



State of New Jersey

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March 19, 2014

MEMORANDUM TO: The State Investment Council

FROM: Christopher McDonough
Acting Director

SUBJECT: **Proposed Investment in Och-Ziff Real Estate Fund III**

The New Jersey Division of Investment (“Division”) is proposing an investment of \$100 million in Och-Ziff Real Estate Fund III (“OZRE III”). 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:

Successful Track Record: Since its formation in 2003 through December 31, 2013, the real estate team has made over 65 investments with a total enterprise value of over \$5.8 billion. OZRE I (2005 vintage fund) is marked at 15.5% net Internal Rate of Return (“IRR”) and a 1.5x net Multiple of Invested Capital (“MOIC”) and OZRE II (2010 vintage fund) is marked at 20.2% net IRR and 1.2x net MOIC, both considered top-quartile for their vintage, in each case based on fair market values as of September 30, 2013.

Unique Partnership Characteristics: The Division’s existing partnership with Och-Ziff, which was presented to the Council in August 2012, consists of a \$1.1 billion commitment across various separate account mandates that invest in private and public assets across its platform (the “Platform”). One of these accounts is a vehicle that invests in U.S. and European real estate and real estate-related assets. This account was created to invest in excess opportunities alongside OZRE II and pursue opportunities that did not fit into the mandate of OZRE II. The investment in OZRE III will be on the same economic terms as the Platform, including a 0.75% management fee on net asset value instead of 1.25% on committed capital, and carried interest payments calculated based on netting the investment returns of all dollars the Division has invested in the Platform.

Niche Exposure: Based on current views of anticipated investment opportunities during its investment period, OZRE III is expected to be a 50/50 split between traditional real estate assets (i.e. - multifamily, office, hotel and retail) and non-traditional real estate assets (including gaming, distressed land and residential, cell towers, parking, golf, debt and senior housing). Since its inception, the firm has invested \$580.45 million (58%) in non-traditional real estate assets with weighted average projected gross MOIC of 2.09x. They have invested \$413.35 million (42%) in traditional real estate assets with weighted average projected gross MOIC of

2.07x. A commitment to OZRE III will provide diversification to the Division's real estate portfolio and provide exposure to non-traditional assets.

Och-Ziff Platform/Alignment of Interest: Och-Ziff is one of the world's largest alternative asset management firms with \$42.3 billion under management (as of March 1, 2014) across all sectors, geographies and asset classes. The real estate team leverages this platform for due diligence and sourcing purposes. The Division has witnessed this collaboration first hand while reviewing opportunities with the real estate team and other investment professionals through its due diligence efforts in the various active separate account vehicles. The partners of Och-Ziff have also been a major investor in Och-Ziff Real Estate since its inception and represent over \$250 million of its total capital commitments in OZRE I and OZRE II.

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

Division Staff and its real estate consultant, R.V. Kuhns and Associates, Inc., 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 71 of the Council's regulations. The Och-Ziff Real Estate Fund III will be considered a non-core real estate investment, as defined under N.J.A.C. 17:16-71.1.

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 March 11, 2014. 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 March 19, 2014 meeting.

Attachments

Fund Name: Och-Ziff Real Estate Fund III

March 19, 2014

Contact Info: Britton Leigh, 9 West 57th Street, 39th Floor, New York, NY 10019

Fund Details:

Total Firm Assets (\$bil.):	\$42.3 bil as of March 1, 2014
Strategy:	Non-Core Real Estate
Year Founded:	1994 (Och-Ziff) / 2003 (OZRE)
Headquarters:	New York, NY
Och-Ziff Commitment:	7.5% up to \$75 million

Key Investment Professionals:

Steven Orbuch, President. Mr. Orbuch is a Founder, the President and a Senior Principal of OZRE, a member of OZRE's investment committee and an Executive Managing Director of Och-Ziff. Prior to forming OZRE in 2003, he was a Managing Director with Blackstone Real Estate Advisors where he participated in the sourcing, acquisition and financing of over \$2 billion of commercial properties across multiple product types and geographic locations.

Nicholas Hecker, Senior Principal. Mr. Hecker is a Senior Principal at OZRE, where he is involved in all aspects of OZRE's business, including fundraising, acquisitions, asset management and dispositions. Prior to joining OZRE, he worked in the Real Estate Group of the Investment Banking Division of Goldman, Sachs & Co. from 2004 to 2006.

Cory Perlstein, Senior Principal. Mr. Perlstein is a Senior Principal at OZRE, where he is involved in all aspects of OZRE's business, including fundraising, acquisitions, asset management and dispositions, with primary responsibility for OZRE's debt-related and lodging investment activities. Prior to joining OZRE, he worked at Blackstone, where he was involved in analyzing investments across all property types.

Investment Summary

OZRE was founded in 2003. The Fund is OZRE's third (3) vehicle in its opportunistic real estate fund series, and follows the successful deployment of the two (2) predecessor funds raised and invested from 2004 to present. Collectively, these predecessor opportunity funds raised over \$1.2 billion of equity commitments. Och-Ziff Real Estate Fund III, is targeting \$1 billion in commitments, of which Och-Ziff will contribute at least 7.5% or \$75 million. The Fund's strategy is to pursue opportunistic real estate investments across the capital structure, which OZRE has done successfully in its prior funds. The team will continue to invest selectively in niche asset classes and complex situations where they can source investment opportunities through proprietary relationships of OZRE or the broader Och-Ziff organization.

Existing and Prior Funds

Funds	Vintage Year	Strategy	Returns as of 9/30/2013 (based on FMV)
Och-Ziff RE Fund I	2005	Non-core	15.5% Net IRR, 1.5x Net MOIC
Och-Ziff RE Fund II	2010	Non-core	20.2% Net IRR, 1.2x Net MOIC

IRR = Internal Rate of Return
MOIC = Multiple of Invested Capital

Vehicle Information:

Inception:	2014 (expected)	Auditor:	Ernst & Young
Fund Size (\$mil.):	\$1.0 bil (targeted)	Legal Counsel:	Debevoise & Plimpton LLP
Management Fee:	0.75% of Net Asset Value		
Carry:	20% (aggregate across OZNJ platform)		
Hurdle Rate:	6% (aggregate across OZNJ platform)		
Management Fee Offsets:	100% offset for directors, transaction, monitoring, breakup and similar advisory fees		

NJ AIP Program

Recommended Allocation (\$mil.):	\$100,000,000	LP Advisory Board Membership:	TBD
% of Fund:	10%	Consultant Recommendation:	Yes
		Placement Agent:	No Placement Agent used in connection with DOI's investment
		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.