

12 JUNE 2008

**Kaupthing Bank hf.**  
**Issue of €25,000,000 Global Duration Portfolio**  
**Excess Return Index Notes due 2013 under the €12,000,000,000**  
**Euro Medium Term Note Programme**

**PART A – CONTRACTUAL TERMS**

Terms used herein shall be deemed to be defined as such for the purposes of the Conditions set forth in the Base Prospectus dated 13 September, 2007 which constitutes a base prospectus for the purposes of the Prospectus Directive (Directive 2003/71/EC) (the "**Prospectus Directive**"). This document constitutes the Final Terms of the Notes described herein for the purposes of Article 5.4 of the Prospectus Directive and must be read in conjunction with the Base Prospectus. Full information on the Issuer and the offer of the Notes is only available on the basis of the combination of these Final Terms and the Base Prospectus. The Base Prospectus is available for viewing at the office of the Issuer at Borgartun 19, 105 Reykjavik, Iceland and copies may be obtained from the Principal Paying Agent at Winchester House, 1 Great Winchester Street, London EC2N 2DB.

*No person has been authorised to give any information or make any representation not contained in or not consistent with these Final Terms, or any other information supplied in connection with the Notes and, if given or made, such information or representation must not be relied upon as having been authorised by the Issuer or any Dealer.*

*By investing in the Notes each investor represents that:*

- (a) *Non-Reliance. It is acting for its own account, and it has made its own independent decisions to invest in the Notes and as to whether the investment in the Notes is appropriate or proper for it based upon its own judgement and upon advice from such advisers as it has deemed necessary. It is not relying on any communication (written or oral) of the Issuer or any Dealer as investment advice or as a recommendation to invest in the Notes, it being understood that information and explanations related to the terms and conditions of the Notes shall not be considered to be investment advice or a recommendation to invest in the Notes. No communication (written or oral) received from the Issuer or any Dealer shall be deemed to be an assurance or guarantee as to the expected results of the investment in the Notes.*
- (b) *Assessment and Understanding. It is capable of assessing the merits of and understanding (on its own behalf or through independent professional advice), and understands and accepts the terms and conditions and the risks of the investment in the Notes. It is also capable of assuming, and assumes, the risks of the investment in the Notes.*
- (c) *Status of Parties. Neither of the Issuer nor any Dealer is acting as a fiduciary for or adviser to it in respect of the investment in the Notes.*

Investors should refer to the section entitled "Risk Factors" in the Base Prospectus for a discussion of certain risks associated with an investment in the Notes. In addition, investors should also note the specific risk factors set out in Annex B.

1. Issuer: Kaupthing Bank hf.
2. (i) Series Number: 20  
(ii) Tranche Number: 1
3. Specified Currency or Currencies: Euro (€)
4. Aggregate Nominal Amount:  
(i) Series: €25,000,000  
(ii) Tranche: €25,000,000
5. Issue Price: 100 per cent. of the Aggregate Nominal Amount
6. (i) Specified Denominations: €100,000  
  
(ii) Calculation Amount: Not Applicable
7. (i) Issue Date: 12 June 2008  
(ii) Interest Commencement Date: 12 June 2008
8. Maturity Date: Interest Payment Date falling on or nearest to 12 June 2013, as modified in accordance with the applicable Business Day Convention
9. Interest Basis: Index Linked Interest (further particulars specified below)
10. Redemption/Payment Basis: Redemption at par
11. Change of interest basis or redemption/ payment basis: Not Applicable
12. Put/Call Options: Not Applicable
13. (a) Status of the Notes: Senior  
(b) Date Board approval for issuance of notes obtained: Not Applicable
14. Method of distribution: Non-syndicated

## PROVISIONS RELATING TO INTEREST (IF ANY) PAYABLE

- |     |  |   |
|-----|--|---|
| 15. | <b>Fixed Rate Note Provisions</b>  | Not Applicable  |
| 16. | <b>Floating Rate Note Provisions</b>   | Not Applicable  |
| 17. | <b>Zero Coupon Note Provisions</b>   | Not Applicable  |
| 18. | <b>Index Linked Interest Note Provisions</b>   | Applicable  |
|     | (i) Index/Formula:   | See Annex A   |
|     | (ii) Party responsible for calculating the Rate of Interest (if not the Calculation Party Agent) and Interest Amount (if not the Agent): | Lehman Brothers International (Europe) or any successor thereof (the " <b>Calculation Agent</b> "). All determinations made by the Calculation Agent for the purposes of the Notes will be made in good faith and, in the absence of manifest error, wilful default or bad faith, will be final and conclusive and neither the Issuer nor the Calculation Agent will have any liability to the Noteholders or any third party in relation to such determinations. |
|     | (iii) Provisions for determining Coupon where calculation by reference to Index and/or Formula is impossible or impracticable:           | See Annex A   |
|     | (iv) Specified Period(s)/Specified Interest Payment Dates:   | The specified Interest Payment Dates shall be 12 June in each year from and including 12 June 2009 to and including the Maturity Date, in each case subject to modification in accordance with the Business Day Convention.   |
|     | (v) Business Day Convention:   | Following Business Day Convention   |
|     | (vi) Additional Business Centre(s):  | New York, London and TARGET   |
|     | (vii) Minimum Rate of Interest:  | 4.25 per cent. per annum  |
|     | (viii) Maximum Rate of Interest:   | 16 per cent. per annum  |

- (ix) Day Count Fraction: Act/360. For the purposes of calculating the Day Count Fraction, the actual number of days in the relevant Interest Period shall be adjusted in accordance with the Business Day Convention.
19. **Equity Linked Interest Note Provisions** Not Applicable
20. **Commodity Linked Interest Note Provisions** Not Applicable
21. **Additional Disruption Events (applicable to Equity Linked Interest Notes only):** Not Applicable
22. **Dual Currency Interest Note Provisions** Not Applicable
23. Target Redemption Note Provisions: Not Applicable
24. Range Accrual Note Provisions: Not Applicable

#### **PROVISIONS RELATING TO REDEMPTION**

25. Issuer Call: Not Applicable
26. Investor Put Not Applicable
27. Target Redemption Note Provisions: Not Applicable
28. Final Redemption Amount €100,000 per Specified Denomination
29. Early Redemption Amount: €100,000 per Specified Denomination

Early Redemption Amount payable on redemption for taxation reasons or on event of default or on an illegality (or, in the case of the Equity Linked Notes, following a De-listing and/or Merger Event and/or Nationalisation and/or Insolvency and/or Tender Offer in accordance with Condition 9(b)(ii)(b) or, following an

Additional Disruption Event (if applicable) or, in the case of Credit Linked Notes, following a Merger Event, and/or the method of calculating the same (*required if Early Redemption Amount different from that set out in Condition 7(f)*):

- |     |   |                |
|-----|---|----------------|
| 30. | Capital Notes Provisions  | Not Applicable |
| 31. | Equity Linked Redemption Notes:   | Not Applicable |
| 32. | Additional Disruption Events (applicable to Equity Linked Redemption Notes only): | Not Applicable |
| 33. | Credit Linked Notes:  | Not Applicable |
| 34. | Commodity Linked Redemption Notes:  | Not Applicable |

#### **GENERAL PROVISIONS APPLICABLE TO THE NOTES**

- |     |   |   |
|-----|---|---|
| 35. | (a) Form of Notes:  | Temporary Global Note exchangeable for a Permanent Global Note which is exchangeable for Definitive Notes only upon an Exchange Event |
|     | (b) New Global Note:  | Yes   |
| 36. | Additional Financial Centre(s) or other special provisions relating to Payment Dates:   | Not Applicable  |
| 37. | Talons for future Coupons or Receipts to be attached to Definitive Notes (and dates on which such Talons mature):   | No  |
| 38. | Details relating to Partly Paid Notes: amount of each payment comprising the Issue Price and date on which each payment is to be made and, consequences (if any) of failure to pay, including any right of the Issuer to forfeit the Notes and interest due | Not Applicable  |

on late payment:

39. Details relating to Instalment Notes:
- (i) Instalment Amount(s): Not Applicable
  - (ii) Instalment Date(s): Not Applicable
40. Redenomination applicable: Redenomination not applicable
41. Other final terms: Not Applicable

#### **DISTRIBUTION**

42. (i) If Syndicated, Names of Managers: Not Applicable
- (ii) Date of Subscription Agreement: Not Applicable
- (iii) Stabilising Manager (if any): Not Applicable
43. If non-syndicated, name and address of relevant Dealer: Kaupthing Bank hf. Borgartun 19
44. U.S. Selling Restrictions: Reg. S Category 2; TEFRA D
45. Additional selling restrictions: Not Applicable

#### **PURPOSE OF FINAL TERMS**

These Final Terms comprise the final terms required for issue and admission to trading on the Luxembourg Stock Exchange's regulated market and for listing on the Official List of the Luxembourg Stock Exchange of the Notes described herein pursuant to the €12,000,000,000 Euro Medium Term Note Programme of Kaupthing Bank hf.

**RESPONSIBILITY**

The Issuer accepts responsibility for the information contained in these Final Terms.

Signed on behalf of the Issuer:

By: Steingimur Lein  
Duly authorised

DAVIA STEFANSSON

## PART B – OTHER INFORMATION

### 1. LISTING AND ADMISSION TO TRADING

- (i) Admission to Trading: Application has been made by the Issuer (or on its behalf) for the Notes to be admitted to trading on the Luxembourg Stock Exchange's regulated market and to be listed on the Official List of the Luxembourg Stock Exchange with effect from 16 June 2008
- (ii) Estimate of total expenses related to trading: €3,550

### 2. RATINGS

- Ratings: The Notes to be issued have been rated:
- Moody's: A1
- Fitch: A-

### 3. INTERESTS OF NATURAL AND LEGAL PERSONS INVOLVED IN THE ISSUE

Save for any fees payable to the Dealer so far as the Issuer is aware, no person involved in the issue of the Notes has an interest material to the offer.

### 4. REASONS FOR THE OFFER, ESTIMATED NET PROCEEDS AND TOTAL EXPENSES

- (i) Reasons for the Offer: Not Applicable
- (ii) Estimated Net Proceeds: Not Applicable
- (iii) Estimated Total Expenses: Not Applicable

### 5. YIELD

- Indication of yield: Not Applicable

### 6. PERFORMANCE OF INDEX/FORMULA, EXPLANATION OF EFFECT ON VALUE OF INVESTMENT AND ASSOCIATED RISKS AND OTHER INFORMATION CONCERNING THE UNDERLYING INDEX (Index-Linked Notes only)

The Note is a product with a highly leverage exposure to the Lehman Brothers Global DURATION Portfolio Excess Return Index. The Index is composed of two individual trading strategies; the G-6 Duration Timing Strategy and the G-5 Cross-Country Yield



Spread Strategy. Further details of these strategies are set out in Annex C. The Interest Amount of the Notes is dependent upon the level of the Index as at the Issue Date and the performance of the Index thereafter up to and including the end of the Interest Period in respect of which such Interest Amount is being paid. As a result any negative performance of the Index in respect of one Interest Period may have a negative impact in respect of the subsequent Interest Periods.

The Notes have a 10 times leveraged exposure to the performance of the Index. The Noteholders will therefore be exposed to the performance of the Index on a leveraged basis.

The level of the Index will be published on the Bloomberg Page LBGLDREU or any successor page that may from time to time publish a level of the Index as determined by the Calculation Agent in its sole discretion.

The performance of the Index (as defined below) may affect the nature and value of the investment return on this Note. In particular, the value of this Note may fluctuate based on the performance of the Index. Selling this Note prior to the Maturity Date may result in a price less than 100% of the Final Redemption Amount of the notes sold, and therefore a potential loss of principal.

Prospective purchasers of this Note should conduct their own investigations and, in deciding whether or not to purchase this Note, form their own views of the merits of an investment related to the Index based upon such investigations and not in reliance on any information given in these Final Terms.

Further details of the risks associated with the Notes are set out in Annex B.

7. **PERFORMANCE OF [THE EQUITY/BASKET OF EQUITIES], EXPLANATION OF EFFECT ON VALUE OF INVESTMENT AND ASSOCIATED RISKS [AND OTHER INFORMATION CONCERNING [THE EQUITY/BASKET OF EQUITIES]]** (*Equity Linked Notes only*)

Not Applicable.

8. **PERFORMANCE OF [THE COMMODITY/BASKET OF COMMODITIES], EXPLANATION OF EFFECT ON VALUE OF INVESTMENT AND ASSOCIATED RISKS [AND OTHER INFORMATION CONCERNING [THE COMMODITY/BASKET OF COMMODITIES]]** (*Commodity Linked Notes only*)

Not Applicable

9. **INFORMATION IN RELATION TO THE REFERENCE ENTITY, EXPLANATION OF EFFECT ON VALUE OF INVESTMENT AND ASSOCIATED RISKS [AND OTHER INFORMATION CONCERNING THE REFERENCE ENTITY]** (*Credit Linked Notes only*)

Not Applicable

10. **PERFORMANCE OF RATE[S] OF EXCHANGE** (*Dual Currency Notes only*)

Not Applicable

11. **OPERATIONAL INFORMATION**

- (i) ISIN Code: XS0368372925
- (ii) Common Code: 036837292
- (iii) Any clearing system(s) other than Euroclear Bank S.A./N.V. and Clearstream Banking, Société Anonyme and the relevant identification number(s): Not Applicable
- (iv) Delivery: Delivery against payment
- (v) Names and addresses of additional Paying Agent(s) (if any): Not Applicable
- (vi) Intended to be held in a manner which would allow Eurosystem eligibility: Yes

## ANNEX A

For the purposes of Condition 5(b)(ii) and subject to Condition 5(b)(iii), the Rate of Interest payable from time to time in respect of the Notes shall be determined by the Calculation Agent in accordance with the following formula (expressed as a percentage rate per annum):

$$12 \text{ month Euribor} + 2.75 \text{ per cent} - 10 \times (\text{Index Annualised Cumulative Return}_N - 0.725\%)$$

where:

"12 month Euribor" means, in respect of each Interest Period, either;

- (a) the offered quotation; or
- (b) the arithmetic mean (rounded if necessary to the fifth decimal place, with 0.000005 being rounded upwards) of the offered quotations,

(expressed as a percentage rate per annum) for the Euro-zone inter-bank offered rate ("Euribor") for 12 month deposits of euro which appears or appear, as the case may be, on Reuters Page EURIBOR01 (or any successor page as determined by the Calculation Agent) (the "Relevant Screen Page") as at 11.00 a.m. (Brussels time) on the day falling two Business Days immediately preceding the start of such Interest Period. If five or more of such offered quotations are available on the Relevant Screen Page, the highest (or, if there is more than one such highest quotation, one only of such quotations) and the lowest (or, if there is more than one such lowest quotation, one only of such quotations) shall be disregarded by the Calculation Agent for the purpose of determining the arithmetic mean (rounded as provided above) of such offered quotations.

The Agency Agreement contains provisions for determining the Rate of Interest in the event that the Relevant Screen Page is not available or if, in the case of (1) above, no such offered quotation appears or, in the case of (2) above, fewer than three such offered quotations appear, in each case as at the time specified in the preceding paragraph.

For these purposes:

The "Index Annualized Cumulative Return<sub>N</sub>" shall be expressed as a percentage amount and shall in respect of each Interest Period N (N=1, 2, 3, 4 and 5) be the product of:

- (i)  $1/N$ ; and
- (ii)  $[(\text{Index}_N/\text{Index}_0) - 1]$

"Index<sub>N</sub>" means in respect of any Interest Period, the Index Closing Level of the Index as determined by the Calculation Agent in its sole discretion ten Index Business Days prior to the last Index Business Day of such Interest Period.

"Index<sub>0</sub>" means the Index Closing Level of the Index ten Index Business Days prior to the Issue Date as determined by the Calculation Agent in its sole discretion.

## 1. CERTAIN OTHER DEFINITIONS

The following words and expressions shall have the following meanings:

**"Business Day"**: means a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in London, New York and TARGET.

**"Business Day Convention"**: means the Following Business Day Convention.

**"Index"**: means Lehman Brothers Global DURATION Portfolio Excess Return Index.

**"Index Business Day"**: means each day on which the Index Sponsor is scheduled to calculate and publish the level of such Index, provided that each such day is also a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in London, New York and TARGET.

**"Index Closing Level"**: means, in respect of any day, the official closing level of that Index (as determined by the Calculation Agent), as made public by the Index Sponsor on the Price Source at or after the Relevant Time on such day, or as otherwise determined by the Calculation Agent in its sole and absolute discretion.

**"Index Sponsor"**: means, Lehman Brothers International (Europe), or any Successor Index Sponsor.

**"Price Source"**: means Bloomberg Page LBGLDREU or any successor page that may from time to time publish a level of the Index as determined by the Calculation Agent in its sole discretion.

**"Relevant Time"**: means 5:00 p.m. London time.

**"Successor Index Sponsor"**: means, in respect of an Index Sponsor, any successor in title or corporation(s) or other entity/ies that is the successor to the Index Sponsor as determined by the Calculation Agent in its sole discretion.

## 2. INDEX DISRUPTION

If the Calculation Agent determines that a level of the Index cannot be determined on any date on which it is required for any reason (a **"Index Disruption Event"**), (i) the Calculation Agent will instead use the level of the Index determined in respect of the next following Index Business Day on which such a level is determined; provided that (ii) if a level cannot be determined in respect of each of the next 8 such following Index Business Days, it may, acting in its sole discretion and in a commercially reasonable manner, choose an appropriate alternative Index (the **"Substitute Index"**) whose investment objective as closely as possible reflects or is representative of the investment objective of the original Index, provided however that for this purpose the Calculation Agent, acting in its sole discretion and in a commercially reasonable manner, may make such adjustments to the Substitute Index as it deems necessary.

If the Calculation Agent determines in its sole and absolute discretion that there is no appropriate alternative Index, the Issuer may elect to redeem the Notes by giving notice to the Noteholders in accordance with Condition 18 of such situation and the Early Redemption Amount (as defined in paragraph 29 of Part A) shall be payable in respect of each Note on the date specified in such notice.

3. **INDEX ADJUSTMENT**

In the event that there is any error in relation to calculation or publication of the level of the Index, the Calculation Agent will make such adjustments to each previously and/or subsequently published level of the Index that are necessary (acting in its sole discretion and in a commercially reasonable manner) in order to rectify such error (provided that no adjustment will be made to amounts already paid under the Notes).

4. **REBASING**

If the Calculation Agent determines that an Index has been or will be rebased at any time, the Index as so rebased (the "**Rebased Index**") will be used for the purpose of determining the level of an Index from the date of such rebasing; provided, however, that the Calculation Agent shall make such adjustments, if any, to the levels of the Rebased Index so that the Rebased Index levels reflects a similar level of the Index before it was rebased. Any such rebasing shall not affect any prior payments made under the Notes.

5. **PRICE SOURCE DISRUPTION**

In the event that, in the sole determination of the Calculation Agent, the Price Source fails to publish a level for the index on any day, the Calculation Agent will use the level of the Index determined in its sole discretion.

6. **INDEX DISCLAIMER**

Each of the Issuer and the Noteholders agrees and acknowledges, in respect of the Index, that the Notes are not sponsored, endorsed, sold or promoted by the Index Sponsor and the Index Sponsor makes no representation whatsoever, whether express or implied, either as to the results to be obtained from the use of such Index and/or the levels at which such Index stands at any particular time on any particular date or otherwise. The Index Sponsor shall not be liable (whether in negligence or otherwise) to any person for any error in such Index and such Index Sponsor is under no obligation to advise any person of any error therein. The Index Sponsor is making no representation whatsoever, whether express or implied, as to the advisability of purchasing or assuming any risk in connection with the Notes. The Issuer and the Calculation Agent shall have no liability to the Noteholders for any act or failure to act by the Index Sponsor in connection with the calculation, adjustment or maintenance of the Index. Although the Calculation Agent will obtain information concerning the Index from publicly available sources it believes reliable, it will not independently verify this information. Accordingly, no representation, warranty or undertaking (express or implied) is made and no responsibility is accepted by the Issuer or its affiliates or the Calculation Agent as to the accuracy, completeness and timeliness of information concerning the Index.

## ANNEX B RISK FACTORS

In addition to the Risk Factors set out on pages 19 to 33 of the Base Prospectus, investors should consider the following factors in connection with an investment in the Notes. The following factors do not purport to be a comprehensive enumeration or explanation of the risks associated with the Index.

The Buyer of these Notes is responsible for its own independent analysis of and decision regarding all matters relating to their purchase and any applicable laws and regulations and the risks involved in the purchase as they relate to the Buyer's own circumstances. The Buyer should consult its own counsel, accountants and other advisors on these and all matters it deems relevant. These Notes are suitable only for, and should be purchased only by an investor who has no need for liquidity and understands and can afford the financial and other risks of an investment in the Notes. Investors in the Notes should be aware that members of the Lehman Brothers group perform multiple roles in connection with the Notes and the Index, some of which may involve them having interests and motivations which conflict with those of the Investors. Lehman Brothers may or may not enter into transactions on sub-components of the Index or which replicate the Index or which reference the Index. Lehman Brothers will have no duty to inform any Investors of such transactions.

### **Lack of Operating History**

The Lehman Brothers Global DURATION Portfolio Excess Return Index has only recently been established as a tradeable strategy and therefore has no history to evaluate its likely performance. Any back-testing or similar analysis performed by any person in respect of the Index must be considered illustrative only and may be based on estimates or assumptions not used by Lehman Brothers International (Europe) when determining the Index Closing Level.

Past performance should not be considered indicative of future performance.

### **Principal Protection**

The principal amount repayable on redemption is not linked to the performance of the Index. Investors should be aware, however, that receipt of this principal repayment at maturity is dependent on the credit worthiness of the Issuer at such time and the secondary market value of the Notes at any time may be significantly less than the amount originally invested.

### **Return**

The Interest Amount of the Notes is dependent upon the level of the Index as at the Issue Date and the performance of the Index thereafter up to and including the end of the Interest Period in respect of which such Interest Amount is being paid. As a result any negative performance of the Index in respect of one Interest Period may have a negative impact in respect of the subsequent Interest Periods.

The Notes have a 10 times leveraged exposure to the Index. The Noteholders will therefore be exposed to the inverse performance of the Index on a leveraged basis.

**No assurance can be given that the assumptions on which the Index is based will successfully meet any stated investment objective.**

## **Liquidity Risk**

The purchase of the Notes by the Noteholders is intended to be a long term investment.

## **Amendments to the Index**

Lehman Brothers International (Europe) as calculation agent with respect to the Index may, in the event that there is any error in relation to calculation or publication the level of the Index, make such adjustments to each previously and /or subsequently published level of the Index as it deems necessary (in its sole discretion) in order to rectify such error.

## **Potential Conflicts of Interest**

Lehman Brothers International (Europe) is the Calculation Agent under the Notes and is also the calculation agent responsible for calculating the Index Closing Level of the Index. Potential conflicts of interest may exist in the structure and operation of the Index and the course of the normal business activities of the Lehman Brothers International (Europe) and any of its affiliates or subsidiaries or their respective directors, officers, employees, representatives, delegates or agents (each a "**Relevant Person**").

During the course of their normal business, each Relevant Person may enter into or promote, offer or sell transactions or investments (structured or otherwise) linked to the Index and/or any of its sub-components. In addition, any Relevant Person may have, or may have had, interests or positions, or may buy, sell or otherwise trade positions in or relating to the Index or any of the sub-components, or may invest or engage in transactions with other persons, or on behalf of such persons relating to the Index or any of these sub-components. Such activity may or may not have an impact on the Index Closing Level of the Index but all persons reading this document should be aware that a conflict of interest could arise where anyone is acting in more than one capacity, and such conflict may have an impact, positive or negative on the Index Closing Level of the Index. Neither Lehman Brothers International (Europe) nor any other Relevant Person has any duty to consider the circumstances of any person when participating in such transactions or to conduct themselves in a manner that is favourable to anyone with exposure to the Index.

**The foregoing list of risk factors is not intended to be exhaustive. All persons should seek such advice as they consider necessary from their professional advisors, legal, tax or otherwise, without reliance on the Lehman Brothers International (Europe) or any of its affiliates, subsidiaries or any of their respective directors, officers, employees, representatives, delegates or agents.**

**Investors should be aware that the Index is proprietary to Lehman Brothers and not replicable. Investors should satisfy themselves that they understand the rationale behind the methodology underlying the strategy following any such additional due diligence as they feel to be necessary. In particular, investors should consider the consequences if any of the assumptions underlying such rationale should prove not to hold true (the prospect of which may be realised at any time but may be more likely in times of economic stress or market dislocation).**



**ANNEX C**  
**THE LEHMAN BROTHERS GLOBAL DURATION PORTFOLIO EXCESS**  
**RETURN STRATEGY**

**OVERVIEW**

The following is a description of the Lehman Brothers Global DURATION Portfolio Excess Return Strategy and the methodology behind the G-6 Duration Timing and G-5 Cross-Country Yield Spread Strategies. The Global DURATION Portfolio Excess Return Strategy is the intellectual property of Lehman Brothers International (Europe) and Lehman Brothers International (Europe) reserves all rights with respect to its ownership of the Global Duration Portfolio Excess Return Index and its methodology.

**What is Global DURATION Portfolio Excess Return Strategy?**

The Global DURATION Portfolio Excess Return Strategy Index is comprised of two individual trading strategies; the G-6 Duration Timing and the G-5 Cross-Country Yield Spread Strategies.

Whereas the G-6 Duration Timing Strategy provides directional macro views on the G-6 bond markets by using signals based on fundamental and financial market indicators, the G-5 Cross-Country Yield-Spread Strategy involves the positioning in cross-country bond yield spreads in the G-5 markets based on indicators of relative risk-premia. The G-6 Duration Timing Strategy and the G-5 Cross-Country Yield Spread Strategy are further described below.

**What is the investment objective behind the Global DURATION Portfolio Excess Return Strategy Index?**

The objective of the Global DURATION Portfolio Excess Return Strategy Index is to use a wide range of macroeconomic and financial markets information to exploit apparently predictable variations in bond excess returns. The Global DURATION Portfolio Excess Return Strategy and its sub-strategies, the G-6 Duration Timing and the G-5 Cross-Country Yield Spread Strategies, utilize signals based on macro economic and financial market information (including business cycles, inflationary pressures, investor risk aversion and rate factors) as signals of approximate market expectations about business cycles (bullish or bearish) and/or financial market conditions (risk favouring or risk averse) and, on the basis of observed historical sensitivities of various financial market indicators to such signals, to trade government bond futures in a systematic manner in response to these signals. There is no assurance that this investment objective will be achieved by the strategies nor that the observed historical sensitivity of such financial market indicators to such signals will continue.

**Who designed the Global DURATION Portfolio Excess Return Index and who calculates it?**

The Global DURATION Portfolio Excess Return Index and any variation thereof is a proprietary index that Lehman Brothers International (Europe) developed and calculates. Lehman Brothers International (Europe) or any affiliate or subsidiary of its designation will act as Calculation Agent for the Index. The Calculation Agent will calculate the level of the Index on each Index Business Day, subject to certain circumstances identified below. The

Calculation Agent's determination with respect to the Index and interpretation of the methodologies, rules and calculations relating to any Index will be final. The methodology for determining the composition of the Index and for calculating its values is subject to modification by the Calculation Agent under certain circumstances, as discussed below.

**When and where are levels for the Global DURATION Portfolio Excess Return Index published?**

Levels for the Global DURATION Portfolio Excess Return Index are published after 5 p.m.(London time) on each Index Business Day, which for purposes of the Global DURATION Portfolio Excess Return Index is any day that is both a London, New York and TARGET Business Day. Levels for the Global DURATION Portfolio Excess Return Index can be found on the Bloomberg page LBGLDREU or any successor source page that may from time to time publish a level of the Index as determined by the Calculation Agent in its sole discretion.

**G-6 Duration Timing Strategy**

The G-6 Duration Timing Strategy trades 2-year government bond futures or the nearest liquid alternative. Approximately 85% of the overall historical risk of the Global Duration Portfolio Excess Return Strategy is taken by the G-6 Duration Timing Strategy with the following weights for each of the following geographies: United States (25%), EU (25%), UK (15%), Japan (15%), Canada (10%) and Australia (10%).

The G-6 Duration Timing Strategy signals are generated by using the following four indicators:

- (a) *Business Cycle*: The signals for this category are based on business cycle indicators which provide a view of the stages of the economic cycle and the shocks to growth expectations;
- (b) *Inflationary Pressures*: The signals for this category are based on inflationary pressures indicators and the level and changes in inflation;
- (c) *Investor Risk Aversion*: The signals for this category are based on investor risk aversion indicators which attempt to measure the long term and short term shocks to investor wealth; and
- (d) *Rate Factors*: The signals for this category are based on rate factors indicators which give an indication of the momentum in bond prices and the slopes of the yield curve.

The G-6 Duration Timing Strategy uses a number of economic data and price data series to calculate the signals. Each signal is determined by using the current value of the economic variable and comparing it to its long-term average (known as the z-score). This quantity is normalized by dividing it with the standard deviation and the result is capped and floored at +1 and -1.

By combining the signals from the above indicators, the G-6 Duration Timing Strategy forms an overall view on the direction (long/short) and magnitude (between -1 and 1) of each contract. The index signals are generated daily and the futures positions are adjusted accordingly.

Since individual futures prices vary in terms of volatility, a constant volatility scaling factor (based on the historical volatility of each respective futures price) is used.

## **G-5 Yield Spread Strategy**

As previously mentioned, the G-5 Yield Spread Strategy involves the positioning in cross-country bond yield spreads of the G-5 market pairs based on indicators of relative risk-premium. The G-5 Yield Spread Strategy trades 10-year government bond futures and approximately 15 % of the overall historical risk taken by the Global DURATION Portfolio Excess Return Strategy is assigned to this part of the strategy with the following weights for each cross-geography: US/EU (25%), US/AU (25%), US/JN (25%), EU/UK (25%).

The G-5 Yield Spread Strategy compares the relative steepness of pairs of yield curves. Each signal is determined by using the current value of the economic variable and comparing it to its long-term moving (or z-score). This quantity is normalized by dividing it with the standard deviation and the result is capped and floored at +1 and -1.

A trading position is also implemented which reflects the strength of each signal for each futures contract. The index signals are generated daily and the futures positions are adjusted accordingly.

Since individual futures prices differs in terms of volatility, a constant volatility scaling factor (based on the historical volatility of each respective futures prices) is used.

The daily return on the Index is calculated as the aggregate daily returns on each of the futures positions. The daily profit and loss record is denominated in euro using a daily FX adjustment.



Reykjavik Iceland, 11<sup>th</sup> of June 2008

To the attention of Ranji Punnoose-Thomas.

Please deliver free of payment with value on June 12<sup>th</sup>, 2008 the following note to Arion's EUROCLEAR account 98822.

*ISIN Kaupthing Bank XS0368372925 nominal value EUR 25,000,000 –  
Issue date June 12, 2008*

Authorised signatures:

Guðný Arna Sveinsdóttir

**Guðný Arna Sveinsdóttir**  
Framkvæmdastjóri fjármála  
Chief Financial Officer