S&P Capital IQ

CONTENTS

American International Group, Inc. NYSE:AIG

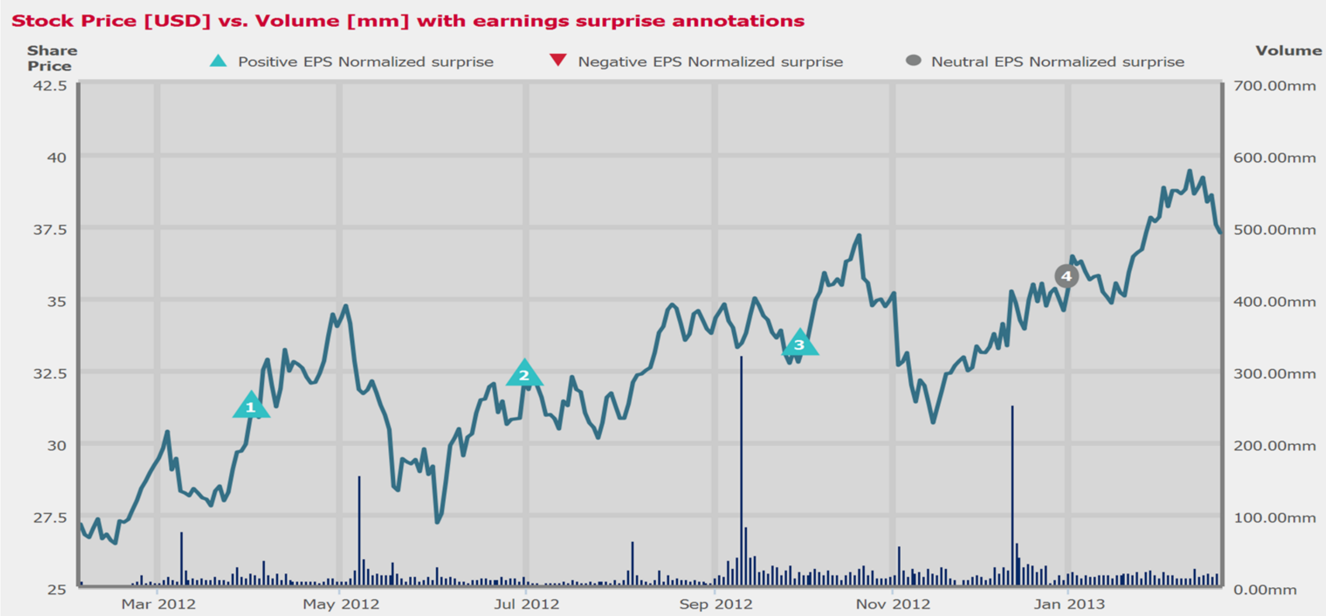
FQ1 2013 Earnings Call Transcripts

Friday, May 03, 2013 12:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2013-			-FQ2 2013-	-FY 2013-	-FY 2014-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.88	1.34	▲52.27	0.85	3.61	4.10
Revenue (mm)	8639.83	8558.00	▼(0.95 %)	8691.14	35331.86	36054.44

Currency: USD
Consensus as of May-03-2013 12:17 PM GMT



- EPS NORMALIZED -	CONSENSUS	ACTUAL	SURPRISE
FQ1 2012	1.39	1.65	▲18.70 %
FQ2 2012	0.60	1.06	▲76.67 %
FQ3 2012	0.89	1.00	▲12.36 %
FQ4 2012	(0.07)	0.20	NM

Call Participants

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Presentation

Operator

Good day, and welcome to the American International Group's First Quarter Financial Results Conference Call. Today's conference is being recorded. And at this time, I would 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

Good morning, and thank you for joining us, everyone. Welcome to AIG's discussion of our first quarter 2013 results. Speaking today will be: Bob Benmosche, our President and CEO; David Herzog, our Chief Financial Officer; Peter Hancock, CEO of AIG Property Casualty; and Jay Wintrob, CEO of AIG Life and Retirement. Other members of senior management are also in the room and available for the question-and-answer period.

Before we get started this morning, I'd like to remind you that today's presentation may contain certain forward-looking statements, which are based on management's current expectations and are subject to uncertainty and changes in circumstances. Any forward-looking statements 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 our 2013 first quarter 10-Q and our 2012 Form 10-K under Management's Discussion and Analysis and under Risk Factors. AIG is not under any obligation to expressly disclaim or 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. Reconciliation of such measures to the most comparable GAAP figures is included in our financial supplement, which is available on AIG's website at aig.com.

Now I'd like to turn the call over to Bob.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Thanks, Liz, and good morning, everybody. And as I've said since mid-2011, the focus of our company and all the people of AIG has been fix the foundation and get the fundamentals right. And while we see noise as we dealt with some of our noncore assets and so on, mark-to-markets of ML II, III and so on, AIA, we've been focusing on the core. And I think what you see is, in the first quarter, is another strong quarter of the fundamentals. This is a quarter we had some positives. Last quarter, we had Sandy, which was a negative. But if you look at the core, and we're going to talk about that this morning, we continue fundamentally to do very well here. Now you look at our liquidity at the end of the quarter, we're at $15 billion. That includes dividends from Life and Retirement and also liability management, which included some of the cash from the prior quarter.

Peter's going to talk to you about our Property Casualty business, that we've seen good improvement in the underwriting, good returns from the investment side as well. But what's most important, if you look at the trend over this period of time from mid-2011, you can see that there's a gradual improvement of the current accident year loss ratio, which is now down to 63.2, again strong improvement. And if you but the growth of the top line, we continue to grow that this quarter. It's growing nicely at about 4% if you take out some of the accounting charges and the end [ph] issue that we're dealing with in terms of conversion there. So strong performance in Property Casualty.

In Mortgage Guaranty business, we have said we've seen that business turn about 2 years ago. We're working through the legacy book. Again a strong quarter for that business and about half of their premiums are now coming from our new underwriting model, which is performing much better than we had in the past.

And our Life and Retirement business, again great distribution numbers in a very tough climate. We're continuing to hold the line on our ability to get the returns we need for that business. And so a success for us as well. And Jay will take you through that.

So I don't want to belabor at this point. I look forward to taking your questions at the end of our comments. What I'd like to do now is turn it over to David, who will highlight some of the financials for you this quarter. David?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Thank you, Bob, and good morning, everyone. As Bob mentioned, our core operations delivered strong operating results this quarter, up 28% over a year ago. And we executed on $2.1 billion in liability management actions during the quarter. We remain committed to our aspirational goals, including $25 billion to $30 billion in capital management and a 10% ROE by 2015.

Turning to Slide 4. First quarter operating earnings per share was $1.34. As you might recall, first quarter of 2012 had over $3 billion in pretax gains related to noncore holdings in AIA and ML III. So the quarter-over-quarter EPS comparison isn't straightforward. Operating ROE, which excludes AOCI from equity, was 9.2% for the quarter on a basis consistent with our long-term aspirational goals, which excluded the deferred tax asset from equity. For purposes of calculating ROE, ROE would have been roughly 200 basis points higher this quarter. Book value per share, excluding AOCI, was $59.39, up 12% from a year ago and 3% from year end.

Operating results begin on Slide 5. Property Casualty delivered an underwriting profit in the quarter driven by continued improvement in the accident year loss ratio. Both our Property Casualty and Life and Retirement businesses benefited from stronger alternative investment returns than we expected. Property Casualty had modest cat losses of around $40 million, less than we expected in the quarter. We realigned our Life and Retirement segment presentation this quarter to provide product segments consistent with our new management structure, which Jay will discuss in more detail in his remarks.

The Direct Investment book and Global Capital Markets benefited from positive marks in the quarter, driven largely by tighter credit spreads. Operating income from the wind-down legacy multisector CDS book, which is reported in Global Capital Markets, improved by roughly $150 million from market appreciation of the underlying coverage securities, which then reduces the liability we carry on the related CDS. The Direct Investment book also benefited from asset appreciation, consistent with our objective to capture the pull to intrinsic over time. These market movements will vary from period-to-period and could be negative in a reporting period.

Interest expense increased modestly from prior year and reflected only a partial quarter of interest savings from our liability management actions that we completed in March. Corporate expenses, including the impact of costs incurred during the quarter for continued infrastructure buildout, were in line with our near-term expected run rate of about $225 million per quarter. There is roughly $35 million or so per quarter of corporate expenses related to our data center consolidation, which begins to wind down going into 2014.

The effective operating tax rate came in at almost 30%. Looking ahead for the rest of the year, we continue to expect an operating tax rate to be roughly in this range. As you may recall, we will not be paying any U.S. income taxes for some time, given our NOLs. We also had a couple of largely offsetting tax adjustments that are not reported as part of operating income. We increased our reserve for uncertain tax positions under FIN 48 by approximately $600 million, related to some legacy matters as a result of current period developments. We also determined that recently identified tax planning strategies met the prudent and feasible criteria and we released, through income, a little over $750 million of our deferred tax asset valuation allowance related to our capital loss carryforwards.

Our capital position remains solid. And on Slide 6, you can see our current debt levels reflect over $2 billion in parent company debt that we called and repurchased in cash tender offers this quarter. In March, we called our $1.1 billion, 7.7% hybrids at par, and we purchased $1 billion in debt in cash tender offers, with an average coupon of around 7.8%. Annualized interest savings on this retired debt is about $165 million. We also have $750 million in callable hybrids with a coupon of 6.45%. Exercising that call would further reduce annual interest expense by almost $50 million. At this time, we do not have any plans in place for further 2013 liability management, outside exercising the hybrid call that is available to us. If we do exercise that call, then between our maturities, the debt we have already retired proactively, we could pare our annual interest expense run rate by roughly $290 million.

Our year-end RBC ratios are also presented on Slide 6 and were 443% for Property Casualty and 532% for Life and Retirement. These are higher than the preliminary estimates that we reported last quarter. Our insurance subsidiaries remain well capitalized, well above their CMA thresholds, and are positioned to deliver sustained dividends and distributions to the holding company. We received distributions from Life and Retirement of over $1.3 billion during the quarter, as shown on Slide 7. Property Casualty is on track to deliver its full year targeted dividend payments later this year.

We continue to expect $4 billion to $5 billion in total in annual dividends and distributions from our insurance companies. Parent company available liquidity is over $15 billion at the end of the quarter, reflecting these distributions and the liability management actions that I mentioned earlier. The parent liquidity balance includes $5.5 billion related to the Direct Investment book and Global Capital Markets, which is currently allocated towards future maturities of liabilities and contingent liquidity stress needs. Nearly 60% of the DIB's debt matures over the next 5 years.

During the quarter, we initiated an investment program at the holding company, whereby we invested $2.3 billion of available cash into high-quality fixed maturity securities, with a duration of just over 3 years and a yield rate of just over 1%. We expect this portfolio to grow to around $3 billion this year. Additionally, the ILFC divestiture continues through the regulatory approval process as expected. Upon closing, the net proceeds that we receive on that transaction will be unencumbered at the holding company.

And at this time, I'd like to turn the call over to Peter for greater detail on the Property Casualty results. Peter?

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

Thank you, David. Good morning, everyone. During the quarter, AIG Property Casualty made good progress towards achieving our goals. We improved our underwriting results and experienced strong investment performance, while expenses remained largely stable.

Turning to Slide 8. Operating income was nearly $1.6 billion, which included moderate catastrophe losses of $41 million, favorable net prior year reserve development of $52 million and better-than-expected net investment income. Continued enhanced risk selection, technical pricing, shifts in our business mix and advances in claims practices contributed to that profitability. Our accident year loss ratio, as adjusted, of 63.2% is slightly better than trend, which has been improving at an average 3 points annually. We expect to continue to see a decline in the accident year loss ratio as a result of our continued underwriting improvements.

This quarter, we began recognizing premiums on excess of loss reinsurance at contract inception rather than ratably over the contract term, which will have no affect on full year net premiums written or net premiums earned, but does impact first quarter comparisons. Changes in foreign exchange, driven by the weakening of the yen, and a first quarter catastrophe bond issuance also reduced reported net premiums. Excluding these effects, top line growth was 4%. We continue to expect modest net premium growth in 2013, as our underwriting actions take hold and we write profitable new business. General operating expenses were up slightly on a gross basis and included moderate severance and other personnel charges.

Turning to Slide 9. Commercial's net premium written were up 4%, excluding the effect of the immediate recognition of ceded premiums on excess of loss reinsurance and the catastrophe bond issuance that I mentioned earlier. In addition, last quarter, we entered into a new reinsurance program in U.S. excess casualty that reduced commercial's first quarter premium by about 1%, but will improve overall profitability.

Maximizing risk-adjusted profitability through optimization of business mix and underwriting excellence remains the focus of AIG Property Casualty. The results of these initiatives are most evident in Commercial's accident year loss ratio, as adjusted, which improved approximately 5 points compared to the prior year. An increase in new business and positive rate changes contributed significantly to growth in Property, which improved 20%, excluding the items mentioned above, and in financial lines. In the U.S., we saw pricing continue to climb, particularly in property and workers' compensation, where rates increased over 8%. Partially offsetting this was continued pressure in certain lines within specialty, and in Europe's Commercial business. Overall, retentions remained strong in those lines of business we wish to grow.

Turning to Slide 10. Consumer net premiums written increased over 4%, excluding foreign exchange and the other items mentioned earlier. Accidents and health experience growth outside the U.S., particularly in individual A&H in Asia Pacific. Personal lines benefited from auto's market share gains in EMEA and expansion in high-value nonauto lines. Consumer's accident year loss ratio was up slightly from the prior year, as 2012 included a $45 million benefit related to changes in actuarial assumptions in accident and health. Acquisition ratios reflected our investment in the profitable direct marketing channel, which grew approximately 8% and accounted for 16% of total consumer premiums.

Slide 11 illustrates our investment portfolio mix. First quarter net investment income increased 11%, reflecting strong alternative investment returns, increased mark-to-market gains on structured securities and redeployment of excess cash held at year end. Alternative investment income was almost $120 million above our expected return.

The first quarter marked another step on our path to increasing the intrinsic value of AIG Property Casualty. Our shift to high-value business, combined with underwriting and claims practice improvements, exemplified how our focus on balancing growth, profitability and risk is helping to produce better margins. We maintain our commitment to capital efficiency and optimizing our risk profile. In Japan, for example, we recently integrated the majority of our operations under one holding company, which will enable greater capital flexibility and create operating efficiencies. We look forward to contributing our planned full year dividends to the holding company during the remainder of the year. In closing, I'm satisfied with our positive momentum. I'm confident that this quarter is only the beginning of a successful year.

Turning to Slide 12. I'd like to comment on Mortgage Guaranty's performance and our outlook for this core insurance holding. The first quarter was another quarter of improving profitability and growth in new business. Delinquency counts continued to fall and Mortgage Guaranty continues to see a growing portion of earned premiums, now almost 50%, from high-quality business written since 2009 and declining losses from legacy runoff exposure. We expect UGC is very well positioned to take advantage of an expanding private mortgage insurance market. Profitability is expected to grow over the course of the year and we'll continue to capitalize on our unique underwriting approach and strong capital position.

Now I'd like to turn it over to Jay.

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

Thanks, Peter, and good morning, everyone. Starting on Slide 13. As you can see, this was another strong quarter for AIG's Life and Retirement business with a 6% increase in operating income from a year ago to $1.4 billion. The year-ago quarter included a $246 million gain in the final Maiden Lane II distribution.

First quarter operating income growth was driven by the robust equity markets, which contributed to strong investment returns on our portfolios of alternative investments and mark-to-market securities. Combined with another positive quarter for our investment in PICC common stock, these portfolios contributed approximately $320 million in investment income, above our expected returns. Strong equity markets also contributed to our growth in assets under management, driving increased fee income. The quarter also benefited from lower mortality costs and our continued active management of crediting rates, which dampened the impact of the low interest rate environment. In addition to strong earnings, as David mentioned, AIG Life and Retirement provided $1.3 billion of liquidity to the holding company through dividends and note repayments from our operating life companies. And we're on target to deliver on our expected dividends to the holding company for 2013.

Total premiums and deposits this quarter were $5.6 billion, roughly flat with the year-ago quarter and 7% higher than the fourth quarter of 2012. Net outflows, the sum of sales less all surrenders, death claims and other benefit payments related to our retail investment products and group retirement businesses, were $244 million, a marked improvement from the previous quarter, each of the business contributing to this favorable trend. Variable annuities were the leading driver of inflows, while fixed annuities showed the greatest incremental improvement in net outflows due to improvement in sales and a decline in surrenders.

We continue to see strong variable annuity sales growth and remain comfortable with our product offering, risk management and the overall environment with respect to the VA business. We also remain disciplined in managing our fixed annuity sales and in-force block. Our cost efficient, flexible annuity platform, based here in Amarillo, Texas, and deep relationships with banks in particular, have allowed us to remain the #1 provider of fixed annuities through the bank channel. The low interest rate environment, however, obviously continues to negatively impact product demand across the industry.

We are now reporting under our new segment presentation, and our new segments and the underlying lines of businesses, which we illustrate on Slide 14, after [ph] recent organizational changes and how we manage the business and allocate resources. Our results are now broadly reported in 2 segments, Retail and Institutional, and we also provide profitability and additional supplemental information for certain key businesses.

The Retail segment includes our individual life and A&H business, fixed annuities, retirement income solutions and retail mutual funds and broker-dealer services. Our retirement income solutions business line now includes both variable and indexed annuities, reflecting the fact that customers [ph] of these products rather than focusing only on asset accumulation, are increasingly interested in guaranteed income. And today, the vast majority of each of these products now include a guaranteed lifetime withdrawal benefit rider option.

The Institutional segment includes our group retirement business, which was previously reported as VALIC, institutional markets and AIG Benefit Solutions, our group benefits joint venture with AIG Property Casualty, under which AIG Life and Retirement reports 50% of the results. Our institutional markets business represents opportunistic offerings, including stable value wrap contracts, structured settlements and pension buyouts. Given our opportunistic approach to the institutional marketplace, you will find [ph] results will fluctuate from period-to-period.

Slide 15 highlights the product diversity across our segments. The contribution of strong alternative investment returns benefited all product lines this quarter. In addition, active spread management benefited both our Retail and Institutional segments. Total base portfolio yields, shown on Slide 16, remained under pressure due to the continued low interest rate environment. And total yield or reported yield reflects the strength of alternative investments and the gain on our investment in PICC stock. We expect that base yields could see pressure for the rest of this year as we continue to take gains on certain portfolios of securities, in order to utilize capital loss carryforwards that are available to us, and due to prevailing low interest rates.

Turning to Slide 17. You can see the trend in base yields and net investment spreads, in each of our leading spread-based businesses, fixed annuities and group retirement. Fixed annuities have benefited from our active management of crediting rates, and net investment spreads increased this quarter. Approximately 73% of our fixed annuity and universal life account values now are at minimum guaranteed crediting rates and we would expect to continue to actively manage spreads. Group retirement also benefited from reductions in crediting rates, which offset the impact of shifting into certain lower-yielding, higher credit quality invested assets, which we mentioned we began last quarter. When considering our fixed product flows, it is important to note that close to half of our sales and deposits were into products with guaranteed minimum interest rates of 1%, while the majority of surrenders, death claims and other benefits were paid from products with a guaranteed minimum interest rate of 3% or above.

In sum, we're off to a good start to the year with solid earnings and distributions to parent. We plan to continue to execute on our growth strategies by leveraging our strong relationships with distribution partners and to increase sales of our broad product portfolio across all channels, while continuing to look for opportunities to run our businesses in the most effective and efficient manner possible.

And now 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. Operator, could we open up the lines now for Q&A?

Question and Answer

Operator

[Operator Instructions] And we'll take our first question from Jay Gelb with Barclays.

Jay H. Gelb
Barclays PLC, Research Division

There's been a significant amount of news around the lift-out [ph] of the team from AIG Property Casualty to Berkshire Hathaway. Could you address that and also give us a sense of whether we should anticipate that more of the leadership could depart?

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Well, I guess, I can only tell you that of the top 3,300 executives of AIG, during 2012 of the top 30% performers of that group, we retained 94% of those people. So I know you want to focus on 4 people in the Property Casualty business. It's a very big and successful business. We're going to lose people to competitors from time-to-time. We have an outstanding team that's still here. You saw how quickly Peter was able to put new executives in charge. I think the reaction to the staff has been very positive. So turnover occurs, but if you can retain 94% of your top 3,300 people running this company -- and by the way, 45% of that group had been with AIG more than 10 years, 15% of that group more than 20 years. So we have experience, we have a deep bench, we have a talented group of people. Not everybody is going to be happy with the company as we go forward. And I can see that our competition is struggling a little bit with their flows and so they have to get in businesses they weren't in traditionally. So I think we're fine and we're moving on. So I think that's the only way I can answer the question.

Jay H. Gelb
Barclays PLC, Research Division

Okay. And then switching gears, could you provide some insight as to when AIG could reinstate its common shareholder dividend and also resume the share buyback?

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

What we said is that we're going to focus on our coverage ratio. We're going to continue to focus on liability management. We also want to make sure that we have completed the sale of ILFC so that, that noncore asset is now completed in terms of the sale, so that we reduce our debt. For example, you know it's not direct, but about $25 billion. That's a key milestone we have to reach. We're continuing to look at our capital plan and doing our stress testing. And we're meeting with the rating agencies to make sure that whatever we do does not cause them any concern. And then our second priority after liability management, we said would be a dividend. And after that, we would still like to do stock buybacks, but we'll do it in a very slow and cautious way to make sure that we do nothing to affect our current ratings and that the rating agencies are satisfied with what we're doing. Because the most important thing for AIG right now is to maintain and build on the confidence that we can make guarantees, booked [ph] sometimes for people's lifetimes. And we'll be here to live up to those guarantees. So that's our highest priority as we go forward. And so as the year progresses, you can see our numbers, you can see our performance. When we think it's prudent and everyone else feels it's prudent, we'll make those decisions.

Operator

And we'll take our next question from Greg Locraft with Morgan Stanley.

Gregory Locraft
Morgan Stanley, Research Division

I just wanted to clarify the ROE goal. It's not inclusive of FAS 115 and the DTA. Is that correct from a book value perspective?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

That's correct.

Gregory Locraft
Morgan Stanley, Research Division

Okay. So just to be clear, you take current state of book value of $67, subtract $20 a share. And so we're really at a $47 book value number and then we sort of grow off of that and we want to earn a 10% ROE against it?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

I'm not quite sure I follow your math. Maybe we could do that offline. I think that's probably the best way to handle that.

Gregory Locraft
Morgan Stanley, Research Division

Okay. I mean, it's just FAS 115 and DTA subtracted from current GAAP book value. But okay. So the goal is 10% ROE x FAS 115, x DTA in 2015. Great. And then the other is just on the capital deployment side. You mentioned $25 billion to $30 billion. Can you update us on how much you have left to do to get to that goal? Like how much has been completed and how much more can you do to meet that?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Yes, sure. This is David. We did -- through 2012, we did $13 billion of common equity share repurchase. And thus far this year, we've done a little over $2 billion of debt capital management. Again, I gave you the interest savings on that. We don't view maturities that are being funded through cash as part of that capital management. That's just part of the ongoing management of the company. So the calls, the early calls on the hybrids, we do consider that part of our capital management goal. So if you think about it, through the end of this year, we'll have done -- with what we've already done, plus the planned call on the hybrid, we will have done close to $16 billion against that $25 billion to $30 billion. And so that's how you -- I mean, that's where we are to date. And then the company continues to generate deployable capital, and we said the $4 billion to $5 billion per year of dividends and distributions from our operating companies. We have interest expense and some parent company expenses of roughly $2 billion or so a year. And so therein lies the generation of deployable capital. And as Bob referenced earlier, the unencumbered proceeds from ILFC, which will be available at the holding company for consideration.

Gregory Locraft
Morgan Stanley, Research Division

Perfect. Great. That's very clear. And then last is just any update on the nonbank SIFI process, the timing. I'm wondering if that's slipping at all and when we might get clarity. And I know that's a bit unfair, but just any help there would be great.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

I think on the SIFI part of it, we're working -- remember we are now being regulated by the Federal Reserve. We've been working through a lot of things with them since they arrived in September. We have a very good working relationship. They have dug in to understand a lot of our businesses. They are now into the process of fully examining the way we stress-test this organization. So the SIFI process is going to be something that we'll have to go through. But I think the biggest issue there probably would be what amounts of additional cushion you may have to have. But as far as the basics, you've got to make sure that you're running these companies, insurance companies, the banks and so on, in a sound way. I mean, there's a huge public outcry of making sure that these institutions don't need taxpayer money. And unfortunately, we have not done a very good job as an industry explaining how much has been done in the last 4 years, with over $400 billion of additional capital being raised to strengthen these institutions, so it's very difficult for them to fail based upon the stress test that everyone is going through today. So a lot of progress has been made. People have still not declared victory, unfortunately. So I think that's the bigger cloud. But I'm pretty confident that SIFI or not SIFI, at the end, we're going to be able to demonstrate the financial strength of this company, that our stress tests are very well done, that we understand risk management, that we've dealt with the noncore assets and that AIG has the financial strength to do its capital management on a go-forward basis in a prudent way. So that's pretty much where we're at. And when SIFI comes, it comes, but it will be more about the ratios than the quality of our numbers.

Operator

And we'll take our next question from John Nadel with Sterne Agee.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

I guess, either for Bob or for David. You opened the call with commentary about focusing on the core. And my question is when -- on an internal basis, when you strip out some of the noise in the quarter, obviously very favorable overall. I'm hoping you can help us discern what you'd view as the true core underlying earnings and ROE? I know David mentioned that ROE on a reported basis was about 11% on equity, excluding the DTA. But I'm interested in your view as to the core results.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

I think I'll let David answer. We normalize for things that are pluses and minuses and we've gone through some of that. And you've got to decide, all of you, I can't give you the answer, John. You've got to think about how you want to deal with partnerships. And we may want to budget it at 8% or 10%, you've got to decide if getting to 11% or 12% is still core. But I would say that if you look at our accident year information, that's a key indicator. You look at the flows in Jay's business, net flows, and understand that our losses in terms of surrenders in the fixed annuity block are at minimums. So therefore, that's actually improving the spreads. So all of that -- I don't know how you would do that, but you have to look at, I would say, just his flows, his spreads and looking at the Mortgage Guaranty and the new book of business coming in. And I think in Property and Casualty, the accident year combined ratio is a hell of an indicator. So those are some of the things I would suggest you want to think about as you examine our ability going forward. David?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Bob, I think you've laid that out very, very well. The items that give rise to variability, things like the alternative investments or the Direct Investment Book that will, again, over time, pull to a level of intrinsic value that will ultimately be monetized. Again, the path from here to there is not a straight line. So again -- and we give you some broad parameters around what's on the balance sheet vis-à-vis the Direct Investment book in terms of the total assets and total liabilities. We also, in the financial supplement, give you some parameters around what the alternative investments are for each of our core businesses, that again, you can make some reasonable assumptions based upon the prior performance and your expectations about what the equity markets and the like will do over time. So what we try to do for you is give you a sense of what those underlying variable items are, so you can make your own determination and assessment about them. Again, we're making risk return tradeoffs in terms of maintaining and holding those assets, as we did with, for example, the Global Capital Markets and some of the wind-down portfolios in the legacy financial products book. Again, over time, we believe there is intrinsic value that's appropriate for us to hang on to, given the risk return. And it will pull to intrinsic, again, over time. So there's some pages in the supplement that give you the underlying balance sheet, so you can make those assumptions.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

I guess, maybe suffice to ask it this way. I assume you believe that the core underlying results are right on track or on track with your overall objective, looking out the next couple of years.

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

I think we remain committed to our long-term aspirational goals. And the results of the company, the progress that Peter and Jay are making, are the basis that give us confidence to remain committed to those goals.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

And just a quick follow-up on Peter's comments, I may have missed it. He made a comment about Commercial Property, and I wasn't clear on whether it was a 20 point improvement in the accident year loss ratio. It seems like too much. Or maybe it was a comment pricing. Could you just clarify that?

John Doyle

John, it's John Doyle. When you normalize for the accounting changes and some of the reinsurance activity in the quarter, it was a 20% increase in net written premium in the quarter.

Operator

And we'll take our next question from Mark Finkelstein with Evercore Partners.

A. Mark Finkelstein
Evercore ISI, Research Division

You gave some new disclosures on the cash and kind of committed to the DIB at the holding company, which is very helpful. If you kind of work back from kind of on balance sheet resources, adding kind of the unencumbered fixed income investments, you get to a number of around $6 billion, which obviously excludes the future proceeds from ILFC or kind of the MetLife escrow, et cetera. But the number is around $6 billion, if my math is right. I'm just kind of curious, if you put SIFI to the side, what is the right number to hold at the holding company in terms of kind of cash and investment resources, knowing you've got CMAs and the way the whole structure works?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Mark, it's David. Yes, your math is correct. If you look at Page 7 of the call deck, you get in that zip code, it's $5.9 billion, $6 billion as of the end of the quarter. And then again, what I said earlier was that, again, at the holding company, we have at the end of the -- when we exit 2013, the run rate interest expense will reflect our cash-funded maturities and the active or proactive debt capital management that we have undertaken this year. So the interest expense will come down accordingly. But nonetheless, we'll have roughly $2 billion-plus, $2.2 billion, $2 billion, something like that, in terms of annual expenses at the holding company to be funded. And again from that -- again we've not given a specific amount or an algorithm or a formula or a stated amount to hold. But that gives you a sense of what prudent financial management would call for. So in any event, then you can go from there in terms of how we're generating deployable capital for consideration once the SIFI designations are known and we understand the requirements of the stress test, et cetera.

A. Mark Finkelstein
Evercore ISI, Research Division

Okay. And then I think you emphasized the $750 million hybrid as the liability management through '13. But you emphasized through '13 and you emphasized liability management generally in talking about kind of the capital position. How should we think about liability management beyond '13?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Well, I think you should think about it as opportunistic. And we will assess the progress that we've made vis-à-vis our coverage ratios that Bob spoke about earlier. And we'll evaluate again all facts and circumstances at the time. So again, we've made very good progress in 2013 on the goals we've set out to improve our coverage ratio. And again, I think that will -- as we have done in the past, we will look to optimize returns for all the various stakeholders. And obviously, capital management is an important part of that.

A. Mark Finkelstein
Evercore ISI, Research Division

Okay. And then just one quick final question, please. I don't know if Brian's there, I assume he is. But how much is the remaining -- what's the update on the remaining pull to intrinsic in the DIB that you estimate currently?

Brian T. Schreiber
Former Chief Strategy Officer, Head of Corporate Mktg & Communications and Executive VP

As we've said in prior quarters, the pull to intrinsic is holding strong. It's approximately $5 billion, consistent with what we had talked about last quarter. That will obviously be realized over a longer period of time. And again, you're seeing the results coming through in the earnings. As David mentioned, the DIB sort of reaches its half-life in 2017. There's another big slug of maturities in '18. So it would be sort of after that point that we'd see a fair amount of that pull to intrinsic, as well at that point, some release of the capital in that business.

A. Mark Finkelstein
Evercore ISI, Research Division

So $5 billion from this point?

Brian T. Schreiber
Former Chief Strategy Officer, Head of Corporate Mktg & Communications and Executive VP

That is correct.

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

That also includes not just the DIB but also the legacy FP portfolio.

Operator

And we'll take our next question from Randy Binner with FBR Capital Markets.

Randolph Binner
FBR Capital Markets & Co., Research Division

So I have a question about the yen. And I think about 20% of the P&C consolidated premiums come in the form of yen premiums. And I don't believe that it's hedged from an earnings perspective. So I understand the call-outs that you gave on how that affected the top line production, but it didn't seem like there was much bottom line impact this quarter. And so I guess, one, I wanted to clarify that there was not a lot of impact from the yen, and that maybe related to the fact that the combined ratio is relatively close to 100. But then also to ask if you have plans to potentially hedge that more actively going forward, if you plan to have profitability improvement.

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

This is Peter. The issue is that Japan, unlike the U.S., is heavily a consumer business. And it's our largest direct marketing operation, which has substantial upfront marketing costs, which are expensed in the current period. So from a GAAP net income point of view, you're absolutely right. The bottom line in yen is actually quite small. But the value of new business that we originate, if you were to capitalize that acquisition cost over the expected life of the persistency of these policies, which are annual policies but have a very high renewal percentage, makes it a very attractive business from a lifetime customer value perspective. So from a value point of view, we are hurt by the weaker yen because that value of new business is reduced. But from a GAAP reported bottom line, we're pretty indifferent. So that does present some hedging dilemmas in terms of GAAP reported volatility. But I think that your way of observing the top line impact is where the visible affect of the yen is most notable. But the GAAP volatility, as a result of yen volatility, is negligible. But from a value point of view, that franchise is valuable, but it will be realized over the life of these customer relationships.

Randolph Binner
FBR Capital Markets & Co., Research Division

So I mean, I guess, is it correct though, that there's not an active hedging program on that value, I guess? And is there anything about what's going on with the movement in the yen that would make you rethink that?

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

We have currency exposures in all 90 countries we operate in. We manage our currency exposures in a top-down way, because we have positives and negatives all over the place. We do not do micro hedging of each line item. So that's all I think I'd say about the hedging approach.

Randolph Binner
FBR Capital Markets & Co., Research Division

Okay. And there's one more if I could just on the very good underlying combined ratio on Property Casualty. Is there more -- business mix and kind of higher-value business are phrases that you've used to describe the result. And I think, like John Nadel, I'm just kind of wondering what we can run rate going forward. Is there more Property business being written here, and so it kind of overearns a little bit in a quarter like the first quarter, but it could get hit if there's higher cat activity as the year goes on? Is that a major feature of what we saw on an underlying basis in the first quarter?

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

Well, I'll have John elaborate. But I think we made it very clear that we think that the first quarter was a light cat quarter. So yes, the cat quarter needs to be normalized for the normal run rate of cats. We have seen a growth in our Property business, especially international property, especially our large limit property. But our aggregate PMLs have been coming down steadily as we manage our aggregations more and more. So I think that it's an inherently volatile line, and so you need to normalize for cat activity. But John, you want to elaborate on that?

John Doyle

I would just add that the exposure growth in property -- I mentioned to John that the premium growth, net written growth in the quarter was about 20%. But the exposure growth was less than that. We saw about 8%, 9% of price improvement in our Property portfolio. And as Peter mentioned, our PMLs are on a now modest decline year-over-year. So the exposure growth has come outside of cat and really outside of our peak zones in the United States.

Operator

And we'll take our next question from Jay Cohen with Bank of America Merrill Lynch.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

On the alternatives, I know some of these are reported with a 1 quarter lag. Based on the movement in the markets in the first quarter, do you have any visibility into the 2Q reported numbers? I mean, it seems like it's setting up to be a better-than-expected quarter again. Can you just talk about that?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Bill Dooley?

William N. Dooley
Executive Vice President of Investments

Well, Jay, you see the same results for the quarter as I do, as far as the general market is concerned. And the 1 quarter lag is only to do with the private equity portfolio, the other one is just a 1 month lag on the hedge funds. So I don't want to assume where the market is going to go, but I'm not going to just agree or disagree with what you just said.

Jay Adam Cohen
BofA Merrill Lynch, Research Division

Fair enough. And I guess, a follow-up to the last question. Peter, you mentioned obviously we need to adjust for catastrophe losses. Do you have a sense of that, excluding catastrophe losses, if loss activity in general was in line or lighter than normal?

John Doyle

Jay, it's John. Our property losses were in line with what we expect, including shock losses in the quarter. I would say that the shock losses, so the more than $10 million losses in property, were in line with what our expectations were but higher than a year ago and higher than the fourth quarter.

Operator

And we'll take our next question from Josh Shanker with Deutsche Bank.

Joshua David Shanker
Deutsche Bank AG, Research Division

First, a numbers question. I want to know if you could walk through how much the DTA was used during the quarter and how much the valuation allowance came off.

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

On the valuation allowance, Josh, we took on the DTA, on the capital loss carryforwards, took down by about $750 million. That was through income. And there was about another $50 million or so that came off through OCI. So in total, the strategies that produced prudent and feasible transactions were about $800 million or so. And then on the DTA utilization, Jeff Farber?

Jeffrey Mark Farber
Former Chief Risk Officer for Commercial Insurance

Well, it's essentially the same thing, right? So we only do our tax return once a year, so when we do the tax return -- but you could kind of think about the earnings for the quarter as a surrogate for usage. So when we continue to use the NOLs actively and we continue to use the -- utilize the life capital loss carryforwards as we have disclosed in the quarter.

Joshua David Shanker
Deutsche Bank AG, Research Division

And I'm not trying to be begrudge Peter or John or James, anything. I'm trying to understand the long-term compensation plan a little bit and some of the specific targets. And when it says on the long-term comp plan, there's specific targets to receive 50% of the bonus, how do those specific targets in the P&C division relate to the aspirational goal of 90% to 95% in 2015?

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

This is Peter. The aspirational goals are laid out in different components. There's a combined number, there's an ROE number. And the one that -- if you want to pick any one of them that is sort of the most important one that we focus on, it's the ROE one. So we, as you know, gave a range for the combined. And you want to be at the lower end of that range if interest rates are high and you're getting your results flattened by high investment income. And you'd be -- so I think that what we view as the alignment between the compensation plan is effectively an ROE goal. And so if we are on the ROE walk that delivers the 2015 goal, then people will feel pleased. So it's, I think, a very strong alignment. We set fairly broad goals. We don't break up the company into little silos. And that's a big change and I think culturally, has people working together across boundaries, whether it's geographic boundaries or business line boundaries, so that everybody wins if we all win as a team. And I think that, that's really showing up in the culture of the company. And our customers are giving us feedback on that. So I think we want to align interests with the shareholders, as well as making sure that our units work together across boundaries well. So it is a pool approach of how the Property Casualty business as a whole achieves its ROE goal, which then drives the ROE goal of AIG.

Joshua David Shanker
Deutsche Bank AG, Research Division

Well, Peter, do you think it's feasible -- look, I'd like you to get paid and make a lot of money. But if you don't hit that 95% or below target, do you think it's feasible that the ROE goal will be achieved?

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

Yes, absolutely.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Absolutely, it could. It's a question of capital-intense products. It's a whole other series of factors that go on here. And what's important is that it's the quality of what we do. Peter has said numerous times that the combined ratio is a consequence of what we do, it's not what we manage. And when you get involved in managing that combined ratio, you could do some dumb things. And there are things you could do to reduce your expense ratio, which isn't reducing your expenses. And there are other techniques you could do in financial engineering. We want people to focus on the fundamentals, focus on accident year loss ratios, run this thing the right way. And in the end, we believe that the combined will get into that range of 90%, 95%. But most important is you want to continue to grow the quality of your earnings and you want to have a better ROE. And if you continue to grow earnings and improve your ROE and shareholder return continues to get better and total shareholder return plus earnings per share, those are the key indicators for us. And if that all moves in the right direction, then I think people should be paid and they will be paid. So I think their senses are very aligned to doing what's right for the shareholders, and they're in there with the shareholders because of the stock-based compensation part of long-term.

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

And I think that I mentioned earlier in the context of discussing our yen exposure, direct marketing hurts our combined ratio, but creates extremely good value. And we've talked many times about the marginal ROE over the lifetime of those customer relationships that had been in the 20s, 20%, based on very reliable actuarial histories. And so we wouldn't want to underspend on direct marketing simply to get under the wire on a combined target. We want to do good, valuable business and build long-term customer relationships that make sense. And for the skeptics, we will publish greater and greater detail about those actuarial assumptions so that you don't think that we are foolishly wasting money on growth.

Operator

And our next question comes from Mike Nannizzi with Goldman Sachs.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Jay, you mentioned monetizing some capital gains in the life sub. Just curious, how much of the $25 billion in gross unrealized gains is there? And how much do you think you can monetize? And I don't know, David, if you could remind us what the timeline for expiration is on those capital losses.

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Yes. Jay, I'll go first, and then maybe you comment. And Bill, if you want to add to it. A very substantial portion, Mike, of the capital loss carryforward DTA expires at the end of 2013. We have -- there's about $1 billion or so that spills over into '14. But the bulk of the carryforward expires at the end of this year. Now the NOLs, just to be clear, the NOLs go out through 2028 and '29, so there's a very ample time there. And then the foreign tax credits are more in the 2020, '21, '22 range. So that gives you a sense of the expiries.

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Right. Yes. No, this is unrelated to the NOL DTA, but just purely the capital gains you get.

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Right. And that's why the focus is on 2013. So the harvesting, et cetera, will, again, be more opportunistic beyond 2013 and '14. Bill, you want to comment?

William N. Dooley
Executive Vice President of Investments

Sure. When you look at just the capital gains by itself, there's other programs that we look at, too, on harvesting gains for tax reasons. And the gain process itself has been going on now last year, and it was restarted in the month of March. And it will continue for the next couple of months. But we're using the gain mechanism also to readjust and reposition the portfolio. So the portfolio, from a duration standpoint, is probably short duration at this time. And we're using this as an opportunity to lengthen the portfolio a little bit and also better balance against some of the products that are in the life companies. And then another example of this is that we're looking at ways to raise liquidity over the period of time for the life companies and for the other companies at AIG. And one of the strategies we've employed is a modified securities lending program. And that gives liquidity to the underlying insurance companies, but at the same time, it generates certain types of tax benefits to us on a simultaneous basis. And there's other transactions and structures that we're using. But the bottom line of everything is it's repositioning some of these portfolios that really haven't been repositioned in many, many years.

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

Mike, this is Jay. I guess, I'd just add one comment to what's already been said, which is obviously it's very economically efficient for us to realize capital gains, given the tax loss carryforward position. But we also very carefully focus on what we can do in terms of reinvestment at any given point in time and what the friction costs are, including the lost investment income if you're not able to reinvest promptly the proceeds of any sales. And so we've targeted certain assets for potential sale, but it's all subject to what we see in the market in terms of potential purchases and as a practical matter, how quickly we can make those purchases.

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

I'd just add to that -- thanks, Jay. The amount that we have actually utilized is actually ahead of what we thought we would do originally, when we first set forth our aspirational goals back in early 2011. So we will have utilized about half of the amount, which exceeded the sort of the 20% to 25% level we were expecting that we could at the time. So Liz, back to you?

Michael Steven Nannizzi
Goldman Sachs Group Inc., Research Division

Can I ask one quick follow-up to Peter? Peter, I guess, you guys had mentioned before a $1 billion run rate or $1 billion savings on expenses and some investments as well. I'm just trying to understand, I mean, we saw the expense ratio fall in U.S. commercial, we saw it rise a bit in international Consumer, and then Consumer in North America was a bit lower than we had. I'm just trying to reconcile those movements. In particular, the G&A expense ratio in U.S. Commercial or in North American Commercial was really low. Can you help me kind of line those dots up a little bit?

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

I'll help you out. I think the basic comment we've made is we have $1 billion of savings for all of AIG. We have said a good piece of it comes from the fact we're doing this whole technology improvement, rebuilding our platforms. We've gone from 28 data centers down to 2. We're moving from 12,500 servers to roughly 2,000 to 3,000, all moved into highly secure locations. All of that will give us a lot more cost savings and benefit. We're rolling out a new 1 claim system, for example, throughout the Property Casualty business. That's a huge investment. Our financial architecture, where we have almost 6,000 people at AIG today working in various aspects of finance, we're rolling out common ledgers and so on, building new processes around that. So this is a fundamental change in how we do business, and it's at the highest level. We keep track of those benefits. We're well on our way to achieve that $1 billion goal. So it's not just a focus on Property Casualty, it's really about the overall of AIG. And at this point, I think we're out of time.

Elizabeth A. Werner
Head of Investor Relations and Vice President

Yes. Thank you, operator. And please, if you have any additional questions, don't hesitate to reach out. We'll be here all day. And thank you very much for dialing in.

Operator
And that does conclude today's conference. Thank you for your participation.