Middle Market Commercial Loans

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As an introduction to the United States Middle Market Collateralized Loan Obligation ("MM CLO"), I will highlight its key attributes and then better define what constitutes the US middle market space

- Key Attributes
  - Relative Value
    - MM CLOs offer domestic and global investors attractive spreads on a risk adjusted basis
  - Diversification
    - MM CLOs present an excellent opportunity for investors to diversify away from traditional CLOs backed only by broadly syndicated leveraged loans
  - Good Growth Prospects
    - There are strong growth prospects in the middle market space. The wave of bank consolidation in the past decade has left a void in this lending space and provided an opportunity for finance companies, asset managers and hedge funds to capitalize by utilizing risk based pricing

Middle Market Commercial Loans

Overall Leveraged Loan Market

Large Syndicated Loans

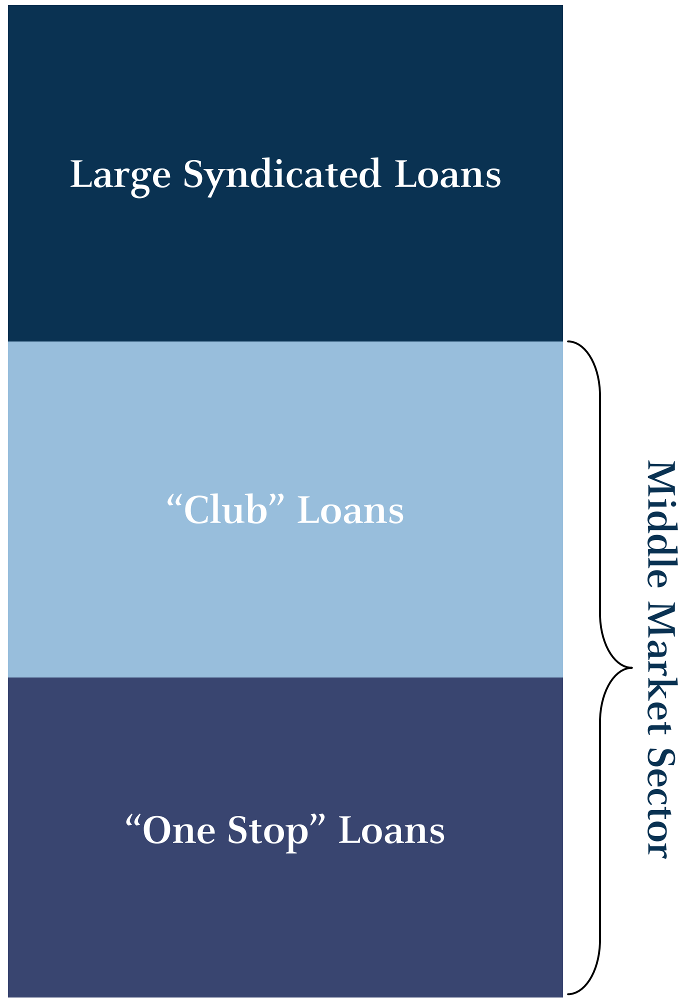
EBITDA:	$50+ million
Loan Size:	$125 million - $1+ billion
Rating:	BB- / Ba3
Pricing:	L+300-325 bps

"Club" Loans

EBITDA:	$25-50 million
Loan Size:	$50-125 million
Rating:	Shadow Rated (B+ / B1)
Pricing:	L+400-600 bps

"One Stop" Loans

EBITDA:	$5-25 million
Loan Size:	$10-75 million
Rating:	Not Rated (Implied B area)
Pricing:	L+550-800 bps



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Defining the Middle Market Commercial Loan

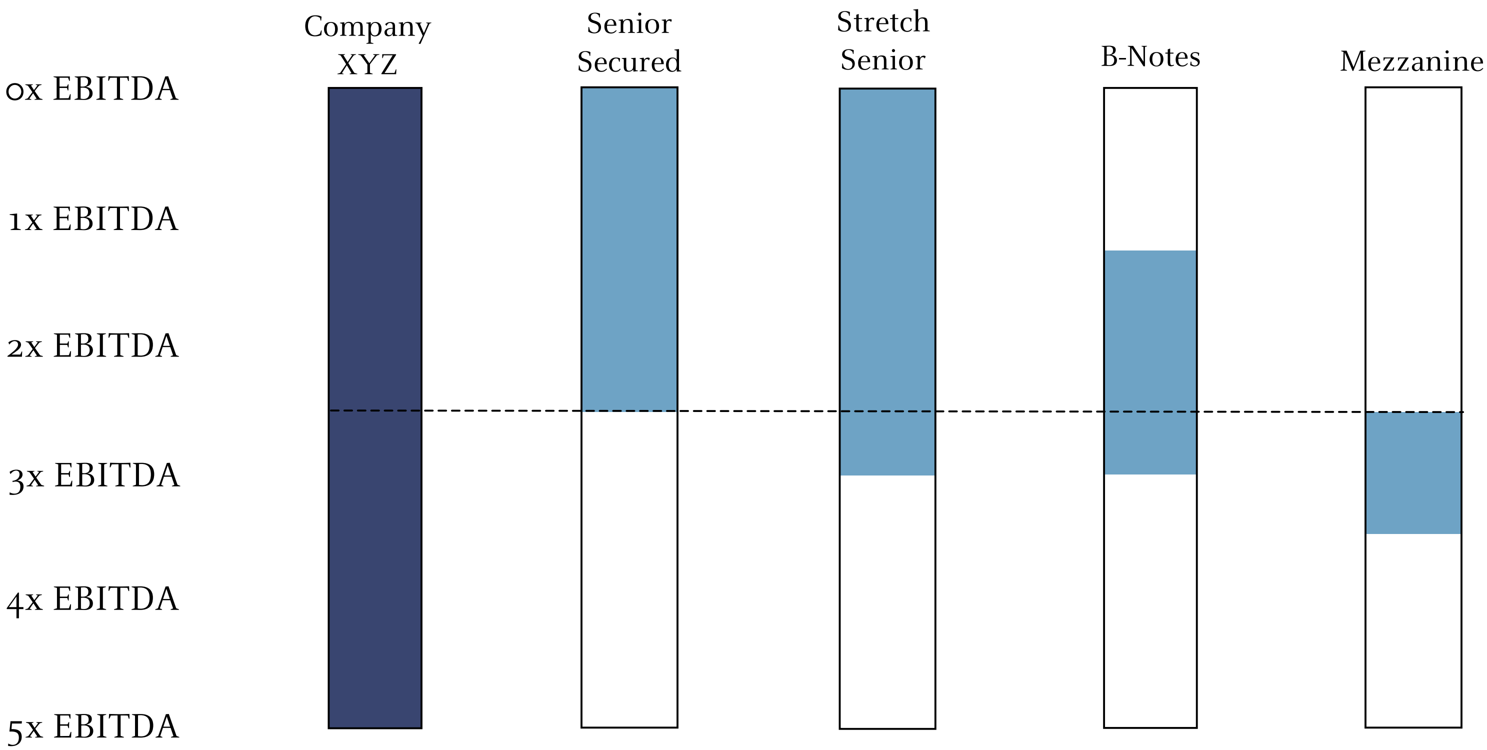
• Obligor:	\$25 million to \$500 million in annual revenue Primarily private companies Personal guarantees are atypical
• Rating:	Typically non-rated (implied "BB" to "B" area)
• Loan Size:	\$10-200 million
• Type:	Asset-based, senior secured, senior cash flow, mezzanine or subordinate cash flow loans
• Collateral:	Operating cash flow, common equity, and any unencumbered assets, e.g., inventory, receivables, equipment, or real estate
• Amortization:	Straight line, balloon, or bullet (revolver or term)
• Term:	Senior secured: 3-5 years Subordinated: 7-10 years
• Payment:	Monthly or quarterly
• Coupon:	Senior secured: L+125-900 (typically floating) Subordinated: 11-12% current (typically fixed) plus deferred interest and/or warrants to yield 18-22% total return
• Use of Proceeds:	Leveraged buyouts, recaps, acquisitions, funding of growth strategies
• Market Size:	\$900 billion

Middle Market Commercial Loans

Middle Market Loan Types

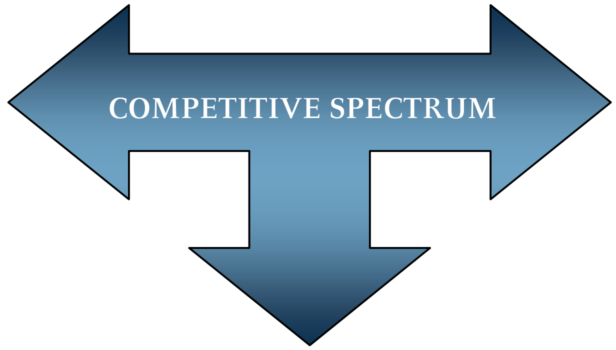
- **Asset-based loans** finance working capital requirements
  - Collateralized by receivables and inventory, may have recourse to inventory
  - Revolver tied to borrower base
  - Expressed in terms of loan to liquidation value
  - Pricing: L+200-350 or P to P+150 bps
- **Cash flow loans** finance needs ranging from working capital to private equity group (PEG) activities, e.g., leveraged buyouts, recaps, and acquisitions
  - Include senior secured, "stretch" senior, "last out" senior, and mezzanine financing
  - Traditional bank lenders target established companies in stable industries
  - Specialty lenders and select bank lenders focus on PEG related activity
  - Primarily collateralized by operating cash flow
  - Underwritten to a multiple of EBITDA or loan to enterprise value
  - Senior secured: L+450-800 bps (floating); Mezzanine: 11-12% (fixed) plus deferred interest and/or warrants to yield 18-22%

Types of Cash Flow Loans (assumes 5x EBITDA firm valuation)



Relative Recoveries		70%	58%	30%	0%

Domestic US Market Participants - Lenders



SENIOR SECURED LENDERS

- Ableco
- Antares
- BNP Paribas
- Callidus
- CapitalSource
- Denali Capital
- GE (Heller)
- Gladstone Capital
- Guggenheim
- Madison Capital
- MCG Capital
- Merrill Lynch Capital Group
- Ramius Capital
- Royal Bank of Scotland

ASSET BASED LENDERS

- CapitalSource
- CIT
- Congress Financial
- Fleet Capital
- Foothill Capital
- GE Capital
- Merrill Lynch Capital Group

MEZZANINE LENDERS

- Ableco
- Albion Alliance
- Allied Capital
- American Capital
- Capital Resource Partners
- CapitalSource
- Gladstone Capital
- J.H. Whitney
- MCG Capital
- Ramius Capital
- William Blair & Co.
- Windjammer Capital
- Numerous Funds

Domestic US Market Participants - Lenders

- The following characteristics are observed across middle market lenders, operating as specialty finance companies. To date, these companies have utilized securitization as a financing source
  - Significant equity capital
  - Conservative operating leverage
  - Experienced management teams
  - Credit focus
    - originate assets with intent to own the risk
    - rarely purchase loans on a "whole loan" basis
    - do not originate to a "box" for capital markets execution, e.g., diversity considerations
    - underwriting not dictated by rating agency view of credit
  - Loans priced on a risk-adjusted basis (no expectation of fee income)
  - Securitization viewed as a financing rather than a vehicle for risk transfer
- Additional participants domestically are collateral managers that originate middle market loans to contribute to CLOs
  - Contribution is equal to about 50% of collateral balance
  - The following characteristics describe the participants:
    - experienced management team
    - strong credit culture and investment professionals
    - loans priced on a risk adjusted basis (no expectation of fee income)
    - ownership of 25% of equity of the securitization with a significant management fee subordinate in the cash flow of the issuance, creating "skin in the game"

Middle Market Commercial Loans

Supply and Demand in the Middle Market

- Number of domestic US banks has declined from 15,000+ in 1990 to less than 8,000 in 2004
  - Major banks have exited middle market due to:
    - > historical mispricing and illiquidity;
    - > focus on higher volume business and fee opportunities
- Absence of traditional bank lenders restricts supply of debt capital
  - Lending multiples return to rational levels
  - Loan pricing returns to risk-based levels
  - Demand for debt capital significantly outpaces supply
- Eight of ten middle market companies expect economic growth over the next twelve months[1]
  - 31% expect to fund growth with debt capital

[1] The Gallup Organization – October 2003 – poll conducted on a sample of 500 middle market companies ($25MM to $500MM annual sales)

Middle Market Commercial Loans

Issuances That Have Included Middle Market Loans[1]

ACAS 2003-2	$397 million	Fourth Quarter 2003
CS 2003-2	$500 million	Fourth Quarter 2003
Navigator CDO 2003	$479 million	Fourth Quarter 2003
Fleet Commercial Loan Trust 2003-2	$1,382 million	Third Quarter 2003
Denali Capital CLO III	$403 million	Third Quarter 2003
ACAS 2003-1	$308 million	Second Quarter 2003
CS 2003-1	$450 million	Second Quarter 2003
CS 2002-2	$325 million	Fourth Quarter 2002
ACAS 2002-2	$210 million	Third Quarter 2002
Fleet Commercial Loan Trust 2002-1	$1,000 million	Third Quarter 2002
GSC Gemini Fund	$693 million	Third Quarter 2002
Denali Capital CLO II	$340 million	Third Quarter 2002
Mariner CDO 2002	$411 million	Third Quarter 2002
CS 2002-1	$275 million	Second Quarter 2002
ACAS 2002-1	$200 million	First Quarter 2002
Ark II 2001-1	$665 million	Fourth Quarter 2001
Denali Capital CLO I	$400 million	Fourth Quarter 2001
MCG 2001-1	$353 million	Fourth Quarter 2001
First Source Obligations Insured Trust	$265 million	First Quarter 2001
Ark 2000-1	$1,307 million	Fourth Quarter 2000
ACAS 2000-1	$154 million	Fourth Quarter 2000
Fleet Commercial Loan Trust 2000-1	$1,000 million	Fourth Quarter 2000
First Source Obligations Trust	$641 million	Fourth Quarter 2000
Antares Funding LP	$600 million	Fourth Quarter 1999
First Source Financial LP	$2,181 million	Third Quarter 1999

[1]Source: Moody's Investors Service, Inc., Standard and Poors Corp., Fitch, Inc. and Wachovia Securities