

September 12, 2008

MEMORANDUM TO: State Investment Council

FROM: William G Clark
Director

SUBJECT: **Proposed Hedge Fund Investment in
LIM Asia Arbitrage Fund, Inc.**

This due memorandum is presented to the State Investment Council (the “Council”) pursuant to N.J.A.C. 17:16-69.9(a) to report on a proposed \$75 million direct absolute return fund commitment to LIM Asia Arbitrage Fund, Inc. to be managed by LIM Advisors Limited based in Hong Kong.

Please note that this investment will be authorized pursuant to Articles 69 and 100 of the Council’s regulations. The LIM investment will be considered a Multi-Strategy Fund investment as defined under N.J.A.C. 17:16-100.1.

The Alternative Investments Procedures adopted by the Council on February 21, 2008 require any potential alternative investment opportunities to be identified and initially evaluated by the applicable staff of the Division of Investment (“DOI”) and the applicable Asset Class Consultant (Cliffwater LLC for direct hedge funds, or “Cliffwater”), in coordination with the DOI Investment Committee (Director, Deputy Director and senior hedge fund staff member).

The DOI Investment Committee identified this proposed investment as a result of internal and external sourcing. Cliffwater and DOI staff proceeded to undertake extensive due diligence on the proposed investment. We completed the same due diligence process as with all the other alternative investment opportunities presented to the Council.

Based on this due diligence, the Division has determined that the proposed investment meets the criteria for investments set forth in the Alternative Investment Procedures.

LIM Advisors Limited is an SFC-registered investment firm founded by George Long in 1995 and currently has \$1.4 billion in assets under management. The firm is based in Hong Kong where most of its 48 employees are located. Mr. Long founded LIM after serving as the CIO for Barclays Global Investors Asia where he was responsible for managing over \$2.5 billion in assets. The LIM Asia Arbitrage Fund employs relative value, convertible bond arbitrage, event-driven, merger arbitrage, high yield and other arbitrage strategies. The fund invests in a variety of individual strategies and financial instruments, seeking to produce positive returns by exploiting specific investment opportunities that involve little or no direct exposure to the general systematic risk of the equity markets. The fund is diversified across over 200 individual positions, and the top ten names account for only 20% of the fund's assets. The majority of the fund's country exposures are in Japan, Korea, Hong Kong, Indonesia, China and Singapore. Since inception of August 2004 through May 2008, the fund has generated an annualized return of 9.58% with volatility of 5.71%, resulting in a Sharpe ratio of 0.91.

A formal written due diligence report for the proposed investment was sent to each member of the Investment Policy Committee of the Council on September 5, 2008, and a meeting of the Committee was held on September 10, 2008. In addition to the formal written due diligence report, all other information obtained by the Division on this investment was made available to the Investment Policy Committee.

After a review of the due diligence conducted on the fund, the Investment Policy Committee of the Council decided to report on the proposed investment to the full Council pursuant to Step 4 of the Alternative Investments Procedures. Under these procedures, the Council may adopt or otherwise act on this report.

Attached to this memorandum is the SIC Investment Committee Fund Review Memorandum for the proposed 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 this investment. In addition, the proposed investment must comply with the Council's "pay to play" regulation (N.J.A.C. 17:16-4). While we are confident that we will work through these issues, the potential exists that a successful resolution will not be reached with this manager.

We look forward to discussing this proposed hedge fund investment at the Council's September 18, 2008 meeting.

WGC/MK:lt
Attachment