



## AIG/Chartis Insurance Update

January 25, 2011

On January 14, 2011 AIG announced that it completed the recapitalization plan that was announced on September 30, 2010. The plan required AIG to repay the approximately \$21 billion outstanding balance on the credit facility with the Federal Reserve Bank of New York (FRBNY). Once the FRBNY credit facility was repaid, all other forms of government support were converted to common shares which are currently held by the U.S. Treasury. These shares represent an ownership stake of approximately 92.1% and will be sold by the U.S. Treasury in a series of public offerings. No specific timeline for the first offering has been announced but the investment banks that will lead the share sale have been selected and investor road-shows are expected to begin within the next few weeks. The first offering could raise between \$15 billion to \$20 billion for the U.S. Treasury.

AIG's first round of government support came in September 2008 when it accepted its first line of credit from the FRBNY in order to address a liquidity crisis that arose from collateral calls on the credit default swap portfolio which resided in the holding company. As the financial markets continued to deteriorate, AIG received additional federal aid. In order to repay the U.S. government, AIG embarked on a plan to sell assets outright or spin off portions of some operations through public offerings. Some of the most significant assets that have been sold or spun off are:

- Transatlantic Holdings – a portion of the operation was sold to the public in June 2009 raising \$1.1 billion.
- American Life Insurance Co. (ALICO) – sold to MetLife in November 2010 for \$16.2 billion.
- AIA Group Ltd. – sold in an initial public offering in October 2010 yielding gross proceeds of approximately \$20.5 billion.

Another significant development for AIG was its return to the debt and credit markets at the end of 2010. Specifically, AIG successfully sold \$2 billion in notes on December 2, 2010. At the end of December, AIG announced that it entered into a \$3 billion credit facility and its insurance operating subsidiary, Chartis, separately entered into a \$1.3 billion letter of credit facility. Thirty-six banks participated among the two facilities.

### Conclusion

From an investor's perspective, the approaching end of the U.S. government's involvement both as AIG's creditor and investor is positive because many private investors feared that their interests may not have been aligned with those of the U.S. government. From a policyholder's perspective, the pending end of U.S. government involvement is equally positive because it will allow AIG to function once again as a "normal" company.

One of the most significant developments for policyholders in the last year was AIG's return to the debt markets and Chartis' entrance into a letter of credit facility. These are two activities that large, publicly traded companies consider part of normal activities but, since the first bailout in September 2008, banks were unwilling to provide lines of credit to AIG or its subsidiaries because the FRBNY facility was secured by company assets. The public debt market was also viewed as inaccessible for the same reason. The successful debt placement and new credit facilities are a vote of confidence in AIG from the credit markets.

Access to credit markets is vital for an insurance company because it allows an insurer to raise additional capital in the event that capital is depleted due to

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excessive losses. The entrance of Chartis into a letter of credit facility is a new development because all capital raising had previously been performed by AIG, the holding company. This development appears to be part of the contingency plan Chartis created in order to allow it to raise capital independent of the holding company. There are currently no plans for Chartis to be sold in a public offering, either in whole or in part, especially considering that it now constitutes the core business of AIG. Regardless, Chartis' independent ability to access credit markets is a good tool to have available in the event the holding company runs into a problem that does not involve Chartis.

The AIG of January 2011 is a very different company than the AIG of September 2008. A few predicted the company's demise and many more believed that the assets sales and government ownership would last well into this decade. There still remains some execution risk – it will take several offerings for the U.S. Treasury to dispose of its holdings of AIG stock and the timing and success of these offerings will be affected by financial market conditions and the performance of AIG's core operations, namely Chartis. We will continue to monitor the progress of stock offerings as well as the financials of AIG and Chartis but the repayment of the FRBNY credit facility and the return to the debt markets are good developments for both investors and policyholders.

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