
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

(Mark One)

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2004

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File Number 1-8787

American International Group, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

13-2592361
(I.R.S. Employer
Identification No.)

70 Pine Street, New York, New York
(Address of principal executive offices)

10270
(Zip Code)

Registrant's telephone number, including area code: (212) 770-7000

Former name, former address and former fiscal year, if changed since last report: None

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of March 31, 2004: 2,608,225,354.

CONSOLIDATED BALANCE SHEET*(in millions) (unaudited)*

| | March 31, 2004 | December 31, 2003 |
|---|-------------------|----------------------|
| Assets: | | |
| Investments, financial services assets and cash: | | |
| Fixed maturities: | | |
| Bonds available for sale, at market value (amortized cost: 2004 – \$301,249; 2003 – \$288,160) | \$ 319,182 | \$ 300,935 |
| Bonds held to maturity, at amortized cost (market value: 2004 – \$10,039; 2003 – \$8,173) | 9,823 | 8,037 |
| Bond trading securities, at market value (cost: 2004 – \$1,884; 2003 – \$252) | 1,966 | 282 |
| Equity securities: | | |
| Common stocks (cost: 2004 – \$11,482; 2003 – \$6,884) | 12,529 | 7,678 |
| Nonredeemable preferred stocks (cost: 2004 – \$1,831; 2003 – \$1,743) | 2,045 | 1,906 |
| Mortgage loans on real estate, net of allowance (2004 – \$101; 2003 – \$101) | 12,218 | 12,295 |
| Policy loans | 6,825 | 6,658 |
| Collateral and guaranteed loans, net of allowance (2004 – \$15; 2003 – \$15) | 2,283 | 2,296 |
| Financial services assets: | | |
| Flight equipment primarily under operating leases, net of accumulated depreciation (2004 – \$5,484; 2003 – \$5,458) | 30,807 | 30,343 |
| Securities available for sale, at market value (cost: 2004 – \$17,940; 2003 – \$15,732) | 17,930 | 15,714 |
| Trading securities, at market value | 4,877 | 3,300 |
| Spot commodities, at market value | 183 | 250 |
| Unrealized gain on interest rate and currency swaps, options and forward transactions | 21,452 | 21,599 |
| Trading assets | 1,886 | 2,548 |
| Securities purchased under agreements to resell, at contract value | 26,351 | 28,170 |
| Finance receivables, net of allowance (2004 – \$445; 2003 – \$453) | 18,494 | 17,609 |
| Securities lending collateral, at cost (approximates market value) | 40,695 | 30,195 |
| Other invested assets | 19,124 | 16,787 |
| Short-term investments, at cost (approximates market value) | 16,782 | 8,914 |
| Cash | 1,920 | 922 |
| Total investments, financial services assets and cash | 567,372 | 516,438 |
| Investment income due and accrued | 5,388 | 4,959 |
| Premiums and insurance balances receivable, net of allowance (2004 – \$257; 2003 – \$235) | 15,835 | 14,166 |
| Reinsurance assets | 28,167 | 27,962 |
| Deferred policy acquisition costs | 26,690 | 26,398 |
| Investments in partially owned companies | 1,497 | 1,428 |
| Real estate and other fixed assets, net of accumulated depreciation (2004 – \$4,363; 2003 – \$4,247) | 5,999 | 6,006 |
| Separate and variable accounts | 51,962 | 60,536 |
| Goodwill | 7,683 | 7,633 |
| Other assets | 13,561 | 12,820 |
| Total assets | \$ 724,154 | \$ 678,346 |

See Accompanying Notes to Financial Statements.

CONSOLIDATED BALANCE SHEET *(continued)**(in millions, except share amounts) (unaudited)*

| | March 31, 2004 | December 31, 2003 |
|---|-------------------|----------------------|
| Liabilities: | | |
| Reserve for losses and loss expenses | \$ 57,725 | \$ 56,118 |
| Reserve for unearned premiums | 22,004 | 20,762 |
| Future policy benefits for life and accident and health insurance contracts | 94,613 | 92,970 |
| Policyholders' contract deposits | 193,384 | 171,989 |
| Other policyholders' funds | 9,581 | 9,100 |
| Reserve for commissions, expenses and taxes | 5,009 | 4,487 |
| Insurance balances payable | 3,352 | 2,592 |
| Funds held by companies under reinsurance treaties | 4,977 | 4,664 |
| Income taxes payable: | | |
| Current | 2,778 | 1,977 |
| Deferred | 7,123 | 5,778 |
| Financial services liabilities: | | |
| Borrowings under obligations of guaranteed investment agreements | 15,414 | 15,337 |
| Securities sold under agreements to repurchase, at contract value | 14,956 | 14,810 |
| Trading liabilities | 4,817 | 6,153 |
| Securities and spot commodities sold but not yet purchased, at market value | 5,227 | 5,458 |
| Unrealized loss on interest rate and currency swaps, options and forward transactions | 15,731 | 15,268 |
| Trust deposits and deposits due to banks and other depositors | 3,516 | 3,491 |
| Commercial paper | 5,294 | 4,715 |
| Notes, bonds, loans and mortgages payable | 51,868 | 50,138 |
| Commercial paper | 2,519 | 1,223 |
| Notes, bonds, loans and mortgages payable | 5,813 | 5,865 |
| Preferred shareholders' equity in subsidiary companies subject to mandatory redemption | 1,682 | 1,682 |
| Separate and variable accounts | 51,962 | 60,536 |
| Minority interest | 3,792 | 3,311 |
| Securities lending payable | 40,695 | 30,195 |
| Other liabilities | 23,350 | 18,282 |
| Total liabilities | 647,182 | 606,901 |
| Preferred shareholders' equity in subsidiary companies | 193 | 192 |
| Shareholders' equity: | | |
| Common stock, \$2.50 par value; 5,000,000,000 shares authorized; shares issued 2004 – 2,751,327,476; 2003 – 2,751,327,476 | 6,878 | 6,878 |
| Additional paid-in capital | 567 | 568 |
| Retained earnings | 63,446 | 60,960 |
| Accumulated other comprehensive income (loss) | 7,315 | 4,244 |
| Treasury stock, at cost; 2004 – 143,102,122; 2003 – 142,880,430 shares of common stock | (1,427) | (1,397) |
| Total shareholders' equity | 76,779 | 71,253 |
| Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity | \$ 724,154 | \$ 678,346 |

See Accompanying Notes to Financial Statements.

CONSOLIDATED STATEMENT OF INCOME*(in millions, except per share amounts) (unaudited)*

| Three Months Ended March 31, | 2004 | 2003 |
|--|-----------------|-----------------|
| Revenues: | | |
| Premiums and other considerations | \$ 16,139 | \$ 13,072 |
| Net investment income | 4,720 | 3,966 |
| Realized capital gains (losses) | 83 | (632) |
| Other revenues | 2,695 | 2,521 |
| Total revenues | 23,637 | 18,927 |
| Benefits and expenses: | | |
| Incurred policy losses and benefits | 13,734 | 11,140 |
| Insurance acquisition and other operating expenses | 5,612 | 4,863 |
| Total benefits and expenses | 19,346 | 16,003 |
| Income before income taxes, minority interest and cumulative effect of an accounting change | 4,291 | 2,924 |
| Income taxes (benefits): | | |
| Current | 1,473 | 689 |
| Deferred | (117) | 187 |
| | 1,356 | 876 |
| Income before minority interest and cumulative effect of an accounting change | 2,935 | 2,048 |
| Minority interest | (98) | (94) |
| Income before cumulative effect of an accounting change | 2,837 | 1,954 |
| Cumulative effect of an accounting change, net of tax | (181) | – |
| Net income | 2,656 | 1,954 |
| Earnings per common share: | | |
| Basic | | |
| Income before cumulative effect of an accounting change | \$ 1.09 | \$ 0.75 |
| Cumulative effect of an accounting change, net of tax | (0.07) | – |
| Net income | 1.02 | 0.75 |
| Diluted | | |
| Income before cumulative effect of an accounting change | \$ 1.08 | \$ 0.74 |
| Cumulative effect of an accounting change, net of tax | (0.07) | – |
| Net income | 1.01 | 0.74 |
| Cash dividends per common share | \$ 0.065 | \$ 0.047 |
| Average shares outstanding: | | |
| Basic | 2,610 | 2,610 |
| Diluted | 2,633 | 2,628 |

See Accompanying Notes to Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

(in millions) (unaudited)

| Three Months Ended March 31, | 2004 | 2003 |
|--|----------|----------|
| Summary: | | |
| Net cash provided by operating activities | \$ 9,220 | \$ 8,831 |
| Net cash used in investing activities | (20,265) | (16,037) |
| Net cash provided by financing activities | 11,992 | 6,642 |
| Change in cumulative translation adjustments | 51 | 59 |
| Change in cash | 998 | (505) |
| Cash at beginning of period | 922 | 1,165 |
| Cash at end of period | \$ 1,920 | \$ 660 |
| Cash flows from operating activities: | | |
| Net income | \$ 2,656 | \$ 1,954 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Noncash revenues, expenses, gains and losses included in income: | | |
| Change in: | | |
| General and life insurance reserves | 6,528 | 6,017 |
| Premiums and insurance balances receivable and payable – net | (910) | (1,058) |
| Reinsurance assets | (205) | (1,387) |
| Deferred policy acquisition costs | (1,097) | (771) |
| Investment income due and accrued | (381) | (229) |
| Funds held under reinsurance treaties | 313 | 454 |
| Other policyholders' funds | 481 | 285 |
| Current and deferred income taxes – net | 684 | 361 |
| Reserve for commissions, expenses and taxes | 521 | (65) |
| Other assets and liabilities – net | 252 | 1,373 |
| Trading assets and liabilities – net | (674) | 409 |
| Trading securities, at market value | (1,577) | (2,027) |
| Spot commodities, at market value | 67 | (117) |
| Net unrealized (gain) loss on interest rate and currency swaps, options and forward transactions | 610 | 357 |
| Securities purchased under agreements to resell | 1,819 | 1,461 |
| Securities sold under agreements to repurchase | 146 | 2,402 |
| Securities and spot commodities sold but not yet purchased, at market value | (231) | (1,859) |
| Realized capital (gains) losses | (83) | 632 |
| Equity in income of partially owned companies and other invested assets | (362) | (44) |
| Amortization of premium and discount on securities | 74 | (2) |
| Depreciation expenses, principally flight equipment | 487 | 447 |
| Provision for finance receivable losses | 90 | 102 |
| Other – net | 12 | 136 |
| Total adjustments | 6,564 | 6,877 |
| Net cash provided by operating activities | \$ 9,220 | \$ 8,831 |

See Accompanying Notes to Financial Statements.

CONSOLIDATED STATEMENT OF CASH FLOWS (Continued)

(in millions) (unaudited)

| | Three Months Ended March 31, | 2004 | 2003 |
|---|------------------------------|--------------------|------|
| Cash flows from investing activities: | | | |
| Cost of bonds, at market sold | \$ 30,088 | \$ 32,933 | |
| Cost of bonds, at market matured or redeemed | 4,122 | 3,661 | |
| Cost of equity securities sold | 3,664 | 1,479 | |
| Realized capital gains (losses) | 83 | (632) | |
| Purchases of fixed maturities | (48,863) | (47,224) | |
| Purchases of equity securities | (4,797) | (1,483) | |
| Mortgage, policy and collateral loans granted | (555) | (516) | |
| Repayments of mortgage, policy and collateral loans | 539 | 418 | |
| Sales of securities available for sale | 620 | 915 | |
| Maturities of securities available for sale | 324 | 1,378 | |
| Purchases of securities available for sale | (3,100) | (3,245) | |
| Sales of flight equipment | 1,080 | - | |
| Purchases of flight equipment | (1,843) | (1,757) | |
| Net additions to real estate and other fixed assets | (182) | (244) | |
| Sales or distributions of other invested assets | 2,138 | 2,168 | |
| Investments in other invested assets | (3,948) | (5,031) | |
| Change in short-term investments | 1,346 | 857 | |
| Investments in partially owned companies | (6) | 285 | |
| Finance receivable originations and purchases | (5,579) | (2,460) | |
| Finance receivable principal payments received | 4,604 | 2,461 | |
| Net cash used in investing activities | \$ (20,265) | \$ (16,037) | |
| Cash flows from financing activities: | | | |
| Receipts from policyholders' contract deposits | \$ 13,088 | \$ 8,756 | |
| Withdrawals from policyholders' contract deposits | (4,507) | (4,023) | |
| Change in trust deposits and deposits due to banks and other depositors | 66 | (14) | |
| Change in commercial paper | 1,875 | 1,929 | |
| Proceeds from notes, bonds, loans and mortgages payable | 6,732 | 5,012 | |
| Repayments on notes, bonds, loans and mortgages payable | (5,118) | (4,640) | |
| Proceeds from guaranteed investment agreements | 1,505 | 1,393 | |
| Maturities of guaranteed investment agreements | (1,428) | (1,214) | |
| Redemption of subsidiary company preferred stock | - | (371) | |
| Proceeds from common stock issued | 40 | 12 | |
| Cash dividends to shareholders | (170) | (123) | |
| Acquisition of treasury stock | (92) | (76) | |
| Other - net | 1 | 1 | |
| Net cash provided by financing activities | \$ 11,992 | \$ 6,642 | |
| Supplementary information: | | | |
| Taxes paid | \$ 493 | \$ 413 | |
| Interest paid | \$ 1,032 | \$ 829 | |

See Accompanying Notes to Financial Statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME*(in millions) (unaudited)*

| Three Months Ended March 31, | 2004 | 2003 |
|--|-----------------|-----------------|
| Comprehensive income: | | |
| Net income | \$ 2,656 | \$ 1,954 |
| Other comprehensive income: | | |
| Unrealized appreciation of investments – net of reclassification adjustments | 4,461 | 1,939 |
| Deferred income tax expense on above changes | (1,532) | (688) |
| Foreign currency translation adjustments* | 106 | 38 |
| Applicable income tax (expense) benefit on above changes | 19 | (5) |
| Net derivative gains arising from cash flow hedging activities | 19 | 193 |
| Deferred income tax (expense) benefit on above changes | 25 | (55) |
| Retirement plan liabilities adjustment, net of tax | (27) | (40) |
| Other comprehensive income | 3,071 | 1,382 |
| Comprehensive income | \$ 5,727 | \$ 3,336 |

*Includes insignificant derivative gains and losses arising from hedges of net investments in foreign operations.
See Accompanying Notes to Financial Statements.

NOTES TO FINANCIAL STATEMENTS

1. Financial Statement Presentation

These statements are unaudited. In the opinion of management, all adjustments consisting only of normal recurring accruals have been made for a fair statement of the results presented herein. All material intercompany accounts and transactions have been eliminated. Certain accounts have been reclassified in the 2003 financial statements to conform to their 2004 presentation. For further information, refer to the Annual Report on Form 10-K of American International Group, Inc. (AIG) for the year ended December 31, 2003.

2. Segment Information

The following table summarizes the operations by major operating segment for the three months ended March 31, 2004 and 2003:

| Operating Segments (in millions) | 2004 | 2003 |
|---|------------------|------------------|
| Revenues: | | |
| General Insurance ^(a) | \$ 10,163 | \$ 7,898 |
| Life Insurance & Retirement Services ^(b) | 10,890 | 8,629 |
| Financial Services ^(c) | 1,786 | 1,693 |
| Asset Management ^(d) | 909 | 828 |
| Other | (111) | (121) |
| Consolidated | \$ 23,637 | \$ 18,927 |
| Operating income^(e): | | |
| General Insurance | \$ 1,567 | \$ 1,144 |
| Life Insurance & Retirement Services | 2,093 | 1,310 |
| Financial Services | 523 | 530 |
| Asset Management | 239 | 175 |
| Other ^(f) | (131) | (235) |
| Consolidated | \$ 4,291 | \$ 2,924 |

(a) Represents the sum of General Insurance net premiums earned, net investment income and realized capital gains (losses).

(b) Represents the sum of GAAP Life Insurance & Retirement Services premiums, net investment income and realized capital gains (losses).

(c) Represents Financial Services commissions, transactions and other fees.

(d) Represents Asset Management commissions and other fees and fee income and net investment income with respect to GICs.

(e) Represents income before income taxes, minority interest and cumulative effect of an accounting change.

(f) Represents other income (deductions) – net and other realized capital gains (losses).

The following table summarizes AIG's General Insurance operations by major operating unit for the three months ended March 31, 2004 and 2003:

| General Insurance (in millions) | 2004 | 2003 |
|------------------------------------|------------------|-----------------|
| Revenues: | | |
| Domestic Brokerage Group | \$ 5,692 | \$ 4,322 |
| Transatlantic | 972 | 758 |
| Personal Lines | 1,081 | 888 |
| Mortgage Guaranty | 162 | 178 |
| Foreign General | 2,249 | 1,762 |
| Reclassifications and Eliminations | 7 | (10) |
| Total General Insurance | \$ 10,163 | \$ 7,898 |
| Operating Income: | | |
| Domestic Brokerage Group | \$ 845 | \$ 552 |
| Transatlantic | 117 | 81 |
| Personal Lines | 89 | 79 |
| Mortgage Guaranty | 100 | 121 |
| Foreign General | 410 | 321 |
| Reclassifications and Eliminations | 6 | (10) |
| Total General Insurance | \$ 1,567 | \$ 1,144 |

The following table summarizes AIG's Life Insurance & Retirement Services operations by major operating unit for the three months ended March 31, 2004 and 2003:

Life Insurance & Retirement Services
(in millions)

| | 2004 | 2003 |
|---|------------------|-----------------|
| Revenues: | | |
| Foreign: | | |
| American International Assurance and Nan Shan Life | \$ 3,761 | \$ 3,070 |
| ALICO, AIG Star Life and AIG Edison Life | 3,064 | 1,906 |
| Other | 128 | 133 |
| Domestic: | | |
| AGLA and AG Life ^(a) | 2,259 | 2,194 |
| VALIC, AIG Annuity and AIG SunAmerica ^(b) | 1,678 | 1,326 |
| Total Life Insurance & Retirement Services | \$ 10,890 | \$ 8,629 |
| Operating Income: | | |
| Foreign: | | |
| American International Assurance and Nan Shan Life | \$ 471 | \$ 164 |
| ALICO, AIG Star Life and AIG Edison Life | 586 | 364 |
| Other | 29 | 43 |
| Domestic: | | |
| AGLA and AG Life ^(a) | 423 | 415 |
| VALIC, AIG Annuity and AIG SunAmerica ^(b) | 584 | 324 |
| Total Life Insurance & Retirement Services | \$ 2,093 | \$ 1,310 |

(a) Includes the life operations of AIG Life Companies.

(b) "AIG SunAmerica" represents the annuity operations of AIG SunAmerica Life Assurance Company, as well as those of First SunAmerica Life Insurance Company and SunAmerica Life Insurance Company.

2. Segment Information *(continued)*

The following table summarizes AIG's Financial Services operations by major operating unit for the three months ended March 31, 2004 and 2003:

| Financial Services <i>(in millions)</i> | 2004 | 2003 |
|--|-----------------|-----------------|
| Revenues: | | |
| Aircraft Finance | \$ 752 | \$ 722 |
| Capital Markets* | 333 | 325 |
| Consumer Finance | 693 | 639 |
| Other | 8 | 7 |
| Total Financial Services | \$ 1,786 | \$ 1,693 |
| Operating income: | | |
| Aircraft Finance | \$ 160 | \$ 174 |
| Capital Markets* | 183 | 211 |
| Consumer Finance | 183 | 148 |
| Other | (3) | (3) |
| Total Financial Services | \$ 523 | \$ 530 |

* Represents AIG Financial Products Corp. and AIG Trading Group Inc.

The following table summarizes AIG's Asset Management revenues and operating income for the three month periods ending March 31, 2004 and 2003:

| <i>(in millions)</i> | 2004 | 2003 |
|-------------------------------------|---------------|---------------|
| Revenues: | | |
| Guaranteed investment contracts | \$ 660 | \$ 625 |
| Institutional Asset Management* | 189 | 155 |
| Brokerage Services and Mutual Funds | 60 | 48 |
| Total | \$ 909 | \$ 828 |
| Operating income: | | |
| Guaranteed investment contracts | \$ 157 | \$ 119 |
| Institutional Asset Management* | 62 | 44 |
| Brokerage Services and Mutual Funds | 20 | 12 |
| Total | \$ 239 | \$ 175 |

* Includes AIG Global Investment Group and certain smaller asset management operations.

3. Earnings Per Share

Earnings per share of AIG are based on the weighted average number of common shares outstanding during the period.

Computation of Earnings Per Share:

| Three Months Ended March 31, <i>(in millions, except per share amounts)</i> | 2004 | 2003 |
|--|-----------------|-----------------|
| Numerator for basic earnings per share: | | |
| Income before cumulative effect of an accounting change | \$ 2,837 | \$ 1,954 |
| Cumulative effect of an accounting change, net of tax | (181) | - |
| Net income applicable to common stock | \$ 2,656 | \$ 1,954 |
| Denominator for basic earnings per share: | | |
| Average shares outstanding used in the computation of per share earnings: | | |
| Common stock issued | 2,752 | 2,752 |
| Common stock in treasury | (142) | (142) |
| Average shares outstanding – basic | 2,610 | 2,610 |
| Numerator for diluted earnings per share: | | |
| Income before cumulative effect of an accounting change | \$ 2,837 | \$ 1,954 |
| Cumulative effect of an accounting change, net of tax | (181) | - |
| Net income applicable to common stock | \$ 2,656 | \$ 1,954 |
| Denominator for diluted earnings per share: | | |

| | | |
|---|----------------|---------|
| Average shares outstanding | 2,610 | 2,610 |
| Incremental shares from potential common stock: | | |
| Average number of shares arising from outstanding employee stock plans (treasury stock method)* | 23 | 18 |
| <hr/> | | |
| Average shares outstanding – diluted | 2,633 | 2,628 |
| <hr/> | | |
| Earnings per share: | | |
| Basic: | | |
| Income before cumulative effect of an accounting change | \$ 1.09 | \$ 0.75 |
| Cumulative effect of an accounting change, net of tax | (0.07) | – |
| Net income | \$ 1.02 | \$ 0.75 |
| <hr/> | | |
| Diluted: | | |
| Income before cumulative effect of an accounting change | \$ 1.08 | \$ 0.74 |
| Cumulative effect of an accounting change, net of tax | (0.07) | – |
| Net income | \$ 1.01 | \$ 0.74 |

* Certain shares arising from employee stock plans were not included in the computation of diluted earnings per share where the exercise price of the options exceeded the average market price and would have been antidilutive. The number of shares excluded were 8 million and 25 million for the first three months of 2004 and 2003, respectively.

The quarterly dividend rate per common share, commencing with the dividend paid September 19, 2003 is \$0.065.

4. Starr International Company, Inc. Plan

Starr International Company, Inc. (SICO) provides a Deferred Compensation Profit Participation Plan (SICO Plan) to certain AIG employees. The SICO Plan came into being in 1975 when the voting shareholders and Board of Directors of SICO, a private holding company whose principal asset consists of AIG common stock, decided that a portion of the capital value of SICO should be used to provide an incentive plan for the current and succeeding managements of all American International companies, including AIG. Participation in the SICO Plan by any person, and the amount of such participation, is at the sole discretion of SICO's Board of Directors, and none of the costs of the various benefits provided under such plan is paid by or charged to AIG. The SICO Plan provides that shares currently owned by SICO may be set aside by SICO for the benefit of the participant and distributed upon retirement. The SICO Board of Directors may permit an early pay-out under certain circumstances. Prior to pay-out, the participant is not entitled to vote, dispose of or receive dividends with respect to such shares, and shares are subject to forfeiture under certain conditions, including but not limited to the participant's voluntary termination of employment with AIG prior to normal retirement age. In addition, SICO's Board of Directors may elect to pay a participant cash in lieu of shares of AIG common stock. If the expenses of the SICO Plan had been reflected by AIG, the pre-tax amounts accrued would have been \$13 million for the first three months of 2004 and \$32 million for the same period of 2003.

5. Commitments and Contingent Liabilities

In the normal course of business, various commitments and contingent liabilities are entered into by AIG and certain of its subsidiaries. In addition, AIG guarantees various obligations of certain subsidiaries.

(a) AIG and certain of its subsidiaries become parties to derivative financial instruments with market risk resulting from both dealer and end user activities and to reduce currency, interest rate, equity and commodity exposures. These instruments are carried at their estimated fair values in the consolidated balance sheet. The vast majority of AIG's derivative activity is transacted by Capital Markets.

(b) Securities sold, but not yet purchased and spot commodities sold but not yet purchased represent obligations of Capital Markets operations to deliver specified securities and spot commodities at their contracted prices, and thereby record a liability to repurchase the securities and spot commodities in the market at prevailing prices.

AIG has issued unconditional guarantees with respect to the prompt payment, when due, of all present and future payment obligations and liabilities of AIG Financial Products Corp. and its subsidiaries (AIGFP) and AIG Trading Group Inc. and its subsidiaries (AIGTG) arising from transactions entered into by AIGFP and AIGTG. Net revenues for the three months ended March 31, 2004 and 2003 from Capital Markets operations were \$333 million and \$325 million, respectively. The Capital Markets operating and reporting unit was established by integrating the operations of AIGFP and AIGTG.

(c) At March 31, 2004, International Lease Finance Corporation (ILFC) had committed to purchase 419 new and used aircraft deliverable from 2004 through 2010 at an estimated aggregate purchase price of \$24.5 billion and had options to purchase 11 new aircraft deliverable from 2004 through 2008 at an estimated aggregate purchase price of \$705 million. ILFC will be required to find customers for any aircraft acquired, and it must arrange financing for portions of the purchase price of such equipment.

(d) SAI Deferred Compensation Holdings, Inc., a wholly-owned subsidiary of AIG, has established a deferred compensation plan for registered representatives of certain AIG subsidiaries, pursuant to which participants have the opportunity to invest deferred commissions and fees on a notional basis. The value of the deferred compensation fluctuates with the value of the deferred investment alternatives chosen. AIG has provided a full and unconditional guarantee of the obligations of SAI Deferred Compensation Holdings, Inc. to pay the deferred compensation under the plan.

6. Employee Benefits

The following table presents the components of the net periodic benefit costs with respect to pensions and other benefits for the three months ended March 31, 2004 and 2003:

| (In millions) | Pensions | | | Postretirement | | |
|--|----------------|------------|-------|----------------|------------|-------|
| | Non-U.S. Plans | U.S. Plans | Total | Non-U.S. Plans | U.S. Plans | Total |
| 2004 | | | | | | |
| Components of net period benefit cost: | | | | | | |
| Service cost | \$ 15 | \$ 23 | \$ 38 | \$ — | \$ 1 | \$ 1 |
| Interest cost | 8 | 40 | 48 | — | 4 | 4 |
| Expected return on assets | (5) | (43) | (48) | — | — | — |
| Amortization of prior service cost | (1) | 1 | — | — | (1) | (1) |
| Amortization of transitional liability | 1 | — | 1 | — | — | — |
| Recognized actuarial loss | 5 | 14 | 19 | — | — | — |
| Net period benefit cost | \$ 23 | \$ 35 | \$ 58 | \$ — | \$ 4 | \$ 4 |

6. Employee Benefit *(continued)*

| <i>(In millions)</i> | Pensions | | | Postretirement | | |
|--|----------------|------------|-------|----------------|------------|-------|
| | Non-U.S. Plans | U.S. Plans | Total | Non-U.S. Plans | U.S. Plans | Total |
| 2003 | | | | | | |
| Components of net period benefit cost: | | | | | | |
| Service cost | \$ 13 | \$ 20 | \$ 33 | \$ – | \$ 1 | \$ 1 |
| Interest cost | 8 | 38 | 46 | – | 4 | 4 |
| Expected return on assets | (5) | (36) | (41) | – | – | – |
| Amortization of prior service cost | (1) | 1 | – | – | (1) | (1) |
| Amortization of transitional liability | 1 | – | 1 | – | – | – |
| Recognized actuarial loss | 5 | 16 | 21 | – | – | – |
| Other | (7) | – | (7) | – | – | – |
| Net period benefit cost | \$ 14 | \$ 39 | \$ 53 | \$ – | \$ 4 | \$ 4 |

7. Recent Accounting Standards

In January 2003, FASB issued FIN 46. FIN 46 changes the method of determining whether certain entities should be consolidated in AIG's consolidated financial statements. An entity is subject to FIN 46 and is called a Variable Interest Entity (VIE) if it has (i) equity that is insufficient to permit the entity to finance its activities without additional subordinated financial support from other parties, or (ii) equity investors that cannot make significant decisions about the entity's operations, or that do not absorb the expected losses or receive the expected returns of the entity. A VIE is consolidated by its primary beneficiary, which is the party that has a majority of the expected losses or a majority of the expected residual returns of the VIE, or both. All other entities not considered VIEs are evaluated for consolidation under other guidance. In December 2003, FASB issued a revision to Interpretation No. 46 (FIN 46R).

The provisions of FIN 46R are to be applied immediately to VIEs created after January 31, 2003, and to VIEs in which AIG obtains an interest after that date. For VIEs in which AIG holds a variable interest that it acquired before February 1, 2003, FIN 46R was applied as of December 31, 2003. For any VIEs that must be consolidated under FIN 46R that were created before February 1, 2003, the assets, liabilities and noncontrolling interest of the VIEs would be initially measured at their carrying amounts with any difference between the net amount added to the balance sheet and any previously recognized interest being recognized as the cumulative effect of an accounting change. In accordance with the transition provisions of FIN 46R, AIG recorded a gain of \$9 million (\$14 million before tax) reported as a cumulative effect of an accounting change for the fourth quarter of 2003 and added approximately \$4.7 billion of assets and liabilities in its consolidated balance sheet at December 31, 2003.

For further discussion on AIG's involvement with special purpose vehicles, see also Note 20 of Notes to Financial Statements in AIG's December 31, 2003 10-K.

In July 2003, the American Institute of Certified Public Accountants issued Statement of Position 03-1, "Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts" (SOP 03-1). This statement was effective as of January 1, 2004, and requires AIG to recognize a liability for guaranteed minimum death benefits and other living benefits related to its variable annuity and variable life contracts and modifies certain disclosures and financial statement presentations for these products. AIG reported for the first quarter of 2004 a one-time cumulative accounting charge upon adoption of \$181 million (\$242 million pretax) to reflect the liability as of January 1, 2004. For the first quarter of 2004, the ongoing earnings impact of AIG's adoption of SOP 03-1 was a \$3 million charge (\$5 million pretax).

As of January 1, 2004, approximately \$11 billion of assets and liabilities were reclassified representing most of the non-U.S. portion of AIG's separate and variable account assets and liabilities to several invested asset captions and the Policyholders' contract deposits liability caption, respectively. The \$11 billion of separate and variable account assets were reclassified as follows: \$4 billion to Short-term investments; \$4 billion to Equity securities – common stocks; \$2 billion to Fixed maturities – bond trading securities; and \$1 billion to various other asset captions.

Except as noted above, AIG issues variable contracts through its separate and variable accounts for which investment income and investment gains and losses accrue directly to, and investment risk is borne by, the contract holder (traditional variable annuities). AIG also issues variable annuity and life contracts through separate and variable accounts where AIG contractually guarantees to the contract holder (variable contracts with guarantees) either (a) total deposits made to the contract less any partial withdrawals plus a minimum return (and in minor instances, no minimum returns), or (b) the highest contract value on a specified anniversary date minus any withdrawals following the contract anniversary. These guarantees include benefits that are payable in the event of death, annuitization, or in minor instances, at specified dates during the accumulation period. Such benefits are referred to as guaranteed minimum death benefits (GMDB), guaranteed minimum income benefits (GMIB), and guaranteed minimum account value benefits (GMAV), respectively. For AIG, GMDB is by far the most widely offered benefit.

7. Recent Accounting Standards *(continued)*

The assets supporting the variable portion of both traditional variable annuities and variable contracts with guarantees are carried at fair value and reported as summary total separate and variable account assets with an equivalent summary total reported for liabilities. Amounts assessed against the contract holders for mortality, administrative, and other services are included in revenue and changes in liabilities for minimum guarantees are included in policyholder benefits in the Consolidated Statement of Income. Separate and variable account net investment income, net investment gains and losses, and the related liability changes are offset within the same line item in the Consolidated Statement of Income.

The vast majority of AIG's exposure on guarantees made to variable contract holders arises from GMDB. Details concerning AIG's GMDB exposures as of March 31, 2004 are as follows:

| <i>(in billions)</i> | Return of Net Deposits Plus a Minimum Return | Highest Specified Anniversary Account Value Minus Withdrawals Post Anniversary |
|---|---|---|
| Account Value | \$ 51 | \$ 13 |
| Net Amount at Risk | 9 | 2 |
| Average Attained Age of Contract Holders by Product | 50-70 years | 50-70 years |
| Range of Guaranteed Minimum Return Rates | 0-5% | 0% |

The following summarizes GMDB liabilities for guarantees on variable contracts reflected in the general account.

| <i>(in millions)</i> | |
|------------------------------|--------|
| Balance at January 1* | \$ 479 |
| Guaranteed benefits incurred | 30 |
| Guaranteed benefits paid | (21) |
| Balance at March 31, 2004 | 488 |

* Includes amounts from the one-time cumulative accounting charge resulting from the adoption of SOP 03-1.

The GMDB liability is determined each period end by estimating the expected value of death benefits in excess of the projected account balance and recognizing the excess ratably over the accumulation period based on total expected assessments. AIG regularly evaluates estimates used and adjusts the additional liability balance, with a related charge or credit to benefit expense, if actual experience or other evidence suggests that earlier assumptions should be revised.

The following assumptions and methodology were used to determine the domestic and foreign GMDB liability at March 31, 2004:

- Data used was up to 5,000 stochastically generated investment performance scenarios.
- Mean investment performance assumptions ranged from approximately 5 percent to 10 percent.
- Volatility assumptions ranged from 16 percent to 19 percent.
- Mortality was assumed at between 60 percent and 100 percent of various life and annuity mortality tables.
- For domestic contracts, lapse rates vary by contract type and duration and ranged from 1 percent to 30 percent. For Japan, lapse rates ranged from 0 percent to 8 percent.
- For domestic contracts, the discount rate was approximately 8 percent. For Japan, the discount rate ranged from 1.5 percent to 7 percent.

In addition to GMDB, AIG's contracts currently include to a lesser extent GMIB. The GMIB liability is determined each period end by estimating the expected value of the annuitization benefits in excess of the projected account balance at the date of annuitization and recognizing the excess ratably over the accumulation period based on total expected assessments. AIG regularly evaluates estimates used and adjusts the additional liability balance, with a related charge or credit to benefit expense, if actual experience or other evidence suggests that earlier assumptions should be revised. As of March 31, 2004, virtually all of AIG's GMIB exposure was transferred via reinsurance agreements.

AIG contracts currently include a minimal amount of GMAV. GMAVs are considered to be derivatives under Financial Accounting Standards Board Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities", and are recognized at fair value through earnings.

In December 2003, FASB issued Statement of Financial Accounting Standards No. 132 (Revised) "Employers' Disclosures About Pensions and Other Post Retirement Benefits" which revised disclosure requirements with respect to defined benefit plans. (See also Note 6.)

8. Information Provided in Connection with Outstanding Debt

The following condensed consolidating financial statements are provided in compliance with Regulation S-X of the Securities and Exchange Commission.

(a) American General Corporation (AGC) is a holding company and a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all outstanding debt of AGC.

American General Corporation:

Condensed Consolidating Balance Sheet

| March 31, 2004 (in millions) | American International Group, Inc. Guarantor | AGC Issuer | Other Subsidiaries | Eliminations | Consolidated AIG |
|---|---|------------------|-----------------------|---------------------|---------------------|
| Assets: | | | | | |
| Invested assets | \$ 1,759 | \$ – | \$ 573,667 | \$ (9,974) | \$ 565,452 |
| Cash | 4 | – | 1,916 | – | 1,920 |
| Carrying value of subsidiaries and partially owned companies, at equity | 77,117 | 22,350 | 7,536 | (105,506) | 1,497 |
| Other assets | 3,158 | 3,332 | 157,330 | (8,535) | 155,285 |
| Total assets | \$ 82,038 | \$ 25,682 | \$ 740,449 | \$ (124,015) | \$ 724,154 |
| Liabilities: | | | | | |
| Insurance liabilities | \$ 396 | \$ – | \$ 385,284 | \$ (12) | \$ 385,668 |
| Debt | 3,917 | 2,677 | 84,332 | (10,018) | 80,908 |
| Other liabilities | 946 | 3,819 | 184,393 | (8,552) | 180,606 |
| Total liabilities | 5,259 | 6,496 | 654,009 | (18,582) | 647,182 |
| Preferred shareholders' equity in subsidiary companies | – | – | 193 | – | 193 |
| Total shareholders' equity | 76,779 | 19,186 | 86,247 | (105,433) | 76,779 |
| Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity | \$ 82,038 | \$ 25,682 | \$ 740,449 | \$ (124,015) | \$ 724,154 |

| December 31, 2003 (in millions) | American International Group, Inc. Guarantor | AGC Issuer | Other Subsidiaries | Eliminations | Consolidated AIG |
|---|---|------------------|-----------------------|---------------------|---------------------|
| Assets: | | | | | |
| Invested assets | \$ 1,865 | \$ – | \$ 524,151 | \$ (10,500) | \$ 515,516 |
| Cash | 19 | – | 903 | – | 922 |
| Carrying value of subsidiaries and partially owned companies, at equity | 71,318 | 21,434 | 9,534 | (100,858) | 1,428 |
| Other assets | 2,885 | 2,602 | 155,836 | (843) | 160,480 |
| Total assets | \$ 76,087 | \$ 24,036 | \$ 690,424 | \$ (112,201) | \$ 678,346 |
| Liabilities: | | | | | |
| Insurance liabilities | \$ 358 | \$ – | \$ 357,691 | \$ (31) | \$ 358,018 |
| Debt | 3,932 | 2,824 | 80,485 | (9,963) | 77,278 |
| Other liabilities | 544 | 3,849 | 168,670 | (1,458) | 171,605 |
| Total liabilities | 4,834 | 6,673 | 606,846 | (11,452) | 606,901 |
| Preferred shareholders' equity in subsidiary companies | – | – | 192 | – | 192 |
| Total shareholders' equity | 71,253 | 17,363 | 83,386 | (100,749) | 71,253 |
| Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity | \$ 76,087 | \$ 24,036 | \$ 690,424 | \$ (112,201) | \$ 678,346 |

8. Information Provided in Connection with Outstanding Debt *(continued)*

American International Group, Inc. and Subsidiaries

Condensed Consolidating Statement of Income

| Three Months Ended March 31, 2004 <i>(in millions)</i> | American International Group, Inc. Guarantor | AGC Issuer | Other Subsidiaries | Eliminations | Consolidated AIG |
|---|---|---------------|-----------------------|-------------------|---------------------|
| Operating income | \$ 80 | \$ – | \$ 4,341 | \$ – | \$ 4,421 |
| Equity in undistributed net income of consolidated subsidiaries | 2,527 | 605 | – | (3,132) | – |
| Dividend income from consolidated subsidiaries | 325 | 24 | – | (349) | – |
| Other | (172) | (30) | 72 | – | (130) |
| Income taxes (benefits) | 104 | (11) | 1,263 | – | 1,356 |
| Minority interest | – | – | (98) | – | (98) |
| Cumulative effect of an accounting change, net of tax | – | – | (181) | – | (181) |
| Net income (loss) | \$ 2,656 | \$ 610 | \$ 2,871 | \$ (3,481) | \$ 2,656 |

| Three Months Ended March 31, 2003 <i>(in millions)</i> | American International Group, Inc. Guarantor | AGC Issuer | Other Subsidiaries | Eliminations | Consolidated AIG |
|---|---|---------------|-----------------------|-------------------|---------------------|
| Operating income | \$ 116 | \$ – | \$ 3,043 | \$ – | \$ 3,159 |
| Equity in undistributed net income of consolidated subsidiaries | 1,800 | 466 | – | (2,266) | – |
| Dividend income from consolidated subsidiaries | 209 | 5 | – | (214) | – |
| Other | (86) | – | (149) | – | (235) |
| Income taxes | 85 | 11 | 780 | – | 876 |
| Minority interest | – | – | (94) | – | (94) |
| Net income (loss) | \$ 1,954 | \$ 460 | \$ 2,020 | \$ (2,480) | \$ 1,954 |

Condensed Consolidating Statements of Cash Flow

| Three Months Ended March 31, 2004 <i>(in millions)</i> | American International Group, Inc. Guarantor | AGC Issuer | Other Subsidiaries | Consolidated AIG |
|---|---|---------------|-----------------------|---------------------|
| Net cash provided by operating activities | \$ 516 | \$ 468 | \$ 8,236 | \$ 9,220 |
| Cash flows from investing: | | | | |
| Invested assets disposed | 7 | – | 48,595 | 48,602 |
| Invested assets acquired | (176) | – | (68,509) | (68,685) |
| Other | (16) | (302) | 136 | (182) |
| Net cash used in investing activities | (185) | (302) | (19,778) | (20,265) |
| Cash flows from financing activities: | | | | |
| Change in debts | (24) | (147) | 3,737 | 3,566 |
| Other | (207) | (19) | 8,652 | 8,426 |
| Net cash provided by (used in) financing activities | (231) | (166) | 12,389 | 11,992 |
| Change in cumulative translation adjustments | (115) | – | 166 | 51 |
| Change in cash | (15) | – | 1,013 | 998 |
| Cash at beginning of period | 19 | – | 903 | 922 |
| Cash at end of period | \$ 4 | \$ – | \$ 1,916 | \$ 1,920 |

8. Information Provided in Connection with Outstanding Debt *(continued)*

American International Group, Inc. and Subsidiaries

| Three Months Ended March 31, 2003 <i>(in millions)</i> | American International Group, Inc. Guarantor | AGC Issuer | Other Subsidiaries | Consolidated AIG |
|---|---|---------------|-----------------------|---------------------|
| Net cash provided by operating activities | \$ 73 | \$ 473 | \$ 8,285 | \$ 8,831 |
| Cash flows from investing: | | | | |
| Invested assets disposed | 50 | – | 45,873 | 45,923 |
| Invested assets acquired | 4 | – | (61,720) | (61,716) |
| Other | (14) | (80) | (150) | (244) |
| Net cash provided by (used in) investing activities | 40 | (80) | (15,997) | (16,037) |
| Cash flows from financing activities: | | | | |
| Change in debts | 56 | (378) | 2,802 | 2,480 |
| Other | (182) | (14) | 4,358 | 4,162 |
| Net cash provided by (used in) financing activities | (126) | (392) | 7,160 | 6,642 |
| Change in cumulative translation adjustments | (1) | – | 60 | 59 |
| Change in cash | (14) | 1 | (492) | (505) |
| Cash at beginning of period | 18 | 1 | 1,146 | 1,165 |
| Cash at end of period | \$ 4 | \$ 2 | \$ 654 | \$ 660 |

(b) AIG Liquidity Corp. is a wholly owned subsidiary of AIG. AIG provides a full and unconditional guarantee of all obligations of AIG Liquidity Corp., which commenced operations in 2003.

AIG Liquidity Corp.:

Condensed Consolidating Balance Sheet

| March 31, 2004 <i>(in millions)</i> | American International Group, Inc. Guarantor | AIG Liquidity Corp. | Other Subsidiaries | Eliminations | Consolidated AIG |
|--|---|---------------------------|-----------------------|--------------|---------------------|
| Assets: | | | | | |
| Invested assets | \$ 1,759 | \$ * | \$ 573,667 | \$ (9,974) | \$ 565,452 |
| Cash | 4 | * | 1,916 | – | 1,920 |
| Carrying value of subsidiaries and partially owned companies, at equity | 77,117 | – | 29,886 | (105,506) | 1,497 |
| Other assets | 3,158 | * | 160,662 | (8,535) | 155,285 |
| Total assets | \$ 82,038 | \$ * | \$ 766,131 | \$ (124,015) | \$ 724,154 |
| Liabilities: | | | | | |
| Insurance liabilities | \$ 396 | \$ – | \$ 385,284 | \$ (12) | \$ 385,668 |
| Debt | 3,917 | * | 87,009 | (10,018) | 80,908 |
| Other liabilities | 946 | * | 188,212 | (8,552) | 180,606 |
| Total liabilities | 5,259 | * | 660,505 | (18,582) | 647,182 |
| Preferred shareholders' equity in subsidiary companies | – | – | 193 | – | 193 |
| Total shareholders' equity | 76,779 | * | 105,433 | (105,433) | 76,779 |
| Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity | \$ 82,038 | \$ * | \$ 766,131 | \$ (124,015) | \$ 724,154 |

* Amounts significantly less than \$1 million.



8. Information Provided in Connection with Outstanding Debt *(continued)*

American International Group, Inc. and Subsidiaries

| December 31, 2003 <i>(in millions)</i> | American International Group, Inc. Guarantor | AIG Liquidity Corp. | Other Subsidiaries | Eliminations | Consolidated AIG |
|---|---|---------------------------|-----------------------|---------------------|---------------------|
| Assets: | | | | | |
| Invested assets | \$ 1,865 | \$ * | \$ 524,151 | \$ (10,500) | \$ 515,516 |
| Cash | 19 | * | 903 | — | 922 |
| Carrying value of subsidiaries and partially owned companies, at equity | 71,318 | — | 30,968 | (100,858) | 1,428 |
| Other assets | 2,885 | * | 158,438 | (843) | 160,480 |
| Total assets | \$ 76,087 | \$ * | \$ 714,460 | \$ (112,201) | \$ 678,346 |
| Liabilities: | | | | | |
| Insurance liabilities | \$ 358 | \$ — | \$ 357,691 | \$ (31) | \$ 358,018 |
| Debt | 3,932 | * | 83,309 | (9,963) | 77,278 |
| Other liabilities | 544 | * | 172,519 | (1,458) | 171,605 |
| Total liabilities | 4,834 | * | 613,519 | (11,452) | 606,901 |
| Preferred shareholders' equity in subsidiary companies | — | — | 192 | — | 192 |
| Total shareholders' equity | 71,253 | * | 100,749 | (100,749) | 71,253 |
| Total liabilities, preferred shareholders' equity in subsidiary companies and shareholders' equity | \$ 76,087 | \$ * | \$ 714,460 | \$ (112,201) | \$ 678,346 |

* Amounts significantly less than \$1 million.

Condensed Consolidating Statement of Income

| Three Months Ended March 31, 2004 <i>(in millions)</i> | American International Group, Inc. Guarantor | AIG Liquidity Corp. | Other Subsidiaries | Eliminations | Consolidated AIG |
|--|---|---------------------------|-----------------------|-------------------|---------------------|
| Operating income | \$ 80 | \$ * | \$ 4,341 | \$ — | \$ 4,421 |
| Equity in undistributed net income of consolidated subsidiaries | 2,527 | — | 605 | (3,132) | — |
| Dividend income from consolidated subsidiaries | 325 | — | 24 | (349) | — |
| Other | (172) | — | 42 | — | (130) |
| Income taxes | 104 | * | 1,252 | — | 1,356 |
| Minority interest | — | — | (98) | — | (98) |
| Cumulative effect of an accounting change, net of tax | — | — | (181) | — | (181) |
| Net income (loss) | \$ 2,656 | \$ * | \$ 3,481 | \$ (3,481) | \$ 2,656 |

* Amounts significantly less than \$1 million.

Condensed Consolidating Statements of Cash Flow

| Three Months Ended March 31, 2004 <i>(in millions)</i> | American International Group, Inc. Guarantor | AIG Liquidity Corp. | Other Subsidiaries | Consolidated AIG |
|---|---|---------------------------|-----------------------|---------------------|
| Net cash provided by operating activities | \$ 516 | \$ * | \$ 8,704 | \$ 9,220 |
| Cash flows from investing: | | | | |
| Invested assets disposed | 7 | — | 48,595 | 48,602 |
| Invested assets acquired | (176) | — | (68,509) | (68,685) |
| Other | (16) | * | (166) | (182) |
| Net cash used in investing activities | (185) | * | (20,080) | (20,265) |
| Cash flows from financing activities: | | | | |

| | | | | |
|--|-------|------|----------|----------|
| Change in debts | (24) | – | 3,590 | 3,566 |
| Other | (207) | * | 8,633 | 8,426 |
| Net cash provided by financing activities | (231) | * | 12,223 | 11,992 |
| Change in cumulative translation adjustments | (115) | – | 166 | 51 |
| Change in cash | (15) | * | 1,013 | 998 |
| Cash at beginning of period | 19 | – | 903 | 922 |
| Cash at end of period | \$ 4 | \$ * | \$ 1,916 | \$ 1,920 |

*Amounts significantly less than \$1 million.

MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

“Management’s Discussion and Analysis of Financial Condition and Results of Operations” is designed to provide the reader a narrative with respect to AIG’s operations, financial condition and liquidity and certain other significant matters.

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Cautionary Statement Regarding Forward-Looking Information

This Quarterly Report and other publicly available documents may include, and AIG’s officers and representatives may from time to time make, statements which may constitute “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. These statements are not historical facts but instead represent only AIG’s belief regarding future events, many of which, by their nature, are inherently uncertain and outside of AIG’s control. These statements may address, among other things, AIG’s strategy for growth, product development, regulatory approvals, market position, financial results and reserves. It is possible that AIG’s actual results and financial condition may differ, possibly materially, from the anticipated results and financial condition indicated in these forward-looking statements. Important factors that could cause AIG’s actual results to differ, possibly materially, from those in the specific forward-looking statements are discussed throughout this Management’s Discussion and Analysis of Financial Condition and Results of Operations. AIG is not under any obligation to (and expressly disclaims any such obligations to) update or alter any forward-looking statement, whether written or oral, that may be made from time to time, whether as a result of new information, future events or otherwise.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG presents its operations in the way it believes will be most meaningful. Statutory underwriting profit (loss) and combined ratios are presented in accordance with accounting principles prescribed by insurance regulatory authorities because these are standard measures of performance used in the insurance industry and thus allow more meaningful comparisons with AIG's insurance competitors. AIG has also incorporated into this discussion a number of parenthetical cross-references to additional information included throughout this Form 10-Q to assist readers seeking related information on a particular subject.

Introduction and Executive Summary

AIG's operations in 2004 are conducted by its subsidiaries principally through four operating segments: General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management. Through these segments, AIG provided insurance and investment products and services to both businesses and individuals in over 130 countries and jurisdictions. This geographic product and service diversification is one of AIG's major strengths and sets it apart from its competitors. Although regional economic downturns or political upheaval could negatively impact parts of AIG's operations, AIG believes that this diversification makes it unlikely that regional difficulties would have a material impact on its operating results, financial condition or liquidity.

Beginning this quarter, AIG is reporting Retirement Services results in the same segment as Life Insurance, reflecting the convergence of protective and retirement products and AIG's current management of these operations.

For further detail, see the discussions with respect to the results of the Life Insurance & Retirement Services and Asset Management in the respective Operational Review discussion herein.

AIG's subsidiaries serve commercial, institutional and individual customers through an extensive property-casualty and life insurance and retirement services network. In the United States, AIG companies are the largest underwriter of commercial and industrial insurance and one of the largest life insurance and retirement services operations as well. AIG's Financial Services businesses include commercial aircraft leasing, capital markets and consumer finance, both in the United States and abroad. AIG also provides asset management services and sells guaranteed investment contracts (GICs) to institutions and individuals.

AIG's 2004 performance reflects implementation of various long-term strategies and defined goals in its various operating segments.

A primary goal of AIG in managing its General Insurance operations is to achieve an underwriting profit – maintaining a combined loss and expense ratio under 100. To achieve this end, AIG is disciplined in its risk selection and premiums must be adequate to cover the risk accepted. AIG believes in strict control of expenses, so it historically has one of the lowest expense ratios in the industry.

AIG patiently builds relationships in markets around the world where it sees long-term growth opportunities. For example, AIG's ability to expand its Chinese operations more quickly and extensively than its competitors is the result of relationships developed over nearly 30 years. AIG's more recent extensions of operations into India, Brazil, Russia and other emerging markets follow the same pattern. Moreover, AIG believes in investing in the economies and infrastructures of these countries and growing with them. When AIG companies enter a new jurisdiction, they typically offer both basic protection and savings products. As the economies evolve, AIG's products evolve with them, to more complex and investment-oriented models.

Another central focus of AIG operations in current years is the development and expansion of new distribution channels. In late 2003, AIG entered into an agreement with PICC Property and Casualty Company, Ltd. (PICC) which will enable AIG companies to market accident and health products throughout China through PICC's agency system. Other examples of new distribution channels used both domestically and overseas include banks, affinity groups and e-commerce.

Growth for AIG may be generated both internally and through acquisitions which both fulfill strategic goals and offer adequate return on investment. In recent years, the acquisitions of AIG Star Life Insurance Co., Ltd (AIG Star Life) and AIG Edison Life Insurance Company (AIG Edison) have broadened AIG's penetration of the Japanese market, the second largest for life insurance in the world. These acquisitions broadened AIG's distribution channels and will result in operating efficiencies as they are integrated into AIG's previously existing companies operating in Japan.

AIG provides leadership on issues of concern to the global and local economies as well as the insurance and financial services industries. In recent years, tort reform and legislation to deal with the asbestos problem have been key issues, while in prior years trade legislation and superfund have been issues of concern.

The following table summarizes AIG's revenues, income before income taxes, minority interest and cumulative effect of an accounting change and net income for the three months ended March 31, 2004 and 2003:

| <i>(in millions)</i> | 2004 | 2003 |
|---|-----------|-----------|
| Total revenues | \$ 23,637 | \$ 18,927 |
| Income before income taxes, minority interest and cumulative effect of an accounting change | 4,291 | 2,924 |
| Net income | \$ 2,656 | \$ 1,954 |

Consolidated Results

The 24.9 percent growth in revenues in the first three months of 2004 was primarily attributable to the growth in net premiums earned from global General Insurance operations as well as growth in both General Insurance and Life Insurance & Retirement Services net investment income and GAAP Life Insurance & Retirement Services premiums. An additional factor in 2004 was the significant improvement resulting in aggregate net realized capital gains in the first three months of 2004 compared to net realized capital losses in the same period of 2003.

The realized capital gains in 2004 reflect an improved economy, stronger corporate balance sheets and a significantly lower level of impairment loss provisions. The realized capital losses in 2003 reflect primarily impairment loss provisions. Upon the ultimate disposition of these holdings, a portion of these losses may be recovered depending on future market conditions.

AIG's income before income taxes, minority interest and cumulative effect of an accounting change increased 46.8 percent in the first three months of 2004 when compared to the same period of 2003. General Insurance and Life Insurance & Retirement Services operating income gains and together with the improvement in realized capital gains (losses) were the primary factors for the increase over 2003 in both pretax income and net income.

The following table summarizes the operations of each principal segment for the three months ended March 31, 2004 and 2003. (See also Note 2 of Notes to Financial Statements.)

| <i>(in millions)</i> | 2004 | 2003 |
|---|------------------|------------------|
| Revenues: | | |
| General Insurance ^(a) | \$ 10,163 | \$ 7,898 |
| Life Insurance & Retirement Services ^(b) | 10,890 | 8,629 |
| Financial Services ^(c) | 1,786 | 1,693 |
| Asset Management ^(d) | 909 | 828 |
| Other | (111) | (121) |
| Total | \$ 23,637 | \$ 18,927 |
| Operating Income^(e): | | |
| General Insurance | \$ 1,567 | \$ 1,144 |
| Life Insurance & Retirement Services | 2,093 | 1,310 |
| Financial Services | 523 | 530 |
| Asset Management | 239 | 175 |
| Other ^(f) | (131) | (235) |
| Total | \$ 4,291 | \$ 2,924 |

(a) Represents the sum of General Insurance net premiums earned, net investment income and realized capital gains (losses).

(b) Represents the sum of GAAP Life Insurance & Retirement Services premiums, net investment income and realized capital gains (losses).

(c) Represents Financial Services commissions, transactions and other fees.

(d) Represents Asset Management commissions and other fees and fee income and net investment income with respect to GICs.

(e) Represents income before income taxes, minority interest and cumulative effect of an accounting change.

(f) Represents other income (deductions) – net and other realized capital gains (losses).

General Insurance

AIG's General Insurance operations provide property and casualty products and services throughout the world. The increase in General Insurance operating income in the first three months of 2004 compared to the same period of 2003 was primarily attributable to strong growth in operating income with respect to Domestic Brokerage Group's and Foreign General's operations. In addition, General Insurance operations had realized capital gains in 2004 compared to realized capital losses in 2003.

Life Insurance & Retirement Services

AIG's Life Insurance & Retirement Services operations provide traditional, financial and investment products throughout the world. AIG's foreign operations provide over 50 percent of AIG's Life Insurance & Retirement Services operating income.

Life Insurance & Retirement Services operating income increased by 59.7 percent in the first three months of 2004 compared to the same period of 2003. This increase resulted from growth in each of AIG's principal Life Insurance & Retirement Services businesses, and realized capital gains in 2004 rather than the realized capital losses realized in 2003.

Financial Services

AIG's Financial Services subsidiaries engage in diversified financial products and services including aircraft leasing, capital market transactions and consumer and insurance premium financing.

Financial Services operating income decreased in the first three months of 2004 compared to the same period of 2003, reflecting ILFC's securitization of approximately \$2 billion in aircraft in the third quarter of 2003 and first quarter of 2004, and the transaction-oriented nature of Capital Markets operations.

Asset Management

AIG's Asset Management operations provide asset management services and sell GICs. These products and services are offered to individuals, and institutions both domestically and overseas.

Asset Management operating income increased 37.1 percent in the first three months of 2004 when compared to the same period of 2003 as a result of the upturn in worldwide financial markets and a strong global product portfolio.

Capital Resources

At March 31, 2004, AIG had total shareholders' equity of \$76.78 billion and total borrowings of \$80.91 billion. At that date, \$72.09 billion of such borrowings were either not guaranteed by AIG or were matched borrowings under obligations of guaranteed investment agreements (GIAs) or matched notes and bonds payable.

During the period from January 1, 2004 through March 31, 2004, AIG repurchased in the open market 1,313,300 shares of its common stock.

Liquidity

At March 31, 2004, consolidated invested assets were \$576.60 billion including \$18.70 billion in cash and short-term investments. Consolidated net cash provided from operating activities in the first three months of 2004 amounted to \$9.22 billion. AIG believes that its liquid assets, cash provided by operations and access to the capital markets will enable it to meet any foreseeable cash requirements.

Outlook

Overall, premium rates in the General Insurance business have continued to be strong both domestically and in key international markets, although the rates of increase have moderated in most lines and begun to fall in certain classes. AIG also continues to be able to modify and limit its contractual obligations by adding appropriate exclusions and policy restrictions. AIG expects total premiums to increase in 2004 resulting in positive growth in cash flow for investments. Thus, General Insurance net investment income is expected to rise in future quarters even in the current low interest rate environment.

In October 2003, AIG entered into an agreement with PICC that will enable AIG to market its accident and health products through PICC's 4,300 branch offices throughout the country. PICC has over 70 percent of the non-life market in China and AIG expects substantial opportunity for growth through this new distribution channel.

In the Life Insurance & Retirement Services segment, AIG expects overall continued growth through expansion in China, where AIG was the first foreign insurance organization to have wholly owned Life Insurance & Retirement Services operations in eight major cities. AIG expects continued growth in India, Korea and Vietnam as well as in the more established Japan market where retirement services operations have developed quickly.

AIG Edison Life was acquired in August of 2003. AIG Edison Life adds to the current agency force in Japan, and provides alternative distribution channels including banks, financial advisers, and corporate and government employee relationships. AIG Edison Life's integration into AIG's existing Japanese operations will provide future operating efficiencies.

Domestically, AIG expects continued strong operating growth in 2004 as distribution channels are expanded and new products are introduced.

In the airline industry, changes in market conditions are not immediately apparent in operating results. Therefore, AIG believes that improvements in that market commencing in 2003 will be gradually reflected in ILFC's results in 2004. In the Capital Markets operations, the integration of AIG Trading Group Inc. and its subsidiaries (AIGTG) into the operations of AIG Financial Products Corp. and its subsidiaries (AIGFP) created operating efficiencies that will continue to be realized and product synergies that should enhance 2004 results, although quarter to quarter variations are to be expected in this transaction-oriented business. AIG also expects increased contributions to Financial Services revenues and income from its consumer finance operations (Consumer Finance) both domestically, as a result of the improving economy, and overseas, as expansion of credit card operations continues and economic conditions improve.

AIG expects its Asset Management operations to continue to benefit from the recovery in the equity markets and global economy.

AIG has many promising growth initiatives underway around the world in its insurance and other operations. Cooperative agreements such as those in Russia and with the PICC are expected to expand distribution networks for AIG's products and investment opportunities and provide models for future growth.

Critical Accounting Estimates

AIG considers its most critical accounting estimates those with respect to reserves for losses and loss expenses, future policy benefits for life and accident and health contracts, deferred policy acquisition costs, and fair value determinations for certain Capital Markets assets and liabilities. These accounting estimates require the use of assumptions about matters, some of which are highly uncertain at the time of estimation. To the extent actual experience differs from the assumptions used, AIG's results of operations would be directly impacted.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG's critical accounting estimates are discussed in detail. The major categories for which assumptions are developed and used to establish each critical accounting estimate are highlighted below.

Reserves for Losses and Loss Expenses (General Insurance):

- *Loss trend factors:* used to establish expected loss ratios for subsequent accident years based on the projected loss ratio with respect to prior accident years.
- *Expected loss ratios for the latest accident year:* for example, accident year 2003 for the year end 2003 loss reserve analysis. For low frequency, high severity classes such as Excess Casualty and Directors and Officers' Liability, expected loss ratios generally are utilized for at least the three most recent accident years.
- *Loss development factors:* used to project the reported losses for each accident year to an ultimate amount.

Future Policy Benefits for Life and Accident and Health Contracts (Life Insurance & Retirement Services):

- *Interest rates:* which vary by territory, year of issuance and products.
- *Mortality, morbidity and surrender rates:* based upon actual experience by geographical region modified to allow for variation in policy form.

Deferred Policy Acquisition Costs (General Insurance):

- Recoverability based upon the current profitability of the underlying insurance contracts.

Life Insurance & Retirement Services:

- *Estimated gross profits:* to be realized over the estimated duration of the contracts (nontraditional life). Estimated gross profits include investment income and gains and losses on investments less required interest, actual mortality and other expenses.

Fair Value Determinations of Certain Assets and Liabilities (Financial Services – Capital Markets):

- *Valuation models:* utilizing factors, such as market liquidity and current interest, foreign exchange and volatility rates.
- AIG attempts to secure reliable and independent current market price data, such as published exchange rates from external subscription services such as Bloomberg or Reuters or third party broker quotes for use in this model. When such prices are not available, AIG uses an internal methodology, which includes interpolation or extrapolation from verifiable prices from trades occurring on dates nearest to the dates of the transactions.

Operating Review

General Insurance Operations

AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of property and casualty insurance both domestically and abroad.

Domestic general insurance operations are comprised of the Domestic Brokerage Group (DBG), which includes The Hartford Steam Boiler Inspection and Insurance Company (HSB); Transatlantic Holdings, Inc. (Transatlantic); Personal Lines, including 21st Century Insurance Group (21st Century); and United Guaranty Corporation (Mortgage Guaranty).

DBG is AIG's primary domestic general division. DBG writes substantially all classes of business insurance accepting such business mainly from insurance brokers. This provides DBG the opportunity to select specialized markets and retain underwriting control. Any licensed broker is able to submit business to DBG without the traditional agent-company contractual relationship, but such broker usually has no authority to commit DBG to accept a risk.

Transatlantic offers, through its reinsurance company subsidiaries, reinsurance capacity, both domestically and overseas, on a treaty and facultative basis for a full range of property and casualty products.

Personal Lines engages in the mass marketing of personal lines insurance, primarily private passenger auto and personal umbrella coverages, as well as providing comprehensive insurance coverage to high net-worth households through its Private Client Group.

Mortgage Guaranty provides guaranty insurance to mortgage providers primarily with respect to conventional first mortgage loans on single family dwellings and condominiums. During 2003, Mortgage Guaranty commenced providing guaranty insurance to providers of student loans.

AIG's Foreign General insurance group accepts risks primarily underwritten through AIU, a marketing unit consisting of wholly owned agencies and insurance entities. The Foreign General insurance group also includes business written by AIG's foreign-based insurance subsidiaries for their

own accounts. (See also Note 2 of Notes to Financial Statements.)

As previously noted, AIG believes it should present and discuss its financial information in a manner most meaningful to its investors. Accordingly, in its General Insurance business, AIG uses certain non-GAAP measures, where AIG has determined these measurements to be useful and meaningful.

A critical discipline of a successful general insurance business is the objective to produce operating income from underwriting exclusive of investment related income. When underwriting is not profitable, premiums are inadequate to pay for insured losses and underwriting related expenses. In these situations, the addition of general insurance related investment income and realized capital gains may, however, enable a general insurance business to produce operating income. If underwriting losses persist over extended periods, an insurance company will likely not continue to exist as a going concern. For these reasons, AIG views underwriting profit to be critical in the overall evaluation of performance. Although in and of itself not a GAAP measurement, AIG believes this measurement is a useful and meaningful disclosure. (See also the discussion under "Liquidity" herein.)

General Insurance operating income is comprised of underwriting profit, net investment income and realized capital gains and losses. These components, as well as net premiums written, net premiums earned and statutory ratios for the three month periods ending March 31, 2004 and 2003 were as follows:

| <i>(in millions, except ratios)</i> | 2004 | 2003 |
|---|------------------|-----------------|
| Net premiums written: | | |
| Domestic General | | |
| DBG | \$ 5,550 | \$ 4,540 |
| Transatlantic | 907 | 768 |
| Personal Lines | 1,113 | 884 |
| Mortgage Guaranty | 154 | 121 |
| Foreign General | 2,489 | 1,930 |
| Total | \$ 10,213 | \$ 8,243 |
| Net premiums earned: | | |
| Domestic General | | |
| DBG | \$ 5,101 | \$ 4,013 |
| Transatlantic | 893 | 692 |
| Personal Lines | 1,035 | 846 |
| Mortgage Guaranty | 134 | 124 |
| Foreign General | 2,076 | 1,612 |
| Total | \$ 9,239 | \$ 7,287 |
| Underwriting profit: | | |
| Domestic General | | |
| DBG | \$ 255 | \$ 243 |
| Transatlantic | 37 | 15 |
| Personal Lines | 43 | 37 |
| Mortgage Guaranty | 71 | 67 |
| Foreign General | 237 | 171 |
| Total | \$ 643 | \$ 533 |
| Net investment income: | | |
| Domestic General | | |
| DBG | \$ 546 | \$ 466 |
| Transatlantic | 72 | 65 |
| Personal Lines | 43 | 32 |
| Mortgage Guaranty | 29 | 43 |
| Intercompany adjustments and eliminations – net | – | 2 |
| Foreign General | 167 | 176 |
| Total | \$ 857 | \$ 784 |
| Realized capital gains (losses) | 67 | (173) |
| Operating income | \$ 1,567 | \$ 1,144 |
| Domestic General: | | |
| Loss Ratio | 77.20 | 77.20 |
| Expense Ratio | 17.59 | 17.00 |
| Combined Ratio | 94.79 | 94.20 |
| Foreign General: | | |
| Loss Ratio | 61.65 | 63.42 |
| Expense Ratio | 25.50 | 25.48 |
| Combined ratio | 87.15 | 88.90 |
| Consolidated: | | |
| Loss Ratio | 73.70 | 74.15 |
| Expense Ratio | 19.52 | 18.98 |
| Combined Ratio | 93.22 | 93.13 |

Net premiums written are initially deferred and earned based upon the terms of the underlying policies. The net unearned premium reserve constitutes deferred revenues which are generally earned ratably over the policy period. Thus, the net unearned premium reserve is not fully recognized as net premiums earned until the end of the policy period.

Commencing in the latter part of 1999 and continuing into and through the current quarter, the commercial property-casualty market place has experienced premium rate increases, although the rate of increase has moderated in the current quarter. DBG also maintains adequate pricing while giving careful attention to underwriting selection, policy terms and conditions, deductibles and attachment points. Overall, DBG's net premiums written increased in the first three months of 2004 over 2003. AIG believes that these premium rate increases will continue in 2004 particularly with respect to long tail lines of business where the insurer's stability is critical to the insured. Based on historical patterns, AIG believes that overall growth in net premiums written will slow as competition for premiums increases in certain lines of business.

Personal Lines' net premiums written in the first three months of 2004 includes \$107 million from the domestic insurance operations of GE that were acquired in August of 2003. The increase in net premiums written apart from this acquisition resulted from increased marketing efforts as well as rate increases in several states. The increase in underwrit-

ing profits in the first three months of 2004 when compared to the same period of 2003 resulted from premium rate increases and growth in net premiums written and earned. Underwriting profits are expected to continue to increase through 2004 as a result of continued marketing efforts, loss cost stabilization and the full year impact of the acquisition.

Mortgage Guaranty's net premiums written increased 26.8 percent in the first three months of 2004 when compared to the same period of 2003. Premium growth and improved persistency were offset by a slight increase in Mortgage Guaranty's delinquency ratio, which is still below the industry average.

Foreign General insurance net premiums written growth was due to premium rate increases as well as flight to quality. Every major region of the worldwide network contributed to this performance. Although AIG expects growth in Foreign General commercial lines rates to moderate in 2004, Foreign General has commenced various initiatives with respect to target markets, products, and distribution to offset this moderation of rate increases.

In comparing the foreign currency exchange rates used to translate the results of AIG's Foreign General operations during the first three months of 2004 to those foreign currency exchange rates used to translate AIG's Foreign General results during the same period of 2003, the U.S. dollar weakened slightly in value in relation to most major foreign currencies in which AIG transacts business. Accordingly, when foreign net premiums written were translated into U.S. dollars for the purposes of the preparation of the consolidated financial statements, total General Insurance net premiums written were approximately 3.4 percentage points more than they would have been if translated utilizing those foreign currency exchange rates which prevailed during the same period of 2003.

AIG, along with most General Insurance entities, uses the loss ratio, the expense ratio and the combined ratio as measures of performance. The loss ratio is the sum of losses and loss expenses incurred divided by net premiums earned. The expense ratio is statutory underwriting expenses divided by net premiums written. The combined ratio is the sum of the loss ratio and the expense ratio. These ratios are relative measurements that describe for every \$100 of net premiums earned or written, the cost of losses and statutory expenses, respectively. The combined ratio presents the total cost per \$100 of premium production. A combined ratio below 100 demonstrates underwriting profit; a combined ratio above 100 demonstrates underwriting loss.

Underwriting profit is measured in two ways: statutory underwriting profit and Generally Accepted Accounting Principles (GAAP) underwriting profit.

Statutory underwriting profit is arrived at by reducing net premiums earned by net losses and loss expenses incurred and net expenses incurred. Statutory accounting generally requires immediate expense recognition and ignores the matching of revenues and expenses as required by GAAP. That is, for statutory purposes, expenses are recognized immediately, not over the same period that the revenues are earned.

A basic premise of GAAP accounting is the recognition of expenses at the same time revenues are earned, the accounting principle of matching. Therefore, to convert underwriting results to a GAAP basis, acquisition expenses are deferred (deferred policy acquisition costs (DAC)) and amortized over the period the related net premiums written are earned. Accordingly, the statutory underwriting profit has been adjusted as a result of acquisition expenses being deferred as required by GAAP. DAC is reviewed for recoverability and such review requires management judgment. (See also Critical Accounting Estimates herein.)

The underwriting environment varies from country to country, as does the degree of litigation activity. Regulation, product type and competition have a direct impact on pricing and consequently on profitability as reflected in underwriting profit and statutory general insurance ratios.

The effects of catastrophes incurred in the first three months of 2004 and 2003 were insignificant. The impact of losses caused by catastrophes can fluctuate widely from year to year, making comparisons of recurring type business more difficult. With respect to catastrophe losses, AIG believes that it has taken appropriate steps, such as careful exposure selection and obtaining reinsurance coverage, to reduce the impact of the magnitude of possible future losses. The occurrence of one or more catastrophic events of unanticipated frequency or severity, such as a terrorist attack, earthquake or hurricane, that causes insured losses, however, could have a material adverse effect on AIG's results of operations, liquidity or financial condition.

General Insurance net investment income grew in the first three months of 2004 when compared to the same period of 2003. AIG is benefiting from the strong cash flow of the past two years, strengthening credit and equity markets and increased income related to partnership investments. (See also the discussion under "Liquidity" herein.)

Realized capital gains and losses resulted from the ongoing investment management of the General Insurance portfolios within the overall objectives of the General Insurance operations. The realized capital gains in the first three months of 2004 reflect an improved economy, stronger corporate balance sheets and a significantly lower level of impairments. The realized capital losses in the first three months of 2003 reflect primarily impairment loss provisions for both equity and fixed income holdings. (See the discussion on "Valuation of Invested Assets" herein.)

The increase in General Insurance operating income in the first three months of 2004 was primarily attributable to strong profitable growth in DBG's and Foreign General's operations and the improvement in realized capital gains (losses) relative to the same period of 2003.

The contribution of General Insurance operating income to AIG's consolidated income before income taxes, minority interest and cumulative effect of an accounting change was 36.5 percent in the first three months of 2004 compared to 39.1 percent in the same period of 2003.

Reinsurance

AIG is a major purchaser of reinsurance for its General Insurance operations. AIG is cognizant of the need to exercise good judgment in the selection and approval of both domestic and foreign companies participating in its reinsurance programs. AIG insures risks globally and its reinsurance programs must be coordinated in order to provide AIG the level of reinsurance protection that AIG desires. AIG purchases reinsurance to mitigate its catastrophic exposure. However, one or more catastrophe losses could negatively impact AIG's reinsurers and result in an inability of AIG to collect reinsurance recoverables. AIG's reinsurance department evaluates catastrophic events and assesses the probability of occurrence and magnitude of catastrophic events through the use of state of the art industry recognized program models among other techniques. AIG supplements these models through continually monitoring the risk exposure of AIG's worldwide general insurance operations and adjusting such models accordingly. While reinsurance arrangements do not relieve AIG from its direct obligations to its insureds, an efficient and effective reinsurance program substantially limits AIG's probable losses.

AIG's general reinsurance assets amounted to \$26.95 billion at March 31, 2004 and resulted from AIG's reinsurance arrangements. Thus, a credit exposure existed at March 31, 2004 with respect to reinsurance recoverable to the extent that any reinsurer may not be able to reimburse AIG under the terms of these reinsurance arrangements. AIG manages its credit risk in its reinsurance relationships by transacting with reinsurers that it considers financially sound, and when necessary AIG holds substantial collateral in the form of funds, securities and/or irrevocable letters of credit. This collateral can be drawn on for amounts that remain unpaid beyond specified time periods on an individual reinsurer basis. At December 31, 2003, approximately 47 percent of the general reinsurance assets were from unauthorized reinsurers. In order to obtain statutory recognition, the majority of these balances were collateralized. The remaining 53 percent of the general reinsurance assets were from authorized reinsurers. The terms authorized and unauthorized pertain to regulatory categories, not creditworthiness. Approximately 90 percent of the balances with respect to authorized reinsurers are from reinsurers rated A (excellent) or better, as rated by A.M. Best, or A (strong) or better, as rated by Standard & Poor's. Through March 31, 2004, these distribution percentages have not changed significantly. This rating is a measure of financial strength.

AIG maintains an allowance for estimated unrecoverable reinsurance and has been largely successful in its previous recovery efforts. AIG's allowance for estimated unrecoverable reinsurance approximated \$140 million as of March 31, 2004. At that date, AIG had no significant reinsurance recoverables from any individual reinsurer which is financially troubled (e.g., liquidated, insolvent, in receivership or otherwise subject to formal or informal regulatory restriction).

AIG's Reinsurance Security Department conducts ongoing detailed assessments of the reinsurance markets and current and potential reinsurers, both foreign and domestic. Such assessments include, but are not limited to, identifying if a reinsurer is appropriately licensed, and has sufficient financial capacity, and the local economic environment in which a foreign reinsurer operates. This department also reviews the nature of the risks ceded and the need for collateral. For example, in AIG's treaty reinsurance contracts, AIG includes credit triggers that require a reinsurer to post collateral when a referenced event occurs. Such credit triggers include, but are not limited to, insurer financial strength rating downgrades, policyholder surplus declines at or below a certain predetermined level or a certain predetermined level of a reinsurance recoverable being reached. In addition, AIG's Credit Risk Committee reviews the credit limits for and concentrations with any one reinsurer.

AIG enters into certain intercompany reinsurance transactions for its general and life operations. AIG enters these transactions as a sound and prudent business practice in order to maintain underwriting control and spread insurance risk among various legal entities. These reinsurance agreements have been approved by the appropriate regulatory authorities. All material intercompany transactions have been eliminated in consolidation.

At March 31, 2004, the consolidated general reinsurance assets of \$26.95 billion include reinsurance recoverables for paid losses and loss expenses of \$4.09 billion and \$18.97 billion with respect to the ceded reserve for losses and loss expenses, including ceded losses incurred but not reported (IBNR) (ceded reserves). The ceded reserves represent the accumulation of estimates of ultimate ceded losses including provisions for ceded IBNR and loss expenses. The methods used to determine such estimates and to establish the resulting ceded reserves are continually reviewed and updated. Any adjustments thereto are reflected in income currently. It is AIG's belief that the ceded reserves at March 31, 2004 were representative of the ultimate losses recoverable. In the future, as the ceded reserves continue to develop to ultimate

amounts, the ultimate loss recoverable may be greater or less than the reserves currently ceded.

Reserve for Losses and Loss Expenses

The table below classifies as of March 31, 2004 the components of the General Insurance reserve for losses and loss expenses (loss reserves) with respect to major lines of business on a statutory basis*:

| <i>(in millions)</i> | |
|-----------------------------|------------------|
| Other Liability Occurrence | \$ 14,413 |
| Other Liability Claims Made | 10,434 |
| Workers Compensation | 7,785 |
| Auto Liability | 5,320 |
| International | 3,070 |
| Property | 3,287 |
| Reinsurance | 2,191 |
| Medical Malpractice | 2,071 |
| Aircraft | 1,629 |
| Products Liability | 1,336 |
| Accident and Health | 1,098 |
| Fidelity/ Surety | 951 |
| Other | 4,140 |
| Total | \$ 57,725 |

* Presented pursuant to statutory reporting requirements as prescribed by the National Association of Insurance Commissioners.

These loss reserves represent the accumulation of estimates of ultimate losses, including IBNR and loss expenses.

At March 31, 2004, General Insurance net loss reserves increased \$2.11 billion from the prior year end to \$38.75 billion. In the first quarter of 2004, net adverse reported loss development for the prior accident years was estimated to be approximately \$200 million. The net loss reserves represent loss reserves reduced by reinsurance recoverables, net of an allowance for unrecoverable reinsurance. The methods used to determine such estimates and to establish the resulting reserves are continually reviewed and updated. Any adjustments resulting therefrom are reflected in operating income currently. It is management's belief that the General Insurance net loss reserves are adequate to cover all General Insurance net losses and loss expenses as at March 31, 2004. While AIG annually reviews the adequacy of established loss reserves, there can be no assurance that AIG's ultimate loss reserves will not adversely develop and materially exceed AIG's loss reserves as of March 31, 2004. In the future, if the general insurance net loss reserves develop deficiently, such deficiency would have an adverse impact on future results of operations.

In a very broad sense, the General Insurance loss reserves can be categorized into two distinct groups, one group being long tail casualty lines of business. Such lines include excess and umbrella liability, directors and officers' liability, professional liability, medical malpractice, general liability, products' liability, and related classes. The other group is short tail lines of business consisting principally of property lines, personal lines and certain classes of casualty lines.

For operations writing short tail coverages, such as property coverages, the process of recording quarterly loss reserve changes is geared toward maintaining an appropriate reserve level for the outstanding exposure, rather than determining an expected loss ratio for current business. For example, the IBNR reserve required for a class of property business might be expected to approximate 20 percent of the latest year's earned premiums, and this level of reserve would be maintained regardless of the loss ratio emerging in the current quarter. The 20 percent factor is adjusted to reflect changes in rate levels, loss reporting patterns, known exposures to large unreported losses, or other factors affecting the particular class of business.

Estimation of ultimate net losses and loss expenses (net losses) for long tail casualty lines of business is a complex process and depends on a number of factors, including the line and volume of the business involved. Experience in the more recent accident years of long tail casualty lines shows limited statistical credibility in reported net losses. That is, a relatively low proportion of net losses would be reported claims and expenses and an even smaller proportion would be net losses paid. A relatively high proportion of net losses would therefore be IBNR.

AIG's carried net long tail loss reserves are tested using loss trend factors that AIG considers most appropriate for each class of business. A variety of actuarial methods and assumptions are normally employed to estimate net losses for long tail casualty lines. These methods ordinarily involve the use of loss trend factors intended to reflect the estimated annual growth in loss costs from one accident year to the next. For the majority of long tail casualty lines, net loss trend factors approximated six percent. Loss trend factors reflect many items including changes in claims handling, exposure and policy forms; current and future estimates of monetary inflation and social inflation and increases in litigation and awards. These factors are periodically reviewed and subsequently adjusted, as appropriate, to reflect emerging trends which are based upon past loss experience. Thus, many factors are implicitly considered in estimating the year to year growth in loss costs recognized.

A number of actuarial assumptions are made in the review of reserves for each line of business.

For longer tail lines of business, actuarial assumptions generally are made with respect to the following:

- Loss trend factors which are used to establish expected loss ratios for subsequent accident years based on the projected loss ratio for prior accident years.
- Expected loss ratios for the latest accident year (i.e., accident year 2003 for the year end 2003 loss reserve analysis) and in some cases, for accident years prior to the latest accident year. The expected loss ratio generally reflects the projected loss ratio from prior accident years,

adjusted for the loss trend (See 1 above) and the impact of rate changes and other quantifiable factors. For low-frequency, high-severity classes such as Excess Casualty and Directors and Officers Liability (D&O), expected loss ratios generally are utilized for at least the three most recent accident years.

- Loss development factors which are used to project the reported losses for each accident year to an ultimate basis.

AIG records quarterly changes in loss reserves for each of its many General Insurance profit centers. The overall change in AIG's loss reserves is based on the sum of these profit center level changes. For most profit centers which write longer tail classes of casualty coverage, the process of recording quarterly loss reserve changes involves determining the estimated current loss ratio for each class of coverage. This loss ratio is multiplied by the current quarter's net earned premium for that class of coverage to determine the quarter's total estimated net incurred loss and loss expense. The change in loss reserves for the quarter for each class is thus the difference between the net incurred loss and loss expense, estimated as described above, and the net paid losses and loss expenses in the quarter.

The process of determining the current loss ratio for each class or business segment begins in the profit centers in the latter part of the previous year. The loss ratios determined for each profit center are based on a variety of factors. These include, but are not limited to, the following considerations: prior accident year and policy year loss ratios; actual and anticipated rate changes; actual and anticipated changes in coverage, reinsurance, or mix of business; actual and anticipated changes in external factors impacting results, such as trends in loss costs or in the legal and claims environment. Each profit center's loss ratio for the following year is subject to review by the profit center's management, by actuarial and accounting staffs, and ultimately by senior management. At the close of each quarter, the assumptions underlying the loss ratios are reviewed to determine if the loss ratios based thereon remain appropriate. This process includes a review of the actual claims experience in the quarter, actual rate changes achieved, actual changes in coverage, reinsurance or mix of business, and changes in certain other factors that may affect the loss ratio. When this review suggests that the initially determined loss ratio is no longer appropriate, the loss ratio for current business would be changed to reflect the revised assumptions.

A comprehensive annual loss reserve review is conducted in the fourth quarter of each year for each AIG General Insurance subsidiary. These reviews are conducted in full detail for each class or line of business for each subsidiary, and thus consist of literally hundreds of individual analyses. The purpose of these reviews is to confirm the reasonableness of the reserves carried by each of the individual subsidiaries, and thereby of AIG's overall carried reserves. The reserve analysis for each business class is performed by the actuarial personnel who are most familiar with that class of business. In completing these detailed actuarial reserve analyses, the actuaries are required to make numerous assumptions, including for example the selection of loss development factors and loss cost trend factors. They are also required to determine and select the most appropriate actuarial method(s) to employ for each business class. Additionally, they must determine the appropriate segmentation of data or segments from which the adequacy of the reserves can be most accurately tested. In the course of these detailed reserve reviews for each business segment, a point estimate of the loss reserve is generally determined. The sum of these point estimates for each of the individual business classes for each subsidiary provides an overall actuarial point estimate of the loss reserve for that subsidiary. The overall actuarial point estimate is compared to the subsidiary's carried loss reserve. If the carried reserve can be supported by actuarial methods and assumptions which are also believed to be reasonable, then the carried reserve would generally be considered reasonable and no adjustment would be considered. The ultimate process by which the actual carried reserves are determined considers not only the actuarial point estimate but a myriad of other factors. Other crucial internal and external factors considered include a qualitative assessment of inflation and other economic conditions in the United States and abroad, changes in the legal, regulatory, judicial and social environments, underlying policy pricing, terms and conditions, and claims handling.

With respect to the 2003 year-end actuarial loss reserve analysis for DBG, the actuaries continued to utilize the modified assumptions which gave additional weight to actual loss development from the more recent years, as identified during the 2002 analysis, with appropriate adjustments to account for the additional year of loss experience which emerged in 2003. Although the actuaries continued to use actuarial assumptions that rely on expected loss ratios based on the results of prior accident years, the expected loss ratio assumptions used gave far greater weight to the more recent accident year experience than was the case in the prior year-end assumptions. No weight was given to the more favorable experience of accident years prior to 1997. Additionally, the actuaries modified their loss cost trend assumptions to reflect the emerging experience from the recent accident years. For example, in setting the expected loss ratios for accident years 2001, 2002 and 2003 for the excess casualty lead umbrella class, the actuaries gave 100 percent weight to the results of the 1997 through 2000 accident years only, giving no weight to the more favorable development of accident years prior to 1997. In addition, they continued to utilize the 7.5 percent annual loss cost trend factor.

Loss development trends for long tail lines such as Excess Casualty and D&O, however, have not followed any consistent trend. This has at times led to overstated loss ratio projections and is a key reason why the actuaries have customarily utilized the historical projection method, which gave

more weight to the experience of older, more mature accident years. For long tail lines, judgment is required in analyzing the appropriate weighting of current trends to avoid overreacting to data anomalies that may distort such current trends. Given the accuracy of the historical approach and the uncertainty of the more recent trends, AIG management decided to give approximately equal weight to the point estimate of the required reserve resulting from the historical assumptions and the point estimate of the required reserve from the modified assumptions described above in determining the actual loss reserve carried at year-end 2003.

AIG does not believe disclosure of specific point estimates calculated by the actuaries would be meaningful. As described more fully below, considerable judgment is required in evaluating loss trends and developments for all classes of business, particularly long tailed lines. Any one actuarial point estimate is based on a particular series of judgments and assumptions of the actuary. Another actuary may give different weights or make different assumptions, and therefore reach a different point estimate. So long as the series of judgments and assumptions are reasonable, no one such point estimate is necessarily a better estimate than another point estimate. Point estimates are used to independently re-affirm the reasonableness of the overall carried reserves. Thus, provided the actuaries confirm the overall reasonableness of AIG's loss and loss expense liabilities, AIG believes that disclosure of such point estimates would not be helpful and in fact could potentially be misleading.

AIG's annual loss reserve does not calculate a range of loss reserve estimates. Because AIG's General Insurance business is primarily in long tail casualty lines driven almost entirely by severity rather than frequency of claims, developing a range around loss reserve estimates would not be meaningful. An estimate is calculated which AIG's actuaries believe provides a reasonable estimate of the required reserve. This amount is evaluated against actual carried reserves.

There is a potential for significant variation in the developing loss reserves, particularly for long tail classes of business such as excess casualty, when actual costs differ from the assumptions for loss cost trends used to test the reserves. For the excess casualty class of business, a five percent change in the assumed loss cost trend from each accident year to the next would cause approximately a \$400 million impact (either positively or negatively) to the net loss and loss expense reserve for this business. For the D&O and related management liability classes of business, a five percent change in the assumed loss cost trend would also cause approximately a \$400 million impact (either positively or negatively) to the net loss and loss expense reserve for such business. For healthcare liability business, including hospitals and other healthcare exposures, a five percent change in the assumed loss cost trend would cause approximately a \$100 million impact (either positively or negatively) to the loss and loss expense reserve for this business. Actual loss cost trends in the early 1990's were negative for these classes, whereas in the late 1990's loss costs trends ran well into the double digits for each of these three classes. The sharp increase in loss costs in the late 1990's was thus much greater than the five percent changes cited above, and caused significant increases in the overall loss reserve needs for these classes. While changes in the loss cost trend assumptions can result in a significant impact on the reserve needs for other smaller classes of liability business, the potential impact of these changes on AIG's overall carried reserves would be much less than for the classes noted above.

Another key assumption for long tail classes such as excess casualty is the loss development factors which are utilized to project the reported losses for each year to an ultimate basis. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past.

There is also the potential for variation when actual loss development differs from the assumptions used with respect to future loss development factors. For the excess casualty class, if future loss development factors differed by five percent from those utilized in the year-end 2003 loss reserve review, there would be approximately a \$400 million impact on the overall AIG loss reserve position. The comparable impact on the D&O and related management liability classes would be approximately \$200 million if future loss development factors differed by five percent from those utilized in the year-end 2003 loss reserve review. For healthcare liability classes, the impact would be approximately \$100 million. For workers' compensation reserves, the impact of a five percent deviation from the loss development factors utilized in the year-end 2003 reserve reviews would be approximately \$600 million (either positively or negatively). Because loss development factors for this class have shown less volatility than higher severity classes such as excess casualty, however, actual changes in loss development factors are expected to be less than five percent. There is some degree of volatility in loss development patterns for other longer tail liability classes as well. However, the potential impact on AIG's reserves would be much less than for the classes cited above.

Asbestos and Environmental Reserves

AIG continues to receive claims asserting injuries from toxic waste, hazardous substances, and other environmental pollutants and alleged damages to cover the cleanup costs of hazardous waste dump sites, referred to collectively as environmental claims, and indemnity claims asserting injuries from asbestos.

The vast majority of these asbestos and environmental claims emanate from policies written in 1984 and prior years. Commencing in 1985, standard policies contained an absolute exclusion for pollution related damage and an absolute asbestos exclusion was also implemented. However, AIG cur-

rently underwrites environmental impairment liability insurance on a claims made basis and has excluded such claims from this analyses.

The majority of AIG's exposures for asbestos and environmental claims are excess casualty coverages, not primary coverages. Thus, the litigation costs are treated in the same manner as indemnity reserves. That is, litigation expenses are included within the limits of the liability AIG incurs. Individual significant claim liabilities, where future litigation costs are reasonably determinable, are established on a case basis.

Estimation of asbestos and environmental claims loss reserves is a complex process. These asbestos and environmental claims cannot be estimated by AIG using conventional reserving techniques as previously described. Significant factors which affect the trends that influence the asbestos and environmental claims estimation process are the inconsistent court resolutions and judicial interpretations which broaden the intent of the policies and scope of coverage. The current case law can be characterized as still evolving and there is little likelihood that any firm direction will develop in the near future. Additionally, the exposure for cleanup costs of hazardous waste dump sites involve issues such as allocation of responsibility among potentially responsible parties and the government's refusal to release parties.

Due to this uncertainty, it is not possible to determine the future development of asbestos and environmental claims with the same degree of reliability as is with other types of claims. Such future development will be affected by the extent to which courts continue to expand the intent of the policies and the scope of the coverage, as they have in the past, as well as by the changes in Superfund and waste dump site coverage issues. AIG and other industry members will continue to litigate the broadening judicial interpretation of the policy coverage and the liability issues.

Although the estimated liabilities with respect to asbestos and environmental reserves are subject to a significantly greater margin of error than for other loss reserves, the asbestos and environmental reserves carried at the balance sheet date are believed to be adequate as these reserves are based on the known facts and current law. Furthermore, as AIG's net exposure retained relative to the gross exposure written was lower in 1984 and prior years, the potential impact of these claims is much smaller on the net loss reserves than on the gross loss reserves. However, if the asbestos and environmental reserves develop deficiently, such deficiency would have an adverse impact on future results of operations. (See the previous discussion on reinsurance collectibility herein.) AIG does not discount its asbestos and environmental reserves.

With respect to known asbestos and environmental claims, AIG established over a decade ago specialized toxic tort and environmental claims units, which investigate and adjust all such asbestos and environmental claims. These units evaluate these asbestos and environmental claims utilizing a comprehensive ground up approach on a claim-by-claim basis. The asbestos and environmental claims are reserved to ultimate probable loss based upon known facts, current law, jurisdiction, policy language and other factors. Each claim is reviewed at least semi-annually utilizing the aforementioned approach and adjusted as necessary to reflect the current information.

In both the specialized and dedicated asbestos and environmental claims units, AIG actively manages and pursues early settlement with respect to these claims thereby reducing its exposure to the unpredictable development of these claims.

With respect to asbestos claims reserves, AIG has resolved all claims with respect to miners and major manufacturers (Tier 1), and payments have been completed or reserves are established to cover future payment obligations. Asbestos claims with respect to products containing asbestos (Tier 2), are generally very mature losses, and have been appropriately recognized and reserved by AIG's asbestos claims operation. AIG believes that the vast majority of the incoming claims with respect to products containing small amounts of asbestos, companies in the distribution chain and parties with remote, ill-defined involvement with asbestos (Tier 3 and 4), should not impact its coverage. This is due to a combination of factors, including peripheral companies increasingly being named in asbestos litigation, smaller limits issued to peripheral defendants, tenuous liability cases against peripheral defendants, attachment points of the excess policies, and the manner in which resolution of these weaker cases would be allocated among all insurers, including non-AIG companies, over a long period of time.

AIG believes the majority of its known long tail environmental exposures have been resolved utilizing a combination of pro-active claim-handling techniques including policy buybacks, complete environmental releases, compromise settlements, and, where indicated, litigation. Current and new claims are generally cases of declining severity. Strong coverage defenses (including late notice) and stronger liability defenses are among the factors contributing to declining severity.

In order to test the overall reasonableness of the asbestos and environmental reserves established using the ground up approach, AIG uses primarily two methods, the market share method and the frequency/ severity method. The market share method produces indicated asbestos and environmental reserves needs by applying the appropriate AIG company market share to estimated potential industry ultimate loss and loss expenses based on the latest estimates from A.M. Best and Tillinghast.

The second method, the frequency/ severity approach, utilizes current information as the basis of an analysis that predicts for each of the next ten years a number with respect to future expected environmental claims and the average se-

verity of each. The estimated trend in frequency is based upon assumptions judged by AIG to be the most reasonable. The trend in severity starts with severities based on current actual average severity using the varying case adequacy assumptions and trending forward under assumptions deemed most reasonable by AIG. A similar frequency/ severity analysis is also performed for asbestos. However, future asbestos claims (IBNR) are projected for each of the next twenty years.

Based on the mean indication of reserve needs with respect to the market share method and based on the median indication of reserve needs with respect to the frequency/severity approach, AIG's net carried reserves were within approximately \$25 million and approximately \$50 million, respectively, of the indicated reserve needs. Hence, each of these methodologies indicated that the reserves carried were reasonable as at December 31, 2003.

Quantitative techniques frequently have to be supplemented by subjective consideration, including managerial judgment, to assure management satisfaction that the overall reserves are adequate to meet projected losses.

A summary of reserve activity, including estimates for applicable IBNR, relating to asbestos and environmental claims separately and combined at March 31, 2004 and 2003 follows:

| (in millions) | 2004 | | 2003 | |
|---|----------|--------|----------|--------|
| | Gross | Net | Gross | Net |
| Asbestos: | | | | |
| Reserve for losses and loss expenses at beginning of year | \$ 1,235 | \$ 386 | \$ 1,304 | \$ 400 |
| Losses and loss expenses incurred* | 49 | 20 | 39 | 15 |
| Losses and loss expenses paid* | (109) | (38) | (110) | (32) |
| Reserve for losses and loss expenses at end of period | \$ 1,175 | \$ 368 | \$ 1,233 | \$ 383 |
| Environmental: | | | | |
| Reserve for losses and loss expenses at beginning of year | \$ 789 | \$ 283 | \$ 832 | \$ 296 |
| Losses and loss expenses incurred* | – | (10) | (18) | (7) |
| Losses and loss expenses paid* | (33) | (13) | (38) | (21) |
| Reserve for losses and loss expenses at end of period | \$ 756 | \$ 260 | \$ 776 | \$ 268 |
| Combined: | | | | |
| Reserve for losses and loss expenses at beginning of year | \$ 2,024 | \$ 669 | \$ 2,136 | \$ 696 |
| Losses and loss expenses incurred* | 49 | 10 | 21 | 8 |
| Losses and loss expenses paid* | (142) | (51) | (148) | (53) |
| Reserve for losses and loss expenses at end of period | \$ 1,931 | \$ 628 | \$ 2,009 | \$ 651 |

* All amounts pertain to policies underwritten in prior years.

The gross and net IBNR included in the reserve for losses and loss expenses at March 31, 2004 and December 31, 2003 were estimated as follows:

| (in millions) | 2004 | | 2003 | |
|---------------|----------|--------|----------|--------|
| | Gross | Net | Gross | Net |
| Combined | \$ 1,028 | \$ 277 | \$ 1,042 | \$ 280 |

A summary of asbestos and environmental claims count activity for the three month periods ended March 31, 2004 and 2003 was as follows:

| (in millions) | 2004 | | | 2003 | | |
|---------------------------------|----------|---------------|----------|----------|---------------|----------|
| | Asbestos | Environmental | Combined | Asbestos | Environmental | Combined |
| Claims at beginning of year | 7,474 | 8,852 | 16,326 | 7,085 | 8,995 | 16,080 |
| Claims during year: | | | | | | |
| Opened | 201 | 967 | 1,168 | 99 | 387 | 486 |
| Settled | (60) | (50) | (110) | (30) | (54) | (84) |
| Dismissed or otherwise resolved | (229) | (856) | (1,085) | (23) | (787) | (810) |
| Claims at end of period | 7,386 | 8,913 | 16,299 | 7,131 | 8,541 | 15,672 |

A.M. Best, an insurance rating agency, has developed a survival ratio to measure the number of years it would take a company to exhaust both its asbestos and environmental reserves for losses and loss expenses based on that company's current level of asbestos and environmental claims payments. This is a ratio derived by taking the current ending losses and loss expense reserves and dividing by the average annual payments for the prior three years. Therefore, the ratio derived is a simplistic measure of an estimate of the number of years it would be before the current ending losses and loss expense reserves would be paid off using recent average payments. The higher the ratio, the more years the reserves for losses and loss

expenses cover these claims payments. These ratios are computed based on the ending reserves for losses and loss expenses over the respective claims settlement during the fiscal year. Such payments include indemnity payments and legal and loss adjustment payments. It should be noted, however, that this is an extremely simplistic approach to measuring asbestos and environmental reserve levels. Many factors, such as aggressive settlement procedures, mix of business and level of coverage provided, have a significant impact on the amount of asbestos and environmental losses and loss expense reserves, ultimate payments made and the resultant ratio.

AIG believes that voluntary payments with respect to environmental claims should be excluded from the calculation of the survival ratio for the environmental claims. That is, involuntary payments are primarily attributable to court judgments, court orders, covered claims with no coverage defenses, state mandated clean up costs, claims where AIG's coverage defenses are minimal and settlements that are made less than six months before the first trial setting. Payments other than these are deemed voluntary because AIG can control the amount and timing of such payments, if any.

AIG's survival ratios for asbestos and environmental claims, separately and combined, excluding voluntary environmental claim payments, were based upon a three year average payment. These ratios at March 31, 2004 and 2003 were as follows:

| | Gross | Net |
|-------------------------|-------------|-------------|
| 2004 | | |
| Survival ratios: | | |
| Asbestos | 4.0 | 3.8 |
| Environmental | 14.2 | 10.6 |
| Combined | 7.0 | 6.4 |
| 2003 | | |
| Survival ratios: | | |
| Asbestos | 3.7 | 3.5 |
| Environmental | 15.7 | 11.8 |
| Combined | 6.6 | 6.2 |

Life Insurance & Retirement Services Operations

AIG's Life Insurance & Retirement Services subsidiaries offer a wide range of traditional insurance and financial and investment products both domestically and abroad. Traditional products consist of individual and group life, annuity, endowment and accident and health policies. Financial and investment products consist of fixed and variable annuities and pensions. (See also Note 2 of Notes to Financial Statements.)

Domestically, AIG's Life Insurance & Retirement Services operations offer a broad range of protection products, including life insurance, group life and health products and payout annuities which include single premium immediate annuities, structured settlements and terminal funding annuities. Home service operations include an array of traditional and investment type products sold through agents. Retirement services include group retirement products, individual fixed and variable annuity operations and annuity run-off operations which include fixed and variable annuities largely sold through merger related discontinued distribution relationships. AIG's principal domestic Life Insurance & Retirement Services operations include AIG American General Life Companies, AIG Annuity Insurance Company, The Variable Annuity Life Insurance Company (VALIC) and SunAmerica Life Insurance Company.

Overseas, AIG's Life Insurance & Retirement Services operations include traditional products such as whole and term life and endowments, personal accident & health products, group products including life and health and fixed and variable annuities. AIG operates overseas principally through American Life Insurance Company (ALICO), American International Assurance Company, Limited (AIA), American International Assurance Company, (Bermuda) Limited (AIA(B)), Nan Shan Life Insurance Company, Ltd. (Nan Shan) and AIG Star Life Insurance Co., Ltd. (AIG Star). AIG added significantly to its presence in Japan with the acquisition of GE Edison Life Insurance Company (now known as AIG Edison Life Insurance Company) (AIG Edison Life), in 2003. ALICO is incorporated in Delaware and all of its business is written outside of the United States. ALICO has operations either directly or through subsidiaries in Europe, Africa, Latin America, the Caribbean, the Middle East, South Asia, and the Far East, with Japan being the largest territory. AIA operates primarily in China (including Hong Kong), Singapore, Malaysia and Thailand. Nan Shan operates in Taiwan. AIG Star operates in Japan.

Life Insurance & Retirement Services operations presented on a major product basis for the three month periods ending March 31, 2004 and 2003 were as follows:

| <i>(in millions)</i> | 2004 | 2003 ^(a) |
|--|--------------|---------------------|
| GAAP premiums: | | |
| Domestic Life: | | |
| Life insurance | \$ 430 | \$ 428 |
| Home service | 206 | 209 |
| Group life/health | 268 | 232 |
| Payout annuities ^(b) | 374 | 420 |
| Total | 1,278 | 1,289 |
| Domestic Retirement Services: | | |
| Group retirement products | 76 | 54 |
| Individual fixed annuities | 13 | 7 |
| Individual variable annuities | 100 | 73 |
| Individual annuities-runoff ^(c) | 20 | 22 |
| Total | 209 | 156 |

American International Group, Inc. and Subsidiaries

| <i>(in millions)</i> | 2004 | 2003 ^(a) |
|---|---------------------|---------------------|
| Foreign Life: | | |
| Life insurance | 3,870 | 3,236 |
| Personal accident & health | 1,029 | 691 |
| Group products | 416 | 349 |
| Total | 5,315 | 4,276 |
| Foreign Retirement Services: | | |
| Individual fixed annuities | 85 | 61 |
| Individual variable annuities | 13 | 3 |
| Total | 98 | 64 |
| Total Foreign | 5,413 | 4,340 |
| Total GAAP premiums | \$ 6,900 | \$ 5,785 |
| Net investment income: | | |
| Domestic Life: | | |
| Life insurance | \$ 380 | \$ 284 |
| Home service | 175 | 168 |
| Group life/health | 31 | 28 |
| Payout annuities | 199 | 169 |
| Total | 785 | 649 |
| Domestic Retirement Services: | | |
| Group retirement products | 542 | 491 |
| Individual fixed annuities | 758 | 569 |
| Individual variable annuities | 55 | 54 |
| Individual annuities-runoff ^(c) | 276 | 331 |
| Total | 1,631 | 1,445 |
| Total Domestic | 2,416 | 2,094 |
| Foreign Life: | | |
| Life insurance | 1,093 | 902 |
| Personal accident & health | 42 | 37 |
| Group products | 107 | 82 |
| Intercompany adjustments | (4) | (3) |
| Total | 1,238 | 1,018 |
| Foreign Retirement Services: | | |
| Individual fixed annuities | 208 | 70 |
| Individual variable annuities | 79 | - |
| Total | 287 | 70 |
| Total Foreign | 1,525 | 1,088 |
| Total net investment income ^(d) | \$ 3,941 | \$ 3,182 |
| Realized capital gains (losses) ^(d) | 49 | (338) |
| Total operating income | \$ 2,093 | \$ 1,310 |
| Life insurance in-force ^(e): | | |
| Domestic | \$ 673,443 | \$ 645,606 |
| Foreign | 968,051 | 951,020 |
| Total | \$ 1,641,494 | \$ 1,596,626 |

(a) Restated to conform to 2004 presentation.

(b) Includes structured settlements, single premium immediate annuities and terminal funding annuities.

(c) Represents runoff annuity business sold through merger related discontinued distribution relationships.

(d) For purposes of this presentation, investment income reflects certain amounts of realized capital gains where the gains are deemed to be an inherent element in pricing certain life products in some foreign countries.

(e) Amounts presented were as at March 31, 2004 and December 31, 2003.

Life Insurance & Retirement Services Results

The increase in operating income in the first three months of 2004 when compared to the same period of 2003 was caused in part by strong growth, particularly overseas, and the improvement in realized capital gains (losses) relative to the same period of 2003.

The contribution of Life Insurance & Retirement Services operating income to AIG's consolidated income before income taxes, minority interest and cumulative effect of an accounting change amounted to 48.8 percent in the first three months of 2004 compared to 44.8 percent in the same period of 2003.

Life GAAP premiums grew in the first three months of 2004 when compared with the same period in 2003. Domestically, the growth is predominantly attributable to Group/life health, Group retirement products and Individual fixed and variable annuities. With respect to Foreign Life, the majority of the growth in GAAP Life & Retirement Services premiums was attributable to the Life insurance and Personal accident & health lines of business. This growth was most significant in Southeast Asia where AIG maintains significant market share established by its strong agency force, and in Japan, where AIG is benefiting from a flight to quality. Foreign Life Insurance & Retirement Services operations produced 78.5 percent and 75.0 of Life Insurance & Retirement Services GAAP premiums in 2004 and 2003, respectively.

As previously discussed, the U.S. dollar weakened in relation to most major foreign currencies in which AIG transacts business. Accordingly, for the first three months of 2004, when foreign life premiums were translated into U.S. dollars for purposes of the preparation of the consolidated financial statements, total life premiums were approximately 5.3 percentage points more than they would have been if translated utilizing exchange rates prevailing in 2003.

Under U.S. GAAP, deposits and certain other considerations received under deferred annuity (variable and fixed) and universal life contracts are not included as GAAP premiums. If such amounts were to be included, the overall growth from 2004 over 2003 would be more dramatic, due in part to large increases in foreign individual fixed annuities.

The growth in net investment income in the first three months of 2004 when compared to the same period of 2003 was attributable to both foreign and domestic invested new cash flow for investment as well as improved returns on nontraditional investments. Additionally, net investment income was positively impacted by the compounding of previously earned and reinvested net investment income. (See also the discussion under "Liquidity" herein.)

Life Insurance & Retirement Services investment portfolios are managed within the overall objectives of the Life Insurance & Retirement Services operations. The realized capital gains in the first three months of 2004 reflect an improved economy, stronger corporate balance sheets and a significantly lower level of impairments. The realized capital losses in the first three months of 2003 reflect impairment loss provisions for certain equity and fixed income holdings. (See also the discussion on "Valuation of Invested Assets" herein.)

Underwriting and Investment Risk

The risks associated with the traditional life and accident and health products are underwriting risk and investment risk. The risk associated with the financial and investment contract products is primarily investment risk.

Underwriting risk represents the exposure to loss resulting from the actual policy experience adversely emerging in comparison to the assumptions made in the product pricing associated with mortality, morbidity, termination and expenses. The emergence of significant adverse experience would require an adjustment to the benefit reserves that could have a substantial impact with respect to AIG's results of operations.

AIG's foreign life companies limit their maximum underwriting exposure on traditional life insurance of a single life to approximately \$1.5 million of coverage and AIG's domestic life companies generally limit their maximum underwriting exposure on traditional life insurance of a single life to \$2.5 million of coverage by using yearly renewable term reinsurance. (See also the discussion under "Liquidity" herein.)

The investment risk represents the exposure to loss resulting from the cash flows from the invested assets, primarily long-term fixed rate investments, being less than the cash flows required to meet the obligations of the expected policy and contract liabilities and the necessary return on investments. (See also the discussion under "Liquidity" herein.)

To minimize its exposure to investment risk, AIG tests the cash flows from the invested assets and the policy and contract liabilities using various interest rate scenarios to assess whether there is a liquidity excess or deficit. If a rebalancing of the invested assets to the policy and contract claims became necessary and did not occur, a demand could be placed upon liquidity. (See also the discussion under "Liquidity" herein.)

The asset-liability relationship is appropriately managed in AIG's foreign operations, as it has been throughout AIG's history, even though certain territories lack qualified long-term investments or there are investment restrictions imposed by the local regulatory authorities. For example, in Japan and several Southeast Asia territories, the duration of the investments is often for a shorter period than the effective maturity of the related policy liabilities. Therefore, there is a risk that the reinvestment of the proceeds at the maturity of the initial investments may be at a yield below that of the interest required for the accretion of the policy liabilities. Additionally, there exists a future investment risk associated with certain policies currently in force which will have premium receipts in the future. That is, the investment of these future premium receipts may be at a yield below that required to meet future policy liabilities.

To maintain an adequate yield to match the interest necessary to support future policy liabilities, constant management focus is required to reinvest the proceeds of the maturing securities and to invest the future premium receipts while continuing to maintain satisfactory investment quality.

To the extent permitted under local regulation, AIG may invest in qualified longer-term securities outside Japan to achieve a closer matching in both duration and the required yield. AIG is able to manage any asset-liability duration difference through maintenance of sufficient global liquidity and to support any operational shortfall through its international financial network. (See also the discussion under "Liquidity" herein.)

Certain foreign jurisdictions have limited long-dated bond markets and AIG may use alternative investments, including equities and foreign denominated fixed income instruments to extend the effective duration of the investment portfolio to more closely match that of the policyholder liabilities.

The asset-liability relationship is appropriately managed in AIG's domestic operations, as there is ample supply of qualified long-term investments.

AIG uses asset-liability matching as a management tool worldwide to determine the composition of the invested assets and appropriate marketing strategies. As a part of these strategies, AIG may determine that it is economically advantageous to be temporarily in an unmatched position due to anticipated interest rate or other economic changes.

A number of guaranteed benefits are offered on certain variable life products. (For further discussion see Note 7 of Notes to Financial Statements.)

DAC for life insurance products arises from the deferral of those costs that vary with, and are directly related to, the acquisition of new or renewal business. Policy acquisition costs for traditional life insurance products are generally deferred and amortized over the premium paying period of the policy. Policy acquisition costs which relate to universal life and investment-type products, including fixed annuities, (nontraditional life products) are deferred and amortized, with interest, as appropriate, in relation to the historical and future incidence of estimated gross profits to be realized over the estimated lives of the contracts. With respect to variable annuities, AIG's policy, as appropriate, has been to adjust amortization assumptions for DAC when estimates of current or future gross profits to be realized from these contracts are revised. With respect to variable annuities sold domestically (representing the vast majority of AIG's variable annuity business), the assumption for the long-term annual net growth rate of the equity markets used in the determination of DAC amortization is approximately 10 percent. A methodology referred to as "reversion to the mean" is used to maintain this long-term net growth rate assumption, while giving consideration to short-term variations in equity markets. Estimated gross profits include investment income and gains and losses

on investments less interest required as well as other charges in the contract less actual mortality and expenses. Current experience and changes in the expected future gross profits are analyzed to determine the impact on the amortization of DAC. The estimation of projected gross profits requires significant management judgment. The elements with respect to the current and projected gross profits are reviewed and analyzed quarterly and are appropriately adjusted.

AIG's variable annuity earnings will be affected by changes in market returns because separate account revenues, primarily composed of mortality and expense charges and asset management fees, are a function of asset values.

DAC for both traditional life and nontraditional life products as well as retirement services products are subject to review for recoverability, which involve estimating the future profitability of current business. This review also involves significant management judgment. If the actual emergence of future profitability were to be substantially different than that estimated, AIG's results of operations could be significantly impacted.

Insurance Invested Assets

AIG's general strategy is to invest in high quality securities while maintaining diversification to avoid significant exposure to issuer, industry and/or country concentrations. With respect to General Insurance, AIG's strategy is to invest in longer duration fixed maturities to maximize the yields at the date of purchase. With respect to Life Insurance & Retirement Services, AIG's strategy is to produce cash flows required to meet maturing insurance liabilities. (See also the discussion under "Operating Review: Life Insurance & Retirement Services Operations" herein.) AIG invests in equities for various reasons, including diversifying its overall exposure to interest rate risk. Equity securities are subject to declines in fair value. Such declines in fair value are presented in unrealized appreciation or depreciation of investments, net of taxes as a component of comprehensive income. Generally, insurance regulations restrict the types of assets in which an insurance company may invest. When permitted by regulatory authorities and when deemed necessary to protect insurance assets, including invested assets, from adverse movements in foreign currency exchange rates, interest rates and equity prices, AIG and its insurance subsidiaries may enter into derivative transactions as end users. (See also the discussion under "Derivatives" herein.)

In certain jurisdictions, significant regulatory and/or foreign governmental barriers exist which may not permit the immediate free flow of funds between insurance subsidiaries or from the insurance subsidiaries to AIG parent. These barriers generally cause only minor delays in the outward remittance of the funds.

The following tables summarize the composition of AIG's insurance invested assets by insurance segment, at March 31, 2004 and December 31, 2003:

| March 31, 2004 (dollars in millions) | General Insurance | Life Insurance & Retirement Services | Total | Percent of Total | Percent Distribution | |
|--|----------------------|---|-------------------|---------------------|----------------------|--------------|
| | | | | | Domestic | Foreign |
| Fixed Maturities: | | | | | | |
| Available for sale, at market value ^(a) | \$ 43,463 | \$ 276,178 | \$ 319,641 | 72.1% | 63.0% | 37.0% |
| Held to maturity, at amortized cost | 9,823 | — | 9,823 | 2.2 | 100.0 | — |
| Equity securities, at market value ^(b) | 5,220 | 9,127 | 14,347 | 3.2 | 35.4 | 64.6 |
| Mortgage loans on real estate, policy and collateral loans | 25 | 20,343 | 20,368 | 4.6 | 67.3 | 32.7 |
| Short-term investments, including time deposits, and cash | 1,724 | 15,357 | 17,081 | 3.9 | 46.1 | 53.9 |
| Real estate | 579 | 2,902 | 3,481 | 0.8 | 22.1 | 77.9 |
| Investment income due and accrued | 956 | 4,341 | 5,297 | 1.2 | 62.5 | 37.5 |
| Securities lending collateral | 6,256 | 34,439 | 40,695 | 9.2 | 79.1 | 20.9 |
| Other invested assets | 5,874 | 6,478 | 12,352 | 2.8 | 83.0 | 17.0 |
| Total | \$ 73,920 | \$ 369,165 | \$ 443,085 | 100.0% | 64.1% | 35.9% |

(a) Includes \$1.97 billion of bond trading securities, at market value.

(b) Includes \$2.04 billion of nonredeemable preferred stocks, at market value.

| December 31, 2003 (dollars in millions) | General Insurance | Life Insurance & Retirement Services | Total | Percent of Total | Percent Distribution | |
|---|----------------------|---|-------------------|---------------------|----------------------|--------------|
| | | | | | Domestic | Foreign |
| Fixed Maturities: | | | | | | |
| Available for sale, at market value ^(a) | \$ 41,610 | \$ 258,139 | \$ 299,749 | 75.9% | 64.1% | 35.9% |
| Held to maturity, at amortized cost | 8,037 | – | 8,037 | 2.0 | 100.0 | – |
| Equity securities, at market value ^(b) | 5,130 | 4,233 | 9,363 | 2.4 | 53.7 | 46.3 |
| Mortgage loans on real estate, policy and collateral loans | 25 | 20,260 | 20,285 | 5.1 | 67.7 | 32.3 |
| Short-term investments, including time deposits, and cash | 1,918 | 6,497 | 8,415 | 2.1 | 50.3 | 49.7 |
| Real estate | 569 | 2,903 | 3,472 | 0.9 | 22.7 | 77.3 |
| Investment income due and accrued | 881 | 4,003 | 4,884 | 1.2 | 62.8 | 37.2 |
| Securities lending collateral | 5,225 | 24,970 | 30,195 | 7.7 | 76.0 | 24.0 |
| Other invested assets | 5,121 | 5,357 | 10,478 | 2.7 | 81.9 | 18.1 |
| Total | \$ 68,516 | \$ 326,362 | \$ 394,878 | 100.0% | 65.4% | 34.6% |

(a) Includes \$282 million of bond trading securities, at market value.

(b) Includes \$1.90 billion of nonredeemable preferred stocks, at market value.

Credit Quality

At March 31, 2004, approximately 64 percent of the fixed maturities investments were domestic securities. Approximately 32 percent of such domestic securities were rated AAA by one or more of the principal rating agencies. Approximately 7 percent were below investment grade or not rated.

A significant portion of the foreign insurance fixed income portfolio is rated by Moody's, Standard & Poor's (S&P) or similar foreign services. Similar credit quality rating services are not available in all overseas locations. AIG annually reviews the credit quality of the foreign portfolio nonrated fixed income investments, including mortgages. At March 31, 2004, approximately 17 percent of the foreign fixed income investments were either rated AAA or, on the basis of AIG's internal analysis, were equivalent from a credit standpoint to securities so rated. Approximately 6 percent were below investment grade or not rated at that date. A large portion of the foreign insurance fixed income portfolio are sovereign fixed maturity securities supporting the policy liabilities in the country of issuance.

Any fixed income security may be subject to downgrade for a variety of reasons subsequent to any balance sheet date.

Valuation of Invested Assets

The valuation of invested assets involves obtaining a market value for each security. The source for the market value is generally from market exchanges or dealer quotations, with the exception of nontraded securities.

Another aspect of valuation is an assessment of impairment. As a matter of policy, the determination that a security has incurred an other-than-temporary decline in value and the amount of any loss recognition requires the judgment of AIG's management and a continual review of its investments.

In general, a security is considered a candidate for impairment if it meets any of the following criteria:

- Trading at a significant discount to par, amortized cost (if lower) or cost for an extended period of time;
- The occurrence of a discrete credit event resulting in (i) the issuer defaulting on a material outstanding obligation; or (ii) the issuer seeking protection from creditors under the bankruptcy laws or any similar laws intended for the court supervised reorganization of insolvent enterprises; or (iii) the issuer proposing a voluntary reorganization pursuant to which creditors are asked to exchange their claims for cash or securities having a fair value substantially lower than par value of their claims; or
- In the opinion of AIG's management, it is possible that AIG may not realize a full recovery on its investment, irrespective of the occurrence of one of the foregoing events.

Once a security has been identified as impaired, the amount of such impairment is determined by reference to that security's contemporaneous market price.

AIG has the ability to hold any security to its stated maturity. Therefore, the decision to sell reflects the judgment of AIG's management that the security sold is unlikely to provide, on a relative value basis, as attractive a return in the future as alternative securities entailing comparable risks. With respect to distressed securities, the sale decision reflects management's judgment that the risk-discounted anticipated ultimate recovery is less than the value achievable on sale.

As a result of these policies, AIG recorded impairment losses, net of taxes, of \$130 million and \$479 million in the first three months of 2004 and 2003, respectively. The recovery in global equity markets and reasonably steady domestic interest rates were the primary reasons for the decline in impairment loss recognition from 2003 to 2004.

No impairment charge with respect to any one single credit was significant to AIG's consolidated financial condition or results of operations, and no individual impairment loss exceeded 1.5 percent of consolidated net income for the first three months of 2004.

Excluding the impairments noted above, the changes in market value for AIG's available for sale portfolio, which constitutes the vast majority of AIG's investments, were recorded in accumulated other comprehensive income as unrealized gains or losses.

At March 31, 2004, the unrealized losses after taxes of the fixed maturity securities were approximately \$886 million. At March 31, 2004, the unrealized losses after taxes of the equity securities portfolio were approximately \$83 million.

At March 31, 2004, aggregate unrealized gains after taxes were \$13.7 billion and aggregate unrealized losses after taxes were \$969 million. No single issuer accounted for more than three percent of the unrealized losses.

At March 31, 2004, the fair value of AIG's fixed maturities and equity securities aggregated to \$345.8 billion. Of this aggregate fair value, 0.29 percent represented securities trading at or below 75 percent of amortized cost or cost.

The impact on net income of unrealized losses after taxes will be further mitigated upon realization, because certain realized losses will be charged to participating policyholder accounts, or realization will result in current decreases in the amortization of certain deferred acquisition costs.

At March 31, 2004, unrealized losses for fixed maturity securities and equity securities did not reflect any significant industry concentrations.

The amortized cost of fixed maturities available for sale in an unrealized loss position at March 31, 2004, by contractual maturity, is shown below:

| <i>(in millions)</i> | Amortized Cost |
|--|-------------------|
| Due in one year or less | \$ 1,335 |
| Due after one year through five years | 5,022 |
| Due after five years through ten years | 11,601 |
| Due after ten years | 19,537 |
| Total | \$ 37,495 |

In the three months ended March 31, 2004, the pretax realized losses incurred with respect to the sale of fixed maturities and equity securities were \$369 million. The aggregate fair value of securities sold was \$6.1 billion, which was approximately 98 percent of amortized cost. The average period of time that securities sold at a loss during the quarter ended March 31, 2004 were trading continuously at a price below book value was approximately seven months.

At March 31, 2004, aggregate pretax unrealized gains were \$21.0 billion, while the pretax unrealized losses with respect to investment grade bonds, below investment grade bonds and equity securities were \$881 million, \$482 million and \$127 million, respectively. Aging of the pretax unrealized losses with respect to these securities, distributed as a percentage of cost relative to unrealized loss (the extent by which the market value is less than amortized cost or cost), including the number of respective items, was as follows:

| Aging (dollars in millions) | Less than or equal to 20% of Cost ^(a) | | | Greater than 20% to 50% of Cost ^(a) | | | Greater than 50% of Cost ^(a) | | | Total | | |
|-------------------------------------|---|--------------------|--------------|---|--------------------|------------|--|--------------------|-----------|---------------------|-----------------------------------|--------------|
| | Cost ^(a) | Unrealized Loss | Items | Cost ^(a) | Unrealized Loss | Items | Cost ^(a) | Unrealized Loss | Items | Cost ^(a) | Unrealized Loss ^(b) | Items |
| Investment grade bonds | | | | | | | | | | | | |
| 0-6 months | \$ 21,095 | \$ 367 | 1,076 | \$ 30 | \$ 10 | 6 | \$ – | \$ – | – | \$ 21,125 | \$ 377 | 1,082 |
| 7-12 months | 9,971 | 356 | 734 | 15 | 4 | 2 | – | – | – | 9,986 | 360 | 736 |
| >12 months | 2,221 | 112 | 255 | 127 | 32 | 12 | – | – | – | 2,348 | 144 | 267 |
| Total | \$ 33,287 | \$ 835 | 2,065 | \$ 172 | \$ 46 | 20 | \$ – | \$ – | – | \$ 33,459 | \$ 881 | 2,085 |
| Below investment grade bonds | | | | | | | | | | | | |
| 0-6 months | \$ 1,698 | \$ 80 | 371 | \$ 52 | \$ 15 | 15 | \$ 12 | \$ 10 | 11 | \$ 1,762 | \$ 105 | 397 |
| 7-12 months | 209 | 16 | 65 | 112 | 29 | 20 | – | – | – | 321 | 45 | 85 |
| >12 months | 1,356 | 151 | 195 | 557 | 158 | 97 | 40 | 23 | 4 | 1,953 | 332 | 296 |
| Total | \$ 3,263 | \$ 247 | 631 | \$ 721 | \$ 202 | 132 | \$ 52 | \$ 33 | 15 | \$ 4,036 | \$ 482 | 778 |
| Total bonds | | | | | | | | | | | | |
| 0-6 months | \$ 22,793 | \$ 447 | 1,447 | \$ 82 | \$ 25 | 21 | \$ 12 | \$ 10 | 11 | \$ 22,887 | \$ 482 | 1,479 |
| 7-12 months | 10,180 | 372 | 799 | 127 | 33 | 22 | – | – | – | 10,307 | 405 | 821 |
| >12 months | 3,577 | 263 | 450 | 684 | 190 | 109 | 40 | 23 | 4 | 4,301 | 476 | 563 |
| Total | \$ 36,550 | \$ 1,082 | 2,696 | \$ 893 | \$ 248 | 152 | \$ 52 | \$ 33 | 15 | \$ 37,495 | \$ 1,363 | 2,863 |
| Equity securities | | | | | | | | | | | | |
| 0-6 months | \$ 903 | \$ 46 | 504 | \$ 72 | \$ 25 | 47 | \$ 6 | \$ 5 | 8 | \$ 981 | \$ 76 | 559 |
| 7-12 months | 75 | 4 | 52 | 70 | 18 | 9 | 7 | 6 | 14 | 152 | 28 | 75 |
| >12 months | 333 | 10 | 89 | 34 | 10 | 42 | 3 | 3 | 34 | 370 | 23 | 165 |
| Total | \$ 1,311 | \$ 60 | 645 | \$ 176 | \$ 53 | 98 | \$ 16 | \$ 14 | 56 | \$ 1,503 | \$ 127 | 799 |

(a) For bonds, represents amortized cost.

(b) As more fully described above, upon realization, certain realized losses will be charged to participating policyholder accounts, or realization will result in a current decrease in the amortization of certain deferred acquisition costs.

As stated previously, the valuation for AIG's investment portfolio comes from market exchanges or dealer quotations, with the exception of nontraded securities. AIG considers nontraded securities to mean certain fixed income investments, certain structured securities, direct private equities, limited partnerships and hedge funds. The aggregate carrying value of these securities at March 31, 2004 was approximately \$67.2 billion.

The methodology used to estimate fair value of nontraded fixed income investments is by reference to traded securities with similar attributes and using a matrix pricing methodology. This technique takes into account such factors as the industry, the security's rating and tenor, its coupon rate, its position in the capital structure of the issuer, and other relevant factors. The change in fair value is recognized as a component of unrealized appreciation.

For certain structured securities, the carrying value is based on an estimate of the security's future cash flows pursuant to the requirements of Emerging Issues Task Force Issue No. 99-20, "Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets." The change in carrying value is recognized in income.

Direct private equities, hedge funds and limited partnerships in which AIG holds in the aggregate less than a five percent interest, are carried at fair value. The change in fair value is recognized as a component of Other comprehensive income.

With respect to hedge funds and limited partnerships in which AIG holds in the aggregate a five percent or greater interest, AIG's carrying value is the net asset value. The changes in such net asset values are recorded in income.

AIG obtains the fair value of its investments in limited partnerships and hedge funds from information provided by the sponsors of each of these investments, the accounts of which are generally audited on an annual basis.

Each of these investment categories is regularly tested to determine if impairment in value exists. Various valuation techniques are used with respect to each category in this determination.

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified financial products and services including aircraft leasing, capital market transactions, and consumer and insurance premium financing. (See also Note 2 of Notes to Financial Statements.)

AIG's Aircraft Finance operations represent the operations of International Lease Finance Corporation (ILFC), which generates its revenues primarily from leasing new and used commercial jet aircraft to domestic and foreign airlines. Revenues also result from the remarketing of commercial jets for its own account, for airlines and for financial institutions.

ILFC finances its purchases of aircraft primarily through the issuance of a variety of debt instruments. The composite borrowing rates at the end of the first three months of 2004 and 2003 were 4.34 percent and 4.57 percent, respectively. (See also the discussions under "Capital Resources" and "Liquidity" herein and Note 2 of Notes to Financial Statements.)

ILFC is exposed to operating loss and liquidity strain through nonperformance of aircraft lessees, through owning aircraft which it would be unable to sell or re-lease at acceptable rates at lease expiration and, in part, through committing to purchase aircraft which it would be unable to lease.

ILFC manages its lessee nonperformance exposure through credit reviews and security deposit requirements. As a result of these measures and its own contingency planning, ILFC did not suffer any material losses from airline shutdowns in the aftermath of the September 11 terrorist attacks, but there can be no assurance that ILFC will successfully manage the risks relating to the impact of possible future deterioration in the airline industry. Over 80 percent of ILFC's fleet is leased to non-U.S. carriers, and this fleet, comprised of the most efficient aircraft in the airline industry, continues to be in high demand from such carriers.

ILFC typically contracts to re-lease aircraft before the end of the existing lease term. For aircraft returned before the end of the lease term, ILFC has generally been able to re-lease such aircraft within two to six months of its return. While some of the lease rates for aircraft that have been redeployed are lower, this is partially offset by low interest rates, which reduce ILFC's financing costs. As a lessor, ILFC considers an aircraft "idle" or "off lease" when the aircraft is not subject to a signed lease agreement or signed letter of intent. ILFC had one aircraft off lease at March 31, 2004 which had been off lease for less than three months. The unleased aircraft was subsequently placed. (See also the discussions under "Capital Resources" and "Liquidity" herein.)

During 2004, ILFC entered into a securitization of a portfolio of 34 aircraft. Certain of AIG's Life Insurance & Retirement Services businesses purchased a large share of this securitization.

ILFC management is very active in the airline industry. Management formally reviews regularly, and no less frequently than quarterly, issues affecting ILFC's fleet, including events and circumstances that may cause impairment of aircraft values. Management evaluates aircraft in the fleet as necessary, based on these events and circumstances in accordance with Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (FAS 144). ILFC has not recognized any impairment related to its fleet, as the existing service potential of the aircraft in ILFC's portfolio has not been diminished. Further, ILFC has been able to re-lease the aircraft without diminution in lease rates to an extent that would require an impairment write-down. (See also the discussions under "Liquidity" herein.)

In the third quarter of 2003, AIG integrated the operations of AIG Trading Group Inc. and its subsidiaries (AIGTG) and AIG Financial Products Corp. and its subsidiaries (AIGFP) thereby establishing the Capital Markets operating and reporting unit. AIG believes that this will result in greater efficiencies and product synergies as well as growth opportunities. As Capital Markets is a transaction-oriented operation, current and past revenues and operating results may not provide a basis for predicting future performance.

AIG's Capital Markets operations derive substantially all their revenues from proprietary positions entered in connection with counterparty transactions rather than from speculative transactions. These subsidiaries participate in the derivatives dealer market conducting, primarily as principal, an interest rate, currency, equity, commodity and credit derivative products business.

As dealers, AIGFP and AIGTG mark transactions to fair value daily. Thus, a gain or loss on each transaction is recognized daily. AIGFP and AIGTG hedge the market risks arising from their transactions. Therefore, revenues and operating income are not significantly exposed to or affected by market fluctuations and volatility. Revenues of the Capital Markets operations and the percentage change in revenues for any given period are significantly affected by the number and size of transactions entered into by these subsidiaries during that period relative to those entered into during the prior period. Operating income and the percentage change in operating income for any period are determined by the number, size and profitability of the transactions attributable to that period relative to those attributable to the prior period. Generally, the realization of trading revenues as measured by the receipt of funds is not a significant reporting event as the gain or loss on Capital Markets trading transactions are currently reflected in operating income as the fair values change from period to period.

Derivative transactions are entered into in the ordinary course of Capital Markets operations. Therefore, income on interest rate, equity, commodity and credit derivatives along

with their related hedges are recorded on a mark to market value or at estimated fair value where market prices are not readily available with the resulting unrealized gains or losses reflected in the income statement in the current year. In the first quarter of 2004, less than five percent of revenues resulted from transactions valued at estimated fair value. The mark to fair value of derivative transactions is reflected in the balance sheet in the captions "Unrealized gain on interest rate and currency swaps, options and forward transactions" and "Unrealized loss on interest rate and currency swaps, options and forward transactions." The unrealized gain represents the present value of the aggregate of each net receivable by counterparty, and the unrealized loss represents the present value of the aggregate of each net payable by counterparty as of March 31, 2004. These amounts will change from one period to the next due to changes in interest rates, currency rates, equity prices and other market variables, as well as cash movements, execution of new transactions and the maturing of existing transactions. (See also the discussion under "Derivatives" herein.) Spread income on investments and borrowings are recorded on an accrual basis over the life of the transaction. Investments are classified as available for sale securities and are marked to market with the resulting unrealized gains or losses reflected in shareholders' equity.

Domestically, AIG's Consumer Finance operations derive a substantial portion of their revenues from finance charges assessed on outstanding mortgages, home equity loans, secured and unsecured consumer loans and retail merchant financing. Overseas operations provide credit cards, personal and auto loans, term deposits, savings accounts, sales finance and mortgages with an emphasis on emerging markets.

Consumer Finance operations are exposed to loss when contractual payments are not received. Collection exposure is managed through the mix of tight underwriting controls, mix of loans and collateral thereon.

Financial Services operations for the three month periods ending March 31, 2004 and 2003 were as follows:

| <i>(in millions)</i> | 2004 | 2003 |
|---|-----------------|-----------------|
| Revenues: | | |
| Aircraft Finance ^(a) | \$ 752 | \$ 722 |
| Capital Markets ^(b) | 333 | 325 |
| Consumer Finance ^(c) | 693 | 639 |
| Other | 8 | 7 |
| Total | \$ 1,786 | \$ 1,693 |
| Operating income: | | |
| Aircraft Finance | \$ 160 | \$ 174 |
| Capital Markets | 183 | 211 |
| Consumer Finance | 183 | 148 |
| Other, including intercompany adjustments | (3) | (3) |
| Total | \$ 523 | \$ 530 |

(a) Revenues were primarily from ILFC aircraft lease rentals.

(b) Revenues were primarily from AIGFP and AIGTG proprietary positions entered into in connection with counterparty transactions.

(c) Revenues were primarily finance charges.

Financial Services Results

ILFC's securitization of approximately \$2 billion in aircraft in the third quarter of 2003 and first quarter of 2004, and the transaction - oriented nature of Capital Markets operations were the primary reason for the decline in operating income in the first three months of 2004 compared to the same period of 2003.

Financial Services operating income represented 12.2 percent of AIG's consolidated income before income taxes, minority interest and cumulative effect of an accounting change in the first three months of 2004. This compares to 18.1 percent in the same period of 2003.

With respect to ILFC, the revenue growth in the first three months of 2004 resulted primarily from the increase in flight equipment under operating lease and the increase in the relative cost of the leased fleet.

The composition by percentage contribution of revenues and operating income for Capital Markets in the first three months of 2004 and 2003 is set forth below. The percentages for operating income are the same as those for revenues because expenses are allocated across all products in proportion to the revenues generated by that product. Material changes in the distribution of revenues and operating income from period to period are not unusual due to the transactional nature of Capital Markets' business.

| | 2004 | 2003 |
|---|------|------|
| Spread income on investments and borrowings | 43% | 46% |
| Interest rate and currency products | 36 | 30 |
| Equity linked products | 5 | 2 |
| Credit linked products | 10 | 14 |
| Commodity and commodity linked products and other revenue | 6 | 8 |

Financial market conditions in the first quarter of 2004 compared with the first quarter of 2003 were characterized by interest rates which were broadly unchanged across fixed income markets globally, a tightening of credit spreads, and higher equity valuations. Capital Markets' results in 2004 compared with 2003 reflected a shift in product segment activity to respond to these conditions. In particular, Capital Markets experienced increases in demand for interest and currency linked products that addressed the risk management needs of its counterparties.

The most significant component of Capital Markets' operating expenses is compensation, which approximated 34 percent and 32 percent of revenues in the first three months of 2004 and 2003, respectively.

Consumer Finance revenues in the first three months of 2004 increased. The increase in revenues in the first three months of 2004 was the result of growth in average finance receivables and credit quality continues to be strong. Further, reductions of the cost to borrow led to an improvement in the operating income over the previous year.

Financial Services Invested Assets

The following table is a summary of the composition of AIG's Financial Services invested assets at March 31, 2004 and December 31, 2003. (See also the discussions under "Operating Review: Financial Services Operations," "Capital Resources" and "Derivatives" herein.)

| (dollars in millions) | 2004 | | 2003 | |
|---|-------------------|------------------|-------------------|------------------|
| | Invested Assets | Percent of Total | Invested Assets | Percent of Total |
| Flight equipment primarily under operating leases, net of accumulated depreciation | \$ 30,807 | 23.8% | \$ 30,343 | 23.9% |
| Finance receivables, net of allowance | 18,494 | 14.3 | 17,609 | 13.9 |
| Unrealized gain on interest rate and currency swaps, options and forward transactions | 21,452 | 16.6 | 21,599 | 17.0 |
| Securities available for sale, at market value | 17,930 | 13.9 | 15,714 | 12.4 |
| Trading securities, at market value | 4,877 | 3.8 | 3,300 | 2.6 |
| Securities purchased under agreements to resell, at contract value | 26,347 | 20.4 | 28,144 | 22.2 |
| Trading assets | 1,886 | 1.5 | 2,548 | 2.0 |
| Spot commodities, at market value | 183 | 0.1 | 250 | 0.2 |
| Other, including short-term investments | 7,405 | 5.6 | 7,392 | 5.8 |
| Total | \$ 129,381 | 100.0% | \$ 126,899 | 100.0% |

As previously discussed, the cash used for the purchase of flight equipment is derived primarily from the proceeds of ILFC's debt financings. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. During the first three months of 2004, ILFC acquired flight equipment costing \$1.84 billion. (See also the discussion under "Operating Review: Financial Services Operations" and "Capital Resources" herein.)

AIG's Consumer Finance operations provide a wide variety of consumer finance products both domestically and overseas. Such products include real estate mortgages, consumer loans, and retail sales finance. These products are funded through various borrowings including commercial paper and medium term notes. AIG's Consumer Finance operations are exposed to credit risk and risk of loss resulting from adverse fluctuations in interest rates. Over half of the loan balance is related to real estate loans which are substantially collateralized by the related properties.

With respect to credit losses, the allowance for finance receivable losses is maintained at a level considered adequate to absorb anticipated credit losses existing in that portfolio.

Capital Markets derivative transactions are carried at market value or at estimated fair value when market prices are not readily available. AIGFP reduces its economic risk exposure through similarly valued offsetting transactions including swaps, trading securities, options, forwards and futures. The estimated fair values of these transactions represent assessments of the present value of expected future cash flows. These transactions are exposed to liquidity risk if AIGFP were required to sell or close out the transactions prior to maturity. AIG believes that the impact of any such limited liquidity would not be significant to AIG's financial condition or its overall liquidity. (See also the discussion under "Operating Review: Financial Services Operations" and "Derivatives" herein.)

AIGFP uses the proceeds from the issuance of notes and bonds and GIA borrowings to invest in a diversified portfolio of securities, including securities available for sale, at market, and derivative transactions. The funds may also be temporarily invested in securities purchased under agreements to resell. The proceeds from the disposal of the aforementioned securities available for sale and securities purchased under agreements to resell have been used to fund the maturing GIAs or other AIGFP financings. (See also the discussion under "Capital Resources" herein.)

Securities available for sale is mainly a portfolio of debt securities, where the individual securities have varying degrees of credit risk. At March 31, 2004, the average credit rating of this portfolio was AA or the equivalent thereto as determined through rating agencies or internal review. AIGFP has also entered into credit derivative transactions to hedge its credit risk associated with \$218 million of these securities. Securities deemed below investment grade at March 31, 2004 amounted to approximately \$98 million in fair value representing 0.6 of one percent of the total AIGFP securities available for sale. \$30 million of this amount is hedged with a credit derivative. There have been no significant downgrades through May 1, 2004.

AIGFP's risk management objective is to minimize interest rate, equity and currency risks associated with its securities available for sale. That is, when AIGFP purchases a security for its securities available for sale investment portfolio, it simultaneously enters into an offsetting fair value hedge such that the payment terms of the hedging transaction exactly offset the payment terms of the investment security. As a result of the hedging transaction, the holder of the investment security pays the return on the underlying security and receives overnight USD LIBOR plus or minus a spread based on the underlying profit on each security on the initial trade date.

The unrealized gains or losses that inure to the security from movements in interest rates, currency rates, or equity prices and the change in value of the related hedging transaction are recorded in operating income currently. The unrealized gain or loss that relates to the change in the un-hedged risk (credit spreads) with respect to these investments is recorded in shareholders' equity, net of tax. When a security is sold, the related hedging transaction is also terminated. The realized gain or loss with respect to each security and its related hedge are recorded in operating income.

Securities purchased under agreements to resell are treated as collateralized transactions. AIGFP takes possession of or obtains a security interest in securities purchased under agreements to resell. AIGFP further minimizes its credit risk by monitoring counterparty credit exposure and, when AIGFP deems necessary, it requires additional collateral to be deposited. Trading securities, at market value are marked to market daily and are held to meet the short-term risk management objectives of AIGFP.

AIGFP is exposed to credit risk. If its securities available for sale portfolio were to suffer significant default and the collateral held declined significantly in value with no replacement or the credit default swap counterparty failed to perform, AIGFP could have a liquidity strain. AIG guarantees AIGFP's debt and, as a result, is responsible for all of AIGFP's obligations.

AIGTG conducts, as principal, market making and trading activities in foreign exchange, and commodities, primarily precious and base metals. AIGTG owns inventories in the commodities in which it trades and may reduce the exposure to market risk through the use of swaps, forwards, futures and option contracts. AIGTG uses derivatives to manage the economic exposure of its various trading positions and transactions from adverse movements of interest rates, foreign currency exchange rates and commodity prices. AIGTG supports its trading activities largely through trading liabilities, unrealized losses on swaps, short-term borrowings, securities sold under agreements to repurchase and securities and commodities sold but not yet purchased. (See also the discussions under "Capital Resources.")

The gross unrealized gains and gross unrealized losses of Capital Markets included in the financial services assets and liabilities at March 31, 2004 were as follows:

| <i>(in millions)</i> | Gross Unrealized Gains | Gross Unrealized Losses |
|--|---------------------------------------|--|
| Securities available for sale, at market value | \$ 2,273 | \$ 2,283 |
| Unrealized gain/ loss on interest rate and currency swaps, options and forward transactions ^(a) | 21,452 | 15,731 |
| Trading assets | 8,960 | 7,059 |
| Spot commodities, at market value | - | 13 |
| Trading liabilities | - | 1,015 |
| Securities and spot commodities sold but not yet purchased, at market value | - | 722 |

(a) These amounts are also presented as the respective balance sheet amounts.

AIGFP's interest rate and currency risks on securities available for sale, at market, are managed by taking offsetting positions on a security by security basis, thereby offsetting a significant portion of the unrealized appreciation or depreciation. At March 31, 2004, the unrealized gains and losses remaining after the benefit of the offsets were \$48 million and \$58 million, respectively.

Trading securities, at market value, and securities and spot commodities sold but not yet purchased, at market value are marked to market daily with the unrealized gain or loss being recognized in income at that time. These securities are held to meet the short-term risk management objectives of Capital Markets operations.

The senior management of AIG defines the policies and establishes general operating parameters for Capital Markets operations. AIG's senior management has established various oversight committees to review the various financial market, operational and credit issues of the Capital Markets operations. The senior management of AIGFP reports the results of its operations to and reviews future strategies with AIG's senior management.

AIG actively manages the exposures to limit potential losses, while maximizing the rewards afforded by these business opportunities. In doing so, AIG must continually manage a variety of exposures including credit, market, liquidity, operational and legal risks.

Asset Management Operations

AIG's Asset Management operations offer a variety of investment related services and investment products, including mutual funds' management, investment asset management and the sale of guaranteed investment contracts, also known as funding agreements (GICs). Such services and products are offered to individuals and institutions both domestically and overseas.

AIG's principal Asset Management operations are conducted through AIG SunAmerica and AIG Global Investment Group. AIG SunAmerica sells and manages mutual funds and provides financial services. AIG Global Investment Group manages invested assets on a global basis and third-party institutional, retail and private equity funds, provides securities lending and custodial services and organizes and manages the invested assets of institutional private equity investment funds. Each of these subsidiary operations receives fees for investment products and services provided.

As previously stated, AIG has reformatted its presentation from Retirement Services and Asset Management to Asset Management. Included in Asset Management are the results of AIG's asset management and brokerage services operations, mutual fund operations and the foreign and domestic guaranteed investment contract operations.

Asset Management revenues and operating income for the three month periods ending March 31, 2004 and 2003 were as follows:

| <i>(in millions)</i> | 2004 | 2003 |
|-------------------------------------|---------------|---------------|
| Revenues: | | |
| Guaranteed investment contracts | \$ 660 | \$ 625 |
| Institutional Asset Management* | 189 | 155 |
| Brokerage Services and Mutual Funds | 60 | 48 |
| Total | \$ 909 | \$ 828 |
| Operating income: | | |
| Guaranteed investment contracts | \$ 157 | \$ 119 |
| Institutional Asset Management* | 62 | 44 |
| Brokerage Services and Mutual Funds | 20 | 12 |
| Total | \$ 239 | \$ 175 |

* Includes AIG Global Investment Group and certain smaller asset management operations.

Asset Management Results

Asset Management operating income increased in the first three months of 2004 compared to the same period of 2003 as a result of the upturn in worldwide financial markets and a strong global product portfolio. The operating income growth results from fees related to the management of mutual funds and various investment portfolios that are in great part contingent upon the growth in the equity markets and customer interest in equity sensitive products. Thus, as equity markets expand and contract, the appetite for private equity investment changes, and the revenues and operating income with respect to the asset management portion of this segment can be expected to be similarly affected. Guaranteed investment contracts, also known as funding agreements (GICs), are sold domestically and abroad to both institutions and individuals. These products are written on an opportunistic basis when market conditions are favorable. Thus, revenues, operating income and cash flow attributable to GICs will vary from one reporting period to the next.

Asset Management operating income represented 5.6 percent of AIG's consolidated income before income taxes, minority interest and cumulative effect of an accounting change in the first three months of 2004. This compares to 6.0 percent in the same period of 2003.

At March 31, 2004, AIG's third party assets under management, including both retail mutual funds and institutional accounts, approximated \$48 billion and the aggregate GIC reserve was \$48.4 billion.

Other Operations

Other income (deductions) – net includes partnership income generated by the investment of capital held by AIG SunAmerica, AIG's equity in certain minor majority-owned subsidiaries and certain partially owned companies, realized foreign exchange transaction gains and losses in substantially all currencies and unrealized gains and losses in hyperinflationary currencies, as well as the income and expenses of the parent holding company and other miscellaneous income and expenses. Other income (deductions) – net amounted to \$(20) million and \$(114) million in the first three months of 2004 and 2003, respectively. The improvement in the first three months of 2004 compared to the same period of 2003 was primarily the result of stronger performance of AIG SunAmerica investments in partnerships.

Capital Resources

At March 31, 2004, AIG had total shareholders' equity of \$76.78 billion and total borrowings of \$80.91 billion. At that date, \$72.09 billion of such borrowings were either not guaranteed by AIG or were AIGFP's matched borrowings under obligations of guaranteed investment agreements (GIAs) or matched notes and bonds payable.

Borrowings

At March 31, 2004, AIG's net borrowings were \$8.82 billion after reflecting amounts that were matched borrowings under AIGFP's obligations of GIAs and matched notes and bonds payable and amounts not guaranteed by AIG. The following table summarizes borrowings outstanding at March 31, 2004 and December 31, 2003:

(in millions)

2004

2003

| | 2004 | 2003 |
|----------------------------------|-----------|-----------|
| AIG's net borrowings | \$ 8,815 | \$ 7,650 |
| AIGF P | | |
| GIAs | 15,414 | 15,337 |
| Matched notes and bonds payable | 16,320 | 15,289 |
| Borrowings not guaranteed by AIG | 40,359 | 39,002 |
| Total | \$ 80,908 | \$ 77,278 |

Borrowings issued or guaranteed by AIG and those borrowings not guaranteed by AIG at March 31, 2004 and December 31, 2003 were as follows:

| <i>(in millions)</i> | 2004 | 2003 |
|---|------------------|------------------|
| AIG borrowings: | | |
| Medium term notes | \$ 767 | \$ 791 |
| Notes and bonds payable | 3,150 | 3,141 |
| Loans and mortgages payable | 336 | 337 |
| Total | 4,253 | 4,269 |
| Borrowings guaranteed by AIG: | | |
| AIGFP | | |
| GIAs | 15,414 | 15,337 |
| Notes and bonds payable | 17,268 | 16,203 |
| Total | 32,682 | 31,540 |
| AIG Funding, Inc. commercial paper | 2,519 | 1,223 |
| AGC Notes and bonds payable | 1,095 | 1,244 |
| Total borrowings issued or guaranteed by AIG | 40,549 | 38,276 |
| Borrowings not guaranteed by AIG: | | |
| ILFC | | |
| Commercial paper | 1,854 | 1,575 |
| Medium term notes | 5,965 | 5,960 |
| Notes and bonds payable ^(a) | 14,795 | 14,431 |
| Loans and mortgages payable ^(b) | 125 | 143 |
| Total | 22,739 | 22,109 |
| AGF | | |
| Commercial paper | 3,202 | 2,877 |
| Medium term notes | 10,082 | 9,714 |
| Notes and bonds payable | 1,723 | 1,739 |
| Total | 15,007 | 14,330 |
| Commercial paper: | | |
| AIG Credit Card Company (Taiwan) | 229 | 250 |
| AIG Finance (Taiwan) Limited | 9 | 13 |
| Total | 238 | 263 |
| Loans and mortgages payable: | | |
| AIGCFG | 616 | 624 |
| AIG Finance (Hong Kong) Limited | 119 | 165 |
| Total | 735 | 789 |
| Other Subsidiaries | 870 | 727 |
| Variable Interest Entity debt: | | |
| ILFC | 459 | 464 |
| AIG Global Investment Group | - | 6 |
| AIG Capital Partners | 145 | 148 |
| AIG SunAmerica | 166 | 166 |
| Total | 770 | 784 |
| Total borrowings not guaranteed by AIG | 40,359 | 39,002 |
| Total Borrowings | \$ 80,908 | \$ 77,278 |

*(a) Includes borrowings under Export Credit Facility of \$1.7 billion.**(b) Capital lease obligations.*

AIGFP uses the proceeds from the issuance of notes and bonds and GIA borrowings to invest in a diversified portfolio of securities and derivative transactions. The borrowings may also be temporarily invested in securities purchased under agreements to resell. (See also the discussions under “Operating Review,” “Liquidity” and “Derivatives” herein.)

AIG Funding, Inc. (Funding), through the issuance of commercial paper, helps fulfill the short-term cash requirements of AIG and its subsidiaries. Funding intends to continue to meet AIG’s funding requirements through the issuance of commercial paper guaranteed by AIG. The issuance of Funding’s commercial paper is subject to the approval of AIG’s Board of Directors.

ILFC and AGF as well as AIG Credit Card Company (Taiwan) – (AIGCCC-Taiwan) and AIG Finance (Taiwan) Limited – (AIGF-Taiwan), both consumer finance subsidiaries in Taiwan, have issued commercial paper for the funding of their own operations. At March 31, 2004, AIG did not guarantee the commercial paper of any of its subsidiaries other than Funding. (See also the discussion under “Derivatives” herein.)

AIG and Funding are parties to unsecured syndicated revolving credit facilities (collectively, the Facility) aggregating \$2.75 billion. The Facility consists of \$1.375 billion in a short-term revolving credit facility and \$1.375 billion in a five year revolving credit facility. The Facility can be used for general corporate purposes and also to provide backup for Funding’s commercial paper programs. There are currently no borrowings outstanding under the Facility, nor were any borrowings outstanding as of March 31, 2004.

AGF is a party to unsecured syndicated revolving credit facilities aggregating \$3.0 billion. The facilities consist of \$1.5 billion in a short-term revolving credit facility and \$1.5 billion in a five year revolving credit facility, which support AGF’s commercial paper borrowings. There are currently no borrowings under these facilities, nor were any borrowings outstanding as of March 31, 2004. AGF had \$8.3 billion in aggregate principal amount of debt securities registered and available for issuance at March 31, 2004. AGF uses the proceeds from the issuance of notes and bonds for the funding of its finance receivables.

Proceeds from the collection of finance receivables will be used to pay the principal and interest with respect to AGF’s debt.

ILFC is a party to unsecured syndicated revolving credit facilities aggregating \$4.2 billion at March 31, 2004. The facilities are used to support ILFC’s maturing debt and other obligations and consist of \$3.15 billion in a short-term revolving credit facility and \$1.05 billion in a three year revolving credit facility. There are currently no borrowings under these facilities, nor were any borrowings outstanding as of March 31, 2004.

At March 31, 2004, ILFC had increased the aggregate principal amount outstanding of its medium term and long-term notes including \$823 million resulting from foreign exchange translation. ILFC had \$11.08 billion of debt securities registered for public sale at March 31, 2004. As of March 31, 2004, \$6.95 billion of debt securities were issued. In addition, ILFC has a Euro Medium Term Note Program for \$5.0 billion, under which \$3.39 billion in notes were sold through March 31, 2004. ILFC has substantially eliminated the cur-

rency exposure arising from foreign currency denominated notes by either hedging the notes through swaps or through the offset provided by operating lease payments. Notes issued under this program are included in Notes and Bonds Payable in the preceding table of borrowings.

ILFC had a \$4.3 billion Export Credit Facility for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.90 percent on these borrowings depending on the delivery date of the aircraft. At March 31, 2004, ILFC had \$1.7 billion outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility. Borrowings with respect to this facility are included in Notes and Bonds Payable in the preceding table of borrowings. During 2003, ILFC entered into various bank financings for a total funded amount of \$1.3 billion. The financings mature through 2009. One tranche of one of the loans totaling \$410 million was funded in Japanese yen and swapped to U.S. dollars.

The proceeds of ILFC's debt financing are primarily used to purchase flight equipment, including progress payments during the construction phase. The primary sources for the repayment of this debt and the interest expense thereon are the cash flow from operations, proceeds from the sale of flight equipment and the rollover and refinancing of the prior debt. (See also the discussions under "Operating Review" and "Liquidity" herein.)

AIGFP has established a Euro Medium Term Note Program under which an aggregate principal amount of up to \$4.0 billion of notes may be outstanding. As of March 31, 2004, \$5.34 billion of notes had been issued under the program, \$3.43 billion of which were outstanding. Notes issued under this program are included in Notes and Bonds Payable in the preceding table of borrowings.

During the first three months of 2004, AIG did not issue any medium term notes, and \$24 million of previously issued notes matured or were redeemed. At March 31, 2004, AIG had \$140 million in aggregate principal amount of debt securities registered for issuance from time to time. AIG has filed a universal shelf registration statement to sell up to \$5.1 billion of debt securities, preferred and common stock and other securities. AIG has no current plans to issue the equity, equity-linked or capital securities included in the registration statement, but intends to continue its customary practice of issuing securities from time to time for general corporate purposes.

On November 9, 2001, AIG received proceeds of approximately \$1 billion from the issuance of Zero Coupon Convertible Senior Debentures Due 2031 with an aggregate principal amount at maturity of approximately \$1.52 billion. Commencing January 1, 2002, the debentures are convertible into shares of AIG common stock at a conversion rate of 6.0627 shares per \$1,000 principal amount of debentures if AIG common stock trades at certain levels for certain time periods. The debentures are callable by AIG on or after November 9, 2006. Also, holders can require AIG to repurchase these debentures once every five years beginning on November 9, 2006.

As of November 2001, AIG guaranteed the notes and bonds of AGC. During 2002, AGC issued \$200 million in notes which matured in March 2003.

Shareholders' Equity

AIG's shareholders' equity increased \$5.53 billion during the first three months of 2004. During the first three months of 2004, retained earnings increased \$2.49 billion, resulting from net income less dividends. Unrealized appreciation of investments, net of taxes increased \$2.93 billion and the cumulative translation adjustment loss, net of taxes, decreased \$125 million. The change from period to period with respect to the unrealized appreciation of investments, net of taxes, was primarily impacted by the decrease in domestic interest rates. During the first three months of 2004, there was a gain of \$44 million, net of taxes relating to derivative contracts designated as cash flow hedging instruments. (See also the discussion under "Operating Review" and "Liquidity" herein and the Consolidated Statement of Comprehensive Income.)

AIG has in the past reinvested most of its unrestricted earnings in its operations and believes such continued reinvestment in the future will be adequate to meet any foreseeable capital needs. However, AIG may choose from time to time to raise additional funds through the issuance of additional securities.

Stock Repurchase

During the period January 1, 2004 through March 31, 2004, AIG repurchased in the open market 1,313,300 shares of its common stock. AIG from time to time may buy its common shares in the open market for general corporate purposes, including to satisfy its obligations under various employee benefit plans.

Dividends from Insurance Subsidiaries

Payments of dividends to AIG by its insurance subsidiaries are subject to certain restrictions imposed by statutory authorities. With respect to AIG's domestic insurance subsidiaries, specifically the payment of any dividend requires formal notice to the insurance department in which the particular insurance subsidiary is domiciled. Under the laws of many states, an insurer may pay a dividend without prior approval of the insurance regulator when the amount of the dividend is below certain materiality thresholds.

With respect to AIG's foreign insurance subsidiaries, the most significant insurance regulatory jurisdictions include Bermuda, Japan, Hong Kong and the Republic of China.

At March 31, 2004, there were no significant statutory or regulatory issues which would impair AIG's financial condition, results of operations or liquidity, but there can be no assurance that such issues will not arise in the future. To AIG's knowledge, no AIG company is on any regulatory or similar "watch list." (See also the discussion under "Liquidity" herein.)

Regulation and Supervision

AIG's insurance subsidiaries, in common with other insurers, are subject to regulation and supervision by the states and jurisdictions in which they do business. The National Association of Insurance Commissioners (NAIC) has developed Risk-Based Capital (RBC) requirements. RBC relates an individual insurance company's statutory surplus to the risk inherent in its overall operations. At March 31, 2004, the risk-based adjusted surplus of each of AIG's domestic general companies and of each of AIG's domestic life companies exceeded each of their RBC standards. Federal, state or local legislation may affect AIG's ability to operate and expand its various financial services businesses and changes in the current laws, regulations or interpretations thereof may have a material adverse effect on these businesses.

AIG's operations are negatively impacted under guarantee fund assessment laws which exist in most states. As a result of operating in a state which has guarantee fund assessment laws, a solvent insurance company may be assessed for certain obligations arising from the insolvencies of other insurance companies which operated in that state. AIG generally records these assessments upon notice. Additionally, certain states permit at least a portion of the assessed amount to be used as a credit against a company's future premium tax liabilities. Therefore, the ultimate net assessment cannot reasonably be estimated. The guarantee fund assessments net of credits for 2003 were \$77 million. Based upon current information, AIG does not anticipate that its net assessment will be significantly different during 2004.

AIG is also required to participate in various involuntary pools (principally workers' compensation business) which provide insurance coverage for those not able to obtain such coverage in the voluntary markets. This participation is also recorded upon notification, as these amounts cannot reasonably be estimated.

A substantial portion of AIG's General Insurance business and a majority of its Life Insurance & Retirement Services business are conducted in foreign countries. The degree of regulation and supervision in foreign jurisdictions varies from minimal in some to stringent in others. Generally, AIG, as well as the underwriting companies operating in such jurisdictions, must satisfy local regulatory requirements. Licenses issued by foreign authorities to AIG subsidiaries are subject to modification and revocation. Thus, AIG's insurance subsidiaries could be prevented from conducting future business in certain of the jurisdictions where they currently operate. AIG's international operations include operations in various developing nations. Both current and future foreign operations could be adversely affected by unfavorable political developments up to and including nationalization of AIG's operations without compensation. Adverse effects resulting from any one country may impact AIG's results of operations, liquidity and financial condition depending on the magnitude of the event and AIG's net financial exposure at that time in that country.

Contractual Obligations and Other

Commercial Commitments

The maturity schedule of AIG's contractual obligations at March 31, 2004 was as follows:

(in millions)

| | Total Payments | Payments due by Period | | | |
|-------------------------------|-------------------|-----------------------------|----------------------------------|----------------------------------|------------------------|
| | | Less Than One Year | One Through Three Years | Four Through Five Years | After Five Years |
| Borrowings* | \$ 72,325 | \$20,854 | \$ 15,609 | \$ 10,762 | \$25,100 |
| Aircraft purchase commitments | 24,511 | 3,172 | 10,115 | 8,810 | 2,414 |
| Total | \$ 96,836 | \$24,026 | \$ 25,724 | \$ 19,572 | \$27,514 |

* Excludes commercial paper and obligations included as debt pursuant to FIN 46R and includes ILFC's capital lease obligations.

The maturity schedule of AIG's other commercial commitments by segment at March 31, 2004 was as follows:*(in millions)*

| | Total Amounts Committed | Amount of Commitment Expiration | | | |
|---|-------------------------------|---------------------------------|----------------------------------|----------------------------------|------------------------|
| | | Less Than One Year | One Through Three Years | Four Through Five Years | After Five Years |
| Letters of credit: | | | | | |
| Life Insurance & Retirement Services | \$ 140 | \$ 110 | \$ – | \$ – | \$ 30 |
| DBG | 212 | 111 | 101 | – | – |
| Standby letters of credit: | | | | | |
| Capital Markets | 1,619 | 53 | 11 | 16 | 1,539 |
| Guarantees: | | | | | |
| Life Insurance & Retirement Services | 3,221 | 177 | 2,173 | 369 | 502 |
| Asset Management | 150 | 83 | 56 | 11 | – |
| Other commercial commitments ^(a) : | | | | | |
| Capital Markets ^(b) | 15,529 | 190 | 1,394 | 2,510 | 11,435 |
| Aircraft Finance ^(c) | 1,446 | – | 597 | 411 | 438 |
| Life Insurance & Retirement Services | 2,359 | 384 | 1,079 | 122 | 774 |
| Asset Management | 2,956 | 2,756 | 118 | – | 82 |
| DBG | 1,940 | – | – | – | 1,940 |
| Total | \$ 29,572 | \$ 3,864 | \$ 5,529 | \$ 3,439 | \$ 16,740 |

*(a) Excludes commitments with respect to pension plans.**(b) Primarily liquidity facilities provided in connection with certain municipal swap transactions.**(c) Primarily in connection with options to acquire aircraft.*

AIG and its subsidiaries do not have any contractual obligations that are subject to “ratings triggers” or financial covenants relating to “ratings triggers” which AIG believes could have a material adverse effect on its financial condition, future operating results or liquidity. “Rating triggers” have been defined by one independent rating agency to include clauses or agreements the outcome of which depends upon the level of ratings maintained by one or more rating agencies. Rating triggers generally relate to events which (i) could result in the termination or limitation of credit availability, or require accelerated repayment, (ii) could result in the termination of business contracts or (iii) could require a company to post collateral for the benefit of counterparties.

Special Purpose Vehicles and Off Balance Sheet Arrangements

AIG uses special purpose vehicles (SPVs) and off balance sheet arrangements in the ordinary course of business. As a result of recent changes in accounting, a number of SPVs and off balance sheet arrangements have been reflected in AIG's consolidated financial statements. In January 2003, FASB issued Interpretation No. 46, “Consolidation of Variable Interest Entities” (FIN 46). FIN 46 addressed the consolidation and disclosure rules for nonoperating entities that are now defined as Variable Interest Entities (VIEs). In December 2003, FASB issued a revision to Interpretation No. 46 (FIN 46R). In November 2002, FASB issued Interpretation No. 45 “Guarantors’ Accounting And Disclosure Requirements for Guarantees, including Indirect Guarantees of Indebtedness of Others” (FIN 45). For additional information related to AIG's activities with respect to VIEs and certain guarantees see Note 7 of Notes to Financial Statements and also Note 20 of Notes to Financial Statements in AIG's December 31, 2003 10-K. Also, for additional disclosure regarding AIG's commercial commitments (including guarantors), see “Contractual Obligations and Other Commercial Commitments” herein.

AIG has restrictive guidelines with respect to the formation of and investment in SPVs and off balance sheet arrangements.

Liquidity

AIG's liquidity is primarily derived from the operating cash flows of its General and Life Insurance & Retirement Services operations.

At March 31, 2004, AIG's consolidated invested assets included \$18.70 billion of cash and short-term investments. Consolidated net cash provided from operating activities in the first three months of 2004 amounted to \$9.22 billion.

Sources of funds considered in meeting the objectives of AIG's Financial Services operations include guaranteed investment agreements, issuance of long-term and short-term debt, maturities and sales of securities available for sale, securities sold under repurchase agreements, trading liabilities, securities and spot commodities sold but not yet purchased, issuance of equity, and cash provided from such operations. AIG's strong capital position and superior credit ratings are integral to managing this liquidity, as they enable AIG to raise funds in diverse markets worldwide. (See also the discussion under “Capital Resources” herein.)

Management believes that AIG's liquid assets, its net cash provided by operations, and access to the capital markets will enable it to meet any foreseeable cash requirements.

The liquidity of the combined insurance operations is derived both domestically and abroad. The combined insurance operating cash flow is derived from two sources, underwriting operations and investment operations. In the aggregate, AIG's insurance operations generated approximately \$17.2 billion in pretax cash flow during the first three months of 2004. Cash flow includes periodic premium collections, including policyholders' contract deposits, cash flows from investment operations and paid loss recoveries less reinsurance premiums, losses, benefits, and acquisition and operating expenses. Generally, there is a time lag from when premiums are collected and, when as a result of the occurrence of events specified in the policy, the losses and benefits are paid. AIG's insurance investment operations generated approximately \$4.5 billion in investment income cash flow during the first three months of 2004. Investment income cash flow is primarily derived from interest and dividends received and includes realized capital gains net of realized capital losses. (See also the discussions under "Operating Review: General Insurance Operations" and "Life Insurance & Retirement Services Operations" herein.)

With respect to General Insurance operations, if paid losses accelerated beyond AIG's ability to fund such paid losses from current operating cash flows, AIG might need to liquidate a portion of its General Insurance investment portfolio and/or arrange for financing. Potential events causing such a liquidity strain could be the result of several significant catastrophic events occurring in a relatively short period of time. Additional strain on liquidity could occur if the investments sold to fund such paid losses were sold into a depressed market place and/or reinsurance recoverable on such paid losses became uncollectible or collateral supporting such reinsurance recoverable significantly decreased in value. (See also the discussions under "Operating Review: General Insurance Operations" herein.)

With respect to Life Insurance & Retirement Services operations, if a substantial portion of the Life Insurance & Retirement Services operations bond portfolio diminished significantly in value and/or defaulted, AIG might need to liquidate other portions of its Life Insurance & Retirement Services investment portfolio and/or arrange financing. Potential events causing such a liquidity strain could be the result of economic collapse of a nation or region in which AIG Life Insurance & Retirement Services operations exist, nationalization, terrorist acts or other such economic or political upheaval. (See also the discussions under "Operating Review: Life Insurance & Retirement Services Operations" herein.)

In addition to the combined insurance pretax operating cash flow, AIG's insurance operations held \$17.08 billion in cash and short-term investments at March 31, 2004. Operating cash flow and the cash and short-term balances held provided AIG's insurance operations with a significant amount of liquidity.

This liquidity is available, among other things, to purchase predominately high quality and diversified fixed income securities and, to a lesser extent, marketable equity securities, and to provide mortgage loans on real estate, policy loans and collateral loans. This cash flow coupled with proceeds of approximately \$38 billion from the maturities, sales and redemptions of fixed income securities and from the sale of equity securities was used to purchase approximately \$54 billion of fixed income securities and marketable equity securities during the first three months of 2004.

Managing Market Risk

Insurance

AIG's insurance operations are exposed to market risk. Market risk is the risk of loss of fair value resulting from adverse fluctuations in interest and foreign currency exchange rates and equity prices.

Measuring potential losses in fair values is performed through the application of various statistical techniques. One such technique is Value at Risk (VaR). VaR is a summary statistical measure that uses historical interest and foreign currency exchange rates and equity prices and estimates the volatility and correlation of each of these rates and prices to calculate the maximum loss that could occur over a defined period of time given a certain probability.

AIG believes that statistical models alone do not provide a reliable method of monitoring and controlling market risk. While VaR models are relatively sophisticated, the quantitative market risk information generated is limited by the assumptions and parameters established in creating the related models. Therefore, such models are tools and do not substitute for the experience or judgment of senior management.

AIG has performed a VaR analysis to estimate the maximum potential loss of fair value for each of AIG's insurance segments and for each market risk within each insurance segment. In this analysis, financial instrument assets include the domestic and foreign invested assets excluding real estate and investment income due and accrued. Financial instrument liabilities include reserve for losses and loss expenses, reserve for unearned premiums, future policy benefits for life and accident and health insurance contracts and policyholders' funds.

Due to the nature of each insurance segment, AIG manages the General and Life Insurance & Retirement Services operations separately. As a result, AIG manages separately the invested assets of each. Accordingly, the VaR analysis was separately performed for the General and the Life Insurance & Retirement Services operations.

AIG calculated the VaR with respect to the net fair value of each of AIG's insurance segments as of March 31, 2004 and December 31, 2003. AIG uses the historical simulation methodology which entails repricing all assets and liabilities under explicit changes in market rates within a specific historical time period. In this case, the most recent three years of historical market information for interest rates, foreign exchange rates, and equity index prices were used to construct the historical scenarios. For each scenario, each transaction was repriced. Portfolio, business unit and finally AIG-wide scenario values were then calculated by netting the values of all the underlying assets and liabilities. The final VaR number represents the maximum potential loss incurred by these scenarios with 95 percent confidence (i.e., only 5 percent of historical scenarios show losses greater than the VaR figure). A one month holding period was assumed in computing the VaR figure.

The following table presents the VaR on a combined basis and of each component of market risk for each of AIG's insurance segments as of March 31, 2004 and December 31, 2003. VaR with respect to combined operations cannot be derived by aggregating the individual risk or segment amounts presented herein.

| (in millions) | General Insurance | | Life Insurance & Retirement Services | |
|---------------|-------------------|----------|--------------------------------------|----------|
| | 2004 | 2003 | 2004 | 2003 |
| Market risk: | | | | |
| Combined | \$ 1,101 | \$ 1,100 | \$ 3,226 | \$ 3,075 |
| Interest rate | 1,223 | 1,173 | 3,007 | 2,967 |
| Currency | 91 | 125 | 305 | 257 |
| Equity | 775 | 797 | 832 | 758 |

The following table presents the average, high and low VaRs on a combined basis and of each component of market risk for each of AIG's insurance segments as of March 31, 2004 and December 31, 2003.

| (in millions) | 2004 | | | 2003 | | |
|---------------------------------------|----------|----------|----------|----------|----------|----------|
| | Average | High | Low | Average | High | Low |
| General Insurance: | | | | | | |
| Market risk: | | | | | | |
| Combined | \$ 1,101 | \$ 1,101 | \$ 1,100 | \$ 888 | \$ 1,120 | \$ 658 |
| Interest rate | 1,198 | 1,223 | 1,173 | 732 | 1,173 | 411 |
| Currency | 108 | 125 | 91 | 94 | 147 | 64 |
| Equity | 786 | 797 | 775 | 781 | 935 | 631 |
| Life Insurance & Retirement Services: | | | | | | |
| Market risk: | | | | | | |
| Combined | \$ 3,151 | \$ 3,226 | \$ 3,075 | \$ 2,262 | \$ 3,419 | \$ 1,299 |
| Interest rate | 2,987 | 3,007 | 2,967 | 2,207 | 3,347 | 1,376 |
| Currency | 281 | 305 | 257 | 204 | 257 | 166 |
| Equity | 795 | 832 | 758 | 762 | 975 | 627 |

Financial Services

Market risk arises principally from the uncertainty that future earnings are exposed to potential changes in volatility, interest rates, foreign currency exchange rates, and equity and commodity prices. AIG generally controls its exposure to market risk by taking offsetting positions. AIG's philosophy with respect to its Capital Markets operations is to minimize or set limits for open or uncovered positions that are to be carried. Credit risk exposure is separately managed. (See the discussion on the management of credit risk below.)

AIG's Market Risk Management Department provides detailed independent review of AIG's market exposures, particularly those market exposures of the Capital Markets operations. This department determines whether AIG's market risks, as well as those market risks of individual subsidiaries, are within the parameters established by AIG's senior management. Well established market risk management techniques such as sensitivity analysis are used. Additionally, this department verifies that specific market risks of each of certain subsidiaries are managed and hedged by that subsidiary.

ILFC is exposed to market risk and the risk of loss of fair value and possible liquidity strain resulting from adverse fluctuations in interest rates. As of March 31, 2004 and December 31, 2003, AIG statistically measured the loss of fair value through the application of a VaR model. In this analysis, the net fair value of Aircraft Finance operations was determined using the financial instrument assets which included the tax adjusted future flight equipment lease revenue and the financial instrument liabilities which included the future servicing of the current debt. The estimated impact of the current derivative positions was also taken into account.

AIG calculated the VaR with respect to the net fair value of Aircraft Finance operations using the historical simulation methodology, as previously described. As of March 31, 2004 and December 31, 2003, the average VaR with respect to the net fair value of Aircraft Finance operations was approximately \$43 million and \$38 million, respectively.

Capital Markets operations are exposed to market risk due to changes in the level and volatility of interest rates, foreign currency exchange rates, equity prices and commodity prices. AIGFP and AIGTG hedge their exposure to these

risks primarily through swaps, options, forwards and futures. To hedge interest rate risks, these subsidiaries may also purchase U.S. and foreign government obligations.

AIGFP and AIGTG do not seek to manage the market risk of each transaction through an individual offsetting transaction. Rather, these subsidiaries take a portfolio approach to the management of their market risk exposures. AIGFP and AIGTG value their entire portfolios of market-sensitive transactions at market value or at estimated fair value when market values are not readily available. Unrealized gains and losses, with respect to this portfolio are reflected in income currently. These valuations represent an assessment of the present values of expected future cash flows of Capital Markets transactions and may include reserves for such risks as are deemed appropriate by AIGFP and AIG's management.

Estimated fair values are based upon the use of valuation models. These models utilize, among other things, market liquidity and current interest, foreign exchange, equity, commodity and volatility rates. These valuation models are integrated into the evaluation of the portfolio, as described above, in order to provide timely information for the market risk management of the portfolio. Based upon this evaluation, AIGFP and AIGTG determines what, if any, offsetting transactions are necessary to reduce the market risk exposure of the portfolio.

AIGFP and AIGTG manage market risk with a variety of transactions, including swaps, trading securities, futures and forward contracts and other transactions as appropriate. The recorded values of these transactions may be different than the values that might be realized if these subsidiaries were required to sell or close out the transactions prior to maturity. AIG believes that such differences are not significant to the results of operations, financial condition or liquidity. Such differences would be immediately recognized when the transactions are sold or closed out prior to maturity.

AIGFP and AIGTG attempt to secure reliable and independent current market prices, such as published exchange prices, external subscription services such as from Bloomberg or Reuters or third party broker quotes for use in this model. When such prices are not available, these subsidiaries use an internal methodology which includes interpolation or extrapolation from observable and verifiable prices nearest to the dates of the transactions. Historically, actual results have not materially deviated from these models.

Systems used by Capital Markets operations can monitor each unit's respective market positions on an intraday basis. The subsidiaries operate in major business centers overseas and are essentially open for business 24 hours a day. Thus, the market exposure and offset strategies are monitored, reviewed and coordinated around the clock.

AIGFP and AIGTG apply various testing techniques which reflect significant potential market movements in interest rates, foreign exchange rates, commodity and equity prices, volatility levels and the effect of time. These techniques vary by currency and are regularly changed to reflect factors affecting the derivatives portfolio. The results from these analyses are regularly reviewed by senior management.

As described above, Capital Markets operations are exposed to the risk of loss of fair value from adverse fluctuations in interest rate and foreign currency exchange rates and equity and commodity prices. AIG statistically measured the losses of fair value through the application of a VaR model across both units.

Capital Markets asset and liability portfolios for which the VaR analyses were performed included over the counter and exchange traded investments, derivative instruments and commodities. Because the market risk with respect to securities available for sale, at market is substantially hedged, segregation of market sensitive instruments into trading and other than trading was not deemed necessary.

AIG calculated the VaR with respect to Capital Markets operations as of March 31, 2004 and December 31, 2003. AIG uses the historical simulation methodology which entails repricing all assets and liabilities under explicit changes in market rates within a specific historical time period. In this case, the most recent three years of historical market information for interest rates, foreign exchange rates, and equity index prices were used to construct the historical scenarios. For each scenario, each transaction was repriced. Portfolio, business unit and finally AIG-wide scenario values were then calculated by netting the values of all the underlying assets and liabilities. The final VaR number represents the maximum potential loss incurred by these scenarios with 95 percent confidence (i.e., only 5 percent of historical scenarios show losses greater than the VaR figure). A one-month holding period was assumed in computing the VaR figure.

The following table presents the VaR on a combined basis and of each component of Capital Markets risk as of March 31, 2004 and December 31, 2003. VaR with respect to combined operations cannot be derived by aggregating the individual risk presented herein.

| <i>(in millions)</i> | 2004 | 2003 |
|----------------------|------|------|
| Market risk: | | |
| Combined | \$ 9 | \$ 5 |
| Interest rate | 9 | 5 |
| Currency | 1 | 1 |
| Equity | 1 | 1 |

The following table presents the average, high and low VaRs on a combined basis and of each component of Capital Markets risk as of March 31, 2004 and December 31, 2003.

| (in millions) | 2004 | | | 2003 | | |
|---------------|---------|------|------|---------|------|------|
| | Average | High | Low | Average | High | Low |
| Combined | \$ 7 | \$ 9 | \$ 5 | \$ 5 | \$ 8 | \$ 4 |
| Interest rate | 7 | 9 | 5 | 5 | 9 | 3 |
| Currency | 1 | 1 | 1 | 1 | 1 | — |
| Equity | 1 | 1 | 1 | 1 | 1 | 1 |

Derivatives

Derivatives are financial arrangements among two or more parties. The returns of the derivatives are linked to or “derived” from some underlying equity, debt, commodity or other asset, liability, or index. Derivatives payments may be based on interest rates and exchange rates and/or prices of certain securities, certain commodities, or financial or commodity indices. The more significant types of derivative arrangements in which AIG transacts are swaps, forwards, futures and options. In the normal course of business, with the agreement of the original counterparty, these contracts may be terminated early or assigned to another counterparty.

The overwhelming majority of AIG’s derivatives activities are conducted by the Capital Markets operations, thus permitting AIG to participate in the derivatives dealer market acting primarily as principal. In these derivative operations, AIG structures agreements which generally allow its counterparties to enter into transactions with respect to changes in interest and exchange rates, securities’ prices and certain commodities and financial or commodity indices. AIG’s customers such as corporations, financial institutions, multinational organizations, sovereign entities, government agencies and municipalities use derivatives to hedge their own market exposures. For example, a futures, forward or option contract can be used to protect the customers’ assets or liabilities against price fluctuations.

A counterparty may default on any obligation to AIG, including a derivative contract. Credit risk is a consequence of extending credit and/or carrying trading and investment positions. Credit risk exists for a derivative contract when that contract has a positive fair value to AIG. To help manage this risk, the credit departments of AIGFP and AIGTG operate within the guidelines set by the AIG Credit Risk Committee. This committee establishes the credit policy, sets limits for counterparties and provides limits for derivative transactions with counterparties having different credit ratings. In addition to credit ratings, this committee takes into account other factors, including the industry and country of the counterparty. Transactions which fall outside these pre-established guidelines require the approval of the AIG Credit Risk Committee. It is also AIG’s policy to establish reserves for potential credit impairment when necessary.

AIG’s Derivatives Review Committee provides an independent review of any proposed derivative transaction. The committee examines, among other things, the nature and purpose of the derivative transaction, its potential credit exposure, if any, and the estimated benefits. This committee does not review those derivative transactions entered into by Capital Markets for their own accounts.

Generally, AIG conducts its businesses in the currencies of the local operating environment. Thus, exchange gains or losses occur when AIG’s foreign currency net investment is affected by changes in the foreign exchange rates relative to the U.S. dollar from one reporting period to the next.

Legal risk with respect to derivatives arises from the uncertainty of the enforceability, through legal or judicial processes, of the obligations of AIG’s clients and counterparties, including contractual provisions intended to reduce credit exposure by providing for the netting of mutual obligations. See also Note 21 of Notes to Financial Statements in AIG’s December 31, 2003 10-K for detailed information relating to Capital Markets derivative activities.

Recent Accounting Standards

In January 2003, FASB issued Interpretation No. 46, “Consolidation of Variable Interest Entities” (FIN 46). FIN 46 changes the method of determining whether certain entities should be consolidated in AIG’s consolidated financial statements. In December 2003, FASB issued a revision to Interpretation No. 46 (FIN 46R).

In July 2003, the American Institute of Certified Public Accountants issued Statement of Position 03-1, “Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts” (SOP 03-1). (For further discussion see Note 7 of Notes to Financial Statements.)

Controls and Procedures

AIG’s disclosure controls and procedures are designed to ensure that information required to be disclosed in the reports that AIG files or submits under the Securities Exchange Act of 1934, as amended (Exchange Act), is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission. Disclosure controls and procedures include controls and procedures designed to ensure that information required to be disclosed by AIG in the reports that it files or submits under the Exchange Act is accumulated and communicated to AIG’s management, including AIG’s Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. AIG’s management, with the participation of AIG’s Chief Executive Officer and the Chief Financial Officer, have evaluated the effectiveness of AIG’s disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation,

AIG's Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures provided reasonable assurance of effectiveness as of the end of the period covered by this report. In addition, there has been no change in AIG's internal control over financial reporting that occurred during the first fiscal quarter that has materially affected, or is reasonably likely to materially affect, AIG's internal control over financial reporting.

PART II – OTHER INFORMATION**ITEM 2. Changes in Securities, Use of Proceeds and Issuer Purchases of Equity Securities**

| Period | Total Number of Shares Purchased ⁽¹⁾⁽²⁾ | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs at End of Month ⁽³⁾ |
|-----------------------|--|------------------------------|--|---|
| January 1 - 31, 2004 | – | \$ – | – | 55,319,100 |
| February 1 - 29, 2004 | – | – | – | 55,319,100 |
| March 1 - 31, 2004 | 1,313,300 | 69.58 | 1,313,300 | 54,005,800 |
| Total | 1,313,300 | \$ 69.58 | 1,313,300 | |

(1) Does not include 15,132 shares delivered or attested to in satisfaction of the exercise price by holders of AIG employee stock options exercised during the three months ended March 31, 2004.

(2) Does not include 23,075 shares purchased by C.V. Starr & Co., Inc. at an average price of \$16.96 to satisfy obligations under its employee stock option and purchase plans.

(3) On July 19, 2002, AIG announced that its Board of Directors had authorized the open market purchase of up to 10 million shares of common stock. On February 13, 2003, AIG announced that the Board had expanded the existing program through the authorization of an additional 50 million shares. The purchase program has no set expiration or termination date.

ITEM 6. Exhibits and Reports on Form 8-K**(a) Exhibits**

See accompanying Exhibit Index.

(b) Reports on Form 8-K

During the three months ended March 31, 2004, there were no Current Reports filed on Form 8-K.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

AMERICAN INTERNATIONAL GROUP, INC.
(Registrant)

/s/ HOWARD I. SMITH

(Howard I. Smith, Vice Chairman, Chief Financial Officer and Chief Administrative Officer)

Dated: May 10, 2004

EXHIBIT INDEX

| Exhibit Number | Description | Location |
|---------------------------|---|--|
| 2 | Plan of acquisition, reorganization, arrangement, liquidation or succession | None. |
| 4 | Instruments defining the rights of security holders, including indentures | Not required to be filed. |
| 9 | Voting trust agreement | None. |
| 10 | Material contracts | None. |
| 11 | Statement re computation of per share earnings | Included in Note (3) of Notes to Financial Statements. |
| 12 | Statement re computation of ratios | Filed herewith. |
| 15 | Letter re unaudited interim financial information | None. |
| 18 | Letter re change in accounting principles | None. |
| 19 | Report furnished to security holders | None. |
| 22 | Published report regarding matters submitted to vote of security holders | None. |
| 23 | Consents of experts and counsel | None. |
| 24 | Power of attorney | None. |
| 31 | Rule 13a-14(a)/15d-14(a) Certifications | Filed herewith. |
| 32 | Section 1350 Certifications | Filed herewith. |
| 99 | Additional exhibits | None. |

American International Group, Inc.

Computation of Ratios of Earnings to Fixed Charges

| Three Months Ended March 31, (in millions, except ratios) | 2004 | 2003 |
|--|--------------|----------|
| Income before income taxes, minority interest and cumulative effect of an accounting change | \$ 4,291 | \$ 2,924 |
| Less – Equity income of less than 50% owned persons | 50 | 30 |
| Add – Dividends from less than 50% owned persons | 3 | 3 |
| | 4,244 | 2,897 |
| Add – Fixed charges | 1,617 | 1,412 |
| Less – Capitalized interest | 14 | 12 |
| Income before income taxes, minority interest, cumulative effect of an accounting change and fixed charges | \$ 5,847 | \$ 4,297 |
| Fixed charges: | | |
| Interest costs | \$ 1,571 | \$ 1,367 |
| Rental expense * | 46 | 45 |
| Total fixed charges | \$ 1,617 | \$ 1,412 |
| Ratio of earnings to fixed charges | 3.62 | 3.04 |
| Secondary Ratio | | |
| Interest credited to GIC and GIA policy and contract holders | \$ 1,093 | \$ 898 |
| Total fixed charges excluding interest credited to GIC and GIA policy and contract holders | \$ 524 | \$ 514 |
| Secondary ratio of earnings to fixed charges | 9.08 | 6.62 |

* The proportion deemed representative of the interest factor.

The secondary ratio is disclosed for the convenience of fixed income investors and the rating agencies that serve them and is more comparable to the ratios disclosed by all issuers of fixed income securities. The secondary ratio removes interest credited to guaranteed investment contract (GIC) policyholders and guaranteed investment agreement (GIA) contractholders. Such expenses are also removed from income before income taxes, minority interest and cumulative effect of an accounting change used in this calculation. GICs and GIAs are entered into by AIG's insurance subsidiaries, principally Sun America Life Insurance Company and AIG Financial Products Corp. and its subsidiaries, respectively. The proceeds from GICs and GIAs are invested in a diversified portfolio of securities, primarily investment grade bonds. The assets acquired yield rates greater than the rates on the related policyholders obligation or agreement, with the intent of earning operating income from the spread.

CERTIFICATIONS

I, M.R. Greenberg, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) [Omitted pursuant to SEC Release No. 33-8238];
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ M.R. GREENBERG

M.R. Greenberg
Chairman and Chief Executive Officer

Date: May 10, 2004

CERTIFICATIONS

I, Howard I. Smith, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of American International Group, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) [Omitted pursuant to SEC Release No. 33-8238];
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ HOWARD I. SMITH

Howard I. Smith
Vice Chairman, Chief Financial Officer and
Chief Administrative Officer

Date: May 10, 2004

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended March 31, 2004, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, M.R. Greenberg, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ M.R. GREENBERG

M.R. Greenberg
Chief Executive Officer

Date: May 10, 2004

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.

CERTIFICATION

In connection with the Quarterly Report on Form 10-Q of American International Group, Inc. (the "Company") for the quarter ended March 31, 2004, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Howard I. Smith, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, that to my knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ HOWARD I. SMITH

Howard I. Smith
Chief Financial Officer

Date: May 10, 2004

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of the Report or as a separate disclosure document.