



State of Rhode Island
Office of the General Treasurer
PSC V (A), LP – Staff Recommendation
July-2023

RECOMMENDATION:

- [Rhode Island Employees Retirement Systems Pooled Trust \(“ERSRI”\)](#): **Approve a commitment of up to €30 million to PSC V (A), LP (“PSC V”)**. ERSRI committed €40 million to PSC IV (B), LP a 2020 vintage fund (exposure shown in *Appendix 1*, performance shown in *Appendix 2*).
- [Rhode Island OPEB System Trust \(“OPEB”\)](#): **Approve a commitment of up to €1 million to PSC V (A), LP (“PSC V”)**.

ASSET CLASS: Private Equity (ERSRI), Private Growth – Private Equity (OPEB)

SUB-STRATEGY: Middle Market Buyout (Europe)

ALLOCATION:

- [Rhode Island Employees Retirement Systems Pooled Trust \(“ERSRI”\)](#): The target allocation for Private Equity is 12.5% and the allocation as of 6/30/2023 is ~16.4%. The current pacing plan for the 2023 vintage is \$200 million committed to 5-10 funds at \$15-40 million per fund. Pending approval of the recommendations above, ERSRI’s 2023 vintage commitments to Private Equity will be ~\$140.8 million¹.
- [Rhode Island OPEB System Trust \(“OPEB”\)](#): The target allocation for Private Growth is 5.0% and the Private Equity sub-strategy is targeted to be ~80% of the asset class (i.e., 4.0% at the OPEB Trust level). The actual allocation to Private Equity of 6/30/2023 is ~0.6%. The current pacing plan for 2023 is \$9 million committed to 5-10 primary funds at \$0.5-2 million per fund. Pending approval of the recommendations above, OPEB’s 2023 vintage commitments to Private Equity will be ~\$5.4 million¹.

PORTFOLIO FIT:

- [Rhode Island Employees Retirement Systems Pooled Trust \(“ERSRI”\)](#): ERSRI’s Private Equity allocation is composed of a core of buyout strategies, complemented by venture capital, growth equity and opportunistic credit investments. Rhode Island targets 60-80% of the allocation to be in buyout strategies and seeks to build a portfolio diversified by geography, sector, and company size. Most of ERSRI’s buyout exposure is composed of U.S.-focused middle-market strategies, with additional diversification provided through investment managers targeting international markets (see *Appendix 3*) to maintain strategic exposures to a wide range of geographies. In particular, Rhode Island focuses on international managers that invest in a pan-regional approach to provide efficient coverage of ex-U.S. regions. Pollen Street’s strategy fits well within the latter segment of the buyout portfolio. PSC V will invest in middle market financial services companies headquartered in Europe. The strategy targets five core subsegments: lending, payments, wealth & asset management, insurance, tech-enabled services. Roughly 50% of the portfolio is expected to be invested in UK-based companies, with the remainder invested in continental Europe. PSC V will target 12-14 companies with EBITDAs of up to €20 million and enterprise values of up to €200 million. Most deals will be majority buyouts but PSC V may also include select minority transactions for which it will seek strong alignment with other co-owners and structured control rights. Pending approval of the proposed

¹ Values based on USD exchange rates as of June 30, 2023.

recommendations, Pollen Street would represent 3.2% of ERSRI's Private Equity portfolio and 10.7% of the global and international-focused buyout exposure (NAV + uncalled commitment) (see *Appendix 4*).

- [Rhode Island OPEB System Trust \("OPEB"\)](#): The Private Growth portfolio allocates to Private Equity (as described above) and Non-Core Real Estate strategies and is ramping up to its target allocation through commitments made in tandem with ERSRI. Pending approval of the recommendations, PSC V would represent 6.7% of OPEB's Private Growth exposure and 9.4% of its Private Equity exposure (see *Appendix 5*).

MERITS:

- [Experienced Team](#): Pollen Street is led by a team of 5 Founding Partners who have worked together for over 17 years and supported by 13 other investment professionals that focus on 2 of the firm's 5 verticals and have developed deep knowledge of these subsectors both at Pollen Street and prior roles. The investment professionals are supported by its 4-person in-house operating team, the Hub, and 3 operating advisors who collectively work to drive operational initiatives such as technology development, digital marketing, customer onboarding, IT procurement, and ESG initiatives. Hub members and advisors are former consultants and industry professionals and are able to both guide portfolio company management as well as step in as temporary executives in roles like Chief Technology Officer during times of management transition.
- [Sector Focus](#): Pollen Street exclusively focuses on the financial services companies and has developed a reputation as a knowledgeable and credible private equity partner to founders and management in this space. The firm has sourced most of its deals through pro-active origination efforts or network introductions by industry executives and advisors. The firm has completed roughly 30 deals in this space dating back to the strategy's existence within RBS. Due to this focused approach, Pollen Street has been able to recycle elements from previously successful growth initiatives at new portfolio companies to successfully implement geographic expansion through M&A, new product rollouts, technology onboarding, and customer acquisition.
- [Pan-European Strategy](#): Pollen Street employs a pan-European approach to financial services private equity investing. As mentioned in the *Portfolio Fit* section, Pollen Street's geographic coverage fits well within Rhode Island's strategy of partnering with pan-regional investment managers outside of the U.S. The firm focuses its activity within the U.K. which is the largest European financial services market, while seeking diversification by targeting smaller markets on continental Europe. In addition, continental Europe has seen less M&A activity in financial services relative to its share of economic contribution to the sector and thus may offer less competitive bidding processes. Many countries in continental Europe also lag the U.K.'s development of financial services markets, allowing Pollen Street to use lessons learned from its investments in companies in the U.K. to drive outcomes on continental Europe as similar themes play out over time.

CONCERNS:

- [Public Listing](#): In 2022 Pollen Street combined with Honeycomb Investment Trust, a public BDC entity, and the combined entity (Pollen Street PLC) was listed on the London Stock Exchange (LSE). As a publicly listed investment manager, Pollen Street will have to manage potential misalignment of interests between its private fund investors and its public shareholders. The firm may be pressured by shareholders to raise larger funds. Shareholders may also demand that an outsized share of carried interest generated by the funds accrue to the "house" rather than be split amongst the investment team, reducing incentives for the team to generate strong outcomes for the funds they manage and potentially making it more challenging to retain high performing investment professionals.
 - [Mitigant – Thoughtful Governance](#): Pollen Street's founding partners have retained significant ownership of the organization. The firm's Founding Partner and CEO Lindsay McMurray and CFO both sit on the public company board and the private equity activities of Pollen Street Capital remain independent from board decisions.
 - [Mitigant – Carried Interest Split](#): Pollen Street's private equity team has thus far retained most of the carried interest it generates, incentivizing strong funds outcomes above the fund hurdle rate of 8%

- **Build out of Credit Strategies:** Pollen Street has built out a sizable credit strategy that now makes up almost half of its gross asset under management. This parallel investment business may draw the firm’s focus and resources away from the private equity strategy to its detriment. Additionally, certain conflicts may arise with respect to allocating opportunities that the firm sources among the equity and credit strategies.
 - **Mitigant – Separation of Strategies:** The private credit business is overseen by a separate investment team of 15 investment professionals, allowing the private equity investment team to focus on its sole strategy. Furthermore, there is no business interaction between these two strategies as no portfolio company in a Pollen Street private equity fund can receive majority financing for any of its credit facilities from the credit strategy without the approval of its investor Advisory Board.
 - **Mitigant – Broader Market View:** By participating in both the equity and credit within the financial services market, Pollen Street may be better positioned to generate sector insights and originate from a more robust deal flow. The firm has historically been able to source investments for its private equity strategy that were first brought to its private credit team. By operating as a lender to non-bank finance companies, Pollen Street may be more familiar with sources of profitability in lending operations and utilize these insights to drive profitability in its portfolio companies participating in the lending subsector.

ESG: Pollen Street is rated as a **Leader** with respect to its ESG practices.

- **ESG:** Pollen Street has developed an ESG Policy, is a UN PRI signatory, and participates in the ILPA ESG Data Convergence Initiative, Initiative Climat International, and the FAIRR Initiative. The firm’s ESG strategy and activities are overseen by an ESG Committee. The firm has a Head of ESG entirely dedicated to working with portfolio companies to set ESG strategic direction, managing ESG initiatives, and sharing best practices across the portfolio. The firms’ investment team receives regular training and evaluates ESG issues in its due diligence. Pollen Street collects roughly 50 ESG data points from its portfolio companies which it incorporates into a proprietary rating system to assign an ESG score to each of its companies. Through ESG value-add, the firm aims to improve this score over a company’s ownership period. Pollen Street reports its ESG initiatives to investors annually.
- **DEI:** Pollen Street is committed to fostering a culture of diversity, equity and inclusion within its firm and portfolio. The firm has a DEI Policy and the firm established a DEI working group within its ESG Committee. Its Chief People Officer leads DEI initiatives within its organization and works with its Head of ESG to share best practices across the portfolio. The firm’s employees are regularly trained in DEI topics. The firm tracks DEI statistics as part of its ESG data collection and scoring initiatives for its portfolio companies, including gender pay gap data and gender employment ratios. Internally, Pollen Street tasks its recruitment partners to present it with diverse shortlists of candidates and over 50% of its hires over the last 18 months were female.

FEES: Fees for PSC V are in-line with industry standards.

- **Management Fee:** The management fee is 2% per year of fund commitments during the investment period and 2% of invested capital thereafter. The management fee is 100% offset by director, transaction, monitoring, and other such fees. ERSRI and OPEB would both receive a 6-month fee waiver for participating in the first close at a size of over €30 million in committed capital.
- **Carried Interest:** The carried interest will be 20% after an 8% hurdle rate is reached with a 100% catch-up. The carried interest will be charged on a fund-wide basis with a clawback provision.

Appendix 1: ERSRI Pollen Street Prior Fund Exposure

Current Partnerships	Fund Exposure*						
	Vintage Year/ Initial Investment	Type	Amount Committed	Amount Drawn	Amount Distributed	Amount Unfunded	Valuation
Pollen Street Capital IV, L.P.	2020	Buyout	€ 40,000,000	€ 22,523,300	€ 3,085,939	€ 17,476,700	€ 23,625,316

*Data as of 3/31/2023

Appendix 2: ERSRI Pollen Street Prior Fund Performance

Current Partnerships	Vintage Year/ Initial Investment	Type	Net Performance*			Public Market Equivalent (PME)	
			Net IRR (%)	Net Multiple of Investment	Distributed to Paid-In Capital	MSCI ACWI Net Index PME IRR**	Fund Excess Return (Fund IRR - PME)
Pollen Street Capital IV, L.P.	2020	Buyout	16.22%	1.19	0.14	-1.20%	17.42%

*Data as of 3/31/2023

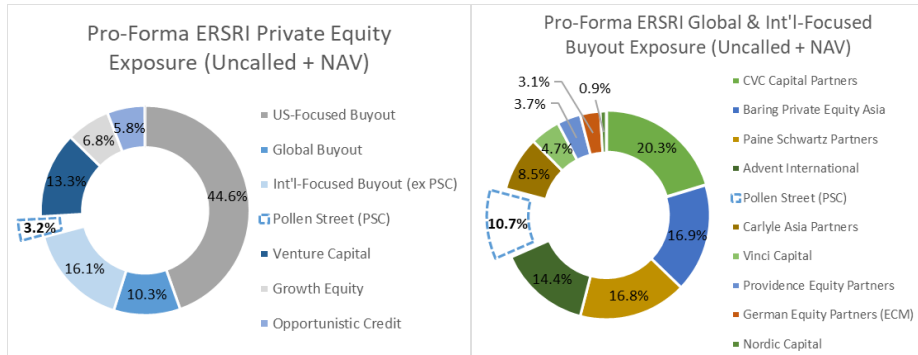
** Long Nickels PME Methodology

Appendix 3: ERSRI Global and International Buyout Managers (Pro-Forma for PSC V)

Global & International-Focused Buyout (ERSRI)				
Manager	Exposure in MM USD* (NAV+Uncalled)	Geographic Focus	Sector Focus	Size
CVC Capital Partners	160	Europe	Diversified	Large & Upper Middle Market
Baring Private Equity Asia	133	Asia	Diversified	Large & Upper Middle Market
Paine Schwartz Partners	132	Global (Majority US)	Sector-Focused (Food & Ag)	Middle Market
Advent International	113	Global	Diversified	Large & Upper Middle Market
Pollen Street Capital (Pro Forma)	84	Europe	Sector-Focused (Financial Services)	Middle Market
Carlyle Asia Partners	67	Asia	Diversified	Large & Upper Middle Market
Vinci Capital	37	LatAm	Diversified	Middle Market
Providence Equity Partners	29	Global (Majority US)	Sector-Focused (Communications & Media)	Large & Upper Middle Market
German Equity Partners (ECM)	25	Europe	Diversified	Middle Market
Nordic Capital	7	Europe	Diversified	Middle Market

*Using 6/30/2023 Exchange Rates

Appendix 4: ERSRI Portfolio Fit (Pro-Forma for PSC V)



Appendix 5: OPEB Portfolio Fit (Pro-Forma for PSC V)

