**From:** Park, Gene
**Sent:** 02/28/2006 08:54:29 AM
**To:** Cassano, Joseph
**CC:** Forster, Andrew; Frost, Alan; Gorton, Gary; Teasel, Sheridan; Fewings, Tom; Budnick, Adam
**Subject:** CDO of ABS Approach Going Forward - Message to the Dealer Community

Joe,

Below summarizes the message we plan on delivering to dealers later this week with regard to our approach to the CDO of ABS super senior business going forward:

We feel that the CDO of ABS market has increasingly become less diverse over the last year or so and is currently at a state where deals are almost totally reliant on subprime/non prime residential mortgage collateral. Given current trends in the housing market, our perception of deteriorating underwriting standards, and the potential for higher rates we are no longer as comfortable taking such concentrated exposure to certain parts of the non prime mortgage securitisations. On the deals that we participate on we would like to see a significant change in the composition of these deals going forward - i.e. more diversification into other non-correlated asset classes.

As a result of our ongoing due diligence we are not comfortable with the mezzanine layers (namely BBB and single A tranches) of this asset class. As a result of changing our internal stresses on this collateral therefore we will no longer be competitive in our ability to write protection on deals which incorporate such a large proportion of mezzanine tranches of subprime deals/non prime deals. Given some of our concerns over correlation in this sector our stressing of exposure below Aa3/AA- is also applied to exposure taken via a CDO and as such we also do not feel that we can currently be competitive where the deals include large percentages of CDO product that themselves reference sub Aa3 rated non prime mortgage collateral. We are still comfortable with our current modelling of tranches rated Aa3/AA- or higher on non prime mortgage deals tranches rated however we are keen to encourage some more diversity in the overall CDO's and as such would like to limit the non-prime residential mortgage bucket on High Grade deals to a maximum of 12.5% and the overall residential mortgage bucket (prime & non-prime) to a maximum of 25.0% (such exposure being taken either directly or via 3rd party CDO's).

We realize that this is likely to take us out of the CDO of ABS market for the time being given the arbitrage in subprime collateral. However, we remain committed to working with underwriters and managers in developing the CDO of ABS market to hopefully become more diversified from a collateral perspective. With that in mind, we will be open to including new asset classes to these structures or increasing allocations to others such as CLOs and EM CDOs.