TESTIMONY ON BEHALF OF STATE TREASURER DENISE L. NAPPIER
SUBMITTED TO THE FINANCE, REVENUE AND BONDING COMMITTEE
APRIL 25, 2017

Good afternoon, Senator Fonfara, Senator Frantz, Representative Rojas, Representative Davis and members of the Finance, Revenue and Bonding Committee. My Name is Wei Huang and I am the Principal Investment Officer for private equity at the Office of the Treasurer. I am testifying on behalf of State Treasurer Denise Nappier.

Thank you for the opportunity to discuss **Raised Bill 1051, A*n Act Concerning CTNEXT Planning Grants-In-Aid and Innovation Place Designation Applications, Invest CT Fund Tax Credit Transferability and State Investments with Venture Capital Firms.***

Treasurer Nappier commends the leadership and members of the Committee for their commitment to strengthening Connecticut's economy through support of businesses in this State. This is a passion that the Treasurer shares because she has long believed that there are numerous opportunities to generate solid returns here in our own backyard.

Investing in Connecticut is by no means a mere altruistic endeavor: The Treasury is in this to make prudent, profitable investment decisions that generate long-term value. Indeed, the merits of such a focus are embedded in the framework that guides the investment of the assets of the Connecticut Retirement Plans and Trust Funds ("CRPTF").

That framework is set forth in the Investment Policy Statement (or "IPS"), which reflects the iterative process that exists between the Treasurer, as principal fiduciary of the investment of the CRPTF, and the State's independent Investment Advisory Council ("IAC"), which endorses the investment strategy and sets the asset allocation strategy. (It bears noting that the IAC includes five members appointed by the Governor and legislative leaders, and five members representing teachers' and state employees' unions.)

The IPS explicitly requires, as part of the process for hiring investment managers, that the Treasury "encourage investment within the State of Connecticut that, as a matter of policy, seeks risk-adjusted, rates of return and adheres to investment evaluation standards as set forth in this statement and State Statutes."[1] These guidelines go on to provide that "[i]n cooperation with State of Connecticut agencies and/or through partnership with public and private entities, these targeted investments will include, but not be limited to, under-served urban and rural markets."[2]

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1 *See Investment Policy Statement for the State of Connecticut Retirement Plans & Trust Funds* at http://www.ott.ct.gov/pensiondocs/IPStatement.pdf at page 14.
2 *Id.*

The impact of the CRPTF's investments in Connecticut can be measured in two ways. The first is where Connecticut-based investment managers have competed for and earned commitments of funds from the State Treasury, which benefits our economy because of the workers employed by the managers and the taxes they and their employees pay. Since inception of the Private Investment Fund in 1987, which includes venture capital,[3] the CRPTF has made $2.7 billion of capital commitments to 25 funds led by 16 Connecticut-based managers. A total value of $3.8 billion has been created through these commitments, and $1.4 billion of capital gains have been generated.

The second way that the CRPTF invests in Connecticut is through underlying investments made in Connecticut-based companies by our investment managers. The funds led by Connecticut-based managers to which the CRPTF has committed capital have invested $820.2 million in 54 underlying entities located in Connecticut, generating a total value of $1.9 billion and $1.1 billion in capital gains.

For example, one of these funds was managed by Connecticut-based RFE Investment Partners VII, based in New Canaan. In August 2011, the fund invested $17.5 million in ShelterLogic, a manufacturer and marketer of sheds, shelters and canopies headquartered in Watertown. The fund remains actively involved in the company and the investment has nearly tripled in value.

More recently, Treasurer Nappier focused the Treasury's investment strategy in Connecticut even further. In 2015, she initiated a targeted in-state investment program and earmarked $145 million for various strategies, including venture capital. After some time spent building the program's structure, the program now is up and running, and thus far the Treasury has committed $10.5 million to Connecticut-based companies.

So in these ways, the CRPTF has made a measurable positive contribution to our State's economy, and is guided by an investment strategy that explicitly includes Connecticut. With that said, the CRPTF is bound by a broader asset allocation strategy which seeks to balance the $30.1 billion portfolio in ways that balances returns and risk and meets an investment return assumption over the long term. There are carefully considered limits

[3] The CRPTF's Private Investment Fund ("PIF") consists of a number of externally managed funds invested across venture capital and corporate finance private equity strategies. Venture Capital typically involves equity capital invested in young or development stage companies.

on the funds' exposures to any one asset class, and, in the case of our exposure to venture capital, we stand at 25.3 percent of the Private Investment Fund – slightly above our target of 25 percent.[4]

Turning to the Raised Bill before you, Treasurer Nappier applauds its objectives to increase investment in Connecticut and to support emerging firms. She would, however, like to register some observations and concerns with the processes it proposes.

Specifically, the legislation directs the Treasurer to consult with the chief executive of Connecticut Innovations on any investment of state funds in a start-up business, venture capital fund, or fund of funds. This consultation would be required not just for Connecticut investments, but would extend to any defined investment in the country or, indeed, the world. This requirement could affect a number of existing contractual arrangements with investment managers that have discretionary authority to invest in venture capital or fund-of-funds. Moreover, it would conflict with both state statute and the Investment Policy Statement, which sets strict requirements for how investment decisions are made.

The legislation also sets requirements that any firm managing state funds for venture capital investment must have an office in Connecticut, at least one employee in the state, and sub-managers who adhere to the same terms. This provision would limit investment choices and reduce overall opportunities for investment gain. At the end of the day, the Treasury must ensure that Connecticut's investments benefit from access to the best investment management services available, no matter where they may be domiciled.

With respect to the reporting requirements set forth in the bill, Treasurer Nappier has no issue here. Transparency has been a hallmark of her administration.

And last, but not least, it deserves mention that the Treasurer serves on the board of Connecticut Innovations, and her office has been able to compare notes on investment opportunities. As a side note, I am her designated representative on the board. A more collaborative relationship with CI is most welcomed. Indeed, the Treasurer's Office has, over the course of the past year, been working closely with CI in an effort to develop appropriate programs to meet the capital needs of Connecticut businesses and to source

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[4] That translates to a venture capital exposure valued at $644.6 million, out of the total Private Investment Fund valued at $2.5 billion, as of September 30, 2016.

prudent investment opportunities. The Treasurer and I remain committed to those efforts.

So, in keeping with what we understand the spirit of this bill to be -- to more effectively use the State's resources to expand investment in Connecticut companies – I respectfully offer the following suggestion: let's maximize the respective strengths and capabilities of Connecticut Innovations and the Treasury. Where CI has considerable expertise is in early stage investments with companies just getting off the ground. In this space there is considerable risk, and CI was designed in a way that it could take the hits to its bottom line in hopes of finding the gems among the coal. Where CI finds the early success stories -- those businesses that have grown beyond the incubation phase and are ready for the next phase of capital and growth -- that is where the CRPTF's investment can be most effectively utilized. The Treasury's investment managers can make the bigger bets on the companies that CI has nurtured, with a better shot at earning the risk-adjusted returns that a fiduciary such as the Treasurer must insist upon.

What this raised bill is striving for is a better-developed pipeline of capital available to companies in Connecticut. Treasurer Nappier is committed to working toward that goal.

Thank you for the opportunity to offer comments on this important legislation. Our Office stands ready to work with you to craft revised language that meets the objectives of the bill and minimizes unintended consequences.