



COMMONWEALTH OF PENNSYLVANIA
PUBLIC SCHOOL EMPLOYEES' RETIREMENT SYSTEM

Public Investment Memorandum

**Santé Health Ventures III, L.P.
& Santé Health Ventures IV, L.P.**

Private Equity Fund Commitment

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Senior Investment Professional, Private Markets

December 19, 2018



Recommendation:

Staff, together with Hamilton Lane Advisors, L.L.C. ("Hamilton Lane"), recommends to the Board a commitment of up to \$75 million to Santé Health Ventures III, L.P. ("SHV III" or the "Fund") and up to \$75 million to Santé Health Ventures IV, L.P.

Founded in 2006 and based in Austin, TX, Santé Ventures ("Santé" or the "Firm") is forming the Fund to continue its strategy of making early stage venture investments within the healthcare sector.

Firm Overview:

Joe Cunningham, M.D., Douglas French, and Kevin Lalande originally came together to form the healthcare ventures practice at Austin Ventures. Although their time at Austin Ventures was successful, they ultimately concluded that their niche strategy was best executed on a standalone basis and spun out, with the blessing of Austin Ventures management, in 2006. They are now raising their third fund since then and have invested approximately \$220 million as Santé Ventures.

The Firm currently has 18 total employees based in two Texas offices, a main office in Austin and a satellite office in Houston. Nine investors are focused on healthcare venture. Notably seven of these nine team members have substantial experience in both venture investing and healthcare industry/practice resulting in a top heavy, senior team executing a hands on process. The internal investment team is supplemented by a Strategic Advisory Council made up of 50 individuals possessing subject matter expertise in a wide range of medical specialties and healthcare disciplines.

Fund Size & Commitment:

Fund III is seeking equity commitments of up to \$200 million, with a hard cap of \$250 million which PSERS staff believe will be hit. Together with two prior funds this will bring total commitments to approximately \$521 million. The GP is targeting internal commitment at 3% or \$7.5mm.

Investment Strategy:

Consistent with their first two funds, Santé seeks to make early stage investments exclusively in the healthcare sector, but diversified across sub-sectors (Biopharma, Services & IT, and Medtech), clinical indications, and end markets. Generally the Fund will invest \$500,000 to \$5 million per round in preferred or convertible preferred securities, often structured around multiple, milestone-based tranches at fixed valuations to manage downside risk. With these check sizes they are targeting typical ownership of 20%+ of each portfolio company. The intention is always to maintain sufficient equity reserves to continue to invest in subsequent rounds over a company's lifecycle in order to maintain/defend the Fund's ownership percentage.

Santé intends to invest a substantial portion of capital in companies based in or science and technology generated in Texas and the Central U.S. Although the West and East Coasts (particularly the San Francisco Bay area and Boston) account for the majority of venture dollars invested, they are well covered and highly competitive markets. In contrast, Texas is also richly endowed with world-class healthcare infrastructure (2nd in number of medical schools, 3rd in number of ongoing clinical trials, 3rd in total life science expenditures) yet has historically lacked dedicated healthcare venture capital. This geographic void presents opportunity for advantaged deal flow and investment terms.



Investment Team:

Santé has assembled a single-purpose, multi-disciplinary team possessing deep experience both as individuals and now as a collective, having successfully executed two prior funds.

Managing Director – Kevin M. Lalande (45) Prior to co-founding Santé Ventures in 2006, Kevin spent seven years with Austin Ventures, a prominent venture capital firm with \$4 billion under management. Before joining Austin Ventures, he was a management consultant with McKinsey & Company, where he served U.S. and European clients in the telecom and computer industries. He is also an accomplished entrepreneur, having co-founded, built, and sold three Internet-based startup companies: NetProfit, sold to a privately held advertising agency in 1996; Serus, sold to Netopia (Nasdaq: NTPA) in 1998; and TimeMarker, sold to PrimeHoldings (OTCBB: PRIM) in 2001. Kevin received a BS in Electrical and Computer Engineering with honors and an MBA from the Harvard Business School with highest distinction (Baker Scholar & Siebel Scholar).

Managing Director – Joe Cunningham, MD, MBA (58) Prior to co-founding Santé Ventures in 2006, Joe was most recently a co-founder of JD Resources, a healthcare strategic advisory and private equity firm. He is the former Vice Chair of the Ascension Health Ventures investment committee. He is also the former Chief Medical Officer of the Providence Health System and Executive Director of the 300-physician Providence Health Alliance, both of which belong to Ascension Health. Joe formerly served on the Board of Trustees of the Texas Medical Association and currently serves on the Medical Advisory Boards of both Health Care Service Corporation (Blue Cross Blue Shield) and the United Health Group, two of the largest insurers in the country. He has extensive management experience and has held numerous leadership positions in medicine. He is recognized nationally for his expertise in healthcare delivery systems, physician associations and compensation models. He is board certified in both Internal Medicine and Quality Assurance and Peer Review.

Managing Director – Douglas D. French, MHA (63) Prior to co-founding Santé Ventures in 2006, Doug was most recently a co-founder of JD Resources, LLC and is the past President and Chief Executive Officer of Ascension Health and the creator of Ascension Health Ventures. With more than 30 years of experience in the field of healthcare and a vast network of relationships, he is one of the most respected and recognized leaders in the industry. He is known as an innovative and creative leader, a successful risk taker, and superb developer of people and organizations. Doug serves on the Boards of Herman Miller, Inc. and four privately held companies. He is also a prior Board member of Ascension Health, Catholic Healthcare West and the Catholic Healthcare Association, MedAssets, Accuro and Emageon.

Partner – James Eadie, MD MBA (45) James received his MD from Harvard Medical School, an MBA from the University of Texas McCombs School of Business, and a BS in bioengineering, summa cum laude, from the University of Michigan. He is board certified in emergency medicine and completed his residency at Massachusetts General Hospital and Brigham and Women's Hospital. Previously, James served in the Air Force and was the medical director and Vice-Chair of Emergency Medicine at Wilford Hall Medical Center, an academic level-one trauma center in San Antonio. He completed two tours in Iraq as a critical care transport team chief and as the emergency department commander. He separated honorably as a Major in 2008.

Chief Scientific Officer – Casey Cunningham, MD (61) Casey Cunningham, MD is the Chief Scientific Officer of Santé Ventures and has served as the acting Chief Medical Officer for several Santé portfolio companies, including Terapio, Molecular Templates (Nasdaq: MTEM) and BetaCat Pharma. Dr. Cunningham was fellowship trained in oncology and hematology at Harvard Medical School, where he subsequently served on the faculty for 8 years. He was also one of the founding members of the Division of Experimental Medicine at the Brigham & Women's Hospital in Boston, where he established a basic research laboratory in Cell and Molecular Biology. Casey returned to Texas in 1999 as the Associate Director of the Mary Crowley Cancer Research Center in Dallas, a position he held until 2007. The MCCRC performs early phase drug development, and Casey was the principal investigator on numerous



trials, with a particular emphasis on gene and cell-based therapies. He has over 60 publications in peer-reviewed journals.

Venture Partner (Partner in SHV3) – Louis Bock (52) Lou joined Santé Ventures as Venture Partner in 2014. Prior to Santé, Lou was a Partner and Co-Founder of Scale Venture Partners from 1997-2014. He was a member of the healthcare team and built the firm's biotech practice. Lou joined Scale in 1997 from Gilead Sciences, where he held positions in research, project management, business development and sales. Prior to Gilead, he was a research associate at Genentech. Lou has been involved with life science companies that have completed 8 IPOs and 4 acquisitions. The current public companies have a market cap in excess of \$6 billion. Lou holds an M.B.A. in finance from California State University, San Francisco and a B.S. in Biology from California State University.

Venture Partner – William “Billy” Cohn, MD (56) Billy is a cardiovascular surgeon and the Director of Minimally Invasive Surgical Technology at the Texas Heart Institute at St. Luke's Episcopal Hospital in Houston, Texas. He is the co-director of the Cullen Cardiovascular Research Laboratory and an Associate Professor of Surgery at Baylor College of Medicine and Adjunct Professor of Bioengineering at The University of Houston. Billy received his undergraduate degree from Oberlin College, and received his medical degree from Baylor College of Medicine, where he remained for general surgical and cardiothoracic surgical residency training and where he served as the last chief resident under the legendary Michael DeBakey. After graduation, he took a teaching position at Harvard Medical School where he rose to the rank of Associate Professor of Surgery and served as an attending cardiothoracic surgeon and Director of Minimally Invasive Surgery at the Beth Israel Deaconess Medical Center for eleven years. Billy has more than 60 United States patents awarded or pending for his medical innovations and has been honored as the Distinguished Inventor of the Year by the Intellectual Property Owners Association. He has published extensively in peer reviewed journals, has authored seven textbook chapters, and serves on the editorial board of the Heart Surgery Forum, Innovations, and CTS Net.

Senior Associate – Derek Mazur (27) Derek joined Santé Ventures in 2014. Prior to joining the firm, he was as a Financial Analyst at Houlihan Lokey in their Healthcare Mergers & Acquisitions practice based in Chicago. Before Houlihan, Derek was an Investment Banking Analyst at SunTrust Robinson Humphrey based in Atlanta, where he focused on a variety of syndicated & leveraged finance, capital markets, and financial advisory engagements. In 2017, he began pursuit of a Masters of Science in Biotechnology at Johns Hopkins University. Derek graduated from Emory University with a B.B.A. in Finance.

Market Opportunity:

At \$3.5 trillion¹, healthcare is an enormous portion of the U.S. economy and large enough to represent the 5th largest economy in the world². In addition to sheer size, healthcare in the US continues to undergo significant changes in the wake of the Affordable Care Act and the system moving from a fee-for-service to value-based reimbursement model while technological shifts, changing consumer preferences, and new entrants from the tech world (Amazon, Apple) present disruptive forces. All of this combines to create a market that is scientifically complicated, highly regulated, and undergoing significant change, thus requiring specialized knowledge, experience, and networks to make successful investments.

The last decade has been a prolific one for healthcare venture investment. According to Pitchbook's Q3 2018 NVCA Monitor, 2018 has been a banner year with deal value and number of deals on pace to be the highest of the decade with valuations increasing alongside. Underlying this, is a tale of two cities with

¹ "NHE-Fact-Sheet." *CMS.gov Centers for Medicare & Medicaid Services*, 6 Dec. 2018, www.cms.gov/research-statistics-data-and-systems/statistics-trends-and-reports/nationalhealthexpenddata/nhe-fact-sheet.html.

² Smith, R. (2018, April 18). The world's biggest economies in 2018. Retrieved from <https://www.weforum.org/agenda/2018/04/the-worlds-biggest-economies-in-2018/>



biopharma, particularly oncology related, attracting significant increases in capital while medical device investment is down year over year. Overall, despite rising pre-money valuations and check sizes, just over 30% of healthcare Series A deals in 2018 have had a pre-money of > \$20mm, leaving a substantial pool of deals which fit Santé's model.

Investment Highlights:

- Unique and experienced team with a multidisciplinary background
- Entrepreneurial investment style
- Respect for the mathematics of venture investment
- Tranche investments to manage downside risk and optimize IRR
- Reduced blind pool risk with two investments already committed
- Unique structure and fees

Investment/Risk Considerations:

- Early stage company risk
- Scientific risk
- Sector focus
- Competition

PSERS History & Performance:

PSERS does not have prior history with the Firm.

Portfolio Fit:

A commitment to Santé Health Ventures III will give PSERS' Private Markets portfolio, specifically in the venture capital space, exposure to the healthcare industry. The Fund represents the first investment in early stage healthcare venture in some time and is a potentially valuable diversifier both to the overall portfolio and existing healthcare exposure which is predominately focused on operating businesses and/or public equities. A commitment to Santé Health Ventures III will be allocated to the Venture Capital sleeve of PSERS' Private Markets portfolio. The table below summarizes PSERS Private Equity exposure as of June 30, 2018 (in millions):

Investment Type	Active Commitments ¹	%	Market Value	%	Unfunded ¹	%	Total Exposure ¹	%
Private Equity	\$ 15,775.2	67.3%	\$ 5,077.5	64.8%	\$ 3,764.6	73.6%	\$ 9,285.5	68.5%
Special Situations	4,231.5	18.2%	1,187.8	15.1%	709.0	13.9%	2,040.9	15.1%
Venture Capital	2,791.9	12.0%	1,004.5	12.8%	538.5	10.5%	1,570.9	11.6%
PE Internal	602.5	2.6%	564.7	7.2%	102.0	2.0%	654.4	4.8%
Total	\$ 23,401.1	100.0%	\$ 7,834.6	100.0%	\$ 5,114.1	100.0%	\$ 13,551.7	100.0%

(1) As of June 30, 2018. Includes post Q1'2018 pending/closed commitments.



Investment Committee Disclosure:

Relationship with Hamilton Lane:	None other than current due diligence project
Placement Agent:	There is no placement agent associated with or compensated for PSERS' investment. Far Hills Group is involved in allocations from LPs other than PSERS.
Source	PSERS investment office
PA Political Contributions:	None
PA Presence:	None
Conflicts:	None Disclosed
History with PSERS:	None
PSERS AIC Meeting Approval:	December 19, 2018

Oversight Responsibility:

Investment Office:	Charles J. Spiller Deputy CIO, Non-Traditional Investments Darren C. Foreman, CAIA Senior Manager, Private Markets Patrick G. Knapp Senior Investment Professional, Private Markets
External Consultant:	Hamilton Lane



Hamilton Lane

December 19, 2018

Board of Trustees
Commonwealth of Pennsylvania
Public School Employees' Retirement System
5 North 5th Street
Harrisburg, PA 17101

Re: Santé Health Ventures III, LP

Dear Trustees:

Santé Ventures ("Santé") was founded in 2006 by Doug French, Joe Cunningham and Kevin Lalande, all of whom continue to maintain broad oversight of firm management, deal sourcing, due diligence, monitoring and value creation. Santé has a well-tenured and growing investment team composed of professionals with extensive experience investing and operating in the healthcare space, with an average of 23 years in the industry; 50% of the investment team possesses medical doctorates, and have meaningful experience as practicing physicians. The investment team is comprised of 3 managing directors and 6 other dedicated investment professionals; the investment team is augmented by 5 data scientists and 4 operations and management professionals. Additionally, Santé benefits from two Venture Partners and 63 Strategic Advisory Council ("SAC") members, who leverage their positions at leading healthcare institutions and extensive personal networks to help provide Santé unique access to de-novo and early-stage deal flow. Deal teams are composed of any number of the managing directors and may be supported by Casey Cunningham, Chief Scientific Officer, who leverages his medical and science background to diligence opportunities and lead select portfolio companies. The General Partner promotes strong alignment of interests through broad distribution of economics; carried interest is distributed across the investment team down to the senior associate-level. Santé is targeting \$200 million in commitments for its third seed and early-stage venture capital fund, Santé Health Ventures III, LP (the "Fund"). Santé expects to hold a final close in March 2019. The General Partner will commit at least 2% of commitments to invest in the Fund.

Consistent with the General Partner's prior funds, the Fund will target investments in life sciences businesses with novel solutions to unmet medical needs. Santé primarily seeks to invest in seed- and early-stage businesses that are generally headquartered in Texas and California; the General Partner expects to allocate approximately 70% of the Fund to businesses that are based in Texas or California, and the remaining 30% of the Fund opportunistically across the United States. Santé expects to allocate a meaningful portion of the Fund to seed-stage, de-novo healthcare ventures, which are built around acquired intellectual property. The investment team's extensive industry networks and established track record position Santé as a preferred partner to founders, driving sustainable deal flow; additionally, the General Partner leverages its two Venture Partners and 63 SAC members to source unique opportunities. Post-investment, Santé leverages its in-house domain expertise to drive hands-on value creation, through meaningful ownership positions and board representation. The General Partner strategically acquires substantial ownership positions in portfolio companies through tranching investments, which limits downside and drives the potential to return the entire Fund in an average exit scenario. The Fund will target 18 to 20 equity investments in the range of \$6 million to \$12 million. While the General Partner has generated mixed net performance across prior funds, significant additional upside is expected in Fund I; additionally, Fund II has generated strong, top quartile performance on a net IRR and multiple basis.

Santé Health Ventures III's investment thesis can be summarized as follows:

- Santé has a cohesive, growing investment team with deep domain expertise



Hamilton Lane

- Targeted sector and regional approach produces unique access to de-novo and early-stage opportunities
- Additional significant upside expected in Funds I and II, and shifting focus to deployment pacing and hold duration

Hamilton Lane's recommendation is based upon the following analytical factors and is made within the context of Commonwealth of Pennsylvania, Public School Employees' Retirement System's ("PSERS") investment guidelines.

- Detailed due diligence, including interviews with industry peers and private equity professionals. The initial review was completed September 26, 2018; the on-site due diligence was conducted December 11, 2018; the Fund was approved by Hamilton Lane's Investment Committee on December 17, 2018 and the recommendation to PSERS was issued December 19, 2018.
- Evaluation of the composition of the investment team, how they work together, compensation structure and other factors that help determine whether a group is likely to be able to replicate past successes as currently configured.
- Detailed Operational Due Diligence, including interviews with Santé's back office team to review the controls and processes surrounding the firm's finance, fund administration, tax, legal, compliance, IT, HR, and accounting functions.
- Evaluation of the Fund's proposed investment strategy within the context of the current investment environment.
- The strategy proposed for the Fund is appropriate for the Private Equity Partnership component of the portfolio.

The individuals at Hamilton Lane who were involved in the due diligence process for the Fund are:

Miguel Luina – Principal, San Francisco Office
Jacob Fertell, Analyst, Bala Cynwyd Office

Based on the above, Hamilton Lane recommends that PSERS commit up to \$150 million, split up to \$75 million to Santé Health Ventures III, LP and \$75 million to Santé Health Ventures IV, LP. The pre-commitment of \$75 million to Santé Health Ventures IV, LP will be subject to certain hurdles and legal negotiations. Hamilton Lane makes this recommendation considering the General Partner's qualifications and PSERS' overall investment guidelines.

This recommendation is given solely for the benefit of PSERS and cannot be relied upon by other investors, considering an investment in the Fund, since their needs, objectives and circumstances may not be identical to those of PSERS. The scope of this recommendation is limited to the investment merits of the Fund. Hamilton Lane does not provide legal or other non-investment-related advice.

Sincerely,

Michael Koenig,
Chief Client Officer

Corina English,
Principal