

New Jersey State Investment Council

March 29, 2017 Regular Meeting

Minutes of the Regular Meeting

Held March 29, 2017 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
Thomas Bruno Jr.
Michael Cleary
Charles Dolan
James Hanson
Guy Haselmann
James Joyner
Timothy McGuckin
Jeffrey Oram
Eric Richard
Mitchell Shivers (via telephone)

Michael Greaney was not in attendance.

Roll Call and Meeting Notice

The Regular Meeting was called to order by Brendan T. Byrne, Jr., Council Chair, at 10:06 a.m. 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 March 29, 2017, was posted on the website of the Division of Investment (Division); faxed to the Times of Trenton, the Bergen Record, and the Courier Post; and e-mailed to the Secretary of State on February 24, 2017. A copy of the notice was posted at the Division and is on file.

Minutes of the Annual Meeting held January 25, 2017

Mr. Byrne presented for adoption the minutes for the annual meeting held January 25, 2017. James Joyner made a motion to approve the minutes, with Guy Haselmann seconding the motion. All Council Members present voted in favor, except Timothy McGuckin who abstained since he was not in attendance at that meeting.

Minutes of the Regular Meeting held January 25, 2017

Mr. Byrne presented for adoption the minutes for the regular meeting held January 25, 2017. Mr. Joyner made a motion to approve the minutes, with Thomas Bruno, Jr. seconding the motion. All Council Members present voted in favor, except Mr. McGuckin who abstained since he was not in attendance at that meeting.

Opening Remarks by Chair

Opening remarks were made by Mr. Byrne. A copy of these remarks are attached.

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Audit Committee Report on Fiscal Year 2016 Audit

Mr. McGuckin reported that the Audit Committee, comprised of himself, Michael Greaney, James Hanson and Michael Cleary, met with the auditor, KPMG, during its planning phase and again following completion of the annual audit. Mr. McGuckin noted that investments managed by the Division on behalf of the pension funds are audited as part of a general audit of the financial statements of the Division of Pensions and Benefits. Mr. McGuckin reported that the auditor issued an unmodified opinion, with no management letter comments related to the Division, and he expressed his appreciation on behalf of the Audit Committee for the work of Division staff.

Director's Report/Update

Director Christopher McDonough presented the Director's Report, providing an update on capital markets, performance and asset allocation, including the Division's progress in reducing the allocation to hedge funds. In response to Eric Richard's question regarding when the target allocation for hedge funds was expected to be reached, Mr. McDonough estimated this was likely to occur sometime in 2018. Mr. McDonough added that the Investment Policy Committee (IPC) would discuss this as part of its overall asset allocation discussion in April. Mr. Haselmann asked about the development of a secondary market for hedge fund interests. Mr. McDonough discussed attempts to develop such a market and agreed that a robust secondary market for full hedge fund positions would be beneficial. Mr. Bruno inquired about the impact of recent legislation requiring separation of PFRS assets from the rest of the pension funds. Mr. McDonough stated that the Division was aware of the legislation and remarked that the legislation presents an administrative challenge given the structure of the current system.

Deputy Director Corey Amon provided an overview of global equity markets and recent changes in monetary policy. Mr. Haselmann reflected on the causes of Europe's underperformance and emphasized the importance of diversification and proper asset allocation. Charles Dolan asked when it would be prudent to reduce exposure to U.S. equity. Mr. McDonough responded that the Division's senior investment team is closely monitoring the market and pruning equity investments as valuations rise. Adam Liebttag suggested that different scenarios for what might be priced into the market be discussed by the IPC at its April meeting.

Mr. McDonough announced the departure of Meghna Desai, the portfolio manager for alternative investments, and stated that Samantha Rosenstock was appointed interim head of the portfolio. Mr. Richard emphasized the importance of providing adequate compensation to Division staff and offered to work with the Division and other Council members to retain talented Division employees. Mr. Haselmann agreed that compensation was an important issue and proposed drafting a formal written letter from the Council. He also requested that the Division provide a copy of the prior consultant report on compensation to new members of the Council. Mr. Liebttag requested that the Council meet with the State Treasurer and Governor's Office to discuss compensation and to request additional employees. Mr. Dolan added that as fiduciaries of the fund, it was the Council's duty to ensure proper staffing. Mr. Byrne stated that he would speak with the State Treasurer regarding this matter.

Private Equity Overview

Michelle Davidson and Matthew Coyne of TorreyCove Capital Partners (TorreyCove) presented an analysis of the Division's private equity portfolio. At the request of Mr. Byrne, Mr. Coyne and Mr. McDonough described the importance of calculating both the investment multiple and net internal rate of return (IRR). In response to questions from Mr. Hanson,

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Mr. Coyne and Ms. Davidson explained the divergent performance of the private equity portfolio versus a public market equivalent index and described changes in the illiquidity premium over time. Mr. Byrne asked about protective strategies in the event of a steep drop in private equity valuations. Ms. Davidson recommended that investors concerned about shifts in the market invest in smaller funds with lower leverage and in distressed funds as a counterbalance. Mr. Liebttag and Jeffrey Oram noted the significant percentage of non-top quartile funds in the private equity portfolio. Mr. McDonough agreed to provide more detail regarding the funds' quartile rankings, and said that the Division continues to monitor funds and evaluate opportunities for secondary sales.

Mr. Timothy McGuckin departed the meeting at this time.

Alternative Investment Notification – EQT Infrastructure III L.P.

Pursuant to the Council's Alternative Investment Modification Procedures, Mr. McDonough notified the Council that, after extensive negotiations, the Division and EQT Infrastructure III L.P. were unable to reach agreement on the terms of the legal documents, and the Division did not participate in the Fund's final closing in February. Mr. McDonough reported that the Division continues to review investment opportunities in this asset class.

Private Equity Investments

CVC Capital Partners VII, L.P.

Jared Speicher of the Division and Ms. Davidson of TorreyCove presented an investment of up to €100 million in CVC Capital Partners VII, L.P., a fund focusing on opportunistic control-oriented large buyout investments in the United States and across Europe. Mr. Speicher described the Fund's investment approach, its investment team and resources, the terms of the investment, and the manager's track record. In response to a question from Mr. Byrne, Mr. Speicher described the fund's geographical investment limitations. Mr. Dolan expressed concern that a shrinking universe of investible companies could make it difficult to find sufficient investment opportunities. Mr. Speicher explained that the universe of public companies has shrunk, but that the fund had a broad mandate to invest in private companies across geographic sectors. Ms. Davidson added that the fund will be making a limited number of investments over a long time period. Ms. Davidson also discussed currency hedging to address concerns raised by Mr. Oram. Mr. Byrne reported that the IPC had reviewed the investment and was satisfied that appropriate and adequate due diligence had been performed.

Mr. Byrne recused himself from the discussion of Neuberger Berman New Jersey Custom Fund III, L.P. to avoid any possible conflict and left the meeting. Mr. Liebttag assumed the role of chair.

Neuberger Berman New Jersey Custom Fund III, L.P.

Robin Clifford of the Division and Mr. Coyne of TorreyCove presented an investment of up to \$200 million in Neuberger Berman New Jersey Custom Fund III, L.P., a customized separate account fund which will invest in small to middle market private equity funds and global co-investment opportunities. Ms. Clifford described the investment rationale and the terms of the investment. Mr. Liebttag asked how this investment affected the Division's overweight position in global buyout funds. Mr. McDonough responded that the Division based on the most recent pacing analysis, it is anticipated that distributions will exceed contributions for the next several years which will reduce the allocation to buyout funds. Mr. Liebttag reported that the IPC had reviewed the investment and was satisfied that appropriate and adequate due diligence had been performed.

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Mr. Byrne returned to the meeting at this time.

Directors Report to the Legislature on Investments in Iran

Ms. Sarnowski presented the March 2017 report issued to the Legislature related to the Iran divestment law enacted in 2007.

Directors Report to the Legislature on Investments in Companies that Boycott Israel

Ms. Sarnowski reported that in August 2016 the Legislature enacted a law that prohibits the pension and annuity funds from investing in companies that boycott Israel. Ms. Sarnowski presented the December 2016 report issued to the Legislature related to this law.

Treasurer's Report

Dr. Marc Miles of the Treasurer's office provided a brief update the strength of New Jersey's economy, discussing unemployment, labor participation, housing, and consumer confidence.

Public Comment

There were no registered speakers.

Adjournment

Mr. Haselmann made a motion to adjourn the meeting, with Mr. Oram seconding the motion. All Council Members present voted in favor. The meeting was adjourned at 12:22 p.m.