



Public Investment Memorandum

Capstone Commonwealth Fund, LP

Tail Risk Mitigation Commitment

Carl Lantz

Senior Portfolio Manager, Traditional Investments

Larry Shank

Portfolio Manager, Traditional Investments

Mike Kondas

Portfolio Manager, Traditional Investments

Michael O'Toole

Senior Investment Professional, Traditional Investments

May 26, 2021



Executive Summary:

PSERS' Investment Office Professionals, together with Aksia L.L.C. ("Aksia"), recommend that PSERS commit \$80 million in Established Program Size ("EPS") with the Capstone Commonwealth Fund L.P. (the "Fund") for the first year of the Fund, with annual top-ups thereafter. This recommendation is based on our assessment of the investment strategy and our evaluation of Capstone Investment Advisors, L.L.C. and its affiliates.

Fund Name	Capstone Commonwealth Fund L.P.
Firm Name	Capstone Investment Advisors, L.L.C
Target Fund Size / Hard Cap	Not applicable. This Fund is not a commingled fund but is instead a fund of one.
Recommended Commitment Amount	\$80 million in Established Program Size for first year of Fund, with annual top-ups thereafter
Existing Relationship	No
Source of Funds	Cash
Asset Class / Sub Asset Class	Tail Risk Mitigation
Investment Office Oversight	Thomas Bauer, Deputy CIO, Traditional Investments Carl Lantz, Senior Manager, External Managers, Traditional Investments
External Consultant Oversight	Aksia

Firm Overview:

Founded in 2004 by CEO Paul Britton and opened to external capital in 2007, Capstone is a global, alternative investment management firm operating across a broad range of derivatives-based, volatility-oriented strategies, with \$8.7 billion in assets under management as of March 31, 2021.

The firm operates in two distinct business lines. The first is a multi-strategy hedge fund business with \$5.6 billion in AUM, which trades derivatives across asset classes and regions, with a focus on volatility and relative value. The second is a solutions business with \$3.1 billion in AUM that provides customized mandates and strategies tailored to client needs across the volatility and derivatives spectrum. PSERS investment with Capstone falls within the solutions business line.

Capstone had 183 employees as of March 31, 2021 with 102 of those based at the primary office in New York and the remainder in London, Amsterdam, Stamford, CT and Los Angeles.

Portfolio Fit:

A commitment to the Fund will be allocated to the Tail Risk Mitigation portfolio. Consistent with the Board's Tail Risk Mitigation Strategy Policy, the recommended commitment amount will result in half of the Tail Risk Mitigation portfolio being managed internally and half being managed externally.



The Fund is not intended to be a duplicate of the internally managed program but instead an effective complement. The Fund will incorporate a broader range of instruments and geographies than the internal program. Also, the Fund will provide us full transparency into positions, enabling ongoing strategic dialogue between PSERS internal and investment team at Capstone.

Investment Strategy:

Capstone will seek to provide protection in a way that outperforms a 25% out-of-the-money 3 month put option on the S&P 500. In the absence of a market decline where the protection typically increases in value, Capstone will seek to reduce the natural bleed of the value of put options through active management of positions and skillful selection of hedges.

Investment Team:

The 7 people listed below include people whose responsibilities encompass both business lines of Capstone, and others whose responsibilities are strictly those of the solutions business. The key investment decision-maker for the Fund is Rish Bhandari who works only in the solutions business. Mr. Bhandari is assisted by other members of the solutions team.

Name	Title	Yrs. Experience Capstone / Total	Prior Experience
Paul Britton	Chief Executive Officer	16/26	Mako Global Derivatives Saratoga Limited
Katrina Paglia	General Counsel & Chief Compliance Officer	2/15	Sculptor Mananagement MD Sass American Express Venable
Felix Cua	Chief Risk Officer	3/25	Citadel Investment Group III Advisors Perot Investments Tequesta Capital Advisors
Rish Bhandari	Senior Portfolio Manager	4/15	Nomura Credit Suisse Lehman Brothers/Barclays Capital
Jordan Sinclair	Director, Derivatives Research Specialist	8/14	BNP Paribas CDK Investments Navigant Consulting
Julian Stein	Director, Client Solutions	0.5/15	Incline Global Perella Weinberg Partners Bank of America
Connie Wu	Associate, Client Solutions	3/3	n/a

As of May 1, 2021



Investment and Risk Highlights:

- Application of Board Level Tail Risk Mitigation Strategy Policy
- Investment Manager
- Tail Hedge Manager Selection
- Fit with Internal Tail Hedging Program
- Performance Benchmarking
- “Fund of One” Structure
- Ongoing Funding
- Hedge Portfolio Construction
- Monetization
- Performance Analysis
- Risks Associated with Track Record

Investment Committee Disclosure:

Relationship with Aksia:	Capstone Investment Advisors, LLC (“Capstone”) does not have a business relationship with Aksia LLC. The interactions/meetings that Capstone has previously had with Aksia have been Due Diligence meetings conducted by Aksia on behalf of its clients.
Introduction Source:	Referral from another large public pension fund.
Placement Agent:	In accordance with Board policy, no placement agents were used, and no payments from or on behalf of PSERS to Placement Agents shall be made in connection with securing PSERS’ investment in the Fund. As confirmed by PSERS’ Office of Chief Counsel on May 25, 2021, this investment complies with the Public School Employees’ Retirement Board Placement Agent Policy.
Political Contributions:	Capstone represents to PSERS that there has not been any political contribution, gift or other item of value made or given to candidates for Pennsylvania office by the Investment Manager or any of its Covered Associates during the prior 36-month period. Capstone represents to PSERS that there has not been any political contribution, gift or other item of value made or given to any member of PSERS’ Board, IOP, or Investment Consultant.
PA Presence:	No
Potential Conflicts:	We are not aware of Capstone having any material conflicts.
Litigation Disclosure:	As of March 31, 2021, there is no pending (i) formal investigation or enforcement proceeding by the SEC or any other regulatory (or self-regulatory) or administrative body with authority over Capstone or its funds, (ii) governmental investigation, inquiry or proceeding regarding material violations of applicable law or regulations of any governmental agency, (iii) material litigation, suits or arbitration, or, (iv) criminal proceeding, in each case that is reasonably expected to have a material adverse effect on Capstone’s funds,
First Time Fund With PSERS:	Yes
PSERS Allocation Implementation Committee Approval:	May 26, 2021

Recommendation:

PSERS’ Investment Office Professionals, together with Aksia, recommend that PSERS invests (1) in the first year \$80 million in the Capstone Commonwealth Fund L.P. and/or related investment vehicles (together, “the Fund”), which amount is known as the Established Program Size (“EPS”) and which itself is the sum of the Annual Premium Budget (“APB” and is equal to ½ the EPS) which is equal to \$40 million and a remaining portion for excess collateral purposes (also equal to ½ the EPS) which is equal to \$40



million, plus reasonable normal investment expenses; and (2) at the start of each subsequent year an amount necessary to ensure that the APB and the excess collateral in the Fund at the start of that year each equal no more than $\frac{1}{2}$ of the Budget (as defined in the Tail Risk Mitigation Strategy Policy), plus reasonable normal investment expenses.