



**State of New Jersey**

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December 8, 2011

MEMORANDUM TO: The State Investment Council

FROM: Timothy Walsh  
Director

SUBJECT: **Proposed Investment in Cerberus/NJ Loan Fund, L.P.**

The New Jersey Division of Investment ("Division") is proposing an investment of **\$300 million** in **Cerberus/NJ Loan Fund, L.P.** This memorandum is presented to the State Investment Council (the "Council") pursuant to N.J.A.C. 17:16-63.9.

The Division is recommending the investment for a number of reasons:

- **Attractive Market Opportunity/Diversification:** A significant supply/demand imbalance of loans being originated to middle-market businesses has created an attractive investment opportunity with potential gross returns in the 9% to 15% range. We expect this investment to be characterized as a fixed income investment (Common Pension Fund B) and will be funded by the reduction of liquid securities yielding approximately 3%.
- **Impressive Track Record:** Cerberus' 16 year track record, with average net returns of 8-12%, compares favorably to other direct lenders and indices. The manager's loan loss rate is 1.2% of the past 14 years.
- **Lender Stability:** Lender stability is an important issue for middle market companies as they look to establish financing relationships. Cerberus has one of the longer tenures as a direct middle market lender which provides a sourcing advantage against other funds.
- **Attractive Terms:** By structuring the investment as a separately managed account, the Division has greater control over the invested assets and more attractive terms.

A report of the Investment Policy Committee ("IPC") summarizing the details of the proposed investment is attached.

Division Staff and its consultant, Strategic Investment Solutions, 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 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 the investment. In addition, the proposed investment must comply with the Council's regulation governing political contributions (N.J.A.C. 17:16-4).

Please note that the investment is authorized pursuant to Articles 23 and 63 of the Council's regulations. The Cerberus/NJ Loan Fund, L.P. will be considered a bank loan fund investment, as defined under N.J.A.C. 17:16-23.1.

A formal written due diligence report for the proposed investment was sent to each member of the IPC and a meeting of the Committee was held on November 22, 2011. In addition to the formal written due diligence report, all other information obtained by the Division on the investment was made available to the IPC.

We look forward to discussing the proposed investment at the Council's December 8, 2011 meeting.

Attachments

**Fund Name: Cerberus/NJ Loan Fund, L.P.** **December 8, 2011**

**Contact Info:** Keith R. Read / Managing Director / 299 Park Avenue, New York, NY / 212-739-1207

<b>Fund Details:</b>	
<p><b>Total Assets:</b> \$22 billion</p> <p><b>Strategy:</b> Direct Lending</p> <p><b>Year Founded:</b> 1992</p> <p><b>Headquarters:</b> New York, NY</p> <p><b>GP Commitment:</b> .5% of NJ Separate Account; 7% of Cerberus Loan Opportunities Funds including GP and Cerberus Employees</p>	<p><b>Key Investment Professionals:</b></p> <ul style="list-style-type: none"> <li>- <i>Management brings a 16-year track record in middle-market lending dating back to the 1996. Chairman of the Lending Business, Kevin Genda (Sr. MD) joined Cerberus in 1995. Prior to joining Cerberus, Genda was VP of new business origination and evaluation at Foothill form 1992 to 1995.</i></li> <li>- <i>President of Cerberus Business Finance, Daniel Wolf (Sr. MD) joined Cerberus in 1997. Prior to joining Cerberus, Wolf was Senior VP for business development and a member of the credit committee at Congress Financial Corp. from 1990 to 1997.</i></li> <li>- <i>Origination team lead by Eric Miller (Sr. MD) joined Cerberus in 1998. Prior to Cerberus, Miller worked as VP in CIT Group/Business Credit, Inc. from 1986 to 1998.</i></li> <li>- <i>Chief Credit Officer, Joseph Naccarato (MD) joined Cerberus in 2000. Previously Naccarato was VP and Senior Credit Officer at Bank of America Commercial Funding from 1997 to 2000.</i></li> </ul>

<p><b>Investment Summary</b></p> <p>The investment will be structured as a separate account investing side-by-side with Cerberus Loan Opportunities Fund I, L.P. Cerberus seeks to invest in loans to companies which exhibit some or many of the following characteristics: (i) an established operating history; (ii) at least \$75 million in annual revenue; (iii) market leadership with defensible positions; (iv) predictable cash flows; (v) substantial asset or enterprise value relative to loan size; (vi) experienced and incentivized management team; and (vii) a well-capitalized and committed sponsor/equity owner.</p> <p><b>Attractive Market Opportunity/Diversification:</b> <i>A significant supply/demand imbalance of loans being originated to middle-market businesses has created an attractive investment opportunity with potential returns in the 9% to 15% range. The investment will be characterized as a fixed income investment (Common Pension Fund B) and will be funded by the reduction of liquid securities yielding approximately 3%.</i></p>	<p style="text-align: center;"><b>Existing and Prior Funds</b></p> <table border="1"> <thead> <tr> <th style="text-align: left;"><u>Funds</u></th> <th style="text-align: left;"><u>Strategy</u></th> <th style="text-align: left;"><u>Returns (gross)</u></th> <th style="text-align: left;"><u>Returns (net)</u></th> </tr> </thead> <tbody> <tr> <td>Historical Cerberus Lending Entity: '97 - '10</td> <td>Direct Lending</td> <td>17.9%</td> <td>12.2%</td> </tr> </tbody> </table>	<u>Funds</u>	<u>Strategy</u>	<u>Returns (gross)</u>	<u>Returns (net)</u>	Historical Cerberus Lending Entity: '97 - '10	Direct Lending	17.9%	12.2%
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**Vehicle Information:**

<p><b>Inception:</b> 2011</p> <p><b>Fund Size:</b> \$300 million</p> <p><b>Management Fee:</b> 1%</p> <p><b>Carry:</b> 17%</p> <p><b>Hurdle Rate:</b> 6%</p> <p><b>Additional Expenses:</b> Org. Expenses up to a max of \$500,000</p>	<p><b>Auditor/Accounting Firm:</b> PricewaterhouseCoopers</p> <p><b>Legal Counsel:</b></p> <p><b>Fund:</b> Lowenstein Sandler PC</p> <p><b>Tax:</b> Schulte Roth and Zabel LLP</p> <p><b>Fund Administrator:</b> JPMorgan Chase</p>
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<b>NJ AIP Program</b>			
<p><b>Recommended Allocation:</b> \$300 million</p> <p><b>% of Fund:</b> NA</p>	<p><b>LP Advisory Board Membership:</b> Yes</p> <p><b>Consultant Recommendation:</b> Yes</p> <p><b>Placement Agent:</b> No</p> <p><b>Compliance w/ Division Placement Agent Policy:</b> NA</p> <p><b>Compliance w/ SIC Political Contribution Reg:</b> Yes</p>	<p><b>Yes</b></p> <p><b>Yes</b></p> <p><b>No</b></p> <p><b>NA</b></p> <p><b>Yes</b></p>	

\*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.