Assured Guaranty Ltd. (AGO)
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Second Quarter 2016 Earnings Call

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Thank you operator. And thank you all for joining Assured Guaranty for our 2016 second quarter financial results conference call.

Today's presentation is made pursuant to the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995.

The presentation may contain forward-looking statements about our new business and credit outlooks, market conditions, credit spreads, financial ratings, loss reserves, financial results or other items that may affect our future results.

These statements are subject to change due to new information or future events. Therefore, you should not place undue reliance on them, as we do not undertake any obligation to publicly update or revise them, except as required by law.

If you are listening to the replay of this call, or if you are reading a transcript of the call, please note that our statements made today may have been updated since this call.

Please refer to the Investor Information section of our website for our recent presentations, SEC filings, most current financial filings, and for the risk factors.

This presentation also includes references to non-GAAP financial measures. We present the GAAP financial measures most directly comparable to the non-GAAP financial measures referenced in this presentation, as well as a reconciliation between such GAAP and non-GAAP financial measures, in our current financial supplement and equity investor presentation which are on our website at AssuredGuaranty.com.

In turning to the presentation, our speakers today are Dominic Frederico, President and Chief Executive Officer of Assured Guaranty Ltd., and Rob Bailenson, our Chief Financial Officer. After their remarks, we will open the call to your questions. As the webcast is not enabled for Q&A, please dial in to the call if you would like to a ask question.

I will now turn the call over to Dominic.

Dominic Frederico, President and Chief Executive Officer

Thank you, Robert, and welcome to everyone joining today's call.

Assured Guaranty's performance continued to be strong in the second quarter of 2016. Rob will give you details about the financial results later on this call. I am going to focus my remarks on our new business production and some significant events that have occurred since our last earnings call, including our acquisition of CIFG, developments related to Puerto Rico, and an enhanced initiative to build the company's value through alternative investments.

In the municipal new-issue bond market in the second quarter of 2016, insured penetration was 6% of the total par volume. In looking at one of our principal target markets, transactions with single-A underlying ratings, nearly a quarter of that par and 57% of the transactions came to market with insurance. This level of penetration was remarkable considering we saw the lowest interest rate environment in the history of the bond insurance industry.

Before the second quarter began, we had never seen AAA 30-year muni rates below 2.47%, but during the quarter, rates descended well below that level, even before the global flight to quality caused by global events including the Brexit vote on June 23rd. By June 30th, rates were down to 2.02%. The next day they pierced the 2% level, and there is little evidence rates will approach historically normal levels this year, as some central banks continue to hold their rates near zero.

In this kind of environment, all bond insurers see their pricing power constrained. At Assured Guaranty, we know it is imperative to remain disciplined not only in our credit selection but also in our pricing, because poor pricing can lock in low returns for years to come. During the second quarter, we continued to focus on transactions that not only meet our underwriting standards, but also produce appropriate returns. Investors, as well as municipal issuers and their advisors, have a stake in the long-term viability of the insurer they use, and that means they understand it is necessary for their insurer to run a profitable business in order to remain financially strong. Rating agencies consider profitability a factor in determining ratings, and knowledgeable fixed income investors also know how important this is.

At about this time last year, we looked at the current pricing in the market and made a decision to more appropriately price our guaranty by raising our prices. That has clearly cost us some market share, but by comparing U.S. municipal transactions closed in the second quarters of 2016 and 2015, you can see that we generated 32% more present value premiums, or PVP, even though we guaranteed 22% less par. First half over first half, PVP was up 68% while par insured was down 11%, and our S&P risk-adjusted pricing was significantly higher this year. Last week, S&P wrote that our municipal risk-adjusted pricing, or “RAP,” ratio was above S&P’s 4% target in both the fourth quarter of 2015 and the first quarter of 2016. Importantly, only Assured Guaranty surpassed that target according to S&P’s July 27th reports on all three active guarantors.

And while we focused on appropriately pricing the new business we wrote, we still continued to lead the industry in the primary municipal bond market, insuring 267 small, medium and large new issues, which represented 53% of the insured par sold in the second quarter.

In the municipal secondary market during the quarter, our $393 million of par insured was 52% higher than in the second quarter of 2015. For the first half, our secondary market volume is running 87% ahead of last year’s pace, and our secondary market PVP is more than three times what it was in the first half of last year.

Most notably, on June 1st, we provided primary-market insurance for 17% of the $2.4 billion of bonds issued to finance the redevelopment of the LaGuardia Airport Central Terminal B. In addition to that $412 million of insured bonds, by the end of July, we had written secondary market bond insurance policies on another $80 million of this landmark domestic infrastructure financing. The demand for our guaranty on this transaction demonstrates the value we provide in larger financings and reflects the significant demand for our product among institutional investors.

A unique advantage we have over other guarantors is that we continue to provide credit enhancement for issuers in the U.S. public finance, U.S. and international structured finance, and international infrastructure finance markets, which is also something S&P identified as a competitive strength in its recent report on us. With experienced underwriters pursuing appropriate transactions in international infrastructure and global structured finance, we do not depend solely on one market to generate insurance premiums, and we are able to further diversify our insured risk profile.

In international infrastructure business in the second quarter, we provided a European institutional investor with secondary-market guarantees on five bond issues by four different regulated UK utility companies, and we made progress on other transactions with the potential to close this year.

Although some activity was delayed in the run-up to and aftermath of the Brexit vote, these transactions are generally on track. The need to finance infrastructure improvements will not go away, and there is continued demand for the replacement of other legacy insurers on non-U.S. transactions.

In addition to producing new financial guaranty business, we build the value of the company through alternative strategies, one of which is acquisitions. On July 1st, we acquired the legacy bond insurer CIFG, which we merged into our Assured Guaranty Corp. subsidiary. Like our previous acquisitions of Radian Asset Assurance and FSA, this acquisition strengthens our franchise by adding a solid book of financial guaranty business and increasing shareholders' equity and statutory capital. At the same time, CIFG-insured bondholders now enjoy greater security and enhanced market liquidity for their insured bonds. The impact of the CIFG acquisition will not be reflected in our financial statements until our third quarter reporting, but Rob will give you additional financial details.

A bonus of buying CIFG is that we have been able to bring on board a few key members of its team. In particular, CIFG's former President and CEO David Buzen will lead a new Alternative Investments department to coordinate our search for new ways to deploy some of our excess capital, including further acquisitions and other opportunities that will benefit from our core competencies in credit, insurance and financial markets.

We plan to continue other aspects of our capital management program, including share repurchases, in parallel with the activities of this new department. Of course, we will take no action that could impair our ability to maintain or improve our ratings or trading value of our insured bonds, nor will we interfere with our capital management strategy – specifically, our share buybacks.

With regard to Puerto Rico, we have had a few eventful months since our last call. A bipartisan bill was enacted by Congress to address Puerto Rico's claim that it needed access to restructuring legislation in order to reach sustainable settlements with creditors. We worked tirelessly to educate legislators about the dangers of establishing a precedent of retroactive impairment of creditors, and the bill the President signed into law on June 30 requires that any restructuring of Commonwealth bonds respect the priorities and liens provided for under Puerto Rico law; preempts Puerto Rico's Moratorium law; provides a framework for consensual restructuring of individual bond issues; and provides some sorely needed supervision for the Commonwealth's government through a financial oversight board with real authority. The PROMESA bill enacted into law is an improvement over some of the earlier drafts, but it does leave room for a potential judicial cramdown, stays creditor legal actions and, critically, does not provide any economic assistance to the island.

Senator Orrin Hatch is leading a task force of the House and Senate members who have been appointed to look into how the Federal government can assist in, or at least remove Federal obstacles to, Puerto Rico's economic recovery. It's too early to tell whether that will lead to helpful legislation.

The PROMESA oversight board, whose members have not yet been appointed, will soon have the authority to approve budgets and restructuring agreements and will have the sole authority to invoke the bankruptcy-like provisions of the Act. It is therefore essential that its members have a deep respect for the rule of law, a solid understanding of economics and public finance, and the ability and willingness to take into account how their actions could affect the cost of public borrowings nationwide.

Characteristically, the current Puerto Rican administration wasted no time in abusing the Act's stay on creditor legal actions, and the absence of the Control Board, to violate PROMESA, as well as its own constitution and laws, and the U.S. constitution and bankruptcy code. The Governor issued unlawful Executive Orders, which PROMESA explicitly preempts, that caused defaults on $911 million of July 1 debt service payments, including $779 million of constitutionally protected general obligation bonds. The suspension of debt service payments pointedly disregards the existing lawful priorities and liens that PROMESA specifically states must be respected.

Assured Guaranty paid net claims of $184 million to cover shortfalls on Puerto Rico's July 1st debt service, almost all for general obligation bonds that Puerto Rico's constitution says must be paid not only before all other debt payments but before all other expenses of any kind. We spent the last week of June trying to get information from Puerto Rico about potential claim payments for July 1, so preparations for claim payment transfers could be made, but were given no information before the claims were received. Nevertheless, within a day of receipt of each claim, funds were transferred to the appropriate trustee, paying agent or secondary-market custodian. No Assured Guaranty insured bondholder had to take any action to receive timely payment of their scheduled principal or interest.

Also, on the day PROMESA was enacted into law, Governor Padilla extended the state of emergency he had declared in May that diverted pledged toll revenues of the Puerto Rico Highways and Transportation Authority to purposes other than the payment of the HTA bonds, purportedly using the diverted toll revenues to fund expenses of its own operations that are subordinated to the HTA bonds and to pay for quote so-called "essential services" on behalf of the Commonwealth. Remarkably, these "essential services" are defined to include payments to the financially distressed Government Development Bank for Puerto Rico, an affiliated, subordinated, inside creditor of HTA. This is another violation of PROMESA, which prohibits transfers of funds outside the ordinary course of business or that are inconsistent with Puerto Rico law. In total, including both the clawback of pledged taxes and the diversion of toll revenues, the Commonwealth had unlawfully misdirected by June 30th approximately $326 million in revenues pledged to the payment of HTA's revenue bonds.

On July 21st, we filed a motion and form of complaint in the Federal District Court in Puerto Rico seeking relief from the PROMESA stay and, upon such relief, seeking a declaration that Puerto Rico's Moratorium law is preempted by Federal bankruptcy law and that the Executive Orders diverting the pledged toll revenues are preempted by PROMESA and violate the U.S.

Constitution. Additionally, it seeks damages for the value of toll revenues diverted and injunctive relief prohibiting the defendants from taking any further action under the Executive Orders.

In a few months, we will presumably have a functioning oversight board. Whether the current government will be willing and able to provide reliable, audited financial information so the board can do the job remains to be seen. Once that information is available and all parties can reliably analyze the financial condition of the various obligors, the chances for successful consensual settlements will improve.

On a positive note, I can say that the securitization transition charges and provisional PREPA rate increases required to move the PREPA Restructuring Support Agreement forward were authorized and the parties continue to work toward obtaining investment grade ratings for the securitization bonds and implementing the restructuring transaction contemplated by the PREPA agreement.

Finally, I want to call your attention to two recent rating agency reports that reflect our commitment to maintaining exceptional financial strength. On July 8th, Kroll Bond Rating Agency affirmed its AA+ financial strength rating, with a stable outlook, for our MAC subsidiary, taking into account MAC's full repayment of the surplus notes it issued to partially fund its initial capitalization, and the resulting transfer of $400 million plus accrued interest to AGM and AGC. In the two-and-three-quarters years from July of 2013 to March 2016, MAC produced over $227 million of statutory net income, making it unnecessary to leave the surplus notes outstanding. The level of stress losses that MAC was able to satisfy under the Kroll's Monte Carlo simulation model was equivalent to a AAA stress scenario. Keep in mind that AA+ is the highest rating Kroll has said it is likely to assign to a financial guarantor in the current environment. Kroll affirmed the same AA+ stable rating for AGM last December.

And most recently, on July 27th, S&P released the report I mentioned earlier, in which it affirmed its AA stable financial strength ratings on all of our insurance and reinsurance subsidiaries, citing, among other things:

- Very strong capital adequacy
- Our strong competitive position, built on market leadership and a well-diversified underwriting strategy
- Our leadership position in the U.S. public finance market in terms of both par insured and premiums written
- Our high quality, liquid investment portfolio and conservative investment strategy
- Experienced management with a well-defined strategy and a track record of success
- And our strong operating performance and enterprise risk management

In determining the AA Stable ratings, one of S&P's scenario analyses assumed every one of our Puerto Rico obligations would default, and that we would pay claims totaling 100% of that debt service over the next four years. They also looked at other scenarios to see whether our capital adequacy score would change if our claim payments totaled 15, 25, 35 or 45 percent of our total Puerto Rican debt service over the entire lives of the transactions. The result, in all scenarios, was that these losses would not change our S&P capital adequacy score.

Importantly, S&P noted favorably our greater flexibility than other guarantors to capitalize on growth trends and pricing opportunities because we write guarantees in a broader range of U.S. public finance sectors and have additional revenue sources provided by our global infrastructure and structured finance businesses.

I will now turn the call over to Rob.

Robert Bailenson - Chief Financial Officer

Thank you, Dominic, and good morning to everyone on the call.

In the second quarter of 2016, operating income was $139 million, compared with $278 million in the second quarter of 2015. Second quarter 2015 operating income was higher than 2016 primarily due to the gains recognized upon the acquisition of Radian Asset.

Financial guaranty insurance and credit derivative revenues were $248 million in the second quarter of 2016, compared with $259 million in the second quarter of 2015. This included accelerations of $136 million in the second quarter of 2016, compared with $98 million in the second quarter of 2015.

Economic loss development in the second quarter of 2016 was $22 million, which reflects $109 million of loss development in the public finance sector, and a benefit of $87 million in the structured finance sector.

Economic loss development in the public finance sector was driven by increases in expected losses on various Puerto Rico credits. As Dominic mentioned, we made claim payments on general obligation and Public Building Authority exposures, which are reflected in the June 30th probability weighted loss estimates.

In the structured finance sector, RMBS was the primary source of the economic benefit, and included the positive effect of accelerating claim payments as a means of mitigating losses on a number of Alt-A transactions.

The effect of declining discount rates embedded in loss development in the second quarter of 2016 was an aggregate loss of $45 million, comprised of $29 million in the public finance sector, and $16 million in the structured finance sector.

Shareholder dividends, repurchases, debt service and operating expenses of the holding companies are supported by the dividend capacity of our insurance subsidiaries. We now have approximately $21 million in cash and investments at the Bermuda holding company and approximately $103 million at the US holding companies.

In the second quarter of 2016, share repurchases totaled $60 million, or 2.3 million shares, with an average purchase price of $25.73 per share. As of today, $150 million remains available to repurchase shares under our current authorization.

Operating shareholders' equity per share at June 30, 2016 was $45.26. This is 17 percent higher than it would have been without the cumulative share repurchases since 2013.

Adjusted book value per share reached $61.86, which is 24 percent higher than it would have been without these repurchases.

As Dominic mentioned, we acquired CIFG on July 1st and we are in the process of allocating the purchase price to the fair value of acquired assets and liabilities. As of June 30th, 2016, CIFG had approximately $640 million of statutory capital and an insured portfolio of about $4.4

billion in net par, which is $900 million lower than previously reported due to the termination of various CDS transactions.

The acquisition will be accretive to Assured Guaranty's earnings per share, operating shareholders' equity and adjusted book value. We now expect that CIFG will increase AGC's statutory capital by $325 to $350 million by the end of 2016.

I'll now turn the call over to our operator, to give you the instructions for the Q&A period.

Question and Answer Session

Operator

(Operator Instructions) Chas Tyson – Keefe, Bruyette & Woods, Inc. - Analyst, KBW.

Chas Tyson – Keefe, Bruyette & Woods, Inc. – Analyst

Hey, guys. Good morning. I just wanted to go back to the S&P report comments that you guys made earlier and your excess capital. What's a good way to think about what kind of Puerto Rico charges are implicit within the $2.6 billion of excess capital? I know the total muni capital charge is around 17% or 18%. Just wondering what's factored into your capital adequacy and the excess capital you have.

Dominic Frederico – Assured Guaranty Ltd. – President and CEO

Well, okay; you were breaking up, and I'm going to ask you one question real quick, Chas. Were you able to hear us clearly when we did our presentation?

Chas Tyson – Keefe, Bruyette & Woods, Inc. – Analyst

Yes. There is an echo (technical difficulty)

Dominic Frederico – Assured Guaranty Ltd. – President and CEO

Okay, because you come across like stutter or so, like --

Rob Bailenson – Assured Guaranty Ltd. – CFO

Choppy.

Dominic Frederico – Assured Guaranty Ltd. – President and CEO

-- digitized. I think your question was, in the $2.6 billion of excess capital, what was the amount of Puerto Rico losses included in that? And understand, for the S&P model it's a scenario analysis that basically does a three-year projection and then a four-year depression scenario, which they run various loss conditions within that.

As we said in the call, they took loss conditions from a low point of a 15% loss to a 45% loss across all; and they also did a five-year nonpayment of any principal and interest. And under that scenario they still came out and concluded the $2.6 billion of excess capital. So I'm sure it's a statistical sampling across all potential conditions.

Chas Tyson – Keefe, Bruyette & Woods, Inc. – Analyst

Okay. Can you talk about the alternative [investments] a little bit more and also rank-order your uses of capital? How much capital must be allocated to that?

Dominic Frederico – Assured Guaranty Ltd. – President and CEO

Okay, you're going to have to repeat the back end of it. So the first part of the question was alternative investments. What was the second part of the question?

Chas Tyson – Keefe, Bruyette & Woods, Inc. – Analyst

On rank-ordering the use of capital.

Dominic Frederico – Assured Guaranty Ltd. – President and CEO

Okay. Remember first and foremost we have excess capital. Not all of that excess capital is able to be immediately transferred to the use for other purposes at the holding company level. Therefore, we have a challenge relative to capital that although is excess cannot be moved easily or on any sort of an immediate basis to provide other sources. Therefore, the challenge to us is to invest that capital at both good risk-adjusted return scenarios to provide further earnings for utilization of capital.

Number two, there is other capital that we can use relative to investments in alternative structures, but they still count as investments. So that it still is capital, stays capital; it's just how we diversify our investment portfolio.

We say it's got to meet our core competencies. So first and foremost we have always been a higher evaluator of outside asset managers. This is kind of one part of that; no different, as we look for other asset managers with a different asset class to provide greater returns but still subject to our investment scrutiny, follow-up, control process, etc.

Number two, when we talk about core competencies you have to understand, as we look at Assured Guaranty, we do consider ourselves experts in the evaluation of credit across many borders, therefore, firms that invest in classes of credit that go according to our own specific strength. For instance, in the CLO market, where we were at one time probably the largest insurers of CLO and have a very sound fundamental knowledge of the entire market including CLO managers, performance, etc., if we find opportunities to invest in those areas, we will take advantage of that as well.

Number two, who knows the municipal market better than we do in terms of municipal credit? So where we find pockets of investment opportunity that deal with core credit competencies in the Company, we believe we can utilize our expertise, the amount of personnel, and bringing in some further outside services, be they other managers, other companies, etc., we believe we can deliver better returns than obviously leaving the capital only to earn the investment portfolio rate of return.

Chas Tyson – Keefe, Bruyette & Woods, Inc. – Analyst

Okay. I'll speak slowly because it seems to work better that way. But on the acquisitions front as well, what are you guys seeing there? And on particular acquisitions or particular assets that may be international, like MBIA UK, where it's a little more difficult to get cash out, how do you guys think about things like that?

Dominic Frederico – Assured Guaranty Ltd. – President and CEO

Well, let me go back to a little bit also part of your question. When you said -- I thought you asked for prioritization. First and foremost, we believe that the share repurchases is still the most accretive form and best use of capital we have in the firm. So to the extent that we can continue to free up capital from the operating companies, the predominant core use of that funds is in the share buybacks; and we have a specific capital management strategy and aggregate objective on an annual basis that we would like to achieve. Number one.

Number two, the second-best use, which really typically doesn't use a lot of capital or quickly returns the capital, is acquisitions. Obviously, the acquisitions have further benefits in that they strengthen our franchise, widen our touch of the marketplace, and further emphasize the value of the Assured guaranty. So acquisitions obviously become number two.

And then number three, as we said, to the extent we've got capital that is trapped for the time being, but we'd like to see it perform at a lot higher level of return, we do have core competencies within the company that would like to utilize some of that trapped capital.

And, remember, I use the term capital, but capital is a multifaceted calculation. As we look at our capital requirements, first and foremost we look at the S&P capital, and that has a very specific calculation, and it treats certain assets as capital or not capital.

So in that case, as you look at an alternative, depending on what its rating, what the asset class is, it could either count or not count on the S&P model. However, you still get the investment income; but that's for another day, another story.

When you go to regulatory capital, these investments in some cases will count as capital. So you're just really investing in a higher-return security as opposed to utilizing any of your capital.

So as I say, look at the three priorities; understand there is a differentiation when you get down to number three in terms of the alternative assets, as to whether it really affects capital or it doesn't. But once again, it's really trying to utilize, like we did when we bought Radian using AGC money. That was capital that we couldn't get out of AGC, and yet it was used to a very fine purpose of making a very accretive transaction. And we could argue technically or mathematically whether that was more accretive than a stock buyback at the time. So we still look at the prioritization of buyback, acquisitions, and then alternative assets.

Chas Tyson – Keefe, Bruyette & Woods, Inc. – Analyst

Okay. Thanks very much, guys.

Dominic Frederico – Assured Guaranty Ltd. – President and CEO

You're welcome.

Operator

Brian Meredith, UBS.

Brian Meredith – UBS – Analyst

Yes, thanks. Good morning, everybody. Dominic, just following on to that question, any color or thoughts on potential for special dividends up to the holding company, given what's going on with the Puerto Rico GOs? Or will we have to hold off on that for a while? And is there any other way that you can extract capital out of the insurance operations?

Dominic Frederico – Assured Guaranty Ltd. – President and CEO

Well, Brian, as we said, A, priority number one is capital management through share buyback. We've also said that, based on the most recent S&P report, we think that provides further support and credible evidence that even under every stress scenario that they could come up with under Puerto Rico, we are more than adequately capitalized -- and overcapitalized at the AAA level of capital.

As I said on previous calls, to me, it would've been nice to have further resolution on Puerto Rico, but to me that's not a necessity. To me, the Puerto Rican resolution, not resolution, default, not default, only really affects the size of the potential special dividend request. I think we have a goal in mind or what I'll call a strategy in terms of what amount of share buybacks we want to achieve in 2016. That buyback at that level would require a special dividend; therefore it is our continued desire to be in the position to request such a dividend to allow us to get the necessary funds to continue the level of share buyback that we think is reasonable, responsible, maintains our strong ratings, and yet still provides our shareholders an adequate valuation of what we believe the shares are worth and try to move it to that area.

Brian Meredith – UBS – Analyst

Is that level of share buyback comparable to the previous couple years?

Dominic Frederico – Assured Guaranty Ltd. – President and CEO

Yes, it is.

Brian Meredith – UBS – Analyst

Great. That's helpful. Then, Dominic, just curious. Could you talk a little bit about the pipeline right now, what it looks like? Granted I know it was good volume on PVP this quarter, but rates have been down for a little while now. Have we seen a slowdown at all?

Dominic Frederico – Assured Guaranty Ltd. – President and CEO

We have not. In certain cases -- so let's break it down by the three markets; and understand we're the only guarantor that really faces all three markets. We are very pleased with the pipeline on the US public finance side; but in terms of repeatable or consistent market, that's probably our most consistent market and has historically been that way even through the financial crisis, etc., and we see a good pipeline, which differentiates Assured, is obviously the larger transactions.

We see very significant transactions on the calendar that we would expect a good opportunity to participate in, from providing some level of reinsurance on those issues. So we're very pleased and happy with the pipeline.

If you look at us year-over-year, we're way ahead, relatively speaking, on the public finance production and yet in spite of a lower par insured, because of our view to raise pricing and make sure we're getting adequately compensated for utilizing the capital.

If we go to the US structured finance market, once again, although production has been slow this year, and once again impeded by interest rates, there is a good calendar there as well. And we're very optimistic and positive about that marketplace and opportunity.

As a matter of fact, in this current Board meeting that we just concluded, one of the things we did -- we do an education session every year for the Board. We did a full analysis of the US structured finance market specifically to address where we see opportunities that we think it's opportunistic enough for us to continue to provide capital, staffing, etc., in that market, with the right profitability opportunities going forward. I think we concluded there absolutely is; and as I said, we're very pleased with the pipeline.

Because as we see that business continue to evolve, one of its past business segments, which was capital relief programs, where you're basically wrapping assets owned by financial institutions that take a capital charge, or give them a capital charge benefit. As you can well appreciate, in today's world of both banking and insurance and especially based on new regulations for Solvency II and Basel III, the amount of new capital being requested or additional capital charges being assessed, we're now seeing a real pickup and increase relative to us performing that kind of capital mitigation type of structure or program that used to be a huge part of our business going back say five or six years.

Then last but not least, in the international markets, we've had good success this year in the international markets. We do have a strong pipeline going through this year and going into next, because you know those deals take quite a long period of time. So it's still lumpy on any quarter-to-quarter basis. And all we're seeing from that is a potential delay, but not the loss of opportunities even as it respects UK infrastructure and UK utilities. So we still are very optimistic, and we see a good pipeline building.

I do expect that we're going to see further concerns in the US public finance market caused by Puerto Rico's behavior. Because although we know that there was a default on July 1st, a lot of that default went into uninsured bondholders' hands, and I would believe that those uninsured bondholders are going to be asking the question of whoever their advisor is: Why didn't I get paid? And when they get that horrible answer -- that's because you had uninsured bonds -- I would hope their response is going to be: Well, don't ever give me an uninsured bond again. If I'm going to be in this market, I want to make sure I'm protected.

And that's why we're here and we see value in that. I hope that will generate additional opportunities as we go through the second half of this year.

Brian Meredith – UBS – Analyst

Great. Thanks for the answers, Dominic.

Dominic Frederico – Assured Guaranty Ltd. – President and CEO

You’re welcome.

Operator

(Operator Instructions) Geoffrey Dunn, Dowling & Partners.

Geoffrey Dunn – Dowling & Partners Securities – Analyst

Thanks. Good morning, guys. I've got a couple questions. First, PREPA. It looks like we're one step away from a completed restructuring. What needs to happen before mid-December to get this new replacement bond issued and get this thing off your BIG list?

Dominic Frederico – Assured Guaranty Ltd. – President and CEO

Well, we're two steps away, to be very honest with you. First step is it's got to be validated by the local Puerto Rican court. And that's just a precautionary measure to make sure this doesn't get further tested or challenged going on in the future. So it's a typical step done in the municipal, especially in the troubled or restructured municipal finance area.

And that's currently being done, I think this month. We expect to see some pushback, but in the main, because this does accomplish a lot of positive things for a lot of people, it will by and large get the validation.

Then the second step, which is I think the one you're referring to, it's got to get an investment-grade rating. I think the validation is a key step to getting the investment-grade rating, so you know that it can't be challenged.

And then lastly, we believe it will probably go through PROMESA as well, only to the extent that PROMESA then gives it the certainty to basically – I hate to use the term cramdown, but there is a segment of creditors here that have not agreed to the deal, that will then be, once again, forced to be accepted by all creditors on a 100% basis. So I think there's really three steps that we have to go through.

I think the value of getting it done is still overwhelmingly positive. And if I'm the Control Board I think it would be awful nice to be able to say I dealt with $9 billion of potential debt service on behalf of all Puerto Rican entities very quickly and got it resolved to the acceptance of everybody involved in the marketplace.

So three things I think happen. It really depends on how fast the Control Board is able to get in place, staff up, and begin to analyze information for that last step of the acceptance by all creditors.

But I think step one and step two -- one, on the validation should be relatively shortly; two, on the rating agency, I would assume that they're going to go pretty much hand-in-hand. And three, relative to the Control Board and PROMESA in terms of them accepting it and validating it as well, that probably takes more towards the end of the year.

Geoffrey Dunn – Dowling & Partners Securities – Analyst

Will you guys issue a statement when the validation is finished?

Dominic Frederico - Assured Guaranty Ltd. - President and CEO

Sure.

Geoffrey Dunn – Dowling & Partners Securities – Analyst

Okay. Then the follow-up question is related --

Dominic Frederico - Assured Guaranty Ltd. - President and CEO

I mean, it will be public anyway. So, I'm sure... we won't have to be the first ones to say that; it will be something that will be caught by everyone.

Geoffrey Dunn – Dowling & Partners Securities – Analyst

All right, perfect. My follow-up on that is, with PROMESA, part of this is how fast can the Control Board get in place. I can't say that anything in Washington seems to move quickly, so what's the risk that this spills into 2017 just because the government can't get its act together and put this Board together?

Dominic Frederico - Assured Guaranty Ltd. - President and CEO

If you said to me would that be the worst thing that could happen to us, I would say no, Geoff. I know you'd like to see this thing resolve itself, get out of BIG, because it does lower the size pretty quickly. And now that we're finally under $5 billion number, because we basically got net debt service of about $200 million as of year-end, so we're about $4.8 billion, it would be nice to have another $700 million or so fall off the schedule.

But -- I can't read what you said there -- oh, there is a new governor coming in. I think it's in his best interest to move this thing along as well. So I think maybe that will add some further acceleration. But to the extent that this slips to 2017, the only real critical piece of that would be the payment due on January 1st. At least we can say with history, every time we've had a payment come up – starting with last January, this July – we've been able to get through those things to everyone's satisfaction and with a positive outcome for all specific bondholders in that scenario. So would I be troubled by 2017? No. Would I like to see it go out in 2016? Absolutely. Either way I think we think we're in really good position. I think it's a deal that makes sense. I think it's a deal that should go and will go through.

And therefore, we've got the patience and the time if necessary.

Geoffrey Dunn – Dowling & Partners Securities – Analyst

All right, and then last question. How does PROMESA affect your probability assessments on reserving? For example, you've got, I think, close to $200 million of constitutionally guaranteed payments coming up in the third quarter for Puerto Rico. If they don't pay it, is that really new news, given what they've already done, and that means you've already reserved for it?

Or does PROMESA provide you with different kind of probability analysis since there is more of a structure going forward? How does PROMESA change your quarterly assessment of reserves, and how does the July 1 default payment affect that assessment?

Dominic Frederico - Assured Guaranty Ltd. - President and CEO

Well, the July 1st default payment, I think does force you to go back. Because remember, on July 1st they did appear to have the option of paying the interest part of the debt service. So, you would say -- well, my assumption was they were going to probably pay interest.

The fact that they didn't -- although we still feel we have a high probability of recovery, because everything this gentleman has done as the governor is illegal, and he breaks every law except the law that he likes. Well, that's not the way we look at our laws and our constitution.

But once again there's a timing involved in that recovery. I think he's trying to threaten the market so that there theoretically would be a greater acceptance of discounts; and as you can see, we've held pretty firm on that. But remember, we're part of a bigger creditor pool.

So these actions do impact probability weighting, without any question. As you say, further acts now, after having had the July 1st default, should it affect probability weightings? Probably not.

If you say to me: Well, how do you evaluate PROMESA, positive or negative in the probability scenario? Because there is so much vagueness -- and it really is going to get down to not only the who but the actions of the Control Board -- it's a little hard to handicap that.

So we will still react to the information that we see and -- as obviously in the quarter we reacted and further increased reserves. And why? Because just in the scenario I described to you, there were scenarios that anticipated interest being paid.

When we didn't get interest being paid, that does create a different weighting to the probability analysis that we have to do relative to GAAP. And we continue to look at that.

If there's another further default on the same basis going forward, would I expect it to have a significant influence on probability? Probably not. But other actions could have taken place as well that would make us reconsider.

In the main, like I said, PROMESA has got some good things in it; it's got some bad things in it. And it really is going to get down to execution. So we still have a huge execution risk.

Geoffrey Dunn – Dowling & Partners Securities – Analyst

All right. So going forward, it's still -- we're still going to see a lot of volatility in the probability assessments and each incremental piece of news, despite having PROMESA in place?

Dominic Frederico - Assured Guaranty Ltd. - President and CEO

Yes, but we're not seeing that much volatility, Geoff. I mean obviously if you look at the quarter, yes; you say we had additional reserves. Rob specified those pretty clearly in terms of what the Puerto Rico impact was.

I could say it's not significant; other people could say it's significant. When you look at the totality of the $5 billion of where our reserves are, we're feeling very good about the adequacy of our reserves.

We think we are responsive to external information as to how we look at it and assess probabilities under the rules of GAAP. And accordingly, therefore, we'll take the necessary actions as we think are necessary.

Geoffrey Dunn – Dowling & Partners Securities – Analyst

Okay.

Rob Bailenson – Assured Guaranty Ltd. – CFO

And, Geoff, you have to look at each credit by credit. So actions that you see on the GOs are going to be -- we look at that scenario. And obviously, not paying interest was one thing that we looked at.

We also looked at Highways and Transportation. You can see that they were not given the toll revenue that they were expected to get, and that's why we have that lawsuit. So you look at that as a probability weighting estimate.

So you have to look at credit by credit what is happening.

Dominic Frederico – Assured Guaranty Ltd. – President and CEO

If you also, Geoff, to step back from the volatility or whatever you want to determine it, as we look at the rest of 2016 we really don't have a whole lot of payments due through the remainder of 2016. So this really becomes a 2017 issue.

I'm not so sure much can happen that's going to change anything in the rest of 2016, because you don't have that same exposure to repayment.

Geoffrey Dunn – Dowling & Partners Securities – Analyst

Okay, thanks.

Dominic Frederico - Assured Guaranty Ltd. - President and CEO

You're welcome.

Operator

Thank you. That does conclude the question-and-answer session. I'd like to turn the conference back over to Robert for any closing remarks.

Robert Tucker – Assured Guaranty Ltd. – Head of IR

Thank you, operator. I'd like to thank everyone for joining us on today's call. If you have additional questions, please feel free to give us a call. Thank you very much.