Sub Prime(r)

September 6, 2007

LEHMAN BROTHERS

Agenda

- What are Sub Prime Mortgages?
- Loan Characteristics & Risk Factors
- Sub Prime Trading Desk Functions
- HEL Deal Structure
- 2006 Sub Prime Performance
- Hedging - ABS Credit Default Swaps

What are Sub Prime Mortgages?

- Sub prime Mortgages or Home equity loans (HEL) are loans made to borrowers with either imperfect or limited credit histories or little equity
  - More than 90% of the market consists of first liens
  - Average FICO's of pools range from 610-640.
  - About 20-30% of market is now purchase money; rest are cash out refinance
  - About 60-65% are full documentation loans; rest are limited/ no doc
  - Typically 80% Loan to Value Ratio

- Due to the additional risk in these loans, they have higher coupons than prime mortgages (typically 150-250 bp higher)

Loan Characteristics

- Interest Payments
  - Fixed-rate (25-30% by market value)
  - Hybrid: 2/28 (55-65%) and 3/27 (5-10%)
    - o 2/28 & 3/27 : Pay fixed-rate of interest for the first 2/3 years, then floating-rate of interest for the remaining term
    - o Hybrids have embedded caps on the loan rate – Initial reset cap, periodic cap, lifetime cap
- Principal Payments
  - Level Pay
  - Interest-only loan
    - o Borrower pays interest only for an initial period (typically 5/10 years)
    - o Increasingly common over the last 3 years

Current coupon on 30 year fixed rate 620 FICO 80 LTV Full Doc is ~11%, up from 9% six months ago (while benchmark rates have rallied)

Product Characteristics by vintage

Vintage	Avg Bal (1,000s)	Doc (% Full)	FICO	Purp (% Purch)	WAC (%)	HYB (%)	IO (%)	2nd Lien (%)	Prop (%MF)	Occup (% Prim)	CLTV	LTV	MI (%)
1999	94	75	598	27	9.95	50	0	2.4	5.5	94	77.8	77.8	2
2000	104	75	595	34	10.41	67	0	2.3	5.4	94	78.1	77.9	20
2001	123	73	601	31	9.78	72	0	1.7	5.4	94	79.0	78.6	32
2002	138	70	613	30	8.73	70	1	1.5	6.3	94	80.8	80.2	23
2003	158	65	621	29	7.65	64	2	1.2	7.4	94	82.0	81.0	18
2004	174	62	624	35	7.15	74	11	1.6	7.5	93	83.6	81.1	6
2005	191	59	626	40	7.25	77	25	3.0	7.3	93	85.3	81.1	8
2006	203	55	627	45	8.18	78	20	5.2	7.2	93	86.5	81.3	4

Source: Lehman Brothers, Loan Performance

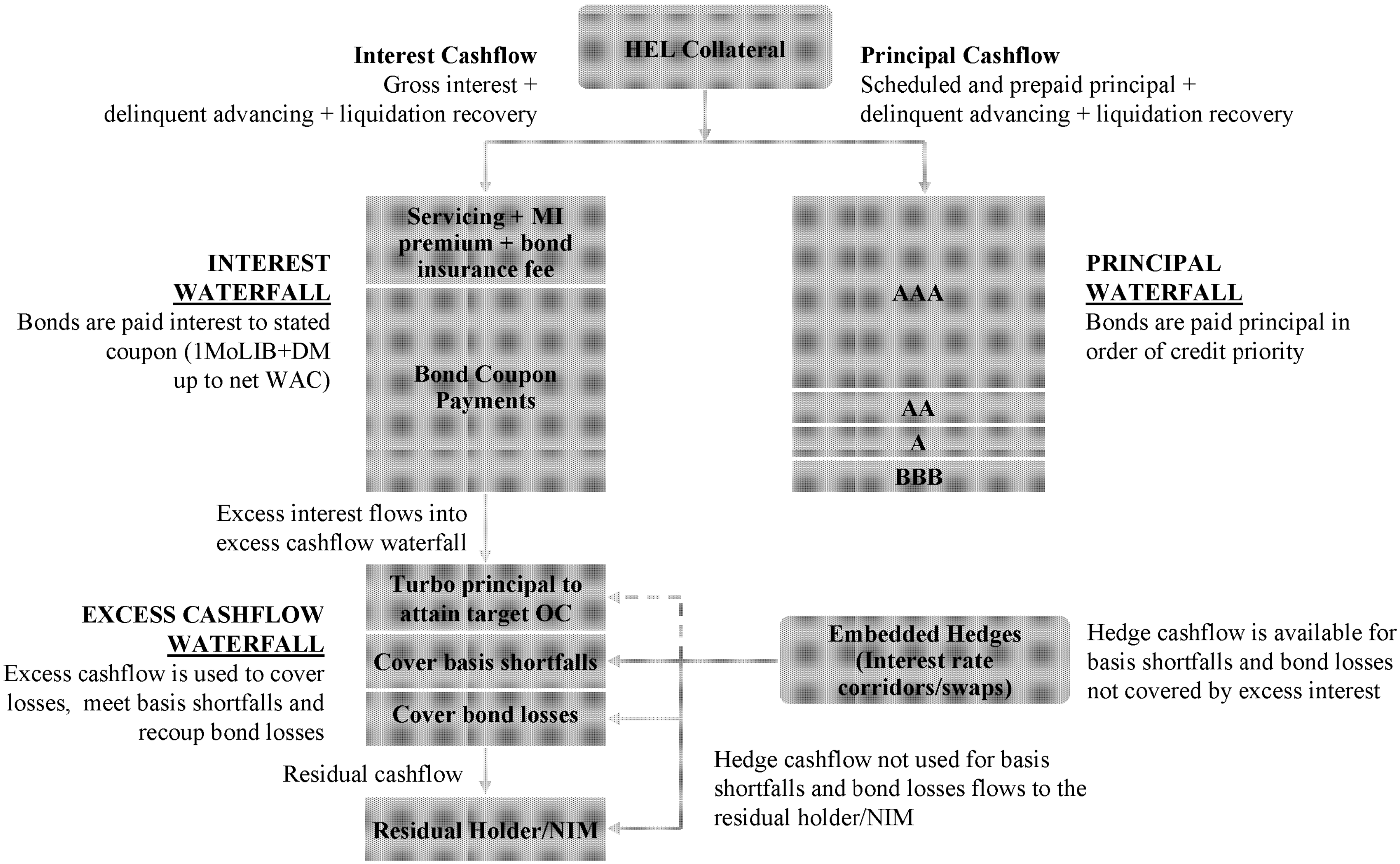
Risks

- Credit Risk – lender may not receive principal back if the value of the home falls below the value of the mortgage and the borrower is unable or unwilling to make payments. Borrowers pay higher rates to compensate for their increased credit risks
- Prepayment Risk – Prepayment option with the borrower. Mitigated to some extent by prepayment penalties on loans. Fast repayments limit total interest payments received from borrowers.
- Basis Risk in ABS securities issued – the mortgages are generally fixed rate for 2 years and then float at a spread to 6 month libor (2/28s) and are financed with floating rate assets based of 1M Libor

Sub prime Trading Desk Functions

- Whole Loan Trading (Sub Prime and Scratch & Dent Loans)
  - Besides buying all loans originated by Lehman-owned affiliates, the desk buys packages through competitive whole loan bids, both sub prime and scratch and dent (non-performing loans or current loans with delinquent history)
  - Sales of whole loans are increasing as we partner with clients
- Hedging
  - Use Rate Swaps, Futures, TBAs, single name CDS and ABX to hedge risks
- Structuring and Securitization
  - Each deal is structured after obtaining ratings from two or more of Moody's, S&P and Fitch and placed in the market through the syndicate desk
- Residuals
  - Sale of residuals (equity piece) key to realizing value on securitization
- Secondary Trading
  - Bid on all Lehman issued Subordinate securities and participate in NIM Bid Lists

An Overview of Structure



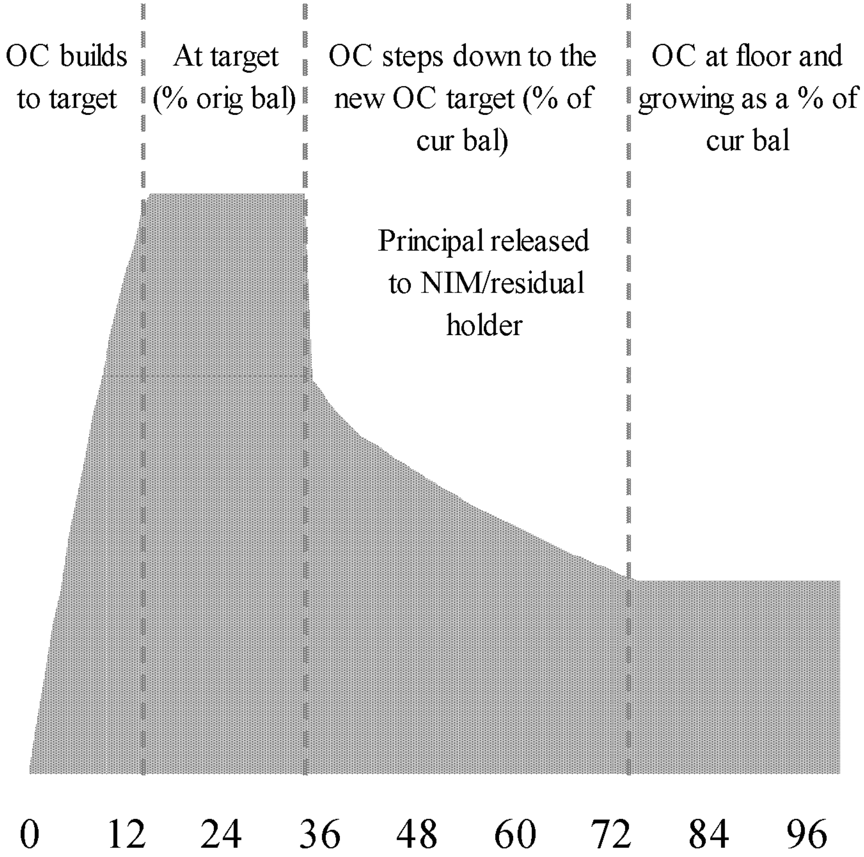
Unique Sub Prime Security Characteristics

- Amortization and Prepayments
  - Different bonds are subject to different combination of prepay, default and basis risk depending on the their position in the cash flow waterfall
- Timing of Principal Writedowns
  - Principal losses occur over time. Subordinate bonds are typically locked out of principal payments until step-down or maturity of AAA bonds
- Reversible Writedowns and Shortfalls
  - Excess spread can be used to cover writedowns and shortfalls
- Available Funds Cap Risk (Interest Shortfalls)
  - HEL coupons are capped at net WAC of the collateral. Derivatives such as amortizing swap and cap used in deals to mitigate this risk
- Clean-up Calls
  - Bond coupon spread steps up 1.5-2.0x times the original amount if the call is not exercised. Typically clean up call level is 10%.

Principal Payments Determined by Triggers and OC

60+ Dq, % of Original Balance (incl FCL, BK, REO)

OC Mechanics



Trigger Specification

- Cumulative Loss Trigger
  - Threshold specified as % of the original balance of the deal
  - Follows a schedule typically stepping up from month 36 to 72-84
- Delinquency Trigger
  - Threshold specified as a percentage of the senior credit enhancement
  - For example, trigger might be specified if 60+ delinquencies are more than 50% of senior credit enhancement
  - Typically toggles between passing and failing

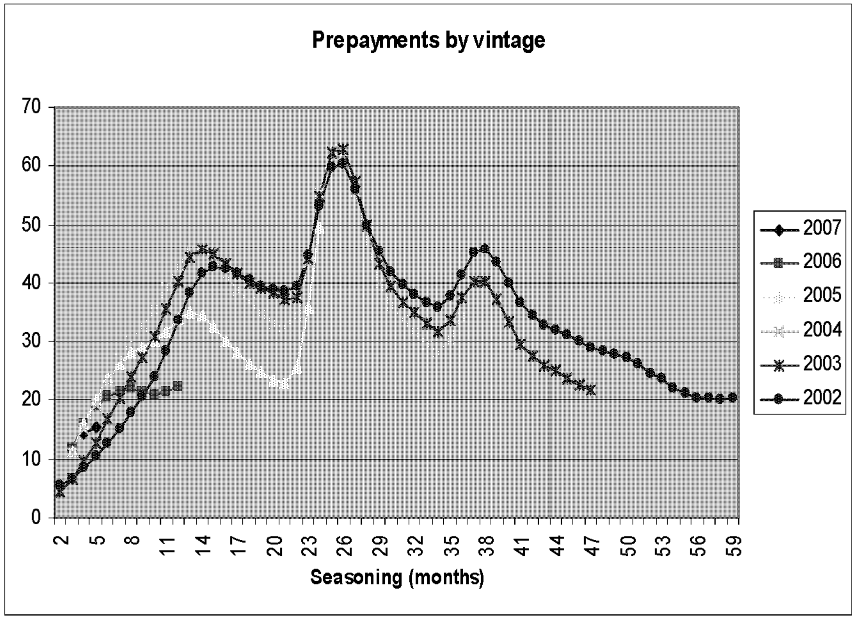
Sources: Intex, Lehman Brothers

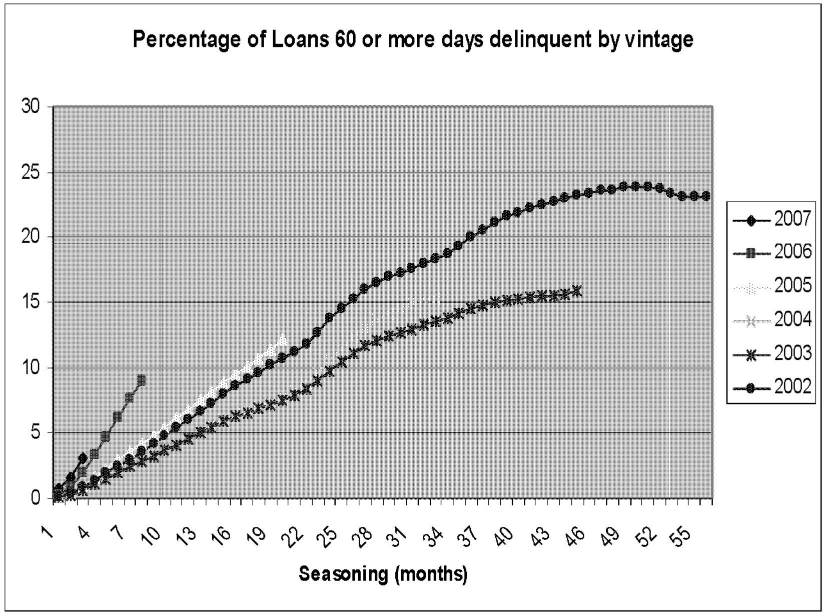
Residuals

- Levered ownership of underlying collateral
- First loss piece in the capital structure
- 3 Components
  - Excess Interest not used as credit support
  - Overcollateralization amounts
  - Prepayment Penalties
- Nims
  - Securitization of the Residual Cash flow
  - <1yr average life often BBB rated
  - Has principal and fixed rate coupon
- Market currently trades ~20% yield to base case prepay and loss assumptions

2006 Subprime Performance

- Early delinquencies on 2006 vintage have been the worst subprime has ever seen
- Prepayment speeds have been slower due to lower refinancing opportunities in an environment of slowing HPA and tightening guidelines

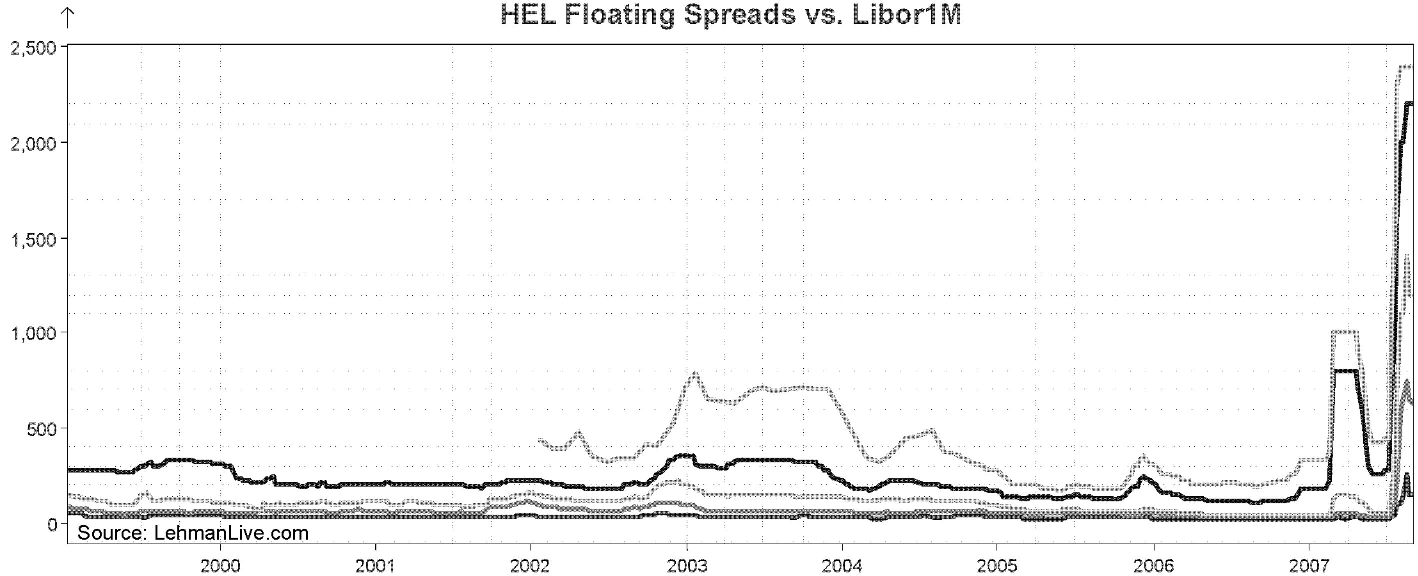




Key drivers of poor 2006 sub prime loan performance

- Macro
  - Slowing HPA
  - Lack of refinance opportunities as industry shrinks and guidelines are tighter; 20-30Bn of loans reset every month in second half of 2007 and first half of 2008
- Collateral Characteristics
  - High Combined Loan-to-value (CLTV) Ratios
  - High % of Stated Documentation and low doc loans
  - Second liens - 30% of all second liens tranches have been downgraded
  - First time homebuyers
  - Layering of risk

Sub Prime Cash Historical Spreads



Key	Axis	Name	Last	Minimum		Maximum		Mean	SD	SD Change
	Left	AAA 3yr PT	150.000	14.000	01/26/2007	250.000	08/17/2007	29.305	16.508	7.820
	Left	AA 5yr	625.000	27.000	01/26/2007	750.000	08/17/2007	64.000	65.836	21.139
	Left	A 5yr	1200.000	38.000	01/26/2007	1400.000	08/17/2007	118.201	125.673	33.541
	Left	BBB 5yr	2200.000	100.000	08/25/2006	2200.000	08/17/2007	253.088	237.462	49.463
	Left	BBB- 5yr	2400.000	170.000	05/20/2005	2400.000	08/03/2007	420.948	436.104	97.550

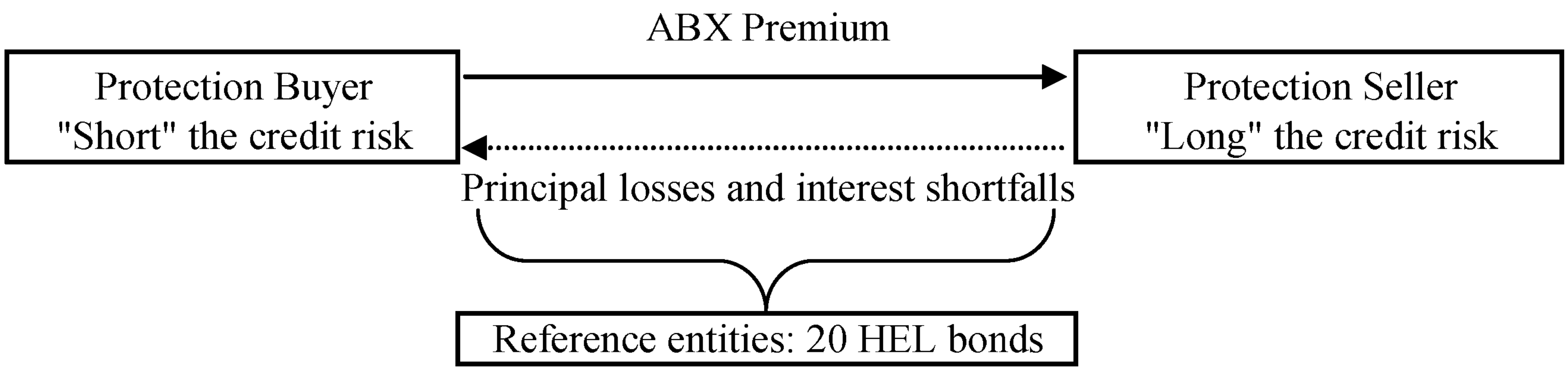
Lehman's Recent Strategy

– Since second half of 2006 - Tightened underwriting guidelines at BNC
  - Eliminated 80/20 combo loan program
  - Eliminated 100% CLTV stated doc
  - Increased FICO cutoff for 100% CLTV full doc to 660
– Since December 2006 - "Carved" deals
  - Loans expected to under-perform carved out of our main deals
  - Example: SASCO 2006-BC6 (carved deal) and SASCO 2006-Z (deal with more adverse collateral) securitized separately
    - After 4 months of performance, SASCO 2006-Z deal has 4 times the delinquencies of the SASCO 2006-BC6 deal
– Past 1 month
  – Closure of BNC to realign resources with current market conditions
  – Sub prime will be originated as a product under Lehman Mortgage Capital

Recent measures to help sub prime borrowers

- Loan modifications
  - Servicers can proactively reach out to borrowers and modify payments for current borrowers facing payment difficulty usually at ARM reset
  - Modifications can include deferred payment, extension of maturity etc
- Early foreclosures
  - Servicers pay borrowers to vacate properties in foreclosure
- Government announcement to allow FHA to take on mortgage refinancing for troubled borrowers
  - FHA does not make direct consumer loans; insures other originators loans
  - Homeowners have to meet certain eligibility criteria
  - Program may target ~80K new households in 2008

Hedging using ABS CDS



Pay-As-You-Go Structure

Payment Type	Direction	Amounts
Fixed	Buyer → Seller	ABX Premium
Floating	Seller → Buyer	Principal writedown Interest shortfalls up to ABX premium
Additional fixed	Buyer → Seller	Reversible principal writedown Reimbursements of interest shortfall

**Here we use the term "buyer" to mean the buyer of protection, also known as the seller of the ABX index.*

The ABX Index and Applications of ABS CDS

- The ABX index is a collection of 20 single-name CDS contracts on a specified basket of HEL bonds
  - 5 sub-indices. One for each rating level – AAA, AA, A, BBB and BBB-
  - A set of 20 deals are selected and bonds across the capital structure from the same 20 deals are represented in each sub-index
  - Index trades on price terms and daily marks are provided by the dealer community
  - New ABX indices introduced every 6 months
  - Creates on-the-run (most recently created) and off-the-run (older vintages) indices
  - First index ABX 06-1 was introduced in January 2006, on-the-run index is the 07-1
  - Includes 20 CDS contracts on deals issued within the last 6 months

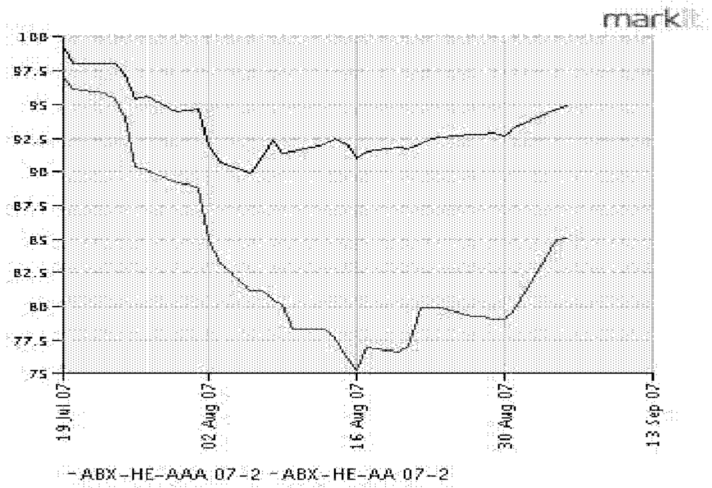
- Applications of ABS Credit Default Swaps
  - Single name CDS used to hedge individual bond positions across the capital structure
  - ABX may be used to express macro views on the housing market without having to worry about specific nuances of individual deals
  - ABX may be used to engage in pairs trading across rating classes and across vintages

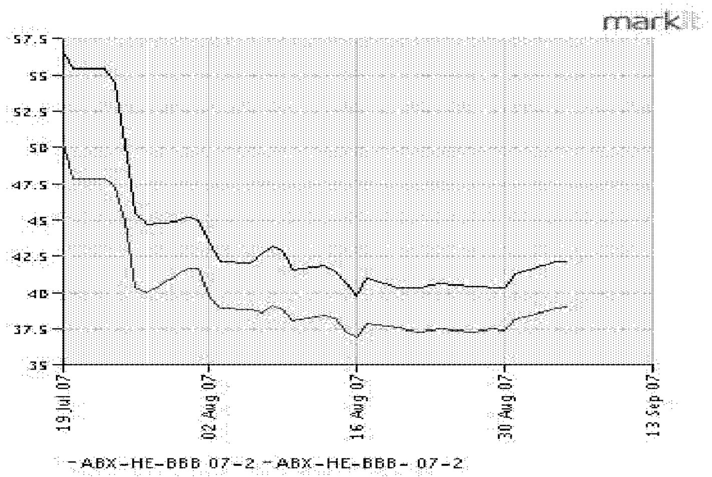
Key Differences Between Corporate CDS and ABS CDS

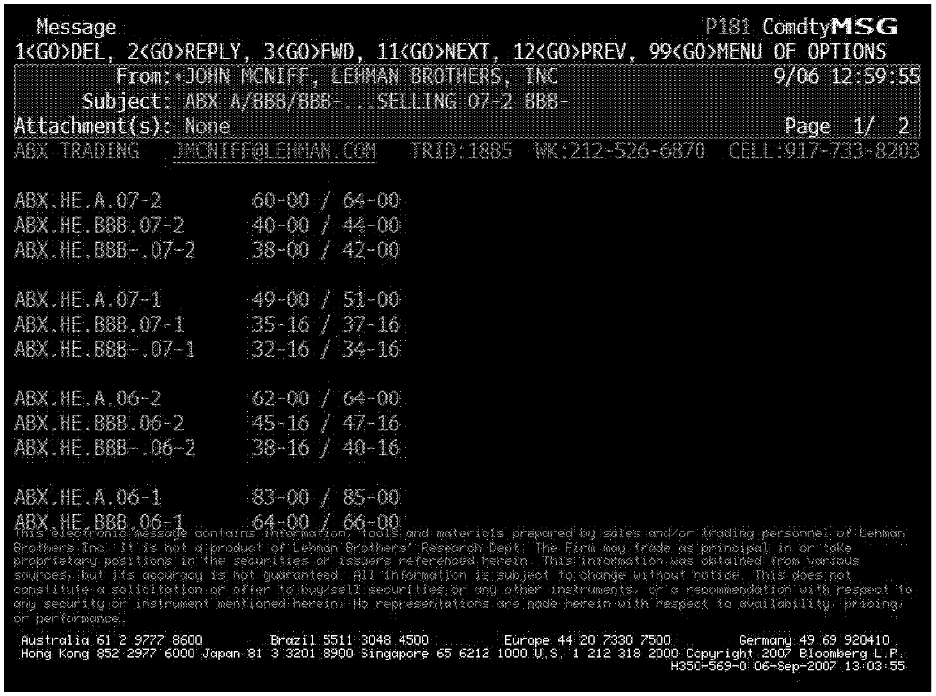
	Corporate CDS	ABS CDS
Reference Entity	A corporation	A single security
Settlement	Physical or cash settlement	Pay-as-you-go with a physical settlement option
Maturity Date	Typically 1-10 years	Earlier of underlying bond legal final maturity or full paydown
Credit Events	Failure-to-pay, bankruptcy, restructuring	Failure-to-pay, writedown, distressed downgrade, maturity extension
Principal Writedown	One time event	Losses occur over time, and can be reversed
Non-payment of Interest	Is a credit event	Not a credit event, but does trigger payment, can be reimbursed
Prepayment Uncertainty	Not applicable	Declining notional due to voluntary prepays and defaults

ABX 2007-1 Historical Spreads and Market Levels

– All ABX indices trading near historic lows with 2007-1 being the worst hit as it comprises deals from second half of 2006







Message P181 Comdty**MSG**

1<GO>DEL, 2<GO>REPLY, 3<GO>FWD, 11<GO>NEXT, 12<GO>PREV, 99<GO>MENU OF OPTIONS

From: JOHN MCNIFF, LEHMAN BROTHERS, INC 9/06 12:59:55

Subject: ABX A/BBB/BBB-...SELLING 07-2 BBB-

Attachment(s): None Page 1/ 2

ABX TRADING JMCNIFF@LEHMAN.COM TRID:1885 WK:212-526-6870 CELL:917-733-8203

ABX.HE.A.07-2	60-00 / 64-00
ABX.HE.BBB.07-2	40-00 / 44-00
ABX.HE.BBB-.07-2	38-00 / 42-00
ABX.HE.A.07-1	49-00 / 51-00
ABX.HE.BBB.07-1	35-16 / 37-16
ABX.HE.BBB-.07-1	32-16 / 34-16
ABX.HE.A.06-2	62-00 / 64-00
ABX.HE.BBB.06-2	45-16 / 47-16
ABX.HE.BBB-.06-2	38-16 / 40-16
ABX.HE.A.06-1	83-00 / 85-00
ABX.HE.BBB.06-1	64-00 / 66-00

This electronic message contains information, tools and materials prepared by sales and/or trading personnel of Lehman Brothers Inc. It is not a product of Lehman Brothers' Research Dept. The Firm may trade as principal in or take proprietary positions in the securities or issuers referenced herein. This information was obtained from various sources, but its accuracy is not guaranteed. All information is subject to change without notice. This does not constitute a solicitation or offer to buy/sell securities or any other instruments, or a recommendation with respect to any security or instrument mentioned herein. No representations are made herein with respect to availability, pricing, or performance.

LEHMAN BROTHERS