

High Yield Commitment



Sankaty Credit Opportunities VI, L.P.

June 11, 2015

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Overview

- Sankaty Advisors, LLC (“Sankaty” or the “Firm”) was formed in 1998 as an independently managed affiliate of Bain Capital, LLC (“Bain Capital”) and currently manages ~\$25.5 billion in committed assets
- Invests across the full spectrum of credit strategies; including leveraged loans, high-yield bonds, distressed debt, direct lending, structured products, non-performing loans (NPLs) and equities
- Sankaty Credit Opportunities VI, L.P. (“COPs VI” or the “Fund”) is being raised with a target of \$3.0 billion to continue the Firm’s distressed and special situations strategy

Market Opportunity

- Default cycle picking up as a result of record setting credit issuance
- New regulations forcing asset sales and curtailing new lending
- Several large industries facing secular challenges, including; energy, retail, metals/mining, media and shipping
- Global economy in flux driven by growth concerns in Europe and emerging markets

Investment Strategy

- Opportunistic credit strategy focused on global distressed securities and special situations
- Geographic Exposure: 50-60% U.S., 40-50% Europe, <10% Asia Pacific
- Expect to have 30-50 positions with an 18 month weighted average life
- Target \$25 million to \$100 million invested capital per deal; generally will not exceed 5% per issuer
- 13% to 17% net IRR/1.5x TVPI fund-level return target including recycling
- Fund-level leverage permitted up to a 20% cap, limited to subscription line
- Fully hedge currency exposure

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Investment Team

- Sankaty has a staff of 232 employees with 111 investment professionals, including 32 senior industry credit analysts. 31 Managing Directors have an average of >20 years experience
- Sankaty is headquartered in Boston, with additional offices across North America, Europe and Asia Pacific

GP “Value Add”

- Experienced and cohesive senior management that has invested through multiple cycles since 1998, with 73 investment professionals at the VP-level and above averaging >7 years at the Firm
- Opportunistic investment strategy, capitalizing on best ideas across the COPs mandate regarding global distressed and special situations
- Scale, geographic footprint and industry-based focus
 - 36 of 111 total investment professionals are based outside the U.S.
 - 14 industry research teams provide sourcing edge and in-depth analysis of each credit covered with >5,000 issuers analyzed since inception, and currently tracks >500 issuers. The mid-market and restructuring groups are also an important source of deal flow
 - Access to Bain Capital platform enhances Sankaty’s ability to source investments and generate deal flow
- Aligned interests
 - 100% employee-owned private partnership
 - Sankaty/Bain Capital committing at least \$150 million to COPs VI

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Potential Risks/Mitigants

- Risk: **Competition from other distressed debt investment managers**
 - *Mitigant: While competition does exist in the distressed space, Sankaty's platform is differentiated due to their deep team, geographic footprint and flexible strategy. Sankaty's investment professionals have extensive experience analyzing companies and investing across market cycles. Furthermore, 36 of 111 total investment professionals are based in Europe and Asia, providing Sankaty a differentiated insight into sourcing channels and legal regimes. Lastly, Sankaty's flexible strategy allows the Firm to opportunistically invest throughout the debt capital structure and across geographies.*
- Risk: **Potential for diminished returns as a result of Sankaty's platform growth**
 - *Mitigant: While Sankaty's team has grown and their global footprint has increased, they have limited the growth of capital for their COPs funds to increase investment selectivity. COPs VI is targeting \$3.0 billion in commitments relative to the \$2.5 billion COPs V investment program which compares favorably to the 26%+ growth in Sankaty's investment team since raising COPs V in 2012.*

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PSERS History & Performance (as of 12/31/2014)

A commitment to COPs VI will represent PSERS' eighth commitment to Bain Capital/Sankaty:

<u>Fund (\$mm)</u>	<u>Portfolio</u>	<u>Vintage</u>	<u>Commitment</u>	<u>Contributions</u>	<u>Distributions</u>	<u>Market Value</u>	<u>Net IRR</u>	<u>MOIC</u>
Sankaty Credit Opportunities IV, L.P.	High Yield	2008	\$ 500.0	\$ 475.0	\$ 558.7	\$ 124.2	12.4%	1.4x
Sankaty Credit Opportunities V-A, L.P.	High Yield	2012	350.0	254.6	17.1	259.6	9.2%	1.1x
Sub-Total Credit Opportunities			\$ 850.0	\$ 729.6	\$ 575.8	\$ 383.7	12.1%	1.3x
Sankaty Middle Market Opportunities Fund, L.P.	High Yield	2010	\$ 250.0	\$ 242.5	\$ 177.7	\$ 118.8	11.6%	1.2x
Sankaty Middle Market Opportunities Fund II, L.P.	High Yield	2013	200.0	69.0	0.0	72.2	8.1%	1.1x
Sankaty Advisors LLC – Bank Loans	High Yield	2009	500.0	500.0	325.0	415.6	10.0%	1.5x
Total Sankaty - PSERS			\$ 1,800.0	\$ 1,541.1	\$ 1,078.5	\$ 990.3	11.0%	1.3x
Bain Capital Asia Fund II, L.P.	Private Equity	2012	\$ 100.0	\$ 57.5	\$ 5.8	\$ 61.5	12.9%	1.2x
Bain Capital Fund XI, L.P.	Private Equity	2013	100.0	16.3	0.0	15.5	(-6.4%)	1.0x
Total Bain Capital/Sankaty - PSERS			\$ 2,000.0	\$ 1,614.9	\$ 1,084.3	\$ 1,067.3	11.0%	1.3x

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Board Issues

- **Pennsylvania Presence:** None
- **Placement Agents:** None
- **PA Political Contributions:** None
- **Relationship with Consultant:**
 - Portfolio Advisors is invested through their discretionary fund relationships with Sankaty and Bain Capital, including Bain Capital Asia Fund I & II; Bain Capital Europe III, Bain Capital VI, VII, VIII, IX, & X; Sankaty COPS I, II, III, & IV; and Bain Venture Fund 2009 & 2012

Recommendation

- Staff, together with Portfolio Advisors, recommends that the Board invest an amount not to exceed \$250 million plus reasonable normal investment expenses

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May 20, 2015

Board of Trustees
Pennsylvania Public School Employees' Retirement System
5 North 5th Street
Harrisburg, PA 17101

Re: Sankaty Credit Opportunities VI, L.P.

Dear Trustees:

Sankaty Advisors LLC, (“Sankaty” or the “Firm”), is seeking to raise \$3 billion of commitments for Sankaty Credit Opportunities VI, L.P. (the “Fund” or “COPs VI”). The Fund is Sankaty’s sixth series of funds in its Credit Opportunities investment program and is being formed to invest opportunistically in global distressed securities and special situations. Formed in 1998, Sankaty is the credit investment affiliate of Bain Capital and manages approximately \$25.5 billion of committed capital. COPs VI expects to hold a first close on July 1, 2015 and anticipates holding a final close in December 2015. The GP plans to commit \$150 million to COPs VI.

COPs VI will target credit and special situations opportunities resulting from market dislocations and/or stressed and distressed corporate issuers. COPs VI’s mandate will include global distressed securities and special situations (see below for further descriptions). The Fund will target securities which are expected to yield greater than 15%. Fund VI has the flexibility to invest across corporate capital structures, geographies and in the public and/or private markets. COPs will invest in cash bonds, senior secured loans, subordinated and mezzanine notes and DIP facilities, and various forms of public and private equity securities, which may be inherited or created as part of a restructuring. Due to the size of the team and the flexibility of the strategy, Sankaty generally will have 30-50 positions in the Fund when fully invested. Sankaty targets \$25-200 million invested capital per deal, and generally will not exceed 5% of net exposure in any individual issuer. Holding periods may vary, but for prior COPs funds, they typically have had a weighted average life of approximately 18 months.

Sankaty utilizes a bottom-up, fundamentally driven investment approach, leveraging the depth and experience of the 108 person investment team, to rigorously analyze credits which may be underfollowed, mispriced or perhaps out of favor with the market due to headline risk. The Firm seeks to uncover opportunities that are either too small to be meaningful to larger peers or too complex for smaller competitors who lack the resources to perform the proper due diligence. When considering an investment that meets the Fund’s return objectives, Sankaty seeks to minimize the downside risk. In addition, Sankaty is able to leverage its significant scale and presence in the public and private fixed income markets.

Sankaty believes that the prior COPs funds have benefited from their flexible nature, allowing Sankaty to shift the mix of assets based on the opportunities available in the broader credit markets. Sankaty believes



that over the anticipated life of the Fund, both of the targeted asset classes (global distressed securities and special situations) will experience windows of attractive risk-adjusted returns. The flexible structure of the Fund is designed to enable it to maximize risk adjusted returns by accessing the best ideas from each of the targeted asset classes.

Portfolio Advisors' recommendation is based upon the following analytical factors and is made within the context of PSERS' investment guidelines.

- Detailed due diligence, including interviews with industry peers and private equity professionals. The on-site due diligence visit was performed on May 7, 2015.
- Evaluation of the composition of the investment team, how they work together, compensation structure and other factors that help determine whether a group is likely to be able to replicate past successes as currently configured.
- Evaluation of the Fund's proposed investment strategy within the context of the current investment environment.
- The strategy proposed for the Fund is appropriate for the High Yield Fixed Income component of the portfolio.

The individuals at Portfolio Advisors who were primarily involved in the due diligence process for the Fund are:

Kenneth Jarvis – Managing Director, Darien Office
Mckay Dunn – Senior Associate, Darien Office

Based on the above, Portfolio Advisors recommends that PSERS commit to up to \$250 million in Sankaty Credit Opportunities VI, L.P. Portfolio Advisors makes this recommendation considering the General Partner's qualifications and PSERS' overall investment guidelines.

This recommendation is given solely for the benefit of PSERS and cannot be relied upon by other investors considering an investment in the Fund, since their needs, objectives and circumstances may not be identical to those of PSERS. The scope of this recommendation is limited to the investment merits of the Fund. Portfolio Advisors does not provide legal or other non-investment-related advice.

Sincerely,

WILLIAM J. INDELICATO
MANAGING DIRECTOR