

**New Jersey State Investment Council  
Minutes of the Regular Meeting  
March 18, 2010**

**Held at Rutgers Student Center, Room 411 ABC  
126 College Avenue, New Brunswick, New Jersey 08901**

Council Members in Attendance:

Orin Kramer, Chair  
Jonathan Berg, Vice Chair  
Mark Kandrak  
James C. Kellogg (participated by phone)  
Karl Kleeberg  
Douglas A. Love  
James P. Marketti  
Timothy McGuckin

Council Members Absent:

James Clemente  
Susan Crotty

**The Regular Meeting was called to order by Chair Kramer at 3p.m.**

**Meeting Notice**

Council Secretary Susan Burrows reported that notice of the Regular Meeting scheduled for March 18, 2010 was sent by mail deposited in the post office, by facsimile and email on March 1, 2010. A copy of the notice is on file as posted in the Division and sent to the Council, the **Times of Trenton**, **The Star-Ledger**, the **Bergen Record**, the **Courier Post** and the Secretary of State.

**Meeting Minutes**

Acting Director Joseph noted that the word "range" was missing on page 2. The minutes of the regular meeting of the Council held on January 21, 2010 were approved unanimously, as amended, on a motion by Council Member Kandrak and seconded by Council Member Love.

**Annual Report**

*Draft of Annual Report for Fiscal and Calendar Year 2009*

Mr. Joseph addressed the Council regarding the draft annual report for fiscal and calendar year 2009. In referencing the fund expenses on page 23, Council Member Marketti asked for an explanation for why the private equity and real estate fund management fees are not available by fund. Acting Director Joseph explained that the Division does not calculate the information for each fund in the aggregate form; however, the information is made available to the Division at the time of every capital call. Mr. Marketti asked if he could review the existing records, and it was agreed that he could. A discussion followed between Mr. Marketti and Chair Kramer about the fees in relation to returns of the alternative investment program.

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Council Member Kandrac inquired if there was data available to compare the costs of assets under management for the Division against the costs for other institutional funds, and more specifically, state pension systems. Chair Kramer stated that if you look at the fourteen public pension funds with assets greater than \$40 billion, the expense basis is significantly higher as these funds are paying for diversification (e.g., through alternative investments). Candace Straight (Governor's liaison to the Council) inquired if there was a study available that has this information. Acting Director Joseph stated that RV Kuhns has such a study which could be made available. Council Member Marketti asked what the cost was prior to the alternative investments. Chair Kramer responded that it was 6 basis points, but that this was during the period that the New Jersey portfolio had much higher volatility, below-average risk-adjusted returns and lacked its current diversification.

Council Member Kandrac inquired about the relationship between the five and ten year returns of 3.10% and 2.34%, respectively, cited in the report and the average rate of return of 8.25% used by the actuaries. Chair Kramer noted that the five year return compared favorably relative to the fund's peers, putting it in the top ten percentile. He also noted that, in 2002, the Council passed a resolution to put together a portfolio that would generate the most attractive risk adjusted return, regardless of the projected return rate set statutorily for the actuary. Council Member Love stated that the actuarial return is a planning number used for assets and contributions. He noted that the number is used for projecting far into the future, which is problematic in the public sector. Council Member Kandrac stated that given the current outflows, and absent contributions, it is recipe for disaster and a real concern. Acting Director Joseph pointed out that the fund paid out \$6.6 billion in benefit payments which presents a challenge in balancing liquidity and returns.

The annual report draft was unanimously approved on a motion by Council Member Berg, seconded by Council Member Love.

**Non-agenda discussion item**

Chair Kramer asked if there were any comments on the draft letter he circulated which was addressed to Chairman Dodd of the Senate Banking Committee and Ranking Minority Member Shelby reiterating Council positions on several governance matters. The letter was unanimously approved as representing the Council's governance positions on a motion by Council Member Marketti, seconded by Council Member Kandrac.

**Investment Plan**

*Investment Plan for Fiscal Years 2010-2011*

Acting Director Joseph presented the investment plan for the remainder of fiscal year 2010 and fiscal year 2011. The plan includes a reduction in large cap and developed international equities to improve the risk profile of the fund, with an increase in fixed income, hedge fund and commodity related investments. Council Member Love inquired if there was any specific language on fixed income duration. Acting Director Joseph replied that this was intentionally left open due to the concern of rising rates. It was confirmed to Council Member Kandrac that the proposed Investment Plan was the unanimous recommendation of the Investment Policy Committee.

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Council Member Kellogg questioned whether the Council should adopt a new plan prior to the naming of a Director. Chair Kramer responded that it is a core Council responsibility to give guidance on asset allocation and that he thought it would be bad governance to wait. Council Member Berg noted that it could be months before a decision was made regarding the Director position. Chair Kramer also stated that the Council could revise the plan at any time, as it had done during the last fiscal year. Council Member Love further clarified that this is a policy decision as opposed to a tactical or market timing decision. It was agreed that Acting Director Joseph would revise the third paragraph of the cover page to include a reason for the proposed increase in hedge funds and commodity/real asset related investments at the request of Council Member Kandrac. Council Member Marketti stated that he opposes the plan in its present form since it increases the alternatives space. A discussion about the expected returns and risk used to formulate the plan ensued between Council Members Marketti and Love, and Pete Keliuotis of SIS. A motion to adopt the plan was made by Council Member Love, with a second by Council Member Berg. Chair Kramer and Council Members Berg, Kandrac, Kleeberg, Love and McGuckin voted to approve the investment plan. Council Members Kellogg and Marketti voted against the plan.

**Proposed Real Asset Investments**

*Memorandum "Proposed Investment in a Commodity-Linked Note Issued by Cargill, Inc." dated March 12, 2010*

Acting Director Joseph reported that a swap program with Cargill, originally proposed on May 16, 2008, could not be accommodated due to operational issues. The Division is now proposing to invest in a commodity-linked note, which is basically a fixed income security that pays the principal, plus or minus the change in the underlying index, at a fixed maturity date. The Division has invested in commodity-linked notes in the past. DAG Weiner stated that the documents are under legal review in response to a question by Ms. Straight regarding how quickly this investment could be closed.

*Memorandum "Proposed Investments in Additional Commodity-Linked Notes" dated March 12, 2010*

Acting Director Joseph stated that the Division was proposing to invest in \$350 million of additional commodity-linked notes with other issuers that meet certain stated criteria. Council Member Kellogg proposed that the maturity should be up to 1.5 years and other issuers, such as General Electric, should be considered. Council Member Love clarified that that the issuers of these notes actually actively manage their portfolios through selective hedging against the index, requiring specific expertise.

**Proposed Alternative Investments**

*Memorandum "Proposed Hedge Fund Investments in Brevan Howard Master Fund Limited and Pershing Square, LP" dated March 12, 2010*

Acting Director Joseph stated that the Brevan Howard fund is a global macro fund, in which the Division is already invested through its investment in the Goldman Sachs multi-strategy fund. The Division's Hedge Fund Consultant, Daniel Stern of Cliffwater, LLC, said that their recommendation was to invest in a macro strategy, recommending Brevan Howard within this strategy as a premier global macro fund. Although the fund began in 2002, the team has been together many years with an extremely successful track record, annualizing at well over 15%, with very low volatility of less than 8% over the same period. The fund invests in fixed income securities and currencies with a top down view achieved by allocating

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capital to multiple traders. Council Member Kellogg stated he was surprised that the fund was charging such high fees. Mr. Stern stated that while some funds are charging 3% and 30%, Brevan Howard is below that. Further, the returns disclosed are all net of fees. Due to limited capacity, the market allows the fund to charge this level of fees. Mr. Nesbitt of Cliffwater stated that during the meltdown, while stocks were down 40%, this manager had returns in excess of 20%. He further stated that while a fiduciary needs to consider costs, it also needs to look at diversification and long term performance. The best performing asset classes over the last ten years were private equity and private real estate, returning 8-9%, and hedge funds at 7.5%. In response to a question from Ms. Straight about Brevan Howard's 2009 performance, Mr. Stern stated that the fund returned in excess of 17%. Council Members Marketti and Kellogg asked to be put on record as opposed to this investment.

Acting Director Joseph summarized that Pershing Square is a concentrated deep-value strategy which was presented to the Council in 2008. Due to a political contribution disqualification, the fund was ineligible for investment for two years. Mr. Stern stated that Pershing Square is a boutique firm managing \$5 billion with a concentrated portfolio on both the long and short side. He noted that Bill Ackman, the founder and portfolio manager, is known for his investment stances; he was early in identifying problems in the mortgage and financial industries. Mr. Stern stated the fund has produced an annualized return since inception of just under 24% but is expected to be somewhat more volatile because of the concentration. The volatility has been about 16%. Mr. Stern noted the fees are attractive at 1.5% and 20%. Acting Director Joseph stated that the recommendation of \$75M on the Pershing Square summary page in the package was incorrect. The recommendation should be \$100 million. Council Member Marketti asked to be put on record as opposed to this investment.

*Memorandum "Proposed Fund of Hedge Funds Follow-On Investments in Goldman Sachs Multi-Strategy Portfolio (NJ), LLC and RC Woodley Park LP" dated March 12, 2010*

Acting Director Joseph presented the proposal to invest an additional \$250 million each into existing hedge funds Goldman Sachs and Woodley Park. He stated that the strategy is to deploy funds to take advantage of the equity markets. The funds will be redeployed into direct equity strategies in the next 12-18 months. Acting Director Joseph responded affirmatively to Council Member Love's question regarding whether the redemption terms would allow that. Mr. Stern clarified to Council Member Marketti that the Division owns such a high percentage of the Goldman Sachs fund because this is a separate account and Goldman Sachs manages in excess of \$20 billion from other investors in these types of strategies. DAG Weiner further clarified that the general partner has an investment in each of these funds. Council Member Marketti stated that he is opposed to these investments.

**Director's Report**

*Memorandum "Investment Reports" dated March 12, 2010*

Acting Director Joseph reported that the Pension Fund returned 0.75% percent compared to the Council benchmark of 0.92% for the month of February. The market value of the fund was \$67.3 billion. Fiscal year to date the Fund is up 14.09% versus the benchmark of 13.55%. He stated that despite the volatility in the markets, domestic equities, emerging markets, fixed income (excluding TIPS), hedge funds and mortgages generated positive return, and most portfolios exceeded their benchmarks.

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Investment Officer Brian Arena reported that there were net sales of \$398 million in US equities spread broadly over industry groups with the exception of financials and industrials where the fund is underweight. He stated that domestic equities returned 3.63% in February, against a benchmark of 3.31% and that for the calendar year the Fund is down .5% versus .6% for the index.

Senior Portfolio Manager Tim Patton reported that there was huge demand for new corporate issues, resulting in many deals being over-subscribed. The poor allocation to the Fund resulted in net sales of corporates for the month. For the month of February, the fixed income portfolio was up .56% versus .30% for the Barclays index. For the fiscal year-to-date period, Common Pension Fund B (excluding TIPS and high yield) returned 10.02% versus 8.07% for the benchmark. Mr. Patton reported that we still like the high yield markets. High yield was up 0.18% for February versus 0.17% for the benchmark, and up 26% for the year-to-date period, versus 23% for the benchmark. He reported that the Fund has added about \$100 million in Build America Bonds since the last meeting resulting in a total investment of over \$700 million. Although spreads have continued to tighten, they offer one of the best investment options available. Given that we were slightly overweight in TIPS, we sold some TIPS because the break even spreads widened. Acting Director Joseph stated that one of the greatest challenges we have is getting allocation to fixed income.

Investment Officer Gilles Michel stated that we were sellers of \$260 million in the international developed markets. The portfolio underperformed the benchmark by 50 basis points primarily due to the sovereign credit crisis in certain geographies triggered by Greece. He stated that although we are underweight these countries, sector allocation to utility and infrastructure stocks negatively impacted performance. Mr. Michel stated that our one year positive stance towards Japan, and 10% overweight, has contributed positively to performance.

Acting Director Joseph stated that while we are cautious given the run up in the S&P, we remain positive on the equity market overall.

Council Member Marketti raised a question about the values for real estate and private equity reported on Schedules 1 and 2. During the ensuing discussion, it was clarified that valuations are not yet available for these funds as of 12/31/09, and the values disclosed represent the 9/30/09 valuations, adjusted for net cash flows. Ms. Straight suggested that it be footnoted wherever current values are not available.

Council Member Marketti inquired why certain fund values were not disclosed on Exhibit 25. Investment Officer Kotwal explained that the net asset value is not always available at the time the package is prepared for the funds. He suggested that, in the future, the latest available value would be included and footnoted.

(Note: Council Member Kandrac departed the meeting during the Investment Report).

**Report on Iran Divestment Status**

*Memorandum "Report on Iran" dated March 1, 2010*

Compliance Officer Susan Sarnowski reported that the Division must annually report the status of the divestment of international companies in certain sectors with equity ties to Iran to the Legislature. She reported that the Division had made considerable progress during the year, and had two positions

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remaining, Gazprom and Petrobras. These positions must be divested by January 4, 2011 to be in compliance with the statute.

**Pending Matters**

Compliance Officer Susan Sarnowski reported that the comment period for the repeal of N.J.A.C. 17:16-2 regarding the engagement of external managers ended on February 5, 2010 and there were no public comments. The Division is precluded from presenting the adoption to the Council under Governor Christie's Executive Order 1 which suspended all adoptions for 90 days. Given that the suspension ends on April 18, the adoption will most likely be presented to the Council at the May meeting.

**Committee Reports**

There were no committee reports.

**Communications**

Mr. Steven Harris reported that there were no reports from the Treasurer.

(Note: Council Member Kellogg signed off the call after the Treasurer's report.)

**Public Comment Period**

Mr. Joel Frank presented a paper to the Council members and spoke about the costs of the funds offered under the Deferred Compensation Plan and other defined contribution retirement plans.

**Adjournment of Meeting**

The meeting was adjourned at 4:27 pm by unanimous vote on a motion by Council Member Love, seconded by Council Member Kleeberg.