

From: Umezaki, Kentaro <komezaki@lehman.com>
Sent: Thursday, April 19, 2007 2:18 PM (GMT)
To: Freidheim, Scott J <Freidheim@lehman.com>; Lowitt, Ian T <ilowitt@lehman.com>; O'Meara, Chris M (NY) <comeara@lehman.com>; Reilly, Gerard <greilly@lehman.com>
Cc: Archer, Mary Pat <marcher@lehman.com>; Gelband, Michael <mgelband@lehman.com>; Umezaki, Kentaro <komezaki@lehman.com>
Subject: RE: Feedback

All:

Thanks for each your responses. Totally get all your points. Two more clarifications from me below. Obviously we should talk at some point as a group as opposed to emails. Looking forward to that opportunity.

A. Process: I have no issues with the process of vetting the content on any of the communications recently. We actually do a very good job of that today. Mary Pat is unquestionably the right person: she speaks for FID absolutely. (In fact in this MD instance, from what I understand, we did debate whether we should add something to the effect of "growing responsibly" (NPE dilemma etc.). It just didn't make the final cut).

B. Content: It may not have been clear from my note that the bulk of the issues I raised are around the content consistency of the messages that come from the various corporate areas to the business decision makers, specifically trading managers and traders. The messages come in "fragments" from different groups, not as a whole. That's what I would like to improve. My detailed views are below if you want to read them.

Thanks,

Ken

Communicating the strategy to trading heads/traders: here's the logic.

1. Who owns the responsibility of managing to our capital constraints?: Executing on our capital strategy largely falls on these trading heads/decisionmakers, as opposed to IBD, IMD, sales, research, Corporate etc. Capital constraints that we have do impact our trader's collective daily behavior, which impacts our revenue outcome. This capital management is an "additional element" if you will that not every LB person deals with regularly.

2. Incentives and motivation: the majority of the trading businesses focus is on revenues, with balance sheet, risk limit, capital or cost implications being a secondary concern. The fact that they haven't

heard that those items matter public forums from senior management recently reinforces this revenue oriented behavior implicitly. In my opinion, this group is not behaving "badly": they are just getting conflicting messages that go unreconciled ("grow revenues" from FID; "manage balance sheet" from Finance, if you will). We also don't have a strong enough mechanism to reinforce "better" behavior around these non-revenue metrics, as comp is tied to revenues at the divisional level. Tough problem to solve given the way we incent today. We've been debating this for a good decade now.....

3. The dilemma of a "unified" message: the capital/risk taking side of the business cannot hear a "different" message than the client side of the business from senior management. If bankers and salespeople don't know that we have capital constraints (if that is the message?) then we will never deliver as Scott called it a "One Firm" view. Ultimately, this is what I think makes the unified message objective for the firm very challenging. Example which we've debated for years: was even a topic in FLA: Do we or don't we have a limit on how much HY LBO related lending/commitment exposure we can have at any given time? There has been no real "one firm" outcome to date in my opinion. I'm not the only one who has this view in FID.

4. Communicate to FID: Given we run a relatively decentralized organization in FID, there are probably 40+ key decisionmakers that are 1 step "below" Mike's directs that need to hear the more detailed consistent message. This is the population that are making capital decisions everyday that don't have enough visibility into what is going on "upstairs" if you will.

> _____
> From: Freidheim, Scott J
> Sent: Wednesday, April 18, 2007 1:07 PM
> To: Umezaki, Kentaro
> Cc: Gelband, Michael; Archer, Mary Pat; Lowitt, Ian T; Reilly, Gerard; O'Meara, Chris M (NY)
> Subject: RE: Feedback
>
> Ken:
> Communicating our Firmwide strategy is a priority. We are doing a lot
> about it and have a process to get everyone's input. On what we're
> doing first. This is the basis upon which Dick has revised his year
> end webcast and remarks to senior leaders following the 4th (2006) and
> 1st (2007) quarter earnings releases. Additionally, we have done a
> lot of work to launch a Dear Colleague articulating the Firm's
> strategy followed by a Dear Colleague articulating our acquisition
> strategy shortly thereafter. We also are planning to run four sets of
> strategy posters for the elevators globally starting monday....each of
> the four elements of the strategy will run separately during the
> course of a five week period. Screen savers will run for two months.
> All of the CAOs have reviewed and signed off on the first Dear
> Colleague and are being sent the poster series next for comment. The
> current plan is also to have the Firm's strategy to be featured in the
> next firmwide newsletter....just as the current newsletter being

> desk-dropped next week features Prime Services. In Europe, we have
> launched a strategy webcast with Jeremy that is live q+a - he has done
> one and is set to do the next in June. In Asia, Jesse is doing it via
> town halls. Dick has already done the town hall in Europe and is set
> to do Asia in May. Clearly, we need to be completely together. I
> think we have a good process in place. Anywhere you think we should
> modify how Dick or any Firmwide piece would be welcome input and
> should be funneled through Mary Pat unless you disagree. I assume
> CAOs speak for divisions and regions. Dick's remarks were sent to all
> CAOs and we received comments from many (including FID). I am adamant
> about ensuring that all divisions and regions sign off and that
> everything we do is One Firm. Please comment on any of the materials
> and we can incorporate/revisit anything to clarify. Having the right
> messages is incredibly important. Thank you for the note, as it
> matters.

> Scott

>

>

> From: Umezaki, Kentaro
> Sent: Wednesday, April 18, 2007 10:45 AM
> To: Lowitt, Ian T; Reilly, Gerard; O'Meara, Chris M (NY); Freidheim,
> Scott J
> Cc: Umezaki, Kentaro; Gelband, Michael; Archer, Mary Pat
> Subject: Feedback

>

> Ian, Scott, Gerry and Chris:

>

> Given our balance sheet belt tightening effort in FID, I thought you
> should get the following feedback post Dick's MD talk last night from
> some of the business people in FID.

>

> Basically, they heard we don't have a balance sheet problem: in fact
> we have excess capacity given our growth in equity and so we have to
> work harder at putting capital to work: Goldfarb's group, more
> principal trades, find bigger trades to do etc. etc. Their view is
> that the message we are sending from Corporate/Finance and "FID
> central" around Q2 balance sheet target, ratings upgrade etc. is
> contrary to the basic message from the chairman:

>

> 1. Inconsistent Messages: As I have said many times already in the
> past, I continue to be somewhat confused as to what the real
> objectives of the firm are around managing financial and risk
> constraints vs. revenue growth. I found I could not adequately
> respond to the people's questions in a way that I felt was credible.
> As we go thru our process around controlling our balance sheet targets
> more efficiently, I'm pretty sure this will come up repeatedly as
> well. As FID is the largest consumer of the firm's capital
> resources, personally I feel I need to get "re-educated" on this so I
> can represent the views of the firm better. FID can't be given
> unresolved conflicting messages from "CAO vs. Chairman", if you will.
> What's the answer?

>

> 2. Balanced Communication: I would very much appreciate it if we
> could get better going forward at sending a more consistent message to
> the organization in these public forums? Of course I totally
> understand the "motivational" aspects of Dick's presentation. But,

> even a simple statement that we are currently on watch for an upgrade
> and it's important to strive for AA for <x> reasons; the importance of
> growing our business in a "fiscally responsible way" etc.would have
> been sufficient to balance the message. (I don't believe "we are
> striving for 22-24% ROE" is sufficient, by the way: too vague).
> Otherwise it's an unfair "fight": revenue growth is what we in FID
> heard from Dick. He didn't say manage our balance sheet.
>
> Unfortunate, but one sentence is all that is/was needed, in my
> opinion.
>
> 3. Let's articulate the strategy!: I think it is time (again) to draft
> a composite message from the differing objectives amongst the
> constituents in the firm's Corporate and Business areas. Sort of a
> "big picture" strategy piece like what Goldfarb presented in FLA a few
> years back. If there is a composite message from the Firm around how
> to grow responsibly, we MUST be able to articulate it? If we don't
> want to do this for some reason, then I'd like to understand the real
> reasons behind why we don't.
>
> In a basic sense, there should be a "living/breathing" document that
> we can continuously recirculate/recalibrate as to what our long term
> goals are and check ourselves as the markets change the rules. A way
> to do this, perhaps, is to articulate our strategic "non-negotiables":
> maybe AA rating is one of them, for instance. Maintaining our culture
> could be another. Cross cycle ROE of 20%+ could be another. Revenue
> growth that exceeds our cost growth could be another. Etc. The
> non-negotiable objectives put no constraints on what we can achieve as
> a firm, but do put reasonable "caps and floors" on how and how quickly
> we can achieve them. There are probably 10 or so of these, and all of
> us know what they are, yet we rarely transform/translate the
> non-negotiables into financial objectives: financial objectives being
> what our people really understand.
>
> In my opinion, we all (including me) gotta get our act together better
> around this stuff given how big a set of businesses we are running and
> how many "new" people we are adding into team LEH every day! Thanks
> for e-listening. Would like to hear your views.
>
> Regards,
>
> Ken