

WEEKLY FINANCE UPDATE

Week Ended August 11th, 2006

* All financials reflect five business days from the previous Friday through Thursday

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Firm & Industry Overview – Ed Grieb / Erik Umlauf

FIRM PERFORMANCE OVERVIEW

- Revenues for the week were \$211 million, 35% below budget
- Lehman Brothers stock closed at \$65.01, down approximately 2% for the week

GLOBAL MARKET UPDATE

- Continued pricing pressure and terrorism fears drove stocks lower this week, with the Dow down -1.4%, the NASDAQ down -1.3%, and the S&P 500 down -1.0%.
- Treasury movement continued to be volatile this week. Economic data showed that inflation continued to build even as growth showed signs of moderating. Weaker than anticipated 3-year auction and investor skittishness ahead of Tuesday's FOMC meeting pushed yields 1-3 bp higher across the curve in a bear flattener early in the week. Following the Fed's pause on Tuesday, Treasuries rallied before selling off on Wednesday as a surge in new issue supply sparked hedging activity. Thursday, saw a short-lived flight to quality rally on news of the foiled terrorist plot before higher than expected retail sales on Friday sparked a sell off. Yields closed the week 5-9 bp higher across the curve.
- The US trade deficit narrowed in June to \$64.8 billion. Exports rose to a record helped by a pick up in economic growth abroad and a weaker dollar. Looking forward, a rising oil-import bill along with consumer appetite for foreign-made goods makes a substantial improvement in the deficit difficult.
- Initial jobless claims came in stronger than expected at 319,000. Claims are likely to creep upwards as companies lay off workers in an attempt to reduce costs in a slowing economy.
- Wholesale inventories increased 0.8% in June. Consumer and business demand still appear to be strong as the inventory-to-sales ratio fell to a record low, indicating inflation threats continue to persist.
- Productivity growth numbers decelerated sharply. The combined compensation and productivity growth figures led to an increase in unit labor costs to 4.2% versus an expected 3.7%. The trend in unit labor costs is clearly higher, but the Fed argues that firms can absorb this increased cost by reducing profit margins.
- June Consumer Credit rose \$10.3 billion. Higher borrowing continues to put money into consumer pockets, increasing inflation risks, but helping to support growth.

COMPETITOR/INDUSTRY UPDATE

Brokerage News

Goldman Sachs

- Obtained a license to operate at the Dubai International Financial Centre (DIFC) in the United Arab Emirates
- Granted a license to trade securities in Russia
- Industrial and Commercial Bank of China is teaming up with Goldman Sachs to help in the design and execution of upcoming QDII funds. ICBC cannot directly invest QDII funds in instruments other than fixed-income, but it can do so by allocating cash to third-party funds. ICBC, the country's biggest lender, has drawn 500 million Yuan (\$63 million) in orders for its first overseas fund and is now partnering with Goldman to woo more.

Morgan Stanley

- Will acquire residential mortgage lender and servicer Saxon Capital Inc. for \$706 million. Saxon was the 14th largest nonprime mortgage servicer last year, handling accounts representing \$26 billion in loans. The company, which also buys and originates loans, held \$6.5 billion in mortgages in its portfolio as of March 31. The deal is expected to be completed by year-end.
- Hired David Spector from Countrywide Financial Corp., the largest US mortgage lender, to run its pan-European residential mortgage business starting in September.
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Merrill Lynch

- Granted approval to trade Vietnam-listed stocks as a foreign investor, giving it access to a \$2.5 billion market
- Named Citigroup's Rahul Malhotra as head of its private client business in India as part of a five-year

expansion plan for the business. Malhotra would start on September 1 and be based in Singapore, overseeing its onshore Indian brokerage operations and its non-resident Indian business. Malhotra has led retail banking in Asia Pacific for Citigroup.

Citigroup

- The NASD fined retail-brokerage unit \$1.1 million for its role in a plot to waive mutual-fund sales charges by using false disability claims. Citigroup was ordered to pay a \$400,000 fine and \$715,000 in restitution to several unidentified mutual funds after the securities regulator discovered more than 100 company brokers improperly obtained thousands of mutual-fund sales-charge waivers by falsely claiming that their customers -- including several hedge funds -- were "disabled" individuals. The ploy took place from mid-2001 through mid-2002.
- China's banking regulator said it had authorized Citibank to invest client funds overseas as part of the country's QDII programme. The Citigroup unit is the seventh bank to win approval.

China M&A

- Dealogic released the top ten M&A advisors in China so far in 2006. China Galaxy Securities Co. topped the list with \$1,822mm deals handled. PWC and Somerley Ltd. took second and third places with \$1,130mm and \$793mm respectively. Merrill Lynch, JP Morgan, and Morgan Stanley made the top 10, taking spots 5, 6, and 8 respectively. Lehman Brothers took number 9 slot with total size of deals handled this year of \$325 million.

Asset Management

Pension Bill Promises Windfall for Fund Firms. The legislation, which is designed to encourage wider participation in defined-contribution plans such as 401k, contains provisions that are likely to sharply increase the number of people pouring their savings into these investments.

'Side-Pocket' Accounts of Hedge Funds Studied. Some hedge-fund firms are setting up separate accounts to hold certain harder-to-value investments. Regulators and investors are concerned about whether these "side pockets" accounts are being handled properly and whether they might help hedge funds overstate performance.

Hartford to Handle Funds In-House as they plan to expand the lineup of funds into stock funds, particularly in the small- and midcap areas. Hartford had \$33bn in mutual fund AUM at second quarter end, up \$7bn from prior year.

ETF Boom Expands With Exchange-Traded Notes. Barclays Bank PLC recently introduced exchange-traded notes tracking two popular commodity indexes: the iPath Goldman Sachs Commodity Index and iPath Dow Jones-AIG Commodity Index.

MotherRock L.P Energy Hedge Fund to Close after suffering big losses in the natural-gas market in June and July. MotherRock's energy fund took the brunt of its losses giving up \$230mm because of investor redemptions and movements in the natural-gas market.

Private Equity Firm First Reserve Corp will launch a record \$7.8bn private equity fund to invest in energy infrastructure, production and service companies. This fund is the largest energy investment pool raised to date.

Repeal of the Florida Intangibles Tax. On July 27, 2006 Florida Governor Jeb Bush signed a bill repealing the Florida Intangible Property Tax. The bill eliminates the annual tax on stocks, bonds and other intangible property held in Florida. The effective date of the bill is January 1, 2007.

Financial Control – Ed Grieb

REGULATORY MATTERS	
REGULATORY:	
Excess Capital-Capital Ratio	<ul style="list-style-type: none"> ▪ LBI \$4.9 bln, up \$42mm from last week <ul style="list-style-type: none"> ➢ Increase due to decrease in LBI-LBIE receivable ▪ LBIE: 136.0% (\$2.0bn), up 6% (\$250mm) from prior week <ul style="list-style-type: none"> ➢ PRR decreased \$100mm due to a decrease in options positions. ➢ LER decreased \$100mm as intercompany balances decreased. ▪ LBJ: Capital Ratio 231%, flat from prior week <ul style="list-style-type: none"> ➢ Excess Net Capital now \$34.3mm versus \$80.9mm last week. ▪ LOTC: \$162mm v \$163mm in prior week ▪ NBLLC: \$292mm v \$292mm in prior week
15C3.3 Reserve	<ul style="list-style-type: none"> ▪ Balance is unchanged at \$3.6bln

TAX UPDATE	
<ul style="list-style-type: none"> ▪ Evaluating global tax risk (including foreign country corporate structure) ▪ Reviewing legal entity and tax reporting issues surrounding new Energy business ▪ LBJ's APA application around transfer pricing has been finalized and currently being reviewed ▪ Investigating merits of investing in Wind and Housing Tax Credit structures to lower future ETR ▪ APB23 restructuring for Asia progressing ▪ Investigating UK thin CAP rules to accomplish additional group relief structure ▪ Designing IRS Audit Plan for 2001-2004 cycle 	

Finance Group Update

IMD	
Major Events	<ul style="list-style-type: none"> - IMD Finance and Risk Management presented a review of the Cash Management Business to Chris O'Meara, Dave Goldfarb and Madelyn Antoncic. - ARS Finance met with Joe Cosic, E&Y Partner, to discuss LBAIM fund of funds audit and timing of Management Company audit which will start in September. - IMD Finance Council diversity members along with Operations Diversity Council, and HR met with Marisa Thalberg, founder and President of Executive Moms to discuss possible participation by Lehman in future Executive Mom events. - Private Equity Finance had Sungard/Investran vendor presentations this week. Next week "The Next Round" will be making their presentation to the same group. - Several members of IMD Finance attended a presentation by Operations of their costs and allocation percentages for the first half of the year made by Rhonda Teadore.
Personnel Change	<ul style="list-style-type: none"> - Sakyi Oduro, an Associate in Private Equity Finance focusing on the Euro Mezz product, has resigned from the firm.

GLOBAL INFRASTRUCTURE FINANCE (GIF)	
Major Events	<ul style="list-style-type: none"> ▪ None

TECHNOLOGY UPDATE	
Infrastructure Control	<ul style="list-style-type: none"> ▪ Neuberger Berman Integration (original live 12/1) - Although the project team is on target with deliverables, the project requires a new feed from IMD (Advantage Billing - critical dependency). Problems with the vendor feed, Advantage, have pushed back delivery dates. The project team has developed a set of high level expectations with regard to tasks and dates to be discussed with IMD on 8/14. Re-cast of the NB Integration timeline will follow shortly. ▪ Sales Person Control (live - Q12007) - Integration work with GSS and MTS continues and is on schedule. Functional specs are 65% complete. Prototyping the workflow in Staffware will begin at the end of August as the remainder of functional specs are finalized. ▪ Aurora Loan Services Integration (live 2007) - BRD walk-throughs and sign-offs are in progress. The FTG budget request will be based on the detailed BRD.

TREASURY	
<u>Rating Agencies</u>	
<ul style="list-style-type: none"> ▪ Agreed Rating Evaluation Service scope and terms with S&P ▪ Agreed Fitch report on LBCB 	
<u>FP&A</u>	
<ul style="list-style-type: none"> ▪ Finalized dividend from LBI and subdebt replacement 	
<u>Creditor Relations</u>	
<ul style="list-style-type: none"> ▪ Agreed attendees and senior plan for IMF with Dave Goldfarb and Chris O'Meara ▪ Met with Giulio di Cerbo (Citibank) to introduce Carlo and explain Italian clearance position 	
<u>Investments</u>	
<ul style="list-style-type: none"> ▪ Produced Investment Overview for Chris O'Meara 	
<u>Asset & Liability Management</u>	
<ul style="list-style-type: none"> ▪ Debt Management - Completed update of EMTN program for 2006. We upsized the EMTN Facility from \$45Bn to \$60Bn to accommodate global growth in projected issuance requirements and upsized the LBBankhaus subshelf to \$2Bn. Mumbai are assisting London in populating missing debt data fields used 	

for core debt MIS reporting.

- **LBBankhaus AG** - Approved upsize of PML warehouse lending line from GBP500mm to GBP750mm. Upsize will enable Bankhaus to fund an additional GBP170mm of PML assets on the next roll date of 15th August. Initiated Legal Entity structure review with counterparts in NY. Commenced review of LBF client collateral posting with LBBAG and potential to migrate to IMD liquidity funds.
- **London Funding Desk** - Met with Gerd Redenbach (portfolio manager of Activest Total Return Fund) to review fund strategy. Funding Desk to revert on SEC and Lehman Equity attribution for investments of this nature. Prepared first draft strategic FX hedging update for review with COM.
- **Lehman India** - Met with Erik Umlauf to review displacement statistics for Global Treasury.
- **Financial Resources** - CP met with Senior Controllers Group to relaunch fortnightly European Financial Resources Committee.
- **Issuance:**
 - Bear 1.25bil 5y:
 - 750mm 5y fixed at 1ml + 21.5 equivalent
 - 500mm 5y FRN at 3ml + 21
 - Merrill 1.25bil 3y:
 - 800mm at 3ml + 9
 - 450mm at 1ml + 9
 - Credit Suisse 2bil 5y, 500mm 10y:
 - 750mm 5y fixed at 1ml + 20.5 equivalent
 - 1.25bil 5y FRN at 3ml + 20
 - 500mm 10 fixed at 1ml + 35
 - Bank of America 1.75bil 5y and 1.25bil 10y:
 - 1bil 5y fixed at 1ml + 10.5 equivalent
 - 750mm 5y FRN at 3ml + 10
 - 750mm 10 fixed at 33
 - 500mm FRN at 3ml + 33

Cash and Collateral Management

- **GCCM:** Graham Kettle and Gavin Netzel are visiting the GCCM Core team in New Jersey from 7th to 11th August to close out on all outstanding European issues and progress with UAT. Focus has mainly been to ensure the European instance of GCCM has been set up correctly with priority attention on static data and accounting methodologies.
- **Peoplesoft:** Completed user acceptance testing for next phase of Peoplesoft rollout to Treasury Workstation. This phase will see Swiss Franc accounts payable transactions processed through LBHIUK's cash account. Go Live scheduled for week of 14th August.
- **Milestones:** Final draft for nostro breaks milestones and nostro query response times complete - to be signed off with Julie Tungate on Monday.

Network Management

- **SWX Warrants:** Agreed with desk to have Citibank provide the settlements and clearing platform for this business. Team needs to keep the pressure on Citibank to ensure they meet the deadlines.
- **Neuberger Berman LLC** - Reviewed Neuberger Berman accounts with BONY to ensure they were properly set up and named. Ensured proper no-lien documentation was put in place for our Exclusive benefit of Customer, EBOC & Proprietary Account for Introducing Brokers, PAIB accounts with the Bank.

Personnel

- Courtney Critchlow has resigned from Lehman Brothers

EUROPE FINANCE UPDATE

EQUITIES

- Volatility
 - \$12.6m on 15 year ATM vanilla put with Hedge fund on Eurostoxx, volatility deemed observable.
 - \$13m on Vallourec relating to unwind of mandatory convertible, collars and hedging.
 - Both trades were with Banking

FID

- Fund Derivatives
 - **Pipeline trade:** The first tranche of Usd 500 mil of the Huan An trade is likely to be traded in September. This is a 6 year, CPPI, issued through Anthracite Cayman Investments Ltd. This is a flagship deal with a Chinese fund manager.
- Energy Update
 - Trading of UK Nat Gas, CO2 and financial Oil underway. Volumes are gradually increasing. P&L and risk relatively flat.
 - Discussions are taking place and BRD documents written for new system feeds/automation of processes.
 - Two new Structured traders started last week. Discussions underway on trades, systems, processes and P&L reporting
 - Power UAT scheduled for Sep/Oct
- CTE CAD 2 - the CAD 2 application for CTE is due to be submitted to FSA on 14 August

IMD

- Project Bullet has ended due to a question on valuation.

MCD

- High Wycombe Finance collective relocation consultation will now complete on 17 August with individual consultations starting then.
- Revised product range to increase SPML volumes still on track to be introduced on 1 September.

TAX

- Structured Finance – Structured Finance are bidding for UK unsecured NPL's – vendor is Citibank. Tax involved in initial structuring discussions.
- BPM STG transaction – closed on the 17 July 2006 revenues c\$8m. We are currently reviewing a further UK potential cash tax benefit of c.\$8m, although this will not impact the rate.
- Derecognition trade – due diligence has been continuing on this trade since its close on 31 May 2006, Oversight committee meeting tabled for the 14 August 2006 to review risk assessment, evaluate any potential benefits and determine next steps, if any.
- LBLF – We have set out our reasons to HMRC why we should not be subject to a mis-declaration penalty. This was an agreed step from a previous meeting in which we attempted to resolve this issue. Depending on the outcome of this correspondence we will need to determine our next steps. We have instructed Freshfields to provide us with an updated risk assessment.
- APB23 Planning
Limited Partnership / Preference Share Structure – In broad terms the proposal is to insert a Scottish LLP above or in place of Spain Holdings and to replace LBIE sub debt with preference or ordinary shares. Treasury, Financial Control and GAAP group were walked through structure. Concept approved in principle but a number of points remain outstanding.
 - (i) Amount of equity versus sub debt to be injected into the LLP
 - (ii) Equity injection into LBIE should this be Tier 1 or Tier 2 capital or a combination?
 - (iii) At what level will UK group be consolidated for UK GAAP purposes – E&Y initial view was at the Luxco level which is not ideal, if this view stands may need to insert another UK co above Lux
 - (iv) Tax group needs to decide timing of Spain liquidation
- MCD structure – the proposal is to split the origination from the structured financing business and equity fund the warehouse company to create group relievable losses. We have established that there are no issues from a UK or US tax perspective. Still needs confirmation from Bankhaus that the Bankhaus security on the loan to UK Holdco is adequate and also need to confirm which entity will provide reps and warranties to the orphan securitization SPV.
- Tax disclosure rules – amended rules came into effect on 1 August 2006 which may require the Firm to disclose certain transactions to HMRC. The advance disclosure is designed to alert HMRC as to potential loopholes to enable them to close them down but does not impact whether a transaction that has been executed works. We have presented to the Equities Exec Committee on these changes and briefed the Capital Markets and IBD lawyers. Presentation to Oversight Committee scheduled for 21 August.

REGULATORY & CONTROL

- Anna Yu and Eric Spahr from the NY Regulatory Reporting team spent the week with the London team and IT, developing a roadmap for global regulatory systems which maximises synergies between CSE and Basel II

- Regulatory Reporting were represented at the August 7th meeting of the FSA's securitisations standing group where the FSA set out their proposal for the practical application of the Basel II securitisation framework, the main components being:
 - a number of visits to member Firms was proposed to discuss all aspects of the securitisation process - to feed into the Pillar 2 review going forward
 - an outline of proposed report formats was reviewed / discussed
 - a discussion of the FSA's current and proposed research into this area

Divisional Information

Capital Markets – Gerry Reilly

CAPITAL MARKETS OVERVIEW

Significant Prior Week Events (8/04 – 8/10)

- **Energy trading** with gains of \$3MM performed above budget this week with gains in Power of \$2MM
- **Volatility Europe** gains of \$25MM were driven by origination gains of \$18MM
- **Strong origination** week with revenues of \$17MM, mostly due to a new client Eurostoxx put, \$6MM, and partial unwind of the Vallourec trade and convertible fees, \$5MM
- **IRP's Net Balance Sheet** increased by \$5B mostly due to Repo 105
- **Equities VaR** increased over the week to \$15MM mostly due to a \$3MM increase in Equities Syndication

FID Weekly Rev (MM) 86 FID finished the week down \$(97) to budget and down \$(78) to prior week.

Out-performers

Energy Trading	3	Due to gains in Power \$2, also was the highest FID performance against budget for the week
Mortgages	20	Includes \$13 in affiliate origination revenues
Interest Rate Products	19	Includes \$10 in Americas in Vega P&L as vols decreased and \$14 in Asia from short overall JPY IR delta offset by losses in option theta and a long JGB floater
Real Estate	11	Driven by \$6 MTM adjustment for LBS Holding SARM and \$6 in carry of various CMBS positions

Under-performers

High Yield	(10)	\$(26) below budget
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Equities Weekly Rev (MM) 47 Equities finished the week down \$(23) vs budget and down \$(19) vs the prior week.

Out-performers

Volatility Europe	24	Mostly driven by gains in Vol Origination \$18, including Eurostoxx put \$13 and Vallourec unwind \$5
Execution Services Europe	10	Includes cash gains of \$5 with commissions of \$6 and a loss ratio of 36%
Prime Services	15	Mostly due to gains in Yield Enhancement for the week on Spain and Netherlands distribution trades

Under-performers

Liquid Markets Americas	8	\$(17) below budget, mostly due to losses in Event Driven \$(6) and Flow Volatility \$(2)
Equity Strategies Asia	(6)	\$(9) below budget, mostly driven by loss in SBI Holding \$(2) and Non Japan Proprietary \$(2)
Convertibles Americas	(3)	\$(6) below budget

Performance Overview:

Net BS	Current Week	Target	Δ PW		C Wk	Target	Δ PW
FID	195,006	170,833	5,921	Equities	60,305	68,000	(528)
<i>Significant w/w movements</i>							
IRP	52,489		5,006	Prime Services	26,356		(150)
Real Estate	32,340		(2,031)	Eq Strategies	1,662		(121)
Mortgages	48,992		(1,182)				

Cash Capital	Current Week	Limit	Δ PW		C Wk	Limit	Δ PW
FID	50,866	48,000	1,065	Equities	11,670	10,000	337
<i>Significant w/w movements</i>							
St Finance	5,289		1,189	Vol Europe	2,877		407
Credit (HG)	2,051		(944)				
High Yield	2,949		699				

Risk Appetite

FID	1,365	1,625	(6)	Equities	418	550	77
<i>Significant w/w movements</i>							
LMP	125		(23)	Syndicate	79		41
Energy	41		(24)	Volatility	194		(23)
Real Estate	556		19				

Value at Risk (VaR)

FID	34.4	55.0	(0.5)	Equities	14.9	22.0	3.8
<i>Significant w/w movements</i>							
LMP	7.4		(1.3)	Syndicate	4.8		2.5
Energy	2.6		(1.4)	Volatility	6.6		0.5
Real Estate	6.0		1.9	LM/ Ex Svcs	7.0		(1.2)

IBD Division – Gerry Reilly

INVESTMENT BANKING OVERVIEW		
Performance overview:		
<ul style="list-style-type: none"> ▪ IBD Revenues for the week were \$74mm, above budget by \$10mm <ul style="list-style-type: none"> -- M&A \$24mm, Equities \$39mm, Fixed Income \$14mm, Other (\$3mm) 		
M&A		
Total M&A Revenues	\$24mm	Above budget by \$4mm
Announced		<ul style="list-style-type: none"> ▪ Cinemark USA, (value undisclosed), acquisition of Century Theatres - \$1.7mm estimated fees in 09/06. ▪ Carlyle Group (together with Finmeccanica), \$3.2bn, sale of Avio to Cinven - \$10.6mm estimated fees in 10/06. ▪ Plains Exploration and Production Company, \$865mm, sale of non-strategic oil & gas properties to Occidental Petroleum Corp. - \$8.7mm estimated fees in 09/06.
Completed		<ul style="list-style-type: none"> ▪ Kerr-McGee Corporation, \$18.2bn, sale to Anadarko Petroleum Corporation - \$17.5mm in Success Fee.
Deals Done Away included:		<ul style="list-style-type: none"> ▪ Texas Pacific Group Inc., \$3.9bn, acquisition of Aleris International Inc. TPG was advised by DB. Aleris was advised by Citi. ▪ Investor Group, comprised of Doughty Hanson & Co Ltd (DH) and Providence Equity Partners LLC of the US, \$2.8bn, acquisition of Caudwell Group. Caudwell Group was advised by Rothschild. ▪ Universal Computer Systems Inc., \$2.6bn, acquisition of Reynolds & Reynolds Co. Universal Computer was advised by CS/DB/GS. Reynolds & Reynolds was advised by JPM.
League Tables (Worldwide)		<p>Announced #7, flat to last week and last year Completed #7, flat to last week, and up from #8 last year</p>
Pipeline (Week 8/11- 8/17)		<ul style="list-style-type: none"> ▪ Predix Pharmaceutical Holdings Inc, \$671mm, sale to Epix Pharmaceuticals, Inc.

EQUITIES

Total Equity Underwriting Revenues **\$39mm**

Above budget by \$20mm

Last week equity volume increased as companies hurried to complete deals ahead of the late-August slowdown. The IPO market continues to struggle as witnessed by the Qimonda and GNC offerings. The Qimonda transaction was downsized 45% and GNC was postponed due to market conditions. The Lehman led Evercore Partners transaction was the best performing IPO of the week, pricing at \$1 above the range and finishing up 16% for the week. We earned fees of \$2.1mm on the deal. In the follow-on market, secondary issuance increased 91% week-over-week as 13 deals priced raising \$2.6bn. A majority of this volume was from increased block activity (5 deals for \$1.5bn). Lehman was active executing blocks of Boston Properties and On Semiconductor totaling \$387mm. Convertibles issuance was active, with Real Estate being the most active sector. We acted as sole books on the \$125mm Retail Ventures offering, earning \$3.0mm in fees.

- **Berkshire Hathaway**, Derivative - \$12.8mm Revenue
- **US Shipping Partners LP**, \$77.5mm, PIPE & Structuring fee - \$6.7mm Revenue
- **Salzgitter AG (Vallourec)**, \$448mm, Cvt - \$4.6mm Revenue
- **Retail Ventures Inc.**, \$125mm, Cvt - \$3.0mm Revenue
- **Evercore Partners Inc.**, \$83mm, IPO - \$2.1mm Revenue
- **Kinder Morgan Energy Partners**, \$224mm, Sec'd/FO - \$2.0mm Revenue
- **Allscripts Healthcare Solutions Inc.**, \$43mm, Block - \$1.5mm Revenue
- **Infrasource Services Inc.**, \$179mm, Sec'd/FO - \$1.4mm Revenue

Deals Done Away included:

- **NRG Energy, Inc. (D)**, \$816mm, Block, via MS

League Tables (Worldwide)

#9, up from #10 last week, and flat to last year

Pipeline (Week 8/11 - 8/17)

- **Annaly**, \$300mm, Sec'd/FO
- **Permian Basin**, \$130mm, Sec'd/FO
- **CV Therapeutics**, \$75mm, Sec'd/FO

FIXED INCOME

Total Debt Underwriting Revenues **\$14mm**

Below Budget by \$17mm

The US *Investment Grade* New Issue supply this week was \$25bn. Of that, Lehman Brothers participated in 5 transactions totaling \$4.4bn. We acted as sole-book runner on a \$1.5bn CVS Corp 5yr & 10 yr Fixed Note. Lehman was a joint-book runner on a \$2bn US Bank 18mo FRN, a \$350mm Pacificorp 30yr Fixed Note, a \$300mm GECC 30yr FRN, and a \$250mm CIT Group Extendible.

The *High Yield* Market Index increased 1/8 of a point to 96.5 this week. In High Yield, US Supply for the week was \$1.3bn of which Lehman participated in no transactions.

- **GECC**, \$300mm, FRN - \$1.0mm Revenue

Deals Done Away included:

- **Seimens AG (D)**, \$5.0bn, IG, via Citi/DB/MS/JPM

League Tables (Worldwide)

#4, down from #3 last week and down from #2 last year

Pipeline (Week 8/11 – 8/17)

- **Travelport Corp Solutions (Blackstone), \$4.3bn, HY**
- **Expedia, \$1.0bn, IG**

BUSINESS INITIATIVES / PERSONNEL CHANGE

2006 Associate class started

New Hires:

Bryan Boudreau, MD, Insurance/Pension Solutions, NY (from Morgan Stanley)
Paul Inouye, MD, Media, Menlo Park (from Piper Jaffray)
David Kostman, MD, Media, NY (from Delta)
William R. Sperry, MD, Industrial, NY (from JP Morgan)

IMD Division – Ed Grieb

BUSINESS PERFORMANCE OVERVIEW		
Total Revenues	\$34.9mm	<ul style="list-style-type: none"> ▪ This week: \$12.8mm, or 26.8% below budget ▪ \$33.2mm lower than prior week's revenues and \$83mm above YTD budget
PIM	\$19.7mm	<ul style="list-style-type: none"> ▪ \$2.7mm below budget and \$7.5mm lower than prior ▪ <u>Fixed Income</u>: \$0.6mm gain from WTS LBH Currency Basket, \$0.6mm gain from Euro Medium Term Note, \$0.5mm gain from Lehman XS Trust Series 2006-GP3 Mortgage Trading ▪ <u>Equities</u>: \$1.4m gain from Kinder Morgan Energy Partners LP, \$0.3mm gain from Ameritrade Holding Corp Block Trade ▪ <u>Asset Management</u>: \$0.3mm gain from LB Bank Sweeps
Asset Mgmt	\$19.5mm	<ul style="list-style-type: none"> ▪ PAM \$10.4mm, Funds \$6.5mm, IAM \$1.4mm, ARS \$1.3mm, AM Admin (\$0.1mm) ▪ \$1.1mm below weekly budget and \$17.8mm lower than prior week due to gains recognized last week from GLG ▪ <u>Absolute Return Strategies</u>: \$0.6mm gain from Satori Tech Fund Investment
Private Equity	(\$3.0mm)	<ul style="list-style-type: none"> ▪ \$9.4mm below budget and \$10.4mm below prior week due to unrealized losses on public investments ▪ <u>Merchant Banking</u>: (\$1.8mm) mtm loss from Blount International ▪ <u>Venture Capital</u>: \$1.6mm mtm gain from Theravance, (\$1.4mm) mtm loss from PEMSTAR, (\$0.6mm) mtm loss from Regeneration Technologies ▪ <u>Credit Related</u>: (\$2.2mm) mtm loss from Crosstex Energy
AUM	\$203.7bn	<ul style="list-style-type: none"> ▪ Increase of \$28.7bn, or 16.4% since year end 2005, and \$1.2bn higher than prior week due to inflows of \$0.8 bn to Liquidity funds, \$0.5 bn increase to PIM cash management business, and \$0.2bn increase in ARS (Strategic Commodities Fund +130mm, Global Macro + \$30mm). These increases were offset by small decreases in Asset Management due to market performance.

BUSINESS INITIATIVES/ PERSONNEL CHANGE	
<p>PIM—Effective September 30, 2006 Polen Capital will no longer be available as a recommended manager on our Manager Access Program (MAP). As such, effective September 30, 2006 Lehman Brothers will no longer provide ongoing due diligence and monitoring on Polen Capital.</p> <p>Private Equity –Private Equity Investment Committee approved up to a \$31.0 million equity investment for the acquisition and entitlement of 10000 Santa Monica Boulevard located in a prime location in Los Angeles, California. The site, situated on one of the last remaining developable land parcels on Santa Monica Boulevard within walking distance of the Century City office district and Beverly Hills retail amenities, is expected to be entitled for the development of approximately 210 luxury condominium units. The investment will be made in partnership with SunCal Companies and is contemplated for inclusion in the LBREP / SunCal Master III LLC.</p> <p>Private Equity – Investment Committee approved a \$19.8 million investment in the Series 2006-1 Class D Notes of GoldenTree Credit Opportunities Financing I, Ltd., a market-value CDO primarily investing in high-yield bonds, bank loans and special situations.</p>	

Treasury – Paolo Tonucci / Heidemarie Echtermann

BUSINESS PERFORMANCE OVERVIEW

Summary of Key Treasury Analytics

Millions, shares, \$ per share, percent

	7/31	8/4	Change
Liquidity			
LBHI MCO1 Year Forward	1,133	962	(171)
LBHI Cash Capital Position	3,934	3,988	54
Excess Investment Returns ¹	131.8	132.5	0.7
Thrift Total Assets	20,921	21,377	456
Thrift Cash Capital Position	6,363	8,029	1,666
LBCB Total Assets	3,174	3,157	(17)
LBCB Cash Capital Position	145	182	37
Bankhaus Total Assets	8,677	8,748	71
Bankhaus Cash Capital Position	306	678	372

	Week of 8/4	3Q 06	YTD
Long-Term Debt Issuance			
Total Issuance (\$mm)	1	3,722	29,032
# of Issuance	1	271	1,274

Balance Sheet / Equity	8/8/2006	August Targets	Variance
Total Assets	503,539	473,512	30,027
Net Assets	272,536	248,326	24,210
Stockholders' Equity	18,271	18,357	(86)
Leverage Equity	17,640	17,650	(10)
Gross Leverage	28.5x	25.8x	2.8x
Net Leverage	15.4x	14.1x	1.4x

Share Repurchase (OM)	Week of 8/11	3Q 06 QTD	FY 2006 YTD
Shares Purchased	899,500	9,409,500	32,009,500
Wavg Purchase Price	\$65.84	\$63.80	\$68.00
Average Close ²	\$65.38	\$63.97	\$68.14
Average 10b-18 ²	\$65.83	\$63.98	\$68.08

Regulatory Capital	7/31	8/4	Change
LBI (CSE Effective Dec 1)	4,988	5,042	54
LBIE	134%	130%	-4%
LBI	242%	234%	-8%

¹ Annualized, excess returns including tax benefits

² Averages excluding blackout dates. 10b-18 is weighted based on order-adjusted straight-line execution.

Europe – Richard Amat

REVENUE OVERVIEW	
Total Revenues	Weekly revenues of \$70.5m vs \$70.1m budget are 1% above budget. Previous week's revenues were \$103.1m.
FID	<ul style="list-style-type: none"> ▪ \$21.0m in the week, versus prior week of \$50.5m and budget of \$34.2m is 39% below budget. ▪ In IRP, \$2.8m was made in Options Exotics including \$2.0m on Volbond 15x20 with BNP Paribas (notional €75m). ▪ Structured Finance made \$5.8m, including \$2.9m in Principal Finance on MTM on futures on mortgages and \$2.2m in Mortgage Subs on MTM on warehouses. ▪ FX made \$2.9m, including \$1.5m in Spot on new business across various currencies. ▪ High Yield made \$1.6m, including \$2.4m on Food and Steel sector remarks.
Equities	<ul style="list-style-type: none"> ▪ \$33.5m in the week, versus prior week of \$20.8m and budget of \$22.9m is 46% above budget. ▪ Volatility made \$24.5m, including \$12.6m made in Risk on 15 year Eurostoxx money put with a hedge fund and \$5.0m fees on partial unwind of Salzgitter's Vallourec trade [both JVs with Banking, 50% offset in EQU Corp]. ▪ In Execution Services, Cash made \$5.6m in the week including \$3.3m in Sector Prop [inc. \$2.6m in Consumers] and Portfolio made \$3.0m including \$1.8m in Agency Programs. ▪ Yield Enhancement made \$3.0m, including \$1.7m on Spanish distribution [Banco Santander] and \$1.3m in Netherlands [principal stock Royal KPN]. ▪ In Converts, \$2.3m was made on Salzgitter's €350m mandatory exchangeable offering [JV with Banking]. ▪ In Equity Corp, \$(6.3)m represents offset re 15 year Eurostoxx money put with a hedge fund and \$(2.5)m represents offset re fees on partial unwind of Salzgitter's Vallourec trade.
Banking	<ul style="list-style-type: none"> ▪ \$21.1m in the week, versus prior week of \$14.7m and budget of \$17.9m is 18% above budget. ▪ ECM made \$14.0m including \$10.2m fees on Salzgitter's Vallourec trade (incl. \$5.0m on partial unwind of derivative trade and \$4.6m on €350m mandatory exchangeable offering) and \$3.2m on 15 year Eurostoxx money put with a hedge fund [all JVs with EQU]. ▪ M&A made \$5.7m including \$4.8m advisory fees on Scottish & Newcastle Plc £487m refinancing of Globe pubs.
Other	<ul style="list-style-type: none"> ▪ Non – Core Offset was \$(7.7)m for the week.

Asia – Enrico Corsalini

BUSINESS PERFORMANCE OVERVIEW

Total Revenues Weekly revenues are \$0.8m this week. YTD revenues are 15% ahead of budget. A weekly summary is below.

FID

Gain of \$0.6m

▪ **Governments : \$0.8m**

\$0.9m : 14y/17y vs. 29y/31y JGB flattener position (\$0.6m PV01) as the curve flattened approximately 1.5bp

\$0.8m : 7y/8y vs. 10y/11y JGB flattener position (\$0.6m PV01) as the curve flattened approximately 1.5bp

(\$0.8m) : intraday loss

▪ **Derivatives : (\$2.4m)**

\$13.4m : short overall JPY IR delta position of \$2.6m as rates increased 5.10bp on average

\$0.4m : JPY swap and swaption intraday trading

(\$5.9m) : long JGB floater position of about JPY 209bn as prices fell

(\$5.6m) : option theta

(\$4.7m) : JPY vega positions in the 1m/10y options into the 2y and 5y swap regions where vols fell 0.35 on average

▪ **CDO : \$1.8m**

\$1.9m : origination fee for START II CLO deal with SCB

(\$0.1m) : global CDO daily P&L allocation

Equities

Loss of (\$2.8m)

▪ **Cash : (\$1.6m)**

(\$1.6m) : Non-Japan Sales (+\$0.5m) & Trading (-\$2.1m)

Flat : Japan Sales (+\$0.8m), Trading (-\$1.1m), & Facilitation (+\$0.2m)

▪ **Volatility : \$3.0m**

\$2.7m : Prop, mainly from McDonald's block trade (+\$2.5m)

\$0.3m : Flow, mainly delta gains on Korean market exposure

▪ **Equity Strategies : (\$5.6m)**

(\$5.6m) : Japan, mainly from Softbank Investment (-\$2.2m) and directional trading on other Japanese stocks

▪ **Prime Services : \$1.5m**

\$0.8m : Equity Finance, mainly from fees and London allocations

\$0.7m : Stat Arb, mainly from commissions

GTS

Gain of \$3.3m

▪ **NY Allocation : \$3.5m**

\$3.1m : India positions

\$0.4m : U.S. hedges

▪ **Asia Positions : (\$0.1m)**

Risk

▪ **Fixed Income VAR is \$7.3m (limit: \$15m)**

FX-delta is long \$18.4m vs. prior week long \$128.7m

▪ **Equities VAR is \$6.4m (limit: \$12m)**

Net delta is long \$528.3m vs. prior week long \$531.2m

Top 4, by market: Japan, long \$281.9m; Hong Kong, long \$47.7m; China, long \$74m; South Korea, long \$48.8m

▪ **Global Trading Strategies VAR is \$2.4m (limit: \$5.5m)**

Positions as of August 10, 2006