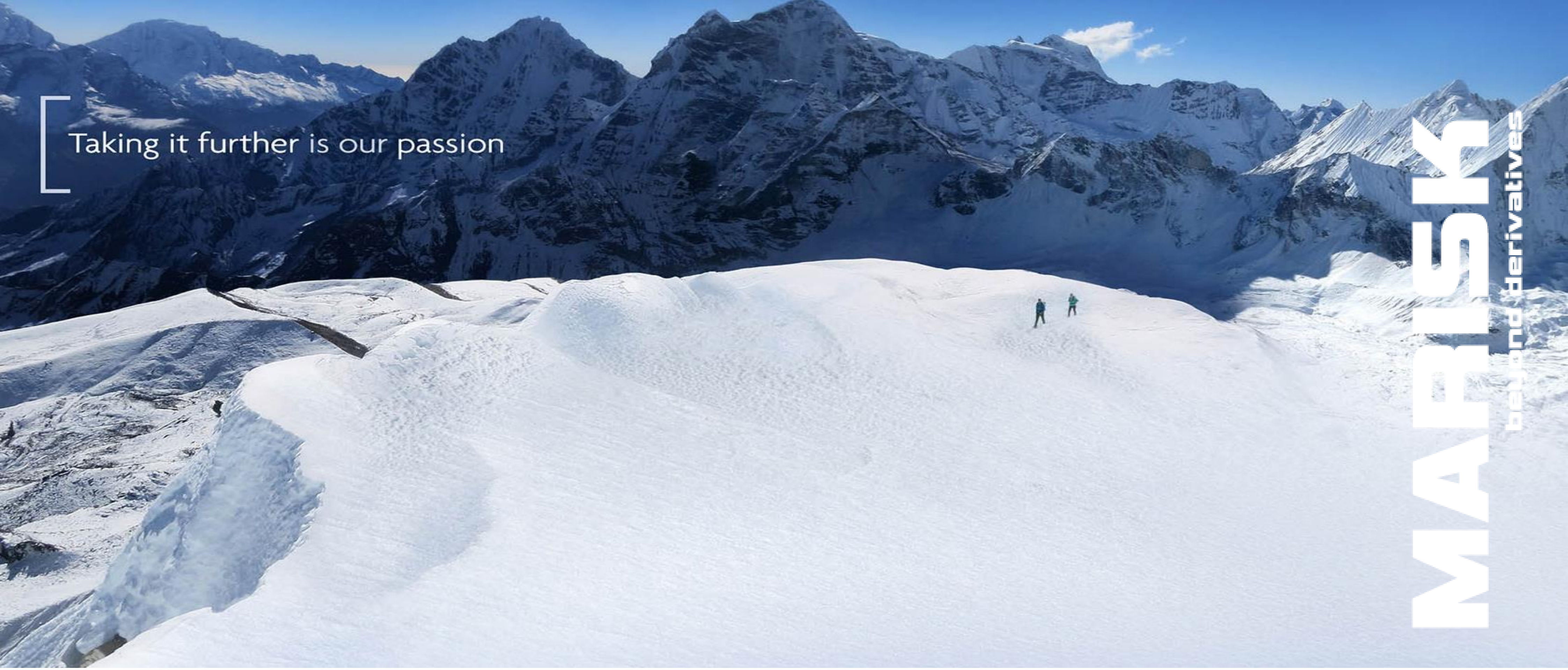


GETTING OVER THE HUMP

2016 Interest Rate Forecast

Marisk Consultants

Introduction

Dany Masri - CEO

2015 was another exciting year at Marisk. We advised on transactions with a value of almost AED5bn spanning a spectrum of industries across the GCC.

The tightening has begun, and the real surprises for us this year were the continued compression of swap spreads (negative from five years and beyond now!) and, of course, the collapse of oil, which hurt many stocks despite the obvious benefits to the consumer. The US Dollar rose another 9% YoY vs. a basket of international currencies, which hit US multinational corporations hard as well. The bond market kept time with the patient Federal Reserve, however some energy-led perturbations in the high yield market arose and are likely with us for 2016. While unemployment trended from 6% to 5% YoY, that 5% GDP growth late in 2014 proved to be a peak, as the US economy now appears troughed around 2% with roughly 1.2% annual inflation. Chair Yellen waited until December to raise the Fed funds target rate, so now LIBORs and shorter dated Treasury yields will become unmoored from the zero bound. So what else is likely in 2016?

We think three more tightenings will occur in 2016, and most short rates will clear 1% by year end. No consensus exists as yet, but the range of expected hikes is between 0 and 6, so why not go with the average? The data is not peaking right now, so we don't see Chair Yellen worried about an overheating economy for some time, and the initial bump of the target rate to a 25-50 bp range will force even the most rampant borrowers to take pause. Undoubtedly, the data or geopolitical scene will soften and the Fed will pause once from an every-other-meeting pace. T-bills, LIBORs, and Prime march higher.

Three increases to the Fed funds target rate (range) will push LIBORs higher throughout 2016, so borrowers will feel a pinch despite a Fed pause. A year after the swap market's soft expectation for short rates was the most precise, we see the Fed's dot plot proving most accurate this year.

2016 Forecasted Levels

Short Rates	31.12.15	Q1 2016	Q2 2016	Q3 2016	Q4 2016
Fed Funds Target	0.50%	0.75%	0.75%	1.00%	1.25%
1m LIBOR	0.43%	0.70%	0.70%	1.00%	1.25%
3m LIBOR	0.61%	0.90%	0.90%	1.20%	1.45%
US Prime Rate	3.50%	3.75%	3.75%	4.00%	4.25%

Historical Data Source: Bloomberg

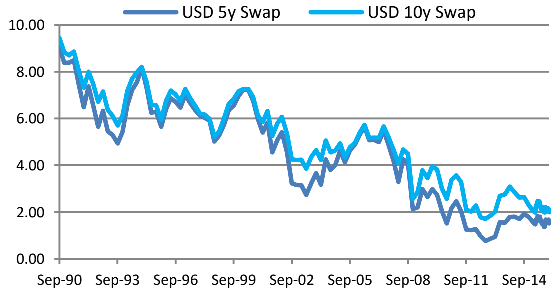
Market Review

2015

How Did Swap Spreads Go So Negative in 2015?

The 30-year swap rate of 2.62% is 40 bps below the 30-year Treasury yield of 3.02% as of year-end. The 5-year swap spread for 3-month LIBOR swaps is -3 bps. Sure, the spell of accommodation from the Federal Reserve has caused those who have money to chase a variety of assets, but how can there be so much pressure on rates that US swap spreads go negative all the way from the 5-year point to the 30-year? The popular culprits: (1) currency gyrations affecting US interest rates, particularly euro and yen weakness and the Chinese yuan revaluation that have been recently rampant, (2) so much relatively lousy credit overseas being bid higher compared to the US, (3) US banks being magnitudes more soluble for the long haul after Wall Street reforms, and (4) swap dealer liquidity drying up from capital constraints and regulatory reflux. All excellent thoughts, but in our mind, the most supportive driver must be that the US rate trade is decidedly one-way, as almost all fixed income investors want floating rate exposure for the long term and almost all borrowers (the other side of the loans and bonds) want fixed rate exposure for the long term. This trade could start to shift in 2016.

We do not believe that swap counterparties, including the collective counterparty of an exchange, are better credits or less likely to fail than the US government, which is one implication of negative swap spreads. Taxing authority over $270 trillion in assets trumps all, and this truth must eventually be priced in, even as balanced budgets and fiscal sanity seem ever farther away for our lawmakers. Also, the dollar strength will persist but probably with less force, and the European Union may turn the corner in 2016 and accept slowing ECB assistance. Our inclination last year was to see this negative spread phenomenon dissipate as short rates rise, and with the latter actually happening in 2016, we still believe spreads will head upward in the back half of the curve.



Swaps exchange fixed or floating payments for one another, and most commercial end users mitigate risk using swaps to hedge cash flows, asset prices, net investments, or debt portfolio valuations. Large commercial banks make revenue by adding spreads to these structures. Please confirm with us that your contemplated structures are in fact appropriate for the risk profile of your organization and that your pricing is reasonable for the risk that your bank is accepting.

Historical 3m LIBOR Swap Rates and 2016 Forecasted Levels

Swap Rates	31.12.15	Q1 2016	Q2 2016	Q3 2016	Q4 2016
2-yr LIBOR Swap	1.18%	1.45%	1.55%	1.90%	2.15%
5-yr LIBOR Swap	1.73%	1.95%	2.25%	2.40%	2.60%
7-yr LIBOR Swap	1.95%	2.25%	2.45%	2.60%	2.75%
10-yr LIBOR Swap	2.19%	2.35%	2.55%	2.65%	2.80%
30-yr LIBOR Swap	2.62%	2.95%	3.10%	3.20%	3.30%

Historical Data Source: Bloomberg

Preview 2016

US Leadership Out Front Again in 2016 for Treasury Market

US Treasuries declined in 2015, a collective occurrence which surprisingly has only happened a handful of times in the past forty years. Declines were led by the 2-year note, as Fed tightening finally came and forced short term rates higher along with it. After amazing buying of the 30-year bond in 2014, the long bond yield rose a quarter-point in 2015, while the 5-, 7-, and 10-year maturities rose a modest 10-12 bps in yield. After extending the duration of the outstanding Treasury portfolio for the past several years, more issuance is expected in the front half of the curve in coming years as longer dated paper starts to cost more. However, we are uncertain that supply and demand will match, and we see new regulatory regimes, a maturing population, and an easily spooked younger investor making more room for emergency capital and less risky assets in portfolios. As such, we expect the yield curve to flatten more in 2016 (it flattened about 30 bps in 2015)—with the potential for some yield inversion in the middle of the curve if the target rate range keeps rising as expected or faster.

Even though we expect the 10-year yield to rise about 50 bps YoY, dragging mortgage rates higher along with it, it would be only a modest surprise if another 2015-style, quiet year came instead. Overseas, yields remain lower (absolutely, as well as relative to their credit risk) than US sovereign paper, and despite overcoming the Greek re-bailout and budget constraints in Europe, the European Central Bank is still in easing mode with GDP stalled, which should keep this anomaly in effect. So even though it lately only happens once a decade on average, we see Treasury price declines and corresponding higher yields again in 2016. The US Presidential election should take the pressure of the news cycle away from every data release and Fed policy statement, but odds-makers anticipate split government and limited agenda advancement on the tax, spending, or energy policy fronts.

Fed tightening should make great debate fodder too! The renewed terror threats globally mean a greater focus on defense, as well as a higher probability for exogenous events to impact financial markets.

While we accurately predicted a continuing yield curve flattening (and expect more of that in 2016), the Fed's solitary 2015 rate hike kept the front end of the Treasury curve lower for longer than we anticipated. Three hikes in 2016 mean pressure at the front, and likely another 50 bp compression in the 2s-10s spread as demand holds long maturities steadier.

US Treasury Yields 2016 Forecasted Levels

Treasury Yields	31.12.15	Q1 2016	Q2 2016	Q3 2016	Q4 2016
2-yr Treasury	1.05%	1.35%	1.40%	1.75%	2.00%
5-yr Treasury	1.76%	2.00%	2.15%	2.35%	2.50%
7-yr Treasury	2.09%	2.30%	2.40%	2.55%	2.70%
10-yr Treasury	2.27%	2.40%	2.50%	2.65%	2.75%
30-yr Treasury	3.02%	3.25%	3.30%	3.40%	3.45%

Historical Data Source: Bloomberg

The Return of a Climbing LIBOR

More Reason to Hedge When Risk Materializes

By the time the S&P 500 bottomed out at 666 in March of 2009, the Federal Reserve's Federal Open Market Committee had already cut the overnight borrowing rate to near zero, and there it stayed for about seven years. With that cut, short term borrowing rates like 1-month LIBOR headed lower, much to the benefit of those who were able to float their interest rates or who chose to hedge cheaply with out-of-the-money-options. 1-Month LIBOR averaged about 0.23% over the last seven years. Well, now that same FOMC has decided the US economy is strong enough to reverse course, and both the Fed funds target rate and LIBORs are on the rise.

This reversal is unlikely to stop, for some time at least. And for those with unhedged loan portfolios, the time is now to revisit the thought processes, likelihoods of refinancing, and overall risk appetite as we enter 2016. From 1970-1990, the Fed funds target rate vacillated around the 10% level. From 1990-2010, it jumped above and below the 5% threshold. The first half of this decade, it has basically been hugging the flat line, so the second half of the decade and the 2020s present uncharted and unknown territory for the Federal Reserve. Discover the costs, get the best available deal (by using a trained, knowledgeable advisor), and prepare to succeed no matter what the future holds. That's hedging.

It's upon us, a rising rate environment. Knowing the cost of derivative exposures in present value terms and over the life of a deal adds an invaluable perspective to the decision-making process. We are here for our clients with the market data, guidance, and modeling tools to help them make smart decisions in 2016 and beyond. Please call us to discuss your portfolio or your current deal any time, and have a fantastic New Year!

Other Movers

Other Movers	31.12.15	Q1 2016	Q2 2016	Q3 2016	Q4 2016
Dow	17,425	17,500	17,800	18,500	19,000
S&P 500 Index	2044	2050	2100	2200	2250
US GDP QQ (ann)	2.0%	1.8%	2.0%	2.4%	2.6%
EURUSD	1.09	1.08	1.05	1.07	1.06
VIX	18°%	15%	16%	15%	14%
Oil ($/bbl WTI)	37	34	45	55	60

Historical Data Source: Bloomberg

Abu Dhabi Water & Power (IWPP) - Design of Optimal Interest Rate Hedging

The Issue

Our client was a JV between ADWEA, TAQA and a consortium of Japanese investors. Prior to engaging Marisk, the Company's debt was 100% floating rate partially hedged to fix at circa 5% across eleven swaps with five international banks for a total notional close to $2bn.

Objectives

We were appointed as independent hedging adviser to work with the client and the debt syndicate arrangers to achieve the following objectives:

- Compile a hedging strategy which both met the hedge requirements of the loan CTA, cost effectively incorporated the existing hedges and which would accommodate:
    - Lender's 75% minimum hedge ratio requirement
    - Comply with the hedging conditions of the Facility Agreement
    - Hedge providers required to meet minimum credit ratings levels
- Recommend the interest rate hedging product – its term, quantum and effective rate paid – in the context of the current market environment and different interest rate scenarios
- Carry out ongoing benchmarking exercises with hedge counterparties to ensure competitive pricing
- Develop an execution strategy to achieve best market execution, while allowing relationship banks the opportunity to participate

Our Approach

The existing hedging was reviewed in the context of the requirements of the loan CTA and the business plan to determine the most appropriate restructuring of the existing hedging. The three alternatives were:

- Blending all the existing hedging into a new hedging strategy
- Retaining the existing hedging and implementing additional forward-starting hedging
- A combination of the two

We produced a brief report which outlined three potential hedging strategies that met with the objective set out and our recommended hedge strategy. The report contained a description of the hedge strategies, clear explanations of pros and cons, indicative market pricing and scenario analysis incorporating different interest rate environments.

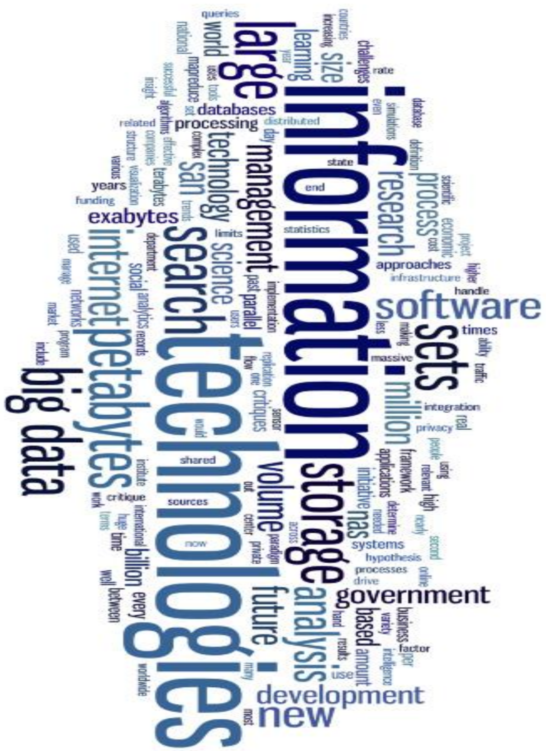
- Utilise Marisk's extensive market knowledge to approach a number of known third party hedge providers meeting the minimum credit rating for indicative pricing.
- Monitor hedge providers' credit ratings
- Recommend a preferred hedge counterparty based on the indicative pricing received and our experience regarding their ability to complete the transaction in a timely manner

The Outcome

By working together with the client, the consortium and the banks, Marisk were able to achieve the following:

- Bespoke hedging strategy to meet the Company's objectives
- Transparent and 'at market' pricing on execution – significant improvement on initial pricing offered from hedge counterparties
- Clear understanding of the hedge strategy
- Regular market updates which kept the client abreast of market movements and allowed tweaking of the hedge strategy accordingly

Riyadh Information Technology – Arranging Flexible Debt Financing Alternative



The Issue

Our client was one of the leading IT infrastructure solutions providers in Saudi Arabia and worked on a tight net profit margin. The Company's contracts were largely with Saudi governments' entities. Payment delays from large clients created liquidity constraints on the company which paid its suppliers within 30-60 days to enjoy substantial rebates.

Objectives

We were appointed as exclusive financial adviser to work with the client and its lenders to achieve the following objectives:

- Arrange flexible financing alternatives to bridge the gap between the realisation of receivables, the need to pay suppliers early and accompany the company's working capital requirements as it grows.
- Approach suitable market counterparties to gauge appetite, pricing and ability to meet time constraints
- Negotiate counterparty pricing and covenant language
- Assist in the negotiation of loan documentation to ensure it was commercially acceptable to the client

Our Approach

Based on our analysis which considered the client's business plan, financials, liquidity, capital structure and the financing requirements, we identified the optimal liquidity strategy. We then worked with the client to structure the financing, the securities in order to ensure it was economic and compliant with the Board requirements. We produced a credit report which outlined two potential financing strategies that met with the objective set out and our recommended strategy.

The report contained a description of the company, its sector of activity a detailed financial analysis, key risks and a financing strategy with clear explanations of pros and cons, indicative facilities term sheet and scenario analysis on key financial ratios.

Compile a term sheet detailing the terms of the requested facilities:

- Utilise Marisk's extensive market knowledge to approach a number of known financial institutions in Saudi Arabia and the GCC
- Recommend a preferred bank counterparty based on the appropriateness, cost effectiveness and indicative pricing received and our experience regarding their ability to complete the transaction in a timely manner
- Coordinate the required compliance documentation to ensure the completion of the financing within the required timeframe
- Next, we coordinated KYC documentation and liaised with the client, our client's audit firm and the lender to ensure the financing documentation was commercially acceptable to all parties.
- Final closing of the financing with NCB-Al Ahli bank

The Outcome

By working together with the client and the banks, Marisk were able to achieve the following:

- Sourcing a new bank counterparty
- Bespoke financing strategy to meet the Company's liquidity objectives
- Co-ordinating the completion of the KYC requirements for the financing implementation
- Cost savings on closing due to finding most competitive counterparty
- Co-ordinating securities and final closing

Transaction Highlights

Hedge advisor: advice and assistance with restructuring and implementation of interest rate hedging transactions to the value of USD 1.7 billion
www.tapco.ae

Debt advisory work relating to the refinancing of banking facilities and sourcing flexible project financing
www.acs.co.sa

Debt advisory work relating to the arrangement and closing of flexible debt financing facilities
www.ebttikar.com

Debt advisory work relating to the arrangement of securities margin trading financing and bank guarantees
www.mubashertrade.com

Contact

MARISK
beyond derivatives

Abu Dhabi

PO BOX 129475
Abu Dhabi
United Arab Emirates

Tel: +971(0)2 672 6177
info@mariskco.com

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