



State of New Jersey

DEPARTMENT OF THE TREASURY
DIVISION OF INVESTMENT
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Lt. Governor

ANDREW P. SIDAMON-ERISTOFF
State Treasurer

June 30, 2011

MEMORANDUM TO: The State Investment Council

FROM: Timothy Walsh
Director

SUBJECT: **Proposed Investment in GSO Capital Opportunities Fund II,
L.P.**

The New Jersey Division of Investment is proposing an investment of \$150 million in **GSO Capital Opportunities Fund II**. This memorandum is presented to the State Investment Council (the "Council") pursuant to N.J.A.C. 17:16-69.9.

NJDOI will be committing to GSO Capital Opportunities Fund II which will seek to build a diversified portfolio comprised primarily of mezzanine and private high yield securities, secured/single tranche debt and private equity investments. GSO expects that it will be the lead or sole mezzanine debt investor and that private equity sponsors will be involved in the majority of its investments. The fund is expected to make 20-30 investments, with the typical size ranging from 2.5% - 7.5% of capital commitments, across a range of issuers and industries. GSO also anticipates investing in both the U.S. and Europe.

GSO Capital Opportunities Fund I, in which NJDOI invested \$100 million, closed on a total of \$2.0 billion of equity commitments in August of 2008. The fund is ranked in the top quartile among its peers. As of March 31, 2011, the fund is valued at 1.40x of original cost on a levered basis and has generated an inception-to-date gross levered IRR of 21.6% and a net IRR of 16.0%. During the same quarter, the total value of the portfolio increased \$83.6 million or 4.3%. GSO COF I's performance during a period of unprecedented volatility in the financial markets is a testament to their investment strategy, investment process and credit selection.

On March 3, 2008, The Blackstone Group (a New York Stock Exchange traded company; symbol BX) acquired a controlling stake in GSO. The combination of GSO's businesses with Blackstone's existing credit-related groups created one of the largest and top performing credit platforms in the alternative asset management business with approximately \$30 billion in assets under management. To date, GSO has assembled a team of 184 employees in New York, London and Houston.

GSO employs a rigorous investment process to evaluate all potential opportunities with preservation of principal as a primary goal. They have generated attractive risk adjusted returns in their mezzanine

activities throughout a difficult economic cycle by maintaining their investment discipline; performing intensive credit work; carefully structuring transactions; and actively managing their portfolio. GSO targets businesses with leading market share positions, sustainable barriers to entry, high free cash flow generation, strong asset values that support the investment, liquidity to withstand market cycles, favorable underlying industry trends, strong internal controls and high quality management teams.

The Division of Investment ("Division") Staff and its private equity consultant, Strategic Investment Solutions, undertook extensive due diligence on these proposed additional investments. We completed the same due diligence process as with all the other alternative investment opportunities presented to the Council. As part of its due diligence process, staff determined that the fund has not engaged a third-party solicitor (a "placement agent") in connection with New Jersey's potential investment.

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 regulation governing political contributions (N.J.A.C. 17:16-4).

Please note that this investment is authorized pursuant to Articles 69 and 90 of the Council's regulations. The GSO Capital Opportunities Fund II will be considered private equity "debt - related" investments, as defined under N.J.A.C. 17:16-90.1.

Formal written due diligence reports for the proposed investment were sent to each member of the Investment Policy Committee on June 17, 2011, and a meeting of the Committee was held on June 21, 2011. In addition to the formal written due diligence reports, all other information obtained by the Division on the investment was made available to the Investment Policy Committee.

We look forward to discussing the proposed investment at the Council's June 30, 2011 meeting.

Attachments

*SIC Investment Committee Fund Review Memo

To: State Investment Council
From: Division Of Investment
Date: June 30 ,2011
Subject: GSO COF II Recommendation

Fund Facts

Fund Name:	GSO Capital Opportunities Fund II
Fund Type:	Private Equity
Current Fund Size:	\$3.0 - 3.75 Billion
Previous Fund Size/Vintage:	\$2 Billion/2008
Final Close:	May 30, 2012
Fund Address:	280 Park Avenue , 11th Floor New York, NY 10017

GP Contact Info

Name:	Beth Chartoff
Telephone:	212-503-2166
Email:	beth.chartoff@gsocap.com

Summary of Terms and Investment Strategy

Investment Strategy:	Mezzanine
Geographic Focus:	Primarily United States, and Europe
GP Co-Investment Amount:	\$100 million, or 5% of Total Capital Commitments
Terms:	
Term:	10 years
Investment period:	5 years
Management Fee:	During the investment period, the management fee will be 1.5% of cost per annum. Post the investment period, the management fee will be 1.25% per annum of the aggregate invested capital, including leverage.
Other Fees:	The management fee will be reduced by 100% of any origination or transaction fees, including commitment, closing, amendment, waiver, directors, organizational, break-up or other similar fees.
Carry/Performance Fee:	20% GP does not receive its share of the carried interest until COF II investors receive 75% return of capital contributions. Catch-up of 80% to the GP and 20% to the LP until the GP received 20% of profits – 20% to the GP thereafter.
Hurdle Rate:	8%
Attorney:	Schulte Rothe & Zabel LLP
Auditor:	Deloitte & Touche LLP
Accounting Firm:	Internal Function

NJ AIP Program:

Recommended Allocation:	150,000,000.00
% of Fund:	5.00%
Placement Agent	No

LP Advisory Board Membership:	TBD
Consultant Recommendation:	Yes
Compliance with SIC Political Contributions 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.