

CINCINNATI FINANCIAL CORP

Form 10-Q

July 26, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

(Mark one)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.

For the quarterly period ended June 30, 2016.

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.

For the transition period from _____ to _____.

Commission file number 0-4604

CINCINNATI FINANCIAL CORPORATION
(Exact name of registrant as specified in its charter)

Ohio 31-0746871
(State or other jurisdiction of (I.R.S. Employer Identification
incorporation or organization) No.)

6200 S. Gilmore Road, Fairfield, Ohio 45014-5141
(Address of principal executive offices) (Zip code)

Registrant's telephone number, including area code: (513) 870-2000

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a nonaccelerated filer or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Nonaccelerated filer Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act):

Yes No

As of July 22, 2016, there were 164,575,858 shares of common stock outstanding.

CINCINNATI FINANCIAL CORPORATION AND SUBSIDIARIES
FORM 10-Q FOR THE QUARTER ENDED JUNE 30, 2016

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Part I – Financial Information

Item 1. Financial Statements (unaudited)

Cincinnati Financial Corporation and Subsidiaries

Condensed Consolidated Balance Sheets

(Dollars in millions except per share data)

| | June 30, 2016 | December 31, 2015 |
|--|------------------|----------------------|
| Assets | | |
| Investments | | |
| Fixed maturities, at fair value (amortized cost: 2016—\$9,518; 2015—\$9,324) | \$10,138 | \$ 9,650 |
| Equity securities, at fair value (cost: 2016—\$3,189; 2015—\$2,938) | 5,242 | 4,706 |
| Other invested assets | 79 | 67 |
| Total investments | 15,459 | 14,423 |
| Cash and cash equivalents | 547 | 544 |
| Investment income receivable | 126 | 129 |
| Finance receivable | 58 | 62 |
| Premiums receivable | 1,529 | 1,431 |
| Reinsurance recoverable | 557 | 542 |
| Prepaid reinsurance premiums | 73 | 54 |
| Deferred policy acquisition costs | 624 | 616 |
| Land, building and equipment, net, for company use (accumulated depreciation: 2016—\$367; 2015—\$459) | 186 | 185 |
| Other assets | 195 | 154 |
| Separate accounts | 797 | 748 |
| Total assets | \$20,151 | \$ 18,888 |
| Liabilities | | |
| Insurance reserves | | |
| Loss and loss expense reserves | \$4,970 | \$ 4,718 |
| Life policy and investment contract reserves | 2,624 | 2,583 |
| Unearned premiums | 2,349 | 2,201 |
| Other liabilities | 743 | 717 |
| Deferred income tax | 844 | 638 |
| Note payable | 28 | 35 |
| Long-term debt and capital lease obligations | 825 | 821 |
| Separate accounts | 797 | 748 |
| Total liabilities | 13,180 | 12,461 |
| Commitments and contingent liabilities (Note 12) | — | — |
| Shareholders' Equity | | |
| Common stock, par value—\$2 per share; (authorized: 2016 and 2015—500 million shares; issued: 2016 and 2015—198.3 million shares) | 397 | 397 |
| Paid-in capital | 1,237 | 1,232 |
| Retained earnings | 4,915 | 4,762 |
| Accumulated other comprehensive income | 1,714 | 1,344 |
| Treasury stock at cost (2016— 33.8 million shares and 2015—34.4 million shares) | (1,292) | (1,308) |
| Total shareholders' equity | 6,971 | 6,427 |
| Total liabilities and shareholders' equity | \$20,151 | \$ 18,888 |

Accompanying Notes are an integral part of these Condensed Consolidated Financial Statements.

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Cincinnati Financial Corporation and Subsidiaries
Condensed Consolidated Statements of Income

| (Dollars in millions except per share data) | Three months | | Six months | |
|--|------------------------|---------|------------------------|---------|
| | ended June 30, 2016 | 2015 | ended June 30, 2016 | 2015 |
| Revenues | | | | |
| Earned premiums | \$1,173 | \$1,111 | \$2,327 | \$2,205 |
| Investment income, net of expenses | 149 | 140 | 294 | 279 |
| Realized investment gains, net | 44 | 60 | 105 | 107 |
| Fee revenues | 3 | 3 | 6 | 6 |
| Other revenues | 2 | 2 | 3 | 4 |
| Total revenues | 1,371 | 1,316 | 2,735 | 2,601 |
| Benefits and Expenses | | | | |
| Insurance losses and contract holders' benefits | 821 | 712 | 1,545 | 1,461 |
| Underwriting, acquisition and insurance expenses | 366 | 340 | 726 | 685 |
| Interest expense | 13 | 13 | 26 | 26 |
| Other operating expenses | 5 | 3 | 7 | 7 |
| Total benefits and expenses | 1,205 | 1,068 | 2,304 | 2,179 |
| Income Before Income Taxes | 166 | 248 | 431 | 422 |
| Provision (Benefit) for Income Taxes | | | | |
| Current | 48 | 70 | 113 | 116 |
| Deferred | (5 |) 2 | 7 | 2 |
| Total provision for income taxes | 43 | 72 | 120 | 118 |
| Net Income | \$123 | \$176 | \$311 | \$304 |
| Per Common Share | | | | |
| Net income—basic | \$0.75 | \$1.07 | \$1.89 | \$1.85 |
| Net income—diluted | 0.74 | 1.06 | 1.87 | 1.84 |

Accompanying Notes are an integral part of these Condensed Consolidated Financial Statements.

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Cincinnati Financial Corporation and Subsidiaries
Condensed Consolidated Statements of Comprehensive Income

| (Dollars in millions) | Three months ended June 30, | | Six months ended June 30, | |
|--|-----------------------------------|---------|---------------------------------|--------|
| | 2016 | 2015 | 2016 | 2015 |
| Net Income | \$123 | \$176 | \$311 | \$304 |
| Other Comprehensive (Loss) Income | | | | |
| Change in unrealized gains on investments, net of tax of \$103, \$(112), \$203 and \$(127), respectively | 186 | (207) | 376 | (235) |
| Amortization of pension actuarial loss and prior service cost, net of tax of \$0, \$1, \$1 and \$1, respectively | 1 | 1 | 1 | 2 |
| Change in life deferred acquisition costs, life policy reserves and other, net of tax of \$(3), \$2, \$(4) and \$1, respectively | (4) | 4 | (7) | 3 |
| Other comprehensive income (loss), net of tax | 183 | (202) | 370 | (230) |
| Comprehensive Income (Loss) | \$306 | \$(26) | \$681 | \$74 |

Accompanying Notes are an integral part of these Condensed Consolidated Financial Statements.

Cincinnati Financial Corporation and Subsidiaries

Condensed Consolidated Statements of Shareholders' Equity

| (Dollars in millions) | Six months ended June 30, | |
|--|------------------------------|----------------|
| | 2016 | 2015 |
| Common Stock | | |
| Beginning of year | \$397 | \$397 |
| Share-based awards | — | — |
| End of period | 397 | 397 |
| Paid-In Capital | | |
| Beginning of year | 1,232 | 1,214 |
| Share-based awards | (10) | (11) |
| Share-based compensation | 13 | 11 |
| Other | 2 | 2 |
| End of period | 1,237 | 1,216 |
| Retained Earnings | | |
| Beginning of year | 4,762 | 4,505 |
| Net income | 311 | 304 |
| Dividends declared | (158) | (151) |
| End of period | 4,915 | 4,658 |
| Accumulated Other Comprehensive Income | | |
| Beginning of year | 1,344 | 1,744 |
| Other comprehensive income, net | 370 | (230) |
| End of period | 1,714 | 1,514 |
| Treasury Stock | | |
| Beginning of year | (1,308) | (1,287) |
| Share-based awards | 23 | 23 |
| Shares acquired - share repurchase authorization | (2) | (20) |
| Shares acquired - share-based compensation plans | (7) | (6) |
| Other | 2 | 2 |
| End of period | (1,292) | (1,288) |
| Total Shareholders' Equity | \$6,971 | \$6,497 |

(In millions)

Common Stock - Shares Outstanding

| | | |
|--|--------|--------|
| Beginning of year | 163.9 | 163.7 |
| Share-based awards | 0.7 | 0.8 |
| Shares acquired - share repurchase authorization | — | (0.4) |
| Shares acquired - share-based compensation plans | (0.1) | (0.1) |
| Other | — | — |
| End of period | 164.5 | 164.0 |

Accompanying Notes are an integral part of these Condensed Consolidated Financial Statements.

Cincinnati Financial Corporation and Subsidiaries
Condensed Consolidated Statements of Cash Flows

| (Dollars in millions) | Six months ended June 30, | |
|---|---------------------------------|----------|
| | 2016 | 2015 |
| Cash Flows From Operating Activities | | |
| Net income | \$311 | \$304 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 24 | 27 |
| Realized investment gains, net | (105) | (107) |
| Stock-based compensation | 13 | 11 |
| Interest credited to contract holders' | 25 | 22 |
| Deferred income tax expense | 7 | 2 |
| Changes in: | | |
| Investment income receivable | 3 | 1 |
| Premiums and reinsurance receivable | (132) | (93) |
| Deferred policy acquisition costs | (26) | (15) |
| Other assets | (39) | (6) |
| Loss and loss expense reserves | 252 | 206 |
| Life policy reserves | 50 | 47 |
| Unearned premiums | 148 | 109 |
| Other liabilities | (42) | (68) |
| Current income tax receivable/payable | 1 | 30 |
| Net cash provided by operating activities | 490 | 470 |
| Cash Flows From Investing Activities | | |
| Sale of fixed maturities | 15 | 19 |
| Call or maturity of fixed maturities | 820 | 675 |
| Sale of equity securities | 208 | 221 |
| Purchase of fixed maturities | (975) | (1,005) |
| Purchase of equity securities | (360) | (229) |
| Purchase of short-term investments | — | (75) |
| Investment in finance receivables | (10) | (6) |
| Collection of finance receivables | 15 | 15 |
| Investment in buildings and equipment, net | (7) | (5) |
| Change in other invested assets, net | (13) | 1 |
| Net cash used in investing activities | (307) | (389) |
| Cash Flows From Financing Activities | | |
| Payment of cash dividends to shareholders | (151) | (145) |
| Shares acquired - share repurchase authorization | (2) | (20) |
| Payments of note payable | (7) | — |
| Proceeds from stock options exercised | 13 | 11 |
| Contract holders' funds deposited | 50 | 41 |
| Contract holders' funds withdrawn | (77) | (67) |
| Excess tax benefits on stock-based compensation | 2 | 4 |
| Other | (8) | (9) |
| Net cash used in financing activities | (180) | (185) |
| Net change in cash and cash equivalents | 3 | (104) |
| Cash and cash equivalents at beginning of year | 544 | 591 |

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| | | |
|--|-------|-------|
| Cash and cash equivalents at end of period | \$547 | \$487 |
| Supplemental Disclosures of Cash Flow Information: | | |
| Interest paid | \$26 | \$26 |
| Income taxes paid | 110 | 83 |
| Noncash Activities | | |
| Conversion of securities | \$3 | \$— |
| Equipment acquired under capital lease obligations | 12 | 6 |
| Cashless exercise of stock options | 7 | 6 |

Accompanying Notes are an integral part of these Condensed Consolidated Financial Statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 1 — Accounting Policies

The condensed consolidated financial statements include the accounts of Cincinnati Financial Corporation and its consolidated subsidiaries, each of which is wholly owned. These statements are presented in conformity with accounting principles generally accepted in the United States of America (GAAP). All intercompany balances and transactions have been eliminated in consolidation.

The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Our actual results could differ from those estimates. Our December 31, 2015, condensed consolidated balance sheet amounts are derived from the audited financial statements but do not include all disclosures required by GAAP.

Our June 30, 2016, condensed consolidated financial statements are unaudited. Certain financial information that is included in annual financial statements prepared in accordance with GAAP is not required for interim reporting and has been condensed or omitted. We believe that we have made all adjustments, consisting only of normal recurring accruals, that are necessary for fair presentation. These condensed consolidated financial statements should be read in conjunction with our consolidated financial statements included in our 2015 Annual Report on Form 10-K. The results of operations for interim periods do not necessarily indicate results to be expected for the full year.

Adopted Accounting Updates

ASU 2014-12, Compensation-Stock Compensation: Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period
In June 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-12, Compensation-Stock Compensation: Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period. ASU 2014-12 requires that performance targets that affect vesting and that could be achieved after the requisite service period be treated as performance conditions. The effective date of ASU 2014-12 was for interim and annual reporting periods beginning after December 15, 2015. The company adopted this ASU and it did not have a material impact on our company's financial position, cash flows or results of operations.

ASU 2015-02, Consolidation-Amendments to the Consolidation Analysis

In February 2015, the FASB issued ASU 2015-02, Consolidation-Amendments to the Consolidation Analysis. ASU 2015-02 makes amendments to the current consolidation guidance, focusing mainly on the investment management industry; however, entities across all industries may be impacted. The effective date of ASU 2015-02 was for interim and annual reporting periods beginning after December 15, 2015. The company adopted this ASU and it did not have a material impact on our company's financial position, cash flows or results of operations.

Pending Accounting Updates

ASU 2014-09 Revenue from Contracts with Customers

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. ASU 2014-09 requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. Insurance contracts do not fall within the scope of this ASU. The effective date of ASU 2014-09 is for annual reporting periods beginning after December 15, 2017. The ASU has not yet been adopted; however, it is not expected to have a material impact on our company's financial position, cash flows or results of operations.

ASU 2015-09, Financial Services-Insurance: Disclosures about Short-Duration Contracts

In May 2015, the FASB issued ASU 2015-09, Financial Services-Insurance: Disclosures About Short-Duration Contracts. ASU 2015-09 requires entities to provide additional disclosures about the liability for loss and loss expense reserves to increase the transparency of significant estimates. ASU 2015-09 also requires entities to disclose information about significant changes in methodologies and assumptions used to calculate the liability for loss and loss expense reserves, including reasons for the change and the effects on the financial statements. ASU 2015-09 also requires entities to disclose a rollforward of the liability of loss and loss expense reserves for annual and interim reporting periods. The effective date of ASU 2015-09 is for annual reporting periods beginning

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after December 15, 2015, and interim reporting periods beginning after December 15, 2016. The ASU has not yet been adopted and will not have a material impact on our company's financial position, cash flows or results of operations, but the ASU will require additional disclosures to our annual and interim reporting periods.

ASU 2016-01, Financial Instruments - Overall (Subtopic 825-10) - Recognition and Measurement of Financial Assets and Financial Liabilities

In January 2016, the FASB issued ASU 2016-01, Financial Instruments - Overall (Subtopic 825-10) - Recognition and Measurement of Financial Assets and Financial Liabilities. ASU 2016-01 revises the accounting related to the classification and measurement of investments in equity securities and the presentation of certain fair value changes for financial liabilities measured at fair value. The effective date of ASU 2016-01 is for interim and annual reporting periods beginning after December 15, 2017. The ASU has not yet been adopted. Management is currently evaluating the impact on our company's consolidated financial position, cash flows and results of operations.

ASU 2016-02, Leases (Topic 842)

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842). The main provision of ASU 2016-02 requires the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under previous GAAP. The effective date of ASU 2016-02 is for interim and annual reporting periods beginning after December 15, 2018. The ASU has not yet been adopted. Management is currently evaluating the impact on our company's consolidated financial position, cash flows and results of operations.

ASU 2016-07, Investments - Equity Method and Joint Ventures (Topic 323): Simplifying the Transition to the Equity Method of Accounting

In March 2016, the FASB issued ASU 2016-07, Equity Method and Joint Ventures (Topic 323): Simplifying the Transition to the Equity Method of Accounting. ASU 2016-07 eliminates the requirement to retroactively adjust an investment, results of operations, and retained earnings once an investment qualifies for use of the equity method. It requires the equity method investor to add the cost of acquiring the additional interest in the investee to the current basis of the investor's previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting without retroactive adjustment. The effective date of ASU 2016-07 is for interim and annual reporting periods beginning after December 15, 2016. The ASU has not yet been adopted; however, it is not expected to have a material impact on our company's consolidated financial position, cash flows or results of operations.

ASU 2016-09, Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting

In March 2016, the FASB issued ASU 2016-09, Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting. ASU 2016-09 simplifies and improves several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The effective date of ASU 2016-09 is for interim and annual reporting periods beginning after December 15, 2016. The ASU has not yet been adopted; however, it is not expected to have a material impact on our company's consolidated financial position, cash flows or results of operations.

ASU 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments

In June 2016, the FASB issued ASU 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. ASU 2016-13 amends previous guidance on the impairment of financial instruments by adding an impairment model that allows an entity to recognize expected credit losses as an allowance rather than impairing as they are incurred. The new guidance is intended to reduce complexity of credit impairment models and result in a more timely recognition of expected credit losses. The effective date of ASU 2016-13 is for

interim and annual reporting periods beginning after December 15, 2019. The ASU has not yet been adopted; however, it is not expected to have a material impact on our company's consolidated financial position, cash flows or results of operations.

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NOTE 2 – Investments

The following table provides cost or amortized cost, gross unrealized gains, gross unrealized losses and fair value for our investment portfolio:

| (Dollars in millions) | Cost or amortized cost | Gross unrealized gains | losses | Fair value |
|---|------------------------------|---------------------------|--------|---------------|
| At June 30, 2016 | | | | |
| Fixed maturity securities: | | | | |
| Corporate | \$ 5,498 | \$ 366 | \$ 27 | \$5,837 |
| States, municipalities and political subdivisions | 3,538 | 264 | — | 3,802 |
| Commercial mortgage-backed | 293 | 17 | — | 310 |
| Government-sponsored enterprises | 170 | — | — | 170 |
| Foreign government | 10 | — | — | 10 |
| Convertibles and bonds with warrants attached | 5 | — | — | 5 |
| United States government | 4 | — | — | 4 |
| Subtotal | 9,518 | 647 | 27 | 10,138 |
| Equity securities: | | | | |
| Common equities | 3,002 | 2,080 | 65 | 5,017 |
| Nonredeemable preferred equities | 187 | 38 | — | 225 |
| Subtotal | 3,189 | 2,118 | 65 | 5,242 |
| Total | \$ 12,707 | \$ 2,765 | \$ 92 | \$15,380 |
| At December 31, 2015 | | | | |
| Fixed maturity securities: | | | | |
| Corporate | \$ 5,294 | \$ 255 | \$ 96 | \$5,453 |
| States, municipalities and political subdivisions | 3,440 | 172 | 1 | 3,611 |
| Commercial mortgage-backed | 287 | 4 | 2 | 289 |
| Government-sponsored enterprises | 284 | — | 6 | 278 |
| Foreign government | 10 | — | — | 10 |
| Convertibles and bonds with warrants attached | 5 | — | — | 5 |
| United States government | 4 | — | — | 4 |
| Subtotal | 9,324 | 431 | 105 | 9,650 |
| Equity securities: | | | | |
| Common equities | 2,749 | 1,787 | 51 | 4,485 |
| Nonredeemable preferred equities | 189 | 32 | — | 221 |
| Subtotal | 2,938 | 1,819 | 51 | 4,706 |
| Total | \$ 12,262 | \$ 2,250 | \$ 156 | \$14,356 |

The net unrealized investment gains in our fixed-maturity portfolio are primarily the result of the continued low interest rate environment that increased the fair value of our fixed-maturity portfolio. Our commercial mortgage-backed securities had an average rating of Aa1/AA at June 30, 2016, and December 31, 2015.

The seven largest unrealized investment gains in our common stock portfolio are from Exxon Mobil Corporation (NYSE:XOM), Honeywell International Incorporated (NYSE:HON), Johnson and Johnson (NYSE:JNJ), The Procter & Gamble Company (NYSE:PG), Hasbro Incorporated (Nasdaq:HAS), 3M Co (NYSE:MMM) and BlackRock Inc. (NYSE:BLK), which had a combined gross unrealized gain of \$647 million. At June 30, 2016, Johnson and Johnson was our largest single common stock holding with a fair value of \$153 million, which was 3.0 percent of our publicly traded common stock portfolio and 1.0 percent of the total investment portfolio.

The table below provides fair values and gross unrealized losses by investment category and by the duration of the securities' continuous unrealized loss positions:

| (Dollars in millions) | Less than 12 months | | 12 months or more | | Total | |
|---|---------------------|-------------------|-------------------|-------------------|------------|-------------------|
| | Fair value | Unrealized losses | Fair value | Unrealized losses | Fair value | Unrealized losses |
| At June 30, 2016 | | | | | | |
| Fixed maturity securities: | | | | | | |
| Corporate | \$ 252 | \$ 9 | \$ 258 | \$ 18 | \$510 | \$ 27 |
| States, municipalities and political subdivisions | 2 | — | 1 | — | 3 | — |
| Commercial mortgage-backed | 5 | — | 9 | — | 14 | — |
| Government-sponsored enterprises | 20 | — | — | — | 20 | — |
| Subtotal | 279 | 9 | 268 | 18 | 547 | 27 |
| Equity securities: | | | | | | |
| Common equities | 546 | 65 | — | — | 546 | 65 |
| Nonredeemable preferred equities | 19 | — | 18 | — | 37 | — |
| Subtotal | 565 | 65 | 18 | — | 583 | 65 |
| Total | \$ 844 | \$ 74 | \$ 286 | \$ 18 | \$1,130 | \$ 92 |
| At December 31, 2015 | | | | | | |
| Fixed maturity securities: | | | | | | |
| Corporate | \$ 1,099 | \$ 63 | \$ 133 | \$ 33 | \$1,232 | \$ 96 |
| States, municipalities and political subdivisions | 47 | 1 | 22 | — | 69 | 1 |
| Commercial mortgage-backed | 103 | 2 | 2 | — | 105 | 2 |
| Government-sponsored enterprises | 100 | 2 | 127 | 4 | 227 | 6 |
| Subtotal | 1,349 | 68 | 284 | 37 | 1,633 | 105 |
| Equity securities: | | | | | | |
| Common equities | 270 | 51 | — | — | 270 | 51 |
| Nonredeemable preferred equities | 35 | — | — | — | 35 | — |
| Subtotal | 305 | 51 | — | — | 305 | 51 |
| Total | \$ 1,654 | \$ 119 | \$ 284 | \$ 37 | \$1,938 | \$ 156 |

Contractual maturity dates for fixed-maturity investments were:

| (Dollars in millions) | Amortized cost | Fair value | % of fair value |
|--|----------------|------------|-----------------|
| At June 30, 2016 | | | |
| Maturity dates: | | | |
| Due in one year or less | \$ 446 | \$454 | 4.5 % |
| Due after one year through five years | 3,046 | 3,273 | 32.3 |
| Due after five years through ten years | 3,708 | 3,896 | 38.4 |
| Due after ten years | 2,318 | 2,515 | 24.8 |
| Total | \$ 9,518 | \$10,138 | 100.0% |

Actual maturities may differ from contractual maturities when there is a right to call or prepay obligations with or without call or prepayment penalties.

The following table provides investment income, realized investment gains and losses, the change in unrealized investment gains and losses, and other items:

| (Dollars in millions) | Three months | | Six months | |
|---|---------------------------|---------|---------------------------|---------|
| | ended June 30, 2016 | 2015 | ended June 30, 2016 | 2015 |
| Investment income: | | | | |
| Interest | \$110 | \$106 | \$219 | \$211 |
| Dividends | 41 | 35 | 78 | 71 |
| Other | — | 1 | 1 | 1 |
| Total | 151 | 142 | 298 | 283 |
| Less investment expenses | 2 | 2 | 4 | 4 |
| Total | \$149 | \$140 | \$294 | \$279 |
| Realized investment gains and losses summary: | | | | |
| Fixed maturities: | | | | |
| Gross realized gains | \$4 | \$7 | \$7 | \$10 |
| Gross realized losses | — | — | (1) | — |
| Other-than-temporary impairments | — | (3) | (2) | (3) |
| Equity securities: | | | | |
| Gross realized gains | 38 | 56 | 100 | 100 |
| Gross realized losses | — | — | (1) | (1) |
| Other-than-temporary impairments | — | (1) | — | (1) |
| Other | 2 | 1 | 2 | 2 |
| Total | \$44 | \$60 | \$105 | \$107 |
| Change in unrealized investment gains and losses: | | | | |
| Fixed maturities | \$178 | \$(184) | \$294 | \$(138) |
| Equity securities | 111 | (135) | 285 | (224) |
| Less income taxes | (103) | 112 | (203) | 127 |
| Total | \$186 | \$(207) | \$376 | \$(235) |

During the three months ended June 30, 2016, there were no equity securities and two new fixed-maturity securities other-than-temporarily impaired. During the six months ended June 30, 2016, there were no equity securities and four fixed-maturity securities other-than-temporarily impaired. There were no credit losses on fixed-maturity securities for which a portion of other-than-temporary impairment (OTTI) has been recognized in other comprehensive income for the three and six months ended June 30, 2016 and 2015. At June 30, 2016, 53 fixed-maturity investments with a total unrealized loss of \$18 million had been in an unrealized loss position for 12 months or more. Of that total, no fixed-maturity investments had fair values below 70 percent of amortized cost. At June 30, 2016, two equity investments with a total unrealized loss of less than \$1 million had been in an unrealized loss position for 12 months or more. Of that total, no equity investments had fair values below 70 percent of amortized cost.

During 2015, we other-than-temporarily impaired 20 securities. At December 31, 2015, 69 fixed-maturity investments with a total unrealized loss of \$37 million had been in an unrealized loss position for 12 months or more. Of that total, five fixed-maturity investments had fair values below 70 percent of amortized cost. There were no equity security investments in an unrealized loss position for 12 months or more as of December 31, 2015.

NOTE 3 – Fair Value Measurements

In accordance with accounting guidance for fair value measurements and disclosures, we categorized our financial instruments, based on the priority of the observable and market-based data for the valuation technique used, into a three-level fair value hierarchy. The fair value hierarchy gives the highest priority to quoted prices with readily available independent data in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable market inputs (Level 3). When various inputs for measurement fall within different levels of the fair value hierarchy, the lowest observable input that has a significant impact on fair value measurement is used. Our valuation techniques have not changed from those used at December 31, 2015, and ultimately management determines fair value. See our 2015 Annual Report on Form 10-K, Item 8, Note 3, Fair Value Measurements, Page 133, for information on characteristics and valuation techniques used in determining fair value.

Fair Value Disclosures for Assets

The following tables illustrate the fair value hierarchy for those assets measured at fair value on a recurring basis at June 30, 2016, and December 31, 2015. We do not have any material liabilities carried at fair value. There were no transfers between Level 1 and Level 2.

(Dollars in millions)

| | Quoted prices in active markets for identical assets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) | Total |
|--|---|---|--|----------|
| At June 30, 2016 | | | | |
| Fixed maturities, available for sale: | | | | |
| Corporate | \$ — | \$ 5,785 | \$ 52 | \$5,837 |
| States, municipalities and political subdivisions | — | 3,802 | — | 3,802 |
| Commercial mortgage-backed | — | 310 | — | 310 |
| Government-sponsored enterprises | — | 170 | — | 170 |
| Foreign government | — | 10 | — | 10 |
| Convertibles and bonds with warrants attached | — | 5 | — | 5 |
| United States government | 4 | — | — | 4 |
| Subtotal | 4 | 10,082 | 52 | 10,138 |
| Common equities, available for sale | 5,017 | — | — | 5,017 |
| Nonredeemable preferred equities, available for sale | — | 225 | — | 225 |
| Separate accounts taxable fixed maturities | — | 754 | 1 | 755 |
| Top Hat savings plan mutual funds and common equity (included in Other assets) | 23 | — | — | 23 |
| Total | \$ 5,044 | \$ 11,061 | \$ 53 | \$16,158 |
| At December 31, 2015 | | | | |
| Fixed maturities, available for sale: | | | | |
| Corporate | \$ — | \$ 5,402 | \$ 51 | \$5,453 |
| States, municipalities and political subdivisions | — | 3,611 | — | 3,611 |
| Commercial mortgage-backed | — | 289 | — | 289 |
| Government-sponsored enterprises | — | 278 | — | 278 |
| Foreign government | — | 10 | — | 10 |
| Convertibles and bonds with warrants attached | — | 5 | — | 5 |
| United States government | 4 | — | — | 4 |
| Subtotal | 4 | 9,595 | 51 | 9,650 |
| Common equities, available for sale | 4,485 | — | — | 4,485 |
| Nonredeemable preferred equities, available for sale | — | 218 | 3 | 221 |
| Separate accounts taxable fixed maturities | — | 736 | 1 | 737 |
| Top Hat savings plan mutual funds and common | 21 | — | — | 21 |

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| | | | | |
|-----------------------------------|----------|-----------|-------|----------|
| equity (included in Other assets) | | | | |
| Total | \$ 4,510 | \$ 10,549 | \$ 55 | \$15,114 |

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Each financial instrument that was deemed to have significant unobservable inputs when determining valuation is identified in the following tables by security type with a summary of changes in fair value as of June 30, 2016. Total Level 3 assets continue to be less than 1 percent of financial assets measured at fair value in the condensed consolidated balance sheets. Assets presented in the table below were valued based primarily on broker/dealer quotes for which there is a lack of transparency as to inputs used to develop the valuations. The quantitative detail of these unobservable inputs is neither provided nor reasonably available to us.

The following table provides the change in Level 3 assets for the three months ended June 30:

| (Dollars in millions) | Asset fair value measurements using significant unobservable inputs (Level 3) | | | | | Total |
|--|---|--|--|--|--|-------|
| | Corporate fixed maturities | accounts taxable fixed maturities | Separate States, municipalities and political subdivisions fixed maturities | Nonredeemable preferred equities | | |
| Beginning balance, April 1, 2016 | \$51 | \$ 1 | \$ — | \$ 2 | | \$54 |
| Total gains or losses (realized/unrealized): | | | | | | |
| Included in net income | — | — | — | — | | — |
| Included in other comprehensive income | — | — | — | — | | — |
| Purchases | 17 | — | — | — | | 17 |
| Sales | — | — | — | (2) | | (2) |
| Transfers into Level 3 | — | — | — | — | | — |
| Transfers out of Level 3 | (16) | — | — | — | | (16) |
| Ending balance, June 30, 2016 | \$52 | \$ 1 | \$ — | \$ — | | \$53 |
| Beginning balance, April 1, 2015 | \$18 | \$ — | \$ 1 | \$ 2 | | \$21 |
| Total gains or losses (realized/unrealized): | | | | | | |
| Included in net income | — | — | — | — | | — |
| Included in other comprehensive income | — | — | — | — | | — |
| Purchases | — | — | — | — | | — |
| Sales | — | — | — | — | | — |
| Transfers into Level 3 | — | — | — | — | | — |
| Transfers out of Level 3 | — | — | — | — | | — |
| Ending balance, June 30, 2015 | \$18 | \$ — | \$ 1 | \$ 2 | | \$21 |

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The following table provides the change in Level 3 assets for the six months ended June 30:

| (Dollars in millions) | Asset fair value measurements using significant unobservable inputs (Level 3) | | | | | Total |
|--|---|--|--|----------------------------------|--|-------|
| | Corporate fixed maturities | Separate accounts taxable fixed maturities | States, municipalities and political subdivisions fixed maturities | Nonredeemable preferred equities | | |
| Beginning balance, January 1, 2016 | \$ 51 | \$ 1 | \$ — | \$ 3 | | \$55 |
| Total gains or losses (realized/unrealized): | | | | | | |
| Included in net income | — | — | — | — | | — |
| Included in other comprehensive income | — | — | — | (1) | | (1) |
| Purchases | 22 | — | — | — | | 22 |
| Sales | — | — | — | (2) | | (2) |
| Transfers into Level 3 | — | — | — | — | | — |
| Transfers out of Level 3 | (21) | — | — | — | | (21) |
| Ending balance, June 30, 2016 | \$ 52 | \$ 1 | \$ — | \$ — | | \$53 |
| Beginning balance, January 1, 2015 | \$ 18 | \$ — | \$ — | \$ 2 | | \$20 |
| Total gains or losses (realized/unrealized): | | | | | | |
| Included in net income | — | — | — | — | | — |
| Included in other comprehensive income | — | — | — | — | | — |
| Purchases | — | — | — | — | | — |
| Sales | — | — | — | — | | — |
| Transfers into Level 3 | — | — | 1 | — | | 1 |
| Transfers out of Level 3 | — | — | — | — | | — |
| Ending balance, June 30, 2015 | \$ 18 | \$ — | \$ 1 | \$ 2 | | \$21 |

Additional disclosures for the Level 3 category are not material.

Fair Value Disclosures for Assets and Liabilities Not Carried at Fair Value

The disclosures below are presented to provide timely information about the effects of current market conditions on financial instruments that are not reported at fair value in our condensed consolidated financial statements.

This table summarizes the book value and principal amounts of our long-term debt:

| (Dollars in millions) | Book value | Principal amount | |
|-----------------------|-----------------------------|------------------|-------------------|
| | | June 30, 2016 | December 31, 2015 |
| Interest rate | | June 30, 2016 | December 31, 2015 |
| Year of issue | | 2016 | 2015 |
| 6.900% 1998 | Senior debentures, due 2028 | \$ 26 | \$ 26 |
| 6.920% 2005 | Senior debentures, due 2028 | 391 | 391 |
| 6.125% 2004 | Senior notes, due 2034 | 369 | 369 |
| | Total | \$786 | \$ 786 |
| | | \$ 793 | \$ 793 |

The following table shows fair values of our note payable and long-term debt:

| (Dollars in millions) | Quoted prices in active markets for identical assets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) | Total |
|------------------------------------|---|---|--|----------|
| At June 30, 2016 | | | | |
| Note payable | \$ | — \$ 28 | \$ | —\$28 |
| 6.900% senior debentures, due 2028 | — | 35 | — | 35 |
| 6.920% senior debentures, due 2028 | — | 516 | — | 516 |
| 6.125% senior notes, due 2034 | — | 457 | — | 457 |
| Total | \$ | — \$ 1,036 | \$ | —\$1,036 |

At December 31, 2015

| | | | | |
|------------------------------------|----|----------|----|--------|
| Note payable | \$ | — \$ 35 | \$ | —\$35 |
| 6.900% senior debentures, due 2028 | — | 31 | — | 31 |
| 6.920% senior debentures, due 2028 | — | 480 | — | 480 |
| 6.125% senior notes, due 2034 | — | 425 | — | 425 |
| Total | \$ | — \$ 971 | \$ | —\$971 |

The following table shows the fair value of our life policy loans included in other invested assets:

| (Dollars in millions) | Quoted prices in active markets for identical assets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) | Total |
|-----------------------|---|---|--|-------|
| At June 30, 2016 | | | | |
| Life policy loans | \$ | — \$ | — \$ 42 | \$ 42 |
| At December 31, 2015 | | | | |
| Life policy loans | \$ | — \$ | — \$ 40 | \$ 40 |

Outstanding principal and interest for these life policy loans totaled \$30 million and \$31 million at June 30, 2016, and December 31, 2015, respectively.

The following table shows fair values of our deferred annuities and structured settlements included in life policy and investment contract reserves:

| (Dollars in millions) | Quoted prices in active markets for identical assets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) | Total |
|------------------------|---|---|--|---------|
| At June 30, 2016 | | | | |
| Deferred annuities | \$ | — \$ | — | \$ 928 |
| Structured settlements | — | 220 | — | 220 |
| Total | \$ | — \$ 220 | \$ 928 | \$1,148 |
| At December 31, 2015 | | | | |
| Deferred annuities | \$ | — \$ | — | \$ 886 |
| Structured settlements | — | 208 | — | 208 |
| Total | \$ | — \$ 208 | \$ 886 | \$1,094 |

Recorded reserves for the deferred annuities were \$863 million and \$860 million at June 30, 2016, and December 31, 2015, respectively. Recorded reserves for the structured settlements were \$173 million and \$174 million at June 30, 2016, and December 31, 2015, respectively.

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NOTE 4 – Property Casualty Loss and Loss Expenses

This table summarizes activity for our consolidated property casualty loss and loss expense reserves:

| (Dollars in millions) | Three months | | Six months | |
|---|----------------|---------|----------------|---------|
| | ended June 30, | | ended June 30, | |
| | 2016 | 2015 | 2016 | 2015 |
| Gross loss and loss expense reserves, beginning of period | \$4,750 | \$4,577 | \$4,660 | \$4,438 |
| Less reinsurance recoverable | 272 | 278 | 281 | 282 |
| Net loss and loss expense reserves, beginning of period | 4,478 | 4,299 | 4,379 | 4,156 |
| Net incurred loss and loss expenses related to: | | | | |
| Current accident year | 808 | 724 | 1,531 | 1,435 |
| Prior accident years | (49) | (70) | (111) | (92) |
| Total incurred | 759 | 654 | 1,420 | 1,343 |
| Net paid loss and loss expenses related to: | | | | |
| Current accident year | 328 | 304 | 474 | 451 |
| Prior accident years | 301 | 294 | 717 | 693 |
| Total paid | 629 | 598 | 1,191 | 1,144 |
| Net loss and loss expense reserves, end of period | 4,608 | 4,355 | 4,608 | 4,355 |
| Plus reinsurance recoverable | 310 | 292 | 310 | 292 |
| Gross loss and loss expense reserves, end of period | \$4,918 | \$4,647 | \$4,918 | \$4,647 |

We use actuarial methods, models and judgment to estimate, as of a financial statement date, the property casualty loss and loss expense reserves required to pay for and settle all outstanding insured claims, including incurred but not reported (IBNR) claims, as of that date. The actuarial estimate is subject to review and adjustment by an inter-departmental committee that includes actuarial management that is familiar with relevant company and industry business, claims and underwriting trends, as well as general economic and legal trends that could affect future loss and loss expense payments. The amount we will actually have to pay for claims can be highly uncertain. This uncertainty, together with the size of our reserves, makes the loss and loss expense reserves our most significant estimate. The reserve for loss and loss expenses in the condensed consolidated balance sheets also included \$52 million at June 30, 2016, and \$44 million at June 30, 2015, for certain life and health loss and loss expense reserves.

For the three months ended June 30, 2016, we experienced \$49 million of favorable development on prior accident years, including \$58 million of favorable development in commercial lines, \$10 million of adverse development in personal lines and \$1 million of favorable development in excess and surplus lines. We recognized favorable reserve development during the three months ended June 30, 2016, of \$23 million for the workers' compensation line, \$20 million for the commercial casualty line, \$15 million for the other commercial lines and \$14 million for the commercial property line due to reduced uncertainty of prior accident year loss and loss adjustment expense for these lines. Our personal auto line developed unfavorably by \$14 million for the three months ended June 30, 2016, largely due to \$8 million of adverse development for accident year 2015. Our commercial auto line developed unfavorably by \$13 million for the three months ended June 30, 2016, due to higher loss cost effects in recent accident years, resulting in an increase of our reserve estimate for claims that have not yet been settled.

For the six months ended June 30, 2016, we experienced \$111 million of favorable development on prior accident years, including \$87 million of favorable development in commercial lines, \$8 million of favorable development in personal lines, \$15 million of favorable development in excess and surplus lines and \$1 million of favorable development in our reinsurance assumed operations. This included \$7 million from favorable development of catastrophe losses for the six months ended June 30, 2016. We recognized favorable reserve development during the six months ended June 30, 2016, of \$35 million for the workers' compensation line, \$23 million for the commercial casualty line, \$22 million for the commercial property line and \$28 million for the other commercial lines due to reduced uncertainty of prior accident year loss and loss adjustment expense for these lines. Our commercial auto line developed unfavorably by \$21 million for the six months ended June 30, 2016, due to higher loss cost effects in recent accident years, resulting in an increase of our reserve estimate for claims that have not yet been settled. Our personal auto line developed unfavorably by \$6 million for the six months ended June 30, 2016 for accident years prior to 2015.

For the three months ended June 30, 2015, we experienced \$70 million of favorable development on prior accident years, including \$63 million of favorable development in commercial lines, \$2 million of adverse development in personal lines and \$9 million of favorable development in excess and surplus lines. We recognized favorable reserve development during the three months ended June 30, 2015, of \$41 million for the workers' compensation line and \$23 million for the commercial casualty line due to reduced uncertainty of prior accident year loss and loss adjustment expense for these lines. Our commercial auto line developed unfavorably by \$11 million for the three months ended June 30, 2015, due to higher loss cost effects in recent accident years, resulting in an increase of our reserve estimate for claims that have not yet been settled.

For the six months ended June 30, 2015, we experienced \$92 million of favorable development on prior accident years, including \$77 million of favorable development in commercial lines, \$1 million of favorable development in personal lines and \$14 million of favorable development in excess and surplus lines. This included \$11 million from favorable development of catastrophe losses for the six months ended June 30, 2015. We recognized favorable development during the six months ended June 30, 2015, of \$56 million for the workers' compensation line, \$20 million for the commercial casualty line and \$15 million for the commercial property line due to reduced uncertainty of prior accident year loss and loss adjustment expenses for these lines. Our commercial auto line developed unfavorably by \$23 million for the six months ended June 30, 2015, due to higher loss cost effects in recent accident years, resulting in an increase of our reserve estimate for claims that have not yet been settled.

NOTE 5 – Life Policy and Investment Contract Reserves

We establish the reserves for traditional life insurance policies based on expected expenses, mortality, morbidity, withdrawal rates, timing of claim presentation and investment yields, including a provision for uncertainty. Once these assumptions are established, they generally are maintained throughout the lives of the contracts.

We use both our own experience and industry experience, adjusted for historical trends, in arriving at our assumptions for expected mortality, morbidity and withdrawal rates as well as for expected expenses. We base our assumptions for expected investment income on our own experience adjusted for current economic conditions.

We establish reserves for the company's universal life, deferred annuity and structured settlement policies equal to the cumulative account balances, which include premium deposits plus credited interest less charges and withdrawals. Some of our universal life policies contain no-lapse guarantee provisions. For these policies, we establish a reserve in addition to the account balance, based on expected no-lapse guarantee benefits and expected policy assessments.

This table summarizes our life policy and investment contract reserves:

| (Dollars in millions) | June 30, December 31, | |
|--|-----------------------|----------|
| | 2016 | 2015 |
| Life policy reserves: | | |
| Ordinary/traditional life | \$ 975 | \$ 943 |
| Other | 44 | 44 |
| Subtotal | 1,019 | 987 |
| Investment contract reserves: | | |
| Deferred annuities | 863 | 860 |
| Universal life | 563 | 558 |
| Structured settlements | 173 | 174 |
| Other | 6 | 4 |
| Subtotal | 1,605 | 1,596 |
| Total life policy and investment contract reserves | \$ 2,624 | \$ 2,583 |

NOTE 6 – Deferred Policy Acquisition Costs

Expenses directly related to successfully acquired insurance policies – primarily commissions, premium taxes and underwriting costs – are deferred and amortized over the terms of the policies. We update our acquisition cost assumptions periodically to reflect actual experience, and we evaluate the costs for recoverability. The table below shows the deferred policy acquisition costs and asset reconciliation.

| (Dollars in millions) | Three months ended June 30, 2016 | | Six months ended June 30, 2015 | |
|--|---|--------|---|--------|
| Property casualty: | | | | |
| Deferred policy acquisition costs asset, beginning of period | \$397 | \$377 | \$388 | \$379 |
| Capitalized deferred policy acquisition costs | 218 | 209 | 428 | 405 |
| Amortized deferred policy acquisition costs | (203) | (196) | (404) | (394) |
| Deferred policy acquisition costs asset, end of period | \$412 | \$390 | \$412 | \$390 |
| Life: | | | | |
| Deferred policy acquisition costs asset, beginning of period | \$221 | \$194 | \$228 | \$199 |
| Capitalized deferred policy acquisition costs | 12 | 12 | 24 | 23 |
| Amortized deferred policy acquisition costs | (11) | (8) | (22) | (19) |
| Amortized shadow deferred policy acquisition costs | (10) | 12 | (18) | 7 |
| Deferred policy acquisition costs asset, end of period | \$212 | \$210 | \$212 | \$210 |
| Consolidated: | | | | |
| Deferred policy acquisition costs asset, beginning of period | \$618 | \$571 | \$616 | \$578 |
| Capitalized deferred policy acquisition costs | 230 | 221 | 452 | 428 |
| Amortized deferred policy acquisition costs | (214) | (204) | (426) | (413) |
| Amortized shadow deferred policy acquisition costs | (10) | 12 | (18) | 7 |
| Deferred policy acquisition costs asset, end of period | \$624 | \$600 | \$624 | \$600 |

No premium deficiencies were recorded in the condensed consolidated statements of income, as the sum of the anticipated loss and loss adjustment expenses, policyholder dividends and unamortized deferred acquisition expenses did not exceed the related unearned premiums and anticipated investment income.

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NOTE 7 – Accumulated Other Comprehensive Income

Accumulated other comprehensive income (AOCI) includes changes in unrealized gains and losses on investments, changes in pension obligations and changes in life deferred acquisition costs, life policy reserves and other as follows: (Dollars in millions)

| | Three months ended June 30, | | | | | |
|---|-----------------------------|------------|---------|------------|------------|---------|
| | 2016 | | | 2015 | | |
| | Before tax | Income tax | Net | Before tax | Income tax | Net |
| Investments: | | | | | | |
| AOCI, beginning of period | \$2,384 | \$ 822 | \$1,562 | \$2,676 | \$ 927 | \$1,749 |
| OCI before realized gains recognized in net income | 331 | 118 | 213 | (260) | (91) | (169) |
| Realized gains recognized in net income | (42) | (15) | (27) | (59) | (21) | (38) |
| OCI | 289 | 103 | 186 | (319) | (112) | (207) |
| AOCI, end of period | \$2,673 | \$ 925 | \$1,748 | \$2,357 | \$ 815 | \$1,542 |
| Pension obligations: | | | | | | |
| AOCI, beginning of period | \$(41) | \$(13) | \$(28) | \$(35) | \$(12) | \$(23) |
| OCI excluding amortization recognized in net income | — | — | — | — | — | — |
| Amortization recognized in net income | 1 | — | 1 | 2 | 1 | 1 |
| OCI | 1 | — | 1 | 2 | 1 | 1 |
| AOCI, end of period | \$(40) | \$(13) | \$(27) | \$(33) | \$(11) | \$(22) |
| Life deferred acquisition costs, life policy reserves and other: | | | | | | |
| AOCI, beginning of period | \$(3) | \$— | \$(3) | \$(14) | \$(4) | \$(10) |
| OCI before realized gains recognized in net income | (5) | (2) | (3) | 7 | 3 | 4 |
| Realized gains recognized in net income | (2) | (1) | (1) | (1) | (1) | — |
| OCI | (7) | (3) | (4) | 6 | 2 | 4 |
| AOCI, end of period | \$(10) | \$(3) | \$(7) | \$(8) | \$(2) | \$(6) |
| Summary of AOCI: | | | | | | |
| AOCI, beginning of period | \$2,340 | \$ 809 | \$1,531 | \$2,627 | \$ 911 | \$1,716 |
| Investments OCI | 289 | 103 | 186 | (319) | (112) | (207) |
| Pension obligations OCI | 1 | — | 1 | 2 | 1 | 1 |
| Life deferred acquisition costs, life policy reserves and other OCI | (7) | (3) | (4) | 6 | 2 | 4 |
| Total OCI | 283 | 100 | 183 | (311) | (109) | (202) |
| AOCI, end of period | \$2,623 | \$ 909 | \$1,714 | \$2,316 | \$ 802 | \$1,514 |

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| (Dollars in millions) | Six months ended June 30, | | | | | |
|---|---------------------------|------------|---------|------------|------------|---------|
| | 2016 | | | 2015 | | |
| | Before tax | Income tax | Net | Before tax | Income tax | Net |
| Investments: | | | | | | |
| AOCI, beginning of period | \$2,094 | \$ 722 | \$1,372 | \$2,719 | \$ 942 | \$1,777 |
| OCI excluding realized gains recognized in net income | 682 | 239 | 443 | (257) | (90) | (167) |
| Realized gains recognized in net income | (103) | (36) | (67) | (105) | (37) | (68) |
| OCI | 579 | 203 | 376 | (362) | (127) | (235) |
| AOCI, end of period | \$2,673 | \$ 925 | \$1,748 | \$2,357 | \$ 815 | \$1,542 |
| Pension obligations: | | | | | | |
| AOCI, beginning of period | \$(42) | \$(14) | \$(28) | \$(36) | \$(12) | \$(24) |
| OCI excluding amortization recognized in net income | — | — | — | — | — | — |
| Amortization recognized in net income | 2 | 1 | 1 | 3 | 1 | 2 |
| OCI | 2 | 1 | 1 | 3 | 1 | 2 |
| AOCI, end of period | \$(40) | \$(13) | \$(27) | \$(33) | \$(11) | \$(22) |
| Life deferred acquisition costs, life policy reserves and other: | | | | | | |
| AOCI, beginning of period | \$1 | \$ 1 | \$— | \$(12) | \$(3) | \$(9) |
| OCI excluding realized gains recognized in net income | (9) | (3) | (6) | 6 | 2 | 4 |
| Realized gains recognized in net income | (2) | (1) | (1) | (2) | (1) | (1) |
| OCI | (11) | (4) | (7) | 4 | 1 | 3 |
| AOCI, end of period | \$(10) | \$(3) | \$(7) | \$(8) | \$(2) | \$(6) |
| Summary of AOCI: | | | | | | |
| AOCI, beginning of period | \$2,053 | \$ 709 | \$1,344 | \$2,671 | \$ 927 | \$1,744 |
| Investments OCI | 579 | 203 | 376 | (362) | (127) | (235) |
| Pension obligations OCI | 2 | 1 | 1 | 3 | 1 | 2 |
| Life deferred acquisition costs, life policy reserves and other OCI | (11) | (4) | (7) | 4 | 1 | 3 |
| Total OCI | 570 | 200 | 370 | (355) | (125) | (230) |
| AOCI, end of period | \$2,623 | \$ 909 | \$1,714 | \$2,316 | \$ 802 | \$1,514 |

Investments realized gains and life deferred acquisition costs, life policy reserves and other realized gains are recorded in the realized investment gains, net, line item in the condensed consolidated statements of income. Amortization on pension obligations is recorded in the insurance losses and contract holders' benefits and underwriting, acquisition and insurance expenses in the condensed consolidated statements of income.

NOTE 8 – Reinsurance

Primary components of our property casualty operations assumed reinsurance include involuntary and voluntary assumed as well as contracts from our reinsurance assumed operations, known as Cincinnati ReSM. Primary components of our ceded reinsurance include a property per risk treaty, property excess treaty, casualty per occurrence treaty, casualty excess treaty, property catastrophe treaty and catastrophe bonds and retrocessions on our reinsurance assumed operations. Management's decisions about the appropriate level of risk retention are affected by various factors, including changes in our underwriting practices, capacity to retain risks and reinsurance market conditions.

Our condensed consolidated statements of income include earned consolidated property casualty insurance premiums on assumed and ceded business:

| (Dollars in millions) | Three months | | Six months | |
|-------------------------|----------------|---------|----------------|---------|
| | ended June 30, | | ended June 30, | |
| | 2016 | 2015 | 2016 | 2015 |
| Direct earned premiums | \$1,137 | \$1,093 | \$2,256 | \$2,169 |
| Assumed earned premiums | 16 | 3 | 31 | 5 |
| Ceded earned premiums | (39) | (37) | (77) | (74) |
| Earned premiums | \$1,114 | \$1,059 | \$2,210 | \$2,100 |

Our condensed consolidated statements of income include incurred consolidated property casualty insurance loss and loss expenses on assumed and ceded business:

| (Dollars in millions) | Three months | | Six months | |
|---|----------------|-------|----------------|---------|
| | ended June 30, | | ended June 30, | |
| | 2016 | 2015 | 2016 | 2015 |
| Direct incurred loss and loss expenses | \$792 | \$675 | \$1,440 | \$1,366 |
| Assumed incurred loss and loss expenses | 11 | 1 | 21 | 0 |
| Ceded incurred loss and loss expenses | (44) | (22) | (41) | (23) |
| Incurred loss and loss expenses | \$759 | \$654 | \$1,420 | \$1,343 |

Our change in ceded incurred compared to prior years resulted from an increase in current accident year losses.

Our life insurance company purchases reinsurance for protection of a portion of the risk that is written. Primary components of our life reinsurance program include individual mortality coverage and aggregate catastrophe and accidental death coverage in excess of certain deductibles.

Our condensed consolidated statements of income include earned life insurance premiums on ceded business:

| (Dollars in millions) | Three months | | Six months | |
|------------------------|----------------|-------|----------------|-------|
| | ended June 30, | | ended June 30, | |
| | 2016 | 2015 | 2016 | 2015 |
| Direct earned premiums | \$75 | \$68 | \$146 | \$133 |
| Ceded earned premiums | (16) | (16) | (29) | (28) |
| Earned premiums | \$59 | \$52 | \$117 | \$105 |

Our condensed consolidated statements of income include life insurance contract holders' benefits incurred on ceded business:

| (Dollars in millions) | Three months ended June 30, | | Six months ended June 30, | |
|--|-----------------------------|-------|---------------------------|-------|
| | 2016 | 2015 | 2016 | 2015 |
| Direct contract holders' benefits incurred | \$80 | \$72 | \$156 | \$144 |
| Ceded contract holders' benefits incurred | (18) | (14) | (31) | (26) |
| Contract holders' benefits incurred | \$62 | \$58 | \$125 | \$118 |

The ceded benefits incurred can vary depending on the type of life insurance policy held and the year the policy was sold.

NOTE 9 – Income Taxes

As of June 30, 2016, and December 31, 2015, we had no liability for unrecognized tax benefits.

The differences between the 35 percent statutory federal income tax rate and our effective income tax rate were as follows:

| (Dollars in millions) | Three months ended June 30, | | | | Six months ended June 30, | | | |
|--|-----------------------------|--------|------|--------|---------------------------|--------|-------|--------|
| | 2016 | | 2015 | | 2016 | | 2015 | |
| Tax at statutory rate: | \$58 | 35.0 % | \$87 | 35.0 % | \$151 | 35.0 % | \$148 | 35.0 % |
| Increase (decrease) resulting from: | | | | | | | | |
| Tax-exempt income from municipal bonds | (8) | (4.8) | (8) | (3.2) | (17) | (3.9) | (16) | (3.8) |
| Dividend received exclusion | (8) | (4.8) | (7) | (2.8) | (16) | (3.7) | (15) | (3.6) |
| Other | 1 | 0.5 | 0 | 0.0 | 2 | 0.4 | 1 | 0.4 |
| Provision for income taxes | \$43 | 25.9 % | \$72 | 29.0 % | \$120 | 27.8 % | \$118 | 28.0 % |

The provision for federal income taxes is based upon filing a consolidated income tax return for the company and its subsidiaries. As of June 30, 2016, we had no operating or capital loss carry forwards.

NOTE 10 – Net Income Per Common Share

Basic earnings per share are computed based on the weighted average number of common shares outstanding. Diluted earnings per share are computed based on the weighted average number of common and dilutive potential common shares outstanding using the treasury stock method. The table shows calculations for basic and diluted earnings per share:

| (In millions except per share data) | Three months ended June 30, | | Six months ended June 30, | |
|--|-----------------------------|-------|---------------------------|-------|
| | 2016 | 2015 | 2016 | 2015 |
| Numerator: | | | | |
| Net income—basic and diluted | \$123 | \$176 | \$311 | \$304 |
| Denominator: | | | | |
| Basic weighted-average common shares outstanding | 164.5 | 164.1 | 164.4 | 164.1 |
| Effect of share-based awards: | | | | |

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| | | | | |
|---|--------|--------|--------|--------|
| Stock options | 1.1 | 0.9 | 1.1 | 0.9 |
| Nonvested shares | 0.9 | 0.5 | 0.8 | 0.5 |
| Diluted weighted-average shares | 166.5 | 165.5 | 166.3 | 165.5 |
| Earnings per share: | | | | |
| Basic | \$0.75 | \$1.07 | \$1.89 | \$1.85 |
| Diluted | 0.74 | 1.06 | 1.87 | 1.84 |
| Number of anti-dilutive share-based awards: | 0.3 | 0.7 | 0.4 | 0.7 |

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The sources of dilution of our common shares are certain equity-based awards. See our 2015 Annual Report on Form 10-K, Item 8, Note 17, Share-Based Associate Compensation Plans, Page 152, for information about equity-based awards. The above table shows the number of anti-dilutive share-based awards for the three and six months ended June 30, 2016 and 2015. We did not include these share-based awards in the computation of net income per common share (diluted) because their exercise would have anti-dilutive effects.

NOTE 11 – Employee Retirement Benefits

The following summarizes the components of net periodic benefit cost for our qualified and supplemental pension plans:

| (Dollars in millions) | Three months ended | | Six months ended | |
|---|--------------------|---------------|------------------|---------------|
| | June 30, 2016 | June 30, 2015 | June 30, 2016 | June 30, 2015 |
| Service cost | \$2 | \$3 | \$5 | \$6 |
| Interest cost | 4 | 4 | 7 | 7 |
| Expected return on plan assets | (4) | (5) | (9) | (9) |
| Amortization of actuarial loss and prior service cost | 1 | 2 | 2 | 3 |
| Net periodic benefit cost | \$3 | \$4 | \$5 | \$7 |

See our 2015 Annual Report on Form 10-K, Item 8, Note 13, Employee Retirement Benefits, Page 146, for information on our retirement benefits. We made matching contributions totaling \$4 million and \$3 million to our 401(k) and Top Hat savings plans during the second quarter of 2016 and 2015 and contributions of \$8 million and \$7 million for the first half of 2016 and 2015, respectively.

We contributed \$5 million to our qualified pension plan during the first six months of 2016. We also contributed \$8 million to our qualified pension plan during the third quarter of 2016 and do not anticipate further contributions during the remainder of 2016.

NOTE 12 – Commitments and Contingent Liabilities

In the ordinary course of conducting business, the company and its subsidiaries are named as defendants in various legal proceedings. Most of these proceedings are claims litigation involving the company's insurance subsidiaries in which the company is either defending or providing indemnity for third-party claims brought against insureds or litigating first-party coverage claims. The company accounts for such activity through the establishment of unpaid loss and loss expense reserves. We believe that the ultimate liability, if any, with respect to such ordinary-course claims litigation, after consideration of provisions made for potential losses and costs of defense, is immaterial to our consolidated financial condition, results of operations and cash flows.

The company and its subsidiaries also are occasionally involved in other legal and regulatory proceedings, some of which assert claims for substantial amounts. These actions include, among others, putative class actions seeking certification of a state or national class. Such proceedings have alleged, for example, breach of an alleged duty to search national databases to ascertain unreported deaths of insureds under life insurance policies. The company's insurance subsidiaries also are occasionally parties to individual actions in which extra-contractual damages, punitive damages or penalties are sought, such as claims alleging bad faith handling of insurance claims or writing unauthorized coverage or claims alleging discrimination by former or current associates.

On a quarterly basis, we review these outstanding matters. Under current accounting guidance, we establish accruals when it is probable that a loss has been incurred and we can reasonably estimate its potential exposure. The company accounts for such probable and estimable losses, if any, through the establishment of legal expense reserves. Based on our quarterly review, we believe that our accruals for probable and estimable losses are reasonable and that the amounts accrued do not have a material effect on our consolidated financial condition or results of operations. However, if any one or more of these matters results in a judgment against us or settlement for an amount that is significantly greater than the amount accrued, the resulting liability could have a material effect on the company's consolidated results of operations or cash flows. Based on our most recent review, our estimate for any other matters for which the risk of loss is not probable, but more than remote, is less than \$1 million.

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NOTE 13 – Segment Information

We operate primarily in two industries, property casualty insurance and life insurance. We regularly review our reporting segments to make decisions about allocating resources and assessing performance. Our reporting segments are:

- Commercial lines insurance
- Personal lines insurance
- Excess and surplus lines insurance
- Life insurance
- Investments

We report as Other the noninvestment operations of the parent company and its noninsurer subsidiary, CFC Investment Company and Cincinnati Re, our reinsurance assumed operations. See our 2015 Annual Report on Form 10-K, Item 8, Note 18, Segment Information, Page 155, for a description of revenue, income or loss before income taxes and identifiable assets for each of the five segments.

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Segment information is summarized in the following table:

| (Dollars in millions) | Three months ended June 30, | | Six months ended June 30, | |
|---|--------------------------------|---------|------------------------------|---------|
| | 2016 | 2015 | 2016 | 2015 |
| Revenues: | | | | |
| Commercial lines insurance | | | | |
| Commercial casualty | \$263 | \$252 | \$520 | \$496 |
| Commercial property | 215 | 203 | 429 | 399 |
| Commercial auto | 147 | 139 | 291 | 275 |
| Workers' compensation | 89 | 90 | 178 | 183 |
| Other commercial | 57 | 61 | 113 | 125 |
| Commercial lines insurance premiums | 771 | 745 | 1,531 | 1,478 |
| Fee revenues | 1 | 1 | 2 | 2 |
| Total commercial lines insurance | 772 | 746 | 1,533 | 1,480 |
| Personal lines insurance | | | | |
| Personal auto | 135 | 125 | 266 | 248 |
| Homeowner | 121 | 114 | 240 | 228 |
| Other personal | 32 | 33 | 65 | 64 |
| Personal lines insurance premiums | 288 | 272 | 571 | 540 |
| Fee revenues | 1 | — | 2 | 1 |
| Total personal lines insurance | 289 | 272 | 573 | 541 |
| Excess and surplus lines insurance | | | | |
| Excess and surplus lines insurance | 45 | 42 | 88 | 82 |
| Fee revenues | — | 1 | — | 1 |
| Total excess and surplus lines insurance | 45 | 43 | 88 | 83 |
| Life insurance premiums | | | | |
| Life insurance premiums | 59 | 52 | 117 | 105 |
| Separate account investment management fees | 1 | 1 | 2 | 2 |
| Total life insurance | 60 | 53 | 119 | 107 |
| Investments | | | | |
| Investment income, net of expenses | 149 | 140 | 294 | 279 |
| Realized investment gains, net | 44 | 60 | 105 | 107 |
| Total investment revenue | 193 | 200 | 399 | 386 |
| Other | | | | |
| Cincinnati Re insurance premiums | 10 | — | 20 | — |
| Other | 2 | 2 | 3 | 4 |
| Total other revenue | 12 | 2 | 23 | 4 |
| Total revenues | \$1,371 | \$1,316 | \$2,735 | \$2,601 |
| Income (loss) before income taxes: | | | | |
| Insurance underwriting results | | | | |
| Commercial lines insurance | \$26 | \$97 | \$76 | \$123 |
| Personal lines insurance | (20) | (25) | 8 | (28) |
| Excess and surplus lines insurance | 5 | 11 | 22 | 15 |
| Life insurance | 1 | 1 | — | (2) |
| Investments | 171 | 178 | 355 | 343 |

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| | | | | |
|----------------------------------|-----------------------|-----------|-------|-------|
| Other | (17) | (14) | (30) | (29) |
| Total income before income taxes | \$166 | \$248 | \$431 | \$422 |
| Identifiable assets: | June 30, December 31, | | | |
| | 2016 | 2015 | | |
| Property casualty insurance | \$2,888 | \$ 2,717 | | |
| Life insurance | 1,422 | 1,325 | | |
| Investments | 15,506 | 14,485 | | |
| Other | 335 | 361 | | |
| Total | \$20,151 | \$ 18,888 | | |

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion highlights significant factors influencing the condensed consolidated results of operations and financial position of Cincinnati Financial Corporation. It should be read in conjunction with the consolidated financial statements and related notes included in our 2015 Annual Report on Form 10-K. Unless otherwise noted, the industry data is prepared by A.M. Best Co., a leading insurance industry statistical, analytical and financial strength rating organization. Information from A.M. Best is presented on a statutory basis. When we provide our results on a comparable statutory basis, we label it as such; all other company data is presented in accordance with accounting principles generally accepted in the United States of America (GAAP).

We present per share data on a diluted basis unless otherwise noted, adjusting those amounts for all stock splits and dividends. Dollar amounts are rounded to millions; calculations of percent changes are based on dollar amounts rounded to the nearest million. Certain percentage changes are identified as not meaningful (nm).

SAFE HARBOR STATEMENT

This is our "Safe Harbor" statement under the Private Securities Litigation Reform Act of 1995. Our business is subject to certain risks and uncertainties that may cause actual results to differ materially from those suggested by the forward-looking statements in this report. Some of those risks and uncertainties are discussed in our 2015 Annual Report on Form 10-K, Item 1A, Risk Factors, Page 26.

Factors that could cause or contribute to such differences include, but are not limited to:

- Unusually high levels of catastrophe losses due to risk concentrations, changes in weather patterns, environmental events, terrorism incidents or other causes
- Increased frequency and/or severity of claims or development of claims that are unforeseen at the time of policy issuance
- Inadequate estimates, assumptions or reliance on third-party data used for critical accounting estimates
- Declines in overall stock market values negatively affecting the company's equity portfolio and book value
- Domestic and global events resulting in capital market or credit market uncertainty, followed by prolonged periods of economic instability or recession, that lead to:
 - Significant or prolonged decline in the fair value of a particular security or group of securities and impairment of the asset(s)
 - Significant decline in investment income due to reduced or eliminated dividend payouts from a particular security or group of securities
 - Significant rise in losses from surety and director and officer policies written for financial institutions or other insured entities
 - Prolonged low interest rate environment or other factors that limit the company's ability to generate growth in investment income or interest rate fluctuations that result in declining values of fixed-maturity investments, including declines in accounts in which we hold bank-owned life insurance contract assets
- Recession or other economic conditions resulting in lower demand for insurance products or increased payment delinquencies
- Difficulties with technology or data security breaches, including cyberattacks, that could negatively affect our ability to conduct business and our relationships with agents, policyholders and others
- Disruption of the insurance market caused by technology innovations such as driverless cars that could decrease consumer demand for insurance products
- Delays, inadequate data developed internally or from third parties, or performance inadequacies from ongoing development and implementation of underwriting and pricing methods, including telematics and other usage-based insurance methods, or technology projects and enhancements expected to increase our pricing accuracy, underwriting profit and competitiveness

- Increased competition that could result in a significant reduction in the company's premium volume
- Changing consumer insurance-buying habits and consolidation of independent insurance agencies that could alter our competitive advantages

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• Inability to obtain adequate ceded reinsurance on acceptable terms, amount of reinsurance coverage purchased, financial strength of reinsurers and the potential for nonpayment or delay in payment by reinsurers

• Inability to defer policy acquisition costs for any business segment if pricing and loss trends would lead management to conclude that segment could not achieve sustainable profitability

• Inability of our subsidiaries to pay dividends consistent with current or past levels

• Events or conditions that could weaken or harm the company's relationships with its independent agencies and hamper opportunities to add new agencies, resulting in limitations on the company's opportunities for growth, such as:

- Downgrades of the company's financial strength ratings
- Concerns that doing business with the company is too difficult
- Perceptions that the company's level of service, particularly claims service, is no longer a distinguishing characteristic in the marketplace

Inability or unwillingness to nimbly develop and introduce coverage product updates and innovations that our competitors offer and consumers expect to find in the marketplace

• Actions of insurance departments, state attorneys general or other regulatory agencies, including a change to a federal system of regulation from a state-based system, that:

- Impose new obligations on us that increase our expenses or change the assumptions underlying our critical accounting estimates
- Place the insurance industry under greater regulatory scrutiny or result in new statutes, rules and regulations
- Restrict our ability to exit or reduce writings of unprofitable coverages or lines of business
- Add assessments for guaranty funds, other insurance-related assessments or mandatory reinsurance arrangements; or that impair our ability to recover such assessments through future surcharges or other rate changes
- Increase our provision for federal income taxes due to changes in tax law
- Increase our other expenses
- Limit our ability to set fair, adequate and reasonable rates
- Place us at a disadvantage in the marketplace
- Restrict our ability to execute our business model, including the way we compensate agents

• Adverse outcomes from litigation or administrative proceedings

• Events or actions, including unauthorized intentional circumvention of controls, that reduce the company's future ability to maintain effective internal control over financial reporting under the Sarbanes-Oxley Act of 2002

• Unforeseen departure of certain executive officers or other key employees due to retirement, health or other causes that could interrupt progress toward important strategic goals or diminish the effectiveness of certain longstanding relationships with insurance agents and others

• Events, such as an epidemic, natural catastrophe or terrorism, that could hamper our ability to assemble our workforce at our headquarters location

Further, the company's insurance businesses are subject to the effects of changing social, global, economic and regulatory environments. Public and regulatory initiatives have included efforts to adversely influence and restrict premium rates, restrict the ability to cancel policies, impose underwriting standards and expand overall regulation. The company also is subject to public and regulatory initiatives that can affect the market value for its common stock, such as measures affecting corporate financial reporting and governance. The ultimate changes and eventual effects, if any, of these initiatives are uncertain.

CORPORATE FINANCIAL HIGHLIGHTS

Net Income and Comprehensive Income Data

| (Dollars in millions except per share data) | Three months ended June 30, | | | Six months ended June 30, | | |
|---|-----------------------------|---------|----------|---------------------------|---------|----------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Earned premiums | \$1,173 | \$1,111 | 6 | \$2,327 | \$2,205 | 6 |
| Investment income, net of expenses (pretax) | 149 | 140 | 6 | 294 | 279 | 5 |
| Realized investment gains, net (pretax) | 44 | 60 | (27) | 105 | 107 | (2) |
| Total revenues | 1,371 | 1,316 | 4 | 2,735 | 2,601 | 5 |
| Net income | 123 | 176 | (30) | 311 | 304 | 2 |
| Comprehensive income | 306 | (26) | nm | 681 | 74 | 820 |
| Net income per share—diluted | 0.74 | 1.06 | (30) | 1.87 | 1.84 | 2 |
| Cash dividends declared per share | 0.48 | 0.46 | 4 | 0.96 | 0.92 | 4 |
| Diluted weighted average shares outstanding | 166.5 | 165.5 | 1 | 166.3 | 165.5 | 0 |

Total revenues rose for the second quarter and the first six months of 2016, compared with the same periods of 2015, primarily due to higher earned premiums. Premium and investment revenue trends are discussed further in the respective sections of Financial Results.

Realized investment gains and losses are recognized on the sales of investments or as otherwise required by GAAP. We have substantial discretion in the timing of investment sales, and that timing generally is independent of the insurance underwriting process. GAAP also requires us to recognize in net income the gains or losses from certain changes in fair values of securities even though we continue to hold the securities.

Net income for the second quarter of 2016, compared with the same period of 2015, decreased \$53 million, reflecting a decrease in property casualty underwriting income of \$47 million after taxes and a \$10 million decrease in after-tax net realized investment gains. Higher catastrophe losses, mostly weather related, were \$56 million more after taxes and unfavorably affected both net income and property casualty underwriting income. After-tax investment income in our investment segment results for the second quarter of 2016 rose \$7 million compared with the same quarter of 2015. Life insurance segment results on a pretax basis for second-quarter 2016 matched second-quarter 2015.

For the six months ended June 30, 2016, net income rose \$7 million compared with the first six months of 2015, primarily due to an \$11 million increase in after-tax investment income. Property casualty underwriting income decreased by \$3 million after taxes, driven by an unfavorable \$50 million effect from higher catastrophe losses that offset improvement in other loss experience from our underwriting operations. After-tax net realized investment gains and losses for the first half of 2016 were \$1 million lower than a year ago. Life insurance segment results on a pretax basis improved by \$2 million.

Performance by segment is discussed below in Financial Results. As discussed in our 2015 Annual Report on Form 10-K, Item 7, Factors Influencing Our Future Performance, Page 45, there are several reasons that our performance during 2016 may be below our long-term targets. In that annual report, as part of Financial Results, we also discussed the full-year 2016 outlook for each reporting segment.

The board of directors is committed to rewarding shareholders directly through cash dividends and through share repurchase authorizations. Through 2015, the company had increased the indicated annual cash dividend rate for 55 consecutive years, a record we believe was matched by only eight other publicly traded companies. In January

2016, the board of directors increased the regular quarterly dividend to 48 cents per share, setting the stage for our 56th consecutive year of increasing cash dividends. During the first six months of 2016, cash dividends declared by the company increased more than 4 percent compared with the same period of 2015. Our board regularly evaluates relevant factors in decisions related to dividends and share repurchases. The 2016 dividend increase reflected our strong earnings performance and signaled management's and the board's positive outlook and confidence in our outstanding capital, liquidity and financial flexibility.

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Balance Sheet Data and Performance Measures

| (In millions except share data) | At June 30, 2016 | At December 31, 2015 |
|---------------------------------|------------------------|-------------------------------|
| Total investments | \$15,459 | \$14,423 |
| Total assets | 20,151 | 18,888 |
| Short-term debt | 28 | 35 |
| Long-term debt | 786 | 786 |
| Shareholders' equity | 6,971 | 6,427 |
| Book value per share | 42.37 | 39.20 |
| Debt-to-total-capital ratio | 10.5 | % 11.3 % |

Total assets at June 30, 2016, increased 7 percent compared with year-end 2015, and included 7 percent growth in investments largely driven by higher fair values for many securities in our portfolio. Shareholders' equity increased 8 percent, and book value per share also increased 8 percent during the first six months of 2016. Our debt-to-total-capital ratio (capital is the sum of debt plus shareholders' equity) was lower than at year-end 2015.

Our value creation ratio is a non-GAAP measure defined below and is our primary performance metric. That ratio was 10.5 percent for the first six months of 2016, and was better than the same period in 2015 primarily due to higher net gains from our investment portfolio. The \$3.17 increase in book value per share during the first six months of 2016 contributed 8.1 percentage points to the value creation ratio, while dividends declared at \$0.96 per share contributed 2.4 points. Value creation ratio trends in total and by major components, along with a reconciliation of the non-GAAP measure to comparable GAAP measures, are shown in the tables below.

| | Three months ended June 30, 2016 | | Six months ended June 30, 2016 | |
|--|---|--------|--------------------------------------|-------|
| | 2016 | 2015 | 2016 | 2015 |
| Value creation ratio major components: | | | | |
| Net income before net realized gains | 1.4% | 2.1 % | 3.8 % | 3.5 % |
| Change in fixed-maturity securities, realized and unrealized gains | 1.8 | (1.8) | 3.0 | (1.3) |
| Change in equity securities, realized and unrealized gains | 1.4 | (0.8) | 3.9 | (1.2) |
| Other | 0.0 | 0.1 | (0.2) | (0.1) |
| Value creation ratio | 4.6% | (0.4)% | 10.5 % | 0.9 % |

| (Dollars are per share) | Three months ended June 30, 2016 | | Six months ended June 30, 2016 | |
|-------------------------------------|--|----------|--------------------------------------|----------|
| | 2016 | 2015 | 2016 | 2015 |
| Book value change per share: | | | | |
| End of period book value | \$42.37 | \$39.60 | \$42.37 | \$39.60 |
| Less beginning of period book value | 40.96 | 40.22 | 39.20 | 40.14 |
| Change in book value | \$1.41 | \$(0.62) | \$3.17 | \$(0.54) |

Change in book value:

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| | | | | |
|--|---------|-----------|---------|-----------|
| Net income before realized gains | \$0.58 | \$0.84 | \$1.48 | \$1.43 |
| Change in fixed-maturity securities, realized and unrealized gains | 0.72 | (0.71) | 1.18 | (0.52) |
| Change in equity securities, realized and unrealized gains | 0.59 | (0.32) | 1.52 | (0.50) |
| Dividend declared to shareholders | (0.48) | (0.46) | (0.96) | (0.92) |
| Other | 0.00 | 0.03 | (0.05) | (0.03) |
| Change in book value | \$1.41 | \$(0.62) | \$3.17 | \$(0.54) |

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| (Dollars are per share) | Three months ended | | Six months ended | |
|--|--------------------|-----------|------------------|-----------|
| | June 30, 2016 | 2015 | June 30, 2016 | 2015 |
| Value creation ratio: | | | | |
| End of period book value | \$42.37 | \$39.60 | \$42.37 | \$39.60 |
| Less beginning of period book value | 40.96 | 40.22 | 39.20 | 40.14 |
| Change in book value | 1.41 | (0.62) | 3.17 | (0.54) |
| Dividend declared to shareholders | 0.48 | 0.46 | 0.96 | 0.92 |
| Total value creation | \$1.89 | \$(0.16) | \$4.13 | \$0.38 |
| Value creation ratio from change in book value* | 3.4 | % (1.5)% | 8.1 | % (1.4)% |
| Value creation ratio from dividends declared to shareholders** | 1.2 | 1.1 | 2.4 | 2.3 |
| Value creation ratio | 4.6 | % (0.4)% | 10.5 | % 0.9 % |

*Change in book value divided by the beginning of period book value

**Dividend declared to shareholders divided by beginning of period book value

DRIVERS OF LONG-TERM VALUE CREATION

Operating through The Cincinnati Insurance Company, Cincinnati Financial Corporation is one of the 25 largest property casualty insurers in the nation, based on 2015 net written premiums for approximately 2,000 U.S. stock and mutual insurer groups. We market our insurance products through a select group of independent insurance agencies as discussed in our 2015 Annual Report on Form 10-K, Item 1, Our Business and Our Strategy, Page 5. At June 30, 2016, we actively marketed through agencies located in 40 states. We maintain a long-term perspective that guides us in addressing immediate challenges or opportunities while focusing on the major decisions that best position our company for success through all market cycles.

To measure our long-term progress in creating shareholder value, our value creation ratio is our primary financial performance target. As discussed in our 2015 Annual Report on Form 10-K, Item 7, Executive Summary, Page 40, management believes this non-GAAP measure is a meaningful indicator of our long-term progress in creating shareholder value, is a useful supplement to GAAP information and has three primary performance drivers:

Premium growth – We believe our agency relationships and initiatives can lead to a property casualty written premium growth rate over any five-year period that exceeds the industry average. For the first six months of 2016, our consolidated property casualty net written premium year-over-year growth was 6 percent, comparing favorably with A.M. Best's February 2016 projection of approximately 2 percent full-year growth for the industry. For the five-year period 2011 through 2015, our growth rate was approximately double that of the industry. The industry's growth rate excludes its mortgage and financial guaranty lines of business.

Combined ratio – We believe our underwriting philosophy and initiatives can generate a GAAP combined ratio over any five-year period that is consistently within the range of 95 percent to 100 percent. For the first six months of 2016, our GAAP combined ratio was 95.4 percent and our statutory combined ratio was 94.1 percent, both including 9.3 percentage points of current accident year catastrophe losses partially offset by 5.0 percentage points of favorable loss reserve development on prior accident years. As of February 2016, A.M. Best projected the industry's full-year 2016 statutory combined ratio at approximately 99 percent, including approximately 5 percentage points of catastrophe losses and a favorable effect of approximately 2 percentage points of loss reserve development on prior

accident years. The industry's ratio again excludes its mortgage and financial guaranty lines of business.

Investment contribution – We believe our investment philosophy and initiatives can drive investment income growth and lead to a total return on our equity investment portfolio over a five-year period that exceeds the five-year return of the Standard & Poor's 500 Index. For the first six months of 2016, pretax investment income was \$294 million, up 5 percent compared with the same period in 2015. We believe our investment portfolio mix provides an appropriate balance of income stability and growth with capital appreciation potential.

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Highlights of Our Strategy and Supporting Initiatives

Management has worked to identify a strategy that can lead to long-term success, with concurrence by the board of directors. Our strategy is intended to position us to compete successfully in the markets we have targeted while appropriately managing risk. Further description of our long-term, proven strategy can be found in our 2015 Annual Report on Form 10-K, Item 1, Our Business and Our Strategy, Page 5. We believe successful implementation of initiatives that support our strategy will help us better serve our agent customers and reduce volatility in our financial results while we also grow earnings and book value over the long term, successfully navigating challenging economic, market or industry pricing cycles.

Manage insurance profitability – Implementation of these initiatives is intended to enhance underwriting expertise and knowledge, thereby increasing our ability to manage our business while also gaining efficiency. Better profit margins can arise from additional information and more focused action on underperforming product lines, plus pricing capabilities we are expanding through the use of technology and analytics. In addition to enhancing company efficiency, improving internal processes also supports the ability of the independent agencies that represent us to grow profitably by allowing them to serve clients faster and to more efficiently manage agency expenses.

We continue to enhance our property casualty underwriting expertise and to effectively and efficiently underwrite individual policies and process transactions. Ongoing initiatives supporting this work include expanding our pricing and segmentation capabilities through experience and use of predictive analytics and additional data. Our segmentation efforts emphasize identification and retention of insurance policies we believe have relatively stronger pricing, while seeking more aggressive renewal terms and conditions on policies we believe have relatively weaker pricing. An area of concentration in 2016 is improving underwriting and rate adequacy for our commercial auto and personal auto lines of business. Our commercial auto policies that renewed during the first six months of 2016 experienced an estimated average price percentage increase in the mid-single-digit range, while our personal auto policies that renewed during that period averaged an estimated price percentage increase near the low end of the high-single-digit range.

Drive premium growth – Implementation of these initiatives is intended to further penetrate each market we serve through our independent agencies. Strategies aimed at specific market opportunities, along with service enhancements, can help our agents grow and increase our share of their business. Diversified growth also may reduce variability of losses from weather-related catastrophes.

We continue to appoint new agencies to develop additional points of distribution. In 2016, we are planning approximately 100 appointments of independent agencies that offer most or all of our property casualty insurance products. During the first six months of 2016, we appointed 44 new agencies that meet that criteria. We also appointed another 64 agencies to market only personal lines insurance products for us. As of June 30, 2016, a total of 1,576 agency relationships market our property casualty insurance products from 2,032 reporting locations. We plan to appoint additional agencies that focus on high net worth personal lines clients. In 2016, we are targeting approximately \$25 million in high net worth new business written premiums, including premiums from our Executive Capstone™ suite of insurance products and services. During the first six months of 2016, our agencies produced for us approximately \$14 million in high net worth new business written premiums. In the first quarter of 2016, we appointed agencies in the state of New Jersey and began to offer personal lines insurance products for the unique needs of high net worth personal lines clients. That state represents our 40th state for marketing property casualty insurance, including 32 states where we market personal lines policies.

Financial Strength

An important part of our long-term strategy is financial strength, which is described in our 2015 Annual Report on Form 10-K, Item 1, Our Business and Our Strategy, Financial Strength, Page 7. One aspect of our financial strength is prudent use of reinsurance ceded to help manage financial performance variability due to catastrophe loss experience. A description of how we use reinsurance ceded is included in our 2015 Annual Report on Form 10-K, Item 7, Liquidity and Capital Resources, 2016 Reinsurance Ceded Programs, Page 101. Another aspect of our financial strength is our investment portfolio, which remains well-diversified as discussed in this quarterly report in Item 3,

Quantitative and Qualitative Disclosures About Market Risk. Our strong parent-company liquidity and financial strength increase our flexibility to maintain a cash dividend through all periods and to continue to invest in and expand our insurance operations.

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At June 30, 2016, we held \$1.952 billion of our cash and invested assets at the parent-company level, of which \$1.772 billion, or 90.8 percent, was invested in common stocks, and \$88 million, or 4.5 percent, was cash or cash equivalents. Our debt-to-total-capital ratio of 10.5 percent remains well below our target limit. Another important indicator of financial strength is our ratio of property casualty net written premiums to statutory surplus, which was 1.0-to-1 for the 12 months ended June 30, 2016, matching year-end 2015.

Financial strength ratings assigned to us by independent rating firms also are important. In addition to rating our parent company's senior debt, four firms award insurer financial strength ratings to one or more of our insurance subsidiary companies based on their quantitative and qualitative analyses. These ratings primarily assess an insurer's ability to meet financial obligations to policyholders and do not necessarily address all of the matters that may be important to investors. Ratings are under continuous review and subject to changes or withdrawal at any time by the rating agency. Each rating should be evaluated independently of any other rating; please see each rating agency's website for its most recent report on our ratings.

All of our insurance subsidiaries continue to be highly rated. As of July 25, 2016, our insurer financial strength ratings were:

| Rating agency | Standard market property casualty insurance subsidiaries | | Life insurance subsidiary | | Excess and surplus lines insurance subsidiary | | Date of most recent affirmation or action |
|--|--|---------|---------------------------|---------|---|---------|---|
| | Rating tier | | Rating tier | | Rating tier | | |
| A.M. Best Co. ambest.com | A+ Superior | 2 of 16 | A Excellent | 3 of 16 | A+ Superior | 2 of 16 | Stable outlook (03/10/16) |
| Fitch Ratings fitchratings.com | A+ Strong | 5 of 21 | A+ Strong | 5 of 21 | - | - | Stable outlook (07/12/16) |
| Moody's Investors Service moody's.com | A1 Good | 5 of 21 | - | - | - | - | Stable outlook (05/24/16) |
| S&P Global Ratings spratings.com | A+ Strong | 5 of 21 | A+ Strong | 5 of 21 | - | - | Stable outlook (06/28/16) |

On March 10, 2016, A.M. Best affirmed, with a stable outlook, its rating for The Cincinnati Life Insurance Company, including a financial strength rating of A (Excellent) and an issuer credit rating of "a+." According to A.M. Best, the ratings reflect Cincinnati Life's positive premium growth trends, good quality investment portfolio, adequate capitalization and strategic role within Cincinnati Financial Corporation. A.M. Best noted factors that could lead to a negative rating action, including: a reduction in A.M. Best's view of the strategic importance of Cincinnati Life to its parent, a material decline in risk-adjusted capital as measured by BCAR, continued spread compression on interest-sensitive reserves that could adversely impact operating earnings or a change in business mix with a greater focus on less creditworthy products.

On May 24, 2016, Moody's Investors Service Ratings affirmed, with a stable outlook, the A1 financial strength rating it assigned to us in September 2008. Moody's reported that our ratings reflect our longstanding franchise, which benefits from strong relationships with independent agents, a focus on small and middle market commercial risks and robust capital adequacy. Moody's cited our strengths, including a conservative reserve position, low financial leverage and substantial holding company liquidity, but noted these strengths are tempered by exposure to catastrophes, limited scale in personal lines, potential investment volatility reflecting a sizeable common equity position and competition from well-capitalized nationwide commercial lines carriers.

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On June 28, 2016, S&P Global Ratings (formerly known as Standard & Poor's Ratings Services) affirmed, with a stable outlook, its financial strength rating of A+ on our standard market property casualty and life insurance subsidiaries. S&P said its rating reflected our strong competitive position, low country and industry risk, and extremely strong capital and earnings. S&P noted its rating could be lowered if capital adequacy deteriorated significantly for a prolonged period or if earnings weakened to substantially less than its base-case assumptions.

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On July 12, 2016, Fitch Ratings affirmed, with a stable outlook, the A+ financial strength rating for our standard market property casualty and life insurance subsidiaries. Fitch reported that the affirmation reflects balance sheet strengths, improved financial performance since 2012, adequate and well-managed reserves, and implementation of claims management and risk management tools. Fitch noted that its rating could be lowered if our combined ratio exceeds 105 percent on a sustained basis, if profitability on recent growth deteriorates, or if we fail to maintain a “very strong” score on Fitch’s Prism capital model.

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CONSOLIDATED PROPERTY CASUALTY INSURANCE HIGHLIGHTS

Consolidated property casualty insurance results include premiums and expenses for our standard market insurance segments (commercial lines and personal lines), our excess and surplus lines segment and our reinsurance assumed operations.

| (Dollars in millions) | Three months ended June 30, | | | Six months ended June 30, | | |
|--|-----------------------------|---------|------------|---------------------------|---------|------------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Earned premiums | \$1,114 | \$1,059 | 5 | \$2,210 | \$2,100 | 5 |
| Fee revenues | 2 | 2 | 0 | 4 | 4 | 0 |
| Total revenues | 1,116 | 1,061 | 5 | 2,214 | 2,104 | 5 |
| Loss and loss expenses from: | | | | | | |
| Current accident year before catastrophe losses | 643 | 645 | 0 | 1,325 | 1,302 | 2 |
| Current accident year catastrophe losses | 165 | 79 | 109 | 206 | 133 | 55 |
| Prior accident years before catastrophe losses | (49) | (70) | 30 | (104) | (81) | (28) |
| Prior accident years catastrophe losses | — | — | 0 | (7) | (11) | 36 |
| Loss and loss expenses | 759 | 654 | 16 | 1,420 | 1,343 | 6 |
| Underwriting expenses | 347 | 324 | 7 | 688 | 651 | 6 |
| Underwriting profit | \$10 | \$83 | (88) | \$106 | \$110 | (4) |
| Ratios as a percent of earned premiums: | | | Pt. Change | | | Pt. Change |
| Current accident year before catastrophe losses | 57.8 | % 60.9 | % (3.1) | 59.9 | % 62.0 | % (2.1) |
| Current accident year catastrophe losses | 14.8 | 7.5 | 7.3 | 9.3 | 6.3 | 3.0 |
| Prior accident years before catastrophe losses | (4.4) | (6.6) | 2.2 | (4.7) | (3.9) | (0.8) |
| Prior accident years catastrophe losses | 0.0 | 0.0 | 0.0 | (0.3) | (0.5) | 0.2 |
| Loss and loss expenses | 68.2 | 61.8 | 6.4 | 64.2 | 63.9 | 0.3 |
| Underwriting expenses | 31.1 | 30.6 | 0.5 | 31.2 | 31.0 | 0.2 |
| Combined ratio | 99.3 | % 92.4 | % 6.9 | 95.4 | % 94.9 | % 0.5 |
| Combined ratio | 99.3 | % 92.4 | % 6.9 | 95.4 | % 94.9 | % 0.5 |
| Contribution from catastrophe losses and prior years reserve development | 10.4 | 0.9 | 9.5 | 4.3 | 1.9 | 2.4 |
| Combined ratio before catastrophe losses and prior years reserve development | 88.9 | % 91.5 | % (2.6) | 91.1 | % 93.0 | % (1.9) |

Our consolidated property casualty insurance operations generated an underwriting profit of \$10 million and \$106 million for the three and six months ended June 30, 2016. The three-month decrease of \$73 million, compared with second-quarter 2015, was driven by an increase of \$86 million in losses from weather-related natural catastrophes. The six-month decrease of \$4 million, compared with the first half of 2015, included an increase of \$77 million in losses from weather-related natural catastrophes. We believe future property casualty underwriting results will continue to benefit from price increases and our ongoing initiatives to improve pricing precision and loss experience related to claims and loss control practices.

For all property casualty lines of business in aggregate, net loss and loss expense reserves at June 30, 2016, were \$229 million higher than at year-end 2015, including \$133 million for the incurred but not reported (IBNR) portion. The \$229 million reserve increase raised year-end 2015 net loss and loss expense reserves by 5 percent.

We measure and analyze property casualty underwriting results primarily by the combined ratio and its component ratios. The GAAP-basis combined ratio is the percentage of incurred losses plus all expenses per each earned premium dollar – the lower the ratio, the better the performance. An underwriting profit results when the combined ratio is below

100 percent. A combined ratio above 100 percent indicates that an insurance company's losses and expenses exceeded premiums.

Our consolidated property casualty combined ratio for the second quarter of 2016 rose 6.9 percentage points, compared with the same period of 2015, including 7.3 points from higher catastrophe losses and loss expenses.

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For the first six months of 2016, compared with the same period of 2015, our consolidated property casualty combined ratio rose 0.5 percentage points, including 3.2 points from higher catastrophe losses and loss expenses.

The combined ratio can be affected significantly by natural catastrophe losses and other large losses as discussed in detail below. The combined ratio can also be affected by updated estimates of loss and loss expense reserves established for claims that occurred in prior periods, referred to as prior accident years. Net favorable development on prior accident year reserves, including reserves for catastrophe losses, benefited the combined ratio by 5.0 percentage points in the first six months of 2016, compared with 4.4 percentage points in the same period of 2015. Net favorable development is discussed in further detail in Financial Results by property casualty insurance segment.

The ratio for current accident year loss and loss expenses before catastrophe losses improved in the first six months of 2016. The 59.9 percent ratio for the first six months of 2016 decreased 2.1 percentage points compared with the 62.0 percent accident year 2015 ratio measured as of June 30, 2015, despite an increase of 0.4 percentage points in the ratio for large losses of \$1 million or more per claim, discussed below.

The underwriting expense ratio increased 0.5 and 0.2 percentage points for the second quarter and first six months of 2016, compared with the same periods of 2015. Strategic investments that include enhancement of underwriting expertise offset the favorable effects of higher earned premiums and ongoing expense management efforts.

Consolidated Property Casualty Insurance Premiums

| (Dollars in millions) | Three months ended June 30, | | | Six months ended June 30, | | |
|--------------------------------------|-----------------------------|---------|----------|---------------------------|---------|----------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Agency renewal written premiums | \$1,057 | \$1,018 | 4 | \$2,085 | \$2,001 | 4 |
| Agency new business written premiums | 143 | 138 | 4 | 268 | 254 | 6 |
| Cincinnati Re net written premiums | 16 | — | nm | 35 | — | nm |
| Other written premiums | (22) | (14) | (57) | (47) | (47) | 0 |
| Net written premiums | 1,194 | 1,142 | 5 | 2,341 | 2,208 | 6 |
| Unearned premium change | (80) | (83) | 4 | (131) | (108) | (21) |
| Earned premiums | \$1,114 | \$1,059 | 5 | \$2,210 | \$2,100 | 5 |

The trends in net written premiums and earned premiums summarized in the table above largely reflect the effects of price increases. Price increase trends that heavily influence renewal written premium increases or decreases and other premium growth drivers for 2016 are discussed in more detail by segment below in Financial Results.

Consolidated property casualty net written premiums for the three and six months ended June 30, 2016, grew \$52 million and \$133 million compared with the same periods of 2015. Each of our property casualty segments continued to grow during the first six months of 2016. Our premium growth initiatives from prior years have provided an ongoing favorable effect on growth during the current year, particularly as newer agency relationships mature over time.

Consolidated property casualty agency new business written premiums rose \$5 million and \$14 million for the second quarter and first six months of 2016, compared with the same periods of 2015. New business written premiums in the second quarter and first half of 2016 were higher than the same periods of 2015 for each of our property casualty insurance segments. New agency appointments during 2015 and 2016 produced an \$18 million increase in standard lines new business for the first six months of 2016 compared with the same period of 2015. As we appoint new agencies that choose to move accounts to us, we report these accounts as new business. While this business is new to

us, in many cases it is not new to the agent. We believe these seasoned accounts tend to be priced more accurately than business that may be less familiar to our agent upon obtaining it from a competing agent.

Net written premiums increased \$35 million for the first half of 2016, compared with the same period of 2015, when we began to expand our reinsurance assumed operations, known as Cincinnati ReSM. Cincinnati Re assumes risks through reinsurance treaties and in some cases cedes part of the risk and related premiums to one or more unaffiliated reinsurance companies through transactions known as retrocessions. For the first six months of 2016, earned premiums for Cincinnati Re totaled \$20 million, compared with none earned in the same period a year ago.

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Other written premiums include premiums ceded to reinsurers as part of our reinsurance ceded program. A decrease in ceded premiums for the second quarter and first half of 2016, compared with the same periods of 2015, contributed less than \$1 million and \$2 million to 2016 net written premium growth.

Catastrophe losses and loss expenses typically have a material effect on property casualty results and can vary significantly from period to period. Losses from natural catastrophes contributed 14.8 and 9.0 percentage points to the combined ratio in the second quarter and first six months of 2016, compared with 7.5 and 5.8 percentage points in the same periods of 2015. Some of those losses were applicable to annual loss deductible provisions of our collateralized reinsurance funded through catastrophe bonds. For our collateralized reinsurance arrangement effective January 18, 2014, aggregate losses occurring from January 18, 2016, through June 30, 2016, totaled \$8 million from two occurrences, where aggregate losses reached the applicable loss deductible provision for the specific geographic locations included in the severe convective storm portion of that coverage. If aggregate losses, after the \$5 million per occurrence deductible, exceed \$160 million during an annual coverage period, we can recover the excess through funds that collateralize the catastrophe bonds. The following table shows consolidated property casualty insurance catastrophe losses and loss expenses incurred, net of reinsurance, as well as the effect of loss development on prior period catastrophe events. We individually list declared catastrophe events for which our incurred losses reached or exceeded \$10 million.

Consolidated Property Casualty Insurance Catastrophe Losses and Loss Expenses Incurred

| (Dollars in millions, net of reinsurance) | | | Three months ended | | | | Six months ended June | | | | |
|--|------------------------------|---------------------------|--------------------|------|-------|------------|-----------------------|-------|------------|-------|-------|
| | | | June 30, | | | | 30, | | | | |
| Dates | Event | Region | Comm.Pers. | E&S | Total | Comm.Pers. | E&S | Total | Comm.Pers. | E&S | Total |
| 2016 | | | | | | | | | | | |
| Apr. 2-3 | Hail, Wind | Midwest, Northeast, South | \$6 | \$6 | \$ — | \$12 | \$6 | \$6 | \$ — | \$12 | |
| Apr. 10-15 | Flood, hail, wind | South | 55 | — | 1 | 56 | 55 | — | 1 | 56 | |
| Apr. 25-28 | Flood, hail, wind | Midwest, South | 9 | 4 | — | 13 | 9 | 4 | — | 13 | |
| Apr. 29-May 3 | Flood, hail, wind | Midwest, South | 18 | 7 | — | 25 | 18 | 7 | — | 25 | |
| May 7-10 | Flood, hail, wind | Midwest, South, West | 14 | 6 | — | 20 | 14 | 6 | — | 20 | |
| May 11-12 | Flood, hail, wind | Midwest, South | 11 | 2 | — | 13 | 11 | 2 | — | 13 | |
| May 21-28 | Flood, hail, wind | Midwest, South, West | 11 | 2 | — | 13 | 11 | 2 | — | 13 | |
| All other 2016 catastrophes | | | 5 | 7 | 1 | 13 | 35 | 18 | 1 | 54 | |
| Development on 2015 and prior catastrophes | | | (1) | 1 | — | — | (6) | (1) | — | (7) | |
| Calendar year incurred total | | | \$128 | \$35 | \$2 | \$165 | \$153 | \$44 | \$2 | \$199 | |
| 2015 | | | | | | | | | | | |
| Feb. 16-27 | Freezing, ice and snow, wind | Midwest, Northeast, South | \$1 | \$ — | \$ — | \$1 | \$33 | \$9 | \$ — | \$42 | |
| Apr. 7-10 | Flood, hail, wind | Midwest, Northeast, South | 8 | 15 | — | 23 | 8 | 15 | — | 23 | |
| Apr. 18-20 | Flood, hail, wind | Midwest, South | 6 | 6 | — | 12 | 6 | 6 | — | 12 | |
| All other 2015 catastrophes | | | 28 | 14 | 1 | 43 | 35 | 20 | 1 | 56 | |
| Development on 2014 and prior catastrophes | | | — | — | — | — | (9) | (2) | — | (11) | |
| Calendar year incurred total | | | \$43 | \$35 | \$1 | \$79 | \$73 | \$48 | \$1 | \$122 | |

The following table includes data for losses incurred of \$1 million or more per claim, net of reinsurance.

| Consolidated Property Casualty Insurance (Dollars in millions, net of reinsurance) | Losses Incurred by Size Three months ended June 30, | | | Six months ended June 30, | | |
|---|--|--------|---------------|---------------------------|---------|---------------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Current accident year losses greater than \$5,000,000 | \$23 | \$5 | 360 | \$23 | \$17 | 35 |
| Current accident year losses \$1,000,000-\$5,000,000 | 34 | 24 | 42 | 76 | 61 | 25 |
| Large loss prior accident year reserve development | 3 | (4) | (175) | 3 | 11 | (73) |
| Total large losses incurred | 60 | 25 | 140 | 102 | 89 | 15 |
| Losses incurred but not reported | 34 | 38 | (11) | 107 | 81 | 32 |
| Other losses excluding catastrophe losses | 399 | 417 | (4) | 801 | 835 | (4) |
| Catastrophe losses | 163 | 78 | 109 | 196 | 120 | 63 |
| Total losses incurred | \$656 | \$558 | 18 | \$1,206 | \$1,125 | 7 |
| Ratios as a percent of earned premiums: | | | Pt. Change | | | Pt. Change |
| Current accident year losses greater than \$5,000,000 | 2.0 | % 0.5 | % 1.5 | 1.0 | % 0.8 | % 0.2 |
| Current accident year losses \$1,000,000-\$5,000,000 | 3.1 | 2.1 | 1.0 | 3.5 | 2.9 | 0.6 |
| Large loss prior accident year reserve development | 0.3 | (0.3) | 0.6 | 0.1 | 0.5 | (0.4) |
| Total large loss ratio | 5.4 | 2.3 | 3.1 | 4.6 | 4.2 | 0.4 |
| Losses incurred but not reported | 3.1 | 3.6 | (0.5) | 4.8 | 3.9 | 0.9 |
| Other losses excluding catastrophe losses | 35.7 | 39.6 | (3.9) | 36.2 | 39.8 | (3.6) |
| Catastrophe losses | 14.6 | 7.3 | 7.3 | 8.9 | 5.7 | 3.2 |
| Total loss ratio | 58.8 | % 52.8 | % 6.0 | 54.5 | % 53.6 | % 0.9 |

We believe the inherent variability of aggregate loss experience for our portfolio of larger policies is greater than that of our portfolio of smaller policies, and we continue to monitor the variability in addition to general inflationary trends in loss costs. Our analysis continues to indicate no unexpected concentration of large losses and case reserve increases by risk category, geographic region, policy inception, agency or field marketing territory. The second-quarter 2016 property casualty total large losses incurred of \$60 million, net of reinsurance, were higher than both the \$54 million quarterly average during 2015 and the \$25 million for the second quarter of 2015. The ratio for these large losses was 3.1 percentage points higher compared with last year's second quarter. The second-quarter 2016 amount of total large losses incurred helped contribute to the increase in the six-month 2016 total large loss ratio, compared with 2015, in addition to a first-quarter 2016 ratio that was 2.2 points lower than the first quarter of 2015. We believe results for the three- and six-month periods largely reflected normal fluctuations in loss patterns and normal variability in large case reserves for claims above \$1 million. Losses by size are discussed in further detail in results of operations by property casualty insurance segment.

FINANCIAL RESULTS

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Consolidated results reflect the operating results of each of our five segments along with the parent company and other activities reported as “Other.” The five segments are:

- Commercial lines property casualty insurance
- Personal lines property casualty insurance
- Excess and surplus lines property casualty insurance
- Life insurance
- Investments

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COMMERCIAL LINES INSURANCE RESULTS

| (Dollars in millions) | Three months ended June 30, | | | Six months ended June 30, | | |
|--|-----------------------------|--------|------------|---------------------------|---------|------------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Earned premiums | \$771 | \$745 | 3 | \$1,531 | \$1,478 | 4 |
| Fee revenues | 1 | 1 | 0 | 2 | 2 | 0 |
| Total revenues | 772 | 746 | 3 | 1,533 | 1,480 | 4 |
| Loss and loss expenses from: | | | | | | |
| Current accident year before catastrophe losses | 429 | 437 | (2) | 897 | 886 | 1 |
| Current accident year catastrophe losses | 129 | 43 | 200 | 159 | 82 | 94 |
| Prior accident years before catastrophe losses | (57) | (63) | 10 | (81) | (68) | (19) |
| Prior accident years catastrophe losses | (1) | — | nm | (6) | (9) | 33 |
| Loss and loss expenses | 500 | 417 | 20 | 969 | 891 | 9 |
| Underwriting expenses | 246 | 232 | 6 | 488 | 466 | 5 |
| Underwriting profit | \$26 | \$97 | (73) | \$76 | \$123 | (38) |
| Ratios as a percent of earned premiums: | | | Pt. Change | | | Pt. Change |
| Current accident year before catastrophe losses | 55.7 % | 58.7 % | (3.0) | 58.6 % | 59.9 % | (1.3) |
| Current accident year catastrophe losses | 16.8 | 5.8 | 11.0 | 10.4 | 5.6 | 4.8 |
| Prior accident years before catastrophe losses | (7.4) | (8.6) | 1.2 | (5.3) | (4.6) | (0.7) |
| Prior accident years catastrophe losses | (0.2) | 0.1 | (0.3) | (0.4) | (0.6) | 0.2 |
| Loss and loss expenses | 64.9 | 56.0 | 8.9 | 63.3 | 60.3 | 3.0 |
| Underwriting expenses | 31.9 | 31.2 | 0.7 | 31.9 | 31.6 | 0.3 |
| Combined ratio | 96.8 % | 87.2 % | 9.6 | 95.2 % | 91.9 % | 3.3 |
| Combined ratio | 96.8 % | 87.2 % | 9.6 | 95.2 % | 91.9 % | 3.3 |
| Contribution from catastrophe losses and prior years reserve development | 9.2 | (2.7) | 11.9 | 4.7 | 0.4 | 4.3 |
| Combined ratio before catastrophe losses and prior years reserve development | 87.6 % | 89.9 % | (2.3) | 90.5 % | 91.5 % | (1.0) |

Overview

Performance highlights for the commercial lines segment include:

Premiums – Earned premiums and net written premiums for the commercial lines segment grew during the second quarter and first half of 2016, primarily due to renewal premium growth that continued to reflect price increases and a higher level of insured exposures. Higher new business written premiums for the first six months of 2016 also contributed to growth. The table below analyzes the primary components of premiums. We continue using predictive analytics tools to improve pricing precision and segmentation while also leveraging our local relationships with agents through the efforts of our teams that work closely with them. We seek to maintain appropriate pricing discipline for both new and renewal business as our agents and underwriters assess account quality to make careful decisions on a case-by-case basis whether to write or renew a policy.

Agency renewal written premiums rose 3 percent for both the three and six months ended June 30, 2016, reflecting price increases and improving economic conditions. During the second quarter of 2016, our overall standard commercial lines policies continued to average estimated renewal price increases at percentages in the low-single-digit range, similar to the first quarter of 2016. We continue to segment commercial lines policies, emphasizing identification and retention of policies we believe have relatively stronger pricing. Conversely, we have been seeking

stricter renewal terms and conditions on policies we believe have relatively weaker pricing, in turn retaining fewer of those policies. As a result, the average change in commercial lines renewal pricing was somewhat lower than in 2015. We measure average changes in commercial lines renewal pricing as the percentage rate of change in renewal premium for the new policy period compared with the premium for the expiring policy period, assuming no change in the level of insured exposures or policy coverage between those periods for the respective policies.

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Our average overall commercial lines renewal pricing change includes the impact of flat pricing of certain coverages within package policies written for a three-year term that were in force but did not expire during the period being measured. Therefore, the change in average commercial lines renewal pricing we report reflects a blend of three-year policies that did not expire and other policies that did expire during the measurement period. For commercial lines policies that did expire and were then renewed during the second quarter of 2016, we estimate that our average percentage price increase for both commercial auto and commercial property lines were in the mid-single-digit range. The estimated average percentage price change for our commercial casualty line of business was an increase in the low-single-digit range, and for workers' compensation it was a decrease in the low-single-digit range.

Renewal premiums for our commercial casualty and workers' compensation lines include the results of policy audits that adjust initial premium amounts based on differences between estimated and actual sales or payroll related to a specific policy. Audits completed during the second quarter and first six months of 2016 contributed \$20 million and \$41 million to net written premiums, respectively. Audits contributed less than \$1 million of the \$10 million net increase in net written premiums for the second quarter of 2016 and \$4 million of the \$54 million net increase in net written premiums for the first six months of 2016, compared with the same periods a year ago. The \$53 million increase in earned premiums during the first six months of 2016, compared with 2015, included an increase from audit premiums of \$1 million.

New business written premiums for commercial lines increased less than \$1 million and \$8 million during the second quarter and first six months of 2016, compared with the same periods of 2015. During the first six months of 2016, new business written premiums grew for each major line of business in our commercial lines segment except for commercial auto, which decreased by less than 1 percent. Trend analysis for year-over-year comparisons of individual quarters are more difficult to assess for commercial lines new business written premiums, due to inherent variability. That variability is often driven by larger policies with annual premiums greater than \$100,000.

Other written premiums include premiums ceded to reinsurers as part of our reinsurance ceded program. A decrease in ceded premiums contributed \$2 million to net written premium growth for the first six months of 2016, compared with the same period of 2015, while second-quarter 2016 ceded premiums essentially matched the same quarter of 2015.

Commercial Lines Insurance Premiums

| (Dollars in millions) | Three months ended June 30, | | | Six months ended June 30, | | |
|--------------------------------------|--------------------------------|-------|-------------|---------------------------|---------|-------------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Agency renewal written premiums | \$718 | \$699 | 3 | \$1,476 | \$1,429 | 3 |
| Agency new business written premiums | 93 | 93 | 0 | 180 | 172 | 5 |
| Other written premiums | (14) | (5) | (180) | (32) | (31) | (3) |
| Net written premiums | 797 | 787 | 1 | 1,624 | 1,570 | 3 |
| Unearned premium change | (26) | (42) | (38) | (93) | (92) | (1) |
| Earned premiums | \$771 | \$745 | 3 | \$1,531 | \$1,478 | 4 |

Combined ratio – The commercial lines combined ratio rose for the three and six months ended June 30, 2016, compared with the same periods last year, largely due to weather-related natural catastrophe losses and loss expenses that were 10.7 and 5.0 percentage points higher, respectively.

Catastrophe losses and loss expenses accounted for 16.6 and 10.0 percentage points of the combined ratio for the second quarter and first six months of 2016, compared with 5.9 and 5.0 percentage points for the same periods a year ago. The 10-year annual average for that catastrophe measure through 2015 for the commercial lines segment was 4.4 percentage points, and the five-year annual average was 5.6 percentage points.

The net effect of reserve development on prior accident years during the second quarter and first six months of 2016 was favorable for commercial lines overall by \$58 million and \$87 million compared with \$63 million and \$77

million for the same periods in 2015. For the six months ended June 30, 2016, our workers' compensation line of business was the largest contributor to the total commercial lines net favorable reserve development on prior accident years, followed by our commercial casualty line of business and other commercial lines, which was largely attributable to director and officer liability insurance. Those contributions were partially offset by unfavorable development for our commercial auto line of business. The net favorable reserve development recognized during the first six months of 2016 for our commercial lines segment was distributed mainly between

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accident years 2015 and 2014, and was primarily due to lower-than-anticipated loss emergence on known claims. Reserve estimates are inherently uncertain as described in our 2015 Annual Report on Form 10-K, Item 7, Critical Accounting Estimates, Property Casualty Insurance Loss and Loss Expense Reserves, Page 46.

The commercial lines underwriting expense ratio increased 0.7 and 0.3 percentage points for the second quarter and first six months of 2016, compared with the same periods of 2015. Strategic investments that include enhancement of underwriting expertise offset the favorable effects of higher earned premiums and ongoing expense management efforts.

Underwriting results and related measures for the combined ratio are summarized in the first table of Commercial Lines Insurance Results. The tables and discussion below provide additional details for certain primary drivers of underwriting results.

Commercial Lines Insurance Losses Incurred by Size

| (Dollars in millions, net of reinsurance) | Three months ended June 30, | | | Six months ended June 30, | | |
|---|-----------------------------|--------|------------|---------------------------|--------|------------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Current accident year losses greater than \$5,000,000 | \$23 | \$5 | 360 | \$23 | \$17 | 35 |
| Current accident year losses \$1,000,000-\$5,000,000 | 33 | 14 | 136 | 69 | 38 | 82 |
| Large loss prior accident year reserve development | 4 | (4) | nm | 3 | 11 | (73) |
| Total large losses incurred | 60 | 15 | 300 | 95 | 66 | 44 |
| Losses incurred but not reported | 2 | 17 | (88) | 66 | 48 | 38 |
| Other losses excluding catastrophe losses | 244 | 274 | (11) | 499 | 546 | (9) |
| Catastrophe losses | 126 | 43 | 193 | 151 | 72 | 110 |
| Total losses incurred | \$432 | \$349 | 24 | \$811 | \$732 | 11 |
| Ratios as a percent of earned premiums: | | | Pt. Change | | | Pt. Change |
| Current accident year losses greater than \$5,000,000 | 2.9 | % 0.7 | % 2.2 | 1.5 | % 1.2 | % 0.3 |
| Current accident year losses \$1,000,000-\$5,000,000 | 4.2 | 1.7 | 2.5 | 4.5 | 2.6 | 1.9 |
| Large loss prior accident year reserve development | 0.6 | (0.5) | 1.1 | 0.2 | 0.7 | (0.5) |
| Total large loss ratio | 7.7 | 1.9 | 5.8 | 6.2 | 4.5 | 1.7 |
| Losses incurred but not reported | 0.3 | 2.2 | (1.9) | 4.3 | 3.2 | 1.1 |
| Other losses excluding catastrophe losses | 31.6 | 37.0 | (5.4) | 32.6 | 37.0 | (4.4) |
| Catastrophe losses | 16.4 | 5.8 | 10.6 | 9.9 | 4.9 | 5.0 |
| Total loss ratio | 56.0 | % 46.9 | % 9.1 | 53.0 | % 49.6 | % 3.4 |

We continue to monitor new losses and case reserve increases greater than \$1 million for trends in factors such as initial reserve levels, loss cost inflation and claim settlement expenses. Our analysis continues to indicate no unexpected concentration of these large losses and case reserve increases by risk category, geographic region, policy inception, agency or field marketing territory. The second-quarter 2016 commercial lines total large losses incurred of \$60 million, net of reinsurance, were higher than both the quarterly average of \$42 million during 2015 and the \$15 million total large losses incurred for the second quarter of 2015. The ratio for these large losses was 5.8 percentage

points higher compared with last year's second-quarter ratio. The second-quarter 2016 amount of total large losses incurred helped contribute to the increase in the six-month 2016 total large loss ratio, compared with 2015, offsetting a first-quarter 2016 ratio that was 2.3 points lower than the first quarter of 2015. We believe results for the three- and six-month periods largely reflected normal fluctuations in loss patterns and normal variability in large case reserves for claims above \$1 million.

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Commercial Lines of Business Analysis

Approximately 95 percent of our commercial lines premiums relate to accounts with coverages from more than one of our business lines. As a result, we believe that our commercial lines business is best measured and evaluated on a segment basis. However, we provide line-of-business data to summarize premium and loss trends separately for each line. The ratios shown in the table below are components of loss and loss expenses as a percentage of earned premiums.

| (Dollars in millions) | Three months ended June 30, | | | Six months ended June 30, | | |
|---|-----------------------------|--------|----------|---------------------------|--------|----------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Commercial casualty: | | | | | | |
| Written premiums | \$278 | \$274 | 1 | \$563 | \$540 | 4 |
| Earned premiums | 263 | 252 | 4 | 520 | 496 | 5 |
| Current accident year before catastrophe losses | 58.7 % | 59.6 % | | 59.5 % | 59.4 % | |
| Current accident year catastrophe losses | — | — | | — | — | |
| Prior accident years before catastrophe losses | (7.5) | (9.1) | | (4.4) | (4.1) | |
| Prior accident years catastrophe losses | — | — | | — | — | |
| Total loss and loss expenses ratio | 51.2 % | 50.5 % | | 55.1 % | 55.3 % | |
| Commercial property: | | | | | | |
| Written premiums | \$223 | \$218 | 2 | \$448 | \$424 | 6 |
| Earned premiums | 215 | 203 | 6 | 429 | 399 | 8 |
| Current accident year before catastrophe losses | 36.3 % | 42.1 % | | 43.8 % | 47.8 % | |
| Current accident year catastrophe losses | 57.6 | 19.6 | | 35.7 | 18.2 | |
| Prior accident years before catastrophe losses | (5.4) | (2.0) | | (3.6) | (2.0) | |
| Prior accident years catastrophe losses | (1.0) | 0.1 | | (1.6) | (1.8) | |
| Total loss and loss expenses ratio | 87.5 % | 59.8 % | | 74.3 % | 62.2 % | |
| Commercial auto: | | | | | | |
| Written premiums | \$156 | \$149 | 5 | \$314 | \$298 | 5 |
| Earned premiums | 147 | 139 | 6 | 291 | 275 | 6 |
| Current accident year before catastrophe losses | 76.3 % | 75.8 % | | 76.9 % | 74.1 % | |
| Current accident year catastrophe losses | 2.2 | 1.3 | | 1.4 | 0.7 | |
| Prior accident years before catastrophe losses | 9.1 | 8.3 | | 7.4 | 8.4 | |
| Prior accident years catastrophe losses | — | (0.2) | | (0.1) | (0.2) | |
| Total loss and loss expenses ratio | 87.6 % | 85.2 % | | 85.6 % | 83.0 % | |
| Workers' compensation: | | | | | | |
| Written premiums | \$86 | \$89 | (3) | \$191 | \$193 | (1) |
| Earned premiums | 89 | 90 | (1) | 178 | 183 | (3) |
| Current accident year before catastrophe losses | 70.9 % | 77.6 % | | 72.2 % | 74.5 % | |
| Current accident year catastrophe losses | — | — | | — | — | |
| Prior accident years before catastrophe losses | (25.5) | (44.8) | | (20.1) | (30.3) | |
| Prior accident years catastrophe losses | — | — | | — | — | |
| Total loss and loss expenses ratio | 45.4 % | 32.8 % | | 52.1 % | 44.2 % | |
| Other commercial lines: | | | | | | |
| Written premiums | \$54 | \$55 | (2) | \$108 | \$113 | (4) |
| Earned premiums | 57 | 61 | (7) | 113 | 125 | (10) |
| Current accident year before catastrophe losses | 37.8 % | 42.7 % | | 42.1 % | 48.6 % | |
| Current accident year catastrophe losses | 3.8 | 3.4 | | 2.2 | 6.6 | |
| Prior accident years before catastrophe losses | (28.2) | (13.6) | | (25.5) | (6.7) | |
| Prior accident years catastrophe losses | 1.3 | 1.2 | | 0.7 | (0.7) | |

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Total loss and loss expenses ratio 14.7 % 33.7 % 19.5 % 47.8 %

As discussed above, the loss and loss expenses ratio component of the combined ratio is an important measure of underwriting profit and performance. Catastrophe losses are volatile and can distort short-term profitability trends, particularly for certain lines of business. Development of loss and loss expense reserves on prior accident years can also distort trends in measures of profitability for recently written business. To illustrate these effects,

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we separate their impact on the ratios shown in the table above. For the six months ended June 30, 2016, the commercial line of business with the most significant profitability challenge was commercial auto. For the first six months of 2016, our commercial auto policies experienced average renewal price percentage increases in the mid-single-digit range, which we believe will help improve profitability in future quarters. We further discuss current initiatives for commercial auto in the Highlights of Our Strategy and Supporting Initiatives section of this quarterly report and in our 2015 Annual Report on Form 10-K, Item 7, Commercial Lines of Business Analysis, Page 67.

PERSONAL LINES INSURANCE RESULTS

| (Dollars in millions) | Three months ended June 30, | | | Six months ended June 30, | | |
|--|-----------------------------|---------|------------|---------------------------|---------|------------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Earned premiums | \$288 | \$272 | 6 | \$571 | \$540 | 6 |
| Fee revenues | 1 | — | nm | 2 | 1 | 100 |
| Total revenues | 289 | 272 | 6 | 573 | 541 | 6 |
| Loss and loss expenses from: | | | | | | |
| Current accident year before catastrophe losses | 180 | 179 | 1 | 360 | 358 | 1 |
| Current accident year catastrophe losses | 34 | 35 | (3) | 45 | 50 | (10) |
| Prior accident years before catastrophe losses | 9 | 2 | 350 | (7) | 1 | (800) |
| Prior accident years catastrophe losses | 1 | — | nm | (1) | (2) | 50 |
| Loss and loss expenses | 224 | 216 | 4 | 397 | 407 | (2) |
| Underwriting expenses | 85 | 81 | 5 | 168 | 162 | 4 |
| Underwriting profit (loss) | \$(20) | \$(25) | (20) | \$8 | \$(28) | nm |
| Ratios as a percent of earned premiums: | | | Pt. Change | | | Pt. Change |
| Current accident year before catastrophe losses | 62.5 % | 65.9 % | (3.4) | 63.0 % | 66.3 % | (3.3) |
| Current accident year catastrophe losses | 12.1 | 12.8 | (0.7) | 7.9 | 9.2 | (1.3) |
| Prior accident years before catastrophe losses | 3.1 | 1.1 | 2.0 | (1.2) | 0.2 | (1.4) |
| Prior accident years catastrophe losses | 0.3 | (0.2) | 0.5 | (0.2) | (0.4) | 0.2 |
| Loss and loss expenses | 78.0 | 79.6 | (1.6) | 69.5 | 75.3 | (5.8) |
| Underwriting expenses | 29.5 | 29.6 | (0.1) | 29.4 | 30.0 | (0.6) |
| Combined ratio | 107.5% | 109.2 % | (1.7) | 98.9 % | 105.3 % | (6.4) |
| Combined ratio | 107.5% | 109.2 % | (1.7) | 98.9 % | 105.3 % | (6.4) |
| Contribution from catastrophe losses and prior years reserve development | 15.5 | 13.7 | 1.8 | 6.5 | 9.0 | (2.5) |
| Combined ratio before catastrophe losses and prior years reserve development | 92.0 % | 95.5 % | (3.5) | 92.4 % | 96.3 % | (3.9) |

Overview

Performance highlights for the personal lines segment include:

Premiums – Personal lines earned premiums and net written premiums for the second quarter and first six months of 2016 continued to grow, primarily due to rising renewal written premiums. Price increases and a high level of policy retention contributed to premium growth. The table below analyzes the primary components of premiums.

Agency renewal written premiums increased 6 percent for both the second quarter and first six months of 2016, largely reflecting rate increases. We estimate that premium rates for our personal auto line of business increased at average percentages near the low end of the high-single-digit range during the first six months of 2016, with the

second-quarter 2016 average increase higher than in the first quarter of 2016. For our homeowner line of business, we estimate that rate increases for the first six months of 2016 averaged a percentage in the mid-single-digit range. For both our personal auto and homeowner lines of business, some individual policies experienced lower or higher rate changes based on each risk's specific characteristics and enhanced pricing precision enabled by predictive models. Personal lines new business written premiums grew 13 percent and 9 percent during the second quarter and first six months of 2016, compared with the same periods of 2015. Nearly all of that growth came from high net

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worth clients of our agencies. First-half 2016 personal lines new business written premiums from high net worth policies totaled approximately \$14 million.

Other written premiums include premiums ceded to reinsurers as part of our reinsurance ceded program. A decrease in ceded premiums contributed less than \$1 million to net written premium growth for both the second quarter and first six months of 2016, compared with the same periods of 2015.

We continue to implement strategies discussed in our 2015 Annual Report on Form 10-K, Item 1, Strategic Initiatives, Page 12, to enhance our responsiveness to marketplace changes and to help achieve our long-term objectives for personal lines growth and profitability. These strategies include initiatives to more profitably underwrite personal auto policies.

Personal Lines Insurance Premiums

| (Dollars in millions) | Three months ended June 30, | | | Six months ended June 30, | | |
|--------------------------------------|--------------------------------|-------|-------------|------------------------------|-------|-------------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Agency renewal written premiums | \$302 | \$285 | 6 | \$538 | \$508 | 6 |
| Agency new business written premiums | 34 | 30 | 13 | 59 | 54 | 9 |
| Other written premiums | (6) | (6) | 0 | (11) | (12) | 8 |
| Net written premiums | 330 | 309 | 7 | 586 | 550 | 7 |
| Unearned premium change | (42) | (37) | (14) | (15) | (10) | (50) |
| Earned premiums | \$288 | \$272 | 6 | \$571 | \$540 | 6 |

Combined ratio – Our personal lines combined ratio improved by 1.7 and 6.4 percentage points for the three and six months ended June 30, 2016, compared with the same periods of 2015, including 0.2 and 1.1 points from lower weather-related natural catastrophe losses and loss expenses.

In addition to the average rate increases discussed above, we continue to refine our pricing to better match premiums to the risk of loss on individual policies. The results of improved pricing precision and broad-based rate increases are expected to help position the combined ratio at a profitable level over the long term. In addition, greater geographic diversification is expected to reduce the volatility of homeowner loss ratios attributable to weather-related catastrophe losses over time.

Catastrophe losses and loss expenses accounted for 12.4 and 7.7 percentage points of the combined ratio for the three and six months ended June 30, 2016, compared with 12.6 and 8.8 percentage points for the same periods of 2015.

The 10-year annual average catastrophe loss ratio through 2015 for the personal lines segment was 10.9 percentage points, and the five-year annual average was 11.4 percentage points.

Personal lines net reserve development on prior accident years netted to an unfavorable \$10 million for the second quarter but a favorable \$8 million for the first six months of 2016. In the first six months of 2016, our homeowner and other personal lines of business developed favorably, largely for accident year 2015, while our personal auto line of business developed unfavorably for several accident years prior to 2015. The six-month personal lines total reserve development was \$7 million more favorable than the same period of 2015 and included a first-quarter 2016 refinement to reserves for loss expenses. The refinement transferred approximately \$10 million of reserves for loss expenses, primarily for our personal auto line of business, to various lines of business in our commercial lines segment. For losses only, our six-month 2016 personal auto prior accident year net reserve development was unfavorable by \$14 million. In the first six months of 2016, our personal lines segment net favorable reserve development was attributable primarily to accident year 2015. Reserve estimates are inherently uncertain as described in our 2015 Annual Report on Form 10-K, Item 7, Critical Accounting Estimates, Property Casualty Insurance Loss and Loss Expense Reserves, Page 46.

The underwriting expense ratio decreased 0.1 percentage points for the second quarter and 0.6 percentage points for first six months of 2016, compared with the same periods of 2015. The decreases reflect an unusually high ratio for

the 2015 periods from changes in estimates related to allocations of deferred acquisition costs by segment. That effect also offset the effect of strategic investments that include enhancement of underwriting expertise.

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Personal Lines Insurance Losses Incurred by Size

| (Dollars in millions, net of reinsurance) | Three months ended June 30, | | | Six months ended June 30, | | |
|---|-----------------------------|--------|------------|---------------------------|--------|------------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Current accident year losses greater than \$5,000,000 | \$— | \$— | nm | \$— | \$— | nm |
| Current accident year losses \$1,000,000-\$5,000,000 | — | 10 | (100) | 6 | 22 | (73) |
| Large loss prior accident year reserve development | (2) | — | nm | (1) | — | nm |
| Total large losses incurred | (2) | 10 | nm | 5 | 22 | (77) |
| Losses incurred but not reported | 23 | 14 | 64 | 34 | 21 | 62 |
| Other losses excluding catastrophe losses | 141 | 136 | 4 | 274 | 270 | 1 |
| Catastrophe losses | 35 | 34 | 3 | 43 | 47 | (9) |
| Total losses incurred | \$197 | \$194 | 2 | \$356 | \$360 | (1) |
| Ratios as a percent of earned premiums: | | | | | | |
| | | | Pt. Change | | | Pt. Change |
| Current accident year losses greater than \$5,000,000 | — % | — % | 0.0 | — % | — % | 0.0 |
| Current accident year losses \$1,000,000-\$5,000,000 | — | 3.5 | (3.5) | 1.0 | 4.1 | (3.1) |
| Large loss prior accident year reserve development | (0.7) | 0.1 | (0.8) | (0.1) | — | (0.1) |
| Total large loss ratio | (0.7) | 3.6 | (4.3) | 0.9 | 4.1 | (3.2) |
| Losses incurred but not reported | 8.1 | 5.1 | 3.0 | 6.0 | 3.9 | 2.1 |
| Other losses excluding catastrophe losses | 48.9 | 50.0 | (1.1) | 47.9 | 49.8 | (1.9) |
| Catastrophe losses | 12.2 | 12.5 | (0.3) | 7.6 | 8.7 | (1.1) |
| Total loss ratio | 68.5 % | 71.2 % | (2.7) | 62.4 % | 66.5 % | (4.1) |

We continue to monitor new losses and case reserve increases greater than \$1 million for trends in factors such as initial reserve levels, loss cost inflation and claim settlement expenses. Our analysis continues to indicate no unexpected concentration of these large losses and case reserve increases by risk category, geographic region, policy inception, agency or field marketing territory. In the second quarter of 2016, the personal lines total large loss ratio, net of reinsurance, was 4.3 percentage points lower than last year's second quarter. The second-quarter 2016 amount of total large losses incurred helped contribute to the decrease in the six-month 2016 total large loss ratio, compared with 2015, in addition to a first-quarter 2016 ratio that was 2.1 points lower than the first quarter of 2015. We believe results for the three- and six-month periods largely reflected normal fluctuations in loss patterns and normal variability in large case reserves for claims above \$1 million.

Personal Lines of Business Analysis

We prefer to write personal lines coverages on an account basis, including auto and homeowner coverages as well as coverages from the other personal business line. As a result, we believe that our personal lines business is best measured and evaluated on a segment basis. However, we provide line of business data to summarize premium and loss trends separately for each line. The ratios shown in the table below are components of loss and loss expenses as a percentage of earned premiums.

| (Dollars in millions) | Three months ended June 30, | | | Six months ended June 30, | | |
|---|-----------------------------|--------|----------|---------------------------|--------|----------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Personal auto: | | | | | | |
| Written premiums | \$ 154 | \$ 142 | 8 | \$ 277 | \$ 256 | 8 |
| Earned premiums | 135 | 125 | 8 | 266 | 248 | 7 |
| Current accident year before catastrophe losses | 79.5 % | 79.7 % | | 79.3 % | 80.8 % | |
| Current accident year catastrophe losses | 1.9 | 2.3 | | 1.4 | 1.2 | |
| Prior accident years before catastrophe losses | 10.6 | 5.8 | | 2.3 | 4.4 | |
| Prior accident years catastrophe losses | (0.1) | (0.1) | | (0.2) | (0.3) | |
| Total loss and loss expenses ratio | 91.9 % | 87.7 % | | 82.8 % | 86.1 % | |
| Homeowner: | | | | | | |
| Written premiums | \$ 140 | \$ 132 | 6 | \$ 243 | \$ 230 | 6 |
| Earned premiums | 121 | 114 | 6 | 240 | 228 | 5 |
| Current accident year before catastrophe losses | 49.1 % | 52.9 % | | 50.3 % | 54.1 % | |
| Current accident year catastrophe losses | 25.4 | 25.6 | | 16.0 | 19.0 | |
| Prior accident years before catastrophe losses | (0.8) | (2.4) | | (3.0) | (3.7) | |
| Prior accident years catastrophe losses | 0.8 | (0.3) | | (0.4) | (0.7) | |
| Total loss and loss expenses ratio | 74.5 % | 75.8 % | | 62.9 % | 68.7 % | |
| Other personal: | | | | | | |
| Written premiums | \$ 36 | \$ 35 | 3 | \$ 66 | \$ 64 | 3 |
| Earned premiums | 32 | 33 | (3) | 65 | 64 | 2 |
| Current accident year before catastrophe losses | 42.0 % | 58.2 % | | 43.1 % | 53.9 % | |
| Current accident year catastrophe losses | 4.7 | 8.4 | | 5.2 | 5.6 | |
| Prior accident years before catastrophe losses | (13.5) | (4.9) | | (9.0) | (1.9) | |
| Prior accident years catastrophe losses | 0.0 | 0.0 | | 0.1 | (0.4) | |
| Total loss and loss expenses ratio | 33.2 % | 61.7 % | | 39.4 % | 57.2 % | |

As discussed above, the loss and loss expenses ratio component of the combined ratio is an important measure of underwriting profit and performance. Catastrophe losses are volatile and can distort short-term profitability trends, particularly for certain lines of business. Development of loss and loss expense reserves on prior accident years can also distort trends in measures of profitability for recently written business. To illustrate these effects, we separate their impact on the ratios shown in the table above. For the six months ended June 30, 2016, the line of business in our personal lines insurance segment with the most significant profitability challenge was personal auto. During the first six months of 2016, premium rate increases that allow for more pricing precision on our personal auto policies continued to be implemented at average percentages near the low end of the high-single-digit range. We continue to work toward greater pricing precision in addition to broad-based rate increases to help improve profitability over the long term.

EXCESS AND SURPLUS LINES INSURANCE RESULTS

| (Dollars in millions) | Three months ended June 30, | | | Six months ended June 30, | | |
|--|--------------------------------|--------|---------------|------------------------------|--------|---------------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Earned premiums | \$45 | \$42 | 7 | \$88 | \$82 | 7 |
| Fee revenues | — | 1 | (100) | — | 1 | (100) |
| Total revenues | 45 | 43 | 5 | 88 | 83 | 6 |
| Loss and loss expenses from: | | | | | | |
| Current accident year before catastrophe losses | 26 | 29 | (10) | 53 | 58 | (9) |
| Current accident year catastrophe losses | 2 | 1 | 100 | 2 | 1 | 100 |
| Prior accident years before catastrophe losses | (1) | (9) | 89 | (15) | (14) | (7) |
| Prior accident years catastrophe losses | — | — | nm | — | — | nm |
| Loss and loss expenses | 27 | 21 | 29 | 40 | 45 | (11) |
| Underwriting expenses | 13 | 11 | 18 | 26 | 23 | 13 |
| Underwriting profit | \$5 | \$11 | (55) | \$22 | \$15 | 47 |
| Ratios as a percent of earned premiums: | | | Pt. Change | | | Pt. Change |
| Current accident year before catastrophe losses | 56.7 % | 69.3 % | (12.6) | 59.8 % | 70.7 % | (10.9) |
| Current accident year catastrophe losses | 3.2 | 0.6 | 2.6 | 1.9 | 0.9 | 1.0 |
| Prior accident years before catastrophe losses | (1.9) | (20.2) | 18.3 | (16.4) | (17.0) | 0.6 |
| Prior accident years catastrophe losses | 0.0 | (0.1) | 0.1 | (0.1) | (0.2) | 0.1 |
| Loss and loss expenses | 58.0 | 49.6 | 8.4 | 45.2 | 54.4 | (9.2) |
| Underwriting expenses | 29.4 | 26.4 | 3.0 | 29.4 | 27.7 | 1.7 |
| Combined ratio | 87.4 % | 76.0 % | 11.4 | 74.6 % | 82.1 % | (7.5) |
| Combined ratio | 87.4 % | 76.0 % | 11.4 | 74.6 % | 82.1 % | (7.5) |
| Contribution from catastrophe losses and prior years reserve development | 1.3 | (19.7) | 21.0 | (14.6) | (16.3) | 1.7 |
| Combined ratio before catastrophe losses and prior years reserve development | 86.1 % | 95.7 % | (9.6) | 89.2 % | 98.4 % | (9.2) |

Overview

Performance highlights for the excess and surplus lines segment include:

• **Premiums** – Excess and surplus lines net written premiums continued to grow during the second quarter and first six months of 2016. Growth in renewal written premiums was the main contributor to the increase.

Renewal written premiums rose 9 percent and 11 percent for the three and six months ended June 30, 2016, compared with the same periods of 2015, reflecting the opportunity to renew many accounts for the first time, as well as higher renewal pricing. June 2016 marked the 70th consecutive month of positive average price changes for the excess and surplus lines segment of our property casualty business. For the second quarter and the first half of 2016, excess and surplus lines policy renewals experienced estimated average percentage price increases near the high end of the low-single-digit range. We measure average changes in excess and surplus lines renewal pricing as the percentage rate of change in renewal premium for the new policy period compared with the premium for the expiring policy period, assuming no change in the level of insured exposures or policy coverage between those periods for respective policies. New business written premiums produced by agencies rose modestly, by \$1 million, for both for the second quarter and first six months of 2016, compared with the same periods of 2015, reflecting careful underwriting in a highly competitive market. Some of what we report as new business came from accounts that were not new to our agents.

We believe our agents' seasoned accounts tend to be priced more accurately than business that may be less familiar to them.

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Excess and Surplus Lines Insurance Premiums

| (Dollars in millions) | Three months ended June 30, | | | Six months ended June 30, | | |
|--------------------------------------|--------------------------------|------|-------------|------------------------------|------|-------------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Agency renewal written premiums | \$37 | \$34 | 9 | \$71 | \$64 | 11 |
| Agency new business written premiums | 16 | 15 | 7 | 29 | 28 | 4 |
| Other written premiums | (2) | (3) | 33 | (4) | (4) | 0 |
| Net written premiums | 51 | 46 | 11 | 96 | 88 | 9 |
| Unearned premium change | (6) | (4) | (50) | (8) | (6) | (33) |
| Earned premiums | \$45 | \$42 | 7 | \$88 | \$82 | 7 |

Combined ratio – The excess and surplus lines combined ratio rose 11.4 percentage points for the second quarter 2016, compared with the same period of 2015, as a lower ratio for current accident year losses and loss expenses before catastrophe losses was offset by less favorable reserve development on prior accident years before catastrophe losses. For the first six months of 2016, the combined ratio improved by 7.5 percentage points, compared with the first six months of 2015, driven by lower ratios for current accident year losses and loss expenses before catastrophe losses. Catastrophe losses and loss expenses accounted for 3.2 and 1.8 percentage points of the combined ratio for the three and six months ended June 30, 2016, compared with 0.5 and 0.7 percentage points for the same periods of 2015. Excess and surplus lines net favorable reserve development on prior accident years as a ratio to earned premiums was 1.9 percent and 16.5 percent for the second quarter and first six months of 2016, compared with 20.3 percent and 17.2 percent for the same periods of 2015. The net favorable reserve development recognized during the first six months of 2016 was distributed almost evenly among accident years 2015, 2014 and 2013. It was due primarily to lower-than-anticipated loss emergence on known claims. Reserve estimates are inherently uncertain as described in our 2015 Annual Report on Form 10-K, Item 7, Critical Accounting Estimates, Property Casualty Insurance Loss and Loss Expense Reserves, Page 46.

The underwriting expense ratio for the second quarter and first six months of 2016 increased, compared with the same periods of 2015. Strategic investments that include enhancement of underwriting expertise offset the favorable effects of higher earned premiums and ongoing expense management efforts.

Excess and Surplus Lines Insurance Losses Incurred by Size

| (Dollars in millions, net of reinsurance) | Three months ended June 30, | | | Six months ended June 30, | | |
|---|--------------------------------|-------|---------------|------------------------------|-------|---------------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Current accident year losses greater than \$5,000,000 | \$— | \$— | nm | \$— | \$— | nm |
| Current accident year losses \$1,000,000-\$5,000,000 | 1 | — | nm | 1 | 1 | 0 |
| Large loss prior accident year reserve development | 1 | — | nm | 1 | — | nm |
| Total large losses incurred | 2 | — | nm | 2 | 1 | 100 |
| Losses incurred but not reported | 9 | 7 | 29 | 7 | 12 | (42) |
| Other losses excluding catastrophe losses | 5 | 7 | (29) | 14 | 19 | (26) |
| Catastrophe losses | 2 | 1 | 100 | 2 | 1 | 100 |
| Total losses incurred | \$18 | \$15 | 20 | \$25 | \$33 | (24) |
| Ratios as a percent of earned premiums: | | | Pt. Change | | | Pt. Change |
| Current accident year losses greater than \$5,000,000 | — % | — % | 0.0 | — % | — % | 0.0 |
| Current accident year losses \$1,000,000-\$5,000,000 | 2.2 | — | 2.2 | 1.1 | 1.2 | (0.1) |
| Large loss prior accident year reserve development | 1.7 | — | 1.7 | 0.7 | — | 0.7 |
| Total large loss ratio | 3.9 | — | 3.9 | 1.8 | 1.2 | 0.6 |
| Losses incurred but not reported | 20.3 | 18.3 | 2.0 | 7.8 | 15.1 | (7.3) |
| Other losses excluding catastrophe losses | 12.7 | 17.5 | (4.8) | 16.6 | 23.5 | (6.9) |
| Catastrophe losses | 3.1 | 0.4 | 2.7 | 1.7 | 0.6 | 1.1 |
| Total loss ratio | 40.0% | 36.2% | 3.8 | 27.9% | 40.4% | (12.5) |

We continue to monitor new losses and case reserve increases greater than \$1 million for trends in factors such as initial reserve levels, loss cost inflation and claim settlement expenses. Our analysis continues to indicate no unexpected concentration of these large losses and case reserve increases by risk category, geographic region, policy inception, agency or field marketing territory. In the second quarter of 2016, the excess and surplus lines total ratio for large losses, net of reinsurance, was 3.9 percentage points higher compared with last year's second quarter. The second-quarter 2016 amount of total large losses incurred helped contribute to the increase in the six-month 2016 total large loss ratio, compared with 2015, offsetting a first-quarter 2016 ratio that was 2.9 points lower than the first quarter of 2015. We believe results for the three- and six-month periods largely reflected normal fluctuations in loss patterns and normal variability in large case reserves for claims above \$1 million.

LIFE INSURANCE RESULTS

| (Dollars in millions) | Three months ended June 30, | | | Six months ended June 30, | | |
|---|--------------------------------|-------|----------|------------------------------|--------|----------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Earned premiums | \$59 | \$52 | 13 | \$117 | \$105 | 11 |
| Separate account investment management fees | 1 | 1 | 0 | 2 | 2 | 0 |
| Total revenues | 60 | 53 | 13 | 119 | 107 | 11 |
| Contract holders' benefits incurred | 62 | 58 | 7 | 125 | 118 | 6 |
| Investment interest credited to contract holders' | (22) | (22) | 0 | (44) | (43) | (2) |
| Underwriting expenses incurred | 19 | 16 | 19 | 38 | 34 | 12 |
| Total benefits and expenses | 59 | 52 | 13 | 119 | 109 | 9 |
| Life insurance segment income (loss) | \$1 | \$1 | 0 | \$— | \$(2) | 100 |

Overview

Performance highlights for the life insurance segment include:

Revenues – Revenues increased for the six months ended June 30, 2016, primarily due to higher earned premiums from term insurance products.

Net in-force life insurance policy face amounts increased to \$54.664 billion at June 30, 2016, from \$52.735 billion at year-end 2015.

Fixed annuity deposits received for the three and six months ended June 30, 2016, were \$14 million and \$26 million compared with \$9 million and \$17 million for same periods of 2015. Fixed annuity deposits have a minimal impact to earned premiums because deposits received are initially recorded as liabilities. Profit is earned over time by way of interest-rate spreads. We do not write variable or equity-indexed annuities.

Life Insurance Premiums

| (Dollars in millions) | Three months ended June 30, | | | Six months ended June 30, | | |
|---|--------------------------------|------|----------|------------------------------|-------|----------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Term life insurance | \$38 | \$35 | 9 | \$75 | \$69 | 9 |
| Universal life insurance | 10 | 9 | 11 | 21 | 19 | 11 |
| Other life insurance, annuity and disability income products | 11 | 8 | 38 | 21 | 17 | 24 |
| Net earned premiums | \$59 | \$52 | 13 | \$117 | \$105 | 11 |

Profitability – Our life insurance segment typically reports a small profit or loss on a GAAP basis because profits from investment income spreads are included in our investment segment results. We include only investment income credited to contract holders (including interest assumed in life insurance policy reserve calculations) in our life insurance segment results. A gain of less than \$1 million for our life insurance segment in the first six months of 2016, compared with a loss of \$2 million for the same period of 2015, was largely due to increased premium revenues in 2016.

Life insurance segment benefits and expenses consist principally of contract holders' (policyholders') benefits incurred related to traditional life and interest-sensitive products and operating expenses incurred, net of deferred acquisition costs. Total benefits increased in the first six months of 2016. Mortality results increased from the same period of 2015 but were slightly less than our 2016 projections.

Operating expenses for the first six months of 2016 increased compared with the same period a year ago. For the first six months of 2016, unlocking of interest rate and other actuarial assumptions decreased the amount of expenses

deferred to future periods, increasing operating expenses. For the first six months of 2015, unlocking increased the amount of expenses deferred to future periods, decreasing operating expenses.

Pretax earnings for the first six months of 2016, and for the comparable period of 2015, were reduced by less than \$1 million due to unlocking of interest rates and other actuarial assumptions.

We recognize that assets under management, capital appreciation and investment income are integral to evaluating the success of the life insurance segment because of the long duration of life products. On a

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basis that includes investment income and realized gains or losses from life-insurance-related invested assets, the life insurance company reported a net profit of \$12 million and \$22 million in the three and six months ended June 30, 2016, compared with a net profit of \$11 million and \$20 million for the same periods of 2015. The life insurance company portfolio had net after-tax realized investment gains of less than \$1 million and \$1 million for the three and six months ended June 30, 2016, compared with \$1 million and \$2 million for the three and six months ended June 30, 2015.

INVESTMENTS RESULTS

Overview

The investments segment contributes investment income and realized gains and losses to results of operations. Investments traditionally are our primary source of pretax and after-tax profits.

Investment Income

Pretax investment income increased 6 percent and 5 percent for the three and six months ended June 30, 2016, compared with the same periods of 2015. Interest income rose due to net purchases of fixed-maturity securities that offset the continuing effects of the low interest rate environment. Higher dividend income reflected rising dividend rates and net purchases of equity securities.

Investments Results

| (Dollars in millions) | Three months ended June 30, | | | Six months ended June 30, | | |
|---|--------------------------------|-------|-------------|------------------------------|-------|-------------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Total investment income, net of expenses | \$149 | \$140 | 6 | \$294 | \$279 | 5 |
| Investment interest credited to contract holders' | (22) | (22) | 0 | (44) | (43) | (2) |
| Realized investment gains, net | 44 | 60 | (27) | 105 | 107 | (2) |
| Investments profit, pretax | \$171 | \$178 | (4) | \$355 | \$343 | 3 |

We continue to position our portfolio considering both the challenges presented by the current low interest rate environment and the risks presented by potential future inflation. As bonds in our generally laddered portfolio mature or are called over the near term, we will be challenged to replace their current yield. The table below shows the average pretax yield-to-amortized cost associated with expected principal redemptions for our fixed-maturity portfolio. The expected principal redemptions are based on par amounts and include dated maturities, calls and prefunded municipal bonds that we expect will be called during each respective time period.

| (Dollars in millions) | % Yield | Principal redemptions |
|---|---------|-----------------------|
| At June 30, 2016 | | |
| Fixed-maturity pretax yield profile: | | |
| Expected to mature during the remainder of 2016 | 4.23 % | \$ 294 |
| Expected to mature during 2017 | 4.79 | 645 |
| Expected to mature during 2018 | 5.77 | 1,011 |
| Average yield and total expected redemptions | 5.22 | \$ 1,950 |

from the remainder of
2016 through 2018

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The table below shows the average pretax yield-to-amortized cost for fixed-maturity securities acquired during the periods indicated. The average yield of 4.65 percent for the first six months of 2016 was lower than the 4.70 percent average yield-to-amortized cost of the fixed-maturity securities portfolio at the end of 2015.

| | Three months ended June 30, 2016 | | Six months ended June 30, 2015 | |
|---|---|-------|---|-------|
| Average pretax yield-to-amortized cost on new fixed-maturities: | | | | |
| Acquired taxable fixed-maturities | 4.30% | 4.48% | 4.50% | 4.42% |
| Acquired tax-exempt fixed-maturities | 2.96 | 3.43 | 3.01 | 3.34 |
| Average total fixed-maturities acquired | 4.03 | 3.93 | 4.08 | 3.90 |

While our bond portfolio more than covers our insurance reserve liabilities, we believe our diversified common stock portfolio of mainly blue chip, dividend-paying companies represents one of our best investment opportunities for the long term. In our 2015 Annual Report on Form 10-K, Item 1, Investments Segment, Page 21, and Item 7, Investments Outlook, Page 88, we discussed our portfolio strategies. We discuss risks related to our investment income and our fixed-maturity and equity investment portfolios in this quarterly report Item 3, Quantitative and Qualitative Disclosures About Market Risk.

The table below provides details about investment income. Average yields in this table are based on the average invested asset and cash amounts indicated in the table, using fixed-maturity securities valued at amortized cost and all other securities at fair value.

| (Dollars in millions) | Three months ended June 30, | | | Six months ended June 30, | | |
|--|-----------------------------|-----------|----------|---------------------------|-----------|----------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Investment income: | | | | | | |
| Interest | \$ 110 | \$ 106 | 4 | \$ 219 | \$ 211 | 4 |
| Dividends | 41 | 35 | 17 | 78 | 71 | 10 |
| Other | — | 1 | nm | 1 | 1 | 0 |
| Less investment expenses | 2 | 2 | 0 | 4 | 4 | 0 |
| Investment income, pretax | 149 | 140 | 6 | 294 | 279 | 5 |
| Less income taxes | 35 | 33 | 6 | 70 | 66 | 6 |
| Total investment income, after-tax | \$ 114 | \$ 107 | 7 | \$ 224 | \$ 213 | 5 |
| Investment returns: | | | | | | |
| Effective tax rate | 23.9 | % 23.9 | % | 23.8 | % 23.7 | % |
| Average invested assets plus cash and cash equivalents | \$ 15,223 | \$ 14,534 | | \$ 15,014 | \$ 14,488 | |
| Average yield pretax | 3.92 | % 3.85 | % | 3.92 | % 3.85 | % |
| Average yield after-tax | 3.00 | 2.94 | | 2.98 | 2.94 | |
| Fixed-maturity returns: | | | | | | |
| Effective tax rate | 27.3 | % 27.2 | % | 27.3 | % 27.1 | % |
| Average amortized cost | \$ 9,480 | \$ 9,143 | | \$ 9,421 | \$ 9,085 | |
| Average yield pretax | 4.64 | % 4.64 | % | 4.65 | % 4.65 | % |
| Average yield after-tax | 3.38 | 3.38 | | 3.38 | 3.39 | |

Net Realized Gains and Losses

We reported net realized investment gains of \$44 million and \$105 million for the three and six months ended June 30, 2016, compared with \$60 million and \$107 million for the same periods of 2015. The total net realized investment gains for the first six months of 2016 included \$99 million in net gains from sales of various common and preferred stock holdings, matching the same period of 2015.

Investment gains or losses are recognized upon the sales of investments or as otherwise required under GAAP. The timing of realized gains or losses from sales can have a material effect on results in any quarter. However, such gains or losses usually have little, if any, effect on total shareholders' equity because most equity and fixed-maturity investments are carried at fair value, with the unrealized gain or loss included as a component of accumulated other comprehensive income (AOCI). Accounting requirements for other-than-temporary impairment (OTTI) charges for the fixed-maturity portfolio are disclosed in our 2015 Annual Report on Form 10-K, Item 8, Note 1, Summary of Significant Accounting Policies, Page 123.

Of the 3,211 securities in the portfolio, no fixed-maturity or equity securities were trading below 70 percent of amortized cost at June 30, 2016. Our asset impairment committee regularly monitors the portfolio, including a quarterly review of the entire portfolio for potential OTTI charges. We believe that if the improving liquidity in the markets were to reverse or the economic recovery were to significantly stall, we could experience declines in portfolio values and possibly additional OTTI charges.

The table below provides additional detail for OTTI charges:

| (Dollars in millions) | Three months ended June 30, 2016 | Six months ended June 30, 2016 | Three months ended June 30, 2015 | Six months ended June 30, 2015 |
|------------------------|--|--|--|--|
| Fixed maturities: | | | | |
| Utilities | \$ — | \$ — | \$ 2 | \$ — |
| Basic industry | — 3 | — 3 | — 3 | — 3 |
| Total fixed maturities | — 3 | 2 3 | 2 3 | 2 3 |
| Common equities: | | | | |
| Financial | — 1 | — 1 | — 1 | — 1 |
| Total common equities | — 1 | — 1 | — 1 | — 1 |
| Total | \$ — 4 | \$ 2 4 | \$ 2 4 | \$ 2 4 |

OTHER

We report as Other the noninvestment operations of the parent company and a noninsurance subsidiary, CFC Investment Company. We also report as Other the underwriting results of Cincinnati Re, our reinsurance assumed operation, including earned premiums, loss and loss expenses and underwriting expenses.

Total revenues for the first six months of 2016 for our Other operations increased, compared with the same period of 2015, primarily due to earned premiums from Cincinnati Re. Total expenses for Other also increased for the first six months of 2016, primarily due to losses and loss expenses and underwriting expenses from Cincinnati Re.

Other loss in the table below represents losses before income taxes. The net result of Cincinnati Re for the first six months of 2016 was a small underwriting loss of less than \$1 million. For both periods shown, Other loss resulted largely from interest expense from debt of the parent company.

| (Dollars in millions) | Three months ended | | | Six months ended | | |
|---------------------------------------|--------------------|--------|-------------|------------------|--------|-------------|
| | June 30, | | % Change | June 30, | | % Change |
| | 2016 | 2015 | | 2016 | 2015 | |
| Interest and fees on loans and leases | \$1 | \$1 | 0 | \$2 | \$3 | (33) |
| Earned premiums | 10 | — | nm | 20 | — | nm |
| Other revenues | 1 | 1 | 0 | 1 | 1 | 0 |
| Total revenues | 12 | 2 | 500 | 23 | 4 | 475 |
| Interest expense | 13 | 13 | 0 | 26 | 26 | 0 |
| Loss and loss expenses | 8 | — | nm | 14 | — | nm |
| Underwriting expenses | 3 | — | nm | 6 | — | nm |
| Operating expenses | 5 | 3 | 67 | 7 | 7 | 0 |
| Total expenses | 29 | 16 | 81 | 53 | 33 | 61 |
| Other loss | \$(17) | \$(14) | (21) | \$(30) | \$(29) | 3 |

TAXES

We had \$43 million and \$120 million of income tax expense for the three and six months ended June 30, 2016, compared with \$72 million and \$118 million for the same periods of 2015. The effective tax rates for the three and six months ended June 30, 2016, were 25.9 percent and 27.8 percent compared with 29.0 percent and 28.0 percent for the same periods last year. The change in our effective tax rate was primarily due to changes in pretax income from underwriting results and realized investment gains and losses, with immaterial changes in the amount of permanent book-tax differences.

Historically, we have pursued a strategy of investing some portion of cash flow in tax-advantaged fixed-maturity and equity securities to minimize our overall tax liability and maximize after-tax earnings. See Tax-Exempt Fixed Maturities in this quarterly report Item 3, Quantitative and Qualitative Disclosures About Market Risk for further discussion on municipal bond purchases in our fixed-maturity investment portfolio. For our property casualty insurance subsidiaries, approximately 85 percent of interest from tax-advantaged fixed-maturity investments and approximately 60 percent of dividends from qualified equities are exempt from federal tax after applying proration from the 1986 Tax Reform Act. Our noninsurance companies own an immaterial amount of tax-advantaged fixed-maturity investments. For our noninsurance companies, the dividend received deduction exempts 70 percent of dividends from qualified equities. Our life insurance company does not own tax-advantaged fixed-maturity investments or equities subject to the dividend received deduction. Details about our effective tax rate are in this quarterly report Item 1, Note 9 – Income Taxes.

LIQUIDITY AND CAPITAL RESOURCES

At June 30, 2016, shareholders' equity was \$6.971 billion compared with \$6.427 billion at December 31, 2015. Total debt was \$814 million at June 30, 2016, \$7 million less than at December 31, 2015. At June 30, 2016, cash and cash equivalents totaled \$547 million compared with \$544 million at December 31, 2015.

SOURCES OF LIQUIDITY

Subsidiary Dividends

Our lead insurance subsidiary declared dividends of \$200 million to the parent company in the first six months of 2016, matching the same period of 2015. For full-year 2015, subsidiary dividends declared totaled \$447 million. State of Ohio regulatory requirements restrict the dividends our insurance subsidiary can pay. For full-year 2016, total dividends that our insurance subsidiary could pay to our parent company without regulatory approval are

approximately \$534 million.

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Investing Activities

Investment income is a source of liquidity for both the parent company and its insurance subsidiary. We continue to focus on portfolio strategies to balance near-term income generation and long-term book value growth.

Parent company obligations can be funded with income on investments held at the parent-company level or through sales of securities in that portfolio, although our investment philosophy seeks to compound cash flows over the long term. These sources of capital can help minimize subsidiary dividends to the parent company, protecting insurance subsidiary capital.

See our 2015 Annual Report on Form 10-K, Item 1, Investments Segment, Page 21, for a discussion of our historic investment strategy, portfolio allocation and quality.

Insurance Underwriting

Our property casualty and life insurance underwriting operations provide liquidity because we generally receive premiums before paying losses under the policies purchased with those premiums. After satisfying our cash requirements, we use excess cash flows for investment, increasing future investment income.

Historically, cash receipts from property casualty and life insurance premiums, along with investment income, have been more than sufficient to pay claims, operating expenses and dividends to the parent company.

The table below shows a summary of operating cash flow for property casualty insurance (direct method):

| (Dollars in millions) | Three months ended June 30, | | | Six months ended June 30, | | |
|--|-----------------------------|---------|----------|---------------------------|----------|----------|
| | 2016 | 2015 | % Change | 2016 | 2015 | % Change |
| Premiums collected | \$1,185 | \$1,119 | 6 | \$2,349 | \$2,206 | 6 |
| Loss and loss expenses paid | (629) | (598) | (5) | (1,191) | (1,144) | (4) |
| Commissions and other underwriting expenses paid | (321) | (302) | (6) | (763) | (715) | (7) |
| Cash flow from underwriting | 235 | 219 | 7 | 395 | 347 | 14 |
| Investment income received | 96 | 94 | 2 | 198 | 189 | 5 |
| Cash flow from operations | \$331 | \$313 | 6 | \$593 | \$536 | 11 |

Collected premiums for property casualty insurance rose \$143 million during the first six months of 2016, compared with the same period in 2015. Loss and loss expenses paid increased \$47 million, including a \$22 million increase for catastrophe losses and loss expenses. Commissions and other underwriting expenses paid rose \$48 million, primarily due to higher commissions paid to agencies, reflecting the increase in collected premiums.

We discuss our future obligations for claims payments and for underwriting expenses in our 2015 Annual Report on Form 10-K, Item 7, Contractual Obligations, Page 93, and Other Commitments also on Page 93.

Capital Resources

At June 30, 2016, our debt-to-total-capital ratio was 10.5 percent, with \$786 million in long-term debt and \$28 million in borrowing on our revolving short-term line of credit. That line of credit had a \$35 million balance at December 31, 2015. At June 30, 2016, \$197 million was available for future cash management needs. Based on our capital requirements at June 30, 2016, we do not anticipate a material increase in debt levels during the remainder of 2016. As a result, we expect changes in our debt-to-total-capital ratio to continue to be largely a function of the contribution of unrealized investment gains or losses to shareholders' equity.

We provide details of our three, long-term notes in this quarterly report Item 1, Note 3 – Fair Value Measurements. None of the notes are encumbered by rating triggers.

Four independent ratings firms award insurer financial strength ratings to our property casualty insurance companies and three firms rate our life insurance company. Those firms made no changes to our parent company debt ratings during the first six months of 2016. Our debt ratings are discussed in our 2015 Annual Report on Form 10-K, Item 7, Liquidity and Capital Resources, Other Sources of Liquidity, Page 91.

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Off-Balance Sheet Arrangements

We do not use any special-purpose financing vehicles or have any undisclosed off-balance sheet arrangements (as that term is defined in applicable SEC rules) that are reasonably likely to have a current or future material effect on the company's financial condition, results of operation, liquidity, capital expenditures or capital resources. Similarly, the company holds no fair-value contracts for which a lack of marketplace quotations would necessitate the use of fair-value techniques.

USES OF LIQUIDITY

Our parent company and insurance subsidiary have contractual obligations and other commitments. In addition, one of our primary uses of cash is to enhance shareholder return.

Contractual Obligations

In our 2015 Annual Report on Form 10-K, Item 7, Contractual Obligations, Page 93 we estimated our future contractual obligations as of December 31, 2015. There have been no material changes to our estimates of future contractual obligations since our 2015 Annual Report on Form 10-K.

Other Commitments

In addition to our contractual obligations, we have other property casualty operational commitments.

Commissions – Commissions paid were \$484 million in the first six months of 2016. Commission payments generally track with written premiums, except for annual profit-sharing commissions typically paid during the first quarter of the year.

Other underwriting expenses – Many of our underwriting expenses are not contractual obligations, but reflect the ongoing expenses of our business. Noncommission underwriting expenses paid were \$279 million in the first six months of 2016.

Technology costs – In addition to contractual obligations for hardware and software, we anticipate capitalizing up to \$6 million in spending for key technology initiatives in 2016. Capitalized development costs related to key technology initiatives were \$4 million in the first six months of 2016. These activities are conducted at our discretion, and we have no material contractual obligations for activities planned as part of these projects.

We contributed \$5 million to our qualified pension plan during the first six months of 2016. We also contributed \$8 million to our qualified pension plan during the third quarter of 2016 and do not anticipate further contributions during the remainder of 2016.

Investing Activities

After fulfilling operating requirements, we invest cash flows from underwriting, investment and other corporate activities in fixed-maturity and equity securities on an ongoing basis to help achieve our portfolio objectives.

We discuss our investment strategy and certain portfolio attributes in this quarterly report Item 3, Quantitative and Qualitative Disclosures About Market Risk.

Uses of Capital

Uses of cash to enhance shareholder return include dividends to shareholders. In January and May 2016, the board of directors declared a regular quarterly cash dividend of 48 cents per share for an indicated annual rate of \$1.92 per share. During the first six months of 2016, we used \$151 million to pay cash dividends to shareholders.

PROPERTY CASUALTY INSURANCE RESERVES

For the business lines in the commercial and personal lines insurance segments, and in total for the excess and surplus lines segment, the following table details gross reserves among case, IBNR (incurred but not reported) and loss expense reserves, net of salvage and subrogation reserves. Reserving practices are discussed in our 2015 Annual

Report on Form 10-K, Item 7, Property Casualty Insurance Loss and Loss Expense Obligations and Reserves, Page 94.

Total gross reserves at June 30, 2016, increased \$258 million compared with December 31, 2015. Case reserves for losses increased \$125 million, IBNR reserves increased by \$129 million and total loss expense reserves

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increased by \$4 million. Accounting for most of the total gross increase was the aggregate of our commercial property, commercial casualty and commercial auto lines of business.

Property Casualty Gross Reserves

| (Dollars in millions) | Loss reserves | | Loss expense reserves | Total gross reserves | Percent of total |
|-----------------------------|---------------|---------------|-----------------------|----------------------|------------------|
| | Case reserves | IBNR reserves | | | |
| At June 30, 2016 | | | | | |
| Commercial lines insurance: | | | | | |
| Commercial casualty | \$933 | \$499 | \$ 540 | \$ 1,972 | 40.1 % |
| Commercial property | 289 | 19 | 53 | 361 | 7.3 |
| Commercial auto | 346 | 97 | 96 | 539 | 11.0 |
| Workers' compensation | 379 | 559 | 92 | 1,030 | 20.9 |
| Other commercial | 122 | 17 | 80 | 219 | 4.5 |
| Subtotal | 2,069 | 1,191 | 861 | 4,121 | 83.8 |
| Personal lines insurance: | | | | | |
| Personal auto | 211 | 20 | 62 | 293 | 6.0 |
| Homeowner | 84 | 25 | 26 | 135 | 2.7 |
| Other personal | 47 | 48 | 5 | 100 | 2.0 |
| Subtotal | 342 | 93 | 93 | 528 | 10.7 |
| Excess and surplus lines | 92 | 87 | 61 | 240 | 4.9 |
| Cincinnati Re | 3 | 26 | — | 29 | 0.6 |
| Total | \$2,506 | \$1,397 | \$ 1,015 | \$ 4,918 | 100.0% |
| At December 31, 2015 | | | | | |
| Commercial lines insurance: | | | | | |
| Commercial casualty | \$897 | \$462 | \$ 542 | \$ 1,901 | 40.8 % |
| Commercial property | 192 | 28 | 42 | 262 | 5.6 |
| Commercial auto | 330 | 66 | 89 | 485 | 10.4 |
| Workers' compensation | 389 | 549 | 91 | 1,029 | 22.1 |
| Other commercial | 139 | 17 | 92 | 248 | 5.3 |
| Subtotal | 1,947 | 1,122 | 856 | 3,925 | 84.2 |
| Personal lines insurance: | | | | | |
| Personal auto | 211 | (7) | 69 | 273 | 5.9 |
| Homeowner | 80 | 13 | 25 | 118 | 2.5 |
| Other personal | 52 | 50 | 5 | 107 | 2.3 |
| Subtotal | 343 | 56 | 99 | 498 | 10.7 |
| Excess and surplus lines | 91 | 80 | 56 | 227 | 4.9 |
| Cincinnati Re | — | 10 | — | 10 | 0.2 |
| Total | \$2,381 | \$1,268 | \$ 1,011 | \$ 4,660 | 100.0% |

LIFE POLICY AND INVESTMENT CONTRACT RESERVES

Gross life policy and investment contract reserves were \$2.624 billion at June 30, 2016, compared with \$2.583 billion at year-end 2015, reflecting continued growth in life insurance policies in force. We discuss our life insurance reserving practices in our 2015 Annual Report on Form 10-K, Item 7, Life Insurance Policyholder Obligations and Reserves, Page 101.

OTHER MATTERS

SIGNIFICANT ACCOUNTING POLICIES

Our significant accounting policies are discussed in our 2015 Annual Report on Form 10-K, Item 8, Note 1, Summary of Significant Accounting Policies, Page 123, and updated in this quarterly report Item 1, Note 1, Accounting Policies.

In conjunction with those discussions, in the Management's Discussion and Analysis in the 2015 Annual Report on Form 10-K, management reviewed the estimates and assumptions used to develop reported amounts related to the most significant policies. Management discussed the development and selection of those accounting estimates with the audit committee of the board of directors.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Our greatest exposure to market risk is through our investment portfolio. Market risk is the potential for a decrease in securities' fair value resulting from broad yet uncontrollable forces such as: inflation, economic growth or recession, interest rates, world political conditions or other widespread unpredictable events. It is comprised of many individual risks that, when combined, create a macroeconomic impact.

Our view of potential risks and our sensitivity to such risks is discussed in our 2015 Annual Report on Form 10-K, Item 7a, Quantitative and Qualitative Disclosures About Market Risk, Page 108.

The fair value of our investment portfolio was \$15.380 billion at June 30, 2016, up \$1.024 billion from year-end 2015, including a \$488 million increase in the fixed-maturity portfolio and a \$536 million increase in the equity portfolio.

| (Dollars in millions) | At June 30, 2016 | | | | At December 31, 2015 | | | |
|---|------------------------|------------------|------------|------------------|------------------------|------------------|------------|------------------|
| | Cost or amortized cost | Percent of total | Fair value | Percent of total | Cost or amortized cost | Percent of total | Fair value | Percent of total |
| Taxable fixed maturities | \$6,295 | 49.5 % | \$ 6,689 | 43.5 % | \$6,170 | 50.3 % | \$ 6,353 | 44.3 % |
| Tax-exempt fixed maturities | 3,223 | 25.4 | 3,449 | 22.4 | 3,154 | 25.7 | 3,297 | 23.0 |
| Common equity securities | 3,002 | 23.6 | 5,017 | 32.6 | 2,749 | 22.4 | 4,485 | 31.2 |
| Nonredeemable preferred equity securities | 187 | 1.5 | 225 | 1.5 | 189 | 1.6 | 221 | 1.5 |
| Total | \$12,707 | 100.0 % | \$ 15,380 | 100.0 % | \$12,262 | 100.0 % | \$ 14,356 | 100.0 % |

At June 30, 2016, our consolidated investment portfolio included \$53 million of assets for which values are based on prices or valuation techniques that require significant management judgment (Level 3 assets). This represented less than 1 percent of investment portfolio assets measured at fair value. See Item 1, Note 3, Fair Value Measurements, for additional discussion of our valuation techniques. We have generally obtained and evaluated two nonbinding quotes from brokers; then, our investment professionals determined our best estimate of fair value. These investments include private placements, small issues and various thinly traded securities.

In addition to our investment portfolio, the total investments amount reported in our condensed consolidated balance sheets includes Other invested assets. Other invested assets included \$30 million of life policy loans, \$33 million of private equity investments and \$16 million of real estate through direct property ownership and development projects in the United States at June 30, 2016.

FIXED-MATURITY INVESTMENTS

By maintaining a well-diversified fixed-maturity portfolio, we attempt to reduce overall risk. We invest new money in the bond market on a regular basis, targeting what we believe to be optimal risk-adjusted, after-tax yields. Risk, in this context, includes interest rate, call, reinvestment rate, credit and liquidity risk. We do not make a concerted effort to alter duration on a portfolio basis in response to anticipated movements in interest rates. By regularly investing in the bond market, we build a broad, diversified portfolio that we believe mitigates the impact of adverse economic factors.

Our investment portfolio had no European sovereign debt holdings at June 30, 2016. On that date, we owned other European-based securities, primarily corporate bonds, totaling \$330 million in fair value. The composition of our European-based holdings at June 30, 2016, did not materially change from the \$339 million fair value total at year-end 2015. We discussed our European-based holdings in our 2015 Annual Report on Form 10-K, Item 7a, Quantitative and Qualitative Disclosures About Market Risk, Page 108.

In the first six months of 2016, the increase in fair value of our fixed-maturity portfolio was driven by the combination of net purchases of securities and an increase in net unrealized gains reflecting a decrease in interest rates. At June 30, 2016, our fixed-maturity portfolio with an average rating of A3/A was valued at 106.5 percent of its amortized cost, compared with 103.5 percent at December 31, 2015.

At June 30, 2016, our investment-grade and noninvestment-grade fixed-maturity securities represented 89.9 percent and 4.5 percent of the portfolio, respectively. The remaining 5.6 percent represented fixed-maturity securities that were not rated by Moody's or S&P Global Ratings.

Attributes of the fixed-maturity portfolio include:

| | At June 30, 2016 | At December 31, 2015 | |
|--|------------------------|----------------------------|-----|
| Weighted average yield-to-amortized cost | 4.67% | 4.70 | % |
| Weighted average maturity | 7.1 yrs | 6.9 | yrs |
| Effective duration | 4.8 yrs | 4.7 | yrs |

We discuss maturities of our fixed-maturity portfolio in our 2015 Annual Report on Form 10-K, Item 8, Note 2, Investments, Page 130, and in this quarterly report Item 2, Investments Results.

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TAXABLE FIXED MATURITIES

Our taxable fixed-maturity portfolio, with a fair value of \$6.689 billion at June 30, 2016, included:

| (Dollars in millions) | At June 30, 2016 | At December 31, 2015 |
|---|---------------------------|----------------------------|
| Investment-grade corporate | \$5,379 | \$ 5,060 |
| States, municipalities and political subdivisions | 353 | 314 |
| Below investment-grade corporate | 458 | 393 |
| Commercial mortgage-backed | 310 | 289 |
| Government sponsored enterprises | 170 | 278 |
| Foreign government | 10 | 10 |
| Convertibles and bonds with warrants attached | 5 | 5 |
| United States government | 4 | 4 |
| Total | \$6,689 | \$ 6,353 |

Our strategy is to buy, and typically hold, fixed-maturity investments to maturity, but we monitor credit profiles and fair value movements when determining holding periods for individual securities. With the exception of United States agency issues that include government-sponsored enterprises, no individual issuer's securities accounted for more than 0.9 percent of the taxable fixed-maturity portfolio at June 30, 2016.

Our investment-grade corporate bonds had an average rating of Baa2 by Moody's or BBB+ by S&P Global Ratings and represented 80.4 percent of the taxable fixed-maturity portfolio's fair value at June 30, 2016, compared with 79.7 percent at year-end 2015.

The heaviest concentration in our investment-grade corporate bond portfolio, based on fair value at June 30, 2016, was the financial-related sectors. It represented 40.2 percent of our investment-grade corporate bond portfolio, compared with 37.9 percent at year-end 2015. At June 30, 2016, the real estate sector, including commercial mortgage-backed securities, accounted for 15.0 percent and the insurance sector accounted for 12.6 percent. No other sector exceeded 10 percent of our investment-grade corporate bond portfolio.

Most of the \$353 million of securities issued by states, municipalities and political subdivisions included in our taxable fixed-maturity portfolio at June 30, 2016, were Build America Bonds.

Our taxable fixed-maturity portfolio at June 30, 2016, included \$310 million of commercial mortgage-backed securities with an average rating of Aa1/AA.

TAX-EXEMPT FIXED MATURITIES

At June 30, 2016, we had \$3.449 billion of tax-exempt fixed-maturity securities with an average rating of Aa2/AA by Moody's and S&P Global Ratings. We traditionally have purchased municipal bonds focusing on general obligation and essential services issues, such as water, waste disposal or others. The portfolio is well diversified among more than 1,400 municipal bond issues. No single municipal issuer accounted for more than 0.7 percent of the tax-exempt fixed-maturity portfolio at June 30, 2016.

INTEREST RATE SENSITIVITY ANALYSIS

Because of our strong surplus, long-term investment horizon and ability to hold most fixed-maturity investments until maturity, we believe the company is adequately positioned if interest rates were to rise. Although the fair values of our existing holdings may suffer, a higher rate environment would provide the opportunity to invest cash flow in higher-yielding securities, while reducing the likelihood of untimely redemptions of currently callable securities. While higher interest rates would be expected to continue to increase the number of fixed-maturity holdings trading below 100 percent of amortized cost, we believe lower fixed-maturity security values due solely to interest rate changes would not signal a decline in credit quality. We continue to manage the portfolio with an eye toward both meeting current income needs and managing interest rate risk.

Our dynamic financial planning model uses analytical tools to assess market risks. As part of this model, the effective duration of the fixed-maturity portfolio is continually monitored by our investment department to evaluate the theoretical impact of interest rate movements.

The table below summarizes the effect of hypothetical changes in interest rates on the fair value of the fixed-maturity portfolio:

| (Dollars in millions) | Effect from interest rate change in basis points | | | | |
|-----------------------|--|----------|----------|---------|---------|
| | -200 | -100 | - | 100 | 200 |
| At June 30, 2016 | \$11,157 | \$10,636 | \$10,138 | \$9,647 | \$9,174 |
| At December 31, 2015 | \$10,585 | \$10,112 | \$9,650 | \$9,189 | \$8,748 |

The effective duration of the fixed-maturity portfolio as of June 30, 2016, was 4.8 years, up from 4.7 years at year-end 2015. The above table is a theoretical presentation showing that an instantaneous, parallel shift in the yield curve of 100 basis points could produce an approximately 4.9 percent change in the fair value of the fixed-maturity portfolio. Generally speaking, the higher a bond is rated, the more directly correlated movements in its fair value are to changes in the general level of interest rates, exclusive of call features. The fair values of average- to lower-rated corporate bonds are additionally influenced by the expansion or contraction of credit spreads.

In our dynamic financial planning model, the selected interest rate change of 100 to 200 basis points represents our view of a shift in rates that is quite possible over a one-year period. The rates modeled should not be considered a prediction of future events as interest rates may be much more volatile in the future. The analysis is not intended to provide a precise forecast of the effect of changes in rates on our results or financial condition, nor does it take into account any actions that we might take to reduce exposure to such risks.

EQUITY INVESTMENTS

Our equity investments, with a fair value totaling \$5.242 billion at June 30, 2016, included \$5.017 billion of common stock securities of companies generally with strong indications of paying and growing their dividends. Other criteria we evaluate include increasing sales and earnings, proven management and a favorable outlook. We believe our equity investment style is an appropriate long-term strategy. While our long-term financial position would be affected by prolonged changes in the market valuation of our investments, we believe our strong surplus position and cash flow provide a cushion against short-term fluctuations in valuation. Continued payment of cash dividends by the issuers of our common equity holdings can provide a floor to their valuation.

The table below summarizes the effect of hypothetical changes in market prices on fair value of our equity portfolio. (Dollars in millions) Effect from market price change in percent

| | -30% | -20% | -10% | — | 10% | 20% | 30% |
|----------------------|---------|---------|---------|---------|---------|---------|---------|
| At June 30, 2016 | \$3,669 | \$4,194 | \$4,718 | \$5,242 | \$5,766 | \$6,290 | \$6,815 |
| At December 31, 2015 | \$3,294 | \$3,765 | \$4,235 | \$4,706 | \$5,177 | \$5,647 | \$6,118 |

At June 30, 2016, Johnson & Johnson (NYSE:JNJ) was our largest single common stock holding with a fair value of \$153 million, or 3.0 percent of our publicly traded common stock portfolio and 1.0 percent of the total investment portfolio. Twenty holdings among eight different sectors each had a fair value greater than \$100 million.

Common Stock Portfolio Industry Sector Distribution

| Sector: | Percent of publicly traded common stock portfolio | | | | | | | |
|------------------------|---|-----------------------|----------|---|-------------------------|-----------------------|----------|---|
| | At June 30, 2016 | | | | At December 31, 2015 | | | |
| | Cincinnati Financial | S&P 500 Weightings | Industry | | Cincinnati Financial | S&P 500 Weightings | Industry | |
| Information technology | 15.5 | % | 19.8 | % | 18.4 | % | 20.7 | % |
| Healthcare | 14.4 | | 14.7 | | 12.2 | | 15.1 | |
| Industrials | 14.1 | | 10.2 | | 14.0 | | 10.0 | |
| Financial | 12.8 | | 15.7 | | 15.4 | | 16.5 | |
| Consumer discretionary | 12.1 | | 12.3 | | 10.6 | | 12.9 | |
| Consumer staples | 11.2 | | 10.6 | | 11.0 | | 10.1 | |
| Energy | 8.4 | | 7.4 | | 7.7 | | 6.5 | |
| Materials | 5.3 | | 2.8 | | 4.9 | | 2.8 | |
| Utilities | 4.0 | | 3.6 | | 3.8 | | 3.0 | |
| Telecomm services | 2.2 | | 2.9 | | 2.0 | | 2.4 | |
| Total | 100.0 | % | 100.0 | % | 100.0 | % | 100.0 | % |

UNREALIZED INVESTMENT GAINS AND LOSSES

At June 30, 2016, unrealized investment gains before taxes for the consolidated investment portfolio totaled \$2.765 billion and unrealized investment losses amounted to \$92 million.

The net unrealized investment gains at June 30, 2016, consisted of a pretax net gain position in our fixed-maturity portfolio of \$620 million and a net gain position in our equity portfolio of \$2.053 billion. The net gain position in our fixed-maturity portfolio increased in the first six months of 2016 due largely to credit spread widening in our corporate bond portfolio, among other factors. The net gain position for our current fixed-maturity holdings will naturally decline over time as individual securities mature. In addition, changes in interest rates can cause rapid, significant changes in fair values of fixed-maturity securities and the net gain position, as discussed in Quantitative and Qualitative Disclosures About Market Risk. Events or factors such as economic growth or recession can also affect the fair value of our equity securities. The seven largest contributors to our common stock portfolio net gain position were Exxon Mobil Corporation (NYSE:XOM), Honeywell International Inc. (NYSE:HON), Johnson & Johnson (NYSE:JNJ), The Procter & Gamble Company (NYSE:PG), Hasbro Inc. (Nasdaq:HAS), 3M Co (NYSE:MMM) and Blackrock Inc. (NYSE:BLK), which had a combined gross unrealized gain position of \$647 million.

Unrealized Investment Losses

We expect the number of securities trading below amortized cost to fluctuate as interest rates rise or fall and credit spreads expand or contract due to prevailing economic conditions. Further, amortized costs for some securities are revised through OTTI recognized in prior periods. At June 30, 2016, 118 of the 3,211 securities we owned had fair values below amortized cost, compared with 414 of the 3,163 securities we owned at year-end 2015. The 118 holdings with fair values below cost or amortized cost at June 30, 2016, represented 7.3 percent of the fair value of our investment portfolio and \$92 million in unrealized losses.

102 of the 118 holdings had fair value between 90 percent and 100 percent of amortized cost at June 30, 2016. Nine of these 102 holdings are equity securities that may be subject to OTTI charges taken through earnings should they not recover by the recovery dates we determined. The fair value of these nine equity securities was \$311 million, and they accounted for \$9 million in unrealized losses. The remaining 93 securities primarily consist of fixed-maturity securities whose current valuation is largely the result of interest rate factors. The fair value of these 93 securities was \$473 million, and they accounted for \$13 million in unrealized losses.

16 of the 118 holdings had fair value between 70 percent and 90 percent of amortized cost at June 30, 2016. Five of these 16 holdings were equity securities that may be subject to OTTI charges taken through earnings should they not recover by the dates we determined. The fair value of these equity securities was \$272 million, and they accounted for \$56 million in unrealized losses. We believe the remaining 11 fixed-maturity securities will continue to pay interest and ultimately pay principal upon maturity. The issuers of these 11 securities have strong cash flow to service their debt and meet their contractual obligation to make principal payments. The fair value of these securities was \$74 million, and they accounted for \$14 million in unrealized losses.

No holdings had fair value below 70 percent of amortized cost at June 30, 2016.

The table below reviews fair values and unrealized losses by investment category and by the overall duration of the securities' continuous unrealized loss position.

| (Dollars in millions) | Less than 12 months | | 12 months or more | | Total | Total |
|---|---------------------|-------------------|-------------------|-------------------|------------|-------------------|
| | Fair value | Unrealized losses | Fair value | Unrealized losses | fair value | unrealized losses |
| At June 30, 2016 | | | | | | |
| Fixed maturity securities: | | | | | | |
| Corporate | \$252 | \$ 9 | \$258 | \$ 18 | \$510 | \$ 27 |
| States, municipalities and political subdivisions | 2 | — | 1 | — | 3 | — |
| Commercial mortgage-backed | 5 | — | 9 | — | 14 | — |
| Government-sponsored enterprises | 20 | — | — | — | 20 | — |
| Subtotal | 279 | 9 | 268 | 18 | 547 | 27 |
| Equity securities: | | | | | | |
| Common equities | 546 | 65 | — | — | 546 | 65 |
| Nonredeemable preferred equities | 19 | — | 18 | — | 37 | — |
| Subtotal | 565 | 65 | 18 | — | 583 | 65 |
| Total | \$844 | \$ 74 | \$286 | \$ 18 | \$1,130 | \$ 92 |
| At December 31, 2015 | | | | | | |
| Fixed maturity securities: | | | | | | |
| Corporate | \$1,099 | \$ 63 | \$133 | \$ 33 | \$1,232 | \$ 96 |
| States, municipalities and political subdivisions | 47 | 1 | 22 | — | 69 | 1 |
| Commercial mortgage-backed | 103 | 2 | 2 | — | 105 | 2 |
| Government-sponsored enterprises | 100 | 2 | 127 | 4 | 227 | 6 |
| Subtotal | 1,349 | 68 | 284 | 37 | 1,633 | 105 |
| Equity securities: | | | | | | |
| Common equities | 270 | 51 | — | — | 270 | 51 |
| Nonredeemable preferred equities | 35 | — | — | — | 35 | — |
| Subtotal | 305 | 51 | — | — | 305 | 51 |
| Total | \$1,654 | \$ 119 | \$284 | \$ 37 | \$1,938 | \$ 156 |

At June 30, 2016, 53 fixed-maturity securities with a total unrealized loss of \$18 million had been in an unrealized loss position for 12 months or more. Of that total, no fixed-maturity securities had a fair value below 70 percent of amortized cost; 10 fixed-maturity securities with a fair value of \$57 million had a fair value from 70 percent to less than 90 percent of amortized cost and accounted for \$11 million in unrealized losses; and 43 fixed-maturity securities with a fair value of \$211 million had fair values from 90 percent to less than 100 percent of amortized cost and accounted for \$7 million in unrealized losses.

At June 30, 2016, two equity securities with a fair value of \$18 million had been in an unrealized loss position for 12 months or more. These equity securities had a fair value from 90 percent to less than 100 percent of amortized cost and accounted for less than \$1 million in unrealized losses.

At June 30, 2016, applying our invested asset impairment policy, we determined that the total of \$18 million, for securities in an unrealized loss position for 12 months or more in the table above, was not other-than-temporarily impaired.

During the second quarter of 2016, two securities were written down through an impairment charge, for a total of four during the six months ended June 30, 2016. OTTI resulted in pretax, noncash charges of less than \$1 million and \$2 million for the three and six months ended June 30, 2016. During the first six months of 2015, no securities were written down through impairment charges.

During full-year 2015, we wrote down 20 securities and recorded \$52 million in OTTI charges. At December 31, 2015, 69 fixed-maturity investments with a total unrealized loss of \$37 million had been in an unrealized loss position for 12 months or more. Of that total, five fixed-maturity investments had fair values below 70 percent of amortized cost. There were no equity security investments in an unrealized loss position for 12 months or more as of December 31, 2015.

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The following table summarizes the investment portfolio by severity of decline:

(Dollars in millions)

| At June 30, 2016 | Number of issues | Cost or amortized cost | Fair value | Gross unrealized gain/loss | Gross investment income |
|--|------------------|------------------------|------------------|----------------------------|-------------------------|
| Taxable fixed maturities: | | | | | |
| Fair valued below 70% of amortized cost | — | \$ — | \$ — | \$ — | \$ — |
| Fair valued at 70% to less than 100% of amortized cost | 103 | 573 | 546 | (27) | 14 |
| Fair valued at 100% and above of amortized cost | 1,355 | 5,722 | 6,143 | 421 | 142 |
| Securities sold in current year | — | — | — | — | 7 |
| Total | 1,458 | 6,295 | 6,689 | 394 | 163 |
| Tax-exempt fixed maturities: | | | | | |
| Fair valued below 70% of amortized cost | — | — | — | — | — |
| Fair valued at 70% to less than 100% of amortized cost | 1 | 1 | 1 | — | — |
| Fair valued at 100% and above of amortized cost | 1,650 | 3,222 | 3,448 | 226 | 54 |
| Securities sold in current year | — | — | — | — | 2 |
| Total | 1,651 | 3,223 | 3,449 | 226 | 56 |
| Common equities: | | | | | |
| Fair valued below 70% of cost | — | — | — | — | — |
| Fair valued at 70% to less than 100% of cost | 9 | 611 | 546 | (65) | 5 |
| Fair valued at 100% and above of cost | 60 | 2,391 | 4,471 | 2,080 | 66 |
| Securities sold in current year | — | — | — | — | — |
| Total | 69 | 3,002 | 5,017 | 2,015 | 71 |
| Nonredeemable preferred equities: | | | | | |
| Fair valued below 70% of cost | — | — | — | — | — |
| Fair valued at 70% to less than 100% of cost | 5 | 37 | 37 | — | 1 |
| Fair valued at 100% and above of cost | 28 | 150 | 188 | 38 | 6 |
| Securities sold in current year | — | — | — | — | — |
| Total | 33 | 187 | 225 | 38 | 7 |
| Portfolio summary: | | | | | |
| Fair valued below 70% of cost or amortized cost | — | — | — | — | — |
| Fair valued at 70% to less than 100% of cost or amortized cost | 118 | 1,222 | 1,130 | (92) | 20 |
| Fair valued at 100% and above of cost or amortized cost | 3,093 | 11,485 | 14,250 | 2,765 | 268 |
| Investment income on securities sold in current year | — | — | — | — | 9 |
| Total | 3,211 | \$ 12,707 | \$ 15,380 | \$ 2,673 | \$ 297 |
| At December 31, 2015 | | | | | |
| Portfolio summary: | | | | | |
| Fair valued below 70% of cost or amortized cost | 9 | \$ 76 | \$ 47 | \$ (29) | \$ 4 |
| Fair valued at 70% to less than 100% of cost or amortized cost | 405 | 2,018 | 1,891 | (127) | 66 |
| Fair valued at 100% and above of cost or amortized cost | 2,749 | 10,168 | 12,418 | 2,250 | 478 |
| Investment income on securities sold in current year | — | — | — | — | 30 |
| Total | 3,163 | \$ 12,262 | \$ 14,356 | \$ 2,094 | \$ 578 |

See our 2015 Annual Report on Form 10-K, Item 7, Critical Accounting Estimates, Asset Impairment, Page 50.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures – The company maintains disclosure controls and procedures (as that term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (Exchange Act)).

Any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives. The company's management, with the participation of the company's chief executive officer and chief financial officer, has evaluated the effectiveness of the design and operation of the company's disclosure controls and procedures as of June 30, 2016. Based upon that evaluation, the company's chief executive officer and chief financial officer concluded that the design and operation of the company's disclosure controls and procedures provided reasonable assurance that the disclosure controls and procedures are effective to ensure:

that information required to be disclosed in the company's reports under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and

that such information is accumulated and communicated to the company's management, including its chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding required disclosures.

Changes in Internal Control over Financial Reporting – During the three months ended June 30, 2016, there were no changes in our internal controls over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Part II – Other Information

Item 1. Legal Proceedings

Neither the company nor any of our subsidiaries are involved in any litigation believed to be material other than ordinary, routine litigation incidental to the nature of our business.

Item 1A. Risk Factors

Our risk factors have not changed materially since they were described in our 2015 Annual Report on Form 10-K filed February 26, 2016.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

We did not sell any of our shares that were not registered under the Securities Act during the first six months of 2016. The board of directors has authorized share repurchases since 1996. Purchases are expected to be made generally through open market transactions. The board gives management discretion to purchase shares at reasonable prices in light of circumstances at the time of purchase, subject to SEC regulations. On October 24, 2007, the board of directors expanded the existing repurchase authorization to approximately 13 million shares. We have 4,064,493 shares available for purchase under our programs at June 30, 2016.

| Period | Total number of shares purchased | Average price paid per share | Total number of shares purchased as part of publicly announced plans or programs | Maximum number of shares that may yet be purchased under the plans or programs |
|------------------|----------------------------------|------------------------------|--|--|
| April 1-30, 2016 | — | — | — | 4,099,493 |
| May 1-31, 2016 | — | — | — | 4,099,493 |
| June 1-30, 2016 | 35,000 | \$ 69.56 | 35,000 | 4,064,493 |
| Totals | 35,000 | 69.56 | 35,000 | |

Item 6. Exhibits

| Exhibit No. | Exhibit Description |
|-------------|---|
| 3.1 | Amended and Restated Articles of Incorporation of Cincinnati Financial Corporation (incorporated by reference to the company's 2010 Annual Report on Form 10-K dated February 25, 2011, Exhibit 3.1) |
| 3.2 | Regulations of Cincinnati Financial Corporation, as amended through May 1, 2010 (incorporated by reference to the company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2010, Exhibit 3.2) |
| 10.1 | Cincinnati Financial Corporation 2016 Stock Compensation Plan (incorporated by reference to the company's Definitive Proxy Statement dated March 16, 2016, Appendix B) |
| 10.2 | First Amendment of Cincinnati Financial Corporation 2016 Stock Compensation Plan (incorporated by reference to Exhibit 99.1 filed with the Company's current report on Form 8-K dated April 11, 2016) |
| 31A | Certification pursuant to Section 302 of the Sarbanes Oxley Act of 2002 – Chief Executive Officer |
| 31B | Certification pursuant to Section 302 of the Sarbanes Oxley Act of 2002 – Chief Financial Officer |
| 32 | Certification pursuant to Section 906 of the Sarbanes Oxley Act of 2002 |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema Document |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document |

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SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CINCINNATI FINANCIAL CORPORATION

Date: July 26, 2016

/S/ Eric N. Mathews

Eric N. Mathews, CPCU, AIAF

Vice President, Assistant Secretary and Assistant Treasurer

(Principal Accounting Officer)

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