

News and Analysis

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Montana explores multi-asset strategies, commits \$125m to private markets

The \$18bn fund may also have opportunities for managers in natural resources, REITs, and high yield.

Dietrich Knauth | 06 Jun 2018

The **Montana State Investment Board** is researching multi-asset strategies to build out a new diversifying strategies, and may also be on the lookout managers in its natural resources and real estate portfolio.

The fund, which manages \$18.4bn in assets in several pension funds and state trusts, including \$11.4bn in pension assets, also reviewed \$125m in private markets commitments at its May 22 meeting.

Diversifying assets it a new asset class for the state, which gave investment staff the go-ahead in February to begin allocating to a target of 0% to 4%.

The asset class includes a potentially wide mix of public markets investments that seek to provide downside protection while maintaining liquidity and providing a better return than just holding onto cash. Creating a new asset class was necessary, according to CIO **Joe Cullen**, to allow the

state pension funds to take advantage of multi-asset strategies and other investments that otherwise would not fit within the state's asset allocation structure.

Montana has started building the asset class with an internally-managed strategy focused on long duration U.S. Treasuries, and currently has an allocation of \$26m, or 0.26% of its pension portfolio.

"If interest rates continue to rise meaningfully, we'll probably add a little bit more to that position, but more meaningful to this asset class of diversifying strategies, [director of public markets] **Rande [Muffick]** and the public markets team are looking at some of these multi asset class managers," Cullen said at the May meeting. "We're looking, we're not going to say 'oh by this date we'll have one' but we're going through a process now during the summer that if one comes out of that process, or two, over the summer, then that's something we'll bring to you in the fall."

Board secretary **Dana Chapman** told *MMR* that no RFP will be issued, and the internal decision process is ongoing and may include Montana's general investment consultant, **RVK**.

In private markets commitments, Montana committed \$30m to **Deerpath Capital Advantage IV**, \$20m to **Builders VC Fund I**, and \$75m to **OCP Asia Fund III**.

Investment officer **Michael Nguyen** said that the Deerpath and OCP commitments were part of a strategic initiative to focus more on credit funds. He called Deerpath a "plain vanilla" credit fund focused on lower-middle market direct lending, with a well-established team, high underwriting standards, and an emphasis on senior secured loans to companies are too small to get bank financing at better rates. The Builders fund is a small \$200m venture fund that looks at technology that solves problems, and offers mentorship to promising startups, such as a computational biology company that uses technology to help evaluation combinations of drugs used to fight childhood leukemia. OCP Fund III, which adds to a \$30m commitment to the manager's previous fund, is a credit strategy focused on Southeast Asia, China, and Australia, Nguyen said.

Ethan Hurley, director of private market investments, said that Montana's \$1.2bn private equity portfolio is North American-centric, buyout focused, and increasingly interested in investing in Asia and in direct fund exposure, rather than fund-of-funds. The portfolio is currently 25% invested in fund-of-funds, but Montana is considering selling some of those investments on the secondary market, Hurley said.

"Given the current environment and how we view our portfolio it is my hope that we will transact this year and reduce some of our legacy non-going concern exposure, particularly on the fund-of-fund side," Hurley said. "I hesitate to say that in a public forum, because the phone calls will start rolling in once these minutes are released."

In natural resources, portfolio value was boosted by rising prices for timber and oil, and Montana said it will be looking for a manager in that space.

"We are starting to look at potentially adding a public REIT manager to the real estate asset class, as we are looking to potentially add a public MLP or midstream equity manager to the natural resources asset class," Hurley said.

Another asset class that may see more activity is high yield, which is currently 2.8% of Montana's pension portfolio. The asset class is also relatively new, with two managers funded in December at \$50m each, **Oaktree Capital Management** and **Shenkman Capital Management**. CIO Cullen said that the asset class has underperformed, which is common during good markets, but it offers downside protection that can play a key role in the overall portfolio mix.

"As a long term asset class, high yield is a great asset class and one that we're likely to increase over time," Cullen said, noting that prices for high yield strategies are not extremely attractive right now. "As things normalize, if they do when they do, we would expect to be more buyers and add a little bit more more high yield. Probably that would be funded over time by a reduction in U.S. equities."

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