State of New Jersey

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Governor

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DEPARTMENT OF THE TREASURY
DIVISION OF INVESTMENT
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ANDREW P. SIDAMON-ERISTOFF
State Treasurer

July 27, 2012

MEMORANDUM TO: State Investment Council

FROM: Timothy Walsh
Director

SUBJECT: **Proposed Investment in Dyal Capital Partners Fund**

The New Jersey Division of Investment ("Division") is proposing an investment of up to $200 million in **Dyal Capital Partners** Fund ("Dyal"). This memorandum is presented to the State Investment Council (the "Council") pursuant to N.J.A.C. 17:16-69.9.

The Division is recommending this investment based on the following factors:

Differentiated Investment Strategy: Dyal (one of six businesses within the Neuberger Berman Alternatives platform) will focus on purchasing minority stakes in established hedge fund managers (AUM of $1.5 to $5 billion). While there have been a number of groups which have raised funds for hedge fund seeding transactions, increasing the competition for those investments, Dyal will face little competition in this space.
High Cash Flows/Attractive Overall Returns: Investments are expected to generate steady and rising cash flow from management fees supplemented by variable cash flow from incentive fees earned by underlying funds. Overall, the investment is conservatively expected to earn low to mid-teen annualized returns with low volatility and significant upside potential.
Ability to Leverage Neuberger Berman Platform: Dyal's ability to leverage NB's platform to provide hedge funds with client introductions, consultant coverage, and other support services make them an attractive partner for hedge funds considering selling stakes in their firms.
Experienced Investment Team: Dedicated investment team of Michael Rees, Sean Ward, and Mark O'Sullivan worked together at Lehman Brothers and were instrumental in acquiring minority equity stakes in hedge funds such as D.E. Shaw & Co., GLG Partners, and Spinnaker Group.
Attractive negotiated fee structure: The Division negotiated a very attractive fee structure on the proposed investment which includes a 0% management fee on un-invested capital and 1.25% on invested capital during the 5-year investment period instead of the listed 2% fee on committed capital during the investment period. This concession will result in an estimated fee savings of $12.5 million during investment period. The Division also negotiated a 0.75% management fee on invested cost after the investment period instead of listed 1.5% fee, resulting in an estimated recurring fee savings per year of $1.5 million. The investment will also have a 20% performance

fee, 8% annualized preferred return and 100% catch-up. The Division will also maintain the ability to veto one to two potential investments.

A report of the Investment Policy Committee ("IPC") summarizing the details of the proposed investment is attached.

Division Staff and its hedge fund consultant, Cliffwater LLC, undertook extensive due diligence on the proposed investment in accordance with the Division's Alternative Investment Due Diligence Procedures. As part of its due diligence process, staff determined that the fund has used third-party solicitors ("placement agents") in the fundraising of the fund but no placement agent was engaged or paid in connection with New Jersey's potential investment.

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 the investment. In addition, the proposed investment must comply with the Council's regulation governing political contributions (N.J.A.C. 17:16-4).

Please note that the investment is authorized pursuant to Articles 69 and 100 of the Council's regulations. The **Dyal Capital Partners** Fund will be considered a Multi–Strategy hedge fund investment, as defined under N.J.A.C. 17:16-100.1.

A formal written due diligence report for the proposed investment was sent to each member of the IPC and a meeting of the Committee was held on July 18, 2012. In addition to the formal written due diligence report, all other information obtained by the Division on the investment was made available to the IPC.

We look forward to discussing the proposed investment at the Council's Aug 2, 2012 meeting.

Attachments

Fund Name: Dyal Capital Partners Fund — August 2, 2012

Contact Info: **Sean Ward, Dyal Capital Partners, 605 Third Ave, New York NY 10158**

Fund Details:

Total Firm Assets ($bil.):	$199.0 billion
Strategy:	Multi-Strategy Hedge Fund
Assets in Strategy($bil.):	$1 billion
Year Founded:	2010
SEC Registration	Yes
GP Commitment:	2.00%

Key Investment Professionals:

Michael Rees, Managing Director and a Senior Principal of Dyal, was a founding employee and shareholder of Neuberger Berman Group, transitioning from Lehman Brothers as part of the management buyout transaction in May of 2009. Michael had numerous roles at Lehman Brothers and was responsible for strategic acquisitions for the Investment Management Division at Lehman Brothers.

Sean Ward, Senior Vice President and Senior Principal of Dyal. Sean has held several roles at Neuberger Berman since it became an independent firm, including Senior Counsel for NB Alternatives. Prior to joining the firm, he was an attorney with Covington & Burling LLP.

Mark O'Sullivan, Senior Vice President and Senior Principal of Dyal. Mark was previously a Senior Vice President in the Private Equity & Principal Investments group at LAMCO LLC.

Investment Summary

Dyal Capital Partners ("Dyal") is managed by the Neuberger Berman Group LLC. The Dyal team managing the fund is part of the NB Alternatives Division which manages $16 billion in several alternative investment strategies. The dedicated investment team of Michael Rees, Sean Ward, and Mark O'Sullivan worked together at Lehman Brothers and were instrumental in acquiring minority equity stakes in hedge funds such as D.E. Shaw & Co., GLG Partners, and Spinnaker Group. Dyal will focus on purchasing minority stakes in established hedge fund managers (AUM of $1.5 to $5 billion). Investments are expected to generate steady and rising cash flow from management fees supplemented by variable cash flow from incentive fees earned by underlying funds. Overall, the investment is conservatively expected to earn low to mid teen annualized return with low volatility and significant upside potential.

Previous Investments (Lehman Prop Capital) Performance as of 9/30/2008*

Vintage Year	Previous Inv Net IRR	Russell 2000 Index Return	Excess Return
2000	54.40%	-4.60%	59.00%

* Cliffwater Estimate

Vehicle Information:

Fund Inception:	2011	Subscriptions:	Capital Calls
Fund Size ($mil.):	$1 billion	Redemptions (notice):	N/A
Management Fee:	1.25% on called capital during inv. period, thereafter 0.75% on invested cost	Lock-up:	5-year Investment period
Profit Allocation:	20%	Prime Broker:	N/A
Highwater Mark:	N/A	Administrator:	Capital Analytics
Hurdle Rate:	8%	Auditor:	KPMG
Additional Expenses:	15-20 bps	Legal Counsel:	Covington & Burling LLP (US); Walkers (Cayman)

NJ AIP Program

Recommended Allocation ($mil):	$200 Million	LP Advisory Board Membership:	TBD
% of Fund:	20%	Consultant Recommendation:	Yes
		Placement Agent:	No
		Compliance w/ Division Placement Agent Policy:	Yes
		Compliance w/ SIC Political Contribution Reg:	Yes

*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.

X GP's signature