

Phoenix Management Services “Lending Climate in America” Survey



**3rd Quarter 2017
Summary, Trends and Implications**

PHOENIX
"LENDING CLIMATE IN AMERICA"

3rd Quarter 2017

SUMMARY, TRENDS AND IMPLICATIONS

- 1. The Gulf Coast is home to half of the United States' petroleum refineries. Due to the major shutdowns experienced during hurricanes Harvey and Irma, during what time period do you believe we will see the biggest effect on domestic gasoline prices?**

The majority of lenders (66%) believe that we will immediately see the biggest effect on domestic gasoline prices due to major shutdowns during hurricane Harvey and Irma. Garnering the second highest amount of responses of 17% each were the lenders that believe we will see the biggest effect on gasoline prices in a) 3Q 2017, and b) 4Q 2017. 0% of lenders believe that we will see the biggest effect on gasoline prices in 1Q 2018 due to the major shutdowns from hurricane Harvey and Irma.

- 2. In September 2017, President Trump expressed his continued interest in getting rid of the United States' debt ceiling. If the debt ceiling is eliminated, which of the following consequences do you think would affect Americans the most?**

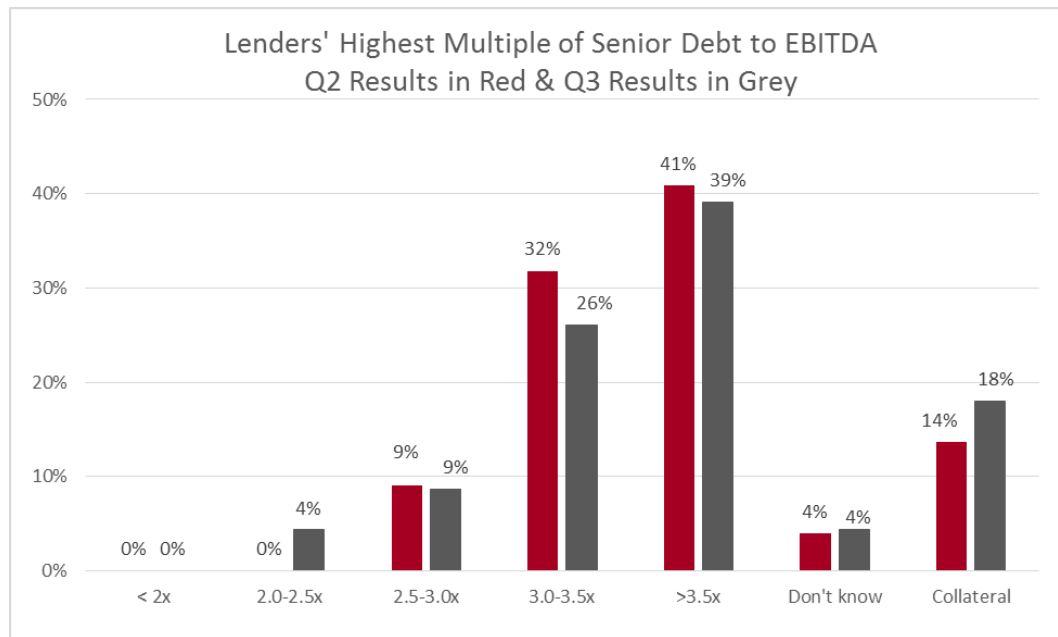
The answer that received the highest percentage response, 65%, were the lenders that believe higher interest rates will be the greatest consequence for Americans if the debt ceiling is eliminated. Lenders that believe elimination of the debt ceiling will result in stock market uncertainty, garnered 30% of the responses, while 5% of lenders believe that a reduction in Government services will be the greatest consequence for Americans if the debt ceiling is eliminated. Of the lenders surveyed, 0% of lenders believe global trade upheaval will be the greatest consequence.

- 3. President Trump has promised to cut taxes and increase infrastructure spending in the near term. What do you think is likely to be the outcome of those initiatives?**

The majority of lenders, garnering 52% of responses, think that there will be a positive outcome – additional spending, financed cheaply given the current interest rate environment - if President Trump were to cut taxes and increase infrastructure spending in the near term. Garnering the second highest amount of responses of 39%, were the lenders that believe there will be no outcome from passing tax reform and materially increasing infrastructure spending. Additionally, 9% of lenders believe that increased spending will balloon the federal debt if President Trump were to cut taxes and increase infrastructure in the near term.

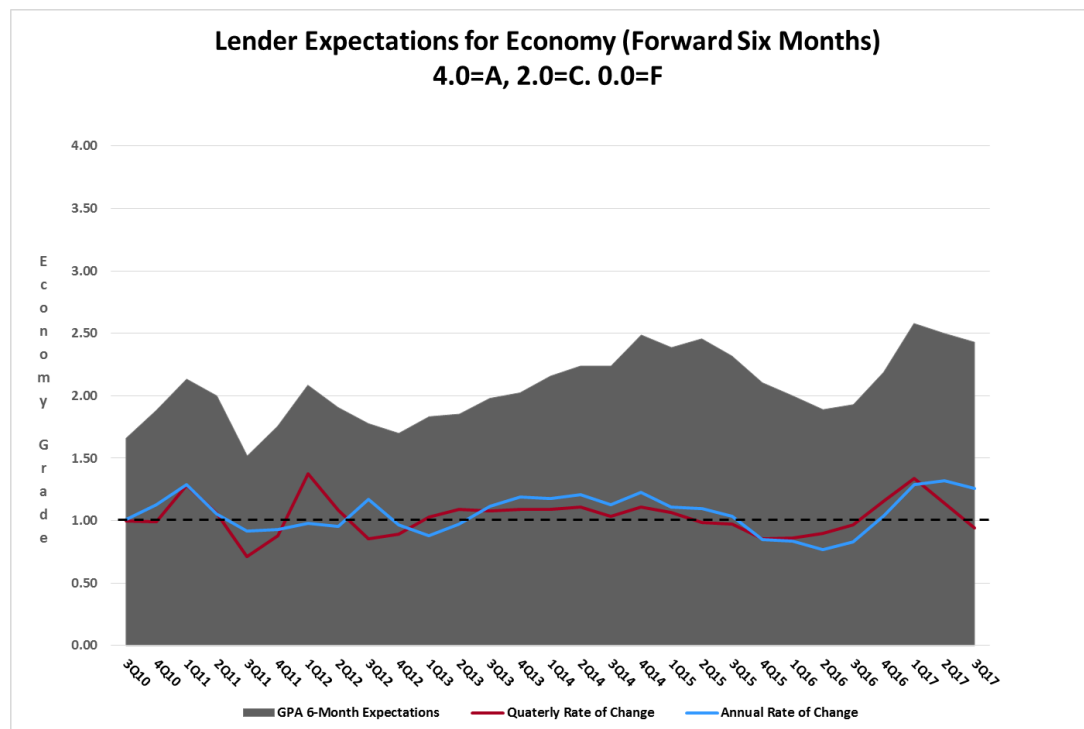
- 4. Leverage multiples shifted this quarter versus the prior quarter.**

Multiples shifted slightly downward in 3Q 2017. 39% of lenders indicated the >3.5x range would be the highest EBITDA ratio they would consider, a 2 percentage point decrease from the prior quarter. The percentage of respondents who would consider a debt to EBITDA ratio of 3.0-3.5x decreased 6 percentage points to 26%. The percentage of lenders who indicated the highest ratio they would consider is between 2.5-3.0x remained unchanged at 9%. 4% percent of respondents stated their institutions highest multiple is in the 2.0-2.5x range, a 2 percentage point increase from the prior quarter's 0%. Zero lenders surveyed continue to indicate less than 2.0x is their institutions highest multiple. In addition, 18% of lenders responded that they were collateral lenders and therefore do not make decisions based on cash flow/leverage multiples.



5. Economic performance expectations decrease for the near term in this quarter's survey.

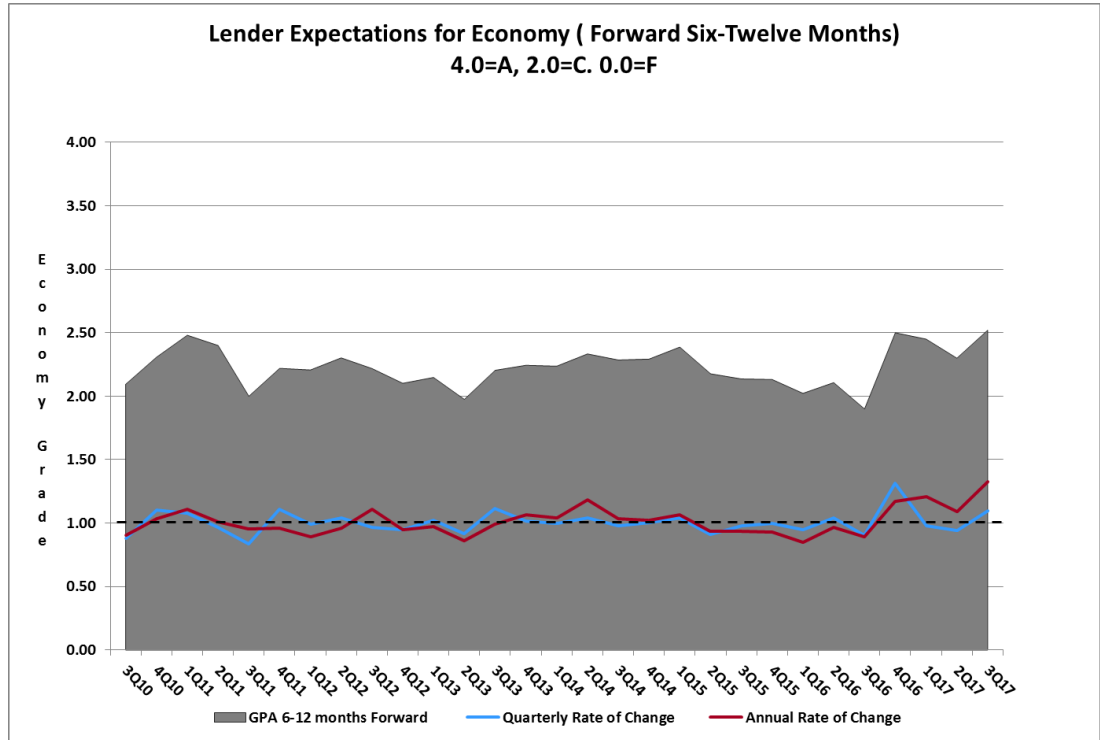
Lenders optimism in the U.S. economy for the short term decreased slightly this quarter and has shifted to a “C” grade; the index GPA decreased to 2.43 from the 2Q 2017 results of 2.50. 48% of the lenders believe the economy will perform at a “B” level over the next six months, compared to 50% in the previous survey. Furthermore, 48% of lenders surveyed believe the economy will perform at a “C” grade, compared to 50% in the previous survey. 4% of Lenders that believe that the economy will perform at a “D” level.



* Rate of Change of 1.0 is at equilibrium and signifies “no change” from the corresponding prior period of comparison.

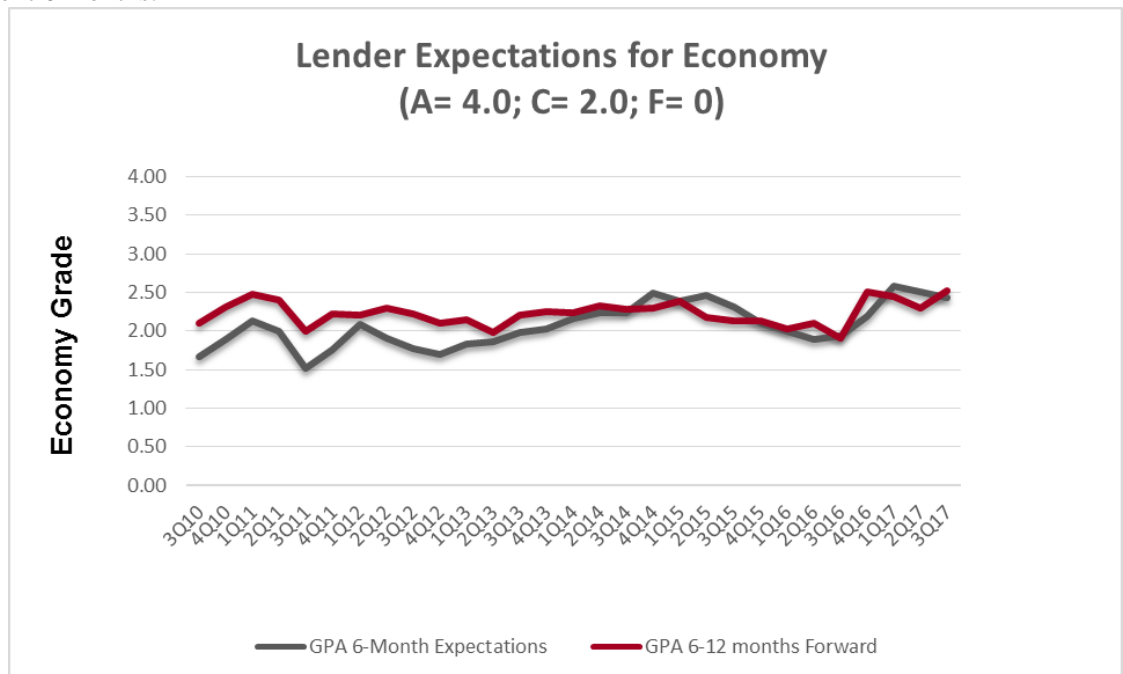
Lenders growth expectations for the U.S. economy beyond six months increased to a higher “B” grade this quarter. The weighted average increased 22 points to a 2.52 GPA from 2.30 in the

previous quarter. 44% of lenders believe the economy will perform at a “B” level in the next six to twelve months, which is 4 percentage points higher than the previous quarter. The percent of lenders (52%) that believe the economy will perform at a “C” level increased 2 percentage points from the previous quarter. The percentage of respondents who believe the economy will perform at a “D” level beyond the next six months declined 10 percentage points to 0%, when compared to the previous quarter. We also saw an increase in the percentage of lenders (4%) that believe that economy will perform at an “A” level, the first time we have received an “A” grade since Q1 2017.



* Rate of Change of 1.0 is at equilibrium and signifies “no change” from the corresponding prior period of comparison.

The 3Q 2017 survey reverses the recent trend of a higher near term GPA than long term GPA. The long term grade of “B” reflects lender’s positive expectations for the economy beyond the next 6 months.



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Survey Results

1. The majority of Lenders believe we will see the biggest effect on domestic gasoline prices immediately after major shutdowns from hurricane Harvey and Irma.

Lenders were asked: The Gulf Coast is home to half of the United States’ petroleum refineries. Due to the major shutdowns experienced during hurricanes Harvey and Irma, during what time period do you believe we will see the biggest effect on domestic gasoline prices?

- 66% of lenders surveyed believe that we will immediately see the biggest effect on domestic gasoline prices after major shutdowns from hurricane Harvey and Irma.
- 17% of lenders believe that we will see the biggest effect on domestic gasoline prices during 3Q 2017.
- 17% of lenders believe that we will see the biggest effect on gasoline prices due to major shutdowns from hurricane Harvey and Irma during 4Q 2017.
- 0% of lenders believe we will see the biggest effect on gasoline prices during 1Q 2017.

2. Lenders believe that higher interest rates will be the consequence to affect Americans the most if President Trump were to eliminate the United States’ debt ceiling

Lenders were asked: In September 2017, President Trump expressed his continued interest in getting rid of the United States’ debt ceiling. If the debt ceiling is eliminated, which of the following consequences do you think would affect Americans the most?

- 65% of lenders believe higher interest rates will be the consequence to affect Americans the most if President Trump were to eliminate the United States’ debt ceiling.
- 30% of lenders think stock market uncertainty would be the consequence to affect Americans the most if the debt ceiling were eliminated.
- 5% of lenders believe that a reduction in Government services will be the greatest consequence if President Trump were to eliminate the debt ceiling.
- 0% of lenders believe global trade upheaval would be the consequence to affect Americans the most if the United States’ debt ceiling was eliminated.

3. Lenders think that a positive outcome of additional spending, financed cheaply given the current interest rate environment will be the result if President Trump cuts taxes and increases infrastructure spending.

Lenders were asked: President Trump has promised to cut taxes and increase infrastructure spending in the near term. What do you think is likely to be the outcome of those initiatives?

- 52% of lenders think positive – additional spending, financed cheaply given the current interest rate environment will be the outcome from President Trump cutting taxes and increasing infrastructure spending.
- 39% of lenders think the outcome would be neutral if President Trump were to cut taxes and increase infrastructure spending.
- 9% of lenders surveyed think negative – tax cuts and increased spending will balloon the federal debt if President Trump were to cut taxes and increase infrastructure spending.

4. Highest Senior Debt to EBITDA Leverage Institutions Would Consider

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

<u>EBITDA Level</u>	<u>2Q 2017</u>	<u>3Q 2017</u>
Greater than 3.5x	41%	39%
Between 3.01x and 3.50x	32%	26%
Between 2.51x and 3.00x	9%	9%
Between 2.01x and 2.50x	0%	4%
Less than 2.0x	0%	0%
Collateral lenders	14%	18%
N/A	4%	4%

5. 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.

<u>Change in Senior Debt to EBITDA Level</u>	<u>2Q 2017</u>	<u>3Q 2017</u>
Increase greater than 0.5x	5%	5%
Increase less than 0.5x	5%	18%
Decrease less than 0.5x	5%	0%
Decrease greater than 0.5x	0%	4%
No change	73%	55%
Collateral lenders	12%	14%
N/A	0%	4%

6. 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.

<u>Factors Affecting Near-Term Economy</u>	<u>2Q 2017</u>	<u>3Q 2017</u>
Unstable Energy Prices	36%	55%
Stability of Stock Market	55%	45%
U.S. Budget Deficit	27%	32%
Sluggish Housing Market	23%	18%
Other	32%	14%
Constrained Liquidity in Capital Markets	5%	9%

7. 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.

<u>Industries Experiencing Most Volatility</u>	<u>2Q 2017</u>	<u>3Q 2017</u>
Retail Trade	86%	91%
Healthcare and Social Assistance	62%	22%
Mining	19%	22%
Real Estate and Rental/Leasing	29%	17%
Manufacturing	5%	13%
Educational Services	5%	13%
Transportation and Warehousing	14%	13%

8. 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.

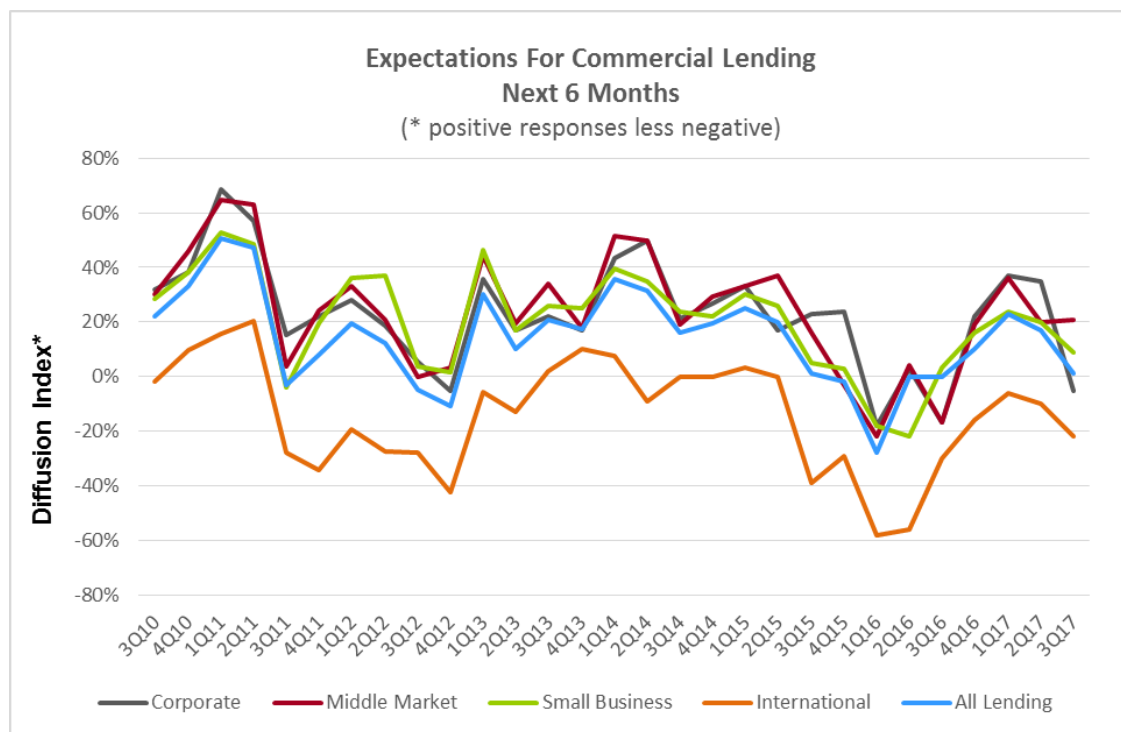
<u>Customers' Plans</u>	<u>2Q 2017</u>	<u>3Q 2017</u>
Capital Improvements	50%	70%
Hiring New Employees	65%	65%
Making an Acquisition	50%	52%
Entering New Markets	40%	48%
Raising Additional Capital	30%	39%
Introducing New Products or Services	50%	30%
"Other" Initiatives	5%	0%

9. 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.

- In 3Q 2017, lenders optimism decreased significantly in large corporate (-5%) and small business (9%). However, expectations increased slightly for middle market in 3Q 2017 with a diffusion index of 21%, a 1 percentage point difference from the previous quarter of 20%. The diffusion index for international lending continued to stay in the negatives, however increasing to a negative 22% from negative 10% in the previous quarter. The diffusion index for the

average for all domestic lending slightly decreased from a 26% in 2Q 17 to 9% in 3Q 17, and the diffusion index for all lending decreased to a 1% from 17% in Q2 2017.



	<u>2Q/2017</u>			<u>3Q/2017</u>		
	<u>Up</u>	<u>Down</u>	<u>Same</u>	<u>Up</u>	<u>Down</u>	<u>Same</u>
Corporate Lending	35%	0%	65%	4%	9%	87%
Middle Market Lending	35%	15%	50%	30%	9%	61%
Small Business Lending	32%	11%	58%	22%	13%	65%
International Lending	5%	15%	80%	5%	27%	68%

- The interest rate diffusion index decreased to 78% compared to 100% the previous quarter. Loan losses diffusion index decreased 41 percentage points to 9% in Q3 2017 compared to 50% in Q2 2017. The bankruptcies diffusion index also decreased this quarter to 22% from 65% in the previous quarter.

	<u>2Q/2017</u>			<u>3Q/2017</u>		
	<u>Up</u>	<u>Down</u>	<u>Same</u>	<u>Up</u>	<u>Down</u>	<u>Same</u>
Loan Losses	55%	5%	40%	26%	17%	57%
Bankruptcies	70%	5%	25%	30%	9%	61%
Interest Rates	100%	0%	0%	78%	0%	22%
Unemployment	5%	15%	80%	13%	22%	65%
Bank Failures	10%	20%	70%	9%	17%	74%

10. U.S. Economy Grade – Next Six Months

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

- Lenders optimism on the U.S. economy decreased slightly this quarter from 2.50 in 2Q 2017 to 2.43 in 3Q 2017, which is a “B” grade. In the current quarter, 48% of respondents believe the economy will perform at a “B” level, which represents a decrease of 2 points from the previous quarter. There was also a slight increase of lenders (48%) that believe the economy will perform at a “C” level, a 2 point decrease from the 2Q 2017 results, while 0% of lenders continue to believe that the economy will perform at a “D” level or “F” level in the near term.

<u>Grade</u>	<u>2Q/2017</u>	<u>3Q/2017</u>
A	0%	0%
B	50%	48%
C	50%	48%
D	0%	4%
F	0%	0%
Weighted Average Grade	2.50	2.43

11. US Economy Grade – Beyond the Next Six Months

Respondents were asked how they expected the U.S. economy to perform beyond the next six months on a grading scale of A through F.

- Lenders expectations for the U.S. economy’s performance in the longer term increased from the prior quarter. The weighted average GPA increased 22 points from a 2.30 in the previous quarter to 2.52, which is a “B” grade. 44% of lenders feel as though the economy will perform at a “B” level beyond the next six months (compared to 40% last quarter). Lenders who believe the economy will perform at a “C” over the next twelve months increased 2 percentage points to a 52%. There was an increase of lenders (4%) that believe the economy will perform at an “A” grade over the next six to twelve months while the percentage of lenders that believe the economy will perform at a “D” grade decreased 10 percentage points to 0%.

<u>Grade</u>	<u>2Q/2017</u>	<u>3Q/2017</u>
A	0%	4%
B	40%	44%
C	50%	52%
D	10%	0%
F	0%	0%
Weighted Average	2.30	2.52

12. Customers’ Future Growth Expectations

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

- The percentage of respondents indicating their customers have “moderate” growth expectations for the next six months to one year increased 9 percentage points from 74% in Q2 2017 to 83% in Q3 2017. With a concentration remaining towards moderation, 0% of lenders ascribe “very strong growth”, and 17% of lenders ascribe “strong growth” for their borrower’s growth in the next six months. Furthermore, 0% of lenders favor “no growth”, a 10 percentage point decrease from the previous quarter’s results of 10%. This continued belief of “moderate growth” is a positive signal from lenders on the U.S. economy.

<u>Indication</u>	<u>2Q/2017</u>	<u>3Q/2017</u>
Very Strong	0%	0%
Strong	16%	17%
Moderate	74%	83%
No Growth	10%	0%

13. 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.

Many lenders are content right now and plan to maintain their current loan structure. However, in 3Q 2017 we did see a slight decrease, 4 percentage points, of lenders that plan to relax their loan structure.

	<u>2Q/2017</u>			<u>3Q/2017</u>		
	<u>Tighten</u>	<u>Maintain</u>	<u>Relax</u>	<u>Tighten</u>	<u>Maintain</u>	<u>Relax</u>
Loans > \$25 million	6%	82%	12%	14%	81%	5%
\$15 – 25 million	6%	82%	12%	5%	91%	4%
\$5-15 million	6%	83%	11%	0%	96%	4%
Under \$5 million	5%	90%	5%	13%	78%	9%
Overall Average	6%	84%	10%	8%	86%	6%

14. 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.

While a majority of lenders continue to maintain their interest rate spreads and fee structures, fewer lenders (9 percentage points less) expect to reduce their interest rates spreads, and more lenders (6 percentage points more) expect to increase their interest rate spreads in Q3 2017 versus Q2 2017.

	<u>2Q/2017</u>			<u>3Q/2017</u>		
	<u>Reduce</u>	<u>Maintain</u>	<u>Increase</u>	<u>Reduce</u>	<u>Maintain</u>	<u>Increase</u>
Loans > \$25 million	24%	70%	6%	10%	81%	9%
\$15 – 25 million	18%	76%	6%	5%	91%	4%
\$5-15 million	11%	78%	11%	9%	73%	18%
Under \$5 million	11%	78%	11%	4%	70%	26%
Overall Average	16%	76%	8%	7%	79%	14%

15. 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.

3Q 2017 displayed a more even dispersion between +1/4 point and +1/2 point increases, with 50% of respondents favoring +1/4 point increase and 41% of respondents favoring an increase of +1/2 point or more.

<u>Bps Change</u>	<u>2Q/2017</u>	<u>3Q/2017</u>
+ 1/2 point or more	73%	41%
+ 1/4 point	26%	50%
Unchanged	0%	9%
- 1/4 point	0%	0%
- 1/2 point or more	0%	0%
Weighted Average	0.46 bps	0.33 bps

16. Current Competition

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

- Regional Banks continues to place at the top in regards to respondents (44%) for the survey. Commercial Finance, at 22% of respondents, saw an increase of 1 percentage point. Additionally, Local Community/Commercial Banks saw a slight decrease with 13% of respondents, and Money Center Banks saw an increase in the number of respondents (17%) from the previous quarter's survey.

	<u>2Q/2017</u>	<u>3Q/2017</u>
Regional Bank	37%	44%
Commercial Finance Co.	21%	22%
Money Center Banks	16%	17%
Local Community/Commercial Bank	21%	13%
Factors	0%	0%
Other	5%	4%