LEHMAN GAR 2008

SuperGroup	Lehman Brothers	Priority	Platinum	Consent Status	Implied – Business Risk
Submitting Unit	HBUS	Date of Proposal	May 12, 2008	Next Review Date	30 April 2009
Global Relationship Manager	Paul Lopez	Global Sector Head	Anthony Bernbaum / Mark Stadler	Customer Since	1970s
Client Relationship Manager	Nicholas J Taylor	Sector	FIG	Sub-sector	Securities

Shareholders	Widely held publicly traded company with 33% insider ownership							
Facility Grade Current : Proposed	CRR Current : Proposed	LGD %	EaD (USDm)	EL (USDm)	RWA Value (USDm)	RWA %	KMV % 1 Year EDF	5 Year CDS (bps) (05/12/08)
3:3	3.3 : 3.3	45	N/A*	N/A*	206.5	N/A*	NA	173
Parental Support Policy Status	Environmental - Sustainability Rating (External / Internal)	Equity data (USDm) / (USD) – 05/09/08				Ratings & Outlook		
		Market Cap.	Current	52 Week High	52 Week Low	Moody's	S&P	Fitch
Guarantee and/or verbal support	N/A	$24bn	$43.5	$82.1 (06/20/07)	$20.3 (03/17/08)	A1/Stable/P1	A+/Negative/A1	AA-/Stable/F1+

* N/A – per GAR support team; not applicable for Direct Submissions due to the extraordinary amount of individual limits

Facilities (USDm)	Present*	Incremental Increase*	Proposed GCRC
Cat A (Direct)	788.1	125.0	913.1
of which Secured	0	-	-
of which Committed	(100.0)	(100.0)	(200.0)
Of which FNII	(17.9)	-	(17.9)
Indirect Cat A (Fronting Guarantees) GTR	106.4	-	106.4
Cat B	2,561.2	907.7	3468.9
of which Collateralised[1]	(1,329.0)	(454.6)	(1783.6)
Total Cat S	8,633.7	874.0	9,507.7
TOTAL	12,089.4	1,906.7	13,996.1
		PRESENT GCRC	N/A

* See Appendix A for Exposure Summary & Appendix B for GCRC Rationale

EXPOSURE SUMMARY

Direct Cat A – Supports client related product cross-selling initiatives:

- With exception of committed RCFs, all direct CAT A is short-dated (<1 yr) and unsecured. The components of Direct CAT A arwe as follow.
  - 85% consists of uncommitted, overnight money market lines for liquidity support in various country markets, but majority in US & UK. Other usage is for unfunded SBLCs/guarantees provided to local exchanges, with maximum contractual maturities of 6 months. These exposures are booked against the main broker/dealer subsidiaries, which are subject to risk-based regulatory capital requirements. Also included are O/D lines supporting GTB mandates in less developed markets that rely more on traditional clearing bank funding.
  - 11% ($100m) consists of committed unsecured 3-yr RCFs. HBUS has hedged $20m of its $50m 3 year RCF via CDS.
  - 4% consists of bond underwriting line.

Indirect Cat A – Supports HSBC Trade Services & transactions originated by other HSBC lending divisions:

- Represents "guarantees" accepted (i) where HSBC is a LC fronting bank on a loan syndicate involving a 3rd party obligor or (ii) as credit support for loans extended by HSBC to 3rd party CB/MMB/PB clients. This is contingent second order risk where primary recourse is to the 3rd party HSBC loan obligor, not LEH. GRM has no control over origination of this type of exposure.

Cat B - Supports OTC capital markets professional counterparty and in part client related business:

- Requirements (majority of which is collateralized) for our Treasury and Global Markets trading / hedging/ portfolio management with LEH as a client and professional counterparty, inclusive of give-ups trading.
- 32% of total CAT B is short-dated (< 1yr). The exposure is largely against regulated broker/dealers, comprised of mostly short-term FX, FI/Eq. trading which is DVP settled, and cash or securities driven collateralized financing transactions.
- Remaining 68% consists of longer dated derivatives and options of which 67%+ is governed by CSA (collateralized with two week period of risk upon default).

Settlement – Supports both OTC capital markets (client and professional counterparty) and GTB businesses:

- 66% of the settlement limits is related to intra-day GTB payment and securities settlement, with CREST settlement bank requirements accounting for about half of these limits. Approximately 2/3 of CREST limits are collateralized by the underlying securities processed through the system, with appropriate margin (overcollateralization) embedded into system. In a CREST secured environment, HSBC's credit exposure is mitigated by the underlying securities and the system also allows such assets to repo in order to generate additional liquidity for HSBC. The client is charged for the provision of intra-day liquidity in the CREST system.
- In most instances outright cash or PCM overdrafts are eliminated with incoming funds transfers from other institutions (or outgoing securities transfers against payments) by end of the business day (e.g., zero sum game). In the majority of instances, the account parties are the primary regulated broker-dealer subsidiaries, which are considered the most creditworthy in the enterprise.

[1] Represents CSA covered facilities and collateralized financing (repo or stock lending/borrowing). Remaining portion represent short-term fixed income/equity dealing which is DVP settled, short-term FX (<1yr), and limits that are guaranteed by parent company as there are regions that cannot yet support CSA (i.e. India).

- Remaining 34% is related to trading of FX/CC Swaps which are predominantly settled via CLS – AAA clearing organization owned by the world's largest financial institutions. CLS operates in a payment vs payment environment, thus outright foreign exchange settlement risk for eligible currencies is eliminated.

[redacted]

Proposal:

1. Global Annual Review (GAR), with next annual review date of April 30th, 2008.
2. Maintain the CRR unchanged @ 3.3, which overrides output of Securities Scorecard of 2.1
3. Renew limits at existing levels. Global limit rationalization exercise has already been undertaken/completed.
4. Propose limits to regularize excesses and to support business growth (see Appendix A):
   - Propose incremental Cat B increase of $908m to regularize excesses and to accommodate business growth, but note the implementation of risk-reducing methodologies which will reduce CAT B requirements.
   - Propose a new 2 year $100m committed Cat A RCF to be extended by HBAP INM to support local GTB mandates.
5. We are not requesting an unallocated GCRC appetite, but wish to reserve the right to submit ad hoc credit requests for new limits to CRM/GHQ GMO, with appropriate Global FIG endorsement.

Recommendation:
We recommend approval as proposed due to:

- We remain comfortable with LEH's risk profile. In summary, from analyzing all information available from public and non-public sources, we consider Lehman an acceptable credit. The industry, nevertheless, is leveraged with high reliance on secured and unsecured wholesale funding sources. As a result, the individual firms are subject to crisis of confidence events that can lead to a rapid collapse of funding support, as evidenced by the demise of the Bear Stearns. Nevertheless, we gain comfort from:
  - **Regulatory Environment**:
    - SEC's Consolidated Supervision regulatory framework - the industry is now subject to consolidated or top-down prudential regulations and oversight (including Basel II implementation);
    - In addition to bank units, U.S. broker dealers now have access to direct central bank funding (Primary Dealer Credit Facility, Term Securities Lending Facility and Term Auction Facility). Foreign regulated bank &/or broker-dealer subsidiaries to the applicable ECB and BOE programs.
    - In addition to granting broker-dealers direct access to Fed window, senior U.S. policymakers and regulators (i.e. Messrs. Paulson & Geithner) have also publicly acknowledged that the largest investment banks are critical to market functioning and economic health. The business models of banks and the largest securities firms (i.e., GIBs) have converged, with banks playing a greater agency role in the credit process, and securities firms doing more of the financing.
  - **Client's Risk Management & Corporate Governance**:
    - Historical performance through the peaks and troughs in the capital markets cycle. Recent results have been satisfactory and it seems that Lehman has escaped the worse of the global credit crisis;
    - Solid risk management infrastructure including systems, controls and oversight (strongest in the peer group);
    - Strong corporate governance & absence of repetitive or material reputation / regulatory missteps;
    - Strong liquidity management framework which again is arguably strongest in peer group;
    - Structural funding support for mortgage and commercial assets through use of regulated bank entities in legal structure to originate and portfolio such assets;

- We remain comfortable with HSBC's exposure to LEH, which is primarily short-dated (<1yr) and subject to risk mitigation via CSAs that govern OTC trading activities.

- Strong relationship income:
  - Solid relationship revenues/returns which support the level of exposure.

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[2] Cash Capital Ratio= Long-Term Capital / Net Assets
[3] Liquidity Ratio w/ Stress Test= Unencumbered Liquidity Pool of Parent Company, Regulated and Bank Units / (Short-Term Financing + 50% of Non Investment Grade Commitments and CSA collateral required for one notch rating downgrade)
[4] Adjusted Leverage Ratio= Net Assets / Capital Funds
[5] Long-Term Capital / Lvl 3 Assets = Long-Term Capital / Level 3 Assets

- HORIS growth of 40% in 2007 to [redacted] (60% out of Asia; main product areas are HSS and PCM). Going forward the priorities are to grow the GTB business (focus on Middle East, Asia and Latam), support continued trading as a major professional counterparty and penetrate institutional investor buy-side windows.

- Areas of vulnerability remain relating to adjustment of intermediation business model, revenue generation and Lehman's large remaining exposure to real estate (largest in peer group). Given the aforementioned, combined with uncertain credit and economic environment, over the next 12 months our priorities for this relationship will be, in order:

1. Minimize risk – pursue a collateralized model in both banking and trading books.
2. Enable markets trading. Where possible, confine OTC derivatives trading to CSA and CRISP eligible transactions in the key treasury centers of HBUS, HBEU, and HBAP. We anticipate exceptions to this guidance in markets where we maintain a GTB relationship with the client, but inadequate legal &/or operational framework to support CSAs. In such non-CSA jurisdictions, risk will be controlled by limiting tenor profile of limits.
3. Protect existing revenue sources.
4. Grow revenue in specific products / regions.

Section 1 - Relationship

1.1. HSBC Relationship

Relationship Strategy	Grow	**Client Buying behaviour**	Credit Cross Sell	**Major Risk/Relationship Reassessment**	Very close monitoring
Exposure Strategy	Maintain	**Estimated Ranking in Banking Group**	Committed Credit Top 30 / Overall Credit Provider Top 10	**Relationship Zone**	Diversified

HORIS Income

- All profitability hurdles were exceeded in 2007 which saw 40.4% HORIS growth.
- 1Q2008 HORIS operating income is up about 110% over the comparable period a year ago to [redacted]. This is primarily due to surge in GTB income in ASP, attributed to deleveraging resulting in higher NII income, regulatory induced change in P-notes (India) and higher transactional volumes.
- AOP 2008 is 20% yoy HORIS revenue growth, which is expected to be driven by:
  - HSS - primarily IFS & CNC in Europe/ME and Asia/India. There is ramp-up of existing markets and strong expectation of winning new ASP & LatAm (i.e., Brazil) markets as come up for bid. Crest liquidity charging implemented at end of 2007, and has contributed to growth in Corporate Banking line item.
  - PCM - In 2008, most of growth projected in Middle East and US, as well as ASP.
  - Global Markets - mainly FX out of Asia incidental to CNC & rates out of US due to interest rate swaps transacted with Lehman's MBS securitization trusts.
- Professional counterparty activity, inclusive give-ups, does not contribute HORIS revenue.

[redacted]

Client vs Professional / Flow Revenues:

- Similar to other GIBs, revenues are generated from "client" or "buy-side" activity, not from "professional counterparty" or "flow" related activity. **As shown below, only 44% of the exposure (CAT A and CAT B) is deemed client-related, generating all of the HORIS profitability**. The balance of exposure is to accommodate "Mother Bank" needs.

	Professional Counterparty*	Client	Totals
Exposure (millions)			
Cat A	124	770	894
(of which committed)		(100)	(100.0)
Cat B	1,792	768	2,561
Settlement	2,937	5,698	8,635
Totals	4,853	7,236	12,089
Rev. (millions)			
GTB & Banking	0	20.960	20.960
Global Markets	0	9.399	9.399
Private Banking**	0	10.679	10.679
Totals	0	41.038	41.038

* *Professional counterparty & liquidity provider – supported in part by Cat B and TSL lines. Includes give-up arrangements and/or assignments, whereby a direct Global Markets client such as a hedge fund or asset manager is "borrowing" or able to transact on HSBC's credit relationship maintained with the investment bank (i.e. Lehman), which is the underlying client's prime broker.*

** *Structured Products sourced by Lehman and distributed to HSBC PB Clients.*

Relationship Summary

- Lehman interacts as a professional counterparty, a client and a competitor. It is one of FIG's most profitable client relationships and the fourth most profitable of the US Broker Dealers.
- HORIS revenue growth in 07 of 40.4% to [redacted] There is strong potential for further growth across many geographies and product areas as the relationship is immature and the company's growth is focussed on Europe, Middle East, Asia and LatAm.
- Global Banking and Markets FIG maintains an extensive and coordinated calling effort with the customer's multiple regional buying windows in the corporate, brokerage and asset management arms.
- For the client relationship, there is a strong and direct correlation between the provision of funding support and revenue growth. Lehman manages credit relationships very effectively and in a globally coordinated fashion (centralized creditor relationship function within Treasury) ensuring credit support is rewarded and lack of support penalized.
- Accordingly, FIG tightly manages the efficient use the Cat A and Cat B credit appetite to help meet the clients funding priorities whilst maximising revenue growth
- Cat B and TSL limits support both professional counterparty trading (on a price and best execution basis) and liquidity provision to HSBC's Global Markets, Private Banking and Asset Management business units. The latter professional counterparty roles do not generate relationship P&L for use of credit.
- Professional counterparty trading is primarily executed through electronic trading platforms and inter-dealer brokers on an agency or riskless principal basis if anonymity is desired.
- Professional counterparty includes give-up arrangements and/or assignments, whereby a Global Markets hedge fund or asset manager client utilizes their Prime Broker's (i.e. GIB) credit lines with HSBC.

Relationship Strategy

- Control risk exposure by pursuing a fundamentally collateralised model in both banking and trading books.
- Maintain HSBC's position as a major professional trading counterparty globally.
- Protect and grow GTB business globally (HSS and PCM).
- Penetrate the institutional investor buy-side (i.e., asset management) windows.
- Build reciprocal debt securities issuance business and syndicate relationships.
- Provide liquidity through secured arrangements (repo, stock borrow, TRS, etc).

Full execution of this strategy will require limited but consistent committed credit support (Cat A) in "flagship" facilities as well as occasional non-traditional financings. We will maintain strict discipline on credit exposure growth, particularly Cat A, and expect revenue growth to substantially exceed RWA growth.

1.2. Reciprocity

Reciprocity management remains a challenge across many Group businesses. Overall, Lehman appears to be a significant net beneficiary of reciprocal business from our private banking and asset management units. Relationship Management must improve leverage but to do so effectively requires quantum improvements in MI, particularly in transparency of value and opportunity.

Credit Provision

- Lehman is not currently a lender in HSBC Finance Syndicated Facility (they have been asked but declined).
- Capital Markets reciprocity has continued to be sharply scaled back through 2007 due to reduction in HSBC Finance fee wallet, inclusive of issuance & derivatives.
- 2007-08 business opportunities for Lehman include:
  - Credit derivatives trading flow with HSBC loan portfolio
  - Asset management (offshore funds) sales & distribution arrangements through HSBC network.

1.3. Competitor & Wallet Analysis

Perceived Total Value of Client Wallet (USD000)	2,173,000

Lehman's exceptionally large wallet covers most of our Global Banking and Markets proposition. We assume we are not going to benefit from material capital structuring, de-risking or M & A Advisory dialogue. Massive opportunities exist globally across securities and institutional investor product sets, including:

- HSS (CNC, CTLA, IFS and AFS)
- PCM (payments and multi currency clearing)
- Securities clearing (LatAm & ASP)
- Securities lending & repo (both financing & trading/collateral driven)
- Structured finance involving less liquid assets
- DCM issuance in countries where they are not represented
- Fixed income and equity sales
- Derivatives
- Commodities (trading, custody and clearing)

Our ability to tap this wallet is driven by a) consistent credit provision, b) geographical footprint, c) product capability and d) coverage capability.

- We are not a top 10 lender. HSBC provides the necessary level of committed support and has an exceptionally good geographical footprint match outside the U.S. They have a growing European (inc. CEE), Middle Eastern and Asian business.
- ***Americas***: Although our product proposition is constrained in the U.S. (no CNC platform), our competitive capability elsewhere is generally sound. LatAm (i.e., Brazil, Mexico) are priority markets in the Americas, leveraging the "globalized" (HBAP) CNC service platform.
- ***Asia***: Standard Chartered, Citibank and local providers are our strongest competitors but we have a top rated CNC platform and have the opportunity to significant further growth in across HK, China, Korea, Taiwan and India.
- ***Europe & Middle East***: Outside of GBP and CREST clearing, our GTB product and service platforms have struggled to compete against BNP, JPM, Citi, DB etc. The exception is the Middle East, due to the strength of the "globalized" CNC platform.
- ***Emerging Markets***: In most emerging markets, PCM should piggyback off CNC.
- Coverage is established in the US and over the past 12 months has been strengthened in Europe, Asia and the Middle East.
- Lehman management has favorably acknowledged HSBC's credit support during difficult market environment, which should allow us to capture market share from banks that have cut back or withdrawn from industry, particularly in emerging markets.

1.4. Pipeline Summary

Deal Title	Products	Status	Up-front Revenue (USD000)	Annual Revenue (USD000)	Expected Mandate Date	Probability of Success %	Originating Country
RFP for CNC in Brazil	CnC	Pitched	0	1,000	6/30/08	50%	US
$150m LoC for Lehman in Australia, priced at 50bps.	Trade Services	Pitched	0	750	5/31/08	50%	Australia
$75m Insurance LoC, priced at 100bps	Trade Services	Pitched	0	750	5/31/08	50%	US
Insurance G/O, Back Office Outsourcing	Futures & Other Markets; HSS: Sub-Custody & Clearing; PCM: Account Services Products	Pitched	0	500	5/31/08	50%	US

Section 2 – Credit & Risks

CRR and Ratings						
Model Used (*)	Model Output CRR	Recommended CRR*	Reason for Override (if applicable)	S&P Rating	Moody's Rating	KMV EDF
NBFI Scorecard	2.1	3.3	Difficult operating environment and likelihood of further write-downs given Lehman's remaining magnitude of mortgage exposure	A+	A1	

(*) Securities scorecard overridden in assigning CRR

2.1. Key Risks & Mitigants

Key Risks for the Lehman:

- Liquidity (funding of regionally diverse global operations)
- Capital
- Overall business model and revenues
- Asset quality (remaining exposure to Alt-A & commercial real estate)
- Market risk
- Undisclosed off-balance sheet liabilities

<u>Liquidity Risk</u>

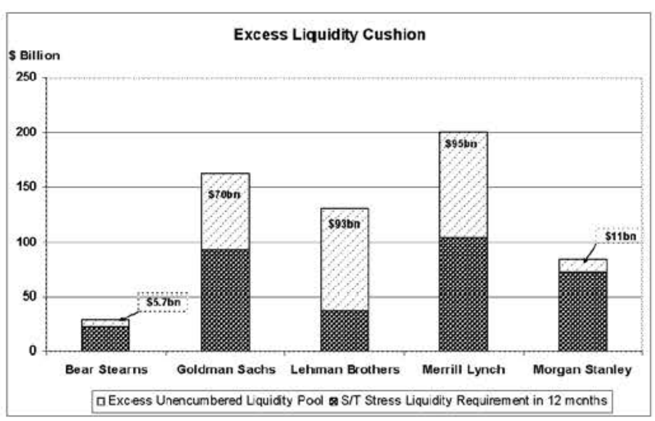
Summary: Lehman has built strong defenses against this risk, including 1) established excess liquidity cushion, 2) reduced reliance on short-term debt combined with distributing & lengthening debt maturities (secured & unsecured), 3) elimintated funding reliance on customer collateral and free credit balances, 4) diversified its funding sources and 5) increased access to traditional commercial bank funding sources through legal entity structure. In addition, Lehman, a Primary Dealer can now access central bank secured funding schemes for overnight and term financing.

- **LEH is not Bear Stearns**, both structurally and in terms of robustness and application of its liquidity management disciplines.
- It is important to note that the primary legal subsidiaries are also rated, thus the liquidity position of such subsidiaries has been subject to independent examination and assessment from a bottom-up perspective as well.
- Since it is the primary issuer of unsecured financing for the consolidated enterprise, the Holdco is the legal entity that bears the refinancing risk if unsecured financing dries up. Refinancing risk at the Holdco is mitigated by the liquidity pool on its own balance sheet and its ability to rely on the repayment of subsidiary advances. The liquidity of subsidiary advances cannot be discerned from public filings, but it is common practice for the Holdco to limit such advances to short duration.
- Regulated subsidiaries bear most of refinancing risk if secured (repos & stock loan) financing dries up. Refinancing risk at the subsidiary level is mitigated by maintenance of own unencumbered securities pool for alternate liquidity purposes, over-funding in the tri-party market (against lower quality collateral), greater reliance on term and extendible secured funding structures, and now, the ability to access Fed and ECB windows (See Section 2.6 Industry Highlights).
- As of April 2008, Lehman indicated that the average tenor of its repo book has been at about 30 days.
- The firm continues to be focused on adding term secured financing, inclusive of equities, focusing on counterparties that deal in and are familiar with underlying asset class, have long and deep funding/trading history with Lehman (i.e., clearing banks, large asset managers).

Excess Liquidity Cushion

- **Our analysis indicates that LEH' EXCESS LIQUIDITY CUSHION (even under stressed scenario) is estimated to be over <u>$93bn, second strongest among its peers</u>.**
- The firm's liquidity pool (cash & unencumbered securities) is managed on a global basis, with currency, geographic and legal entity components.
- EXCESS LIQUIDITY CUSHION (stressed) is defined as:

  Global cash component ($33bln @ 3/20)
  (+)
  Unencumbered assets
  (-)
  All maturing unsecured obligations within 12 months
  (-)
  Additional collateral required under CSA (assume 1 notch ratings downgrade)
  (-)
  Assumed 50% funding of non-investment grade commitments.

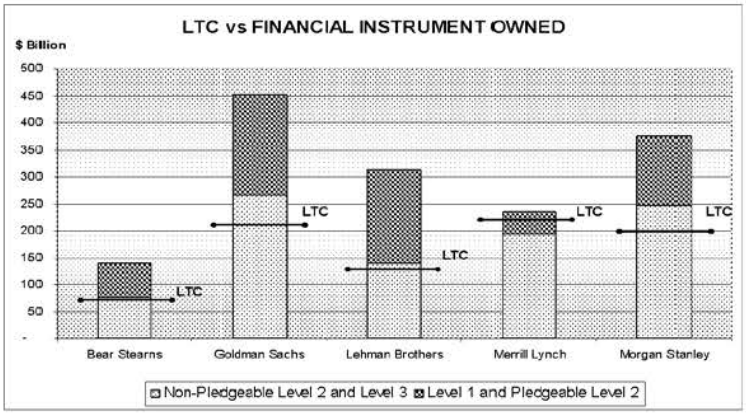


<u>Capital Adequacy Risk</u>

Summary: The company is well capitalized (tripled long-term capital or "LTC" in the last 4 years to $153bn @ 1Q08) and continues to access the capital markets, even if at higher spreads. As Bear Stearns once again illustrated, even a "well-capitalized" financial institution can collapse very quickly absent liquidity. The best mitigant against this risk (run on the

bank) is to curtail gross leverage, the build-up of less liquid assets, and reliance on short-term debt. We expect the industry to reduce leverage (&/or raise more capital) in an orderly fashion to voluntarily reduce risk profile, but also resulting from prodding of regulators. Lehman is well on course to reducing leverage, which is reinforced by both management statements and actions to date.

- Our analysis indicates that LEH's LTC can absorb / finance level 3 assets *in their entirety* and a significant portion of level 2 assets that are repo ineligible (i.e. equities & derivative receivables) with the Federal Reserve under the PDCF and TSLF programs (see chart below, yellow shade). This coverage ratio is estimated at 90%, which is considered solid and is the second strongest coverage behind ML. All of LEH's trading assets or inventory is marked-to-market daily inclusive of bank securities and loan portfolios.



- LEH's equity capital was also bolstered by recent (April 1, 2008) issuance of $4bn convertible preferred equity, which augmented shareholders' equity and reduced gross and net pro-forma leverage.
- Unlike most other GIB enterprises, the primary US registered broker-dealer entity (EFHC), issues subordinated notes placed with 3rd party investors, which qualify as regulatory capital. These direct issuances limit the amount of senior debt downstreamed by holdco as subordinated debt and thereby, total enterprise capital double leverage.

Continued access to capital markets:

- Lehman has continued accessing the capital markets with limited impact on spreads. Even with CDS gapping out during the quarter, the company tapped the market numerous times, with the result that it has already completed about 95% of its funding needs for 2008 (and this is to fund growth as well as maturing debt). The company issued $4bln senior debt at a coupon of 5.625% (5 yrs), a further preferred issue of $1.9bln in Feb08, and $2.5bln of senior notes at a coupon of 6.875% (10 years) in April. CDS spreads have continued to fall during past couple of weeks and are now trading well inside 200bps again.
- The holdco's liquidity pool was $34bn at the end of Q1 driven by a reduction in commercial paper. In addition the holdco has $64bn of unencumbered assets and $99bn at the regulated entities. Net leverage has declined to 15.8x @ 1Q08 from 16.4x at year end, which is still above historical norms and with further de-leveraging a management priority.
- The company issued $4bn convertible preferred equity securities in April 2008 to enhance its capital position. The transaction was well oversubscribed and underscored its full access to capital markets.
- Lehman has emphasized that a "substantial amount" of its repo collateral is eligible to be pledged to the Federal Reserve discount window, through its broker-dealer subsidiary.
- In addition, the company has used its structuring capabilities to create liquid, highly-rated, investment grade securities (e.g., through CDOs or CLOs) out of its less liquid holdco or non-regulated subsidiary unencumbered securities liquidity pool that can also be pledged to the PDCF.

Business model and revenues

Summary: **Given its fundamental benefits in dispersing risk and economic value, we do not believe the "originate to distribute" business model is dead, but certainly on vacation, until issuers, underwriters, regulators, rating agencies (i.e., new methodologies) and investors enhance the prudential framework governing such activities. We think the long-term prospects for a well-run, client-driven, innovative and nimble independent investment bank such as Lehman remain promising, though the industry may generate lower returns "through the cycle" going forward.**

- Business profile of these firms is conductive to volatility in earnings from exogenous market performance: 33% Equities, 31% Fixed Income, 20% Investment Banking and 16% Investment Mgmt.
- That said, Fixed Income business is comprised of non-correlated activities (Prime brokerage, FX and commodities; Interest Rate; Credit; Securitised Products and Real Estate) which have intra-compensated under-performance amongst some of them.
- Heavy exposure to the US (at 50% of total revenues) but decreasing (was 63% in 2006). The firm is trying to diversify with strong commitments to developing Middle East, ASP and LatAm.
- Increase in proprietary trading (in-house hedge funds), non vanilla ABS issuance inclusive MBS and CDOs and funded leveraged loans, significantly increased overall risk profile (see further on VaR below).
- Increase in merchant banking/private equity and alternative investment management activities seeded with firm's own capital. We anticipate such investments to continue to rise due to enhanced focus on "distressed" opportunities in 2008, similar to prior credit cycles. Principal transactions and investment banking revenues as well as asset management revenues may be adversely affected in 2008 due to lower principal gains or even mark-downs, as well as reduced performance-driven fees.

- The rapid expansion of structured finance, particularly securitization, along with investors' insatiable search for yield, caused the "originate to distribute" business model embraced by the industry to thrive. As the current credit crises has illustrated, these financial developments have resulted in banks increasing their exposure to liquidity, particularly as it resided off-balance sheet and hidden to own management and most regulators.

Asset Quality

Summary: We expect Lehman to manage through what are obvious real-estate related asset concentrations on its balance sheet built up as a result of illiquidity across financial markets. This expectation is based on firm's proven risk management acumen, earnings contribution from its other global businesses that have and are likely to continue to offset the weaknesses in real estate, and its stable liquidity position, which provides time for the firm to manage through and reduce its risk profile in an orderly fashion. We note that the firm has continued to print CMBS & CLO deals in 1Q08 ($5bn after quarter-end), which has allowed the firm to offload some of its inventory to investors.

- Continuing build-up of less liquid &/or illiquid risk assets on the balance sheet is the key risk, as evidenced by rise in level 3 assets. The growth rate in such assets tapered off in 1Q08, which is an encouraging and positive sign. Level 3 assets increased to $42.5bn or 13% of inventory positions @ 1Q08, from $20.8bn (7%) @ 2Q07, resulting mainly from the reclassification of certain level 2 assets (i.e., mortgages & ABS) into level 3, and acquisitions (private equity & funded loans).
- The key management misstep appears to have been to continue to originate assets, particularly leveraged loans, ALT-A and commercial mortgages when the securitization and secondary markets for such assets were already seizing up. We believe management was originally too optimistic in its assumptions on the duration and breadth of the credit dislocation. In addition, it takes time to slow or reduce origination and for commitments to customers to roll off.
- Nevertheless, liquidity has not been an impediment to the firm carrying such assets until more suitable exit opportunity materializes. Selling such assets in a fire sale or when current valuations may reflect not only actual or likely fundamental value erosion (i.e., credit losses) but also an illiquidity discount and technical pressure from heavy shorting is not a viable option.
- Although Lehman remains exposed to the U.S. mortgage business, the firm has significantly scaled down its mortgage-related operations and its participation in other troubled asset categories is limited:
  - Does not own or sponsor any SIVs.
  - Net exposure to monolines is small due to hedges and credit reserves against these exposures.
  - Modest long position in ABS CDO (i.e., VIEs) due to smaller market share & focus on distribution of all parts of capital structure. Modest off-balance sheet VIEs where it has provided guarantees to investors.
  - Significantly reduced its unfunded non-investment grade acquisition lending commitments.
  - In ABCP market, generally participates as agent, and only provides liquidity backstops to a very limited extent to programs.
- 1Q08 balance sheet included $101bn in gross ($81bn net investment) real estate positions (RMBS, CMBS, properties, REITs, whole loans) down slightly from $105bn ($84bn) @ FYE07, which is the largest exposure in the peer group.
- Within real estate, the first is most exposed to further loss in its commercial mortgage position, which is considered the most difficult to hedge. As of the end of 1Q08, the firm's commercial mortgage balance was $36.1bn (down from $38.9bn @ FYE2007), excluding FAS 140 gross up.
- Though underlying credit performance has held up very well, the CMBS market has effectively shut down and spreads have widened considerably, as reflected by the CMBX indices leading to marks taken on these assets ($1.4bn gross/$1.0bn net of risk hedges in 1Q08). Management believes that the fundamental value of such assets is not impaired, with the following considerations providing some flexibility in seeking the best value proposition in exiting positions:
  - Whole loans are of high quality with overwhelming majority with LTV < 80%
  - The loans are performing and overall default rates on commercial real estate remain low by historical standards
  - Diversification by property type & geography
  - Will hedge exposure to extent possible (i.e., CMBX), looking to generate returns from structuring/securitization
  - Positions financed by long-term debt, thus would be considered "unencumbered" collateral
  - Positions held in bank units, thus could be pledged to alternate liquidity sources of such units (i.e., FHLBs, Fed, ECB)
  - Positions have been liquidated or sold in range where management has marked them in the book

Market Risk

***Summary:* While VaR increased throughout FY07 on an absolute basis, VaR in relationship to tangible equity has remained less than 1%. VaR trended down during 1Q08 and ended the quarter @ $106m (vs $124m @ FYE07), which is consistent with management's strategy of reducing its risk profile.**

- Stress VaR/Tangible Equity ratio is 30%. While the absolute level has increased in recent years, LEH' tangible equity base growth has largely outpaced that of absolute VaR.
- Similar to most of Street, VaR has increased sharply since 2Q07 mostly due to higher volatilities in the market combined with increases in inventory positions. VaR is more heavily weighted toward recent market action.

	Bear Stearns	Goldman Sachs	Lehman Brothers	Merrill Lynch	Morgan Stanley
Ave VaR/Tangible Equity	0.58%	0.88%	0.95%	0.44%	0.75%
High VaR/Tangible Equity	0.90%	0.68%	1.19%	0.83%	0.56%
Stress VaR*/ Tangible Equity	22.87%	17.17%	30.19%	20.92%	14.20%

* Stress VaR represents an aggregation of all reported highs by risk sector (interest and credit, equity, commodity and currency) and excludes diversification assumptions, defined as "High VaR". High VaR is then multiplied by the square root of ten linearly creating an estimate of exposures to a ten day holding period and then multiplied by eight to simulate a market stress. 95% Confidence Interval.

Source: Fitch Ratings Special Report 4Q07 Peer Data For Securities Firms

- We recognize that VaR is an incomplete measure, as it does not quantify extreme risks in the tails of the distribution and the credit and market risks in less liquid assets. Accordingly, we monitor the growth and composition of less liquid assets to gauge the scope and trends in the organization's risk appetite. It is important to note that real estate investments (i.e., real estate held for sale) are not financial instruments & therefore not contemplated within the VaR calculation.
- Technically, the robustness or effectiveness of LEH's VaR model can be inferred from a publicly reported statistical measure: the historical daily net trading revenues frequency distribution, which would detail how many times during the period the daily trading losses exceeded the reported aggregate net trading VaR amount. A 95% confidence interval means there is a 1-in-20 chance that actual daily trading net revenues would be expected to decline by an amount in excess of the reported revenue volatility measure ($48m for FY07). Lehman reported 16 days in FY07 with daily trading losses exceeding $25m, up from 2 in FY06. This actual experience would slightly exceed the statistical expectation in a 95% confidence interval, but is still superior to the results of most other firms during this period of high market volatility and illiquidity.

Undisclosed off-balance sheet liabilities

***Summary:* Lehman's disclosure while not perfect and certainly room for further improvement has improved measurably and can be argued is the best in the peer group in terms of transparency. From this disclosure, we can surmise that Lehman's exposure or risk to off-balance sheet obligations is by far the smallest in the peer group, due in large part to discipline maintained around distribution. While these risk amounts do not represent an insignificant burden on the profitability of the firm in worst case scenario, it is unlikely such burden will hit all at once, but spread over several quarters. In addition, and potential liquidity demands relating to unwind of such vehicles or put back to the firm can be absorbed under its contingent liquidity framework. It is also important to note that such highly rated instruments can now be pledged to the PDCF &/or TSLF.**

- The industry has been actively involved in structuring and underwriting CDOs, CLOs, conduits and CLNs which take the accounting form of Variable Interest Entities (VIEs), which are either consolidated or unconsolidated based on certain accounting tests. In connection with these activities, the firms provide downside protection guarantees to investors guaranteeing return of their principal investment.
- The primary concern expressed relating to VIEs regards the additional liquidity stress that may be brought to bear on the "sponsor" should the trustee of the VIE be required to liquidate assets in the event certain loss levels are triggered. While under no legal obligation to do, the sponsor make take the underlying assets onto its balance sheet, particularly in times of secondary market illiquidity, either to limit its losses under the guarantee to investors or reputational and franchise considerations.
- The actual risk of loss to the sponsor is mitigated by the underlying assets of the VIE which serve as collateral for the guarantee obligation and any hedging strategies put in place. There is insufficient disclosure or granular detail on the underlying assets of the VIEs, current ratings, and loss rates experienced on the collateral as well structural details to make an adequate assessment on whether such guarantees will be called upon.
- Lehman discloses "maximum exposure to loss (fair value)" in credit default related and mortgage related unconsolidated VIEs totalling $6.6bn, as of 1Q08. Consolidated VIEs totalled $9.3bn ($6.0bn net non-recourse financing) included in real estate available for sale, as of 1Q08. Such low exposures illustrate the firm's "moving" versus "storage" principles and discipline.

2.2. CDS Benchmark

Pricing / CDS Benchmark (USD 000)	**Annualized**
Cat A committed facilities	100,000
Tenor (years)	3
CDS (bps)	197.0
CDS cost (per annum)	1,970.0
Operating Income derived from Cat A committed facilities	N/A
Opportunity Profit / Loss	N/A
Operating Profit before Provisions	N/A
Operating Profit before Provisions & after CDS cost	N/A

2.3. Company Background

Lehman Brothers was originally founded as a partnership more than 155 years ago. It was acquired by American Express in 1984 and subsequently spun off in an IPO in 1994. Lehman is now a public company whose common shares trade on the NYSE. Employees own approximately one-third of the firm. Lehman offers an extensive, yet restrictive, stock award program so that employees think and act like owners. The company operates under three main business lines:

- **Investment Banking** underwrites securities for corporate and government clients and provides M&A advisory services to corporations and governmental entities in the U.S. and abroad.

- **Capital Markets** provides securities sales, trading, and research for institutional clients and acts as a market maker in a wide variety of equity, fixed income, and derivative products. The company is a leading trader in corporate debt (both high-grade and high-yield), ABS, MBS, CMBS, Municipals, and is a major dealer in CP. Lehman's distribution network includes a large sales force with a worldwide presence, backed by a highly regarded research department. Capital Markets also includes a modestly sized risk arbitrage portfolio and provides secured financing and securities clearing to prime brokerage customers.
- **Investment Management** segment, formerly Client Services, consists of the global Private Investment Management and Asset Management businesses. Private Investment Management provides investment and wealth management services to high-net-worth individuals and businesses. Asset Management consists of Neuberger Berman, acquired in 2003, other smaller acquisitions, and Lehman's organically grown asset management business.

2.4. Management

The company's Executive Commitee is the principal governing body of Lehman Brothers, and is comprised of representatives from every major area of the organization, including the senior managers from the company's operations in the European and Asia Pacific regions. The Executive Commitee facilitates management's ability to run the business as a whole, as opposed to managing the business units separately.

Executive Committee:

Chairman & CEO: Richard S. Fuld	Vice Chairman & Chief Legal Officer: Thomas A Russo
President & Chief Operating Officer: Joseph M. Gregory	Global Head of Mortgage Capital: Theodore P. Janulis
CEO of Lehman Brothers Europe: Jeremy M. Isaacs	Global Head of Global Fixed Income: Andrew J. Morton
Chief Operating Officer, Europe & Middle East: Benoit Savoret	CEO of Lehman Brothers Asia: Jasjit S. Bhattal
Global Head of Investment Banking: Hugh E. McGee III	Global Head of Investment Management: George H. Walker
Head Strategic Partnerships & Princpal Investing: David Goldfarb	Chief Financial & Administrative Officer: Erin Callan
Head of Client Relationship Management: Stephen M. Lessing	
Head of Global Equities: Herbert H. McDade III	

This management structure is reinforced by a control infrastructure to monitor and manage each type of risk on a global basis throughout the company. Like other firms, Lehman Brothers follows a multi-level, overlapping approach for monitoring and managing its market and credit risk which includes many independent groups (i.e., Risk Committee, Global Risk Management Division, Market Risk, Trading Management, Middle Office, Product Control, Audit, Finance, Legal and Compliance). The base level of control is at the trading desks where various risk management functions are performed, including daily mark to market by traders and on-going monitoring of inventory aging and pricing by trading desk managers, product area managers and the independent risk managers for each product area. The next level of management of market risk occurs in the Trade Analysis department, which independently reviews the prices of the company's trading positions and regularly monitors the aging of inventory positions. The final level of the risk management process is the Risk Committee ("RMC"), which is composed of senior management from the various product areas and from credit, trade analysis and risk management. The RMC, chaired by the CEO, is the primary vehicle for establishing the firm's overall risk appetite and setting risk control policies and procedures. The Global Risk Management Division ("Group"), which also reports directly to the CEO, functions as the executive branch of the RMC. The Group utilizes qualitative as well as quantitative information in managing trading risks.

2.5. Strategy

Main Strategy for the Client	Geographic Expansion ; Improved Market Share ; Reduce Cost Base

- Strategy is to grow market share and diversify by business, clients and geographies.
- Key product drivers are Asset Management, Prime brokerage, Fixed Income (energy & commodities, EM, credit products).
- Key thrust ex US is Asia, Australia, Emerging Markets (Turkey, Brazil & others) and Gulf Cooperation Council (GCC) states.

2.6. Industry Highlights

Client's Industry Trends	Consolidating
Client Stage	Late

Fundamental Credit Trends:

- The US Securities Industry continues to face a more difficult funding environment in 2008, with much higher costs or widening of risk premiums and less availability of funds. This extends to certain secured funding (i.e., repos backed by mortgage whole loans), off-balance sheet asset-based funding through bank sponsored or independent conduits and other structured finance sources (i.e. TRS & structured repo). Structured finance was used to finance mostly consumer and less liquid assets prior to securitization as well as provide higher yielding products to targeted investors (i.e., SIVs and auction rate note programs). Due to widespread contraction of liquidity in the structured finance market, we expect firms to be much more judicious with capital.

- While universal bank and broker risk spreads were right on top of each other prior to the market dislocation, they have widened out due to brokers' greater reliance on wholesale funding sources and investors' perception of vulnerability to heightened systemic risks. Nevertheless, the brokers have continued to show that they maintain access to the capital markets. We anticipate management to rein in certain business areas (i.e., balance sheet), enhance return hurdles and maintain focus on priority clients.

- Various indices including those for ABX, CMBS, RMBS, investment grade CDS and leveraged loans have become the only available source of public pricing information on less liquid assets and are used as proxy or reference by market participants (i.e. hedge funds) to either speculate (long or short), hedge or price own positions, thus influencing and even potentially manipulating accounting/market valuations, though fundamental credit quality of assets not impaired.

Liquidity Management:

- On the liquidity management front, the independent investment banks have been historically disadvantaged to their commercial or universal bank brethren due to their greater reliance on wholesale funding sources, which are less reliable in times of stress. Nevertheless, the investment banks' robust cash capital models have so far enabled the industry to weather the storm, thus maintaining the confidence of core industry lenders and investors, albeit at higher risk premiums.

- Firms have augmented the funding of good quality collateral through bank units that operate in a deposit protected or insured environment (i.e. FDIC) or have access to FHLB advances and ECB repos. These options were not available to Bear Stearns.

- Firms are also now able to tap the Fed window and other central bank liquidity schemes for more reliable collateralized funding at reasonable pricing and haircuts to alleviate any liquidity pressures. This option was also not available to Bear Stearns.

Regulatory support:

- The Federal Reserve has taken unprecedented steps in order to ensure market stability in the wake of Bear Stearns' collapse. The Fed has established additional sources of liquidity through:
  1) **Primary Dealer Credit Facility** ("PDCF"), which allows LEH and other primary dealers to pledge a specified range of collateral (investment-grade corporate securities, municipal securities, MBS, and ABS) to obtain overnight loans; and
  2) **Term Securities Lending Facility** ("TSLF") that will lend up to $200bn of Treasuries to LEH and other primary dealers by a pledge of Agencies debt, Agencies MBS, private label AAA RMBS, CMOs, CMBS and other asset-backed securities excluding CDOs, CLOs and CBOs. TSLF allows primary dealers such as LEH (EFHC subsidiary) to swap difficult-to-finance securities with the Federal Reserve for up to 28 days and receive Treasuries in return.
- There are also two primary international central bank funding initiatives: 1) participation in the BOEs open market operations, which provide members with central bank money via short-term repos, long-term repos and outright purchases of high-quality bonds, and 2) participation in ECBs open market operations and standing facilities (LEH has access through LEBB).
- The U.S. Treasury is currently developing a new regulatory framework for industry regulation and oversight. We believe this is a positive step as US Treasury is taking pro-active steps to ensure that there is a stronger regulatory framework going forward.

Legal Structure Trends:

- Investment bank consolidated holding company capital requirements under the CSE framework are modelled after Basel II metrics (i.e., Tier 1, Tier 2 and RWA). Public reporting of these metrics is expected in latter part of 2008, facilitating greater transparency and comparative analysis of financial institutions (banks & non-banks).
- Over time, due to CSE framework implementation, consolidation of legal entities with the emergence of passport or multi-branch bank entities in Europe.
- Bank operating subsidiaries are likely to represent an increasing percentage of consolidated balance sheet footings as they are more suitable funding vehicles for certain assets and conduct customer lending activities, including warehousing. As reflected by the rise in Level 3 assets, portfolio activities in bank subsidiaries are likely to be temporarily augmented for "money good" or performing assets rather than a distressed sale due to current lack of buyers.
- In context of aforementioned along with early adoption of FAS 157 on enterprise-wide basis by industry, greater earnings volatility and uncertainty are inherent due to wide swings in market valuations of assets (and liabilities). This includes dealer and bank portfolios of loans and securities.
- In preparation for the adoption of Basel II capital standards (i.e. Tier 1, Tier 2 and Total Capital) in 2008, Lehman and its peers have issued large amounts of subordinated debt and preferred stock, including hybrids over the last 2 years.

2.7. Peer Group Analysis

Key global peers are Goldman Sachs, Merrill Lynch, and Morgan Stanley.

Fiscal 2007	Goldman Sachs	Morgan Stanley	Lehman	Merrill Lynch
Ratings	Aa3/AA-	Aa3/AA-	A1/A+	A1/A+
Market Cap (M) (5/6/08)	81,141	52,269	24,161	41,768
5 year CDS (bps) (5/6/08)	86.8	106.5	155.5	144.6
Return on Equity (%)	30.56	8.83	20.05	(19.75)
Adjusted Leverage (X)	9.8x	17.3x	10.2x	15.03x
Total Capital (M)	240,274	252,701	145,640	230,019

*Year End 2007 Data
Adjusted Leverage= Net Assets / Capital Funds
Total Capital = Long-Term Capital

- The four remaining U.S. securities houses have similar business profiles, with some being more diversified than others, such as Morgan Stanley and Merrill Lynch, which have retail brokerage and private client operations that arguably remove some "through the cycle" revenue volatility as well as sizable retail and institutional asset management operations, which tend to contribute more annuity-based fees.

- Subprime and structured securities write-offs have had varying impacts on industry participants with Bear Stearns, Merrill Lynch and Morgan Stanley taking write-offs of $2.6bn, $24.7bn, and $9.4bn respectively, while Goldman Sachs, and to a lesser extent Lehman Brothers managed to mitigate these loss-driving write-downs and post good returns.

- Significant third and fourth quarter write-downs have resulted in some rating agency actions, but significant across the board ratings downgrades are not expected as the banks' strong franchises and financial resources, as well as their ability to attract additional capital will allow them to withstand a significant period of stress.

- Disclosure of subprime and CDO exposure and other problem asset areas varies by firm making a direct comparison difficult. For example, some firms provide gross balance sheet exposures, while others provide "net exposure" information. The appended table has been compiled by Bernstein Analysis from information in conference calls and 10-K's.

- On a percentage of tangible equity LEH had the largest exposure to MBS/CDO's at 496%, followed by MER at 271%. We also note that LEH has the largest aggregate residential and commercial mortgage inventory. MER had the largest illiquid risk asset exposure inclusive of off-balance sheet committed lending facilities, both in absolute and relative terms to tangible common equity (source: Moody's Investor Service Q1'08).

Brokers' Exposures to Troubled Asset Classes
USD Billions

	BSC	GS	LEH	MER	MS
Total MBS/ABS/CDO Inventory	46.0	54.1	91.0	82.0*	56.7
MBS/ABS/CDO Inventory (ex SFAS 140)		46.6	79.0		
Commercial Mortgages - Gross	15.0	19.0	39.5		31.5
Commercial Mortgages - Net				18.0	17.5
Residential Mortgages	31.0		39.5	64.8*	25.2
o/w Subprime Mortgages	1.8	2.1	5.3	6.6*	8.8
CDOs - Gross		0.3	1.0	30.4	
CDOs - Net	0.8			4.8	3.6
Retained Interests	8.0	4.6	11.1	10.1	5.3

Exposure as a % of Tangible Equity
As a % of Tangible Equity

	BSC	GS	LEH	MER	MS	Avg
Total MBS/ABS/CDO Inventory	424%	143%	496%	271%*	208%	309%
MBS/ABS/CDO Inventory (ex-SFAS 140)		123%	430%			
Commercial Mortgages - Gross	138%	50%	215%		116%	130%
Commercial Mortgages - Net				59%	64%	
Residential Mortgages	286%		215%	214%	93%	202%
Subprime Mortgages	16%	6%	29%	22%*	32%	21%
CDOs - Gross		1%	5%	100%		36%
CDOs - Net	7%			16%	13%	12%
Retained Interests	74%	12%	61%	33%	19%	40%

*Net Exposures

Sources: Corporate Rrports, Bernstein Analysis

- The rise in mortgage assets across the firms, and by inference Level 3 assets, is closely correlated with the firms' leading standing as underwriters of mortgage and asset-backed securities. The "originate to distribute" business model adopted by all the firms, and more broadly the global banking sector to one extent or another, relied on securitization and structured products to move the assets off the firms' balance sheet. Securitization, particularly of mortgage-related assets, has effectively shut down. In addition to securitization, this business model included mortgage origination, secondary market purchases, mortgage servicing, warehouse financing, and securitization. Once the securitization exit was shut off, less liquid assets started to pile up on the firms' balance sheet due to pipeline commitments and before they could completely throttle the origination end.

2.8. Financial Analysis

Financial Summary:

- Satisfactory performance results versus some of the peers in a very challenging market and credit environment, particularly weak fixed income market in the U.S.
- Leverage finance, mortgages and structured products remained weak, but other businesses - investment banking, secondary equities, M&A advisory, investment management continued positive momentum.
- Lehman's hedge program provided a meaningful offset to the sharp downward asset valuation adjustments.
- Sound and enhanced liquidity position and lower level of leveraged loan commitments.
- Leverage levels have started to trend downward, with firm shifting to risk reducing or deleveraging mode.
- Opportunistically increased its equity base, though no immediate need to do so, but with view to future.
- Strong risk management culture and systems.
- Increasingly diverse product offering and geographic platform. Continuation of development outside of the U.S., particularly in Asia-Pacific.
- While in a growth mode in certain emerging markets, the firm, like its peers, is in an overall cost rationalization mode, to help mitigate the impact of lower revenues.
- Asset quality is concentrated in real estate, which exposes firm to ongoing valuation adjustments & earnings volatility.

(US$ millions)	Feb-08	Nov-07	Nov-06	Nov-05	Nov-04	Nov-03
Total revenue	12,370	59,003	46,709	32,420	21,250	17,287
Net revenues	3,500	19,257	17,583	14,630	11,576	8,647
Net income	489	4,192	4,007	3,260	2,369	1,699
Pre-tax margin	18.9%	31.2%	33.6%	33.0%	30.4%	29.3%
Compensation / net revenue	52.5%	49.3%	49.3%	49.3%	49.5%	49.9%
ROAE	8.6%	20.8%	23.4%	21.6%	17.9%	18.2%
Total assets	786,035	691,063	503,545	410,000	357,168	312,061
Collateralized finanacing transaction	368,681	301,234	225,156			
Net assets	393,221	369,800	266,311	211,340	175,221	163,182
Equity capital	24,832	22,490	21,929	18,794	14,920	14,484
Total capital	153,117	128,839	87,491	79,466	71,406	58,013
Gross leverage (x)	31.7	30.7	23.0	21.8	23.9	21.5
Total assets / Total capital (x)	5.1	5.4	5.8	5.2	5.0	5.4
Net assets / Equity capital (x)	15.8	16.4	12.1	11.2	11.7	11.3

Profitability
Q1'08

- LEH reported $489m in net income with net valuation write-downs of $1.8bn in residential and commercial mortgages and leveraged loans. Despite the write-downs, LEH posted strong performance in Rates, FX, investment management, and high grade corporate debt underwriting. Performance is consistent with industry trends.

- We believe Lehman would continue to face some earnings pressures throughout 2008 from expected declines in investment banking revenues and further potential write-downs of commercial and residential mortgages, and leveraged loans and commitments. **Nevertheless, we expect the company to be profitable during 2008**. Risk appetite is expected to remain conservative and mindful of funding pressures.

FYE November 2007

- **Record performance in 2007**. Pre-tax income was up 2% y-o-y to $6bn, driven by record results in all three business segments – Capital Markets, Investment Banking, and Investment Management.
  - **Capital Markets**.
    - Equities reported net revenues of $6.3bn in 2007, a 76% increase from $3.6bn in the prior year driven by strong customer flows, private equity investment, and the firm's investment in GLG Partners (a hedge fund that went public in November) generating an estimated $500m gain
    - Results from equity capital markets were partially offset by weakness in fixed income performance reflecting challenging credit environment and $1.5bn write-downs in subprime-related securities and leverage loan commitments.
  - **Investment Banking**
    - Record net revenues of $3.9bn, driven by robust debt & equity underwriting and advisory activities booked largely in the first half of 2007.
  - **Investment Management.**
    - Net revenues were a record $3.1bn, up 28% from 2006, reflecting strong net fund inflows outside U.S. which underscored its geographic diversification.
    - AUM grew to $282bn, up 25% from the prior fiscal year due to a combination of both net inflows and asset appreciation.

- Regionally, Lehman generated 50% of revenues outside the U.S (roughly in line with peers). Geographic diversification helped mitigate the dislocations in the U.S. and European fixed income businesses.

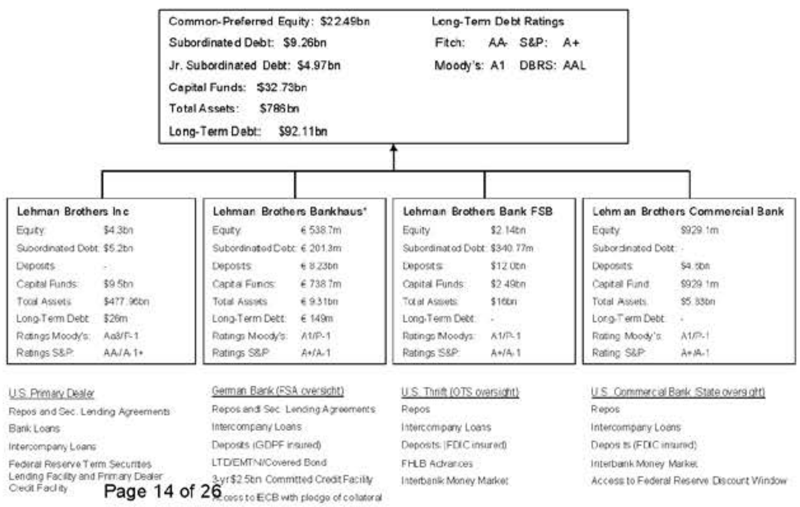
Liquidity

- Lehman uses their 3 regulated banking entities to provide funding for certain mortgage and corporate loan assets.
- Liquidity pool at Holdco was $34bn at the end of 1Q08 and $36bn at COB yesterday (5/9/08).
- Bank has over $7bn of excess liquidity to fund qualifying assets with an additional $8bn of capacity, some of which comes through the Home Loan bank.
- Has not lost any material repo funding capability.
- $115bn of tri-party secured financing (total repo – (treasuries + agencies).
- Capital funding is over 90% of desired 2008 level through mid-April, 2008.
- LEH has minimal reliance on CP, short-term unsecured financing or asset-backed commercial paper programs.
- Net leverage down to 15.4x from 16.1x at year end (prior to new capital raise of $4bn).

Debt/Funding Profile

- During 1Q08 and FY2007, Lehman issued $18.2bn and $86.3bn of long-term borrowings, respectively.
- Long-term borrowings increased to $128.4 @ 1Q08, up from $123.2bn, respectively, principally to support the growth of assets as well as to pre-fund a portion of current 2008 maturities.
- As of FYE07, 54% of long-term debt outstanding was issued outside the United States which helps reduce refinancing risk.
- To further reduce refinancing risk, Lehman sets limits for the amount of long-term borrowings maturing over any three, six and twelve month horizon at 12.5%, 17.5% and 30% of outstanding long-term borrowings, respectively — that is, $15.4 billion, $21.6 billion and $37.0 billion, respectively, at FYE07. If Lehman were to operate with debt above these levels, it would not include the additional amount as a source of cash capital.
- Lehman Brothers Holdings' $2.0bn unsecured, committed revolving credit agreement matures in March, 2011. In

Lehman Brothers Holdings Inc Funding Sources



*Financial figures as of 11/06

April 2010, Lehman Brothers Bankhaus AG's and Lehman Brothers Treasury Co. B.V.'s $2.5 billion multi-currency unsecured, committed expires. Both facilities are actively used for general operating purposes, although there were no borrowings under either at FYE07. Both facilities do not contain any MAC clauses.

- Lehman owns three bank entities: Lehman Brothers Bank, (a U.S.-based thrift institution), Lehman Brothers Commercial Bank, (a U.S.-based industrial bank), and Lehman Brothers Bankhaus, (a German bank). These regulated bank entities operate in a deposit-protected environment and are able to source low-cost unsecured funds that are primarily core deposits. These are generally insulated from a company-specific or market liquidity event, thereby providing a more reliable funding source for mortgage products and selected loan assets as well as enhancing funding diversification. In aggregate, these bank subsidiaries had $28.8bn in deposits outstanding @ 1Q08 (vs. $29.4bn @ FYE07).

- As of 1Q08, the company disclosed $37.2bn of debt liabilities measured at fair value including $600m of gains during quarter under FAS 157/159, up slightly from $36.2bn outstanding at FYE07. Such debt liabilities comprise largely its equity-linked retail structured note issuance targeting wealthy Asian and European investors. Such retail issuances remain healthy and have allowed the company to meet its funding plan.

Asset Quality

- Total assets based increased by 56% between FYE06 and 1Q208 primarily as a result of growth in collateralized financing transactions and net assets. Net assets increased 48% from $266bn FYE06 to $393bn @ 1Q08, due to increases across most inventory classes, as well as increase in customer secured receivables. Included in net assets are real estate held for sale, certain high yield instruments (inclusive funded loans), private equity & other principal investments, all which experienced strong growth during the period.

- Secured receivables consist of reverse repos, secured primarily by U.S. Government and Agency securities, customer margin loans and securities borrowed, which are typically secured by marketable corporate debt and equity securities. Margin debt is fully collateralized by securities that are marked-to-market daily, with advance rates established in compliance with various regulatory and internal guidelines. Securities borrowed transactions are also considered lower risk, but the underlying securities are generally equities that are in turn lent to short sellers and arbitrageurs who are part of Lehman's prime brokerage client base. These assets are generally of short-term duration (less than 30 days), turn over very quickly and require nominal capital support due to overcollateralization.

- We deduct assets related to collateralized financing transactions such as reverse repos and securities borrowed, where government, mortgage-backed, corporate and equity securities are bought, borrowed, sold and lent in generally offsetting amounts to generate net interest and facilitate trading, from total assets to arrive at "net assets". These represented about 47% of Lehman's total assets @ 1Q08, up slightly from 44% @ FYE07.

- At 1Q08, residential ($32bn) and commercial ($59bn) mortgages, ABS inventory & real estate held-for-sale totalled $107bn, down slightly from $111bn @ FYE07. Of this total, $23bn (vs. $25bn) was sold to or financed by third parties on a non-recourse basis. Lehman does not consider itself to be at economic risk from these assets (FAS 140 gross up).

- The components of the residential mortgage portfolio are:

	1Q08	**FYE07**
Subprime Whole Loans	$1.3	$1.7
Subprime Retained Interests in Securitizations	$2.7	$3.6
Prime & Alt-A	$14.6	$12.7
European Mortgages	$9.5	$10.2
Total	**$28.1**	**$28.2**

This exposure is significant and represents a higher than optimal asset concentration in real estate, which will pose a significant burden on the firm not just from a profitability perspective but also liquidity or funding perspective.

- On the commercial side, $25bn represented whole loans, with about 90% of the loans floating rate with an average term of 2-3 yrs. The CMBS component is largely AAA-rated and regionally diversified, about half of the portfolio in the U.S. and the other half in Europe and Asia.

- In addition, the firm had less than $1bn of ABS CDOs on the balance sheet @ 1Q08, and after consideration of hedges, Lehman remained modestly net short in the ABS CDOs asset class.

- LEH securitized $10bn of assets in 1Q08, down from $26.4bn the comparable period a year ago.

Leverage / Double Leverage

- Adjusted leverage (calculated as net assets/equity capital) fell slightly to 15.8X @ 1Q08 from 16.4x at FYE07. Similar to other firms, this ratio ended FYE07 on the high side of the historical range due to illiquid market conditions combined with customer market-making, which resulted in a sharp growth of assets. However, leverage (gross or net) is expected to continue to trend down to a more "normalized" level taking into account the more constrained liquidity environment.

- Historically, broker-dealer organizations have been allowed to operate with higher balance sheet leverage ratios than other financial intermediaries because: 1) A significant portion of their assets and liabilities reflected "matched book" or collateralized financing activity, which were viewed as more resilient or immune to severe liquidity disruptions experienced by the unsecured capital markets, from time to time, and 2) The overwhelming majority of their assets including inventory, collateral backing collateralized financing transactions and loans, were carried at liquidating or "market" values and, therefore, capital accounts did not ordinarily need to be discounted to cushion unrecorded erosion from historic cost values (like a bank). The dislocation experienced in the marketplace over the past year has overturned these two fundamental underpinnings that supported higher industry leverage, thus we expect the industry to operate under more conservative leverage metrics going forward.

- Lehman aims to maintain a primary equity double leverage ratio (the ratio of equity investments in LBHI's subsidiaries to its total equity capital) of 1.0x or below. Lehman's primary equity double leverage ratio was 0.91x and 0.88x as of November 30, 2007 and 2006, respectively.
- Certain regulated subsidiaries are funded with subordinated debt issuances and/or subordinated loans from LBHI, which are counted as regulatory capital. LEH's policy is to fund subordinated debt advances by LBHI to subsidiaries for use as regulatory capital with long-term debt issued by LBHI having a maturity at least one year greater than the maturity of the subordinated debt advance.

Broker Regulatory Capital

- Excess net capital was ~ $7bn. The potential down streaming of the RCF to support regulatory requirements would increase double leverage and in the event the broker was deemed not sufficiently capitalized the regulators could step in and not permit the upstreaming of funds to the Holding Company to meet its debt service. We are comfortable with this risk due to the fact that regulated entities have historically been and are currently deemed well capitalized. In addition, early warning Tangible Net Worth covenants are in place.

2.9. Broker's & Rating Agency View / Comment on KMV / Equity Data

- LEH is followed by 20 equity analysts of which 10 have a 'buy' recommendation and 9 have a 'hold'.
- The consensus view is favorable due to LEH's broadening (product and geography) business franchise.
- As noted above, Moody's and Fitch's outlook for LEH is 'Stable'; S&P's is 'Negative.'

2.10. Support Policy, Documentation & Security

- Currently have in place unconditional guarantee from LEH for the following entities (noted below).
- See attached Appendix for Parental Support Framework for each Legal Entity. Implied support or contractual guarantees through ISDA or other agreements exist for the remaining subsidiaries.
- In our view LEH is willing and intends to support its subsidiaries (both implicitly and explicitly) in order to preserve its franchise and reputation.
- Its subsidiaries are wholly-owned and or indirectly and/or directly controlled by the parent.
- In its long history LEH has never walked away from any of its subsidiaries or allowed any to fail.

Security

CAT A

- 15% of total CAT A exposure is against unregulated subsidiaries (including $50million committed 3 yr RCF to Holdco).
- 85% of total CAT A exposure (majority S/T money market) is against the main broker/dealer subsidiaries, which are considered the most credit worthy obligors in the enterprise for the following reasons:
  - incorporated in G7 jurisdictions with strong regulatory framework including oversight and enforcement powers;
  - subject to risk-based minimum capital requirements, thus maintain adequate stand-alone financial resources; and
  - have access to central bank liquidity facilities for alternate funding (previously unavailable to this industry sector).

CAT B

- The overwhelming majority of CAT B long-dated derivative exposure is covered by Collateral Support Annex ("CSA") with daily MTM and margin calls.
- The remaining CAT B exposure is largely against regulated broker/dealer subsidiaries. We further take comfort from the following considerations:
  - Exposures are largely short-dated (< 1 yr) and represent contingent market risk relating to securities transactions (buys and sells) settling DVP.
  - Include collateralized financing transactions which are documented pursuant to industry standard agreements (MSLA, GMRA and ISDA).

In addition, Lehman unconditionally guarantees all its subsidiaries in ordinary course, except for its US broker/dealer subsidiary.

HBUS					
Lehman Brothers Inc	No	YES	YES	5,000,000	500,000
Lehman Brothers Financial Products	No	YES	YES	2,000,000	250,000
Lehman Commercial Paper Inc	Explicit SLBH	NO			
Lehman Brothers Finance SA	Explicit SLBH	YES	YES	25,000,000	500,000
Lehman Brothers Special Financing Inc	Explicit SLBH	YES	YES	10,000,000	500,000
Lehman Brothers Holdings Inc		NO			
Lehman Brothers Commercial Corp	Explicit SLBH	YES	YES	5,000,000	500,000
Lehman Brothers International (Europe) Ltd	Explicit SLBH	YES	YES	1,000,000	500,000
HBEU					
Lehman Brothers Commercial Corp	Explicit SLBH	YES	YES	5,000,000	500,000
Lehman Brothers Inc	No	YES	YES	5,000,000	500,000
Lehman Brothers Special Financing Inc	Explicit SLBH	YES	YES	5,000,000	500,000
HSBC France					
Lehman Brothers Commercial Corp	Explicit SLBH	YES	YES	0	1,000,000
Lehman Brothers Finance SA (CCF FP)	No	YES	YES	0	Euro 500,000
Lehman Brothers Special Financing Inc	Explicit SLBH	YES	YES	0	1,000,000
HBAP					
Lehman Brothers Asia Holding Limited		IFEMA	NO	Awaiting confirmation from Asia	
Lehman Brothers Inc		YES	NO		
Lehman Brothers Special Financing Inc	No	YES	YES		
Lehman Brothers International (Europe)	Explicit SLBH	YES	pending		

Section 3 - Policy

3.1 Statement of Facility Data Accuracy

GRM to the best of his ability confirms that the information is accurate based on our current system capabilities.

3.2 Conditions of previous approval

N/A

3.3 Reputation Risk

Lehman seeks to maintain its reputation by screening potential clients and by conducting its business activities in accordance with high ethical standards and all applicable laws in each of its operating environments. Lehman has robust internal policies and procedures which enable all employees from the front office to support/control areas to adhere to high standards which mitigate any possible legal proceedings. Lehman enjoys a high degree of respect amongst its competitors, clients and regulators. However, as a large underwriter and distributor of ABS and structured credit products, we can expect an escalation of arbitration claims and outright litigation by aggrieved investors against the Street as a whole for poor due diligence &/or unsuitability, which is likely to be a further drag on profitability.

3.4 Compliance Issues

Lehman Brothers has a global KYC on file and attests that its managers and business subsidiaries adhere to KYC standards and policies on a global basis.

3.5 HSBC Group Audit Findings

Unqualified opinion.

3.6 Environmental / Social Risk - Sustainability

N/A

3.7 Regulatory Risk

The securities and financial services industries are subject to extensive regulation under both federal and state laws in the U.S. and under the laws of the many other jurisdictions. It is regulated by a number of self-regulatory organizations such as the National

Association of Securities Dealers, the Municipal Securities Rulemaking Board and the National Futures Association, and by national securities and commodities exchanges, including the New York Stock Exchange.

All regulatory risk will be well publicized and have wide-spread ramifications across the entire sector.

Although the final outcome is far from determined, all market participants (regulators, investors, dealers) anticipate a much higher degree of regulatory oversight and likely revisions to the capital and liquidity framework. The industry has a proven record of being able to adjust to all market cycles and regulatory and political environments.

Section 4 - Summary & Recommendations

4.1 Global Relationship Manager

Approval recommended on business and credit merits.

4.2 Team Head

4.3 Global Sector Head

4.4 Client Relationship Manager

4.5 Credit Risk Management

4.6 Global Corporate Banking

GHQ CRF

APPENDIX A: EXPOSURE SUMMARY

Lehman Brothers Holdings Inc - Global exposure (as of 5/5/08)					
Counterparty	CBID	CAT A	CAT B	TSL/PSL	Total
USD (000s)					
Capital Growth Investments Ltd	CGIL	5,000		20,000	25,000
Lehman Brothers Inc	EFHC	325,128	708,547	2,563,200	3,596,875
Lehman Brothers Asia Holdings	LBAH		100		100
Lehman Brothers Asia Ltd	LBAI		135,000	550,000	685,000
Lehman Brothers Futures	LBFA	114,196			114,196
Lehman Brothers Fixed Income Securities	LBFC		52,000	6,000	58,000
Lehman Brothers Finance Asia plc	LBFQ		1,500	10,000	11,500
LB India Holdings Mauritius II Ltd	LBIU		45,000		45,000
Lehman Brothers Japan Inc	LBJI		6,000	25,000	31,000
Lehman Brothers Serv	LBSI	20,000			20,000
Lehman Brothers Securities	LBSP	35,000		50,000	85,000
Lehman Commercial Paper Inc	LCPI	92,421	200		92,621
Lehman Brothers Bankhaus	LEBB	50,000			50,000
Lehman Brothers Finance SA	LMFI		270,200		270,200
Lehman Brothers Special Financing	SLBF		598,900	190,000	788,900
Lehman Brothers Holdings	SLBH	74,248	30,000	874,340	978,588
Lehman Brothers Commercial Corp	SLCC		52,500	225,000	277,500
Lehman Brothers Holdings Group	SLHP	152,942		200,000	352,942
Lehman Brothers International	SLIL	11,539	621,250	3,897,636	4,530,425
South Pacific Mortgage	SPMY			22,540	22,540
Lehman Brothers Bank FSB	LBBK	14,000			14,000
Lehman Financial Products	LBFP		40,000		40,000
Total exposure		894,474	2,561,197	8,633,716	12,089,387

HBUS limits as of 5/5/08			Traded Products		
COUNTERPARTY (all limits in $ thousands)	CBID	CAT A	CAT B Limit	Description	SETTLEMENT LIMIT
Lehman Brothers Holdings Inc.	SLBH	[illegible]			
Lehman Brothers Finance SA	LMFI		75,000	XPR (CSA)	
Lehman Brothers Commercial Corp.	SLCC		50,000	XPR (CSA)	200,000
Lehman Brothers Inc.**	EFHC	300,000	61,000 85,000	BOND, FMC, REPO XPR (CSA)	1,000,000 300,000
Lehman Brothers Special Financing Inc.	SLBF		425,000 7,000	XPR (CSA) Swaps	150,000
Lehman Brothers International (Europe)	SLIL		15,000 18,750	XPR (CSA) REPO, OPT, BON	5,000
Lehman Commercial Paper Inc.	LCPI	82,215			
Lehman Brothers Bank FSB	LBBK	14,000			
Lehman Brothers Financial Products Inc.	LBFP		40,000	XPR (CSA)	
TOTAL HBUS		446,215	776,750		1,655,000
HSI limits as of 5/5/08			Traded Products		
Lehman Brothers Inc.	EFHC		50,000 500	BOND, REPO, FUS FFI	5,000
TOTAL HSI			50,500		5,000

Committed Cat A:	50,000	690,000	CSA-backed Cat B
GTR:	96,215	89%	percentage of total Cat B (HBUS)

**NOTE:

1) CAT A at HBUS includes $300m Money Market Facility, with the following sublimits:
$300m SBLC sublimit to six months for use by Lehman Brothers Inc.
$100m Money Market sublimit to one month for use by Lehman Brothers Holdings Inc.
$200m Money Market sublimit to one month for use by Lehman Commercial Paper Inc.
$200m SBLC sublimit to six months for use by Lehman Brothers International Europe Inc.
2) Settlement includes $1bn day loan limit

APPENDIX B: GCRC RATIONALE

PROPOSED GCRC FOR 2008 LEH GAR

	HSBC Entity	Limit/Product Type	Counterparty Name	Increases / (Decreases)	Comment / Rationale
Committed CAT A					
	INBOM	Loan	Lehman Brothers Capital Private Limited	100,000	Ongoing discussions with GRM, RRM, Global FIG to set-up this line. Limit required to support the client's newly launched NBFC Business in India.
	Total			**100,000**	
Uncommitted CAT A					
	INBOM	Loan/OD/GTEE	Lehman Brothers Securities Private Limited	25,000	Increase of Loan/ OD/ GTE lines to support the client's expanding Broking Operations in india
	Total			**25,000**	
CAT B					
	HBEU	**REGULARIZE CAT**	**LBIE**	**300,000**	**To regularize existing CAT B excesses at HBEU.**
	HBEU	Stock L/B	LBIE	150,000	To support new / incremental growth plan of Stock L/B activities in US, Europe, and Asia (Korea, Taiwan, and possibly India). Warren McCormick is now based in the US and is keen to drive the business expansion (note, trades are booked at HBEU). HSBC is now in Lehmans top tier relationships from nowhere a year ago.
	HASE	FEX	Lehman Brothers Inc	1,000	Support increased trading requirements at 3m tenor
	HBAP SEL	FEX	Lehman Brothers Int'l (Europe)	50,000	Following heavy increase in trading volume with LB in Korea and request fron Head Regional FX trading
	HBAP VNM	FEX	Lehman Brothers Inc	1,500	To support a new FX relationship in Vietnam.
	HBME, UAE (AEHBME)	FEX	Lehman Brothers Inc	5,000	Increase in business expected. Lehman has just asked for new cash accounts to be opened in Qatar, Jordan and Bahrain, together with Custody Accounts
	HKH	XPR	Lehman Brothers (shared limit)	50,000	Accommodate new FFR weightings and allow for continued trading
	HKH	Eq. Deriv	Lehman Brothers (shared limit)	40,000	Cover excess and allow continued trading on equity derivatives
	HKH	Stock L/B	Lehman Brothers (shared limit)	5,000	Accommodate growing SBL volume (currently at limit)
	HSBC BKH	FEX	Lehman Brothers Special Finance	76,000	Lehman Brothers Commercial Corporation has lent THB loan to property developers and other companies related to property business in Thailand by subscriobing the bonds issued by those companies. LBFINYK will be the FX booking entity for other Lehman Brothers's ubsidiaries . This is why the request limits are under LBFINYK rather than Lehman Brothers Commercial Corporation. Due to Bank of Thailand's regulation, non resident has to book FX on shore with its custodian bank, which is HSBC BKH in this case. This is the reason why FX activities with Lehman Brothers has significantly increased. We expect to receive the revenue of 5 bps per each USD booked with BKH.
	HSBC BKH	FI	Lehman Brothers Finance Asia Pte Ltd	7,200	Lehman Brothers Finance Asia would like to invest in government bonds in Thailand with expected transaction size of USD 100 million. The client has awarded BKH HSS to be its local custodian. The tenor of government bonds that the client would like to trade may be range from 1 year to 15 years. The proposed limits will accommodate the client's intention to trade government bonds and book FX with BKH TCM. In addition, this is to support the client's business to flow smoothly as we has been awarded to be the clients' custodian bank.
	HSBC BKH	FEX	Lehman Brothers Finance Asia Pte Ltd	12,000	Lehman Brothers Finance Asia would like to invest in government bonds in Thailand with expected transaction size of USD 100 million. The client has awarded BKH HSS to be its local custodian. The proposed limits will accommodate the client's intention to trade government bonds and book FX with BKH TCM. In addition, this is to support the client's business to flow smoothly as we has been awarded to be the clients' custodian bank.
	INHBAP	FEX	Lehman Brothers Asia Limited	75,000	Client has indicated that they are looking to deal in 3 year currency options which would require higher limits as risk-weightages for 3 year tenors are higher. Also, the Assets under Custody for this client are expected to rise around 50% during 2008. Client is expected to hedge 35-40 % of its portfolio at any given time. ISDA executed- CSA Not Applicable. Supported by Guarantee from Lehman Brothers Holdings Inc.
	INHBAP	FEX	LB India Holdings Mauritius II Limited	10,000	Limit increase required for supporting the hedge of client's FDI hedge. ISDA executed- CSA Not Applicable. Supported by Guarantee from Lehman Brothers Holdings Inc.
	INHBAP	XPR	Lehman Brothers Capital Private Limited	50,000	IRS /CSW lines will be required in case the entity wishes to have HSBC India as counterparty for swaps
	Global	**FLOW Trading**	**Lehman Brothers Group**	**75,000**	**10% cushion to accommodate and provide flexibility to flow trading.**
	Total			**907,700**	**$300m to cover existing excesses at HBEU**
Settlement					
	HBAP SEL	TSL	Lehman Brothers Int'l (Europe)	50,000	To support FX CAT B increase proposal as noted above.
	HBAP VNM	TSL	Lehman Brothers Inc	10,000	To support new FX trading activity
	HBME, UAE (AEHBME)	TSL	Lehman Brothers Inc	25,000	Increase in business expected. Lehman has just asked for new cash accounts to be opened in Qatar, Jordan and Bahrain, together with Custody Accounts
	HBUS	TSL	Lehman Brothers Sepcial	150,000	To accommodate current excesses. Current line of $190m vs settlement peak of $270m.
	HSBC BKH	TSL	Lehman Brothers Special	80,000	To support FX trading as noted above.
	HSBC BKH	TSL	Lehman Brothers Finance Asia Pte Ltd	100,000	To support FX trading as noted above.
	HSBC MAR	PSL	Capital Growth Investment	50,000	Increase in PSL is being requested based on utilisation of limits
	INBOM	PSL	Lehman Brothers Securities Private Limited	50,000	Increased settlement limits expected as client's business will expand in 2008. 2007 was the first year of operations for the broking entity.
	INBOM	PSL	Lehman Brothers Capital Private Limited	75,000	Recently launched NBFC Business. LB Capital has already been utilising USD 15-20M of PSL limits. Such requirements are currently being met out of re-allocations from LBAI. With increase in business activities in 2008, we expect settlement limits to be increasingly required
	INHBAP	PSL	Lehman Brothers Asia Limited	200,000	Large volume of inward and outward flows have necessitated borrowing of DSL limits from other HSBC Group offices. USD 300M increase seen as necessary to support stock exchange trades during 2008. LBAI custodises with INM HSS and thus support in the form of limits is crucial
	INHBAP	TSL	Lehman Brothers Fixed Income Securities Private Limited	4,000	Increase in TSL required for larger trade settlements expected during 2008 on account of increased business levels.
	Global	**FLOW Trading**	**Lehman Brothers Group**	**80,000**	**10% cushion to accommodate and provide flexibility to flow trading.**
	Total			**874,000**	
			Total	1,906,700	

- The above noted figures reflect input and recommendation from CSTs / RRMs in AM, EUR, ME, and AP

- Key drivers of the need to increase limits are:

1) Higher volatility in the market
2) Weakening USD since the majority of our limits are centralized in USD.
3) Business growth in capital markets activities which is largely driven by of higher level of B/D's client assets.
4) We also factor in approximately 10% of general headroom to CAT B and Settlement primarily support flow trading volume which has also increased in general.

Major Group Subsidiaries and Security Details:

1. Financial information as of 30NOV07, unless otherwise indicated.
2. Financial analysis is deferred to the granting HSBC unit where a guarantee does not exist, pursuant to a local review. The necessity of a guarantee from the holding company for a facility extended to a regulated subsidiary is considered a subjective consideration by the granting unit, taking into account such factors as the size and risk profile of the facility extended. The holding company generally issues a guarantee in support of unregulated subsidiaries, upon request by creditors and/or counterparties.
3. The holding company manages its operating subsidiaries on a coordinated global basis, with a view to the profitability, regulatory capital, legal and tax efficiency of the enterprise as a whole. Intercompany advances between the holding company and subsidiaries are material. On this basis, along with other subjective considerations, support of operating units is implied without regard to the existence of formal guarantees from the holding company.
4. The holding company, acts primarily as a central bank or the downstream financing arm of the consolidated organization. In this capacity, it serves as a clearinghouse for internally and externally generated funds. The holding company is the primary unsecured debt and equity issuer in the capital markets. Such long-term debt and equity are used to fund investments in, and advances to, subsidiaries including subordinated debt advances, which may qualify as regulatory capital for certain regulated subsidiaries. Short-term unsecured debt raised at the holding company, primarily commercial paper and medium-term notes, is also down-streamed to subsidiaries in the form of senior short-term advances, which are typically structured to mature before the parent company's own debt obligation. These intercompany advances are viewed as highly liquid since: 1) minimal risk of regulatory interference as the holding company has a senior claim on its broker-dealer subsidiary that ranks pari passu with other 3rd party senior claims, and; 2) such advances are typically funding marketable securities holdings at the subsidiary level, which can readily be sold, repoed or re-hypothecated, with the cash then up-streamed to repay maturing debt at the holding company. Such an asset-liability funding and liquidity profile is consistent with general industry practice.
5. As per the new parental support framework, G-7 regulated entities are rated one notch above the holding company, guaranteed special purpose OTC trading subsidiaries and other non G-7 regulated subsidiaries the same as the parent, and all others P-1 unless overridden based on strong implicit/explicit parent support considerations. Subsidiary CRRs are listed in the right hand column based on new PSF.

COMPANY	DESCRIPTION	@ 11/30/07, consolidated, unless noted ($ millions)
Lehman Brothers Holdings Inc. Delaware, USA (SLBH)	SLBH, incorporated in 1983, is the ultimate parent company of the organization. SLBH is publicly traded and listed on the NYSE ("LEH"). It was founded 150 years ago and became a public company with its spin-off from American Express in 1994. SLBH's operations are segregated into three business segments: Investment Banking, Capital Markets and Asset Management.	Total Assets: $691,063 Subordinated Debt:$9,259 Preferred Trust: $4,977 Shareholders' Equity: $22,490 Capital Funds: $36,726 CRR 3.3
Lehman Brothers Inc. Delaware (EFHC)	EFHC is the principal operating subsidiary of SLBH. EFHC is an SEC-registered broker-dealer and primary dealer in U.S. government securities, and a member of all principal securities and commodities exchanges in the U.S. as well as the NASD. As a primary dealer, EFHC buys, sells and finances government securities directly with the Federal Reserve Bank of New York as part of the Bank's open market activities. EFHC trades foreign exchange on a global basis. Unlike most other broker-dealers, EFHC issues commercial paper and subordinated debt directly to third parties.	Total Assets: $495,426 Subordinated Debt: $5,228 Shareholders' Equity: $4,446 Capital Funds: $9,674 Net Capital: $2,700 Excess Net Capital: $2,100 Regulated subsidiary: CRR 3.2
Lehman Brothers Bank FSB USA (LBBK)	LBBK is a federally chartered savings bank, whose deposits are insured by the FDIC. It primarily originates and purchases residential mortgage loans and funds itself through bank deposits and FHLB advances. LBB can also fund commercial mortgages and investment grade US loans. Can access the Fed discount window.	
Lehman Brothers Commercial Bank Delaware	LBCC is a state chartered industrial bank, whose deposits are insured by the FDIV. It primarily originates commercial and industrial loans, commercial real estate loans, warehouse loans, and interest rate products and funds itself through bank deposits. Can access the Fed discount window.	
Lehman Commercial Paper Inc.. New York (LCPI)	LCPI is a wholly-owned subsidiary of LBI and engages in the trading and distribution of commercial paper and other exempt money market instruments, including banker's acceptances (BAs) and certificates of deposit (CDs). LCPI's wholly owned subsidiaries principally hold residential and commercial mortgages and mortgage-backed securities and investments in real estate partnerships. LCPI also originates and invests in loans to investment grade and non-investment grade companies. As part of these activities, LCPI provides warehouse loans secured by mortgage loans and other assets. LCPI acts as a dealer for about 700 U.S. and foreign commercial paper issuers, and makes markets in BAs and CDs for over 100 of the world's largest banks.	(@ 11/30/06) Total Assets: 38,949 Shareholders Equity: $399 Unregulated subsidiary guaranteed by SLBH, upon request: CRR 3.3
Lehman Brothers Commercial Corporation Delaware	LBCA is a wholly-owned subsidiary of SLBH. LBCC activities include OTC foreign exchange and options trading.	Unregulated limited purpose OTC trading subsidiary, but guaranteed by SLBH pursuant to master ISDA agreements:

(LBCA)	CRR 3.3

Lehman Brothers International (Europe) U.K. (SLIL)	SLIL, incorporated in the U.K. in 1990, houses Lehman Brothers' international investment banking activity, proprietary government bond trading, eurobond trading, short and medium term money market activities and international stock lending operations. SLIL acts as a broker and principal trader in U.K. and foreign equities including securities in emerging markets and equity derivative products, and as a broker in options and Gilts. It is also a market maker in various major U.K. and foreign equities. SLIL is a member of the LSE and various continental European exchanges and is regulated by the FSA as a broker-dealer. SLIL is a wholly-owned subsidiary of **Lehman Brothers Holdings plc (SLHP)**, which is an intermediate UK-based holding company serving as a financing company or money desk for the U.K. operations. LBIE benefits from a full guarantee from LBHI on master ISDA agreements & bi-lateral extension s of credit, upon request. LBIE is viewed as major self-financing regulated operating subsidiary, which is considered acceptable stand-alone credit for customary treasury & banking transactions.	Total Assets: $451,954 Subordinated Debt: - Preference shares: $7,100 Shareholders' Equity: $6,015 Capital Funds: $13,115 LBIE (regulated subsidiary): CRR 3.2 SLHP (unregulated): CRR 4.1
Lehman Brothers Bankhaus AG Germany (LEBB)	LEBB is a fully-licensed German bank founded 1987, which is engaged in traditional bank lending and financing activities as well as investment banking activities (M&A and corporate finance). It is a licensed commercial bank incorporated under the German Stock Corporation Act and regulated by the German Federal Regulator. As a member of the Association of German Banks it participates in the German Depositors Protection Fund which insures deposits from non-bank customers. The bank finances itself primarily using unsecured and secured money market facilities. LBBAG has a $2.5 billion 3-year committed, unsecured revolving credit facility provided by a syndicate of relationship banks. Can access the ECB discount window. The bank has a branch office in London. LEBB benefits from a full guarantee from LBHI on master ISDA agreements & bi-lateral extensions of credit, upon request. LEBB is viewed as a major self-financing and regulated operating subsidiary, which is considered an acceptable stand-alone credit for customary treasury and banking transactions.	Total Assets: Euro 16.2bn Subordinated Debt: Euro 331m Shareholders' Equity: Euro 821.6m Capital Funds: Euro 1,152.6m Regulated subsidiary: CRR 3.2
Banque Lehman Brothers SA France BLBR	BLBR is a fully licensed French bank and finance company. It is engaged in investment banking activities (mergers & acquisitions and corporate finance). BLBR has SVT (Specialiste en Valeurs du Tresor), or Senior Primary Government Bond dealer status, which was granted by the French Ministry of Finance, enabling it to be a reporting dealer in French government securities. BLBR is viewed as a self-financing and regulated operating subsidiary, which is considered an acceptable stand-alone credit for short-term treasury and banking transactions.	Regulated subsidiary: CRR 3.2
Lehman Brothers Japan Inc. (LBJI) Cayman Islands	LBJI is a wholly-owned subsidiary of SLBH. Its Tokyo branch, which opened in 1986, engages in a broad range of investment banking and capital markets activities, including syndications, and multi-currency fixed income and equity trading. LBJI is a licensed securities company in Japan and a member of the Tokyo and Osaka Stock Exchanges and the Tokyo Financial Futures Exchange and other major regional exchanges and, as such, is regulated by the MoF, JDSA and such exchanges. LBJI is also a primary dealer in Japan Government Securities (JGBs) trading directly with the Bank of Japan (BoJ).	LBJI is viewed as a major self-financing and regulated operating subsidiary, which is considered an acceptable credit for customary short-term treasury and banking transactions. Regulated subsidiary: CRR 3.2
Asia/Pacific Operations	The Asian subsidiaries outside of Japan are divided along product lines in order to achieve better product flexibility and market penetration. These operations, located in Hong Kong and Singapore, are grouped under <u>Lehman Brothers Asia Holdings Limited (LBAH)</u>, a subsidiary of LBI incorporated in Hong Kong. LBAH is fully guaranteed by SLBH. LBAH is a holding company for Lehman Brothers' regulated subsidiaries outside of Japan, operating primarily as a funding vehicle for the non-Japan Asian region. LBHA relies both on external and internal funding for this purpose. Principal subsidiaries of LBHA are: • <u>Lehman Brothers Securities Asia Limited (LBSH)</u>, incorporated in Hong Kong, is registered by the Hong Kong Securities and Futures Commission as a securities dealer, and deals in Hong	Financial statements, as available, are the responsibility of the local HSBC dealing center. However, we note that such subsidiaries are guaranteed by SLBH, upon request. The provision of such guarantee is generally dependent on the scope of business transacted. Regulated subsidiaries (CRR 3.2): LBSH, LBFA, LBAI, LBFC

	Kong equity agency trading and is a trading member of the Stock exchange of Hong Kong. LBSA is guaranteed by SLBH, upon request. • Lehman Brothers Futures Asia Limited (LBFA), incorporated in Hong Kong, is a clearing member of the Hong Kong Futures Exchange. • Lehman Brothers Asia Limited (LBAI), incorporated in Hong Kong, acts as an agent in U.S. securities, debt instruments, options and commodity futures transactions. LBAI is licensed by the Hong kong Securities and Futures Commission for various regulated activities namely dealing in securities and futures and advising on securities and corporate finance. LBAI is also accepted by the Stock Exchange of Hong Kong to act as sponsor for Hong Kong IPO transactions. For US customer agency transactions, LBAI is a fully guaranteed subsidiary of EFHC (NYSE Rule 322). • Lehman Brothers Commercial Corporation Asia Ltd. (LBCA), incorporated in Hong Kong engages in trading of fixed income and equities, as well as related products (repos), both as principal and agent, LBCA is a fully guaranteed subsidiary of SLBH. • Lehman Brothers Finance Asia Pte (LBFQ), established in Singapore in 2007 is mainly engaged in financial services and brokerage business for wholesale market. LBFQ is a fully guaranteed subsidiary of EFHC, available upon request. • Lehman Brothers Fixed Income Securities Pvt. Ltd. (LBFC), was authorized by the Reserve bank of India to serve as a primary dealer in Indian bond markets, effective 01 November 2007. • Lehman Brothers Financial Services India Private limited (LBSI), is a Lehman group entity in India, regulated as per Indian Companies Act and providing certain back-office services to Lehman Brothers group entities. Guarantee provided by SLBH for credit extended. • Lehman Brothers Securities Private Limited (LBSP), is a securities broking entity regulated by the Securities & Exchange Board of India (SEBI). Guarantee provided by SLBH for credit extended. • LB India Holdings Mauritius II Limited (LBIU), is a FDI entity investing in India. Guarantee provided by SLBH for credit extended (ie ISDA agreement). • Lehman Brothers Capital Private Limited, which is obligor under proposed INM committed credit facility. Will be guaranteed by SLBH.	LBSP Unregulated subsidiaries (CRR3.3): LBCA, LBAH, LBFQ, LBSI, LBIU
Derivatives	Lehman Brothers acts as principal in fixed income derivative product transactions primarily through Lehman Brothers Special Financing Inc., Delaware (SLBF), and in equity derivative products transactions primarily through Lehman Brothers Finance S.A., Switzerland (LMFI), which are guaranteed by SLBH. In addition, Lehman Brothers has established a triple-A rated structured derivative products company, Lehman Brothers Financial Products Inc., Delaware (LBFP), which is a consolidated subsidiary of EFHC. However, LBFP is a bankruptcy remote stand-alone unit and is evaluated and rated as such. LBFP has an enhanced continuation structure to ensure that swap obligations will be fulfilled to maturity.	With the exception of LBFP, financial statements are not available, nor required, based on parental credit support. With the exception of LBFP, all other subsidiaries are fully guaranteed by SLBH pursuant to master ISDA agreements (CRR 3.3). **LBFP @ 11/30/06** Assets: $523 Equity: $284
Capital Growth Investments Ltd (CGIL)	Incorporated on 12/31/05 in Mauritius to conduct trading activities.	CRR: 4.1
Lehman Brothers Delta (Cayman) No 2 (LBDC)	Limited liability company, which provides equity finance.	CRR: 4.1
South Pacific Mortgage ltd. (SPMY)	London-based and registered company that engages in residential mortgage lending.	CRR: 4.1
TL II Asset Management	Limited is deleted as no usage	

APPENDIX D
Summary of HSBC Committed Revolving Credit Facilities

Facility # 1: $50m commitment in a $2.0bn 3-year unsecured revolving credit facility ("RCF").

Borrower: Lehman Brothers Holdings Inc. (SLBH) – ultimate holding company

Lender: HBUS

Agent: JPMorgan Chase Bank, N.A.

Purpose: General corporate purposes / working capital. Periodic usage is expected.

Closing Date: 14-Mar-08

Maturity: 14-Mar-11

Base Rate: At SLBH's option: LIBOR+; Fed Funds +; or Base Rate+ (Higher of Agent's Prime Rate or overnight Effective Federal Funds Rate + .50%)

Margin: based on SLBH's senior unsecured debt ratings, as follows

Moody's/S&P Debt Rating	Facility Fee	Margin	Utilization Fee*
>=Aa3 or AA-	9.0	36.0	10.0
A1 or A+ (current rating)	**10.0**	**40.0**	**10.0**
A2 or A	11.0	51.5	15.0
A3 or A-	12.0	63.0	15.0
Baa1 or BBB+ or below	15.0	72.5	20.0

* Payable if the RCF is outstanding more than 180 days in a 4 calendar period.

Covenants: Usual and customary for a RCF of this kind, and to include:
• Minimum TNW of not less than $12.9bn.

Law: State of New York

Facility # 2: $50m commitment in a $2.5bn 3-year unsecured revolving credit facility

Borrower: Lehman Brothers Bankhaus AG (LEBB)

Guarantor: SLBH

Lender: HBEU

Agent: Citibank

Purpose: General corporate purposes / working capital. Periodic usage is expected.

Closing Date: April 16, 2007

Maturity: April 16, 2010

Pricing: Facility fee: 4.5bps;
Drawn: LIBOR/EURIBOR + 12.5bps;
Utilization fee: 3bps (on usage over 65%)

Covenants: Usual and customary for a RCF of this kind, and to include:
• Minimum TNW (guarantor) of not less than $7.0bn.

Law: English

3) (INDICATIVE TERM SHEET)

Facility:	Bi-lateral INR equivalent of USD100 million unsecured committed revolving loan facility available for a 24-month term. Borrowing currency is INR.
Borrower:	Lehman Brothers Capital Private Limited
Guarantor:	Lehman Brothers Holdings Inc.
Lender:	HBAP INM
Closing Date:	TBD
Purpose:	Cash capital facility to support the company's business as a Reserve Bank of India (RBI) regulated Non-Banking Financial Company (NBFC). The facility is required to support the on-going working capital requirements of the Borrower. **Usage expected.**
Extension of Facility:	Every 12 months at the bank's sole discretion for an additional 12-month tenor.

Commitment Fees:

Utilization level	*Fees as a percentage of unutilized facility amount**
Less than 25%	0.35%
between 25% and 50%	0.20%
between 50% and 60%	0.10%
Greater than 60%	Nil

**Utilization based fees to be paid quarterly in arrears, based on the average utilization level over the last quarter. Fees have been quoted on an annualized basis.*

Drawn Pricing:	Mutually agreed at the time of drawdown and applicable for the full tenor of the drawdown, with an all-inclusive quote based on HSBC's internal Cost of Funds. In the event of rating downgrade of Guarantor, the Lender reserves the right to revise the pricing of the drawn loans, along with revision of the commitment fee matrix linked to utilization level.
Interest Periods:	Interest on the loan will be charged on daily balances at the agreed rate but subject to fluctuation at Lender's discretion and payable monthly in arrears to the debit of your current account.
Default Interest Rate:	Default interest will be charged at 2% over Lender's Prime Lending Rate (PLR)
Events of Default:	Consistent with HBUS Holdco RCF facility.
Governing Law:	India