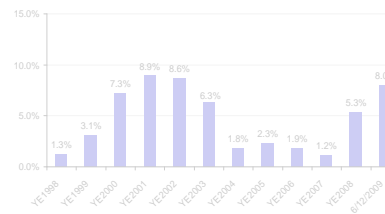
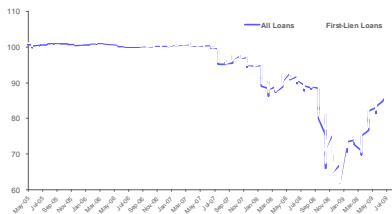


# State of the Financing Markets Webcast

September 9, 2009



# State of the Financing Markets – Agenda

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## **Agenda**

Overall Market Conditions

Overview of Current Sources and Terms of Capital

Successfully Closing Deals in Today's Market

## **Moderators**

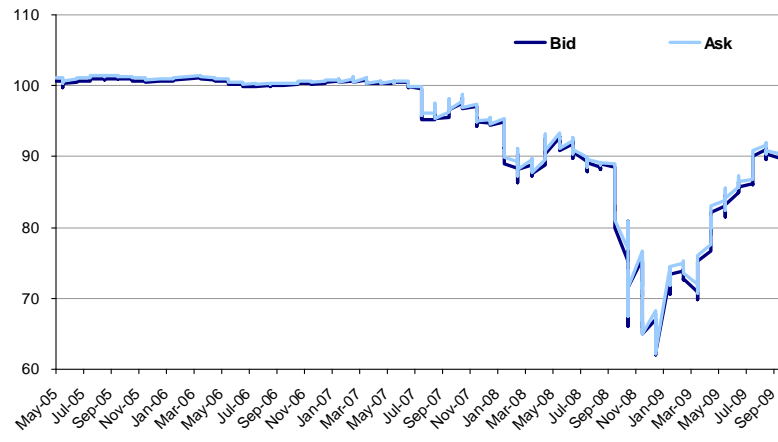
Ron Kahn  
Managing Director  
Telephone: (312) 580-6280  
Email: rkahn@lincolninternational.com

Bob Horak  
Managing Director  
(312) 580-2804  
Email: rhorak@lincolninternational.com

# Overall Market Conditions

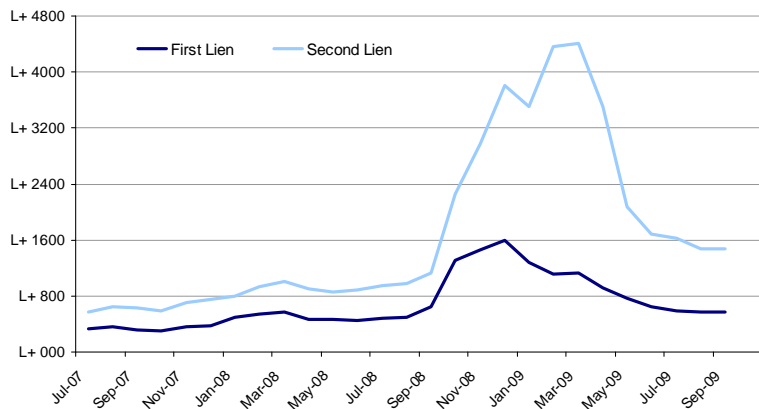
*Technical aspects of the market have been improving*

## Average Bid and Ask of Leveraged Loans



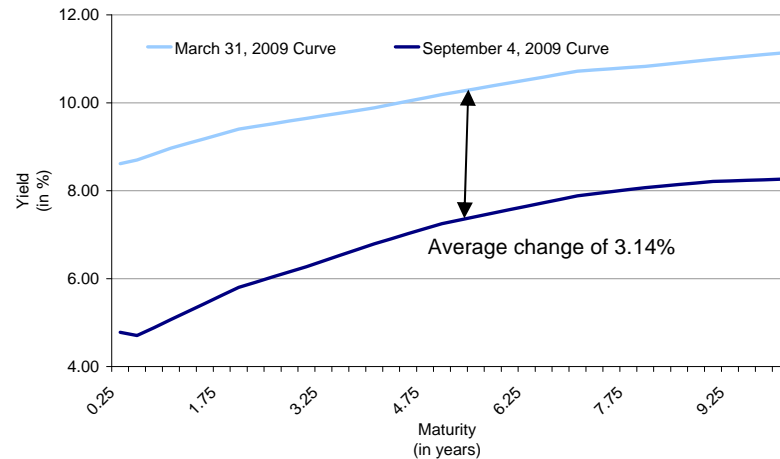
Source: Standard & Poor's Leveraged Commentary and Data

## Average First and Second Lien Secondary Spreads (Index of 15 Largest Issuers with Both Tranches)



Source: Standard & Poor's Leveraged Commentary and Data

## Bloomberg US Industrial BB Yield Curve



Source: Bloomberg

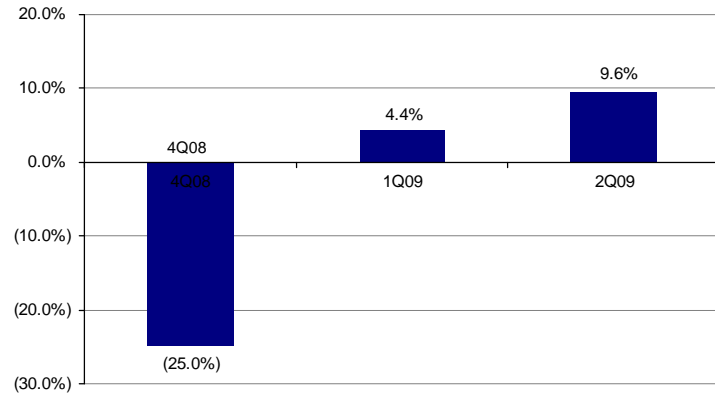
## Market Dynamics

- The LCD index has improved substantially since January 2009
- Reduced return opportunities in the secondary market are pushing financing sources back into the primary market
- With more sources of capital returning to the market, the pricing on some First and Second Lien Loans has begun to decline

# Performance and Credit Quality – Conflicting Signals

*The availability of capital is improving, but only for those companies with strong fundamentals*

## Quarter-over-quarter EBITDA Change for Four Largest Public Filers in Each Industry of S&P/LSTA Loan Index

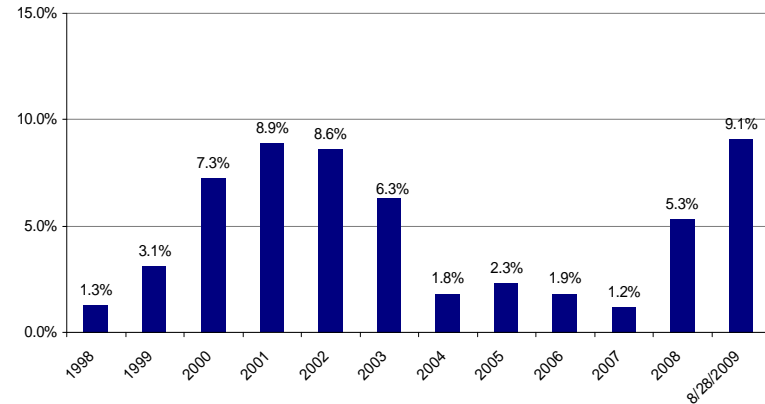


Source: Standard & Poor's Leveraged Commentary and Data

## Market Dynamics

- Conventional wisdom would say that the broader economy is out of the recession and company performance is improving
- However, credit is available for only the highest-quality companies
- The recent stagnation in loan volume and M&A activity is due to a combination of:
  - Lack of visibility into many borrowers' future performance
  - Underwriting standards of lenders still providing capital remaining very tight

## Percentage of Issuers with Outstandings in Payment Default or Bankruptcy



Source: Standard & Poor's Leveraged Commentary and Data

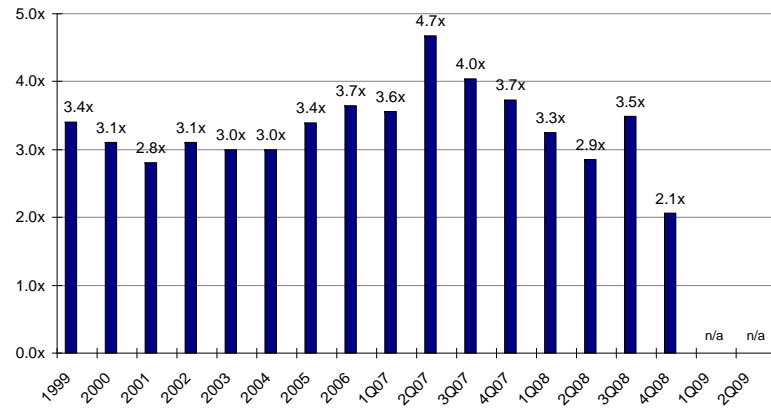
## Market Dynamics

- Defaults have been rising and are expected to continue to increase throughout 2009
- Increase in defaults delayed by:
  - Covenant-light transactions
  - Use of equity cures
  - PIK toggle provisions
- Increased restructuring activity continues

# Senior Cash Flow Market

*Decreased availability of senior debt has driven senior leverage downwards and pricing upwards*

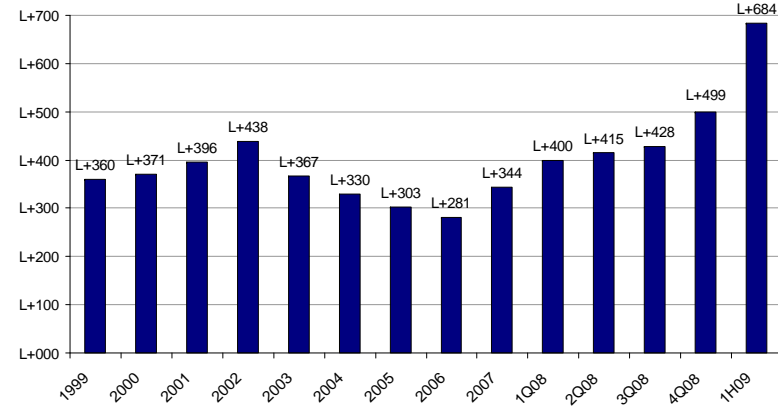
## Average Senior Debt Multiples of LBO Middle Market Loans



Source: Standard & Poor's Leveraged Commentary and Data

Note: Data on Average Senior Debt Multiples is not available for 1Q09 and 2Q09 due to lack of market activity

## Average Institutional Spreads of Middle Market Loans (Issuers with EBITDA of Less Than \$50 million)



Source: Standard & Poor's Leveraged Commentary and Data

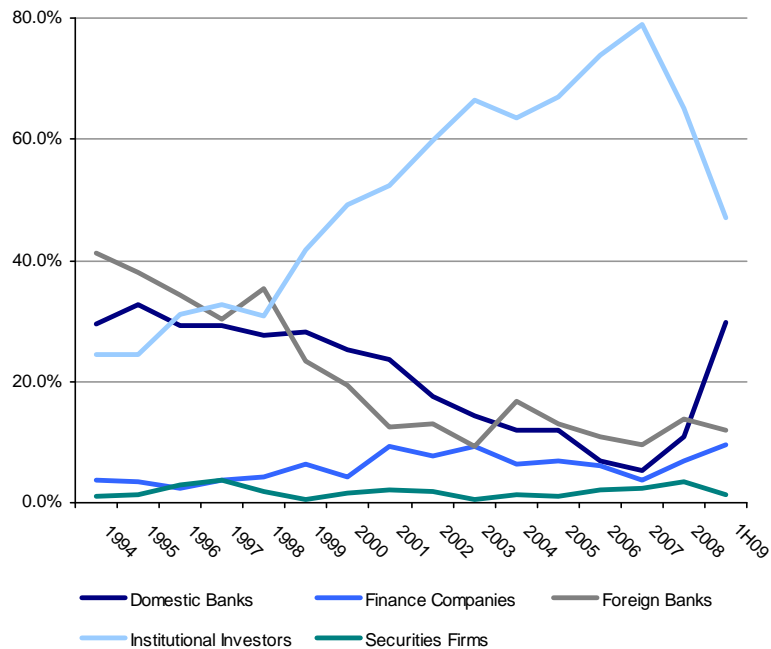
## Market Dynamics

- Senior cash flow lending for companies with under \$10 million of EBITDA is extremely limited
- Cash flow loans are limited to companies with strong fundamentals that are perceived to be recession resistant
- “Club” deals are the norm, with hold sizes rarely exceeding \$20-\$25 million and often in the \$10-\$15 million range
- Regional banks are becoming more active in club cash flow transactions
- Due to the decline in financial performance in 4Q08, lenders are now less focused on TTM performance and more focused on the last six months or 2009 run rate
- Senior lenders are increasingly focused on the “agency” role when deciding whether to participate in a transaction
- Increased amortization now required – focus on fixed charge coverage
- Any changes to the existing agreements (i.e., forbearance agreements, amendments, waivers) are resulting in a re-pricing of the outstanding loans

# Sources of Senior Debt Capital

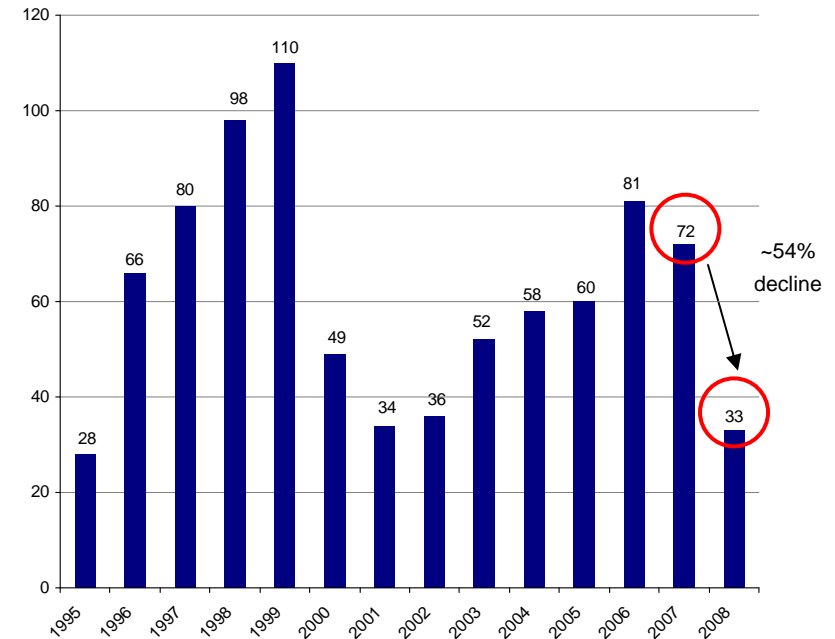
*Liquidity in the senior cash flow lending market has been significantly impacted by reduced participation from CLOs / institutional investors*

## Primary Market for Highly Leveraged Loans by Broad Investor Type



Source: Standard & Poor's Leveraged Commentary and Data

## Most Active Pro Rata Investors (Lenders that Made Ten or More Primary Commitments)



Source: Standard & Poor's Leveraged Commentary and Data

## Market Dynamics

- Institutional investors have been forced to exit the market because of their inability to obtain leverage
- As a result, banks and insurance companies have emerged as the primary providers of senior debt today
- Without the ability to access new sources of leverage, we do not anticipate significant changes in the senior cash flow market

# Asset-based Lending Market

*Asset-based lending has re-emerged as an attractive funding alternative for companies with appropriate collateral*

## Asset-based Lending Market Dynamics

### Funding Availability

- Liquidity exists in this traditional structure provided an issuer has a significant base of assets
- However, asset-based lenders are becoming more conservative and focused on company fundamentals

### Relative Cost Advantages

- Pricing has increased in tandem with the broader credit markets; however, it remains lower than cash flow loans by approximately 200 - 250 bps
- Closing fees are increasing as negotiating leverage has returned to the lending community

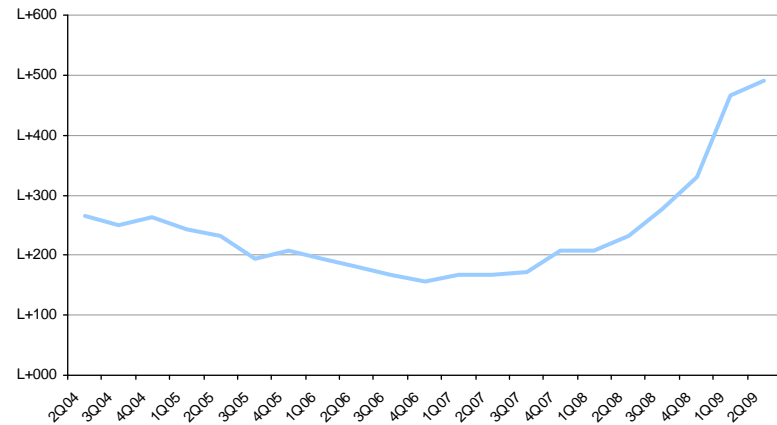
### Not a Universal Remedy

- Not available for service businesses or companies with little base of hard assets
- Increased reporting requirements

### Reliability of Appraisals

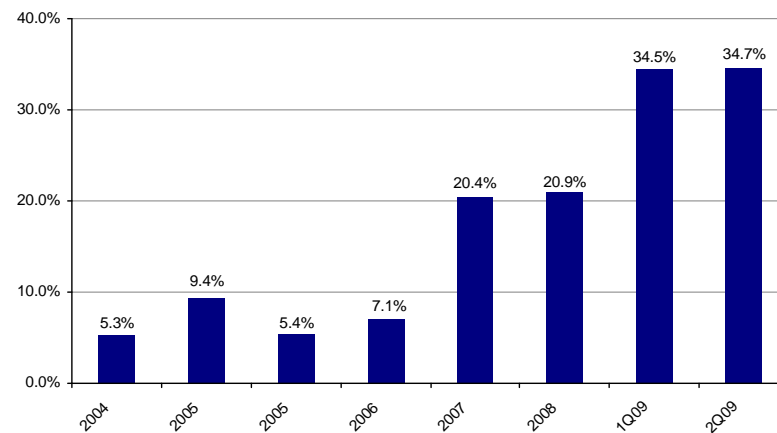
- In light of the recent economic downturn, asset-based lenders have begun questioning the reliability of asset appraisals and, as a result, are reducing the amount of term loans they are prepared to provide borrowers

## Asset-based Pricing



Source: Standard & Poor's Leveraged Commentary and Data

## Asset-based Lending as a Percentage of All Leveraged Loans

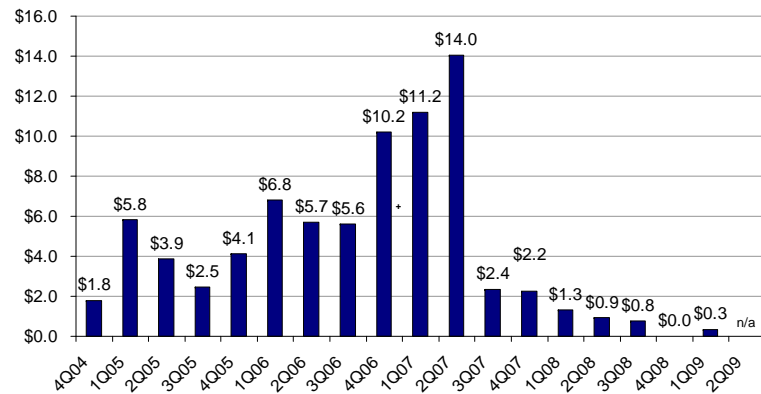


Source: Standard & Poor's Leveraged Commentary and Data

# Second Lien Loans Market

*"Second Lien Lenders Poised for Return to Stage" – Buyouts magazine, August 3, 2009*

## Second Lien Quarterly Volume in the Total Market (\$ in billions)



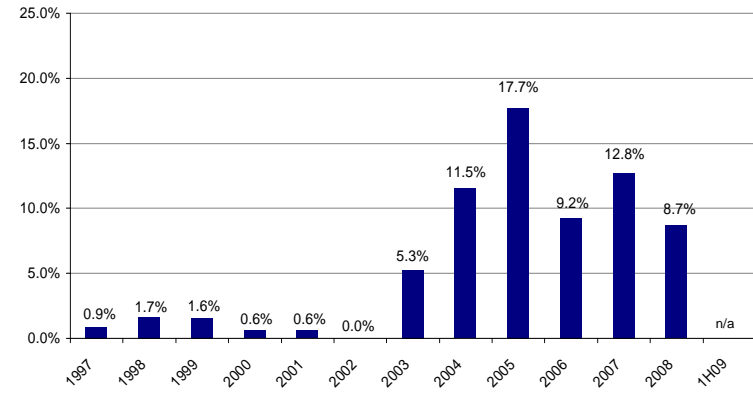
Source: Standard & Poor's Leveraged Commentary and Data

Note: Data on Second Lien Quarterly Volume is not available for 2Q09 due to lack of market activity

## Market Dynamics

- Market conditions have once again begun to resemble the environment in which second lien loans originated
  - Asset-based lenders are becoming more conservative, leaving more collateral value for second lien lenders
  - Higher priced sub-debt leaves the door open for an alternative security
- Inter-creditor terms and issues need to be carefully managed

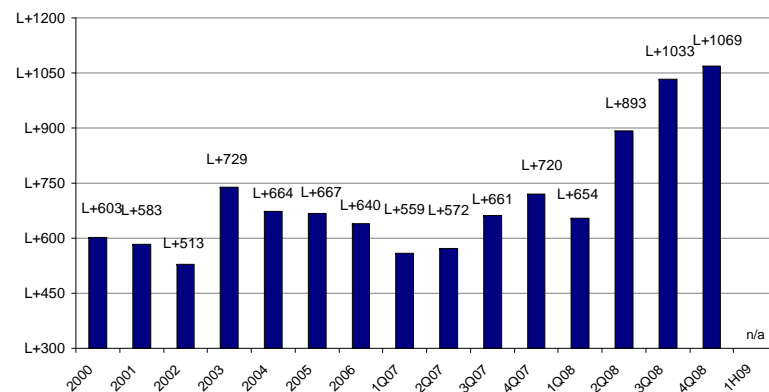
## Second Lien Loans as a Percentage of Mid-Market Volume



Source: Standard & Poor's Leveraged Commentary and Data

Note: Above Data on Second Lien Loans is not available for 1H09 due to lack of market activity

## Second Lien Pricing



Source: Standard & Poor's Leveraged Commentary and Data

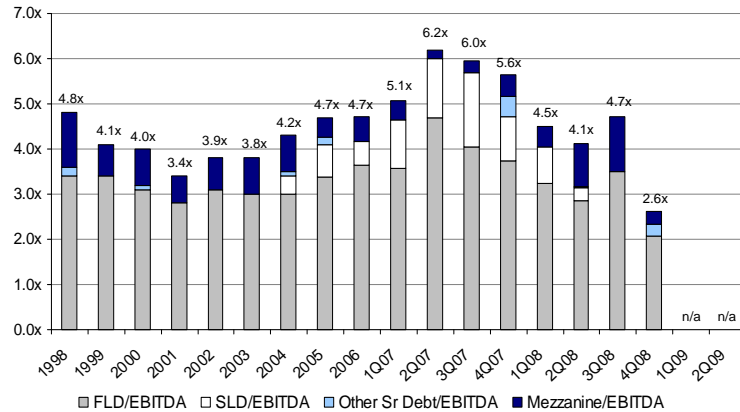
Note: Data on Second Lien Pricing is not available for 1H09 due to lack of market activity



# Mezzanine Debt Market

*Mezzanine debt has become all but essential in completing any kind of financing*

## Average Total Debt Multiples of Middle Market LBOs



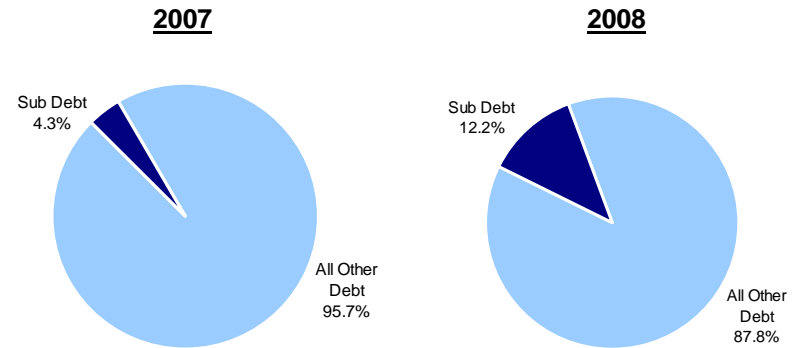
Source: Standard & Poor's Leveraged Commentary and Data

Note: Data on Average Total Debt Multiples is not available for 1Q09 and 2Q09 due to lack of market activity

## Market Dynamics

- Mezzanine debt is now being used more frequently to:
  - Support LBO transactions due to reduced levels of senior debt
  - De-leverage companies that have excess senior debt
  - Perform dividend recapitalizations to replace failed M&A sale processes

## Sub Debt as a Percentage of Total Leverage (Issuers with EBITDA of Less than \$50 million)



Source: Standard & Poor's Leveraged Commentary and Data

## Mezzanine Pricing











- Cash coupons of 12% - 14%
- PIK rates of 2% - 4%
- Closing fees of 2% - 3%
- All-in yields of 16% - 20%
- Warrants are increasingly required; co-investments are becoming less of an alternative to warrants
- Pre-payment penalties are increasingly stringent and make-whole provisions are becoming more prevalent

# Lincoln's View of Current Credit Market

*Lincoln's presence in the market has provided a detailed knowledge of the current market conditions*

|                    | Pricing   | Multiples  |
|--------------------|---|--|
| Asset Based Senior | <ul style="list-style-type: none"> <li>L + 350 – 450</li> </ul>   | <ul style="list-style-type: none"> <li>n/a</li> </ul>                        |
| Cash Flow Senior   | <ul style="list-style-type: none"> <li>L + 600 – 650</li> </ul>   | <ul style="list-style-type: none"> <li>2.00x – 2.50x EBITDA</li> </ul>       |
| Second Lien Loans  | <ul style="list-style-type: none"> <li>L + 800 – 1200</li> </ul>  | <ul style="list-style-type: none"> <li>2.75x – 3.25x EBITDA</li> </ul>       |
| Subordinated Debt  | <ul style="list-style-type: none"> <li>Cash Coupons of 12% – 14%</li> <li>PIK Rates of 2% – 4%</li> <li>All-in Yields of 16% – 20%</li> </ul> | <ul style="list-style-type: none"> <li>3.00x – 3.50x EBITDA</li> </ul>       |
| Equity             | <ul style="list-style-type: none"> <li>n/a</li> </ul>   | <ul style="list-style-type: none"> <li>Generally in excess of 40%</li> </ul> |

# Successfully Closing Deals in Today's Market

| 2009 Selected Transactions that Have Closed or are Currently in Process   |  |   | Keys to a Successful Financing  |  |
|---|--|---|---|--|
| <br>has refinanced its portfolio company<br><br>\$50,000,000<br>Subordinated Debt   | <br>has refinanced its portfolio company<br><br>\$30,000,000<br>Senior Credit Facilities<br>\$8,000,000<br>Second Lien Term Loan | <br>has refinanced its portfolio company<br><br>\$6,700,000<br>Subordinated Debt<br>\$4,000,000<br>Preferred Equity | <ul style="list-style-type: none"> <li>• Need to conduct broad process of contacting financing sources</li> <li>• Must have relationship with an experienced deal champion within the lending organization to ensure reliable and timely feedback on the transaction</li> <li>• Propose an appropriate capital structure that meets market expectations</li> <li>• Expect longer, more time-consuming process with increased due diligence</li> </ul> |  |
| <br>has refinanced its portfolio company<br><br>with<br> | <br>has been recapitalized  | Private Equity Group<br>Is refinancing its portfolio company<br>Manufacturer of Specialty Chemicals<br>\$55,000,000<br>Senior Credit Facilities<br>\$30,000,000<br>Subordinated Debt  |   |  |
| Private Equity Group<br>Is refinancing its portfolio company<br>Manufacturer of Precision Components<br>\$10,000,000<br>Subordinated Debt<br>\$16,000,000<br>Preferred Equity   | Private Equity Group<br>Is refinancing its portfolio company<br>Manufacturer of Extreme Sports Products<br>\$25,000,000<br>Senior Credit Facilities  |   |   |  |

**Lincoln's Debt Advisory Group adds the following value to each assignment:**

- Broad, robust process ensures *best available pricing and terms*
- Generation of multiple alternatives *enhances certainty of closing*
- Transparent process keeps *client totally informed*
- Lincoln's independence assures there is *no conflict of interest*
- Maximum leverage of time and resources for management team and financial sponsor