



State of New Jersey

Agenda item #4 a

CHRIS CHRISTIE
Governor

DEPARTMENT OF THE TREASURY
DIVISION OF INVESTMENT
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Lt. Governor

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State Treasurer

October 15, 2010

MEMORANDUM TO: The State Investment Council

FROM: Timothy Walsh
Director

SUBJECT: **Proposed additional investments to existing Hedge Fund Investments in King Street Capital, L.P. and Davidson Kempner Institutional Partners Fund, L.P.**

This due diligence memorandum is presented to the State Investment Council (the "Council") pursuant to N.J.A.C. 17:16-69.9 to report on proposed \$50 million **additional** commitments to King Street Capital, L.P. and Davidson Kempner Institutional Partners Fund, L.P.

Please note that these investments are authorized pursuant to Articles 69 and 100 of the State Investment Council's (the "Council") regulations. The King Street Capital, L.P. Fund and Davidson Kempner Institutional Partners Fund, L.P. will be considered credit oriented investment and equity oriented investment, respectively, as defined under N.J.A.C. 17:16-100.1.

The Division of Investment ("Division") Staff and its hedge fund consultant, Cliffwater LLC, undertook extensive due diligence on these proposed additional investments. We completed the same due diligence process as with all the other alternative investment opportunities presented to the Council.

The King Street Capital, L.P. is a distressed/event driven hedge fund, was started by Francis Biondi and Brian Higgins in April 1995. The firm manages \$19.6 billion, \$18.7 billion in global focus with U.S. concentration and \$875 million in concentrated European exposure. They deploy a long/short approach to distressed and event driven situations and seek to generate positive alpha from, both, long or short positions. They also invest in capital structure trades. The key risk in the portfolio is the specific issuer risk which is mitigated by diversified portfolio of core 75 to 125 positions. They make limited use of leverage. The firm has 174 employees including 63 investment professionals. The fund's year-to-date performance ended September 30, 2010 is 3.80%. The annualized return since inception in April 1995 to September 30, 2010 is 14.43% with 4.50% annualized standard deviation. The division initially invested \$100 million on March 31, 2007. The original investment has generated 42.53% return over the period

April 1, 2007 to September 30, 2010; the annualized rate of return over the period is 10.39%.

The Davidson Kempner Capital Management, LLC was founded by Marvin H. Davidson in May 1983. The Davidson Kempner Institutional Partners Fund for tax exempt investors was started in May 1995. The firm manages \$14.3 billion of which \$13.2 billion is in the event driven strategy. The fund primarily invests in merger arbitrage, bankruptcy and restructuring situations. They also invest in convertible arbitrage, event driven equities and distressed opportunities. The firm employs a bottoms-up approach based on extensive research and understanding of factors affecting the future performance of the company and the industry sector. They typically do not use leverage. The firm has 81 investment professionals and 86 operations and back office personnel. The fund had a low management fee of 1% which was raised to 1.5% on January 1, 2007 for new investors; old investors were grandfathered at 1%. The management fee for \$50 million additional investment will be 1.5%. Blended management fee for \$150 million committed capital works out to 1.167%. The funds performance has been very strong. Fund returned 7.17% year-to-date ended September 30, 2010. Since inception in March 1996, the annualized return and the standard deviation ended September 30, 2010 were 9.70% and 3.76%, respectively. The division initially invested \$100 million on December 1, 2006. The original investment has generated 26.96% return over the period December 1, 2006 to September 30, 2010; the annualized rate of return over the period is 6.43%.

We will work with representatives of the Division of Law and outside counsel to review and negotiate specific terms of the legal documents to govern each investment. In addition, each proposed investment must comply with the Council's "pay to play" regulation (N.J.A.C. 17:16-4).

Formal written due diligence reports for the proposed investments were sent to each member of the Investment Policy Committee on October 13, 2010, and a meeting of the Committee was held on October 14, 2010. In addition to the formal written due diligence reports, all other information obtained by the Division on the investments was made available to the Investment Policy Committee.

We look forward to discussing the proposed investments at the Council's October 21, 2010 meeting.

Attachments

SIC Investment Committee Fund Review Memo

To: State Investment Council
From: SIC Investment Committee
Date: October 21, 2010
Subject: King Street Capital Management, LLC Recommendation

Fund Facts

Fund Name:	King Street Capital, LP
Fund Type:	Distressed/Event Driven
Current Fund Size:	\$18.7 billion
Inception:	April-95
Fund Address:	65 East 55th Street, 30th Floor New York, NY 10022

GP Contact Info

Name:	Laila Festini Iqbal
Telephone:	(212) 812-3134
Email:	liqbal@kingstreet.com

Summary of Terms and Investment Strategy

Investment Strategy:	Long/short credit strategy with a focus on distressed and event driven situations. Fund invests in securities at all level of capital structure, from bank debt to equity, and seeks to generate returns from both long and short positions over various market cycles.
Fee Terms:	
Management and Performance Fees:	Management fee - 1.5% Performance fee - 20%
Other Fees:	Fund expenses - approximately 5 basis points
Hurdle Rate:	None
Liquidity/Redemption Terms:	
Lock-up:	1 year
Redemption:	Quarterly with 65 days notice; 25% per quarter investor level gate; 25% fund level gate; 5% early redemption fee on assets in excess of investor level gate
Side Pocket:	Up to 15%. Incentive fee is paid when investment is monetized.

NJ AIP Program:

Recommended Allocation Current:	\$50 million addition to existing \$141 mil investment
% of Fund:	1.02%
% of New Jersey State Pension Plan:	0.28%
% of AIP Hedge Fund Allocation (\$4.7b):	4.06%

Consultant Recommendation:	Yes
*see due diligence memo	
Compliance with SIC "Pay to Play" Reg:	Side letter already in place

* This review memorandum was prepared in accordance with the State Investment Council rules governing the Alternatives Investment Program and the policies and procedures related thereto.

SIC Investment Committee Fund Review Memo

To: State Investment Council
From: SIC Investment Committee
Date: October 21, 2010
Subject: Davidson Kempner Advisors, Inc Recommendation

Fund Facts

Fund Name:	Davidson Kempner Institutional Partners, LP
Fund Type:	Event Driven
Current Fund Size:	\$13.2 billion
Inception:	November-95
Fund Address:	65 East 55th Street, 19th Floor New York, NY 10022

GP Contact Info

Name:	Eric Epstein
Telephone:	(212) 446-4010
Email:	eepstein@dkpartners.com

Summary of Terms and Investment Strategy

Investment Strategy:	Event driven fund that primarily invests in merger arbitrage, bankruptcy and restructuring situations. They also have smaller allocations to convertible arbitrage, event driven equities and distressed opportunities. The manager applies a bottom-up approach based on extensive research and a deep understanding of key factors driving each event.
Fee Terms:	
Management and Performance Fees:	Management fee - 1.5% on new capital 1.0% on existing capital Performance fee - 20%
Other Fees:	Fund expenses - approximately 10 basis points
Hurdle Rate:	None
Liquidity/Redemption Terms:	
Lock-up:	None
Redemption:	Quarterly with 65 days notice.
Side Pocket:	Up to 5%. Incentive fee is paid when investment is monetized.

NJ AIP Program:

Recommended Allocation Current:	\$50 million addition to existing \$125 mil investment
% of Fund:	1.32%
% of New Jersey State Pension Plan:	0.26%
% of AIP Hedge Fund Allocation (\$4.7b):	3.72%

Consultant Recommendation:	Yes
*see due diligence memo	
Compliance with SIC "Pay to Play" Reg:	Side letter already in place

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