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### Federal Reserve Bank of New York Meeting with AIG Notes

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## **AIG Meeting Notes**

September 12, 2008

AIG – Jacob Frenkel (Vice Chairman), Steve Bensinger (CFO), David Herzog (SVP & Comptroller), Robert Gender (VP & Treasurer), Alan Pryor (EVP – Financial Services Division)

FRBNY – Trish Mosser, Jim Mahoney, Bill Dudley

AIG is facing serious liquidity issues that threaten its survival viability.

There are potential credit rating agency downgrades. Moody's Committee meets on Monday September 15 (currently rated AA3, downgraded at least one notch)... S&P already has AIG on negative watch (as of today)... Fitch already has AIG on negative watch.

Rating triggers:

GICs are issued out of AIG-Financial Products (AIG-FP), insured by the holding company.

- downgrade by 1 rating agency leads to \$10B in collateral calls, plus an additional \$4B-\$5B in portfolio obligations that are puttable if downgraded (total of \$15B in liquidity needs)
- downgrade by 2 rating agencies – additional \$3B in liquidity needs
- If downgraded, they must post half of the additional collateral within 2 days, and the other half in 10 days.

Markets are also punishing AIG. Stock prices are off about 40% today, and CDS is traded at about 1400 bp (up from about 10 bp eighteen months ago).

Some banks are already pulling away; some banks are even turning down AIG in the secured (repo) borrowing markets

AIG is having problems rolling its commercial paper (CP). \$2.5B in CP matured today, but they were able to roll only \$1.1B, the remaining \$1.4B was funded out of the parent.

AIG has a total of about \$15B in CP, which has backstop (backup lines of credit) from a consortium of banks; AIG may have to draw on lines on Monday, which is a material event and so will become publicly known and have negative implications.

AIG also has ABCP facilities of about \$5B, and these have no backup lines

AIG's repo book is all investment grade, mostly structured mortgage products... Things that have, in the past, been used as repo collateral... but the combination of being perceived as a weak counterparty and risky, illiquid collateral is resulting in counterparties stepping away....

Securities lending (mostly out of the insurance companies) – about \$69B in liabilities, and the holding company has only enough cash to fund ½ of that, if the securities lending counterparties turn away from the AIG name.

Mobility of liquidity – most cash within the organization is ‘trapped’ in regulated entities and is not freely transferable to AIG holding company or AIG Financial Products (the derivatives and trading sub) for its liquidity needs.

Today, the holding company started with \$9B in liquidity, used \$1.4 for CP, but was able to upstream about \$1.4B in ‘dividends’ from subs up to holding company, but little ability, in general, to use subs to upstream liquidity to holding co or its non-regulated subs.

Bottom line: Treasurer estimates that parent and AIG FS sub have 5-10 days before they are out of liquidity.

Plans to address liquidity stress? AIG is aggressively pursuing:

- Asset sales – but many viable assets to sell have distressed and illiquid markets into which to sell
- Equity issuance – not viable at this time – 3 months ago, AIG raised \$20B in capital. It is all gone.
- Holding company has about \$12B in ‘Fed-eligible’ assets (that is, PDCF collateral... note, however, this does not include the restriction on assets that have ‘available prices’)
- The various insurance subs have very large quantity of high quality assets, but the restrictions on pledging those are very unclear.

Unwinding in event of bankruptcy is likely to be very messy, because derivatives book is large and complex \$2.7 Trillion, largely of very long-term structure products. \$1 Trillion is concentrated in 12 large counterparties. Book is very far from balanced, although they could not give a MTM value. One of the challenges they are already facing is very aggressive marks from counterparties and strategic unwinding of “in the money” positions, and this will likely accelerate in coming days adding to the cash drain. Their super senior CDO book is about \$80 bn and at present they have approximately \$19 billion in collateral posted against it.

Access to Fed facilities:

They have what they describe as a very small thrift, and so limited ability to borrow from DW. Recently they drew up a plan to become a primary dealer over a 6-12 month period, but obviously do not have the time to implement that plan. They explicitly asked about how to obtain an IPC 13-3 loan. They are very willing to open their books to us, and give us a better sense of their risk profile, the complexity of their book and detailed liquidity profile as soon as possible (ie this weekend.)