

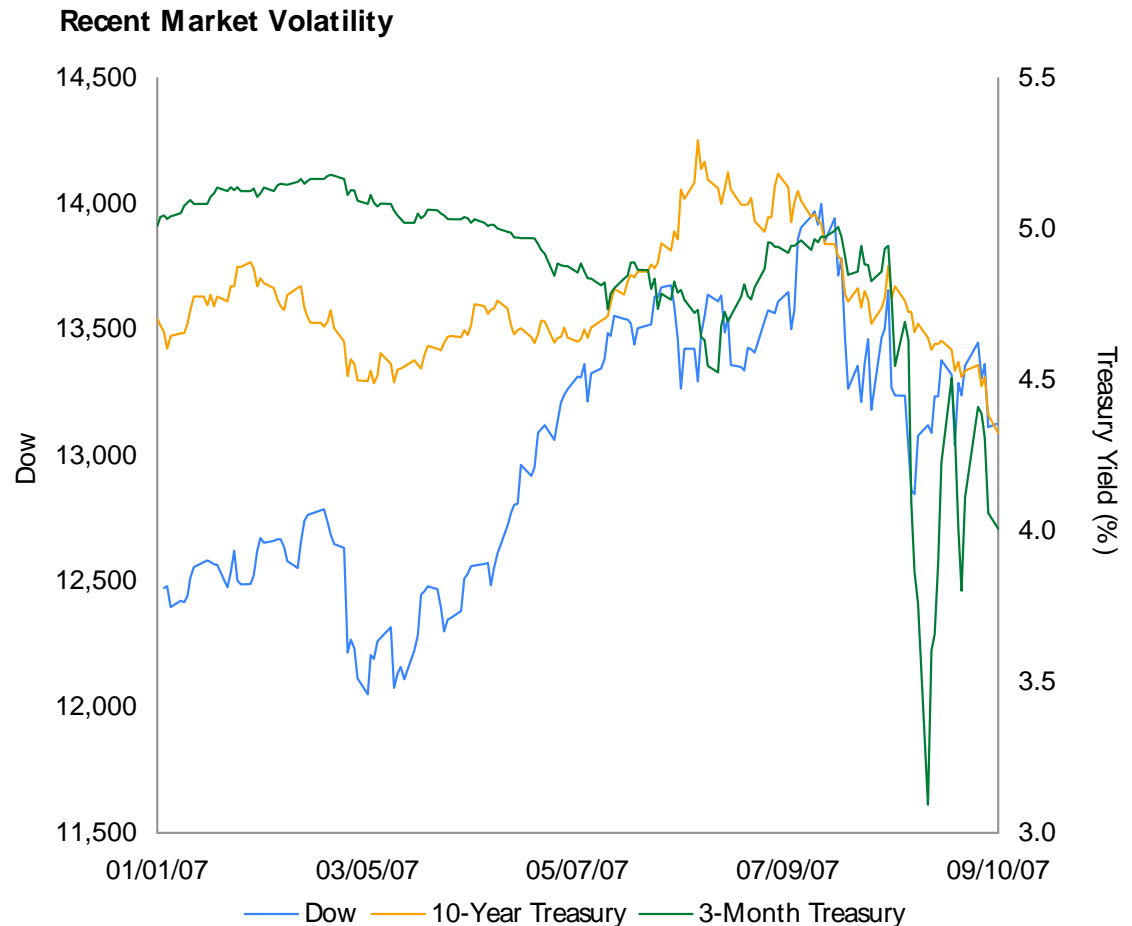
Iowa Finance Authority

2007 HousingIowa Conference

Subprime Lending Challenges, Part I: How We Got Here

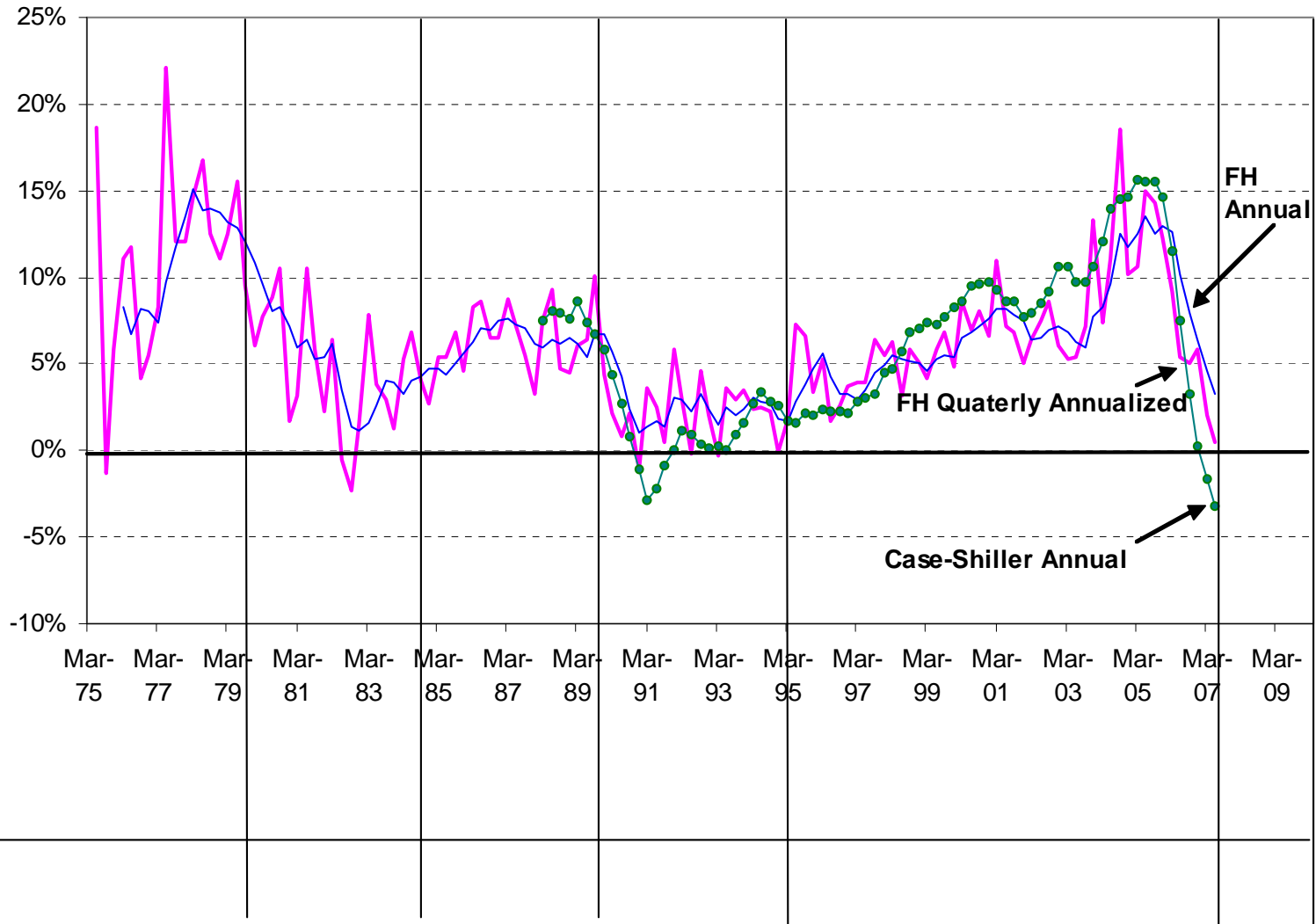
Overview of Recent Disruption in the Credit Markets

- ◆ Through August, there was a disruption in the global credit market, originally caused by the fallout in the subprime lending sector. Subprime concerns spread to the commercial paper market as money market investors backed away from commercial paper due to collateral concerns
- ◆ Treasury yields – especially short maturities hit lows as investors sought the “safe haven” of treasuries
- ◆ Credit spreads widened across investment classes
- ◆ On August 17, the Federal Reserve reduced its discount rate by 50 basis points to “promote the restoration of orderly conditions in financial markets”
- ◆ On August 31, President Bush announced proposals to relax FHA rules to allow more guarantees for low income borrowers who wish to refinance and to suspend IRS rules on how renegotiated and foreclosed mortgages lead to taxable income
- ◆ Liquidity has improved but the market continues to be subject to headline risk and further shakeout



FHLMCs Home Price Index

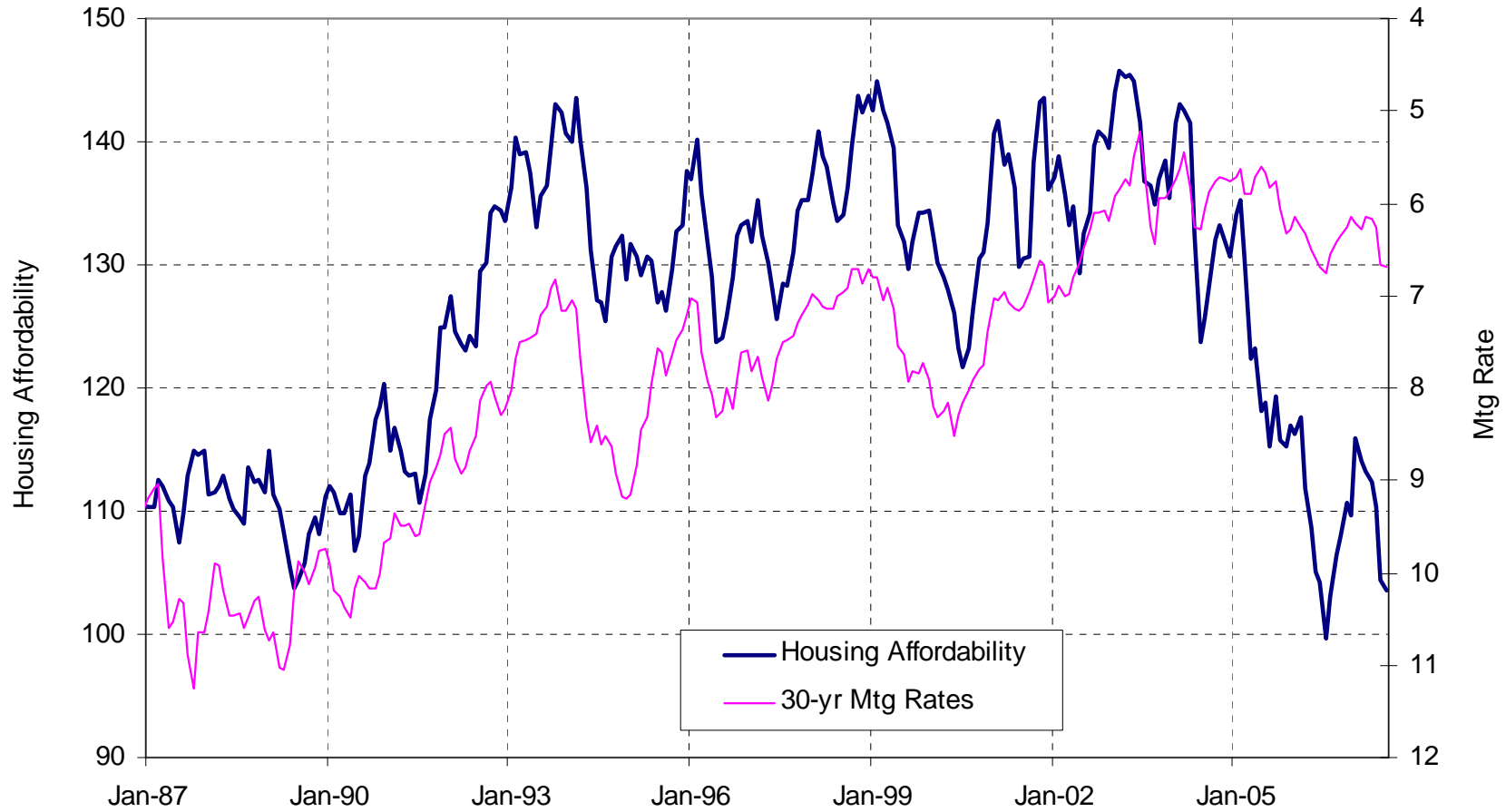
Quarterly Data Annualized and Annual Data



Source: Freddie Mac

Latest data: Q2 2007. Quarterly FH Annualized = 0.4%; FH Annual = 3.3%; CS Annual = -3%

Housing Affordability



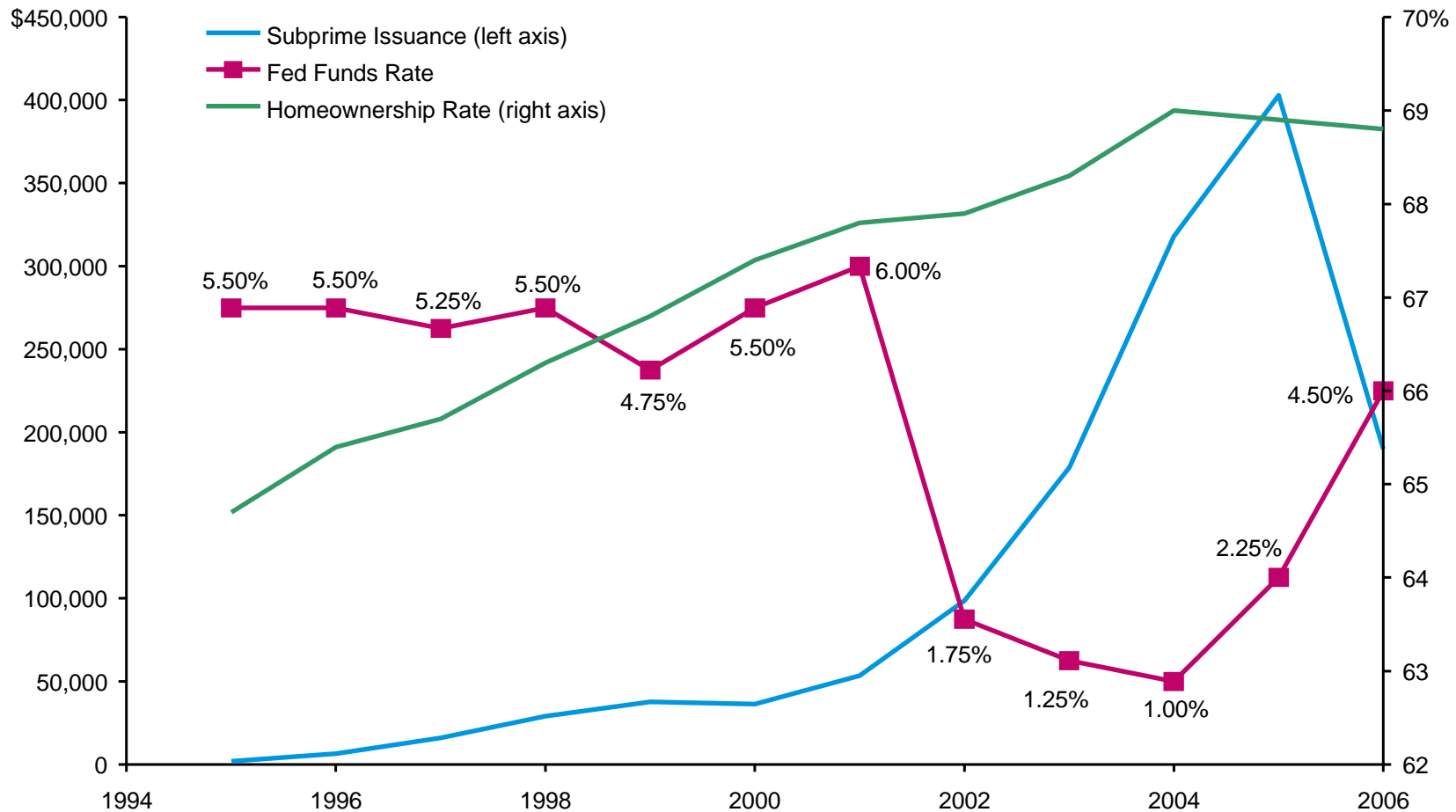
Source: National Association of Realtors, Freddie Mac

Latest is estimated: Jul 2007: Housing Affordability = 103.6; 30-yr no-point Mtg Rate = 6.70

Overview of the Subprime Market

Growth of the Subprime Market

Issuance of Subprime MBS, \$ in Millions



Source: First American LoanPerformance, Census Bureau.

Overview of the Subprime Market

What is Subprime?

- ◆ Characteristics of Subprime Borrowers
 - Two or more 30-day delinquencies in past 12 months or one or more 60-day delinquency in past 24 months
 - Judgment, foreclosure, repo or charge-off in past 24 months
 - Bankruptcy in past 5 years
 - Debt service to income ratio 50%+
 - Non traditional documentation/proof of income
 - Subprime borrowers generally have low F.I.C.O. scores

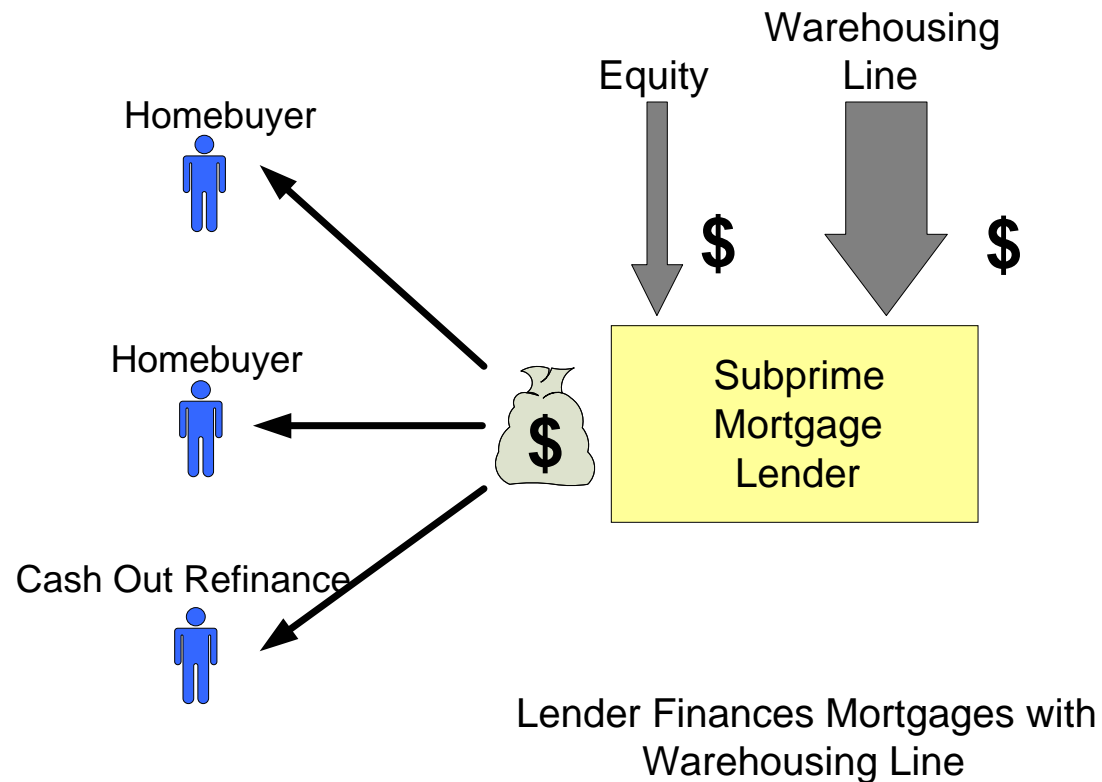
- ◆ F.I.C.O. Score
 - A number between 300 and 850, calculated by Fair Isaac Corporation using a proprietary statistical model
 - Represents an individual's or family's credit history
 - Composition of F.I.C.O. Score
 - 35% – payment punctuality
 - 30% – amount of debt – ratio of revolving debt to revolving credit available
 - 15% – length of credit history
 - 10% – types of credit used
 - 10% – recent credit obtained

Dramatic Growth of the Subprime Market

- ◆ Low interest rates allowed for the proliferation of adjustable rate mortgages and other “exotic” products
- ◆ Flawed assumptions as to home price appreciation led to increased subprime adjustable rate lending
- ◆ Today, subprime loans account for approximately 15% of \$10 trillion mortgage market
- ◆ Up to 80% of subprime loans are adjustable rate – often underwritten to initial low rate
- ◆ As of the beginning of 2007, 11.8% of subprime loans were 60 days or more delinquent and 4.6% were pending foreclosure – these numbers are increasing
- ◆ Overall mortgage delinquencies have hovered around 4% since 1990 and recently edged up to 4.9%
- ◆ Approximately \$1.7 billion of outstanding subprime loans in Iowa (78% of which are ARMs and 54% of which are cash-out refinancings) have been securitized; these loans have a delinquency rate of 15% and a foreclosure rate of 8.6%

Overview of the Subprime Market

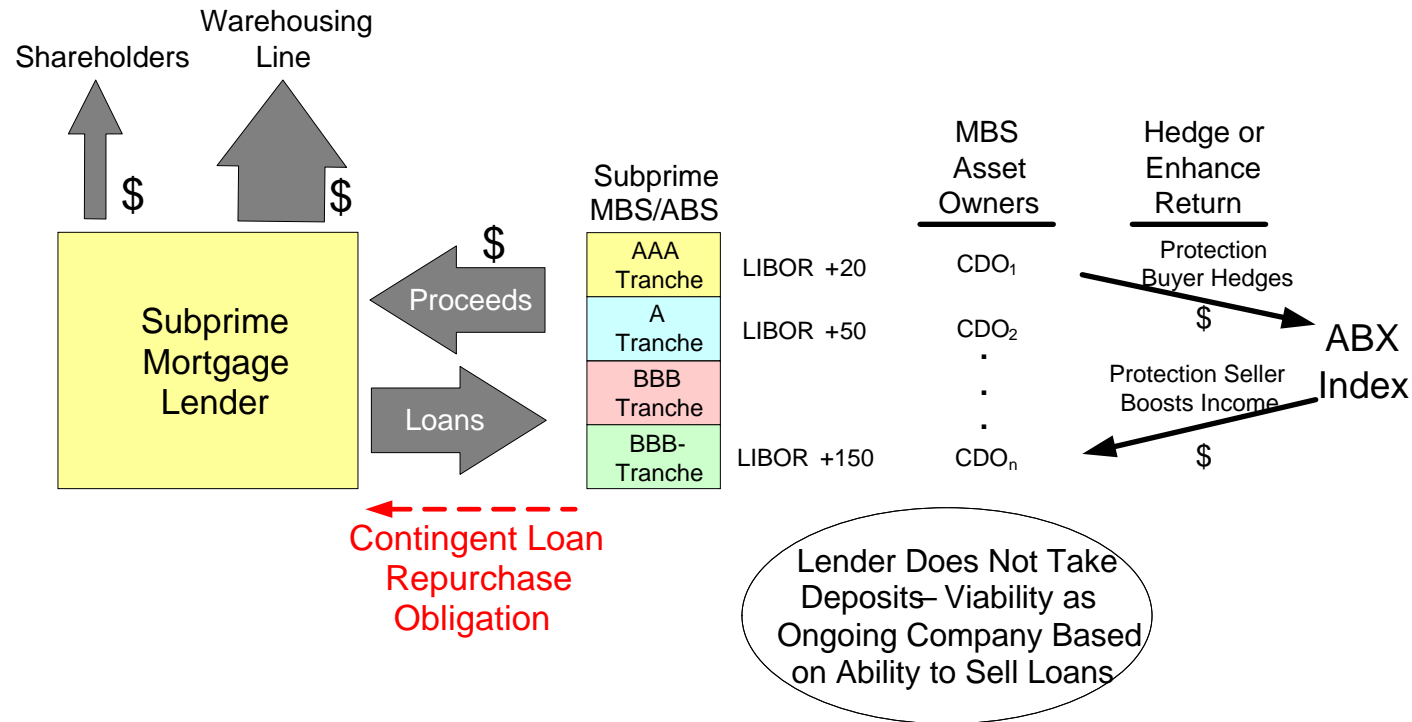
How have subprime loans been funded?



- ◆ Many subprime lenders are not banking institutions and are without regulatory oversight or capital requirements
- ◆ Securitization of loan reduces regulatory supervision

Overview of the Subprime Market

How are subprime loans securitized?



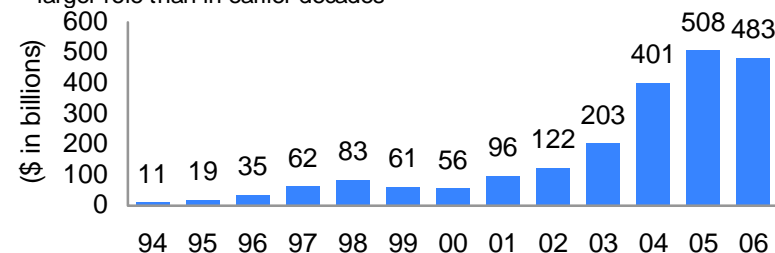
- ◆ No regulatory oversight/capitalization requirements
- ◆ Lender governed by:
 - Warehouse line provider requirements
 - Market pricing on lowest rated debt
 - Ability of asset owners to hedge risk
- ◆ Lender sets credit standards

Subprime Loans Packaged into Structured Investments

- ◆ Secondary market demand for high-yielding mortgage products gave rise to highly structured investments that packaged subprime loans
- ◆ **The credit of the structured investments (RMBS and CDOs) was based upon assumptions of continuous strong home price appreciation and continued access to low cost refinancing of ARMS, enabled by higher home equity values**
- ◆ Underwriting standards deteriorated, as originators migrated away from cash flow-income based metrics to collateral-based underwriting to meet secondary market demand
- ◆ **Hedge funds and banks then used RMBS/CDO as collateral for loans to fund their purchase**
- ◆ **As delinquencies rose the value of the collateral came under question and margin calls ensued**
- ◆ **Rating agencies issued downgrades**

Growth in Subprime RMBS Issuance

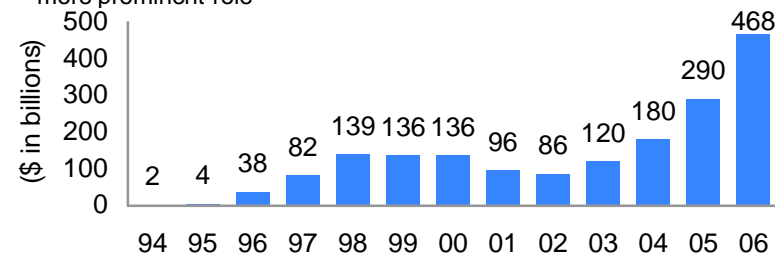
- ◆ Subprime mortgage-backed security issuance surged in recent years, playing a much larger role than in earlier decades



Source: Inside MBS & ABS and UBS

Growth in CDO Issuance

- ◆ There was an accompanying jump in collateralized debt obligations (CDO) issuance to a more prominent role



Source: Credit UBS CDO Research

% of Central Banks that Have Approved Specific Asset Classes

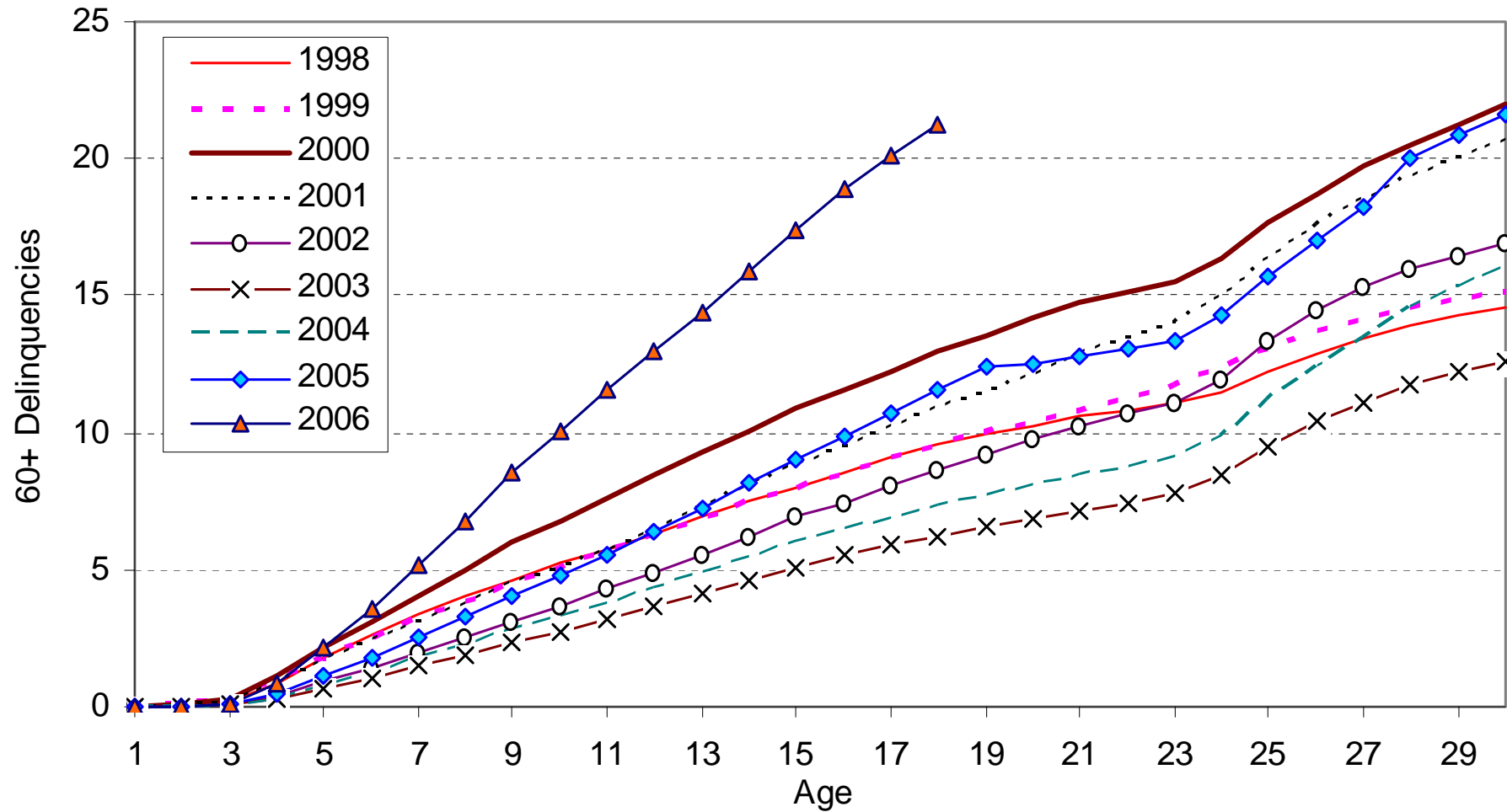
	2006	2005	2004	2003	2002	2001	2000	1999	1998
U.S. Agencies	84	82	76	78	75	71	62	68	54
Sovereign Eurobonds	64	60	60	58	58	61	60	66	66
MBS/ ABS	44	39	39	27	22	17	19	12	2
Corporates	40	38	38	32	28	22	20	15	10
Landesbank Debt	40	37	33	27	30	30	32	28	12
Canadian Provinces	11	9	10	10	8	9	10	10	12
Equities	18	5	3	2					

Source: UBS Central Bank Surveys, 1998-2006

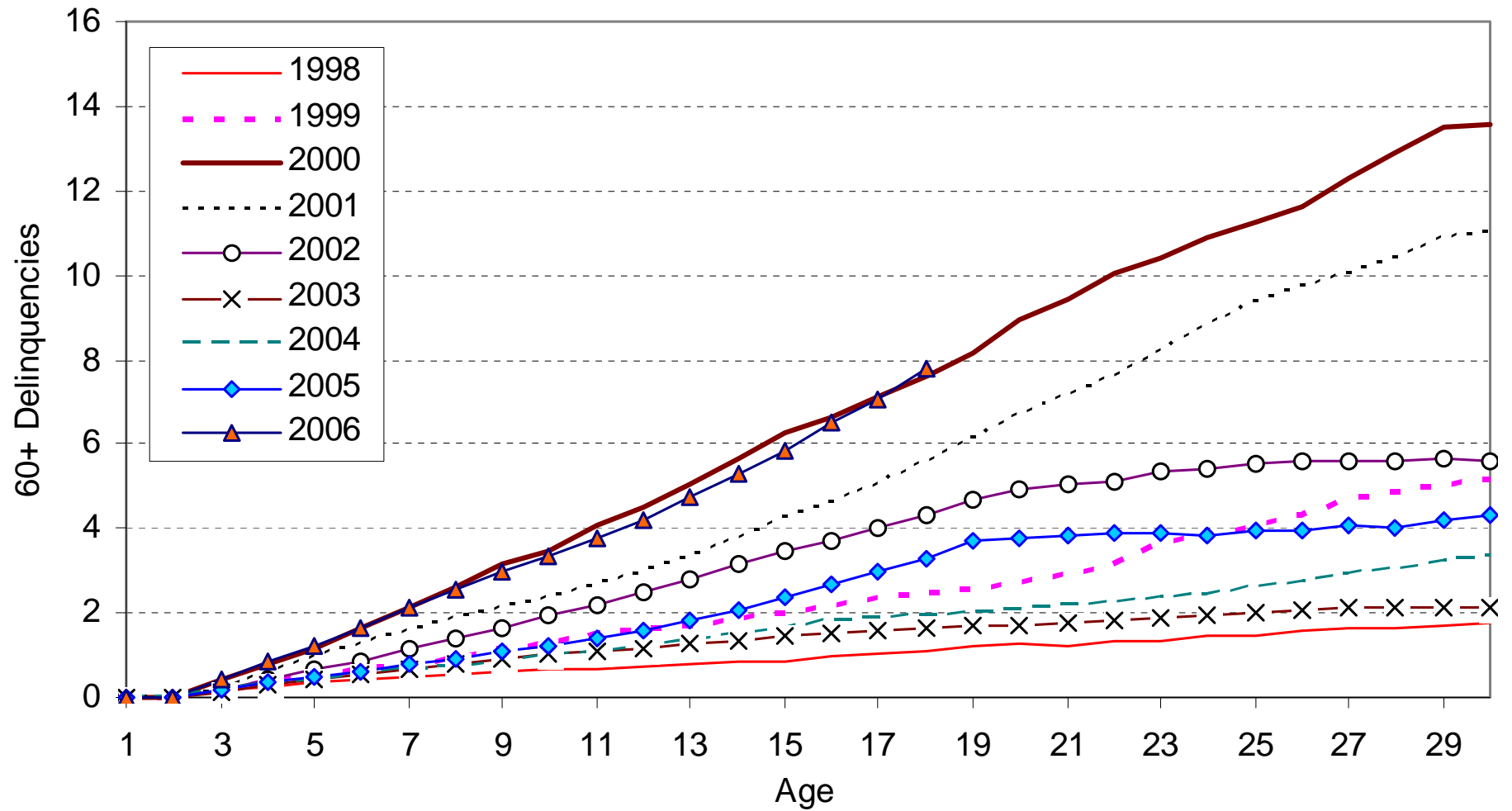
Collateral Characteristics

Product	Orig. Year	CLTV	%IO	%40Yr	%PiggyBack	%Purchase	%CLTV>80	%CLTV>=90	%Full Doc	FICO
Prime ARMs	2001	67	21	0	0	32	4	3	60	730
	2002	66	41	0	1	27	3	2	55	734
	2003	68	41	0	11	34	10	7	47	734
	2004	73	65	0	23	53	20	15	49	735
	2005	74	83	0	27	56	22	17	48	739
	2006	75	91	0	32	48	26	18	34	736
	2007	72	94	0	30	29	21	8	17	734
Alt-A ARMs	2001	73	17	0	3	47	20	15	36	705
	2002	73	27	0	5	45	17	13	34	711
	2003	78	55	0	24	50	34	27	29	709
	2004	83	74	0	39	61	47	40	33	708
	2005	84	84	0	48	64	51	45	28	713
	2006	85	86	1	55	60	57	51	19	711
	2007	83	76	4	46	41	50	41	13	712
Subprime ARMs	2001	81	0	0	4	34	45	25	71	598
	2002	81	1	0	4	33	47	27	66	605
	2003	84	6	0	11	35	56	38	63	613
	2004	85	21	0	20	40	61	45	59	619
	2005	86	33	8	29	46	63	50	55	626
	2006	88	20	37	34	46	68	56	53	623
	2007	86	20	40	23	36	67	52	56	619

Subprime 2006: The Worst Ever! (60D+ Delinquencies)



Alt-A – 60D+ Delinquencies



The External Environment – The Subprime Problem

The Local Environment (by Origination Year)

Asset Class Type	Origination Year	MSA	Active Loans	Current Balance (\$ in millions)	Total Number of Loans	Total Origination		ARM %	60+ Day Delinquent (OTS)	Foreclosure
						Amount (\$ in millions)	Balance Remaining			
Subprime	2000	IA	179	\$ 9	2,902	\$ 179	\$ 49,721	65%	23%	7.0%
Subprime	2001	IA	413	23	3,339	229	56,659	71	26	9.6
Subprime	2002	IA	1,039	70	5,514	431	67,180	79	29	15.4
Subprime	2003	IA	1,973	155	6,549	566	78,561	75	25	12.6
Subprime	2004	IA	3,836	326	8,853	802	85,063	80	22	11.8
Subprime	2005	IA	8,139	731	10,769	1,002	89,839	82	12	7.8
Subprime	2006	IA	4,621	423	5,020	466	91,452	74	6	4.0
Total			20,100	\$ 1,737	42,946	\$ 3,674	\$ 86,000	78%	15%	8.6%

How IA Compares to Selected States (Ranked by 60+ Days Delinquent from Best to Worst)

Asset Class Type	Origination Year	MSA	Active Loans	Current Balance (\$ in millions)	Total Number of Loans	Total Origination		ARM %	60+ Day Delinquent (OTS)	Foreclosure
						Amount (\$ in millions)	Balance Remaining			
Subprime	2000-06	FL	326,138	\$ 52,441	722,231	\$ 106,140	49.41%	78.12%	7.26%	3.38%
Subprime	2000-06	CA	505,723	144,203	1,565,264	393,132	36.68	82.37	8.08	3.77
Subprime	2000-06	CT	44,269	8,069	103,852	17,763	45.43	76.77	9.23	4.73
Subprime	2000-06	NJ	71,903	16,000	209,977	43,783	36.55	81.95	10.73	5.36
Subprime	2000-06	NY	136,416	32,883	317,264	73,964	44.46	66.64	10.75	8.52
Subprime	2000-06	PA	109,646	12,541	201,071	22,706	55.23	68.11	10.95	3.90
Subprime	2000-06	IL	148,392	22,407	369,377	57,825	38.75	86.35	13.48	7.02
Subprime	2000-06	MA	60,049	13,556	175,658	37,402	36.24	80.60	14.22	6.24
Subprime	2000-06	IA	20,100	1,737	42,946	3,674	47.28	78.86	14.93	8.60
Subprime	2000-06	MN	57,091	9,171	139,617	21,750	42.17	85.42	17.91	6.30
Subprime	2000-06	OH	132,761	13,230	248,824	24,508	53.98	70.94	20.63	8.37

Source: *First American Loan Performance*. Note: This data is comprised of subprime loans that have been private label securitized. UBS estimates that these loans comprise approximately 80% of all subprime loans originated in the given years.

Iowa Subprime Statistics

Zip Code	City/Town	Current Balance (\$)	% of Subprime for the State	# of Active Loans	Avg Loan Balance Outstanding (\$)	Original Stated LTV	% Loans Refi for Rate	% Loans Refi for Cashout	% Loans Used to Purchase Home	For Remaining Loans				Average FICO
										ARM%	% 60 + Day Delinquent	% Foreclosure	%	
50317	Des Moines	66,305,320	3.5	834	79,503	85	17	51	32	71	15	9.1	605	
50315	Des Moines	65,671,942	3.4	778	84,411	86	15	49	37	75	17	10.0	608	
51503	Council Bluffs	46,941,052	2.5	446	105,249	84	13	57	30	68	13	6.4	616	
51501	Council Bluffs	46,542,051	2.4	611	76,174	85	15	54	31	70	16	9.6	610	
50310	Des Moines	39,316,067	2.1	409	96,127	85	14	52	34	75	14	7.5	611	
50021	Ankeny	33,527,926	1.8	281	119,316	85	15	32	53	79	19	10.9	620	
52806	Davenport	30,625,473	1.6	313	97,845	86	21	44	35	74	18	10.7	610	
50322	Urbandale	29,648,603	1.6	246	120,523	84	15	49	36	72	10	5.3	620	
52404	Cedar Rapids	28,762,163	1.5	342	84,100	85	15	39	45	74	14	8.0	609	
50265	West Des Moines	28,745,473	1.5	249	115,444	84	15	42	42	74	11	6.9	623	
50313	Des Moines	28,333,300	1.5	358	79,143	84	19	49	32	72	19	9.5	603	
50320	Des Moines	28,083,273	1.5	247	113,697	86	12	37	50	78	16	8.3	616	
52804	Davenport	27,419,880	1.4	342	80,175	85	14	55	30	78	14	8.2	607	
52405	Cedar Rapids	26,822,355	1.4	303	88,523	86	16	50	34	70	11	6.7	612	
50316	Des Moines	25,971,168	1.4	356	72,953	85	14	57	28	69	18	11.3	600	
52402	Cedar Rapids	25,886,404	1.4	273	94,822	86	19	55	25	74	16	8.5	608	
52722	Bettendorf	25,375,425	1.3	226	112,281	84	22	46	32	77	11	8.6	617	
52302	Marion	25,126,002	1.3	240	104,692	85	15	42	42	75	11	4.6	615	
52803	Davenport	22,444,466	1.2	283	79,309	85	10	56	33	77	23	14.8	607	
52403	Cedar Rapids	21,323,168	1.1	245	87,033	85	18	58	24	76	16	6.8	608	

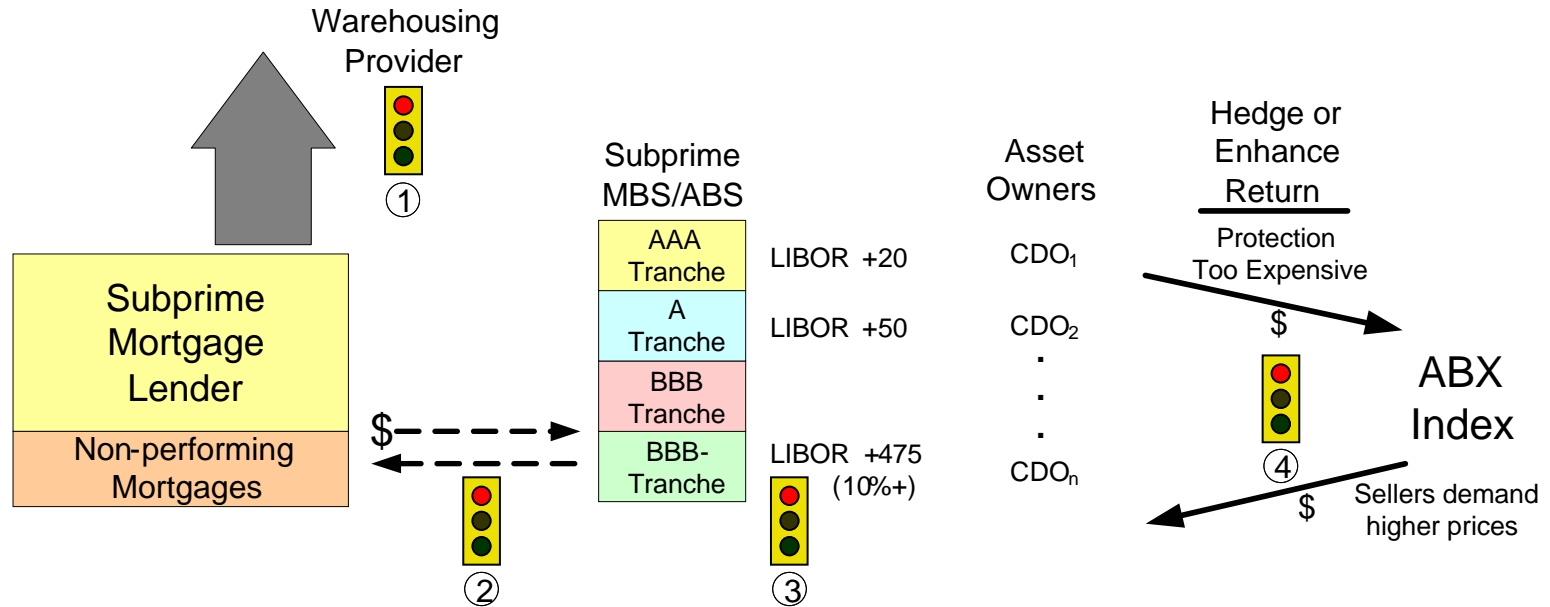
Local Environment: Top 10 Counties with the highest current balances of subprime loans in Iowa

County	Current Balance (\$)	% of Subprime for the State	# of Active Loans	Avg Loan Balance Outstanding (\$)	Original Stated LTV	% Loans Refi for Rate	% Loans Refi for Cashout	% Loans Used to Purchase Home	For Remaining Loans				Average FICO
									ARM%	% 60 + Day Delinquent	% Foreclosure	%	
Polk	506,045,340	26.6	5,119	98,856	85	14	46	39	74	15	8.9	614	
Linn	154,679,130	8.1	1,643	94,144	85	17	50	33	74	13	6.8	610	
Scott	142,665,078	7.5	1,555	91,746	85	17	51	31	75	16	10.7	609	
Pottawattamie	118,848,070	6.2	1,323	89,832	84	14	55	30	71	16	9.1	612	
Black Hawk	71,467,444	3.8	950	75,229	85	14	56	30	71	13	7.0	605	
Woodbury	60,054,075	3.2	823	72,970	85	15	57	27	68	15	7.3	607	
Warren	48,086,156	2.5	415	115,870	84	14	50	35	69	20	9.3	612	
Dallas	45,374,832	2.4	418	108,552	85	17	44	38	76	12	7.3	620	
Johnson	39,778,109	2.1	314	126,682	84	17	47	35	71	11	7.0	622	
Story	36,005,856	1.9	350	102,874	84	13	47	39	79	15	8.7	617	

Source: First American Loan Performance. Note: This data is comprised of subprime loans that have been private label securitized. We estimate that these loans comprise approximately 80% of all subprime loans originated in the given years. Data as of April 2007

Overview of the Subprime Market

Why did problems in subprime market occur?



Problems Occur at Every Step as Loan Defaults/Repurchases Increase

12 Lenders sold or shut within 12 months; Dozen more on "Ailing" List

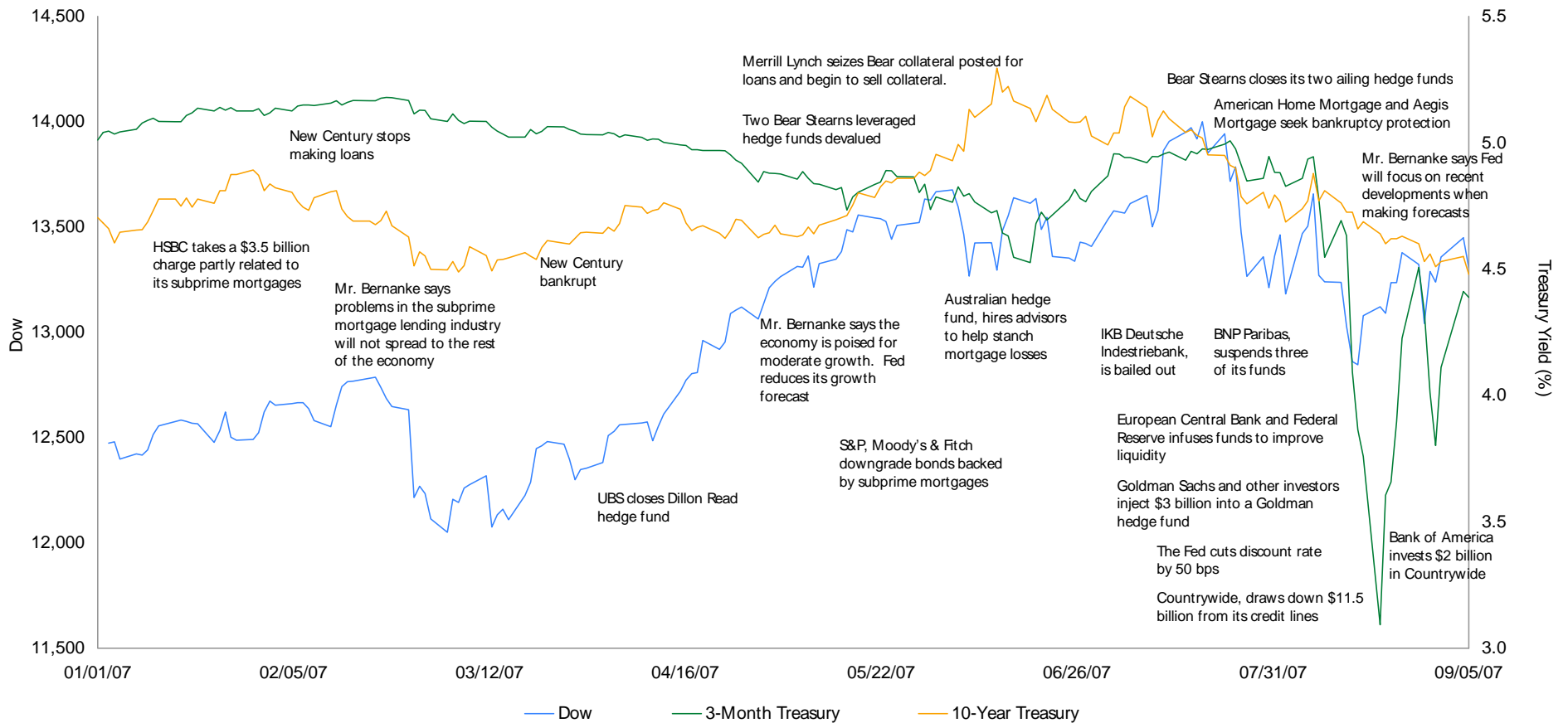
- 1: Warehouse Lender Pulls Line
- 2: Asset Owners Hire Loan Investigators to Force Buyback
- 3: Defaults on Existing Debt Occur—Financing Costs Rise
- 4: Insurance Costs Rise—Speculation Distorts Market

Subprime Originations (\$ million) – Rankings & Current Status

Rank	Lender	2006 Volume	Mkt Share	Notes
1	HSBC Finance, IL	\$52,800	8.30%	Shutting down its mortgage services office in Indiana, eliminating 600 jobs (Aug 2007); Shutting down Decision One unit eliminating 750 jobs (Sep 2007)
2	New Century Financial, CA	\$51,600	8.10%	Filed for Chapter 11 bankruptcy (Apr 2007)
3	Countrywide Financial, CA	\$40,596	6.30%	Cut 900 jobs, plans to cut as much as 20% (10-12k) of its workforce in the next 3 months (Sep 2007)
4	CitiMortgage, NY	\$38,040	5.90%	Announced to lay off of 557 employees in FL offices (May 2007)
5	WMC mortgage, CA	\$33,157	5.20%	GE announced its plans to sell its WMC mortgage unit; WMC has reduced its staff from 1,200 to ~700 over the past year (Jul 2007)
6	Fremont Investment & Loan, CA	\$32,300	5.00%	Ceased subprime lending (Mar 2007); Ellington announced plans to buy Fremont's real estate business (Apr 2007)
7	Ameriquest mortgage, CA	\$29,500	4.60%	ACC Capital Holdings, owner of Ameriquest; shut retail branches (May 2007)
8	Option One mortgage, CA	\$28,792	4.50%	Owned by H&R Block; Sale to Cerberus may fall apart (Sep 2007)
9	Wells Fargo Home mortgage, IA*	\$27,869	4.40%	Shut subprime wholesale lending unit (Jul 2007); announced to cut back on Alt-A originations (Aug 2007)
10	First Franklin Financial Corp, CA	\$27,666	4.30%	Sold to Merrill Lynch (Sep 2006); Merrill announced plans to cut an unspecified # of jobs at First Franklin (Sep 2007)
11	Washington Mutual, WA	\$26,600	4.20%	Tightened underwriting standards and eliminated 2/28s (Jul 2007)
12	Residential Funding Corp., MN	\$21,200	3.30%	GMAC-RFC Holding Corp is parent company
13	Aegis mortgage Corp., TX	\$17,000	2.70%	Filed for Chapter 11 bankruptcy (Aug 2007)
14	American General Finance, IN	\$15,070	2.40%	Wholly-owned indirectly by AIG
15	Accredited Home Lenders, CA	\$15,767	2.50%	Halted mortgage applications and ~1,600 employees will be laid off; Rejected Lone Star's revised buyout offer (Aug 2007)
16	BNC mortgage, CA	\$14,500	2.30%	Subsidiary of Lehman; Shut down-- eliminating 1,200 employees (Aug 2007)
17	Chase Home Finance, NJ	\$11,550	1.80%	Tightened underwriting standards and eliminated 2/28s (Jul 2007)
18	Equifirst, NC	\$10,750	1.70%	Sold to Barclays (Jan 2007)
19	NovaStar Financial, KS	\$10,233	1.60%	Closed its WarehouseUSA unit (Apr 2007); seeking "strategic alternatives"; receives \$1.9bb credit line from Wachovia (May 2007)
20	Ownit mortgage Solutions, CA	\$9,500	1.50%	Shut down (Dec 2006)
21	Resmae mortgage Corp., CA	\$7,659	1.20%	Exits Chapter 11 bankruptcy protection; wholly-owned by RMC Mortgage Holdings, an affiliate of Citadel (Jun 2007)
22	Mortgage Lenders Network USA, CT	\$6,000	0.90%	Filed for Chapter 11 bankruptcy (Feb 2007)
23	ECC Capital Corp., CA	\$5,485	0.90%	Sold to Bear Stearns (Oct 2006)
24	Fieldstone Mortgage Company, MD	\$4,991	0.80%	Sold to C-Bass; Wholesale operations closed after liquidity problems at C-Bass (Aug 2007)
25	Nationstar Mortgage (Centex), TX	\$4,619	0.70%	Sold to Fortress (Mar 2006)
Total for Top 25 Lenders:		\$543,243	84.90%	
Total B&C Originations:		\$640,000	100.00%	

Source: Inside B&C Lending.

Timeline of Events



Stages of the Crisis

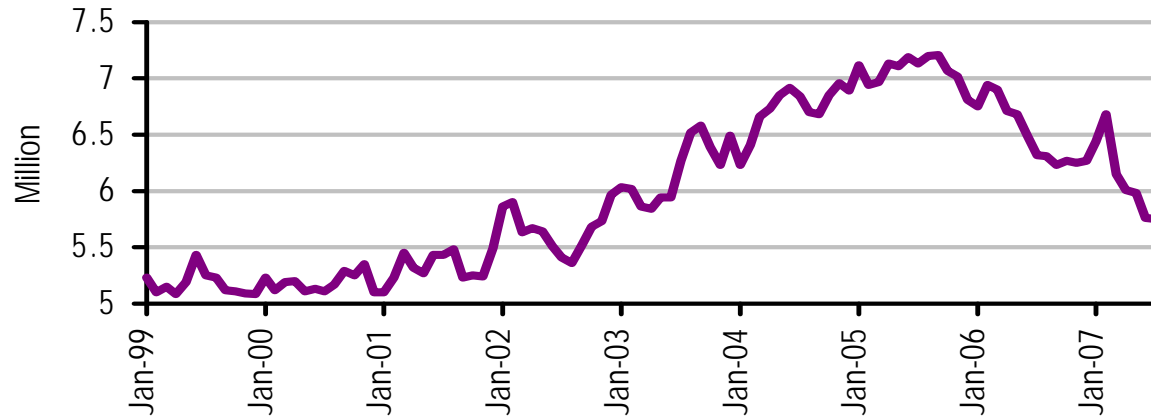
- ◆ Stage 1: February, 2007
 - Subprime Originators exit the market due to early pay defaults

- ◆ Stage 2: late June 2007-????
 - The Financial Crises (Deleveraging, financing issues, funding issues for originators and ABCP conduits).
 - This stage of the crises began with the liquidation of the Bear Stearns hedge funds in late June. This in turn led to a tightening of financing which in turn led to a virtual suspension in trading of non-agency MBS securities, turmoil in the ABCP market, and originator difficulties. This crises has prompted the Fed to act.

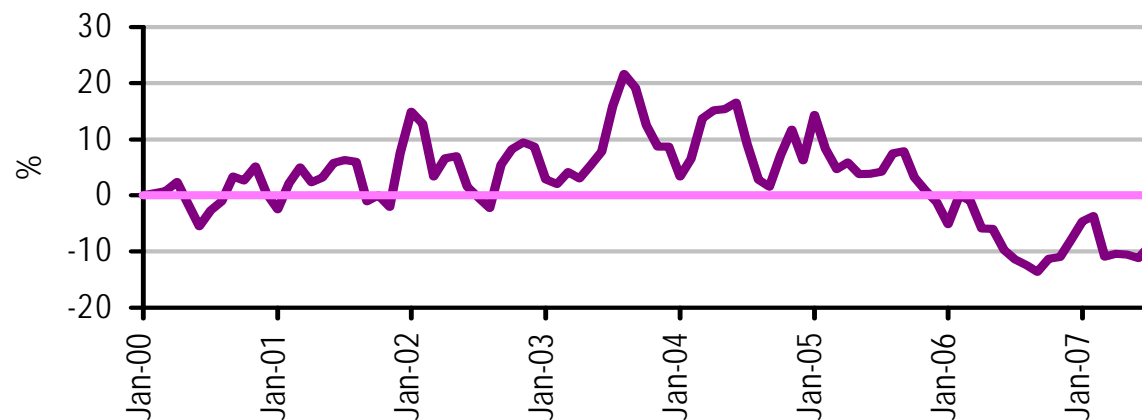
- ◆ Stage 3: late 2007-mid-2009
 - The real economy will slow. Home price declines and softening home sales means lower employment in housing construction and the mortgage and real estate industry. These industries must resize. There will be secondary effect on building materials.
 - There will be indirect effects because (1) general tightening of credit standard will further weaken housing and (2) moderating HPA means less home equity extraction and lower consumer spending.

Housing Market Weaker: Existing Home Sales Down

Annual Rate

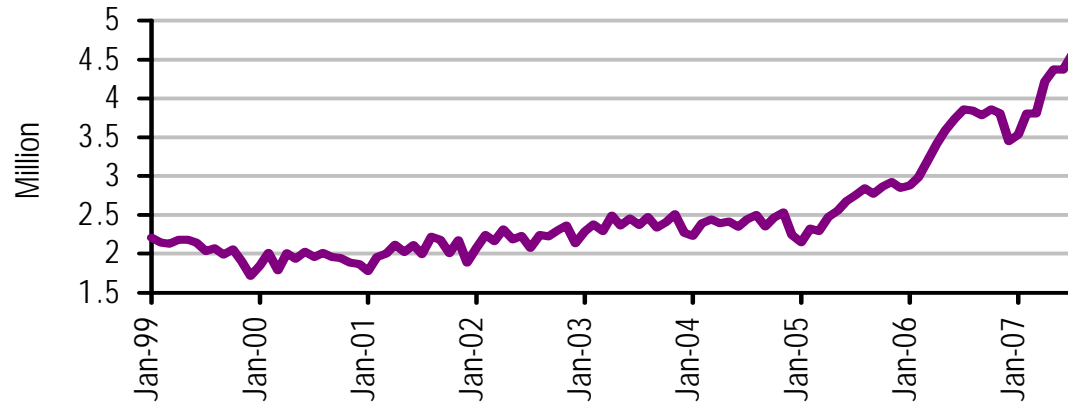


% Change YOY

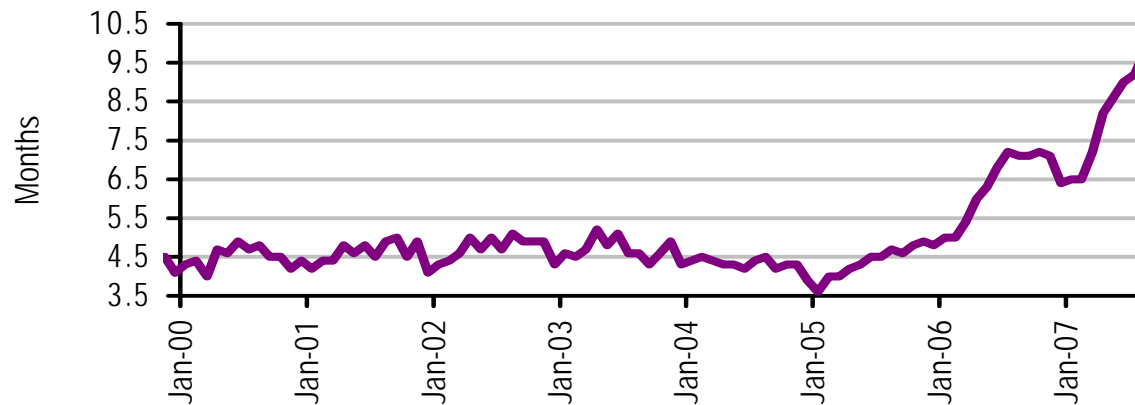


Existing Home Inventory UP

Existing Home Inventory



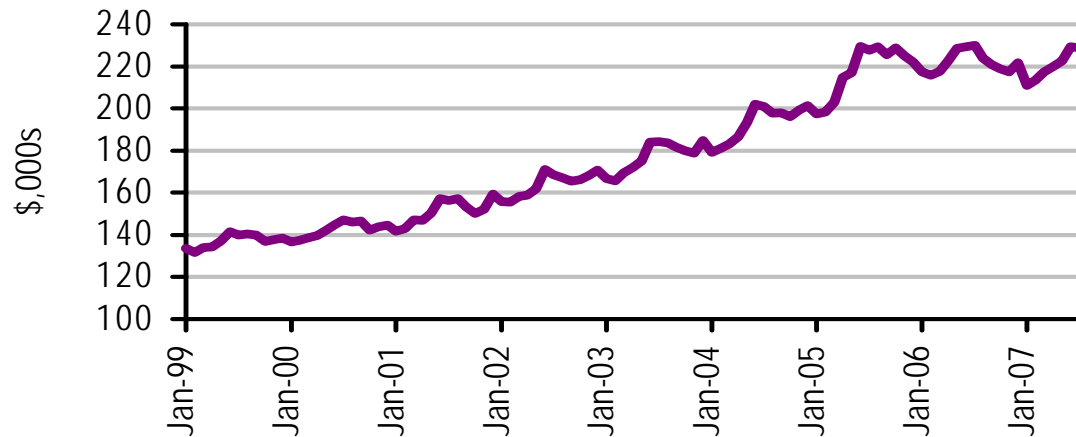
Existing Home Inventory—Months Supply



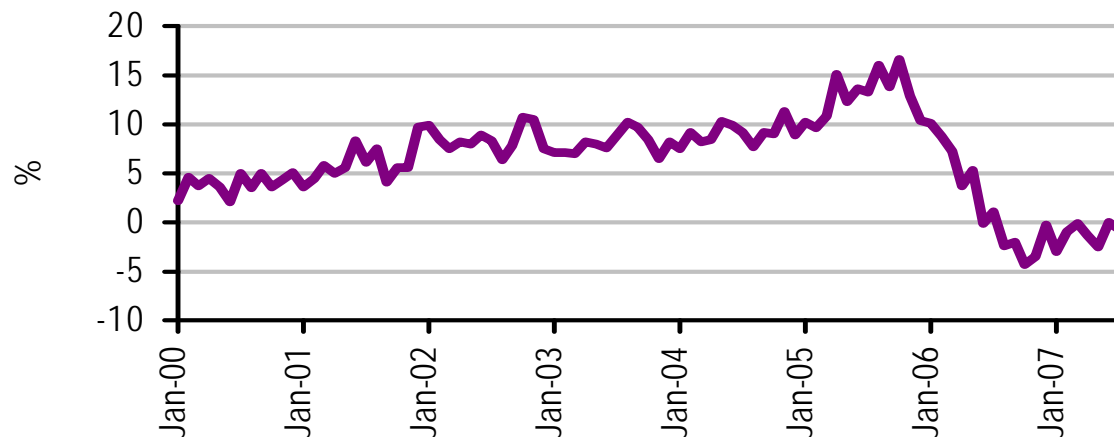
Last date: 8/31/07

Existing Home Prices Have Stalled

Existing Home Sales—Median Price



Existing Home Sales—Median Price Change YOY



Last date: 8/31/07

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