AMERICAN INTERNATIONAL GROUP

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Background

AIG Inc. and its subsidiaries operate under several external capital regimes including state and sovereign regulators as well as rating agencies

Summary of select relevant standards

Insurance Capital Standard ("ICS")[1]

- Financial Stability Board tasked International Association of Insurance Supervisors (IAIS), which includes the Federal Reserve Board (FRB), to develop the ICS framework
- First round of "field testing" completed[2]
- As a G-SII, and an Internationally Active Insurance Group ("IAIG") AIG will need to comply with ICS
- ICS will likely be applicable to the P&C companies even if a Life spin-off were to occur[3]

Regulations for nonbank SIFIs

- SIFI designation entails FRB supervision
- FRB is still developing the capital framework

Standard & Poor's (S&P)

- Ratings use a combination of qualitative and quantitative information
- Capital adequacy (available vs. required) is a key input into ratings
- Required capital in the S&P model explicitly quantifies diversification benefits at multiple levels

Moody's & A.M. Best

- No consolidated capital model for AIG Inc.
- Quantitative models for insurance subs
- Qualitative assessment includes benefits for diversification

1. In the case of AIG, the sovereign lead regulator (NY Federal Reserve Bank) would have the authority to implement the ICS standards
2. ICS is expected to expected be adopted and implemented in 2020
3. IAIG includes insurers with premiums written in at least 3 jurisdictions and at least 10% of premiums outside of home jurisdictions; size threshold of $50 BN in assets or $10 BN in premiums. AIG P&C business would qualify under those criteria

Executive Summary

- AIG Inc.'s ability to return capital to shareholders is governed, among other factors, by two constraints:
  - Maintaining credit ratings
  - Meeting regulatory capital requirements
- Under both constraints, cross P&C / Life diversification benefits, which are only available with AIG remaining a multiline business, are quantified using established capital calculation methodologies. For instance:
  - S&P's consolidated capital model estimates a $5-10BN *reduction* in required capital for AIG as a whole compared to the sum of standalone required capital across AIG's Life and P&C entities[1]
  - Moody's and A.M. Best explicitly make reference to the value of diversification in determining overall credit ratings[2]
  - Under the emerging ICS standard, the results of the IAIS mandated "field test" indicate that AIG Inc. would require substantially less capital as a whole vs. the sum of standalone Life and P&C entities individually
- AIG will also need to comply with any capital constraints imposed by the FRB – however, no such rules exist currently
- Based on the aforementioned, the loss of diversification benefits if a Life/P&C split occurred would impose additional capital constraints and as a result would likely impact AIG's ability to return capital to shareholders

1. Source: Consolidated AIG Inc. S&P capital model as provided to Oliver Wyman by AIG
2. A.M. Best and Moody's do not deploy a quantitative capital model at the AIG Inc. consolidated level

Diversification benefits calculated by S&P model[1] (methodology)

	Diversification category	Description	Applicable to	
A	**Within P&C** **Within Life** **Within Investments[2]**	Reduction in risk due to the diversity of products & risk types within business lines (e.g., the offsetting effect of longevity and mortality risks)	✓ AIG Inc. ✓ AIG business units as standalone entities	C: *Subject To 50% S&P **Haircut***
B	**Across Life and P&C**	Reduction in overall risk profile due to exposure to two heterogeneous segments of the industry	✓ AIG Inc. × AIG business units as standalone entities	
D	**Asset-Liability Management (ALM) offset**	Reduced potential for losses due to the aggregate impact of interest rate movements on businesses with offsetting asset/liability duration profiles	✓ AIG Inc. • *Partially applicable to AIG business units based on distribution of parental assets between business units*	***Not** Subject To 50% S&P Haircut*

1. Source: Consolidated AIG Inc. S&P capital model as provided to Oliver Wyman by AIG
2. Some of these diversification benefits may be lost if calculated separately for AIG subsidiaries as standalone companies

Diversification benefits calculated by latest S&P consolidated model for AIG

	Risk factor / business line diversification type	Gross diversification benefits ($BN)[1] Status quo		Gross diversification benefits ($BN)[1] Post splitting of business		Net diversification benefits of maintaining status quo ($BN)
A	Within P&C	2.2		2.2		0
	Within Life	0.4		0.4		0
	Within Investments	2.5		2.5[4]		0
B	Life vs. P&C	4.1		-		4.1
	Business line diversification benefits	9.3[5]	−	5.2[5]	=	4.1
C	Business line diversification benefits post S&P haircut (50%)	4.7 *(=9.3*50%)*		2.6 *(=5.2*50%)*		2.1
D	ALM offset benefit	7.5		2.1[2]		5.4
	Total diversification benefits (S&P)	**12.2**	−	**4.7**	=	**7.5**

Calculated $7.5BN net diversification benefit is:

- Derived from S&P's capital model
- Inclusive of S&P's 50% haircut
- A net benefit - after accounting for diversification benefits that would remain post-split such as intra-BU diversification

Estimated range: $5-10BN[3]

1. All numbers based on S&P Insurance Capital Model results, targeting AA rating, as provided by AIG to Oliver Wyman (without independent verification of the model by Oliver Wyman)
2. Midpoint estimate based on equal distribution of parental assets to Life and P&C entities post-split
3. Minimum of range based on assumption that all of parental assets are assigned to Life entity. Conversely, the maximum of the range is based on the parental assets being assigned to the P&C entity
4. Some of these diversification benefits may be lost if calculated separately for AIG subsidiaries as standalone companies. Therefore, the diversification benefits of maintaining status quo may be understated
5. Numbers do not add-up in this view due to rounding

APPENDIX

Diversification benefits: other ratings agencies

*“A breakup of AIG and loss of SIFI status (assuming this were the effect) would be **credit negative** for the company, **removing the diversification benefit** of the multiline insurance operations…”*

– Moody’s

*The top-down analysis includes the exposure to risk generated by activities at the parent/holding company, […] as well as the **benefits of earnings diversification** that may come from being a member of a diversified organization.*

– A.M. Best

Source: Moody’s Nov 2, 2015 Credit Outlook, “Activist Investor Carl Icahn’s Push for AIG Breakup Is Credit Negative” ; A.M. Best’s Dec 18, 2015 Credit Rating Methodology

Global regulatory regimes explicitly incorporate diversification benefits
Insurance Capital Standard and Solvency II

Description

- ICS proposal recognizes diversification at multiple levels including **within** risk types including:
  – Life and Non-life insurance risk
  – Market risk (e.g., interest rate risk diversification)
- ICS also considers diversification **across** each of these risk types
- Certain diversification benefits that are applicable to AIG Inc. both within risk types and across risk types would only be partially applicable (or non-applicable) to AIG subsidiaries as standalone entities[1]
- Solvency II also explicitly recognizes diversification benefits at a Group level when assessing solvency capital requirements

ICS intra-life insurance risk correlation matrix

	Mortality	Longevity	Morbidity /disability	Lapse	Expe-nses
Mortality	100%	-25%	25%	0%	25%
Longevity	-25%	100%	0%	25%	25%
Morbidity/ disability	25%	0%	100%	0%	50%
Lapse	0%	25%	0%	100%	50%
Expenses	25%	25%	50%	50%	100%

ICS cross risk correlation matrix

Risk	Non-life	Catast-rophe	Life	Market	Credit
Non-life	100%	25%	**0%**	25%	25%
Catast-rophe	25%	100%	25%	25%	25%
Life	**0%**	25%	100%	25%	25%
Market	25%	25%	25%	100%	25%
Credit	25%	25%	25%	25%	100%

Source: AIG Inc. template for IAIS field testing as provided to Oliver Wyman by AIG; numbers may be subject to change with the finalization of ICS

1. For instance, the 0% correlation between Life and Non-life risks will result in substantial reduction of diversification benefits under a Life separation scenario