

Managing to a “Bad Asset” Solution

Objectives and Key Challenges

Objectives

- Contain the Problem; initiate a fresh start
- Manage / focus investor, regulatory and rating agency concerns
- Maximize long-term value of troubled assets
- Bolster capital
- Increase financial flexibility
- Reduce leverage
- Preserve/utilize any tax losses associated with dispositions
- Dampen stock price volatility
- Maintain upside through equity participation
- Free mgmt from nuisance of loss producing assets



Key Challenges

- Replenish capital lost in asset dispositions
- Finance NewCo assets
- Achieving optimal capital structure on economical terms
 - Equity / preferred / sub-debt / senior; privately / publicly issued
- Avoiding onerous regulatory constraints ('40 Act)
- Avoid Section 23A & 23B issues (Bank/affiliate extensions of credit and sales of assets)
- Pros and Cons of on versus off Balance Sheet Financing
- Achieving off Balance Sheet treatment under US GAAP
- Achieving/preserving recognition of tax losses

“Bad Assets” – Spectrum of Alternatives

Sale Alternative	Status Quo: Opportunistic Selling	NewCo w/3 rd Party Manager	NewCo w/LB as Manager
Spin Alternative	RBIT Spin-off	<ul style="list-style-type: none"> ▪ <u>Description:</u> <ul style="list-style-type: none"> – Bad assets contributed to a 3rd party vehicle in exchange for equity participation – Assets become independently managed – Vehicle to assume other banks’ assets as well ▪ <u>Pros:</u> <ul style="list-style-type: none"> – Assets transfer off balance sheet – Equity upside participation – Breadth of vehicle may enhance ability to attract financing ▪ <u>Cons:</u> <ul style="list-style-type: none"> – Financing required <ul style="list-style-type: none"> – LB may be asked to participate – Potential hit to Parent equity if m-t-m valuation discrepancy arises and/or selling discount is required – Valuation dynamics; asset-for-equity calculus 	<ul style="list-style-type: none"> ▪ <u>Description:</u> <ul style="list-style-type: none"> – Bad assets contributed to a newco – LB serves as manager of assets and raises 3rd party debt and equity ▪ <u>Pros:</u> <ul style="list-style-type: none"> – Assets transfer off balance sheet – Equity upside participation – LB continues to manage its destiny <ul style="list-style-type: none"> – Potentially better story for shareholders ▪ <u>Cons:</u> <ul style="list-style-type: none"> – Financing required <ul style="list-style-type: none"> – May be more challenging to raise given portfolio / asset profile / diversification
	<ul style="list-style-type: none"> ▪ <u>Description:</u> <ul style="list-style-type: none"> – Effectively status quo scenario – look to move assets when opportunities arise – Option to transfer bad assets to a subsidiary to provide transparency ▪ <u>Pros:</u> <ul style="list-style-type: none"> – Potentially avoids “big bath” headlines a la UBS – Opportunistic approach drives flexibility ▪ <u>Cons:</u> <ul style="list-style-type: none"> – Still on balance sheet – Slow process; continued exposure to market swings (+/-) – Financing may still be required for individual sales 		