State of New Jersey

DEPARTMENT OF THE TREASURY
DIVISION OF INVESTMENT
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September 23, 2015

MEMORANDUM TO: The State Investment Council

FROM: Christopher McDonough
Director

SUBJECT: **Proposed Investment in Dyal Capital Partners III L.P. & Related Co-Investment Separate Account**

The New Jersey Division of Investment ("Division") is proposing an investment of up to $200 million in Dyal Capital Partners III L.P. ("Dyal III") and up to $100 million to a related co-investment separate account managed by Dyal Capital Partners ("Dyal"). This memorandum is presented to the State Investment Council (the "Council") pursuant to N.J.A.C. 17:16-95.2.

Dyal III will take non-control, minority investments in private equity investment management companies, which is a natural continuation of its existing business in acquiring similar stakes in hedge funds managers. The co-investment account will invest in overage and co-investment opportunities. The Division has been a lead investor in Dyal Funds I & II, which have both generated strong returns and cash flows.

The Division is recommending this investment based on the following factors:
Performance/Return Attributes: The Dyal funds have demonstrated strong risk-adjusted returns since inception.
As of 3/31/15:
- Dyal I - Net Internal Rate of Return ("IRR") of 15.22%, Multiple on Invested Capital "(MOIC")of 1.22x and Distributions to Paid-In ("DPI") of 0.28x (*Top-Quartile on a DPI basis)
- Dyal II – Net IRR of 24.25%, MOIC of 1.02x and DPI of 0.02x (*Top-Quartile on all metrics)

*According to Thomson Reuters/Cambridge Global PE/VC Benchmark

Furthermore, Dyal I has already returned, on a net basis, 26% of the Division's invested capital as of 6/30/15. The high cash flowing nature of the Fund's investment is an attractive attribute as cash is regularly distributed from management fees earned on existing and future funds/products. This is supplemented with expected near-term exits which Dyal will benefit from in the form of its share of balance sheet and carry profits.
Experienced Team/Platform: The Dyal team consists of 20 people with a wealth of experience in cultivating and executing transactions dating back to their days at Lehman Brothers (examples

include: GLG Partners, Ospraie, Marble Bar, Spinnaker and DE Shaw); as well as the 12 transactions that they've executed since the formation of Dyal.

Lack of Competition: Regulatory restrictions have reduced more traditional financial institutions' ability to acquire stakes in PE firms. In general, conflicts and competitive dynamics typically preclude other private equity shops from these type of transactions, and there are a limited number of firms with the knowledge and experience in acquiring stakes in alternative asset management platforms.

Private Equity/Industry Growth: The alternative investment industry continues to grow at a rapid pace as it benefits from attractive risk/return characteristics. Un-invested capital is at an all-time high and fundraising continues to be robust. In Preqin Ltd.'s recent *Preqin Investor Outlook: Alternative Assets, H2* 2015, a survey of LPs showed that over the next 12 months, LPs expected to increase allocations to PE by 42%, while longer term 51% said they would increase allocations. In addition, a June 2015 Citi Business Advisory Services report forecasted Private Equity Assets under Management going from $3.8 trillion to $5.2 trillion over the next 5 years.

Private Equity Model: The Private Equity structure is conducive to Dyal's investment strategy of buying stakes in investment management companies and participating in management fees, returns from GP commitments and carry profits. The long-tailed nature of private equity funds and the fees that are generated from having several funds active over long periods of time are attractive from a cash flow perspective. Coupled with the fact that the long-term performance of the PE asset class has been attractive: 14.43% over the last 20 years according to Cambridge Associates data. Moreover, alternative asset firms continue to aggregate assets and complementary strategies (i.e. - credit platforms) as the industry continues to get larger.

Terms: Given the Division's broad relationship with Neuberger Berman, the Division has negotiated preferential economics that are lower than the standard terms outlined. The Division's effective management fee rate across all of its Dyal investments is estimated to be less than 1%, with a carry rate less than 15% based on certain return assumptions.

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

Division Staff and its consultant, Cliffwater LLC, undertook extensive due diligence on the proposed investments.

As part of its due diligence process, staff determined that the fund and related separate account have not engaged a third-party solicitor (a "placement agent") in connection with New Jersey's potential investments.

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 investments. We have obtained a preliminary Disclosure Report of Political Contributions in accordance with the Council's regulation governing political contributions (N.J.A.C. 17:16-4) and no political contributions have been disclosed. We will obtain an updated Disclosure Report at the time of closing.

Please note that the investments are authorized pursuant to Article 95 of the Council's regulations. Dyal Capital Partners III L.P. and related co-investment separate account will be considered opportunistic investments, as defined under N.J.A.C. 17:16-95.1.

A formal written due diligence report for the proposed investments was sent to each member of the IPC and a meeting of the Committee was held on September 15, 2015. In addition to the formal written due diligence report, all other information obtained by the Division on the investments was made available to the IPC.

We look forward to discussing the proposed investments at the Council's September 23, 2015 meeting.

Attachments

Fund Name: Dyal Capital III, L.P. & Related Co-Investment Separate Account — September 23, 2015

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

Fund Details:

Total Firm Assets:	$250 billion
Strategy:	Opportunistic
Assets in Strategy:	$2.5 billion
Year Founded:	2010
SEC Registration	Yes
GP Commitment:	1%; $5 million to co-investment transactions

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. Mr. Rees had numerous roles at Lehman Brothers and was responsible for strategic acquisitions for the Investment Management Division at Lehman Brothers.

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

Investment Summary

Dyal Capital Partners is one of six businesses within the $20 billion Neuberger Berman Alternatives platform. 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. The Division has been a lead investor in both Dyal I & II, which have both generated strong returns and cash flows back to NJ. The Fund will focus on acquiring minority equity interests in investment management companies that are believed to be positioned for sustained earnings growth. The focus will be on managers that built a lasting business capable of attracting inflows from large, sophisticated investors. They will seek out private equity managers that have diversified sources of return by managing or being able to manage multiple products. These will be high quality, sustainable firms as demonstrated by their length of time in business, diverse ownership and diverse client base. In addition to the investment in Dyal III, the Division will also be able to invest in overage and co-investment opportunities in Dyal III through establishing a co-investment account.

Existing Fund

Funds	Strategy	Vintage	Returns as of 3/31/2015
Dyal NJ Investors I	Buyout	2012	15.22% Net IRR, 1.22x Net TVPI, 0.28x Net DPI
Dyal NJ Investors II	Buyout	2014	25.25% Net IRR, 1.02x Net TVPI, 0.02x Net DPI

IRR = Internal Rate of Return; TVPI = Total Value to Paid-In; DPI= Distributions to Paid-In

Vehicle Information:

Fund Inception:	2015	Investment Period:	5 years
Fund Size:	$2.5 billion	Administrator:	Capital Analytics
Management Fee:	2% on committed, 1.5% on invested until year 15, and 0% thereafter	Auditor:	KPMG LLP
Profit Allocation:	20%	Legal Counsel:	Fried Frank
Hurdle Rate:	8%		
Offsets:	100% fee offset		
Co-invest Account:	No fee; no carry		

NJ AIP Program

Dyal Capital III, LP recommended Allocation:	$200 million	LP Advisory Board Membership:	TBD
Co-investment separate account recommended Allocation:	$100 million	Consultant Recommendation:	Yes
% of Dyal III:	8.00%	Placement Agent:	No
% of Co-Invest Account:	100.00%	Compliance w/ Division Placement Agent Policy:	N/A
		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.