Timothy Geithner/NY/FRS
Sent by: Michael Held/NY/FRS

09/14/2008 04:44 PM

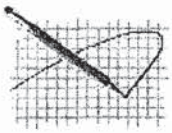
To Edward Quince/BOARD/FRS, Donald L Kohn/BOARD/FRS

cc

bcc Michael Silva/NY/FRS@FRS, Tanshel Pointer/NY/FRS@FRS, Meg McConnell/NY/FRS@FRS

Subject Fw: Pros and Cons on AIG lending

----- Forwarded by Michael Held/NY/FRS on 09/14/2008 04:40 PM -----



Alejandro LaTorre/NY/FRS

09/14/2008 03:49 PM

To Adam Ashcraft/NY/FRS@FRS, Alejandro LaTorre/NY/FRS@FRS, Christopher Calabia/NY/FRS@FRS, Elise Liebers/NY/FRS@FRS, Hayley Boesky/NY/FRS@FRS, Jim Mahoney/NY/FRS@FRS, Patricia Mosser/NY/FRS@FRS, Paul Whynott/NY/FRS@FRS, Richard Charlton/NY/FRS@FRS, Tobias Adrian/NY/FRS@FRS, William Walsh/NY/FRS@FRS, Catherine Voigts/NY/FRS@FRS, Timothy Geithner/NY/FRS@FRS, Michael Silva/NY/FRS@FRS, Meg McConnell/NY/FRS@FRS, William Dudley/NY/FRS@FRS, William Rutledge/NY/FRS@FRS, Terrence Checki/NY/FRS@FRS, Susan Stiehm/NY/FRS@FRS, Arthur Angulo/NY/FRS@FRS

cc Tanshel Pointer/NY/FRS@FRS

Subject Pros and Cons on AIG lending

Attached are the following documents:

1. A note describing the pros and cons of lending to AIG

2. A spreadsheet provided by AIG detailing the firms with the largest exposures to AIG (i.e. what firms stand to lose in the event of AIG default). The relevant column is "Total Exposure to AIG, Ranked". With the exception of the "lending" column, these figures are loss estimates. Derivative loss estimates are derived from current MTM provided by AIG.

3. A presentation describing what we know on AIG subsidiaries based on publicly available information.

If there are questions, let us know.

Regards,

Alex

Pros and Cons of Lending to AIG.doc Counterparty_Exposure_Report_9142008.xls AIG Subsidiaries.ppt

Pros and Cons of Lending to AIG

S&P's current financial strength rating for AIG is AA+ for the leading insurance companies and AA- on the senior debt of the parent company (put on negative outlook due to risk management issues).

Pros:

1. Collapse would be extremely complex to resolve given global nature of the firm; lending could contain market dislocations already happening due to Lehman.

2. Lending could provide "bridge finance" to implement strategic plan (e.g. longer-term asset sales, capital infusions, etc.);

    - Lending could bolster market confidence in strengthen perception of the plan with appropriate safeguards for the Federal Reserve.

    - AIG's fair value on ABS CDO aggressive ($25B); greater than internal ($9B) and rating agency loss estimates (S&P:$8B).

    - Allows time to sell assets from the investment portfolio an orderly fashion (i.e., avoids liquidity spiral, negative feedback loops)

    - Firm could sell the ABS CDO risk, sell subsidiaries, mortgage portfolio, municipal securities, or raise more capital.

3. Collapse could lead to dislocation in sec lending/repo markets, CP markets and exacerbate risk aversion generally; lending could alleviate spillover effects on other firms involved in similar activities (e.g., GE Finance).

4. Lending might allow AIG to avoid bankruptcy; allows AIG to perform on balance sheet CDO swaps, which provide reg capital relief to European banks; failure would lead to $18B increase in European bank capital requirements.

    - Swaps allow banks to hold 1.6% in regulatory capital as opposed to 8%.

    - Total notional exposure of $290B; down from $80B as deals wound down.

    - ABN Amro, Den Danske, Calyon, BNP, Deutsche most affected.

5. Lending could contain dislocations in CDS market; AIG is a commonly traded name and "tear ups" could leave dealer books significantly unbalanced.

6. Non-trivial exotic derivatives book would be difficult to unwind in an orderly fashion.

FRBNYAIG00497

Cons:

1. Could diminish incentive to pursue private sector solutions and/or solutions proposed by insurance regulators, which, according to AIG and NYSID, appear to be moving forward.

    - Infusion of capital from private equity, which could happen today ($15B)

    - Asset swap between P+C and Parent where Parent sells equity in Life insurance business in return for municipal securities, for use as collateral ($20B)

    - Immediate sale of assets ($13B; $5B auto-related; $8B annuity)

    - Berkshire Hathaway is investigating the provision of liquidity on Guaranteed Investment Contracts ($5B)

2. Market must be highly confident that strategic plan will succeed; may not be well-received if turmoil ensues following Lehman bankruptcy.

3. Lending could precipitate failure and the exit strategy would not be clear.

    - Increases moral hazard as other insurance companies seek protection.

4. Lending to AIG could be perceived as inconsistent with treatment of Lehman.

5. Assets available from Ins. Co. subs may not be sufficient to cover potential liquidity shortfalls as many of the subs do not appear to be sources of strength.

    - Life Ins. Co. subs have significant unrealized losses on investments.

    - P&C could be source of strength; paid $1.4B dividends, but amounts small relative to size of hole.

6. Forbearance could address increases in European bank capital requirements; makes lending unnecessary.

7. Without punitive terms, lending could reward poor risk management practices cited by rating agencies (e.g. S&P).

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Counterparty Exposure Report, millions of dollars

Counterparty Exposure to AIG					
Mark to Market Exposure on Derivatives			Lending	Total Exposure to AIG	
ABS CDO*	Other Derivatives	Other CDO**	to AIG	I + ii+ iii + iv	
i	ii	iii	iv		
0.5	291.4	1,627.1	10,033.3	11,952.3	Barclays
3.0	14.0	4,399.6	8,253.3	12,669.9	Deutsche Bank
7.0	149.0	1,860.4	6,910.3	8,926.7	Goldman Sachs
0.0	140.7	5,867.4	6,676.3	12,684.4	BNP Paribas
1.5	16.0	285.4	5,477.1	5,780.0	UBS
0.3	237.4	-2.2	5,459.4	5,694.9	Bank of America
0.0	163.5	159.9	5,019.3	5,342.8	Citigroup
0.0	22.0	-71.1	4,995.8	4,946.7	ING
0.1	71.0	427.1	4,605.0	5,103.1	HSBC
0.0	122.3	173.4	4,554.3	4,850.0	Credit Suisse
0.6	69.8	21.7	3,558.2	3,650.3	Banco Santander
0.0	315.0	0.0	3,546.5	3,861.5	Lehman Brothers
2.7	18.5	204.2	3,051.5	3,276.8	Merrill Lynch
0.0	0.0	0.0	2,930.1	2,930.1	Dresdner
0.0	101.0	2,014.6	2,688.2	4,803.7	Morgan Stanley
0.4	133.0	-7.0	1,901.1	2,027.5	Royal Bank of Scotland
0.0	0.0	14,051.2	632.0	14,683.2	ABN Amro
0.0	29.0	0.0	1,859.5	1,888.5	Sumitomo Mitsui
0.0	0.5	0.0	1,711.5	1,712.0	MUFG
5.9	348.1	3,971.2	1,708.0	6,033.3	Societe Generale
0.0	17.0	0.0	1,350.0	1,367.0	Helaba
0.0	41.0	-7.1	1,090.2	1,124.1	Intesa SanPaolo
0.0	58.5	696.9	1,080.0	1,835.4	BayLB
0.3	0.1	-3.3	1,039.6	1,036.6	Wachovia
0.0	0.0	2,553.5	947.5	3,500.9	JP Morgan
0.0	0.0	0.0	85.8	85.8	Bear Steams
0.0	0.0	0.0	945.0	945.0	Kredeitbank
0.0	29.0	0.0	851.1	880.1	Svenska Handelsbanken
0.0	97.0	389.3	838.5	1,324.8	Mizuho
0.0	0.0	0.0	27.0	27.0	Daiwa Securities
0.0	83.0	194.4	635.4	912.8	Standard Chartered
0.0	489.0	287.8	616.8	1,393.6	Unicredit Group
1.6	0.0	6,108.5	599.6	6,709.6	Calyon
0.0	1.0	0.0	599.5	600.5	Toronto Dominion
0.0	0.0	0.0	549.0	549.0	LBBW
0.0	0.0	0.0	545.2	545.2	Scotiabank
0.0	1.3	0.0	518.7	520.0	RBC
0.0	184.0	8,847.1	327.0	9,358.1	Danske
0.0	0.0	0.0	295.8	295.8	Citadel
0.0	0.7	0.0	146.7	147.4	Bank of Montreal
0.0	0.0	0.0	84.9	84.9	Jefferies
0.0	29.0	386.9	70.5	486.4	Fortis Securities
0.0	-1.5	0.0	2.8	1.2	Newedge
0.0	0.0	0.0	0.0	0.0	BGI (Cash Equivalent Fund II)
0.2	4.0	-147.6	0.0	-143.4	CIBC
0.7	0.0	54.8	0.0	55.5	Coral Purchasing (DZ Bank)
0.0	0.0	0.0	0.0	0.0	First Clearing LLC
0.3	0.0	911.3	0.0	911.6	Rabobank

*FRBNY loss estimate, **FRBNY 25% loss assumption

Total Exposure to AIG, Ranked

1	ABN Amro	14,683.2
2	BNP Paribas	12,684.4
3	Deutsche Bank	12,669.9
4	Barclays	11,952.3
5	Danske	9,358.1
6	Goldman Sachs	8,926.7
7	Calyon	6,709.6
8	Societe Generale	6,033.3
9	UBS	5,780.0
10	Bank of America	5,694.9
11	Citigroup	5,342.8
12	HSBC	5,103.1
13	ING	4,946.7
14	Credit Suisse	4,850.0
15	Morgan Stanley	4,803.7
16	Lehman Brothers	3,861.5
17	Banco Santander	3,650.3
18	JP Morgan	3,500.9
19	Merrill Lynch	3,276.8
20	Dresdner	2,930.1
21	Royal Bank of Scotland	2,027.5
22	Sumitomo Mitsui	1,888.5
23	BayLB	1,835.4
24	MUFG	1,712.0
25	Unicredit Group	1,393.6
26	Helaba	1,367.0
27	Mizuho	1,324.8
28	Intesa SanPaolo	1,124.1
29	Wachovia	1,036.6
30	Kredeitbank	945.0
31	Standard Chartered	912.8
32	Rabobank	911.6
33	Svenska Handelsbanken	880.1
34	Toronto Dominion	600.5
35	LBBW	549.0
36	Scotiabank	545.2
37	RBC	520.0
38	Fortis Securities	486.4
39	Citadel	295.8
40	Bank of Montreal	147.4
41	Bear Steams	85.8
42	Jefferies	84.9
43	Coral Purchasing (DZ Bank)	55.5
44	Daiwa Securities	27.0
45	Newedge	1.2
46	BGI (Cash Equivalent Fund II)	0.0
47	First Clearing LLC	0.0
48	CIBC	-143.4

Other CDO expsure RANKED
(predominantly regulatory capital arbitrage, notional)

1	ABN	56,205
2	Danske	35,388
3	Calyon	24,434
4	BNP Paribas	23,470
5	Deutsche Bank	17,598
6	Societe Generale	15,885
7	JP Morgan	10,214
8	Morgan Stanley	8,058
9	Goldman Sachs	7,442
10	Barclays	6,508
11	Rabobank	3,645
12	BayLB	2,788
13	HSBC	1,708
14	Mizuho	1,557
15	Fortis Securities	1,548
16	Unicredit Group	1,151
17	UBS	1,142
18	Merrill Lynch	817
19	Standard Chartered	778
20	Credit Suisse	693
21	Citigroup	640
22	Coral Purchasing (DZ Bank)	219
23	Banco Santander	87
24	Lehman Brothers	-
25	Dresdner	-
26	Sumitomo Mitsui	-
27	MUFG	-
28	Helaba	-
29	Bear Steams	-
30	Kredeitbank	-
31	Svenska Handelsbanken	-
32	Daiwa Securities	-
33	Toronto Dominion	-
34	LBBW	-
35	Scotiabank	-
36	RBC	-
37	Citadel	-
38	Bank of Montreal	-
39	Jefferies	-
40	Newedge	-
41	BGI (Cash Equivalent Fund II)	-
42	First Clearing LLC	-
43	Bank of America	(9)
44	Wachovia	(13)
45	Royal Bank of Scotland	(28)
46	Intesa SanPaolo	(28)
47	ING	(284)
48	CIBC	(590)

Restricted FR

AIG Subsidiaries: Are they a Source of Strength?

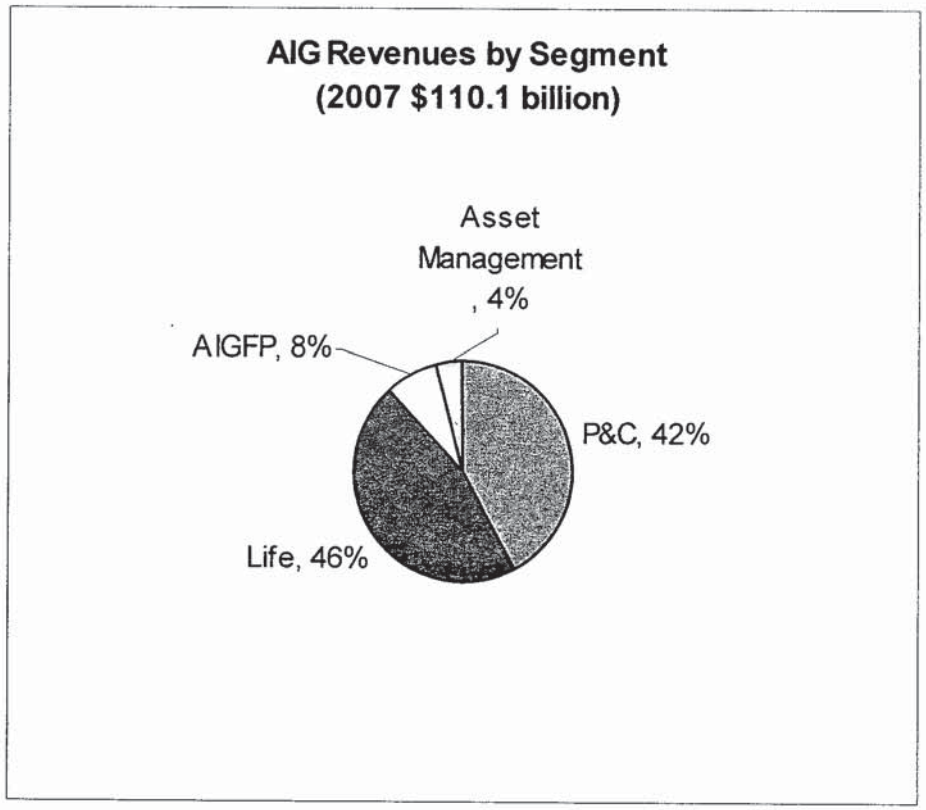
Chris Calabia, Erika Gottfried, Min Kim, Elise Liebers,
Alexander Psomas, Danielle Vicente

Bank Supervision Group

Sunday, September 13, 2008

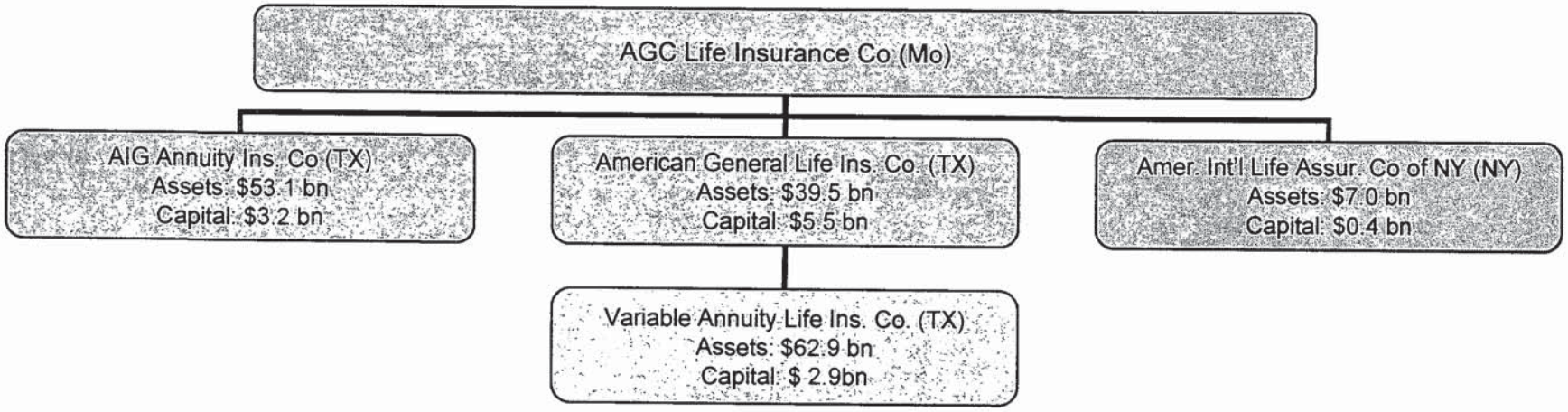
Ability to support has weakened

- Realized & significant unrealized losses on investments
- 380 subsidiaries, largest ≈ 10%
- Dividends to parent down sharply overall
  - 2007: $4.9 billion
  - 2008 YTD: $1.4 billion, 90% from P&C



Simplified Organizational Chart

Life Insurance



AIG - Summary of Financial and Ratings Information of Major Subsidiaries

Financial data as of 6/30/08

($ in millions)	American Life Insurance Co.	Variable Annuity Life	AIG Annuity Insurance Co	American General Life	SunAmerica Life	National Union Fire Insurance Co.	American Home Assurance	American International Life
Type of Business	L&H Insurance	L&H Insurance	L&H Insurance	L&H Insurance	L&H Insurance	P&C	P&C	L&H Insurance
Home State	DE	TX	TX	TX	AZ	PA	NY	NY
Ratings*								
S&P	AA+ WN (9/12/08)	AA+ WN (9/12/08)	AA+ WN (9/12/08)	AA+ WN (9/12/08)	AA+ WN (9/12/08)	AA+ WN (9/12/08)	AA+ WN (9/12/08)	AA+ WN (9/12/08)
Moodys	Aa2 OS (5/28/08)	Aa2 ON (8/7/08)	Aa2 ON (8/7/08)	Aa2 ON (8/7/08)	Aa2 ON (8/7/08)	Aa3 OS (5/28/08)	Aa3 OS (5/28/08)	Aa2 ON (8/7/08)
Fitch	AA+ WN (8/22/08)	AA+ WN (8/22/08)	AA+ WN (8/22/08)	AA+ WN (8/22/08)	AA+ WN (8/22/08)	na	AA+ WN (8/22/08)	AA+ WN (8/22/08)
Balance Sheet Highlights								
Total Assets	$105,606	$62,880	$53,078	$39,489	$38,003	$34,190	$27,867	$7,005
% of Consolidated Assets ($1.0 trillion)	10.1%	6.0%	5.1%	3.8%	3.6%	3.3%	2.7%	0.7%
Bonds	$53,832	$24,287	$40,098	$23,880	$16,878	$14,171	$15,614	$5,640
Separate Accounts	$37,122	$26,649	$373	$2,685	$215	na	na	$120
Total Capital	$7,113	$2,911	$3,224	$5,513	$4,748	$12,195	$6,527	$440
Asset Valuation Reserve	$363	$471	$1,012	$289	$1,047	na	na	$715
Unrealized Gains (Loss)	($706)	($111)	$23	($906)	($497)	$72	na	$2
Total Adjusted Capital (YE 2007)	na	$3,632	$4,878	$6,839	$5,976	$11,373	$7,041	$662
Authorized Control RBC Ratio (YE2007)	na	$568	$666	$1,063	$836	$2,818	$1,602	$92
RBC Ratio (YE 2007)	na	639%	732%	644%	714%	404%	440%	715%
Income Statement Highlights								
Net Income (excl. Capital Gains)	$580	$249	$191	$151	$300	$679	$491	$33
Realized Capital Gains (Loss)	($381)	($1,551)	($2,325)	($1,260)	($1,085)	$206	$1,185	($290)
Dividends to Parent**								
2008 (first six months)	$0	$0	$0	$0	$0	$1,109	$268	$50
2007	$1,033	$700	$400	$551	$700	$1,120	$615	$100
2006	$200	$400	$150	$208	$349	$0	$0	$62
2005	$50	$400	$0	$441	$480	$98	$32	$50
2004	$50	$360	$0	$301	$26	$207	$63	$0

* WN: Watch Negative, OS: Outlook Stable, ON: Outlook Negative

** In 2007, AIG parent collected $4.9 billion in dividends. In the first half of 2008, AIG parent collected $1.4 billion in dividends. (Source: 10K)

What happens in a sale?

The loss rate at which equity becomes zero	
American Life Insurance Co.	8%
Variable Annuity Life	5%
AIG Annuities Insurance Co	8%
National Union	35%
SunAmerica Life	14%
American Home Assurance	22%
American General Life	12%
American International Life Assurance Co. of NY	16%

- Using a weighted average, all the subsidiaries shocked would wipe out their capital in a liquidation if assets are sold at a 12% loss or greater.
- P&C entities are more resilient and can withstand losses on their assets of greater than 20%.