

# Panorama



Global Perspectives on the Debt Capital Markets

*Winter 2009-2010*



BNY MELLON

**Who's helping you?**

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# To the Reader...

With new debt issuance showing tentative signs of renewal in the first quarter of 2010, this winter edition of *Panorama* explores a question that seems particularly relevant to participants in the debt capital markets:

## *What do investors want?*

The question is timely as well as relevant. Economies around the world are starting to show signs of recovery, and there is reason to believe that the increase in issuance may presage an overall upswing in the debt capital markets globally. So we asked four business development heads of BNY Mellon Corporate Trust—responsible for the Europe, Middle East, and Africa region; Structured Credit; Public Finance; and the Asia-Pacific region—to pose the question to key institutional investors in their respective markets.

They did so in virtual roundtable discussions, with each participant speaking from the comfort of his or her private office, and with each discussion moderated by the respective BNY Mellon Corporate Trust business development head. Based on the discussions, each about 45 minutes in length, and after conferring together and identifying both common themes and market differences, the moderators authored this issue's main articles.

The answers the investors gave to the question are illuminating.

Two points in particular light up the discussions. One point is the broad and adamant consensus among these diverse investors—hailing from different parts of the world and expert in varying specialties—

about the key needs they expect issuers to fill. Simply put, what investors want from issuers is transparency, simplicity, and ready access to needed information as the basis of well-documented, explicitly understood transactions. What's striking is the unanimity of this demand, which had top priority among all our roundtable participants.

Equally unanimous is that the global financial crisis of the last 24 months, profound as it was in so many ways, did not shake the faith of these investors in the merits of a fundamental investment approach based on bottom-up analytical work. If anything, in fact, it reconfirmed the investors' faith in the basics of that approach.

The second point these investor discussions illuminate is the diversity of emphasis from roundtable to roundtable.

Investors in the EMEA region, for example, see the global financial crisis as a call for the standardization of issuance documentation as a way of achieving the kind of transparency that will incentivize ongoing investment.

Among investors—and in this case, an attorney as well—who are experts in structured products, there is the sense that it will take a while for some of the asset classes that

seemed so vital before the crisis to return to viability.

Our roundtable on public finance found investors emphasizing both the importance of systems and servicing *and* the need for person-to-person contact between issuers and investors.

And investors in the Asia-Pacific region, noting a growing trend of investments diversifying away from banks and toward the debt markets, suggested that issuers identify and target their specific investor base in a widening investor universe.

Put together the consensus and the separate emphases demonstrated in these roundtable discussions, and you have a profile of investors ready to do the hard work institutional investing requires in the debt capital markets—and challenging issuers to respond. It bodes well for the tentative resurgence of debt issuance—and for the continuing health of the debt capital markets in 2010.

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# Renewing the Debt Capital Markets: A Widened Role for Trustees

**By Scott Posner**

Chief Executive Officer  
BNY Mellon Corporate Trust

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What role can a third-party trustee play in helping to renew or revive the debt capital markets?

By definition, a trustee carries out the essential role of supporting debt transactions, helping issuers navigate the debt capital markets and ensuring that bondholder interests are protected. In fulfilling this role, the trustee performs functions that facilitate the orderly workings of the debt markets.

Over the past few years, however, the workings of the debt markets have seemed anything but orderly. In trustee markets in the U.S., issuance is down 52 percent from its peak in 2005. Elsewhere in the world, the same period saw levels of debt issuance trending downward. While 2010 has started off with something of a renewal of debt issuance activity globally, the situation remains fluid.

## **New Issuance**

Real recovery will come only when the global economic upturn that is now stirring picks up enough steam to fuel a new wave of capital-raising. Once that happens, investors looking for places to put their money will find plenty of opportunities in debt issuance.

Following this particular global financial crisis, however, investors returning to the debt capital markets seem to be seeking some changes. In the pages that follow, you will read what investors are asking of issuers as a recovering global economy brings them back to the debt capital markets—namely, more information, fuller disclosure, simpler and more standardized investment structures, more communication, and greater attention to investor needs. These are reasonable, thoughtful requests that deserve to be heard by issuers around the world.

BNY Mellon Corporate Trust is uniquely positioned to deliver this message and to help support the investor-issuer communication so important to the revival of vibrant debt capital markets. You are holding in your hands one of the ways we do that—by publishing *Panorama* and thereby giving voice to participants in the market and keeping the discussion among them active and substantive.

In fact, I believe that the trustee's role will increasingly require feeding and maintaining those lines of communication that can be so important in reviving and strengthening the operational activities of the debt capital markets. And I believe it will require four ingredients in particular to do that work successfully—expertise, collaboration, innovation, and leadership.

### The Four Ingredients for a Trustee in a Revived Debt Market

First, the well of expert capabilities that will be needed to support investor calls for more detailed information and for simplified structures is both wide and deep. Even standardization—of documentation if not of structure—may ease the process for the investor, but the volume and scope of knowledge and skill needed will still be a tall order for issuers and for those providing them trustee services.

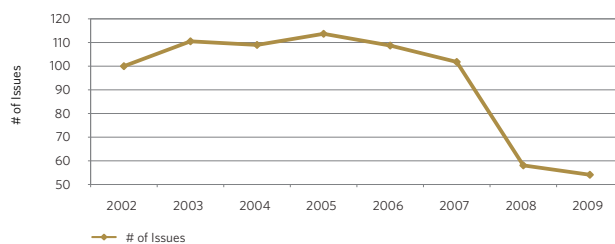
Second, I believe trustees will increasingly be called on to engage with their clients in a collaborative, consultative fashion. The days of automatic, almost reflexive service delivery are over. We trustees must listen well to our clients; we must “connect” with them as we offer tailored solutions that can help them achieve their strategic aims.

Third, the revival of issuance activity in a renewed debt capital market will increasingly require a commitment to innovation. No market can sustain momentum without regenerating itself over and over. That means the kind of fresh solutions that emerge from that collaboration with clients I just described, and it means investment in the tools and technologies that can keep clients in step with, if not ahead of, market shifts.

Finally, it comes down to leadership, measured not only by industry rankings, but by qualities that include a record of performance, financial strength and stability, vision and a willingness to act on vision—even when it means breaking with convention.

In bringing all this to the clients we serve, trustees will benefit both issuers and investors. We will also be playing our indispensable role in strengthening the connection between the two and thereby helping to revive the capital markets that are so essential to the world of finance.

United States Trustee Markets Issuance



Includes US domestic municipal, corporate, and structured debt.  
Source: ThomsonReuters



# Europe's Investors Tell Issuers: 'Make It Clear, Keep It Simple'

**By Michael Whelan**

Head of Business Development  
Europe, Middle East, and Africa Region

## Roundtable Participants:

**Andrew Littell**

Chief Operating Officer and Head Trader  
Resource Europe Management Ltd.

**Craig MacDonald**

Head of Investment Grade Credit  
Standard Life Investments

**Rob Reynolds**

Chief Investment Officer and Senior Portfolio Manager  
Resource Europe Management Ltd.

**Paul Tapper**

Director and Portfolio Manager  
Egret Management LLP

**Marcus Wilhelm**

Senior Pension Consultant  
Siemens Financial Services GmbH

Transparency and simplicity and more of both: That is what a representative sample of Europe's institutional investors wants and expects from issuers as the global economy continues what panelist Rob Reynolds called its "slow recovery mode."

Hailing from a range of the continent's financial institutions, the five investment experts concurred that, as Egret's Paul Tapper put it, "transparency in discussions with investors and also in how the structure works and in documentation is absolutely essential," as is "simplicity in documentation and structure." With investors themselves feeling the pressure of increased oversight, they will be applying greater scrutiny to and demanding greater simplicity from debt issuers. And as all the panelists agreed, if issuers don't provide those two essentials—simpler investment structures and a clear window into underlying collateral, covenants, ratings, and other aspects of an investment—then, in Tapper's words, they just won't be "successful in raising funds."

## Investment Approach: 'No Dramatic Change,' But More Diligence

But this doesn't mean that the crisis has transformed the basics of investment behavior. In a wide-ranging conversation with panelists in Edinburgh, London, and Munich, the recommended modifications articulated by the five panelists were more of format than fundamentals. Resource Europe Management's Andrew Littell and Egret's Tapper, for example, both report a shift in focus to trading in discounted assets, "buying into a rising market," as Resource Europe's Reynolds puts it. At Siemens Financial Services, pension consultant Marcus Wilhelm describes revisions to the firm's value-at-risk

model that add a short-term analytical perspective to the traditional long-term view in order to get what Wilhelm calls “earlier signals.” Standard Life’s Craig MacDonald, acknowledging that “in hindsight, there could have been a greater focus on liquidity,” says there has been no “dramatic change” to his firm’s basic model for managing fixed-income credit instruments. “The key drivers have been the same for credit in this market as they have been in other bad times,” says MacDonald. “Does the business model work? Does the quality of management work? What is the strength of the cash flow?”

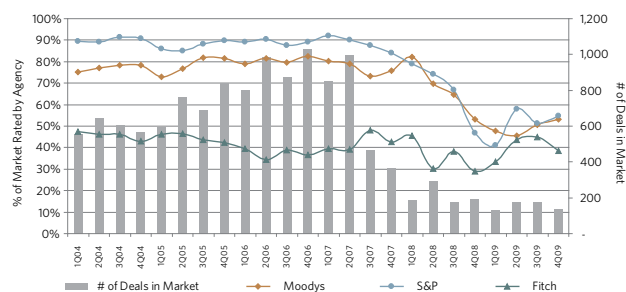
What’s clear from the discussion is that investors have raised the stakes on how they explore those questions and what they will accept as satisfactory answers. Scrutiny in general will be closer and more persistent, the focus on risk will be tighter and sharper, and some asset classes freely invested in before the global financial crisis might not make the cut in the wake of the crisis. But like their counterparts around the world, Europe’s investors see this as something positive—the crisis serving as a sobering reminder that it is time to return to those textbook practices basic to investing that seem to have been marginalized during the boom years of the recent past.

### ‘The More Transparent the Better’

Transparency is the overriding demand, and it covers information about everything—portfolio positions, underlying assets, ratings, documentation, compliance, and more. Concern about “relatively thin information” from some issuers pre-dates the global financial crisis, says Egret’s Tapper, who finds as an investor that he often must initiate requests for information but concedes that when he does, the information he seeks is forthcoming “in quite a useful format.” Going forward, says Tapper, “any borrower that wants to change a term or condition in his deal now realizes that he has to be far more transparent about what’s going on in his business.”

On every front, says MacDonald, “the more transparent the better.” But where asset-backed deals in particular are concerned, the level of transparency needs to rise “quite significantly.” Without complete and comprehensive transparency, investors can too easily find that their ability to act has been undermined. This is

**Percent of Global Structured Deals With Rating**  
(By S&P, Moody's and Fitch)



Source: Asset Backed Alert

exactly what happened in the asset-backed market. “A number of investors now own an underlying asset rather than a triple-A monoline wrap, and they don’t really know what that asset is,” asserts MacDonald. “And they’ve got no real leverage to improve transparency.” That must change, MacDonald declares; investors must have dependable “information on the underlying ratings, performance indicators,” and more. Pension consultant Wilhelm says Siemens looks for transparency on exposure issuer by issuer, and he adds: “We expect our global custodian to give us a view on that.”

At the same time, the investors are sensitive to issuers’ need to maintain confidentiality of information. Resource Europe’s Andrew Littell cites premature leaks of Collateralized Loan Obligation (CLO) shadow credit ratings that made their way into the public domain—with obvious inappropriate impact on the market.

How to reconcile the two demands—transparency and confidentiality? MacDonald asserts that issuer-investor communication is key. “Ongoing regular communication in the good times provides a level of confidence in the bad times,” he says. “We have always penalized companies that we meet only when they want to sell us debt.” While transactions in the debt capital markets can be short-term, our European panelists seem to affirm the need for long-term communication among participants.

What role would such one-on-one communication leave for rating agencies, once seen as key players in ensuring transparency? Among the European investors as among their global colleagues, rating agencies come in for their share of criticism. Littell noted what he called “a lag between performance and the up-to-dateness of a credit rating.” As his colleague Rob Reynolds put it, “that’s a potential exposure for us if we have to wait three weeks to a month for a rating estimate.” Others agreed that the credibility of some rating agency judgments had proven to be “questionable” and that substantive discrepancies between ratings of different agencies were “awkward.”

But there was also general agreement that credit ratings play a “helpful” role and are “integral” to the process, as Reynolds expressed it—so long as it’s understood they comprise only one component of the due diligence process.

As to shadow ratings, the inherent inconsistencies in the shadow system—rating estimates varying from one agency to another, and ratings available only to a select audience—mitigate against investor confidence. It’s the reason why “more public ratings will probably be helpful to investors going forward,” according to Paul Tapper, while his fellow panelists concurred that borrowers “will be pushed towards public ratings” in the future.

Bottom line? There may be nuanced differences in their specific perspectives, but Europe’s investors are in fundamental agreement that more information, in more detail, more readily delivered is a *sine qua non* of a renewed debt capital market.

### **Simplification—Via Standardization**

One key way to achieve such transparency, as our panelists enthusiastically and unanimously agreed, is through simplification of both deal structure and documentation.

All the panelists expressed reservations about what Marcus Wilhelm referred to as “fancy” deals—the kind of market value-based structures that unraveled in the global financial crisis, with such profound consequences. The group’s sense of caution in dealing with such structured credits at any time “has just been further enshrined in our thinking,” says Paul Tapper.

But investors don’t just want simpler structures, Tapper goes on; “they will want to see more standardized structures—in particular in the CLO market.” There, the sheer diversity of documentation has proven “exceedingly complex,” says Tapper, and for some managers who juggle numbers of CLOs, “it’s frankly too complicated.”

That situation “absolutely has to change,” echoes Andrew Littell. “Critical things like where you draw the line and how you interpret what defines a triple-C asset clearly differs” from manager to manager.

“Drawing lines” would seem to be an idea whose time has come. Today’s new pension mandates, to take just one example, typically prescribe restrictions and exposure caps. Such requirements constitute a step toward the kind of standardization that Littell sees as “probably the way forward for the next generation of CLOs.”

## Oversight

The glue that must hold together these new levels of transparency and the simplifying of structures and documentation is the oversight process. This is particularly pertinent given the general consensus among panelists that any regulatory reform is likely to be indifferent, if not insignificant. And oversight scrutiny, all the panelists agree, has increased markedly over the last two years as a direct result of market volatility and is expected to continue to be intense going forward.

Both external and internal oversight are affected. Externally, regulators are asking for more, although, says Paul Tapper, "I'm not quite sure where it leads." Client oversight has also become more intense—"the level of scrutiny has increased," as MacDonald puts it. Perhaps more significant has been an expansion of client scrutiny from simple assessment of performance to real feedback and more back-and-forth involvement in understanding such things as downgrades. This may be a signal that the idea of ongoing investor-issuer communication is being taken seriously—and is here to stay.

Internal audit and compliance oversight, the panelists agreed, has not changed in fundamental structure but, like external oversight, has also become more intense. Oversight resources have been added; there is more governance in the sense of more people involved, more meetings held, more reports required. The impression is not just that oversight has risen to the top of the senior management agenda, but that it has become a more expansive topic as well, covering more issues more frequently and with sharper scrutiny.

## 'Something of a Renaissance'

Looking ahead, panel participants agree that we are entering "a new era of austerity," in Rob Reynolds' words. All concurred that leverage would continue to come down. Yet despite the profundity and scope of the global financial crisis, none of the panelists was unfamiliar with its effects. As Reynolds said, "I remember the last cycle."

But if all believe the impact of the crisis will fade, all affirm that the lessons about transparency and simplicity must endure. Paul Tapper put it this way: "The managers that will be successful in raising funds will have to provide transparency and simplicity... Without it, people will question why they should do something that has previously blown up in their face."

When issuers can rise to new levels of transparency and simplicity, however, Europe's investors believe the debt capital markets are on the way to what Rob Reynolds describes as "something of a renaissance—from a lower leverage platform, where credit gets paid, and there is appropriate return for the risk being taken: a better credit investment environment in the next two to three years."



# Structured Finance in the Americas: The Comeback Will Take Time

**By Jean Wynn**

Head of Business Development  
Structured Credit

## Roundtable Participants:

**Randall S. Bauer**

Senior Portfolio Manager  
Head of Structured Products Group  
Federated Investors, Inc.

**Arvind Rajan**

Head of Quantitative Research and Risk Management  
Prudential Fixed Income Management

**Thomas Teles**

Head of the Mortgage & Asset-Backed Securities Team  
Goldman Sachs Asset Management

**Jonathan Zonis**

Partner  
Clifford Chance LLP

The global financial crisis saw structured products in particular suffer a loss not just of value but also of credibility. It is mostly because of that latter loss, say four experts, that it will take time for certain asset classes to re-emerge as healthy, viable investments. Even then, a new model for fixed-income investing will be needed, one requiring greater simplicity, enhanced transparency, and more rigorous standards than prevailed before the crisis.

Still, there is unanimity among the four—senior portfolio management executives at three pre-eminent asset management institutions and a lawyer specializing in structured debt legal documentation and practices—that the new model will not re-draw the fundamentals of investment approach, and that it will neither limit nor restrict the range of asset classes that investment professionals will seek out. “While the landscape may have altered radically,” says Prudential’s Arvind Rajan, “our approach has not. We would look at any investment opportunity provided it is appropriate risk-wise and attractive.”

## Lessons Learned, Adjustments Made

For these experts in structured debt, by definition and character among the most complex and complicated transactions in the world of finance, the unraveling that began in 2007 only confirmed the obvious—that this is a business best executed by professionals. Structured securities are a realm in which “transparency of collateral performance and structure is paramount,” in the words of Tom Teles of Goldman Sachs Asset Management (GSAM). That is why, Teles says, “we avoid transactions where we can’t model the cash flows or where we receive limited information regarding collateral.”

In short, this is a business that can be unforgiving of imprecision or blurred understanding. Yet, as Arvind Rajan put it—and as is widely known—“mainly on the strength of ratings, investors who didn’t understand how to analyze structured finance” at all were in the market in great numbers, investing in difficult-to-analyze vehicles ranging from collateralized debt obligations (CDOs) to structured investment vehicles (SIVs).

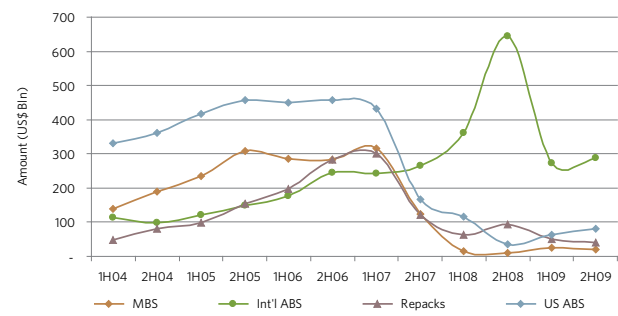
Federated’s Randy Bauer recalls “a period where investors, because of the expansion of the financial-system-wide leverage, were in a position to make so many securities purchases that at some point they ceased being sufficiently demanding about what they wanted, and so they got what they asked for”—structured deals they did not fully explore nor understand—with unfortunate results both for many of those investors and for the market as a whole.

Ironically, says attorney Jonathan Zonis of international law firm Clifford Chance, whose clients are mostly Brazil-based, the converse confirms the point. The emerging markets where, typically, “we don’t see a lot of structured products” survived the global financial crisis “relatively more unscathed than the developed markets,” says Zonis. And part of the reason there has been “more reticence to add layers of structure” in the Brazil market, for example, “even if there might be some benefits to doing so,” is simply that the disclosure process seems so arduous to issuers. Now, says Zonis, the market is appreciating that “transparency with investors can certainly benefit issuers.”

For all the professional investors on our panel, wariness vis-à-vis structured products has long been the watchword. Yet the battering those products took in the global financial crisis prompted all to implement still more adjustments in the way their organizations look at risk while affirming that, in Teles’s words, the basic “approach to investments and investment risk has not changed.” At GSAM, Teles reports, “we now classify more bottom-up security risks as macro top-down risks” in response to the “increased volatility across asset classes in 2008” and the generally “unprecedented environment of the past 24 months.”

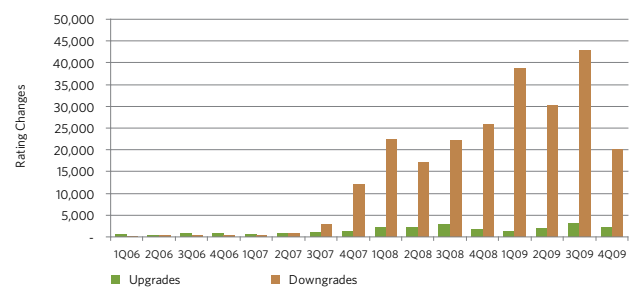
Federated, says Randy Bauer, has also tweaked its risk analysis process while continuing to validate its overall investment approach. “We didn’t stop buying structured

**Global Structured Market Activity**  
(By Security Type)



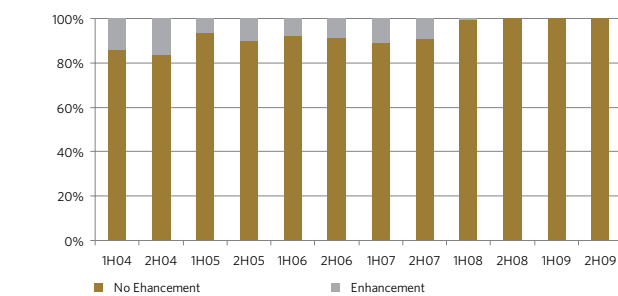
Source: Asset Backed Alert

**United States Mortgage Securities Upgrades/Downgrades**  
(By S&P)



Source: Bloomberg

**United States Public Structured Debt Volume**  
(Enhanced vs Non-Enhanced Deals)



Percent of US public ABS deals issued with a credit enhancer known to Asset Backed Alert.  
Source: Asset Backed Alert

products in 2008,” says Bauer. “We just bought the ones that we thought we could be comfortable owning... That’s what we did before the—call it the ‘leverage overshoot’—and that’s what we do today...in the context of a massive technical occurring in the marketplace.”

At Prudential Fixed Income Management, according to Arvind Rajan, both portfolio and risk management have responded to what he calls the “challenges and relative value opportunities arising from the divergence between fundamentals and market technicals.” So in their risk analysis process, Prudential’s fixed-income managers address mark-to-market risk and “the underlying fundamental risk, looking for vulnerabilities and exploitable gaps.” And given that “the asset class fundamentals have changed quite a lot over the last couple of years on the underlying collateral,” the risk managers and the Structured Finance Group of Prudential Fixed Income Management have incorporated these changes into their models—changes in the housing market when it comes to residential mortgage-backed securities (RMBS), for example, or the extension risks inherent in commercial mortgage-backed securities (CMBS). The approach, however—multi-dimensional risk analysis—remains consistent.

### Getting Needed Information

The issue is information—reliable, pertinent, in the right level of detail, and at the right depth of transparency to ensure that nothing is being either consciously or unconsciously dismissed or obscured. This means that the source of information as well as its content must always be evaluated and assessed. Like their counterparts around the world, these structured finance experts have reservations about the use of credit-agency ratings when it comes to understanding structured products.

As a lawyer, says Jonathan Zonis, he tries to “diminish their level of importance” in disclosure documents, but he concedes that ratings constitute a “very enticing... and user-friendly” shorthand for investors. It is that very convenience factor that Arvind Rajan instances as having damaged “the whole process of securitization.” There was once “a tremendous economy of scale allowing a few rating agencies to determine the safety of securities,” Rajan explains, “thus enabling those securities to be sold to a much larger and less

sophisticated investor base.” That larger market is now greatly diminished, and “those investors are basically out of the system because the system itself has been damaged by the blind reliance on ratings.” So while aware of ratings, all the organizations represented on our panel evaluate transactions internally. Says Randy Bauer: “At the end of the day, you have to do your own work... That’s the responsibility of the portfolio management people at every shop.”

The responsibility embraces finding information, assessing its quality, and only then evaluating it for investment purposes. The first essential, therefore, is that all the pertinent information is available. When assessing RMBS deals, for example, says GSAM’s Tom Teles, “for most deals, we can find the loan-by-loan details on the collateral, but where it’s not available, we tend to avoid those securities.” A second essential is timeliness, which, notes Rajan, is frequently an issue; CMBS information might be “lagging the market in terms of recognizing changes in net operating incomes and debt service coverage ratios,” for example. For all these reasons, *caveat emptor* remains the prevailing principle. Relying on a range of sources and validating as best they can the information they gather are core in-house functions for these investors—and where the source is iffy or the validation difficult, they simply do not buy. As Federated’s Bauer puts it: “Structure can make up for a small hole in an information set, because you’ll never have perfect information on everything.” But structure can’t compensate for serious deficiencies: “We’re certainly not going to say, ‘Gee, I don’t know what’s in it, but I have 50 percent enhancement so I’ll buy it anyway.’... Structure always has to be analyzed in conjunction with content.”

### Which Structures?

What does all this mean for structured products now and in the future in a region where such products once were so firmly established? For these professional investors, who had always shown caution about structured products, there is no “sea change,” as Bauer says; “it’s just a reinforcement of the things we’ve done traditionally.” What he calls “the terminally damaged securitized asset classes like ABS (asset-backed securities) CDOs”—particularly highly engineered

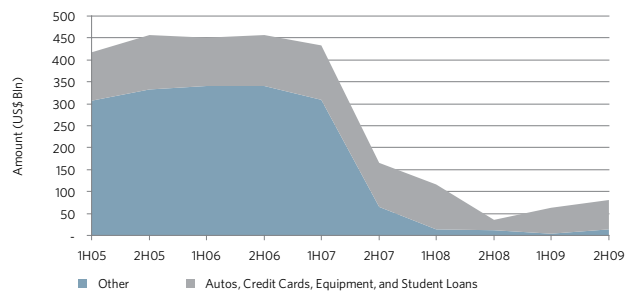
instruments like CDO-squareds and hybrids combining cash and synthetic CDOs—“were never any material part of our investment portfolios.” They are likely to continue to be excluded in the future in favor of what Bauer calls “the classic traditional asset classes: the cars, the cards, to a certain extent the equipment finance, the student loans.”

The outlook for mortgage-backed securities is similar. “With respect to non-agency RMBS,” says Arvind Rajan, “the reason we haven’t had a revival of the new issue market is because this is perhaps the sector that was most damaged in the pre-crisis days.” The “damage” came through “including loans that shouldn’t have been made in securitizations, and then layering all sorts of structures that few knew how to analyze, such as ABS CDOs, on top of those ABS.” And with the Federal Reserve seemingly poised to end its purchases of agency mortgage-backed securities, and little appetite for non-agency products on the private side, “it is going to take a while for the market to regain its footing,” Rajan says.

Jonathan Zonis sees investors looking elsewhere for opportunities—to covered bonds, a “relatively simple structure” common in Europe, and to lower-grade credits coming to market from the emerging markets, especially as dollar debt becomes increasingly attractive.

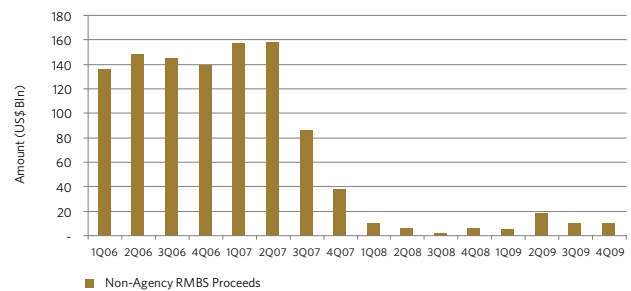
But no one is writing off structured finance. “It’s not to say we would never consider another CLO,” says Bauer, nor refuse to invest again in RMBS. But the bottom line is that structures have to get better, and, in Rajan’s word, “the environment” has to change. Specifically, the market must ensure more rigorous underwriting standards, stringent fraud detection programs, correct pricing, transparency, efficiencies in servicing, and “skin in the game” at the origination stage. In addition, says Bauer, investors must be confident that the reasons for an investment “are not to feed a massive leverage machine” but are “for real investment by professionals who understand the asset class and can be comfortable investing in it.” And he adds: “Right now, those conditions do not exist.”

### United States ABS Issuance (Volume by Collateral Type)



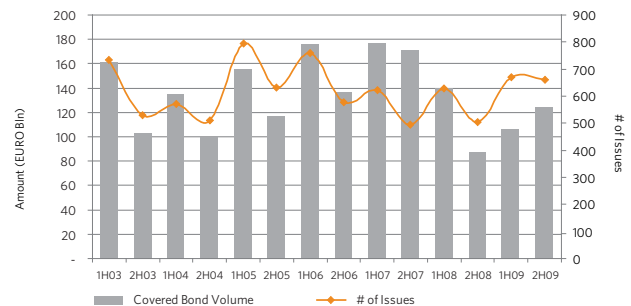
Volume of US public and private ABS deals backed by autos, credit cards, equipment, and student loans.  
Source: Asset Backed Alert

### Non-Agency RMBS Issuance



Source: Asset Backed Alert

### Global Covered Bonds (Funding Activity)



Covered bonds, as defined by Bloomberg League Tables, include Pfandbrief issuances.  
Source: Bloomberg

## Oversight: Persistent and Expert

When such conditions do exist again, they will be persistently monitored through oversight, which GSAM's Teles calls "a key control function in our business"—as it is universally in all the organizations at our roundtable.

What's essential with oversight, asserts Arvind Rajan, is that it "should be conducted by professionals close to the market" in order to make it possible "to adjust quickly to changes in the economy and the market, and to regulatory regimes." Rapid response is key; like time and tide, the capital markets wait for no one, and assessing every market shift to identify and quantify its risk is an urgent necessity that requires "both a qualitative top-down process and a rigorous bottom-up quantitative framework." Past experience provides only limited insight, Rajan continues; "each crisis is going to play out differently... You can't apply a cookie-cutter approach by just looking at previous scenarios or crises. You also need to be on top of developing risks in today's market."

And where the market for structured products is concerned, what's happening is simple: Structures need to improve if the market is to revive, and that is likely to take time.



# Public Finance: Investors Will Drive Market Renewal

**By Mark Brown**

Head of Business Development  
Public Finance

## Roundtable Participants:

**Thomas Gamello**

Municipal Research Group Manager  
BNY Mellon Cash Investment Strategies, a division of  
The Dreyfus Corporation

**Colleen Meehan**

Director of BNY Mellon Cash Investment Strategies, a  
division of The Dreyfus Corporation

**Mary Jo Ochson**

Chief Investment Officer for Tax-Exempt Money Market  
and Municipal Bond Investment Groups  
Senior Portfolio Manager  
Federated Investors, Inc.

Effective systems, policies, and procedures. Experience in the market. Due diligence based on the latter and facilitated by the former. These—the very attributes that enabled major public finance investors to “manage through” the global financial crisis—are the keys to successful investing in the municipal market going forward. That is the common theme expressed by representatives of two of the nation’s leading investment firms specializing in municipal finance.

But these experts add another ingredient to the recipe for a viable, vibrant market in the municipal space, citing what they suspect and hope will be an emerging trend—namely, issuers taking the initiative to consult with investors as part of the process of structuring an issue. “Everybody is working together a little bit better now,” says Colleen Meehan of The Dreyfus Corporation—a development all of our panelists see as a positive sign for public finance investment in the future.

## Tested and Validated

Although the panelists all agreed that the municipal market has been buoyed by the government-backed Build America Bond (BAB) program, which has both extended the market and limited bond price deterioration, BABs have been but one bright spot in an otherwise difficult market. In fact, as Meehan recalled in the discussion, this is a market that has been particularly bruised by the financial crisis, suffering the collapse of the auction-rate securities market in 2008 as well as the global credit crunch. Conservatism of investment philosophy, the philosophy followed by both investment firms represented on our panel, Dreyfus and Federated, could not by itself have “saved” these investors during the turmoil of the past few years. Rather, it was, in the words of Federated’s Mary Jo Ochson, “the policies and procedures that we already had in place and that we’re very glad we had in place.”

At Federated, that meant a collection of risk committees—on derivatives risk, counterparty risk, credit risk, and more—that met daily and sometimes several times a day, as needed. At these meetings, experienced professionals were able to “go through all our exposures firm-wide and department-wide,” see the situation exactly, and, empowered by the firm’s systems infrastructure, respond appropriately. The result was that it was “relatively easy for us to adapt to the crisis,” says Ochson.

The same was true at Dreyfus, which, like Federated, stayed the course on its “conservative investment philosophy” throughout the crisis. The systems capabilities underlying firm-wide processes and procedures enabled rapid and effective responses to the crisis, says Colleen Meehan. A pre-trade compliance system, post-trade compliance system, diversification systems, reporting systems: As with Federated, Dreyfus, in Meehan’s words, “had the systems in place to be able to manage the risk.”

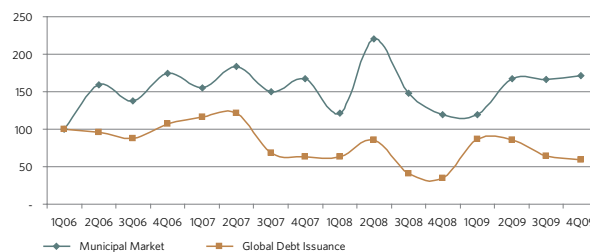
And those fierce early days of the crisis tested the systems as never before. “It was a crazy time,” Meehan recalls. “There were downgrades every Friday afternoon. But because we had those systems in place and had all the reporting capabilities, basically, everything worked.”

Ochson concurs wholeheartedly. “I don’t know what we would have done, actually, if we hadn’t had these things in place,” she says. “You had to have a state-of-the-art system that could show you your exposures in a heartbeat... You had to be able to see what you owned immediately.”

They could, and they did—and as a result, there was not a single put contract that wasn’t honored.

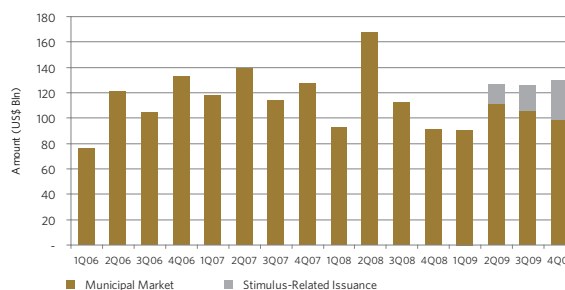
For both these investment management firms, the point is clear: The systems and processes had to have been in place before the fact of the crisis. The daily meetings at Federated at the height of the crisis worked smoothly because of the normal practice of weekly meetings; Dreyfus’ technology-based reporting systems worked reliably in a time of tumult just as they worked reliably on a daily basis. The sustained investment over time in technology-based systems and in experienced people

**United States Municipal vs Global Issuance**  
(Indexed to 1Q06 Issuance Levels)



US municipal debt compared to global debt issuance (excluding US municipal debt) indexed to 1Q06 issuance proceed levels. Source: ThomsonReuters

**United States Municipal Issuance**  
(Issuance Proceeds)



US municipal issuance. Stimulus-related issuance includes Build America Bonds (BABs), Qualified Zone Academy Bonds (QZABs), Clean Renewable Energy Bonds (CREBs), and Qualified School Construction Bonds (QSCBs). Source: ThomsonReuters

to make use of the systems was returned a thousand-fold when it counted. The crisis didn't change these investment management firms' behaviors; it validated their worth.

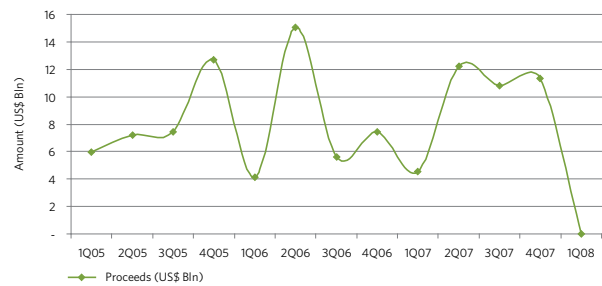
### Independent Due Diligence

Perhaps most potently validated was the practice of individual firms doing their own due diligence—a value shared by these investors' colleagues around the world. As throughout these roundtables, the message for issuers is clear: More information, in more detail, delivered with greater timeliness is going to be an increasingly urgent requirement going forward. This demand for comprehensive transparency is pertinent because, as Ochson points out, only some nine percent of the municipal bond market is now insured versus 50 percent before the crisis. In this regard, credit-rating agency ratings will remain “a piece of the puzzle,” in Meehan's words, but they will be only that—one element in a tapestry of needed information. The same is true of liquidity facilities and bond insurers; their word on an issuer will be duly considered, but it will not take the place of an investor's own assessment of the issuer's credit-worthiness.

There's little give on this issue of transparency. As explained by Tom Gamello, municipal research group manager for Dreyfus, it's a binary equation. “If we're not happy with the initial disclosure document and can't get what we need from the issuer, we're willing to pass on the issue.” Moreover, “if investors and potential investors have an opportunity to work on the continuing disclosure documents,” Gamello goes on, that's when they can “indicate to issuers up front the type of information that must be disclosed.” If it is not forthcoming, Gamello says, Dreyfus will pass on the security—something that “happens more than it used to.”

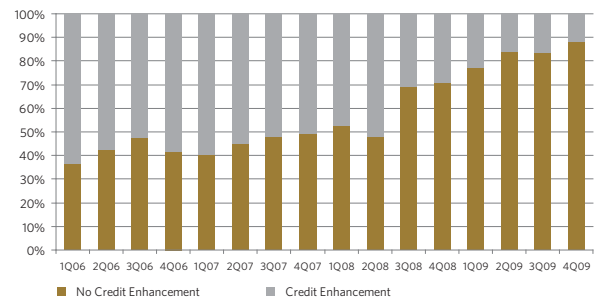
And yes, the disclosure demands are becoming more stringent. For example, Gamello cites the “need to see the standby bond purchase agreement *in toto*,” something that investors were historically content to accept in summary form in the official statement. Investors also want covenants with no slack and tightened requirements for debt service reserve funds.

**United States Municipal Auction Rate Securities Issuance**  
(Funding Activity)



Source: ThomsonReuters

**United States Municipal Credit Enhancement Trends**  
(Amount with Enhancement)



Source: ThomsonReuters

Bottom line? As independent investor reviews of credits grow more detailed and more rigorous, information demands on issuers are also growing, and as these investors are frank to state, the timeliness of issuer response is as important as the content of the information. “If we are not going to have time to review the document, and the underwriter says ‘We’re going to price it,’ we’re willing to say that our due diligence isn’t complete”—and to pass on the issue, says Gamello.

What does the due diligence consist of, and what tools do investors use to perform it? “We look at the structure of each issue,” says Colleen Meehan. In doing so, credit-agency ratings can play a “helpful” role, but, like their colleagues in all our roundtables, the public finance panelists expressed concerns about the timeliness of ratings.

Yet in what may be a helpful hint for the rating agencies, Federated’s Ochson, while concurring that staleness of ratings has been an issue, also believes that the agencies have been charting a new course and “seem to be moving in the right direction.” She cites in particular their “special reports” and the fact that “they’re trying to do more outreach;” they seem “actually to want to talk to the investors before they come out with criteria.” Meehan cautiously agrees that such initiatives may enhance the credibility and usefulness of ratings. “As long as you’re doing the rest of the work,” she says, looking to ratings as “another piece of information” can indeed be helpful.

But doing “the rest of the work” independently is essential, the panelists concur, and it is an ongoing job that engages both of these investment management organizations as they seek new and better ways to evaluate investments in the municipal market.

### **Tightening the Rules**

The job is likely to be further stretched by what the panelists agree are increasingly exacting regulatory reforms. “In our little muni world,” says Federated’s Ochson, “you’re starting to see the SEC get a little bit more involved again in disclosure.” The trend is a tightening one, as our panelists agree: “They’ve been going along that path for quite some time,” says Meehan. She cites a move toward more rigorous

standards for risk-limiting conditions “within the money market fund industry,” while Ochson offers the observation that “they’re trying to shorten things like notice period.”

The panelists see some of the proposed rule changes as closing the barn door after the horse has escaped, and they are not yet convinced that the new disclosure demands being put forth will have the desired effect. “More isn’t always better,” says Ochson. Investors, she maintains, would like to see more consistency of presentation across financial statements, “not just more financial statements.” It’s the quality of the disclosure that counts, she goes on—and to see it “in a format in which you can easily compare one to the other.” But rather than see such standardization mandated in regulation, Ochson thinks it will come from “investor discipline.” Gamello agrees. It is investors, he says, who “have driven a lot of the improvements we’ve seen.”

### **Investor-Driven**

Investors will continue to do so, the panelists believe. “The more that people demand certain covenants,” says Ochson, “the more they demand certain information—like a purchasers’ council to go through really complex documentation—the better. And I think we’re moving that way.”

At the same time, the panelists see issuers making the right moves in terms of “strengthening covenants and enhancing security features,” in Ochson’s words. “You now tend to see debt service reserve funds on the bond side funded with cash—not just a promise to fund them.” To the extent issuers enhance such security structures, say the panelists, they will also enhance their ability to tap the municipal market.

Perhaps even more significant, Meehan cites issuers who, as they put together an issue, “are actually getting the investors’ comments on what works, what doesn’t work, liquidity providers, maturity duration, and things like that... Everybody is working more as a team,” and such teamwork, the panelists agree, is essential for renewing a public finance investment environment that is vital and rewarding for all its participants.

# A Message for Debt Issuers in the Asia-Pacific Market: Target Your Investor Base

**By John-Paul Marotta**  
Head of Business Development  
Asia-Pacific Region

## Roundtable Participants:

**Chetan Baxi**

Chief Operating Officer  
SC Lowy Financial Services

**Frank Kwong**

Head of Debt Syndicate for Asia  
BNP Paribas

**Michel Lowy**

Chief Executive Officer  
SC Lowy Financial Services

For the debt capital markets in the Asia-Pacific region, the outlook is decidedly bullish. “Investors are keen to buy,” as Frank Kwong puts it; participation is up; the credit markets have re-started; and the economy as a whole is growing and in need of capital. For issuers ready to fulfill investor needs, the prospects are certainly favorable, say our roundtable participants—especially for those issuers prepared to target a specific investor base.

Hong Kong-based Kwong of BNP Paribas regards as a “positive” sign the considerable number of transactions that have come to the market—each of them “very well oversubscribed by investors.” As interesting as the number of investors is the “investor composition... relative to what we’ve seen pre-credit crisis.” Specifically, Kwong notes the heightened interest from private banks—relative to somewhat diminished enthusiasm from commercial banks. And SC Lowy founder and CEO Michel Lowy adds that geography also plays a role. “We’ve experienced problems with onshore-offshore investment structures,” says Lowy, “and as a result, investors are more comfortable with countries such as Japan and Australia, where outcomes are more certain.”

Still, investor interest in debt capital is on the rise overall across the region. What accounts for the increased interest? Frank Kwong cites “diversifying away from the banks,” both as an after-effect of their troubles during the global financial crisis and because issuers want longer dated funding and will “look to the debt markets to finance” that funding. Merger-and-acquisition activity is a harbinger of this shift, Kwong believes, asserting that where M&A transactions traditionally relied on syndicated loans, 2009 saw “large-sized transactions raised in the bond market.” Increasingly, he says, the

ability to lock in liquidity and pay a reasonable price is making the bond market the place “to finance large-sized acquisitions.” He adds: “It is a remarkable shift from the banking market into the capital markets.”

### Safe and Simple

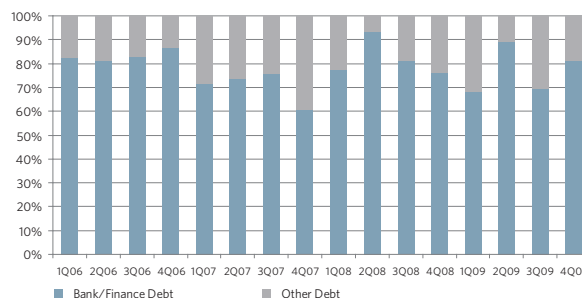
The panelists agree that the new stirrings in the debt markets are taking place at the top—with investment-grade deals by major, high-quality global issuers in those markets where, as SC Lowy’s Chetan Baxi says, the legal foundation is proven. And they agree that “protection is what investors are looking at,” in Baxi’s words, “and they are looking at downside protection much more significantly.”

It is why sovereigns “get the best bid from investors,” as Kwong says, and it’s why there is little appetite for high-yield investments—and certainly for such structures as derivative-embedded notes. “If we start going into structures,” says Kwong, “investors will have to look in very close detail at waterfall, at whether security is being protected, and how security can be enforced... I think it’s probably going to take some time before investors start diving back into the high-yield private space.” Instead, “simple is good,” so for the most part, the offering is “fixed-rate vanilla bonds.”

“Right now,” Baxi asserts, “what investors need from an issuer is very clear guidance on how the company will operate in times of stress and what are the rights and the legal recourse that investors will have in any situation—operational, legal, shareholder dispute, or otherwise.”

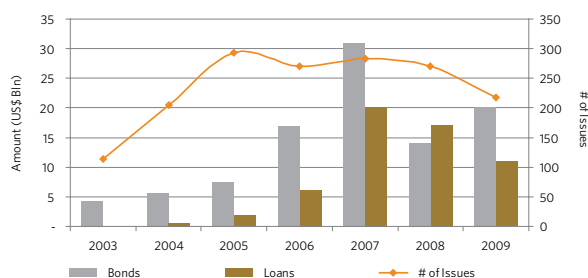
This emphasis on safe-and-simple is not solely about assessing the investment itself; it derives from a deep-seated investor demand for transparency about exactly how an issuer’s internal processes work and how investors can be certain they will get paid when they exit. Baxi, an expert in distressed debt, likens this demand to the deeper analyses distressed investors traditionally perform. They go “beyond just the financial model for the company to actually look at the time value of enforcement rights.” Such an analysis demands a more rigorous decision-making process for investors and raises the bar on their comfort level with an issuer.

**Asia-Pacific Corporate Debt Issuance**  
(Proceeds by Industry Type)



Cross-border (XS ISIN) debt issued by APAC corporations into foreign markets.  
Source: Dealogic

**Islamic Financing**  
(Funding Activity)



Source: Bloomberg

Still, as elsewhere around the world, our Asia-Pacific panelists agree that the need for transparency and the demand for comfort do not mean automatic exclusion for any particular kind of investment or jurisdiction. With the right resources and sufficient experience in a market, says Baxi, investors can determine the value of any investment opportunity. While Kwong points out that “enforcement problems in different jurisdictions have persuaded investors not to participate” in many high-yield structures, “there are investors out there,” says Baxi, “that will take on very difficult situations.”

For the bulk of investors, however, the compass is today pointing to a number of key “areas of interest,” as Baxi refers to them—namely, “consumer finance companies in Japan and Japan overall,” refinancing issues in Australia, fixed income in both Japan and Australia, and “a lot more cross-border issues coming up.”

## Ratings

What role will the rating agencies play in this renewal of the debt capital markets in the Asia-Pacific region?

Our panelists agree that in the sub-investment grade arena, the rating agencies have “never really” played a major role in supplementing investors’ own “homework,” to use Kwong’s word. “Asian investors have been in stressed situations many more times” than their counterparts around the world, adds Chetan Baxi,

and as a result, they have “already” gone beyond the rating agencies in doing their own assessments of sub-investment grade and high-yield corporate investments.

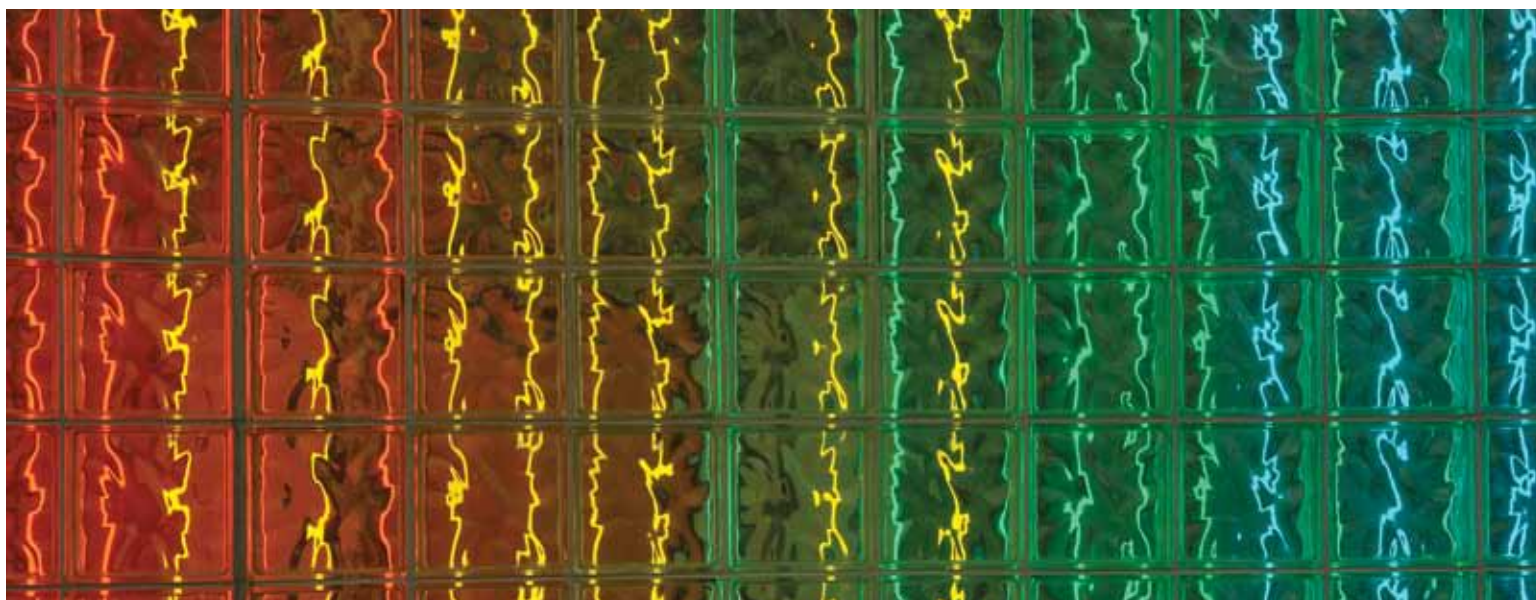
The panelists concur that the rating agencies tend to lag behind market realities—particularly, says Frank Kwong, “in the mortgage market, where the rating agents have been very slow to analyze mortgages as security packages in domestic markets.”

At the same time, a lot of debt issuers “on the investment-grade side... tend to be government-linked,” Kwong says, “and not all of them are very transparent.” Rating-agency assessments can be very useful in such cases.

## Sukuk and Sharia

A topic particularly pertinent to the Asia-Pacific region is the impact of Islamic law, Sharia, on finance, as seen in such instruments as sukuk—in effect, bonds that comply with Sharia. In a region of the world that holds the world’s largest concentration of Muslims, awareness of Sharia and its role in finance is essential, although our panelists agree that the power and scope of its impact “has a long way to go,” as Chetan Baxi puts it.

The issue, says Baxi, is that the secondary market continues to display “a huge amount of uncertainty” about Sharia in terms of both “levels of debt and



the rights of creditors.” Certainly there has been ample discussion “about issuing guidelines and even regulations around credit protection.” But as yet, Baxi asserts, the reality has not been tested. Until it has been well tested over time so that there are precedents to point to, the uncertainty in the secondary market will persist.

### Going Forward—Fast

What do our roundtable participants foresee for the debt capital markets in the region going forward a year to 18 months?

All assert that there has been “a deepening” of the investor base with a new focus on the debt markets. But with investment-grade activity “coming back and coming back strong,” in Baxi’s words, “issuers that are not investment-grade are going to have a difficult time.” And that, in turn, will affect “what investors are going to be able to look at and where they’ll put their money.”

This analysis leads to the observation—the recommendation—that issuers should “be specific and target a specific investor base” rather than trying “to go out into the market.”

This deepened investor base comprises, in Baxi’s view, “not only traditional global guys, the private-equity guys, the venture capital guys,” but also “a number of domestic funds that are ready to apply their money in situations that they understand and that they can get comfortable with.” Our panelists urge issuers to look hard and analytically at this deepened investor base and meet different segments of the base on their own terms specific to their interests.

Adds Frank Kwong: “We’re increasingly seeing corporate participation in a number of transactions, including private sub-investment grade trades where the corporates know their domestic markets well.” High-net-worth individuals, numerous across the region, also “know the market well and are willing to invest in highly structured transactions.” Bottom line? “I wouldn’t rule out a smallish capital-raising event through what you would consider minor-player investors in domestic markets.”

The message to Asia-Pacific issuers is clear: Investors are looking “very, very specifically,” as Baxi puts it—at structures, price, jurisdictions, etc. Issuers need to look back at investors in those same terms so that they can be “aligned with the particular group of investors who are attuned to looking at their specific situation.” And, he contends, if there is money on the sidelines waiting for the right discounted prize, investors will need “on-the-ground origination platforms and access to the banks on a much more consistent basis” to seize the opportunities.

So what do our panelists see up ahead? They are not looking for “a watershed moment,” as Chetan Baxi characterizes it, but rather are anticipating a steady stream of “sub-performing and non-performing assets” coming to market.

Where might some of these non-performing assets come from? Kwong mentions Korea and suggests the possibility of “balance sheet reshuffling out of China,” where word has it that the banks “are looking to raise capital.” Lowy cautions that “while China is a large market, the opaqueness of information available makes it less attractive as a market than such countries as Japan and Australia.” Of Korea, he says it is “a sophisticated distressed market, but with too much local competition.”

But wherever the non-performing assets come from, says Chetan Baxi, the banks will need to target investors in terms of their “commitment to the market and ability to restructure and manage the assets that are going to come out.”

For issuers active in the Asia-Pacific debt capital markets, that is the watchword in general: Target your investors on the basis of their specific interests and bring your debt issuance to them on terms that appeal to them and that are geared to meet their own individual investment needs.

# The Evolving Marketplace

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# Corporate Trust: Service Leadership in an Evolving Marketplace

**By Andrew Zelter**

Head of Global Business  
Development

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Against the backdrop of a decline in global debt issuance, 2009 was a year of considerable activity for BNY Mellon Corporate Trust. We were able to achieve a substantial measure of success in our business development efforts during the year, thus further strengthening our position as the world's leading provider of debt services. Two transformational developments, in my view, led to this success:

First, changing market needs demanded an expansion in the scope of client services beyond the traditional set of product offerings, and second, issuers exhibited an exceptional willingness to change service providers.

As the roundtables reported on in these pages make clear, the volatility within the marketplace over the last 18 months has stirred changes that are transforming the way investors and issuers approach the capital markets. Even as investors return to fixed-income investing, they do so in a context of concerns that have prompted both a strategic rethinking and tactical shifts in the way they manage investments and portfolios. By the same token, even as debt issuance volume and overall market activity have improved, issuers, still mindful of the volatility of the recent past, are reconfiguring the scope and content of their offerings.

Our role in serving both investors and issuers affords us a front-row seat on the market's evolution, and our ability to respond to changing needs—to assume the servicing of existing and restructured programs—has been at the heart of our continued success.

## **Changing Service Needs**

We need only look to our global portfolio of transactions throughout the course of 2009, for example, to note a tangible change in the scope and character of services our issuer and investor clients require. Today's demands are for services not typically thought of as within the service provider purview—clearly reflecting needs that have gone beyond traditional issuer service requirements. For example, we have recently enhanced our suite of services to include more robust independent price and asset verification, loan-level analytics, and other transparency-linked initiatives.

We are also reaching out to a widening range of participants in the market. A case in point is our partnership with Microsoft to deliver to state and local

governments a solution for meeting their requirements under the American Recovery & Reinvestment Act of 2009 (ARRA) for project fund administration, tracking, and reporting. Across the U.S., the Act's transparency requisites have meant added pressure on systems and staff; the combination of BNY Mellon Corporate Trust's public-finance-sector expertise with Microsoft's familiar and user-friendly software offered an immediate solution.

In addition, we have aligned our global acquisition strategy to changing marketplace needs. For example, in acquiring Portsmouth Financial Systems, a developer of modeling and analytics of structured credit transactions, we added the capability to offer a new service with a variety of features—initially for mortgage-backed securities, in due course for other structured assets. Similarly, our acquisition of Pinnacle Arbitrage Compliance, one of the largest independent U.S. firms devoted exclusively to compliance services for tax-exempt bond issuers and conduit borrowers, widens our portfolio of services for the entire arbitrage compliance process, enabling us to provide issuers with seamless reporting and information as they seek to maximize investment returns on bond funds.

### Raising the Bar on Service Provision

As we see it, and as the roundtable discussions seem to confirm, these changes are transforming, not transient. And the pace of this change has been noteworthy in many respects. What has brought this home to us with particular force over the past year is the unprecedented number of instances in which BNY Mellon has been appointed to act in a successor capacity. Historically, issuers have been reluctant to replace their incumbent service agent, yet over the past several months, BNY Mellon has been appointed as successor agent on hundreds of transactions worldwide. The reasons for this are simple, as you'll see illustrated in many of the case-studies in the pages that follow: As the leading global trustee, we bring to bear the right combination of expertise, innovation, and client collaboration needed to tailor and deliver the solutions that work.

Many of our successorships have resulted from resignations due to role conflict—where the service provider was also the lender or arranger, for example. Other successorship opportunities were either

covenant-triggered, resulting from institutional downgrades, or derived from the incumbent service provider's inability to support the particular program structure. Given the unprecedented number of successor appointments in 2009, it is clear that this is not an isolated phenomenon but a profound change in the scope of service provision the debt capital markets will need in the future.

### Internal Changes

How are we responding to these marketplace changes and to the transformation we see happening?

In addition to our focus on innovation, product expansion, and strategic acquisitions, we continue to play a key role as a thought leader developing market intelligence and sharing it with other leading participants in the debt capital markets. Our survey of attendees at the Annual Global ABS Conference in London during June, 2009, provided valuable insight on the securitization markets and on the role of the trustee in providing greater transparency, a critical component to the future success of the market. Our Municipal Finance Market Study, launched at the Government Finance Officers Association National Conference in Seattle, also in June, took the pulse of the public finance sector in the U.S. at a critical moment in that sector's history. A forum we sponsored in Washington in September, 2009, as part of our Leadership Series, focused on Rebuilding the Mortgage Market, Loan by Loan and featured distinguished mortgage industry leaders from both the government and private sectors. Summaries of the discussions and analyses of the conclusions were disseminated throughout the industry.

And of course, you are reading another example of the market intelligence we gather, analyze, and share. It is further evidence of our commitment, in the midst of evolutionary transformation, to continue to set the standard for service provision—in every sense of the phrase—for the debt capital markets.

STATE OF MISSOURI,  
CITY OF ST. LOUIS.

I, the undersigned, Recorder of Deeds  
hereby certify that the foregoing  
was filed for record in my office on this  
day of January A. D. 1891, at 3  
o'clock P.M. truly recorded in Book 996 Page  
WITNESS my hand and official seal on this

... continue a lien on the ...  
... REOF, C. E. Rainwater President, and John H. Overall  
Secretary, of said party of the first part, by order of  
the Board of Directors thereof, and also in conformity  
with resolutions duly passed and adopted at a meeting  
of the stockholders of said Railway Company, duly  
called and held on the 1<sup>st</sup> day of October A. D.  
1890, have hereunto set their hands and affixed the  
corporate seal of said Company, this 1<sup>st</sup> day of  
October A. D., 1890; and the said party of the  
second part has caused these presents to be  
signed by its corporate name by  
its President, and its corporate seal to be  
affixed hereto, attested by  
its Secretary.

RD  
recorder  
234  
BOOK 996  
FILED FOR RECORD  
JAN 10 1891  
338  
A. A. HOBBS,  
RECORDER



... Louis Winchuck ...  
By C. E. Rainwater  
Address:  
John H. Overall  
Secretary.  
St. Louis Trust  
By J. H. Overall

# Case Studies

## Workin' on the Railroad

It was 1890, and in the American heartland, the city of St. Louis was struggling to overcome—or catch up with—the growing dominance of Chicago as the region's commercial and financial center.

Chicago had early been a “railroad town,” while St. Louis had long remained wedded to steamboats. Illinois and Iowa had built the first railroad bridge across the Mississippi more than 30 years before, when a young Illinois attorney named Abraham Lincoln started making his name as a railroad lawyer, while the river interests who held sway in St. Louis continued to champion the principle of free navigation for boats across the river.

But bridge-building had made it possible for freight and passengers from New York to reach the western bank of the Mississippi—and all that lay beyond it—in some 42 hours, an astounding achievement that had once and for all given the edge to the railroads over riverboats. By 1874, the city fathers of St. Louis deferred to reality and built a road and rail bridge across the river, and in little time, the city that had once thought of itself as a shipbuilding town and bustling port now saw itself as the jumping-off point for western expansion—and a great hub for rolling stock and the people and goods it carried.

So by the late 1880s, legendary railroad developer Jay Gould had little trouble orchestrating an agreement among the owners of six railway companies “for the purpose of raising means for the construction, equipment and operation” of a comprehensive railroad system that would connect track, yards, warehouses, and auxiliary facilities to move people and goods east and west across the city. To “raise the means,” mortgage bonds valued at \$3.5 million were issued October 1, 1890—with an established 40-year maturity date of October 1, 1930. The trustee

appointed for the bond, the St. Louis Trust Company, was the local predecessor of the institution known today as BNY Mellon.

In 1902, the bonds were purchased by the Terminal Railroad Association of St. Louis, successor organization to the original agreement, and 20 years later, in 1922, the bonds were used as collateral for the Association's Refunding and Improvement Mortgage Bonds. Twenty years after that, in 1942, a Supplemental Indenture extended the bonds to mature on July 1, 1974.

But the mortgages have never been released. Instead, as the Association sells property subject to the lien, the proceeds from the sale are deposited with the trustee, BNY Mellon Corporate Trust, which then remits the money to the agent for the 1942 supplemental bonds to pay off the issue.

The rivalry between St. Louis and Chicago today plays out in the ballpark and on the gridiron rather than in financial competition. Trains no longer dominate cross-country travel. The bonds issued on October 1, 1890 have long since stopped buying equipment for railcars. But to pay off those bonds, business is still being transacted, value is still being created, and bondholder interests are still being carefully protected and advanced by the long-term trustee of record, today embodied in BNY Mellon Corporate Trust.

# Case Studies

## A Creative Approach to Risk

NEW YORK — Facing an uncomfortable level of risk exposure in the wake of the global financial crisis, a well known global financial institution devised a creative solution for removing toxic assets from its balance sheet—establishing a separate fund management company and selling its risky assets. Experts believe the approach might set a precedent and could help revive asset-backed securities markets.

But the size of the solution—more than \$10 billion—meant that the institution needed a service provider with comprehensive resources and exceptional expertise. It

turned to its longtime partner, BNY Mellon Corporate Trust, to serve as collateral administrator, document custodian, trustee, registrar, and paying agent, trusting that the market leader in servicing whole loans and asset-backed finance would be the right choice to administer this sizable transaction and to ensure timely and accurate reporting.

It's a trust that has been amply satisfied.

## Operating at Full Capacity

LOS ANGELES — The financing authority of a Western state wanted to do block trading but found its trustee didn't offer that capability. It wanted to allocate fixed-income trades to multiple bond issues, but again, its trustee lacked the capacity. And when it found it could not withdraw funds from a frozen money market account, it realized it was operating with one hand tied behind its back. The authority decided to seek a new trustee that could help it make better use of its existing cash.

BNY Mellon Corporate Trust filled the bill. To this major issuer, BNY Mellon offered the power and flexibility that

dramatically expanded and extended the authority's trading capabilities. Block trading, allocation to multiple issues, access to funds, service, technology, and a range of investment options: it's what a trustee is supposed to offer. BNY Mellon delivered, and now this state's financing authority operates at full capacity.

## Partnership Trust

TOKYO — As part of its strategy of principal investment, a large Japanese financial institution sought a trustee to establish and manage a money trust on its behalf. The investment amount was substantive, but what was essential to the financial institution was not only that the trustee have the resources and expertise needed, but also that it be able to tailor the trust to client instructions about how the funds were to be invested.

BNY Mellon Corporate Trust had the resources and expertise to effect transactions across a range of asset classes and geographies, and it was able to demonstrate to the client its efficiency and flexibility as a partner.

From the opening of the account through due diligence on assets to trust accounting and reporting, BNY Mellon consulted closely with the client, creating the teamwork of a true collaboration in order to tailor the solutions needed.

## One-Stop Shopping for Debt Restructuring

SÃO PAULO — As a result of the global financial crisis, debt restructuring has become a common practice throughout the world—and the Brazilian market is no exception. But where banking creditors once assumed full responsibility for a restructuring, despite often lacking sufficient internal capacity and expertise, today's debtors are looking for a third-party provider that can act as an independent agent among the parties and deliver all needed services. That was the case for a major company in Brazil's key agribusiness sector when currency fluctuations and the need for funds to finance production prompted renegotiation of existing debt.

The company turned to BNY Mellon Corporate Trust—and found just what was needed. BNY Mellon offered independence and provided all needed local and cross-border services. Acting as collateral agent, guarantee agent, and inter-creditor liaison, BNY Mellon ensures the execution of the contract, controls the guarantees and covenants, holds and distributes the funds, and plans creditors' meetings. For this key company, BNY Mellon provided one-stop shopping—a single solution to multiple needs.

## Old Hand for a New Product

MEXICO CITY — Issuing an innovative debt product is difficult at any time, but a major infrastructure provider in a Latin American country found itself doing so while the regulations governing the innovative instrument were still in flux. That and a marketplace still hurting from numerous securitization defaults made the issuance a particularly complex and demanding process. And that, in turn, imposed a burden of uncertainty on the infrastructure development the issue would fund.

Top priority for the issuer was to choose a trustee with the expertise and capacity to handle complex structures

and with a global reputation that the local market would recognize and trust instantly. The choice was simple: BNY Mellon's local team of recognized trust professionals was ready with the global experience and strength needed to make the issuance a success. The team's creative enhancements, melding global resources and local savvy, was an added benefit on top of a successful result.

## Facility Agent

LONDON — When the arrangers of a large syndicated loan realized that the complexity of the deal put it beyond the resources of their own back and middle offices, they decided to outsource the operation to a private-label facility agent. After all, the operational requirements for monitoring, recording, and reporting on a sensitive deal are hardly the core business of investment banking, so this firm turned to an entity for which such activities are core—BNY Mellon Corporate Trust.

BNY Mellon rounded out the client's back-office and middle-office capabilities with all the technology,

processing capacity, and agency expertise needed to do the job. A Master Services Agreement defined the client's ownership of the relationship and set forth BNY Mellon's responsibilities for processing support; the mechanics were transitioned quickly, and the needed support was in place virtually immediately.

# Case Studies

## College Material

NEW YORK — With consumer credit dwindling in the wake of the financial crisis, students in search of college loans faced a new challenge—one that might imperil their dreams of higher education.

Then a pair of well known Wall Street firms had the idea of creating a short-term student loan financing capacity that would tap into the market for asset-backed commercial paper (ABCP) and that would be backed by the government—a potentially powerful incentive to the money market investors who buy ABCP. To make it happen, the co-arrangers needed to line up a long list of

participants in addition to the government agency—and find a third-party administrator to provide the operational infrastructure. Requirements for the job? Student loan expertise, substantive custodial capacity and reporting capabilities, investment flexibility, and the resources to customize the process.

BNY Mellon Corporate Trust met all the requirements. Today, with \$30 billion in outstanding investments, this unique conduit funds not just student loans but educational dreams as well.

## Simplicity Works

LONDON — Assigned as custodian and agent for a note program governed by Islamic law, or Sharia, BNY Mellon Corporate Trust was suddenly tasked to take on another challenge—i.e., customizing a methodology for tracking and reporting on the underlying securities of the note program.

The solution was absolutely simple and absolutely on target. A spreadsheet dedicated to the program and showing all assets held under each note in the program is updated periodically by issuer and custodian alike. Low-maintenance, low-cost, and easily accessible to all who

need access, the spreadsheet does exactly what its users need it to do. For BNY Mellon, it was a matter of finding the right tool for the job—nothing less, and nothing more.

## Issuing Debt in a Cautious Time

SINGAPORE — In the wake of the global financial crisis—a slow time for debt issuance—a leading multinational corporation decided to issue a huge, global, multifaceted bond offering. In size and complexity, the issuance constituted a major challenge—especially because time was of the essence.

Already familiar with BNY Mellon Corporate Trust's strong support on other transactions, the multinational looked no further for help in meeting this substantive challenge.

BNY Mellon got the job done in less than a month. A dedicated deal team was assigned, with a single point of contact to ensure there would be no compromise in realizing the issuer's needs. The aim was to meet or beat every milestone, keep the momentum going forward relentlessly, and thus lessen the pressure on the issuer and lead managers.

With BNY Mellon serving multiple roles, this huge transaction was executed seamlessly, quickly, and successfully.

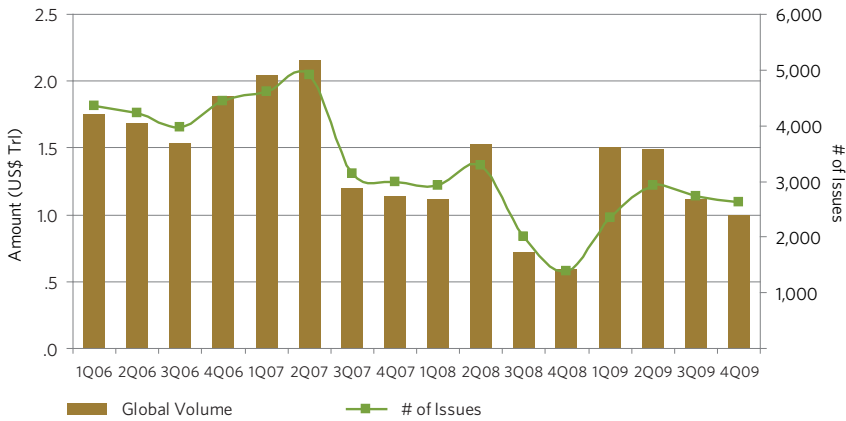
# The Debt Markets by the Numbers

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Graphs and analysis compiled by BNY Mellon Corporate Trust Strategy & Product Management.

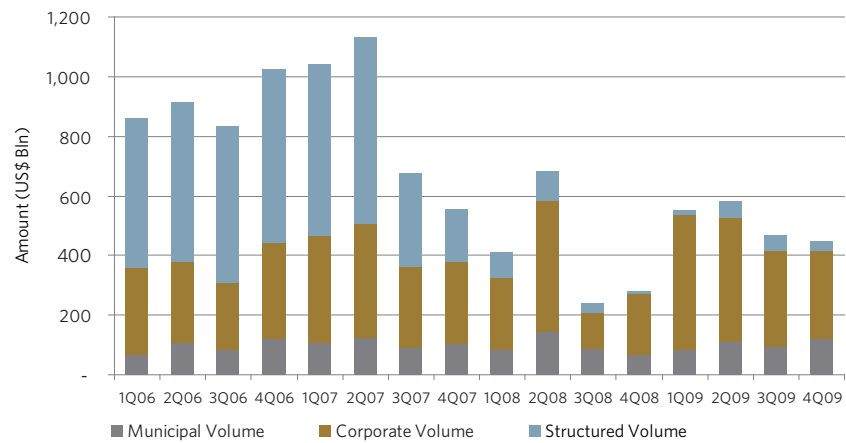
# Debt Issuance

## Global Debt Activity



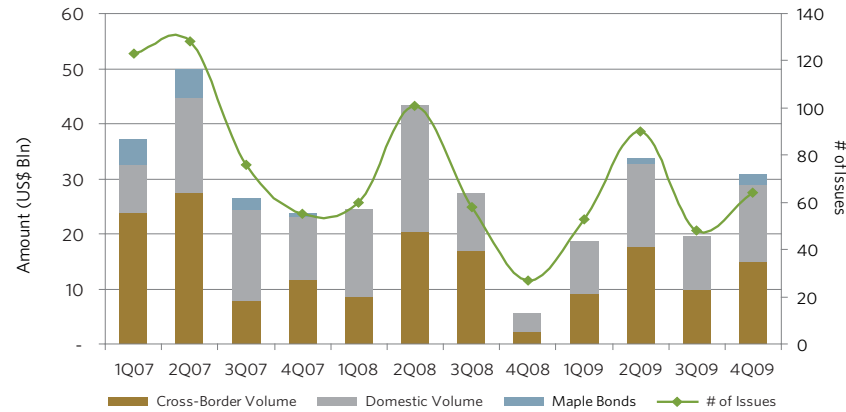
Includes ABS, MBS, and taxable municipals known to ThomsonReuters.  
Source: ThomsonReuters

## United States Debt Activity



Includes all US municipal finance, corporate finance, and structured (ABS and MBS) known to ThomsonReuters.  
Source: ThomsonReuters

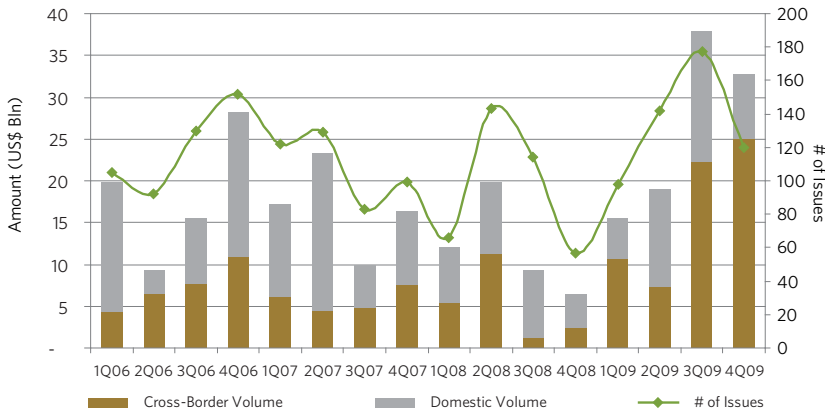
## Canada Debt Activity



Includes Private and public corporate and structured debt in Canada known to ThomsonReuters.  
Source: ThomsonReuters

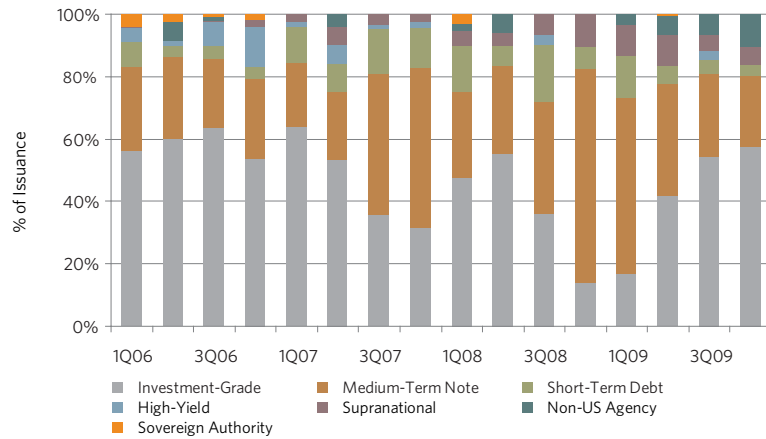
# Debt Issuance

## Latin America Debt Activity



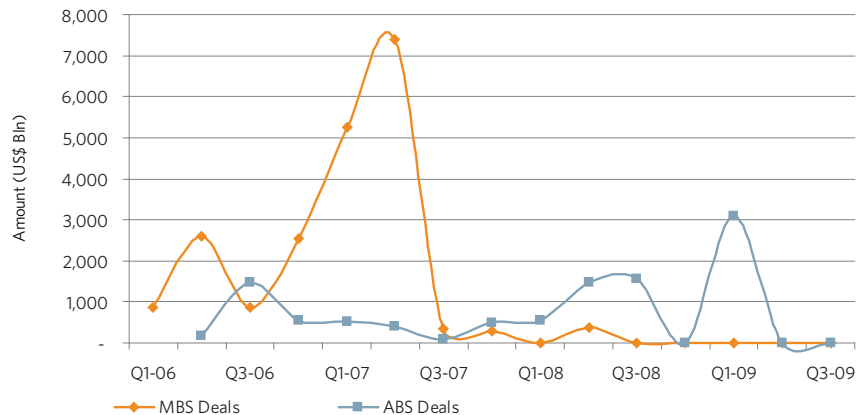
Includes private and public corporate and structured debt in Latin America known to Bloomberg and Dealogic.  
Source: Bloomberg, Dealogic

## Asia-Pacific Cross-Border Corporate Debt (Issuance by Bond Type)



Percent of total of XS ISIN volume issued corporate debt in the APAC market quarterly. Corporate debt includes medium-term notes, investment-grade, high-yield, sovereign/supranational, non-US agency, and short-term debt as defined by Dealogic.  
Source: Dealogic

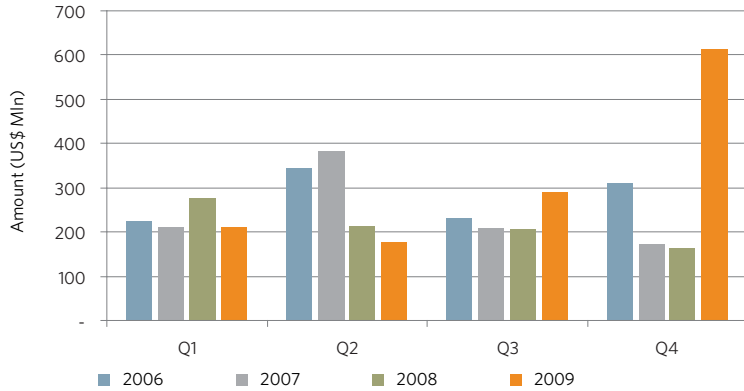
## Asia-Pacific Cross-Border Structured Debt (MBS & ABS Issuance)



Total of XS ISIN structured debt volume issued in the APAC market quarterly. Structured debt includes ABS and MBS issued publicly and known to Dealogic. May not include all structured deals placed in the defined market.  
Source: Dealogic

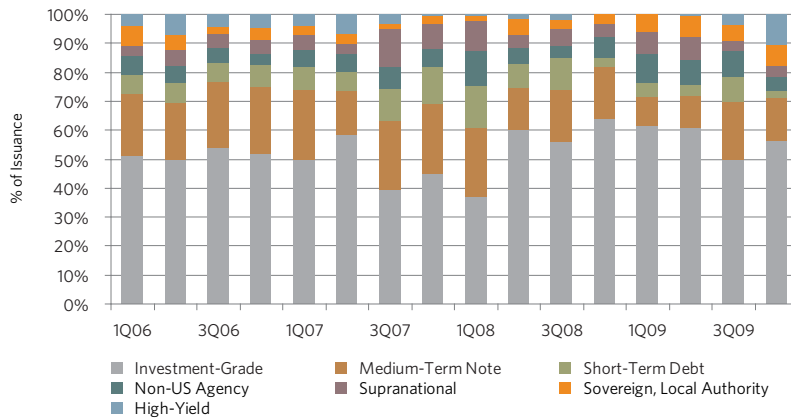
# Debt Issuance (continued)

## Asia-Pacific Cross-Border Corporate Debt (Average Deal Size by Quarter)



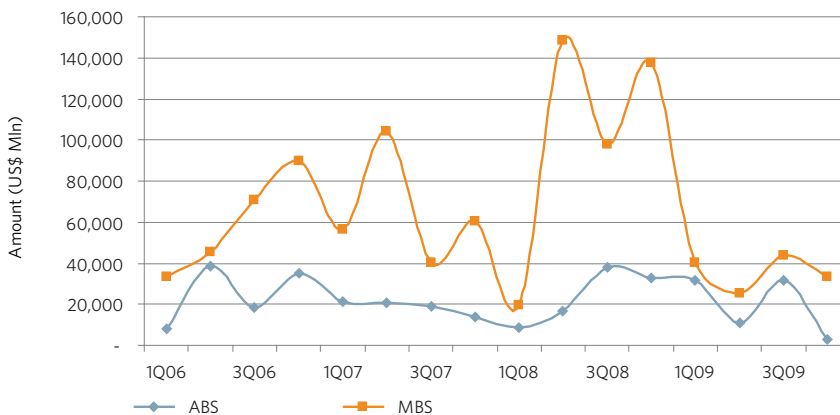
Average deal size of XS ISIN issued stand-alone corporate debt in the APAC market quarterly. Corporate debt includes investment-grade, high-yield, sovereign/supranational, non-US agency, and short-term debt. Source: Dealogic

## Europe, Middle East and Africa Cross-Border Debt (Issuance by Bond Type)



Percent of total of XS ISIN volume issued corporate debt in the EMEA market quarterly. Corporate debt includes medium-term notes, investment-grade, high-yield, sovereign/supranational, non-US agency, and short-term debt as defined by Dealogic. Source: Dealogic

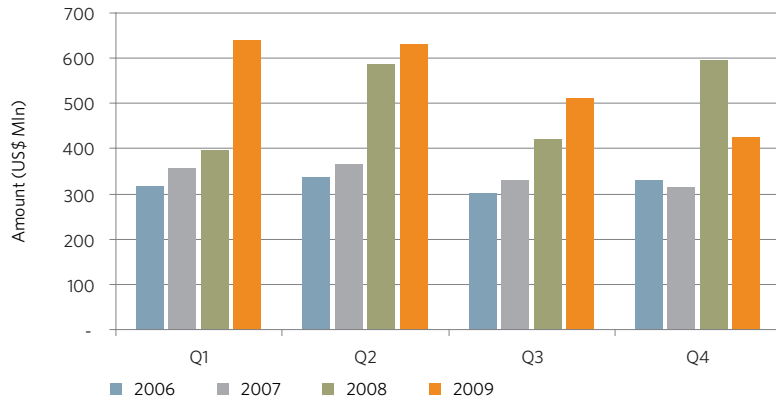
## Europe, Middle East and Africa Cross-Border Structured Debt (MBS & ABS Issuance)



Total of XS ISIN structured debt volume issued in the EMEA market quarterly. Structured debt includes ABS and MBS issued publicly and known to Dealogic. May not include all structured deals placed in the defined market. Source: Dealogic

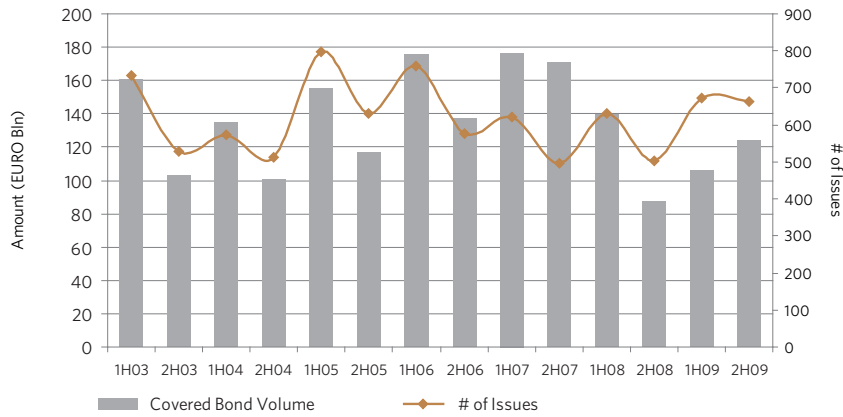
# Debt Issuance

## Europe, Middle East and Africa Cross-Border Corporate Debt (Average Deal Size by Quarter)



Average deal size of XS ISIN issued stand-alone corporate debt in the EMEA market quarterly. Corporate debt includes investment-grade, high-yield, sovereign/supranational, non-US agency, and short-term debt.  
Source: Dealogic

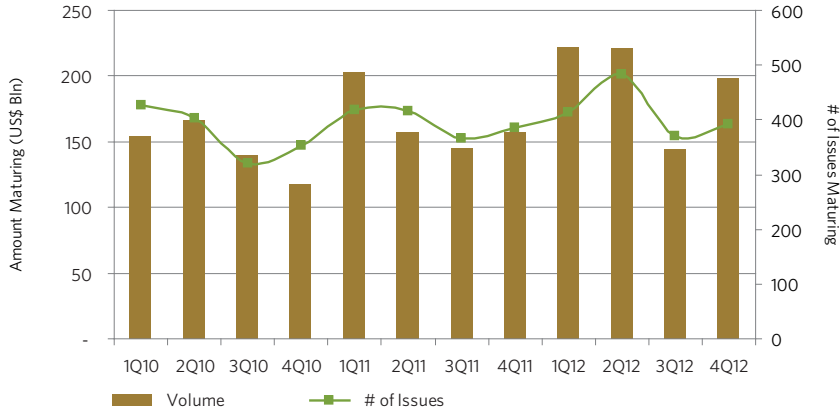
## Global Covered Bonds (Funding Activity)



Covered bonds, as defined by Bloomberg League Tables, include Pfandbrief issuances.  
Source: Bloomberg

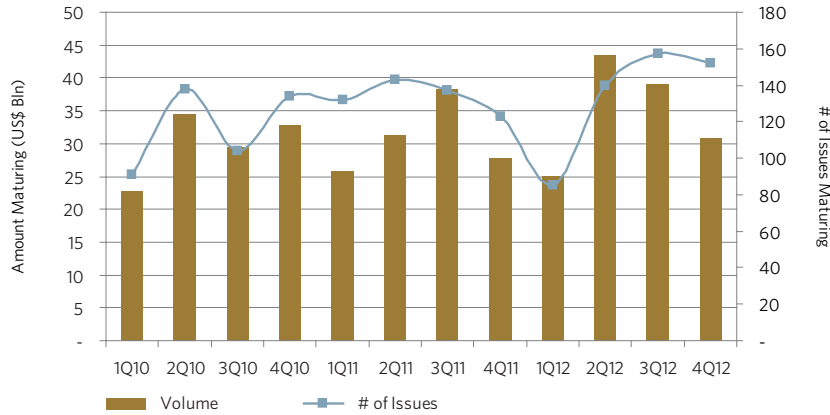
# Maturing Debt

## United States Maturing Corporate Straight Debt (Three-Year Maturity Schedule)



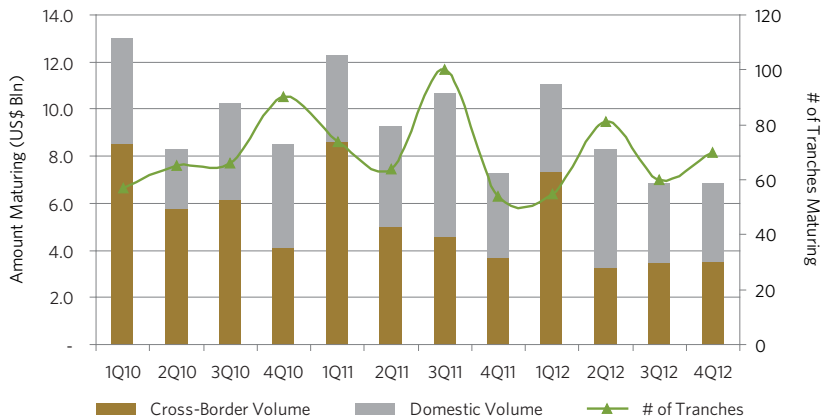
Comprises US straight debt issued between 1/1/1989 and 12/31/2009, still outstanding, with a maturity between 1/1/2010 and 12/31/2012.  
Source: ThomsonReuters

## United States Maturing Structured Debt (Three-Year Maturity Schedule)



Comprises US ABS and MBS debt issued between 1/1/1989 and 12/31/2009, still outstanding, with a maturity between 1/1/2010 and 12/31/2012.  
Source: ThomsonReuters

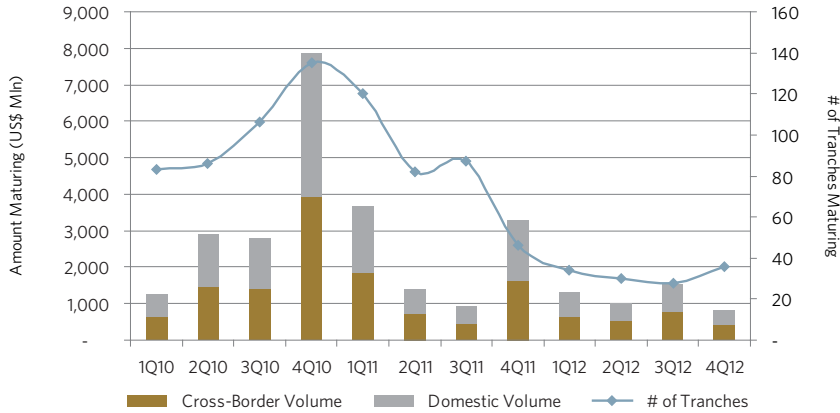
## Latin America Maturing Corporate Debt (Three-Year Maturity Schedule)



Comprises Latin America corporate and sovereign debt issued between 1/1/1999 and 12/31/2009, still outstanding, with a maturity between 1/1/2010 and 12/31/2012.  
Source: Bloomberg, Dealogic

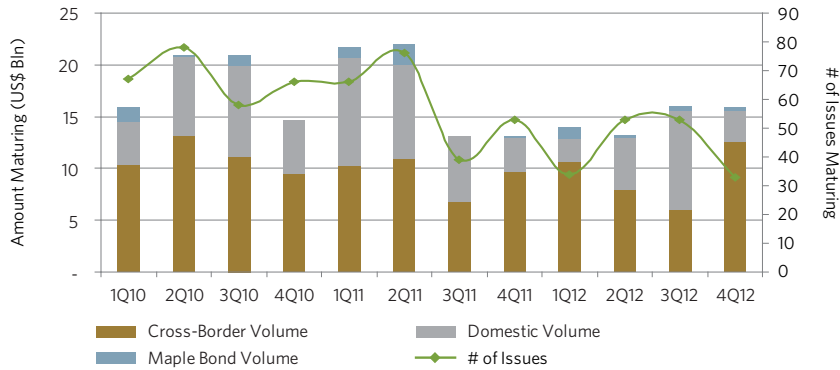
# Maturing Debt

## Latin America Maturing Structured Debt (Three-Year Maturity Schedule)



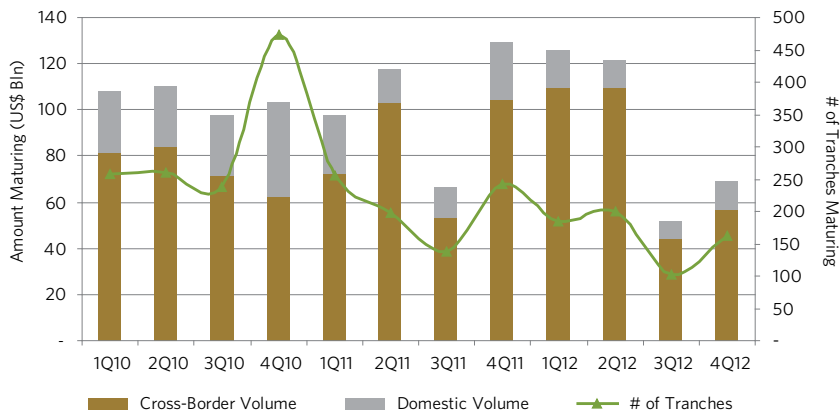
Comprises Latin America ABS and MBS debt issued between 1/1/1993 and 12/31/2009 still outstanding, with a maturity between 1/1/2010 and 12/31/2012.  
Source: Bloomberg, Dealogic

## Canada Maturing Debt (Three-Year Maturity Schedule)



Comprises Canadian cross-border, domestic, and Maple corporate and structured debt issued between 1/1/1986 and 12/31/2009, still outstanding. Corporate debt includes investment-grade, high-yield, and agency/sovereign issued securities. Structured debt includes ABS or MBS.  
Source: ThomsonReuters

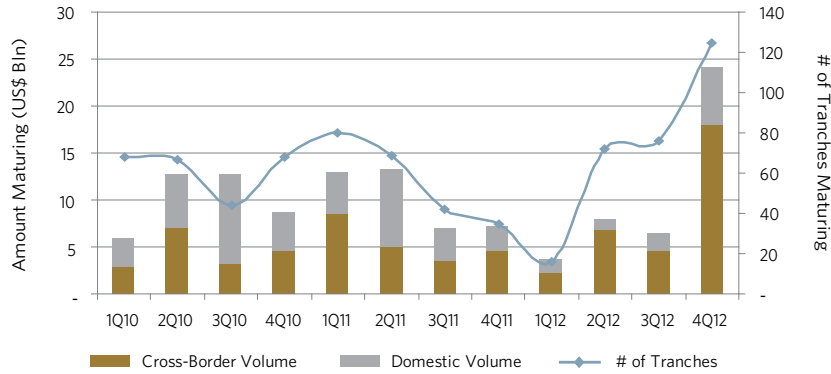
## Europe, Middle East and Africa Maturing Corporate Debt (Three-Year Maturity Schedule)



Comprises corporate and sovereign debt by EMEA domiciled issuers between 1/1/1985 and 12/31/2009, still outstanding, with a maturity between 1/1/2010 and 12/31/2012. Does not include MTN Issuance.  
Source: Dealogic

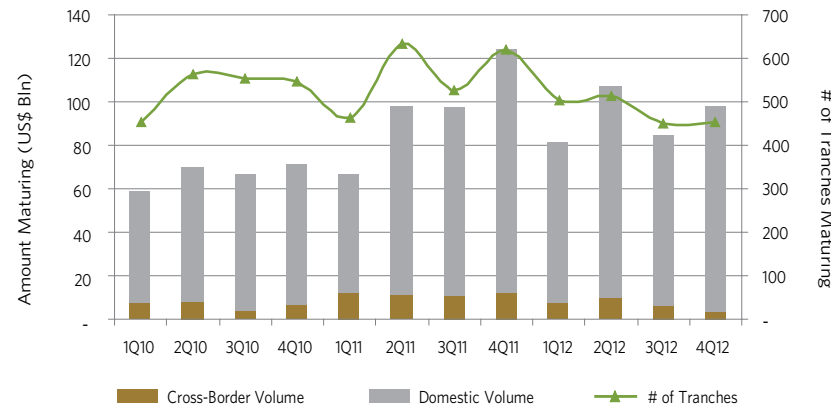
# Maturing Debt (continued)

## Europe, Middle East and Africa Maturing Structured Debt (Three-Year Maturity Schedule)



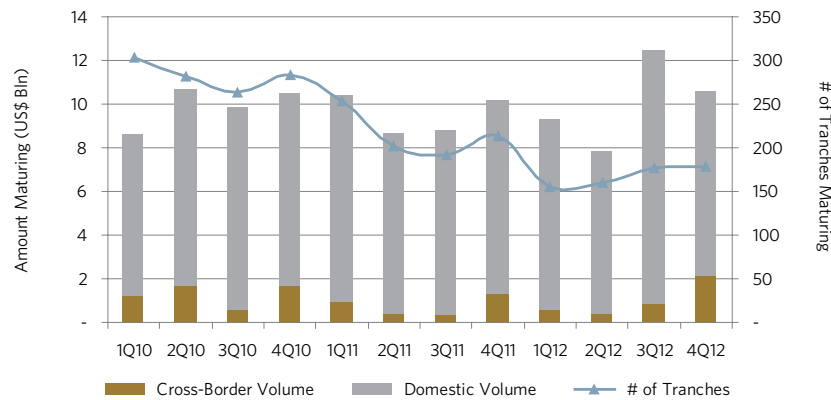
Comprises ABS and MBS debt by EMEA domiciled issuers between 1/1/1985 and 12/31/2009 still outstanding, with a maturity between 1/1/2010 and 12/31/2012.  
Source: Dealogic

## Asia-Pacific Maturing Corporate Debt (Three-Year Maturity Schedule)



Comprises corporate and sovereign debt by APAC domiciled issuers between 1/1/1986 and 12/31/2009, still outstanding, with a maturity between 1/1/2010 and 12/31/2012. Does not include MTN issuance.  
Source: Dealogic

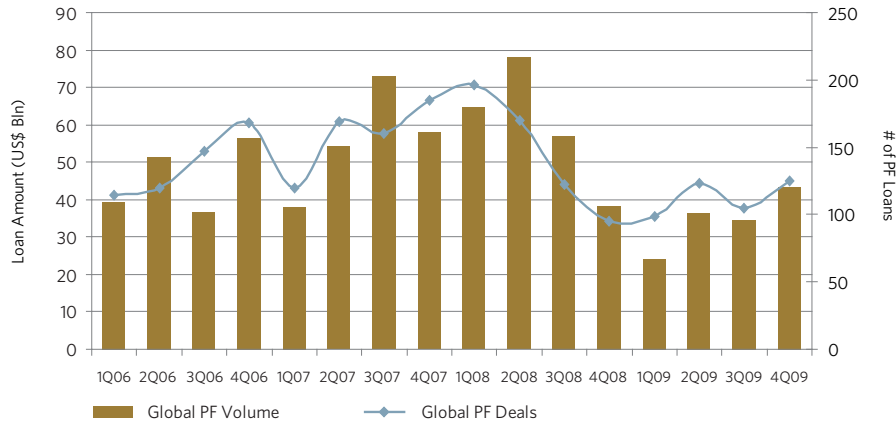
## Asia-Pacific Maturing Structured Debt (Three-Year Maturity Schedule)



Comprises ABS and MBS debt by APAC domiciled issuers between 1/1/1994 and 12/31/2009 still outstanding, with a maturity between 1/1/2010 and 12/31/2012.  
Source: Dealogic

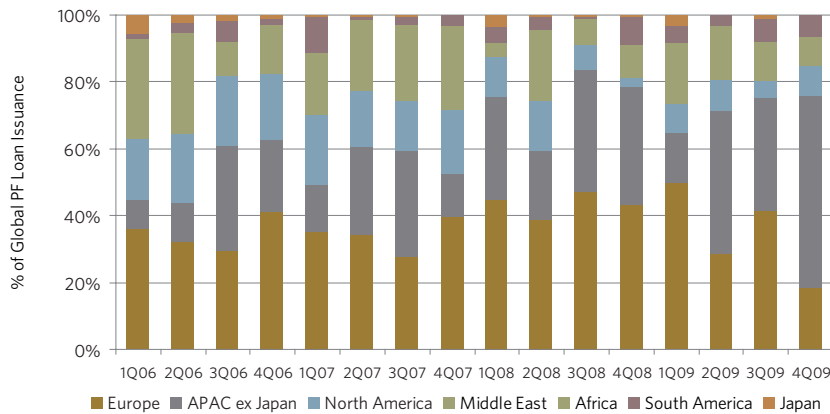
# Project Finance

## Global Project Finance (Funding Activity)



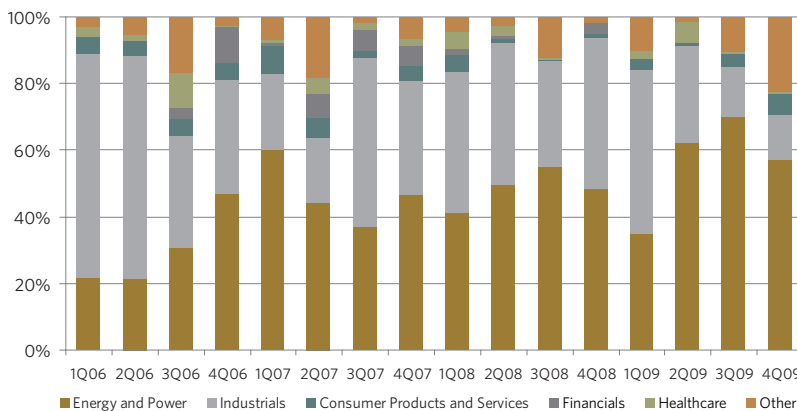
Loan transactions with proceeds directed to project finance initiatives as defined by ThomsonReuters.  
Source: ThomsonReuters

## Global Project Finance Loans (By Domicile Region)



Loan transaction volume in specified domicile regions with proceeds directed to project finance initiatives known to ThomsonReuters.  
Source: ThomsonReuters

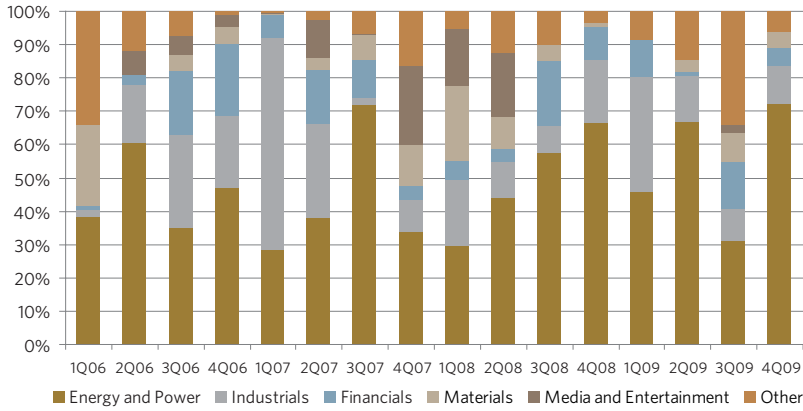
## Europe Project Finance Loan Volume (By Project Industry)



Loan transaction volume in Eastern, Central, and Western Europe domicile regions with proceeds directed to project finance initiatives as defined by ThomsonReuters.  
Source: ThomsonReuters

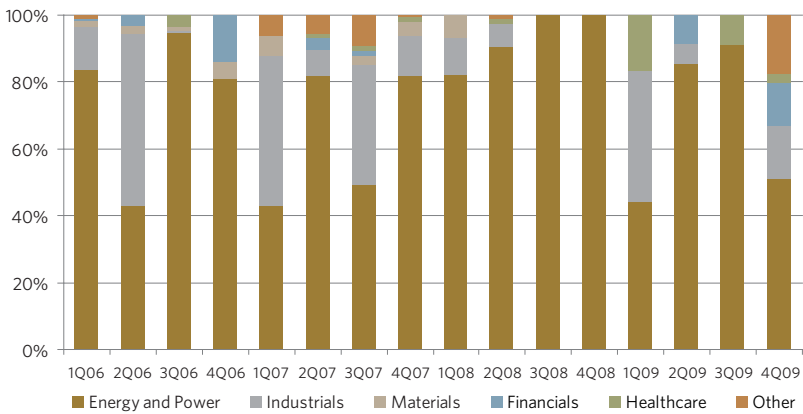
# Project Finance (continued)

## Asia-Pacific Project Finance Loan Volume (By Project Industry)



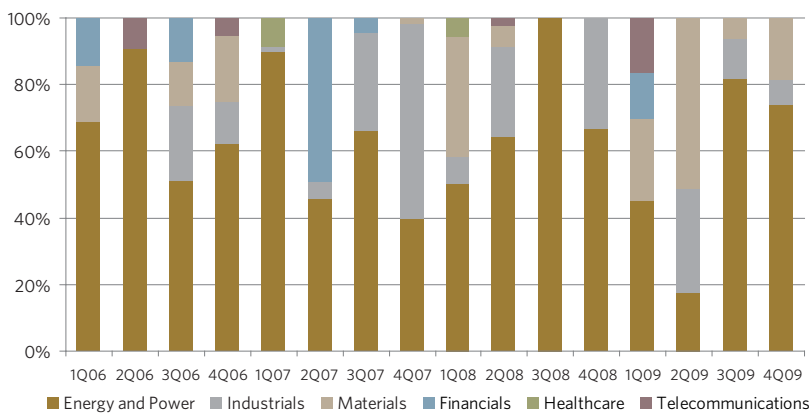
Loan transaction volume in Asia-Pacific and Australasia domicile regions with proceeds directed to project finance initiatives as defined by and known to ThomsonReuters.  
Source: ThomsonReuters

## North America Project Finance Loan Volume (By Project Industry)



Loan transaction volume in North America domicile regions with proceeds directed to project finance initiatives known to ThomsonReuters.  
Source: ThomsonReuters

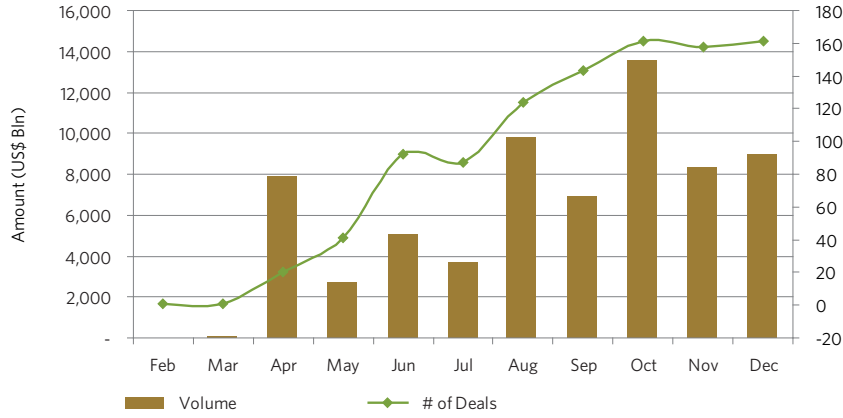
## Latin America Project Finance Loan Volume (By Project Industry)



Loan transaction volume in Central America, South America, and Caribbean domicile regions with proceeds directed to project finance initiatives known to ThomsonReuters.  
Source: ThomsonReuters

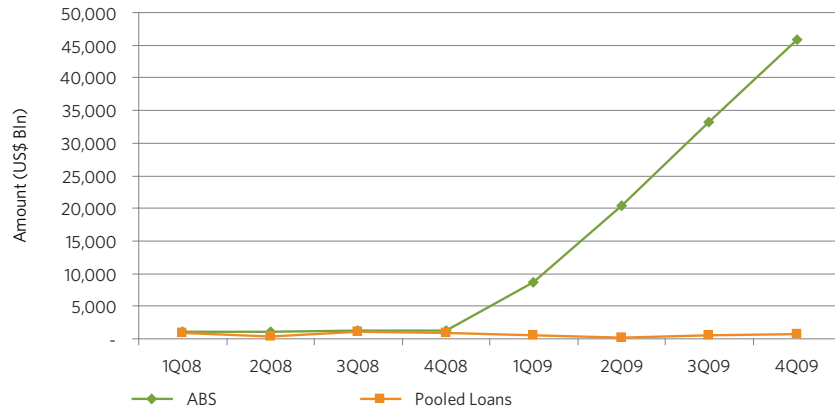
# U.S. Stimulus

## 2009 Public Finance Bond Issuance Under ARRA (American Recovery and Reinvestment Act of 2009)



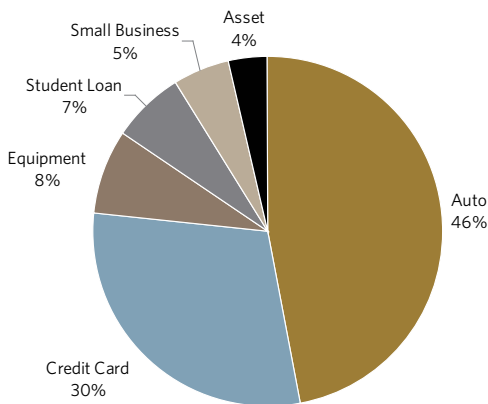
Issuance activity comprises public finance bond authorizations under ARRA including Build America Bonds (BABs), Clean Renewable Energy Bonds (CREBs), Qualified School Construction Bonds (QSCBs), and Qualified Zone Academy Bonds (QZABs) since 1/1/2009 known to ThomsonReuters.  
Source: ThomsonReuters

## United States TALF Eligible Securities Issued 2008-2009



Includes all term ABS loan facility-eligible securities known to Bloomberg.  
Source: Bloomberg

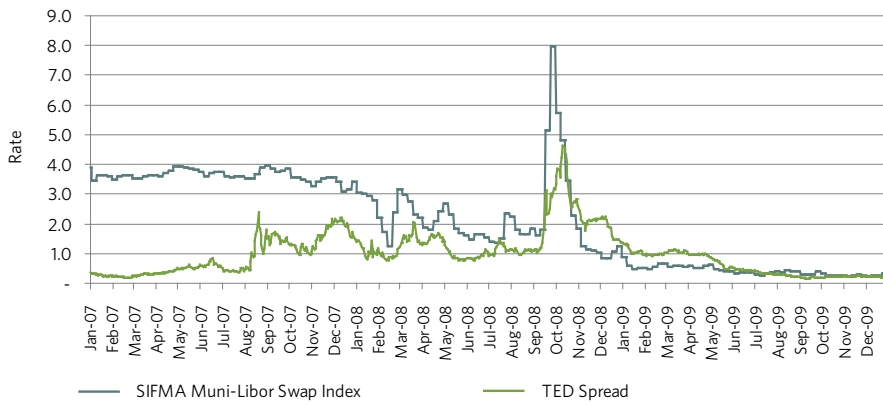
## Collateral Type of TALF Eligible Securities 2009 (US\$ 110.3 Bln)



Source: Bloomberg

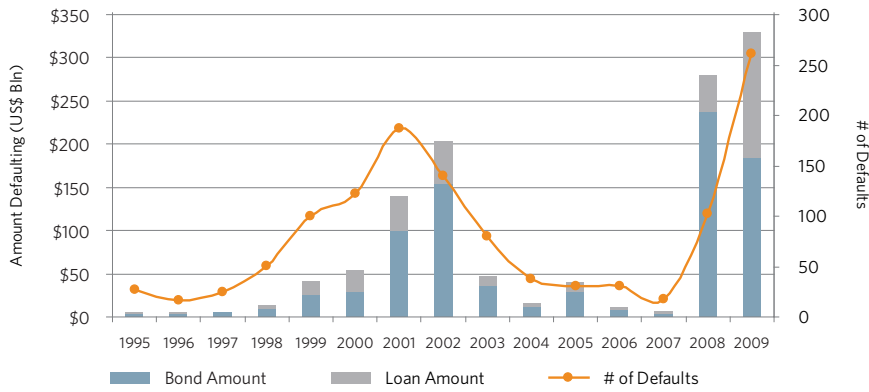
# Broad Market Indicators

## TED Spread and Libor-SIFMA Municipal Swap Index (Rate Changes)



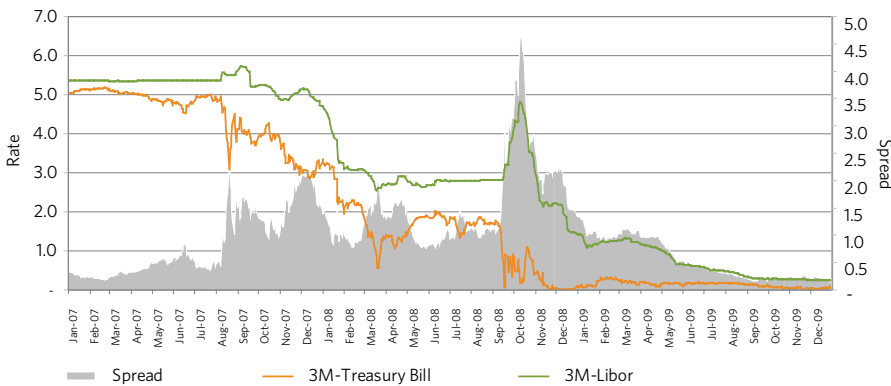
TED Spread calculated as difference between 3-month Libor and 3-month Treasury Bill.  
Source: Bloomberg

## Default Rate on All Moody's Rated Corporate Securities



Source: Moody's

## 3-Month T-Bill and Libor (Historical Rates and Spread)



Spread calculated as difference between 3-month Libor and 3-month Treasury Bill, commonly referred to as the TED Spread.  
Source: Bloomberg

## Profile of a Leader

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# Credit Ratings

As of January 2010

Listed below are the credit ratings for The Bank of New York Mellon Corporation and a principal banking subsidiary, The Bank of New York Mellon.

<b>The Bank of New York Mellon Corporation</b>	<b>Moody's</b>	<b>S&amp;P</b>	<b>Fitch</b>	<b>DBRS</b>
Long-term Senior Debt	Aa2	AA-	AA-	AA (low)
Subordinated Debt	Aa3	A+	A+	A (high)
Trust Preferred Securities	Aa3	A	A+	A (high)
Short-term	P1	A-1+	F1+	R-1 (middle)
Outlook	Stable	Stable	Stable	Stable (long-term) Stable (short-term)

<b>The Bank of New York Mellon</b>	<b>Moody's</b>	<b>S&amp;P</b>	<b>Fitch</b>	<b>DBRS</b>
Long-term Deposits	Aaa	AA	AA	AA
Long-term Senior Debt	Aaa	AA	AA-	AA
Short-term Deposits	P1	A-1+	F1+	R-1 (high)
Outlook	Stable	Stable	Stable	Stable (long-term) Stable (short-term)

A security rating is not a recommendation to buy, sell, or hold securities. The rating may be subject to revision or withdrawal at any time by the assigning rating organization. Each rating should be evaluated independently of the other ratings.

# Market Leadership

For 225 years, BNY Mellon has been a strong, stable company with excellent long-term credit ratings. The quality of our execution and service is recognized across the industry.

## **Top Trustee in the U.S.**

*(Thomson Reuters, 2009)*

## **Top Municipal Debt Trustee in the U.S.**

*(Thomson Reuters, 2009)*

## **Global Corporate Trust Services Provider of the Year**

*(Infrastructure Investor, 2010)*

## **Best in Corporate Trust: Australia, India and Korea**

*(The Asset magazine Triple A Awards - Securities & Fund Services 2010)*

## **Best Investor Services House**

*(Euromoney Awards for Excellence 2009*

*BNY Mellon: Corporate Trust and Asset Servicing)*

## **Safest U.S. Bank**

*(Global Finance magazine "World's 50 Safest Banks 2009")*

## **#1 Superregional Bank (U.S.)**

*(Fortune World's Most Admired Companies, 2009)*

## **Perfect Marks in 2010 Corporate Equality Index**

*(Human Rights Campaign Foundation)*

## **America's Best CEOs**

*(Institutional Investor, 2009 - Robert Kelly,*

*BNY Mellon's Chairman & CEO, No. 4 spot - Large-Cap Bank CEOs)*

# BNY Mellon Corporate Trust Worldwide Locations

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## Europe and Middle East

### The Bank of New York Mellon

One Canada Square  
Canary Wharf  
London E14 5AL  
England

### The Bank of New York Mellon\*

Lower Ground  
30 Cannon Street  
London EC4M 6XH  
England

### The Bank of New York Mellon

Merck House, Seldown Land  
Poole, Dorset BH15 1PX  
England

### The Bank of New York Mellon

13-15 Boulevard de la Madeleine  
75001 Paris  
France

### The Bank of New York Mellon

Bockenheimer Landstrasse 24  
D-60323 Frankfurt am Main  
Germany

### BNY Financial Services

Hanover Building, Windmill Lane  
Dublin 2  
Ireland

### The Bank of New York Mellon (Luxembourg) S.A. - Italian Branch

Via Carducci 31  
20123 Milano  
Italy

### The Bank of New York Mellon (Luxembourg) S.A.

Aerogolf Centre, 1A Hoehenhof I-1736  
Senningerberg  
Luxembourg

### The Bank of New York Mellon

Jose Abascal 45, Planta 4  
28003 Madrid  
Spain

### The Bank of New York Mellon

Dubai International Financial Centre  
The Exchange Building 5 North, Level 6, Room 601  
P.O. Box 506723, Dubai  
United Arab Emirates

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## Latin America

### The Bank of New York Mellon

25 De Mayo 195, 6th Floor  
Buenos Aires  
Argentina

### The Bank of New York Mellon

Avenida Presidente Juscelino Kubitschek  
1455 - 6º andar  
04543 011 São Paulo - SP  
Brasil

### The Bank of New York Mellon

Torre Reforma 115 Building  
Paseo de la Reforma No. 115  
Col. Lomas de Chapultepec  
C.P. 11000  
Mexico

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## Canada

### BNY Trust Company of Canada

4 King Street, Suite 1101  
Toronto, Ontario M5H 1B6  
Canada

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## United States

### **The Bank of New York Mellon Trust Company, N.A.**

505 North 20th Street, Suite 950  
Birmingham, AL 35203

### **The Bank of New York Mellon Trust Company, N.A.**

1225 West Washington Street, Suite 126  
Tempe, AZ 85281

### **The Bank of New York Mellon Trust Company, N.A.\***

5730 Katella Avenue  
Cypress, CA 90630

### **The Bank of New York Mellon Trust Company, N.A.**

700 South Flower Street, Suite 500  
Los Angeles, CA 90017

### **The Bank of New York Mellon Trust Company, N.A.**

550 Kearny Street, Suite 600  
San Francisco, CA 94108

### **The Bank of New York Mellon Trust Company, N.A.**

1775 Sherman Street, Suite 2775  
Denver, CO 80203

### **The Bank of New York Mellon Trust Company, N.A.**

10161 Centurion Parkway, 2nd Floor  
Jacksonville, FL 32256

### **The Bank of New York Mellon Trust Company, N.A.**

900 Ashwood Parkway, Suite 425  
Atlanta, GA 30338

### **The Bank of New York Mellon Trust Company, N.A.**

2 North LaSalle Street, Suite 1020  
Chicago, IL 60602

### **The Bank of New York Mellon Trust Company, N.A.**

300 North Meridian Street, Suite 910  
Indianapolis, IN 46204

### **The Bank of New York Mellon Trust Company, N.A.**

614 West Main Street, Suite 2600  
Louisville, KY 40202

### **The Bank of New York Mellon Trust Company, N.A.**

301 Main Street, Suite 1510  
Baton Rouge, LA 70825

### **The Bank of New York Mellon Trust Company, N.A.**

601 Poydras Street, Suite 2225  
New Orleans, LA 70130

### **The Bank of New York Mellon Trust Company, N.A.**

222 Berkeley Street, 2nd Floor  
Boston, MA 02116

### **The Bank of New York Mellon Trust Company, N.A.**

719 Griswold Street, Suite 930  
Detroit, MI 48226

### **The Bank of New York Mellon Trust Company, N.A.**

911 Washington Avenue, Suite 300  
St. Louis, MO 63101

### **The Bank of New York Mellon**

385 Rifle Camp Road  
West Paterson, NJ 07424

### **The Bank of New York Mellon\***

2 Hanson Place  
Brooklyn, NY 11217

### **The Bank of New York Mellon**

101 Barclay Street, 21 West  
New York, NY 10286

### **The Bank of New York Mellon\***

111 Sanders Creek Parkway  
Syracuse, NY 13057

### **The Bank of New York Mellon\***

401 S. Salina Street  
Syracuse, NY 13022

### **The Bank of New York Mellon Trust Company, N.A.**

525 Vine Street, Suite 900  
Cincinnati, OH 45202

### **The Bank of New York Mellon Trust Company, N.A.**

Skylight Office Tower  
1660 West 2nd Street, Suite 830  
Cleveland, OH 44113

### **The Bank of New York Mellon Trust Company, N.A.**

6525 West Campus Oval, Suite 200  
New Albany, OH 43054

# BNY Mellon Corporate Trust Worldwide Locations (continued)

## **The Bank of New York Mellon Trust Company, N.A.**

Williams Center Tower I  
One West Third St., Suite 1005  
Tulsa, OK 74103

## **The Bank of New York Mellon Trust Company, N.A.**

1600 Market Street, Suite 1500  
Philadelphia, PA 19103

## **The Bank of New York Mellon Trust Company, N.A.**

525 William Penn Place, 7th Floor  
Pittsburgh, PA 15259

## **The Bank of New York Mellon Trust Company, N.A.**

One Financial Plaza, Suite 1435  
Providence, RI 02903

## **The Bank of New York Mellon Trust Company, N.A.**

919 Congress, 5th Floor  
Austin, TX 78701

## **The Bank of New York Mellon Trust Company, N.A.**

2001 Bryan Street, 11th Floor  
Dallas, TX 75201

## **The Bank of New York Mellon Trust Company, N.A.**

601 Travis, 16th Floor  
Houston, TX 77002

## **The Bank of New York Mellon Trust Company, N.A.\*\***

2220 Chemsearch Blvd., Suite 150  
Irving, TX 75062

## **The Bank of New York Mellon Trust Company, N.A.**

600 E. Las Cosinas Blvd., Suite 1300  
Irving, TX 75039

## **The Bank of New York Mellon Trust Company, N.A.**

919 East Main Street, Suite 1602  
Richmond, VA 23219

## **The Bank of New York Mellon Trust Company, N.A.**

Two Union Square  
601 Union Street, Suite 520  
Seattle, WA 98101

## **The Bank of New York Mellon Trust Company, N.A.**

330 E. Kilbourn Avenue, Suite 809  
Milwaukee, WI 53202

## **Australia**

### **BNY Mellon Australia Pty Ltd.\***

Unit 3, 5-15 Epsom Road  
Rosebery NSW 2018  
Australia

### **BNY Mellon Australia Pty Ltd.**

Level 2, 35 Clarence Street  
Sydney, NSW 2000  
Australia

## **Asia-Pacific**

### **The Bank of New York Mellon**

Level 12, Three Pacific Place  
1 Queen's Road East  
Hong Kong

### **BNY Mellon International Operations (India) Private Ltd.\***

Level 5, Tower VI, Cypercity  
Magarpatta City, Hadapsar  
Pune 411013  
India

### **The Bank of New York Mellon Trust (Japan), Ltd.**

Fukoku Seimei Building,  
2-2-2, Uchisaiwai-cho, Chiyoda-ku  
Tokyo 100-0011  
Japan

### **The Bank of New York Mellon**

Young-Poong Bldg., 23rd Floor, 33 Seolin-dong  
Chongro-ku. C.P.O. Box 4906  
Seoul 110-752  
Korea

### **The Bank of New York Mellon**

10th Floor Philamlife Tower  
8767 Paseo de Roxas  
Makati City 1200  
Metro Manila  
Philippines

### **The Bank of New York Mellon**

One Temasek Avenue  
No. 02-01 Millenia Tower  
Singapore 039192

# BNY Mellon Corporate Trust Regional Contacts

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## Europe, Middle East and Africa

**Michael Whelan**  
+44 207 964 8802

## Latin America

**Erin Courcey**  
+1 212 815 7138

## Canada

**Ross Neilson**  
+1 416 933 8506

## United States

Public Finance, Corporate Finance and  
Specialty Products

**Mark P. Brown**  
+1 770 698 5183

Structured Credit

**Andrew Zelter**  
+1 212 815 2142

## Asia-Pacific

**John-Paul Marotta**  
+852 2840 6633

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