TESTIMONY OF RODNEY CLARK

MANAGING DIRECTOR, RATINGS SERVICES,

STANDARD & POOR'S FINANCIAL SERVICES LLC

BEFORE

THE SUBCOMMITTEE ON CAPITAL MARKETS, INSURANCE, AND GOVERNMENT SPONSORED ENTERPRISES

UNITED STATES HOUSE OF REPRESENTATIVES

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Mr. Chairman, Mr. Ranking Member, Members of the Subcommittee, good morning. My name is Rodney Clark. I serve as a managing director in Standard & Poor's Ratings Services business, and from 2005 until very recently, I served as S&P's lead ratings analyst covering American International Group ("AIG"). I am pleased to appear before you today, and intend to cover three broad topics: (i) the history of S&P's ratings on AIG; (ii) our reasoning in arriving at those rating opinions, particularly those that we published over the last six months; and (iii) our views with respect to the effect of AIG's troubles on the creditworthiness of its subsidiaries.

At the outset, I would like to take a moment to speak generally about our ratings process and to explain what ratings are and are not intended to convey.

S&P's Credit Ratings

S&P's credit ratings are our current opinions on the future credit risk of an entity or a debt obligation. They express our opinion about the capacity and willingness of an entity to meet all of its contractual and financial obligations as they come due. S&P's ratings do not speak to the market value of a security or the volatility of its price and they are not recommendations to buy, sell or hold a security; they simply provide a tool for investors to use as they assess risk and differentiate credit quality of obligors and the debt they issue.

S&P forms its rating opinions through quantitative and qualitative analysis performed by rating analysts. These analysts gather information about a particular obligor or debt issue, analyze the information according to our published criteria, form opinions about the information and then present their findings to a committee of analysts that votes on what ratings to assign. After a rating opinion is formed, S&P publishes the opinion in real-time and for free on its Web site, www.standardandpoors.com. We also generally publish a narrative along with our ratings that provides additional detailed information about our opinion.

This is the process by which S&P arrived at its ratings on AIG, which I will now address in some detail.

S&P's AIG Rating History

Attached to my written submission is a table listing our global ratings history on AIG since 1990. As the table shows, as of June 1990 S&P's rating on AIG was 'AAA.' This is our highest rating, and it reflected our view that AIG's capacity to meet its financial commitments was extremely strong. Our view took into consideration AIG's internationally diversified business mix, historically superior earnings performance, conservative balance sheet management, and exceptional liquidity characteristics. Our opinion began to change, however, starting in March 2005. Since then, S&P has lowered its rating of the company four times.

Recent Ratings Actions on AIG

S&P downgraded AIG on March 30, 2005, when it lowered AIG's rating from 'AAA' to 'AA+'. Our opinion of AIG had changed in large part due to the company's involvement in a number of questionable financial transactions, and reflected our revised assessment of AIG's management, internal controls, corporate governance and culture. In publishing this rating change, we expressed the view that AIG's globally diversified financial services group was still expected to generate very strong earnings and profits. We also reported that the company had told us that its new management had initiated a rigorous review of internal controls.

In June 2005, we again lowered our rating on AIG — this time to 'AA' — reflecting our revised credit assessment based on significant accounting adjustments that had just been announced by the company. Despite strong overall earnings, we believed that AIG's adjusted financial statements indicated greater volatility and lower profitability than had been previously reported. At this time, AIG's capitalization — that is, its ability to absorb losses — was considered good.

In February 2008, S&P placed a negative outlook on the company based on concerns about the way AIG was determining the fair value of credit default swaps — or "CDS" – it had entered into. As has recently been widely reported, CDS are essentially guarantees of credit risk on securities or entities. AIG's CDS guaranteed an array of structured finance securities, including securities backed by subprime residential mortgages.

Three months later, in May 2008, we lowered our rating on AIG further to 'AA-'. This rating action was based in large part on our reaction to the company's announcement of an after-tax loss of $7.8 billion, including $5.9 billion in losses related to its CDS portfolio. S&P maintained a negative outlook on AIG throughout the summer of 2008.

In August, following a deal-by-deal credit analysis of AIG's investment and CDS portfolios, S&P reached its view — and stated publicly — that AIG's actual credit-related losses in these areas would likely amount to around $8 billion with significantly higher mark-to-market losses.

As has been well publicized, AIG's financial condition deteriorated sharply in September 2008 following substantial market disruptions, including government takeovers of Freddie Mac and Fannie Mae, the bankruptcy of Lehman Brothers, and the sale of Merrill Lynch, among other things. These events led to a sudden drop in the market value of AIG's investments and, more importantly, the investments of third parties that had purchased CDS guarantees from AIG.

In light of these events, on September 12, 2008, S&P placed its ratings of AIG and all AIG subsidiaries on CreditWatch with negative implications. Three days later, on September 15, 2008, as AIG's condition continued to deteriorate, S&P lowered its rating further to 'A-'. As stated in our published reports at the time, our decision to downgrade AIG was based primarily on a combination of AIG's reduced flexibility in meeting collateral needs and its increasing CDS-related losses.

Two days later, on September 17, 2008, the Federal Reserve Bank of New York extended an $85 billion borrowing facility to AIG. Were it not for this government assistance, we believe that AIG's creditworthiness would have continued to deteriorate. Indeed, our current rating on AIG, which remains at 'A-', includes a six-notch "uplift" to account for federal government support. Thus, without government support, our rating on AIG today would be 'BB-'.

S&P's Current Outlook For AIG

Two weeks ago, on March 2, 2009, S&P affirmed its 'A-' rating on AIG. This rating, as noted, is adjusted to account for continuing federal government support. We expect that, as the federal government's recapitalization improves AIG's access to equity capital, the pressure on debt holders will likely be reduced.

In our view, the government's continuing actions with respect to AIG have significantly reduced the risk of further rapid deterioration in the company's creditworthiness. However, we maintain our negative outlook on the company going forward. This is based in part on intermediate-term concerns about the company's ability to retain key staff and to engage in profitable new business, as well as its ability to carry out plans to raise capital by selling off some of its subsidiaries, particularly in light of the current lack of liquidity in the capital markets.

Our ongoing negative outlook for AIG also reflects our expectation that there will be increased pressure on the company's insurance businesses, as well as an overall susceptibility to broader market trends in light of AIG's weakened position. Although at this point we have not seen clear evidence of long-term damage to AIG's insurance franchise, there have been widespread reports that competitors are actively pursuing AIG's accounts and key underwriting personnel. If in our view these factors become a significant threat to future business prospects, we could lower AIG's rating again. On the other hand, if AIG's business were to stabilize and government support continues, we would consider revising the outlook to stable.

The Relationship Between AIG and its Subsidiaries

With respect to the effect of AIG's troubles on the creditworthiness of its subsidiaries, we believe those subsidiaries are to some extent insulated. For example, if AIG had been forced into bankruptcy, the bankruptcy would have likely included a relatively small number of AIG's subsidiaries — such as AIG Financial Products Corp. — with only a marginal impact on AIG's insurance subsidiaries. That is because the insurance subsidiaries' capital is generally insulated by state insurance laws and regulations.

Nevertheless, when S&P lowered its credit rating on AIG to 'A-' on September 15, we also lowered the ratings on most of AIG's insurance subsidiaries to 'A+' from 'AA+', where they remain today. While AIG's financial problems have no direct effect on the solvency of its insurance subsidiaries, we believe the creditworthiness of those subsidiaries is nevertheless indirectly affected in two primary respects. First, financial problems at AIG generally make it less likely that AIG will provide additional capital to its subsidiaries in the event the subsidiaries suffer investment losses of their own or otherwise require recapitalization. This concern is somewhat muted by AIG's receipt of government support — indeed, the parent company just recently recapitalized certain of its U.S. and Asian life insurance subsidiaries. Nevertheless, there is, in our view, still some risk that recapitalizations of subsidiaries will be less likely to continue while the parent company seeks to stabilize itself.

The second issue we see affecting the creditworthiness of AIG's insurance subsidiaries relates more generally to overall reputational risk resulting from the parent company's financial problems. For example, it may be more difficult for the subsidiaries to retain and attract new customers where there is uncertainty surrounding the parent company — particularly in light of the widely-held expectation that some of the subsidiaries will be sold off by AIG as part of the ongoing effort to strengthen its balance sheet.

As a general matter, S&P believes that AIG's insurance subsidiaries are currently well capitalized to meet their policy obligations. The strength of the subsidiaries is a positive factor in our view of AIG's overall creditworthiness. Our ratings on any particular subsidiary could change in the event of a sale of the subsidiary by AIG. The nature of the change would likely depend on the buyer and the impact of the sale on the subsidiary's competitive position, capital structure, and earnings. It is quite possible that the ratings on some subsidiaries could move in a different direction than others.

The Effect of S&P's Ratings on the Decline of AIG

Another subject the Subcommittee asked me to address is whether S&P's ratings may have contributed to the decline of AIG. While some have argued that S&P was too slow to downgrade AIG, others have said that we acted too aggressively and that our downgrades contributed to AIG's decline. We believe that AIG's difficulties resulted from the convergence of many factors, including the unprecedented and substantial deterioration in the market value of AIG's assets and CDS portfolio. Our rating changes were driven by, and reflected our view of, these developments. In any event, we do not believe it would have been appropriate or consistent with our independent role in the markets for S&P to have refrained from taking any rating action we otherwise believed was warranted based on changing credit risks simply out of deference to a particular issuer. Our ratings are not driven by market sentiment. Rather, our role is to act as independent observers offering our views of creditworthiness.

Lack of Involvement in Government Aid Packages

Finally, in my invitation to testify, the Subcommittee asked me to describe any involvement S&P may have had in connection with the structuring or restructuring of the government's support packages to AIG. Although S&P has been informed by government officials about the actions that have been taken, we have had no participation in the structuring or restructuring of these packages; nor has S&P provided, or been asked to provide, any advice or consultation to the government in connection with its support of AIG.

Conclusion

I thank you for the opportunity to participate in this hearing, and I would be happy to answer any questions you may have.

Table of S&P ratings history for American International Group Inc. since June 1990

Date	Rating/Outlook
26-Jun-1990	AAA/Stable
29-Oct-2004	AAA/Negative
15-Mar-2005	AAA/Watch Neg
30-Mar-2005	AA+/Watch Neg
03-Jun-2005	AA/Negative
10-Nov-2006	AA/Stable
12-Feb-2008	AA/Negative
08-May-2008	AA-/Watch Neg
21-May-2008	AA-/Negative
12-Sep-2008	AA-/Watch Neg
15-Sep-2008	A-/Watch Neg
17-Sep-2008	A-/Watch Dev
03-Oct-2008	A-/Watch Neg
02-Mar-2009	A-/Negative