

# **Loan Market Update**

## ***2009 CIPA Conference***

A large red square containing the text "UNION BANK OF CALIFORNIA" in white, sans-serif, all-caps font, centered within the square.

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# The Credit Crisis – Round One

***“The loans we dated”***

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***“We didn’t lose the game, we just ran out of time”*** – Vince Lombardy

- Beginning in the summer of 2007, cracks started to form in the system
  - Collateralized loan obligations (“CLOs”) were the first big problem area
  - Sub-prime mortgages were a significant piece of the CLO market
- Unlike traditional loans, CLO loans were designed to be warehoused and quickly securitized into the global market
  - Less credit due diligence vs. traditional loans
  - Accounted for as an investment
- Credit concerns caused liquidity in CLO market to disappear
  - Large mark to market write-downs on “investment grade” securities
- Impact was wide spread, but many banks were not directly affected

# The Credit Crisis – Round Two

***“The loans we married”***

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***“If you owe the bank \$100, that’s your problem. If you owe the bank \$100 million, that’s the bank’s problem” – J. Paul Getty***

- The credit crisis has now spread to traditional bank loan portfolios
  - Commercial real estate
  - Commercial / industrial (particularly in troubled industries)
  - Consumer debt (mortgages, home equity lines, credit cards)
- Fed announced up to \$599 billion in losses from 19 largest banks
- WSJ reported up to \$206 billion in losses from 940 regional banks
- This round of the credit crisis has impacted the entire banking industry

# Fallout From the Credit Crisis

## *Impact to the banking industry*

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**Losses from write downs and provisions have caused banks to:**

- Seek government bail-out funds
  - Nearly \$600 billion committed to date in TARP and other government relief
- Raise new equity
  - Several banks have either completed or announced plans to raise \$8 billion in new equity
- Conserve capital
  - Exit / curtail lending activities – particularly in troubled / non-core segments
- Consolidate
  - Oliver Wyman estimates that the current 8,000 banks in the U.S. will reduce by 2,000 or more
- Fail
  - Since 01/01/08, regulators have seized 58 banks - 33 so far this year

# Fallout From the Credit Crisis

## *Impact to the banking industry*

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*“Nothing is so permanent as a temporary government program”*

- Milton Friedman

### ■ **REGULATION**

- Greater oversight of lending practices
- More frequent / thorough reviews of portfolio quality
- Greater general business oversight including appropriate compensation

### ■ Much tighter internal oversight

- Frequent portfolio reviews / stress tests

### ■ Banks must balance external reputation / client relations with need to pro-actively manage capital and credit risk

# Fallout From the Credit Crisis

## *Impact to oil and gas lending*

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### ■ Positives

- Despite precipitous drop in commodity prices, oil and gas remains relatively strong vs. other sectors
- High quality collateral which can be readily evaluated
- Proven borrowing base structure with low historical loss content
- Relatively transparent industry – identifiable risks
- Faint signs of life in bank originations and syndications

### ■ Negatives

- Extreme price volatility = credit uncertainty
- Increased credit exposure on commodity derivatives
- Fallout from isolated credit issues in sector
- Many banks are sidelined due to overall capital constraints, credit issues
- Several banks active in the sector are merging

# Fallout From the Credit Crisis

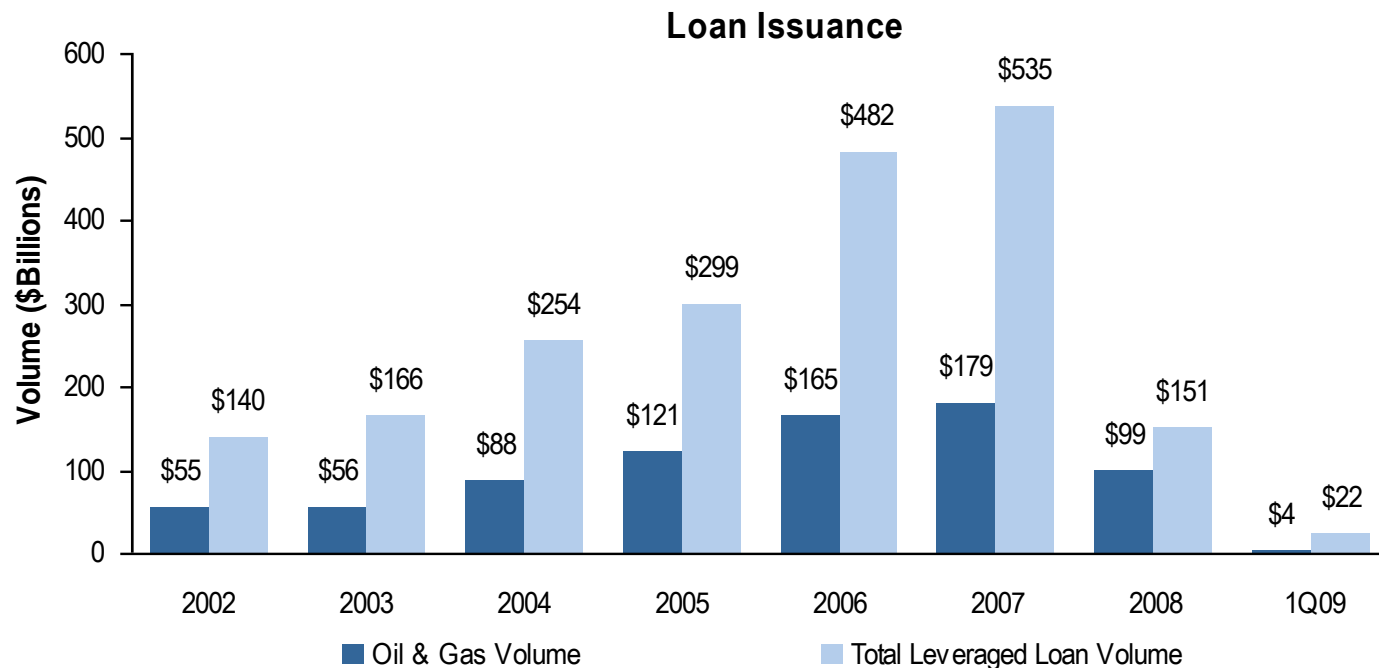
## *What to expect from your banks*

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- With scarce capital, shorter tenors have become more common
  - Borrowers are refinancing existing 5 year loans with max. 3 year tenors
  - 364-day facilities accounted for more than 70% of broad industry investment-grade issuances in 1Q09
- Going forward, a selective and cautious lending environment is expected to prevail
  - Smaller deals with shorter tenors
  - Reliance on club of relationship lenders – but clubs harder to form
  - Longer response time on requests
  - Less flexibility on terms / advance rates
  - Greater pricing at all levels of the credit spectrum
  - Substantial fees for waiver consents
  - Expectation of significant long term ancillary business
  - Borrowers will probably have to spread commodity hedging exposure to more counterparties – potential future exposure calculations are being revised

# Oil & Gas Transaction Issuance

- Amid continued weakness in the economy and lack of M&A activity, 2nd quarter '09 lending conditions are expected to remain tight

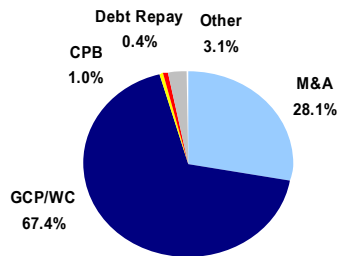


Source: LPC

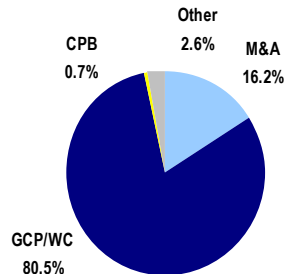


# Oil & Gas Transaction Issuance

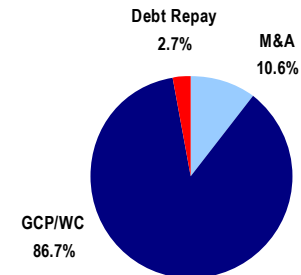
**2007 Deal Composition**  
\$178.7 Billion of Issuance



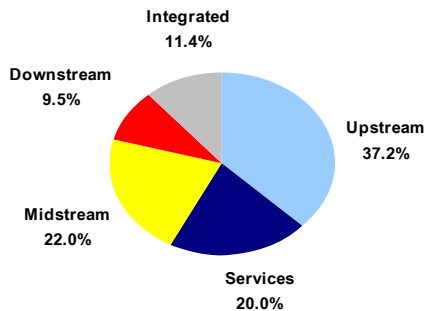
**2008 Deal Composition**  
\$99.3 Billion of Issuance



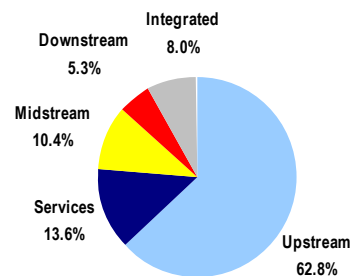
**1st Qtr 2009 Deal Composition**  
\$3.9 Billion of Issuance



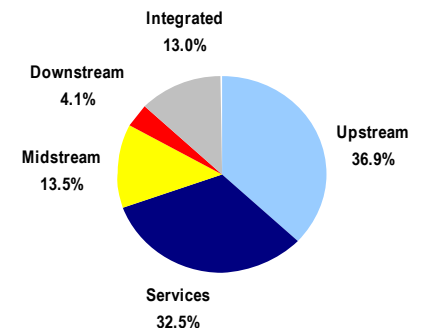
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**2008 Deal Composition**  
\$99.3 Billion of Issuance

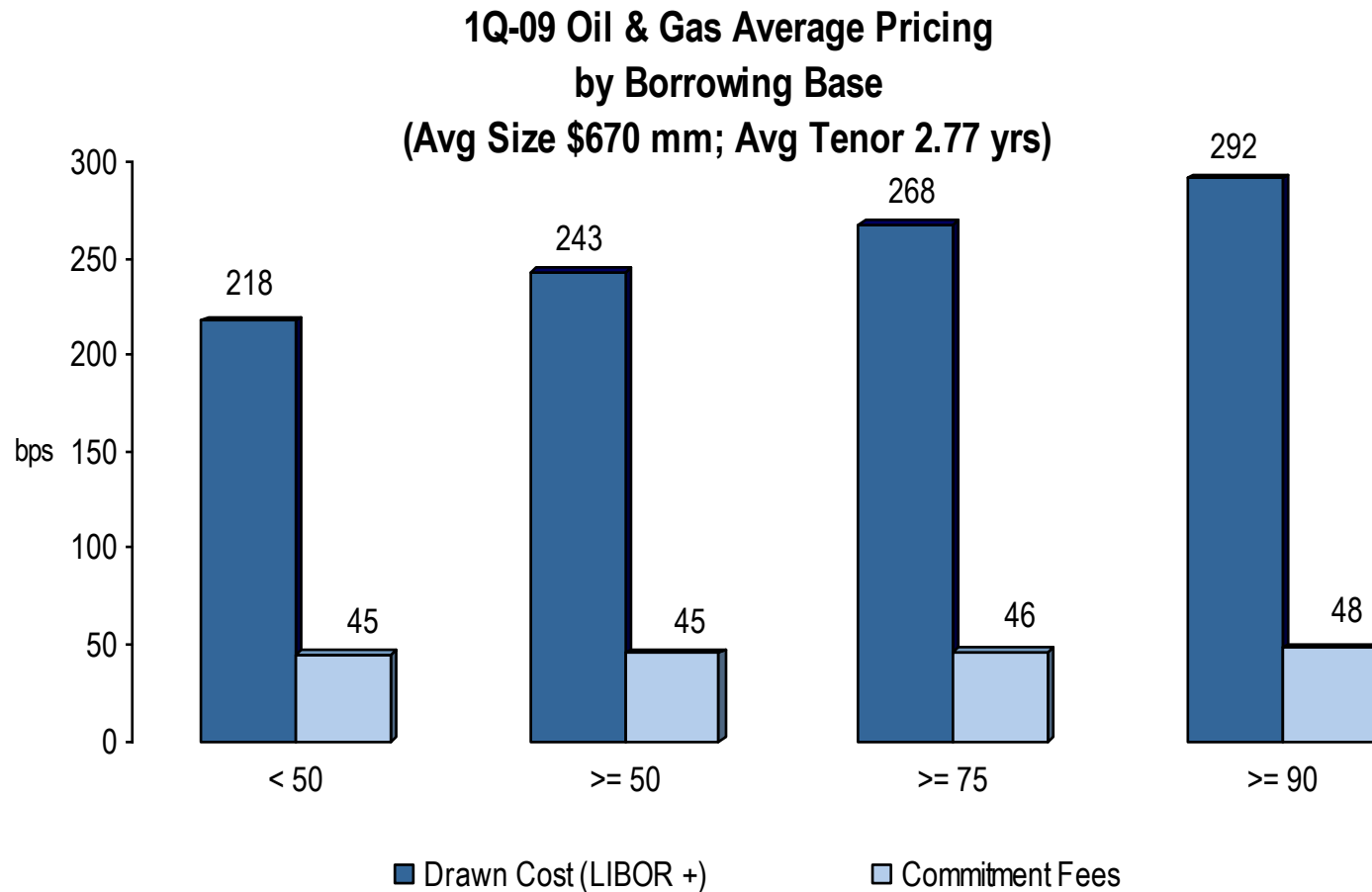


**1st Qtr 2009 Deal Composition**  
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# Loan Market Update

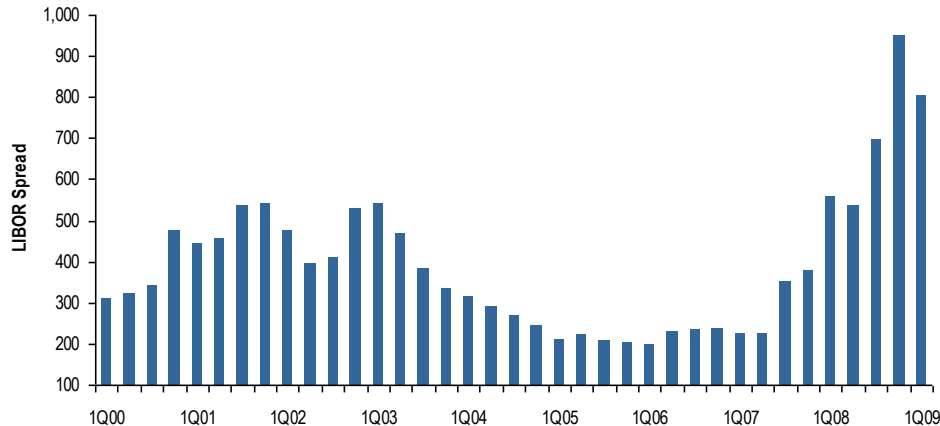
## *Oil & gas loan pricing*



# Loan Market Update

## *Oil & Gas Transaction Issuance*

Average Secondary Spread, Oil & Gas Loans



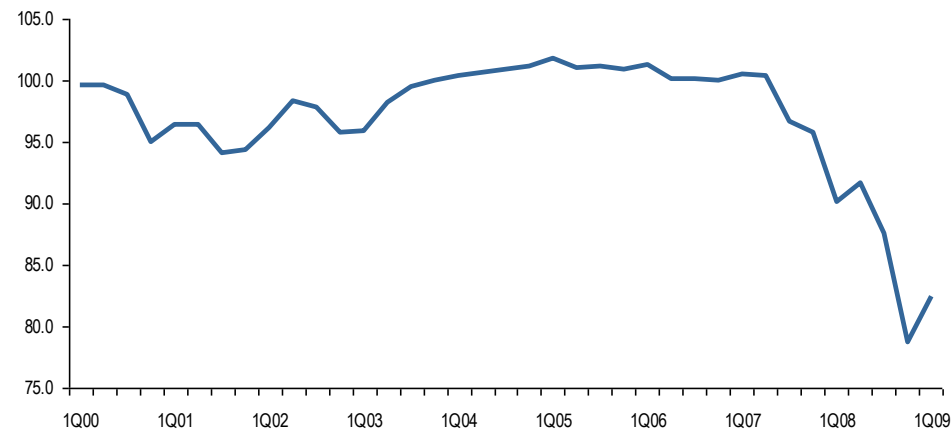
- Asset buyers have begun to demand premium fees, margins, and terms across the credit spectrum  
Banks and non-bank lenders have witnessed an increased cost of capital
- Some lenders are engaged in secondary market purchase programs to take advantage of familiar names at discount prices

▪ Pricing and upfront fee increases were felt across the ratings spectrum, impacting even the highest-rated names

- For issuers with existing deals tied to market-based pricing, new deals show a resetting of floors and caps

Source: LPC

Average Bids, Oil & Gas Loans



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# Union Bank Overview

## *Facts and figures*

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- With \$69 billion in total assets, Union Bank is the 16th largest U.S. bank and among the best capitalized banks in the U.S.
  - Rated A+ / A2 / A+ (S&P / Moody's / Fitch)
- Union Bank has experienced minimal impact from the disruption in the capital markets
  - No sub-prime exposure
  - No TARP money
  - Healthy, growing deposit base
  - No funding concerns
- Wholly-owned by Mitsubishi UFJ Financial Group, Inc., Japan's largest bank by market value

# Union Bank Capabilities

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- Petroleum Group – Uninterrupted 27 year track record arranging financing transactions for the oil and gas industry
- Expertise in:
  - Structuring, underwriting and syndication of 1<sup>st</sup> lien and 2<sup>nd</sup> lien transactions
  - Commodity, interest rate and currency hedging
  - Cross-border and Canadian \$ transactions through our Calgary branch
  - Direct equity investments
  - Treasury management and investment products
  - 1031 like-kind exchange services
- Commitments to the oil and gas industry totaling \$5.2 billion
- Lending staff of 26 professionals, including four petroleum engineers
- Syndications & Placement consists of 11 professionals

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