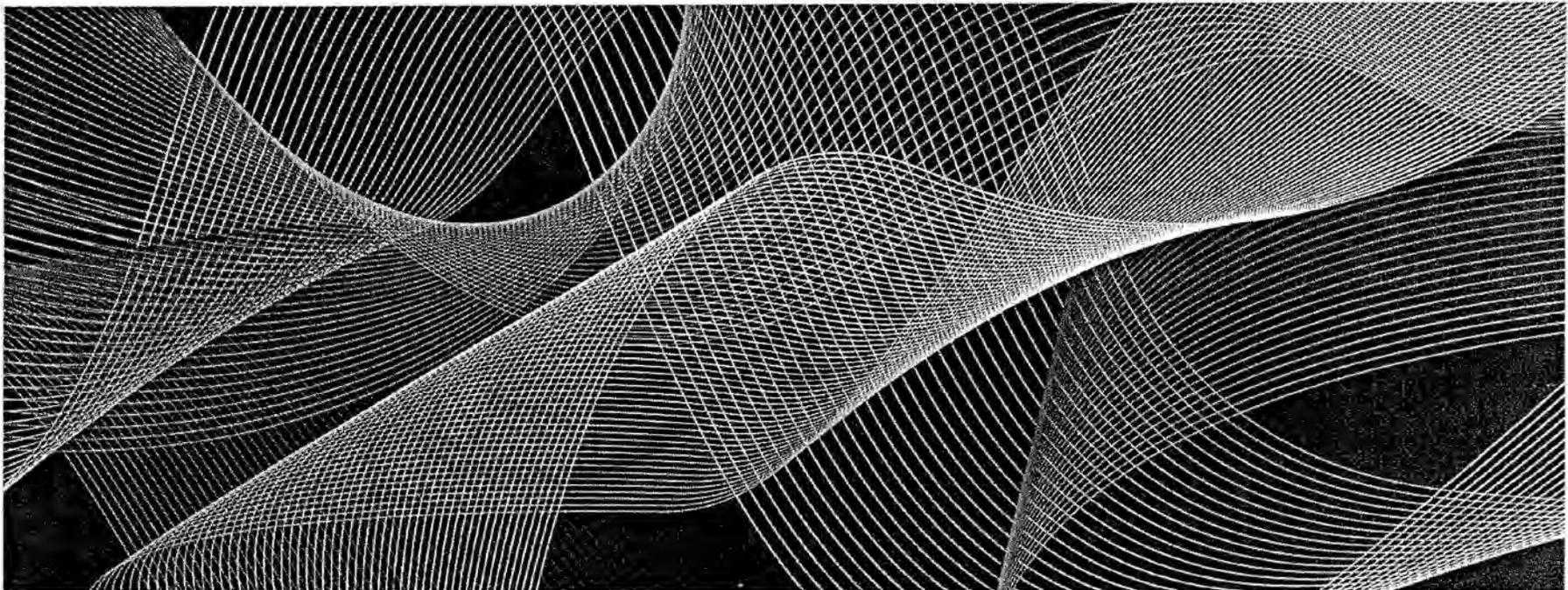


LEHMAN BROTHERS

September 10, 2008

Funding Lehman Brothers



Confidential Presentation

Agenda

- ◆ Introduction To The Funding Framework
- ◆ How Balance Sheet Is Funded
- ◆ 2008 Q3 Liquidity Update
- ◆ Lessons From The Bear Stearns Liquidity Event

Introduction To The Funding Framework

Overview Of The Funding Framework

- ◆ Established in the aftermath of the liquidity event of 1998, the Lehman Brothers Funding Framework is based on a set of conservative principles guiding the funding of assets and mitigating our liquidity risk. It has been refined and augmented over the years as Lehman enters new businesses and as the liquidity risk of existing businesses changes.
 - ◆ At its core are the following principles
 - Remain in a state of constant liquidity readiness
 - Do not rely on asset sales, increase in operational effectiveness or access to the unsecured debt market in a time of crisis
 - Be proactive with your key stakeholders before and during a liquidity event: regulators, creditors, trading counterparts and rating agencies
 - ◆ It is structured around three dimensions
 - Liquidity pool to cover cash outflows over a 12 month horizon at the Holdings Company
 - Cash capital to cover funding of illiquid assets as well as contingent liquidity risk
 - Secured funding plan to mitigate the liquidity risk associated with short-term secured funding, including the prime broker business
 - ◆ The conservativeness embedded in our Funding Framework (e.g., we fund boxed positions with cash capital, irrespective of the liquidity characteristics of the positions) is what distinguishes our Framework from that of our peers
-

Cash Capital Uses

All unsecured funding requirements in normal operating conditions require cash capital

	Examples	Cash Capital Principle
Illiquid positions	<ul style="list-style-type: none"> ◆ Corporate and commercial whole loans ◆ Long-term non-trading assets ◆ Exchange margin & other LT collateral ◆ Fixed income, equity derivative and FX 	<ul style="list-style-type: none"> ◆ Funded 100% with cash capital ◆ Determine whether a position is illiquid by looking at its fundability in a stress liquidity event
Secured haircuts on long inventory	<ul style="list-style-type: none"> ◆ Reverse repo agreements and borrowed securities ◆ Collateralized funding to counterparts 	<ul style="list-style-type: none"> ◆ Cash capital charge dependent on asset haircut ◆ Haircuts conservatively estimated and regularly reviewed ◆ If asset cannot be reliably funded on a secured basis in a liquidity event, the haircut assessed against the asset is 100%
Operational friction	<ul style="list-style-type: none"> ◆ Inventory in the “box” ◆ Cash at banks 	<ul style="list-style-type: none"> ◆ Unsecured financing assessed a “box” charge irrespective of liquidity characteristics ◆ Cash at banks deemed not to be freely available to Holdings
Legal entity trapped	<ul style="list-style-type: none"> ◆ Intercompany margin postings ◆ Structural trapped liquidity 	<ul style="list-style-type: none"> ◆ Margin posted by other entities into regulated entities ◆ Surplus cash due to regulatory capital requirements
Contingent liquidity	<ul style="list-style-type: none"> ◆ CP backstops ◆ High-yield revolvers ◆ Secured lines of credit 	<ul style="list-style-type: none"> ◆ Prefund unfunded loans to mitigate contingent liquidity risk ◆ Revolvers typically include covenants that prevent draws in distressed market events
“Match funding”	<ul style="list-style-type: none"> ◆ Integrated transaction on asset and liability side 	<ul style="list-style-type: none"> ◆ Asset and liability have self-funding and self-liquidating characteristics ◆ Structures reviewed on an individual basis

Cash Capital Sources

	Examples	Cash Capital Principle
Equity and long term debt	<ul style="list-style-type: none"> ◆ Equity ◆ Preferred and trust preferred ◆ Long term debt with remaining term > 1yr 	<ul style="list-style-type: none"> ◆ Limit amount of maturing debt over any rolling three, six and twelve month horizon (12.5%, 17.5% and 30.0% of total, respectively) ◆ If debt limits are exceeded, do not recognize excess as reliable liquidity ◆ Source diversity by limiting individual aggregate holdings to 5% of Lehman Brothers' total debt outstanding
Cash capital structures	<ul style="list-style-type: none"> ◆ Evergreen structures ◆ Non-extendible structures ◆ Structured notes 	<ul style="list-style-type: none"> ◆ Extendible secured and unsecured structures with terms > 1yr ◆ Structures with completely reliable funding with remaining terms > 1 yr
Restricted entity cash capital	<ul style="list-style-type: none"> ◆ Certificates of deposit ◆ Schuldschein 	<ul style="list-style-type: none"> ◆ Liabilities with insurance wrap
Committed facilities	<ul style="list-style-type: none"> ◆ Revolving credit facilities 	<ul style="list-style-type: none"> ◆ \$2.0 billion U.S. and \$2.5 billion European syndicated facilities ◆ Routinely drawn and repaid for working capital purposes ◆ Average utilization is 33-50% ◆ Included as a source only when drawn

 No reliance on hot money such as customer free credits or short term debt as a cash capital source

Contingent Liquidity Risk

- ◆ The Funding Framework is designed to set rules in order to protect the Firm in a stress liquidity environment. In a stress environment, whether Lehman-specific or market-wide, we plan for an increase in cash capital requirements due to
 - Unfunded loan commitments that get drawn due to a contraction in the market liquidity or due to a series of credit events impacting Lehman's banking clients
 - One-notch downgrade of Lehman's credit ratings
- ◆ The committed portfolio is very diversified across clients and industries, which is an effective liquidity risk mitigant
- ◆ To further mitigate the risk, the majority of loan commitments are booked in the bank entities
 - Best suited to handle commitment risk because of access to the insurance-protected deposit markets, the Central Bank and, in the case of the U.S. bank entities, FHLB borrowing windows
 - Additionally, the liquidity risk is prefunded with cash capital based on a quantitative assessment of the draw, which takes into account client ratings and industries
- ◆ A downgrade of Lehman's ratings would mechanically result in an increase in cash capital requirements – primarily due to additional cash collateralization of our derivatives receivables
 - The increase in funding requirements due to a one-notch downgrade is also funded with cash capital

Managing Secured Liquidity Risk

- ◆ Short term secured financing represents the largest source of secured funding for the Firm. Consequently, one key objective is to ensure that these funding sources are maintained in adverse market environments
 - Do not want to put Lehman Brothers in a position where a lack of liquidity results in an impairment of the franchise
- ◆ Manage secured liquidity using a four-pronged risk mitigation strategy, which conservatively assumes: (a) no reliance on Holdings' liquidity; (b) no reliance on customer collateral or free credits



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How Balance Sheet Is Funded

Funding 2008 Q2 Balance Sheet

	As of 5/31/08	Repo	Cash Capital	Banks ⁽¹⁾	Holdings' Liquidity Pool ⁽²⁾	Other Funding Sources
Cash and Cash equivalents	7		2		4	
Government & Agencies	27	22	1	3	2	
Commercial Paper & Other Money Mkt Instruments	5	3	1			
Mortgage and Asset-Backed Securities						
Commercial Mortgages	29		20	10		
Residential Mortgages	25		14	11		
Other Asset Backed Securities	7	3		3		
FAS 140 Gross Up	12					12 ⁽³⁾
Total Mortgage and Asset-Backed Securities	72	\$37bn of non Govies/ Agency repos	34	24		12
Real Estate Held For Sale	21		8	2		10 ⁽⁴⁾
Corporate Debt and Other						
Loans & other	32		25	8		
Bonds	18	2	14	1		
Total Corporate Debt and Other	50	2	39	9		
Listed equities and restricted equities	40	28	5	2		5 ⁽⁵⁾
Private equity	8		7	1		
Corporate equities	48	28	12	3		5
Derivatives and other contractual agreements	47		21	1		26 ⁽⁶⁾
Inventory Sub-total	269	59	115	41	2	53
Receivables	42			2		40 ⁽⁷⁾
Property, equipment and leasehold improvements	4		4			
Other assets	6		6			
TOTAL NET ASSETS	328	59	127	43	6	93
Cash and securities segregated	13					13 ⁽⁸⁾
Collateralized Lendings (Reverse repos & borrows)	295	84	3	2	39 ⁽⁹⁾	166 ⁽¹⁰⁾
Identified intangible assets and goodwill	4		4			
TOTAL ASSETS	639	143	135	45	45	272

1. Includes \$6 billion of cash capital (equity) provided by Holdings

2. Includes \$15 billion of cash capital surplus

3. Non-recourse financing on consolidated securitizations (securities sold to investors)

4. Non-recourse financing on consolidated real estate positions (third party financing)

5. Self-funded trades funded with short-term debt

6. Derivative payables (classified as short inventory)

7. Customer and other payables

8. Client cash (included in customer payables)

9. Primarily Government and Agency securities

10. Primarily Firm's short positions and FAS 140 Gross up

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Funding Projected 2009 Q4 Balance Sheet

	As of 11/30/09	Repo	Cash Capital	Banks	Holdings' Liquidity Pool ⁽¹⁾	Other Funding Sources
Cash and Cash equivalents	5		2	1	2	
Government & Agencies	57	50	2	3	2	
Commercial Paper & Other Money Mkt Instruments	5	3	1			
Mortgage and Asset-Backed Securities						
Commercial Mortgages	5		1	4		
Residential Mortgages	5		2	3		
Other Asset Backed Securities	4		2	2		
FAS 140 Gross Up						
Total Mortgage and Asset-Backed Securities	14	\$24bn of non Govies/ Agency repos	5	9		
Real Estate Held For Sale						
Corporate Debt and Other						
Loans & other	50		29	21		
Bonds	18		6	12		
Total Corporate Debt and Other	68		35	33		
Listed equities and restricted equities	36	21	12			3
Private equity	8		7	1		
Corporate equities	44	21	19	1		3
Derivatives and other contractual agreements	58		25	10		23
Inventory Sub-total	245	74	87	56	2	26
Receivables	40		4	3		33
Property, equipment and leasehold improvements	4		4			
Other assets	6		6			
TOTAL NET ASSETS	300	74⁽²⁾	103⁽³⁾	60⁽⁴⁾	4	59
Cash and securities segregated	13		-	-	-	13
Collateralized Lendings (Reverse repos & borrows)	282	79	11	7	40	145
Identified intangible assets and goodwill	4		4			
TOTAL ASSETS	600	153	118	67	44	217

1. Includes \$15 billion of cash capital surplus

2. \$50 billion shown in the Gameplan document = \$74 billion + \$6 billion of ECB repos shown in the Banks column

3. \$111 billion shown in the Gameplan document = \$103 billion + \$8 billion of capital provided by Holdings to the Lehman bank entities shown in the Banks column

4. \$45 billion shown in the Gameplan document = \$60 billion - \$6 billion of ECB repos - \$8 billion of capital provided by Holdings

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2008 Q3 Liquidity Update

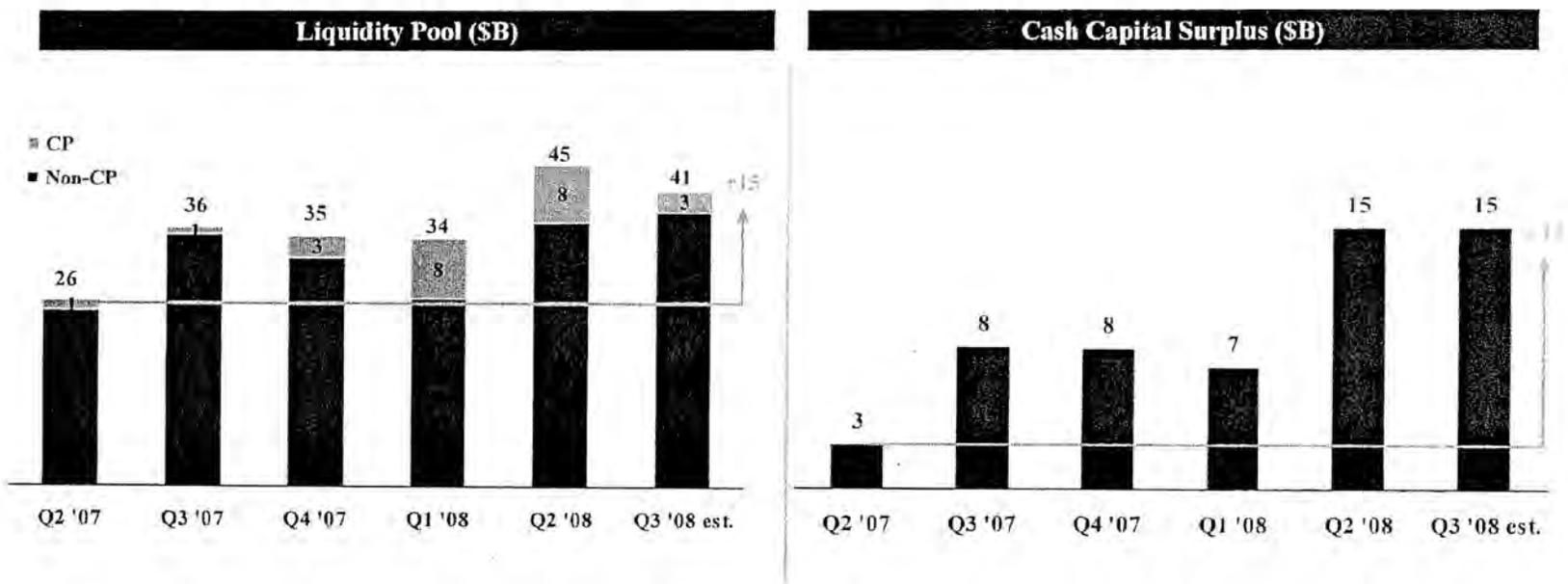
Overview

- ◆ Despite a challenging market environment, Lehman Brothers was able to maintain the status quo broadly in terms of liquidity – primarily as a result of deleveraging its balance sheet (which was done for risk reasons)
- ◆ Holdings' liquidity pool, adjusted for the reduction in our CP program, essential unchanged
- ◆ Cash capital surplus at Holdings projected to be unchanged
- ◆ Strength of the repo book as measured by average tenor and overfunding remained unchanged
- ◆ Lehman bank entities have been able to raise deposits thanks to their insurance protection. We expect to grow LBCB rapidly now that the “de novo” period has expired
- ◆ Looking forward, we face limited long-term debt refinancing risk: only \$19 billion of long-term debt is rolling into current portion over the next twelve months

Liquidity Pool and Cash Capital Surplus

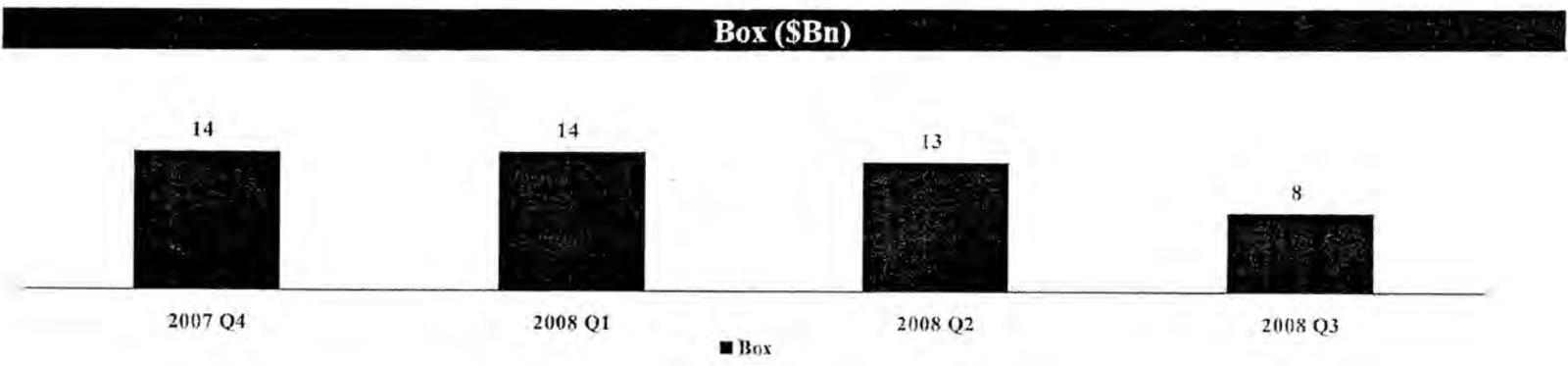
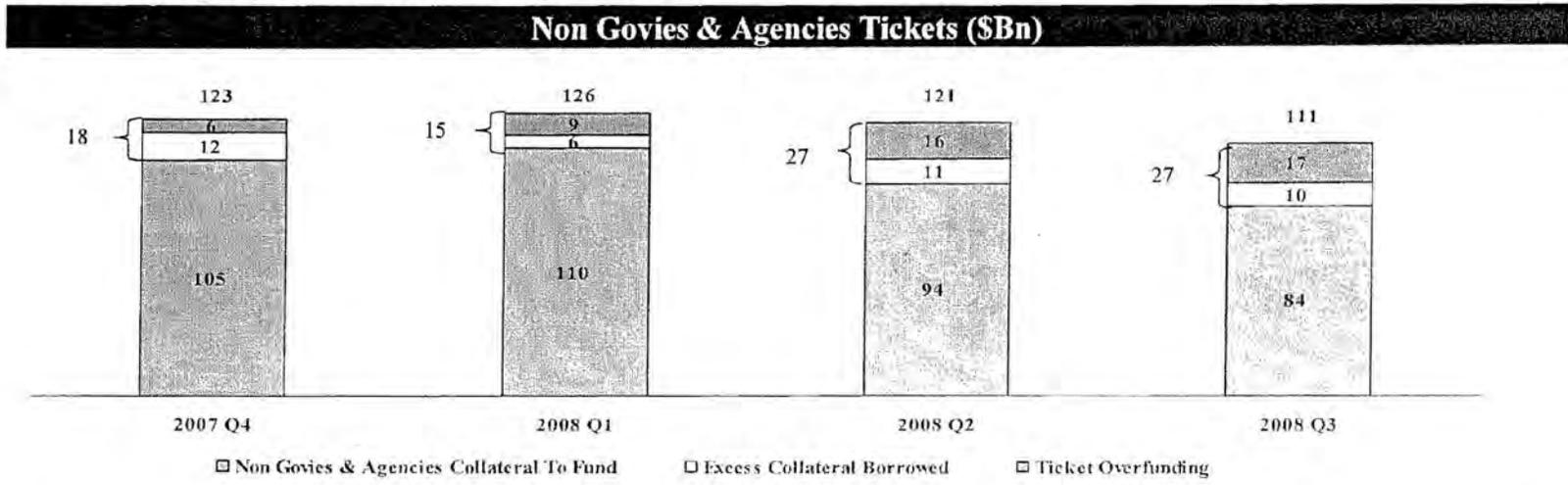
We have a \$41B liquidity pool and \$15B cash capital surplus at Holdings

- ◆ Since Q3 '07 when the funding environment became more challenging, we have grown our liquidity pool by \$15 billion and our cash capital surplus by \$12 billion
 - We will close Q3 '08 with an estimated liquidity pool of \$41 billion, roughly unchanged after adjusting for the reduction in our commercial paper outstanding. The ratio of liquidity pool to unsecured debt projected to mature within the twelve months stands at 147%.
 - Cash capital surplus will be near record levels of about \$15 billion at the end of Q3 '08



Reduction in Funding Requirements

Deleveraging of balance sheet during Q3 drove reduction in secured funding requirements. Overfunding remained stable at \$27 billion.

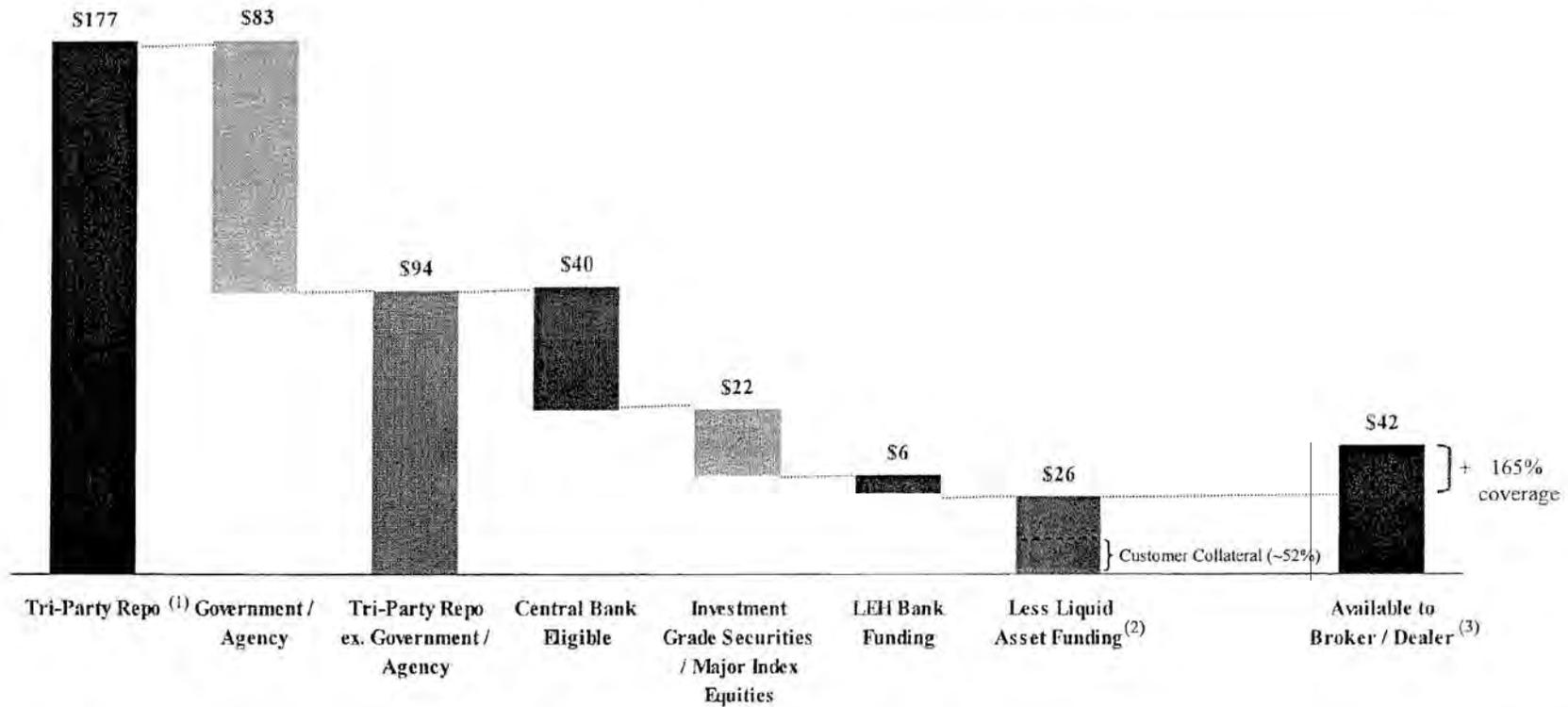


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Liquidity Risk Of Secured Funding

Liquidity risk of our secured funding continues well contained.

Tri-Party Repo Book Collateral - August 31, 2008 Projection (\$Bn)



Q2 '08:	\$188B	\$83B	\$105B	\$40B	\$24B	\$8B	\$33B	\$50B (+150% coverage)
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1. Gross exposure
 2. 28% of the \$26B is >1 month duration
 3. Includes Liquidity Pool (\$41B), Bankhaus (\$0.9B) and LBIE (\$1.3B)

Strength Of Secured Funding

Secured funding has remained very resilient during Q3 with significant overfunding of our tri-party repo book and term funding for non-central bank eligible collateral of greater than one month.

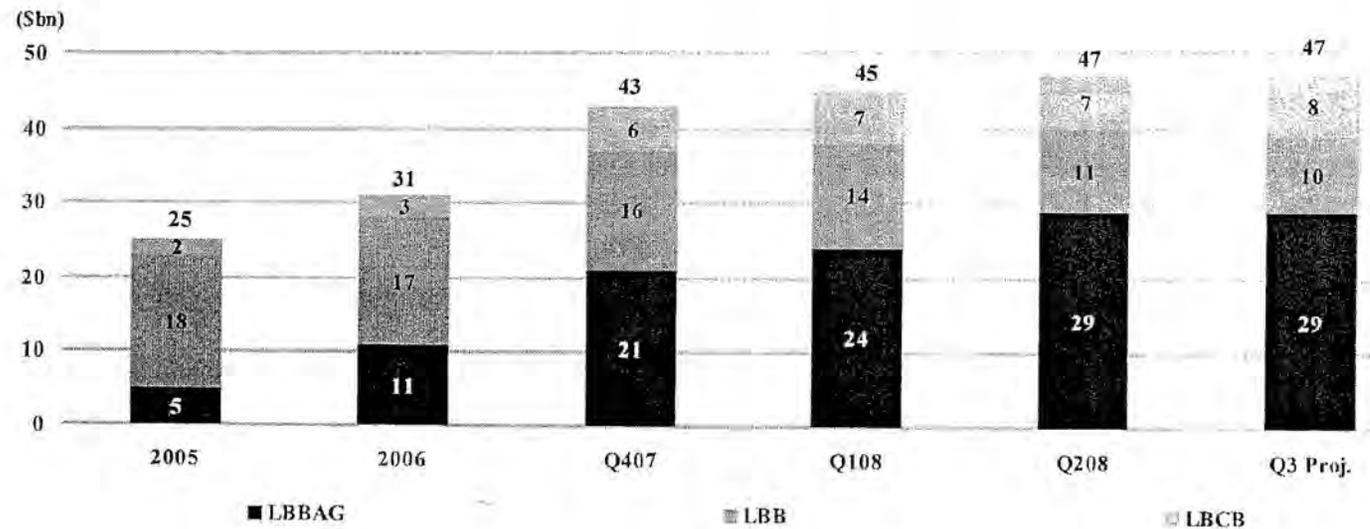
Non-Traditional ¹ Repo Book Metrics

Triparty Repo Book	Q407	Q108	Q208	Q308 Estimate	Q3 vs Q2 Change
Total Overfunding (\$B)	\$18	\$15	\$27	\$27	0%
Tickets	\$6	\$9	\$16	\$17	8%
Excess Collateral	\$12	\$6	\$11	\$10	-9%
Average tenor (days)	27	22	35	31	-4
Central bank eligible	-	-	30	25	-5
Non Central bank eligible	-	-	38	36	-2
% Overnight	52%	56%	42%	44%	2%
% <=1 week	13%	18%	12%	9%	-3%
% > 1 week	<u>35%</u>	<u>25%</u>	<u>46%</u>	<u>47%</u>	1%
% > 1 month	100%	100%	100%	100%	0%
	24%	20%	29%	29%	0%

Lehman Brothers Bank Entities

We project rapid growth of assets funded in LBCB (Utah-based Industrial Bank) in Q4 after the expiration of its “de novo” period. Bank funding has proved to be very resilient in this market environment.

Bank Entities Total Assets



Long-Term Debt Maturity Schedule

- ◆ We finish the quarter with a projected \$114 billion of long-term debt with an average life of approximately 7.5 years.
- ◆ We manage the debt refinancing risk by setting strict limits on the amount of long-term debt maturing within any quarterly (7.5%), half-year (12.0%) and full-year (20.0%) intervals
 - As of August 31, these limits are \$8.5 billion, \$13.7 billion and \$22.8 billion, respectively
 - If we were to operate above these levels, we would not include the excess amount as a source of cash capital
- ◆ We completed our 2008 refinancing plan at the end of Q2 and we do not need to issue more long-term debt for the rest of the year (although we may do so for opportunistic reasons)
- ◆ \$19 billion of long-term debt is projected to roll into current portion in the next twelve months
 - Expect to cover this refinancing through long-term debt issuance and growth of our bank entities

Long-Term Debt Maturity Schedule (\$ Bn)

	<u>Qtr</u>	<u>LTD</u>	<u>Extendibles</u>	<u>Total</u>	
11/30/2009	2009 Q4	5,480	477	5,957	} \$19.0 bn
2/28/2010	2010 Q1	3,232	84	3,317	
5/31/2010	2010 Q2	5,414	826	6,240	
8/31/2010	2010 Q3	3,323	116	3,439	
11/30/2010	2010 Q4	2,039	0	2,039	
2/28/2011	2011 Q1	3,041	0	3,041	
5/31/2011	2011 Q2	6,250	25	6,275	
8/31/2011	2011 Q3	3,107	59	3,166	
11/30/2011	2011 Q4	1,441	0	1,441	
2/29/2012	2012 Q1	4,625	0	4,625	
5/31/2012	2012 Q2	2,764	730	3,494	
8/31/2012	2012 Q3	5,746	0	5,746	
11/30/2012	2012 Q4	3,323	0	3,323	
2/28/2013	2013 Q1	5,092	0	5,092	
5/31/2013	2013 Q2	1,839	0	1,839	
8/31/2013	2013 Q3	2,616	0	2,616	
11/30/2013	2013 Q4	1,081	0	1,081	
2/28/2014	2014 Q1	4,147	0	4,147	
5/31/2014	2014 Q2	1,462	0	1,462	
8/31/2014	2014 Q3	1,403	0	1,403	
Total		67,426	2,318	69,744	
Mature after 2014Q3		44,091	0	44,091	
Grand Total		111,517	2,318	113,834	

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Lessons From The Bear Stearns Liquidity Event

Lehman Brothers Is Different From Bear Stearns

- ◆ Lehman Brothers had stronger liquidity metrics at the end of Q2 '08 than Bear Stearns at the end of Q1 '08
 - 30% greater balance sheet but 3 times its equity, post the \$6 billion June '08 capital raise
 - Bear Stearns' short-term debt stood at 1.5x its liquidity pool vs. 0.8x for Lehman Brothers
- ◆ Bear Stearns had very few unencumbered assets
 - Half of BSC STD was secured, which might have exacerbated the liquidity crisis in view of the exceptionally low amounts of unencumbered assets
- ◆ Bear Stearns was very reliant on customer free credit balances; if it lost these, it would need to quickly create substantial secured funding capacity for equities at a time when lenders would be likely to pull away
- ◆ Bear Stearns had almost no margin for error in terms of liquidity management. A reduction in short-term debt or in customer free credit balances would leave it in a precarious liquidity position

Key Liquidity Metrics (\$ Billions)

	2008 Q1	2008 Q2	LEH / BSC
	Bear Stearns	Lehman Brothers	
Net balance sheet	254	328	1.3x
Tangible equity ⁽¹⁾	11	33	3.0x
Net leverage ⁽¹⁾	22.6x	9.9x	0.4x
Liquidity pool	17	45	2.6x
STD excluding current portion	16	14	0.9x
Current portion of LTD ⁽²⁾	10	21	2.1x
Total short-term debt	26	35	1.4x
Short-term debt / Liquidity pool	1.5x	0.8x	0.5x
Unencumbered assets (unregulated chain)	5	61	13.5x
Total unencumbered assets	14	148	10.3x
Free credit balances	43	8	0.2x

1. Tangible equity and net leverage for LEH are proforma for the June 2008 \$6 billion capital raise

2. BSC current portion of LTD was not reported for 2008 Q1. Data is estimated based on 2007 Q4 data

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Liquidity Event Of Week Of March 17 (I) – Broker Dealers

- ◆ During the week of March 17, Lehman Brothers was under significant funding pressure, which we were able to mitigate through a series of actions
 - Secured Funding
 - We started the week with \$13 billion of repo overfunding in harder to fund asset classes
 - We also funded an additional \$4.5 billion of collateral through Bankhaus where we have been building excess capacity since the summer of 2007
 - Prime Broker
 - We absorbed the loss in prime broker cash balances by relying on the LBIE “excess” liquidity pool (which, because it was “trapped,” was not included in the LBHI liquidity pool) and by recalculating the lock up on a daily basis
 - LBI experienced a very modest (\$75 million) loss of liquidity in prime broker cash balances that week.
- ◆ As a result, the loss of liquidity experienced by the broker dealers was absorbed within the broker dealers and did not require the use of the Holding Company liquidity pool

Key Liquidity Inflows/Outflows During Week Of March 17 (\$ Billions)

	Secured Funding			Prime Broker (LBIE)		
	Decreases	Increases/ Upgrades	Balance	Decreases	Increases	Balance
17-Mar	(8.7)	3.2	(5.5)	(5.0)	0.8	(4.2)
18-Mar	(3.8)	-	(3.8)	(2.7)	2.8	0.1
19-Mar	(3.0)	5.1	2.1	(1.2)	1.5	0.3
20-Mar	-	-	-	(1.2)	1.1	(0.1)
21-Mar	Market Closed (Good Friday)					
Total	(15.5)	8.3	(7.2)	(10.1)	6.2	(3.8)
Mitigation strategy						
Overfunding repo book	2.7			LBIE excess liquidity pool	3.8	
Bankhaus funding	4.5					
Total	7.2					
"Dry powder" : Overfunding repo book	~10					

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Liquidity Event Of Week Of March 17 (II) – Holdings

- ◆ Holdings also faced funding pressure – primarily due to the reduction of its commercial paper program and, to a lesser extent, the posting of derivative margins
- ◆ We mitigated this loss of liquidity by:
 - Increasing operational effectiveness: we executed on a plan developed over the weekend to reduce the amount of trapped cash in LBI and increase funding in Bankhaus. These actions generated approximately \$3 billion on March 17
 - Launching the Freedom CLO and executing a previously planned European securitization
 - Drawing on our European committed facility. We draw on our committed facilities 33-50% of the time to avoid any signaling effect

Key Liquidity Inflows/Outflows During Week Of March 17 (\$ Billions)

	Commercial Paper			O/S (EOD)	Derivatives	Operational	Other	LBHI Liquidity Pool			Other Details
	Maturities	Issued	Balance		in/(out)flows	effectiveness		SOD	EOD	Change	
				Balance	Balance	Balance					
17-Mar	(6.2)	2.2	(4.0)	7.9	(0.0)	3.0	0.0	31.1	30.1	(1.0)	
18-Mar	(3.2)	3.7	0.5	8.4	(1.2)	(0.4)	(0.1)	30.1	28.9	(1.2)	
19-Mar	(3.5)	3.3	(0.2)	8.2	0.9	-	0.7	28.9	30.3	1.4	European mortgage securitization
20-Mar	(3.1)	3.4	0.3	8.5	(1.0)	-	3.1	30.3	32.7	2.4	Draw on committed facility, Freedom
21-Mar					Market Closed	(Good Friday)					
Total	(16.0)	12.6	(3.4)		(1.3)	2.6	3.7	31.1	32.7	1.6	

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