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ANALYST QUICK NOTES
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American International Group Inc. (NYSE: AIG: BUY)
Target Price: $75
Jacob Kilstein, CFA
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Overview

- AIG is down YTD due to poor 4Q16 results, but a CEO transition and potential lower taxes can lift the shares.
- On March 9, CEO Peter Hancock submitted his resignation to the board. The shares rose 2.5% on the news.
- We don't think the resignation was voluntary, as Carl Icahn, a board member with 5% ownership, had been publicly pushing for his ouster last year. Icahn wanted someone who better knew the P&C business and was more open to change.
- The shares are down 5% YTD, while the market is up 5%.
- A 4Q earnings miss (and net loss), due to a $5.6 billion reserve charge, a lower ROE target (9.5% from 10.0%), and news of board member and activist investor John Paulson's stock sale caused shares to drop 9% on February 14, the largest one-day drop since 2011.
  - The 4Q after-tax operating loss came to $2.8 billion or $2.72 per share, while the consensus forecast had called for operating income of $0.42 per share.

Thesis

- We like the price after the shares dropped. They have fluctuated between $60 and $68 recently and we see the share price of $62 as a good entry point.
  - Number one catalyst, tax breaks: If the effective tax rate drops to 20% from 28.5%, EPS will get a big boost. We see legislation passing in 2H17 and EPS benefitting as soon as 4Q17.
  - Second: We also expect stronger investment returns as the Fed raises interest rates – but not much for now, as rates are still too low.
  - Third, deregulation: Republicans want less onerous burdens for businesses, and financial institutions stand to benefit. AIG, in particular, may shed its SIFI designation, which would free up capital.

Now what?

- On March 23, AIG management reiterated its 2017 goals, which gives us confidence.
    - 9.5% ROE, driven by loss ratio improvement/risk selection.
    - Cost cuts.
    - A two-year plan to return $25 billion to stockholders.
- We think the CEO transition will be good for the shares, as employee morale and investor sentiment can rise.
    - A CEO with Property & Casualty expertise should help that business.
    - Activist shareholders Icahn and Paulson want to break up the company, make it smaller and remove the SIFI label – all of which are stronger possibilities with CEO Hancock gone.

Earnings and growth

- Our EPS estimates are for $5.09 in 2016 and $6.09 in 2017.

Valuation

- The shares trading at a discount P/E and price/book than peers.
    - P/E: 12.1x vs. 16.8x for peers.
    - P/B: 0.8x vs. 1.4x for peers.
    - Yield: 2.1%, in line with peers.
- Target price of $75 implies peer 9.5x multiple.
- Risks: more reserve charges, low rates, weak markets, strong USD.
- We see a 20% upside + 2.1% yield = 22% total return.