Recommendation for HPS Specialty Loan Fund V

To:	RISIC
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The purpose of this memo is to provide RISIC with a summary of Cliffwater's recommendation on HPS Specialty Loan Fund V. ("HPS SLF V" or the "Fund"). Cliffwater has completed its investment due diligence and operational due diligence and recommends the Fund as part of ERSRI's Private Credit allocation.

Summary of HPS SLF V

Fund Overview: HPS SLF V will make direct loans to upper middle-market companies primarily located in the U.S.

People and Organization: HPS Investment Partners ("HPS" or "the Firm") was founded in 2007 to manage both private and public credit strategies. The Firm had previously been a subsidiary of J.P. Morgan Asset Management ("J.P. Morgan"), but the management team bought out J.P. Morgan in March 2016 through a deferred payment structure. The Firm subsequently sold an interest of approximately 15% to Dyal and utilized the proceeds to further reduce J.P. Morgan's interest in the HPS. The Firm is currently led by Scott Kapnick, who serves as CEO, and a deep senior team of 41 managing directors across all strategies. HPS has teams focused on direct lending, mezzanine, real estate credit, European financial assets, CLOs, leveraged loans, and liquid credit opportunities. As of June 1, 2021, HPS manages a total of $72 billion of assets including $49 billion in private credit. The direct lending team currently manages $29 billion of assets. HPS has over 400 employees, including 159 investment professionals, located in 12 offices globally. The headquarters is in NYC. The direct lending team is led by Michael Patterson and is comprised of 80 investment professionals including shared resources with the mezzanine strategy. The Fund has an eight-member investment committee comprised of Scott Kapnick, Scot French who leads the mezzanine strategy, Michael Patterson, Purnima Puri who leads public credit, and Faith Rosenfeld, chief administrative officer.

Investment Strategy and Process: The Fund will seek to directly originate senior secured loans to middle-market companies. The Fund will target non-sponsor companies and sponsor-backed companies where there is a sourcing angle or timing issue that allows HPS to generate premium pricing. The direct lending team will invest primarily in first lien loans, but may invest in second lien loans on an opportunistic basis. The Fund targets upper middle market companies with EBITDA of $75 million to $350 million. HPS may invest in larger companies where there is some competitive advantage from a sourcing angle or the Firm believes there is a premium driven by a market dislocation or idiosyncratic event. The typical leverage profile of HPS' companies is between 3.0 and 5.0 times net debt-to-EBITDA and/or a loan-to-value of 70% or lower. The average leverage through HPS' investment in the prior fund, a 2016 vintage, has been 4.2 times net debt-to-EBITDA. The portfolio will consist of 70 to 100 loans with investment sizes ranging from 1% to 3%. HPS expects 50% to 70% of deals to be non-sponsored, or not sponsor sourced, and 30% to 50% of deals to be sponsored. The target cash yield for the portfolio is 9% to 11%. Industry concentration is expected to be diversified with most sector exposures below 15%. HPS anticipates holding most loans for two to four years. The strategy will primarily be North America focused with a secondary focus on Europe, Australia, and New Zealand. North America is expected to be 70% to 85% of the portfolio.

Performance: Since 2010, HPS has raised $16 billion across three prior commingled funds and separate accounts. The commingled funds have generated a combined net levered IRR of 7.5% as of December 31, 2020. As of December 31, 2020, HPS' commingled direct funds have generated a net levered IRR of 7.5% since 2010. Investing in the S&P Leveraged Loan Index during the same period, at the same pace, would have generated a return of 4.6%. HPS has outperformed the Index by 2.9%.

Investment Terms: Cliffwater finds the investment terms, taken as a whole, to be in accordance with industry standards. The Fund is offered in an unlevered and levered structure. The levered structure is expected to be levered 0.5 to 0.8 times. The management fee for the unlevered and levered vehicles is 1.5% on gross assets, including leverage. The fee for the levered vehicle is capped at 1.5% of committed capital. Cliffwater has negotiated a fee discount of 0.25% for its clients. The investment period is three years with a six-year fund term. The carried interest for both the unlevered and levered vehicles is 15% on a deal-by-deal basis. The preferred return is 5% for the unlevered vehicle and 7% for the levered vehicle. The preferred return does not include capital drawn for management fees and is not compounded.

<u>Cliffwater Recommendation</u>
Cliffwater recommends an investment of up to $50 million to the levered structure of HPS Specialty Loan Fund V as part of ERSRI's Private Credit allocation.