



Tenex Capital Partners III, L.P. - Staff Memo

RECOMMENDATION: Approve up to \$30 million to Tenex Capital Partners III, L.P. Previously, ERSRI committed \$25 million to Tenex Capital Partners II, L.P., a 2016 vintage fund.

ASSET CLASS: Private Equity

SUB-STRATEGY: Lower middle-market buyout

ALLOCATION: The target allocation for private equity is 11.25% (increased in 2017 from 7%) and the allocation as of 9/30 is 8.5%. The pacing plan for private equity is \$270 million per year committed to 5 - 10 primary funds per year at \$20 - \$60 million per primary fund.

PORTFOLIO FIT: ERSRI has emphasized deploying into middle and lower middle-market buyout strategies with a sector focus and/or operational value-add strategy. Tenex primarily targets middle-market, operationally underperforming, family-owned companies and corporate carve-outs where they focus on driving operational value-add through their deep operational expertise. This strategy is complementary to the bulk of ERSRI's private equity portfolio that focuses on backing average to above average performing companies. The strategy is expected to perform well in a dislocated or volatile market environment.

MERITS: Tenex has a focus on operational leverage as opposed to financial leverage to achieve target returns. The team structure is differentiated in that the operations team is part of the firm management and investment committee and involved in due diligence. Each deal is staffed with an operations and investment team member. Other firms typically drop in operating members post-acquisition and they are not part of firm management or investment committees. Tenex uses this team and approach to make value-oriented investments in underperforming companies where they can bring the companies to or above industry average performance.

CONCERNS: Fund I is currently marked below the median benchmark return. This is attributable to losses in companies with cyclical end markets. Since Fund I, Tenex has focused its strategy to target underperforming companies that are outside of cyclical end markets and has added deal sourcing resources to see more opportunities. Fund II lacks substantial realizations given the immaturity of the portfolio. However, it is performing well and ranks in the second quartile.

ESG: Tenex ranks as an integrator on ESG. ESG items are part of their current due diligence workstream. The team gave examples of turning down deals due to ESG risks uncovered. They are currently developing more standardized KPIs to track certain metrics and be proactive to make positive changes.

FEES: The fees are in accordance with industry standards. There is a 2% management fee that steps down to 1.75% on net invested after the investment period. There is a 20% carry with an 8% preferred return.