

***Some actionable ideas in credit
and equities***

Sean J. Egan

President, Egan-Jones Ratings

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Overview

I. Where we are

II. Where we are going

III. Resulting opportunities

Major Market Drivers

Hyper-activity of the Central Banks

Weakening Sovereign Credit Quality

De Facto Restructuring of Troubled
Economies

Major Market Drivers (cont'd)

Hyper-activity of the Central Banks - well covered (is continuing)

Weakening Developed Country
Sovereign Credit Quality - worse

De Facto Restructuring - will explain

Weakening Major Sovereign Credit Quality

- Japan: 230+% debt to GDP
- US: \$100+T unfunded liabilities
- UK: near 7% deficit, and losing banking
- EU: Serial crises

- Massive problems -> chaos?

Weakening Major Sovereign Credit Quality

A problem that is too big to solve, won't be "solved" – the parameters will simply be changed

The “Elegant Solution”

- Past 5 years have focused on recapitalizing banks and reducing global interest rates
- Next 5 years will be focused on eliminating the debt overhang & address the Reinhart and Rogoff problem

Three Step “Elegant Solution”

- Central banks buy sovereign debt from banks (near par)
- Central banks offer to reduce rate for reforms in banking and fiscal policies
- Central banks transfer sovereign bonds and related liabilities to a SPV

[and the debt is basically forgiven]

Catalyst – ? Depositor Skittishness, DB Issues

- Greece - 90+% write-off
- Cypress - depositors eviscerated
- Runs on weaker banks leads to ECB backstop and more intervention.
- DB's capital (2.8% but only 2% with EUR10B derivative losses). Will be OK

**Framework for a typical restructuring -
Finding the fulcrum**

Opportunity : finding the fulcrum

Framework for a typical restructuring -
finding the fulcrum – ie, where debt
can be supported (economically and
politically).

Recent examples: homebuilders and the
monolines (huge rebound)

Opportunities over 6 to 18 Mos.

	Safe	Questionable	Gone
Germany	Nearly Everything		
France	Large Banks & Firms	Others	
Italy & Spain		Largest Banks & Firms	Most others
The Exotics			Nearly Everything

Next Opportunity: Yield Mean Reversion

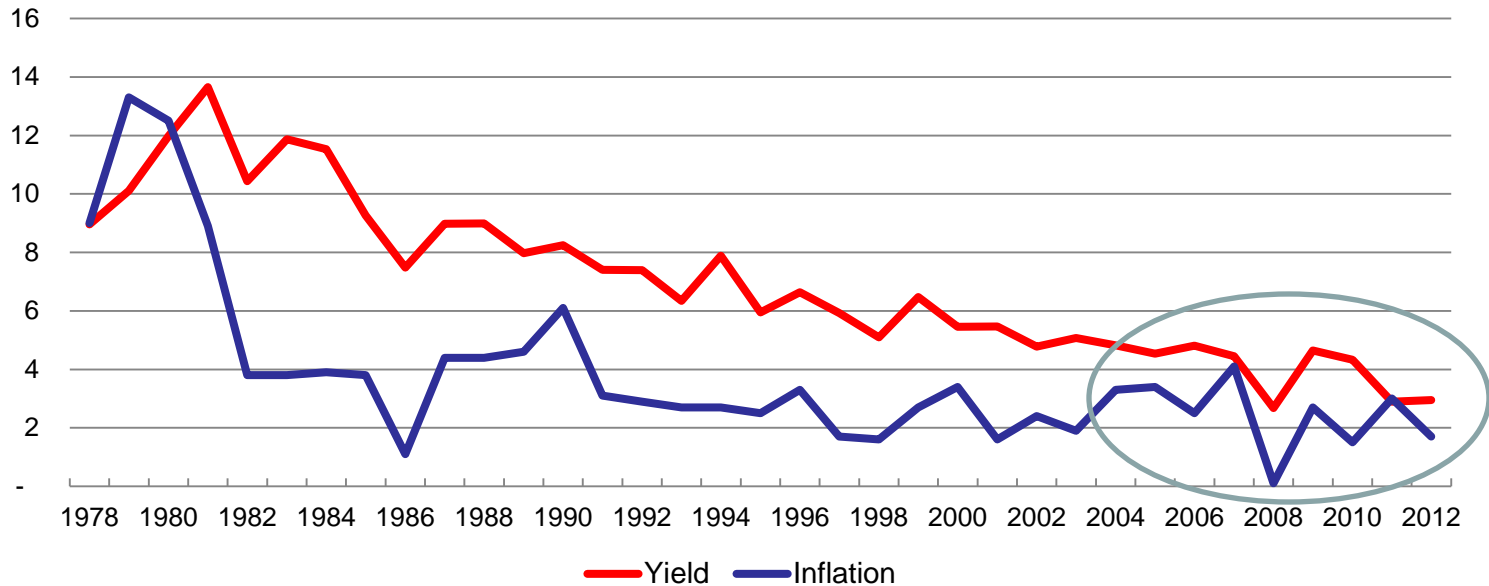
Long-dated, low coupon, low credit risk bonds and strips

- Normal yields are 336bps over inflation
- Current yields are 118bps over

- Hike in yield as the economy improves or the targeted inflation is manifested
- The fear factor is slipping

Normal Yield less Inflation: 3.36%

30 Year Treas. Yield & Inflation (%)



	<u>Yield</u>	<u>Inflation</u>	Yield less <u>Inflation</u>
Median%	6.56	3.20	3.36
Current%	2.88	1.70	<u>1.18</u>
Difference			2.19%

Opportunities over 6 to 12 Mos.

	Description	100bps: % change	200bps: % change
T 7 1/8's 02/15/23	US Treas. due in 2023	-7.8%	-14.9%
T 3 1/8 02/15/43	US Treas. due in 2043	-17.1%	-30.4%
SP 0 02/15/43	Treas. Strip due in 2043	-25.9%	-44.6%
JNJ 4.85 05/15/41	J&J due in 2041	-14.6%	-26.2%

Caution!

!But wait until after the Bank of Japan's massive buying and depressing yields!

Next Opportunity: UK's slippage

Premise: the UK economy is driven by banking, and to a lesser extent by insurance services, media, and tourism. The credit crisis, the government's control of major banks, and the EU's attacks will continue to pressure the UK.

The UK's slipping credit quality

	Annual Ratios (source for past results: IMF)					
INDICATIVE CREDIT RATIOS	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>P2012</u>	<u>P2013</u>	<u>P2014</u>
Debt/ GDP (%)	64.6	78.0	86.3	94.5	102.2	110.4
Govt. Sur/Def to GDP (%)	-11.5	-10.2	-7.8	-6.9	-6.4	-6.8
Adjusted Debt/GDP (%)	64.6	107.7	114.9	122.5	129.5	137.1
Interest Exp/Taxes (%)	7.0	10.4	11.1	10.4	11.5	11.8
GDP Growth (%)	1.8	0.9	0.2	-0.5	-0.5	0.5
Foreign Reserves/Debt (%)	2.8	2.9	2.9	2.6	2.4	2.2
Implied Sen. Rating	A-	BBB+	BBB	BBB	BBB	B+

UK CDS

	5 Year	
	<u>CDS</u>	<u>Debt/GDP%</u>
Germany	33.9	81.7
United States	34.3	73.6
United Kingdom	45.2	88.7
France	72.5	89.9
Spain	271.8	85.3
Italy	275.7	126.1
Portugal	427.0	119.7

Next Opportunity: organic growth, pricing power, and some barriers

- Premise: rising premium on real growth
- IACI/Interactive
- Revs growing at 29% per year
- Core business (search and Match)
operating income rising 48%
- Network effect/ some barriers
- Forward P/E of 12.3
- Risk: control by Barry Diller (43%)

Summary of Opportunities

Europe's Elegant Solution - using
bankruptcy template, focus on the
“money good” sectors

Depressed Yields - as BOJ's actions
wane, look for mean revision

UK squeeze - core industries slipping,
credit quality and CDS squeeze

Growth Premium – IAC Interactive

Contact:

Peter Arnold 646-998-6496

parnold@egan-jones.com
