Securitized Products Weekly Call

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Overview

IndyMac Loan Modification Program – Details and Implications

DIAL-IN and REPLAY INFORMATION

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Access Code:	**1255508**
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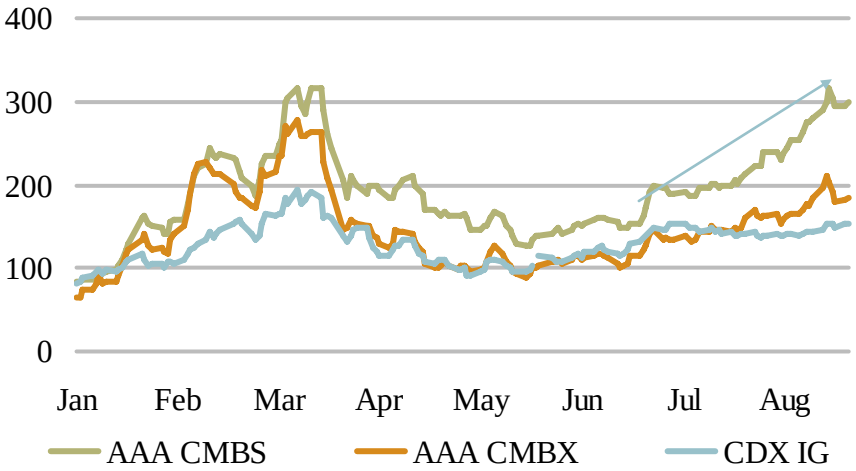
August 27, 2008

PLEASE SEE ANALYST CERTIFICATIONS AND IMPORTANT DISCLOSURES ON SLIDE 21

LEHMAN BROTHERS

Weekly Recap: Further Widening in CMBS

CMBS Spreads versus Other Sectors



Notable Events

8/20	MBA Purchase Index falls to lowest level since 2002
8/20	FDIC announces intent to modify loans serviced by Indymac
8/25	Existing home sales at 5 million units, inventories at 11.2 months of supply
8/26	July new home sales rose 2.4% month-over-month
8/26	Case-Shiller 20-city composite drops 6% annualized
8/26	FDIC announces problem list increased to 117 banks

Source: Lehman Brothers, Markit

Market Monitor

	8/26	7/31	6/30	5/30	3/31
2y Treasury	2.35	2.53	2.63	2.64	1.57
10y Treasury	3.78	3.98	3.98	4.06	3.43
5y Swap Spread	100	92	98	85	92
LBOX (bp)	103	100	107	99	105
CC LOAS (bp)	69	69	43	34	49
Jumbo Basis	18-24+	11-11	7-16	6-05	12-09+
Alt-A SS Basis	35-09	33-11	19-16	18-10+	20-09+
07-1 AAA	48.5	47.8	49.2	58.1	56.3
07-1 BBB	5.0	5.0	5.1	5.0	9.8
06-1 AAA	89.2	88.9	91.8	94.0	89.5
06-1 BBB	9.2	9.8	9.7	11.7	17.8
CMBS AAA SD	300	240	197	145	190
CMBS AJ	645	535	450	420	580
CDX.IG	144	132	140	108	143
CDX.HY	723	693	674	585	684

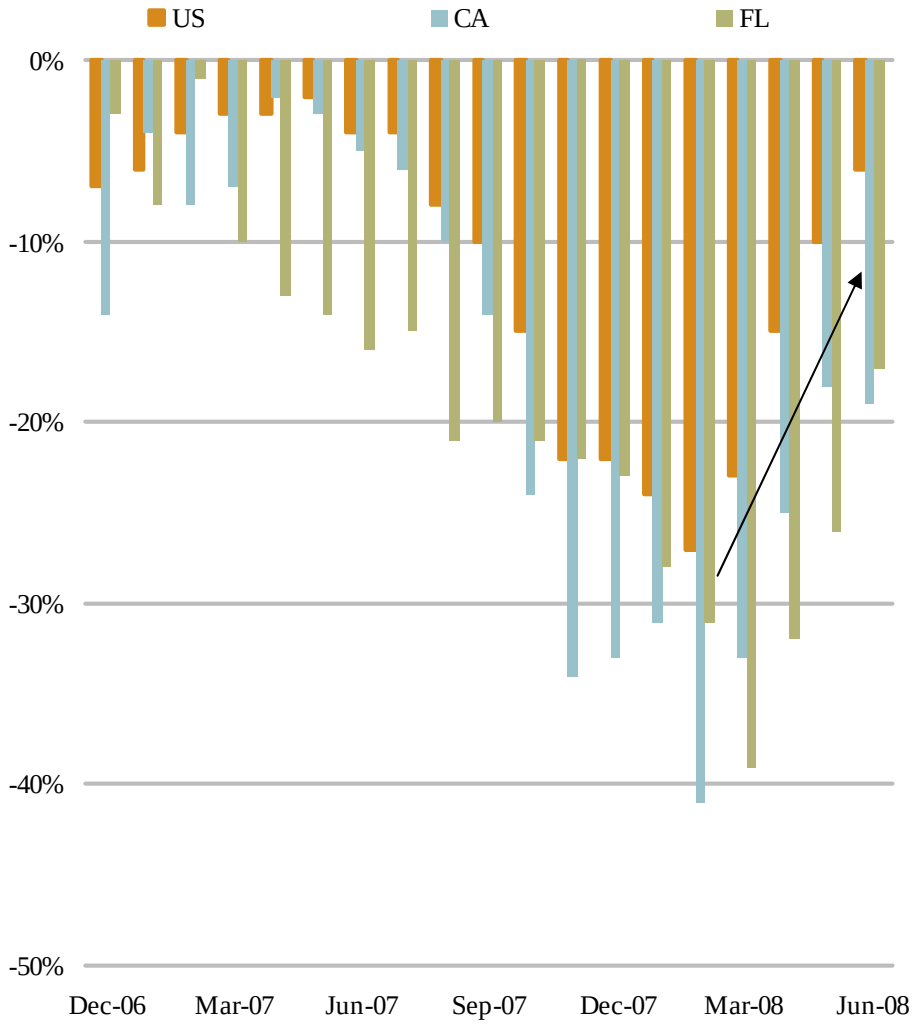
Further Improvements in Home Price Data

Annualized HPA on the Case Shiller Indices

	Feb-08	Mar-08	Apr-08	May-08	Jun-08
Phoenix	-49	-40	-41	-30	-32
San Francisco	-61	-42	-27	-14	-21
Miami	-35	-54	-49	-43	-21
Las Vegas	-57	-53	-24	-35	-19
San Diego	-43	-31	-31	-17	-18
Los Angeles	-51	-43	-27	-23	-17
Tampa	-37	-40	-25	-9	-14
Washington	-30	-26	-12	-12	-11
Portland	-17	-13	3	5	-3
Seattle	-12	-10	9	-6	-3
Detroit	-31	-25	-23	-15	-1
New York	-14	-12	-11	-6	2
Chicago	-24	-23	1	-3	2
Charlotte	-4	3	3	12	4
Atlanta	-16	-16	-8	8	7
Dallas	-8	13	14	12	8
Cleveland	-18	-4	35	-7	9
Minneapolis	-41	-31	-24	7	12
Boston	-17	-13	1	13	15
Denver	-14	-1	10	11	18
Composite-20	**-32**	**-26**	**-15**	**-10**	**-6**

Source: Case Shiller, Lehman Brothers.

Annualized HPA on the Case Shiller Indices %



While REOs are Being Liquidated at a Faster Pace, They Still Don't Match the Speed of Foreclosure Additions

- The pace of REO liquidations has increased in the last few months
- But it is still half the pace at which foreclosures are being added to the system
- To clear REO + foreclosure inventories at the current pace, it would take close to 2 years

Trends in Inventories and Foreclosure Sales

	Inventory (1000 units)			Monthly Sales (1000 units)		New Foreclosures (1000 units)	Inventory in Months of Sales		
	Total	REO	Foreclosure	Total	REO Liquidations		Total	REO	REO + Foreclosure
1H06	3,331	91	219	558	12	20	6.0	7.4	25.4
2H06	4,275	124	262	526	13	34	8.1	9.3	29.1
1H07	4,060	181	333	510	18	40	8.0	9.9	28.2
Q3 07	4,260	241	427	455	22	70	9.4	11.0	30.5
Q4 07	4,291	301	530	416	25	84	10.3	11.9	32.8
Jan-08	4,506	352	612	408	31	101	11.1	11.5	31.5
Feb-08	4,200	374	660	419	32	103	10.0	11.6	32.0
Mar-08	4,331	393	687	412	40	86	10.5	9.9	27.1
Apr-08	4,482	415	714	408	47	97	11.0	8.7	23.8
May-08	4,317	437	737	416	51	96	10.4	8.6	23.0
Jun-08	4,293	451	765	405	55	97	10.6	8.2	22.1

Source: Lehman Brothers, Loan Performance. We also used REO data from the agencies and estimated such numbers for bank portfolios. About 70-80% of REO/Foreclosure come from non-agency securitizations (captured in Loan performance data)

This Trend is More Pronounced in California and Florida

- California and Florida account for about 75% of the total foreclosure inventory in the US
- In California, REO sales are about a third of new foreclosure additions
- In Florida, they are a sixth of new foreclosure additions (partly explained by the judicial process in Florida)

Trends in Inventories and Foreclosure Sales

California

	Inventory (1000 units)		Monthly Changes (1000 units)		Inventory in Months of REO Sales	
	REO	Foreclosure	REO Sales	New Foreclosures	REO	REO + Foreclosure
1H06	1	11	0.1	1.4	8.3	121
2H06	4	27	0.2	5.9	18.2	135
1H07	18	74	1.1	14.6	17.3	86
Q3 07	40	139	2.2	26.6	17.8	80
Q4 07	61	205	3.3	34.9	18.4	80
Jan-08	82	264	5.1	53.6	16.1	68
Feb-08	92	295	5.4	45.6	17.1	72
Mar-08	100	320	7.9	41.1	12.6	53
Apr-08	111	349	10.5	50.6	10.6	44
May-08	123	376	12.3	50.7	10.0	41
Jun-08	130	395	14.9	40.9	8.8	35

Florida

	Inventory (1000 units)		Monthly Changes (1000 units)		Inventory in Months of REO Sales	
	REO	Foreclosure	REO Sales	New Foreclosures	REO	REO + Foreclosure
1H06	1	10	0.2	0.4	5.2	58
2H06	0	2	0.2	2.3	1.4	10
1H07	5	33	0.4	5.1	14.9	104
Q3 07	11	60	0.7	10.4	17.4	109
Q4 07	17	90	1.0	14.1	16.9	106
Jan-08	21	115	1.5	16.8	14.4	91
Feb-08	24	130	1.6	18.7	15.2	99
Mar-08	26	142	2.0	16.9	12.9	84
Apr-08	29	154	2.5	17.4	11.2	72
May-08	31	167	3.1	18.9	10.2	65
Jun-08	34	179	3.6	18.1	9.4	59

Source: Lehman Brothers, Loan Performance. We also used REO data from the agencies and estimated such numbers for bank portfolios. About 70-80% of REO/Foreclosure come from non-agency securitizations (captured in Loan performance data)

IndyMac Loan Modification Program – Details and Implications

Akhil Mago
Madhuri Iyer

LEHMAN BROTHERS

The FDIC Announced a Plan to Modify Delinquent Borrowers on the Portfolio Owned/Serviced by IndyMac Last Week

Plan Details

- FDIC/Indymac plan attempts to modify delinquent borrowers through a combination of rate reduction, term extension, and principal forbearance to target a 38% DTI ratio
- Program carried through only in cases where investor NPV is positive (modification NPV > foreclosure/REO disposition NPV)

Scope

- Delinquent loans owned/serviced by IndyMac. Seeking GSE/loan investor approval
- Owner occupied loans eligible only – no investor properties
- Excludes Option ARM borrowers that have gone delinquent prior to recast
- No FICO, LTV/CLTV requirements.

The Plan Aims to Target a 38% Mortgage DTI for the Borrower Through a Four-Stage Approach and Checks for a Positive Investor NPV at Each Stage

1. Capitalize delinquent PITI into principal balance
   - Servicer recoups prior advanced amounts

2. Interest rate reduction
   - Minimum rate is floored at 3% for up to five years
   - Increase rate by 1% every year after year 5, capped at Freddie Mac reference rate at the time of modification
   - After which the rate remains fixed for the remaining loan term

3. Extend amortization term to 40 years
   - For trusts that might have legal final of 30 years, convert to 40-year amortization with balloon at 30 years

4. Principal forbearance
   - No interest charged on the forbearance amount
   - Lien remains in place and borrower remains responsible for the amount at maturity/payoff

While Modifications Will Likely Improve Value for Delinquent Loans, the Perverse Incentive of Current Borrowers to Go Delinquent is a Concern

- Income verification is critical for success since borrowers have an incentive to under-state income
  - Uncertainty around handling multiple borrowers, recent change in income etc.

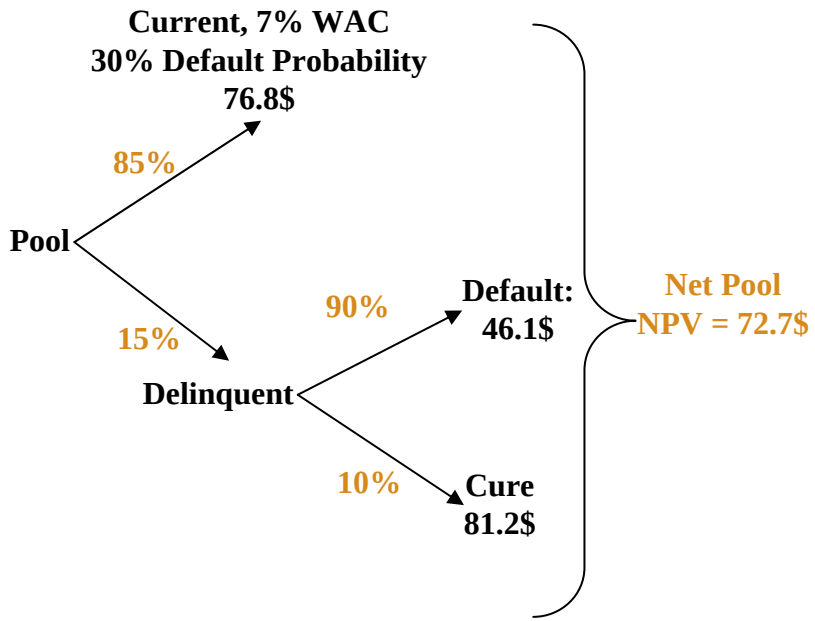
- The re-default assumption used in the NPV calculation is unclear
  - If actual re-default rates are higher than expected, then investor NPV might be negative in certain cases
  - Further, the liquidation value if the loan re-defaults depends on future HPA drops

At an Aggregate Loan Level, Whether Modifications Add Value or Not Varies as a Function of Current Borrowers that Start to Go Delinquent, Re-Default Rates and Severity Assumptions on Re-Default

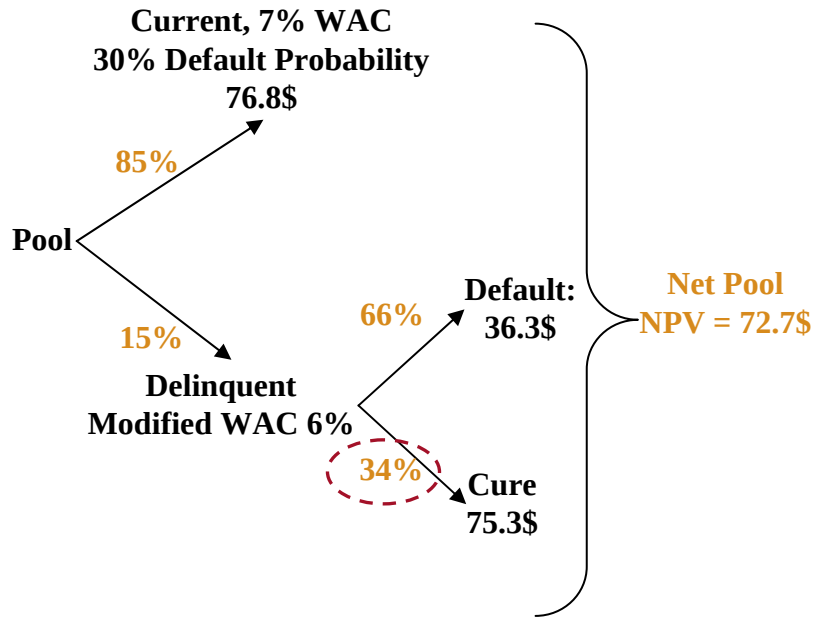
Breakeven Cure Rate Computation to Be Indifferent from an NPV Standpoint

- We solve for the cure rates needed for delinquent loans in a scenario where the servicer modifies the rate lower by 1% on delinquent loans
  - We assume that loss severities on loans that re-default will be higher by 10% due to further home price declines as defaults get back-ended
  - We assume no additional current borrowers start to go delinquent to apply for the plan

NPV, No Modification Scenario



NPV, Modification (1% Rate Redn, 10% Higher Severity on Re-Defaults)



The Breakeven Cure Rate Could be Significantly Higher if We Account for the Perverse Incentive of Current Borrowers to Go Delinquent to Qualify for the Modification

Breakeven Cure Rates Across Scenarios of Higher Severities and Perverse Incentive

- Breakeven cure rates on modified delinquent loans could be as high as 70% after accounting for both perverse incentive and higher loss severities on re-defaults

Cure Rates for Modified Delinquent Loans to Be Indifferent to Modification, 7% WAC Pool

	Breakeven Cure-Rates for Modified Dq Loans across WAC			
Scenario	**6.5%**	**6.0%**	**5.5%**	**5.0%**
Base Case	12%	14%	16%	19%
High Severities (10% Additional)	23%	**34%**	37%	41%
Perverse Incentive (15% Additional Dq.)	54%	**59%**	66%	75%
High Severities and Perverse Incentive	59%	69%	75%	81%

Across the Capital Structure, the Impact of Rate Modifications Varies Widely Across the Wide Variety of Structures in the Alt-A Market

Impact on Bonds Varies Widely Across Structures

- Some of the elements of deal structure that are important are
  - Bond coupon type – fixed-rate, IO, net-WAC pass throughs, LIBOR-floaters with AFC cap etc.
  - Principal and interest being commingled together
  - Principal payment priority, pre/post credit support depletion
  - Level of loss determine if cash flows are PO-like or IO-like – credit IOs benefit in back-ended losses

- We show the impact on three sample deal structures in the next few slides in an extreme scenario where all loans are modified
  - Alt-A fixed rate shifting interest deal
  - Alt-A hybrid shifting interest deal, net-WAC passthrough bonds
  - Alt-A hybrid XS/OC deal, LIBOR-floater bonds

Example 1: Sample Alt-A Fixed Rate Deal

Sample Alt-A FRM Shifting Interest Deal	
Structure	Shifting Interest
Bond Coupon	**Seniors:** Floaters, Inverse Floaters (IOs) **Subordinates:** Net WAC Passthrough
Principal and Interest Combined?	Yes
Can Principal be Used to Pay Interest?	Yes
Senior Principal Payment Priority	Combination of sequential/pro-rata structures, goes pro-rata when subs are written down. Also includes NAS Bonds, SS/JM tranches.
Loss Allocation	Combination of reverse-sequential/pro-rata structures

Source: Lehman Brothers, Deal Prospectus.

Valuations on Subordinates and Excess IOs are Hurt, While Junior Mezz NAS Bonds and Senior IOs Benefit in Most Modification Scenarios

Valuations Across Default Scenarios, Alt-A FRM Shifting Interest Deal

Tranche	Valuation	No Mod	Mod, Same Defaults	Mod, Reduced Defaults	Mod, Reduced+ Back-Ended Defaults	Optimistic Outcome
Collateral						
	Price	**57.9**	**54.2**	**54.4**	**54.6**	**58.1**
	Collateral Loss	13.6%	13.6%	11.2%	11.2%	6.4%
	Duration	4.1	4.1	4.2	4.3	4.5
Front pay bond, Pro-rata Loss						
	Price	67.8	66.0	68.5	71.5	74.4
	Tranche Loss	3.9%	10.5%	6.1%	3.7%	0.0%
	Duration	3.3	3.3	3.2	3.0	3.0
Excess IO (Coupon from Premium Loans)						
	Price	26.8	0.0	0.0	0.0	30.2
	Tranche Loss	0.0%	0.0%	0.0%	0.0%	0.0%
	Duration	4.1	0.0	0.0	0.0	4.3
NAS bond, Junior Mezz						
	Price	38.7	34.1	42.6	43.7	53.3
	Tranche Loss	72.4%	81.7%	65.1%	66.8%	0.0%
	Duration	3.8	3.4	4.6	4.5	6.0
Subordinate						
	Price	8.3	0.0	0.0	0.0	21.8
	Tranche Loss	99.6%	100.0%	100.0%	100.0%	99.4%
	Duration	0.7	0.0	0.0	0.0	2.0

Source: Lehman Brothers, Intex. No Mod refers to our base case scenario. Mod Same Defaults is a scenario in which we reduce the WAC for the entire pool by 1% and total defaults remain the same as in the No Mod Scenario. We lower the total defaults by 20% in the Mod Reduced Defaults Scenario. Mod Reduced+Backended Defaults is one in which defaults are reduced by 20% and back-ended. In the optimistic scenario, we reduce the WAC for the pool by 0.25% and solve for a default scenario in which the collateral benefits through the modification.

Example 2: Sample Alt-A Hybrid Deal, Shifting Interest Structure

Sample Alt-A Hybrid Shifting Interest Deal	
Structure	Shifting Interest
Bond Coupon	Net WAC Passthrough
Principal and Interest Combined?	Yes
Can Principal be Used to Pay Interest?	Yes, though this would not be required in the case of rate reductions
Senior Principal Payment Priority	Pro Rata
Loss Allocation	Reverse-Sequential

Source: Lehman Brothers, Deal Prospectus.

Valuations on Pro-Rata Super-Seniors are Hurt Across Default Scenarios, While Cuspy Junior Mezz and Subordinate Bonds Benefit from Lower/Back-ended Defaults

Valuations Across Default Scenarios, Alt-A Hybrid Shifting Interest Deal

Tranche	Valuation	No Mod	Mod, Same Defaults	Mod, Reduced Defaults	Mod, Reduced+ Back-Ended Defaults	Optimistic Outcome
Collateral						
	Price	**63.1**	**60.2**	**60.8**	**61.2**	**64.8**
	Collateral Loss	11.0%	11.0%	8.8%	8.8%	4.8%
	Duration	3.3	3.3	3.4	3.5	3.7
Pro-Rata Pay Super-Senior Bond						
	Price	70.2	66.9	66.6	66.3	68.3
	Tranche Loss	1.4%	1.3%	0.5%	0.3%	0.0%
	Duration	3.4	3.4	3.5	3.6	3.6
Pro-Rata Pay Junior Mezz Bond						
	Price	52.2	49.4	57.7	61.2	68.3
	Tranche Loss	48.7%	48.6%	30.1%	20.2%	0.0%
	Duration	2.0	2.0	2.7	3.1	3.6
Subordinate						
	Price	7.0	5.9	7.1	11.6	21.3
	Tranche Loss	99.8%	99.8%	99.7%	99.5%	99.2%
	Duration	0.7	0.7	0.8	1.3	2.3

Source: Lehman Brothers, Intex. No Mod refers to our base case scenario. Mod Same Defaults is a scenario in which we reduce the WAC for the entire pool by 1% and total defaults remain the same as in the No Mod Scenario. We lower the total defaults by 20% in the Mod Reduced Defaults Scenario. Mod Reduced+Backended Defaults is one in which defaults are reduced by 20% and back-ended. In the optimistic scenario, we reduce the WAC for the pool by 0.25% and solve for a default scenario in which the collateral benefits through the modification.

Example 3: Sample Alt-A Hybrid Deal, XS/OC Structure

Sample Alt-A Hybrid XS/OC Deal	
Structure	XS/OC
Bond Coupon	Floater, capped at the Net Pool WAC
Principal and Interest Combined?	No
Senior Principal Payment Priority	Combination of sequential/pro-rata structures
Loss Allocation	Combination of reverse-sequential/pro-rata structures

Source: Lehman Brothers, Deal Prospectus.

All Bonds Have Higher Cap Risk Due to the Lower Collateral Net-WAC. Junior Mezz Bonds and Subordinates Benefit in the Backended Defaults Scenario. While More Support is Leaked to the Mezzanine Bonds in a Backended Scenario, XS Spread is Also Higher

Valuations Across Default Scenarios, Alt-A Hybrid Deal XS/OC Deal

Tranche	Valuation	No Mod	Mod, Same Defaults	Mod, Reduced Defaults	Mod, Reduced+ Back-ended Defaults	Optimistic Outcome
Collateral						
	Price	**57.1**	**51.7**	**52.3**	**52.5**	**59.3**
	Collateral Loss	25.0%	25.0%	22.9%	22.9%	11.7%
	Duration	3.6	3.8	4.1	4.2	4.5
Front pay Super-Senior Bond						
	Price	90.0	87.6	86.9	85.0	86.7
	Tranche Loss	0.0%	0.0%	0.0%	0.0%	0.0%
	Duration	0.9	1.0	1.1	1.2	1.2
3rd Pay Super-Senior Bond						
	Price	36.7	31.5	34.2	34.4	37.2
	Tranche Loss	8.3%	32.0%	7.5%	6.1%	0.0%
	Duration	7.7	7.7	8.2	8.2	7.8
Pro-Rata Pay Junior Mezz Bond						
	Price	47.7	29.7	39.7	43.2	57.4
	Tranche Loss	48.0%	70.8%	53.9%	48.8%	0.0%
	Duration	2.4	1.7	2.7	3.0	4.4
Subordinate						
	Price	8.4	2.0	2.8	7.2	35.1
	Tranche Loss	100.0%	100.0%	100.0%	100.0%	0.0%
	Duration	1.3	0.7	0.9	1.8	7.7

Source: Lehman Brothers, Intex. No Mod refers to our base case scenario. Mod Same Defaults is a scenario in which we reduce the WAC for the entire pool to 4% and total defaults remain the same as in the No Mod Scenario. We lower the total defaults by 20% in the Mod Reduced Defaults Scenario. Mod Reduced+Backended Defaults is one in which defaults are reduced by 20% and back-ended. In the optimistic scenario, we reduce the WAC for the pool by 0.25% and solve for a default scenario in which the collateral benefits through the modification.

Additionally, the Impact of Modifications Depends on Overall Loss Expectations. For Example, with Higher Overall Defaults, the 3rd Pay Super-Senior Becomes a Credit IO that Benefits from Extended Durations in a BackEnded Scenario

Valuations Across Default Scenarios, Low Losses

Tranche	Valuation	No Mod	Mod, Same Defaults	Mod, Reduced+ Back-ended Defaults
Collateral				
	Price	57.1	51.7	52.5
	Collateral Loss	25.0%	25.0%	22.9%
	Duration	3.6	3.8	4.2
3rd Pay Super-Senior Bond				
	Price	**36.7**	31.5	**34.4**
	Tranche Loss	8.3%	32.0%	6.1%
	Duration	7.7	7.7	8.2

Valuations Across Default Scenarios, High Losses

Tranche	Valuation	No Mod	Mod, Same Defaults	Mod, Reduced+ Back-ended Defaults
Collateral				
	Price	53.1	48.2	49.7
	Collateral Loss	32.0%	32.0%	28.4%
	Duration	2.4	2.5	3.2
3rd Pay Super-Senior Bond				
	Price	**18.9**	15.5	**20.1**
	Tranche Loss	100.0%	100.0%	100.0%
	Duration	3.0	3.3	4.0

Source: Lehman Brothers, Intex. No Mod refers to our base case scenario. Mod Same Defaults is a scenario in which we reduce the WAC for the entire pool to 4% and total defaults remain the same as in the No Mod Scenario. We lower the total defaults by 20% in the Mod Reduced Defaults Scenario. Mod Reduced+Backended Defaults is one in which defaults are reduced by 20% and back-ended. In the optimistic scenario, we reduce the WAC for the pool by 0.25% and solve for a default scenario in which the collateral benefits through the modification.

In Summary

Overall Impact on Collateral

- **Whether modifications increase/decrease overall collateral NPV depends on assumptions around the perverse incentive of current borrowers to go delinquent, re-default rates and loss severity assumptions on re-defaults**
- In our stylized example, cure rates on modified delinquent loans would need to be be as high as 70% after accounting for both perverse incentive and higher loss severities on re-defaults for the trust to be indifferent to modification at an aggregate level.

Impact Across the Capital Structure

- **Impact on valuation across the capital structure is highly structure-specific. Important to focus on the bond coupon type, whether principal and interest are commingled, principal payment priority pre/post credit support depletion and level of losses**
- In the shifting interest deal with principal and interest commingled, rate modifications generally hurt subordinate valuations and excess IOs (allocated coupon from premium loans). Modifications likely benefit senior inverse IOs due to extension
- In the shifting interest, net WAC passthrough deal, modifications reduce value for most senior tranches due to lower coupon. Junior AAAs /subordinates might benefit due to back-ended losses.
- In the XS/OC deal, cap risk increases for all tranches. Super senior getting hurt due to coupon cap shortfalls and back ended principal recoveries. Backended defaults typically benefit the junior AAAs/subordinate tranches.

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Explanation of the Lehman Brothers Mortgage Model

The Lehman Brothers Mortgage Valuation Model allows investors to analyze mortgage-backed (MBS), asset-backed (ABS) and commercial mortgage-backed securities (CMBS). The model collects pertinent and material information needed to evaluate and calculate the risk measures of the security. The model provides option-adjusted spreads and durations along with other risk measures using Lehman Brothers' Prepayment, Default, and Term Structure Models.

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