# American International Group, Inc. NYSE:AIG

*FQ4 2011 Earnings Call Transcripts*

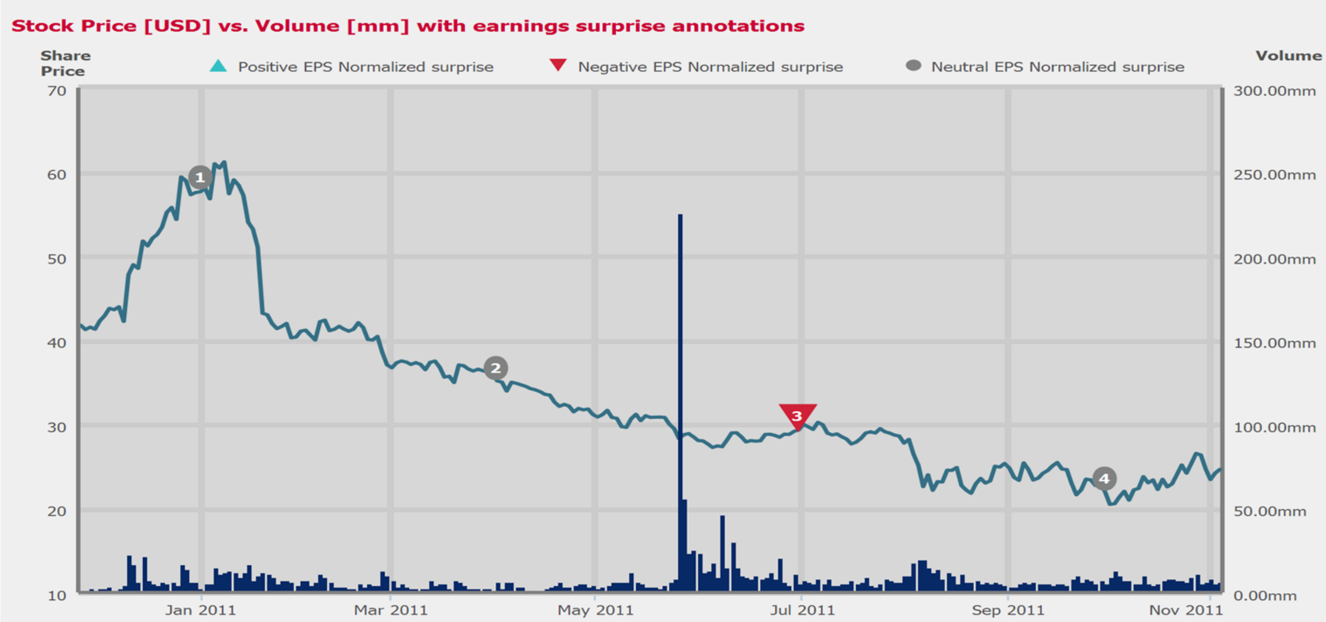
Friday, February 24, 2012 1:00 PM GMT

## S&P Capital IQ Estimates

| | -FQ4 2011- | | | -FQ1 2012- | -FY 2011- | |
|---|---|---|---|---|---|---|
| | CONSENSUS | ACTUAL | SURPRISE | CONSENSUS | CONSENSUS | ACTUAL |
| **EPS Normalized** | 0.65 | 0.82 | ▲26.15 | 0.65 | 0.82 | 1.02 |
| **Revenue (mm)** | 13192.09 | 17409.00 | ▲31.97 | 12517.09 | 54160.49 | 64237.00 |

Currency: USD

Consensus as of Feb-24-2012 12:53 PM GMT




| | - EPS NORMALIZED - | | |
|---|---|---|---|
| | CONSENSUS | ACTUAL | SURPRISE |
| **FQ4 2010** | (14.02) | (16.20) | NM |
| **FQ1 2011** | (0.09) | 1.30 | NM |
| **FQ2 2011** | 0.96 | 0.69 | ▼1 (28.12 %) |
| **FQ3 2011** | (0.28) | (1.60) | NM |

# Call Participants

## EXECUTIVES

**Brian T. Schreiber**
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*Head of Investor Relations and Vice President*

**Jay Steven Wintrob**
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# Presentation

**Operator**

Good day, and welcome to the American International Group's Fourth Quarter Financial Results Conference Call. Today's call is being recorded. At this time, I'd like to turn the conference over to Mr. 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, everyone.

Before we get started, I would 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 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 factors described in our 2011 10-K, under Management's Discussion and Analysis and under Risk Factors. 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 reconciliations of such measures to the most comparable GAAP figures are included in our financial supplement, which is available on AIG's website.

Thank you. And at this time, I'd like to turn it over to our CEO, Bob Benmosche.

**Robert Benmosche**

Thanks, Liz, and good morning, everybody. For those of you who are following the presentation online, go to Page 3, if you would. And we're going to talk a little bit about 2011, and think about where you were a year ago. For us here, a year ago is probably a decade ago, but it was actually only 12 months.

When we started the year off, we had the whole recapitalization of AIG with the Federal Reserve and the U.S. Treasury. And many of you said, "I don’t think they can make it. This just doesn't seem right." And by the way, we were 3 years early for what it is we were required to do at that point in time. But, in fact, we closed in January of 2011. We had some divestitures to continue to reduce the level of debt in our SPV for AIA and ALICO. And you saw we sold Star & Edison, a tough sale, but we got it done; Nan Shan in Taiwan, a tough sale, we got it done; as well as selling off the remaining MetLife Securities so to bring the SPV down to the level we are today, which is well below the starting point of $26 billion.

We had to strengthen our liquidity during the year, continue to get access to debt markets and other facilities, including banks. As you saw, we negotiated our revolving credit facility for $4.5 billion. We did our contingent capital note, and even ILFC was able to get out there and show its strength in the marketplace to deal with its credit needs.

But one of the conditions of closing, if you recall, was we had to raise equity capital. That was the condition of closing, that we could assess the market. And we saw in May, we were able to sell 100 million shares of AIG stock alongside the Treasury's 200 million shares of stock. That demonstrated our ability to access the capital markets. And in fact, we were able to then extinguish the Series G, which was bridged to us until we actually made this accomplishment.

And so in the second half -- we finished the first half, and as we started the second half, we told all of you that we're going from saving AIG to building AIG. The crisis was over. And so as we focus in the second half of the year, some of the things we did that weren't anticipated until 2012, latter part of 2012, we did our senior debt hybrid exchange. We also repurchased -- and have the authorization to repurchase AIG shares for $1 billion. It was just done at the end of the year. So that shows our beginning to do our capital management as we talked we're going to be able to do.

But when we think about capital management and where we are, one of the things we anticipate is we will be regulated by the Federal Reserve Bank of New York, is our assumption. And therefore, we're doing everything we can to make sure we do put in the disciplines and be ready for them when they arrive.

One of the things they do require is stress testing. And so we made our best guess as to how you'd run the stress test. We don’t have all of the information. They haven't given us direction on what to do. But in attempting to understand what they announced recently, we've run a stress test of AIG, assuming we've got most of the major pieces correct.

We wanted to understand where our Tier 1 capital was and see if that's a binding constraint on capital management. What we found is, okay, you have to have 5% minimum and maybe 1.5 points on top of that to be a SIFI. We came out in the 8% range of Tier 1 capital, which means if we got it right in terms of our interpretation of the rules and we got some other things right in terms of how we attempted to execute it, we could have as much as $10 billion of extra Tier 1 capital in this company. And we said we're over-solving for capital early on because we want to make sure that people understand we are financially strong.

That doesn't mean there's $10 billion that we're going to put to work right away. It just says that Tier 1 capital looks like it may not be a binding constraint. What is a binding constraint is the operations of this company, our ability to generate cash. And as you can see, in 2011, we generated almost $3 billion of dividends out of the insurance companies, almost $1 billion in the fourth quarter alone. So we're continuing to see the cash flows come in. We're comfortable with our capital ratios right now, and so the real challenge is getting operating performance right for this company. You see that in the fourth quarter.

We also had to deploy a lot of cash in 2011 because we had a huge pile of cash at the beginning of the year because we thought we're going to buy Maiden Lane II. We have succeeded in putting all of that cash to work throughout the year. You see that in our income in the fourth quarter, so you see the evidence of that money working. We've been asked a lot of questions about how much of Maiden Lane II did you get. So I might as well just answer it so that you don’t keep asking it. Of the -- up until now, there's one more tranche to go, but up until now while we've added a lot of mortgage-backed securities to our asset class that we have for the general account and so on, we've only purchased just under $2 billion of the assets coming out of Maiden Lane II. As we shared with you through the year, we had found that other institutions that want to reduce their risk-weighted assets, we were able to find some pretty good product, better-quality credit and a pretty good yield. So that's what we chose to do instead of competing for pieces of Maiden Lane II. We felt more comfortable with the whole thing. But if we didn't get the whole thing, we were very careful about what we bought within the Maiden Lane II. So just want to put that to bed, if I could.

So our crisis is over. We had a good 2011. A lot of people say, "You made it, but -- " There's a but.

So let's go to Page 4. What are some of the buts that I keep hearing? But it's a soft market. Try to assess [ph] operate within the soft market. Rate's not coming back. You've heard us say throughout the year that we are now working hard to get at least earn our cost of capital. Peter has talked very eloquently about risk-adjusted profitability, and we've got to look at the risk we're riding and do it in a more holistic way, because our new organization allows us to do that. So you can see we got rate, 4% in U.S. and Canada workers comp, and we've been talking about issues in workers comp now for the last 1.5 years. The market is beginning -- our competitors are beginning to see the financial effect of that. But when you look at workers comp and property, up 8%, so we're getting rate.

But the reserves. We're concerned about the quality of the reserves. You see in the fourth quarter, we added about $13 million to the reserve. So on a year-to-date basis, we added about $195 million to the reserve. When you think of that $195 million for the year, and, again, you saw it throughout the year, it wasn't a surprise in the fourth quarter, when you think about that, keep in mind what percentage that is of a $71 billion reserve. It's very infinitesimal.

So we are very confident. As we look at our reserves, we're still, in many of our products, above the central estimate of the outside actuaries. We've got a lot of people focusing on our claims, our claims process and our reserve process. So I don't know what more we can do other than give you another year to see that the reserves are in very good shape.

Can we generate cash flow to do capital management? There was a big piece along with the DTA. So that we have the tax cash flows as we earn taxable income as well as the dividends, and so on. As you can see in here, very strong in the fourth quarter, strong for the year.

But the low-interest-rate environment. You know the equity markets. Your franchises were damaged. It's tough to make money in a low-interest-rate environment. If you look at our ability at SunAmerica, they have performed very well. If you look at -- remember, it's not just the portfolio rate, it's what your crediting rates are. And yes, there's going to be some pressure. But it's not as dramatic as everybody wants to say. And then sales continue, not at the pace they were, because people still need to save their money. They can't just sit in cash. So look at our numbers, our flow. As you can see, we had net flows again of $673 million, very strong for the year.

But the housing crisis. The housing crisis is going to drag you down. You're in the mortgage business. Look at the other primary insurers, you got a problem. We have told all of you over the last 2 years, we have redesigned the way we write business at United Guaranty. They have a multivariate model that is extremely successful. We're getting better-than-expected returns, and in fact, the ROEs on the new business we're writing is in the 20% range. So while we have a housing crisis, we see that pretty much behind us, and you're going to see this business, which is now the leader of the industry, continue to pull out with really good numbers as we move into 2012 and '13.

And so the last but is but the DTA. It says that you really are not confident about your future profitability. Well, we are. And the DTA comes through and says, "We have a clear view now that we could use the tax benefits here within the time frame that's allowed for them." In fact, we think it says that we're well on our way to our aspirational goals, well on our way. And in fact, as we get to 2015 and achieve those aspirational goals, we think we'll probably use up somewheres around 65% of this DTA on the way. So net to us is the fourth quarter is a clear demonstration that this company has not only survived, it's got its strength, it's got its key people, and we're moving in the right direction, and we're going to continue to build value for our clients, for our shareholders and have a great place for our employees to thrive in.

So on that note, let me turn it over to David Herzog, who'll take you through some of the numbers.

**David Lawrence Herzog**
*Former Chief Financial Officer and Executive Vice President*

Thank you, Bob, and good morning, everyone. This morning, I'll go over some of the highlights over the quarter, and then Peter and Jay will comment on specifically the results of Chartis and SunAmerica. And I'm going to build on Bob's themes that he set forth. And I would characterize the quarter as pivotal, both for what did happen and for what did not happen.

And what did happen is our core insurance businesses made $1.3 billion despite $467 million of CAT losses. What did happen is SunAmerica had another solid quarter with strong sales, strong flows and driven by growing distribution. What did happen, as Bob referenced, is continued capital flows from our operating companies to our holding company for capital management, which is a key pillar of our long-term aspirational goals. And what did happen, as Bob mentioned, is we completed our assessment of the DTA valuation allowance that we set out in our 10-Qs earlier in the year, where we concluded that it is more likely than not that we're going to realize a substantial portion of our DTAs based principally on our return to sustainable profitability.

And what did not happen is the need for significant Chartis loss reserve development charge. In fact, loss reserve development for the year and for the quarter were benign.

If you turn to Slide 5, you can see the increase in GAAP net income to $19.8 billion, which included $17.7 billion related to the reversal of the valuation allowance. Net income per share was $10.43, which included $9.34 per share from the valuation allowance. After-tax operating income, which is our principal non-

GAAP measure, was $0.82 per share versus a loss of about $16 a share a year ago that included the reserve strengthening. Importantly, our GAAP book value per share increased 18% to $55.33, reflecting the valuation allowance. And book value per share, excluding AOCI, was $52.69. Also impacting book value in the first quarter of 2012, but to a far lesser extent than the valuation allowance, is the EITF 09-G. That's the new DAC standard. In the 10-K, we provide the GAAP after-tax impact to book value of 09-G, and that's about $3.7 billion or about $1.95 per share excluding AOCI, and that'll be recorded in the first quarter. The future earnings impact of 09-G are largely related to the direct marketing activities at Chartis.

Moving to Slide 6. In core insurance operations, Chartis' pretax operating income was impacted, as I mentioned, by $467 million in CAT losses, including $368 million from the Thailand floods. This was a record CAT year for Chartis, totaling nearly $3.3 billion. Despite the CAT loss -- losses for the year, Chartis delivered $629 million in dividends to the parent the fourth quarter and $1.5 billion for the year.

SunAmerica, as I said, had another strong quarter with pretax operating income of $931 million. SunAmerica's results included 200 -- a little over $200 million from a favorable legal settlement, which was offset by a little over $100 million from an IBNR reserve increase that Jay will comment on in a minute.

For both Chartis and SunAmerica, alternative investment returns were weak for the quarter compared to a very strong fourth quarter a year ago. Total fourth quarter alternative investment income declined by a little over $700 million from a year ago. Last year's fourth quarter alternative investment returns were roughly 14% on an annualized basis, making for a tough comparison. For the full year, alternative investment returns were around 7% versus 9% in 2010. Looking ahead to

the first quarter, we'd expect the returns to improve sequentially given the fourth quarter performance and the one-quarter lag for our private equity investments. We continue to expect an approximate 10% annualized return over the long term for the alternative investments.

Moving to our non-core operations. ILFC reported fourth quarter results of $119 million profit versus last year's loss. ILFC is benefiting from managing its fleet aggressively. In the quarter, we reported about $40 million of charges related to airline bankruptcies. As you know, we filed an S-1 last September, which is consistent with our view that this is the non-core business. ILFC's book value was approximately $7.5 billion at the end of 2011.

One thing I want to share with you is the impact on our book value as it might relate to an IPO or a sale of ILFC. It is possible that our book value could be negatively impacted. For example, if we monetize ILFC at its net book value, our book value could decline by approximately $2.7 billion or $1.50 per share. Within corporate, we report a $484 million gain due to the hybrid tender that Bob had referenced.

Turning to Slide 7, you can see the breakdown of our deferred tax assets for which we no longer hold a valuation allowance against, with the exception of the life insurance capital loss carryforwards, for which we hold an approximate $7.2 billion allowance. We are focused on strategies to capture a portion of the value of this asset, but we are retaining the allowance against this for now.

Going forward, we continue to expect an effective tax rate of somewhere between 25% and 30% on our operating income. What is most important about the judgment we made with respect to releasing the valuation allowance is it signifies our view that we have returned to sustainable profitability.

On Slide 8, you can see the impact to the fourth quarter and the full year from our capital management activity. In the fourth quarter, our capital management activities included arranging an additional $0.5 billion contingent capital facility and renewing a $4.5 billion credit facility. We also exchanged $2.4 billion in hybrid securities and began our share buyback program. We repurchased $70 million of our stock at an average price of $22.75. We expect to complete the $1 billion authorization in the foreseeable future.

Capital management is a fundamental part of how we will run this company with our goal of maximizing investor returns.

Slide 9 highlights parent company liquidity sources of $14 billion at year end. The full year 2011, our insurance operating companies paid dividends and note repayments to the holding company of over $3 billion, and we expect to reach $4 billion to $5 billion this year supporting our ongoing capital management plans.

And with that, I'd like to turn it over to Peter for a discussion of Chartis.

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

Thank you, David. Good morning, everybody. I've got a couple of Chartis slides in the earnings presentations, but they're just for your reference. So I'm going to focus on a few notable items from the quarter. And those include catastrophes, reinsurance strategy, reserves, our geographic alignment, our growth plans, especially in the direct marketing channel.

So overall, I was pretty pleased with our performance in the fourth quarter. Excluding catastrophes, actual business results were pretty strong, as were some of our key performance indicators, reflecting progress in our strategic initiatives to improve profit, generate growth and better manage our risks.

As David noted, this was a historic year for CAT losses, and I must say I'm very proud of how our 11,000 claims professionals worldwide handled this by working extremely hard to deliver excellent claims service to our customers, and we received very good feedback on that from both customers and regulators.

We continue to consider our claims organization to be really an important competitive advantage that separates us from the rest of the market. As I reflect on the level of catastrophe losses in 2011, I'm satisfied with how well our efforts to manage our risk appetite resulted in a level of losses in line with the industry if you benchmark it as a proportion of capital, and that's Chartis' capital, not AIG's.

The effective management of our catastrophe exposure is also clearly recognized by the reinsurance market during our very successful Jan 1 renewal season. Today, Chartis has a more efficient blueprint for its reinsurance strategy through a combination of managing our risk appetite, improvements to the structure of catastrophe reinsurance program and the issuance of $1.45 billion in multi-year CAT bonds over the past 2 years. That reduces our reliance on traditional reinsurance.

Underwriting results in the quarter included a favorable prior-year reserve development of $13 million. And for the full year 2011, Chartis had insignificant net adverse prior-year reserve development of $72 million. And our $68 billion in held reserves are regularly reviewed by internal and third-party actuaries as part of an enhanced risk management framework.

Similar to others in the industry, we experienced increased frequency and severity related to the most recent accident years in primary workers comp. In environmental liability, we saw increases for multi-year policies written in prior years. These were offset by improvements in excess casualty and executive liability products.

Excess casualty, workers compensation, specialty workers compensation and asbestos, the 4 lines with the largest reserve increases in the fourth quarter of 2010, experienced overall net favorable development in the fourth quarter of 2011. Chartis continues to reduce our writings in these lines of business. They represented 5.1% of our net premiums in the fourth quarter compared to 6.2% in the comparable period in 2010.

Expense trends were consistent with the increase in higher value-added consumer lines, which have higher acquisition costs but lower combined ratios, and from our strategic investments in systems and processes that yield greater expense savings and improved service and efficiency in the long run. We also expect an additional increase in our expense ratio in 2012 due to our growth in direct marketing, and I'll discuss that a bit more later.

The fourth quarter premium trends are consistent with our emphasis on profitability and capital optimization. Our mix of business demonstrates Chartis' flexibility in deploying capital across businesses and geographies, targeting them where the greatest opportunity for profitable returns exist, given market -- current market conditions and our long-term strategic view.

Our international business was 51% of our total net premiums in the quarter, an increase from 47% in the comparable period the year before. And on the Consumer side, it represented 43% of net premiums compared to 40% in the comparable period in 2010.

So we're very proud of the leadership we're demonstrating in the marketplace with respect to rates and terms and conditions. Rates in the U.S. and Canada region increased approximately 4%. Specifically, workers compensation and property experienced the most notable increases, and they were needed, at approximately 8% increase in both lines.

We recently announced the alignment of our geographic operations within 3 principal regions: the Americas, Asia Pacific and EMEA. The new alignment promotes greater operational efficiency and allows us to utilize financial and human capital optimally. It also provides greater focus on strategic growth economy countries such as China, India and Brazil, among others, that are vital to our growth plans.

With respect to China specifically, this has been a very good month for further improving our prospects in that truly extraordinary country. We've established a long-term strategic relationship with China, highlighted by the fact that we're the largest foreign-owned insurer in China, with more operating licenses and premiums than any other insurer based outside the country. This past week, I visited with Vice President Xi Jinping in Washington and thanked him for his commitment to open up mandatory third-party liability insurance for motor vehicles to foreign-invested insurance companies.

We were also able to renew our longstanding relationship with the People's Insurance Company of China, in which we hold a 9.9% equity stake.

And third, we celebrated the opening of our new office in Jiangsu province in China. This is our fifth license in China, and the region includes 80 million people, with a per capita GDP equivalent to that of a midsized European nation. We're well-positioned in China, and we expect to broaden our relationship there, including through direct marketing opportunities.

Beyond China, we're executing a direct marketing strategy in approximately 50 countries. We're able to transfer our successful DM strategies in Japan, Korea and Israel to other parts of Asia Pacific and elsewhere. Even with an increase in our expense ratio due to EITF 09-G, which we expect to be around 1 point on our combined ratio depending on our marketing costs, we believe that the DM-related business offers very attractive risk-adjusted returns, and we're going to continue to grow that channel.

Let me conclude by saying that I believe that we're very much on pace to achieve our goals by year end 2015. We also continue to measure and refine the risk-adjusted profitability of all our businesses, and we're directing capital and resources to optimize profitability where we see the opportunities. We still have work to do, but our people and platform give me great confidence that we're on the right track.

So next, I'd like to hand over to Jay.

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

Thank you, Peter, and good morning, everybody. SunAmerica delivered a solid fourth quarter with improved year-over-year net flows, sales and base investment spreads. David mentioned the unusual items in the quarter. I just want to add that the IBNR reserve addition of $105 million this quarter reflected new information about the debt claim verification procedures disclosed in recently announced settlements with other companies, including longer lookback periods, and that's what drove that increase.

Taking a look at Page 12. Compared to last year, SunAmerica's fourth quarter earnings were negatively impacted by lower alternative investment returns of approximately 1% in the quarter versus last year's strong alternative investment returns of approximately 14% annualized, as David mentioned earlier, and to a lesser extent, call and tender income and the ML II fair value mark. If you just look at those 3 items alone, the alternative investment change lesser call and tender and the ML II mark, that accounted for a $530 million decline from the prior year.

Looking ahead to 2012, we would expect full year investment returns to reflect the benefit of last year's cash deployment and base investment spreads to be relatively stable.

Sales were strong across all of our product lines and total net flows. As Bob mentioned, we're positive for the fourth consecutive quarter. We benefited from being reinstated on all distribution platforms and added to some new ones, and surrenders remained relatively stable.

Term life and private placement VUL sales delivered strong fourth quarter results, leading to retail life sales growth of 9% and total life sales growth of 24% from a year ago.

I think the sustained positive net flows continue to reflect our product diversity. Sales of group retirement products increased nearly 27% as our focus on individual rollover deposits continue to produce results. However, we do expect sales of individual rollover deposits to slow in the near term due to the low-interest-rate environment. Variable annuities, held by stronger equity markets in the quarter, also showed good momentum, with fourth quarter sales up 24% year-over-year, and this positive trend has continued into the first quarter of this year. Our discipline in the VA market has served us well. For example, our guaranteed benefit rider fees remain above industry averages, and we were the first in the industry to index our living benefit fees to market volatility, as measured by the VIX Index, reducing our exposure to changes in volatility. And just last month, we launched our latest iteration of a derisk product with a volatility control fund designed to reduce the impact of market fall on fund performance.

Also in the quarter, our mutual fund sales continue to accelerate due to strong fund performance and the success of recent product offerings. And while mutual funds are not our highest-margin products, their modest capital requirements allow them to contribute to our returns.

Sales of fixed annuities decelerated in the fourth quarter as expected, given the very steep decline in Treasury rates between the start of the third and fourth quarters. For example, the base crediting rate on bank-sold fixed annuities declined between 25 and 45 basis points depending on the product structure from the start of the third quarter to the end of the fourth quarter. And given the current interest-rate environment, with base crediting rates on new fixed annuities below 2%, we would expect weak fixed annuity sales trends to continue.

Despite that, we'll continue to actively manage our product pricing, in particular, new and renewal crediting rates. We'll review new money rates for fixed annuities weekly and have the flexibility to manage crediting rates on over half of our in-force fixed annuity and universal life in-force account values.

On Slide 13, we show the general improvement in base investment yields and base net investment spreads throughout the year, driven by our redeployment in cash and disciplined new and renewal crediting rate actions. In the fourth quarter, we saw some impact in base yield from lower interest rates, and we would expect additional pressure into next year, all things equal with rates.

On Slide 14, we assume a continued low-interest-rate environment and the implications for operating earnings. Given our current new money rates, our disciplined approach to pricing and active management of crediting rates, we would expect our pretax earnings to be impacted between really $0 and about $10 million this year, solely from low rates and between $65 million and $80 million next year due to the current low level of rates. While the macro environment does present challenges, we've not changed our view on statutory capital over the next 2 years, which remains strong, and we expect our product diversity and distribution breadth to provide continued growth opportunities at attractive returns.

And with that, I'll turn it back over to David to wrap us up.

**David Lawrence Herzog**
*Former Chief Financial Officer and Executive Vice President*

Thank you, Jay, and turning to Slide 15. We consider United Guaranty part of our core insurance business, and it continues to be an industry leader in the mortgage insurance market. The company led new business written in the industry, and in the fourth quarter, we wrote over $7 billion of new insurance. United Guaranty's fourth quarter included $42 million favorable reserve development.

I'd like to highlight another sequential decline in delinquencies and the delinquency rate of just under 14%, at 13.8%. Reserves remain steady, with a reserve per delinquency of $27,000. I think more importantly, I would note that we helped over 40,000 families stay in their home.

And finally, we've also provided some additional disclosure on non-core assets in the Appendix. I'd like to highlight that as a result of the recent sales of Maiden Lane II securities in February that the Federal Reserve Bank of New York senior loan will be repaid in March. And as a result, AIG will begin receiving payments on our Maiden Lane II interest this year. Any proceeds in excess of our principal and interest will be allocated 5/6 to the Federal Reserve and 1/6 to AIG. All proceeds from Maiden Lane II for AIG will be used to repay any remaining balance in the AIA SPV preferred interest. With respect to ML III, payments continue to come in as expected and amounted to just over $1 billion in the fourth quarter.
At this time, I'd like to turn it over to the operator for questions.

# Question and Answer

**Operator**

[Operator Instructions] And we'll take our first question from Josh Shanker with Deutsche Bank.

**Joshua David Shanker**
*Deutsche Bank AG, Research Division*

Can you talk a little bit about the loss emergence trend? You said in the 10-K that you use a shorter-term development pattern to set the reserves for excess casualty. That sounds like a contradiction to me. So maybe you can flush that out. And can you talk a little about what's going on in environmental so we can be confident it's not a recurring event but a onetime event?

**Robert S. Schimek**
*Executive Vice President and Chief Executive Officer of Commercial*

Hey, Josh, it's Rob Schimek. Let me start with your question on excess casualty. You might want to rewind back to the fourth quarter of 2010. It was actually in the fourth quarter of 2010 that we shortened the period that we were looking at excess casualty trends. It actually resulted in us increasing our reserves in 2010, and that was us giving more reliance on the development that we were experienced in the more recent years as it relates to business that had been written previously. And so really, we're simply saying we stayed consistent with that time period that we shortened down in 2010. But it just so happens that the more recent years are showing a better result than they did just a year ago.

The next point regarding environmental, I think I want to highlight a couple of things. There's 2 pieces of disclosure in the 10-K that I think people should be making sure they focus on. The first is the difference between the "asbestos and environmental" and then the environmental line of business that we write. So with respect to that, you might want to take a look at Pages 93 and 102 of the 10-K, although I'm positive -- I know that you have in particular, but I think some other people might benefit by taking a look at that disclosure. What I would note is that with respect to the disclosure we provide on Page 93, we provide a discussion of the fact that we write environmental business through a profit center referred to as the environmental profit center that sits inside of our commercial business. You'd note that the through the first 9 months of the year, we experienced some level of adverse development in the environmental book of business. Following that adverse development, we spent a lot of our fourth quarter conducting a ground-up study of the claims in environmental, and our fourth quarter adverse development is the result of a very focused effort trying to make sure that we were really getting at a claim-by-claim evaluation of that exposure. Historically, we've used more traditional actuarial methods. I think that this is an improvement on what we've been doing historically, because in the end, the best way to get to this exposure is really on a case-by-case claims review in connection with the work that's being done by the actuaries. I'd also want to observe for you that this tends to be from accident years 2003 and prior and that most of that business was business written by this actuarial profit -- this environmental profit center is written on a multi-year basis, and so we are, at this point in time, dealing with those multi-year policies that were written 2003 and prior.

**Joshua David Shanker**
*Deutsche Bank AG, Research Division*

And then of the policy years '08 and '09, which evolve into accident years '09, '10 a lot of your most sober critics say that they're worried about the reserves there, and there was a little bit of reserve development on the unfavorable side for those years. Can we just go through those? And then I will disappear into the queue, I guess.

**Robert S. Schimek**
*Executive Vice President and Chief Executive Officer of Commercial*

Yes, no problem, Josh. I would say that consistent with what you're seeing from other participants in the marketplace, it's been more so related to the workers compensation line of business, so it's not something broad-based across all of the businesses that we wrote in 2008, 2009, 2010. But in particular with respect to workers compensation, we've done, we think, a very good job of pushing rate in workers compensation and in managing our exposure on workers compensation. That book of business has continued to shrink, and it's a place where we've conducted a lot of work regarding the structural drivers of loss to get our hands around what's actually causing the losses in the first place as well as using predictive modeling to help us do a better job with respect to risk selection. And we think we'll continue to get better with respect to all aspects of that as we move forward.

**Operator**

We'll take our next question from Michael Nannizzi with Goldman Sachs.

**Michael Steven Nannizzi**
*Goldman Sachs Group Inc., Research Division*

I just have one question, Peter. In Chartis, the expense ratio looked like -- well, the, I should say, the combined ratio in Commercial lines was a bit higher in the fourth quarter. It looks like the expense ratio was a contributor there and just particularly within international. Just trying to understand what happened there, if you could.

**Robert S. Schimek**
*Executive Vice President and Chief Executive Officer of Commercial*

Sure. Mike, it's Rob Schimek. I'll comment on that for Peter. Let me start by making a couple of observations. First, as you know, our international commercial business has a much heavier 1/1 renewal date. So if you actually go back and look at the premium trend, one thing you will observe is that the earned premium and the written premium relationship changes throughout the year. So, for example, in the first quarter of the year, our written premium outpaced earned premium for commercial international by $700 million. But by the fourth quarter, earned premium outpaced written premiums, so the exact opposite, by $400 million. That actually causes a pretty significant change, a swing in our expense ratio. And you'll notice that it's almost a 10-point swing in the expense ratio from the first quarter to the fourth quarter. That's not unusual for us. That, actually, if you go back and take a look over time, you'll see that, that same type of relationship existed in the prior year. So that's one point to make. The second thing I'll make observation regarding expenses is international commercial is really the heartbeat of where a lot of our efforts are going with respect to some improvements that we're making with respect to our infrastructures. So we're in the process of a very large SAP implementation, probably the largest and most complex SAP implementation for a financial services company in the history of the world, occurring in Europe as we speak. In addition to that, we have Solvency II and a significant legal entity restructuring. So there's truly some additional expense there as well as typical seasonality. The last point that I'd make regarding the loss side of the house for international commercial is that it's largely on the casualty side of the house, and we're continuing to use the same kinds of efforts with respect to international commercial casualty as we do with respect to the U.S. commercial casualty, which is focused really on predictive modeling, evaluating the structural drivers of losses and pushing for improvement in rate so that we can get the appropriate risk-adjusted profitability. So I think it's really the combination of those 3 items, focusing in particular on the expense ratio in the quarter.

**Michael Steven Nannizzi**
*Goldman Sachs Group Inc., Research Division*

Great, and I mean, if I think about it, so we're at 99.4 for Chartis overall on a full year underlying combined. Thinking about 09-G, I'm guessing that's 50 to 100 basis points on total Chartis, thinking about the migration of the business toward consumer lines, some investments in technology, better pricing that you've kind of talked about and any loss trend experience in '11, like how should we think about the basket, those basket or that basket of attributes as we look at profitability from Chartis from here? Is it sort of a J in terms of profitability declining and then starting to pick up? Or how should we think about that?

**Robert S. Schimek**
*Executive Vice President and Chief Executive Officer of Commercial*

I'll reiterate the overall observation that Peter made, which is that we certainly believe we continue to be on pace for our 2015 goals. That will result in different sort of dimensions to the solution. The first, with respect to expenses. You can expect our expense ratio to improve more in 2013, 2014 as we complete some of our efforts with respect to the investments that I described for you just a moment ago within the international commercial business. And with respect to losses, I think you should continue to expect that we'll be making ongoing progress, and we're really focused heavily on using the tools and the technical pricing expertise that we're focused on heavily these days to make sure that that's a continual area of progress. So I think you should -- what I would look at if I were you is I'd look at are they making continual progress on the underlying loss ratio, understanding that we think we have very strong plans and a very determined view that we will achieve our expense goals by 2015.

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

Rob, I'll just add a little bit just on the direct marketing, the pace of growth there. Our current course and speed would add about 0.8 to the combined ratio, but I would love to deliver you the news that the expense ratio impact would be twice that, because we have the bandwidth to grow faster than that, because the prospective ROE on that business is very, very attractive, well above our cost of capital. And so I think that we can demonstrate that through greater disclosures going forward if and when we accelerate the pace of our DM spend. But our current course and speed will be just under 1 point on the combined from the DM, but I think that our way of thinking about that business is economics, not accounting.

**Michael Steven Nannizzi**
*Goldman Sachs Group Inc., Research Division*

And what would be the loss ratio on that same basis? What will be the loss ratio impact if you're getting 80 points of benefit from -- or deterioration on the expense side, what's the offsetting impact on the loss side?

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

It's the combined ratio of that business is in the high 80s, depending on the country. So it's very attractive business. The issue is bandwidth and how much of it you can do how fast. And so we are expanding in 50 countries, prioritizing about a dozen, and we have extended -- extensive experience in terms of persistency, cross-sell, upsell ratios from our experience in Japan, Korea and Israel over the last dozen years. So we have a good framework that applies in many countries, so -- but I think that we can give you more disclosure on that going forward as we fine-tune the pace. But right now, our current pace of growth in that business would add about 0.8 to the expense ratio under the new EITF 09-G.

**Robert Benmosche**

And I'd like to add that one of the things that I've said before and I want to repeat now is that we have not invested enough in technology to really do the data mining, predictive data mining and so on, that we need to do, and so we are going to continue to see that number flow through the expense ratio. And our issue here is to really position us well for the future, and that is the -- for example, we have 27 million claim records in our workers comp area that we never extensively studied. We're now working with Johns Hopkins University to really understand those claims, what they say, what they mean and how we use that as a standard for processing claims and understanding claims going forward. So we're investing heavily around this so that you will continue to see the pattern of expenses from now and before continuing. But we did say we would get to $1 billion saved by the time we get to 2015, and we're on track to do that. But expenses are not a driver. What Peter talked about is having the right growth and the right risk-adjusted profitability of that growth and being able to explain to you if the numbers because of the accounting come out a little different than before, we'll make sure you see what that is. But this is about growing smartly and still leveraging technology as we do it, which, as Rob said, is going to cost us some money, and that's not our driver.

**Operator**

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

**Edward A. Spehar**
*BofA Merrill Lynch, Research Division*

It's Edward Spehar, and then I think Jay will have one question as well. I'm wondering if you could talk a little bit about why you weren't more aggressive with the share buyback in the fourth quarter. And sort of related question on capital generation, cash flow, the $4 billion to $5 billion of subsidiary dividends that you see, could you tell just approximately how that would break down between Chartis and Sun? And again, remind us about the uses of cash at the holding company.

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

Sure, it's Brian Schreiber. On the first question about the share repurchase, keep in mind that the authorization was in November so we had a very short window. We were also subject to volume limitations on how much we could participate in, in daily volume. And it was our intention to not be very heavy in the stock on low-volume days. So that's, I hope, answers that first question.

In terms of the question on the uses of the parental liquidity, there are several. Obviously, we won a variety of stress tests and try and maintain a level of parental liquidity sufficient to meet those stress tests. We also have a variety of obligations, short-term maturities, debt service that we have to meet, and we also have a plan to reduce contingency -- contingent liquidity risk at the company and take down the level of repos and funding arrangements that could result in additional liquidity need. So we keep adequate reserves for that and, again, make sure that we do have adequate resources for our planned and anticipated capital management activities.

**David Lawrence Herzog**
*Former Chief Financial Officer and Executive Vice President*

Ed, one other -- I guess, your other part of your question is with respect to the 2012 dividends. About $2.5 billion of the $4.5 billion might come from Chartis, and we'd expect somewhere around $2 billion from SunAmerica.

**Edward A. Spehar**
*BofA Merrill Lynch, Research Division*

Okay, and just could you talk about just the numbers on the uses of the holding company beyond the sort of the contingent liquidity, just the normal uses of cash at the holding company?

**Robert S. Schimek**
*Executive Vice President and Chief Executive Officer of Commercial*

Yes, debt service is roughly $400 million, parental per quarter -- parental holding company expense is roughly $250 million or so per quarter.

**Edward A. Spehar**
*BofA Merrill Lynch, Research Division*

Okay, and I think Jay has a question.

**Jay Adam Cohen**
*BofA Merrill Lynch, Research Division*

Yes, just really quickly on the commercial pricing. Obviously, good to hear that you're getting momentum in the fourth quarter. Can you talk about what you saw in January? I assume probably a fairly active January season on the commercial side. Can you talk, at least qualitatively, about the direction of pricing. Did it continue to accelerate?

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

I think that the trend is certainly continuing, but perhaps, John Doyle, you want to give a little bit more color on that?

**John Doyle**

Sure, Peter. Yes, Jay, we saw no slowdown in the momentum in January. We continue to be encouraged by where retention stands relative to the prices we've been pushing. Rob mentioned Europe. 1/1's a particularly big day for our business there, and retention was slightly below expectations, but rates were ahead of expectations. So we felt good about that. So there's decent momentum and we're continuing to push and lead the way.

**Operator**

And we'll take our next question from Andrew Kligerman with UBS.

**Andrew Kligerman**
*UBS Investment Bank, Research Division*

Great. A couple of quick questions. On your capital position, Bob, you threw around a lot of numbers earlier. What would you estimate to be redeployable capital, and would an opportunity, say, come in an equity offering be a viable situation where you could deploy it?

**Robert Benmosche**

I'm going to have David and Brian -- there's a combination of what's available now. So if something happened in the next 2 weeks, that's one availability. The other one is dealing with the sale of assets, recognizing we have the SPV here that has to be paid down as a priority, so we're looking at that priority. So I would say that until such time as we clear up the balance remaining on the ALICO AIA SPV, there isn't a whole lot of cash based upon what we can do from sales and so on until that's done. So we're working through that constraint. Brian and his team have given a lot of thought to that. That's why we said we were looking forward to the IPO of ILFC, but the markets really are not welcoming right at this time, so we're still seeing that as a delay until things improve in the airline industry as well as in the markets. So I would say, Brian, it's kind of limited in terms of what we really have in the short term.

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

Yes, as we explained, when we were on the road for the equity offering last year, it was that the bulk of the initial capital management activities would be funded by the monetization of core assets, and then the remaining portion through dividends from the operating companies, so -- and again, we set an expectation that capital management wouldn't really start in earnest until 2013. I think you're seeing evidence now that we are a bit ahead of plan. But again, it's the value of those non-core assets when they get monetized that will provide the bulk of the resources for capital management.

**Andrew Kligerman**
*UBS Investment Bank, Research Division*

Got it. And then just quickly, it's a nice opportunity there to get a gain on the debt extinguishment. Do you see any near-term opportunities there, maybe with some of the hybrid securities?

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

At the current time, we don't have any plans for additional hybrid exchanges.

**Andrew Kligerman**
*UBS Investment Bank, Research Division*

Okay, and then just lastly, with regard to the international commercial operations. So you had an expense ratio in the fourth quarter of 40.1%. It was 43.4%. And it looks like in past years, you were kind of low mid-30s. So when does that expense ratio come down? I think you mentioned 2013, 2014, do we sort of see this elevated level of close to 40% through 2012? And then where should we expect to come down to, low to mid-30s?

**Robert S. Schimek**
*Executive Vice President and Chief Executive Officer of Commercial*

Hey, Jay, it's Rob. On international commercial -- Andrew, excuse me. On the international commercial, what I want to give you a flavor of is timing with respect to these expense initiatives. So we're doing a very significant legal entity restructuring in preparation for Solvency II. We expect the vast majority of that will be completed at the end of 2012, certainly by the beginning of 2013. We are in the process -- separately, we're in the process of implementing SAP as I described. We have a very significant rollout of SAP occurring in the month of March, but we'll continue to roll that out across the rest of Continental Europe through 2012 and all the way through 2013. So that's -- those -- the timing for the backbone infrastructure work that we're doing will take us all the way through at least the end of 2013 before we start to see improvements in that area of the world.

**Andrew Kligerman**
*UBS Investment Bank, Research Division*

At which time, we would probably see a significant dropoff in the expense ratio, maybe down to below mid-30s at that point?

**Robert S. Schimek**
*Executive Vice President and Chief Executive Officer of Commercial*

What ends up happening is, as you know, we can't get the benefits until we actually put the technology in place, so we're doing both a complete change in our target operating model structure in Europe, taking our geographies in which we're doing a lot of our efforts down from 20 different places down to a handful of different places, and that'll create significant benefits, but we're not going to get that until we actually can roll the technology out in 2013. So you're right, generally speaking, you'll start to see that, and we hope it's -- we plan for it to be pretty significant in 2014, 2015.

**Operator**

And we'll take our next question from Dan Johnson at Citadel.

**Daniel B. Johnson**
*Citadel LLC*

Most have already been asked and answered, so I'll just go with a clarification on the ILFC evaluation. I think you had mentioned that there's a book value differences that I think you said at book value sale for ILFC, that's about a $2.7 billion difference. Very simply, is this linear that if you end up selling ILFC for $1 billion less than their carrying -- or their book value that the $2.7 billion goes to $3.7 billion? Or is there something else we need to consider?

**David Lawrence Herzog**
*Former Chief Financial Officer and Executive Vice President*

Yes, Dan, it's David. It's not exactly linear. It gets a little bit smaller, but I think you have the gist of it. Because again, the driver of that is obviously the difference between book and tax.

**Daniel B. Johnson**
*Citadel LLC*

Yes, understood. And then maybe just for Peter, a rather broad question just given that you've got almost 20% of the business in traditional Europe. Would love just to hear some comments of what your folks are seeing on the ground in terms of how the economic conditions there are impacting the business currently and thoughts on how it might impact it, plus or minus, for the rest of the year?

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

Well, I think that in the short term, the uncertainty in the Eurozone is helping us. Some of our competitors, especially local competitors, have experienced significant downgrades in their credit rating, while we've had stable to stronger credit outlook. And so there's a bit of a flight to quality to us. I take small joy in that, even though there's some short-term gains from that growth, because I think it's a symptom of a longer-term, deeper malaise in the European economy, and that can't be good in terms of ultimate demand. So short-term share gains, and I'd even think about Greece, where we have seen a pickup in our volume at very attractive rate, it's, to me, a symptom of flight to quality. But I do -- I am concerned about long-term growth rate in Europe and as things stabilize. But there's, I think, some light at the end of that tunnel. I'm pleased by the results in the last 2 weeks in terms of policy at the macro level. But it's an important part of our commercial franchise. I think that, like the U.S. market, it's mature. We need to choose our shots. We need to manage the cycles well, keep our eye on the expenses so that we don't feel we have to write bad business to cover our fixed costs. And we need to use our capital sparingly and target it at the more attractive growth economies.

**Operator**

And we'll take our next question from Josh Stirling with Stanford -- Sanford Bernstein.

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

So I wanted to expand the conversation a little bit about some of the capital thresholds. How much excess you'd have over time in some of the underlying drivers of that? And I specifically wanted to get a little bit more color around some of the other key capital and liquidity tests beside -- beyond the Tier 1 ratio you flagged. So if you could give us a sense of what the ratings agency coverage ratios you think that you're being held to are, sort of for the holding company liquidity versus debt service. You recently, I think, had put in place the capital maintenance agreements, which has minimum RBC levels, it would be helpful to know. And then also, could you just walk us through technically how we should think about the DTA, the new -- the valuation allowance playing through into capital under various measures. That, I think, would be a big help as we do our modeling in the future.

**David Lawrence Herzog**
*Former Chief Financial Officer and Executive Vice President*

Okay, Josh, it's David. I'll take the last question first, on the DTA, how to think about that. As Bob mentioned, as we think about between now and 2015, we'll use about 2/3 of the total NOLs or the FTCs in combination, and those cash flows will actually come to the parent company by way of tax-sharing arrangements or treaties that have been in place for a very long period of time. So those cash flows will ultimately flow to the holding company and will be a part of the parent company cash flow. Because as you think about the cash that will come, it's the dividend, the after-tax dividends, from the operating companies, which we've talked a lot about, the tax-sharing payments that will come through the tax-sharing treaties and, as Brian mentioned, the monetization of the non-core assets. And we've laid some things out in the Appendix, Pages 17 to 19 in the deck. You can get a pretty good sense of what those cash flows might ultimately be. It's the combination of all of the above that gives us the confidence in why we are committed to our long-term aspirational goals. It gives us the funding that we need and also the capital resources to fund the business growth, as Peter and Jay have talked about. So that's maybe the last part of your comment. I think -- and others can certainly chime in with respect to the capital hurdles, there really aren't any new constraints that we're coming across. I think we've laid those out fairly clearly. Bob talked about the capital requirements with respect to perhaps of Fed oversight. But again, there are other things. With respect to the rating agencies. Our ratings are very important. We place a very high degree of importance on that. That's an important consideration. So it's the coverage ratios and the leverage ratios are not any different for us than they are for any other similarly rated company. So for single-A company, I think the coverage ratio's in the 5x to 8x range. Again, they are no different for us than they are for others. And leverage ratio, and again, I think this ties back to comments Bob made, leverage ratios are -- we've got plenty of headroom there. That's -- again, when we did the recap, we "oversolved" for capital, and that's not a constraint, although it's a consideration, and we -- we're mindful of that over time. So hopefully that's helpful to you.

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

Great, great. And so if I take from all this that sort of in theory, you guys can model forward some substantial capital excess in the future, but at the moment, combination of liquidity and things sort of makes it a much more modest number.

**David Lawrence Herzog**
*Former Chief Financial Officer and Executive Vice President*

Well, I think maybe just to clarify again, I would say we are and remain committed to our long-term aspirational goals as we laid out for the world on our recent offering last year. So again, I think the pacing of that will be driven by, again, the framework that I laid out, but as well as monetization -- importantly, monetization of non-core assets and how that plays into considerations of our Fed readiness and where and when we become -- if we become regulated by the Federal Reserve.

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

No, I think that all makes sense. Of course, we're just all in the business of trying to figure out the timing of all that. Just a one follow-up question related to, I think, Brian's comment about sort of the slow pace of share repurchases. I mean, obviously, float's a consideration. In order to make all these repurchases at any meaningful level, presumably you'd have to be negotiating with the government. I'm wondering if you could give us a sense of what -- to the extent that they've shared any vision -- any view with you in sort of how they think about exiting the remainder of the position. Obviously, that's a huge concern or opportunity for investors today.

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

Yes, that's a question you'd probably have to address to the U.S. Treasury. We're focused on operating the business and don't engage in discussions about that. So that's really what I can say.

**Operator**

We'll take our last question from Greg Locraft with Morgan Stanley.

**Gregory Locraft**
*Morgan Stanley, Research Division*

Just wanted to clarify one quick thing. It's -- I pretty much got everything I needed, but just the ROE aspirational goal of '10 and '15, which book value do I use for that? Is it the 55 and grow that forward? Or is it some other book value I should be using? I'm trying to tie it to an earnings number.

**David Lawrence Herzog**
*Former Chief Financial Officer and Executive Vice President*

Yes, we assume that aspirational goal that the DTA was not part of that calculus.

**Gregory Locraft**
*Morgan Stanley, Research Division*

Okay, so just -- again, just very simply, can you just do the math for me? What should I be doing to the 55 book? Should I taking it to something different?

**David Lawrence Herzog**
*Former Chief Financial Officer and Executive Vice President*

Yes, it's a good question, and that's why we put in the financial supplement, both with and without, so we've done the math for you. Without, for the quarter, we were at 7 2; with, 6 9, I believe, is the number that's in the financial supplement.

**Elizabeth A. Werner**
*Head of Investor Relations and Vice President*

It's on Page 5.

**David Lawrence Herzog**
*Former Chief Financial Officer and Executive Vice President*

Page 5 of the financial supplement.

**Elizabeth A. Werner**
*Head of Investor Relations and Vice President*

[indiscernible] today. Bob, I will open it up to you for any closing remarks.

**Robert Benmosche**

I just want to say that this is another quarter, and we've got more to go. And I think what you see here is the foundation is extremely strong. The company is extremely strong. Our clients have been with us all the way through it and are very confident in us. And so look forward to talking to you at the end of the first quarter. Thank you all very much.

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