

Confidential Presentation to:

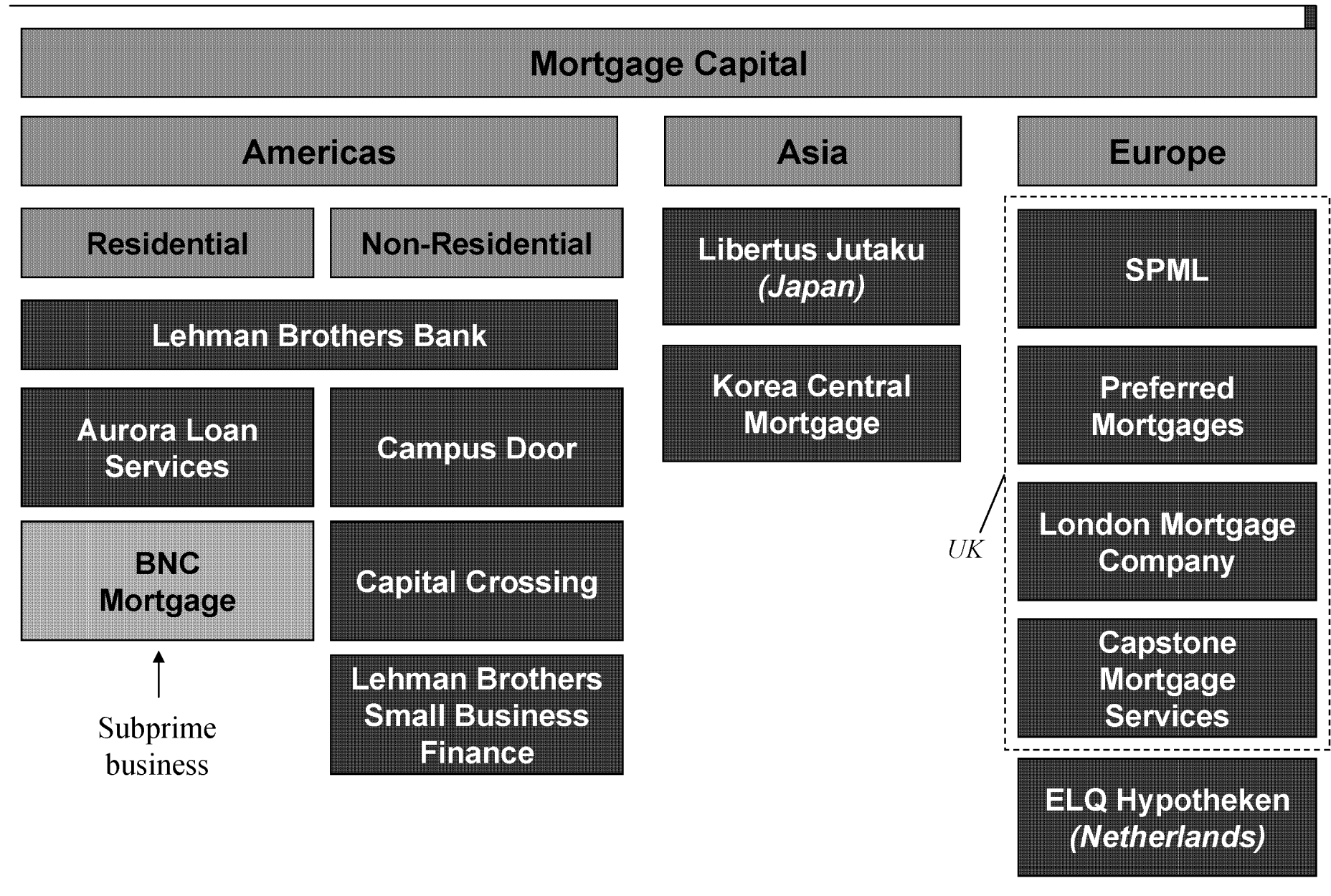
Board of Directors

Update on Lehman Brothers' Subprime
Mortgage Origination Business

March 20, 2007

LEHMAN BROTHERS

Mortgage Capital Organization



I-Bank Purchases of Residential Mortgage Originators

I-Bank	Mortgage Business	Acquired	Credit Quality	Price (\$MM)
Lehman Brothers	London Mortgage Co. (U.K.)	May 2006	Non-conforming	\$12
	SIB Mortgage Corp	March 2004	Alt-A	\$13
	Preferred Mortgages (U.K.)	December 2003	Non-conforming	\$134
	Financial Freedom (Sold July 2004)	October 2000	NA	\$40
	BNC Mortgage	July 2000	Subprime	\$176
	SPML (U.K.)	December 1999	Non-conforming	\$28
	Finance America	May 1999	Subprime	\$12
	Aurora Loan Services	July 1998	Alt-A	\$10
Merrill Lynch	First Franklin	September 2006	Subprime	\$1,310
	Freedom Funding (U.K.)	July 2006	Non-conforming	NA
	20% Min. Interest in OwnIt (shut down Dec '06)	June 2005	Subprime	NA
	Mortgages plc (U.K.)	November 2004	Non-conforming	NA
	Wilshire Credit Corp	January 2004	Subprime servicing	\$52
Bear Stearns	ECC Capital (Subprime Mortgage Orig. Platform)	October 2006	Subprime	\$26
	EMC Mortgage	Founded in 1990	Subprime	NA
Morgan Stanley	CityMortgage Bank (Russia)	December 2006	Prime	NA
	Saxon Capital	August 2006	Subprime	\$706
	Advantage Home Loans (U.K.)	December 2005	Non-conforming	NA
Deutsche Bank	MortgageIT	July 2006	Alt-A	\$429
	Chapel Funding (DB Home Lending)	May 2006	Subprime	NA
Goldman Sachs	Southern Pacific	May 1999	Subprime	\$39
Credit Suisse	SPS Holdings	January 2005	Subprime servicing	\$100
Barclays	Equifirst	January 2007	Subprime	\$225

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Subprime Landscape Shifting Dramatically

Top 20 Subprime Originators of 2006

Rank	Firm	2006 Production (\$BN)			Status
		Total	Wholesale	Retail	
1	New Century	51.6	47.5	4.1	Funding frozen, stock delisted, criminal investigation
2	HSBC	50.8	38.6	12.2	Impairment charge up 70%; fired senior U.S. managers
3	Countrywide	40.6	25.4	15.2	Foreclosures at 5-yr high; cutting jobs
4	CitiMortgage	38.0	17.9	20.2	Buying distressed businesses (took stake in Opteum unit)
5	WMC Mortgage (GE)	33.2	33.2	0.0	Cutting 20% of workforce
6	Fremont General	32.3	32.3	0.0	Stock down 45% YTD; selling subprime operation
7	Ameriquest	29.5	22.6	6.9	Cutting workforce; selling business
8	Option One (H&R Block)	28.8	26.8	2.0	Near agreement to sell business
9	Wells Fargo	27.9	8.9	19.0	Cutting workforce
10	First Franklin	27.7	25.4	2.3	Bought by Merrill Lynch in 2006 (\$1.3B)
11	Washington Mutual	26.6	26.6	0.0	Cutting workforce
12	ResCap (GMAC)	21.2	20.9	0.3	4Q06 operating loss of \$651M
13	Aegis Mortgage (Cerberus)	17.0	10.2	6.8	CEO ousted in 4Q06; wholesale subprime business discontinued
14	Accredited Home Lenders	15.8	13.4	2.4	Stock down 60% YTD; considering strategic options
15	BNC (Lehman Brothers)	13.7	13.7	0.0	
16	Chase Home Finance	11.6	6.9	4.6	
17	American General Finance	11.5	10.5	1.0	
18	Mortgage Lenders Network	11.2	NA	NA	Went bankrupt in February; Lehman hired part of salesforce
19	Equifirst	10.8	10.8	0.0	Bought by Barclays in 2007 (\$225M)
20	NovaStar	10.5	NA	NA	Stock down 78% YTD

Other Notables

Ownit	9.5	NA	NA	Out of business; partially-owned by Merrill Lynch & BofA
ResMae	7.7	NA	NA	Bought by Citadel in 2007 (\$180M)
ECC	5.5	NA	NA	Bought by Bear Stearns (\$26M)
Fieldstone	5.0	NA	NA	Bought by C-Bass in 2007 (\$260M)
Nationstar	4.6	3.6	1.0	Bought by Fortress in 2006 (\$575M)



Sold or Bankrupt



In Play

Types of Residential Mortgages

	Prime	Alt-A (Aurora)	Subprime (BNC)
Loan Pricing / Terms	<ul style="list-style-type: none"> ◆ Avg. balance: \$250,000 ◆ Fixed rate; Hybrid ARM; IOs ◆ Avg LTV <80% ◆ Rate (30 yr Fixed): 6.13% ◆ Primarily full documentation ◆ Primary residence/Investment property 	<ul style="list-style-type: none"> ◆ Avg. balance: \$216,000 ◆ Fixed rate (40%); ARMs/ Hybrid ARMs (52%); IOs (65%) ◆ Avg LTV / CLTV: 80% / 92% ◆ Rate: Prime Mortgage +1.62% ◆ Full / Stated Docs: 20% / 47% ◆ Investment property: 18% ◆ Cash out Refi: 24% 	<ul style="list-style-type: none"> ◆ Avg. Loan Size: \$175,000 ◆ Hybrid ARM (70%); IOs (22%) ◆ Avg LTV / CLTV: 81% / 86% ◆ Rate: Prime Mortgage +2.23% ◆ Full / Stated Docs: 59% / 38% ◆ Investment property: 7% ◆ Cash out Refi: 63%
Borrower Characteristics	<ul style="list-style-type: none"> ◆ Generally documented income ◆ Typical FICO > 700 ◆ DTI up to 40% 	<ul style="list-style-type: none"> ◆ Self-employed, stated income ◆ Avg FICO: 703 ◆ Avg DTI: 39.5% 	<ul style="list-style-type: none"> ◆ Self-employed, stated income ◆ Avg FICO: 620 ◆ Avg DTI: 41.9% ◆ Credit issues (ie; bankruptcy)

2006 US Residential Mortgage Market Origination Breakdown

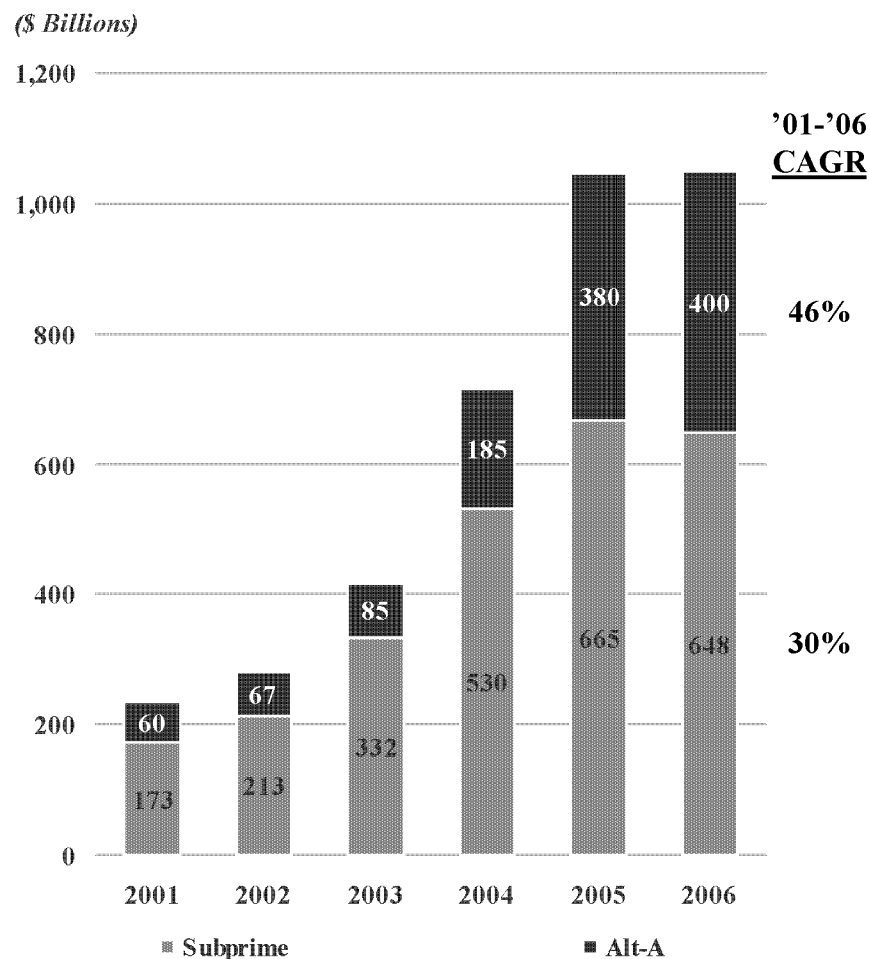


Subprime Mortgage Origination Market Overview

Rapid growth in sub-prime mortgage originations fuelled by credit product innovation and increased appetite for credit risk from capital markets

Subprime and Alt-A Mortgage Origination Volume ⁽¹⁾

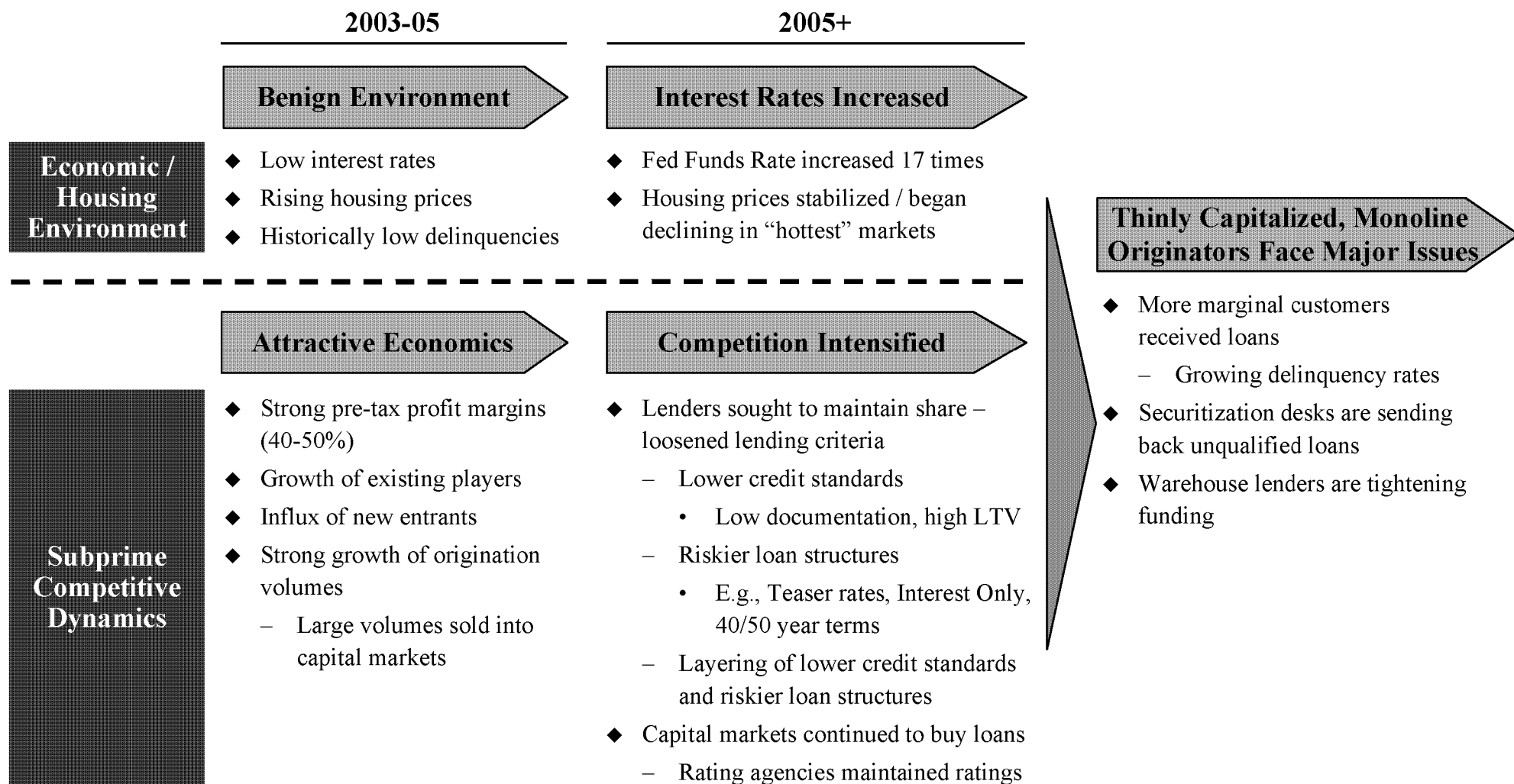
Market Commentary



- ◆ 30% CAGR from 2001-2006
 - Overall market (over same period) grew at a 6% CAGR
- ◆ 22% of overall mortgage market in 2006 vs. 8% in 2001
- ◆ Drivers of subprime market growth
 - Credit and product innovation
 - Advances in evaluating household credit risk
 - Products developed to meet customers' credit profile
 - Increasing risk appetite in capital markets
 - Growth of securitization market
 - MBS / CDOs have provided higher yielding investments in low interest rate environment

Evolution of Subprime Market Dynamics

Attractive economics led to growth of businesses. Lending standards loosened as firms tried to maintain share, coinciding with housing market deterioration

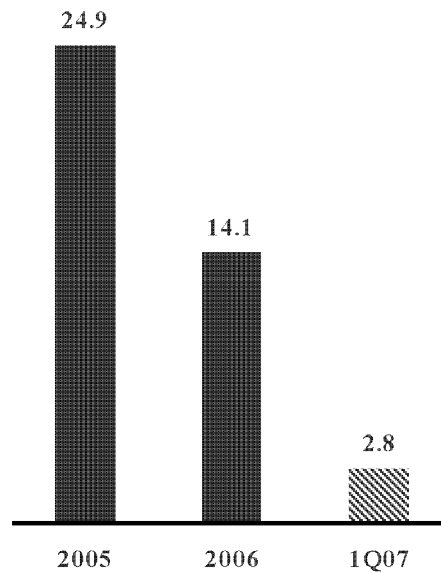


Evolution of BNC Economics

Deterioration in economics driven by decline in origination volumes, reduced gain on sale / securitization revenue from capital markets and rise in delinquencies

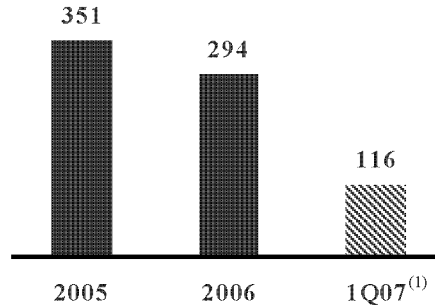
Origination volume is declining...

(\$ BN)



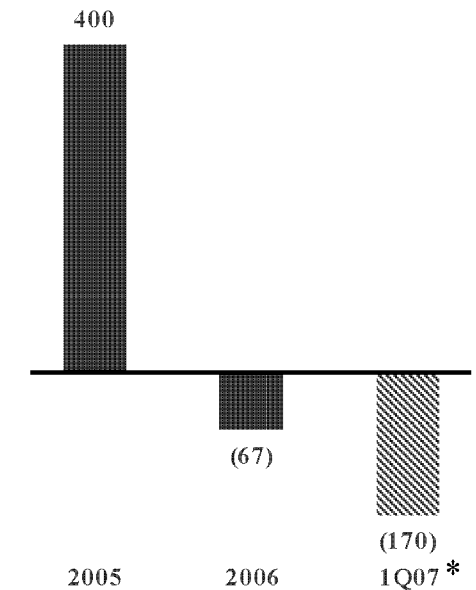
...as is the amount gained on sale / securitization...

(bps)



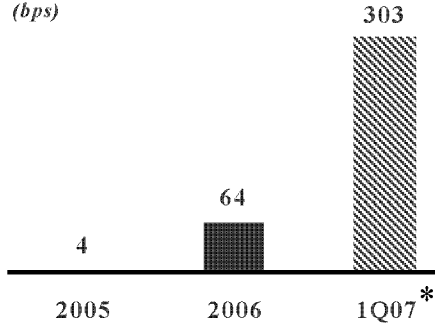
...resulting in lower pre-tax income

(\$ MM)



...while loan loss reserves are increasing...

(bps)



*** 2007 Q1 high loan loss reserve provision & pre-tax level driven by historical & Mark to Market losses**

(1) Assumes no gains on securitization for period.

Recent and Planned Changes to BNC

Address immediate excess capacity and reconfigure for future market opportunities

New Leadership Team	Reduction in Force	Change in Operating Model (May 2007+)
<ul style="list-style-type: none"> ◆ New CEO – Steve Skolnik <ul style="list-style-type: none"> – Ex-First Franklin ◆ New Head of Sales – Tim Owens <ul style="list-style-type: none"> – Ex-Option One 	<div style="text-align: center; background-color: #cccccc; padding: 5px;">2006</div> <ul style="list-style-type: none"> ◆ Reduced headcount by 23% (510 employees) vs. yr end 2005 levels <ul style="list-style-type: none"> – 55 Account Executives – 455 admin / ops staff 	<ul style="list-style-type: none"> ◆ Convert from branch model (34 locations) to regional operational center model (ultimately 5 locations) ◆ Align officer & account executive compensation to loan performance
<ul style="list-style-type: none"> ◆ New COO – Scott Anderson <ul style="list-style-type: none"> – Ex-Accredited ◆ New Head of Eastern Ops – [XX] <ul style="list-style-type: none"> – Ex-MLN 	<div style="text-align: center; background-color: #cccccc; padding: 5px;">2007</div> <ul style="list-style-type: none"> ◆ Additional 26% headcount reduction planned for May <ul style="list-style-type: none"> – 49 Account Executives – 372 admin / ops staff 	<ul style="list-style-type: none"> ◆ Migrate account executive production from correspondent to wholesale channel ◆ Double Ops staff efficiency by employing best practice file flows ◆ Continue to work with trading desk on new products and optimizing profitability of existing products

BNC uniquely positioned to succeed in future environment due to vertically integrated model, leadership team and planned operational / operating model changes

Contingency Planning Underway for Prolonged Downturn Scenarios

- ◆ Origination volumes currently hard to predict – submissions high, but
 - Recent guideline changes may reduce pull-through
 - Spike may be one-time event based on displacement in industry
 - Macroeconomic / housing environment may continue to deteriorate
 - Ultimate status of some competitors unclear (i.e., Fremont, New Century)

- ◆ Scenarios already mod
 - \$1 Billion per month (expected workforce and location reductions adequate)
 - \$750 Million per month (eliminate 53 additional positions and 3 locations)
 - \$500 Million per month (eliminate 115 additional positions and 4 locations)

- ◆ Additional scenarios being evaluated – regular updates with Joe and Finance organization

Drivers of Business Economics – Per Loan Basis

	Recent Trough	Stabilized Market	Positive Environment
	<ul style="list-style-type: none"> ◆ Low gain on sale / securitization ◆ Lower origination volume leads to higher costs ◆ High level of defaults 	<ul style="list-style-type: none"> ◆ Medium gain on sale / securitization ◆ Unit costs fall <ul style="list-style-type: none"> – Volume pick-up – Staff reductions – Operating model changes ◆ Medium level of defaults 	<ul style="list-style-type: none"> ◆ High gain on sale / securitization ◆ Unit costs fall further <ul style="list-style-type: none"> – Further positive scale effects – Staff reductions & upgrades – Operating model changes ◆ Low level of defaults

Revenues

Gain on Sale / Securitization	50 bps	200 bps	250 bps
Carry	30 bps	30 bps	30 bps

Costs

Cost of Origination	250 bps	177 bps	150 bps
Loan Loss Reserve	100 bps	55 bps	35 bps

Pre-Tax Income	(270) bps	(2) bps	95 bps
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BNC Run Rate Financials, incl. Trading Desk, ex-Allocations - Scenarios

Expect to reach Stabilized Market by Q4 and Positive Environment by 2008

	Recent Trough	Stabilized Market	Positive Environment
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<i>(\$ in millions)</i>			
Revenue	\$48	\$276	\$504
Pre-tax income	(\$185)	(\$25)	\$148
Pre-tax margin	(385%)	(9%)	29%

If Positive Environment is not realized, additional retrenchment may be required

Risk and Credit Changes to Enhance Performance

Sampling of changes made to BNC processes and criteria 2006-07

Risk

- ◆ Rigorous Monthly Risk Review process implemented – credit focus
- ◆ Monthly FPD / EPD and Reps & Warranties loss reserve meeting
- ◆ Transfer of servicing to Chase from Option One

Credit Criteria

- ◆ 80/20 loans
 - Terminated exceptions
 - Increased minimum FICO score to 640
- ◆ First time homebuyers
 - Maximum of 90% Combined Loan to Value (CLTV)
 - Maximum of 1 unit
- ◆ Stated Documentation
 - 100% CLTV and Loan to Value (LTV) eliminated
 - Maximum of 50% Debt to Income
- ◆ Other FICO increases
 - Minimum FICO of 660 for Full Documentation 100% CLTV / LTV

Categories to be added & some wording changes

Dave

BNC and Market Average Loan Characteristics

Guideline changes significantly changed loan characteristics from 1H 2006 to 1Q 2007

	1H 2006		1Q 2007
	BNC	Market	BNC
Delinquency	5.3% ↓	5.0%	To fill - we have data now; will do this tonight
FICO	626.7 ↓	628.0	
LTV	82.3% ↓	81.4%	
CLTV	87.2% ↑	87.5%	
Full Docs	51.9% ↓	54.8%	
2nd Lien	26.7% ↑	33.2%	

↓ BNC worse than market 1H 2006
 ↑ BNC better than market 1H 2006

Balance Sheet Subprime Risk Exposure

Actively manage subprime risk exposure

Current Exposure

- ◆ Firm strategy has been to securitize and sell all loans into capital markets
 - To mitigate risk, Firm actively hedges balance sheet positions
 - Risk Transfer model has protected the Firm from significant losses that afflicted firms taking a Balance Sheet Lender approach e.g., HSBC
 - HSBC kept loans on balance sheet, with limited hedging
- ◆ Current subprime “economic” balance sheet \$9.6B
 - Whole loans \$8.0B
 - Securities \$0.82B
 - Investment grade \$0.57B
 - Non-investment grade \$0.25B
 - Residuals \$0.68B
 - Investment grade \$0.45B
 - Non-investment grade \$0.23B
 - Servicing \$0.1B

Exposure Issues Going Forward

- ◆ Limited ability to sell below Investment Grade risk profitably in current environment
 - Balance sheet will increase ~\$1B per month
 - Constrain Firm’s ability to use balance sheet for other activities (Firm net Balance Sheet ~\$300B)
 - Growth of non-Investment Grade risk
 - Growth of Risk Appetite
- ◆ More difficult to hedge inventory positions
 - More difficult to hedge effectively – correlations may not work as well
 - Increased Mark To Market volatility
- ◆ Lack of investor appetite
 - ABS CDO vehicles: investor losses significant – may not have risk appetite
 - Investors will be skeptical of perceived value of underwriting changes

Limited Contagion To Related Markets

Prime / Alt-A Mortgages

- ◆ Significant migration to higher quality credits by investors
- ◆ Credit performance not problematic – delinquencies are within expected range
- ◆ Greater risk of subprime impacting house prices negatively, which in turn could reduce origination volumes in Prime / Alt-A

UK subprime

- ◆ Less mature market than US
 - Loan terms & pricing currently less aggressive, but competition is intensifying – may put pressure on the economics of Lehman's business in the near term
- ◆ Loan to value, delinquency and default rates lower than US
- ◆ House price appreciation higher & more evenly distributed – supported by fundamental housing shortage

ABS CDOs

- ◆ Existing market losses are manageable
- ◆ Outlook for further originations is questionable in near term

Asset Backed Commercial Paper

- ◆ Structural integrity of facilities should withstand asset underperformance
- ◆ Have not seen liquidity issues in broader markets

Broader credit markets

- ◆ Only limited widening of spreads

Range of Opportunities in Current Marketplace

Actively monitoring for opportunistic situations: based on price / value, fit and current Lehman gaps

Platform Acquisitions

- ◆ First Franklin, Equifirst
 - Too expensive
- ◆ Fremont
 - Passed - culture
- ◆ MLN
 - Passed – price and legal risk

Servicing Platforms

- ◆ New Century, ABN Amro
 - Under review
- ◆ Netbank
 - Too expensive

Distressed Assets

- ◆ New Century
 - Purchase of residuals
- ◆ Various loan acquisitions
- ◆ Distressed bond acquisitions

Human Capital

- ◆ MLN
 - 150 operational and sales staff
- ◆ OwnIt
 - 50 operational and sales staff

Summary and Planned Next Steps

- ◆ Most of large subprime independents have gone out of business, have been sold or are selling
- ◆ But subprime market is here to stay
 - Meets a clear need from households
 - Profitability will return when environment improves
 - Lending standards tighten, pricing improves & excess capacity is removed – starting to see this
 - Outlook becomes stable enough for the return of capital markets' risk appetite
- ◆ Have taken and planning to take further corrective action to the business
 - New leadership team in place
 - Reduction in headcount & locations (based on expected origination volumes), and changes to operating model
 - Tightened lending standards, increased pricing – loan loss provisions will come down after Q1
- ◆ Plan predicated on return of capital markets' risk appetite and ability to sell non-investment grade risk profitably by early 2008
 - Pre-tax margin expected to return to 25-30%
 - If investor appetite does not return, will need to revisit options