



COMMONWEALTH OF PENNSYLVANIA
PUBLIC SCHOOL EMPLOYEES' RETIREMENT SYSTEM

Public Investment Memorandum

Blue Point Capital Partners IV, L.P.

Private Equity Commitment

Michael Tyler
Portfolio Manager

November 7, 2017



Recommendation:

Staff, together with Hamilton Lane, recommends the Board commit up to \$70 million to Blue Point Capital Partners IV, L.P. ("Blue Point IV" or the "Fund").

Firm Overview:

Blue Point Capital Partners IV, L.P. is being established by Blue Point Capital Partners, LLC ("Blue Point", or the "Firm"). Blue Point is the General Partner sponsoring this North American focused lower mid-market buyout fund. The current partners of Blue Point have a 19-year history of investing together in primarily control transactions in lower middle-market companies. The Firm has a strong focus on investing in businesses that can benefit from Blue Point's toolkit – over 50% of the prior two funds use at least two of the Firm's three major tools: Asian strategies, data and digital strategies, or mergers & acquisitions. While investing nationwide, the Firm believes strongly in the benefits of investing in its near-home regions, evidenced by the fact that over half of deals in the two prior funds are located within driving distance of its offices in Cleveland, Charlotte and Seattle. Frequently, it is the first institutional investor in its investee companies. The Firm is seeking total capital commitments for Blue Point IV of \$600 million. Management (the General Partner and related entities) expect to commit approximately 3-4% of total commitments, with a minimum of 2% coming from the General Partner.

Blue Point is led by Charles "Chip" Chaikin, John LeMay, Julianne "Juli" Marley, Mark Morris and Sean Ward (collectively, the "Partner Group" or the "Partners"). The Firm was founded in 1990 in Cleveland as Society Venture Capital Corporation, later renamed Key Equity Capital, as the private equity investment arm of KeyCorp, a bank holding company. The Partner Group has been together since 1998, when they all worked at the Firm as associates. Blue Point was established as a spin-out from KeyCorp in 2000, and has since raised and managed three successful, independent private equity funds.

The three funds have an aggregate total commitment of over \$1.2 billion. The firm has invested in over 40 platform companies through its vintage 2001, 2007 and 2014 funds.

Fund Size:

Blue Point IV is seeking equity commitments of \$600 million with a hard cap of \$700 million. Initial interest suggests the fund will be oversubscribed, hit the hard cap, and have a first and only close in December 2017.

Investment Strategy:

Blue Point IV will continue the core investment strategy the Firm has executed since 1990. Blue Point IV will focus primarily on sourcing and making control investments in lower middle-market companies located in the Midwest, Southeast and West Coast (collectively, the "Preferred Regions") that generate between approximately \$20 million and \$200 million in revenue and approximately \$5 million and \$25 million in EBITDA. The Firm typically commits between approximately \$25 million and \$50 million of total equity per portfolio company. The Firm believes its longevity and strong franchise within the Preferred Regions provide it with multiple sourcing channels and in some cases, permit access to less competitive transactions. The Firm maintains long-term relationships with business owners and their advisors in each Preferred Region through its expansive network of financial and operating professionals, as well as through its active involvement in the local communities. While the Firm is also a regular investor outside of the Preferred Regions, approximately 52% of the two prior fund's platform investments are located within driving distance of a Blue Point office in Cleveland, Charlotte and Seattle. Partly as a result of the regional focus, nearly 80% of the prior two funds' investments made through March 31, 2017 have not been acquired via an auction, but have been derived from an exclusive or less competitive process. In addition, the regional focus has often allowed the Firm to experience a lengthier, more detailed due diligence process. In certain situations, it has enabled the Firm to invest in businesses that require particularly active management to achieve their strategic objectives, which has been possible given its



proximity to the businesses. Blue Point has been the first institutional partner for its portfolio companies and was the first institutional control investor in 70% of the two prior funds' deals.

The Firm's competitive advantage lies in its highly disciplined and focused value-add process developed over the 27-year life of the Firm. A Value-Add Memo is developed during deal underwriting, to ensure the target has the attributes that are suited to the Firm's core tools and competencies. An institutionalized execution process is monitored and managed continuously to ensure long-term goals are met. While each portfolio company's value add plan is individualized, a substantial portion of EBITDA growth has come through one or more of three principal tools:

1. **Asian Strategies:** Through its Shanghai office and Asian experience, Blue Point provides additional cost reduction and/or revenue-generating opportunities by helping companies execute Asian growth or supply chain initiatives. These initiatives can include creating supply chain teams, establishing production facilities, creating wholly owned foreign enterprises, setting up joint ventures and building relationships with Asian partners. To date, just over half of the prior two funds have used the resources of the Shanghai office. Blue Point maintains full-time resources in its Shanghai office who can provide direct assistance to portfolio companies in hiring, training, and managing a supply chain team.
2. **Data & Digital Strategies:** Improving the way portfolio companies collect, analyze and act on data is an important component of Blue Point's value-add plan. In most cases, this refers to the way companies price their product or service as well as how they manage their inventories and interact with their customers. The Firm believes that greater use of the systems and analytics now available can meaningfully increase margins and revenues, and reduce working capital. In addition to data initiatives, Blue Point has in-house e-commerce and digital marketing expertise and assists its companies in this complex but critical area. Approximately 35% of the prior two funds' companies have executed or are executing data and digital strategies. The Firm believes this offers lower middle-market companies a way to fundamentally distinguish themselves from less sophisticated competitors.
3. **Mergers & Acquisition Strategy:** M&A is also a large part of the value add plan for many investments. Nearly 70% of the prior two fund's portfolio companies have executed add-on acquisitions. The latest fund has executed 16 add-on acquisitions alone – allowing for strategic development, synergies and scale, and often reducing the average entrance purchase multiple for the investment.

In addition to the above, Blue Point actively partners with management to develop other company specific tactical and strategic plans. The Firm makes use of its talented pool of operating partners and outside executives to help drive execution of those plans.

Team:

The Blue Point investment team is comprised of 15 members with an average of 12 years investing experience in the lower middle-market, with diverse backgrounds in finance, operations and consulting. The 5 Partners have worked together for the last 19 years, resulting a combined 105 years of experience in their target market, and experience through varying economic cycles.

Name	Title, Location	Total Yrs. Experience	Prior Experience
Sean Ward	Partner, Cleveland	29	KeyBank, analyst
Mark Morris	Partner, Seattle	24	KeyBank, analyst
Juli Marley	Partner, Charlotte	33	Ernst & Young, sr. manager
Chip Chaikin	Partner, Cleveland, Shanghai	31	Sara Lee Corp, business development; Mercer Mgt., consulting



John LeMay	Partner, Cleveland	30	BCG, consulting; Salomon Brothers, analyst
Dennis Wu	Managing Director, Shanghai	12	Delphi, purchasing director; Shanghai Printronics, product engineering
Brian Castleberry	Principal, Charlotte	13	Red Ventures, VP; HOPE Int'l advisor, analyst
Charley Geiger	Principal, Seattle	13	Duff Phelps, associate; Watson Wyatt, investment consultant
Jeff Robich	Principal, Cleveland	11	Valley Forge PE, director; Societe Generale, analyst
Johnathan Pressnell	Principal, Cleveland	12	Greenbrier Equity, principal; KeyBank, analyst; Ernst & Young, auditor
Jim Marra	Dir. of Business Development, Cleveland	31	Citicorp, various positions
Laurie Kong	Sr. Associate, Shanghai	10	Accenture, IBM, consultant
Rick Soukup	Sr. Associate, Cleveland	7	Incline Equity, analyst
Evan Cottington	Associate, Cleveland	4	Linsalata Capital, KeyBank, analyst
Bobby Grebenc	Associate, Cleveland	2	KeyBank analyst

Investment Instruments:

Parameters for investing will be maintained as in prior funds. Blue Point IV will primarily target buyout opportunities of established businesses with a history of profitability; high operating margins, strong recurring cash flows, moderate customer concentration risk, and limited cyclicality, to which the Blue Point core tool kit can be best applied. Specifically, targeted are those sectors where Asian strategies, data and digital strategies, and M & A strategies are likely to be additive.

Market Opportunity:

Blue Point believes there are ample lower middle-market companies in its Preferred Regions in which private equity penetration is limited. The Firm believes its strong regional franchise will continue to enhance deal flow and reinforce the importance of trusted relationships, allowing for proprietary acquisition of companies on a less competitive basis; this results in conservative price multiples and prudently leveraged balance sheets. There is an abundance of targets where Blue Point and its operating partners have industry-specific expertise, particularly in manufacturing and business services, including engineered products, industrial outsourcing, specialty distribution and environmental services. Within these sectors, there are sufficient numbers of quality companies with the preferred attributes of high operating margins, strong barriers to entry, recurring cash flows, moderate customer concentration and limited cyclicality.

Investment Highlights:

Focus on Core Target Sectors
Since inception, Blue Point has targeted industrial manufacturing and services, consumer (primarily value-add distribution) and business services opportunities, developing significant industry expertise. They seek businesses with high operating margins, significant barriers to entry, strong recurring cash flows, moderate customer concentration and limited cyclicality. Blue Point has maintained offices in Cleveland, Charlotte and Seattle since 1998, providing regional market knowledge and access throughout the Midwest, Southeast and West Coast of the United States.



Partnership Approach in Relation to Lower Middle-Market Businesses

The Firm aims to be the first source of institutional capital and positions itself as a value-additive partner capable of professionalizing businesses through its operational expertise. Blue Point targets control positions but encourages management to roll over equity, incentivizing long-term, sustainable growth of the platform. Working with target companies, Blue Point will pursue a range of investment opportunities, including management-led buyouts, restructurings, recapitalizations, as well as companies seeking internal growth through institutional capital. Blue point will target 60%-90% ownership and at least one board seat for every portfolio company.

Disciplined Approach to Value Creation Drives Operational Improvements

Blue Point leverages three primary value creation levers; consisting of Asian expansion, introduction of data and digital strategies, and strategic add-on acquisitions. Blue Point seeks to maintain purchase price discipline and conservative leverage to provide downside protection and financial flexibility to pursue these strategies.

Strong Performance vs Benchmarks

Blue Point I showed strong MoC and net IRR, and was a strong second quartile performer versus the HL Benchmark for North American Small Cap Buyouts and outperformed the Kaplan and Schoar Public Market Equivalent (PME) Benchmark measured against the Dow Jones Wilshire 5000 index. Under the current second-generation management team, both Funds II and III have been top quartile performers vs the HL Benchmark for North American Small Cap Buyout and outperformed the KS-PME Benchmark.

Performance and Benchmarks

Blue Point Capital Partners, LLC Prior Investment Performance (6/30/17)						Hamilton Lane Benchmark North American Small Cap Buyout (3/31/17)			KS-PME Benchmark vs DJW 5000 ¹ (6/30/17)
Fund	Vintage	% Drawn	DPI	MoC	Net IRR	Spread vs. Top Quartile			Market is 1.00
						DPI	MoC	Net IRR	
Fund I	2000	87%	1.6x	1.6x	11.2%	-0.5x	-0.6x	-179 bps	1.03
Fund II	2006	96%	1.8x	2.2x	18.3%	0.1x	0.5x	+519 bps	1.48
Fund III	2014	58%	0.3x	1.5x	24.7%	0.0x	0.1x	+419 bps	1.19
Total			1.3x	1.8x	14.4%				1.21

¹ KS-PME is the Kaplan and Schoar Public Market Equivalent vs Dow Jones Wilshire 5000 Index

Investment / Risk Considerations:

Investment Pacing and Return Dispersion

Given Blue Point's stated goal of minimizing cyclicity, actual investment pacing has been loosely correlated to economic cycles, for instance peaking in 2007, falling dramatically in 2008, then regaining momentum through 2014 and remaining relatively constant since. While this may be the result of a number of macro and micro economic factors or investing opportunities, there is no escaping the conclusion that investors, particularly those exposed to U.S. light industrial, business service and engineered products sectors, will inevitably be affected by swings in the economic cycle. Blue Point has, however, demonstrated an ability to drive realizations across market cycles. Blue Point's first two funds had over one-third of investments returning less than 0.5%; this has been offset with significant realizations over 3.0X. 37% of Fund I and 59% of Fund II investments to date (6.30.17) have been over 3.0X. Current momentum of the Blue Point team suggests continual improvement of investing and exit execution will continue into the next fund.



Illiquidity
There is little certainty of the timing of distributions. An investment in Blue Point IV should be viewed as an illiquid investment. It is uncertain as to when profits, if any, will be realized. Losses on unsuccessful investments may be realized before gains on successful investments are realized. The return of capital and the realization of gains, if any, generally will occur only upon the partial or complete disposition of an investment. While an investment may be sold at any time, it is generally expected that this will not occur for a number of years after the initial investment. Before such time, there may be no current return on the investment. Furthermore, the expenses of operating the Partnership (including the Management Fee payable to the General Partner) may exceed its income, thereby requiring that the difference be paid from the Partnership's capital, including unfunded commitments. As previously noted, stage of macro economic cycles may affect timing of exits.
Concentration of Investments
Blue Point IV will participate in a limited number of investments and may seek to make several investments in one industry or one industry segment or within a short period. As a result, the portfolio could become more concentrated, and the performance of a few holdings or of a particular industry may substantially affect its aggregate return.
Fund Size Increase
Blue Point's three prior funds ranged in size from \$400 to \$425 in total commitments. Fund IV is targeted at \$600 million with a hard cap at \$700 million, which will likely be met. Larger fund sizes can be a precursor to an increase in target investment sizes, where the GP is now competing against a more competitive environment of larger private equity firms. Evolution away from the core strategies that made the fund successful is a potential risk. Often larger funds have shown inverse relations to performance for a particular manager. Here, Blue Point is targeting the same number of investments as the prior fund, and the same top end for equity check bite size. What is different is the lower end of equity check size is being moved up from \$10 million to \$25 million; this alone can account for most of the increase in fund size, all other factors being equal. The smaller end of the equity check size are now part of the opportunity set for making add-on acquisitions, of which 16 have already been done in Fund III. These add on investments are often all equity investments, adding to the justification for a larger fund size.

PSERS History & Performance:

The table that follows summarizes Blue Point I, II, and III performance with 6.30.17 valuations. All three funds have generated consistent, attractive performance on a net IRR, DPI and MoC basis.

Fund (\$M)	Vintage	Fund Size	Drawn	Distributed	NAV	DPI	MoC	Net IRR
Fund I	2000	\$415	\$360	\$563	\$0	1.6x	1.6x	11.2%
Fund II	2006	401	384	675	187	1.8x	2.2x	18.3%
Fund III	2014	425	247	65	307	0.3x	1.5x	24.7%
Total		\$1,241	\$991	\$1,303	494	1.3x	1.8x	14.4%

Portfolio Fit:

A commitment to Blue Point IV will be allocated to the Private Equity portfolio. An additional commitment to Blue Point IV will allow PSERS to continue its relationship with a high-conviction manager that is well positioned to execute on its investment strategy of making lower mid-market investments in light industrial and business service companies where it feels it has a competitive advantage in deal sourcing and



application of its evolved and proven value-add toolkit. This commitment will sustain lower mid-market exposure in the overall portfolio.

The table below summarizes PSERS' projected exposure inclusive of a recommended \$70 million commitment to the Fund: (6/30/17)

Investment Type	Active Commitments ¹	%	Market Value	%	Unfunded ¹	%	Total Exposure ¹	%
Private Equity	\$ 15,172.4	65.4%	\$ 5,400.4	67.2%	\$ 3,885.1	70.5%	\$ 9,285.5	68.5%
Special Situations	4,754.8	20.5%	1,049.2	13.1%	991.7	18.0%	2,040.9	15.1%
Venture Capital	2,797.0	12.1%	996.1	12.4%	574.8	10.4%	1,570.9	11.6%
PE Internal	465.4	2.0%	592.8	7.4%	61.5	1.1%	654.4	4.8%
Total	\$ 23,189.5	100.0%	\$ 8,038.5	100.0%	\$ 5,513.2	100.0%	\$ 13,551.7	100.0%

(1) As of June 30, 2017. Includes post Q2'2017 pending/closed commitments.

Investment Committee Disclosure:

Relationship with Hamilton Lane:	None Disclosed
Placement Agent:	SixPoint Partners; PSERS will not bear directly or indirectly any placement agent fee or expense, finder's fee or any similar fee or expense regardless of whether a placement agent was used in connection with PSERS or any other investors commitment. In the event any such fees are passed on to PSERS, there will be a dollar-for-dollar offset against management fees or other form of reimbursement until the full amount of fees are offset.
PA Political Contributions:	None Disclosed
PA Impact:	<p>U.S. Drinks, LLC; 1 PA location; 172 employees; \$10.1M payroll; PSERS value \$3.9M. U.S. Drinks is the holding company of The Lion Brewery, Inc. Based in Wilkes-Barre, PA and founded in 1905, Lion is a beverage producer that operates primarily as a contract packager of specialty soft drinks, including healthy, organic, and ethnic beverages, and craft and traditional beers.</p> <p>AWP, Inc.; 4 PA locations, 218 employees, \$3.6M payroll; PSERS value \$4.7M ("AWP") is a leading provider of professional traffic control design and execution services in support of utility infrastructure maintenance and construction activity. Headquartered in Kent, Ohio, AWP is in the process of expanding its Eastern U.S. footprint.</p>
Conflicts:	None Disclosed
First Time Fund With PSERS:	No, PSERS committed \$103.75 M to Fund I; \$100 M to Fund II, and \$60M to Fund III
PSERS AIC Approval:	November 7, 2017

Oversight Responsibility:

Investment Office:	Charles J. Spiller Deputy CIO, Non-Traditional Investments Darren Foreman Senior Portfolio Manager Michael Tyler Portfolio Manager
External Consultant:	Hamilton Lane



Hamilton Lane

October 13, 2017

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

Re: Blue Point Capital Partners IV, L.P.

Dear Trustees:

Blue Point Capital Partners (“Blue Point”) was founded in 1990 as Society Venture Capital Corporation as the private equity arm of KeyBank; the General Partner spun out from KeyBank in 2000 and rebranded itself as Blue Point. Blue Point’s investment team is comprised of 13 investment professionals, including five partners, one managing director, four principals, one senior associate and two associates, with all five partners having been with the firm since inception. All investment professionals are generalists and deal teams are typically led by a partner and supported by one to two additional investment professionals, as well as an operating partner. The General Partner currently maintains four external operating partners on retainer and leverages these resources during its diligence and value creation processes, from the initial screening through its exit. Blue Point is targeting \$600 million in commitments from limited partners for its fourth buyout fund, Blue Point Capital Partners IV, L.P. (the “Fund”). Blue Point expects to hold a first and final close in November or December 2017. The General Partner will commit at least 2% of commitments to invest in or alongside the Fund.

The Fund will target investments in industrial manufacturing and services, consumer and business services companies operating in the lower-middle market. The General Partner’s consistent focus on these target sectors has allowed it to develop deep, industry-specific expertise. Blue Point seeks businesses with high operating margins, significant barriers to entry, strong recurring cash flows, moderate customer concentration risk and limited cyclicity in its “Preferred Regions” of the United States, consisting of the Midwest, Southeast and West Coast. The General Partner aims to be the first source of institutional capital, positioning itself to lower-middle market business owners and operators as a value-additive partner capable of professionalizing and transforming their business. The Fund will employ a disciplined approach to value creation, targeting companies that can benefit from three core value creation levers, (i) Asia expansion, (ii) data and digital strategies and (iii) M&A. Blue Point’s ability to apply its industry expertise and external operating resources to transform lower-middle market businesses into professional enterprises makes the companies attractive targets for both financial sponsors and strategic buyers. The Fund will primarily target equity investments in the range of \$25 million to \$50 million, targeting companies with enterprise values between \$50 million and \$200 million. Blue Point estimates that the Fund will make 12 to 15 investments. Blue Point has generated consistently attractive net returns across prior funds, with top-quartile performance in Funds II and III on a net IRR, DPI, and TVPI basis.

Blue Point Capital Partners IV’s investment thesis can be summarized as follows:

- Blue Point has a senior investment team supported by experienced operating partners
- The General Partner employs a disciplined value creation approach to lower middle-market business



Hamilton Lane

- Blue Point has generated consistent, attractive performance with additional expected upside from the unrealized portfolio

Hamilton Lane's 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 initial review was completed July 18, 2017; the on-site due diligence was conducted September 12, 2017; the fund was approved by Hamilton Lane's Investment Committee on October 2, 2017 and the recommendation to PSERS was issued October 13, 2017.
- 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 Hamilton Lane who were involved in the due diligence process for the Fund are:

Christian Kallen – Managing Director, Bala Cynwyd Office

Jenith Jacob – Associate, Bala Cynwyd Office

Conor Kelly – Analyst, Bala Cynwyd Office

Jacob Fertell – Analyst, Bala Cynwyd Office

Based on the above, Hamilton Lane recommends that PSERS commit up to \$70 million in Blue Point Capital Partners IV, L.P. Hamilton Lane 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. Hamilton Lane does not provide legal or other non-investment-related advice.

Sincerely,

Michael Koenig,
Managing Director

Corina English,
Vice President