Jefferies Insights
OCTOBER 2017

Dear Clients / Partners,

Whether you are in the investment management business or running a public or private company, you are faced with the challenges of managing people who have a myriad of options. To make it even more complex, you need to do this while you are trying to make smart investment decisions. We thought long and hard about both of these and wanted to share with you our thoughts and observations about the similarities of both challenges. We hope this letter, which we believe reflects the Jefferies culture, gives you more of a sense of us and Jefferies. More importantly, we hope it may help you and your people put some important topics in perspective. As always, please accept our sincere thanks for trusting us with your business.

Careers or Investing: Compelling Opportunity vs. Merely Intriguing

At a recent breakfast with a dozen of our analysts who had recently completed their first year at Jefferies, a question was asked about our own personal career paths. This was in the context of discussing our juniors' careers and the forks in the road they anticipate will await them in their future. In explaining our own career decisions, what became clear is that each of our decisions were ultimately pretty darn easy and borderline obvious. If after doing the hard work an opportunity was truly compelling, we took it. If it wasn't, we moved past it and never looked back. Jefferies was easy for us because it was a true Wall Street firm with incredible entrepreneurial spirit and culture, had a meaningful and important foundation that could be built upon, and was the size that a new business, team or even just one individual could have a meaningful impact. In our minds, these characteristics would afford us a chance to have a career with something we both valued – purpose. (As an aside, while clearly biased, we strongly believe that each of these important boxes are easily checked today at Jefferies – perhaps more so than ever.) As we said to these young future leaders who have been told by many that working in an investment bank is a perfect first stop on a journey, perhaps the next stop only makes sense if it too is "compelling," not just "intriguing." And by the way, perhaps the firm they are with today is the best firm and opportunity they will ever know.

The thought of "compelling" as the linchpin of major career decisions led us to recognize that the same is true for investment decisions. The work involved with investing includes value assessment at entry point, ability to help add long term value to the investment, understanding the short term and long term competitive position, and the ability to invest enough capital to justify the amount of time it will

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take to achieve appropriate compounded long-term returns. Downside scenarios and volatility assessment are also critical components to the investment process.

Our experience is that affirmative decisions to pivot and take a new job or boldly make a new investment should only derive from a conclusion of "compelling opportunity," not a "merely interesting" chance to follow the direction of the often wrong herd. One can find that the totality of the facts make clear that an opportunity is distinct or perhaps unique, and only then is it time to pounce. If a handful of the many factors we just highlighted line up but one or two of them do not, act at your own peril and recognize you are flipping a coin with your valuable career or investable cash hanging in the balance.

Evidence of what we are saying can be found in the track records of great investors. What they all have in common is that they tend to pull the trigger selectively, generally very selectively. Whether it's Warren Buffet, Carl Icahn, or George Soros, they are prepared to back up the truck when they see clear opportunity, but aren't afraid to sit on their hands for long periods of time in which nothing compelling presents itself. They never find money burning a hole in their pockets. At Jefferies and our parent company Leucadia, we try to adhere to this same discipline. Often, it is easier said than done.

Similarly, those that have gone furthest in their careers or done the most good and made the most progress in their lives generally don't quit lightly and don't change focus without a compelling reason. You didn't see Jeff Bezos, Howard Schultz or Tilman Fertitta panic or "bolt" when things inevitably got tough. Great leaders persevere and help solve the problems, and that is what makes them leaders. While writing this actually makes both of us squirm, we are personally approaching 30 and 20 years, respectively, at Jefferies. We joined Jefferies only after the lights went out at our prior firms – in one's case, the challenges were insurmountable and, in the other, it was one merger too many. All this being said, we also acknowledge that sometimes (not as often as many think) the new opportunity is too perfect to pass up and in that case, the right decision may be to leave.

It is easy to buy stocks and bonds, do deals or change jobs. It is difficult to be successful, to have the discipline of a high bar in decisions and to persevere through thick and thin times. In our humble opinions, maintaining patience, keeping perspective, doing the hard work, and persevering and being unrelentingly disciplined in one's decisions pays off in the long term.

We wish all a happy career and healthy investing,

Rich and Brian

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Economics and Strategy

Expensive + Expensive = Cheap

This past August was one of the least eventful for financial markets in modern history. The S&P went nowhere while front end rates rallied a meager 20bps. Jackson Hole was a dud. The economic data came through largely as expected. And there were no meaningful political accomplishments from the new administration.

We see two main drivers going forward for a 'spoos and blues' trading structure ('Spoos + Blues' is a long S&P position hedged with 4-year forward Eurodollar interest rate futures):

1. A positive supply shock induced by deregulation, which will continue to keep growth and employment strong while inflation wanes
2. The wind-down of a potentially Machiavellian Yellen Fed, and the rise of a market-backstopping Trump Fed

It's the latter point which became crucial to our reengagement in 'spoos and blues' earlier this summer. Recall that in Janet Yellen's June press conference, and then again in her July semiannual congressional testimony, she backed away from the word transitory when describing the consistently low inflation prints from the first half of the year. Up to that point she had tried to dismiss this weakness so as to continue with a stepped-up accommodation removal process (a posture that I have maintained had a strong political motivation). And to be sure, she was quite hawkish for the first half of 2017. Post-election Janet raised rates in December, March, and June. Further, she brought expectations for the balance sheet normalization process into 2017, when most folks had thought it would kick off in 2018. Nonetheless, by the middle of this year there was nowhere for Janet to hide – she had to give up her hawkishness given the inflation data.

Janet's retrenchment signaled the end of political risks associated with a Machiavellian Fed – risks that had kept us out of both spoos and blues since the election. In essence our "Lil' Janet" found herself handcuffed by the data. And that opened up a beautiful entry back into risk parity. Now you may look forward and ask why the upcoming Trump Fed will be so positive for risk parity? Some are forecasting that monetary purists such as John Taylor, Kevin Warsh, or Glen Hubbard will get the chair, and that would surely create a rocky road for spoos and blues. I however am betting against these folks. I believe Cohn was floated for a very specific reason. He is not an academic economist, and he has no strong monetary policy doctrine. If Trump and his advisors are clever, they will stick with someone just like that. They don't need a QE-hating, Taylor rule-following, rate-normalizing academic type in the seat. They need a street-smart banker who will make sure that financial markets are backstopped into the 2018 midterm elections and beyond. They need a political operative with little, or preferably no, monetary policy doctrine.

To this point it should not be lost on anyone that Trump is old enough to remember the extraordinary public battles between LBJ and Bill Martin in the 1960s. The last thing Trump wants is an independent and uncooperative FOMC like LBJ had on his hands. And while Cohn may have blown his chances at the job, there are plenty of other Cohn-like figures who fit the political parameters. Mnuchin could take it. Or any one of a number of former or current bank CEOs could be in the mix. In that sense I see no reason for folks to get bent out of shape if Cohn is discarded. The key point is that Trump will appoint someone (actually a set of people) who will help him further his political agenda. This of course requires backstopping financial markets, not ranting about monetary policy purity.

In the end this new Fed will not be fighting some ghost of inflation, nor will it whine about balance sheet size or overly accommodative monetary policy. Of course, if the economy and markets are doing well, this new guard will raise rates a few more times and wind the balance sheet down, but there will be no Bill Martin types who act preemptively against inflation risks. Further, and more importantly for risk parity trades, if markets wobble and Trump's economic record starts to erode, they will quickly backstop and juice the markets whether inflation risks are elevated or not. The Trump Fed structure, along with a strong positive supply shock from deregulation, is about as good as it gets for risk parity. It is the perfect backdrop for spoos and blues.

I must say though, I did have many folks push back on this view over the summer by claiming that both equities and bonds look expensive. They ask, how can I essentially be a buyer of both? My response to that is simple. While on their own each asset class may show some hints of expensiveness, together, with their natural dual-hedging properties you get an "expensive + expensive = cheap" outcome. Remember, spoos and blues is really just a bet on the Fed reaction function, and when Trump won, there was a real risk Janet would NOT backstop him in the event of a hiccup. There was also a material risk she would try to become a spanner in the works. The reaction function thus became blurred. But as stated above, earlier this summer Janet's power to disrupt was usurped by the data—and now her time is up. A new set of sheriffs are coming to town, and they are not the sort to take the Jell-O shots away or act as a thorn in the administration's side. They are the ones who will be serving Billionaire Martinis upon any sign of market adversity.

— David Zervos, Chief Market Strategist

A Ray of Sunshine

Global equities produced broad-based US$ returns through the third quarter. A weak dollar, firming commodity prices and expanding Purchasing Managers' Index (PMI) numbers lifted global indices despite the tensions on the North Korean Peninsula. While the developed world central banks are talking tighter policy, Brazil loosened rates by 100bp. Relaxed monetary policy in EM is helping global trade to recover and providing a useful backstop to growth. We believe equity markets are benefiting from a 'disinflationary boom' (i.e., low inflation that keeps central bankers on hold alongside blossoming growth).

The rising tide of growth has lifted many boats – shipping, shipbuilding, copper steel, as well as silicon wafer makers – industries that many investors had written off 24 months ago. Even Greece's PMI manufacturing hit a nine-year high in August! Aside from better growth, one of the more visible improvements has been better capex and also the first signs of higher wages. After a long period when companies hoarded their profits, there is evidence that the money is being recycled into the economy through investment spending and better remuneration. This is great news for equity markets.

China continues to run a loose monetary and fiscal policy, underwriting domestic profits, while Japan's earnings appear to have been less influenced by a weaker yen. In Europe, the strength of the euro has become a concern but intra-European trade has picked up while retail sales remain firm. Meanwhile U.S. multi-nationals have enjoyed a renaissance helped by the week greenback.

— Sean Darby, Global Head of Equity Strategy

U.S. Outlook – Federal Reserve Initiates Balance Sheet Normalization, Refocuses on Rates

At the September 20 FOMC meeting, the Federal Reserve announced a change in the System Open Market Account (SOMA) reinvestment policy and the beginning of balance sheet normalization in the U.S. effective in October.

The pace of U.S. balance sheet normalization had previously been laid out in the "Addendum to the Policy Normalization Principles and Plans" that the FOMC released in June. The process of rolling-off U.S. balance sheet security holdings is scheduled to begin slowly, with the initial roll-off caps for Treasuries of $6 billion and a $4 billion cap for MBS. The size of the caps will increase by $6 billion at 3-month intervals for Treasuries and increase by $4 billion at 3-month intervals for MBS. The maximum roll-off will be $30 billion for Treasuries and $20 billion for MBS. The FOMC projections indicate that the normalization process would reduce the size of the Federal Reserve SOMA balance sheet security holdings by $1.75 trillion over the next three and one half years.

There are still significant issues about the U.S. balance sheet normalization process that need to be addressed. For example, it is not clear why the interest rate normalization process is data dependent, but the balance sheet normalization process would only be altered in the event of a “material deterioration in the outlook” that the FOMC could not address with adjustments to the federal funds rate.

The FOMC also remains noncommittal about the target size of balance sheet securities holdings and has been ambiguous about the longer-term goal for the composition of such. While the balance sheet normalization process that will be initiated in October will reduce the size of the balance sheet, it will not return the composition of SOMA security holdings to the pre-crisis composition because it will reduce but not eliminate all of the MBS holdings. Pre-crisis, roughly one third of SOMA securities holdings were comprised of Treasury bills, but the balance sheet normalization process does not increase bill holdings.

So, the FOMC still has work to do in order to normalize both the size and the composition of securities holdings.

In addition, Fed policymakers left the Interest Rate on Excess Reserves (IOER) and fed funds rate target range unchanged at the September 20 FOMC meeting but signaled that the FOMC intends to resume raising rates going forward. The combination of the September 20 policy statement and the Summary of Economic Projections (SEP) indicated that the FOMC is ready to refocus attention back to rate normalization once the balance sheet normalization process has been initiated in October. This reinforces the message from reserve bank presidents Bill Dudley, Loretta Mester and Esther George, who have all made recent public comments suggesting the FOMC is ready to resume rate normalization, with the next rate hike possibility being as early as the December FOMC meeting. The SEP also kept three rate hikes on the table in 2018.

Finally, the September 20 policy statement acknowledged that the recent spate of hurricanes will cause “storm-related disruptions” to U.S. economic activity in the near-term and also recognized that increases in prices of “gasoline and some other items in the aftermath of the hurricanes will likely boost inflation temporarily.” Nonetheless, policymakers were inclined to continue along the path of normalizing U.S. monetary policy because “past experience suggests that the storms are unlikely to materially alter the course of the national economy in the medium-term.”

Nonetheless, the confusing picture that is likely to emerge from the high frequency data releases in the months ahead will complicate the policy decision process in the U.S.

— *Ward McCarthy, Chief Financial Economist*

European Outlook – ECB and BoE Prepare to Adjust Policy; EU and UK Struggle to Adjust Relations

Slowly but surely the global central banks are taking steps to normalize policy, with the U.S. Fed preparing to reduce its balance sheet, the Bank of England (BoE) aiming to raise rates in the coming months, and the ECB looking to ‘adjust’ QE purchases next year.

In some ways, the ECB’s position is not all that different to 2015, before QE started: headline inflation remains subdued, the official core inflation forecasts are again being revised lower, and long term inflation expectations and wage growth remain adrift of where the ECB would like them to be. And the currency, a tailwind boosting growth in 2016 and 2017, could soon become a drag.

Nonetheless, the confidence surveys across the region are robust, unemployment is falling, and the ECB feels justified to start phasing out some of the extraordinary stimulus it had been providing. The meeting on 26 October will be key, as the ECB outlines its actions for the first half of 2018 at least. With the Governing Council weary of an unwarranted tightening in monetary conditions, the markets are preparing for a gradual reduction in monthly QE size; but anything more aggressive, such as an outright taper, would surprise expectations.

Peeking ahead to a post-QE world where the central banks are not indiscriminately purchasing large chunks of government debt, individual country fundamentals could start to matter much more. The pace and effectiveness of economic reforms in France will be more closely scrutinized. Similarly, as next year's Italian elections approach, the outlook for 2018 is less certain without the safety net of indefinite central bank intervention. There will also be more uncertainty about the role that Germany may be prepared to play in any future European bailout after the election result that reduced Angela Merkel's domestic standing and authority.

In the UK, the policy debate is heating up, both with respect to Brexit and the BoE. The Monetary Policy Committee (MPC) is preparing to reverse the emergency rate cut of 2016, with a move in November or in February in play. The collective judgement seems to be that Brexit reduces the UK's trend growth rate, which means that the MPC may look to raise interest rates even on what are seen as relatively soft GDP prints.

As far as Brexit negotiations are concerned, Theresa May signaled her preference for a transitional arrangement in 2019 and 2020 with the UK contributing to the EU Budget in exchange for maintaining the existing trading arrangements. But that still doesn't address the issue of the broader divorce bill, nor the future trade relationship after 2020 and, importantly, Ireland. Fifteen months after the Brexit vote, the UK outlook remains murky, with the negotiations seemingly producing limited progress. FULL REPORT

— *David Owen, Chief European Financial Economist*
— *Marchel Alexandrovich, European Financial Economist*

Actionable Ideas for Companies and Sponsors

MERGERS AND ACQUISITIONS

Mitigating Deal Risks Associated with Chinese Acquirors

Through August 2017, China outbound M&A volume was 50% lower than the record $181 billion seen through August of 2016. The major factors driving this slowdown are a series of capital constraints formally implemented by Chinese authorities designed to restrict capital movement out of China and stabilize their currency. The principal components of these regulations restrict foreign transactions which are: (i) greater than $1 billion outside the acquiror's core industry or for the purchase of real estate, or (ii) any transaction greater than $10 billion. Compounding the uncertainties of China's regulations is a heightened level of scrutiny from foreign governmental authorities for national security reasons, exemplified by the U.S. government in September 2017 blocking the $1.3 billion acquisition of Lattice Semiconductor by Canyon Bridge, a Silicon Valley private equity firm funded by the Chinese government.

Given this backdrop, sellers of businesses to Chinese acquirors should demand additional protections to address the internal and external headwinds Chinese buyers will continue to face including (i) demanding larger reverse break fees – there are current examples of reverse break fees as high as 10% of deal value compared to typical 3-5% reverse break fees, (ii) attaining escrow deposits at the signing of the transaction, (iii) shortening the seller's time period to terminate e.g. the drop date, and (iv) conducting up-front due diligence on any Chinese buyer's ability to fund a transaction, including requiring proof of access to funds.

Pre-Emptive Buyouts Now Dominating the Private Equity Landscape

For the first time since 2006, secondary buyouts in 2017 eclipsed sales to corporate buyers, and with this trend, financial sponsors have increased their focus on pre-emptively securing transactions. Pre-emptive strategies are taking many forms including: (i) offering risk reducing terms including public company contract terms and fully backstopped equity commitments to eliminate closing risk and reduce time to closing; and (ii) making pre-emptive offers during auction processes which include completed due diligence, committed financing and fully negotiated contract terms early in the auction process. In recent sale processes completed by Jefferies for Duravant (sold by Odyssey Investment Partners), First Watch Restaurants (sold by Freeman Spogli), PDC Brands (sold by Yellow Wood Partners) and Truck Hero (sold by TA Associates), financial sponsors have aggressively pushed to accelerate or truncate the process to improve their probability of winning.

Numerous M&A Strategies Being Pursued in Response to Perceived Threat of Amazon

The breadth of Amazon's online and offline presence has had a dramatic impact on the strategic response by companies across many segments of the retail industry to counter the perceived and actual competitive impact of Amazon's powerful market position.

To date, strategic responses have fallen into three broad categories. First, some retailers have chosen the path to go private to avoid the pressure of quarterly earnings, as they take the steps to transform their businesses in response to Amazon's impact. This includes Staples Inc., which announced its $6.6 billion go-private sale to Sycamore Partners in June 2017, and the Nordstrom family, which in September announced the selection of Leonard Green Partners as their partner in preparation for a formal offer to take the company private. Second, offline retailers have bolstered their online capabilities by acquiring successful online retailers. This includes Wal-Mart, which acquired both the online discount retailer Jet.com for $3.3 billion and Bonobos, the men's online apparel company for $310 million, and PetSmart Inc, which acquired Chewy's.com, the online pet food and products company for $3.4 billion. Finally, other companies have pursued more offensive M&A strategies. This includes Home Depot, which acquired BlackLocus, a retail data analytics and tools company, to drive innovation for nationwide retail solutions across online and offline sales.

EQUITY CAPITAL MARKETS

Record SPAC Issuance Will Continue Throughout 2018

With 24 SPAC IPOs priced this year, 2017 has become the most active year for SPAC IPOs in over a decade. We expect SPAC issuance to continue to be strong throughout 2018 because of a number of factors including: (i) the universe of SPAC sponsors has expanded beyond executives with deep sector expertise and public market experience to now include financial sponsors and venture capital firms; (ii) the emergence of more favorable SPAC structures; (iii) dedicated SPAC institutional investors who are now able to recycle/reinvest capital into new SPAC IPOs; (iv) sector-focused institutional investors, who are increasing their participation in SPAC IPOs, as they are now seeing evidence that the SPAC structure can work; and (v) the successful completion of acquisitions on the back end. Regarding the latter, in 2017 YTD, nine SPACs have completed acquisitions, including three acquisitions between $850 million and $3.8 billion, and an additional 13 acquisitions are pending.

Recent Changes to the JOBS Act Broadens to All IPO Issuers and Selected Follow-on Issuers

Recent changes to the JOBS Act have given a vastly larger number of issuers the well-known advantages versus traditional SEC filing strategies, including timing flexibility, confidential SEC feedback prior to any public filing and limiting exposure to market volatility. Specifically, effective July 10, 2017, the JOBS Act now allows confidential submissions of draft registration statements for All IPOs, including submissions by issuers that do NOT qualify as Emerging Growth Companies. In addition, confidential submissions can now be deployed for follow-on issuances as long as the SEC registration is filed within 12 months of an initial registration statement; and since the new follow-on rules went into effect, four companies have utilized confidential filings for S-1 follow-on offerings.

The Return of a Robust European Follow-on Market

On the back of strong fund inflows, $25 billion of equity issuance occurred in Europe in July and August, an 80% increase over last year, and in September, $17 billion of overnight follow-on offerings priced, the highest monthly volume in over two years. This volume included six $1+ billion transactions successfully completed in France, Germany and the Netherlands, pricing at an average discount of 2.2%, tighter than the 3.7% average for $1+ billion transactions in the first eight months of 2017. Numerous sectors contributed to this strong issuance volume, including financials, real estate, technology, power, telecom and retail. We expect this European trend of overnight follow-on offerings to continue, as investors look for alpha in follow-on transactions amidst a favorable backdrop for European equities.

DEBT CAPITAL MARKETS

Record Strength of Leveraged Finance Market Driving 100% First-Lien Refinancing and Access to the Subordinated Note Market

The strong leveraged loan market has driven first lien leverage levels to record levels, providing companies with the opportunity to refinance into less expensive "all-first-lien" debt structures. Even after accounting for the breakage cost from paying the call premium on the junior debt, the interest savings are typically substantial. In addition, the strength of the high yield market is allowing issuers to tap the often-closed Subordinated Note Market, allowing issuers to raise incremental financing beyond the levels that senior debt is restricted to. Recently we have seen Subordinated Notes used to fund acquisitions, refinance other debt and to fund dividends. Most recently, Golden Nugget raised $670 million Senior Subordinated Note priced at par with an 8.75% coupon, as part of a larger dividend financing that also included a $1.045 billion Incremental Term Loan and a $745 million Senior Note add-on. Jefferies acted as lead left bookrunner on the Golden Nugget financing.

Shift to Secured Bonds When Ratings Impact Loan Investor Demand

Below the corporate family rating of B3 with Stable outlook, the majority of 1st lien term loan demand typically falls away, resulting in unacceptable outsized yield levels for issuers. In addition, at these rating levels for smaller issuers, maintenance covenants are typically required by loan investors, which also is unattractive to a large subset of issuers. Recently we have seen several instances of companies working around these market constraints by shifting their financings to Senior Secured Notes. By moving to the high yield bond market, issuers can access a much deeper investor base that is not hampered by strict ratings constraints and can avoid maintenance covenants. We recently saw this shift to work around credit ratings during the $7.3 billion financing of Avantor's acquisition of VWR Corp. when Avantor downsized their term loans and shifted to $1.5 billion 7-year Secured Notes and €500 million of 7-year Secured Notes. We also saw this shift at FXI Holdings, which launched Senior Secured Notes to avoid potential term-loan maintenance covenants. Jefferies was lead left bookrunner on the FXI Holdings financing and a bookrunner on the Avantor financing.

Use of Partial Paydowns to Reprice Loans to Record Low Speeds

As companies look to take advantage of the record leveraged loan market, we have seen repricings try to break new boundaries below L+200. As with any repricing action, lenders have the option to be paid down at par, and when issuers are pursuing record breaking pricing levels, this possibility is significantly heightened. To mitigate this potential outcome, we have seen companies offer partial paydown of the term loan from either cash on hand or newly raised bonds to improve the likelihood of success and to cover these potential drops.

RESTRUCTURING AND RECAPITALIZATION

Utilization of IPCOs or BrandCos in Retailing Restructuring Transactions

As domestic retailers continue to face mounting secular challenges and an unprecedented wave of bankruptcy filings, institutional investors, strategic buyers and retailers themselves are increasingly evaluating the use of both intellectual property companies (“IPCOs”) and BrandCos to attract capital and to redefine their business models.

Regarding IPCO structures, both Claire’s and J Crew have recently used IPCOs to raise incremental capital despite high leverage levels on their respective balance sheets. Claire’s established an unrestricted subsidiary that holds 17.5% of Claire’s U.S. intellectual property and this subsidiary backed a $130 million loan and a debt exchange that postponed certain of Claire’s maturities. J. Crew also transferred trademarks and other intangible assets valued at $250 million into an unrestricted IPCO subsidiary. Regarding BrandCos, several strategic and financial investors have acquired the intellectual property, including the brand names, of numerous distressed retailers either on a stand-alone basis or in partnership with others who will operate a scaled down version of the retailer’s store footprint or liquidate the assets. This structure has been used in transactions for Aeropostale, Frederick’s of Hollywood, Sharper Image and BCBG.

MUNICIPAL FINANCE

Using Customized Defeasance Refundings to Refinance High Coupon Build America Bonds (BABs)

BABs are taxable municipal bonds with a federal subsidy of 32.7% of the coupon payment. More than $181 billion of BABs were issued in 2009 and 2010. Many of these BABs included a standard muni 10-year par call, and therefore, high coupon BABs with par calls in 2019 and 2020 may be able to be advance-refunded for savings at today’s low rates. However, issuer’s contemplating refunding BABs should be aware that the current interpretation of the tax regulations indicates that legally defeased BABs will be treated as reissued for tax purposes, resulting in the termination of the federal subsidy. Issuers therefore should consider using advance refundings that do not result in the legal defeasance of their BABs, such as crossover or economic defeasance refundings.

Best Research Ideas

AMERICAS

Semiconductors – The 4th Tectonic Shift in Computing: To a Parallel Processing / IoT Model

Jefferies believes the computing industry is at the start of the fourth major development towards a parallel processing / Internet of Things (IoT) model. The firm forecasts a paradigm shift driven by lower memory costs, cheap data storage and improvements in parallel processing hardware and software. Jefferies believes INTC has the most to lose as the key data center incumbent, and NVDA has the most to gain as the role of MPUs transitions to GPUs. NVDA’s position will be entrenched for years due to their prior investment in CUDA, their market leading parallel processing platform, and Nvidia’s Titan X can have up to 6,000 GPU cores, two full orders of magnitude higher than the highest core count MPUs. Jefferies views NVDA, AMD, XLNX, CAVM, MXIM, TXN, ADI and MCHP as the primary beneficiaries of the shift to the parallel model and upgraded CAVM and XLNX to Buy in conjunction with this report. FULL REPORT

— Mark Lipacis, Equity Research Analyst, Semiconductors

U.S. Equity Strategy – JEF’s SMID-Cap Themes: 8 is Enough, Go with the Momentum and 7 Other Themes

Jefferies added momentum to the list of preferred SMID-Cap strategy themes. When performing the monthly factor analysis for SMID-Cap equities, the firm found that price momentum was coming back into favor for the group. Specifically, price momentum usually works well for small caps and, seasonally, acts best in 4Q. The preferred momentum factor highlighted was the one month change in the 200DMA. The additional seven SMID-Cap themes are: growth, size, quality, overseas revenue exposure, healthy balance sheet, M&A and active over passive. FULL REPORT

— Stephen DeSanctis, U.S. Equity SMID-Cap Strategist

U.S. Insights – Research Rundown: The Latest Franchise Picks and Focus Stocks

Jefferies published the third installment of the "Research Rundown" report, revisiting the Jefferies Franchise Picks List, which has outperformed the S&P 500 by 1674bps since its inception in December 2013. Franchise Picks include stocks with differentiated analysis, where risk reward skews compelling, and analyst conviction is high. Jefferies also refreshed the firm's Focus List, consisting of 90 institutionally relevant stocks in which Jefferies analysts have observed elevated interest. Franchise Picks are also on the Focus List, which includes many top picks for the respective analysts. Since publishing the report, Jefferies downgraded NWL to Hold and removed the stock from the Franchise Pick list, as the thesis that synergies would drive upside has played out. Jefferies also recently added GPS to the list with a sum-of-the-parts analysis suggesting 50%+ upside from current levels, and Jefferies believes the Old Navy brand is worth significantly more than currently implied by GPS' enterprise value. Stocks currently on the Franchise Picks list are: ABBV, ATVI, ALLY, GOOGL, BLL, BA, CVX, DISH, DLPH, DXC, FLT, GPS, HAIN, IR, KEY, MPC, MUSA, NVDA, OC, PX, PYPL, SRCL, TXT and UAA. FULL REPORT

— Jefferies U.S. Equity Research

EMEA

Yoox Net-A-Porter – On Form, On Time, Online: Initiating with a Buy

YNAP is the only quoted pure play on Digital Luxury, anywhere. Online is the only channel expected to show strong growth in the next five+ years. YNAP is the global leader in the space, and 2017 is the year when its recent aggregation is being managed and engineered to start delivering growth, margins and cash in 2018. Jefferies' Buy rating reflects our view of significant upside in the stock, with a 12-month price target of €33. FULL REPORT

— Flavio Cereda Parini, Equity Research Analyst, European Luxury Goods

Roche – TOGA Party: Opportunity in the Face of Adversity: Reiterate Buy, Raise PT to CHF290

New product launches and indications are being underestimated for Roche while the fear of biosimilars dominates. Jefferies has laid out base business, royalty income/ expense, pipeline, biosimilar erosion and margin expectations in detail, while demonstrating above consensus revenue and EPS, increasing the price target to CHF290 and highlighting the potential for special dividends and accretive M&A as cash continues to build. FULL REPORT

— Jeffrey Holford, Equity Research Analyst, Global Pharmaceuticals

ASIA

Japan Equity Strategy – Board Structure Reform: Progress Stalling

Two years after Japan's Corporate Governance Code was enacted, Jefferies finds that progress is stalling. However, changes over the past two years show that the majority of companies are open to reform. Further progress requires tightening the Corporate Governance Code and revamping the JPX400. Version 3.0 of Jefferies' Board Structure Reform report rates and ranks the boards of all TOPIX500 index companies. After a detailed review, Jefferies has bad news and good news: The bad news is that progress is stalling. The good news is that only 20-30% of companies are opposed to reform. FULL REPORT

— Zuhair Khan, Equity Research Analyst, Japan Strategy

India Healthcare Services – Unmet Demand Conundrum: Initiating Coverage

Indian hospitals need to alter their business model to focus on affordable healthcare and patients outside Tier-I cities to sustain their rich valuations. The premium segment is slowing on rising competition and narrowing supply demand gap with margins under pressure too. Growth in most existing hospitals has moderated over the past eight quarters, led by increased competition and a narrowed supply-demand gap in the premium segment. Hospital managements have also indicated that growth (single digit) will be largely led by pricing and mix. Jefferies expects margins to be under pressure due to competition (higher costs) and government policies (lower pricing). In this context, the firm initiates coverage of NARH and HCG with Buy, which appear best placed given their growing presence outside Tier-I cities. Additionally, Jefferies initiates on APHS with Hold as growth and margin challenges may endure. FULL REPORT

— Piyush Nahar, Equity Research Analyst, India Healthcare

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NOTABLE RECENT TRANSACTIONS

Real Estate July 2017
CLUBCORP — The World Leader in Private Clubs
$2,190,000,000
Sale to
Apollo Global Management
Joint Financial Advisor

Consumer September 2017 / August 2017
STAPLES
$3,900,000,000
Credit Facility to Finance Acquisition by
Sycamore Partners
Joint Lead Arranger
$1,000,000,000
Senior Unsecured Notes Offering
Joint Bookrunner

Energy September 2017
MPLX Energy Logistics
$1,050,000,000
Acquisition of pipelines and facilities from **Marathon Petroleum Corp.**
Sole Financial Advisor

Technology August 2017
neustar
$1,750,000,000
Credit Facility to Finance Acquisition by
Golden Gate Capital and **GIC Special Investments**
Joint Lead Arranger

Consumer September 2017
The Nature's Bounty Co.
$2,250,000,000
Credit Facility to Finance Acquisition by
KKR
Joint Lead Arranger

Healthcare July 2017
CHILTERN
$1,200,000,000
Sale to
Laboratory Corporation of America
Sole Financial Advisor

Gaming September 2017
Golden Nugget
$2,561,000,000
Credit Facility
Joint Lead Arranger
$1,415,000,000
Senior Unsecured and Senior Subordinated Notes Offering
Joint Bookrunner

Industrials July 2017 Pending
EQT
$875,000,000
Acquisition of 90% interest in
Global Gateway South
Sole Financial Advisor

Industrials August 2017
HAYWARD
$1,385,000,000
Credit Facility to Finance Acquisition by
CCMP Capital Advisors, **MSD Partners** and **Alberta Investment Management Corp.**
Joint Lead Arranger

Healthcare August 2017 Pending
ENVIGO
$924,000,000
Merger with **Avista Healthcare Public Acquisition Corp.**
Sole Financial Advisor

Finance July 2017
Metro Bank
£278,000,000
Common Stock Offering
Joint Bookrunner

Real Estate August 2017
Digital Realty
$1,350,000,000
Senior Unsecured Notes Offering
Joint Bookrunner

Finance September 2017
automotiveMastermind
$500,000,000
Plus $57,000,000 earn-out
Sale to
IHS Markit Ltd.
Sole Financial Advisor

Industrials July 2017 / June 2017
DURAVANT
$870,000,000
Credit Facility to Finance Acquisition by
Warburg Pincus
Joint Lead Arranger
Undisclosed
Sale to
Warburg Pincus
Lead Financial Advisor

Healthcare August 2017
PRA Health Sciences
$530,000,000
Acquisition of
Symphony Health Solutions
Sole Financial Advisor

Consumer July 2017
Floor & Decor
$429,000,000
Common Stock Offering
Joint Bookrunner

Healthcare August 2017
Surgery Partners
$1,735,000,000
Debt Financing Package to Finance Acquisition of
National Surgical Healthcare
Joint Lead Arranger
$400,000,000
Tender Offer and Consent Solicitation for Senior Notes
Sole Dealer Manager and Sole Solicitation Agent

Technology July 2017
Mitel
$530,000,000
Acquisition of
ShoreTel, Inc.
Sole Financial Advisor

Finance August 2017
enova
$250,000,000
Senior Unsecured Notes Offering
Sole Active Bookrunner

Technology September 2017 Pending
Imagination
£550,000,000
Sale to
Canyon Bridge Capital Partners, Inc.
Joint Financial Advisor

Technology July 2017 / August 2017
syncsort + Vision Solutions
$1,260,000,000
Sale to
Centerbridge Partners, L.P.
Joint Financial Advisor
$865,000,000
Credit Facility to Finance Acquisition by
Centerbridge Partners, L.P.
Joint Lead Arranger

Media August 2017
tv azteca
$400,000,000
Senior Unsecured Notes Offering
Joint Bookrunner

Consumer July 2017
BCBGMAXAZRIAGROUP
$460,000,000
Restructuring and Sale to
Marquee Brands LLC and **Global Brands Group Holding Limited**
Financial Advisor to the Company

Healthcare July 2017 / August 2017
CERTARA
$850,000,000
Sale to
EQT Partners AB
Lead Financial Advisor
$270,000,000
Credit Facilities to Finance Acquisition by **EQT Partners AB**
Joint Lead Arranger

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(as of August 31, 2017)

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