

COMPANY UPDATE

Merrill Lynch & Co., Inc. (MER)

Buy

Perfect Storm has MER squarely in its sights; lowering estimates

What's changed

We are significantly lowering our 3Q and 2007 estimates on MER to \$0.15/\$6.75 from \$1.95/\$9.05 to account for an extremely challenging operating environment in 3Q2007. These estimates include a multi-billion dollar write down due to weakness in mortgages, leveraged loans, and CDO's. We are also marginally lowering our 2008-2009 estimates and reducing our price target to \$94 from \$108.

Implications

We are lowering estimates following a weak reporting season from the November year-end brokers. MER appears to be caught in the cross hairs of a number of headwinds in the quarter – leveraged loan losses, mark to market losses on their CDO exposure, and deteriorating mortgage fundamentals. Our new estimates assume the firm will post a \$1.5 bn loss in its FICC business which is likely to include multi-billion dollar write-downs and losses. MER should receive some stability from its GWM business and 49.8% ownership of BLK, but not likely enough to offset what could turn out to be very poor results in the GMI business.

Valuation

MER currently trades at 1.6x current book value, compared with its 3-year average P/BV multiple of 2.0x. Our new \$94 price target assumes the stock will trade at 1.9x our 2Q2008 book value in twelve months.

Key risks

Risks to our view include (1) a sustained slowdown in the global equity markets, (2) a substantial credit spread widening, and (3) ongoing deterioration in consumer credit and confidence.

Impact on related securities

Although we are only lowering estimates on MER today, we believe the other firms in our universe that report earnings in October are at risk but their product diversity could shield them more than MER.

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Brokers & Asset Managers

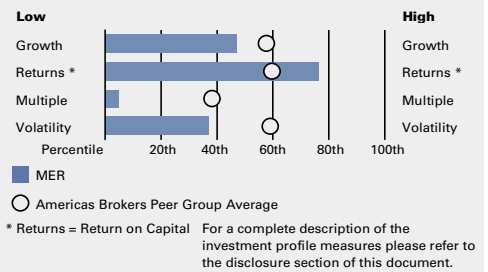
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Investment Profile: Merrill Lynch & Co., Inc.

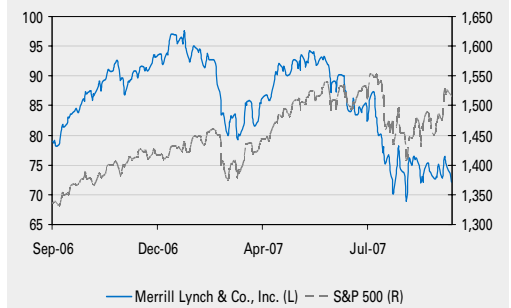


Key data	Current
Price (\$)	72.12
12 month price target (\$)	94.00
Market cap (\$ mn)	67,086.0

	12/06	12/07E	12/08E	12/09E
Revenue (\$ mn) New	34,659.0	32,669.7	40,725.0	44,382.0
Revenue (\$ mn) Old	34,659.0	37,789.7	41,315.0	44,782.0
EPS (\$) New	7.60	6.75	10.00	11.00
EPS (\$) Old	7.60	9.05	10.25	11.10
P/E (X)	9.5	10.7	7.2	6.6
P/B (X)	2.3	1.6	1.3	1.1
ROE (%)	21.2	17.0	23.1	23.0

	6/07	9/07E	12/07E	--
EPS (\$)	2.24	0.15	2.09	--

Price performance chart



Share price performance (%)	3 month	6 month	12 month
Absolute	(14.1)	(15.8)	(8.1)
Rel. to S&P 500	(15.2)	(20.3)	(19.7)

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 9/25/2007 close.

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Merrill Lynch & Co., Inc.: Summary financials

Profit model (\$ mn)	12/06	12/07E	12/08E	12/09E	Balance sheet (\$ mn)	12/06	12/07E	12/08E	12/09E
Investment banking fees	4,680.0	5,189.2	5,701.5	6,213.5	Cash & equivalents	32,109.0	0.0	0.0	0.0
Commissions	5,952.0	5,903.9	7,615.6	8,432.6	Cash and securities for reg.	13,449.0	0.0	0.0	0.0
Principal transactions	7,034.0	9,598.4	8,470.8	9,053.9	Total securities	385,216.0	0.0	0.0	0.0
Asset management	6,539.0	4,968.0	6,393.8	7,323.0	Repos	296,978.0	0.0	0.0	0.0
Other	5,798.0	3,440.2	6,923.2	7,189.9	Securities borrowed	--	--	--	--
Net interest income	4,656.0	3,570.0	5,620.0	6,169.1	Broker receivables	--	--	--	--
Credit card fee	--	--	--	--	Customer receivables	--	--	--	--
Provision for consumer loans	--	--	--	--	Other receivables	89,381.0	0.0	0.0	0.0
Net revenue	34,659.0	32,669.7	40,725.0	44,382.0	Total receivables	89,381.0	0.0	0.0	0.0
Personnel/compensation	(17,003.0)	(15,549.9)	(18,884.0)	(20,423.3)	Property plant and equipment, net	2,924.0	0.0	0.0	0.0
Total non-interest expense	(24,233.0)	(23,425.9)	(27,415.1)	(29,763.1)	Intangibles	2,457.0	3,644.0	3,644.0	3,644.0
Income/(loss) from uncons. subs.	0.0	0.0	0.0	0.0	Other assets	--	--	--	--
Profit/loss on disposal of assets	0.0	0.0	0.0	0.0	Total assets	841,299.0	1,102,903.9	1,158,049.1	1,215,951.6
Total other net	0.0	0.0	0.0	0.0	Comm. paper and short-term debt	18,110.0	0.0	0.0	0.0
Pretax profit	10,426.0	9,243.8	13,309.9	14,618.9	Deposits	84,124.0	0.0	0.0	0.0
Provision for income taxes	(2,927.0)	(2,758.7)	(3,993.0)	(4,385.7)	Total securities sold	0.0	0.0	0.0	0.0
Minority interest	0.0	0.0	0.0	0.0	Repos	24,929.0	0.0	0.0	0.0
Net income pre-pref. dividends	7,499.0	6,485.0	9,316.9	10,233.2	Securities loaned	98,862.0	0.0	0.0	0.0
Preferred dividends	(188.0)	(268.0)	(288.0)	(300.0)	Other	266,116.0	0.0	0.0	0.0
Net income pre-exceptionals	7,311.0	6,217.0	9,028.9	9,933.2	Brokers payables	--	--	--	--
Post tax exceptionals	(1,177.0)	0.0	0.0	0.0	Customer payables	--	--	--	--
Net income post tax exceptionals	6,134.0	6,217.0	9,028.9	9,933.2	Total payables	109,792.0	0.0	0.0	0.0
EPS (diluted, pre-except) (\$)	7.68	6.75	10.00	11.00	Accrued expenses & other liabs.	2,801.0	0.0	0.0	0.0
DPS (\$)	1.00	1.40	1.50	1.60	Total long-term debt	181,400.0	0.0	0.0	0.0
BVPS (\$)	41.37	45.09	53.58	62.98	Other liabilities	12,314.0	0.0	0.0	0.0
Tangible BVPS (\$)	34.77	38.28	41.30	46.43	Total liabilities	798,448.0	1,061,134.9	1,112,471.9	1,165,743.2
Growth & margins (%)	12/06	12/07E	12/08E	12/09E	Capital units & pref securities	3,813.0	0.0	0.0	0.0
Net revenue growth	33.2	(5.7)	24.7	9.0	Preferred stock	3,145.0	4,624.0	4,624.0	4,624.0
Net income growth	21.6	1.4	45.2	10.0	Total common equity	35,893.0	37,145.0	40,953.2	45,584.4
EPS growth	48.8	(12.1)	48.1	10.0	Minority interest	0.0	0.0	0.0	0.0
Pretax margin	30.1	28.3	32.7	32.9	Total stockholders' equity	39,038.0	41,769.0	45,577.2	50,208.4
After tax margin	17.7	19.0	22.2	22.4	Total liabilities & equity	841,299.0	1,102,903.9	1,158,049.1	1,215,951.6
					Ratios (%)	12/06	12/07E	12/08E	12/09E
					ROA	1.0	0.6	0.8	0.8
					ROE	19.6	15.4	20.7	20.7

Note: Last actual year may include reported and estimated data.

Source: Company data, Goldman Sachs Research estimates.

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EPS estimate revisions driven by bleak outlook for trading and significant mark to market hits

The primary driver to our estimate revisions largely emanate from our anticipation for mark to market hits in both the fixed income and equity markets businesses. Aside from capital markets, most of our estimate changes were largely tweaking, and included a \$100 mn reduction in our debt origination estimate due to volatility in the credit markets during the quarter.

On the fixed income side of the business, we are assuming a \$1.5 bn total loss on the business, driven largely by our expectation for roughly \$4.0 bn in mark to market losses. The mark to market losses are likely made up by a combination of leveraged loan losses (\$1.5 bn), CDO exposure and associated write-down of inventory (\$2.0 bn), and other mortgage related and residual write-downs (\$0.5 bn). Outside of these write-downs and a more challenging credit environment in general, we don't believe there was a substantial difference from the second quarter environment. To put these write-downs in context, many of Merrill's peers have already taken substantial write downs in the just reported earnings period. Both Lehman Brothers and Bear Stearns were negatively impacted by roughly \$700 mn net write-downs in their leveraged loan and mortgage businesses, while Morgan Stanley took \$940 mn in net write-downs on leveraged loan commitments.

On the equities front, higher levels of volatility is likely to have made for a challenging environment in the equity linked business, although extremely high levels of client activity and share volumes likely drove solid cash equities results.

Exhibit 1: Revisions to our estimates

\$ in millions, except per share data and where noted

	3Q07E		Change		2007E		Change		2008E		Change		2009E		Change	
	New	Old	Absolute	Percent	New	Old	Absolute	Percent	New	Old	Absolute	Percent	New	Old	Absolute	Percent
Debt Origination	350.0	450.0	(100.0)	(22%)	1,770.0	2,020.0	(250.0)	(12%)	2,000.0	2,200.0	(200.0)	(9%)	2,200.0	2,350.0	(150.0)	(6%)
Equity Origination	475.0	475.0	0.0	0%	1,885.0	1,910.0	(25.0)	(1%)	2,150.0	2,150.0	0.0	0%	2,350.0	2,350.0	0.0	0%
Strategic Advisory Services	425.0	400.0	25.0	6%	1,621.0	1,596.0	25.0	2%	1,750.0	1,750.0	0.0	0%	1,900.0	1,900.0	0.0	0%
Investment Banking	1,250.0	1,325.0	(75.0)	(6%)	5,276.0	5,526.0	(250.0)	(5%)	5,900.0	6,100.0	(200.0)	(3%)	6,450.0	6,600.0	(150.0)	(2%)
FICC	(1,500.0)	2,300.0	(3,800.0)	(165%)	5,719.0	9,819.0	(4,100.0)	(42%)	10,250.0	10,600.0	(350.0)	(3%)	11,000.0	11,250.0	(250.0)	(2%)
Equity markets	1,225.0	2,000.0	(775.0)	(39%)	7,759.0	8,534.0	(775.0)	(9%)	9,150.0	9,200.0	(50.0)	(1%)	9,800.0	9,800.0	0.0	0%
Capital markets	(275.0)	4,300.0	(4,575.0)	(106%)	13,478.0	16,353.0	(4,875.0)	(27%)	19,400.0	19,800.0	(400.0)	(2%)	20,800.0	21,050.0	(250.0)	(1%)
Total Global Markets and Investment Banking	975.0	5,625.0	(4,650.0)	(83%)	18,754.0	23,879.0	(5,125.0)	(21%)	25,300.0	25,900.0	(600.0)	(2%)	27,250.0	27,650.0	(400.0)	(1%)
Global Wealth Management (GWM)	3,488.2	3,488.2	0.0	0%	14,244.7	14,239.7	5.0	0%	15,825.0	15,815.0	10.0	0%	17,532.0	17,532.0	0.0	0%
Corporate	(80.0)	(80.0)	0.0	0%	(329.0)	(329.0)	0.0	0%	(400.0)	(400.0)	0.0	0%	(400.0)	(400.0)	0.0	0%
Total net revenues	4,383.2	9,033.2	(4,650.0)	(51%)	32,669.7	37,789.7	(5,120.0)	(14%)	40,725.0	41,315.0	(590.0)	(1%)	44,382.0	44,782.0	(400.0)	(1%)
Compensation expense	2,089.8	4,368.3	(2,278.5)	(52%)	15,549.9	17,630.7	(2,080.8)	(12%)	18,884.0	19,023.0	(139.0)	(1%)	20,423.3	20,610.1	(186.8)	(1%)
% of revenue	47.7%	48.4%			47.6%	46.7%			46.4%	46.0%	(139.0)	(1%)	46.0%	46.0%		
Non-comp expense	1,995.0	2,000.0	(5.0)	(0%)	7,876.0	7,881.0	(5.0)	(0%)	8,531.1	8,659.6	(128.5)	(1%)	9,339.8	9,425.8	(86.0)	(1%)
% of revenue	45.5%	22.1%			24.1%	20.9%			20.9%	21.0%			21.0%	21.0%		
Total operating expenses	4,084.8	6,368.3	(2,283.5)	(36%)	23,425.9	25,511.7	(2,085.8)	(8%)	27,415.1	27,682.6	(267.6)	(1%)	29,763.1	30,035.9	(272.8)	(1%)
% of revenue	93.2%	70.5%			71.7%	67.5%			67.3%	67.0%			67.1%	67.1%		
Operating income	298.4	2,664.9	(2,366.5)	(89%)	9,243.8	12,278.0	(3,034.2)	(25%)	13,309.9	13,632.3	(322.4)	(2%)	14,618.9	14,746.1	(127.2)	(1%)
Operating margin	6.8%	29.5%			28.3%	32.5%			32.7%	33.0%			32.9%	32.9%		
Income taxes	89.5	799.5	(710.0)	(89%)	2,758.7	3,669.0	(910.3)	(25%)	3,993.0	4,089.7	(96.7)	(2%)	4,385.7	4,423.8	(38.2)	(1%)
Tax rate	30.0%	30.0%			29.8%	29.9%			30.0%	30.0%			30.0%	30.0%		
Preferred stock dividend	72	72	0.0		268	268	0.0		288	288	0.0		300	300	0.0	
Net income	208.9	1,865.4	(1,656.6)	(89%)	6,485.0	8,609.0	(2,123.9)	(25%)	9,316.9	9,542.6	(225.7)	(2%)	10,233.2	10,322.3	(89.0)	(1%)
EPS	\$0.15	\$1.95	(\$1.80)	(92%)	\$6.75	\$9.05	(\$2.31)	(25%)	\$10.00	\$10.25	(\$0.25)	(2%)	\$11.00	\$11.10	(\$0.10)	(1%)
Shares (diluted)	918.3	918.3	0.0	0%	921.3	921.3	0.0	0%	903.3	903.3	0.0	0%	903.3	903.3	0.0	0%

Source: Company data, Goldman Sachs Research estimates.

Reg AC

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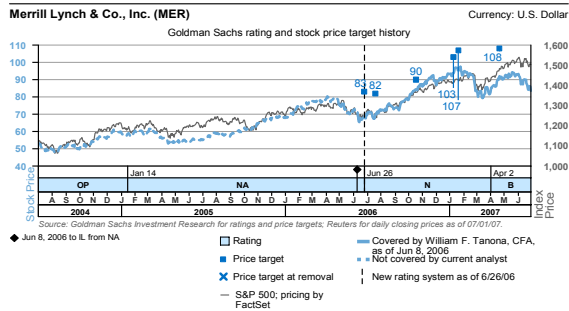
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