The Syndicated Loan Market

- Who is the LSTA (and what is our focus)?
- Description of loan market (size, segments, lender constituency)
- Secondary market (and what it shows)
- Pressures in the loan market (and for borrowers)
Who is the LSTA?

The Loan Syndications and Trading Association is the trade association for the floating rate corporate loan market. The LSTA promotes a fair, orderly, and efficient corporate loan market and provides leadership in advancing the interest of all market participants. The LSTA undertakes a wide variety of activities to foster the development of policies and market practices designed to promote just and equitable marketplace principles and to encourage cooperation and coordination with firms facilitating transactions in loans and related claims.

The LSTA seeks to enhance public understanding of the corporate loan market and to serve the public interest by encouraging adherence to high ethical standards by all market participants. The LSTA plays a pivotal role in monitoring and bringing consensus to this important asset class by acting as a forum for the analysis and discussion of issues and developments relating to the loan market and advocating the shared interests of its membership. The Association formulates policy through its Board of Directors after consensus is developed through the active involvement of individual officers and employees of Member firms.

The LSTA stands out among financial market trade associations because it represents all segments of the market it serves: primary sales; par/near par and distressed trading; and bank and non-bank portfolio management. The LSTA membership totals more than 280 institutions.
U.S. Corporate loan market is a vital source of capital for American business

According to government data, the U.S. syndicated loan market totals nearly $2.8 trillion of committed lines and outstanding loans.

It is a key source of financing for many large and middle market companies in the U.S.
4 key U.S. large corporate loan market segments

**Investment grade loan market**
- Loans to companies rated >= BBB-/Baa3 AND with a relatively low LIBOR spread
- 2007 lending: $658 billion
- 2008 lending: $319 billion

**Leveraged loan market**
- Loans to companies rated < BBB-/Baa3 or unrated & with a high spread*
- Divided into bank (pro rata) and non-bank segments
- 2007 lending: $689 billion
- 2008 lending: $294 billion

**Institutional loan market**
- Leveraged loans with non-bank lenders (such as mutual funds, CLOs, insurance companies, hedge funds, etc)
- 2007 lending: $426 billion
- 2008 lending: $69.6 billion

**Secondary loan market**
- Market in which loans trade following the close of primary syndication
- Most U.S. loan trading involves leveraged loans
- 2007 trading: $442 billion
- 2008 trading: $510 billion

*Traditionally LIB+150, increased to LIB+350 in 1Q09

Source: Reuters LPC for primary lending; LSTA for secondary trading
Overall primary loan volume is down materially

At $764B, new loan volume in 2008 is at lowest level since 1994

At $104B, 1Q09 loan issuance is down 41% from 1Q08
Non-bank term loan outstandings

Outstandings ($Bils.)

Source: S&P/LCD
Pressures on the secondary

- 2007: Supply-demand imbalance
- 2008: Deleveraging
- 2009: Credit?
Dislocation: Loan prices decline sharply in 2008

- Loan prices come under considerable pressure in past 18 months
- This unusual behavior has impacted leveraged companies’ ability to access financing

Source: LSTA/LPC MTM Pricing
Trading activity remained relatively robust in 4Q08
More loans are trading < 80 cents on the dollar, which was typically considered “distressed”
However, there is an increasing disconnect between price and credit quality

Source: LSTA trade data study
Prices have declined even for companies with high ratings and no downgrades.

Even higher rated companies are trading at levels previously considered distressed.

- Typical trade price of BBB- names declined from 97.87 in 4Q07 to 85.15 in 4Q08.
- Typical trade price of BB+ rated names declined from 97.7 in 4Q07 to 80.09 in 4Q08.

Source: LSTA trade data study
Default rates are climbing

<table>
<thead>
<tr>
<th>LTM $Defaults / Outstanding-12 months</th>
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<tbody>
<tr>
<td>LTM # of Issuers in default / Total Issuers-12 months</td>
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Initially defaults were defined by small companies

Defaults becoming materially larger

“Shadow” default rate higher – above 9%

Amendments are becoming more difficult

Loss given default could worsen

Source: LSTA/LPC MTM Pricing, Standard & Poor’s LCD
Impact on borrowers

- Pressures
  - Deleveraging
  - Defaults
  - Consolidation
  - Liquidity

- Impact
  - New issue yields
  - Amendments
  - Refinancing cliff
Bank consolidation impacts liquidity

The Bank Universe Snapshot 1987-2008

Over the last several years the lending community has observed much consolidation. Regardless of whether lenders came together in a bid to gain market access to new products or as a result of fallout from recent market dislocation, the lending universe has dramatically contracted. Above is a partial listing of bank consolidation over the last 21 years.
Buyside is less active in 2008 – and may contract in 2009

Number of investor groups that made 10 or more primary commitments each year

- 1996: 22
- 1997: 29
- 1998: 48
- 1999: 54
- 2000: 42
- 2001: 64
- 2002: 76
- 2003: 98
- 2004: 116
- 2005: 168
- 2006: 218
- 2007: 261
- 2008: 85

*With the slow down in deal number, for the latest period LCD uses $100M of estimated allocations as a cut-off*

Source: Standard and Poor’s LCD
Leveraged loan prices fall, secondary yields increase, Primary squeezed out

- Default rates have climbed, but currently are below peak of last cycle
- Loan prices well below last downturn
- Secondary spreads go into the thousands over LIBOR
- Primary market cannot compete

Source: LSTA/LPC MTM Pricing, Standard & Poor’s LCD
Constraints: Companies need amendments And have to pay up

As the economic environment weakens, more companies are seeking amendments or covenant waivers for their loans

48 covenant amendments tracked in Jan/Feb; annualizes to nearly 300 – and pace may quicken

With low secondary prices, reduced lender liquidity and different lenders, amendments are more expensive

Source: S&P/LCD

* The data above comprises publicly available covenant amendment information tracked by a loan information company (S&P/LCD). It does not include information that has not been made public.
CLO issuance buoys institutional loan growth
Both markets stop in 2008

Source: Thomson Reuters LPC, Intex, Wachovia
The 2005-2007 bulge of leveraged loans will mature…
And will need to be refinanced

Issuance boom from 2005-2007 will mature in 2011-2014
However, loans will need to be refinanced a year earlier (2010-2013)
Revolvers will create nearer term refinancing pressure

Source: LSTA, S&P/LCD, Intex, Wachovia
CLO reinvestment period will end,
Reducing demand as loan maturities hit

- CLO issuance peaked in 2007 (Outstandings in red)
- CLO reinvestment periods range 5-7 years (Blue reflects “frozen” amt of CLOs as reinvestment ends)
- As reinvestment periods end, CLOs will no longer be able to buy new loans
- In turn, “re-investible” dollars will decline
- Blue line reflects MAXIMUM “reinvestible” CLO dollars – eg, if all loans in CLOs are repaid
- In reality, reinvestible dollars will be much lower (dotted lines)

Source: LSTA, S&P/LCD, Intex, Wachovia
There may be a significant refinancing shortfall

Starting in 2011, there will be a large volume of loans that must be refinanced

Because CLOs will be entering the end of their reinvestment periods, they will not be able to refinance these maturing loans

*This is probably an unrealistic best case scenario*

Source: S&P/LCD, Wachovia Securities, LSTA
How to address refinancing cliff?

Expected refinancing schedule

- Issuance boom from 2005-2007 will mature in 2011-2014
- However, loans will need to be refinanced a year earlier (2010-2013)