LAMPERT DEBT ADVISORS

State of the Debt Capital Markets

ADDRESSING THE DEBT FINANCING NEEDS OF MIDDLE MARKET COMPANIES AND FINANCIAL SPONSORS

Volume V, Issue I

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Contents

By the Numbers

Unemployment

7.9% (Jan)

Prime Rate

3.25%

Treasury Yields

2-Year Note - 0.26%

10-Year Note - 2.01%

EURO/USD

$1.34

3-Mo LIBOR

0.29%

LIBOR Swaps (USD)

2-Year - 0.41%

5-Year - 1.01%

Leveraged Loan Volume

$55B (Jan)

High-Yield Volume

$31B (Jan)

Lampert Debt Advisors specializes in structuring and raising capital for middle market companies. We are dedicated to meeting the debt financing needs of privately-owned, sponsor-backed and publicly traded growth companies. We focus on companies seeking to raise between $15 and $150 million through the placement of creative financing solutions. Our principals have completed over $20 billion in financings across a diverse range of industries and financing structures.

Summary

The Economy

- Despite relatively slender U.S. growth during 2012, we are more optimistic about the near-term outlook for the economy and its implications for investing than at any time in the past three years.
- Economic growth will likely improve to 3+% in 2013 despite the effect of the likely spending sequester (automatic spending cuts of $110 billion in 2013).
- The employment picture has continued its slow trend of modest improvement, but we expect it to remain a consistent drag on the economy and consumer sentiment. January unemployment remained essentially unchanged at 7.9%.
- During 2013, we envision limited changes in the Fed's accommodative policy that has pushed the Fed funds rate to near-zero and helped cap the LIBOR one, three and six month rates below 50 bps.

The U.S. Credit Markets

- The current high levels of liquidity characterizing our markets are yielding historically low financing rates without precedent in our lifetimes.
- As of February 14th, the middle-market premium reached an all-time high of 173 bps (L+554 vs. L+382). For context, during the last red-hot debt market, 2007, the premium borne by mid-market credits was 39 bps (301 bps vs. 262 bps).
- According to S&P, CLO issuance over the past 6 months has totaled $42.83 billion, including a shade over $12.2 billion year-to-date.
- Assuming a LIBOR floor of 1.25% and ignoring any original issue discount (OID), the current average yield on middle market institutional loans is 6.79%
- Harkening back to the halcyon days of 2007, covenant-lite loans have returned to represent a meaningful portion of new-issuance.

The Economy

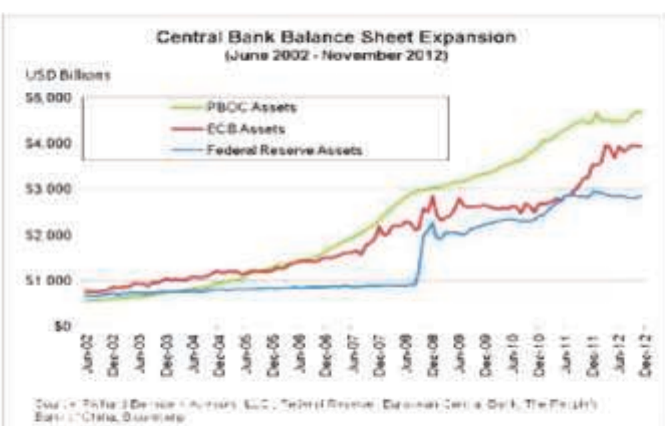
The Year in Review

As Yogi Berra once said, **"it's like déjà vu all over again."** Nowhere does this hold more true than in our year-end review of the economy, comparing today to last year. The following table of key statistics shows how little has changed in the past year:

($ in trillions)	2011	2012	Change
Unemployment Rate	8.3%	7.9%	0.4%
GDP Growth	1.8%	2.2%	0.4%
Fed Funds Rate	0-0.25%	0-0.25%	UNCH
10-Year Treasuries	1.97%	1.91%	6 bps
Federal Debt Load	$14.9	$16.1	$1.2
President	Obama	Obama	UNCH

The retrospective statistics described above paint a picture of **an economy little changed year-over-year**. Last year's outlook was clouded by the Eurozone crisis, a slow-down in Chinese production and fears of the fiscal cliff. While these factors heightened concerns of a repeat recession, **monetary expansion in all three zones kept the world economy on a firm, yet modest growth track**. Despite relatively slender U.S. growth during 2012, we are more optimistic about the near-term outlook for the economy and its implications for investing than at any time in the past three years. We are also **less concerned with the potential for disruptions in our ongoing recovery**. In short, **our recessionary concerns have been washed away by the rising tide of worldwide liquidity**.

The scope of **worldwide monetary expansion by virtually all leading central banks is without precedent**. This deluge of liquidity makes the first decade of the millennium look like a puddle compared to a flood zone. Growth in central bank assets has been largely uncoordinated, but the impact on worldwide liquidity has been uniform. The following table illustrates the level of expansion by each of the three largest central banks in the world: China, Eurozone and U.S.



Domestic attention has been paid to the dramatic expansion in Federal Reserve assets, with continual increases arising from monthly purchases aggregating about $85 billion. Transaction rates for leveraged buyouts are approaching the U.S. Treasury yields that prevailed less than three years ago. However, the U.S. effect is dwarfed by worldwide growth in central bank assets. Chinese and ECB holdings are $1.5 trillion and $1 trillion greater than those of the U.S., respectively. Monetary efforts by the People's Bank of China have been conducted to maintain their economic growth engine in the face of retreating demand from the U.S. and Europe. The EU has stabilized capital flows within its member countries, but it has come at the cost of a bloated balance sheet that threatens to bring further devaluation to their currency.

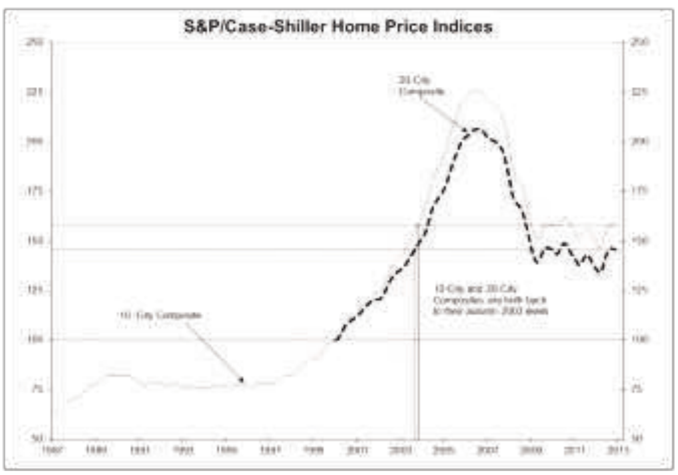
Outside of these majors, countries like Switzerland, with limited need for monetary expansion, and Japan, with a substantial need for stimulus, have been forced to offset the deleterious effects of currency appreciation with asset purchases. In effect, they are **engaging in the first skirmishes of what could be a brutal currency war** in which nations **purposefully devalue their currency to stimulate aggregate demand**. The forced resignation of the Japanese Central Bank head was a clarion call to the BOJ to drive exports through currency depreciation. The high level of popular support for the new Prime Minister, Shinzo Abe, will continue to steel his hand as he bends the Bank of Japan into a more stimulus-oriented posture. **The result may be currency wars that heighten worldwide liquidity, create supply/demand imbalances and spur global inflation.**

In the near-term, we are **encouraging the aggressive use of debt to acquire operating and financial assets**. In the long-term, we see worldwide inflation affecting both commodities and investment assets, alike. **We expect rates to remain at unprecedentedly low levels for the foreseeable future, but thereafter the flipside of heightened liquidity occurs**. **Inflationary pressure promotes higher asset values while the real value of fixed rate obligations declines, providing a unique environment to harvest gains.** The question of whether or not to invest then revolves around the outlook for the economy and its impact on investment decisions.

Consumer Sector Outlook

The consumer continues to be the main engine of U.S. economic growth. In turn, the consumer outlook is driven by housing economics, employment and personal income– all of which are captured in measurements of consumer confidence and sentiment.

The housing market turnaround began in earnest during 2012 and has continued into 2013, with both volume and price improvements. As the chart indicates, housing sales have returned to and exceed the monthly sales levels achieved prior to 2008. Sales prices for the S&P/Case-Shiller 20-City Composite climbed 5.5% for the twelve months ended November 2012.



With home prices on the mend, reduced housing stock overhang from the foreclosure bulge and historically-low mortgage rates facilitating transactions, we envision the strength of the housing market playing a large contributing to consumers' sense of well-being going forward.

The employment picture has continued its slow trend of modest improvement. In previous issues, we have outlined some of the reasons the employment situation is one of the most intractable issues for the current administration to resolve. **We expect it to remain a consistent drag on the economy** and consumer sentiment. January unemployment remained essentially unchanged at 7.9%, while nonfarm payroll additions of 157,000 remain well below the 200,000 per month needed to reduce unemployment.

Personal income spiked in 4Q12 on the strength of an improving economy, and as importantly, on accelerated dividend payout schemes adopted by companies to confront impending tax increases. However, the net impact to consumers will be muted by the concomitant return of higher payroll taxes attendant with the expiration of fiscal stimulus programs introduced during Obama's first term. December spending increases were approximately half the increase in November, largely attributable to fiscal cliff concerns, which gave rise to an improved savings rate of 6.5% of personal income, up from 4.1% in November. **With the fiscal cliff largely resolved, we believe consumer spending will play an increasing role in the achievement of a more robust economy**, bolstered by lower finance costs for both consumption and investment expenditures by consumers.

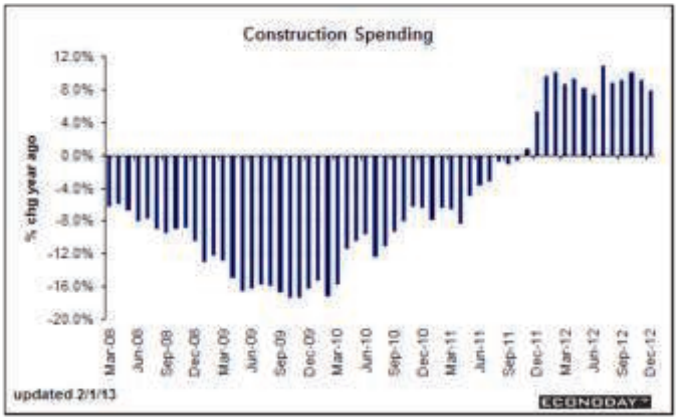
Overall, the U.S. consumer remains cautious. Consumer confidence measures by both the University of Michigan and the Conference Board retrenched in the face of the fiscal cliff and Congress's inability to resolve it. **But given recent stock price movements, housing market improvements and an outlook for low financing rates, we anticipate consumer confidence to revert to higher levels paired with more robust consumer spending**.

Industrial Sector

The U.S. **industrial sector has continued to buttress the measured pace of recovery**. While we were dismayed by news that 4Q12 GDP declined by 0.1%, we attribute the decline to cautiousness in the face of the election and the daily doomsday drumbeat from the media. While the combined impact of government spending cuts and higher taxes would have a strong deterrent effect on the economy, we believe media attention fanned the flames of concern beyond the possible impact. **Once resolved, we have seen evidence of how transitory the impact was. New orders ended the year on a crisp upturn, rising 4.6% in December compared to a 0.7% increase in November**. Driven largely by end of year defense orders, the increase was 1.2% excluding defense and represented the seventh increase in the last eight months. **Shipments also continued to grow, as they recorded a 1.3% increase on the heels of a 1.8% rise in November**.

The level of factory orders at year end support our view of a strong 2013. Further evidence takes the form of recent purchasing managers surveys. Both of the Institute for Supply Management's key indices, the ISM Manufacturing Index and the ISM Services Index are above 50, the level demarcating growth. The non-manufacturing survey for December posted 56.1, a 1.4 point gain, and the strongest rate of monthly growth since February. **The manufacturing survey notched a 2.9% rise to 53.1, with all five components- new orders, production, supplier**

deliveries and inventory and employments- all registering above 50. Business activity, the equivalent of a production index on the manufacturing side, showed especially strong growth rates as did new orders, both ending the session around 60. Employment had its best growth since March. The Markit PMI Manufacturing Survey (purchasing managers) reflects a similar growth outlook at a January reading of 56.1.



And finally, at long last, **construction spending appears to be restored as housing starts rise, infrastructure projects commence and corporations and commercial enterprises take advantage of low rates to stimulate spending**. During the month, the construction sector added 28 thousand jobs to non-factory payrolls, representing nearly 20% of the jobs created during the month.

The Year Ahead

The Economy: **Economic growth will be adversely affected by the ongoing government spending negotiations and the likely spending sequester** (automatic spending cuts of $110 billion in 2013) if agreement is not reached. However, we believe Congress will fail to reach agreement and the sequester will occur, but have a modest impact. We further believe that its impact will be offset later in the year by improved aggregate demand; an improvement supported by reduced uncertainty and greater confidence arising from the automatic, non-political structure of the cuts and the ongoing impact of record-low interest rates. Growth will arise from improved industrial output, robust consumer spending and an improving trade balance driven by a sharply-reduced need for oil and energy imports.

GDP Growth: 2012 - 2.8%, 2013 LDA Prediction - 3.3%

Interest Rates: The global explosion in liquidity will continue to **keep interest rates low across the yield curve and compressed along the ratings spectrum**. We envision limited changes in the Fed's accommodative policy that has pushed the Fed funds rate to near-zero, helped cap the LIBOR one, three and six month rates below 50 bps and moved 10-year Treasuries to a rate that approximates the underlying inflation rate. Toward year end, we believe the Fed will begin unwinding some of the stimulus programs by either reducing purchases or not reinvesting proceeds from principal payments received.

Fed funds: 2012 - 0 to 25 bps, 2013 LDA Prediction - 25 to 50 bps

10-year Treasury: 2012 - 2.05%, 2013 LDA Prediction - 3.00%

Employment: **Unemployment will remain an intractable problem despite the ebullient outlook we are presenting**. While we project an improving growth profile for the economy, we believe the rate of absorption will continue to be low. Industrial capacity utilization ended the year up marginally at 0.5%, effectively absorbing a 1.6% capacity increase. With total payroll increases of 2.2 million, the absorption rate appears to be approximately 1 million people for a 1% increase in production utilization. However, the civilian workforce grew from 242.3 million to 244.7 million, or 200 thousand per month on average. With a participation rate of 63.6% (unchanged during the year), the economy needs to generate 127.2 thousand net new jobs per month just to maintain the current level of unemployment. Our expected growth rate of 3.3% should translate into increased payrolls of slightly more than 2.6 million. With an absorption of new workers of 1.5 million, the remaining 1.1 million would represent a decline of 0.7% in the unemployment rate.

Unemployment rate: 2012 - 7.9%, 2013 LDA Prediction - 7.2%

Inflation: It is irrefutable that the Fed's implementation of QE3 and the uncoordinated activities of the key central banks will ultimately result in inflation. However, competitive currency devaluations, whether overt, as in the case of the Bank of Japan, or covert, as in the case of Banco Central do Brasil, will act as a near-term governor on inflationary pressures. **As USD-denominated import prices decline, imports become less expensive and act to inhibit price increases on domestic production**. Furthermore, given a high level of unemployment, **wage pressures will remain benign for the foreseeable future**. Lastly, **continued excess capacity will limit the impact of allocating scarce capacity on prices; as capacity utilization rises, low interest rates and high liquidity should expedite capacity increases to keep inflation in check**. The result will be an inflation rate at or near the Fed's targeted rate of 2.0% during 2013.

Inflation Rate (CPI): 2012 - 1.7%, 2013 LDA Prediction - 2.2%

Conclusion

With interest rates at the lowest levels in a half-century and a strong stable economic environment, we are en-

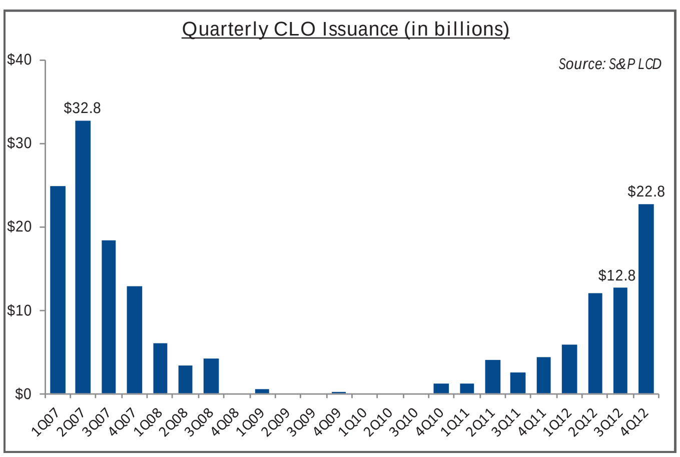
couraging the aggressive use of debt to acquire operating and financial assets. We are advising our clients that the **next decade will be a golden era for leveraged equity investments**. The economy will stimulate growth amongst most participants, with cheap capital providing an incremental push to above average growth through internal development, capacity expansion and acquisitions. **Longer term, we see worldwide inflation resulting from global monetary expansion affecting commodities, services and investment assets**. As heightened liquidity promotes higher asset values, the opportunity to sell assets purchased during the next two to three years at appreciated values improves while the real value of fixed rate liabilities declines, providing an ever-increasing margin of gain on investments. **The result will be fortunes made tomorrow for the adventurous today**.

The U.S. Credit Markets

Market Bifurcation

There has certainly been no shortage of news touting the recent strength of the credit markets and with good reason. Treasury yields are hovering near all-time lows, and large leveraged companies have been able to borrow at rates typically reserved for BBB or better credits, but what about the middle-market? Companies large and small have benefited from record amounts of liquidity arising from the Fed's easy-money policies of the past 4 years; however, as illustrated by the middle-market premium, defined as the delta between the average middle-market institutional spread and that of large cap loans, large-caps are reaping much greater rewards. **For the week ending February 14th, the middle- market premium reached an all-time high of 173 bps (L+554 vs. L+382).** For context, during the last red-hot debt market, **2007, the premium borne by mid-market credits was 39 bps (301 bps vs. 262 bps).**

The disparity, in large part, stems from the underlying sources of much of the liquidity- CLOs and loan mutual funds. According to S&P, CLO issuance over the past 6 months has totaled $42.83 billion, including a shade over $12.2 billion year-to-date.



Similarly, loan mutual funds have seen nearly $10 billion of in-flows over the past 6 months as investors have shifted capital away from high-yield funds and their attendant fixed interest rates. Such vehicles are generally governed by investment guidelines which preclude them from investing in non-syndicated loans (i.e. the vast majority of middle-market issuance), due to their illiquidity.

With so much capital sloshing around the large-cap market, a technical imbalance favoring borrowers has resulted in spread compression for new-issues and repricings, alike. Concerning the latter, where a large cap can achieve significant interest savings through a modest repricing due to the size of the facility, the same exercise may not be worth the effort for a smaller loan.

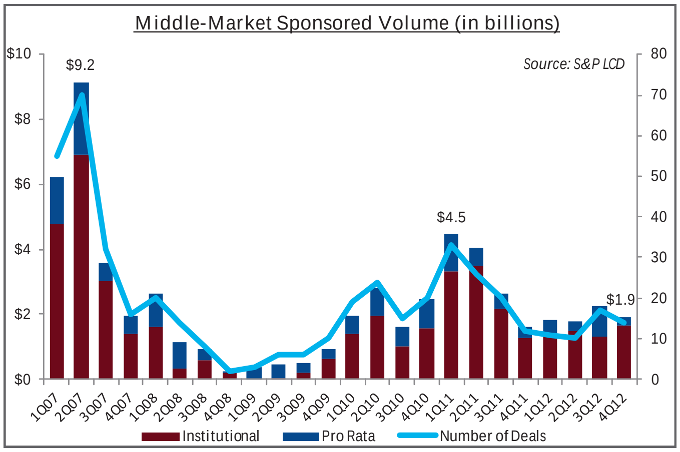
Despite this premium, given current 3-month LIBOR of 0.3%, borrowing costs for all issuers are at historically-low levels. Assuming the prevailing market LIBOR floor of 1.25%, and ignoring any original issue discount (OID), **the current average yield on middle-market institutional loans is 6.79%. For comparison, in February 2007, middle-market spreads reached a jaw-dropping low of 301 bps. However, and here's the kicker, LIBOR stood at 5.35%, producing a comparable yield of 8.36%.** The key takeaway? With rates this low, it is unlikely we will see any meaningful further decline and therefore, we're advising clients to execute today on any financing needs foreseeable within the next year.

Looking Ahead

As spring approaches (earlier than usual according to the Prognosticator of Prognosticators aka, Punxsutawney Phil) we've taken a close look at the recent market trends to provide our clients with a window into what can be expected in the year to come.

Volume: As the CLO and mutual fund engines continue to purr, we expect 2013 volume to be robust. Through the first 6 weeks of 2013, new-issue volume topped $110 billion, representing a 150% increase from the same period in 2012. Underpinning volume expectations thus far have been the announcements of several high-profile buyouts including Heinz and Dell. However, as noted previously, we expect LBOs across the market to pick up considerably in 2013 as record low borrowing costs afford and even encourage, aggressive asset valuations.

That should be welcomed news for loan market participants who have been transacting in a dismal M&A environment for the last year and a half. As the following chart details, middle-market sponsored loan volume has been hovering right around $2 billion per quarter for the past year.



Pricing & Structure: Investors' recent acceptance of more aggressive structures is likely to continue absent any meaningful macro shocks to the system. Harkening back to the halcyon days of 2007, covenant-lite loans have returned to represent a meaningful portion of new-issuance despite some moderate resistance from the buy-side over the last few weeks. Further, we expect to see leverage levels continue their ascent throughout the year as investors are forced to acquiesce to higher levels in order to put capital work. Through the first 2 weeks of February, average debt to EBITDA for new-issues stood at 4.5x, up a half turn from February 2012.

All told, we believe the tailwinds of an improving economic picture and pent-up demand amongst debt investors will contribute to a robust 2013 and look forward to helping our clients take advantage of this highly-unique investing environment.

About Us

Advisory Services: Lampert Debt Advisors is dedicated to meeting the funding and growth needs of companies by advising on the creation, placement and execution of debt financing solutions. Our team of debt capital markets experts possesses an average of 20 years of experience in completing transactions. With real time knowledge of the investing interests of over 400 lenders and debt investors and our Debt Financing Auction Platform, we are positioned to ensure clients of the best possible execution under prevailing market circumstances. Completed transactions are cost-effective, time-efficient and enable management to focus on their business success. Lampert Debt Advisors executes transactions through Lampert Capital Markets, Inc., a FINRA-registered broker dealer.

Restructuring Advisory: In addition, LDA works with companies that are experiencing distress and in need of professional guidance to restructure existing indebtedness. After performing a thorough analysis and preparing a customized, strategic proposal, LDA works closely with clients to negotiate loan modifications and mediate the sometimes strained relationships with their lenders.

We aim to address lender angst and introduce new capital through the use of our financing process, thereby positioning the company to move forward as a stronger, healthier organization.

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