



State of New Jersey

DEPARTMENT OF THE TREASURY
DIVISION OF INVESTMENT
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Governor

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State Treasurer

November 2, 2012

MEMORANDUM TO: The State Investment Council

FROM: Timothy Walsh
Director

SUBJECT: **Proposed Additional Investment in SONJ Private Opportunities Fund II, L.P.**

The New Jersey Division of Investment ("Division") is proposing an additional investment of \$400 million in SONJ Private Opportunities Fund II, L.P. 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:

Attractive Terms

The fees and structure of the SONJ II add-on are improved from the prior programs. Some of the key negotiated terms are as follows:

- Venture Capital: 25 bps management fee
- Co-investments/Secondaries/Etc.: 75 bps management fee
- 8% preferred return (net after fees) across all investments
- European style waterfall: All called capital including fees, plus the preferred return must be returned to the Division before Black Rock can start receiving carry
- No-fault divorce clause

Maintains the Division's Co-Investment Capabilities

It is vital to the Division's alternative investment portfolio that it maintains an allocation to co-investments from any and all sources of deal flow. The Division receives co-investment opportunities on a weekly, if not daily basis from mostly existing managers, but also from Black Rock relationships and from managers in which the Division is not invested with to date but maintains a good relationship.

Ability to Leverage Resources

The Division and Black Rock have developed a close working relationship since 2006 with a major factor being the proximity of the two groups to each other, which increases the ability of the Division to leverage Black Rock resources. The nature of the relationship will continue to

be one in which the Division maximizes Black Rock's resources and the broader Black Rock platform (e.g. investment personnel, research), to help build staff's expertise in particular areas and assist in the implementation of the broader alternatives portfolio, including private equity and real assets – from sourcing to diligence to education sessions.

Strong Performance for SONJ II

SONJ II's strategy is primarily opportunistic, with a focus on selecting the best available deals measured on a risk/return basis from a diverse group of well-respected GPs with whom Black Rock and the Division have relationships. In addition, the flexible nature of the mandate allows for Black Rock/Division to invest in hard to access, best-in-breed venture capital firms and the ability to take advantage of dislocations in the market such as buying secondary interests from motivated sellers. The strategy has been proven out by SONJ II's current performance (14.9% Net IRR, 1.25x MOIC), which is considered Top-Quartile on an IRR and multiple basis.

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

Division Staff and its private equity consultant, Strategic Investment Solutions, 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 not engaged a third-party solicitor (a "placement agent") 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 90 of the Council's regulations. With respect to the additional private equity investment, a portion will be classified as buyout and a portion will be classified as venture capital as those terms are defined under N.J.A.C. 17:16-90.1.

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 November 2, 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 November 8, 2012 meeting.

Attachments

Fund Name: SONJ Private Opportunities Fund II, L.P. - Add on **November 8, 2012**

Contact Info: Lynn Baranski, 1 University Square Drive, Princeton, NJ 08540, (609) 282-3612

Fund Details:		<p>Key Investment Professionals: <u>Russ</u> Steenberg, Global Head / Managing Director: Hired by Merrill Lynch Investment Managers in 1999 to establish a private equity fund of funds and direct co-investment business. PEP was formed in July 1999 as a business unit of MLIM and was combined with BlackRock in October 2006. Prior to joining MLIM to form PEP, Mr. Steenberg was employed by AT&T Investment Management Company, where he was instrumental in building one of the earliest private capital programs in the institutional investment community. Lynn Baranski, CIO /Managing Director: Ms. Baranski has over 20 years of private equity investment experience. Prior to joining Private Equity Partners in 2001, she worked for four years as a Portfolio Manager and Research Analyst in Adviser's fixed income division in the European High Yield Group and US Bank Loan Portfolio Group, respectively. Jay Park, Managing Director: Mr. Park has over 17 years of private equity investment experience. Prior to joining Private Equity Partners in 2001, he spent four and a half years working in Merrill Lynch's Direct Investment Group.</p>
Firm AUM (\$bil.):	\$3.56 trillion	
Strategy:	Buyout	
Year Founded:	1988	
Headquarters:	Princeton, NJ	
GP Commitment:	2%	

Investment Summary	Existing and Prior Funds		
<p>The New Jersey Division of Investment ("NJDOI" or "Division") is proposing an additional commitment of up to \$400 million to SONJ Private Opportunities II, L.P. ("SONJ II") managed by BlackRock Private Equity Partners ("PEP"). The strategy for the additional commitment will be largely similar to the existing SONJ II account - invest globally across private equity, including venture capital, growth capital, buyouts, recapitalizations, distressed debt, and mezzanine debt. This will include co-investments, primary fund commitments, and secondaries.</p> <p>The primary focus for the additional SONJ II allocation is to continue the direct co-investment strategy which will comprise a significant portion of the SONJ II Add-on. These opportunities are sourced from other NJDOI GPs; GPs with whom PEP has a relationship; and other GPs currently unaffiliated with either NJDOI or PEP. In addition, SONJ II will take advantage of PEP's access to top-tier venture capital managers to enhance the returns of NJDOI's private equity program. PEP has demonstrated access to certain well-regarded venture funds.</p>	<u>Funds</u>	<u>Strategy</u>	<u>Returns</u>
	SONJ I	Buyout	0.87% Net IRR, 1.04x MOIC
	SONJ II	Buyout	14.9% Net IRR, 1.25x MOIC

Vehicle Information:

Inception:	2007	Auditor:	Deloitte & Touche, LLP
Fund Size (\$mil.):	\$800 million	Legal Counsel:	Ropes & Gray, LLC
Management Fee:	<u>Venture Capital:</u> 25 bps <u>Co-Investments/Secondaries/Etc.:</u> 75 bps		
Carry:	10%		
Hurdle Rate:	8%		
Additional Expenses:	100% fee offset		

NJ AIP Program

Recommended Allocation (\$mil):	Additional \$400 million	LP Advisory Board Membership:	N/A
% of Fund:	98%	Consultant Recommendation:	Yes
		Placement Agent:	No
		Compliance w/ Division Placement Agent Policy:	N/A
		Compliance w/ SIC Political Contribution Reg:	Yes