STATE OF THE MARKET TODAY AND WHAT TO EXPECT TOMORROW

Thomson Reuters LPC’s Second Annual Middle Market Loan Conference
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From 40,000 feet...

- Global volumes are steady as refinancing activity dominates
- M&A-related lending picks up; U.S. market drives jump in activity

U.S. Leveraged lending: supply/demand re-balance

- Supply of new issue loans picks up
- Demand from loan mutual funds slows, yields tick up, CLO issuance roars on!

U.S. Middle Market

- Banks navigate through Leveraged Lending Guidance
- Lenders voice concerns over convergence with BSL: Cov-lite for smaller companies; narrowing middle market yield premium
- But, do divergence and diversity reign? No shortage of debt providers...
  - Leverage is more conservative, smaller companies see higher yields
  - No shortage of debt offerings from first-lien to unitranche
2013 Global Loan Issuance Hits $4T Record, but...
GLOBAL M&A LOAN ISSUANCE IS A FRACTION OF PRE-CRISIS LEVELS AS EUROPEAN MARKET LAGS, WHILE...

GLOBAL M&A LENDING

SOURCE: THOMSON REUTERS LPC
...U.S. M&A LENDING PICKS UP, APPROACHING $200B SO FAR IN 2014

U.S. M&A loan issuance:
- 2007 record: $471B
- 2013: $360B
New money represents 40% of U.S. lending for the first time in six years
**OVERVIEW**

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Some wishes do finally come true!

M&A-related financings are on the rise

Lev. M&A loan issuance ($Bils.)

May 29, 2014

TRLPC 2nd ANNUAL MIDDLE MARKET LOAN CONFERENCE

SOURCE: THOMSON REUTERS LPC
Refinancings dominated lending activity

U.S. Leveraged Loans:
1Q14 is 3rd busiest on record
REFIs are 3rd highest at $180B

U.S. Leveraged Institutional Loans:
1Q14 is 3rd busiest on record
REFIs are 3rd highest at $112B

May 29, 2014

Source: Thomson Reuters LPC
IT’S ALL ABOUT THE INVESTORS...

PRO RATA VS. INSTITUTIONAL MARKET SHARE

Share of lev. loan issuance

CLO ISSUANCE & RETAIL FUND FLOWS

SOURCE: THOMSON REUTERS LPC, LIPPER
Refi surge defied 2013 forecasts; Leveraged finance reached record $1.47T

LEVERAGED LOAN AND HIGH YIELD BOND ISSUANCE

- HY Bonds
- Leveraged loans
- Lev. Loans Refi
- Lev. Loans New Money

Issuance ($Bils.)

- 1993
- 1994
- 1995
- 1996
- 1997
- 1998
- 1999
- 2000
- 2001
- 2002
- 2003
- 2004
- 2005
- 2006
- 2007
- 2008
- 2009
- 2010
- 2011
- 2012
- 2013 Forecast
- 2013 Actual
- 2014 Forecast

SOURCE: THOMSON REUTERS LPC, THOMSON REUTERS
Will 2014 be a repeat? New money expected up moderately; Refi’s expected down

**LEVERAGED LENDING: NEW MONEY**

- Issuance ($Bils.)
  - Lev. New Money: Dark blue
  - LPC Survey Estimate: Light blue

**LEVERAGED LENDING: REFINANCINGS**

- Issuance ($Bils.)
  - Lev. Refinancings: Orange
  - LPC Survey Estimate: Light blue

*SOURCE: THOMSON REUTERS LPC*
**2014 Outlook:** Leveraged Pro Rata down to $450B, Institutional down to $565B as Refis Slow

**Leveraged Lending: Pro Rata**

**Institutional Loan Issuance**

*Source: Thomson Reuters LPC*
1Q14 LEV. PRO RATA WAS 5TH HIGHEST ON RECORD; INSTITUTIONAL WAS 3RD HIGHEST
LOAN ASSETS MANAGED BY CLOs & LOAN MUTUAL FUNDS REACH RECORD LEVELS

CLO ASSETS UNDER MANAGEMENT

LOAN MUTUAL FUNDS ASSETS UNDER MANAGEMENT

SOURCE: THOMSON REUTERS L.P., LIPPER
But, demand shifts with loan mutual fund outflows beginning in mid-April

Weekly since 2005

Weekly 2011/12/13/14 comparison

SOURCE: LIPPER, A THOMSON REUTERS COMPANY
Loan funds do not dominate demand but they do dominate sentiment; inst. accounts pause

**SHARE OF INDEX OUTSTANDINGS***

- **41%** CLOs*
- **36%** Other
- **22%** Loan Funds

**LOAN OUTSTANDINGS BY INVESTOR TYPE**

- CLOs
- Loan Funds (mutual funds & ETFs)
- Other

*Based on:
- a universe of 779 U.S. CLOs
- S&P/LSTA Leveraged Loan Index outstandings
- the most recent data available

**SOURCE:** THOMSON REUTERS LPC COLLATERAL, LIPPER
DEMAND SLOWS WHILE SUPPLY GROWS: M&A EMERGES IN APRIL/MAY & PIPELINE PICKS UP

MONTHLY LEVERAGED M&A LENDING

WEEKLY U.S. INSTITUTIONAL LOAN PIPELINE

SOURCE: THOMSON REUTERS LPC
As supply/demand re-balance, par-plus share drops in secondary
PRIMARY MARKET LOAN SPREADS TICK UP; SECONDARY LOAN PRICES SOFTEN

U.S. INSTITUTIONAL TERM LOAN SPREADS

CLO LOAN HOLDINGS: AVG. LOAN BIDS

Contractual spread (bps)

Share of loans held by U.S. CLOs

Avg. loan bid (% of par)

SOURCE: THOMSON REUTERS LPC, LPC COLLATERAL
The average yield on institutional term loans ticks up in 2Q14
EXPECT THE UNEXPECTED? WILL PRIMARY MARKET YIELDS STAY UP?

INSTITUTIONAL TERM LOAN YIELDS

<table>
<thead>
<tr>
<th>Yield (3 years)</th>
<th>Monthly</th>
<th>Quarterly</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jan-10</td>
<td></td>
<td></td>
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<tr>
<td>Jun-10</td>
<td></td>
<td></td>
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<tr>
<td>Nov-10</td>
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<td>Apr-11</td>
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<td>Sep-11</td>
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<td>Feb-12</td>
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<td>Jul-12</td>
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<tr>
<td>Dec-12</td>
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<td>May-13</td>
<td></td>
<td></td>
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<tr>
<td>Oct-13</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mar-14</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

FLEX ACTIVITY

<table>
<thead>
<tr>
<th># of flexes up/down</th>
<th>Avg. yield adjustment up/down</th>
</tr>
</thead>
<tbody>
<tr>
<td>4-12</td>
<td>-1.5%</td>
</tr>
<tr>
<td>13-20</td>
<td>-1%</td>
</tr>
<tr>
<td>21-60</td>
<td>0.5%</td>
</tr>
<tr>
<td>&gt;60</td>
<td>1%</td>
</tr>
</tbody>
</table>

B, BB YIELDS

<table>
<thead>
<tr>
<th>Yield (3-year term)</th>
<th>B</th>
<th>BB</th>
</tr>
</thead>
<tbody>
<tr>
<td>0-10</td>
<td></td>
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<tr>
<td>1-5</td>
<td></td>
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<tr>
<td>6-10</td>
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<tr>
<td>11-15</td>
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<tr>
<td>&gt;15</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

SOURCE: THOMSON REUTERS LPC
Meanwhile, demand remains strong from CLOs: issuance expectations move up for 2014

ANNUAL CLO ISSUANCE

CLO issuance

LPC Survey Estimate

2014 CLO issuance estimates ($B.)

SOURCE: WELLS FARGO SECURITIES, THOMSON REUTERS LPC
AS MANAGERS ISSUE VOLCKER-COMPLIANT CLOs

CLO ISSUANCE AND AAA NEW ISSUE SPREADS

- Issuance
- Average AAA spread (excl. MM)
**Middle market CLOs hold loans with higher contractual spreads**

**Contractual loan spreads – All U.S. CLOs vs. Middle Market CLOs**

- U.S. Middle Market CLOs have a higher share (47%) of loans with contractual spreads in the 400-plus bps range.
- The corresponding share for all U.S. CLOs is 28%.
$3.3B of completed MM CLO issuance is ahead of lenders’ expectation of $4.0B in 2014

MIDDLE MARKET CLO VOLUME

2014 CLO ISSUANCE EXPECTATIONS

SOURCE: THOMSON REUTERS LPC, WELLS FARGO LLC
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May 29, 2014

Lender survey: What was the biggest change in the MM in 1Q14?

WHAT WAS THE BIGGEST CHANGE IN 1Q14?

- Leveraged lending guidance is front & center!
- Dealflow controversy:
  - Some say increased level of activity
  - Pick up in new money M&A
  - But most say dealflow remained weak
  - Not enough M&A
- Lower pricing / yield compression
- More aggressive leverage and terms
- Difficult to find quality deals at low leverage
- Continued use of covenant-lite structure
- Fewer covenants on weaker borrowers
- More TLB activity in leveraged middle market
- MM deals becoming more broadly syndicated
- More clubs, less underwrites
- Still too much liquidity
- I-banks continue to move down market
- Prevalence of stretch senior deals

LEVERAGED LENDING GUIDANCE SUMMARY

- Deals treated as “leveraged” include:
  - Proceeds used for buyouts, dividends, etc.
  - Senior debt/EBITDA > 3x
  - Total debt/EBITDA > 4x
  - Loans to vehicles that engage in leveraged finance (CLOs, BDCs, etc.)
  - Fallen angels* (included only upon modification or waiver)
  - ABL* (incl. only if part of entire debt structure of a leveraged borrower)
- Deals treated as “criticized” include:
  - If a company cannot show the ability to amortize 100% of its senior debt or 50% of its total debt within 5 to 7 years
  - Issuers with leverage in excess of 6x debt/EBITDA after asset sales
How will Leveraged Lending Guidance impact banks’ ability to invest in leveraged loans?

LPC Survey: Impact of Leveraged Lending Guidance Survey

- No impact - banks will continue to buy HLT deals
- Modest impact - banks will be more selective in buying HLT deals
- Significant impact - a noticeable drop off in banks purchasing HLT deals

% of respondents


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Banks lower their leverage tolerance for middle market deals as LLG is front and center

SPONSORED: SENIOR DEBT TO EBITDA

SPONSORED: TOTAL DEBT TO EBITDA

4Q13 Survey  1Q14 Survey  2Q14 Survey

4Q13 Survey  1Q14 Survey  2Q14 Survey

SOURCE: THOMSON REUTERS LPC
BUT, NON-BANK LENDERS CONTINUE TO EXHIBIT HIGHER TOLERANCE FOR LEVERAGE IN MM

SPONSORED: SENIOR DEBT TO EBITDA

SPONSORED: TOTAL DEBT TO EBITDA

% of non-bank respondents

1st lien debt to EBITDA

Total debt to EBITDA

SOURCE: THOMSON REUTERS LPC
WILL SMALLER DEALS GO COV-LITE THIS YEAR?

COVENANT-LITE VOLUME
LARGE CORPORATE VS. MIDDLE MARKET

MIDDLE MARKET COVENANT LITE EXPECTATIONS FOR 2014

Volume will grow but only at upper end of MM ($40-$50M+ EBITDA)
Volume will grow and move down market (<$40M EBITDA)
Remain the same
Volume will decline

% of survey respondents
**What structure/term loosening concerns you most in the middle market?**

<table>
<thead>
<tr>
<th>Structure/Term</th>
<th>% of Respondents</th>
</tr>
</thead>
<tbody>
<tr>
<td>Covenant-lite term loans</td>
<td>50%</td>
</tr>
<tr>
<td>Higher leverage levels</td>
<td>40%</td>
</tr>
<tr>
<td>Lower pricing/yields</td>
<td>20%</td>
</tr>
<tr>
<td>Wide covenant cushions</td>
<td>10%</td>
</tr>
<tr>
<td>Second-lien loans</td>
<td>0%</td>
</tr>
<tr>
<td>Builder baskets</td>
<td>0%</td>
</tr>
</tbody>
</table>

**Banks Versus Non-Banks**

- **Covenant-lite term loans**: 50% (Banks) vs. 40% (Non-Banks)
- **Higher leverage levels**: 40% (Banks) vs. 30% (Non-Banks)
- **Lower pricing/yields**: 20% (Banks) vs. 10% (Non-Banks)
- **Wide covenant cushions**: 10% (Banks) vs. 5% (Non-Banks)
- **Second-lien loans**: 0% (Banks) vs. 0% (Non-Banks)
- **Builder baskets**: 0% (Banks) vs. 0% (Non-Banks)

**May 29, 2014 TRLPC 2nd Annual Middle Market Loan Conference**

**Source:** Thomson Reuters LPC
**MOUNTING PRESSURE? MORE CAPITAL, BIGGER HOLDS IN 2014**

Market players reported allocating more capital to lend in the MM and higher hold levels year over year.
**SURVEY: WILL YOU HIT BUDGETS THIS YEAR?**

**YOY EXPECTED CHANGE IN VOLUME**

<table>
<thead>
<tr>
<th>% of respondents</th>
<th>Banks</th>
<th>Non-banks</th>
</tr>
</thead>
<tbody>
<tr>
<td>80%</td>
<td></td>
<td></td>
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<tr>
<td>60%</td>
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<td></td>
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<tr>
<td>40%</td>
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<tr>
<td>20%</td>
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<tr>
<td>0%</td>
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</tbody>
</table>

- -30%
- -20-30%
- -10-20%
- 0-10%
- +0-10%
- +10-20%
- +20-30%
- +30%

**WHY OR WHY NOT?**

- **YES!**
  - Seeing (hoping for) better volume
  - More M&A discussions
  - Built out origination platform
  - Taking bigger hold sizes
  - Strong technicals
  - More focused on lower middle market
  - Bigger product offering

- **NO!**
  - Lack of M&A
  - Too much competition
  - High credit hurdles
  - Leveraged Lending Guidance
  - Structures are too weak
  - Covenant lite pushing down market
  - Pass rate is high
  - Portfolio churn is a big issue

**DO YOU EXPECT TO HIT YOUR LENDING GOAL?**

<table>
<thead>
<tr>
<th>% of respondents</th>
<th>Yes</th>
<th>No</th>
</tr>
</thead>
<tbody>
<tr>
<td>80%</td>
<td></td>
<td></td>
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<tr>
<td>60%</td>
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<td>40%</td>
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<tr>
<td>0%</td>
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</tbody>
</table>

- +0-10%
- +10-20%
- +20-30%
- +30%
- >30%
**1Q14 VOLUME WAS LACKLUSTRE**

**SPONSORED VS. NON-SPONSORED MM VOLUME**

**MM LOAN ISSUANCE**

- **Refinancing**
- **New money (beg. 1Q03)**

*Source: Thomson Reuters LPC*
75% of respondents said they were unable to lend as much as they desired in 1Q14.

DID YOU REACH YOUR 1Q14 LENDING GOAL?

WHAT FACTORS CONTRIBUTED TO THIS?

- **Those who fell below goals attributed to:**
  - Few deals fit Leveraged Lending Guidance
  - Too much competition
  - Lack of supply / limited M&A
  - Too much refinancing activity
  - Uncertainty caused by govt. dysfunction
  - Acquisitions fell through
  - Insufficient yields
  - Poor allocations
  - Low quality deals
  - Weak covenants/structures

- **Those who met goals attributed to:**
  - Existing portfolio company activity
  - Moved up market, moved down market
  - Higher holds
  - Lower budget
  - Direct origination
  - Saw more M&A than in prior quarters
  - Strong pipeline carried over from 4Q13
  - Did deals overseas / global capability

SOURCE: THOMSON REUTERS LPC
And hoped for a pick-up in M&A lending

2Q14 issuance growth expectations

What will drive bulk of activity in 2Q14?

% of respondents

Refi's / Amends and extends
Other
M&A/LBO
Dividend recaps
Capex spending / Working capital
Amendments

% of respondents

0% 10% 20% 30% 40% 50%

0% 10% 20% 30% 40% 50%

Non-Sponsored Sponsored

% of respondents

0% 10% 20% 30% 40% 50%

2Q14 issuance growth expectations

(>15%) (5-15%) Flat +5-15% >+15%

0% 10% 20% 30% 40% 50%

0% 10% 20% 30% 40% 50%

Source: Thomson Reuters LPC
**Lender Survey:**

**What will be most important issue in 2Q14?**

### What was the biggest change in 1Q14?
- Leveraged lending guidance is front & center!
- Dealflow controversy:
  - Some say increased level of activity
  - Pick up in new money M&A
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- Still too much liquidity
- L-banks continue to move down market
- Prevalence of stretch senior deals

### Most important issue in 2Q14?
- Leveraged lending guidance – will we see an impact on banks?
- Feedback from initial SNC reviews
- Educating sponsors on banks’ limitations
- **Large cap structures seeping into MM**
- Avoid doing covenant-lite deals
- **Pricing/spreads**
- LBO volume / pick up in M&A activity
- Structural weakness in credit agreements
- Issuer supply
- **Leverage levels**
- Economic backdrop
- Too much liquidity
MM Private LBO, Large MM Institutional LBO, and Broadly Syndicated LBO Comparison in 1Q14

**Debt to EBITDA for LBO Deals**

- Private MM
- Institutional MM
- Large Corp.

**1Q14 Avg. Purchase Price & Multiple**

- Private MM
- Institutional MM
- Large Corp.

**Avg. EBITDA**

- Private MM
- Institutional MM
- Large Corp.

**Avg. Equity Contribution**

- Private MM
- Institutional MM
- Large Corp.
Will MM Yields Converge?

**Yield Premiums**
- LC 1st lien
- LC 2nd lien
- MM 1st lien
- MM 2nd lien

**Upward Flexes Dominate in MM**

Yield (3-years)

<table>
<thead>
<tr>
<th>Year</th>
<th>LC 1st lien</th>
<th>LC 2nd lien</th>
<th>MM 1st lien</th>
<th>MM 2nd lien</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>2011</td>
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<td>2012</td>
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<td>2013</td>
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<tr>
<td>2014</td>
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</tbody>
</table>

MM institutional flex volume ($M.)

- **Down**
- **Up**

**Source:** Thomson Reuters LPC
And even so, do diversity and... divergence reign in the middle market?

**QUARTERLY MIDDLE MARKET TERM LOAN YIELDS (3-YEAR)**

- LC Institutional All-in Yield
- MM Private Deal TLA
- MM Institutional Term Loan All-in Yield
- MM Private TLB
- Unitranche
- Second Lien

May 29, 2014
RISK/RETURN: SMALLER BORROWERS PRODUCE MORE ENTICING YIELDS AND LESS LEVERAGE

<table>
<thead>
<tr>
<th>AVERAGE YIELD BY EBITDA RANGE</th>
<th>AVG. YIELD &amp; LEVERAGE BY EBITDA</th>
</tr>
</thead>
<tbody>
<tr>
<td>*Leverage on Institutional MM Deals</td>
<td>Debt to EBITDA</td>
</tr>
<tr>
<td>Leverage on Private MM Deals</td>
<td>1st Lien TL Yield</td>
</tr>
<tr>
<td>*Institutional MM TL Yield</td>
<td>Private MM Deals TL A&amp;B Yield</td>
</tr>
<tr>
<td>▲ Private MM Deals TL A&amp;B Yield</td>
<td></td>
</tr>
</tbody>
</table>

- AVERAGE YIELD BY EBITDA RANGE:
  - 2.0
  - 2.5
  - 3.0
  - 3.5
  - 4.0
  - 4.5
  - 5.0
  - 5.5
  - 6.0
  - 6.5
  - 7.0
  - 7.5
  - 8.0
  - 8.5
  - 9.0
  - 9.5

- AVG. YIELD & LEVERAGE BY EBITDA:
  - Debt to EBITDA: 2.0
  - 3.0
  - 4.0
  - 5.0
  - 6.0
  - 7.0

- Yield (3-year):
  - 1Q13
  - 2Q13
  - 3Q13
  - 4Q13
  - 1Q14

- Private MM Deals TL A&B Yield:
  - <$5M
  - >$5-15M
  - >$15-25M
  - >$25-40M
  - >$45-50M
  - >$50M

SOURCE: THOMSON REUTERS LPC
LEVERAGE CREEPS UP FOR SMALLER ISSUERS IN 1Q14 (EXCEPT FOR UNITRANCHE)

1Q14 AVERAGE VS. 2013

- Avg. Senior Leverage
- Avg. Junior Leverage
- Average EBITDA

- Debt to EBITDA
- Avg. EBITDA ($Mils.)
MM issuers get their pick of products...second liens are in vogue

**What structure will sponsors favor?**

<table>
<thead>
<tr>
<th>Structure</th>
<th>2014 Outlook Survey</th>
<th>2013 Outlook Survey</th>
</tr>
</thead>
<tbody>
<tr>
<td>1st / 2nd lien</td>
<td></td>
<td></td>
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<tr>
<td>Stretch senior</td>
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<td></td>
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<tr>
<td>1st lien / mezz</td>
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<td></td>
</tr>
<tr>
<td>Unitranche</td>
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</tr>
</tbody>
</table>

**MM second lien volume**

Source: Thomson Reuters LPC

May 29, 2014
IT’S NOT JUST ABOUT BANKS ANYMORE...

SOURCES AND TYPES OF AVAILABLE DEBT CAPITAL

Traditional Banks

Finance Companies

CLOs

BDCs

Hedge Funds / Credit Opportunity Funds

Insurance Companies

Mezzanine Funds

Private Equity Funds

Traditional

Sub Debt

Preferred Stock

Common Equity

Libor +

150 - 350

Libor +

350 - 500

Libor +

400 - 900

12 - 15%

15 - 17%

20 - 25%

25% +
GAME CHANGERS TODAY! SNC REVIEWS/VOLCKER/RISK-RETENTION/ M&A PICK-UP…

LEVERAGED BUYOUT FINANCINGS

QTRLY: BIGGEST LBO LOAN FINANCING

SOURCE: THOMSON REUTERS LPC
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