Transcript of Assured Guaranty Ltd.
Earnings Conference Call
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Managing Director of Investor Relations and Corporate Communications

Good morning and thank you for joining Assured Guaranty for our fourth quarter 2012 financial results conference call.

Today's presentation is made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. It may contain forward-looking statements about our new business and credit outlooks, market conditions, credit spreads, financial ratings, loss reserves, financial results, future reps and warranty settlement agreements 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 the 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.

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 ask a question.

I will now turn the call over to Dominic.

Dominic Frederico
President and Chief Executive Officer

Thank you Robert, and thank you all for your continued support of Assured Guaranty and for joining us on today's fourth quarter earnings call.

I am pleased to report that 2012 was another solid year for Assured Guaranty. Once again, we succeeded by executing our core strategies, which have consistently produced positive operating earnings and continue to create shareholder value.

These strategies led to significant accomplishments in 2012, specifically:

- We generated $535 million of operating income, our third year in a row with operating income in excess of $500 million.

- We increased operating shareholders' equity per share to a record level of $30.05 per share.

- We repurchased 2.1 million shares at an average price of $11.76, and the share price ended the year 21% higher at $14.23, and as of yesterday's close, it was 57% higher.

- We doubled our quarterly dividend to $0.09 per share early in the year and further raised it to $0.10 per share in the first quarter of 2013 for a total increase of 122%.

- We executed reassumption transactions with Radian Asset Assurance and with Tokio Marine & Nichido Fire Insurance Co. for a total economic benefit of $191 million.

- We produced a total of $210 million of PVP, insuring $16.8 billion of par direct and reinsured transactions. We accomplished this in a persistently unfavorable business environment caused by unprecedented low interest rates, tight credit spreads and uncertainty about our ratings caused by Moody's having us on review for three-quarters of the year. And we did it while consistently maintaining our rigorous underwriting and pricing standards.

- In U.S. public finance, we insured 1,770 new issues and secondary market positions during the year, representing $14.5 billion in par. Our penetration of new issues in our target market of single-A issuers was 30% of the transactions sold and 12% of par sold during the year.

- We also guaranteed $620 million of par in structured finance, which contributed $43 million of PVP.

- In our residential mortgage loss mitigation efforts, we caused providers of representations and warranties, or R&W, to pay or agree to pay approximately $500 million, including amounts related to two new R&W agreements signed during the year. This brings the total receipts and commitments from R&W providers to $2.9 billion to date.

- We also purchased $396 million of bonds we had previously insured, at an average cost of 63% of the par, which created approximately $250 million of the economic value. Such wrapped bond purchases mitigate losses, improve our excess capital position and increase future investment income.

- We agreed to terminate 53 policies totaling $4.1 billion of net par outstanding, while still collecting 96% of the expected premiums - further increasing our excess capital.

- We experienced improvement in our insured portfolio as structured finance transactions amortized and our overall below-investment-grade exposure decreased by 13% during the year.

- Finally, we lowered our insured leverage, with the ratio of statutory net par outstanding to qualified statutory capital declining 12%. Since the acquisition of AGM in 2009, that ratio has fallen by 41%.

Now I want to discuss two other recent developments – our victory in the Flagstar Bank case and Moody's failure to assign us financial strength ratings based on their published criteria instead of subjective speculation.

On February 5, Federal Judge Jed Rakoff awarded Assured Guaranty substantially all of the damages we sought for Flagstar's refusal to honor its RMBS rep and warranty repurchase obligations. We believe the ruling will be upheld if appealed, and we will receive approximately $90 million as compensation for claims paid to date, plus additional amounts to be determined by the court - which we estimate to be at least $20 million for interest, costs and attorneys' fees, in addition to amounts requested for future claims.

This is the first trial related to RMBS rep and warranty putbacks that has come to a final court ruling, and it sets a strong precedent in support of our industry in similar cases. The decision establishes clear liability as it relates to originators and securitizers of RMBS, and it articulates the responsibility of rep and warranty providers to honor contractual obligations to purchase defective mortgage loans.

Additionally, this decision, which definitively clarifies issues related to causation and statistical sampling, should prompt regulators, auditors and the boards of our remaining rep and warranty providers to seriously question their reserve levels and related disclosures. For example, we have put back $2.1 billion of defective loans to Credit Suisse and $2.4 billion to UBS utilizing the same process and control procedures that we used with the Flagstar portfolios. These amounts are based on collateral losses which are generally at least four times Assured Guaranty's projected bond losses on these portfolios. The amounts that we just discussed also exclude any further calculation of fees and interest like those that will be awarded to us in the Flagstar litigation.

Turning to Moody's, on January 17 they announced an unjustified downgrade of our financial strength rating. The next morning, we issued a five-page rebuttal detailing Moody's lack of transparency, contradictory explanations and disregard for their own capital model. It is on our website, and I urge you to read it.

On January 24, the flaws of Moody's rating process became even more obvious when they published a Credit Opinion on AGM containing a Financial Strength Scorecard - which lists the main factors used by Moody's to determine our financial strength rating and provides a score based on their published criteria for rating financial guaranty companies. Unlike the rating change announcement, which was widely distributed via a press release, the Credit Opinion was made available only to subscribers of Moody's research products. This new scorecard is comparable to the one they published ten months earlier on March 26, 2012, and the comparison is alarming.

On the 2012 scorecard, AGM had an overall rating score of Aa2, and Moody's then adjusted the overall rating down one notch – from Aa2 to Aa3 based on their speculative concerns over future qualitative issues of market demand and penetration.

Now, ten months later, the scorecard shows that the company earned a stronger rating score, resulting now in an overall rating of Aa1 - a notch higher than in March 2012, and one of the highest ratings a financial institution can achieve. But even though our current overall rating score is higher, Moody's adjusted the rating down, without proper justification, to come up with a lower overall adjusted rating of A2. So even though AGM got stronger based on Moody's own published ratings criteria, AGM was somehow downgraded, and significantly so.

Moody's made this four-notch adjustment without any of the transparency called for in their own Code of Professional Conduct. That code states that Moody's will publicly disclose "any material modifications to its rating methodologies and related significant practices, procedures and processes." It also specifies pre-implementation requests for comment and publication of sufficient information for a financial market professional to understand the basis for a credit rating. As the client, we can't understand the basis of the credit rating.

The absence of such disclosures renders the Moody's review process incomprehensible. It also does not comply with the Dodd-Frank Act's call to increase rating agency transparency and follow established procedures for changes in rating agency methodology. This kind of opaque and arbitrary behavior, where modeled results are discarded and a subjective valuation is applied, has prompted the Justice Department to bring a civil fraud suit against another rating agency.

As I previously stated, when capital and the quality of your insured portfolio no longer matter in regard to your financial strength rating, there is a serious problem with the process. Moody's unsupported and unjustified downgrade of Assured Guaranty adds to the mountain of evidence that there needs to be comprehensive regulation and oversight of the rating agencies.

Getting back to our 2012 activity, we also acquired MIAC, a financial guaranty company that was already licensed in 37 states and the District of Columbia. We renamed the company Municipal Assurance Corporation, and intend to begin writing U.S. municipal business in MAC this year.

I want to be clear that we are launching MAC to increase our municipal bond insurance penetration by expanding our current base of demand. The new company is simply an additional platform. AGM and AGC, both of which are rated AA- with a *Stable Outlook* by S&P, are key components of our business franchise and valuable brands. MAC will complement those brands and provide us with additional flexibility to address new market needs, while also providing new competitive positioning.

The launching of MAC is part of our permanent commitment to the U.S. public finance market, where we expect to see more opportunities as interest rates rise and credit spreads widen - as they eventually will. We will fund MAC internally and cede it a portfolio of municipal risks to leverage its capital base, provide earnings at inception and respond to clients looking for a new municipal-only platform.

We also believe our structured finance and international infrastructure businesses have significant potential. We continue to engage issuers and their advisors in the asset-backed market, as well as large financial institutions seeking credit protection for selected assets and more efficient capital management.

In infrastructure finance, we anticipate more international opportunities in 2013. In the U.K., the government is currently seeking to tap into the capital markets for alternative funding sources for public-private partnerships. We offer solutions that allow pension funds and life insurance companies to invest in capital market infrastructure financings.

We expect to be able to take advantage of the opportunities in all these markets because we have proven our financial strength and the value of our insurance time and again. Paying claims reliably and on time is indisputable proof of this, and we have done so for municipal investors in Jefferson County, Alabama; Harrisburg, Pennsylvania; and Stockton, California, all of which have declared or attempted to declare bankruptcy in a charged political atmosphere.

However, these public officials must recognize that it is their, or their predecessors' actions, that have caused their financial difficulties; and their behavior in dealing with these issues will have long-term consequences. While they have budgeted themselves into financial difficulty through unsustainable expenditures, they should not attempt to use creditors or bond insurers as scapegoats. When a municipality breaches the trust of its creditors – which often includes bondholders that reside and vote in that same community – it harms all of its constituents by limiting its access to the capital markets and increasing its funding costs, and potentially those of other municipalities.

We have seen that the vast majority of municipal issuers practice sound financial management, and that the ones we insure overwhelmingly value our ability to work with them to deal with any problems before they become serious. In each of the three cases I just mentioned, we attempted to work constructively with local authorities to negotiate an equitable resolution for all parties.

Looking forward, our goal remains to write as much quality business as possible that meets our strict underwriting and pricing standards. However, as long as interest rates remain low and credit spreads tight, pressure will be put on our ability to write large volumes of new business. This, combined with the runoff of our existing portfolio and our other capital-creating strategies, will continue to increase our excess capital position.

In January 2013, we announced a $200 million share repurchase program that will be financed entirely with holding company funds in order to preserve the capital strength of the operating companies. We will look to augment this repurchase program going forward as our capital levels become more redundant and we have the funds available at the holding company. We have developed strategies to increase holding company funds to be available for share repurchases in the future.

In closing, I thank our shareholders and policyholders for their continued support. As the economy recovers, Assured Guaranty is well positioned as the proven leader in bond insurance. We've demonstrated the fundamental demand for our product even when interest rates are at their lowest. We have shown we have the financial strength to effectively serve our target markets. And we clearly have the financial flexibility and the right mix of strategies to continue to create shareholder value. We look forward to protecting policyholders, saving issuers money and building value for shareholders in 2013 and beyond.

I will now turn the call over to Rob Bailenson for additional details regarding our financial results.

Robert Bailenson Chief Financial Officer

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

Fourth quarter 2012 operating income increased 7% to $184 million, or $0.95 cents per share, compared with $172 million, or $0.94 cents per share, in the fourth quarter of 2011.

The primary driver of the increase in operating income was premium accelerations, which totaled $153 million in the fourth quarter of 2012. This included $96 million from terminations. The remainder was attributable to refundings of public finance transactions due to the low interest rate environment. The comparable fourth quarter 2011 total premium accelerations were $48 million. In addition to the immediate benefit to operating income, terminations and refundings have the added benefit of deleveraging our insured portfolio and increasing excess capital, as reflected in the 12% decline in the statutory net par to qualified statutory capital ratio, which went from 95:1 at the end of 2011, to 84:1 at the end of 2012.

Net investment income is relatively flat compared with fourth quarter 2011. Our general portfolio reinvestment rate has declined in this low interest rate environment; however, our loss mitigation bonds, which are typically purchased at a discount, and produce relatively high yields have helped to offset this without taking on any incremental risk. The overall pre-tax book yield was 3.85% at December 31, 2012 and 4.00% at December 31, 2011. Excluding bonds purchased for loss mitigation purposes, pre-tax yield was 3.51% as of December 31, 2012, compared with 3.69% as of December 31, 2011.

Loss expense was $127 million for the quarter, compared with $82 million in the fourth quarter of 2011. U.S RMBS was the largest contributor of loss expense in both quarterly periods.

Loss expense is different from net economic loss development due to the amortization of unearned premium reserve on transactions with expected losses.

Net economic loss development was $73 million during the fourth quarter of 2012, driven primarily by U.S. RMBS, including additional provisions for loss adjustment expenses as we continue to pursue loss mitigation strategies, and changes in assumptions on one specific transaction. Offsetting these increases were improvements in the TruPS portfolio. Changes in risk-free rates were not significant during fourth quarter of 2012.

The Flagstar judgment earlier this month was an important development in affirming the Company's R&W claims and our rights to fully recover under breaches of R&W. We will continually update our loss and R&W models to reflect a range of possible scenarios, including a final decision with respect to the recoveries of interest and costs and any potential appeal.

Fourth quarter 2012 interest expense declined by $4 million to $21 million, which represents a recurring quarterly cost savings due to the retirement of the equity units. The effective tax rate on operating income was 26.3% for the fourth quarter of 2012, compared with 19.6% for the fourth quarter of 2011.

On a full year basis, the effective tax rate was 25.0% for 2012 and 24.4% for 2011, which is in line with our expectations. The effective tax rate on operating income varies from quarter to quarter due to the amount of income in different jurisdictions.

Operating shareholders' equity per share was $30 dollars and 5 cents per share, up 5% from year-end 2011, which equates to an operating ROE of 9.7%.

Adjusted book value increased by 2% to $9.2 billion, driven by new business, and by re-assumption agreements with Radian and Tokio Marine. On a per-share basis, ABV declined to $47 dollars and 17 cents per share, from $49 dollars and 32 cents per share at year end 2011, mainly due to the issuance of 13.4 million shares upon conversion of the equity units.

Full year 2012 operating income was $535 million, or $2 dollars and 81 cents per share, which compares with $601 million, or $3 dollars and 24 cents per share. Operating income in 2012 includes an after-tax loss on Greek sovereign exposures of $136 million, which was partially offset by after tax commutation gains of $53 million related to the Radian and Tokio transactions.

With respect to the Moody's downgrade, I would also like to point out that the Company had commitments for 47 new U.S. municipal issues that had sold with our insurance, but had not yet closed, at the time of Moody’s announcement. All of those transactions, which aggregate to $385 million in par, have closed, or are in the process of closing, with no pricing concessions.

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

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now begin the question-and-answer session. And the first question comes from Mark Palmer with BTIG.

Mark Palmer: Good morning.

Dominic Frederico: Good morning, Mark.

Mark Palmer: Has the company seen any change in the willingness of counterparties, who had previously been reluctant to negotiate on R&W to come to the table as a result of the Flagstar ruling?

Dominic Frederico: I'd say in general, Mark, the people that we had reasonable discussions with, continue and maybe, there's a little bit more sense of urgency, but less of that than you would normally have thought, based on as we believe, the completeness of the Flagstar ruling. And especially, I've referred to the leverage in our deals, to settle with Assured Guaranty would still expose some of these counterparties to other claims by other bond holders, but obviously those bond holders are not part of our, what I'd call contracted relationship group. Therefore, don't have the same rights, and there's a very public case, which I don't need to quote that you can see the difference between an insurance settlement and potentially open market or third-party private label investor settlements.

And therefore, the significant leverage for us, still kind of surprises us that there isn't more of a sense of urgency when these banks, and we're talking specifically here at UBS and Credit Suisse, have significant multibillion dollar exposures where the Assured loss is obviously a percentage of that, and therefore we believe it makes the most sense to deal with the party that has the contractual rights, but not as much as you would think. So we'll continue to monitor that and obviously we hope to continue to be able to successfully negotiate settlements, but at least we proven if you want to take this all the way to the court room, we are more than happy to do that and we've been quite confident in our rights, and therefore ultimate remedies and if that's the way this will go, Assured has obviously the liquidity, the financial wherewithal, to be able to stand there and meet the requirements and ultimately get the full value of our settlements.

Mark Palmer: Okay. One other question, what is the status of the company's efforts to bring on an additional rating agency?

Dominic Frederico: Those efforts continue as you could appreciate. We have to be comfortable with their methodologies to make sure that there is proper disclosure that they're going to be done in accordance with the regulations that exist albeit rather scant at the time. And obviously we'd like to make sure that these ratings will be consistent over time, so that we're not going to be put in any reactionary position. So our plan is to have that happen in 2013 and whether it's one or two additional ratings, we'll see how that plays out but you can assume we're working very hard and our folks to deal in the rating agency area continue to provide data to them, they get further feedback et cetera from the parties that we're discussing ratings with.

Mark Palmer: Very good. Thanks very much.

Dominic Frederico: You're welcome.

Operator: Thank you. And the next question comes from Geoff Gribling from Caspian Capital.

Geoff: Hey, guys.

Dominic Frederico: Good morning.

Geoff: Good morning. So, first of all, I wanted to thank you for preparing the Detroit slide in the slide deck. That was useful. But I also wanted to ask about Puerto Rico because that seems like another topical area and it seems like you guys have reasonable exposure, it looks like about $2 billion GO-ish type exposure and then about $1 billion of highway bonds net par. I wanted to ask about that, just the nature of those and kind of your thoughts there in terms of the risk to those exposures?

Dominic Frederico: Well, Puerto Rico is another one of those troubled credits that we continue to monitor aggressively. As you know, there has been a change in local government, the new governor has at least communicated that he has a desire to correct what is probably the biggest issue with Puerto Rico, which is the low amount of funding on the retirement obligations, which we think could put a drag on the system. As you point out, a lot of our exposure is in the general obligation, and we have a lot of further exposure to revenue type bonds that, theoretically, should be self-sufficient based on the revenue streams to which they apply, which obviously has not been the case, because of this further other economic slowdown.

So, there's more exposure, half of it roughly related to G.O. revenue, the other exposures either relate to local tax or other revenue streams. So, it's a complicated process, obviously, as you point out it's significant, we monitor it. We believe that the right measures are being taken, but obviously they need the benefit like most of the world does in a better economic recovery and we continue to take a very, very close look at that and continue to engage ourselves, wherever we can, with what's happening locally. But we're encouraged by, as I said, the new government and what there seems to be the commitment to solve, which is the biggest problem, which is the low funding of the pension liability.

Geoff: Got you. Okay. That's it for me. Thanks.

Dominic Frederico: You're welcome.

Operator: Thank you. And the next question comes from Geoffrey Dunn from Dowling & Partners.

Geoffrey Dunn: Thanks. Good morning.

Dominic Frederico: Good morning, Geoff.

Geoffrey Dunn: Dominic, could you talk a little bit about the reaction of your trading spreads and your clients since the downgrade? I think Rob indicated you've closed all the muni deals that were pending, but can you give a little more color on the environment for your wrap?

Dominic Frederico: Well, the environment is still most impacted by interest rates. And, as we continue to maintain a federal policy of low interest rates, as we said in both my commentary and Rob's, we're going to be hard-pressed to generate revenue volume irrespective of spreads. Now specifically the spreads, as you well know, our credit default swap spreads have come in substantially post the downgrade. We have closed all the deals, principally, that were outstanding at the time. New business volume is slow, once again related to more economic uncertainty, what's going to happen relative to sequestering, especially if that hits the Build America Bonds, what's going to happen with municipal interest; so there is just so much uncertainty hanging over the market that it's hard for us to get a good read. Obviously, we do believe the Moody's downgrade has cost us some level of activity within a market where if our penetration was 3% and this takes it down to 2.2%, you're talking maybe $12 million of future earned premium, which will be spread out over 30 years. So, it's not economically significant to us, but it's something that we continue to monitor.

And the last thing that I would say is the good news is that, it doesn't appear that there's been any impact whatsoever in our efforts or opportunities in the international markets, and we're very hopeful that we're going to actually book some business that we're going to be very proud to announce in the upcoming quarters relative to the international operations. So, by and large its had an impact, not significant in this market. It's hard to have anything significant because of the interest rates. But the good news is, at least the international market continues to provide opportunity. Our credit spreads have actually come in, which is positive relative to the overall organization and obviously we have communicated to you that we do have plans to be able to compensate for some of these impacts, but unless we get some real movement in interest rates, we're going to still be fairly well exposed to a benign new business market in the United States.

Geoffrey Dunn: Okay. And that actually leads to my second question about international. Can you go into a little more detail, what is changing or evolving that 2013 looks more optimistic on the business front? You still have economic pressures over there. So I'm just curious what is changing that makes it a more interesting opportunity?

Dominic Frederico: Well, I'd go a couple of things. One, so like it or not, at least the Moody's rating now has a stable outlook to it. And a lot of people were just saying, okay, how far is the knife going to fall? So at least that has been resolved and in that marketplace, the AA wasn't really a requirement. As you look at what the requirement there is for investors, it's more getting the support and participation of the institutional investors, which we've done, and our European office has done a fantastic job of continuing to go around and continuing to provide data and therefore maintain their support. And typically as we get an opportunity on a deal, we will actually go out and solicit letters from investors that will be more than happy to provide a letter of comfort that says they will be more than happy to invest in the bonds. So, that works for us.

Number two, in that market, our value of our product is a lot more than just the guarantee. Obviously they value our surveillance significantly. Three, the bank funding is starting to dry up there and if you think about where rules around say swaps are going, a lot of the local financing is typically done, in some cases offshore, and there is always a swap put on the currency. Well as you can appreciate, swap has turned out to be a four letter word in today's regulatory environment, and therefore that's going to be harder and harder. It's got more long term implications relative to accounting and capital, so there's a movement away and more interest in creating long-term capital market fundings. And then, last but not least, everyone is trying to stimulate their economy. One of the easiest ways to do it is obviously investing in your own infrastructure, and the majority of the European opportunities are infrastructure projects.

Geoffrey Dunn: Okay, great. Thank you.

Dominic Frederico: You're welcome.

Operator: Thank you. And the next question comes from Bill Clark with KBW.

William Clark: Good morning. Obviously, refundings is hard to predict given where rates are and where they may go. I just wanted to talk a little bit about the termination side. I'm just wondering if you could comment, maybe on the pipeline. Fourth quarter was certainly a pretty big level, just wondering if that's something you think kind of took some opportunities out that you could potentially see going forward, or if you still see a pretty good pipeline for the future.

Dominic Frederico: I'll break that down into two pieces. So, let's deal with the refunding side. So on the refunding side, obviously we've been benefited by a significant refunding activity relative from the low interest rates in the marketplace that really stimulate that type of opportunity and demand. And what we see is a similar level in 2013 that we saw in 2012, because you kind of go back to see what was the issue rate in 2002 and 2003, as you're hitting the 10-year call. So, we're pretty optimistic that 2013 represents a pretty good year.

For your second question on terminations and accelerations, obviously we have a targeted list, easy to grab the low hanging fruit, as you could well appreciate it. Yet we still see reasonable activity, now obviously 2012 was a very unique year for that. But there are similar opportunities in 2013 and it's hard for me to give you an approximate 'we'll equal to the same level as 2012', all I could tell you it's still very significant both from what we're negotiating to terminate as part of a wider, broader settlement with a counterparty, as they're looking to clean up their balance sheet and move some assets around.

They need our acceptance to that. And therefore, we typically try to put in some further negotiations of other things we like. As you know, we like to buyback insured securities where we can at a discount, and that allows us to retire a lot of obligation, and therefore accelerate the recognition of any unearned premium reserve we have for that and there's still a very active market for that in 2013. So, although 2012 was a great year, I expect 2013 to be a very good year as well in that regard.

William Clark: Okay. That's helpful. Thanks.

Dominic Frederico: You're welcome.

William Clark: And then on the share repurchase authorization of $200 million. Just wondering if you can maybe give some commentary on how aggressive you plan to be with that going forward?

Dominic Frederico: Well, as I said… we're waiting for this question, so thank you for asking. We appreciate that as we look at the company, its market position, its market opportunities, and we talked about interest rates leading to a low-level demand and continued amortization of the portfolio. We have significant capital that we need to retire. We've always said we would be a very efficient capital manager. We put in an initial, and I'll highlight initial, share repurchase authorization of $200 million. We'd like to get through that in a reasonable timeframe without really significantly impacting or impairing the stock, but still to be efficient in how we dispose of that authorization and obviously our goal is to continue further authorizations until we believe we've brought the capital down to a reasonable level relative to both the portfolio, ratings and new business opportunities.

William Clark: Okay, great. That was all I had. Thanks.

Dominic Frederico: You're welcome.

Operator: Thank you and the next question comes from Josh Bederman from Pyrrho Capital.

Joshua Bederman: Hi, guys. Just following up on the last question a little bit, can you give some color around some of the - I guess – structural changes or the flexibility that you're envisioning to actually upstream the excess capital into the holding company? Thanks.

Dominic Frederico: Yeah, you appreciated…and you've obviously hit the question right on the head. Biggest issue we have in the ability to buy back shares is how much free capital, free cash we can get to the holding company in Bermuda. And there are obviously a lot of legal and regulatory restrictions in moving money around. So what you can infer from that is, we've obviously developed strategies that deal with: These are the legal or the regulatory side of what's limiting or needs to be acquired to further move cash in addressing each one of those areas with the goal to significantly increase the amount of cash availability and free capital that would reside in the holding company that can be used for the repurchasing of shares. And what we're going to tell you is, as we get approval and therefore free up the capital, we will disclose that and release it to you at that time.

But obviously we don't want to front anybody, especially when it's a regulator, to say, "Well, this is kind of what we're doing" until they actually give us their approval. There are some structural things that we have to do as well that we're working on, that would also continue, to assist in this issue of freeing up capital to move to the holding company. So, all I can tell you is, we've got things in motion and as they come to fruition, we will disclose and we will talk to you on a regular basis about the available cash flow that sits in the holding company, so you can figure out, then, what's available for share repurchase.

Joshua Bederman: Great. Thank you.

Dominic Frederico: You're welcome.

Operator: Thank you. And the next question comes from Rob Maton from Schneider Capital.

Rob Maton: Good morning.

Dominic Frederico: Good morning, Rob

Rob Maton: I guess sticking with the same topic there, separating the regulatory needs to move – move money to the holding company. Could you talk about the amount of excess capital that you feel like you have relative to rating agency models at this point?

Dominic Frederico: We opened this door so now we can't shut it. But okay, so, let's keep it going. Based on our best guess, and remember the rating agencies are not very transparent when it comes to free capital, and specifically, as we sit here today, we've never received a full capital model from Moody's. So, if you want to add another tick mark of disgrace to their rating, put that one on your list, that we still to this day do not have a capital model from these people. Yet, they did do a credit scorecard, which I'm very amazed by, because it does have capital adequacy as part of that scorecard, although they never shared it with us. Very nice of them. So, let's set them aside.

As far as we can determine on S&P, as of year-end, we have about $800 million of excess capital at the AAA level -- and that's our determination, so, make sure you count it that way, and remember we have to maintain AAA capital, the one with the AA because we failed the large obligor test. So, that's the best rating agency number I can give you as of today.

Rob Maton: Okay. And then over time, I would assume the continued runoff of the U.S. RMBS is the biggest – one of the biggest drivers of continued capital generation relative to those models?

Dominic Frederico: You are exactly right. So, let's talk about that for a quick second. So, if you look at the capital models, and although we still disagree with the levels -- but since they never really give us any chance to put forth those objections, because it typically doesn't matter in our rating as I said -- and we actually were arguing with S&P not too long ago about an upgrade. And so, what could we do to get this upgrade? And we said, "What about another large rep and warranty agreement?" and they said "Look, you're already significantly over the AAA, you're already over our highest capital level for capital adequacy that we have. So, that doesn't do it." And we're like okay, so thanks for your help.

Anyway, even if you look at the numbers, the majority, and understand this, the majority of our capital requirement per the rating agencies still relates to the RMBS portfolio. So, that is the 800-pound gorilla sitting on the side of the room. As that improves, runs offs or gets subject to another settlement, it substantially then would reduce the amount of capital, which is the majority of the capital we're holding to support our rating agency ratings, would then get released. So, it's not simply amortization. It's obviously looking at improvements in the market. It's looking at further rep and warranty deals that would have a significant impact and therefore accelerate how we would view our excess capital position as it affects the rating agencies.

Rob Maton: Okay. Thanks.

Dominic Frederico: You're welcome.

Operator: Thank you. And the next question comes from Marie Lunackova of UBS.

Marie Lunackova: Good morning, everybody. My first question is on the MIAC, how much of capital do you plan to allocate to this new subsidiary and what is the timeline for starting writing the business?

Dominic Frederico: Okay. The capital that we have initially targeted is $800 million, coming out of both AGM and AGC. So it will be directly owned by those two companies. So, when you think of it on a legal ownership basis, its benefits go straight up into the operating companies. We hope to begin writing some time towards the middle to latter middle of the year based on just finalizing ratings for the company and approving the transactions that would in effect fund the capital and move the portfolio into that organization, so it's properly leveraged.

Marie Lunackova: Okay. And the ratings, are you still targeting to get at least two ratings?

Dominic Frederico: Yes.

Marie Lunackova: Okay. Then the other question I have about the troubled credits, like Jefferson County, the latest development, could you give us any color on what it actually means, what is happening there, and could it have any impact on your loss reserves for that exposure?

Dominic Frederico: Well, you know. We always thought we have set up reasonable loss reserves, we continue to evaluate that based on current activity, where we see Jefferson County today, we believe we have adequate reserves, obviously provided, and the settlements and discussion we've had continues to leave us with that view that we're adequately reserved.

Obviously, there is a lot of moving parts down there, as you can appreciate. We think we're in a pretty good position relative to what was the deal that was on the table and what that meant for our reserve level, what this last deal theoretically that was being pushed around in the last few weeks and what that means.

So, we're very comfortable with our position, reserve levels. It's an unfortunate situation, but that's why you have bond insurance. And we stand ready to honor… and we've, as you saw in this last quarter, once the trustee failed to make the payment, we went around the trustee and made the payment ourselves, because we think that's the right thing to do. And we continue to honor insured obligations. That had no impact at all on our reserve level. We obviously anticipate that situation as being part of what we think is the ultimate shortfall that we would have to absorb as part of any negotiated settlement.

In terms of our other troubled children, you saw recently in Stockton, where the judge has now scheduled a trial to discuss eligibility. We still think that's positive as long as we continue to get our message out, and we are a little bit upset with the characterization that we did not try to negotiate. But when you tell us we have to take an 80% haircut and that's your deal, I don't consider that negotiation. So, we will see how that weaves its way through the proceedings for the court hearing on bankruptcy and what would develop thereafter.

Obviously, in my little presentation or prepared comments, I'm sick and tired of municipalities blaming outside parties for their problems. We didn't generate these contracts. We didn't authorize these expenditures. We don't control their budget, and for them to say it's our fault is just ridiculous. And obviously, like anybody else, if you want to walk away from your obligations, there are consequences, there are reactions. We have consequences in our actions that we honor, and we think it's the right thing to do. These existing elected officials need to honor their own and take a hard look inside. A mirror is a tough evaluator of your behavior and it's time for these people to start putting some mirrors up in front of them.

And then last, but not least, our friends in Harrisburg, Pennsylvania: There has always been an issue of stranded debt after the sale of assets, it's going to be the issue of who is going to pay for the stranded debt. I think, it's around, based on our best guess, $20 million. So it's not a number that obviously should be a problem for anyone. Remember, we have the county and the city guarantee behind our obligations there. So ultimate liability is still yet to be determined, but we think we're adequately reserved there as well.

Marie Lunackova: Okay, and on Stockton, the fact that Ambac settled, does it set any precedent for other monolines, or it has no impact whatsoever on the negotiation?

Dominic Frederico: We give them a ton of credit, and obviously they got something done, which didn't appear to be possible. If you really look at it, which they didn't release a lot of detail, it just looks like they've provided some capital and maximum amount of annual payments based on availability and extended maturity. That's typically how you work these things out. So, it's nice to see that some level of sensibility did reign, and they got something done. We would obviously look to a similar deal if that was available.

But as we said, no one has offered us any proposal other than for us to take a significant haircut. That's not justified based on where we sit in that whole creditor pool. As we talked about, we're less than 10% of the general-fund budget, yet they wanted us to take 40% of the pain. That doesn't make any sense to us, and if that means we're being unrealistic, uncooperative, okay, so, call us what you like, we're just trying to be reasonable. And I think the Ambac deal is a reasonable…if I understand it, which I don't know all the details… appears like a reasonable compromise that you typically see in these type of situations.

Marie Lunackova: Okay. Thank you very much. That's all.

Dominic Frederico: You're welcome.

Operator: Thank you. And the next question comes from Darren Marcus with MKM partners.

Darren Marcus: Hi, good morning. Just curious, the rep and warranty recoverable jumped this quarter, I guess, by about $70 million or so. And given the Flagstar ruling, I'd have expected it to be up a bunch more. So can you just talk about why it didn't increase your reserve, given I guess increased confidence that you'll have more settlements, and you guys are right in essence. Thanks.

Robert Bailenson: Yes, our rep and warranty asset did jump $70 million, and part of that was due to Flagstar, but on other individual cases or other individual rep and warranty providers, we view them each individually. We look at the circumstances at the time, where we are as part of the litigation. And we probability weight them at that time. So obviously, if this thing went all the way through to appeal and our judgment is affirmed. It would have an effect on other transactions, but at this point the effect that we have is – the effect we have is on Flagstar.

Darren Marcus: Okay. Thanks a lot. I appreciate it.

Operator: And the next question is a follow-up from Geoffrey Dunn from Dowling & Partners.

Geoffrey Dunn: Thanks. Dominic, on the $800 million to MAC, is that hard capital contribution or something that's aided by the intended seeding to that company?

Dominic Frederico: That's hard capital based on your definition, right. So it's equity ownership of the two operating companies in MAC, obviously they will get soft capital through the unearned premium reserve, that they would get passed down through this portfolio session at both AGM and AGC made to them to constitute that company.

Pretty much it's good, if it had to stand on its own two-feet, a company with a significant portfolio, strong earnings, all municipal business, no below investment grade. So it would be a very good strong company, which is the idea because we want it out there to see if we can attract institutional investors more back into the market because of the muni-only strong portfolio good earnings.

And two, obviously there are other buyers out there that would like a muni-only solution, now some cases they are going to prefer that, other cases they rather had the strength and liquidity and the size of Assured Guaranty Municipal (AGM). So, we'll have two flavors. We'll segment the market. So, one doesn't cannibalize the other and we'll hope to generate additional penetration and create a better competitive positioning on a muni only basis with that company.

Geoffrey Dunn: Okay. And going at 800 versus like five, six and other new starts are doing, that goes along with trying to attract –more attract the institutional buyers?

Dominic Frederico: Yeah. And then, when you throw in the rash you're going to have claims paying well over $1 billion, which we think is you're kind of price of poker to get in the game.

Geoffrey Dunn: Okay. And structurally putting at the below AGC and AGM is that just because of the – the capital considerations versus the largest obligor test of those two entities?

Dominic Frederico: No. It's really based on – we want to make sure everybody appreciates that this is not any segmentation. This is not anything relative to the fact that we've got three operating platforms. The one is owned by the other two. So, everyone acts as a group, all funding is kind of comingled. They bear the financial wherewithal on strength of the entire company.

Geoffrey Dunn: Okay. And then last question as it pertains to capital management. I think I know the answer to this, but long-term benefit being in Bermuda versus a nearer-term consideration that might make capital management easier. Is Bermuda still the right domicile and is AG Re still an important platform for the longer term strategy?

Dominic Frederico: No. The fact that you put longer term strategy at the end of that, that's exactly the issue. And, Jeff, it's not a question that doesn't get asked. It's kind of question that does get a lot of analysis. Obviously, you can make a short-term decision that looks like it has huge benefits, but it's the old roach motel - once you go in, can't go out and we've got to be very mindful of that. And you got to say yourself, what is the probability of the market returning to what it used to be, and it doesn't have to be what it used to be in 2005.

If you can get penetration up in say the U.S. municipal market to say, anywhere between 20 and 35, and maybe serviced by two to four insurance companies, as you get the international market flowing again, and everything we see in the international market would indicate that there should be an active market there, because of this issue relative to swaps, this issue with bank financing, this issue with bank capital, Solvency 2, Basel III, all these things would really support significantly capital market executions, and the use a financial guarantee, you should have a robust market.

Now, when does that return, when do they finally require the full implementation of all these proposals relative to capital and regulation? We're all sitting here on the same basis they continue to push back implementation. So, you got to look at that longer-term view and how much that ultimately means. And if we didn't think we had other strategies, Geoff, that we could use, probably that gets even a higher level of screening.

But we do believe, and you'll see as we go through this year with further announcements, that we're fairly comfortable that we've got a methodology or a way of attacking this issue. So that, we get more of the benefit of capital flow into the Bermuda holding company.

Geoffrey Dunn: Okay. Thank you.

Dominic Frederico: You're welcome.

Operator: Thank you. This concludes our question-and-answer session. I would like to turn the conference back over to management for any closing remarks.

Robert S. Tucker: 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.

Operator: Thank you. The conference has now concluded. Thank you for attending today's presentation. You may now disconnect your phone lines.