

# Phoenix Management Services' "Lending Climate in America" Survey

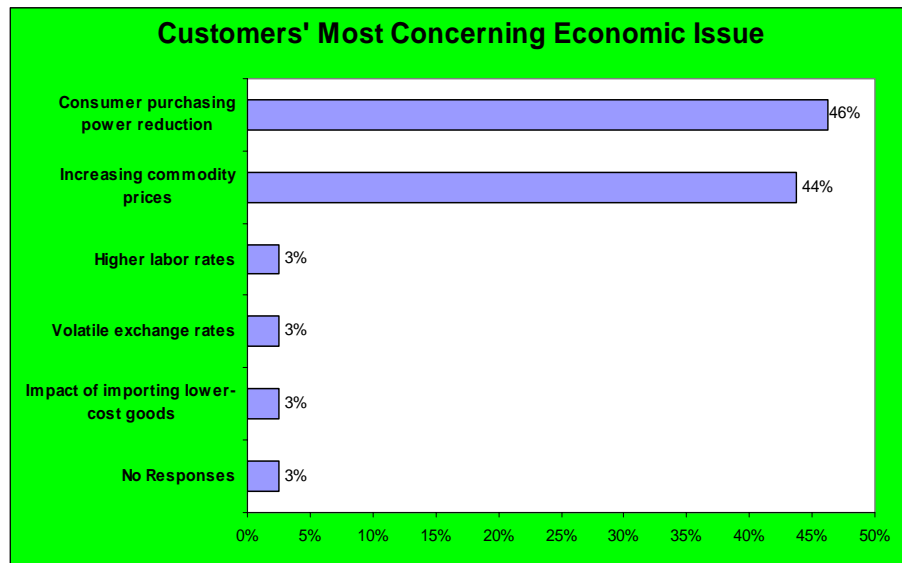


**3rd Quarter 2008  
Summary, Trends and Implications**

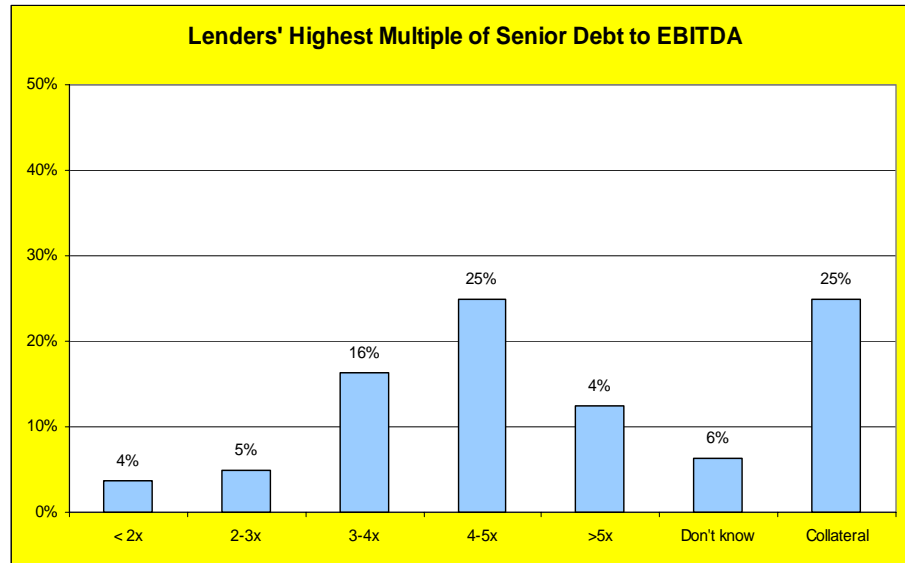
**PHOENIX  
“LENDING CLIMATE IN AMERICA”  
QUARTERLY SURVEY**

**3rd Quarter 2008**

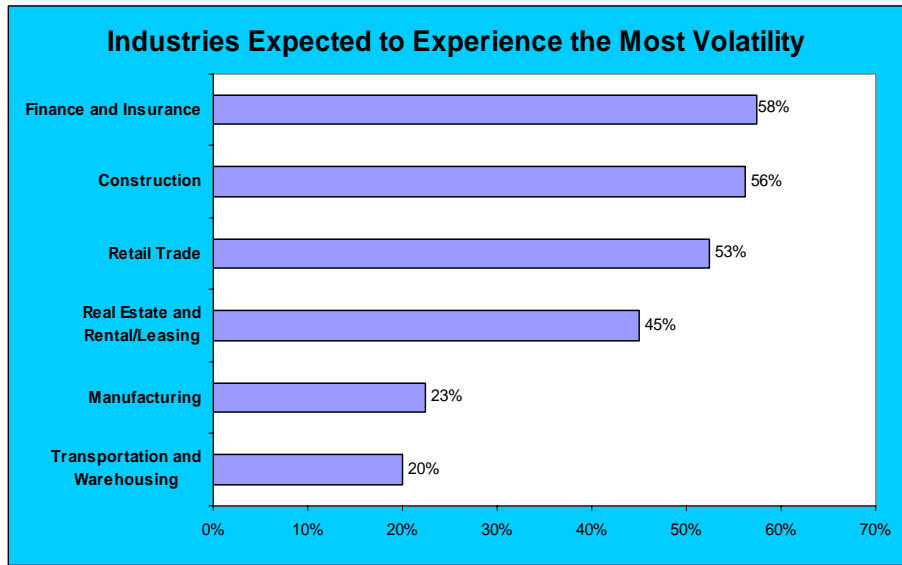
- 1. Fifty-one percent of lenders believe inflation levels will trend equivalent to current levels over the next six months.** Thirty percent of respondents opined that inflation will trend higher over the next six months. The remaining nineteen percent of respondents believe inflation will trend lower (or had no response) over the next six months.
- 2. Nearly half - 46 percent – of respondents designated the reduction in consumer purchasing power due to the decline in disposable income as the economic issue borrowers/customers are most concerned with in the near term.** Forty-four percent indicated increasing commodity prices as the most concerning economic issue. Three percent of lenders indicated the following issues/responses: higher labor rates, volatile exchange rates, impact of importing lower-cost goods, and no response to this question.



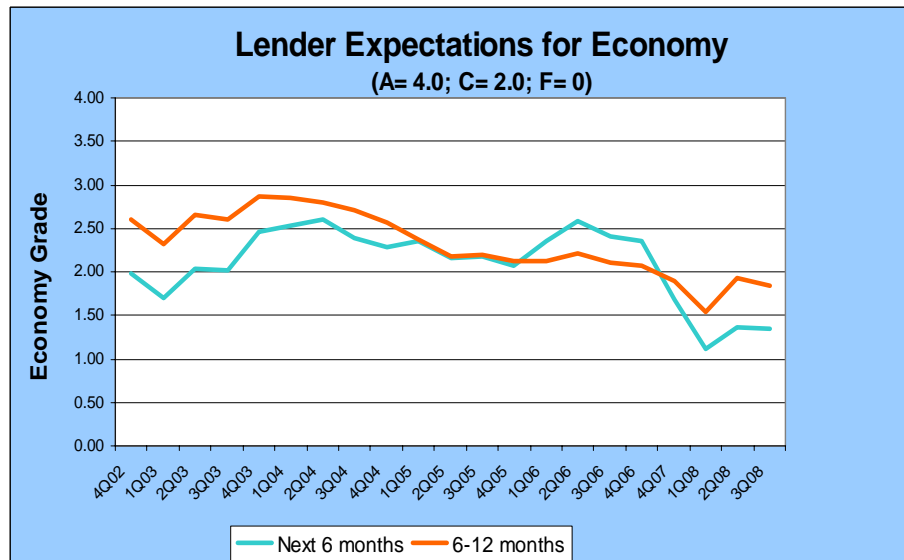
- 3. Twenty-five percent of lenders indicated their financial institution would consider a loan request with a Senior Debt to EBITDA multiple as high as 4-5x.** Nine percent of respondents indicated their institution would only consider a loan request with a multiple of less than 3x, while another sixteen percent of lenders opined they would consider a loan request with a multiple as high as 3-4x. Four percent of respondents indicated they would consider a loan request with a Senior Debt to EBITDA multiple greater than 5x. Twenty-five percent of respondents indicated they are collateral lenders and do not utilize cash flow multiples as the primary factor in credit decisions.



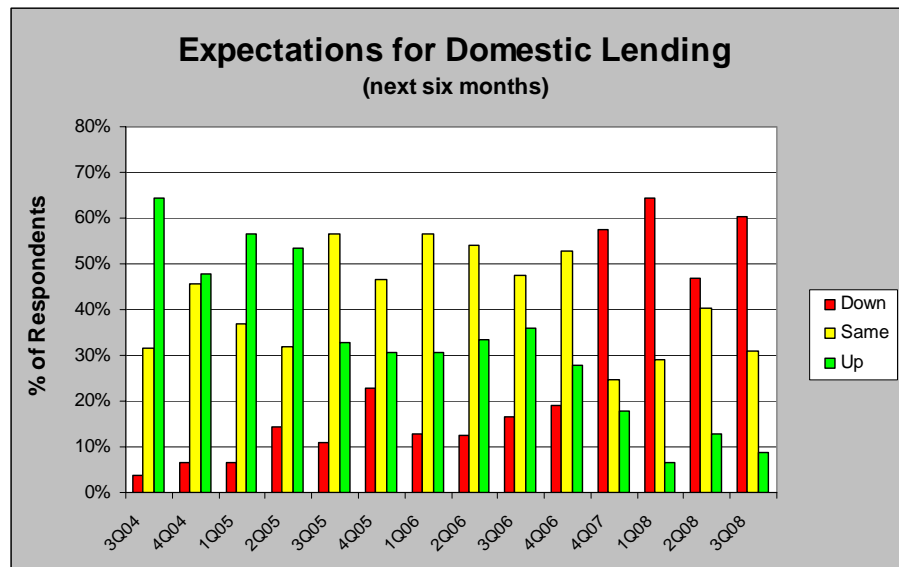
4. **Twenty-eight percent of lenders believe their institution will have no change in the highest Senior Debt to EBITDA multiple it will consider in regards to a new loan request.** Eighteen percent of respondents believe internally that multiple will decrease less than 0.5x, while another eight percent believe that multiple will decrease by more than 0.5x. Six percent of lenders opined that the multiple would increase at their financial institution over the next six months. Twenty-three percent of respondents indicated they were collateral lenders and did not specifically focus on that multiple.
  
5. **Seventy-five percent of lenders designated constrained liquidity in the capital markets as the factor with the strongest potential to impact the near-term economy.** The sluggish housing market was chosen by 58 percent of respondents as having significant potential to have near-term economic impact. Thirty percent of lenders chose the unstable energy prices, while fourteen percent designated the outcome of the upcoming presidential election. Finally, four percent chose the U.S. budget deficit and one percent chose the Iraqi war as having strong potential to impact the near-term economy.
  
6. **Fifty-eight percent of respondents anticipate the Finance and Insurance industry will experience the most volatility in the next six months.** When asked to identify three industries that will experience the most volatility in the next six months, while 58 percent of lenders designated the finance and insurance industry, fifty-six percent choose the Construction industry as the most likely to experience volatility and fifty-three percent of lenders chose the Retail Trade industry. Forty-five percent of lenders believe the Real Estate and Rental/Leasing industries will experience the most volatility. Twenty-three percent of lenders believe the Manufacturing industry will experience the most volatility. The last industry to register a meaningful percentage – Transportation and Warehousing – was selected by twenty percent of respondents.



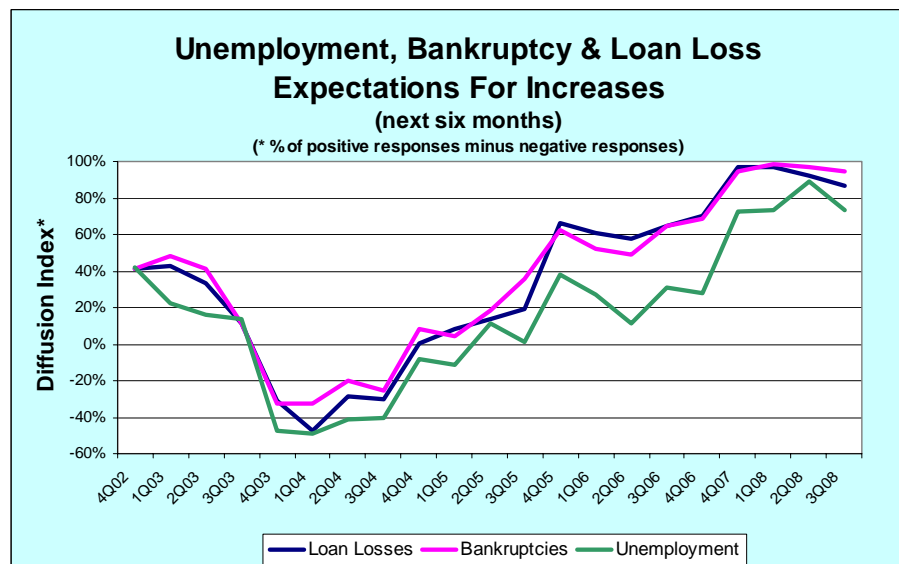
7. **Forty-three percent of respondents' customers anticipate introducing new products or services in the next six months.** Forty-one percent of customers plan on raising capital in the next two quarters. Twenty-five percent each of lenders' customers anticipate making an acquisition and entering new markets in the next six months. Twenty-one of customers plan on making new capital investments, while fourteen percent intend on hiring new employees.
  
8. **Lenders expectations for the economy deteriorated slightly from the previous quarter.** Lenders expect the economy to perform at a high "D" level during the next six months. The respondents' expectations for longer-term improvement remained better than the near-term outlook with a "C" expectation level.

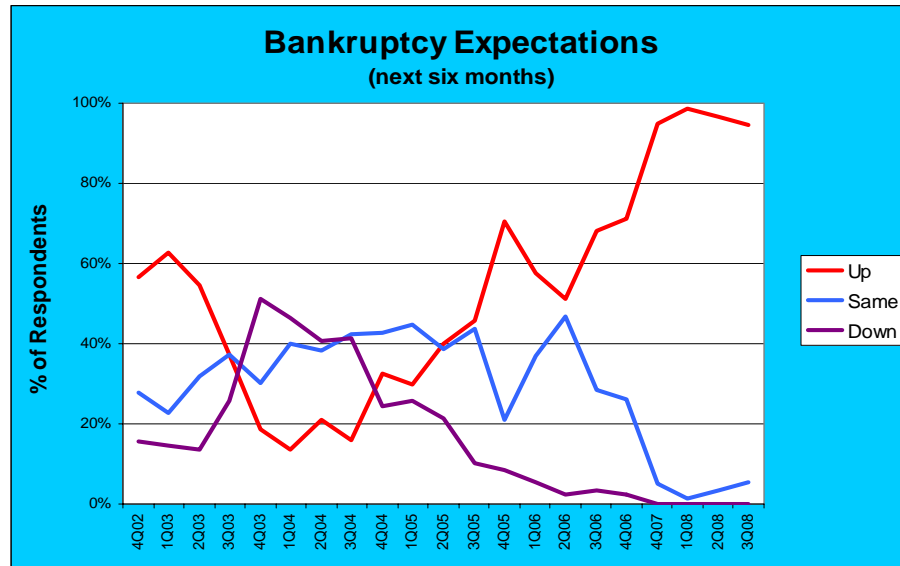


9. The percentage of respondents with their customer having no growth expectations over the next 6 - 12 months rose significantly from the previous quarter to fifty percent – the highest level recorded in this survey in the last eight years. Forty-nine percent of lenders opined their customers had moderate growth expectations, down from 66 percent in the previous quarter.
10. The loan demand diffusion index (the percentage of respondents forecasting a higher percentage less those anticipating a lower percentage) reversed a short-lived positive trend as respondents were more pessimistic across all lending segments in this survey. The overall diffusion index for all lending segments deteriorated to negative 46 percentage points (from negative twenty-eight percentage points in the previous survey). Respondents indicated that, on average for all domestic lending categories, nine percent have expectations for increased loan demand (versus 13 percent in the prior quarter).

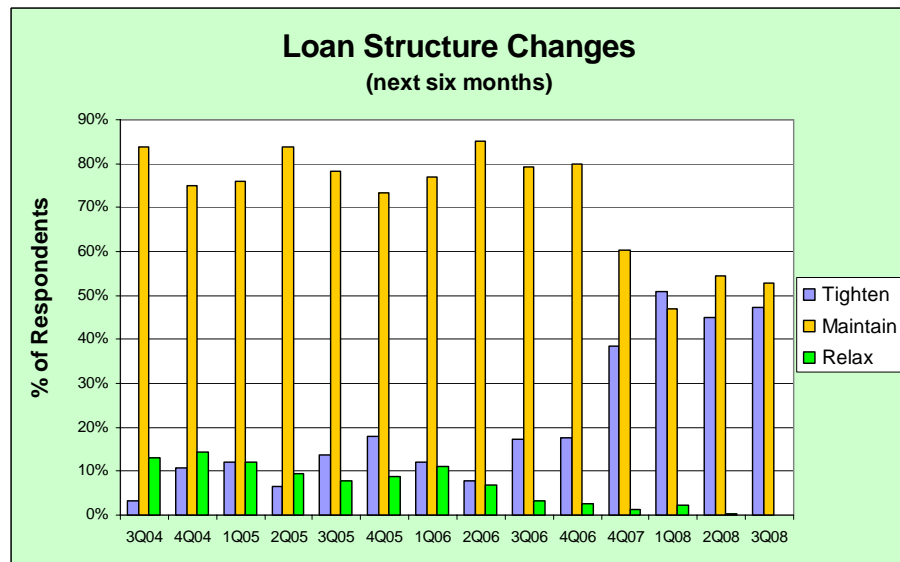


11. Lenders remained consistent with expectations of deteriorating credit quality equivalent with recent surveys. The loan loss diffusion index was at 86 percent, slightly down from the previous quarter, while ninety-five percent of lenders anticipate higher bankruptcies. The percentage of respondents anticipating higher unemployment fell to 74 percent – down from 89 percent in the previous quarter.

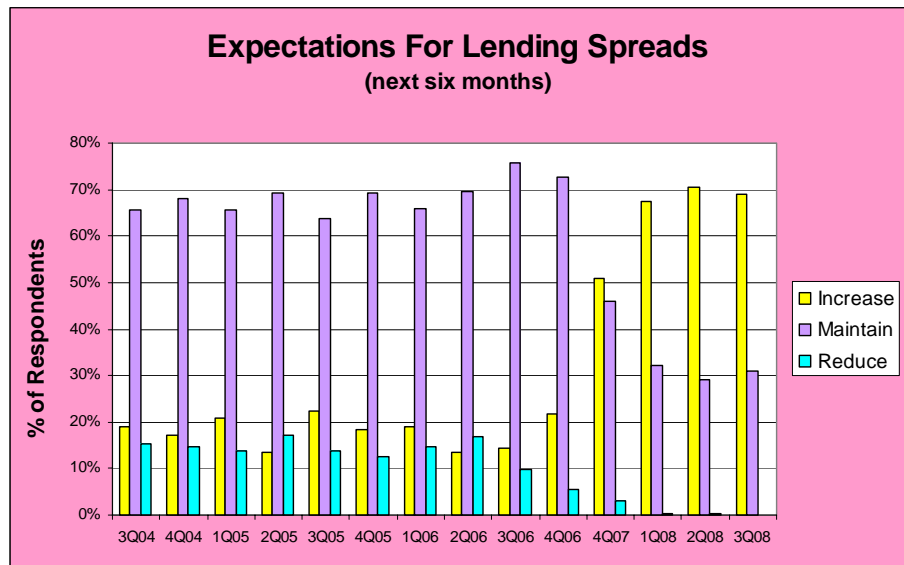




- 12. The percentage of lenders anticipate interest rates will increase over the next six months decline to 45 percent (versus sixty percent in the previous survey).** Thirty-two percent of lenders believe rates will remain unchanged, while the remaining Twenty-three percent of respondents believes that interest rates will decrease over the next six months.
- 13. The percentage of lenders expecting to tighten their existing loan structures remained steady at forty-seven percent (versus forty-five percent in the previous survey).** As a result, the percentage of respondents planning to maintain their loan structure was relatively flat at fifty-three percent.



**14. A steady percentage of lenders anticipate increasing their current lending spreads in this interest rate environment.** Sixty-nine percent of respondents (versus 70 percent in the previous quarter) expect to increase lending spreads from their current levels.



**Phoenix Management**  
**“Lending Climate in America”**  
**3rd Quarter 2008**

**Survey Results**

**1. Anticipation of Near-Term Inflation Trends**

Lenders were asked, over the next six months, how did they anticipate that overall levels of inflation would trend.

- Approximately half of respondents— fifty-one percent – believe that overall levels of inflation will be equal to current levels.
- Thirty percent of respondents opined that the near-term overall levels of inflation will be higher than current levels.
- Eighteen percent of lenders responded that inflation in the next months will be lower than current levels.
- The remaining one percent of lenders did not give a response to this question.

**2. Economic Issue that Borrowers/Customers are Most Concerned With**

Respondents were asked which economic issue that their borrowers/customers are MOST concerned with in the near term.

- Forty-six percent of respondents replied their borrowers/customers are most concerned with their reduction in consumer purchasing power due to the decline in disposable income.
- Forty-four percent indicated the biggest concern was increasing commodity prices.
- Three percent of respondents gave the following responses: higher labor rates, volatile exchange rates, and the impact of importing lower-cost goods.

**3. Highest Senior Debt to EBITDA Multiple Institutions Would Consider**

Respondents were asked what was the highest multiple of Senior Debt to EBITDA their financial institution would consider with regard to a loan request.

- Twenty-five percent indicated their institution would consider a loan request with a leverage multiple as high as the 3.0x – 3.5x range.
- Twenty-five percent of respondents replied they are collateral lenders and, therefore, do not make credit decisions based on cash flow/leverage multiples.
- Sixteen percent believed their institution would consider a loan request with a Senior Debt to EBITDA multiple as high as the 2.5x – 3.0x range.
- Thirteen percent of lenders opined their financial institution would consider a loan request with a leverage multiple of greater than 3.5x.

- Six percent indicated they did not know what the highest leverage multiple was that their institution would consider in regards to a loan request.
- Five percent of lenders indicated their financial institution would consider a loan request with a leverage multiple as high as 2.0x – 2.5x.
- Four percent of lenders responded their financial institution would only consider a loan request with a leverage multiple lower than 2.0x.
- The remaining six percent of lenders did not give a response to this question.

#### **4. Anticipated Change in Senior Debt to EBITDA Multiple**

Respondents were asked, over the next six months, how the Senior Debt to EBITDA multiple would change at their financial institution.

- Twenty-eight percent indicated that the Senior Debt to EBITDA multiple will not change at their financial institution over the next six months.
- Twenty-three percent of respondents replied they are collateral lenders and, therefore, do not make credit decisions based on cash flow/leverage multiples.
- Eighteen percent believed the leverage multiple will decrease less than 0.5x during the next six months.
- Thirteen percent of lenders stated they did not know if the leverage multiple would change at their institution over the next six months.
- Eight percent believed the Senior Debt to EBITDA multiple will decrease more than 0.5x during the next six months.
- Six percent opined the Senior Debt to EBITDA multiple will increase during the next six months.
- The remaining six percent of lenders did not give a response to this question.

#### **5. Factors with Strongest Potential to Affect Near-Term Economy**

Respondents were asked, over the next six months, which TWO factors had the strongest potential to affect the economy.

- Seventy-five percent designated constrained liquidity in the capital markets as the factor with the strongest potential to affect the near-term economy (an increase of nineteen percentage points from the previous survey).
- Fifty-eight percent designated the sluggish housing markets as the factor with the strongest potential to affect the near-term economy.
- Thirty percent of respondents replied unstable energy prices have the strongest potential to affect the economy over the next six months.

- Fourteen percent opined that the outcome of the upcoming presidential election had the strongest potential to affect the economy during the next six months.
- Four percent chose the U.S. budget deficit as the factor with the strongest potential to affect the economy in the next six months.
- Seven percent believed that other factors (than the five factors specifically mentioned) have the greatest potential to affect the economy in the next six months.

## **6. Industries Expected to Experience Greatest Volatility**

Respondents were asked, over the next six months, which industries will experience the most volatility (i.e. Chapter 11 filings, mergers and acquisitions, declining profits, etc.).

Respondents were asked to select the top three industries.

- Fifty-eight percent of respondents believed the finance and insurance industry will experience the greatest volatility over the next six months.
- Fifty-six percent designated the construction industry as the industry expected to weather the greatest volatility in the near term.
- Fifty-three percent believed the retail trade industry would experience the most volatility.
- Forty-five percent responded that the real estate and rental/leasing industry would experience the most volatility during the next six months.
- Twenty-three percent opined the manufacturing industry would experience the most volatility.
- Twenty percent designated the transportation and warehousing industry as the anticipated most volatile industry over the next six months.
- Ten percent believed the accommodation and food service industry as the anticipated most volatile industry over the next six months.
- The balance of the industry choices did not register designations greater than five percent from the respondents.

## **7. Customers' Plans in the Next Six to Twelve Months**

Respondents were asked which of the following actions their customers planned in the next six to twelve months. Lenders were asked to designate all potential customer actions that applied.

- Forty-three percent responded their customers intend to introduce new products or services in the next 6-12 months.
- Forty-one percent indicated their customers are planning on raising additional capital in the next six to twelve months.
- Thirty-five percent indicated their customers are planning on entering new markets and making an acquisition.
- Twenty-one percent responded their customers plan on making new capital investments in the next 6-12 months.
- Fourteen percent of respondents indicated their customers plan on hiring new employees in the next 6-12 months.
- Thirteen percent responded their customers plan on engaging in "other" business actions in the next 6-12 months.

## **8. Economic Indicators**

Respondents were asked whether they expected the following economic indicators to be up, down, or remain the same over the next six months.

- The percentage of lenders anticipating "Down" economic indicators increased across all lending segments versus the previous survey. As a result, the diffusion index for all lending segments declined to negative 46 percentage points - an 18 percentage point deterioration from the previous quarter and the lowest metric in four years.
- Lenders maintained their negative credit quality outlook, as an overwhelming majority of respondents believe that loan losses and bankruptcies will increase. The percentage of respondents forecasting an increase in interest rates (down 25 percentage points) significantly decreased this period.

	2Q/2008			3Q/2008		
	<u>Up</u>	<u>Down</u>	<u>Same</u>	<u>Up</u>	<u>Down</u>	<u>Same</u>
Corporate Lending	8%	50%	42%	8%	62%	30%
Middle Market Lending	18%	44%	38%	10%	55%	35%
Small Business Lending	13%	47%	40%	8%	64%	28%
International Lending	21%	31%	48%	11%	42%	47%
	<u>Up</u>	<u>Down</u>	<u>Same</u>	<u>Up</u>	<u>Down</u>	<u>Same</u>
Loan Losses	92%	0%	8%	88%	1%	11%
Bankruptcies	97%	0%	3%	95%	0%	5%
Interest Rates	65%	3%	32%	40%	7%	53%
Unemployment	89%	0%	11%	75%	1%	24%
Bank Failures	77%	0%	23%	81%	3%	16%

## 9. U.S. Economy Grade – Second Half of 2008

Respondents were asked how they expected the U.S. economy to perform during the second half of 2008 (next six months) on a grading scale of A through F.

- Respondents' outlook for the economy's near-term performance maintained its high "D" grade level for the second half of 2008. The percentage of lenders who believe that the economy will perform at a "D" level increased to 60 percent from 55 percent in the prior quarter.

	2Q/2008	3Q/2008
A	0%	0%
B	0%	0%
C	40%	37%
D	55%	60%
F	5%	3%
Weighted Average Grade	1.35	1.34

## 10. U.S. Economy Grade – First Half of 2009

Respondents were asked how they expected the U.S. economy to perform during the first half of 2009 ("out" six months) on a grading scale of A through F.

- Lenders' expectations for the "out six-month" period were higher than expectations for the next six months for the fourth consecutive quarter – in contrast to the previous four surveys where the longer-term outlook was more negative than the near-term outlook. Respondents anticipating the economy to perform at a "D" level or lower during the first half of 2009 increased to 22 percent (increasing from 18 percent in the previous survey).

	2Q/2008	3Q/2008
A	0%	0%
B	13%	8%
C	69%	70%
D	16%	21%
F	2%	1%
Weighted Average	1.94	1.85

## 11. Customers' Future Growth Expectations

Lenders assessed their customers' growth expectations for the next six months to a year.

- One out of two respondents indicated their customers have no growth expectations for the next six months to one year – the highest level for this designation in the last eight years of lending surveys.

	2Q/2008	3Q/2008
Very Strong	0%	0%
Strong	2%	1%
Moderate	66%	49%
No Growth	32%	50%

## 12. Loan Structure

Respondents were asked whether their financial institutions planned to tighten, relax, or maintain their loan structures (collateral requirements, guarantees, advance rates, loan covenants, etc.) in each of four different-sized loan categories.

- Respondents indicating their financial institutions would tighten their loan structures increased all loan sizes. The overall average of financial institutions planning to tighten their loan structures rose from 45% in the prior quarter survey to 47%.

	2Q/2008			3Q/2008		
	<u>Tighten</u>	<u>Maintain</u>	<u>Relax</u>	<u>Tighten</u>	<u>Maintain</u>	<u>Relax</u>
Loans > \$25 million	52%	48%	0%	53%	47%	0%
\$15 – 25 million	48%	52%	0%	51%	49%	0%
\$5-15 million	40%	60%	0%	42%	58%	0%
Under \$5 million	41%	58%	1%	43%	57%	0%
Overall Average	45%	54%	1%	47%	53%	0%

### 13. Interest Rate Spread

Lenders were asked whether their financial institutions planned to reduce, maintain or increase their interest rate spreads and fee structures on similar credit quality loans.

- Sixty-nine percent of respondents plan to increase their current interest rate spreads and fee structures on all sizes of loans – a historically high percentage of respondents and in line with recent surveys.

	2Q/2008			3Q/2008		
	Reduce	Maintain	Increase	Reduce	Maintain	Increase
Loans > \$25 million	0%	38%	62%	0%	31%	69%
\$15 – 25 million	0%	30%	70%	0%	32%	68%
\$5-15 million	0%	22%	78%	0%	31%	69%
Under \$5 million	2%	25%	73%	0%	29%	71%
Overall Average	1%	29%	70%	0%	31%	69%

### 14. The Fed and Interest Rates

Respondents were asked in what direction the Fed would move interest rates and by how much in the coming six months.

- Respondents forecasted an increasing interest rate environment – albeit not as robust a forecast increase as last quarter. The percentage of lenders anticipating a 25 bps or more increase in interest rates fell to forty-five percent (versus sixty percent in the prior quarter survey).

	2Q/2008	3Q/2008
-More than 1.0	0%	0%
-1.0	0%	1%
-.75	0%	1%
-.50	7%	7%
-.25	3%	13%
0	28%	32%
+.25	25%	21%
+.50	30%	17%
+.75	3%	0%
+1.0	2%	6%
More than 1.0	0%	1%
Weighted Average	+ 20 basis points	+ 12 basis points

## 15. Current Competition

Respondents were asked to identify the segment of the industry from which they were experiencing the most competition.

- The percentage of lenders identifying regional banks as the primary source of competition increased to forty-three percent this survey – as compared to forty percent last quarter. Similarly, respondents designating commercial finance organizations as the primary source of competition increased to twenty-six percent versus 20 percent in the previous survey.

	2Q/2008	3Q/2008
Money Center Banks	10%	9%
Local Commercial/ Community Banks	13%	10%
Factors	8%	6%
Regional Banks	40%	43%
Commercial Finance Organizations	20%	26%
Other	8%	6%