Q4 2020 Earnings Call

Company Participants

- Brian Duperreault, President and Chief Executive Officer
- David McElroy, Executive Vice President and Chief Executive Officer, General Insurance
- Kevin Hogan, Executive Vice President and Chief Executive Officer of Life and Retirement
- Mark Lyons, Executive Vice President Chief Financial Officer
- Peter Zaffino, President and Global Chief Operating Officer, AIG Chief Executive Officer, General Insurance
- Sabra Purtill, Head of Investor Relations

Other Participants

- Elyse Greenspan
- Erik Bass
- Josh Shanker
- Tom Gallagher
- Tracy Benguigui
- Yaron Kinar

Presentation

Operator

Good day and welcome to AIG's Fourth Quarter 2020 Financial Results Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Ms.Sabra Purtill, Head of Investor Relations. Please go ahead, ma'am.

Sabra Purtill {BIO 1764408 <GO>}

Thank you, Orlando. Good morning and thank you all for joining us. Today's call will cover AIGg's fourth quarter and year-end 2020 financial results announced yesterday afternoon. The news release, financial results presentation and financial supplement are available on our website www.aig.com. Our 10-K for 2020 will be filed on Friday, February 19.

Our speakers today include Brian Duperreault, CEO; Peter Zaffino, President and COO of AIG; and Mark Lyons, Chief Financial Officer. Following their prepared remarks, we will have time for Q&A. David McElroy, CEO of General Insurance; Kevin Hogan, CEO of Life and Retirement; and Doug Dachille, Our Chief Investment Officer will be available for Q&A.

Today's remarks may contain forward-looking statements, including comments relating to company performance, strategic priorities, including AIG's intent to pursue a separation of its Life and Retirement business, business mix and market conditions, including 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 materially differ. Factors that could cause results to differ include the factors described in our third quarter 2020 report on Form 10-Q and our annual 2019 annual report on Form 10-K and our other recent filings made with the SEC. AIG is not under any 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 at www.aig.com.

I'll now turn the call over to Brian.

Brian Duperreault {BIO 1645891 <GO>}

Good morning and thank you for joining us today. I'd like to highlight some of the important milestones we achieved in 2020 and then I'll turn it over to Peter to provide more detail on our results for General Insurance and Life and Retirement as well as updates on strategic initiatives such as the separation of the Life and Retirement business and AIG 200. Lastly, Mark will provide a CFO update.

2020 was an extraordinary year during which our company demonstrated tremendous resiliency. We quickly and effectively transitioned more than 90% of our workforce in over 50 countries to remote working. We established a cross functional task force to implement best practices to protect the health and safety of colleagues while continuing to deliver high quality service to clients, distribution partners and other stakeholders. AIG continues to effectively manage through COVID-19 and its collateral effects on the global economy because of the strong foundation we began to build beginning in late 2017.

We instilled a culture of underwriting excellence, adjusted risk tolerances, implemented best-in-class reinsurance programs, strengthened our vast global footprint, derisked the balance sheet and maintained a balanced and diversified investment portfolio. And in October, we announced our intention to separate the Life and Retirement

Business from AIG, which was made possible by the work our team has done to strengthen General Insurance in particular and position each business as a market leader.

Before I turn it over to Peter, I want to note that this is the last earnings call I will participate in. As you know, we announced that on March 1 I will become Executive Chairman of the Board and Peter will take over as President and Chief Executive Officer. The transition will be seamless. Peter and I have tackled many of the systemic and pervasive fundamental problems from the past and the company is now positioned for long term sustainable and profitable growth.

While there is still work to be done, I've every confidence that AIG stakeholders will continue to reap the benefit of the hard work that is taking place across the organization on our journey to make AIG a top performing company. The turnaround of General Insurance and the enterprise wide transformation at AIG is on a scale I have not seen in my 45 plus year career. I take great pride in what the team has accomplished I know that the company and our colleagues will be in great hands with Peter as the CEO of AIG.

Now I'll turn the call over to Peter.

Peter Zaffino {BIO 15942020 <GO>}

Thanks, Brian. Good morning, everyone and thank you for joining us today. This morning, I'd like to cover four topics that are key areas of focus for us in 2021 and which we will update you on each quarter. The separation of Life and Retirement from AIG, capital management, progress we've made on AIG 200, and financial and operating highlights for General Insurance and Life and Retirement. 2020 was a pivotal year for AIG and I'm pleased to report that 2021 has gotten off to a good and fast start due to the momentum we have coming into the new year. Like 2020, this year will be another year of substantial progress for our company.

As Brian noted, we made a critical and strategic decision last October to separate the Life and Retirement business from AIG. We could not have made this decision without the significant turnaround taking place in General Insurance and solid performance in Life and Retirement. Our fourth quarter results provided further evidence that each of our businesses remain financially strong, market leaders and well-positioned for profitable growth over the long term in their respective markets.

Since our last earnings call, we've been working purposefully and with a sense of urgency on several fronts related to separation. We are actively working towards an IPO of up to 19.9% of Life and Retirement with teams focused on standalone audited financials, actuarial work and rating agency discussions among other things. Based on our work to date, we continue to believe that no additional equity capital will be required given the improvement in our subsidiary capital positions over the last few years.

Additionally, in connection with our October announcement, we received inquiries from parties interested in strategically aligning with us and potentially purchasing the 19.9% stake in Life and Retirement. We are pleased with the level of interest and quality of potential partners for Life and Retirement business and believe a sale of a minority stake could be an attractive option for AIG, its shareholders and other stakeholders.

We are carefully weighing the relative merits of this path compared to a minority IPO, taking into account the impact on value creation for AIG, execution, certainty, regulatory and rating agency implications and delivery of Life and Retirement's growth strategy over the long term. As you know, any decisions we make will be subject to regulatory approvals. Overall, I am very pleased with the progress we're making on the separation and we'll provide a further update in the near term.

Turning to capital management. We ended 2020 with parent liquidity of $10.5 billion, a $2.9 billion increase from 2019. We entered 2021 with significant financial flexibility as a result of our focus on derisking, capital management and liquidity, particularly in 2020 as a result of COVID-19. We will continue to invest in our businesses to support growth and operational transformation, and we will return at least $500 million of capital to our shareholders through stock repurchases in the first half of 2021. This amount will more than offset dilution from stock-based compensation, which at a minimum will be a core principle of our capital management strategy going forward.

As we move forward on the path to separate Life and Retirement and generate capital, we will continue to focus on delevering and investing in growth in our businesses. We also intend to be active and prudent managers of capital and return it to shareholders when appropriate. Our current expectation is that an initial disposition of 19.9% of Life and Retirement whether through a minority IPO or sale to a third party will generate net proceeds such that some portion can be used towards further share repurchases.

And while it is not currently a priority, over time, we may consider inorganic growth opportunities that would be accretive to our businesses and growth strategy and otherwise create value for our shareholders and other stakeholders. Once we make a decision on the initial step of the separation of Life and Retirement, we will provide more detail on our medium and longer term capital management priorities.

Now I'd like to provide an update on AIG 200. As a reminder, AIG 200 has four core objectives; under writing excellence, modernizing our operating infrastructure, enhancing user and customer experience, and becoming a more unified company. Throughout 2020, we made measurable progress in spite of the ongoing remote work environment and in some cases accelerated certain initiatives. On December 31, we completed the sale of our shared services operations to Accenture, which streamlines our operating model. We've made significant progress in driving improvements in infrastructure and systems architecture, while reducing real estate costs and other general operating expenses.

We exceeded our target run rate savings for 2020 and the costs required to achieve were lower than initially expected. We exited 2020 with a $400 million run rate benefit, which was 30% ahead of the guidance we provided in 2020. The success of AIG 200 to-date demonstrates the discipline and rigor that the team leading the strategic initiative is using. The team is taking decisive action as we execute to position the company for the long term. AIG 200 success to-date also reflects the resiliency and flexibility of our global colleagues who have embraced change while making significant contributions to our progress.

In 2021, a major focus of AIG 200 will be advancing our digital strategy through effective use of data and process enabling technologies as well as driving greater operational efficiencies and improved customer experience. We also expect to make significant progress in 2021 on a global data warehouse in support of our finance and underwriting transformations. Our overall target for AIG 200 remain unchanged. We still expect to achieve run rate savings of $650 million by the end of 2021 and to deliver aggregate run rate savings of $1 billion by the end of 2022 against the total investment of $1.3 billion.

Turning to our financial results. I'll start with General Insurance. In the fourth quarter of 2020, we saw growth in net premium written in our commercial businesses with year-over-year net premium written increasing 7% after adjusting for foreign exchange driven by improved retention and higher rates. North America commercial grew approximately 10% with meaningful growth from AIG Re and international was up 5% after adjusting for foreign exchange. As we previously outlined, North America Personal Insurance continued to experience reduced net premium volumes. This was primarily due to our decision to strategically reposition our high net worth business to Syndicate 2019, the partnership we established with Lloyd's, which resulted in higher ceded premium and the impact of COVID-19 on lines such as travel and accident health. While it's still very early in the year based on what we are seeing, we expect a similar overall growth trend to continue particularly in commercial and we will achieve top-line growth for the full-year 2021.

Turning to the combined ratio. We achieved another quarter of positive results in our core business with continued improvement in underwriting margins. In the fourth quarter, the accident year combined ratio excluding CATs improved by 290 basis points to 92.9% compared to 95.8% a year ago. This improvement was led by our commercial businesses, which improved our accident year combined ratio excluding CATs by 440 basis points with international commercial improving by 490 basis points and North America commercial improving by 400 basis points. The adjusted accident year combined ratio for the full-year 2020 was 94.1%, a 190 basis point improvement year-over-year. Commercials adjusted accident year combined ratio for the full-year 2020 was 93.2%, a 340 basis point improvement year over year. These combined ratio improvements reflect very strong performance as General Insurance continues to benefit from an improved business mix in the commercial portfolio, driven by the strategic underwriting actions we've been taking.

Turning to rate. In the fourth quarter, we continue to see considerable improvement and tighter terms and conditions. In commercial, we saw a sustained strong rate momentum and improvement across all lines of business with the exception of workers compensation. For the fourth quarter, our commercial business achieved rate increases of approximately 15%. North America commercial rate increases were 21% in the fourth quarter compared to 14% in the prior year quarter. This improvement was driven by excess casualty, which saw rate increases of 45%, financial lines with rate increases of over 25% led by 35% increases in D&O, retail property and Lexington wholesale property both achieving approximately 30% rate increases, and Lexington casualty with 25% rate increases.

International commercial rate increases remained strong at 14% in the fourth quarter with second half 2020 rate improvement accelerating from the first half of the year. The largest rate increases were in global energy with over 30% increases, financial lines with 20% increases, Talbot with over 15% increases, and commercial property with 15% increase.

Turning to Validus Re 1/1 renewals. Overall, we saw solid risk adjusted rate improvements in U.S. Property CAT, U.S. Casualty, international CAT, marine and energy, financial lines and specialty lines. For U.S. Proportional business, material underlying rate improvement was generally applicable for our assumed portfolio. In international, rate improvements were achieved in essentially every territory. Validus achieved a material increase in net written premium at the January 1 renewal period, which generated better balance across our portfolio led by international property. New business along with final signings across our portfolio were very favorable as well.

With respect to reinsurance AIG purchased, overall, we're extremely pleased with the outcome of our January 1 renewals in a challenging market environment. This was a critical year for us to evolve our reinsurance program strategically to reflect our significantly improved underlying portfolio. In General Insurance, we maintained our philosophy of partnership with reinsurers and reducing volatility in the portfolio. We restructured our core placements in every major treaty. Keep in mind that AIG places over 35 treaties at 1/1, so I'll provide a few key highlights.

We reduced the aggregate amount of property catastrophe limit purchase as a result of a significantly reduced gross exposure in property PMLs. We reduced the catastrophe per current attachment point in North America from $500 million to $200 million for all territories except the Southeast and Gulf, which remained at $500 million. We reduced the global shared aggregate limit retention in North America from $750 million to $500 million. We purchased a CAT program for PCG, our high net worth business that protects Syndicate 2019 at AIG without taking on additional net limit. We reduced our overall catastrophe premium cost by over $150 million.

In our casualty quota share, we improved the ceding commission by 4 points and reduced our overall cession. We also introduced a new excess layer of $10 million excess of $15 million to remain consistent with our risk appetite. Those were just some of the highlights of our 1/1 renewal season. We are particularly pleased with the ongoing support we receive from the global reinsurance market, particularly our core partners. With respect to Life and Retirement, the business continued sequential improvement generating quarterly adjusted pre-tax income of $1 billion and adjusted return on segment common equity of 16.4%.

For the full year 2020, adjusted pre-tax income was $3.5 billion and adjusted return on segment common equity was 13.9%. Result for 2020 reflected higher private equity returns and higher call and tender income driven by lower interest rates and tighter credit spreads. This was partially offset by the impact of COVID-19 mortality, lower fair value option bond income and base spread compression. Life and Retirement's strong performance in the face of macroeconomic stress and high levels of volatility during 2020 is a testament to the quality of its balance sheet, diversified product offerings and disciplined risk management.

The hedge program performed as expected throughout the year and the balance sheet remained strong. Life and Retirement has a large and diverse in-force portfolio and as a result of the fortitude sale has relatively limited net exposure to legacy blocks of business, no long-term care exposure and limited risks associated with pre 2010 variable annuity living benefits. This broad portfolio across products and channels was particularly advantageous during 2020.

Given the disruption in retail sales, during the year, the team focused on attractive opportunities to deploy capital in the institutional markets business resulting in strong growth for both pension risk transfer transactions, direct and through reinsurance, and GIC issuances. Group Retirement maintained steady payroll deduction periodic deposits and improved large group plan retention results. Overall, Life and Retirement remains well positioned to meet the ever growing needs for protection, retirement savings and lifetime income solutions.

As I mentioned, we entered 2021 with significant momentum and a continued sense of urgency on our path to becoming a top performing company. I'd like to thank our colleagues around the world for their focus and determination in supporting one another while delivering significant value to our stakeholders. Thanks to their efforts we made tremendous progress in 2020, a year when the world changed for everyone and every organization. The responsibility, accountability and opportunity that commercial enterprises face today surpass anything corporate America and the global business community have ever faced.

In the months and years ahead, we will continue to adapt and evolve and introduce a stronger version of AIG as we strive to become a leading global insurance franchise. I'm privileged to be taking on the role of Chief Executive Officer of AIG and appreciate the opportunity to lead this company. I want to thank Brian for his partnership over the many years we've worked together and for asking me to join him at AIG back in 2017.

Professionally, the last few years have presented the greatest challenge in my career, but I know that this experience will also be the most rewarding. And I want to extend a special thanks to Brian on behalf of all of our colleagues for his leadership, commitment to solving complex problems and building a foundation of stability that has positioned us well for the future. I look forward to continuing our work together as Brian steps into his new role as Executive Chairman.

Now I'll turn it over to Mark.

Mark Lyons {BIO 21746221 <GO>}

Thank you, Peter and good morning, everyone. Before I go into the fourth quarter results, I want to highlight that we resegmented our financials this quarter and now have three business segments; General Insurance, Life and Retirement, and other operations. The historical recasted information and description of the changes were in the 8-K filed on February 1 and posted on our website and were principally the elimination of the legacy segment and the realignment of its book into Life and Retirement and other operations as well as some small shifts within General Insurance.

Turning to the quarter. AIG reported adjusted pre-tax income or APTI of $1.1 billion and adjusted after tax income of $827 million or $0.94 per diluted share compared to $923 million or $1.03 per share in the fourth quarter of 2019. The key drivers of this quarter were: First, a General Insurance accident year 2020 combined ratio ex CAT of 92.9%, which is a 290 basis point improvement over the fourth quarter of 2019; Second, strong Life and Retirement APTI of $1 billion driven by individual and group retirement as well as institutional markets activity and strong net investment income; Thirdly, $3.2 billion of consolidated net investment income on an APTI basis primarily reflecting higher private equity and hedge fund income.

Moving to General Insurance. Fourth quarter adjusted pre-tax income was $809 million, up $31 million year-over-year as increased net investment income from alternatives offset the impact of higher catastrophe losses, which totaled $545 million pre-tax or 9 loss ratio points this quarter compared to 6.5 loss ratio points in the prior year quarter. The CAT losses were comprised of $367 million of natural CATs primarily related to fourth quarter events Hurricane Zeta, the East Troublesome and Silverado fires and Hurricanes Delta, along with revised estimates for Hurricane Sally, which occurred late in the quarter and Hurricane Laura where Delta has a similar path.

Additionally, there were $178 million of COVID related losses primarily related to travel contingency and Validus Re. Prior year development or PYD was slightly unfavorable this quarter at $45 million compared to favorable development of $139 million in the prior year quarter. This quarter included $51 million of net unfavorable development in North America and $6 million of net favorable development internationally. The North America unfavorable PYD was driven mostly by financial lines, EPLI, E&O and mergers and acquisition insurance, primarily from accident years 2016 to 2018 and thus not covered by the ADC with favorable indications primarily in GL,Agrium some workers' compensation units and short tail lines.

As an additional lens, the $45 million of unfavorable development was also split as $5 million unfavorable in global commercial lines and $40 million unfavorable in global personal lines primarily driven by adverse development in prior year CATs as opposed to attritional losses. As usual, there is net favorable amortization from the ADC, which amounted to $52 million this quarter. I'll point out that our 2020 net premium profile is now skewed towards our international operations totaling 57% of global net premium.

Furthermore, the international book is nearly evenly balanced between commercial and personal lines and this demonstrates the truly global platform of our General Insurance business led by an international book that has had better results with less volatility than North America. We expect these proportions to stay approximately the same in 2021, but skewed a bit less towards international as North America commercial growth strengthens. A key indicator of the turnaround of our General Insurance business is the improvement in the accident year ex CAT combined ratio results for North America and international commercial lines.

As Peter has noted, North American commercial had an accident quarter combined ratio ex CAT that was 400 basis points better than last year's quarter to 93.6% and international commercial lines improved their accident year combined ratio ex CAT by 490 basis points to 89.2%. We continue to view the current accident year prudently with an appropriate view towards the margin of safety as the book has undergone a massive transformation and also anticipate continued margin expansion into 2021 resulting from the favorable global market conditions.

As Peter discussed, our personal insurance premium and underwriting results continue to be impacted by the repositioning of our high net worth business and the global pandemic. North America personal lines was impacted the most with an accident year combined ratio ex CAT of 102.6% versus 92.2% in the prior year quarter and a 55% drop in net premiums written. In 2021, our year-over-year comparisons will begin to improve. Although the first quarter will still be unfavorable since COVID was just beginning to impact travel and Syndicate 2019 was formed in the second quarter of 2020.

On the other hand, our international personal insurance business continues to perform well with a 93.9% accident year ex CAT combined ratio, which is 130 basis point improvement from 95.2% in 2019, reflecting favorable Japanese auto trends and improving business mix, offset slightly by the travel book. Expense management also contributed to the improvement with 160 basis point reduction in the General Insurance expense ratio, driven by lower acquisition ratio compared to the prior year quarter.

Lastly, before we leave General Insurance, we'd like to reiterate our outlook for a sub 90 accident year combined ratio ex CAT by the end of 2022. The 94.1% that we achieved in 2020 is a significant accomplishment, but there is more to come with the significant re-underwriting of the book over the past few years as well as the current very firm commercial lines market. We are highly confident that we will achieve more progress in 2021 and 2022 as we reestablish AIG's leadership in General Insurance.

Now turning to Life and Retirement. Adjusted pre-tax income was $1 billion for the quarter, up 20% compared to the prior year quarter. Total Life and Retirement premium and deposits increased by 4% compared to the prior year quarter driven by two large GIC issuances. In addition, pension risk transfer activity grew sequentially. Life and Retirement continued to see a rebound in retail annuity sales as distribution partners became more accustomed to the new environment with higher sequential sales for both variable and index annuities.

Fixed annuities sales were lower sequentially as Life and Retirement maintained pricing discipline in this challenging rate environment. Although still lower than the prior year, index annuity sales continued to grow sequentially contributing strong positive net flows helping offset declines in variable and fixed annuity net flows. Group retirement net flows improved from the prior year quarter due to strong group plan acquisition and retention results reflecting the investments made to modernize that platform.

On February 8, AIG announced the sale of its retail mutual fund business. This sale has a nearly immaterial impact on APTI, but will benefit our overall net flow metrics given the platform has generally experienced significant outflows over the last few years. Base investment spreads for variable and index annuities, fixed annuities and group retirement were virtually flat sequentially. As noted in previous quarters, Life and Retirement's reported base investment spread compression was impacted by substantially lower returns on cash and short-term investments through 2020. Excluding this impact based on the environment we see today, we continue to expect base spread compression across the portfolio in the range of 8 to 16 basis points annually.

Recognizing the limits of sensitivities especially in times of macro economic uncertainty and this higher market volatility, our sensitivity estimates for U.S. Equity markets and rates are as follows: we would expect a plus or minus 1% change in equity market returns to respectively increase or decrease adjusted pre-tax income by approximately $40 million to $50 million annually A plus or minus 10 basis points movement on the 10 year reinvestment rates would increase or decrease earnings by approximately $10 million to $20 million annually. As always, it is important to note that these market sensitivity ranges are not exact, nor linear since our earnings are also impacted by the timing and degree of movements as well as other factors.

Moving to other operations, which now includes portions of the legacy segment from prior General Insurance exposures had an adjusted pre-tax loss of $720 million, inclusive of $292 million of losses for consolidation and eliminations, which this quarter principally reflects realized capital gains on private equities, which are recorded as NII in the subsidiaries, but eliminated in other operations' APTI and recorded as realized capital gains in net income, not AATI.

For the quarter, corporate interest expenses were slightly higher than the prior year, reflecting the interest on the $4.1 billion of senior notes issued in May 2020 and other operations GOE was down $38 million from the comparable quarter last year. For 2021, we expect both corporate interest expense and GOE to decrease due to debt repayments and lower corporate expenses. However, we expect continued volatility in asset management and in the consolidation and elimination lines due to returns interest rates and credit spread volatility.

Shifting to investments. Net investment income on an APTI basis was $3.2 billion or $236 million lower than the fourth quarter of 2019 principally due to the June 2020 sale of Fortitude. whose investment income was included in the prior year's quarter. Adjusting the fourth quarter 2019 accordingly, this quarter's net investment income on an APTI basis was $262 million or 9% higher than the prior year and reflected the strongest quarterly returns in 2020 for hedge funds and private equity as well as having strong bond tender and call premiums. It's also worth noting that on a full year basis, net investment income on an APTI basis excluding Fortitude was $11.8 billion.

Turning to the balance sheet. At December 31, 2020, book value per common share was $76.46, up 3.5% from September 20, 2020 and adjusted book value per share was $57.01, up slightly from September 30. As Peter mentioned at year-end AIG parent had cash and short-term liquidity assets of $10.5 billion and during the quarter, we repaid our December debt maturity of $708 million bringing our debt leverage for year-end 2020 to 28.4%, which is 220 basis points lower than second quarter of 2020 when we raised $4.1 billion of senior notes to pre-finance 2020 and 2021 maturing debt. Our primary operating subsidiaries remain profitable and well-capitalized.

For General Insurance, we estimate the U.S. Pool fleet risk-based capital ratio for year-end 2020 to be approximately 455% and Life and Retirement is estimated to be approximately 430%, both above our target ranges and both providing a good absorbency buffer. The impacts from investment downgrades and credit losses to our RBC ratios were less than anticipated reflecting a high quality investment portfolio that is positioned well to navigate the uncertain environment. And With respect to the capital management in 2021 as intended, we repaid $1.5 billion of maturing senior notes on February 1, which reduces our leverage ratio by about 1.6 points on a pro forma basis approaching towards our 25% leverage target.

In addition, we re-purchased approximately 92 million of shares to offset dilution associated with AIG warrants that were exercised prior to expiration on January 19, 2021. As Peter mentioned, we intend to repurchase additional common shares in the first half of 2021 to manage dilution and in addition, we expect to execute some liability management actions in the first half of 2021 to facilitate the Life and Retirement separation.

And with that, I'll now turn it back over to Brian.

Brian Duperreault {BIO 1645891 <GO>}

Thank you Mark. Operator, we're ready for the Q&A.

Questions And Answers

Operator

(Question And Answer)

Thank you. (Operator Instructions) And we will take our first question from Elyse Greenspan with Wells Fargo. Your line is open, please go ahead.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Morning. My first question going back, Peter, to some of your introductory comments on Life and Retirement. You pointed to, however, the 19.9% transaction takes place that some portion of the proceeds would be able to use for further share repurchases. So I'm just trying to get a sense when you make that comment, what are you guys assuming for, I guess, the leverage target for L&R as a standalone entity? And then also, is the goal for RemainCo AIG still to get its leverage target within the vicinity of I think you guys have pointed to around 25%?

A - Brian Duperreault {BIO 1645891 <GO>}

Okay. So, Peter, the question is, on the repurchase and leverage at AIG I believe so. Do You want to start and maybe Mark, can jump in if he has to.

A - Peter Zaffino {BIO 15942020 <GO>}

Yes, sure. I think Elyse, what I said in my October comments and then just reinforced and provided a little bit more detail on the prepared remarks is that, we have made assumptions in terms of the standalone Life and Retirement business with acceptable debt and capital structure that is going to work with the rating agencies.

We've also had assumed how we would set up AIG, the remaining company, with the guidance that Mark's given on our de-levering. I focused that in my prepared remarks. It's our first priority. And we think that based on the base case, getting Life and Retirement set up, getting the de-levering done at AIG, we think we will have capital available for share repurchase. That was the context of the comment I made. I don't know if you want to add anything, Mark.

A - Mark Lyons {BIO 21746221 <GO>}

No, I think you covered it, Peter.

A - Peter Zaffino {BIO 15942020 <GO>}

Okay.

Q - Elyse Greenspan {BIO 17263315 <GO>}

Okay. And Then my follow up. You guys gave some pretty healthy price increases for another quarter throughout your Commercial Lines business. We're getting asked questions or I am right in terms of just the pricing cycle and the continued upward momentum from here. So as you guys think about 2021 and beyond, I mean, do you think that we can continue to see this level of price increases throughout your Commercial Lines book in both North America and internationally for the good part of 2021 and perhaps into 2022?

A - Brian Duperreault {BIO 1645891 <GO>}

Peter?

A - Peter Zaffino {BIO 15942020 <GO>}

Thanks, Elyse. Yes, this momentum will continue as we look into 2021. We expect to see rate increases to continue. We expect to see these rate increases to be above loss cost. We expect that these rate increases will be balanced across our global portfolio and across multiple lines of business. And so this is a very disciplined market, one that our capacity is highly valued. And as we deploy it in property and casualty, we're going to be very disciplined in making sure we get the right price for the exposure, make sure that we're there to solve problems for our broker, distribution partners and clients.

A - Brian Duperreault {BIO 1645891 <GO>}

I think, Mark, wants to add something, Peter.

A - Mark Lyons {BIO 21746221 <GO>}

Yes, if I could, Elyse, also as Peter kind of noted, we -- the momentum has been strong. We have really seen no evidence of deceleration of it. It's pretty broad-based across all lines and geographies. and I would just remind you that the timing was different internationally versus in North America, so it started a little bit later. So it's trajectory is going to be different by definition, and thus far no slowdowns.

A - Brian Duperreault {BIO 1645891 <GO>}

Okay. Thanks, Elyse. We'll go to the next questioner.

Operator

And next we'll hear from Tom Gallagher with Evercore. Please go ahead.

Q - Tom Gallagher {BIO 3311667 <GO>}

Thanks. First, Brian, just wanted to say best of luck to you in the new role.

A - Brian Duperreault {BIO 1645891 <GO>}

Thanks.

Q - Tom Gallagher {BIO 3311667 <GO>}

And Peter, just wanted to come back on the consideration of the private sale for the 19.9% stake in L&R. Should we think about this as just the sale of the stake or are you considering doing something more strategic, including reinsuring a portion of your in-force block or outsourcing investment management functions. Anything you could add.

A - Brian Duperreault {BIO 1645891 <GO>}

Hey, Peter.

A - Peter Zaffino {BIO 15942020 <GO>}

Well, as I mentioned in my prepared remarks, I mean, we have received a number of inbound inquiries, high-quality companies and those high-quality companies see the real value in our Life and Retirement franchise, a very diversified portfolio, minimal legacy. And so how they are approaching AIG is that they want to do something strategically on the 19.9%, because that's what we've outlined.

But we are focused on how we drive long-term value for Life and Retirement with any partner that we decide to go with. In the event we do go with that over the initial public offering and that's we're working towards that as a primary focus. So I don't want to go into the specific details, because we don't have them. But you should just think about it as, if we did enter into an agreement, it would be about positioning the business for more long-term success.

Q - Tom Gallagher {BIO 3311667 <GO>}

Got you. And then, just my follow up is, just I guess how are you thinking about the adverse development you saw on the '16 to '18 accident years? Particularly 2016 seems to be a recurring problematic year. Do you feel there's some conservatism in there? How does that inform your picks going forward? Any -- and anything we should be thinking about with regard to what you saw with the year-end review? Thanks.

A - Brian Duperreault {BIO 1645891 <GO>}

Okay, Tom. Mark, I think (inaudible).

A - Mark Lyons {BIO 21746221 <GO>}

Yes, happy to. Hey, Tom, how are you? So a few things I could just point out is, that in North America, we had -- we recognized in Financial Lines, I'd say, on the EPLI side, a little bit on the E&O side, and the mergers and acquisitions insurance, some little changes in M&A insurance, originally it was a product that was really to sellers and now sellers and buyers, that kind of changes your forecasted utilization and things like that. So there's some recognition there, which I think makes some sense.

In the past, when we've talked about this, we've always focused on like primary D&O and SCAs and so forth, and every assumption that we had on the public side is still coming to bear. No matter how we look at it, our Commercial book, our national book. the SCAs continue to drop as the underwriting continues to improve, and that's been a steady pattern. What we would say this time is really on the private not-for-profit side, mostly centered in the EPLI.

We saw some trends that we recognized. But we think we're in pretty good shape. We think we pretty much nailed it at this point. And I would say, the second part of your question on a go-forward this book has had such massive transformation that the predictive value, given the turnover of the past to the future, is almost non-existent. So we use it, we try to carve all those things out, index forward. But the impact of that on such a transformed book is negligible. So the net is, we're very comfortable with where '19 and '20 are.

A - Brian Duperreault {BIO 1645891 <GO>}

Okay. Next questioner, please.

Operator

And next we will hear from Tracy Benguigui with Barclays. Please go ahead. Your line is open.

Q - Tracy Benguigui {BIO 21808177 <GO>}

Thank you. Congratulations to both Brian and Peter. Brian, I would say, go find a nice island to live that you found one many years ago.

A - Brian Duperreault {BIO 1645891 <GO>}

Thanks, Tracy.

Q - Tracy Benguigui {BIO 21808177 <GO>}

Yes. I have some similar questions about the reserve development. Maybe you could just talk about how you feel about rate adequacy and liabilities since you've had some adverse development in Excess Casualty, and I noticed it is one of the only Commercial Lines where you've actually had net premiums written decline.

A - Peter Zaffino {BIO 15942020 <GO>}

Maybe I'll start and then -- thanks, Tracy, and then I'll turn over to Mark. Just two things to keep in mind. One is the net premium written, what I said in my prepared remarks on how we've restructured the reinsurance fee, $10 million excess of $15 million was purchased in December, so you would have seen that as an impact on net premium written for the casualty lines in the fourth quarter. So that's one.

And two is, I just want to reinforce, Mark's, point and give you an example in terms of what we're doing with the Excess Casualty book. We had talked about we were, years ago, over 90% lead in what we were doing in Excess Casualty and wanted to make sure that we were getting better balance. And so the team led by Dave McElroy, Barbara Luck have done an amazing job. We now have increased like our mid excess by over 400% in terms of policy count.

So the book is changing and getting better balance across the portfolio. And You don't really see that, but I think that's to Mark's point before when he was commenting on the vast changes, the improvement of the portfolio, So that just needs to emerge a little bit over time. But I think we have done some very strong work on the underwriting side and the balance is much better as we position ourselves for the future.

Mark, I don't know if you want to add anything in terms of just Excess Casualty specifically.

A - Mark Lyons {BIO 21746221 <GO>}

Yes, sure. Two things, One I'll follow up on your direct question, which is on the rate changes and rate adequacy. And secondly, I think on the finsub we could have done a little better job. We said Excess Casualty was really the Lexington casualty, which really has primary in it. The traditional admitted casualty book, that's either written out of American Home or like London or Bermuda has performed very, very well during the year. And so I'm just letting you know that this is not an issue whatsoever. So it's really a combination of Lexington primary and excess.

But my comments will now address all of that. So as you know, rate changes have not only been large, they've been compound over a period. The terms and conditions, which drive this line of business are tighter and tighter. And whether you have a calm or an aggressive view of loss cost trends that could affect casualty businesses, getting further away from risk is the preferred way to go, and that's the strategy that Peter and Dave have put in place moving that portfolio higher. So you're further away from risk in case anything unforeseen happens.

So we're very comfortable with that. We're very comfortable on our indications are that the rate adequacy as opposed to rate change is stronger on new business than it is on renewal business, which you'd expect to be the case in a hard cycle of acceleration like we have. And we continue to see inferior rate adequacy on the business we're not renewing. So that's what I call the implicit lift as opposed to the explicit lift. So we feel good about that.

Q - Tracy Benguigui {BIO 21808177 <GO>}

Okay, excellent. And at this point, it's been a few months since your initial announcement to separate L&R, and I know you've had a lot of discussions with various market constituents. I'm just wondering, at this stage, how firm is your 19.9% initial sale target? I get your point, it would be a full separation. But just wanted to get a sense if you had, maybe more flexibility by the rating agencies or you've figured out a way to accelerate your debt structure that could lead to a different path?

A - Brian Duperreault {BIO 1645891 <GO>}

Peter, I think you should address that one.

A - Peter Zaffino {BIO 15942020 <GO>}

Okay. Yes. Thanks, Tracy. The 19.9% remains the base case. We think it's the best way forward for the organization. We're working on all the different work streams that I outlined in my prepared remarks, working with all of our stakeholders and believe that that will be the path that maximizes value for the organization.

Q - Tracy Benguigui {BIO 21808177 <GO>}

Thank you.

A - Brian Duperreault {BIO 1645891 <GO>}

Okay. Our next question please -- questioner.

Operator

And next we will hear from Yaron Kinar with Goldman Sachs. Please go ahead.

Q - Yaron Kinar {BIO 17146197 <GO>}

Good morning, everybody, and I'll reiterate the congratulatory comments to Brian and Peter. I guess my first question is on the comment around expectation of similar growth trend in Commercial Lines. Are you saying that you expect commercial net premiums written to be in the high-single-digit range in 2021? And I guess, what I'm trying to get at is, why wouldn't we see further acceleration from 4Q levels, considering that rates remain very robust, you have less reinsurance purchase and potentially we see an economic recovery.

A - Brian Duperreault {BIO 1645891 <GO>}

Peter?

A - Peter Zaffino {BIO 15942020 <GO>}

Thanks, Yaron. It is hard to give specific guidance in terms of whether it's going to be high-single-digits or even more, I mean, we have a lot of momentum in the commercial portfolio. We talked about strong retention, strong rate. New business in 2020 was impacted by, if I look globally, particularly in international and some of the specialty classes, our new business was very strong, but it wasn't at the normal levels that we expect within 2021.

And again, we're still in the global pandemic. We'll see with the economic recovery. We're cautious but we're optimistic that new business will continue to pick up and we believe our retentions will get stronger. And so we're very optimistic that we'll have very good growth balance across commercial globally next year. I don't know, Dave, if you want to add anything in particular on the new business and your optimism of growth?

A - David McElroy {BIO 15192036 <GO>}

Yes. Thank you, Peter. In a simple way, I just -- I think we've had a couple of turns with the book. We look at this as less limit reduction. Okay? And then our new business opportunities have always continued to be on the Commercial side on a $3 billion range worldwide with the platform that we have. And then I look at our -- the renewal retention rate, okay? We can forecast rate, but we also have certain positions that we think that we can actually consistently earn those rates going forward. Okay? We are not in a commodity position in our portfolio.

And if you look at this worldwide in terms of the different franchises we have, we think that the rate we're looking at and the risk-adjusted rate and the -- and what -- how we're thinking about the portfolio, they are very defendable. So there was a lot of work done over the last couple of years. Okay? And we freely admit that in terms of addressing the exposure that might have been an outlier exposure. We feel very comfortable with where we are going into 2021 with a portfolio that we can add to not only on rate, but new business and then our renewal retention.

Okay? And key point, and it's worth saying, the limit reduction that went through in these last two years, we are through that portal. And therefore, if anything, we're adding risk and we're thinking about growth with risk -- not just risk on top of -- limits on top of accounts, but additional risk with additional clients and that's actually where we think very strongly that the brand and the formidable nature of what is AIG, we will succeed in 2021. Okay? That's very much part of the plan is that we've taken some of the outlier exposures down to the studs. And now we are very comfortable with the portfolio that we have going forward.

A - Brian Duperreault {BIO 1645891 <GO>}

I think, Mark, wanted to add something too David.

A - Mark Lyons {BIO 21746221 <GO>}

Yes, Yaron, if I could, I'm going to purposely give you an arithmetic view, and it's this Peter touched on it a bit with the XOL when he was talking about some of the reinsurance. So loss occurring contracts, you basically have ceded written, all bulleted, right, in the quarter, and then it's earned smoothly. Risk attaching quota shares, you see the recognition quarter-by-quarter.

So from a net earned basis, which is what's going to really matter, you're going to see much more uplift on a net earned basis over the course of the year. The benefit of a smaller session on the casualty quota share will overwhelm the additional XOL session. So you'll see that increase, right, but it won't be at 1Q, you're going to see that over the course of the year.

Q - Yaron Kinar {BIO 17146197 <GO>}

Okay, got it. Very, very helpful comments. Thank you. And then switching over to L&R. A lot of moving parts this quarter, pandemic mortality, alternative income, a little bit of AIG 200. Can you help us think about kind of the core earnings power of that business, whether as an earnings power or ROE that you talked about in the past, how should we think about that going forward?

A - Brian Duperreault {BIO 1645891 <GO>}

Peter, do you want to take that?

A - Peter Zaffino {BIO 15942020 <GO>}

Yes, I'll give it to Kevin (inaudible).

A - Kevin Hogan {BIO 4650423 <GO>}

Yes, thanks, Yaron. So, I think Mark's comments highlighted the sensitivities to equity markets and interest rate levels. This year, we did benefit from some strong market support that, frankly, is laid out in the noteworthy items in the earnings deck. And we had a strong year based on where the markets were with both alts and the call and tender income.

We continue to target low- to mid-double-digit returns for the medium-term and our current pricing conditions suggest we are able to continue that. And so I think it's really the alternatives are the big anomaly this year, we turn those to normalized levels. The call and tender income strength could continue based on where interest rates are, and that's, to a certain extent, the wild card.

Q - Yaron Kinar {BIO 17146197 <GO>}

Thank you.

A - Brian Duperreault {BIO 1645891 <GO>}

Okay. Next questioner, please.

Operator

And next we will hear from Josh Shanker with Bank of America. Please go ahead.

Q - Josh Shanker {BIO 21718992 <GO>}

Yes, thank you very much for taking my call. I want to just go back to that guidance, and we'll call it guidance about a 90% accident year ex CAT combined ratio in General Insurance in 2022. Is that a year forecast or was that an exit forecast? And the other part, I'll give both my questions upfront. If you told me we'd have 15% to 20% rate increases in 2020 and maybe in 2021, I would think you could improve the combined ratio by more than 300, 400 basis points in harmony with AIG 200. Do you have any thoughts on those two areas?

A - Brian Duperreault {BIO 1645891 <GO>}

So let's have Mark talk about it, the 90%, and then we'll take it from there. Go ahead.

A - Mark Lyons {BIO 21746221 <GO>}

So, I think, Peter and I go back and forth on this. On the 90%, which we are, Josh, reiterating, Peter will get into some of the expense ratio aspects of it. With regard to loss ratio, that was the second part of it, well, we would expect improving margins as well as we go through '21 and '22. We're viewing that as exit, though, Josh. So that's much closer and equivalent to 4Q. But the -- but nevertheless, you have to watch the compound growth or change, because as the book continues to improve and it's improved fabulously, the degree of improvement narrows and narrows and narrows that you can do. So the big, huge changes have already occurred. But we're comfortable on our cadence and approach to get there.

Peter?

A - Peter Zaffino {BIO 15942020 <GO>}

Yes, can I just add to that? Thanks, Josh. I mean, a couple of things to keep in mind. One is, AIG 200 contributes a meaningful portion of the improvement in expense ratio. Now, while I said $400 million was the exit run rate of 2020, that hasn't even fully earned in yet. So we expect the full $1 billion by 2022, so you can just do the math that that will contribute to the expense ratio and overall combined ratio.

The other is, we think there's two components to growth. One is, Dave mentioned it that we think that the portfolio is in a very good place for top line growth, and we would expect to see that to continue in 2021 and 2022. In addition, contributing to that growth will be we need less reinsurance, I think the terms and conditions that we were able to improve at 1/1 speak volumes in terms of the trajectory and what we would expect for reinsurance going forward, that will contribute.

I think when we do and the team has proven, it does very good work on operational excellence that when we separate Life and Retirement, AIG RemainCo, we will find ways to improve the expense ratio as we work through the actual separation, and we have a very disciplined expense behavior in the company. And then just the rate above loss cost and as we continue to reposition the portfolio, we think there will be improvement in the loss ratio as we look to the future. So when you add all of those components together, we are very confident that we will be below the 90% as we exit 2022.

A - Brian Duperreault {BIO 1645891 <GO>}

And Josh, don't forget this is a -- Josh, don't forget this is both commercial and personal. It's the entire book of business going below 90% And the Personal Lines. is not getting the kind of rate increases in commercial. So you just got to put that weighted average in too. Do you have -- you asked your questions, didn't you, Josh.

Q - Josh Shanker {BIO 21718992 <GO>}

Those were two. Good luck in your new roles and congratulations to everyone.

A - Brian Duperreault {BIO 1645891 <GO>}

I appreciate that, Josh. Thank you very much. I think we have maybe time for one more question.

Operator

All right. And we will hear from Erik Bass with Autonomous Research. Please go ahead. Your line is now open.

Q - Erik Bass {BIO 19920101 <GO>}

Hi, thank you. I Just wanted to follow up on Tom's question about the potential sale, of the 19.9% stake in L&R. Can you just discuss how you're thinking about the benefits of that approach versus an IPO and some of the key considerations on which makes more sense for delivering long-term value?

A - Brian Duperreault {BIO 1645891 <GO>}

Peter?

A - Peter Zaffino {BIO 15942020 <GO>}

Yes. And Mark, you can weigh in. I mean, certainly, the path with the IPO is very clear with the 19.9% IPO sale. When we look at -- I think the heart of your question on the private is that it has to be a better alternative for us. We have to be more strategic, more financially advantageous. And making certain that when we look at the 19.9%, we don't look at that in isolation, we look at the 80.1% and how we position the Life and Retirement business for the future. So those are the things, among other factors, that we will consider in terms of, do we go through the IPO or would we do a private sale as we work through the coming months.

Q - Erik Bass {BIO 19920101 <GO>}

Got it. Thank you (inaudible).

A - Brian Duperreault {BIO 1645891 <GO>}

Yes, -- do you have another follow up, there? Erik?

Q - Erik Bass {BIO 19920101 <GO>}

Yes, please. Just one other on Life and Retirement. I was just hoping you could provide some additional detail on the mortality results this quarter. Any sensitivity to general population, COVID deaths or maybe another metric to help us think about the potential impacts in Q1.

A - Brian Duperreault {BIO 1645891 <GO>}

Kevin, do you want to do that?

A - Kevin Hogan {BIO 4650423 <GO>}

Yes, absolutely. Thanks, Erik. So look, the reality is it's hard to isolate COVID deaths. So the way we approach it in looking at our portfolio is to focus on the total portfolio, actually to expected versus pricing. And in this context, we saw mortality for the year continue to be acceptable relative to our pricing in terms of short-run variances driven by COVID. Either way, we look at this as an earnings and not a capital event, and we haven't seen any data that suggest a change to our long-term assumptions.

That being said, based on our best understanding of what are the COVID-related deaths, we estimate that up to 40% of the reported claims -- COVID reported claims could be an acceleration of claims we would otherwise expect in the next five years. And again, based on our best understanding of the COVID deaths, we estimate our exposure to the population, of approximately $65 million to $75 million per 100,000 population -- deaths, which is a slightly better estimate than what we would have assumed a couple of quarters ago.

Q - Erik Bass {BIO 19920101 <GO>}

Great. Thank you.

A - Brian Duperreault {BIO 1645891 <GO>}

Okay. So, thank you all for all your questions. Before I end the call, I want to thank everyone who's been part of the multi-year journey that began when I joined AIG in 2017 to fix the fundamental needed - fundamentals needed for AIG to, once again, be a leading insurance franchise.

What has been accomplished over the last few years would not have been possible without the extraordinary efforts of AIG's exceptional talent at all levels of the organization and I'm thankful for everyone's dedication and commitment to this great organization. I'm also grateful to the clients and distribution, reinsurance partners, shareholders, regulators and many other stakeholders who have actively supported me since I returned to AIG. I look forward to being a part of the next chapter of AIG under Peter's leadership. Be well, stay safe and healthy.

Operator

And Ladies and gentlemen, this concludes today's call. We do thank you for your participation. You may now disconnect.