Introductions

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Corporate M&A thrived in 2015, while LBO activity faded, reaching a three-year low of $68.5 billion in 2015, from a post-credit-crunch high of $85.3 billion in 2014.
Key Drivers for Leveraged Buyout Activity

Private Equity Dry Powder

- Capital Raised ($ in billions)
- Cumulative Overhang ($ in billions)

Primary Market for Leveraged Loans

- Banks
- Non-Banks

U.S. Private Equity Activity by Year

- Deal Value ($B)
- # of Deals Closed

Private Debt Dry Powder

- Capital Raised ($ in billions)
- Cumulative Overhang ($ in billions)

Source: S&P Capital IQ, Pitch Book, Preqin
Overview of Transaction Structures

Average Middle-Market LBO Purchase Price Multiples

Debt Multiples of Sponsored Middle-Market Loans

Average LBO Capital Structure

All-In Spreads of Institutional Loans Backing LBO's

Source: S&P LCD (Middle-Market Defined as Less Than $50 Million EBITDA)
Leveraged Lending Regulatory Environment

**Leveraged Lending Issues in Lead-Up to Financial Crisis**

- Differences in underwriting for loans held versus loans distributed to the market
- Absence of meaningful financial covenants
- Inadequate reporting or aggregating of enterprise-wide exposure
- Insufficient documentation to support validation of financial sponsor projections and/or enterprise values

**Updated Interagency Leveraged Lending Guidance Issued in 2013 and FAQs Issued in 2014**

Purpose is to ensure:

- Institutions engage in transactions that reflect a sound business premise, an appropriate capital structure, reasonable cash flow and reasonable leverage (i.e., prohibition against non-pass originations)
- Borrowers have the capacity to repay and de-lever over a reasonable period of time
- Institutions define exposure and concentration limits
- Management information systems reporting is comprehensive and aggregate across all business lines

*Guidance applies to all supervised financial institutions that originate, hold, distribute or participate in leveraged lending activities*

**2015 Shared National Credit Press Release: Statement on Leveraged Lending**

- Volume of non-pass loans declined sharply post issuance of FAQs
- Weak underwriting characteristics continue to include minimal deleveraging capacity
- Loan covenant protection deteriorated as evidenced by reduced number of financial maintenance covenants, the use of net debt in leverage covenants, excessive headroom, springing features and various accordion features including incremental facilities that allow increased debt above starting leverage and the dilution of senior secured positions
- Incremental facilities are drawing attention because of their increased usage in conjunction with relaxation of other structural elements such as covenants and restricted payments