To: Ventura County Employees' Retirement Association

From: NEPC Consulting Team

Date: April 28, 2025

Subject: VWH Partners IV (Private Credit)

Recommendation

NEPC and VCERA's CIO recommend that the Board of the Ventura County Employees' Retirement Association ("VCERA" or the "Plan") approve an additional commitment of $25 million to VWH Capital Management ("VWH," the "Manager," the "Firm")'s VWH Partners Fund IV (the "Fund," or "Fund IV"). This would raise VCERA's commitment from $75 million to $100 million.

NEPC views the Fund as a suitable investment that is additive to VCERA's private credit portfolio. The Fund has been rated "1" by NEPC's Private Investment Committee, indicating strong conviction in VWH's investment thesis and ability to execute.

In 2022, VCERA committed $50 million to VWH Partners III which had been rated "1" by the Private Investment Committee. Through September 30, 2024, VWH Partners III has generated a net internal rate of return ("IRR") of 20.6% with approximately $26 million invested.

NEPC and VCERA's CIO believe that VWH Partners Fund IV continues to fit well in VCERA's Private Credit allocation for the following reasons:

- **Rising NPL (non-performing loan) Supply:** GSEs (government sponsored enterprises) began auctioning NPLs in 2014 and 2015 in small volume, $700 million and $7.5 billion respectively. Sale volume continues to increase since then and included approximately $7 billion in sales in 2020. The federal mandate for the GSEs to reduce its footprint in the market is one that transcends political regime change. Currently, distressed mortgage inventory including the GSEs and HUD (Housing and Urban Development Department) represent roughly ~ $85 billion. The sharp increase in opportunity set is represented by HUD, which recently proposed transitioning its existing NPL sales initiatives into a permanent program in which it would sell NPLs to private investors. As a result of the augmented opportunity set, we believe the targeted fundraise of $1.25 billion is reasonable.
- **Experienced CIO:** Vivien Huang has more than two decades of experience in the mortgage industry. Most recently, prior to founding VWH, she served as the Head of Structured Mortgage Products at JPMorgan. There, she managed a $45 billion portfolio focused on agency mortgage-backed securities and a $300 million portfolio of RMBS (residential mortgage-backed securities), CMBS (commercial mortgage-backed securities), and agency MBS (mortgage-backed securities). Prior to JPM, she was a managing director at Goldman Sachs, also focused on agency mortgages. She was the first mainland Chinese born female promoted to managing director at Goldman Sachs North America.
- **Access to less-competitively bid auctions:** As a MWBE (minority and women-owned business enterprises), the Fund will have access to smaller, less competitively bid pools. Fannie Mae issues Community Impact Pools (CIP) and Freddie Mac issues Extended Timeline Pool Offerings (EXPO). Both CIP and EXPO are offered exclusively to MWBEs and not-for-profits. Since late 2014, when the GSEs started NPL offerings, there have only been two winning bidders (and only

one repeat bidder) in the CIP and EXPO programs. These programs account for a small percentage of total offerings but are mandated to grow commensurate with demand. That said, these pools are smaller in size and, considering that VWH is raising an amount greater than $1 billion, VWH will need to also rely on broadly available auctions, which they have also experienced success in (largest buyer of NPLs since 2020 from GSEs).

- **Capital Market Proficiency:** VWH has issued 9 securitization deals backed by $3.1 billion NPLs which have attracted the interest of large institutional pools of capital. VWH's securitization shelf has historically been oversubscribed and has exhibited strong performance versus peers. Securitization for VWH is used as a financing mechanism for the portfolio, in which the senior and mezzanine tranches are sold to institutional investors, with VWH retaining the equity tranche (60%-90% of the NPL financed, allowing for further investment in additional NPL pools). In this structure, VWH gets permanent financing without mark-to market volatility that could trigger margin calls, which would allow the Fund to remain opportunistic during market dislocation. The CIO is incredibly versed in US securitized products from beginning her career at Freddie Mac, to team and system build-outs at Goldman Sachs and JPMorgan. She has the network, contacts, and trading partners to create and sell securitized notes in the primary market.
- **Independent Servicing:** VWH is not affiliated with any special servicers, and as such, it 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 (no conflict of interest). Additionally, by having multiple servicers there is less chance of regulatory risk versus having one single servicing partner. Furthermore, many of these special servicer partners have a significant presence in Dallas, which allows for closer communication and supervision as it relates to loss mitigation waterfalls.

Overview of Ventura Private Credit Program (PC)

As of March 31, 2025, VCERA has committed $1,230 million to Private Credit with approximately $700 million invested, compromising 8.2% of total plan assets.

Through September 30, 2024, the Private Credit allocation has generated a net IRR of 10.66% per annum with a Total Value to Paid-In Capital (TVPI) ratio of 1.28x. Results have been achieved through a broad mix of Direct Lending, Real Estate, Distressed and Opportunistic Lending strategies.

Fund Overview

VWH Capital Management is a Dallas-based asset management firm specializing in asset-backed structured products. The Firm was founded by Vivien Huang in 2014 as an investment management firm focused on capitalizing on dislocations in the structured credit market. This includes investments in non-performing, sub-performing and re-performing and newly originated US residential and credit-linked assets. The Firm manages roughly $4 billion across three private credit funds. VWH moved its headquarters from New York, NY to Dallas, Texas in 2023 to better attract talent and be closer to its servicing partners. Since the prior fundraise (Fund III), VWH has grown the team from 13 to 27 professionals. VWH now employs seven professionals on the investment side, ten on the asset management side and ten within non-investment and back-office roles. As a result of the sharp growth in headcount, there has been a healthy amount of turnover among new hires. However, there have been no departures from the investment team recently.

VWH is currently raising VWH Partners Fund IV targeting $1.25 billion in aggregate capital commitments. The Firm has begun marketing the Fund in Q4 2024 and is expecting a final close date of Q4 2025 or Q1 2026. Fund IV will have a 3-year investment period from the final closing and a 3-year harvest period, with the option of up to two, 1-year extensions. This Fund life is shorter than typical private credit funds, as the expected fund term is expected to be 6 years. The Fund is targeting a net IRR of 15%+ with a net equity multiple on invested capital of ~1.5x.

The Fund will target NPLs through public auctions offered by GSEs. VWH will participate in both broadly available auction pools as well as parallel auction programs held exclusively for MWBE and non-for-profit organizations and community groups, which offer a strong advantage to source opportunities. Given the limited number of participants in some of these auctions which are available to VWH, the clearing prices of these less-competitively-bid pools are typically lower than broader auction pools. VWH's portfolio will comprise a mix of both large and small, broadly offered loan pools as well as MWBE-specific loan pools. These loan pools will be purchased at a meaningful discount to par value, loan servicing rights will be transferred to a third-party servicer chosen by the Fund, and loan pools will be aggregated for the purposes of securitization. If successful in securitization, VWH will retain the subordinate tranche(s) and sell- off senior and mezzanine tranches for further investment in NPL pools. Over the fund term, VWH will look to manage these non-performing loans and restructure them into a re-performing asset. In addition to the core focus, the Fund will participate in opportunistic investments such as "Fix-n-Flip" on NPLs turned to real estate (REO – real estate owned) and may engage in tactical purchases in mortgage and other credit-related assets.

Overall, performance across the three vintages has been strong, given market conditions and is trending more positively with each vintage. Fund I and Fund II are currently harvesting, while Fund III is still in its investment period, however it has largely wrapped up its capital deployment, as it has called 80% of commitments, and has already returned 33% of called capital as of September 2024. Fund III is a 2022 vintage that has produced a 20.8% net IRR and 1.25x net MOIC, with a 0.34x DPI, performing exceptionally well at a size that will be similar to Fund IV. The Fund was able to take advantage of dislocation caused by rapidly rising rates and spread widening in 2H2022 and subsequent tightening in 2024. Fund I (2018 vintage) has a net IRR of roughly 10.2%, which is below target, partially owing to the COVID pandemic which resulted in GSEs suspending their NPL auctions until late 2021, which coincided with Fund I's investment period, causing significant delays in capital deployment and delays in liquidation timelines, which is crucial to IRR calculations. Fund II was a 2022 vintage that raised roughly $255 million in capital commitments (fund-of- one) structure which has produced a 12.0% net IRR through 2H2024. This fund was also similarly impacted by factors affecting Fund I, and experienced markdowns from rising rates in 2022 on the existing portfolio, which saw the value of modified mortgages (new mortgage terms made at the then market rates) to be marked down.

In this vintage, the Fund will likely have a more favorable investing environment, as Residential NPLs are countercyclical investment assets. Mortgage delinquencies typically rise with higher unemployment rates, which results in a larger potential supply of NPLs. If unemployment rates rise, more borrowers will likely fall behind on their mortgage obligations. VWH typically looks to avoid foreclosures in these pools, as the Fund would prefer to get existing non-performing mortgage loans to re-performing status in order to realize greater returns on the secondary market. Market conditions appear to be favorable as the housing supply has remained tight, in which, borrowers have been benefitting from lower mortgage rates versus current market rates. Lastly, the Housing and Urban Development Department (HUD) has reinitiated its program to sell NPLs, as a permanent program, as of December 2024. This represents a substantial, and previously untapped opportunity to bid on roughly $51 billion of additional distressed mortgage inventory, making it larger than the amount of NPLs held by the GSEs and Freddie Mac combined (GSEs $20 billion, Freddie Mac $15.5 billion).

This is a niche opportunistic strategy in which the return drivers are driven by US housing market dynamics and the servicing ability of acquired loan portfolios. Given the niche focus, Fund IV would serve as both a diversifier and a return-seeking allocation within VCERA's broader private credit allocation.

VCERA should consider the following risks associated with the Fund:

- **Extension Risk:** The liquidation timeline is key to realizing an attractive IRR. Extension of loan modifications and foreclosure due to issues with servicing or legal proceedings can reduce the overall returns to investors. VWH hand selects servicers based solely on ability to service each pool; it also models out each loan with zip code level projections and builds timeline extension scenarios into its bidding models.
- **Key Person Risk:** Ms. Huang is the key person for the Fund. If she ceases to be involved in the day-to- day management of the strategy, NEPC would not be comfortable recommending this product. Should she be incapacitated or otherwise unable or unwilling to participate in the day-to-day management of the Fund, the investment period will be automatically suspended. The investment period will not resume until a qualified replacement is made. If the Key Person Event is not cured or waived within 180 days, the investment period will be terminated
- **Political Risk:** There is a potential for MWBE offerings to be deemphasized across the GSEs. However, this has not been an announced policy agenda item for the incoming administration. The risk that this occurs during the investment period of the Fund seems low; however, if it were to occur, Ms. Huang could still participate freely in the broadly available auctions, in which the Firm has also experienced success. As VWH has established itself in the market as one of the largest buyers of NPLs (and as competition has thinned out since the GFC), VWH has become less dependent on CIP/EXPO pools to gain exposure.
- **Mark-to-Model Risk:** The portfolio is largely marked-to-model on a quarterly basis with an independent audit performed annually. The Fund will use current and historical market information to determine the fair market value of its assets. Every six months, the Fund secures an independent broker price opinion (BPO) on every property in the portfolio. This is used in monitoring and valuation processes for the Fund and unrealized gains and losses are taken into consideration when determining the fair market value, and VWH may adjust the value by any cash distributions or contributions to the Fund.
- **Headline Risk:** Special servicers are tasked with collecting interest, principal and escrow payments from a borrower. These are usually higher-touch relationships than a primary servicer. Special servicers deal specifically with delinquent borrowers and are tasked with bringing a loan into good standing by facilitating loan modifications, approving short sales, or bringing about foreclosure proceedings. There have been multiple lawsuits both civil class action and federal (Consumer Financial Protection Bureau - CFPB) against various loan servicers. Accusations range from mistakes and nefarious practices that cost homeowners' money and their homes through inappropriate fees and billing and wrongfully held foreclosure sales. While VWH does not own a servicer outright, there is a risk that a special servicer VWH contracts with will be the subject of such headlines.

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.
- This memo for the Fund provides a summary of information and documentation received by NEPC from the manager through phone calls and meetings. The product has been rated by NEPC's Alternative Assets Committee.
- Information used to prepare this report was obtained directly from the investment manager, and market index data was provided by other external sources. While NEPC has exercised reasonable professional care in preparing this report, we cannot guarantee the accuracy of all source information contained within.
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In addition, it is important that investors understand the following characteristics of non- traditional investment strategies including hedge funds, real estate, and private equity:

- Performance can be volatile, and investors could lose all or a substantial portion of their investment.
- Leverage and other speculative practices may increase the risk of loss.
- Past performance may be revised due to the revaluation of investments.
- These investments can be illiquid, and investors may be subject to lockups or lengthy redemption terms.
- A secondary market may not be available for all funds, and any sales that occur may take place at a discount to value.
- These funds are not subject to the same regulatory requirements as registered investment vehicles.
- Managers may not be required to provide periodic pricing or valuation information to investors.
- These funds may have complex tax structures and delays in distributing important tax information.
- These funds often charge high fees.
- 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.