

New Jersey State Investment Council

October 4, 2017 Regular Meeting

Minutes of the Regular Meeting

Held October 4, 2017 at the War Memorial, George Washington Ballroom, 1 Memorial Drive, Trenton, New Jersey.

Council Members in Attendance:

Brendan T. Byrne, Jr., Chair
Adam Liebttag, Vice Chair
Thomas Bruno Jr. (via telephone)
Michael Cleary
Charles Dolan (via telephone)
Michael Greaney
James Hanson
Guy Haselmann
James Joyner
Timothy McGuckin
Brady Middlesworth
Jeffrey Oram
Eric Richard
Mitchell Shivers

Roll Call and Meeting Notice

The Regular Meeting was called to order by Brendan T. Byrne, Jr., Council Chair, at 10:09 a.m. Ernestine Jones-Booker, Council Secretary, performed roll call reported that notice of the Regular Meeting scheduled for October 4, 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 September 1, 2017. A copy of the notice was posted at the Division and is on file.

Minutes of the Regular Meeting held July 27, 2017

Mr. Byrne presented for adoption the minutes for the regular meeting held July 27, 2017. Mr. Byrne made a motion to approve the minutes, with Mitchell Shivers seconding the motion. All Council Members present voted in favor, except for Thomas Bruno, Jr., who abstained. James Joyner joined the meeting after adoption of the minutes.

Opening Remarks by Chair

Mr. Byrne made some brief opening remarks, announcing a net return of 13.07 percent (unaudited) for Fiscal Year 2017. He noted that the fund's average returns were above the median for public funds and in the top quartile of funds when adjusted for risk. Mr. Byrne commended Division staff for its creativity and hard-nosed bargaining, referring to the Division's recent recognition for its innovative FAIR Program and Owl Rock initiative. Mr. Byrne welcomed Mr. Bruno back to the Council. He thanked Ned Thomson for his short tenure with the Council, and stated that New Jersey residents would benefit from Mr. Thomson's actuarial background in the Legislature.

Election of Chair and Vice Chair

Jeffrey Oram reported that the Nominating Committee, consisting of himself, Guy Haselmann and Timothy McGuckin, met telephonically on October 3rd and decided to nominate Mr. Byrne to continue to serve as Chair and Adam Liebttag to

New Jersey State Investment Council

October 4, 2017 Regular Meeting

continue to serve as Vice Chair of the Council. Mr. Bruno made a motion to close nominations that was seconded by Mr. Shivers. All members of the Council present voted in favor of the motion. Mr. Byrne was elected as Chair by all members of the Council present, with the exception of Eric Richard, who abstained. Mr. Liebttag was elected as Vice Chair by all members of the Council present.

Appointments of Members to Council Committees

Mr. Byrne reappointed himself, Mr. Liebttag, Mr. Haselmann, Mr. McGuckin, Mr. Oram and Mr. Shivers to the Executive and Investment Policy Committees; and he reappointed Michael Cleary, Charles Dolan, Michael Greaney, James Hanson and Mr. McGuckin to the Audit Committee.

2018 Proposed State Investment Council Meeting Dates

Mr. Byrne presented a tentative meeting schedule for 2018. Director Chris McDonough noted that the meetings were being scheduled on Thursdays instead of Wednesdays in order to provide staff with more time to prepare meeting materials.

Director's Report and Update Presentations

Mr. McDonough presented the Director's Report, providing an update on the performance of the portfolio as a whole and the performance of specific asset classes. He compared the Pension Fund's performance, including its long term performance per unit of risk, to that of other large pension funds. Mr. Byrne asked how the Division characterizes global diversified credit in relation to other asset classes. Mr. McDonough explained that the global diversified credit asset class is similar to the high yield bond asset class, but with less liquidity. He stated the global diversified credit investments have outperformed the high yield market historically.

Brian Arena of the Division presented an overview of the domestic equity portfolio for Fiscal Year 2017. Mr. Byrne and Mr. Haselmann congratulated Mr. Arena's team for its strong performance over a long period of time. Mr. Byrne asked how proposed changes in tax law will affect companies in the S&P index (large cap) versus the Russell index (small cap). Mr. Arena responded that generally tax changes benefit smaller companies, especially if they encourage acquisitions, but certain proposed changes (e.g., changes encouraging the repatriation of cash) will benefit larger companies as well. Additionally, at the request of Mr. Byrne, Mr. Arena provided an estimate of about 1.04% beta of the domestic portfolio.

Melanie Lomas of the Division presented an overview of the international equity portfolio for the past fiscal year. Mr. Haselmann inquired whether the Division hedges all of its currency risk, to which Ms. Lomas answered that at times the Division will hedge currencies, however, currently the Division did not have currency hedges in place due to the uncertainty of currency movements, particularly as there are questions pertaining to the sustainability of the US dollar's recent strength. Mr. Haselmann emphasized the importance of weighing currency risk going forward. In response to an inquiry from Mr. Shivers, Ms. Lomas reported a positive net impact on the portfolio from currency hedging in Fiscal Year 2017. At Mr. Oram's request, Ms. Lomas described the risk profile of the emerging market portfolio relative to the benchmark.

Tim Patton, Kevin McGrath and Michael Pascucci of the Division discussed the fixed income portfolio. Mr. Haselmann lauded the team's ability to generate consistent returns in a difficult environment. Mr. McGrath responded to an inquiry from Mr. Hanson describing the allocation among different rating categories. Mr. Byrne inquired about liquidity in the

New Jersey State Investment Council

October 4, 2017 Regular Meeting

high yield market, to which Mr. McGrath responded that liquidity varies depending on the investment, but noting that even the most liquid investments are difficult to sell during times of stress. Mr. Shivers asked about the effect of illiquidity on the accuracy of valuations, to which Mr. McGrath described the various mechanisms used by the market to assess value. Finally, in response to a comment from Mr. Byrne, Mr. McGrath described the turnover within the below investment grade space.

Deputy Director Corey Amon provided a public markets outlook, and Mr. McDonough provided an update on capital market performance, portfolio performance and asset allocation for the current fiscal year. Mr. Haselmann disagreed with the Division's optimistic outlook, citing to the high ratio of equity market capitalization relative to GDP and various global socioeconomic risk scenarios, and expressed his concern that financial market valuations has skewed the assessment of the risk/reward profile of various asset classes. Mr. Byrne noted the strong disagreements in outlook among various experts, and stated that diversification of the portfolio is intended to manage the risk of mistiming changes in the markets.

Mr. McDonough updated the Council regarding the receipt of proceeds from the lottery enterprise and the State's quarterly pension contribution. Mr. McDonough also notified the Council of modifications to Fairview Capstone Partners, L.P., Fairview Capstone Partners II, L.P., and Dyal III NJ Investors LP.

State of New Jersey Cash Management Fund

Linda Brooks of the Division presented an overview of the State of New Jersey Cash Management Fund (CMF), discussing the purpose of the Fund, its history, its permitted types of investments, and its recent performance. Mr. Byrne and Mr. Haselmann thanked Ms. Brooks for her efforts. In response to questions from Mr. Haselmann and Mr. Oram, Ms. Brooks stated that the CMF did not use margin and did not invest in repurchase agreements. Mr. Shivers asked if the CMF was able to transact directly with other funds administered by the Division, to which Ms. Brooks answered that it did so.

Real Assets Investment

Stonepeak Infrastructure Fund III, L.P.

Kevin Higgins of the Division, along with Matt Coyne of TorreyCove, presented an investment of up to \$125 million in Stonepeak Infrastructure Fund III L.P., a fund focusing on infrastructure assets in North America. Mr. Higgins described the fund's investment strategy and the background and experience of the investment team. He also described the returns of prior funds and the attractive terms of the investment. Mr. Hanson praised the fund's adherence to ESG principles, and inquired about the increase in fund size from prior funds. Mr. Higgins and Mr. Coyne responded that the increased fund size was intended to eliminate the need for third-party capital. At the request of Mr. Byrne, Mr. Higgins outlined the Division's process for selecting infrastructure funds. Mr. Byrne also asked about the fund's exit strategy for investments, to which Mr. Higgins and Mr. Coyne described the long-term nature of the fund's investments. Mr. Byrne reported that the IPC had discussed the investment and was satisfied that appropriate and adequate due diligence had been performed.

Private Equity Investment

TPG Growth IV, L.P. and TPG Rise Fund, L.P.

Mr. Pascucci, along with Michelle Davidson of TorreyCove, presented an investment of up to \$125 million in TPG Growth IV, L.P. and up to \$75 million in TPG Rise Fund, L.P., both of which are small and middle-market growth equity and buyout funds managed by TPG Growth. Mr. Pascucci and Ms. Davidson described the expertise and historical performance of the funds' investment team, the funds' investment strategy, and the terms of the investments. Mr. Byrne asked whether the

New Jersey State Investment Council

October 4, 2017 Regular Meeting

Rise Fund was unique within the private equity space and questioned how the allocation among the two funds was determined. Mr. Pascucci responded that other funds have a similar strategy, but not with the same level of resources or expertise, and stated the allocation was based pro rata on the total size of each fund. Mr. Byrne reported that the IPC had reviewed the investment and was satisfied that appropriate and adequate due diligence had been performed.

Private Debt Investment

Chatham Private Debt and Strategic Capital Fund

Jessie Choi of the Division and Pete Kelioutis of Cliffwater presented an investment of up to \$200 million in Chatham Private Debt and Strategic Capital Fund, a fund focused on stressed and distressed investing as well as direct lending to middle market companies. Ms. Choi and Mr. Kelioutis described the fund's investment team and its successful track record, the fund's investment strategy, and the investment's favorable terms. Mr. Byrne reported that the IPC had reviewed the investment and was satisfied that appropriate and adequate due diligence had been performed.

Proposed Revisions to Procurement Procedures

Mr. Amon presented an update to the Division's Procurement Procedures for Investment Advisers and Consultants to include securities lending agents under the procedures. At the request of Mr. Byrne, Mr. Amon summarized the Division's securities lending program. Mr. Byrne made a motion to approve the revised procedures as presented, with Mr. Shivers seconding the motion. All members of the Council present voted in favor.

Annual Report on Sudan Divestment Law

Susan Sarnowski of the Division presented the Division's annual report to the Legislature concerning investments in companies engaged in business in Sudan. Ms. Sarnowski reported that there were no divestments in the past year and no current holdings that were in violation of the applicable statute.

Treasurer's Report

Dr. Marc Miles of the State Treasurer's office reported on the State's labor and housing markets and revenue forecasts. Dr. Miles provided an update on the status of the State's pension fund contribution and described initiatives to modernize the Division of Taxation and redesign the website for the Division of Pensions and Benefits. Dr. Miles welcomed feedback on these initiatives.

Public Comment

Jacob Toporek, Executive Director of the New Jersey State Association of Jewish Federations, spoke regarding the pension funds' investment in Danske Bank. Mr. Byrne asked Mr. McDonough to engage the Attorney General's office to determine whether the investment in Danske Bank was in violation of P.L. 2016, chapter 24.

Michael Malloy and Newell Benedict of the New Jersey Retired Public Employees Organization (NJRPEO) spoke regarding employer contributions to the pension plan and a proposed reorganization of the Division of Investment and the Division of Pensions and Benefits within the State government. Mr. Haselmann clarified his comments at a prior Council meeting regarding the effect of pension fund underfunding on the Council's ability to make asset allocation decisions.

Adjournment

Mr. Byrne 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 12:45 p.m.