AIG warns imminent failure will have global consequences

Asks government for an additional $30 billion

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In a bid to avoid default, the American International Group (AIG) warned regulators that the "company's collapse could cripple money market funds, force European banks to raise capital, cause competing life insurers to fail and wipe out the taxpayers' stake in the firm," reported *Bloomberg News* on Monday.

AIG is seeking $30 billion in fresh capital to add to the $152 billion of taxpayers' money already in place. The request came after AIG posted a $61.7 billion fourth quarter loss, the worst quarterly loss in US corporate history.

Quoting from a draft presented by AIG to the Federal Reserve Board and Treasury on February 26, labeled "strictly confidential," *Bloomberg News* said the giant insurance firm is appealing for a fourth injection of taxpayers' money to avoid a "catastrophic" collapse with consequences far worse than the demise of Lehman Brothers six months ago. The AIG statement warns, "What happens to AIG has the potential to trigger a cascading set of further failures which cannot be stopped except by extraordinary means."

The substance of these "extraordinary means" is not spelled out. The US government is exhausting traditional ways of dealing with the economic crisis. Those based on monetary policy came to an end last December when the Fed announced it was effectively setting the Federal Funds rate at zero, and Obama's fiscal policy of stimulus spending has failed to calm the markets or restore investor confidence.

History tells of two other approaches. One is a massive devaluation of the dollar. This would essentially be an attempt by the US—akin to a declaration of trade war—to transfer the burden of the crisis to rival capitalist powers. The other is so-called "shock therapy"—used in the 1980s in the US, Latin America and other countries—involving drastic cuts in the living standards of the working class by various means, including police repression if necessary.

"Insurance is the oxygen of the free enterprise system," says AIG's statement. "Without the promise of protection against life's adversities, the fundamentals of capitalism are undermined."

There is a large element of cynicism in this assertion.

Many workers have experienced the difficulty of collecting money from insurance companies to pay for medical bills. As for AIG's professed interest in maintaining "the promise of protection against life's adversities," such altruistic concerns are entirely subordinate to the insurance giant's interest in collecting the insurance premiums made by millions of working class families.

As for the "fundamentals of capitalism" being "undermined," this is an allusion to the markets' addiction to cash from institutional investors--pension funds, mutual funds and insurance companies—which is the major source of new capital to finance capitalist ventures. Now that AIG's investments, which generated billions in profits, are failing, it asks for additional cash from working class families, in the form of public funds taken from the taxes these families pay to the government.

CNN.com carries an article dated March 6 in which it explains how AIG got into trouble. According to CNN, "The securities-lending program was designed to increase AIG's life insurance profit.... AIG, like other insurers...would ‘loan' debt securities it held in return for cash collateral. AIG would then invest the cash collateral, keeping some of the returns as profit.

"AIG often invested this collateral in residential mortgage-backed securities, which became difficult to sell as the housing market turned. In December, the Federal Reserve Bank of New York bailed AIG out of the business by buying $39.9 billion, face amount, of the securities at a discounted price of $19.8 billion, so that AIG could pay off customers and close its US securities-lending business.

"In its annual report, AIG said that to compete with 'more favorable terms offered by other lenders of securities,' AIG asked its customers to post collateral less than the 102 percent historically required by insurance regulators."

To fully grasp the level of irresponsibility and negligence of the once mighty insurance giant, it must be understood that the whole investment strategy had as its starting point the money inflow from life insurance policy holders. Thus, capital that would go to payments for the death of a father, which his wife and children would need to survive, was gambled on risky mortgage products, now known as "toxic assets." AIGs motivation was to pocket extra profits.

AIG's statement to the Fed and Treasury includes language suggesting that American capitalists are coming to the realization that the current crisis could quickly bring down the world economic system. The report warns of the global implications in the most alarming way.

"It is questionable whether the economy could tolerate another shock to the system that a failure of AIG would produce," the company declares. "The value of the US dollar might fall, Treasury borrowing costs could rise, and the agency would face doubts about the ability of the US to support its banking system."

In another passage, AIG speaks of the possibility that European banks would have to raise $10 billion to rescue credit default swaps (insurance contracts against a company defaulting), which they bought, and could face rating downgrades.

"Under the present environment," the statement continues, "a downgrade of a few notches carries the risk of pushing the bank to bankruptcy."

Bloomberg News, in its account, notes: "Life insurance customers, their faith shaken in the industry, would redeem some of their $19 trillion in US policies, overwhelming firms already weakened by the credit crisis, AIG said."

AIG's concern is not with the factory and office workers who bought insurance policies. It is concerned with saving its own skin and that of the entire US financial system.

This becomes clear when it warns regulators of the consequences for those who have already benefited from taxpayers' money. *Bloomberg News* writes: "Goldman Sachs and Deutsche Bank AG were among at least two dozen financial institutions that were paid $50 billion from the bailout funds received by AIG." Others that received payments include Morgan Stanley, Royal Bank of Scotland and HSBC Holdings.

"AIG's presentation," *Bloomberg News* reports, "said that without more US help, investment losses would mean 'AIG will not be able to repay its obligations' and that cash previously provided by the US, which controls a 79.9 percent stake in the insurer, could be lost."

This is a blunt admission that all of the measures taken by the administrations of Bush and Obama offer no real solution to the crisis. The only thing accomplished has been to ensure the bloated salaries of those responsible for the reckless behavior that precipitated the crisis in the first place.