

COMMONWEALTH OF PENNSYLVANIA
PUBLIC SCHOOL EMPLOYEES' RETIREMENT SYSTEM

Public Investment Memorandum

Searchlight Capital III, L.P.

Special Situations Commitment

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February 19, 2019



Recommendation:

PSERS Investment Professionals, together with Hamilton Lane, recommends to the Board a commitment of up to \$150 million to Searchlight Capital III, L.P. (“Fund III” or the “Fund”). Searchlight Capital Partners, L.P. (“Searchlight” or the “Firm”) is sponsoring the Fund to make value-oriented investments in private equity and distressed situations across North America and Europe.

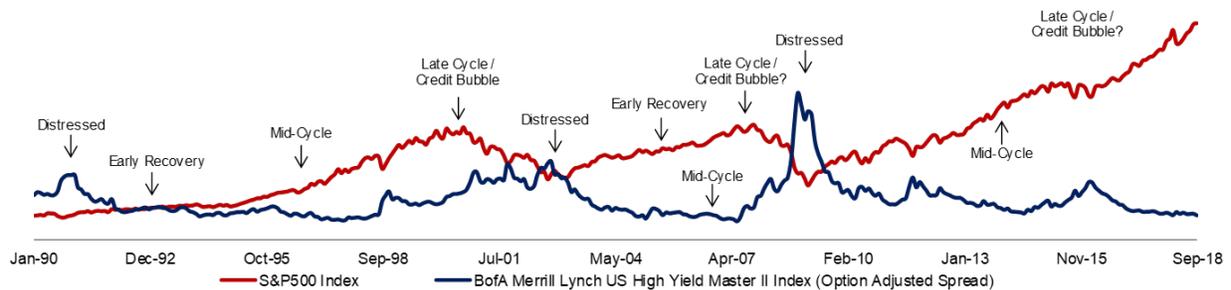
Firm Overview:

Searchlight Capital Partners, L.P. (“Searchlight” or the “Firm”) was founded in 2010 by Oliver Haarmann, Erol Uzumeri and Eric Zinterhofer (the “Founding Partners”) and has a team of 62 professionals (including 32 investment professionals) across the Firm’s three offices in New York, London and Toronto. Searchlight employs a value-oriented investment philosophy which seeks to deliver strong performance during all economic cycles. Searchlight completed the final closing of its first private equity fund, Searchlight Capital, L.P., (“Fund I”) in March 2012 with \$864 million of committed capital, of which \$25 million was committed by the General Partner. Searchlight completed the final closing of its second private equity fund, Searchlight Capital II, L.P. (“Fund II”) in December 2015, with \$1,939 million of committed capital, of which \$39 million was committed by the General Partner (the “Prior Funds”). PSERS previously committed \$74 million to Fund II. Searchlight additionally completed the final closing of the Searchlight Opportunities Fund, L.P. (“SOF”) in April 2018 with \$386 million of committed capital, of which \$15 million was committed by the General Partner.

Searchlight is currently raising its third private equity fund, Searchlight Capital III, L.P., and is seeking aggregate commitments of \$2.75 billion. Searchlight is targeting a first closing for Fund III in April 2019, with the final close expected by mid-2019 and the General Partner will commit at least \$55 million.

Market Opportunity:

Equity and credit markets fluctuate along short-to-medium term cycles, which can present opportunities to shift between private equity and distressed debt investment opportunities. The diagram below indicates that the US is in the late stages of a market cycle and PSERS Investment Professionals believe that low credit spreads and inflated equity markets are unlikely to perpetuate over the long-term. Searchlight’s investment strategy will allow Fund III to optimize its investment strategy according to market conditions.



The ability to invest across a company’s capital structure is critical to Searchlight’s capacity to make investments at attractive values. During times of dislocation, when M&A activity is limited for traditional private equity firms, Searchlight will primarily focus on pursuing distressed opportunities. During periods of recovery, when distressed opportunities are less attractive, Searchlight will primarily focus on pursuing private equity investments. The Firm’s ability to be productive across market cycles allows it to remain selective and disciplined during periods of frothiness, at which point Searchlight will more actively seek to make investments with structural downside protection.

Given historical periods between economic cycles, it is likely that some period of market dislocation will occur during the term of Fund III, as North American and Western European markets are nearly ten years into an expansionary cycle.



Portfolio Fit:

Searchlight's investment strategy will serve to complement PSERS' existing portfolio and a commitment to Fund III will enable PSERS to re-invest with a high-conviction manager. Other firms pursuing a similar investment strategy are generally much larger than Searchlight, and as a result, they typically invest in larger opportunities. A commitment to Fund III will be allocated to the Special Situations bucket of PSERS' Private Markets portfolio.

The table below summarizes PSERS' projected Private Markets exposure inclusive of a recommended \$150 million commitment to Fund III:

Investment Type (\$M)	Market Value	%	Unfunded ¹	%	Total Exposure ¹	%
Private Equity	\$ 5,309.2	64.6%	\$ 3,921.4	71.7%	\$ 9,230.5	67.4%
Special Situations	1,140.2	13.9%	918.0	16.8%	2,058.2	15.0%
Venture Capital	1,130.9	13.8%	562.3	10.3%	1,693.2	12.4%
PE Internal	636.4	7.7%	69.5	1.3%	705.8	5.2%
Total	\$ 8,216.6	100.0%	\$ 5,471.1	100.0%	\$ 13,687.7	100.0%

(1) As of September 30, 2018. Includes post Q3'2018 pending/closed commitments.

Investment Strategy:

Searchlight employs a value-oriented investment philosophy which seeks to deliver strong performance across economic cycles. Consistent with Searchlight's Prior Funds, Fund III will primarily target control positions in middle-market companies located in North America and Western Europe in the consumer discretionary, communication services, information technology, industrials, consumer staples and, opportunistically, education sectors. Searchlight focuses on under-managed businesses held at attractive valuations relative to intrinsic values with multiple levers for value creation, exit optionality and attractive cash flow characteristics. Fund's III's average equity investment is expected to range between \$100 million and \$200 million and it is anticipated that Fund III will complete approximately 15 total investments (three to four new investments per year). The anticipated hold period for each investment is approximately five years.

Investment Structure:

Searchlight prioritizes risk-adjusted returns in its investment approach and will often seek to structure its investments with preferred instruments, or other forms of liquidation preference to minimize downside risk. Fund III will pursue complex transactions including distressed debt purchases, post-reorganization equity purchases, bankruptcy reorganizations followed by debt-for-equity swaps, minority private equity investments, leveraged buyouts, corporate partnerships, public equity purchases, and subordinated debt instruments with equity optionality, each of which was implemented in the Prior Funds.

Searchlight's return thresholds will vary by transaction depending on the deal's risk/reward and other structural considerations (e.g., downside protection through ownership of debt securities). However, in all cases Fund III will look to generate equity-like returns. As a result, underwriting thresholds typically range from 20-30% IRR and 2x-3x MoC. The Fund will not require the use of fund level leverage to achieve target returns. However, Fund III expects to enter into a fund-level credit facility to allow the Fund to bridge capital calls.

The main source of the Fund's returns will typically be a result of investment appreciation; however, dividends may be an important component as well depending on the structure of the Fund's investment. Searchlight typically seeks to structure its investments with an attractive levered free cash flow yield, and also seeks to position its investments to benefit from appreciation through purchasing its investments at attractive valuations, and executing upon post-investment value creation initiatives.



Investment Instruments:

Searchlight will employ its investment strategy via equity or debt securities. As previously mentioned, Fund III will seek to achieve attractive risk-adjusted returns by investing in equity and other structured investments with equity-like governance and return profiles, and distressed debt securities with equity-like returns that will often convert into a controlling equity investment through a restructuring. Searchlight's structured investments often resemble debt or preferred equity instruments with features such as a hard maturity, fixed return, negative control rights, and liquidation preference, but are also designed with equity-like upside potential and governance, with features such as warrants and board representation.

Investment Team:

As discussed above, Searchlight was founded in 2010 by Oliver Haarmann, Erol Uzumeri and Eric Zinterhofer and has a team of 62 professionals. Searchlight's investment team is comprised of 32 investment professionals, made up of the Firm's three Founding Partners, seven Partners, seven Managing Directors, four Principals and eleven Associates. In addition to the Firm's investment professionals, Searchlight has finance, legal, IT and investor relations functions in-house.

Searchlight's IC meets on a weekly basis (and more frequently on an as needed basis) in which all investment professionals participate via video conference. Since Searchlight's inception, there has been an intense focus on defining and following a systematic and thorough investment process. The process is designed to be iterative to encourage frequent discussion of recent updates in order to highlight potential opportunities and issues as soon as possible. Though all Searchlight investment professionals participate in the Investment Committee process, the formal voting members of the Investment Committee for each of the Prior Funds and Fund III consist of the Firm's Founding Partners.

The table below highlights the experience of Searchlight's Founding Partners, Partners, Managing Directors, and Principals:

Name	Role	Yrs. Experience Searchlight / Total	Prior Experience
Oliver Haarmann	Founding Partner	9 / 26	KKR, Dillon Read, Bankers Trust
Erol Uzumeri	Founding Partner	9 / 26	Ontario Teachers', CVC International
Eric Zinterhofer	Founding Partner	9 / 24	Apollo, Morgan Stanley, JP Morgan
Ralf Ackermann*	Partner	1 / 16	Apollo, Goldman Sachs, Greenhill
François Dekker	Partner	7 / 19	Bain Capital, Morgan Stanley
Andrew Frey	Partner	8 / 21	Quadrangle, TPG, Blackstone, Lehman
Darren Glatt	Partner	6 / 18	Apollo, Apax, Cypress Group, Bear Stearns
Tom Hendrick	Partner	2 / 31	SVP, DLJ / Credit Suisse, Citibank, Merrill Lynch
Albert Shin*	Partner, Head of SOF*	2 / 24	SVP, AKS Advisors, Saunders Karp & Megrue, Goldman Sachs
Eric Sondag	Partner	8 / 20	GTCR Golder Rauner, Wasserstein
Timothy Austin	Managing Director	7 / 13	Morgan Stanley, Rothschild
Phil Bacal	Managing Director	6 / 11	Catalyst Capital, Credit Suisse
Steven Colder*	Managing Director	2 / 21	SVP, Ewing Mgmt. Group, Aurora Capital, Bowles Hollowell Conner
Christopher Cruz	Managing Director	8 / 12	Oaktree, UBS
Heber Ramos de Freitas	Managing Director	3 / 13	BC Partners, Terra Firma, Morgan Stanley
Adam Reiss	Managing Director	8 / 11	Silver Lake Partners, Goldman Sachs
Nicoló Zanotto	Managing Director	6 / 13	Gladstone Capital Mgmt., Providence Equity, Morgan Stanley
Qais Hammad	Principal	3 / 8	Providence Equity, Citigroup
Grant Johnston	Principal	1 / 5	Hellman & Friedman, Morgan Stanley
Jonathan Laloum	Principal	4 / 8	Deutsche Bank
Meghan Roach	Principal	5 / 12	Ontario Teachers', KPMG
Prateek Puri*	Principal	1 / 5	Blantyre Capital, Champ Private Equity, Booz & Company
Michele Scheggia	Principal	3 / 5	Morgan Stanley

* Indicates professionals dedicated to the Searchlight Opportunities Fund ("SOF").



Investment Highlights:

- Stable & Experienced Senior Investment Team
- Flexible, Value-Oriented Investment Strategy
- Fund II – Strong Performance to Date
- Economic
- Sector Specialization
- Proprietary Sourcing

Investment / Risk Considerations:

- Searchlight's Distressed Investment Experience
- Fund I – Relative Underperformance & Gross/Net Spread
- Increase in Fund Size
- Competition
- Liquidity & Leverage Profile

PSERS History & Performance:

PSERS previously committed \$74 million to Fund II, a 2015 vintage / \$1.94 billion fund. The table below summarizes PSERS' performance in Fund II as September 30, 2018:

<u>Fund (\$M)</u>	<u>Vintage</u>	<u>Commitment</u>	<u>Contributions</u>	<u>Distributions</u>	<u>NAV</u>	<u>Net IRR</u>	<u>Net MoC</u>
Searchlight Capital II, L.P.	2015	\$ 74.0	\$ 37.5	\$ 10.8	\$ 45.0	28.6%	1.49x

Investment Committee Disclosure:

Relationship with Hamilton Lane:	Hamilton Lane has not historically committed discretionary capital to Searchlight. In addition to PSERS, Hamilton Lane is evaluating Fund III on behalf of another advisory client that is pursuing the opportunity and considering a >\$100M commitment to the Fund.
Introduction Source:	Fund Sponsor
Placement Agent:	Searchlight has not engaged a placement agent in soliciting business from PSERS and no placement agent will receive any fees in connection with an investment in the Fund by PSERS. Searchlight has retained Credit Suisse Securities (USA) LLC ("Credit Suisse") as a Placement Agent to assist in the marketing of Fund III primarily to investors in a specific and pre-determined geography outside of the United States. Furthermore, only Limited Partners whose commitments to Fund III are made in connection with the services provided by Credit Suisse will bear the cost of the fee received by Credit Suisse and the costs associated with the engagement of Credit Suisse will be borne by the Fund subject to a 100% offset against the amounts of management fees payable.
PA Political Contributions:	None Disclosed
PA Presence:	Yes
Potential Conflicts:	We are not aware of Searchlight having any investment conflicts.
First Time Fund With PSERS:	No, PSERS committed \$74M to Searchlight Capital II
PSERS Allocation Implementation Committee Approval:	February 18, 2019



Oversight Responsibility:

Investment Office:	Charles J. Spiller Deputy CIO, Non-Traditional Investments James F. Del Gaudio Portfolio Manager Darren C. Foreman Sr. Portfolio Manager
External Consultant:	Hamilton Lane Advisors, L.L.C.



Hamilton Lane

January 25, 2019

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

Re: Searchlight Capital III, L.P.

Dear Trustees:

Searchlight Capital Partners, L.P. ("Searchlight") was founded in 2010 by Oliver Haarmann, Erol Uzumeri and Eric Zinterhofer, who held senior roles at various general partners and limited partners and possess meaningful private equity experience. Searchlight has grown since inception and currently maintains 62 full-time employees, including 32 investment professionals and 30 back-office professionals; the investment team consists of 3 Founding Partners, 7 Partners, 7 Managing Directors, 6 Principals and 9 Associates. Deal teams typically include a Founding Partner, Partner and/or Managing Director, Managing Director and/or Principal and an Associate. Deal team staffing decisions are based on industry expertise and the target company's geographic location, however Searchlight often cross-staffs deals across its three offices, furthering global investment knowledge across the firm. Investment professionals are supported by 6 Senior Advisors, who utilize sector expertise to help assist asset management and implement value creation initiatives at the company-level. Searchlight is targeting \$2.75 billion in commitments for its third turnaround buyout fund, Searchlight Capital III, L.P. (the "Fund"). Searchlight expects to hold a first close in April 2019 and a final close in mid-2019. The General Partner will commit at least 2% of commitments to invest in the Fund.

Consistent with the General Partner's prior funds, the Fund will primarily target middle-market companies located in North America and Western Europe in the consumer discretionary, communication services, information technology, industrials, consumer staples and, opportunistically, education sectors. Searchlight focuses on under-managed businesses held at attractive valuations relative to intrinsic values with multiple levers for value creation and attractive cash flow characteristics. The General Partner uses its in-depth sector knowledge to develop targeted subsectors of focus and adjusts its themes based on the current economic environment. After establishing focused core sector themes, Searchlight sources opportunities by leveraging its network and relationships with intermediaries and management teams prior to an investment, leading to significant direct deal flow. The General Partner primarily targets control positions in order to implement value creation initiatives at portfolio companies. Searchlight will typically seek to enhance value through balance sheet stabilization and company institutionalization. Additionally, the General Partner has generated value organically at portfolio companies by augmenting or replacing management teams and providing strategic guidance. In an effort to pursue downside protection and prioritize risk-adjusted returns in its investment approach, Searchlight will often seek to structure its investments with preferred instruments, or other forms of liquidation preference to minimize downside risk potential. The Fund will target 15 equity investments in the range of \$100 million to \$200 million. The General Partner has been able to generate relatively attractive net performance; Fund II is generating top-quartile returns with additional upside expected in the unrealized portfolio.

Searchlight Capital III's investment thesis can be summarized as follows:

- Experienced investment team led by Founding Partners with continued focus on institutionalization
- Value-oriented investment approach allows flexibility across market cycles



Hamilton Lane

- The General Partner has generally achieved attractive risk-adjusted performance with a strong focus on downside protection

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 September 24, 2018; the on-site due diligence was conducted December 14, 2018; the Fund was approved by Hamilton Lane's Investment Committee on January 22, 2019 and the recommendation to PSERS was issued January 25, 2019
- 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
- Detailed operational due diligence, including interviews with Searchlight's back office team to review the controls and processes surrounding the firm's finance, fund administration, tax, legal, compliance, IT, HR, and accounting functions
- 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 Markets – Special Situations 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

Jeff Sowden – Analyst, Bala Cynwyd Office

Daniel Demchick – Analyst, Bala Cynwyd Office

Based on the above, Hamilton Lane recommends that PSERS commit up to \$150 million in Searchlight Capital III, 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,
Chief Client Officer

Corina English,
Principal