Assured Guaranty Ltd. (AGO)
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Q4 and Year-End 2015 Earnings Call

Robert Tucker
Managing Director, Corporate Communications and Investor Relations

Thank you operator. And thank you all for joining Assured Guaranty for our 2015 fourth quarter and year-end 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 a 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.

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.

During 2015, Assured Guaranty once again achieved outstanding results and made significant progress on our four key business strategies:

- generating current and future revenue through new business production:
- managing capital efficiently;
- executing alternative strategies, such as, acquisitions and commutations; and
- mitigating losses.

Specifically, in 2015:

- We earned record operating income of $699 million, or $4.69 per share – which are respective increases of 42% and 66% year-over-year
- We increased operating shareholders' equity per share and adjusted book value per share to record levels of $43.11 and $61.18, respectively
- We achieved an operating return on equity of 11.8%, up from 8.1% in the previous year
- We increased the present value of new business production by 7% over our 2014 PVP
- We also completed our acquisition of Radian Asset, which contributed $654 million to our claims-paying resources, $193 million to operating shareholders' equity, and $570 million to adjusted book value at the time of acquisition, as well as approximately $2.13 per share to 2015 operating income
- And we increased our quarterly dividend to twelve cents per share and repurchased 21 million common shares, thereby returning to shareholders a total of $627 million of our excess capital, equal to 15% of our market capitalization at the start of the year. This week our board increased the dividend again to 13

cents and authorized more share repurchases, which Rob will tell you more about.

It is also fair to say that 2015 was the year Assured Guaranty substantially put the effects of the Great Recession behind us. Our exposure to residential mortgage-backed securities, in excess of $35 billion at the end of 2008, has amortized or otherwise diminished by 80% to $7 billion, with much of the remaining exposure subject to loss-sharing agreements with providers of representations and warranties. We have now completed our direct pursuit of rep and warranty claims, which has further validated our loss mitigation abilities. Since January 2008, we have recovered $3.6 billion and, in total, expect to recover $4.2 billion from rep and warranty providers, including future benefits to be received under settlement agreements.

The market is increasingly recognizing the proven robustness of our business model and the compelling value of our guaranty product, which includes not only the certainty of payment provided by our unconditional guaranty of principal and interest when due, but also:

- Disciplined credit selection, underwriting and enterprise risk management

- Long-term surveillance of insured bonds and the ability to protect our capital through remediation and loss mitigation, while insulating insured investors from negotiations and litigation associated with workouts and restructurings

- Enhanced market liquidity, based on $500 million of daily trading volume in bonds we insure

- The stability of our insured bonds' market value compared with the same troubled issuer's uninsured bonds

- And on the issuer side, our proven record of reducing financing costs, improving market access, broadening distribution and saving issuers money.

We believe growing awareness of this value proposition is fueling growth in the demand for bond insurance. In U.S. public finance, annual primary-market par insured was 36% higher in 2015 than in 2014, far outpacing overall municipal new issuance growth of 20%, and reaching a penetration rate of 6.7% of all par sold, the highest annual level since 2009. Fourth quarter industry penetration was even higher at 7.3% of par. In our most active market segment, transactions with underlying ratings in the single-A category, guarantors insured 54% of the new issue transactions and 22% of the par sold.

Insured penetration grew despite even lower interest rates and tighter credit spreads than in the preceding year. The index for thirty-year AAA yields averaged approximately 35 basis points below its 2014 average. During the year, credit spreads tightened to levels not seen since 2008. While these conditions constrained pricing, we maintained our discipline and were even able to improve pricing as the year progressed. Clearly, the growth in demand is driven not by the rate environment but by improved perception of our guaranty's fundamental value. If long-term interest rates increase, growth could accelerate significantly.

Assured Guaranty led the municipal bond insurance market in both par insured and number of transactions during 2015, capturing 60% of all insured new-issue par and 54% of the insured transactions. Our 1,009 primary-market transactions represented $15.1 billion of insured par, a 41% increase -- and more than $5 billion more than the combined total for the rest of the industry.

We were the insurer of choice for bonds issued in amounts of $10 million or less, leading the industry with 662 transactions totaling $3.4 billion in par insured. Also, reflecting improved acceptance of our insurance by institutional investors, we guaranteed 55 transactions sold with insured par of $50 million or more, of which 15 exceeded $100 million. Once again demonstrating the exceptional value of our guaranty, we insured 64 transactions with underlying ratings in the double-A category, whose aggregate par amount totaled $1.8 billion. Counting secondary market activity, our total 2015 U.S. public finance par insured reached $16.1 billion.

An important strength of Assured Guaranty is our diversified strategy, which allows us to avoid dependency on a single market. In 2015, our international infrastructure and global structured finance businesses each contributed more than $26 million to our PVP, together representing 31% of total PVP.

Our international infrastructure business had its best production year since 2008. We have patiently and persistently worked to rebuild the European market for financial guarantees, which was damaged during the global financial crisis, and we are confident that our effort will continue to pay off. We still have opportunities to replace other monoline guarantors on existing transactions and also to generate new premiums through refinancings and restructurings of some of our current exposures. We are also making progress toward guaranteeing a number of new project financings.

In global structured finance in 2015, we closed an additional bilateral transaction with a life insurance company, as well as a number of other transactions. Additionally, we obtained an A+ rating from A.M. Best, the second highest rating in their rating scale, for AGRO, our Bermuda-based specialty reinsurance subsidiary. The A.M. Best rating is particularly relevant for the insurance company clients AGRO serves.

Our accomplishments in 2015 were achieved against the backdrop of magnified headlines concerning Puerto Rico. Let me put this in perspective.

First, as rating agencies have affirmed, even under highly stressed rating agency assumptions, our potential Puerto Rico losses are manageable within our current rating levels. The average annual debt service on all of our Puerto Rico exposures over the next ten years is roughly equivalent to what our investment portfolio generates in income each year, and no rational person expects 100% losses on each of our 11 different exposures, many of which are constitutionally protected or secured.

The next thing to realize is that the Puerto Rico downgrades immediately showed the market an important benefit of our insurance. Puerto Rico-related bonds we insured have consistently traded better than their uninsured equivalents since the downgrades and often by wide margins.

Also, I want to emphasize that negative headlines do not trigger losses. We have repeatedly been able to use our capital, liquidity and market access to work through troubled credits with outcomes far superior to what was initially offered – as witnessed by the outcomes in Detroit, Jefferson County and Stockton.

In fact, the most recent example is the recovery plan contemplated by the Restructuring Support Agreement with the Puerto Rico Electric Power Authority. Puerto Rico's legislative assembly and governor have approved enabling legislation that serves as a foundation for PREPA's recovery plan, and if the remaining conditions are met and the recovery plan is implemented, it results in no losses for Assured Guaranty and commits bond insurers to provide very manageable additional financing support for PREPA to set it on the road to modernization, long-term sustainable rates for consumers and continued access to efficient financing. This recovery plan could serve as a model for consensual restructurings of other Puerto Rico credits.

Having said that, there is still no excuse for the current behavior of Governor Padilla and other Puerto Rico officials. Instead of building on the success of the PREPA agreement as a model solution for other credits, the Governor and his administration have been spending their time in Washington, D.C. lobbying the U.S. Congress to retroactively change established law to permit chapter 9 bankruptcy in Puerto Rico, or even broader restructuring powers that would give the Commonwealth rights unavailable to the states.

That the U.S. Treasury is advocating for this dangerous proposal, to break binding legal commitments, will undermine the belief that America keeps its commitments and the rule of law that enabled our nation to become the leading global model for economic success. For Treasury to claim this would not be a taxpayer bailout is to ignore the harm it would cause to millions of U.S. taxpayers who invested in good faith in Puerto Rico's debt.

Congress is being asked to reward fiscal and operational mismanagement and to condone poor disclosure, poor governance and lax tax enforcement, all of which are well-documented in Puerto Rico's own disclosures, as well as the corrupt cronyism most recently highlighted by the guilty plea of a high-ranking campaign finance official of the governor's own political party. This would be a terrible message to send to municipal borrowers - that it is OK to manage incompetently and corruptly, and OK to abandon legal commitments when it is politically inconvenient to keep them.

The Puerto Rico government is acting with disdain for the rule of law and its own constitution, and is violating the U.S. Constitution. For example, purportedly to make payments on certain general obligation debt due at the beginning of January 2016, the governor issued executive orders for the government to retain, or "claw back," tax and other revenues pledged to secure the payment of certain other bonds. This action caused a payment default, and a claim that Assured Guaranty paid, on Puerto Rico Infrastructure Financing Authority revenue bonds, and if allowed to stand, the revenue clawback would eventually force two of our other insured revenue bond issues to default. Assured Guaranty and other bond insurers have brought suit in Federal court asserting that this attempt to claw back pledged tax revenue is unconstitutional because it impairs the payment priority granted to the revenue bonds – whose proceeds were used to fund essential public services - by subordinating their payment to the payment of the Commonwealth's general expenditures. This impairment of contract and taking of collateral violates multiple provisions of the U.S. Constitution.

The governor seized on the lawsuit to promote his politically motivated crisis narrative. He claimed the suit was the beginning of the legal chaos he had asserted would ensue unless the U.S. Congress promptly met his administration’s demands to allow repudiation of his government’s contractual and constitutional obligations.

Then, on January 29, 2016, Puerto Rico unveiled a restructuring proposal to creditors concocted without any prior consultation with creditors. It appears to be intentionally unworkable because the commonwealth wants Congress instead to provide restructuring authority that Puerto Rico can use as a negotiating club or for an eventual attempt to cram down creditors.

These political maneuvers are delaying the progress of consensual restructuring and structural reform that Puerto Rico desperately needs if it is to regain access to the municipal bond market and rebuild its economy.

If Puerto Rico succeeds in getting some form of chapter 9, it will obviously harm Puerto Rico’s bondholders, some of whom live on the island, who have invested a significant portion of their life savings in supposedly bankruptcy-proof debt and have been partners with Puerto Rico for many decades, helping the island to build its roads, airports, hospitals, schools and other infrastructure. But it will also harm all the citizens of Puerto Rico, whose government will lose access to efficient financing, incur huge legal costs, drive away private investment and cause long-term economic harm far greater than any possible debt relief. And it will harm people in states and municipalities across the country, whose cost of borrowing will likely rise, as investors will be compelled to price in the possibility that state governments will insist on the kind of retroactive special treatment Puerto Rico is demanding, or retroactively change their own laws regarding use of chapter 9.

Puerto Rico has significant structural, operational and economic problems that will not be solved by bankruptcy. To the extent such problems exist, they are largely of Puerto Rico’s own making. Yet, instead of doing everything within their power to legally manage their debt, reform their government, better manage their revenue collection and expenses, and rebuild their economy, Puerto Rico officials have deliberately pushed a self-fulfilling crisis narrative to influence Washington lawmakers. To embrace the Commonwealth’s narrative suggests an irrational belief that harming creditors who are mainly U.S. taxpayers will benefit Puerto Rico, when the reality is that it will prevent the long-term solutions and partnerships that are necessary to bolster the island’s economy to the benefit of its people.

With the government in Puerto Rico doing everything in its power to unjustly impair creditors, how does it expect anyone to provide further credit to the island to help build its economy?

We believe there is a constructive role for the Federal government that does not involve granting bankruptcy authority. And, with regard to Puerto Rico's creditors, only consensual restructurings can assist in the commonwealth's long-term recovery. We are prepared to work diligently with all stakeholders to achieve solutions that promote economic growth, provide Federal control over fiscal management and facilitate efficient financing through the capital markets. These practical and moral priorities are where Puerto Rico should be focused.

I am further dismayed at the recent position of certain Puerto Rican officials who have stated that they will reject any U.S. congressional efforts to create a financial control board. If they are claiming a humanitarian crisis that is the result of years of fiscal mismanagement and poor governance, how can they still claim any right to self-govern their financial operations?

The Puerto Rico government cannot have it both ways. Without significant governmental reform, the situation in Puerto Rico will not improve.

Coming back to how we create value, there are two key strategic activities that can improve future earnings and deploy some of our excess capital. One is acquisitions, like that of Radian. As inactive legacy financial guarantors finalize their own rep and warranty agreements and terminate poorly performing exposures, they may become appropriate acquisition targets. The second is the reassumption of business we previously ceded to third-party reinsurers, which typically involve a commutation premium paid to us that is recognized immediately in earnings. As an example, we reassumed $855 million of net par exposure in 2015.

Turning to our loss mitigation and capital management strategies, I've mentioned our trailblazing, highly successful RMBS recovery efforts. We also manage risk and improve capital efficiency by terminating transactions that are below investment grade or carry rating agency capital charges disproportionately high for their credit quality. During 2015, we terminated $3.9 billion of net par exposure.

Similarly, we purchase bonds we have guaranteed to mitigate losses, reduce capital charges, or improve our investment portfolio returns without taking on additional risk. In 2015, we purchased $945 million of such wrapped bonds.

Through terminations, wrapped bond purchases, refinancings and scheduled amortization of insured transactions, we reduced our net below-investment-grade exposure by $3.1 billion in 2015, even after acquiring an additional $3 billion of below-investment-grade exposure in conjunction with the Radian transaction. Our overall par exposure also declined, while claims-paying resources increased, leading to a 15% reduction in insured leverage.

Our 2015 results have proven again that Assured Guaranty's business model works and our operating strategies are sound. We are looking to the future with great confidence. Our financial position is strong and stable, the value of our financial guaranty product has never been more evident, and we have abundant capital to protect our policyholders, write new business, invest in new opportunities and continue returning excess capital to shareholders.

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.

Our full year operating income of 699 million dollars, or 4 dollars and 69 cents per share, was the highest ever recorded by the Company. It was fueled by the Radian acquisition, high levels of refundings, and a variety of loss mitigation strategies, including a settlement with our last significant provider of reps and warranties.

Our fourth quarter 2015 operating income was 117 million dollars, or 83 cents per share, compared with operating income of 81 million dollars or 50 cents per share in the fourth quarter of 2014. This represents a 44 percent increase in operating income, or a 66 percent increase on a per share basis.

Our fourth quarter results reflect:

- refundings that resulted in premium accelerations
- the contribution to earnings from the Radian portfolio, and
- the continued success of our loss mitigation efforts.

It also includes changes in U.S. public finance loss reserves reflecting recent developments in Puerto Rico.

Financial guaranty and credit derivative revenues were 312 million dollars in the fourth quarter of 2015, compared with 178 million dollars in the fourth quarter of 2014. This increase relates primarily to higher accelerations of 180 million dollars from refundings and terminations.

Investment income in the fourth quarter of 2015 was higher than the fourth quarter of 2014 by 35 million dollars. The increase was mostly a result of nonrecurring income generated by loss mitigation securities that were acquired at discounts and subsequently paid off at par.

Total economic loss development was 133 million dollars in the fourth quarter of 2015. This was driven mainly by changes in the expected losses on various Puerto Rico exposures, and higher estimated delinquencies on HELOC transactions with mortgages that have interest-only reset features.

The impact of changes in the risk-free discount rates was a loss of 6 million dollars across all sectors.

In February of this year, we completed our previous buyback authorization, and earlier this week, our Board authorized an additional 250 million dollars in share repurchases.

Shareholder dividends, share repurchases and recurring debt service and operating expenses of the holding companies are supported by the dividend capacity of our insurance subsidiaries and cash at the holding companies. As of this week we had 41 million dollars in cash and investments at the Bermuda holding company and approximately 98 million dollars at the US holding companies.

After three years of steady execution of the share repurchase programs, we have repurchased 31 percent of our outstanding shares for a total of 1.5 billion dollars. Its accretive impact on our key financial metrics are clear.

Full year 2015 operating income per share was 26.4 percent higher than it would have been without these repurchases.

The corresponding impact on adjusted book value and operating shareholders equity were increases of 21.5 percent and 14.6 percent, respectively.

As a result of share repurchases and the execution of our various strategies, including the Radian acquisition, operating shareholders' equity and adjusted book value per share increased to record highs of 43 dollars and 11 cents per share, and 61 dollars and 18 cents per share, respectively.

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

Question and Answer Session transcript will be provided when available