Assured Guaranty Ltd. (AGO)
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Third Quarter 2022 Earnings Call

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Thank you operator. And thank you all for joining Assured Guaranty for our Third Quarter 2022 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 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 most recent presentations and 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, along with 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.

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 welcome to everyone joining today's call.

We continued to build shareholder value of Assured Guaranty during the third quarter and first nine months of 2022. As of September 30, 2022, Assured Guaranty's adjusted operating shareholders' equity per share of $91.82 and adjusted book value per share of $137.87 were both record highs. Adjusted operating income per share of $2.11 for the third quarter and $3.88 for the first nine months represented increases of 369% and 49%, respectively, compared with last year's periods.

New business production continued to be strong in the third quarter with $95 million of PVP, substantially the same as in the third quarter of last year and our best quarter so far this year. This year's third quarter was our best third quarter in international public finance and second-best in U.S. public finance in more than a decade.

We believe there has been a permanent shift in the market toward a greater appreciation of our value proposition, as

- the pandemic;
- the volatility in the markets and the global economy;
- geopolitical unpredictability; and
- climate-related natural disasters

have reminded investors of the vulnerabilities of their investments.

Municipal bond yields, which had risen dramatically in the first half of this year, continued to climb in the third quarter, with the benchmark yield for 30-year AAA G.O. bonds finishing at 3.9%. Credit spreads remain tighter than has been typical over the past decade, although they have widened somewhat over the course of the year.

While interest rate increases and credit spread widening are promising facts, U.S. municipal bond issuance volume has not kept pace with last year's. There have been fewer refundings this year, whereas in past years, refundings had helped drive high total new issue volumes during the years of ultra-low interest rates. Additionally, year-to-date demand has been curtailed by approximately $92 billion in net outflows from municipal bond funds and ETFs.

Even with the reduced issuance volume, this was the third consecutive year in which insured volume in the primary market exceeded $21 billion during the first nine months. You would have to go back to 2009 to see a higher insured volume. At 7.8% of par issued, the industry penetration rate was the second highest in over a decade for the first three quarters.

For Assured Guaranty year-to-date, strong demand for our secondary market municipal bond insurance offset some of the impact of lower overall issuance. In the secondary market, we wrote more insured par in the first three quarters of 2022 than in any first-nine-month period of the last decade. Our $2.2 billion of secondary insured par totaled more than 11 times that of last year's first three quarters. With fewer opportunities to purchase insured bonds in the primary market, investors have evidently been seeking the security and other benefits of our guaranty through the secondary market, which we believe is a sign of fundamental demand that is likely to be reflected in the primary market as volume returns. Holders of uninsured bonds may also want insurance because it has the potential to stabilize the market value of a position compared to the uninsured position should a credit come under financial stress. Our secondary market policies command comparatively higher premiums and have made an important contribution to our strong PVP this year.

Assured Guaranty remains the market leader for bond insurance, insuring approximately 56% of all primary market insured par sold during the first nine months of 2022.

In total, our insured par sold in the primary and secondary markets was $15.1 billion, the third largest amount we have insured during the first nine months of any year in the last decade. This included $4.8 billion of par from 21 U.S. public finance transactions that each involved at least $100 million of insured par. During the third quarter of 2022, our insured par sold in the primary and secondary markets totaled $3.4 billion, of which $480 million was secondary-market par.

We were pleased to continue adding value on double-A credits, where we believe investors see our guaranty on high-quality credits as a mitigant of various risks. During the third quarter, we insured $683 million of par on 24 primary and secondary transactions with double-A underlying ratings. In aggregate, for the first nine months of 2022, we insured more than $2.3 billion of par on 103 primary and secondary market transactions that either S&P or Moody's, or both, had assigned double-A underlying ratings.

Outside U.S. public finance, our international public finance business had its best third quarter since 2009, producing $37 million of PVP and bringing its year-to-date PVP to $67 million. We guaranteed transactions in the transportation, airport, water and other utility sectors. We have good prospects for a strong finish to the year, including local authority debt and other transactions.

In global structured finance, we are currently processing mandates in such areas as

- subscription finance,
- diversified payment rights,
- whole business securitization and
- portfolio capital management for banks and insurance companies.

Our new business production benefits from our strong financial strength ratings. Last month, Kroll Bond Rating Agency affirmed the AA+ ratings it applies to our U.S., U.K. and

European insurance subsidiaries. In separate reports on AGM and AGC, KBRA highlighted the companies' substantial claims-paying resources, "ability to withstand KBRA's conservative stress scenario losses" and our "skilled management team."

Also last month, the Puerto Rico Highways and Transportation Authority settlement and plan of adjustment was approved by the District Court in Puerto Rico and the plan is expected to be implemented before year-end. Resolving HTA reduces our total remaining insured Puerto Rico net par exposure to about one-half of one percent of our total insured portfolio.

With regard to PREPA, after mediation had reached an impasse, the court has allowed certain litigation to proceed while directing further mediation to resume concurrently. The PREPA bonds have robust creditor protections but, as always, we prefer to resolve the matter consensually if possible, as we have attempted to do for many years.

Overall, our insured portfolio has improved significantly in the last five years, with below investment grade exposure diminishing from 4.8% of insured net par outstanding in September 2017 to 2.5% today, as a result of our loss mitigation efforts. And it's important to remember that only a portion of that BIG exposure is ever likely to produce actual losses.

As many of you know, we acquired our asset management business in October 2019 with the aims of

- one, diversifying our revenue sources by adding a fee-based revenue stream and
- two, gaining an in-house platform to increase our investment returns through alternative investments.

We refocused the firm and have now almost fully wound down the legacy funds that we wished to exit.

In terms of our key objectives, as of September 30th, our asset management business had more than $17.5 billion of assets under management, substantially all of which is fee-earning. In comparison, at the end of 2019, with a comparable amount of AUM, less than half was fee-earning.

We've also made progress on the second objective. Since we began investing in AssuredIM funds, those investments have generated an annualized internal rate of return of over 10%, which is markedly higher than any other insurance segment investment. Keep in mind that these investments are marked to market on the income statement and will therefore show more volatility than our fixed income investments. However, the current marks do not change our expectation of our ultimate returns.

The capital markets have continued to experience volatility.

- In October, the 10-year treasury yield went above 4% for the first time since 2008, and last week, the open market committee added another 75 basis points to the Fed funds rate.
- In the municipal market, the benchmark yield on tax-exempt AAA 30-year G.O.s also exceeded 4% last month, a level last seen in January of 2014.
- In the muni market, yields are now roughly 260 basis points higher than they where they averaged in 2021.

Given the current environment of higher interest rates and what appears to be a weakening economy, we would expect to benefit from further spread widening and a potential return of municipal issuance volume to higher levels. If these occur, demand for municipal bond insurance should increase, and I can tell you that so far in the fourth quarter, the municipal market saw greater insured penetration, while Assured Guaranty increased its market share and found more frequent opportunities to insure transactions with larger par amounts.

We also believe that, in volatile global markets, many participants in infrastructure and structured finance are likely to have good reasons to employ the versatile tools we offer to manage risk.

Our outlook is positive as we continue to focus on our core principles of

- disciplined risk management,
- excellent customer service, and
- prudent capital management that is optimized for the benefit of our policyholders, clients and 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.

I am pleased to report strong adjusted operating income in third quarter 2022 of $133 million, or $2.11 per share. This represents a 369% increase on a per share basis, compared with the third quarter of 2021. As a reminder, in the third quarter of last year we refinanced $600 million of long-term debt, which resulted in a $138 million loss on the extinguishment of higher coupon long-term debt.

Third quarter insurance segment adjusted operating income was $159 million, compared with $214 million in the prior year. These results include strong, and relatively predictable, scheduled earnings generated by our financial guaranty contracts and fixed maturity investment portfolio, offset by some fair value movements in other investments.

In terms of premiums, third quarter 2022 net earned premiums and credit derivative revenues were $92 million, compared with $114 million in the same period of last year. The decrease relates primarily to $13 million of net earned premiums on certain transactions in the third quarter of 2021 that did not recur, and lower accelerations and updates to debt service assumptions in the third quarter of 2022. Refundings were $12 million in the third quarter of 2022, compared with $15 million in the third quarter of 2021, which is consistent with our expectations.

Deferred premium revenue on investment grade exposures has been approximately $3.5 billion for each of the last eight quarters, as our new business production has replenished the normal amortization of the in-force book of business. As Dominic mentioned, financial guaranty new business production was strong in the third quarter of 2022, despite reduced primary market issuance. Higher interest rates and a more active secondary market contributed to a stable level of deferred premium revenue.

Net investment income from the available-for-sale and short-term investment portfolio is also a relatively predictable stream of income, and was consistent on a quarter-over-quarter basis, at $69 million.

As Dominic also mentioned, the economic environment - characterized by market volatility, and rising interest rates - impacted several components of adjusted operating income, adjusted operating shareholders' equity and adjusted book value.

The largest component of the quarter-over-quarter variance for the insurance segment's adjusted operating income is the fair value movement attributable to investments. Specifically, fair value losses related to alternative investments in the third quarter of 2022 of $11 million, compared with gains of $33 million in the third quarter of 2021. This includes investments in AssuredIM funds whose inception-to-date mark is a pretax gain of $107 million representing a 10.3% annualized return. This is in line with our targeted return, demonstrating the value of our investment diversification strategy to enhance overall returns.

With respect to the Puerto Rico Contingent Value Instruments - the Company received these instruments in the first and third quarters of 2022 under the GO/PBA Plan and HTA support agreement, and we now manage these recoveries as trading securities. In third quarter 2022, the related fair value loss was $8 million on a pretax basis, primarily due to rising interest rates.

Economic loss development, which was a net benefit of $72 million in the third quarter of 2022, was also affected by the rising interest rate environment as it included a benefit of $25 million related to higher risk-free rates used to discount expected losses.

The economic benefit was mainly driven by a $95 million benefit in U.S. RMBS, which had several components, including:

- a benefit related to the purchase of a loss mitigation security,

- a benefit on assumed RMBS where we shared proportionally in a ceding company's rep and warranty settlement, and
- additional benefits related to updated second lien default assumptions, higher recoveries on charged-off second lien loans, and improved performance in certain other transactions.

The net effect of economic loss development and the amortization of related deferred premium revenue resulted in a benefit in loss expense of $75 million in the third quarter of 2022.

The Asset Management segment's adjusted operating loss was $3 million in the third quarter of 2022, an improvement over last year's adjusted operating loss of $7 million. The more favorable results were due to

- higher asset management fees compared with third quarter of 2021 as the increase in fee-earning opportunity fund AUM more than offset the decline in AUM associated with the wind-down funds, and
- lower segment operating expenses.

As of September 30, 2022 we have only about $200 million of AUM in our wind-down funds, compared with $800 million of AUM as of September 30, 2021.

AUM in opportunity funds as of September 30, 2022 was $2 billion, up from $1.6 billion as of September 30, 2021, due to fundraising in our healthcare strategy.

Foreign exchange rates also moved significantly in the third quarter, and while the strengthening U.S. dollar relative to the British pound does not have a material effect on adjusted operating income, it can have a material effect on GAAP net income, as well as all of our non-GAAP book value metrics.

The effective tax rate is a function of taxable income across tax jurisdictions and varies from period to period. In the third quarter of 2022, the tax provision includes a $20 million benefit attributable to a return-to-provision adjustment.

With respect to our capital management objectives, we repurchased 1.8 million shares for $97 million in the third quarter of 2022. Subsequent to the quarter close, we repurchased 785,000 shares for $42 million. As of now, the remaining authorization to repurchase shares is $261 million.

Continued share repurchases, along with our positive adjusted operating income, new business production, and favorable loss development have increased operating shareholders' equity and adjusted book value per share to new records of over $91 and $137, respectively. While quarterly operating results vary from period to period, the consistent quarterly increases in these book value metrics reflect how the successful execution of our key strategic initiatives build shareholder value over the long term.

Since the beginning of our repurchase program in 2013, we have returned $4.6 billion to shareholders under this program, resulting in a 72% reduction in total shares outstanding.

From a liquidity standpoint, the holding companies currently have cash and investments of approximately $127 million, of which $75 million resides in AGL. These funds are available for liquidity needs, or for use in the pursuit of our strategic initiatives to either expand our business or repurchase shares to manage our capital.

2022 has been a year of great progress, particularly in terms of our Puerto Rico exposure.

- Aside from PREPA, our remaining exposure to defaulting Puerto Rico credits are covered under the HTA Plan, for which we are awaiting the Effective Date to be announced.
- In third quarter we received $147 million in cash and $672 million in original notional Contingent Value Instruments as part of the pending HTA settlement.
- Our exposure to Puerto Rico salvage assets in the form of recovery bonds and CVIs have also been declining as opportunities arise to sell those securities. During the third quarter, we sold approximately 20% of par or notional value of the amounts received under the settlement agreements, for a total reduction of 48% on a year-to-date basis. In addition, $87 million of the CVIs paid down subsequent to quarter end.

As we look forward to the fourth quarter and beyond, we remain optimistic that:

- the interest rate environment will benefit new insurance business production, and
- asset management and alternative asset strategies will continue to contribute to the Company's progress towards its long-term strategic goals.

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

QUESTION & ANSWER SESSION

Operator
[Operator Instructions]

The first question today comes from the line of Brian Meredith from UBS. Please go ahead. Your line is now open.

Brian Meredith, *UBS*
Hey, thanks. A couple of questions here first. I'm just curious, Dominic, there was a disclosure by MBIA that they're undergoing some strategic evaluation from Barclays. I'm just curious your kind of thoughts on whether that would make a good strategic fit with AGO, any opportunities there?

Dominic Frederico
Well, Brian, thanks for the question. We heard that same comment in the market as well. Obviously, we've been continuing as one of our strategic objectives is always to consolidate the other remaining monolines. And like any other opportunity, we'll look at it if given the opportunity and see if it makes sense and whether we can meet the credit terms of our credit underwriting standards, and look at what else is in the portfolio.

Brian Meredith
Great. Thanks. And then second question, I'm just curious, to look at the dividend capacity out of the insurance ops right now, it's relatively low. Maybe give us kind of the views of maybe a special dividend, particularly, could you get one when HTA ultimately comes through and everything finally gets done?

Dominic Frederico
Well, I'll let Rob answer the specifics. But yeah, we, obviously, look at other all means in terms of meeting our cash flow requirements to the holding company to allow us to operate or execute our strategic objectives, one of them which is capital management.
Obviously, as Puerto Rico continues to wind down, we get down to basically one exposure which is PREPA. And remember, the regulators were giving us a special dividends even with Puerto Rico back in the day and then, obviously, COVID hit and changed things dramatically.

So we think the environment is getting in the right structure for us to go back to the market or go back to the regulators and have the discussion about special dividends. Obviously, if we want to achieve further strategic objectives, that's important for us to be able to accelerate or increase our cash flow to the holding company.

Robert Bailenson
And then, Brian, as you look at Page 12 of the equity investment presentation, you can see the remaining capacity at AGM and AGC, but that's just for this year. So that will be replenished in the next year. So remember, it's either 10% of policy or surplus or your net investment income. So that will be replenished.

In addition to AG Re will have more capacity going into next year as well. So - and obviously, we're always looking to increase that dividend capacity through possible dividends from our U.K. operations. And so we continue to try to maximize our dividend capacity with our operating subsidiaries.

Brian Meredith
Got you. And then Dom, I want to go just quickly back to my first question. Just curious from your perspective, is there the ability for AGO to do a transaction for all of MBIA? Or would you be purely focused on National if something was possible?

Dominic Frederico
Well, that's pretty spoken to, Brian. So at the end of the day, we really - at this point, we've looked at the portfolio from a reinsurance perspective over time. But obviously, we'd have

to do a complete update of our understanding of what's in each of the organizations and see what makes sense. And if there's something that makes sense, then, obviously, we would consider it.

Brian Meredith
Great. Thank you.

Dominic Frederico
No problem.

Operator
Thank you. [Operator Instructions] The next question today comes from the line of Tommy McJoynt from KBW. Please go ahead. Your line is now open.

Tommy McJoynt, *Keefe, Bruyette, & Woods*
Hey. Good morning, guys. Thanks for taking my question...

Dominic Frederico
Good morning, Tommy.

Robert Bailenson
Good morning, Tommy.

Tommy McJoynt
Good morning. Yeah. So I won't ask you to say specifically about your interest in MBIA, but just perhaps from your seat, kind of a unique standpoint, do you think that other multiline insurance companies might have interest in an asset like that? I guess said another way, is it possible that other insurers could aim to enter the bond guaranty market, I guess with the positive outlook of higher rates and wider spreads? Or is the stigma of Puerto Rico really likely to keep some entrants away from this market?

Dominic Frederico
Well, speaking from a third-party perspective, I don't this stigma of Puerto Rico make any difference at all at this point in time. I think it's a credit that's getting its way to resolving. Obviously, based on the creditworthiness of the government and the activities and its actions was making difficult for them going forward to get further bond insurance applied to any of their debt,, but that's for another day. So I don't think Puerto Rico matters at all.

I think it really looks at the regulatory environment. So remember, when you get into this business, you not only have regulators, you have rating agencies, which are two very high hurdles. And if a company is willing to climb those hurdles and they would take a look at it. But for us to try to speculate on whether a P&C company or a title company or a life company wants to get into the financial guaranty business. And we welcome the competition. I think Assured is very well positioned relative to the marketplace, to our standing with our clients and the performance that we've done and the track record that we have amassed, which is not easy to duplicate at this point in time. Plus, we've always said in this business, you need a track record, you need earnings and you need a deferred revenue source to really make a sense for the capital in play.

So if you say that these companies that have left big enough to establish that benchmark or that foothold to allow you to go forward in the business. Like you said, it's not for us to determine, it’s just for us to determine whether it's attractive to us or not. And if we see competition then we see competition.

Tommy McJoynt
Got it. Thanks. I guess on that topic of thinking about regulators and rating agencies and dealing with both, I guess, on the topic of a special dividend and the potential size of it, do rating agencies look at it really differently than regulators might? I know you guys were trying to work on coming up with an updated figure of the - I think it was an S&P report kind of estimating how much excess capital you had in excess of a AAA rating that was, I think, last out in 2019. So just any update on that and really just kind of thinking about how regulators look at it from the perspective versus rating agencies?

Dominic Frederico
Well, I think the regulator rating agencies do have different perspectives, right? Obviously, the rating agencies are more based on a specialized scenario. Regulators have a lot more criteria. They have a different capital model than the rating agencies do and yet as a financial guarantor you are probably responsible for both.

In terms of the excess capital, so we anticipated the question. So the numbers come down over the last 2 years due to our - I'm reading our prepared remarks, so bear with me on this. So the numbers come down over the past 2 years due to our successful capital management program, basically resolutions related to Puerto Rico, and we're very comfortable that we have substantial excess capital.

The last time we gave you this information was for the year-end 2019, where we had approximately $2.6 billion of S&P AAA excess capital, very important to note, it's on a AAA basis. However, between then and the year-end 2021, we repurchased $1 billion of our common shares, $1 billion worth of common shares, paid approximately $140 million in dividends, paid over $700 million of PR debt service excluding settlements, invested over $500 million through AGAS and other high cap charge investments. And despite using this $2.14 billion of capital, our S&P excess AAA capital is still $1.8 billion as of year-end 2021. So hopefully, that gives you your answer.

Tommy McJoynt
Yes, that's what we're looking for. Thanks for having that prepared for us.

Dominic Frederico
No problem.

Tommy McJoynt
And then just last question and I think it looked like in the slides that the industry's U.S. public bond insurance penetration actually looks like it dipped a little bit in the third quarter, just if I base the penetration in the first half and compare it to what it was for the first 9 months. So it looks like it declined a bit sequentially, which is a bit surprising given the backdrop. Any sense of what drove that?

Dominic Frederico
Yeah. I mean remember, that's very relative to who's in the marketplace at any given period of time. And of course, the market volume is way, way down. So the issuers that are in the market are probably the more liquid issuers that are probably going to use bond insurance least. I think as you see the statistics for the complete year, you'll get a very different answer relative to the penetration rate. It's still kind of flat with the prior year, which is still way above years 4 to 5 years ago.

So we're making progress in penetration. We think with the rising interest rates, the widening of credit spreads, the economic uncertainty, we think demand is now positioned to really start to increase substantially. And we'll hopefully see that in the fourth quarter when we give you our fourth quarter and year-end statistics.

Tommy McJoynt
Great. Thanks for answering those questions.

Dominic Frederico
No problem.

Operator
Thank you. The next question today comes from the line of Jackie Cavanaugh from Putnam. Please go ahead. Your line is now open.

Jackie Cavanaugh, *Putnam Investments*
Hi, guys. Can you hear me, okay?

Dominic Frederico
Yeah, we can, Jackie. How are you?

Jackie Cavanaugh
Hi. Thank you so much for taking my question. I guess just a follow-up to the prior question, and thanks for going through the different capital sources. But does the regulator or the rating agencies care at all about the AOCI marks? And does that impact their analysis or the way they might think about a special or the capital excess just given the magnitude of the marks? Thank you.

Robert Bailenson
The mark doesn't affect our statutory capital and it doesn't have an effect on rating agency capital. Obviously, it will be a discussion that we talk about with the rating agencies, but it doesn't go - it doesn't affect surplus or rating agency capital.

Jackie Cavanaugh
Okay. Great. So they're sort of agnostic to it, just like the Street kind of looks through it?

Dominic Frederico
They don't look through it, it is just not part of their model. So one looks at claims paying resources, one looks at statutory capital, which doesn't count statutory capital...

Robert Bailenson
S&P starts with our surplus and our stat capital and then rating agencies just obviously - I mean the regulators will look at surplus. But as Dominic said earlier, there are other regulatory tests that we need to talk about with them and deal with them when it comes to getting special dividends.

Jackie Cavanaugh
Got it. Okay. I know you've told me that before, but I just wanted to confirm, given the magnitude of the mark. So thank you very much.

Robert Bailenson
You are welcome.

Dominic Frederico
Well, the marks are the marks and at the end of day, it doesn't change our economic outlook and returns on those assets. Obviously, some adjustments will affect certain parts of the balance sheet. But over time, we would think - we believe that things will return to basically normal, and the mark should start to reverse.

Jackie Cavanaugh
Great. Thanks, guys.

Dominic Frederico
You are welcome.

Operator
Thank you. The next question today comes from the line of Geoffrey Dunn from Dowling & Partners. Please go ahead. Your line is now open.

Geoffrey Dunn, *Dowling & Partners*
Thanks. Good morning. Dominic, I don't remember the years where you discussed this, but in the aftermath of the Great Recession, you speculated at where the municipal bond market could ultimately recover to under kind of the new model of being a AA, et cetera. I want to say we're like 25% penetration, but part of that recovery was based on rates

going up and spreads going out. So obviously, that's happening now and who knows if it will be sustained.

But in your vision of where the muni bond market for FG goes or even the global market for financial guaranty goes, what else do you think needs to happen other than what we've been seeing on rates and spreads to reach what you think could be a fully recovered sustainable financial guaranty business model going forward?

Dominic Frederico
One word, Geoff, one word, stability. So rates are getting to an area where we're very comfortable, it's going to really further increase demand for municipal insurance. But it's got to stay over time, right? We can't get the rates go up like a balloon and down like a popped balloon.

If these rates will hold and if the Fed and the treasury stay constant, then I think it creates that absolutely conducive market for growth for us. And we started to do some analysis, right? So a couple of cute little tidbits of information, Robert took them away from me so now I don't see it.

So the one I'll tell you is the 1% rise in interest rates is worth 10% on PVP. So think about a 1% rise in interest rates, 10% on PVP. So that's just keeping everything else constant.

Thank you, Robert.

To give you an idea, if we look at debt service on the same amount of par. Remember, we get paid based on rate times debt service. So 2021 debt service resulted in a 135% of par. 2022's debt service resulted in 193% of par because of the change in the interest rate. We get paid based on debt service. So think about that impact will have on future premium, not only will we calculate as PVP, but we get to earn over the future periods. And in a rising interest rate environment, you're not happy refunding. So we're not going to get this acceleration that robs future periods of earnings.

Now the earnings will be stable over time, will grow according to the PVP growth year-over-year, and add to that earning stream year-over-year over year. So we are very optimistic as we look at the market today and the only we hope for is stability, that its stable at this rate, that it stays that way for a period of time, a few years at least before there is panic in the streets and they start lowering rates again.

Robert Bailenson
And Geoff – I was just saying, Geoff, as you saw, we - the secondary was very strong over the last couple of quarters and is generally a leading indicator to the primary as well. And so if you get stability and less volatility, the issuance will pick up in the primary market.

Dominic Frederico
Yeah. So a little fact that we look at is secondary market activity, and that's typically a forerunner of primary market activity. And to give you an idea of secondary market activity

in the current year 9 months to date, we've written $60 million of PVP in the secondary market compared to $4 million last year - $60 million versus $4 million. And that's typically a precursor, an indicator where the primary market is going.

Geoffrey Dunn
Okay. And then it's been - it might be probably a decade and a half since financial guaranty companies really talked about the different hurdle rates across - return hurdle rates across muni structured and international. But as you weigh potential M&A, I'm just curious if you could share some sort of range on hurdle rates on new business so we can get a gauge of what type of return on a M&A opportunity might be compelling enough for you to look at versus retaining the capital for buyback and growth?

Dominic Frederico
When you look at it on that basis, Geoff, you have to say the return on a M&A basis got to be north of 15 because we think the capital return on the buyback of stock is in the 11% to 13% range. We're writing new business anywhere between, say, 8% to 11% depending on the transaction. And depending on the service of business.

So international would have a higher than that, great. But obviously, international is not the major part of our business, U.S. public finance. When we look at rate returns on a transaction-by-transaction basis plus for the quarter. But remember, that's also on regulated capital, not the capital that has to be absorbed in the company.

So the excess capital is not in that calculation. So the real returns are less than that, but I can't fault the profit center for writing business and regulatory capital enhanced returns, and they're not responsible for the excess capital in the company. So as we look at that hurdle rate for the M&A, it's got to be north of 15%.

Geoffrey Dunn
Okay...

Dominic Frederico
It's got to make sense credit wise and everything else relative to the organization. I'm sorry, Geoff.

Geoffrey Dunn
Right. And then just financially, is there any kind of return leverage preference between reinsurance versus an outright acquisition?

Dominic Frederico
In the old days the outright acquisition had a lot of benefits, right? It got us the portfolio rerated more than the investor base, which we really don't need anymore, but that was important to us back in the day like the FSA transaction. And then we got a huge discount on the capital and the capital was substantial to get a discount on.

Now the capital bases they are a lot smaller, so the discount, if there are any, is not going to be the same value to us that it used to be. So for us, we're agnostic from reinsurance through acquisitions, both of them will provide the portfolio we want at the risk rating we want at the premium level that we want.

Geoffrey Dunn
Okay. And my last question, do you recall the discount, the statutory capital that you paid for FSA?

Dominic Frederico
Wow, the statutory capital - I can tell you the book value, right, we paid 37% to 38% - represent a 62. And then as we went through the transaction, we got into the 50s and then the later transaction was probably in the 20s to 30s. So as the portfolios got smaller, they got less volatile, there was less capital to be discounted. So they were bigger back in 2009. I think the next one was like 2011 or '12, which might have been 50% and then the ones in 2013 and '15, if they were the years if I remember correctly were probably in the 20% to 25% range.

Robert Bailenson
Yes. So that was – so discount was like 63% for FSA just to make sure we're clear, we paid like 37% of book value...

Geoffrey Dunn
Got it. Okay, thanks, guys.

Dominic Frederico
You are welcome.

Operator
Thank you. The next question today comes from the line of Giuliano Bologna from Compass Point. Please go ahead. Your line is now open.

Giuliano Bologna, *Compass Point*
Another great quarter on the performance. But what I would be curious is actually following up a little bit on the kind of pricing and return question. When I think about the spread environment, obviously, spreads have widened, so you're going to generate savings there, your end customers have increased. I'm curious where returns have gone from a return on capital perspective on where business was before rates prior versus kind of where it is now and where that could go? Is that - I'm curious how much improvement potential there is from a return on capital perspective for new business in this kind of better operating environment?

Dominic Frederico
Yeah. I think the improvement is reasonably large. So if you think about it, Giuliano, so public finance is the largest book of the business, right? And obviously, the most

competitive end of the business, more susceptible to competition in the marketplace, more for uninsured versus insured.

And if you look at it, we do it on a transaction-by-transaction basis, I'm trying to remember from the top of my head. So in most quarters, we're trying to achieve a 10% minimum return. And I think we get that most of the time, but there probably were some quarters, say, 1 year ago or 2 years ago, they might have dipped below 10 to like 8 or 9. And then with some transactions that were competitive, you might even go lower and the other transactions where we really added value, you're able to go higher. I'm giving the average.

As we look at the book today, I'd say - and remember, we're just at the beginning of seeing this enhanced flow of business and rates and premium and spreads. This quarter, I think every business line was over 10%. International is always over 10% and really be odd that it wouldn't be. But even in the domestic U.S. public finance, if I remember the number correctly, it was north of 10. And like I said, that's at the very beginning stages of what we're seeing is a return of reasonable rates and spreads to the marketplace. We think spreads have a lot more widening than that to experience as the economy rolls forward to potentially a recession.

Robert Bailenson
And if you just think of the basic math, Giuliano, as Dominic said, you're going to get paid on debt service for public financing for all of our clients' business, the higher the interest rate and wider the spreads you are getting paid more dollars, but the denominator of that capital charge it stays the same. So by definition, your returns must go up.

Dominic Frederico
I was referring to someone else in the market, if you look at their published financial statements.

Giuliano Bologna
So I guess kind of going back to another question on the kind of consolidation trends in the industry or the desire to consolidate the rest of the industry. I'd be curious, obviously, reinsurance can achieve effectively the same thing. But as the remaining entities that are out there are running off. The opportunity to do large reinsurance field, I'd say gets smaller and smaller.

I'm curious if there was any preference for acquiring the legal entities, you expect acquired capital at a discount of capital and also you get the benefit of higher investment income to boost for dividend capacity...

Dominic Frederico
Yes. No, you hit it right on the head, right? So reinsurance gets you a very highly rated, well-premiumed risk exposure that fits into your risk model and is accepted by your credit underwriting standards. That's reinsurance. What's missing when you get to the acquisition of the entire company, two pieces, one, breadth of customer, we've already

got that. So we don't need that anymore. But back in 2009, that was important to us, and acceptance of the paper in the marketplace.

And then the third thing, as you just pointed out, the discount on capital. But these capital bases have shrunk substantially because of, obviously, refundings, runoff, et cetera. So the value of the discount even if you say I could get a 30% discount, it’s on a very small capital base. So for us, the reinsurance gets us to pick the risk that we want, meets our underwriting standards. It gets a premium level that gives us that level of return that we targeted. So one is better than the other to a certain extent unless you get a really good value on the discounted capital.

Giuliano Bologna
That's very helpful. Thank you for taking my questions. I'll jump back in the queue.

Dominic Frederico
Good to hear from you, Giuliano.

Robert Bailenson
Yeah. Thank you, Giuliano.

Operator
Thank you. This concludes the question-and-answer session. I would now like to return the conference back over to our host, Robert Tucker for closing remarks.

Robert Tucker
Thank you, operator, and 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
This concludes today's conference call. Thank you all for attending. You may now disconnect your lines. Have a great day.