

Arizona PSPRS sees benefits to playing VC lottery

The Phoenix pension fund also plans to expand its co-investment program from 10 to 20 percent.

By Rebecca Szkutak - 22 November 2019



The Arizona Public Safety Personnel Retirement System is remodeling its investment buckets. The reorganization won't change its venture strategy, but the nature of the asset class already is changed.

The Phoenix pension fund is currently creating a private markets allotment that will encompass private equity, real estate and real assets. The strategy shift also includes plans to expand its co-investment program from 10 percent to 20 percent.

While this portfolio infrastructure shift won't impact the amount of money going to venture, Mark Steed, the chief investment officer of the APSPRS, said that change is coming to the venture strategy.

The pension's venture platform will continue to make up 15 percent to 20 percent of the private equity portion of the private markets distribution, which equates to 3 percent to 5 percent of the more than \$10.5 billion pension fund.

"I do think we will fundamentally approach venture differently going forward than we have in the past, but that's not driven by asset allocation. That's just driven by what's going on in venture," Steed said.

Steed elaborated that while their current portfolio has performed well compared to market standards and peers, they will take a closer look at diversification and what positive changes the fund can make in that direction.



“Venture might be the only asset class where diversification helps,” Steed said. “Venture follows a power law distribution, which means that there are a few winners that drive a lot of the returns. If you are being selective you better hope that you pick that handful of winners.”

He added that a lot of people say that if you can’t access certain managers you shouldn’t be investing in venture, but he doesn’t agree and says it may work better to be less selective.

“You want to be diversified because effectively the cost of the lottery tickets is less than the payout,” Steed said. “If you had a lottery where you bought all the tickets, and the payout is more than the cost of the tickets, which isn’t how it is supposed to go, you would play that game all day long because you would have a positive outcome.”

The pension invests across stages and across geographies with notable exposure to the Asian market.

“We are trying to access that global investment premium for early-stage venture so we will select relationships that best work with that,” Steed said.

APSPRS typically targets investment sizes that range from \$5 million to \$30 million in size on average, but sometimes larger. The pension fund also deploys capital through co-investments. Steed said roughly a third of the fund’s venture commitments are through co-investments. The fund’s co-investments range from \$1 million to \$15 million in size.

Steed said the pension doesn't favor investing in particular industries because the good investment opportunities in venture are changing. He looks for firms that are more focused on what's new and up-and-coming and not making too many repeat investments into the same area.

He added that the key is making sure to work with the right managers to have a good chance to be successful regardless of industry or trend.

"It's really difficult to see trends coming because venture, almost by definition, creates things that have never existed before," Steed said.

Recent commitments from the pension plan include a \$50 million commitment to Trustbridge Partners VI, which invests in early-stage companies, including consumer and media, and is managed by Shanghai-based Trustbridge Partners.

The fund also made an \$50 million commitment to Vivo Capital Fund IX, with an additional \$20 million commitment for co-investment opportunities. Vivo Capital in Palo Alto invests in healthcare startups.

"There are lots of ways to lose money in venture and you've got to find the right partner. A great operator who can add value, who is fishing in the right pond," Steed said. "My prediction is if you work with people like that, and are aligned, you have good reasons to be optimistic."

The pension's private equity portfolio saw a return of 11.36 percent in the fiscal year ending in June 2018, which ranked it fifth among public pensions in the United States, according to the 2019 yearly American Investment Council public pension study.

The pension was also ranked 92nd in a list of the top venture capital limited partners by Preqin.

LP Info

Arizona Public Safety Personnel Retirement System

Website: <https://www.psprs.com>

Description: Public pension fund

Location: Phoenix, Arizona

Phone: (602) 255-5575

CIO: Mark Steed

Total AUM: \$10.5 billion

Venture allocation: 3% to 5%

Typical commitment size: \$5 million to \$30 million

Recent commitments: \$50 million commitment to Trustbridge Partners VI and \$50 million to Vivo Capital Fund IX

Geographic preference: Global