



State of New Jersey

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September 29, 2017

MEMORANDUM TO: The State Investment Council

FROM: Christopher McDonough
Director

SUBJECT: **Proposed Investment in Stonepeak Infrastructure Fund III LP**

The New Jersey Division of Investment (“Division”) is proposing an investment of up to \$125 million in Stonepeak Infrastructure Fund III LP (“Fund”). This memorandum is presented to the State Investment Council (the “Council”) pursuant to N.J.A.C. 17:16-69.9.

The Fund will continue the successful track record of Stonepeak Infrastructure Partners (“Stonepeak”) on two prior funds focusing on infrastructure assets in the U.S. and Canada lower-to-upper middle market. These assets tend to have high barriers to entry, stable and predictable cash flows, low operational risk, and strong underlying growth characteristics which shield them from macro factors.

The Division is recommending this investment based on the following factors:

North American and Diversified Orientation: Stonepeak exclusively focuses on North America infrastructure which avoids currency and country risks. The Fund has the flexibility to invest across multiple sectors and the team has a track record of capitalizing on cyclical and secular industry trends.

Experienced and Long-tenured Team: The co-founders Michael Dorrell and Trent Vichie are infrastructure veterans with deep operational experience. They have worked together for 16 years and have successfully built infrastructure platforms. At Stonepeak, they have assembled a team of senior professionals with whom they have worked previously and who have complementary experience. Turnover is low vs. other organizations.

Disciplined Approach: The team is disciplined in assessing value, price and risk. The team has a reputation for walking away from transactions that exceed their parameters. Additionally, downside protection is central to their investment structuring. Transactions are structured with multiple covenants and counterparty operating contracts, which significantly reduce downside risk.

Competitive Advantage through Early Entrance: The co-founders Mr. Dorrell and Mr. Vichie worked together at Macquarie Bank in Australia when the infrastructure sector was in its infancy. They relocated to New York in 2001 and 2000 respectively to help establish a US infrastructure platform for Macquarie. The team has deep relationships across the North American infrastructure

industry. Stonepeak has a track record of originating investments off-market through their relationships (73% of prior funds). As a result, they often get early access to deals, and an opportunity to engage and execute without significant market competition.

Strong and Consistent returns with Conservative Leverage Usage: Stonepeak Infrastructure Fund LP was marked at net returns of 14.3% Internal Rate of Return (“IRR”) and 1.41x with 41% net debt to total capitalization as of March 31, 2017. Stonepeak Infrastructure Fund II marked at net 31.2% IRR and 1.23x with 25% net debt to total capitalization as of March 31, 2017.

Alignment of Interest and Attractive Fee structure: Stonepeak is offering a 15% carry (vs. 20%) for first close investors, which they are extending to the Division with certainty of closing. They are also offering a discounted management fee of 1.375% (vs. 1.5%) based on the aggregate commitments from TorreyCove clients. Stonepeak management is committing 1% of the aggregate fund commitments and their carry is widely distributed among the entire team.

A report of the Investment Policy Committee (“IPC”) summarizing the details of the proposed investment is attached.

Division staff and its real asset consultant, TorreyCove Capital Partners, undertook extensive due diligence on the proposed investment in accordance with the Division’s Alternative Investment Due Diligence Procedures.

The fund utilized Campbell Lutyens & Co. Ltd (the "placement agent") as third-party solicitor in connection with the potential investment. Staff has determined that the placement agent and its representatives met the registration, licensing and experience requirements set forth in the Division’s Placement Agent Policy (the "Policy"). Pursuant to the Policy, Stonepeak has disclosed the contract between the Fund and the placement agent, specifying the scope of services to be performed by the placement agent and the fee arrangement between the placement agent, the general partner and any other third party.

We will work with representatives of the Division of Law and outside counsel to review and negotiate specific terms of the legal documents to govern the investment. We have obtained a preliminary Disclosure Report of Political Contributions in accordance with the Council’s regulation governing political contributions (N.J.A.C. 17:16-4) and no political contributions have been disclosed. We will obtain an updated Disclosure Report at the time of closing.

Please note that the investment is authorized pursuant to Articles 69 and 71 of the Council’s regulations. Stonepeak Infrastructure Fund III LP will be considered a real asset investment, as defined under N.J.A.C. 17:16-71.1.

A formal written due diligence report for the proposed investment was sent to each member of the IPC and a meeting of the Committee was held on September 20, 2017. In addition to the formal written due diligence report, all other information obtained by the Division on the investment was made available to the IPC.

We look forward to discussing the proposed investment at the Council’s October 4, 2017 meeting.

Attachments

Fund Name: Stonepeak Infrastructure Fund III LP **September 29, 2017**

Contact Info: *Michael Dorrell, 717 Fifth Ave, New York, NY 10022*

Fund Details:		Key Investment Professionals: <i>Michael Dorrell</i> , Senior Managing Director and Co-Founder of Stonepeak. Mr. Dorrell formerly worked as a Senior Managing Director in Private Equity and co-head of the infrastructure group at Blackstone, and prior to that was a Senior Managing Director at Macquarie. <i>Trent Vichie</i> , Senior Managing Director and Co-Founder of Stonepeak. Mr. Vichie worked as a Senior Managing Director in Private Equity and co-head of the infrastructure investment group at Blackstone, and prior to that was a Managing Director at Macquarie. <i>Luke Taylor</i> , Senior Managing Director with Stonepeak, serving as the sector head for transportation and as a member of Stonepeak's Investment Committee. Mr. Taylor formerly was a Vice President at Macquarie and has over 15 years of experience in infrastructure. <i>Jack Howell</i> , Senior Managing Director with Stonepeak, serving as both the sector head for midstream and a member of Stonepeak's Investment Committee.
Total Firm Assets (\$bil; 06/30/16):	\$5.7 billion	
Strategy:	Infrastructure	
Year Founded:	2011	
Headquarters:	New York	
GP Commitment:	1% of capital commitments	

Investment Summary

Fund III will be a continuation of the strategy set forth in the prior two funds focusing on infrastructure assets in the U.S. and Canadian lower-to-upper middle market requiring \$100.0 million to \$1.0 billion of equity. The team focuses on assets that are inflation-linked, long-lived and which provide an essential service. These assets tend to have high barriers to entry, stable and predictable cash flows, low operational risk, and strong underlying growth characteristics which shields them from macro factors. Investment opportunities typically involve operational improvement and expansion rather than greenfield/new construction. Investment initiatives will be in the form of accretive platform bolt-ons, customer and volume growth, and re-optimization of the business and/or asset to correct prior under-utilization or under-management.

Existing and Prior Funds

<i>Funds</i>	<i>Vintage Year</i>	<i>Strategy</i>	<i>Returns as of March 31, 2017</i>
Stonepeak Infrastructure Fund LP	2013	Infrastructure	14.3% Net IRR, 1.26x Net MOIC
Stonepeak Infrastructure Fund II LP	2016	Infrastructure	31.2% Net IRR, 1.17x Net MOIC

IRR = Internal Rate of Return; MOIC = Multiple on Invested Capital

Vehicle Information:

Inception:	2017	Auditor:	Pricewaterhouse Coopers
Fund Size (\$mil.):	\$7.0 billion	Legal Counsel:	Simpson Thacher & Bartlett LLP
Management Fee:	1.375%		
Carry:	15%		
Hurdle Rate:	8%		
Additional Expenses:	100% management fee offset		

NJ AIP Program			
Recommended Allocation (\$mil.):	up to \$125 million	LP Advisory Board Membership:	TBD
% of Fund:	1.79%	Consultant Recommendation:	Yes
		Placement Agent:	Yes
		Compliance w/ Division Placement Agent Policy:	Yes
		Compliance w/ SIC Political Contribution Reg:	Yes

*This review memorandum was prepared in accordance with the State Investment Council rules governing the Alternatives Investment Program and the policies and procedures related thereto.