Insights – Distressed Assets Q4 2016

Lehman products – time to say goodbye?

Is it worth to still hold on to investment products issued by Lehman Brothers? Or is it time to say goodbye, sell these products in the secondary market and redeploy the proceeds elsewhere? In this short note we provide investors with some background and a framework to make an informed decision. The two main dimensions are the amount of additional recoveries and the expected timing of these cash flows.

The filing of Lehman Brothers Holding Inc. ("LBHI") for Chapter 11 protection on September 15, 2008 started the largest and probably most complex bankruptcy proceeding in history. A myriad of Lehman investment products, such as capital protected or yield enhancing notes, were distributed to thousands of investors across Europe. Today these products still are among the most widely held illiquid legacy assets in investor portfolios. Many of these structures were issued by Lehman Brothers Treasury Co. B.V. ("LBT") backed by a guarantee of its parent LBHI.

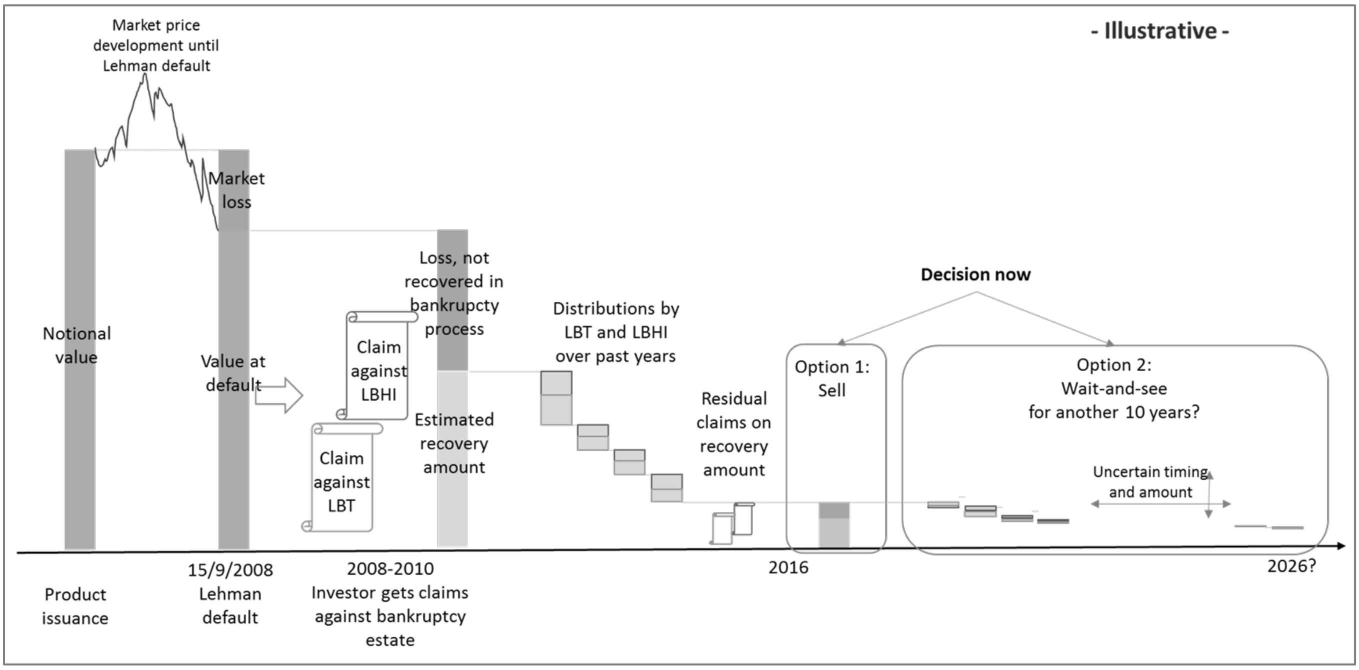

Figure: Illustrative recovery process for a Lehman investment product

When looking at the potential recovery amounts of these products the following factors need to be taken into consideration:

- **Product value at default**: Many investment products have incurred substantial mark-to-market losses during the unfolding of the sub-prime crisis and were valued well below their notional amounts at the default date. An investment product's claim value against the bankruptcy estate is determined by its market value on September 15, 2008 and limits the potential recovery amount. Across all LBT-issued products the average admissible amount is only 76% of the notional amount and can range from less than 5% to more than 100%.

- **Recovery through Lehman liquidation**: Lehman's liquidators are trying to recover as much value as possible through carefully selling off assets such as real estate and private equity investments. The amount ultimately recovered is yet unknown and will depend on how markets develop over the coming years. What is clear today is that the value of Lehman's assets are not sufficiently covering its liabilities. Depending on the seniority of a claim against Lehman, there is a very substantial loss that will not be recoverable.
- **Distributions to date**: Over the past eight years most of the higher quality assets have been sold off by the liquidators of Lehman and proceeds have been distributed to creditors through semi-annual distributions. Of course, the more has been distributed to creditors the lower the estimate for the remaining payouts. It is widely believed that more than half of the ultimate total recovery has already been paid out.

How long will it take to fully liquidate Lehman? When we look other complex and multi-jurisdictional insolvency proceedings, we see that the liquidation of LBHI to last for another ten years is quite likely. What is also evident is that future distributions tend to become smaller and smaller.

An investor owning Lehman products today faces the following decision:

- **Sell**: There are specialized buyers and intermediaries, such as Multiplicity, that facilitate secondary market transactions on Lehman bonds resp. claims against LBHI. The settlement of such transactions has become relatively standardized and easy to process. An investor can quite easily clean out his portfolio of residual Lehman products and reinvest the money.
- **Wait-and-see**: An investor can also hold on to his/her Lehman position and hope to collect distributions that exceed what is currently paid in the secondary market. As the market for defaulted bonds tend to dry up at some point, a plan to sell out the assets a few years down the road might not be optimal.

Please do not hesitate to contact us for an indicative pricing on your Lehman products, or any other impaired investments you may hold.

Thomas Ritter is a founding partner of Multiplicity Partners. He is responsible for the firm's distressed assets business and has more than 17 years of experience in alternative investment industry with focus on secondary markets, portfolio management and structuring. Prior to founding Multiplicity Partners, he held various roles at Horizon21, Man/RMF and Credit Suisse. Thomas holds a MSc in Finance from the ICMA Centre, University of Reading, and is a CFA and CAIA Charterholder

About Multiplicity Partners

Multiplicity Partners is an investment boutique specialised in providing liquidity solutions to holders of private market funds and distressed assets. The firm also offers a range of advisory and governance services across alternative assets.

Multiplicity Partners has been an active participant in the secondary market for fund interests and distressed assets since 2010, acting as buy- and sell-side advisor, investment manager and principal investor. The team has successfully completed dozens of transactions across a wide range of illiquid and complex financial assets and established a global network of industry contacts. Each partner contributes more than 15 years of relevant experience, giving us the collective capabilities to effectively identify, analyse and execute attractive investment opportunities in hard-to-value assets.

Multiplicity Partners is an independent and management-owned company. Personal accountability of senior professionals ensures quality of work, reliability and attention to details.

Multiplicity Partners is a member of the Financial Services Standards Associations (VQF), a self-regulatory organization in Switzerland pursuant to the Anti-Money Laundering Act – officially recognized by the Swiss Federal Financial Market Supervisory Authority (FINMA). The company is authorized by FINMA to distribute collective investment schemes to qualified investors in Switzerland. Multiplicity Partners is audited by PricewaterhouseCoopers (PwC), Switzerland.

Multiplicity Partners is a member of Invest Europe and an Associate Member of SECA (The Swiss Private Equity & Corporate Finance Association).

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