

## Q3 2021 Earnings Call

### Company Participants

- David McElroy, Executive Vice President and Chief Executive Officer, General Insurance
- Mark Lyons, Executive Vice President and Chief Financial Officer
- Peter Zaffino, President & Chief Executive Officer
- Quentin McMillan, Head of Investor Relations

### Other Participants

- Brian Meredith, Analyst
- Elyse Greenspan, Analyst
- Joshua Shanker, Analyst
- Meyer Shields, Analyst
- Michael Phillips, Analyst

### Presentation

#### Operator

And ladies and gentlemen, please standby. Good day and welcome to the AIG's Third Quarter 2021 Financial Results Conference Call. Today's conference is being recorded. And now at this time, I would like to turn the conference over to Quentin McMillan. Please go ahead, sir.

#### Quentin McMillan {BIO 19411547 <GO>}

Thank you, Jake. Today's remarks may contain forward-looking statements, including comments related to company performance, strategic priorities, including AIG's pursuit of separation of its Life and Retirement business, business mix and market conditions, and the effects of COVID-19 on AIG. These statements are not guarantees of future performance or events and are based on management's current expectations. Actual performance and events may differ materially.

Factors that could cause results to differ include factors described in our third quarter 2021 report on Form 10-Q, our 2020 annual report on Form 10-K and other recent filings made with the SEC. AIG is under no obligation and expressly disclaims any obligation to update any forward-looking statements whether as a result of new information, future events or otherwise. Additionally, some remarks may refer to non-GAAP financial measures. The reconciliation of such measures to the most comparable GAAP figures is included in our earnings release, financial supplement and earnings presentation, all of which are available on our website [www.aig.com](http://www.aig.com).

With that, I would now like to turn the call over to Peter Zaffino, President and CEO of AIG.

## **Peter Zaffino** {BIO 15942020 <GO>}

Good morning and thank you for joining us today to review our third quarter results. I'm pleased to report that AIG had another outstanding quarter as we continue to build momentum and execute on our strategic priorities. We continue to drive underwriting excellence across our portfolio, we're executing on AIG 200 to instill operational excellence in everything we do, we are continuing the work on the separation of Life and Retirement from AIG, and we're demonstrating an ongoing commitment to thoughtful capital management.

I will start my remarks with an overview of our consolidated financial results for the third quarter. I will then review our results for General Insurance, where we continue to demonstrate market leadership in solving risk issues for clients while delivering improved underwriting profitability and more consistent results. I will also comment on certain market dynamics, particularly in the property market as well as recent CAT activity and related reinsurance considerations as we approach year-end. Next, I'll review results from our Life and Retirement business, which we continue to prepare to be a standalone company. I will also provide an update on the considerable progress we're making on the operational separation of Life and Retirement from AIG and our strong execution of AIG 200.

I will then review capital management where our near-term priorities remain unchanged from those I've outlined in the past, debt reduction, return of capital to shareholders, investment in our business through organic growth and operational improvements. Finally, I will conclude with our recently announced senior executive changes that further position AIG for the long term. These appointments were possible due to the strong bench of internal talent and significantly augment the leadership team across our company. I will then turn the call over to Mark, who will provide more detail on our financial results and then we'll take your questions.

Starting with our consolidated results, as I said, AIG had another outstanding quarter continuing the terrific trends we've experienced throughout 2021. Against the backdrop of a very active CAT season and the persistent an ongoing global pandemic, our global team of colleagues continue to perform at an incredibly high-level delivering value to our clients, policyholders and distribution partners. Adjusted after-tax income in the third quarter was \$0.97 per diluted share compared to \$0.81 in the prior year quarter. This result was driven by significant improvement in profitability in General Insurance, very good results in Life and Retirement, continued expense discipline and savings from AIG 200 and executing on our capital management strategy.

In General Insurance, global commercial drove strong top line growth and we were especially pleased with our adjusted accident year combined ratio, which improved 280 basis points year-over-year to 90.5%. These excellent results in General Insurance validate the strategy we've been executing on to vastly improve the quality of our portfolio and build a top performing culture of disciplined underwriting. One data point that I believe demonstrates the incredible progress we have made is our accident year

combined ratio for the first nine months of 2021, which was 97.7%, that's including tax. This represents a 770 basis point improvement year-over-year with 600 of that improvement coming from the loss ratio and 170 from the expense ratio.

In Life and Retirement, we again had solid results, primarily driven by improved investment performance and increased call and tender income. This business delivered a return on adjusted segment common equity of 12.2% for the third quarter and 14.3% for the first nine months of the year and we recently achieved an important milestone in the separation process by closing the sale of a 9.9% equity stake in Life and Retirement to Blackstone for \$2.2 billion in cash. We continue to prepare the business for an IPO in 2022 and we'll begin moving certain assets under management to Blackstone. We ended the third quarter with \$5.3 billion in Parent liquidity after redeeming \$1.5 billion in debt outstanding and completing \$1.1 billion in share repurchases. Year-to-date, we have reduced financial debt outstanding by \$3.4 billion and have returned \$2.5 billion to shareholders through share repurchases and dividends. We expect to redeem or repurchase an additional \$1 billion of debt in the fourth quarter and to repurchase a minimum of \$900 million of common stock through year-end to complete the \$2 billion of stock repurchase we announced on our last call. Through these actions, we've made clear our continuing commitment to remain active and thoughtful about capital management.

Now let me provide more detail on our business results in the third quarter. I will start with General Insurance where, as I mentioned earlier, growth in net premiums written continue to be very strong and we achieved our 13th consecutive quarter of improvement in the adjusted accident year combined ratio. Adjusting for foreign exchange, net premiums written increased 10% year-over-year to \$6.6 billion. This growth was driven by Global Commercial, which increased 15% with Personal Insurance flat for the quarter. Growth in Commercial was balanced between North America and International with North America increasing 18% and International increasing 12%. Growth in North America Commercial was driven by excess casualty which increased over 50%, Lexington wholesale which continue to show leadership in the E&S market and grew property and casualty by over 30%, financial lines which increased over 20% and crop risk services which grew more than 50% driven by increased commodity prices. And International Commercial financial lines grew 25%, Talbot had over 15% growth and liability had over 10% growth. In addition, gross new business in Global Commercial grew 40% year-over-year to over \$1 billion. In North America, new business growth was more than 50% and in International, it was more than 25%.

North America new business was strongest in Lexington, financial lines and retail property. International new business came mostly from financial lines and our specialty businesses. We also had very strong retention in our in-force portfolio with North America improving retention by 200 basis points and International improving retention by 700 basis points. Turning to rate, strong momentum continued with overall global commercial rate increases of 12%. In many cases, this is the third year where we have achieved double-digit rate increases on our portfolio. North America commercials overall 11% rate increases were balanced across the portfolio and led by excess casualty which increased over 15%, financial lines which also increased over 15%, and Canada where rates increased by 17% representing the 10th consecutive quarter of double-digit rate increases. International commercial rate increases were 13% driven by EMEA excluding Specialty, which increased

by 22%; U.K. excluding Specialty, which increased 21%; Financial Lines, which increased 24%; and Energy, which was up 14%, its 11th consecutive quarter of double-digit rate increase.

Turning to Global Personal Insurance, we had a solid quarter that reflected a modest rebound in net premiums written in Travel and Warranty offset by results in the Private Client Group due to reinsurance sessions related to Syndicate 2019 and non-renewals in peak zones. Shifting to underwriting profitability, as I noted earlier, General Insurance's accident year combined ratio ex-CAT was 90.5%. The third quarter saw a 150 basis point improvement in the accident year loss ratio ex-CAT and a 130 basis point improvement in expense ratio, all of which came from the GOE ratio. These results were driven by our improved portfolio mix achieving rate in excess of loss cost trends, continued expense discipline and benefits from AIG 200.

Global Commercial achieved an impressive accident year combined ratio ex-CATs of 88.9%, an improvement of 290 basis points year-over-year and the second consecutive quarter with a sub 90% combined ratio results. The accident year combined ratio ex-CATs for North America Commercial and International Commercial were 90.5% and 86.8% respectively, an improvement of 370 basis points and 210 basis points. In Global Personal Insurance, the accident year combined ratio ex-CATs was 94.2%, an improvement of 220 basis points year-over-year driven by improvement in the expense ratio. Given the significant progress we have made to improve our combined ratios and our view that the momentum we have will continue for the foreseeable future, we now expect to achieve a sub 90 accident year combined ratio ex-CAT for full year 2022. After three years of significant underwriting margin improvement, we believe that the sub 90 accident year combined ratio ex-CAT is something that not only will be achieved for full year 2022, but that there will continue to be runway for further improvement in future years.

Turning to CATs, as I said earlier, the third quarter was very active with current industry estimates ranging between \$45 billion and \$55 billion globally. We reported approximately \$625 million of net global CAT losses with approximately \$530 million in Commercial. The largest impacts from Hurricane Ida and flooding in Europe where we saw net CAT losses of approximately \$400 million and \$190 million respectively. We have put significant management focus into our reinsurance program, which continues to perform exceptionally well to reduce volatility, including strategic purchases for wind [ph] that we made in the second quarter.

Reinsurance recoveries in our International per occurrence, Private Client Group per occurrence, and other discrete reinsurance programs also reduced volatility in the third quarter. We expect any fourth quarter CAT losses to be limited. Given that we are close to attaching on our North America aggregate cover and our aggregate cover for rest of the world, excluding Japan. We have each and every loss deductible to \$75 million for North America wind, \$50 million for North America earthquake, and \$25 million for all other North America perils and \$20 million for International. Our worldwide retention has approximately \$175 million remaining, before attaching in the aggregate, which would essentially be for Japan CAT.

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Taking a step back for a moment, I want to acknowledge the frequency and severity of natural catastrophes in recent years. Since 2012 and excluding COVID, there have been 10 CATs with losses exceeding \$10 billion and nine of those 10 occurred in 2017 through the third quarter of this year. Average CAT losses over the last five years have been \$114 billion, up 30% from the 10-year average, and up 40% from the 15-year average. And to 2021 catastrophe losses exceed \$100 billion and we're already at \$90 billion through the third quarter, this will be the fourth year in the last five years in which natural catastrophes have exceeded this threshold.

We've never seen consistent CAT losses at this level and as an industry, need to acknowledge that frequency and severity has changed dramatically as a result of climate change and other factors. I'll make three observations. First, while CAT models tended to the trend acceptable over the last 20 years, that has not been the case over the last five years. Second, over the last five years, on average, models have been 20% to 30% below the expected value at the lower return periods. If you add in wildfire, those numbers dramatically increase. Third, industry losses compared to model losses at the low end of the curve have been deficient and need rate adjustments to reflect the significant increase in frequency in CATs.

To address these issues at AIG, we have invested heavily in our CAT research team to develop our own view of risk in this new environment. As a result of this work, we made frequency and severity adjustments for wildfire, U.S. wind, storm surge, flood as well as numerous other perils in International. We will continue to leverage new scientific studies, improvements in vendor model work and our own claims data to calibrate our views on risk over time to ensure we are appropriately pricing CAT risks. Across our portfolio, our strategy and primary focus has been and will continue to be to deliver risk solutions that meet our clients' needs while aligning within our risk appetite, which takes into consideration terms and conditions, strategic deployment of limits and a recognition of increased frequency and severity. The significant focus that we've been applying to the critical work we've been doing is showing through in our financial results as you've seen over the course of 2021 with improving combined ratios both including and excluding CATs.

Now turning to Life and Retirement, earnings continue to be strong and in the third quarter were supported by stable equity markets, modestly improving interest rates relative to the second quarter and significant call and tender income. Adjusted pretax income in the third quarter was approximately \$875 million. Individual Retirement, excluding Retail Mutual Funds which we sold in the third quarter, maintained its upward trajectory with 27% growth in sales year-over-year. Our largest retail product index annuity was up 50% compared to the prior year quarter.

Group Retirement collectively grew deposits 3% with new group acquisitions ahead of prior year, but below a robust second quarter. Kevin and his team continue to actively manage the impacts from a low interest rate and tighter credit spreads environment and their earlier provided range for expected annual spread compression has not changed as base investment spreads for the third quarter were within the annual eight to six points guidance.

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With respect to the operational separation of Life and Retirement, we continue to make considerable progress on a number of fronts. Our goal is to deliver a clean separation with minimal business disruption and emphasis on speed execution, operational efficiency and thoughtful talent allocation. We have many work streams in execution mode including designing a target operating model that will position Life and Retirement to be a successful standalone public company separating IT systems, datacenters, software applications, real estate and material vendor contracts and determining where transition services will be required in minimizing their duration with clear exit plans. We continue to expect an IPO to occur in the first quarter of 2022 or potentially in the second quarter subject to regulatory approvals and market conditions.

As I mentioned on our last call, due to the sale of our affordable housing portfolio and the execution of certain tax strategies, we are no longer constrained in terms of how much of Life and Retirement we can sell on an IPO. Having said that, we currently expect to retain a greater than 50% interest immediately following the IPO and to continue to consolidate Life and Retirement's financial statements until such time as we fall below the 50% ownership threshold. As we plan for the full separation of Life and Retirement, the timing of further secondary offerings will be based on market conditions and other relevant factors over time.

With respect to AIG 200, we continue to advance this program and remain on track to deliver \$1 billion of run rate savings across the company by the end of 2022 against the cost to achieve \$1.3 billion. \$660 million of run rate savings are already executed or contracted with approximately \$400 million recognized to date in our income statement. As with the underwriting turnaround, which created a culture of underwriting excellence, AIG 200 is creating a culture of operational excellence that is becoming the way we work across AIG.

Before turning the call over to Mark, I'd like to take a moment to discuss the senior leadership changes we announced last week. Having made significant progress during the first nine months of 2021 across our strategic priorities and in light of the momentum we have heading towards the end of the year, this was an ideal time to make these appointments. I'll start with Mark, who will step into a newly created role, Global Chief Actuary & Head of Portfolio Management for AIG on January 1st. As you all know, over the last three years, Mark has played a critical role in the repositioning of AIG. He originally joined AIG in 2018 as our Chief Actuary and this new role will get him back into the core of our business, driving portfolio improvement, growth and prudent decision making by providing guidance on important performance metrics within our risk appetite and evolving our reinsurance program.

Shane Fitzsimons will take over from Mark as Chief Financial Officer on January 1st. Shane joined AIG in 2019 and a strong leadership help to accelerate aspects of AIG 200 and instill discipline and rigor around our finance transformation, strategic planning, budgeting and forecasting processes. He has a strong financial and accounting background having worked at GE for over 20 years and many senior finance roles including as Head of FP&A and Chief Financial Officer of GE's International operations. Shane has already begun working with Mark on a transition plan and we've shifted his AIG 200 and Shared Services responsibility to other senior leaders.

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We also announced that Elias Habayeb has been named Chief Financial Officer of Life and Retirement. Elias has been with AIG for over 15 years and was most recently our Deputy CFO and Principal Accounting Officer for AIG as well as the CFO for General Insurance. Elias has deep expertise about AIG and his transition to Life and Retirement will be seamless as he is well known to that management team, the investments team that is now part of Life and Retirement, our regulators, rating agencies and many other stakeholders. Overall, I'm very pleased with our team, our third quarter results and the tremendous progress we're making on many fronts across AIG.

With that, I'll turn the call over to Mark.

### **Mark Lyons** {BIO 6494178 <GO>}

Thank you, Peter, and good morning to all. I am extremely pleased with the strong adjusted earnings this quarter of \$0.97 per share and our profitable General Insurance calendar quarter combined ratio which includes CATs of 99.7%. The year-over-year adjusted EPS improvement was driven by a 750 basis point reduction in the General Insurance calendar quarter combined ratio, strong growth in net premiums written and earned and a related 280 basis point decrease in the underlying accident year combined ratio ex-CAT. Life and Retirement also produced strong APTI of \$877 million along with a healthy adjusted ROE of 12.2%.

The quarter's strong operating earnings and consistent investment performance helped to increase adjusted book value per share by 3% sequentially and nearly 9% compared to one year ago. The strength of our balance sheet and strong liquidity position were highlights in the period as we made continued progress on our leverage goals with a GAAP net leverage reduction of 90 basis points sequentially and 350 basis points from one year ago today to 26.1%, generated through retained earnings and liability management actions.

Shifting to General Insurance, due to our achieved profitable growth to date together with demonstrable volatility reduction and smart cycle management makes us even more confident in achieving our stated goal of sub 90% accident year combined ratio ex-CAT for full year 2022 rather than just exiting 2022.

Shifting now to current conditions, the markets in which we operate persist in strength and show resiliency. AIG's global platform continues to see rate strengthening internationally, which adds to our overall uplift unlike more U.S. centric competitors. As you recall, International Commercial rate increases lagged those in North America initially, but beginning in 2021, as noted by Peter in his remarks, International is now producing rate increases that surpass those strong rates still being achieved in North America and in some areas, meaningfully so. These rate increases continue to outstrip loss cost trends on a global basis across a broad band of assumptions and are additive towards additional margin expansion. In fact, for a more extensive view, within North America over the three-year period 2019 through 2021, product lines that achieved cumulative rate increases near or above 100% are found with an excess casualty both admitted and non-admitted, property lines both admitted and non-admitted and financial lines. We believe these

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levels of tailwind will continue driving earned margin expansion into the foreseeable future.

In the current inflationary environment, it's important to remember that products with inflation sensitive exposure basis such as sales, receipts and payroll act as an inflation mitigant and furthermore are subject to additional audit premiums as the economy recovers. Last quarter, we provided commentary about U.S. portfolio loss cost trends of 4% to 5% and then some aspects were viewed as being near-term. We believe that this range still holds, but now gravitates towards the upper end given another quarter of data and in fact, our U.S. loss cost trends range from approximately 3.5% to 10% depending on the line of business.

From a pricing perspective, we feel that we are integrating these near-term inflationary impacts into our rating and portfolio tools and we are not lowering any line of business loss cost trends since lighter claims reporting may be misconstrued as a false positive due to COVID-19 societal impact. It's also worth noting that all of our North America Commercial Lines loss cost trends with the exception of workers' compensation are materially lower than the corresponding rate increases we are seeing. This discussion around compound rate increases and loss cost trends collectively give rise to the related topic of current year loss ratio picks or indications and the result in bookings. The strong market that we now enjoy in conjunction with a significant underwriting transformation at AIG has driven other aspects of the portfolio that affect loss ratios.

In many lines and classes of business, the degree that cumulative rate changes have outpaced cumulative loss cost trend is substantial and these lead to meaningfully reduce loss ratio indications between 2018 and the 2021 years. Unfortunately, this is where most discussions usually cease with external stakeholders. However, in reality, that is not the end of the discussion, but merely the beginning. Some other aspects that can have material favorable implications towards the profitability of underlying businesses are; one, terms and conditions which can rival price and the impact; two, a much more balanced submission flow across the insured risk quality spectrum, thereby improving rate adequacy and mitigating adverse selection; three, strategic capacity deployment across various layers of an insurance power which can produce preferred positioning and ongoing a retention with the customer; and four, reinsurance that tempers volatility and mitigates net losses.

Accordingly, even if modest loss ratio beneficial impacts are assigned to each of these nuances, they will additionally contribute to further driving down the 2021 indicated loss ratio beyond that signaled by rate versus loss trend alone. And these are real and these are happening. So why our product lines booked at this implied level of profitability by any insurer? Well, there is at least four reasons. First, insurers assume the heterogeneous risk of others and each year is composed of different exposures rendering so called on level projections to be in perfect. Second, most policies are written on an occurrence basis which means the policy language can be challenged for years if not decades, potentially including novel theories of liability. Third, many lines are extremely volatile and even if every insured is underwritten perfectly -- even if every insured is underwritten perfectly. And fourth, booking an overly optimistic initial loss ratio nearly increases the chance of



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future unfavorable development. Therefore, these types of issues require prudence in the establishment of initial loss ratio picks for most commercial lines of business.

Shifting now to our third quarter reserve review, approximately \$42 billion of reserves were reviewed this quarter, bringing the year-to-date total to approximately 90% of carried pre-ADC reserves. I'd like to spend a little time taking you through the results of our quarterly reserve analysis, which resulted in minimal net movement confirming the strength of our overall reserve position. On a pre-ADC basis, the prior year development was \$153 million favorable. On a post-ADC basis, it was \$3 million favorable. And when reflecting the \$47 million ADC amortization on the deferred gain, it was \$50 million favorable in total. This means that our overall reserves continue to be adequate with favorable and unfavorable development balanced across lines of business, resulting in an improved yet neutral alignment of reserves.

I'll be forward looking at the quarter on a segment basis. I'd like to strip away some noise that's in the quarter, so we don't get overly lost in the details. One should think of this quarter's reserve analysis as performing all of the scheduled product reviews and then having to overlay two seemingly unrelated impacts caused by the receipt of a large subrogation recovery associated with the 2017 and 2018 California wildfires.

The first of these two impacts is the direct reduction from North America Personal Insurance reserves of \$326 million resulting from the subrogation recoveries. As a result, we also had the reverse a previously recorded 2018 accident year reinsurance recovery in North America Commercial insurance of \$206 million. Since the attachment point was no longer penetrated once the subrogation recoveries were received. These two impacts from the subrogation recovery resulted in a net \$120 million of favorable development. So, excluding their impact restates the total general insurance PY date as being \$70 million unfavorable in total rather than the \$50 million of favorable development discussed earlier. This is a better framework to discuss the true underlying reserve movements this quarter.

This \$70 million of global unfavorable stems from \$85 million unfavorable in global CAT losses together with \$15 [ph] million favorable in global non-CAT or attritional losses. The \$85 million unfavorable in CAT is driven by marginal adjustments involving multiple prior year events from 2019 and 2020. The \$15 million non-CAT favorable stems from the net of \$255 million unfavorable from global commercial and \$270 million of favorable development, predominantly from short-tail personal lines businesses within accident year 2020, mostly in our International book. Consistent with our overall reserving philosophy, we were cautious towards reacting to this \$270 million favorable indication until we allow the accident year this season.

North America commercial had unfavorable development of \$112 million, which was driven by financial lines strengthening of approximately \$400 million with favorable development in other lines led by workers' compensation with approximately \$200 million emanating mostly from accident year 2015 and prior and approximately \$100 million across various other units. North America Financial Lines were negatively impacted by primary public D&O largely in the more complex national accounts arena and within private not-for-profit

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D&O unit in addition to sell excess coverage mostly in the public D&O space with 90% emanating from accident years 2016 to 2018.

International Commercial has unfavorable development of \$143 million which was comprised of financial lines strengthening in D&O and professional indemnity of approximately \$300 million, led by the U.K. and Europe, but the accident year impacts are more spread out. Favorable development was led by our Specialty businesses at roughly \$110 million with an additional favorable of approximately \$50 million stemming from various lines and regions.

Now, as Peter noted, the changes we made to our underwriting culture and risk appetite over the last few years, coupled with strong market conditions are now showing through in our financial results. U.S. Financial Lines, in particular, through careful underwriting and risk selection has meaningfully reduced our exposure to securities class actions or SCA losses over the last few years. Evidence of this underwriting change is best seen through the proportion of SCAs for which the U.S. operation has provided coverage. In 2017, AIG provided D&O coverage to 67 insureds involved in SCAs, which represents 42% of all U.S. Federal security class actions in that year. Whereas in 2020, that shrunk suggest 18% and through nine months of 2021 is only 15% insureds or 14%. This is significant because roughly 60% to 70% of public D&O lost dollars historically M&A from SCAs.

The North America private not-for-profit D&O book has also been significantly transformed. The policy retention rate year between 2018 and 2021, which is a key strategic target is just 15%. Again, it should also be noted that the corresponding cumulative rate increase over the same period is nearly 130%. This purposeful change in risk selection criteria away from billion-dollar revenue large private companies and non-profit universities and hospitals to instead a more balanced, middle market book will also drive profitability substantially.

International Financial lines has implemented similar underwriting actions with comparable three-year cumulative rate increases along with a singular underwriting authority around the world has respect U.S. listed D&O exposure through close collaboration with the U.S. Chief Underwriting Officer. In summary, our reserving philosophy remains consistent and that we will continue to be prudent and conservative. This is evidenced by our slower recognition of attritional improvements in short tail lines from accident year 2020 and from the sound decisions that strengthen Financial Line reserves, even though there are some interpretive challenges stemming from a difficult claims environment, changes within our internal claims operations over the last couple of years and potential COVID-19 impacts on claim reporting patterns. All of these underwriting actions we've taken over the last few years make us even more confident in our total reserve position across both prior and current accident years.

Moving on to Life and Retirement, the year-to-date ROE has been a strong 14.3% compared to 12.8% in the first nine months of last year. APTI during the third quarter saw higher net investment income and higher fee income offset by the unfavorable impact from the annual actuarial assumption update, which is \$166 million pre-tax, negatively affected the ROE by approximately 250 basis points on an annual basis and EPS by \$0.15 per share. The main source of the impact was in the Individual Retirement division

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associated with fixed annuity spread compression. Life Insurance reflected a slightly elevated COVID-19 related mortality provision in the quarter, but our exposure sensitivity of \$65 million to \$75 million per 100,000 population deaths proved accurate based on the reported third quarter COVID related deaths in the United States. Mortality exclusive of COVID-19 was also slightly elevated in the period.

Within Individual Retirement, excluding the retail mutual fund business, net flows were a positive \$250 million this quarter compared to net outflows of \$110 million in the prior year quarter, largely due to the recovery from the broad industry wide sales disruption resulting from COVID-19 which we view as a material rebound indicator. Prior sensitivities in respect to yield and equity market movements affecting APTI continue to hold true and new business margins generally remain within our target at current new money returns due to active product management and disciplined pricing approach.

Moving to other operations, the adjusted pre-tax loss before consolidations and eliminations was \$370 million, \$2 million higher than the prior quarter of 2020, driven by higher corporate GOE primarily from increases in performance-based employee compensation, partially offset by higher investment income and lower corporate interest expense resulting from year-to-date debt redemption activity.

Shifting to investments, overall net investment income on an APTI basis was \$3.3 billion, an increase of \$78 million compared to the prior year quarter, reflecting mostly higher private equity gains. By business, Life and Retirement benefited most due to asset growth, higher call and tender income and another strong period of private equity returns. General Insurance's NII declined approximately 6% year-over-year due to continued yield compression and underperformance in the hedge fund position. Also, General Insurance has a much higher percentage allocation to private equity and hedge funds, which is likely to change moving forward.

As respect to share count, our average total diluted shares outstanding in the quarter were 864 million and we repurchased approximately 20 million shares. The end of period outstanding shares for book value per share purposes was approximately \$836 million and anticipated to be approximately \$820 million at year-end 2021 depending upon share price performance given Peter's comments on additional share repurchases.

Lastly, our primary operating subsidiaries remain profitable and well capitalized with General Insurance's U.S. pool fleet risk-based capital ratio for the third quarter estimated to be between 450% and 460% and the Life and Retirement U.S. fleet is estimated to be between 440% and 450%, both above our target ranges.

With that, I'll now turn it back over to Peter.

**Peter Zaffino** {BIO 15942020 <GO>}

Great, Mark. Thank you. Operator, we'll take our first question.

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## Questions And Answers

### Operator

(Operator Instructions) And we will begin with Elyse Greenspan with Wells Fargo.

#### Q - Elyse Greenspan {BIO 17263315 <GO>}

Hi, thanks. Good morning. My first question, when you guys -- Peter, when you make the comment that you think you'll hit sub 90% for full year 2022 and then you said that there would be runway for further improvement in future years, I'm just trying, when you kind of think 2022 and beyond, what are you guys assuming for both pricing and loss trend as we kind of think out the next year even beyond that timeframe?

#### A - Peter Zaffino {BIO 15942020 <GO>}

Well, thanks, Elyse. Let me answer the first part why we are so confident that the momentum that we have and the sub 90% combined ratio is achievable. When you look at this quarter and last quarter, just the improvement from the core of the business is, continues to improve at an accelerated pace. And Dave McElroy and the leadership team on the underwriting side, Shane who has not moved in the CFO role, drive an AIG 200, just the execution has been terrific. And why we're confident is just again the momentum when we look at the fundamentals of the business, we're growing top line. We talked, Mark and I, about that we're getting pricing above loss cost developing margin expense ratio, all of that goes into our confidence. We have higher retentions on a policy count, very strong new business and think that a flight to quality. We have more relevance each quarter in the marketplace.

And so the assumptions are modest. It's not that it has to stay in the same pricing environment, but it is one that we are going to continue to be very disciplined of driving profitability and making sure that where we're deploying capital that on a risk adjusted basis, we're going to be getting margin. So I think that -- again, I don't want to give guidance beyond that, but feel that next year we have the momentum, we're executing on all of our strategic imperatives and we're delivering the results.

#### Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay, thanks. And then my follow-up on, you guys said that the Life IPO should take place in the Q1, perhaps in the second quarter of next year, how do we think about capital return? I know you guys have laid out a plan for this year, but how should we think about capital return on next year and is that dependent on when and the ultimate size of what you bring to market with the Life and Retirement business in the IPO?

#### A - Peter Zaffino {BIO 15942020 <GO>}

Well, we were trying to give a lot of guidance in terms of what we intend to do in the short run because of the number of moving pieces. We have strong liquidity, which is what we had talked about in the prepared remarks. Some of the big moving pieces as we get to the back half of the year will be the affordable housing proceeds, the closing of Blackstone, the fact that we're going to continue to execute on debt reduction, share

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repurchases. And I think as we get to the fourth quarter call and we have a better line of sight in terms of what we think the actual timing will be on the IPO plus liquidity at year-end, we'll give further guidance as we move forward, but for now, I think we're just going to stick with what we've outlined and we continue to execute on that each quarter.

**Q - Elyse Greenspan** {BIO 17263315 <GO>}

Okay, thank you.

**A - Peter Zaffino** {BIO 15942020 <GO>}

Thanks, Elyse. Next question.

## Operator

We will now take the next question from Meyer Shields with KBW.

**Q - Meyer Shields** {BIO 4281064 <GO>}

Thanks. I guess first question for Peter, you laid out pretty conservative case for the frequency and severity of catastrophes, how should we think about what Validus Re is interested in writing in that context?

**A - Peter Zaffino** {BIO 15942020 <GO>}

Thanks, Meyer. Well, I mean Validus Re, since we've acquired them, we have not increased risk appetite. And as a matter of fact, they take a very conservative position in terms of their net. And I think that was evidenced in the quarter in terms of our overall CAT number, that's number one. I think Chris Schaper and the team have done a terrific job of diversification on the portfolio. So we've reduced our aggregates in peak zone such as Florida significantly from the original portfolio that we acquired. We're getting better balance in the portfolio across the world and that's with multiple parallels and multiple geographies. So I think that that continuation of that strategy of getting balanced diversification and making sure that we're not taking significant nets in the portfolio and making sure that we're driving risk-adjusted returns as we look to one-one is going to be very important for Validus Re, but we've been executing on that throughout the year.

**Q - Meyer Shields** {BIO 4281064 <GO>}

Okay, understood. Thanks. And then as a follow-up for Mark, is there any way of describing -- I mean, you made a very strong case for conservatism in the current accident year loss guys. I'm wondering how you're thinking about that level of conservatism in recent accident years as of 9/30.

**A - Peter Zaffino** {BIO 15942020 <GO>}

Go ahead, Mark.

**A - Mark Lyons** {BIO 6494178 <GO>}

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Thanks. Yeah, thank you, Peter. Thanks, Meyer. Actually we feel very good about accident year '20 and '21 (Technical Difficulty) core of your question. And I think I made a pretty strong case for the changes that have occurred, which I think have been -- I think pretty in the list on it. And interestingly overall, I'm confident not just in the current accident years. I'm confident where we are on the reserve position even. And for financial lines and in total across the book, you can kind of say, well, why are you confident and there's a lot of reasons for it. I mean, when Dave McElroy and his group got it in here, they started making some pretty material underwriting changes step by step. And I think it's just endemic upon the analysis of it for not only the past years, but with the current year to focus exactly what those changes were and then go back with a very tight eye to look at it and that's exactly what we did. But the transformation of the book as I itemized on private not-for-profit and public is been enormous. So I feel very strongly about where we are on those recent years.

#### **A - Peter Zaffino** {BIO 15942020 <GO>}

Mark as you mentioned Financial Lines, I think maybe Dave could provide some context as to some of the changes and how he is looking at the portfolio. So, Dave, maybe you can add to what Mark commented on.

#### **A - David McElroy** {BIO 15192036 <GO>}

Yes. Thank you, Peter. Thank you, Mark. See I know it's probably top of mind, but the Financial Lines book has been one that has been stored at AIG. And most of you know, I've been involved with P&L in Financial Lines for my entire 40-year career. So I've seen the bodies float by me, I've the strategies avowed and disavowed. And we know exactly what we are doing when we came in here to look at this portfolio. So today, I would say that both North America and International are completely different and fundamentally different books than what we had in the 16 to 18 cohort years. That's personal to me. That's also Michael Price who is running North America for us.

But we did the things that are -- that matter. And we've been doing it across all of our lines of business in terms of risk selection, limit management, portfolio balance, the diligence on terms and conditions, Mark talked about little bit on private. And then we're measuring it on claims. So this is what -- this I view this as the story that we needed to complete, Mark hit our public company book that is by and large the measure of D&O underwriter. And if you're in the public company space, you're talking about your securities class action exposure and the 67% of your annual loss costs are driven by those cases.

So when you think about that, let's say, it's a math equation of 200 of these are normally filed at 5,500 total public company. So risk selection matters. What we found here was probably chasing premium versus chasing quality accounts. So, we might -- we were overweighted in technology and life science and healthcare, new economy and unicorns trying to go public instead of trying to build a portfolio of what I consider be stable, less volatile stocks. So from a company class industry standpoint, we gave some more definition to our underwriting teams about what they should be looking at and then trying to stay away from what I consider to be the target rich environment of the plaintiffs bar which are stock volatility, market cap volatility and basically a ready-made securities class action case.

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So that's a lot of the re-underwriting that's been done. It's -- we know it's going to take a little bit of time. The evidence of that is now showing up. We've taken out \$65 billion of limits. You've heard our story around \$650 billion of limits taken out across the portfolio, \$65 billion of it is in these products alone. And more importantly and that's sort of often how I'm looking at the businesses is we took it out on primary D&O, okay. So the natural order of looking at large Fortune 500 companies used to be at \$25 million, they're now at \$10 million. 81% of our portfolio is at \$10 million there versus what would have been \$25 million four years ago. The same with a, what I consider to be Nasdaq Mid Cap, they were 15s and 10s, they are now 5. 66% of the book is now 5.

So we've compressed limits. We've addressed the retention issue. We're trying to -- we recognize that M&A bump up claims were actually affecting primary underwriters and I think that's been on other calls, they were affecting primary underwriters more desperately than excess underwriters. So we increased our retentions there. These are all the tools that were always available to us. We just actually push them forward. And we're trying to get in front of it, but basically we believe strongly that this portfolio today is a very different portfolio from a risk selection standpoint, from a balance perspective in terms of excess in side A [ph] versus primary versus the limits versus our controlling the aggregate.

I would also sort of finalize that by saying this is a claims made book. So in many ways, we will actually know within that three to five year window all the work that's been done and our frequency and severity has dropped dramatically in these 2021 years. Not only securities class actions, we're running at less than half, but because of limit management, we're running at two-thirds lower in terms of limits exposed to class action manager -- class action suits as well. So these are the tools (Multiple Speakers)

**A - Peter Zaffino** {BIO 15942020 <GO>}

Actually it's coming through very much. We would probably want to take another question.

**A - David McElroy** {BIO 15192036 <GO>}

Yeah, I am finished. And then, by the way we have gotten compounded rate increases of 100%. So I apologize, that's (Multiple Speakers)

**A - Peter Zaffino** {BIO 15942020 <GO>}

Thank you. Next question.

**Operator**

Next we will hear from Michael Phillips with Morgan Stanley.

**Q - Michael Phillips** {BIO 21023048 <GO>}

Thanks. Good morning. I'll be two quick ones I think. Mark, your comments on again the loss pick thing. Number two was I think about, well, the current stuff and it's long tailed and actually the risk and so we're going to be conservative (inaudible) industry. I think that was

your number two. Can you tell us, has there been any kind of shift in your book given everything else you guys have done in from occurrence to claims made in the commercial lines of book? So anything noteworthy that would shift away from occurrence to claims made?

**A - Mark Lyons** {BIO 6494178 <GO>}

Great question, Michael. So I would say there is only a handful that are really claims made, right. It's management liability, it's professional indemnity that really drive it and actually super tough product liability and cases that's really claims made. It's one thing that shift its growth, it's another thing that shift its net, right. So as we've used different reinsurances over time that changes the proportions. So we're comfortable with the mix of a currency claims made. There is growth in Financial Lines as Peter pointed out and there is some growth in excess casualty. The nets are somewhat different, but we think appropriate for what we've done.

**Q - Michael Phillips** {BIO 21023048 <GO>}

Okay, perfect. Thanks. And then if I may just a real quick pointed on two on the last question to Dave answers in the professional lines. There's clearly lots of concerns in the past 18 months or so because of securities class actions and IPOs inspects. Would you say given all the Dave's comments there that you think your exposure to that type of risk is pretty limited?

**A - Mark Lyons** {BIO 6494178 <GO>}

Well, yeah, I think how Dave explained is the way the business actually flows -- business actually work. So the key thing is upfront identifying the right classes and the right risk which they've really done I think exceptionally well. And then the second is what goes through the court systems given the FSCAs even though we are massively reduced in the FCAs. You got to go through all the motions to dismiss and another procedurals that take you there. So that's what Dave's comment about three plus three to five years has to work its way through the court system. But given our reduced exposure back to similar answer, that makes us feel strongly about the recent accident year.

**Q - Michael Phillips** {BIO 21023048 <GO>}

Okay. Thanks, Mark.

**Operator**

Next question Joshua Shanker, Bank of America.

**Q - Joshua Shanker** {BIO 5292022 <GO>}

At the risk of being labelled pariah, I'm going to go back to the D&O questions a little bit. Can we talk little bit about the accident year picks, not necessarily for AIG, although can be, what sort of combined ratios were 16, 17 and 18 producing in retrospect? We've seen tremendous pricing come through. Is D&O business broadly for the industry written in those years being written at a substantial underwriting loss. And the extent to which you



took the reserve charges in this quarter, a lot of the business I think was syndicated, are the Syndicate feeling the same kind of theme that you are or you getting ahead of what you think are losses to come?

**A - Peter Zaffino** {BIO 15942020 <GO>}

Mark, what do you comment on Josh's question on loss ratios? And then I think Dave should talk about the pricing.

**A - Mark Lyons** {BIO 6494178 <GO>}

Josh, I know you're speaking of business. And if you go back -- because speaking to the industry is a little different, I don't want to get out ahead of the industry. But I know you are a schedule fee guy. You go back and look at that, of course, that's U.S. only and you can look direct, not just in that. And that's a combination of management liability and professional right in there, but we know it's dominated by the management liability side. So you can go back and look at the annual statements through 2020 and get an idea, but with regard to syndication and Dave will pick this up better than I will, but generally primaries are 100% written. And as you go up the tower, there could be some co-participations. But it's not syndicated like in a huge property transaction the way you're thinking of it. But Dave, do you want to pick that up.

**A - David McElroy** {BIO 15192036 <GO>}

Yeah, thanks, Mark. And, Joshua, the only thing I'd say there is that you've seen a lot of variability in the schedule piece in terms of portfolios over the years. There can be 40 to 50 point differences consistently, so that speaks to risk selection in the portfolios. But that said, there is definitely verticality that's been happening in those years that is showing up in the 2019 and 2022, 2020 years because the courts did not close for this motion dismiss and the securities class action. So, in fact, if you look at cornerstone, there were equal number of settlements in 2020 during COVID that there were in 2019.

So verticality still exists in this business, market cap loss disclosed damages and what that happened. So I think there's a lot of immaturity in those years that will continue to show up because the cases are still sort of fermenting. There is a three-year to five-year window on these claims made. It all ties to the motion dismissed. But they continue to be argued. I think what we saw was a lot of them were argued. And then when they are decided on in the client's behalf, then you start negotiating settlements, okay. If the company wins, they normally go away therapeutics or defense costs, but that's still an unknown in that 16 to 18 cohort year as the verticality of loss in those cases, okay. A number of them got settled in '20, there is a number that are still getting settled in '21 and there still be a number that will be settled in '22.

**Q - Joshua Shanker** {BIO 5292022 <GO>}

I am now holding at one question for you guys. And just congratulations on everyone's new role.

**A - Peter Zaffino** {BIO 15942020 <GO>}

Thank you. Next question.

## Operator

Brian Meredith with UBS. Go ahead.

### A - Peter Zaffino {BIO 15942020 <GO>}

And if it's a financial question on the Financial Lines, it will be the last one because I'm going to have to turn it over to Dave again.

### Q - Brian Meredith {BIO 3108204 <GO>}

Thanks. I'll give you a broader based one. If I look at the return on attributed equity for the General Insurance business right now, you had some corporate cost there, it's still below a double-digit return on equity. I guess my question is, is that's your goal to achieve a double-digit ROE in that business? And what is the underlying combined ratio need to be in order to achieve that given the kind of current catastrophe outlook in interest rate environment?

### A - Peter Zaffino {BIO 15942020 <GO>}

Thanks, Brian. As we've said in the past and I really have the same answer, which is we're really focused on driving the profitability earnings, reducing volatility. We're making great progress on the combined ratio looking at the investment portfolio over time to have less volatility on the property and casualty side. We're working through the separation. And it's hard to give you an answer in terms of the absolute combined ratio and returns until we know all the math in terms of the numerator and denominator meaning we just need a little bit more time over the next couple of quarters to separate Life and Retirement, have the paths of the IPO and the capital structure that we will outline in more detail for you, but we know that that is an important guidance in terms of when we are in future state and we'll work towards that. But I think now with a number of moving pieces between the 9.9% in terms of what we're doing to set up the IPO and what we're doing with General Insurance in terms of growth, we see a lot of opportunities to grow with margin and with improved combined ratios over time. And so that's really the primary focus now and that giving the ROE guidance once we know the variables a little bit more fixed, we can do that.

### Q - Brian Meredith {BIO 3108204 <GO>}

That's fair. Thanks. And then just one other, just quick one, have you done any work or maybe just some general perspective on what LGTI could mean for your Life Insurance business?

### A - Peter Zaffino {BIO 15942020 <GO>}

Well, we are in progress of implementing the new standards and working through it. And so we're analyzing the guidance that's been issued today, formulating approach. We know that we have the IPO coming up, so we have enormous amount of resources on it, but it's

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really just too early for us to provide the estimates, but it's a key area of focus for the company and one that will give guidance as we get in subsequent quarters.

**Q - Brian Meredith** {BIO 3108204 <GO>}

Got it, thanks.

**A - Peter Zaffino** {BIO 15942020 <GO>}

Thanks, Brian. I think that's going to wrap it. Looking at, I really appreciate it -- appreciate the time, want to thank all of our colleagues for all the great work and hope everybody has a great day. Thank you.

## Operator

And with that ladies and gentlemen, this will conclude your conference for today. We do thank you for your participation and you may now disconnect.

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