



State of Rhode Island
Office of the General Treasurer

**Level Equity Growth Partners V, L.P. &
Level Equity Opportunities Fund 2021, L.P.**
- Staff Recommendation
June-2021

RECOMMENDATION: Approve a commitment of up to \$30 million to Level Equity Growth Partners V, L.P. and a commitment of up to \$20 million to Level Equity Opportunities Fund 2021, L.P. Level Equity Growth Partners V, L.P. will pursue investments in lower-middle-market software and technology-enabled services companies, while Level Equity Opportunities Fund 2021, L.P. will invest in subsequent funding rounds of more mature companies already in Level Equity's portfolio and will invest in the same financing rounds as the main fund in situations where there is additional equity needs beyond what the main fund can contribute. ERSRI previously committed \$17.5 million to Level Equity Growth Partners IV (2018 vintage) and \$15 million to Level equity Opportunities Fund 2018 (2018 vintage).

ASSET CLASS: Private Equity

SUB-STRATEGY: Lower Middle-Market Growth Equity

ALLOCATION: The target allocation for private equity will be 12.5% effective July 1, 2021 (increasing from 11.25% previously but now including opportunistic distressed debt investments) and the actual allocation as of 5/31 is 10.4%. The pacing plan for private equity is \$300 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-market buyout and growth strategies with a sector focus and/or operational value-add strategy. Level targets high-growth lower middle-market firms in the software and technology-enabled services sectors. Level typically invests alongside founders as first institutional capital to help grow and professionalize their businesses. Level Equity Growth Partners V, L.P. ("LEGP V") will pursue both majority and minority investments, seeking to include minority protections in non-control deals. Level Equity Opportunities Fund 2021, L.P. ("LEOF 2021") will invest in subsequent funding rounds of more mature companies already in the Level Equity portfolio and will invest in the same financing rounds as the main fund in situations where there is additional equity needs beyond what the main fund can contribute.

There are different styles of growth equity investing. Level's implementation of growth equity, which focuses on partnering with management teams who roll a significant portion of equity, acting as the first institutional capital, and limiting its use of leverage, fits squarely into ERSRI's target exposure. This commitment will take the portfolio's growth equity exposure to 7.6% based on current NAV plus unfunded commitments in commitments made up to this point.

MERITS: Level's co-founders have worked together for 17 years and are well versed in the software and technology ecosystem. They have demonstrated a strong track record with five of the firm's six prior growth funds generating returns in excess of a 20% net IRR. At the core of the strategy is the firm's data driven direct sourcing model. The data analysis allows the investment team to efficiently track metrics it expects to be strong indicators of growth. The data then guides where the large direct outbound calling effort targets and prioritizes where senior team members spend time meeting prospective company founders. Through this system, Level can consistently find high growth bootstrapped companies, typically outside of processes. Even if the company eventually engages an advisor to conduct a sale process, Level will

have already built a relationship with the management team and familiarity with the business prior to that sales process. This proactive relationship building is very valuable as it allows the firm to stand out in these competitive situations.

CONCERNS: Level Equity is targeting a larger fund size across the main fund and the opportunity fund. This could cause strategy drift as it may be more difficult to invest in small companies, especially in minority investment structures. However, Level has consistently invested in a blend of minority and majority transactions across its history, with no material difference in performance. The larger majority deals the firm has executed have largely continued to be in-line with their strategy of providing first institutional capital to growing bootstrapped companies that are sourced through their direct outreach approach. The growth of the team as they continue to promote from within will allow Level to add a few more companies to Fund V than prior funds. We do expect to see a few more select larger deals in Fund V, but continued deployment into the smaller deals and minority transactions. Lastly, the larger fund size has given Level the ability to build a portfolio operations team that has driven value in areas such as talent recruitment, marketing and sales strategies and technology consultation.

ESG: Level is classified as an ESG **Integrator**. The firm has developed a Responsible Investment Policy which draws from a variety of external codes and standards. Level's investment professionals are trained to incorporate ESG consideration into their due diligence and present any ESG risks and opportunities to the Investment Committee. The firm recommends that its portfolio companies adopt an ESG policy and perform annual reviews of ESG initiatives and compliance, which is presented to its companies' Boards. There is a strong culture of emphasizing diversity and inclusion at the firm. Level has an internal Diversity Committee and implements firmwide anti-bias training.

FEES: The blended fees from the recommended mix of commitments to LEGP V and LEOF 2021 are in accordance with industry standards. The management fee for LEGP V is 2.5% on commitments during the investment period, followed by a 2.0% fee on funded commitments thereafter. The management fee for LEOF 2021 is 1.0% on invested capital. The management fees for both funds are 100% offset by monitoring, directors' transaction, break-up and other fees. Carry for LEGP V is 20% over an 8% return hurdle, with an 80/20 GP/LP catch-up. Carry for LEOF 2021 is 15%, or 20% over a 20% return hurdle, with an 85/15 GP/LP catch-up.