

CINCINNATI FINANCIAL CORP

Form 10-Q

April 24, 2014

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 March 31, 2014.

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 (State or other jurisdiction of incorporation or organization)	31-0746871 (I.R.S. Employer Identification No.)
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6200 S. Gilmore Road, Fairfield, Ohio (Address of principal executive offices)	45014-5141 (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 April 21, 2014, there were 163,519,128 shares of common stock outstanding.

CINCINNATI FINANCIAL CORPORATION
FORM 10-Q FOR THE QUARTER ENDED March 31, 2014

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Part I – Financial Information

Item 1. Financial Statements (unaudited)

CINCINNATI FINANCIAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(In millions except per share data)

	March 31, 2014	December 31, 2013
Assets		
Investments		
Fixed maturities, at fair value (amortized cost: 2014—\$8,609; 2013—\$8,638)	\$9,180	\$9,121
Equity securities, at fair value (cost: 2014—\$2,545; 2013—\$2,523)	4,426	4,375
Other invested assets	72	68
Total investments	13,678	13,564
Cash and cash equivalents	521	433
Investment income receivable	116	121
Finance receivable	83	85
Premiums receivable	1,396	1,346
Reinsurance recoverable	546	547
Prepaid reinsurance premiums	27	26
Deferred policy acquisition costs	564	565
Land, building and equipment, net, for company use (accumulated depreciation: 2014—\$424; 2013—\$420)	207	210
Other assets	79	73
Separate accounts	725	692
Total assets	\$17,942	\$17,662
Liabilities		
Insurance reserves		
Loss and loss expense reserves	\$4,375	\$4,311
Life policy and investment contract reserves	2,435	2,390
Unearned premiums	2,035	1,976
Other liabilities	545	611
Deferred income tax	721	673
Note payable	104	104
Long-term debt and capital lease obligations	834	835
Separate accounts	725	692
Total liabilities	11,774	11,592
Commitments and contingent liabilities (Note 12)	—	—
Shareholders' Equity		
Common stock, par value—\$2 per share; (authorized: 2014 and 2013—500 million shares; issued: 2014 and 2013—198 million shares)	397	397
Paid-in capital	1,191	1,191
Retained earnings	4,287	4,268
Accumulated other comprehensive income	1,578	1,504
Treasury stock at cost (2014 and 2013—35 million shares)	(1,285) (1,290
Total shareholders' equity	6,168	6,070
Total liabilities and shareholders' equity	\$17,942	\$17,662

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

(In millions except per share data)

	Three months ended March 31,	
	2014	2013
Revenues		
Earned premiums	\$1,027	\$931
Investment income, net of expenses	135	128
Realized investment gains, net	22	41
Fee revenues	3	1
Other revenues	2	2
Total revenues	1,189	1,103
Benefits and Expenses		
Insurance losses and policyholder benefits	732	568
Underwriting, acquisition and insurance expenses	320	300
Interest expense	14	13
Other operating expenses	4	5
Total benefits and expenses	1,070	886
Income Before Income Taxes	119	217
Provision for Income Taxes		
Current	20	54
Deferred	8	9
Total provision for income taxes	28	63
Net Income	\$91	\$154
Per Common Share		
Net income—basic	\$0.56	\$0.95
Net income—diluted	0.55	0.94

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

(In millions)	Three months ended March 31,	
	2014	2013
Net Income	\$91	\$154
Other Comprehensive Income		
Unrealized gains on investments available-for-sale, net of tax of \$41 and \$124, respectively	76	232
Net change in pension actuarial loss and prior service cost, net of tax of \$0 and \$1, respectively	(1) 1
Change in life deferred acquisition costs, life policy reserves and other, net of tax of \$0 and \$0, respectively	(1) —
Other comprehensive income, net of tax	74	233
Comprehensive Income	\$165	\$387

CINCINNATI FINANCIAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(In millions)	Common Stock				Accumulated Other Comprehensive	Treasury	Total Share- holders' Equity
	Outstanding Shares	Amount	Paid-in Capital	Retained Earnings	Income	Stock	
Balance December 31, 2012	163	\$394	\$1,134	\$4,021	\$1,129	\$(1,225)	\$5,453
Net income	—	—	—	154	—	—	154
Other comprehensive income, net	—	—	—	—	233	—	233
Dividends declared	—	—	—	(66)	—	—	(66)
Treasury stock acquired—share repurchase authorization	—	—	—	—	—	—	—
Other	—	1	12	—	—	(2)	11
Balance March 31, 2013	163	\$395	\$1,146	\$4,109	\$1,362	\$(1,227)	\$5,785
Balance December 31, 2013	163	\$397	\$1,191	\$4,268	\$1,504	\$(1,290)	\$6,070
Net income	—	—	—	91	—	—	91
Other comprehensive income, net	—	—	—	—	74	—	74
Dividends declared	—	—	—	(72)	—	—	(72)
Treasury stock acquired—share repurchase authorization	—	—	—	—	—	(7)	(7)
Other	—	—	—	—	—	12	12
Balance March 31, 2014	163	\$397	\$1,191	\$4,287	\$1,578	\$(1,285)	\$6,168

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

CINCINNATI FINANCIAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In millions)	Three months ended March 31,	
	2014	2013
Cash Flows From Operating Activities		
Net income	\$91	\$154
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	13	9
Realized gains on investments, net	(22)	(41)
Stock-based compensation	6	5
Interest credited to contract holders	10	11
Deferred income tax expense	8	9
Changes in:		
Investment income receivable	5	(2)
Premiums and reinsurance receivable	(50)	(82)
Deferred policy acquisition costs	(5)	(19)
Other assets	(5)	(2)
Loss and loss expense reserves	64	10
Life policy reserves	49	13
Unearned premiums	59	83
Other liabilities	(102)	(88)
Current income tax receivable/payable	8	(3)
Net cash provided by operating activities	129	57
Cash Flows From Investing Activities		
Sale of fixed maturities	24	12
Call or maturity of fixed maturities	252	221
Sale of equity securities	31	98
Purchase of fixed maturities	(236)	(325)
Purchase of equity securities	(33)	(108)
Investment in finance receivables	(4)	(8)
Collection of finance receivables	7	7
Investment in buildings and equipment, net	(3)	(1)
Change in other invested assets, net	1	2
Net cash provided by (used in) investing activities	39	(102)
Cash Flows From Financing Activities		
Payment of cash dividends to shareholders	(67)	(65)
Purchase of treasury shares	(7)	—
Proceeds from stock options exercised	8	6
Contract holders' funds deposited	20	24
Contract holders' funds withdrawn	(32)	(31)
Other	(2)	4
Net cash used in financing activities	(80)	(62)
Net change in cash and cash equivalents	88	(107)
Cash and cash equivalents at beginning of year	433	487
Cash and cash equivalents at end of period	\$521	\$380
Supplemental disclosures of cash flow information:		
Interest paid	\$—	\$—
Income taxes paid	11	54
Non-cash activities:		

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Conversion of securities	\$—	\$43
Equipment acquired under capital lease obligations	5	12
Cashless exercise of stock options	4	9

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, 2013, condensed consolidated balance sheet amounts are derived from the audited financial statements but do not include all disclosures required by GAAP.

Our March 31, 2014, 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 2013 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.

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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 invested assets:

(In millions)	Cost or amortized cost	Gross unrealized gains losses		Fair value
At March 31, 2014				
Fixed maturity securities:				
States, municipalities and political subdivisions	\$3,113	\$143	\$12	\$3,244
Convertibles and bonds with warrants attached	17	—	—	17
United States government	7	—	—	7
Government-sponsored enterprises	211	—	20	191
Foreign government	10	—	—	10
Commercial mortgage-backed	206	2	2	206
Corporate	5,045	468	8	5,505
Subtotal	8,609	613	42	9,180
Equity securities:				
Common equities	2,418			