UBS Virtual Specialty Insurance/Reinsurance Conference

Company Participants

- Christopher Schaper, Chief Executive Officer
- Mark Lyons, Executive Vice President and Chief Financial Officer
- Sabra Purtill, Deputy Chief Financial Officer, Head of Treasury

Other Participants

- Brian Meredith, Analyst

Presentation

Brian Meredith {BIO 3108204 <GO>}

Good afternoon, everybody. This is Brian Meredith. I'm the North American Insurance analyst here at UBS and welcome to our next fireside chat here with AIG. Quick introduction here of who we have with us. First, we've got Chris Schaper, who is the CEO of AIG RE. He is going to give us some updates on the reinsurance market and how AIG is responding, ask him some questions about that. We've also got Mark Lyons, Chief Financial Officer; Sabra Purtill, the Deputy CFO and Shelley Singh, Investor Relations. We'll focus on some other questions with them as well little bit later.

To begin though, I know Mark and Chris have some introductory comments they want to convey to everybody. And with that I'm going to turn it over to Mark.

Mark Lyons {BIO 6494178 <GO>}

Great. Thank you, Brian. And it's great to be here again. I don't think it was that long ago, maybe August or something, it is sometime in the summer.

Brian Meredith {BIO 3108204 <GO>}

Yeah.

Mark Lyons {BIO 6494178 <GO>}

Great. So thanks for the invite for you and your team and asking us here and setting everything up to that.

So a few introductory comments. First of, I think it's clear in October. We had a few announcements that came out and besides normal earnings, we had some management changes that we discussed. But I think perhaps the primary announcement that of interest the most was centered on our attention to the separate our Life & Retirement businesses. And I think as we noted on the call that we, in conjunction with a set of advisors, thought that was in the best long-term interest of value creation and are going in that route. And quite frankly, none of that would be possible without a strong general insurance operations. And I think we've talked at length about the material changes that have occurred over the last few years to enable that. So I just want to kind of put that out there. Firstly, the momentum in general Insurance I think is palpable. And I'm sure, Brian, you and your constituents have a few questions in that regard and we're happy to go there.

So with that, it's just a very, very brief introduction. Let me turn that over to Chris for him to make a few comments as well.

Christopher Schaper {BIO 17403314 <GO>}

Great. Okay guys. Thanks, Mark. And it's great to be here as well. Good afternoon, everyone. I'm Chris Schaper. I'm the CEO of AIG Re. I thought I give you a little background on AIG Re for those that are not very familiar with the Company, the organization itself.

First off, we started in mid 2019 and the Company is up as comprised of companies that were within the Validus Group. And for those that -- to give a little bit background on Validus, Validus had both insurance and reinsurance operations as part of it. The reinsurance businesses were segmented off and are now part of AIG Re.

In particular, they encompass three enterprises, Validus -- sorry, I apologize, Validus Re is one of the entities in AIG Re. So Validus Re itself is a traditional reinsurer and deploys capital through its balance sheet as a traditional reinsurance would. Talbot Treaty is another enterprise that is part of AIG Re. It was part of Validus Re when the acquisition occurred as well. Talbot Treaty is part of Talbot Syndicate. And Talbot Syndicate in essence deploys capital through a Lloyd's syndicate approach. And then there is AlphaCat. And AlphaCat is an asset manager that operates in the reinsurance space and it has roughly about $4 billion of assets under management. So those three enterprises were part of the Validus Group initially and now would make up AIG Re.

It certainly been a very busy year for the team. COVID-19 has continued impact in the reinsurance market quite substantially. And in particular beyond that, it's also been a very active storm season for 2020. And so from a frequency point of view, as you know, we got into the Greek alphabet for the various storms that took place in 2020.

Prior to that, certainly the last few years were very active as well from a storm point of view. So twin COVID and the active storm season and other issues associated within the reinsurance market, it's become a very dynamic environment.

What we're seeing in the market right now is that positive pricing is certainly taking place in almost every line. Still early on for more terms and signings, but those are being worked through as we speak. That's been very active capital flow in the reinsurance space. You may have seen significant new scale ups or new start-ups for both traditional reinsurance as well as for alternative capital entities. But overall makes really interesting time for those of us in the reinsurance space and of itself. That being said, just a few other comments that this is not 2002 or 2006. We're -- at that point in existing markets, we're frankly scrambling to engage. This is very different. This is an incumbent market. Existing entities with strong balance sheets, with strong client-broker relationships, with strong bench strength, with strong operations, et cetera, are definitely there to take on this particular market, which again is different from where things were previously. And those enterprises frankly are the ones that have a very strong position for success.

Our clients right now prefer certainly markets that are very active, there they seek to -- that seek to offer quotes out to the market and seek to deploy their capital effectively and seek to properly engage kind of across the board within the spectrum of reinsurance. And so, again, we're seeing some very -- it's very active time period right now, but again, those enterprises that have all of those underlying components that I just mentioned are very, very good shape to actually execute.

I'm sure we'll talk about the reinsurance market overall, but those are just a few opening comments and I'll turn it back over to you, Brian.

Questions And Answers

Q - Brian Meredith {BIO 3108204 <GO>}

Thanks, Chris. Yeah. So why don't we just follow on to that, get a lot more detail here and just thoughts here. So obviously genuine renewals coming up here. One of the markets everybody loves to focus on is property CAT, which was clearly -- Validus was one of the leaders and probably still is one of the leaders in property CAT reinsurance. Maybe you can talk a little bit about what you see happening in the North American property CAT market for property CAT reinsurance? And then maybe also the property retro market and kind of the interplay there and what you're seeing happening?

A - Christopher Schaper {BIO 17403314 <GO>}

Sure. Okay, yeah, so North American reinsurance, yes, first off, North America represents about 50% of the business that we have. So just generally in the overall insurance space, very important market in of itself. In that market, need to separate business out between loss based business -- loss based treaties, if you will, versus non-loss based treaties. And those that have not been loss based, we're certainly seeing rate increases really kind of across the board. I think it's kind of the first comment that I'll make. Where we are seeing treaties that have had losses that have come in, whether those are through property, certain circumstances or other circumstances, we're definitely seeing further rate improvement that's happening there beyond what we had seen in the normal market where there were no losses. So pretty much kind of across the board. As I said, we're seeing very strong rate movement in that respective area.

That being said, the incumbent markets are really the markets that are really leading this entire area. So we may have seen some additional firms that are trying to come into being here. Those companies are really not that, I would just say, influential at all in this particular market. It's really the incumbents. And those are the ones that are focusing on the rates and the quotes and getting all of that sorted for the respective markets.

From a retro point of view, yes for sure, we're seeing rate movement in the retro space. And that -- those rates can be certainly significant double-digit rate increases that are taking place in the retro space. And that being said, there is additional capital that's come in and that actually perhaps creates greater competition in that overall field. So we are seeing enhanced competition that's taking place in the retro market year-over-year from what we saw last year. So all the rates are up, competition is up as well.

Q - Brian Meredith {BIO 3108204 <GO>}

Interesting. So I'm just curious on that topic Chris, and we'll get more into market conditions here in a second. Just remembering back with Validus, I mean Validus was the very active user of retrocessional reinsurance as well to manage the exposure and take advantage of market conditions and stuff. Has that changed at all in the new AIG construct? And is there still a relationship and how do you manage that?

A - Christopher Schaper {BIO 17403314 <GO>}

Yeah, I mean Validus certainly is active on both spectrums of that. And really that in and of itself has not specifically changed relative to Validus pre AIG or Validus post AIG. And its -- they're active prior, they're active currently. Focus on us prior and certainly current is on properly underwriting risk across the board. So that tenant is absolutely part of the perspective that we bring to the table as an organization. The issue of further protecting the organization through different management means such as retrocessional protections, et cetera, is also -- has been a mainstay of the organization and continues to be to this day.

As we think about that, we do think about various structures, so we can have structural changes that may be integrated year-over-year. But in general, in terms of the user retrocessional protection and how we think about it, is definitely part of the risk management program that we have.

Q - Brian Meredith {BIO 3108204 <GO>}

Got you. Perfect, thank you. And then we talked about property CAT, property retro sounds good. What about some of the other areas of the property market maybe non-property, non-CAT property, as well as quota share, risk programs, how those -- how's that market shaping up right now?

A - Christopher Schaper {BIO 17403314 <GO>}

Yeah, on the quota shares, the value proposition there is again the underwriting rate movement that's happening in the primary lines of business. Those lines are on the move. So from a quota share point of view, we think that there is an intriguing area for us to engage in. I would view that will continue to move down that path with certain markets. It's not -- we don't really just kind of spread ourselves across everywhere. We are particularly selective and how we think through the insurance that we're engaging with. And there are companies that actually have greater influence in terms of how they try to engage with the market and those companies are the companies that we're seeking to do more business with if you will. So from a quota share point of view, yeah, we think that there is an interesting aspect of the business happening there. But again, primarily due to the rate movement, that's happening in the underlying business. So that would be intriguing for us.

When you think beyond the pure property space, casualty markets are definitely moving. They're moving for real reason. When you think about what's existing in the financial environment and also think about social inflation and different issues such as that, there is a real need for those areas to accelerate in rate.

So again, it's about being with the right companies that are tackling those issues on a regular basis. And so we think there's some opportunities there too.

Q - Brian Meredith {BIO 3108204 <GO>}

That's terrific. And then, maybe kind of going across the pound over to Europe, what do you see going on in Europe right now?

A - Christopher Schaper {BIO 17403314 <GO>}

Yeah. We see - we do see right movement there too. And I think, I mean, there's certain areas that are important that you look at across the board, and it tends to be - the U.S. tends to move, kind of depending on the circumstances, more specifically than what you would see in the European markets, but we are seeing European markets move as well. So, we think there's value proposition there too.

And that's a different - it's a different portion of the world, and they have different exposures that they're - they take on. You know, hurricane risk is not one of those, but they do have wind-based risk, et cetera.

So there are differences, but we are seeing a movement that's happening there in those markets in themselves. And so we think there is some interesting opportunities there as well.

Q - Brian Meredith {BIO 3108204 <GO>}

Interesting. I mean, I haven't heard that comment as far as moving in European reinsurance pricing for a while, at least to be upside.

A - Christopher Schaper {BIO 17403314 <GO>}

Yeah, it's true. And we've seen it in some other markets too outside of that. They hadn't seen that movement happen previously. So, as far as I'd say, generally you see rate movements that are happening. So we say that definitely a difference will be seen in the 2021 renewal than what we had seen prior.

Q - Brian Meredith {BIO 3108204 <GO>}

Got you. And let's just back onto the cap comment with respect to capital. I appreciate what you're saying that, it's the incumbents that are kind of driving this marketplace right now. But we have seen a lot of new capital get raised this year, and instead of new startups seen that have happened. And then, also, you've got a lot of trapped capital sitting in the alternative market right now that is clearly kind of tied up. Do you think that market changes as we go throughout 2021, maybe that capital is more of an influence on big year renewals, something like that happens, what happens is trapped capital, kind of releases.

A - Christopher Schaper {BIO 17403314 <GO>}

Yes. Do I - let's make sure I am clear on your question? Do you view -- is the question whether I view that the alternative capital coming, rate is going to have an influence?

Q - Brian Meredith {BIO 3108204 <GO>}

Yeah, What -- I guess what I'm trying to do is when I get questions a lot of times people says like, okay, great, one, one's fine, but do you think it gets better or worse during the course of 2021. Some companies will say, I'm going to deploy more capital. I'm going hold back on some of my capital, because I think it gets better here going forward.

And that may be conditioned upon what happens with some of this new capital that's in the marketplace, or, perhaps the $15 billion to $20 billion of trapped capital with alternative players. Does that start to free-up as COVID losses become more, more norm?

A - Christopher Schaper {BIO 17403314 <GO>}

Yeah, it'll take a little time, yes for that. I mean, rest I would say your numbers are probably right and accurate in terms of how we're seeing it. And, yes, I mean it's going to take a little time for things to play out fully in terms of what COVID may or may not mean for the overall industry itself. As that does, get known though for sure that, there's an opportunity for that money to be released, and then, kind of considered to be deployed, right. So, it doesn't necessarily have to be deployed, but it's considered to be deployed.

So there is - yes, there's an opportunity possibly for that to be coming back into the market. But it's going to take a little time for those circumstances to be known. So in the meantime, I think we're going to have - that's not something that's going to happen, altogether quickly in 2021. I think that's going to take definitely some time through that year, if not beyond that for sure.

Q - Brian Meredith {BIO 3108204 <GO>}

Got you. It makes sense. And then, it's around a little bit here, as we looked throughout 2021, any thoughts on kind of what Florida could potentially look like or the Japanese renewals?

A - Christopher Schaper {BIO 17403314 <GO>}

Yeah, I mean, I think, they're progressively -- I think, similarly from what we've seen in one-one, I think we would see those progressing as well in terms of rates. I would imagine that would be taking place. And there certainly have been -- there have been storms that happened in Japan over the past few years, and so that needs to be considered. There has also been -- certainly frequency that's taking place you know relative to wind events, obviously in 2020.

Now the frequency issue is important and obviously severity going along with frequency is even that much more important. And I would just say that, all those particular items need to be effectively thought through, if you're deploying capital. So I would envision that you'll see continual movement in those respective territories as we progress through the renewal cycle.

Q - Brian Meredith {BIO 3108204 <GO>}

Great, thanks. And let's pivot over to AlphaCat. We talked little bit of alternative capital. What are you seeing in AlphaCat with respect to funds managed or is there increasing investor demand for this asset class? How the investors -- are they more diligent in kind of when they look to make these investments given what we've seen historically?

A - Christopher Schaper {BIO 17403314 <GO>}

Yeah. There's -- I mean there's certainly an interest in insurance and reinsurance space, there's no doubt with that. And every year that happens, I would say investors get more and more intelligent, which is important to us. So we wanted to have -- we want to make sure that we have many investor coming into space that is very, very -- that they're very knowledgeable. I would say year-over-year we're certainly seeing that. And they're good conversations that happen as a result.

So I think, what you ultimately seeing here is, alternative capital thinking through insurance or reinsurance more considerably than they had previously, particularly when they looking at their own environments relative to investment opportunities that they might have.

And so, a combination between knowledge of the space that is enhanced year-over-year, along with capital available has certainly shown to actually increase the interest in our space. So I will anticipate that that will continue. And so, yes, I mean, there's definitely an interest in AlphaCat and I would just say overall in the alternative capital space within reinsurance business.

Q - Brian Meredith {BIO 3108204 <GO>}

Great, thanks. Pivot a little bit, more specifically COVID related losses. I know you mentioned in the last call that part of the COVID related charge was Validus Re. Where does the losses typically come from in Validus when you see a COVID related loss? And then, should we expect COVID related losses as you think? And let's say not necessarily from Validus, but just the industry in general, to continue to see some more COVID related losses as we go into 2021 because some of the lag that you got with the reinsurers as well as attachment point, you're probably going to start to get hit on some of these programs.

A - Christopher Schaper {BIO 17403314 <GO>}

I think you'll probably still see some COVID coming in 2021 as renewed item. As the programs get renewed, the insurers are trying to give you a fresh or refreshed view of their loss areas, which you need to understand the risk that you're taking on. So I would imagine that as we continue to move through 2021 that will continue to get, no additional information relative to that from a prospective insurers.

If you think about it like when the renewal cycle tends to be -- you've got April renewal cycle, the June, July, kind of October in terms of kind of key time periods. So, I would expect that we're going to see that. We tend to see the losses coming through on the BI side -- on the property in BI side that for sure is the area.

And then we also would see it, kind of, in the event and credit side of the house as well. But, everything's manageable for sure and it's a matter of just understanding the perspective of your insured, in terms of how they're thinking about COVID and how they're thinking about the loss scenario. So some insured are at X point and some are at Y and they all have different perspectives as to how they see no COVID playing out of it, but doesn't be the primary resolution.

Q - Brian Meredith {BIO 3108204 <GO>}

Are there still disputes between what the Stephens think that are COVID related losses in the reinsurers are? I know that early on there was a lot of questions about whether CAT reinsurance contracts actually pick up some of this COVID related losses. Is that kind of been settled?

A - Christopher Schaper {BIO 17403314 <GO>}

Yeah, I mean, I wouldn't want to say disputes and there may be a difference.

Q - Brian Meredith {BIO 3108204 <GO>}

Yeah, that's better word.

A - Christopher Schaper {BIO 17403314 <GO>}

But, I think there's -- whenever there's wording out there, you're always working through it with the respective market and new brokers as well. So, I think, mostly level-headed parties come to the table and just try to, kind of, get out what everyone was thinking about.

But, there's always -- there's wording that can be a little bit more broad than others and that could be interpreted more broadly, or less. So, yes, I would say that there's still be continual conversations happening.

I think in the greater scheme of things, I would just say that, a lot of the perspectives have been already kind of brought to the table. I don't sort of know, if you're really going to see anything that is, kind of, headline news in terms of how's everyone's worrying that one would've thought about.

So, I think, in many ways there's an understanding as to how wordings should be considered. How it ultimately plays out will still be kind of TBD. But again, I think, for the most part, the parties have a sense for what is likely coverage and what is likely not yet covered. So, it's still going to play out a bit further.

Q - Brian Meredith {BIO 3108204 <GO>}

Got you. I think you kind of alluded to what my next question is, and that was my -- what kind of notable changes are you seeing in terms and conditions going into this dual season, right? I mean, COVID (inaudible) I guess it wouldn't be COVID exclusion, but communicable diseases exclusions, those types of things or are there any other interesting ones that are kind of popping up?

A - Christopher Schaper {BIO 17403314 <GO>}

Yes, so the communicable diseases, as you said. I would also say that, cyber has certainly been an avenue that has been very significantly discussed. As people think about potential loss activity that could occur, obviously, that area is one that is pretty paramount for everybody to think through, to consider. So that's been one area that we've had a decent amount of conversation.

There have been some term and condition changes associated with that on our contracts as a result. There should have been rate movement there too, without a doubt there's been rate movement on the cyber business. So, I would say that, that's probably -- we're looking at key areas where there have been the discussions, that's probably been the most significant outside of the communicable disease arena.

Q - Brian Meredith {BIO 3108204 <GO>}

Got it. It is the cyber side. Yeah, I mean it sounds like there has been some reasonable amount of loss activity in the cyber business this year, is that true?

A - Christopher Schaper {BIO 17403314 <GO>}

There been some, but yeah, I mean, it's up, but that's not, I would say, my opinion. That's not really the issue. I mean, obviously, losses are always an area of conversation for all parties, but I would say, frankly, the more significant issue is the fact that cyber can be very extreme circumstance if -- running through multiple policyholders, one particular circumstance, one particular event, right. It can it can have very significant ripple effects throughout not just one or two or three policyholders, millions of policyholders, and that could have an effect overall on the insurer and ultimately, it's in the reinsurance. So, it's much more of an endemic issue. It's much more of a kind of a very specific issue within the coverage itself, as opposed to just losses that may be starting to show up now. So, it's just a -- it's a deeper discussion with a deeper issue than just purely a loss issue in terms of what we're seeing today.

Q - Brian Meredith {BIO 3108204 <GO>}

Yeah, makes sense. And another one that I'm trying to ask most companies is what are your thoughts on the current CAT models out there? I mean, obviously alternative markets used to -- use some fairly heavily AIR, RMS. Do they adequately reflect the frequency and severity of hurricanes and other types of catastrophe losses out there right now? And how do you use them? How do you think about them in your business? What's your thought on -- are we seeing an increase in frequency and severity?

A - Christopher Schaper {BIO 17403314 <GO>}

I think we've complaint to an increase in frequency that's have, I think this year is an example of that. Obviously, 2005 is another example of that. So, we've seen that, but obviously, everyone's got to be cautious about kind of jumping on the frequency band rate, you've got to take it under a very -- take a very specific viewpoint on that and just try to put into context.

The models we think of models as certainly a strong tool for us to use. I mean, we've always been a very significantly focused model shop here. And we think it's very an extremely important for us to consider that. We have an entire research business. That's part of our overall reinsurance team, greater than 50 people or so that are part of our reinsurance research operation within reinsurance, so just typically for research.

And has everything from PhDs to modelers, to different people with different quantitative skills, et cetera. So, it's a very important aspect of our -- of how we think about risk. And with the models, we use some models for certain types of risks and exposures, and we use other models for other types of risks and exposures.

And what's most important is that you focus on validated and addressing each model, that's what's really important. You need to look at each model in terms of what it's trying to offer you, and assess whether you think there's significant value or not so much, and then try to think is there a need to augment that further.

And so when we look at models, as I said, I mean, we use as mentioned a couple names and obviously those would be important names for us and there are other modeling firms that are out there that we think bring value to the table as well. So, we do look at models as an integral part of what we do.

As far as thinking through the frequency and severity issues, I think what is important; we're doing it independent of the models is looking at climate change and really trying to understand what that might mean. And then trying to think through, should the models be augmented to try to consider that.

I think there's a couple other things that are important to consider here and that is, on the one hand, you need to think about kind of the short-term perspective that you want to bring to the table, make sure you understand that. And I'm not saying that within the models you have short-term and long-term kind of effects, if you want to think through the -- how to augment models, so you can think that's what I said that's not what I'm trying to get to.

What I'm trying to get to here is that, it's important that we think through kind of a short and medium term perspective, and also think through a long-term perspective, because we're trying to make sure that we're able to effectively execute for our insurance, but we also need to make sure that when we execute, they're executing safely and effectively for AIG. And then we also need to be thinking through, how that -- what that means to regulatory bodies et cetera, making sure that we're really thinking through the spectrum of our respective parties as we consider models integrating into our business.

So there's a lot to actually do, which is also why, first of all, I think it's terrific that we have the researched team the way that we do. They're their own business in and of themselves. And they helps us quite substantially and trying to think through these varying issues as we're trying to consider risk on a regular basis.

Q - Brian Meredith {BIO 3108204 <GO>}

Makes a lot of sense. So -- and one more here, just on the reinsurance side. I mean, or two more actually, one, you kind of talked about it, but just kind of dig a little more, as you think of -- that was good, probably you answered that one. One question I've kind of ask everybody, as we look into 2021 in the reinsurance markets, what do you think the surprises could be, or is there a surprise? I mean, what do you think, potentially happen would be like, wow, that's a surprise, I couldn't -- didn't expect that to happen?

A - Christopher Schaper {BIO 17403314 <GO>}

Yeah. Wait I'm in Bermuda [ph] here, right? And the other day someone mentioned to me that there was a snowstorm coming in the northeast and they said, I don't know if you're worried. I said it's COVID year, I think it could possibly snow for me as well even with everything that's happened during this. It doesn't work on anything out for sure.

I think there will be surprises I do. I think that -- I think one surprise that people would have right now is the fact that this market has not translated into a market that many has thought, I mean it was just a few months ago, where everyone was thinking that, capital has gone, you got to bring in new capital, you've got to try to figure out, how did -- a new capital got to come and deploy itself, et cetera, has not played out that one. It has been very different -- very, very different from, I would say, just a few months ago in terms of how people were thinking about this. I mentioned in some opening remarks just about the incumbents. And this is an incumbency market right now. This is not everybody was anticipated to the degree that it is.

You have various strong companies that are executing very well. They are looking for additional ratings across the board. And so I think that the surprise might be, how any of these new firms will ultimately try to get gains from this particular market? How they maybe thinking about things? And that's not to take anything away from what they're trying to do. I'm not trying to do that. But what I am saying is that I think -- you've asked me about an area of surprise, I think that might be one that's on the forefront right now.

We look beyond that. I think that it really will come down to more events, how things are playing out, how the economic environment will ultimately play out as well. I think as we come through this whole COVID circumstance, what does it ultimately means for us collectively, not just as a society, but certainly at from a business to business point of view and how do we want to think about that. So I think that's one unknown that's out there and I think within that we actually may have some surprises about how we think about business models, how we think about engaging our existing business as well as our existing capital and what's the best way forward relative to that. So maybe there is a few perspectives I would suggest.

Q - Brian Meredith {BIO 3108204 <GO>}

Sounds good. So let's pivot a little bit here and get Mark involve a little bit here, but -- Chris, you can absolutely comment too. See the returns --

A - Mark Lyons {BIO 6494178 <GO>}

Hey, Brian.

Q - Brian Meredith {BIO 3108204 <GO>}

Yeah.

A - Mark Lyons {BIO 6494178 <GO>}

Would you mind, I'd made a couple notes as you're going through with Chris.

Q - Brian Meredith {BIO 3108204 <GO>}

Yeah.

A - Mark Lyons {BIO 6494178 <GO>}

He is a provider as opposed to us as a purchaser on the insurance side. It's a little bit, perhaps, I could offer on that in various things that I made notes. One is, the Validus in particular with a proprietary approach to modeling and taking little bits and pieces we're augmenting it dramatically. It's probably more the exception in the role and are over generalize on purpose. But I think it's probably fair to say that AIR has used more by reinsurers and RMS more by primary carriers. It's a very generalized statement.

The tails are lot thicker in AIR depending upon the geography and the peril, of course. But if it helps you with the excess pricing, that's what you're going to use, right, more times than not. So I'll offer that. I'd say secondly as you're asking about other areas in the future, 4 -1s, 6-1s [ph] as various areas. From an AIG purchasing perspective, we're not really concerned about availability, let's say, Japan capacity in 4-1. That's a big 4-1 effective they market that is we handle all of that on our 1-1. So we won't have that risk. We won't have any of that issue on a go-forward basis.

And on the topic of on some of the retro, the terms and conditions aspects, you both were talking about the exclusions. So whether it's communicable disease or what have you, or terrorism, I think it's also maybe more in the retro market, more clear of what they're including. These are named peril approaches, right? So you don't have this blanket, didn't sneak through with lousy wording or not. If it's named peril, they're explicitly denoted. So that's kind of a shift that had changed as well.

So back to your surprise question. So the terms and conditions of a tight retro market are going to affect the terms and conditions of the reinsurance market, which could affect the terms and conditions of the primary market presumably once we left home the bag, right, on those things. So will new capacity come in and relax not on price, but on broadening. Terms and conditions are not being named peril, things like that, don't know. It's too early to tell on that.

My last comment will be in this in AIG like holding company perspective in this because PMLs have been dropped dramatically by AIG over the years as Peter has talked about. This really allows opportunity from an AIG Inc. perspective that Validus really sees, risk reward opportunities, all good for them. That could be some expansion there while in the overall AIG context, we're still reducing PMLs in the aggregate.

So, you've got -- Validus has its business plan than AIG has the balance sheet plan as well, a plan, as to not overexposure and the right trade-off. So, anyway, I just want to offer those as a segue.

Q - Brian Meredith {BIO 3108204 <GO>}

Yeah. That that was – so that was kind of an add-on to my question, I mean, this changes your ceded reinsurance program. I mean, you've talked about how it changes the cede reinsurance program will actually benefit your underlying combined ratio. I'm assuming that reducer ceded purchases, right, maybe you can explain a little bit how it affects your underlying? And then also, does that mean that we may see rising PMLs, increasing kind of volatility on the margin here going forward?

A - Mark Lyons {BIO 6494178 <GO>}

Again, it reflects, I'd say, there's a couple ways it helps, achieving the combined ratio goals. The most obvious is the bigger premium you're keeping net. So it's a smaller spend, I got a bigger denominator basically in my expense ratio, right. So it's helpful for that as a componentry.

I think more importantly, it changes the mix of business depending upon whether it's core to share excess or loss that we change. To the extent that we keep more in a hardening, more profitable market on a core to share basis that alters your net mix of business and more rate is fixed at a rates net, as opposed to ceding improved rate performance.

So it helps with that, to the extent that we have different proportions of progress that's a wells CATs, you don't get cede commission's on those, right? So as that mixture changes, it helps your acquisition ratio, because you have a smaller proportion giving you a zero -- effectively. So it's the changes in the mix of business that would provide the OpEx on the expense ratio, both through a bigger net written premium and through changes in the form of the reinsurance that you're purchasing.

Q - Brian Meredith {BIO 3108204 <GO>}

Got you. Okay. So not necessarily increased volatility. Got it all right.

A - Mark Lyons {BIO 6494178 <GO>}

Okay, in terms of the purchases, what are the lenses you look through is not just net underwriting gain, it's the distribution of it, right? So you're looking at your return periods to make sure you're not exposing your balance sheet in any untoward way.

Q - Brian Meredith {BIO 3108204 <GO>}

Got you. Got you. So, no hot topic, can we pivot, maybe to the separation of life business? And one of the questions get -- get a lot of questions about is, on the separation of life insurance business, why don't you consider selling-off pieces of the life insurance operations, right? You know, wouldn't that create potentially more value particularly, there's an active market right now for buying that stuff, a pretty competitive market right now buying annuity blocks etcetera, etcetera. Is there something maybe that we're not considering when we -- when people ask that question and say, well, why don't they do it?

A - Mark Lyons {BIO 6494178 <GO>}

Yeah, there's a lot of synergies that may be the iceberg under the water that isn't as obvious. I mean it's not like every legal entity or every business is doing its own product design or it has a different view mortality or longevity or have a hedge program. That's unique to that. All of that is done horizontally across the board and distribution is leveraged a lot more and it opens the door to PRTs and things of that nature. So it's -- I mean, you never say never, Brian, to something super creative and accretive came in, we wouldn't necessarily shut the door. But that's not the main goal. The main goal is to leverage the platform, leverage the long-term viability of it and we think that's best on keeping it together than separate it.

A - Sabra Purtill {BIO 1764408 <GO>}

And I would just add in that regard is to remind people that we've said that the goal is separation -- full separation and the first step of that is the sale of a minority stake, probably through an IPO. That doesn't mean at other stages the Life and Retirement couldn't look at lots of business and all the rest. But from AIG's objective, what we want is a full legal entity separation and to do that, we continue to take the steps from a legal perspective to effect separation.

Q - Brian Meredith {BIO 3108204 <GO>}

Gotcha. Okay, so that makes sense. So it doesn't rule out transactions, it's just your ultimate goal is to separate the whole thing. But yeah, it's an attractive deal came out to sell a block of life for annuity block or whatever was. Okay, that's good. That’s just helpful.

A - Sabra Purtill {BIO 1764408 <GO>}

And what we've said to people and our employees and our brokers and their staff is, our goal is separation. We're moving down that path. It's not our intention to break things up into pieces and sell them as pieces. We will sell 19.9% stake in the entire entity as the first step.

Q - Brian Meredith {BIO 3108204 <GO>}

Right. That 19.9%, I guess maybe just remind us kind of what do you anticipate the use of proceeds are going to be? How much do you need to pay down debt with the proceeds from that?

A - Mark Lyons {BIO 6494178 <GO>}

Yeah, it's kind of a good question. I mean even before this, Brian, we had debt pre-COVID, right? We had debt as a priority in the capital management strategy. That's clearly still the case. It doesn't preclude other uses of course, but we've kind of described the fact that currently with $4.1 billion raise that we did and some of that was pre-funding, right, maturing debt that we expect at the end of the first quarter to be down with reasonable earnings expectations as well as the maturing debt rolling off that was pre-funded to be back closer to where we were pre-COVID in an AIG Inc. standpoint. But in order to separate, we've given some general guidance of that will be increased debt in order to -- in a structural sense in order to provide the vehicle to pay off AIG's debt. So, there is a real mechanism in place and therefore a goal to continue to have debt reduction as the primary motivator.

A - Sabra Purtill {BIO 1764408 <GO>}

And just to relate people to since this is a public forum, there is two parts of proceeds so to speak from separation. The first would be the initial debt capitalization of the Life and Retirement holding company. I think you can look at precedent transactions that have been done like Equitable where the holding company will borrow money and then use that for pre-IPO dividend to the holding company. That first chunk of proceeds, Mark has been very clear about, would be used to reduce AIG debt.

And then the second amount of proceeds would be the proceeds from the equity stake and for that, that will depend on whether or not we've achieved the debt targets that we've laid out through the use of the first bunch of proceeds. And we're obviously having conversations with the rating agencies around initial capitalization because it is our goal to maintain the insurance financial strength ratings of the legal entities today. The debt ratings will just be an outcome of book leverage calculations and those conversations. But our goal would be that we would, upon full separation, have to separately capitalized holding companies and that AIG's goal would be to have a lower debt ratio as a fully separated entity than we have today.

During the first part of separation, just remember that we would still be consolidating Life and Retirement because we would own 80.1% of it.

A - Mark Lyons {BIO 6494178 <GO>}

Right. So part of that overall goal, Brian, is maintain the ratings, maintain strong RBC, maintain a debt structure, debt part of the capital structure that's competitive and not out of line on either side, right, on Life and Retirement or on the GI, RemainCo piece. So they're primary goals and as Sabra said, that's what we're in depth discussion with the rating agencies about.

Q - Brian Meredith {BIO 3108204 <GO>}

Good outcome. Okay. And then, another one, just curious of your thoughts, so one of the pushback that I get from investors on the separation is, they -- we said we've been there, done that with MET and AXA, right. And wasn't really any value creation when MET spun Brighthouse out to MET shareholders, as well as ditto for AXA shareholders with Equitable. What do you think is different about your separation of your life insurance business versus those two?

A - Mark Lyons {BIO 6494178 <GO>}

Well, first off, we have -- we're a clear composite. Some of those may have been a spin-off of a like kind of subsidiary. So, I think, the transparency of AIG has been, maybe that's an oxymoron, right, on some of those areas. So the insight into Life and Retirement and GI, I think will become so much more clear. The strategies become so much more clear and the investors can be targeted to that.

If you -- if Brian and you know this as well as anyone, if you look back at our stock performance and then pick your period of time, we tend to trade at the lesser of either and a lot of that is due to the -- you can't really see what the underpinnings are. Number one.

Number two is, it's been life and retirement that's really been the salvation of the cash flows to the parent since with before GI was losing money. So, now you have two strong independent platforms. Each of which, in my view, are undervalued. And that value will emerge on its own or -- and you really leverage that structure and the platform that each have.

So, back to that, it's clarity of strategy, clarity of earnings potential, and I think that's some of the main differences.

Q - Brian Meredith {BIO 3108204 <GO>}

Got you. That makes a lot of sense. And just one last question, I got to touch on the Commercial lines business, primary businesses once. Just your thoughts pricing, excessive trend still a really good market for margin expansion as we look into 2021.

A - Mark Lyons {BIO 6494178 <GO>}

Yes, it is. And as we said on the call, we focus on the Commercial lines business, and that's where most of the action is, right, at the end of the day. So, Peter goes into a lot of detail on that. We see it in strength in the U.S. We see it in the strength internationally. It kind of echoing what Chris really said earlier as well. So, that's another distinguishing feature on this cycle. It's not one line of business-driven. It's not one geography-driven. It's really everywhere.

But what I want to caution is that, yes, there's margin expansion. Let me be clear on that. Yes, there's margin expansion. The degree of margin expansion given that in rough numbers half of our book is personal lines is a dampening effect.

So, let's take Peter's numbers in the last quarter. They're like up 17% roughly. And what you're going to have is that worldwide commercial. And if you look at personal lines, you get a few points. Let's make the math easy three points, right.

So, it's roughly split 50/50, that's a 10% average rate increase. Great. Happy to have it. But it's not the level of margin expansion that you would glean. I'm talking about North American Commercial lines only. So, definite margin expansion, I'm just trying to manage expectation.

Q - Brian Meredith {BIO 3108204 <GO>}

No, I get -- I completely get it. Now, let's focused more on the 17% Commercial lines thinking about margins that business, and I get the Personal lines just got its own pressures and own dynamics with travel and a bunch of other things make sense.

Good. All right. So, I think we've hit the 45 minute mark. I want to thank you all very much. Chris, thank you for your insightful comments with respect to the reinsurance markets and everything. I really, really appreciate it. And Mark, Sabra, Shelley, thank you for your time today. Really appreciate it.

A - Mark Lyons {BIO 6494178 <GO>}

Thank you.

A - Christopher Schaper {BIO 17403314 <GO>}

Thank you.