



Yale SCHOOL OF MANAGEMENT  
*Program on Financial Stability*

## EliScholar – A Digital Platform for Scholarly Publishing at Yale

---

YPFS Resource Library

---

9-14-2008

### FRBNY Alejandro LaTorre e-mail to Timothy Geithner re Pros and Cons on AIG lending

Alejandro LaTorre

<https://elischolar.library.yale.edu/ypfs-documents/4813>

---

This resource is brought to you for free and open access by the Yale Program on Financial Stability and [EliScholar](#), a digital platform for scholarly publishing provided by Yale University Library. For more information, please contact [ypfs@yale.edu](mailto:ypfs@yale.edu).

**Alejandro LaTorre/NY/FRS**

09/14/2008 03:48 PM

To

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

cc

Tanshel Pointer/NY/FRS@FRS

bcc

Subject

Pros and Cons on AIG lending

History:

This message has been forwarded.

Attached are the following documents:

1. A note describing the pros and cons of lending to AIG
2. A spreadsheet provided by AIG detailing the firms with the largest exposures to AIG (i.e. what firms stand to lose in the event of AIG)

default). The relevant column is "Total Exposure to AIG, Ranked". With the exception of the "lending" column, these figures are loss estimates. Derivative loss estimates are derived from current MTM provided by AIG.

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

If there are questions, let us know.

Regards,

Alex



Pros and Cons of Lending to AIG.doc Counterparty\_Exposure\_Report\_9142008.xls AIG Subsidiaries.ppt

## Pros and Cons of Lending to AIG

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

### Pros:

1. Collapse would be extremely complex to resolve given global nature of the firm; lending could contain market dislocations already happening due to Lehman.
2. Lending could provide "bridge finance" to implement strategic plan (e.g. longer-term asset sales, capital infusions, etc.);
  - Lending could bolster market confidence in strengthen perception of the plan with appropriate safeguards for the Federal Reserve.
  - AIG's fair value on ABS CDO aggressive (\$25B); greater than internal (\$9B) and rating agency loss estimates (S&P:\$8B).
  - Allows time to sell assets from the investment portfolio an orderly fashion (i.e., avoids liquidity spiral, negative feedback loops)
  - Firm could sell the ABS CDO risk, sell subsidiaries, mortgage portfolio, municipal securities, or raise more capital.
3. Collapse could lead to dislocation in sec lending/repo markets, CP markets and exacerbate risk aversion generally; lending could alleviate spillover effects on other firms involved in similar activities (e.g., GE Finance).
4. Lending might allow AIG to avoid bankruptcy; allows AIG to perform on balance sheet CDO swaps, which provide reg capital relief to European banks; failure would lead to \$18B increase in European bank capital requirements.
  - Swaps allow banks to hold 1.6% in regulatory capital as opposed to 8%.
  - Total notional exposure of \$290B; down from \$80B as deals wound down.
  - ABN Amro, Den Danske, Calyon, BNP, Deutsche most affected.
5. Lending could contain dislocations in CDS market; AIG is a commonly traded name and "tear ups" could leave dealer books significantly unbalanced.
6. Non-trivial exotic derivatives book would be difficult to unwind in an orderly fashion.

**Cons:**

1. Could diminish incentive to pursue private sector solutions and/or solutions proposed by insurance regulators, which, according to AIG and NYSID, appear to be moving forward.
  - Infusion of capital from private equity, which could happen today (\$15B)
  - Asset swap between P+C and Parent where Parent sells equity in Life insurance business in return for municipal securities, for use as collateral (\$20B)
  - Immediate sale of assets (\$13B; \$5B auto-related; \$8B annuity)
  - Berkshire Hathaway is investigating the provision of liquidity on Guaranteed Investment Contracts (\$5B)
2. Market must be highly confident that strategic plan will succeed; may not be well-received if turmoil ensues following Lehman bankruptcy.
3. Lending could precipitate failure and the exit strategy would not be clear.
  - Increases moral hazard as other insurance companies seek protection.
4. Lending to AIG could be perceived as inconsistent with treatment of Lehman.
5. Assets available from Ins. Co. subs may not be sufficient to cover potential liquidity shortfalls as many of the subs do not appear to be sources of strength.
  - Life Ins. Co. subs have significant unrealized losses on investments.
  - P&C could be source of strength; paid \$1.4B dividends, but amounts small relative to size of hole.
6. Forbearance could address increases in European bank capital requirements; makes lending unnecessary.
7. Without punitive terms, lending could reward poor risk management practices cited by rating agencies (e.g. S&P).

# Counterparty Exposure Report

All Figures mm USD

Bank	Security	Credit Facilities			FP Repo 9/8/2008	Lending	Lending	One-Day	Total Credit Exposure
	Lending 9/11/2008	Unfunded 7/10/2008	L/Cs 6/30/2008	Funded 6/30/2008		Total Prior Day	Total	Change	
Barclays	9,128	596	101	109	100	10,067	10,033	(34)	7,986.1
Deutsche Bank	7,616	596		42		8,274	8,253	(20)	26,170.6
Goldman Sachs	6,740	170				6,901	6,910	9	27,292.1
BNP Paribas	5,635	596	115	86	245	6,695	6,676	(18)	23,460.6
UBS	4,874	547			56	5,557	5,477	(80)	5,444.1
Bank of America	4,769	650	40			5,483	5,459	(24)	783.5
Citigroup	2,584	852		224	1,360	5,031	5,019	(12)	639.7
ING	4,786	43		168		5,025	4,996	(29)	-284.3
HSBC	3,342	664		174	425	4,579	4,605	26	1,873.4
Credit Suisse	3,719	625			210	4,573	4,554	(19)	693.5
Banco Santander		415	3,130	13		3,558	3,558	-	1,705.9
Lehman Brothers	2,768	410		139	230	3,573	3,546	(27)	
Merrill Lynch	2,479	557			15	3,072	3,051	(20)	8,339.1
Dresdner	2,755				175	2,942	2,930	(12)	
Morgan Stanley	2,193	348			148	2,695	2,688	(7)	8,058.3
Royal Bank of Scotland	990	657		254		1,899	1,901	2	1,154.3
ABN Amro	632					632	632	-	56,204.7
Sumitomo Mitsui		432	181	273	973	1,860	1,860	-	
MUFG		572	314	825		1,711	1,711	-	
Societe Generale	1,132	418		159		1,709	1,708	(1)	32,744.2
Helaba			1,350			1,350	1,350	-	
Intesa SanPaolo		74	808	208		1,090	1,090	-	-28.4
BayLB			1,050	30		1,080	1,080	-	2,787.7
Wachovia	444	596				1,031	1,040	9	793.4
JP Morgan	52	803	14	78		948	947	(0)	10,213.9
Bear Stearns	86					88	86	(2)	
Kreditbank					945	945	945	-	
Svenska Handelsbanken		119	507	225		851	851	-	
Mizuho		260	39	330	210	839	839	-	1,557.1
Daiwa Securities	27					27	27	(0)	
Standard Chartered		93	136	406		635	635	-	777.7
Unicredit Group			300	317		617	617	-	1,151.4
Calyon		174	327	99		600	600	-	28,887.1
Toronto Dominion		173			427	600	600	-	
LBBW			549			549	549	-	
Scotiabank		337	201	8		545	545	-	
RBC		313	206			519	519	-	
Danske				215	112	327	327	-	35,388.3
Citadel	296					298	296	(2)	
Bank of Montreal		97	50			147	147	-	
Jefferies	85					86	85	(1)	
Fortis Securities				71		71	71	-	1,547.6
Newedge	3					3	3	(0)	
BGI (Cash Equivalent Fund II)						-	-	-	
CIBC						-	-	-	
Coral Purchasing (DZ Bank)						-	-	-	2,162.3
First Clearing LLC						-	-	-	
Rabobank						-	-	-	4,384.2

FP CDS			Other Derivatives	S/T Investments		Credit	Credit	One-Day Total Payables	
ABS CDO exposure 9/8/2008	Other CDO exposure	Collateral 9/8/2008	mtm, \$mm	Unsecured 9/11/2008	Secured	Exposure Prior Day	Exposure	Change	
1,478	6,508	1,010	365.5		1,800	2,810	3,176	366	18,384.9
8,572	17,598	859	1.7	1,900	1,800	2,911	4,561	1,650	34,425.7
19,850	7,442	6,879	167.0			6,879	7,046	167	34,369.4
	23,470	139	121.1	300		2,209	560	(1,649)	30,267.0
4,302	1,142	951	16.1		2,000	2,951	2,967	16	10,937.3
792	(9)	207	182.5			207	389	182	6,425.4
	640		141.0			-	141	141	5,800.0
	(284)		21.6	900		900	922	22	4,733.1
165	1,708	173	60.8			173	234	61	6,539.2
	693		110.9			-	111	111	5,358.7
1,619	87	90	91.5	1,000		676	1,182	506	5,355.6
	-		299.7			-	300	300	3,846.2
7,522	817	2,204	27.8	100	800	3,304	3,132	(172)	11,418.4
	-		0.0	1,300		1,270	1,300	30	2,930.1
	8,058	106	103.7		2,000	706	2,210	1,504	10,850.2
1,182	(28)	435	258.8	2,600		3,335	3,294	(41)	3,314.3
	56,205		0.0		1,500	1,500	1,500	-	56,836.7
	-		32.9	600		300	633	333	1,892.4
	-		0.0	1,500		1,500	1,500	-	1,711.5
16,859	15,885	4,271	337.9	2,500		6,771	7,109	338	34,790.2
	-		0.0	500		500	500	-	1,350.0
	(28)		36.1			-	36	36	1,097.9
	2,788		57.2	400		400	457	57	3,924.9
807	(13)	75	0.1			75	75	0	1,833.1
	10,214	52	0.0		400	52	452	400	11,161.4
	-		0.0			-	-	-	85.8
	-		0.0			0	-	-	945.0
	-		24.7	1,050		1,050	1,075	25	875.8
	1,557		97.7			-	98	98	2,493.3
	-		0.0			-	-	-	27.0
	778		95.4			-	95	95	1,508.5
	1,151		443.7			-	444	444	2,211.8
4,453	24,434	1,231	0.0	1,600		2,828	2,831	3	29,486.7
	-		0.5			0	0	0	600.0
	-		0.0	300		165	300	135	549.0
	-		0.0			-	-	-	545.2
	-		7.7	1,128		1,900	1,136	(764)	526.4
	35,388		178.9			0	179	179	35,894.2
	-		0.0			-	-	-	295.8
	-	400	2.6	786		400	1,189	789	149.3
	-		0.0			-	-	-	84.9
	1,548		31.1			-	31	31	1,649.2
	-		-1.5			-	(2)	(2)	1.2
	-	6	0.0			6	6	-	0.0
590	(590)	357	0.0			617	357	(260)	0.0
1,943	219	290	0.0			290	290	-	2,162.3
	-		0.0			-	-	-	0.0
739	3,645	52	0.0	400		152	452	300	4,384.2

70,876  
25  
0.000352728

Counterparty Exposure Report, millions of dollars

Counterparty Exposure to AIG				Lending		Total Exposure to AIG		
Mark to Market Exposure on Derivatives								
ABS CDO*	Other Derivatives	Other CDO**	to AIG					
i	ii	iii	iv	I + ii+ iii + iv				
0.5	291.4	1,627.1	10,033.3	11,952.3	Barclays		1	
3.0	14.0	4,399.6	8,253.3	12,669.9	Deutsche Bank		2	
7.0	149.0	1,860.4	6,910.3	8,926.7	Goldman Sachs		3	
0.0	140.7	5,867.4	6,676.3	12,684.4	BNP Paribas		4	
1.5	16.0	285.4	5,477.1	5,780.0	UBS		5	
0.3	237.4	-2.2	5,459.4	5,694.9	Bank of America		6	
0.0	163.5	159.9	5,019.3	5,342.8	Citigroup		7	
0.0	22.0	-71.1	4,995.8	4,946.7	ING		8	
0.1	71.0	427.1	4,605.0	5,103.1	HSBC		9	
0.0	122.3	173.4	4,554.3	4,850.0	Credit Suisse		10	
0.6	69.8	21.7	3,558.2	3,650.3	Banco Santander		11	
0.0	315.0	0.0	3,546.5	3,861.5	Lehman Brothers		12	
2.7	18.5	204.2	3,051.5	3,276.8	Merrill Lynch		13	
0.0	0.0	0.0	2,930.1	2,930.1	Dresdner		14	
0.0	101.0	2,014.6	2,688.2	4,803.7	Morgan Stanley		15	
0.4	133.0	-7.0	1,901.1	2,027.5	Royal Bank of Scotland		16	
0.0	0.0	14,051.2	632.0	14,683.2	ABN Amro		17	
0.0	29.0	0.0	1,859.5	1,888.5	Sumitomo Mitsui		18	
0.0	0.5	0.0	1,711.5	1,712.0	MUFG		19	
5.9	348.1	3,971.2	1,708.0	6,033.3	Societe Generale		20	
0.0	17.0	0.0	1,350.0	1,367.0	Helaba		21	
0.0	41.0	-7.1	1,090.2	1,124.1	Intesa SanPaolo		22	
0.0	58.5	696.9	1,080.0	1,835.4	BayLB		23	
0.3	0.1	-3.3	1,039.6	1,036.6	Wachovia		24	
0.0	0.0	2,553.5	947.5	3,500.9	JP Morgan		25	
0.0	0.0	0.0	85.8	85.8	Bear Stearns		26	
0.0	0.0	0.0	945.0	945.0	Kreditbank		27	
0.0	29.0	0.0	851.1	880.1	Svenska Handelsbanken		28	
0.0	97.0	389.3	838.5	1,324.8	Mizuho		29	
0.0	0.0	0.0	27.0	27.0	Daiwa Securities		30	
0.0	83.0	194.4	635.4	912.8	Standard Chartered		31	
0.0	489.0	287.8	616.8	1,393.6	Unicredit Group		32	
1.6	0.0	6,108.5	599.6	6,709.6	Calyon		33	
0.0	1.0	0.0	599.5	600.5	Toronto Dominion		34	
0.0	0.0	0.0	549.0	549.0	LBBW		35	
0.0	0.0	0.0	545.2	545.2	Scotiabank		36	
0.0	1.3	0.0	518.7	520.0	RBC		37	
0.0	184.0	8,847.1	327.0	9,358.1	Danske		38	
0.0	0.0	0.0	295.8	295.8	Citadel		39	
0.0	0.7	0.0	146.7	147.4	Bank of Montreal		40	
0.0	0.0	0.0	84.9	84.9	Jefferies		41	
0.0	29.0	386.9	70.5	486.4	Fortis Securities		42	
0.0	-1.5	0.0	2.8	1.2	Newedge		43	
0.0	0.0	0.0	0.0	0.0	BGI (Cash Equivalent Fund II)		44	
0.2	4.0	-147.6	0.0	-143.4	CIBC		45	
0.7	0.0	54.8	0.0	55.5	Coral Purchasing (DZ Bank)		46	
0.0	0.0	0.0	0.0	0.0	First Clearing LLC		47	
0.3	0.0	911.3	0.0	911.6	Rabobank		48	

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

3,275.4



**Total Exposure to AIG, Ranked**

ABN Amro	14,683.2
BNP Paribas	12,684.4
Deutsche Bank	12,669.9
Barclays	11,952.3
Danske	9,358.1
Goldman Sachs	8,926.7
Calyon	6,709.6
Societe Generale	6,033.3
UBS	5,780.0
Bank of America	5,694.9
Citigroup	5,342.8
HSBC	5,103.1
ING	4,946.7
Credit Suisse	4,850.0
Morgan Stanley	4,803.7
Lehman Brothers	3,861.5
Banco Santander	3,650.3
JP Morgan	3,500.9
Merrill Lynch	3,276.8
Dresdner	2,930.1
Royal Bank of Scotland	2,027.5
Sumitomo Mitsui	1,888.5
BayLB	1,835.4
MUFG	1,712.0
Unicredit Group	1,393.6
Helaba	1,367.0
Mizuho	1,324.8
Intesa SanPaolo	1,124.1
Wachovia	1,036.6
Kreditbank	945.0
Standard Chartered	912.8
Rabobank	911.6
Svenska Handelsbanken	880.1
Toronto Dominion	600.5
LBBW	549.0
Scotiabank	545.2
RBC	520.0
Fortis Securities	486.4
Citadel	295.8
Bank of Montreal	147.4
Bear Stearns	85.8
Jefferies	84.9
Coral Purchasing (DZ Bank)	55.5
Daiwa Securities	27.0
Newedge	1.2
BGI (Cash Equivalent Fund II)	0.0
First Clearing LLC	0.0
CIBC	-143.4

**Other CDO exposure RANKED**  
(predominantly regulatory capital arbitrage,  
notional)

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





|

||

Cell: D22

Comment: Administrator:  
Includes ABN AMRO

Cell: F22

Comment: MAMADEO:  
Includes ABN Amro

Cell: D31

Comment: Administrator:  
Includes Bear Sterns

Restricted FR

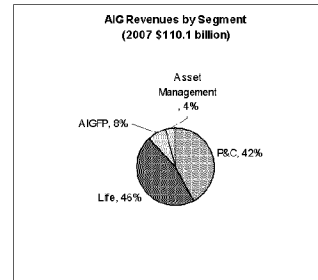
AIG Subsidiaries:  
Are they a Source of Strength?

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

Bank Supervision Group  
Sunday, September 13, 2008

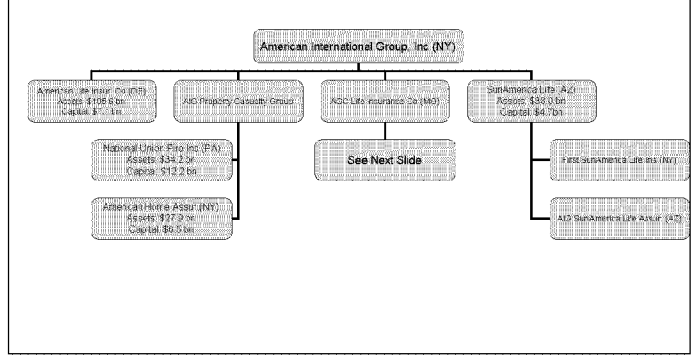
## Ability to support has weakened

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

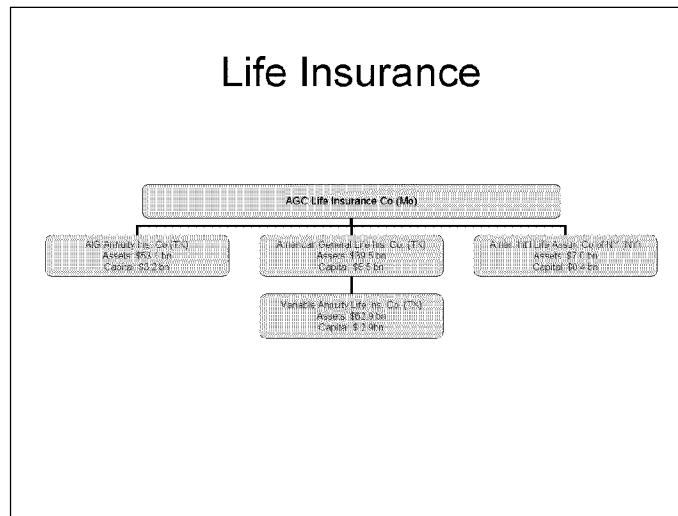




# Simplified Organizational Chart



# Life Insurance



**AIG - Summary of Financial and Rating Information of Major Subsidiaries**

Financial data as of 9/30/03

US Subsidiary	American Life	Variable Annuity	AIG Annuity	American General	SwanAmerica Life	National Union Fire	American Home	American
	Insurance Co.	Life	Insurance Co.	Life	Life	Insurance Co.	Insurance	International Life
Type of Business	LOI Insurance	LOI Insurance	LOI Insurance	LOI Insurance	LOI Insurance	IGC	PGC	LOI Insurance
Home State	DE	TX	TX	TX	AZ	PA	NY	NY
<b>Rating<sup>1</sup></b>								
Swan	A++ NR (01/03)	A++ NR (01/03)	A++ NR (01/03)	A++ NR (01/03)	A++ NR (01/03)	A++ NR (01/03)	A++ NR (01/03)	A++ NR (01/03)
MetLife	A-2 (02/02)	A-2 (01/02)	A-2 (01/02)	A-2 (01/02)	A-2 (01/02)	A-2 (01/02)	A-2 (01/02)	A-2 (01/02)
Met	A-2 NR (02/03)	A-2 NR (02/03)	A-2 NR (02/03)	A-2 NR (02/03)	A-2 NR (02/03)	A-2 NR (02/03)	A-2 NR (02/03)	A-2 NR (02/03)
<b>Balance Sheet Highlights</b>								
Total Assets	\$11,048	\$1,230	\$3,171	\$10,409	\$2,800	\$4,170	\$7,287	\$7,143
% of Capitalized Assets (\$10 trillion)	0.1%	0.3%	1.1%	3.9%	3.9%	2.7%	2.7%	0.7%
Fixed	\$10,953	\$1,237	\$1,199	\$7,023	\$1,670	\$1,371	\$1,514	\$1,548
Separate Accounts	\$3,122	\$164	\$373	\$2,851	\$2.5	na	na	\$1.20
Total Equity	\$1,113	\$211	\$1,214	\$1,513	\$1,341	\$1,195	\$1,227	\$440
Asset-Liability Reserve	\$361	\$411	\$1,202	\$1,282	\$1,260	na	na	\$1.11
Unrealized Gains (Loss)	(\$706)	\$1.1	\$23	(\$300)	(\$477)	\$75	na	\$2
Total Adjusted Capital (YE 2007)	na	\$1,573	\$4,878	\$4,193	\$1,579	\$1,173	\$7.84	\$462
Adjusted Capital (FDIC Ratio) (YE 2007)	na	\$560	\$666	\$1,260	\$266	\$230	\$1,002	\$72
RE: Ratio (YE 2007)	na	639%	732%	646%	749%	686%	407%	7.2%
<b>Income Statement Highlights</b>								
Net Income (incl. Capital Gains)	\$18	\$349	\$101	\$151	\$380	\$794	\$431	\$13
Revised Capital Gains (Loss)	(\$381)	(\$1,574)	(\$1,225)	(\$1,240)	(\$1,927)	\$304	\$1,125	(\$230)
<b>Dividends to Parents<sup>2</sup></b>								
2003 (First six months)	\$0	\$0	\$0	\$0	\$0	\$1,119	\$238	\$50
2007	\$1,023	\$700	\$400	\$251	\$700	\$1,110	\$615	\$100
2006	\$303	\$400	\$150	\$101	\$249	\$0	\$1	\$12
2005	156	\$400	\$0	\$441	\$480	\$91	\$23	\$50
2004	136	\$360	\$0	\$101	\$23	\$20*	\$43	\$0

<sup>1</sup> NR: Watch Negative; CS: Credit not Stable; CH: Outlook if negative

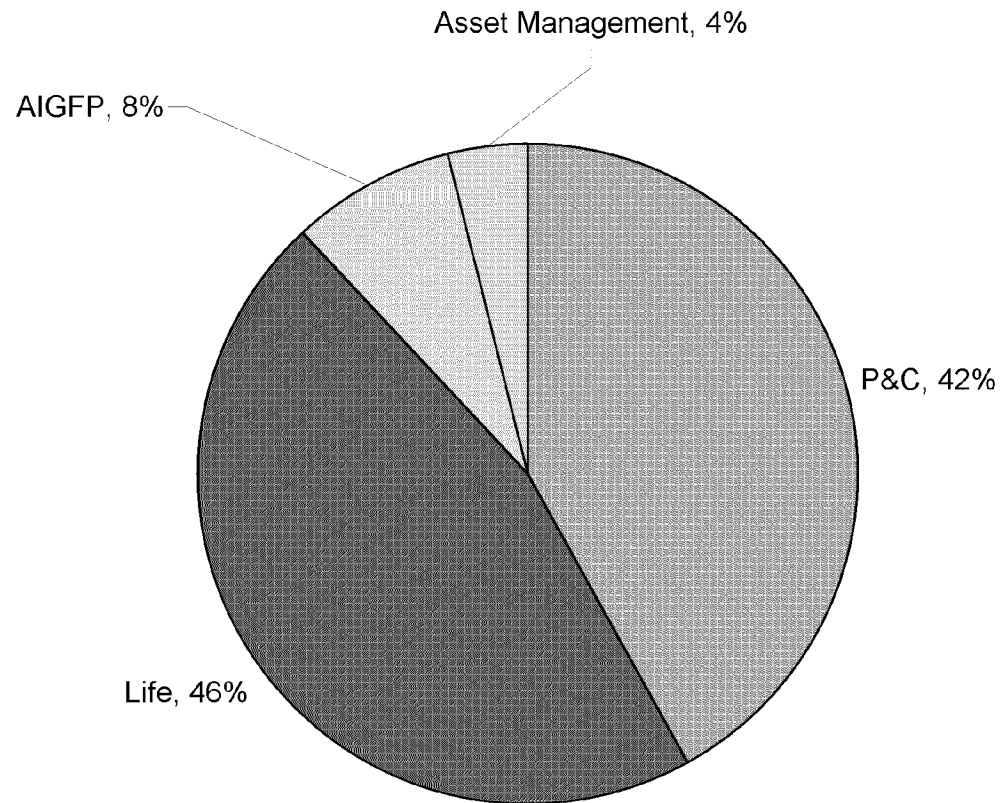
<sup>2</sup> In 2007, AIG parent collected \$4.4 billion in dividends in the first half of 2006; AIG parent collected \$1.4 billion in dividends (Source: 10K)

### What happens in a sale?

The loss rate at which equity becomes zero	
American Life Insurance Co.	8%
Variable Annuity Life	5%
AIG Annuities Insurance Co	8%
National Union	35%
SunAmerica Life	14%
American Home Assurance	22%
American General Life	17%
American International Life Assurance Co. of NY	16%

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

## AIG Revenues by Segment (2007 \$110.1 billion)



AIG Revenues	
P&C	42%
Life	46%
AIGFP	8%
Asset Management	4%

