S&P Capital IQ

CONTENTS

American International Group, Inc. NYSE:AIG

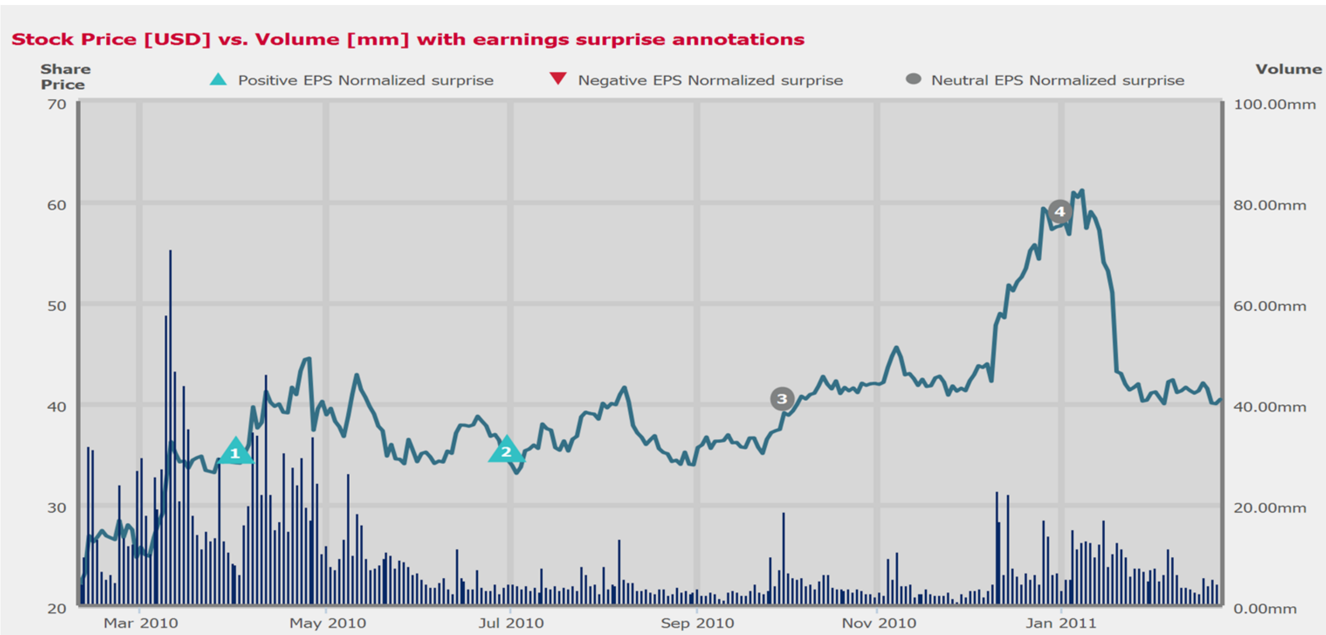
FQ1 2011 Earnings Call Transcripts

Friday, May 06, 2011 12:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2011-			-FQ2 2011-	-FY 2011-	-FY 2012-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	(0.09)	1.30	NM	0.67	3.15	2.76
Revenue (mm)	14974.32	17817.00	18.98	14351.78	60586.43	58635.78

Currency: USD
Consensus as of May-06-2011 5:13 AM GMT



	- EPS NORMALIZED -		
	CONSENSUS	ACTUAL	SURPRISE
FQ1 2010	0.48	1.21	152.08 %
FQ2 2010	0.98	1.99	103.06 %
FQ3 2010	0.93	(1.47)	NM
FQ4 2010	(14.02)	(16.20)	NM

Call Participants

EXECUTIVES

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Elizabeth A. Werner
Head of Investor Relations and Vice President

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

Peter Hancock

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

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

William N. Dooley
Executive Vice President of Investments

ANALYSTS

Andrew Kligerman
UBS Investment Bank, Research Division

Dan Johnson
Citadel Investment Group

Eric Berg
Lehman Brothers

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

R. Scott Frost
BofA Merrill Lynch, Research Division

Presentation

Operator

Good day, everyone, and welcome to American International Group's First Quarter Financial Results Conference Call. Today's conference is being recorded. Now I'd like to turn the call over to Ms. Liz Werner, Head of Investor Relations. Please go ahead.

Elizabeth A. Werner
Head of Investor Relations and Vice President

Good morning, and thank you for joining us. Before we get started today, I'd like to remind you that today's presentations may concern 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 performances and events may differ possibly materially from such forward-looking statements. Factors that could cause these include the factors described in our 10-Q, under Management's Discussion and Analysis and under Risk Factors, and in our 10-K, under Risk Factors. AIG is not under 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 at our financial supplement, which is available on AIG's website at www.aig.com.

And with that, I'd like to turn our call over to our CEO, Bob Benmosche.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Okay, good morning, and thank you, Liz. We have a lot to cover today but let me start with the fact that it's a major quarter for us. We had paid back the Federal Reserve. That's 2 years ahead of schedule. Unfortunately, that requires us to take our final charge of $3.3 billion. Let me ask each of you to pay attention to the DTA, the deferred tax asset. We have now written off $23 billion, but that's the 80% of the company that was taken by the government to give us the loan in the first place. While we've taken the charge in this quarter, and get a total of $23 billion over the last 3 years, what it represents to us is that over the next few years, we will not pay about 1/3 of that in taxes. So we will report after-tax income to all of you, taking into account what wouldn't be the taxes. When it comes into the holding company, because of the DTA, we will actually have that money available to fund our capital management program over the next several years. Though it's behind us, we have it done. We're now dealing with the U.S. Treasury shares as we think about demonetizing that and paying back the American taxpayer. So we're finished on that aspect. Our debt's been covered by the Fed. We're ready to move forward.

If you look at the results in the quarter, we continued to show strong operating results of the company. We have a lot of pluses and minuses that went on as you all saw, but the fact is the underlying core businesses are doing extremely well. If we look at Chartis, for example, we did have significant cat [catastrophe] losses in the first quarter, unprecedented as you see, not only for us but for others. But the fact is, the top line grew, without Fuji, about 6.2%. In addition to that, we continued to de-emphasize those lines that have caused difficulty in the reserves in the past. And so we see that, at the end of the year, those lines represented about 6.7% of our premiums and by the way, in 2006, those lines represented 22% of our premiums. They're now close to 5% in the first quarter. So we continue to de-emphasize those lines and at the same time, we're continuing to grow at the top line of the organization.

We did, in fact, close on our Berkshire transaction, which we've reported to all of you. You can see that we bought $3.5 billion of coverage basically for about $1.6 billion. But more importantly, we got back $200 million, which says that we're redundant [ph] $200 million at that point in time. And so when we talk about the quality of our reserves at Chartis, we continue to stress that when we compare what we've done at the end of the year to outside actuaries, we are still above the midpoint, essential estimates of all of the outside actuaries have looked at it, which we historically have never been. But we have strong reserves and some people might say, but wait a minute, you've just added to the development in the first quarter. So if you're doing okay, how could you possibly add to the first quarter? And I think it's important that we answer that right at this point in time because we want to make sure it's clear that we believe, with all great deal of confidence, that we have our reserves correct. So Rob, if you could, as the CFO of Chartis, explain the legal settlement that anticipated and why we chose to do what we did in the first quarter on reserve development.

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Sure. Yes, good morning. The largest component of the prior-year development in Chartis relates to the settlement agreement that we've disclosed in Footnote 11 of our 10-Q. Following that settlement, we restated our statutory financial statements dating back into the 1980s, which resulted in an increase in our participation in the workers' compensation residual market. While we have the significant amount of IBNR already established for the years that these would relate to, we concluded it was prudent to add to the reserves rather than to use a portion of our existing IBNR to cover this assessment.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

So as you can see, this is conservatism on our part, but we want to make sure we got this right and we keep it right on a go-forward basis. I also want to stress, and that's why I think it's important that you understand the deferred tax asset, we do have about $2 billion of stock capital sitting in Chartis, and it's important that we preserve that $2 billion. And because of the accounting rules, we did the Berkshire deal, primarily to show from a GAAP basis that we would have the profits in the future, such that we could preserve that $2 billion. And so the transaction was done more around the DTA and preserving our capital at this time in Chartis rather than concern about our reserves and what's been setup for the asbestos. So that's pretty much where Chartis is. We have, in fact, reorganized and this decision positions us better for the future. And so we want to make sure we focus on commercial, as well as consumer. We're focusing on ourselves as a global organization while we have the U.S. and international operation. We have to operate far more seamlessly like our clients do, and make sure that we're focusing not necessarily on the top line but getting the right combined ratios and the right risk-adjusted return for the equity committed to the business. Peter is in that role now. We made that change in the first quarter, and he’s off and running, and is going extremely well for us.

Okay, move on to SunAmerica. Again, they had a very strong quarter. You could see in 2010, we had strong positive flows on annuities, for example. Our life sales has started to come back, and the first quarter also showed very positive flows on annuity products. And we continued to be #1 in the banking system, on selling fixed annuities, and it's very well-received. And you can see also that we have good stable income.

On ILFC. We showed that we sold some planes in the first quarter and keep in mind that ILFC is not just about buying and leasing aircraft, it's about managing the fleet. And up until now, we have not done a very effective job over the last many years of dealing with legacy aircraft. We are now dealing with that. But you’ll see a charge in the first quarter, and we still have a profit at ILFC, but you'll see us throughout the years selling off aircraft. But we still see this business on a normalized basis earning about $600 million. But in that $600 million, we're also assuming about $300 million of impairment or cost related to selling some of the older planes that we have in the inventory. But we also announced that we have a 133 new aircraft we're going to be buying to continue to keep this business strong in the marketplace, as the leader in the marketplace. And we also have approximately, I think, it's seventy four 787 [Boeing 787] done order in their early delivery of 787s. So that also gives us a strong edge there.

We continue to run this business as an investment. We have the debt worked out, we have the future worked out in terms of how we managed the fleet. We've got a strong management team in place now. And to the extent over the next period of time, a year or 2, whatever it is, if we can monetize some of these assets, we're giving that serious considerations. So again, it is not cored AIG but we think we've got it well-run, well-managed and well-positioned in the company.

At United Guaranty. Again, we see that business showing a profit this quarter. Their new model is working extremely well at the front end. They're still maintaining good sales. We see the performance of the new business very strong. They continue to work on claims management, doing effective job there as well. We expect that business to enhance our profitability going forward and not be a drag as it's been in the last couple of years.

So I'm going to turn it over to David now, but just for us, the fact that we have come to unprecedented times, unprecedented vilification of the company sometimes in the press. The team is strong, the morale is high, our momentum is gaining, and so we're pretty confident as we move into 2011, we'll see a stronger and more streamlined and more transparent AIG. So David?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Thanks, Bob, and good morning, everybody. Let's turn to Slide 7. First quarter 2011 net income was $269 million, down from about $1.8 billion a year ago. First quarter, this year, included a pre-tax non-cash charge of $3.3 billion for the accelerated amortization of the prepaid commitment fee relating to the repaying and the terminating of the Fed Reserve Bank of New York's Credit Facility and we did that 2 years early. Importantly, after-tax operating income attributable to AIG, our principal non-GAAP measure, which we believe over time, is the best way to view the businesses. It was over $2 billion for the quarter versus $637 million a year ago. On a per share basis, after-tax operating income was $1.30 for this quarter versus $0.95 a year ago. I'll take you through the EPS in a few minutes because it can be perhaps a little bit counterintuitive, particularly this quarter.

Annualized operating ROE was 10.4% for the quarter and that excludes AOCI. Including AOCI, it was about 9.5% and it was up from about 4% a year ago. Again, there were some noteworthy items that we've highlighted in the first page of the press release.

Let's turn to Slide 8 to look at the consolidated performance. Again, after-tax operating income was a little over $2 billion for the quarter. Chartis had an operating loss of $463 million, after including pre-tax $1.7 billion of catastrophe losses, largely from the Japan earthquake and tsunami.

SunAmerica posted $1.143 billion of operating income in the quarter, up a little over 2% from a very strong quarter a year ago. ILFC had operating income of $117 million for the quarter, compared to a loss of $56 million a year ago. ILFC took, as Bob mentioned, impairment charges of about $113 million for the quarter due largely to some opportunistic sales of about 10 aircraft. The impairment charge in the first quarter of 2010, $430 million. As ILFC manages its fleet and its age -- in the age of the fleet and the composition of the fleet, we would expect to see some impairment charges or possibility losses on opportunistic sales from time-to-time but generally not more than about $300 million a year going forward.

United Guaranty posted a profit of $13 million, driven mainly by favorable prior-year development in the second lien business, which benefited from operational improvements in claims management. In the first lien book, we had favorable trends in newly reported delinquencies and steady trends and the cure rates, but that was more than offset by higher overturns of previously denied or rescinded claims as mortgage lenders and servicers continue to deploy additional resources to address loan documentation issues on their end. The other segment had a profit of about $1.5 billion that was largely driven by about $750 million of appreciation on our ML III interest, driven by increases in value in the underlying multi-sector CDO assets in the portfolio but it was essentially flat the last year. It also includes improvements in the Direct Investment books comprised of our mass investment program and the run-off of the FP asset book, which is mark-to-market and that had about a $500 million gain in it, largely from tightening of credit spreads in the Capital Markets.

Our remaining investment in AIA appreciated almost $1 billion in the quarter, slightly offset by the final monetization of the MetLife position which had been recorded on a mark-to-market basis prior to now.

Let's now turn to Slide 9 and look at after-tax operating income reconciliation. This page shows a reconciliation from the after-tax operating income of about $2 billion, then net income attributable to

AIG of $269 million. The after-tax impact of the $3.3 billion charge on the amortization was about $2.4 billion. The income from discontinued operations was $1.6 billion, largely from the sale of the Star and Edison businesses. We have net realized capital losses for the quarter, mainly from foreign exchange and derivatives, not accounted for under FAS 133.

Finally, we need to adjust for taxes. Since we apply a pro forma tax on our operating income and the items on this page are shown net of tax. In reality, as Bob said, we really are not going to pay much income tax to the U.S. as we have very large deferred tax assets, which I'll talk about in a moment. But and I also would point out that we had a full valuation allowance on those deferred tax assets at this time. I'll take you through a slide or 2 in a few minutes to show you how that works.

Let's turn now to EPS on Slide 10. Earnings per share from continuing operations was a loss of $1.41 in the quarter in '11 versus income per share of $2.16 a year ago. For details of that, I would refer you to Page 5 of our Financial Supplement. Earnings per share from discontinued operations was $1.06 in the quarter versus $0.50 a year ago. Together, we had an EPS loss of $0.35 per share, even though we had net income of $269 million. Because we had 2 items associated with restructuring, filling about $800 million, that gets subtracted from the earnings numerator in the EPS calculation in this quarter, the EPS loss occurs. That charge goes to EPS calculation, not through the income statement. Again, after-tax operating EPS was $1.30 versus $0.95 a year ago.

I should point out that the weighted average shares increased to 1.558 billion shares for the quarter, up from 136 million a year ago, and that was driven by the issuance of 1.655 billion shares in January to the U.S. Treasury as part of our restructuring.

Now let's take a look at our capital structure on Page 11. With the recapitalization that occurred in January, we simplified our capital structure and reduced leverage. Leverage has come down substantially. The senior financial debt total capitalization has decreased from 26% at year end to just under 12% at the end of the quarter. Our book value is currently $47.66 a share and $43.49 ex-AOCI. And again, I want to remind you that excludes any value for the deferred tax asset as we have a full valuation allowance on our DTA.

Now let's turn to Chartis on Slide 13. Chartis reported pre-tax operating loss of $463 million, as I mentioned a moment ago, versus $879 million of income a year ago. The current quarter loss reflects the $1.7 billion cat losses, including about $1.3 billion related to the Japan earthquake and then we had additional $400 million from the New Zealand earthquake, the Australian floods and the U.S. winter storms. Net premiums written were $9.2 billion in the first quarter of 2011, up almost 20% from the $7.6 billion in the first quarter a year ago. And ex-Fuji [ph], and the impact of foreign exchange though, Chartis premiums increased about 6% in the quarter. Catastrophe losses were $1.2 billion higher than a year ago and prior-year development was essentially insignificant in the quarter. The 4 business lines with the largest reserve strengthening at year end showed almost no activity in the first quarter. The combined ratio on an accident-year basis, excluding cats, was 98.7% and it was flat the last year.

The expense ratio improved in part due to impacts from the Fuji acquisition and lower domestic expenses, those were partially offset by some international increases for strategic investments, improving regional governance, risk management and some of the financial infrastructure systems in Solvency II readiness that we're preparing for.

Let's now turn to Slide 14 for a view of the Chartis premiums. Let's really focus on the 6.2% increase during the period, which excludes FX in Fuji. The growth is largely driven by the U.S. region from increased retention and a significant new customer program underwritten in the first quarter, as well as a modest organic growth in almost all of our international regions. Chartis continues to execute on its strategy to grow its higher margin and less capital intensive lines of business, and as required implementing corrective actions on underperforming businesses to ensure that these businesses meet our overall profitability measures. In the first quarter of 2011, the international share of Chartis overall net written premium was 55%, up from 50% a year ago.

Now I'm going to turn quickly to investments and I'm going to start with Chartis on Page 15. Net investment income for Chartis was $1.2 billion in 2011, up 10% from a year ago. The primary driver of the increase was improved investment and partnerships and the effect of consolidating Fuji. Chartis has some excess cash still to be deployed over the coming months and we can talk about that as well as the muni holdings, perhaps in the Q&A session.

Let's now turn to SunAmerica on Page 17. SunAmerica's operating income, as I said a moment ago, was $1.143 billion, up 2% or so, from last year. Premiums, deposits and other considerations reached $6.2 billion in the quarter, up 31.4% which I'll talk about more in a moment. Net investment income was up $47 million, driven by investment partnership returns and the Maiden Lane II residual interest valuation increases. DAC amortization was up about 27%, largely driven by an unlocking in the investment spread assumptions in our group retirement product line as a result of the Federal Reserve rejecting our offer to repurchase the ML II asset portfolio.

As you can see on the chart at the bottom left corner of the slide, SunAmerica's operating income has continued to be strong and stable, posting essentially $1 billion of operating income in the last 5 quarters. The pie chart at the bottom right-hand corner of the slide shows the contribution of each of SunAmerica's businesses to its operating income. These different businesses provide balance and diversification to SunAmerica's earnings.

Let's now turn to Slide 18, premiums, deposits and other considerations. SunAmerica's premiums, deposits and other considerations, as I said a moment ago, increased 31.4% on increased sales of fixed and variable annuities, as well as mutual funds. Life insurance sales increased 17% for the quarter versus a year ago. Western National, while continuing to maintain its pricing discipline, increased sales by almost $1 billion as certain bank partners negotiated lower commissions in exchange for higher crediting rates which made Western National's offerings more attractive to policy holders.

Let's turn to Slide 19. SunAmerica's investment income was up almost 2%, driven mainly by the Maiden Lane II performance, higher private equity hedge fund returns, partially offset by lower base yields. The slow run-off of higher yielding assets will put some pressure on the investment yields going forward, although we've taken actions to reinvest excess cash which should benefit the base rate portfolio in the future.

We still have some substantial cash balances that we will be reinvesting. We've made good progress in April and we'll start to see the impact of that in the second quarter.

On Slide 20. At both VALIC and Western National, net spreads improved. Partnership income and a decrease in the average cost of funds, i.e. our interest crediting rate, more than offset lower base yields and investments.

Now I'm going to turn and pick a quick word or 2 on our taxes, Page 22. As Bob mentioned, we have very substantial deferred tax assets that are available to offset future tax obligations. The slide lays out the gross attributes, the gross assets and a framework for utilizing or realizing those assets. All of the assets, as I said, have a full valuation allowance that offset them. Accordingly, none of these assets are included in our book value. This will become more straightforward as we apply our framework for assessing the need for the valuation allowance in the coming quarters.

And finally, on Page 23. Commencing this quarter, we once again will use a full year estimate of income and taxes to calculate a tax rate like virtually every other company. The last few years, we used a discreet period method because of the uncertainty around our annual results. Because of our tax attributes, we will not be paying very much tax, as I said before. As long as we have a full valuation allowance on the deferred tax assets, we will apply a pro forma-type rate on our operating earnings to show you what the tax rate would be if we were paying or accruing taxes. Because of the impact of the tax remunies, our tax rate on a pro forma basis for operating earnings will be somewhere between 25% and 30% for the year.

Other discrete items in the quarter will impact the overall rate in any given quarter. Items that are presented net of tax are shown using that similar rate. As long as we have a full valuation allowance, virtually all of the tax impacts of the 25% to 30% rate will be reversed before we show net income. And finally, I just want to point out last night in our Q, we included some extended discussion in the Outlook section about our aspirational long-term goals.

With that, I'll turn it back to Bob.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Great. And just before we go to questions, I'd like to reiterate something that David had just pointed out in terms of the DAC unlocking in SunAmerica because of the ML II. We are, in fact, making a very good progress investing that money. Some of the investment is bidding on aspects of ML II. However, we found many other sources. And so approximately, 1/3 of that money has now been invested. Generally, the yields are between 8% and 9%, and we're dealing with fixed, as well as some of the floaters that are part of ML II. So we've made really good progress over the last several weeks dealing with these headwinds, so we're trying to neutralize that effect as we get into the second quarter. And as you look at the results for this quarter, you can see that Chartis still represents about 40% to 45%. It's the ballpark of its percent of operating earnings of the company, and therefore, when we look at the company as a whole, we still believe that some of the parts are left in the whole and the company makes more sense as it is. Combined all of the risk diversification between our Property Casualty business and the Life and Annuity business and other businesses we have. So we're pretty comfortable with the deck we have and just you can see, pretty balanced.

So let me turn it back to Liz and then we'll take questions.

Elizabeth A. Werner
Head of Investor Relations and Vice President
Thank you. Operator, we can open the line for questions at now.

Question and Answer

Operator

[Operator Instructions] We'll turn first to Andrew Kligerman with UBS Securities.

Andrew Kligerman
UBS Investment Bank, Research Division

Two questions. First, read through the aspirational goals that you have going from 6% to 10% and then being able to generate through 2015, roughly $25 billion to $30 billion and today, sitting with the 12% debt-to-capital, I was surprised with the priorities or I'm just wondering with regard to the priorities for 2011, that says, executing one or more primary offerings at AIG common stock. So maybe you could explain some of the rationale behind that, given the earnings power that you've described in your aspirational goals?

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Andrew, you have to keep in mind that in December, when we said we were going to pay back the Federal Reserve and we were going to terminate $30 billion of direct government support, as well as the implied support of the United States government beyond the $30 billion, although some said there will be no more money but there was the implication for sure. To do that and unplugged, and remember, many of you said 2 years ago that AIG was gone and may it rest in peace. And here we are, strong, vibrant and moving forward. However, not everybody kind of believes that yet. And so therefore, we have to oversolve [ph] towards the heat [ph]. And therefore, we have to demonstrate without any question that we have strong credit ratings, both at the insurance companies, and particularly the insurance companies, as well as the holding company. And therefore, we were told, for example, last year that ILFC would never be able to access the unsecured market ever again. The good news is, it never occurred. And we were told that AIG would have a very difficult time accessing the unsecured markets again after what happened. And again, it never happened the second time. However, we had to make sure that we could demonstrate access to the Capital Markets in every form. And therefore, part of the deal to be able to close with the Federal Reserve in and get people comfortable at the rating agencies, we have to raise $3 billion of primary capital and part of that is to give back to the U.S. Treasury its G, the Series G. So this is nothing more than showing that we can raise money, we could do it effectively, and that this company is very, very strong going forward. And as you continue to see throughout 2011, as you've seen in 2010, that the operations of the core businesses continue to be strong. We believe they can begin to manage, probably in the second half of 2012 the amount of equity we require in this company to support the liabilities that we have. So it's really around that philosophy, and we want to make sure we project ourselves as a very strong company that can always live up to its guarantees at this point in time.

Andrew Kligerman
UBS Investment Bank, Research Division

Okay, so Bob, so I should interpret that as sort of required as opposed to something that AIG needs to do, the capital raise there?

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

It's something -- we just need to show that we can do it and to make sure that we had more than enough, but we've gone through a lot of pain. The people and the government that has supported us during this crisis, want to make sure that once AIG goes off on its own, and we are on our own at this stage of the game, that they like us but not that much. And so they don't want to ever have to come back, and they don't want us to leave here in any form crippled in any way that says the government sends us on our way, and we were not financially strong sales. So it's really dealing with those perceptions. We're dealing with it, which is why we say that probably by mid-2012, and that's why we stressed the deferred tax assets and understanding it because that will be a source of funds that allow us to begin to buy back the 80% of the company that was basically taken as part of the requirement together for some to leave us alone. So that's the whole concept.

Andrew Kligerman
UBS Investment Bank, Research Division

Okay, I'm with it. It would be somewhat dilutive but I understand. And just lastly, on the partnership income. So you ended the quarter with about $19.4 billion in that class of asset and a 14% return. What's AIG's objective with that asset class going forward? Do you want to grow that? And what types of returns on average do you think you can do over time?

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Let me turn it over to Bill Dooley.

William N. Dooley
Executive Vice President of Investments

Yes, it's an asset class where we're comfortable where we are right now on. I don't see us growing that substantially. Both insurance companies have allocations to that asset class. The one in SunAmerica, I think, their assets are a little bit more aggressive than the Chartis assets. So we could target somewhere between an 8% and a 6% return on that. So this quarter was much better than that but over a period of time, I mean that's what we're expecting to get on a run rate basis.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Maybe Jay would want to comment from SunAmerica's point of view.

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

Yes, 2 points, Andrew. One is the increase on the balances, especially with respect to SunAmerica, is not so much from allocating new money to that sector. It's from strong appreciation in the fair value over the last 2 years at the markets have done well and this portfolio has done very well. But in terms of what we're targeting, we don't have any plans to increase our holdings of alternatives in SunAmerica as a percentage of our total invested assets much beyond where we are now, and we've always been sort of in the 5-ish percent range. It's not a hard and fast target but again, a lot of the increase is really the appreciation that we've seen in the market as opposed to putting new money to work in the sector in the last couple of years.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Andrew, just keep in mind. I'm sure you know this. That's really about the liabilities as well. So that's all part of the match that goes on.

Andrew Kligerman
UBS Investment Bank, Research Division

Absolutely.

Operator

We'll move to Dan Johnson with Citadel.

Dan Johnson
Citadel Investment Group

A couple of questions if you would. Maybe most importantly, among some of the assumptions that you put in the 10-Q last night was the outlook for Chartis. Maybe you could help us understand a little bit more of the details behind the plan to both bring down the combined ratio while growing the top line. At the same time, maybe you can tell us a little bit about where you think you might be growing, what sort of macro market assumptions are behind those projections. And then I've got a separate question as well, please.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Let me have Peter Hancock -- well, he's new to the role. He's knee-deep in the data. So you've got it, Peter.

Peter Hancock

So the assumptions in the outlook are -- first of all, long-term outlook, it goes out to 2015, but to some extent what we are projecting is a continuation of current trends, which is faster growth in our international business than in our domestic business, faster growth in emerging markets than the international in general, faster growth in specialty lines and faster growth in consumer lines versus commercial lines. All of that is against the backdrop of the significant reduction in premium written in the lines that caused us to strengthen reserves in the fourth quarter. Those 4 lines constituted about 22% of net premium written constituted about in 2006, and that was down to 6.7% in 2010 and under 6% in the first quarter. So we are changing business mix at a macro level. Secondly, we are investing in infrastructure in particular, the global claims initiative. We've invested over $200 million in the global claims initiative, which we expect to help us get our combined down by -- the loss ratio, in particular, down by about 2 points. And third, we have instituted organizational changes in the way we operate, globalizing our product areas and putting individuals in charge, not only of global commercial and global consumer lines, but within them, the sublines, which will move barriers to using common infrastructure, which will help us on the expense ratio. And also, help us allocate our financial capital whether returns are greatest relative to risks. So all of these steps, we think, will achieve the aspirational goals by 2015. And then last but not least, we're investing significantly in technical pricing tools to equip our very experienced team of underwriters with state-of-the-art tools to leverage the data that we have a unique comparative advantage in, which we haven't used to the degree we could have done in the past.

Dan Johnson
Citadel Investment Group

So if I summarize on, at least, on the top line comments that in areas you're looking to grow, you expect to grow well north of the 6%, but there are certain areas that you're shrinking, have been shrinking in and maybe will continue to shrink in, that will bring down the growth areas down to an aggregate mid-single digits. Is that fair?

Peter Hancock

Well, let me put it this way. Our outlook is based on no hardening in the macro environment. Our outlook is premised on no radical increase in interest rates beyond the forward curve. And third, while we have, for planning purposes, a top line assumption and a combined ratio assumption, that's not how we manage the business. We manage the business based on targeting risk-adjusted profitability, which may, depending on the pricing environment and the reaction of customers to our offerings and pricing strategy, that higher or lower top line growth or a different combined depending on the mix of short-tail versus long-tail business. So to some extent, we are moving away from any kind of top line targeting. We think that leaves you to do business at the margin, which is unattractive. So the top line will be what it will be. We think it will grow to about 6% based on our best estimate, but we are really, instead, targeting risk-adjusted profitability.

Dan Johnson
Citadel Investment Group

Understood. Okay. Second question's on the deferred tax asset. I think that's Slide 22. There is discussion about changes to the corporate tax rate. Who knows if anything happens there? But what sort of scenario should we be thinking about that if -- or some say that the top rate come -- the corporate, excuse me, comes down to a mid-20s, and certain loopholes are sort of taken out instead. How should we think about the sort of value of the 3 different buckets you show here if we took corporate rates, say, down into the mid-20s?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Dan, it's David Herzog. I think you understand the levers. Again, since we have a full valuation allowance on it, there won't be any affect on our GAAP book value. And from a utilization standpoint, obviously, the present value of that asset will come down, commensurate with the reduction in the rate. So again, our expectation is that we should be able to utilize, should be able to generate, which then will translate into our framework from an accounting standpoint that we're going to -- that we have a goal to utilize the NOL to certainly, to utilize the foreign tax credits and to utilize the vast majority of the nonlife capital loss carryforwards. What, again, is a bit more challenging to us is in the life capital loss carryforwards. That $8.1 billion asset is a bit more challenging for us because of the presence or the lack thereof of gross attributes, or gross gains that can be used to realize that asset. So again, I think you can understand the lever in terms of what that is. So a reduction in the rate, while it would be helpful in other respects, but from a realization standpoint, it would clearly diminish the value of this.

Dan Johnson
Citadel Investment Group

Yes, I understood. Well, I can come back at a later to understand that.

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Another, I mean, keep in mind, I mean, the other thing is that the tax rate, that our underlying operating companies are all connected to the holding company by way of a tax share agreement. It's been in place for a very long period of time. And so that's still the mechanism by which we're going to monetize these assets.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Can I -- just want to follow-up, permitted on the Chartis comment to reinforce some things about the outlook, in the confidence in the outlook. There's been a lot of talk about the brain train here at AIG. The fact is that's not the case. We've had incredible retention of our employees, and more importantly, we've had incredible retention in the worst of times of our clients. If you think about the fact is that we still have retained almost 92% of our clients during this period of time. We've retained a little over 80% of their policies. Some of the policies, for example, we did lose was D&O coverage. But I will tell you that over the last year and it's continuing to 2011, we're getting that coverage back. We are winning more and more of that. As people have seen that AIG is actually going to be here and they can count on us going forward, and there's no more question about our solvency as a growing concern. So with the fact that just a data point, that of the top 2,000 people that operate AIG today in leadership positions, 57% had been with our company more than 10 years, 20%, more than 20 years. And so we're having a strong experienced, well-established team of leaders around this company that know how to do it and how to do it right. And they are focused. And that's the benefit we have with our clients, because that's what the clients are looking for, the people and the people who can solve their problems. So that energy is here, of that top 2,000 people. Only 3% left for all reasons in 2010. So we've got enormous retention of that group going forward, and that's the group that's gaining this momentum as we move into the first quarter that is producing these results, and that's why we have this strong outlook for the future.

Dan Johnson
Citadel Investment Group

Bob, that's great. While you're there, just on the concept of systemically important financial institutions, what do you think that's going to mean for AIG and when will we know?

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

I have no clue when we'll know. I sort of asked that question a while ago and I got that answer. So I assume that's still the answer. My sense would be that as an insurance company, remember, we are becoming an insurance company and not a trading company. So the aspects that cause the difficulty have been completely derisked, that fee is derisked. And in fact FP today represents maybe $150 million downside and $1.5 billion to $1 billion, upside. So that's all part of what got us in trouble. So my sense would that we will be regulated by the Fed. That's my guess. And my guess is the insurance companies will continue to be regulated by the states and countries we do business in. And I think what the Fed will be looking is predominantly the holding company and making sure that we do the things we need to do to support the enterprise and not taking it in ordinate risk at the holding company level, because clearly, the way we are going to drive our ROE over time is to deal with the fact that we have capital maintenance agreements with our insurance company. So it's a two-way street. So clearly, we got to make sure that we get our RBC to a level that is acceptable for the insurance company and the quality ratings we need. And therefore, we can also, so that it will help us on the immediate, the insurance company levels and because we'll be able to show strength in our ability to move capital around the company in a very effective way. So I think -- my sense is you won't see, but we don't know, we won't see the kind of Tier I capital issues that you see racing in the banking community at this stage of the game. But we'll have to wait and see.

Operator

Next, we'll move to Paul Newsome with Sandler O'Neill.

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

I wanted to ask about insurance pricing for the property-casualty business. AIG has historically been the leader in pricing. We saw some glimmers of hope of party market and commercial. I know you said that your assumption is for no hard market. But could you talk about what you're trying to do, yourself, in terms of pricing?

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Peter, will talk about that.

Peter Hancock

Yes. Well, I think that we, in pricing, are already operating in a competitive market. So we can't do anything, per se, about the market. What we can do is price individual policy to reflect what we think are a fair return on the risk. But the net result of that is, what we observed in the market, is relatively stable in the first quarter. Casualty market, there's been a little bit of increase in some lines [ph]. But the most promising sliver of hope is in property CAT where we've seen, in the U.S., double-digit growth in rates in the last 3 weeks and overseas, even more than that. So encouraging trends there. But overall, I think it's too early to call any kind of turn in the market.

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

And separately, I wanted to ask about -- just to clarify from a cash flow perspective perhaps, is AIG at the point where they're generating cash flow or are you still having to sort of put money down into the subsidiaries? Just wasn't really clear as to whether or not you need the access to capital markets or if at this point, you're as self-sustaining from a cash flow perspective?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Paul, it's David Herzog. I guess, a couple of things. One, as part of our capital management protocol and framework that we've put in place throughout the company, we have instituted capital maintenance agreements between the parent company and the operating companies. And what does that is clarifies and brings transparency to how we think about capital, capital management and it helps really operationalize the diversification benefits of the capital flows within the company. It also helps support a notion, if you will, of strength from above, that we are accumulating a pool of resources at the holding company in order to support the strength and the opportunities down in the operating company. So the long and short of it is, the operating companies are in a position -- and we expect that we will pay dividends from the operating companies out of operating earnings up to the holding company. And so the dividend capacity of these operating companies, as we sit here today, is very significant. So for Chartis, it's in excess of $3 billion and for the SunAmerica companies, about $1.4 billion and the teams, the management teams are all aligned around achieving those dividend flows from the operating companies to the holding companies. And as I said a minute ago, also, in addition to the dividends, importantly, are those tax sharing payments. And so regardless of the rate, there are tax sharing payments that will flow from the operating companies to the holding company, and the holding company will not pay taxes because of our very valuable tax assets. And so that's from an operating cash flow standpoint, and I believe, in the Q, you can see the net flow position of the SunAmerica companies, maybe, Jay, you want to comment on the robust performance in the quarter?

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

Thank you, David. First of all, in terms of a direct answer to where I think was the question from Paul, the SunAmerica Financial Group companies have been net cash generators, I think now, for over a year or so. There is no need for cash being put into the SunAmerica Financial Group companies. And as David mentioned, we're actually in the strong dividend paying position and that's what we started doing already in the fourth quarter of last year. A slightly different topic, though, in terms of the fund flow is, as you can see, in the business, we had a significant improvement in our, not only in our top line premium deposits and other considerations across basically, all of the major product lines, but also the net flows have become much stronger. They're positive and the surrenders remain at or below historic levels. Persistency is very good. So we see continued progress going here and even into the second quarter.

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Jay and Paul, one of the thing I'm going to -- we're going to do this in 2 parts with respect to Chartis. We put in the quarter, put down about $3.7 billion and that was really in 2 pieces and I'll take the first piece and I'll ask our CFO for Chartis, Rob Schimek to comment on the second piece. But there were 2 pieces. The $2 billion piece, Schimek will talk about and I'll take the $1.7 billion. What we did, Paul, with respect to the ownership structure inside the company of the United Guaranty companies, our mortgage guaranty company. Effectively what we did was injected capital and took a dividend or distribution, if you will, out of the operating company that owned United Guaranty. So think of it as a replacement capital. Cash went it. United Guaranty, which was a capital came out. And that capital, the cash that was in the Chartis companies has been redeployed into appropriate assets for the various insurance companies. So that was $1.7 billion. Effectively, the cash went in, came back out and we had other assets in other parts of the company that we were able to redeploy, get the assets into Chartis. So Rob, you want to? Yes, Peter, go ahead.

Peter Hancock

So just to be clear. Prior to this, UGC was owned by Chartis. After this, UGC is now owned by AIG holding companies. So that's what that maneuver achieved.

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

And it's Rob Schimek. The primary motivator there is that as a subsidiary of Chartis, UGC was not a capital-efficient structure, so obviously, putting it up with the parent company rather than having it down in Chartis is more efficient overall from capital perspective for Chartis. The second element of the capital that was infused into Chartis, as David referred to, was about $2 billion of additional cash that was put into Chartis. That was put in following our reserve strengthening at year end. Obviously, the strengthening reduced the surplus inside of the Chartis companies but also importantly, increased the risk-based capital of charge, for example, that the new reserves we've added are trapped [ph]. And so therefore, there were 2 adverse effects on the RBC ratio. One, reduced surplus and two, higher levels of capital charges, so the new capital that AIG put into the structure or into Chartis, ultimately provided us with a benefit of getting our RBC back to what we feel is a comfortable level.

Operator

Next, we'll move to Scott Frost with Bank of America Merrill Lynch.

R. Scott Frost
BofA Merrill Lynch, Research Division

Thanks for the clarification on the tax rate. Could you remind me what is again the timetable or I guess restrictions on any kind of monetizing of the AIA or the Maiden Lane III interests? And is it fair or accurate to say that the DTA could or would be used to offset any taxes on a sale? And I have a follow-up.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Yes, I think, philosophically right now, AIA is part of the SPV with treasury, and we can monetize that later this year. But part of the issue we're thinking about is strategically, how we want to handle that asset. Right now, it's part of AIG. We have other alternatives we're considering to be deal with the SPV. And so a value principal would be that to the extent we could retain our ownership in this fast-growing market, we sold off 2/3. That doesn't mean we want to eliminate all of it, but that depends on how we deal with the SPV. So clearly, we're working hard on Nan Shan to make sure that closes and that's $2 billion would come in. And we're looking, potentially, of monetizing other assets that we have so that AIA might be solved much later on if at all.

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

And Scott, with respect to the DTA, it would offset to the extent there's a gain. It would help us utilize that tax asset.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Do you want to also to comment on the monetization of cash flows coming out of Maiden Lane III and how that shows up?

David Lawrence Herzog
Former Chief Financial Officer and Executive Vice President

Scott, the value of ML III is carried on our books, as I think, you probably are aware of as a mark-to-market assets. So inside the Maiden Lane III, SPV, so to speak, are the remaining CDO investments that were acquired back in November of 2008. The cash flow estimates inside that portfolio are upwards of about $45 billion of nominal cash flows. Also when you apply those cash flows over the long period of time, the waterfall is such that the Federal Reserve Bank of New York has a first priority of senior note that gets paid off at year end. That was about $17 billion. Then next in line, so to speak, is obviously their interest carry on it is their first and then, our $5 billion of the principal that we had invested and then, our taking fee, so to speak, gets paid next. And then, we share the upside 1/3, 2/3. So again the cash flow is on ML III, likely won't emerge for quite some time given the presence of the large senior note position. But nonetheless, there's still significant value inside the Maiden Lane III SPV.

R. Scott Frost
BofA Merrill Lynch, Research Division

Okay. And if I could ask you a question about the FP breakout. The way I'm reading it is you've got $278 billion total notional, $38 billion mez, up and $19 billion CDO squared, is that the right -- and then rest of it -- And then $221 billion will be the reg cap portfolio, is that right? I think it's in the back of the supplement, like Page 37. But what I wanted to ask you is do you have any sense of -- I mean, I know the portfolio has been derisked as much as you can derisk it. But with respect to Basel III, do you have any view as to whether or not that would or wouldn't give banks there a further incentive to unwind? Is that something that's contemplated or do you have any views on that?

Peter Hancock

I'll take that if you like. I don't think Basel III has a material impact on our unwind strategy. I think that banks have had an outlook on Basel III over the last year and half. And both, ourselves and counterparties, have had every motivation to unwind and simplify this portfolio. We're getting close to the point where what's left represent, as Bob says, very modest downside, and we estimate about $150 million P&L downside and about 10x that in terms of upside. But some liquidity risk against it but the contingent liquidity risk is embedded in our stressed [indiscernible] and more than adequately covered by the liquidity cushion that we have as a holding company. So I think, you can think of this as a runoff portfolio that will amortize, often throw of some decent returns but not recurring income. It the one-off windfall.

R. Scott Frost
BofA Merrill Lynch, Research Division

Okay. And that last question. For the nonreg cap portfolio is there any sort of amortization schedule that you've put anywhere? I didn't see one but I may have missed it, but do we have any ideas to how that kind of eventually runs off, the nonreg cap part?

William N. Dooley
Executive Vice President of Investments

Well, this -- this is Bill Dooley, sorry. They all have final maturity dates. So it's going to take a while for this to roll off. But because of our valuation on those on a future value basis, we think we're going to capture the income on these positions.

Peter Hancock

The deploys, we have not disclosed the amortization schedule.

William N. Dooley
Executive Vice President of Investments

That's correct. Right. But you just need to have termination at some point.

Elizabeth A. Werner
Head of Investor Relations and Vice President

Operator, we're going to take our last question now and finish it up. Anyone left in queue, we'll be sure to call you immediately following the call.

Operator

We'll take that question from Eric Berg of RBC Capital Markets.

Eric Berg
Lehman Brothers

Maybe. Jay or David, or whoever you deem appropriate. One of the unfortunate developments in the current quarter is that the stock market has given up quite a bit of its early gains and interest rates have fallen. I was just taking a look pretty steeply both on the long end and the short end of the yield curve. So my question is just how is all this going to affect -- I have 2 questions. How is this going to affect SunAmerica, especially on the interest rate side? And secondly, while I certainly heard Jay's comments about you're not increasing your investments or you have no intention to substantially increase your investments and partnerships, what is the near-term outlook for partnership income? Would you expect it to continue to be as strong in the June quarter or if not as strong, stronger than your baseline expectations in the June quarter than it was in the March quarter?

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Jay, you're up.

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

A couple of comments. First of all, in the quarter, not that I follow these things closely, I think the market, the equity market is still substantially up for the quarter even after the most recent selloff. Interest rates, you're correct. Number two, the most equity-sensitive part of the investment portfolio in SunAmerica Financial Group are the alternatives. The hedge fund results are recorded on a one-month lag. So really, the second quarter for us would be the month of March, April and May as you take a look at sort of the aggregate result there. I don't -- at this point in time and definitely not predicting, but I'm not expecting any big issues with alternative investment income based on the results we've seen for March and early results for April, but there's still May to complete. And private equity, it's just too early to tell. It's basically dependent on distributions from funds, completion of liquidity events and so on and so forth. On the rates, the interest rate's moving down, will have some impact on the fair value of the liabilities associated with VA guarantees. But our hedging program is designed to address that on an economic basis as far as the volatility that flows through the GAAP P&L, again, too early to estimate that. But again, at this point in time, I don't see the market action as having a dramatic impact on results at this point in time for SunAmerica. I should say that all of these activity has not slowed down the good momentum that was displayed on the top line in the first quarter, and we continue to see good progress moving in the second quarter thus far.

Eric Berg
Lehman Brothers

Yes. When you said just one quick last one, when you say that you don't expect major developments on the alternatives, what do you mean by -- are you saying in effect that your expected continuation of sort of what you saw in the first quarter is that what you mean?

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

No. Actually, not really going to comment on the -- predict the results of portfolios large and diverse as ours. Just saying that if you look at the change in value of the pick of the S&P 500 and assume that the quarter starts on March 1 up to today, I think you had positive results to today and I think that probably will be helpful on balance of the portfolio. For planning purposes, we expect the SunAmerica Financial Group alternative investment portfolio to return approximately 10%. The results, as you know, are very lumpy. We have achieved, over performed on the 10% over a long period of time. Certainly, the first quarter is an example of that. We aren't planning for those kinds of returns. I think the first quarter yield was roughly 16.5% in the SunAmerica portfolio. But for planning purposes at 10%, but the market will the dictate that, and we will call it out in the financial supplement as we do every quarter. You can take that into account as the way you look at the model of the company.

Elizabeth A. Werner
Head of Investor Relations and Vice President

Thank you, operator. At this time, we'd like to conclude our call. Thank you for joining us, and we look forward to speaking with you in the future.

Robert Herman Benmosche
Former Chief Executive Officer, President and Director

Thank you all very much.

Operator
And with that, we'll conclude today's conference. Thank you, everyone, for joining us today.