American Overseas Group Limited Announces Second Quarter 2012 Net Loss Available to Common Shareholders of $2.5 Million and Operating Income of $1.5 Million.

HAMILTON, Bermuda, September 27, 2012 (BUSINESS WIRE) -- American Overseas Group Limited (BSX:AORE.BH) (Pink Sheets: AORE.PK) ("AOG" or the "Company") today reported second quarter 2012 net loss available to common shareholders of $2.5 million, or $0.93 per diluted share. This compares to net loss available to common shareholders of $1.5 million, or $0.58 per diluted share, for the second quarter 2011. Net loss available to common shareholders for the first six months of 2012 was $6.9 million, or $2.61 per diluted share, compared to net income of $4.5 million, or $1.70 per diluted share, for the first six months of 2011.

During the second quarter of 2012, operating income, a non GAAP financial measure, was $1.5 million, or $0.57 per diluted share, compared to an operating loss of $2.5 million, or $0.95 per diluted share, during the second quarter of 2011. Operating income for the first six months of 2012 was $1.7 million, or $0.66 per diluted share, compared to operating income of $2.3 million, or $0.88 per diluted share, for the first six months of 2011.

The Company's net income (loss) is calculated in conformity with U.S. generally accepted accounting principles ("GAAP"). The Company also provides information regarding its operating income, a non-GAAP financial measure, because the Company's management and Board of Directors, as well as many research analysts and investors, also evaluate financial performance on the basis of operating income, which excludes non-operating items such as realized investment gains or losses, unrealized gains or losses on credit derivatives and foreign currency gains or losses. Please refer to "Explanation of Non-GAAP Financial Measures" below for a description of operating income and for a reconciliation of operating income to net income.

Commenting on the financial results, the Company's Chief Executive Officer, David Steel, noted that, "Our 2012 second quarter net loss was largely the result of a $2.4 million net change in fair value of credit derivatives during the period and loss development on our financial guaranty reinsurance exposures. As noted in the past, we view operating income, which among other items excludes unrealized gains and losses on derivatives, as a better measure of quarterly performance. Our 2012 second quarter operating income of $1.5 million was largely driven by earned premiums net of our loss development primarily related to our US RMBS exposures. For the first six months of 2012, operating income was $1.7 million."

Summary of Operating Results

The Company reported a net loss of $2.5 million for the quarter ended June 30, 2012.

Earned premiums in the second quarter 2012 of $5.4 million were 49% higher than the $3.6 million earned in the second quarter 2011. After eliminating accelerated premiums from refundings of $3.1 million from total earned premiums, earned premiums in the second quarter 2012 were $2.3 million; this was 34% lower than the comparable 2011 period, which included accelerated premiums from refundings of $0.1 million. Earned premiums for the first six months 2012 of $8.4 million were 5% higher than the $8.0 million of earned premiums for the first six months of 2011. After eliminating accelerated premiums from refundings of $3.8 million, earned premiums for the first six months of 2012 were $4.6 million; this was 31% lower than the comparable period in 2011, which included accelerated premiums from refundings of $1.3 million. The decrease in earned premiums in the second quarter and first six months of 2012 as compared to the respective 2011 periods was primarily due to commutations and run off of the reinsured portfolio.

Net change in fair value of credit derivatives totaled a loss of $2.4 million in the second quarter 2012, compared to a $1.4 million loss in the second quarter of 2011. Net change in fair value of credit derivatives for the second quarter of 2012 was comprised of $3.0 million in unrealized losses and $0.6 million of realized gains. Net change in fair value of credit derivatives for the second quarter of 2011 was comprised of $0.1 million in unrealized gains on derivatives, and $1.5 million of realized losses. The net unrealized loss in the second quarter 2012 was primarily attributable to: (i) the increase in gross unrealized losses on credit derivative policies of $41.5 million as reported to us by our primary insurers, offset by (ii) the increase in the adjustment for the Company's own non-performance risk of $38.5 million. The increase in gross unrealized losses on credit derivative policies was primarily due to deterioration in pricing across the portfolio of collateralized debt obligations and other asset backed securities written in credit derivative form. In accordance with the Financial Accounting Standards Board ("FASB") Accounting Standards Codification 820 - "Fair Value Measurements and Disclosures" ("ASC 820"), the Company calculates an adjustment for its own non-performance risk. The effect of the ASC 820 requirement on AOG's derivative liabilities on the balance sheet was a reduction of $108.4 million at June 30, 2012. Net change in fair value of credit derivatives for the six months ended June 30, 2012 and 2011 were an $8.1 million loss and $1.1 million gain, respectively.

Net investment income for the second quarter 2012 was $1.9 million, 21% below the $2.4 million recorded in the first quarter 2011. For the six months ended June 30, 2012, net investment income was $4.0 million, 15% below the $4.7 million recorded in the first six months of 2011. The decrease in investment income in the three and six months ended June 30, 2012 was primarily the result of a decline in the book yield on the Company's investments from 3.2% as of June 30, 2011, to 2.5% as of June 30, 2012.

There were no realized gains on investments for the second quarter and first six months of 2012 compared to immaterial and $0.7 million realized gains for the same periods in 2011, respectively.

Losses and loss adjustment expenses were $3.4 million in the second quarter 2012, contributing to a loss ratio of 63%, compared to losses and loss adjustment expenses of $3.1 million and a loss ratio of 86% for the comparable 2011 period. For the six months ended June 30, 2012, losses and loss adjustment expenses were $4.1 million, contributing to a loss ratio of 49%, compared to losses of $3.6 million and a loss ratio of 44% for the comparable period in 2011. The increase in the six months ended June 30, 2012 loss ratio was primarily attributable to further adverse development on US residential mortgage backed securities ("RMBS") policies.

Acquisition expenses were $2.3 million in the second quarter of 2012 compared to $1.6 million for the comparable 2011 period. Acquisition expenses are closely related to earned premiums, and the increase in acquisition expenses for the second quarter 2012 as compared to the comparable 2011 period was primarily due to the increase in earned premiums in the period. Acquisition expenses for the first six months of 2012 and 2011 were $3.8 million and $3.5 million, respectively, consistent with the comparable earned premiums for those periods.

Second quarter 2012 operating expenses of $1.4 million were $0.3 million, or 18%, below the level in the second quarter of 2011. For the first six months of 2012 and 2011, operating expenses were $3.1 million and $3.6 million, respectively. The decrease in operating expenses reflects the Company's cost reduction efforts.

Balance Sheet

Total assets of $384.7 million at June 30, 2012 were $16.5 million below the level at December 31, 2011. This decrease was primarily related to the reduction in deferred policy acquisition costs and net reinsurance balances receivable due to the run off of the Company's reinsured portfolio and was slightly offset by the increase in the Company's recoverable on paid losses. Shareholders' equity of $87.1 million was $6.8 million, or 7.2%, below the level at December 31, 2011, primarily due the net loss from operations for the first six months. Book value per share was $32.91, a decrease of 7.4% from year-end 2011. Operating book value per share and adjusted operating book value per share, both of which are non-GAAP financial measures, were $52.23 and $78.50, respectively, at June 30, 2012, compared to $51.64 and $80.20, respectively, at December 31, 2011. Please refer to "Explanation of Non-GAAP Financial Measures" below for a description of operating book value per share and adjusted operating book value per share and for a reconciliation of each to book value.

Subsequent Events:

The Company’s operating subsidiary, American Overseas Reinsurance Company Limited (“AORE”), entered into a Settlement, Commutation and Release Agreement, dated as of August 20, 2012 (the “Agreement”), which, if consummated, would commute (the “Commutation”) the entire portfolio of financial guaranty reinsurance business it has assumed from Financial Guaranty Insurance Company (“FGIC”). A rehabilitation proceeding for FGIC pursuant to Article 74 of the New York Insurance Law is currently pending before the Supreme Court of the State of New York (the “Court”), and the effectuation of such Commutation is subject to approval of the Agreement by the Court. Approval of the Agreement is within the Court’s discretion, and no assurance can be given that such approval will be granted or when it will be granted. If the Court approves the Agreement, AORE will make a commutation payment to FGIC in the amount of $64.8 million and the Commutation will become effective upon FGIC’s receipt of such payment. The aggregate outstanding par value of the reinsurance portfolio proposed to be commuted was $4.4 billion as of June 30, 2012. The Commutation would have resulted in a GAAP loss of approximately $13.0 million if it had been completed at June 30, 2012.

Reports entitled, “Stratification of AORE Reinsured Portfolio Before and After Commutation with FGIC, Pro forma as of December 31, 2011” and “Mortgage and CDO Exposure (Q4 2011) Before and After Commutation with FGIC, Pro forma as of December 31, 2011” will be posted to AOG’s website under “Investor Information” and “Exposure Info.”

Forward-Looking Statements

This release contains statements that may be considered "forward-looking statements" within the meaning of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These statements include, without limitation, the Company's expectations respecting the volatility of its insured portfolio, losses, loss reserves and loss development, the adequacy and availability of its liquidity and capital resources, its current run off strategy, its consideration of other reinsurance businesses, its expense reduction measures and Court approval of the Commutation and the receipt of funds thereunder. These statements are based on current expectations and the current views of the economic and operating environment and are not guarantees of future performance. A number of risks and uncertainties, including economic competitive conditions, could cause actual results to differ materially from those projected in forward-looking statements. The Company's actual results could differ materially from those expressed or implied in the forward-looking statements. Among the factors that could cause actual results to differ materially are: (i) the Company's ability to execute its business strategy, including with respect to any new reinsurance businesses; (ii) changes in general economic conditions, including inflation, foreign currency exchange rates, interest rates and other factors; (iii) the loss of significant customers with which the Company’s operating subsidiary American Overseas Reinsurance Company Limited (the “Operating Subsidiary”) has a concentration of its reinsurance in force; (iv) legislative, regulatory and Court developments; (v) changes in regulations or tax laws applicable to the Company or its customers; (vi) more severe or more frequent losses associated with the Operating Subsidiary's insured portfolio; (vii) losses on credit derivatives; (viii) changes in the Company's accounting policies and procedures that impact the Company's reported financial results; (ix) the effects of ongoing and future litigation and (x) other risks and uncertainties that have not been identified at this time. The Company undertakes no obligation to revise or update any forward-looking statement to reflect changes in conditions, events, or expectations, except as required by law.

Explanation of Non-GAAP Financial Measures

The Company believes that the following non-GAAP financial measures included in this release serve to supplement GAAP information and are meaningful to investors:

Operating income (loss): The Company believes operating income (loss) is a useful measure because it measures income from operations, unaffected by non-operating items such as realized investment gains or losses, unrealized gains or losses on credit derivatives and foreign currency gains or losses. Operating income (loss) is typically used by research analysts and rating agencies in their analysis of the Company.

Operating book value per share and adjusted operating book value per share: The Company believes the presentation of operating and adjusted operating book value per share to be useful because they give a measure of the value of the Company, excluding non-operating items such as unrealized gains and losses on credit derivatives. The Company derives operating book value by beginning with GAAP book value and adding back the unrealized gain or loss portion of its derivative liability, excluding the impact of credit impairments. Adjusted operating book value per share begins with operating book value as calculated above and then adding or subtracting the value of:

a. GAAP unearned premium reserves (on policies classified as financial guarantee);

b. Deferred acquisition costs;

c. Unearned premiums reserves and the present value of estimated future installment premiums net of ceding commissions on credit derivative policies (discounted at 0.72% at June 30, 2012 and 0.83% at December 31, 2011);

d. Unrealized appreciation or depreciation of investments; and

e. Noncontrolling interest in subsidiary – Class B preference shares.

Credit impairments on insured credit default swap ("CDS") contracts: Management measures and monitors credit impairments on AORE’s credit derivatives, which are expected to be paid out over the term of the CDS contracts. The credit impairments are a non-GAAP financial measure which management believes to be useful to analysts and investors in reviewing the results of our entire portfolio of policies. Management considers credit derivative policies as a normal extension of AORE's financial guarantee business and reinsurance in substance.

Reconciliations of these non-GAAP financial measures to the most comparable GAAP measures are set forth below.

Information About the Company

American Overseas Group Limited is a Bermuda-based holding company. Its operating subsidiary, American Overseas Reinsurance Company Ltd., has historically provided financial guaranty reinsurance for U.S. and international public finance and structured finance transactions. More information can be found at www.aoreltd.com.

American Overseas Group Limited
Consolidated Balance Sheets
(unaudited)
As at June 30, 2012 and December 31, 2011
(dollars in thousands)

	June 30, 2012	December 31, 2011
Assets		
Investments:		
Fixed-maturity securities held as available for sale, at fair value (Amortized cost: $196,904 and $261,914)	$ 209,900	$ 274,809
Cash and cash equivalents	8,284	13,253
Restricted cash	119,288	49,429
Accrued investment income	1,352	1,593
Reinsurance balances receivable, net	-	13,505
Recoverables on paid losses	6,565	6,158
Deferred policy acquisition costs	38,527	41,890
Deferred expenses	390	433
Other assets	392	153
Total Assets	$ 384,698	$ 401,223
Liabilities and Equity		
Liabilities:		
Loss and loss expense reserve	$ 62,243	$ 80,998
Unearned premiums	102,713	110,187
Accounts payable and accrued liabilities	526	1,121
Reinsurance balances payable, net	7,758	-
Derivative liabilities	57,598	48,303
Redeemable Series A preference shares ($1,000 redemption value and $0.10 par value; authorized shares - 75,000; issued and outstanding shares - 59,700 at June 30, 2012 and December 31, 2011)	59,700	59,700
Total Liabilities	290,538	300,309
Shareholders' Equity:		
Common shares	2,648	2,643
Additional paid-in capital	231,524	231,468
Accumulated other comprehensive income	12,996	12,895
Retained deficit	(160,019)	(153,103)
Total Shareholders' Equity	87,149	93,903
Noncontrolling interest - Class B preference shares of subsidiary	7,011	7,011
Total Equity	94,160	100,914
Total Liabilities and Equity	$ 384,698	$ 401,223

American Overseas Group Limited
Consolidated Statements of Operations
(unaudited)
For the three and six months ended June 30, 2012 and 2011
(dollars in thousands except share and per share amounts)

	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Revenues				
Net premiums earned	$ 5,369	$ 3,612	$ 8,395	$ 8,024
Change in fair value of credit derivatives				
Realized gains (losses) and other settlements	674	(1,473)	1,248	(19)
Unrealized gains (losses)	(3,034)	118	(9,368)	1,125
Net change in fair value of credit derivatives	(2,360)	(1,355)	(8,120)	1,106
Net investment income	1,884	2,350	3,962	4,748
Net realized gains on sale of investments	-	8	-	694
Total other-than-temporary impairment losses	-	-	-	-
Portion of impairment losses recognized in other comprehensive income (loss)	-	-	-	-
Net other-than-temporary impairment losses (recognized in earnings)	-	-	-	-
Foreign currency gains (losses)	(286)	200	(97)	512
Total revenues	**4,607**	**4,815**	**4,140**	**15,084**
Expenses				
Losses and loss adjustment expenses	3,381	3,121	4,120	3,564
Acquisition expenses	2,305	1,556	3,803	3,456
Operating expenses	1,376	1,669	3,135	3,569
Total expenses	**7,061**	**6,346**	**11,058**	**10,589**
Net income (loss) available to common shareholders	**$ (2,454)**	**$ (1,531)**	**$ (6,918)**	**$ 4,495**
Net income (loss) per common share:				
Basic	$ (0.93)	$ (0.58)	$ (2.62)	$ 1.70
Diluted	(0.93)	(0.58)	(2.61)	1.70
Weighted average number of common shares outstanding:*				
Basic	2,647,178	2,642,641	2,645,210	2,641,187
Diluted	2,651,411	2,642,641	2,647,772	2,649,699

* Shares outstanding and net income (loss) per common share for the quarter and six months ended June 30, 2012, reflect the effects of a 1 for 10 reverse stock split on November 8, 2011.
For comparative purposes, the outstanding shares and net income (loss) per common share for the quarter and six months ended June 30, 2011 have been adjusted to reflect the change in capital structure as if the reverse stock split had occurred in that period.

Reconciliation of net income to operating income:

	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Operating income				
Net income (loss) available to common shareholders	$ (2,454)	$ (1,531)	$ (6,918)	$ 4,495
Less: Realized (gains) on sale of investments and other-than-temporary impairment losses	-	(8)	-	(694)
Less: Unrealized (gains) losses on credit derivatives	3,034	(118)	9,368	(1,125)
Add back: credit impairment on derivatives	653	(666)	(812)	156
Less: Foreign currency (gains) losses	286	(200)	97	(512)
Operating income	$ 1,518	$ (2,523)	$ 1,735	$ 2,320
Net income (loss) per diluted share	$ (0.93)	$ (0.58)	$ (2.61)	$ 1.70
Less: Realized (gains) on sale of investments and other-than-temporary impairment losses	0.00	(0.00)	0.00	(0.26)
Less: Unrealized (gains) losses on credit derivatives	1.14	(0.04)	3.53	(0.42)
Add back: credit impairment on derivatives	0.25	(0.25)	(0.31)	0.06
Less: Foreign currency (gains) losses	0.11	(0.08)	0.04	(0.19)
Operating income per diluted share	$ 0.57	$ (0.95)	$ 0.66	$ 0.88

Reconciliation of book value to operating book value and adjusted operating book value:

	As at June 30, 2012	As at Dec 31, 2011
Shares outstanding [(1)]	2,648	2,643
Operating Book Value		
Shareholders' Equity (Book Value)	87,149	93,903
Derivative liability [(2)]	57,248	47,880
Credit impairments on derivatives	(6,094)	(5,283)
Operating book value per share	52.23	51.64
Noncontrolling interest in subsidiary - Class B preference shares	7,011	7,011
Unearned premiums [(3)]	103,476	111,123
Deferred acquisition costs	(38,527)	(41,890)
Present value of installment premiums [(4)]	10,607	12,117
Unrealized gains on investments	(12,996)	(12,895)
Adjusted operating book value per share	$ 78.50	$ 80.20

(1) Shares outstanding and book values per share for the quarter and six months ended June 30, 2012 reflect the effects of a 1 for 10 reverse stock split on November 8, 2011. For comparative purposes, the outstanding shares and the book values per share for the quarter and six months ended June 30, 2011 have been adjusted to reflect the change in capital structure as if the reverse stock split had occurred in that period.

(2) Represents only the unrealized gains portion of the derivative liability.

(3) Includes unearned premium balances on financial guaranty and credit derivative policies. The unearned premiums on financial guaranty policies include the present value of future installment premiums, net of ceding commissions.

(4) Estimated present value of future installments, net of ceding commissions, on policies written in credit derivative form only. At June 30, 2012 and December 31, 2011, the discount rate was 0.72% and 0.83%, respectively.

The Company will post its second quarter 2012 financial results to its website at www.aoreltd.com under "Investor Information". If you are a shareholder of American Overseas Group Limited and wish to receive a hard copy of the financial statements by mail, please contact:

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