

Attachment 1b

# NEPC Research Investment Due Diligence Rating

## 400 Capital Management *Asset Based Term Fund II*

**March 31, 2019**

**Product Rating: 2**



BOSTON | ATLANTA | CHARLOTTE | CHICAGO | DETROIT | LAS VEGAS | PORTLAND | SAN FRANCISCO

# 400 Capital Management

## Asset Based Term Fund II

Strategy Information	
<b>Firm and Strategy</b>	<i>400 Capital Management – Asset Based Term Fund II</i>
<b>Rating Universe/FPL</b>	<i>Opportunistic Credit</i>
<b>Benchmark</b>	<i>HFRI RV: Fixed Income-Asset Backed Securities</i>
<b>Proposed Rating</b>	<b>2</b>
<b>Research Owner</b>	<i>Kevin Bliss</i>

Rating Matrix	
<b>People</b>	<b>2</b>
<b>Process</b>	<b>1</b>
<b>Portfolio</b>	<b>2</b>
<b>Performance</b>	<b>3</b>
<b>Products/Pricing</b>	<b>2</b>

### Firm Overview

400 Capital Management LLC (“400CM” or the “Firm”) was founded in October 2008 by Chris Hentemann, Paul Jablansky, and Heloisa Chaney. The Firm manages approximately \$3.4 billion across its flagship product, Credit Opportunities Fund (“COF” or the “Flagship Fund”); Asset Based Term strategies; and nine SMAs/Fund of Ones.

As of March 31, 2019, the Firm employs 42 professionals and is based in New York with a satellite office in London. It specializes in structured credit investments across a range of sectors, including but not limited to, Residential Mortgage Backed Securities (RMBS), Commercial Mortgage Backed Securities (CMBS), other Asset Backed Securities (ABS), Collateralized Loan Obligations (CLOs), and products related to distressed structured credit portfolios.

### Firm History

Prior to launching 400CM, Mr. Hentemann spent over 12 years at Banc of America Securities (“BAS”), from May 1996 to October 2008. During this time, he played a key role in the creation and development of the bank’s MBS, ABS, and CMBS market-making, securitization, and proprietary trading businesses. Mr. Hentemann also led the international expansions of these businesses to Europe and Asia. At the time of his departure from BAS, Mr. Hentemann was the Head of the Global Structured Products, a role he held since January 2007. This group was responsible for investing in RMBS, CMBS, ABS, collateralized loan obligations (CLOs), collateralized debt obligations (CDOs), as well as certain tax and credit derivative instruments. In 2007, despite the subprime overhang, many banks encouraged their trading desks to assume more risk. Mr. Hentemann, given his discomfort with the market environment and the risk controls, departed the firm in early 2008.



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Soon after his departure, Mr. Hentemann began working on the business plan for 400CM. 400CM was officially launched in October 2008. However, it proved to be an extremely difficult asset raising environment. In early 2009, the team presented to potential investors, including a few capital seeding firms. However, Mr. Hentemann decided against taking any seed capital due to the onerous terms that were proposed at the time. Instead the team decided to start trading on February 1, 2009 with principal capital and the Fund was launched with \$2.5 million. By late 2009 the Firm continued to have difficulty gaining traction with investors, which caused initial co-founder, Mr. Jablansky, to leave for another opportunity in March of 2010.

Mr. Hentemann has grown the Firm to approximately \$3.4 billion in assets under management and 42 professionals. The Firm's flagship fund, Credit Opportunities Fund, accounts for the majority of its assets today, with \$1.8 billion in assets under management. It manages approximately \$1.2 billion in custom accounts, \$227 million in the Asset Based Term Fund I, and has received approximately \$185 million in commitments for Asset Based Term Fund II.

### **Strategy Description**

400 Capital Management ("400CM" or the "Firm") is raising the Asset Based Term Fund II ("ABTF II", the "Strategy", or the "Fund"), the second iteration in the Firm's series of illiquid asset-backed structured credit strategies. 400CM was founded in 2009 by Chris Hentemann as an asset management firm focused on capitalizing on dislocations and other opportunities in structured credit.

The Strategy employs an opportunistic and flexible mandate to invest in the illiquid structured credit markets. The Fund's strategy can be thought of in four distinct buckets: 1) opportunities within structured products that have been dislocated and stressed as a result of the market volatility and liquidity challenges presented by the COVID-19 pandemic; 2) purchasing re-performing single-family mortgages ("RPLs") from the Government Sponsored Entities ("GSEs") Freddie Mac; 3) opportunistic investing in high quality ABS issued through the Term Asset-Backed Securities Leverage Facility ("TALF") and other specialty finance opportunities; 3) European regulatory capital relief through direct loan acquisition or regulatory capital relief transactions such as CDS.

The Firm raised \$227.1 million for ABTF I and its harvest period will end in August 2020. Given the liquidity profile of the Fund and its underlying assets, NEPC believes that it is likely that the GP will elect to trigger its extension following the culmination of Fund I's stated term.

400CM is seeking to raise \$400 million with a hard cap of \$500 million for Fund II. Given the market size of the Fund's intended strategies, NEPC anticipates that it will find ample opportunity in the market to deploy the intended capital. The Fund is targeting a 12%-to-15% net IRR with a 1.5x-to-2.0x net multiple.

The Fund is structured as a drawdown style vehicle with a two-year investment period and a five-year term. It is subject to a one-year extension at the General Partner's ("GP's") discretion and an additional one-year extension with the approval of at least 50% of Limited Partners ("LPs"). The first close occurred on June 19, 2019 and will be followed by a final close on June 20, 2020, or when the Fund reaches a maximum capacity of \$500 million. NEPC has secured at least \$100 million of capacity for our clients.



## 400 Capital Management

### *Asset Based Term Fund II*

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#### **Investment Thesis/Analyst Opinion**

ABTF II will target opportunities in a non-competitive investment landscape due in large part to the barriers of entry, small deal size, and the need for proprietary sourcing of deals. Additionally, there is a level of complexity that requires a highly specialized team to deliver on the investment thesis. NEPC believes that the 400CM team is well positioned to identify and execute on current and future market opportunities in the structured credit space.

Current market conditions lend well to the Fund's investment universe. First, dislocation across risk assets in Q1 2020 dramatically shifted the investment landscape across both credit and equity. Structured credit was impacted materially by liquidity impairment resulting from margin calls, forced liquidations, and to a lesser extent, broader questions around the consumer as the COVID-19 pandemic halted the US and global economies. 400 Capital is well positioned to take advantage of liquidity-driven impairments by using cash reserves to purchase quality dislocated assets at a discount.

Second, the GSEs are under pressure from Congress and other government authorities to reduce balance sheet exposure to credit risk through risk transfer programs. Both 400CM and peers in the space generally expect conservatorship of the GSEs to continue beyond 2020 and for continued pressure to derisk their balance sheets. This lends well to the SCRT and SLST programs as the government will continue to support a robust pipeline of opportunities coming to market in the foreseeable future.

Third, residential real estate has a generally favorable outlook as it pertains to the Strategy's lot banking sleeve. The Strategy may target residential homebuilding in high growth markets experiencing demonstrated positive net migration and observable supply limitations. The structure of the deals can lend protection to 400CM in the event of homebuilder default. 400CM is anticipating limited demand for new lot banking commitments in the near-term due to recent market dislocations and questions around the consumer and real estate markets. The Firm does not anticipate any new lot banking commitments in ABTF II, but does reserve the ability to do so, without utilizing leverage, if an attractive opportunity presents itself.

Finally, the European market is ripe with opportunity in risk transfer and nonperforming loans as regulators continue to encourage the reduction of risk from European banks to pre-crisis levels. The Fund will primarily target bank deleveraging in Portugal due to the strong housing recovery, relative strength of the local economy, and short liquidation timelines. The Portuguese market in particular is one driven by strong on-the-ground relationships. To this end, the 400CM team has partnered with local servicers in Portugal that provide local insights, diligence, and servicing. However, the team does not have a dedicated native Portuguese speaker and its reliance on third parties for a significant portion of the sub-strategy's execution is an area that warrants close monitoring.



# 400 Capital Management

## Asset Based Term Fund II

### Investment Positives:

- **Sourcing and Structuring** – Over the years, Chris Hentemann and his senior investment team have developed a deep network of relationships that helps them source niche and complex deals. Over 80% of ABTF I deals were sourced privately via bi-lateral (single lender) or club (multiple lenders) channels. In addition to sourcing, the investment team has also demonstrated expertise in structuring deals and securitizing assets. This has provided 400CM with a considerable edge over peers in the space since not many can access these trades or have a demonstrated success in securitizing assets. ABTF I traffics in an off-the-run investment arena. This is because investments tend to be small (\$10 million to \$20 million), complex, and often require a knowledgeable team with specialized skill set to underwrite it. We anticipate this environment to carry forward into Fund II.
- **Flexible Mandate** – The Fund targets a wide array of investments across structured credit including special situations, risk-transfers, and liquidity premium opportunities in the primary and secondary markets. The flexible mandate allows 400CM to invest where the team believes the best risk-return exists, instead of being anchored to only one investment theme. Additionally, the Fund’s expanded mandate allows it to be an early investor in the Federal Reserve’s relaunched TALF program if the team finds it to be an attractive opportunity. This should allow the Fund to move faster than some peers who are still in the process of establishing funds to take advantage of TALF.
- **Team Experience and Continuity** – The investment team at 400CM has significant experience investing in the structured credit markets. The senior members at the Firm have worked together for over two decades and have developed a consistent investment process.
- **Investment Breadth** – The Firm’s core business is investing across the spectrum of multi-sector structured credit investments. Over its tenure, the Firm has successfully rotated capital across different sectors, within sub-sectors (agency vs. non-agency), as well as across the capital structure (tranches).
- **Fees** – 400CM will aggregate NEPC client assets in order to qualify for the minimum investment of Share Class A. Investors in Share Class A receive a 0.5% discount on management fees and 5.0% discount on carry, ultimately paying 1.0% management fee and 15.0% carry over a 6.0% hurdle.
- **Sizing** – The Firm is implementing a hard cap of \$500 million on the Fund. A disciplined approach to Fund size ensures illiquid opportunities remain a manageable focus area for the Firm. It also reflects an appropriate approach to invest in capacity constrained investments.



# 400 Capital Management

## *Asset Based Term Fund II*

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### **Investment Negatives:**

- **Nascent performance** – ABTF II’s predecessor fund, ABTF I, a 2017 vintage fund, has achieved a current net multiple of 1.15x and a net IRR of 13.5% just under two years into its life and in a relatively benign structured credit market. This is across 10 deals and all performance to date is unrealized. While ABTF I investments are performing at or above expectations, it is still early in the life of Fund I to definitively categorize performance.
- **Key Person Risk** – The key person clause lists CIO Chris Hentemann and Principals Bill Sanders, Alex Cha, and Todd Leigh, and requires that Mr. Hentemann and at least two of the three Principals remain devoted to the Fund. It does not list Messrs. Schiavone or Willoughby or any other member of the private credit team.
- **Concentration** – ABTF II intends to take a similar portfolio construction approach to ABTF I, which has participated in 10 deals to date. This adds an element of concentration risk to the Fund. 400CM expects that Fund II will consist of 15-to-20 deals.
- **Complexity** – The Firm will likely invest in complex securities and transactions. Often these securities have collateral assets which are unique and during times of market stress may experience high degrees of illiquidity.
- **Leverage** – 400CM has structured the Fund in a manner that allows the lot banking strategy to use significant leverage at the project level. This leverage may be cross collateralized across all projects from the Holding Company. This could lead to an asset/liability mismatch in the event that a leverage provider decides to close a leverage line or a project is extended. However, because of recent market dislocation and in particular around forced deleveraging amongst peers, 400CM has deemphasized both the lot banking its potential use leverage within the Fund. It does not expect to complete any lot banking in ABTF II, but if it does, the Fund is not expected to use leverage.



## 400 Capital Management

### *Asset Based Term Fund II*

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#### **People: 2**

The Firm has 42 full time employees, 24 of which are investment professionals. The majority of senior investment professionals have worked together over the past 15 years, dating back to their time at Banc of America Securities. The investment team experienced several evolutions of the securitization market while at BAS. This experience working on the securitization side of the business has equipped the investment team with a unique edge in sourcing and structuring investments.

400CM's Founder and Chief Investment Officer Chris Hentemann will be responsible for oversight of the Fund, with Private Credit Portfolio Manager Chris Schiavone and Residential Credit Portfolio Manager Jeff Willoughby responsible for day-to-day management of the portfolio. Messrs. Schiavone and Willoughby will leverage existing teams and resources within the Firm to source, diligence, and execute opportunities. ABTF II will leverage the existing Residential and European teams at the Firm for sourcing opportunities. It may also source investments opportunistically from the CMBS, ABS, CLO, and Corporate teams.

Mr. Schiavone joined 400CM in June 2015 as Portfolio Manager specializing in Private Credit. He is responsible for idea generation and portfolio management of the private credit sleeve of the Firm's various funds, including its flagship fund, the 400 Capital Credit Opportunities Fund. He has over 21 years of experience. Prior to joining 400CM, he was responsible for sourcing, structuring, executing, and managing distressed opportunities at Perella Weinberg. Prior to his time at Perella, he was Head of Residential MBS origination at BAS.

Mr. Willoughby joined 400CM in July 2019 as Portfolio Manager specializing in residential credit and is responsible for sourcing, structuring, monitoring, and executing investment opportunities in the residential space. Prior to joining 400CM, Mr. Willoughby spent six years at Freddie Mac, where he was Co-head of Loan Portfolio Management and Structuring. He was responsible for a \$65 billion securities portfolio and a \$56 billion loan portfolio at Freddie. It is in this role that he executed several risk transfer deals with 400CM, some of which were allocated in ABTF I. Prior to his time at Freddie, he spent 11 years at BAS, where he worked with Mr. Hentemann.

In addition to Messrs. Schiavone and Willoughby, 400CM has recently added two dedicated employees focused on the Strategy. Kirk Meyers joined 400CM in September 2019 and serves as a Portfolio Manager on the Firm's private credit strategies. He is responsible for sourcing, structuring, monitoring, risk management, and execution. Mr. Meyers joined the Firm from Wells Fargo where he previously served as a Managing Director and Co-head of Mortgage Finance Securitization. Alex Andrzejewski joined 400CM in October 2019 and serves as an Associate Director of Private Credit. Prior to joining 400CM, he founded a real estate fintech company, ResiRoots, where he served as CEO. Prior to that, Mr. Andrzejewski worked at Altisource Asset Management and Banc of America, where he managed credit impaired mortgage exposure.

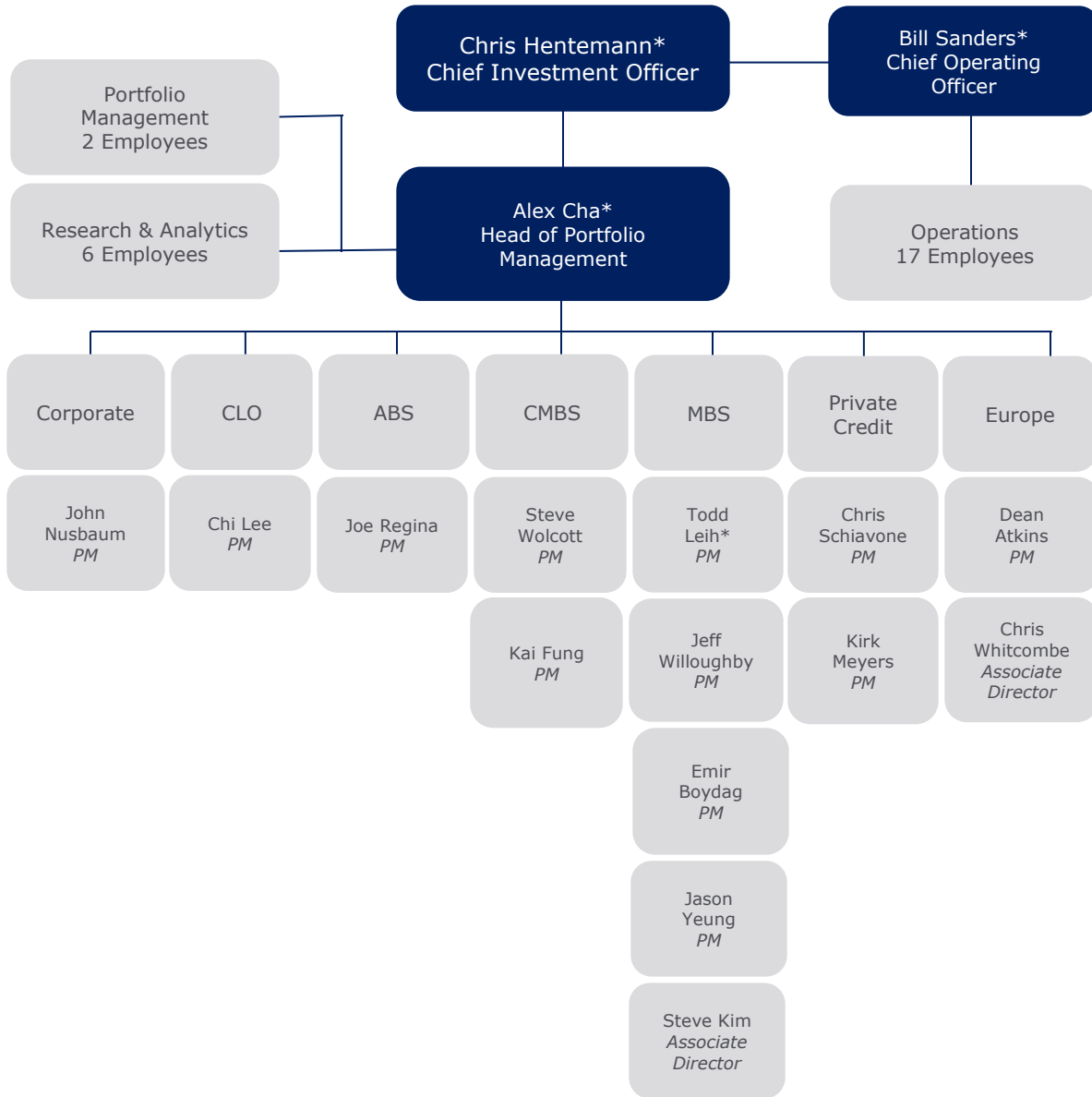
Mr. Hentemann and his team have an impressive track record in the structured credit market, including the residential mortgage space, and NEPC maintains a high conviction in 400CM's ability to source and execute on opportunities. With recent changes to the Fund's intended opportunity set, NEPC believes that ABTF II is complimentary to the team's core skillset and a natural extension of the Firm's product offerings.



# 400 Capital Management

## Asset Based Term Fund II

### Organization Chart



\*Indicates membership on the Investment Committee

### Succession Planning

The team at 400CM remains committed through the foreseeable future. However, should Mr. Hentemann cease involvement with the Firm, the key person clause would be triggered and would likely lead to the dissolution of 400CM.

# 400 Capital Management

## *Asset Based Term Fund II*

### **Process: 1**

The Firm employs a consistent process across its platform, blending top-down macro views with bottom-up fundamental security selection. It makes investment decisions on a combination of systematic and non-systematic risk, return, and valuation considerations. This allows the team to shift allocations tactically within its funds, as well as identify the best strategy to allocate opportunities to across the liquidity and risk spectrums.

400CM utilizes a multi-portfolio manager approach with sector specialists responsible for identifying and communicating attractive opportunities to the Investment Committee ("IC"), consisting of Messrs. Hentemann, Sanders, Cha, and Leih. The Fund targets opportunities in largely off-the-run investment arenas due to the proprietary nature of its investments.

Deal sourcing is designed to leverage the breadth and depth of the Firm's relationships, including from broker/dealers, direct engagement with management teams, legal and banking partners, and proprietary relationships through joint ventures and servicing partners. The team undertakes a highly selective investment process for ABTF II, choosing the best opportunities from a risk-return perspective. The Fund is aided in this by the nature of the market – opportunities and deal flows far exceed the size of the Fund, allowing it to select only the most attractive opportunities to pursue.

Ideas are typically sourced by analysts and portfolio managers through its proprietary joint ventures, established relationships with European banks, and industry contacts. Initial analysis typically includes a financial document review, qualitative review, capital structure analysis, and industry analysis. 400CM places a heavy emphasis on financial modeling, review of underlying loans, potential covenants, and market research.

The investment process begins with deal screening with weekly portfolio management team meetings to review new investment ideas. All new ideas must gain investment committee ("IC") approval before moving on in the process. After sourcing and approval from the IC, preliminary financial modeling is completed in addition to legal, financial, and tax structure analysis. A term sheet is issued at this stage in the process.

Following the initial underwriting, deep due diligence is conducted with particular focus on key valuation drivers, collateral and loan review and analysis, and operating partner review when applicable. If an idea makes it through the deep due diligence, it is brought back to the IC for a debate on the updated findings and modeling, document review, and IC approval for investment. Once the IC approves an idea and it is added to the portfolio, members of the team perform monthly position-level reviews with the private credit portfolio managers, quarterly re-underwriting of positions, and continuous monitoring of exit strategies.

The private credit team will be the primary team sourcing and diligencing ideas, but other teams may be utilized throughout the process given the experience and breadth of the team. Position sizing and portfolio construction decisions are a team effort and decided through the discussions of the team.

# 400 Capital Management

## Asset Based Term Fund II

### Portfolio: 2

ABTF II is targeting a mid-teen net internal rate of return, or IRR, and a net multiple of invested capital of 1.5x-to-2.0x. It intends to achieve this by investing primarily in opportunities across residential and commercial real estate, consumer finance, and specialty finance in the US and Western Europe. The Fund is designed to leverage the Firm's extensive relationships through broker/dealers, direct engagement with management teams, legal and financing partners, and proprietary relationships with joint venture and servicing partners.

ABTF II employs an opportunistic and flexible mandate to invest in the illiquid structured credit markets. The Fund will assemble a portfolio primarily across dislocated asset-backed securities as a result of the market volatility and liquidity challenges presented by the COVID-19 pandemic, re-performing mortgage-backed securities, opportunistic investing in programs like TALF and other specialty finance, and European bank deleveraging.

Opportunity	Strategy Examples	ABTF I	ABTF II
Market Dislocation	<ul style="list-style-type: none"><li>Structured products</li><li>Special situations</li><li>Non-performing loans</li></ul>	10%	30%-50%
GSE Residential Risk Transfer	<ul style="list-style-type: none"><li>GSE reperforming loans</li><li>Structured loan sales</li><li>Bank capital relief transactions</li></ul>	50%	20%-30%
Specialty Finance	<ul style="list-style-type: none"><li>TALF program participation</li><li>Residential land banking</li></ul>	15%	20%-30%
European Bank Deleveraging	<ul style="list-style-type: none"><li>Direct loan acquisitions</li><li>NPL securitizations</li><li>Regulatory capital relief transactions</li></ul>	25%	10%-20%

## 400 Capital Management

### *Asset Based Term Fund II*

#### **Dislocated Assets**

The primary opportunity set that has presented itself since the initial launch of the Strategy has been within dislocated structured credit. This opportunity manifested in the latter half of Q1 2020 as a result of market pressure associated with the COVID-19 pandemic. Structured products have historically lagged general trends in equity and corporate credit markets both on the upside and downside. However, several market events in March 2020 caused structured products in particular to underperform both equity and corporate credit markets.

While relatively isolated from broader market volatility during the majority of Q1 2020, events during the week of March 23<sup>rd</sup>, 2020 – and in particular during the preceding weekend – sent structured credit markets into a spiral caused by deleveraging, forced selling, and illiquidity. In a short period of time, the market saw several large BWICs (secondary auctions for loans, bonds, and securities) as several large REITs, ETFs, mutual funds, and highly levered asset managers were forced to meet margin calls and redemptions. This deleveraging and forced liquidation of large pools of assets caused a dramatic reduction in the market value of nearly all credit products, but most severely within the mortgage and asset-backed space.

400 Capital anticipates more volatility in the near- to intermediate-term within structured credit. Uncertainty remains around the ultimate impact of COVID-19 on the consumer, particularly within auto loans, consumer lending, mortgages, and student loans. Further volatility or market stress will present an opportunity for the Fund to act as a liquidity provider and purchasing quality assets at attractive prices. This opportunity set is a natural extension of 400CM's key competencies and the Fund's structure allows it to target longer term opportunities that would not be as appropriate in its flagship hedge fund.

#### **Reperforming Loans**

A key component of the ABTF II strategy will be participation in the Freddie Mac Seasoned Credit Risk Transfer ("SCRT") and Seasoned Loans Structured Transaction ("SLST") programs. These programs are a fundamental part of Freddie Mac's seasoned loan offerings which are intended to reduce its less-liquid assets and transfer credit risk to market participants via economically reasonable transactions. The Fund will typically target first-loss credit tranches, which offers attractive risk-adjusted net yield potential in the mid-teens. 400CM estimates that approximately \$100 billion of outstanding first-loss paper remains on the GSE balance sheets.

SCRT certificates are backed by seasoned RPLs with at least 12 months of nondelinquent current-pay. An SCRT deal will typically include guaranteed senior certificates, non-guaranteed subordinate certificates, interest-only ("IOs"), mortgage insurance, and non-economic residual certificates. 400CM expects that Freddie Mac will complete one SCRT deal per quarter for approximately \$8 billion notional issuance per annum.

SCRT certificates can be attractive due to the unique borrower profile, including seasoned pre-crisis origination, manageable repayment schedules, and embedded value of home price appreciation. Reperforming collateral and home price appreciation typically leads to these certificates trading at attractive levels on the secondary market, giving 400CM a clear exit strategy at attractive prices as other market participants seek to acquire the rights to the securities and their underlying whole loans.



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The Fund may also participate in the Freddie Mac SLST program. SLST securities are backed by loans with less than 12 months of current-pay and moderately delinquent RPLs. Winning bidders in the program have the right to purchase 100% of the subordinate certificates in an SLST securitization. Winning bidders (the "Certificate Holder") commit to retaining the subordinate certificates for three years and have the right to appoint a servicer to work through the servicing and management of the subordinate RPLs. Following the three year period following issuance but prior to the seventh year following the issuance, the Certificate Holder may sell 100% of the retained certificates to a single subsequent purchaser. Certificate Holders may then sell part or all of the certificates to market participants following the seventh year period after issuance.

400 Capital is not affiliated with any special servicers and can hire servicers based on ratings and efficacy. Investment decisions are made purely on an IRR decision basis without consideration for the revenue stream of an in-house servicer. The Fund will utilize two servicers for the SLST portion of the portfolio, SPS Servicing and Fay Servicing ("Fay").

Given the terms of the Fund, it is likely that 400CM would seek to sell its certificates as early as permissible under the program. Similar to the SCRT program, strong demand for reperforming loans on the secondary market offers an attractive exit point for the Fund. Target IRRs for the SCRT and SLST investments are 12%-to-14% net.

### **Specialty Finance**

Specialty finance is the most nimble and opportunistic sleeve of ABTF II and is intended to capitalize on niche opportunities. The Fund's mandate allows it to participate in special government lending programs, niche lending, and residential land banking.

#### *Term Asset-Backed Securities Loan Facility*

On March 23, 2020, the Federal Reserve announced the re-launch of the Term Asset-Backed Securities Loan Facility ("TALF II"). TALF was originally introduced in 2008 and launched in March 2009 as a way to incentivize investments into the ABS market. It accomplished this by offering inexpensive, nonrecourse leverage to qualified investors in order to facilitate the purchase – and in turn the issuance – of high-quality ABS.

Though TALF II presents attractive risk-adjusted return potential, it does not come without key considerations and risks. First, Investors must be mindful of the duration of the opportunity set. Investors in a dedicated TALF II fund may only have a portion of their committed capital put to work if investment grade spreads tighten rapidly and, as a result, lose their attractiveness on a relative value basis compared to the lending terms provided by the Fed. The ability for ABTF II to participate in TALF II without raising a dedicated vehicle offers an attractive alternative for opportunistic investors because committed capital can be used elsewhere if the TALF II opportunity dissipates quickly.

Second, investors should be mindful of a manager's credit underwriting expertise when considering an investment in TALF II. Due to the nonrecourse nature of the lending facility, many market participants are launching TALF-dedicated products. NEPC believes that the government-backed financing will attract some market participants who do not have deep expertise in the structured credit markets. NEPC has confidence in 400CM's ability to perform in-depth, repeatable credit underwriting on ABS across the capital stack.

#### *Residential Lot Banking*

The passage of the *Economic Growth, Regulatory Relief, and Consumer Protection Act of 2018* impaired bank appetite for certain forms of real estate lending, including a decrease in traditional bank lending for acquisition, development, and construction lending. These regulatory changes and the subsequent market impact have allowed asset managers to



## 400 Capital Management

### Asset Based Term Fund II

become liquidity providers in the space, negotiating attractive terms in exchange for funding.

The Firm has established a joint venture to source, service, underwrite, and provide capital to regional homebuilders in high growth markets experiencing demonstrated net migration and observable supply limitations. 400CM's strategic partner, Builder Capital ("BC"), sources homebuilders with limited access to traditional lending but who have track records of delivering similar products through lot bank financing. The team at BC has over 25 years of experience providing over \$1 billion for the acquisition and development of more than 22,000 residential homes.

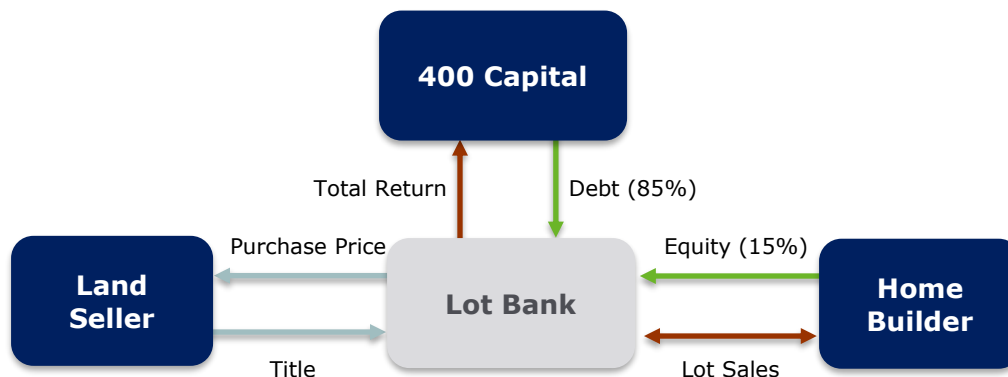
Builder Capital shares in the economics of deals through the life of the process. It receives a 50 basis point origination fee, a 50 basis point servicing fee, and a profit sharing agreement in which it receives 25% of all profits of the joint venture above a 10% hurdle. The Firm has established quality controls and economic alignment of interests to incentivize a beneficial partnership with BC. These include a co-invest structure in which BC is required to commit to a 5% co-investment on all deals; a legal clause holding the partners at BC personally liable for damages subject to "bad acts"; monthly, quarterly, and annual reporting obligations including quarterly third party valuations and annual audits; and a "last out" profit share that ensures the Fund receives payments before BC.

400CM has established contractual, self-amortizing agreements through the lot bank in which homebuilders agree to purchase a predetermined amount of lots at predetermined prices throughout the progress of the projects. A Lot Banking Special Purpose Entity ("SPE") is established with 85% debt financing from 400CM and 15% equity financing from the homebuilder. The SPE concurrently agrees to sell the project to the homebuilder over time pursuant to the agreed upon lot takedown schedule and pricing.

The event of default gives the SPE control of the assets without any extended legal or foreclosure process. For example, if the homebuilder reneges on the purchase schedule, the SPE has no further legal or financial obligation to the homebuilder and can move immediately to sell the asset. Homebuilders do not have an ownership stake in the SPE and 400CM takes full title to the project.

The general structure of the lot bank is as follows:

- (1) Lot bank is capitalized by 400CM debt financing (85%) and home builder equity (15%)
- (2) Lot bank purchases land from the seller and retains the title to the real estate
- (3) Lot bank sells lots to the homebuilder over time



Source: 400CM

## 400 Capital Management

### *Asset Based Term Fund II*

#### **European Bank Deleveraging**

The Fund is expected to participate in European bank deleveraging through regulatory capital relief ("Reg Cap") and nonperforming loans ("NPLs") by purchasing portfolios in partnership with local loan servicers. These transactions are heavily dependent on relationships and typically occur by invitation only or with extremely limited competition. This is due in large part to the bank's preference to prioritize the certainty of deal execution and engage with known or repeat investors.

Regulatory efforts in Europe have encouraged the willingness and ability of European banks to engage in asset sales of their risky balance sheet assets. This has created an attractive market opportunity in which there is a projected €400bn of future asset sales over the next 18-to-24 months, €25 billion of which can be attributed to Portuguese banks. 400CM will seek to acquire nonperforming loans from banks through direct loan sales and bi-lateral or fully syndicated risk transfer transactions.

400CM will target portfolios with high expected recoveries from the residential real estate market. It has targeted Portugal as a priority due to the strong housing recovery, relative strength of the local economy, and short liquidation timelines. To this end, the Firm has developed relationships through its European team with local servicers that provide it with on-the-ground sourcing, due diligence, and on-going servicing, a critical necessity in the European market.

It has also developed strategic relationships with Portuguese bank management, advisors, and asset specialists. 400CM provides speed and certainty of execution to the banks and receive attractive financing terms in return.

#### **Performance: 3**

ABTF II's predecessor fund, ABTF I, a 2017 vintage fund, has achieved a current net multiple of 1.15x and a net IRR of 13.5% just under two years into its life and in a relatively benign structured credit market. This is across 10 deals and all performance to date is unrealized. While ABTF I investments are performing at or above expectations, it is still early in the life of Fund I to definitively categorize performance. The Fund targets a net IRR of 12%-to-15% and a net multiple of 1.5x-to-2.0x.

#### **Products/Pricing: 2**

ABTF II is targeting opportunities in the United States and Western Europe and is expected to invest in 15-to-20 issuers. Investments are expected to range between \$10 million and \$50 million, depending on whether the asset sourced is a single issuer or a portfolio of issuers. It is anticipated that the Fund will recycle interest and principal received during the two-year investment period.

The Strategy represents a natural extension of the team's skillset and experience in structured credit. 400CM has developed a reputation as a prominent player in the structured credit markets, with particular expertise in agency and non-agency residential mortgage backed securities. ABTF II is an extension of the Firm's product offerings, leveraging its relationships with the GSEs, within the residential real estate market, and in Europe to access a thinly-traveled market landscape.

The Fund offers two share classes based on minimum investment. Share Class A charges investors a 1.0% management fee on invested capital with a minimum investment of \$25 million. Share Class B charges investors a 1.5% management fee on invested capital with a minimum investment of \$5 million. 400CM will aggregate NEPC client capital in order to meet the minimum investment size of Share Class A, allowing clients with allocations under the stated minimum to benefit from reduced management fees and carried interest.



## 400 Capital Management

### *Asset Based Term Fund II*

The Fund charges 15% carried interest on Share Class A and 20% on Share Class B. Both share classes offer a preferred return of 6%. The return of capital, the hurdle rate, and the carry are based on the performance at the Fund level. The priority of distributions follows:

- First, 100% to Limited Partners ("LPs") until such LPs receive distributions equal to its funded commitments;
- Second, 100% to LPs until they receive a 6% annual internal rate of return on their capital contributions on drawn commitments;
- Third, 100% to the General Partner ("GP") until carried interest equal 15% (Share Class A) or 20% (Share Class B);
- Thereafter, 85% to LPs and 15% to the GP (Share Class A), or 80% to LPs and 20% to the GP (Share Class B).

400CM will aggregate NEPC client capital in order to meet the minimum investment size of Share Class A, allowing clients with allocations under the stated minimum to benefit from reduced management fees and carried interest.

Other fees may include custody fees, filing fees, system expenses, valuation expenses, and organizational expenses. The investment manager is responsible for office rent, utilities, furniture and fixtures, stationery, administrative services, salaries and bonuses, entertainment expenses, employee insurance, payroll taxes, organizations expenses in excess of \$500,000, and any placement agent fees.

All other expenses are paid by the Fund and include but may not be limited to management fees, legal expenses of the Fund, compliance expenses, up to \$500,000 of expenses in connection with the formation and organization of the Fund, accounting, data services, and other analytical systems.

#### **Key Person Clause**

Messrs. Hentemann, Sanders, Cha, and Leih (the "Principals") are named as key persons for the Firm and Fund. If during the investment period, Mr. Hentemann or two of the three other Principals cease to devote all of their time to the Firm and such time to the Fund as is necessary and appropriate to manage its affairs for a period longer than 60 consecutive calendar days or 90 calendar days on a rolling twelve month basis, a key person event will be triggered.

If a key person event is triggered, the General Partner will notify Limited Partners and the investment period will be suspended for 120 days or until two-thirds of Limited Partners vote to reinstate the investment period.

#### **GP Removal Provisions**

The Fund may be terminated or the General Partner removed by majority approval of the LPs following either a Cause Event or the cessation of the investment period following a Key Person Event.

A Cause Event is defined as either (i) the conviction of a key person for a material violation of U.S. federal securities law or any other law involving the material breach of fiduciary duty; (ii) the conviction of a key person of a felony under any federal or state law; (iii) an action or failure to take an action if such action or failure constitutes gross negligence, willful misconduct, actual fraud, or reckless disregard for such person's duties to the Fund; or (iv) a material breach of any covenant, agreement, representation or warranty contained in the Partnership Agreement.

LPs may designate an alternative liquidator if they have acted to terminate the Fund, have removed the GP, or if no GP remains.



## 400 Capital Management

### Asset Based Term Fund II

Due Diligence Process	
<b>How was this fund sourced?</b>	<p>NEPC has an established relationship with 400 Capital through the Firm's flagship hedge fund, the Credit Opportunities Fund ("COF"), a 1-rated product on the Hedge Fund FPL. COF was added to the FPL in MMM, 2013.</p> <p>400CM partnered with another firm for the bulk of the assets in ABTF I due to its smaller size. NEPC Research expressed interest in participating in ABTF II and secured up to \$100 million in aggregate client capacity in the Fund.</p>
<b>Please describe the level of due diligence completed?</b>	<p>NEPC has held several meetings with 400CM focused on ABTF II, both in person and on the phone. Case studies and marketing materials were provided by 400CM and reviewed by NEPC, along with a separate RFI and data requests that were completed at NEPC's request.</p> <p>In addition to reviewing materials provided by 400CM, NEPC conducted research of third party data and market studies to gain comfort with the GSE programs and joint ventures utilized by the strategy.</p>
<b>Date of Team Vetting / Revisit</b>	January 6, 2020 / April 27, 2020



## 400 Capital Management

### Asset Based Term Fund II

Key Fund Terms & Attributes – Private Markets	
<b>Target / Max Fund Size</b>	\$400 million / \$500 million hard-cap
<b>Minimum Investment</b>	Series A: \$25 million, subject to GP discretion Series B: \$5 million, subject to GP discretion
<b>GP Commitment</b>	1.0%
<b>Target Final Close</b>	June 20, 2020
<b>Investment Period</b>	Two years from Fund’s final closing date
<b>Fund Term</b>	Five years from the final closing date with two one-year extensions; One at the discretion of the GP, one at the discretion of the LP
<b>Target Fund Return</b>	12%-to-15% net IRR with a 1.5x-to-2.0x net multiple
<b>Leverage</b>	400CM may seek warehouse financing to aggregate assets to pool assets into a rated vehicle for takeout through securitization
<b>Management Fee</b>	Series A 1.0% on Invested Capital Series B 1.5% on Invested Capital
<b>Carried Interest</b>	Series A: 15.0% Series B: 20.0%
<b>Preferred Return</b>	6.0%
<b>Distribution Waterfall</b>	(i) 100% to LP until LP has received distributions equal to its funded commitments; (ii) 100% to LP until LP has received distributions equal to a 6% annual compounded IRR on its funded commitments (the “Preferred Return”); (iii) 100% to the GP until the GP has received distributions equal to 15%/20% of the sum of all amounts distributed to LPs, and; (iv) thereafter, 85%/80% to the LP, 15%/20% to the GP (the “Carried Interest”)
<b>Other Fees</b>	Fund covers certain expenses up to \$500,000
<b>Fund Auditor</b>	KPMG LLP
<b>Fund Legal Counsel</b>	Onshore: Akin Gump Strauss Hauer & Feld LLP Offshore: Ogier



### Disclaimers and Disclosures

- Past performance is no guarantee of future results.
- The opinions presented herein represent the good faith views of NEPC as of the date of this report and are subject to change at any time.
- Information on market indices was provided by sources external to NEPC, and other data used to prepare this report was obtained directly from the investment manager(s). While NEPC has exercised reasonable professional care in preparing this report, we cannot guarantee the accuracy of all source information contained within.
- This report may contain confidential or proprietary information and may not be copied or redistributed to any party not legally entitled to receive it.

In addition, it is important that investors understand the following characteristics of non-traditional investment strategies including hedge funds, real estate and private equity:

1. Performance can be volatile and investors could lose all or a substantial portion of their investment
2. Leverage and other speculative practices may increase the risk of loss
3. Past performance may be revised due to the revaluation of investments
4. These investments can be illiquid, and investors may be subject to lock-ups or lengthy redemption terms
5. A secondary market may not be available for all funds, and any sales that occur may take place at a discount to value
6. These funds are not subject to the same regulatory requirements as registered investment vehicles
7. Managers may not be required to provide periodic pricing or valuation information to investors
8. These funds may have complex tax structures and delays in distributing important tax information
9. These funds often charge high fees
10. Investment agreements often give the manager authority to trade in securities, markets or currencies that are not within the manager's realm of expertise or contemplated investment strategy