



# Fiscal Year 2025 Private Credit Strategic Plan

Santa Barbara County Employees' Retirement System

June 26, 2024



# Table of Contents

	<u>Page</u>
I. Portfolio Review	3
– Portfolio Highlights and Timeline of Events	
– Portfolio and Manager Performance	
II. Private Credit Strategic Plan	11
– Fiscal Year 2024 Strategic Plan Update	
– Pacing Plan	
– Fiscal Year 2025 Strategic Plan	
III. Private Credit Fund Pipeline	19
IV. Appendix	21

# SBCERS Private Credit Portfolio Review

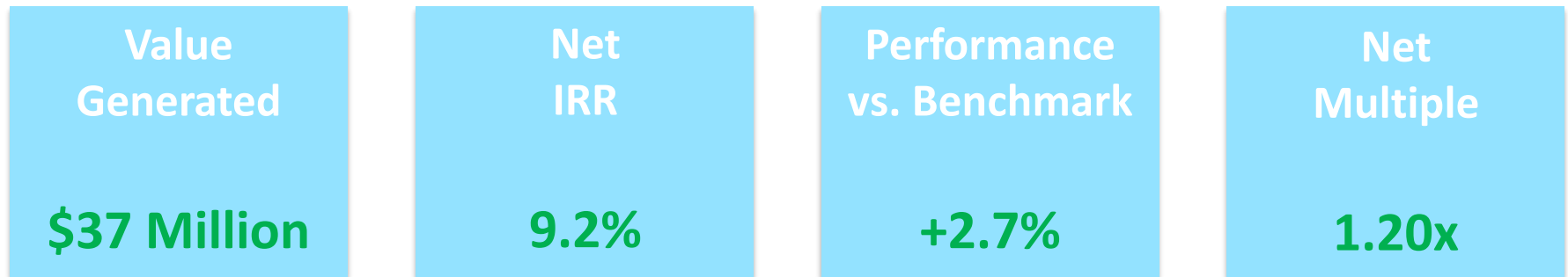




# SBCERS Private Credit Portfolio Highlights

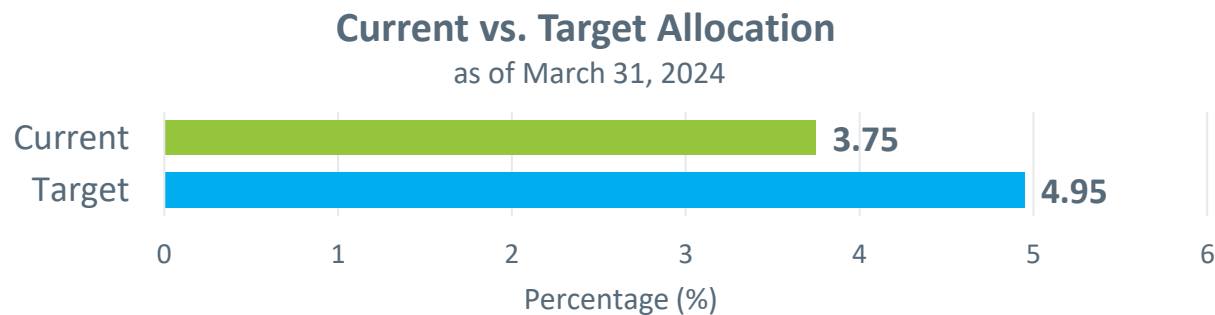
SBCERS is in the 7<sup>th</sup> year of building the Private Credit Portfolio.

## Performance Highlights Since Inception in 2018



## Strategic Objective

- RVK aims to assist SBCERS in establishing a diversified Private Credit Portfolio. The Portfolio has a strong foundation of high-quality managers.
- The Private Credit Portfolio is on pace to achieve the target allocation by late 2027.



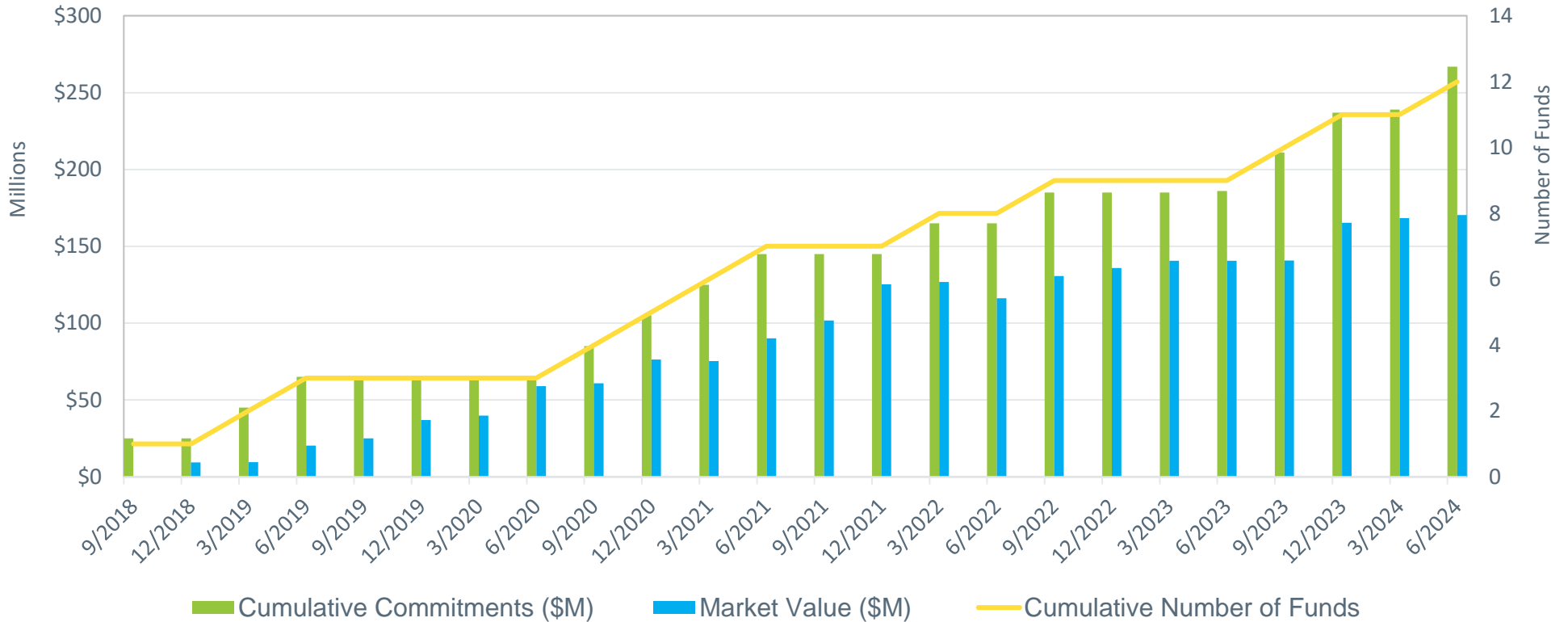
Performance is as of 3/31/2024 and has been calculated by RVK. IRR is the annualized since-inception net internal rate of return. Multiple is the since inception sum of distributions and valuation divided by paid-in capital.

# SBCERS Private Credit Portfolio Timeline of Events

Date	SBCERS Private Credit Portfolio Event
September 2016	The current asset allocation is initially approved, including an 11% allocation to Non-Core Fixed Income
February 2017	RVK reviews a structure analysis, comparing potential sub-asset class structures within Non-Core Fixed Income
March 2018	The Board approved a Non-Core Fixed Income structure of 33% EMD, 33% Bank Loans, 33% Private Credit
July 2018	\$25 million commitment to <b>AG Direct Lending Fund III</b> (first private credit investment)
February 2019	\$20 million commitment to <b>First Eagle Direct Lending Fund IV</b> (previously called THL Credit Direct Lending)
April 2019	\$20 million commitment to <b>PIMCO Private Income Fund</b> (first evergreen fund)
October 2019	The current asset allocation is reconfirmed (initially approved in September 2016)
July 2020	\$20 million commitment to <b>Deerpath Capital V</b>
December 2020	\$20 million re-up commitment to <b>AG Direct Lending Fund IV</b> (first private credit re-up)
February 2021	\$20 million re-up commitment to <b>First Eagle Direct Lending Fund V</b>
June 2021	\$20 million re-up commitment to <b>Deerpath Capital VI</b>
September 2021	Private Credit Portfolio Investment Guidelines added to the SBCERS Investment Policy Statement
June 2022	\$20 million commitment to <b>AG Direct Lending Evergreen Fund</b>
August 2022	The Board approved a Non-Core Fixed Income structure of 25% EMD, 30% Bank Loans, 45% Private Credit
September 2022	\$20 million commitment to <b>Ares Pathfinder Core Fund</b>
September 2023	\$25 million commitment to <b>Marathon Dislocation Credit Fund II</b>
October 2023	\$25 million commitment to <b>KKR US Direct Lending Evergreen Fund</b>
May 2024	\$27.5 million commitment to <b>Pantheon Credit Opportunities III</b>

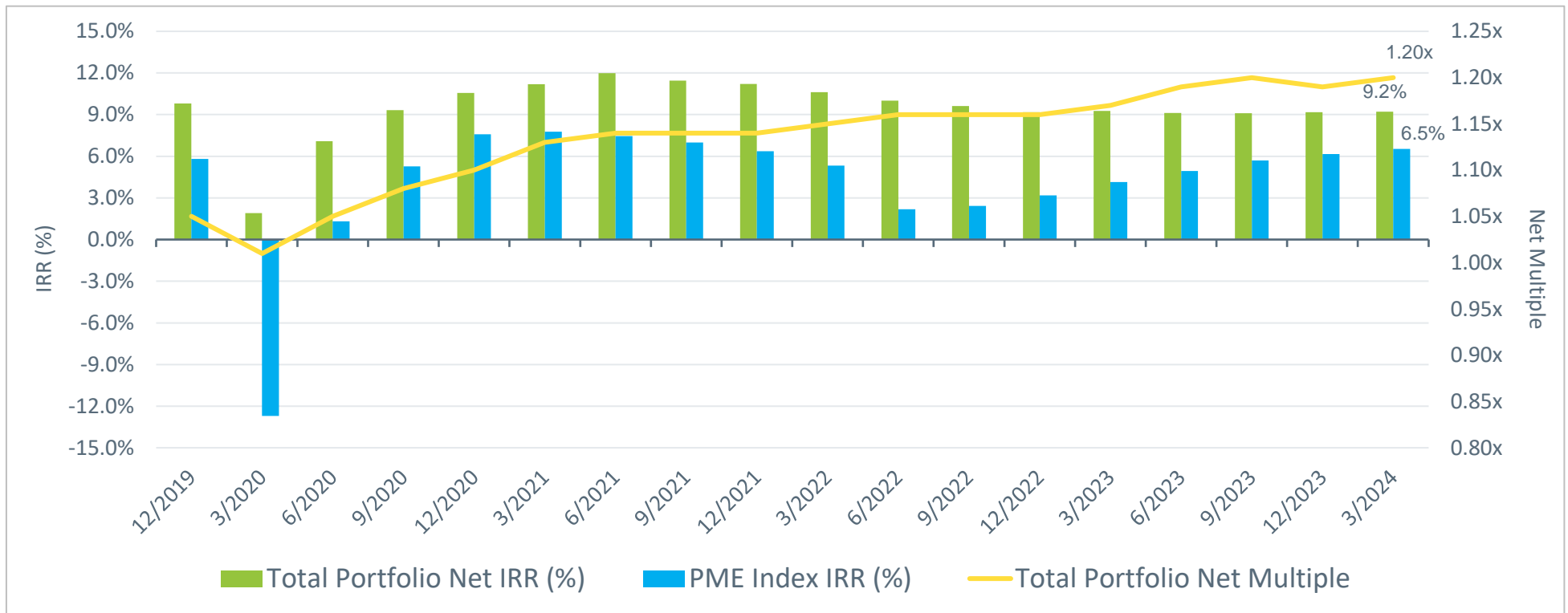
# SBCERS Private Credit Activity

SBCERS Private Credit Portfolio Growth



- SBCERS has committed \$267 million to 12 funds across eight managers since the Private Credit Program was launched in 2018.
- Individual vintage year commitments have been approximately \$40-\$50 million, in-line with the initially recommended annual pacing as the private credit portfolio ramps to the target allocation.

# Private Credit Portfolio Performance (As of 3/31/2024)



- The Portfolio's since inception net IRR of 9.2% outperformed the Credit Suisse Leveraged Loan Index (PME Index) by **2.7%**.
- The Portfolio's since inception net multiple of 1.20x is within our expectations.

Performance is as of 3/31/2024 and has been calculated by RVK. PME Index IRR represents the IRR calculated using the Credit Suisse Leveraged Loan Index, assuming an index investment with the same cash flow timing.

# Private Credit Manager Performance (As of 3/31/2024)

Fund	Vintage	Strategy Type	Vehicle Type	Leverage	Net IRR	PME Index IRR	IRR Quartile
AG Direct Lending Fund III	2018	Direct Lending (LMM)	Drawdown	Yes	9.98%	5.11%	2 <sup>nd</sup>
First Eagle (THL) Direct Lending Fund IV	2019	Direct Lending (LMM)	Drawdown	No	7.06%	6.19%	3 <sup>rd</sup>
PIMCO Private Income Fund	2019	Multi-Strategy	Evergreen	Yes	8.91%	7.28%	3 <sup>rd</sup>
Deerpath Capital V	2020	Direct Lending (LMM)	Drawdown	No	8.41%	6.47%	3 <sup>rd</sup>
AG Direct Lending Fund IV	2020	Direct Lending (M/LMM)	Drawdown	Yes	12.66%	6.10%	2 <sup>nd</sup>
First Eagle (THL) Direct Lending Fund V	2021	Direct Lending (LMM)	Drawdown	Yes	9.45%	6.72%	3 <sup>rd</sup>
Deerpath Capital VI	2021	Direct Lending (LMM)	Drawdown	No	8.77%	6.71%	3 <sup>rd</sup>
AG Direct Lending Evergreen Fund	2022	Direct Lending (M/LMM)	Evergreen	Yes	6.57%	11.37%	4 <sup>th</sup>
Ares Pathfinder Core	2022	Asset Backed	Evergreen	No	N/M	N/M	N/M
Marathon Dislocation Credit Fund II	2023	Distressed	Drawdown	No	N/M	N/M	N/M
KKR US Direct Lending Evergreen Fund	2023	Direct Lending (UMM)	Evergreen	No	N/M	N/M	N/M
Pantheon Credit Opportunities III	2024	Multi-Strategy	Drawdown	No	N/M	N/M	N/M
<b>Total Portfolio</b>					9.23%	6.52%	

Peer group data provided by Preqin. Each direct lending fund has been compared against the Private Debt - Direct Lending peer group and uses the most up-to-date data as of 06/2024. PIMCO Private Income Fund is compared against the broader Private Debt peer group and uses the most up-to-date data as of 06/2024. Peer groups contain both levered and unlevered strategies.

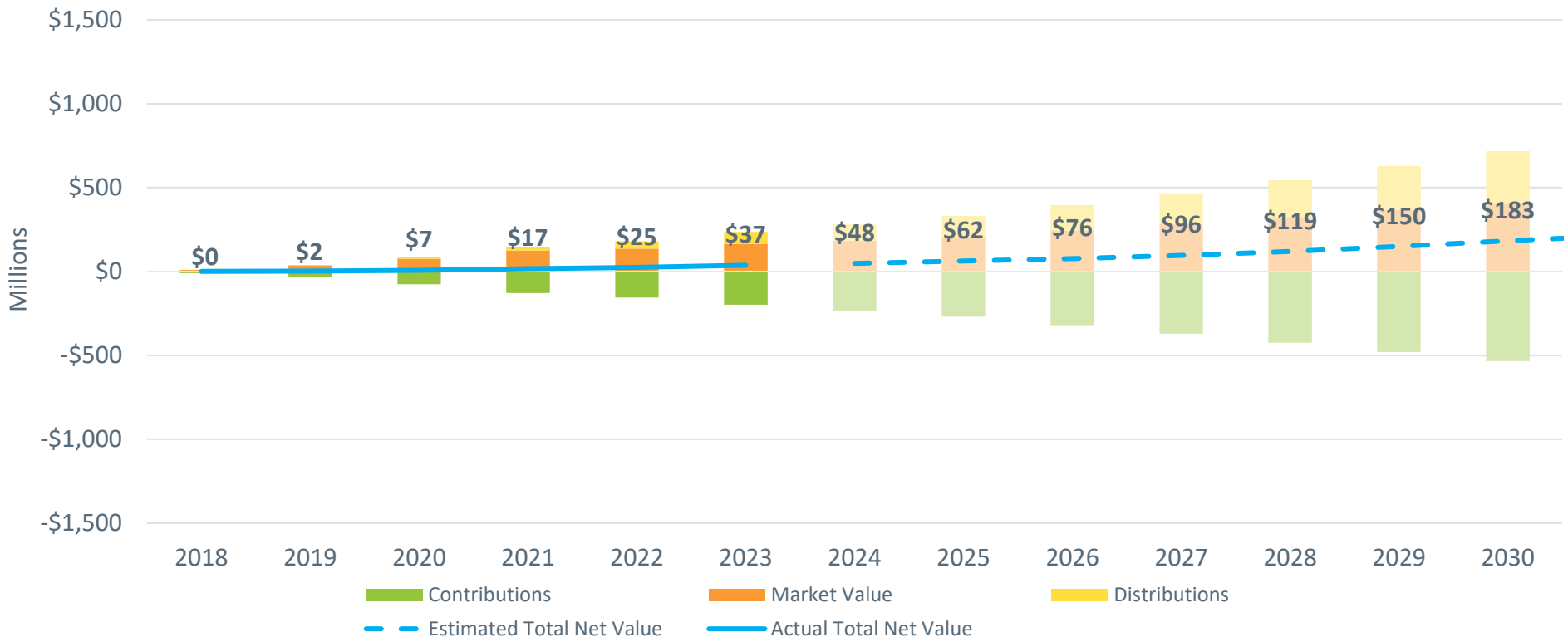
- **Direct Lending** – loans to private companies backed by future cash flows
  - Lower Middle Market (LMM) – Companies with \$5m to \$35m of EBITDA
  - Middle Market (MM) – Companies with \$35m to \$100m of EBITDA
  - Upper Middle Market (UMM) – Companies with EBITDA greater than \$100m
- **Multi-Strategy** – Exposure across private credit sub-sectors (direct lending, real estate debt, asset backed, specialty finance, etc.).
- **Asset Backed** – loans to private companies secured by specific collateral pools (loans and mortgages, receivables financing, long-term and short-term leases, intellectual property, etc.).
- **Distressed** – loans to companies that have either defaulted, is under bankruptcy protection, or is in some other type of financial distress that requires outside capital.



# Private Credit Portfolio Value Creation Analysis

- The Private Credit Portfolio generated \$37 million in value since it was launched in 2018.
- Including new commitments, the value of the Private Credit Portfolio is expected to increase over time as existing investments mature and additional capital is contributed to the Portfolio.
- RVK estimates the Private Credit Portfolio will have created approximately \$183 million in total net value by 2030.

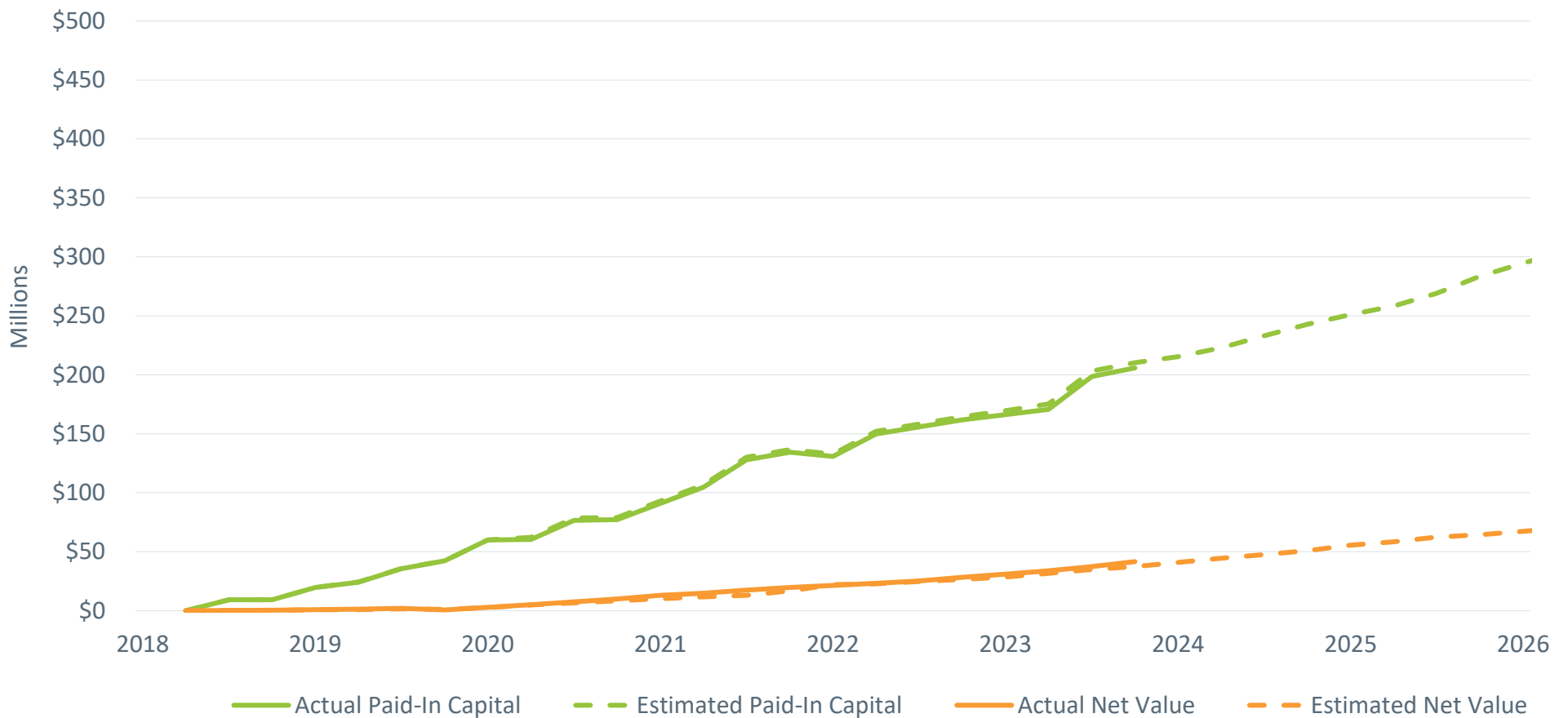
**Total Net Value**



# Paid-in-Capital vs Value Creation

- The Private Credit Portfolio has generated \$37 million in value with \$205 million in paid-in capital since the portfolio's inception in 2018.

## Estimated versus Actual - Paid-In Capital



# SBCERS Private Credit Strategic Plan



# Strategic Plan Summary

- The **Strategic Plan** is a near-term investment strategy designed to achieve the long-term investment objectives of the SBCERS Private Credit Portfolio.
- RVK is working with the SBCERS staff to maintain the annual Fiscal Year Strategic Plan. SBCERS' preferences around Portfolio administration, diversification, and views on different market segments have been implemented accordingly.
- SBCERS Private Credit Portfolio long-term objectives:
  1. Augment the long-term risk-adjusted returns of SBCERS' Non-Core Fixed Income.
  2. Deliver a robust and consistent level of return, primarily from the income generated by its underlying investments.
  3. Provide diversification to SBCERS' overall investment program.

# Fiscal Year 2024 Strategic Plan Update

## Review of themes and objectives identified for Fiscal Year 2024

### Manager Relationships

- Build a new relationship with at least one additional private credit investment manager to maintain manager diversification.

### Pacing Plan

- Commit \$55 million between two private credit funds in order to reach the target allocation by approximately late 2027.

### Strategic Exposure

- Consider commitments to new or lesser allocated sub-strategies such as distressed, specialty finance, or asset-backed debt to achieve sub-strategy diversification.

### Status



- Committed to KKR US Direct Lending Evergreen Fund and Marathon Dislocation Credit Fund II



- Consistently committed to two funds annually since the Portfolio's inception



- Committed to a distressed fund in Marathon Dislocation Credit Fund II



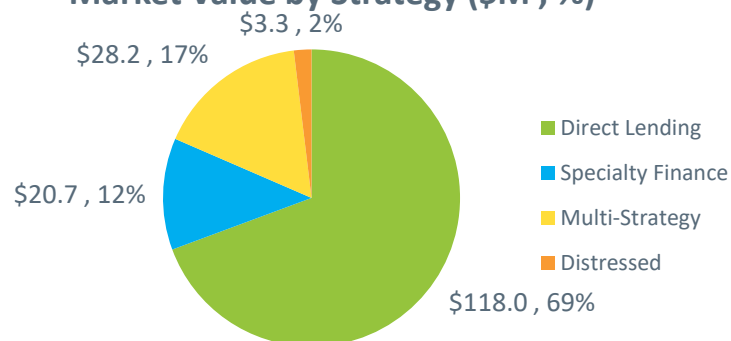
# Private Credit Portfolio Summary

Strategic Plan:  
Manager Relationships

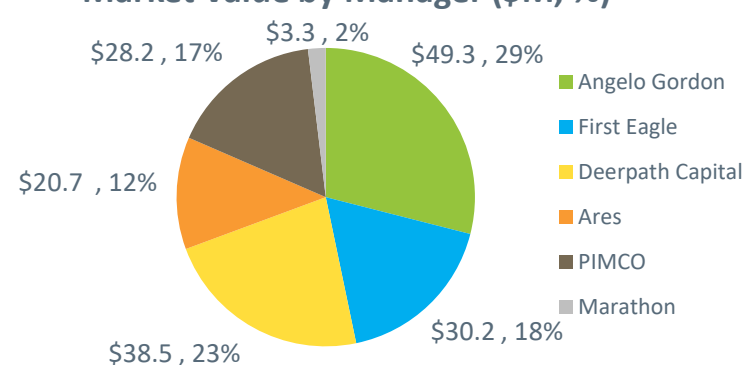
- The Private Credit Portfolio will remain diversified across several managers, as no more than 35% of commitments may be allocated to a single investment manager, as outlined in the IPS.

Fund	Vintage	Commitment (\$M)	Unfunded Commitment (\$M)	Market Value (\$M)	Market Value Allocation (%)
AG Direct Lending Fund III	2018	\$25	\$2.0	\$14.5	8.5%
First Eagle (THL) Direct Lending Fund IV	2019	\$20	\$6.6	\$12.3	7.2%
PIMCO Private Income Fund	2019	\$20	\$0.0	\$28.2	16.6%
Deerpath Capital V	2020	\$20	\$0.0	\$20.5	12.1%
AG Direct Lending Fund IV	2020	\$20	\$1.0	\$20.0	11.8%
First Eagle (THL) Direct Lending Fund V	2021	\$20	\$0.3	\$17.9	10.5%
Deerpath Capital VI	2021	\$20	\$5.4	\$18.0	10.6%
AG Direct Lending Evergreen Fund	2022	\$24	\$9.0	\$14.8	8.7%
Ares Pathfinder Core	2022	\$20	\$0.0	\$20.7	12.2%
Marathon Dislocation Credit Fund II	2023	\$25	\$21.8	\$3.3	1.9%
KKR US Direct Lending Evergreen Fund	2023	\$25	\$25.0	\$0.0	0.0%
Pantheon Credit Opportunities III	2024	\$27.5	\$27.5	\$0.0	0.0%
<b>Total Portfolio</b>		<b>\$267</b>	<b>\$98.6</b>	<b>\$170.1</b>	<b>100.0%</b>

Market Value by Strategy (\$M, %)



Market Value by Manager (\$M, %)



# Pacing Recommendation

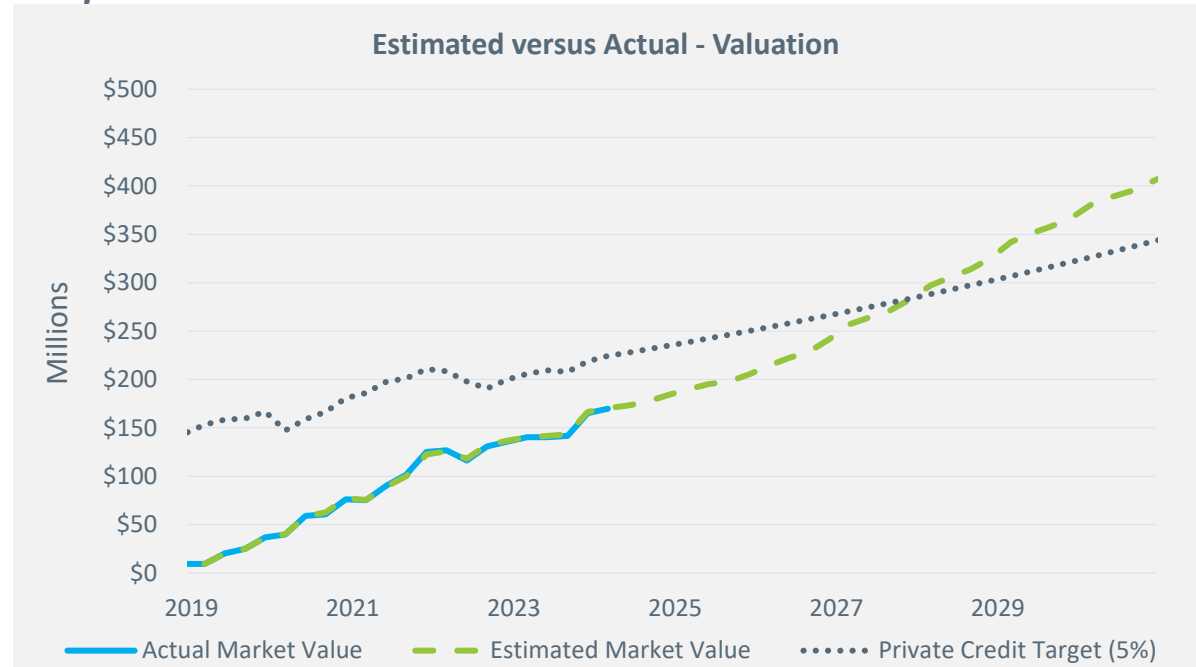
- In Fiscal Year 2024, RVK recommended annual commitments of \$55 million to reach the target allocation.
- After updating our pacing analysis for Fiscal Year 2025, RVK recommends slightly decreasing the annual commitment schedule to \$50 million following Calendar Year 2024.
- The SBCERS' allocation to private credit is expected to reach the target allocation of 4.95% by approximately late 2027.

## Recommendation

Year	Commitments
2024	\$55 million
2025	\$50 million
2026	\$50 million
2027	\$50 million
2028	\$50 million

**RVK recommends annual commitments of \$55 million in 2024, followed by annual commitments of \$50 million to achieve the target allocation by approximately late 2027.**

## Expected Results

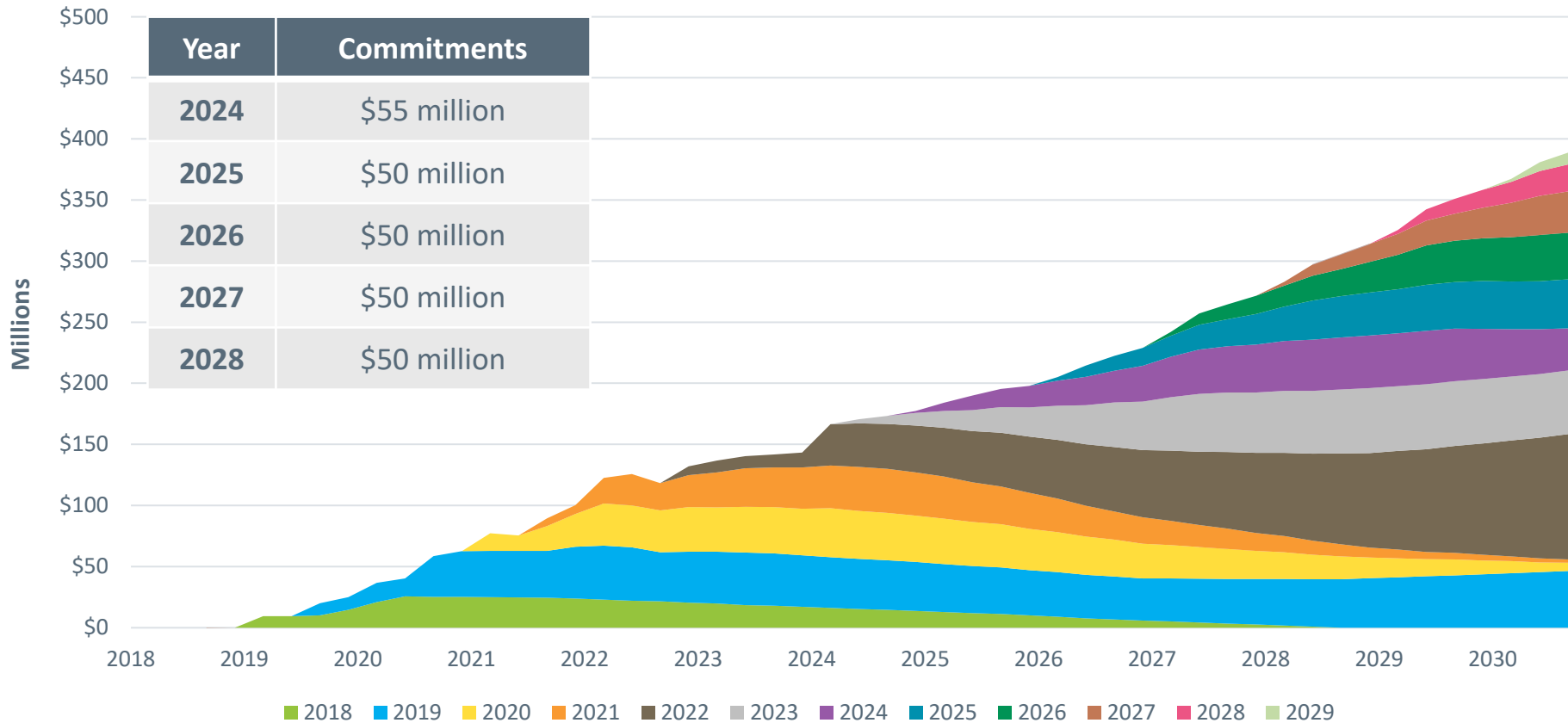


# Pacing and Vintage Year Diversification

**RVK recommends the following commitment schedule, keeping in mind:**

- Vintage year concentration is a risk in private credit
- Annual commitments are likely to represent multiple funds and strategies
- Recommended commitments are approximate
- Attractive private credit opportunities may not present equally each year

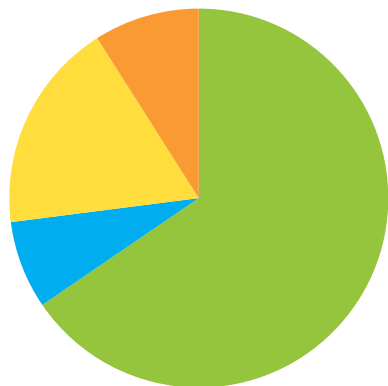
**Estimated Total Valuation by Vintage Year**



# Portfolio Targets

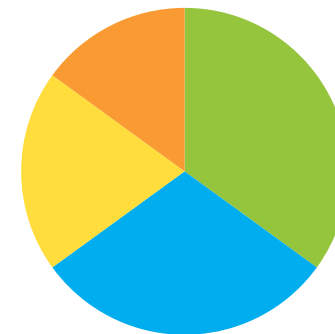
- In the initial buildout of the SBCERS Private Credit Portfolio, an emphasis was placed on strategies operating within senior secured direct lending.
- As addressed in the Private Credit Portfolio Investment Guidelines in the Investment Policy Statement, RVK would like to introduce additional private credit sub-strategies for SBCERS' consideration.
- RVK seeks to assist SBCERS build a Private Credit Portfolio diversified across several different private credit sub-strategies and collateral types.
- In the following illustration, RVK proposes to include asset-backed debt and specialty finance sub-strategies in the SBCERS Private Credit Portfolio over the long term.

**Current SBCERS Private Credit Portfolio**



■ Direct Lending ■ Asset-Backed ■ Multi-Strategy ■ Distressed

**Long-Term Proposed SBCERS Private Credit Portfolio**



■ Direct Lending ■ Asset-Backed ■ Multi-Strategy ■ Distressed

# Fiscal Year 2025 Strategic Plan

## Identifying Fiscal Year 2025 Private Credit Portfolio Objectives

### Manager Relationships

- Build a new relationship with at least one additional private credit investment manager to maintain manager diversification.

### Pacing Plan

- Commit \$55 million between two private credit funds in order to reach the target allocation by approximately late 2027.

### Strategic Exposure

- Consider commitments to new or lesser allocated sub-strategies such as distressed or asset-backed debt to achieve sub-strategy diversification.

## Forward Calendar

Date	SBCERS Private Credit Portfolio Event
June 2024	Present the 2024 Private Credit Strategic Plan
2 <sup>nd</sup> Half 2024	Recommend approximately \$27.5 million commitment
1 <sup>st</sup> Half 2025	Recommend approximately \$25 million commitment



# Private Credit Fund Pipeline



# RVK Private Credit Manager Pipeline

## Asset-Backed / Specialty Finance

### Evergreen

- Atalaya Asset Income Fund Evergreen
- Ares Pathfinder Core

### Closed-End

- Atalaya Special Opps Fund IX
- Castlake Income Opportunities Fund III
- First Eagle Asset-Based Lending
- Victory Park Asset-Backed Opportunistic Credit Fund II
- Waterfall Private Asset-Backed Credit Fund I

## Diversified Direct Lending

### Evergreen

- Angelo Gordon Direct Lending Evergreen Fund
- Blackstone Senior Direct Lending Fund
- Blue Owl Diversified Lending Fund
- Comvest Credit Partners Evergreen Fund
- KKR Direct Lending Evergreen Fund

### Closed-End

- First Eagle Direct Lending Fund VI
- Deerpath Capital Partners VII
- Monroe Capital Private Credit Fund V

## Distressed Debt / Special Situations

### Closed-End

- Anchorage Credit Opportunities Fund IX
- Angelo Gordon Credit Solutions Fund III
- Beach Point Capital Opportunities Fund V
- BlackRock Global Credit Opportunities Fund III
- H.I.G. Bayside Loan Opportunity Fund VIII
- Marathon Dislocation Credit Fund II
- Monarch Capital Partners Fund VI
- Oaktree Opportunities Fund XII
- Silver Point Distressed Opportunity Institutional Partners II
- SVP Capital Solutions Fund II\*

## Opportunistic Strategies

### Evergreen

- Grosvenor Evergreen Performing Credit Fund
- Carlyle Flexible Credit Opportunities
- Sixth Street TAO Replacement

### Closed-End

- Pantheon Credit Opportunities III

Forward calendar will change based on market conditions, fundraising environment, general partner turnover, fund performance, and other circumstances.

\* Indicates MWBE firms.

# Appendix



# Pacing Study Outline

## OBJECTIVE

Set a reasonable 5-year target commitment allocation schedule that results in the total fund approaching the private credit allocation.

- *The commitment pacing plan should be revisited annually*

## PROCESS

RVK uses proprietary software to model the existing portfolio and expected forward commitments. A number of assumptions are made throughout this analysis and include the following:

- *Private credit investment cash flow/valuation patterns based on historical data from Preqin Alternatives*
- *A custom annualized growth rate for the overall total composite, net of spending rate*

## OUTPUT

The pacing study provides a recommended annual commitment volume to meet the total fund's private credit target.

- *Vintage commitments shown below may be made to one or more investment managers depending on the size of the commitment*
- *Likely to approach private credit target slowly to minimize vintage year risk*



# Pacing Study Assumptions

RVK utilized the following assumptions in this analysis:

The expected net growth rate assumes a compound return of 6.47%, based on RVK's most recent asset allocation study.

Future proposed annual commitments are allocated between two private credit fund commitments annually.

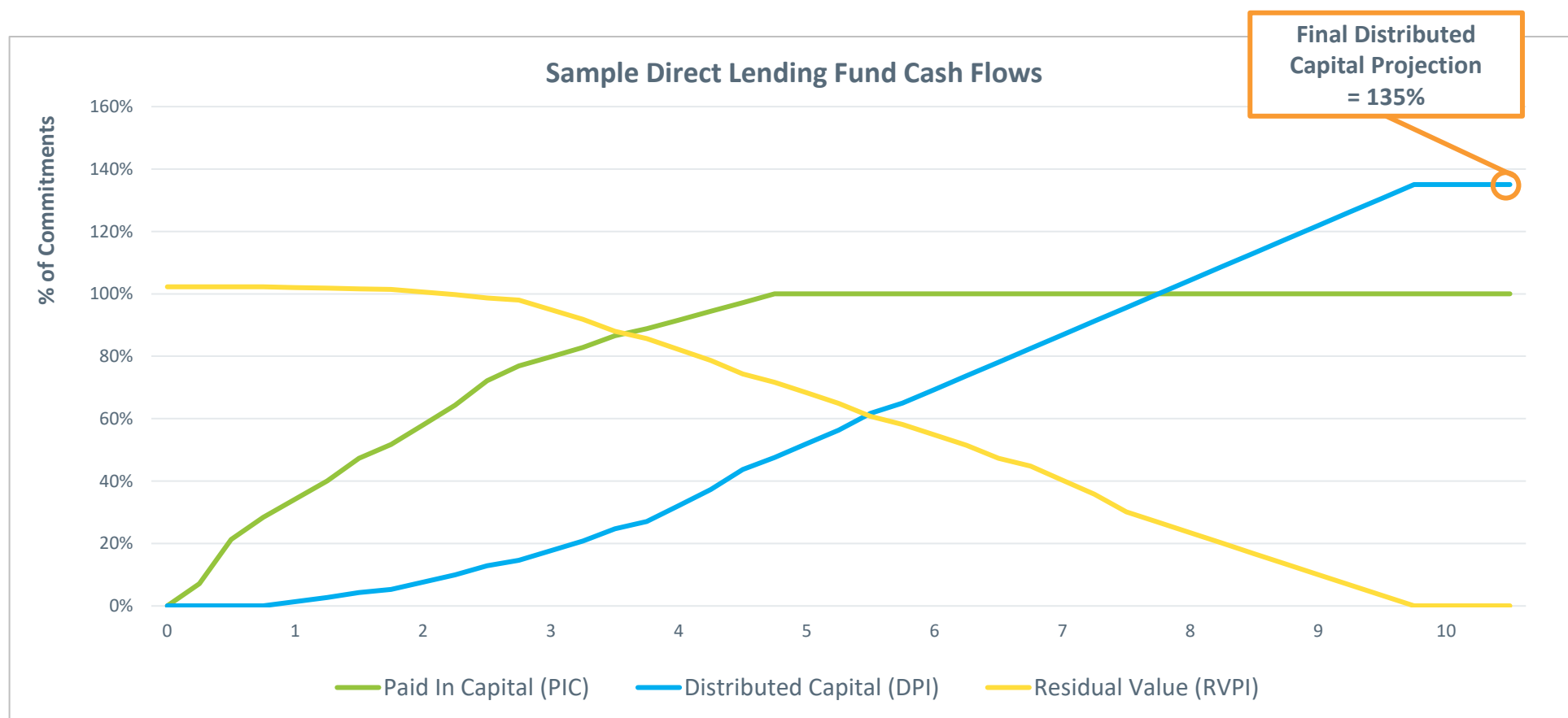
Fund cash flow projections for both existing and proposed traditional fund commitments are based on historical, weighted averages from the Private Debt – Direct Lending peer group, provided by Preqin.

Fund cash flow projections for both existing and proposed evergreen fund commitments assume an annual total return of 8%, derived entirely from reinvested income.



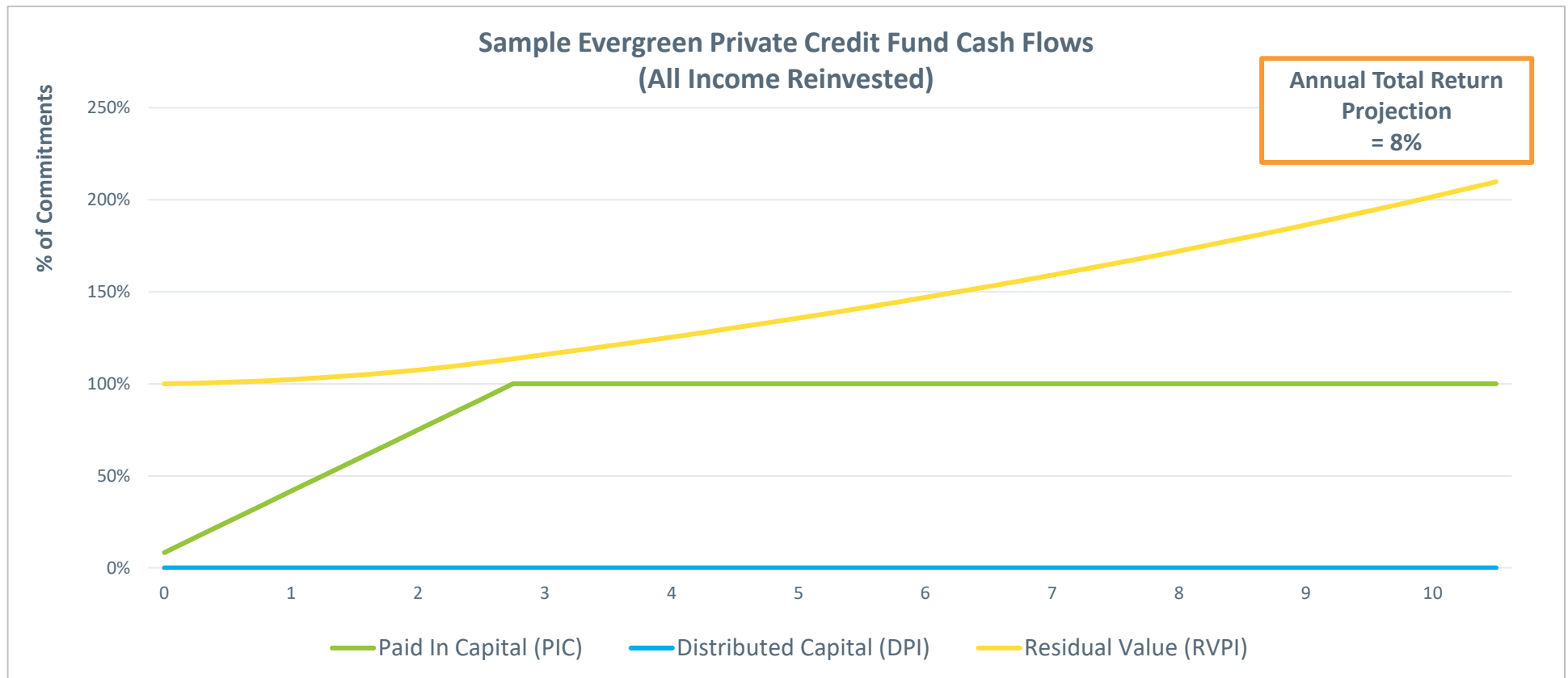
# Pacing Study Methodology – Direct Lending Funds

The purpose of the pacing study is to develop estimates based on long-term industry averages for use in general cash flow and allocation target planning. The pacing study depicts cash flow and valuation estimates utilizing average historical data. Actual cash flows and allocation percentages may vary substantially from these estimates due to market conditions. This analysis should be used for planning purposes only, and no expectations should be made that actual cash flows and allocation percentages will occur at the exact time and level depicted.



# Pacing Study Methodology – Evergreen Funds

The evergreen private credit funds assume an annual total return of 8%, derived mostly from the income that is **reinvested**. As such, the evergreen funds will project zero distributions throughout the life of the funds, with the residual value of the fund growing at 8% annually.



# Glossary

<b>Contribution</b>	A cash flow into the private market investment, sent by the investor. Also described as 'Paid In (Capital)'.
<b>Distribution</b>	A cash flow out of the private market investment, received by the investor.
<b>Commitment</b>	The maximum amount of capital an investor expects they would invest during a fund's life. Most funds call between 95% and 100% of commitments.
<b>Net Cash Flows</b>	The sum of contributions and distributions.
<b>Total Net Value</b>	$(\text{Distributions} + \text{Net Asset Value}) - \text{Contributions}$ This represents all value created by an investment, both realized and unrealized.
<b>Total Value to Paid In (TVPI)</b>	The ratio $(\text{Distributions} + \text{Net Asset Value}) / \text{Contributions}$ . This represents the total value created in a fund as a normalized value.
<b>Distributions to Paid In (DPI)</b>	The ratio $\text{Distributions} / \text{Contributions}$ . This represents the realized value created in a fund as a normalized value.
<b>Residual Valuation (RVPI)</b>	The ratio $(\text{Net Asset Value}) / \text{Contributions}$ . This represents the unrealized value created in a fund as a normalized value.
<b>Internal Rate of Return (IRR)</b>	A dollar-weighted measure of return. IRR is defined as the discount rate that reduces the net present value of an investment to zero. IRR almost always represents inception to date annualized returns.
<b>Growth Rate</b>	The assumed growth rate of the total fund. The total fund is assumed to grow at the geometric value from the client's most recent asset allocation minus any expected spending rate plus any expected contributions unless otherwise stated.

PORTLAND

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