

Surviving the Storm: Telecom Weathers the Financial Market

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- The Perfect Storm: Financial Melt-Down Factors
- The Height of The Storm
- Aftermath
- Rebuilding Realities
- The Bottom Line



- Total Assets of \$61.2 Billion
- Net Earnings Increased 28% to \$533.4 Million
- Average Loan & Lease Volume Increased 28% to \$45.4 Billion
- 97.2% Loans & Leases Ranked Outstanding in Accordance with Highest Regulatory Credit Quality Measurements
- \$314 Million in Patronage Distributed to Customer-Owners
 - \$207 Million Paid in Cash



➤ Total Portfolio

- 240 Customers
- \$3.9 Billion Commitments
- \$3.2 Billion Outstandings

➤ Wireline Portfolio

- 189 Customers
- \$2.9 Billion Commitments
- \$2.3 Billion Outstandings

➤ CATV Portfolio

- 25 Customers
- \$545 Million Commitments
- \$481 Million Outstandings

➤ Wireless Portfolio

- 26 Customers
- \$488 Million Commitments
- \$377 Million Outstandings



➤ There's Lots of Blame to Go Around

- Lenders
 - Subprime Mortgages & Related Financial Instruments
 - Credit Cards
 - Syndicated loan structures
- Government
 - Rates Artificially Held Too Low, Too Long
 - Lack of oversight
- Personal
 - The “Golden Age of Spending”



➤ Lender Factors

- Lower Rates Fueled Credit Demand
- Lending Practices Out of Control
 - Mortgage Lenders Wildly Aggressive
 - Birth of Subprime Market - \$6 Billion Issued in 2006
 - Higher Risk = Higher Yields (Fees & Interest Rates)
 - Little Incentive to Make Good Loans
 - Loans Securitized & Sold Around the World
 - Off balance sheet transactions
- Rating Agencies Failed to Quantify Risk
 - AAA Ratings Awarded – Same as Government Debt
- New Investors Entered Market
 - Hedge Funds
 - Institutional Loan Funds
- Imprudent Investment Strategies



- Fundamentals of Lending Ignored
 - 5 C's of Credit
 - Conditions
 - Capital
 - Capacity
 - Collateral
 - Character

- Too many intermediaries



➤ Government

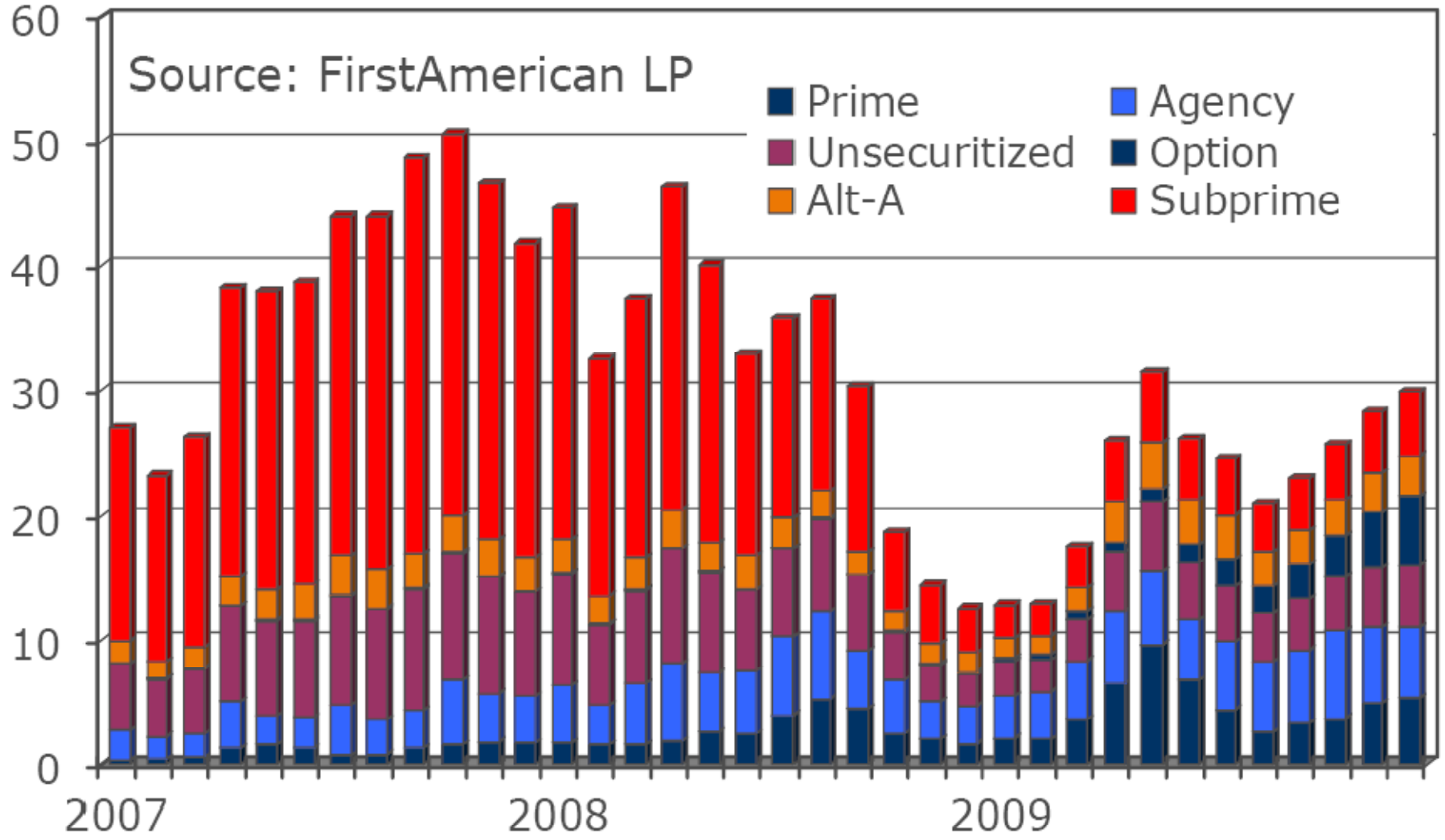
- “Central bankers . . . along with other financial regulators, were asleep at the wheel, failing to appreciate the scale of risks being built up ... by keeping money too cheap for too long.” *The Economist*
- Fed Lowered Rates & Kept Them Low
 - Fueled Credit Demand
- Fed Banks Around the World Followed Suit
- Policies Lead to Increased Leverage
 - Ratio of Total Debt to Total Equity Increased
 - 10-15x Normal for Conservative Bank
 - Ballooned to 30x



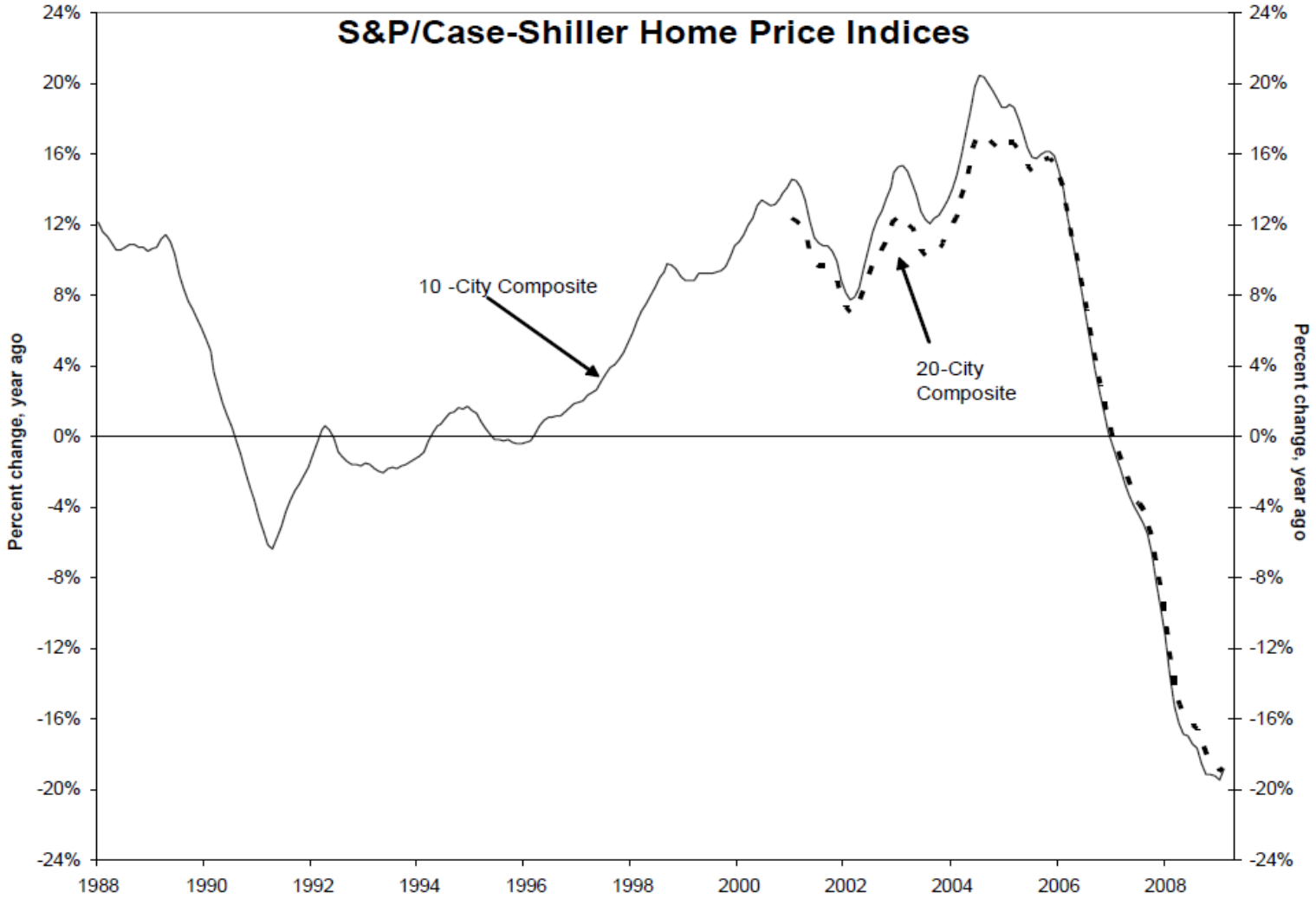
➤ Personal/Consumer

- Adjustable Interest Rates Kick In
- Real Estate Values Decline
- Job Losses Accelerate
- Dramatic Fall in Spending
- Increase in bankruptcies

Rate Resets by Volume \$B



Home Price Indices



Source: Standard & Poor's & Fiserv



- Record Making Loan Default Rates
- Banks Stuck with Non-Performing Assets/CDO's
- High Profile Failures, Write-Offs & Lack of Liquidity
 - Fannie Mae & Freddie Mac Bailout
 - Massive Commercial & Investment Bank Write-Offs
 - \$1 Trillion in Losses Pulled \$10 Trillion Capacity from Market
 - AIG
 - Bear Sterns
 - Lehman Brothers
 - Merrill Lynch
 - Wachovia
 - Washington Mutual



- Crisis of
 - Liquidity
 - Capital
 - Confidence

- Banks UNWILLING to Lend to Other Banks

- Short Term Rates Spiked

30 Day LIBOR History





- \$468.3 Billion Spent as of 5/18/09
 - 586 Financial Firms
 - \$69.8 Billion to AIG
 - \$102.5 Billion to Citi & Bank of America
 - \$32.3 Billion to Detroit Automakers
 - \$84.9 Billion to Freddie & Fannie

- Continued Mistrust Fueled by “Reckless” Spending
 - Corporate Trips, Corporate Jets, No Accountability
 - Calls for Transparency & Oversight

\$787 Billion Investment & Recovery Act



- 35% Tax Cuts & 65% Spending
- Tax Cuts
 - \$400 to Individuals & \$800 to Couples
 - Amounts to Extra \$13 per Week per Person, Beginning in June
- \$120 Billion to Infrastructure & Science
 - \$7.2 Billion Broadband
- \$105.9 Billion Education & Training
- \$37.5 Billion Energy
- \$24.3 Billion to “Helping Americans Hit Hardest by Economic Crisis”



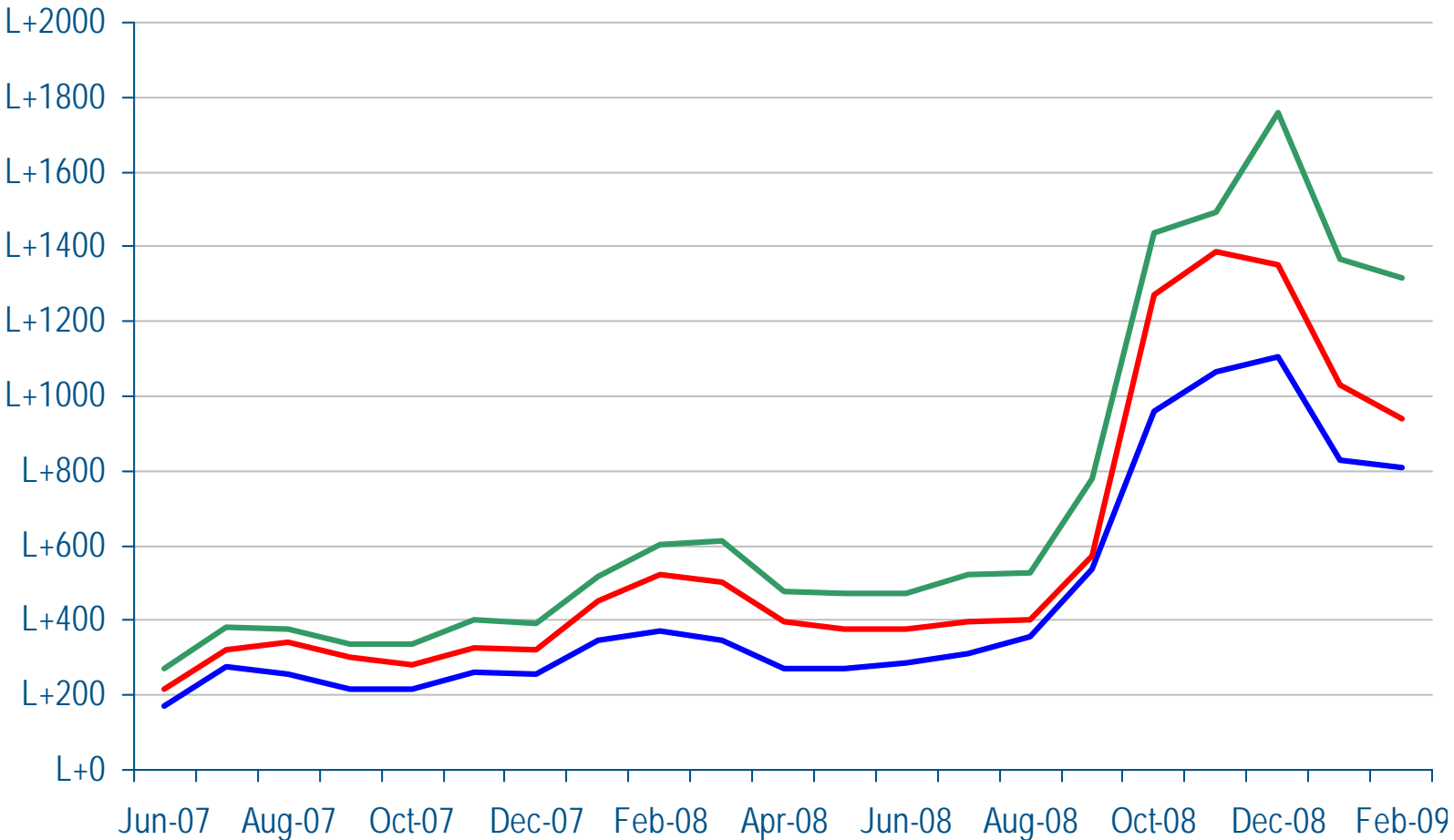
➤ Capital Markets Reaction

- Flight to Quality
- Tighter Covenants
- Lower Leverage (Debt/EBITDA)
- Shorter Tenors
- Amortizing Loans – Nothing Back End Loaded
- Limit Distributions
- Pricing to Risk
- Reluctant to Buy into New Credits
- Banks Driving Majority of Investment
 - Investment Funds Shied away from Marketplace

Aftermath: Pricing Up



Average Spreads to Maturity by Corporate Credit Rating
Reflects 15 Largest Index Names in Each Category

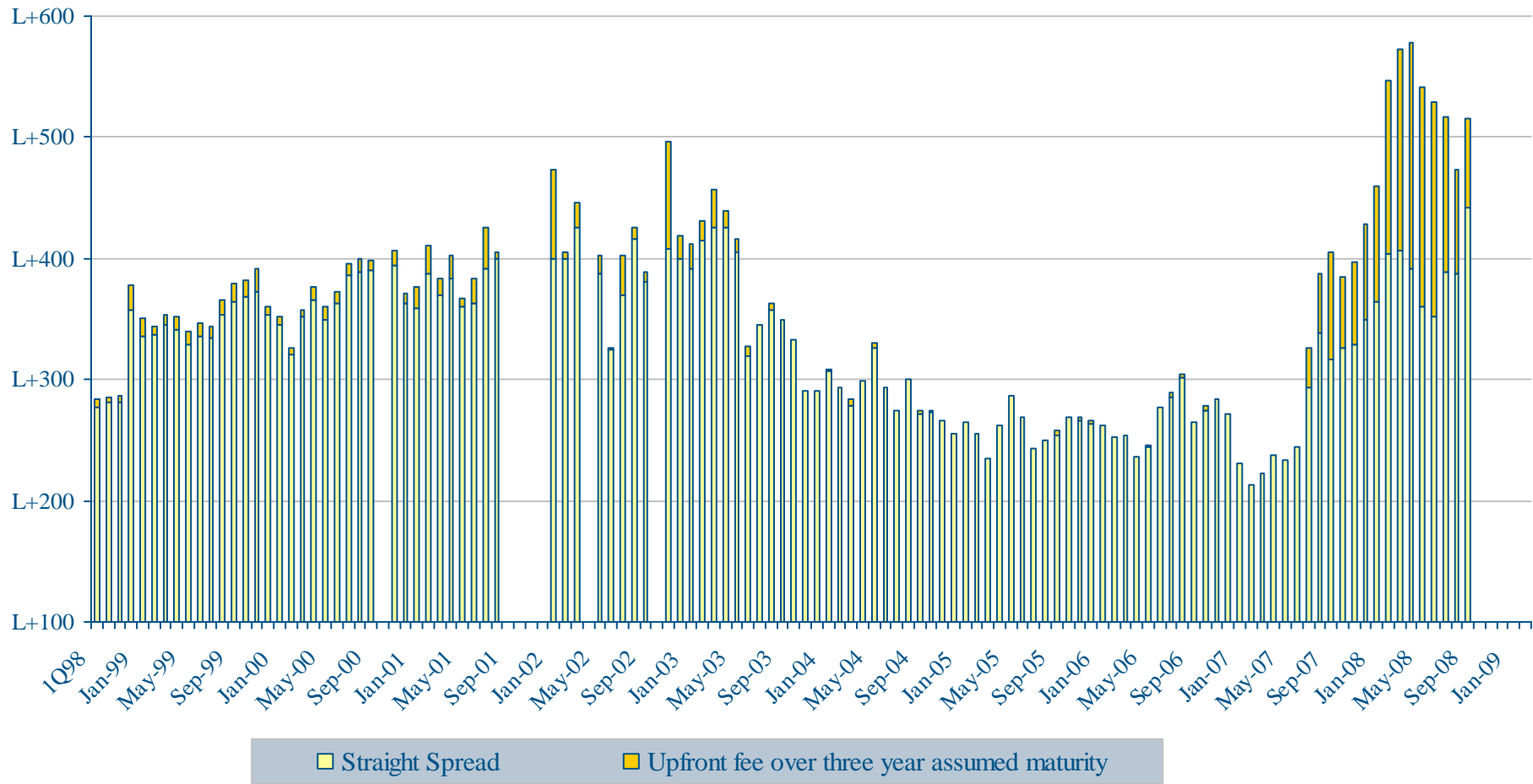


Source: Standard and Poor's LCD and S&P/LSTA Leveraged Loan Index; June 2007 – 1/29/09

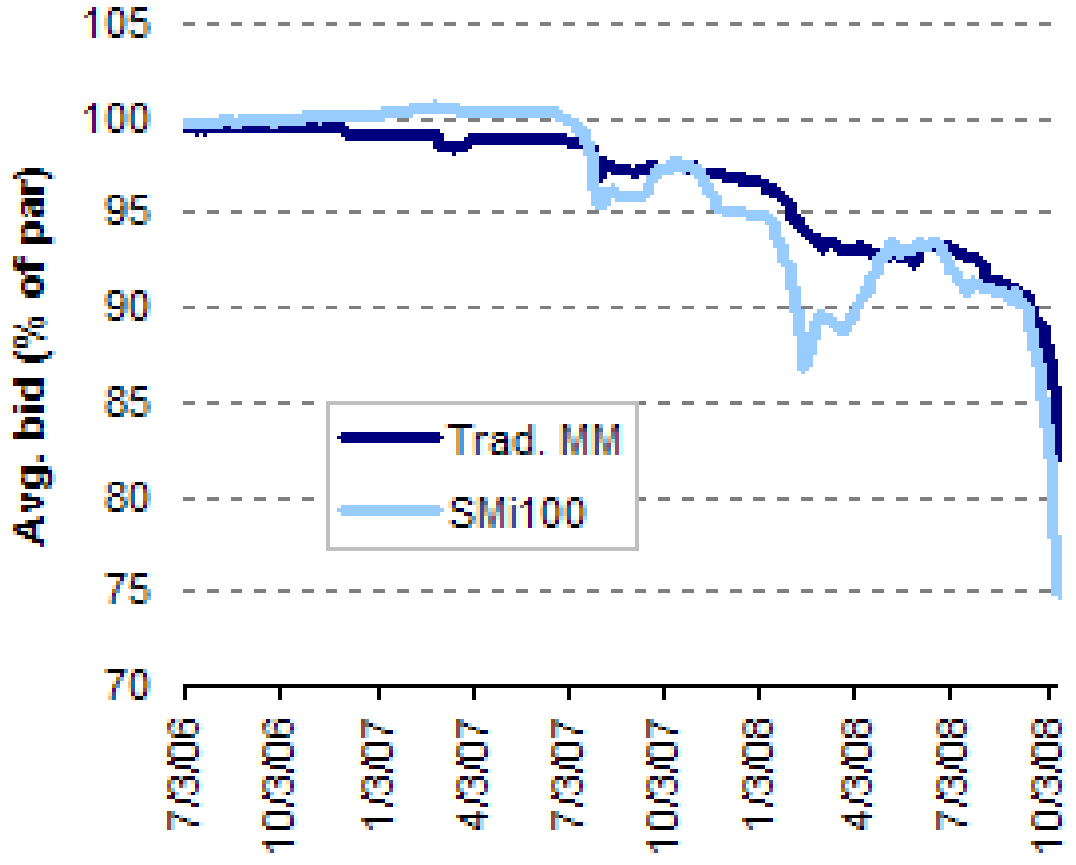
Aftermath: Pricing Up



Average All-in New-issue First-Lien Spread of B+/B Institutional Loans
 Assumes upfront fee is amortized evenly over a three-year assumed life



Aftermath: Secondary Markets Down





- RLEC, Cable & Other Infrastructure Valuation Decline in Response To
 - Less Access to Capital
 - Declining Cash Flows
 - Regulatory Uncertainty
 - Competition
 - Economy



History of Private ILEC Transaction Values

	\$ Per Connection			
	<u>All Sales</u>		<u>Non System</u>	
	Avg	Med	Avg	Med
2000	3,626	3,100	4,517	4,755
2001	3,714	3,453	3,742	3,508
2002	3,177	3,182	3,141	2,917
2003	3,153	2,650	3,155	2,650
2004	3,554	3,064	3,554	3,064
2005	3,543	3,251	3,543	3,251
2006	4,567	3,462	4,726	3,644
2007	3,070	3,012	3,070	3,012
2008	3,193	2,917	3,316	2,920

	Revenue and OIBDA Multiples			
	<u>All Sales</u>		<u>Non System</u>	
	Avg	Med	Avg	Med
2000	n.a.	6.0	n.a.	11.7
2001	n.a.	3.9	n.a.	9.2
2002	n.a.	4.0	n.a.	8.4
2003	n.a.	3.2	n.a.	7.7
2004	3.2	3.1	7.4	7.4
2005	3.2	3.2	7.0	7.1
2006	3.2	3.3	7.4	7.1
2007	3.0	2.9	6.8	6.7
2008	2.7	2.8	6.3	6.2

Notes: JSICA observations & estimates. Per connection multiples prior to 2007 calculated on an access line basis. Connections include ILEC lines, CLEC Lines, data subs and video subs.

Source: The ILEC Advisor, Volume 15 Issue 3, March 2009, JSI Capital Advisors



- Expect Conservative Lending Based on Realistic Assumptions
- Limited Capital Goes to *Strongest* Credits
- Tighter Loan Structures
- Price Matched to Loan Risk
- Leverage
 - Lower Multiples (3.5x is the new 4.5x)
 - Highly Leveraged Deals Very Difficult to Finance
- Expect Thorough Due Diligence from Lender
 - Assumptions Will be Challenged



➤ Clearly Communicate the Strength of your Project and Business

- Realistic Business Plan – It **Will** be Challenged
 - Based off Attainable Goals
 - Ensures Market Demand is In Line with Goals
 - Demonstrates Capital Structure Matches Business Plan
- Diversified Revenue Streams
 - Reduce Impact of Regulated Revenue Streams with Non-Regulated Services
 - Bundle Services in an Effort to Increase ARPU and Retain Access Lines
 - Stave Off Competition with Robust Service Offerings and Local Touches
- Reduced Reliance on Cost Recovery Mechanisms
 - USF & Access Charges will Likely Decline, Be Proactive
- Experienced Management Team



➤ Lenders are Looking to Fund

- Industry Consolidation
 - RLEC Market
 - Cable TV Market
- Continued Investment in Infrastructure and New Technology
 - Investment MUST Increase Revenue and/or Lower Costs
- New Investment into Rural Wireless
 - Funds for Wireless Investment May Not be Financed on a Standalone Basis
- Entry Into Video/Data Market
 - Cable System Acquisition
 - IPTV Build Outs
 - Well Planned Projects Critical, as Not Always Economical



- Capital is Available from
 - RUS
 - CoBank
 - RTFC
 - Local Bank
 - TARP???

- Under current market guidelines
 - Lower Leverage Multiples
 - More equity for acquisitions
 - Shorter tenors
 - Market fees/rates



Thank You

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