

DAVID Y. IGE
GOVERNOR



DEPT. COMM. NO. 177

WESLEY K. MACHIDA
DIRECTOR

LAUREL A. JOHNSTON
DEPUTY DIRECTOR

EMPLOYEES' RETIREMENT SYSTEM
HAWAII EMPLOYER-UNION HEALTH BENEFITS TRUST FUND
OFFICE OF THE PUBLIC DEFENDER

STATE OF HAWAII
DEPARTMENT OF BUDGET AND FINANCE
P.O. BOX 150
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ADMINISTRATIVE AND RESEARCH OFFICE
BUDGET, PROGRAM PLANNING AND
MANAGEMENT DIVISION
FINANCIAL ADMINISTRATION DIVISION
OFFICE OF FEDERAL AWARDS MANAGEMENT (OFAM)

December 29, 2016

The Honorable Ronald D. Kouchi,
President and Members of the Senate
Twenty-Ninth State Legislature
State Capitol, Room 409
Honolulu, Hawaii 96813

The Honorable Joseph M. Souki,
Speaker and Members of the House
of Representatives
Twenty-Ninth State Legislature
State Capitol, Room 431
Honolulu, Hawaii 96813

Dear President Kouchi, Speaker Souki and Members of the Legislature:

For your information and consideration, I am transmitting a copy of the Innovation Economy 2016 report, as required by Act 260, Session Laws of Hawaii 2007. In accordance with Section 93-16, HRS, a copy of this report has been transmitted to the Legislative Reference Bureau and the report may be viewed electronically at <http://ers.ehawaii.gov/resources/reports-to-legislature>.

Sincerely,

A handwritten signature in black ink, appearing to read "Wesley K. Machida".

WESLEY K. MACHIDA *for*
Director of Finance

Enclosure

c: Legislative Reference Bureau

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EMPLOYEES' RETIREMENT SYSTEM
OF THE STATE OF HAWAII

INNOVATION ECONOMY
2016

Act 260, Session Laws of Hawaii 2007, expresses the State's desire to increase economic growth through the development of the State's human resources, and employing these highly skilled resources to leverage increases in innovation across the State's economy.

The Board of Trustees of the Employees' Retirement System (ERS) acknowledges the intent of Act 260. Accordingly, the ERS, through its investment policies and an appropriate-sized funding allocation, has demonstrated a commitment to supporting an innovation economy while at the same time pursuing its objectives of achieving attractive venture capital investment return for the benefit of its beneficiaries.

The ERS Board approved the creation of a Hawaii Targeted Investment Program (HiTIP) Policies and Procedures on March 10, 2008, which included the adoption of funding criteria, as required by Act 260. A \$25 million program funding allocation and a comprehensive HiTIP operating structure were approved on November 10, 2008 and December 8, 2008, respectively. The purpose of the HiTIP is to invest venture capital in locally-based early-stage technology companies through a portfolio of local, regional, and national venture capital funds within an institutional investment program structure. Under a competitive search process, the ERS selected a discretionary investment manager to operate and manage the HiTIP, which is projected to have a program lifespan of up to 15 years.

The ERS is required to annually report any Hawaii venture capital investment. For calendar-year 2016, the ERS has supported Act 260 through the following investment measures:

- Since inception, HiTIP has committed its full allocation of \$25.25 million into seven private equity funds and one Hawaii-based co-investment.
- The HiTIP program was designed to cover the major industry sectors of the Hawaiian entrepreneurial ecosystem. As a percent of committed capital, HiTIP is allocated 37% to Information Technology, 28% to Clean Technologies, 25% to Life Sciences, and 10% to Dual-Use.
- HiTIP funds have looked at 705 investment opportunities with 432 Hawaii-based companies. Of these companies, 54 are being tracked for a potential future investment.
- HiTIP Funds have invested into four companies operating in or that were started in Hawaii. Total direct investment by HiTIP funds into Hawaiian companies is \$32.8 million, 130% of HIERS' HiTIP commitment. Including capital from co-investors, \$134 million has been invested into Hawaiian companies, 536% of HIERS' HiTIP commitment. Multiple Hawaii based companies are in discussions with HiTIP funds for potential investment.

- The HiTIP portfolio has experienced seven initial public offerings (IPOs) since inception. Epic Venture Partners IV portfolio company Everspin Technologies (MRAM) went public in October 2016. Another Epic portfolio company, Instructure (INST), the largest position in the fund by value, went public in November 2015. Pantentes Talgo (TGO) from Vantera Transformative Energy and Materials Fund went public in May 2015. Conatus Pharmaceuticals (CNAT) and Aratana Therapeutics (PETX) from MPM BioVentures V and Receptos (RCPT) from Polaris Venture Partners VI went public in 2013. Versastem (VSTM) from MPM BioVentures V went public in 2012.
- As of September 30, 2016, the gross Internal Rate of Return (IRR) of the HiTIP fund is 8.6% with a Distributed to Paid-In Ratio (DPI) of 0.25x and a Total Value to Paid-In Ratio (TVPI) of 1.27x.
- In September 2016, the ERS Board authorized an investment commitment of up to \$35.0 million for a HiTIP Fund II, subject to final due diligence and adoption of updated HiTIP policies.