Operator

Greetings, and welcome to Ambac Financial Group, Inc. First Quarter 2022 Earnings Call. (Operator Instructions) As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host, Charles Sebaski, Head of Investor Relations; Claude LeBlanc, Chief Executive Officer; and David Trick, Chief Financial Officer. I will now turn the conference over to Charles. Please go ahead, sir.

Charles Sebaski – Managing Director, Head of Investor Relations

Thank you. Good morning, and thank you all for joining today's conference call to discuss Ambac Financial Group's first quarter 2022 financial results.

We'd like to remind you that today's presentation may contain forward-looking statements about our business, including, but not limited to, new business, credit outlooks, market conditions, credit spreads, financial ratings, loss reserves, loss mitigation, loss recoveries, investment returns or other items that may affect our future results. These statements 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 of events. Actual performance and events may differ, possibly materially, from such forward-looking statements.

Factors that could cause this include the factors described in our most recent SEC-filed quarterly or annual report under Management's Discussion and Analysis of Financial Conditions and Results of Operation and under Risk Factors. Ambac is not under any obligation and expressly disclaims any obligation to update any forward-looking statement whether as a result of new information, future events or otherwise.

Today's presentation contains non-GAAP financial measures. The reconciliations of such measures to the most comparable GAAP figures are included in our earnings press release, which is available on our website at ambac.com.

Please note that presentations have been posted to the Events and Presentations section of our IR website which support our comments today.

I would now like to turn the call over to Mr. Claude LeBlanc.

Claude LeBlanc – President and Chief Executive Officer

Thank you, Chuck, and welcome to everyone joining today's call.

For the quarter ending March 31, 2022, Ambac reported net profit of $2 million, or $0.04 per diluted share, and adjusted earnings of $14 million or $0.30 per diluted share. In addition, this quarter we announced a share buyback program which began in April and, to date, we have repurchased over 1.5 million shares for just over $13 million dollars, or an average price of $8.78/share. Yesterday we announced the addition of $15 million to our share repurchase program, bringing the total unused authorized amount to $21.8 million.

David will discuss our results in more detail shortly.

As previously shared with investors, 2021 was a transition year for Ambac as we launched our Specialty P&C insurance business and progressed our strategy to become a growth-oriented company. Our results for the first quarter of 2022 for our specialty P&C insurance platform are a clear reflection of our early successes, which are very encouraging.

We experienced growth across both our Specialty P&C participatory fronting and Insurance Distribution businesses, with total specialty P&C insurance production of nearly $70 million, representing a 71% increase from the first quarter of last year.

This growth is being driven by the scaling and expansion of our new businesses, further supported by the favorable market conditions and the progressing secular shifts in the insurance market. As it relates to market conditions, we have continued to see rate increases at moderating pace in most lines of business, a dynamic which supports the continued growth of the rapidly evolving program and fronting markets in the U.S. The MGA market is estimated to be generating between $60 and $65 billion of premium annually, having doubled over the last decade, fueling the growth of the fronting market, which grew by nearly 53% year over year in 2021. This is a trend we anticipate will continue in the coming years, subject to market conditions.

For the first time this quarter, in addition to our traditional consolidated reporting, we are now providing segment reporting on our two growing operating businesses:

- Everspan Group, which we will report in our Specialty P&C insurance segment, and
- Cirrata Group, which we will report in our Insurance Distribution segment

Our Specialty P&C insurance business, Everspan Group, was launched in the second quarter of 2021, and our strategy from the beginning was to differentiate our business model from other fronting businesses. A key component of this differentiation is our ability and willingness to retain up to 30% of underwriting risk, which creates significant alignment of interest with Everspan's reinsurance partners. This distinction further expands our ability to differentiate Everspan as a leading solutions and service market for our valued program administrators.

In the first quarter of 2022 this strategy has been successful in generating $24 million in gross premium written across the 10 programs launched over the last year, including 3 this quarter, representing a run-rate of approximately $100 million, which we expect to grow in consecutive quarters, with a strong pipeline of prospective programs going into the second quarter.

Our leadership team at Everspan is represented by industry executives with proven track records in all key aspects of our business model—underwriting, actuarial and claims.

Turning to our distribution business, our Insurance Distribution segment, led by Xchange, our first MGU partner, is profitable and growing, having placed over $45 million in premiums for the first quarter of 2022, an increase of nearly 13% over the prior year, which represents a record quarter for the company. Going forward, we expect the company will continue to successfully expand its business and distribution network, both organically as well as through select strategic transactions.

Recently we announced that Xchange entered into a renewal rights transaction for a $13 million portfolio of Employer Stop Loss (or "ESL") business. The transaction was self-funded, is expected to be immediately accretive to earnings and is anticipated to expand Xchange's ESL premiums by over 15%. As importantly, we believe this transaction will open up new distribution relationships nationally in Xchange's core ESL business.

Overall, we are very pleased with the progress each of our P&C insurance businesses has shown this quarter and we believe we are well positioned for continued growth, both organically and through strategic transactions, in 2022.

Turning now to our Legacy Financial Guarantee business, during the quarter we had two significant developments at AAC. As previously announced, the Plan of Adjustment in Puerto Rico, which related to our GO and PBA exposures, was finalized on March 15th. This facilitated a reduction to our Puerto Rico insured principal and interest exposure by $450 million, and since the end of the quarter we have further

reduced our Puerto Rico exposure by $716 million, eliminating all of our remaining PRIFA and CCDA exposures. As a result, as of today, our only remaining insured Puerto Rico exposure is to HTA and our residual exposure to COFINA.

These transactions collectively represent a 49% reduction in our remaining Puerto Rico exposure, which led to Ambac's recognized gain of $198 million in the quarter.

As it relates to our remaining HTA exposure in Puerto Rico, the HTA Plan of Adjustment was filed on May 2nd and we expect that it will be confirmed and become effective before the end of the year. However, until the Title III process is concluded for HTA, some uncertainty still exists around the final outcome.

Looking at the balance of our portfolios, we continue to reduce risk in the insured portfolio through active de-risking and natural portfolio run-off. Net par exposure was $27 billion at March 31, down nearly $1 billion or 4% from December 31, 2021.

Ambac's watchlist and adversely classified credits were reduced to $9.6 billion at March 31st, down approximately $0.6 billion, or 6% from the prior year end.

Overall, Ambac has removed a material amount of uncertainty from its legacy insured portfolios over the last couple of quarters. Absent new material developments in the insured portfolios, we would anticipate this to result in lower future loss volatility.

The other significant development at AAC during the quarter related to a New York Court of Appeals ruling in an unrelated RMBS litigation known as "HEAT". While this decision did not involve any of our RMBS cases, the decision in the Court of Appeals limits damage recoveries for one of our various paths to recovery in certain of our RMBS cases. As a result of this change in law AAC reduced its rep & warranty subrogation recoverable by ($186) million. Changes in discount rates and underlying insured RMBS transaction performance contributed an additional $38 million to the overall reduction of the recoverable.

As it relates to our RMBS loss recovery efforts, we are actively pursuing all claims in our rep & warranty litigations, and in our main case against Bank of America/Countrywide we are preparing for trial and look forward to resolving our claims as favorably and as expeditiously as possible. As more fully described in letters filed with the court on March 24th and March 28th by our outside counsel, Ambac has multiple paths in that case to recover our claims payments in addition to significant pre-judgment interest, which began accruing more than 10 years ago. Furthermore, we believe that HEAT does not impact our two primary paths to full recovery: (i) Discovery and (ii) Reimbursement, neither of which was addressed by HEAT.

At trial, Ambac intends to prove the following:

First, in light of the recent HEAT decision, through multiple paths, we intend to prove that Countrywide discovered the breaches without the need for notice. We have been preparing the Discovery case against Countrywide for years and have always planned to prove Discovery along with our noticed breach approach at trial.

Ambac's Discovery case is also unique in the RMBS space given that Countrywide originated approximately 85% of the loans in the transactions at issue in the case, meaning that Countrywide employees reviewed every application for every loan that Countrywide originated. Countrywide's role as originator of most of the loans at issue in the litigation makes our case markedly different from other outstanding RMBS litigations. Countrywide also discovered breaches through its role as sponsor of each securitization transaction and as servicer of the loans. As such, Countrywide discovered breaches of reps and warranties without the need for any notice.

Second, Ambac has a separate Reimbursement claim under its Insurance and Indemnity Agreements with Countrywide. As an insurer, Ambac has an extra form of protection through contractual rights and remedies provided in these agreements. An appellate court has already held that the sole remedy repurchase protocol, which is what was at issue in HEAT, does not apply in our Reimbursement claim. Other RMBS plaintiffs, like trustees, do not have this kind of alternative path to recovery.

Third, we intend to prove that Countrywide prevented Ambac from providing additional notices by failing to timely provide Ambac with loan files and other materials in its possession. We also intend to prove the futility of providing further notices. Countrywide refused to repurchase all but a small number of defective loans that Ambac noticed, even those that its own internal fraud and quality control divisions acknowledged to be defective.

With respect to other cases, we are making progress on our fraud-only case against Countrywide and our cases against First Franklin and Nomura, which we hope to progress to trial as early as next year. To dimensionlize our damages, as we look across all cases against RMBS sponsors, in Countrywide we are seeking damages of well over $2 billion and in our other cases – First Franklin, our fraud-only case against Countrywide, and Nomura - we are seeking aggregate damages of more than $1 billion. We have confidence in our claims and intend to vigorously pursue them to fair and final resolution.

As a reminder… the recoverable on our balance sheet for our breach-of-contract cases does not include pre-judgment interest or any recovery from our fraud-only claims, both of which could be material.

I will now turn the call over to David to discuss our financial results for the quarter. David?

David Trick – Chief Financial Officer

Thank you, Claude, and good morning, everyone.

Before I discuss our first quarter results, I'd like to emphasize two changes we made to the presentation of our financial results this quarter. First, our results are being presented on a year-over-year basis rather than on a sequential basis, our former presentation method. Secondly, we have begun disclosing our results through three segments: Legacy Financial Guarantee insurance, Specialty Property and Casualty insurance and Insurance Distribution. Both of these changes are a result of the continued growth and expansion of our new businesses relative to the continued run-off of the Legacy Financial Guarantee business.

For the first quarter of 2022, Ambac reported net income of $2 million, or $0.04 per diluted share, compared to net income of $17 million, or $0.08 per diluted share, in the first quarter of 2021. Adjusted earnings for the first quarter were $14 million, or $0.30 per diluted share, compared to adjusted earnings of $41 million, or $0.59 per diluted share in the first quarter of 2021.

The difference between adjusted earnings and GAAP net income for the first quarter of 2022 related mostly to the exclusion of $14 million of insurance intangible amortization from adjusted income.

The reduction in net income for the first quarter 2022, as compared to the first quarter 2021, was primarily caused by the $33 million gain on extinguishment of debt in the first quarter of 2021 related to the junior surplus note exchange transactions.

Other notable variances relative to the prior period include higher loss and loss expenses and lower investment income, offset by higher gains from interest rate derivatives and higher VIE gains.

As part of our new segment disclosure, and as Claude referenced, we are now reporting several new metrics, including "P&C insurance production." P&C insurance production is a combination of both gross premiums written at Everspan and premiums placed through our Insurance Distribution segment. P&C production is a proxy for the basis upon which program fees, earned premium and gross commission income will be generated.

Gross premium written at Everspan was $24 million in the first quarter compared to a di minimus amount in the first quarter of 2021 and up over three times from the $7 million written in the fourth quarter of 2021. Premiums placed in the Distribution business totaled $45 million in the first quarter compared to $40 million in the first quarter of 2021, an increase of 12%.

Taken together, P&C insurance production was $69 million in the first quarter, up 71% over the first quarter of 2021 and over two times the production of last quarter. First quarter is seasonally the largest quarter of the year for the Insurance Distribution business.

Premiums earned were $15 million in the first quarter compared to $14 million in the first quarter of 2021. Financial Guarantee earned premiums continue to trend downward as a result of our active de-risking efforts and organic run-off of the insured portfolio.

Everspan's contribution to net earned premium, although modest, was just over $1 million for the quarter as compared to nil for the prior period and over double the prior quarter. In addition, we would highlight that of the $24 million of gross written premiums in the quarter, Everspan retained $5 million of net written premium, which will earn in over the next year.

Everspan also collected $1 million of program fees, approximately a quarter of which were earned in the first quarter and the remainder of which will also earn in over the year. As Everspan continues to add programs, and as each program grows gross premiums written, we would expect to see both earned premium and program fees grow exponentially.

Our Distribution segment also continues to grow; as previously noted $45 million of premiums were placed in the quarter, a 12% increase from the $40 million placed last year. Insurance Distribution business revenue comes from commissions earned based off the amount of premium it places. And for the first quarter gross commissions were $9 million, up 19% from $7 million in the prior year period.

The Insurance Distribution segment produced $2.7 million of EBTIDA for the first quarter, up almost 13% over the first quarter 2021.

Investment income for the first quarter was $5 million, down from $49 million in the first quarter of 2021.

The decrease in investment income during the first quarter was related to three items. First, pooled fund investments generated a net gain of about $1 million in the quarter compared to $28 million in the first quarter of 2021. Given market conditions, we believe our pooled funds performed well in the quarter. This compares to extraordinary pooled fund performance in the first quarter of 2021 at approximately 4.6% or a 20% annualized rate. Secondly, we incurred a $9 million loss on Puerto Rico plan consideration classified as trading, which represented a small component of our large overall gain from the Puerto Rio restructuring in the quarter. Thirdly, we lost $7 million of income as a result of the refinancing of Ambac LSNI notes, a large portion of which we owned in the investment portfolio. However, interest expense was also down by a similar and offsetting amount year over year.

During the first quarter we also recorded realized gains of $9 million from a class action litigation recovery related to RMBS bonds we formerly owned in the Legacy Financial Guarantee segment investment portfolios.

Loss and loss expenses were $24 million in the first quarter 2022 compared to $8 million in the first quarter 2021. Public Finance experienced $(190) million of positive development in the first quarter compared to a $9 million loss in the prior year, all of which was driven by Puerto Rico.

Future development of our Puerto Rico loss reserves, which now solely relate to our HTA exposure, will be influenced by many factors, including the confirmation and consummation of the HTA plan, our ability to execute risk mitigation opportunities, timing, the value and liquidity of new bonds and CVI subrogation

related to HTA, as well as a number of other factors. While future development in our Puerto Rico reserves may occur, we do not currently anticipate such development to be significantly material.

The structured finance portfolio generated a loss and loss expense of $213 million this quarter compared to a benefit of $8 million in the first quarter of last year. This change resulted primarily from a $224 million reduction to our rep & warranty credit, $186 million of which was the direct result of the previously mentioned New York Court of Appeals decision. In addition there was a $27 million reduction related to an increase in discount rates and $11 million related to a reduction in underlying transaction losses.

Net gains on derivative contracts, which are positioned as a partial economic hedge against interest rate exposure in the Financial Guarantee and investment portfolios, were $57 million for the first quarter, compared to gains of $25 million for the first quarter 2021. The interest rate derivative portfolio is designed to benefit from rising rates as a partial economic hedge against rate exposure in Ambac's Financial Guarantee insured and investment portfolios.

Operating expenses were $34 million, up from $33 million in the first quarter. The slight increase in operating expenses for the first quarter was due to higher defensive legal expenses in the Legacy Financial Guarantee segment; higher headcount and other expenses associated with building and growing our new businesses; and growth-related sub-producer commissions in the Insurance Distribution segment; partially offset by lower corporate consulting and advisory fees.

Turning to the balance sheet, shareholder's equity decreased $2.77 per share to $19.65 per share, or $0.9 billion at March 31, 2022 from year-end 2021. The decrease was due to net unrealized losses on investments of $105 million and $23 million of foreign currency translation losses.

Adjusted Book Value decreased to $841 million or $18.07 per share at March 31, 2022, from $874 million or $18.88 per share at December 31, 2021. This $0.81 per share decrease was primarily due to foreign currency translation losses and the impact of higher risk-free rates used to discount economic future installment premiums.

At March 31, 2022, AFG, on a stand-alone basis, excluding investments in subsidiaries, had cash, investments and net receivables of approximately $243 million, or $5.22 per share, including approximately $118 million of liquid assets.

I will now turn the call back to Claude for some brief closing remarks.

Claude LeBlanc – President and Chief Executive Officer

In conclusion, we are excited by the material progress and growth we have seen in our specialty P&C insurance platform as the fronting and MGA markets continue to show strong growth and profitability.

We continue to see attractive opportunities to deploy capital in our Insurance Distribution business in order to grow organically and through strategic transactions. We also see meaningful opportunities to capture growth and expense synergies across our growing businesses through our dedicated business services unit supporting the existing and future technology, distribution and infrastructure needs of our distribution partners.

We will also continue our focused de-risking and loss recovery efforts in key areas of our Legacy Financial Guarantee companies and, at the appropriate time, will explore strategic options for this business, with the goal of maximizing value for our shareholders.

As we continue the transition and expansion of our P&C platform, we believe the company’s value will be increasingly driven by the individual segments, and therefore aligned with our strategic focus on the Specialty P&C insurance and Distribution businesses. These new businesses are characterized by capital light models, EBITDA managed and growth focused. Accordingly, we believe the framework for evaluating our new business, and for Ambac as a whole, will need to include such new metrics, separate

and distinct from our Legacy Financial Guarantee business, which today is capital intensive and event driven. We further believe the assessment of value for each underlying segment in addition to our holding company capital better reflects the value of our enterprise. We look forward to continuing to update you on our progress in the coming quarters.

Operator, please open the call for questions.

Operator

Thank you, gentleman. We are now conducting a question and answer session. (Operator Instructions)

We have our first question from the line of David Belport of Wells Fargo Advisors, please go ahead.

David Belport – Wells Fargo Advisors

Yes. Good morning. I have a question regarding the warrants that expire April 30, 2023. Has there been any talk or discussion as far as extending the warrant time with regard to the potential for a delay in the, in the trial? Obviously these are 10-year warrants, and just wondering whether there is any possibility of extending those warrants, and I believe there should be. Thank you.

David Trick – Chief Financial Officer

Hi, thanks for the question. No, honestly, we have not had that discussion. But thank you for the feedback. We will certainly take it under consideration and provide you with any appropriate feedback once we've had an opportunity to review your question.

David Belport – Wells Fargo Advisors

Okay. Thank you.

Operator

Thank you. (Operator Instructions) Your next question from Sean Farinaccio with Rosen Equities. Please go ahead.

Sean Farinaccio – Rosen Equities LLC

Hi, good morning. Thanks for letting me ask a question. I was encouraged by some of the language in the press release about trying to see some of these litigation claims pursued to ultimate judication given the long timeline here. I actually followed Ambac back in 2007, 2008 when some of this stuff was kind of incepted, and I saw some of the conduct that went on with some of the originators and securitizers, so I'm very interested to seeing you guys being able to put some of that into trial. So, I appreciate that. And I'm interested to know, do you think that there's the potential for the trials to be delayed if we need some time to figure out a new mechanism to kind of judge how to gauge how many of these loans need to have, how we basically re-underwrite these loans, like, based on the ruling of the DLJ case?

Claude LeBlanc – President and Chief Executive Officer

Thanks for your question, Sean. As we described in our letter to Justice Reed on March 28th –which we reference is available on the court sites and we will have it available on our investor section of our website as well—we believe that the HEAT US Bank decision should not have any impact on the timing of our trial or the scope of our trial. And we believe that we should be able to proceed to trial as scheduled in September. It’s impossible to tell if other issues or other cases develop in other directions. But as we've explained extensively in my prior remarks, and in the letter, our case is very uniquely positioned and differentiated in the market, which is also why we believe there's a clear path to trial in September.

Sean Farinaccio – Rosen Equities LLC

Makes a lot of sense to me. I actually read that letter and it was good to kind of see articulated some of the ways that you're in a different situation relative to the trustee and have some different differentiating factors in terms of your rights and contractual aspects of the case. I was also encouraged that you guys came back into the market, buying stock. I think that's also very important that you've illustrated that some of the parts of valuation the company here, barely scratch any value to event-driven potential proceeds or value that could be ascribed to AFG from AAC in the medium- to long-term. And I also like that you reupped the buyback in the last few days.

And I'm wondering…let's say, over the course of the year, if you continue to get distributions from the Specialty P&C businesses, do you think that there's scope to even add more to that buyback if prices remain compelling later on in the year?

David Trick – Chief Financial Officer

Thanks. You know it's something we will take into consideration. Stock buyback is something that we evaluate on a regular basis and try to weigh— liquidity versus opportunity to market, buy the stock where we can be opportunistic versus capital deployment in new business opportunities. So, it's a recurring and evolving evaluation of capital deployment and, certainly, it's one we'll continue to evaluate as weeks and months go by here. And we'll see where we come out on the current authorization and where our opportunities to deploy capital are throughout the course of the year. So, that's something we continue to and will regularly continue to evaluate.

Sean Farinaccio – Rosen Equities, LLC

Well, I'll just endorse the thinking to this point, strongly. So I appreciate the color and thanks for your time guys.

David Trick – Chief Financial Officer

Appreciate it. Thank you.

Operator

Thank you. There are no further questions at this time. This concludes today's conference. Thank you for your participation. You may disconnect your line at this time.