

Ambac

2012 Quarterly Operating Supplement

Q2

Company Profile

Ambac Financial Group, Inc., headquartered in New York City, is a holding company whose affiliates provided financial guarantees and financial services to clients in both the public and private sectors around the world. As previously announced, on November 8, 2010, Ambac filed for a voluntary petition for relief under Chapter 11 of the United States Bankruptcy Code (“Bankruptcy Code”) in the United States Bankruptcy Court for the Southern District of New York (“Bankruptcy Court”). The Bankruptcy Court entered an order confirming Ambac’s plan of reorganization on March 14, 2012. However, Ambac is not currently able to estimate when it will be able to consummate such reorganization. Until the plan of reorganization is consummated and Ambac emerges from bankruptcy, Ambac will continue to operate in the ordinary course of business as “debtor-in-possession” in accordance with the applicable provisions of the Bankruptcy Code and the orders of the Bankruptcy Court. Ambac Financial Group, Inc.’s common stock trades in the over-the-counter market under ticker symbol ABKFQ. Upon consummation of the plan of reorganization, Ambac’s existing common stock will be cancelled and extinguished and the holders thereof will not be entitled to receive, and will not retain, any property or interest on account of such common stock.

Ambac's principal operating subsidiary, Ambac Assurance Corporation, is a guarantor of public finance and structured finance obligations.

Company Information

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To obtain a copy of Ambac Financial Group, Inc.’s latest annual or quarterly report filed with the Securities and Exchange Commission or the most recent Annual Report to Stockholders, please visit our website at www.ambac.com.

Ambac Financial Group, Inc.
Quarterly Operating Supplement
Second Quarter 2012

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Note 1: Internal Ambac Assurance credit ratings contained in this Supplement are provided solely to indicate the underlying credit quality of guaranteed obligations based on the view of Ambac Assurance. In cases where Ambac Assurance has insured multiple tranches of an issue with varying internal ratings, or more than one obligation of an issuer with varying internal ratings, a weighted average rating is used. Ambac Assurance credit ratings are subject to revision at any time and do not constitute investment advice. Ambac Assurance, or one of its affiliates, has insured the obligations listed and may also provide other products or services to the issuers of these obligations for which Ambac may have received premiums or fees.

Note 2: Information contained in this report is unaudited.

Key Financial Data
(Dollars in millions except share data)

| | 2Q 2012 | 1Q 2012 | 2011 | 2010 | 2009 | 2008 |
|---|-----------|-----------|-----------|-----------|-----------|-----------|
| Summary GAAP Financial Data: | | | | | | |
| Statement of Operations: | | | | | | |
| Net premiums earned | \$103 | \$95 | \$406 | \$546 | \$797 | \$1,023 |
| Net investment income | 94 | 112 | 355 | 359 | 554 | 739 |
| Change in fair value of credit derivatives | (7) | (7) | 48 | 60 | 3,813 | (4,031) |
| Gain (loss) on variable interest entities (VIEs) | 6 | 15 | (214) | (617) | 7 | - |
| Loss and loss expenses | 741 | (2) | 1,859 | 719 | 2,815 | 2,228 |
| Underwriting and operating expenses | 34 | 37 | 141 | 254 | 206 | 274 |
| Interest expense | 32 | 34 | 128 | 181 | 154 | 349 |
| Reorganization items | 1 | 2 | 50 | 32 | - | - |
| Net (loss) income attributable to Ambac Financial Group, Inc. | (811) | 253 | (1,960) | (753) | (15) | (5,609) |
| Net (loss) income per diluted share attributable to AFG, Inc common shareholders | (\$2.68) | \$0.84 | (\$6.48) | (\$2.56) | (\$0.05) | (\$22.31) |
| Balance Sheets: | | | | | | |
| Total non-VIE investments | \$6,687 | \$6,945 | \$6,877 | \$6,853 | \$8,703 | \$10,293 |
| Premium receivable | 1,830 | 1,918 | 2,028 | 2,423 | 3,718 | 29 |
| Subrogation recoverable | 442 | 519 | 660 | 714 | 903 | 10 |
| Total VIE assets | 16,620 | 16,858 | 16,543 | 17,931 | 3,277 | n/a |
| Total assets | 26,612 | 27,373 | 27,114 | 29,047 | 18,886 | 17,260 |
| Unearned premium reserve | 3,138 | 3,291 | 3,457 | 4,008 | 5,687 | 2,382 |
| Loss and loss expense reserve | 7,608 | 6,924 | 7,044 | 5,289 | 4,772 | 2,276 |
| Obligations under investment and payment agreements | 443 | 547 | 547 | 806 | 1,291 | 3,358 |
| Long-term debt ⁽¹⁾⁽²⁾ | 144 | 227 | 224 | 208 | 1,632 | 1,624 |
| Liabilities subject to compromise ⁽¹⁾ | 1,707 | 1,707 | 1,707 | 1,695 | - | - |
| Ambac Financial Group, Inc. stockholders' (deficit) equity | (4,416) | (3,577) | (3,813) | (2,009) | (2,288) | (3,782) |
| Summary Statutory Data of Ambac Assurance: | | | | | | |
| Invested assets | \$5,795 | \$5,982 | \$5,854 | \$5,943 | \$8,009 | \$10,397 |
| Loss and loss expense reserve | 3,786 | 3,537 | 3,226 | 2,478 | 1,141 | 1,169 |
| Estimated impairment losses on credit derivatives | - | - | - | - | 3,842 | 3,352 |
| Policyholders' Surplus | 100 | 233 | 495 | 1,027 | 802 | 1,554 |
| Qualified statutory capital | 621 | 521 | 688 | 1,540 | 1,154 | 3,484 |
| Total claims-paying resources | \$7,310 | \$7,534 | \$7,450 | \$7,877 | \$10,790 | \$13,501 |
| Net par outstanding | \$251,162 | \$263,408 | \$272,504 | \$318,854 | \$390,406 | \$434,310 |
| Net debt service outstanding | \$396,286 | \$418,328 | \$433,484 | \$509,429 | \$619,566 | \$695,954 |

1) Long-term debt for 2010 and beyond represents surplus notes issued by Ambac Assurance Corporation and the Segregated Account of Ambac Assurance Corporation. Long-term debt for all years excludes the portion of long-term debt associated with variable interest entities. Long-term debt associated with Ambac Financial Group, Inc. for 2010 and beyond is included under liabilities subject to compromise on the unaudited Consolidated Balance Sheets.

2) The decline in 2012 was the result of Ambac Assurance exercising options to repurchase surplus notes with an aggregate par value of \$789.2 million.

Ambac Assurance

Claims-Paying Resources ⁽¹⁾ and Statutory Financial Ratios

| (\$ Thousands, Except Ratios) | June 30, 2012 | December 31, 2011 |
|--|--------------------|--------------------|
| Contingency reserve | \$521,457 | \$192,738 |
| Policyholders' Surplus ⁽²⁾⁽³⁾ | 100,000 | 495,293 |
| Qualified statutory capital | 621,457 | 688,031 |
| Unearned premiums | 1,557,595 | 1,700,424 |
| Losses and loss adjustment expenses | 3,786,218 | 3,226,327 |
| Segregated Account liabilities ⁽³⁾ | (436,277) | - |
| Policyholders' reserves | 5,528,993 | 5,614,782 |
| Present Value of Future Installment Premiums ⁽⁴⁾ | 678,922 | 770,880 |
| Ambac Assurance UK Ltd. Claims-Paying Resources ⁽⁵⁾ | 1,102,009 | 1,064,683 |
| Total Claims-Paying Resources | \$7,309,924 | \$7,450,345 |
| Net financial guarantees in force ⁽⁶⁾ | \$396,285,818 | \$433,483,509 |
| Claims-Paying Ratio ⁽⁷⁾ | 54 : 1 | 58 : 1 |
| Gross financial guarantees in force | \$434,912,229 | \$474,304,676 |
| Gross par outstanding | \$274,092,541 | \$296,463,186 |

- 1) Total claims-paying resources quantifies total resources available to pay claims.
- 2) Surplus Notes with a par value of \$1,300 million and \$2,089 million are included in the capital and surplus for June 30, 2012 and December 31, 2011, respectively. The Surplus Notes rank senior to Ambac's equity investment in Ambac Assurance. There is residual value to Ambac in Ambac Assurance only to the extent that funds remain at Ambac Assurance after the payment of claims under outstanding financial guaranty policies and the redemption, repurchase or repayment in full of the Surplus Notes and Ambac Assurance's auction market preferred shares.
- 3) Pursuant to a prescribed practice by the State of Wisconsin Office of the Commissioner of Insurance, Ambac Assurance is not obligated to make payments to the Segregated Account if its surplus is less than \$100,000. Accordingly \$436,277 of losses in the Segregated Account did not reduce Ambac Assurance's surplus at June 30, 2012.
- 4) Present value of future installment premiums includes premiums on installment financial guarantee insurance contracts (excluding Ambac UK) and credit derivatives. Present value calculations utilize Ambac internal estimates discounted at 5.1%.
- 5) Ambac UK's claims paying resources will become available to Ambac Assurance only to the extent Ambac UK receives approval from its regulator to dividend monies to Ambac Assurance. Components of Ambac UK's claims paying resources are discounted at Ambac UK's investment rate of return.
- 6) Includes Ambac UK net financial guarantees in force of \$39,868,184 and \$42,716,953 as of June 30, 2012 and December 31, 2011, respectively. Financial guarantees in force includes principal and interest on insurance policies and credit derivative contracts.
- 7) Claims-paying Ratio is net financial guarantees in force divided by total claims-paying resources.

Ambac Assurance

Rollforward of Statutory Policyholders' Surplus⁽¹⁾

(in thousands)

| | For the six months ended June 30, 2012 | For the year ended December 31, 2011 |
|--|---|---|
| Policyholders' Surplus, beginning of period | \$ 495,293 | \$ 1,026,920 |
| Net income (loss) ⁽²⁾⁽³⁾⁽⁴⁾ | 700,071 | (835,795) |
| Issuance of surplus notes - segregated account ⁽³⁾ | - | 3,000 |
| Issuance of junior surplus notes - segregated account ⁽⁵⁾ | - | 36,082 |
| Exercise of surplus notes - general account ⁽⁴⁾ | (789,179) | - |
| Change in contingency reserves ⁽⁶⁾ | (328,306) | 306,010 |
| Change in investment in subsidiaries | 36,866 | 39,764 |
| Unrealized gain (loss) on non-impaired, BIG investments | 2,742 | (24,177) |
| Other changes in surplus | (17,487) | (56,511) |
| Policyholders' Surplus, end of period ⁽⁷⁾ | <u>\$ 100,000</u> | <u>\$ 495,293</u> |

- 1) Information for Ambac Assurance and the Segregated Account of Ambac Assurance are combined for the purposes of this schedule.
- 2) Net income for the six months ended June 30, 2012 excludes losses of the Segregated Account of Ambac Assurance of \$436,277. Net loss for the year ended December 31, 2011 excludes losses of the Segregated Account of Ambac Assurance of \$0.
- 3) Net income (loss) includes incurred losses under commutations in 2012 and 2011. In 2012, the Segregated Account commuted insurance policies (\$341,000 of par outstanding) with a cash payment of \$17,475. These commutations generated net incurred losses of \$10,485 in 2012. In 2011, the Segregated Account commuted insurance policies (\$4,002,129 of par outstanding) with cash payments totaling \$256,085 and the issuance of segregated account surplus notes with a par value of \$3,000. These commutations generated net incurred losses of \$24,121 in 2011.
- 4) Net income for the six months ended June 30, 2012 includes a gain on the exercise of surplus note call options of \$600,733. Additionally, the exercise of surplus note call options reduced surplus directly by \$789,179, the par of the related surplus notes, resulting in an overall surplus reduction of \$188,446, which is equal to the total cash payment.
- 5) In May 2011, the Segregated Account issued junior surplus notes with a par value of \$36,082 in connection with a settlement agreement to terminate Ambac's office lease with One State Street LLC.
- 6) Effective December 31, 2011, Ambac Assurance received regulatory approval from the Wisconsin Insurance Commissioner to release \$430,332 of contingency reserves during the year ended December 31, 2011.
- 7) Pursuant to a prescribed practice by the State of Wisconsin Office of the Commissioner of Insurance, the results of the Segregated Account are not included in Ambac Assurance's statutory financial statements if Ambac Assurance's surplus is less than \$100,000.

Ratio of Net Claims Presented

| (\$ Thousands) | 2012 | 2011 | 2010 | 2009 | 2008 |
|--|------------|-------------|-------------|-------------|-------------|
| Net claims presented and paid (recovered) - Insurance ⁽¹⁾ | (\$37,433) | \$147,762 | \$290,519 | \$1,458,498 | \$571,012 |
| Net claims presented and not paid - Insurance ⁽²⁾ | 884,994 | 1,357,181 | 1,411,445 | - | - |
| Net Credit Derivatives payments | - | - | (263) | 47,749 | 7,153 |
| Net Credit Derivatives commutation payments ⁽³⁾ | - | - | 4,589,107 | 1,380,628 | 1,850,000 |
| Total net claims presented for payment | \$847,561 | \$1,504,943 | \$6,290,808 | \$2,886,875 | \$2,428,165 |
| Net insurance premiums and credit derivative fees | \$204,319 | \$422,971 | \$577,195 | \$846,001 | \$1,085,482 |
| Ratio of net claims presented ⁽⁴⁾ | 414.8% | 355.8% | 1089.9% | 341.2% | 223.7% |

Estimated Future Gross RMBS Claim Payments (Recoveries) ^{(5) (6)}

| (\$ Thousands) | |
|----------------|---------------------|
| 2012 | 578,970 |
| 2013 | 963,888 |
| 2014 | 848,775 |
| 2015 | 404,826 |
| 2016 | 234,737 |
| 2017 | 159,398 |
| 2012 | 578,970 |
| 2013-2017 | 2,611,623 |
| 2018-2022 | 305,904 |
| 2023-2027 | 70,183 |
| 2028-2032 | 48,170 |
| After 2032 | 857,869 |
| Total | <u>\$ 4,472,718</u> |

- 1) Net claims presented and paid (recovered) are net of subrogation received of \$63,095, \$104,805, \$107,914, \$111,737, and \$11,719 for the six months ended June 30, 2012, and the full years ended December 31, 2011, 2010, 2009, and 2008, respectively. Includes the issuance of surplus notes at par value in the amount of \$0, \$3,000, and \$50,000 for the six months ended June 30, 2012 and the years ended December 31, 2011 and 2010, respectively.
- 2) On March 24, 2010, Ambac Assurance established a Segregated Account. The purpose of the Segregated Account is to segregate certain Ambac Assurance liabilities, and in connection with such segregation Ambac Assurance has allocated certain policies to the Segregated Account. On June 4, 2012, the Rehabilitation Court approved the Rehabilitator's motion to make partial interim policy claim payments to Segregated Account policyholders. As a result, the Segregated Account will, begin paying 25% of each permitted policy claim that has arisen since the commencement of the Segregated Account Rehabilitation Proceedings and 25% of each policy claim submitted and permitted in the future. Claims presented and not paid are included in our net insurance reserves. Please see discussion in Ambac's June 30, 2012 Form 10-Q.
- 3) 2010 credit derivative commutation payments include the issuance of surplus notes by Ambac Assurance at par in the amount of \$2,000,000.
- 4) Ratio of net claims presented is total net claims presented for payment divided by net premiums earned and other credit enhancement fees.
- 5) Represents management's estimate of future loss obligations, gross of reinsurance recoveries and net of subrogation recoveries. Future losses exclude claims presented and unpaid through June 30, 2012. Actual payments or recoveries may differ from estimates.
- 6) Gross of estimated recoveries of \$30,508, \$1,571,218, \$953,809 and \$258,016 in 2012, 2013, 2014 and 2015, respectively for breaches of representation and warranties on certain RMBS transactions.

Summary of Net Insurance Loss Reserves (GAAP) and Credit Derivative Impairments

| (\$ Thousands) | 6/30/12 | 12/31/11 | 12/31/10 | 12/31/09 |
|---|--------------------|--------------------|--------------------|--------------------|
| Total insurance reserves ⁽¹⁾ | 7,002,618 | 6,230,780 | 4,424,450 | 3,777,321 |
| Estimated credit impairment losses on credit derivatives ⁽²⁾ | 22,294 | 36,940 | 22,055 | 4,208,198 |
| Total impairment losses | 7,024,912 | 6,267,720 | 4,446,505 | 7,985,519 |
| Mark-to-market reserve (asset) on credit derivatives ⁽²⁾ | 189,323 | 153,713 | 199,629 | (1,168,707) |
| Grand total net insurance loss reserves and credit derivatives | <u>\$7,214,235</u> | <u>\$6,421,433</u> | <u>\$4,646,134</u> | <u>\$6,816,812</u> |

Summary of Below Investment Grade Exposures⁽³⁾

| (\$ Thousands) | Segregated Account Net Par Outstanding | Total Net Par Outstanding | Total Impairment Losses |
|--|---|------------------------------|----------------------------|
| Public Finance: | | | |
| Lease & tax backed | \$0 | \$1,133,642 | \$65,885 |
| Transportation revenue | 86,286 | 618,682 | 51,912 |
| General obligation | - | 504,264 | 63,480 |
| Housing | - | 775,741 | 956 |
| Health care | - | 72,487 | 68 |
| Other | - | 986,095 | 15,917 |
| Total Public Finance | <u>86,286</u> | <u>4,090,911</u> | <u>198,218</u> |
| Structured Finance: | | | |
| Mortgage-backed & home equity - first lien & other | 11,139,395 | 11,139,395 | 3,962,460 |
| Mortgage-backed & home equity - second lien | 8,246,043 | 8,246,043 | 792,253 |
| Student loans | 7,237,968 | 7,264,874 | 942,315 |
| Other | 137,000 | 3,001,094 | 1,047,363 |
| Total Structured Finance | <u>26,760,406</u> | <u>29,651,406</u> | <u>6,744,391</u> |
| International Finance: | 306,495 | 4,855,383 | 82,303 |
| Total | <u>\$27,153,187</u> | <u>\$38,597,700</u> | <u>\$7,024,912</u> |

1) As a result of the claim moratorium on the Segregated Account of Ambac Assurance by the Rehabilitator, \$3,653,621 of claims have been presented and not paid. Total insurance reserves are inclusive of claims presented and not paid.

2) Total net mark-to-market losses are \$211,617 as of June 30, 2012, and \$190,653, \$221,684, and \$3,039,491 as of December 31, 2011, 2010, and 2009, respectively and are reported on the consolidated balance sheet under derivative liabilities and derivative assets.

3) On March 24, 2010, Ambac Assurance established a Segregated Account. The purpose of the Segregated Account is to segregate certain Ambac Assurance liabilities, and in connection with such segregation Ambac Assurance has allocated certain insurance policies to the Segregated Account. Please see discussion in Ambac's December 31, 2011 Form 10-K.

Net Insurance Premiums Earned and Fees on Credit Derivatives (GAAP)

| 2012 (\$ Thousands) | First Quarter | Second Quarter | Third Quarter | Fourth Quarter | Year-to Date |
|--|---------------|----------------|---------------|----------------|--------------|
| Public Finance | \$39,016 | \$39,283 | | | \$78,299 |
| Structured Finance ⁽¹⁾ | 18,293 | 6,632 | | | 24,925 |
| International Finance | 21,851 | 21,261 | | | 43,112 |
| Total Normal Insurance Premiums Earned | 79,160 | 67,176 | - | - | 146,336 |
| Accelerated Premiums Earned | 15,790 | 35,866 | | | 51,656 |
| Total Premiums Earned | \$94,950 | \$103,042 | - | - | \$197,992 |
| Fees on credit derivative contracts ⁽²⁾ | \$3,254 | \$3,073 | | | \$6,327 |

| 2011 (\$ Thousands) | First Quarter | Second Quarter | Third Quarter | Fourth Quarter | Full Year |
|--|---------------|----------------|---------------|----------------|-----------|
| Public Finance | \$42,400 | \$42,541 | \$40,359 | \$39,784 | \$165,084 |
| Structured Finance | 29,691 | 25,034 | 22,123 | 20,458 | 97,306 |
| International Finance | 19,778 | 20,365 | 20,738 | 22,450 | 83,331 |
| Total Normal Insurance Premiums Earned | 91,869 | 87,940 | 83,220 | 82,692 | 345,721 |
| Accelerated Premiums Earned | (70) | 11,331 | 18,835 | 30,153 | 60,249 |
| Total Premiums Earned | \$91,799 | \$99,271 | \$102,055 | \$112,845 | \$405,970 |
| Fees on credit derivative contracts ⁽²⁾ | \$5,323 | \$4,224 | \$3,829 | \$3,625 | \$17,001 |

Net Unearned Premium Amortization and Estimated Future Installment Premiums

| (\$ Millions) | Net Unearned Premium Amortization (GAAP) ⁽³⁾ | Fees on Credit Derivative Contracts (GAAP) | Estimated Net Future Installments ⁽⁴⁾ |
|-----------------------------------|---|--|--|
| 2012 (3rd and 4th Qtrs) | 127.6 | 5.9 | 74.4 |
| 2013 | 228.3 | 10.6 | 119.2 |
| 2014 | 208.0 | 7.3 | 107.9 |
| 2015 | 195.7 | 3.8 | 100.7 |
| 2016 | 185.0 | 2.4 | 94.0 |
| 2017 | 174.3 | 2.2 | 88.4 |
| 2012 (3rd and 4th Qtrs) | 127.6 | 5.9 | 74.4 |
| 2013-2017 | 991.3 | 26.3 | 510.2 |
| 2018-2022 | 729.2 | 7.9 | 358.1 |
| 2023-2027 | 519.8 | 0.1 | 245.7 |
| 2028-2032 | 333.9 | - | 170.0 |
| After 2032 | 239.0 | - | 144.5 |
| Total | \$2,940.8 | \$40.2 | \$1,502.9 |

- 1) For the three months ended March 31, 2012 and June 30, 2012, respectively, \$4,417 and \$12,758 of premium receivables relating to a non-investment grade obligation were deemed uncollectible and written off via a reduction to net insurance premiums earned.
- 2) Fees on credit derivative contracts are included in "Realized gains and losses and other settlements on credit derivative contracts" on the unaudited Consolidated Statement of Operations.
- 3) Represents unearned premium amounts for both upfront and installment paying policies, net of deferred ceded premiums, which is reported separately as an asset on the unaudited Consolidated Balance Sheet. Depicts amortization of existing guaranteed portfolio, assuming no advance refunding as of June 30, 2012. Actual future installments may differ from estimated because borrowers may have the right to call or terminate a transaction or the guaranteed obligation may be subject to prepayment. The unearned premium amortization disclosed in the above table consider the use of contractual lives for many bond types that do not have homogeneous pools of underlying collateral, which results in a higher unearned premium than if expected lives were considered. If those bond types are retired early as a result of rate step-ups or other early retirement provision incentives for the issuer, premium earnings may be negative in the period of call or refinancing.
- 4) Represents management's estimate of future installment premium collections net of reinsurance. Actual premium collections may differ from estimated because borrowers may have the right to call or terminate a transaction or the guaranteed obligation may be subject to prepayment. Estimated net future installments excludes amounts eliminated as a result of the Consolidations Accounting Standard (\$301.9 million). Please see discussion in Ambac's June 30, 2012 Form 10-Q.

Fixed Income Investment Portfolio

As of June 30, 2012

| INCOME ANALYSIS BY TYPE OF SECURITY | Fair Value | Amortized Cost | Pre-tax Yield to Maturity ⁽¹⁾ | YTD GAAP Investment Income |
|--|-------------|----------------|--|----------------------------|
| Investment category (\$ thousands) | | | | |
| Financial Guarantee investments: | | | | |
| Long-term investments | | | | |
| U.S. government obligations | 375,067 | 373,293 | 0.70% | 1,864 |
| U.S. agency obligations | 80,485 | 76,187 | 4.21% | 1,625 |
| Municipal obligations ⁽²⁾ | 1,935,583 | 1,768,713 | 5.15% | 46,770 |
| Foreign obligations | 68,842 | 65,089 | 3.75% | 1,459 |
| Corporate obligations | 1,039,028 | 972,419 | 4.57% | 21,700 |
| Mortgage and asset-backed securities | 1,626,594 | 1,416,946 | 13.57% | 123,090 |
| Total long-term investments | 5,125,599 | 4,672,647 | 7.19% | 196,508 |
| Short-term investments | 940,865 | 940,676 | 0.17% | 707 |
| Other ⁽³⁾ | 100 | 100 | | 338 |
| Total Financial Guarantee investments | 6,066,564 | 5,613,423 | 6.02% | 197,553 |
| Investment expenses | | | | (2,344) |
| Financial Guarantee net investment income | | | | 195,209 |
| Financial Services investments: ⁽⁴⁾ | | | | |
| Long-term investments | | | | |
| U.S. government obligations | 22,160 | 21,983 | | 178 |
| U.S. agency obligations | 4,215 | 3,866 | | 126 |
| Corporate obligations | 63,667 | 67,591 | | 461 |
| Mortgage and asset-backed securities | 461,309 | 465,949 | | 9,846 |
| Total long-term investments | 551,351 | 559,389 | | 10,611 |
| Short-term investments | 35,788 | 35,786 | | 19 |
| Total Financial Services investments | 587,139 | 595,175 | | 10,630 |
| Corporate investments: | | | | |
| Short-term investments | 33,406 | 33,406 | | 114 |
| Total Corporate investments | 33,406 | 33,406 | | 114 |
| Total Investments | \$6,687,109 | \$6,242,004 | | 205,953 |

RATING DISTRIBUTION OF INVESTMENT PORTFOLIO ⁽⁵⁾⁽⁶⁾

| Rating | Percent of Investment Portfolio | | |
|--|---------------------------------|---------------|-------------|
| | Fin. Guar. | Fin. Services | Combined |
| AAA | 29% | 59% | 32% |
| AA | 30 | 18 | 28 |
| A | 13 | 1 | 12 |
| BBB | 9 | 6 | 9 |
| Below investment grade ⁽⁷⁾ | 14 | 16 | 14 |
| Not rated | 5 | - | 5 |
| | <u>100%</u> | <u>100%</u> | <u>100%</u> |
| Duration of Financial Guarantee investment portfolio | | | 3.9 |

- 1) "Yield to maturity" refers to the rate of interest to be earned over the expected remaining life of the investments in the portfolio, and is calculated based on amortized cost, estimated future cash flows and call schedules. Actual maturities may differ from stated maturities because borrowers may have the right to call or prepay obligations. For floating rate positions "yield to maturity" is based on the current interest rate and not forward rates.
- 2) Includes taxable and tax-exempt municipal obligations with a fair value of \$545,110 and \$1,390,473 respectively.
- 3) Includes income earned on loans, which are classified separately on the balance sheet.
- 4) Financial Services investments relate primarily to the investment agreement business.
- 5) Ratings are based on the lower of Standard & Poor's or Moody's rating. If guaranteed, rating represents the higher of the underlying or wrapped rating.
- 6) Rating distribution is calculated based on amortized cost.
- 7) Includes Ambac Assurance insured RMBS bonds purchased as part of our loss remediation strategy.

Expense Analysis (GAAP)

2012

| (\$ Thousands) | First Quarter | Second Quarter | Third Quarter | Fourth Quarter | Full Year |
|---|------------------|-------------------|------------------|-------------------|------------------|
| Financial Guarantee operating expenses: | | | | | |
| Compensation | \$ 13,824 | \$ 13,441 | | | \$ 27,265 |
| Non-compensation | 11,554 | 13,271 | | | 24,825 |
| Total Financial Guarantee operating expenses | 25,378 | 26,712 | - | - | 52,090 |
| Financial Services operating expenses | 792 | 923 | | | 1,715 |
| Corporate and other operating expenses | 1,930 | (593) | | | 1,337 |
| Total gross operating expenses | \$ 28,100 | \$ 27,042 | \$ - | \$ - | \$ 55,142 |
| Ceding commissions and change in deferred acquisition costs . . . | 8,434 | 6,525 | | | 14,959 |
| Total operating expenses, net of deferred expenses. | \$ 36,534 | \$ 33,567 | \$ - | \$ - | \$ 70,101 |
| Reorganization costs | \$ 2,461 | \$ 767 | | | \$ 3,228 |
| Total gross operating expenses, including reorganization costs . . . | \$ 30,561 | \$ 27,809 | \$ - | \$ - | \$ 58,370 |

2011

| (\$ Thousands) | First Quarter | Second Quarter | Third Quarter | Fourth Quarter | Full Year |
|---|------------------|-------------------|------------------|-------------------|-------------------|
| Financial Guarantee operating expenses: | | | | | |
| Compensation | \$ 16,612 | \$ (805) | \$ 14,276 | \$ 13,845 | \$ 43,929 |
| Non-compensation | 16,644 | 941 | 15,621 | 15,369 | 48,575 |
| Total Financial Guarantee operating expenses | 33,256 | 136 | 29,897 | 29,214 | 92,503 |
| Financial Services operating expenses | 2,614 | 2,707 | 2,719 | 2,401 | 10,441 |
| Corporate and other operating expenses | 477 | 990 | 1,801 | 1,755 | 5,023 |
| Total gross operating expenses | \$ 36,347 | \$ 3,833 | \$ 34,417 | \$ 33,370 | \$ 107,967 |
| Ceding commissions and change in deferred acquisition costs . . . | 9,120 | 11,700 | 10,443 | 2,075 | 33,338 |
| Total operating expenses, net of deferred expenses. | \$ 45,466 | \$ 15,533 | \$ 44,860 | \$ 35,445 | \$ 141,304 |
| Reorganization costs | \$ 24,805 | \$ 6,470 | \$ 8,519 | \$ 10,067 | \$ 49,861 |
| Total gross operating expenses, including reorganization costs . . . | \$ 61,151 | \$ 10,303 | \$ 42,936 | \$ 43,437 | \$ 157,827 |

Historical Financial Guarantee Exposures Outstanding ⁽¹⁾

| (\$ Millions Net Par Value) | June 30, | December 31, | | | Segregated Account June 30, 2012 |
|---|-----------|--------------|-----------|-----------|-------------------------------------|
| | 2012 | 2011 | 2010 | 2009 | |
| Public Finance: | | | | | |
| Lease and tax backed | \$56,390 | \$59,864 | \$65,843 | \$73,081 | \$9 |
| General obligation | 39,041 | 42,959 | 48,241 | 54,047 | 11 |
| Utility | 20,562 | 22,529 | 26,360 | 30,835 | 415 |
| Transportation | 17,651 | 18,945 | 20,722 | 22,501 | 328 |
| Higher education | 11,962 | 13,618 | 15,279 | 16,577 | - |
| Housing | 8,456 | 8,823 | 9,878 | 10,247 | - |
| Health care | 6,698 | 7,824 | 9,603 | 11,987 | 86 |
| Other | 1,834 | 2,255 | 3,423 | 3,892 | - |
| Total Public Finance | 162,594 | 176,817 | 199,349 | 223,167 | 849 |
| Structured Finance: | | | | | |
| Mortgage-backed & home equity | 21,181 | 23,164 | 27,488 | 32,407 | 21,181 |
| Investor-owned utilities | 8,334 | 9,049 | 10,685 | 13,212 | 385 |
| Student loan | 7,354 | 7,824 | 11,408 | 14,518 | 7,244 |
| Other CDOs | 7,292 | 8,060 | 11,463 | 18,313 | 578 |
| Asset-backed and conduits | 3,624 | 4,732 | 10,005 | 16,455 | - |
| CDO of ABS >25% MBS | - | - | - | 16,718 | - |
| Other | 1,926 | 2,316 | 2,750 | 3,092 | 327 |
| Total Structured Finance | 49,711 | 55,145 | 73,799 | 114,715 | 29,715 |
| International Finance ⁽²⁾: | | | | | |
| Investor-owned and public utilities | 9,997 | 10,510 | 10,861 | 10,388 | - |
| Asset-backed and conduits | 9,281 | 9,560 | 10,738 | 13,691 | 18 |
| Sovereign/sub-sovereign | 7,301 | 7,282 | 7,119 | 6,859 | - |
| Transportation | 5,810 | 5,914 | 6,744 | 7,584 | 256 |
| Other CDOs | 3,714 | 4,375 | 6,775 | 9,083 | 1,048 |
| Mortgage-backed & home equity | 1,308 | 1,397 | 1,898 | 3,386 | 271 |
| Other | 1,446 | 1,504 | 1,571 | 1,533 | - |
| Total International Finance | 38,857 | 40,542 | 45,706 | 52,524 | 1,593 |
| Grand Total | \$251,162 | \$272,504 | \$318,854 | \$390,406 | \$32,157 |
| Percent of Total Net Par Outstanding | | | | | |
| Public Finance | 64.7% | 64.9% | 62.5% | 57.2% | 2.6% |
| Structured Finance | 19.8% | 20.2% | 23.2% | 29.4% | 92.4% |
| International Finance | 15.5% | 14.9% | 14.3% | 13.4% | 5.0% |
| Total Net Par Outstanding | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |

(1) Included in the above exposures are structured credit derivatives. Total structured credit derivative net par outstanding amounted to \$12,884, \$14,167, \$18,766, and \$43,276 at June 30, 2012 and December 31, 2011, 2010, and 2009, respectively.

(2) International transactions include components of domestic exposure.

Geographic Distribution of Financial Guarantee Exposures Outstanding

| (\$ Millions Net Par Value) | June 30, | | December 31, | | | |
|---------------------------------------|-----------|--------|--------------|-----------|-----------|-----------|
| | 2012 | % | 2011 | 2010 | 2009 | 2008 |
| Domestic: | | | | | | |
| California | \$34,361 | 13.7% | \$36,133 | \$39,210 | \$43,388 | \$45,343 |
| New York | 17,305 | 6.9% | 18,267 | 20,944 | 22,865 | 25,972 |
| Florida | 12,875 | 5.1% | 13,906 | 15,910 | 17,816 | 18,724 |
| Texas | 11,713 | 4.7% | 12,983 | 14,776 | 16,941 | 17,674 |
| New Jersey | 9,083 | 3.6% | 9,650 | 10,415 | 11,654 | 12,204 |
| Illinois | 7,935 | 3.2% | 8,524 | 9,351 | 10,472 | 10,544 |
| Massachusetts | 5,524 | 2.2% | 5,799 | 6,576 | 8,255 | 8,184 |
| Pennsylvania | 4,813 | 1.9% | 5,301 | 6,036 | 7,405 | 10,879 |
| Colorado | 4,783 | 1.9% | 5,010 | 5,786 | 6,392 | 6,818 |
| Washington | 4,347 | 1.7% | 4,772 | 5,710 | 6,124 | 6,249 |
| Mortgage and asset-backed | 24,805 | 9.9% | 27,896 | 37,493 | 48,862 | 62,438 |
| Other states | 74,761 | 29.8% | 83,721 | 100,941 | 137,708 | 153,601 |
| Total Domestic | 212,305 | 84.5% | 231,962 | 273,148 | 337,882 | 378,630 |
| International: | | | | | | |
| United Kingdom | 22,090 | 8.8% | 22,317 | 22,215 | 22,840 | 20,151 |
| Australia | 4,916 | 2.0% | 5,176 | 6,292 | 6,034 | 4,952 |
| Italy | 3,242 | 1.3% | 3,346 | 3,674 | 3,821 | 2,843 |
| Austria | 924 | 0.4% | 956 | 999 | 1,149 | 905 |
| Germany | 591 | 0.2% | 619 | 692 | 765 | 812 |
| Internationally diversified | 4,594 | 1.8% | 5,318 | 7,793 | 9,914 | 14,937 |
| Other international | 2,500 | 1.0% | 2,810 | 4,041 | 8,001 | 11,080 |
| Total International | 38,857 | 15.5% | 40,542 | 45,706 | 52,524 | 55,680 |
| Grand Total | \$251,162 | 100.0% | \$272,504 | \$318,854 | \$390,406 | \$434,310 |

Rating Distribution of Net Financial Guarantee Exposures Outstanding ⁽¹⁾

As of June 30, 2012

| Rating | Percentage of Guaranteed Portfolio | | |
|---------------|------------------------------------|------------------------------|-------|
| | Public Finance | Structured and International | Total |
| AAA | <1 | 2 | 1 |
| AA | 30 | 9 | 23 |
| A | 55 | 24 | 44 |
| BBB | 13 | 26 | 17 |
| BIG | 2 | 39 | 15 |
| | 100 | 100 | 100 |

(1) Based upon internal Ambac ratings. See Note 1 on the Table of Contents page.

25 Largest Domestic Public Finance Exposures

| (\$ Millions) | Ambac Rating ⁽¹⁾ | AADS ⁽²⁾ | Net Par Outstanding | % of Total Net Par Outstanding |
|--|--------------------------------|---------------------|------------------------|--------------------------------------|
| California State - GO | A | \$197.9 | \$2,848 | 1.1% |
| New Jersey Transportation Trust Fund Authority - Transportation System | A + | \$165.7 | 2,058 | 0.8% |
| Bay Area Toll Authority, CA Toll Bridge Revenue ⁽³⁾ | AA - | \$82.9 | 1,581 | 0.6% |
| MTA, NY, Transportation Revenue (Farebox) ⁽³⁾ | A | \$91.7 | 1,432 | 0.6% |
| NYS Thruway Authority, Highway & Bridge Revenue | AA - | \$134.7 | 1,414 | 0.6% |
| Washington State - GO | AA | \$115.8 | 1,412 | 0.6% |
| Massachusetts School Building Authority, MA, Sales Tax Revenue | AA | \$96.0 | 1,248 | 0.5% |
| Massachusetts Commonwealth - GO | AA | \$88.1 | 1,218 | 0.5% |
| New Jersey Turnpike Authority Revenue | A | \$76.1 | 1,153 | 0.5% |
| Los Angeles Unified School District, CA - GO | AA - | \$80.5 | 1,000 | 0.4% |
| Central Texas Turnpike, System Revenue | BBB + | \$106.4 | 986 | 0.4% |
| Port Authority of New York & New Jersey, Consolidated Revenue | AA - | \$71.0 | 907 | 0.4% |
| Sales Tax Asset Receivable Corporation, NY, Revenue | A | \$76.0 | 846 | 0.3% |
| New York City, NY - GO | AA | \$46.7 | 838 | 0.3% |
| Golden State Tobacco Securitization Corp., CA, Enhanced Tobacco Settlement | A | \$53.5 | 833 | 0.3% |
| Puerto Rico Sales Tax Financing Corporation | A + | \$173.9 | 805 | 0.3% |
| New Jersey Economic Development Authority - School Facilities Construction | A + | \$51.1 | 802 | 0.3% |
| New York City, NY Water and Sewer System Revenue | AA - | \$53.1 | 797 | 0.3% |
| South Carolina Transportation Infrastructure Bank Revenue | A | \$56.1 | 785 | 0.3% |
| Puerto Rico Highways & Transportation Authority, Transportation Revenue ⁽³⁾ | BBB + | \$47.7 | 770 | 0.3% |
| Chicago, IL - GO | A + | \$36.6 | 742 | 0.3% |
| University of California Board of Regents, General Revenue | AA - | \$43.2 | 713 | 0.3% |
| New York Convention Center Development Corporation, Hotel Fee Revenue | A - | \$43.6 | 651 | 0.3% |
| Dallas Area Rapid Transit, TX, Sales Tax Revenue | AA | \$47.3 | 643 | 0.3% |
| Missouri Joint Municipal Electric Utility Commission, Project Revenue | A - | \$40.4 | 636 | 0.3% |
| Total: | | | <u>\$27,118</u> | <u>10.8%</u> |

1) See Note 1 on the Table of Contents page.

2) Average Annual Debt Service, net of reinsurance.

3) On March 24, 2010, Ambac Assurance established a Segregated Account. The purpose of the Segregated Account is to segregate certain segments of Ambac Assurance's liabilities, and in connection with such segregation Ambac Assurance has allocated all or a portion of this transaction to the Segregated Account.

25 Largest Structured Finance Exposures

| (\$ Millions) | Ambac Rating ⁽¹⁾ | Net Par Outstanding | % of Total Net Par Outstanding |
|--|-----------------------------|---------------------|--------------------------------|
| CDO of ABS < 25% MBS | A | \$1,470 | 0.6% |
| Vermont Student Assistance Corporation Revenue Bonds ⁽²⁾ | BIG | 1,264 | 0.5% |
| Wachovia Asset Securitization Issuance II, LLC 2007-HE2 ⁽²⁾ | BIG | 1,263 | 0.5% |
| Ballantyne Re Plc ⁽³⁾ | BIG | 900 | 0.4% |
| Wachovia Asset Securitization Issuance II, LLC 2007-HE1 ⁽²⁾ | BIG | 867 | 0.3% |
| The National Collegiate Student Loan Trust 2007-4 ⁽²⁾ | BIG | 856 | 0.3% |
| Spirit Master Funding | BBB | 770 | 0.3% |
| Michigan Higher Education Student Loan Authority ⁽²⁾ | BIG | 718 | 0.3% |
| Timberlake Financial, LLC | BIG | 620 | 0.2% |
| The National Collegiate Student Loan Trust 2007-3 ⁽²⁾ | BIG | 570 | 0.2% |
| Progress Energy Carolinas, INC | A - | 558 | 0.2% |
| Countrywide Asset-Backed Certificates Trust 2005-16 ⁽²⁾ | BIG | 523 | 0.2% |
| Countrywide Revolving Home Equity Loan Trust 2005-F ⁽²⁾ | BIG | 514 | 0.2% |
| Ares XI CLO, Ltd. | AA + | 508 | 0.2% |
| Option One Mortgage Loan Trust 2007-FXD1 ⁽²⁾ | BIG | 506 | 0.2% |
| Local Insight Media Finance LLC | BIG | 489 | 0.2% |
| Massachusetts Educational Financing Authority Revenue Bonds ⁽²⁾ | BIG | 488 | 0.2% |
| Morgan Stanley Credit Corporation Heloc Trust 2007-1 ⁽²⁾ | BIG | 486 | 0.2% |
| Privately Placed RMBS Transaction ⁽²⁾ | BIG | 461 | 0.2% |
| Niagara Mohawk Power Corporation | A | 444 | 0.2% |
| Countrywide Asset Backed Certificates Trust 2005-17 ⁽²⁾ | BIG | 434 | 0.2% |
| Impac CMB Trust Series 2005-7 ⁽²⁾ | BIG | 429 | 0.2% |
| Countrywide Asset Backed Certificates Trust 2006-11 ⁽²⁾ | BIG | 420 | 0.2% |
| Fairway Loan Funding Company | AA + | 405 | 0.2% |
| Kinney Hill Credit Opportunities Funds | A | 385 | 0.2% |
| Total: | | <u>\$16,348</u> | <u>6.5%</u> |

25 Largest International Finance Exposures

| (\$ Millions) | Ambac Rating ⁽¹⁾ | Net Par Outstanding | % of Total Net Par Outstanding |
|--|-----------------------------|---------------------|--------------------------------|
| Mitchells & Butlers Finance plc-UK Pub Securitization ⁽³⁾ | A + | \$2,023 | 0.8% |
| Romulus Finance s.r.l. ⁽³⁾ | BIG | 1,445 | 0.6% |
| Telereal Securitization plc ⁽³⁾ | A + | 1,406 | 0.6% |
| Punch Taverns Finance plc-UK Pub Securitization ⁽³⁾ | BIG | 1,210 | 0.5% |
| National Grid Electricity Transmission ⁽³⁾ | A - | 1,151 | 0.5% |
| Aspire Defence Finance plc ⁽³⁾ | BBB + | 1,147 | 0.5% |
| Channel Link Enterprises ⁽³⁾ | BBB - | 1,120 | 0.4% |
| Regione Campania ⁽³⁾ | BBB + | 1,083 | 0.4% |
| Capital Hospitals plc ⁽³⁾ | BBB - | 967 | 0.4% |
| Ostregion Investmentgesellschaft NR 1 SA ⁽³⁾ | BIG | 912 | 0.4% |
| RMPA Services plc ⁽³⁾ | BBB + | 810 | 0.3% |
| Anglian Water ⁽³⁾ | A - | 805 | 0.3% |
| National Grid Gas ⁽³⁾ | A - | 747 | 0.3% |
| Powercor Australia | A - | 743 | 0.3% |
| CitiPower | A - | 711 | 0.3% |
| Scotia Gas Networks ⁽³⁾ | BBB | 703 | 0.3% |
| Dampier to Bunbury Natural Gas Pipeline | BBB | 699 | 0.3% |
| Spirit Issuer plc ⁽³⁾ | BIG | 698 | 0.3% |
| Private CMBS Transaction ⁽³⁾ | AAA | 695 | 0.3% |
| Catalyst Healthcare (Manchester) Financing plc ⁽³⁾ | BBB - | 661 | 0.3% |
| CDO of HY Corporate | AA | 657 | 0.3% |
| Babcock & Brown Air Funding I Limited | BBB + | 622 | 0.2% |
| Broadcast Australia | BBB | 589 | 0.2% |
| South East Water (Finance) Limited ⁽³⁾ | BBB | 574 | 0.2% |
| European Single-Borrower CMBS Transaction | AA | 504 | 0.2% |
| Total: | | <u>\$22,682</u> | <u>9.0%</u> |

1) See Note 1 on the Table of Contents page.

2) On March 24, 2010, Ambac Assurance established a Segregated Account. The purpose of the Segregated Account is to segregate certain segments of Ambac Assurance's liabilities, and in connection with such segregation Ambac Assurance has allocated all or a portion of this transaction to the Segregated Account.

3) All or a portion of transaction guaranteed by Ambac Assurance UK, Ltd.

Net Exposure Amortization ⁽¹⁾

As of June 30, 2012

| (\$ Millions) | Total, including Segregated Account | | Segregated Account | |
|-----------------------------------|---|--|---|--|
| | Estimated Net Debt Service Amortization | Ending Net Financial Guarantees in Force | Estimated Net Debt Service Amortization | Ending Net Financial Guarantees in Force |
| 2012 (3rd and 4th Qtrs) | \$12,830 | \$383,456 | \$2,120 | \$41,819 |
| 2013 | 23,839 | 359,617 | 3,219 | 38,600 |
| 2014 | 20,959 | 338,658 | 2,565 | 36,035 |
| 2015 | 22,586 | 316,072 | 2,236 | 33,799 |
| 2016 | 19,775 | 296,297 | 1,852 | 31,947 |
| 2017 | 19,578 | 276,719 | 1,663 | 30,284 |
| 2012 (3rd and 4th Qtrs) | \$12,830 | \$383,456 | \$2,120 | \$41,819 |
| 2013-2017 | 106,737 | 276,719 | 11,535 | 30,284 |
| 2018-2022 | 90,785 | 185,934 | 6,494 | 23,790 |
| 2023-2027 | 64,626 | 121,308 | 5,289 | 18,501 |
| 2028-2032 | 51,590 | 69,718 | 5,415 | 13,086 |
| After 2032 | 69,718 | - | 13,086 | - |
| Total | \$396,286 | | \$43,939 | |

(1) Depicts amortization of existing guaranteed portfolio (principal and interest), assuming no advance refundings, as of June 30, 2012. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay guaranteed obligations.