

New Jersey State Investment Council

July 22, 2015 Regular Meeting

Minutes of the Regular Meeting

Held July 22, 2015 at the Trenton War Memorial, George Washington Ballroom, 1 Memorial Drive, Trenton, New Jersey.

Council Members in Attendance:

Brendan T. Byrne, Jr., Chair
Adam Liebttag, Vice Chair
Marty Barrett
Michael Cleary
Charles Dolan
Michael Greaney
James Hanson
Guy Haselmann
James Joyner (arrived during Director's Report)
Mitchell Shivers

Benjamin "Max" Hurst, Timothy McGuckin, and Jeffrey Oram were not in attendance.

Roll Call and Meeting Notice

The Regular Meeting was called to order by Brendan T. Byrne, Council Chair, at 10:07AM. Ernestine Jones-Booker, Council Secretary, performed roll call and reported that a quorum of the State Investment Council (Council) was present. Ms. Jones-Booker reported that notice of the Regular Meeting, scheduled for July 22, 2015, was posted on the website of the Division of Investment (the Division), faxed to the Times of Trenton, the Bergen Record, and the Courier Post, and e-mailed to the Secretary of State on June 19, 2015. A copy of the notice was posted at the Division and is on file.

Opening Remarks

Mr. Byrne noted that the fiscal year to date performance of the fund was 4.58% at the end of May, and indicated that given the state of the markets during the month of June, it was likely that the overall expected returns for FY15 would be below the 7.9% actuarial rate of return. He emphasized the importance of diversification, and lauded the Division staff for outperforming the benchmark by 73 bps fiscal year to date.

Director's Report/Update

Director Chris McDonough presented the Director's Report, noting that FYTD fund performance will be finalized and reported at the next meeting in September. Mr. McDonough provided an update on the performance of the portfolio as a whole and the performance of specific asset classes. Mr. McDonough reported on portfolio shifts in asset allocation toward the recently adopted FY16 targets. Mr. McDonough provided an overview of capital markets. Charles Dolan observed the discrepancy in performance between asset classes and noted the benefits of diversification.

Deputy Director Corey Amon provided an overview of key investment themes, discussing economic and market conditions in the United States, and providing an update on global market crises in Greece and China. Guy Haselmann cautioned against expecting a high level of positive returns in the future, and urged diversification away from fully-priced assets. He noted the Council's recently adopted asset allocation was designed to weather contingencies going

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forward. Mr. Byrne cited an abnormally high Shiller ratio in the public equity markets, but noted that it is impossible to predict market direction and agreed that diversification offered the best protection for the fund.

Mr. McDonough and Jason MacDonald of the Division provided an overview of the Division's private equity and real estate portfolios. Mr. McDonough corrected the public misperception that the Division was dramatically increasing its exposure to alternatives in recent years, noting that there were lower net commitments to the alternatives portfolio within the last five years than within the first five years of the program. James Hanson referenced the pace of commitments relative to the pace of distributions in the private equity portfolio and inquired if the portfolio was under or over committed. Mr. McDonough responded that, in terms of asset allocation, the fund is under-allocated to private equity, but given the state of the private equity market, recommended maintaining the existing allocation going forward.

Pursuant to the Council's Alternative Investment Modification Procedures, Mr. McDonough notified the Council of two hedge fund redemptions, including full redemptions from Archipelago Partners and Arden Garden State NJ Fund LP. Mr. McDonough indicated that the Division was redeeming from Archipelago because the Fund's portfolio had matured to the extent that the Division felt there was no longer a need for a multi-manager program. He reported that the Division was redeeming from Arden due to the recent departure of key investment professionals.

Finally, Mr. McDonough noted a correction to the Debt Related Real Estate and Private Real Assets components of the FY16 Asset Allocation Policy Benchmarks. The components, as reported at the prior meeting, remained unchanged from FY15; however, they were mislabeled in the Council materials last meeting.

Minutes of Regular Meeting held May 27, 2015

Mr. Byrne presented for adoption the minutes for the regular meeting held May 27, 2015. Mitchell Shivers made a motion to approve the minutes, with Mr. Haselmann seconding the motion. All Council Members present voted in favor.

Election of Nominating Committee

Mr. Byrne made a motion to elect Mr. Oram, Mr. McGuckin, and Mr. Haselmann to continue to serve on the Council's Nominating Committee. All members of the Council present voted in favor except Mr. Haselmann, who abstained. Mr. Byrne asked the Nominating Committee to present its nominations for Chair and Vice Chair at the September meeting.

JLL Partners V, L.P. Update

Mr. McDonough reported that the Division took a number of steps with respect to the Division's investment in JLL Partners V, L.P., including evaluation of the future expected value of the fund, exploration of different options for disposing of New Jersey's interest in either the fund or, more specifically, in ACE Cash Express Inc., consultation with Aon Hewitt regarding socially responsible investment policies, and improvement of its due diligence reporting process. Mr. Byrne noted that the Council works cooperatively with the Division, but does not have the statutory power to order a sale of the investment. He noted that illiquid investments are complicated to unwind, and the Division is acting with all deliberate speed, consistent with its fiduciary obligations to plan beneficiaries. Mr. Haselmann and Adam Liebttag noted that the IPC had a hearty discussion with Division staff regarding the matter, and Mr. Liebttag requested that the matter be revisited at every Council meeting until the issue is resolved.

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Selection of Private Equity Investment Consultants

Mr. MacDonald reported that the Division selected TorreyCove Capital Partners as its primary investment consultant for private equity along with four other secondary consultants to include Cliffwater LLC, LP Capital Advisors, Strategic Investment Solutions and Wilshire Associates Inc. Mr. MacDonald provided a summary of the bidder selection and evaluation process. In response to a question from Mr. Dolan regarding risk management, Mr. MacDonald described the risk management products and services to be provided by TorreyCove.

Private Equity Investments

American Industrial Partners Capital Fund VI, L.P.

Robin Clifford of the Division, along with Faraz Shooshani of Strategic Investment Solutions, presented an investment of up to \$200 million in American Industrial Partners Capital Fund VI, L.P., a private equity buyout fund focused on investing in industrial companies in North America. Ms. Clifford noted AIP's deep cohesive investment team, proprietary deal flow dissimilar to its peers, and top-quartile investment returns. Ms. Clifford summarized the terms of the investment. Mr. Hanson asked whether the longer investment period for the fund (six years) represented a trend in these types of investments. Mr. Shooshani responded that it is not a trend, and that the Division expected capital to be deployed in sooner than six years. Mr. Haselmann noted the hurdle rate, and Mr. Liebttag inquired whether the \$200 million commitment was to be phased in over time. Mr. McDonough responded that the \$200 million commitment would likely be cut back because the fund was oversubscribed, and the capital would be called by the General Partner as needed within the investment period. Mr. Byrne reported that the Investment Policy Committee discussed the investment and was satisfied that the due diligence that was performed was adequate and appropriate.

Excellere Capital Fund III, L.P.

Mr. MacDonald and Mr. Shooshani presented an investment of up to \$50 million in Excellere Capital Fund III, L.P., a lower mid-market private equity fund. Mr. MacDonald noted the strong top-quartile performance of Excellere's prior two funds, its differentiated investment strategy, and its above-average general partner commitment. In response to a question from Marty Barrett, Mr. Shooshani outlined the timing of incentive payments to the fund manager. Mr. Byrne reported that the Investment Policy Committee discussed the investment and was satisfied that the due diligence that was performed was adequate and appropriate.

GoldenTree Distressed Separate Account

Mr. MacDonald and Mr. Shooshani of SIS presented an investment of up to \$300 million in a separate account managed by GoldenTree Asset Management, with up to \$200 million investing pro-rata alongside GoldenTree's 2014 distressed fund, and up to \$100 million reserved for additional distressed opportunities. Mr. MacDonald noted the Division's previous relationship with GoldenTree and GoldenTree's attractive terms and exposure to distressed investment opportunities. Mr. Byrne asked regarding the state of the market for distressed opportunities, to which Mr. MacDonald responded that the Division wanted to have dry powder available in the event of a market downturn. Mr. Byrne reported that the Investment Policy Committee discussed the investment and was satisfied that the due diligence that was performed was adequate and appropriate.

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Hedge Fund Investments

Mr. McDonough summarized the Division's reallocation of funds in the hedge fund portfolio, including \$1.15 billion in redemptions. A portion of these funds (\$450 million) will be invested in two new absolute return investment opportunities.

Laurion Capital, LP and Laurion Capital Global Markets Fund Ltd.

Jessie Choi and Samantha Rosenstock of the Division, along with Pete Keliotis of Cliffwater, presented investments of up to \$100 million in Laurion Capital L.P., and up to \$100 million in Laurion Capital Global Markets Fund Ltd. The Laurion Capital fund is a global macro hedge fund focusing on volatility, arbitrage and relative values strategies, and the Laurion Capital Global Markets fund is an extension of the Laurion Capital fund, isolating specific strategies within that fund. Ms. Choi reported the manager had excellent top-quartile risk-adjusted returns, and described the favorable terms of the investment, noting that the terms of the investment were superior to other funds in its peer group. Mr. Byrne noted the degradation of the fund's returns in 2014 and questioned whether there was enough liquidity in the market to support the fund's increased capacity. Ms. Choi responded that majority of what the fund trades is very liquid and the returns in 2014 were reflective of the recent muted macro environment. Mr. Haselmann commented that he felt this investment was important, given government hyperactivity in the marketplace and the Division's redemption out of other funds with similar strategies. Mr. Dolan noted the fund's outperformance in the tumultuous markets of the last decade. Mr. Shivers inquired about the firm's reported assets under management, to which Mr. Keliotis responded that the reported amount was based on gross exposure and was therefore overreported. Mr. Byrne reported that the Investment Policy Committee discussed the investment and was satisfied that the due diligence that was performed was adequate and appropriate.

Stone Milliner Macro Fund, L.P.

Ms. Choi, Ms. Rosenstock, and Mr. Keliotis presented an investment of up to \$250 million in Stone Milliner Macro Fund, L.P., a global macro trading fund with an emphasis on the currency and interest rate markets. Ms. Choi noted the fund's experienced portfolio managers, its top decile risk adjusted returns, and its low correlation to both the equity market and the Division's other fund managers. Ms. Choi described the investment's attractive terms, including below market fees. Mr. Byrne reported that the Investment Policy Committee discussed the investment and was satisfied that the due diligence that was performed was adequate and appropriate.

Kingdom of Sweden Debt Obligations

Mr. Amon summarized a memorandum provided to Council members on Kingdom of Sweden debt obligations. Mr. Amon reported that the Kingdom of Sweden has an issuer rating of Aaa by Moody's Investor Services, Inc., AAA by Standard & Poor's Corporation and AAA by Fitch Ratings; however, individual bonds issued by the Kingdom are no longer rated. Mr. Amon stated that the Division was seeking approval by the Council to purchase unrated debt obligations issued by the Kingdom of Sweden in the future, provided the Kingdom maintains the above issuer ratings. Mr. Haselmann spoke in favor of granting the approval. Mr. Dolan inquired how the status of the issuer rating is monitored, to which Susan Sarnowski of the Division responded that the Division's custodian, State Street, performs compliance checks for the entire portfolio daily. Mr. Haselmann moved to approve the purchase of unrated Kingdom of Sweden debt obligations, subject to the conditions listed in the memorandum and discussed above. Mr. Dolan seconded the motion. A roll call vote was taken, with Council members Byrne, Barrett, Cleary, Dolan, Greaney, Hanson, Haselmann,

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Joyner, Liebtag, and Shivers voting in favor of the motion to approve the future purchase of unrated Kingdom of Sweden debt obligations, subject to the proviso that the Kingdom maintains its issuer ratings Aaa by Moody's Investor Services, Inc., AAA by Standard & Poor's Corporation and AAA by Fitch Ratings, and none opposed.

Verbal Report on Qualified Independent Representative (QIR) Policy

Ms. Sarnowski reported that the Division's Qualified Independent Representative (QIR) Policy, which was adopted in 2013, requires the Division to report to the Council on compliance with the Policy. Ms. Sarnowski reported that the Division is in compliance with the Policy and that the Division had obtained the required representations from each of the QIRs and designated support personnel under the Policy.

Treasurer's Report

Mr. Byrne noted the recent resignation of State Treasurer Andrew Sidamon-Eristoff and praised him for his service to the State of New Jersey. Dr. Cohen of the Treasurer's office announced further administrative changes at the Treasury and the Office of Legislative Services. Dr. Cohen reported on the State's economy, labor market and fiscal condition.

Public Comment

Tom Bruno, Chair of the NJ PERS Board of Trustees, requested a fee audit and a cost/benefit analysis for alternative investments. Mr. Byrne proposed that Mr. Bruno could possibly meet with Timothy McGuckin, the audit committee chair, to address the issue. Mr. Liebtag supported the request for obtaining a cost-benefit analysis, and Mr. Haselmann and Mr. Hanson stated that any such analysis should focus on net investment returns, rather than just the amount of fees paid. Mr. Haselmann also cautioned against relying on much of the information regarding alternative investments being reported in the press.

Roger Schwartz, Roberto Cabanas, Elizabeth Parisian, and Trina Scordo of NJ Communities United and NJ Hedge Clippers expressed concerns about the State's investments in hedge funds. Mr. Byrne acknowledged receipt of a memorandum from NJ Communities United, pointing out it was received just prior to the meeting.

Frank Abella Jr. of Community Informatics expressed concern regarding the valuation of alternative investments.

Beverly Brown Ruggia and Phyllis Salowe-Kaye of New Jersey Citizen Action and Bruce Davis of the New Jersey NAACP spoke regarding the Division's investment in JLL Partners.

Adjournment

James Joyner made a motion to adjourn the meeting, with Michael Cleary seconding the motion. All Council Members present voted in favor. The meeting was adjourned at 1:39pm.