Financial Services Investing Perspectives
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How We Got Here....in 5 Slides

U.S. Total Debt\(^{(1)}\)

Source: Federal Reserve, Ned Davis Research.
Total debt includes domestic financial and non-financial debt plus foreign debt.
US Home Price Appreciation since 1900

How We Got Here....in 5 Slides

U.S. Mortgage Equity Withdrawals

(% of disposable income, 4-quarter moving average)

Source: Haver, BEA, NAHB, Conference Board, EIA, Morgan Stanley Research.
The financial obligations ratio is an estimate of the ratio of debt payments to disposable personal income. Debt payments consist of required payments on outstanding mortgage, consumer debt, automobile lease payments, rental payments on tenant-occupied property, homeowners’ insurance, and property tax payments.
### How We Got Here....in 5 Slides

<table>
<thead>
<tr>
<th>Savings Rate</th>
<th>Amount ($bn)</th>
<th>% Reduction</th>
<th>% of GDP</th>
<th>Consumption % of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.0%</td>
<td>(32)</td>
<td>(0.3%)</td>
<td>(0.2%)</td>
<td>74.1%</td>
</tr>
<tr>
<td>3.0%</td>
<td>182</td>
<td>1.7%</td>
<td>1.3%</td>
<td>72.6%</td>
</tr>
<tr>
<td>5.0%</td>
<td>397</td>
<td>3.7%</td>
<td>2.8%</td>
<td>71.1%</td>
</tr>
<tr>
<td>7.0%</td>
<td>612</td>
<td>5.8%</td>
<td>4.3%</td>
<td>69.6%</td>
</tr>
<tr>
<td>9.0%</td>
<td>826</td>
<td>7.8%</td>
<td>5.8%</td>
<td>68.1%</td>
</tr>
<tr>
<td>11.0%</td>
<td>1,041</td>
<td>9.8%</td>
<td>7.3%</td>
<td>66.6%</td>
</tr>
<tr>
<td>13.0%</td>
<td>1,256</td>
<td>11.9%</td>
<td>8.8%</td>
<td>65.1%</td>
</tr>
<tr>
<td>15.0%</td>
<td>1,470</td>
<td>13.9%</td>
<td>10.3%</td>
<td>63.6%</td>
</tr>
<tr>
<td>17.0%</td>
<td>1,685</td>
<td>15.9%</td>
<td>11.8%</td>
<td>62.1%</td>
</tr>
<tr>
<td>19.0%</td>
<td>1,899</td>
<td>17.9%</td>
<td>13.3%</td>
<td>60.6%</td>
</tr>
<tr>
<td>21.0%</td>
<td>2,114</td>
<td>20.0%</td>
<td>14.7%</td>
<td>59.2%</td>
</tr>
</tbody>
</table>

Source: Federal Reserve Board Bureau of Economic Analysis; Research Estimates
Impact on Financial System Has Been Severe

- Massive duration mismatch for institutions outside the scope of the Federal Reserve system created liquidity crisis
- Fundamental insolvency of Fannie Mae and Freddie Mac
- Bank system capital adequacy / insolvency issues
- Housing prices / asset deflation
- Malfunction of overnight secured market due to counterparty concerns and varied treatment of derivative / repo exposure in different “bailouts”

- Good news is we’re making progress…..
  - Acronym brigade (TARP, CPP, TALF, SSFI, PDCF, TACF, etc….)
  - Nationalization of Fannie and Freddie
  - Some capital has been raised; banks being allowed to fail
  - Federal guarantees to help restart main funding markets

- But more progress needs to be made…..
  - Financial sector earnings will disappoint in Q4; more capital is needed
  - Asset deflation continues; home prices unlikely to bottom until Spring 2010
Financial Services Investing Perspectives

Where are we in the Credit Cycle?

Exhibit 5: We estimate cumulative losses of $1.8TN or 8% of outstandings estimated cumulative losses (starting in mid-2007) by product, $bn

<table>
<thead>
<tr>
<th>Product (bn)</th>
<th>Losses from US credit</th>
<th>Cumulative loss rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Subprime mortgage</td>
<td>312</td>
<td>22%</td>
</tr>
<tr>
<td>Home equity</td>
<td>115</td>
<td>10%</td>
</tr>
<tr>
<td>All other mortgage **</td>
<td>362</td>
<td>4%</td>
</tr>
<tr>
<td>Total mortgage</td>
<td>780</td>
<td>7%</td>
</tr>
<tr>
<td>Commercial real estate</td>
<td>234</td>
<td>7%</td>
</tr>
<tr>
<td>Cards</td>
<td>226</td>
<td>23%</td>
</tr>
<tr>
<td>Auto</td>
<td>133</td>
<td>12%</td>
</tr>
<tr>
<td>Commercial</td>
<td>390</td>
<td>6%</td>
</tr>
<tr>
<td>Total pre-tax losses</td>
<td>1,763</td>
<td>8%</td>
</tr>
<tr>
<td>Tax rate *</td>
<td>26%</td>
<td>--</td>
</tr>
<tr>
<td>Total after-tax losses</td>
<td>1,322</td>
<td>--</td>
</tr>
</tbody>
</table>

* Assumes 22.4% for Option ARM, 12.5% for Alt A, 1.6% for prime mortgages.

** 35% tax rate normally, but some losses come from failed institutions which don’t get a tax shield.

Source: Goldman Sachs Research.

Exhibit 6: Through the end of 3Q, $845bn of these losses are recognized write-downs, excess provisions, and failed institutions’ equity since mid-2007

<table>
<thead>
<tr>
<th>Gross Write-downs</th>
<th>US</th>
<th>Europe</th>
<th>Rest of the world</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brokers</td>
<td>97.0</td>
<td>79.7</td>
<td>0.9</td>
<td>177.5</td>
</tr>
<tr>
<td>Banks</td>
<td>212.7</td>
<td>111.0</td>
<td>14.2</td>
<td>338.0</td>
</tr>
<tr>
<td>Specialty Finance</td>
<td>37.4</td>
<td>--</td>
<td>--</td>
<td>37.4</td>
</tr>
<tr>
<td>Insurance &amp; Asset Mgr</td>
<td>38.8</td>
<td>6.6</td>
<td>--</td>
<td>45.4</td>
</tr>
<tr>
<td>Total</td>
<td>386.9</td>
<td>196.3</td>
<td>15.1</td>
<td>598.3</td>
</tr>
</tbody>
</table>

US Banks provision above trend (3Q07 - 3Q08)
Failed institutions’ equity 103.2

Note: Specialty Finance include Financial Cusitrons; Banks include C & JPM

Source: FDIC, Goldman Sachs Research.
### Financial Services Investing Perspectives

#### 5th Inning

<table>
<thead>
<tr>
<th>Estimated losses borne by banks</th>
<th>Capital for new on-balance sheet assets</th>
<th>Capital for future originations*</th>
<th>Tax shield for credit losses</th>
<th>Overall capital shortfall</th>
<th>Capital injections to date**</th>
<th>Additional gov’t capital injections planned</th>
<th>Remaining capital need</th>
</tr>
</thead>
<tbody>
<tr>
<td>1,460-1,910</td>
<td>80</td>
<td>140</td>
<td>440-570</td>
<td>1,240-1,550</td>
<td>710</td>
<td>320</td>
<td>210-520</td>
</tr>
</tbody>
</table>

* Reflects additional bank balance sheets assets due to reduction in securitization

**Includes government capital injections made prior to November 3, 2008

Source: Bank of England, Bloomberg WDCI; McKinsey analysis

Banks could get this by
- Raising external capital
- Retaining earnings
- De-leveraging
- Further government intervention

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* Source: Bank of England, Bloomberg WDCI; McKinsey analysis
We want to be the beneficiaries of forced and voluntary deleveraging of financial assets, particularly credit assets, globally.

- Large LBO Loans
- Residential Mortgages
- ABS
- Auto Loans
- Unsecured Loans
- CMBS / Commercial Mortgages

Our rules of the road for investing in distressed assets:

- Must have edge in terms of asset origination – proprietary “flow”
- Must have captive servicing capacity and ability to monitor credit
- All underwriting must be done on asset-by-asset basis with full re-underwriting of all collateral for secured loans. Need to have an “edge” which creates proprietary point of view on asset valuation / underwriting.
- Must partner with team with deep sector expertise on credit side, preferably with track record of purchasing assets in secondary market.
In October 2008, we completed a minority investment in Bayview Asset management ("Bayview")

- Bayview actively manages a $2 billion fund that purchases whole mortgage loans and mortgage-backed securities
- The Company operates a highly rated mortgage servicer that takes a high-touch approach toward servicing by having a lower loan count to employee ratio than any of its competitors
- Bayview fit our investment criteria as a platform that should benefit from the deleveraging of financial assets
  - They have been purchasing and originating loans for over 15 years and have deep sector expertise
  - Bayview has a full underwriting team that is able to analyze every credit they purchase
  - They own their servicing platform and are able to ensure that their assets are properly serviced in manner that optimizes value
- Our relationship with Bayview gives us a unique capability to analyze mortgage related credits and evaluate other potential opportunities
- Since we completed our investment, we have worked closely with Bayview on several potential transactions in which they have served as one of our lead advisors
We believe that the next 3 years will be unique opportunity to invest in depository sector in environment of significant distress.

Combination of factors leads to excellent investment opportunity:
  ▶ Availability of assisted transactions with FDIC
  ▶ Continued capital inadequacy at all levels of sector
  ▶ Dearth of quality management
  ▶ Pricing umbrella as large institutions re-price credit and deposits to allow them to return to profitability

Opportunity not replicable in publicly traded banks due to legacy issues discussed previously and their need to deleverage

Bayview allows us to analyze thrift and bank balance sheets for credit risk
Financial services are highly cyclical by sub sector, but these cycles of capital formation / destruction create opportunity for strong companies who expand at the trough.

<table>
<thead>
<tr>
<th>Sector</th>
<th>Peak - Peak</th>
<th>Trough - Peak</th>
<th>Trough - Peak Period</th>
<th>Current Peak - Trough</th>
</tr>
</thead>
<tbody>
<tr>
<td>P&amp;C Insurance</td>
<td>43.7%</td>
<td>110.6%</td>
<td>'00 - '02</td>
<td>(20.9%)</td>
</tr>
<tr>
<td>Life &amp; Health Insurance</td>
<td>31.1%</td>
<td>75.1%</td>
<td>'02 - '04</td>
<td>(34.9%)</td>
</tr>
<tr>
<td>Commercial Finance</td>
<td>5.8%</td>
<td>107.2%</td>
<td>'99 - '02</td>
<td>(49.5%)</td>
</tr>
<tr>
<td>Depositories</td>
<td>93.6%</td>
<td>215.8%</td>
<td>'90 - '93</td>
<td>(60.6%)</td>
</tr>
</tbody>
</table>

Source: Factset. Represents indexed stock price change of industry groups. It is for information purposes only and is not meant to be indicative of the potential performance of Stone Harbor.
Banking sector today presents profound dislocation in valuation – “6σ” event.

Range of Historical Multiples
(Distribution of Daily Historic Price-to-Book Multiples 2002-2007)

When overlaid against 1989–1991 cycle, the opportunity becomes more apparent

Source: Piper Jaffray, SNL Financial, Capital IQ.

Source: Represents indexed stock price change of SNL Bank and Thrift Index per SNL Financial. SNL Bank and Thrift Index includes all banks and thrifts listed on major exchanges (NYSE, AMEX, NASDAQ) in SNL's coverage universe.
Investment activities will be based on the following four strategies in the U.S. small and mid cap bank / thrift and specialty finance segments:

A. Regional Bank Acquisition Roll-Ups

B. Failed Banks / Thrifts

C. Special Bank Situations

D. Specialty Finance Companies
## Value Creation

### Strategy

#### A. Regional Bank Acquisition Roll Ups

- $250 million to $5.0 billion “healthy” banks / thrifts across attractive metropolitan areas
- Gain scale
- Transform pro forma business model to industry best practices
- Acquire at low multiples
- Reduce costs through de-duplication and efficiencies
- Grow retail / commercial revenue streams
- Sell improved earnings at growth multiples

#### B. Failed Banks / Thrifts

- Acquire failed banks / thrifts
- No assumption of bad assets
- Gain scale
- Transform and grow core franchise
- Buy in at low deposit premiums
- Grow revenues and improve cost / income of core franchise
- Sell improved earnings at growth multiples

#### C. Special Bank Situations

- Acquire banks / thrifts that are capital impaired
- Problem assets are limited and quantifiable
- Work out problem assets
- Transform pro forma business
- Buy in at distressed discounts
- Turn around problem assets
- Grow revenues and improve cost / income of core franchise
- Sell improved earnings at growth multiples

#### D. Specialty Finance Companies

- Buy specialty finance companies or de novo businesses by lifting out experienced management teams
- Leverage acquired banks’ clients through cross-sell
- Leverage acquired banks’ low cost funding
- Buy in at discount or de novo
- Recruit management expertise / skill set from the firm’s unique banking network
- Improve / grow franchise
- Sell improved earnings at growth multiples

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**Confidential**
I. Buy Right
- Depressed multiples
- Value core franchise
- Superior due diligence
- Credit exposure valuations
- Attractive demographics
- Scalable platform
- Address social issues

II. Integrate
- Efficient conversions
- Cost de-duplication
- Realize efficiencies of scale
- Centralize operations
- Centralize support functions (risk, HR, finance, legal, etc.)

III. Improve Core Franchise
- Focus on core deposits
- Add business banking
- Add commercial
- Add specialties
- Build fee businesses
- Wealth management
- Work out problem assets

IV. Grow Organically
- Sales culture
- Cross-sell
- Client acquisition
- Share of wallet
- Incentive alignment
- Recognition reward

V. Sell Right
- Growth multiples
- Sustained organic growth
- Improved business mix
- Superior earnings / fundamentals
- IPO

Acquire Anchor Franchise

Follow-Up Acquisitions

Realize Benefits of Scale

Improve Core Franchise Value

Organic Growth

Exit at Growth Multiples and Higher Earnings