

---

# Value Investing Congress

## “A Few Thoughts About Risk”

David Einhorn

November 29, 2007

# Disclaimer

---

VIAGRA is prescribed to treat erectile dysfunction (ED).

If you take any medicines that have nitrates in them (like nitroglycerin for chest pain)—every day or even once in a while—you should NOT take VIAGRA.

Discuss your general health status with your doctor to ensure that you are healthy enough to engage in sexual activity. If you experience chest pain, nausea, or any other discomforts during sex, seek immediate medical help.

Although erections lasting for more than 4 hours may occur rarely with all ED treatments in this drug class, to avoid long-term injuries, it is important to seek immediate medical help.

If you are older than age 65, or have serious liver or kidney problems, your doctor may start you at the lowest dose (25 mg) of VIAGRA. If you are taking protease inhibitors, such as for the treatment of HIV, your doctor may recommend a 25-mg dose and may limit you to a maximum single dose of 25 mg of VIAGRA in a 48-hour period.

In rare instances, men taking PDE5 inhibitors (oral erectile dysfunction medicines, including VIAGRA) reported a sudden decrease or loss of vision. It is not possible to determine whether these events are related directly to these medicines or to other factors. If you experience sudden decrease or loss of vision, stop taking PDE5 inhibitors, including VIAGRA, and call a doctor right away.

Sudden decrease or loss of hearing has been rarely reported in people taking PDE5 inhibitors, including VIAGRA. It is not possible to determine whether these events are related directly to the PDE5 inhibitors or to other factors. If you experience sudden decrease or loss of hearing, stop taking VIAGRA and contact a doctor right away.

If you have prostate problems or high blood pressure for which you take medicines called alpha blockers, your doctor may start you on a lower dose of VIAGRA.

Remember to protect yourself and your partner from sexually transmitted diseases.

The most common side effects of VIAGRA are headache, facial flushing, and upset stomach. Less commonly, bluish vision, blurred vision, or sensitivity to light may briefly occur.

# Disclaimer

---

THESE MATERIALS SHALL NOT CONSTITUTE AN OFFER TO SELL OR THE SOLICITATION OF AN OFFER TO BUY ANY INTERESTS IN GREENLIGHT OR ANY OF ITS AFFILIATES. SUCH AN OFFER TO SELL OR SOLICITATION OF AN OFFER TO BUY INTERESTS MAY ONLY BE MADE PURSUANT TO A DEFINITIVE SUBSCRIPTION AGREEMENT BETWEEN GREENLIGHT AND AN INVESTOR.

The information set forth in this presentation has been obtained from publicly available sources. It is provided for informational purposes only and should not be deemed as a recommendation to buy or sell the securities mentioned or to invest in any investment product. The information has not been independently verified by Greenlight or any of its affiliates. Neither Greenlight nor any of its affiliates makes any representations or warranties regarding, or assumes any responsibility for the accuracy, reliability, completeness or applicability of, any information, calculations contained herein, or of any assumptions underlying any information, calculations, estimates or projections contained or reflected herein.

Investment accounts managed by Greenlight and its affiliates may have a position in any of the securities discussed in this presentation. Greenlight may reevaluate its holdings in such positions and sell or cover certain positions.

# Top of the Morning to You

---

Given some confidence level  $\alpha \in (0,1)$  the VaR of the portfolio at the confidence level  $\alpha$  is given by the smallest number  $l$  such that the probability that the loss  $L$  exceeds  $l$  is not larger than  $(1 - \alpha)$

$$\begin{aligned}\text{VaR}_\alpha &= \inf\{l \in \mathcal{R} : P(L > l) \leq 1 - \alpha\} \\ &= \inf\{l \in \mathcal{R} : F_L(l) \geq \alpha\}\end{aligned}$$

# Value-at-Risk

---

From *Wikipedia*:

“The maximum loss not exceeded with a given probability defined as the confidence level, over a period of time. It is commonly used by security houses or investment banks to measure the market risk of their asset portfolios.”

# Value-at-Risk

---

A simple definition:

*95% of the time I don't expect  
to lose more than X*

# Value-at-Risk

---

- Should risk managers concentrate on VaR?
- Wikipedia says:  
“VaR does not give any information about the severity of loss by which it is exceeded.”

# Broker-Dealer 2<sup>nd</sup> Quarter VaR

---

	<u>VaR (\$MM)</u>
Lehman Brothers	87
Bear Stearns	29
Merrill Lynch	71
Morgan Stanley	93



# Broker-Dealer VaR

---

	<u>2<sup>nd</sup> Quarter</u>	<u>3<sup>rd</sup> Quarter</u>
	<u>VaR (\$MM)</u>	<u>Net Writedowns</u>
Lehman Brothers	87	700
Bear Stearns	29	475
Merrill Lynch	71	7,800
Morgan Stanley	93	800

# Broker-Dealer VaR

---

	<u>3<sup>rd</sup> Quarter</u>	<u>4<sup>th</sup> Quarter</u>
	<u>VaR (\$MM)</u>	<u>Net Writedowns</u>
Lehman Brothers	100	??
Bear Stearns	35	1,200
Merrill Lynch	85	??
Morgan Stanley	84	3,700

# Conclusions on VaR

---

- Not the appropriate way to measure risk
- Risk managers should focus on tails
- VaR in the tails does not solve Fat Tails
- Similar risk management failure in other financial institutions

# FAS 159:

## Profiting From Your Own Demise

- FAS 159 is a new fair value accounting standard
- Allows companies to value individual Assets and Liabilities at fair value
- Fair valuing only the Asset side of the balance sheet creates a mismatch
- FAS 159 eliminates the mismatch

# FAS 159:

## Profiting From Your Own Demise

- Fair valuing Liabilities works fine for market risk (rates up, value down)
- Problem: The issuer's idiosyncratic risk drives down the value of its own liabilities
- GAAP accounting does not equal good accounting

# FAS 159

---

If your own credit spread  
widening counts as revenue...

# FAS 159

---

... and you pay compensation  
as a percent of revenue ...

# FAS 159

---

... the most profitable and  
lucrative day in the history  
of your firm will be ...



# FAS 159

---

**THE DAY YOU GO BANKRUPT!**



# Are FAS 159 Gains Real?

---

“I think the gains are real. It really reflects the change in fair value. There’s somebody on the other side of that trade who lost money.”

Bear Stearns CFO

# FAS 159: Gains on Widening of Own Credit Spreads

---

(Third Quarter, \$ in millions)

	<u>Gains</u>	<u>Pretax Income</u>
Lehman Brothers	??	1,205
Bear Stearns	225	175
Merrill Lynch	600	(3,465)
Morgan Stanley	390	2,246

# Lehman's FAS 159 Gain

---

“Within Fixed Income Capital Markets, the Firm recorded very substantial valuation reductions, most significantly on leveraged loan commitments and residential mortgage-related positions. These losses were partially offset by large valuation gains on economic hedges and other liabilities. The result of these valuation items was a net reduction in revenues of approximately \$700 million.”

Lehman Press Release

# Lehman's FAS 159 Gain from 10Q

## *Borrowings and Deposit Liabilities*

<b>(\$ in billions)</b>	<b>Aug 31,2007</b>	<b>Nov 30, 2006</b>
<b>Short Term Borrowings</b>		
Amount carried at fair value <sup>(1)</sup>	\$ 5.5	\$ 3.8
Principal Amount	\$ 5.5	\$ 3.7
<b>Deposit liabilities at banks</b>		
Amount carried at fair value <sup>(1)</sup>	\$ 13.7	\$ 14.7
Principal Amount	\$ 13.8	\$ 14.7
<b>Unsecured long-term borrowings</b>		
Amount carried at fair value <sup>(1)</sup>	\$ 23.0	\$ 11.0
Principal Amount	\$ 24.5	\$ 11.1
<b>Total Difference</b>	<b>\$ 1.6</b>	<b>\$ -</b>

# Lehman's FAS 159 Gain From 10Q

---

- (1) Substantially all of the borrowings recorded at fair value are structured notes and contain two parts: a note and an embedded forward or option component. The difference between the aggregate principal balance and the aggregate fair value represents cumulative changes in Holdings' credit spreads as well as changes to the embedded forward or option component. During the 2007 three and nine months, a substantial portion of the change in fair value is associated with the embedded forward or option component, which is risk managed and part of our capital markets activities.

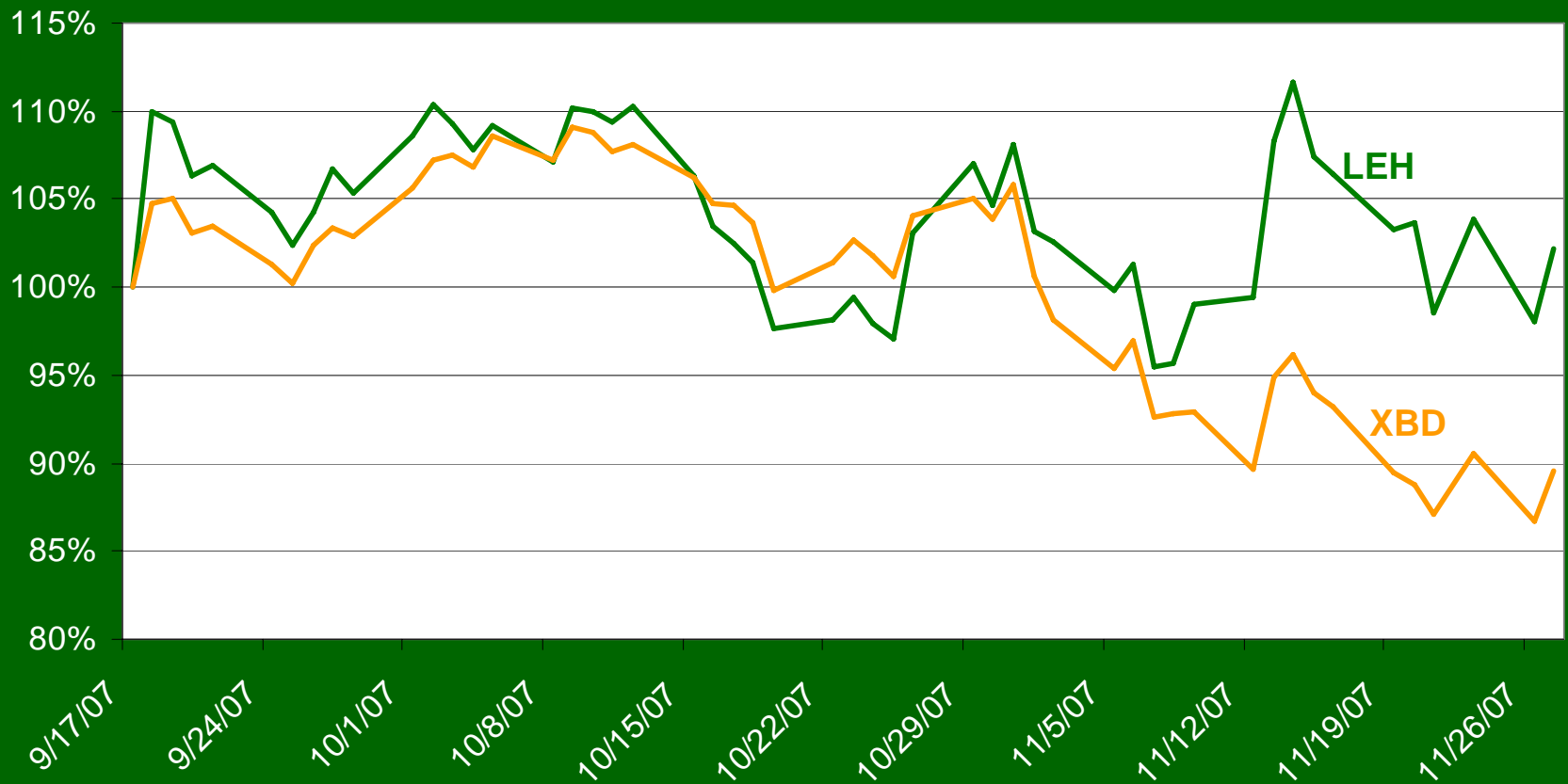
# Lehman 3<sup>rd</sup> Quarter Charge...

---

Loss on Levered Loans	“Well over \$1 billion”
Loss on Residential Mortgages	“Less than levered loans”
FAS 159 Gain on Liabilities	\$1.6 billion less the ‘embedded option’
<hr/>	
Total	\$700 million

# Lehman Stock Price

Price since earnings release on September 17, 2007





# Some Lehman History

---

- The 2008 credit meltdown created rumors Lehman reached the brink of insolvency
- While insolvency was overblown, the mortgage market stopped
- Lehman had large mortgage exposure, but took no writedowns (mark-to-model)
- The market rapidly recovered and Lehman pulled through

# Why has Lehman held up?

---

- A “good quarter” – reported earnings of \$1.54
- They say they hedged
- Originate to move, not own
- November estimates of \$1.75 have not come down
- 2008 estimates of \$7.75 – a record year – have not come down
- Sell-side consensus chance of write-down is “minimal”

# Lehman's Balance Sheet

<b>Assets (\$ in millions)</b>	<b>Aug 31,2007</b>	<b>Nov 30, 2006</b>
Cash and cash equivalents	\$ 7,048	\$ 5,987
Segregated cash and securities	10,579	6,091
Financial instruments and other positions	302,297	226,596
Collateralized agreements	287,427	225,156
Receivables	38,391	27,971
Property, equipment and other assets	9,366	8,382
Identifiable intangibles and goodwill	4,108	3,362
<b>Total Assets</b>	<b>\$ 659,216</b>	<b>\$ 503,545</b>

<b>Liabilities (\$ in millions)</b>	<b>Aug 31,2007</b>	<b>Nov 30, 2006</b>
Short-term and long-term borrowings	\$ 171,580	\$ 123,228
Short financial instruments	140,840	125,960
Collateralized financings	256,077	176,557
Payables and accrued liabilities	68,986	58,609
<b>Total Liabilities</b>	<b>\$ 637,483</b>	<b>\$ 484,354</b>
<b>Stockholder's equity</b>	<b>21,733</b>	<b>19,191</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 659,216</b>	<b>\$ 503,545</b>

# Lehman Exposures

## *Financial instruments and other inventory positions owned and shorted*

(\$ in millions)	Owned		Short	
	Aug 31, 2007	Nov 30, 2006	Aug 31, 2007	Nov 30, 2006
Mortgages and mortgage-backed	\$ 88,007	\$ 57,726	\$ 246	\$ 80
Government and agencies	37,108	47,293	63,776	70,453
Corporate debt and other	52,151	43,764	8,620	8,836
Corporate equities	64,283	43,087	40,393	28,464
Derivatives and other contracts	35,711	22,696	27,725	18,017
Real estate held for sale	20,044	9,408	-	-
CP and other money market	4,993	2,622	80	110
<b>Total</b>	<b>\$ 302,297</b>	<b>\$ 226,596</b>	<b>\$ 140,840</b>	<b>\$ 125,960</b>

# Lehman Exposures

## Securitization Activity

(\$ in billions)	Aug 31, 2007			Nov 30, 2006		
	Residential		Other	Residential		Other
	IG <sup>(1)</sup>	HY		IG <sup>(1)</sup>	HY	
Interests in securitizations	\$ 9.2	\$ 1.7	\$ 3.4	\$ 5.3	\$ 2.0	\$ 0.6
Weighted-average life (years)	7	6	5	5	6	5
Average constant prepayment rate	15.4%	26.4%	-	27.2%	29.1%	-
Weighted-average credit loss assumption	0.2%	2.3%	0.5%	0.6%	1.3%	-

<sup>(1)</sup> The amount of investment-grade interests in securitizations related to agency CMOs was approximately \$4.5 billion and \$1.9 billion at Aug 31, 2007 and Nov 30, 2006

# Lehman Exposures

## *Lending-Related Commitments*

(\$ in millions)	Total Contractual Amount	
	Aug 31, 2007	Nov 30, 2006
Lending Commitments		
High grade <sup>(1)</sup>	\$ 26,977	\$ 17,945
High yield <sup>(2)</sup>	\$ 11,497	\$ 7,558
Contingent acquisition facilities		
Investment grade	\$ 4,104	\$ 1,918
Non-investment grade	\$ 27,039	\$ 12,766
Mortgage commitments	\$ 12,432	\$ 12,246
Secured lending transactions	\$ 93,155	\$ 82,987
<b>Total</b>	<b>\$ 175,204</b>	<b>\$ 135,420</b>

<sup>(1)</sup> Net credit exposure, after consideration of hedges, of \$14.4 billion and \$4.9 billion at Aug 31 2007 and Nov 30 2006.

<sup>(2)</sup> Net credit exposure, after consideration of hedges, of \$10.4 billion and \$5.9 billion at Aug 31 2007 and Nov 30 2006.

# Lehman Exposures

---

## *Other Contingent Exposures*

(\$ in millions)	Total Contractual Amount	
	Aug 31, 2007	Nov 30, 2006
Derivative Contracts <sup>(1)</sup>	\$ 767,563	\$ 534,585
Municipal securities commitments	\$ 7,313	\$ 1,599
Other commitments with VIEs	\$ 8,334	\$ 4,902
Standby letters of credit	\$ 1,792	\$ 2,380
Private equity commitments	\$ 5,016	\$ 1,088
<b>Total</b>	<b>\$ 790,018</b>	<b>\$ 544,554</b>

<sup>(1)</sup> We believe the fair value of the derivative contracts is a more relevant measure of the obligations because we believe the notional value amount overstates the expected payout. The fair value of these derivative contracts approximated \$11.1 billion and \$9.3 billion as of Aug 31 2007 and Nov 30 2006

# Lehman Exposures

---

## *No Loss on Level III Instruments*

(\$ in millions)	Balance May 31	Purchases, Sales, Net	Transfers In/(Out)	Gains/ (Losses)	Balance Aug 31
<b>Mortgages and mortgage-backed</b>	<b>\$ 11,920</b>	<b>\$ 1,854</b>	<b>\$ 9,588</b>	<b>\$ (616)</b>	<b>\$ 22,746</b>
Corporate debt and other	3,592	(690)	96	36	3,034
Corporate equities	4,048	658	261	88	5,055
Derivative assets, net	1,280	(59)	(160)	541	1,602
<b>Total</b>	<b>\$ 20,840</b>	<b>\$ 1,763</b>	<b>\$ 9,785</b>	<b>\$ 49</b>	<b>\$ 32,437</b>



# What Will Happen

---

- Either they will recognize losses or they won't
- If they do, everyone will be surprised
- If they don't, they will underearn prospectively those banks that did

## 2006 Revenue Mix

- Fixed Income  $\approx$  48%
- Securitization  $\approx$  15%
- Underwriting and advisory  $\approx$  18%

# Criteria Caixa Net Asset Value

---

(all numbers in € millions; prices as of Nov 28, 2007)

## Public Investments

Gas Natural	6,738
Telefonica	5,946
Repsol YPF	3,799
Abertis	2,844
Banco BPI	1,047
Other public	1,585
	<hr/>
	€ 21,959

## Private Investments

	€ 4,766
Post-IPO Debt	(1,137)
	<hr/>
NAV Pre-Tax	€ 25,588
Taxes on embedded gains	(1,843)
	<hr/>
NAV After-Tax	€ 23,745
<b>NAV per share</b>	<b>€ 7.04</b>
<b>Current price</b>	<b>€ 5.21</b>
<b>Discount to NAV</b>	<b>26.0%</b>

# Criteria Caixa

---

- IPO'd as an investment company
- Parent *La Caixa* is the largest Spanish retail savings bank
- Formation of portfolio
- Near-term strategy
- Long-term transformation from investment company to operating company
- Discount to NAV should become a premium to book