Assured Guaranty Ltd.

Assured Guaranty Ltd. Presentation delivered at the Keefe, Bruyette & Woods 2013 Insurance Conference on 09/25/2013

Interviewer

Alright, I think we'll go ahead and get started with the next presentation. We're pleased to welcome Assured Guaranty to the 2013 KBW Insurance Conference. Assured Guaranty is a very strong financial guarantee franchise that successfully navigated the financial crisis. They've certainly had success over the last several years on the rep and warranty front and they remain well-positioned to capitalize on any industry recovery here in the future. Here to tell us more about the story are several members of the senior management team; we have President and Chief Executive Officer Dominic Frederico, Chief Financial Officer Robert Bailenson, Chief Risk Officer Howard Albert, and kicking it off will be the Head of Investor Relations, Robert Tucker.

Robert Tucker

Good morning. I'd like to thank KBW for inviting us to speak today, and I'd like to thank you for joining us for the Assured Guaranty presentation. I also want to remind you that all comments made today are covered under the Safe Harbor Provisions of the US FCC. Please note that if you are listening to a replay of this presentation, or if you're reading the transcript of the presentation, our statements made today may have been updated since this presentation. With that, I'd like to turn it over to Dominic Frederico, the President and CEO of Assured Guaranty. After his prepared remarks we will open up the call to any questions you might have.

Dominic Frederico

The call, very good. Okay, good morning. And once again thanks for coming and thanks for the interest. As I thought about this presentation, I always try to wonder, what are the questions that you most want answered. And, as I thought about it, I said, this is a story

that we need to continue to tell and to continue to prove. But it really involves about three things.

One, it really reflects a strategic vision; how we viewed the company from the onset of the IPO, how we obviously set up the discipline, and how we underwrite and how we manage the portfolio. Two, beyond strategic vision is execution, right? Are you able to then execute the strategies and stay to the principles and deliver the kind of results. And then three is, are we positioned for the future. What is the value proposition going forward, both from a market and a shareholder point of view?

So, the first slide I think, goes back to the view of strategic vision and execution. And I put this in here to kind of show you that, where we were pre-crisis and where are we today? A lot has been said about the strength of financial guarantors, the leverage ratios that they have, their ability to survive tough economic conditions. But I think if you pay close attention to the numbers, so what I did was, I chose a January of 2008, kind of pre-crisis. We had say seven triple AAA companies competing in a market place and of course obviously today. And there's some interesting numbers there that you're going to notice. For instance, the significant deleveraging of the company, from over $600 billion of par outstanding today to $487 billion, and I say strategic deleveraging.

And you'll see that represented in the next two numbers, which shows, what is the public finance component of that number versus what is the structure financed and international. And as you can see since January of 2008, we have amortized, paid off, terminated, $120 billion of structured finance.

So if you look at the leverage of the company back in those days and the composition of its leverage in terms of the portfolio, you'd say, wow you were 54 percent public finance, today you're 76. You had the $185 billion of structured exposure, now down to 65. So, we've built a stronger, more stable in terms of performance, company - yet we did it to the worst economic cycle of anyone in this room's history.

Let's look at some other numbers. Total investments of 24 percent over the same period, geez, in an area of low business production, high claim payments, you actually grew the liquidity in the company – and you didn't grow it -- you grew significantly, 24 percent.

The number that's not on the schedule, and I'll give it to you, the stat capital of the firm in January of 2008 was 4.8 billion. Today it's 5.9 billion. So, approximately a 20 percent increase over the same period. And you say, well, okay you went from four-eight capital to five-nine, and at the same time your portfolio came from 626 down to 487. So, significant deleveraging, building up stat capital, and then of course -- the punch line to all of this – and oh, by the way folks, during this period we paid approximately $5.5 billion of RMBS losses. So, when someone says to us, geez we're concerned about your stability, we're concerned about your survivability. Can you handle crisis? I'm going to say, excuse me? I think the numbers clearly indicate the strength and continued viability and vitality of the company going forward.

Second interesting component I think for all of you in the room and everyone listening, is the value proposition. So, we're a company of strategy, vision and execution, and we're also a company of value. And this is the most reflective slide we're going to give you of value, right. As of 6/30, our adjusted book value is $49.06 a share. And there are the components of the value. It's true what I'll call fundamental value in the assets and the liabilities of the company, that we eliminate the mark-to-market, and that has really nothing to do with us, it's one of the silly accounting conventions that we're responsible to adhere to for GAAP, but it has no economic consequence to us, we never pay off of a mark, we don't have that kind of exposure, we don't trade this, it's not a quoted book. We have basically, manuscript exposures, not indexes, filtrated out in the open market place.

And of course the last component is our future revenues and you say, geez, you guys account future revenues but hang on a second folks this is future revenues, but we already have cash in hand. This already sits on the balance sheet, this is something that we cannot lose, it's true value that will just be earned over time.

When you compare that, showing the different schematic against stock price, say okay, what am I missing? So, here's a company that survived the crisis, didn't survive the crisis,

matter a fact, they got substantially stronger than the financial crisis, and yet here they are still trading substantially below book, and substantially, incredibly substantially, below adjusted book. Which we do believe is a true valuation of the company, because it does reflect all losses known as of today.

It's constantly been growing as you go back over the history of the company through its IPO. 344 percent increase, 80 percent compound annual growth rate, and we'll be there too shabby of numbers. Now, as we look forward you say okay, how do we continue to further create shareholder value? We're in a pretty horrific market relative to interest rates and the impact they have on production levels. We're in a still uncertain environment relative to less the economy, but, still to rating agency and rating agency uncertainty on how they deal with certain issues. So, you've two real negative pressures against the company from the standpoint of its ability to create new business.

So we say, okay, if you're not going to have to huge new business opportunities, how else we can create value for our shareholders?. How else can we deliver economic results and economic performance? So, first thing is, obviously we've been a good returner of capital, both in the standpoint of dividends. So, post-crisis we substantially increased the dividend as you would hope we would. Once we determined that we had adequate capital for rating agency purposes, and this is part of our efficient capital management strategy. And remember job one in all of this is to maintain ratings that allow us to still face the market and to be able to trade in the market place. So, with that as a consideration, we then affect as best a policy as we can to deliver value to the shareholders, and first is dividend and second is share repurchasing. And then, the share repurchase number to date, we have repurchased as of the second quarter, $244 million of, stock roughly representing about six percent of the outstanding shares at the time. Obviously this will continue to be a significant part of our strategic direction going forward, because it goes back to those value slides and say, if you trade at that kind of a discount, you know, you would be hard pressed to come up with a transaction that this company can execute that would provide greater value than the buyback of stock.

Second thing, once again, in terms of the ability to write business in this market place, well we have another production source. So, we go to that as an additional source of putting in

more unearned premium reserve, more par outstanding on the books and that is the recapturing of reinsurance. So, if you remember the first slide where I showed you $140 billion decrease in outstanding par that's net of the fact that we recovered or recaptured approximately $38 billion of par. So, really, the true remodeling, reclassification adjustment or readjustment of the portfolio when encompass $178 billion, which is reflected in the structure finance decreased between'08 and today and in the international decrease between '08 and today. So, we not only were able to pay all losses, continue to build up capital, continue to build up liquidity but at the same time we repositioned the portfolio to bring in that higher component to public finance business less reliant on structured finance. And why is that? Because the structured still has a concern in the market because there is some acceleration in those exposures, where in the public finance you don't have acceleration. So, when you look at the -- what is the threat to the franchise and the company, you've started to really minimize that, you really started to negate it significantly.

In the new business side as I said, as long as interest rate stay where they are our ability to do significant amounts of new business is really impaired. So, what have we done? Have we sat idly? No. We formed the new company called Municipal Insurance Corporation. Why? Because we believe that there is a market place out there that wants to deal with or face a municipal only insurer. There's your municipal only insurer. And number two, we think there is another segment of the market that says, I want to write a simple story, clean portfolio, something I can look and analyze granularly risk by risk and not have to try to figure out what it means, there it is.

We believe it also sets us up very well well from the standpoint of issuers that want to use that platform, buyers that want to buy that investment and therefore creates another competitive tool for us to use as hopefully the market returns as some normalization as interest rates rise, spreads widen, as well as to be able to face any competitor in the market place on an equal basis. The only difference there is that is significantly capitalized, 800 million of capital, about a billion-five of claims paying resources and it makes money on day one because of the portfolio that we ceded it, so, significant strong, well-capitalized, liquid, large portfolio organization.

Second thing back to the -- or third thing back to the alternative strategy would be on capital management, new business, reinsurance recapturing, R&W activity and bond repurchasing. And that I don't need to tell you that Assured's been the most successful company in the rep and warranty activity. We did the first deal, struck in this area, our Bank of America deal. We won the first case ever tried, our Flagstar case. Today, as the slide shows we've recovered roughly $3.5 billion or have commitments, or basically collateralized reinsurance, to recover $3.5 billion of our previously or to be paid RMBS losses.

And yet, we're not done. We show you the current litigation that's still out there, but beyond the litigation there's probably three other counterparties that we're in active negotiation to try to resolve some differences. This has a significant impact, believe it or not still, on what is the value proposition and the ability to further execute strategies within the organization. Your question is, well, how? Not only do we recapture losses, and therefore we in effect write back capital or write up earnings, and Assured has always been a very conservative estimator of the benefit of the value of these recoveries, although we've been the most successful at it in this industry. So, you always have an economic gain. More importantly though for the purposes of going back to the capital management, still the majority of our capital allocation that we see from the rating agencies is related to the RMBS portfolio. As we can break the back of these three litigations and there's three other significant counterparties in negotiation. The amount of capital benefit that that drives to the company really makes the economic consequences, not insignificant, but the real value is going to be in the capital. If you think about capital and how we need to manage it relative to maintaining ratings, and if 50 percent if it's still tied up in RMBS, 50 percent, huge number. If we could break the back of that over the next year to two years, think of the amount of excess capital we have to give us further flexibility on how we address the market and how we create value.

To the right of the slide we've given you a little information on the bond purchasing program. Obviously as we looked at this location in the market relative to the price of our insured securities, we aggressively move in and buy those securities. In the old days we did it mitigate loss, we then expanded it to improve capital position. Today, we're actually using it to enhance yield. We're buying short-term maturities that are still trading at a

discount to enhance the return on our portfolio. And in most cases we buy, say a security that will pay out over eighteen months, when you get an eight or nine percent yield, and when you think about new money being put to work at about two percent as you see, that's a significant enhancement to return for the overall portfolio.

So, we use it in a lot of ways. We're still negotiating with some counterparties that are trying to deal with some of their other problems, where you get the opportunity to buy back some of the other troubled securites still at good prices, even though spreads have come in and the pricing as gone up. And we just executed one recently.

Last among the alternative strategies is this whole area called Terminations. So, we've responded to the criticisms in the market of too much leverage against capital in the portfolio, so we went out and targeted exposures where large principle balance outstanding or par balance outstanding, small economic, high cap charge, go to the counterparty and see if we can negotiate a deal.

In a lot of cases, believe it or not, because the counterparties are typically banks, mostly European, they were dealing with their own capital issues. So they were coming to us and say, we need to move the security from this company to that, or we'd like to sell or we'd like to place it as collateral. In our agreements, they're prohibited to doing that without our approval. So, when they came to us for that kind of a change or amendment we say, well look why don't we just tear up the deal? And I think our average has been -- we have retained about 90 plus percent of the economics in all these deals.

So, think of it, you were paid for a 10 or 20 year exposure, you're able to tear it up this year and keep the majority of the economics. So, you got to accelerate those earnings which help support our bottom line and then period of very low new business production. So, another way to enhance value, lower leverage, lower cap charges, so this was an all good all good. Now, you'll say, well hang on a second, you're kind of stealing from the future in accelerating that premium recognition today. You're right. So, unless we see the market start to return, interest rates widen out, that loss of future earnings will ultimately come back and give us issues relative to earnings a few years out because we now curtailed the portfolio. We made it shorter by taking down some of these long-term liabilities.

Last but not the least on the strategy, we said, okay, we've been constituting our capital principally in equity, and is that the most efficient capital composition of the company as we look forward and see what is the most efficient business model for our organization to have. We said, you know what, the capital base should be a combination of all things including equity debt and, to the extent you can get it, placed with highly rated insurance companies, reinsurance.

So, in 2012 we went out and executed an excess of loss reinsurance that sits over the municipal portfolio and the whole thing was engineered to get us rating agency capital. Really be non-economic, in other words we don't ever expect a loss at that level but it got us capital credit -- right, at the lowest cost we can execute. And we'd compared at that time that to debt, and this was the lower cost. This now is coming up towards two yea, where we have the option to terminate and we're going to terminate and rewrite and our goal here is to put this in place. We've got a lot more interest so we'll probably have a higher amount of coverage but at a lower cost. So, if you think about the capital base, how much does equity cost you in terms of cost in capital? How much does debt cost you in terms of the cost in capital? How much is reinsurance? You get a blended number, where we think we have a very efficient cost of capital, therefore we continue to put a high level return on the capital base of the company. So, this was an excellent -- once again, strategic objective executed, deliver the result that we had hoped to achieve.

In terms of the portfolio, coming out of the crisis obviously everyone had to put a lot of securities under below investment grade and understand that these are our ratings, not the ratings agencies ratings, but our ratings are typically more conservative, believe it or not than theirs. But the nice thing this slide shows you is you could see the continued decline in the below investment grade. Are we finished? Absolutely not, this number has to be roughly, say two percent of the outstanding portfolio would be an average number. So, if you have round numbers, 500 billion a portfolio, and you'd like it to be 10 billion not 20. So, we still have a lot of work here.

Interesting thing, we have three deals currently in the market that if we successfully resolve them which we hope to that will take a billion dollars out of this number just in the

fourth quarter alone, just by these deals coming off being settled. Obviously you can figure out who they are, Harrisburg is one. Jefferson County is another and the third we haven't disclosed. So, they would have huge impacts as well as the normal amortization. So, you could see as good as $2 billion number come up with this schedule in the fourth quarter if things work out and wow we'd be below $20 billion. No reason to take out party hats and noise makers but yet it's a significant improvement and continues to show the betterment of the portfolio.

Look to the future, it's kind of, continue what you've been doing. Continue to execute on the alternative strategies which really is the R&Ws, the bond purchases, the terminations, the recapturing of reinsurance. Obviously try to raise much new business as we can but under on our standards, and we have changed standards as you can appreciate, as the market has changed a bit in terms of exposures that we're willing to write. Continue the capital management which is critically important as we see tremendous value in buying back of our shares. And obviously the last thing that we've talked about on the earning call if you listen to that is capital flexibility. We are hoping to announce in this earnings call further advancement or accomplishment.

Once again, I will get back to what I've said at the start. We're a company of strategic vision and execution and that's why we're here and that's what we try to do and I think we've demonstrated that pretty well over the last number of years. So, with that, I will open it up the questions. Hopefully I didn't take too long, and I'm more than happy to respond to anything. And at the table, as you know we have very experienced individuals from the company that can respond specifically Howard in the Chief Risk side and Rob in the CFO. Yes please?

Questioner

Hi. I'm totally unfamiliar with your company but, what is it that investors are just not getting then? Because your stock price has been on this downward trend. And so, what is the risk that investors are seeing that you think is not -- is overstated?

Dominic Frederico

Well first, we move in general direction with the general financial market. So, anytime there is a quantitative easing, no quantitative easing, bond support, no bond support, we're going to go up and down that flagpole as well. Number two, because – the municipal market today I believe has created more uncertainty over the security behind certain of their, bond issuance. The question of, well, can these guys take further losses? I think we've demonstrated that we have the ability to absorb losses and that's kind of how we build this company from a risk management. You know, you've got Stockton California, you've got Jefferson County, you now have Puerto Rico. So, every time you turn around you have Detroit. Let's not forget our favorite motor city. Right? Sot there are big numbers out there, but I don't think people get the relationship of a big number relative to a true economic loss on the municipal side. But it's a scary enough headline to make people kind of step back.

But I think, most importantly most people that invest in the market and you guys are all out there so you correct me where I'm wrong, look at a growth story. And if you really look at Assured Guaranty, you'd say this is a value story, it's not a growth story. Right? With zero interest rates, we're not going to write a significant amount new business. And yeah, we're pretty creative and we're able to be able to continue to create economic value, but people are saying, I can't rely on that in the long-term. You're exactly right, neither can we. We have to see some revision or return to interest rates at some normalized level, say in a couple of years to at least start to build back the unearned premium reserve, go back to schedule on page five. The UPR is down about 2 billion I think since '08. Well, I agree with that criticism but then I don't. Because this doesn't become a part of how much new business I write. It really becomes a part of how much capital do I need to stay into the business that I'm in. And if we right size the capital relative to the business opportunity, whose ever our shareholders is going to be really, really, really happy.

Questioner

Dominic, just maybe we can touch back on Puerto Rico for a second, so that's certainly been in the news a lot lately. They've had a new government there, seems to be taking some of the proper steps to try and turn things around there, at least on the revenue side.

Can you just talk me a little bit more about in detail about your exposure there and what you think might happen there?

Dominic Frederico

Well, we dress them up and then see if we can take them out.

Howard Albert

All right, well you know we have $5.7 billion to a number of credits there, and we've been getting a lot of questions. And I've been trying to put it in the context of history of municipalities, or even sovereigns, who have faced political and economic crisis. And I guess the first thing to think about is in every disaster that we've seen of a municipality or even a sovereign it's always a political disaster first. It's always a problem of will. And as you pointed out the one thing, at least, we're seeing in Puerto Rico is very strong political will toward resolving their problems.

And if you look at Greece, if you look at Portugal, if you look at Detroit, if you look at Stockton, we've seen huge failures of political will across the board for all of those. On the other hand, if you look at New York which went through a very serious economic crisis, if you look at Philadelphia that went through an economic crisis, political will in both those cases really saved them. In the case of the Governor of Puerto Rico, what have we seen? We've seen someone who basically went -- met with the rating agencies, saw the writing on the wall and said, we have to address this because no one sees market access as more important. It's not -- it's more important for Puerto Rico than probably any municipality you know.

And so what did they do? They engaged in pension reform, they increased the income tax, they increase -- significantly increased revenues for the aqueduct and sewer authority for the highway and transportation authority and as a result well, I would say they're not done. They have reduced their revenue gap from what was at peak of $3.3 billion in 2009 to about 800 million this year. Do I think they'll make it? Do I think that would really be the gap? No. They have a history of doing a little bit worse than they say and they probably

will again. But they don't usually miss by a lot and they're heading in the right direction. And even when we had this recent crisis just a couple of weeks ago, which by the way kudos to anyone who bought the six and a half, 6.5, 20 40, at yield of 10/08 because as of today you would've make at 21 percent return of investment of two weeks. But even when they saw that, the letter that came out from the Treasurer and the Chairman of the board of the GDP had a number of other steps that they could take to get there. So, I think the number one most important thing about Puerto Rico is the political will is there.

The second thing to look at, in my opinion, is the fundamentals. And I keep asking my question, are they over some sort of a tipping point? Is there a point at which it doesn't matter what you do, you're economy is done. You literally have a debt burden that your economy can't possibly support. And we've looked at that relative to Detroit, relative again to Greece and Portugal, relative to Chicago. And interestingly, as I do the math and I do have some math here. So, if you look at Detroit, you take the 18 billion that Kevin Orr says is there, is their total debt including unfunded pension liabilities. And you divide that by the 700 thousand people who are left in Detroit. We've got about $25,000 a person. If you add that to the $55,000 a person that every American has as our share of the national debt, you've got 80,000 relative to per-captia income in Detroit of about 15,000. So, you've got like five times.

In Puerto Rico, that number prior to their pension, their unfunded pension liability is about one, and with their unfunded pension liability included is about one and a half. Greece, just using their debt, because I have no idea what other hidden things there were but just looking at their debt, you're at 1.6 times. Portugal, you're at 1.2 times. Chicago, you're probably at about one time. So, I really think fundamentally Puerto Rico is not pass that tipping point yet, they may be on a slide toward it. When you read articles they'd say they're going to depopulate from 3.7 million down to 2.5 million between now and 2050. I think they may be heading in that direction, but I think it's a very long slide before they get there.

Now, the one question that people keep asking once they hear that is, well, can the market do them in? Will the market seize up as they did two weeks ago and put them a position where they can't possibly refinance their debt. And obviously what we saw which was very

encouraging was we saw investors from other pockets come in and begin to invest once yield's got above a certain point and that was very helpful. But I also think that if they really -- if this really were a crisis of liquidity, that's where I think the U.S. government might be able to step in and do something. It's a bit of speculation when you get to that but I think that, you know, kind of a Mario driving moment for Puerto Rico would be extremely helpful because that's the only thing that I see getting in their way in the short run. And my guess is when this thing dribbles over a long period of time, then of course the last thing you'll ask is well, what does it mean for us and what can we do about it?

What it means for us, I guess, if you look at $5.7 billion of exposure, and you say this is likely to be -- remember there's no bullet, there's no chapter nine, we're not going to get accelerated against. All that's going to happen if something goes wrong is we're going to pay a principal and interest over some period of time as things get restructured and they're likely to engage in some sort of a restructuring. So, put a severity on it and let's say… and this is what do I often present stress tests for our board and let's say you said 20 percent. So, 20 percent severity on $5.7 billion,issay 1.1 after tax, it's about 800. And that's before we try to do something to mitigate our loss. But one most obvious thing that we would do as we've done in the past is step in and buy our own paper if the trades well enough, and that's been a very successful mitigation tool. So, in the absolute worst case, we're talking about that kind of a number against $12 billion of claims spend in the resources.

Dominic Frederico

Yes. And I would caution against the worst case and understand exactly what worst case means, because if you look at it, and Howard hit me on the head. Most of it is about commitment and political will. If you look at every municipality what you've got? You typically have a basically renewable energy source of revenue. It's going to be there all the time. No one can depopulate to zero, and they still have other revenue source. So remember, when we do per capita numbers on Puerto Rico, you're kind of looking at the small end of the telescope because remember most of their economy is driven by tourism which means their population expands every week based on who steps off airplanes and goes in business, their beaches and casinos etcetera. So it's about political will more than anything.

Number two, the majority or half or at least half of our exposure's revenue bonds. Now, let's go back and remember what a revenue bond is, right? You get the revenue provided from the facility, asset or service. Therefore, when you look at severities on revenue bonds they're significantly less. What has the Governor done? He's increased income taxes, gas taxes and water rates. The goal was to put the water authority on its own footing, the electrical utility on its own footing and the transportation on its own footing to make them cash neutral, relative to the central government. You do that and you just took care of half of our problem. And we believe the rate increases had been proposed to get that done. So ok, now you're talking about basically general obligations of the Puerto Rico government and as Howard nailed the head - they don't have that chapter nine hammer.

The only thing where you can get a significant kind of out of body experience which was non-negotiated is if there's a bankruptcy because you're having a third party now kind of calling the shot. Here you don't have that. Therefore, with the requirement that they need access, critically, with the political will behind it, I don't think we get to that kind of standoff here. As Howard said, I think we have a pretty good handle on the numbers. As we look at our exposures, yeah, where I would be concerned is the general obligation bonds, that's about half the exposure we have out there. But, I kind of like the dynamics on what I see so far being provided by the government. Does that means we're out of the woods? Absolutely not. We continue to monitor, we spend a lot of time, obviously as you can understand. But these are people that understand their need to get to the capital markets and they're people that seem to be making the right economic moves to make sure they get this thing in a better balance position, and always remember long-term liabilities. You got plenty of time to correct the issue and you've got assets. Although, Puerto Rico tends to sell off everything they can find that creates value. There are still assets out there they can be monetized.

Interviewer

Any other questions from the audience here? No. I think we've got a couple of minutes left. So, maybe Dominic, just a broader question, industry type question. It used to be financial guarantee industry was like mid to high teens type R.O.E business, certainly as

you said, the interest rate environment probably isn't something that supports that type of environment right now, but maybe in the future. But, just with all the capital moving as well. What type of R.O.Es do think the industry could get back to in the future? Do you think that mid to high teens is achievable, or do you think it settles somewhere lower just because of the capital standards?

Dominic Frederico

Yes. I think more of the latter, I think it settles somewhere lower. I think all companies in the financial services business because of the concern of the -- scare of the meltdown and the new capital requirements whether it's Basel III, Solvency II, wherever you turn around it's a lot more restrictive. So, for us it's understood what the capital requirements are, make sure we get to that level of capital to make it efficient, and I believe you can still deliver a plus 10 return in our business, even in today's circumstances. And then obviously as interest rates would improve, the return and what is relative to the absolute value of return in the portfolio since most of our assets were in the investable securities.

Interviewer

Okay, great. Thanks. Alright. Well, if there's nothing else I think we'll end it there, and thank you very much for coming today.

Dominic Frederico

Thanks.