S&P Capital IQ

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American International Group, Inc. NYSE:AIG

FQ4 2013 Earnings Call Transcripts

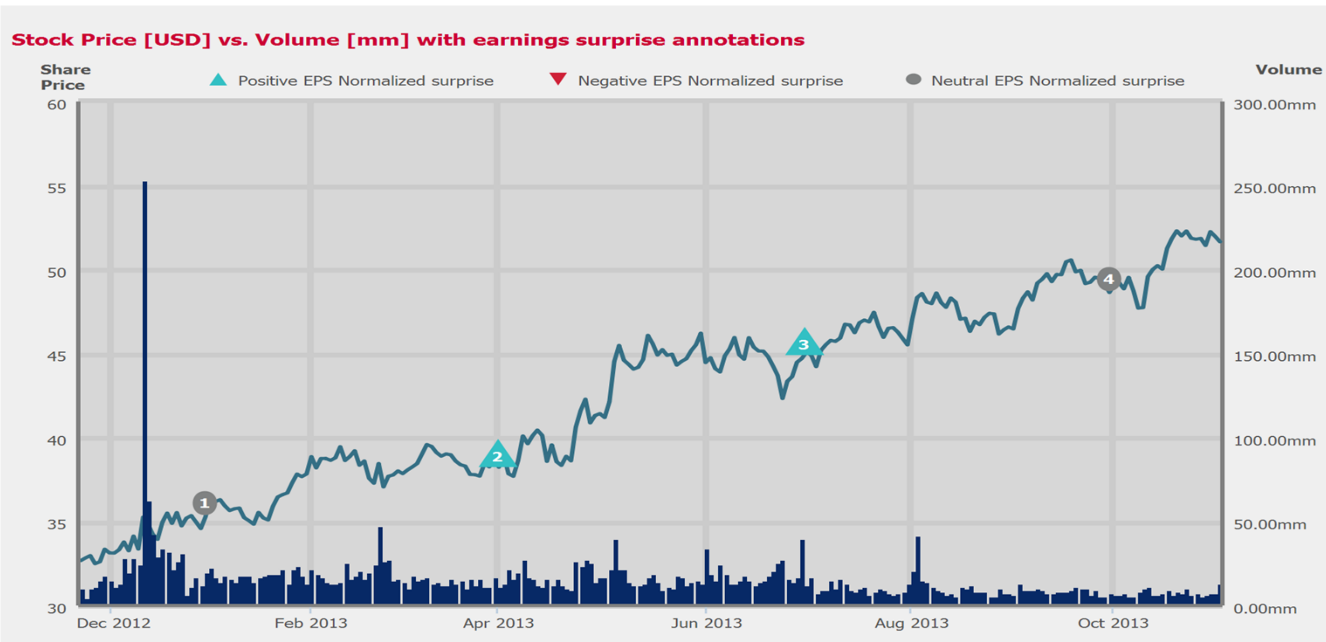
Friday, February 14, 2014 1:00 PM GMT

S&P Capital IQ Estimates

	-FQ4 2013-			-FQ1 2014-	-FY 2013-	
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL
EPS Normalized	0.97	1.15	▲18.56	1.05	4.41	4.56
Revenue (mm)	8557.14	8621.00	▲0.75	8630.25	34479.38	33953.00

Currency: USD

Consensus as of Feb-14-2014 11:28 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2012	(0.07)	0.20	NM
FQ1 2013	0.88	1.34	▲52.27 %
FQ2 2013	0.86	1.12	▲30.23 %
FQ3 2013	0.96	0.96	0.00 %

Call Participants

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Legacy Chief Executive Officer

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Former Chief Financial Officer and Executive Vice President

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John Doyle

Kevin T. Hogan
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Presentation

Operator

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

Elizabeth A. Werner
Head of Investor Relations and Vice President

Thank you, and good morning. Before we get started, I'd like to remind you that today's presentation may contain forward-looking statements, which are based on management's current expectations and are subject to the uncertainty and changes in circumstances. Any forward-looking statements that are not guarantees of future performance or events, actual performance and events may differ possibly materially from such forward-looking statements. Factors that could cause this include the factors described in AIG's third and second quarter Form 10-Q and our 2012 Form 10-K under Management Discussion & Analysis of financial condition and results of operations and under Risk Factors, as well as in the same sections within AIG's 2013 Form 10-K when it is filed 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. Today's presentation may contain non-GAAP financial measures. The reconciliation of such measures to the most comparable GAAP figures is included in our financial supplement, which is available on our website, www.aig.com.

At this time, I'd like to turn over our earnings calls our CEO, Bob Benmosche. Bob?

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Yes. Thanks Liz and good morning to everybody. And turn to Page 3, let me start off with the capital management, which is very important. As you saw, we announced a dividend increase and we've added to our share repurchase another $1 billion, so this will leave us with about $1.4 billion available for share repurchase at this time. And this reflects the strength not of the fourth quarter, but the entire year and actually the last several years, as we look at cleaning up what stressed our company to see what would happen under adverse situations and making sure we have the capital and liquidity to meet a stress event and continue maintaining our strong ratings and improve those ratings, in fact, over time. So this year is in line with that. In addition, now we continue our debt management as you've seen. And most important, in the quarter, we were able to sell ILFC and close out the doubt about that transaction, and so we expect that to close in the second quarter of this year. That will, as you know, be the last major non-core asset that AIG is selling.

Peter will talk to you about our Property Casualty business. The underlying results continue to be very strong in my opinion. This has been a dramatic turnaround within the company in how it was designed in the past and where we are today, and we'll take you through the details. But strong top line, accident year loss ratios continue to improve. But remember, it's not a linear business, it zigzags. I know that's technical term for some of you but, I mean, so it goes up and down and it doesn't go straight. And so you'll see that the trends, I feel, are very strong.

Our Mortgage Guaranty business continues to do well, a dramatic turnaround from where we were 5 years ago, but that's part of the strong risk selection model that was put in place as well as recovery in the market. And there are -- Jay will talk about our Life and Retirement business. We've had very strong sales. That business is really doing extremely well and continues to do well across all of the products. And so, I'll let Jay bring you up to date on the details of this. So let me turn it over to David, who will give you the highlights of the financials, and then we'll take you through the other key businesses. David?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Thank you, Bob, and good morning, everyone. As Bob mentioned, we saw strong performance in our insurance operations, with operating earnings for the quarter in excess of $2.5 billion. For the full year our insurance businesses collectively generated an excess of $10 billion pretax operating earnings.

Looking ahead to 2014, we'd expect continued progress in expanding our risk-adjusted returns through growth and capital efficiency. The sale of ILFC, as Bob mentioned, to AerCap is on track for closing in the second quarter. The transaction was valued at $5.4 billion upon announcement using a $24.93 share price for AerCap. And any adjustment in that value on closing will reflect the change in the AerCap share price and will be recorded as a nonoperating gain or loss on sale. Upon closing, AIG will receive net cash of about $2.4 billion, which will be held at the parent company available for general corporate purposes. Our retained 46% interest in AerCap will be held at the holding company and will be accounted for under the equity method of accounting, with the equity earnings from AerCap included in our other segment operating results. The lockup expiration on AerCap shares begins to phase out 9 months following the closing date. We will be prudent in maximizing our value as you have seen in our past dispositions of invested assets. As part of the ongoing focus on capital management, as Bob mentioned, our Board approved the 25% increase in our quarterly dividend to $0.125 a share and authorized the repurchase of additional shares with an aggregate purchase price of up to $1 billion. This gives us $1.4 billion of capacity.

Turning to our financials on Slide 4. Net income for the quarter was $2 billion and included several largely offsetting nonoperating items detailed on Page 6 of our financial supplement. One such item, footnoted on Page 6 of the financial supp, relates to an impairment charge on our investment in life settlements totaling about $832 million before tax. This charge was prompted by the continued underperformance relative to our mortality assumptions. Accordingly, we revised our future mortality assumptions and discount rates for valuation purposes. Overall, we expect this $3.6 billion portfolio to have a mid single-digits return. Our operating ROE for the quarter was 7.3%, in line with our full year of about 7.5%. Since our earnings are tax-effected for purposes here and we are not paying taxes to the U.S. government given our NOLs, our ROE, excluding the DTA, is about 190 points higher than that. Book value per share, excluding AOCI, at $64.28, grew 11% from year-end 2012.

Our operating results begin on Slide 5, and you can see solid growth in our insurance operating income from a year ago, and Peter and Jay will speak to their respective businesses. The direct investment booking and Global Capital Markets earnings collectively were strong with a little over $600 million for the quarter and reflect market pricing due to their mark-to-market accounting treatment that can create some volatility from period-to-period. We expect these earnings to moderate over time as the portfolio winds down and the investments approach their expected recovery values. In addition, we continue to proactively and opportunistically reduce the direct investment book's footprint.

During the fourth quarter of 2013, we repurchased about $466 million worth of DIB related debt. And during the first quarter of 2014, we reduced the direct investment book debt by a little over $2 billion through both a make-whole call that we announced in December and open market purchase transactions, all of these using cash within the direct investment book specifically allocated for this purpose. At year-end, we had roughly $7.9 billion of net asset value in the Direct Investment book in Global Capital Markets.

Corporate expenses totaled about $213 million for the quarter, down from a year ago, due to lower data center restructuring costs and other related expenses on restructuring costs. We expect corporate expenses would run at about $225 million to $250 million quarterly run rate in 2014. Other expenses included a severance charge of about $265 million related primarily to the Property Casualty business and relates to our migration towards shared service centers, which Peter will speak to you in his remarks. Also reported in other were $170 million of gains related to AIG real estate sales transactions. Our reported operating effective tax rate for the quarter was about 32%. Our current outlook for 2014 is an annual operating effective tax rate of somewhere between 31% and 32%.

Slide 6 presents a summary of our DTA, which totals a little over $21 billion at year-end, up from just shy of $17 billion a year ago. While our tax attribute-related DTA, i.e. the net operating loss carryforwards and the foreign tax credits, have declined by about $1.4 billion through the utilization of the NOLs, our net other DTLs and DTAs increased by almost $6 billion. The increase relates to the sale of securities with gains, transactions that resulted in tax basis step-up and a reduction in the unrealized appreciation of our AFS securities. In the fourth quarter, we recognized another $540 million of income related to the release of the valuation allowance from the capital loss carryforwards. In aggregate, we have utilized roughly 86% of the capital loss carryforwards. For the ROE calculation that normalizes for the tax attribute DTA, we subtract about $17 billion from stockholders' equity.

Turning to Slide 7. You can see the impact of our capital management activity in 2013. During the quarter, we issued $1 billion of 10-year notes at a little over 4% interest and we repurchased some debt at the parent company and did -- totaling a little over $1 billion that had an average coupon of about 7.5%. Including the div [ph] of when you take into account all the things we've done in 2013 with respect to our liability management and maturities, we've reduced our leverage by over $7 billion and reduced our annualized interest expense by roughly $350 million.

On the equity side, during the quarter, we distributed about $147 million in dividends to our shareholders and deployed just over $400 million towards the repurchase of 8.3 million shares. While the ILFC transaction impacted how active we were in the market during the quarter, we remain focused on continued execution of our repurchase authorizations. We will continue to be opportunistic in the future, going forward towards our debt capital management as well.

As you can see on Slide 8, our insurance operations remained the source of financial liquidity, as we sent $4.3 billion in dividends and distributions to the parent in the quarter, including $90 million of dividends from Mortgage Guaranty, its first dividend since 2010. For the full year, dividends and distributions totaled $8.9 billion, well above our expectation of the $4 billion to $5 billion we've talked about in the past. I would point out that the full year dividends from Life and Retirement included about $800 million related to litigation settlement proceeds received by Life and Retirement that were remitted up to the parent company. Additionally, $1.5 billion in the fourth quarter dividends from Property Casualty resulted largely from some restructuring activity that we've been working on for quite some time.

Our expectation for 2014 is to have dividends and distributions from the operating companies of somewhere between $5 billion and $6 billion. In addition to these dividends, we expect tax sharing payments from the insurance companies to parent of approximately $1 billion in 2014 and roughly $2 billion in 2015 as our local insurance company statutory NOL DTAs are utilized. These dividends, combined with our capital management activities I've mentioned earlier, result in a parent cash, short-term investments and unencumbered securities of just over $13 billion as of the end of the quarter. Included in final liquidity is $5.9 billion related to the Direct Investment book and Global Capital Markets, which is allocated for its future debt maturities and contingent liquidity stress needs. As we've indicated in the past, nearly 80% of the Direct Investment book's liability will mature between now and the end of 2018.

So with that, I'd like to turn the call over to Peter for comments on Property Casualty.

Peter D. Hancock
Former Chief Executive Officer, President and Director

Thank you, David, and good morning everybody. Today, I'd like to discuss the highlights of the quarter and the year, as well as our outlook for 2014. Let me begin by saying the year marked significant accomplishments that we believe are indicative of our future direction. Our balanced approach to growth, risk and profitability, drove our business mix shift, our underwriting actions and our capital management achievements. We're pleased with our progress and look forward to continuing on our path towards increasing returns.

Turning to Slide 9. In the fourth quarter, net premiums written grew 6% from a year ago on a normalized basis, with growth coming from each of our major business lines. For the full year, our net premiums written were over $34 billion or up 4% on a normalized basis. In the quarter, commercial lines delivered net premiums written growth of 7%, with improvement in each product line. This is the first quarter in 2013 with a comparable top line comparison to casualty as there's no longer an impact from the global excess casualty quarter [ph] share as it ended in 2012. Specialty delivered the strongest top line improvement on a normalized basis from a year ago, with noteworthy growth in the Europe and Asia Pacific regions.

Property also developed strong growth, both in the fourth quarter and full year. Our global property business is benefiting from significant international growth as we leverage our recently expanded in-house engineering capabilities and execute on our global approach to capital allocation.

Looking ahead to 2014, we expect continued growth across our businesses, including casualty, where the re-underwriting of our book is largely complete. We remain focused on retaining our highest-quality business and see positive rate increase in the United States.

Pricing continued to be positive and largely exceeded loss cost trends. Global commercial rates increased 2.6% in the quarter, and the U.S. market continued to lead rates improvements with a 5% increase in the quarter. The U.S. casualty led with a 6.5% increase followed by U.S. financial lines, which were up 4.2%, and U.S. property at 3.7%. Continued favorable underwriting trends were offset by increased severe losses in the fourth quarter. Improved underwriting results, over the course of the year, were a result of our pricing actions, enhanced risk selection, technical underwriting and investment in claim handling.

Severe losses in the third and fourth quarter reflected higher frequency and severity and exposure growth following the low level of severe losses in the first half. Our full year severe losses were somewhat in excess of our expectations, so we accept a modest amount of volatility for the increased returns. We expect to continue to see a decline in the accident year loss ratio as a result of our underwriting improvements.

Over the last 3 years, we continued to manage down our growth exposure to catastrophes and refined our global approach to reinsurance, which has led to a consolidation of our reinsurance purchases and a reduction in the number of counterparties and contracts. While we don't disclose all of our reinsurance programs, we'd like to provide a few highlights that illustrate the role reinsurance plays in our business strategy. In our corporate cat program, which we renewed in the fourth quarter, the attachment point is $3 billion and provides significant protection up to $5.5 billion for individual losses in U.S. and Canada, and up to $4 billion for accumulation of losses worldwide. In 2013, we also continued our strategy of accessing the capital markets. During the year, as part of our cat program, we entered into 2 separate multiyear cat bond transactions providing combined reinsurance protection of $525 million. Our Consumer business, which is presented on Slide 11, underwent a transition in 2013 as we increased rates in Japan A&H and personal lines and engaged in product portfolio management in the United States. We continued selective growth in key markets. We experienced a higher level of travel and accident losses in the quarter, which we don't expect to be a sustained issue given the short-term nature of this business. Consumer remains on track for modest improvements in both growth and profitability in 2014. Additionally, the investments we're making in Japan will help provide a more competitive operating platform and a lower-cost structure in the long term. Under Kevin Hogan's new leadership, we look forward to executing on a strategy of targeted growth in markets where we can achieve meaningful scale and applying some of the principles that have worked well in commercial. We look forward to discussing more details of our consumer strategy over the coming months.

Two items of note in the quarter are the severance charge that was recorded in AIG's other operations and our reserve actions. The expense savings associated with the $265 million severance charge largely pertain to Property Casualty and will emerge beginning in 2014 and become more significant in 2015. However, for the full year 2014, investments in the business will result in a relatively flat expense ratio compared to 2013. We began the final phase of the Fuji integration work in the second half of 2013, which will continue into the second half of 2015. The cost of this initiative is estimated to be approximately $250 million, when combined with our purchase price, still represents a meaningful discount to the fair value of the underlying assets and liabilities acquired. We believe the full integration of our Japanese business, which currently has an 8% market share, will position us well in the second largest nonlife insurance market in the world.

Slide 13 presents prior year development for the fourth quarter and full year. We continue to review our reserves quarterly and take timely action to address changes in development trends. In the fourth quarter, we added $225 million to our pre-2004 runoff environmental reserves based on our updated review.

Our analysis of pollution products looked into individual cases, which indicated large increases in the value of certain previously reported cases due to new developments such as the discovery of additional contamination in certain sites, legislative changes, court rulings, expansion of plaintiff damages and increased cost of remediation technologies. In addition, there was a 1-point adverse impact to our current accident year loss ratio related to these multiyear runoff lines of business.

In the fourth quarter, we obtained approval from our Pennsylvania regulator to better align payout pattern and mortality assumptions for our excess workers' compensation reserves using our own experience and to utilize a more economic discount rate assumption for our primary workers' compensation reserves. These actions reflect our work with regulators over the course of the year and the significant analysis we completed to better model our runoff excess worker's compensation book.

Fourth quarter, the total net discount benefit was $325 million, which included a benefit of $647 million on excess workers' compensation reserves and a charge of $322 million on primary workers' compensation reserves. We also expect to record an additional workers' compensation loss reserve discount benefit of approximately $100 million in the first quarter of 2014 associated with the merger of internal pooling arrangements effective January 1, 2014.

In the fourth quarter, we made $2.6 billion of cash dividend payments to the parent company and $4.1 billion for the full year. During 2013, we worked with our regulators to simplify our legal entity structure. We consolidated our U.S. and Bermuda insurance exposures into one U.S. pool to increase our diversification benefits. These restructuring transactions resulted in $1.5 billion, in the fourth quarter, of dividend payments to the parent company and $1.8 billion for the full year.

Turning to Slide 14. Mortgage Guaranty's operating performance continues to improve, with operating income for the quarter of $48 million. Mortgage Guaranty continues to benefit from its proprietary risk selection model and an improving housing market, with 59% of earned premiums generated by high-quality business written after 2008.

Mortgage Guaranty closed the year with a record level of domestic, first-lien new insurance written of $49.4 billion. The delinquency ratio fell to 5.9% at the end of the quarter, representing the lowest level since the fourth quarter of 2007. UGC continues to be strongly capitalized and holds an investment portfolio that's highly liquid, with 81% of the investments rated A or better. As the leading U.S. mortgage insurer, UGC currently insures 800,000 mortgages across United States.

Now I'd like to return the call over to Jay to discuss Life and Retirement results.

Jay Steven Wintrob
Former EVP of Life & Retirement, CEO of AIG Life & Retirement and President of AIG Life & Retirement

Thanks a lot, Peter, and good morning, everyone. 2013 was a record year for AIG Life and Retirement. And we had our best year in top line results, generating nearly $29 billion in premiums and deposits and in delivering on the bottom line with $5.1 billion of pretax operating income.

Turning to Slide 15. Operating income in the fourth quarter was $1.4 billion, up 29% from a year ago due primarily to fee income growth, active spread management throughout the year and higher net investment income. Returns on alternative investments were approximately $200 million above expectations and 52% higher than the prior year period, driving much of the increase in our net investment income. These results and our solid capital position enabled AIG Life and Retirement to distribute over $1.3 billion to the holding company this quarter and deliver full year dividends and loan repayments to AIG of more than $4.4 billion. Giving effect to these dividends, we still grew shareholders' equity x AOCI by 11% to nearly $35 billion.

The success of our retail investment product strategy was a key driver of this significant increase in our sales volumes. Our all products, all channels distribution platform continues to generate outstanding results. Retail premiums and deposits grew 88% from the year-ago quarter, reflecting growth across all of our investment products. Individual variable annuity sales were $2.3 billion for the quarter and $8.2 billion for the full year. We remain comfortable with this run rate of sales, particularly given the actions we've taken over the years to derisk this product.

Fixed annuity sales increased over 90% in 2013, and sales in the fourth quarter were nearly 4x what they were in the year-ago period. Consumer demand for fixed annuities has improved from the year-ago quarter, though sales have moderated somewhat from the third quarter due to interest rates declining from peak levels reached last quarter and our related disciplined pricing actions. We also saw increased premiums and deposits in our institutional businesses, with growth in both group retirement and institutional markets on a year-over-year basis.

As of year-end, our assets under management were $318 billion up 10% from year-end 2012. Over the course of the year, we saw improved net flows across all of our retail investment products, higher separate account balances and an increase in institutional assets under management. Net flows in 2013 were nearly $4.6 billion, driven by the substantial sales improvement in our retail product that I just discussed.

We continue to grow our stable value wrap business in the quarter and saw a year-over-year increase of $14 billion in stable value wrap assets under management. These sources of AUM growth more than offset the impact of rising rates on our invested asset portfolio. And for the first time in 4 quarters, we experienced sequential growth in our general account asset balance. So overall, we're pleased with the growth in assets under management we're seeing across our portfolio of businesses.

Slide 16 highlights the strong operating income results of our businesses. Retail operating income increased 37% versus the year-ago quarter as a result of enhanced spreads, growth in fee income on separate accounts and higher net investment income. Institutional operating income increased 19% versus the year-ago period and similarly benefited from crediting rate actions, higher fee income on separate accounts and the higher net investment income. The increases in net investment income were largely attributable to greater partnership returns, an appreciation in hybrid securities, non-agency RMBS and other invested assets accounted for using the fair value method. We also experienced better-than-expected mortality in our Life Insurance business, which contributed to the favorable year-over-year performance in the quarter.

Our Retirement Income Solutions business continued to grow profitably, with operating income up over 70% from the year-ago quarter. We're seeing strong demand for our products, which we believe are differentiated in the market based on the income options we offer and our award-winning customer service. Over the past almost 4 years, we've redesigned our products to reduce risk to AIG, and I think the strategy is paying off. In our Retirement Income Solutions business, of our $24 billion of variable annuities with guaranteed minimum withdrawal benefits, 71% include benefits with strong derisking features such as the VIX indexing of our rider fees, volatility control funds and requirement -- required minimum allocations to the fixed account. Given its relative size, we view our variable annuity business as an opportunity to generate attractive returns, especially as competitors reduce their appetite for additional exposure while consumer demand for income solutions remains robust.

Slide 17 shows our investment portfolio, composition returns and yields. Net investment income benefited from the strong alternative investment returns in the quarter, as I mentioned earlier. Overall, the total portfolio base yield declined 4 basis points from the year-ago period as we continue to invest premiums, deposits and cash flow from the portfolio at new money yields below the overall base portfolio yield. Over the course of 2013, portfolio cash flow included proceeds from asset sales which generated significant tax gains in our fixed investment portfolio designed to utilize our capital loss carryforwards. Since inception of our gains realization program to utilize those capital loss carryforwards in 2012, our overall portfolio base yield has been negatively impacted by 13 basis points on an annualized basis as a result of the action. It's worth noting, however, that our base yield increased 3 basis points sequentially, mainly attributable to increased income recorded on residential mortgage-backed securities related to appreciation in the home price index, as well as an increase in estimated future cash flows when compared to the prior quarter.

Moving to Slide 18. We continue to actively manage crediting rates, which is reflected in the decline in cost of funds for both our fixed annuities and group retirement businesses on both a year-over-year and sequential basis. Net spreads expanded for both fixed annuities and group retirement from the year-ago period and the prior quarter. And at year-end, 73% of our fixed annuity and universal account values were at minimum guaranteed crediting rates.

So in closing, 2013 was a strong year for AIG Life and Retirement, with record sales and profits. This year, we remain focused on executing against our strategic initiatives, which includes growing our distribution organization and increasing the productivity of our wholesalers, affiliated agents and financial advisers, leveraging our strong relationship with distribution partners to increase penetration of our broad retail product portfolio within firms, maintaining a leadership position and offering competitive and profitable retirement income solutions and continuing to look for opportunities to grow our institutional businesses where we can achieve the most attractive risk-adjusted returns.

And with that, I'll turn it back to Liz to open up the Q&A.

Elizabeth A. Werner
Head of Investor Relations and Vice President
Thank you, Jay, and operator, can we open up the lines for questions this morning?

Question and Answer

Operator

[Operator Instructions] We'll go first to Brian Meredith with UBS.

Brian Robert Meredith
UBS Investment Bank, Research Division

A couple of quick questions here first. Peter, I'm just curious, with 2.5% or 2.3% kind of rate increases globally, do you think we can continue to see the magnitude of improvement in your loss ratios here going forward?

Peter D. Hancock
Former Chief Executive Officer, President and Director

Yes. We have a fair degree of confidence that the 3-year trend of accident year loss ratio improvement will continue. As you know, a lot of the improvement is baked into this year through renewals, so we have a high degree of confidence on that.

Brian Robert Meredith
UBS Investment Bank, Research Division

And is it coming from maybe just mix instead of absolute rate, and that's why you're still getting the big improvement?

Peter D. Hancock
Former Chief Executive Officer, President and Director

It's a combination of all the initiatives we've made to make sure that we have re-underwritten the books that were causing problems. So the U.S. casualty book has been substantially re-underwritten, getting rate where we needed rate, investment in much, much tighter claims to reduce claims leakage. So it's a whole combination of factors which had been underway for 2 years and that are now starting to come through as we actually start to believe in the trends that have been established.

Unknown Executive

Brian, it's Tom [indiscernible]. We expect to see continued good growth in our commercial business in Latin America, in Asia, Japan, as well as the Middle East and Africa. I mean that business continues to perform quite well from a loss ratio point of view. We also rolled out some new products around the world that will contribute to an improvement of the business. So we're expecting underwriting results on a normalized basis to continue to improve next year.

Brian Robert Meredith
UBS Investment Bank, Research Division

Great. And then just quickly on capital management for David. As I look at your common equity this year, it was up a little over $2.5 billion, and then if you x AOCI, it was at close to $8 billion. So I'm just kind of curious why aren't we seeing more capital management, more share buyback or is that something we may be able to expect on the horizon at kind of a faster pace than we've seen?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Yes, sure. Thanks, Brian. As we said before, listen, we've remained and do remain committed to the $25 billion to $30 billion of overall capital management. To date, we've done about $20 billion -- well, I don't know, $16 billion or so of that, in common equity buybacks. We've done some debt. We're increasing the dividend. I think the overall approach is to be prudent, to be deliberate and orderly about the pace at which we go. We want to be, in the long-term scheme of things, do this in an orderly way. And so, we're balancing the perspectives of many different stakeholders at the table. So the fact that we're increasing our dividend, increasing or getting an additional share repurchase authorization, I think you should take as a sign of our confidence, our board's confidence in the underlying financial underpinnings of the company. And as I said, we remain committed to the $25 billion to $30 billion of capital management between 2011 and 2015. So we're going at a pace we think is appropriate. Bob, if you want to add any commentary to that, I'd welcome that at this time.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Well, David said it exactly right. Keep in mind that considering where we've been, and we have the core direction, we want to make sure we do this in a very thoughtful, routine and prudent way.

Operator

We'll go next to Mark Finkelstein with Evercore.

A. Mark Finkelstein
Evercore ISI, Research Division

Peter, can you elaborate on the A&H losses and Private Client Group losses and consumer, please?

Peter D. Hancock
Former Chief Executive Officer, President and Director

I think I'll ask Kevin Hogan to handle that one. So, Kevin, why don't you discuss that?

Kevin T. Hogan
Executive Vice President and Chief Executive Officer of Global Consumer Insurance

Yes, sure. Mark, these are primarily related to some wholesale travel business in the fourth quarter, we had some severe losses and travel delays. And then on the Private Client Group, also there were a handful of losses associated with the severe weather. We've taken appropriate underwriting actions across the portfolio in the U.S. throughout 2013, and we anticipate this to be a short-term impact on the results.

A. Mark Finkelstein
Evercore ISI, Research Division

Okay, perfect. And then I guess, also staying there, just thinking about the expense ratio, you've kind of had the severance charges, but the outlook for the expense ratio in '14 is relatively flat, I think if I heard those comments correctly. And I know in the past you talked about kind of expense ratio staying high through '14 and into '15. What is the current thinking on when we'll start to see some of the infrastructure and the IT spend moderate and start to see the actual expense ratio coming down?

Peter D. Hancock
Former Chief Executive Officer, President and Director

Well, the big expenditure in 2014 relates to Japan, as I mentioned. We're spending about $250 million in fully integrating the Fuji acquisition into our AIU operation. And that's a spend that we started in July of last year and will last through July 2015, so it really peaks of this year as we make some very major investments in infrastructure and branch rationalization in Japan. So that's the big item. And then offsetting that is a continuation of the process we started in 2011 of integrating the Property Casualty business into one seamless AIG as opposed to a number of separate profit centers with duplicative infrastructure. And so this year, we will be really streamlining, removing excess layers of management in areas where they're duplicative so that we can be as responsive to customers and grow and redeploy people and capital where the opportunities are greatest. But I think that the expense ratio has been affected by a combination of these investments, as well as the reduced denominator of sort of the shrinkage in the U.S. casualty business, so there's negative operating leverage carrying which, as I mentioned, has really started regaining top line growth again as we have re-underwritten the casualty books. So I think that we feel good about the outlook on the expense front, but I don't think there's going to be a dramatic change until 2015.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

And I'll just add to that, I know we're all focused on the expense ratio, but we need to focus on the accident year loss ratio and the growth of this business and another thing that as Peter has talked about, over the last year or 2, is that we've invested heavily in our engineering center, which will improve our ability to assess this, investing huge amounts of money in clients. So we have a better data around our underwriting intuition and do a better job there, that's adding to the expense ratio. When you look at monies we're spending to put in the fraud unit, the subrogation unit and the claims area, all of these are adding expense. And the beneficiary of that is an improved and reliable and consistent accident year loss ratio. So you really have to think about the strategic work that he's talked about over the last 2 years in how you're seeing a benefit across the entire combined ratio. And then also it takes a while to earn it to the benefits of what we're targeting, just mentioned earlier, David, that the actuaries have to see the trend. And it takes a long time for trends to emerge. And I think you'll see this continue to progress over the next several years.

A. Mark Finkelstein
Evercore ISI, Research Division

Okay. All very fair points. Just one very, very quick one if I may, which is the increase in the statutory dividends that you're assuming for '14 over '13, is that all from improvement in earnings, or is there more capital efficiency improvements at P&C or any other items that are helping to improve that number?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Mark, it's David. It's a combination of continued strength in earnings, so we're continuing to generate the deployable capital. But there is some amount that I haven't -- I haven't quantified it publicly, but there's some amount that is -- we're moving some higher-than-needed capital in some of the operating companies up to the holding company. So we're continuing to evaluate the amount of capital that we're holding in the operating companies. We want to make sure that we've got plenty of capital for our ratings, put plenty of capital to maintain our competitive positioning and to fund our growth. But the businesses are continuing to generate very substantial capital, and we will migrate some of the capital ratios down a bit over time as we have -- as we said we would do.

Operator

We'll go next to Jay Cohen with Bank of America Merrill Lynch.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Two questions. One is, you had mentioned the accident year loss ratio being negatively impacted by some multiple year contracts, I didn't quite get that, I think it was at 1 point. And then secondly, with your stock trading below book value, the capital that you'll generate from the ILFC sale, should we assume that share repurchase will be a primary use of that capital?

Peter D. Hancock
Former Chief Executive Officer, President and Director

So, Jay, I'll start on the first one then I'm going to probably enlist James Bracken to help you by -- flog the GAAP accounting treatment. But basically, these are contracts, these are policies written pre-2004. They were multiyear in nature where, because they're multiyear and we're receiving premiums still, means that as claims get made, they appear in the current accident year. But these are discontinued business from pre-2004 that appeared in the current accident year as an anomaly.

James Bracken

All right. Just one clarification. So they're being earned in, we've received all of the premium and think of them as multiyear claims made colorful. So they cover -- they've run for a number of years and we're still got a bit to earn out and we still see some revenue recorded in the NPE line of the other segment. And they attach -- some loss activity attaches to them, but it relates to run-off business.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

And was that 1 point on the guarantees?

Peter D. Hancock
Former Chief Executive Officer, President and Director

Yes. It's 1 point in the entire...

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

1 point for the total company in the quarter.

Peter D. Hancock
Former Chief Executive Officer, President and Director

Yes. 1 point of accident year loss ratio for the entire company.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Right. And as far as capital management is concerned, what we've said along is that our first priority is our credit ratings because that speaks to our ability to live up to the promises we make. So it's really about our coverage ratio, debt management and so on. We once said that we want to have some dividends to flow back to our shareholders, like the primary bill after those 2 have been achieved with share buybacks. And so when ILFC closes, we'll make a determination at that time, and we'll continue to evaluate our capital management program around our stress testing of the company which is, right now, we'll do one starting in November and we'll do another one around May. And then we take a look at where the companies, where we think the issues are in the marketplace and then we present to the board what we think is appropriate capital actions based upon what we see at that time. So actually to get to the point, as David pointed out, the $25 billion to $30 billion. We can see the dividends coming up to the holding company, we can see the DTA beginning to get monetized. Our priority is to continue to maintain a strong company while, at the same time, giving what makes sense to the shareholders as quickly as we can.

Operator

We'll go next to Paul Newsome with Sandler O'Neill.

Jon Paul Newsome
Sandler O'Neill + Partners, L.P., Research Division

I want to talk -- sorry, a little bit more about the expense in Property Casualty. I think maybe I'd like to ask in a big picture perspective, if you go back to AIG before its problems, this was a company that had a relatively low expense ratio and a pretty average loss ratio. And that was kind of how they made their money by having a lower expense ratio than their peers. Today, we're looking at a loss ratio which is much improved and actually kind of looks a lot like the peers broadly speaking, but has an expense ratio that's higher. Is the goal here to have a business that is heavy on loss control and heavy on back expenses and a lower loss ratio over time or, ultimately, are we talking about a company that wants to make its competitive advantage once again in expenses?

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

I think you should think of us having a very competitive combined ratio, both loss ratio and expense ratio. I think that's what Peter is working towards. But you need to look at the loss ratio and look at it on an accident year basis historically. If I go back to our releases and information we have provided you, I don't know that the accident year loss ratio for both prior years looked at from this year, will be what you saw. So I think there's a difference. And if you back it in, which is what you need to do, prior year development -- and if you look at the prior year development over the last several years and looking at what we've had to do, you can see that the accident years were pretty high. So what you're going to see is continued improvement in the loss ratio, continued improvement in underwriting and systems around underwriting, continued investment in technology, so we have a very strong, bulletproof processing capability here at AIG that's state-of-the-art. And then you'll see our expense ratios start to come down and still see improvements in loss ratio. But we need to continue to invest in a lot of tools to make sure that, that loss ratio 5 years from now is what we said was an the last [indiscernible] or slightly better. And so we're building this company not only for the 2014 but for 2018, 2020. We really have to have a strong foundation for the future, and that's what we're building at.

Jon Paul Newsome
Sandler O'Neill + Partners, L.P., Research Division

So to try and interpret your comments, it sounds to me like your competitive advantage, if you achieve your goals, will ultimately be a very competitive loss -- a better loss ratio than most and an expense ratio that's maybe in line with your peers. Is that kind of the idea, big picture, long term?

Peter D. Hancock
Former Chief Executive Officer, President and Director

I don't view either of these ratios as a source of competitive advantage. They are outcomes of what we do for our customers. So our competitive advantage comes by the expertise that we have, in the risks that we take ourselves or help our customers to manage if they choose to retain them. And so, the investments that we are making to become true experts in the risks that we've chosen to specialize in around the world and to use the relationships that we've developed over decades with customers both large, medium and small in the consumer and commercial space. And so as a result of that, we are investing in what it takes to be experts. And that will lead to a higher expense ratio than what was the case historically. But those historical expense ratios will also somewhat flattened by reinsurance strategies with large ceding commissions, which we don't do on the same scale anymore. The other thing is, as Bob said, you got to look at those restated accident year loss ratios in '98 to 2003, which were way above industry averages, and we never want to return to those sorts of underwriting impairments. So we're really sharpening up how we manage our risks, so that we have a competitive combined ratio, as Bob says, and a sustainable way through the cycle. And so, the other thing we're really focused on is a better tradeoff between profitability and growth in this, so we don't feel we're forced to grow top line in a soft market. So we want to get our fixed costs down. We're focused on the mix between fixed costs and variable cost, so that we have the ability to scale back volumes in a soft market, so we manage the cycle better in the future.

Operator

We'll go next to Josh Stirling with Sanford Bernstein.

Josh Stirling
Sanford C. Bernstein & Co., LLC., Research Division

A question, I think, for Peter and John perhaps, or one of the two. When I look at the commercial business, and I do some adjustments for severe losses and I think normalizing for the higher expenses in the quarter from incentives and stuff, I get to something like an underlying accident year x cat combined in commercial maybe as low as a 92, which looks like a very nice improvement from last year and a lot of progress in total. And I'm kind of curious just where are we going to get to on this number? And is -- when you look at peers, you can sometimes see -- you can often see sort of high 80s x cat accident year combined ratio underlying numbers. And I think that's what you would need to get to your low-90s, all-in calendar year target. Is that a realistic end goal for this story?

John Doyle

Josh, it's John. Yes, we expect to continue to see in 2014 accident year loss ratio improvement again normalized. Peter talked to bit about the severe losses on the quarter, they were slightly elevated relative to our expectations for the full year, a bit better than expected in the first half of the year and higher than expected. So that contributed to slightly higher 2013 accident year results than what we expect. We talked about expenses, we do expect this year to see an improvement in the expense ratio over time, as Peter pointed out. We did mention shared service centers right, we have some redundant work going on as we build out our shared service capabilities in different parts of the world, in Europe and Asia, in Colombia as well. So yes, we do expect to continue to see an improvement in the year in a combined ratio results for commercial.

Josh Stirling
Sanford C. Bernstein & Co., LLC., Research Division

Great. If I can ask just sort of a different question for Kevin. Welcome back to the company, I think we're all happy to have you here. I want to talk about the consumer business. So over the -- and I know there's a lot of things going on, we talked about Japan. But in aggregate, sort of results have been flat, in the past couple of quarters, on the loss ratio side, I think been a bit of a disappointment. I'm wondering if you could just sort of -- you referenced some things you're doing sort of more tactically re-underwriting, some repricing. I'm wondering if you could give us some color on sort of some specifics and the magnitude of actions you're taking to drive margins in over the next year or 2?

Kevin T. Hogan
Executive Vice President and Chief Executive Officer of Global Consumer Insurance

Okay. Thanks, Josh. Well, the reality is, is that AIG has done a terrific job on the commercial underwriting area in the last couple of years and now a little bit ahead of some of the disciplines that we're adopting in the consumer area, and the focus is on the large portfolio. So in Japan, we have reviewed and taken rate some of the large audit portfolios as well as the core A&H businesses. And in the United States as well, we're taking a hard look at the Private Client Group business state by state, and have filed a number of rate adjustments in both the homeowners and the automobile businesses there. We're also in the process of introducing similar tools to what's been used in the commercial in terms of the global raters and focusing on rate adequacies in the various portfolios, including those which are the strategic business expansion areas where we're introducing the appropriate technical skills from the get-go in our greenfield operations. So growth is an important aspect of the consumer business as we try to generate a customer insight driven business, but we are doing it with the appropriate underwriting disciplines. And that is a very important part of our renewed focus.

Josh Stirling
Sanford C. Bernstein & Co., LLC., Research Division

That's great. If I could just sneak one quick in. A couple of times now, we've heard from management suggesting the actuaries are lagging in recognizing the underwriting -- results improvement from underwriting and claims. I'm wondering, Charlie, if you could give us some color on how you're doing the analysis. And are you using the more faster IMPROVER's report method? Are you kind of looking at lagging methods like the Bornhuetter-Ferguson and expected loss ratio? And how much more would you characterize margin improvement have yet to actually work through at the income statement?

Charles S. Shamieh
Legacy Chief Executive Officer

Josh, I think Peter's comments earlier really relate to a lot of the investments especially in the claims area, and we've talked about workers' compensation. And so one of the key difficulties the actuaries have is that settlements patterns are changing, pace and curves are changing. And we're getting much better case reserve information. And what Peter's talking about is it's very difficult sometimes to distinguish between that case reserve strengthening and what's really going on in the business. But we're certainly using a whole wide range of techniques that look forward and try to give appropriate credit for all the investments that the claims team is making in those initiatives. And so -- and I think with more track record on the pace and in the curves, the confidence in that increases. And really, that's what Peter is talking about.

The statistical credibility that you give to the 1 or 2 years of emergence will be better. And the only other statistic I'd give you is that we've reached today an inflection point where, over last 2 years, if you consider the re-underwriting of the casualty book, we now have just over 50% of our reserves that are coming from the better underwriting that Peter and John talked about earlier. And so as that increases, I think you'll also see a natural improvement in future periods as the quality of the underwriting comes through and becomes a higher percentage of overall reserves.

Operator

We'll go next to Jimmy Bhullar with JPMorgan.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

First, a question for David, maybe if you could just talk about where you are on your interest coverage ratio now and what your aspiration is. And then second for Peter, on the loss ratio, accident year loss ratio, maybe if you could discuss the reasons for the deterioration of the loss ratio this quarter. You mentioned 1 point because of the 2004 and, 3 or 4 business. But even with that, it would have been worse than previously. And then, I'm not sure if you quantified the benefit of the cost savings plan and the severance plan that you just announced, but if you could maybe just talk about how much you've spent -- expect to save on that once it starts to fully reflect in your results this year or next year?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Okay, Jimmy, thanks and appreciate the question. There are 3 things I want to sort of leave you with, with respect to our debt capital management that's ties into our focus on coverage ratios. One is we did achieve the goals we had set out for 2013, vis-à-vis the coverage ratio and interest expense run rate savings. So again, we did it opportunistically and, again, struck a balance of being able to allocate capital to share buyback, dividends as well as share repurchase. So again, point one, 2013 goals met. Secondly, with respect to the direct investment book in the liability management that Brian Schreiber and the team are overseeing, we funded that with cash that was allocated in the DIB very specifically for that purpose. So those proceeds were -- or the funds we used for that had no effect essentially on cash or capital we have available for share buyback or other forms of equity capital management. And again, we'll continue to look to optimize the value of the direct investment book over time. And as I said, 80% of it's gone at the end of 2018. If we can accelerate that without sacrificing value, we certainly will. And thirdly then, the point being we continue to generate deployable capital, again, 5 to 6 plus the tax sharing payments. I would look for us to continue to very opportunistically focus on debt capital management as it presents itself, I think I did expect we would continue to make progress on our coverage ratio primarily through earnings improvements. But that also from time to time, we will look at the capital management debt buybacks, et cetera, as they present themselves. So as Bob said, we're focused on our ratings and we'll strike an appropriate balance. We haven't set any specific targets for 2014. I think, again, we're in a pretty solid place based on what we did in 2013.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

But it doesn't seem like you're done buying and reducing your debt maybe not as much as before. But do you still expect to reduce that a little bit?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

I think we'll -- yes, we'll continue to be opportunistic in how we think about it, so I wouldn't give you any specific targets of what we will do or won't do. But again, we'll be opportunistic. We are focused on continued improvement in the coverage ratio again, and I think we can do that primarily through earnings, but we'll look at other ways to approach that. I'll give it over to Peter.

Peter D. Hancock

Former Chief Executive Officer, President and Director

Jimmy, thanks for the question. I think that I'll just give you some quick answer on the timing of expense savings that are related to the severance which is that we really have not disclosed the precise savings we expect in the calendar year 2014 because we want to be extremely thoughtful about the way we execute what is effectively around an organizational streamlining to better serve our customers where we're not approaching this with a finite sort of deadline during the course of the year. We want to make it absolutely sure that we execute this in a way that makes us better serve our customers. And so, we'll be quite thoughtful about the execution. So we have a broad range of ideas that is, I think, sufficient to say that we think that we will maintain an expense ratio that's fairly stable this year, but we're not disclosing precise numbers in our quarterly schedule of savings. On the accident year loss ratio, as Bob said, this is a business that zigs and zags, and understand which of those as zigs and zags are noise and which ones are signal. You need to dig a little bit under the surface to normalize severe storms and so on quarter-to-quarter. And I think that's probably best done offline in a follow-up discussion with James.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

Sure. And maybe if I can just ask one more quick question. On the AerCap stock, obviously it's gone up a lot in value. Have you thought about hedging your position? And are there any limitations on you doing that if you wanted to?

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Jimmy, we're not going to talk about ILFC. Once it closes, we would be glad to talk about what the options are. But let's get to closing and then we'll know what we can talk about.

Elizabeth A. Werner
Head of Investor Relations and Vice President

Operator, I think we can take just one more question and then we'll have to call it a day.

Operator

Okay. Our last question today will come from Tom Gallagher with Crédit Suisse.

Thomas George Gallagher
Crédit Suisse AG, Research Division

Just a quick one for David. The $5 billion to $6 billion of annual dividends that you're expecting out of the insurance companies now, I guess the run rate had been $4 billion to $5 billion. And should we -- so we should expect that for the next 2 years from a visibility standpoint, is that the goal? And then you would add on the DTA utilization on top of that. And so, if those numbers are correct, the high end of that would be $8 billion by 2015, is that the right math?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Yes. I think I'll limit my remarks to 2014. And I -- so that's what -- that's where the commentary that I want to share with you and the investment community because that's the line of sight that we want to provide. As I've said before, again, as we continue to generate deployable capital, we want to maintain, I think, first and foremost, strong capital positions in our operating companies. And as they continue to generate capital, we'll give you as much insight to that as possible. Again, I think the DTA payments as I've said is roughly $1 billion in 2014 and $2 billion in '15 and it'll go from there. And so, there'll be a very substantial cash flow to the holding company. So again, the $4 billion to $5 billion is what we said back in 2011 when we reintroduced the company, and that's a very sound foundation. But again, we've seen opportunities to redeploy some capital that's above and beyond the levels we need to hold at those operating companies. And again, that's what we want to do, get it up to the holding company, so that it's most fungible at that level.

Thomas George Gallagher
Crédit Suisse AG, Research Division

Got it. And then the -- was just a little confused about the $4 billion or so of dividends that were taken up in 4Q from the insurance companies. Can you just reconcile what -- where the $4 billion went? Because if I look at HoldCo cash and investments, they were up by a small fraction of that. So where did the $4 billion go?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Yes. Sure, it's a very fair question. So we had -- one of the things we did was we improved the diversification of the capital in a couple of our operating companies through -- via some internal restructurings we did with the light settlement portfolio. So we took -- we accelerated some cash out of the OpCos, we used that cash to improve the diversification of some of the capital. Punch line is it had no effect on the level of capital or cash we had available at the holding company for capital management or other general corporate purposes. So that's really where it went. So about a little -- almost $2 billion of it went for that, so it was some internal improvements we made.

Thomas George Gallagher
Crédit Suisse AG, Research Division

Okay. And then one last one for me for Kevin. Just on the comments on increasing rates in Japan A&H, in auto, can you just comment on what's happening there because the -- I just want to know, is this to keep pace with loss cost trends because you obviously had some elevation of -- you had cited travel and accident? I don't know if that's specifically related to it, or should we expect the rate you're getting to actually improve margin?

Kevin T. Hogan
Executive Vice President and Chief Executive Officer of Global Consumer Insurance

Well, thanks, Tom. The actions that we're taking in Japan are really related to an overall portfolio review, Fuji Fire and Marine, a relatively recent acquisition. We've taken an extensive review, and this is really a primary area where we have improved our selection parameters and rates, and we have seen the improvements in the overall profile of the results as a result. In terms of the A&H business, it's more of a reflection of responding to some changing trends in the underlying results in the marketplace, and [indiscernible] we will see it as an improved underwriting result going forward.

Elizabeth A. Werner
Head of Investor Relations and Vice President

Okay. Thank you, everyone, for joining us this morning. And we'll certainly be happy to take all the other follow-up questions. And we're all here, so please feel free to reach out. Thank you.

Operator
Again, ladies and gentlemen, thank you for your participation. This will conclude today's conference.