



State of New Jersey

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DEPARTMENT OF THE TREASURY
DIVISION OF INVESTMENT
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ELIZABETH MAHER MUOIO
State Treasurer

SHOAIB KHAN
Director

July 24, 2024

MEMORANDUM TO: The State Investment Council

FROM: Shoaib Khan
Director

SUBJECT: **Risk Mitigation Strategies Investment – Capula Tail Risk Fund Limited Dynamic Class and Capula Global Relative Value Fund Limited**

The Division of Investment (“Division”) is proposing an investment up to \$100 million in Capula Tail Risk Fund- Dynamic Class (“DTR”) and up to \$100 million in Capula Global Relative Value Fund Limited (“GRV”) (the “Funds”) managed by Capula Investment Management (the “Firm”). This memorandum is presented to the State Investment Council (the “Council”) pursuant to N.J.A.C. 17:16-69.9.

The Division is recommending this investment based on the following factors:

Alignment of Interest: The GRV flagship fund is capacity constrained and, at various times, has been soft-closed to new investors and has a well-documented history of returning capital to LPs. This approach demonstrates their commitment to prioritizing returns and maintaining a cautious stance on capacity. Additionally, a portion of the GRV fund is invested in tail risk strategies, which provides a significant incentive for the GP to continuously enhance the strategy. This structure helps align the interest of the fund manager closely with ours.

Proven Track Record: The Firm has a long history of success in the market, supported by extensive experience. It consistently extracts value using advanced research tools and its strong infrastructure. This is crucial in an investment style known for high barriers to entry and a high failure rate. The firm’s track record shows a solid ability to navigate market challenges effectively.

Idea Generation: The team has developed effective governance, infrastructure, idea generation processes, and risk management, as evidenced by their long track record both as a firm and previously at J.P. Morgan. The team’s collective experience has enabled the Funds to consistently identify strategies and capitalize on investment opportunities while managing risk effectively.

A report of the Investment Policy Committee (“IPC”) summarizing the details of the proposed investment is attached. Division staff and the Division’s hedge fund consultant, Cliffwater LLC,

undertook extensive due diligence on the proposed investment in accordance with the Division's Alternative Investment Due Diligence Procedures.

As part of its due diligence process, staff determined that the Firm has not engaged a third-party solicitor ("placement agent").

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 the investment.

We have obtained a preliminary Disclosure Report of Political Contributions in accordance with the Council's regulation governing political contributions (N.J.A.C. 17:16-4) and no political contributions have been disclosed. We will obtain an updated Disclosure Report at the time of closing.

Capula has a Responsible Investment Policy (RI Policy) which was formalized in 2023 and applies to all market risk-taking activity within the firm. The Enterprise Risk Committee (ERC) has oversight of the policy while the investment team is responsible for following the policy. The policy is reviewed annually and updated as needed. In accordance with the State Investment Council's ESG Policy, the Division of Investment's Corporate Governance Team completed its review of Capula Investment Management LLP's Environmental, Social and Governance efforts.

Please note that the investment is authorized pursuant to Articles 69 and 100 of the Council's regulations, and the Funds will be considered Absolute Return Strategy investments, as defined under N.J.A.C. 17:16-100.1.

A formal written due diligence report for the proposed investment was sent to each member of the IPC and a meeting of the IPC was held on July 12, 2024. We look forward to discussing the proposed investment at the Council's July 24, 2024 meeting.

Attachments

Sincerely,

Shoaib Khan
Director, New Jersey Division of Investment

Capula Global Relative Value and Capula Tail Risk Fund - Dynamic Class

- **DOI Commitment:** up to \$200 million; up to \$100 million to Capula Global Relative Value ("GRV") and up to \$100 million to Capula Tail Risk Fund- Dynamic Class ("DTR")
- **Strategy:**
 - Return Enhancer : Capula GRV
 - Downside Protection : Capula DTR
- **Investment Focus:**
 - Capula GRV: Fixed Income arbitrage fund primarily investing in bonds that seek to produce consistent returns with no market exposures, targeting a Sharpe ratio over 1.
 - Capula DTR : Designed to offer protection during equity market drawdowns, helping to shield the overall portfolio.
- **Target Returns:**
 - Capula GRV: Net return of 8-12% per year with a Sharpe greater than 1.
 - Capula DTR: Seeks to produce a large stress gain during a high volatility sell-off while maintaining a flat average annual carry over market cycles.
- **Investment Thesis:**
 - Strong alignment of interest
 - Consistent history of strong returns and alpha generation
 - Experienced senior team
 - Dynamic tail hedge allocation and wealth preservation

Fund Name: Capula Global Relative Value Fund, Ltd		July 24, 2024	
Contact Info: Matthew Jamieson, 510 Madison Avenue, New York, NY 10022			
Fund Details:			

Total Firm Assets (\$bill):	\$29.4 billion	Key Investment Professionals:	
Strategy:	Market Neutral - Fixed Income Arbitrage	Yan Huo is a Co-Founder and Managing Partner of Capula. Prior to founding Capula, Mr. Huo was the head of fixed income at UFJ. He started his professional career at J.P. Morgan where he worked in the derivatives research and proprietary position business. He previously served as a member of the US Treasury Borrowing Advisory Committee.	
Year Founded:	2005	Masao Asai is a Co-Founder and Partner of Capula. Prior to founding Capula, Mr. Asai was an executive vice president at UFJ International as the head of proprietary trading after his earlier position as a proprietary trader and the head of yen fixed income in Tokyo. Earlier in his career, Mr. Asai, was the head of FX spot, swap, and proprietary trading at Tokai Bank.	
Headquarters:	London, England	Bing-Le Wu is a Partner and Head of European RV. He leads the firm's enhanced fixed income fund. Prior to joining the firm in 2008, Mr. Wu spent over 13 years at J.P. Morgan as a managing director of that firm's European proprietary trading business and was responsible for the fixed income portfolio. Earlier in his career, Mr. Wu was in derivative research, supporting interest rate and credit derivative trading.	
SEC Registration	Yes (GP's US Affiliate)	Taku Iida is a Partner and Senior Portfolio Manager at Capula. He joined Capula in 2009 and is currently part of the Relative Value team trading the Yen. Prior to joining Capula, Mr. Iida was an Associate at J.P. Morgan from 2006 to 2009. Earlier in his career, he was an analyst at Taylor Investment Advisors.	
GP Commitment:	6%	Gavin Estcourt is a Partner and the Chief Risk Officer at Capula since 2022. Prior to joining Capula, he was the head of Market Risk at Citi. Earlier in his career, he was EMEA Chief Risk Officer and Global Head of Market Risk at Nomura, and prior to Citi, he was a Managing Director, head of GRC and Commodity Market Risk at Bank of America.	

Investment Summary		Annualized Returns			
The strategy focuses on identifying alpha opportunities primarily within G3 markets by actively trading principally government bonds, futures, and interest rate swaps. It incorporates a tail risk sub-strategy that seeks to provide downside protection against significant market downturns, and thereby generate more stable returns during periods of heightened volatility. The approach provides a market neutral alpha source, with the objective to minimize exposure to overall market movements.		Capula Global Relative Value	HFRI Relative Value Index	3 Month T-Bills + 3.0%	
		1 Year	7.81%	8.22%	8.51%
		3 Year	7.31%	4.16%	5.80%
		5 Year	6.97%	4.62%	5.12%
		Since Inception	8.30%	5.27%	4.52%
		As of 3/31/2024 Source of Returns - Cliffwater			

Vehicle Information:			
Fund Inception:	2005	Redemptions (notice):	Quarterly liquidity; 45 days notice; 25% Investor Level Gate
Fund Size:	\$14.1 billion	Lock-up:	24 month soft lock with 3% early redemption fee
Management Fee:	2.00%	Prime Brokers:	Barclays, BNP Paribas, Merrill Lynch, J.P. Morgan, Morgan Stanley, Societe Generale
Profit Allocation:	20.00%	Custodians:	Bank of NY Mellon, HSBC Bank, State Street
Highwater Mark:	Yes	Auditor:	Ernst & Young
Hurdle Rate:	None	Legal Counsel:	Seward & Kissel, Simmons & Simmons
Admin Expenses:	Approximately 32 bps		

NJ AIP Program			
Recommended Allocation (\$mil):	up to \$100 million	LP Advisory Board Membership:	N/A
% of Fund:	94.00%	Consultant Recommendation:	YES
		Placement Agent:	None
		Compliance w/ Division Placement Agent Policy:	N/A
		Compliance w/ SIC Political Contribution Reg:	YES

*This review memorandum was prepared in accordance with the State Investment Council rules governing the Alternatives Investment Program and the policies and procedures related thereto.

Fund Name: Capula Tail Risk Fund Ltd. (Dynamic Class) **July 24, 2024**

Contact Info: Matthew Jamieson, 510 Madison Avenue, New York, NY 10022

Fund Details:

Total Firm Assets (\$bil):	\$29.4 billion	Key Investment Professionals:
Strategy:	Tail Risk/Defensive Macro	Yan Huo is a Co-Founder and Managing Partner of Capula. Prior to founding Capula, Mr. Huo was the head of fixed income at UFJ. He started his professional career at J.P. Morgan where he worked in the derivatives research and proprietary position business. He previously served as a member of the US Treasury Borrowing Advisory Committee
Year Founded:	2005	Masao Asai is a Co-Founder and Partner of Capula. Prior to founding Capula, Mr. Asai was an executive vice president at UFJ International as the head of proprietary trading after his earlier position as a proprietary trader and the head of yen fixed income in Tokyo.
Headquarters:	London, England	Earlier in his career, Mr. Asai was the head of FX spot, swap, and proprietary trading at Tokai Bank
SEC Registration	Yes (of GP's Affiliate)	Bing-Le Wu is a Partner and Head of European RV. He leads the firm's enhanced fixed income fund. Prior to joining the firm in 2008, Mr. Wu spent over 13 years at J.P. Morgan as a managing director of that firm's European proprietary trading business and was responsible for the fixed income portfolio. Earlier in his career, Mr. Wu was in derivative research, supporting interest rate and credit derivative trading
GP Commitment:	1%	Taku Iida is a Partner and Senior Portfolio Manager at Capula. He joined Capula in 2009 and is currently part of the Relative Value team trading the Yen. Prior to joining Capula, Mr. Iida was an Associate at J.P. Morgan from 2006 to 2009. Earlier in his career, he was an analyst at Taylor Investment Advisors.
		Gavin Estcourt is a Partner and Chief Risk Officer at Capula since 2022. Prior to joining Capula, he was the head of Market Risk at Citi. Earlier in his career, he was EMEA Chief Risk Officer and Global Head of Market Risk at Nomura, and prior to Citi, he a Managing Director, head of GRC and Commodity Market Risk at Bank of America.

Annualized Returns

The strategy seeks to provide positive returns in times of liquidity and systemic crises whilst seeking to minimize carry costs during normal market conditions. Such protection during market downturns may reduce the risk of significant wealth erosion and may, in turn, mitigate underfunding risk. New Jersey will allocate to the dynamic share class, which implements predetermined triggers to capitalize on market stress events.		Capula Tail Risk Fund (Dynamic)(Hypothetical)	Long Rolling 3M S&P Puts	Euekahedge Talk Risk Fund Index	
		1 Year	1.12%	0.90%	-5.09%
		3 Year	3.25%	-3.08%	-1.68%
		5 Year	5.62%	-3.45%	2.64%
		Since Inception	2.12%	-4.76%	-3.65%

As of 3/31/2024

Source of Returns - Cliffwater

Vehicle Information:

Fund Inception:	2010	Redemptions (notice):	Weekly liquidity; 30 days notice
Fund Size:	\$2.4 billion	Lock-up:	None
Management Fee:	0.90%	Prime Brokers:	Barclays, BNP Paribas, Merrill Lynch, J.P. Morgan, Societe Generale
Profit Allocation:	20.00%	Custodians:	Bank of NY Mellon, HSBC Bank, State Street
Highwater Mark:	No	Auditor:	Ernst & Young
Hurdle Rate:	None	Legal Counsel:	Seward & Kissel, Simmons & Simmons
Admin Expenses:	Approximately 21 bps		

NJ AIP Program

Recommended Allocation (\$mil):	up to \$100 million	LP Advisory Board Membership:	N/A
% of Fund:	99.00%	Consultant Recommendation:	YES
		Placement Agent:	None
		Compliance w/ Division Placement Agent Policy:	N/A
		Compliance w/ SIC Political Contribution Reg:	YES

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