

December 14, 2007

MEMORANDUM TO: State Investment Council

FROM: William G. Clark
Director

SUBJECT: **Proposed Private Equity Investment in The Resolute Fund II, LP and Carlyle Mezzanine Partners II, LP.**

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 two proposed private equity investments: a \$100 million commitment to The Resolute Fund II, L.P and a \$75 million commitment to Carlyle Mezzanine Partners II, LP.

Please note that these investments will be authorized pursuant to Articles 69 and 90 of the Council's regulations. The investment in Resolute will be considered a "Buyout Fund" investment, while the Carlyle fund will be a "Debt related" investment as defined under N.J.A.C. 17:16-90.1.

The Alternative Investments Procedures adopted by the Council on January 20, 2005 require any potential alternative investment opportunities to be identified and initially evaluated by the Head of Alternative Investments of the Division (myself in an acting capacity) and the applicable Asset Class Consultant (Strategic Investment Solutions for private equity, or "SIS") in coordination with the DOI Investment Committee (Ike Michaels, Deputy Director and myself).

Based on this due diligence, the Division has determined that these proposed investments meet the criteria for investments set forth in the Council's Alternative Investment Policy.

The Resolute Fund II, LP is a middle-market partnership, which will seek to employ a hands-on, value added operational strategy to generate attractive investment returns. The principal hallmarks of the partnership are the experience, success and continuity of the team. The managing principals have been investing together in private equity transactions at The Jordan Company (TJC) for as many as 25 years, with the most recently added managing principal having joined the firm more than 16 years ago. In addition to the managing principals, TJC employs six senior investment professionals with an average tenure at the firm of approximately ten years and six junior investment professionals. This experience investing over market cycles, has generated consistent, attractive risk-adjusted returns that are largely a function of the managing principals' discipline and experience set.

Carlyle Mezzanine Partners II, LP (CMP II) is a proposed "re-up" with the Carlyle Group's mezzanine team. NJDOI committed \$50 million to CMP I which thus far is performing to plan. CMP II will seek to follow the same strategy as Fund I, investing largely in the subordinated debt of middle-market companies with leading, defensible market positions, sustainable cash flows, margins and profitability. The managing partners of CMP successfully invested Fund I in a difficult environment for mezzanine type investments and, given that credit spreads have now widened and loan terms have become more stringent, the opportunity set and the terms for mezzanine investments are now more attractive. We believe the partners of CMP in fund II will be able to capitalize on this current environment.

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 the proposed investments meet the criteria for investments set forth in the Alternative Investments Policy.

A formal written due diligence report for these proposed investments was sent to each member of the Investment Policy Committee of the Council on December 7, 2007, and a meeting of the Committee was held on December 12, 2007. In addition to the formal written due diligence reports, all other information obtained by the Division on this investment 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 4 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 will not be reached with one or both of the general partners.

We look forward to discussing the proposed private equity investment at the Council's December 20, 2007 meeting.

WGC:cpp
Attachment