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Sent: 1/4/2008 4:25 PM.

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Subject: Loan Syndicate Year-End Recap/Outlook.

Another Successful Year for Lehman Brothers' Syndicated Leveraged Loan Franchise:

Despite the market correction which took place over the summer, Lehman Brothers completed another successful year in the syndicated loan business. Lehman's US leveraged loan volume almost tripled, reaching a record high of more than \$142 billion, an increase from \$49 billion in 2006. In 2007, Lehman Brothers acted as a Joint Lead Arranger on 74 leveraged loans, of which 31 were \$1.0 billion or greater and 12 deals that were \$2.0 billion or greater. Lehman Brothers participated in many of the marquee deals of 2007, helping the firm increase its market share and league table standings. This year Lehman Brothers was Lead Left Arranger on 44 deals, up significantly from last year's 26 deals. These deals included: the \$1,375 million Credit Facility for Pinnacle Foods Finance; the \$775 million Credit Facility for Yankee Candle, in which Lehman also acted as Quarterback for the High Yield Bonds in conjunction with the LBO; the \$1,330 million Credit Facility for Entegra Power Group; the \$2,050 million Credit Facility for Dresser Inc.; and the \$1,350 million Credit Facility for Sequa Corporation, which Lehman successfully syndicated post the mid-year market correction.

This past year Lehman provided committed financing for some of the largest deals ever financed in the leveraged loan market, including TXU and First Data. During an especially turbulent fourth quarter, Lehman was one of the most active underwriters, successfully syndicating deals for LKQ Corporation, Tenaska Power (TPF II), Varel International and Sequa Corporation. Looking forward to 2008, Lehman will continue to provide this superior execution in a challenging market environment.

Year-End Review

2007 was not another routine year for the leveraged loan market. A swift and severe correction occurred and is far from over going into 2008.

There was no question that the market at the end of 2006 and in early 2007 was cruising at an unsustainable pace, with a rapidly growing new-issue forward calendar - though what would derail it, when, and how severe the correction would be, was still up for debate. The housing crisis had established itself by 2007 as a worthy threat to trigger a market meltdown. The loan market shuddered in late February as the China sell-off and mounting housing fears combined to send the broader markets tumbling. However, it wasn't until June, once the forward calendar had swelled to a massive \$210 billion and the news that two hedge funds were forced to the brink of collapse due to subprime losses, that the market careened off-course. The news prompted a vicious backlash on leveraged loans by way of drying up demand from the long-time buoy of the loan market, the CLOs. Volatility was rampant throughout the second-half as the market struggled to find consistent sources of demand. Heading into 2008, the market tone continues to be cautious and tentative as the remaining forward calendar pushes into the

new year.

The following expectations and trends are noteworthy heading into 2008:

Supply:

* After record supply of more than \$535 billion in 2007, we believe that issuance should be closer to \$350 billion, buoyed by the remaining \$156 billion in the pipeline. For context, this would leave issuance levels above the \$295 billion in 2005, but well below the 2006 level of \$480 billion.

* LBO activity is expected to decline in 2008. Given the higher cost of debt and lower attainable leverage levels, sponsors are now looking at much lower multiples to achieve targeted returns. However, the average purchase price multiple has only declined by half a turn.

* Strategic buyers are likely to drive M&A activity as LBOs face greater difficulty meeting economic hurdles.

* Opportunistic refinancing will be reduced as a result of much higher market yields, however, a natural level of refinancing will occur to deal with maturities, IPO related refinancings and acquisitions.

Demand:

* Market capacity for large transactions is constrained because of limited CLO issuance. Reduced demand for CLO liabilities (particularly in the AAA tranches) has deprived the loan market of growth from its largest investor class. Instead of CLOs, the new loan market will rely on recently established "credit opportunity" funds, hedge funds and banks returning to prominence (with a subsequent increase in pro rata tranches). The new, largely opportunistic investor base brings greater volatility to the market compared to the buy-and-hold CLOs.

* Despite the sidelined CLOs, most players have stuck with the loan market and with the increase in opportunistic participants the total of active institutional accounts increased in 2007, reaching 307 from 254 a year ago. If the CLO problem persists, some managers will be forced to exit in 2008, while others consolidate. These departures should be balanced by a number of relative-value players entering the market to take advantage of today's wider spreads.

* LCDS and LCDX volumes soared in 2007 - a trend that is expected to continue in 2008 as the indices give investors for the first time the opportunity to short paper and hedge the market. The products are more transparent and liquid than the cash loan market giving accounts the ability to enter and exit the asset class with greater ease - resulting in greater volatility in recent months. With no accurate measure for the price of risk in the loan market historically, we expect the LCDX to continue to serve as a key indicator of market sentiment.

Credit Fundamentals:

* Given how aggressively the latest generation of LBO's are leveraged, default rates are expected to rise materially over the next 12 to 18 months. This will likely have the effect of constraining leverage levels from returning to the pre-market correction levels.

* Because of loans' senior position in the capital structure and traditionally higher recovery rates, we believe there will still be demand for the loan asset class in the event of a credit cycle downturn.

New-issue:

* The underwriting community is still undergoing a healing process having incurred significant losses in the latest generation of LBO's. The willingness to commit will be tempered by this and the near term results will likely be lower commitment levels, wider caps and lower leverage

* New-issue timing will be driven largely by market windows as arrangers wait to take advantage of any rallies

* While the market has stepped up in size for transactions such as Chrysler Financial, First Data and TXU - demand will require yields of L + 350 - 450 to continue to attract the non-traditional buyers who have populated these books (a fluid benchmark given the volatile secondary). The 9% yield for the senior most part of the capital structure may be a constraint on new deals being committed.

For the detailed 2008 outlook please see Lehman Brothers' Fixed Income Research - U.S. Credit Strategy Publication - "When Will Liquidity Return"/ Leveraged Loans and CLOs.

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