



RSA's Big Deals for the Home Place

Private placement investments in Alabama companies by the Retirement Systems of Alabama have been one of the state's most powerful forces for economic development — creating 282,564 jobs in 11 years, and yielding a return that beat stocks and bonds.

BY CHARLIE INGRAM // PHOTO BY ROBERT FOUTS

In December 2014, the Alabama Supreme Court ruled in favor of the Retirement Systems of Alabama in *Denson v. Bronner*, a lawsuit brought by two RSA members seeking to prohibit RSA's private placement investments in Alabama companies and various real estate holdings in the state. The lawsuit claimed that those investments generated a lower return than investments in stocks

and bonds.

A year later, RSA head David Bronner — ever ready to spar with detractors — landed a return punch in the December 2015 issue of *The Advisor*, a newsletter for RSA members. "TO MY CRITICS," Bronner wrote in bold print and all capital letters, "it is with great pleasure to point out that our best performing investments in 2015 came from the private

placements sector.

"Both the private placements and real estate show the importance of diversification of a large investment portfolio. Just maybe, investing a small percentage of our assets in our state pays off in more ways than originally thought."

David Bronner and Hunter Harrell work to benefit state retirees and the state itself.



RSA ended up buying a plant near Muscle Shoals that started out life in 2007 as a project for Canada-based National Steel Car. Chicago-based Navistar now leases the facility.

Denson v. Bronner was just another in a long line of swipes at the 71-year-old Bronner, who has been the RSA's chief executive officer since 1973. Under his tenure, RSA assets have grown from \$500 million to \$32.6 billion, as membership in the pension system has surpassed 339,000.

RSA was ranked in the top 12 percent of the nation's largest pension funds at the end of its 2015 fiscal year, according to State Street Investment Analytics. In 2015, the stock market saw its worst year since 2008, and some large pension funds lost value. RSA saw a 1 percent return but still heard the cry of critics. Currently, for example, consideration is being given to proposals that would change Alabama's pension fund options. It's really nothing new for Bronner.

"The politicians of the state, including the governor, are elected to solve problems, and if they're lucky, they get two terms, eight years," he says. "But some get four years, and if they didn't solve the problems, they're outta here."

"But the pension fund guy has to worry about the 18-year-olds and the 21-year-olds who come to work for the state. It's my job to make sure they have something 30 and 40 years from now. Our objectives are totally opposite, so you're always going to have conflict between the politicians and the guy who's looking long-term."

To be sure, RSA investments have their good years and not-so-good years, and some of the RSA's private placement

investments have fared better than others.

They are not all winners. But RSA has had more than its share of winners in the private placement sector, and those winners pay off in more ways than return on investment, Bronner and others say.

Only about 5 percent of RSA's assets are in private placements within Alabama, whereas private placement investments in the United States and overseas account for almost 25 percent of RSA's portfolio.

"We definitely would prefer to do these investments with Alabama companies," says Hunter Harrell, director of RSA's private placements since 2003. "It benefits RSA, the state of Alabama's tax base and the people of Alabama by providing additional employment, which in turn generates additional income that in turn provides all the ancillary-type businesses that revolve around people having more money."

RSA's largest-ever private placement investment was also one of its best. It started in 2006 when RSA provided additional working capital for Wise Metals in Muscle Shoals, a manufacturer of aluminum for beverage cans. From then until 2014, RSA invested \$580 million in Wise Metals and acquired a 15 percent equity stake.

When the company was sold in 2014, RSA had been repaid for all of those loans and received \$58.7 million for its equity share. "I think that's a pretty good return," Harrell says. "It's certainly better than average. We try to get equity in our

transactions because that's where the upside is. We're not always able to do that, but it's generally part of the negotiation process."

In addition to money that RSA made from dealing with Wise Metals, there was an additional benefit to the state. The new owner, Netherlands-based Constellium, broke ground last year on a \$900 million expansion to manufacture aluminum parts for the automotive industry. When completed, that should mean even more jobs at the 1,200-employee facility.

In a different deal, in south Alabama, RSA acquired a 19 percent equity stake in Monroe County businesses that were sold to Georgia-Pacific in 2010 as the Alabama River and Alabama Pine pulp mills, also referred to as the Alabama River Group.

RSA investments there dated to the late 1980s and totaled some \$462 million. RSA received \$79.5 million for its equity in that scenario. Georgia-Pacific has since announced a \$110 million project at what is now known as Georgia-Pacific Cellulose operations to upgrade wood yards and a pulp machine.

Not all RSA investments yield such returns. Some go south, but even then RSA has in all likelihood taken steps to mitigate the damage and given itself a chance to recover. A good example is its involvement with Canada-based National Steel Car, which broke ground in 2007 on a huge plant near Muscle Shoals to build railroad freight cars. The plant was to be a mile long and employ 1,800 workers.

It didn't happen. The project quickly derailed, running head-on into the 2008 recession and leaving RSA to sort through the wreckage. RSA initially invested \$350 million to help build the plant, but it became apparent that the Canadian owner didn't have the funds to finish the construction. In 2009, RSA's investment to finish construction of the facility reached more than \$550 million.

"They didn't have enough money to finish the plant, and by the time we figured that out, we decided to complete the plant and take ownership, because you can't have a half-built plant just sitting there in north Alabama," Harrell says.

RSA had taken the right steps, however, to give itself a way out. "We started out in this investment being sure we had

a lien on all the assets,” Harrell says. “We negotiated the right to buy the property around the facility, approximately 650 acres, and we did that. So we had the plant, the hard assets, and the acreage, too, and that’s what we try to do — to make these loans as secure as we can.”

RSA took ownership of the plant in 2010, but demand for rail cars at the time was anemic, owing to the ongoing recession. In 2011, however, Chicago-based Navistar signed a 10-year lease to occupy the facility. Navistar, the nation’s top producer of school buses and medium and heavy-duty trucks, has since subleased roughly a third of the plant to FreightCar America. Navistar employs roughly 300 people at the facility, and FreightCar America has 850 employees, according to a Navistar spokesperson.

“If things always went like clockwork, there would be no need for lawyers, bankruptcy attorneys and all of that,” Harrell says. “Unlike most transactions that mature and pay off and everybody goes their happy way, we took this one back and are managing it. If everything

goes to our plan and their purchase options, I think we’ll be fine. And we are getting monthly income from that facility.”

Bronner and Harrell both would like to invest in more Alabama companies, but there simply aren’t as many opportunities here as elsewhere. “I do know as the little bureaucrat that it’s a lot harder for me to do things in Alabama than it is in New York or California or Europe or Asia,” Bronner says. “We have all those investments, but if we (Alabama) don’t invest in ourselves, we’re just sitting here hoping somebody else will come in and invest in us.”

Bronner cites a recent RSA investment in an Auburn company, SIO2 Medical Products, as a strong example of the kind of investment he wants to make. The company’s founder, New York inventor and businessman Bob Abrams, established a small presence in Auburn some 20 years ago with a company that developed and marketed plastic containers for pharmaceuticals, consumer products and food service industries.

In 2013, SIO2 Medical Products opened in Auburn with 300 employees. Together, Abrams’ companies in Auburn now have more than 500 employees, many of them in better-than-average-pay jobs. RSA backed SIO2 Medical Products with an \$80 million loan.

The company, according to its website, “manufactures products that combine the durability of plastics with the barrier properties and product contact surface of glass.” In short, the material is well suited for delivering protein-based drugs, which have a skyrocketing demand.

“The level of sophistication at the RSA was much greater than I’ve found in very few of the normal sources (of financing),” says Abrams, who has plans to build a similar plant in Switzerland. “They understood the long-term importance of this industry and that it was just going to grow — that it’s the future of the pharmaceutical industry. Auburn, we hope, is going to grow substantially over the next five to 10 years.”

Such growth, from Bronner’s perspective, is the prescription Alabama needs.

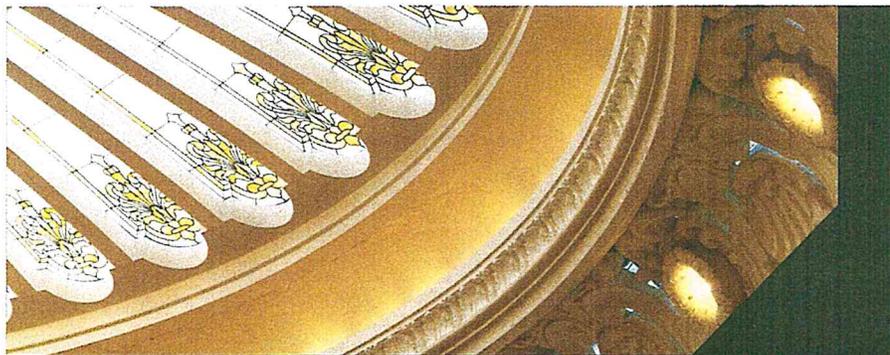
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How Private Placements Fit Into the RSA Portfolio

As of late December, RSA's portfolio of \$32.6 billion included \$7.6 billion in private placements, or 23.5 percent of the total, with Alabama private placements making up 5 percent of the total. The private placements refer mainly to investments made in companies, both debt and equity deals, along with real estate holdings.

Based on a study by M. Keivan Deravi, an economics professor at Auburn University at Montgomery, the amount of money RSA has invested in Alabama private placements has generated more in returns than if it had been invested in stocks and bonds.

Between 1990-2011, RSA invested \$5.6 billion in Alabama companies and real estate, in 2011 dollars. If invested in stocks and bonds, that money could have generated a return of \$541.6 million, or a return of roughly 10 percent. But Deravi's study notes that RSA investments are estimated to have generated \$1.1 billion in additional tax revenues for the state, which means a return of 19 percent.

The study says that between 1990-2011, RSA investments generated an additional \$28 billion in cumulative gross domestic product for the state, \$14 billion in cumulative earnings and 282,564 fulltime jobs. Based on that data, the study concludes that for every \$1 of RSA funds invested in Alabama, the return has been \$1.57.

Charlie Ingram and Robert Fouts are freelance contributors to Business Alabama. Ingram is based in Birmingham and Fouts in Montgomery.