

ASSURED GUARANTY LTD
Form S-1/A
May 12, 2004

[QuickLinks](#) -- Click here to rapidly navigate through this document

As filed with the Securities and Exchange Commission on May 12, 2004.

Registration No. 333-115173

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

AMENDMENT NO. 1

to

FORM S-1

REGISTRATION STATEMENT

UNDER

THE SECURITIES ACT OF 1933

Assured Guaranty Ltd.

(Exact name of Registrant as specified in its charter)

Bermuda

(State or other jurisdiction of
incorporation or organization)

**30 Woodbourne Avenue
Hamilton HM08 Bermuda
Telephone: (441) 296-4004**

(Address, including zip code, and telephone number,
including area code, of Registrant's principal executive offices)

6351

(Primary Standard Industrial
Classification Code Number)

Not Applicable

(I.R.S. Employer
Identification No.)

**CT Corporation System
111 Eighth Avenue, 13th Floor
New York, New York 10011**

(Name, address, including zip code, and telephone number,
including area code, of agent for service)

Assured Guaranty US Holdings Inc.

(Exact name of Registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

**1325 Avenue of the Americas
New York, New York 10019
Telephone: (212) 974-0100**

(Address, including zip code, and telephone number,
including area code, of Registrant's principal executive offices)

6351

(Primary Standard Industrial
Classification Code Number)

Applied For

(I.R.S. Employer
Identification No.)

**Geraldine Egler
Assured Guaranty Corp.
1325 Avenue of the Americas
New York, New York 10019
Telephone: (212) 974-0100**

(Name, address, including zip code, and telephone number, including
area code, of agent for service)

Copies to:

James M. Michener

Assured Guaranty Ltd.
30 Woodbourne Avenue
Hamilton HM08 Bermuda
(441) 296-4004

Edward S. Best

Mayer, Brown, Rowe & Maw LLP
190 South LaSalle Street
Chicago, Illinois 60603
(312) 782-0600

Michael Groll

LeBoeuf, Lamb, Greene & MacRae, L.L.P.
125 West 55th Street
New York, NY 10019-5389
(212) 424-8000

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

Approximate date of commencement of the proposed sale of the securities to the public: As soon as practicable after the Registration Statement becomes effective.

If any of the securities being registered on this form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box.

If this form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If delivery of the prospectus is expected to be made pursuant to Rule 434, check the following box.

The Registrants hereby amend this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrants shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, or until the Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

The information in this prospectus is not complete and may be changed. These securities may not be sold until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell nor does it seek any offer to buy these securities in any jurisdiction where the offer or sale is not permitted.

SUBJECT TO COMPLETION, DATED MAY 12, 2004.

\$200,000,000
Assured Guaranty US Holdings Inc.
% Senior Notes due
Fully and Unconditionally Guaranteed by
Assured Guaranty Ltd.

The notes will be issued by Assured Guaranty US Holdings Inc., or the issuer. The notes will bear interest at the rate of % per year. Interest on the notes is payable on and of each year, beginning on , 2004. The notes will mature on , . The issuer may redeem some or all of the notes at any time at the redemption price discussed under the caption "Description of Notes and Guarantees - Optional Redemption." In addition, the issuer may redeem all of the notes under the circumstances described under "Description of Notes and Guarantees - Redemption for Changes in Withholding Taxes." The notes will be fully and unconditionally guaranteed by Assured Guaranty Ltd., or the guarantor, the parent corporation of the issuer.

The notes will be unsecured senior obligations of the issuer and will rank equally with all other unsecured senior indebtedness of the issuer from time to time outstanding. The guarantees will be unsecured senior obligations of the guarantor and will rank equally with all other unsecured senior indebtedness of the guarantor from time to time outstanding.

Investing in the notes involves risks. See "Risk Factors" beginning on page 12.

	Per Note	Total
Public offering price (1)	%	\$
Underwriting discount	%	\$
Proceeds, before expenses, to the issuer	%	\$

(1) Plus accrued interest from , 2004, if settlement occurs after that date.

The Securities and Exchange Commission, state securities regulators, the Minister of Finance and the Registrar of Companies in Bermuda and the Bermuda Monetary Authority have not approved or disapproved of these securities, or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The underwriters expect to deliver the notes to purchasers in book-entry form only through the facilities of The Depository Trust Company on or about , 2004.

Banc of America Securities LLC

JPMorgan

The date of this prospectus is , 2004.

Table of Contents

Prospectus Summary	1
Risk Factors	13
Forward-Looking Statements	26
Formation Transactions	27
Assured Guaranty US Holdings Inc.	28
Use of Proceeds	28
Capitalization of Assured Guaranty	29
Selected Combined Financial Information	30
Pro Forma Combined Financial Information of Assured Guaranty	32
Management's Discussion and Analysis of Financial Condition and Results of Operations	33
Business	65
Management	103
Beneficial Ownership of Common Shares	117
Relationship with ACE	118
Material Tax Considerations	124
Description of Notes and Guarantees	129
Underwriting	142
Legal Matters	144
Experts	144
Where You Can Find More Information	144
Enforceability of Civil Liabilities under United States Federal Securities Laws and Other Matters	145
Index to Financial Statements	F-1

You should rely only on the information contained in this prospectus. We and the underwriters have not authorized any other person to provide you with different information. This prospectus is an offer to sell only the notes offered hereby, but only under circumstances and in jurisdictions where it is lawful to do so. The information contained in this prospectus is current only as of its date.

PROSPECTUS SUMMARY

The following summary highlights information contained elsewhere in this prospectus and may not contain all of the information that may be important to you. You should read all of the information in this prospectus, including the combined financial statements and related notes, and the risks of investing in the notes discussed under "Risk Factors," before making an investment decision.

References in this prospectus to "Assured Guaranty," the "guarantor," "we," "us" and "our" refer to Assured Guaranty Ltd. and, unless the context otherwise requires or unless otherwise stated, its subsidiaries. Reference in this prospectus to "Holdings" or the "issuer" are to Assured Guaranty US Holdings Inc., the issuer of the notes and a wholly owned subsidiary of Assured Guaranty. The notes are being offered by Holdings. For purposes of the offering of notes, Assured Guaranty Ltd. is not, and will not be, acting as agent for Holdings and nothing in this prospectus should be read as implying that it is, or will be, so acting. When we refer to net par in this prospectus, we mean the par value of an obligation for which we have provided credit support, net of any amounts that we have ceded or retroceded to reinsurers. Our executive offices are located at 30 Woodbourne Avenue, Hamilton HM08 Bermuda, and our telephone number is 441-296-4004.

Overview

Assured Guaranty US Holdings Inc., the issuer of the notes, is a wholly owned subsidiary of Assured Guaranty and was formed as a holding company to hold the shares of Assured Guaranty Corp. and Assured Guaranty Financial Products. Assured Guaranty is a Bermuda-based company providing credit enhancement products to the municipal finance, structured finance and mortgage markets. We apply our credit expertise, risk management skills and capital markets experience to develop insurance, reinsurance and derivative products that meet the credit enhancement needs of our customers. We market our products directly and through financial institutions. We serve the U.S. and international markets.

Our financial results include three operating segments:

Financial guaranty direct, which protects the holder against an issuer's failure to pay principal and interest when due or other credit events.

Financial guaranty reinsurance, which indemnifies another financial guarantor, the ceding company, against part or all of the loss the ceding company may sustain under financial guaranty policies it has reinsured to us.

Mortgage guaranty, which protects mortgage lenders and investors against the default of borrowers on mortgage loans, and provides reinsurance to mortgage guaranty insurers.

Our other segment includes businesses that we have exited. The following table sets forth gross written premiums and the combined ratio for each of our segments for the year ended December 31, 2003.

	Gross Written Premiums ⁽¹⁾		Combined Ratio ⁽²⁾
	Amount	Percent	
(\$ in millions)			
Financial guaranty direct	\$ 71.2	27.0%	58.0%
Financial guaranty reinsurance	168.7	63.8	73.3
Mortgage guaranty	24.4	9.2	58.7
Total operating segments	\$ 264.3	100.0%	65.6%
Other	84.9		112.6
Total	\$ 349.2		83.7%

- (1) Gross written premiums represents total premiums for insurance and credit derivatives written and reinsurance assumed during the period.
- (2) The combined ratio is the sum of the loss ratio (the ratio calculated by dividing net losses and loss adjustment expenses by net premiums earned) and the expense ratio (the ratio calculated by dividing profit commission expense, acquisition costs and operating expenses by net premiums earned). A combined ratio under 100% generally indicates an underwriting profit; a combined ratio over 100% generally indicates an underwriting loss.

Our businesses have a history of strong income generation, producing cumulative net income of \$444.1 million since January 1, 2000. As of December 31, 2003, we had cash and invested assets of \$2.2 billion, total assets of \$2.9 billion and shareholder's equity of \$1.4 billion (\$1.3 billion on a pro forma basis after giving effect to the transactions described under "Formation Transactions"). Our invested assets as of December 31, 2003 consisted entirely of cash and fixed maturity securities with an average rating of AA+. Our past performance may not be indicative of future results.

Assured Guaranty Corp., our principal U.S. insurance subsidiary, maintains financial strength ratings of "AAA" (Extremely Strong) from Standard & Poor's Ratings Services, a division of the McGraw-Hill Companies, Inc. ("S&P"), the highest of its 21 ratings categories, and "Aa1" (Excellent) from Moody's Investors Service, Inc. ("Moody's"), the second highest of its 21 ratings categories. Our principal Bermuda insurance subsidiary maintains financial strength ratings of "AA" (Very Strong) from S&P, its third highest ratings category, "Aa2" (Excellent) from Moody's, its third highest ratings category, and "AA" (Very Strong) from Fitch, Inc. ("Fitch"), the third highest of its 24 ratings categories. A financial strength rating is an opinion with respect to an insurer's ability to pay under its insurance policies and contracts and is not a recommendation to buy, hold or sell any security issued by an insurer, including the notes.

We have approximately 110 employees in offices located in the United States, Bermuda and the United Kingdom.

Business Fundamentals

We believe the credit enhancement markets offer attractive growth opportunities and financial returns over the long term. In recent years, new issuance volumes in the municipal and structured finance sectors have been increasing. From 1997 to 2002, insured U.S. asset-backed finance volume increased at a compound annual growth rate of 16%, and insured U.S. municipal finance volume increased at a compound annual growth rate of 10%. Asset-backed finance is a commonly-used technique in which debt instruments are issued that are backed by loans or accounts receivable (other than mortgage loans) originated by banks, credit card companies or other providers of credit. While growth rates may fluctuate from year to year, we believe demand for financial guaranty insurance and reinsurance will continue to be strong as a result of: (1) continuing demand for asset securitization, or the process of aggregating similar instruments, such as loans or mortgages, into a negotiable security, in the United States, (2) continued development of new structured products and expansion into new asset classes, (3) continued high level of issuances of U.S. municipal finance obligations and (4) increasing privatization initiatives and growing use of asset securitization in Europe. We cannot assure you that these circumstances will persist or that demand for financial guaranty insurance or reinsurance will continue to be strong.

We believe our business offers attractive and recurring revenues as a result of the stable nature of our earned premiums (that portion of written premiums that applies to the expired portion of the policy term and is therefore recognized as revenue under generally accepted accounting principles), the significant contribution of net investment income and the low frequency of loss associated with our businesses. A significant portion of our premiums are received up front and recognized as earned

premiums over the life of the contract. As of December 31, 2003, we had \$625.4 million of unearned premiums (that portion of written premiums that is allocable to the unexpired portion of the policy term) recorded on our balance sheet. The remainder of our premiums are received on an installment basis and earned over each installment period. As of December 31, 2003, our estimate of the net present value of future premiums, discounted at 6% per year, expected to be earned under existing installment contracts was \$309.8 million. In addition, our invested assets, which were \$2.2 billion at December 31, 2003, generate recurring investment income.

Competitive Strengths

We believe that our competitive strengths enable us to capitalize on the opportunities in the credit enhancement markets. These strengths include:

Underwriting discipline and financial structuring expertise. We have a disciplined approach to underwriting that emphasizes profitability over market share. We have substantial experience in developing innovative credit enhancement solutions to satisfy the diverse risk and financial management demands of our customers.

Established market relationships. Over the past 15 years we have developed strong relationships with key participants in our markets, including issuers, investors, financial guarantors and financial institutions. We seek to distinguish ourselves from our competitors by providing innovative credit enhancement solutions and superior execution and client service.

Experienced management and underwriting team. Our senior management has an average of more than 16 years of experience in the insurance, credit or financial guaranty markets. We also have a team of 15 senior underwriters with an average of approximately 12 years of financial guaranty or similar credit experience.

Multiple locations and licenses. We have operations in Bermuda, the United States and the United Kingdom. We have a range of licenses that allows us to participate in many sectors of the credit enhancement market.

Corporate Strategy

Our objective is to build long-term shareholder value by achieving strong profitability through disciplined underwriting, proactive risk management and the growth of our business. Our goal is to improve our return on average equity (excluding the impact of realized gains and losses on investments and unrealized gains and losses on derivative financial instruments) to approximately 11% in 2004. In addition, our medium-term goal is to generate returns consistent with those of the leading performers in the financial guaranty industry. The major elements of our strategy are:

Expand our direct financial guaranty business. We intend to expand our direct financial guaranty business beyond our historical focus on credit derivatives by substantially increasing the amount of traditional financial guaranty insurance we write in U.S. and international markets. We believe the market for financial guaranty insurance will grow as the issuance of municipal and structured finance obligations continues to be strong, as capital providers continue to seek to reduce risk exposures and as the market for credit enhancement products develops further. We intend to write business in a manner consistent with achieving our goal of obtaining a "Aaa" rating from Moody's to match our "AAA" rating from S&P.

Expand our financial guaranty reinsurance business. Our commitment to the financial guaranty reinsurance market, readiness to execute transactions and financial strength afford us a significant opportunity to profitably gain market share. We intend to utilize the benefits of our Bermuda license to improve our returns in this business.

Transition our mortgage guaranty business. We intend to write investment grade mortgage guaranty insurance and reinsurance that is consistent with our ratings objectives. Our industry experience and licenses enable us to provide mortgage credit enhancement in the form of either financial guaranty insurance or mortgage guaranty insurance to meet the specific needs of mortgage lenders and investors.

Expand our position in international markets. We intend to capitalize on significant growth opportunities in international markets. Our initial focus for international expansion is privatization finance initiatives ("PFI") in the United Kingdom, the largest market for financial guaranty insurance outside the United States, and public/private partnerships ("PPP") in the rest of Europe.

Maintain our commitment to financial strength. We recognize the importance of our excellent financial strength ratings and intend to write business in a manner consistent with achieving our goal of obtaining a "Aaa" rating from Moody's to match our "AAA" rating from S&P. We will maintain our financial strength through disciplined risk selection, prudent operating and financial leverage and a conservative investment posture.

Manage our capital efficiently. We will monitor rating agency capital adequacy requirements to appropriately deploy capital to optimize the execution of our business plan and our return on capital.

Risks Relating to Our Company

As part of your evaluation of us, you should take into account the risks we face in our business. These risks include:

Possibility of Ratings Downgrade. The ratings assigned to our insurance subsidiaries are subject to periodic review and may be downgraded by one or more of the rating agencies as a result of changes in the views of the rating agencies or adverse developments in our or our subsidiaries' financial conditions or results of operations. Any such downgrade could have an adverse effect on the affected subsidiary's results of operations or financial condition.

New Business Strategy. Because our new strategy emphasizes financial guaranty insurance and reinsurance and deemphasizes certain other lines of business in which we have historically operated, we cannot assure you that we will be able to successfully implement this strategy. Recent employee layoffs and resignations may adversely affect our ability to implement our new strategy. Any failure to implement all or any part of our strategy could have a material adverse effect on our results of operations.

Dependence on Customers. We have derived a substantial portion of our revenues from financial guaranty reinsurance premiums. For the years ended December 31, 2003, 2002 and 2001, 45%, 21% and 31%, respectively, of our gross written premiums were provided by four ceding companies. A significant reduction in the amount of reinsurance ceded by one or more of our principal ceding companies could have a material adverse effect upon our results of operations.

Business Subject to General Economic and Capital Markets Factors. Our business, and the risks associated with our business, depend in large measure on general economic conditions and capital markets activity. Prevailing interest rate levels also affect demand for financial guaranty insurance.

Adequacy of Loss Reserves. We establish liabilities, or loss reserves, to reflect the estimated cost of claims incurred that we will ultimately be required to pay in respect of insurance and reinsurance we have written. If our loss reserves at any time are determined to be inadequate, we will be required to increase loss reserves at the time of such determination. This could cause a material increase in our liabilities and a reduction in our profitability, or possibly an operating loss and reduction of capital.

Competition. We face significant competition in our business, and our revenues and profitability could decline as a result of competition. Four companies accounted for the vast majority of the gross written premiums for the entire financial guaranty industry in 2003. We also face competition from other forms of credit enhancement. There are also a relatively limited number of financial guaranty reinsurance companies and mortgage guaranty companies.

Taxation. We manage our business so that we and our non-U.S. subsidiaries (other than Assured Guaranty Re Overseas Ltd.) will not be subject to U.S. income tax. However, we cannot be certain that the U.S. Internal Revenue Service will not contend successfully that we or any of our foreign subsidiaries is/are engaged in a trade or business in the United States and thus subject to additional taxation in the United States.

For more information about these and other risks, see "Risk Factors" beginning on page 11. You should carefully consider these risk factors together with all of the other information included in this prospectus before making an investment decision.

Corporate Structure

Assured Guaranty was incorporated in Bermuda in August 2003 as a subsidiary of ACE Limited, our former parent ("ACE"), for the sole purpose of becoming a holding company for ACE's subsidiaries conducting its financial and mortgage guaranty businesses, which we refer to as the transferred businesses, in connection with our initial public offering, or IPO. Certain of the transferred businesses were originally conducted by subsidiaries of Capital Re Corporation ("Capital Re"), which was acquired by ACE in December 1999.

Following our IPO, ACE beneficially owns 26,000,000 of our common shares, or approximately 35% of our outstanding common shares (18,650,000 common shares, or 25% of our outstanding common shares if the underwriters' option to purchase additional common shares as part of the IPO is exercised in full). We have a number of continuing agreements with ACE, including reinsurance agreements pursuant to which we have ceded or will cede to ACE certain risks and services agreements pursuant to which ACE will provide us with various administrative services. All of these agreements and arrangements are more fully described under "Relationship with ACE."

Each of our operating subsidiaries conducted business under names including "ACE," "AGR" and/or "Capital Re." As part of the formation transactions described under "Formation Transactions," we have changed, or are in the process of changing, the names of each of these subsidiaries to the respective names set forth below (or derivations of these names).

The following organization chart illustrates the corporate relationships among us and our principal subsidiaries (all ownership interests are 100% except where noted):

The Offering

Issuer	Assured Guaranty US Holdings Inc.
Guarantor	Assured Guaranty Ltd.
Securities Offered	\$200,000,000 aggregate principal amount of % Senior Notes due
Maturity Date	,
Interest	The issuer will pay interest on the notes semi-annually on and of each year, beginning , 2004. The notes will bear interest at the rate of % per year.
Ranking	The notes will be unsecured senior obligations of the issuer and will rank equally with all other unsecured senior indebtedness of the issuer from time to time outstanding. The guarantees of the guarantor will be unsecured senior obligations of the guarantor and will rank equally with all other unsecured senior indebtedness of the guarantor from time to time outstanding. The notes will be structurally subordinated to all obligations of the issuer's subsidiaries from time to time outstanding, including claims with respect to trade payables. The guarantees will be structurally subordinated to all obligations of the guarantors' subsidiaries from time to time outstanding, including claims with respect to trade payables. As of March 31, 2004, the issuer's subsidiaries had \$0 of indebtedness outstanding and the guarantor's subsidiaries had \$202 million of indebtedness outstanding (after giving effect to the transactions described under "Formation Transactions").
Covenants	The indenture governing the notes contains covenants that, among other things, limit the ability of the guarantor and its subsidiaries to (1) incur indebtedness secured by the capital stock of designated subsidiaries, (2) dispose of the capital stock of designated subsidiaries or (3) engage in mergers, consolidations, amalgamations and sales of all or substantially all of their assets. See "Description of Notes and Guarantees Covenants."
Optional Redemption	The issuer may, at its option, redeem some or all of the notes at any time, at the "make-whole" price described in this prospectus, plus accrued and unpaid interest to the redemption date. See "Description of Notes and Guarantees Optional Redemption." In addition, the issuer may redeem all of the notes under the circumstances described under "Description of Notes and Guarantees Redemption for Changes in Withholding Taxes."
Use of Proceeds	To repay indebtedness owed to a subsidiary of ACE incurred in connection with the formation transactions described under "Formation Transactions."

No Public Market

The notes will be a new issue of securities and will not be listed on any securities exchange or included in any automated quotation system. The underwriters have advised us that they intend to make a market for the notes, but they are not obligated to do so and may discontinue their market-making activities at any time without notice.

Additional Notes

The issuer may, without notice to or the consent of the then existing holders of the notes, issue additional notes ranking equally and ratably with the notes in all respects except for the issue price, issue date and the payment of interest accruing prior to the issue date of the additional notes or the first payment of interest following the issue date of the additional notes. The additional notes will be consolidated and form a single series with the notes offered hereby and will have the same terms as to status, redemption or otherwise as the notes offered hereby.

Recent Developments

Results for the Quarter ended March 31, 2004

On May 11, 2004, we reported our results for the three-months ended March 31, 2004. We reported net income of \$46.9 million for the first quarter ended March 31, 2004, an increase of 48% compared with net income of \$31.8 million for the first quarter of 2003.

Gross Written Premiums by Segment

	Three Months Ended March 31,	
	2004	2003
	(in millions)	
Financial guaranty direct	\$ 25.6	\$ 14.0
Financial guaranty reinsurance	52.4	29.8
Mortgage guaranty	14.0	8.1
Sub-total	\$ 92.0	\$ 51.9
Other	(93.6)	60.9
Total	\$ (1.5)	\$ 112.7

Gross premiums written were a negative \$1.5 million in the quarter. Gross premiums written in our other segment (which represents our exited lines of business) were reduced by \$97.8 million in the quarter due to the accounting for the unwinding of equity layer credit protection products. Partially offsetting this premium reduction was the recognition of \$10.4 million of gross premiums written in the financial guaranty direct segment due to the closing out of transactions in which we no longer participate; excluding this amount, gross premiums written in the financial guaranty direct segment grew 9%.

Net Premiums Earned by Segment

	Three Months Ended March 31,	
	2004	2003
	(in millions)	
Financial guaranty direct	\$ 40.7	\$ 14.7
Financial guaranty reinsurance	20.4	16.9
Mortgage guaranty	8.4	9.6
Sub-total	\$ 69.5	\$ 41.2
Other	17.2	22.4
Total	86.7	63.6
Municipal refunding premiums	2.9	3.3
Sub-total	\$ 83.8	\$ 60.3

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

Net premiums earned were \$86.7 million in the first quarter of 2004, up 36% compared with \$63.6 million in the first quarter of 2003. Financial guaranty direct net premiums earned included \$24.2 million associated with the closing out of transactions types that we do not expect to underwrite in the future. Financial guaranty reinsurance net premiums earned were \$20.4 million, up 21% from \$16.9 million in the first quarter of 2003. Included in this amount were \$2.9 million of municipal bond refunding premiums, compared with \$3.3 million in the first quarter of 2003. Mortgage guaranty net premiums earned were \$8.4 million, compared with \$9.6 million in the first quarter of 2003, reflecting the run-off of our quota share mortgage guaranty reinsurance business.

Investment income in the quarter was \$24.4 million, up modestly compared with \$24.1 million in the first quarter of 2003. The average portfolio yield was 4.8%, compared with 5.3% in the prior year on an investment portfolio of \$2.2 billion at March 31, 2004. The portfolio's average credit quality remained at AA+/Aa2. As a result of IPO-related transactions in the other segment, we expect a \$163 million reduction in the investment portfolio in the second quarter.

Combined Ratio

	Three Months Ended March 31,	
	2004	2003
Loss ratio	27.3%	36.5%
Expense ratio	35.9	41.6
Combined ratio	63.2%	78.1%

Loss and loss adjustment expenses in the quarter were \$23.7 million, or 27% of net premiums earned ("loss ratio"), compared with \$23.2 million or a 36.5% loss ratio in the first quarter of 2003. Both loss ratios are significantly affected by the other segment and the closing out of transactions in the financial guaranty direct segment in preparation for our IPO.

Our profit commission expense, acquisition costs and other operating expenses were \$31.2 million in the quarter and 35.9% as a percent of net premiums earned ("expense ratio"), as compared to \$26.4 million or a 41.6% expense ratio in the first quarter of 2003. The increase in expenses reflects the addition of IPO-related and holding company expenses as well as \$1.5 million of severance expenses in the quarter.

Our shareholder's equity as of March 31, 2004 was \$1,510 million. On a pro forma basis giving effect to the formation transactions described under "Formation Transactions" and the transactions described under "Supplemental Pro Forma Condensed Combined Financial Information (Unaudited)" our shareholder's equity as of March 31, 2004 was \$1,385 million.

Resignation of Senior Officer

On March 31, 2004, Joseph W. Swain III, who until December 2003 had been the chief executive officer of ACE's financial guaranty business and was thereafter the President-Reinsurance of Assured Guaranty US Holdings Inc., resigned. In his resignation, Mr. Swain cited differences with management over our new business strategy and our ability to execute this strategy as a result of his concerns about the relevant experience of certain members of management, staffing levels and corporate culture. Management believes these concerns are unfounded. We have promoted Robbin Conner, a senior executive of Assured Guaranty Corp., to replace Mr. Swain as the head of our financial guaranty reinsurance business. Please see "Management" for a discussion of Mr. Conner's business experience.

Summary Combined Financial Information of Assured Guaranty

The following table sets forth summary combined financial and other information of Assured Guaranty. The summary combined statement of operations data for each of the years ended December 31, 2003, 2002 and 2001 and the summary combined balance sheet data as of December 31, 2003 and 2002 are derived from our audited combined financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") and appear elsewhere in this prospectus. The summary combined balance sheet data as of December 31, 2001 are derived from our audited combined financial statements, which have been prepared in accordance with GAAP.

These historical results are not necessarily indicative of results to be expected for any future period. You should read the following summary combined financial information together with the other information contained in this prospectus, including "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the combined financial statements and related notes included elsewhere in this prospectus.

	Year Ended December 31,		
	2003	2002	2001
(\$ in millions)			
Statement of operations data:			
Gross written premiums	\$ 349.2	\$ 417.2	\$ 442.9
Net written premiums ⁽¹⁾	491.5	352.5	206.6
Net earned premiums	\$ 310.9	\$ 247.4	\$ 293.5
Net investment income	96.3	97.2	99.5
Net realized investment gains	5.5	7.9	13.1
Unrealized gains (losses) on derivative financial instruments	98.4	(54.2)	(16.3)
Other income	1.2	3.6	2.9
Total revenues	512.3	302.0	392.9
Loss and loss adjustment expenses	144.6	120.3	177.5
Profit commission expense	9.8	8.5	9.0
Acquisition costs	64.9	48.4	51.1
Operating expenses	41.0	31.0	29.8
Goodwill amortization			3.8
Interest expense	5.7	10.6	11.5
Total expenses	266.1	218.8	282.8
Income before income taxes	246.2	83.2	110.1
Provision (benefit) for income taxes	31.7	10.6	22.2
Net income before cumulative effect of new accounting standard	214.5	72.6	87.9
Cumulative effect of new accounting standard, net of taxes			(24.1)
Net income	\$ 214.5	\$ 72.6	\$ 63.8
Balance sheet data (end of period):			
Investments and cash	\$ 2,222.1	\$ 2,061.9	\$ 1,710.8

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

Year Ended December 31,

	Year Ended December 31,		
Prepaid reinsurance premiums	11.0	179.5	171.5
Total assets	2,857.9	2,719.9	2,322.1
Unearned premium reserve	625.4	613.3	500.3
Reserve for losses and loss adjustment expenses	522.6	458.8	401.1
Long-term debt	75.0	75.0	150.0
Total liabilities	1,420.2	1,462.6	1,260.4
Accumulated other comprehensive income	81.2	89.0	43.3
Shareholder's equity	1,437.6	1,257.2	1,061.6
Pro forma information: ⁽²⁾			
Debt	\$	200.0	
Shareholder's equity		1,311.6	
Book value per share ⁽³⁾		17.27	

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

Year Ended December 31,

	2003	2002	2001
--	------	------	------

(\$ in millions)

GAAP financial information:

Loss and loss adjustment expense ratio ⁽⁴⁾	46.5%	48.6%	60.5%
Expense ratio ⁽⁵⁾	37.2	35.5	30.6
Combined ratio	83.7%	84.1%	91.1%

Statutory financial information (end of period):

Contingency reserve ⁽⁶⁾	\$ 410.5	\$ 315.5	\$ 228.9
Policyholders' surplus	980.5	835.4	833.2

Additional financial guaranty information (end of period):

Net in-force business (principal and interest)	\$ 130,047	\$ 124,082	\$ 117,909
Net in-force business (principal only)	87,524	80,394	75,249
Present value of gross premiums written ⁽⁷⁾	238.8	215.5	195.0
Net present value of installment premiums in-force ⁽⁸⁾	309.8	260.2	159.7

- (1) Net written premiums exceeded gross written premiums for the year ended December 31, 2003 due to \$154.8 million of return premium from two terminated ceded reinsurance contracts.
- (2) The pro forma information reflects adjustments to give effect to the transactions described under "Formation Transactions" and "Pro Forma Combined Financial Information."
- (3) Based on 75,937,417 shares outstanding.
- (4) The loss and loss adjustment expense ratio is calculated by dividing loss and loss adjustment expenses by net earned premiums.
- (5) The expense ratio is calculated by dividing the sum of profit commission expense, acquisition costs and operating expenses by net earned premiums.
- (6) Under statutory accounting principles, financial guaranty and mortgage guaranty insurers are required to establish contingency reserves based on a specified percentage of premiums. A contingency reserve is an additional liability reserve established to protect policyholders against the effects of adverse economic developments or cycles or other unforeseen circumstances.
- (7) Represents gross premiums related to financial guaranty contracts written in the current period, including the full amount of upfront premiums received and the present value of all installment premiums, discounted at 6% per year. See "Management's Discussion and Analysis of Financial Condition and Results of Operations - Segment Results of Operations" for a reconciliation to gross written premiums.
- (8) Represents the present value of installment premiums on all in-force financial guaranty business, net of reinsurance ceded and ceding commissions, discounted at 6% per year.

RISK FACTORS

An investment in the notes involves a number of risks. You should carefully consider the following information about these risks, together with the other information contained in this prospectus, before investing in the notes. The risks and uncertainties described below are not the only ones we face. However, these are the risks our management believes are material. Additional risks not presently known to us or that we currently deem immaterial may also impair our business or results of operations. Any of the risks described below could result in a significant or material adverse effect on our results of operations or financial condition and consequently our ability to make payments in respect of the notes and the guarantees. You could lose all or part of your investment.

This prospectus also contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in the forward-looking statements as a result of certain factors, including the risks described below and elsewhere in this prospectus. See "Forward-Looking Statements."

Risks Related to Our Company

A downgrade of the financial strength or financial enhancement ratings of any of our insurance subsidiaries could adversely affect our business and prospects and, consequently, our results of operations and financial condition.

Financial strength ratings have become an increasingly important factor in establishing the competitive position of insurance and reinsurance companies. The objective of these ratings is to provide an opinion of an insurer's financial strength and ability to meet ongoing obligations to its policyholders. Ratings reflect the rating agencies' opinions of our financial strength, and are neither evaluations directed to investors in the notes nor recommendations to buy, sell or hold the notes. As of the date of this prospectus, Assured Guaranty Corp. has been assigned a "AAA" (Extremely Strong) rating from S&P, the highest of the 21 ratings categories used by S&P, and a "Aa1" (Excellent) rating from Moody's, the second highest of the 21 ratings categories used by Moody's. All of our other insurance company subsidiaries have been assigned "AA" (Very Strong) ratings from S&P, the third highest ratings category used by S&P, "Aa2" (Excellent) ratings from Moody's, the third highest ratings category used by Moody's, and "AA" (Very Strong) ratings from Fitch, the third highest of the 24 ratings categories used by Fitch. A financial strength rating is an opinion with respect to an insurer's ability to pay under its insurance policies and contracts in accordance with their terms. The opinion is not specific to any particular policy or contract. Financial strength ratings do not refer to an insurer's ability to meet non-insurance obligations and are not a recommendation to purchase or discontinue any policy or contract issued by an insurer or to buy, hold, or sell any security issued by an insurer, including the notes. Assured Guaranty Corp.'s S&P ratings outlook is "Negative." While an S&P outlook is not necessarily a precursor to a ratings change, a "Negative" outlook means a rating may be lowered.

In addition, AGRI and AGRO carry financial enhancement ratings from S&P of "AA" (Very Strong).

The ratings assigned by S&P, Moody's and Fitch to our insurance subsidiaries are subject to periodic review and may be downgraded by one or more of the rating agencies as a result of changes in the views of the rating agencies or adverse developments in our or our subsidiaries' financial conditions or results of operations due to underwriting or investment losses or other factors. We are in ongoing discussions with S&P and Moody's regarding our ratings, including the impact on our ratings of the formation transactions described under "Formation Transactions", the IPO and our new business strategy. As a result, the ratings assigned to our insurance subsidiaries by either or both of S&P and Moody's may change at any time. In the case of AGRO and Assured Guaranty Mortgage, their ratings are dependent upon contractual support provided by AGRI.

If the ratings of any of our insurance subsidiaries were reduced below current levels by any of the rating agencies, it could have an adverse effect on the affected subsidiary's competitive position and its prospects for future business opportunities. A downgrade may also reduce the value of the reinsurance we offer, which may no longer be of sufficient economic value for our customers to continue to cede to our subsidiaries at economically viable rates.

With respect to a significant portion of our in-force financial guaranty reinsurance business, in the event of certain downgrades, the ceding company has the right to recapture business ceded to the affected subsidiary and assets representing substantially all of the statutory unearned premium and loss reserves (if any) associated with that business, with a corresponding negative impact to earnings, which could be significant. Alternatively, the ceding company can increase the commissions it charges us for cessions. Any such increase may be retroactive to the date of the cession, requiring the affected subsidiary to refund a portion of related premium previously earned, with a corresponding negative impact to earnings, which could be significant. In the event of a downgrade of any of our subsidiaries that write or insure exposures relating to contracts that allow for the use of derivative instruments to transfer credit risk, or credit derivatives, a downgrade below negotiated levels may allow a counterparty to terminate its agreements, resulting in the possible payment of a settlement amount. A downgrade also will increase the possibility that we may have to pledge collateral for the benefit of a counterparty.

A downgrade may also negatively impact the affected company's ability to write new business or negotiate favorable terms on new business.

Our success depends on our ability to successfully execute our new business strategy.

Our strategy is to focus on two core businesses: (1) financial and mortgage guaranty insurance and (2) financial guaranty reinsurance.

The fact that Assured Guaranty Corp., through which we write financial guaranty insurance, carries a triple-A rating from S&P but not from Moody's places it at a competitive disadvantage against companies rated triple-A by both S&P and Moody's. The absence of a triple-A rating from Moody's may adversely affect the desirability of our financial guaranty insurance, and in fact may preclude us from successfully marketing our financial guaranty insurance in certain markets. Furthermore, while we have a substantial in-force book of financial guaranty direct business, the majority of that exposure was written in the credit derivatives market rather than in the more traditional third-party financial guaranty insurance market. We may not be able to successfully expand relationships with issuers, servicers and other parties that are necessary to generate business in the traditional financial guaranty insurance market. Finally, Assured Guaranty Corp. presently is licensed in 45 states and the District of Columbia, and is seeking licenses in those U.S. jurisdictions where it is not presently licensed. Assured Guaranty Corp. may not be able to obtain those licenses, or may face delays in obtaining those licenses.

We are combining our mortgage guaranty business and our financial guaranty business. We intend to write mortgage guaranty insurance that is rated investment grade. We may not be able to source mortgage guaranty insurance business of this type in sufficient amounts or at adequate premium rates.

We intend to write more of our financial guaranty reinsurance through AGRI, which is rated in the double-A category by both S&P and Moody's, and less of this business through Assured Guaranty Corp., which is rated AAA/Aa1. The absence of a triple-A rating from S&P or Moody's places AGRI at a competitive disadvantage against companies rated triple-A by S&P or Moody's.

Because our strategy includes focusing on new lines of business in which we and our senior management have less experience, we cannot assure you that we will be able to successfully implement this strategy. In addition, recent employee layoffs and resignations have resulted in the loss of some experienced employees and reduced staff levels generally, which could adversely affect our ability to

successfully implement our new strategy. Any failure to implement all or any part of our strategy could have a material adverse effect on our results of operations.

We are dependent on a small number of ceding companies to provide us with a substantial part of our reinsurance business.

Historically, we have derived a substantial portion of our revenues from financial guaranty reinsurance premiums. Ambac Assurance Corporation ("Ambac"), Financial Guaranty Insurance Company ("FGIC"), Financial Security Assurance Inc. ("FSA") and MBIA Insurance Corporation ("MBIA") in the aggregate accounted for 45%, 21% and 31% of our gross written premiums for the years ended December 31, 2003, 2002 and 2001. For the year ended December 31, 2003, 25% and 11% of our gross written premiums were ceded by FSA and MBIA, respectively. For the year ended December 31, 2002, 11% of our gross written premiums was paid by Dresdner Bank and in 2001, FSA and Credit Suisse provided 13% and 10%, respectively, of our gross written premiums. Gross written premiums from Dresdner Bank and Credit Suisse were paid with respect to equity layer credit protection, a business that we have exited.

A significant reduction in the amount of reinsurance ceded by one or more of our principal ceding companies could have a material adverse effect upon our results of operations. A number of factors could cause such a reduction. For example, there is likely to be some reluctance among our principal ceding companies to cede business to us as a result of our intent to compete with them in the direct financial guaranty business. In addition, primary insurers may retain higher levels of risk. Also, the volume of municipal bond and structured securities new issuances, together with the levels of and changes in interest rates and investor demand, may significantly affect the new business activities of primary financial guaranty insurers and, consequently, their use of reinsurance.

Additionally, our ability to receive profitable pricing for our reinsurance depends largely on prices charged by the primary insurers for their insurance coverage and the amount of ceding commissions paid by us to these primary insurers.

General economic factors, including fluctuations in interest rates and housing prices, may adversely affect our loss experience and the demand for our products.

Our business, and the risks associated with our business, depend in large measure on general economic conditions and capital markets activity. Our loss experience could be materially adversely affected by extended national or regional economic recessions, business failures, rising unemployment rates, interest rate changes or volatility, changes in investor perceptions regarding the strength of financial guaranty providers and the policies or guaranties offered by such providers, investor concern over the credit quality of municipalities or corporations, terrorist attacks, acts of war, or combinations of such factors. These events could also materially decrease demand for financial guaranty insurance. In addition to exposure to general economic factors, we are exposed to the specific risks faced by the particular businesses, municipalities or pools of assets covered by our financial guaranty products.

Prevailing interest rate levels affect capital markets activity which in turn affects demand for financial guaranty insurance. Higher interest rates may result in declines in new issue and refunding volume which may reduce demand for our financial guaranty products. Lower interest rates generally are accompanied by narrower interest rate spreads between insured and uninsured obligations. The purchase of insurance during periods of narrower interest rate spreads generally will provide lower cost savings to the issuer than during periods of wider spreads. These lower cost savings could be accompanied by a corresponding decrease in demand for financial guaranty insurance. However, the increased level of refundings during periods of lower interest rates historically has increased the demand for insurance.

Under the standard mortgage insurance policies that we reinsure, a default on the underlying mortgage generally will give the insurer the option to pay the entire loss amount and take title to the mortgaged property or pay the coverage percentage in full satisfaction of its obligations under the policy. Due to a strong housing market in recent years, insurers have been able to take advantage of paying the entire loss amount and selling properties quickly. If housing values depreciate or fail to appreciate, the primary insurers' ability to recover amounts paid on defaulted mortgages may be reduced or delayed, which in turn may lead to increased losses under our related reinsurance contracts and have a material adverse affect on our results of operations or our financial condition in general.

If claims exceed our loss reserves, our financial results could be significantly adversely affected.

Our results of operations and financial condition depend upon our ability to assess accurately and manage the potential loss associated with the risks that we insure and reinsure. We establish loss and loss adjustment expense reserves based on estimates involving actuarial and statistical projections of our expectations of the ultimate settlement and administration costs of claims on the policies we write. We use actuarial models as well as historical insurance industry loss development patterns as estimates of future trends in claims severity, frequency and other factors to establish our estimate of loss reserves. Establishing loss reserves is an inherently uncertain process. Accordingly, actual claims and claim expenses paid may deviate, perhaps materially, from the reserve estimates reflected in our combined financial statements.

If our loss reserves at any time are determined to be inadequate, we will be required to increase loss reserves at the time of such determination. This could cause a material increase in our liabilities and a reduction in our profitability, or possibly an operating loss and reduction of capital.

Adverse selection by ceding companies may adversely affect our financial results.

A portion of our reinsurance business is written under treaties, which generally give the ceding company some ability to select the risks ceded to us as long as they are covered by the terms of the treaty. There is a risk under these treaties that the ceding companies will adversely select the risks ceded to us by ceding those exposures that have higher rating agency capital charges or that the ceding companies expect to be less profitable. We attempt to mitigate this risk in a number of ways, including requiring ceding companies to retain a minimum amount, which varies by treaty, of the ceded business. If we are unsuccessful in mitigating this risk, our financial results may be adversely affected.

Our financial guaranty products may subject us to significant risks from individual or correlated credits.

The breadth of our business exposes us to potential losses in a variety of our products as a result of a credit problem at one company ("single name" exposure). For example, we could have direct exposure to a corporate credit for which we write and/or insure a credit derivative. We could also be exposed to the same corporate credit risk if the credit's securities are contained in a portfolio of collateralized debt obligations ("CDOs") we insure, or if it is the originator or servicer of loans or other assets backing structured securities that we have insured. A CDO is a debt security backed by a pool of debt obligations. While we track our aggregate exposure to single names in our various lines of business and have established underwriting criteria to manage risk aggregations, there can be no assurance that our ultimate exposure to a single name will not exceed our underwriting guidelines, or that an event with respect to a single name will not cause a significant loss. In addition, because we insure or reinsure municipal bonds, we can have significant exposures to single municipal risks. While the risk of a complete loss, where we pay the entire principal amount of an issue of bonds and interest thereon with no recovery, is generally lower than for corporate credits as most municipal bonds are backed by tax or other revenues, there can be no assurance that a single default by a municipality would not have a material adverse effect on our results of operations or financial condition.

Some of our direct financial guaranty products may be riskier than traditional financial guaranty insurance.

Unlike our triple-A monoline financial guaranty competitors, a substantial portion of our financial guaranty direct exposures have been assumed as credit derivatives. Traditional financial guaranty insurance provides an unconditional and irrevocable guaranty that protects the holder of a municipal finance or structured finance obligation against non-payment of principal and interest, while credit derivatives provide protection from the occurrence of specified credit events, including non-payment of principal and interest. Credit derivative products generally also provide for settlement of an entire exposure, rather than a missed payment obligation as in traditional financial guaranty, upon the occurrence of a credit event, which could require us to sell assets or otherwise generate liquidity in advance of any potential recoveries.

Competition in our industry may adversely affect our revenues.

We face significant competition in our business, and our revenues and profitability could decline as a result of competition.

The financial guaranty industry is highly competitive. The principal sources of direct and indirect competition are other financial guaranty insurance companies, most of which have greater financial resources and superior financial strength ratings than we do. Four companies, Ambac, FGIC, FSA and MBIA, accounted for the vast majority of the gross written premiums for the entire financial guaranty industry in 2003. We also face competition from other forms of credit enhancement, including structural enhancement incorporated in structured and other obligations and letters of credit, guaranties and credit derivatives provided primarily by foreign and domestic banks and other financial institutions, some of which are governmental enterprises or have been assigned the highest ratings awarded by one or more of the major rating agencies.

There are also a relatively limited number of financial guaranty reinsurance companies. As a result, the industry is particularly vulnerable to swings in capacity based on the entry or exit of one or a small number of financial guaranty reinsurers.

New entrants into the financial guaranty industry could have an adverse effect on our prospects either by furthering price competition or by reducing the aggregate demand for our reinsurance as a result of additional insurance capacity. The most significant barriers to entry for new financial guaranty competitors are rating agency requirements and regulatory capital requirements, as well as the limited availability of experienced management. New entrants or additional reinsurance capacity would likely have an adverse effect on our business. An investor group, which includes MBIA, recently announced the formation of a new Bermuda-based triple-A rated financial guaranty reinsurer, and we cannot assure you what impact, if any, such entity may have on the financial guaranty reinsurance market.

With respect to mortgage guaranty reinsurance, we compete with a number of other reinsurance companies as well as with alternatives to reinsurance, including risk-sharing arrangements with affiliates of the mortgage insurers and lender-owned captives. Many of these competitors have greater experience and relationships in these markets. See also "Business Competition."

We are dependent on key executives and the loss of any of these executives, or our inability to retain other key personnel, could adversely affect our business.

Our success substantially depends upon our ability to attract and retain qualified employees and upon the ability of our senior management and other key employees to implement our business strategy. We believe there are only a limited number of available qualified executives in the business lines in which we compete. Although we are not aware of any planned departures, we rely substantially upon the services of Dominic J. Frederico, our President and Chief Executive Officer, and Michael J.

Schozer, the President of Assured Guaranty Corp. Although each of these individuals will have employment agreements with us, we cannot assure you that we will be able to retain their services. The loss of the services of either of these individuals or other key members of our management team could adversely affect the implementation of our business strategy, which could have a material adverse effect on our business. We do not currently maintain key man life insurance policies with respect to any of our employees. The inability to attract and retain other talented personnel could also adversely affect our business.

Reduction in staffing levels could adversely affect our ability to successfully implement our new business strategy.

In connection with the IPO and the implementation of our new business strategy, we are reducing our total headcount to approximately 100 people through reductions in force and attrition. Some of our employees who have left or who have been terminated had relevant experience and their loss could adversely affect our ability to successfully implement our new business strategy. In addition, if our new business strategy is successful in generating a substantial amount of new business, we may be required to seek additional staff. We cannot assure you that we will be able to identify and hire experienced new staff on a timely basis.

Our business could be adversely affected by Bermuda employment restrictions.

Our location in Bermuda may serve as an impediment to attracting and retaining experienced personnel. Special considerations apply to our Bermuda operations. Under Bermuda law, non-Bermudians, other than spouses of Bermudians and individuals holding permanent resident certificates or working resident certificates, are not permitted to engage in any gainful occupation in Bermuda without a work permit issued by the Bermuda government. A work permit is only granted or extended if the employer can show that, after a proper public advertisement, no Bermudian, spouse of a Bermudian or individual holding a permanent resident certificate or working resident certificate is available who meets the minimum standards for the position. The Bermuda government has announced a policy that places a six-year term limit on individuals with work permits, subject to specified exemptions for persons deemed to be key employees. All of our Bermuda-based employees who require work permits have been granted provisional permits by the Bermuda government, including our President and Chief Executive Officer, Chief Financial Officer, General Counsel and Secretary and Chief Actuary. It is possible that we could lose the services of one or more of our key employees if we are unable to obtain or renew their work permits, which could have a material adverse affect on our business.

We may be adversely affected by interest rate changes affecting the performance of our investment portfolio.

Our operating results are affected, in part, by the performance of our investment portfolio. Changes in interest rates could also have an adverse effect on our investment income. For example, if interest rates decline, funds reinvested will earn less than expected. Our investment portfolio contains interest rate-sensitive instruments, such as bonds, which may be adversely affected by changes in interest rates. See "Management's Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies Valuation of Investments."

In addition, our investment portfolio includes mortgage-backed securities. As of December 31, 2003, mortgage-backed securities constituted approximately 25% of our invested assets. As with other fixed maturity investments, the fair market value of these securities fluctuates depending on market and other general economic conditions and the interest rate environment. Changes in interest rates can expose us to significant prepayment risks on these investments. In periods of declining interest rates, mortgage prepayments generally increase and mortgage-backed securities are prepaid more quickly,

requiring us to reinvest the proceeds at then-current market rates. During periods of rising interest rates, the frequency of prepayments generally decreases. Mortgage-backed securities having an amortized value less than par (*i.e.*, purchased at a discount) may incur a decrease in yield or a loss as a result of slower prepayment.

Interest rates are highly sensitive to many factors, including monetary policies, domestic and international economic and political conditions and other factors beyond our control. We do not engage in active management, or hedging, of interest rate risk, and may not be able to mitigate interest rate sensitivity effectively.

The performance of our invested assets affects our results of operations and cash flows.

Income from our investment portfolio is one of the primary sources of cash flows supporting our operations and claim payments. For the years ended December 31, 2003, 2002 and 2001, our net investment income was \$96.3 million, \$97.2 million and \$99.5 million, respectively, in each case exclusive of net realized gains on investments. If our calculations with respect to our policy liabilities are incorrect, or if we improperly structure our investments to meet these liabilities, we could have unexpected losses, including losses resulting from forced liquidation of investments before their maturity. The investment policies of our insurance subsidiaries are subject to insurance law requirements, and may change depending upon regulatory, economic and market conditions and the existing or anticipated financial condition and operating requirements, including the tax position, of our businesses.

We have retained Lazard Freres Asset Management and Hyperion Capital Management, Inc. to manage our investment portfolio. The performance of our invested assets is subject to their performance in selecting and managing appropriate investments. These investment managers have discretionary authority over our investment portfolio within the limits of our investment guidelines.

Our net income may be volatile because a portion of the credit risk we assume is in the form of credit derivatives that are accounted for under FAS 133, which requires that these instruments be marked-to-market quarterly.

Any event causing credit spreads (*i.e.*, the difference in interest rates between comparable securities having different credit risk) on an underlying security referenced in a credit derivative in our portfolio either to widen or to tighten will affect the fair value of the credit derivative and may increase the volatility of our earnings. Credit derivatives are classified as derivatives under Statement of Financial Accounting Standards No. 133. Derivatives must be accounted for either as assets or liabilities on the balance sheet and measured at fair market value. Although there is no cash flow effect from this "marking to market," net changes in the fair market value of the derivative are reported in our statement of operations and therefore will affect our reported earnings. If the derivative is held to maturity and no credit loss is incurred, any gains or losses previously reported would be offset by corresponding gains or losses at maturity. See "Management's Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies Valuation of Derivative Financial Instruments."

Common events that may cause credit spreads on an underlying municipal or corporate security referenced in a credit derivative to fluctuate include changes in the state of national or regional economic conditions, industry cyclicality, changes to a company's competitive position within an industry, management changes, changes in the ratings of the underlying security, movements in interest rates, default or failure to pay interest, or any other factor leading investors to revise expectations about the issuer's ability to pay principal and interest on its debt obligations. Similarly, common events that may cause credit spreads on an underlying structured security referenced in a credit derivative to fluctuate may include the occurrence and severity of collateral defaults, changes in demographic trends

and their impact on the levels of credit enhancement, rating changes, changes in interest rates or prepayment speeds, or any other factor leading investors to revise expectations about the risk of the collateral or the ability of the servicer to collect payments on the underlying assets sufficient to pay principal and interest.

An increase in our subsidiaries' risk-to-capital ratio or leverage ratio may prevent them from writing new insurance.

Rating agencies and insurance regulatory authorities impose capital requirements on our insurance subsidiaries. These capital requirements, which include risk-to-capital ratios, leverage ratios and surplus requirements, limit the amount of insurance that our subsidiaries may write. Our insurance subsidiaries have several alternatives available to control their risk-to-capital ratios and leverage ratios, including obtaining capital contributions from us, purchasing reinsurance or entering into other loss mitigation agreements, or reducing the amount of new business written. However, a material reduction in the statutory capital and surplus of a subsidiary, whether resulting from underwriting or investment losses or otherwise, or a disproportionate increase in the amount of risk in force, could increase a subsidiary's risk-to-capital ratio or leverage ratio. This in turn could require that subsidiary to obtain reinsurance for existing business (which may not be available, or may be available on terms that we consider unfavorable), or add to its capital base to maintain its financial strength ratings. Failure to maintain such ratings could limit that subsidiary's ability to write new business, which could materially adversely affect our results of operations and financial condition.

We may require additional capital in the future, which may not be available or may be available only on unfavorable terms.

Our capital requirements depend on many factors, including our in-force book of business and rating agency capital requirements. To the extent that our existing capital is insufficient to meet these requirements and/or cover losses, we may need to raise additional funds through financings or curtail our growth and reduce our assets. Any equity or debt financing, if available at all, may be on terms that are not favorable to us. If our need for capital arises because of significant losses, the occurrence of these losses may make it more difficult for us to raise the necessary capital. If we cannot obtain adequate capital on favorable terms or at all, our business, operating results and financial condition could be adversely affected.

Adequate soft capital support may not be available.

Financial guaranty insurers and reinsurers typically rely on providers of lines of credit, credit swap facilities and similar capital support mechanisms (often referred to as "soft capital") to supplement their "hard capital." The ratings of soft capital providers directly affect the level of capital credit which the rating agencies attribute to the financial guaranty insurer or reinsurer when rating its financial strength. We intend to maintain soft capital facilities with providers having ratings adequate to provide the desired capital credit, although no assurance can be given that one or more of the rating agencies will not downgrade or withdraw the applicable ratings of such providers in the future. In addition, we cannot assure you that an acceptable replacement provider would be available in that event.

We may require additional liquidity in the future, which may not be available or may be available only on unfavorable terms.

We require liquidity in order to pay our operating expenses, interest on our debt and dividends on our common shares, and to make capital investments in our operating subsidiaries. We anticipate that our need for liquidity will be met by (1) the ability of our subsidiaries to pay dividends or to make other payments to us, (2) external financings, and (3) income from our investment portfolio. Some of our subsidiaries are subject to legal and rating agency restrictions on their ability to pay dividends and

make other permitted payments, and external financing may or may not be available to us in the future on satisfactory terms. Our other subsidiaries are subject to legal restrictions on their ability to pay dividends and distributions. See "Dividend Policy" and "Business Regulation." While we believe that we will have sufficient liquidity to satisfy our needs over the next 12 months, there can be no assurance that adverse market conditions, changes in insurance regulatory law or changes in general economic condition that adversely affect our liquidity will not occur. Similarly, there can be no assurance that adequate liquidity will be available to us on favorable terms in the future.

Liquidity at our operating subsidiaries is used to pay operating expenses, claims, reinsurance premiums and dividends to us, as well as, where appropriate, to make capital investments in their own subsidiaries. Liquidity at the issuer is also used to make payments under the Tax Allocation Agreement with ACE Financial Services, described under "Relationship with ACE Tax Allocation Agreement." While we believe that the operating cash flows of our subsidiaries will be sufficient to meet their needs, we cannot assure you that this will be the case, nor can we assure you that existing liquidity facilities will prove adequate to their needs, or be available to them on favorable terms in the future.

Changes in tax laws could reduce the demand or profitability of financial guaranty insurance, or negatively impact our investment portfolio.

Any material change in the U.S. tax treatment of municipal securities, the imposition of a "flat tax," the imposition of a national sales tax in lieu of the current federal income tax structure in the United States, or changes in the treatment of dividends, could adversely affect the market for municipal obligations and, consequently, reduce the demand for financial guaranty insurance and reinsurance of such obligations.

The Jobs and Growth Tax Relief Reconciliation Act of 2003, enacted in May 2003, significantly reduces in certain situations the federal income tax rate for individuals on dividends and long-term capital gains through 2008. This tax change may adversely affect the market for municipal obligations and, consequently, reduce the demand for financial guaranty insurance and reinsurance of these obligations, which could reduce our revenue and profitability from the writing of such insurance and reinsurance. Future potential changes in U.S. tax laws might also affect demand for municipal securities and for financial guaranty insurance and reinsurance of those obligations.

Changes in U.S. federal, state or local laws that materially adversely affect the tax treatment of municipal securities or the market for those securities, or other changes negatively affecting the municipal securities market, also may adversely impact our investment portfolio, a significant portion of which is invested in tax-exempt instruments. These adverse changes may adversely affect the value of our tax-exempt portfolio, or its liquidity.

Legislative and regulatory changes and interpretations could harm our business.

Changes in laws and regulations affecting insurance companies, the municipal and structured securities markets, the financial guaranty and mortgage guaranty insurance and reinsurance markets and the credit derivatives markets, as well as other governmental regulations, may subject us to additional legal liability, or affect the demand for the products that we provide. For example, recent uncertainty regarding the accounting for structured securities significantly, though temporarily, reduced new issuances of certain types of structured securities.

Our ability to meet our obligations, including in respect of the notes and the guarantees, may be constrained by our holding company structure.

Assumed Guaranty and Holdings are both holding companies and, as such, have no direct operations of their own. They do not expect to have any significant operations or assets other than their ownership of the shares of their subsidiaries. Dividends and other permitted payments from their

operating subsidiaries are expected to be their primary source of funds to meet ongoing cash requirements, including debt service payments and other expenses. Their insurance subsidiaries are subject to regulatory and rating agency restrictions limiting their ability to declare and to pay dividends and make other payments to Assured Guaranty or Holdings, as applicable. The inability of our insurance subsidiaries to pay sufficient dividends and make other permitted payments to us could have a material adverse effect on our ability to satisfy our ongoing cash requirements, including in respect of the notes and the guarantees, and on our ability to pay dividends to our shareholders. For more information regarding these limitations, see "Business Regulation."

Our insurance subsidiaries have no obligation to pay interest or principal due on the notes or to make funds available to us for that purpose, whether in the form of loans, dividends or other distributions. Accordingly, our ability to repay the notes at maturity or otherwise may be dependent upon our ability to refinance the notes, which will in turn depend, in large part, upon factors beyond our control.

ACE has the ability to exert significant influence over our operations.

ACE beneficially owns approximately 35% of our common shares (approximately 25% if the underwriters' option to purchase additional common shares in the IPO is exercised in full). In addition, two of our directors, including our President and Chief Executive Officer, are also directors of ACE. Prior to the IPO, our Chairman, Donald Kramer, was Vice Chairman and a director of ACE and, though he is no longer a director of ACE, remains employed by ACE. ACE will have the ability to exert significant influence over our policies and affairs, the election of our board of directors and any action requiring a shareholder vote, including amendments to our Bye-Laws and approval of business combinations. The interests of ACE may differ from the interests of our other shareholders in some respects. See "Relationship with ACE."

ACE may have conflicts of interest with us.

ACE has entered into agreements with us which may give rise to conflicts of interest. See "Formation Transactions" and "Relationship with ACE." In addition, ACE has invested in, and may in the future invest in, other entities engaged in or intending to engage in financial or mortgage guaranty insurance and reinsurance, some of which may compete with us. ACE has also entered into, or may in the future enter into, agreements with companies that may compete with us. We do not have any agreement or understanding with ACE regarding the resolution of potential conflicts of interest. In addition, we may not be in a position to influence ACE's decision to engage in activities that would give rise to a conflict of interest. ACE may take actions that are not in our best interests.

We are dependent on certain contractual arrangements with ACE and we may be unable to replace these arrangements with similar or more favorable agreements upon their expiration.

In connection with the IPO and the transactions described under "Formation Transactions" and "Relationships with ACE," we and our insurance subsidiaries have entered into a series of agreements with ACE and its affiliates. See "Formation Transactions" and "Relationship with ACE." The board of directors existing prior to the IPO has approved the terms of these agreements, but the agreements will not be reviewed or approved by the independent directors who have joined our board upon completion of the IPO. These agreements became effective shortly after the completion of the IPO. Several of these agreements govern our relationship with ACE and its affiliates with respect to various services that ACE and its affiliates have agreed to provide to us following the completion of the IPO. After the expiration of these agreements, we may not be able to replace these services and arrangements in a timely manner or on terms and conditions, including cost, as favorable as those we have with ACE. In addition, we have entered into reinsurance arrangements and other transactions with ACE with respect to the businesses that we have exited in connection with the IPO. These arrangements and other transactions have been approved by our board existing prior to the IPO but have not been and will not be approved by the independent directors that have joined our board since completion of the IPO. See "Relationship with ACE" and "Business - Other."

We will have significant reinsurance recoverables from ACE.

As previously described, we have entered into reinsurance arrangements and other transactions with ACE with respect to the businesses that we have exited in connection with the IPO. As a result, we expect to have substantial reinsurance recoverables from ACE and therefore will be subject to the risk that ACE cannot or will not pay amounts owed to us under these reinsurance arrangements. In connection with the IPO, we entered into several reinsurance agreement with subsidiaries of ACE described under "Relationships with ACE Reinsurance Transactions" that are considered retroactive reinsurance contracts. Under applicable accounting rules related to retroactive reinsurance, we would not be able recognize a reinsurance recoverable on future adverse loss development, if applicable, until we pay the underlying loss and we are reimbursed by ACE. This difference in timing will cause our results of operations to otherwise be lower during the period in which we recognize a loss for adverse development on one of these agreements, notwithstanding the reinsurance, and will be recaptured through income in the period in which we actually pay the underlying loss.

Assured Guaranty is a Bermuda company and it may be difficult for you to enforce judgments against Assured Guaranty or against its directors and executive officers.

Assured Guaranty is incorporated pursuant to the laws of Bermuda and its business is based in Bermuda. In addition, certain of Assured Guaranty's directors and officers reside outside the United States, and a portion of its assets and the assets of such persons may be located in jurisdictions outside the United States. As such, it may be difficult or impossible to effect service of process within the United States upon Assured Guaranty or those persons, or to recover against Assured Guaranty or them on judgments of U.S. courts, including judgments predicated upon the civil liability provisions of the U.S. federal securities laws. Further, no claim may be brought in Bermuda against Assured Guaranty or its directors and officers in the first instance for violation of U.S. federal securities laws because these laws have no extraterritorial application under Bermuda law and do not have force of law in Bermuda; however, a Bermuda court may impose civil liability, including the possibility of monetary damages, on it or its directors and officers if the facts alleged in a complaint constitute or give rise to a cause of action under Bermuda law.

Assured Guaranty has been advised by Conyers Dill & Pearman, our special Bermuda counsel, that there is doubt as to whether the courts of Bermuda would enforce judgments of U.S. courts obtained in actions against Assured Guaranty or its directors and officers, as well as the experts named

herein, predicated upon the civil liability provisions of the U.S. federal securities laws, or original actions brought in Bermuda against Assured Guaranty or such persons predicated solely upon U.S. federal securities laws. Further, Assured Guaranty has been advised by Conyers Dill & Pearman that there is no treaty in effect between the United States and Bermuda providing for the enforcement of judgments of U.S. courts, and there are grounds upon which Bermuda courts may not enforce the judgments of U.S. courts. Some remedies available under the laws of U.S. jurisdictions, including some remedies available under the U.S. federal securities laws, may not be allowed in Bermuda courts as contrary to public policy in Bermuda. Because judgments of U.S. courts are not automatically enforceable in Bermuda, it may be difficult for you to recover against Assured Guaranty based upon such judgments.

A newspaper quote from a proposed member of the underwriting syndicate in the IPO could result in Securities Act liability to us.

Prior to the effectiveness of the registration statement covering our IPO, an analyst of Fox-Pitt, Kelton, Inc, a proposed member of the underwriting syndicate in the IPO, was quoted in a newspaper article expressing an opinion as to the expected trading value of our common shares relative to other companies in our industry. We did not have any involvement in the preparation of the article nor did we ask the analyst to express any opinion regarding this offering or the expected trading value of our common shares. Fox-Pitt, Kelton, Inc. elected not to participate in the IPO.

An investor in our IPO might assert that the newspaper article constitutes a prospectus that does not meet the requirements of the Securities Act of 1933. If the newspaper article were to be found to be a prospectus that did not meet the requirements of the Securities Act, persons who read the newspaper article and who purchased our common shares in the IPO may have the right, for a period of one year from the date of the violation, to obtain recovery of the consideration paid in connection with their purchase of our common shares or, if they had already sold their common shares, attempt to recover losses resulting from their purchase of our common shares. Any liability would depend on the number of common shares purchased by the recipients.

Risks Relating to the Notes and the Guarantees

The terms of the notes and the guarantees do not restrict our ability to incur additional unsecured debt, pay dividends or repurchase our securities.

Neither the guarantor nor its subsidiaries, including the issuer, are restricted under the terms of the indenture governing the notes from incurring additional unsecured debt. If the guarantor or the issuer were to incur additional debt or liabilities, their ability to pay their obligations in respect of the guarantees and the notes, as the case may be, could be adversely affected. In addition, we are not restricted from paying dividends or issuing or repurchasing our securities under the indenture.

The notes will be effectively subordinated to the debts and obligations of our subsidiaries.

Since both the guarantor and the issuer are holding companies, their rights and the rights of their creditors (including the holders of the notes) to participate in any distribution of the assets of any subsidiary upon such subsidiary's liquidation or reorganization or otherwise would be subject to prior claims of the subsidiary's creditors, except to the extent that the guarantor or the issuer, as the case may be, may itself be a creditor with recognized claims against the subsidiary. The right of creditors of the issuer (including the holders of the notes) and the guarantor (including the holders of the notes who are creditors of the guarantor by virtue of the guarantees) to participate in the distribution of the stock owned by them in certain of their respective subsidiaries, including their insurance subsidiaries, may also be subject to approval by certain insurance regulatory and other authorities having jurisdiction over such subsidiaries.

None of our subsidiaries will guarantee the notes. As a result of the foregoing, the notes will effectively be subordinated to the prior payment of all of the existing and future liabilities and obligations (including trade payables) of our subsidiaries (other than the issuer). The notes do not limit the ability of any of our subsidiaries to incur additional indebtedness, liabilities and obligations.

Our option to redeem the notes in certain circumstances may adversely affect your return on the notes.

The notes will be redeemable at our option under the circumstances and on the terms described under "Description of Notes and Guarantees." Redemption may occur at a time when prevailing interest rates are relatively low. If this happens, you generally will not be able to reinvest the redemption proceeds in a comparable security at an effective interest rate as high as that of the redeemed notes.

Absence of a public market for the notes could cause purchasers of the notes to be unable to resell them for an extended period of time.

There is no established public trading market for the notes. The notes will not be listed on any securities exchange or included in any automated quotation system. We cannot assure you that an active trading market for the notes will develop or, if such market develops, how liquid it will be. If a trading market does not develop or is not maintained, holders of the notes may experience difficulty in reselling, or an inability to sell, the notes. If a market for the notes develops, any such market may be discontinued at any time. If a public trading market develops for the notes, future trading prices of the notes will depend on many factors, including, among other things, prevailing interest rates, our operating results and the market for similar securities. Depending on prevailing interest rates, the market for similar securities and other factors, including our financial condition, the notes may trade at a discount from their principal amount.

FORWARD-LOOKING STATEMENTS

Some of the statements under "Prospectus Summary," "Risk Factors," "Management's Discussion and Analysis of Financial Condition and Results of Operations," "Business" and elsewhere in this prospectus may include forward-looking statements which reflect our current views with respect to future events and financial performance. These statements include forward-looking statements both with respect to us specifically and the insurance and reinsurance industries in general. Statements which include the words "expect," "intend," "plan," "believe," "project," "anticipate," "may," "will," "continue," "further," "seek," and similar words or statements of a future or forward-looking nature identify forward-looking statements for purposes of the federal securities laws or otherwise.

All forward-looking statements address matters that involve risks and uncertainties. Accordingly, there are or will be important factors that could cause our actual results to differ materially from those indicated in these statements. We believe that these factors include but are not limited to those described under "Risk Factors" above and the following:

downgrades of the financial strength ratings assigned by the major rating agencies to any of our insurance subsidiaries at any time, which has occurred in the past;

our inability to execute our new business strategy;

developments in the world's financial and capital markets that adversely affect our loss experience, the demand for our products or our investment returns;

more severe losses or more frequent losses associated with our products;

changes in regulation or tax laws applicable to us, our subsidiaries or customers;

decreased demand for our insurance or reinsurance products or increased competition in our markets;

loss of key personnel;

the effects of mergers, acquisitions and divestitures;

changes in accounting policies or practices; and

changes in general economic conditions, including interest rates and other factors.

The foregoing review of important factors should not be construed as exhaustive, and should be read in conjunction with the other cautionary statements that are included in this prospectus. We undertake no obligation publicly to update or review any forward-looking statement, whether as a result of new information, future developments or otherwise.

If one or more of these or other risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, actual results may vary materially from what we projected. Any forward-looking statements you read in this prospectus reflect our current views with respect to future events and are subject to these and other risks, uncertainties and assumptions relating to our operations, results of operations, growth strategy and liquidity. All subsequent written and oral forward-looking statements attributable to us or to individuals acting on our behalf are expressly qualified in their entirety by this paragraph. You should specifically consider the factors identified in this prospectus that could cause actual results to differ before making an investment decision.

FORMATION TRANSACTIONS

Assured Guaranty Corp., our financial guaranty insurance subsidiary, was organized in 1985 and has been writing financial guaranty coverages since January 1988. In April 1992, Assured Guaranty Corp.'s parent, Capital Re, became a public company. In February 1994, Capital Re entered the mortgage business with the formation of Assured Guaranty Mortgage, a New York domiciled insurance company. Shortly thereafter, AGRO was formed as a Bermuda-domiciled insurance company. In December 1999, ACE acquired Capital Re.

Assured Guaranty was incorporated in Bermuda in August 2003 for the sole purpose of becoming a holding company for ACE's subsidiaries conducting its financial and mortgage guaranty businesses, which we refer to as the "transferred businesses," in connection with our IPO. Certain of the transferred businesses were originally conducted by subsidiaries of Capital Re.

As part of the overall plan of formation of Assured Guaranty, the following formation transactions occurred:

ACE, through a U.S. subsidiary, formed Assured Guaranty US Holdings as a Delaware holding company to hold the shares of Assured Guaranty Corp. and Assured Guaranty Financial Products.

ACE's U.S. subsidiary transferred the shares of Assured Guaranty Corp. and Assured Guaranty Financial Products to Assured Guaranty US Holdings in exchange for stock of Assured Guaranty US Holdings and a \$200 million promissory note.

AGRO transferred 100% of the stock ownership in ACE Capital Title to ACE Bermuda in exchange for a \$39.5 million promissory note which has since been repaid.

Subsequent to entering into the underwriting agreement with respect to the IPO, ACE transferred its common shares to ACE Bermuda and caused:

its U.S. subsidiary to transfer 100% of the stock ownership in Assured Guaranty US Holdings and Assured Guaranty Finance Overseas to us in exchange for 35,171,000 of our common shares and two promissory notes of Assured Guaranty in an aggregate amount of \$1 million; and

a Bermuda subsidiary to transfer 100% of the stock of AGRI to us in exchange for 38,629,000 of our common shares and a \$1 million promissory note of Assured Guaranty.

Each of our operating subsidiaries conducted business under names including "ACE," "AGR" and/or "Capital Re." As part of the formation transactions we have changed, or are in the process of changing, the names of each of these subsidiaries to the respective names set forth in this prospectus (or derivations of these names).

ACE and its subsidiaries also entered into a number of transactions with our subsidiaries in order to reinsure or otherwise assume certain risks related to the businesses reported in our other segment. See "Relationship with ACE."

We also entered into a number of other agreements with ACE and its subsidiaries that govern certain aspects of our relationship with ACE after the IPO, including services agreements under which ACE and its subsidiaries have agreed to provide certain services to us for a period of time after the IPO.

ACE beneficially owns 26,000,000 common shares, or approximately 35% of our outstanding common shares (18,650,000 common shares, or approximately 25% of our outstanding common shares if the underwriters' option to purchase additional common shares in the IPO is exercised in full).

In addition, upon completion of these formation transactions and completion of the IPO, unvested stock options to purchase ACE ordinary shares held by our officers or employees immediately vested and any unvested restricted ACE ordinary shares held by these individuals were forfeited. We expect to incur an after-tax charge in the second quarter of 2004 of approximately \$9.5 million relating to the accelerated vesting of stock options and additional compensation we are providing to our officers or employees in exchange for their forfeiture of their restricted shares. See "Management Transaction from ACE to Assured Guaranty Plans."

ASSURED GUARANTY US HOLDINGS INC.

Assured Guaranty US Holdings Inc., the issuer of the notes, was formed in connection with the transactions described under "Formation Transactions" as a holding company to hold the shares of Assured Guaranty Corp. and Assured Guaranty Financial Products. It is a wholly owned subsidiary of Assured Guaranty and was formed under the laws of the State of Delaware in February 2004. Its principal executive offices are at 1325 Avenue of the Americas, New York, New York, and its telephone number is (212) 974-0100.

USE OF PROCEEDS

The net proceeds from the issue of the notes are estimated to be approximately \$ (after deducting underwriting discounts and commissions and other offering expenses) and will be used to repay indebtedness owed to a subsidiary of ACE that was incurred in connection with the formation transactions described under "Formation Transactions." This indebtedness matures at the earlier of (i) September 30, 2004 and (ii) the closing of this offering. The indebtedness bears interest at 1.5% per year.

CAPITALIZATION OF ASSURED GUARANTY

The table below shows Assured Guaranty's combined capitalization as of December 31, 2003, on a pro forma basis giving effect to the formation transactions described under "Formation Transactions," the transactions described under "Supplemental Pro Forma Condensed Combined Financial Information (Unaudited)" beginning on page F-49 and as further adjusted to give effect to issuance of the notes in this offering and the application of the net proceeds from this offering.

You should read this table in conjunction with "Use of Proceeds," "Selected Combined Financial Information" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the combined financial statements and related notes that are included elsewhere in this prospectus.

	As of December 31, 2003		
	Actual	Pro forma	Pro forma As Adjusted
(\$ in millions, except per share amounts)			
Debt:			
Monthly income preferred securities of affiliate ⁽¹⁾	\$ 75.0		\$
Promissory note to ACE		\$ 200.0	
Notes offered hereby			\$ 200.0
Total debt	\$ 75.0	\$ 200.0	\$ 200.0
Shareholder's equity:			
Common shares, \$0.01 par value, 500,000,000 shares authorized, 75,937,417 shares issued and outstanding pro forma	\$ 16.4	\$ 0.8	\$ 0.8
Additional paid-in capital	955.5	1,247.5	1,247.5
Unearned stock grant compensation	(5.5)	(17.8)	(17.8)
Retained earnings	390.0		
Accumulated other comprehensive income	81.2	81.2	81.2
Total shareholder's equity	1,437.6	1,311.6	1,311.6
Total capitalization	\$ 1,512.6	\$ 1,511.6	\$ 1,511.6
Ratio of total debt to total capitalization	5.0%	13.2%	13.2%

(1)

Represents \$75 million of Monthly Income Preferred Securities of Capital Re LLC. Capital Re LLC remains a subsidiary of ACE.

SELECTED COMBINED FINANCIAL INFORMATION

The following table sets forth selected combined financial and other information of Assured Guaranty. The selected combined statement of operations data for each of the years ended December 31, 2003, 2002, and 2001 and the selected combined balance sheet data as of December 31, 2003 and 2002 are derived from Assured Guaranty's audited combined financial statements, which have been prepared in accordance with GAAP and appear elsewhere in this prospectus. The selected combined statement of operations data for the year ended December 31, 2000 and the selected combined balance sheet data as of December 31, 2001 are derived from Assured Guaranty's audited combined financial statements, which have been prepared in accordance with GAAP. The selected combined statement of operations data for the year ended December 31, 1999 and the selected combined balance sheet data as of December 31, 2000 and 1999 are derived from Assured Guaranty's unaudited combined financial statements.

You should read the following selected combined financial information together with the other information contained in this prospectus, including "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the combined financial statements and related notes included elsewhere in this prospectus.

	Year Ended December 31,				
	2003	2002	2001	2000	1999 ⁽¹⁾
	(\$ in millions)				
Statement of operations data:					
Gross written premiums	\$ 349.2	\$ 417.2	\$ 442.9	\$ 206.0	\$ 203.5
Net written premiums ⁽²⁾	491.5	352.5	206.6	188.6	198.9
Net earned premiums	\$ 310.9	\$ 247.4	\$ 293.5	\$ 140.7	\$ 192.6
Net investment income	96.3	97.2	99.5	98.1	73.3
Net realized investment gains (losses)	5.5	7.9	13.1	8.6	(6.5)
Unrealized gains (losses) on derivative financial instruments	98.4	(54.2)	(16.3)		
Other income	1.2	3.6	2.9	2.5	5.0
Total revenues	512.3	302.0	392.9	249.9	264.4
Loss and loss adjustment expenses	144.6	120.3	177.5	30.4	201.8
Profit commission expense	9.8	8.5	9.0	10.8	11.0
Acquisition costs	64.9	48.4	51.1	49.1	42.3
Operating expenses	41.0	31.0	29.8	26.2	24.1
Goodwill amortization			3.8	3.8	
Interest expense	5.7	10.6	11.5	11.5	11.5
Total expenses	266.1	218.8	282.8	131.8	290.7
Income (loss) before income taxes	246.2	83.2	110.1	118.1	(26.4)
Provision (benefit) for income taxes	31.7	10.6	22.2	24.9	(10.6)
Net income before cumulative effect of new accounting standard	214.5	72.6	87.9	93.2	(15.7)
Cumulative effect of new accounting standard, net of taxes			(24.1)		
Net income (loss)	\$ 214.5	\$ 72.6	\$ 63.8	\$ 93.2	\$ (15.7)

Year Ended December 31,

	2003	2002	2001	2000	1999
--	------	------	------	------	------

(\$ in millions)

Balance sheet data (end of period):

Investments and cash	\$ 2,222.1	\$ 2,061.9	\$ 1,710.8	\$ 1,549.6	\$ 1,292.3
Prepaid reinsurance premiums	11.0	179.5	171.5	28.8	28.6
Total assets	2,857.9	2,719.9	2,322.1	1,913.7	1,622.2
Unearned premium reserve	625.4	613.3	500.3	444.6	396.8
Reserve for losses and loss adjustment expenses	522.6	458.8	401.1	171.0	195.4
Long-term debt	75.0	75.0	150.0	150.0	150.0
Total liabilities	1,420.2	1,462.6	1,260.4	919.2	840.7
Accumulated other comprehensive income	81.2	89.0	43.3	42.3	
Shareholder's equity	1,437.6	1,257.2	1,061.6	994.5	781.6

Per share data:⁽³⁾

Earnings per share:					
Basic	\$ 2.86	\$ 0.97	\$ 0.85	\$ 1.24	\$ (0.21)
Diluted	2.86	0.97	0.85	1.24	(0.21)
Book value per share	19.17	16.76	14.15	13.26	10.42

GAAP financial information:

Loss and loss adjustment expense ratio ⁽⁴⁾	46.5%	48.6%	60.5%	21.6%	104.8%
Expense ratio ⁽⁵⁾	37.2	35.5	30.6	61.2	40.2

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

Combined ratio	83.7%	84.1%	91.1%	82.8%	145.0%
Ratio of earnings to fixed charges ⁽⁶⁾	36.49x	8.18x	9.90x	10.89x	
Pro forma ratio of earnings to fixed charges ⁽⁶⁾	19.18x				

Statutory financial information:

Contingency reserve ⁽⁷⁾	\$	410.5	\$	315.5	\$	228.9	\$	183.8	\$	155.1
Policyholders' surplus		980.5		835.4		833.2		786.0		464.6

Additional financial guaranty information (end of period):

Net in-force business (principal and interest)	\$	130,047	\$	124,082	\$	117,909	\$	102,744	\$	94,035
Net in-force business (principal only)		87,524		80,394		75,249		65,756		59,073
Present value of gross premiums written ⁽⁸⁾		238.8		215.5		195.0		139.5		
Net present value of installment premiums in-force ⁽⁹⁾		309.8		260.2		159.7		94.0		

- (1) ACE purchased the entities comprising Assured Guaranty as part of its purchase of Capital Re on December 30, 1999. The selected combined statement of operations data for the year ended December 31, 1999 reflects the financial position and results of operations of the entities as included in Capital Re's financial statements during those periods. The remaining selected combined financial information represents the financial position and results of operations of the entities comprising Assured Guaranty based on ACE's purchase accounting basis in the entities. The principal differences are \$94.6 million of goodwill at December 31, 1999 and related goodwill amortization of \$3.8 million in each of the years ended December 31, 2001 and 2000.
- (2) Net written premiums exceeded gross written premiums for the year ended December 31, 2003 due to \$154.8 million of return premium from two terminated ceded reinsurance contracts.
- (3) Based on 75,000,000 shares outstanding immediately prior to the IPO.
- (4) The loss and loss adjustment expense ratio is calculated by dividing loss and loss adjustment expenses by net earned premiums.
- (5) The expense ratio is calculated by dividing the sum of profit commission expense, acquisition costs and operating expenses by net earned premiums.
- (6) For purposes of computing these ratios, earnings consist of net income before income tax expense (excluding interest costs capitalized) plus fixed charges to the extent that such charges are included in the determination of earnings. Fixed charges consist of interest costs

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

(including interest costs capitalized) plus one-third of minimum rental payments under operating leases (estimated by management to be the interest factor of such rentals). Due to our loss in 1999, our fixed charges exceeded our earnings (as computed under applicable SEC rules for this purpose) by \$26.4 million. Pro forma ratio is calculated by assuming the sale of \$200,000,000 aggregate principal amount of notes in this offering bearing an interest rate of 6.00%, the net proceeds of which are applied as discussed under "Use of Proceeds."

- (7) Under statutory accounting principles, financial guaranty and mortgage guaranty insurers are required to establish contingency reserves based on a specified percentage of premiums. A contingency reserve is an additional liability reserve established to protect policyholders against the effects of adverse economic developments or cycles or other unforeseen circumstances.
- (8) Represents gross premiums related to financial guaranty contracts written in the current period, including the full amount of upfront premiums received and the present value of all installment premiums, discounted at 6% per year. See "Management's Discussion and Analysis of Financial Condition and Results of Operations - Segment Results of Operations" for a reconciliation to gross written premiums. Information for years prior to 2000 is unavailable.
- (9) Represents the present value of installment premiums on all in-force financial guaranty business, net of reinsurance ceded and ceding commissions, discounted at 6% per year. Information for years prior to 2000 is unavailable.

PRO FORMA COMBINED FINANCIAL INFORMATION OF ASSURED GUARANTY

As a newly formed company, Assured Guaranty has no actual results of operations. In this prospectus, we therefore are presenting pro forma combined financial information with respect to the businesses that ACE has transferred to us as described under "Formation Transactions," upon the completion of the IPO. This pro forma combined financial information is intended to illustrate the performance of our business following completion of the IPO and as if we had commenced our operations as of the beginning of the year presented.

The pro forma adjustments include (a) the estimated incremental operating costs that we will incur as a stand-alone public company, primarily a holding company executive management team, board of directors' fees, directors' and officers' liability insurance, independent auditors' fees, and the cost of changes in vendors or payment terms related to certain services currently provided by ACE, (b) long-term debt included in the historical combined financial statements that will be excluded from the transactions described under "Formation Transactions," and interest thereon, (c) the estimated effects of debt expected to be issued (and related interest expense at 6% per year) and related return of capital to ACE as described under "Formation Transactions," (d) the incremental cost of separate executive stock option and restricted stock programs, and (e) related U.S. income taxes at 35%, where applicable.

We caution that the pro forma condensed combined balance sheet and pro forma condensed combined statement of operations presented herein are not indicative of the actual results that we will achieve once we commence operations. Many factors may cause our actual results to differ materially from the pro forma condensed combined balance sheet and statement of operations, including our exit from the lines of business included in our other segment, our underwriting results, the amount of our investment income, and other factors.

The following table summarizes the pro forma effects on historical combined net income for the year ended December 31, 2003 and on historical combined shareholder's equity as of December 31, 2003. Further details on the pro forma adjustments and the individual financial statement line items that will be affected are included in our supplemental pro forma condensed combined financial information (unaudited) included elsewhere in this prospectus. See "Supplemental Pro Forma Condensed Combined Financial Information (Unaudited)" beginning on page F-49.

	Year Ended December 31, 2003	As of December 31, 2003
	(\$ in millions)	
Historical combined net income	\$ 214.5	
Historical combined shareholder's equity		\$ 1,437.6
(a) Estimated incremental operating costs	(14.0)	
(b) Interest on long-term debt retained by ACE	5.7	
Long-term debt retained by ACE		75.0
(c) Interest on long-term debt to be issued	(12.0)	
Return of capital to ACE		(200.0)
(d) Stock option and restricted stock programs	(1.6)	(2.8)
(e) Related income tax benefit	5.0	1.8
Pro forma net income	\$ 197.6	
Pro forma shareholder's equity		\$ 1,311.6

**MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our combined financial statements and accompanying notes which appear elsewhere in this prospectus. It contains forward-looking statements that involve risks and uncertainties. Please see "Forward-Looking Statements" for more information. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those discussed below and elsewhere in this prospectus, particularly under the headings "Risk Factors" and "Forward-Looking Statements."

Executive Summary

We are a Bermuda-based company providing credit enhancement products to the municipal finance, structured finance and mortgage markets. We apply our credit expertise, risk management skills and capital markets experience to develop insurance, reinsurance and credit derivative products that meet the credit enhancement needs of our customers. We market our products directly and through financial institutions. We serve the U.S. and international markets.

Our financial results include three operating segments: financial guaranty direct, financial guaranty reinsurance and mortgage guaranty. For financial reporting purposes, we have a fourth segment, which we refer to as other. The other segment consists of a number of businesses that we have exited including equity layer credit protection, trade credit reinsurance, title reinsurance, life, accident and health reinsurance ("LA&H") and auto residual value reinsurance. Because we exited some of these businesses after December 31, 2003, our results of operations for the quarter ended March 31, 2004 will reflect the results of operations of these businesses through the date as of which we exited them.

We derive our revenues principally from premiums from our insurance, reinsurance and credit derivative businesses, net investment income, net realized gains and losses from our investment portfolio and unrealized gains and losses on derivative financial instruments. Our premiums are a function of the amount and type of contracts we write as well as prevailing market prices. We receive premiums on an upfront basis when the policy is issued or the contract is executed and/or on an installment basis over the life of the applicable transaction.

Our investment income is a function of our invested assets and the yield that we earn on those assets. The investment yield will be a function of market interest rates at the time of investment as well as the type, credit quality and maturity of our invested assets. In addition, we could realize capital gains or losses on securities in our investment portfolio as a result of changing market conditions, including changes in market interest rates, and changes in the credit quality of our invested assets.

Unrealized gains and losses on derivative financial instruments are a function of changes in the estimated fair value of our credit derivative contracts. We expect these unrealized gains and losses to fluctuate primarily based on changes in credit spreads and the credit quality of the referenced entities. We generally hold these derivative contracts to maturity. Where we hold a derivative contract to maturity, the cumulative unrealized gains and losses will net to zero if we incur no credit losses on that contract.

We expect that our expenses will primarily consist of losses and loss adjustment expenses ("LAE"), profit commission expense, acquisition costs, operating expenses, interest expense and income taxes. Losses and LAE will be a function of the amount and types of business we write. Losses and LAE are based upon estimates of the ultimate aggregate losses inherent in the portfolio. The risks that we will take have a low expected frequency of loss and generally will be investment grade at the time we accept the risk. Profit commission expense represents payments made to ceding companies generally based on the profitability of the business reinsured by us. Acquisition costs are related to the

production of new business. Certain acquisition costs are deferred and recognized over the period in which the related premiums are earned. Operating expenses consist primarily of salaries and other employee-related costs. These costs will not vary with the amount of premiums written. We estimate that our incremental expenses in connection with becoming a public company are approximately \$14.0 million per year, primarily attributable to the salaries of our executive officers and other public company expenses. In November 2003 and February 2004, we reduced our personnel and other expenses and, as a result, expect to save approximately \$16.0 million of operating expenses per year on an annualized basis. Interest expense will be a function of outstanding debt and the contractual interest rate related to that debt. Income taxes will be a function of our profitability and the applicable tax rate in the various jurisdictions in which we do business.

In connection with the IPO, we entered into several reinsurance agreement with subsidiaries of ACE described under "Relationship with ACE Reinsurance transactions" that are considered retroactive reinsurance contracts. Under applicable accounting rules related to retroactive reinsurance, we would not be able to recognize a reinsurance recoverable on future adverse loss development, if applicable, until we pay the underlying loss and we are reimbursed by ACE. This difference in timing will cause our results of operations to otherwise be lower during the period in which we recognize a loss for adverse development on one of these agreements, notwithstanding the reinsurance, and will be recaptured through income in the period in which we actually pay the underlying loss.

Critical Accounting Policies

Our combined financial statements include amounts that, either by their nature or due to requirements of GAAP, are determined using estimates and assumptions. The actual amounts realized could ultimately be materially different from the amounts currently provided for in our combined financial statements. We believe the items requiring the most inherently subjective and complex estimates to be reserves for losses and LAE, valuation of derivative financial instruments, valuation of investments, other than temporary impairments of investments, premium revenue recognition, deferred acquisition costs and deferred income taxes. An understanding of our accounting policies for these items is of critical importance to understanding our combined financial statements. The following discussion provides more information regarding the estimates and assumptions used for these items and should be read in conjunction with the notes to our combined financial statements.

Reserve for Losses and Loss Adjustment Expenses

Reserve for losses and LAE includes case reserves, incurred but not reported reserves ("IBNR") and portfolio reserves.

Case reserves are established when specific insured obligations are in or near default. Case reserves represent the present value of expected future loss payments and LAE, net of estimated recoveries but before considering ceded reinsurance from insured obligations that are in or near default. Financial guaranty insurance and reinsurance case reserves are discounted at 6.0%, which is the approximate taxable equivalent yield on the investment portfolio in all periods presented.

IBNR is an estimate of the amount of losses where the insured event has occurred but the claim has not yet been reported to us. In establishing IBNR, we use traditional actuarial methods to estimate the reporting lag of such claims based on historical experience, claim reviews and information reported by ceding companies. We record IBNR for mortgage guaranty reinsurance within our mortgage guaranty segment and for title reinsurance, auto residual value reinsurance and trade credit reinsurance within our other segment.

We also record portfolio reserves for our financial guaranty insurance and reinsurance, credit derivatives and mortgage guaranty reinsurance. Portfolio reserves are established with respect to the portion of our business for which case reserves have not been established. Portfolio reserves are

established in an amount equal to the portion of actuarially estimated ultimate losses related to premiums earned to date as a percentage of total expected premiums for that in-force business. Actuarially estimated ultimate losses of financial guaranty exposures are developed considering the net par outstanding of each insured obligation, taking account of the probability of future default, the expected timing of the default and the expected recovery following default. These factors vary by type of issue (for example municipal, structured finance or corporate), current credit rating and remaining term of the underlying obligation and are principally based on historical data obtained from rating agencies. Actuarially estimated ultimate losses on mortgage guaranty reinsurance are principally determined based on the historical industry loss experience, net of expected recoveries. During an accounting period, portfolio reserves principally increase or decrease based on changes in the aggregate net amount at risk and the probability of default resulting from changes in credit quality of insured obligations, if any.

We update our estimates of loss and LAE reserves quarterly. Loss assumptions used in computing loss and LAE reserves are updated periodically for emerging experience, and any resulting changes in reserves are recorded as a charge or credit to earnings in the period such estimates are changed. Due to the inherent uncertainties of estimating loss and LAE reserves, actual experience may differ from the estimates reflected in our combined financial statements, and the differences may be material.

The following tables summarize our reserve for losses and LAE by segment, by type of reserve and by segment and type of reserve as of the dates presented. For an explanation of changes in these reserves see " Combined Results of Operations."

	As of December 31,		
	2003	2002	2001
	(\$ in millions)		
<i>By segment:</i>			
Financial guaranty direct	\$ 29.9	\$ 26.0	\$ 8.9
Financial guaranty reinsurance	72.8	47.2	65.3
Mortgage guaranty	24.1	28.7	31.4
Other	395.7	356.9	295.4
	\$ 522.6	\$ 458.8	\$ 401.1
	As of December 31,		
	2003	2002	2001
	(\$ in millions)		
<i>By type of reserve:</i>			
Case basis	\$ 128.9	\$ 122.1	\$ 53.5
IBNR	319.0	281.1	269.0
Portfolio	74.6	55.6	78.5
	\$ 522.6	\$ 458.8	\$ 401.1

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

As of December 31, 2003

	Financial Guaranty Direct	Financial Guaranty Reinsurance	Mortgage Guaranty	Other	Total
(\$ in millions)					
<i>By segment and type of reserve:</i>					
Case basis	\$ 2.0	\$ 35.3	\$ 1.8	\$ 89.8	\$ 128.9
IBNR			13.1	305.9	319.0
Portfolio	27.9	37.5	9.2		74.6
Total	\$ 29.9	\$ 72.8	\$ 24.1	\$ 395.7	\$ 522.6

The following table sets forth the financial guaranty in-force portfolio by underlying rating:

Ratings	As of December 31, 2003	
	Net Par Outstanding	% of Net Par Outstanding
(\$ in billions)		
AAA	\$ 26.2	29.9%
AA	17.6	20.1
A	29.9	34.2
BBB	12.3	14.1
Below investment grade	1.5	1.7
Total exposures	\$ 87.5	100.0%

Our risk management department is responsible for monitoring our portfolio of credits and maintains a list of closely monitored credits. The closely monitored credits are divided into four categories: Category 1 (low priority; fundamentally sound, greater than normal risk); Category 2 (medium priority; weakening credit profile, may result in loss); Category 3 (high priority; losses likely, case reserve established); Category 4 (claim paid or incurred). Credits that are not included in the closely monitored credit list are categorized as fundamentally sound, normal risk. See "Business Risk Management" for further definition and discussion of closely monitored credits. The following table provides financial guaranty net par outstanding by credit monitoring category as of December 31, 2003:

Description:	As of December 31, 2003	
	Net Par Outstanding	% of Net Par Outstanding
(\$ in millions)		
Fundamentally sound, normal risk	\$ 85,794.8	98.0%
Closely monitored:		
Category 1	1,309.5	1.5
Category 2	251.8	0.3
Category 3	131.1	0.1
Category 4	36.8	0.0
Sub total	1,729.2	2.0
Total	\$ 87,524.0	100%

As of December 31, 2003

Valuation of Derivative Financial Instruments

On January 1, 2001, we adopted FAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("FAS 133"), which established accounting and reporting standards for derivative instruments. FAS 133 requires recognition of all derivatives on the balance sheet at fair value.

We issue credit derivative financial instruments, including a few index-based derivative financial instruments, that we view as an extension of our financial guaranty business but which do not qualify for the financial guaranty insurance scope exception under FAS 133 and therefore are reported at fair value, with changes in fair value included in our earnings.

Since we view these derivative contracts as an extension of our financial guaranty business, we believe that the most meaningful presentation of these derivatives is to reflect revenue as earned premium, to record estimates of losses and LAE on specific credit events as incurred and to record changes in fair value as incurred. When we determine that a loss on a derivative contract is probable, we establish reserves for the loss. Other changes in fair value are included in unrealized gains and losses on derivative financial instruments. We generally hold derivative contracts to maturity. However, in certain circumstances such as for risk management purposes or as a result of a decision to exit a line of business, we may decide to terminate a derivative contract prior to maturity. Where we hold a derivative to maturity, the cumulative unrealized gains and losses will net to zero if we incur no credit losses on that contract. However, in the event that we terminate a derivative contract prior to maturity the unrealized gain or loss will be realized through premiums earned and loss incurred.

The fair value of these instruments depends on a number of factors including credit spreads, changes in interest rates, recovery rates and the credit ratings of referenced entities. Where available, we use quoted market prices to determine the fair value of these credit derivatives. If the quoted prices are not available, particularly for senior layer CDOs and equity layer credit protection, the fair value is estimated using valuation models for each type of credit protection. These models may be developed by third parties, such as rating agencies, or developed internally based on market conventions for similar transactions, depending on the circumstances. These models and the related assumptions are continuously reevaluated by management and enhanced, as appropriate, based upon improvements in modeling techniques and availability of more timely market information. The majority of our single name credit derivatives are valued using third-party market quotes. Our exposures to CDOs are typically valued using a combination of rating agency models and internally developed models.

Valuation models include the use of management estimates and current market information. Management is also required to make assumptions on how the fair value of derivative instruments are affected by current market conditions. Management considers factors such as current prices charged for similar agreements, performance of underlying assets, and our ability to obtain reinsurance for our insured obligations. Due to the inherent uncertainties of the assumptions used in the valuation models to determine the fair value of these derivative products, actual experience may differ from the estimates reflected in our combined financial statements, and the differences may be material.

The fair value adjustment for the year ended December 31, 2003 was a \$98.4 million gain as compared to a \$54.2 million loss for the year ended December 31, 2002. The change in fair value is related to many factors but primarily due to changes in credit spreads. For example, the 2003 gain of \$98.4 million primarily relates to an approximate 60-65% tightening in investment grade corporate spreads over that period, and the 2002 loss of \$54.2 million primarily relates to an approximate 20-25% widening.

Valuation of Investments

As of December 31, 2003, 2002 and 2001, we had total investments of \$2.2 billion, \$2.1 billion and \$1.7 billion, respectively. The fair values of all of our investments are calculated from independent market quotations.

As of December 31, 2003, approximately 94% of our investments were long-term fixed maturity securities, and our portfolio had an average duration of 5.4 years. Changes in interest rates affect the value of our fixed maturity portfolio. As interest rates fall, the fair value of fixed maturity securities increases and as interest rates rise, the fair value of fixed maturity securities decreases. The following table summarizes the estimated change in fair value net of related income taxes on our investment portfolio as of December 31, 2003 based upon assumed changes in interest rates:

Change in Interest Rates	Estimated Increase (Decrease) in Fair Value
	(\$ in millions)
300 basis point rise	\$ (244.7)
200 basis point rise	(167.9)
100 basis point rise	(86.3)
100 basis point decline	76.0
200 basis point decline	155.2
300 basis point decline	230.0

Other than Temporary Impairments

We have a formal review process for all securities in our investment portfolio, including a review for impairment losses. Factors considered when assessing impairment include:

a decline in the market value of a security by 20% or more below amortized cost for a continuous period of at least six months;

a decline in the market value of a security for a continuous period of 12 months;

recent credit downgrades of the applicable security or the issuer by rating agencies;

the financial condition of the applicable issuer;

whether scheduled interest payments are past due; and

whether we have the ability and intent to hold the security for a sufficient period of time to allow for anticipated recoveries in fair value.

If we believe a decline in the value of a particular investment is temporary, we record the decline as an unrealized loss on our balance sheet in "accumulated other comprehensive income" in shareholder's equity. If we believe the decline is "other than temporary," we write down the carrying value of the investment and record a realized loss in our statement of operations. Our assessment of a decline in value includes management's current assessment of the factors noted above. If that assessment changes in the future, we may ultimately record a loss after having originally concluded that the decline in value was temporary.

Other than temporary declines in the fair value of fixed maturity securities were \$0.1 million and \$5.8 million for the years ended December 31, 2003 and 2002, respectively. The 2002 impairment loss as a percentage of the total fair value of our investments at the beginning

of 2002 was 0.3%.

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

The following table summarizes the unrealized losses in our investment portfolio by type of security and the length of time such securities have been in a continuous unrealized loss position as of the dates indicated:

Length of Time in Continuous Unrealized Loss	As of December 31, 2003		As of December 31, 2002	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
(\$ in millions)				
Municipal securities				
0-6 months	\$ 56.2	\$ (1.0)	\$ 8.6	
7-12 months	8.3	(0.2)	0.2	
Greater than 12 months			0.7	\$ (0.1)
	<u>64.5</u>	<u>(1.2)</u>	<u>9.5</u>	<u>(0.1)</u>
Corporate securities				
0-6 months	35.1	(0.5)		
7-12 months	9.5	(0.7)	4.7	(1.8)
Greater than 12 months			4.7	(0.2)
	<u>44.6</u>	<u>(1.2)</u>	<u>9.4</u>	<u>(2.0)</u>
U.S. Government obligations				
0-6 months	16.2	(0.2)		
7-12 months				
Greater than 12 months				
	<u>16.2</u>	<u>(0.2)</u>		
Mortgage and asset-backed securities				
0-6 months	125.2	(1.6)	18.1	(0.1)
7-12 months	29.8	(0.5)	12.0	(0.1)
Greater than 12 months			0.6	
	<u>155.0</u>	<u>(2.1)</u>	<u>30.7</u>	<u>(0.2)</u>
Total	<u>\$ 280.3</u>	<u>\$ (4.7)</u>	<u>\$ 49.6</u>	<u>\$ (2.3)</u>

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

The following table summarizes the unrealized losses in our investment portfolio by type of security and remaining time to maturity as of the dates indicated:

Remaining Time to Maturity	As of December 31, 2003		As of December 31, 2002	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
(\$ in millions)				
Municipal securities				
Due in one year or less				
Due after one year through five years	\$ 9.2	\$ (0.1)		
Due after five years through ten years	10.6	(0.1)		
Due after ten years	44.7	(1.0)	\$ 9.5	\$ (0.1)
	<u>64.5</u>	<u>(1.2)</u>	<u>9.5</u>	<u>(0.1)</u>
Corporate securities				
Due in one year or less			0.3	
Due after one year through five years	10.2	(0.1)	5.3	
Due after five years through ten years	8.5	(0.4)		
Due after ten years	25.9	(0.7)	3.8	(2.0)
	<u>44.6</u>	<u>(1.2)</u>	<u>9.4</u>	<u>(2.0)</u>
U.S. Government obligations				
Due in one year or less				
Due after one year through five years	0.1			
Due after five years through ten years	9.3			
Due after ten years	6.8	(0.2)		
	<u>16.2</u>	<u>(0.2)</u>		
Mortgage and asset-backed securities				
	<u>155.0</u>	<u>(2.1)</u>	<u>30.7</u>	<u>(0.2)</u>
Total	\$ 280.3	\$ (4.7)	\$ 49.6	\$ (2.3)

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

The following table summarizes, for all securities sold at a loss through December 31, 2003 and 2002, the fair value and realized loss by length of time such securities were in a continuous unrealized loss position prior to the date of sale:

Length of Time in Continuous Unrealized Loss Prior to Sale	Year Ended December 31,			
	2003		2002	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
	(\$ in millions)			
Corporate securities				
0-6 months	\$ 12.4	\$ (0.4)	\$ 51.8	\$ (2.0)
7-12 months			14.5	(0.7)
Greater than 12 months				
	12.4	(0.4)	66.3	(2.7)
U.S. Government securities				
0-6 months	9.4	(0.4)	20.5	(0.1)
7-12 months				
Greater than 12 months				
	9.4	(0.4)	20.5	(0.1)
Mortgage and asset-backed securities				
0-6 months	5.7	(0.1)	39.6	(0.4)
7-12 months				
Greater than 12 months				
	5.7	(0.1)	39.6	(0.4)
Total	\$ 27.5	\$ (0.9)	\$ 126.4	\$ (3.2)

Premium Revenue Recognition

Premiums are received either upfront or in installments. Upfront premiums are earned in proportion to the expiration of the related risk. Each installment premium is earned ratably over its installment period, generally one year or less. For the years ended December 31, 2003, 2002 and 2001, approximately 34.0%, 50.8% and 61.9%, respectively, of our gross written premiums were received upfront, and 66.0%, 49.2% and 38.1%, respectively, were received in installments. For the financial guaranty direct and financial guaranty reinsurance segments, earned premiums related to upfront premiums are greater in the earlier periods of an upfront transaction when there is a higher amount of risk outstanding. The premiums are allocated in accordance with the principal amortization schedule of the related bond issue and are earned ratably over the amortization period. When an insured issue is retired early, is called by the issuer, or is in substance paid in advance through a refunding accomplished by placing U.S. Government securities in escrow, the remaining unearned premium reserve is earned at that time. Unearned premium reserve represents the portion of premiums written that is applicable to the unexpired amount at risk of insured bonds.

In our reinsurance businesses, we estimate the ultimate written and earned premiums to be received from a ceding company at the end of each quarter and the end of each year because some of our ceding companies report premium data anywhere from 30 to 90 days after the end of the relevant period. Written premiums reported in our statement of operations are based upon reports received by ceding companies supplemented by our own estimates of premium for which ceding company reports have not yet been received. As of December 31, 2003, the assumed premium estimate and related

ceding commissions included in our combined financial statements are \$31.7 million and \$9.1 million, respectively. Key assumptions used to arrive at management's best estimate of assumed premium are premium amounts reported historically and informal communications with ceding companies. Differences between such estimates and actual amounts are recorded in the period in which the actual amounts are determined. Historically, the differences have not been material. We do not record a provision for doubtful accounts related to our assumed premium estimate. Historically there have not been any material issues related to the collectibility of assumed premium. For the years ended December 31, 2003, 2002, and 2001, we recorded a provision for doubtful accounts related to our premium receivable of \$0 million, \$0.3 million and \$0 million, respectively.

Deferred Acquisition Costs

Acquisition costs incurred that vary with and are directly related to the production of new business are deferred. These costs include direct and indirect expenses such as ceding commissions, brokerage expenses and the cost of underwriting and marketing personnel. As of December 31, 2003 and 2002, we had deferred acquisition costs of \$178.7 million and \$157.3 million, respectively. Ceding commissions paid to primary insurers are the largest component of deferred acquisition costs, constituting 80.2% and 77.7% of total deferred acquisition costs as of December 31, 2003 and 2002, respectively. Management uses its judgment in determining what types of costs should be deferred, as well as what percentage of these costs should be deferred. We periodically conduct a study to determine which operating costs vary with, and are directly related to, the acquisition of new business and qualify for deferral. Acquisition costs other than those associated with our credit derivative products are deferred and amortized in relation to earned premiums. Ceding commissions received on premiums we cede to other reinsurers reduce acquisition costs. Anticipated losses, LAE and the remaining costs of servicing the insured or reinsured business are considered in determining the recoverability of acquisition costs. Acquisition costs associated with credit derivative products are expensed as incurred.

Deferred Income Taxes

As of December 31, 2003 and 2002, we had a net deferred income tax liability of \$55.6 million and \$43.0 million, respectively. Certain of our subsidiaries are subject to U.S. income tax. Deferred income tax assets and liabilities are established for the temporary differences between the financial statement carrying amounts and tax bases of assets and liabilities using enacted rates in effect for the year in which the differences are expected to reverse. Such temporary differences relate principally to deferred acquisition costs, reserve for losses and LAE, unearned premium reserves, net operating loss carryforwards ("NOLs"), unrealized gains and losses on investments and derivative financial instruments and statutory contingency reserves. A valuation allowance is recorded to reduce a deferred tax asset to the amount that is more likely than not to be realized.

As of December 31, 2003, AGRO had a stand-alone NOL of \$89.0 million, which is available to offset its future U.S. taxable income. Substantially all of this NOL will be available until 2017, and the remainder will be available until 2023. AGRO's stand-alone NOL is not permitted to offset income of any other members of AGRO's consolidated group due to certain tax regulations. Under applicable accounting rules, we are required to establish a valuation allowance for NOLs that we believe are more likely than not to expire before utilized. Management believes it is more likely than not that \$20.0 million of AGRO's \$89.0 million NOL will not be utilized before it expires and has established a \$7.0 million valuation allowance related to the NOL deferred tax asset. The valuation allowance is subject to considerable judgment and will be adjusted to the extent actual taxable income differs from estimates of future taxable income that may be used to realize NOLs.

Combined Results of Operations

The following table presents summary combined statement of operations data for the years ended December 31, 2003, 2002 and 2001.

	Year Ended December 31,		
	2003	2002	2001
(\$ in millions)			
Revenues:			
Gross written premiums	\$ 349.2	\$ 417.2	\$ 442.9
Net written premiums	491.5	352.5	206.6
Net earned premiums	\$ 310.9	\$ 247.4	\$ 293.5
Net investment income	96.3	97.2	99.5
Net realized investment gains	5.5	7.9	13.1
Unrealized gains (losses) on derivative financial instruments	98.4	(54.2)	(16.3)
Other income	1.2	3.6	2.9
Total revenues	512.3	302.0	392.9
Expenses:			
Loss and loss adjustment expenses	144.6	120.3	177.5
Profit commission expense	9.8	8.5	9.0
Acquisition costs	64.9	48.4	51.1
Operating expenses	41.0	31.0	29.8
Other expenses	5.7	10.6	15.3
Total expenses	266.1	218.8	282.8
Income before provision (benefit) for income taxes	246.2	83.2	110.1
Provision for income taxes	31.7	10.6	22.2
Net income before cumulative effect of new accounting standard	214.5	72.6	87.9
Cumulative effect of new accounting standard, net of taxes			(24.1)
Net income	\$ 214.5	\$ 72.6	\$ 63.8
Underwriting gain (loss) by segment:			
Financial guaranty direct	\$ 29.5	\$ 3.6	\$ 17.0
Financial guaranty reinsurance	24.8	39.6	26.0
Mortgage guaranty	11.4	16.2	14.6
Other	(15.2)	(20.3)	(31.5)
Total	\$ 50.5	\$ 39.2	\$ 26.1

The summary combined statements of operations provided above are based on historical financial statement information. This information is not necessarily representative of the net income we will have going forward. We organize our business around four financial reporting segments: financial guaranty direct, financial guaranty reinsurance, mortgage guaranty and other. There are a number of lines of business that we have exited, which are included in the other segment. However, the results of these businesses are reflected in the above numbers. These businesses include equity layer credit protection, trade credit reinsurance, title reinsurance, LA&H and auto residual value reinsurance.

Summary of Significant Affiliate Transactions

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

Included in our results of operations are three significant transactions entered into with affiliated entities (see "Relationship with ACE Reinsurance Transactions"):

AGRI Affiliate Reinsurance Transaction: On December 31, 2001, AGRI entered into an excess of loss reinsurance contract with a subsidiary of ACE. Under the terms of this reinsurance

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

contract, AGRI paid \$125.0 million for 25 years of reinsurance coverage. This coverage provided a \$400.0 million aggregate limit, a \$50.0 million per risk limit and a \$5.0 million per risk deductible. The cost and benefit from this contract are included in the other segment. We terminated this agreement effective December 31, 2003 and recorded a receivable of \$131.9 million consisting of ceded unearned premium of \$115.0 million and reinsurance recoverables on paid losses of \$16.9 million. There was no earnings impact from the termination of this contract.

Assured Guaranty Corp. Affiliate Reinsurance Transaction: Assured Guaranty Corp. entered into an excess of loss reinsurance contract with a subsidiary of ACE, effective January 1, 2001. Under the terms of this reinsurance contract, Assured Guaranty Corp. paid \$27.5 million in 2001 and \$25.0 million in 2002 for ten years of reinsurance coverage. This coverage provided a \$150.0 million aggregate limit. The cost and benefit from this contract are included in the other segment. We terminated this agreement effective June 30, 2003 and received a cash payment of \$53.8 million, consisting of unearned premium of \$39.8 million, loss reserves of \$12.5 million and profit commissions of \$1.5 million. There was no earnings impact from the termination of this contract.

AGRO Affiliate Reinsurance Transaction: AGRO entered into a significant reinsurance transaction with an affiliate of ACE, which it fully ceded to a subsidiary of ACE, both effective July 1, 2001. This transaction is reported in the other segment and resulted in both gross and ceded premiums written of \$6.0 million, \$11.7 million and \$73.8 million in 2003, 2002 and 2001, respectively. Accordingly, this transaction had no effect on our net written premiums or our net income.

Net Income

Net income was \$214.5 million, \$72.6 million and \$63.8 million for the years ended December 31, 2003, 2002 and 2001, respectively. The increase of \$141.9 million in 2003 as compared with 2002 is primarily due to the significant increase in unrealized gains on derivative financial instruments due primarily to the tightening of credit spreads on our derivative financial instruments. Unrealized gains on derivative financial instruments increased from an after-tax loss of \$48.9 million in 2002 to an after-tax gain of \$83.4 million in 2003, an increase of \$132.3 million. In addition, underwriting income increased from \$39.2 million in 2002 to \$50.5 million in 2003. Most of this increase is attributable to the growth and improved profitability of the financial guaranty direct segment. The \$8.8 million increase in net income for 2002 as compared to 2001 is primarily related to improved underwriting results in our financial guaranty reinsurance, mortgage guaranty and other segments, offset by the decline in underwriting gain in the financial guaranty direct segment.

Gross Written Premiums

Gross Written Premiums	Year Ended December 31,		
	2003	2002	2001
	(\$ in millions)		
Financial guaranty direct	\$ 71.2	\$ 47.4	\$ 46.0
Financial guaranty reinsurance	168.7	84.6	70.4
Mortgage guaranty	24.4	47.6	47.4
Other	84.9	237.6	279.1
	\$ 349.2	\$ 417.2	\$ 442.9

Gross written premiums for the year ended December 31, 2003 were \$349.2 million compared to \$417.2 million the year ended December 31, 2002. In 2003, we achieved strong results in the financial guaranty reinsurance segment and financial guaranty direct segment as gross written premiums increased \$84.1 million, or 99.4%, and \$23.8 million, or 50.2%, respectively, over 2002. The increase in

the financial guaranty reinsurance segment was mainly driven by the municipal finance reinsurance business, which increased due to large cessions on European project finance transactions as well as an increase in the volume of new issues of insured municipal bonds. In the financial guaranty direct segment, the growth in gross written premiums was mainly attributable to an increase in structured finance premiums. These gains were offset by a decline in gross written premiums of \$152.7 million in the other segment and a \$23.2 million reduction in the mortgage guaranty segment. Gross written premiums in the other segment decreased \$152.7 million due to our decision to cease writing new equity layer credit protection business in 2003. The decline in gross written premiums in the mortgage guaranty segment in 2003 is primarily due to the continued runoff of our quota share business.

Gross written premiums for the year ended December 31, 2002 were \$417.2 million, a decrease of \$25.7 million, or 5.8%, compared to the year ended December 31, 2001. This decrease is primarily due to large nonrecurring transactions recognized in 2001, the AGRO Affiliate Reinsurance Transaction and a large auto residual value reinsurance transaction, both of which impact the other segment. This decline was partially offset by increases in the other financial guaranty reinsurance segment as well as modest increases in the mortgage guaranty and financial guaranty direct segments.

Net Written Premiums

Net Written Premiums	Year Ended December 31,		
	2003	2002	2001
	(\$ in millions)		
Financial guaranty direct	\$ 70.0	\$ 46.3	\$ 43.5
Financial guaranty reinsurance	162.1	82.6	68.6
Mortgage guaranty	24.4	47.6	47.6
Other	235.0	175.9	46.9
Total	\$ 491.5	\$ 352.5	\$ 206.6

Net written premiums for the year ended December 31, 2003 increased by \$139.0 million, despite the 16.3% decline in gross written premiums. This increase is due to the termination of the Assured Guaranty Corp. Affiliate Reinsurance Transaction at June 30, 2003 and the AGRI Affiliate Reinsurance Transaction at December 31, 2003, described previously in the " Summary of Significant Affiliate Transactions," reflected in the other segment. The termination of these contracts contributed \$154.8 million in net written premiums for the year ended December 31, 2003. Excluding the other segment, growth in net written premiums in the financial guaranty reinsurance, financial guaranty direct and mortgage segments was consistent with the growth of gross written premiums.

For the year ended December 31, 2002, net written premiums were \$352.5 million, an increase of \$145.9 million, or 70.6%, compared to the year ended December 31, 2001, despite a \$25.7 million, or 5.8%, decline in gross written premiums for 2002 compared to 2001. Net written premiums grew at a faster pace than gross written premium primarily due to the purchase of reinsurance in 2001 (see " Summary of Significant Affiliate Transactions"), reflected in the other segment. Net written premiums in the other segment increased \$129.0 million due to cessions of \$125.0 million related to the AGRI Affiliate Reinsurance Transaction in 2001, as well as positive trends in the equity layer credit protection line in 2002 compared to 2001. Excluding the other segment, net written premiums increased consistent with the increase in gross written premiums in the financial guaranty reinsurance, financial guaranty direct and mortgage guaranty segments.

Net Earned Premiums

Net Earned Premiums	Year Ended December 31,		
	2003	2002	2001
	(\$ in millions)		
Financial guaranty direct	\$ 70.2	\$ 43.9	\$ 30.0
Financial guaranty reinsurance	92.9	79.3	62.2
Mortgage guaranty	27.6	45.3	39.7
Other	120.2	78.9	161.6
Total	\$ 310.9	\$ 247.4	\$ 293.5

Net earned premiums for the year ended December 31, 2003 increased by \$63.5 million, or 25.7%, compared to the year ended December 31, 2002. Net earned premiums increased \$26.3 million, \$13.6 million and \$41.3 million in the financial guaranty direct segment, financial guaranty reinsurance segment and the other segment, respectively. The increase of \$26.3 million in the financial guaranty direct segment is primarily due to the growth in our structured finance portfolio. In the financial guaranty reinsurance segment, net earned premiums increased from \$79.3 million to \$92.9 million due to municipal finance refunding activity and an increase in par insured outstanding. The increase in the other segment is mainly attributable to our decision to exit the LA&H business, which resulted in a reduction in earned premiums of \$32.2 million in 2002 as a result of transferring this book of business to an affiliate of ACE. Net earned premiums declined in the mortgage segment from \$45.3 million to \$27.6 million related to a reduction in our treaty book of business.

Net earned premiums decreased by \$46.1 million, or 15.7%, for the year ended December 31, 2002 compared to the year ended December 31, 2001. Net earned premiums in 2002 grew in all segments except the other segment, which decreased \$82.7 million. Net earned premiums increased 46.3%, 27.5% and 14.1% in the financial guaranty direct segment, financial guaranty reinsurance segment and mortgage guaranty segment, respectively. The increase in the financial guaranty direct segment is attributable to an increase in structured finance premiums. In 2002, net earned premiums increased in the financial guaranty reinsurance segment largely due to municipal finance refunding activity. The growth in net premiums earned in these segments was partially offset by a \$82.7 million decrease in the other segment. This decrease included an \$89.0 million decrease in the auto residual value reinsurance business and a \$56.8 million decrease in the LA&H business, partially offset by a \$63.0 million increase in the equity layer credit protection business.

Net Investment Income

Net investment income was \$96.3 million, \$97.2 million and \$99.5 million for the years ended December 31, 2003, 2002 and 2001, respectively. Net investment income has remained relatively level across the periods as declining investment yields offset increasing investment balances. Pre-tax yields to maturity were 4.9%, 5.5% and 5.9% for the years ended December 31, 2003, 2002 and 2001, respectively. The decrease in investment yields is due to declining market interest rates as well as a more conservative investment profile in AGRI. Over this period the yield to maturity of the Lehman Aggregate Index, a commonly used benchmark for investment yields, declined from 5.7% as of December 31, 2001 to 4.2% as of December 31, 2003.

Net Realized Investment Gains

Net realized investment gains, principally from the sale of fixed maturity securities, were \$5.5 million, \$7.9 million and \$13.1 million for the years ended December 31, 2003, 2002 and 2001, respectively, net of \$0.1 million, \$5.8 million and \$9.3 million of other than temporary impairment losses for the years ended December 31, 2003, 2002 and 2001, respectively. Net realized investment gains, net of related income taxes, were \$3.8 million, \$5.8 million and \$9.9 million for the years ended December 31, 2003, 2002 and 2001, respectively.

Unrealized Gains (Losses) on Derivative Financial Instruments

Derivative financial instruments are recorded at fair value as required by FAS 133. However, as explained under "Critical Accounting Policies," we record part of the change in fair value in the loss and LAE reserves as well as unearned premium reserve. The fair value adjustment for the year ended December 31, 2003 was a \$98.4 million gain as compared to a \$54.2 million loss for the same period in 2002. The change in fair value is related to many factors but primarily due to tightening credit spreads. For example, the 2003 gain of \$98.4 million primarily corresponds to an approximate 60-65% tightening in investment grade corporate spreads over that period, and the 2002 loss of \$54.2 million corresponds to an approximate 20-25% widening of such spreads.

The gain or loss created by the estimated fair value adjustment will rise or fall based on estimated market pricing and may not be an indication of ultimate claims. Fair value is defined as the amount at which an asset or liability could be bought or sold in a current transaction between willing parties. We generally plan to hold derivative financial instruments to maturity. Where we hold derivative financial instruments to maturity, these fair value adjustments would generally be expected to reverse resulting in no gain or loss over the entire term of the contract.

Loss and Loss Adjustment Expenses

Loss and Loss Adjustment Expenses	Year Ended December 31,		
	2003	2002	2001
	(\$ in millions)		
Financial guaranty direct	\$ 16.3	\$ 25.4	\$ 3.0
Financial guaranty reinsurance	25.7	5.3	5.1
Mortgage guaranty	(0.7)	8.9	6.2
Other	103.3	80.6	163.2
Total	\$ 144.6	\$ 120.3	\$ 177.5

Loss and loss adjustment expenses for the year ended December 31, 2003 were \$144.6 million, an increase of \$24.3 million, or 20.2%, compared to the year ended December 31, 2002. The increase is attributable to a \$20.4 million increase in the financial guaranty reinsurance segment and a \$22.7 million increase in the other segment, and is partly offset by a \$9.1 million decrease in the financial guaranty direct segment and \$9.6 million decrease in the mortgage guaranty segment. Loss and loss adjustment expenses increased in the financial guaranty reinsurance segment due to an increase in case activity associated with CDOs assumed through treaties. The increase in loss and loss adjustment expenses for the other segment is primarily due to the increase in a case reserve related to one auto residual value reinsurance contract. The \$9.6 million decline in loss and loss adjustment expenses in the mortgage guaranty segment is due to favorable loss development on older contracts. The \$9.1 million decline in the financial guaranty direct segment is due to the improved credit environment as compared to 2002. See "Segment Results of Operations" for further explanations of these changes.

Loss and loss adjustment expenses for the year ended December 31, 2002 were \$120.3 million, a decrease of \$57.2 million, or 32.2%, compared to the year ended December 31, 2001. The \$57.2 million reduction in 2002 compared to 2001 is due to an increase in loss and loss adjustment expenses in the financial guaranty direct and mortgage guaranty segments due to a deteriorating credit environment, offset by an \$82.6 million decrease in the other segment due to the change in the mix of business, as we exited the auto residual value reinsurance and LA&H businesses. See " Segment Results of Operations" for further explanations of these changes.

Profit Commission Expense

Profit commissions allow the reinsured to share favorable experience on a reinsurance contract due to lower than expected losses. Profit commissions primarily relate to our mortgage guaranty segment. Profit commissions for the years ended December 31, 2003, 2002 and 2001 were \$9.8 million, \$8.5 million and \$9.0 million, respectively. In 2003 profit commission expense related to the mortgage segment declined due to a reduction in net earned premiums, offset by an increase in profit commission related to the financial guaranty reinsurance segment. Profit commission expense declined from \$9.0 million in 2001 to \$8.5 million in 2002 as a result of higher losses resulting in lower profit commission expense in the mortgage segment.

Acquisition Costs

Acquisition costs primarily consist of ceding commissions, brokerage fees and operating expenses that are related to the acquisition of new business. Acquisition costs that vary with and are directly related to the acquisition of new business are deferred and are amortized in relation to earned premium. For the years ended December 31, 2003, 2002 and 2001, acquisition costs were \$64.9 million, \$48.4 million and \$51.1 million, respectively. The increase of \$16.5 million in 2003 is consistent with the increase in earned premium. In 2002, acquisition costs decreased by \$2.7 million, primarily due to the transfer of our LA&H business to an affiliate. Acquisition costs as a percentage of net earned premiums were 20.9%, 19.6% and 17.4% in 2003, 2002 and 2001, respectively.

Operating Expenses

For the years ended December 31, 2003, 2002 and 2001, operating expenses were \$41.0 million, \$31.0 million and \$29.8 million, respectively. The increases are principally due to changes in staffing levels and other resources as we focused on growing the financial guaranty direct segment.

Other Expenses

For the years ended December 31, 2003, 2002 and 2001, other expenses were \$5.7 million, \$10.6 million and \$15.3 million, respectively. The \$4.9 million decrease in 2003 is due to the reduction in interest expense related to the repayment of \$100.0 million of debt in 2002. The decrease in 2002 is principally due to the absence of goodwill amortization, which was \$3.8 million in 2001 and 2000. Effective January 1, 2002, goodwill is no longer amortized.

Income Tax

For the years ended December 31, 2003, 2002 and 2001, income tax expense was \$31.7 million, \$10.6 million and \$22.2 million, respectively. Our effective tax rate was 12.9%, 12.7% and 20.2% for the years ended December 31, 2003, 2002 and 2001, respectively. Our effective tax rates reflect the proportion of income recognized by each of our operating subsidiaries, with U.S. subsidiaries taxed at the U.S. marginal corporate income tax rate of 35%, UK subsidiaries taxed at the UK marginal corporate tax rate of 30%, and with no taxes for our Bermuda holding company and subsidiaries.

Accordingly, our overall corporate effective tax rate fluctuates based on the distribution of taxable income across these jurisdictions.

Cumulative Effect of New Accounting Standard

On January 1, 2001, we adopted FAS 133, "Accounting for Derivative Instruments and Hedging Activities." FAS 133 requires that all derivatives be recognized in the combined balance sheet at fair value, with changes in fair value reflected in earnings. In 2001, we recorded an expense of \$24.1 million for the cumulative effect of adopting this standard, net of \$12.3 million of deferred income taxes.

Segment Results of Operations

Our financial results include three operating segments: financial guaranty direct, financial guaranty reinsurance and mortgage guaranty. For financial reporting purposes, we have a fourth segment, which we refer to as other. As we implement our new mortgage guaranty strategy, we will consider whether to continue to report the results of our mortgage guaranty business as a separate segment. Management uses underwriting gains and losses as the primary measure of each segment's financial performance. Underwriting gain (loss) includes net premiums earned, loss and loss adjustment expenses, acquisition expenses, profit commission expense and other operating expenses that are directly related to the operations of our insurance businesses. This measure excludes certain revenue and expense items, such as investment income, realized gains and losses, unrealized gains and losses on derivative financial instruments, goodwill amortization and interest expense, that are not directly related to the underwriting performance of our insurance operations, but are included in net income.

Financial Guaranty Direct Segment

The financial guaranty direct segment consists of our primary financial guaranty insurance business and our credit derivative business. Our financial guaranty direct segment began as a means to diversify our financial guaranty business's historical focus on reinsurance. We have been building our market presence in the financial guaranty direct market over the past seven years, beginning with our single-name credit default swap business in 1996. In 2000, we expanded our direct product offerings to include credit protection on CDOs and asset-backed and mortgage-backed securities, and began to build a primary monoline infrastructure, beginning a licensing program in the United States.

Financial guaranty insurance provides an unconditional and irrevocable guaranty that protects the holder of a financial obligation against non-payment of principal and interest when due. Financial guaranty insurance may be issued to the holders of the insured obligations at the time of issuance of those obligations, or may be issued in the secondary market to holders of municipal bonds and structured securities. As an alternative to traditional financial guaranty insurance, credit protection on a particular security or issuer can also be provided through a credit derivative, such as a credit default swap. Under a credit default swap, the seller of protection makes a specified payment to the buyer of protection upon the occurrence of one or more specified credit events with respect to a reference obligation or a particular reference entity. Credit derivatives typically provide protection to a buyer rather than credit enhancement of an issue as in traditional financial guaranty insurance.

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

The table below summarizes the financial results of our financial guaranty direct segment for the periods presented:

	Year Ended December 31,		
	2003	2002	2001
	(\$ in millions)		
Gross written premiums	\$ 71.2	\$ 47.4	\$ 46.0
Net written premiums	70.0	46.3	43.5
Net earned premiums	\$ 70.2	\$ 43.9	\$ 30.0
Loss and loss adjustment expenses	16.3	25.4	3.0
Profit commission expense		(0.1)	(0.1)
Acquisition costs	2.8	2.4	0.9
Operating expenses	21.6	12.5	9.2
	\$ 29.5	\$ 3.6	\$ 17.0
Losses and loss adjustment expense ratio	23.2%	57.9%	10.0%
Expense ratio	34.8	33.7	33.3
	58.0%	91.6%	43.3%

For the years ended December 31, 2003, 2002 and 2001, the financial guaranty direct segment contributed \$71.2 million, \$47.4 million and \$46.0 million to gross written premiums, respectively, which represent an increase of \$23.8 million and \$1.4 million in 2003 and 2002, respectively. Of the \$23.8 million increase in 2003, \$21.1 million was written as credit derivatives and \$2.7 million was written as financial guaranty insurance, which we began writing in 2003. We began writing financial guaranty insurance in 2003, writing \$1.5 million of municipal finance business and \$1.2 million of structured finance business, of which \$1.1 million was home equity loan securitizations issued in the public markets.

Gross and net written premiums in this segment generally have been received on an installment basis, reflecting our focus on the structured finance and credit derivatives markets. In 2003, 2002 and 2001, installment premiums represented 94.9%, 95.6% and 67.8% of gross written premiums in this segment, or \$67.6 million, \$45.3 million and \$31.2 million, respectively. The contribution of upfront premiums to gross written premiums were \$3.6 million, \$2.1 million and \$14.8 million in 2003, 2002 and 2001, respectively. Although premiums are typically received on an installment basis on credit derivatives, in 2001, \$14.8 million of upfront premiums were written, primarily related to two transactions. Gross written premiums in 2002 were flat compared to 2001 due to these transactions.

For the years ended December 31, 2003, 2002 and 2001, net written premiums were \$70.0 million, \$46.3 million and \$43.5 million, respectively. The growth in net written premiums is primarily due to growth in gross written premiums as we typically retain a substantial portion of this business.

Management uses the "present value of gross premiums written" to evaluate new business production for our financial guaranty business, including both financial guaranty insurance and reinsurance and credit derivative contracts. This measure consists of upfront premiums plus the present value of installment premiums (discounted at 6%) for contracts entered into during the reporting period. Management uses this measure to provide a meaningful summary of new business production in our financial guaranty direct and financial guaranty reinsurance segments, as both upfront and installment premiums are included in our revenues. The present value of gross premiums written differs from gross written premiums as shown in our financial statements and should not be considered as a substitute for gross written premiums determined in accordance with GAAP.

Management also uses the "net present value of installment premiums in-force" in our financial guaranty direct and financial guaranty reinsurance segments as a measure of our future premiums on our in-force book of installment premium business. It is calculated net of reinsurance ceded and using a discount rate of 6%. There is no GAAP measure that is comparable to the net present value of installment premiums in-force.

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

The following table reconciles gross written premiums as presented in our statement of operations to the present value of gross premiums written and presents the net present value of installment premiums in-force, as well as gross par written and net par outstanding:

	Year Ended December 31,		
	2003	2002	2001
	(\$ in millions)		
Gross written premiums	\$ 71.2	\$ 47.4	\$ 46.0
Less installment premiums included above	(67.6)	(45.3)	(31.2)
	3.6	2.1	14.8
Upfront gross premiums			
Present value of installment premiums related to contracts written in current period	90.2	93.9	101.8
	93.8	96.0	116.6
Present value of gross premiums written			
Gross par written:			
Municipal finance	\$ 48	\$ 113	\$ 209
Structured finance	6,980	6,734	7,481
	7,028	6,847	7,690
Total			
As of period end:			
Net present value of installment premiums in-force	\$ 217.1	\$ 187.3	\$ 113.4
Net present value of installment premiums in-force, net of related income taxes	151.9	134.8	77.0
Net par outstanding:			
Municipal finance	\$ 2,138	\$ 1,869	\$ 1,873
Structured finance	21,561	18,575	13,649
	23,699	20,444	15,522
Total			

The present value of gross premiums written in a period is the result of the gross par written, the annual premium rate charged and the duration of the underlying security. The annual premium rate fluctuates based on credit spreads, asset category, credit rating and other security-specific characteristics, as well as market conditions, competition and other broader economic and market factors. For the years ended December 31, 2003, 2002 and 2001, the present value of gross premiums written was \$93.8 million, \$96.0 million and \$116.6 million, respectively. In 2003, the present value of gross premiums written declined 2.3%, although gross par written grew 2.6%, due to lower credit spreads in the market as well as a change in the mix of asset categories we underwrote. For example, during 2003 we stopped underwriting single name credit default swaps, underwriting only \$150 million of gross par, whereas we underwrote \$547 million and \$422 million of gross par in 2002 and 2001, respectively. In 2002, the present value of gross premiums written declined 17.7%, compared to an 11% decline in gross par written, from \$7.7 billion to \$6.8 billion. In the challenging credit environment we were more stringent in our underwriting standards and pricing, which reduced overall volumes in 2002.

The change in net present value of installment premiums in-force is a measurement used by management to evaluate the future net earned premium on business that has already been underwritten. The net present value of installment premiums in-force was \$217.1 million, \$187.3 million and \$113.4 million as of December 31, 2003, 2002 and 2001, respectively. In 2003, the net present value of installment premiums in-force was up 15.9% versus the prior year, reflecting the addition of \$90.2 million in present value of installment premiums related to contracts written in the period, partially offset by reported net earned premiums of \$70.2 million. In 2002, the net present value of installment premiums in-force was up 65.2% to \$187.3 million, reflecting the strong level of production

related to contracts written in the period, compared to a relatively low starting level, as we began to expand our financial guaranty direct operations.

Net earned premiums for the years ended December 31, 2003, 2002 and 2001, were \$70.2 million, \$43.9 million and \$30.0 million, respectively, an increase of \$26.3 million, or 59.9%, in 2003, and \$13.9 million, or 46.3%, in 2002. The increase in net earned premiums across these periods reflects the amortization of upfront premiums and the growing volume of installment premiums generated in the growing book of contracts, as evidenced by the increase in net par outstanding and net present value of installment premiums in-force. Net par outstanding grew from \$15.5 billion at year-end 2001 to \$20.4 billion at year-end 2002, up 31.7%, to \$23.7 billion at year-end 2003, up 15.9%.

Loss and loss adjustment expenses were \$16.3 million, \$25.4 million and \$3.0 million, respectively, for the years ended December 31, 2003, 2002 and 2001. Our loss and loss adjustment expenses are affected by changes in the mix, size and credit trends in our book of business, and by changes in our reserves for loss and loss adjustment expenses for prior periods. Our loss ratio is principally affected by the mix of business in our net earned premiums, credit events in our net par outstanding, market credit spreads and premium rates, among other factors. The loss ratios for the years ended December 31, 2003, 2002 and 2001 were 23.2%, 57.9% and 10.0%, respectively. The decline in the loss ratio in 2003 was due to an improvement in the credit environment compared to 2002. Additionally, in 2003 we substantially reduced the new single name corporate credit derivatives business we write; this business generates a higher loss ratio than our other financial guaranty direct businesses. The increase in the loss ratio in 2002 as compared with 2001 reflected a deterioration in the credit environment, as we incurred \$15.8 million of loss and loss adjustment expenses for three specific credit events. Two of these three events related to single name credit default swaps on which we were given notice of default in the fourth quarter of 2002 and the third credit event related to a total rate of return swap on Argentine mortgage bonds, which were impacted by currency devaluation and failed attempts to remedy the impairments to the bonds. In addition to these credit events, loss and loss adjustment expenses incurred also increased as a result of an increase in the portfolio reserve in 2002, precipitated by the stressed corporate credit environment resulting in an unprecedented level of corporate defaults in 2002 and 2001.

For the years ended December 31, 2003, 2002 and 2001, acquisition costs were \$2.8 million, \$2.4 million and \$0.9 million, respectively. The year over year increases in acquisition costs are primarily due to an increase in transaction rating agency fees related to the growth in gross written premiums as well as the increase in the proportion of such premiums subject to premium taxes.

Operating expenses for the years ended December 31, 2003, 2002 and 2001 were \$21.6 million, \$12.5 million and \$9.2 million, respectively. These increases were primarily due to the increase in required staff levels to support the growth in this segment as well as an increase in costs to establish the required platforms and infrastructure to enter the financial guaranty insurance business. Expense ratios were generally consistent at 34.8%, 33.7% and 33.3% for the years ended December 31, 2003, 2002 and 2001, respectively.

Financial Guaranty Reinsurance Segment

In our financial guaranty reinsurance business, we assume all or a portion of risk undertaken by other insurance companies that provide financial guaranty protection. A decline in reinsurance capacity due to two significant competitors exiting this market has created opportunities for growth in this business segment. The financial guaranty reinsurance business consists of structured finance and municipal finance reinsurance lines. Premiums on municipal finance are typically written upfront and earned over the life of the policy, and premiums on structured finance are typically written on an installment basis and earned ratably over the installment period.

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

The table below summarizes the financial results of our financial guaranty reinsurance segment for the periods presented:

	Year Ended December 31,		
	2003	2002	2001
	(\$ in millions)		
Gross written premiums	\$ 168.7	\$ 84.6	\$ 70.4
Net written premiums	162.1	82.6	68.6
Net earned premiums	\$ 92.9	\$ 79.3	\$ 62.2
Loss and loss adjustment expenses	25.7	5.3	5.1
Profit commission expense	1.5	0.5	
Acquisition costs	33.9	29.0	24.7
Operating expenses	7.0	4.9	6.4
Underwriting gain	\$ 24.8	\$ 39.6	\$ 26.0
Loss and loss adjustment expense ratio	27.7%	6.7%	8.2%
Expense ratio	45.6	43.4	50.0
Combined ratio	73.3%	50.1%	58.2%

	Year Ended December 31,		
	2003	2002	2001
Gross Written Premiums			
Municipal finance	\$ 117.1	\$ 48.1	\$ 37.0
Structured finance	51.6	36.5	33.4
Total	\$ 168.7	\$ 84.6	\$ 70.4

Gross written premiums for our financial guaranty reinsurance segment include upfront premiums on transactions underwritten during the period, plus installment premiums on business primarily underwritten in prior periods. Consequently, this amount is affected by changes in the business mix between municipal finance, which tends to be upfront premium, and structured finance, which tends to be installment premium. For the year ended December 31, 2003, 62.2% of gross written premiums in this segment were upfront premiums and 37.8% were installment premiums.

In 2002 and 2001, upfront premiums were 56.4% and 52.7%, respectively, of gross written premiums of this segment. Gross written premiums for the years ended December 31, 2003, 2002 and 2001 were \$168.7 million, \$84.6 million and \$70.4 million, respectively, which represent an increase of \$84.1 million and \$14.2 million in 2003 and 2002, or 99.4% and 20.2%, respectively. The principal driver of gross written premium growth over the period has been the strong growth in municipal finance premiums, which grew 143.4% and contributed 69.4% of the segment's gross written premiums in 2003 and grew 30.0% and contributed 56.8% of segment gross written premiums in 2002. Structured finance gross written premiums also grew, increasing 41.3% in 2003 and 9.3% in 2002.

Our municipal finance reinsurance growth has been driven by strong growth in insured U.S. municipal bond issuance over the period as well as the several European PFI transactions ceded to us in 2003. Premium rates on European transactions are typically higher than premium rates on U.S. municipal finance transactions. In 2003, we assumed \$503.7 million of gross par written from European project finance transactions.

For the years ended December 31, 2003, 2002 and 2001, gross written premiums in our structured finance line of business were \$51.6 million, \$36.5 million and \$33.4 million, respectively. The \$15.1 million increase in gross written premiums from 2002 to 2003 and the \$3.1 million increase in

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

gross written premiums from 2001 to 2002 was due to changes in the business mix and volume of installment premiums received in these periods.

The following table reconciles gross premiums written as presented in our statement of operations to the present value of gross premiums written and presents the net present value of installment premiums in-force:

	Year Ended December 31,		
	2003	2002	2001
	(\$ in millions)		
Gross written premiums	\$ 168.7	\$ 84.6	\$ 70.4
Less installment premiums included above	(63.8)	(36.9)	(33.3)
Upfront gross written premiums	104.9	47.7	37.1
Present value of installment premiums related to contracts written in current period	40.1	71.8	41.3
Present value of gross premiums written	\$ 145.0	\$ 119.5	\$ 78.4
Gross par written: ⁽¹⁾			
Municipal finance	\$ 6,720	\$ 7,486	\$ 4,661
Structured finance	3,295	5,563	3,425
Total	\$ 10,015	\$ 13,049	\$ 8,086
As of period end:			
Net present value of installment premiums in-force ⁽¹⁾	\$ 92.7	\$ 72.9	\$ 46.3
Net present value of installment premiums in-force, net of taxes ⁽¹⁾	61.9	47.4	30.1
Net par outstanding: ⁽¹⁾			
Municipal finance	\$ 50,538	\$ 47,509	\$ 46,436
Structured finance	13,287	12,441	13,291
Total	\$ 63,825	\$ 59,950	\$ 59,727

⁽¹⁾ This data is reported on a one-quarter lag due to the timing of receipt of reports prepared by our ceding companies.

For the years ended December 31, 2003, 2002 and 2001, the present value of gross premiums written was \$145.0 million, \$119.5 million and \$78.4 million, respectively. The increase in 2003 of \$25.5 million, or 21.3%, is primarily due to an increase in volume in the U.S. municipal finance business and large cessions on European project finance transactions. In 2002, the present value of gross premiums written increased \$41.1 million, or 52.4%, as a result of an increase in gross par written in this period from \$8.1 billion to \$13.0 billion, an increase of 61.4%.

The net present value of installment premiums in-force for the years ended December 31, 2003, 2002 and 2001 was \$92.7 million, \$72.9 million and \$46.3 million, respectively. The increase in the net present value of installment premiums in-force was driven by increases in the present value of installment premiums related to contracts written in the current period, offset principally by installment premiums received on contracts written in previous periods.

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

Gross par written has fluctuated over the periods presented, rising 61.4% to \$13.0 billion in 2002 from \$8.1 billion in 2001 and declining 23.3% in 2003 to \$10.0 billion. The growth in 2002 reflects growth in cessions from the primary financial guaranty companies and reflects growth in insured par U.S. municipal and structural finance markets. See "Business." In 2003, we underwrote less gross par,

reflecting lower cessions from our ceding companies of U.S. municipal and structural finance business. This decline was partially offset by \$503.7 million in gross par written on 2003 European PFI deals.

Net Written Premiums	Year Ended December 31,		
	2003	2002	2001
	(\$ in millions)		
Municipal finance	\$ 116.5	\$ 46.6	\$ 35.2
Structured finance	45.6	36.0	33.4
Total	\$ 162.1	\$ 82.6	\$ 68.6

For the years ended December 31, 2003, 2002 and 2001, net written premiums were \$162.1 million, \$82.6 million and \$68.6 million, respectively. The year over year increase of \$79.5 million and \$14.0 million in 2003 and 2002, respectively, is consistent with the increases in gross written premium described above. Of this increase, \$69.9 million and \$11.4 million in 2003 and 2002, respectively, was attributable to our municipal finance line, which is consistent with the year over year increase in municipal gross written premiums, explained above. The increase of \$9.6 million and \$2.6 million in 2003 and 2002, respectively, in our structured finance line of business also follows the pace of gross written premiums described above.

Net Earned Premiums	Year Ended December 31,		
	2003	2002	2001
	(\$ in millions)		
Municipal finance	\$ 52.9	\$ 42.7	\$ 31.1
Structured finance	40.0	36.6	31.1
Total	\$ 92.9	\$ 79.3	\$ 62.2

Included in municipal reinsurance net premiums are refundings of: \$ 19.2 \$ 14.0 \$ 4.5

Growth in our net earned premiums over the period has been driven by growth in both the municipal and structured finance lines of business, as evidenced by the growth in net par outstanding, unearned premium reserves and the net present value of installment premiums in-force. However, the municipal finance business's contribution also includes an increase in refunding premiums, which reflect the unscheduled pre-payment or refundings of underlying municipal bonds due to lower interest rates. These unscheduled refunding premiums are sensitive to market interest rates and we evaluate our net earned premiums both including and excluding these premiums.

For the years ended December 31, 2003, 2002 and 2001, net earned premiums were \$92.9 million, \$79.3 million and \$62.2 million, respectively, an increase of \$13.6 million, or 17.2%, in 2003, and \$17.1 million, or 27.5%, in 2002. The municipal finance line accounted for \$10.2 million of the \$13.6 million increase in 2003, reflecting higher earned premium and gross par insured as well as a \$5.2 million increase in refunding related premiums. In 2002, refundings in our municipal finance line accounted for \$9.5 million of the \$17.1 million increase, largely due to \$14.0 million of refundings driven by the continued decline in interest rates as compared to \$4.5 million in 2001, an increase of \$9.5 million. Structured finance net earned premiums increased by \$3.4 million in 2003 and \$5.5 million in 2002.

Losses and LAE were \$25.7 million, \$5.3 million and \$5.1 million, respectively, for the years ended December 31, 2003, 2002 and 2001. Our loss and LAE ratios for the years ended December 31, 2003, 2002 and 2001 were 27.7%, 6.7% and 8.2%, respectively. The increase in the loss ratio from 6.7% to 27.7% in 2003 is primarily attributable to an increase in losses and LAE incurred in the structured finance line of business due to credit deterioration in collateralized debt obligations assumed through reinsurance treaties. Case reserves related to these collateralized debt obligations were increased in the

fourth quarter after completion of risk management's credit analysis, which included discussions with ceding companies. In 2002 and 2001, the level of loss experience was relatively consistent.

For the years ended December 31, 2003, 2002 and 2001, acquisition costs were \$33.9 million, \$29.0 million and \$24.7 million, respectively. The increases in acquisition costs over the periods are directly related to the increases in earned premium.

Operating expenses for the years ended December 2003, 2002 and 2001, were \$7.0 million, \$4.9 million and \$6.4 million. Operating expenses in 2003 increased by \$2.1 million as compared to 2002 as a result of the entry of our Bermuda subsidiary, Assured Guaranty Re International, into the financial guaranty reinsurance market. The decline in operating expenses in 2002 as compared to 2001 is primarily due to the change in business mix as we increased our focus on our financial guaranty direct operations. The expense ratios were 45.6%, 43.4% and 50.0% in 2003, 2002 and 2001, respectively.

Mortgage Guaranty Segment

The mortgage guaranty segment consists primarily of reinsurance. Mortgage guaranty insurance provides protection to mortgage lending institutions against the default of borrowers on mortgage loans that, at the time of the advance, had a loan-to-value ("LTV") ratio in excess of a specified ratio. We primarily function as a reinsurer in this industry and assume all or a portion of the risks undertaken by primary mortgage insurers. We intend to use our mortgage guaranty platform to write investment grade rated mortgage guaranty business.

The table below summarized the financial results of our mortgage guaranty segment for the periods presented:

	Year Ended December 31,		
	2003	2002	2001
	(\$ in millions)		
Gross written premiums	\$ 24.4	\$ 47.6	\$ 47.4
Net written premiums	24.4	47.6	47.6
Net earned premiums	\$ 27.6	\$ 45.3	\$ 39.7
Loss and loss adjustment expenses	(0.7)	8.9	6.2
Profit commission expense	7.3	8.3	9.2
Acquisition costs	5.0	8.0	7.2
Operating expenses	4.6	3.9	2.5
Underwriting gain	\$ 11.4	\$ 16.2	\$ 14.6
Loss and loss adjustment expense ratio	(2.5)%	19.6%	15.6%
Expense ratio	61.2	44.6	47.6
Combined ratio	58.7%	64.2%	63.2%

Gross written premiums for the years ended December 31, 2003, 2002 and 2001 were \$24.4 million, \$47.6 million and \$47.4 million, respectively. The decline in gross written premiums is due to the continued runoff of our quota share business, as well as significant refinancing activity due to the low interest rate environment. Results for 2002 include \$10.4 million of gross written premiums from one non-recurring transaction.

Net written premiums for the years ended December 31, 2003, 2002 and 2001 were \$24.4 million, \$47.6 million and \$47.6 million, respectively. The change is consistent with the trend in gross written premiums, as we do not cede a significant amount of our mortgage guaranty business.

For the years ended December 31, 2003, 2002 and 2001, net earned premiums were \$27.6 million, \$45.3 million and \$39.7 million, respectively. In each of the three years there were decreases in net earned premiums related to our quota share business. In 2002, this decline was offset by the non-recurring transaction described above, which generated \$10.4 million of earned premium.

Loss and loss adjustment expenses were \$(0.7) million, \$8.9 million and \$6.2 million, respectively, for the years ended December 31, 2003, 2002 and 2001. The loss and loss adjustment expense ratios for the years ended December 31, 2003, 2002 and 2001 were (2.5%), 19.6% and 15.6%, respectively. The negative loss ratio for 2003 is primarily a result of favorable loss experience related to older contracts, which are running off. This decrease was also attributable to higher than expected appreciation in real estate values, resulting in both lower frequency of claims and lower severity of losses. In 2002, the increase in the loss and loss adjustment expense ratio was primarily due to a single contract that was written during 2002 that had \$2.8 million of net earned premiums and was reserved at a 100% loss and loss adjustment expense ratio.

Profit commission expense for the year ended December 31, 2003, 2002 and 2001 was \$7.3 million, \$8.3 million and \$9.2 million, respectively. The decline in profit commission expense on a year-over-year basis is due to the decline in net earned premiums related to business that has a profit commission element, including our quota share business.

Acquisition costs for the years ended December 31, 2003, 2002 and 2001 were \$5.0 million, \$8.0 million and \$7.2 million, respectively. The decline in acquisition costs in 2003 as compared to 2002 is primarily due to the shift in business from quota share reinsurance to excess of loss reinsurance, as ceding commissions generally are not paid on excess of loss reinsurance. The increase in acquisition costs from 2001 to 2002 is commensurate with the increase in earned premiums.

Operating expenses for the years ended December 31, 2003, 2002 and 2001 were \$4.6 million, \$3.9 million and \$2.5 million, respectively. The expense ratio, which includes profit commission expense, was 61.2%, 44.6% and 47.6% for the years ended December 31, 2003, 2002 and 2001, respectively. The increase in the expense ratio in 2003 from 2002 is primarily due to the steady level of operating expenses required to support the business, as compared to a declining earned premium base, as discussed above.

Other Segment

Our other segment consists of certain non-core businesses that we have exited prior to, or in connection with, the IPO including equity layer credit protection, trade credit reinsurance, title reinsurance, LA&H reinsurance and auto residual value reinsurance. Also included in the other segment is the impact of the affiliate reinsurance transactions described under " Combined Results of Operations Summary of Significant Affiliate Transactions" above. These reinsurance contracts were purchased for the benefit of all of our operating segments. We do not allocate the costs nor the related benefits of these transactions to each of the segments but rather record the impact of these transactions in the other segment.

Due to our decision to exit the above businesses, the following discussion focuses on net earned premiums and underwriting results of each business within this segment.

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

The following table provides details of net earned premiums and underwriting results by line of business:

	Year Ended December 31,		
	2003	2002	2001
	(\$ in millions)		
Net earned premiums:			
Equity layer credit protection	\$ 61.8	\$ 84.0	\$ 21.0
Trade credit reinsurance	51.2	27.8	23.5
Title reinsurance	10.7	7.3	6.5
LA&H		(32.2)	24.6
Auto residual value reinsurance	4.2	2.3	91.3
Affiliate reinsurance	(7.7)	(10.3)	(5.3)
Total	\$ 120.2	\$ 78.9	\$ 161.6
Underwriting gain (loss):			
Equity layer credit protection	\$ (1.0)	\$ (19.7)	\$ (18.4)
Trade credit reinsurance	(3.3)	(0.3)	(0.3)
Title reinsurance	6.8	3.3	1.1
LA&H	(0.6)	(1.3)	1.2
Auto residual value reinsurance	(24.5)	(8.1)	(10.1)
Affiliate reinsurance	7.4	5.8	(5.1)
Total	\$ (15.2)	\$ (20.3)	\$ (31.5)

In 2001, we entered the equity layer credit protection market with \$21.0 million of net earned premiums. In 2002, net earned premiums increased by \$63.0 million, reflecting favorable pricing for such transactions in the capital markets. We ceased writing new equity layer credit protection business during 2003, and net earned premiums declined from \$84.0 million for the year ended December 31, 2002 to \$61.8 million for the year ended December 31, 2003. The unprecedented level of corporate defaults in 2001 and 2002 along with expenses associated with our entry into the business resulted in underwriting losses of \$18.4 million in 2001 and \$19.7 million in 2002. For the year ended December 31, 2003, the underwriting loss in equity layer credit protection decreased to \$1.0 million as a result of the termination of three trades, which produced an underwriting gain of \$16.5 million.

Trade credit reinsurance net earned premiums were \$23.5 million, \$27.8 million and \$51.2 million for the years ended December 31, 2001, 2002 and 2003, respectively. The growth in earned premium is a result of steadily increasing writings in this line over the periods as a result of several competitors exiting this market. Underwriting losses for the years ended December 31, 2001, 2002 and 2003 were \$0.3 million, \$0.3 million and \$3.3 million, respectively. We intend to cease writing new trade credit business in 2004.

Net earned premiums for the title reinsurance business grew steadily, from \$6.5 million to \$7.3 million and \$10.7 million for years ended December 31, 2001, 2002 and 2003, respectively. This business has made modest contributions to underwriting results, with gains of \$1.1 million, \$3.3 million and \$6.8 million in 2001, 2002 and 2003, respectively. The \$6.8 million of underwriting gain for the year ended December 31, 2003 was primarily due to favorable prior year loss reserve development. In connection with the IPO, ACE Capital Title was sold to ACE or one of its subsidiaries and our other title reinsurance business was reinsured by, or assigned to, a subsidiary of ACE.

LA&H had net earned premiums of \$24.6 million in 2001 and negative \$32.2 million in 2002. The fluctuation in net earned premium was related to the timing of new business written and novations and commutations of in-force business in early 2002, in connection with our exiting the LA&H business.

LA&H generated a \$1.2 million underwriting gain in 2001. The underwriting losses of \$1.3 million in 2002 and of \$0.6 million in 2003 were related to the litigation and settlement of a disputed contract.

Auto residual value reinsurance net earned premiums were \$91.3 million, \$2.3 million and \$4.2 million for the years ended December 31, 2001, 2002 and 2003, respectively. The decrease in earned premium in 2002 was due to a non-recurring transaction in 2001 with net earned premiums of \$86 million. Underwriting losses were \$10.1 million, \$8.1 million and \$24.5 million for the years ended December 31, 2001, 2002 and 2003, respectively. The underwriting loss of \$24.5 million in 2003 is a result of an increase in reserves for losses and loss adjustment expenses related to a dispute with World Omni (see note 15 of notes to combined financial statements for further discussion). We ceased writing new business in this line in 2001.

Net earned premiums related to affiliate reinsurance were negative \$5.3 million, \$10.3 million and \$7.7 million for the years ended December 31, 2001, 2002 and 2003, respectively, and primarily represent the cost of the Assured Guaranty Corp. Affiliate Reinsurance Transaction and AGRI Affiliate Reinsurance Transaction for these periods. As a result of losses of \$15.0 million and \$14.4 million ceded under these contracts in 2002 and 2003, respectively, affiliate reinsurance generated an underwriting gain of \$5.8 million and \$7.4 million, respectively. The underwriting loss of \$5.1 million in 2001 was approximately equal to the cost of the affiliate reinsurance for this period.

Liquidity and Capital Resources

Our liquidity, both on a short-term basis (for the next twelve months) and a long-term basis (beyond the next twelve months), is largely dependent upon: (1) the ability of our subsidiaries to pay dividends or make other payments to us; (2) external financings; and (3) investment income on our invested assets. Our liquidity requirements include the payment of our operating expenses, interest on our debt, and dividends on our common shares. We may also require liquidity to make periodic capital investments in our operating subsidiaries. In the ordinary course of our business, we evaluate our liquidity needs and capital resources in light of holding company expenses, debt-related expenses and our dividend policy, as well as rating agency considerations. Based on the amount of dividends we expect to receive from our subsidiaries and the income we expect to receive on our invested assets, management believes that we will have sufficient liquidity to satisfy our needs over the next twelve months, including the ability to pay our obligations on the notes. Beyond the next twelve months, the ability of our subsidiaries to declare and pay dividends may be influenced by a variety of factors including market conditions, insurance regulations and general economic conditions. Consequently, although management believes that we will continue to have sufficient liquidity to meet our debt service and other obligations over the long term, no guaranty can be given that we will not be required to seek external debt or equity financing in order to meet our operating expenses or debt service obligations.

We anticipate that a major source of our liquidity, for the next twelve months and for the longer term, will be amounts paid by our operating subsidiaries as dividends. Certain of our operating subsidiaries are subject to restrictions on their ability to pay dividends. See "Business Regulation." The amount available at Assured Guaranty Corp. to pay dividends in 2004 with notice to, but without the prior approval of, the Maryland Insurance Commissioner is approximately \$25.6 million. Dividends paid by a U.S. company to a Bermuda holding company presently are subject to withholding tax at a rate of 30%. The amount available at AGRI to pay dividends in 2004 in compliance with Bermuda law is \$569.1 million. Each of Assured Guaranty Corp. and AGRI has committed to S&P and Moody's that it will not pay more than \$10.0 million per year in dividends.

Liquidity at our operating subsidiaries is used to pay operating expenses, claims, payment obligations with respect to credit derivatives, reinsurance premiums and dividends to us, as well as, where appropriate, to make capital investments in their own subsidiaries. In addition, certain of our

operating companies may be required to post collateral in connection with credit derivatives and reinsurance transactions. Management believes that these subsidiaries' operating needs generally can be met from operating cash flow, including gross written premium and investment income on their respective investment portfolios. ACE currently maintains certain letters of credit on behalf of our subsidiaries in an aggregate amount of approximately \$26 million. We are currently negotiating with a third party for replacement letters of credit.

Net cash provided by operating activities was \$203.2 million, \$278.3 million and \$159.9 million during the years ended December 31, 2003, 2002 and 2001, respectively. These cash flows were primarily provided by premium received and investment income. Net cash provided by operating activities was \$203.2 million compared to \$278.3 million in 2002. The net cash provided by operating activities decreased by \$75.1 million despite the increase of \$142.0 million in net income in 2003 compared to 2002. The increase in net income is primarily due to the change in the market value of derivative financial instruments as the unrealized gains (losses) on derivative financial instruments increased from a loss of \$54.2 million in 2002 to income of \$98.4 million in 2003. This change had no cash flow impact. Operating cash flow was negatively impacted by the decrease in cash received on written premiums of approximately \$70 million in 2003 compared to 2002 primarily driven by the decreased premium writings of equity layer credit protection in 2003, which is reflected in the change in unearned premium reserves in the statement of cash flows.

In 2002, net cash provided by operating activities increased by \$118.4 million compared to 2001. This increase was driven primarily by the \$152.5 million of premium paid in 2001 by us to an affiliate for the Assured Guaranty Corp. Affiliate Reinsurance Transaction and the AGRI Affiliate Reinsurance Transaction.

Net cash used in financing activities was \$35.0 million, \$6.0 million and \$5.2 million during the years ended December 31, 2003, 2002 and 2001, respectively. During the years ended December 31, 2003, 2002 and 2001, ACE contributed capital of \$3.7 million, \$84.2 million and \$8.2 million, respectively, to us. These capital contributions were utilized to pay interest on long-term debt. The capital contribution in 2002 also included \$75.0 million for the purpose of the repayment of our long-term debt. In all years, these were non-cash contributions. Dividends paid to ACE were \$35.0 million, \$8.0 million and \$5.5 million during the years ended December 31, 2003, 2002 and 2001, respectively.

The following table summarizes our contractual obligations as of December 31, 2003:

As of December 31, 2003					
	Less Than One Year	1-3 Years	4-5 Years	After 5 Years	Total
(\$ in millions)					
Long-term debt				\$ 75.0	\$ 75.0
Lease obligations	\$ 3.3	\$ 10.0	\$ 6.4		19.7
Total	\$ 3.3	\$ 10.0	\$ 6.4	\$ 75.0	\$ 94.7

Credit Facilities

Assured Guaranty Corp. is party to a non-recourse credit facility with a syndicate of banks including Deutsche Bank AG which provides up to \$175 million specifically designed to provide rating agency-qualified capital to further support Assured Guaranty Corp.'s claims paying resources. The facility expires in November of 2010 and is subject to annual extension for an additional term of one year in order to maintain its term at seven years.

Assured Guaranty has entered into a credit agreement with a syndicate of banks, for which ABN AMRO Incorporated is acting as lead arranger and sole bookrunner providing for a \$250 million

unsecured credit facility to which each of Assured Guaranty, Assured Guaranty Corp. and Assured Guaranty (UK) is a party, as borrower. Banc of America Securities LLC acts as co-arranger for the facility, and Bank of America (an affiliate of Banc of America Securities LLC) participates as a lender. As of the date of this prospectus, no amounts were outstanding under this facility.

The \$250 million unsecured credit facility is a 364-day facility available for general corporate purposes, and any amounts outstanding under the facility at its expiration will be due and payable one year following the facility's expiry. Under the facility, Assured Guaranty has a borrowing limit not to exceed \$50 million, and Assured Guaranty (UK) has a borrowing limit not to exceed \$12.5 million. The facility's financial covenants require that Assured Guaranty (a) maintain a minimum net worth of 75% of its *pro forma* net worth (determined as of the first required reporting date under the facility), (b) maintain an interest coverage ratio of at least 2.5:1.0, and (c) maintain a maximum debt-to-capital ratio of 30%. In addition, the facility will require that Assured Guaranty Corp. (a) maintain qualified statutory capital of at least 80% of its statutory capital as of the fiscal quarter prior to the closing date of the facility, (b) maintain a ratio of aggregate net par outstanding to qualified statutory capital of not more than 150:1, and (c) maintain a maximum debt-to-capital ratio of 35%. While the obligations of the borrowers under the facility are several, a default by one borrower will give rise to a right of the lenders to terminate the facility and accelerate all amounts then outstanding.

Investment Portfolio

Our investment portfolio consisted of \$2,052.2 million of fixed maturity securities, \$137.5 million of short-term investments and had a duration of 5.4 years as of December 31, 2003. Our fixed maturity securities are designated as available for sale in accordance with FAS 115 "Accounting for Certain Investments in Debt and Equity Securities." Fixed maturity securities are reported at fair value in accordance with FAS 115, and the change in fair value is reported as part of accumulated other comprehensive income.

The following table summarizes our investment portfolio as of December 31, 2003:

	Amortized Cost	Unrealized Gain	Unrealized Loss	Estimated Fair Value
	(\$ in millions)			
U.S. government and agencies	\$ 255.2	\$ 16.3	\$ (0.4)	\$ 271.1
Obligations of state and political subdivisions	788.4	65.4	(1.0)	852.8
Corporate securities	268.1	21.5	(1.1)	288.6
Mortgage-backed securities	538.9	13.2	(2.1)	549.9
Structured securities	75.8	2.3	(0.1)	77.9
Foreign government and agencies	11.4	0.5		11.9
Total available for sale	1,937.7	119.2	(4.7)	2,052.2
Short-term investments	137.5			137.5
Total investments	\$ 2,075.3	\$ 119.2	\$ (4.7)	\$ 2,189.7

As of December 31, 2003, we held the following investments denominated in currencies other than U.S. dollars:

Currency	Amortized Cost	Estimated Fair Value
	(\$ in millions)	
Sterling	\$ 30.6	\$ 31.7
Euro	3.7	3.7
Australian Dollar	0.6	0.6
	\$ 34.9	\$ 36.0

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

The amortized cost and estimated fair value of fixed maturity securities available for sale as of December 31, 2003, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. See note 9 of the notes to our combined financial statements for information on our fixed maturity securities available for sale as of December 31, 2003 and 2002.

	Amortized Cost	Estimated Fair Value
	(\$ in millions)	
Due within one year	\$ 21.8	\$ 22.2
Due after one year through five years	229.1	242.6
Due after five years through ten years	299.2	323.6
Due after ten years	848.7	913.9
Mortgage-backed securities	538.9	549.9
	\$ 1,937.7	\$ 2,052.2
Total	\$ 1,937.7	\$ 2,052.2

Fair value of the fixed maturity securities is based upon quoted market prices provided by either independent pricing services or, when such prices are not available, by reference to broker or underwriter bid indications. Our investment portfolio does not include any non-publicly traded securities. For a detailed description of our valuation of investments see " Critical Accounting Policies."

We review our investment portfolio for possible impairment losses. For additional information, see " Critical Accounting Policies."

The following table summarizes the ratings distributions of our investment portfolio as of December 31, 2003 and 2002. Ratings are represented by the lower of the Moody's and S&P classifications.

	As of December 31,	
	2003	2002
AAA or equivalent	74.6%	78.0%
AA	13.9	12.1
A	10.7	9.1
BBB	0.8	0.8
	100.0%	100.0%
Total	100.0%	100.0%

As of December 31, 2003 and 2002, our investment portfolio did not contain any securities that were not rated or rated below investment grade.

Short-term investments include securities with maturity dates equal to or less than one year from the original issue date. Our short-term investments are composed of money market funds, discounted notes and certain time deposits for foreign cash portfolios. Short-term investments are reported at cost, which approximates the fair value of these securities due to the short maturity of these investments.

Under agreements with our cedents and in accordance with statutory requirements, we maintain fixed maturity securities in trust accounts for the benefit of reinsured companies and for the protection of policyholders, generally in states where we or our subsidiaries, as applicable, are not licensed or accredited. The carrying value of such restricted balances as of December 31, 2003 and 2002 was \$370.0 million and \$355.2 million, respectively.

Under certain derivative contracts, we are required to post eligible securities as collateral, generally cash or U.S. government or agency securities. The need to post collateral under these transactions is

generally based on marked to market valuations in excess of contractual thresholds. The fair market values of our pledged securities totalled \$154.8 million as of December 31, 2003 and \$194.7 million as of December 31, 2002.

Market Risk

Market risk represents the potential for losses that may result from changes in the value of a financial instrument as a result of changes in market conditions. The primary market risks that impact the value of our financial instruments are interest rate risk, basis risk, such as taxable interest rates relative to tax-exempt interest rates, and credit spread risk. Each of these risks and the specific types of financial instruments impacted are described below. Senior managers in our risk management department are responsible for monitoring risk limits and applying risk measurement methodologies. The estimation of potential losses arising from adverse changes in market conditions is a key element in managing market risk. We use various systems, models and stress test scenarios to monitor and manage market risk. These models include estimates made by management that use current and historic market information. The valuation results from these models could differ materially from amounts that actually are realized in the market. See "Critical Accounting Policies Valuation of Investments."

Financial instruments that may be adversely affected by changes in interest rates consist primarily of investment securities. The primary objective in managing our investment portfolio is generation of an optimal level of after-tax investment income while preserving capital and maintaining adequate liquidity. Investment strategies are based on many factors, including our tax position, fluctuation in interest rates, regulatory and rating agency criteria and other market factors. Two external investment managers, Hyperion Capital Management and Lazard Freres, manage our fixed maturity investment portfolio in accordance with investment guidelines approved by our Board of Directors.

New Accounting Pronouncements

In May 2003, FASB issued FAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity" ("FAS 150"), which establishes standards for classifying and measuring certain financial instruments with characteristics of both liabilities and equity. FAS 150 requires the classification of a financial instrument that is within its scope as a liability (or an asset in some circumstances). FAS 150 is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003. The adoption of FAS 150 did not have a material impact on the combined financial statements.

In April 2003, FASB issued FAS No. 149, "Amendment of FASB Statement No. 133 on Derivative Instruments and Hedging Activities." This Statement amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts (collectively referred to as derivatives) and for hedging activities under FAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." This Statement improves financial reporting by requiring that contracts with comparable characteristics be accounted for similarly. For example, this Statement requires that financial guaranty insurance for which the underlying risk is linked to a derivative be accounted for as a derivative. This Statement is effective for contracts entered into or modified after June 30, 2003, except for the provisions of this Statement that relate to FAS No. 133 implementation issues that have been effective for fiscal quarters that began prior to June 15, 2003, and for hedging relationships designated after June 30, 2003. All provisions are to be applied prospectively, except for the provisions of this Statement that relate to FAS No. 133 implementation issues that have been effective for fiscal quarters that began prior to June 15, 2003. These provisions are to be applied in accordance with their respective effective dates. The adoption of FAS 149 did not have a material impact on the combined financial statements.

In December 2002, FASB issued FAS No. 148, "Accounting for Stock-Based Compensation Transition and Disclosure" ("FAS 148"). FAS 148 provides alternative methods of transitioning for a voluntary change to the fair-value based method of accounting for stock-based employee compensation. FAS 148 amends the disclosure requirements of FAS No. 123, "Accounting for Stock-Based Compensation" ("FAS 123"), to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based compensation and the effect of the method used on reported results. FAS 148 is effective for companies with fiscal year ending after December 15, 2002. We continue to account for stock-based compensation plans in accordance with Accounting Principles Board Opinion No. 25 ("APB 25").

Effective January 1, 2002, we adopted FAS No. 141, "Business Combinations" and FAS No. 142, "Goodwill and Other Intangible Assets." FAS No. 141, which supercedes APB 16, "Business Combinations," requires business combinations initiated after June 30, 2001 to be accounted for using the purchase method of accounting and provides specific criteria for initial recognition of intangible assets apart from goodwill. FAS No. 142, which supercedes APB 17, "Intangible Assets," requires that goodwill and intangible assets with indefinite lives no longer be amortized but instead tested for impairment at least annually. FAS No. 142 established new accounting and reporting standards for acquired goodwill and other intangible assets. It requires that an entity determine if the goodwill or other intangible assets has an indefinite or a finite useful life. Those with indefinite useful lives will not be subject to amortization and must be tested annually for impairment. See note 5 of the notes to our combined financial statements for further information.

In January 2003, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 46, "Consolidation of Variable Interest Entities" ("FIN 46"), as an interpretation of Accounting Research Bulletin No. 51, "Consolidated Financial Statements." FIN 46 addresses consolidation of variable interest entities ("VIEs") by business enterprises. An entity is considered a VIE subject to consolidation if the equity investment at risk is not sufficient to permit the entity to finance its activities without additional subordinated financial support or if the equity investors lack one of three characteristics of a controlling financial interest. First, the equity investors lack the ability to make decisions about the entity's activities through voting rights or similar rights. Second, they do not bear the obligation to absorb the expected losses of the entity if they occur. Lastly, they do not claim the right to receive expected returns of the entity if they occur, which are the compensation for the risk of absorbing the expected losses. FIN 46 requires that VIEs be consolidated by the entity that maintains the majority of the risks and rewards of ownership. This interpretation applies immediately to VIEs created after January 31, 2003 and to VIEs in which an enterprise obtains interest after that date. FASB deferred the effective date of FIN 46 until the end of the first interim or annual period ending after December 15, 2003 for VIEs created before February 1, 2003. The adoption of FIN 46 did not have a material impact on our combined financial statements.

In November 2002, FASB issued FASB Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" ("FIN 45"). FIN 45 outlines certain accounting guidelines, effective for fiscal years beginning after December 15, 2002, from which our insurance transactions and derivative contracts are excluded. In addition, FIN 45 expands the disclosures required by a guarantor in its interim and annual financial statements regarding obligations under certain guaranties. These disclosure requirements are effective for the year ended December 31, 2002. Our financial position and results of operations did not change as a result of the adoption of FIN 45.

BUSINESS**Overview**

We are a Bermuda-based company providing credit enhancement products to the municipal finance, structured finance and mortgage markets. We apply our credit expertise, risk management skills and capital markets experience to develop insurance, reinsurance and derivative products that meet the credit enhancement needs of our customers. We market our products directly and through financial institutions. We serve the U.S. and international markets.

Our financial results include three operating segments:

Financial guaranty direct, which protects the holder against an issuer's failure to pay principal and interest when due or other credit events.

Financial guaranty reinsurance, which indemnifies another financial guarantor, the "ceding company," against part or all of the loss the ceding company may sustain under financial guaranty policies it has reinsured to us.

Mortgage guaranty, which protects mortgage lenders and investors against the default of borrowers on mortgage loans, and provides reinsurance to mortgage guaranty insurers.

Our other segment includes businesses we have exited. The following table sets forth information for each of our segments for the year ended December 31, 2003:

	Gross Written Premiums		Combined Ratio
	Amount	Percent	
	(\$ in millions)		
Financial guaranty direct	\$ 71.2	27.0%	58.0%
Financial guaranty reinsurance	168.7	63.8	73.3
Mortgage guaranty	24.4	9.2	58.7
	\$ 264.3	100.0%	65.6%
Total operating segments			
Other	84.9		112.6
Total	\$ 349.2		83.7%

Our businesses have a history of strong income generation, producing cumulative net income of \$444.1 million since January 1, 2000. As of December 31, 2003, we had cash and invested assets of \$2.2 billion, total assets of \$2.9 billion and shareholder's equity of \$1.4 billion (\$1.3 billion on a pro forma basis after giving effect to the transactions described under "Formation Transactions"). Our invested assets as of December 31, 2003 consisted entirely of cash and fixed maturity securities with an average rating of AA+. Our past performance may not be indicative of future results.

Financial strength ratings are an important factor in establishing our competitive position in the markets in which we compete. The objective of these ratings is to provide an independent opinion of our financial strength and ability to meet our ongoing obligations to our policyholders. Ratings reflect the rating agencies' opinions of our financial strength, and are neither evaluations directed to investors

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

in the notes nor recommendations to buy, sell or hold the notes. As of the date of this prospectus, our insurance company subsidiaries have been assigned the following insurance financial strength ratings:

	Moody's	S&P	Fitch
Assured Guaranty Corp.	Aa1(Excellent)	AAA(Extremely Strong)*	Not rated**
AGRI	Aa2(Excellent)	AA(Very strong)	AA(Very strong)
AGRO	Aa2(Excellent)	AA(Very strong)	AA(Very strong)
Assured Guaranty Mortgage	Aa2(Excellent)	AA(Very strong)	AA(Very strong)

*
Assured Guaranty Corp.'s S&P ratings outlook is "Negative."

**
ACE and Fitch both agreed to withdraw Assured Guaranty Corp.'s Fitch rating.

Competitive Strengths

We believe that our competitive strengths enable us to capitalize on the opportunities in the credit enhancement markets. These strengths include:

Underwriting discipline and financial structuring expertise. We have a disciplined approach to underwriting that emphasizes profitability over market share. We have substantial experience in developing innovative credit enhancement solutions to satisfy the diverse risk and financial management demands of our customers. We emphasize an analytical underwriting process organized around integrated teams consisting of credit and quantitative analysts, risk management professionals and lawyers.

Established market relationships. Over the past 15 years we have developed strong relationships with key participants in our markets, including issuers, investors, financial guarantors and financial institutions. We seek to distinguish ourselves from our competitors by providing innovative credit enhancement solutions and superior execution and client service. We intend to capitalize on our long-standing relationships as we expand our presence in financial guaranty insurance and international markets.

Experienced management, underwriting team and board. Our senior management has an average of more than 16 years experience in the insurance, credit and financial guaranty markets. Our President and Chief Executive Officer, Dominic Frederico, has 29 years of insurance industry experience and has been the senior ACE executive supervising our business; and Michael Schozer, President of Assured Guaranty Corp., has 13 years of financial guaranty and banking experience. We also have a team of 15 senior underwriters with an average of approximately 12 years of financial guaranty or similar credit experience. Our board of directors also has substantial financial services industry experience.

Multiple locations and licenses. We have operations in Bermuda, the United States and the United Kingdom. We have a range of licenses that allows us to participate in many sectors of the credit enhancement market.

Corporate Strategy

Our objective is to build long-term shareholder value by achieving strong profitability through disciplined underwriting, proactive risk management and the growth of our business. Our goal is to improve our return on average equity (excluding the impact of realized gains and losses on investments and unrealized gains and losses on derivative financial instruments) to be consistent with the returns of the leading performers in the financial guaranty industry. The major elements of our strategy are:

Expand our direct financial guaranty business. We intend to expand our direct financial guaranty business beyond our historical focus on credit derivatives by substantially increasing the amount of

traditional financial guaranty insurance we write in U.S. and international markets. We believe the market for financial guaranty insurance will grow as the issuance of municipal and structured finance obligations continues to be strong, as capital providers continue to seek to reduce risk exposures and as the market for credit enhancement products develops further. We believe that we have an opportunity to expand our market position as investors seek to diversify their exposure to the small group of primary financial guarantors. We intend to write business in a manner consistent with achieving our goal of obtaining a "Aaa" rating from Moody's to match our "AAA" rating from S&P.

Expand our financial guaranty reinsurance business. Our commitment to the financial guaranty reinsurance market, readiness to execute transactions and financial strength afford us a significant opportunity to profitably gain market share. Decisions by two major competitors to exit this market have significantly reduced reinsurance capacity at a time when we believe demand for financial guaranty reinsurance is growing. We intend to utilize our flexible operating platform to improve our returns in this business.

Transition our mortgage guaranty business. We intend to write investment grade mortgage guaranty insurance and reinsurance that is consistent with our ratings objectives. Our industry experience and licenses enable us to provide mortgage credit enhancement in the form of either financial guaranty insurance or mortgage guaranty insurance to meet the specific needs of mortgage lenders and investors.

Expand our position in international markets. We intend to capitalize on significant growth opportunities in international markets. Our initial focus for international expansion is privatization finance initiatives in the United Kingdom, the largest market for financial guaranty insurance outside the United States, and public/private partnerships in the rest of Europe.

Maintain our commitment to financial strength. We recognize the importance of our excellent financial strength ratings and intend to write business in a manner consistent with achieving our goal of obtaining a "Aaa" rating from Moody's to match our "AAA" rating from S&P. We will maintain our financial strength through disciplined risk selection, prudent operating and financial leverage and a conservative investment posture.

Manage our capital efficiently. We will monitor rating agency capital adequacy requirements to appropriately deploy capital to optimize the execution of our business plan and our return on capital.

Industry Overview

Financial Guaranty Insurance

Financial guaranty insurance provides an unconditional and irrevocable guaranty that protects the holder of a financial obligation against non-payment of principal and interest when due. Financial guaranty insurance may be issued to the holders of the insured obligations at the time of issuance of those obligations, or may be issued in the secondary market to holders of municipal bonds and structured securities. Both issuers of and investors in financial instruments may benefit from financial guaranty insurance. Issuers benefit because the insurance may have the effect of lowering an issuer's cost of borrowing to the extent that the insurance premium is less than the value of the difference between the yield on the insured obligation (carrying the credit rating of the insurer) and the yield on the obligation if sold on the basis of its uninsured credit rating. Financial guaranty insurance also increases the marketability of obligations issued by infrequent or unknown issuers, as well as obligations with complex structures or backed by asset classes new to the market. Investors benefit from increased liquidity in the secondary market, added protection against loss in the event of the obligor's default on its obligation, and reduced exposure to price volatility caused by changes in the credit quality of the underlying insured issue.

Edgar Filing: ASSURED GUARANTY LTD - Form S-1/A

As an alternative to traditional financial guaranty insurance, credit protection relating to a particular security or issuer can be provided through a credit derivative, such as a credit default swap. Under the terms of a credit