

May 16, 2008

MEMORANDUM TO: State Investment Council

FROM: William G. Clark
Director

SUBJECT: Proposed Private Equity Investments in GSO Capital Opportunities Fund, L.P., JLL Partners Fund VI, L.P., TPG VI, L.P., TPG Financial Partners, L.P., and HIG Bayside Debt & LBO Fund II, L.P.

This due diligence memorandum is presented to the State Investment Council (the "Council") pursuant to N.J.A.C. 17:16-69.9 (a) to report on five proposed private equity investments: a \$100 million commitment to GSO Capital Opportunities Fund, L.P., \$150 million to JLL Partners Fund VI, L.P., \$400 million to TPG VI, L.P., \$100 million to TPG Financial Partners, L.P., and \$100 million to HIG Bayside Debt & LBO Fund II, L.P.

Please note that these investments will be authorized pursuant to Articles 69 and 90 of the Council's regulations. The investments in JLL VI, TPG VI and TPG Financial Partners are considered "Buyout Funds" and the investments in GSO and HIG Bayside are considered "Debt Related" investments as defined under N.J.A.C. 17:16-90.1.

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 (Strategic Investment Solutions for Private Equity or "SIS") in coordination with the DOI Investment Committee (Director, Deputy Director, and the Senior Staff member for the applicable alternative asset class).

As a result of internal and external sourcing, the DOI Investment Committee identified these proposed investments. SIS and Division staff proceeded to undertake extensive due diligence on the proposed investments. 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 these proposed investments meet the criteria for investments set forth in the Alternative Investments Policy.

GSO Capital Opportunities Fund, L.P. is a debt and special situation oriented private equity fund that can participate in all parts of the capital structure, including first and second lien loans, mezzanine and high yield debt, structured equity and private equity, allowing the Fund to seek the best risk-adjusted returns. GSO Capital Opportunities Fund will focus on middle and upper-middle market transactions across a variety of industries and asset categories, leveraging the Firm's in-house research capabilities and industry vertical specialization.

The Fund will be led by Bennett Goodman, Tripp Smith and Doug Ostrover (the "Principals") who have worked together for over 15 years. GSO Capital Opportunities Fund recently merged with Blackstone and should be considered a "re-up" to our existing investment in Blackstone Mezzanine Partners II. The fund will be hard capped at \$1.5 billion, of which the Division is proposing a \$100 million commitment. The aforementioned Partners are committing in excess of \$100 million to the current Fund.

JLL Partners Fund VI, L.P. is a U.S. focused middle market buyout fund. JLL VI intends to pursue a strategy of investing in well-established companies that have exceptional management, strong competitive position within their industry, sustainable competitive advantages relative to competitors and good growth prospects. Growth of the businesses will be achieved both organically and through acquisitions. Specifically, JLL will focus on buying control of fundamentally sound companies in complicated situations, including restructurings, and backing exceptional managers in building strong companies through a series of acquisitions.

NJDOI committed to their previous fund, JLL Partners Fund V, in December 2005, and has been very satisfied with the performance to date. JLL Partners Fund VI will be capitalized at \$2.5 billion, of which the division is proposing a \$150 million commitment to Fund VI.

TPG VI, L.P. is a U.S. and internationally focused large buyout fund. Texas Pacific Group is known for investing in complex situations with a contrarian ideology. Two of the three founders worked for the Bass Family in the early 1980s and developed an ability to buy complex and distressed situations and often times transform these businesses before realization. In light of the current economic investment environment, TPG's heritage, skill set, and breadth of resources is relatively better suited to take advantage of the opportunities that may avail themselves over the ensuing months/years.

TPG VI is targeting \$18 billion and will seek investment opportunities between \$250 million and \$1 billion of equity. The Division is currently an investor in TPG V (a \$15.3 billion fund) and TPG TAC (Loan Fund). The Division is proposing a \$400 million commitment to Fund VI.

TPG Financial Partners, L.P. is a financial services “overage” fund seeking to make investments in control and non-control financial services assets. In light of the current turmoil in the financial services sector, TPG is launching this fund, which is structured to take advantage of the current environment. The Partnership will make non-control investments in large financial services firms, and those stakes will be by definition less than 50%. TFP will also participate in control transactions by co-investing with TPG V and TPG VI, which in some cases could result in combined stakes of up to 100% in certain companies. The Division is proposing a \$100 million commitment.

HIG Bayside Debt & LBO Fund II, L.P. is a lower to mid-market distressed buyout fund focused on the U.S. and Europe. H.I.G. Bayside II will be the firm’s second distressed debt and stressed LBO fund.

H.I.G. is a leading small and mid cap alternative investment firm with over \$4.5 billion of equity capital under management across a number of strategies (private equity, distressed, growth/ venture capital and hedge fund) in the U.S. and Europe. HIG Bayside Debt & LBO Fund II will target lower middle market distressed debt for control, stressed/distressed LBO's and to a limited extent, non-control distressed debt investments. The Fund will invest its capital across both the US and Europe although the US is expected to account for a significant majority of its activities. The Fund will seek to acquire underperforming, stressed or distressed companies requiring operational turnaround and/or financial restructuring to unlock value. The Division is proposing a \$100 million commitment to the fund.

For all of our recommended private equity investments, management fees are reasonable, and all the legal and economic terms associated with the partnerships are fair and consistent with market standards.

Formal written due diligence reports for these proposed investments were sent to each member of the Investment Policy Committee of the Council on May 9, 2008, and a meeting of the Committee was held on May 15, 2008. In addition to the formal written due diligence reports, all other information obtained by the Division on these investments was made available to the Investment Policy Committee.

After review of the extensive due diligence, the Investment Policy Committee of the Council decided to report on the proposed investments to the full Council pursuant to Step 3 of the Alternative Investments Procedures. Under these procedures, the Council may adopt or otherwise act on this report.

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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 each investment. In addition, each 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 may not be reached with one or more of those general partners.

We look forward to discussing the proposed private equity investments at the Council's May 22, 2008 meeting.

WGC: cpp
Attachment