarding urban regeneration, noting that Mr. Schulte has been talking about this for a decade and has created strategies to take advantage of it. He explained that, since the last time PECH came before the Board, they have expanded their team to add depth and a more diversified point of view. The PECH team has been fortunate to have made some mistakes early in its history, with mistakes that did not lead to losing money; most importantly, they learned about picking the right people. Mr. Draper discussed the risks associated with the investment, including operating risk, which is present with all intermediaries, and the currently-higher level development risk. He said the transfer of the WSIB's direct investment in Alere to PECH is consistent with the stated strategy to move away from direct staff oversight of operating companies. In addition, at the time the original investment was made, PECH was smaller, and Alere was a disproportionate amount of PECH's holdings, thus the co-investment; PECH is larger now and it is now more appropriate to move it back to them.

Mr. Humphrey, Courtland Partners, said the REOC structure utilized by the WSIB provides the advantages that are atypical, including greater control by the WSIB, and that, during the economic downturn, the REOC portfolio performed very well, partly due to the control that WSIB maintains, which leads to better investment discipline showing up in returns. He discussed historical returns, income returns, gross to net spreads, strategies, the management team, and overall results.

Mr. Humphrey shared concerns about the proposed investment, including relative underperformance of two REOCs, which he said needs to be taken in context, explaining that one group invested right before the downturn, and on a long-term basis they will perform; operating risk; and key person risk, which includes Mr. Schulte, as well as key REOC personnel. He said there needs to be a focus on succession planning, and that WSIB staff does a good job on that.

Discussion ensued regarding the amount of the PECH portfolio invested in traditional versus non-traditional property types; expected returns for unusual property types versus the strategy of investing in traditional property types in the best locations in the best cities; and diversity within REOC locations and platforms.

Mr. Schulte, PECH, said that the WSIB partnership with PECH has been in place for over 15 years with good continuity in leadership; however, they are bringing in new individuals. PECH staff spends a lot of time thinking about the durability of the team and the long term. He said the PECH team is solely dedicated to the WSIB and its investments, investing in real estate through REOCs. He shared the key focal points of investing in REOCs; the role of PECH as an intermediary; themes of the firm, including a focus on globalization, urbanization, and consolidation, which is more of a threat; the changing landscape of real estate investment in the U.S.; and the increasing scarcity of high-quality assets. Mr. Schulte discussed the diversification of the portfolio, criteria for choosing REOCs and locations, and the process of growing a REOC, sharing a brief overview of each of the REOCs in the PECH portfolio. He said the PECH team tries to apply insight in painting a picture of the future to assist with long-term vision and strategy, and the partnership among PECH, the WSIB, and REOC management has resulted in good performance.

Discussion ensued around the preparations that the REOCs are making for the next market downturn, including focus on strategy and organizational design, and appreciation for the partnership with PECH to date.

[Mr. Longbrake left at 2:16 p.m.]

> **Treasurer McIntire moved that the Private Markets Committee recommend to the Board an additional investment of $500 million, plus fees and expenses, in Principal Enterprise Capital Holdings LLC and the transfer to PECH of the WSIB's direct $200 million commitment to Alere Property Group, subject to continuing due diligence and final negotiation of terms and conditions. Mr. Fox seconded, and the motion carried unanimously.**

PRIVATE MARKETS CLOSING LOG
The Private Markets Closing Log was presented for informational purposes.

OTHER ITEMS
There were no other items to come before the Committee, and the meeting adjourned at 2:28 p.m.