High Beta Instruments: Looking for Yield

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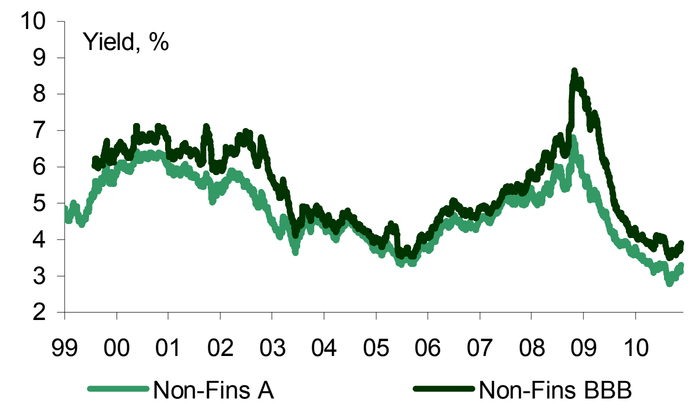
Introduction

- Investors have begun to seek investments and strategies away from investment grade non-financials to fulfill their yield requirement.
- In the new investment cycle, structured credit products are unlikely to attract investors.
- The average non-financial single-A and BBB low yields has created an acute problem for yield seekers.

Non-Financial single-A and BBB yield



Opportunity 1: Extend duration

- Extend duration within investment grade non-financials.
- Credits satisfying the 4.5% yield criteria represent c. €53bn.
- Risks: long duration + inflation exposure + credit risk.
- Average default rate over a 10-year time period: 8% for BBBs.
- Rating downgrades increase the capital cost of holding BBB credits and should be factored into the investment decision.
- Issuance has increased at the long end. This trend will continue as the EUR corporate market continues to mature.

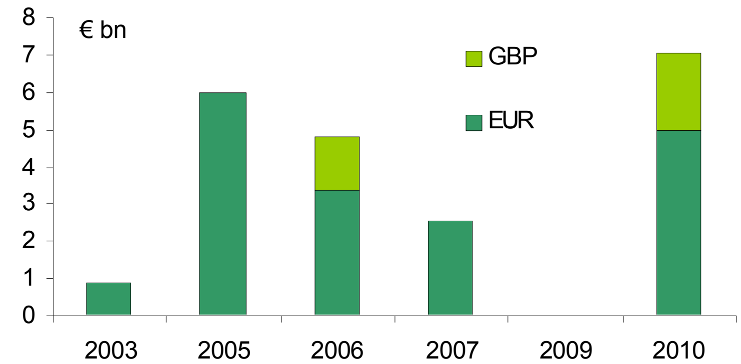
Opportunity 2: Sovereign Risk

- Investors can achieve their 4.5% to 6% yield targets by investing in Greece, Ireland and Portugal.
- Yet, they have shown no appetite for these distressed sovereigns over the last year.
- Fundamentals are unlikely to change anytime soon.
- Spain and Italy do satisfy the 4.5% yield criteria…
- …but investors will prefer exposure to a diversified portfolio of corporate credits vs idiosyncratic sovereign risk.

Opportunity 3: Corporates Hybrids

- A small sub-sector of the market but with growing interest from investors.
- With 27 issuers making up the basket, investors can now take a portfolio view.
- With the asset class providing an average asset swap spread of 300bp, the asset class does provide value.
- Asset managers concentrate on the creditworthiness of the issuer and then on the structure.

Hybrid Issuance



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Opportunity 3: Corporates Hybrids (Cont'd)

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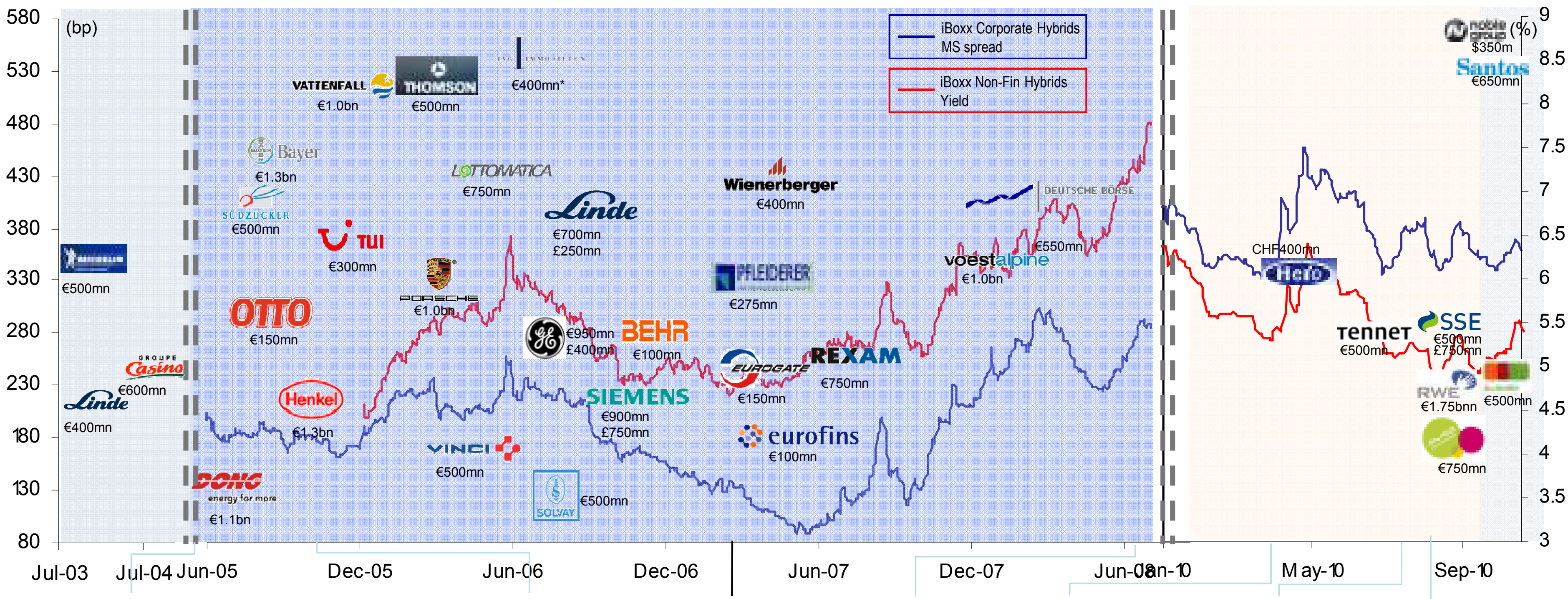
Evolution of the Corporate European Hybrid Capital Market



Opportunity 4: High Yield

- Investors will continue to seek yield via Non Investment Grade Securities.

- In a benign default landscape, investors are comfortable with the high yield asset class which is growing in size and diversification.

- We expect 2011 to be another big issuance year.

- The senior secured market also saw sizeable issuance in 2010 year and should keep growing, as loan markets continue to be constrained.

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Opportunity 4: High Yield (Cont'd)

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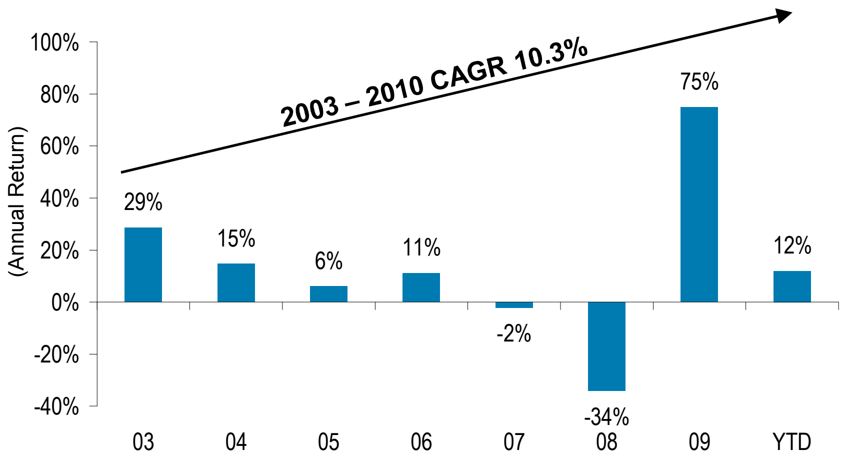
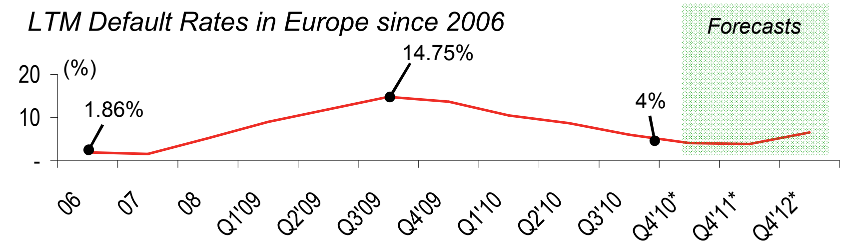
1. Historical Returns



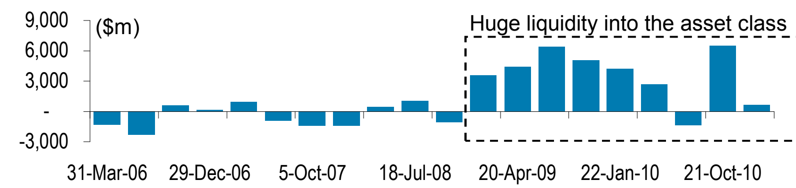
Source: Merrill Lynch – Global High Yield Index

2. Defaults rates and liquidity into the asset class

LTM Default Rates in Europe since 2006

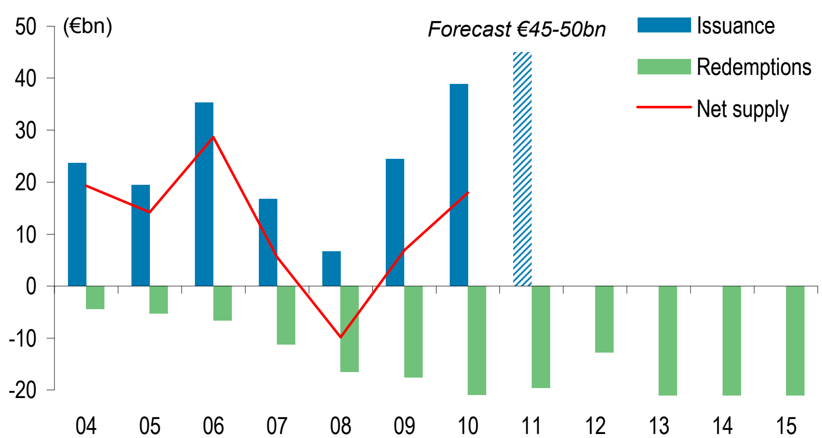


Inflows/outflows in the HY asset class (quarterly)



Source: S&P: Global Default Rates Historic and Future, LCD News

3. Expected Supply in Europe



Source: Dealogic, BNP Paribas

4. Returns Expectations

- **Limited performance of spreads on average**
  - **Inflows would not trigger spread performance but help digest primary pipeline**
- **Low default rates**
- **Returns in line with current yields:**
  - **8.4% for European HY EUR**
  - **7.9% for US HY USD**
- **Sovereign risk could skew European HY to the downside**

Opportunity 5: Emerging Markets

- A growing segment of the market so far dominated by USD issuers.
- An opportunity to diversify credit risk.
- Emerging market economies have recovered from the financial crisis quicker than their developed peers.
- Middle East's OPEC countries are likely to benefit from an estimated capital inflow of $540 billion in 2011.
- Growth prospects in the emerging Europe region remain mixed.

Global Corporate EM index