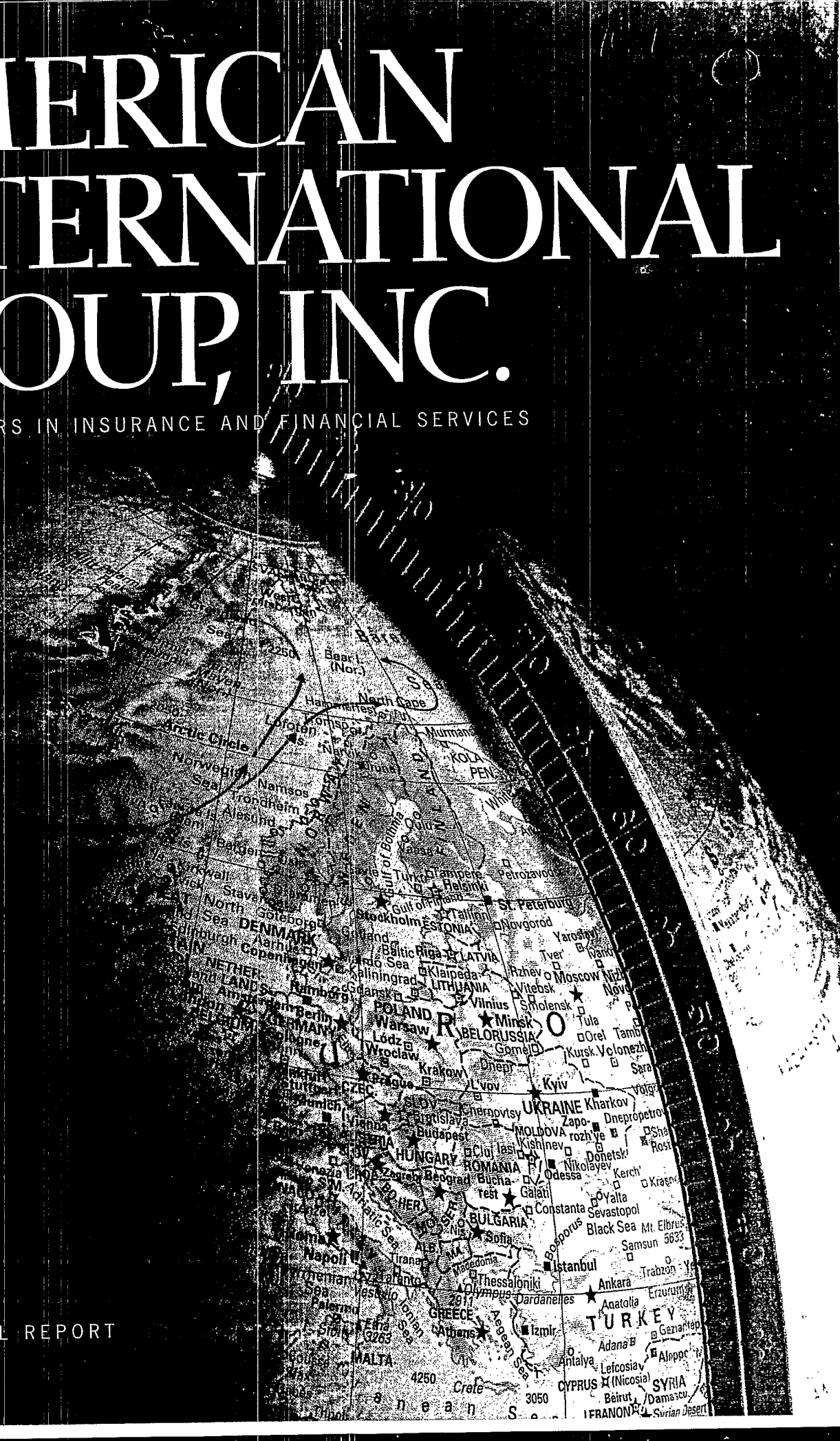


AMERICAN INTERNATIONAL GROUP, INC.

WORLD LEADERS IN INSURANCE AND FINANCIAL SERVICES

1998 ANNUAL REPORT



...leading U.S.-based international insurance
organization and among the largest underwriters of commercial and industrial coverages in
the United States. Its member companies write property, casualty, marine, life and financial
services insurance in approximately 130 countries and jurisdictions, and are engaged in a
range of financial services businesses.

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Financial Highlights

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| (in millions, except per share data and ratios) | 1998 | 1997 | % Change |
|---|--------------|--------------|-------------|
| General insurance operating income* | \$ 2,723 | \$ 2,344 | 16.2 |
| Life insurance operating income* | 1,815 | 1,550 | 17.1 |
| Financial services operating income | 913 | 701 | 30.2 |
| Income before taxes and minority interest | 5,529 | 4,731 | 16.9 |
| Net income | 3,766 | 3,332 | 13.0 |
| Net income per common share** | 3.57 | 3.15 | 13.3 |
| Book value per common share | 25.85 | 22.87 | 13.0 |
| Cash dividends per common share | .21 | .19 | 10.5 |
| Revenues | \$ 33,296 | \$ 30,602 | 8.8 |
| Assets | 194,398 | 163,971 | 18.6 |
| Capital funds (shareholders' equity) | 27,131 | 24,001 | 13.0 |
| Combined loss and expense ratio | 96.36 | 96.20 | |

*Excluding realized capital gains (losses)

**Based on diluted shares

Net Income

(Millions of dollars)

| | |
|------|-------|
| 1998 | 3,766 |
| 1997 | 3,332 |
| 1996 | 2,897 |
| 1995 | 2,510 |
| 1994 | 2,176 |

Revenues

(Millions of dollars)

| | |
|------|--------|
| 1998 | 33,296 |
| 1997 | 30,602 |
| 1996 | 27,943 |
| 1995 | 25,614 |
| 1994 | 22,122 |

Assets

(Millions of dollars)

| | |
|------|---------|
| 1998 | 194,398 |
| 1997 | 163,971 |
| 1996 | 148,431 |
| 1995 | 134,136 |
| 1994 | 114,346 |

Capital Funds (Shareholders' Equity)

(Millions of dollars)

| | |
|------|--------|
| 1998 | 27,131 |
| 1997 | 24,001 |
| 1996 | 22,044 |
| 1995 | 19,827 |
| 1994 | 16,422 |

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Letter to Shareholders

AIG had record earnings in 1998, a year characterized by financial and economic turmoil in Asia, volatility in world financial markets, and an ebbing of investor confidence, particularly in emerging markets. As the year progressed, however, there were a number of positive signs that global problems were finally being addressed in a more constructive manner, and the outlook is somewhat brighter than it was a year ago.

AIG's net income rose 13.0 percent to \$3.77 billion, or \$3.57 per share. Other financial highlights of 1998 included:

- Income before taxes and minority interest gained 16.9 percent to \$5.53 billion;
- Revenues increased 8.8 percent to \$33.3 billion;
- Assets rose 18.6 percent to \$194 billion;
- At year-end, AIG's shareholders' equity totaled \$27.1 billion; and
- AIG's return on equity was 15.0 percent.

At December 31, 1998, AIG's stock market capitalization passed the \$100 billion mark, reaching \$101.4 billion, or \$119.6 billion, reflecting the acquisition of SunAmerica Inc. on January 1, 1999. This ranked AIG 15th in market capitalization among all U.S. public corporations, and 26th among all global companies. In mid-March 1999, as this annual report went to press, AIG's market capitalization had risen to approximately \$149 billion.

Worldwide general insurance operations generated \$2.0 billion of new cash flow in 1998, including interest and reinvested dividends, and our life insurance cash flow totaled \$8.0 billion.

AIG holds Triple-A ratings from the principal rating services, Moody's and Standard & Poor's.

Review of 1998

Operating in global markets roiled by unprecedented volatility, especially in Asia, was the order of the day in 1998. The widely publicized financial dislocations that occurred unsettled investors, as many institutions and hedge funds reported significant losses. Late in the year, Russia defaulted on its debt, which led to a sharp devaluation of the Russian currency. In addition, shortly after year-end, Brazil devalued its currency and interest rates rose, propelling the country into recession. It became apparent that political forces in Brazil were resisting the fiscal plans that President Cardoso recommended, plans which in the long run would benefit the economy. We are cautiously optimistic that he will be successful in achieving economic stability for Brazil.



Maurice R. Greenberg
Chairman and
Chief Executive Officer

On the positive side, the G-7 countries responded to the global financial uncertainty by reducing interest rates, and the IMF altered its approach to affected countries by moderating the severe policies and measures it had earlier advocated. Trade surpluses increased in 1998 in a number of countries, largely as a result of sharply reduced imports, while in Southeast Asia, progress is being made toward enacting legislation on bankruptcy and foreclosure procedures.

The United States property-casualty market continues to be very competitive. There are now signs, however, that certain classes of business may have reached a level where prices are stabilizing, and, as reported in our year-end 1998 earnings press release, in a number of specialty classes we are obtaining rate increases. During the year, AIG non-renewed \$450 million of domestic business that failed to meet our underwriting and pricing standards. We also made a number of changes in our Domestic Brokerage Group to enable it to confront the challenges of the domestic marketplace more effectively. As a result, we have a more responsive organization and one that is better able to operate in the intensely competitive world we face today.

Letter to Shareholders

(CONTINUED)

Consolidation in the insurance industry continued in 1998 with a number of mergers, acquisitions and international alliances. In some cases, consolidations resulted from weakness rather than strength, with little strategic rationale. AIG has primarily focused on internal growth as a basic strategy, although we have made both opportunistic and strategic acquisitions on occasion. That was the case with our acquisition of SunAmerica Inc. in a pooling-of-interests transaction for AIG stock valued at approximately \$18 billion. SunAmerica, an outstanding performer and a leader in asset accumulation products for both the retirement and pre-retirement markets, officially became a wholly owned subsidiary of AIG on January 1, 1999. (See page 52 for an overview of SunAmerica.)

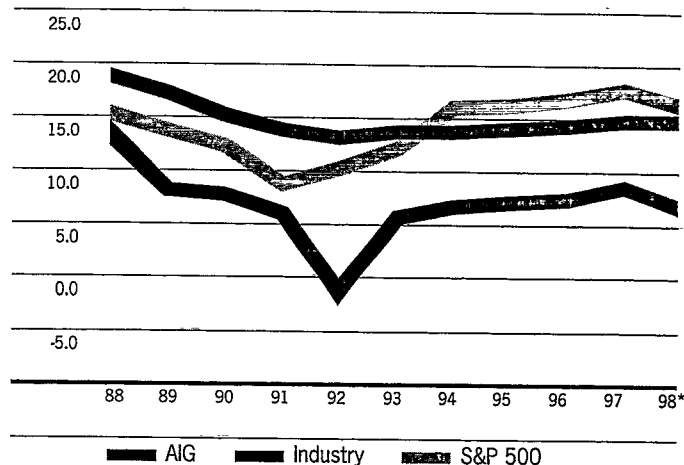
Retirement savings is a worldwide issue, as state-run pension plans are inadequately funded in many countries, and the baby boom generation is becoming concerned about retirement income. The privatization of government-run pension plans taking place in many countries is an indication that state-run plans are seeking to change their historic structure, thus forcing individuals to provide increasingly for their own retirement.

SunAmerica's strength is in the U.S. market for retirement savings products. We believe a major opportunity exists to introduce its products and marketing skills into overseas markets where AIG has extensive and longstanding operations. By capitalizing on our global network, we plan to introduce SunAmerica products into a number of such markets in the near future. Steps are already underway to implement this strategy. There are also opportunities domestically to utilize SunAmerica's nearly 10,000 independent financial advisers and their nationwide distribution system to market AIG's domestic life insurance products. In addition, the mutual fund business of SunAmerica complements AIG's fund business and will strengthen our product offerings and distribution in this area. We were also attracted to SunAmerica because of the company's strong entrepreneurial culture, creativity, dynamic leadership, strict expense control and sharp bottom line focus, characteristics that will blend well with the AIG culture.

During 1998, AIG made three other important investments, acquiring over 50 percent ownership of both Transatlantic Holdings, Inc. and 20th Century Industries, and purchasing all of the outstanding shares of SELIC Holdings, Ltd., parent company of Starr Excess Liability Insurance Company, Ltd. All three companies are now consolidated subsidiaries of AIG, whereas they had formerly been minority-owned investments. Another significant move in 1998 was our long term investment agreement with The Blackstone Group Holdings, L.P., whereby AIG acquired a limited partnership interest in Blackstone. AIG has had a long and very successful relationship investing with Blackstone, and we intend to continue to do so in the future.

Return on Equity

(Percent)



* Industry and S&P 500 Estimated
Industry and S&P 500 Source: Conning & Company



left to right

Evan G. Greenberg
President and
Chief Operating Officer

Thomas R. Tizzio
Senior Vice Chairman,
General Insurance

Another priority for us during 1998 was our continued emphasis on developing and capitalizing on technology to enhance AIG's distribution networks and levels of service to brokers, agents and customers. Electronic commerce, and in particular the use of the Internet to attract new customers and improve service to existing customers, is an important focus for AIG worldwide.

Business Segment Results

In AIG's general insurance business, worldwide net premiums written increased 8.8 percent in 1998 to \$14.59 billion, including the consolidated half-year results of Transatlantic Holdings, Inc. and 20th Century Industries. Income before income taxes, realized capital gains and minority interest for general insurance gained 16.2 percent to \$2.72 billion. AIG posted a record adjusted underwriting profit of \$530.8 million for the year, and a combined ratio of 96.36, compared to an estimated 103.7 for the property-casualty industry. AIG's general insurance operations have one of the lowest expense ratios in the industry, which provides us with a distinct competitive advantage. AIG added \$551.6 million to our general insurance net loss and loss adjustment reserves in 1998, and at December 31, these reserves stood at \$24.6 billion.

Letter to Shareholders

(CONTINUED)

Industry catastrophe losses increased in 1998, as Hurricane Georges caused insured losses of approximately \$3.0 billion in the Caribbean and the Southeastern United States. This was the largest single catastrophe to impact the insurance industry in several years. Overall, industry catastrophe losses totaled an estimated \$10.1 billion in 1998, compared to a relatively modest \$2.6 billion in 1997. For AIG, net catastrophe losses amounted to \$110 million, compared to only \$16 million the prior year.

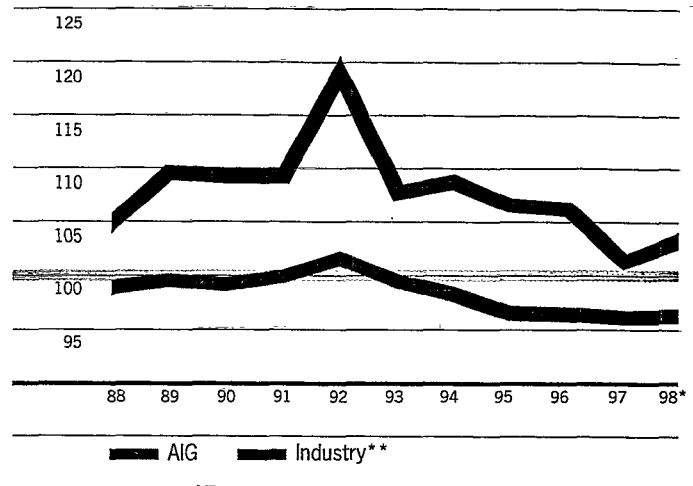
During 1998, AIG's Domestic Brokerage Group maintained its focus on underwriting discipline and strict expense control. Our mergers and acquisitions insurance unit has become a leader in assisting clients with strategic alternatives to eliminate, manage or reduce the impact of liabilities in M&A transactions, including solutions to environmental issues, litigation, accrued liabilities and retirement benefit obligations. Meanwhile, AIG Risk Finance has carved out a profitable role in structuring advanced risk management solutions and managing strategic risks. The Domestic Brokerage Group companies also developed tailored management liability programs for both Nasdaq and New York Stock Exchange listed companies, underscoring AIG's leadership and innovation in both products and distribution.

Our Domestic Personal Lines business had a very successful year, with net premiums written rising 75.2 percent to \$1.42 billion, including the consolidated operations of 20th Century Industries. The AIG Auto Insurance Program is achieving strong results nationwide based on targeted underwriting, excellent customer service, state-of-the-art technology and high visibility marketing and advertising support. The Specialty Auto Division had a 25.4 percent gain in net premiums written, offering products for the non-standard auto market in 27 states. 20th Century Industries had satisfactory operating results, despite an increasingly competitive auto insurance market on the West Coast and an additional \$40 million provision for potential claim payments relating to the Northridge earthquake. On a global basis, AIG now has approximately \$3 billion in personal auto net premiums written.

United Guaranty Corporation (UGC), AIG's subsidiary for mortgage guaranty insurance, also had a strong increase in net premiums written and a 24.5 percent gain in operating income to \$221.9 million. In its first major investment outside the United States, UGC and its joint venture partners have formed a new mortgage insurance company in Israel.

Combined Loss and Expense Ratio

(After dividends to policyholders)



* Industry Estimated

** Stock Companies

Industry Source: Conning & Company

A combined ratio of less than 100 reflects an underwriting profit.



left to right

Frank G. Wisner
Vice Chairman, External Affairs

Howard I. Smith
Executive Vice President,
Chief Financial Officer and Comptroller

Edward E. Matthews
Vice Chairman, Investments and
Financial Services

Robert M. Sandler
Executive Vice President,
Senior Casualty Actuary and
Senior Claims Officer

Edmund S.W. Tse
Vice Chairman, Life Insurance

AIG's overseas property-casualty insurance operations reported outstanding underwriting results, an increase in local currency net premiums written of 17.5 percent, including the now consolidated foreign operations of Transatlantic Holdings, Inc., and a 10.8 percent gain in operating income to \$960.1 million. American International Underwriters (AIU) continued its emphasis on opportunities created by technological advances, increased privatization and infrastructure development.

In Japan, AIU's largest country market, our business continues to flourish despite the weak Japanese economy. The "flight to quality" has benefited AIG's Japanese operations, which have their own Triple-A financial strength ratings from Standard & Poor's. Our direct auto business through the Japan branch of American Home Assurance Company had a very successful first full year of operations.

In Southeast Asia and China, AIU did well, reflecting our long-established market positions and outstanding agency force. The concern over financial stability throughout the region has provided AIU with opportunities to attract new commercial and consumer clients.

Letter to Shareholders

(CONTINUED)

Operating results in the United Kingdom and Continental Europe were very good. In the Central Europe and Commonwealth of Independent States Division, where AIG has the most extensive network of any international insurer, we expanded with new general insurance operations in Lithuania, Kazakhstan and Slovakia. Operations in the Middle East and Africa also had good growth in 1998, and our direct marketing joint venture company in Israel, AIG Golden Ltd., is off to an encouraging start. In Latin America, results improved over the prior year, and our strategic plans should produce stronger performance in the future. Our Latin American insurance network expanded in 1998, with the acquisition of a majority interest in a life and non-life insurer in El Salvador.

Transatlantic Holdings, Inc., in which we have long held a minority ownership interest, became a consolidated subsidiary in 1998 when AIG acquired over 50 percent of the company. Transatlantic is the largest broker-market reinsurance organization in the United States and a recognized leader in the specialty casualty field. Its extensive overseas operations account for a growing share of Transatlantic's business. Transatlantic had a solid year, with an increase in net premiums written and good contributions from both its domestic and overseas reinsurance operations.

AIG's Life Division reported 1998 premium income rose 16.4 percent in local currency. Operating income before realized capital gains increased 17.1 percent to \$1.81 billion. Our life premiums continued to be impacted adversely by foreign exchange fluctuations for most of the year. However, if the turnaround in financial and currency markets that took place late in 1998 continues, the impact on future life premium growth in U.S. dollars would be moderated.

Our Asian life business did extremely well in 1998 in a very difficult environment. American International Assurance Company, Ltd. (AIA), which is the largest life insurer in Southeast Asia, turned in a very creditable performance, benefiting from its many years in the region and its network of thousands of agents. Nan Shan Life Insurance Company, Ltd., one of the largest life companies in Taiwan and a strong, consistent performer, also had a very good year. ALICO Japan, as with our operations throughout Asia, benefited from its Triple-A ratings, and had double-digit premium growth despite a stagnant Japanese life insurance industry.

In an expansion of AIG's network in Central Europe, American Life Insurance Company (ALICO) and our joint venture partner acquired a majority interest in the Bulgarian Post Bank, A.D. ALICO, one of the largest international life insurance companies in the world, with \$202.8 billion of life insurance in-force, has the most extensive international life network in Central and Eastern Europe, with operations in Poland, Hungary, Czech Republic, Slovakia and Romania.

The AIG Life Companies (U.S.) achieved a 20 percent gain in operating income to \$150 million. The addition of SunAmerica to the AIG family will provide important new growth opportunities for our existing U.S. life business, and plans are well underway to mobilize the SunAmerica distribution network to market AIG's U.S. life products.

The Financial Services Group had a 30.2 percent increase in operating income to a record \$913.1 million. International Lease Finance Corporation (ILFC) had an outstanding year. Its aircraft leasing business was particularly strong in Europe, and aircraft sales were also very satisfactory. ILFC's widely diversified global client base is an important asset, ensuring the company is not overly reliant on income from any single region of the world. ILFC is the premier company in its industry; its outstanding relationships with airlines and aircraft manufacturers, excellent order positions, skilled management, and financial strength combine to ensure continued success.

AIG Financial Products Corp. (AIGFP) also produced record operating results. AIGFP's focus is on structured financial transactions tailored to specific client needs. It is a recognized leader in its field, and increasingly teams with other AIG units, including AIG Risk Finance, to structure creative risk management solutions for its multinational client base.

AIG Trading Group Inc. (AIGTG) faced a difficult operating environment in the latter part of 1998, but was able to post reasonable results despite declines in trading markets for both its currency and metals businesses. AIGTG is a leading participant in the field of hedged trading and market making in foreign exchange, interest rates and base and precious metals, with a growing global network of offices and relationships. AIGTG also works closely with AIG Risk Finance and other AIG companies in structuring transactions to meet its clients' financial and risk management requirements.

AIG Global Investment Group, Inc.'s investment management business continued to expand, in both its third-party marketable securities business and its direct investment funds. We intend to integrate our third-party marketable securities business with that of SunAmerica in 1999, while continuing to expand our direct investment fund business. AIG's global network, in-depth knowledge of emerging markets and strong asset management skills, combined with years of experience operating in Asia, Latin America, Europe and the United States, provide an excellent platform for further growth in the asset management business. During the year, several new direct investment funds were launched. AIG now has nearly \$14 billion of direct investment funds and third-party assets under management worldwide.

AIG Consumer Finance Group, Inc. introduced its first AIG credit card in the Philippines in 1998. The Group also expanded its consumer finance operations into Poland, acquiring Bank Podlaski S.A., a Polish bank with all the requisite licenses for consumer finance, and taking a majority interest in an originator of installment sales financing to consumers through Polish retailers. It also entered the Argentine consumer finance market with the purchase of a majority interest in Compania Financiera Argentina, S.A. The consumer finance business represents an opportunity for AIG to market additional financial products and services through our existing network.

Letter to Shareholders

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Investment Results and Financial Market Developments

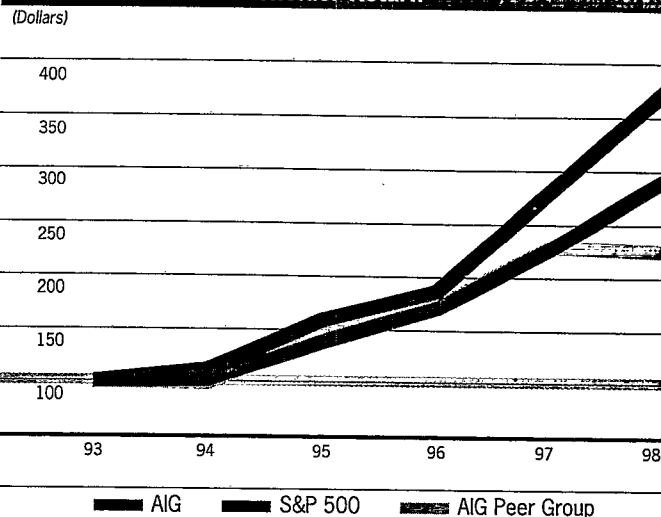
AIG's global investment portfolios did well in 1998. General insurance net investment income, including partial year results of Transatlantic Holdings, Inc. and 20th Century Industries, gained 18.3 percent to \$2.19 billion, while life insurance net investment income rose 11.6 percent to \$3.23 billion. At year-end, AIG's insurance investment portfolios totaled \$87.6 billion, of which \$38.9 billion was derived from general insurance and \$48.7 billion from life insurance.

The U.S. economy turned in a strong performance in 1998, as gross domestic product grew at a 3.9 percent annual rate with negligible inflation, capping the best three-year period since the mid-1980's. In this environment, U.S. financial markets did well and the Federal Reserve held interest rates steady for the first half of 1998. In the third quarter, the Federal Reserve announced a succession of three rate cuts which were deemed a preemptive strike against fears of a widening global economic slowdown, combined with concern of a possible credit crunch. The interest rate cuts resulted in restored market confidence and enhanced liquidity, paving the way for rate reductions around the world. The U.S. bond market also benefited with one of the lowest 30-year bond rates in years, closing 1998 at 5.09 percent. For the year, the Standard & Poor's 500 Stock Index posted a total return of 28.6 percent.

In spite of slow growth in corporate earnings and overall economic activity, European equity indices rose, although experiencing a correction in the third quarter. European bond markets posted positive returns in local currency as inflation pressures remained low.

In Japan, the long-awaited economic turnaround has still not materialized, as the Japanese government has adopted only a piecemeal approach to implementing the policies necessary to restore confidence in the economy and solve the serious problems still afflicting Japanese banks and other financial institutions. The Nikkei index closed the year down 9.28 percent, a new nine-year low. Japan's policy with respect to its currency changed several times during the year: early in 1998, a new bank bailout plan and easier monetary policy led to a weaker yen, while later in the year the yen strengthened by approximately 20 percent, and more recently, has tended to weaken. Consumers in Japan remain reluctant to spend, and the U.S. trade deficit with Japan rose sharply in 1998.

Cumulative Total Shareholder Return*



Source: Standard & Poor's Compustat Services, Inc.

* Value of \$100 invested on December 31, 1993, including reinvested dividends.

Stock Split, Dividend Increase and Stock Performance

The Board of Directors declared a three-for-two split of AIG's common stock in the form of a 50 percent common stock dividend, which was paid on July 31, 1998 to shareholders of record on June 26, 1998. The Board also increased the regular quarterly dividend to 5.6 cents per share, effective with the September dividend, an increase of 12.0 percent.

AIG's common stock gained 33.3 percent during 1998, compared to a decrease of 3.2 percent for a group of peer companies, and an increase of 26.7 percent for the Standard & Poor's 500 Stock Index. Over the past five years, with dividends reinvested, AIG stock has appreciated 278 percent, compared to 126 percent for the peer group and 194 percent for the S&P.

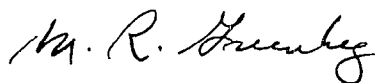
Board of Directors Changes

We would like to note with special thanks the contributions made over the past several years by AIG Director Lloyd M. Bentsen, who retired from our Board in 1998. Senator Bentsen was an important voice in our deliberations and we will miss his counsel and support in the future.

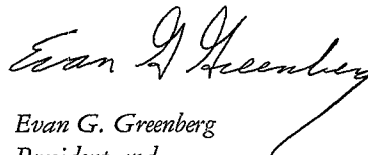
In early 1999, Eli Broad, Chairman and Chief Executive Officer of SunAmerica Inc., and Jay S. Wintrob, SunAmerica Vice Chairman and Chief Operating Officer, were elected to the AIG Board. In addition, Ellen V. Futter, President of the American Museum of Natural History, joined the Board in March. We are pleased to welcome these new Directors to our Board.

Conclusion

1998 will go down in the history books as a very challenging year, but one in which AIG performed well. We faced both a global economic crisis and a soft property-casualty insurance market in the United States—twin challenges for our managers, which they confronted extremely well. AIG has never been stronger or better positioned to capitalize on the many opportunities we see ahead. On behalf of the Board of Directors and management, we thank our employees, agents and brokers around the world for their contributions this past year.



M.R. Greenberg
Chairman and
Chief Executive Officer

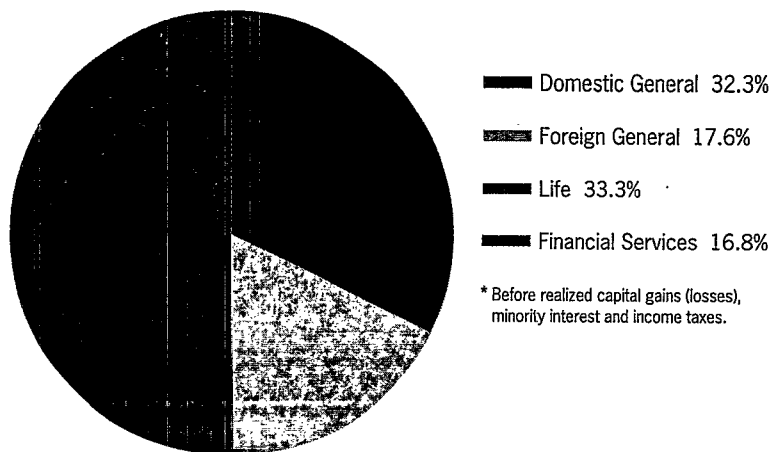


Evan G. Greenberg
President and
Chief Operating Officer

Review of Operations

AIG's net income rose to a new record high of \$3.77 billion in 1998, an increase of 13.0 percent over 1997. This Review of Operations discusses AIG's 1998 results, and highlights the business strategies and contributions made by each of our major business segments.

1998 Pretax Income by Major Business Segment*



* Before realized capital gains (losses), minority interest and income taxes.

AIG's general insurance operations are among the largest underwriters of commercial and industrial insurance in the United States, and our international property-casualty network is the most extensive of any insurance organization. Our general insurance business is composed of Domestic General-Brokerage, Domestic Personal Lines, United Guaranty Corporation and Foreign General.

General Insurance Underwriting Results

| <i>(in millions, except ratios)</i> | 1998 | 1997 |
|---|-------------------|------------|
| Net Premiums Written | \$14,586.1 | \$13,407.5 |
| Adjusted Underwriting Profit | 530.8 | 490.2 |
| Net Investment Income | 2,191.8 | 1,853.5 |
| Income Before Realized Capital Gains | 2,722.6 | 2,343.7 |
| Realized Capital Gains | 205.2 | 128.2 |
| Operating Income | 2,927.8 | 2,471.9 |
| Net Reserves for Losses and Loss Expenses | 24,618.9 | 21,171.5 |
| Combined Ratio | 96.36 | 96.20 |

Review of Operations

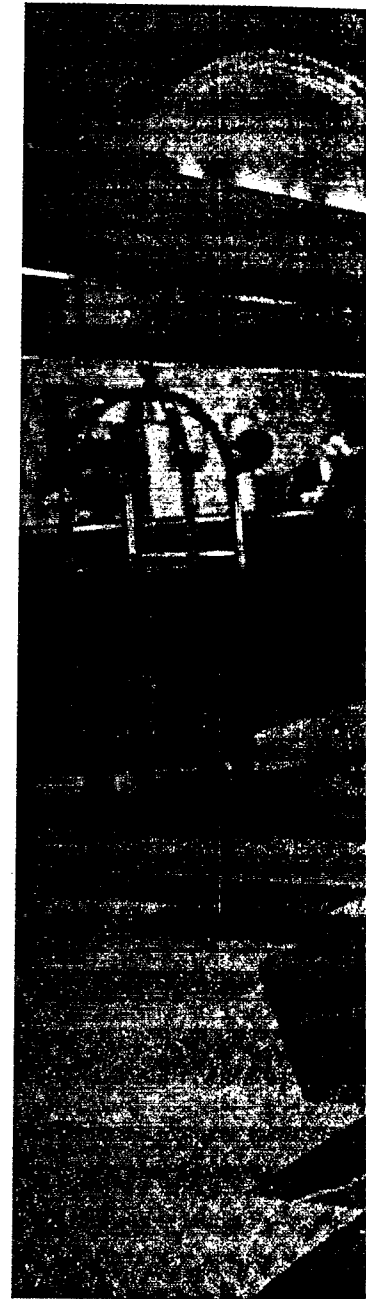
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The Domestic General-Brokerage Group (DBG) markets property-casualty insurance products and services through brokers to large, mid-sized and smaller companies in Corporate America. Offering some of the largest capacity available in the marketplace, DBG companies in particular are leaders in many specialty classes. The principal operating units in the Group are National Union Fire Insurance Company of Pittsburgh, Pa., American Home Assurance Company, AIG Environmental, Lexington Insurance Company, AIG Risk Management and AIG Risk Finance. The DBG companies hold Triple-A financial strength ratings, an important asset in a market increasingly focused on insurer solvency and stability. In 1998, AIG increased its ownership of Transatlantic Holdings, Inc. to more than 50 percent, and consequently, Transatlantic is now a consolidated subsidiary of AIG.

Domestic General-Brokerage

| <i>(in millions)</i> | 1998 | 1997 |
|--------------------------------------|-----------|-----------|
| Net Premiums Written | \$8,001.8 | \$7,885.0 |
| Income Before Realized Capital Gains | 1,354.0 | 1,214.8 |

The refocusing of DBG's underwriting, marketing and management resources through the creation of three customer groups, which are responsible for delivering the totality of DBG's products to their markets, continued to yield favorable results in 1998. This has enabled DBG to provide easier access for both brokers and clients to its products, to respond more quickly to total client needs, and to facilitate cross-marketing efforts across product lines throughout the Group.





Marriott International, Inc. is a leading worldwide hospitality company with over 1,800 hotels and resorts, as well as senior living communities, and food distribution centers. Marriott faces an increasing variety of complex management liability exposures. For comprehensive management

liability protection, Marriott turns to National Union and other AIG companies for directors, officers and corporate liability coverage that includes Year 2000 risks and enhancements addressing securities claims, bankruptcy, employment practices liability, pollution liability

and other risks. At the Fairview Park Marriott in Falls Church, Virginia, Marriott's risk manager and its director of insurance discuss some of the management liability exposures specific to the hospitality industry.

Review of Operations

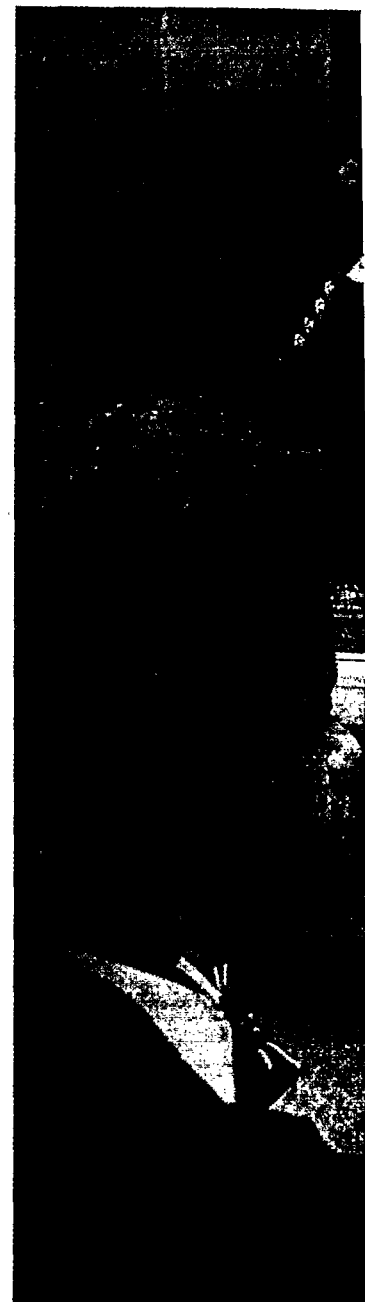
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National Accounts (corporations with \$700 million and over in revenues), Commercial Accounts (companies in the \$100-\$700 million range), and Middle Market Accounts (businesses with revenues under \$100 million) marshal the entire range of AIG's domestic underwriting and service capabilities for their target clients. The traditional AIG profit center structure has always had a strong emphasis on product development, underwriting, marketing and claim services, and the new structure has simply sharpened that focus.

National Union Fire Insurance Company of Pittsburgh, Pa. is a leading provider of directors and officers (D&O) liability and other management and professional liability insurance and services. It is also a major writer of employment practices liability, fidelity and surety coverages. National Union underscored its market leadership in 1998 by introducing D&O GoldSM, the only D&O policy to address new management liability exposures, such as those associated with governmental investigations and Year 2000-related risks. IPO GoldSM was launched to provide the same expansive protection as D&O Gold, with additional provisions specifically designed for companies undertaking initial public offerings.

Last year we reported that National Union had entered an agreement with The Nasdaq Stock Market, Inc., in which National Union and other AIG companies offer a specially designed package of management liability risk protection products and services to Nasdaq-listed companies. This program has been highly successful in its first full year, and has now been broadened beyond management liability to include other coverages. Later in 1998, National Union also reached an agreement with the New York Stock Exchange, Inc. to offer a package of management liability products and services developed exclusively to meet the global needs of NYSE-listed companies.

AIG's claim management expertise and capability is a fundamental component of our outstanding franchise in the management liability area. Significant enhancements were introduced in 1998, including broadened litigation management services through the establishment of a loss mitigation unit. The unit assists clients of National Union and other AIG member companies in managing the financial impact of litigation.





Headquartered in Memphis, Guardsmark, Inc. has grown over the past 35 years to become one of the country's leading security services providers. In 1998, AIG and Guardsmark celebrated a business association that has

spanned 20 years, a period in which AIG member companies have provided a range of insurance coverages to Guardsmark. Being on the cutting edge with new products and services to meet its insureds' changing requirements is a key component

of DBG's strategy. Whether a company's challenge is to control, transfer or finance risk, AIG creates specifically designed programs that deliver bottom line results.

Review of Operations

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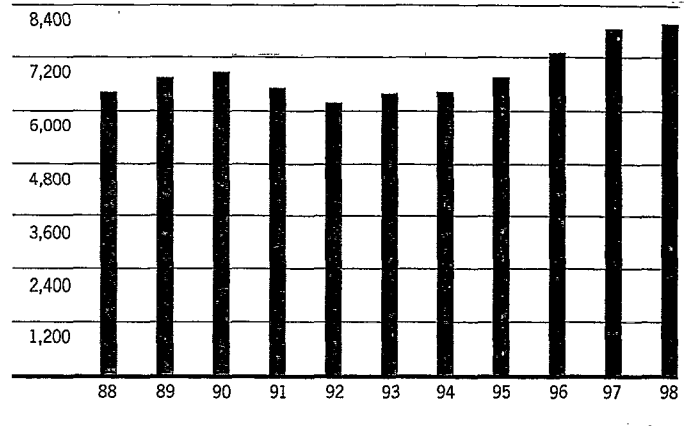
American Home Assurance Company is AIG's principal domestic provider of commercial umbrella/excess liability and primary and excess workers' compensation insurance. To better sharpen its customer focus and distribution channels, American Home's excess casualty division realigned its operations through the creation of middle market, commercial and national account teams. The division launched a number of new products in 1998, including third-party impaired property coverage, and endorsements to middle market umbrella liability policies that provide coverage for catastrophic D&O and employment practices liability claims.

The workers' compensation division began transacting small workers' compensation business via the Internet, and also initiated plans to broaden its Internet capability to provide customer billing, claim information and certificates of coverage. The division responded to the continuing soft market by supplying small businesses with low cost, high-quality programs, and medium-sized companies with an integrated service approach utilizing teams of underwriters, loss control consultants and claim specialists.

AIG Environmental is the leading U.S. provider of environmental insurance coverages and services, whether for large complex risks such as ports and rail yards, or smaller exposures such as local dry cleaners and shopping centers. A significant opportunity that began to show results for AIG Environmental in 1998 was the deregulation of the power industry. In addition, there is an increased awareness and concern among insureds over the extent of potential liabilities related to the transfer of properties which might be contaminated. Such exposures are created by the increased privatization of government or military property where contamination is an issue, and by sales of commercial real estate and merger and acquisition transactions. Product offerings from AIG Environmental help facilitate the completion of these types of transactions by protecting the buyer, the seller or both parties from the risk associated with unknown environmental liability, and also control site cleanup costs. AIG Environmental also launched a secured creditor impaired property policy designed to protect the interests of financial institutions in connection with real estate transactions. The policy, which offers protection against defaults on commercial loans with environmental conditions, attracted lenders based on its cost effectiveness and ability to streamline an otherwise complex loan process.

Domestic General—Brokerage Net Premiums Written

(Millions of dollars)



Lexington Insurance Company is the largest U.S. excess and surplus lines insurer, specializing in difficult-to-place property-casualty risks. In 1998, Lexington continued to target employment practices liability, professional liability, health care, specialty personal lines and inland marine covers as priority areas. In its continuing efforts to provide integrated coverages and services tailored to specific market niches, Lexington introduced several new products in 1998. In its employment practices liability business, Lexington developed coverage to protect the rapidly growing alternative staffing industry, as well as specialized coverage for law firms, investment banks, insurance brokers, accounting firms, architects/engineers, and other professional organizations. The design professional area reported strong premium growth, as did the health care unit. In a sector where the increase in capitated contracts between managed care organizations and health care providers continued to rise, Lexington's provider excess loss business showed good growth.

In early 1998, AIG increased its ownership of SELIC Holdings, Ltd., which owns **Starr Excess Liability Insurance Company, Ltd. (Starr Excess)**, to 100 percent. Starr Excess provides high limits of excess general liability insurance, excess directors and officers insurance, and excess professional liability insurance worldwide. During the year, Starr Excess changed its corporate domicile from Bermuda to the state of Delaware and also opened a branch in London. The domicile change was undertaken to enhance Starr Excess's ability to provide ready access for brokers in the U.S. market, while maintaining its strong presence in and access to the Bermuda market.

AIG Risk Management (AIGRM) provides customized primary casualty and risk management programs to Fortune 2000 and large regional companies under an array of financial arrangements. As a pioneer in this business, AIG continues to maintain a strong leadership position and global capability. AIGRM also provides risk management and risk transfer coverages to foreign-based multinational corporations operating in the United States, as well as industry specialty programs in transportation, construction, energy and public entities.

In its specialized industry operations, AIGRM's experienced underwriters are complemented with claim, loss control, premium audit and service professionals, all with industry-specific knowledge. For example, in 1998, a product integration team strategy was launched nationwide for the construction industry, which brings together casualty construction products and services with other specialty products such as excess umbrella, professional liability, environmental, property and surety coverages, for a seamless array of coverages from a single source.

Review of Operations

(CONTINUED)



Bruckmann, Rosser, Sherrill & Co. (BRS) is a limited partnership that makes private equity investments in management buyouts and recapitalizations. Among the companies in BRS' portfolio is California Pizza Kitchen, fast becoming one of the most recognizable restaurant concepts in

the country. When investing in buyouts and recapitalizations, BRS turns to AIG to appraise liabilities of the company before an investment is made. Once the investment is completed, AIG also works with BRS to develop insurance programs that address the specific exposures the part-

nership may face as new owners, including directors and officers coverage. At the California Pizza Kitchen on Manhattan's Upper East Side, BRS Chief Financial Officer and the President of AIG's Mergers & Acquisitions Division discuss the restaurant group's expansion plans.



The **AIG Risk Finance Division**, a market leader in the design and implementation of creative risk financing solutions, serves clients typically requiring the most advanced risk management capabilities. Drawing on the worldwide resources of AIG's insurance and financial services companies, AIG Risk Finance provides highly structured programs that feature a blend of financial, insurance and capital market strategies to enhance balance sheet strength, address solvency and liquidity concerns, and help manage strategic risks. The Division expanded its operations both domestically and on an international level, where representative offices were established in London, Paris, Tokyo, Sydney and Johannesburg.

One of our newer Divisions, the **Mergers & Acquisitions (M&A) Division**, provides a broad array of insurance, risk management and financial products and services to clients engaged in mergers, acquisitions and divestitures. The Division's focus is on minimizing or eliminating existing liabilities within an M&A transaction and on preparing the successor company for dealing with potential future liabilities. Capitalizing on the insurance and financial services resources of AIG member companies throughout the world, the Division's teams of professionals deliver solutions within the compressed time frame in which such transactions typically occur.

The **AIG Warranty Products Division** provides a range of extended warranty products to markets worldwide through direct solicitation, brokers and third-party administrators. The Warranty Products Division underwrites manufacturers' warranties and extended service contracts, which offer protection beyond the manufacturer's original warranty. The Division's underwriting flexibility and superior service, combined with the Triple-A rated financial strength of AIG member companies, provide a competitive advantage in warranty markets worldwide.

Transatlantic Holdings, Inc. (Transatlantic), the largest publicly traded U.S.-based reinsurance organization, provides, through its subsidiaries Transatlantic Reinsurance Company, Trans Re Zurich and Putnam Reinsurance Company, a full range of treaty and facultative reinsurance products worldwide, with an emphasis on specialty classes. Transatlantic has an international network of offices located in the United States, Canada, Latin America, Europe and Asia. In 1998, AIG increased its ownership of Transatlantic to more than 50 percent, and Transatlantic is now a consolidated subsidiary of AIG. Transatlantic reported record 1998 earnings, with solid contributions from both domestic and international operations.

Review of Operations

(CONTINUED)

In the United States, Transatlantic faced a very competitive marketplace in 1998, but still reported an increase in net premiums written, with the gains concentrated in automobile liability and in specialty casualty classes including medical malpractice, other professional liability, accident and health, and directors and officers liability.

Transatlantic's non-U.S. business now accounts for approximately half of its total book. The company opened representative offices in Rio de Janeiro and Shanghai during the year, and also entered into an exclusive arrangement with a representative agency in South Africa. London branch net premiums written were strong, as Transatlantic continued to achieve lead market status in a growing number of classes. The Paris office nearly doubled its net premiums written, with a significant portion of the growth occurring in Central and Eastern Europe. In Asia, the Hong Kong and Tokyo offices reported growth despite the economic weakness in the region.

AIG also has a number of domestic specialty insurance companies, including **Audubon Insurance Company**, which provides personal and small commercial coverages in several Southern states; **AIG Aviation, Inc.**, which specializes in insurance facilities for commercial airlines and general aviation clients worldwide; and **AI Transport, Inc.**, AIG's transportation insurance unit for the United States and Canada.

The quality and responsiveness of AIG's claim management services are the fundamental promise we make to our insureds, and they help define our franchise in the areas where AIG is a leader. Our two claims companies for domestic operations, **AIG Claim Services, Inc. (AIGCS)** and **AIG Technical Services, Inc. (AIGTS)**, seek to enhance the effectiveness of our services to clients, particularly in the area of mitigating and reducing losses, as well as the management of claims. We are very proud of AIG's claim services, which we believe are cutting-edge. Based on the positive feedback we receive from our clients, AIG offers creativity, flexibility and efficiency in claim management that increasingly surpass industry standards.

AIGCS provides a broad spectrum of cost containment and claim management services for AIG's workers' compensation and property-casualty clients. These include integrated medical case management, litigation management, and specific capabilities addressing a range of needs, from clients in middle market businesses to the nation's largest corporations. In 1998, AIGCS introduced IntelliRisk NetSource, an Internet-based risk management system for commercial and middle market customers that allows insureds and brokers to retrieve real-time information, including account, policy, claim and payment data. AIGCS also implemented a new workers' compensation telephonic case management program featuring registered nursing teams working directly with injured workers to obtain optimum medical and return-to-work results.

AIGTS is responsible for managing specialty claims and litigation management, including D&O liability, professional liability, health care and medical malpractice liability, fidelity, surety, financial institutions, environmental, toxic tort, high exposure property and excess casualty. In 1998, AIGTS continued to build close working relationships with its AIG underwriting partners, a quality that sets AIGTS apart from other claim operations in the industry. In addition, as part of its customer service enhancement program, AIGTS established a service center dedicated to providing pertinent claim information to its clients. The staff counsel program now includes over 200 trial attorneys in 27 locations nationwide, providing insureds with the most effective representation possible.

Review of Operations

(CONTINUED)

AIG's Domestic Personal Lines business consists of the Mass Marketing and Specialty Auto Divisions and, with the acquisition by AIG of a majority interest, 20th Century Industries. Net premiums written increased 75 percent to over \$1.4 billion, including the positive impact from the partial-year consolidation of 20th Century. Operating income more than doubled.

Domestic Personal Lines

| (in millions) | 1998 | 1997 |
|--------------------------------------|-----------|---------|
| Net Premiums Written | \$1,422.2 | \$811.7 |
| Income Before Realized Capital Gains | 158.5 | 70.4 |

The Mass Marketing and Specialty Auto Divisions reported excellent results in 1998, with voluntary auto premiums growing 38 percent, for total premiums of more than \$1 billion. The consolidation of 20th Century Industries into operations for the third and fourth quarters added another \$390 million in premiums.

The Mass Marketing Division, providing coverage for preferred and standard personal auto risks, increased its policyholder count by 53 percent in 1998. For the third consecutive year, new policy sales nearly doubled in direct-to-consumer programs. Affinity business also continued to grow, reporting a 58 percent increase in new policy sales. At year-end, the Division reached a significant agreement with MBNA America Bank, N.A., the largest independent credit card lender in the world, to underwrite auto, homeowners and personal umbrella insurance products for MBNA customers. The Division also opened a fourth call center in 1998, and its product portfolio was expanded to include life and health insurance, auto and home warranty coverages, and commercial coverages for smaller businesses.

The Specialty Auto Division's core business is high risk automobile coverage. Net premiums written in 1998 rose 25 percent and autos insured increased 39 percent. Technological enhancements included the creation of an Internet site to provide billing and coverage information to agents, automation of interfaces with the agent to enhance the Division's point-of-sale policy writing software, and automation in claim processing. The resulting efficiency gains enabled the Division to maintain a cost advantage over its competitors, without compromising the commission level of the independent agents who are the Division's primary distribution channel.

20th Century Industries, which writes direct personal automobile insurance in California and adjacent states, became a consolidated AIG subsidiary in the third quarter. 20th Century, with one of the lowest expense ratios in the industry, increased its market share in California and expanded its operations into three new Western states. 20th Century now writes personal auto coverage in California, Arizona, Nevada, Washington and Oregon. With its expansion in Northern California well under way, this region represents 30 percent of 20th Century's new auto business in California, up from 13 percent only three years ago.

United Guaranty Corporation (UGC) subsidiaries write mortgage guaranty insurance for financial institutions and mortgage investors nationwide. The mortgage guaranty insurance provided by UGC's subsidiaries protects residential lenders and investors against loan losses caused by borrower default. 1998 marked the tenth consecutive year in which UGC has reported record financial results.

| United Guaranty Corporation | | |
|--------------------------------------|----------------|-------------|
| <i>(in millions)</i> | 1998 | 1997 |
| Net Premiums Written | \$362.7 | \$340.8 |
| Income Before Realized Capital Gains | 221.9 | 178.2 |

In 1998, mortgage insurance from United Guaranty helped nearly 193,000 families refinance their mortgages or purchase homes with low down payments. Mortgage interest rates remained at historically low levels throughout 1998, contributing to a record \$1.43 trillion in residential mortgage originations, the highest loan volume ever in the history of the U.S. housing industry. United Guaranty's level of new insurance set an annual production record of \$24.5 billion, a 58 percent increase over 1997. The loans insured included many mortgage refinances, resulting in slower growth of United Guaranty's total risk in force. Loan quality improved, however, as older portfolio loans were replaced with new production. United Guaranty introduced a number of new insurance products during 1998, including the Borrower AdvantageSM plan, a lower down payment option for borrowers with solid credit histories, and expanded captive reinsurance structures to increase risk-sharing opportunities for a greater number of mortgage lenders.

To broaden opportunities for mortgage insurance in international markets, UGC created its first joint venture outside the United States, a mortgage insurance enterprise in Israel. E.M.I.-Ezer Mortgage Insurance Company Ltd. is the first company to offer such coverage in Israel.

Review of Operations

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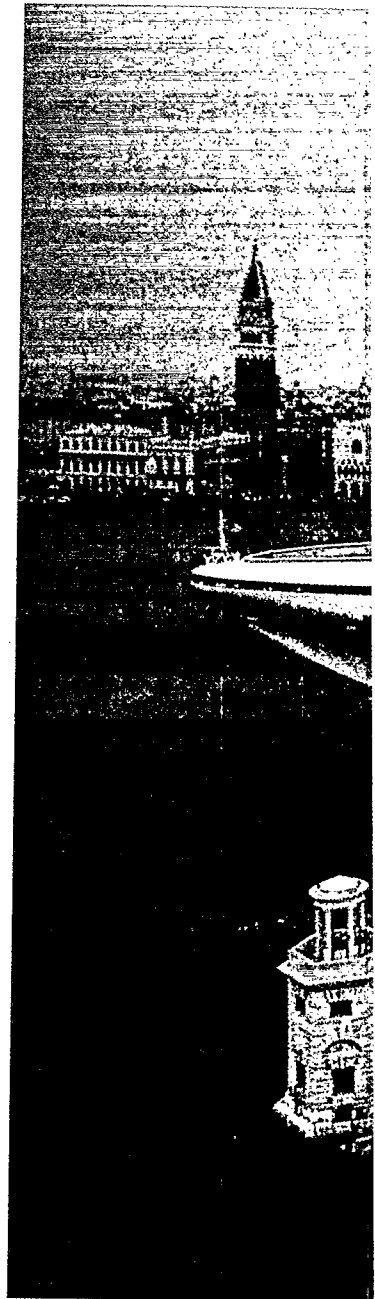
The Foreign General Group comprises AIG's international property-casualty operations, the most extensive worldwide network of any insurance organization. This network encompasses offices in over 70 countries in Asia, the Pacific Rim, Europe, Africa, the Middle East and Latin America. Operating through American International Underwriters (AIU), the Group markets a full range of property-casualty products to U.S. and foreign-based multinational corporations, local commercial companies and consumers.

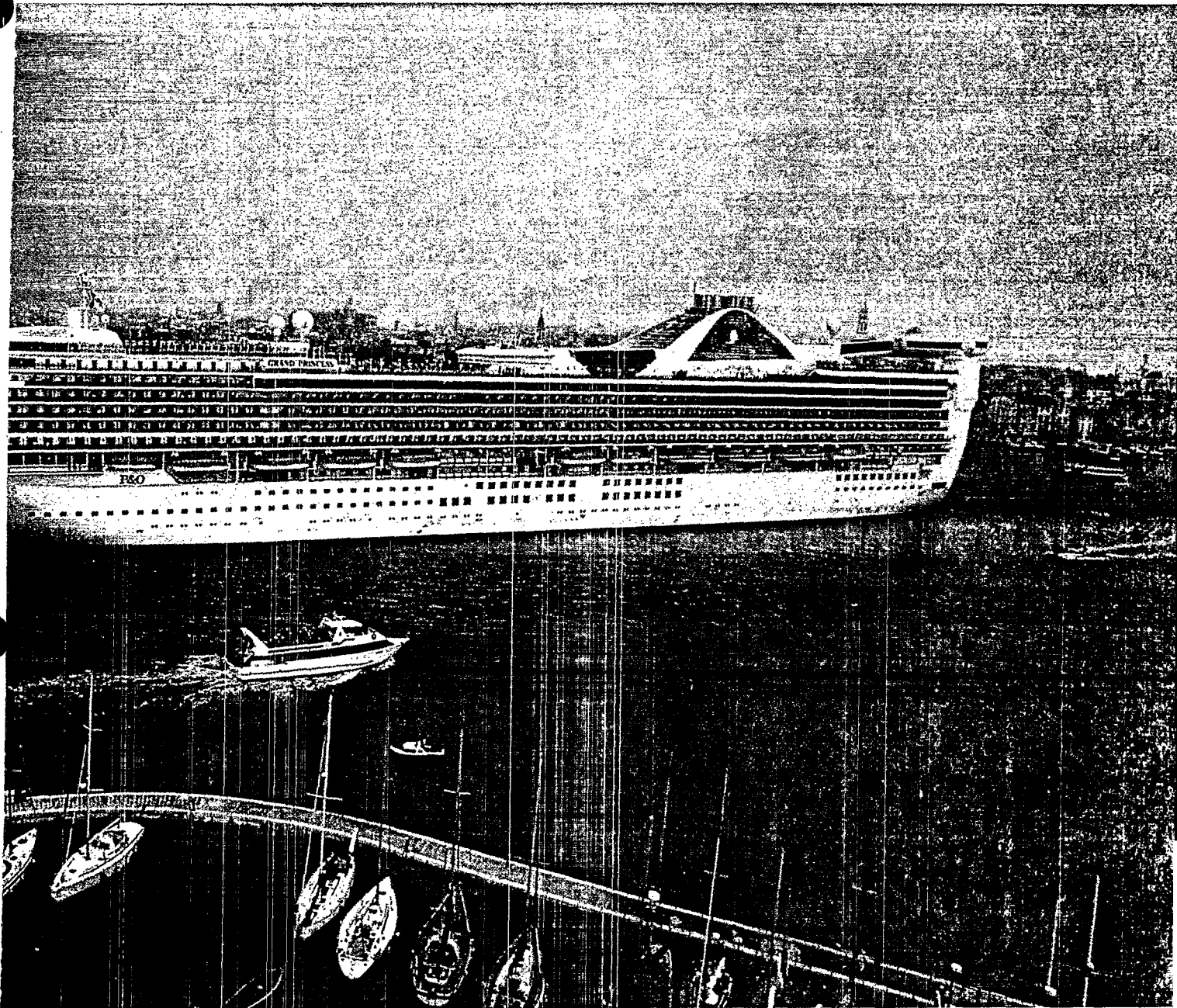
Foreign General

| <i>(in millions)</i> | 1998 | 1997 |
|--------------------------------------|-----------|-----------|
| Net Premiums Written | \$4,799.4 | \$4,370.0 |
| Income Before Realized Capital Gains | 960.1 | 866.3 |

In a year of intense competition in the worldwide property-casualty industry, with excess capital and capacity, as well as economic stress and financial volatility in many countries, AIU achieved outstanding performance with solid growth, excellent underwriting results and record operating income. Its strategy continued to emphasize opportunities stemming from technological advances, increased privatization, the growing middle class in emerging markets, infrastructure development, and AIG's global network.

In Japan, a country still mired in recession, AIU's property-casualty operations outperformed the industry. Attention focused on developing innovative new products, building new distribution channels, providing top quality claim service and leveraging the Triple-A financial strength ratings held by AIG's Japanese branch operations. These initiatives, in turn, were supported by staff and agent training programs conducted at the recently opened AIG Learning and Development Center, and by greater application of technology-driven agency support systems, expanded reliance on database marketing and increased use of Internet marketing opportunities.





AIU's worldwide network is a key competitive asset in designing and implementing global insurance programs for multinational companies. AIU's in-country underwriters, claims adjusters and loss control consultants have first-hand knowledge of local risks, policy forms, rates and tariffs, business practices,

and the political and regulatory environments of their countries. The Peninsular and Oriental Steam Navigation Company (P&O), one of the world's largest shipping groups, has relied on AIU's international network to meet its insurance and risk management needs for more

than 12 years. P&O's cruise fleet, which includes Princess Cruises, is one of the three largest in the world. Delivered last year, the 109,000-ton Grand Princess, shown here cruising past St. Mark's Square in Venice, is the largest cruise ship ever built.

Review of Operations

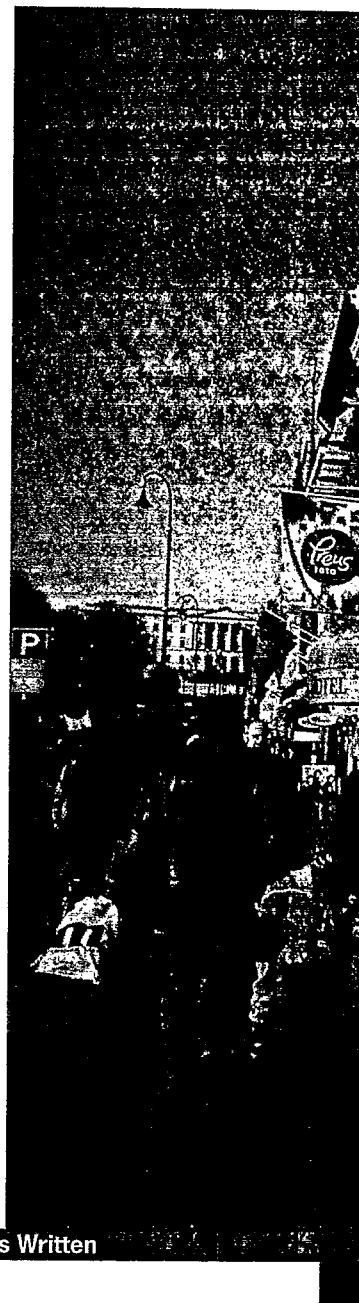
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The Japan branch of American Home Assurance Company had steadily rising direct sales of its rate differentiated auto insurance coverage. American Home, the first company in Japan to receive a license to sell auto insurance in this way, developed a very successful marketing campaign, resulting in the company becoming one of the best known brands in the Japanese insurance market. Recognizing the importance of first-rate customer service, American Home continued to emphasize its claim and call center operations, which have received extremely high marks in customer satisfaction surveys.

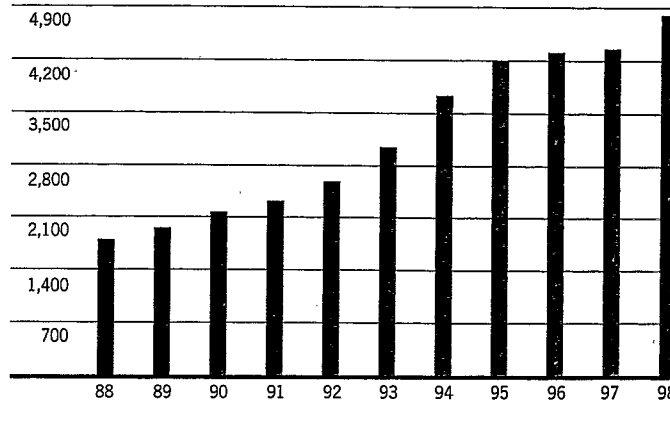
The Southeast Asia and China Divisions performed well in 1998 despite the economic problems in the region. AIU's longstanding presence in Asia, extensive network and top-rated financial strength and stability enabled it to benefit from a regional "flight-to-quality" as major lenders, financial institutions, corporations and consumers turned to AIU for insurance coverage.

New financial lines and extended warranty products were introduced and a state-of-the-art customer call center was established in Hong Kong. During the year, AIU entered into a strategic relationship with Fubon, the largest general insurer in Taiwan. AIU's China operations generated substantial growth in net premiums written, and AIU remains the only foreign general insurer with a license to operate in both Shanghai and Guangzhou.

The U.K./Ireland Division achieved excellent results in a challenging market. A major provider of insurance products and services to the largest companies in the United Kingdom, and increasingly to the middle market, AIG Europe (UK) Limited derived much of its growth from a continued focus on specialty products such as accident and health, and risk management; success in the alternative risk financing sector; and an increased presence in serving the specialty insurance needs of middle market companies through the U.K. branch network. Over the past three years, the Division has been building a new capability in workers' compensation, emphasizing a managed care approach, including working closely with clients on safety engineering and loss control. These efforts began to produce significant benefits in 1998, and increasingly distinguish AIG from its competitors in the workers' compensation field.



Foreign General Net Premiums Written
(Millions of dollars)





AIG has long been a leader in providing travel and accident insurance through the worldwide AIU network. The sharp increase in international travel for both business and pleasure has created important new opportunities. In 1998, AIG Norway signed an agreement

with VIA Gruppen, Norway's largest travel agency, to sell travel and trip cancellation coverages to VIA Gruppen customers through its network of 95 offices nationwide. The agreement with VIA established an important new distribution channel for AIG Norway and opened the door for

many cross-selling opportunities. Pictured in front of VIA's flagship office in downtown Oslo, AIG Norway's Country Manager reviews recent trends in the Norwegian travel market with VIA's President.

Review of Operations

(CONTINUED)



In 1998, AIG Europe (UK) Limited received top honors from the prestigious British Insurance Awards as "Claims Team of the Year" for the creation of a unique employers liability insurance product called *accel*. Unlike traditional programs, *accel* utilizes registered general nurses to actively manage each case, leading to faster recovery times and improved health outcomes for claimants. *Accel*, which can also result in meaningful cost savings for clients, is an example of AIG's innovative and client-oriented approach to claim services. At left, staff nurses attend to casework at the company claim center in Croydon, Surrey.

Paris-based AIG Europe S.A., serving Continental Europe, reported good growth in both premiums and operating income. AIG has a fully integrated pan-European network encompassing underwriting, claim service and corporate systems. This unique market positioning gives AIG Europe a distinct advantage in several areas, including its fleet auto program. Consolidation in the European insurance industry presents AIG Europe with increased opportunities. As the universe of brokers and insurers in the market shrinks, AIG Europe's focus on specialty products, its broadened distribution networks, including a greater effort in the middle market, and its emphasis on customer service and product innovation represent a competitive advantage. During the year, AIG Europe also addressed the systems and business implications of the introduction of the euro in January 1999, enabling the company to respond positively to client requests for euro-denominated global programs.

In the Central Europe and Commonwealth of Independent States Division, AIU continued to expand its network. Poland, Hungary and Romania all had good premium growth. New general insurance operations were launched in Slovakia, Kazakhstan and Lithuania. With operations in 13 countries at year-end 1998, AIG has the largest and most extensive general insurance network of any international insurer in the region. Early in 1999, AIG received a license to operate a general insurance business in Azerbaijan.

In the Africa and the Middle East, Mediterranean and South Asia Divisions, new financial lines products were launched in South Africa, and crisis management and specialty casualty products were introduced in a number of countries. AIG Golden Ltd., AIG's joint venture direct response property-casualty company in Israel, had a successful first year, and was granted a license to sell an expanded line of personal coverages which it intends to launch in 1999.

AIG companies have played a pioneering role in Malaysia's insurance industry for the past 50 years. Today, through a strategic alliance with the Automobile Association of Malaysia (AAM), the Malaysian branch of American Home, AHA Malaysia, continues this tradition of leadership through the introduction of affinity insurance programs for associations. With its AAM agreement, AHA Malaysia is the only company able to offer auto insurance to AAM's 184,000 members through the association's established marketing channels. Here, AIG and AAM executives discuss the program at an emergency road service site in Johor Bahru, the capital of Johor province.



In Latin America, AIU reported improved results, in spite of a worsening economic climate in the region late in the year, and the impact of Hurricanes Georges in Puerto Rico and the Caribbean, and Mitch in Central America. Argentina had an excellent year, and AIG's joint venture with Unibanco in Brazil completed its first full year. This significant relationship, in Latin America's largest market, has important potential for AIG in both the Brazilian non-life and life sectors. During the year, AIG acquired 51 percent of Union y Desarrollo, S.A., one of the largest life and general insurance companies in El Salvador. AIG now has general insurance operations in 20 countries throughout the region.

The Australasia Division achieved profitable results in a highly competitive market, with accident and health and financial lines performing particularly well.

AIU's North American Division provides U.S.-based multinationals with global programs. The trade credit and political risk division turned in especially strong results. Targeted to smaller and medium-sized North American companies that are just beginning to expand overseas, AIU's WorldRisk™ product achieved excellent acceptance. Putting the extensive resources of AIG's global network at the disposal of smaller companies, WorldRisk provides customized coverage for physical damage, liability, marine, foreign travel accident, kidnapping, ransom and extortion, while also providing emergency medical assistance.

Review of Operations

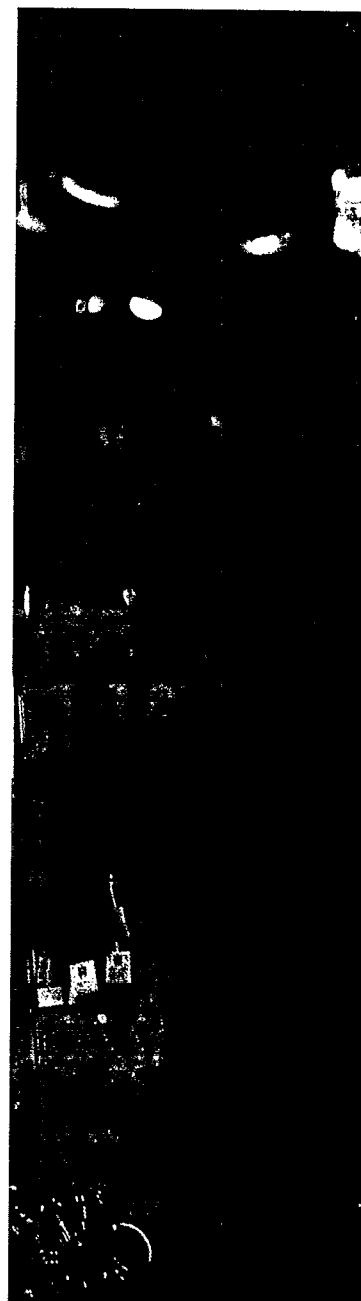
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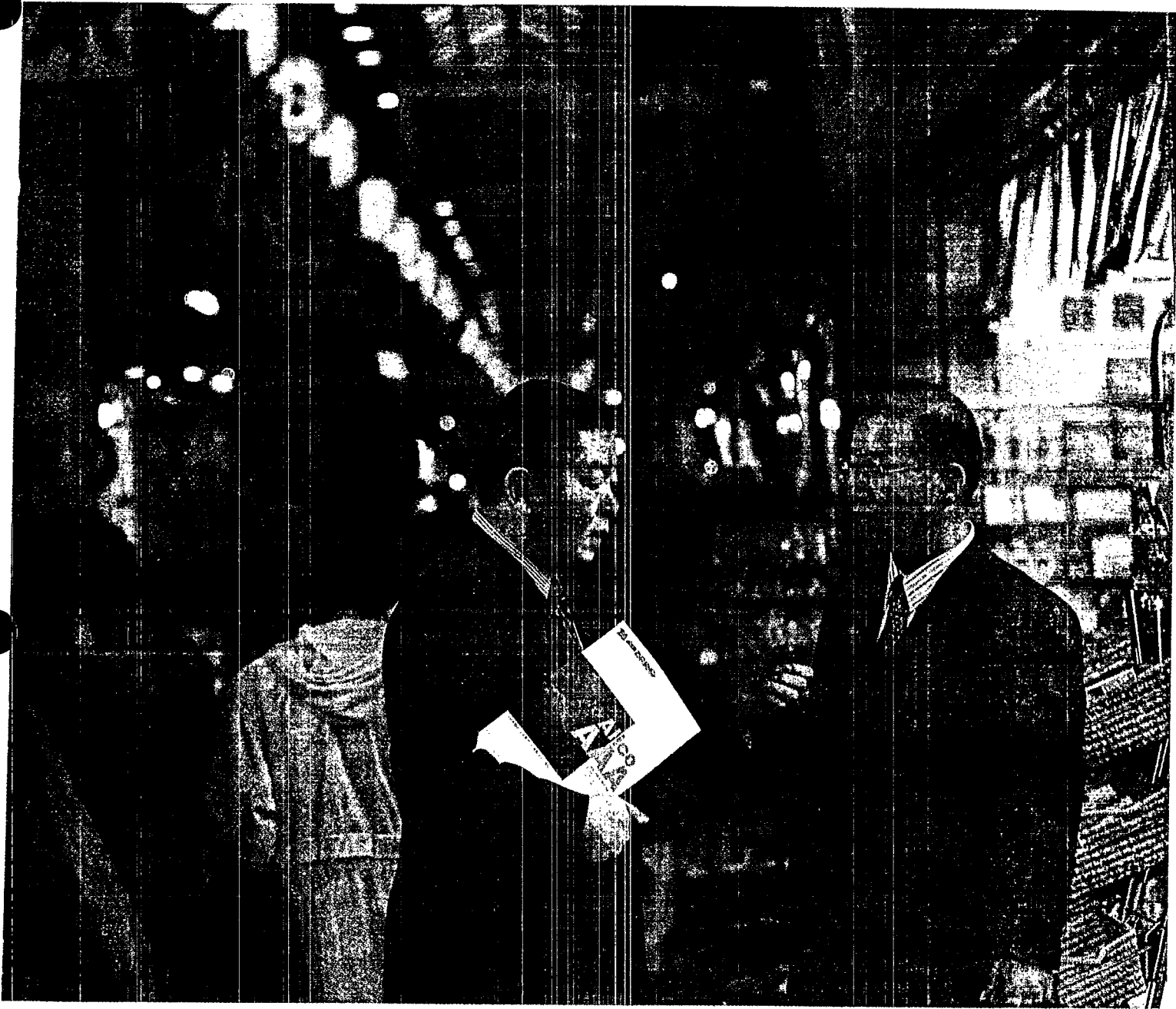
AIG's life business, the most extensive worldwide network of any life insurer, had outstanding results in 1998, accounting for over 33 percent of AIG's total pretax income. Overseas operations, which represent the vast majority of AIG's life business, are conducted principally through American International Assurance Company, Ltd., Nan Shan Life Insurance Company, Ltd., Philippine American Life and General Insurance Company, and American Life Insurance Company. The AIG Life Companies (US.) are making a growing contribution to life results.

| Life | | |
|--------------------------------------|-------------------|-------------|
| <i>(in millions)</i> | 1998 | 1997 |
| Premiums | \$10,246.7 | \$9,925.6 |
| Income Before Realized Capital Gains | 1,814.7 | 1,550.3 |
| Realized Capital Gains (Losses) | (34.7) | 21.2 |
| Operating Income | 1,780.0 | 1,571.5 |

American International Assurance Company, Ltd. (AIA), AIG's life insurance company covering Southeast Asia, is the largest life insurer in the region with a network of branches, subsidiaries and affiliates in Thailand, Malaysia, Singapore, Hong Kong, Indonesia, Brunei, Macao, Korea, Australia and New Zealand. AIA also has a growing presence in China with branch offices in Shanghai and Guangzhou. AIA commands leading positions in its major markets. It had a good year in 1998, despite the continued economic and financial turmoil in many Southeast Asian economies.

AIA's 1998 results are a direct reflection of the company's core strategy emphasizing financial strength, product innovation, strong local reputation, extensive and high quality distribution network, and broadening distribution channels. The "flight to quality" brought on by an increased concern for the safety of their savings among insureds in the region benefited AIA, with its top financial ratings and reputation. During the year, Standard & Poor's re-affirmed AIA's Triple-A financial strength rating, the only Southeast Asian insurer to hold S&P's highest rating.





The strength and versatility of ALICO Japan's agency network, comprised of nearly 10,000 registered agents nationwide, is a key component of the company's strategy and success in the Japanese life insurance market. ALICO Japan developed

the country's first sales force of general insurance agents that also sell life insurance products. Pictured here in Kyoto's Nishiki marketplace is Kazuo Akamatsu, (left) Chairman of the ALICO Japan Agents Federation, the association for Japanese

full-service agents who sell ALICO's products. Mr. Akamatsu, one of ALICO Japan's top-selling agents for many years, meets with a client to discuss a seminar the Agents Federation plans to conduct for policyholders.

Review of Operations

(CONTINUED)

In an uncertain market environment such as prevailed during 1998, product innovation and the ability to move quickly to meet changing customer needs are essential. AIA responded well, introducing new products such as the "currency-indexed rider" that protects the U.S. dollar value of a life policy's benefit proceeds in the face of local currency weakness. In Malaysia, AIA launched a new endowment policy that provides financial security amid the uncertain financial environment.

AIA also continued to develop its distribution network in 1998. With an agency force that numbers over 60,000, AIA has an unmatched capability. During the year, AIA added to its agency network, standing out as one of the few companies offering promising career opportunities in the current economic climate. It also developed new distribution channels, establishing a regional data base in Hong Kong to cross-market additional products to current AIA policyholders. Other distribution initiatives included the creation of a bancassurance unit to capitalize on opportunities to market insurance products through banks and bank affiliates.

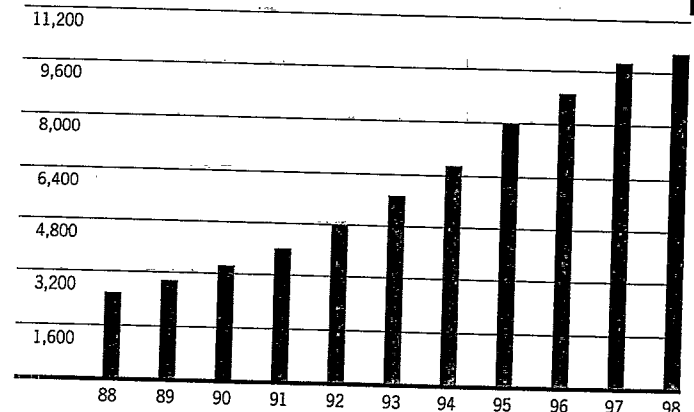
Providing outstanding customer service is an AIA hallmark. In 1998, a wide range of quality service initiatives were undertaken. AIA Shanghai's role as a provider of quality service was recognized as it was awarded ISO 9002 recognition, the first life insurer to obtain this certification in China. In Hong Kong, a customer call center was set up to provide one-stop customer service for the entire AIA network, as well as for other AIG member companies.

AIA Hong Kong, the leading life insurer in its market, expanded its operations substantially as its agency force grew by 40 percent. First year premiums rose 15 percent in an overall stagnant market. AIA had an excellent year in China. Operating results in Shanghai were very strong, as first year premiums increased by 120 percent, and six new agency offices were opened. In Guangzhou, first year premiums tripled and the size of the agency force more than doubled.



Life Premiums

(Millions of dollars)





Following extensive renovations, the AIA Building at No. 17 The Bund in Shanghai (in background) was opened in May 1998. The neoclassical structure, which first housed AIG predecessor companies beginning in 1927, now serves as headquarters for the rapidly expanding life operations

of AIA Shanghai, whose agency force grew by more than 50 percent during 1998. Ding Huiming (left) is a team leader of the agency force, as well as a top producer. Above, she explains the terms of a life insurance policy to a new client.

Review of Operations

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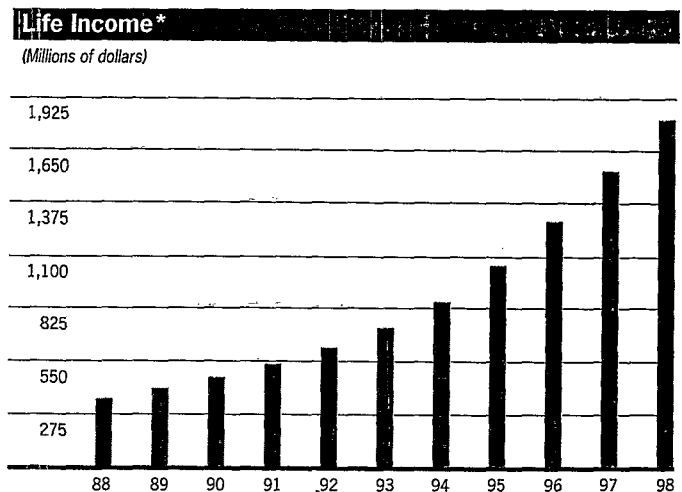
AIA Singapore reported good results, with its new business market share rising in 1998. Accounting for nearly one-half of total market volume, AIA is the largest life insurer in Singapore. At AIA Thailand, the nation's largest life insurer, market share for individual life rose and AIA continued to command the top market position in group insurance. AIA Malaysia focused on expanding its operations into the provinces, where life insurance penetration is low but growth potential is high.

Nan Shan Life Insurance Company, Ltd. (Nan Shan), Taiwan's third largest life insurer with an agency force of 33,000, is one of AIG's best performing life companies. Nan Shan's first year premiums were particularly strong, ranking the company second in the industry by this measure. Nan Shan was recognized for the sixth straight year by an industry publication as "the most recommended" life company with the "best agents" in the industry.

Philippine American Life and General Insurance Company (Philamlife), the largest life insurance company in the Philippines, reported good original currency premium growth and a strong increase in operating income. Philamlife extended its market reach through alternative distribution channels including direct mail, telemarketing and bancassurance, and the company's personal lines business expanded into the auto sector.

American Life Insurance Company (ALICO), which is among the largest international life insurance companies in the world, operates in over 50 countries worldwide, including Japan, Western, Central and Eastern Europe, the Middle East, Africa, South Asia, Latin America and the Caribbean. ALICO's branches and subsidiaries market a wide range of life and health products through a network of approximately 22,000 agents and brokers. The ALICO product line includes traditional life, accident and health, group insurance for large and small organizations, pensions and annuities. ALICO holds a AAA financial strength rating from Standard & Poor's, the highest that S&P awards, and in 1998 Moody's awarded ALICO its highest insurance financial strength rating, Aaa. ALICO had an excellent year, with record premiums and operating income.

ALICO is the largest full line foreign life insurer in Japan. The company achieved strong 1998 results, outperforming the Japanese life insurance industry by a significant margin, in a year in which the accumulation of bad debts caused some large and well-known Japanese financial institutions to fail or be merged out of existence. ALICO Japan emphasized its financial strength and stability, especially its Triple-A ratings and its AIG affiliation. The company's 1998 performance reflected its focus on new product development, agent and sales force recruiting and training, and operating efficiency.



* Before realized capital gains.



Greece has long been one of ALICO's most successful European markets, and in 1999, ALICO Greece will celebrate its 35th anniversary. Top-selling ALICO Greece agent Pantelis Papadomanolakis (right) exemplifies the dedication and high professional standards that distinguish the ALICO sales force, and consistently result in ALICO being ranked among the top life insurance companies in Greece. At a café in Athens' Plaka district, Mr. Papadomanolakis reviews the benefits of an individual life insurance policy with a policyholder.

Review of Operations

(CONTINUED)

ALICO's Western European operations experienced solid growth in 1998. In the United Kingdom, ALICO expanded its position in the industry and became a market leader in guaranteed income bonds and index-linked bonds. In the French market, ALICO S.A., operating as AIG Vie, achieved good growth across its primary lines of business.

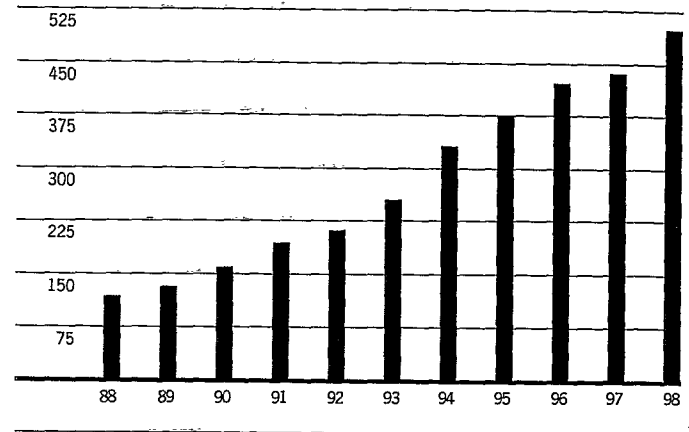
In the Iberia, Central and Eastern Europe Region, First American Polish Life Insurance and Reinsurance Company, S.A. (AMPLICO Life), had an outstanding year. ALICO's and AMPLICO Life's applications for pension company and pension fund licenses were approved in 1998 and early 1999, respectively. In Slovakia, First American Slovak Insurance Company, in only its third full year of operation, saw its agency sales force grow to over 500. ALICO and its partner, EFG Bank Group, acquired a major interest in the Bulgarian Post Bank, A.D., while late in 1998, ALICO received authorization to open a life company in Romania. ALICO Greece continued to provide technical support to the Region's operations and maintained its strong position in the Greek life market.

In the Middle East, ALICO established a solid base for future growth through increases in the agency force, introduction of new and innovative insurance plans, and expansion of a managed care network. ALICO is the leading life insurance company in the Middle East. Early in 1999, ALICO received permission to increase its ownership in Pharaonic American Life Insurance Company—ALICO to 75 percent, becoming the first foreign investor in Egypt to own a majority share of a local insurance company.

In Latin America, Unibanco Seguros S.A., AIG's insurance joint venture in Brazil with Unibanco, completed its first full year of operations. ALICO expanded its relationship with Unibanco in 1998 by agreeing to acquire from Unibanco a 50 percent interest in Prever S.A. Seguros e Previdencia (Prever), the second largest private pension company in Brazil. El Pacifico Vida, ALICO's joint venture life insurance operation in Peru, had strong growth in premiums and ALICO's life company in Colombia, Colmena AIG Compania de Seguros de Vida S.A., had good first year premium growth.

Life Insurance In-Force

(Billions of dollars)



The **AIG Life Companies (U.S.)** had an excellent year, as premium income grew 33 percent to a record level of \$738 million and operating income rose 20 percent to an all-time high of \$150 million. Assets surpassed \$15 billion and total life insurance in-force exceeded \$61 billion by year-end. Annuity and pension sales were particularly strong. The Accident and Health Division had good growth in its corporate accident, special risk and leisure travel business. The two principal U.S. life companies, American International Life Assurance Company of New York and AIG Life Insurance Company, hold Triple-A financial strength ratings, with the support of AIG, from both Standard & Poor's and Moody's.

AIG's **Global Pension Division** achieved strong growth in both revenues and operating income. In the United States, the Division is a leader in the terminal funding market. The Division reported good results in its Asian pension business, where recognition of AIG's financial strength provides a competitive advantage, particularly in Thailand. In Europe, the new alliance between Unionvita S.p.A., ALICO's Italian joint venture life company, and San Paolo IMI, Italy's largest investment bank, produced a significant increase in new pension business.

The **Group Management Division (GMD)**, which provides employee benefit programs to multinational and indigenous companies worldwide, reached record premium levels in 1998. GMD wrote the group life account for Wal-Mart Stores, Inc., which became effective in early 1999. Covering nearly 550,000 lives, this is believed to be the largest such contract written in the United States. AIA United HealthCare, AIG's managed care joint venture with United HealthCare Limited in Hong Kong, completed its first full year of operations with the acquisition of a number of major multinational clients and the addition of new products for the small group and middle markets. In Brazil, GMD launched Unibanco AIG Saude, a third-party administrator and preferred provider organization with 20,000 network providers across Brazil.

Review of Operations

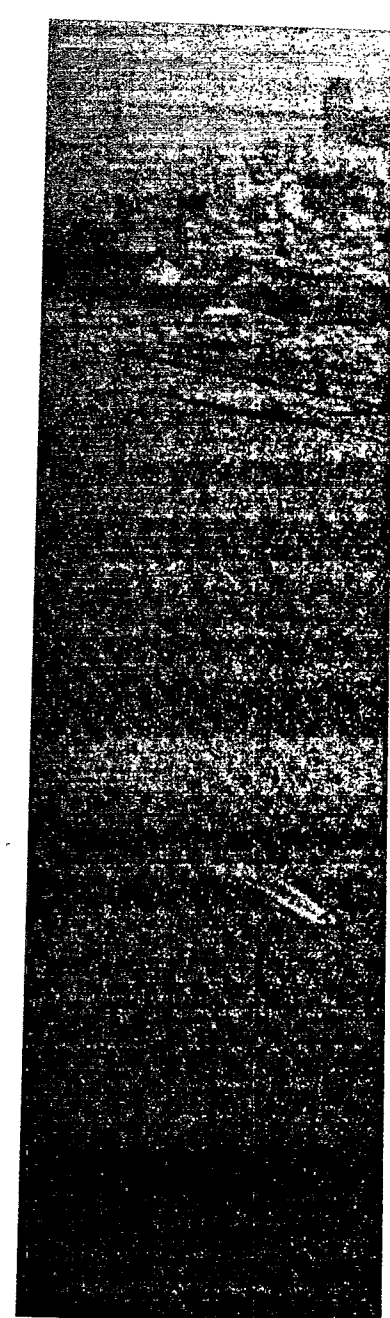
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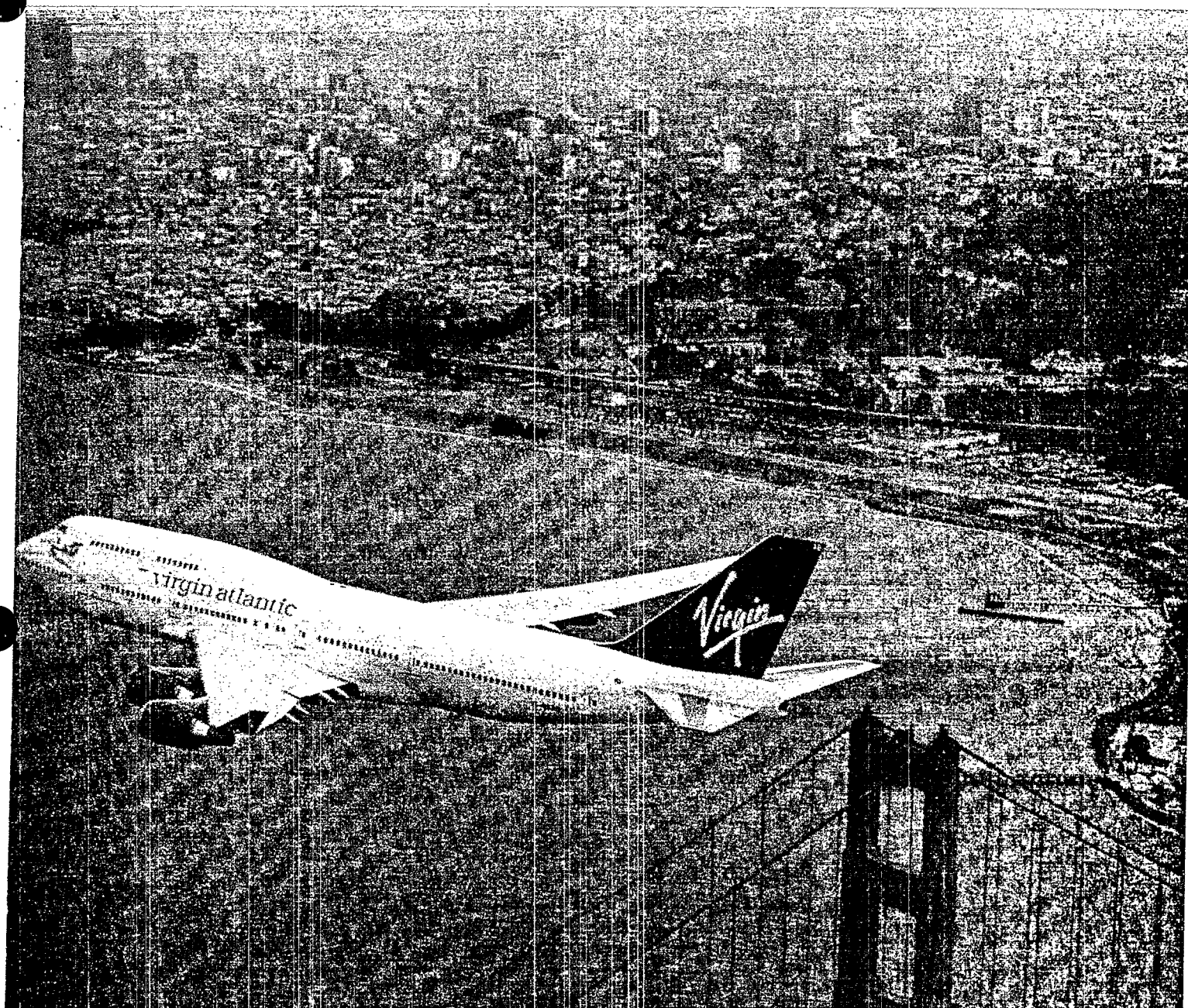
The Financial Services Group consists of businesses that complement AIG's core insurance business, and those where we can add value and achieve a competitive advantage by capitalizing on our Triple-A ratings, global network, entrepreneurial culture and financial structuring expertise. The principal companies in the Group are International Lease Finance Corporation, AIG Financial Products Corp., AIG Trading Group Inc., AIG Global Investment Group, Inc. and AIG Consumer Finance Group, Inc. In 1998, operating income for Financial Services rose 30 percent.

| Financial Services | | |
|---------------------------|---------|---------|
| (in millions) | 1998 | 1997 |
| Operating Income | \$913.1 | \$701.3 |

International Lease Finance Corporation (ILFC), the international market leader in the leasing and remarketing of advanced technology commercial jet aircraft to airlines around the world, achieved record financial results in 1998, while expanding all core business activities—aircraft leasing, sales and portfolio management. Revenues rose 7.8 percent to \$2 billion and operating profit increased 29.6 percent to \$495.7 million. At year-end, ILFC's modern jet portfolio consisted of 352 owned and 60 managed aircraft, with orders outstanding for aircraft to be delivered through the year 2006.

During 1998, ILFC expanded its worldwide leadership position in new aircraft leasing by becoming a launch customer for the Airbus A340-500/600 long-range aircraft designed to seat 315 to 385 passengers and scheduled to be in service in the year 2002. Additionally, ILFC placed further orders for Boeing 737, 757, 767 and 777 aircraft, as well as incremental orders for the Airbus A320 family of aircraft.





In 1998, ILFC celebrated its 25th anniversary. The first company to offer operating leases in the history of the commercial aircraft industry, ILFC has benefited as airlines increasingly choose to take advantage of the financial flexibility offered by leasing

as part of a fleet operating strategy. ILFC has played a key role in Virgin Atlantic Airways' growth since 1989, when ILFC leased two Boeing 747-200 aircraft to the international carrier. Currently, the airline leases three Airbus A340-300 aircraft from ILFC, and four

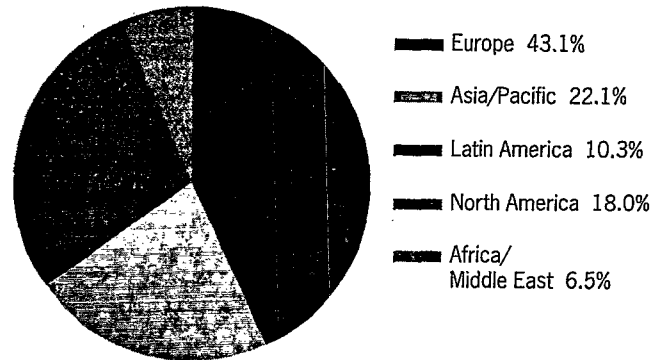
Boeing 747-400s, including the one shown here over San Francisco Bay. Virgin's ILFC-leased aircraft serve routes throughout its global network, from its base in London to cities in North America, Europe and Asia.

Review of Operations

(CONTINUED)

Strong demand in Europe offset the soft aircraft market in Asia. In its largest transaction of the year, ILFC leased 16 new Airbus A319/320 aircraft to Iberia Airlines, the flag carrier of Spain. In 1998, ILFC formed a number of new customer relationships with airlines throughout the world. In addition to Iberia, other new customers in Europe included Alitalia and Meridiana Airlines, both of Italy, Olympic Airways of Greece, Color Air of Norway, Lithuanian Airlines, Futura Airlines of Spain, and Star Airlines of France. In the Middle East, ILFC's new customers include Royal Jordanian Airlines, and in the Caribbean, Air Jamaica. In North America, ILFC re-established its relationship with Canadian Airlines International, with the lease placement of three aircraft under ILFC management.

ILFC 1998 Revenues by Region



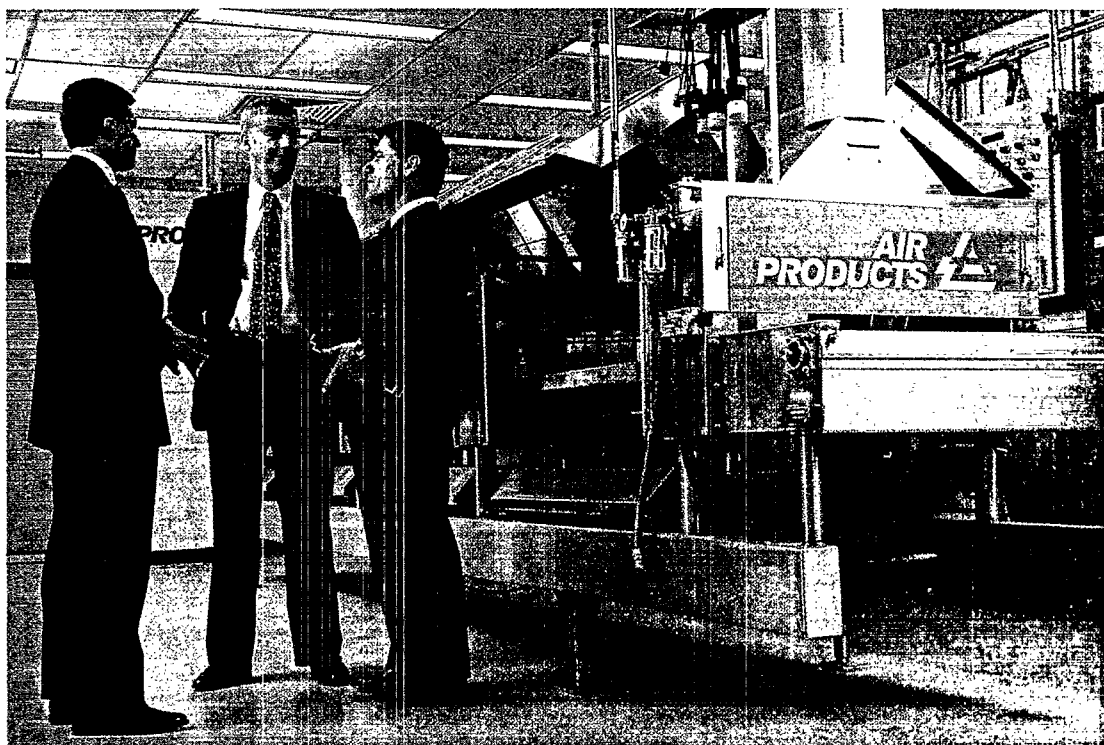
ILFC significantly expanded its business with existing customers during the year. ILFC signed lease agreements with Air France for five new Airbus A319 and two new Boeing 777 aircraft, making the airline one of ILFC's largest customers. ILFC concluded six lease agreements with TWA for Boeing and McDonnell Douglas aircraft. ILFC also signed agreements for two new Boeing 747-400 aircraft to Air New Zealand, one of the company's oldest customers. Additional aircraft were placed with a variety of existing customers in Asia and the Middle East, as well as Europe and North and South America.

During 1998, ILFC took delivery of 59 new aircraft, sold 31 aircraft and 15 engines from its portfolio, and placed 108 aircraft on lease. A number of the aircraft ILFC sold were put under ILFC management via the company's growing portfolio management business.

AIG Financial Products Corp. (AIGFP) and its subsidiaries engage as principal in a wide variety of standard and customized interest rate, currency, equity and credit product transactions with top-tier corporations, financial institutions, governments, agencies and institutional investors around the world. AIGFP helps clients raise domestic and cross-border capital, manage debt efficiently, hedge foreign exchange exposures, and optimize investments in global equity markets. Its expertise in legal, regulatory, accounting and tax matters facilitates corporate finance transactions for clients, including those transactions arising from acquisitions and divestitures, overseas expansion and joint venture activities. AIGFP also raises funds through municipal reinvestment contracts and other private and public security offerings, investing the proceeds in a diversified portfolio of high-grade securities. Its wide range of transactions benefits from AIG's Triple-A debt rating.

AIGFP has its headquarters in Westport, Connecticut, and offices in Hong Kong, Tokyo, London and Paris. AIGFP operates in Europe as Banque AIG, a fully licensed, Triple-A rated French bank.

Air Products and Chemicals, Inc. is an international supplier of industrial gases and related equipment, and specialty and intermediate chemicals, with annual sales of nearly \$5 billion. AIGFP's broad-based relationship with Air Products encompasses products utilized in the company's debt portfolio management program, as well as in its currency risk management program. At Air Products' frozen food research and development laboratory in Pennsylvania, an AIGFP executive discusses the details of an upcoming transaction with Air Products' treasury officers.



AIGFP had an excellent year in 1998, with strong results from its core business lines. Structured and client-specific interest rate, currency and equity products continued to provide a solid foundation to AIGFP's earnings. In Europe, AIGFP executed several transactions that benefited clients as most Western European currencies and interest rates converged at year-end into the euro. Business was particularly strong in North America, led by innovative products for corporate, insurance, pension and leasing clients. AIGFP signaled its growing presence in the global credit derivatives market through several transactions with financial institutions seeking cost-effective mitigation of risk in their loan portfolios.

The year 1998 was characterized by volatility in financial markets, particularly in August and September, as stock prices fell sharply following the Russian debt default, interest rate spreads widened, and liquidity evaporated. This increased volatility in fixed income and equity markets provided AIGFP with the opportunity to create innovative financing and investment structures that allowed clients to capitalize on these market conditions. Market dislocations also served to highlight and validate AIGFP's low risk tolerance and rigorous risk management.

Review of Operations

(CONTINUED)

AIG Trading Group Inc. (AIGTG), through its subsidiaries, engages in hedged trading and market making in foreign exchange, interest rates, and base and precious metals. It provides risk management services to multinational corporations, financial institutions, commercial producers and users, institutional investors and sovereign entities. AIGTG operates through a worldwide network of offices including its Greenwich, Connecticut headquarters, London, Paris, Geneva, Hong Kong, Singapore, Johannesburg and Toronto. AIGTG had a reasonable year in 1998, considering the extremely difficult conditions in many of the markets in which it operates.

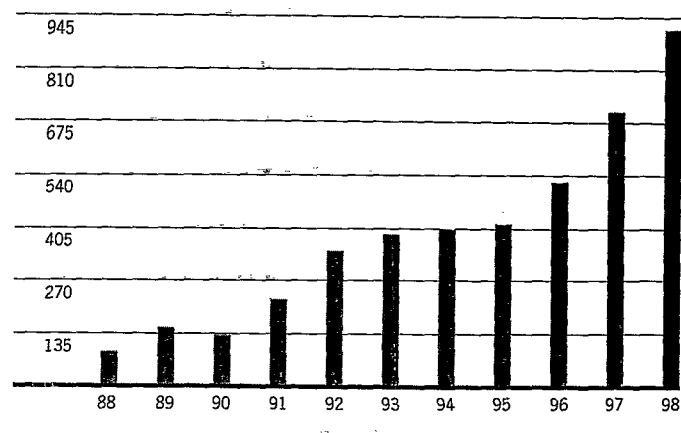
AIGTG's foreign exchange, interest rate and metals businesses are conducted through AIG International Inc. (AIGI). In foreign exchange, AIGI is a first-tier market maker in spot, forward and options transactions. An active dealer in emerging market currencies and interest rate products, AIGI profitably weathered the turbulence in these markets during the latter part of 1998. AIGI's commitment to market making and producing dynamic political-economic research has enabled it to continue to expand its customer base in a highly competitive environment. In 1998, AIGI continued its leading role in structured metals transactions, and helped manage or restructure the hedge books of several major producers. AIGI's base metals business also achieved significant growth.

In early 1999, AIGI and Dow Jones Indexes entered into an agreement to jointly market the Dow Jones-AIG Commodity Index (DJ-AIGCISM). This index uniquely weights individual commodities to provide institutional investors with a diversified benchmark for commodities as an asset class. The DJ-AIGCI appears daily in *The Wall Street Journal*.

AIG International Asset Management, Inc. (AIGIAM), AIGTG's asset management subsidiary, manages alternative investments in a variety of categories. It experienced substantial growth in 1998, doubling assets under management to approximately \$1.3 billion for a client base that spans 35 countries with more than 250 investors, including central banks, commercial banks and pension funds. AIGIAM's products seek to provide attractive, consistent returns that are not correlated to traditional fixed income and equity markets.

Financial Services Operating Income

(Millions of dollars)



AIG Global Investment Group, Inc. and various other investment management subsidiaries of AIG manage nearly \$14 billion of third-party institutional, retail, and fund assets on a global basis, in addition to the \$144.93 billion of AIG assets described in the "Investments" section (pages 48-50). These subsidiaries are responsible for product design and origination, investment management, marketing and distribution of third-party asset management products, including direct investment, retail mutual funds, institutional accounts, and real estate investment, development and management.

AIG's investment management products and businesses continued to expand around the world. In 1998, a joint venture was completed with International Finance Corporation and Dyer & Blair (Africa) Limited, a Kenyan stock brokerage firm, to focus on the pension, institutional and retail markets of East Africa. By year-end, the new company, AIG Global Investment Company (East Africa), Limited, commenced operations. Also completed during the year was a joint venture to distribute asset management products to the pension, institutional and retail markets of the Czech Republic.

AIG subsidiaries also develop, market and manage several direct investment funds for emerging markets. AIG is rapidly becoming a leading sponsor of private equity funds for emerging markets, with approximately \$7 billion of fund assets under management. A core tenet of AIG's investment philosophy is that the best investment decisions are made by people who have an in-depth understanding of local markets and economies. Accordingly, AIG's direct investment capabilities consist of specialized professionals based in more than 15 countries, many of whom are local nationals of the countries in which AIG invests. In 1998, four private equity funds were closed: the AIG Global Emerging Markets Fund, with capital commitments of approximately \$1 billion; the AIG Silk Road Fund, Limited with \$70 million; the AIG New Europe Fund, L.P. with \$270 million; and the AIG Asian Opportunity Fund, L.P. with \$650 million. In early 1999, the AIG Southern Cone Fund, L.P. held its first closing with \$130 million in capital commitments.

AIG's real estate investment management subsidiary is responsible for the investment, development and management of real estate on a global basis, as well as managing the worldwide portfolio of AIG-owned properties. Recent investments included retail and property development projects, joint venture development of over 3,000 apartment units in the United States, and start up of a property development company in Eastern Europe. Additionally, it sponsored and began managing the AIG French Property Fund B.V. with committed capital of more than \$210 million.

Review of Operations

(CONTINUED)

AIG Private Bank Ltd., AIG's Zurich-based private banking subsidiary, formerly known as UeberseeBank AG, specializes in providing asset management and private banking services for a worldwide clientele. In addition to Zurich, it has a branch office in Geneva, and representative offices in Lugano, Hong Kong and Singapore. By adopting the AIG name, AIG Private Bank will emphasize its close connection to other AIG companies and realize the value of AIG's global identity. During the year, the bank established AIG Global Investment Corp. (Switzerland) A.G., a wholly-owned subsidiary which will provide global asset management and investment advisory services to private and institutional clients.

AIG Consumer Finance Group, Inc. (AIGCFG), through its subsidiaries, is engaged in developing a worldwide consumer finance business, with a primary emphasis on emerging markets. AIGCFG expanded its operations in 1998, completing acquisitions in Poland, Argentina and Thailand. In Poland, AIG acquired Bank Podlaski S.A., renamed AIG Bank Polska S.A., as well as a majority share in Credit Leasing Assistance, S.A., a marketing intermediary. In Argentina, the Group purchased a majority stake in Compania Financiera Argentina, S.A., an Argentine finance company. AIGCFG also completed its majority acquisition of Bangkok Investment Public Company, Limited, a consumer finance company with a significant share of the Thai auto finance market, and renamed it AIG Finance (Thailand) Public Company, Limited. AIG's flagship finance company in Hong Kong, SPC Credit, Ltd., remained profitable despite sharply fluctuating interest rates caused by the economic turmoil in Southeast Asia. In the Philippines, 1998 was marked by the launch of AIG's first credit card.

In addition to the new credit card, AIGCFG's products include a wide range of personal, auto and mortgage loans, consumer durables financing, and a variety of deposit and savings products. AIGCFG markets its products through branches, advanced telemarketing, agents, direct mail and financial intermediaries. In Southeast Asia, its initiatives are linked to AIG's life and general insurance operations, where the AIG name lends strong support and market acceptance.

A.I. Credit Corp., one of the largest premium finance companies in the United States, reported a slight reduction in premium finance volume in 1998, due to continued rate weakness in the commercial insurance premium marketplace.



In 1998, AIG Consumer Finance Group, Inc. launched AIG's first credit card in the Philippines. The AIG card is closely tied to AIG's insurance operations in the Philippines, where the Philam name provides strong support and cross-selling opportunities. New and innovative features distinguish the AIG card from

others in the Filipino credit card market, beginning with the telephone application process, a service based on AIG's advanced call center and credit scoring technology. Leveraging the Philam relationship, the AIG credit card was also the first to include free outpatient medical check-ups as part of its service,

as well as offering cardholders the opportunity to purchase a comprehensive medical insurance plan at a substantial discount. In Manila, an AIG cardholder purchases guidebooks, magazines and maps of the Philippine provinces at a hotel gift shop.

Review of Operations

(CONTINUED)

Investments

AIG's invested assets totaled \$144.93 billion at year-end 1998, compared to \$122.45 billion at year-end 1997, an increase of 18.4 percent. Of this total, 27 percent is derived from general insurance operations, 33 percent from life insurance, 39 percent from financial services and less than one percent from other sources. General insurance net investment income rose 18.3 percent in 1998 to \$2.19 billion, while life insurance net investment income increased 11.6 percent to \$3.23 billion.

Total general insurance invested assets rose 22.1 percent in 1998 to \$38.88 billion at year-end. Domestic General invested assets were \$31.03 billion, while Foreign General invested assets amounted to \$7.85 billion. Worldwide general insurance cash flow was \$2.0 billion, with 74.0 percent of the total, or \$1.44 billion, generated by domestic operations.

Domestic General net investment income rose 18.1 percent to \$1.75 billion, comprising 80.0 percent of total general insurance net investment income. Tax-exempt municipal bond purchases totaled \$776.2 million. These purchases had an average maturity of 18.6 years and a yield to maturity of 5.06 percent. The tax-exempt bond portfolio totaled \$16.4 billion, with an average coupon of 5.90 percent, an average effective maturity of 10.8 years and a yield to maturity of 5.96 percent.

Composition of Consolidated Invested Assets at December 31, 1998



| | | |
|---|--|-------|
| ■ | Taxable fixed maturities | 32.8% |
| ■ | Tax-exempt fixed maturities | 9.8% |
| ■ | Equity securities | 4.1% |
| ■ | Flight equipment | 11.3% |
| ■ | Other financial services assets | 26.1% |
| ■ | Mortgage loans, policy & collateral loans, and real estate | 6.8% |
| ■ | Cash & other short term investments | 9.1% |

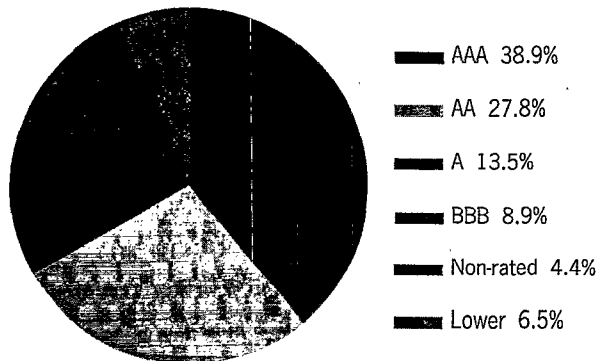
The Domestic General taxable bond portfolio totaled \$6.64 billion, consisting of U.S. treasury bonds and notes, other high grade securities, and high yield corporate bonds. In 1998, the U.S. Treasury portfolio had a total return of 10.49 percent, compared to the benchmark Merrill Lynch Government Index return of 10.03 percent.

The U.S. equity portfolio, which totaled \$2.82 billion at year-end, accounted for 9.1 percent of total Domestic General invested assets. AIG's domestic private investment portfolio was carried at a cost of \$618 million and had a market value of \$766 million at year-end 1997. During 1998, AIG received \$175 million in income and capital gains from this portfolio, net of fees and expenses, as well as \$144 million in capital distributions. As a result of the reinvestment of portfolio cash flows and new capital invested of \$311 million, this portfolio was carried at a cost of \$786 million with a market value of \$1.01 billion at year-end 1998.

Net investment income produced by Foreign General insurance operations amounted to \$438.1 million, an increase of 18.7 percent over 1997. Foreign General cash flow was \$508.0 million, with \$176 million invested in direct equity investments, and \$63 million in the Eurodollar and Yankee bond markets.

Life insurance invested assets were \$48.72 billion at year-end, an increase of 18.7 percent over year-end 1997. Foreign life investments totaled \$35.74 billion, or 73.4 percent of the total, and are mainly in the country of origin, where life insurance is frequently the principal savings vehicle for the local population. The longer duration of these life liabilities permits a more flexible and longer term investment policy. Net investment income generated by life insurance operations amounted to \$3.23 billion, with foreign life operations contributing \$2.31 billion, or 71.5 percent of the total.

Domestic General and Life Insurance Bond Portfolio Ratings



Review of Operations

(CONTINUED)

Domestic life investments are concentrated in high grade fixed income securities. The investment portfolio of \$12.97 billion at year-end was comprised 56 percent of high grade corporate bonds and U.S. Treasury securities, 9 percent of collateralized mortgage obligations with no derivative holdings, 8 percent of policy loans, 8 percent of high grade commercial mortgages, 7 percent of below-investment grade bonds, and 12 percent of cash, equities and miscellaneous invested assets.

AIG's real estate investments at year-end amounted to \$1.55 billion, with the majority of these properties used for company occupancy purposes. The current market value of these properties considerably exceeds their carrying value. During 1998, AIG originated \$424 million of new domestic commercial mortgage loans. At year-end, AIG's worldwide mortgage loan portfolio was \$3.29 billion, of which commercial mortgages in the United States represented \$1.02 billion. At that date, no U.S. loans were in default and only a nominal amount of foreign loans were in default. The foreign mortgage loan portfolio of \$2.27 billion consists principally of mortgage loans in European, Asian and Latin American countries where AIG has a strong life insurance presence.

Financial services invested assets amounted to \$56.62 billion at year-end, of which \$27.59 billion, or 48.7 percent, related to AIG Financial Products Corp. The majority of AIGFP's assets represents its investment of proceeds from the issuance of guaranteed investment agreements, notes and other bonds in short and medium term securities of high credit quality.

Aircraft owned by ILFC and under lease to commercial airlines around the world are the other principal component of financial services invested assets. At year-end, the net book value of the fleet totaled \$16.33 billion. All of ILFC's fleet consists of new generation, technologically advanced aircraft that are in the highest demand from its airline customers and are expected to remain so. The customer base is also well diversified among airlines and geographic areas, with no single customer accounting for more than 10 percent of ILFC's worldwide revenues in any of the last three years.

General and Life Insurance Invested Assets

December 31, 1998

(in millions)

| General Insurance | Domestic | Foreign | Total |
|-----------------------------------|------------------|-----------------|------------------|
| Fixed maturities | \$ 23,055 | \$ 5,542 | \$ 28,597 |
| Equity securities | 2,820 | 1,103 | 3,923 |
| Mortgage loans on real estate | — | 15 | 15 |
| Policy loans | — | 6 | 6 |
| Collateral and guaranteed loans | — | 49 | 49 |
| Short-term investments and cash | 510 | 363 | 873 |
| Other invested assets | 4,026 | 433 | 4,459 |
| Investment income due and accrued | 430 | 138 | 568 |
| Real estate | 188 | 205 | 393 |
| Total | \$ 31,029 | \$ 7,854 | \$ 38,883 |

| Life Insurance | Domestic | Foreign | Total |
|-----------------------------------|------------------|------------------|------------------|
| Fixed maturities | \$ 9,402 | \$ 23,761 | \$ 33,163 |
| Equity securities | 59 | 1,658 | 1,717 |
| Mortgage loans on real estate | 1,013 | 1,734 | 2,747 |
| Policy loans | 1,028 | 1,510 | 2,538 |
| Collateral and guaranteed loans | — | 1,115 | 1,115 |
| Short-term investments and cash | 553 | 3,486 | 4,039 |
| Other invested assets | 706 | 720 | 1,426 |
| Investment income due and accrued | 177 | 723 | 900 |
| Real estate | 34 | 1,036 | 1,070 |
| Total | \$ 12,972 | \$ 35,743 | \$ 48,715 |



SunAmerica

THE RETIREMENT SPECIALIST

SunAmerica Inc., which became the newest member of the AIG family of companies on January 1, 1999, is a leader in one of the country's fastest-growing markets: retirement savings. In 1998, SunAmerica earned fees or investment income on approximately \$110 billion of assets and provided 1.8 million Americans with a broad range of high-quality retirement savings products and investment services. In its 1998 fiscal year, SunAmerica's total sales increased 60 percent to a record \$8.5 billion.

Products and Services

SunAmerica offers a wide variety of products and services including:

- fixed and variable annuities
- mutual funds
- investment counseling
- trust services
- guaranteed investment contracts

The SunAmerica family of companies includes:

SunAmerica Life Companies — The SunAmerica Life Companies (SunAmerica Life, Anchor National, CalAmerica, First SunAmerica and SunAmerica National) collectively rank among the largest issuers of fixed and variable annuities and guaranteed investment contracts in the United States and rank in the top 2 percent of all U.S. life insurers, based on assets.

SunAmerica Asset Management Corp. — SAAMCO manages a family of 21 retail mutual funds, with more than \$3 billion of assets.

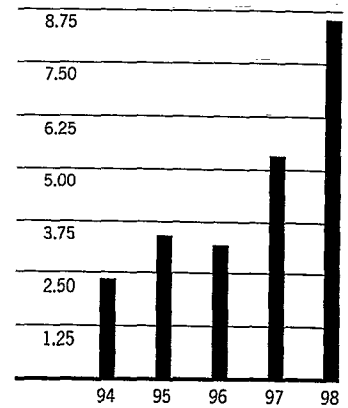
Resources Trust Company — RTC, which focuses exclusively on self-directed retirement plans, provides trust services to more than 200,000 retirement accounts, with combined assets of \$13 billion.

The SunAmerica Financial Network — SunAmerica's six wholly owned broker-dealers (Royal Alliance, SunAmerica Securities, Advantage Capital, FSC Securities, Sentra Securities, and Spelman & Co.) comprise the nation's largest network of independent registered representatives, with more than 9,700 representatives under contract.



Total Sales*

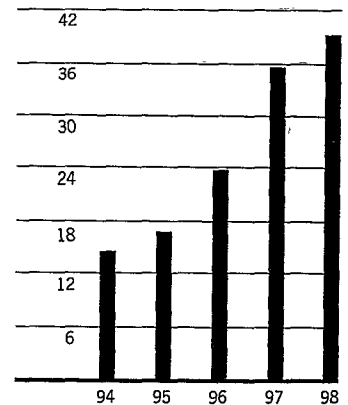
(Billions of dollars)



* For years ended September 30.

Total Assets*

(Billions of dollars)



* As of September 30.

right to left

Eli Broad
Chairman and
Chief Executive Officer

Jay S. Wintrob
Vice Chairman and
Chief Operating Officer