

# New Jersey Division of Investment

Director's Report

February 3, 2014

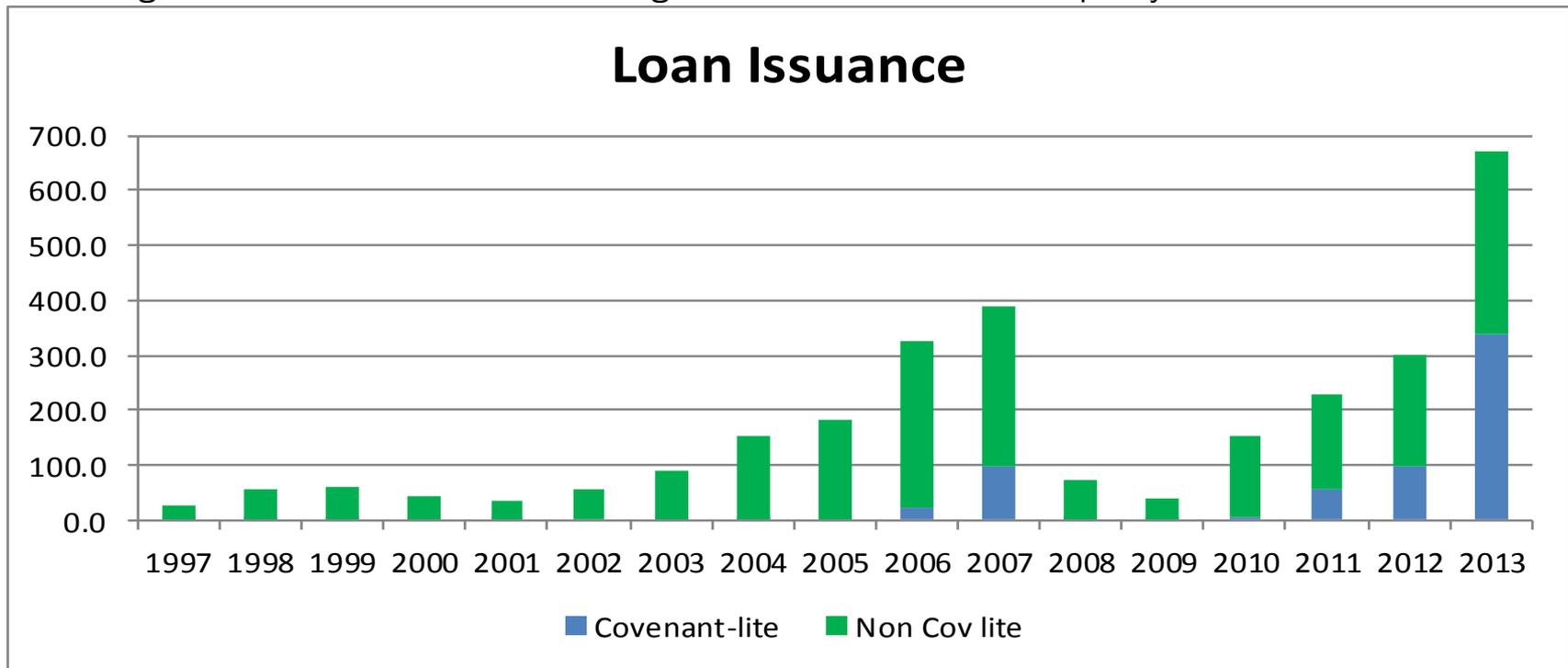
State Investment Council Meeting

*“The mission of the New Jersey Division of Investment is to achieve the best possible return at an acceptable level of risk using the highest fiduciary standards.”*

# Investment Market Update

The Fed announced on December 18, 2013 that they were officially beginning to taper their bond purchasing program, decreasing purchases by \$10 billion from \$85 billion to \$75 billion per month. On January 29, 2014, they announced an additional \$10 billion reduction in pace of purchases.

Minutes from the December Fed Meeting show concerns among the members over financial stability, including the increase in issuance of leveraged loans and the decline in quality of these loans.

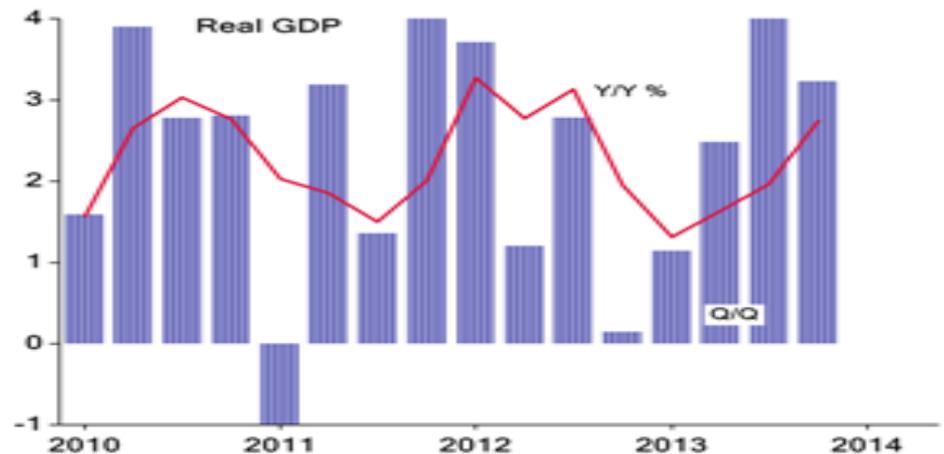


# Investment Market Update

US non-farm payrolls increased only 74,000 (vs. a forecast of 197,000) in December. The unemployment rate fell to 6.7% from 7% as the labor “participation rate,” the share of the population that’s working or looking for work, declined to 62.8% (1978 lows). There is speculation that the numbers were negatively impacted by inclement weather and could be revised.



US. GDP increased 3.2% in Q4 based on initial estimates. Household and business spending experienced meaningful pick-ups.



# Capital Markets Update (through December 31, 2013)

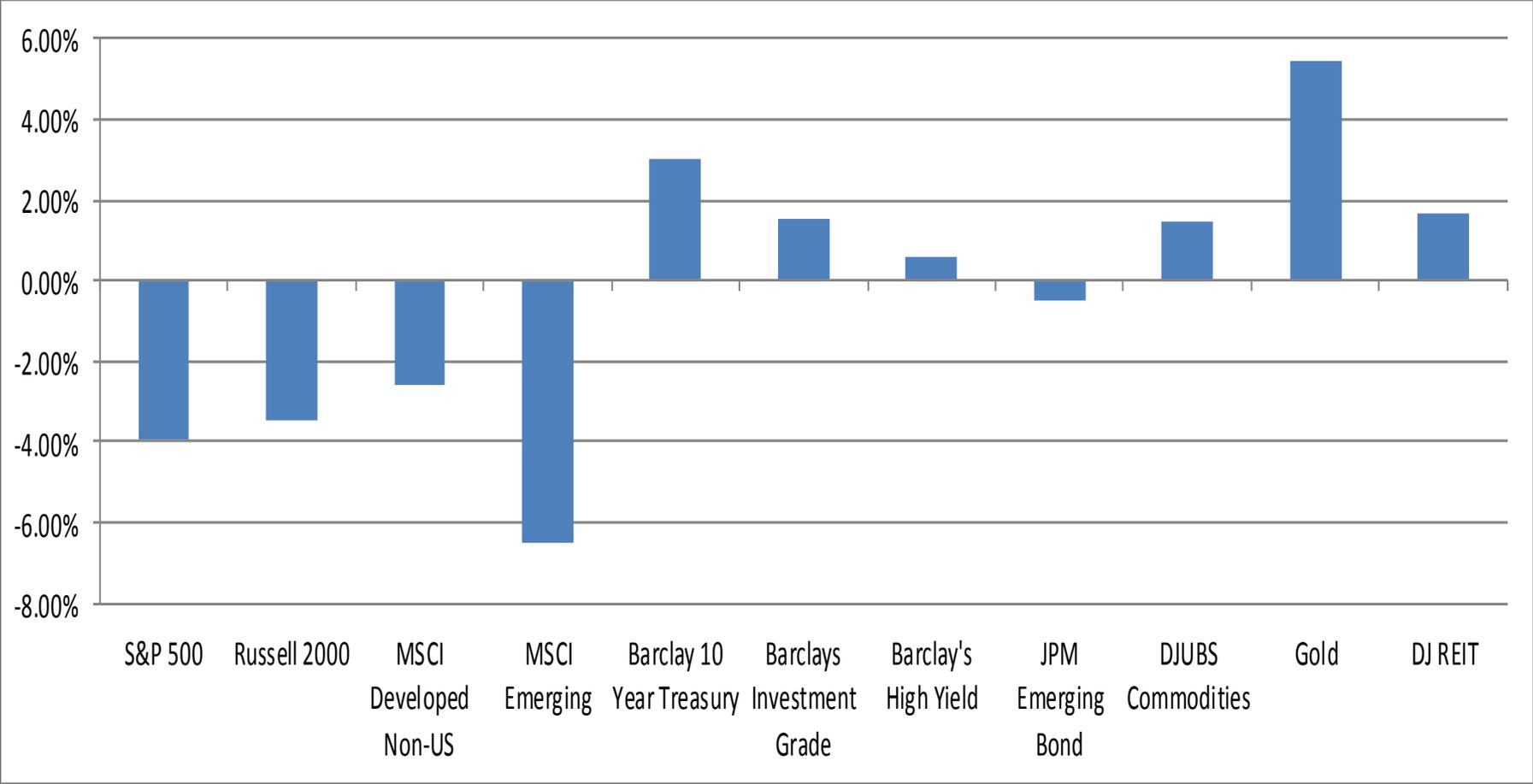
## 2013 Equity Market Returns

## 10 Year Treasury Yield



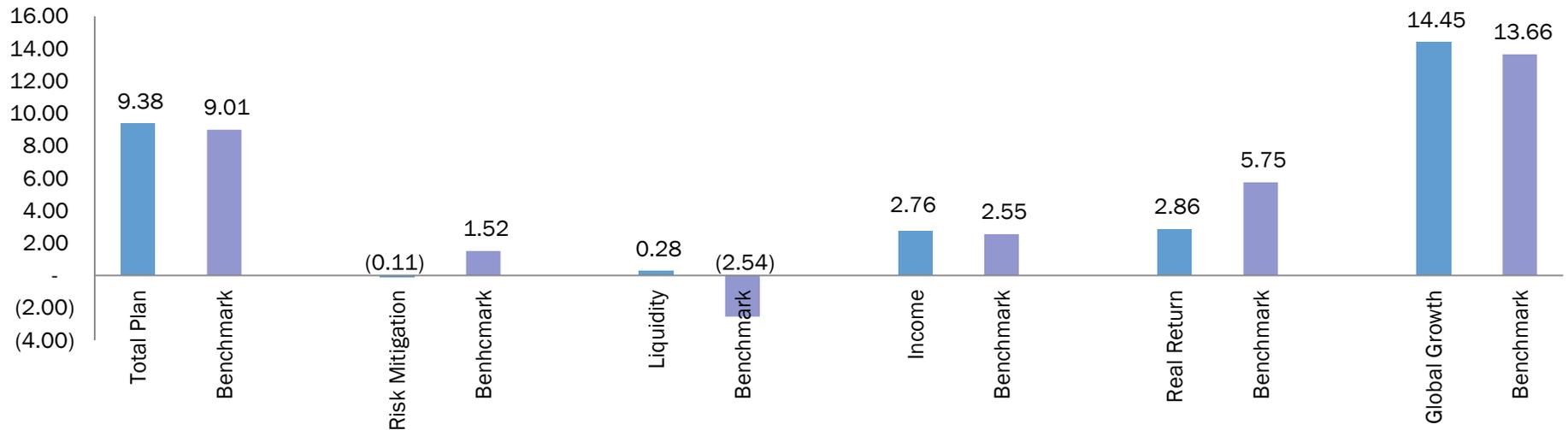
	Dec. 31, 2013	MTD %	FYTD %	1 Yr %	3Yrs %	5 Yrs %	10 Yrs %	
<b>Domestic Equity</b>	<b>S&amp;P 500</b>	2.52	16.30	32.38	16.16	17.92	7.41	1
	<b>Russell 2000</b>	1.97	19.82	38.83	15.67	20.06	9.05	2
<b>International Equity</b>	<b>MCSI EAFE</b>	1.50	17.94	22.78	8.16	12.43	6.97	3
	<b>MSCI EMF</b>	(1.45)	7.70	(2.60)	(2.06)	14.78	11.19	4
<b>Bond</b>	<b>Barclays Agg</b>	(0.57)	(1.06)	(1.96)	3.30	4.47	4.56	5
	<b>Barclays HY</b>	0.54	3.18	7.46	9.32	18.93	8.62	6
	<b>Barclays US Tips</b>	(1.97)	(2.14)	(11.27)	4.26	5.43		7
<b>Commodity</b>	<b>DJUBS Com</b>	1.24	1.06	(9.52)	(8.11)	1.51	0.82	8

# Calendar Year to Date Returns as of January 29, 2014



Source: Cliffwater and Bloomberg

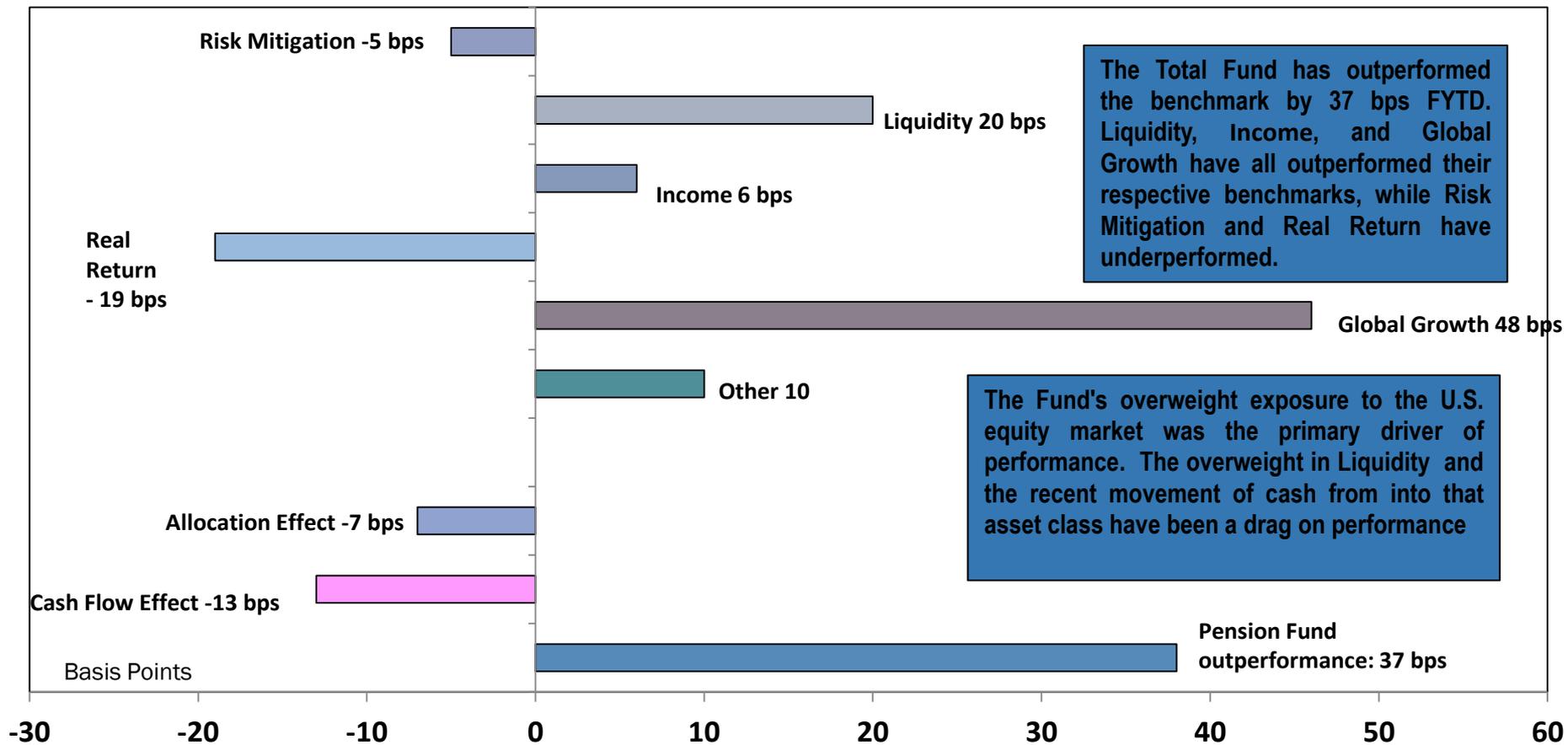
# Fiscal Year to Date Return as of December 31, 2013



Asset Class (thru Dec. 31, 2013)	Nov %	Dec%	FYTD %	1-Year	2-Year	No.
<b>Risk Mitigation</b>	0.72	1.44	(0.11)	5.06	3.87	1
<b>Liquidity</b>	(0.11)	(0.40)	0.28	(3.62)	0.16	2
<b>Income</b>	0.59	0.00	2.76	3.14	6.95	3
<b>Real Return</b>	0.39	1.26	2.86	7.76	7.83	4
<b>Global Growth</b>	2.07	1.99	14.45	23.22	19.99	5
<b>Total Pension Fund ex P&amp;F Mort.</b>	<b>1.43</b>	<b>1.25</b>	<b>9.38</b>	<b>14.60</b>	<b>13.96</b>	6
<b>Total Policy Benchmark</b>	0.78	1.42	9.01	12.43	12.62	7
<b>Estimated Market Value</b>	<b>\$76.8 Billion</b>					8

# Pension Fund Attribution vs. Benchmark

## Fiscal Year to Date through December 31, 2013



Allocation Effect indicates the effect of asset allocation bets, i.e. overweights or underweights vs. the target allocations  
 Cash Flow Effect reflects the impact of cash flows – i.e. money added to or taken from asset classes

# Division of Investment Updates

- Reduced risk and increased cash in the portfolio:
  - Moved from \$1.8 billion overweight position in equities to an underweight and moved from a slight overweight in Investment Grade Credit to a \$500 million underweight relative target weights. Raised over \$3.2 billion in cash since last SIC meeting. Net sellers of:
    - US Equity: \$1,100 million
    - Dev. International Equity: \$725 million
    - Emerging Equity: \$250 million
    - Investment Grade Fixed Income: \$875 million
    - High Yield: \$250 million
  - Increased hedges on the Equity Portfolio
  - Reduced Fixed Income portfolio duration from 6.44 on October 31, 2013 to 5.68 as of January 23, 2014
  - Created new internal portfolio to invest increased cash holdings in short term Treasuries and Corporates
- Rebalanced the optimized Developed Non-US equity portfolio to realign with the November benchmark rebalance. The optimization decreased the risk exposure as measured by predicted Tracking Error from 24 bps to 21 bps.
- Received 59 responses to RFP for Developing Market and International Small Cap Advisors. SIS is currently reviewing responses with objective to narrow list to a manageable number of firms for in depth due diligence.

# January 27, 2014 Asset Allocation

Line #	Asset Class	Long Term Target Range	Current Allocation	FY 2014 Target	Over/Under Weight 2014 Target	Current Assets	Adjustments to Exposure based on Hedges	Total Net Exposure	FY 2014 Target (\$)	Over/Under Weight for 2014	Over/Under Weight (\$) vs. FY 2014 Target w/ Hedges	Line #
1	<b>RISK MITIGATION</b>	<b>0-5%</b>	<b>3.17%</b>	<b>3.50%</b>	<b>-0.33%</b>	<b>2,382,852,761</b>		<b>2,382,852,761</b>	<b>2,634,127,113</b>	<b>(251,274,352)</b>	<b>(251,274,352)</b>	1
2	Absolute Return HFs	0-5%	3.17%	3.50%	-0.33%	2,382,852,761		2,382,852,761	2,634,127,113	(251,274,352)	(251,274,352)	2
3	<b>LIQUIDITY</b>	<b>2-15%</b>	<b>9.05%</b>	<b>4.50%</b>	<b>4.55%</b>	<b>6,810,074,341</b>		<b>5,934,661,132</b>	<b>3,386,734,859</b>	<b>3,423,339,482</b>	<b>3,065,926,982</b>	3
4	Cash Equivalents	0-15%	5.62%	1.00%	4.62%	4,233,000,000		4,233,000,000	752,607,746	3,480,392,254	3,480,392,254	4
5	Common B Short Term	0.00%	0.69%	0.00%	0.69%	518,000,709		518,000,709	0	518,000,709	518,000,709	5
6	TIPS	0-10%	2.07%	2.50%	-0.43%	1,557,854,604		1,557,854,604	1,881,519,366	(323,664,762)	(323,664,762)	6
7	US Treasuries	0-10%	0.67%	1.00%	-0.33%	501,219,028	(357,412,500)	143,806,528	752,607,746	(251,388,718)	(608,801,218)	7
8	<b>INCOME</b>	<b>20-40%</b>	<b>23.14%</b>	<b>26.30%</b>	<b>-3.16%</b>	<b>17,418,806,099</b>		<b>17,418,806,099</b>	<b>19,793,583,732</b>	<b>(2,374,777,633)</b>	<b>(2,374,777,633)</b>	8
9	Investment Grade Credit	8-23%	11.51%	12.10%	-0.59%	8,659,561,275		8,659,561,275	9,106,553,732	(446,992,457)	(446,992,457)	9
10	High Yield Fixed Income	0-10%	5.18%	5.50%	-0.32%	3,896,543,061		3,896,543,061	4,139,342,606	(242,799,545)	(242,799,545)	10
11	Credit-Oriented HFs	0-6%	3.22%	3.50%	-0.28%	2,425,698,815		2,425,698,815	2,634,127,113	(208,428,298)	(208,428,298)	11
12	Debt-Related PE	0-4%	1.11%	2.00%	-0.89%	834,609,165		834,609,165	1,505,215,493	(670,606,328)	(670,606,328)	12
13	Debt Related Real Estate	1-4%	0.99%	2.00%	-1.01%	746,009,941		746,009,941	1,505,215,493	(759,205,552)	(759,205,552)	13
14	P&F Mortgage	--	1.14%	1.20%	-0.06%	856,383,842		856,383,842	903,129,296	(46,745,454)	(46,745,454)	14
15	<b>REAL RETURN</b>	<b>3-12%</b>	<b>5.96%</b>	<b>6.00%</b>	<b>-0.04%</b>	<b>4,483,286,722</b>		<b>4,483,286,722</b>	<b>4,515,646,479</b>	<b>(32,359,757)</b>	<b>(32,359,757)</b>	15
16	Commodities/RA	2-7%	2.61%	2.50%	0.11%	1,962,175,451	0	1,962,175,451	1,881,519,366	80,656,085	80,656,085	16
17	Equity Related Real Estate <sup>1</sup>	2-7%	3.35%	3.50%	-0.15%	2,521,111,271		2,521,111,271	2,634,127,113	(113,015,842)	(113,015,842)	17
18	<b>GLOBAL GROWTH</b>	<b>45-65%</b>	<b>58.46%</b>	<b>59.70%</b>	<b>-1.24%</b>	<b>43,999,010,455</b>		<b>43,841,868,626</b>	<b>44,930,682,464</b>	<b>(931,672,009)</b>	<b>(1,088,813,838)</b>	18
19	US Equity	15-35%	27.33%	26.50%	0.83%	20,568,815,353	(142,014,136)	20,426,801,217	19,944,105,281	624,710,072	482,695,936	19
20	Non-US Dev Market Eq	8-20%	13.13%	12.70%	0.43%	9,879,219,924	(10,638,207)	9,868,581,717	9,558,118,380	321,101,544	310,463,337	20
21	Emerging Market Eq	5-15%	6.79%	8.00%	-1.21%	5,109,887,316	(4,489,486)	5,105,397,830	6,020,861,972	(910,974,656)	(915,464,142)	21
22	Equity-Oriented HFs	0-8%	4.07%	4.00%	0.07%	3,061,269,900		3,061,269,900	3,010,430,986	50,838,914	50,838,914	22
23	Buyouts/Venture Cap <sup>2</sup>	4-10%	7.15%	8.50%	-1.35%	5,379,817,962		5,379,817,962	6,397,165,845	(1,017,347,883)	(1,017,347,883)	23
24	<b>OTHER</b>	<b>0.00%</b>	<b>0.22%</b>	<b>0.00%</b>	<b>0.22%</b>	<b>166,744,269</b>		<b>166,744,269</b>	<b>0</b>	<b>166,744,269</b>	<b>166,744,269</b>	24

<sup>1</sup> Current assets do not include receivables of \$417 million primarily related to Real Estate secondary sale

<sup>2</sup> Current assets do not include receivables of \$68 million primarily related to Private Equity secondary sale

Based on estimated values

# State Investment Council

## Notifications

# Alternative Investment Notifications

## ❑ **GLP China Logistics Fund I**

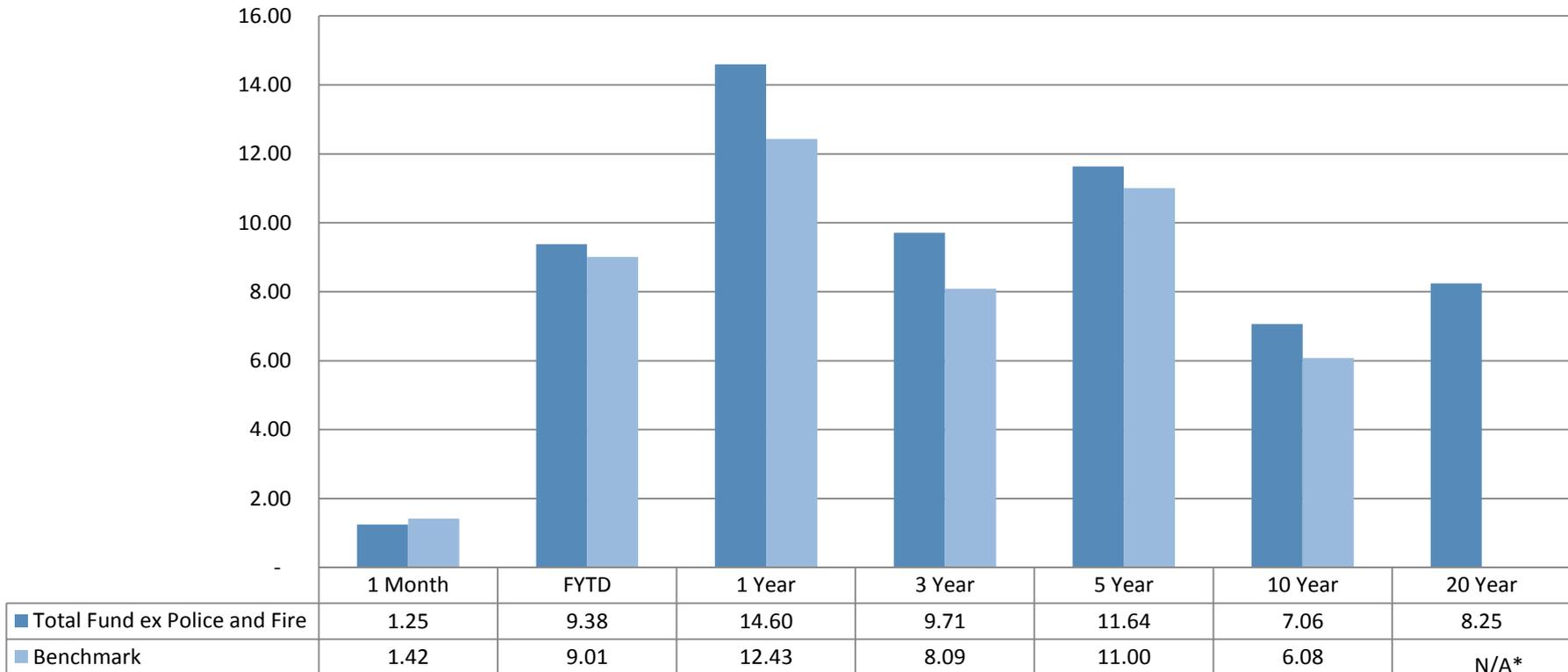
- ❑ On September 19, 2013 the Division presented a commitment of \$75 million to GLP China Logistics Fund I to the State Investment Council.
- ❑ GLP and its prospective limited partners were working with a very truncated timeline to close the fund in early November.
- ❑ The Division worked diligently to meet the timeline and was ready and able to close; however, there were significant legal hurdles on both sides that could not be overcome in time to close on the investment. Therefore the Division will not be investing in this fund.

### **Purpose of Notification:**

The Division is notifying the SIC of these activities under its Modification Procedures.

# Performance Appendix

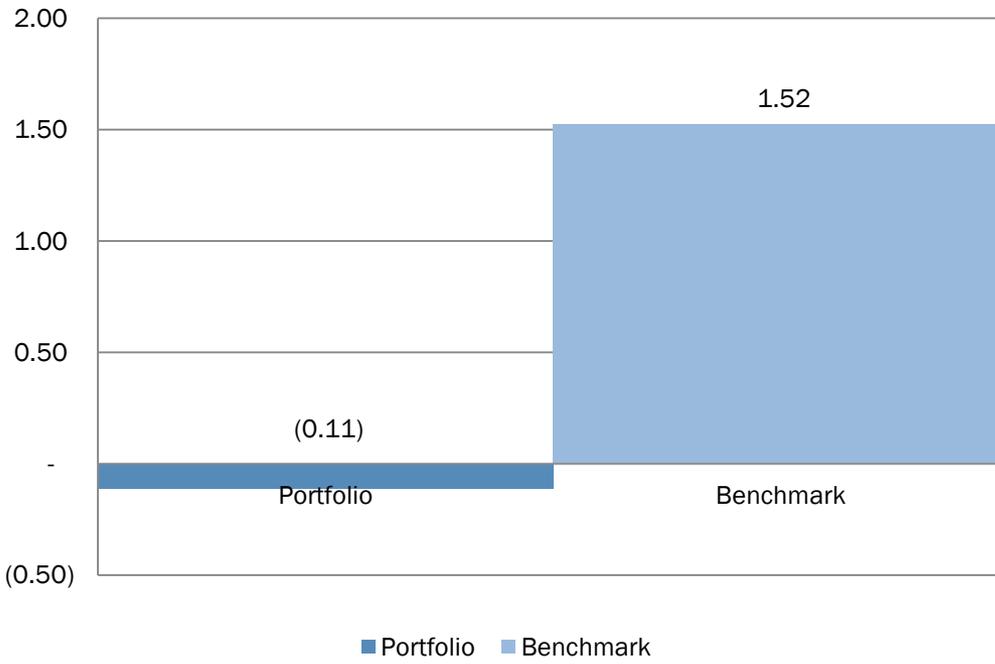
# Total Fund ex Police and Fire Mortgage Performance as of Dec 31, 2013



- The Total Fund ex Police and Fire returned 1.25% in December to bring the Fiscal Year to Date return to 9.38% and the Calendar Year return to 14.60%.
- The Fund has outperformed the benchmark for the fiscal year and calendar year to date.
- The Fund is ahead of the benchmark for all periods shown.

\*Benchmark return not available for 20-Year period

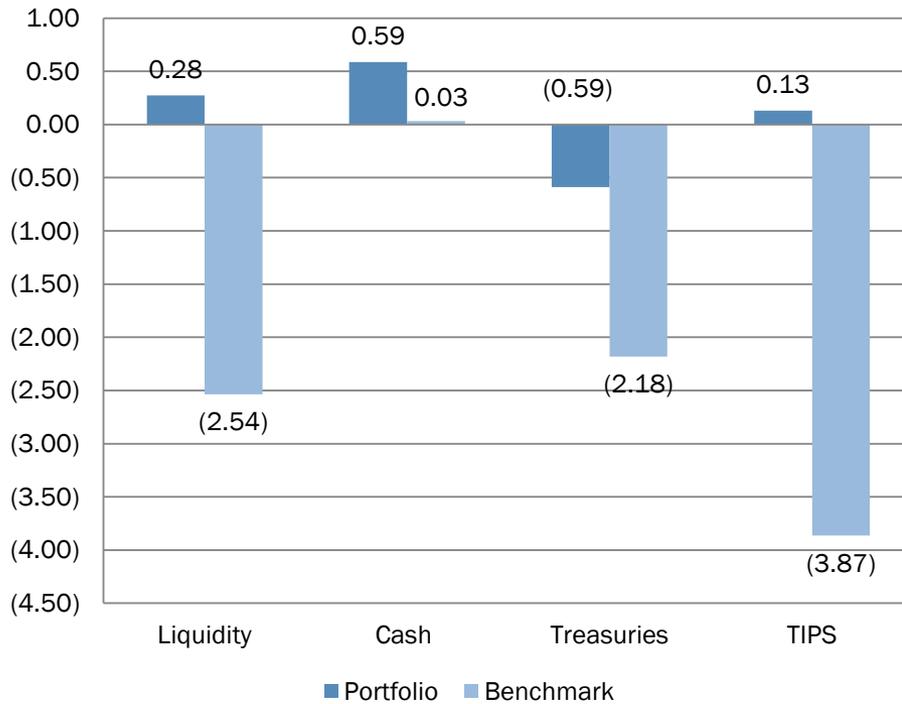
**Risk Mitigation FYTD Performance as of Dec 31, 2013**



Returns as of Dec 31, 2013	1 Month	FYTD	CYTD	1 Year	2 Year
Absolute Return Hedge Funds	1.44	(0.11)	5.06	5.06	3.87
Fund of Fund Lag	0.34	2.05	4.14	4.14	4.18
<i>Difference</i>	1.10	(2.16)	0.92	0.92	(0.32)

- The Risk Mitigation return is composed of the returns of the Absolute Return Hedge Funds. The returns are generally reported on a one month lag for direct funds and one to two months for fund of funds.
- The Absolute Return Hedge Funds as a group have returned -0.11% FYTD and 5.06% CYTD in what has been a challenging environment for macro oriented managers. CTA funds have outperformed discretionary macro funds over these periods.

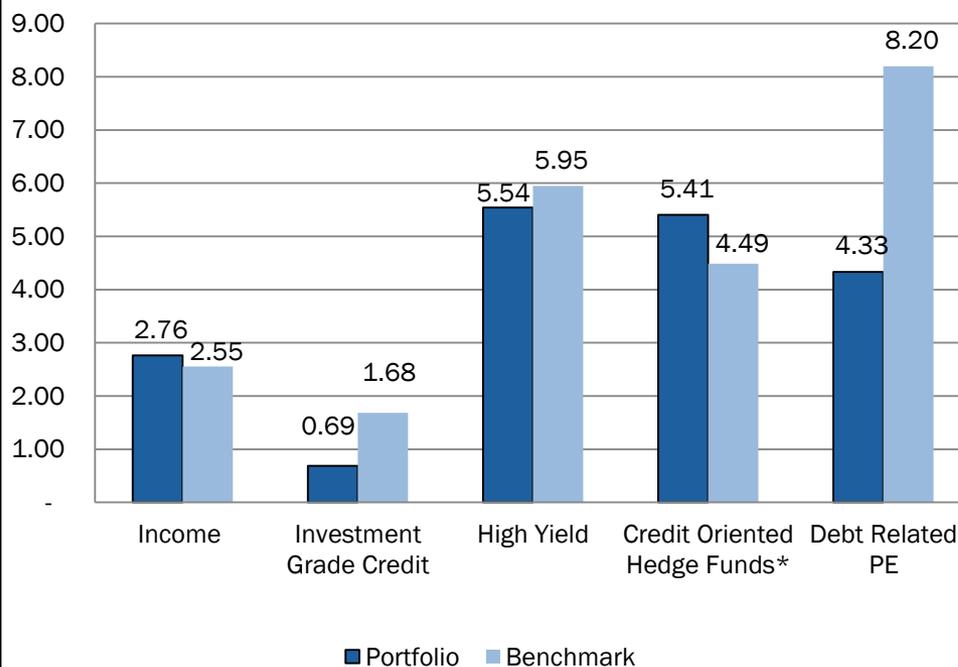
### Liquidity FYTD Performance as of Dec 31, 2013



Returns as of Dec 31, 2013	1 Month	FYTD	CYTD	1 Year	2 Year
Cash Equivalents	0.03	0.59	2.04	2.04	2.182
91 day treasury bill	0.01	0.03	0.07	0.07	0.092
<i>Difference</i>	<i>0.02</i>	<i>0.56</i>	<i>1.97</i>	<i>1.97</i>	<i>2.09</i>
US Treasuries	(0.25)	(0.59)	(6.22)	(6.22)	0.669
Custom Benchmark	(1.25)	(2.18)	(6.08)	(6.08)	2.292
<i>Difference</i>	<i>1.00</i>	<i>1.59</i>	<i>(0.14)</i>	<i>(0.14)</i>	<i>(1.62)</i>
TIPS	(1.43)	0.13	(8.84)	(8.84)	0.828
Custom Tips Benchmark	(2.14)	(3.87)	(16.19)	(16.19)	(4.55)
<i>Difference</i>	<i>0.71</i>	<i>4.00</i>	<i>7.36</i>	<i>7.36</i>	<i>5.38</i>

- The Liquidity portfolio has outperformed the benchmark by 281 basis points FYTD as all three segments of the portfolio have outperformed their respective benchmarks.
- An overweight to cash has helped performance as cash has outperformed both Treasuries and TIPS for the period.
- The TIPS portfolios has benefited from having a longer duration than the benchmark.

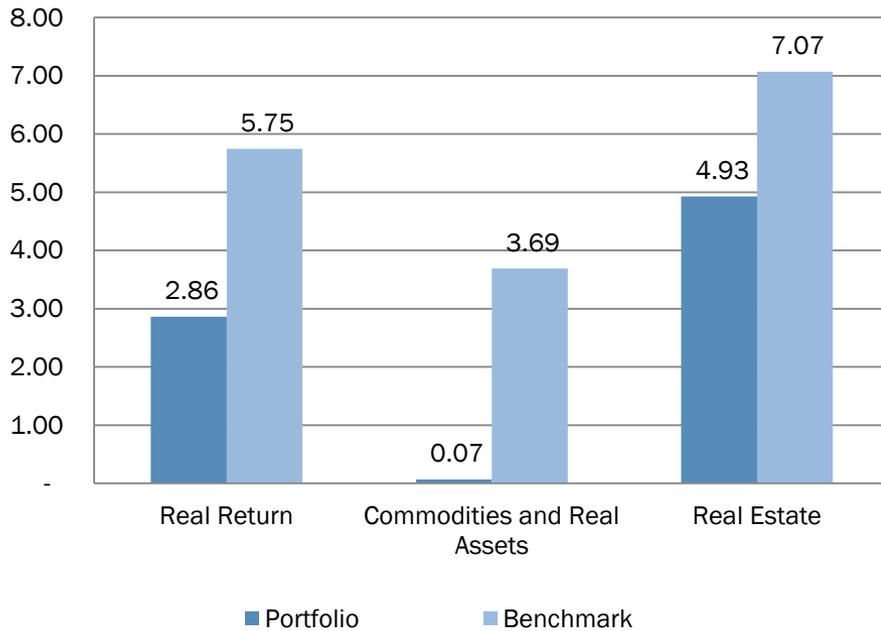
## Income FYTD Performance as of Dec 31, 2013



Returns as of Dec 31, 2013	1 Month	FYTD	CYTD	1 Year	2 Year
Investment Grade Credit	(0.67)	0.69	(3.32)	(3.32)	2.53
Custom IGC Benchmark	(0.36)	1.68	(3.46)	(3.46)	3.07
<i>Difference</i>	<i>(0.31)</i>	<i>(0.99)</i>	<i>0.14</i>	<i>0.14</i>	<i>(0.54)</i>
High Yield	0.53	5.54	11.40	11.40	15.55
Barclays Corp High Yield (Daily)	0.54	5.95	7.45	7.45	11.55
<i>Difference</i>	<i>(0.01)</i>	<i>(0.40)</i>	<i>3.95</i>	<i>3.95</i>	<i>4.00</i>
Credit-Oriented Hedge Funds*	1.49	5.41	16.21	16.21	14.68
Fund of Fund Lag	1.13	4.49	13.74	13.74	11.50
<i>Difference</i>	<i>0.36</i>	<i>0.92</i>	<i>2.47</i>	<i>2.47</i>	<i>3.18</i>
Debt-Related Private Equity	0.49	4.33	21.10	21.10	18.71
Cambridge Assoc. PE Qtr Lag	5.06	8.20	16.98	16.98	16.40
<i>Difference</i>	<i>(4.57)</i>	<i>(3.87)</i>	<i>4.12</i>	<i>4.12</i>	<i>2.31</i>

- The Income portfolio has outperformed the benchmark by 21 basis points FYTD.
- The Investment Grade Credit portfolio has underperformed the benchmark FYTD as the portfolio has a lower-beta, higher quality securities and very minimal exposure to the financial sector. This positioning has caused the portfolio to underperform in what has been a risk on environment.
- Both traditional high yield and alternative high yield portfolios have performed well FYTD, up in excess of 5%. Over the trailing one and two year periods, alternative high yield allocations have drive the outperformance.
- Outperformance for the Credit Oriented Hedge Fund portfolio has been driven by managers with higher net exposure.

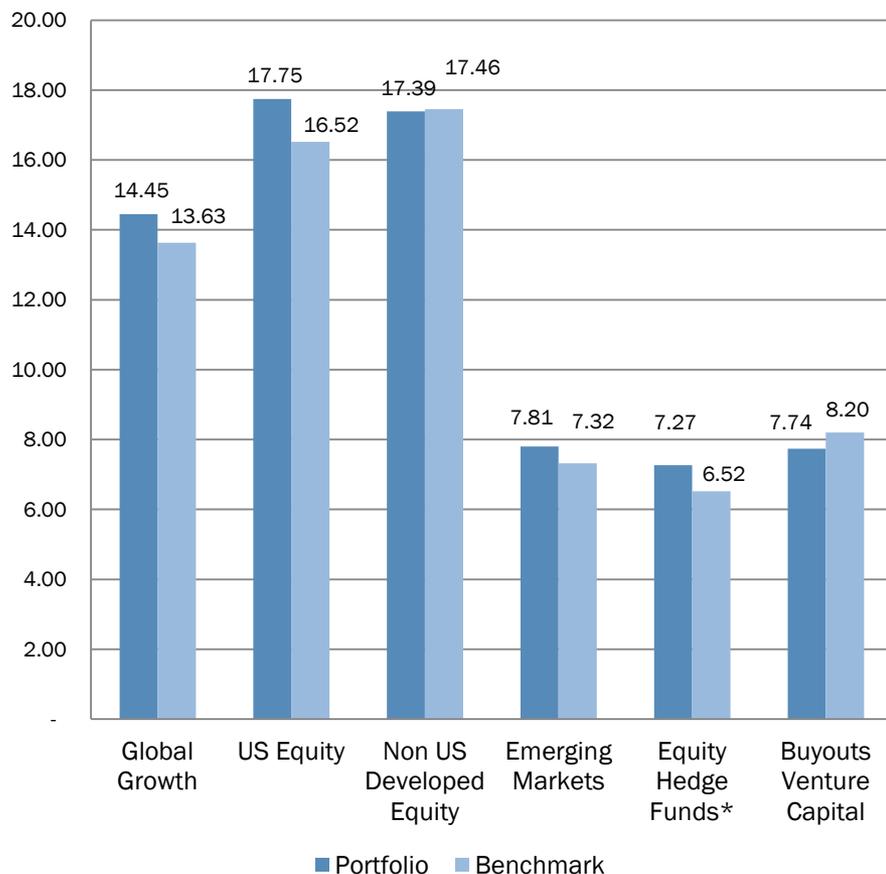
### Real Return FYTD Performance as of Dec 31, 2013



Returns as of Dec 31, 2013	1 Month	FYTD	CYTD	1 Year	2 Year
Commodities & Real Assets	(0.31)	0.07	(5.55)	(5.55)	(1.58)
Custom Real Return Index	2.80	3.69	5.19	5.19	4.16
<i>Difference</i>	(3.11)	(3.62)	(10.74)	(10.74)	(5.74)
Real Return Real Estate	2.41	4.93	16.44	16.44	12.94
Real Estate Benchmark	3.35	7.07	12.97	12.97	11.75
<i>Difference</i>	(0.95)	(2.14)	3.47	3.47	1.19

- The Real Return portfolio underperformed by 290 basis points FYTD, however, since the bulk of the portfolio is reported on a lag, the Division believes the performance of the portfolio is understated.
- Commodity performance as hurt by strategies tied to long commodity indices, which performed poorly.

### Global Growth FYTD Performance as of Dec 31, 2013



Returns as of December 31, 2013	1 Month	FYTD	CYTD	1 Year	2 Year
Domestic Equity	2.85	17.75	34.02	34.02	25.51
S&P 1500 Super Composite (Daily)	2.54	16.52	32.80	32.80	24.21
<i>Difference</i>	0.31	1.23	1.22	1.22	1.31
Non-US Dev Market Eq	1.52	17.39	22.12	22.12	20.01
NJDI ex Iran& Sudan EAFE + Canada	1.42	17.46	21.52	21.52	19.24
<i>Difference</i>	0.10	(0.07)	0.60	0.60	0.76
Emerging Market Eq	(0.73)	7.81	(2.94)	(2.94)	8.10
NJDI Iran + Sudan Free EM Index	(1.44)	7.32	(2.38)	(2.38)	8.25
<i>Difference</i>	0.71	0.49	(0.56)	(0.56)	(0.15)
Total Equity Oriented Hedge Funds*	2.09	7.27	18.49	18.49	13.28
HFRI Fund Of Funds Lag	0.68	6.52	6.57	6.57	
<i>Difference</i>	1.41	0.74	11.92	11.92	13.28
Buyouts-Venture Capital	2.48	7.74	18.92	18.92	15.59
Cambridge Associates PE 1 Qtr Lag	5.06	8.20	16.98	16.98	16.4
<i>Difference</i>	(2.59)	(0.46)	1.94	1.94	(0.81)

- The Global Growth portfolio has outperformed the benchmark 82 basis points FYTD. The Fund's overweight to Global Growth, in particular US and Developed non-US equity, has positively impacted total fund performance FYTD.
- The Domestic Equity portfolio is ahead of the benchmark by 123 basis points FYTD.
- The Developed Market Non US equity portfolio is behind the benchmark by 7 basis points FYTD. The total Developed Non US Equity portfolio is ahead of the benchmark by over 60 basis points on a trailing one year basis.
- The Emerging Markets portfolio had a strong month of relative performance in December, which moved the portfolio ahead of the benchmark FYTD.

\*Reported on a one month lag