Special Meeting April 11, 2018

POLICE AND FIREFIGHTERS' PENSION BOARD
SPECIAL BOARD MEETING
888 South Andrews Avenue, Suite 202
Fort Lauderdale, FL 33316
Wednesday, April 11, 2018, 9:00 A.M.

Board Members

Ken Rudominer, Chair	P
Richard Fortunato, Vice Chair	P
Scott Bayne, Secretary	P
Jim Naugle, Trustee	P
Jeff Cameron, Trustee	P
Dennis Hole, Trustee	P
Derek Joseph, Trustee	P
Lynn Wenguer, Executive Director	P

Also Present
Alexandra Goyes, Deputy Director
Fred Nesbitt, Board Communication Director
Robert Klausner, Board Attorney
Kevin Schmid, CAPTRUST
Paul DeBold, Retirees Association President
James Egan, Stone Ridge Asset Management
Paul Germain, Stone Ridge Asset Management
Patrick McCauley, Capital Dynamics
Tom Hall, Capital Dynamics
Gena Cheng, USAA
Ben Christian, USAA
Tim Hyland, Boyd Watterson
John Frady, Boyd Watterson
Brian Convey, Boyd Watterson
Jamie Opperlee, Prototype Inc.

ROLL CALL/CALL TO ORDER
The meeting was called to order at 9:00 a.m. A quorum was present.

FIXED INCOME ALTERNATIVES

Alternative Lending/Private Credit:

Stone Ridge Paul Germain, James Egan

Mr. Germain said all loans in the portfolio were prime, indexed, high-yielding and low duration. There were approximately 200,000 loans in the portfolio from several developed markets.

Mr. Germain descried the difference between traditional lenders and alternative lenders and said alternative lenders' costs were 70% lower than traditional costs due to technology. They used partner platforms, instead of traditional banks, to make the process more efficient. He stated they concentrated on consumers, ex-students and small businesses.

Mr. Germain explained that compared to bonds, their yields were higher and duration much lower.

Mr. Germain informed Chair Rudominer that there was no rating system for these types of loans but they considered them to be "A-" rated.

Mr. Germain stated for the last 12 months, the performance of the fund had been 6.47%.

Mr. Germain explained how their underwriting and loan process worked and said they only approved 5% of the small business loan applications. He stated they received a daily mark to a model developed by Duff and Phelps on the entire portfolio.

Mr. Egan stated banks were not making these types of loans anymore. He described how they had selected the 10 alternative lending platforms they used. Mr. Egan explained that these platforms were not banks; they were facilitating transfers of capital. He said banks were funding some of the loans but not originating and servicing them because the platforms were so much more efficient at it. Mr. Germain said they thought of the platforms as finance companies that utilized technology to enhance efficiency.

Mr. Egan said the platforms were responsible for underwriting and Stone Mountain LENDEX bought the loans outright from the platforms.

Mr. Egan descried two of the platforms' performances since 2006 and compared them with bank loan performances.

Mr. Germain said the key issue to watch was unemployment; this was the best predictor of repayment rates.

Mr. Schmid asked about income distributions and Mr. Germain stated they distributed all of the income quarterly.

Mr. Schmid explained they were permitted to make this kind of alternative investment as a fixed income replacement.

Mr. Klausner asked the legal structure for an investor and Mr. Egan stated they were buying shares of a mutual fund.

Mr. Hole asked if any of the platforms had gone down. Mr. Germain explained that they were required to have a back-up servicer in the event the primary servicer was not performing.

Mr. Schmid reminded the Board that the drawback of something so liquid was that returns were not as good. The fee for this fund was 1.5%

Mr. Klausner asked how dependent Stone Ridge was on the financial engineering from Beijing and Mr. Schmid explained this was how they evaluated the risks in the portfolio. He said this evaluation was helpful but was not the primary engine.

Mr. Schmid said $15 million was the stated minimum commitment but he believed there was some flexibility.

Patrick McCauley, Tom Hall

Capital Dynamics-Private Credit Fund

Mr. McCauley said this fund was managed by a senior team with an excellent track record of a 15.5% return after fees. They managed $15 billion across a wide range of mostly institutional clients. They were focused on the middle market, which outperformed large-cap in private markets. They used specialized teams to run each strategy. Mr. Hall described their team and their backgrounds.

Mr. McCauley stated private credit was attractive for three reasons: higher yields; downside protection and Inflation protection. He explained that they made loans only to smaller companies that were owned by private equity firms, which managed the companies and helped protect against things going wrong. Mr. McCauley said in the event of default, they would get paid first or take the company's equipment and/or real estate to cover the loan.

Mr. Hall explained that their loans were fully secured and had a very low default rate of 3%.

Mr. McCauley said the companies they lent to were not big enough to access the bond market; they had to use private lenders and were charged higher yields. These were floating rate loans, which provided inflation protection and rising rates.

Mr. Hall stated their target - the middle market - included over 200,000 businesses and 50 million jobs. Private equity firms currently had approximately $1 trillion of capital looking for acquisitions over the next few years.

Mr. Hall said with their relationships and experience from Credit Suisse, they took the lead in sourcing, pricing, structuring and documenting the loans, which allowed them to increase the returns by up to 2.5%.

Mr. Hall stated they gained an operating advantage by being on the Capital Dynamics platform, because Capital Dynamics had relationships with over 250 private equity sponsors, allowing them to be selective. Capital Dynamics also had a technological advantage that allowed them to screen faster and perform underwriting and diligence faster.

Mr. Hole asked if they ever had conflicts of interest and Mr. Hall explained that they had a co-investment business that invested directly in the businesses and they had a fund-to-fund business that invested in the private equity funds. They would not lend alongside the co-investment business, even though they were not controlling the company, because there was an implied conflict.

Mr. Hall said diversification was very important and they diversified across borrowers, industries and sponsors. He said their process provided transparency and checks and balances throughout the process.

Mr. Klausner asked the structure of the fund and Mr. McCauley said it was a Delaware vehicle.

Mr. Klausner asked about the SEC enforcement issue on the Renewable Energy Infrastructure Team from Capital Dynamics and Mr. McCauley explained that they had self-reported and the SEC had investigated. Ultimately, they had not been found guilty and had been fined $275,000. That issue had nothing to do with this fund.

Mr. Klausner asked the relationship between the broker/dealer and this partnership and Mr. McCauley stated their broker/dealer provided an extra level of regulatory oversight and allowed them to construct compensation that closely aligned with performance. The broker/dealer was the distributer for the funds. There were no additional fees associated with the broker/dealer.

Mr. McCauley said they wanted to raise $400 million for this fund and the first closing would be mid to late summer. Their target of net returns was 10-12%. It was a seven-year fund but they expected to have the money back in five to six years. The management fee was 1.25% plus 15% carried interest after investors received a 7% return.

Mr. McCauley stated they were offering investors a 10% fee discount to come into the first close for this fund. Investors making a $25 million commitment would be given an additional 10% discount and Investors making a $50 million commitment would be given another 10% discount. This would result in a fee of 88 basis points.

Mr. Schmid asked how they performed risk control after the loans were made and Mr. Hall said this was accomplished by their software system and their reporting and management contacts they maintained with borrowers. Borrowers provided monthly reports and they were in constant contact with sponsors and the management teams. The team's backgrounds in distressed investing prepared them for when they were forced to be responsible for a business that defaulted.

Mr. Schmid and Mr. Klausner discuss differences between Stone Ridge and Capital Dynamics: Stone Ridge was more liquid, with Capital Dynamics, once they were in, they would not be able to transfer shares to anyone else. Their fee structures were very different: with Capital Dynamic, they would pay less in a management fee but the back-end fee would affect the long-term rate of return. Mr. Klausner said the most important question for the Board was whether they wanted to tie up the money. Mr. Bayne recalled that part of the Board's thought process involved the knowledge that this would be illiquid.

Mr. Schmid added that with Stone Ridge, they would put in $25 million and begin earning income from day one. With Capital Dynamics, it could take three years to get $25 million invested.

Mr. Klausner noted that with Capital Dynamics, the Board would have very strong bargaining power on the documents. Capital Dynamics would probably provide a side letter giving the Board whatever they wanted. Mr. Schmid said he had worked with Capital Dynamics before and their practice was to compile a document with all side letters from all investors and provide the opportunity to opt in or out to each. Mr. Klausner wanted the responsible party to understand that they were a fiduciary to the Board. He wanted them to follow an ERISA standard of care and to agree they were bound by Florida law, which would provide significant protections.

Government Real Estate:

USAA Gena Cheng, Ben Christian

Ms. Cheng said the company started as an insurance co-op for military service people and their families. She stated they conducted their business with service, loyalty, honesty and integrity. The real estate company was a subsidiary started in 1982 and had $20 billion in assets under management. Of that, half was their own capital. Their products ranged from core funds, value-added investing, equity and debt, all in the private markets.

Ms. Cheng said they had outperformed the NPI for the last ten years. Even during the financial crisis, they had outperformed the NPI and there had been no defaults.

Mr. Christian stated the Government Building Fund was a consistent performer. Their return target was currently 5.5-6% net. He explained that the fund was stable because it lacked volatility; the leases were supported by long-term, fixed-rate debt.

Mr. Christian said they were focused on buying and providing build-to-suit capital for Class A office buildings that were leased to federal agencies. Their strategy was tailor made to meet the government's needs.

Mr. Christian explained they purchased buildings that were not highly specialized; they could be utilized by the private sector. Their lease structure helped manage volatility. Mr. Christian said this fund was a leader in sustainability. They were always in the top 20% of the Global Real Estate Sustainability Benchmark for real assets (GRESB) ranking.

Mr. Christian said they currently had 10 assets, 4.5 million square feet, and $2.2 billion under management. Half were acquisitions and half were build-to-suit. The assets were "somewhat D.C.-centric." Ms. Cheng informed the Board that they focused on leasing only to agencies that provided essential services.

Mr. Christian said their returns compared vary favorably to the index. Per the Odyssey Index, they had roughly 2.5 times the returns with half the volatility. He stated the fund was able to ride through turbulent markets.

Mr. Hole asked if build-to-suits got out of hand and Mr. Christian explained that the buildings they worked with would be appropriate for private sector use. If the government made additional customizations, there was a restoration clause to bring the building back to being suitable for the private sector at the end of the lease.

Mr. Hole asked about the cash management fee and Mr. Christian stated the fees were on a cumulative sliding scale.

Mr. Bayne asked if USAA had any Florida properties for the GB fund and Mr. Christian replied there was a DEA office in Weston.

Chair Rudominer asked if USAA ever sold the build-to-suit buildings and Mr. Christian said their strategy was to get through the first term and then consider selling. He said with a 15-year lease, they typically had four years to determine whether they wanted sell or keep the property with the remaining 10-year lease term intact.

Ms. Wenguer asked if the call would be all at once and Mr. Christian explained it would probably be over a period of time, over the next four to six quarters.

Boyd Watterson Tim Hyland, John Frady, Brian Convery

Mr. Convery stated they had $8 billion in assets under management with $2.3 billion in real estate. The GSA Fund had returned double digits each year and on a cash flow basis, returned 8.5% net. They had just launched the State Fund this year.

Mr. Convery described their team and investors, which included the international Association of Firefighters and the Erie County Pennsylvania Police and Fire Department.

Mr. Convery explained that the federal government owned half of their buildings and leased the other half. The leased half represented 200 million square feet, most of which was concentrated in 24 states.

Mr. Convery stated their return objective for the GSA strategy was 7-9% net income return and the State strategy was a little higher.

In the GSA strategy, Mr. Convery stated they looked for mission critical buildings, and those with a high degree of customization to ensure a long tenancy cash flow. Within the GSA strategy, they had 99 buildings, diversified by geography and agency, including seven buildings in Florida.

Mr. Convery said the State fund would be structured and managed very similar to that of the GSA strategy. They would stagger the leases and debt leverage would be from 40%-50%. Mr. Convery explained they focused on agencies they believed would grow and were important to the federal government, such as Homeland Security and the Department of Defense.

Mr. Convery stated they would only invest in state with a credit rating of “AA-“ or better and had created their own credit model to evaluate states, based on demographics and debt.

Mr. Klausner asked the ratio for states to own or lease properties. Mr. Convery replied most states had a ratio of approximately 80% owned to 20% leased, but this varied significantly by location. Washington, Texas, Florida and California had a higher ratio of leases.

Mr. Convery said they looked for newer, build-to-suit buildings that had renewal rates in the high 90s and long-term leases.

Mr. Frady explained they anticipated a return of 8.8% from the State Fund, 8.3% from the GSA Fund. He noted the average core fund return was approximately 4%. He compared the risk return ratio of their funds to other types of asset classes and said there was no other investment that would create this type of cash yield without being much more risky.

Mr. Nesbitt noticed that a lot of the investments were in law enforcement and asked if they ever invested in police stations. Mr. Convery stated they had invested in a few police stations in the State Fund; in the GSA Fund, they had DEA, FBI and Immigration and Customs Enforcement buildings. If a city had credit of “AA-“ or better, they would consider a police station there.

Mr. Nesbitt recalled that Fort Lauderdale had been seeking a Public/Private Partnership to build a new police station but had been told that no one would build it because it was too specialized. Mr. Convery said this was viable, with the right developer. Mr. Hyland said they would be willing to discuss this with the City.

There being no further business to come before the Board at this time, the meeting was adjourned at 12:53 p.m.

Secretary	Chairman

Any written public comments made 48 hours prior to the meeting regarding items discussed during the proceedings have been attached hereto.

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