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AIG Second Quarter Earnings Call, 2007

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Company Ticker: AIG US
Date: 2007-08-09
Event Description: Q2 2007 Earnings Call

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Current PX: 64.85
YTD Change(\$): -6.81
YTD Change(%): -9.503

Bloomberg Estimates - EPS
Current Quarter: 1.575
Current Year: 6.671
Bloomberg Estimates - Sales
Current Quarter: 30566.208
Current Year: 122687.981

Q2 2007 Earnings Call

Participants

- Martin J. Sullivan
- Joseph Cassano
- Robert E. Lewis
- Andrew Foster
- Edmund S. W. Tse
- Frank H. Douglas
- Frederick W. Geissinger
- Jay S. Wintrob
- Nicholas Walsh
- William Nutt, Jr.
- Richard W. Scott
- Robert W. Clyde
- Charlene Hamrah

MANAGEMENT DISCUSSION SECTION

Charlene Hamrah

Non-GAAP Financial Measures

The information provided today may also contain certain non-GAAP financial measures

The reconciliation of such measures to the comparable GAAP figures are included in Q2, 2007 financial supplement available in the investor information section of AIG's corporate website

Martin J. Sullivan

Q2 Results

Major Business Contributions

- As you have seen from our results, AIG had a strong Q2 owing to a diversified global business portfolio
- Major contributions to our results came from general insurance, life insurance and retirement services, asset management and capital markets
- Partnership returns remained strong, positively affecting investment income

Net Income and ROE

- Net income was \$4.28B, a 34.1% increase over Q2 2006
- Q2 adjusted net income, which excludes realized capital gains and losses and the effective hedging activities that did not qualify for hedge accounting treatment under FAS 133 was a record \$4.63B or \$1.77 per diluted share, a 12% increase compared to \$1.58 per diluted share in Q2 2006

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- Return on equity, using adjusted net income as the measure, was 19.8% for Q2

Assets, Shareholders Equity and Share Repurchases

- Total assets now exceed \$1 trillion
- Shareholders' equity at June 30th stood at just over \$104B including retained earnings of some \$92.3B
- Book value per share increased to \$40.44, excluding \$2.34B in payments advanced to purchase shares, book value was \$41.34
- We purchased over 22mm shares in Q2 and an additional 24.5mm shares through August 6
 - That puts our YTD share repurchases at approximately 49mm shares or 67% of the \$5B in repurchases planned for 2007

H2 Prospects

- Looking towards H2, we have good reason to be confident about AIG's growth prospects
- Our diverse worldwide operations are well positioned to respond to opportunities that will arise from major global economic trends
 - At the same time, we are undertaking organizational and financial initiatives that will enhance future returns
- We continue to develop our economic capital model, and last evening, we posted a progress update on our website
- Our businesses remain focused on their objectives and they continue to bring new products and services to market through multiple distribution channels

Business Segments Review

General Insurance Results

- Quickly looking at our major business segments, General Insurance results were led by the Domestic Brokerage Group, which posted improved underwriting results due to favorable loss trends and higher net investment income

Capitalizing on Opportunities

- To offset the continued pressure on rates in certain lines and regions, our General Insurance operations are capitalizing on the opportunities offered by:
 - Our broad product mix
 - Ability to deliver unique products to market
 - Our geographic footprint
 - And expanding distribution platform while maintaining underwriting discipline

Foreign General

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- Foreign General, which also had an excellent quarter is accelerating growth by investing in India, Russia, the Middle East, and China
- Following the close of the quarter, AIU was granted a subsidiary license in China that will allow us to expand our capabilities, achieve operational and capital efficiencies and, with regulatory approval, provide a platform to establish new branches in other areas of China over time
- Domestic Personal Lines remain focused on achieving underwriting profits and extending the strong competitive position of the Private Client Group

Domestic Life Insurance and Payout Annuities

- Domestic Life Insurance and Payout Annuities operating income increased largely as a result of solid growth in reserves and higher net investment income
 - These businesses expect to see continued top line growth through further enhancement of the product portfolio, expanded distribution, and increased demand from the institutional marketplace

Domestic Retirement Services

- In Domestic Retirement Services, all three major product lines reported improved deposits with operating income increasing largely as a result of higher net investment income from partnerships and other yield enhancements
- Our Group Retirement division remains focused on targeted asset retention strategies
 - The variable annuity business continues to improve as we roll out products that provide guaranteed income for life
- Despite the challenging sales environment, our long-term commitment to the fixed annuity product line and strong bank relationships has AIG Annuity well positioned to take advantage of any change in the yield curve and/or interest rate environment that favors long-term guaranteed fixed-rate savers

Life and Retirement Services Results

- Life and Retirement Services results in Q2 reflect the continued demand for investment oriented products and sales of risk based accident and health products throughout our global operations

Southeast Asia

- In Southeast Asia, AIA remains the leading market player, distributing our products through approximately 140,000 hired insurance agents
 - While also developing alternative distribution such as our recent agreement with the Bank of Investment and Development of Vietnam

China

- In China, we are making good progress in expanding our geographical footprint, increasing the number of sales offices by seven this quarter, giving us a total of 90 and strengthening our distribution capabilities, especially in Bank Assurance where production has increased significantly

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- Additionally, we wrote more than 2,100 group cases in the quarter, bringing total cases written since we received our license in May 2006 to more than 5,600

Japan

- Market conditions remain challenging in Japan as a result of increased competition, the effect of additional regulatory oversight, changes to the tax deductibility of insurance premiums and the weak yen
- Dollar life insurance products, which have substantially higher profit margins continue to sell well
- Medical production is anticipated to improve due to the recent launch of a new product targeting a younger generation of clients

Financial Services

- Financial Services operating income declined compared to Q2 2006 as growth at Capital Markets was offset by the decline in Consumer Finance results
- Aircraft Leasing results were up slightly, as ILFC did not sell any aircraft in Q2 2007 compared to three sold in Q2 2006
 - However, the sales environment is improving
- We see the current sub-prime environment as an opportunity for American General Finance despite the short-term pressures
- AGF's conservative, disciplined approach to lending will position the company well for the new order in the mortgage market
- Overseas, we continue to expand our Consumer Finance operations with recent efforts focused on India, Mexico, and Thailand

Asset Management Results

- In asset management, Guaranteed Investment Contracts benefited from an increase in partnership income and the Matched Investment Program contributed to the growth in income
- Despite the decline in operating income, our Institutional Asset Management business continues to make significant strides, attracting new client assets and expanding the breadth of its product offerings
 - AIG Investments successfully launched several new private equity and real estate funds in H1, which generate both a base management fee and the opportunity for future performance fees

Closing Remarks

- Now as I mentioned at the outset, I'm intentionally limiting my discussion of the quarter's operating performance and our strategic growth initiatives in order to fully address the concerns that have been raised by many in the investment community about our exposure to the US residential mortgage market
- This morning we provided a document in the investors section of the AIG corporate website that summarizes the areas within AIG that include this exposure, namely United Guaranty, American General Finance and AIG Financial Products, as well as our investment portfolio
- Bob Lewis, AIG's SVP and Chief Risk Officer, will walk you through the information in that document

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- With these details, we hope that you will have a better understanding of the respective businesses and portfolios and what we believe is a well-managed risk profile
- AIG's investment and credit offices monitor developments in this area very closely
- We believe we are well positioned even in the event of further deterioration in this market

Robert E. Lewis

Opening Remarks

Over the past several weeks, the US mortgage market has been the subject of a considerable amount of press and stress as a consequence of an increase in delinquencies in the private mortgage market, a tightening in credit availability, and the difficulties some funds have experienced in situations where high leverage and strained liquidity have forced them to realize large losses, and in some cases, cease operations

- Although there are clear signs that this stress will continue for some time, much of the dialogue has suggested that there is a considerable amount of confusion about the market in general, its participants, how it functions, and where the potential for future stress is greatest

In order to provide information to investors about our activities in the US residential mortgage market, we have prepared a slide presentation which was posted to our web site earlier this morning

- I would now like to walk you through that presentation and afterwards we will take your questions

US Residential Mortgage Market Activities

Market Dislocation and Pricing

- Referring to slide three of the presentation, AIG is active in many segments of the residential mortgage market from lending, to mortgage insurance, to investments, to Super Senior portfolio protections
- Certain segments of the market have experienced credit deterioration, which is affecting the current results in AIG's mortgage insurance business
 - AIG also holds residential mortgage-related securities and recognizes that the current market dislocation has caused quoted prices in many of them to decline
 - AIG views such declines as temporary as the robust cash flow characteristics, combined with the reasonably short maturity structure of most of these securities will exert a very strong pull to par, even if markets remain unstable
- AIG views recent pricing as indicative of market turmoil unrelated to the fundamental financial characteristics of these securities

Declines in Housing Values

- In addition, we believe that it would take declines in housing values to reach depression proportions, along with default frequencies never experienced, before our AAA and AA investments would be impaired
- AIG does not need to liquidate any investment securities in a chaotic market due to its strong liquidity and cash flow as well as its superior financial strength
- I am confident in our people and our risk management processes

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- Our exposures to this market are prudent given the nature of our business and our financial strength
- AIG has the financial wherewithal and expertise to take advantage of opportunities as they arise in the future

Risk Management Processes

- In all the areas where we're active, we have strong risk management processes undertaken by experienced professionals
- The risks we take are analyzed based upon our own independent analyses, modeling and monitoring
- Risk tolerances and appetites are formulated and implemented within authorities allocated by senior management and ongoing review and analysis is undertaken both in the businesses as well as at the corporate enterprise risk management level
 - Although the market may continue to experience a period of adjustment and volatility, our exposures are understood and well managed within an appropriate risk tolerance for a strong world leader in insurance and financial services

American General Finance and United Guaranty

- Turning to slide four of the presentation, AIG is active in several segments of the US mortgage market
- Through American General Finance, we originate mortgages by extending first and second lien mortgages to borrowers
- United Guaranty provides mortgage guaranty insurance for first and second lien mortgages that protects lenders against credit losses

Credit Protection through Credit Default Swaps

- Our insurance companies invest in Residential Mortgage-Backed Securities or RMBS in which the underlying collateral are pools of mortgages that are repaid from the underlying mortgage payments
- We, including AIG Financial Products invest also in collateralized debt obligations or CDOs and Asset Backed Securities or ABS, some of which also include RMBS as collateral
 - And also AIG Financial Products provides credit protection through credit default swaps on the Super Senior AAA + tranche of CDOs

Residential Mortgage Market Functioning

- Slide five describes how the residential mortgage market functions
- Starting on the left-hand side of the slide, lenders provide mortgage loans to borrowers to enable them to purchase or refinance a home
- The borrower provides the lender with a security interest in the home and pays mortgage principal and interest on the loan to the lender
- Mortgage insurers provide mortgage insurance on certain mortgages to lenders to protect them from certain credit losses on the mortgages
- Lenders either hold the mortgages on their balance sheets or sell the mortgages for securitization

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- Mortgages have been placed in collateral pools with thousands of other mortgages

Credit Ratings

- Dealers create special purpose vehicles, which issue residential mortgage-backed securities to the market, which may have different risk levels
- The rating agencies analyze the relative priority of the risk levels in the structures and assign various credit ratings to the levels based upon the credit quality of the underlying mortgages in the pool, the value of the collateral and the order of priority to receive interest and principal payments
- Monolines insurers like MBA -- MBIA, Ambac etcetera may guarantee or wrap certain tranches of our MBS and elevate their credit ratings to AAA
- Dealers always create other collateralized debt obligations with various collateral pools sometimes with the combination of asset types such as bank loans, corporate debt, RMBS, commercial mortgage-backed securities and other asset-backed securities
 - Investors then invest in these securities and are repaid from the payments made by the underlying borrowers in the pools after securitization services distribute the cash flows according to the priority of cash flows to the various risk layers
- Other credit protection providers may provide protection above the AAA tranche known as Super Senior or AAA + protection
- As mentioned earlier and shown on slide six, American General Finance participates as a mortgage lender, United Guaranty provides mortgage insurance to many lenders, AIG insurance companies and AIGFP [AIG Financial Products] invest in securitization vehicles such as RMBS, CMOs, CDOs and ABS
 - And AIGFP provides Super Senior credit protection by writing credit default swaps on the most senior risk layers in these structures

American General Finance

Turning to slide eight, American General Finance, AGF, is AIG's domestic consumer finance division

AGF is a portfolio-based lender whose products include real estate, non-real estate and retail sales finance loans that originates real estate loans through its 1,500 branches in 45 states Puerto Rico and the US Virgin Islands

AGF also originates and acquires loans through a centralized real estate operation

AGF underwrites and prices its products to perform within target ranges for delinquency and net charge-offs

- Their disciplined lending approach includes a state-of-the-art credit risk management system that allows them to track more than 350 individual real estate markets

This credit-focused approach enabled AGF to anticipate and mitigate much of the risk inherent in today's mortgage market

Unlike many industry players, AGF did not relax underwriting standards when the market overheated in late 2005 and 2006

During that time AGF continued its disciplined underwriting which has resulted in higher quality loans, strong first lien and fixed rate mortgages and no negative amortization products

Real Estate Growth

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- As demonstrated on slide nine, the trend in AGF's real estate receivable growth significantly slowed beginning in Q3 2005
 - This shows that AGF anticipated some of the real estate market issues and sacrificed short-term growth for long-term credit quality and earnings stability

AGF Credit Quality

- On slide 10, although delinquency and losses are somewhat higher than last year's all-time lows, AGF's credit quality remains strong and is substantially better than its target ranges
- Since the market downturn in 2005, real estate 60-plus day delinquency has risen only 43BPS to 1.95%
 - And net charge-offs remain extremely low at 37BPS less than half of our target range

FICO Score Breakdown

- On slide 11, we present detailed data on AGF's real estate portfolio showing a breakdown by FICO score range, vintage and other factors
 - Of the total \$19.2B portfolio, over 50% of the mortgage borrowers have a FICO score greater than or equal to 660 at origination
- Borrowers with a FICO score of 620 to 659 represent 17% of the portfolio
 - And borrowers with a FICO of less than 620 represent 31% of the portfolio
- Further delineation of the portfolio shows that the loan-to-value is more conservative as the FICO score declines, strengthening to 75% at the below 620 range
- As the real estate market softened in late 2005, AGF made a conscious decision to slow growth and maintain its consistent underwriting standards as shown by the tracking of loans produced in 2005 to early 2007

Loans

- AGF loans with LTVs greater than 95.5%, represent 19% of the portfolio, but they have performed well with a low 60-plus day delinquency of 1.53%, and only 548mm of these loans have a FICO below 660
- Low documentation loans, which make up 2.6% of the portfolio, have also performed well with a delinquency of just 2.3%
- AGF interest-only loans have a low delinquency of only 1.7%, and they include just \$299mm of loans with a FICO below 660 or 1.6% of the total real estate portfolio

Risk Management

- As previously highlighted and outlined on slide 12, AGF's conservative lending approach has differentiated them from many of the mortgage players
- AGF has mitigated risks by requiring full income verification on almost its entire real estate book in addition to having 85% of the portfolio as fixed-rate mortgages
- Only 11% of the overall real estate loan portfolio is due to reset by year-end 2008

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- Furthermore, AGF does not delegate underwriting on purchased loans to unrelated parties, has not made option adjustable-rate mortgages or ARMs, and has not made loans to LTV's above 100%
 - AGF tracks and adjusts underwriting standards monthly or quarterly

Summary

- In summary, AGF has a history of strong risk management and has successfully anticipated the risk in today's mortgage market by adhering to disciplined underwriting standards
 - Although the credit quality of AGF's mortgages can be affected by general economic conditions
- AGF has a dedicated focus on performing within charge offs and delinquency ranges and will continue to exercise prudent risk management

United Guaranty

Moving on to AIG's mortgage insurance subsidiary United Guaranty in slide 14

UGC has been insuring high credit quality, high LTV loans since 1963

Products include mortgage guaranty insurance on first and second-lien mortgages, which protect lenders against credit losses

AGF sources its business from major US lenders and, as a key component of its diversification strategy, currently provides first loss credit protection in 13 international markets

In order to maintain these long-standing relationships, UGC ensures a wide variety of mortgage products

UGC has experienced an average 10 year loss ratio through 2006 of 27% in its first-lien business

- But recent exposure to some higher risk products has negatively affected short-term results

UGC's sophisticated default and pricing models and predictive real estate scoring systems enable UGC to manage its risks and product mix over the long-term cycles of the business

Delinquency Rate

- The graph on slide 15 shows that UGC's primary first-lien delinquency rate is consistently below that of the mortgage insurance industry
 - This first-lien business constitutes 90% of UGC's net domestic mortgage risk-in-force
 - Although the difference has varied over time and has narrowed to 70BPS in recent months, UGC has historically outperformed the industry
 - This performance is driven in part by UGC's decision not to participate in significant volumes of bulk mortgage insurance, most of which was in the high-risk segment of the market

Portfolio Mix

- As shown on the portfolio mix slide on page 16, 90% of UGC's 25.9B of domestic mortgage risk-in-force consists of first mortgage risk, while the second mortgage business represents 10%
- Total delinquency on the first mortgage book is 3.8%

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- Loans with FICO score less than 620 constitute 8.5% of UGC's domestic mortgage risk
- Almost 70% of their net risk-in-force has FICO scores greater than 660
- Given the recent growth in US mortgage originations and the rapid runoff of older books fueled by historically low interest rates, 62% of UGC's risk-in-force is from book years 2005 through early 2007
- UGC has slightly over 16% of its risk in low documentation loans
- You can see from the chart that as the credit risk increases measured by FICO score
 - The concentration in limited documentation decreases with only \$100mm of risk in loans to borrowers with FICO scores less than 620
- The same can be said for option ARMs and interest-only products
- The \$2.3B of risk in these two products represent 9% of UGC's total risk-in-force
 - Exposure to borrowers with FICO scores less than 620 represent a mere 61mm or 0.2% of UGC's total risk

Domestic Mortgage Risk-In-Force

- The chart on slide 17 shows that second liens comprise only 10% of UGC's domestic mortgage risk-in-force
- Nonetheless, they are producing 58% of Q2 2007 losses incurred and are disproportionate to the total domestic mortgage insurance book
 - Although the softening of the housing market has affected all segments of business, high LTV, second-lien product is particularly sensitive to home price declines
- Second-lien default earlier due -- second liens default earlier due to the lack of a foreclosure requirement for claims to be paid as compared to first-lien mortgages that may take 12 to 18 months to go from delinquency to claim
 - As a result of this accelerated claim paying process, these losses are expected to work through the portfolio much faster
- Significant tightening of product and program eligibility in 2006 for second-lien business is resulting in improved credit quality and new business production

Risk Mitigating Factors

- There are a number of risk mitigating factors described on slide 18
- In light of the cyclical nature of the mortgage insurance business, UGC employs risk-sharing arrangements via captive reinsurance with most of its major lending customers
 - It purchases quota share reinsurance on portions of its sub-prime first-lien business and segments of its second-lien product
 - It has an aggregate stop loss provision of generally 10% on its second-mortgage product
 - And UGC maintains an exclusion for fraud on both its first and second-lien business
- Ensuring primarily prime, high FICO score loans within a highly diverse book geographically, UGC's largest business remains its first-lien fixed-rate mortgage insurance for single-family, owner-occupied residences
- Financial performance of UGC may remain under pressure because of current market conditions

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- But tighter underwriting standards by lenders, as well as elimination of certain risk factors by UGC will improve credit quality of new business production
- Moreover, current market conditions have reinforced the benefits of mortgage insurance resulting in higher volume and improved pricing for UGC

Insurance Investment Portfolios

Turning on to AIG's Insurance Investment Portfolios in slide 20, our insurance companies invest in the residential mortgage market across most security types

- Including agency pass-through and collateralized mortgage obligation issuances, prime jumbo non-agency CMOs, Alt-A and sub-prime RMBS, and other housing-related paper

Total insurance company holdings aggregate approximately \$94.6B at June 30, 2007 or about 11.4% of AIG's cash and invested assets, which is considerably underweight the overall bond market concentration in mortgage-related securities of about 28%

- About 83% or \$78.5B represents non-agency securities and are concentrated in the highest rate tranches with about 89% AAA rated and an additional 8% rated AA

Holdings rated BBB or below totaled approximately 400mm, well under 1% of the portfolio and less than one-tenth of 1% of cash and invested assets

About 10% of the 78.5B is also wrapped by monoline insurance

Non-agency RMBS is issued in tranche structures, such that the lower-rated tranches absorb any losses on the underlying collateral and insulate the higher-rated tranches from loss

- The sizing of the different tranches vary somewhat depending on the nature of the collateral and rating agency models and analysis

As a general rule, AAA and AA securities can withstand very significant default losses within the collateral

Breakdown of Investments and Sub-Prime RMBS

- Slide 21 presents a schematic showing the breakdown of our insurance company's \$28.7B in investments and sub-prime RMBS
- Residential mortgage-backed securities are structured with a pool of collateral of thousands of mortgages
- The securities are divided into tranches with different claims on the waterfall of cash flows emanating from the borrower's principal and interest payments on the underlying mortgages
- The AAA tranche has the first priority claim on these cash flows, followed by the AA tranche, the A tranche, down to the lowest equity-related tranche
- AIG's investments are made up primarily of AAA and AA tranches, representing together over 97% of our exposure
- Virtually all of our exposure is investment grade with a further 2.4% in A and BBB tranches

Breakdown of Exposure by Issuance

- Slide 22 shows the breakdown of our exposure by issuance year or vintage and by credit rating

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- As mentioned on the previous slide, AIG focuses almost exclusively on AAA and AA-rated investments
- The large portion of exposure to the 2005, 2006 and 2007 vintages, 98.3%, including 45.7% in the 2006 vintage is the result of our investing primarily in the shorter maturities of this asset class
- The weighted average life of the portfolio is 3.35 years
 - And therefore, earlier vintages have already substantially paid down
- Our decision to purchase the shorter maturity tranches is a result of both the need to match the duration of our liabilities in the book and our conservative credit risk appetite

Credit Perspective

- Turning to slide 23
- From a credit perspective, AIG views the AAA and AA RMBS market as a very safe asset class, with minimal risk of ultimate loss
 - First, the underlying mortgages have to be of high quality with LTV's averaging around 80%
 - AIG's underwriting approach is to avoid the higher-risk 80/20 or so called "piggy-back" loans and option adjustable-rate mortgages
 - Second, the securities are structured in a way as to provide significant subordination cushion to absorb a certain amount of losses at the lower level, higher risk tranches
 - For example, the loss cushion between the AAA tranche is generally 20 to 25% at inception and for the AA tranche the cushion is approximately 18%
 - In addition, the majority of AIG's RMBS holdings are structured to pay down early as the underlying mortgages amortize
 - As a result, the subordination cushion generally increases over time
- An additional structural enhancement is the amount of excess interest held that could be used to absorb losses
- In the typical sub-prime capital structure, this excess interest is approximately 2% per annum
- Finally, in some cases AIG uses third-party mortgage insurance to provide additional capital recovery and obtains monoline insurance wraps on approximately \$2B of its sub-prime portfolio

Structural Enhancements

- As described on slide 24, clearly the strength in our portfolio is also an indicator of the organizations with which we do business
- The originator and servicers of the mortgage pools are generally those organizations with strong financial discipline
- AIG generally targets shorter-term sub-prime securities
 - In addition to the structural enhancements contained in our RMBS holdings, AIG receives additional comfort from a number of other key factors
- AIG's RMBS portfolio is highly diversified in terms of location, tenor and size as reflected in the thousands of underlying mortgages in the pool

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 Event Description: Q2 2007 Earnings Call

Market Cap: 166,300.60
 Current PX: 64.85
 YTD Change(\$): -6.81
 YTD Change(%): -9.503

Bloomberg Estimates - EPS
 Current Quarter: 1.575
 Current Year: 6.671
 Bloomberg Estimates - Sales
 Current Quarter: 30566.208
 Current Year: 122687.981

- The underlying collateral is closely monitored by AIG by the respective collateral managers as well as by the rating agencies

Residential Mortgage Portfolios

- Over the past few months, a number of institutions have faltered because of their problems with their residential mortgage portfolios
 - The rating agencies have indicated that the 2006 vintage might incur losses of between 11 and 14%, approximately twice the high of 6.5% incurred in the year 2000
- Assuming the high end of the range, this would still be substantially below the cushions afforded to the AAA and AA tranches of approximately 25 and 18% respectively
 - To put these subordination cushions into context, assuming a depression scenario when housing prices could decline dramatically, say in the 30 to 40% range, there would have to be defaults by the borrowers in these pools approaching 45 to 60% to start to effect the AAA and double AA tranches
 - In the 2000 vintage defaults reached 20% resulting in the 6.5% loss experienced
- Our insurance companies also invest in collateralized debt obligations containing sub-prime mortgage collateral

Holdings of Sub-Prime Related CDO Paper

- Slide 25 shows that the holdings of sub-prime related CDO paper in AIG insurance portfolios are modest at \$253mm, they are secured by AAA and AA underlying collateral and are currently performing in accordance with AIG's underwriting expectations
 - AIG does not anticipate losses on its CDO holdings

Alternative Investments

- Turning to slide 26, within alternative investments AIG has no direct private equity investments exposed to the residential mortgage market, nor do we have any knowledge of any indirect exposures through our private equity investments
- Finally, we do not have any investments in hedge funds focused on the residential mortgage market

Financial Products Update

On slide 28, we begin our discussions of the activities of AIG Financial Products in the residential mortgage industry
 AIGFP's exposure to the market is derived through two sources

- First, they write extremely risk remote, Super Senior or AAA+ credit protection on highly diversified pools of assets, some of which include residential mortgages
- Second, they are cash investors in highly rated securities where some portion of the underlying collateral, which may include collateral from many sectors, includes residential mortgages

Credit Default Swap

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- While both of these activities involve significant notional exposure, the risk actually undertaken is very modest and remote and has been structured and managed effectively
- AIGFP has been running a successful business of writing Super Senior credit default swap or CDS protection since 1998
- As of June 30 this year they had a total net CDS exposure across all asset classes of \$465B
- The Super Senior portion, is the least likely to incur any losses in these deals since losses are allocated on a sequential basis from lowest to highest quality
- Before AIGFP would be at risk for its first dollar of loss, these structures would have to experience exceptional losses that eroded all of the tranches below the Super Senior level, including a very significant AAA layer of protection

Multi-Sector CDO

- AIGFP's entire Super Senior book covers many different classes with the bulk of it in corporate loans totaling \$258B
 - It also includes \$128B of exposure to prime mortgages, none of which represent US residential exposure
- The balance of 79B relates to multi-sector CDOs that FP helped to structure
 - These multi-sector CDOs consist of very diverse pools of reference securities, some of which are exposed to US sub-prime RMBS collateral
 - Of this 79B, 15B has no US sub-prime RMBS exposure and 64B has some collateral that represents US sub-prime RMBS exposure
- We are going to focus on this segment of the portfolio in this section of the presentation
- The multi-sector CDOs on which FP provides Super Senior protection are extremely granular with typically 175 to 200 different underlying rated obligations in the collateral pool
 - In those deals that do have some sub-prime RMBS exposure, the percentage is typically 50% or less
- The collateral pool is usually made up of other collateral such as auto loans, credit card receivables, CMBS or other assets
- In all cases, every transaction AIGFP has conducted has been carefully structured and screened as to collateral, manager and structure to ensure that AIG continues to receive the maximum protection to its position

Super Senior CDO Exposure

- Continuing on slide 29, the 64B of Super Senior CDO exposure that has some degree of US sub-prime collateral is split among 103 different deals. 45 of these deals totaling 45B of net exposure consist of multi-sector collateral, defined as high-grade
 - And being predominantly AAA and AA by virtue of the subordination embedded in each individual underlying security
- The average attachment point in these deals is in well excess of the regular AAA attachment point
- On average it is around 16% with a large part of this subordination, 44% on average being itself AAA
- Our notional net exposure to all of the highly rated sub-prime collateral after detectable subordination is 17.5B

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- The remaining \$19.4B of net Super Senior exposure is spread across 58 deals, where the multi-sector collateral is predominantly mezzanine such BBB securities again by virtue of its subordination in each and every individual obligation
- The attachment point on these deals is structured to be significantly out-of-the-money, at an average of 36%, and again a large percentage of the total subordination, 30% on average, is itself AAA

Notional Net Exposure to Sub-Prime Collateral

- Our notional net exposure to all of the sub-prime collateral in these deals after accounting for the high amounts of subordination is \$8.8B
- Given the diligence employed in selecting and structuring these deals, none of the AIGFP deals have experienced any significant collateral deterioration
 - There are only three deals out of the entire 103 multi-sector CDO transactions that have experienced any negative rating actions on any tranches subordinate to AIGFP's position
 - These three deals are rapidly amortizing and make up less than 0.5% of our CDO exposure totaling just \$296mm

Super Senior Protection

- Turning to Slide 30 with Super Senior protection, we're talking about a very remote risk
 - Which is defined and calculated not just by rating agency models but also by our own very rigorous internal models used on each deal AIGFP structures
- FP underwrites protection on Super Senior tranches of portfolios based on simulating the loss distribution of the underlying securities over the life of the transaction
- The simulation is conducted on a security-by-security basis with different security types treated differently with respect to, for example, recovery rates
- The determination of the attachment point for the most senior layer, the Super Senior tranche, is based on the assumption that the exposure to the portfolio will occur during a severe recession until the maturity of the transaction
- A Super Senior tranche must show zero losses 99.85% of the time in this severe recession scenario

Scrutiny Layers

- Prior to the simulation, a portfolio must pass several layers of scrutiny
 - First, we conduct due diligence on the originator of the portfolio focusing on the underwriting process
 - Second, the transaction must be structured so as to afford AIG the maximum protections to be acceptable
 - Third, the portfolio must meet various diversification criteria, for example, different asset categories and a portfolio cannot exceed certain concentration limits
 - Geographical diversification is also important
 - Fourth, each underlying security is subject to scrutiny by AIGFP credit officers and treated as stressed or less creditworthy in the simulation

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Risk Analysis and Underwriting

- Finally, the risk analysis and underwriting for each individual transaction must be approved by the credit trading team, the AIGFP credit officers and then finally by AIG's Credit Risk Committee
- All of AIGFP's deals are subjected to an exceptional degree of due diligence both at the inception of the deal and on a daily basis going forward
 - It is this due diligence that led FP to dramatically scale back their operations in this sector at the end of 2005 due to growing concerns about both the increasing percentages of US sub-prime RMBS exposure in the CDOs and the quality of some of the underlying collateral
 - As a result, they withdrew from making any further commitments to providing Super Senior protection on any deals that had US sub-prime RMBS collateral as they felt the new production was of a significantly poor quality

Multi-Sector Cash CDO Securities

- Accordingly their exposure to the more risky vintages of 2006 and 2007 are minimum
 - It is also the case that because AIGFP's exposure is always at the very top of the payment waterfall, over half their transactions have started to amortize and hence the exposure is currently being reduced
- As outlined on slide 31, the \$3.6B of multi-sector cash CDO securities, the second source of US residential mortgage exposure at AIGFP is virtually all AAA rated
- Further, the total exposure to all sub-prime collateral originated in 2006 and 2007 is only \$10mm

Enterprise Risk Management Process

Turning to slide 34

AIG has a strong enterprise risk management process where risks to the mortgage market are identified, assessed, analyzed, monitored and managed at all levels of its organization

All business units involved in the mortgage markets have credit function and carry out underwriting practices that utilize their own analysis and conclusions prior to inception of risk exposures, as well as on an ongoing basis

The foundation of AIG's decision-making process is based on this independent analysis

The fundamental analysis by the rating agencies is an important component of our analysis

- However, their ratings do not drive our decisions

CRC Reviews

- Decisions are made under credit authorities granted by AIG's corporate-level credit risk committee or CRC
- The CRC also reviews and governs credit risk tolerances for the business units
- AIG's corporate credit risk management department and the credit risk committee conduct regular reviews of the portfolios and provide independent assessments to senior management
- AIG establishes prudent credit reserves for all its exposures through a process that includes recommendations from the business units and approval by AIG actuaries, controllers, and AIG's Chief Credit Officer
- In conclusion, I will repeat what I said earlier

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- As Chief Risk Officer of AIG, I'm confident in our people and our risk assessment processes
 - Our exposures to this market are prudent, given the nature of our businesses and our financial strength

Martin J. Sullivan

Summary

Bob has described in detail for you AIG's presence in the US residential mortgage industry and our exposure to the sub-prime segment of the market

As he has discussed, AGF's businesses are performing better than delinquency and net charge-off target ranges

Disciplined underwriting, based over 50 years of experience in the sub-prime market, is serving the company well

UGC

- As a broad player in the cyclical market, in a cyclical market UGC has experienced a low domestic mortgage loss ratio over the past 10 years
- UGC is currently experiencing a significant decline in operating income, due primarily to unfavorable loss experience in its domestic second and first-lien mortgage businesses as a result of the continued softening in the US housing market
 - However, UGC is beginning to observe tighter underwriting standards on new business production within the mortgage market

Exposures to Residential Mortgage-Backed Securities Market

- Exposures to the residential mortgage-backed securities market within AIG's insurance investment portfolios are of a higher quality and enjoy a substantial protection through collateral subordination
- AIG does not need to trade mortgage-related securities and does not depend on them for its liquidity needs
- Temporary market disruptions may have some non-economic effect on AIG through unrealized losses
 - However the sound credit quality of the portfolios should result in collection of substantially all principal and interest under any reasonable scenario

Financial Products Portfolio

- AIG's Financial Products portfolio, Super Senior credit default swaps is well structured, undergoes ongoing monitoring, modeling and analysis and enjoys significant protection from collateral subordination
- Certainly, we will be following this market closely during this period of volatility and correction and we will continue to manage these risks carefully
 - However, in every period of uncertainty, there is also opportunity

Future Perspective

Given the high quality of our investments and our superior financial strength, AIG is poised to take advantage of these opportunities as they arise

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As I said, with all the uncertainty, recent volatility and on some occasions even panic in the market, hopefully we have demonstrated that with our superior financial strength, liquidity, and cash flow

- While we believe AIG is a very safe haven in stormy times and while I remain extremely confident about our future

Q&A

<Q - Joshua Shanker>: I hate to start off with questions on the mortgage space, but I am sure I am not the only one. My first question regards AIG's financial products. I am trying to understand, A, has there been any slowing of business generation as there might be less buyers for the less subordinated tranches? Two, has AIG corporate been a purchaser of any of the less subordinated tranches from AIG Financial Products? And the third question is given some of the ratios that we've seen for Q2 2007, which actually look pretty good in American General, should we be concerned about what Q3 2007's ratios are going to be looking like?

<A - Martin Sullivan>: Okay. Joshua, we have Joe Cassano on the line. So, Joe, would you like to respond to the first part?

<A - Joseph Cassano>: Sure. Actually Josh, I've also got Andy Foster with me, who trades our credit business here in the UK. And why don't we answer it together. And Andy, why don't you give Josh a response to what we see going on in the market now?

<A - Andrew Foster>: I think in terms of whether we are going to be slowing down our business, as Bob outlined, the CDOs and writing protection on those, that basically stopped completely back at the end of the 2005 when we stopped taking sub-prime as collateral. Given the increasing percentage in all the CDOs, that meant that we actually -- we were effectively ruled out of that market. So, yes, that part of our business is effectively stopped.

<A - Joseph Cassano>: And Josh, to add further to that, obviously with the last four weeks of market volatility here, there isn't -- people -- we aren't seeing new portfolios of other assets to write right now, and so there has been a bit of a slowdown in the flow within the credit business. As you know, the financial products platform is fairly diverse, and we still see good flows in our equity business, our commodities business, our currencies and REITs businesses.

<Q - Joshua Shanker>: In terms of in the past pre-2005, was AIG corporate a buyer of any of the less subordinated tranches --?

<A - Joseph Cassano>: If it did happen, it happened coincidentally and it may have been very small, but it's -- we actually -- we don't work in a coordinated fashion with the parent in terms of the Super Senior portfolios that we have been writing protection on. And if it happens, it has to be a de minimus one-off kind of thing. I can't imagine that there is much of it that has gone on.

<Q - Joshua Shanker>: Okay, very good. And the American General question about ratios in Q3 2007?

<A - Martin Sullivan>: Yes, Joshua, Rick Geissinger is here, so he can answer that.

<A - Frederick Geissinger>: Our credit quality statistics for the end of Q2 are strong as Bob mentioned. We set target ranges back in 1996, and we are well below those for delinquency, which was -- the target range was 3 to 4%, charge-off range was 0.75 to 1.25. But we are well below those target ranges within which we can operate the business at a 15% after-tax ROE or better. If you look at historical seasonality -- delinquency and charge-offs get a little worse every year in the third and Q4. So you can expect to see those numbers be a little bit higher. We do have July results and the change in delinquency and charge-offs is slightly up, but de minimus.

<Q - Andrew Kligerman>: First question, partnership income, it was phenomenally strong this point. Could you give a little color at this point in time how the performance would be if the quarter stopped right now and then I will ask a follow-up question in what [audio gap]

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<A - **Robert Lewis**>: I think it will be a bit difficult to tell you exactly what it would look like if the quarter stopped right now. I think we have said repeatedly that we expect our partnership portfolio including our hedge fund portfolio yield somewhere between 10 and 15% a quarter on a long-term basis. We have been significantly north of that for I believe, the last six quarters, the last five quarters anyway.

<Q - **Andrew Kligerman**>: Do you think that it would be down materially from that target range?

<A - **Robert Lewis**>: No. I really can't give you a number at this point.

<Q - **Andrew Kligerman**>: Okay. How about

<A - **Martin Sullivan**>: Andrew, at many times our anticipated range is between 10 and 15%.

<Q - **Andrew Kligerman**>: I know that. I am just kind of curious because it's been a rocky quarter, but I will move on. Japan, could I get an update on the regulatory environment that was mentioned in the press release and how that might affect the Japan A&H sales going forward?

<A - **Martin Sullivan**>: Absolutely. In fact Bob Clyde is on the line from Tokyo. So, Bob you could you respond to Andrew?

<A - **Robert Clyde**>: Yes. Hi Andrew. The regulatory environment is still pretty strict. As you know the claims reviews that we have been going through have been public information and that has put a little bit of pressure I think on sales for the industry. This is an industry-wide issue. We, in Q1 the FSA undertook an industry-wide claims review covering claims for the periods of 2001 to 2005 and required us to submit our results to the FSA on April 13th. At Q1 we reserved for our best estimate an exposure for additional claims resulting from this review and subsequent follow-up with our claimants. And we have had charges as you know for additional claims and reserves in Q2.

<Q - **Andrew Kligerman**>: Yes. Hello. The Japan sales, my question was are they going to pick up again now, are they ready to move north, or do you think there will still be pressure for a while?

<A - **Robert Clyde**>: Yeah, Andrew. I'm sorry. We expect H2 to be better than H1 by a few percentage points frankly. We have got -- we anticipate that -- on June 25th ALICO Japan launched a new return or premium medical product called Returns, which has been well-received by our agency force and also direct marketing. Direct marketing premiums will take some time to be realized, but the initial response rate to our TV advertising has been good. In addition, ALICO has launched a revitalization plan for agency with renewed emphasis on medical sales. Edison Life has seen increased interest in its cancer products and Star Life continues to produce strong medical sales as it expands its agency and branch channels. And furthermore, while we continue to rationalize our marketing spend in ALICO Japan over this past year, that has had a dampening effect on sales. It is clearly improving our profitability, which will help drive the bottom line I think going forward.

<Q - **Andrew Kligerman**>: Okay. And then just lastly, you mentioned that you had strong commercial property, commercial liability rates, or results, it was a little weaker in excess casualty and D&O, could you give us just a sense of the rates, where they are going in some kind of a range right now?

<A - **Martin Sullivan**>: Sure, I will give you an overview Andrew and then I will ask Chris and Nick to respond between domestic and international. As we mentioned on our first-quarter call, we saw an uptick in competition in April. That continued somewhat through the quarter. Rates domestically were down 7 to 10% internationally in the 10% range, but I would say that again we saw a further uptick in competition in the month of July. Overall, terms and conditions are still holding reasonably well particularly outside of the US, but we're seeing some pressure on deductibles. It is not a significant change, but it is a little difference in scenario. But let me just hand over to Chris to add some more color there.

<A - **Christopher Swift**>: Yes, further on the D&O rates, they were down for the quarter about 10 to 15% and on excess liability down about 8 to 10%. As Martin said, July was a little tougher month. It was the first time our overall portfolio and property actually went to negative rates, down a few points. So, I think Q3 is heating up a little bit more than Q2.

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<A - **Martin Sullivan**>: Nick, internationally?

<A - **Nicholas Walsh**>: On the foreign side our plan called for about a 5% decline and we're running about 10 as Martin said, but remember that half of Foreign Gen is consumer business rather than commercial, so the effect of the cycle is different. And the effect is different across product and region. In general, property pricing is probably under most competitive pressure and terms are being negotiated, but the principal markets are withstanding those. On the casualty side, pricing is reasonably flat but there is pressure on terms as far as deductibles are concerned. And in financial lines, particularly management liability or D&O, the effect on major cap in Australia and in the UK is quite competitive and there is broadening of coverage in Europe. But, that's much more a function of the sophistication of the development of the market rather than effect on capacity.

<A - **Martin Sullivan**>: I would just add Andrew that the one market that is very competitive at the moment is the aviation market. It just seems to get more competitive every single day.

<Q - **Jay Gelb**>: First on an overall basis on the investment portfolio, can you walk us through the accounting treatment of when AIG may need to take mark-to-market adjustments in the investment portfolio because of the sub-prime issue? And if you could sort of quantify that quarter to date, that would be helpful. Then I had a follow-up.

<A - **Robert Lewis**>: Yes. Normally we would take a mark-to-market if one of two things were true. I mean one obviously, if we sold the securities, actually there are three things. Two, if we had an intention to sell the securities, or three, there is a technical provision of the accounting rules called EITF 99-20, which generally would apply to only the lower-rated tranches, but which might require a mark-to-market in effect if the anticipated cash flows on a given security were to change in a manner that was deemed to be adverse to the holder. Though at this point, it is really either sale or intent to sell and we don't see either of those being a likelihood on this portfolio.

<Q - **Jay Gelb**>: So, just to follow-up on that. Since there is no expected material deterioration on the cash flow trends in the residential mortgage-backs or the rest of the portfolio, you would not anticipate a downward mark-to-market in the investment portfolio at this point?

<A - **Robert Lewis**>: Not on any general basis. I mean we do have small pieces of the lower-rated pieces and some of those might need to be looked at.

<Q - **Jay Gelb**>: But nothing for the AA or AAA, which is the vast majority of the portfolio?

<A - **Robert Lewis**>: No.

<Q - **Jay Gelb**>: Okay. And then on page 67 of the supplement, you disclosed in the mortgage-backed securities the non-agency Alt-A and the second liens, can you give the vintage years for those or just the 2006 and 2007?

<A - **Robert Lewis**>: Yes. I might mention the second lien is almost all wrapped by monolines as well.

<Q - **Jay Gelb**>: So, that is all wrapped with the AAA?

<A - **Robert Lewis**>: It's almost all, not all.

<Q - **Jay Gelb**>: Okay.

<A - **Robert Lewis**>: Potentially all. The second lien is about half 2007 and half earlier. That is all very short paper. And on the Alt-A, give me a moment. On the Alt-A by vintage, the total 2007 is about 14%, 2006 is about 43%, 2005 is 31%, earlier is about 12%.

<Q - **Jay Gelb**>: Okay. Thanks for that. And then on the property/casualty side, there continued to be some adverse development in the 2000 year and prior. I was just wondering if you can give us a little more color on that and when perhaps do you see that trend easing?

<A - **Martin Sullivan**>: Jay, Frank is here, so I will ask Frank to comment.

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<A - Frank Douglas>: Yes. We highlighted that again this quarter. It was a little bit heavier than Q1, the development as you note from – actually it is 2002 and prior, I believe you said 2000 and prior. Excess casualty was about 140mm of that this quarter and about 110mm came from Transatlantic. Most of that by the way was also excess casualty.

What it largely relates to are latent type of claims, a lot of which wouldn't really hit us today, given the changes that have occurred since the soft market. For example, some of the large losses relate to pharmaceuticals or construction defects or product aggregates where we are dropping down from an excess attachment to pick up primary claims that have exceeded an underlying aggregate. Our current policy forms and underwriting guidelines would actually eliminate a lot of those claims.

So we do think the exposure we have for after 2002 to those kinds of claims is going to be dramatically less. As to when they may stop. These claims are not going to go away next quarter. They are latent, the nature of claims such as product aggregates are very hard to predict. They don't follow a normal loss development pattern because you don't have any claim at all until the underlying aggregate is eroded. So it is hard say exactly when they are going to disappear. But we are many years now removed from the soft cycle. And we do expect them to diminish each year as we go forward. This was an adverse quarter. I don't think this quarter should be regarded as the ongoing expectation.

<Q - Thomas Chohnoky>: Yes. I have a couple of questions. Bob, in your presentation you described some disaster scenarios for your mortgage portfolio. However, on the CDOs your wrapping in in Financial Products. Can you -- if you did I apologize, I missed it. But can you kind of give us a sensitivity analysis or perhaps go into a little more detail of what could really cause losses to emerge on some of these CDO's? What kind of economic conditions would we have to have?

<A - Robert Lewis>: I guess the short answer Tom is an extreme economic event. As I mentioned in my presentation. AIGFP does a considerable amount of modeling on stress scenarios to first determine where the attachment point would be on the writing of a Super Senior cover. So that modeling that is undertaken is intended to stress the underlying values of the collateral pool, which is a diversified portfolio of CDOs, and to stress that under extreme economic conditions. And after that, to determine that their attachment point would be above that of an extreme condition in the marketplace. Joe Cassano you might to add some color on that.

<A - Joseph Cassano>: Yes, hey Tom, it's Joe Cassano and Andy Foster here. One of the other things you have to look at in those CDO pools along with what Bob said about, the way we model it is we are looking at a continuous recessionary cycle that lasts for what we anticipate to be the life of the underlying CDO security that we are wrapping. So there's a fairly extensive severe recession that needs to go on. But the other thing is that the granularity and the diversity within the underlying CDOs and then the collateralization that takes effect within those CDOs and maybe Andy you want to talk a little bit to that.

<A - Andrew Foster>: Absolutely. Obviously, all the pools are extremely diverse. And I think in terms of – the direct answer to your question is what could they sustain. I think if you look back a few slides earlier. when Bob was outlining sort of the loss scenarios and the stressors that the underlying securities can take when we were looking at the AIG investment portfolio. Don't forget obviously within the CDOs you have got subordination upon subordination, so you need the scenario where you eating through into the sort of AA, AAA type underlying securities. And then even if you did manage to have that scenario, obviously all of our CDOs then have additional subordination on top of that, so you'd have to eat through that and then eat through the additional subordination. So what we are modeling is this sort of disastrous type scenario and even in those cases our CDOs are not blowing up for the reason that we are modeling these and our VAR is at this 99.85 percentile. So...

<A - Joseph Cassano>: It is hard to – sometimes I feel like it is hard to get this message across, but these are very much hand picked. We are very much involved in the process of developing the portfolios in which we are going to wrap and then picking the attachment points. And people who have been willing to work with us in order to do that to create the value that they do in these underlyings. And so the combination of the diversity, the combination of the underlying credit quality and then the stresses that we put it through to make sure that we can hit these marks, it is hard for us, without being flippant, to even see a scenario within any kind of realm or reason that would see us losing \$1 in any of those transactions.

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<Q - **Thomas Cholnoky**>: That's okay.

<A - **Joseph Cassano**>: Just okay?

<Q - **Thomas Cholnoky**>: I agree with you. I tend to think that this market is overreacting because – anyway that's a separate point.

<A>: That's why I'm sleeping a little bit easier at night Tom.

<Q - **Thomas Cholnoky**>: Joe, did you get involved with any CDO squareds at all?

<A - **Joseph Cassano**>: It is one of those markets that we never got comfortable with, Tom and it has been around for a long time and it is just something that doesn't – there are people who do and I don't want to criticize it too much. It is just a place where we couldn't get comfortable with the risk involved.

<A>: Exactly. We have always had this desire and need to be able to look through to all of the underlying obstacles and be able to stress those, and pick them very selectively, choose the obstacles that are going to go into our CDOs. So, when you get into the CDO squared product, that's actually much harder to do. So, we shied away from that and didn't do any deals where it was CDO squared.

<Q - **Thomas Cholnoky**>: Okay. And then on the BBBs, I guess that has been an area that has been of concern to some area and that maybe 60% coverage might not be enough on these. I mean, is that – I mean how should we look at that? Is there something there that we need to worry about or are you really comfortable that you've really hand picked through these as well?

<A>: Well, I mean absolutely we hand picked them. So, we are extremely comfortable. The diligence that we did in all of our portfolios was across all of them. Perhaps to give you an illustration, if you look at the rash of downgrades that you have seen across all the different collateral in all the different sectors, it's less than – so for our existing CDOs, it is less than 0.5% of all the underlying collateral is currently on review for a downgrade. And to think how many have been sort of – have had that sort of negative watch listing.

And also, one of the key points to take away is definitely that we stopped this business at the end of 2005. Most of the stresses that people are sort of really concerned about I think are very heavily concentrated in 2006 and 2007. We have almost zero exposure to that, and again as Bob outlined in the slides, there is almost zero exposure, net exposure after our subordination to all of that collateral assuming it was all wiped out tomorrow with zero recovery. We have an extremely small amount to that. And I think that's -- again it is not just the portfolio construction, it is the structure of the CDOs and then it is the vintage that we decided to invest in.

<Q - **Thomas Cholnoky**>: Okay. And then, sorry, if I could just ask one operating question, Martin. I understand that ALICO was given – recently won a partnership with the Japan Post and I was just wondering how we should look at that on a go-forward basis on what that may do for Japan production?

<A - **Martin Sullivan**>: Yes, we are in ongoing dialogue with Japan Post on a number of opportunities. We've been in advance of ourselves in giving any color at this moment in time because as you know, it is going to take a period of time for the post office to privatize in its current form and we are sort of working with them in a number of initiatives. So, as something more concrete is available we will be happy to disclose that.

<Q - **Thomas Cholnoky**>: I assume that would be more of a 2008 event as opposed to 2007?

<A - **Martin Sullivan**>: Well. I think the privatization is going to be taken a number of years. So certainly forward-looking.

<Q - **William Wilt**>: I will stick with the same theme, Foreign Life. Looking at Asia, Foreign Life in Asia, operating income down about 4%. It looked like it all came or most of that came from life insurance down about 8% to operating income, premium deposits under considerations was up nicely as – it was moderately positive. I wanted to see if there was some color that could be provided there?

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<A - **Edmund Tse**>: Those numbers released that is somewhat misleading is strictly based on Q2. And because this comparing to the last year's same quarter, the last year there was a one-off for item adjustment of certain investment income in the unit trust, and which was \$144mm. And if you normalize that in current quarters, operating income for the Life or Foreign Life, is up from 3.7 up to 14.3% and the same applies if you take the Life itself, because applying this income or applying just to the life insurance so that you normalize it and we will take double-digit operating income increase.

<Q - **William Wilt**>: Okay. That is good to know. Thank you. The second one, if I may. On the second lien mortgage insurance with United Guaranty. There was a reference in the presentation to stop loss reinsurance. Maybe, a quick recap of how that works. I thought it was 10% of the notional exposure? Is that 2.5B or 250mm aggregate stop loss? And I wonder how close you were to hitting that aggregate stop loss? Thanks.

<A - **Martin Sullivan**>: We've got Billy Nutt with us here. So Billy?

Answer – William Nutt, Jr. : Thank you William. We don't implement stop loss limits on all of our second lien policies. As you see on the chart in the presentation that Bob Lewis presented, chart 16 of our domestic mortgage net risk-in-force 10% of that is related to second liens, which is \$2.5mm. And with average stop loss limit on that of about 10%, you're looking at about \$250mm of total stop loss, which is rather modest. Some of our policies are close to their stop loss limits, but a number of them are not even close to their stop loss limits and that is due to the diversification of the portfolio.

<Q - **William Wilt**>: That is helpful. So it would be too simple looking at I guess page 17 the domestic second lien losses of 159mm in Q2. It is too simple to just take that number add losses in Q1 and presume that you're close to in a view being able to benefit from the stop loss?

Answer – William Nutt, Jr. : Well. That would be too simple, but we will benefit from the aggregate stop loss limits in some of our policies.

<Q - **Daniel Johnson**>: Within the Life and Retirement segment couple of questions please. We used to have disclosure on the runoff block. Honestly maybe I have missed it. It was running around 15-ish billion or so. Can you give us an update on where that is at?

<A - **Martin Sullivan**>: Chris Swift will respond to that.

<A - **Christopher Swift**>: Dan are you referring to the domestic fixed and variable annuities that we put into runoff?

<A - **Martin Sullivan**>: I believe that was what was in there although I can't entirely be sure. But yes, it was about 15mm -- billion-ish for the last couple of quarters coming down and then it looks like it disappeared from the supplement or moved possibly.

<A - **Christopher Swift**>: We did make a supplement change, broke out Life and Retirement Services differently. If you look at the fixed annuity line for Domestic Life, we also combined that with the old Domestic Life runoff. And within the Retirement Services, there is a runoff category also where we just provide reserves. It's running off as expected and I don't think there is anything abnormal in there. But it is declining. I think reserves are closer to the 12B level than 15.

<Q - **Daniel Johnson**>: Okay. Thank you for that. Within the retirement services business, can you give us a sense -- there was some commentary in the Q, but maybe you could give a little more discussion around about what the flows look like in light of redemption profiles and new business effort?

<A - **Martin Sullivan**>: Jay is on the line from California. So Jay, can you respond to that?

<A - **Jay Wintrob**>: Sure. Thank you. Good morning Dan. First of all in the supplement I think the flows are pretty clearly laid out. And mainly that's going to be driven prospectively by TBOC sales, that is because we've disclosed we continue to expect renders at these kind of levels or higher in the fixed annuity business due to the shape of the curve and the fact that we are five years out from our record sales years. We are seeing some improvement in the VALIC

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group business, and also in the variable annuity business. And again on the sales side, with sales momentum I think we can improve on the flow side. It will be harder with fixed annuities because it's so subject to the two factors I mentioned -- the shape the curve and the fact that we are five years out on our two record sales years starting at the end of this year.

<Q - Daniel Johnson>: Great, okay. So that's on the Life side. On the P&C side, the workers comp discount rate change, I'm certainly not an expert on this one. Can you give us a little color around what drills that? What I think if I read right is \$155mm adjustment. And then I think we all look at the different accident years between say the good years and the bad years. Can you help us sort of rethink about your disclosure of the accident years excluding that 155mm positive?

<A - Martin Sullivan>: Well hopefully Frank is the expert.

<A - Frank Douglas>: Yeah, this is Frank Douglas. The work comp discount, which we adjust quarterly was previously subjected to really a full actuarial analysis only in Q4s. What we changed this quarter, which we do disclose in the Q is that we are now updating the analysis quarterly. And that did result in an increase in the discount of 155mm for workers' comp, 125mm of overall discount including discount in other lines.

I think that's not a one-time aberration. This is a process that we are going to continue going forward and as our work comp reserves increase the discount in those reserves is going to increase. It's spread across all accident years as we have a significant volume of workers comp reserves in all accident years. You would see in the disclosure we have on accretion of discount, you would see that number was 12mm this quarter. That would tell you what the prior accident year impact was of the unwinding of the discount in prior accident years and the balance of the discount is being put up in the current accident year against our workers' comp reserves.

So, the prior accident year reserves will continue to -- discount will continue to accrete or unwind every quarter. But as we do an updated evaluation each quarter of our workers' comp losses and their payout pattern and interest rates, the amount of discount in any one quarter could vary from what the change was the prior quarter. But as our work comp reserves increase, our discount will increase proportionally with it. And if you look at our 10-K, you would get a picture for how it's changed over the longer-term period. How much discount is remaining by accident year. We don't show that every quarter, but if you look at it by -- in the 10-K, I think you would be able to see the general pattern by which it amortizes or unwinds.

<Q - Daniel Johnson>: Maybe my better question is, sort of was that 155 in the 120?

<A - Frank Douglas>: No.

<Q - Daniel Johnson>: Okay. That's the answer to the question. Thank you very much.

<A - Frank Douglas>: We do not include discounting in the loss development. All of the loss development tables are based on undiscounted losses. Thanks, Dan.

<Q - Tamara Kravec>: Two questions. First just going back to the mortgage insurance business, the first lien business, which you had put in your release is 77% of the total there. And it generated about 42% of the losses and I guess -- I just wanted to get more granular on specifically where that business is underperforming in terms of the losses rising. Is it in particular vintages, particular FICO scores, LTVs. You have broken it down, but if you can just give a little bit more details on that. And then my second question is you are well on your way with the buyback and you've articulated before that you are looking for 5 billion this year and just wondering, given the pace that you are on right now, would you consider exceeding that and doing the full 8B this year or are you sticking with what you originally laid out? Thanks.

Answer -- William Nutt, Jr.: First of all a correction. In the domestic -- a correction in your statement, the domestic mortgage net risk-in-force, 90% of that is in the domestic first-lien business and 10% is in the domestic second-lien business. The first-lien business represented 58% of our losses incurred and that is generally occurring along all segments of the business in terms of FICO scores, but in particular we are seeing stress in those states that have experienced an economic recession, the upper Midwest, Indiana, Ohio, Michigan, West Virginia. Those markets that

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have been in a manufacturing recession. We are also beginning to see some deterioration in incidents and severity in California and Florida now.

<A - Martin Sullivan>: And on the second part of your question, on the stock repurchase, obviously we have authorization up to 8B. We said we would do 5B in 2007. Obviously we will keep our options open and if there was any change in that timing, obviously we would disclose that to the market.

<Q - Mark Lane>: Frank, can you talk about the commercial side loss cost trends and have you seen any changes or what is your thought about how loss costs trends will develop over the next year on the commercial side?

<A - Frank Douglas>: Well, I can tell you how they have developed up until now. Obviously, it is an extrapolation that it will happen over the next year, but certainly what we have seen and reported each quarter for the last several years has been favorable loss trends for primarily accident years 2003 and forward. We are still seeing those favorable trends in accident year 2006, which is the newer phenomenon that we have seen in the last two quarters. Obviously, one can't say because we have seen that for these two quarters it is going to automatically continue for the next four quarters, but that might be an assumption one might want to make. I am not saying we make that. We assume our reserves are adequate based on an assumption that loss costs are going to continue to rise from one accident year to the next. After each quarter's data comes in, we reevaluate with the updated data and we have been able to avoid having to raise some of our loss ratios frankly because the prior accident years and the more recent years continue to develop better than expected. So the prior -- as the accident year loss ratios goes down for 2003 through 2006 it alleviates the pressure to increase the loss ratio for the current accident year. Whether that will continue is obviously unknown, but that has obviously been the pattern we have seen for the last couple of years.

<Q - Mark Lane>: So, basically going forward you are saying you are just kind of watching, I mean there is really nothing that you can do to anticipate anything. It is just you are watching and you are using historic trend and you will adjust it if it is not a trend basically?

<A - Frank Douglas>: Yes, as Chris noted earlier, if rates are going down and if they accelerate in a negative way, that obviously puts upward pressure on the current year loss ratio. However, that can be mitigated or offset completely in some cases or recently in almost all cases by the favorable emergence from prior years. So, it is a quarterly analysis we do for every profit center for every product now. We look at what losses came in from all accident years including the most recent years and we put into the equation what the rate changes earning in the quarter are and come up with an indicated current year loss ratio.

<Q - Mark Lane>: Do you have the developed accident year loss ratio as of June 30th from 2006?

<A - Frank Douglas>: For many classes we are developing the accident 2006 losses. For other classes we are using expected loss ratio method [audio gap].

<Q - Mark Lane>: But do you have like as of June 30th, do you have the developed accident year 2006 -- I am sorry the --

<A - Frank Douglas>: The number at the AIG level is currently 62.9.

<Q - Mark Lane>: At June 30th?

<A - Frank Douglas>: That is our current AIG all property casualty segments combined loss ratio.

<Q - Mark Lane>: 2006 developed as of June 30th.

<A - Frank Douglas>: Right. That compares with 64.4 currently for accident year 2007.

<Q - Mark Lane>: Perfect. Okay. On the Foreign Life, I know you have answered this question, I mean, if the business is very difficult to analyze even with the increased disclosure. Earnings have been under pressure for a number of quarters, particularly in Japan. Premium production of the single side, single premium side has been extremely robust for the last several quarters. So, when are we going to start to see that hit the bottom line? Can you talk about profit emergence within Foreign Life over the next six to 12 months? It is just very difficult to figure out any trend

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there.

<A - Edmund Tse>: Really just how soon all those robust single premiums will hit the bottom line and so a little bit more difficult to answer. It depends a lot on the consistency. But over time definitely the increase in AUM because of the single-premium products. And that will contribute a lot more to our bottom line consistently over the year. And as you can see it, we have very consistent growth either in top line or in many countries even in bottom line over the last few quarters. And maybe Chris you could add some color to it?

<A - Christopher Swift>: Sure Edmund. It's the profit emergency is a little slower with our single paid business compared to our regular premium business as Edmund was referring to, but where we price it is in essence the net spreads that we get in it are attractive and it will emerge over time. As Edmund said in his opening comments and we have some comparability issues this quarter. If you really take that away Foreign Life is up 14%ish which is probably on the high-end of a long-term expected growth rate but probably not too far from where we really see the total Foreign Life business going. We have commented in the past in Japan on Star and Edison is being year end of the inflection point where we think they could start to grow faster, we still see that and believe that as we head into the 2008 planning cycle.

<Q - Jay Cohen>: Shifting back to the portfolio. It seems like the folks within Financial Products and American General Finance really saw the writing on the wall to some extent with the whole mortgage issue in the sub-prime side and the pull back. Was there any communication between those folks and the investment folks? Because it seems like the buying of this stuff on the portfolio side continued pretty aggressively in 2006. Although it is hard to tell. What is the communication lines like between these different areas?

<A - Robert Lewis>: First of all -- First of all Jay, I think it is -- this is Bob Lewis. I think it is fair to note that there are some structural differences in the business, that I think Billy might comment on. There are some structural reasons in the business why the timing of an effective change is slower in UGC's business to take effect than it can be on the investment side or the AFP side. Billy you might want to just sort of mention that reason.

Answer -- William Nutt, Jr.: Sure. I will be pleased to Bob. Jay, UGC and American General Finance really have different business models. We are a broad market mortgage insurer; AGF is a niche mortgage lender. We must participate in the broad market with all of our major lenders, which includes insuring some segments of the higher-risk products as well as insuring a large market share of their A paper business. And so we basically follow the fortunes of the market. We follow the fortunes of the lender where AGF can pull in and out of markets depending upon the dynamics that are going on in those markets. Also what is important to note is UGC is in first dollar loss position where AGF has equity or other credit protection before they incur a loss. We do communicate across units, we understand each other's respective businesses. But we have distinct business models.

<A - Robert Lewis>: And then coming over to the investment side. I would like to mention that there is some structural reasons for the investment that has to do with matching our liabilities. Richard you want to explain.

<A - Richard Scott>: Yes. I might mention that, there is so many different facts that one might put out there. But one thing you should understand is we did change our basic underwriting in 2006 and 2007, particularly with regard to Alt-A where we switched to almost exclusively Super Senior structured AAAs which have subordination under them, more akin to sub-prime deals than a typical Alt-A deal would have. We do have good communication across groups. We do talk to FP we do talk to AIG Finance, we do talk amongst ourselves. I do think that everyone should understand that since this is primarily a AAA portfolio, we are not overly concerned about modest or even fairly aggressive deterioration in these markets. But the switch in the Alt-A portfolio in particular to the much more highly protected tranches was certainly directly related to our perception of the underwriting standards in the market.

<Q - Jay Cohen>: That's helpful and then just one quick follow-up. Just to understand the mark effect. You have said initially that the quoted prices for many of the securities has gone down. But it sounds like that would not necessitate a mark-to-market on your behalf. Is that right?

<A - Richard Scott>: All of our assets get marked through the balance sheet with a difference in fair value going to other comprehensive income. I mean whether or not we intend to sell them or not. But whether or not it goes through

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reported realized gains and losses is a question. i.e. is marked-to-market through the income statement is a function of either deciding to sell it or selling it.

<A - Robert Lewis>: Jay, virtually all of the RMBS securities that we hold are unavailable-for-sale. So they do – as Richard just said, they get marked-to-market on a quarterly basis through accumulated other comprehensive income. Only to the extent that there was any determination that there was an other than temporary impairment in those securities would there be an income statement effect. And I think we have talked through this presentation and why we don't believe that is going to occur.

<Q - Jay Cohen>: Right. That is what I thought initially. Okay. Great. Thanks.

<A - Martin Sullivan>: Jay, I would also just draw your attention on page 14 of the presentation where we obviously layout that the average domestic mortgage loss ratio for UGC over the last 10 years is some 27%. As Billy has mentioned before I guess you could define the environment he's trading in at the moment is the mortgage insurance definition of a cat loss.

<Q - Charles Gates>: Two questions. My first question, haven't the two recent Supreme Court decisions, the one June 18th concerning securities underwriters and the one June 21 concerning this year Tellabs, weren't they very important, arguably positives for your business and loss cost trends?

<A - Martin Sullivan>: Yes. Chris is going to respond.

<A - Christopher Swift>: Charlie, obviously on the surface they're positive. But, you have to be very cautious. And as we have seen in the past when you get big decisions that are favorable that things tend to change in the marketplace and the plaintiff's bar figures ways to get around it. So on the surface and right now we think they are positive but we haven't taken any account of those decisions into our loss ratios.

<Q - Charles Gates>: I guess the only other question at this time would be with regard to all these concerns about marking assets to market. I don't think I can recall a day when the yield on the ten year was down 10BPS before to 4.76. Isn't that a very important positive from the standpoint of marking securities to market?

<A - Christopher Swift>: In general I would say, yes, it is, since we tend to have a modestly, I would say, an intermediate duration portfolio.

<Q - Charles Gates>: I guess the only other question, on page 29 of the mortgage presentation, you show this year credit default swap of \$19.4B where the collateral is predominantly BBB. To what extent is that a source of worry?

<A - Martin Sullivan>: Joe or Andy you could respond to that?

<A - Joseph Cassano>: Yes, hi Charlie. Maybe we -- that was the same question that Tom Cholnoky was asking too when he looked at that. I think maybe to put that further in perspective, that underlying pool are pools of BBB assets, but when you pool those up, they have created other BBB -- AAA rather, excuse me, AA assets and then we have attached above that AAA group when they got pooled. And as we were saying to Tom in the previous answer, going through the stress test that we have and having hand selected the underlying assets that are involved in these portfolios and then stressing the underlying CDOs or the BBBs that are in there, we are quite comfortable that there is no issue with those portfolios.

And we wanted to make sure, in this presentation we broke out exactly what everything looked like in order to give everybody the full disclosure, but we see no issues at all emerging and we see no dollar of loss associated with any of that business in any reasonable scenario that anyone can draw. When I say a reasonable, I mean a severe recession scenario that you can draw out for the life of those securities.

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