

UBS Investment Research

Lehman Brothers

Lehman Has Options, Albeit Costly Ones

■ Serious Issues, But Some Options Exist

While LEH certainly has some major issues it is dealing with (the biggest being asset exposures & potential client erosion), we think the company has a few options (albeit some costly ones), that management can exercise to help get them out of this dilemma and eventually get the company on the path to recovery. We think the most likely are a sizable asset sale and maybe a sale of Neuberger.

■ Keys Are Protecting Client & Employee Franchise & Avoiding Fire Sale

While clients & employees are nervous, from what we can tell, there's only been modest erosion at this point. Importantly, we think Lehman has more staying power given the existence of the Fed facility, its healthy liquidity profile, strong capital ratios, and the fact that repo counterparties have held firm.

■ Time is Not on Their Side, and A Sizable Asset Sale Has Its Costs

Still, the longer the concerns about the firm's viability linger, the pressures on the client franchise will likely intensify. In our view, mgmt needs to do something meaningful in the near term to change perceptions. While a sizable asset sale would remove some risk from LEH's balance sheet, it would also generate a pretty big hit to book value (not sure on another capital raise), so there is no free lunch.

■ Valuation: Issues & Unknowns Keep Us At Neutral

Given the remaining risk exposures, unknowns around the costs of a large asset sale, the weak macro backdrop, and the limited time horizon we continue to be Neutral. Our price target goes to \$22 from \$32, based on 0.7x our forward book value estimate.

Highlights (US\$m)	11/06	11/07	11/08E	11/09E	11/10E
Revenues	17,583	19,257	11,077	18,068	19,612
Pre-tax profits	5,605	5,713	(1,782)	4,876	5,628
Net income	3,641	3,825	(1,440)	3,113	3,625
EPS (UBS, US\$)	6.81	7.25	(2.84)	4.00	4.60
Net DPS (UBS, US\$)	0.48	0.60	0.68	0.76	0.84

Profitability & Valuation	5-yr hist av.	11/07	11/08E	11/09E	11/10E
ROE %	-	20.1	-3.5	10.2	10.7
P/Op x	11.1	9.7	NM	5.0	4.4
P/BVPS x	1.7	1.8	0.6	0.6	0.5
PE (UBS) x	11.1	9.7	-7.1	5.0	4.4
Net dividend yield %	0.6	0.9	3.4	3.8	4.2

Source: Company accounts, Thomson Financial, UBS estimates. (UBS) valuations are stated before goodwill-related charges and other adjustments for abnormal and economic items at the analysts' judgement.

Valuations: based on an average share price that year, (E): based on a share price of US\$20.20 on 22 Jul 2008 16:58 EDT

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Global Equity Research

Americas

Investment Services

12-month rating **Neutral**
Unchanged

12m price target **US\$22.00**
Prior:US\$32.00

Price **US\$20.20**

RIC: LEH.N BBG: LEH US

23 July 2008

Trading data

52-wk range	US\$67.66-12.40
Market cap.	US\$11.3bn
Shares o/s	559m (COM)
Free float	97%
Avg. daily volume ('000)	8,830
Avg. daily value (US\$m)	240.9

Balance sheet data 11/08E

Shareholders' equity	US\$33.3bn
P/BVPS x	0.6
Tier one capital ratio	-

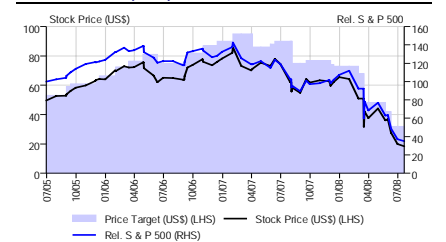
Forecast returns

Forecast price appreciation	+8.9%
Forecast dividend yield	3.7%
Forecast stock return	+12.6%
Market return assumption	7.6%
Forecast excess return	+5.0%

EPS (UBS, US\$)

	11/08E		11/07	Actual
	From	To	Cons.	
Q1	-	0.81	0.81	1.96
Q2	-	(5.14)	(5.14)	2.21
Q3E	-	0.61	0.27	1.54
Q4E	-	0.87	0.64	1.54
11/08E	-	(2.84)	(3.70)	
11/09E	-	4.00	3.68	

Performance (US\$)



Source: UBS

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This report has been prepared by UBS Securities LLC

ANALYST CERTIFICATION AND REQUIRED DISCLOSURES BEGIN ON PAGE 9.

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LEH Has Options (But It'll Cost Them Some)

While Lehman certainly has some major issues it is dealing with, we think the company has a few options (albeit some costly ones), that management can exercise to help get them out of this dilemma and eventually get the company on the path to recovery. In our view, while the issues are tough, we don't think that the worst case scenario of a major client exodus and/or a forced asset liquidation comes to fruition. The problem is that time is not on their side and a significant reduction in the key illiquid asset buckets, as painful as it might be in this environment, is probably Lehman's best risk-adjusted path out (it's not like no clients have pulled or a bunch more aren't nervous). Just so we're clear, we think there is some possibility that Lehman can muddle through this for the next year or two (only if the market bails them out) as it works through its balance sheet issues and maintains the client/employee franchise, but given our reasonably somber macro view, there is also a chance that if they try that route, the credit markets and macro environment can continue to work against them and make the situation worse (the past week or so has been kind to financial stocks, but it's hard to bet the company's future on that continuing).

In our view, the main issues at this point are Lehman's remaining "problem" asset exposures, the related fears over Lehman's client franchise (which get amplified by the drop & volatility in its stock), the less than favorable macro backdrop, and lingering concerns over the future structure of the industry (and where Lehman fits in). While each broker faces these issues on some level, the asset concentration issues are more acute at Lehman at this point (well, Merrill's is pretty tough too), and the company unfortunately has to be concerned about perception becoming reality when it comes to protecting its client franchise. To that end, while clients and employees are nervous, from what we can tell, there's only been modest client erosion at this point. Importantly, we think Lehman has more staying power given the existence of the Fed facility, the company's healthy liquidity profile, strong capital ratios, and the fact that repo counterparties have held firm despite the pressure on Lehman's stock. Given that we don't see Lehman facing a massive liquidity crisis, we have a hard time coming up with a catalyst which would force liquidation of assets at fire sale prices. Still, given the real issues facing Lehman on the exposure side we think the firm could have some tough sledding ahead and it is tough to think that there is much new business coming in the door given the distractions around the stock price and senior management's attention being drawn away from business as usual (combined with seasonality and still tough credit markets, don't expect a great 3Q).

That being said, we think Lehman has a handful of potential scenarios it is working on which could alleviate the current pressure, but as with most things in life, timing is critical. We think the potential scenarios for Lehman are as follows: 1) Sell a significant block of risk assets (north of \$30 billion); 2) Sell the whole firm; 3) Take the firm private; 4) Sell/IPO Neuberger Berman; 5) Announce a strategic partnership with a very credible partner; 6) Announce a meaningful share buyback. In our view, while we discuss each scenario later, we feel the most likely scenario is the sale of a large block of risky assets, possibly in concert with the sale of Neuberger as a way to partially plug any hit to book value realized on the asset sale (in all fairness, it's possible that Neuberger

actually pushes this to happen) to possibly avoid another capital raise. A significant asset disposal would alleviate a chunk of the concerns around the balance sheet, though we think the haircut realized on the sale would likely be significant given the likely size of the sale and illiquidity of the pool (on page 5, we run through some scenarios that show impacts to capital ratios and book value on some pretty sizeable asset sales with some pretty large exit costs).

In our view, the transaction could be an outright sale, or some form of a structured transaction where Lehman could even provide financing to the buyer of the assets as a possible way to offset some of the hit on price or to entice a wider set of bidders. We think the most important factor here is that the transaction would be focused on removing a big chunk of risky assets from Lehman's books. In our view, we think this needs to happen in weeks and not months as there could be an increasing supply of risk assets coming into the market as other financial firms look to offload risk as well. While a significant hit to equity from a sizable asset sale would bring book value down meaningfully, we think the market has largely priced this into Lehman's shares. At the same time, we think Lehman's capital ratios (13.5% pro forma Tier 1 for what it's worth) would remain on very solid footing even after assuming a sizable hit to Tier 1 capital, so we don't think an additional capital raise would necessarily have to happen along with this scenario.

Adding it all up, while the stock appears very cheap on a historical basis and any traditional valuation range (currently at 0.6x book or 0.75x tangible book) and we believe that Lehman will eventually work its way through its issues, given the remaining risk exposures/potential further write-downs, the unknowns around a potential asset sale, the weak macro backdrop and limited time horizon, we continue to be Neutral on the shares. We are cutting our price target for LEH to \$22 from \$32, based on 0.7x our forward book value, down from 1.0x, acknowledging the reality that Lehman certainly seems to have some options, but that they likely come at a steep price.

We Don't Foresee a Forced Liquidation

It seems at times that the market is pondering whether Lehman will remain a going concern and whether the firm will need to sell itself, or a large chunk of its assets in short order (when there's no liquidity) in an attempt to survive. While we understand the mindset after living through Bear and actually do think a sizeable asset disposal is Lehman's best ticket out, we have a hard time envisioning how a forced asset sale situation could be pushed upon the company. Specifically, we think the likelihood of a forced liquidation scenario is relatively remote given the existence of the Fed's Primary Dealer Credit Facility, Lehman's healthy capital position (\$12 billion of equity raises versus net losses of \$2.8 billion and 13.5% pro forma Tier 1 ratio), the firm's liquidity profile (\$45 billion at the parent company), the fact that there has been only what we'd call tolerable client slippage so far, and that the large bank & investment bank peers are unlikely to pull repo & trading lines (given that they're all in this together at this point and the regulators would rather not re-live the Bear scenario). One final point on liquidity: Lehman has been over funding its repo agreements and termed out its non-government/agency repo agreements to 35 days and completed its long-term debt financing needs for the rest of 2008, which should take additional pressure off of near-term liquidity concerns.

Client Franchise is Lehman's Linchpin

While it is difficult to see through all the noise around charge-offs/illiquid asset exposures and we don't get a glimpse at the daily P&L, we do think Lehman's historically strong client franchise is showing a few signs of stress, but remains reasonably intact as clients continue to trade with the firm and look to them for expertise in many product areas. For what it's worth, we're trying to balance the tough reality the company is facing, without losing sight of the fact that Lehman has built out a great equities franchise and strong banking platform globally, in an effort to balance its traditionally dominant fixed income platform – and remember, a good chunk of this business is DVP (delivery vs. payment), so even nervous clients can potentially stick around to see how this situation plays out without having much counterparty risk (prime brokerage, clearing, OTC derivatives and maybe even asset management could be another story).

To that end, while we saw visible client and asset slippage in prime brokerage, clearing, derivatives and asset & wealth management at Bear in the late days, we've only seen spotty occurrences to this point at Lehman. (FYI, while there's little doubt in our minds that clients are nervous, we do think this is a better and more diverse franchise with deeper relationships, besides a more protected balance sheet). In addition, run rate revenues of \$4.2 billion in 2Q (ex charge-offs & gains), though down from the roughly \$5 billion quarterly run rate over the previous year, are still fairly healthy given that 2Q saw a slow down in client activity across the board. While some investors were a little spooked by the 17% y/y decline in prime brokerage balances this past quarter, we do think a portion of this is attributable to Lehman's issues, but plenty is likely related to deleveraging in the market and a little related to Lehman's client segmentation efforts. Putting it all together, yes, revenues will likely slow for everyone in 3Q given seasonality & market concerns, but the point is that clients, while no doubt nervous, have mostly stuck by Lehman's side.

Market Continues to Question Asset Exposures & Marks

As great as Lehman's track record is, the company got caught owning too many illiquid assets relative to the size of its equity base when the music stopped. Maybe most importantly, we think time isn't on Lehman's side and investors would like to see a sizeable asset disposal in short order in an effort to remove the risk of a run on the client franchise (whether it be an outright sale or some form of a structured transaction shouldn't matter). Given our overall negative view on the credit, economic and capital markets backdrop, we do think that Lehman's remaining "problem" exposures (\$83 billion across residential and commercial mortgage, real estate, other ABS, and leveraged loans) will continue to weigh on the shares and likely lead to further write-downs as the credit crisis drags on. In addition, we think there are some legitimate questions around the future worth of some of Lehman's chunkier real estate related exposures such as Archstone (\$1.8 bn in equity marked at 75 cents & \$2.5 bn in debt marked between that and par) and SunCal (\$1.6 billion marked in the 70-75 cent range).

To be fair, while the remaining exposures are large, we would note that Lehman has taken \$17 billion of gross marks across the portfolios since the beginning of 2007 and it seems like they are the only firm that has taken any meaningful hits against their commercial real estate book thus far. In addition, with the

exception of 2Q08 when hedges broke down, Lehman has done a reasonable job offsetting the bulk of its negative asset marks with hedge gains and we think these hedges are likely working a bit better so far in 3Q given the declines in some of the synthetic credit indices. Still, given that risk exposures are 2.6x stockholders' equity or 2.9x tangible equity (yes, we know these numbers are not that different than Merrill's) we think the market will continue to keep a lid on Lehman's share price. At the end of the day, we're not saying that we know the intrinsic value of the underlying "problem assets", just that Lehman likely doesn't have the luxury of time in order for us all to wait and find out. In our view, until Lehman actually sells down this exposure or markets rebound (don't hold your breath), pressure will remain on the stock.

Capital & Liquidity Ratios Should Be Able To Handle an Asset Sale

Given that we think an asset sale is the most likely scenario, the tables below walk through the potential impact on book value per share and also Lehman's Tier 1 ratio in the event of a large asset disposition. To be clear, given that we have very little color on the individual asset exposures, individual marks, and what the individual exit costs would be, the scenarios below are our best guesstimates. The basic takeaway is that while we think a significant asset sale would cause a major negative hit to book value, Lehman's Tier 1 ratio and leverage ratios would likely remain in pretty good shape given its strong starting point, and the firm's overall risk profile would improve materially. For example, if Lehman were to sell \$40 billion of risk assets and realize a 30% haircut, this would result in a pretax loss of \$12 billion or an after-tax hit to book of roughly \$8 billion. In this scenario, book value per share would decline to roughly \$22 from \$33, but Lehman's Tier 1 ratio would remain a pretty solid 12.0%, putting it second only to Morgan Stanley. This would also leave Lehman with a much more manageable \$43 billion of risk assets and risk exposures would fall to 1.8x stockholders' equity from its current level of 2.6x. Still, it is unclear what assets would get sold and what the risk profile of what the remaining exposures would be.

Table 1: Asset Sale Scenario Impact on Book Value

Notable Asset Exposures	5/31/2008		
	Value (\$ bil)		
Senior Commercial Real Estate Loans	\$19.5		
Mezzanine Commercial Real Estate Loan	\$5.9		
Commercial Real Estate Equity	\$7.2		
Archstone Equity	\$1.8		
Archstone Debt	\$2.5		
SunCal	\$1.6		
Alt-A	\$10.2		
UK Residential Mortgage	\$9.3		
Other ABS	\$6.5		
Leveraged Loans	\$11.5		
Scenarios	1	2	3
Asset Sale (\$ bil)	\$40	\$40	\$40
% Haircut on Assets	25%	30%	35%
Pretax Loss (\$ bil)	\$10	\$12	\$14
After-Tax Loss (\$ bil)	\$7	\$8	\$9
Current Book Value Per Share	\$33	\$33	\$33
Adjusted Book Value Per Share	\$24	\$22	\$20

Source: Company financials and UBS estimates

Table 2: Asset Sale Scenario Impact on Tier 1

Decrease in Tier 1 Capital (\$ bil)	Decrease in Risk Weighted Assets (\$ bil)			
	\$20	\$30	\$40	\$50
\$4	12.8%	13.5%	14.3%	15.1%
\$6	11.8%	12.4%	13.1%	13.9%
\$8	10.8%	11.4%	12.0%	12.7%
\$10	9.8%	10.3%	10.9%	11.5%

Lehman's Estimated Tier 1 Ratio

Source: UBS estimates

Possible Scenarios

As mentioned above, we think management is not going to rest on its laurels and hope the company can muddle through its issues over the next year or two – there's just way too much at stake. As such, we think there are a handful of potential scenarios that Lehman could be working on, with the most likely outcome being some combination of a significant reduction in the company's illiquid assets and potentially a monetization of Neuberger Berman. In our view, going private, an outright sale of the company and selling a stake to a strategic investor are not likely outcomes and wouldn't fully address Lehman's issues. Nonetheless we talk through the list of options below:

- (1) **Significant Asset Sale:** We think this scenario is the most feasible and the most likely outcome given Lehman-specific issues and the current state of the financial markets. Lehman could arrange to offload a sizable slug of its risk assets to a distressed buyer, and while this action would likely cause a meaningful realized loss on the assets (given today's limited liquidity and wide bid/ask spreads), it would remove or at a minimum severely dull the most significant issue hanging over the company at the moment. Unfortunately, this type of transaction would also take some time to put together (especially considering the granularity of the commercial real estate portfolio), but we feel pretty confident that senior management is actively looking at its alternatives and this is probably near the top of the priority list. While some critics might say that Lehman would be giving away any potential upside of the assets it sells, we think that right now the firm needs to focus on survival and can then go back to focusing on generating attractive returns. On that note, given Lehman's healthy capital ratios, management could actually start thinking about reinvesting at some point following this significant de-risking of the balance sheet and freeing up of capital. That being said, trying to make a guesstimate on how much assets Lehman needs to sell and how big of a haircut they would need to take is extremely difficult (see our scenario analysis above).

- (2) **Sell Neuberger Berman:** Given the pressures, we wouldn't be surprised to see senior management at Neuberger push for some type of a spin off, MBO or an outright sale as a way to realize value for employees and distance themselves from the balance sheet problems at Lehman. Timing isn't great (for Lehman or to maximize value), but it is what it is and there are both positives and drawbacks to such a transaction. On the positive side, Neuberger is a very valuable asset that's worth something over half of Lehman's current market cap (really depends on how you define it -- legacy Neuberger, include Lehman asset management?, include the private client business?). Anyway, whether it's a sale, MBO or IPO, we think there's value there and Lehman could use the proceeds/gain (LEH paid \$2.6 billion for Neuberger in 2003) to fund an asset disposition program and stack the deck against having to raise additional capital at any point. On the flip side, we are not sure how the rating agencies would feel about Lehman selling its largest annuity-like business (we think Merrill ran into this issue when looking at possibly selling its BlackRock stake) and we also think that investors and counterparties might have concerns if Lehman became a pure play investment bank, still exposed to a meaningful amount of risk assets (meaning any hypothetical sale has to coincide with the reduction of risk assets).
- (3) **Sale of the Firm:** Another option is selling the entire firm, which would certainly remove the downward pressure on the stock and also remove the distractions facing senior management. However, we have to believe that this is just about last on management's priority list given valuation, integration issues and most importantly, they'd be potentially giving up control of this great firm they've built over the past 10-15 years. Besides, timing isn't that great as many of the larger financial firms that would theoretically be interested have serious balance sheet issues of their own. In addition, while this might be a stretch, we think that a potential bidder is implicitly saying that they are somewhat comfortable with the assets on Lehman's books and where they are marked. If correct, we wonder if potential buyers might instead choose to buy similar assets from a distressed seller (or Lehman) and avoid taking on the franchise risk, going concern issues and integration headaches.
- (4) **Go Private:** Similar to selling the entire firm, this scenario takes pressure off the stock price and also alleviates the distractions of a public currency getting whipped around by market psychology. That being said, we think there are several reasons why this type of arrangement would not work. First, we go back to funding....where's it gonna come from? We're talking about getting levered money, to go out and by an already levered entity – sounds like a tough transaction to finance in this market. Also, we are not so sure can you be a large global broker dealer without attaining financing via the capital markets, and being a private entity would make it more difficult for counterparties and rating agencies to conduct the type of credit analysis they would probably like in order to maintain a certain level of comfort. In addition, there is an issue with buying out your employees' equity stakes at a price well below book value, so perhaps some promise of higher comp and a future IPO would be needed, which could hurt the profitability of the investment. In addition, we think a firm's ability to

compete effectively in prime brokerage or something like the long-dated swaps business would be severely restricted. Bottom line, we don't see how this scenario could be pulled off.

- (5) **Announce a Strategic Partnership or JV with a Credible Partner:** While a say 20%/25% investment by a credible investor could potentially help on the perception front, with all due respect, we think it'll take a pretty "real" investor with some strategic relevance given the previous investments made by the "smart money" in some of the distressed financials. As Lehman's capital ratios are solid and management talked about this as a potential opportunity (albeit that they could buy the shares in the open market given all the activity), we actually think it might be a decent call to raise the cash and use it to de-lever the balance sheet.
- (6) **Announce a Meaningful Share Buyback:** While capital is in decent shape with a pro forma Tier 1 of 13.5% and a Neuberger sale would only improve it, and this would possibly give the shares a short-term boost, we think investors would ultimately view this as a poor use of precious capital given all the issues facing Lehman, so we don't think this is anywhere near the top of management's list (or rating agencies).

■ Lehman Brothers

Lehman Brothers is an international investment bank based in New York that offers services to institutions and high net worth individuals in the United States and worldwide. Lehman was spun off from American Express in 1994 as an independently owned company listed on the NYSE. The Company has three primary business segments: investment banking, capital markets and client services.

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UBS Investment Research: Global Equity Rating Allocations

UBS 12-Month Rating	Rating Category	Coverage ¹	IB Services ²
Buy	Buy	57%	38%
Neutral	Hold/Neutral	36%	35%
Sell	Sell	8%	29%
UBS Short-Term Rating	Rating Category	Coverage ³	IB Services ⁴
Buy	Buy	less than 1%	31%
Sell	Sell	less than 1%	38%

1:Percentage of companies under coverage globally within the 12-month rating category.

2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.

3:Percentage of companies under coverage globally within the Short-Term rating category.

4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

Source: UBS. Rating allocations are as of 30 June 2008.

UBS Investment Research: Global Equity Rating Definitions

UBS 12-Month Rating	Definition
Buy	FSR is > 6% above the MRA.
Neutral	FSR is between -6% and 6% of the MRA.
Sell	FSR is > 6% below the MRA.
UBS Short-Term Rating	Definition
Buy	Buy: Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.
Sell	Sell: Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.

KEY DEFINITIONS

Forecast Stock Return (FSR) is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months.

Market Return Assumption (MRA) is defined as the one-year local market interest rate plus 5% (a proxy for, and not a forecast of, the equity risk premium).

Under Review (UR) Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation.

Short-Term Ratings reflect the expected near-term (up to three months) performance of the stock and do not reflect any change in the fundamental view or investment case.

EXCEPTIONS AND SPECIAL CASES

UK and European Investment Fund ratings and definitions are :

Buy: Positive on factors such as structure, management, performance record, discount; Neutral: Neutral on factors such as structure, management, performance record, discount; Sell: Negative on factors such as structure, management, performance record, discount.

Core Banding Exceptions (CBE) : Exceptions to the standard +/-6% bands may be granted by the Investment Review Committee (IRC). Factors considered by the IRC include the stock's volatility and the credit spread of the respective company's debt. As a result, stocks deemed to be very high or low risk may be subject to higher or lower bands as they relate to the rating. When such exceptions apply, they will be identified in the Company Disclosures table in the relevant research piece.

Company Disclosures

Company Name	Reuters	12-mo rating	Short-term rating	Price	Price date
Lehman Brothers ^{2, 4, 6a, 6b, 7, 16, 22}	LEH.N	Suspended	N/A	US\$18.32	21 Jul 2008

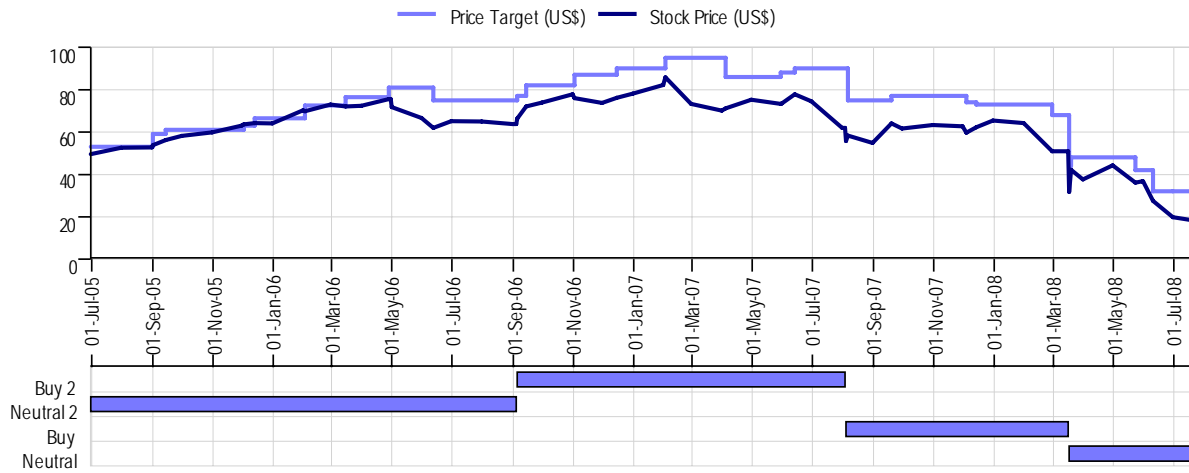
Source: UBS. All prices as of local market close.

Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date

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- 6b. This company/entity is, or within the past 12 months has been, a client of UBS Securities LLC, and non-securities services are being, or have been, provided.
7. Within the past 12 months, UBS Securities LLC has received compensation for products and services other than investment banking services from this company/entity.
16. UBS Securities LLC makes a market in the securities and/or ADRs of this company.
22. UBS AG, its affiliates or subsidiaries held other significant financial interests in this company/entity as of last month`s end (or the prior month`s end if this report is dated less than 10 working days after the most recent month`s end).

Unless otherwise indicated, please refer to the Valuation and Risk sections within the body of this report.

Lehman Brothers (US\$)



Source: UBS; as of 21 Jul 2008

Note: On August 4, 2007 UBS revised its rating system. (See 'UBS Investment Research: Global Equity Rating Definitions' table for details). From September 9, 2006 through August 3, 2007 the UBS ratings and their definitions were: Buy 1 = FSR is > 6% above the MRA, higher degree of predictability; Buy 2 = FSR is > 6% above the MRA, lower degree of predictability; Neutral 1 = FSR is between -6% and 6% of the MRA, higher degree of predictability; Neutral 2 = FSR is between -6% and 6% of the MRA, lower degree of predictability; Reduce 1 = FSR is > 6% below the MRA, higher degree of predictability; Reduce 2 = FSR is > 6% below the MRA, lower degree of predictability. The predictability level indicates an analyst's conviction in the FSR. A predictability level of '1' means that the analyst's estimate of FSR is in the middle of a narrower, or smaller, range of possibilities. A predictability level of '2' means that the analyst's estimate of FSR is in the middle of a broader, or larger, range of possibilities. From October 13, 2003 through September 8, 2006 the percentage band criteria used in the rating system was 10%.

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