

NJ DIVISION OF INVESTMENT

Director's Report

State Investment Council
March 24, 2021

“The mission of the New Jersey Division of Investment is to achieve the best possible return at an acceptable level of risk using the highest fiduciary standards.”

Capital Markets Update (through February 28, 2021)

	Calendar YTD	Fiscal YTD	One Year	Three Years (Annualized)	Five Years (Annualized)
Global Equity Indices					
MSCI ALL Country World Index	1.85	26.31	30.25	10.29	14.23
US Equity Indices					
Russell 3000	2.66	28.57	35.31	14.95	17.38
Russell 1000	2.04	27.00	34.27	14.96	17.35
Russell 2000	11.58	53.79	50.97	14.82	17.88
Russell Growth	-0.18	26.64	45.21	20.81	22.13
Russell Value	5.71	30.61	23.32	8.32	12.15
Non-US Equity Indices					
MSCI EAFE	1.15	23.01	22.46	4.58	9.72
MSCI Emerging Markets	3.85	36.19	36.05	6.34	15.23
Fixed Income Indices					
Bloomberg Barclays U.S. Aggregate	-2.15	-0.89	1.38	5.31	3.55
Bloomberg Barclays U.S. Treasury	-2.75	-3.39	-0.13	4.95	2.57
Bloomberg Barclays U.S. Credit	-2.90	1.30	2.36	6.62	5.52
Bloomberg Barclays U.S. High Yield	0.70	12.12	9.38	6.57	8.96
Commodities					
Bloomberg Commodities Index	9.25	31.24	20.14	-1.09	2.34
Real Estate					
Bloomberg U.S. REIT Index	2.69	12.43	3.02	9.52	7.93

FY21 Public Market Update: Asset Allocation and Net Returns (February 28, 2021)

Asset Class	ASSET ALLOCATION As of February 28, 2021			FYTD through February 28, 2021	
	Mkt Value (in \$ millions)	Actual (%)	Target (%)	NJ	Benchmark
<u>GLOBAL GROWTH</u>					
US Equities	23,378	27.64%	27.00%	28.36%	28.58%
Non-US Developed Market Equities	11,860	14.02%	13.50%	23.64%	23.06%
Emerging Market Equities	5,664	6.70%	5.50%	39.22%	36.32%
<u>INCOME</u>					
Investment Grade Credit	6,662	7.88%	8.00%	-0.46%	-0.24%
High Yield	1,635	1.93%	2.00%	12.75%	12.09%
<u>DEFENSIVE</u>					
U.S. Treasuries	5,875	6.95%	5.00%	-3.56%	-3.39%

Notification: Modification to Exeter Core Industrial Club Fund II, L.P. and Exeter Industrial Core Fund III, LP.

Background: The Pension Fund has made commitments totaling \$400 million across three funds sponsored by Exeter Property Group (“Exeter”) as follows: Exeter Core Industrial Venture Fund (Fund I, \$200 million in 2012), Core Industrial Club Fund II (\$100 million in 2016), and Exeter Industrial Core Fund III LP (\$100 million in 2019). Of the three funds, only Fund III is still in its investment period, with \$77.3 million of uncalled capital. Fund I has been fully realized and liquidated.

Modification: In January 2021 Exeter entered into an agreement with EQT whereby EQT would acquire a 100% interest in the firm. In addition to acquiring Exeter, EQT will also acquire a portion of carried interest in Fund III from Exeter’s founder and majority owner. The Division intends to consent to the change in control and transfer of carried interest.

Impact on Pension Fund: The Division believes that the change in control and transfer of carried interest will be beneficial to the Pension Fund. The senior management team at Exeter remains the same with no changes being made to the operation and management of the funds and underlying investments. There is also no change to the investment committees or how Exeter makes investment, leasing and other property operating decisions. The compensation paid by EQT includes stock with vesting and lock-up provisions to incentivize the Exeter team’s long-term commitment to the firm. The carry distribution to Exeter professionals (other than the founder) will not change and will continue to provide an alignment of interest with the fund’s investors. Finally, the acquisition by EQT provides financial stability to the firm going forward.

**The Director is notifying the SIC of this modification in accordance with the
Alternative Investment Modification Procedures**

Notification: Modification to Wheelock Street Real Estate Fund III, L.P.

Background: The Pension Fund has made commitments totaling \$375 million across four investment vehicles sponsored by Wheelock Street Capital (“Wheelock”) as follows: Wheelock Street Real Estate Fund III, L.P. (\$100 million in 2012), Wheelock SREF NJ Co-invest Feeder, L.P. (\$50 million in 2012), Wheelock Street Real Estate Fund IV, L.P. (\$125 million in 2014) and Wheelock Street Real Estate Fund V, L.P. (\$100 million in 2016). The Wheelock funds, and Fund III in particular, have contributed strong performance to the real estate portfolio. Fund III is approaching the end of its term and has only a handful of remaining assets.

Modification: Wheelock is proposing to extend the term of Fund III to December 2023. This extension will allow the Fund to fully monetize most of its remaining assets and to complete the renovation of its final asset. In conjunction with the extension, Wheelock is proposing to reduce the management fee by suspending the management fee on the final asset during construction. Once the asset is operating, the management fee applicable to the asset will be charged on the fair market value rather than the equity invested. The change in methodology is expected to result in a substantial decrease in the amount of management fees paid to Fund III during the extended term of the fund. The Division intends to consent to the extension and the change in methodology used to calculate the management fee.

Impact on Pension Fund: The extension of the fund term will allow the fund to more effectively monetize the remaining assets in its portfolio and therefore is expected to be beneficial to investors. The change in methodology used to calculate the management fee is also expected to benefit investors by substantially reducing the amount of the fee. In the unlikely event that the management fee increases due to the fair market value of the asset exceeding the equity invested in the asset, the amount of the increased fee would be offset by the increased sale proceeds.

**The Director is notifying the SIC of this modification in accordance with the
Alternative Investment Modification Procedures**

Notification: Modification to Cerberus, Sixth Street Knight TAO, and Crayhill

Background: The Pension Fund has committed capital to Cerberus NJ Credit Opportunities Fund, L.P. (\$300 million in 2012), Knight TAO, L.P. (\$400 million in 2014 plus another \$300 million in 2015), and Crayhill NJ Fund LP (\$150 million in 2017). As of December 31, 2020, Cerberus NJ Credit Opportunities Fund, L.P. (“Cerberus”) had a market value of \$388 million (with \$70 million of unfunded commitments), Knight TAO, L.P. (“Sixth Street Knight TAO”) had a market value of \$526 million (with \$310 million of unfunded commitments), and Crayhill NJ Fund LP (“Crayhill”) had a market value of \$31 million (with \$136 million of unfunded commitments). Each of these funds can recycle gains and/or principal to some degree.

Modification: The Division is modifying the recycling provisions for each fund to allow the Division to periodically elect to change the recycling of gains to either (i) fully recycle, (ii) partially recycle (in the case of Cerberus and Crayhill only), or (iii) fully distribute.

Impact on Pension Fund: The Pension Fund is currently below its target allocation to Private Credit. In the immediate term, this modification allows the Division to quickly deploy capital into Private Credit by electing to have more gains recycled rather than distributed. More broadly, the modification provides the Division with more control over the timing of capital deployment within the Private Credit portfolio. This modification would have no impact on any of the respective funds’ other liquidity provisions.

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Notification: Modification to Owl Rock Co-Investment Vehicle

Background: When the Division presented an investment in Owl Rock Capital Corporation in 2016, it also presented an investment of up to \$200 million in a related separate account vehicle for overage and co-investment opportunities. The terms of the co-investment vehicle presented to the Council included a management fee of 0%, a performance fee of 0% and a veto right on all proposed co-investment opportunities.

Modification: In connection with the Pension Fund's pending \$150 million commitment to Owl Rock Diversified Lending 2020 Fund, the Division is proposing to expand the co-investment mandate to include both overage opportunities over which the Division has veto rights as well as pro-rata co-investment opportunities alongside certain Owl Rock investment vehicles over which the Division would not have veto rights. The Division would retain the right to periodically stop (and restart) deployment of capital in the co-investment vehicle.

Impact on Pension Fund: This modification will provide the Division with additional opportunities to deploy capital in the Private Credit space, which is currently underweight its target. While the Division will retain control over the speed of overall capital deployment, it will have less discretion over specific fund investments. The modification will have no impact on fees.

**The Director is notifying the SIC of this modification in accordance with the
Alternative Investment Modification Procedures**

Notification: Modification to Funds Managed by Dyal and Owl Rock

Background: The Pension Fund has made commitments into a number of investments with Dyal Capital Partners (“Dyal”) and Owl Rock Capital Partners LP (“Owl Rock”). The Dyal investments include \$200 million to Dyal NJ Investors, L.P. in 2012, \$250 million to Dyal II NJ Investors, L.P. in 2014, \$200 million to Dyal III US Investors, L.P. in 2015, and \$100 million to Dyal III NJ Investors, L.P. in 2017. The Owl Rock investments include \$400 million to Owl Rock Capital Corporation in 2016 and \$100 million to Owl Rock Capital Technology Finance Corp in 2018, plus pending investments of \$150 million to Owl Rock Diversified Lending 2020 Fund and \$200 million into a co-investment mandate investing pro-rata alongside certain Owl Rock direct lending funds. In addition, the Pension Fund has (or will have) an investment in certain Owl Rock management company entities (Owl Rock Capital Group, Owl Rock Capital Technology Holdings, and Owl Rock Capital Diversified Holdings).

Per State Street, as of December 31, 2020, the combined Dyal investments had a market value of \$750 million with \$318 million of unfunded commitments. The combined Owl Rock investments had a market value of \$430 million with \$51 million of unfunded commitments, excluding the value of any management company investments.

Modification: Dyal and Owl Rock plan to combine with Altimar Acquisition Corporation to form Blue Owl Capital Inc. (“Blue Owl”), which, if approved, will trigger a change in control of the Investment Advisors for each of the respective Dyal and Owl Rock funds to an Investment Advisor controlled by Blue Owl.

Impact on Pension Fund: The Division does not anticipate that this combination will have a material impact on the Pension Fund. Although the ownership is changing, the investment teams of the respective Investment Advisors are not changing, nor are the terms of any of the respective Investment Advisory agreements.

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Alternative Investment Modification Procedures**

Notification: Modification to Funds Managed by Owl Rock

Background: In addition to the Pension Fund's \$400 million commitment to Owl Rock Capital Corporation ("ORCC") in 2016, the Pension Fund invested in 250,000 Class A Units in what is now Owl Rock Capital Group ("ORCG"). On January 4, 2021, a Form S-4 was filed with the Securities and Exchange Commission ("SEC") outlining a pending business combination between ORCG, Dyal Capital Partners and certain other parties to form Blue Owl Capital Inc. ("Blue Owl"). As of December 31, 2020, the value of the Pension Fund's interest in ORCG was estimated at approximately \$71.5 million.

Modification: As a Class A unitholder in ORCG, the Pension Fund has the option to receive consideration in the form of (a) Blue Owl Holdings Units in Blue Owl Capital Holdings LP, (b) Blue Owl Carry Units in Blue Owl Capital Carry LP, and (c) shares of Blue Owl Class C common stock (together the "Partnership Units"). The Division expects to submit, on or before March 19, 2021, a revocable election to receive the Partnership Units subject to successful negotiation of terms and conditions acceptable to the Division. In the event the Division doesn't come to terms, the Pension Fund would, instead of the Partnership Units, receive (x) shares of Blue Owl Class A common stock and (y) shares of Blue Owl Class E common stock (together the "Default Election Option").

Impact on Pension Fund: The Pension Fund will not be liable for any additional commitments of capital as a result of the pending Blue Owl transaction. Nor will there be any management fees, incentive fees, carried interest or other similar fees paid by the Pension Fund in connection with the Blue Owl transaction, or in the Pension Fund's potential role as a Limited Partner in either Blue Owl Capital Holdings LP or Blue Owl Capital Carry LP. Regardless of election option, the existing management team will remain in place.

Compared to the Default Election Option, the Partnership Units are less liquid, not subject to daily market volatility, and result in higher distributions to tax-exempt entities like the Pension Fund. Also, the Partnership Units can be exchanged on a quarterly basis (subject to certain limitations) into Blue Owl Class A common stock, which will be exchange-tradeable, public securities. Taking all these factors together, the Division anticipates that the election of Partnership Units should be a net benefit to the Pension Fund compared to the Default Election Option.

**The Director is notifying the SIC of this modification in accordance with the
Alternative Investment Modification Procedures**