



COMMONWEALTH OF PENNSYLVANIA
PUBLIC SCHOOL EMPLOYEES' RETIREMENT SYSTEM

Public Investment Memorandum

Incline Equity Partners IV, L.P.

Private Equity Fund Commitment

Luke M. Jacobs
Portfolio Manager, Private Markets

September 19, 2016



Recommendation:

Staff, together with Portfolio Advisors, recommends to the Board a commitment of up to \$100 million to Incline Equity Partners IV, L.P. ("Fund IV" or the "Fund"). Incline ("Incline" or the "Firm"), a Pittsburgh based investment firm, is sponsoring the Fund to provide control-oriented growth capital to lower middle-market companies.

Firm Overview:

Incline is a private equity firm headquartered in Pittsburgh, PA. They are a provider of control-oriented growth capital to lower middle-market companies in need of a strategic partner. They focus on investing in one of three industry sectors: value-added distribution, outsourced services, and specialized light manufacturing. They are an experienced and successful private equity team with a track record of investing across multiple economic cycles.

Fund Size

Fund IV is seeking equity commitments of up to \$550 million (excluding GP commitment).

Investment Strategy:

Incline's strategy for Fund IV will be to make control-oriented equity investments generally between \$20 million and \$50 million in lower middle market companies with enterprise values generally in the \$50 million to \$200 million range. Incline will focus on change of control buyouts, corporate divestitures and large minority recapitalizations in the value-added distribution, outsourced business and industrial services and specialized light manufacturing sectors in the lower end of the North American middle market, an investment strategy that the Principals have successfully executed together for the past fifteen years (since PNC Equity Partners inception). Fund IV's investment objective is to achieve a superior return on investment, principally in the form of long-term capital appreciation, for its investors. Fund IV will invest primarily in the United States.

Investment Team:

Fund IV investment decisions will require approval by the Principals, who are: John C. Glover, Wali C. Bacdayan and Justin L. Bertram. The table below highlights the experience of the key investment professionals:

Name	Title	Yrs. Experience Firm / Total	Prior Experience
Jack Glover	Partner	20 / 25	Wheat First Butcher Singer
Wali Bacdayan	Partner	19 / 22	Dean Witter Reynolds, Inc.
Justin Bertram	Partner	18 / 20	Bear Stearns
Leon Rubinov	Partner	5 / 15	Sterling Partners
Deanna Barry	CFO	20 / 27	PNC Bank, KPMG

Investment Instruments:

The fund will make private investments in equity, equity-oriented, or other securities in connection with privately negotiated transactions.



Market Opportunity:

Purchase price multiples in the lower middle market tend to be lower as compared to multiples paid for larger businesses for several reasons. First, sale processes for lower middle market companies tend to be less efficient than those for larger companies. Smaller transactions are typically executed by investment banking boutiques and business brokers with fewer resources than their more sophisticated counterparts. Second, in addition to sales processes being less efficient, senior and mezzanine debt capital is often not as readily available in this segment of the market. Lastly, small companies frequently lack some key element of a complete business strategy or management team. These are all factors why pricing in the lower middle market is appealing, because they often have not fully exploited their competitive advantage and/or market opportunity.

Accordingly, smaller companies are generally more responsive to changes which strengthen their management teams, strategic plans and/or operations practices. In smaller companies, it is often easier to identify best practices and operational adjustments that will grow a company and enhance enterprise value beyond a strict reliance on financial leverage or exit multiple arbitrage.

Investment Highlights:

Experienced Management Team
Incline's Principals have led, co-led or managed each of the investments made by the prior funds and were primarily responsible for sourcing and/or managing such investments on behalf of these funds. Incline's team are experienced private equity investors in the lower middle market and have proven their ability to invest across a broad range of economic cycles and market conditions.
Proven Investment Strategy
The Principals have demonstrated their ability to consistently source attractive investment opportunities and create value for investors over various economic cycles. Since 2001, the Funds have invested approximately \$519 million in their sectors of expertise. Realized investments have averaged annual EBITDA growth of approximately 16%. They have completed 93 add-on acquisitions over 3 funds.
Consistent Investment Results
Since 2001, Incline has generated (realized and unrealized) a Net IRR of 16.5% and a Net MOIC of 1.67X.
Market Opportunity
Incline, which began as PNC Equity, has been investing in this space since 2001. Fund IV will be a continuation of that strategy of pursuing control-oriented equity investments in lower middle market companies, which Incline generally defines as companies with enterprise values in the \$50 million to \$200 million range. Incline believes that the lower middle market will offer attractive investment opportunities to experienced investors in this segment like Incline because it remains a less efficient market than the mergers and acquisitions markets for larger companies. Incline believes that companies in this market segment are more receptive to the operational focus and strategic discipline brought by Incline's active portfolio management approach which can result in meaningful improvements in company performance. Incline's active portfolio management approach is based on company specific value-creation strategies which include (i) identifying areas for operational improvement, (ii) completing strategic acquisitions and (iii) augmenting a company's management team and board of directors when appropriate.

Investment/Risk Considerations:

Fund Size
The Fund size, targeted at \$500 million, will be the largest fund the firm has raised thus far. In pursuing Fund IV's investment strategy, the Principals will continue to utilize a rigorous investment process that has been refined over their long tenure together and has generated significant value creation for investors. This process has been in place since 2001 and we expect the same disciplined approach in Fund IV. Long time presence in this market niche, robust deal pipeline, as well as stability of the leadership team should not hinder deployment of capital over time.



Liquidity & Leverage Profile:

The Fund is expected to be invested ("Investment Period") within five years of its final closing. Fund IV may borrow money to pay the reasonable expenses of the Fund, or to provide short-term bridge financing to a portfolio company (or prospective portfolio company) or to provide interim financings to the extent necessary to consummate the purchase of a portfolio company.

PSERS History & Performance:

Since 2001, PSERS has committed approximately \$176 million to three Incline (formerly PNC) managed partnerships. As of June 30, 2016, they have generated a 16.7% net IRR and a 1.67x net MOIC for PSERS. The table below summarizes PSERS' historical performance by partnership:

Fund (\$mm)	Portfolio	Vintage	Commitment	Contributions	Distributions	NAV	Net IRR	MOIC
PNC Equity Partners I	PE	2001	43	39	77	0.4	21.1%	1.96x
PNC Equity Partners II	PE	2007	68	58	77	19	11.1%	1.65x
Incline Equity Partners III	PE	2012	65	32	6	37	15.1%	1.37x
Total			\$ 176	\$ 130	\$ 160	\$ 57	16.5%	1.67x

Portfolio Fit:

A commitment to Fund IV will give PSERS' Private Markets portfolio continued exposure to the lower middle market companies that Incline has invested in. We believe that this is a niche area of the market that is overlooked by larger buyout firms. Incline has historically displayed a proven success of executing buyout transactions while stressing a disciplined approach and consistent growth while minimizing capital loss. PSERS has been investing with the Incline team (formerly PNC) since 2001.

Finance Committee Disclosure:

Relationship with Portfolio Advisors:	Portfolio Advisors has invested in Incline
Placement Agent:	Yes, but none used for PSERS
PA Political Contributions:	None Disclosed
PA Presence:	Yes
Conflicts:	None Disclosed
History with PSERS:	Yes
PSERS AIC Meeting Approval:	Approved on September 19, 2016

Oversight Responsibility:

Investment Office:	Charles J. Spiller Deputy CIO, Non-Traditional Investments	Luke M. Jacobs Portfolio Manager
External Consultant:	Portfolio Advisors LLC	



August 29, 2016

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

Re: Incline Equity Partners IV, L.P.

Dear Trustees:

Incline Equity Partners (“Incline” or the “Firm”) is a growth buyout firm that seeks to invest in or acquire growing, profitable, privately-held companies in the lower middle market. The Firm is currently seeking to raise \$450-500 million (with a \$550 million hard cap) of limited partnership interests for Incline Equity Partners IV, L.P. (“IEP IV”, “Fund IV” or the “Fund”). Fund IV will seek to make control-oriented equity investments generally between \$20 million and \$50 million in lower middle market companies with enterprise values generally in the \$50 million to \$200 million range. Incline will focus on change of control buyouts, corporate divestitures and large minority recapitalizations in the value-added distribution, outsourced services and specialized light manufacturing sectors (the “Core Business Sectors”), an investment strategy that the Partners of Incline have successfully executed together for the past 15 years. The first closing is scheduled for the end of November or early December 2016. The intent is to hold a dry close and only draw management fees on the new fund once Fund III is fully invested, which is anticipated to occur in the first few months of 2017. The GP and affiliates will be committing at least \$15 million of total commitments to the Fund.

Incline believes that the lower middle market will offer attractive investment opportunities because it is a less efficient market than the M&A markets for larger companies. Companies within this market segment tend to be more receptive to the operational focus and strategic discipline brought by Incline’s active portfolio management approach, which can result in meaningful improvements in company performance. Incline’s active portfolio management approach is based on company-specific value-creation strategies which include: (i) identifying areas for operational improvement, (ii) completing strategic acquisitions and (iii) augmenting a company’s management team and board of directors when appropriate.

Fund IV will focus on investments in the four Core Business Models (route-based distribution, customer-based distribution, outsourced services and specialized light manufacturing) that operate within three Core Business Sectors (value-added distribution, outsourced services and specialized light manufacturing) where the Principals have considerable prior investment experience. Incline prefers these business models because they are often characterized by opportunities to achieve economies of density, strong barriers to entry, healthy recurring cash flows, loyal and diverse customer bases, high operating margins and stable market share dynamics. By honing in on these core business models, Incline believes that it will be able to quickly



and more thoroughly diligence and execute on these investment opportunities. Incline does not expect to pursue investment opportunities that fall outside of these Core Business Models, but it may pursue such investment opportunities on a select basis if they otherwise fit Incline's investment criteria.

Portfolio Advisors' recommendation is based upon the following analytical factors and is made within the context of Commonwealth of Pennsylvania Public School Employees' Retirement System's ("PSERS") investment guidelines.

- Detailed due diligence, including interviews with industry peers and private equity professionals. The on-site due diligence visit was performed on August 19, 2016.
- 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 Private Equity Partnership component of the portfolio.

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

Adam Clemens – Managing Director, Darien Office

Lenis Leung – Vice President, Darien Office

Based on the above, Portfolio Advisors recommends that PSERS commit to up to \$100 million in Incline Equity Partners IV, 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