

Lehman Brothers Holdings, Inc.
Q2 2008 Guidance Call
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Lehman Brothers Holdings Inc. (LEH)
Q2 2008 Guidance Conference Call
June 9, 2008

Operator: Good morning and welcome to Lehman Brothers Conference Call. Parties will be on a listen-only mode until the question-and-answer session. [Operator instructions]. This call is being recorded, if you have any objections you may disconnect.

I would now like to turn the call over to Mr. Ed Grieb, Director of Investor Relations. Sir, you may begin.

<<Edward Grieb, Director of Investor Relations>>

Thank you for joining us today. Before we begin, let me point out that this presentation contains forward-looking statements. These statements are not guarantees of future performance. They only represent the firm's current expectations, estimates, and projections regarding future events. The firm's actual results and financial condition may differ, perhaps materially, from the anticipated results and financial condition in any such forward-looking statements. These forward-looking statements are inherently subject to significant business, economic, and competitive uncertainties and contingencies, many of which are difficult to predict and beyond our control.

For more information concerning the risks and other factors that could affect the firm's future results and financial condition, see risk factors and management's discussion and Analysis of Financial Condition and Results of Operations" in the firm's most recent Annual Report on Form 10-K and most recent quarterly report on Form 10-Q that's filed with the SEC.

The firm's financial statements for the second fiscal quarter of 2008 are not finalized until they are filed in its quarterly report on Form 10-Q for the second fiscal quarter of 2008. The firm is required to consider all available information through the finalization of its financial statements in the possible impact on its financial conditions and result of operations for the reporting period including the impact of such information on the complex and subjective judgments that will be discussed on today's call.

As well as estimates the Firm made and preparing certain of the preliminary information included in these remarks. Subsequent information or events may lead to material difference between the preliminary results of operations described in these remarks and the result of operations that will be described in the Firm's subsequent earnings release and between such subsequent earnings release and results of operations described in the Firm's quarterly report on Form 10-Q to the second fiscal quarter of 2008.

Those differences maybe adverse, listeners to these remarks should consider the possibility. This presentation contains certain non-GAAP financial measures, information relating to these financial measures can be found under the footnote in this mornings preliminary earnings press release, which is been posted on the Firm's website www.lehman.com and filed with the SEC in an Form 8-K available at www.sec.gov.

Now I would like to turn the call over to our Chief Financial Officer, Erin Callan. Erin?

<<Erin Callan, Executive Vice President and Chief Financial Officer>>

Thank you, Ed. Good morning everybody, and I really appreciate your joining on such short notice this morning. Today, I want to cover the press releases we issued earlier in the day. The press release of our second quarter estimated earnings and the offering of 6 billion of equity, which is comprised of 4 billion of common and 2 billion of mandatory convertible preferred stock.

First, very importantly upfront [Indiscernible] since we are only approximately one-week into our quarterly financial closing process, the financial information we are talking about today is all preliminary and represents estimates that are still subject to refinement and to change as indicated in the release we expect about the followup call covering our full results with greater detail and another presentation next Monday June 16th.

I will take Q&A at the end. However again be patient given the preliminary nature of these earnings numbers. Please understand expect that some of the answers I am going to give will be more limited than usual. And certain questions we may not be able to answer at this time but we will have the intent to answer them next week. There will be an opportunity for additional Q&A with a presentation on June 16.

The estimated net loss in our press release this morning that we reported for the second quarter is 2.8 billion, which results in a diluted EPS loss of approximately \$5.14 per share. These amounts include approximately 4.9 billion of mark-to-market adjustments principal investment losses and other dynamic hedging losses. Our estimated net revenues for the quarter are negative 700 million. Compensation expense is 2.3 billion, non-personnel is 1.1 billion and our tax rate for the quarter is approximately 32%. Preferred dividends this quarter about 100 million. And we estimated our diluted share account to be 559 million shares ahead of today's offering. Book value per share again without accounting this morning's transaction at the end of the quarter is estimated to be slightly over \$34 per share. The net loss of 2.8 billion compared to net income of 489 million last quarter and 1.3 billion in the second quarter of 2007. Importantly and you'll hear this throughout the call during the quarter we executed on a number of the capital and liquidity goals that we set out for ourselves which includes as follows:

Lowering growth and net leverage to less than 25 times and less than 12.5 times respectively. Both of those numbers are prior to today's capital raise. Reducing our growth assets by approximately 130 billion and our net assets by approximately 60 billion with a large part of the reduction as I will talk about in detail coming from less liquid asset categories and also providing significant price visibility for marking the remainder of our inventory. We significantly reduced our exposure to asset classes such as residential and commercial mortgages, and real estate help us our sales of approximately 15 to 20% in each case. In acquisition and finance exposure by almost 35%. We also reduced our high yield or non-investment grade debt inventory in the aggregate which includes our funded acquisition and finance tradition by greater than 20% in the quarter. I wanted to be clear at this point that we do not intend to lower our leverage ratios from these levels. From the liquidity perspective, we've made great progress rolling our fast capital surplus to approximately 15 billion at the surplus from 7 billion in the first quarter. We grew our liquidity pools on this 45 billion and that compares with 34 billion at the end of the first quarter. We completed and it's entirely our budgeted funding plans for the full year of 2008 of approximately 34 – 33 billion that also includes 5.5 billion of public bench mark long-term debt that we've executed in the last two months of loans.

Weak [ph] amount of time increasing our over funding amount from the repurchase side increasing those to approximately 25% in offer funding from 15% last quarter. We executed on all of these goals in a market environment over the specially challenging and the consistent with our commitments we made at beginning of the quarter. Our growth in net market-to-market adjustments this quarter was 3.6 billion and 3.7 billion respectively and came primarily in the residential and commercial mortgage books. For the quarter we benefitted to more widening of our credit spreads on our own debt [ph] and recorded approximately 400 million of gains on structured debt liabilities since end of February.

Our hedges on illiquid assets generated approximately a 100 million of additional losses this quarter as a gain from some hedging activity will more than offset by law facing orders and I will talk about that in more detail. The overall efficiency of hedges this quarter was significantly impacted from the unprecedented dislocation between our derivative hedges and the underlining cash market as seen that took place through out the broader capital market. In addition to the hedging of our less liquid asset exposures we also maintain defensive positions in our credit-related business.

Market movement in the quarter including in a normal of shift in bases resulted in approximately 700 million in losses this quarter. Our principal and private equity portfolios also incurred losses of approximately 500 million and in our combined basis aggregating all these losses continued asset repricing for 3.7 billion principle on other losses all sorts of negatively impact our revenues by a total of approximately 4.9 billion.

Let me look at this number verus the 700 million of negative reported revenues this co response to run rate revenues for the quarter of approximately 4.2 billion and while it was very challenging and eventful market environment. As we look forward our underlying client franchise remains from remarkably strong given the broader market contacts for the quarter across our peer group.

Capital market client revenues declined by only about 2% quarter-over-quarter we continue to see our share of volume with our institutional capital market clients increased. Our U.S. fixing con-trading share increased to 12.8% year-to-day from 12.2 last year. And we improved our global equity-trading share for the year across most major stock exchanges. Longer-term we see real opportunity in the capital markets as the competitive landscape is improving in our favor and as a risk is being priced more appropriately.

When asked about of the viability of a mid teens ROE earnings model with lower leverage we see the recent trends supporting higher ROE in margins and a markedly advanced – advantageous competitive environment from Lehman Brothers. For example we also strenghtend [ph] shrinkage on market share investment banking this year including completed M&A where we've grown our global market share to 24.4% from 19.4% last year and our global equity market share rose to 5.8% from 3.6% last year.

An activity levels across all our business, which were flow early in the quarter picked up in the later part of the quarter. Let me goes to some additional detail on our revenues and net income performance to give me [ph] more perspective. Our capital markets revenue of negative 2.4 billion or significantly impacted by the mark-to-market adjustment and other launches that I noted earlier. This compared with 1.7 billion in a sequential period and 3.6 billion in the second quarter of last year. Within capital market this income revenues were negative 3 – 3 billion and equities capital market revenues 600 million. With the equity revenue is been impacted by a \$300 million principal related loss this quarter. We layout our growth in net mark-to-market adjustment on page nine of this mornings earnings release just simplify. In residential mortgages, our growth adjustments were approximately 2.4 billion. These losses arose primarily from two different factors. First the collapse of a large mortgage hedge fund Peloton and then went through Bear Stearns at the beginning of the quarter cost significant price deterioration, particularly at the top of the capital structure for resi assets. Second as I mentioned earlier we actively reduced our exposure throughout the quarter particularly in high risk positions such as non-performing loans and subprime, which still allow us better pricing information on this asset class.

sOur residential hedges provided only 400 million of benefits this quarter in other words hedges offset approximately 17% of the losses, as a remainder this compares to a benefit of over 70% in the prior quarter and similar amount in Q3, Q4 '07. This lower benefit resulted from the dislocation between cash assets and the asset-backed single name and inductor [Ph] evidence that we use as hedges. That's our net right downs in residential mortgages were 2 billion, it is was noting that it was an extremely active quarter for secondary traded of residential product out side these asset losses our business generated strong operating revenues on the back of that trading activity.

Another non-residential asset-backed securities, our growth and net adjustments were approximately 300 million, there are of righty variety of different debt instruments included in this category such as franchise related hold business financing, student loans small business loans, auto loans, credit cards most of which were categorized as level 2 assets in the first quarter. These assets include asset-backed issuances as well as whole loans. In response to specific questions on this category, these asset do not include any ABS CDO balances, were exposure in ABS CDO's is approximately 600 million and its included in our residential mortgage exposure lines.

last quarter approximately 12% of the balance of asset-backed securities with unrelated and therefore reported as below investment grade. We'd now received double aid ratings on significant amount of this previously non-related portion. Commercial mortgages and real estate had growth mark-to-market curdling approximately \$1 billion this quarter result over 7 billion of commercial mortgage positions across different parts of the capital structure to over a 170 different client accounts and primarily in the and upon the home loans. The briefing [ph] scale of the selling is a sign of the return of investor appetite to this asset class and gives us very good price absorbability in marking the remainder of our commercial block. Also more than 75% of the 7 billion sale volume were outside outright sales without financing and [Indiscernible] sales were consistent with the 20% [Indiscernible] portion of this total book. However during the quarter we did see spreads on our commercial hedges tighten by several 100 basis points, for example the CMBX 4 series have tightened anywhere from a 100 to 300 basis points depending on the trench. While the spreads on our largely floating rate positions did not change materially. That's our hedges including single name and index derivative had losses of approximately 400 million resulting in an aggregate commercial mark-to-market adjustment of 1.4 billion.

I would like to stop for a moment and comment on the many questions we have received about few investments Archstone is the first. Archstone is a company, which owns a very diversified portfolio of high quality apartment asset, the underlying fundamentals of which continued to improve. For example, it had first quarter '08 same-store revenue growth of 5% now with standing our performance in recognition of the change in real estate market evaluation metric we have taken a significant mark on that position, the current mark reflects a projected mid-teens internal rate of return on that capital. As a matter of Lehman policy and consisting with industry proactive, we do not disclose specific marks. Similarly our SunCal exposure, which reside, in both our fixed income and third party managed funds area represents approximately 1.6 billion of unlevered direct Lehman exposure. The exposure had been marked to reflect an approximate 15% unleveraged internal rate of return. That mark takes into account, recent similar large transactions that have occurred in relevant markets. For example, of the total exposure, approximately 250 million is in the Inland Empire with an adjusted basis of approximately 20,000 per lot [Ph]. Moving on, in acquisition finance our growth to net mark-to-market adjustment so approximately 300 million and 400 million respectively.

It's been suggested we've not been sufficiently aggressive in marking on in our inventory in fact I believe our successful hedging performance over the past year has muted the magnitude of our growth markdowns. To give you the cumulative size of growth losses we've taken on new asset classes since the beginning of fiscal '07 most of which occurred in the past 12 months. In residential mortgages and other asset backed securities.

We've taken over 11 billion of aggregate write-downs. In commercial mortgages and real estate held for sale. We've taken approximately 3.5 billion of growth write-downs. In acquisition finance we've written down almost 2 billion of assets. In total we've taken approximately 17 billion in growth mark-to-market adjustment since the beginning of last year offset by hedging benefits of approximately 7.5 billion given the lot of benefits from hedging this period I'd like to make a few comments on our hedging strategy that believed against a liquid asset.

First and foremost it remains our intent to actively hedge our exposures with the goal of mitigating

the impact of market movements. We believe the ineffectiveness of our hedges this quarter was an operation. Shooting cash assets is not practical because of limits on borrow derivatives are and will today the most efficient hedging option and we do not expect further divergens between derivatives and cash from here. I'd also like to point how each month of the quarter with quite distinct March would characterize by the effective power plants and a class of their sterns, which bolt the tremendous pressure on the Singapore as the residential mortgage capital structure.

This is evident in the level of growth rate downs we again saw in receives [ph] March. April is characterized by the dislocation of credit spread tightening between cash and derivative and lastly in May we saw some returns in normal sake in fact excluding asset mark may with one of our stronger run rate revenue months. Within the broader context of fixed income capital markets our overall client activity levels remain strong.

Fixed income client revenues were down slightly from the strong first quarter. Year to-date 2008, client revenues are up substantially versus last year and importantly our relationship with clients and counter parties remains strong with no material loss of lenders, clients, no counter parties during the quarter .We saw continued strong secondary plus and securitized products, I mean that suppose energy, credit, interest rates and financing which are all up significantly versus the year ago.

Equities capital market revenues were approximately 600 million decline 60%, but included within the mark - equity segment our losses on private equity and principal. The market environment in this area was also challenging this quarter for principal as we experienced estimated losses up 300 million and equity driven in part by depreciation of our investment in GLJ. As you know, we had a gain of approximately 200 million on principal and private equity last quarter to a \$500 million swing period-over-period for that segment.

In the second quarter of '07, the comparable gain was approximately 300 million

Excluding these principle in private equity market, we saw client revenues in the equities business remain essentially flat versus the comparable periods. Volatility revenues decline versus both [Ph] period what execution services remain solid year-over-year but down versus the trailing quarter. And time services had recurred revenues even in a face of continuity leveraging by hedge fund post the events of mid-March.

Turning to investment banking we had revenues of approximately 860 million, which were flat to last quarter down 25% versus the year ago, and flat in the context of significantly declining market activity. Debt underwriting revenues were down versus last quarter at investment grade issuance remains strong versus both [Ph] comparable period contains stronger high yield revenues.

Equity underwriting revenues were out more 50% from last quarter, and flat versus the year ago on strong issuance and participation by Lehmann in the financial sector well IPR [Ph] activity remain lower than the year ago period. Advisory revenues were also lower given the current financing environment for investment management revenues of approximately 850 million decline 12% versus last quarter and 10% higher than the second quarter of '07.

Private investment management revenues remain strong in both fixed income and equities, asset management decline 20% versus the first quarter primarily on the back of the decline in incentive revenue and income from minority investments and third party hedge fund manager.

We expect our assets under management balances to be essentially flat this quarter at 277 billion despite all market trend level.

Moving to expenses for the quarter, our total compensation expense is estimated to be 2.3 billion, which reflects the \$480 million increase from last quarter. During the quarter we encouraged severance cost that were included in this comp expense. Also during the quarter our headcount

decline by 900 people most notably in the U.S. and we continue to scale our businesses to do respective opportunity.

For the quarter our non personnel expense totalled 1.1 billion in this area we've implemented a num up further cost heading initiative during the quarter, which will generate approximately 250 million in annualized saving going forward particularly in real estate occupancy.

Now let me make a few additional comments at – that our balance sheet and our capital we ended the quarter with total stock holder equity of approximately 26 billion again prior to the capital rates and up 6% from the first quarter. This includes the issuance of 4 billion of convertible preferred stock in April.

Our long-term capital rose to a 156 billion from a 153 billion at the end of the first quarter. In addition to the - we raise in April, we've raise an additional 5.5 billion in benchmark long-term issuance of this quarter including 2 billion of 30 year subordinated debt. Consequently, as I mentioned earlier we've completed our entire budgeted funding plan for all of 2008 and do not need to revisit the debt market.

Book value per share declined in this quarter to approximately \$34 per share driven our net loss taking it to account today's capital rate, we estimate book value per share to be approximately \$33 billion a share – I am sorry \$33 per share as we have previously stated our goal in the second quarter was to bring to down growth and net leverage most importantly we wanted to accomplish that by reducing exposure to residential and commercial mortgages and leverage finance exposures and we've done this. For the quarter we estimate we reduced our total assets by approximately 130 billion from 786 billion at February 29th. With reduction in gross assets combined with our convertible preferred issue as on April we expect to report a gross leverage ratio less than 25 times again this excludes the latest capital rates which brings us below 22 times.

We reduced our net assets by approximately 60 billion in this quarter resulting a net leverage of under 12.5 time versus 15.4 in the first quarter and again less than 10 times net leverage with the capital rate. I'll provide more on these specific reductions and exposures on our earnings call on June 16. However, I do feel comfortable stating today that residential mortgage commercial mortgages and real estate help for sales will each be down between 15 and 20% and acquisition finance exposures down approximately 35% on the quarter.

sOur deleveraging with aggressive as you can see and its complete for level three assets just make a comment I can not give you any specific announce at this time as at two early in a coursing process of our books. With the valuations of all our assets its complete our positions must not to be evaluated and that includes 1000 of positions to determine the level of our price transparency and absorbability on May 30th, in order to proprietarily classify them for our 10-Q disclosure. Once we see complete this - I am sure with the number of reclassifications into and out of level three this quarter certainly do a number of sales that took place out of level three and also transfers. Our CFC capital ratios for Tier-1 in total capital are very strong and we will provide additional details next week on those number for the conference call.

To address the capital rate we also announce today the offering of 6 billion of equity compared to 4 billion of common equity and 2 billion of mandatory convertible preferred stock both offering were substantially over subscribed have been fully allocated in next months trading. The proceeds of the offering will be used in both for capital and wide of our loss for the quarter and in to increase our financial flexibility to be clear we do not expect to used proceeds of this equity rate to further decrease leverage, but rather to take advantage of future market opportunity, which our bounden [ph] and overall we stand extremely well capitalize to take advantage of these new opportunity

From a risk management perspective we continued to operate in our discipline manner we're known for. Our balance sheet and exposure levels declines throughout the period as discussed

and this is reflected in our risk numbers as well. Our period end evaluated risk was 75 million on an unweighted basis and 104 million on a weighted basis. This compares to un-weighted VaR of 89 million at the end of last quarter and weighted VaR of 106 million at February 29. From a counterparty exposure perspective on non-investment grade to derivative counterparty exposure continues to be approximately only 5% and our exposure to monolines remains minimum. Liquidity in the framework and a bit more detail first given to on President in market events over the past few months let me review some of the recent funding and liquidity actions we taken to be responsive. We have significantly increased our cash capital surplus and liquidity pools in mid March we completed our targeted funding plans to be year we increase the funding provided by our banks would customer deposits for less liquid assets and we will continue to grow this funding source and we increase the over funding amounts in our tri-party rebound [ph] and extended the maturities of these facilities. We ended the quarter with holding company liquidity pool approximately 45 billion, which is our largest ever this compares to our liquidity pool was holding a 34 billion in the first quarter.

For note the liquidity pool primarily invested cash, bank deposit, government securities, and overnight report collateralized by government securities. As discussed in the past, our liquidity framework is just to cover our expected cash outlook at the Holding Company for a 12-month period with accelerating new cash and the unsecured market or selling assets outside the liquidity pool.

At the end of the second quarter the 45 billion of our liquidity pool was well in excess of our short-term unsecured financing liabilities, which includes the current portion of the long-term debt totaling 31 billion. That the combination of short-term debt and long-term debt rolling into current portion approximately that 31 billion.

Additionally, our bank entities in regulator broker dealers carry significant access for liquidity in the form of unencumbered collateral to funds qualifying assets. As I have noted previously we have adjusted the Fed new primary dealer to credit facility application with no outstanding balance at quarter end. The last time we accessed its facility was April 16th on an overnight basis.

I will provide more details on our secured funding decision on our forward earnings call on June 16th. All in all this was an extraordinarily active quarter from an operating perspective it was a very challenging market environment where our practice of utilizing dividends [ph] - significantly hedge our less liquid market exposure did not provide the benefits we have seen in prior quarters and our...

Extensive [ph] positioning strategy also working against us. We also experienced a fair amount of volatility ROE in the quarter arising from the fall out of the events of mid March. At the same time we took significant and dramatic steps to reduce our asset exposures to reduce our leverage while simultaneously improving our liquidity in capital position. Deleveraging is complete, we do not expect to take the balance sheet to show down from here. In spite of developable market environments our employees continue to safely focus on our clients and providing quality valued services enabling us to continue to take market share and key aspects above our business as we get the last three months even in the light of the most difficult quarter in our history. We are raising additional equity of 6 billion, which serves to mitigate the loss of 2.8 billion this quarter and to give us full flexibility going forward. Our lower leveraged enhanced equity base and rescale business platform leave us well positioned as we enter the second half of 2008. A time when we are seeing more business opportunities including institutional capital markets activity increasing after slow starting Q2. A pick up in investment banking activity particularly since familiar [ph] with quarter. New asset management mandates in our expanding platform and our growing presence on outside the U.S. where markets continue to develop more rapidly than inside the United States.

And so, our client driven business model as they providing us with some competitive advantage. There is significant global person out there, we've talked about the four and we'll continue focusing on our clients, delivering value to them everyday and providing the financial and more

importantly the intellectual capital that they expect from us. We'll stayed focused on core discipline we known for risk, expense, liquidity and capital management as we move into the second half.

Now I will be happy to take questions, however just to repeat again given the preliminary nature of these earnings number please understand and accept that some of my answers maybe more limited within usual and certain new question we may not be able to answer at this time. So, operator you could open it up to question.

Q&A

Operator: [Operator Instructions]. The first question is from Bill Tanona. [Goldman Sachs]

<Q - William Tanona>: Goldman Sachs, Hi Erin.

<A - Erin Callan>: Hi Bill, how are you doing?

<Q - William Tanona>: Good.

<A - Erin Callan>: Right.

<Q - William Tanona>: So, just obviously your guys were pretty defensive I would say this quarter as you went to the whole deleveraging process. I guess that, how do you kind of change the attitude of the traders and try to get back into kind of a profit making mistake mode with after going through that type of deleveraging process?

<A>: Fair plus Bill, I think part of the rational for us this quarter of why we're so aggressive, why we [Indiscernible] with the target and why we've had such a tight schedule, it was exactly that we didn't want to create a long-term distraction factored to the business operators. So, we've done that, we knew it's a target work, we're exclusive from the beginning of the quarter, they knew they were slightly end of the tunnel we're already seeing in back in business into the terms of risk taking in an active way. And I am sorry, I think that the disciplined of getting the joint primarily in a single quarter was important to keep the mindset focussed.

<Q>: Is that also why it was possibly know strategic investors involved in kind of exist this capital raising you guys hope to as it gone as aggressively as you should haven't didn't need for - didn't have a need for additional kind of balance sheet hope that you will.

<A>: Yeah, I guess on the strategic outlook for several years, we have – our object – we talked to sell interest in a strategic partner. So, it's not to say we don't continue to have each interest, if there is an appropriate partner for us, but that will be consistent with our objective and certainly balance sheet is not something we need at this point from the strategic partner.

<Q>: Okay, helpful. And then I guess also you've commented briefly on the level three assets, also given the commentary that you had provided in the level of liquidation's that you have done in the number of sales that were done I mean it's safe to assume that's your level three assets are going to be down materially here in the – in the quarter?

<A>: Bill that not safe to assume certainly there is been a significant portion that were went out the door in the sales at a level 3, but there is a number of other asset reclassifications that I am expecting can happen this quarter. For example, our U.K. resiporfolio [ph] would be a good case. That market really launched its price transparency during the quarter. So, it's too early to tell how the sum total of all these effects will take place, but I can give an assurance that, that number is going down that's not my expectation.

<Q>: Okay, fair enough. And then I guess just lastly obviously comp and non-comp expenses had

jumped up but now you have talked about severance and some other factors been there, but as we think about those line items going forward I mean what type of comp in that revenue ratio should we assume and also were kind of base one non-comp expenses should we assume that I guess just lastly given with your all the capital ratios that you done this quarter, what is your expectations for the our view that you still think that the core [ph] Lehman franchise can generate particularly in this environment?

<A>: Yeah. So, let me address your first two. It's a little difficult to comment on comp obviously we spend a long time during the first quarter in the context of positive revenue, thinking long and hard of that the appropriate comps to revenue ratio, which was 52.5 for the quarter but selecting a lower revenue environment and need to hear or they are doing the course of this quarter. I think we are just enough to see greater visibility as we get out in a year it's very hard to predict right now. We are going to be competitive hard to say yeah what competitive means.

<A>: Well don't have a strong perspective I can give you on that, on non-comp expenses that a 1 billion at this quarter, think that should be pretty consistent as we move forward and talk about the savings were implementing for the rest of the year if it come down of that but I don't expected to check up from here. On order we, as I talked about during the course of the presentation lot was I [indiscernible] on can you achieve reasonable returns with lower leverage and as I talked about, we are staying higher our hedge were getting paid more for our intellectual capital and for our balance sheet capital able so we are seeing better margins in the business and this is moment in time on our leverage ratio we don't anticipate staying here as we complete the transformation of this balance sheet away from less liquid asset so I still think on a cross-cycle basis a mid things are away as a realistic assumption.

<Q>: Thanks. Thank you.

<A>: You're welcome.

Operator: The next question is from Guaymas Schelske [Ph].

<Q>: Good morning Erin.

<A - Erin Callan>: Hi Guay. How do you doing?

<Q>: Good within just to make sure of that before interrupting your sort of percentage reductions numbers correctly is it stable assume then that of the 130 billion were so in asset reduction that about 25 billion is in the Resi [Ph] and commercial real estate finance and leverage finance category?

<Q>: It – In terms of the com - mortgage inventory across the board as fairly closer to 20 billion.

<Q>: Okay, and then leverage fit whatever the leverage finance

<A>: That the leverage finance is more meaningful that's gong to be a bigger number.

<Q>: A bigger percentage.

<A>: Of that would be you can really wanted to give, the specific number but as it given to be approximation of the balance sheet number that at this point, we – we've – we actually pull back on that and we will definitely give those numbers next Monday.

<Q>: Okay that's fair but it - it's I just want to make sure that I was applying the right percentage of just to the right numbers.

<A>: Yes.

<Q>: Can you – can you response from may be two credit into are going to say that of bit that the 130 billion of asset sales must to be the absolutely easiest of assets to the sales can you give some flavor for some of them more difficult asset class reductions and whether there in line with those in overall percentages and the expanse of which the you might of with therefore been the bullet was some of those a little more difficult the asset class the asset and we reflective those prices across ask the reminder of the book.

<A>: Yes it also it very much is the latter guide so the logistic gives an adequate of evidence of that at this point and some is more given more next way look at that in terms of that residential block and what we sold their that the vast majority for what we sold within the formal home loan but its not the security portion but it's the security portion arguably has greater price transparency in the market and we sold home loans in a significant part less than sub-prime in NPLs.

<A>: So, we did now [ph] the risk asset classes which did gives us a tremendous amount of visibility back into pricing the rest of our ending [ph] inventory the story on a commercial side is very similar obviously everything that we sold on a commercial side within the home loan category that does reflect the market appetite that it harder to find and the bid for cash securities without providing financing which more generously loaded to do. So the bids that we found where back into a convertible home loan market. I mentioned selling to a 170 customers those for the assets I think gives us a very, very strong sense of where the bid is and to 20% of those shares [ph] were Mezzanine. So details where not limited to our AAA security portfolio, in fact is there anything there was the other way around. We were selling to this component of these asset classes.

<Q>: Okay that's helpful just I have that clarity there. Can you talk a little bit more about the \$6.5 billion other asset back portfolio I think there is been a lot of confusion and so whether those are CDO assets or not because of the way that our footnote was worded in your 10-Q and I just think that we would all appreciate along clarity on what that is?

<A>: Yes. I appreciate you bringing that up its either asset back loan and all security. So what measurement of footnote in our Q is a technical reference to CDO and our technology its not intended to be common part what our CDO. So they talk about it if things like credit card receivables aircraft loans, franchise lending loans et cetera and as I mentioned earlier we only have approximately 600 million on ABS, CDO and that is in the residential line item.

<A>: Its truly a category that we intend to design to - cover any other asset-backed security that we may have in our portfolio, so it covers many, many different positions. So, unfortunately the footnote reference to CDOs was a reference of a technology type not a reference of the assets.

<Q>: Okay that, that – I just wanted to make sure I understood that because of the way the footnote was awarded. So, thank you for that. Thanks.

<A>: Appreciate that.

<Q>: And then finally, you talked a little bit about, what's your one might look like under the new CSCE or Basel II basis and that you been talk about that more in next week that kind of implies that basically you will be doing your initial Basel II disclosure at that time. I been - I do believe that's an - that's going to be an industry event when it happens that basically everybody is going to – disclosing at around the same time. Is that your understanding and therefore should we sort of - assuming that everybody will be disclosing that now with second quarter earnings.

<A>: Yeah, everyone will be disclosing in their queue, I can't tell you that I am not sure actually don't think many will disclose it in their earnings release. And what we'll do next Monday I will said just again in the interest of transparency and giving guidance is well disclosed the range that's our best estimate again this is the kind of thing take a lot of work at the end of the quarter.

So, we think it will be helpful to give a range next week but as we expect you are more or likely seeking more way to their queue. But it will be in the queue.

<A – Erin Callan>: Yes

<Q>: Okay that's great, okay thank you very much Erin.

<A – Erin Callan>: Thanks guys.

Operator: The next question is from Glenn Schorr.

<Q - Glenn Schorr>: Hi Erin.

<A – Erin Callan>: Good morning, Glenn.

<Q - Glenn Schorr>: Good morning, a just let me start out with a clarity question that the 20% mix you've said the sales in commercial real estate were 20% of [Indiscernible] did you comment about breakdown in the commercial book between, how much it's equity versus male versus senior in the remaining book?

<A – Erin Callan>: I didn't comment but just as a guidance and again, I'll get into this in more detail in next week roughly 80% as senior and 20% in [Indiscernible].

<Q - Glenn Schorr>: And nothing equity?

<A – Erin Callan>: So it's not in the commercial mortgage line item.

<Q - Glenn Schorr>: Okay, okay. And I know you're not commending on marks on Archstone decide that it's been marked in each quarter but just sure us where would the mark show up like in the table or page 9 would it be in anyone of those budget?

<A – Erin Callan>: Yeah it will show up on page 9, it will show up in that commercial mortgage related positions line item.

<Q - Glenn Schorr>: Okay and that's worth been whereas I look been and I got the '07 in first class quarter tables?

<A – Erin Callan>: Yeah it's been there consistently.

<Q - Glenn Schorr>: Okay [Indiscernible] and then in terms of the 15 to 20% reduction in resi commercial and real estate loans, I think there is an assumption in that by me and others that if...

<Q>: If you had it your way you said last more than 20% you would have reduced it by say 50%. I don't know if that's correct or not, but can you talk about like did you want to reduce by 50 you got to take what the market gives you and then what's like, what's normal because there is also an assumption and I don't think it's the same in CDO and yes we'd like all that crap off our balance sheet. But here I'm assuming that there are some positions that you actually want to hold no to overtime I wander if you could talk....

<A>: Yeah I think your later point is the correct one right. So, in all these things you spoke of selling these assets with the balancing act between what you are selling out today and what are to de-risk your concentrated exposure. And what's the P&L status going forward. So, they talked about – we've pretty taken 11 billion of cumulative write downs in the [Indiscernible] we certainly think where these things have marked they have real value. But the objective is how to take down the risk in a measured way that's meaningfully, while preserving the upside that we think inherent in the asset class where we've been a great operator. So, we did not target no intent to sell more

than 20%. It's not to say we could not stay over the market we could have okay but it was deliberative strategy and in terms of that balancing act of what upside we want to retain and of what – and also awareness to you to go into your question. How much of that impact you want to have in the market. The larger you do sales and if you write into a portfolio sales 30 billion of raising mortgages you will create a market event on pricing.

<A>: Highlight about this quarter is that - not the strategy that we talked. This was a vigilant day-by-day effort 10 million of inventory – and here 20 there to optimize the pricing outcome to the firm and our shareholders and it was very difficult to do it in that passion. So we didn't want to do it's a portfolio trade and just walk away there would have been a significant P&L impact for taking that approach.

<Q>: And what are these lots of realized write downs and other wards those most of this produced by sale or is this just markdowns as well, is there any combination you talk about?

<A>: Yeah, sure real life losses associated with the special is actually pretty immaterial given the size of the sales. So the losses for the quarter are truly write downs reflective of the market conditions and deterioration of prices here in the course of quarter and the better price visibility that we had this quarter given all that activity than we had in prior quarters.

<Q>: Okay, last one. For, Erin.

<A>: No problem.

<Q>: So in April you had the capital raise and it was a little bit of reversing free and I think some that you mentioned is not overly credible [Indiscernible] finance perspective. And then in mid May, you talked about the mark being something is a lot smaller than that the first quarters mark and you mentioned that May was better so it just felt like this was a bigger loss. So I think we are kind of praised for that the effective [Ph] hedges and the impact of mark so that we are just seen to accelerate in – in May even though May. You mentioned with just a better month?

<Q>: I'm not actual

<A>: I will be [Ph] making some comments some on it. That the corollary to make the right down number for this quarter, okay. Then the March, March a bit adjustment of three-six growth, Ainslie compares apples to apples in Q1 of something about 5 billion, so the debt was a slow down in the faith [Ph] of right down on a gross investment basis, so I got a stroll in the hedging in terms of the outcomes, and a lot of that change threw glittering [Ph] the month of April we talk about the racy [Ph] part cap structure they can affected in March. April I had a lot to do with [Indiscernible] cash consultants and the version that went on to in that mind, and there is some part of the portfolio just to be that - even now its mark throughout the quarter, you do you final marking obviously at the end of the quarter and it more difficult to more collateral and so that by nature will back ended in terms of have a lots of at the P&L.

<Q>: That make sense. [Indiscernible] my question. Thank you.

<A>: That is my pleasure.

Operator: The next question is from Prashant Bhatia.

<Q - Prashant Bhatia>: Hi

<A>: Hi Prashant , how are you doing.

<Q - Prashant Bhatia>: Yeah how are you.

<A>: I'm fine thanks.

<Q - Prashant Bhatia>: Okay on the [Indiscernible] sell asset are you open to doing some thinking like a BlackRock, UBS transaction or is that shows something that – if to get incremental [Ph] to the P&L to do from your finance

<A>: I guess two thing, one I would be open to during that kind of a transaction, if I can take a piece of the upside, so that would be a critical aspect David [ph]. And two I wouldn't want to do it on terms, where we gave generous financing to the buyers, so we speak, so as we talk about we've been very habitant to do the transactions we've done this quarter with the financing we wanted to place to the cash debt. So, we'd have to be in a way, but either had very good financing terms from our perspective and also, but we could retain upside in meaningfully.

<Q>: Okay and that seems to reflect your confidence and where that pull of that that you should probably down to about 65 billion as marked right now.

<A>: Exactly, so I don't want to give a way, but I think it's a material upside there.

<Q>: Okay, and then as we think about the equity, you've raised about 12 billion this year in total, but you only taken 2.8 billion in losses. Obviously you deleverage, but should we think about excess equity as really being held up against this, how to value portfolio or how do you think about that in terms, how much equity are hold against the portfolio?

<A>: No, I'm actually comfortable that we have sufficient equity to cover those aspects as we stand, I think the additional equity in some ways, which you may appreciates is a bit of our and not signed it's about what level of equity, do we need as an organization to both of these balance sheets so we can get back to running our business on a day-to-day basis and start distractions and discussions we have with related to the questions about our balance sheets.

<A>: So, it's up with that number. In fact we have done a good job and summarizing what that confidence number is and that was our objective so it's not specific position is designed to end the charter about the Lehman Brothers and let us get back to business.

<Q>: Okay you can be offensive with this equity it's not held up again.

<A>: Exactly and not the intention.

<Q>: Okay and then just on the equity need trading, if you look at the last, four, five quarters and normalize for the private equity and structured gains and losses. It looks like you're running at about a 1 billion spore in revenue, this quarter normalizes is about 900. Is there anything other than environment that - taken that number down or can we get back to normal from your perspective?

<A>: Yeah I think if you look at the volumes that took place during the quarters of the quarters March with a very, very quite month on equity volumes. So, that - with that numbers reflecting as you point out it but throughout [ph] the environment it does not reflect or reflect anything unique to our franchise with that – I think continue to do quite well.

<Q>: Okay than just finally, on the – on the record prime brokerage revenue. Just a feel for fixed income versus equity I don't know – even now if you look at it that way but if you do what was the driver there what we're seeing on both....

<A>: Yeah [Indiscernible] I don't have the breakdown between those two businesses yet and I can cover that next week.

<Q>: Great thanks.

<A>: You're welcome thank you. Active but let me – let me just fire up on it. I think that – the driver consistent with my earlier points is our ability to get paid and appropriate cost of capital for these of our balance sheet...

<A>: So, it really about margin in the business that is [Indiscernible] the performance of prime brokerage for the quarter.

<Q>: Okay. Thanks.

<A>: Okay.

Operator: The next question is from Mike Mayo.

<Q - Mike Mayo>: Good morning.

<A>: Good morning Mike. How are you doing?

<Q - Mike Mayo>: Good. Can you just get us from the 3.6 billion gross mark-to-market loss to the 4.9 billion number, you gave[ph] in your opening comment.

<A>: Yes. So, it's a combination of 3.6 previously as we talked about at the gross mark. 5 billion of at principal losses, which I discussed.

<Q - Mike Mayo>: I am sorry, how much.

<A>: 500 million of principal losses and 700 million of losses on additional on hedging strategies.

<Q - Mike Mayo>: And those hedging..

<A>: Actually I am working out the 3-7 Mike is the net. So, it's 3-7 plus 500 plus 700.

<Q - Mike Mayo>: And how much for the severance costs?

<A>: Severance costs about a 150 million.

<Q - Mike Mayo>: Okay. And then going back to the [Indiscernible] capital. So, this is all excess capital that you are raising since you are comfortable with the net leverage ratio. On the other hand you want to keep the confidence that you think this capital raise will bring. So, what's your timing for redeploying the new 6 billion of capital or should we think of that you are redeploying maybe 3 billion of capital, which is – in excess of loss that you are taking quarter?

<A>: Yeah I think start[ph] we thinking about the 3 billion, clearly first and foremost and reason to raise common equity is to fill the whole in the common equity component in the capital structure and get us back to a more normalized and optimized cap structure as it relate to common versus hybrid relationship which post loss with [Indiscernible] as far as 60:40. So, I think the common was to lever so take this back to a much stronger common equity based versus our hybrid and so I think you should be thinking about the 3 billion and what's the timeframe I think certainly over the next six months....

<A - Erin Callan>: Environment [Audio Dip] to money to work.

<Q>: And then last question is the harder one had we know that you take in the enough write-down in your real estate book, that's the general question for maybe some specific, how - what present have you write-down your residential mortgages you had 11 billion of gross write-down to

what [Audio Dip] percentage basis of the original total?

<A - Erin Callan>: Okay. So a little I don't have the - your original total [Audio Dip] come back to on that, with that specifically translate into, I think it's from to the confidence level on write-down, it's the following two points. One is [Audio Dip] the aggregate number is very large that we taken since Q3 on predictably last year. And so that give me confident in the actual accumulated loss across those portfolio address the - in commercial. I think that the piece so that is very, very important as we were probably the most active seller of our assets in the market of this quarter all the [Audio Dip] these asset classes and then they talk about earlier we want to selling AAA we were selling a entire capital structure and we were selling risk assets. I think unquestionably our price visibility we got from these transactions was tremendous and so much more activity for us certainly than we did last quarter. So I think the confidence [Audio Dip] at the remaining inventory that there can only to be higher than it was given all that sales activity the visibility the number of clients we down with and the results an impact on our remaining inventory....

<Q - Mike Mayo>: And then how much was Alt-A reduced and any color you can given Alt-A and like what percent of Alt-A is kind of tripe - AAA to...

<A - Erin Callan>: Yeah, I will give that and next week Mick I don't have the breakout yet on the balance sheet between Alt-A and some of the other asset classes within resis. So, we will give that before next Monday.

<Q - Mike Mayo>: All right. Thank you.

Operator: The next question is from Jim Mitchell [Buckingham Research].

<Q - James Mitchell>: Yeah, good morning.

<A - Erin Callan>: Hi, Jim.

<Q - James Mitchell>: How are you? Just a quick follow up lot of the questions have been ask and answered, but on the hedging is that sort of the many you sell down the asset so you can close out the associated hedge or is there timing thing where you still hold on to the hedges why you work through that. I am just trying to think through as you - will you reduce asset, so we also reduced the basis risk on hedges?

<A - Erin Callan>: Yeah, remember we have a dynamic hedging strategy right. So, it's not so simple as this hedge against this position and what the duration it is, but we certainly try to match the duration the hedges brought out to the asset. We are at 100% hedge because we are in a risk business, and also they are dynamic in nature. So, the path of the experience of the hedges at this quarter relatively - in no way is related particularly to the sell down of the asset. Nor do I feel like we end the quarter with an amount of hedges that varies in a meaningful way from the proportion of the hedges we had going into the quarter so, I think we - we also managed the hedge is dynamically with the size of the portfolio. So, it's not - for sitting there at least for the all bunches of hedges have gone now with the assets gone...

<Q>: No I really wants to be a in our concerned about how much basis was still afternoon it would be nice to resets some color on if that is been reduced along with the..

<A>: While I am say - faired to say its been reduced propotionally with the assets [Indiscernible].

<Q>: That's fair enough. Okay great. Thanks.

Operation: And next question is from David Trone [Fox-Pitt Kelton]

<Q - David Trone>: Yeah, hey. Let me followup in the last one you could be hedging operation

comment that you made it is seen pretty confident of that but couldn't you see pears, selling assets at potentially lower prices than and you haven't show the dynamic could continue and is seems like [Indiscernible] lower to be. Always we possible given that you know you've been aggressive in selling a new kind of creator the, this snowball of reprising downward.

<A>: Yeah, I guess on – on net point. David, I would say the approbation on the dividend versus cash markets. Is not necessarily – selling as much to the related to liquidity. There wanted to be clear on that so what now we seen half that in – and the dividend markets exact, there is – liquidity on the correlation of the cash market there are in party who are willing to finance cash asset at this point as you know from the pullback on balance sheet and lending. And so what's happened is if you want to expressed you on any of these assets classes if you expressed in unfounded derivative format because that's the easiest way to do it.

<A – Erin Callan>: I mean, I think the predominant of the difference is driven by liquidity not by price of changes in the market due to selling and do I expect liquidity to change or in the cash market versus the driven [ph] market soon. No, but do we feel good that the amount of the further divergent is pretty limited even that at some point you run out of basis points, yes.

<Q>: In the Alt-A segment either is the high profile thereby UBS and is that safe – could you characterize where you were relative to that price, at?

<A – Erin Callan>: Relative to the UBS prices from their presentation back the month and half ago.

<Q>: Yes.

<A – Erin Callan>: Well, what I can tell you is that at the time of their presentation on March where consistent with there. Obviously, there is an price action since standing but I was consistent with their market at that point in time.

<Q>: Okay, so you – how about next week could you tell us if were below that point or further?

<A – Erin Callan>: Well, we never – tell you significant Mark noted that we tell you Mark across assets classes but I can certainly give you a sense of whether there is been deterioration in prices from that point in time.

<Q>: Okay, okay. And then switching gears to your credit, your counterparty comment. Somethings are fine, how is that different obviously – obviously it's different from mid March. But could you kind of contrast I think the less obviously in nature of the discussions between now versus the tougher period when bear was...

<Q>: Now collapsing?

<A>: Yeah, I think it to be fair the discussions at this point are not about our viability or the factor [ph] will be here or the fact that we have sufficient liquidity and we put back to that on a number of different levels through our own actions obviously to some extent through the transactions. So, I don't think your any question on the part of our any of our counterparties are lenders that they will be repaid by Lehman Brothers. I shows a good debate that's been had about the investment in banking sector its return profile as we move forward in lower leverage environment, but we are not having any conversation to counterparties or lenders about whether they feel confident extending funds and credit to us.

<Q>: Okay, that's a good segment. And one last question this is a, your deleveraging or the connection if we go back to the late 1990's we had an equity boom and even your pears were doing only about 20 times leverage, but you are putting a rough 30% or we just right now tough to imagine in an environment like this that there will be another boom ever again, but of course there

will be why couldn't if the with a net [ph] boom that mergers in the few years is centered on something other than credit why could you go back to higher or we and has blend cross cycle to something closer to 20?

<A>: That's not possible [Indiscernible] what I wanted to do it's been very careful conservative about the - our expectation we set.

<Q>: Okay, fair enough. Thank you.

<A>: Lastly, I wanted - I wanted to come back to one earlier points of clarification, the question about the commercial mortgage line items. There are some non-consolidated equity pieces in that line item. The amount is much less than the [Indiscernible] mortgage debt and the real estate help for sales items. I just wanted to clarify they are - there is small amount of non-consolidated equity in that line items.

Operator: Are you ready for the next question.

<A>: Ma'am thank you.

Operator: The last question is from Douglas Sipkin.

<Q - Douglas Sipkin>: Yeah, hi good morning.

<A>: Good morning Doug.

<Q - Douglas Sipkin>: Just three questions, [Indiscernible]. First of a little back when you did in the first half you have indicated that you could have raised double, triple what you did sums the little curios, why you didn't take advantage that - of that at a - at a better price. Especially knowing that you were embarking on - an initiative to strength the balance sheet and likely it would - should be observing some losses along the way.

<A>: Okay. Very importantly Doug at the end of March we did not have the visibility on the loss that we ultimately suffered in the quarter. So, we didn't have that expectation I'm also as I've talked about earlier the de leveraging itself did not create a meaningful P&L event I wanted to now clear it about that. So, there were price reductions in the quarter asset write-downs associated with the environment but it wasn't because we were selling assets that we experienced significant losses.

<A>: Both of those putting it's were really not [indiscernible] relevant at that point of the end of our March.

<Q>: Okay, second question is can you just talk about the particular areas were you are starting to see meaningful pricing power I know you mentioned parts of fix things and trading could you drill down into - into some of our more specific places. What areas is really think your opportunity with capacity come it beyond?

<A>: Yeah certainly as you mentioned the flow businesses and [indiscernible] there was much higher margins to be made on trading those assets clauses that we seeing in a very longtime. Interestingly as I mentioned earlier time grow bridge [Ph] given the pull back our balance sheet across the broad in our industry the ability to charge more appropriate levels to produce our own balance sheet as been very constructive during the course of that quarter. The equity flow business, is also have been able to happened have really demonstrated our great ability to make money throughout the board we've seen a very big change in acquisition finance and our M&A activity in terms of what we can get to be extend we want a go down of path of committed financing and in fact committed financing as not necessarily equip for M&A advice. So that's a big change in general or for the relationship loans were we provide balance sheet to our clients in

parts of relationships are being charged deactively and more consisting with market levels, so its really across in the board in every asset clause and inversely happy were we doing business...

<Q>: Okay great and then finally if you just walk us through you mentioned obviously the trends of March, April, May I mean just can you if you characterize how much better of May was in April and any color on early trends into June.

<A>: Yeah, May as they mentioned with one of our best run rate revenue month so as that you pretty much could adjust straight line outward from March to May to give a feel for the change in activity and I think you are going to find when others report in our sector if that was consistent across the Board. Obviously we are only one week into June so hate to make a trend of it but the first week of June was very strong in consistent with May.

<A>: Great, thank you.

Operator: That concludes today's question and answer session.

<<Erin Callan, Executive Vice President and Chief Financial Officer>>

I want to thank everybody for joining us today again on pretty short notice. I am going to be happy to be back here talking to you weekend today and 16th with more details about the quarter and we appreciate your patients and appreciate your getting up and having the time to talk to us on this call and also for those who particularly support us in our capital rise and we look forward to moving into the next step of the paradigm and getting - getting a lot more interests in activity around the business as we proceed. So thanks everybody for today and we will be back next Monday talking to you on further detail. Thanks.