



# Cincinnati Financial Corporation

## 2008 Third-quarter Letter to Shareholders

November 7, 2008

### To Our Shareholders, Friends and Associates:

We are more convinced than ever that our long-term approach to business will help us come out of this difficult period a better and more focused company.

In this document, you'll read about our initiatives to extend your company's advantages and preparations to seize new opportunities. You'll also read about our commitment to create two kinds of capital strength that give us flexibility under pressure. Our intention is to protect and preserve both kinds, adding to this capital over time. First, we have strong financial capital and flexibility. Secondly, we have invested in relationships and accumulated tremendous people capital – loyal agents who help us underwrite profitably; loyal policyholders who value broad insurance coverages and superior service; and loyal associates willing to step up their efforts. Both types of capital give us welcome advantages in these uncertain times:

**Exceptional liquidity.** We have strong cash flow from operations, thanks to our agents' consistent willingness to let us earn their profitable business. Our insurance subsidiaries have capital that exceeds required levels, and we hold significant additional assets at the parent company level. These assets are there if we need them, giving us flexibility through difficult periods to maintain our record of increasing dividends for 48 consecutive years and to continue growing our insurance business. Our operations do not depend on bank loans to meet payroll, pay claims or cover other normal business expenses.

**A rebalanced investment portfolio.** Over the past year, you have heard about significant sales, not just of Fifth Third Bancorp, but also sales of other stocks. As we continue to apply our new investment guidelines, we are diversifying away from concentrated positions in single stocks or industries. Our recent sales are part of this strategic portfolio restructuring and give us the flexibility to reinvest proceeds where we see potential for both current income and long-term return.

**Disciplined and focused company associates.** Our resolve is to stay calm and to deepen our commitment to outperform on service to our agents and their clients. Aligning ourselves ever more closely with local agents can only build our resilience, mitigating whatever additional setbacks may occur in the wider markets, in our industry and for our company. Our energy level and activity have never been higher.

At a time when our policyholders needed us, our associates' outstanding response to storm claims created satisfied customers – customers who will continue to buy our policies for years to come and share the value of a Cincinnati policy with their friends and neighbors. And at a time when many businesses are contracting, we believe we can and must stay energized, expand our marketing territories, add new agency relationships and introduce new products and technology.

An unrelenting focus on what we can control – disciplined investing and underwriting as well as excellent service to our agents – will go a long way to offset what we can't control, as individuals or as individual companies. We will dedicate ourselves to maintaining that focus and moving steadily toward growth and long-term prosperity. Thank you for your investment and your faith in our daily efforts to return value to you by marketing the value of Cincinnati service and solid insurance protection.

Respectfully,

/S/ James E. Benoski

James E. Benoski  
Vice Chairman of the Board

/S/ John J. Schiff, Jr.

John J. Schiff, Jr., CPCU  
Chairman of the Board

/S/ Kenneth W. Stecher

Kenneth W. Stecher  
President and Chief Executive Officer

Your company offers a series of shareholder communications throughout the year to keep you informed. All past publications are available on our Web site [www.cinfin.com/investors](http://www.cinfin.com/investors). Each piece was accurate at the time it was posted online; please refer to the most recent item below for the most timely information.

## About the Company

Cincinnati Financial meets the needs of agencies and policyholders through our insurance group and three complementary subsidiaries:

**The Cincinnati Insurance Company** leads our A++ A.M. Best-rated standard market property casualty insurance group, which includes **The Cincinnati Casualty Company** and **The Cincinnati Indemnity Company**. This group markets a broad range of business, homeowner and auto policies through our select group of local independent insurance agencies in 34 states. These companies support each agency's ability to provide exceptional value and service to the people and businesses in its community. Our local field representatives work out of their homes, customizing products to meet policyholder needs, responding personally and promptly to claims and strengthening relationships.

Two other subsidiaries of The Cincinnati Insurance Company also market insurance products. **The Cincinnati Life Insurance Company**, rated A+ by A.M. Best, markets life insurance policies, disability income policies and annuities. **The Cincinnati Specialty Underwriters Insurance Company**, rated A by A.M. Best, began offering excess and surplus lines insurance products in 2008.

Three subsidiaries of Cincinnati Financial support our insurance operations. **CSU Producer Resources Inc.** offers insurance brokerage services to our independent agencies to support their access to Cincinnati Specialty Underwriters. **CFC Investment Company** offers commercial leasing and financing services to our agents and their clients. **CinFin Capital Management Company** provides asset management services to institutions, corporations and nonprofit organizations.

## 2007 Fourth-quarter and Full-year Letter to Shareholders – mid-February 2008

This message from our chairman and our president includes recent news releases about financial results announced February 6 and actions taken by the board of directors at its February 1 meeting. *The Cincinnati Experience*, a profile of our operating philosophy, accompanies this letter.

## The Cincinnati Experience – mid-February 2008

The Cincinnati Insurance Company, Cincinnati Financial Corporation's lead subsidiary, ranks among the top 25 U.S. property casualty insurer groups based on net written premiums. In *The Cincinnati Experience*, you'll read about how our relationship-based approach creates value and loyalty, supporting premium growth.

## 2007 Annual Report on Form 10-K – late-February 2008

The *Annual Report on Form 10-K* is a detailed document published by every publicly traded company as required by the U.S. Securities and Exchange Commission. In our report, we describe your company's operations, its results and trends, along with supporting data, discussions, audited financial statements and accompanying notes.

## 2008 Shareholder Meeting Notice and Proxy Statement – mid-March 2008

This statement informs you of items requiring shareholder action at the 2008 Annual Meeting of Shareholders on May 3, 2008. It identifies board members, detailing director and executive officer compensation and board activities. Notice cards, mailed in March, tell how to easily obtain the *Proxy Statement* and vote.

## Chairman and President's Letter – late-March 2008

Accompanying the Proxy Statement are the 2007 condensed balance sheets and income statements, six years of summary financial data and an annual message from our chairman and our president. Their letter presents management's perspectives on your company's 2007 performance and trends that may affect performance in 2008 and beyond.

## First-quarter 2008 Letter to Shareholders – mid-May 2008

This message from our chairman and our president includes recent news releases about financial results announced April 30, results of shareholder votes at the 2008 Annual Meeting of Shareholders and actions of the board at its May meeting. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by May 12, 2008.

## Second-quarter 2008 Letter to Shareholders – mid-August 2008

This executive perspective includes our August 6 news release with financial results. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by August 11, 2008.

## Third-quarter 2008 Letter to Shareholders – mid-November 2008

This executive perspective includes our October 29 news release with financial results. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by November 10, 2008.

# Recent News Releases

## Cincinnati Financial Reports Profitable 2008 Third Quarter

- Positive net and operating income for three- and nine-month periods
- Book value holds steady for the quarter at \$28.87 on September 30

### Cincinnati, October 29, 2008 – Cincinnati Financial Corporation (Nasdaq: CINF) today reported:

- Net income of \$247 million, or \$1.50 per share, in the 2008 third quarter, compared with \$124 million, or 72 cents, in the 2007 third quarter. Third-quarter 2008 realized investment gains were significantly higher. Common stocks sales to lock in gains and diversify the portfolio more than offset previously announced non-cash impairment charges.
- Operating income\* of \$74 million, or 45 cents per share, in the 2008 third quarter, compared with \$114 million, or 66 cents, in the 2007 third quarter. Previously announced catastrophe losses reduced 2008 third-quarter operating income by 25 cents per share compared with 5 cents last year. Nine-month operating income of \$1.54 per share included an 87-cent catastrophe loss impact compared with a 10-cent impact on last year's nine-month operating income of \$2.49 per share.

### Financial Highlights

(Dollars in millions except share data)	Three months ended September 30,			Nine months ended September 30,		
	2008	2007	Change %	2008	2007	Change %
<b>Revenue Highlights</b>						
Earned premiums .....	\$ 781	\$ 811	(3.7)	\$ 2,355	\$ 2,447	(3.8)
Investment income .....	130	152	(14.5)	412	451	(8.5)
Total revenues .....	<b>1,186</b>	982	20.8	<b>2,806</b>	3,283	(14.5)
<b>Income Statement Data</b>						
Net income .....	\$ 247	\$ 124	99.5	\$ 268	\$ 669	(59.9)
Net realized investment gains and losses ...	<u>173</u>	<u>10</u>	nm	<u>16</u>	<u>238</u>	(93.2)
Operating income* .....	<u>\$ 74</u>	<u>\$ 114</u>	(35.4)	<u>\$ 252</u>	<u>\$ 431</u>	(41.6)
<b>Per Share Data (diluted)</b>						
Net income .....	\$ 1.50	\$ 0.72	108.3	\$ 1.64	\$ 3.86	(57.5)
Net realized investment gains and losses ...	<u>1.05</u>	<u>0.06</u>	nm	<u>0.10</u>	<u>1.37</u>	(92.7)
Operating income* .....	<u>\$ 0.45</u>	<u>\$ 0.66</u>	(31.8)	<u>\$ 1.54</u>	<u>\$ 2.49</u>	(38.2)
Book value .....				\$ 28.87	\$ 38.47	(25.0)
Cash dividend declared .....	\$ 0.39	\$ 0.355	9.9	\$ 1.17	\$ 1.065	9.9
Weighted average shares outstanding .....	<b>164,242,185</b>	172,399,539	(4.7)	<b>163,834,163</b>	173,423,199	(5.5)

\* The Definitions of Non-GAAP Information and Reconciliation to Comparable GAAP Measures on [www.cinfin.com](http://www.cinfin.com) defines and reconciles measures presented in this release that are not based on Generally Accepted Accounting Principles or Statutory Accounting Principles.

\*\* Forward-looking statements and related assumptions are subject to the risks outlined in the company's safe harbor statement (see Page 13).

nm Not meaningful

## Insurance Operations Highlights

- \$727 million in third-quarter 2008 consolidated property casualty net written premiums compared with \$736 million in the 2007 third quarter. Strong contribution of new business written by agencies partially offset the effects of competition in the commercial markets and current economic trends. Excess and surplus lines operations launched in January 2008 added \$4 million to new business in the third quarter and \$8 million year-to-date.
- Property casualty underwriting loss of \$9 million in 2008 third quarter compared with underwriting profit of \$21 million in the 2007 third quarter. 2008 property casualty results were reduced by catastrophe losses.
- Three- and nine-month property casualty combined ratio near breakeven despite catastrophe losses from Hurricane Ike.
- 3 cents per share contribution from life insurance operations to third-quarter operating income, down from 5 cents.

## Investment and Balance Sheet Highlights

- Book value of \$28.87 at September 30, 2008, almost flat from \$28.99 at June 30, 2008, but down from year-end

2007 on valuation changes in first half of year.

Property casualty statutory surplus rose slightly from its midyear level.

- Pretax investment income of \$130 million in 2008 third quarter compared with \$152 million in 2007 third quarter. Dividend income from the equity portfolio declined due to dividend cuts, some from positions that the company has since sold or reduced.
- Equity sales of portions of selected positions locked in gains or reduced concentrations. Proceeds to be reinvested in sectors with better total return prospects. Sales helped reduce financial sector concentration by 25 percent since midyear.

## Outlook\*\*

- Outlook for specific full-year 2008 metrics unchanged from September update. Management anticipates full year profitability and continued capital strength, which supports our cash dividend and continued investment in insurance operations, even in a difficult economic and industry environment.

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## Financial and Operational Strength for Current Challenges and Ongoing Success

Kenneth W. Stecher, president and chief executive officer, commented, “The current instability of financial markets highlights the value of operating in a transparent and conservative way, building a cushion of financial strength over a period of years. A long-term perspective governs all of our major decisions – to the consistent benefit of our policyholders, agents, shareholders and associates. We continue to focus on our risk management program, with the goal of more specifically defining our risk limits, aligning our operating plan accordingly and improving management’s ability to identify and respond to changing conditions.

“Exceptional liquidity arises from our strong cash flows and prudent cash balances. All of our insurance subsidiaries continue to be highly rated, operating with a level of capital far exceeding regulatory requirements. Statutory surplus of our property casualty insurance companies increased slightly during the third quarter of 2008. Plus, unlike many insurers, we hold significant additional assets at the parent company level, increasing our flexibility through all periods to maintain our cash dividend and

to continue to invest in and expand our insurance operations.

“New internal parameters for our investment portfolio, including more conservative limits on sector and issuer concentrations, are helping us prepare to withstand future challenges. Recent sales of selected common stock holdings are part of a strategic rebalancing, providing cash for reinvestment into sectors that we believe have better prospects for both current income and long-term appreciation. In early October we sold approximately 9 million additional shares of Fifth Third Bancorp (NASDAQ: FITB), reducing our position to 20 million shares. In total, we have reduced our financial sector holdings 25 percent since midyear, moving this sector more in line with our longer-term targets. In large part, common stock sales occurred when we exercised appropriate sell discipline to lock in gains.

“At quarter-end, fixed-maturity investments represented almost 60 percent of the portfolio, a level management believes is appropriate. We view our diversification to be consistent with our view of prudent risk management. Going forward, we will evaluate all of our fixed-maturity and equity investments using

our investment parameters and risk limits and adding to both the fixed maturity and equity portfolios, as appropriate. We believe our current capital position can withstand short term pressures, such as the market volatility that we have experienced in October,” Stecher noted.

### **Third Quarter 2008 Underwriting Results and Full-year 2008 Property Casualty Outlook**

Steven J. Johnston, FCAS, MAAA, CFA, chief financial officer, said, “As we work to write profitable insurance business, we continue to face unfavorable pricing and economic trends. At this time, we continue to believe that 2008 full-year written premiums could decline by 5 percent, or slightly more, if pessimistic views of these trends prove accurate and commercial insurance pricing continues to be very competitive.

“A more optimistic view could result in a rate of decline for full-year 2008 premiums closer to the 4.2 percent we experienced so far in 2008. This pace is appropriate and consistent with our agents’ practice of selecting and retaining accounts with manageable risk characteristics that support the lower prevailing prices. It reflects the advantages of our three year policies. We believe this pace also reflects the advantages we achieve by maintaining an experienced field force. Our representatives live in our agents’ communities and serve their clients, providing us with quality intelligence on local market conditions. Since the end of the third quarter, our first Texas representative has begun to explore relationships with agencies in the Austin market, and our second team member is scheduled to relocate to the Dallas market in November.

“We continue to pioneer this and other new paths to future growth. During the third quarter, we introduced our excess and surplus lines capabilities to additional agencies in more states, staying on track with our plans to have these products available in 33 states by year end. We continued appointing new agencies and working to position our personal lines for profitable future growth, including introducing personal lines capabilities in new geographies. We look to 2009 for momentum in all of these initiatives, as well as advances in our technology that will make it easier for agents and their policyholders to do business with our company.”

Johnston continued, “High catastrophe losses continued to temper property casualty profitability despite satisfactory underlying trends. Our commercial lines combined ratio was 96.6 percent for the nine-month period, despite a 5.5 percentage-point rise in commercial catastrophe losses. We continue to see the potential for the full-year 2008 combined ratio for our overall property casualty operations to remain slightly above 100 percent.

“We’re taking that conservative view of the combined ratio because of the record catastrophe losses this year. Hurricane Ike moved into the Midwest on September 14, causing unusually high winds in Ohio, Indiana and Kentucky. Our third-quarter estimate of gross losses from that storm was \$105 million, making it the single largest gross catastrophe event in the company’s history. Net of reinsurance, the loss is estimated at \$57 million. Our reinsurance program, an important part of our risk management efforts, protected our surplus from outsized losses as intended. Virtually all of the losses reported by our policyholders occurred in the Midwest.

“Through October 24, we had received approximately 18,000 claims from Hurricane Ike, of which more than 80 percent have been closed. To restore the affected layers of our catastrophe reinsurance treaty, we incurred a reinstatement premium of \$11 million, which reduced written and earned premiums for the three- and nine-month periods.”

Johnston noted, “In mid-2008, we modified our defined benefit pension plan and began transitioning to a sponsored 401(k) with company matching of associate contributions. This action reduces the company’s future risk while offering associates an up-to-date, more flexible benefits program. The pension plan now includes only associates 40 years of age or older on August 31, 2008, who elected to remain in the plan. We now expect fourth-quarter 2008 results to reflect a settlement cost of approximately \$26 million, largely related to benefit distributions to those who left the qualified pension plan. Going forward, we expect potential savings from lower funding requirements for the pension plan to be offset by company matching contributions to 401(k) accounts for associates who do not accrue pension plan benefits.”

### **Risk Management Strengthens Investment Opportunities**

Stecher added, “Our rebalancing actions, together with market and economic forces, have significantly changed our investment portfolio over the past 12 months. The decision to rebalance our portfolio grew out of our implementation of an enhanced risk management process, which involves modeling outcomes, setting tolerances and acting to optimize use of our capital. We considered opportunities to reduce volatility risk while retaining upside potential. After common stock sales made since midyear, our financial sector holdings now account for approximately 30 percent of the market value of our equity portfolio, down 25 percent.

“While our equity portfolio now is better positioned for total return, it is producing lower dividend income. We expect full-year 2008 pretax investment income to be less than

90 percent of the 2007 level, with no resumption of earned dividend growth in 2009. We also expect our highly rated and diversified \$5.941 billion bond and short-term investment portfolio to continue providing steady interest income. We generally hold bonds to maturity, redeeming them at full value of the principal.”

Stecher concluded, “We believe that our strong surplus position and superior insurer financial strength ratings are competitive advantages that help our agents market our policies.

In this market, consistency and predictability are our most valuable differentiators. Our financial strength supports the consistent, predictable performance that our policyholders, agents, associates and shareholders have always expected and received. We will continue to manage our capital to withstand significant challenges. We believe our capital position and cash flow continues to support our cash dividend, which the board sees as a priority over repurchase in this market.”

## Consolidated Property Casualty Insurance Operations

(Dollars in millions)	Three months ended September 30,			Nine months ended September 30,		
	2008	2007	Change %	2008	2007	Change %
Written premiums . . . . .	\$ 727	\$ 736	(1.3)	\$ 2,292	\$ 2,392	(4.2)
Earned premiums . . . . .	\$ 751	\$ 777	(3.3)	\$ 2,262	\$ 2,348	(3.6)
Loss and loss expenses excluding catastrophes	460	511	(9.9)	1,362	1,409	(3.3)
Catastrophe loss and loss expenses . . . . .	63	13	375.8	219	28	688.6
Commission expenses . . . . .	124	127	(3.0)	409	440	(6.9)
Underwriting expenses . . . . .	110	102	9.0	287	270	6.3
Policyholder dividends . . . . .	3	3	0.8	11	9	18.9
Underwriting profit (loss) . . . . .	\$ (9)	\$ 21	(144.8)	\$ (26)	\$ 192	(113.3)
Ratios as a percent of earned premiums:						
Loss and loss expenses excluding catastrophes	61.3%	65.7%		60.2%	60.0%	
Catastrophe loss and loss expenses . . . . .	8.4	1.7		9.7	1.2	
Loss and loss expenses . . . . .	69.7	67.4		69.9	61.2	
Commission expenses . . . . .	16.5	16.5		18.1	18.7	
Underwriting expenses . . . . .	14.7	13.0		12.6	11.5	
Policyholder dividends . . . . .	0.4	0.4		0.5	0.4	
Combined ratio . . . . .	101.3%	97.3%		101.1%	91.8%	
Reserve development impact on loss and						
loss expense ratio . . . . .	13.7%	6.5%		8.9%	5.4%	

- 1.3 percent and 4.2 percent declines in third-quarter and nine-month 2008 property-casualty net written premiums, reflecting weakening economy, soft pricing and disciplined underwriting.
- \$92 million in third-quarter 2008 new business written directly by agencies, up 12.1 percent from \$82 million in last year’s third quarter.
- Positive benefits from growth initiatives seen in third quarter including \$8 million in nine-month net written premiums from excess and surplus lines operations launched in January 2008.
- New state, new agency and other initiatives also contributed. Agency relationships rise to 1,118 with 1,369 reporting

- locations marketed property casualty insurance products at quarter end, up from 1,092 agency relationships with 1,327 reporting locations at year-end 2007.
- 101.3 percent third-quarter and 101.1 percent nine-month 2008 GAAP combined ratios. Near breakeven performance achieved in both periods despite significantly higher catastrophe losses. The effects of soft pricing and loss cost inflation were offset by higher savings from favorable development on prior year reserves.
- \$63 million in third-quarter 2008 catastrophe losses, due primarily to Hurricane Ike.

(In millions, net of reinsurance)

Dates	Cause of loss	Region	Three months ended September 30,			Nine months ended September 30,		
			Commercial lines	Personal lines	Total	Commercial lines	Personal lines	Total
<b>2008</b>								
	First quarter catastrophes		\$ (1)	\$ 0	\$ (1)	\$ 21	\$ 21	\$ 42
	Second quarter catastrophes		(2)	(10)	(12)	66	34	100
Jul. 19	Wind, hail, flood, water, hydrostatic	Midwest	3	3	6	3	3	6
Jul. 26	Wind, hail, flood, water, hydrostatic	Midwest	1	8	9	1	8	9
Sep. 12-14	Hurricane Ike	South, Midwest	20	37	57	20	37	57
	All other		1	0	1	3	3	6
	Development on 2007 and prior catastrophes		1	2	3	(2)	1	(1)
	Calendar year incurred total		<u>\$ 23</u>	<u>\$ 40</u>	<u>\$ 63</u>	<u>\$ 112</u>	<u>\$ 107</u>	<u>\$ 219</u>
<b>2007</b>								
	First quarter catastrophes		(1)	1	0	5	2	7
	Second quarter catastrophes		2	1	3	4	4	8
Sep. 20-21	Wind, hail, flood	Midwest	1	6	7	1	6	7
	All other		4	2	6	18	8	26
	Development on 2006 and prior catastrophes		(5)	2	(3)	(11)	(9)	(20)
	Calendar year incurred total		<u>\$ 1</u>	<u>\$ 12</u>	<u>\$ 13</u>	<u>\$ 17</u>	<u>\$ 11</u>	<u>\$ 28</u>

## Insurance Segment Highlights

### Commercial Lines Insurance Operations

(Dollars in millions)

	Three months ended September 30,			Nine months ended September 30,		
	2008	2007	Change %	2008	2007	Change %
Written premiums . . . . .	<u>\$ 538</u>	<u>\$ 544</u>	(1.2)	<u>\$ 1,759</u>	<u>\$ 1,851</u>	(4.9)
Earned premiums . . . . .	<u>\$ 582</u>	<u>\$ 600</u>	(3.0)	<u>\$ 1,743</u>	<u>\$ 1,810</u>	(3.7)
Loss and loss expenses excluding catastrophes	<u>348</u>	<u>395</u>	(11.8)	<u>1,034</u>	<u>1,068</u>	(3.3)
Catastrophe loss and loss expenses . . . . .	<u>23</u>	<u>1</u>	nm	<u>112</u>	<u>17</u>	574.2
Commission expenses . . . . .	<u>91</u>	<u>94</u>	(4.3)	<u>304</u>	<u>330</u>	(7.8)
Underwriting expenses . . . . .	<u>87</u>	<u>79</u>	10.6	<u>223</u>	<u>202</u>	10.6
Policyholder dividends . . . . .	<u>3</u>	<u>3</u>	0.8	<u>11</u>	<u>9</u>	18.9
Underwriting profit . . . . .	<u>\$ 30</u>	<u>\$ 28</u>	7.2	<u>\$ 59</u>	<u>\$ 184</u>	(67.8)
Ratios as a percent of earned premiums:						
Loss and loss expenses excluding catastrophes	<u>59.8%</u>	<u>65.8%</u>		<u>59.3%</u>	<u>59.0%</u>	
Catastrophe loss and loss expenses . . . . .	<u>4.0</u>	<u>0.2</u>		<u>6.4</u>	<u>0.9</u>	
Loss and loss expenses . . . . .	<u>63.8</u>	<u>66.0</u>		<u>65.7</u>	<u>59.9</u>	
Commission expenses . . . . .	<u>15.6</u>	<u>15.8</u>		<u>17.5</u>	<u>18.3</u>	
Underwriting expenses . . . . .	<u>14.9</u>	<u>13.1</u>		<u>12.8</u>	<u>11.1</u>	
Policyholder dividends . . . . .	<u>0.6</u>	<u>0.5</u>		<u>0.6</u>	<u>0.5</u>	
Combined ratio . . . . .	<u>94.9%</u>	<u>95.4%</u>		<u>96.6%</u>	<u>89.8%</u>	
Reserve development impact on loss and loss expense ratio . . . . .	<u>15.0%</u>	<u>7.1%</u>		<u>10.1%</u>	<u>5.6%</u>	

- 1.2 percent and 4.9 percent declines in third-quarter and nine-month 2008 commercial lines net written premiums, primarily a result of weakening economy, soft pricing and disciplined underwriting.
- \$77 million in third-quarter 2008 new commercial lines business written directly by agencies, up 6.0 percent from \$72 million in last year's third quarter. Nine-month new business rose 6.3 percent to \$229 million from \$216 million.
- Improved third-quarter 2008 combined ratio despite 3.8 percentage-point rise in the contribution of catastrophe losses. Savings from favorable development on prior year reserves rose substantially.
- Higher nine-month 2008 combined ratio primarily due to 5.5 percentage-point rise in the contribution of catastrophe losses. Other factors contributing to the change in the ratio were higher savings from favorable development on prior year reserves, lower pricing, normal loss cost inflation and higher underwriting expenses. Lower commission expenses partially offset these increases.
- Higher savings from favorable development on prior year reserves continued to reflect fluctuations in savings for the commercial casualty line of business.

## Personal Lines Insurance Operations

(Dollars in millions)	Three months ended September 30,			Nine months ended September 30,		
	2008	2007	Change %	2008	2007	Change %
Written premiums . . . . .	\$ 184	\$ 192	(4.0)	\$ 525	\$ 542	(3.1)
Earned premiums . . . . .	\$ 167	\$ 177	(5.4)	\$ 518	\$ 538	(3.6)
Loss and loss expenses excluding catastrophes	111	116	(4.1)	328	341	(3.8)
Catastrophe loss and loss expenses . . . . .	40	12	222.3	107	11	858.0
Commission expenses . . . . .	32	33	(2.1)	103	110	(5.8)
Underwriting expenses . . . . .	22	23	(2.5)	62	68	(9.1)
Underwriting profit (loss) . . . . .	\$ (38)	\$ (7)	(457.8)	\$ (82)	\$ 8	nm
Ratios as a percent of earned premiums:						
Loss and loss expenses excluding catastrophes	66.3%	65.4%		63.2%	63.3%	
Catastrophe loss and loss expenses . . . . .	23.8	7.0		20.7	2.1	
Loss and loss expenses . . . . .	90.1	72.4		84.0	65.4	
Commission expenses . . . . .	19.4	18.7		19.9	20.4	
Underwriting expenses . . . . .	12.9	12.7		12.0	12.6	
Combined ratio . . . . .	122.5%	103.8%		115.9%	98.6%	
Reserve development impact on loss and loss expense ratio . . . . .	9.1%	4.0%		5.1%	4.6%	

- 4.0 percent and 3.1 percent declines in third-quarter and nine-month 2008 personal lines net written premiums due to lower policy counts and pricing changes that reduced premiums per policy. Higher new personal lines business partially offset those factors.
- \$11 million in third-quarter 2008 personal lines new business written directly by agencies, up 11.8 percent from \$10 million in last year's third quarter. Nine-month new business rose 6.7 percent to \$30 million from \$28 million.
- 18.7 percentage-point rise in third-quarter 2008 combined ratio largely due to higher catastrophe losses. In addition to catastrophes, lower pricing and normal loss cost inflation continued to weigh on homeowner results. However, the loss and loss expense ratio for the largest line of business in this segment, personal auto, remained very healthy.
- Higher savings from favorable development on prior year reserves continue to reflect normal fluctuations in savings for the other personal line of business, which includes personal umbrella liability coverages.



## Life Insurance Operations

(In millions)	Three months ended September 30,			Nine months ended September 30,		
	2008	2007	Change %	2008	2007	Change %
Written premiums .....	\$ 44	\$ 39	13.9	\$ 135	\$ 126	6.7
Earned premiums .....	\$ 30	\$ 34	(12.2)	\$ 93	\$ 99	(6.8)
Investment income, net of expenses .....	30	28	5.0	89	85	4.3
Other income .....	0	1	(103.7)	1	4	(61.7)
Total revenues, excluding realized investment gains and losses .....	60	63	(6.1)	183	188	(2.8)
Contract holders benefits .....	41	36	11.5	115	98	16.7
Expenses .....	11	15	(21.7)	33	44	(25.2)
Total benefits and expenses .....	52	51	1.9	148	142	3.7
Net income before income tax and realized investment gains and losses .....	8	12	(38.8)	35	46	(23.0)
Income tax .....	3	4	(36.2)	12	16	(22.0)
Net income before realized investment gains and losses .....	\$ 5	\$ 8	(40.1)	\$ 23	\$ 30	(23.6)

- \$135 million in total nine-month 2008 life insurance segment net written premiums. Written premiums include life insurance, annuity and accident and health premiums.
- 3.8 percent increase to \$108 million in nine-month 2008 written premiums for life insurance products in total.
- 23.3 percent increase to \$23 million in nine-month 2008 written premiums for fixed annuity products.
- 9.8 percent rise to \$58 million in nine-month 2008 term life insurance written premiums, reflecting marketing advantages of competitive, up-to-date products, personal service and policies backed by financial strength.

- 4.9 percent rise in face amount of life policies in force to \$64.901 billion at September 30, 2008, from \$61.875 billion at year-end 2007.
- \$7 million decrease in nine-month 2008 operating profit, primarily due to less favorable mortality experience.
- During 2008, the LifeHorizons term insurance product was redesigned and a new 20-year term worksite product was introduced. These improvements support opportunities to cross-sell life insurance products to clients of the independent agencies that sell Cincinnati's property casualty insurance policies.

## Investment and Balance Sheet Highlights

### Investment Operations

(In millions)	Three months ended September 30,			Nine months ended September 30,		
	2008	2007	Change %	2008	2007	Change %
Investment income:						
Interest .....	\$ 83	\$ 77	6.8	\$ 238	\$ 229	3.8
Dividends .....	46	75	(38.9)	169	219	(22.8)
Other .....	3	4	(7.3)	10	11	(4.0)
Investment expenses .....	(2)	(4)	52.2	(5)	(8)	37.8
Total investment income, net of expenses .....	130	152	(14.5)	412	451	(8.5)
Investment interest credited to contract holders .....	(16)	(14)	(10.7)	(47)	(43)	(10.4)
Realized investment gains and losses summary:						
Realized investment gains and losses .....	401	20	nm	441	371	19.1
Change in fair value of securities with embedded derivatives .....	(8)	(3)	(174.8)	(13)	1	nm
Other-than-temporary impairment charges .....	(121)	(1)	nm	(400)	(2)	nm
Total realized investment gains and losses .....	272	16	nm	28	370	(92.4)
Investment operations income .....	\$ 386	\$ 154	151.6	\$ 393	\$ 778	(49.4)

- 14.5 percent and 8.5 percent declines in third-quarter and nine-month 2008 pretax net investment income, primarily due to dividend reductions of financial sector common and preferred holdings, including reductions earlier in the year on positions subsequently sold or reduced.
- Third-quarter pretax realized investment gains of \$272 million included \$401 million in net gains from investment sales and bond calls. These gains included \$360 million from sales of 38 million shares of Fifth Third, \$112 million from the sale of other financial stocks and \$27 million from the sale of various non-financial common stock holdings. These gains were partially offset by realized losses of \$80 million, primarily from the sales of certain distressed bonds and preferred shares in the financial sector.
- Third-quarter pretax realized investment gains of \$272 million achieved despite \$121 million in non-cash charges for other-than-temporary impairments, which included \$47 million to write down preferred shares of Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation. Total third-quarter charges represented 1.2 percent of invested assets.
- Impairments of equity securities accounted for more than 80 percent of total nine-month other-than-temporary impairment charges, reflecting the portfolio mix, the historic weighting in financial sector securities and the unprecedented decline in overall stock market values during 2008.

(Dollars in millions except share data)

	At September 30, 2008	At December 31, 2007
<b>Balance sheet data</b>		
Invested assets . . . . .	\$ 10,160	\$ 12,261
Total assets . . . . .	14,303	16,637
Short-term debt . . . . .	69	69
Long-term debt . . . . .	791	791
Shareholders' equity . . . . .	4,687	5,929
Book value per share . . . . .	28.87	35.70
Debt-to-capital ratio . . . . .	15.5%	12.7%

	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
<b>Performance measures</b>				
Comprehensive income (loss) . . . . .	\$ 41	\$ (149)	\$ (927)	\$ 30
Return on equity, annualized . . . . .	21.0%	7.4%	6.7%	13.4%
Return on equity, annualized, based on comprehensive income (loss) . . . . .	3.5	(8.9)	(23.3)	0.6

- \$10.160 billion in investment assets at September 30, 2008, compared with \$10.379 billion at June 30, 2008. Cash and equivalents at \$347 million at quarter-end, compared with \$333 million at June 30.
- Shareholders' equity was \$4.687 billion, or \$28.87 per share, at September 30, 2008, essentially unchanged from June 30, 2008, but down from year-end 2007 due to declines in investment values during the first six months of 2008.
- \$5.941 billion A1/A+-average rated bond portfolio at September 30, 2008, containing a diverse mix of taxable and tax-exempt securities.
- \$4.137 billion equity portfolio includes \$1.737 billion in pretax unrealized gains.
- \$3.687 billion in statutory surplus for the property casualty insurance group at September 30, 2008, compared with \$3.650 billion at June 30, 2008. The ratio of common stock to statutory surplus for the property casualty insurance group portfolio was 67.5 percent at September 30, 2008, compared with 86.0 percent at year-end 2007.
- No repurchases of common stock during the third quarter. Approximately 8.5 million shares remain authorized for repurchase.

For additional information or to hear a replay of the October 29 conference call webcast, please visit [www.cinfin.com/investors](http://www.cinfin.com/investors).

**Cincinnati Financial Corporation**  
**Condensed Balance Sheets and Statements of Income (unaudited)**

(Dollars in millions)

	September 30, 2008	December 31, 2007
<b>Assets</b>		
Investments .....	\$ 10,160	\$ 12,261
Cash and cash equivalents .....	347	226
Premiums receivable .....	1,103	1,107
Reinsurance receivable .....	846	754
Other assets .....	1,847	2,289
Total assets .....	<u>\$ 14,303</u>	<u>\$ 16,637</u>
<b>Liabilities</b>		
Insurance reserves .....	\$ 5,719	\$ 5,445
Unearned premiums .....	1,583	1,564
Deferred income tax .....	236	977
6.125% senior notes due 2034 .....	371	371
6.9% senior debentures due 2028 .....	28	28
6.92% senior debentures due 2028 .....	392	392
Other liabilities .....	1,287	1,931
Total liabilities .....	<u>9,616</u>	<u>10,708</u>
<b>Shareholders' Equity</b>		
Common stock and paid-in capital .....	1,456	1,442
Retained earnings .....	3,482	3,404
Accumulated other comprehensive income .....	956	2,151
Treasury stock .....	(1,207)	(1,068)
Total shareholders' equity .....	<u>4,687</u>	<u>5,929</u>
Total liabilities and shareholders' equity .....	<u>\$ 14,303</u>	<u>\$ 16,637</u>

(Dollars in millions except per share data)

	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
<b>Revenues</b>				
Earned premiums .....	\$ 781	\$ 811	\$ 2,355	\$ 2,447
Investment income, net of expenses .....	130	152	412	451
Realized investment gains and losses .....	272	16	28	370
Other income .....	3	3	11	15
Total revenues .....	<u>1,186</u>	<u>982</u>	<u>2,806</u>	<u>3,283</u>
<b>Benefits and Expenses</b>				
Insurance losses and policyholder benefits .....	563	559	1,693	1,533
Commissions .....	130	136	428	466
Other operating expenses .....	137	127	365	345
Total benefits and expenses .....	<u>830</u>	<u>822</u>	<u>2,486</u>	<u>2,344</u>
Income Before Income Taxes .....	356	160	320	939
Provision for Income Taxes .....	109	36	52	270
<b>Net Income</b> .....	<u>\$ 247</u>	<u>\$ 124</u>	<u>\$ 268</u>	<u>\$ 669</u>
<b>Per Common Share:</b>				
Net income-basic .....	\$ 1.51	\$ 0.72	\$ 1.64	\$ 3.89
Net income-diluted .....	\$ 1.50	\$ 0.72	\$ 1.64	\$ 3.86

# Other News Releases

## Cincinnati Financial Corporation Declares Regular Quarterly Cash Dividend

**Cincinnati, August 18, 2008 – Cincinnati Financial Corporation (Nasdaq: CINF)** today announced that the board of directors has declared a 39 cents per share regular quarterly cash dividend payable October 15, 2008, to shareholders of record as of September 19, 2008. The current dividend level reflects the 9.9 percent increase in the quarterly dividend rate announced by the board in February. That action set the stage for the 48<sup>th</sup> consecutive increase in the annual cash dividend.

Kenneth W. Stecher, president and chief executive officer, commented, “The board declared another quarterly cash dividend at the level established in February. The board supports

management’s view that our solid insurance operations will continue to contribute to our earnings and that our investment operations can sustain our financial position. The board indicated that its intention remains to continue rewarding shareholders with cash dividends that rise consistently.

“Our capital position and cash flow continue to support our current cash dividend payout. We expect the company’s performance will allow these measures to remain at a level that provides our board the flexibility to consider future increases for our shareholders,” Stecher said.

## Inside Cincinnati

Since our last *Letter to Shareholders*, these associates merited promotions:

Andy Agerton, AIC – Senior Claims Representative

Lori Bagoly – Underwriting Superintendent

Rich Balestra, CFA – Portfolio Manager

Erin Barlow, API – Underwriting Specialist

Cary Barrow, AFSB – Senior Underwriting Specialist

Vanessa Barry – Senior Claims Specialist

Scott Beckman – Underwriting Specialist

Kevin Beykirch – Regional Director

Marle Billman – Associate Superintendent, Casualty Claims

Chris Boydston, AIC – Senior Claims Representative

Bradley Boyett – Underwriting Superintendent

Sheri Bugher, AIC – Associate Superintendent, Casualty Claims

Sandy Burden, CISA – Group Manager, I.T. Portfolio Management/Architecture

Kristie Bushman – Underwriting Superintendent

Bill Chandler, AIM – Assistant Territory Manager

Dawn Chapel, CPCU, APA, ARe, AU – Chief Underwriting Specialist

Sarah Chiasson – Underwriting Superintendent

Jennifer Conklin, AIM, AIS – Underwriting Specialist

David Conlon, AIC – Senior Claims Representative

Thomas Dameron – Chief Underwriting Specialist

Gregory DePew, CFA – Portfolio Manager

Chris Draper, CPCU, AU – Underwriting Superintendent

James Ducar – Senior Claims Examiner

Rocky Edwards – Senior Claims Specialist

David Ellis, AIC – Claims Specialist

Angie Engelke – Chief Underwriting Specialist

Kyle Fader, AIC – Senior Claims Representative

Carol Fuller – Senior Claims Examiner

Todd Gagnon, API – Underwriting Specialist

Matt Gardner, AIC, AIM – Senior Claims Representative

Thomas Goodwin, AAI, AIM, AIS, ASLI, AU – Underwriting Specialist

Ryan Gustafson, AIC – Claims Specialist

Jenny Harvey – Systems Analyst

Christopher Heldman – Senior Analyst

Rusty Hymer – Chief Underwriting Specialist

Nicole Ippolito, AIC – Claims Specialist

John James, AIC, SCLA – Field Claims Superintendent

Phil Jankowski, CPCU – Senior Claims Representative

Scott Jeschke, AIC – Claims Specialist

Craig Johnson – Superintendent, Casualty Claims  
 Nolan Joseph – Claims Specialist  
 Adam Kadish – Programmer  
 Kathy Kerr, AIC – Senior Claims Representative  
 Keith Klatt, AIC – Claims Specialist  
 Gregory Knifley, CPCU – Underwriting Specialist  
 Joy Knifley – Underwriting Specialist  
 Mary Kretchmer, AIC – Field Claims Superintendent  
 Michael Kuhl, AIS – Senior Analyst  
 Art Leatham – Senior Machinery & Equipment Specialist  
 Laura Lewis, CPCU, AIM, AIS, API, ARe – Underwriting Specialist  
 Lynn Lilly – Manager, Payroll  
 Donnie Lowery – Associate Superintendent, Surveillance  
 Robert Lozo, AIC – Senior Claims Specialist  
 John Luebke, CPCU, AIC, AIM, SCLA – Field Claims Manager  
 Ernie Macke, PMP – Senior Project Manager  
 Dan Mays, CPCU, AIC, AIM, ARM, CIC, CRM – Senior Loss Control Consultant  
 Bill McCullough – Chief Underwriting Specialist  
 Michael McGuire, CPCU – Senior Underwriting Specialist  
 Dana McKenzie, AIC – Senior Claims Representative  
 Steve Mikesell – Senior Underwriter  
 Paul Miller, CPCU, AIM, APA, API, AU – Underwriting Superintendent  
 Tracy Miller, CPCU, CPIW, AIC – Senior Claims Specialist  
 Julie Montgomery – Senior Claims Representative  
 David Morel – P&C Senior Actuarial Analyst  
 Suzi Morgan – Manager, Machinery & Equipment Support  
 Laura Nickol – Underwriting Director, Field  
 Shawn Niehaus, CPCU, AIM, ARe – Underwriting Specialist  
 Doug Nordhausen – System Engineer  
 Jeffrey O’Leary, AIC – Claims Specialist  
 Nick Orgill – Claims Specialist  
 Roxanna Otto, AIS – Underwriting Superintendent  
 Heather Paul, CPCU – Underwriting Superintendent  
 Nathan Perry II, API – Underwriting Specialist  
 Joseph Pierro, AU – Underwriting Specialist  
 Wayne Pinney – Machinery & Equipment Field Manager  
 Sandy Pohlman, CPCU, ARC – Regulatory Specialist  
 Toni Postell – Supervisor, Workers’ Compensation Claims  
 Bob Rook, AU – Chief Underwriting Specialist  
 Duane Russell – Claims Specialist  
 Christina Scherpenberg – Senior Accountant  
 Andrew Schnell – Manager, Corporate Accounting  
 Jeff Shive, CPCU, AIM, AIC – Field Claims Manager  
 Laura Siebert, API – Underwriting Superintendent  
 Jill Slater – Programmer Analyst  
 Mike Slusser – Senior Claims Representative  
 Sue Smith – Senior Systems Analyst  
 Paul Snyder, AIS – Underwriting Specialist  
 Jeff Spangler, CPCU, CSP – Loss Control Field Director  
 Melissa Stegmaier, AIC, AIS, SCLA – Senior Claims Representative  
 Katie Stickel – Claims Specialist  
 Cathy Story, CPCU, APA – Senior Auditor  
 Tim Tiernan – Senior Business Analyst  
 Donna Vanover – Diamond Systems Specialist  
 Ernie Wang – Programmer  
 Shannon Ward – Diamond Systems Specialist  
 Jennifer Whitmer, AIS – Senior Personnel Specialist  
 Suzanne Wilkerson – Specialist, I.T. Administration  
 Steve Wilsbacher, AIC – Senior Claims Specialist  
 Michael Wood, CPCU, CPA, CIA, AIAF – Manager, Accounting & Agency Services  
 Dawn Woodrick, CPCU – Underwriting Superintendent  
 Kip Zepf – Senior Programmer

## Professional Development

Agents of Cincinnati Insurance have a new tool to develop educational plans for their staff. Modeled after popular GPS navigation devices, the Agency Development Roadmap helps agencies plan a route to success for each member of their agency team. The roadmap includes checklists to customize training in areas such as personal effectiveness skills, desktop computing efficiency, general insurance or specific knowledge of commercial and personal lines products.

On December 1, 2008, our Education & Training department is changing its name to Learning & Development. Our new name better reflects our philosophy – continuing education works best when the learner values and initiates it. Whether our associates or agents want to conquer a new subject or add deeper layers of understanding to a professional topic they are familiar with, the Learning & Development department is committed to delivering the tools they need.

We encourage and reward associates who continue their professional insurance education, earning credentials by meeting high academic, ethical and length-of-experience standards. Congratulations to the following associates who completed a series of courses to earn a designation; Jeff Poe, Chartered

Property Casualty Underwriter (CPCU); Sandy Burden, Certified Information Systems Auditor (CISA); Luana Dillingham, Fellow, Life Management Institute (FLMI); Steve Dunn, Michelle Gregov, Kevin Gullette and Michael Leininger, Certified Insurance Counselor (CIC); Deborah Naegele, Certified Life Underwriter (CLU); and Nieata Bailey, Mona Helton and Sherry Meyer, Certified Professional Insurance Women (CPIW).

The ABC Award recognizes exemplary productivity, service and quality in exceptional associates. The ABC Award committee recently granted the quarterly Above and Beyond the Call (ABC) award to Shawn Niehaus, CPCU, AIM, ARe, Underwriting Specialist, and Darin Riley, Policy Service Specialist. Congratulations to these quarterly winners! At the Queen City Club on October 29, Robert Meyer, Systems Engineer, was named ABC of The Year. This honor is awarded annually to just one of the quarterly winners. Bob's ingenuity was key to identifying and resolving a problem with a recent software upgrade. He worked extended hours to make the necessary repairs while maintaining system availability. Bob is a consistent performer whose dedication to his job, teammates and customers earn the respect of those around him.

## Financial Services

The company's three financial services subsidiaries continue to support our insurance relationships and broaden our offerings. As of September 30, 2008, CFC Investment Company, which offers equipment and vehicle leases and loans, reported 2,253 accounts representing \$74 million in net receivables. CinFin Capital Management Company, which offers asset management services, reported \$858 million under management in 52 accounts. During the first nine months of 2008, The Cincinnati Specialty Underwriters Insurance Company and our wholly owned brokerage, CSU Producer Resources Inc., have

begun marketing excess and surplus lines insurance in 23 states, remaining on track to have these products available in 33 active states before year-end. Cincinnati Specialty Underwriters has added the property line of business in five states and will continue to introduce new lines of business throughout the remainder of the year, including miscellaneous professional and excess casualty. Availability of CSU's new offerings has enhanced your company's ability to write new standard market property casualty business, as we work with agents to round out accounts that require both admitted and nonadmitted market solutions.

## Public Responsibility

The effectiveness of state-based insurance regulation is again the subject of debate after the federal assistance recently extended to parts of the financial services sector, including some organizations with insurance operations. Advocates for federal regulation of insurance suggest that federal oversight of the insurance industry could have avoided the need for this assistance. Representatives of the National Association of Insurance Commissioners recently testified in Congress that state insurance regulators had no jurisdiction over any of the financial services companies that recently reached the brink of failure. Further, they stated that none of the pending optional federal

charter proposals would give that jurisdiction to proposed federal insurance regulators. NAIC representatives also testified that the state-regulated insurance industry continues to face more stringent investment restrictions and capital-to-surplus requirements than the federally-regulated financial services sector.

Policyholder risks and coverage needs vary because of diverse geographic, climatic and economic conditions. We continue to believe that state regulators are in the best position to respond with regulations and insurance products that consider that diversity.

# Cincinnati Financial Corporation Safe Harbor

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 2007 Annual Report on Form 10-K, Item 1A, Risk Factors, Page 21. Although we often review and update our forward-looking statements when events warrant, we caution our readers that we undertake no obligation to do so.

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
  - 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:
    - Multi-notch downgrades of the company’s financial strength ratings
    - Concerns that doing business with the company is too difficult or
    - Perceptions that the company’s level of service, particularly claims service, is no longer a distinguishing characteristic in the marketplace
  - Further decline in overall stock market values negatively affecting the company’s equity portfolio and book value; in particular further declines in the market value of financial sector stocks
  - Securities laws that could limit the manner, timing and volume of our investment transactions
  - Events, such as the credit crisis triggered by subprime mortgage lending practices, that lead to:
    - Significant decline in the value of a particular security or group of securities, such as our financial sector holdings, 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
  - Recession or other economic conditions or regulatory, accounting or tax changes resulting in lower demand for insurance products
  - 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
  - Inaccurate estimates or assumptions used for critical accounting estimates
  - 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
  - Changing consumer buying habits and consolidation of independent insurance agencies that could alter our competitive advantages
  - Increased frequency and/or severity of claims
  - Delays or inadequacies in the development, implementation, performance and benefits of technology projects and enhancements
  - Ability to obtain adequate reinsurance on acceptable terms, amount of reinsurance purchased, financial strength of reinsurers and the potential for non-payment or delay in payment by reinsurers
  - Increased competition that could result in a significant reduction in the company’s premium growth rate
  - Underwriting and pricing methods adopted by competitors that could allow them to identify and flexibly price risks, which could decrease our competitive advantages
  - Personal lines pricing and loss trends that lead management to conclude that this segment could not attain sustainable profitability, which could prevent the capitalization of policy acquisition costs
  - Actions of insurance departments, state attorneys general or other regulatory agencies that:
    - Restrict our ability to exit or reduce writings of unprofitable coverages or lines of business
    - Place the insurance industry under greater regulatory scrutiny or result in new statutes, rules and regulations
    - Increase our expenses
    - 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
    - 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
  - 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, terrorism or construction delays, 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, 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 recent measures affecting corporate financial reporting and governance. The ultimate changes and eventual effects, if any, of these initiatives are uncertain.

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## Contact Information

Communications directed to the company's secretary, Steven J. Johnston, chief financial officer, are shared with the appropriate individual(s). Or, you may directly access services:

**Investors:** Investor Relations responds to investor inquiries about Cincinnati Financial Corporation and its performance.  
Heather J. Wietzel – Vice President, Investor Relations  
513-870-2768 or [investor\\_inquiries@cinfin.com](mailto:investor_inquiries@cinfin.com)

**Shareholders:** Shareholder Services provides stock transfer services, fulfills requests for shareholder materials and assists registered shareholders who wish to update account information or enroll in shareholder plans.  
Jerry L. Litton – Assistant Vice President, Shareholder Services  
513-870-2639 or [shareholder\\_inquiries@cinfin.com](mailto:shareholder_inquiries@cinfin.com)

**Media:** Corporate Communications assists media representatives seeking information or comment from Cincinnati Financial Corporation or its subsidiaries.  
Joan O. Shevchik, CPCU, CLU – Senior Vice President, Corporate Communications  
513-603-5323 or [media\\_inquiries@cinfin.com](mailto:media_inquiries@cinfin.com)

### Cincinnati Financial Corporation

The Cincinnati Insurance Company  
The Cincinnati Casualty Company  
The Cincinnati Indemnity Company  
The Cincinnati Specialty Underwriters Insurance Company

The Cincinnati Life Insurance Company  
CSU Producer Resources Inc.  
CFC Investment Company  
CinFin Capital Management Company

#### Mailing Address:

P.O. Box 145496  
Cincinnati, Ohio 45250-5496

Phone: 513-870-2000

Fax: 513-870-2066

[www.cinfin.com](http://www.cinfin.com)

#### Street Address:

6200 South Gilmore Road  
Fairfield, Ohio 45014-5141





# Cincinnati Financial Corporation

## 2008 Second-quarter Letter to Shareholders

August 13, 2008

### To Our Shareholders, Friends and Associates:

You may be surprised by the sheer pace of your company's changes during the second quarter.

One announcement quickly followed the other, as you'll read inside this document. You'll learn that your company has entered the second half of 2008 with a new president and chief executive officer who advanced through our ranks; with higher catastrophe losses at the six-month mark than we generally have all year; with a significant rebalancing of our equity portfolio through a partial sale of our largest holding; and yet with only modest changes to our outlook for full-year 2008.

It started with good news in mid-June, when we made executive transitions in normal course. As Jim Benoski moved toward retirement, we acted to assure continuity and to advance plans to prepare our next generation of leaders. We believe our local independent agency customers are best served when we attract and retain dedicated people, expose them broadly to our operations and round out their experience to increase their effectiveness. Good people have always been and will continue to be the source of Cincinnati's strengths.

As we prepared internally for these positive changes, we didn't know that external forces would also lead to other changes in the same time frame. During the second quarter, we experienced record catastrophe losses along with lower investment asset values and investment income, all leading to risk management concerns and downgrades by two ratings agencies. Then, in July, we announced another big change – our sale of slightly more than half of our long-held Fifth Third common stock holding that had reduced its dividend payable.

After all these changes, you may ask: What comes next? Is Cincinnati still the same company I chose to invest in and trusted to increase my shareholder dividends and shareholder value over the long term?

Ken Stecher accepted the role of president and chief executive officer because he saw an incredible opportunity to lead a company with a culture and reputation for integrity, strength and points of difference that give us advantages in the marketplace. He'll see that it remains the same company you selected – ethical, conservative and based on personal relationships and trust.

We all believe in Cincinnati's unique, agent-centered mission and proven strategies. They have benefited many people, from shareholders and policyholders to agents, associates and claimants. They will never go out of style. We'll be applying those strategies as external conditions evolve, whether that means competition or weather or economic and insurance cycles.

With support from our capable executive team, our agents and associates, Ken intends to honor those who put your company in his hands by meeting two goals that allow us to preserve and expand on our mission:

- On the financial side, we stabilized our capital and are establishing policies to preserve that stability over the coming generations. Our investment philosophy stands; we will continue to balance near-term income generation with the potential for long-term book value growth.
- On the insurance side, our priority is to increase ease of doing business for our agencies, both by advancing our technology and by leveraging our local presence and decision making in their communities.

Together, we'll preserve Cincinnati's strengths and change what needs to be changed. What we do not see changing now or in the future is the contribution of our solid insurance operations to our earnings; our ability to sustain a strong capital position and produce strong cash flow; and our board's intention to reward shareholders with cash dividends that rise year after year.

Sincerely,

/S/ John J. Schiff, Jr.

John J. Schiff, Jr., CPCU  
Chairman of the Board

/S/ James E. Benoski

James E. Benoski  
Vice Chairman

/S/ Kenneth W. Stecher

Kenneth W. Stecher  
President and  
Chief Executive Officer

In 2008, we are offering shareholders the same types of information about our company as in prior years, but on a different schedule. As each item is published, it appears on our Web site, [www.cinfin.com](http://www.cinfin.com), in an integrated annual report format. Many items will be available to you earlier than you received them in the past, because you no longer have to wait until all sections of our annual report are printed. Items available now are titled in color, and those coming soon are titled in gray.

## About the Company

Cincinnati Financial meets the needs of agencies and policyholders through our insurance group and three complementary subsidiaries:

**The Cincinnati Insurance Company** leads our A++ A.M. Best-rated standard market property casualty insurance group, which includes **The Cincinnati Casualty Company** and **The Cincinnati Indemnity Company**. This group markets a broad range of business, homeowner and auto policies through our select group of local independent insurance agencies in 34 states. These companies support each agency's ability to provide exceptional value and service to the people and businesses in its community. Our local field representatives work out of their homes, customizing products to meet policyholder needs, responding personally and promptly to claims and strengthening relationships.

Two other subsidiaries of The Cincinnati Insurance Company also market insurance products. **The Cincinnati Life Insurance Company**, rated A+ by A.M. Best, markets life insurance policies, disability income policies and annuities. **The Cincinnati Specialty Underwriters Insurance Company**, rated A by A.M. Best, began offering excess and surplus lines insurance products in 2008.

Three subsidiaries of Cincinnati Financial support our insurance operations. **CSU Producer Resources Inc.** offers insurance brokerage services to our independent agencies to support their access to Cincinnati Specialty Underwriters. **CFC Investment Company** offers commercial leasing and financing services to our agents and their clients. **CinFin Capital Management Company** provides asset management services to institutions, corporations and nonprofit organizations.

## 2007 Fourth-quarter and Full-year Letter to Shareholders – mid-February 2008

This message from our chairman and our president includes recent news releases about financial results announced February 6 and actions taken by the board of directors at its February 1 meeting. *The Cincinnati Experience*, a profile of our operating philosophy, accompanies this letter.

## The Cincinnati Experience – mid-February 2008

The Cincinnati Insurance Company, Cincinnati Financial Corporation's lead subsidiary, ranks among the top 25 U.S. property casualty insurer groups based on net written premiums. In *The Cincinnati Experience*, you'll read about how our relationship-based approach creates value and loyalty, supporting premium growth.

## 2007 Annual Report on Form 10-K – late-February 2008

The *Annual Report on Form 10-K* is a detailed document published by every publicly traded company as required by the U.S. Securities and Exchange Commission. In our report, we describe your company's operations, its results and trends, along with supporting data, discussions, audited financial statements and accompanying notes.

## 2008 Shareholder Meeting Notice and Proxy Statement – mid-March 2008

This statement informs you of items requiring shareholder action at the 2008 Annual Meeting of Shareholders on May 3, 2008. It identifies board members, detailing director and executive officer compensation and board activities. Notice cards, mailed in March, tell how to easily obtain the *Proxy Statement* and vote.

## Chairman and President's Letter – late-March 2008

Accompanying the Proxy Statement are the 2007 condensed balance sheets and income statements, six years of summary financial data and an annual message from our chairman and our president. Their letter presents management's perspectives on your company's 2007 performance and trends that may affect performance in 2008 and beyond.

## First-quarter 2008 Letter to Shareholders – mid-May 2008

This message from our chairman and our president includes recent news releases about financial results announced April 30, results of shareholder votes at the 2008 Annual Meeting of Shareholders and actions of the board at its May meeting. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by May 12, 2008.

## Second-quarter 2008 Letter to Shareholders – mid-August 2008

This executive perspective includes our August 6 news release with financial results. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by August 11, 2008.

## Third-quarter 2008 Letter to Shareholders – mid-November 2008

This executive perspective includes our October 29 news release with financial results. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by November 10, 2008.

# Recent News Releases

## Cincinnati Financial Reports Second-quarter 2008 Profit

**Cincinnati, August 6, 2008 – Cincinnati Financial Corporation (Nasdaq: CINF) today reported:**

- Net income at \$63 million, or 38 cents per share in the second quarter of 2008, compared with net income of \$351 million, or \$2.02 per share, in the second quarter of 2007. A return to profitability in the second quarter after the first quarter loss brought six-month net income per share to 13 cents compared with \$3.13 last year. Realized capital losses were significantly lower in the second quarter compared with first-quarter 2008.
- Operating income\* at \$69 million, or 42 cents per share, in the second quarter of 2008, compared with \$164 million, or 94 cents per share, in the comparable 2007 period. Record catastrophe losses reduced second-quarter operating income by 45 cents per share compared with 4 cents per share in last year's second quarter. Six-month operating income at \$1.08 per share included a 62 cent impact from catastrophe losses compared with \$1.82 per share including a 5 cent impact.
- Atypically high catastrophe losses of \$113 million resulted in a consolidated property casualty underwriting loss of \$27 million in this year's second quarter.

### Financial Highlights

(Dollars in millions except share data)

	Three months ended June 30,			Six months ended June 30,		
	2008	2007	Change %	2008	2007	Change %
<b>Revenue Highlights</b>						
Earned premiums	\$ 794	\$ 822	(3.3)	\$ 1,575	\$ 1,637	(3.8)
Investment income	130	150	(13.4)	282	298	(5.5)
Total revenues	917	1,270	(27.8)	1,621	2,301	(29.6)
<b>Income Statement Data</b>						
Net income	\$ 63	\$ 351	(82.0)	\$ 21	\$ 545	(96.2)
Net realized investment gains and losses	(6)	187	(103.9)	(157)	228	(169.0)
Operating income*	\$ 69	\$ 164	(57.6)	\$ 178	\$ 317	(43.8)
<b>Per Share Data (diluted)</b>						
Net income	\$ 0.38	\$ 2.02	(81.2)	\$ 0.13	\$ 3.13	(95.8)
Net realized investment gains and losses	(0.04)	1.08	(103.7)	(0.95)	1.31	(172.5)
Operating income*	\$ 0.42	\$ 0.94	(55.3)	\$ 1.08	\$ 1.82	(40.7)
Book value				\$ 28.99	\$ 39.74	(27.1)
Cash dividend declared	\$ 0.39	\$ 0.355	9.9	\$ 0.78	\$ 0.71	9.9
Weighted average shares outstanding	165,044,463	173,423,572	(4.8)	164,601,462	173,871,612	(5.3)

### Insurance Operations Highlights

- 103.5 percent second-quarter 2008 property casualty combined ratio, compared with 88.6 percent for the 2007 second-quarter. The most significant reason for the increase was the 13.5 percentage point rise in the catastrophe loss contribution.
- Decrease in property casualty net written premiums narrowed to 2.5 percent in the second quarter from 8.3 percent in the first quarter, benefiting from \$100 million of new business, with new commercial lines business up 21.2 percent and new personal lines business up 7.7 percent. Pricing remains competitive in both commercial and personal lines. Recently launched excess and surplus lines operations contributed \$4 million of new business since January 1.
- 6 cents per share contribution from life insurance operations to second-quarter operating income, up from 5 cents.

### Investment and Balance Sheet Highlights

- \$130 million of second-quarter pretax investment income compared with \$150 million for the same period last year.

- Book value of \$28.99 per share compared with \$35.70 at year-end 2007. Invested assets and book value declined primarily on lower market values of financial sector and other equity holdings.

### Full-year 2008 Outlook\*\*

- Property casualty net written premium target unchanged. Competitive pricing could lead to full-year 2008 premiums declining as much as 5 percent.
- Combined ratio could rise above 100 percent due to high catastrophe losses, as recently announced.
- Expected lower investment income now estimated to be as much as 10 percent below the 2007 level due to lower anticipated dividends from common stocks and the lower number of Fifth Third Bancorp (NASDAQ:FITB) shares held after recent sale. Portfolio strategies, including reinvestment of proceeds from Fifth Third sale, continue to focus on balancing near-term income generation with long-term book value growth potential.

\* The Definitions of Non-GAAP Information and Reconciliation to Comparable GAAP Measures on [www.cinfin.com](http://www.cinfin.com) defines and reconciles measures presented in this release that are not based on Generally Accepted Accounting Principles or Statutory Accounting Principles.

\*\* Forward-looking statements and related assumptions are subject to the risks outlined in the company's safe harbor statement (see Page 13).

nm Not meaningful

## **Responding to Current Challenges and Positioning for Continued Success**

Kenneth W. Stecher, president and chief executive officer, stated, "Volatile weather patterns and financial markets hampered our results for the first half of 2008. Our strong business relationships and solid financial foundation allowed us to respond confidently and flexibly to these challenges while acting on our promise of prompt and fair claims service.

"Our financial position remains solid, having absorbed costs associated with the severe storms and with declining valuations of holdings in our equity investment portfolio. Independent agents continue to find that our policies are the best match for their better accounts, appreciating the value of our financial strength and our standout service. Over recent months, we repositioned our investment portfolio, improving our risk profile and adding to our long-term prospects for investment income growth and capital appreciation.

"Also looking to the long-term future, we added depth in our next generation of leadership. The executive transitions we announced in June will broaden and round out the experience of our managers. As a team, we are focused on serving our agent customers and achieving continued growth in earnings and book value over the long term. Our capital position and cash flow continue to support our current cash dividend payout and the board's intention to continue our 48-year tradition of annually increasing cash dividends to our shareholders."

## **Results Reflect Core Underwriting Expertise and Strength of Agency Relationships**

Stecher said, "Our second-quarter results were driven by weather-related events that were largely responsible for the rise in our combined ratio over the same quarter last year. Catastrophe losses totaled \$113 million, as we tracked seven events that each contributed \$5 million or more to our loss and loss expenses. These storms caused primarily wind, hail and flood damage to our policyholders across 21 states. Our local claims representatives, assisted by four full teams of volunteer representatives from around the country, have already closed approximately 70 percent of the 3,565 reported claims as of July 31. Agents tell us that this prompt and personal claims service is a source of new business referrals.

"Our agents continued to bring the company quality business that allowed us to underwrite insurance near breakeven levels for the first six months of 2008 despite the high catastrophe losses. Agents and underwriters are working together to select and retain appropriately priced accounts, taking the case-by-case approach that has served us so well through all market and pricing cycles.

"As expected, our net written premiums declined 2.5 percent in the second quarter and a little more than 5 percent during the first half, reflecting competitive industry pricing and disciplined company underwriting. Agents continue to market Cincinnati's advantages to their value-oriented clients, leveraging our customized, multi-year commercial coverage packages, superior claims service and high financial strength ratings."

Stecher continued, "We're seeing a steady flow of new business submissions from agents, some resulting from our rollover initiatives that help agents lower expenses by reducing

the number of carriers they represent. We see substantial growth opportunities in our newer states, and we're planning to appoint our first agencies in Texas before year-end. Plus, we've already appointed 37 new agencies this year in our 34 active states. Historically, in several of those 34 states we marketed commercial policies, but not personal insurance. Now, more of our agencies in more states are able to bring our personal lines products to their valued clients, thanks to technology advances that make our processes easier and more efficient.

"In addition, we expect premium growth to continue benefiting from expansion of our capabilities in excess and surplus lines. During the second quarter, we added property excess and surplus coverages in the five initial states where we already marketed general liability, entered five more states to market general liability and continued planning for marketing in the total of 33 states by year end. These new capabilities allow us to provide both admitted and non-admitted coverage solutions to our agents and their business insurance clients, attracting new standard market property casualty business as agents and businesses that require excess and surplus solutions also look to Cincinnati to provide the complete insurance program.

"At the same time these activities generate growth, they also further diversify our book of business, geographically and by product line, helping us manage risk to improve the stability of our underwriting results and add to our overall financial strength."

## **2008 Property Casualty Outlook Update**

Steven J. Johnston, chief financial officer, commented, "Our updated guidance for full-year 2008 results reflects current market trends and our actual six-month catastrophe loss experience. Unusually high industrywide storm activity through the first half of 2008 may lead to a full-year 2008 combined ratio above 100 percent."

Key assumptions for full-year 2008 combined ratio guidance include:

- Current accident year loss and loss expense ratio excluding catastrophe losses – Will reflect the same market trends that contributed to an increase in this ratio in 2007 and are further pressuring the 2008 ratio. Year-to-date accident year loss ratio excluding catastrophe losses was 66.0 percent compared with 60.9 percent in the first half of 2007. The average accident year loss ratio excluding catastrophe losses was 61.4 percent from 2004 to 2007.
- Catastrophe loss ratio – May contribute up to 9 percentage points to the full-year 2008 combined ratio. Catastrophes are unpredictable for any given year, contributing 10.3 percentage points in the first half of 2008. These losses have contributed on average 3.7 percentage points to the company's combined ratio in the past 10 years, ranging from 2007's low of 0.8 points to 1998's high of 6.1 points.
- Savings from favorable development on prior period reserves – May benefit the full-year 2008 combined ratio by approximately 4 percentage points based on current trends. Net savings from favorable development on prior period reserves improved the 2008 first half combined ratio by 6.6 percentage points, compared with 4.7 points for the same period in 2007.

Even as market conditions soften, management will continue to rely on actual loss experience over the next six months and

on sound actuarial estimation techniques in determining loss and loss expense reserves. Historically, management has targeted loss and loss expense reserves in the upper half of the actuarially established range.

Johnston also said, “Our expectations for premium volume have not changed. Competitive pricing could result in our full-year 2008 net written premiums declining by as much as 5 percent. We continue to maintain our underwriting standards, declining inadequately priced new business and non-renewing selected accounts. Our agents help us target accounts with manageable risk characteristics that support the lower prevailing prices.

“We have updated our investment income guidance based on changes in the equity portfolio in the past 12 months, the reduced level of dividend income anticipated from equity holdings, the investment of insurance operations cash flow and the current portfolio attributes. We now believe that full-year 2008 investment income may decline as much as 10 percent from the 2007 level. This expectation considers Fifth Third’s 66 percent reduction in its quarterly cash dividend in June 2008 and our sale of 35 million shares of Fifth Third in July 2008.”

### Investment Income Declines in the Near-term as We Improve Balance of Growth and Risks

Stecher added, “Investment income declined during the second quarter of 2008 as we received lower cash dividends from several of the financial institution stocks in our equity portfolio, including \$20 million less from Fifth Third. We are working to return to previous levels of investment income by systematically identifying secure sources of interest income as well as common stocks of companies with the potential for growth in earnings

and dividends. Our investment income philosophy stands – to balance near-term income generation with the potential for long-term book value growth.

“Our bond portfolio has held up well in the current challenging environment. As of June 30, the bond portfolio was trading at more than 98 percent of its stated par value. It is a diverse mix of taxable and tax-exempt securities, covering a wide range of sectors, industries and maturities. The fixed income portfolio exceeds by a comfortable margin the \$5.7 billion we currently estimate we will need to pay claims, including those not yet reported to us, that occurred through the end of the second quarter. Looking back over the past 15 years, our property casualty reserve estimate has proven consistently adequate. A prudent view of a continuation of the current economic and credit trends could be expected to lead to further declines in bond portfolio values and potentially to related other-than-temporary impairment charges. Nonetheless, the bond portfolio and our strong record of reserve adequacy are pillars of our financial strength and our high financial strength ratings.

“In recent quarters, we have chosen to sell some or all of our positions in common stocks with reduced dividend growth prospects, including some financial services holdings. In July, we sold 35 million shares, or slightly more than half, of our Fifth Third holding. This decision reflected our recent efforts to better diversify the portfolio, a part of managing our enterprise risk. We anticipate applying to our portfolio of common stocks a set of enhanced investment parameters that our board and investment department currently are considering for adoption. These new parameters would align our investment strategy with specific risk tolerances, thereby improving our ability to identify and respond to changing conditions,” Stecher said.

### Consolidated Property Casualty Insurance Operations

(Dollars in millions)	Three months ended June 30,			Six months ended June 30,		
	2008	2007	Change %	2008	2007	Change %
Written premiums . . . . .	\$ 790	\$ 810	(2.5)	\$ 1,566	\$ 1,656	(5.4)
Earned premiums . . . . .	\$ 761	\$ 787	(3.3)	\$ 1,512	\$ 1,571	(3.8)
Loss and loss expenses excluding catastrophes	445	444	0.1	903	898	0.5
Catastrophe loss and loss expenses . . . . .	113	11	900.6	156	15	973.9
Commission expenses . . . . .	142	151	(6.0)	285	312	(8.5)
Underwriting expenses . . . . .	84	89	(4.5)	177	169	4.6
Policyholder dividends . . . . .	4	2	68.0	7	6	28.9
Underwriting profit . . . . .	\$ (27)	\$ 90	(129.7)	\$ (16)	\$ 171	(109.5)
Ratios as a percent of earned premiums:						
Loss and loss expenses excluding catastrophes	58.4%	56.5%		59.7%	57.2%	
Catastrophe loss and loss expenses . . . . .	14.9	1.4		10.3	0.9	
Loss and loss expenses . . . . .	73.3%	57.9%		70.0%	58.1%	
Commission expenses . . . . .	18.6	19.2		18.9	19.8	
Underwriting expenses . . . . .	11.0	11.2		11.7	10.8	
Policyholder dividends . . . . .	0.6	0.3		0.5	0.4	
Combined ratio . . . . .	103.5%	88.6%		101.1%	89.1%	

- 2.5 percent and 5.4 percent declines in second-quarter and six-month 2008 property-casualty net written premiums, reflecting softer pricing and disciplined underwriting.
- \$100 million in second-quarter 2008 new business written directly by agencies, up 22.8 percent from \$81 million in last year's second quarter.
- \$4 million in first-half net written premiums from excess and surplus lines operations launched in January 2008.
- 1,110 agency relationships with 1,354 reporting locations marketed property casualty insurance products at June 30, 2008, up from 1,092 agency relationships with 1,327 reporting locations at year-end 2007.
- 103.5 percent second-quarter and 101.1 percent six-month 2008 GAAP combined ratios. Increase in both periods primarily due to higher catastrophe losses.
- Second-quarter 2008 combined ratio increased 14.9 percentage points from the 2007 second quarter. The increase reflected a 13.5 percentage point higher contribution from catastrophe losses and a 4.6 percentage point higher contribution from losses and case reserve increases greater than \$250,000 as well as the effect of softer pricing and normal loss cost inflation. These increased losses were partially offset by an 11.4 percentage point higher savings from favorable development on prior period reserves.
- \$113 million in second-quarter 2008 catastrophe losses, due primarily to wind, hail and flood damage from storms in the South and Midwest.

### Catastrophe Loss and Loss Expenses Incurred

(In millions, net of reinsurance)

Dates	Cause of loss	Region	Three months ended June 30,			Six months ended June 30		
			Commercial lines	Personal lines	Total	Commercial lines	Personal lines	Total
<b>2008</b>								
Jan. 4-9	Wind, hail, flood, freezing	South, Midwest	\$ 0	\$ 0	\$ 0	\$ 3	\$ 3	\$ 6
Jan. 29-30	Wind, hail	Midwest	0	0	0	6	4	10
Feb. 5-6	Wind, hail, flood	Midwest	(2)	(1)	(3)	6	8	14
Mar. 14	Tornadoes, wind, hail, flood	South	0	0	0	5	1	6
Mar. 15-16	Wind, hail	South	(2)	1	(1)	2	5	7
Apr. 9-11	Wind, hail, flood	South	19	2	21	19	2	21
May 10-12	Wind, hail, flood	South, Mid-Atlantic	4	3	7	4	3	7
May 22-26	Wind, hail	Midwest	7	2	9	7	2	9
May 29- Jun 1	Wind, hail, flood, water, hydrostatic	Midwest	6	6	12	6	6	12
Jun. 2-4	Wind, hail, flood, water, hydrostatic	Midwest	6	7	13	6	7	13
Jun. 5-8	Wind, hail, flood	Midwest	13	11	24	13	11	24
Jun. 11-12	Wind, hail, flood, water, hydrostatic	Midwest	11	12	23	11	12	23
All Other			4	4	8	4	4	8
Development on 2007 and prior catastrophes			0	0	0	(3)	(1)	(4)
Calendar year incurred total			<u>\$ 66</u>	<u>\$ 47</u>	<u>\$ 113</u>	<u>\$ 89</u>	<u>\$ 67</u>	<u>\$ 156</u>
<b>2007</b>								
Mar. 1-2	Wind, hail, flood	South	\$ 0	\$ (1)	\$ (1)	\$ 6	\$ 1	\$ 7
Jun. 7-9	Wind, hail, flood	Midwest	2	3	5	2	3	5
All Other			6	5	11	14	6	20
Development on 2006 and prior catastrophes			(3)	(1)	(4)	(6)	(11)	(17)
Calendar year incurred total			<u>\$ 5</u>	<u>\$ 6</u>	<u>\$ 11</u>	<u>\$ 16</u>	<u>\$ (1)</u>	<u>\$ 15</u>

# Insurance Segment Highlights

## Commercial Lines Insurance Operations

(Dollars in millions)	Three months ended June 30,			Six months ended June 30,		
	2008	2007	Change %	2008	2007	Change %
Written premiums . . . . .	\$ 597	\$ 613	(2.7)	\$ 1,222	\$ 1,306	(6.5)
Earned premiums . . . . .	\$ 586	\$ 607	(3.3)	\$ 1,161	\$ 1,210	(4.1)
Loss and loss expenses excluding catastrophes	342	330	3.7	685	673	1.7
Catastrophe loss and loss expenses . . . . .	66	5	1,220.0	89	16	465.2
Commission expenses . . . . .	105	112	(6.1)	214	235	(9.2)
Underwriting expenses . . . . .	68	68	1.4	136	123	10.7
Policyholder dividends . . . . .	4	2	67.9	7	6	28.9
Underwriting profit . . . . .	\$ 1	\$ 90	(99.3)	\$ 30	\$ 157	(81.1)
Ratios as a percent of earned premiums:						
Loss and loss expenses excluding catastrophes	58.4%	54.5%		59.1%	55.7%	
Catastrophe loss and loss expenses . . . . .	11.3	0.8		7.6	1.3	
Loss and loss expenses . . . . .	69.7%	55.3%		66.7%	57.0%	
Commission expenses . . . . .	17.9	18.5		18.4	19.4	
Underwriting expenses . . . . .	11.6	11.0		11.7	10.2	
Policyholder dividends . . . . .	0.7	0.4		0.6	0.	
Combined ratio . . . . .	99.9%	85.2%		97.4%	87.0%	

- 2.7 percent and 6.5 percent declines in second-quarter and six-month 2008 commercial lines net written premiums, primarily a result of market competition.
- \$87 million in second-quarter 2008 new commercial lines business written directly by agencies, up 21.2 percent from \$71 million in last year's second quarter. Six-month new business rose 6.4 percent to \$152 million from \$143 million.
- 14.7 percentage point rise in second-quarter 2008 combined ratio largely due to higher loss and loss expense ratio. Lower commission expense offset a slight rise in other underwriting expenses.
- 14.4 percentage point rise in second-quarter 2008 loss and loss expense ratio due to higher catastrophe losses and higher losses and case reserve increases greater than \$250,000, as well as the effect of softer pricing and normal loss cost inflation. Those increases were somewhat offset by a higher level of savings from favorable development on prior period reserves.
- \$38 million increase in second-quarter losses and case reserve increases greater than \$250,000. The increase largely reflected the normal fluctuations of loss patterns, normal variability in the large case reserves for our workers' compensation claims, several unusually large losses related to non-catastrophe weather and a higher number of executive risk losses between \$250,000 and \$1 million.
- 12.6 percentage point improvement in combined ratio due to savings from favorable development on prior period reserves for the second quarter of 2008, compared with 7.1 percentage points of savings for the same 2007 period. 7.6 percentage point improvement in the combined ratio due to savings from favorable development for the first half of 2008 compared with 4.8 percentage points in same 2007 period.



## Personal Lines Insurance Operations

(Dollars in millions)

	Three months ended June 30,			Six months ended June 30,		
	2008	2007	Change %	2008	2007	Change %
Written premiums	\$ 191	\$ 197	(3.0)	\$ 341	\$ 350	(2.6)
Earned premiums	\$ 174	\$ 180	(3.3)	\$ 351	\$ 361	(2.7)
Loss and loss expenses excluding catastrophes	102	114	(10.7)	217	225	(3.6)
Catastrophe loss and loss expenses	47	6	646.8	67	(1)	nm
Commission expenses	36	39	(7.3)	71	77	(7.5)
Underwriting expenses	16	21	(22.8)	41	46	(12.2)
Underwriting profit (loss)	\$ (27)	\$ 0	nm	\$ (45)	\$ 14	nm
Ratios as a percent of earned premiums:						
Loss and loss expenses excluding catastrophes	58.4%	63.2%		61.7%	62.3%	
Catastrophe loss and loss expenses	27.0	3.5		19.3	(0.3)	
Loss and loss expenses	85.4%	66.7%		81.0%	62.0%	
Commission expenses	20.6	21.5		20.2	21.2	
Underwriting expenses	9.3	11.7		11.5	12.8	
Combined ratio	115.3%	99.9%		112.7%	96.0%	

- 3.0 percent and 2.6 percent declines in second-quarter and six-month 2008 personal lines net written premiums due to lower policy counts and pricing changes that reduced premiums per policy. Higher new personal lines business and premium increases related to rising insured values partially offset those factors.
- \$10 million in second-quarter 2008 personal lines new business written directly by agencies, up 7.7 percent. Six-month new business rose 3.9 percent to \$19 million from \$18 million.
- 15.4 percentage point rise in second-quarter 2008 combined ratio largely due to higher catastrophe losses. The higher catastrophe losses were partially offset by improvements in the loss and loss expense ratio excluding catastrophe losses and by lower commission and other underwriting expenses.
- 4.8 percentage point improvement in the second-quarter 2008 loss and loss expense ratio excluding catastrophe losses, primarily due to fluctuations in prior period reserve development on a year-over-year basis.
- Savings from favorable development of prior period reserves reduced the loss and loss expense ratio by 7.2 and 3.3 percentage points in the first quarter and first half of 2008. Savings reduced the segment ratio by 0.3 and 4.7 percentage points in the same 2007 periods. Fluctuations in prior period reserve development for the personal lines segment largely are due to quarterly fluctuations in savings for the other personal line of business, which includes personal umbrella coverages.

## Life Insurance Operations

(In millions)

	Three months ended June 30,			Six months ended June 30,		
	2008	2007	Change %	2008	2007	Change %
Written premiums	\$ 47	\$ 45	3.3	\$ 90	\$ 87	3.6
Earned premiums	\$ 33	\$ 35	(4.7)	\$ 63	\$ 66	(4.0)
Investment income, net of expenses	29	28	5.3	58	56	4.0
Other income	1	1	(34.5)	1	2	(41.1)
Total revenues, excluding realized investment gains and losses	63	64	(0.8)	122	124	(1.1)
Contract holders benefits	38	34	11.3	74	62	19.7
Expenses	10	16	(38.0)	21	29	(27.0)
Total benefits and expenses	48	50	(4.2)	95	91	4.7
Net income before income tax and realized investment gains and losses	15	14	11.4	27	33	(17.1)
Income tax	5	5	18.5	9	11	(16.6)
Net income before realized investment gains and losses	\$ 10	\$ 9	8.0	\$ 18	\$ 22	(17.3)



- \$90 million in total six-month 2008 life insurance segment net written premiums. Written premiums include life insurance, annuity and accident and health premiums.
- 3.2 percent increase to \$73 million in six-month 2008 written premiums for life insurance products in total.
- 8.2 percent rise to \$39 million in six-month 2008 term life insurance written premiums, reflecting marketing advantages of competitive, up to date products, providing personal attention and offering policies backed by financial strength and stability.
- 3.3 percent rise in face amount of life policies in force to \$63.945 billion at June 30, 2008, from \$61.875 billion at year-end 2007.
- \$3.8 million decrease in six-month 2008 operating profit, primarily due to less favorable mortality experience.
- 2008 plans include redesign of all life term insurance products. In addition to the worksite term product, updates are planned for the full worksite life portfolio. These improvements support opportunities to cross-sell life insurance products to clients of the independent agencies that sell Cincinnati's property casualty insurance policies.

## Investment and Balance Sheet Highlights

### Investment Operations

(In millions)	Three months ended June 30,			Six months ended June 30,		
	2008	2007	Change %	2008	2007	Change %
Investment income:						
Interest	\$ 79	\$ 76	4.0	\$ 155	\$ 152	2.2
Dividends	50	72	(30.5)	123	144	(14.4)
Other	3	4	(32.9)	7	7	(2.4)
Investment expenses	(2)	(2)	5.7	(3)	(5)	26.1
Total investment income, net of expenses	<u>130</u>	<u>150</u>	(13.4)	<u>282</u>	<u>298</u>	(5.5)
Investment interest credited to contract holders	<u>(16)</u>	<u>(14)</u>	9.8	<u>(31)</u>	<u>(28)</u>	10.2
Realized investment gains and losses summary:						
Realized investment gains and losses	57	290	(80.4)	40	351	(88.5)
Change in fair value of securities with embedded derivatives	(3)	3	(226.3)	(6)	4	(255.8)
Other-than-temporary impairment charges	<u>(65)</u>	<u>0</u>	nm	<u>(278)</u>	<u>0</u>	nm
Total realized investment gains and losses	<u>(11)</u>	<u>293</u>	(103.8)	<u>(244)</u>	<u>355</u>	(168.8)
Investment operations income	<u>\$ 103</u>	<u>\$ 429</u>	(75.9)	<u>\$ 7</u>	<u>\$ 625</u>	(98.8)

- 13.4 percent and 5.5 percent declines in second-quarter and six-month 2008 net investment income, primarily due to dividend reductions of financial institution stocks.
- \$11 million realized investment loss in second-quarter 2008 compared with realized investment gain of \$293 million in second-quarter 2007. \$244 million realized investment loss in 2008 six-month period compared with realized investment gain of \$355 million in the same 2007 period.
- Second-quarter pretax realized investment loss reflected \$65 million in non-cash charges for other-than-temporary impairments, which included the recognition of the significant market value decline of one large pharmaceutical holding.

(Dollars in millions except share data)

	At June 30, 2008	At December 31, 2007
<b>Balance sheet data</b>		
Invested assets	\$ 10,460	\$ 12,261
Total assets	14,811	16,637
Short-term debt	69	69
Long-term debt	791	791
Shareholders' equity	4,707	5,929
Book value per share	28.99	35.70
Debt-to-capital ratio	15.4%	12.7%

	Three months ended June 30,		Six months ended June 30,	
	2008	2007	2008	2007
<b>Performance measures</b>				
Comprehensive income (loss)	\$ (653)	\$ 171	\$ (967)	\$ 184
Return on equity, annualized	5.0%	20.7%	0.8%	16.0%
Return on equity, annualized, based on comprehensive income (loss)	(51.5)	9.8	(36.4)	5.3

- \$10.460 billion in investment assets at June 30, 2008, compared with \$12.261 billion at year-end 2007. The decrease in investment assets was largely due to lower market valuations of equity holdings, primarily in the financial sector, reflecting broad concerns across the marketplace about credit quality, liquidity and the general health of the economy.
- Shareholders' equity declined to \$4.707 billion, or \$28.99 per share, at June 30, 2008, down from \$5.929 billion, or \$35.70, at year end 2007, largely due to lower market values for investment assets.
- \$5.926 billion Aa3/A+-rated bond portfolio at June 30, 2008, containing a diverse mix of taxable and tax-exempt securities.
- \$4.453 billion equity portfolio includes \$1.888 billion in pretax unrealized gains.
- \$3.650 billion in statutory surplus for the property casualty insurance group at June 30, 2008, compared with \$4.307 billion at year-end 2007. The ratio of common stock to statutory surplus for the property casualty insurance group portfolio was 71.6 percent at June 30, 2008, compared with 86.0 percent at year-end 2007.
- 23.0 percent ratio of investment securities held at the holding-company level to total holding-company-only assets at June 30, 2008, comfortably within management's below-40 percent target.
- Repurchases of the company's common stock totaled 821,003 shares at a cost of \$29 million in the second quarter. Approximately 8.5 million shares remain authorized for repurchase.

For additional information or to hear a replay of the August 6 conference call webcast, please visit [www.cinfin.com/investors](http://www.cinfin.com/investors).

## Electronic Delivery

Cincinnati Financial Corporation is pleased to offer the convenience of electronic delivery of shareholder communication, including annual reports, interim letters to shareholders and proxy statements – even proxy voting online. With your consent and at no cost to you, we can notify you by e-mail when these materials become available on the Internet at [www.cinfin.com](http://www.cinfin.com).

### Electronic delivery benefits you and your company:

- **Immediate availability** – Immediate availability of important information – no more waiting for the mail to arrive.
- **Less clutter** – The average consumer is receiving more mail today than ever, making it easy to miss important information.
- **Cost savings** – Electronic delivery saves money for Cincinnati Financial – your company.

### Plus, it's better for the environment.

You can benefit from electronic delivery whether you directly hold registered shares or hold your investments through a participating brokerage/financial institution. You will need to provide an e-mail address, account number(s) and the last four digits of the Social Security number of the account holder. If you provide this information, you can give your consent for electronic delivery immediately. While you may cancel your consent for electronic delivery at any time, we are confident that you will find this option an efficient and effective way to receive important information about your investment.

To enroll, select Electronic Delivery from the Investors page of [www.cinfin.com](http://www.cinfin.com). If you hold multiple accounts directly or through a broker, you will need to enroll each account separately – including joint tenant and custodial accounts – to stop paper mailings.

**Enroll Today**

**Cincinnati Financial Corporation**  
**Condensed Balance Sheets and Statements of Income (unaudited)**

(Dollars in millions)	June 30, 2008	December 31, 2007
<b>Assets</b>		
Investments .....	\$ 10,460	\$ 12,261
Cash and cash equivalents .....	333	226
Premiums receivable .....	1,150	1,107
Reinsurance receivable .....	777	754
Other assets .....	2,091	2,289
Total assets .....	<u>\$ 14,811</u>	<u>\$ 16,637</u>
<b>Liabilities</b>		
Insurance reserves .....	\$ 5,659	\$ 5,445
Unearned premiums .....	1,609	1,564
Deferred income tax .....	380	977
6.125% senior notes due 2034 .....	371	371
6.9% senior debentures due 2028 .....	28	28
6.92% senior debentures due 2028 .....	392	392
Other liabilities .....	1,665	1,931
Total liabilities .....	<u>10,104</u>	<u>10,708</u>
<b>Shareholders' Equity</b>		
Common stock and paid-in capital .....	1,452	1,442
Retained earnings .....	3,298	3,404
Accumulated other comprehensive income .....	1,163	2,151
Treasury stock .....	(1,206)	(1,068)
Total shareholders' equity .....	<u>4,707</u>	<u>5,929</u>
Total liabilities and shareholders' equity .....	<u>\$ 14,811</u>	<u>\$ 16,637</u>

(Dollars in millions except per share data)	Three months ended June 30,		Six months ended June 30,	
	2008	2007	2008	2007
<b>Revenues</b>				
Earned premiums .....	\$ 794	\$ 822	\$ 1,575	\$ 1,637
Investment income, net of expenses .....	130	150	282	298
Realized investment gains and losses .....	(11)	293	(244)	355
Other income .....	4	5	8	11
Total revenues .....	<u>917</u>	<u>1,270</u>	<u>1,621</u>	<u>2,301</u>
<b>Benefits and Expenses</b>				
Insurance losses and policyholder benefits .....	595	490	1,131	974
Commissions .....	148	160	298	330
Other operating expenses .....	110	112	228	218
Total benefits and expenses .....	<u>853</u>	<u>762</u>	<u>1,657</u>	<u>1,522</u>
Income (Loss) Before Income Taxes .....	64	508	(36)	779
Provision for Income Taxes .....	1	157	(57)	234
<b>Net Income</b> .....	<u>\$ 63</u>	<u>\$ 351</u>	<u>\$ 21</u>	<u>\$ 545</u>
<b>Per Common Share:</b>				
Net income—basic .....	\$ 0.38	\$ 2.04	\$ 0.13	\$ 3.16
Net income—diluted .....	\$ 0.38	\$ 2.02	\$ 0.13	\$ 3.13

# Other News Releases

## Cincinnati Financial Corporation Declares Regular Quarterly Cash Dividend

**Cincinnati, May 23, 2008 – Cincinnati Financial Corporation (Nasdaq: CINF)** today announced that the executive committee of its board of directors has declared a 39 cents per share regular quarterly cash dividend payable July 15, 2008, to shareholders of record on June 20, 2008.

The current dividend level reflects the 9.9 percent increase in the quarterly dividend rate declared in February, setting the stage for 2008 to become the 48<sup>th</sup> year of consecutive increases in the indicated annual cash dividend.

Chairman and Chief Executive Officer John J. Schiff, Jr., CPCU commented, “Our board of directors believes we have the operating strength to maintain our outstanding dividend record. We plan to increase shareholder value over the long term by continuing to focus on strong agency relationships, front-line underwriting, quality claims service, solid policy reserves and total return investing.”

## Cincinnati Financial Corporation Director Appointed as Chief of Navy Reserve, United States Navy

- *Dirk J. Debbink resigned effective June 30, 2008, after four years of board service*
- *Board goes forward with 13 directors as of July 1, 2008*

**Cincinnati, July 3, 2008 – Cincinnati Financial Corporation (Nasdaq: CINF)** today announced that Dirk J. Debbink, a director on the company’s board since 2004, has been appointed Vice Admiral and Chief of Navy Reserve, U.S. Navy. Debbink was recalled to active military duty in Washington, D.C., and confirmed by the U.S. Senate effective June 27, 2008. He tendered his resignation from the Cincinnati Financial board of directors, effective June 30, 2008.

Thirteen directors serve on the board following Debbink’s departure and the previously announced addition of Kenneth W. Stecher to the board. Stecher was named on June 16, 2008, as the company’s president and chief executive and appointed to the board effective July 1, 2008. John J. Schiff, Jr., CPCU, continues as chairman of the board. James E. Benoski continues as vice chairman of the board, as he transitions toward retirement.

Stecher commented, “Dirk was a member of our audit committee, now comprised of six other independent directors, and our executive committee, which also is a group of six directors with business and insurance expertise. The talent on our board is deep, and we expect our directors will work together without missing a beat. Our seasoned directors are great assets as we work through a challenging period for our company, our insurance industry and the financial sector.

“While we will miss working with Dirk, we are pleased to see this well-deserved recognition of his dedication, character and leadership. We understand that all Americans benefit from the willingness of our highest-caliber leaders to serve our country. As he steps up to his new responsibilities for the U.S. Navy, we thank him for all he did to step up for Cincinnati Financial and our shareholders over the past four years.”

## Inside Cincinnati

Cincinnati recently announced transitions within our executive team. Several Cincinnati leaders now have new or expanded roles to broaden and round their experience in support of our agencies. We also named a new chief financial officer. Steve Johnston had previously served as chief financial officer with an independent agency-focused property casualty carrier.

Ken Stecher, our new president and CEO, commented, “I’m deeply honored to lead the company and pleased with the tremendous support I know I’ll receive from the entire leadership team. I’ll benefit from Jim’s wise mentorship and Jack’s keen focus on the agents who bring Cincinnati policies and services to clients in their communities.”

**John J. Schiff, Jr.**, and **James E. Benoski** continue to serve as chairman and vice chairman of the board, respectively. Jim is transitioning toward retirement.

**Kenneth W. Stecher**, promoted to president and chief executive officer, is a 40-year associate and a seasoned leader. He was previously our chief financial officer.

**Steven J. Johnston, FCAS, MAAA, CFA**, joined Cincinnati as chief financial officer for the company and subsidiaries. He also is treasurer and secretary for Cincinnati Financial and secretary for its subsidiaries. He brings more than 25 years of insurance, financial, actuarial and technology experience.

Additional executives were promoted or moved to expanded or different responsibilities:

**Thomas A. Joseph, CPCU**, senior vice president, is promoted to president of The Cincinnati Casualty Company, now heading up our personal insurance operations and continuing to lead our reinsurance team.

**Eric N. Mathews, CPCU, AIAF**, senior vice president, was additionally named principal accounting officer.

**Martin J. Mullen, CPCU**, is promoted to senior vice president and chief claims officer with oversight of both Field Claims and Headquarters Claims.

**Larry R. Plum, CPCU, ARe**, senior vice president, now heads up government relations and special projects serving the executive team.

**Ronald L. Robinson**, vice president, is promoted to manager of Field Claims, reporting to the chief claims officer.

**J.F. Scherer** is promoted to executive vice president, continuing to lead insurance sales and marketing, now including oversight of research and development.

**Charles P. Stoneburner II, CPCU**, senior vice president, now runs our commercial insurance operations, transitioning from his leadership of our large field claims force.

**Timothy L. Timmel**, senior vice president, continues to lead operations with oversight of several additional staff and administrative departments.

Since our last Letter to Shareholders, these associates also merited promotions:

Jane Abney – Chief Underwriting Specialist

Michael Allen – Programmer

Kirsten Amspaugh – Senior Communications Analyst and Manager, Administration

Mary Ashley – Senior Systems Analyst

Dick Aten, CPCU, AIC, AIM – Associate Manager

Debbie Athas – Claims Specialist

Michele Baker, AIS – Underwriting Specialist

Lynnette Beach, AU – Underwriting Superintendent

Tony Betliskey – Storage Engineer

Stephanie Borg – Underwriting Specialist

Tiffany Brandabur, AIM, API – Underwriting Manager

Shanda Breen, AIC – Senior Claims Specialist

Doug Brockway, CPCU – Regional Director

Marty Bruce, CPCU, AIM, ARe, ARM – Associate Territory Manager

Bob Carey, Jr., AU – Underwriting Specialist

Liz Carley – Superintendent, Headquarters Claims

Mark Casey – Chief Underwriting Specialist

Steven Catania – Network Systems Lead

Danielle Chaney – Senior Programmer Analyst

Robert Chasteen – PeopleSoft Group Manager

Christopher Coffaro – State Agent

Scott Courtney, CPCU, AIC, ARM – Senior Loss Control Consultant

Kyle Crawford – Senior Diamond Support Analyst

Scott Cupp, API – Senior Underwriter

Adam Davis, AU – State Agent

Dana Dawson, AIM – Underwriting Superintendent

Evan Derr – Senior Underwriter

Mike DeStazio, AIC – Regional Associate Manager, Casualty Claims

David Dietz, AIC – Associate Superintendent

Rebecca Duff – Senior Loss Control Consultant

Rick Dugan, AIC – Regional Manager, Casualty Claims

Sean Ernst – Senior Underwriter

Hank Faglie, Jr., CPCU, AIC, AIM – Supervisor, Casualty Claims

Greg Feistel – Field Claims Superintendent

Joe Fisher, AIS – Chief Underwriting Specialist

Bill Foltz, AIC – Senior Claims Representative

Leslie Fredricks – Senior Diamond Support Analyst

Tim Fritz – Senior Claims Representative

Patricia Garbacik – Claims Specialist

Laura Lee Gayfield, CPCU, ARM – Underwriting Specialist

Joe Gilmer, CPCU, CIC – Regional Director

Sharon Grubbs – Filings Specialist

Mark Guanciale, CIC – Regional Director

Chris Guibord, AIM – Chief Underwriting Specialist

Kevin Hagedorn – Underwriting Superintendent

Mike Hageman – Supervising Forensic Examiner

Jason Hardesty – Accountant

Lesley Harris, AIC – Claims Specialist

Beth Hemmelgarn – Senior Systems Engineer

Ted Hilgeman, CPCU, CPA – Manager, Corporate Accounting

Richard Hill, AIC – Associate Superintendent

Kerri Hinkel, AIM, API – Senior Web Content Analyst

Al Hoeweler, Jr., CPCU – Chief Underwriting Specialist

Mary Alice Hounshell, AIC – Senior Claims Specialist

Robyn Jacobs – Director, Data Entry

Bill Jansen – Field Audit Manager

Timothy Johnson, AIC – Claims Specialist

Dave Keller, AFSB – Bond Field Director

Dennis Kennett – Senior Machinery & Equipment Representative

Steve Kistner, AIC – Senior Claims Representative

Ron Klimkowski, AIC, CIC – Field Supervisor, Sales & Marketing

Brian Krieger – Senior Claims Specialist

Mike Lane, CPCU, AIM, AIT, API – Senior Group Manager

Robert Leist – Systems Engineer

Nancy Liebowitz, CPCU, AU – Underwriting Superintendent

LeAnna Mack – Business Analyst

Melissa Madden – Systems Analyst

Bill Mallard – Senior Business Analyst

Tim McCord, AIC – Senior Claims Representative

Sean McKinley, CLU – Life Field Director

Jennifer McKinney-Taylor, CPCU, AIC, AIM, API – Senior Claims Examiner

Carrie McKittrick, CPCU, AIM, AIT – Underwriting Superintendent

Brad McLaughlin – Underwriting Superintendent

Brett Meadors – Underwriting Specialist

Trisha Meece, API – Senior Underwriter

Chris Mills, AIC – Senior Claims Representative

Michael Mirizzi – Underwriting Specialist

Holly Moorhead – Senior Personal Lines Marketing Representative

Mark Morrow, CPCU, AIM – Regional Field Claims Manager

Angie Mosher, AIC – Underwriting Specialist

Daniel Muraski – Senior Group Manager

Matt Murphy, AIC – Senior Claims Specialist

Charlene Naylor, CPCU, AIM – Senior Support Manager

Tom Nelson – Senior Life Regional Director  
 Mike Noe – Senior Underwriting Specialist  
 Jim Ogle, CPCU, AIC – Manager, Casualty Claims  
 Nancy Olson, CPCU, AIC – Senior Claims Representative  
 Tina Ostenkamp, AIC – Senior Claims Examiner  
 Brian Rawlings, AIS, AU – Senior Underwriter  
 Kathy Reuter – Manager, Central Files  
 Julie Roudabush – Senior Underwriter  
 Lisa Routh, CPCU, AIM – Senior Division Manager  
 Holly Sanders, CPCU – Senior Underwriter  
 Scott Sanderson, CPCU, AIC – Associate Manager  
 Emily Sandlin – Senior Underwriter  
 Elizabeth Schirm – Superintendent, Executive Risk Claims and  
 Associate Manager, Claims Education  
 Joe Schutte IV – Associate Programmer  
 Stacey Shadd – Specialist, IT Quality Assurance & Standards  
 Cathy Shell, SCLA – Senior Claims Representative  
 Raymond Shields, Jr. – Claims Specialist  
 Alok Sinhasan – Lead Senior Systems Engineer  
 Denise Slatter – Senior Diamond Support Analyst  
 Matthew Snyder – Unix Administrator  
 Jeffrey Sousa – Underwriting Specialist  
 Traci Stamper – Senior Systems Support Supervisor  
 Mike Stecher – Senior Underwriter  
 Julie Sullivan, AIC, SCLA – Superintendent, Headquarters Claims  
 Brian Sunderman – Senior Underwriter

Sheila Sundrla, AIC, AIM, SCLA – Senior Claims Representative  
 Mike Swiadras – Senior Machinery & Equipment Specialist  
 Kay Swisshelm – Superintendent, Central Files  
 Mike Szczepanski – Chief Underwriting Specialist  
 Mark Szuch, CPCU – Chief Underwriting Specialist  
 Ron Tebbe, AIM, API – Underwriting Manager  
 Mike Telarico, CPCU, API, AU, CIC – Regional Director  
 Paul Thibault, ARM – Loss Control Field Director  
 Mike Thomas, AIM – Supervisor, Workers'  
 Compensation: Norcross  
 Rajesh Thurairatnam – Senior Actuarial Analyst  
 Denise Toth, CPCU, AIC – Senior Claims Representative  
 Georgie VanWinkle – Project Manager  
 Gayathri Vijayasathy – Programmer Analyst  
 Joe Vinson – Loss Control Field Director  
 Paul Voda, AIC, AIM – Superintendent, Headquarters Claims  
 Duane Wagenknecht, CPCU – Field Audit Superintendent  
 Michael Wagonfield – Senior Programmer Analyst  
 Troy Walters – Senior Machinery & Equipment Representative  
 Sean Whalen, AIC – Senior Claims Specialist  
 Kelli Williams – Underwriting Specialist  
 Kevin Yuenger, CPCU, ChFC, CIC, CLU, LUTCF –  
 Life Field Director  
 Scott Zemberi, CPCU, AIM, ARe, AU – Underwriting  
 Superintendent

## Professional Development

Offering free education to our agents sets Cincinnati apart from our competition. In August, we revamped our Agent Learning Center so that agents can manage their staff development with ease. They can now appoint an agency training coordinator to see, track and assign training for all agency personnel. The coordinator can also create customized learning plans for individuals by searching our general categories or by assigning courses to meet the needs of those who work in more specific areas. Using a blend of online courses, classroom and Web events, agents can benefit from tailored training programs that meet the individual needs of new and established team members.

We encourage and reward associates who continue their professional insurance education, earning credentials by meeting high academic, ethical and length-of-experience standards. Congratulations to associates who completed a series of courses to earn the Chartered Property Casualty Underwriter (CPCU) designation: Scot Feldmeyer, James Kelso and Amy Stitzel.

The ABC Award recognizes exemplary productivity, service and quality in exceptional associates. The ABC Award committee recently granted the quarterly Above and Beyond the Call (ABC) award to Doug Helton, IT Claims/CSU Development Support; Robert Meyer, IT Infrastructure; and Lynn Stahr, IT Project & Request Management. Congratulations to these quarterly winners!

## Financial Services

The company's three financial services subsidiaries continue to successfully leverage our insurance relationships and broaden our offerings. As of June 30, 2008, CFC Investment Company, which offers equipment and vehicle leases and loans, reported 2,328 accounts representing \$80 million in net receivables. CinFin Capital Management Company, which offers asset management services, reported \$883 million under management in 56 accounts as of June 30, 2008. During the first six months of the year, The Cincinnati Specialty Underwriters Insurance Company and our wholly-owned brokerage, CSU Producer Resources Inc., have begun marketing excess and surplus lines

insurance in 10 states and remain on track to market in the planned 33 of our 34 active states before year-end. Cincinnati Specialty Underwriters has added the property line of business in five states and will continue to introduce new lines of business throughout the remainder of the year, including miscellaneous professional and excess casualty. Availability of CSU's new offerings has enhanced your company's ability to write new standard market property casualty business, as we work with agents to round out accounts that require admitted and non-admitted market solutions.

# Safe Harbor

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 2007 Annual Report on Form 10-K, Item 1A, Risk Factors, Page 21. Although we often review and update our forward-looking statements when events warrant, we caution our readers that we undertake no obligation to do so.

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
  - 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:
    - Multi-notch downgrades of the company’s financial strength ratings
    - Concerns that doing business with the company is too difficult or
    - Perceptions that the company’s level of service, particularly claims service, is no longer a distinguishing characteristic in the marketplace
  - Further decline in overall stock market values negatively affecting the company’s equity portfolio and book value; in particular further declines in the market value of financial sector stocks, including Fifth Third Bancorp (NASDAQ:FITB)
  - Securities laws that could limit the manner, timing and volume of our investment transactions
  - Events, such as the credit crisis triggered by subprime mortgage lending practices, that lead to:
    - Significant decline in the value of a particular security or group of securities, such as our financial sector holdings, 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
  - Recession or other economic conditions or regulatory, accounting or tax changes resulting in lower demand for insurance products
  - 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
  - Inaccurate estimates or assumptions used for critical accounting estimates
  - 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
  - Changing consumer buying habits and consolidation of independent insurance agencies that could alter our competitive advantages
  - Increased frequency and/or severity of claims
  - Delays or inadequacies in the development, implementation, performance and benefits of technology projects and enhancements
  - Ability to obtain adequate reinsurance on acceptable terms, amount of reinsurance purchased, financial strength of reinsurers and the potential for non-payment or delay in payment by reinsurers
  - Increased competition that could result in a significant reduction in the company’s premium growth rate
  - Underwriting and pricing methods adopted by competitors that could allow them to identify and flexibly price risks, which could decrease our competitive advantages
  - Personal lines pricing and loss trends that lead management to conclude that this segment could not attain sustainable profitability, which could prevent the capitalization of policy acquisition costs
  - Actions of insurance departments, state attorneys general or other regulatory agencies that:
    - Restrict our ability to exit or reduce writings of unprofitable coverages or lines of business
    - Place the insurance industry under greater regulatory scrutiny or result in new statutes, rules and regulations
    - Increase our expenses
    - 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
    - Limit our ability to set fair, adequate and reasonable rates
    - Place us at a disadvantage in the marketplace or
    - Restrict our ability to execute our business model, including the way we compensate agents
  - Adverse outcomes from litigation or administrative proceedings
  - 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
  - Investment activities or market value fluctuations that trigger restrictions applicable to the parent company under the Investment Company Act of 1940
  - Events, such as an epidemic, natural catastrophe, terrorism or construction delays, 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, 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 recent measures affecting corporate financial reporting and governance. The ultimate changes and eventual effects, if any, of these initiatives are uncertain.

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## Contact Information

Communications directed to the company's secretary, Steven J. Johnston, chief financial officer, are shared with the appropriate individual(s). Or, you may directly access services:

**Investors:** Investor Relations responds to investor inquiries about Cincinnati Financial Corporation and its performance.  
Heather J. Wietzel – Vice President, Investor Relations  
513-870-2768 or [investor\\_inquiries@cinfin.com](mailto:investor_inquiries@cinfin.com)

**Shareholders:** Shareholder Services provides stock transfer services, fulfills requests for shareholder materials and assists registered shareholders who wish to update account information or enroll in shareholder plans.  
Jerry L. Litton – Assistant Vice President, Shareholder Services  
513-870-2639 or [shareholder\\_inquiries@cinfin.com](mailto:shareholder_inquiries@cinfin.com)

**Media:** Corporate Communications assists media representatives seeking information or comment from Cincinnati Financial Corporation or its subsidiaries.  
Joan O. Shevchik, CPCU, CLU – Senior Vice President, Corporate Communications  
513-603-5323 or [media\\_inquiries@cinfin.com](mailto:media_inquiries@cinfin.com)

### Cincinnati Financial Corporation

The Cincinnati Insurance Company  
The Cincinnati Casualty Company  
The Cincinnati Indemnity Company  
The Cincinnati Specialty Underwriters Insurance Company

**Mailing Address:**

P.O. Box 145496  
Cincinnati, Ohio 45250-5496

Phone: 513-870-2000

Fax: 513-870-2066

[www.cinfin.com](http://www.cinfin.com)

The Cincinnati Life Insurance Company  
CSU Producer Resources Inc.  
CFC Investment Company  
CinFin Capital Management Company

**Street Address:**

6200 South Gilmore Road  
Fairfield, Ohio 45014-5141





# Cincinnati Financial Corporation

## 2008 First-quarter Letter to Shareholders

May 27, 2008

### To Our Shareholders, Friends and Associates:

The early months of 2008 brought rocky weather of all kinds to Cincinnati Financial and The Cincinnati Insurance Companies. Our policyholders were caught in severe storms, resulting in \$43 million of catastrophe losses in the first quarter followed by additional events in April and May. This increased storm activity contrasted sharply with the atypically storm-free 2007.

It's no surprise that the timing and severity of storms is unpredictable. But we expect and plan for them. We make sure we have staff trained to respond to policyholders and financial resources to pay claims. Year after year, we maintain solid reinsurance agreements and policy reserves to add to our flexibility.

We're weathering other storms too.

The property casualty insurance underwriting cycle is at the stage called a soft market, with carriers aggressively competing by cutting prices. We expect and plan for soft markets by building up our underwriting strength, as well as agency and policyholder relationships. Our agents work with our underwriters to help us identify and retain the highest quality accounts with clear potential to be profitable over the long term. We continue to identify new ways to serve our agencies, appoint new agencies and take advantage of our automation to write business in new areas.

Nor can we claim to be totally surprised at the stormy financial markets, which currently are reducing our investment income growth rate and book value. The current storm is widespread and powerful, yet our premiums-to-surplus ratio remains a healthy 0.75 to 1, and we remain one of the few insurer groups with A.M. Best Co's highest rating, the A++ (Superior). We believe our total return investment philosophy, which encompasses selecting and holding securities that offer both current income and appreciation potential, will yet prove to be the most enduring shelter from this storm's worst damage.

You'll see the impact of all of these storms in our first-quarter results – and you'll also see that they did not cause us to change our outlook for full-year 2008. At our annual meeting of shareholders we discussed our belief that we can still achieve modest full-year property casualty profitability, total premiums as much as 5 percent lower than the 2007 level and growth in investment income.

Yes, it's been rocky weather to start 2008 with the confluence of higher storm claims, market competition and a difficult investment environment, and the rain continues to fall. We're going to focus on our proven strategies, deliberately conceived to produce a stronger company over the long term and to take us through all kinds of weather and economic cycles. Our goal remains to increase your return on your investment.

We believe better weather will return.

Sincerely,

/S/ John J. Schiff, Jr.

John J. Schiff, Jr., CPCU  
Chairman and Chief Executive Officer

/S/ James E. Benoski

James E. Benoski  
Vice Chairman, President, Chief Operating Officer,  
and Chief Insurance Officer

In 2008, we are offering shareholders the same types of information about our company as in prior years, but on a different schedule. As each item is published, it appears on our Web site, [www.cinfin.com](http://www.cinfin.com), in an integrated annual report format. Many items will be available to you earlier than you received them in the past, because you no longer have to wait until all sections of our annual report are printed. Items available now are titled in color, and those coming soon are titled in gray.

## About the Company

Cincinnati Financial meets the needs of agencies and policyholders through our insurance group and three complementary subsidiaries:

**The Cincinnati Insurance Company** leads our A++ A.M. Best-rated standard market property casualty insurance group, which includes **The Cincinnati Casualty Company** and **The Cincinnati Indemnity Company**. This group markets a broad range of business, homeowner and auto policies through our select group of local independent insurance agencies in 34 states. These companies support each agency's ability to provide exceptional value and service to the people and businesses in its community. Our local field representatives work out of their homes, customizing products to meet policyholder needs, responding personally and promptly to claims and strengthening relationships.

Two other subsidiaries of The Cincinnati Insurance Company also market insurance products. **The Cincinnati Life Insurance Company**, rated A+ by A.M. Best, markets life insurance policies, disability income policies and annuities. **The Cincinnati Specialty Underwriters Insurance Company**, rated A by A.M. Best, began offering excess and surplus lines insurance products in 2008.

Three subsidiaries of Cincinnati Financial support our insurance operations. **CSU Producer Resources Inc.** offers insurance brokerage services to our independent agencies to support their access to Cincinnati Specialty Underwriters. **CFC Investment Company** offers commercial leasing and financing services to our agents and their clients. **CinFin Capital Management Company** provides asset management services to institutions, corporations and nonprofit organizations.

## 2007 Fourth-quarter and Full-year Letter to Shareholders – mid-February 2008

This message from our chairman and our president includes recent news releases about financial results announced February 6 and actions taken by the board of directors at its February 1 meeting. *The Cincinnati Experience*, a profile of our operating philosophy, accompanies this letter.

## The Cincinnati Experience – mid-February 2008

The Cincinnati Insurance Company, Cincinnati Financial Corporation's lead subsidiary, ranks among the top 25 U.S. property casualty insurer groups based on net written premiums. In *The Cincinnati Experience*, you'll read about how our relationship-based approach creates value and loyalty, supporting premium growth.

## 2007 Annual Report on Form 10-K – late-February 2008

The *Annual Report on Form 10-K* is a detailed document published by every publicly traded company as required by the U.S. Securities and Exchange Commission. In our report, we describe your company's operations, its results and trends, along with supporting data, discussions, audited financial statements and accompanying notes.

## 2008 Shareholder Meeting Notice and Proxy Statement – mid-March 2008

This statement informs you of items requiring shareholder action at the 2008 Annual Meeting of Shareholders on May 3, 2008. It identifies board members, detailing director and executive officer compensation and board activities. Notice cards, mailed in March, tell how to easily obtain the *Proxy Statement* and vote.

## Chairman and President's Letter – late-March 2008

Accompanying the Proxy Statement are the 2007 condensed balance sheets and income statements, six years of summary financial data and an annual message from our chairman and our president. Their letter presents management's perspectives on your company's 2007 performance and trends that may affect performance in 2008 and beyond.

## First-quarter 2008 Letter to Shareholders – mid-May 2008

This message from our chairman and our president includes recent news releases about financial results announced April 30, results of shareholder votes at the 2008 Annual Meeting of Shareholders and actions of the board at its May meeting. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by May 12, 2008.

## Second-quarter 2008 Letter to Shareholders – mid-August 2008

This message from our chairman and our president includes our August 6 news release with financial results. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by August 11, 2008.

## Third-quarter 2008 Letter to Shareholders – mid-November 2008

This message from our chairman and our president includes our October 29 news release with financial results. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by November 10, 2008.

# Recent News Releases

## Cincinnati Financial Reports First-quarter 2008 Results

Cincinnati, April 30, 2008 – Cincinnati Financial Corporation (Nasdaq: CINF) today reported:

- First-quarter net loss of \$42 million, or 26 cents per share, compared with net income of \$194 million, or \$1.11 per share, in the first quarter of 2007. The realized investment loss in the first quarter of 2008 included other-than-temporary impairment charges of \$214 million largely due to recognition on the income statement of significant declines in market values of four equity investments. These non-cash charges lower the carrying value of these investments.
- Operating income\* of \$109 million, or 66 cents per share, compared with \$153 million, or 88 cents per share. Catastrophe losses reduced first-quarter operating income by 17 cents compared with 1 cent in last year's first quarter.
- Total property casualty underwriting profit of \$10 million compared with strong \$81 million for the first quarter of 2007.

### Financial Highlights

(Dollars in millions except share data)

	Three months ended March 31,		
	2008	2007	Change %
<b>Revenue Highlights</b>			
Earned premiums	\$ 780	\$ 815	(4.2)
Investment income	152	148	2.6
Total revenues	704	1,031	(31.7)
<b>Income Statement Data</b>			
Net income (loss)	\$ (42)	\$ 194	nm
Net realized investment gains and losses	(151)	41	nm
Operating income*	<u>\$ 109</u>	<u>\$ 153</u>	(29.0)
<b>Per Share Data (diluted)</b>			
Net income (loss)	\$ (0.26)	\$ 1.11	nm
Net realized investment gains and losses	(0.92)	0.23	nm
Operating income*	<u>\$ 0.66</u>	<u>\$ 0.88</u>	(25.0)
Book value	\$ 33.40	\$ 39.08	(14.5)
Cash dividend declared	\$ 0.39	\$ 0.355	9.9
Weighted average shares outstanding	165,105,311	174,274,157	(5.3)

### Insurance Operations Highlights

- 98.6 percent first-quarter 2008 property casualty combined ratio, compared with 89.6 percent for the 2007 first-quarter.
- Catastrophe losses added 5.7 percentage points to the property casualty combined ratio for the 2008 first quarter, compared with an unusually low 0.4 percentage points for the same quarter one year ago.
- Commercial and personal lines marketplace competition continues to intensify. First-quarter 2008 property casualty net written premiums decreased 8.3 percent, reflecting softer pricing, disciplined underwriting and timing differences.
- 5 cents per share contribution from life insurance operations to first-quarter operating income, down from 7 cents.

### Investment and Balance Sheet Highlights

- 2.6 percent growth in pretax investment income.
- Book value of \$33.40 per share compared with \$35.70 at year-end 2007. Invested assets and book value declined primarily on lower market values of financial sector equity holdings.
- 2.93 million shares of common stock repurchased at a cost of \$109 million.

### Full-year 2008 Outlook Unchanged\*\*

- Property casualty net written premiums could decline as much as 5 percent for the full year due to competitive pricing.
- Combined ratio could be in the 96 percent to 98 percent range for the full year.
- Investment income growth is expected to be below last year's 6.6 percent increase as financial sector holdings evaluate dividend levels. Portfolio strategies continue to focus on balancing near-term income generation with long-term book value growth.

\* The Definitions of Non-GAAP Information and Reconciliation to Comparable GAAP Measures on [www.cinfin.com](http://www.cinfin.com) defines and reconciles measures presented in this release that are not based on Generally Accepted Accounting Principles or Statutory Accounting Principles.

\*\* Forward-looking statements and related assumptions are subject to the risks outlined in the company's safe harbor statement (see Page 13).

nm Not meaningful

## **Challenging Markets – Insurance and Investments**

Chairman and Chief Executive Officer John J. Schiff, Jr., CPCU, commented, “This was a tough quarter for Cincinnati Financial as both the insurance and investment markets presented unusual challenges. Soft pricing in the property casualty insurance market pressured our growth and profitability while pressure on financial stocks in our portfolio reduced our net income and book value.

“We firmly believe – and our 55 plus year history supports our confidence – that Cincinnati’s strategies will work as designed, helping us rise above these challenges. After carefully reviewing our position, we are confirming our previously announced outlook, including all of our estimates for full-year performance. We will continue to support agents by providing local service and local decision making authority. We will continue to invest, looking for opportunities that will let us ride out this market cycle with the high level of financial strength and stability that our agents and policyholders rely on.”

## **Long-term Investment in Property Casualty Business**

James E. Benoski, vice chairman, president and chief insurance officer, said, “Our new excess and surplus lines operation is off to a good start. It increases our underwriting capabilities, adding a new layer of flexibility to write the whole account, even when part of it isn’t a good fit for a standard market business policy. We began quoting and issuing excess and surplus business during the first quarter, adding almost \$1 million to net written premiums and putting much more in the pipeline.”

“We initiated our excess and surplus business with the ability to underwrite general liability in five states. We plan to expand both coverage offerings and operating territory. By year-end, we plan to offer commercial property insurance, along with miscellaneous professional liability and excess casualty. Cincinnati agents benefit not only from prompt and efficient policy processing, but also from the ease of accessing services such as loss control and personal attention from knowledgeable underwriters. Our reputation for superb claims handling and other value-added services also is encouraging agencies to select Cincinnati’s excess and surplus lines carrier as their preferred market to serve this segment of their clients. We’re very satisfied with progress to date.”

Benoski added, “This year began with severe weather in the South and Midwest. We incurred \$43 million of catastrophe losses during the quarter, quite a contrast to \$3 million for last year’s first quarter. Of almost 2,500 catastrophe claims our commercial and personal policyholders reported in the five events during the quarter, approximately 85 percent are already closed. Our claims representatives’ prompt responses and personal service are creating tremendous policyholder loyalty that will help agents market Cincinnati policies in the current competitive marketplace.”

## **2008 Property Casualty Outlook Update**

Kenneth W. Stecher, chief financial officer and executive vice president, commented, “We continue to expect our full-year 2008 results will reflect current commercial lines pricing trends, leading to as much as a 5 percent decline in net written premiums and a combined ratio in the range of 96 percent to 98 percent. Softer pricing is likely to continue to challenge us as we hold steady to our core business values of strong agency relationships, policyholder retention and accurate risk classification.

“We also continue to make deliberate decisions not to write or renew certain business. In this environment, we have been careful to maintain our underwriting discipline. Across our industry, the expectation is for full-year 2008 net written premiums to decline 0.5 percent with the combined ratio at 98.6 percent.”

Stecher noted that the combined ratio target relies on three assumptions:

- Current accident year loss and loss expense ratio excluding catastrophe losses – Will reflect the same market trends that contributed to an increase in this ratio in 2007 and are further pressuring the 2008 ratio.
- Catastrophe loss ratio – May contribute approximately 4.5 percentage points to the full-year 2008 combined ratio. Catastrophes are unpredictable for any given year. These losses have contributed on average 3.7 percentage points to the company’s combined ratio in the past 10 years, ranging from 2007’s low of 0.8 points to 1998’s high of 6.1 points.
- Savings from favorable development on prior period reserves – May benefit the full-year 2008 combined ratio by approximately 4 percentage points based on current trends. Even as market conditions soften, management continues to rely on sound actuarial analysis in determining loss and loss expense reserves.

Stecher added, “We believe this level of full-year performance will allow us to sustain our industry leading position in the commercial lines insurance marketplace. We are taking steps in our personal lines insurance operations to enhance our opportunities in the changing marketplace. We also expect our life insurance business to continue its contribution to our earnings.

“As the preferred market for our agents’ best business, we are well positioned to carry out our commitments, supporting market stability and contributing to their success. While we believe we may see a positive contribution from our new excess and surplus lines operations, our 2008 targets do not take into account any contribution. It will take some time before that operation is of sufficient size to materially influence our overall corporate results.”

### Investment Performance Affected by Recent Market Activity

Schiff commented, "Our equity investing strategy has been key to the long-term growth of our assets and shareholders' equity. We identify companies with the potential for sales, earnings and dividend growth, a strong management team and favorable outlook. Over the years, these equities have generally offered a steady flow of dividend income along with the potential for capital appreciation.

"Broad concerns about credit quality, liquidity and the general health of the economy have disrupted the financial markets, causing unusual volatility in our equity portfolio. Valuations of a number of our holdings have been significantly influenced and, in some cases, dividend payouts have been reduced. As a result, our book value declined further in the first quarter. We are making some changes in our portfolio and we took a non-cash charge to earnings to reduce our carrying cost for some holdings, including four equity investments. We adjusted our carrying value to quarter-end market value because we concluded that the decline in the value of these holdings to below our cost was 'other than temporary.' Other-than-temporary impairment losses represent a non-cash charge to income.

"Our bond portfolio, however, continued to hold steady, with a total value of \$5.965 billion at quarter-end, up 2.0 percent from the year-end level. The flight to quality and the resulting lower interest rates for risk-free securities continued to support bond valuations, helping offset the effects of increasing risk premiums

and credit spreads in the first quarter of 2008. Our focus remains on portfolio strategies to balance near-term income generation and long-term book value growth. While decisions to sell investments that no longer meet our investment criteria could have a negative impact on income in the short-term, reinvestment in securities with lower, but more secure, yields should help us weather the present storm.

"We are committed to sustaining the strong capitalization that supports our high insurer financial strength ratings, giving our agents a distinct marketing advantage for their value-oriented clients. On March 26, A.M. Best Co. affirmed our issuer credit and financial strength ratings. Best said its stable outlook on our ratings reflects our group's 'superior risk-adjusted capitalization and its historical ability to generate solid operating results through underwriting cycles, which will enable the group to absorb any near-term increases in volatility as a result of its investment philosophy or weather-related events.'

"Our ratio of property casualty written premiums to statutory surplus, an important measure of that financial strength, rose slightly at March 31, 2008, to 0.75 from 0.72 at year-end 2007, but remains more than 10 percent stronger than the industry average," Schiff noted. "Cincinnati Financial has the resources and tenacity to get through times such as these in good shape.

"We returned \$168 million to shareholders in the first three months of 2008 through cash dividends and repurchase activity," Schiff concluded.

### Combined Property Casualty Insurance Operations

(Dollars in millions)

	Three months ended March 31,		
	2008	2007	Change %
Written premiums	\$ 776	\$ 846	(8.3)
Earned premiums	\$ 751	\$ 785	(4.3)
Loss and loss expenses excluding catastrophes	458	455	0.8
Catastrophe loss and loss expenses	43	3	1,230.8
Commission expenses	144	161	(10.9)
Underwriting expenses	93	82	14.5
Policyholder dividends	3	3	(1.7)
Underwriting profit	\$ 10	\$ 81	(87.1)
Ratios as a percent of earned premiums:			
Loss and loss expenses excluding catastrophes	61.0%	57.9%	
Catastrophe loss and loss expenses	5.7	0.4	
Loss and loss expenses	66.7	58.3	
Commission expenses	19.1	20.5	
Underwriting expenses	12.4	10.4	
Policyholder dividends	0.4	0.4	
Combined ratio	98.6%	89.6%	

- 8.3 percent decline in first-quarter property-casualty net written premiums reflecting softer pricing, disciplined underwriting and timing differences.
- \$74 million in first-quarter 2008 new business written directly by agencies compared with \$80 million in last year's first quarter, down 7.5 percent.
- Excess and surplus lines contributed almost \$1 million in net written premiums in its first quarter of operations.
- Lower level of commission expense, largely due to softer pricing, offset higher other underwriting expenses.
- 1,098 agency relationships with 1,337 reporting locations marketed our insurance products at March 31, 2008, up from 1,092 agency relationships with 1,327 reporting locations at year-end 2007.
- \$13 million of net savings from favorable development on prior period reserves improved the first-quarter 2008 combined ratio by 1.8 percentage points, compared with \$30 million and 4.0 points for the same period in 2007.
- \$43 million in first-quarter 2008 catastrophe losses, due primarily to wind and hail damage from storms in the South and Midwest.

## Catastrophe Loss and Loss Expenses Incurred

(In millions, net of reinsurance)

Dates	Cause of loss	Region	Three months ended March 31,		
			Commercial lines	Personal lines	Total
<b>2008</b>					
Jan. 4-9	Wind, hail, flood, freezing	South, Midwest	\$ 3	\$ 3	\$ 6
Jan. 29-30	Wind, hail	Midwest	5	5	10
Feb. 5-6	Wind, hail, flood	Midwest	8	9	17
Mar. 14	Tornadoes, wind, hail, flood	South	5	1	6
Mar. 15-16	Wind, hail	South	4	4	8
Development on 2007 and prior catastrophes			(3)	(1)	(4)
Calendar year incurred total			<u>\$ 22</u>	<u>\$ 21</u>	<u>\$ 43</u>
<b>2007</b>					
Jan. 12-15	Wind, hail, ice, snow	Midwest	\$ 2	\$ 1	\$ 3
Feb. 14-15	Wind, hail, ice, snow	Mid-Atlantic	1	1	2
Feb. 23-25	Wind, hail, ice, snow	Midwest	3	0	3
Mar. 1-2	Wind, hail, flood	South	6	2	8
Development on 2006 and prior catastrophes			(2)	(11)	(13)
Calendar year incurred total			<u>\$ 10</u>	<u>\$ (7)</u>	<u>\$ 3</u>

## Insurance Segment Highlights

### Commercial Lines Insurance Operations

(Dollars in millions)

	Three months ended March 31,		
	2008	2007	Change %
Written premiums	<u>\$ 625</u>	<u>\$ 693</u>	(9.8)
Earned premiums	\$ 574	\$ 604	(4.9)
Loss and loss expenses excluding catastrophes	343	344	(0.2)
Catastrophe loss and loss expenses	22	10	110.4
Commission expenses	109	123	(12.0)
Underwriting expenses	68	57	21.9
Policyholder dividends	3	3	(1.7)
Underwriting profit	<u>\$ 29</u>	<u>\$ 67</u>	(56.8)
Ratios as a percent of earned premiums:			
Loss and loss expenses excluding catastrophes	59.7%	56.9%	
Catastrophe loss and loss expenses	<u>3.9</u>	<u>1.8</u>	
Loss and loss expenses	63.6	58.7	
Commission expenses	18.9	20.4	
Underwriting expenses	11.9	9.3	
Policyholder dividends	0.6	0.5	
Combined ratio	<u>95.0%</u>	<u>88.9%</u>	

- 9.8 percent lower first-quarter 2008 commercial lines net written premiums, primarily a result of intensifying market competition.
- \$66 million in first-quarter 2008 commercial lines new business written directly by agencies compared with \$72 million in last year's first quarter, down 8.3 percent.
- 95.0 percent first-quarter 2008 commercial lines combined ratio, an increase of 6.1 percentage points over first-quarter 2007 due mostly to higher catastrophe losses, lower pricing, normal loss cost inflation and higher underwriting expenses. Lower commission expenses partially offset these increases.

- 3.9 percentage points of first-quarter 2008 catastrophe losses, more than double last year's unusually low level.
- 2.5 percentage point improvement in combined ratio due to savings from favorable development on prior period reserves for the first three months of both 2008 and 2007.
- Commercial lines insurance industry combined ratio for full-year 2008 estimated at 97.5 percent with decline in net written premiums estimated at 2.3 percent.

## Personal Lines Insurance Operations

(Dollars in millions)

	Three months ended March 31,		
	2008	2007	Change %
Written premiums	\$ 150	\$ 153	(2.0)
Earned premiums	\$ 177	\$ 181	(2.2)
Loss and loss expenses excluding catastrophes	115	111	3.7
Catastrophe loss and loss expenses	21	(7)	376.2
Commission expenses	35	38	(7.7)
Underwriting expenses	24	25	(3.6)
Underwriting profit (loss)	\$ (18)	\$ 14	(223.6)
Ratios as a percent of earned premiums:			
Loss and loss expenses excluding catastrophes	65.1%	61.4%	
Catastrophe loss and loss expenses	11.6	(4.1)	
Loss and loss expenses	76.7	57.3	
Commission expenses	19.8	20.9	
Underwriting expenses	13.6	13.8	
Combined ratio	110.1%	92.0%	

- 2.0 percent lower first-quarter 2008 personal lines net written premiums on lower policy counts, steady new business levels and pricing changes that reduced premiums per policy.
- \$8 million in first-quarter 2008 personal lines new business written directly by agencies, down 0.5 percent.
- 110.1 percent first-quarter 2008 personal lines combined ratio. The ratio reflects significantly higher catastrophe losses and a modest increase in the loss and loss expense ratio excluding catastrophe losses due to lower pricing and normal loss cost inflation.

- 11.6 percentage-point contribution from first quarter 2008 catastrophe losses, compared with a benefit of 4.1 points in the first quarter of 2007 due to savings primarily from fourth-quarter 2006 events.
- \$1 million of reserve strengthening added 0.7 percentage points to the combined ratio in the first three months of 2008, compared with 9.0 percentage points of savings from favorable development on prior period reserves for the same period last year. 2007 savings included 6.1 points in savings on prior period catastrophe loss reserves.
- Personal lines insurance industry combined ratio for full-year 2008 estimated at 99.5 percent with net written premiums rising approximately 1.4 percent.

## Life Insurance Operations

(In millions)	Three months ended March 31,		
	2008	2007	Change %
Written premiums .....	\$ 44	\$ 42	3.8
Earned premiums .....	\$ 29	\$ 30	(3.2)
Investment income, net of expenses .....	29	28	2.7
Other income .....	1	1	(45.7)
Total revenues, excluding realized investment gains and losses .....	59	59	(1.4)
Contract holders benefits .....	35	27	30.4
Expenses .....	12	13	(14.1)
Total benefits and expenses .....	47	40	15.7
Net income before income tax and realized investment gains and losses .....	12	19	(37.2)
Income tax .....	4	6	(39.5)
Net income before realized investment gains and losses .....	\$ 8	\$ 13	(36.0)

- \$44 million in first-quarter 2008 life insurance segment net written premiums. Written premiums include life insurance, annuity and accident and health premiums.
- 3.2 percent increase to \$35 million in written premiums for life insurance products in total.
- 9.0 percent rise to \$18 million in term life insurance written premiums, reflecting marketing advantages of competitive, up to date products, providing close personal attention and offering policies backed by financial strength and stability.
- 1.5 percent rise in face amount of life policies in force to \$62.803 billion at March 31, 2008, from \$61.875 billion at year-end 2007.
- \$5 million decrease in first-quarter 2008 operating profit, primarily due to less favorable mortality experience.
- 2008 plans include redesign of all life term insurance products. In addition to the worksite term product, updates are planned for the full worksite life portfolio. These improvements support opportunities to cross-sell life insurance products to clients of the independent agencies that sell Cincinnati's property casualty insurance policies.

## Investment and Balance Sheet Highlights

### Investment Operations

(In millions)	Three months ended March 31,		
	2008	2007	Change %
Investment income:			
Interest .....	\$ 76	\$ 76	0.5
Dividends .....	73	72	1.6
Other .....	5	3	35.7
Investment expenses .....	(2)	(3)	40.0
Total investment income, net of expenses .....	152	148	2.6
Investment interest credited to contract holders .....	(16)	(14)	6.0
Realized investment gains and losses summary:			
Realized investment gains and losses .....	(16)	61	nm
Change in fair value of securities with embedded derivatives .....	(2)	1	nm
Other-than-temporary impairment charges .....	(214)	0	nm
Total realized investment gains and losses .....	(232)	62	nm
Investment operations income (loss) .....	\$ (96)	\$ 196	nm



- 2.6 percent growth in first-quarter 2008 net investment income due to cash flow for new investments that produced higher interest and dividend income.
- \$232 realized investment loss in first-quarter 2008 compared with realized investment gain of \$62 million in first quarter 2007.
- First-quarter pretax realized investment loss included \$214 million non-cash charge for other-than-temporary impairments that recognize significant market value declines, largely for four equity holdings.

(Dollars in millions except share data)

	At March 31, 2008	At December 31, 2007
<b>Balance sheet data</b>		
Invested assets .....	\$ 11,704	\$ 12,261
Total assets .....	15,945	16,637
Short-term debt .....	69	69
Long-term debt .....	791	791
Shareholders' equity .....	5,449	5,929
Book value per share .....	33.40	35.70
Debt-to-capital ratio .....	13.6%	12.7%
	Three months ended March 31,	
	2008	2007
<b>Performance measures</b>		
Comprehensive income (loss) .....	\$ (313)	\$ 13
Return on equity, annualized .....	(3.0)%	11.5%
Return on equity, annualized, based on comprehensive income (loss) .....	(22.1)	0.8

- \$11.704 billion in investment assets at March 31, 2008, compared with \$12.261 billion at year-end 2007. The decrease in investment assets was largely due to lower market valuations of equity holdings, primarily in the financial sector, reflecting broad concerns across the marketplace about credit quality, liquidity and the general health of the economy.
- Shareholders' equity declined to \$5.449 billion, or \$33.40 per share, at March 31, 2008, down from \$5.929 billion, or \$35.70, at year end 2007, largely due to lower market values for investment assets.
- Lower market values were the primary reason for the comprehensive loss for the first three months of 2008. Net and comprehensive loss resulted in negative returns on equity for the 2008 first quarter.
- \$4.027 billion in statutory surplus for the property casualty insurance group at March 31, 2008, compared with \$4.307 billion at year-end 2007. The ratio of common stock to statutory surplus for the property casualty insurance group portfolio was 82.3 percent at March 31, 2008, compared with 86.0 percent at year-end 2007.
- 27.4 percent ratio of investment securities held at the holding-company level to total holding-company-only assets at March 31, 2008, comfortably within management's below-40 percent target.
- Repurchases of the company's common stock totaled 2.93 million shares at a cost of \$109 million in the first quarter. Approximately 9 million shares remain authorized for repurchase.

For additional information or to hear a replay of the April 30 conference call webcast, please visit [www.cinfin.com/investors](http://www.cinfin.com/investors).

**Cincinnati Financial Corporation**  
**Condensed Balance Sheets and Statements of Operations (unaudited)**

(Dollars in millions)	March 31, 2008	December 31, 2007
<b>Assets</b>		
Investments .....	\$ 11,704	\$ 12,261
Cash and cash equivalents .....	237	226
Premiums receivable .....	1,113	1,107
Reinsurance receivable .....	757	754
Other assets .....	2,134	2,289
Total assets .....	<u>\$ 15,945</u>	<u>\$ 16,637</u>
<b>Liabilities</b>		
Insurance reserves .....	\$ 5,524	\$ 5,445
Unearned premiums .....	1,585	1,564
Deferred income tax .....	750	977
6.125% senior notes due 2034 .....	371	371
6.9% senior debentures due 2028 .....	28	28
6.92% senior debentures due 2028 .....	392	392
Other liabilities .....	1,846	1,931
Total liabilities .....	<u>10,496</u>	<u>10,708</u>
<b>Shareholders' Equity</b>		
Common stock and paid-in capital .....	1,448	1,442
Retained earnings .....	3,298	3,404
Accumulated other comprehensive income .....	1,880	2,151
Treasury stock .....	(1,177)	(1,068)
Total shareholders' equity .....	<u>5,449</u>	<u>5,929</u>
Total liabilities and shareholders' equity .....	<u>\$ 15,945</u>	<u>\$ 16,637</u>

(Dollars in millions except per share data)	Three months ended March 31,	
	2008	2007
<b>Revenues</b>		
Earned premiums .....	\$ 780	\$ 815
Investment income, net of expenses .....	152	148
Realized investment gains and losses .....	(232)	62
Other income .....	4	6
Total revenues .....	<u>704</u>	<u>1,031</u>
<b>Benefits and Expenses</b>		
Insurance losses and policyholder benefits .....	536	484
Commissions .....	150	170
Other operating expenses .....	118	106
Total benefits and expenses .....	<u>804</u>	<u>760</u>
<b>Income Before Income Taxes</b> .....	(100)	271
<b>Provision for Income Taxes</b> .....	(58)	77
<b>Net Income (Loss)</b> .....	<u>\$ (42)</u>	<u>\$ 194</u>
<b>Per Common Share:</b>		
Net income—basic .....	\$ (0.26)	\$ 1.12
Net income—diluted .....	\$ (0.26)	\$ 1.11

# Other News Releases

## Cincinnati Financial Corporation Declares Regular Quarterly Cash Dividend

**Cincinnati, May 23, 2008 – Cincinnati Financial Corporation (Nasdaq: CINF)** today announced that the executive committee of its board of directors has declared a 39 cents per share regular quarterly cash dividend payable July 15, 2008, to shareholders of record on June 20, 2008.

The current dividend level reflects the 9.9 percent increase in the quarterly dividend rate declared in February, setting the stage for 2008 to become the 48th year of consecutive increases in the indicated annual cash dividend.

Chairman and Chief Executive Officer John J. Schiff, Jr., CPCU commented, “Our board of directors believes we have the operating strength to maintain our outstanding dividend record. We plan to increase shareholder value over the long term by continuing to focus on strong agency relationships, front-line underwriting, quality claims service, solid policy reserves and total return investing.”

## Cincinnati Financial Corporation Holds Shareholders’ and Directors’ Meetings

- *Directors elected and board committees reaffirmed*
- *Hollenbeck elevated to corporate officer*

**Cincinnati, May 5, 2008 – Cincinnati Financial Corporation (Nasdaq: CINF)** today announced that at the company’s annual meeting on May 3, 2008, shareholders elected one director for a term of two years and four directors for terms of three years to the 13 member board. Shareholders also ratified the selection of Deloitte & Touche LLP as independent registered public accounting firm and approved amending the company’s Code of Regulation to provide express authority for uncertificated shares.

The board of directors also met and named Martin F. Hollenbeck, CFA, CPCU, as senior vice president and manager – investments, assistant secretary and assistant treasurer for Cincinnati Financial Corporation. Hollenbeck currently is vice president and manager – investments for the company’s insurance subsidiaries, as well as president and chief operating officer of CFC Investment Company and president and member of the board of CinFin Capital Management Company. In addition to the chartered financial analyst and chartered property casualty underwriter professional designations, he holds a master’s degree in business from Xavier University and a bachelor’s degree in economics from Northern Kentucky University.

Chairman and Chief Executive Officer John J. Schiff, Jr., CPCU, commented: “We thank shareholders for approving our selection of Deloitte & Touche and our nominees to the board. The directors who were elected Saturday, as well as our continuing directors, bring their extensive business knowledge and experience to help guide Cincinnati Financial through challenges and opportunities. We also welcome Marty as a corporate officer. Marty has served our company for more than 20 years. We greatly appreciate his leadership of our investment operations, which continue to drive the company’s long-term performance.”

Elected to the board were Kenneth C. Lichtendahl, president, chief executive officer and director of Tradewinds Beverage Company, based in Cincinnati;

W. Rodney McMullen, vice chairman of The Kroger Co., based in Cincinnati; Thomas R. Schiff, chairman, chief executive officer and agent of John J. & Thomas R. Schiff & Co. Inc., a privately owned independent insurance agency, based in Cincinnati; John F. Steele, Jr., chairman and chief executive officer of Hilltop Basic Resources Inc., a family owned aggregates and ready-mixed concrete supplier to the construction industry, based in Cincinnati; and Larry R. Webb, CPCU, president, director, principal owner and agent of Webb Insurance Agency Inc., a privately owned independent insurance agency based in Lima, Ohio.

The board also announced committee service for the coming year, in line with the independence requirements of applicable law and the listing standards of Nasdaq:

- **Audit** – William F. Bahl, Gregory T. Bier, Dirk J. Debbink, Kenneth C. Lichtendahl (chair), Gretchen W. Price, Douglas S. Skidmore and John F. Steele, Jr.
- **Compensation** – Kenneth C. Lichtendahl, W. Rodney McMullen (chair), Gretchen W. Price and E. Anthony Woods.
- **Executive** – William F. Bahl, James E. Benoski, Dirk J. Debbink, W. Rodney McMullen, John J. Schiff, Jr. (chair), Larry R. Webb and E. Anthony Woods.
- **Investment** – William F. Bahl, James E. Benoski, Gregory T. Bier, W. Rodney McMullen, John J. Schiff, Jr. (chair), Thomas R. Schiff and E. Anthony Woods. Richard M. Burrige, CFA, continues to serve as committee adviser.
- **Nominating** – William F. Bahl (chair), Kenneth C. Lichtendahl, Gretchen W. Price and Douglas S. Skidmore.

Schiff noted, “Through their committee assignments and their dedication to understanding our insurance business, our directors work toward a prosperous future for the shareholders of Cincinnati Financial, supporting stability for our agents, policyholders and associates.”

# Inside Cincinnati

At the company's annual meeting on May 3, 2008, Martin F. Hollenbeck, CFA, CPCU, was named a corporate officer at the senior vice president level.

Since our last *Letter to Shareholders*, these associates merited promotions:

Scott Albaugh, AIM, CPCU – Associate Territory Manager  
Greg Anderson – Senior Claims Specialist  
Greg Aumann – Senior Systems Specialist  
Scott Babb, AIC, AIM – Field Claims Manager  
Michelle Baker – Senior Programmer Analyst  
Jessica Ball – Senior Underwriter  
Jennifer Bartos, AU – Underwriting Specialist  
Nick Benjamin – Datacenter Facilities Manager  
Ben Bessler – Senior Underwriter  
Russ Blessing, AIS – Underwriting Specialist  
Mindy Bockewitz, AU – State Agent  
Mark Bowling – Senior Programmer Analyst  
Christine Brant – Claims Specialist  
Chris Byers – Underwriting Superintendent  
Mitch Carson, ALCM, ARM, CSP – Loss Control Field Supervisor  
Mario Castro, AIC – Claims Specialist  
Marcie Caudill – Underwriting Superintendent  
Connie Caudill, AIM – Underwriting Specialist  
Chris Chapin, AIC, AIM – Field Claims Manager  
Scott Chapman – Programmer  
Angela Cheek, AIM, API, CPCU – Underwriting Specialist  
Robert Cheeseman – Senior Network Engineer  
Brian Clapp – Senior Regional Director  
Jon Cooper, AIM, SCLA – Field Claims Manager  
Steve Corbly, AIM, CPCU – Associate Territory Manager  
Lynn Dassel, AIM, AU, CPCU – Senior Underwriting Manager  
Dave Dassel, AIM, AIS – Underwriting Superintendent  
Melissa Davidson – Claims Specialist  
David DeMara, AIC – Field Claims Superintendent  
Dumesha Dubose – Senior Underwriter  
Mel Ducklo, API – Underwriting Specialist  
Jana Emmons, API – Senior Underwriter  
Ryan Evans – Senior Programmer  
Alan Everson – Underwriting Specialist  
Vicki Faller – Regulatory Affairs Analyst  
Scot Feldmeyer, AIM – Underwriting Superintendent  
Tim Fitz, AIC – Superintendent  
Scott Fitzharris, AIM, API, CPCU – Underwriting Specialist  
Steve Fogle – Associate Superintendent  
Douglas Greer, AIS – Underwriting Superintendent  
Forrest Gregg, Jr. – Chief Underwriting Specialist  
Antonio Gregov, AIC – Senior Claims Specialist  
Michelle Gregov, CPCU – Regional Director  
Maureen Grogan, AU – Chief Underwriting Specialist  
Michelle Grove – Underwriting Specialist  
Tom Habig, AIC – Senior Claims Representative  
Melissa Hallbach – Tax Manager  
Chris Harrison, CPCU – Senior Field Analyst  
Tom Heming – Senior Regional Director  
Chris Hill – Underwriting Superintendent  
Christine Horton, API – Senior Diamond Support Analyst  
Lynn Hovekamp, AIC – Superintendent  
Seddrick Hubbard – Underwriting Specialist  
Melissa James – Senior Underwriter  
Craig Jenkins, AIC – Field Claims Superintendent  
Debbie Jenkins, CPCU – Regional Director  
Ming Jiang – Senior Programmer Analyst  
Josh Johnston, AIC – Claims Specialist  
Sean Jones – Senior Underwriter  
Pat Kalimootoo, AIS – Specialist  
Terron Kemp, AIC – Senior Claims Specialist  
Ken Kerby, AIC, AIM, CPCU – Associate Manager Claims Audit  
Mark Kinzer – Senior Regional Director  
Kevin Klatt, AIC – Senior Claims Representative  
Kristy Koerner – Senior Underwriter  
Shirley Krieger, AIC – Supervising Examiner  
Shane Krummen – Specialist  
Paul Kumpar – Senior Investigator  
Kristen Kurtz, CPCU – Senior Underwriter  
Joel LaFrage, ARM – Senior Loss Control Consultant  
Scott Lagedrost – Senior Underwriter  
Jason Laub, AIM – Underwriting Superintendent  
Matt Laws, Jr. – State Agent  
Matt Leugers – Programmer  
Aaron Levenson – Programmer Analyst  
Jack Lindeman – Underwriting Director  
Patrick Loftis – Senior Investment Analyst  
Dan Longacre, AIC – Senior Claims Specialist  
La'Brina Love – Senior Underwriter  
Robin Maddox – Regional Director  
Dan McCaffrey, AFSB – Underwriting Director  
Marcus McClellan, AIC, CPCU – Senior Claims Specialist  
Scott McConkey, CLU, LUTCF – Senior Manager  
Kurt McKenna, AIS – Underwriting Superintendent  
Scott Meyer – Underwriting Specialist  
Matthew Miller – Underwriting Specialist  
Robert Miller – Personnel Superintendent  
Jennifer Mitchell – Senior Requirements Analyst  
Chris Monahan, AIM, CIC, CPCU – Field Director  
Steven Mosure – Senior Claims Specialist  
Dan Mullen – Supervisor Casualty Claims  
Jim Murphy – Underwriting Specialist  
Carl Musselman – Senior Machinery & Equipment Specialist  
Rhonda Napper, AIM – Underwriting Superintendent  
John Nicely – Systems Analyst  
Ryan Osborn – Division Manager  
Mike Otis – Regional Director  
Kay Patch, AIC – Senior Claims Representative  
Jay Patel – Systems Analyst  
Sean Patrick – Senior Underwriter

Darla Pauley, AIC – Senior Claims Specialist  
 Dennis Phelps – Claims Specialist  
 Robert Polinchock – Machinery & Equipment Specialist  
 Betsy Pierce – Senior Programmer Analyst  
 John Redmond, CPCU – Regional Director  
 Jody Reisch – Regional Director  
 Ryan Rhoads – Senior Underwriter  
 Jody Rhude, CIC, CPCU – Field Director  
 Lisa Rhude, CIC, CPCU – Field Director  
 Darren Richter – Underwriting Specialist  
 Aaron Rieth – Senior Underwriter  
 Scott Robinson, AIM, ARe, CPCU – Senior Underwriting Manager  
 Angela Schneider, API – Underwriting Superintendent  
 Jim Shadle – Claims Specialist  
 Paul Shadrick, AIC – Senior Claims Representative  
 Brian Shaffer, AIM – Underwriting Superintendent  
 Bill Sheldon, CIC – Regional Director  
 Meg Shumaker – State Agent  
 Tammy Siler, CPCU – Chief Underwriting Specialist  
 Chris Snyder – Senior Underwriter  
 Alok Soni – Senior Systems Analyst  
 Damian Stark, AIM, API, AU, CPCU – Underwriting Specialist  
 Scott Stevens – Underwriting Specialist  
 Jim Stires – Field Director  
 Jason Stofel – Senior Underwriter

Lisa Sucher, AIC – Claims Specialist  
 Mary Sweeney – Specialist  
 Andy Tebbe, AIM, API – Underwriting Manager  
 Mary Thomas – Underwriting Specialist  
 Jeffrey Thullen – Lead Network Analyst  
 Julie Tucker, AIM, AIS, API – Underwriting Specialist  
 Thomas Ulrich – Senior Underwriter  
 Tracy Valis – Diamond Support Analyst  
 James Van Horn – Senior Claims Specialist  
 Doronna Vickers – Analyst  
 Jeff Viel, AIM, RPLU – Underwriting Director  
 Peggy Volk – Claims Specialist  
 Sherell Walker – Underwriting Specialist  
 Julie Wallace, AIT – Systems Analyst  
 Jennifer West, API, CPCU – Underwriting Specialist  
 Billy Williams – Database Engineer  
 Michael Wood, AIAF, CIA, CPA, CPCU – Internal Auditor Specialist  
 Glen Wooldridge – Senior Claims Specialist  
 Nicholas Wright – Senior Field Underwriter  
 Karen Wright, API – Diamond Senior Analyst  
 Joe Wurzelbacher – Accountant  
 Joe Yannetti, CPCU – Underwriting Superintendent  
 John Zimmer – Chief Underwriting Specialist

## Electronic Delivery

Cincinnati Financial Corporation is pleased to offer the convenience of electronic delivery of shareholder communication, including annual reports, interim letters to shareholders and proxy statements – even proxy voting online. With your consent and at no cost to you, we can notify you by e-mail when these materials become available on the Internet at [www.cinfin.com](http://www.cinfin.com).

### Electronic delivery benefits you and your company:

- **Immediate availability** – Immediate availability of important information – no more waiting for the mail to arrive.
- **Less clutter** – The average consumer is receiving more mail today than ever, making it easy to miss important information.
- **Cost savings** – Electronic delivery saves money for Cincinnati Financial – your company.

### Plus, it's better for the environment.

You can benefit from electronic delivery whether you directly hold registered shares or hold your investments through a participating brokerage/financial institution. You will need to provide an e-mail address, account number(s) and the last four digits of the Social Security number of the account holder. If you provide this information, you can give your consent for electronic delivery immediately. While you may cancel your consent for electronic delivery at any time, we are confident that you will find this option an efficient and effective way to receive important information about your investment.

To enroll, select Electronic Delivery from the Investors page of [www.cinfin.com](http://www.cinfin.com). If you hold multiple accounts directly or through a broker, you will need to enroll each account separately – including joint tenant and custodial accounts – to stop paper mailings.

**Enroll Today**

## Professional Development

We continue to build on the education and training support your company offers to local independent agencies, using this proven strength to help earn our position as the preferred carrier in each agency. We have reorganized and stepped up training activities to introduce newly appointed agencies to our systems and processes. In June, we are implementing a new approach, sending a quick-start team to each new agency. These teams will demonstrate our commitment to making it easy for agency staff to do business with Cincinnati, introducing them to individuals who can help them work effectively with tools from various departments including Commercial Lines, Personal Lines, Agency Accounting and Information Technology.

We encourage and reward associates who continue their professional insurance education, earning credentials by meeting

high academic, ethical and length-of-experience standards. Congratulations to Shannon Daugherty and Greg Knifley who completed a series of courses to earn the Chartered Property Casualty Underwriter (CPCU) designation; to Ted Hilgeman, who earned the Certified Public Accountant (CPA) designation; and to Angela Burns who recently passed the Ohio Bar Exam.

The ABC Award recognizes exemplary productivity, service and quality in exceptional associates. The ABC Award committee recently granted the quarterly Above and Beyond the Call (ABC) award to Carrie McKittrick, AIM, CPCU, Personal Lines, and Carol Ward, Headquarters Claims. Congratulations to these quarterly winners!

## Financial Services

The company's three financial services subsidiaries continue to successfully leverage our insurance relationships and broaden our offerings. As of March 31, 2008, CFC Investment Company, which offers equipment and vehicle leases and loans, reported 2,450 accounts representing \$83 million in net receivables. CinFin Capital Management Company, which offers asset management services, reported \$957 million under management in 64 accounts.

CSU Producer Resources Inc., the new, wholly owned insurance brokerage subsidiary of parent-company Cincinnati Financial Corporation, began accepting excess and surplus lines risks in Ohio, Indiana, Illinois, Wisconsin and Georgia. CSU Producer Resources has binding authority on all classes of business written through The Cincinnati Specialty Underwriters Insurance Company and maintains appropriate agent and surplus

lines licenses to process non-admitted business. Cincinnati Specialty Underwriters and CSU Producer Resources plan to expand into all states except Delaware on an excess and surplus lines basis as the new companies obtain the necessary state regulatory approvals.

We structured our new excess and surplus operations to exclusively serve the needs of the independent agencies that currently market our standard market insurance policies. CSU Producer Resources currently markets and underwrites general liability coverages and plans to expand this to include commercial property, multi-peril insurance, miscellaneous professional liability and excess casualty in coming months. Our excess and surplus lines operation issued nearly \$1 million of new premiums in the first quarter of 2008.

# Safe Harbor

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 2007 Annual Report on Form 10-K, Item 1A, Risk Factors, Page 21. Although we often review and update our forward-looking statements when events warrant, we caution our readers that we undertake no obligation to do so.

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
  - Sustained decline in overall stock market values negatively affecting the company’s equity portfolio and book value; in particular a sustained decline in the market value of Fifth Third shares, a significant equity holding
  - Securities laws that could limit the manner, timing and volume of our investment transactions
  - Recession or other economic conditions or regulatory, accounting or tax changes resulting in lower demand for insurance products
  - Events, such as the subprime mortgage lending crisis, that lead to:
    - Significant decline in the value of a particular security or group of securities, such as our financial sector holdings, 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
  - 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
  - Inaccurate estimates or assumptions used for critical accounting estimates
  - 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
  - Changing consumer buying habits and consolidation of independent insurance agencies that could alter our competitive advantages
  - 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:
    - Downgrade of the company’s financial strength ratings
    - Concerns that doing business with the company is too difficult or
    - Perceptions that the company’s level of service, particularly claims service, is no longer a distinguishing characteristic in the marketplace
  - Delays or inadequacies in the development, implementation, performance and benefits of technology projects and enhancements
  - Ability to obtain adequate reinsurance on acceptable terms, amount of reinsurance purchased, financial strength of reinsurers and the potential for non-payment or delay in payment by reinsurers
  - Increased competition that could result in a significant reduction in the company’s premium growth rate
  - Underwriting and pricing methods adopted by competitors that could allow them to identify and flexibly price risks, which could decrease our competitive advantages
  - Personal lines pricing and loss trends that lead management to conclude that this segment could not attain sustainable profitability, which could prevent the capitalization of policy acquisition costs
  - Actions of insurance departments, state attorneys general or other regulatory agencies that:
    - Restrict our ability to exit or reduce writings of unprofitable coverages or lines of business
    - Place the insurance industry under greater regulatory scrutiny or result in new statutes, rules and regulations
    - Increase our expenses
    - 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
    - Limit our ability to set fair, adequate and reasonable rates
    - Place us at a disadvantage in the marketplace or
    - Restrict our ability to execute our business model, including the way we compensate agents
  - Adverse outcomes from litigation or administrative proceedings
  - 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
  - Investment activities or market value fluctuations that trigger restrictions applicable to the parent company under the Investment Company Act of 1940
  - Events, such as an epidemic, natural catastrophe, terrorism or construction delays, 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, 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 recent measures affecting corporate financial reporting and governance. The ultimate changes and eventual effects, if any, of these initiatives are uncertain.

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## Contact Information

Communications directed to the company's secretary, Kenneth W. Stecher, chief financial officer and executive vice president, are shared with the appropriate individual(s). Or, you may directly access services:

**Investors:** Investor Relations responds to investor inquiries about Cincinnati Financial Corporation and its performance.  
Heather J. Wietzel – Vice President, Investor Relations  
513-870-2768 or [investor\\_inquiries@cinfin.com](mailto:investor_inquiries@cinfin.com)

**Shareholders:** Shareholder Services provides stock transfer services, fulfills requests for shareholder materials and assists registered shareholders who wish to update account information or enroll in shareholder plans.  
Jerry L. Litton – Assistant Vice President, Shareholder Services  
513-870-2639 or [shareholder\\_inquiries@cinfin.com](mailto:shareholder_inquiries@cinfin.com)

**Media:** Corporate Communications assists media representatives seeking information or comment from Cincinnati Financial Corporation or its subsidiaries.  
Joan O. Shevchik, CPCU, CLU – Senior Vice President, Corporate Communications  
513-603-5323 or [media\\_inquiries@cinfin.com](mailto:media_inquiries@cinfin.com)

### Cincinnati Financial Corporation

The Cincinnati Insurance Company  
The Cincinnati Casualty Company  
The Cincinnati Indemnity Company  
The Cincinnati Specialty Underwriters Insurance Company

The Cincinnati Life Insurance Company  
CSU Producer Resources Inc.  
CFC Investment Company  
CinFin Capital Management Company

#### Mailing Address:

P.O. Box 145496  
Cincinnati, Ohio 45250-5496

Phone: 513-870-2000

Fax: 513-870-2066

[www.cinfin.com](http://www.cinfin.com)

#### Street Address:

6200 South Gilmore Road  
Fairfield, Ohio 45014-5141





Cincinnati Financial Corporation

# Chairman and President's Letter

March 2008

In 2008, we are offering shareholders the same types of information about our company as in prior years, but on a different schedule. As each item is published, it appears on our Web site, [www.cinfin.com](http://www.cinfin.com), in an integrated annual report format. Many items will be available to you earlier than you received them in the past, because you no longer have to wait until all sections of our annual report are printed. Items available now are titled in color, and those coming soon are titled in gray.

## About the Company

Cincinnati Financial meets the needs of agencies and policyholders through our insurance group and three complementary subsidiaries:

**The Cincinnati Insurance Company** leads our A++ A.M. Best-rated standard market property casualty insurance group, which includes **The Cincinnati Casualty Company** and **The Cincinnati Indemnity Company**. This group markets a broad range of business, homeowner and auto policies through our select group of local independent insurance agencies in 34 states. These companies support each agency's ability to provide exceptional value and service to the people and businesses in its community. Our local field representatives work out of their homes, customizing products to meet policyholder needs, responding personally and promptly to claims and strengthening relationships.

Two other subsidiaries of The Cincinnati Insurance Company also market insurance products. **The Cincinnati Life Insurance Company**, rated A+ by A.M. Best, markets life insurance policies, disability income policies and annuities. **The Cincinnati Specialty Underwriters Insurance Company**, rated A by A.M. Best, began offering excess and surplus lines insurance products in 2008.

Three subsidiaries of Cincinnati Financial support our insurance operations. **CSU Producer Resources Inc.** offers insurance brokerage services to our independent agencies to support their access to Cincinnati Specialty Underwriters. **CFC Investment Company** offers commercial leasing and financing services to our agents and their clients. **CinFin Capital Management Company** provides asset management services to institutions, corporations and nonprofit organizations.

## 2007 Fourth-quarter and Full-year Letter to Shareholders – mid-February 2008

This message from our chairman and our president includes recent news releases about financial results announced February 6 and actions taken by the board of directors at its February 1 meeting. *The Cincinnati Experience*, a profile of our operating philosophy, accompanies this letter.

## The Cincinnati Experience – mid-February 2008

The Cincinnati Insurance Company, Cincinnati Financial Corporation's lead subsidiary, ranks among the top 25 U.S. property casualty insurer groups based on net written premiums. In *The Cincinnati Experience*, you'll read about how our relationship-based approach creates value and loyalty, supporting premium growth.

## 2007 Annual Report on Form 10-K – late-February 2008

The *Annual Report on Form 10-K* is a detailed document published by every publicly traded company as required by the U.S. Securities and Exchange Commission. In our report, we describe your company's operations, its results and trends, along with supporting data, discussions, audited financial statements and accompanying notes.

## 2008 Shareholder Meeting Notice and Proxy Statement – mid-March 2008

This statement informs you of items requiring shareholder action at the 2008 Annual Meeting of Shareholders on May 3, 2008. It identifies board members, detailing director and executive officer compensation and board activities. Notice cards, mailed in March, tell how to easily obtain the *Proxy Statement* and vote.

## Chairman and President's Letter – late-March 2008

Accompanying the Proxy Statement are the 2007 condensed balance sheets and income statements, six years of summary financial data and an annual message from our chairman and our president. Their letter presents management's perspectives on your company's 2007 performance and trends that may affect performance in 2008 and beyond.

## First-quarter 2008 Letter to Shareholders – mid-May 2008

This message from our chairman and our president includes recent news releases about financial results announced April 30, results of shareholder votes at the 2008 Annual Meeting of Shareholders and actions of the board at its May meeting. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by May 12, 2008.

## Second-quarter 2008 Letter to Shareholders – mid-August 2008

This message from our chairman and our president includes our August 6 news release with financial results. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by August 11, 2008.

## Third-quarter 2008 Letter to Shareholders – mid-November 2008

This message from our chairman and our president includes our October 29 news release with financial results. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by November 10, 2008.

# To Our Shareholders, Friends and Associates:

Your company achieved record operating income in 2007, even as the commercial property casualty insurance market experienced its fourth consecutive year of pricing declines.

For the first time in our history, property casualty written premiums for the full year declined. We expected heightened competition and lower premium revenues to erode insurance underwriting profitability; instead, we saw offsetting benefits that led to a record \$306 million in underwriting income.

- We finished 2007 practically unscathed from catastrophe losses our policyholders would more typically experience over the course of a year.
- Years of careful, ongoing underwriting efforts also helped as losses from previous years trended lower than we had anticipated.

Early in 2008, we already see weather that is not as gentle; an economy and financial markets that are less certain; and daily reminders that intense price competition remains. Once again, we are bracing ourselves for lower premium pricing and the higher loss and expense ratios such pricing causes. If current trends continue, our 2008 premiums could fall as much as 5 percent and our combined ratio could rise to the 96 to 98 percent range, compared with the 1.9 percent premium decline and healthy 90 percent ratio in 2007. We know we have to work harder and win more accounts just to slow the decline or stay even. To move ahead we have to seize new opportunities.

In any environment, our agent-centered, relationship-based approach to doing business brings opportunities to grow and prosper. We believe that our local independent agents have the confidence of policyholders in their communities. Both our agents and our policyholders choose Cincinnati policies because they are seeking quality insurance experiences that reward that confidence.

To honor our relationships, create loyalty and increase growth over the long term, we must have the courage and persistence to respond to challenges in a distinctly Cincinnati way. We intend to optimize your company's advantages by preserving and extending a unique Cincinnati experience to our agents and policyholders.

## Commercial Lines: The Cincinnati Experience – Selling Value and Service

With the continuing soft market for commercial insurance, carriers that want to grow are competing very aggressively and sometimes taking underwriting shortcuts. In this environment, we will price flexibly to protect our proven, high-quality renewal accounts. When we quote new business for our agents, we similarly insist that pricing must correlate with the quality of the risk.



John J. Schiff, Jr., CPCU, chairman and chief executive officer, and James E. Benoski, vice chairman, president and chief operating officer

Because our quote often isn't the lowest, this selectivity compels us to offer special value and service advantages that our agents can sell.

### **Top Claims Service**

That value begins with good claims service. *Business Insurance* reported in December on a recent survey of 13,000 commercial insurance buyers whose firms had revenues ranging from \$10 million to \$500 million. A larger percentage of respondents considered their satisfaction "excellent" for Cincinnati than for any other carrier. The survey evaluated willingness to pay claims, claims coordination with the agent and claims responsiveness. In 2008, we are increasing claims service satisfaction by giving our agents online access to claims information.

### **Updated Products and Markets**

We're updating coverage products in 2008 to make our policies more attractive, including a new optional endorsement that protects against liability arising from a business's use of Web-based technology. Our contractor policyholders will benefit from our new, streamlined process to issue surety bonds for single projects up to \$250,000 or total projects up to \$400,000.

Our local agents are well positioned in their communities to write contractor accounts, which represent a significant portion of our general liability book of business. We will continue in 2008 to serve our agents' construction accounts, while seeking to complement this business by writing more property-dominant accounts.

### **Availability of Excess and Surplus Policies**

At the beginning of 2008, we launched two new subsidiaries for the purpose of becoming a market for our agents' excess and surplus lines accounts. Now we are offering more flexible, limited coverage for commercial accounts with special risk characteristics that cannot obtain coverage using state-regulated policy forms and rates.

The Cincinnati Specialty Underwriters Insurance Company qualified for an A.M. Best Co. rating of A (Excellent) and began writing general liability E&S policies in five states in January. Over 2008, we plan to add property, miscellaneous professional and excess casualty. Through CSU Producer Resources, our new insurance brokerage that exclusively serves appointed agents of The Cincinnati Insurance Company, we plan to offer E&S policies by year-end 2008 in all 34 states where we market commercial lines.

Opportunities to write E&S policies may help us offset the continued decline in our commercial premiums. Agents welcome our entry because we are bringing the Cincinnati experience – our relationship-based approach – to this market. Our E&S underwriters responsible for policy pricing and issuance seamlessly perform the additional functions of E&S brokers. Our E&S philosophy is integrated with our standard lines philosophy: We value and trust the agent's local knowledge. Agents perform frontline underwriting, with access to our commercial lines field marketing



representatives. Agents and their clients get full support including underwriting, claims and loss control services, effective processing technology and compensation comparable to our standard market commissions.

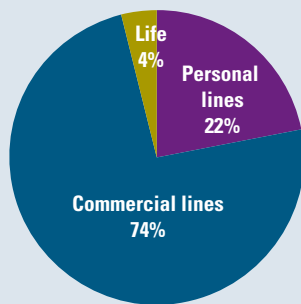
### Improved Agent-facing Technology

Technology improvements are helping our agents meet client preferences and respond efficiently to policyholder inquiries. Agencies in the 19 states where we use our e-CLAS® system to process businessowners policies recently began using our new direct bill payment option, CinciBill™. By year-end, we expect to offer e-CLAS with CinciBill in 31 of our 34 active states and to make substantial progress toward a direct bill solution for policies not processed through e-CLAS. Additionally, we plan to introduce online policy viewing, already available to our associates for more than 75 percent of commercial policies, to our agents in 2008.

### Multi-year Policy Periods

While all of these new initiatives will help us compete on value and service, one of the most effective sales advantages we give agents has been around for a long time. Ninety percent of our commercial packages have multi-year terms, providing stability to agents and policyholders.

Premium Mix  
Percent of 2007 consolidated  
net earned premiums  
(Percent)

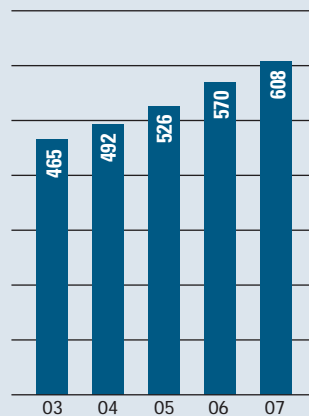


Our revenues include investment income and realized gains (or losses) generated by the portfolio as well as earned premiums from our commercial, personal and life insurance segments. Consolidated earned premiums of \$3.250 billion in 2007 reflected the steadily increasing level of competition in the property casualty insurance marketplace.

Over the past five years, higher pretax income from investments reflected portfolio expansion and dividend increases by companies in the common stock portfolio.

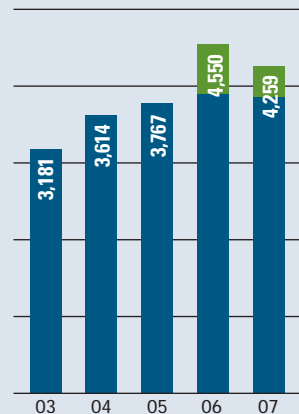
Total realized investment gains and losses contributed 9.0 percent of revenues in 2007 and 15.1 percent in 2006,

Consolidated Pretax  
Investment Income  
Less expenses  
(Dollars in millions)



compared with less than 3 percent in 2003 through 2005. Our most significant source of realized investments gains (or losses) normally is sales of equity securities. We generally reach the decision to divest an equity position after careful analysis of the direction that company is heading and of its ability to meet our investment parameters.

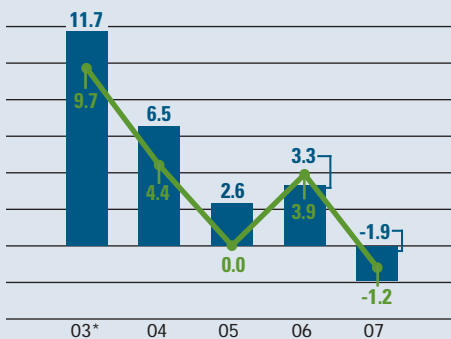
Revenues  
(Dollars in millions)



■ In 2007, realized investment gains of \$382 million reflected four significant transactions greater than \$50 million – the sale of shares of Exxon Mobil Corporation, the block sale of shares of Fifth Third Bancorp, the sale of our holding in FirstMerit Corporation and the disposition of the majority of our holdings in real estate investment trusts. In 2006, realized investment gains of \$684 million largely were from the sale of our holding in Alltel Corporation.

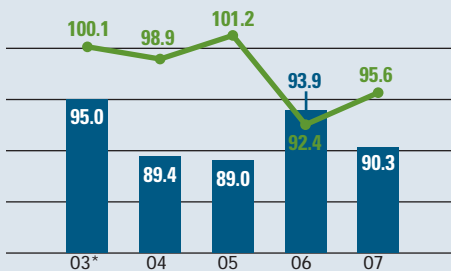
Property Casualty Net Written  
Premium Growth  
Statutory  
(Percent)

■ The Cincinnati Insurance Companies  
◆ Estimated industry (A.M. Best)



Property Casualty Combined Ratio  
Statutory  
(Percent)

■ The Cincinnati Insurance Companies  
◆ Estimated industry (A.M. Best)



We believe we can achieve above-industry-average growth in written premiums and industry-leading profitability over the long term by building on our proven strategies: strong agency relationships, local underwriting, quality claims service, solid reserves and total return investing.

In 2007, we wrote less new property casualty business than the prior year, and market pricing trends led to slightly lower written premiums. We continued to build our company for the long term. Agencies continued to successfully market our products to their better accounts. They helped us write \$325 million of new property casualty business and helped maintain the persistency of our renewals at more than 90 percent.

The improvement in the combined ratio reflected lower catastrophe losses and higher savings from favorable development on prior period reserves. The combined ratio is the percentage of each premium dollar spent on claims and expenses – the lower the ratio, the better the performance.

We commit to maintaining over the entire period our same policy provisions and rates on selected coverages, including property, general liability, inland marine and crime. Other coverages in the package are written and priced annually. In return for this security, the policyholder has no downside, remaining free to continue the policy or not. In fact, few opt out. The company and our agents benefit from lower annual administrative expenses, as well as persistency that rises to a very high 96 percent at the interim annual anniversaries of multi-year policies.

### Personal Lines: The Cincinnati Experience – Building Scale

In personal lines, we work to support the strengths of our local independent agents, who benefit from opportunities to prove their value to people who are centers of influence in their communities. Individuals relying on our home and auto policies receive the same claims service with a human touch that our commercial policyholders enjoy, including prompt, personal responses rather than service-center responses.

To effectively support our agents in personal lines, going forward, we need to reduce our expenses, manage geographical risk concentrations and price more accurately. Our agents generated a 16.9 percent increase in new personal lines business in 2007, and we believe the changes we are making have us heading in the right direction. To make further progress and leverage our product and service advantages into the future, we believe we must add to our scale in 2008.

2008 plans include new agency appointments and geographical expansion for personal lines. Currently, all six of our personal lines of business are available in only 22 states, compared with 34 for commercial lines. Opening for business in some of those untapped states would help spread and reduce our catastrophe risk. With scale, we can continue our investment in updated automation, spreading the expense across a larger premium volume to improve our profitability. Finally, we can implement more pricing points based on risk data, fine-tuning our rates for each risk to produce very competitive premiums for our agents' higher quality accounts. Only by receiving these benefits of scale can we assure our agents' access to a competitive, stable personal lines market.

\* The Definitions of Non-GAAP Information and Reconciliation to Comparable GAAP Measures on [www.cinfin.com](http://www.cinfin.com) defines and reconciles measures presented in this report that are not based on Generally Accepted Accounting Principles or Statutory Accounting Principles.

## **Ample Room to Grow**

We see many opportunities to jump start personal lines expansion in 2008. Agents in 17 states accounting for 97.5 percent of our premium volume were using our Web-based personal lines policy processing system at year-end. Now we are picking up the pace to roll out to eight more states in 2008. In two of those states – Maryland and North Carolina – our automation makes it practical to market some lines of business for the first time. In three others – Arizona, South Carolina and Utah – our agencies have been waiting for Cincinnati personal lines while writing only commercial business. They represent other personal lines carriers, but many are interested in gaining the advantages of Cincinnati claims service and products for their personal lines clients. This expansion enlarges our footprint outside of the Midwest and Southeast, increasing geographic diversification.

## **Data Plus Knowledge = Selection**

We continue to position for growth by steadily improving our policy credits and rates. When our policyholder insures both a home and auto, in many states we now can apply a premium credit to the homeowner policy, as well as continue to credit the auto policy. Another 2008 initiative will increase our inclusion in popular online tools agents and policyholders use to compare carriers. We plan this year to further segment our rates, adding multiple pricing points based on risk-specific data, while also retaining the Cincinnati territory rating approach that recognizes local and regional differences. Though our pricing will reflect quantifiable characteristics, risk selection and underwriting will continue to rely on the agent's knowledge and evaluation of each risk.

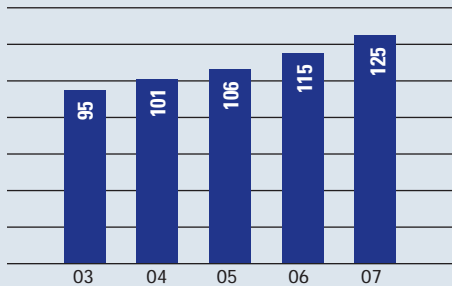
## **Proven Policies**

Our efforts to grow also hinge on product superiority. Our philosophy has been to include coverages or terms and conditions that give the policyholder some advantage beyond the typical policy. While many carriers have reduced or eliminated earthquake coverage, we continue in most geographical areas to build it into our executive homeowner policies, recognizing that over the past century earthquakes have caused insured property damage in every state. Our Executive Classic™ has many such points of difference, from coverage for earthquakes and landslides to hydrostatic water pressure, as well as ordinance or law coverage up to the dwelling limit. In 2008, an optional endorsement to our homeowner policies will add mechanical breakdown coverage for major home systems such as heating and air conditioning, which are not covered in typical homeowner policies.

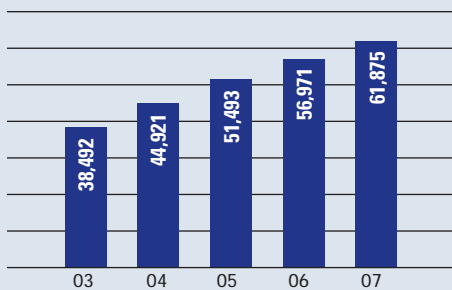
## **Life Insurance: The Cincinnati Experience – Distribution and Product Simplicity**

The Cincinnati Life Insurance Company operates within an industry characterized by complex distribution systems and ultra sophisticated, changing products. As a life insurer within a property casualty focused organization, we determined that the best way to bring value to our agents, our

Cincinnati Life — Net Earned Premiums  
(Dollars in millions)



Cincinnati Life — Gross Life Policy Face Amounts In Force  
Excluding annuities, accident and health business  
(Dollars in millions)



Net earned premium growth for The Cincinnati Life Insurance Company arose from increased premiums for term life insurance, our largest life insurance product line. We also market whole and universal life products, fixed annuities and disability income products. We offer many of these products through payroll deduction programs available to employees at their worksites.

These life insurance products provide our property casualty agency force with cross-selling opportunities for both commercial and personal accounts. We continue to introduce new term products with features our agents and their clients indicate are important. Gross in-force policy face amounts increased to \$61.875 billion at year-end 2007.

policyholders and our company was to commit to the independent agency system and to maintain a simple, up-to-date product portfolio. Following this strategy, we have raised policy face amounts in force at a rate of 16.8 percent annually, to \$62 billion in 2007 from \$18 billion at the beginning of 1999.

### Term and Worksite, a Natural Fit

We are preparing to introduce features in 2008 that will make us more competitive by increasing our rating flexibility. Banded rates will apply different factors to policies with higher face amounts. A new Super Select Plus rate classification will allow us to further refine rates based on the health of the applicant.

All of our term insurance products and all products available to employees through our worksite marketing program will be updated to assure they are competitive. The simplicity of our term insurance products, along with our distinctive return-of-premium option, appeals to our agents. The worksite program is a natural fit that can help Cincinnati's policyholders with small commercial businesses offer voluntary benefits to staff through payroll deduction. Plans for this year include extra support for agents who cross-sell life policies to the company's personal lines policyholders.

### Investment: The Cincinnati Experience – Selecting and Managing for Quality

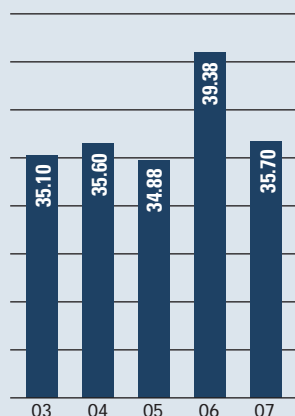
Uncertainty and instability have prevailed in the financial markets over recent months. One source of uncertainty has been the property casualty industry's potential exposure to the credit markets, including sub-prime mortgages. Our investment portfolio contains no mortgage loans.

Our bond portfolio, which has no mortgage-backed securities, continues to hold steady. The flight to quality and the resulting lower rates for risk-free securities supported bond valuations, helping to offset the effects of increasing risk premiums and credit spreads in the last quarter of 2007. We believe that the market may have judged our company's portfolio too harshly on this score in the short term and that we are well positioned for the long term.

We have a substantial municipal bond portfolio, selected for yield and quality, consisting of securities backed by general obligations and essential services revenues. Municipal bonds representing about 87 percent of that portfolio's value are insured. Although many of the bond insurers are suffering some well publicized problems, our average underlying ratings are strong for our insured bonds, minimizing our potential downside risk.

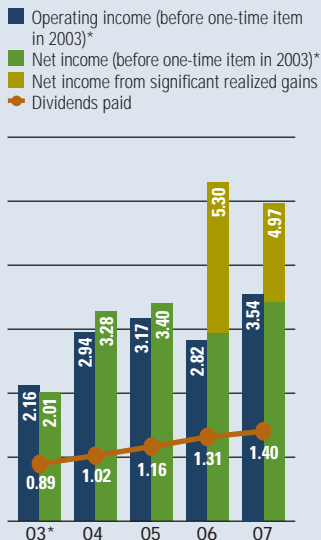


**Book Value**  
Per common share  
(Dollars)



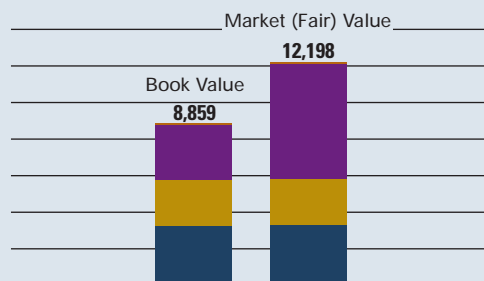
Over the long-term, we believe growth in book value is the most significant measure of our long-term trends. Book value captures both our insurance and investment performance in a single measure that also reflects the benefits of our share repurchase program. Book value has been level over the past five years as lower market values of financial sector equity holdings brought year-end 2007 book value near the 2003 level. Book value continued to benefit from \$2.219 billion in unrealized investment gains on equity holdings at year-end 2007.

**Net Income/Dividends Paid**  
Per common share  
(Dollars)



Insurance performance is one component of net income and operating income, or net income before any realized investment gains and losses. In 2007, operating income grew to a record level, largely due to the low level of catastrophe losses and high level of savings from favorable development on prior period reserves. Operating income also includes investment income, net of expenses, which grew 6.6 percent in 2007.

**Consolidated Investment Portfolio**  
As of December 31, 2007  
(Dollars in millions)



(In millions)	Book Value	Market (Fair) Value
Taxable fixed maturity	\$ 3,265	\$ 3,284
Tax-exempt fixed maturity	2,518	2,564
Common equity	2,715	6,020
Preferred equity	260	229
Short-term	101	101
<b>Total</b>	<b>\$ 8,859</b>	<b>\$ 12,198</b>

Turning to our equity portfolio, banks and other financial sector stocks make up about 55 percent of our equity portfolio and about 35 percent of your company's total investment portfolio. This concentration offers us the advantages of good dividend income but exposes us to market volatility when sector issues arise. Needless to say, the sector is under pressure. To varying degrees, the financial services firms in our portfolio are addressing a challenging credit quality environment and related issues. Some of our holdings are evaluating their dividend levels in light of their own capital requirements and earnings outlook, potentially slowing our investment income growth.

We emphasize portfolio strategies to maximize both income and capital appreciation over the long-term and we are monitoring our holdings in the financial sector closely. We remain committed to sustaining strong capitalization.

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## Consistent and Transparent

We adhere to our investment philosophy, working to assure the credit quality of our bonds and to selectively invest in blue chip, dividend-paying stocks per our stated criteria: we look for common stocks with increasing sales and earnings, proven management, favorable outlooks, annual dividend yields that meet or exceed that of the overall market and have the potential for future dividend increases as well as price appreciation.

Our cash flow from healthy insurance operations has always been adequate to fund our insurance liabilities. This success on the insurance side of our operations supports the investment side, giving us the flexibility to follow our total return, buy-and-hold approach. You can see exactly what securities your company owns at any time by reviewing our quarter-ending portfolios on the Investor's page of [www.cinfin.com](http://www.cinfin.com).

## Year After Year

Your company's board of directors is committed to producing steady value for shareholders. We returned \$546 million to shareholders during 2007, including \$306 million through repurchases of our common stock and \$240 million of cash dividends paid.

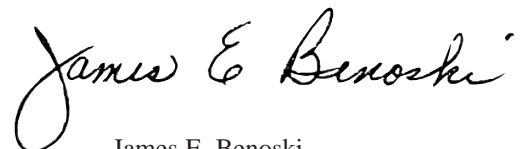
Record repurchase activity in 2007 included an accelerated stock repurchase under which we bought 4 million shares. In authorizing the ASR, the board also increased its repurchase authorization to an additional 13 million shares. In February 2008, the board of directors authorized a 9.9 percent increase in the regular quarterly cash dividend to an indicated annual rate of \$1.56 per share. This action set the stage for a 48<sup>th</sup> consecutive year of increase in that measure.

That track record shows that we are working for a positive *year-after-year* experience for you, our shareholders, as well as our agents, policyholders and associates. In this era when *year-over-year* success is the goal usually measured, we promise to look further down the road, choosing actions that help Cincinnati stand out from the competition and rewarding your confidence.

Respectfully,



John J. Schiff, Jr., CPCU  
Chairman  
Chief Executive Officer



James E. Benoski  
Vice Chairman  
President  
Chief Operating Officer  
Chief Insurance Officer

March 26, 2008

# Condensed Balance Sheets and Income Statements

Cincinnati Financial Corporation and Subsidiaries

(Dollars in millions)

	At December 31,	
	2007	2006
<b>Assets</b>		
Investments .....	\$ 12,261	\$ 13,759
Cash and cash equivalents .....	226	202
Premiums receivable .....	1,107	1,128
Reinsurance receivable .....	754	683
Other assets .....	2,289	1,450
Total assets .....	<u>\$ 16,637</u>	<u>\$ 17,222</u>
<b>Liabilities</b>		
Insurance reserves .....	\$ 5,445	\$ 5,305
Unearned premiums .....	1,564	1,579
Deferred income tax .....	977	1,653
6.125% senior notes due 2034 .....	371	371
6.9% senior debentures due 2028 .....	28	28
6.92% senior debentures due 2028 .....	392	392
Other liabilities .....	1,931	1,086
Total liabilities .....	<u>10,708</u>	<u>10,414</u>
<b>Shareholders' Equity</b>		
Common stock and paid-in capital .....	1,442	1,406
Retained earnings .....	3,404	2,786
Accumulated other comprehensive income .....	2,151	3,379
Treasury stock .....	(1,068)	(763)
Total shareholders' equity .....	<u>5,929</u>	<u>6,808</u>
Total liabilities and shareholders' equity .....	<u>\$ 16,637</u>	<u>\$ 17,222</u>

(Dollars in millions except per share data)

	Years ended December 31,		
	2007	2006	2005
<b>Revenues</b>			
Earned premiums .....	\$ 3,250	\$ 3,278	\$ 3,164
Investment income, net of expenses .....	608	570	526
Realized investment gains and losses .....	382	684	61
Other income .....	19	18	16
Total revenues .....	<u>4,259</u>	<u>4,550</u>	<u>3,767</u>
<b>Benefits and Expenses</b>			
Insurance losses and policyholder benefits .....	1,963	2,128	1,911
Commissions .....	624	630	627
Other operating expenses .....	480	463	406
Total benefits and expenses .....	<u>3,067</u>	<u>3,221</u>	<u>2,944</u>
<b>Income Before Income Taxes</b> .....	<b>1,192</b>	<b>1,329</b>	<b>823</b>
<b>Provision for Income Taxes</b> .....	<b>337</b>	<b>399</b>	<b>221</b>
<b>Net Income</b> .....	<b>\$ 855</b>	<b>\$ 930</b>	<b>\$ 602</b>
<b>Per Common Share</b>			
Net income—basic .....	\$ 5.01	\$ 5.36	\$ 3.44
Net income—diluted .....	\$ 4.97	\$ 5.30	\$ 3.40

# Six-year Summary Financial Information

Cincinnati Financial Corporation and Subsidiaries

(Dollars in millions except per share data)

	Years ended December 31,					
	2007	2006	2005	2004	2003	2002
<b>Financial Highlights</b>						
Net income	\$ 855	\$ 930	\$ 602	\$ 584	\$ 374	\$ 238
One-time items*	—	—	—	—	15	—
Net income before one-time items*	\$ 855	\$ 930	\$ 602	\$ 584	\$ 359	\$ 238
Net realized investment gains and losses, after tax	245	434	40	60	(27)	(62)
Net income before net realized investment gains and losses, before one-time items*	\$ 610	\$ 496	\$ 562	\$ 524	\$ 386	\$ 300
Comprehensive income	(368)	1,057	99	287	815	(232)
<b>Per Share Data (diluted)</b>						
Net income	\$ 4.97	\$ 5.30	\$ 3.40	\$ 3.28	\$ 2.10	\$ 1.32
One-time items*	—	—	—	—	0.09	—
Net income before one-time items*	\$ 4.97	\$ 5.30	\$ 3.40	\$ 3.28	\$ 2.01	\$ 1.32
Net realized investment gains and losses, after tax	1.43	2.48	0.23	0.34	(0.15)	(0.35)
Net income before net realized investment gains and losses, before one-time items*	\$ 3.54	\$ 2.82	\$ 3.17	\$ 2.94	\$ 2.16	\$ 1.67
Cash dividends declared	1.42	1.34	1.21	1.04	0.90	0.81
Book value	35.70	39.38	34.88	35.60	35.10	31.43
<b>Ratio Data</b>						
Investment yield-to-cost (pretax)	6.9%	6.8%	7.0%	7.2%	7.5%	7.9%
Debt-to-capital	12.7	11.0	11.5	11.2	8.9	9.7
Return on equity (ROE) before one-time items*	13.4	14.4	9.8	9.4	6.0	4.1
ROE based on comprehensive income before one-time items*	(5.8)	16.4	1.6	4.6	13.5	(4.0)
<b>Property Casualty Insurance Operations (Statutory)</b>						
Written premiums	\$ 3,117	\$ 3,178	\$ 3,076	\$ 2,997	\$ 2,815	\$ 2,613
Written premiums (adjusted)*	3,149	3,172	3,097	3,026	2,789	2,496
Earned premiums	3,125	3,164	3,058	2,919	2,653	2,391
Loss ratio	46.6%	51.9%	49.2%	49.8%	56.1%	61.5%
Loss expense ratio	12.0	11.6	10.0	10.3	11.6	11.4
Underwriting expense ratio	31.7	30.4	29.8	29.3	26.5	25.5
Combined ratio (reported)	90.3%	93.9%	89.0%	89.4%	94.2%	98.4%
Combined ratio (adjusted)*	90.3%	93.9%	89.0%	89.4%	95.0%	99.6%
Policyholders' surplus	\$ 4,307	\$ 4,723	\$ 4,194	\$ 4,191	\$ 2,783	\$ 2,340
<b>Commercial Lines Property Casualty Insurance Operations (Statutory)</b>						
Written premiums	\$ 2,413	\$ 2,442	\$ 2,290	\$ 2,186	\$ 2,031	\$ 1,905
Written premiums (adjusted)*	2,444	2,435	2,306	2,209	2,009	1,795
Earned premiums	2,411	2,402	2,254	2,126	1,908	1,721
Loss ratio	44.8%	48.4%	46.6%	43.4%	51.2%	57.8%
Loss expense ratio	13.1	12.7	11.0	10.9	12.7	12.5
Underwriting expense ratio	31.3	29.7	29.5	29.4	27.0	25.0
Combined ratio (reported)	89.2%	90.8%	87.1%	83.7%	90.9%	95.3%
Combined ratio (adjusted)*	89.2%	90.8%	87.1%	83.7%	91.6%	96.8%
<b>Personal Lines Property Casualty Insurance Operations (Statutory)</b>						
Written premiums	\$ 704	\$ 736	\$ 786	\$ 811	\$ 784	\$ 708
Written premiums (adjusted)*	705	737	791	817	780	701
Earned premiums	714	762	804	793	745	670
Loss ratio	53.2%	62.9%	56.7%	66.7%	68.8%	71.0%
Loss expense ratio	8.1	8.3	7.2	8.9	8.9	8.7
Underwriting expense ratio	32.8	32.4	30.4	29.0	25.2	26.8
Combined ratio (reported)	94.1%	103.6%	94.3%	104.6%	102.9%	106.5%
Combined ratio (adjusted)*	94.1%	103.6%	94.3%	104.6%	103.9%	106.8%
<b>Life Insurance Operations (Statutory)</b>						
Written premiums	\$ 167	\$ 161	\$ 205	\$ 193	\$ 143	\$ 220
Net income before realized investment gains and losses	7	(1)	10	26	27	20
Net income	39	28	21	28	20	17
Gross life insurance face amount in force	61,875	56,971	51,493	44,921	38,492	32,486
Admitted assets excluding separate account business	2,283	2,026	1,882	1,713	1,572	1,477
Risk-based capital						
Total adjusted capital	506	556	511	491	443	420
Authorized control level risk-based capital	66	67	52	47	50	47

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# 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 2007 Annual Report on Form 10-K, Item 1A, Risk Factors, Page 21. Although we often review or update our forward-looking statements when events warrant, we caution our readers that we undertake no obligation to do so.

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
  - Inaccurate estimates or assumptions used for critical accounting estimates
  - 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
  - Changing consumer buying habits and consolidation of independent insurance agencies that could alter our competitive advantages
  - 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:
    - Downgrade of the company's financial strength ratings
    - Concerns that doing business with the company is too difficult or
    - Perceptions that the company's level of service, particularly claims service, is no longer a distinguishing characteristic in the marketplace
  - Sustained decline in overall stock market values negatively affecting the company's equity portfolio and book value; in particular a sustained decline in the market value of Fifth Third shares, a significant equity holding
  - Securities laws that could limit the manner and timing of our investment transactions
  - Recession or other economic conditions or regulatory, accounting or tax changes resulting in lower demand for insurance products
  - Events, such as the subprime mortgage lending crisis, that lead to a significant decline in the value of a particular security or group of securities, such as our financial sector holdings, and impairment of the asset(s)
  - 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
  - Delays or inadequacies in the development, implementation, performance and benefits of technology projects and enhancements
  - Ability to obtain adequate reinsurance on acceptable terms, amount of reinsurance purchased, financial strength of reinsurers and the potential for non-payment or delay in payment by reinsurers
  - Increased competition that could result in a significant reduction in the company's premium growth rate
  - Underwriting and pricing methods adopted by competitors that could allow them to identify and flexibly price risks, which could decrease our competitive advantages
  - Personal lines pricing and loss trends that lead management to conclude that this segment could not attain sustainable profitability, which could prevent the capitalization of policy acquisition costs
  - Actions of insurance departments, state attorneys general or other regulatory agencies that:
    - Restrict our ability to exit or reduce writings of unprofitable coverages or lines of business
    - Place the insurance industry under greater regulatory scrutiny or result in new statutes, rules and regulations
    - Increase our expenses
    - 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
    - Limit our ability to set fair, adequate and reasonable rates
    - Place us at a disadvantage in the marketplace or
    - Restrict our ability to execute our business model, including the way we compensate agents
  - Adverse outcomes from litigation or administrative proceedings
  - 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
  - Investment activities or market value fluctuations that trigger restrictions applicable to the parent company under the Investment Company Act of 1940
  - Events, such as an epidemic, natural catastrophe, terrorism or construction delays, 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, 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 recent measures affecting corporate financial reporting and governance. The ultimate changes and eventual effects, if any, of these initiatives are uncertain.



# Subsidiary Officers and Directors

As of February 28, 2008, listed alphabetically  
The Cincinnati Insurance Company (CIC)  
The Cincinnati Indemnity Company (CID)  
The Cincinnati Casualty Company (CCC)

The Cincinnati Specialty Underwriters Insurance Company (CSU)  
The Cincinnati Life Insurance Company (CLIC)

CSU Producer Resources Inc. (C-SUPR)  
CFC Investment Company (CFC-I)  
CinFin Capital Management (CCM)

## Executive Officers

### James E. Benoski

CIC, CID, CCC, CSU, C-SUPR Vice Chairman  
CIC, CID, CCC, CSU, CLIC, C-SUPR Chief Executive Officer  
CIC, CID, CSU, C-SUPR President  
CIC, CID, CCC, CSU, CLIC Chief Insurance Officer  
Director of all subsidiaries

### Donald J. Doyle, Jr., CPCU, AIM

CIC, CID, CCC, CSU, C-SUPR Senior Vice President – Excess & Surplus Lines  
CSU Director

### Craig W. Forrester, CLU

CIC, CID, CCC, CLIC Senior Vice President – Information Technology

### Martin F. Hollenbeck, CFA, CPCU

CIC, CID, CCC, CLIC Vice President – Investments  
CFC-I President and Chief Operating Officer  
CCM President and Director

### Thomas A. Joseph, CPCU

CIC, CID, CCC Senior Vice President – Commercial Lines  
CIC, CID, CCC, CSU Director

### Eric N. Mathews, CPCU, AIAF

CIC, CID, CCC, CLIC Senior Vice President – Corporate Accounting

### Larry R. Plum, CPCU, AR

CCC President  
CIC, CID Senior Vice President – Personal Lines  
CIC, CID, CCC, CSU, CLIC Director

### David H. Popplewell, FALU, LLIF

CLIC President and Chief Operating Officer; Director

### J. F. Scherer

CIC, CID, CCC, CLIC Senior Vice President – Sales & Marketing  
CIC, CID, CCC, CSU, CLIC, CFC-I Director

### John J. Schiff, Jr., CPCU

CIC, CID, CCC, CLIC Chairman of the Executive Committee  
CIC, CID, CCC, CSU, CLIC, C-SUPR, CFC-I Director

### Joan O. Shevchik, CPCU, CLU

CIC, CID, CCC Senior Vice President – Corporate Communications

### Kenneth W. Stecher

CIC, CID, CCC, CSU, CLIC, C-SUPR Chairman, Chief Financial Officer, Executive Vice President and Secretary  
CFC-I Chief Financial Officer, Senior Vice President and Secretary  
CSU, C-SUPR, CCM Treasurer  
Director of all subsidiaries

### Charles P. Stoneburner II, CPCU, AIM

CIC, CID, CCC Senior Vice President – Field Claims

### Timothy L. Timmel

CIC, CID, CCC, CLIC, CFC-I Senior Vice President – Operations  
CIC, CID, CCC, CSU, CLIC, CFC-I Director

## Senior Officers

### Michael R. Abrams

CIC, CID, CCC, CLIC, CCM Vice President – Investments

### Donald R. Adick, FLMI

CLIC Senior Vice President – Life Marketing Administration

### Dawn M. Alcorn

CIC, CID, CCC Vice President – Administrative Services

### Brad E. Behringer

CLIC Senior Vice President and Chief Underwriter

### David L. Burbrink

CLIC Vice President – Life Field Services

### Teresa C. Cracas

CIC, CID, CCC, CLIC Vice President – Planning & Risk Management

### Richard W. Cumming, ChFC, CLU, FSA, MAAA

CIC, CID, CCC, CLIC Senior Vice President and Chief Actuary  
CLIC Director

### Joel W. Davenport, CPCU, AAI

CIC, CID, CCC Vice President – Commercial Lines

### J. Michael Dempsey, CLU

CLIC Vice President – Life Marketing Administration

**Mark R. DesJardins, CPCU, AIM, AIC, ARP**  
CIC, CID, CCC Vice President – Education & Training

### W. Dane Donham, AIM

CIC, CID, CCC Vice President – Commercial Lines

### Harold L. Eggers, CLU, FLMI, FALU, HIAA

CLIC Vice President – Life Policy Issue

### Frederick A. Ferris

CIC, CID, CCC Vice President – Commercial Lines

### Bruce S. Fisher, CPCU, AIC

CIC, CID, CCC Vice President – Headquarters Claims

### Carl C. Gaede, CPCU, AFSB

CIC, CID, CCC Vice President – Bond & Executive Risk

### Gary B. Givler

CIC, CID, CCC Vice President – Headquarters Claims

### David T. Groff, CPCU, FCAS, MAAA

CIC, CID, CCC Vice President – Staff Underwriting

### Kevin E. Guilfoyle

CFC-I Senior Vice President – Leasing

### David L. Helmers, CPCU, API, ARE, AIM

CIC, CID, CCC Vice President – Personal Lines

### Theresa A. Hoffer

CIC, CID, CCC, CLIC Vice President – Corporate Accounting  
CIC, CID, CCC Treasurer

### Timothy D. Huntington, CPCU, AU

CIC, CID, CCC Vice President – Commercial Lines

### Thomas H. Kelly

CIC, CID, CCC Vice President – Bond & Executive Risk

### Christopher O. Kendall, CPCU, AIT, AIM, ARE, ARM, ARP

CIC, CID, CCC Vice President – Commercial Lines

### Gary J. Kline, CPCU

CIC, CID, CCC Vice President – Commercial Lines

### Robert L. Laymon

CIC, CID, CCC Vice President – Bond & Executive Risk

### Steven W. Leibel, CPCU, AIM

CIC, CID, CCC Vice President – Personal Lines

### Jerry L. Litton

CFC-I Treasurer

### Richard L. Mathews, CPCU

CIC, CID, CCC, CLIC Vice President – Information Technology

### Richard P. Matson

CIC, CID, CCC, CLIC, CFC-I Vice President – Purchasing/Fleet

### David E. McKinney, CPCU, AIM

CIC, CID, CCC, Vice President – Commercial Lines

### Kenneth S. Miller, CLU, ChFC

CIC, CID, CCC, CLIC Senior Vice President – Investments

### Robyn C. Muhlberg

CIC, CID, CCC, CLIC Vice President – Information Technology

### Martin J. Mullen, CPCU

CIC, CID, CCC Vice President – Headquarters Claims

### Gary A. Nichols

CIC, CID, CCC Vice President – Headquarters Claims

### Glenn D. Nicholson, LLIF

CLIC Senior Vice President and Senior Marketing Officer; Director

### Michael K. O'Connor, CFA, CPCU, AFSB

CIC, CID, CCC, CLIC, CCM Vice President – Investments

### Todd H. Pendery, FLMI

CIC, CID, CCC, CLIC Vice President – Corporate Accounting

CLIC Treasurer

### Marc C. Phillips, CPCU, AIM

CIC, CCC, CID Vice President – Commercial Lines

### Ronald L. Robinson

CIC, CID, CCC Vice President – Field Claims

### Michael A. Rouse

CIC, CID, CCC Vice President – Commercial Lines

### Thomas J. Scheid

CIC, CID, CCC, CLIC Vice President – Inspection Services & Facilities

### Gregory D. Schmidt, CPCU, ARP, CPP, ACP, ARC

CIC, CID, CCC, CLIC Vice President – Staff Underwriting

### J. B. Shockey, CPCU, CIC, CLU

CIC, CID, CCC Vice President – Sales & Marketing

### David W. Sloan

CFC-I Vice President – Leasing

### Scott K. Smith, CPCU, ARM, AIM, AU, AAI

CIC, CID, CCC Vice President – Commercial Lines

### Steven A. Soloria, CFA, CPCU

CIC, CID, CCC, CLIC, CCM Vice President – Investments  
CCM Secretary

### Gary B. Stuart

CIC, CID, CCC Vice President – Sales & Marketing

### Duane I. Swanson, CIC

CIC, CID, CCC Vice President – Sales & Marketing

### Philip J. Van Houten, CFE, FCLS

CIC, CID, CCC Vice President – Special Investigations

### Stephen A. Ventre, CPCU

CIC, CID, CCC Vice President – Commercial Lines

### Jody L. Wainscott

CIC, CID, CCC Vice President – Research & Development

### Michael B. Wedig, CPA

CIC, CID, CCC, CLIC Vice President – Corporate Accounting

### Paul W. Wells

CIC, CID, CCC, Vice President – Bond & Executive Risk

### Mark A. Welsh

CIC, CID, CCC, CLIC Vice President – Regulatory & Consumer Relations

### Mark S. Wietmarschen

CIC, CID, CCC Vice President – Commercial Lines

### Heather J. Wietzel

CIC, CID, CCC Vice President and Investor Relations Officer

### Gregory J. Ziegler

CIC, CID, CCC, CLIC, CFC-I Vice President – Personnel

### Teresa C. Cracas

CIC, CID, CCC, CLIC Counsel

### Eugene M. Gelfand

CIC, CID, CCC, CLIC Counsel

### Mark J. Huller

CIC, CID, CCC, CLIC Senior Counsel

### G. Gregory Lewis

CIC, CID, CCC, CLIC Counsel

### Lisa A. Love

CIC, CID, CCC, CLIC Senior Counsel

### Stephen C. Roach

CIC, CID, CCC, CLIC Counsel

## Non-Officer Directors

### William F. Bahl, CFA, CIC

CIC, CID, CCC, CSU, CLIC

### Gregory T. Bier, CPA (Ret.)

CIC, CID, CCC, CSU, CLIC

### W. Rodney McMullen

CIC, CID, CCC, CSU, CLIC

### Thomas R. Schiff

CIC, CID, CCC, CSU, CLIC

### Larry R. Webb, CPCU

CIC, CID, CCC, CSU

### E. Anthony Woods

CIC, CID, CCC, CSU, CLIC

## CIC Directors Emeriti

### Vincent H. Beckman

### Robert J. Driehaus

### Richard L. Hildbold, CPCU

### Robert C. Schiff

### William H. Zimmer

# Cincinnati Financial Corporation Officers and Directors

(as of July 1, 2008)

## Directors

### William F. Bahl, CFA, CIC

Chairman  
Bahl & Gaynor Investment Counsel Inc.  
Director since 1995 (1)(3)(4)(5\*)

### James E. Benoski

Vice Chairman  
Cincinnati Financial Corporation  
Director since 2000 (3)(4)

### Gregory T. Bier, CPA (Ret.)

Managing Partner (Ret.), Cincinnati Office  
Deloitte & Touche LLP  
Director since 2006 (1)(4)

### Kenneth C. Lichtendahl

President and Chief Executive Officer  
Tradewinds Beverage Company  
Director since 1988 (1\*)(2)(5)

### W. Rodney McMullen

Vice Chairman  
The Kroger Co.  
Director since 2001 (2\*)(3)(4)

### Gretchen W. Price

Chief Financial Officer  
philosophy inc.  
(skincare and cosmetics)  
Director since 2002 (1)(2)(5)

### John J. Schiff, Jr., CPCU

Chairman  
Cincinnati Financial Corporation  
Director since 1968 (3\*)(4\*)

### Thomas R. Schiff

Chairman and Chief Executive Officer  
John J. & Thomas R. Schiff & Co. Inc.  
(insurance agency)  
Director since 1975 (4)

### Douglas S. Skidmore

President and Chief Executive Officer  
Skidmore Sales & Distributing Company Inc.  
(food distribution)  
Director since 2004 (1)(5)

### Kenneth W. Stecher

President and Chief Executive Officer  
Cincinnati Financial Corporation  
Director since 2008 (3)(4)

### John F. Steele, Jr.

Chairman and Chief Executive Officer  
Hilltop Basic Resources Inc.  
(aggregates/concrete supplier)  
Director since 2005 (1)

### Larry R. Webb, CPCU

President  
Webb Insurance Agency Inc.  
Director since 1979 (3)

### E. Anthony Woods

Chairman and Chief Executive Officer  
SupportSource LLC  
(health care consulting)  
Director since 1998 (2)(3)(4)

- (1) Audit Committee
  - (2) Compensation Committee
  - (3) Executive Committee
  - (4) Investment Committee; also  
Richard M. Burridge, CFA, adviser
  - (5) Nominating Committee
- \* Committee Chair



W.F. Bahl



J.E. Benoski



G.T. Bier



K.C. Lichtendahl



W.R. McMullen



G.W. Price



J.J. Schiff, Jr.



T.R. Schiff



D.S. Skidmore



K.W. Stecher



J.F. Steele, Jr.



L.R. Webb



E.A. Woods

## Officers

### John J. Schiff, Jr., CPCU

Chairman

### James E. Benoski

Vice Chairman

### Kenneth W. Stecher

President and Chief Executive Officer

### Steven J. Johnson, FCAS, MAAA, CFA

Chief Financial Officer, Secretary and Treasurer

### Martin F. Hollenbeck, CFA, CPCU

Senior Vice President and Manager –  
Investments, Assistant Secretary and Assistant  
Treasurer

### Eric N. Mathews, CPCU, AIAF

Principal Accounting Officer, Vice President,  
Assistant Secretary and Assistant Treasurer

## Directors Emeriti

Vincent H. Beckman  
Michael Brown  
Robert J. Driehaus  
John E. Field, CPCU  
Jackson H. Randolph  
Lawrence H. Rogers II  
John Sawyer

Robert C. Schiff  
Frank J. Schultheis  
David B. Sharrock  
John M. Shepherd  
Thomas J. Smart  
Alan R. Weiler, CPCU  
William H. Zimmer

# Shareholder Information

Cincinnati Financial Corporation had approximately 12,000 shareholders of record and approximately 46,000 beneficial shareholders as of December 31, 2007. Many of the company's independent agent representatives and most of the 4,087 associates of its subsidiaries own the company's common stock.

## Common Stock Price and Dividend Data

Common shares are traded under the symbol CINF on the NASDAQ Global Select Market.

Quarter:	2007				2006			
	1 <sup>st</sup>	2 <sup>nd</sup>	3 <sup>rd</sup>	4 <sup>th</sup>	1 <sup>st</sup>	2 <sup>nd</sup>	3 <sup>rd</sup>	4 <sup>th</sup>
High	\$ 45.92	\$ 47.62	\$ 44.79	\$ 44.84	\$ 45.56	\$ 47.01	\$ 48.44	\$ 49.07
Low	42.24	42.57	36.91	38.37	42.07	41.43	45.93	44.25
Period-end close	42.40	43.40	43.31	39.54	42.07	47.01	48.12	45.31
Cash dividends declared	0.355	0.355	0.355	0.355	0.335	0.335	0.335	0.335

## Annual Meeting

Shareholders are invited to attend the Annual Meeting of Shareholders of Cincinnati Financial Corporation at 9:30 a.m. on Saturday, May 3, 2008, at the Cincinnati Art Museum in Eden Park, Cincinnati, Ohio. You may listen to an audio webcast of the event by visiting the Investors section of the company's Web site, [www.cinfin.com](http://www.cinfin.com).

## Independent Registered Public Accounting Firm

Deloitte & Touche LLP  
250 East Fifth Street  
Cincinnati, Ohio 45202-5109

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## Contact Information

Communications directed to the company's secretary, Kenneth W. Stecher, chief financial officer and executive vice president, are shared with the appropriate individual(s). Or, you may directly access services:

**Investors:** Investor Relations responds to investor inquiries about Cincinnati Financial Corporation and its performance.

Heather J. Wietzel – Vice President, Investor Relations  
513-870-2768 or [investor\\_inquiries@cinfin.com](mailto:investor_inquiries@cinfin.com)

**Shareholders:** Shareholder Services provides stock transfer services, fulfills requests for shareholder materials and assists registered shareholders who wish to update account information or enroll in shareholder plans.

Jerry L. Litton – Assistant Vice President, Shareholder Services  
513-870-2639 or [shareholder\\_inquiries@cinfin.com](mailto:shareholder_inquiries@cinfin.com)

**Media:** Corporate Communications assists media representatives seeking information or comment from Cincinnati Financial Corporation or its subsidiaries.

Joan O. Shevchik, CPCU, CLU – Senior Vice President, Corporate Communications  
513-603-5323 or [media\\_inquiries@cinfin.com](mailto:media_inquiries@cinfin.com)

## Cincinnati Financial Corporation

The Cincinnati Insurance Company  
The Cincinnati Casualty Company  
The Cincinnati Indemnity Company  
The Cincinnati Specialty Underwriters Insurance Company

The Cincinnati Life Insurance Company  
CSU Producer Resources Inc.  
CFC Investment Company  
CinFin Capital Management Company

### Mailing Address:

P.O. Box 145496  
Cincinnati, Ohio 45250-5496

Phone: 513-870-2000

Fax: 513-870-2066

[www.cinfin.com](http://www.cinfin.com)

### Street Address:

6200 South Gilmore Road  
Fairfield, Ohio 45014-5141





# Cincinnati Financial Corporation

## 2008 Shareholder Meeting Notice and Proxy Statement

March 20, 2008

### **To the Shareholders of Cincinnati Financial Corporation:**

You are cordially invited to attend the Annual Meeting of Shareholders of Cincinnati Financial Corporation, which will take place at 9:30 a.m. on Saturday, May 3, 2008, at the Cincinnati Art Museum, located in Eden Park, Cincinnati, Ohio. The business to be conducted at the meeting includes:

1. Electing one director for a term of two years and four directors for terms of three years,
2. Ratifying the selection of Deloitte & Touche LLP as the company's independent registered public accounting firm for 2008,
3. Amending the company's Code of Regulations to provide express authority for uncertificated shares,
4. Transacting such other business as may properly come before the meeting.

Shareholders of record at the close of business on March 5, 2008, are entitled to vote at the meeting.

Whether or not you plan to attend the meeting, please cast your vote as promptly as possible. We encourage you to vote via the Internet. It is convenient and saves your company significant postage and processing costs. You also may submit your vote by telephone or by mail, if you prefer.

Your Internet or telephone vote must be received by 11:59 p.m. Eastern Daylight saving Time on May 2, 2008, to be counted in the final tabulation. Your interest and participation in the affairs of the company are appreciated.

/S/ Kenneth W. Stecher

Kenneth W. Stecher  
Secretary

## About This Proxy Statement

The mission of the board is to encourage, facilitate and foster the long-term success of Cincinnati Financial Corporation. The board directs management in the performance of the company's obligations to our independent agents, policyholders, associates, communities and suppliers in a manner consistent with the company's mission and with the board's responsibility to shareholders to achieve the highest sustainable shareholder value over the long term.

### Notice and Access Background

The board is committed to full, fair, accurate, timely and clear disclosure in our periodic reports and other public statements. Under new rules from the Securities and Exchange Commission (SEC), this year we are making proxy materials and our annual report available to our shareholders on the Internet. To announce their availability, we are sending a Notice that tells how to easily obtain them online or through the mail. The Notice also provides instructions on proxy voting for matters before shareholders, whether online, by telephone or through the mail.

We are offering the same types of information about our company as in prior years, but on a different schedule. As each item is published, it appears online in an integrated annual report format. Many items will be available to you earlier than you received them in the past, because you no longer have to wait until all sections of our annual report are printed.

To ease the transition for shareholders accustomed to paper annual report and proxy mailings, your company is electing this year to mail information beyond the new requirements. We will send a Second Notice in April with a proxy card to simplify voting by mail. It will be followed by a mailing of this Proxy Statement with a Chairman's and President's Letter. The letter presents management's perspectives on your company's 2007 performance and trends that may affect performance in 2008 and beyond.

With either Notice card in hand to find your individualized and secure Control Number, you may visit [www.proxyvote.com](http://www.proxyvote.com) to view the Proxy Statement and 2007 Annual Report, to request printed copies of these materials or to vote. Shareholders and other interested individuals also may view these and other materials by visiting the Investor section of [www.cinfin.com](http://www.cinfin.com). Shareholders can choose to receive information via electronic delivery.

### Annual Report and Annual Report on Form 10-K

You can obtain our 2007 Annual Report on Form 10-K as filed with the SEC at no cost in several different ways. You may view, search or print the document online from the Investors section of [www.cinfin.com](http://www.cinfin.com). You may ask that a copy be mailed to you by contacting the secretary of Cincinnati Financial Corporation or directly requesting it from Shareholder Services. Please see the Investor Contact Page of our Web site for details.

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## About the Annual Meeting

***Who is soliciting my vote?*** – The board of directors of Cincinnati Financial Corporation is soliciting your vote for the 2008 Annual Meeting of Shareholders.

***Who is entitled to vote?*** – Shareholders of record at the close of business on March 5, 2008, may vote.

***How many votes do I have?*** – You have one vote for each share of common stock you owned on March 5, 2008.

***How many votes can be cast by all shareholders?*** – 164,263,431 outstanding shares of common stock can be voted as of the close of business on March 5, 2008.

***How many shares must be represented to hold the meeting?*** – A majority of the outstanding shares, or 82,131,716, must be represented to hold the meeting.

***How many votes are needed to elect directors and to approve the proposals?*** – The nominees for director receiving the five highest vote totals will be elected as directors. Our independent registered public accounting firm is ratified if affirmative votes cast are at least a majority of the stock represented at the meeting. The proposal to amend the company's Code of Regulations will be approved if votes cast in favor of the proposal are at least a majority of the company's outstanding common stock.

***How do I vote?*** – Shareholders may vote by proxy, whether or not you attend the meeting, in one of three ways:

- Internet – Please follow the instructions on the First or Second Notices that instruct you to visit [www.proxyvote.com](http://www.proxyvote.com) to complete an electronic proxy card. You will need the Control Number given on the Notices. The deadline for Internet voting is 11:59 p.m., Eastern Daylight-saving Time, May 2, 2008.
- Telephone – Please follow the instructions on the First or Second Notices that instruct you to call the toll-free telephone number provided with the Notices. You will need the Control Number given on either Notice. The deadline for telephone voting is 11:59 p.m., Eastern Daylight-saving Time, May 2, 2008.
- Mail – Please complete, sign, date and return the proxy card provided as part of our Second Notice. You also may request a proxy card by following the instructions on the First or Second Notices.

We are mailing First Notices by March 24, 2008, and Second Notices the week of April 1, 2008.

***If I prefer to vote by mail, where do I locate my proxy card?*** – This year, if you hold shares directly in your name, your proxy card will arrive with our Second Notice. The proxy card is not enclosed with this proxy statement. If you cannot locate the card, you may obtain another by calling 1-800-690-6903.

***Can I change my vote or revoke my proxy?*** – Yes. Just cast a new vote by Internet or telephone or send in a new signed proxy card with a later date. If you hold your Cincinnati Financial common stock certificates directly in your name, you may send a written notice of revocation to the secretary of the company. If you hold your Cincinnati Financial common stock certificates directly in your name and attend the annual meeting, you also may choose to vote in person at the meeting. To do so, at the meeting you can request a ballot and direct that your previously submitted proxy not be used. Otherwise, your attendance itself does not constitute a revocation of your previously submitted proxy.

**What if I vote “abstain?”** – A vote to abstain has no effect on the votes required to elect directors or ratify our independent registered public accounting firm. A vote to abstain has the same effect as a vote against the proposal to amend the Code of Regulations.

**Can my shares be voted if I don’t return my proxy and don’t attend the annual meeting?** – If your shares are registered in your name, the answer is no. If your shares are registered in the name of a bank, broker or other nominee and you do not direct your nominee as to how to vote your shares, applicable rules provide that the nominee generally may vote your shares on any of the routine matters scheduled to come before the meeting. Routine matters at the 2008 annual meeting include the election of directors and ratification of the independent registered public accounting firm. Routine matters do not include the proposed amendment to the Code of Regulations. If a bank, broker or other nominee indicates on a proxy that it does not have discretionary authority to vote certain shares on a particular matter, these shares (called broker non-votes) will be counted as present in determining whether we have a quorum but will not be counted for the purpose of determining the number of votes cast for the proposed amendment to the Code of Regulations. In other words, a broker non-vote is effectively a “No” vote.

**How are the votes counted?** – Votes cast by proxy are tabulated prior to the meeting by the holders of the proxies. Inspectors of election appointed at the meeting count the votes and announce the results. The proxy agent reserves the right not to vote any proxies that are altered in a manner not intended by the instructions contained in the proxy.

**Could other matters be decided at the meeting?** – We do not know of any matters to be considered at the annual meeting other than the election of directors, ratification of the company’s independent registered public accounting firm and amendment of the Code of Regulations, as described in this proxy statement. For any other matters that do properly come before the meeting, your shares will be voted at the discretion of the proxy holder.

**Who can attend the meeting?** – The meeting is open to all interested parties.

**Can I listen to the meeting if I cannot attend in person?** – If you have access to the Internet, you can listen to a live webcast of the meeting. Instructions will be available on the Investors page of [www.cinfin.com](http://www.cinfin.com) approximately two weeks before the meeting. An audio replay will be available on the Web site within two hours after the close of the meeting.

## **Business to Be Conducted at the Meeting**

### **Election of Directors**

The board of directors currently consists of 13 directors divided into three classes, and each year shareholders elect the directors in one class to serve terms of three years. The term of office of five of the directors expires as of the 2008 Annual Meeting of Shareholders. To balance our classes, one nominee is standing for election to a term of two years.

**The board of directors recommends a vote FOR Larry R. Webb as director to hold office until the 2010 Annual Meeting of Shareholders and Kenneth C. Lichtendahl, W. Rodney McMullen, Thomas R. Schiff and John F. Steele, Jr. as directors to hold office until the 2011 Annual Meeting of Shareholders and until their successors are elected.**

We do not know of any reason that any of the nominees for director would not accept the nomination, and it is intended that votes will be cast to elect all five nominees as directors. In the event, however, that any nominee should refuse or be unable to accept the nomination, the people acting under the proxies intend to vote for the election of such person or people as the board of directors may recommend.

See Information Regarding the Board of Directors, Page 10, for more information on our board and its members.

### **Management's Proposal to Ratify Appointment of the Independent Registered Public Accounting Firm**

The audit committee has appointed the firm of Deloitte & Touche LLP as the company's independent registered public accounting firm for 2008. Although action by shareholders in this matter is not required, the audit committee believes that it is appropriate to seek shareholder ratification of this appointment and to seriously consider shareholder opinion on this issue.

Representatives from Deloitte & Touche LLP, which also served as the company's independent registered public accounting firm for the last calendar year, will be present at the 2008 Annual Meeting of Shareholders and will be afforded the opportunity to make any statements they wish and to answer appropriate questions.

To ratify the appointment of Deloitte & Touche LLP, a majority of votes cast at the meeting must be voted for the proposal.

**The board of directors recommends a vote FOR the proposal to ratify appointment of the independent registered public accounting firm.**

See Audit-Related Matters, Page 15, for more information on our independent registered public accounting firm.

### **Management's Proposal to Amend Cincinnati Financial Corporation's Code of Regulations**

At its meeting on August 10, 2007, the board of directors voted to recommend to shareholders that the company provide for express authorization for uncertificated shares as required by NASDAQ listing standards by amending Article IV of the Code of Regulations as follows:

**“Article IV, Section 1. Form.** If shares are represented by certificates, certificates for shares of the Corporation shall be in such form as the board of directors may, from time to time, approve. The Board of Directors may provide that some or all of any or all classes

and series of the Corporation's shares shall be uncertificated shares, provided that such authorization shall not apply to shares represented by a certificate until the certificate is surrendered to the corporation and that the authorization shall not apply to a certificated security issued in exchange for an uncertificated security. Within a reasonable time after the issuance or transfer of uncertificated shares, the Corporation shall send to the registered owner of the shares a written notice containing the information required to be set forth or stated on certificates pursuant to division (A) of Section 1701.25 of the Ohio Revised Code.”

Our company’s shares are traded on the NASDAQ Global Select Market and the company is therefore required to comply with all applicable NASDAQ listing standards. Beginning January 1, 2008, all equity securities listed on NASDAQ were required to be eligible for Direct Registration System (DRS). A DRS allows an investor to establish a book-entry securities position on the books of the issuer. That position can be used to electronically transfer that securities position between the transfer agent and the broker-dealer through facilities administered by a registered clearing agency, such as a securities depository. The book-entry position can be established either through the issuer's transfer agent or through the investor's broker-dealer. Cincinnati Financial Corporation intends to continue offering physical share certificates, unless otherwise requested by a shareholder.

The SEC has stated that a DRS provides for “more accurate, quicker and more cost-efficient transfers; faster distribution of sale proceeds; reduced number of lost or stolen certificates and a reduction in the associated certificate replacement costs.”

Under applicable Ohio law, a corporation’s board of directors may authorize the issuance of uncertificated securities under prescribed circumstances, unless the Articles of Incorporation or Regulations provide otherwise. Our company currently is authorized to issue uncertificated securities and complies with the applicable NASDAQ listing requirement even though our Articles of Incorporation and Code of Regulations presently do not expressly address this issue. We believe it is prudent to amend the Code of Regulations to provide express authority for uncertificated shares. Amending the Code of Regulations requires the affirmative vote of a majority of the outstanding shares.

Adoption of this proposal to amend the Code of Regulations requires the affirmative vote of the holders of at least a majority of the company's outstanding common stock. Abstentions and broker non-votes will therefore have the same effect as votes against the proposal. Proxies for common shares solicited by the board will be voted FOR the proposal unless shareholders specify a contrary choice in their proxies.

**The board of directors recommends a vote FOR the amendment to the Code of Regulations.**

## Security Ownership of Principal Shareholders and Management

Under Section 13(d) of the Securities Exchange Act of 1934 (Exchange Act), a beneficial owner of a security is any person who directly or indirectly has or shares voting power or investment authority over such security. A beneficial owner under this definition need not enjoy the economic benefit of such securities. The following are the only shareholders known to the company who are deemed to be beneficial owners of at least 5 percent of our common stock as of February 29, 2008. John J. Schiff, Jr. and Thomas R. Schiff are directors of the company.

Title of Class	Name and Address of Beneficial Owner	Amount and Nature of Beneficial Ownership	Footnote Reference	Percent of Class
Common stock	John J. Schiff, Jr., CPCU Cincinnati Financial Corporation 6200 South Gilmore Fairfield, OH 45014	12,415,444	(1)(2)(3)(4)(5)	7.53
Common stock	Thomas R. Schiff Cincinnati Financial Corporation 6200 South Gilmore Fairfield, OH 45014	9,429,786	(1)(2)(5)(6)	5.72

John J. Schiff, Jr., and Thomas R. Schiff are brothers.

The outstanding common shares beneficially owned by each other director and nondirector executive officers as of February 29, 2008, are shown below:

Name of Beneficial Owner	Amount and Nature of Beneficial Ownership	Footnote Reference	Percent of Class
<b>Other Directors</b>			
William F. Bahl, CFA, CIC	220,154	(7)	0.13
James E. Benoski	524,435	(3)(5)	0.32
Gregory T. Bier	3,869		-
Dirk J. Debbink	12,063		0.01
Kenneth C. Lichtendahl	17,546		0.01
W. Rodney McMullen	21,793		0.01
Gretchen W. Price	10,439		0.01
Douglas S. Skidmore	20,791	(8)	0.01
John F. Steele, Jr.	6,566		-
Larry R. Webb, CPCU	477,051	(9)	0.29
E. Anthony Woods	15,850		0.01
<b>Nondirector Executive Officers</b>			
Donald J. Doyle, Jr., CPCU, AIM	71,426	(3)(5)	0.04
Craig W. Forrester, CLU	83,631	(3)(4)(5)	0.05
Martin F. Hollenbeck, CFA, CPCU	33,957	(3)(4)(5)	0.02
Thomas A. Joseph, CPCU	157,741	(3)(5)	0.10
Eric N. Mathews, CPCU, AIAF	89,360	(3)(5)	0.05
Larry R. Plum, CPCU, ARe	271,904	(3)(4)(5)	0.16
David Popplewell, FALU, LLIF	162,570	(3)(5)	0.10
Jacob F. Scherer, Jr.	242,065	(3)(5)	0.15
Joan O. Shevchik, CPCU, CLU	64,496	(3)(5)	0.04
Kenneth W. Stecher	213,776	(3)(5)	0.13
Charles P. Stoneburner II, CPCU, AIM	39,374	(3)(5)	0.02
Timothy L. Timmel	270,091	(3)(4)(5)	0.16
<b>All directors and nondirector executive officers as a group (25 individuals)</b>	<b>17,527,225</b>		<b>10.63</b>

Except as otherwise indicated in the notes below, each person has sole voting and investment authority with respect to the common shares noted.

- (1) Includes 4,034,825 shares owned of record by the John J. and Mary R. Schiff Foundation and 3,092,693 shares owned of record by the John J. Schiff Charitable Lead Trust, the trustees of all of which are Mr. J. Schiff, Jr., Mr. T. Schiff and Ms. Suzanne S. Reid, who share voting and investment authority equally.
- (2) Includes 107,186 shares owned of record by the John J. & Thomas R. Schiff & Co. Inc. pension plan, the trustees of which are Mr. J. Schiff, Jr., and Mr. T. Schiff, who share voting and investment authority; and 114,249 shares owned by John J. & Thomas R. Schiff & Co. Inc. of which Mr. J. Schiff, Jr., and Mr. T. Schiff are principal owners.

- (3) Includes shares available within 60 days from exercise of stock options in the amount of 477,080 shares for Mr. J. Schiff, Jr.; 373,127 shares for Mr. Benoski; 57,093 shares for Mr. Doyle; 45,776 shares for Mr. Forrester; 26,777 shares for Mr. Hollenbeck; 123,908 shares for Mr. Joseph; 54,622 shares for Mr. Mathews; 138,503 shares for Mr. Plum; 121,965 shares for Mr. Popplewell; 143,753 shares for Mr. Scherer; 40,237 shares for Ms. Shevchik; 123,511 shares for Mr. Stecher; 24,073 shares for Mr. Stoneburner II; and 143,753 shares for Mr. Timmel.
- (4) Includes shares held in the company's nonqualified savings plan for highly compensated associates in the amount of 12,025 shares for Mr. J. Schiff, Jr.; 897 shares for Mr. Forrester; 3,138 shares for Mr. Hollenbeck; 2,111 shares for Mr. Plum; and 6,886 shares for Mr. Timmel. Individuals participating in this plan do not have the right to vote or direct the disposition of shares.
- (5) Includes shares pledged as collateral in the amount of 1,146,551 shares for Mr. J. Schiff, Jr.; 962,113 shares for Mr. T. Schiff; 26,000 shares for Mr. Benoski; 13,895 shares for Mr. Doyle; 15,354 shares for Mr. Forrester; 3,010 shares for Mr. Hollenbeck; 32,680 shares for Mr. Joseph; 30,544 shares for Mr. Mathews; 119,292 shares for Mr. Plum; 40,129 shares for Mr. Popplewell; 96,331 shares for Mr. Scherer; 21,323 shares for Ms. Shevchik; 28,478 shares for Mr. Stecher; 15,301 shares for Mr. Stoneburner II and 116,571 shares for Mr. Timmel.
- (6) Includes 12,800 shares owned by the Thomas R. Schiff Foundation of which Mr. Schiff has voting and investment authority.
- (7) Includes 1,132 shares owned of record and held by Bahl & Gaynor Profit Sharing Trust, of which Mr. Bahl is trustee; and 8,821 shares held in the Bahl Family Foundation, of which Mr. Bahl is president; and 10,256 shares held in trusts for the benefit of his children, for which Mr. Bahl is not the trustee and has no investment or voting rights for the trusts.
- (8) Includes 7,035 shares owned of record by Skidmore Sales Profit Sharing Plan, of which Mr. Skidmore is an administrator and shares investment authority.
- (9) Includes 186,257 shares owned of record by a limited partnership of which Mr. Webb is a general partner and 43,478 shares owned of record by a trust for the benefit of his wife and children.

### **Section 16(a) Beneficial Ownership Reporting Compliance**

Directors, executive officers and 10 percent shareholders are required to report their beneficial ownership of our stock according to Section 16 of Exchange Act. Those individuals are required by SEC regulations to furnish the company with copies of all Section 16(a) forms they file.

SEC regulations require us to identify in this proxy statement anyone who filed a required report late during the most recent calendar year. Based on our review of forms we received, or written representations from reporting persons stating that they were not required to file these forms, we believe that, during the calendar year 2007, all Section 16(a) filing requirements were satisfied on a timely basis except for the following.

Eric N. Mathews surrendered 491 free and clear shares at \$42.37 per share to fund the exercise of 1,020 nonqualified stock options at an exercise price of \$20.37 per share on March 15, 2007. The Form 4 filed on March 16, 2007, reporting the exercise did not address the surrender of the 491 shares. A Form 4 was filed on March 22, 2007, to report the surrender of the 491 shares.

John F. Steele, Jr. purchased 3,570 shares in the open market at \$39.92 per share on August 15, 2007, and reported the transaction in a Form 5 filed on February 1, 2008.

### **Information Regarding Nondirector Executive Officers**

Executive officers are elected to one-year terms at the annual meetings of the boards of directors of the company and its subsidiaries. Unless otherwise indicated, each executive officer has served continuously since first elected to that position. For each nondirector executive officer, listed are principal positions held currently and over the past five years in the company, our lead property casualty insurance subsidiary, and other subsidiaries when the officer serves as president.

Cincinnati Financial owns 100 percent of its four subsidiaries: The Cincinnati Insurance Company, CFC Investment Company, CinFin Capital Management Company and CSU Producer Resources Inc. The Cincinnati Insurance Company leads the property casualty group and owns 100 percent of its four subsidiaries: The Cincinnati Casualty Company, The Cincinnati Indemnity Company, The Cincinnati Specialty Underwriters Insurance Company and The Cincinnati Life Insurance Company. Some executive officers also serve on various subsidiary boards.



Nondirector Executive Officer (ages and titles as of February 29, 2008)	Primary Title(s) and Business Responsibilities since February 2003 in Cincinnati Financial Corporation and Subsidiaries	Executive Officer since
Donald J. Doyle, Jr., CPCU, AIM (41)	Senior vice president since 2004 of The Cincinnati Insurance Company. Vice president until 2004 of The Cincinnati Insurance Company. Responsible for excess and surplus lines operations.	2008
Craig W. Forrester, CLU (49)	Senior vice president of The Cincinnati Insurance Company. Responsible for information technology systems.	2003
Martin F. Hollenbeck, CFA, CPCU (48)	President since 2008 of CinFin Capital Management Company. President and chief operating officer since 2008 of CFC Investment Company. Vice president since 2005 of The Cincinnati Insurance Company. Assistant vice president until 2005. Responsible for investment operations, leasing and asset management services.	2008
Thomas A. Joseph, CPCU (52)	Senior vice president of The Cincinnati Insurance Company. Responsible for commercial lines underwriting operations except machinery and equipment.	2003
Eric N. Mathews, CPCU, AIAF (52)	Vice president, assistant secretary and assistant treasurer of Cincinnati Financial Corporation. Senior vice president of The Cincinnati Insurance Company. Responsible for property casualty accounting.	2001
Larry R. Plum, CPCU, ARe (61)	President of The Cincinnati Casualty Company. Senior vice president of The Cincinnati Insurance Company. Responsible for personal lines underwriting operations, meetings and travel.	1988
David H. Popplewell, FALU, LLIF (64)	President and chief operating officer of The Cincinnati Life Insurance Company. Responsible for life insurance operations.	1997
Jacob F. Scherer, Jr. (55)	Senior vice president of The Cincinnati Insurance Company. Responsible for sales and marketing, including new commercial lines business and relationships with independent agencies.	1995
Joan O. Shevchik, CPCU, CLU (57)	Senior vice president of The Cincinnati Insurance Company. Responsible for corporate communications.	2003
Kenneth W. Stecher (61)	Executive vice president since 2006, chief financial officer, secretary and treasurer of Cincinnati Financial Corporation. Chairman and executive vice president since 2006, chief financial officer and secretary of The Cincinnati Insurance Company. Senior vice president until 2006 of Cincinnati Financial Corporation and The Cincinnati Insurance Company. Mr. Stecher is the principal accounting officer.	1999
Charles P. Stoneburner II, CPCU, AIM (56)	Senior vice president since 2008 of The Cincinnati Insurance Company. Vice president until 2008. Assistant vice president until 2005. Secretary until 2004. Responsible for field claims operations.	2008
Timothy L. Timmel (59)	Senior vice president of The Cincinnati Insurance Company. Responsible for operations areas including corporate communications, education and training, field claims, government relations, legal and personnel.	1997

## Information Regarding the Board of Directors

The board of directors currently consists of 13 directors divided into three classes, and each year the directors in one class are elected to serve terms of three years. This means that shareholders generally elect one-third of the members of the board of directors annually. The term of office of five directors expires as of the 2008 Annual Meeting of Shareholders.

According to the Sixth Article of the company's Articles of Incorporation, the three classes of the company's directors must be of nearly equal size, with no class having more than one more director than any other class. Because two directors retired in 2007, lowering the size of the board to 13 directors, the classes became unbalanced with five directors whose terms expire in 2008 and 2009 and three directors whose terms expire in 2010. To rebalance the classes, of the five directors with terms expiring in 2008, one director, Larry R. Webb, is nominated for election to a term of two years expiring 2010 and four directors are nominated for election to terms of three years expiring 2011.

For each nominee for election to the office of director and each current director whose term does not expire at this time, listed below are principal business positions held currently and over the past five years. Some directors also serve on various subsidiary boards.

### **Nominees for Directors for Terms Expiring 2011 (ages and titles as of February 29, 2008)**

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Kenneth C. Lichtendahl (59)	Director since 1988. President, chief executive officer and director of Tradewinds Beverage Company, based in Cincinnati.
W. Rodney McMullen (47)	Director since 2001. Vice chairman since 2003 of The Kroger Co., based in Cincinnati. Executive vice president until 2003 of strategy, planning and finance.
Thomas R. Schiff (60)	Director since 1975. Chairman, chief executive officer and agent of John J. & Thomas R. Schiff & Co. Inc., a privately owned independent insurance agency based in the Cincinnati area. Chief executive officer of Lightborne Properties, Lightborne Communications and Lightborne Publications, media companies based in the Cincinnati area.
John F. Steele, Jr. (54)	Director since 2005. Chairman since 2004 and chief executive officer of Hilltop Basic Resources Inc., a family owned aggregates and ready-mixed concrete supplier to the construction industry, based in the Cincinnati area. President until 2004. Director since 2006 of Smook Bros. (Thompson) Inc.

### **Nominee for Director for Term Expiring 2010 (age and title as of February 29, 2008)**

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Larry R. Webb, CPCU (52)	Director since 1979. President, director, a principal owner and agent of Webb Insurance Agency Inc., a privately owned independent insurance agency based in Lima, Ohio.
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### **Continuing Directors for Terms Expiring 2010 (ages and titles as of February 29, 2008)**

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Gregory T. Bier, CPA (Ret.) (61)	Director since 2006. Former managing partner (retired), Cincinnati office of Deloitte & Touche LLP. Director since 2008 of LifePoint Hospitals Inc.
Dirk J. Debbink (52)	Director since 2004. Chairman since 2007 of MSI General Corporation, a design/build construction firm based in Oconomowoc, Wisconsin. President until 2007. Rear Admiral, Reserve Deputy Commander and Chief of Staff, U.S. Pacific Fleet; and, since 2007, Deputy Chief of U.S. Navy Reserve.
Douglas S. Skidmore (45)	Director since 2004. Chief executive officer since 2003, president and director of Skidmore Sales & Distributing Company Inc., a family-owned, full-service distributor and broker of quality industrial food ingredients, based in the Cincinnati area. Chief executive officer since 2006 of Essex Grain Products Inc., a subsidiary of Skidmore Sales & Distributing Company Inc. Managing partner since 2004, Mustang Real Estate Holdings LLC.

## Continuing Directors for Terms Expiring 2009 (ages and title as of February 29, 2008)

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William F. Bahl, CFA, CIC (56)	Director since 1995. Chairman of Bahl & Gaynor Investment Counsel Inc., based in Cincinnati. Trustee until 2006 of The Preferred Group of Funds. Director since 2005 of LCA-Vision Inc.
James E. Benoski (69)	Director since 2000. President since 2006, chief insurance officer since 2004 and vice chairman of Cincinnati Financial Corporation and The Cincinnati Insurance Company, a subsidiary of the company. Chief operating officer since 2006 of Cincinnati Financial Corporation. Chief executive officer since 2006 of The Cincinnati Insurance Company; senior vice president – headquarters claims until 2006.
Gretchen W. Price (53)	Director since 2002. Chief financial officer since 2008 of philosophy inc., an international skin care and cosmetics company, based in Phoenix, Arizona. Vice president until 2008 of go-to-market reinvention for global operations of Procter & Gamble, based in Cincinnati. Vice president until 2007 of finance and accounting for global operations.
John J. Schiff, Jr., CPCU (64)	Director since 1968. Chairman, chief executive officer and, until 2006, president of Cincinnati Financial Corporation. Director and, until 2006, chairman, president and chief executive officer of The Cincinnati Insurance Company. Director of John J. & Thomas R. Schiff & Co. Inc., a privately owned independent insurance agency; Fifth Third Bancorp; and The Standard Register Company; all Cincinnati-area companies.
E. Anthony Woods (67)	Director since 1998. Chairman and chief executive officer of SupportSource LLC, a healthcare consulting firm. Chairman of Deaconess Associations Inc., a healthcare holding company, based in Cincinnati. Chairman since 2006 and director since 2004 of LCA-Vision Inc.

### Meetings of the Board of Directors

Board members are encouraged to attend the Annual Meeting of Shareholders, all meetings of the board and the meetings of committees of which they are a member. The annual meeting of directors is held immediately following the annual shareholders' meeting at the same location. In May 2007, all of the company's then 15 directors attended the Annual Meeting of Shareholders. The board of directors of the company met seven times and the executive committee of the board met five times during 2007. The directors met in executive session four times during 2007. All directors attended at least 80 percent of the board and committee meetings of which they are members.

### Corporate Governance

#### *Codes of Conduct and Committee Charters*

On February 1, 2008, the board of directors re-adopted the Corporate Governance Guidelines, the Code of Ethics for Senior Financial Officers and the Code of Conduct. Charters for the audit, compensation, executive and nominating committees of the board have been updated and re-approved within the last four months. The guidelines, codes and charters are available on our Web site at [www.cinfin.com](http://www.cinfin.com).

#### *Communicating with the Board*

Shareholders may direct a communication to board members by sending it to the attention of the secretary of the company, Cincinnati Financial Corporation, P.O. Box 145496, Cincinnati, Ohio, 45250-5496. The company and board of directors have not established a formal process for determining whether all shareholder communication received by the secretary will be forwarded to directors. Nonetheless, the board welcomes shareholder communication and has instructed the secretary of the company to use reasonable criteria to determine whether correspondence should be forwarded. The board believes that correspondence has been and will continue to be forwarded appropriately. However, exceptions may occur, and the board does not intend to provide management with instructions that limit its ability to make reasonable business decisions. Examples of exceptions would be routine items such as requests for publicly available information that can be provided by company associates; vendor solicitations that appear to be mass-directed to board members of a number of companies; or correspondence that raises issues related to

specific company transactions (insurance policies or investment accounts) where there may be privacy concerns or other issues.

In some circumstances, the board anticipates that management would provide the board or board member with summary information regarding correspondence.

### **Board Composition and Director Independence**

Each year, based on all relevant facts and circumstances, the board determines which directors satisfy the criteria for independence. To be found independent, a director must not have a material relationship with the company, either directly or indirectly as a partner, other than a limited partner, controlling shareholder or executive officer of another organization that has a relationship with the company that could affect the director's ability to exercise independent judgment.

Directors deemed independent are believed to satisfy the definitions of independence required by the rules and regulations of the SEC and the listing standards of NASDAQ. The board has determined that these directors and nominees meet the applicable criteria for independence as of February 1, 2008: William F. Bahl, Gregory T. Bier, Dirk J. Debbink, Kenneth C. Lichtendahl, W. Rodney McMullen, Gretchen W. Price, Douglas S. Skidmore, John F. Steele, Jr. and E. Anthony Woods. When making its determination as to Mr. Bier, the board considered the fact that a subsidiary of the company employs two of his adult children and a daughter-in-law in non-officer positions, and determined that these relationships presented no material conflict of interest and would not affect his ability to exercise his independent judgment in his role as a director. Following the re-election of the directors included in this proxy, a majority (nine) of the 13 directors would meet the applicable criteria for independence under the listing standards of NASDAQ.

### **Standing Committees of the Board of Directors**

The board of directors has five standing committees. Current committee assignments are noted below. The board of directors will review committee assignments at its meeting on May 3, 2008. Charters for the audit, compensation, executive and nominating committees are available on our Web site at [www.cinfin.com](http://www.cinfin.com).

***Audit Committee*** – The purpose of the audit committee is to oversee the process of accounting and financial reporting, audits and financial statements of the company. The committee met four times during the last year. The report of the audit committee begins on Page 15.

Seven independent directors serve on the audit committee: William F. Bahl, Gregory T. Bier, Dirk J. Debbink, Kenneth C. Lichtendahl (chair), Gretchen W. Price, Douglas S. Skidmore and John F. Steele, Jr. Each of these individuals meets the NASDAQ standards for audit committee member independence and also is independent for purposes of Section 10A-3 of the Exchange Act. Further, Mr. Bahl, Mr. Bier and Ms. Price qualify as financial experts according to the SEC definition and meet the standards established by NASDAQ for financial expertise.

***Compensation Committee*** – The compensation committee discharges the responsibility of the board of directors relating to compensation of the company's directors and officers, including its principal executive officers and its internal audit officer. The committee also administers the company's stock-and performance-based compensation plans. The committee met six times during the last year. The report of the compensation committee begins on Page 17.

Four independent directors serve on the compensation committee: Kenneth C. Lichtendahl, W. Rodney McMullen (chair), Gretchen W. Price and E. Anthony Woods.

***Executive Committee*** – The purpose of the executive committee is to exercise the powers of the board of directors in the management of the business and affairs of the company between meetings of the board of directors. The committee met five times during the last year.

Seven directors serve on the executive committee: William F. Bahl, James E. Benoski, Dirk J. Debbink, W. Rodney McMullen, John J. Schiff, Jr. (chair), Larry R. Webb and E. Anthony Woods. Independence requirements do not apply to the executive committee.

***Investment Committee*** – The investment committee provides oversight of the policies and procedures of the investment department of the company and its subsidiaries and reviews the invested assets of the company. The objective of the committee is to oversee the management of the portfolio to ensure the long-term security of the company. The committee met 10 times during the last year.

Seven directors serve on the investment committee: William F. Bahl, Gregory T. Bier, James E. Benoski, W. Rodney McMullen, John J. Schiff, Jr. (chair), Thomas R. Schiff and E. Anthony Woods. Richard M. Burrige, CFA, a former director, serves as an adviser to the committee. Independence requirements do not apply to the investment committee.

***Nominating Committee*** – The nominating committee identifies, recruits and recommends qualified candidates for election as directors and officers of the company and as directors of its subsidiaries. The committee also nominates directors for committee membership. Further, the committee oversees compliance with the corporate governance policies for the company. The committee met three times during the last year.

Four independent directors serve on the nominating committee: William F. Bahl (chair), Kenneth C. Lichtendahl, Gretchen W. Price and Douglas S. Skidmore.

## **Consideration of Director Nominees**

The nominating committee considers many factors when determining the eligibility of candidates for nomination as director. The committee's goal is to nominate candidates who contribute to the board's overall effectiveness in meeting its mission. The committee is charged with identifying nominees with certain characteristics:

- Demonstrated character and integrity
- An ability to work with others
- Sufficient time to devote to the affairs of the company
- Willingness to enter into a long-term association with the company, in keeping with the company's overall business strategy

The nominating committee also considers the needs of the board in accounting and finance, business judgment, management, industry knowledge, leadership and such other areas as the board deems appropriate. The committee further considers factors included in the Corporate Governance Guidelines that might preclude nomination or re-nomination.

In particular, the nominating committee seeks to support our unique, agent-centered business model. The committee believes that the board should include a variety of individuals, serving alongside independent insurance agents who bring a special knowledge of policyholders and agents in the communities where we do business.

Potential board nominees generally are identified by referral. The nominating committee follows a five-part process to evaluate nominees for director. The committee first performs initial screening that includes reviewing background information on the candidates, evaluating their qualifications against the established criteria and, as the committee believes is appropriate, discussing the potential candidates with the individual or individuals making the referrals. Second, for candidates who qualify for additional consideration, the committee interviews the potential nominees as to their background, interests and potential commitment to the company and its operating philosophy. Third, the committee may seek references from sources identified by the candidates as well as sources known to the committee members. Fourth, the committee may ask other members of the board for their input. Finally, the committee develops a list of nominees who exhibit the characteristics desired of directors and satisfy the needs of the board. The committee recommended no new director nominees in 2007.

The nominating committee considers qualified candidates referred by shareholders for nomination as director. Information about such a candidate should be provided in writing to the secretary of the company, giving the candidate's name, biographical data and qualifications, and emphasizing the characteristics set forth in our Corporate Governance Guidelines available on our Web site at [www.cinfin.com](http://www.cinfin.com). Preferably, any such referral would contain sufficient information to enable the committee to preliminarily screen the referred candidate for the needs of the board, if any, in accounting and finance, business judgment, management, industry knowledge, leadership, and also the board's independence requirements. Such information should be provided by August 1 to receive appropriate consideration for the annual meeting held in the following year. The nominating committee does not differentiate among candidates based on the source of the nomination. Since the 2007 annual shareholders' meeting, no fees were paid to any third party to identify, evaluate, or assist in identifying and evaluating potential nominees.

## **Certain Relationships and Transactions**

The audit committee follows a written policy for review and approval of transactions involving the company and related persons, defined as directors and executive officers or their immediate family members, or shareholders owning 5 percent or greater of our outstanding stock. The policy covers any related transaction that meets the minimum threshold for disclosure in the proxy statement under the relevant SEC rules, generally transactions involving amounts exceeding \$120,000 in which a related person has a direct or indirect material interest.

**Policy.** Related person transactions must be approved by the audit committee. As it examines individual transactions for approval, the committee considers:

- Whether the transaction creates a conflict of interest or would violate the company's Code of Conduct
- Whether the transaction would impair the independence of a director
- Whether the transaction would be fair
- Any other factor the committee deems appropriate

**Procedure.** Consideration of transactions with related parties is a regular item on the committee's agenda. Most of the transactions fall into the categories of standard agency contracts with directors who are principals of independent insurance agencies that sell our insurance products or with directors and executive officers who purchase the company's insurance products on the same terms as such products are offered to the public. Because the committee does not believe these classes of transactions create conflicts of interest or otherwise violate our Code of Conduct, the committee deems such transactions pre-approved.

The following transactions in 2007 with related persons were determined to pose no actual conflict of interest and approved by the committee pursuant to its policy.

Michael Brown was a director of Cincinnati Financial Corporation (until May 5, 2007) and a director and president of Cincinnati Bengals Inc. that purchased property and casualty insurance from our insurance subsidiary for premiums totaling \$380,405. Cincinnati Bengals Inc. paid \$177,883 to Cincinnati Financial Corporation's registered investment adviser subsidiary for investment advisory services. Cincinnati Financial Corporation and our subsidiaries made payments to Cincinnati Bengals Inc. for tickets and suite rental in the amount of \$141,400.

John J. Schiff, Jr. is chairman of the board and chief executive officer of Cincinnati Financial Corporation, and a director of The Cincinnati Insurance Company, The Cincinnati Indemnity Company, The Cincinnati Casualty Company, The Cincinnati Life Insurance Company, The Cincinnati Specialty Underwriters Insurance Company, CFC Investment Company and CSU Producer Resources Inc. John J. Schiff, Jr., and Thomas R. Schiff, also a director of Cincinnati Financial Corporation, are principal owners and directors of John J. & Thomas R. Schiff & Co. Inc., a privately owned insurance agency that represents a number of insurance companies, including our insurance subsidiaries. The company's insurance subsidiaries paid John J. & Thomas R. Schiff & Co. Inc. commissions of \$6,226,453. The company purchased various insurance policies through John J. & Thomas R. Schiff & Co. Inc. for premiums totaling \$1,261,614.

John J. & Thomas R. Schiff & Co. Inc. purchased group health coverage from our insurance subsidiary for a premium of \$122,737 and paid rent to the company in the amount of \$122,445 for office space located in the headquarters building.

Jacob F. Scherer is the senior vice president of the sales and marketing department of Cincinnati Financial Corporation's insurance subsidiaries. Mr. Scherer's father is the president of the B.F. Scherer Insurance Agency Inc. In November 2007, Cincinnati Financial purchased 9,905 shares of Cincinnati Financial Corporation common stock at the market price of \$401,499 from the B.F. Scherer Insurance Agency Inc.

John M. Shepherd was a director of Cincinnati Financial Corporation (until May 5, 2007) and chairman, chief executive officer and a principal owner of The Shepherd Chemical Company. Mr. Shepherd, The Shepherd Chemical Company and its subsidiary and affiliated entities purchased property and casualty insurance from our insurance subsidiaries for premiums totaling \$676,987.

Douglas S. Skidmore is a director of Cincinnati Financial Corporation and principal owner, director, chief executive officer and president of Skidmore Sales & Distributing Company Inc. that purchased property, casualty and life insurance from our insurance subsidiaries for premiums totaling \$342,914.

Larry R. Webb is a director of Cincinnati Financial Corporation and president, director and a principal owner of Webb Insurance Agency Inc., a privately owned insurance agency that represents a number of insurance companies, including our insurance subsidiaries. The company's insurance subsidiaries paid Webb Insurance Agency Inc. commissions of \$614,689. Mr. Webb is a beneficiary of The E. Perry Webb Marital Trust from which Cincinnati Financial purchased 193,740 shares of Cincinnati Financial Corporation common stock at the market price of \$8,195,625 in September 2007.

A brother of Timothy L. Timmel, senior vice president of operations of the company's insurance subsidiaries, is a secretary of the company's property casualty insurance subsidiary and manager of workers' compensation claims in the Headquarters Claims department with 30 years of experience in both the Field Claims and Headquarters Claims departments. In 2007, Mr. Timmel's brother earned compensation consisting of salary, cash bonus, stock-based compensation and perquisites totaling \$158,566. The amount of compensation was established by the company in accordance with our employment and compensation practices applicable to associates with equivalent qualifications and responsibilities and holding similar positions.

## **Audit-Related Matters**

### **Report of the Audit Committee**

The audit committee is responsible for monitoring the integrity of the company's consolidated financial statements, the company's system of internal controls, the qualifications and independence of the company's independent registered public accounting firm, the performance of the company's internal audit department and independent registered public accounting firm and the company's compliance with certain legal and regulatory requirements. The committee has sole authority and responsibility to select, determine the compensation of, and evaluate the company's independent registered public accounting firm. The committee has seven independent directors and operates under a written charter. The board has determined that each committee member is independent under the standards of director independence established by the NASDAQ listing requirements and is also "independent" for purposes of Section 10A(m)(3) of the Securities Exchange Act of 1934.

Management is responsible for the financial reporting process, including the system of internal controls, for the preparation of consolidated financial statements in accordance with generally accepted accounting principles and for the report on the company's internal control over financial reporting. The company's independent registered public accounting firm is responsible for auditing those financial statements and expressing an opinion as to their conformity with accounting principles generally accepted in the United States of America (GAAP) and for attesting to management's report on the company's internal control over financial reporting. The committee's responsibility is to oversee and review the financial reporting process and to review and discuss management's report on the company's internal control over financial reporting. The committee is not, however, professionally engaged in the practice of accounting or auditing and does not provide any expert or special assurance as to such financial statements concerning compliance with laws, regulations or generally accepted accounting principles or as to auditor independence. The committee relies, without independent verification, on the information provided to it and on the representations made by management and the independent registered public accounting firm.

The committee reviewed and discussed the audited consolidated financial statements for the fiscal year ended December 31, 2007, with management, the internal auditors and Deloitte & Touche LLP.

The committee also discussed with management, the internal auditors and Deloitte & Touche LLP the process used to support certifications by the company's chief executive officer and chief financial officer that are required by the SEC and the Sarbanes Oxley Act of 2002 to accompany the company's periodic filings with the SEC and the processes used to support management's annual report on the company's internal controls over financial reporting.

The committee also discussed with Deloitte & Touche LLP matters that independent registered public accounting firms must discuss with audit committees under accounting principles generally accepted in the United States of America and standards of the Public Company Accounting Oversight Board, including, among other things, matters related to the conduct of the audit of the company's consolidated financial statements and the matters required to be discussed by Statement on Auditing Standards No. 61, as amended, "Communication with Audit Committees," and Statement on Auditing Standards No. 114, "Communication with Those Charged With Governance."

Deloitte & Touche LLP also provided written disclosures and the letter required by Independence Standards Board Standard No. 1, "Independence Discussions with Audit Committees," and represented that it was independent from the company. The committee discussed with Deloitte & Touche LLP its independence from the company. When considering Deloitte & Touche LLP's independence, the committee considered whether services it provided to the company beyond those rendered in connection with its audit of the company's consolidated financial statements, reviews of the company's interim condensed consolidated financial statements included in its Quarterly Reports on Form 10-Q and the attestation of management's report on internal control over financial reporting were compatible with maintaining its independence. The committee also reviewed, among other things, the audit, audit-related and tax services performed by, and the amount of fees paid for such services, to Deloitte & Touche LLP. The committee received regular updates on the amount of fees and scope of audit, audit-related and tax services provided.

Based on the above-mentioned review and these meetings, discussions and reports, and subject to the limitations on the committee's role and responsibilities referred to above and in the committee's charter, the committee recommended to the board that the company's audited consolidated financial statements for the fiscal year ended December 31, 2007, be included in the company's Annual Report on Form 10-K. The committee also selected Deloitte & Touche LLP as the company's independent registered accounting firm for the fiscal year ending December 31, 2008, and is presenting the selection to the shareholders for ratification.

Submitted by the audit committee:

William F. Bahl, Gregory T. Bier, Dirk J. Debbink, Kenneth C. Lichtendahl (chair), Gretchen W. Price, Douglas S. Skidmore and John F. Steele, Jr.

### **Fees Billed by the Independent Registered Public Accounting Firm**

The audit committee engaged Deloitte & Touche LLP to perform an annual audit of the company's financial statements for the year ended December 31, 2007.

	Year Ended December 31,	
	2007	2006
Audit Fees	\$2,145,000	\$2,185,000
Audit-related Fees	212,027	287,122
Tax Fees	329,777	379,796
Deloitte & Touche LLP Total Fees	<u>\$2,686,804</u>	<u>\$2,851,918</u>

### **Services Provided by the Independent Registered Public Accounting Firm**

All services rendered by the independent registered public accounting firm are permissible under applicable laws and regulations. In 2007 and 2006, all services rendered by the independent registered accounting firm were pre-approved by the audit committee, and no fees were charged pursuant to the de minimis safe harbor exception to the pre-approval requirement described in the audit committee charter.

Under the pre-approval policy, the audit committee pre-approves specific services related to the primary service categories of audit services, audit-related services, tax services, and other services. A "one-time" pre-approval dollar limit for specified services related to a specific primary category is established for the audit period. Examples of non-audit services specified under the policy requiring pre-approval may include: financial and tax due diligence, benefit plan audits, American Institute of Certified Public Accountants (AICPA) agreed upon procedures, Global Investment Performance Standards audits, security and privacy control-related assessments, technology control assessments, technology quality assurance, financial reporting control assessments, enterprise security architecture assessment, tax controversy assistance (IRS examinations), sales tax and lease compliance, employee benefit tax, tax compliance and support, tax research, corporate finance modeling assistance, and allowable actuarial reviews and assistance.

Engagements for services falling below the dollar threshold approved for specified services may be entered into with the consent of the chief financial officer. The committee must individually approve engagements for permissible services not included in the pre-approval list or that exceed the dollar threshold established



for such services. All engagements are periodically reported to the audit committee. Pursuant to the rules of the SEC, the fees billed by the independent registered public accounting firm for services are disclosed in the table above.

**Audit Fees** – These are fees for professional services performed by the independent registered public accounting firm for the audit of the company’s annual financial statements; audit of management’s assessment of internal control over financial reporting; review of financial statements included in our Form 10-K and Form 10-Q filings; and services that are normally provided in connection with statutory and regulatory filings or engagements.

**Audit-related Fees** – These are fees for assurance and related services performed by the independent registered public accounting firm that are reasonably related to the performance of the audit or review of our financial statements. These services include: employee benefit plan audits; examination of Global Investment Performance Standards assertions; and information systems expense reviews.

**Tax Fees** – These are fees for professional services performed by the independent registered public accounting firm with respect to tax compliance and preparation including review of our tax returns and related research as well as IRS audit assistance. In addition to these items, \$8,780 of the tax fees in 2007 were related to tax advice, planning or consulting for retired executives. Our independent registered public accounting firm does not perform any tax shelter work on our behalf.

## **Compensation of Named Executive Officers and Directors**

### **Report of the Compensation Committee**

The compensation committee reviewed and discussed the Compensation Discussion and Analysis with management. Based on the review and discussions, the compensation committee recommended to the board of directors that the Compensation Discussion and Analysis be included in our 2008 proxy statement.

Submitted by the compensation committee:

Kenneth C. Lichtendahl, W. Rodney McMullen (chair), Gretchen W. Price and E. Anthony Woods

### **Compensation Committee Interlocks and Insider Participation**

In 2007, no executive officer of our company served on the board of directors or compensation committee of any entity that compensates any member of the company’s compensation committee.

Until his retirement from the board at the May 2007 Annual Meeting of Shareholders, Michael Brown was a director of Cincinnati Financial Corporation and a director and president of Cincinnati Bengals Inc. John J. Schiff, Jr., chairman and chief executive officer of Cincinnati Financial Corporation, was a director of Cincinnati Bengals Inc. Cincinnati Bengals Inc. has no compensation committee. During the year ended December 31, 2007, Cincinnati Financial Corporation and our subsidiaries paid Cincinnati Bengals Inc. for tickets and suite rental in the amount of \$141,400. Cincinnati Bengals Inc. purchased property and casualty insurance from our insurance subsidiaries with annualized premiums of \$380,405 and paid fees to our registered investment advisor subsidiary of \$177,883.

## **Compensation Discussion and Analysis**

The following discussion and analysis contains statements regarding individual and company performance targets and goals. These targets and goals are disclosed in the limited context of Cincinnati Financial Corporation’s compensation programs and should not be understood to be statements of management’s expectations, outlook, estimates of results or other guidance. We specifically caution investors not to apply these statements to other contexts. We encourage investors to read our Annual Report on Form 10-K for more comprehensive discussion of our expectations for company performance, as well as factors we have identified as risks to our ability to achieve our targets.

### **Introduction**

The compensation committee of the board of directors (committee) is responsible for determining compensation for the executive officers named in the Summary Compensation Table, Page 28 (named

executive officers). The committee endeavors to ensure that overall compensation paid to the named executive officers is appropriate and in line with our overall compensation objective to attract, motivate, reward and retain the executive talent required to achieve our corporate objectives and increase shareholder value. Generally, the types of compensation and benefits provided to the named executive officers are similar to those provided or available to other executive officers, non-executive officers and full-time exempt associates. The key characteristics of our compensation program are:

- We employ our executive officers “at will,” without severance agreements or employment contracts;
- We align executive officer and shareholder financial interests and focus on the long term;
- We can attract, motivate, reward and retain a talented and stable executive officer staff;
- We consider competitive compensation practices and relevant factors without establishing targets for total compensation at specific benchmark percentiles;
- We structure compensation so that a significant portion of the named executive officer’s compensation is realized only when we achieve certain performance measures and when our stock price increases;
- We use processes that include committee review of competitor and internal performance data, compensation practices and plans, management recommendations based on evaluations of individual and company performance; and
- We rely on long-standing, consistently and appropriately applied practices with respect to the timing and pricing of grants of stock-based compensation.

## **Compensation Philosophy**

***Single profit center.*** Our compensation philosophy parallels our business philosophy. We view Cincinnati Financial Corporation as a single profit center in which all operating areas share responsibility for successes and challenges of the enterprise as a whole. Compensation decisions for named executive officers reflect the overall performance of the company as well as individual efforts to establish and maintain relationships with our independent agent customers and position our enterprise and our agents for profitable growth. These efforts produce cash flow from our insurance operations that we invest to obtain both current income and long-term capital appreciation. We believe consistent application of this strategy over the long term, rather than short-term actions, has driven and will continue to drive our operations and generate shareholder value.

***Long-term focus.*** Our compensation practices match our business practices and are designed to achieve steady progress over the long term. We provide what we believe to be adequate and stable current compensation (salary and annual bonus) that generally increases incrementally over time and long-term compensation (equity grants) that generally links the value of that compensation to the performance of the company as a whole and to increases in shareholder value. Our long-term focus also permits us to make compensation decisions for our named executive officers based on our best judgment of the appropriateness of an individual’s actions and the progress achieved in the context of the current environment. This approach allows compensation to reflect progress toward long-term objectives, even when events or conditions in the company, industry or economy affect our reported financial results or when longer periods are required to show the effect of actions taken. We believe these compensation practices encourage named executive officers to maintain a long-term focus on appropriate selection, pricing and management of risk and business strategies, generating cash flow for investments through all insurance market cycles.

We believe long-term trends, seen over multiple reporting periods, generally are better indicators of performance and responsiveness to conditions. The committee places the greatest emphasis on book value growth to assess long-term trends. Book value growth captures both insurance and investment performance in a single measure that also reflects the benefits of our share repurchase program. We also measure average annual total return to shareholders, which captures both changes in the market price of our common stock and the steadily increasing cash dividends we have paid to shareholders. In keeping with our overall compensation philosophy, however, the committee does not employ a mechanical formula to directly tie compensation decisions to either book value growth or average annual total return to shareholders for any specific period of time.

***Broad-based stock-compensation grants.*** We believe people tend to value and protect most that which they have paid for, generally by investing their time, effort or personal funds. Over the long run, we believe

shareholders are better served when associates at all levels have a significant component of their financial net worth invested in the company. For that reason, we grant awards of stock-based compensation not only to our directors and named executive officers, but generally to all full-time exempt associates of the company. We believe this approach encourages associates at all levels to make decisions in the best interest of the company as a whole, linking their personal financial success with the organization's success. Although we do not have access to information about broker accounts, we estimate that approximately 90 percent of our current associates hold shares of Cincinnati Financial Corporation. Recently adopted stock ownership guidelines applicable to all directors and officers will help the committee monitor ownership for all directors and officers. Our Director and Officer Stock Ownership Guidelines may be found at [www.cinfin.com](http://www.cinfin.com).

We award stock-based compensation not only to reward service to the company, but also to provide incentive for individuals to remain in the employ of the company and help it prosper. Over the last two years, the grant date fair value of stock-based compensation has ranged from approximately 15 to 40 percent of the total amount of compensation set by the committee each year for named executive officers (salary, variable cash bonus, incentive cash bonus, and stock-based awards).

***Benchmarking, compensation consultants and peer groups.*** We believe our business philosophies and strategies differentiate our company in many positive ways, while diminishing comparability to industry peer groups. Except by establishing targets for performance-based compensation under certain incentive plans, we do not tie compensation at any level to specific benchmarks or formulas.

We believe the levels of compensation we provide should be competitively reasonable and appropriate for our business needs and circumstances. Our approach is to consider competitive compensation practices and relevant factors rather than establishing total compensation at specific benchmark percentiles. This enables us to respond to dynamics in the labor market, when necessary, and provides us with flexibility in maintaining and enhancing our executive officers' focus, motivation and enthusiasm for our future.

While we do not compare compensation of individual named executive officers with executives carrying similar titles across a peer group, the committee informally reviews peer group performance and compensation data to gain a sense of whether we are providing generally competitive compensation for our named executive officers individually and as a group. The committee traditionally has monitored corporate performance and compensation levels for the named executive officers of five property casualty companies that were part of the 29-member Standard & Poor's Composite 1500 Property & Casualty Insurance Index (The Chubb Corporation, Ohio Casualty Corporation, Safeco Corporation, Selective Insurance Group, and The Travelers Companies Inc.)

Of the property casualty companies included in that Index, the five we monitored were selected because they market their products through the same types of independent insurance agencies that represent our company and they provide both commercial lines and personal lines of insurance as we do. For 2006, the most recent year for which compensation data is available, cash compensation (base salary, variable cash bonus and non-equity incentive compensation) and total compensation paid to our named executive officers was 44 percent and 34 percent, respectively, of our peer group's average for these measures. This comparison reinforces our belief that compensation paid to our named executive officers, as a group, is in the low range compared with our peer group. The same peer group is defined in and serves as the basis for one of three performance objectives in the Cincinnati Financial Corporation 2006 Incentive Compensation Plan (Incentive Compensation Plan). See Annual Incentive Bonus, Page 22, for more information about this plan.

In 2008, the committee amended the peer group, replacing Ohio Casualty Corporation with The Hartford Financial Services Group, Inc. because Ohio Casualty merged with Liberty Mutual in 2007 and no longer reports data as a publicly traded company. The committee determined that Hartford, a highly rated company that offers property and casualty insurance products primarily through independent agents, would be an appropriate addition to the peer group.

The committee does not employ compensation consultants for recommendations concerning executive compensation. Historically, our chief executive officer has provided the committee with peer group performance and compensation data collected by the chief financial officer from publicly available proxy statements and Form 10-K filings. In 2006 and 2007, similar data was obtained from Equilar, an independent subscription service that automates the collection of such information.

***Tax consequences.*** A goal of the committee is to maximize the company's tax deductibility of compensation. The Cincinnati Financial Corporation 2006 Incentive Compensation and 2006 Stock Compensation Plans give the committee the ability to provide named executive officers with tax-efficient incentive bonuses and stock-based compensation based upon the achievement of pre-established performance targets for compensation paid to those individuals. The committee reserves the right to award non-performance-based compensation to individual named executive officers above \$1 million that is not tax deductible. Historically, the committee has not been concerned when non-performance-based compensation has exceeded the \$1 million limit imposed by Section 162(m) of the Internal Revenue Code because the compensation we pay to our named executive officers as a group is at the low end of the range of compensation paid by our peers. In 2007, a portion of the non-performance based compensation paid to Messrs. Schiff and Benoski was not tax deductible due to the value of de minimis perquisites and benefits and adjustments in base salary and annual cash bonuses in line with adjustments to salaries and annual cash bonuses for all of our exempt associates as a group. For information about how 2007 salaries and annual cash bonuses were determined, see Components of Compensation, Base Salary and Annual Bonus, Page 22.

***Employment agreements, change in control provisions and post-retirement benefits.*** We do not have employment agreements with any of our named executive officers, who are all at-will employees. Our long-standing corporate perspective has been that employment contracts do not provide the company with any significant advantage. We believe our corporate culture, current compensation practices and levels of stock ownership by our executive officers have resulted in stability in our executive officer group, which includes the named executive officers who average 31 years with the company.

We only use a change in control provision in our 2006 Stock Compensation Plan, and that provision applies to all associates receiving awards under the plan, not just to executive officers. The change in control provision of that plan contains a "double trigger," which requires both a change in control event, as defined in the plan, and termination of the associate's employment due to the change in control within a specified time period. The double trigger ensures that we will become obligated to accelerate vesting of prior awards only if the executive is actually or constructively discharged because of the change in control event. The committee granted awards under the 2006 Stock Compensation Plan beginning in 2007.

We occasionally provide post-retirement benefits to long-tenured, executive officer-level associates who continue to provide services to the company after retirement from their executive positions. These post-retirement benefits are intended to compensate the associate for ongoing services associated with maintaining continuity of relationships and providing guidance to their successors and other associates. We have no formal agreements with any of the current named executive officers for specific post-retirement benefits upon their future retirement. However, when a named executive officer retires, we may choose to provide him or her with modest cash compensation, office space, access to administrative support, and continuation of certain health and welfare benefits generally available to all associates in exchange for services rendered. In 2007, two associates who had previously retired from executive positions received one or more of the described benefits at a total cost to the company of approximately \$60,000.

## **Compensation Practices Summary**

***Role of executive officers.*** The chief executive officer makes recommendations to the committee for base salary and annual bonus compensation for the other named executive officers. The chief executive officer provides the committee with performance assessments of the named executive officers to support those recommendations. He also provides the committee with data sheets that summarize compensation history and the latest available peer group data. The chief executive officer's recommendations for salary and annual bonus are based on his assessment, with input from the chief operating officer, of each individual's performance and current compensation compared with changes in responsibilities during the year, if any, and his assessment of what the company can afford to pay based on the performance of the company in the current year.

Similarly, the chief executive officer recommends awards of stock-based compensation for the other named executive officers. All such compensation had been in the form of stock options until 2007 when awards of restricted stock units were first granted. At all levels of the organization, the number of stock options and restricted stock units recommended generally is determined by title or level of responsibility. The number of stock options awarded at all levels of the organization, including the named executive officers was unchanged for several years until 2007 when awards of restricted stock units were introduced.

See Long-Term Stock-Based Compensation, Page 24, for details about how levels of stock-based compensation are determined. On occasion, the chief executive officer has recommended deviations above an established grant level for individuals, following special circumstances such as temporary assumption of another executive officer's duties or outstanding performance on special projects.

**Role of committee.** The committee makes the final determination of base salary, annual bonus and awards of incentive and stock-based compensation for the chief executive officer and, taking into account the recommendations of the chief executive officer, for each of the other named executive officers.

The committee meets in the fourth quarter of each calendar year to set salaries for the upcoming year and award cash bonuses for the current year. It meets in the first quarter of the calendar year to grant stock-based and incentive compensation awards and consider the payment of any incentive compensation earned upon satisfaction of performance goals established in the prior year's incentive compensation award grant.

In addition to the recommendations of the chief executive officer, the committee also considers its own experience with and information received from and about the named executive officers, including:

- Interactions of the board and its committees with the named executive officers. The chief executive officer, chief operating officer and chief financial officer regularly attend board meetings and provide commentary on activities of the company as well as their areas of responsibility. Other named executive officers in operating positions make presentations to the board and otherwise have contact with board members from time to time.
- The chief executive officer's and the chief operating officer's ongoing reports to the board and its committees about individual named executive officer activities and performance.
- Business results and business unit results, including reports:
  - filed with the SEC,
  - provided regularly to the board by management, including non-public financial, insurance and investment performance summaries, and
  - provided to the board on an as-needed or as-requested basis.

The committee also informally considers specific financial and operational metrics for business segments, business units and other subsets of the organization. Management monitors and provides these reports to the directors, including committee members, on an ongoing basis. This information is shared with the board and the committee through a variety of channels. For example:

- Comparisons of growth, profitability and selected other trends to averages for the entire property casualty industry or major subsets, such as the average for the commercial or personal lines insurance segments presented in our public filings. For statutory data, we most frequently rely on data prepared by A.M. Best Co., a worldwide insurance-rating and information agency. For data based on GAAP, in 2006 we began to use information provided by SNL Financial LLC, a sector-specific information and research firm in the financial information marketplace.
- Reports from and board discussions with our strategic planning officer regarding progress toward achievement of our corporate strategic goals.
- Reports and board discussions with executive officers responsible for broad areas of our insurance, investment and operational activities, including our named executive officers, about management's assessment of business unit and overall industry trends based on a variety of data monitored by the business units.

The committee does not have a pre-defined framework that determines which of these factors may be more or less important, and the emphasis placed on specific factors may vary among the named executive officers. Ultimately, it is the committee's judgment of these factors, in its normal deliberations and in executive session, along with competitive data and discussions with and recommendations from the chief executive officer, that form the basis for determining the compensation for the named executive officers.

Following discussions with the chief executive officer, the committee acts to approve or adjust the current cash compensation recommendations for the other named executive officers. In executive session, the committee also establishes the current cash compensation for the chief executive officer. The committee

chair is responsible for communicating to the chief executive officer the committee's evaluation of the performance of the chief executive officer and the level of compensation approved for the chief executive officer.

Similarly, the committee considers the chief executive officer's recommendations for stock-based awards for the other named executive officers. Stock-based awards to the chief executive officer are determined in executive session. See Stock-Based Award Grant Practices, Page 25, for details about how stock-based grants are made.

Throughout the year, the committee may act on the chief executive officer's recommendations concerning material changes to compensation or changes to the mix of certain components of compensation for named executive officers in conjunction with promotions or changes in responsibilities.

## **Components of Compensation**

The primary components of compensation are discussed below.

### **Base Salary and Annual Bonus**

Non-incentive cash compensation for named executive officers consists of base salary and variable pay in the form of an annual cash bonus. Base salary reflects the requirements and responsibilities of each officer's particular role, the performance of his current responsibilities and market conditions. Advancement in abilities, experience and responsibilities are recognized with increases in base salary. The change in the annual cash bonus reflects base salary, length of service, individual performance and company performance. While awards of cash bonuses are discretionary, we normally do not consider compensation in this form "at risk." Practically, we evaluate each named executive officer's base salary and annual cash bonus as a unit. In 2007, non-incentive cash compensation, as reported, as a percentage of total compensation reported in the Summary Compensation Table ranged from 57 percent to 69 percent for individual named executive officers.

Amounts shown as salary in the Summary Compensation Table on Page 28 reflect adjustments to base salary made the preceding November as well as any adjustments during the calendar year. In November 2006, the committee increased the sum of base salary and cash bonus by 13 percent to \$4,599,136 for the group of named executive officers. Within the group, Mr. Schiff declined increases in salary or bonus for 2006, while increases to annualized cash compensation for Mr. Benoski and Mr. Stecher of 40 percent and 32 percent respectively, substantially exceeded the average for the group due to mid-year compensation adjustments for promotions and increased responsibilities.

In November of 2007 the committee increased non-incentive cash compensation by 4 percent to \$4,800,520 for the group named executive officers. Each named executive officer's salary and bonus was increased by 4 percent and 5 percent respectively, coinciding with increases in the company-wide salary and bonus pool. The committee established these pools based on the company's financial results at nine months and projected trends through the end of the year. Satisfactory efforts to maintain profitability, increase new business and sustain policyholder retention, tempered by the level of revenue and an expected reduction in book value at year-end, led the committee to establish the pool for annual salary increases at the same rate as in 2006 and to lower the rate of increase for the pool of cash bonuses to 5 percent in 2007 from 7 percent in 2006.

### **Annual Incentive Bonus**

Under the Incentive Compensation Plan, the five most highly compensated named executive officers also are eligible to receive an award of up to \$1 million in cash annually based on achievement of specific performance-based criteria. The compensation committee primarily intends to use the Incentive Compensation Plan to maximize the tax deductibility of cash compensation it wishes to award under the plan when performance goals are achieved, if any.

Under the plan, an incentive cash bonus may be awarded when the company achieves any two of the following performance goals:

- A specified percentage increase in gross direct written premiums for the calendar year over those for the prior year (*Gross direct written premium is insurance business written by our independent insurance agencies. It does not include premiums from assumed or ceded business, such as reinsurance or state pools, or premiums from annuities. The committee selected this measure of premium growth because it demonstrates the success of our agency-centered business activities*);

- A specified percentage increase in operating income for the calendar year over that of the prior year. (In calculating the company's operating income, the effects of capital gains and losses and accounting changes shall not be considered nor will losses attributable to catastrophes that are assigned catastrophe numbers by the American Insurance Services Offices (now known as the Property Claim Services (PCS) unit of ISO).) *(Because accounting changes and losses attributable to catastrophes are excluded from operating income as defined by the Incentive Compensation Plan, this measure differs from the "net income before realized investment gains and losses" or "operating income" measures that are provided in our quarterly earnings releases and other shareholder communications and reconciled to GAAP under Regulation G);*
- Exceeding the median annual percentage increase in earnings per share for the company's peer group for the calendar year, including the effects of catastrophic losses, but excluding the effects of capital gains and losses and accounting changes. *(Earnings per share as defined by the Incentive Compensation Plan is equivalent to the "net income before realized investment gains and losses before one-time items" or "operating income before one-time" measures that are provided in quarterly earnings releases and other shareholder communications and reconciled to GAAP under Regulation G).*

These performance goals consider our key growth metric, property casualty insurance premiums, as well as overall performance excluding items that can distort results in the short-term, such as catastrophe losses, accounting changes and realized investment gains and losses. Exclusion of certain items like realized investment gains also eliminates the opportunity for named executive officers to make investment decisions they otherwise would not make merely to achieve payouts of awards, while exclusion of items like catastrophe losses from certain performance goal definitions focuses the named executive officers' attention on appropriate events that are within their ability to control.

The target for payout is achievement of two of the three goals. The committee believes that the cyclical nature of the insurance business could result in years in which one of the goals may not be met, but the company may nevertheless produce superior performance for which it wishes to award incentive bonuses based on its achievement of the other two goals. For instance, when direct written premium growth is difficult to achieve, the company may write very profitable business and otherwise operate its business to satisfy or exceed targets for operating income and earnings per share compared with the peer group. The two out of three target permits the annual incentive compensation award to be flexible and incent the named executive officer throughout all phases of the market cycle.

The level of award determined for incentive compensation grants under the plan are the maximum amounts the committee may choose to pay if the two of three target is achieved. Payout of awards is a two-step process. No payment may be authorized if the target is not achieved. If the target is achieved, the committee considers whether it will exercise its discretion to reduce the amount of or eliminate the award for any named executive officer in light of factors the committee deems appropriate, including each officer's individual performance. Incentive bonuses under the plan are paid as soon as practical after payment of the award is authorized by the committee.

Shareholders approved the Incentive Compensation Plan in May 2006. Because it was not available to the committee for grants in the first 90 days of 2006, the period of time in which performance targets must be established to qualify as performance-based compensation under Section 162(m), all cash bonuses paid to the named executive officers in 2006 were discretionary. See Base Salary and Annual Bonus, Page 22 for information about cash bonuses.

The committee made grants under the Incentive Compensation Plan in March 2007. In setting the variable performance targets and amounts for the grants, the committee considered the current salary and projected levels of variable compensation for 2007 of each eligible named executive officer, industry trends and internal company projections for premium growth and profitability. The targets established by the committee, applicable to all 2007 grants under the Incentive Compensation Plan, were a 1.5 percent increase in 2007 gross direct written premiums and a 1.5 percent increase in 2007 operating income. The committee also established award amounts of \$400,000 for Mr. Schiff, \$300,000 for Mr. Benoski, \$150,000 for Mr. Stecher and \$100,000 for Mr. Scherer. Mr. Joseph is eligible to participate in the plan beginning in 2008. The company's performance versus these targets will be evaluated by the committee in March 2008 after performance data is available.

## Long-Term Stock-Based Compensation

Our longstanding policy is to strongly encourage stock ownership by all associates, not only the named executive officers. The named executive officers are eligible to receive stock-based awards under shareholder-approved stock-based compensation plans. In granting options and other stock-based compensation to the named executive officers, the committee intends not only to reward them for past service to the company, but also to develop executives who are shareholders with a stake in the future prosperity of the company and an incentive to remain employed by the company.

Until 2007, incentive stock-based awards were entirely in the form of stock options that vested in equal amounts over the three years following the date of grant, supporting the company's long-term focus. Beginning in 2007, awards of performance-based restricted stock units that cliff vest after three years if performance targets are achieved were added to the mix of equity awards granted to the named executive officers. Stock-based awards granted to all associates in any year generally total less than 1.0 percent of total shares outstanding. In 2007, stock-based awards granted to the five named executive officers represented approximately 11.5 percent of all equity grants awarded that year and less than 0.1 percent of total shares outstanding.

Performance-based restricted stock units tie vesting of a portion of stock-based compensation to performance goals and also support the committee's efforts to maximize the company's federal income tax deduction for executive compensation. Stock options tie the compensation realized from such awards, if any, to changes in the stock price experienced by shareholders generally.

The three-year performance period for awards of restricted stock units reinforces the company's long-term focus and matches the period after which stock option awards are fully vested and exercisable. If the restricted stock units vest, the award is paid in shares of common stock, one share for each restricted stock unit. For performance-based restricted stock units, the committee expects to set targets that it considers are achievable, but that will require a slight stretch, based on market conditions and the current insurance industry environment at the time of grant.

Historically, the committee made decisions about stock-based compensation based on the number of shares underlying the award, which remained constant year over year, rather than the cost of the awards in any given year. See the discussion under Stock-Based Award Grant Practices beginning on Page 25. With the introduction of the restricted stock units in 2007, the number of stock options awarded was reduced to accommodate awards of restricted stock units. In determining the allocation of 2007 stock-based compensation between stock options and restricted stock units, the committee emphasized the following objectives:

- Keep the overall cost to the company of stock-based compensation in line with the cost of stock-based compensation comprised only of stock options,
- Continue to emphasize stock options that require associates to make a personal investment upon exercise, and
- Award a sufficient number of restricted stock units that upon vesting will strengthen the associate's ability to collateralize loans to exercise stock options and ability to satisfy applicable stock ownership guidelines.

Based on recommendations made by the chief executive officer and the chief financial officer, at its meeting on January 31, 2007, the committee granted stock-based awards under the 2006 Stock Compensation Plan and awarded both stock options and restricted stock units to the named executive officers as follows: 25,000 nonqualified stock options and 6,100 performance-based restricted stock units each to Messrs. Schiff and Benoski and 7,500 nonqualified stock options and 1,850 performance-based restricted stock units each to Messrs. Stecher, Joseph, and Scherer. See 2007 Grant of Plan-Based Awards, Page 29, for details about these awards.

Under the terms of the 2007 awards of performance-based restricted stock units, the named executive officers' restricted stock units will vest on March 1, 2010, if the sum of "operating income" for the three calendar years ending December 31, 2007, through December 31, 2009, equals or exceeds 315 percent of operating income for 2006. For these performance-based restricted stock unit awards, the definition of operating income is the same as the definition of operating income in the Incentive Compensation Plan discussed above.



At its meeting on February 18, 2008, the committee granted stock-based awards in the form of both stock options and restricted stock units to the named executive officers as follows: 30,000 nonqualified stock options and 9,480 performance-based restricted stock units each to Messrs. Schiff and Benoski and 8,000 nonqualified stock options and 2,880 performance-based restricted stock units each to Messrs. Stecher, Joseph and Scherer.

Performance-based restricted stock units granted in 2008 will vest according to the amount of operating income achieved over the three calendar years ending December 31, 2010. Threshold, target and maximum aggregate three-year performance targets of 285 percent, 300 percent and 315 percent of 2007 operating income were established for threshold, target and maximum awards of 6,320, 7,900 and 9,480 shares respectively for Messrs. Schiff and Benoski and 1,920, 2,400 and 2,880 shares respectively for Messrs. Stecher, Joseph and Scherer. As with the 2007 performance-based restricted stock unit awards, the committee used the definition for operating income set forth in the Incentive Compensation Plan, but amended that definition to include an annual cap for the contribution of favorable development on prior period reserves of 2.5 percent to address the extraordinarily high favorable development in 2007.

Additionally, named executive officers are eligible to receive stock bonuses under the company's broad-based Holiday Stock Bonus Plan, which annually awards one share of common stock to each full-time associate for each year of service up to a maximum of 10 shares. This plan, in effect since 1976, encourages stock ownership at all levels of the company.

### ***Stock-Based Award Grant Practices***

In awarding stock options and other forms of stock-based compensation, the committee follows certain general precepts:

- **Timing** – The committee has historically granted stock-based compensation awards at approximately the same date every year, at its first regularly scheduled meeting of the calendar year. This meeting is scheduled to occur within the two weeks preceding the first meeting of the board of directors that occurs in the last week of January or first week of February each year. Although this schedule has led to stock-based grants during the period immediately before the announcement of year-end results, the committee believes the consistency of this practice eliminates concerns over the timing.

In 2008, the committee continued this process for all associates receiving grants of stock options and service-vesting restricted stock units. Not receiving grants of stock-based compensation at that first meeting in 2008 were 23 officers, including the five named executive officers, who make up the group the committee has determined should receive performance-based stock-based compensation.

The committee asked for additional information to consider in the development of alternative performance goals and targets. At its February 18, 2008 meeting the committee granted stock options and performance-based restricted stock units to these 23 officers. For 2009, the committee intends to resume its practice of granting all stock-based compensation awards at its first meeting of the year.

- **Option Exercise Price** – All stock-based compensation is granted at fair market value on the date of grant. For stock-based awards in 2007 and 2008 under the 2006 Stock Compensation Plan and Stock Option Plan VII, fair market value is defined as the average of the high and low sale price on NASDAQ on the grant date. For stock options granted before 2007 under Stock Option Plan VII and earlier plans, the fair market value is defined as the closing price on NASDAQ on the business day prior to the grant date. The grant date is the date of the committee meeting at which the grant is made. Fair market value for awards under the 2003 Director Stock Plan and the Holiday Stock Bonus Plan is the average of the high and low sale price on NASDAQ on the grant date. The committee does not delegate timing or pricing of stock-based awards to management.
- **Procedure** – The chief executive officer recommends tiers of stock-based awards for each level of responsibility throughout the organization, based on job titles. Managers participate in the stock-based award process by confirming which full-time associates at each level they believe should be eligible for a stock-based award. The number of shares may be adjusted for individuals or groups after committee deliberations and ultimately is determined and granted by the committee. The committee does not delegate authority to management to grant stock options or other stock-based awards.

## Retirement Benefits

The named executive officers participate in two retirement plans.

**Tax-qualified defined benefit plan.** The Cincinnati Financial Corporation Retirement Plan (Retirement Plan) is a tax-qualified defined benefit plan available to all full time associates. To become a member of the Retirement Plan, associates must be at least 21 years of age and have worked at least 1,000 hours in a 12-month period. Members of the Retirement Plan earn one year of service for each calendar year in which they work at least 1,000 hours. Members also earn service for time that they are paid, or entitled to be paid, but do not actually work. These times include vacation, holidays, illness and military duty and some periods of disability. The maximum amount of service that may be earned under the Retirement Plan is 40 years. Vesting is 100 percent after five years of service and there are no deductions for Social Security or other offset amounts.

The Retirement Plan defines earnings for any given plan year as the base rate of salary in effect on the last day of the plan year, subject to the maximum recognizable compensation under Section 401(a)(17) of the Internal Revenue Code. Bonuses, stock-based awards and other forms of compensation do not contribute to earnings under the Retirement Plan.

Normal retirement age as defined in the Retirement Plan is age 65. The normal retirement pension is computed as a single life annuity. The annual benefit payment is the greater of the following two calculated amounts:

The first calculated amount is the sum of:

1. 0.45 percent per year of the member's highest five-year average earnings for the first 15 years of service, plus
2. 1.35 percent per year of the member's highest five-year average earnings up to \$35,000 for the first 15 years of service, plus the sum of:
  - a. 0.6 percent per year of the member's highest five-year average earnings for years 16 through 40 plus
  - b. 1.8 percent of the member's highest five-year average earnings up to \$35,000 for years 16 through 40.

The second calculated amount is the sum of:

1. 0.9 percent per year of the member's highest five-year average earnings for the first 15 years of service plus
2. 1.2 percent per year of the member's highest five-year average earnings for years 16 through 40.

The normal form of benefit payment under the terms of the Retirement Plan is a single life annuity for unmarried members and a joint and 50 percent survivor annuity for married members. The plan permits members to elect to receive payment of benefits in the following forms:

- Single life only
- Single life only with 60-month or 120-month guarantee
- Joint and 50 percent contingent annuitant
- Joint and 66.67 percent contingent annuitant
- Joint and 100 percent contingent annuitant
- Lump sum

Alternative forms of benefit payment are offered to provide plan members some flexibility in retirement income and estate planning by giving them the option of electing monthly benefits with or without a survivor's benefit. Generally, the single life annuity alternative provides the largest monthly benefit, but does not provide a survivor's benefit. All other payment forms are the actuarial equivalent of the single life annuity alternative. Alternatives other than the single life annuity provide slightly lower monthly benefits to the plan member, depending on such factors as presence of survivor's benefit, the member's age and any contingent annuitant's age. The lump sum payment permits plan members to roll the present value of their benefit into an Individual Retirement Account and defer income taxes until the member withdraws funds from that account.

**Supplemental Retirement Plan.** The second retirement plan in which the named executive officers participate is The Cincinnati Financial Corporation Supplemental Retirement Plan (SERP). The SERP is unfunded and subject to forfeiture in the event of bankruptcy.

The SERP is a non-tax-qualified plan maintained by the company to pay eligible associates the difference between the amount payable under the tax-qualified plan and the amount they would have received without the tax-qualified plan's limit due to Section 401(a)(17) and Section 415 of the Internal Revenue Code. Accordingly, the SERP definitions for service, normal retirement and annual earnings are the same as those for the Retirement Plan except the SERP's definition of annual earnings is not limited and there is no limit on number of years of service.

The SERP is integrated with Social Security. The integration level is equal to the average of the integration levels for the period of the member's employment, using wages paid, with a maximum of \$6,000 for years beginning before 1976 and wages subject to Social Security tax for all years after 1976.

The pension benefit under the SERP is payable only in the form of a single lump sum. The normal retirement pension benefit for current members of the SERP is the sum of 0.75 percent of the member's highest five-year average annual earnings below the integration level plus 1.25 percent of the member's highest five-year average annual earnings in excess of the integration level, multiplied by the number of years of service, minus the pension benefit payable from the Retirement Plan.

All of the named executive officers were members of the SERP on or before January 1, 2006. For members added to the SERP on or after December 1, 2006, the normal retirement benefit under the SERP will be equal to the excess of the member's monthly benefit under the Retirement Plan as of the member's retirement date, without regard to the limit on earnings under Section 401(a)(17) of the Internal Revenue Code and without regard to any limit on benefits under Section 415 of the Internal Revenue Code over the member's monthly benefit payable under the Retirement Plan as of the member's retirement date.

Both retirement plans permit early retirement between age 60 and age 65, provided the member has at least five years of service. Benefits for early retirement are calculated by adjusting for life expectancy and reducing the benefit payable at age 65 by 0.5 percent per month for each month prior to age 65 that the member elects to begin receiving pension benefits. For example, if a member elects to retire at age 60, he would receive 70 percent (60 months X 0.5 percent = 30 percent reduction) of the life-expectancy adjusted benefit payable at age 65.

Actuarial work related to both the Retirement Plan and SERP is performed by Towers Perrin, which provides human resource strategy, design and management; actuarial and management consulting to the financial services industry; and reinsurance intermediary services. The committee engaged Towers Perrin to provide actuarial and consultative services related to the design of the company's retirement and employee benefit plans. Towers Perrin also brokers our property casualty and certain working reinsurance treaties, and we have used Towers Perrin for various projects, including access to catastrophe loss modeling.

Members of the SERP are added to the plan by the committee, acting upon the recommendation of the chief executive officer. Messrs. Stecher, Scherer, and Joseph were added to the SERP effective January 1, 2006, because the benefits they could receive under the Retirement Plan were limited by the application of Section 401(a) and Section 415 of the Internal Revenue Code.

**Defined contribution plans.** The company also makes available a 401(k) savings plan to all associates and the Cincinnati Financial Corporation Top Hat Savings Plan, a deferred compensation plan for highly compensated associates. The company makes no cash contributions to the 401(k) or top-hat plans. The purpose of the plans is to assist in attracting and retaining associates by providing them a tax-attractive means to save a portion of their earnings to supplement retirement benefits provided by one or both defined benefit plans. See the narrative discussion following the 2007 Nonqualified Deferred Compensation Plan, beginning on Page 33, for more information about the Top Hat Savings Plan.

### **Perquisites and Other Personal Benefits**

Perquisites and other personal benefits are intended to support our corporate objectives or the performance of an individual's responsibilities. The perquisites and personal benefits offered to the named executive officers, and generally to all of the company's officers, consist of personal umbrella liability insurance coverage, life insurance, executive tax services, use of a company car, safe driver award, executive health exams, club dues and spouse travel to and meals associated with certain business functions. Management is

responsible for administering these programs. From time to time, the committee reviews these programs and may recommend changes or additions. The committee reviews the types and level of perquisites offered but does not control directly the actual amounts of named executive officer compensation paid pursuant to these programs.

The committee believes that the level of perquisites and personal benefits we offer our officers is de minimis (totaling no more than \$14,263 for any named executive officer in 2007). Because the level of perquisites is low and each perquisite has business value, the committee does not consider them when monitoring total compensation levels.

### Summary Compensation Table

Name and Principal Position	Year	Salary (\$)	Bonus (\$)	Stock Awards (\$ (1))	Option Awards (\$ (2))	Non-Equity Incentive Plan Compensation (\$)	Change in Pension Value and Non-qualified Deferred Compensation Earnings (\$ (3))	All Other Compensation (\$)	Total Compensation (\$)
John J. Schiff, Jr. Chief Executive Officer Cincinnati Financial Corporation	2007	\$ 777,308	\$ 447,037	\$ 74,266	\$ 554,382	-	\$ 262,699	\$ 5,219	\$ 2,120,911
	2006	775,000	425,750	452	666,042	-	340,695	6,070	2,214,009
James E. Benoski Chief Insurance Officer, President and Chief Operating Officer Cincinnati Financial Corporation	2007	658,882	479,154	248,674	269,872	-	320,303	9,568	1,986,453
	2006	500,709	456,337	452	1,373,420	-	147,682	7,873	2,486,473
Kenneth W. Stecher Chief Financial Officer and Executive Vice President Cincinnati Financial Corporation	2007	553,963	352,119	75,692	80,988	-	352,143	9,908	1,424,813
	2006	445,842	335,351	452	430,095	-	914,825	9,649	2,136,214
Thomas A. Joseph Senior Vice President The Cincinnati Insurance Company	2007	364,459	274,991	22,770	175,085	-	139,437	12,111 (4)	988,853
	2006	323,105	261,896	452	208,542	-	459,641	12,742	1,266,378
Jacob F. Scherer, Jr. Senior Vice President The Cincinnati Insurance Company	2007	411,090	380,632	22,770	175,085	-	139,082	14,263 (5)	1,142,922
	2006	367,843	362,507	452	208,542	-	415,387	14,565	1,369,296

- (1) Amounts shown in this column reflect amounts expensed during the year for stock awards under the Holiday Stock Bonus Plan and restricted stock units under the 2006 Stock Compensation Plan. Awards under the Holiday Stock Bonus Plan are valued at full market value, determined by the average of the high and low sales price on NASDAQ on the date of grant, multiplied by the number of shares. The per share fair market values were \$40.39 and \$45.24 for the grant dates of November 21, 2007, and November 22, 2006, respectively. There were no awards of restricted stock units in 2006. Assumptions used in the valuation of restricted stock units are disclosed in our 2007 Annual Report on Form 10-K, Part II, Item 8, Note 8, Page 96. There were no forfeitures of stock or restricted stock unit awards in 2007 or 2006.
- (2) Assumptions used in the valuation of option awards are disclosed in our 2007 Annual Report on Form 10-K, Part II, Item 8, Note 8, Page 96. There were no forfeitures of option awards in 2007 or 2006.
- (3) Nonqualified deferred compensation earnings are not above-market or preferential. Amounts shown reflect annual increases for the Retirement Plan and SERP as follows: \$60,659 and \$202,040 respectively for Mr. Schiff; \$154,893 and \$165,410 respectively for Mr. Benoski; \$83,447 and \$268,696 respectively for Mr. Stecher; \$75,045 and \$64,392 respectively for Mr. Joseph; and \$63,856 and \$75,226 respectively for Mr. Scherer.
- (4) Includes \$4,623 for expenses associated with spouse travel to business events; \$2,118 for premiums paid for a personal umbrella liability insurance policy; \$3,281 for executive tax services; premium paid for a life insurance policy; use of a company car; executive health examination; and a safe driver award.
- (5) Includes \$3,210 for expenses associated with spouse travel to business events; \$2,939 for club dues; \$4,568 for personal use of a company car; premiums paid for personal umbrella liability and life insurance policies; executive tax services and a safe driver award.

## 2007 Grant of Plan-Based Awards <sup>(1)</sup>

Name	Grant Date	Estimated Possible Payouts Under Non-Equity Incentive Plan Awards	Estimated Possible Payouts Under Equity Incentive Plan Awards	All Other Stock Awards: Number of Share of Stock or Units (#) (2)	All Other Option Awards: Number of Securities Underlying Options (#)	Exercise or Base Price of Option Awards (\$/Sh) (3)	Grant date fair value of stock and option awards
		Target (\$)	Target (#)				
John J. Schiff, Jr.	1/31/2007*				25,000	\$ 44.79	\$ 269,195
	1/31/2007**		6,100				273,219 (4)
	3/23/2007***	\$ 400,000					
	11/21/2007****			10			404
James E. Benoski	1/31/2007*				25,000	44.79	269,195
	1/31/2007**		6,100				273,219 (4)
	3/23/2007***	300,000					
	11/21/2007****			10			404
Kenneth W. Stecher	1/31/2007*				7,500	44.79	80,759
	1/31/2007**		1,850				82,862 (4)
	3/23/2007***	150,000					
	11/21/2007****			10			404
Thomas A. Joseph	1/31/2007*				7,500	44.79	80,759
	1/31/2007**		1,850				82,862 (4)
	11/21/2007****			10			404
Jacob F. Scherer, Jr.	1/31/2007*				7,500	44.79	80,759
	1/31/2007**		1,850				82,862 (4)
	3/23/2007***	100,000					
	11/21/2007****			10			404

- \* Cincinnati Financial Corporation Stock Option Plan No. VII
- \*\* Cincinnati Financial Corporation 2006 Stock Compensation Plan
- \*\*\* Cincinnati Financial Corporation 2006 Incentive Compensation Plan
- \*\*\*\* Holiday Stock Bonus Plan

- (1) No material modifications or repricing occurred with respect to any outstanding option or other stock-based award in 2007.
- (2) The grant date fair value for shares awarded under the Holiday Stock Bonus Plan is 100 percent of the average of the high and low sales price on NASDAQ on the date of grant, which was \$40.39 on November 21, 2007.
- (3) The option exercise price is 100 percent of the average of the high and low sales price on NASDAQ on the date of grant, which was \$44.79 on January 31, 2007
- (4) The grant date fair value of the performance-based restricted stock unit is 100 percent of the average of the high and low as reported on NASDAQ on the date of grant, which was \$44.79 on January 31, 2007, unadjusted for the present value of future dividends that holders of restricted stock units do not receive during the vesting period.

Total 2007 compensation for each named executive officer was below the respective 2006 total. The contribution of stock-based awards was lower in 2007 because of the difference in the cost and composition of stock-based awards made in those years. In addition, total compensation in 2006 included attributions of compensation from expensing of all outstanding stock options for Messrs. Benoski and Stecher and attributions of compensation for all accrued benefits under the SERP for Messrs. Stecher, Joseph and Scherer.

Total compensation disclosed in the Summary Compensation Table does not reflect compensation actually received by the named executive officer nor decisions made by the compensation committee for any individual named executive officer for any given year. For example, amounts shown for stock awards and option awards reflect the amount expensed by the company in that year, not an amount received by the named executive officer. Similarly, amounts shown for changes in pension value reflect changes in the actuarial present value of benefits under retirement to be distributed in the future, not any amounts received by the named executive officer.

Amounts shown in the Summary Compensation Table for salary, bonus and total compensation include amounts the named executive officer chose not to receive currently, but to save for retirement under the Top Hat Savings Plan. See 2007 Nonqualified Deferred Compensation Plan, Page 33.

Because annual adjustments to base salary are effective the first pay period in December, amounts reflected in the Salary column do not exactly match the base salaries set by the committee for the following year. In November 2006, the committee set 2007 base salaries of \$775,000 for Mr. Schiff; \$656,681 for Mr. Benoski; \$552,264 for Mr. Stecher; \$363,341 for Mr. Joseph; and \$409,829 for Mr. Scherer. In November of 2005, the committee set 2006 base salaries of \$775,000 for Mr. Schiff; \$429,363 for Mr. Benoski; \$407,807 for Mr. Stecher; \$319,752 for Mr. Joseph; and \$364,344 for Mr. Scherer. In May 2006, the committee increased the base salaries of Messrs. Benoski and Stecher to \$529,363 and \$457,807 respectively. See Compensation Practices Summary, Page 20 for information regarding these salary adjustments.

Mr. Schiff declined increases in his salary or cash bonus in November 2006. See Base Salary and Annual Bonus, Page 22.

The terms of all of the stock-based awards granted in 2007 and prior years provide for immediate vesting upon retirement at normal retirement age or retirement with 35 years of service. Because Messrs. Benoski and Stecher satisfy one or both of these age and service conditions, Statement of Financial Accounting Standards (SFAS) No. 123(R) requires us to expense the full amount of these awards in the year of grant. Accordingly, amounts shown in the Stock Awards and Option Awards columns of the Summary Compensation Table for 2007 for Messrs. Benoski and Stecher reflect the full SFAS 123(R) value of awards granted in 2007. Amounts shown in those columns for 2006 reflect attribution of SFAS 123(R) compensation from unvested portions of stock-based awards granted in years prior to 2006 as well as the full SFAS 123(R) value of awards granted in that year. For all other named executive officers, amounts shown in these columns reflect the ratable portion of current and past grants of stock-based compensation award expensed during the year.

Amounts shown in the “Change in Pension Value and Nonqualified Deferred Compensation Earnings” column of the Summary Compensation Table represent the annual incremental changes in the present values of benefits under the company’s defined benefit and SERP plans. See Retirement Benefits, Page 26. Amounts shown in 2006 for Messrs. Stecher, Joseph and Scherer include the total present value of benefits then payable under the SERP because they were first added to the plan effective January 1, 2006.

## Outstanding Equity Awards at 2007 Year-End

Name	Option Awards (1)				Stock Awards (3)	
	Number of Securities Underlying Unexercised Options (#) Exercisable (2)	Number of Securities Underlying Unexercised Options (#) Unexercisable (2)	Option Exercise Price (\$)	Option Expiration Date	Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights That Have Not Vested (#)	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested (\$)
John J. Schiff, Jr.	115,763		\$41.14	1/5/2008	6,100	\$ 241,194
	11,025		30.72	8/24/2008		
	115,763		30.60	1/27/2009		
	25,125		26.95	1/25/2010		
	55,125		32.81	1/31/2011		
	55,125		34.96	1/28/2012		
	55,125		32.45	2/1/2013		
	55,125		38.80	1/19/2014		
	42,000	21,000	41.62	1/25/2015		
	16,667	33,333	45.26	2/2/2016		
	25,000	44.79	1/31/2017			
James E. Benoski	47,960		26.95	1/25/2010	6,100	241,194
	55,125		32.81	1/31/2011		
	55,125		34.96	1/28/2012		
	55,125		32.45	2/1/2013		
	55,125		38.80	1/19/2014		
	42,000	21,000	41.62	1/25/2015		
	16,667	33,333	45.26	2/2/2016		
	25,000	44.79	1/31/2017			
Kenneth W. Stecher	4,199		38.87	2/7/2008	1,850	73,149
	1,808		30.72	8/24/2008		
	5,513		30.60	1/27/2009		
	16,538		26.95	1/25/2010		
	16,538		32.81	1/31/2011		
	16,538		34.96	1/28/2012		
	16,538		32.45	2/1/2013		
	16,538		38.80	1/19/2014		
	14,000	7,000	41.62	1/25/2015		
	5,000	10,000	45.26	2/2/2016		
	7,500	44.79	1/31/2017			
Thomas A. Joseph	3,308		38.87	2/7/2008	1,850	73,149
	3,308		30.72	8/24/2008		
	5,513		30.60	1/27/2009		
	16,538		26.95	1/25/2010		
	16,538		32.81	1/31/2011		
	16,538		34.96	1/28/2012		
	16,538		32.45	2/1/2013		
	16,538		38.80	1/19/2014		
	14,000	7,000	41.62	1/25/2015		
	5,000	10,000	45.26	2/2/2016		
	7,500	44.79	1/31/2017			
Jacob F. Scherer, Jr.	16,538		38.87	2/7/2008	1,850	73,149
	11,025		30.72	8/24/2008		
	16,538		30.60	1/27/2009		
	16,538		26.95	1/25/2010		
	16,538		32.81	1/31/2011		
	16,538		34.96	1/28/2012		
	16,538		32.45	2/1/2013		
	16,538		38.80	1/19/2014		
	14,000	7,000	41.62	1/25/2015		
	5,000	10,000	45.26	2/2/2016		
	7,500	44.79	1/31/2017			

- (1) Option shares awarded and exercise price have been adjusted to reflect stock splits and stock dividends where applicable
- (2) One-third of each option award vests and becomes exercisable on the first, second, and third anniversaries of the grant provided the associate is continuously employed with the company or its subsidiaries. The vesting date of each option award is listed in the table below by expiration date:

Grant Date	Vesting Dates			Expiration Date
1/5/1998	1/5/1999	1/5/2000	1/5/2001	1/5/2008
2/7/1998	2/7/1999	2/7/2000	2/7/2001	2/7/2008
8/24/1998	8/24/1999	8/24/2000	8/24/2001	8/24/2008
1/27/1999	1/27/2000	1/27/2001	1/27/2002	1/27/2009
1/25/2000	1/25/2001	1/25/2002	1/25/2003	1/25/2010
1/31/2001	1/31/2002	1/31/2003	1/31/2004	1/31/2011
1/28/2002	1/28/2003	1/28/2004	1/28/2005	1/28/2012
2/1/2003	2/1/2004	2/1/2005	2/1/2006	2/1/2013
1/19/2004	1/19/2005	1/19/2006	1/19/2007	1/19/2014
1/25/2005	1/25/2006	1/25/2007	1/25/2008	1/25/2015
2/2/2006	2/2/2007	2/2/2008	2/2/2009	2/2/2016
1/31/2007	1/31/2008	1/31/2009	1/31/2010	1/31/2017

- (3) The restricted stock unit awards granted in 2007 will vest on March 1, 2010, if performance targets are achieved, or upon retirement at age 65 or with 35 years of continuous service.

### 2007 Option Exercises and Stock Vested

Name	Option Awards		Stock Awards (1)	
	Number of Shares Acquired on Exercise (#)	Value Realized on Exercise (\$)	Number of Shares Acquired on Vesting (#)	Value Realized on Vesting (\$)
John J. Schiff, Jr.	-	\$ -	-	-
James E. Benoski	6,274	35,596	-	-
Kenneth W. Stecher	6,204	73,089	-	-
Thomas A. Joseph	-	-	-	-
Jacob F. Scherer, Jr.	16,538	364,798	-	-

- (1) Prior to 2007 the company made no stock-based awards other than stock options and the Holiday Stock Bonus Plan.

### 2007 Pension Benefits

Name	Plan Name	Number of Years Credited Service (#)	Present Value of Accumulated Benefit (\$) (1) (2)
John J. Schiff, Jr.	Qualified Pension Plan	22	\$ 1,304,764
	Supplemental Retirement Plan	22	1,207,649
James E. Benoski	Qualified Pension Plan	36	1,052,278
	Supplemental Retirement Plan	36	1,077,157
Kenneth W. Stecher	Qualified Pension Plan	40	1,199,392
	Supplemental Retirement Plan	40	1,084,824
Thomas A. Joseph	Qualified Pension Plan	31	901,612
	Supplemental Retirement Plan	31	443,270
Jacob F. Scherer, Jr.	Qualified Pension Plan	24	670,005
	Supplemental Retirement Plan	24	423,511

- (1) Amounts shown were calculated as of December 31, 2007, using the Pension Benefit Guaranty Corporation Immediate Interest Rate published on December 15, 2006, which was 2.75 percent, and the 1982 Group Annuity Mortality Table for males, set back one year.
- (2) Amounts shown for Messrs. Schiff and Benoski reflect action by the Retirement Committee effective January 1, 2000, to transfer the accrued benefit amount of each SERP member to the Retirement Plan as an additional special benefit that will be paid from the tax qualified Retirement Plan. Any additional benefit amounts accrued from the SERP after January 1, 2000, will be paid from the SERP.

See Retirement Benefits, Page 26, for details about plans providing retirement benefits to the named executive officers.

As of December 31, 2007, Messrs. Schiff and Stecher are eligible to elect early retirement under the Retirement Plan and the SERP. Mr. Benoski is older than the normal retirement age.

Messrs. Joseph, Scherer, and Stecher became members of the SERP effective January 1, 2006.



## 2007 Nonqualified Deferred Compensation Plan <sup>(1) (2)</sup>

Name	Executive contributions in 2007	Aggregate earnings in 2007	Aggregate balance at 2007 Year End
	(\$) (3)	(\$)	(\$) (4)
John J. Schiff, Jr.	\$ -	\$ (51,768)	\$ 476,107
James E. Benoski	-	-	-
Kenneth W. Stecher	-	2,372	29,718
Thomas A. Joseph	10,917	2,472	67,556
Jacob F. Scherer, Jr.	42,000	14,664	494,922

- (1) The company does not make contributions to the Top Hat Savings Plan.
- (2) No withdrawals or distributions occurred in 2007.
- (3) The named executive officer's contributions shown in this column are also reported in the Summary Compensation Table in the salary or bonus columns, and included in the amounts shown for total compensation.
- (4) Of the amounts shown in this column, \$4,458, \$9,963, \$42,000 for Messrs. Stecher, Joseph and Scherer, respectively, were reported in the Summary Compensation Table for 2006.

Compensation payable to the named executive officers may be deferred pursuant to the Top Hat Savings Plan. Under the Top Hat Savings Plan, highly compensated individuals, including the named executive officers, may elect to defer up to 25 percent of salary and up to 100 percent of any annual cash bonus, provided that the total amount of salary and bonus deferred does not exceed the maximum amount permitted by the Internal Revenue Code, which was \$45,000 in 2007. Deferral elections are made before the plan year for which compensation is to be deferred and are effective for the entire year and may not be modified or terminated for that year. Compensation deferred by the named executive officer is credited to the individual's deferred compensation account maintained by the company.

We do not contribute to or match contributions to this plan. Participants are prohibited from borrowing or pledging amounts credited to their accounts. Fifth Third Bank is the third-party administrator of the Top Hat Savings Plan. Under the plan, individuals choose one or more of specified investment alternatives, including an alternative for Cincinnati Financial Corporation common stock. Earnings credited to the named executive officer's account are calculated based on the performance of the applicable investment choice(s) selected by the named executive officer. We do not guarantee any level of return on contributions to the Top Hat Savings Plan.

Distributions from the Top Hat Savings Plan are made as soon as administratively feasible after retirement, other termination of employment or death, or pursuant to a qualified domestic relations order. Distributions to the named executive officers due to retirement or other termination of employment are not permitted until 180 days after employment terminates. Other than distributions pursuant to qualified domestic relations orders, distributions are made in the form of either a single lump sum payment or monthly installments of not less than 12 months or more than 120 months, depending upon the participant's prior election. To the extent that a participant chooses to have earnings credited based on the Cincinnati Financial Corporation common stock election, the participant may choose to receive any benefit payments in the form of stock. All other distributions are made in cash.

### ***Potential Payments upon Termination or Change of Control***

As of December 31, 2007, the only benefit a named executive officer could receive upon any termination of employment, except for retirement, is the balance of a Top Hat Savings Plan account disclosed in the "Aggregated Balance at 2007 Year End" column of the 2007 Nonqualified Deferred Compensation Plan table above. In the case of retirement, named executive officers who are at least 65 years of age additionally could receive vested retirement benefits and accelerated vesting of outstanding stock-based awards, while for retirement at age 60 without 35 years of service a named executive officer could receive a vested early retirement benefit, but no acceleration of outstanding stock-based awards. Named executive officers who retire before reaching 60 years of age but who have achieved 35 years of continuous service or who retire due to total and permanent disability could receive accelerated vesting of outstanding stock-based awards. The following table reflects the values of retirement benefits and the acceleration of vesting of stock-based awards assuming retirement on December 31, 2007.

## Potential Payments upon Termination

Name	Retirement Plan	SERP	Accelerated Vesting of Stock-Based Awards
John J. Schiff, Jr.	\$1,287,717 (1)	\$1,191,871 (1)	\$1,178,804 (2)
James E. Benoski	1,052,278	1,077,157	1,178,804
Kenneth W. Stecher	1,046,543 (1)	946,577 (1)	347,590
Thomas A. Joseph	-	-	347,590 (2)
J.F. Scherer	-	-	347,590 (2)

(1) Reflects early retirement benefit calculation.

(2) Could receive accelerated vesting only for retirement due to permanent total disability

## 2007 Director Compensation <sup>(1)</sup>

Name	Fees Earned or Paid in Cash (\$)	Stock Awards (\$)(2)	All Other Compensation (\$)(3)	Total (\$)
William F. Bahl	\$ 91,500	\$ 60,003	\$ 7,667	\$ 159,170
Gregory T. Bier	87,000	60,003	6,908	153,911
Michael Brown	6,000	6,020	1,337	13,357
Dirk J. Debbink	33,000	33,031	6,939	72,970
Kenneth C. Lichtendahl	49,500	49,527	7,709	106,736
W. Rodney McMullen	84,000	60,003	2,742	146,745
Gretchen W. Price	46,500	46,517	1,330	94,347
Thomas R. Schiff	82,500	60,003	1,584	144,087
John M. Shepherd	9,000	9,030	1,759	19,789
Douglas S. Skidmore	39,000	39,012	4,614	82,626
John F. Steele, Jr.	37,500	37,526	6,245	81,271
Larry R. Webb	55,500	55,508	11,611 (4)	122,619
E. Anthony Woods	88,500	60,003	8,893	157,396

(1) Directors listed in this table are non-employee directors. Messrs. Schiff and Benoski are directors who are also executive officers of the company. Their compensation as named executive officers is shown in the Summary Compensation Table and supporting tables beginning on Page 28. They receive no additional compensation for their service as directors.

(2) Stock awards are valued at full fair market value determined by the average of the high and low sales price on NASDAQ on January 30, 2008, the date of grant, times the number of shares awarded. The per share fair market value on January 30, 2008, was \$39.09. The number of shares awarded to each director is reflected below:

Name	Shares Granted (#)	Name	Shares Granted (#)
William F. Bahl	1,535	Thomas R. Schiff	1,535
Gregory T. Bier	1,535	John M. Shepherd	231
Michael Brown	154	Douglas S. Skidmore	998
Dirk J. Debbink	845	John F. Steele, Jr.	960
Kenneth C. Lichtendahl	1,267	Larry R. Webb	1,420
W. Rodney McMullen	1,535	E. Anthony Woods	1,535
Gretchen W. Price	1,190		

There were no forfeitures of awards under this plan in 2007.

(3) For all directors, except Mr. Webb, amounts reflect perquisites in an aggregate amount of less than \$10,000 of one or more of the types described in Perquisites and Other Personal Benefits, Page 27.

(4) Includes \$9,342 for expenses associated with spouse travel to business events and premiums for personal umbrella liability and life insurance policies.

Non-employee directors are paid cash fees of:

- \$4,500 for attendance at each parent or subsidiary company's board meeting and
- \$1,500 for attendance at each meeting of a parent or subsidiary board committee.

Fees for all meetings in any one day are not to exceed \$6,000. Beginning in 2008, non-employee directors also will receive an annual retainer of \$50,000. Non-employee directors are reimbursed for travel expenses incurred in attending meetings. Non-employee directors also receive compensation in the form of common stock under the Cincinnati Financial Corporation 2003 Non-Employee Directors' Stock Plan (2003 Stock Plan). The purpose of this shareholder-approved plan is to attract and retain the services of experienced and knowledgeable non-employee directors and to strengthen the alignment of interests between the non-employee directors and shareholders. Shares received under the plan assist directors in achieving ownership levels consistent with the recently adopted Director and Officer Stock Ownership Guidelines. Under the plan, directors receive unrestricted shares of the company's common stock with a fair market

value on the date of grant equal to the cash director's fees received by such directors during the last calendar year, up to a maximum of \$60,000 of cash fees. Awards to individual directors may slightly exceed \$60,000 in value as the plan provides for rounding up to whole shares.

The committee grants awards for each director's prior year's board service under the 2003 Stock Plan at its first scheduled meeting each calendar year. See Stock-Based Award Grant Practices, Page 25. Amounts shown in the Stock Awards column reflect grants awarded under the 2003 Stock Plan at the committee's meeting on January 30, 2008, based on cash fees earned for board service in 2007.

The company also provides non-employee directors with life insurance, personal umbrella liability insurance and spouse travel and meals to certain business events. See Perquisites and Other Personal Benefits, Page 27, for details about these benefits. Amounts contained in the All Other Compensation column reflect the aggregate cost of these individual benefits.

The company does not provide non-employee directors with retirement benefits, benefits under health and welfare plans or compensation in any form not described above, nor does it have any agreement with any director to make charitable donations in the director's name.

## **Conclusion**

### **Shareholder Proposals for Next Year**

Any qualified shareholder who wishes to present a proposal for action at the 2009 Annual Meeting of Shareholders must submit the proposal to Cincinnati Financial Corporation, P.O. Box 145496, Cincinnati, Ohio 45250-5496, on or before November 26, 2008, to be included in our proxy statement and proxy for the 2009 annual meeting. Any such proposal must conform to the rules and regulations of the SEC and otherwise be in accordance with other federal laws as well as the laws of the State of Ohio. If the date of the 2009 annual meeting is not within 30 days of May 3, 2009, the deadline will be a reasonable time before we begin to print and mail the proxy material for the 2009 Annual Meeting of Shareholders. In addition, the proxy solicited by the board for the 2009 annual meeting will confer discretionary authority on the persons named in such proxy to vote on any shareholder proposal presented at that meeting if we receive notice of such proposal later than February 7, 2009, without the matter having been discussed in such proxy.

### **Cost of Solicitation**

Proxies may be solicited by our directors, officers or other employees, either in person or by mail, telephone or email. The cost of soliciting proxies will be borne by the company. We have contracted with Broadridge Financial Solutions Inc. to provide Internet and telephone voting service for our direct shareholders of record. We ask banks, brokerage houses, other custodians, nominees and fiduciaries to forward copies of the proxy material to beneficial owners of shares or to request authority for the execution of proxies; and we have agreed to reimburse reasonable out-of-pocket expenses incurred.

### **Other Business**

Management does not know of any other matter or business that may be brought before the meeting; but if any other matter or business properly comes before the meeting, it is intended that a vote will be cast pursuant to the accompanying proxy in accordance with the judgment of the person or persons voting the same.

/S/ Kenneth W. Stecher

Kenneth W. Stecher

Secretary

March 20, 2008

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## Contact Information

Communications directed to the company's secretary, Kenneth W. Stecher, chief financial officer and executive vice president, are shared with the appropriate individual(s). Or, you may directly access services:

**Investors:** Investor Relations responds to investor inquiries about Cincinnati Financial Corporation and its performance.

Heather J. Wietzel – Vice President, Investor Relations

513-870-2768 or [investor\\_inquiries@cinfin.com](mailto:investor_inquiries@cinfin.com)

**Shareholders:** Shareholder Services provides stock transfer services, fulfills requests for shareholder materials and assists registered shareholders who wish to update account information or enroll in shareholder plans.

Jerry L. Litton – Assistant Vice President, Shareholder Services

513-870-2639 or [shareholder\\_inquiries@cinfin.com](mailto:shareholder_inquiries@cinfin.com)

**Media:** Corporate Communications assists media representatives seeking information or comment from Cincinnati Financial Corporation or its subsidiaries.

Joan O. Shevchik, CPCU, CLU – Senior Vice President, Corporate Communications

513-603-5323 or [media\\_inquiries@cinfin.com](mailto:media_inquiries@cinfin.com)

### Cincinnati Financial Corporation

The Cincinnati Insurance Company

The Cincinnati Casualty Company

The Cincinnati Indemnity Company

The Cincinnati Specialty Underwriters Insurance Company

The Cincinnati Life Insurance Company

CSU Producer Resources Inc.

CFC Investment Company

CinFin Capital Management Company

#### Mailing Address:

P.O. Box 145496

Cincinnati, Ohio 45250-5496

Phone: 513-870-2000

Fax: 513-870-2066

[www.cinfin.com](http://www.cinfin.com)

#### Street Address:

6200 South Gilmore Road

Fairfield, Ohio 45014-5141



Cincinnati Financial Corporation

# 2007 Annual Report

(including Annual Report  
on Form 10-K)

February 2008

In 2008, we are offering shareholders the same types of information about our company as in prior years, but on a different schedule. As each item is published, it appears on our Web site, [www.cinfin.com](http://www.cinfin.com), in an integrated annual report format. Many items will be available to you earlier than you received them in the past, because you no longer have to wait until all sections of our annual report are printed. Items available now are titled in color, and those coming soon are titled in gray.

## About the Company

Cincinnati Financial meets the needs of agencies and policyholders through our insurance group and three complementary subsidiaries:

**The Cincinnati Insurance Company** leads our A++ A.M. Best-rated standard market property casualty insurance group, which includes **The Cincinnati Casualty Company** and **The Cincinnati Indemnity Company**. This group markets a broad range of business, homeowner and auto policies through our select group of local independent insurance agencies in 34 states. These companies support each agency's ability to provide exceptional value and service to the people and businesses in its community. Our local field representatives work out of their homes, customizing products to meet policyholder needs, responding personally and promptly to claims and strengthening relationships.

Two other subsidiaries of The Cincinnati Insurance Company also market insurance products. **The Cincinnati Life Insurance Company**, rated A+ by A.M. Best, markets life insurance policies, disability income policies and annuities. **The Cincinnati Specialty Underwriters Insurance Company**, rated A by A.M. Best, began offering excess and surplus lines insurance products in 2008.

Three subsidiaries of Cincinnati Financial support our insurance operations. **CSU Producer Resources Inc.** offers insurance brokerage services to our independent agencies to support their access to Cincinnati Specialty Underwriters. **CFC Investment Company** offers commercial leasing and financing services to our agents and their clients. **CinFin Capital Management Company** provides asset management services to institutions, corporations and individuals.

## 2007 Fourth-quarter and Full-year Letter to Shareholders – mid-February 2008

This message from our chairman and our president includes recent news releases about financial results announced February 6 and actions taken by the board of directors at its February 1 meeting. *The Cincinnati Experience*, a profile of our operating philosophy, accompanies this letter.

## The Cincinnati Experience – mid-February 2008

The Cincinnati Insurance Company, Cincinnati Financial Corporation's lead subsidiary, ranks among the top 25 U.S. property casualty insurer groups based on net written premiums. In *The Cincinnati Experience*, you'll read about how our relationship-based approach creates value and loyalty, supporting premium growth.

## 2007 Annual Report on Form 10-K – late-February 2008

The *Annual Report on Form 10-K* is a detailed document published by every publicly traded company as required by the U.S. Securities and Exchange Commission. In our report, we describe your company's operations, its results and trends, along with supporting data, discussions, audited financial statements and accompanying notes.

## 2008 Shareholder Meeting Notice and Proxy Statement – mid-March 2008

This statement informs you of items requiring shareholder action at the 2008 Annual Meeting of Shareholders on May 3, 2008. It identifies board members, detailing director and executive officer compensation and board activities. Notice cards, mailed in March, tell how to easily obtain the *Proxy Statement* and vote.

## Chairman and President's Letter – late-March 2008

Accompanying the Proxy Statement are the 2007 condensed balance sheets and income statements, six years of financial data and an annual message from our chairman and our president. Their letter presents management's perspectives on your company's 2007 performance and trends that may affect performance in 2008 and beyond.

## First-quarter 2008 Letter to Shareholders – mid-May 2008

This message from our chairman and our president includes recent news releases about financial results announced April 30, results of shareholder votes at the 2008 Annual Meeting of Shareholders and actions of the board at its May meeting. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by May 12, 2008.

## Second-quarter 2008 Letter to Shareholders – mid-August 2008

This message from our chairman and our president includes our August 6 news release with financial results. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by August 11, 2008.

## Third-quarter 2008 Letter to Shareholders – mid-November 2008

This message from our chairman and our president includes our October 29 news release with financial results. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by November 10, 2008.



# Cincinnati Financial Corporation

## 2007 Annual Report on Form 10-K

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**United States Securities and Exchange Commission  
Washington, D.C. 20549**

**Form 10-K**

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

**For the fiscal year ended December 31, 2007.**

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 of incorporation)

31-0746871  
(I.R.S. Employer Identification No.)

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

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

**Securities registered pursuant to Section 12(b) of the Act:**

None

**Securities registered pursuant to Section 12(g) of the Act:**

\$2.00 par, common stock  
(Title of Class)

6.125% Senior Notes due 2034  
(Title of Class)

6.9% Senior Debentures due 2028  
(Title of Class)

6.92% Senior Debentures due 2028  
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer.

See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Exchange Act.

(Check one): Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

The aggregate market value of voting stock held by nonaffiliates of the Registrant was \$6,768,139,815 as of June 30, 2007.

As of February 15, 2008, there were 165,466,108 shares of common stock outstanding.

Document Incorporated by Reference

Portions of the definitive Proxy Statement for Cincinnati Financial Corporation's Annual Meeting of Shareholders to be held on May 3, 2008, are incorporated by reference into Parts II and III of this Form 10-K.



# Part I

## Item 1. Business

### CINCINNATI FINANCIAL CORPORATION – INTRODUCTION

We are an Ohio corporation formed in 1968. Our lead subsidiary, The Cincinnati Insurance Company, was founded in 1950 to market property casualty insurance, which is our main business. Our headquarters is in Fairfield, Ohio. At year-end 2007, we had 4,087 associates, with 2,924 headquarters associates providing support to 1,163 field associates.

Cincinnati Financial Corporation owns 100 percent of four subsidiaries: The Cincinnati Insurance Company, CSU Producer Resources Inc., CFC Investment Company and CinFin Capital Management Company. In addition, the parent company has an investment portfolio, owns the headquarters building and is responsible for corporate borrowings and shareholder dividends. The Cincinnati Insurance Company owns 100 percent of our four insurance subsidiaries.

In addition to The Cincinnati Insurance Company, our standard market property casualty insurance group includes subsidiaries The Cincinnati Casualty Company and The Cincinnati Indemnity Company. This group markets a broad range of business, homeowner and auto policies in 34 states. Other subsidiaries of The Cincinnati Insurance Company include The Cincinnati Life Insurance Company, which markets life insurance policies, disability income policies and annuities, and The Cincinnati Specialty Underwriters Insurance Company, which began offering excess and surplus lines insurance products in January 2008.

The three other subsidiaries of Cincinnati Financial are CSU Producer Resources, which offers insurance brokerage services to our independent agencies so their clients can access our excess and surplus lines insurance products; CFC Investment Company, which offers commercial leasing and financing services to our agents, their clients and other customers; and CinFin Capital Management Company, which provides asset management services to institutions, corporations and individuals.

Our filings with the Securities and Exchange Commission are available, free of charge, on our Web site, [www.cinfin.com](http://www.cinfin.com), as soon as possible after they have been filed with the SEC. These filings include our annual reports on Form 10-K, our quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934. In the following pages we reference various Web sites. These Web sites, including our own, are not incorporated by reference in this Annual Report on Form 10-K.

Periodically, we refer to estimated industry data so that we can give information about our performance versus the overall insurance industry. Unless otherwise noted, the industry data is prepared by A.M. Best Co., a leading insurance industry statistical, analytical and insurer financial strength and credit 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).

## OUR BUSINESS AND OUR STRATEGY

### INTRODUCTION

Our company was founded more than 50 years ago by independent agents to support the ability of local independent property casualty insurance agents to deliver quality financial protection to people and businesses in their communities. Today, we operate much the same way, actively marketing standard market commercial insurance policies in 34 states through a select group of independent insurance agencies. We actively market all of our personal lines insurance policies in 22 of those states and began in January 2008 to market excess and surplus lines policies in five states through the same agencies that offer our standard market property casualty insurance products. We also seek to become the life insurance carrier of choice for the agencies that market our property casualty insurance products and offer other financial services to help agents and their clients, the policyholders.

Our company distinguishes itself in three key ways:

- We cultivate relationships with the independent insurance agents who market our policies and we make our decisions at the local level
- We achieve claims excellence, covering the spectrum from our response to reported claims to our approach to establishing reserves for not-yet-paid claims
- We invest for long-term total return, using available cash flow to purchase equity securities after covering insurance liabilities by purchasing fixed-maturity securities

## **CULTIVATING RELATIONSHIPS WITH INDEPENDENT INSURANCE AGENTS**

The U.S. property casualty insurance industry is a highly competitive marketplace with over 2,000 stock and mutual companies operating independently or in groups. No single company or group dominates across all product lines and states. Standard market insurance companies (carriers) can market a broad array of products nationally or:

- choose to sell a limited product line or only one type of insurance (monoline carrier)
- target a certain segment of the market (for example, personal insurance)
- focus on one or more states or regions (regional carrier)

In addition to the widely known standard market for property casualty insurance, the excess and surplus lines market exists due to a regulatory distinction. Generally, excess and surplus lines insurance carriers provide insurance that is unavailable to businesses in the standard market due to market conditions or due to characteristics of the insured that are caused by nature, the insured's history or the nature of their business. Insurers operating in the surplus lines market are generally small, specialty insurers or specialized divisions of larger insurance organizations. Each markets through surplus lines insurance brokers.

Standard market property casualty insurers generally offer their products through one or more distribution channels:

- independent agents, who represent multiple carriers,
- captive agents, who represent one carrier exclusively, or
- direct marketing through the mail or Internet

Some carriers use more than one channel. For the most part, we compete with standard market insurance companies that market through independent insurance agents.

### **Independent Agency Distribution System**

We are committed to the independent agency distribution system, offering our broad array of insurance products through this channel. We recognize that locally based independent agencies have relationships in their communities that can lead to policyholder satisfaction, loyalty and profitable business. Our field associates provide service and accountability to the agencies, living in the communities they serve and working from offices in their homes, providing 24/7 availability to our agents.

At year-end 2007, our 1,092 agency relationships had 1,327 reporting agency locations marketing our standard market insurance products. An increasing number of agencies have multiple, separately identifiable locations, reflecting their growth and consolidation of ownership within the independent agency marketplace. Reporting agency locations describes our agents' scope of business and our presence within our 34 active states. At year-end 2006, our 1,066 agency relationships had 1,289 reporting agency locations marketing our insurance products. At year-end 2005, we had 1,024 agency relationships with 1,252 reporting agency locations. In addition to providing data on reporting agency locations, we continue to give agency relationships metrics, such as our penetration within each agency relationship.

## Property Casualty Earned Premiums by State

In our 10 highest volume states, 882 reporting agency locations wrote 69.1 percent of our 2007 total standard market property casualty earned premium volume compared with 70.0 percent in 2006.

(Dollars in millions)	Reporting agency locations	Net earned premiums	Percent of total earned	Average premium per location
<b>Year ended December 31, 2007</b>				
Ohio	218	\$ 664	21.2 %	\$ 3.0
Illinois	116	283	9.1	2.4
Indiana	101	218	7.0	2.2
Pennsylvania	77	188	6.0	2.4
North Carolina	69	154	4.9	2.2
Georgia	66	150	4.8	2.3
Michigan	95	146	4.7	1.5
Virginia	56	140	4.5	2.5
Wisconsin	47	114	3.6	2.4
Tennessee	37	103	3.3	2.8
<b>Year ended December 31, 2006</b>				
Ohio	220	\$ 695	22.0 %	\$ 3.2
Illinois	116	291	9.2	2.5
Indiana	98	225	7.1	2.3
Pennsylvania	75	190	6.0	2.5
Michigan	92	160	5.1	1.7
Georgia	62	147	4.6	2.4
North Carolina	70	144	4.5	2.1
Virginia	55	142	4.5	2.6
Wisconsin	51	119	3.8	2.3
Kentucky	38	103	3.2	2.7

In 2006, the most recent period for which data is available, Cincinnati Insurance was the No. 1 or No. 2 carrier in approximately 75 percent of the reporting agency locations that have represented us for more than five years. The independent agencies that we choose to market our products share our philosophies. They do business person to person; offer broad, value-added services; maintain sound balance sheets and manage their agencies professionally. On average, we have a 14.9 percent share of the property casualty insurance in our reporting agency locations. Our share is 20.5 percent in reporting agency locations that have represented us for more than 10 years; 9.7 percent in agencies that have represented us for five to 10 years; 4.6 percent in agencies that have represented us for one to five years; and 0.8 percent in agencies that have represented us for less than one year.

Over the next decade, industry analysts predict successful agencies will have opportunities to increase their size on average almost three-fold. Agencies are expected to continue to pursue consolidation opportunities, buying or merging with other agencies to create stronger organizations and expand service. In addition to the growing networks of agency locations owned by banks and brokers, other agencies are addressing the consolidation by forming voluntary associations. These associations, or "clusters," share back office and other functions to enhance economies, while maintaining their individual ownership structures.

Our largest single agency relationship accounted for approximately 1.2 percent of our total agency earned premiums in 2007. No aggregate of locations under a single ownership structure accounted for more than 2.5 percent of our total agency earned premiums in 2007.

### Strengthening Our Agency Relationships

We follow a number of strategies to strengthen our relationships with the independent property casualty insurance agencies that market our products.

#### Emphasis on Relationships and Local Decision-making

We continue to expand the services we provide that support agency opportunities. Accessible field representatives are the first layer of support. Headquarters associates also provide agencies with underwriting, accounting and technology assistance and training. Company executives, headquarters underwriters and special teams regularly travel to visit agencies. Agents have opportunities for direct, personal conversations with our senior management team, and headquarters associates have opportunities to refresh their knowledge of marketplace conditions and field activities.

The field marketing representatives are joined by field representatives specializing in claims, loss control, machinery and equipment, bond, premium audit, life insurance and leasing. For example, our field machinery and equipment and loss control representatives perform inspections and recommend specific actions to improve the safety of the policyholder's operations and the quality of the agent's account.

Agents tell us they agree with the need to carefully select risks and assure pricing adequacy. They appreciate the time our associates invest in creating solutions for their clients while protecting profitability, whether that

means working on an individual case or developing modified policy terms and conditions that preserve flexibility, choice and other sales advantages.

### **Risk-specific Underwriting**

We seek to be a consistent, predictable and reasonable property casualty carrier that agencies can rely on to serve their clients. Our field and headquarters underwriters make risk-specific decisions about both new business and renewals. On a case-by-case basis, we select risks we can cover on acceptable terms and at adequate prices rather than underwriting solely by geographic location or business class.

For new commercial lines business, this case-by-case underwriting and pricing is coordinated by the local field marketing representatives. Our agents and our field marketing, loss control, premium audit, bond and machinery and equipment representatives get to know the people and businesses in their communities and can make informed decisions about each risk. These field marketing representatives also are responsible for selecting new independent agencies, coordinating field teams of specialized company representatives and promoting all of the company's products within the agencies they serve. Commercial lines policy renewals are managed by headquarters underwriters who are assigned to specific agencies and consult with local field staff, as needed.

We apply our risk-specific underwriting philosophy to personal lines new and renewal business in a different process. Each agency selects personal lines business from within the geographic territory that it serves, based on the agent's knowledge of the risks in those communities or familiarity with the policyholder. New and renewal business activities are supported by headquarters associates assigned to individual agencies.

### **Competitive Insurance Products**

We are committed to offering the property casualty products and services local agents need to serve their clients – the policyholders. Our products are structured to allow flexible combinations of property and liability coverages in a single package with a single expiration date. This approach brings policyholders convenience, discounts and a reduced risk of coverage gaps or disputes. At the same time, it increases account retention and saves time and expense for the agency and our company.

Our commercial lines packages are typically offered on a three-year policy term for most insurance coverages, a key competitive advantage. Although we offer three-year policy terms, premiums for some coverages within those policies are adjustable at anniversary for the next annual period, and policies may be cancelled at any time at the discretion of the policyholder. Contract terms often provide that rates for property, general liability, inland marine and crime coverages, as well as policy terms and conditions, are fixed for the term of the policy. The general liability exposure basis may be audited annually. Commercial auto, workers' compensation, professional liability and most umbrella liability coverages within multi-year packages are rated at each of the policy's annual anniversaries for the next one-year period. The annual pricing could incorporate rate changes approved by state insurance regulatory authorities between the date the policy was written and its annual anniversary date, as well as changes in risk exposures and premium credits or debits relating to loss experience, competition and other underwriting judgment factors. We estimate that approximately 75 percent of 2007 commercial premiums were subject to annual rating or were written on a one-year policy term.

In our experience, multi-year packages are somewhat less price sensitive for the quality-conscious insurance buyers who we believe are typical clients of our independent agents. Customized insurance programs on a three-year term complement the long-term relationships these policyholders typically have with their agents and with the company. By reducing annual administrative efforts, multi-year policies lower expenses for our company and for our agents. The commitment we make to policyholders encourages long-term relationships and reduces their need to annually re-evaluate their insurance carrier or agency. We believe that the advantages of three-year policies in terms of improved policyholder convenience, increased account retention and reduced administrative costs outweigh the potential disadvantage of these policies, even in periods of rising rates.

Our personal lines policies are offered on a one-year term, except homeowner policies in three states that represent less than one percent of total personal lines premium volume. Competitive advantages of our personal lines coverages include our credit structure and customizable endorsements for both the personal auto and homeowner policies. A newly introduced personal auto policy endorsement is replacement cost coverage for newly purchased vehicles. Popular homeowner endorsements include replacement cost for contents, inflation guard, identity theft expense coverage and advocacy services, flexible water damage coverages and enhanced replacement cost coverage for older homes.

### **Technology Solutions**

We seek to employ technology solutions and business process improvements that complement our core values of local underwriting decisions, strong relationships with our independent agencies and superior claims service. In recent years, we have made significant investments in state-of-the-art information technology platforms, systems and Internet-based applications to:

- allow our agencies and our field and headquarters associates to collaborate more efficiently,

- provide our agencies the ability to access our systems and client data to process business transactions from their offices,
- automate our internal processes so our associates can spend more time serving agents and policyholders, and
- reduce duplication and make our processes more efficient to reduce company and agency costs.

Agencies access our systems and other electronic services via CinciLink®, our secure agency-only portal. CinciLink provides an array of Web-based services and content that make it easier to do business with us, such as commercial and personal lines rating and processing systems, policy loss information, sales and marketing materials, educational courses on our products and services, and electronic libraries for property and casualty coverage forms and state rating manuals.

**Commercial Lines Technology** – WinCPP® is our commercial lines premium quoting system. WinCPP is available in all of our agency locations in 32 of the 34 states in which we actively market insurance and provides quoting capabilities for nearly 100 percent of our new and renewal commercial lines business. In 2008, we plan to introduce WinCPP in our newest states – Washington and New Mexico. WinCPP provides a real-time agency interface, CinciBridge™, which allows automated movement of key underwriting data from an agent's management system to WinCPP, reducing agents' data entry and allowing seamless quoting and rating capabilities.

Many small business accounts written as Businessowners Policies (BOP) and Dentist's Package Policies (DBOP) are eligible to be issued at our agency locations through our Web-based e-CLAS® policy processing system. (A businessowners policy combines property, liability and business interruption coverages for small businesses.) e-CLAS provides full policy lifecycle transactions including: quoting, issuance, policy changes, renewal processing and policy printing at the agency location. These features make it easier and more efficient for our agencies to issue and service these policies. At year-end 2007, e-CLAS was in use in 17 states representing 85 percent of our BOP and DBOP premiums, which are included in the specialty packages commercial line of business. We continue to roll out e-CLAS to additional states for these policy types, including two new states since the beginning of 2008. e-CLAS also utilizes CinciBridge to provide real-time agency interface. Our primary long-term technology objective is to complete development of e-CLAS for all of our commercial lines of business.

To respond to agency needs, a direct bill payment option is being made available for commercial lines policyholders. Our first step is to make the direct bill option available for policies issued through e-CLAS. We rolled out this capability to selected agencies in 2007 with full agency rollout in early 2008. Similar direct billing capability for selected commercial policies not issued through e-CLAS is anticipated by the end of 2008 with the intent to offer this capability for all policies as soon as practicable.

Since 2004, we have been streamlining internal processes and achieving operational efficiencies in our headquarters commercial lines operations through deployment of iView™, a policy imaging and workflow system. This system provides online access to electronic copies of policy files, enabling our underwriters to respond to agent requests and inquiries more quickly and efficiently. iView also automates internal workflows through electronic routing of underwriting and processing work tasks. At year-end 2007, more than 74 percent of in-force non-workers' compensation commercial lines policy files were administered and stored electronically in iView.

**E&S Technology** – Cincinnati Specialty Underwriters and CSU Producer Resources employ a Web-based policy administration system to quote, bind, issue and deliver policies electronically to agents. This system also provides integration to existing document management and data management systems, allowing for straight-through processing of policies and billing.

**Personal Lines Technology** – Diamond is a real-time personal lines policy processing system, supporting all six of our personal lines of business and allowing once and done processing. Diamond incorporates features frequently requested by our agencies such as direct bill and monthly payment plans, local and headquarters policy printing options, data transfer to and from popular agency management systems and real-time integration with data from third-party sources needed to calculate final premiums such as insurance scores, MVR reports and address verification. At year-end 2007, Diamond was in use in 17 states representing approximately 97.5 percent of our personal lines premium volume. In 2008, we expect to deploy Diamond to agencies in eight additional states. Although we already market personal lines products in Maryland, Montana, New Hampshire, North Carolina and Vermont, we expect agencies in these states to respond favorably to Diamond's advantages. We also expect to deploy Diamond to agencies in Arizona, South Carolina and Utah, new markets for our personal lines products.

In 2006, we introduced PL-efiles, a policy imaging system, to our personal lines operations. Through year-end 2007, we had transitioned information on current Diamond personal lines policies to PL-efiles and continue to work on imaging older policy information. The transition replaces paper format with electronic copies of policy documents. PL-efiles complements the Diamond system by giving personal lines underwriters and support staff

online access to policy documents and data that enable them to respond to agent requests and inquiries quickly and efficiently.

**Claims Technology** – Our property and casualty claims operation has streamlined processes and achieved operational efficiencies through the use of CMS, our claims file management system. Initially deployed in late 2003, CMS allows field and headquarters claims associates to process all reported claims in a virtual claim file. We continue to refine the system to add capabilities to make our associates more effective. During 2006, we issued tablet computers to our field claims representatives. These units allow our claims representatives to view and enter information into CMS from any location, including an insured's home or agent's office, and to print claim checks using portable printers. Agency access to selected CMS information was tested in the fourth quarter of 2007, with the full rollout due to be completed in early 2008.

### **Life Insurance Offerings Strengthen Agency Relationships**

We support the independent agencies affiliated with our property casualty operations in their programs to sell life insurance. The products offered by our life insurance subsidiary round out and protect accounts and improve account persistency. At the same time, the life operation looks to increase diversification of revenue and profitability sources for both the agency and our company.

Our property casualty agencies make up the main distribution system for our life insurance products. We also develop life business from other independent life insurance agencies to provide us with penetration in geographic markets not served through our property casualty agencies. We are careful to solicit business from these other agencies in a manner that does not conflict with or compete with the marketing and sales efforts of our property casualty agencies. We emphasize up-to-date products, responsive underwriting, high quality service and competitive pricing.

### **Excess and Surplus Lines Operation Further Enhances Agency Relationships**

In January 2008, we began accepting excess and surplus lines business from Cincinnati's independent agencies in Georgia, Illinois, Indiana, Ohio and Wisconsin. These agencies have access to The Cincinnati Specialty Underwriters Insurance Company's product line through CSU Producer Resources, the new, wholly owned insurance brokerage subsidiary of parent-company Cincinnati Financial Corporation. CSU Producer Resources has binding authority on all classes of business written through CSU and maintains appropriate agent and surplus lines licenses to process non-admitted business. CSU and CSU Producer Resources plan to expand into all states except Delaware on an excess and surplus lines basis as the new companies obtain the necessary state regulatory approvals.

We structured our new E&S operations to exclusively serve the needs of the independent agencies that currently market our standard market insurance policies. When all or a portion of a current or potential client's insurance program requires E&S coverages, those agencies now can write the whole account with Cincinnati, gaining benefits not often found in the broader E&S market.

Producers can submit risks to CSU Producer Resources from a variety of classes, reflecting the mix of accounts Cincinnati agencies currently write in their non-admitted E&S markets. CSU Producer Resources currently markets and underwrites general liability coverages and plans to expand this to include commercial property, multi-peril insurance, miscellaneous professional liability and excess casualty in coming months.

Agency producers have direct access through CSU Producer Resources to our dedicated E&S underwriters, and they also can tap into their agencies' broader Cincinnati relationships to bring their policyholders services such as experienced and responsive loss control and claims handling. Our new E&S policy administration system delivers electronic copies of policies to producers within minutes of underwriting approval and policy issue. CSU Producer Resources gives extra support to our producers by remitting surplus lines taxes and stamping fees and retaining admitted market affidavits, where required.

CSU was capitalized with \$200 million from its parent company, The Cincinnati Insurance Company. That high level of funding underscores our commitment to help our independent agencies. Everything we do to increase their competitive advantages and success also helps us achieve our own long term growth and profitability goals.

### **Programs, Products and Services to Support Agency Growth**

We complement the insurance operations by providing products and services that help attract and retain high-quality independent insurance agencies. When we appoint agencies, we look for organizations with knowledgeable, professional staffs. In turn, we make an exceptionally strong commitment to assist them in keeping their knowledge up to date and educating new people they bring on board as they grow. Numerous activities at our headquarters, in regional and agency locations, and online fulfill this commitment:

- At our headquarters, we conduct agency management roundtables for agency principals, as well as our regular schedule of commercial lines, personal lines and life insurance agent schools and seminars. These generally focus on Cincinnati product and underwriting information and sales tips. In addition to schools for agents, we make available seats for agents in our structured classroom training for new underwriting

associates. Agency staff may return to their agencies after the class or stay and become fully grounded in Cincinnati philosophy by serving as an associate for a few years before returning to the agency.

- Associates travel to regional and agency locations to instruct classes and provide a variety of educational support services. Teams conduct seminars on a variety of topics, such as marketing seminars to promote cross-marketing of our products. Cincinnati associates also co-host client seminars with our agencies on a variety of topics such as risk transfer techniques. These customized programs address liability issues specific to classes of business, such as contractors or dentists.
- Agency staff can access the Learning Center through CinciLink, our secure agency-only Web site. The Learning Center offers convenient, online courses and Web conferences, including Cincinnati product information, Microsoft® Office topics and general business subjects. Our new producer and customer service representative curricula guide students through a progression of online courses and classroom instruction.

Except travel-related expenses for courses held at our headquarters, most programs are offered at no cost to our agencies. While that approach may be extraordinary in our industry today, the result is quality service for our policyholders and increased success for our independent agencies.

In addition to broad education and training support, we make financial services available through our non-insurance subsidiaries. We believe that providing these services enhances agency relationships with their clients, increasing loyalty while diversifying the agency's revenues. CFC Investment Company offers equipment and vehicle leases and loans for independent insurance agencies, their commercial clients and other businesses. It also provides commercial real estate loans to help agencies operate and expand their businesses. CinFin Capital Management markets asset management services to agencies and their clients, as well as other institutions, corporations and individuals.

### Superior Financial Strength Ratings

In addition to the ratings of our parent company senior debt, independent ratings firms award our property casualty and life operations insurer financial strength ratings based on their quantitative and qualitative analyses. These ratings assess an insurer's ability to meet its financial obligations to policyholders and do not necessarily address all of the matters that may be important to shareholders.

We believe that our strong surplus position and superior insurer financial strength ratings are clear, competitive advantages in the segment of the insurance marketplace that our agents serve. Our financial strength supports the consistent, predictable performance that our policyholders, agents, associates and shareholders have always expected and received, and it must be able to withstand significant challenges. We seek to ensure that our performance remains consistent and predictable by aligning agents' interests with those of the company, giving them outstanding service and compensation and earning their best business by enhancing their ability to serve the businesses and individuals in their communities.

As of February 29, 2008, financial strength ratings were unchanged from those reported for our standard market property casualty and life operations in our 2006 Annual Report on Form 10-K. As of December 21, 2007, our new excess and surplus lines subsidiary was awarded its first financial strength rating, an A (Excellent) with a stable outlook, from A.M. Best.

	Parent Company Senior Debt Rating	Standard Market Property Casualty Insurance Subsidiaries Financial Strength Ratings	Life Insurance Subsidiary Financial Strength Ratings	Excess and Surplus Subsidiary Financial Strength Ratings	Outlook
		Rating Tier	Rating Tier	Rating Tier	
A. M. Best Co.	aa-	A++ Superior 1 of 16	A+ Superior 2 of 16	A Excellent 3 of 16	Stable
Fitch Ratings	A+	AA Very Strong 4 of 21	AA Very Strong 4 of 21	- - -	Stable
Moody's Investors Services	A2	Aa3 Excellent 4 of 12	- - -	- - -	Stable
Standard & Poor's Ratings Services	A	AA- Very Strong 4 of 21	AA- Very Strong 4 of 21	- - -	Stable

- **A.M. Best Co.** - On May 21, 2007, A.M. Best affirmed its financial strength rating (FSR) of A++ (Superior) for our standard market property casualty group, citing its superior risk-adjusted capitalization, very strong operating performance, network of independent agents and strong overall underwriting results despite challenges to achieve profitability in the homeowner line of business. A.M. Best also affirmed its issuer credit ratings of aa+ for those property casualty insurance subsidiaries. Additionally, A.M. Best affirmed the FSR of A+ (Superior) and the issuer credit rating of aa- for The Cincinnati Life Insurance Company. The outlook for all ratings is stable.

On December 21, 2007, A.M. Best assigned an FSR of A (Excellent) and an issuer credit rating of a to The Cincinnati Specialty Underwriters Insurance Company, our new excess and surplus lines subsidiary. A.M. Best cited an excellent level of risk-adjusted capital and the explicit and implicit support garnered from being part of Cincinnati Financial, somewhat offset by execution risk associated with a new initiative and increased competitiveness in the E&S market. The outlook is stable.

- **Fitch Ratings** – On October 8, 2007, Fitch Ratings affirmed its AA (Very Strong) insurer financial strength ratings for our three standard market property casualty insurance companies and The Cincinnati Life Insurance Company. Fitch said the ratings are based on the strong financial condition of our operating subsidiaries, excellent financial flexibility and successful total return investment strategy. The ratings consider the group's investment concentration in a small number of common stocks and geographic concentration in Ohio and Midwestern states. The ratings outlook is stable.
- **Moody's Investors Service** – On September 18, 2007, Moody's Investors Service affirmed its Aa3 insurance financial strength ratings of the standard market property casualty insurance companies. Moody's said the ratings reflect our solid regional franchise emphasizing superior claims service, our relationship strategy with agents, strong commercial lines profitability, strong risk-adjusted capitalization and substantial holding company liquidity. These ratings consider our investment concentration risk, technology risk and increased competition in small and middle market commercial lines. The outlook is stable.
- **Standard & Poor's Ratings Services** - On July 23, 2007, Standard & Poor's Ratings Services affirmed the AA- (Very Strong) financial strength ratings and counterparty credit ratings for our standard market property casualty and life insurance companies. Standard & Poor's cited our very strong distribution channel and low-cost infrastructure, extremely strong capitalization, high degree of financial flexibility and improved operating performance. Offsetting these strengths are a very aggressive investment strategy, underperformance in the homeowner line of business and a relatively high catastrophe exposure. The outlook is stable.

Statutory surplus for our property casualty insurance group was \$4.307 billion at year-end 2007, with the ratio of the group's investments in common stock to statutory surplus at 84.5 percent, in line with our targeted sub-100 percent level. Statutory surplus for our property casualty insurance subsidiary was \$4.750 billion at year-end 2006, with the ratio of the group's investments in common stock to statutory surplus to statutory surplus at 96.7 percent. The life insurance company's statutory surplus was \$477 million at year-end 2007, with the ratio of life insurance company's investments in common stock to statutory adjusted capital and surplus at 70.6 percent. Life statutory surplus was \$479 million at year-end 2006, with the ratio at 88.8 percent.

Cincinnati Life's statutory adjusted risk-based surplus decreased 8.9 percent to \$506 million at year-end 2007, from \$556 million a year earlier. Statutory adjusted risk-based surplus as a percentage of liabilities, a key measure of life insurance company capital strength, was 28.5 percent at year-end 2007 compared with an estimated industry average ratio of 10.9 percent. A higher ratio indicates an insurer's stronger security for policyholders and capacity to support business growth.

At year-end 2007 and 2006, the risk-based capital (RBC) for our property casualty and life operations was exceptionally strong and well above levels that would have required regulatory action.

We continue to review the risk management and capital requirement changes that rating agencies have suggested for our industry. Additionally, we began a formal implementation of enterprise risk management in 2005. Responsibility for enterprise risk management has been assigned at the officer level, supported by a team of representatives from business areas. The team reports to our president, our chief executive officer and our board of directors, as appropriate, on detailed and summary risk assessments, risk metrics and risk plans. Our use of operational audits, strategic plans and departmental business plans, as well as our culture of open communications and our fundamental respect for our code of conduct, continue to help us manage risks on an ongoing basis.

While the potential for volatility exists due to our catastrophe exposures, investment philosophy and bias toward incremental change, the ratings agencies consistently have asserted that we have built appropriate financial strength and flexibility to manage that volatility. We remain committed to strategies that emphasize long-term stability over short-term benefits that might accrue by quick reaction to changes in market conditions.

For example, through all market and economic cycles we maintain strong insurance company statutory surplus, a solid, conservative reinsurance program, sound reserving practices and low interest rate risk, as well as low debt and strong capital at the parent-company level. Investments at the parent company give us flexibility to support our capitalization policies for the subsidiaries, improve the ability of the insurance companies to write additional premiums and maintain high insurer financial strength ratings for the protection of policyholders.

We believe that our property catastrophe reinsurance program provides adequate protection for large loss events. Our strong capital position would allow the payment of claims if an event exceeded our reinsurance program. Currently participating on our property per risk and casualty per-occurrence programs are Hannover Reinsurance Company, Munich Reinsurance America, Partner Reinsurance Company of the U.S. and Swiss Reinsurance America Corporation and its subsidiaries, all of which have A.M. Best insurer financial strength ratings of A (Excellent) or A+ (Superior). Over the past several years, we also modified policyholder deductibles



for both commercial and personal lines property coverages to reduce our exposure to a single significant catastrophic event.

Our ratio of property casualty net written premiums to statutory surplus was 0.7 at year-end 2007, 2006 and 2005. This ratio is a common measure of operating leverage used in the property casualty industry. It serves as an indicator of the company's premium growth capacity. The estimated property casualty industry net written premium to statutory surplus ratio was 0.8 at year-end 2007, 0.9 at year-end 2006 and 1.0 at year-end 2005.

### **Growing with Our Agencies**

One of our primary objectives is to increase our written premiums more rapidly than the industry. We believe our agencies are growing more rapidly than the industry, and we seek to maintain or increase our share of each agency's business as it grows.

To help us maintain or increase our share within each agency, we are further improving service through the creation of smaller marketing territories that permit our local field marketing representatives to devote more time to each agency relationship. At year-end 2007, we had 106 field marketing territories, up from 102 at the end of 2006 and 100 at the end of 2005. In 2007, we also appointed our first agencies in eastern Washington and New Mexico, our 33<sup>rd</sup> and 34<sup>th</sup> states of operation. While we continually study the regulatory and competitive environment in states where we could decide to actively market our property casualty products, we have not announced plans to enter any of those states in the near future.

Another way we seek to increase overall premiums is to expand our agency plant within our current marketing territories. Our objective is to appoint additional sales offices, or points of distribution, each year. We are targeting 65 appointments in 2008.

In measuring progress towards this goal, we include appointment of new agency relationships with Cincinnati (the primary focus of our goal). For those that we believe will produce a meaningful amount of new business premiums, we also include appointment of agencies that merge with a Cincinnati agency and new branch offices opened by existing Cincinnati agencies. We made 66, 55 and 57 new appointments in 2007, 2006 and 2005, respectively. Of these new appointments, 50, 42 and 41, respectively, were new relationships. These new appointments and other changes in agency structures led to a net increase in reporting agency locations of 38 in 2007, 37 in 2006 and 39 in 2005. We are very careful to protect the franchise for current agencies when selecting and appointing new agencies.

## **ACHIEVING CLAIMS EXCELLENCE**

Our claims philosophy reflects our belief that we will prosper as a company by responding to claims person to person, paying covered claims promptly, preventing false claims from unfairly adding to overall premiums and building financial strength to meet future obligations. We also believe that our company should have the financial strength to pay claims while also creating value for shareholders, leading to our emphasis on the establishment of adequate loss reserves.

### **Superior Claims Service**

Our 748 locally based field claims representatives work from their homes, assigned to specific agencies. They respond personally to policyholders and claimants, typically within 24 hours of receiving an agency's claim report. We believe we have a competitive advantage because of the person-to-person approach and the resulting high level of service that our field claims representatives provide. We also help our agencies provide prompt service to policyholders by giving agencies authority to immediately pay most first-party claims under standard market policies up to \$2,500.

Catastrophe response teams are comprised of volunteers from our experienced field claims staff. As hurricanes threaten, these associates travel to strategic locations near the expected impact area. This puts them in position to quickly get to the affected area, set up temporary offices and start calling on policyholders. Cincinnati takes pride in giving our field personnel the tools and authority they need to do their jobs. In times of widespread loss, our field claims representatives confidently and quickly resolve claims, often writing checks for damages on the same day they inspect the loss. CMS introduced new efficiencies that are especially evident during catastrophes. Electronic claim files allow for fast initial contact of policyholders and easy sharing of information between rotating storm teams, headquarters and local field claims representatives.

Cincinnati's claims associates work hard to control costs where appropriate. They have vendor resources that provide negotiated pricing to our insureds and claimants and that help us determine appropriate pricing for medical cost-related claims. Our field claims representatives also are educated continuously on new techniques and repair trends. They can leverage their local knowledge and experience with area body shops, which helps them negotiate the right price with any facility the policyholder chooses.

We staff a Special Investigations Unit with former law enforcement and claims professionals who are available to gather facts to uncover potential fraud. While we believe it's our job to pay what is due under each policy, we also want to prevent false claims from unfairly increasing overall premiums. Our SIU also operates a computer

forensic lab, using sophisticated software to recover data and mitigating the cost of computer-related claims for business interruption and loss of records.

## **Loss and Loss Expense Reserves**

When claims are made by or against policyholders, any amounts that our property casualty operations pay or expect to pay for covered claims are termed losses. The costs we incur in investigating, resolving and processing these claims are termed loss expenses. Our consolidated financial statements include property casualty loss and loss expense reserves that estimate the costs of not-yet-paid claims incurred through December 31 of each year. The reserves include estimates for claims that have been reported to us plus our estimates for claims that have been incurred but not yet reported called IBNR, along with our estimate for loss expenses associated with processing and settling those claims. We develop the various estimates based on individual claim evaluations and statistical projections. We reduce the loss reserves by an estimate for the amount of salvage and subrogation we expect to recover. For over 10 years, our annual review has led us to report savings from favorable development of loss reserves on prior accident years.

We encourage you to review several sections of the Management's Discussion and Analysis where we discuss our loss reserves in greater depth. In Item 7, Critical Accounting Estimates, Property Casualty Insurance Loss and Loss Expense Reserves, Page 37, we discuss our process for analyzing potential losses and establishing reserves. In Item 7, Property Casualty Insurance Reserves, Page 65, we review reserve levels, including 10-year development of our property casualty loss reserves.

## **INVESTING FOR LONG-TERM TOTAL-RETURN**

While we seek to generate an underwriting profit in our insurance operations, our investments historically have provided our primary source of net income and contributed to our financial strength, driving long-term growth in shareholders' equity and book value.

Under the direction of the investment committee of the board of directors, our investment department portfolio managers seek to balance current investment income opportunities and long-term appreciation so that current cash flows can be compounded to achieve above-average long-term total return. We invest some portion of cash flow in tax-advantaged fixed-maturity and equity securities to maximize after-tax earnings. Premium payments, generally received before claims are made, particularly for casualty business lines, create substantial cash flow for investment.

Insurance regulatory and statutory requirements established to protect policyholders from investment risk have always influenced our investment decisions on an individual insurance company basis. After covering both our intermediate and long-range insurance obligations with fixed-maturity investments, we historically used available cash flow to invest in equity securities. Investment in equity securities has played an important role in achieving our portfolio objectives and has contributed significantly to total portfolio net unrealized investment gains of \$3.339 billion (pretax) at year-end 2007. We remain committed to our long-term equity focus, which we believe is key to our company's long-term growth and stability.

## **OUR SEGMENTS**

Consolidated financial results primarily reflect the results of our four reporting segments. These segments are defined based on financial information we use to evaluate performance and to determine the allocation of assets.

- Commercial lines property casualty insurance
- Personal lines property casualty insurance
- Life insurance
- Investments

We also evaluate results for our consolidated property casualty operations, which is the total of our commercial lines and personal lines segments. Revenues generated by our consolidated property casualty operations were a lower percent of the total in 2007 and 2006 due to sales of investment assets, which are included in the investments segment results. Revenues, income before income taxes, and identifiable assets for each segment are shown in a table in Item 8, Note 17 of the Consolidated Financial Statements, Page 105. Some of that information also is discussed in this section of this report, where we explain the business operations of each segment. The financial performance of each segment is discussed in the Management's Discussion and Analysis of Financial Condition and Results of Operations, which begins on Page 32.

## **COMMERCIAL LINES PROPERTY CASUALTY INSURANCE SEGMENT**

The commercial lines property casualty insurance segment contributed \$2.411 billion of net earned premiums to total revenues and \$261 million to income before income taxes in 2007. Commercial lines net earned premiums grew 0.4 percent in 2007, 6.6 percent in 2006 and 6.0 percent in 2005.

Approximately 95 percent of our commercial lines premiums are written to provide 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 growth and profitability trends separately for our business lines. The seven commercial business lines are:

- Commercial casualty – Commercial casualty insurance provides coverage to businesses against third-party liability from accidents occurring on their premises or arising out of their operations, including liability coverage for injuries sustained from products sold as well as coverage for professional services, such as dentistry. Specialized casualty policies may include liability coverage for employment practices liability (EPLI), which protects businesses against claims by employees that their legal rights as employees of the company have been violated, and other acts or failures to act under specified circumstances as well as excess insurance and umbrella liability, including personal umbrella written as an endorsement to commercial umbrella coverages. The commercial casualty business line includes liability coverage written on both a discounted and non-discounted basis as part of commercial package policies.
- Commercial property – Commercial property insurance provides coverage for loss or damage to buildings, inventory and equipment caused by fire, wind, hail, water, theft and vandalism as well as business interruption resulting from a covered loss. Commercial property also includes crime insurance, which provides coverage for losses due to embezzlement or misappropriation of funds by an employee, and inland marine insurance, which provides coverage for a variety of mobile equipment, such as contractor's equipment, builder's risk, cargo and electronic data processing equipment. Various property coverages can be written as stand-alone policies or can be added to a package policy. The commercial property business line includes property coverage written on both a non-discounted and discounted basis as part of commercial package policies.
- Commercial auto – Commercial auto coverages protect businesses against liability to others for both bodily injury and property damage, medical payments to insureds and occupants of their vehicles, physical damage to an insured's own vehicle from collision and various other perils, and damages caused by uninsured motorists.
- Workers' compensation – Workers' compensation coverage protects employers against specified benefits payable under state or federal law for workplace injuries to employees. We write workers' compensation coverage in all of our active states except North Dakota, Ohio, Washington and West Virginia, where coverage is provided solely by the state instead of by private insurers. West Virginia plans to allow private insurers to market workers' compensation beginning in July 2008.
- Specialty packages – Specialty packages include coverages for property, liability and business interruption tailored to meet the needs of specific industry classes, such as artisan contractors, dentists, garage operators, financial institutions, metalworkers, printers, religious institutions, or smaller, main street businesses. Businessowners policies, which combine property, liability and business interruption coverages for small businesses, are included in specialty packages.
- Surety and executive risk – This business line includes:
  - Contract and commercial surety bonds, which guarantee a payment or reimbursement for financial losses resulting from dishonesty, failure to perform and other acts.
  - Fidelity bonds, which cover losses that policyholders incur as a result of fraudulent acts by specified individuals or dishonest acts by employees.
  - Director and officer liability insurance, which covers liability for alleged errors in judgment, breaches of duty and wrongful acts related to activities of for-profit or nonprofit organizations. Our director and officer liability policy can optionally include EPLI coverage.
- Machinery and equipment – Specialized machinery and equipment coverage can provide protection for loss or damage to boilers and machinery, including production and computer equipment, from sudden and accidental mechanical breakdown, steam explosion, or artificially generated electrical current.

Our emphasis is on products that agents can market to small- to mid-size businesses in their communities. Of our 1,327 reporting agency locations, six market only our surety and executive risk products and three market only our personal lines products. The remaining 1,318 locations, located in all 34 states in which we actively market, offer some or all of our standard market commercial insurance products.

In 2007, our 10 highest volume commercial lines states generated 66.7 percent of our earned premiums compared with 67.7 percent in the prior year. Earned premiums in the 10 highest volume states decreased 1.1 percent in 2007 but rose 3.5 percent in the remaining 24 states.

## Commercial Lines Earned Premiums by State

(Dollars in millions)	Reporting agency locations	Net earned premiums	Percent of total earned	Average premium per location
<b>Year ended December 31, 2007</b>				
Ohio	216	\$ 397	16.5 %	\$ 1.8
Illinois	115	234	9.7	2.0
Pennsylvania	77	170	7.0	2.2
Indiana	100	158	6.6	1.6
North Carolina	69	147	6.1	2.1
Virginia	56	119	4.9	2.1
Michigan	95	115	4.8	1.2
Wisconsin	47	94	3.9	2.0
Georgia	66	88	3.7	1.3
Tennessee	37	81	3.5	2.2
<b>Year ended December 31, 2006</b>				
Ohio	219	\$ 410	17.1 %	\$ 1.9
Illinois	116	238	9.9	2.1
Pennsylvania	75	172	7.2	2.3
Indiana	98	160	6.7	1.6
North Carolina	70	136	5.7	1.9
Michigan	92	124	5.2	1.3
Virginia	55	120	5.0	2.2
Wisconsin	51	96	4.0	1.9
Georgia	62	84	3.5	1.4
Tennessee	37	81	3.4	2.2

### Commercial Lines Insurance Marketplace

For commercial lines, our competition for the types and sizes of accounts we typically write in the standard market, predominantly consists of those companies that also distribute through independent agencies. The independent agencies that market our commercial lines products typically represent six to 12 standard market insurance carriers, including both national and regional carriers, some of which may be mutual companies.

Softening market conditions in recent years have blurred the distinctions between national and regional carriers; however, we often observe certain characteristics as we compete within each agency. National and many regional carriers are more likely to appoint a greater number of agencies and focus on specific types of products or certain size accounts. They often seek to take greatest advantage of tools that enhance their efficiency and the ease of doing business with their organization. Time-intensive services may be offered only to larger accounts. They may be less interested in the smaller accounts that require significant attention. Regional carriers are more likely to utilize an agency strategy, focusing on differentiating themselves through relationships and service. They often seek to place decision-making closer to the local market level and have begun to target larger accounts to develop or retain their position within agencies. In our experience, the level of competition varies state by state and region by region, regardless of the mix of carriers represented within a specific agency.

Overall, the softening commercial lines marketplace of the past several years continued to intensify in 2007. Over this period, anecdotal reports of very aggressive pricing have grown in frequency. Over the course of 2007, we saw more situations where underwriting discipline appeared to slip as carriers sought to capture market share. Many carriers appear to be managing the soft market conditions by working aggressively to protect their renewal portfolios.

### PERSONAL LINES PROPERTY CASUALTY INSURANCE SEGMENT

The personal lines property casualty insurance segment contributed \$714 million of net earned premiums to total revenues and \$43 million to income before income taxes in 2007. Personal lines net earned premiums declined 6.3 percent in 2007 and 5.3 percent in 2006 after rising 1.4 percent in 2005.

We prefer to write personal lines coverage on an account basis that includes both auto and homeowner coverages as well as coverages that are part of our 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 growth and profitability trends separately for three business lines:

- Personal auto – This business line includes personal auto coverages that protect against liability to others for both bodily injury and property damage, medical payments to insureds and occupants of their vehicle, physical damage to an insured's own vehicle from collision and various other perils, and damages caused by uninsured motorists. In addition, many states require policies to provide first-party personal injury protection, frequently referred to as no-fault coverage.

- Homeowners – This business line includes homeowner coverages that protect against losses to dwellings and contents from a wide variety of perils, as well as liability arising out of personal activities both on and off the covered premises. The company also offers coverage for condominium unit owners and renters.
- Other personal lines – This includes the variety of other types of insurance products we offer to individuals such as dwelling fire, inland marine, personal umbrella liability and watercraft coverages.

We market both homeowner and personal auto insurance products through 812 of our 1,327 reporting agency locations in 22 of the 34 states in which we offer standard market commercial lines insurance. We market homeowner products through 21 locations in three additional states (Maryland, North Carolina and West Virginia.) The remaining 494 locations largely are in states where we do not yet actively market these products. A smaller number are those where we have determined, in conjunction with agency management, that our personal lines products are not appropriate for their agencies at this time.

In 2007, our 10 highest volume personal lines states generated 84.9 percent of our earned premiums compared with 84.7 percent in the prior year. Earned premiums in the 10 highest volume states declined 6.5 percent in 2007 and declined 5.2 percent in the remaining states.

### Personal Lines Earned Premiums by State

(Dollars in millions)	Reporting agency locations	Net earned premiums	Percent of total earned	Average premium per location
<b>Year ended December 31, 2007</b>				
Ohio	200	\$ 266	37.3 %	\$ 1.3
Georgia	58	61	8.6	1.1
Indiana	71	59	8.3	0.8
Illinois	81	49	6.8	0.6
Alabama	33	37	5.2	1.1
Kentucky	36	37	5.2	1.0
Michigan	64	31	4.4	0.5
Florida	10	23	3.2	2.3
Virginia	22	21	3.0	1.0
Wisconsin	29	20	2.9	0.7
<b>Year ended December 31, 2006</b>				
Ohio	204	\$ 285	37.4 %	\$ 1.4
Indiana	65	65	8.5	1.0
Georgia	52	63	8.3	1.2
Illinois	76	53	6.9	0.7
Alabama	25	39	5.1	1.6
Kentucky	33	38	5.0	1.2
Michigan	64	36	4.7	0.6
Wisconsin	28	23	3.1	0.8
Florida	10	22	2.9	2.2
Virginia	19	22	2.8	1.2

### Personal Lines Insurance Marketplace

In addition to carriers that market through independent agents, our personal lines competition also includes carriers that market through captive agents and direct writers, which our agencies' clients may investigate independently. The independent agencies that market our personal lines products typically represent four to six standard personal lines carriers.

Over the past several years, we have seen increased competition in the personal lines marketplace, driven by industrywide improvement in results and favorable frequency and severity trends. The increased competition in the past several years also reflected implementation of tiered rating systems by a growing number of carriers. Carriers that have adopted these systems rely on increasingly more data to identify multiple relevant variables to segment the market, including credit-based information.

We expect that competition in the personal auto and homeowner markets will continue to increase over the next 12 to 24 months. Many personal lines carriers have reported strong operating results in the past three years and continue to have healthy capital to support business growth. We believe these carriers are focused on gaining market share through the introduction of new products and services and increased advertising expenditures.

### LIFE INSURANCE SEGMENT

The life insurance segment contributed \$125 million of net earned premiums and \$3 million in income before income taxes in 2007. Life insurance segment profitability is discussed in detail in Item 7, Life Insurance Results of Operations, Page 56. Life insurance net earned premiums grew 9.0 percent in 2007, 7.9 percent in 2006 and 5.7 percent in 2005.

The overall mission of our company is supported by The Cincinnati Life Insurance Company. Cincinnati Life helps meet the needs of our agencies, including increasing and diversifying agency revenues. We primarily focus on life products that produce revenue growth through a steady stream of premium payments.

By diversifying revenue and profitability for both the agency and our company, this strategy enhances the already strong relationship built by the combination of the property casualty and life companies.

Cincinnati Life seeks to become the life insurance carrier of choice for the independent agencies that work with our property casualty operations. We emphasize up-to-date products, responsive underwriting and high quality service as well as competitive commissions. At year-end 2007, approximately 82 percent of our 1,327 property casualty reporting agency locations offered Cincinnati Life's products to their clients. We also develop life business from 545 other independent life insurance agencies. We are careful to solicit business from these other agencies in a manner that does not conflict with or compete with the marketing and sales efforts of our property casualty agencies.

### **Life Insurance Business Lines**

Four lines of business – term insurance, universal life insurance, worksite products and whole life insurance – account for approximately 91.5 percent of the life insurance segment's revenues:

- Term insurance – policies under which a death benefit is payable only if the insured dies during a specific period of time or term. For policies without a return of premium provision, no benefit is payable if the insured survives to the end of the term. For policies with a return of premium provision, a benefit equal to the sum of all paid premiums is payable if the insured survives to the end of the term. While premiums are fixed, they must be paid as scheduled. The proposed insured is evaluated using normal underwriting standards.
- Universal life insurance – long-duration life insurance policies. Contract premiums are neither fixed nor guaranteed; however, the contract does specify a minimum interest crediting rate and a maximum cost of insurance charge and expense charge. Premiums are not fixed and may be varied by the contract owner. The cash values, available as a loan collateralized by the cash surrender value to withdrawing policyholders, are not guaranteed and depend on the amount and timing of actual premium payments and the amount of actual contract assessments. The proposed insured is evaluated using normal underwriting standards.
- Worksite products – term insurance, whole life insurance, universal life and disability insurance offered to employees through their employer. Premiums are collected by the employer using payroll deduction. Policies are issued using a simplified underwriting approach and for smaller face amounts than similar, regularly underwritten policies. Worksite insurance products provide our property casualty agency force with excellent cross-serving opportunities for both commercial and personal accounts. Agents report that offering worksite marketing to employees of their commercial accounts provides a benefit to the employees at low cost to the employer. Worksite marketing also connects agents with new customers who may not have previously benefited from receiving the services of a professional independent insurance agent.
- Whole life insurance – policies that provide life insurance for the entire lifetime of the insured; the death benefit is guaranteed never to decrease and premiums are guaranteed never to increase. While premiums are fixed, they must be paid as scheduled. These policies provide guaranteed cash values that are available as a loan collateralized by the cash surrender value to withdrawing policyholders. The proposed insured is evaluated using normal underwriting standards.

In addition, Cincinnati Life markets:

- Disability income insurance - provides monthly benefits to offset the loss of income when the insured person is unable to work due to accident or illness.
- Deferred annuities - provide regular income payments that commence after the end of a specified period or when the annuitant attains a specified age. During the deferral period, any payments made under the contract accumulate at the crediting rate declared by the company but not less than a contract-specified guaranteed minimum interest rate. A deferred annuity may be surrendered during the deferral period for a cash value equal to the accumulated payments plus interest less the surrender charge, if any.
- Immediate annuities - provide some combination of regular income and lump sum payments in exchange for a single premium. Most of the immediate annuities written by our life insurance segment are purchased by our property casualty companies to settle casualty claims.

### **Life Insurance Marketplace**

Our property casualty agencies comprise the main distribution system for our life insurance segment. While other life insurance carriers continue to expand the use of nontraditional distribution channels, such as banks or direct sales as alternatives to the agency channel, we intend to market solely through independent agencies,

with an emphasis on enhancing relationships with agencies affiliated with our property casualty insurance operations.

When marketing through our property casualty agencies we have specific competitive advantages:

- Because our property casualty operations are held in high regard, property casualty agency management is predisposed to consider selling our life products.
- Marketing efforts for both our property casualty and life insurance businesses are directed by our field marketing department, which assures consistency of communication and operations. Life field marketing representatives are available to meet face-to-face with the agency personnel and their clients as well.
- The resources of our life headquarters underwriters and other associates are available to the agents and field team to assist in the placement of business. Fewer and fewer of our competitors provide direct, personal support between the agent and the insurance carrier.

We continue to emphasize the cross-serving opportunities of our life insurance, including term and worksite products, for the property casualty agency's personal and commercial accounts. In both the property casualty and independent life agency distribution systems we enjoy the advantages of offering competitive, up-to-date products, providing close personal attention combining financial strength and stability.

- We primarily offer products addressing the needs of businesses with key person and buy-sell coverages. We offer personal and commercial clients of our agencies quality, personal life insurance coverage.
- Term insurance is our largest life insurance product line. We continue to introduce new term products with features our agents indicate are important, such as a return of premium rider and redesigning our underwriting classifications to better meet the needs of the agency's clients.

Because of our strong capital position, we can offer a competitive product portfolio including guaranteed products, giving our agents a marketing edge. Our life insurance company maintains strong insurer financial strength ratings: A.M. Best – A+ (Superior), Fitch – AA (Very Strong) and Standard & Poor's – AA- (Very Strong). Our life insurance company has not chosen to establish a Moody's rating.

Current statutory laws and regulations require life insurance companies to hold redundant reserves, particularly for preferred risk underwriting classes. These redundant reserves, in turn, depress statutory earnings and require a large commitment of capital. Redundant reserves are a significant issue, not just for our life insurance operations, but for all writers of term insurance and universal life with secondary guarantees. However, larger carriers may be able to better absorb or may be able to securitize the statutory reserve strain associated with competitively priced term insurance and universal life with secondary guarantees.

The National Association of Insurance Commissioners recognizes the problems caused by redundant reserves and is considering a principles-based reserving system rather than the current formulaic system. While still capturing all material risks, a principles-based system would allow a company to use its own experience, subject to credibility standards and appropriate margins for uncertainty. Also, under the proposed principles-based system, the insurer would fully document and disclose all its assumptions and methods to regulatory officials.

## INVESTMENTS SEGMENT

The investment segment contributed \$990 million of our total revenues in 2007, primarily from net investment income and realized investment gains and losses from investment portfolios managed for the holding company and each of the operating subsidiaries. After deducting interest credited to contract holders of the life insurance segment, the investments segment contributed \$931 million of income before income taxes, or 78.0 percent of our total income before income taxes.

The fair value (market value) of our investment portfolio was \$12.198 billion and \$13.699 billion at year-end 2007 and 2006, respectively. The cash we generate from insurance operations historically has been invested in three broad categories of investments:

- Fixed-maturity investments – Includes taxable and tax-exempt bonds and redeemable preferred stocks
- Equity investments – Includes common and nonredeemable preferred stocks
- Short-term investments – Primarily commercial paper

(In millions)	At December 31, 2007		At December 31, 2006	
	Book value	Fair value	Book value	Fair value
Taxable fixed maturities	\$ 3,265	\$ 3,284	\$ 3,357	\$ 3,389
Tax-exempt fixed maturities	2,518	2,564	2,382	2,416
Common equities	2,715	6,020	2,400	7,564
Preferred equities	260	229	221	235
Short-term investments	101	101	95	95
Total	\$ 8,859	\$ 12,198	\$ 8,455	\$ 13,699

During 2007 and 2006, sales and market value declines of equity securities more than offset purchases and market value appreciation. Sales of, or reductions in, selected large holdings are discussed below.

We consider insurance department regulations and ratings agency comments, as well as the trend in certain ratios, to determine what portion of new cash flow should be invested in equity securities at the parent and insurance subsidiary levels. Key among these ratios is the property casualty group's ratio of investments in common stocks to statutory surplus and the parent company's ratio of investment assets to total assets.

At year-end 2007, the ratio of common stock to statutory surplus was 84.5 percent compared with 96.7 percent at year-end 2006. The ratio of investment assets to total assets for the parent company was 28.4 percent at year-end 2007 compared with 31.5 percent at year-end 2006.

### Fixed-maturity and Short-term 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 continuous 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 continuously investing in the bond market, we build a broad, diversified portfolio that we believe mitigates the impact of adverse economic factors. We place a strong emphasis on purchasing current income-producing securities for the insurance companies' portfolios. Within the fixed-maturity portfolio, we invest in a blend of taxable and tax-exempt securities with an eye toward maximizing credit adjusted after-tax yields. With the exception of U.S. agency paper (government-sponsored entities), no individual issuer's securities accounted for more than 0.6 percent of the fixed-maturity portfolio at year-end 2007. Our investment portfolio contains no mortgage loans and our fixed-maturity portfolio has no mortgage-backed securities.

### Fixed-maturity and Short-term Portfolio Ratings

Our investments in U.S. agency paper and insured municipal bonds over the past several years have led to a significant rise in the percentage of A and higher rated fixed-maturity holdings, based on fair value. The majority of our non-rated securities are tax-exempt municipal bonds from smaller municipalities that chose not to pursue a credit rating. Credit ratings as of December 31 for the fixed-maturity and short-term portfolio were:

(Dollars in millions)	At December 31, 2007		At December 31, 2006	
	Fair value	Percent to total	Fair value	Percent to total
<b>Moody's Ratings</b>				
Aaa, Aa, A	\$ 4,103	69.0 %	\$ 4,039	68.5 %
Baa	1,070	17.9	1,086	18.4
Ba	280	4.7	266	4.5
B	105	1.8	122	2.1
Caa	36	0.6	28	0.5
Ca	0	0.0	0	0.0
C	0	0.0	0	0.0
Non-rated	355	6.0	359	6.0
Total	\$ 5,949	100.0 %	\$ 5,900	100.0 %
<b>Standard &amp; Poor's Ratings</b>				
AAA, AA, A	\$ 3,589	60.3 %	\$ 3,631	61.5 %
BBB	1,092	18.4	1,044	17.7
BB	258	4.3	310	5.3
B	125	2.1	131	2.2
CCC	33	0.6	10	0.2
CC	0	0.0	0	0.0
C	0	0.0	0	0.0
D	0	0.0	0	0.0
Non-rated	852	14.3	774	13.1
Total	\$ 5,949	100.0 %	\$ 5,900	100.0 %

Attributes of the fixed-maturity portfolio include:

	Years ended December 31,	
	2007	2006
Weighted average yield-to-book value	5.3 %	5.3 %
Weighted average maturity	8.0 yrs	8.7 yrs
Effective duration	4.8 yrs	5.1 yrs

We discuss the maturity of our fixed-maturity portfolio in Item 8, Note 2 of the Consolidated Financial Statements, Page 93.



## **Taxable Fixed-maturities**

Our taxable fixed-maturity portfolio (at fair value) includes:

- \$896 million in U.S. agency paper, which is rated AAA by both Moody's and Standard & Poor's.
- \$1.874 billion in investment-grade corporate bonds that have a Moody's rating at or above Baa 3 or a Standard & Poor's rating at or above BBB-.
- \$287 million in high-yield corporate bonds that have a Moody's rating below Baa 3 or a Standard & Poor's rating below BBB-.
- \$227 million in convertible bonds and redeemable preferred stocks.

Our strategy typically is to buy and hold fixed-maturity investments to maturity but we monitor credit profiles and market value movements when determining holding periods for individual securities.

Similar to the equity portfolio, the taxable fixed-maturity portfolio is most heavily concentrated in the financial sector, including banks, brokerage, finance and investment and insurance companies. The financial sector represented 27.5 percent and 27.3 percent, respectively of book value and fair value of the taxable fixed-maturity portfolio at year-end 2007, compared with 27.2 percent and 27.7 percent, at year-end 2006. Although it is our largest concentration in a single sector, we believe our percentage in the financial sector is below average for the corporate bond market as a whole. No other sector or industry accounted for more than 10 percent of the taxable fixed-maturity portfolio.

## **Tax-exempt Fixed-maturities**

We traditionally have purchased municipal bonds focusing on general obligation and essential services bonds, such as sewer, water or others. While no single municipal issuer accounted for more than 1 percent of the tax-exempt municipal bond portfolio at year-end 2007, there are higher concentrations within individual states. Holdings in Illinois, Indiana, Michigan, Ohio and Texas accounted for 62.5 percent of the municipal bond portfolio at year-end 2007.

In recent years, we have purchased insured municipal bonds because of their excellent credit-adjusted after-tax yields. At year-end 2007, bonds representing \$2.212 billion, or 87 percent, of the fair value of our municipal portfolio were insured with an average rating of AAA. Because of our emphasis on general obligation and essential services bonds, the underlying rating of our insured municipal bond portfolio is approximately A1. We believe this portion of the portfolio would experience little, if any, fair value adjustment in the event of a ratings downgrade of one or more of the major bond insurers.

## **Short-term Investments**

Our short-term investments consist primarily of commercial paper, demand notes or bonds purchased within one year of maturity. We make short-term investments primarily with funds to be used to make upcoming cash payments, such as taxes. At year-end 2007, we had \$101 million in short-term investments.

## **Equity Investments**

Our equity investment portfolio includes both common stocks and nonredeemable preferred stocks. Approximately 82.2 percent of the equity portfolio is made up of a core group of common stocks that we monitor closely to gain an in-depth understanding of their organizations and industries. The portfolio also includes a broader group of smaller positions. The average dividend yield-to-cost for our equity investments was 10.2 percent at year-end 2007 compared with 9.9 percent at year-end 2006.

## **Common Stocks**

At year-end 2007, 32.4 percent of our common stock holdings (measured by fair value) were held at the parent company level. Our common stock investments generally are securities with annual dividend yields that meet or exceed that of the overall market and have the potential for future dividend increases. Other criteria we evaluate include increasing sales and earnings, proven management and a favorable outlook. When investing in common stock, we seek to identify a limited group of companies in which we can become well versed. As a corollary, we frequently accumulate sizeable holdings over a period of time. At year-end 2007, we held more than 5 percent of two companies: Fifth Third Bancorp and Piedmont Natural Gas Company.

At year-end 2007, there were 15 holdings in which we held a fair value of at least \$100 million:

### Largest Common Stock Holdings

(Dollars in millions)		As of and for the year ended December 31, 2007				
	Actual cost	Fair value	Percent of fair value	Earned dividend income	Earned dividend to fair value	
Fifth Third Bancorp	\$ 185	\$ 1,691	28.1 %	\$ 121	7.2 %	
The Procter & Gamble Company	206	552	9.2	10	1.8	
Exxon Mobil Corporation	58	484	8.0	8	1.7	
U.S. Bancorp	270	332	5.5	16	4.8	
PNC Financial Services Group, Inc.	62	309	5.1	12	3.9	
AllianceBernstein Holding L.P.	113	295	4.9	17	5.8	
Johnson & Johnson	218	267	4.5	6	2.2	
Wyeth	62	196	3.3	5	2.6	
Wells Fargo & Company	128	194	3.2	7	3.6	
Huntington Bancshares Inc.	188	152	2.5	4	2.6	
Piedmont Natural Gas Company, Inc.	64	147	2.4	6	4.1	
Wachovia Corporation	186	140	2.3	6	4.3	
National City Corporation	132	140	2.3	16	11.4	
Chevron Corporation	56	123	2.1	3	2.4	
General Electric Co.	106	116	1.9	3	2.6	
All other common stock holdings	681	882	14.7	31	3.5	
Total	<u>\$ 2,715</u>	<u>\$ 6,020</u>	<u>100.0 %</u>	<u>\$ 271</u>		

In 2007, the most significant changes in the common stock portfolio were:

- ExxonMobil – We sold 3.8 million shares of our holding in Exxon Mobil Corporation common stock in 2007. We sold a portion of this holding to try to achieve a higher yield.
- Fifth Third – We sold 5.5 million shares of our holdings in Fifth Third common stock in 2007. We sold these shares to fund an accelerated share repurchase agreement.
- FirstMerit – We sold all of our holding in FirstMerit Corporation in 2007. We sold these shares because the investment no longer met our criteria.
- REITs – We divested the majority of our real estate investment trust holdings in 2007. We believed the fundamentals for this sector no longer supported their valuation.

We sold all of our holdings in Alltel Corporation common stock in 2006. Because of a restructuring that Alltel announced in late 2005, we determined that it no longer met our investment parameters.

Our buy-and-hold strategy, along with our emphasis on a small group of equities and long-term investment horizon has resulted in significant concentrations within the portfolio. These investments have built up substantial accumulated unrealized appreciation over a number of years. At year-end 2007, the largest industry concentrations within our common stock holdings were the financial sector at 56.7 percent of total fair value and the healthcare sector at 10.1 percent.

### Nonredeemable Preferred Stocks

We evaluate preferred stocks in a manner similar to the evaluation we make for fixed-maturity investments, seeking attractive relative yields. We generally focus on investment-grade preferred stocks issued by companies that have a strong history of paying common dividends, which provides us with another layer of protection. When possible we seek out preferred stocks that offer a dividend received deduction for income tax purposes.

Additional information regarding the composition of investments is included in Item 8, Note 2 of the Consolidated Financial Statements, Page 93.

### OTHER

We report as “Other” the operations of the parent company, CFC Investment Company, CinFin Capital Management Company (excluding investment activities) and CSU Producer Resources as well as other income of our insurance subsidiary. As of year-end 2007, CFC Investment Company had 2,590 accounts and \$92 million in receivables, compared with 2,897 accounts and \$108 million in receivables at year-end 2006. As of year-end 2007 and 2006, CinFin Capital had 64 institutional, corporate and individual clients. Assets under management were \$977 million at year-end 2007 compared with \$960 million at year-end 2006.

# REGULATION

## STATE REGULATION

The business of insurance primarily is regulated by state law. All of our insurance company subsidiaries are domiciled in the State of Ohio, except The Cincinnati Specialty Underwriters Insurance Company, which is domiciled in the State of Delaware. Each subsidiary is governed by the insurance laws and regulations in its respective state of domicile. We also are subject to state regulatory authorities of all states in which we write insurance. The state laws and regulations that have the most significant effect on our insurance operations and financial reporting are discussed below.

- Insurance Holding Company Regulation – Our insurance company subsidiaries primarily engage in the property casualty insurance business and secondarily in the life insurance business, both subject to regulation as an insurance holding company system in the subsidiaries' respective states of domicile. These regulations require that we annually furnish financial and other information about the operations of the individual companies within the holding company system. All transactions within a holding company affecting insurers must be fair and equitable. Notice to the state insurance commissioner is required prior to the consummation of transactions affecting the ownership or control of an insurer and prior to certain material transactions between an insurer and any person or entity in its holding company group. In addition, some of those transactions cannot be consummated without the commissioner's prior approval.
- Subsidiary Dividends – All of our insurance company subsidiaries are 100 percent owned by The Cincinnati Insurance Company, which is 100 percent owned by Cincinnati Financial Corporation. The dividend-paying capacity of our insurance company subsidiaries is regulated by the laws of the applicable state of domicile. Under these laws, our insurance subsidiaries must provide a 10-day advance informational notice to the insurance commissioner for the domiciliary state prior to payment of any dividend or distribution to its shareholders. In all cases, ordinary dividends may be paid only from earned surplus, which for the Ohio subsidiaries is the amount of unassigned funds set forth in an insurance subsidiary's most recent statutory financial statement. For the Delaware subsidiary, it is the amount of available and accumulated funds derived from the subsidiary's net operating profit of its business and realized capital gains.

The insurance company subsidiaries must give 30 days notice to and obtain prior approval from the state insurance commissioner before the payment of an extraordinary dividend as defined by the state's insurance code. You can find information about the dividends paid by our insurance subsidiary in 2007 in Item 8, Note 8 of the Consolidated Financial Statements, Page 96.

- Insurance Operations – All of our insurance subsidiaries are subject to licensing and supervision by departments of insurance in the states in which they do business. The nature and extent of such regulations vary, but generally have their source in statutes that delegate regulatory, supervisory and administrative powers to state insurance departments. Such regulations, supervision and administration of the insurance subsidiaries include, among others, the standards of solvency that must be met and maintained; the licensing of insurers and their agents and brokers; the nature and limitations on investments; deposits of securities for the benefit of policyholders; regulation of policy forms and premium rates; policy cancellations and non-renewals; periodic examination of the affairs of insurance companies; annual and other reports required to be filed on the financial condition of insurers or for other purposes; requirements regarding reserves for unearned premiums, losses and other matters; the nature of and limitations on dividends to policyholders and shareholders; the nature and extent of required participation in insurance guaranty funds; the involuntary assumption of hard-to-place or high-risk insurance business, primarily workers' compensation insurance; and the collection, remittance and reporting of certain taxes and fees.

Legislative and regulatory developments through 2007 added to the uncertainty that already existed for the insurance industry in Florida. In February 2007, we asked our agents that they not send us new business submissions. This request extended to all lines of insurance and other business areas until June 2007 when we resumed accepting new directors and officers, surety, machinery and equipment and life insurance coverages, subject to existing guidelines. We continue not to seek new insurance relationships for our remaining commercial lines and personal lines. This marketing stance remains in force. It did not affect directly policies already in force, which we continue to support and address at renewal, in line with our current underwriting guidelines and in compliance with Florida rules and regulations. In 2007, our written premiums from Florida agencies were 3.2 percent of total written premiums. Our Florida market share was estimated at 0.29 percent in 2006.

On August 24, 2007, the company received administrative subpoenas from the Florida Office of Insurance Regulation seeking documents and testimony concerning insurance for residential risks located in Florida and communications with reinsurers, risk modeling companies, rating agencies and insurance trade associations. We produced documents to respond to the subpoenas. The Office of Insurance Regulation cancelled and has not rescheduled the hearing noticed in the subpoena for October 18, 2007.

We continue to assess the changing insurance environment in Florida and hope to resume writing our complete portfolio of insurance products in the state as the market stabilizes.

- Insurance Guaranty Associations – Each state has insurance guaranty association laws under which the associations may assess life and property casualty insurers doing business in the state for certain obligations of insolvent insurance companies to policyholders and claimants. Typically, states assess each member insurer in an amount related to the insurer's proportionate share of business written by all member insurers in the state. Our insurance subsidiaries incurred a charge of \$2 million from guaranty associations in 2007 and received a net refund of \$500,000 in 2006. We cannot predict the amount and timing of any future assessments or refunds on our insurance subsidiaries under these laws.
- Shared Market and Joint Underwriting Plans – State insurance regulation requires insurers to participate in assigned risk plans, reinsurance facilities and joint underwriting associations, which are mechanisms that generally provide applicants with various basic insurance coverages when they are not available in voluntary markets. Such mechanisms are most commonly instituted for automobile and workers' compensation insurance, but many states also mandate participation in FAIR Plans or Windstorm Plans, which provide basic property coverages. Participation is based upon the amount of a company's voluntary market share in a particular state for the classes of insurance involved. Underwriting results related to these organizations, which tend to be adverse to our company, have been immaterial to our results of operations.
- Statutory Accounting – For public reporting, insurance companies prepare financial statements in accordance with GAAP. However, certain data also must be calculated according to statutory accounting rules as defined in the NAIC's Accounting Practices and Procedures Manual (SAP). While not a substitute for any GAAP measure of performance, statutory data frequently is used by industry analysts and other recognized reporting sources to facilitate comparisons of the performance of insurance companies.
- Insurance Reserves – State insurance laws require that property casualty and life insurance subsidiaries analyze the adequacy of reserves annually. Our appointed actuaries must submit an opinion that reserves are adequate for policy claims-paying obligations and related expenses.
- Risk-Based Capital Requirements – The NAIC's risk-based capital (RBC) requirements for property casualty and life insurers serve as an early warning tool for the NAIC and state regulators to identify companies that may be undercapitalized and may merit further regulatory action. The NAIC has a standard formula for annually assessing RBC. The formula for calculating RBC for property casualty companies takes into account asset and credit risks but places more emphasis on underwriting factors for reserving and pricing. The formula for calculating RBC for life insurance companies takes into account factors relating to insurance, business, asset and interest rate risks.

## FEDERAL REGULATION

Although the federal government and its regulatory agencies generally do not directly regulate the business of insurance, federal initiatives often have an impact. Some of the current and proposed federal measures that may significantly affect our business are discussed below.

- The Terrorism Risk Insurance Act of 2002 (TRIA) – TRIA was originally signed into law on November 26, 2002, and extended on December 22, 2005, in a revised form, and extended again on December 26, 2007. TRIA provides a temporary federal backstop for losses related to the writing of the terrorism peril in property casualty insurance policies. TRIA now is scheduled to expire December 31, 2014. Under regulations promulgated under this statute, insurers are required to offer terrorism coverage for certain lines of property casualty insurance, including property, commercial multi-peril, fire, ocean marine, inland marine, liability, aircraft, surety and workers' compensation. In the event of a terrorism event defined by TRIA, the federal government would reimburse terrorism claim payments subject to the insurer's deductible. The deductible is calculated as a percentage of subject written premiums for the preceding calendar year. Our deductible in 2007 was \$388 million (20 percent of 2006 subject premiums) and we estimate it will be \$395 million (20 percent of 2007 subject premiums) in 2008.
- Office of Foreign Asset Control (OFAC) – Subject to an Executive Order signed on September 24, 2001, intended to thwart financing of terrorists and sponsors of terrorism, financial institutions were required to block and report transactions and attempted transactions between their organization and persons and organizations named in a list published by OFAC. We currently use a combination of software, third-party vendor and manual searches to accomplish our transaction blocking and reporting activities.
- Investment Advisers Act of 1940 – Our subsidiary, CinFin Capital Management Company, operates an investment advisory business and is therefore subject to regulation by the SEC as a registered investment adviser under the Investment Advisers Act of 1940. This law imposes certain annual reporting, recordkeeping, client disclosure and compliance obligations on CinFin Capital Management.

## Item 1A. Risk Factors

Our business involves various risks and uncertainties that may affect achievement of our business objectives. Many of the risks could have ramifications across our integrated business activities. For example, while risks related to setting insurance rates and establishing and adjusting loss reserves are insurance activities, errors in these areas could have an impact on our investment activities, growth and overall results. The following discussion should be viewed as a starting point for understanding the significant risks we face. It is not a definitive summary of their potential impact or of our strategies to manage and control the risks. Please see Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, Page 32, for a discussion of those strategies.

The risks and uncertainties below are not the only ones we face. There are additional risks and uncertainties that we currently do not believe are material at this time. There also may be risks and uncertainties of which we are not aware. If any risks or uncertainties discussed here develop into actual events, they could have a material adverse effect on our business, financial condition or results of operations. In that case, the market price of our common stock could decline materially.

Readers should carefully consider this information together with the other information we have provided in this report and in other reports and materials we file periodically with the Securities and Exchange Commission as well as news releases and other information we disseminate publicly.

### **We rely exclusively on independent insurance agents to distribute our products.**

We market our products through independent, non-exclusive insurance agents. These agents are not obligated to promote our products and can and do sell our competitors' products. We must offer insurance products that meet the needs of these agencies and their clients. We need to maintain good relationships with the agencies that market our products. If we do not, these agencies may market our competitors' products instead of ours, which may lead to us having a less desirable mix of business and could affect our results of operations.

Events or conditions that could diminish our agents' desire to produce business for us and the competitive advantage that our independent agencies enjoy:

- Downgrade of the financial strength ratings of our insurance subsidiaries. We believe our strong insurer financial strength ratings, in particular the A++ (Excellent) rating from A.M. Best of our standard market property casualty insurance subsidiaries, are an important competitive advantage. Only 16 other insurance groups, or 1.6 percent of all rated insurance groups, qualify for the A++, A.M. Best's highest rating. If our property casualty ratings are downgraded, our agents might find it more difficult to market our products or might choose to emphasize the products of other carriers.
- Concerns that doing business with us is difficult, perceptions that our level of service is no longer a distinguishing characteristic in the marketplace or perceptions that our business practices are not compatible with agents' business models. This could occur if agents or policyholders believe that we are no longer providing the prompt, reliable personal service that has long been a distinguishing characteristic of our insurance operations.
- Delays in the development, implementation, performance and benefits of technology projects and enhancements or independent agent perceptions that our technology solutions are inadequate to match their needs.

A reduction in the number of independent agencies marketing our products, the failure of agencies to successfully market our products or the choice of agencies to reduce their writings of our products could affect our results of operations if we are unable to replace them with agencies that produce adequate and profitable premiums.

Further, policyholders may choose a competitor's product rather than our own because of real or perceived differences in price, terms and conditions, coverage or service. If the quality of the independent agencies with which we do business were to decline, that also might cause policyholders to purchase their insurance through different agencies or channels. Consumers, especially in the personal insurance segments, may increasingly choose to purchase insurance from distribution channels other than independent insurance agents, such as direct marketers.

Please see Item 1, Our Business and Our Strategy, Page 1, for a discussion of our relationships with independent insurance agents.

### **Our ability to properly underwrite and price risks and increased competition could adversely affect our results.**

Our financial condition, cash flow and results of operations depend on our ability to underwrite and set rates accurately for a full spectrum of risks. We establish our pricing based on assumptions regarding the level of losses that will occur within classes of business, geographic regions and other criteria.

To properly price our products, we must collect and properly analyze data, the data must be sufficient, reliable and accessible, we need to develop appropriate rating methodologies and formulae, and identify and respond to trends quickly. If rates are not accurate, we may not generate enough premiums to offset losses and expenses or we may not be competitive in the marketplace.

Setting appropriate rates could be hampered if a state or states where we write business refuses to allow rate increases that we believe are necessary to cover the risks insured. At least one state requires us to purchase reinsurance from a mandatory reinsurance fund. Such reinsurance funds can create a credit risk for insurers if not adequately funded by the state and, in some cases, the existence of a reinsurance fund could affect the prices charged for our policies. The effect of these and similar arrangements could reduce our profitability in any given period or limit our ability to grow our business.

The insurance industry is cyclical and intensely competitive. From time to time, the insurance industry goes through prolonged periods of intense competition during which it is more difficult to attract new business, retain existing business and maintain profitability. Competition in our insurance business is based on many factors, including:

- Competitiveness of premiums charged
- Relationships among carriers, agents, brokers and policyholders
- Underwriting and pricing methodologies that allow insurers to identify and flexibly price risks
- Compensation provided to agents
- Underwriting discipline
- Terms and conditions of insurance coverage
- Speed at which products are brought to market
- Technological innovation
- Ability to control expenses
- Adequacy of financial strength ratings by independent ratings agencies such as A.M. Best
- Quality of services provided to agents and policyholders
- Claims satisfaction and reputation

If our pricing is incorrect or we are unable to compete effectively because of one or more of these factors, our premium writings could decline and our results of operations and financial condition could be materially adversely affected.

Please see Item 7, Commercial Lines, Personal Lines and Life Insurance Results of Operations, Page 44, Page 51 and Page 56, for a discussion of our competitive position in the insurance marketplace.

### **Managing technology initiatives and meeting new data security requirements are significant challenges.**

While technology can streamline many business processes and ultimately reduce the cost of operations, technology initiatives present short-term cost, implementation and operational risks. In addition, we may have inaccurate expense projections, implementation schedules or expectations regarding the efficacy of the end product. These issues could escalate over time. If we are unable to find and retain employees with key technical knowledge, our ability to develop and deploy key technology solutions could be hampered.

We necessarily collect, use and hold data concerning individuals and businesses with whom we have a relationship. Threats to data security rapidly emerge and change, exposing us to rising costs and competing time constraints to secure our data in accordance with customer expectations and statutory and regulatory requirements. A breach of our security that results in unauthorized access to our data could expose us to data loss, litigation, damages, fines and penalties, significant increases in compliance costs and reputational damage.

Please see Item 1, Technology Solutions, Page 4 for a discussion of our technology initiatives.

### **The effects of changes in industry practices and regulations on our business are uncertain.**

As industry practices and legal, judicial, regulatory, social and other environmental conditions change, unexpected and unintended issues related to insurance pricing, claims, and coverage, may emerge. These issues may adversely affect our business by impeding our ability to obtain adequate rates for covered risks, extending coverage beyond our underwriting intent or by increasing the number or size of claims. In some instances, unforeseeable emerging and latent claim and coverage issues may not become apparent until some time after we have issued the insurance policies that could be affected by the changes. As a result, the full extent of liability under our insurance contracts may not be known for many years after a policy is issued.

Further, the National Association of Insurance Commissioners (NAIC) and state insurance regulators are continually reexamining existing laws and regulations governing insurance companies and insurance holding

companies, specifically focusing on modifications to statutory accounting principles, interpretations of existing laws and the development of new laws and regulations that affect a variety of financial and nonfinancial components of our business. Any proposed or future legislation or NAIC initiatives, if adopted, may be more restrictive on our ability to conduct business than current regulatory requirements or may result in higher costs. The effects of such changes could adversely affect our results of operations.

Please see Item 7, Critical Accounting Estimates, Property Casualty and Life Insurance Reserves, Page 37, for a discussion of our reserving practices.

**Our loss reserves, our largest liability, are based on estimates and could be inadequate to cover our actual losses.**

Our consolidated financial statements are prepared using GAAP. These principles require us to make estimates and assumptions that affect the amounts reported in the Consolidated Financial Statements and accompanying Notes. Actual results could differ materially from those estimates. For a discussion of the significant accounting policies we use to prepare our financial statements and the material implications of uncertainties associated with the methods, assumptions and estimates underlying our critical accounting policies, please refer to Item 8, Note 1 of the Consolidated Financial Statements, Page 87, and Item 7, Critical Accounting Estimates, Property Casualty and Life Insurance Reserves, Page 37.

Our most critical accounting estimate is loss reserves. Loss reserves are the amounts we expect to pay for covered claims and expenses we incur to settle those claims. The loss reserves we establish in our financial statements represent an estimate of amounts needed to pay and administer claims arising from insured events that have occurred, including events that have not yet been reported to us. Loss reserves are estimates and are inherently uncertain; they do not and cannot represent an exact measure of liability. Accordingly, our loss reserves for past periods could prove to be inadequate to cover our actual losses and related expenses. Any changes in these estimates are reflected in our results of operations during the period in which the changes are made. An increase in our loss reserves would decrease earnings, while a decrease in our loss reserves would increase earnings.

The estimation process for unpaid loss and loss expense obligations involves uncertainty by its very nature. We continually review the estimates and adjust the reserves as facts regarding individual claims develop, additional losses are reported and new information becomes known. Adjustments due to loss development on prior years are reflected in the calendar year in which they are identified. The process used to determine our loss reserves is discussed in Item 7, Critical Accounting Estimates, Property Casualty and Life Insurance Reserves, Page 37.

Unforeseen losses, the type and magnitude of which we cannot predict, may emerge in the future. These additional losses could arise from changes in the legal environment, catastrophic events, increases in loss severity or frequency, or other causes. Such future losses could be substantial.

**We could experience an unusually high level of losses due to catastrophic or terrorism events or risk concentrations.**

In the normal course of our business, we provide coverage against perils for which estimates of losses are highly uncertain, in particular catastrophic and terrorism events. Catastrophes can be caused by a number of events, including hurricanes, tornadoes, windstorms, earthquakes, hailstorms, explosions, severe winter weather and fires. Due to the nature of these events, we are unable to predict precisely the frequency or potential cost of catastrophe occurrences. The extent of losses from a catastrophe is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event.

We have natural catastrophe exposure to:

- Hurricanes in the gulf and southeastern coastal regions.
- Earthquakes in the New Madrid fault zone, which lies within the central Mississippi valley, extending from northeast Arkansas through southeast Missouri, western Tennessee and western Kentucky to southern Illinois, southern Indiana and parts of Ohio.
- Tornado, wind and hail in the Midwest and Southeast and, to a certain extent, the mid-Atlantic.

The occurrence of terrorist attacks in the geographic areas we serve could result in substantially higher claims under our insurance policies than we have anticipated. While we do insure terrorism risk in all areas we serve, we have identified our major terrorism exposure as general commercial risks in the metropolitan Chicago area as well as small co-op utilities, small shopping malls and small colleges throughout our 34 active states. Additionally, our life insurance subsidiary could be adversely affected in the event of a terrorist event or an epidemic such as the avian flu, particularly if the epidemic were to affect a broad range of the population beyond just the very young or the very old. Our associate health plan is self-funded and could similarly be affected.

Our results of operations would be adversely affected if the level of losses we experienced over a period of time exceeded our actuarially determined expectations. In addition, our financial condition would be adversely

affected if we were required to sell securities prior to maturity or at unfavorable prices to pay an unusually high level of loss and loss expenses. Securities pricing might be even less favorable if a number of insurance companies needed to sell securities during a short period of time because of unusually high losses from catastrophic events.

Our geographic concentration ties our performance to business, economic, environmental and regulatory conditions in certain states. We market our property casualty insurance product in 34 states, but our business is concentrated in the Midwest and Southeast. We also have exposure in states where we do not actively market insurance when clients of our independent agencies have business or properties in multiple states.

The Cincinnati Insurance Company also participates in three assumed reinsurance treaties with two reinsurers that spread the risk of very high catastrophe losses among many insurers. In 2008, we have exposure of up to \$7 million of assumed losses in three layers, from \$1.0 billion to \$1.7 billion, from a single event under an assumed reinsurance treaty for Munich Re Group. The other two assumed reinsurance treaties are immaterial.

In the event of a severe catastrophic event or terrorist attack elsewhere in the world, our insurance losses may be immaterial. However, the companies in which we invest might be severely affected, which could affect our financial condition and results of operations. Our reinsurers might experience significant losses, potentially jeopardizing their ability to pay losses we cede to them. A catastrophe or epidemic event also could affect our operations by damaging our headquarters facility or disrupting our associates' ability to perform their assigned tasks.

Please see Item 7, Critical Accounting Estimates, Property Casualty and Life Insurance Reserves, Page 37, for a discussion of our reserving practices.

**Our ability to obtain or collect on our reinsurance protection could affect our business, financial condition, results of operations and cash flows.**

We buy property casualty and life reinsurance coverage to mitigate the liquidity risk of an unexpected rise in claims severity or frequency from catastrophic events or a single large loss. The availability, amount and cost of reinsurance depend on market conditions and may vary significantly. If we are unable to obtain reinsurance on acceptable terms and in appropriate amounts, our business and financial condition may be adversely affected.

In addition, we are subject to credit risk with respect to our reinsurers. Although we purchase reinsurance to manage our risks and exposures to losses, this reinsurance does not discharge our direct obligations under the policies we write. We would remain liable to our policyholders even if we were unable to recover what we believe we are entitled to receive under our reinsurance contracts. Reinsurers might refuse or fail to pay losses that we cede to them, or they might delay payment. For long-term cases, the creditworthiness of our reinsurers may change before we can recover amounts to which we are entitled. A reinsurer's insolvency, inability or unwillingness to make payments under the terms of its reinsurance agreement with our insurance subsidiaries could have a material adverse effect on our financial position, results of operations and cash flows.

Prior to 2003, we participated in USAIG, a joint underwriting association of individual insurance companies that collectively functions as a worldwide insurance market for all types of aviation and aerospace accounts. At year-end 2007, 29.8 percent, or \$225 million, of our total reinsurance receivables were related to USAIG, primarily for September 11, 2001, events. Although more than 99 percent of the reinsurance recoverables associated with USAIG are backed by securities on deposit, if we are unable to collect these receivables, our financial position and results of operations could be materially affected. We no longer participate in new business generated by USAIG and its members.

Please see Item 7, 2008 Reinsurance Programs, Page 70, for a discussion of our reinsurance treaties.

**Our ability to realize our investment objectives could affect our financial condition, our results of operations or cash flows.**

We invest premiums received from policyholders and other available cash to generate investment income and capital appreciation, maintaining sufficient liquidity to pay covered claims and operating expenses, service our debt obligations and pay dividends. At year-end 2007, our investment portfolio was \$12.198 billion, or 73.3 percent of our total assets. In 2007, our investment segment contributed 21.8 percent of our revenue and 78.0 percent of our total income before income taxes.

Investment income is an important component of our revenues and net income. The ability to achieve our investment objectives is affected by factors that are beyond our control, such as inflation, economic growth, interest rates, world political conditions, terrorism attacks or threats, adverse events affecting other companies in our industry or the industries in which we invest and other widespread unpredictable events. These events may adversely affect the economy generally and could cause our investment income or the value of securities we own to decrease. A significant decline in our investment income could have an adverse effect on our net income, and thereby on our shareholders' equity and our policyholders' surplus. For more detailed discussion of risks associated with our investments, please refer to Item 7A, Qualitative and Quantitative Disclosures About Market Risk, Page 73.



Our investment performance also could suffer because of the types or concentrations of investments, industry groups and/or individual securities in which we choose to invest. Market value changes related to these choices could cause a material change in our financial condition or results of operations.

At year-end 2007, common stock holdings made up 49.4 percent of our investment portfolio. Of those equities, 56.7 percent were in financial sector companies. Adverse news or events affecting equities, and this sector specifically, such as unfavorable developments related to subprime lending, could affect our net income, book value and overall results.

One of our financial sector investments, Fifth Third, accounted for 28.5 percent of our shareholders' equity at year-end 2007 and dividends earned from our Fifth Third investment were 20.0 percent of our investment income in 2007. Based on 2007 results, a 10 percent change in dividends earned from our Fifth Third holding would result in a \$12 million change in pretax investment income and an \$11 million change in after-tax earnings. Every \$1.00 change in the market price of Fifth Third's common stock has approximately a 26 cent impact on our book value per share. A 20 percent change in the market price of Fifth Third's common stock from its year-end 2007 closing price would result in a \$338 million change in assets and a \$220 million change in after tax unrealized gains.

Because we currently own more than 10 percent of Fifth Third's outstanding shares and because our CEO serves as a director of Fifth Third, we are limited in the amount of Fifth Third stock we could sell in any given period and the timing of any sale. This limitation could lead us to hold a sizeable position in Fifth Third even if it would no longer meet our investment parameters. This could result in a variety of adverse consequences depending on the reason we had concluded Fifth Third no longer met our investment parameters. For example, if Fifth Third were to stop paying dividends on its common stock, we would not be able to quickly sell a part of our holdings to reinvest in other income-earning investments, which would have a material effect on our results of operations. We also insure property, liability, surety and life insurance exposures for Fifth Third and rely on the bank to service many of our corporate accounts, associate payroll and 401(k) plan.

Please see Item 1, Investments Segment, Page 15, Item 7, Investments Results of Operations, Page 57, and Liquidity and Capital Resources, Page 60, for discussion of our investment activities.

**Our status as an insurance holding company with no direct operations could affect our ability to pay dividends in the future.**

Cincinnati Financial Corporation is a holding company that transacts substantially all of its business through its subsidiaries. Our primary assets are the stock in our operating subsidiaries and our investments. Consequently, our cash flow to pay cash dividends and interest on our long-term debt depends on dividends we receive from our operating subsidiaries and income earned on investments held at the parent-company level.

Dividends paid to us by our insurance subsidiary are restricted by the insurance laws of Ohio, its domiciliary state. These laws establish minimum solvency and liquidity thresholds and limits. Currently, the maximum dividend that may be paid without prior regulatory approval is limited to the greater of 10 percent of statutory surplus or 100 percent of statutory net income for the prior calendar year, up to the amount of statutory unassigned surplus as of the end of the prior calendar year. Dividends exceeding these limitations may be paid only with prior approval of the Ohio Department of Insurance. Consequently, at times, we might not be able to receive dividends from our insurance subsidiary or we might not receive dividends in the amounts necessary to meet our debt obligations or to pay dividends on our common stock. This could affect our financial position.

Please see Item 1, Regulation, Page 19, and Item 8, Note 8 of the Consolidated Financial Statements, Page 96, for discussion of insurance holding company dividend regulations.

**We could make investment decisions or experience market value fluctuations that trigger restrictions applicable to the parent company under the Investment Company Act of 1940.**

Compared with other insurance holding companies, we hold a significant level of investment assets at the parent company level. If these investment assets grow to account for more than 40 percent of parent company's total assets, excluding assets of our subsidiaries, we might become subject to regulation under the Investment Company Act of 1940. Our operations are limited by the constraint that investment securities held at the holding company level should remain below the 40 percent threshold described above. Efforts to stay below the threshold could result in:

- Disposal of otherwise desirable investment securities, possibly under undesirable conditions. Such dispositions could result in a lower return on investment, loss of investment income, and if we were unable to manage the timing of the dispositions, we also might realize unnecessary capital gains, which would increase our annual tax payment.
- Limited opportunities to purchase equity securities that hold the potential for market value appreciation, which could hamper book value growth over the long term.

- Maintenance of a greater portion of our portfolio of equity securities at the insurance subsidiary, which would cause the parent to be more reliant on its subsidiaries for cash to fund parent-company obligations, including shareholder dividends and interest on long-term debt.

If the parent company's investment assets were to exceed the 40 percent ratio to its total assets, excluding investment in its subsidiaries, and if it were determined that the holding company was an unregistered investment company, the holding company might be unable to enforce contracts with third parties, and third parties could seek rescission of transactions with the holding company undertaken during the period that it was an unregistered investment company, subject to equitable considerations set forth in the Investment Company Act. In addition, the holding company could become subject to monetary penalties or injunctive relief, or both, in an action brought by the SEC.

### **Our business depends on the uninterrupted operation of our facilities, systems and business functions.**

Our business depends on our associate's ability to perform necessary business functions, such as processing new and renewal policies and claims. We increasingly rely on technology and systems to accomplish these business functions in an efficient and uninterrupted fashion. Our inability to access our headquarters facilities or a failure of technology, telecommunications or other systems could significantly impair our ability to perform such functions on a timely basis or affect the accuracy of transactions. If sustained or repeated, such a business interruption or system failure could result in a deterioration of our ability to write and process new and renewal business, serve our agents and policyholders, pay claims in a timely manner, collect receivables or perform other necessary business functions. If our disaster recovery and business continuity plans did not sufficiently consider, address or reverse the circumstances of an interruption or failure, this could result in a materially adverse effect on our operating results and financial condition.

## **Item 1B. Unresolved Staff Comments**

None

## **Item 2. Properties**

Cincinnati Financial Corporation owns our headquarters building located on 100 acres of land in Fairfield, Ohio. This building contains approximately 800,000 total square feet. The property, including land, is carried in our financial statements at \$68 million as of December 31, 2007, and is classified as land, building and equipment, net, for company use. John J. & Thomas R. Schiff & Co. Inc., a related party, occupies approximately 6,750 square feet (1 percent).

Construction of a 690,000 total square foot underground garage and third office tower at our headquarters building began in early 2005. We estimate a completion date of July 2008 for the project. We believe this estimated \$100 million expansion will accommodate our business needs for the foreseeable future.

The construction project is on schedule and on budget. As of December 31, 2007, construction costs totaled \$86 million, which is classified as land, building and equipment, net, for company use.

Cincinnati Financial Corporation owns the Fairfield Executive Center, which is located on the northwest corner of our headquarters property. This is a four-story office building containing approximately 124,000 square feet. The property is carried in the financial statements at \$7 million as of December 31, 2007, and is classified as land, building and equipment, net, for company use. Our subsidiaries occupy approximately 90 percent of the rentable square feet and unaffiliated tenants occupy approximately 10 percent. In 2008, subsidiary operations in this building will relocate to the third office tower at our headquarters location. Portions of the space will be available for lease during 2008.

In 2007, The Cincinnati Life Insurance Company sold a four-story office building in Springdale, Ohio. The property was carried in the financial statements at \$3 million as of December 31, 2006, and was classified as other invested assets. A capital gain of \$2 million was realized on the sale of the property.

The Cincinnati Insurance Company owns an unoccupied building on 16 acres of land in Springfield Township, Ohio, approximately six miles from our headquarters. We plan to renovate the 51,000 square foot building to serve as a disaster recovery and backup data processing center at an estimated cost of \$26 million.

The property, including land, is carried on our financial statements at \$3 million as of December 31, 2007, and is classified as land, building and equipment, net, for company use.

## **Item 3. Legal Proceedings**

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

## **Item 4. Submission of Matters to a Vote of Security Holders**

No matters were submitted to a vote of security holders of Cincinnati Financial during the fourth quarter of 2007.

## Part II

### Item 5. Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Cincinnati Financial Corporation had approximately 12,000 shareholders of record and approximately 46,000 beneficial shareholders as of December 31, 2007. Many of our independent agent representatives and most of the 4,087 associates of our subsidiaries own the company's common stock. We are unable to accurately quantify those holdings because many are beneficially held.

Our common shares are traded under the symbol CINF on the Nasdaq Global Select Market.

Quarter:	2007				2006			
	1 <sup>st</sup>	2 <sup>nd</sup>	3 <sup>rd</sup>	4 <sup>th</sup>	1 <sup>st</sup>	2 <sup>nd</sup>	3 <sup>rd</sup>	4 <sup>th</sup>
High close	\$ 45.92	\$ 47.62	\$ 44.79	\$ 44.84	\$ 45.56	\$ 47.01	\$ 48.44	\$ 49.07
Low close	42.24	42.57	36.91	38.37	42.07	41.43	45.93	44.25
Period-end close	42.40	43.40	43.31	39.54	42.07	47.01	48.12	45.31
Cash dividends declared	0.355	0.355	0.355	0.355	0.335	0.335	0.335	0.335

Our ability to pay cash dividends may depend on the ability of our insurance subsidiary to pay dividends to the parent company. The dividend restrictions of our insurance company subsidiaries are discussed in Item 8, Note 8 of the Consolidated Financial Statements, Page 96.

The following summarizes securities authorized for issuance under our equity compensation plans as of December 31, 2007:

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights at December 31, 2007	Weighted-average exercise price of outstanding options	Number of securities remaining available for future issuance under equity compensation plan (excluding securities reflected in column (a)) at December 31, 2007
	(a)	(b)	(c)
Equity compensation plans approved by security holders	10,676,202	\$ 36.86	10,560,257
Equity compensation plans not approved by security holders	-	-	-
Total	10,676,202	\$ 36.86	10,560,257

Additional information about stock-based associate compensation granted under our equity compensation plans is available in Item 8, Note 16 of the Consolidated Financial Statements, Page 102.

The board of directors has authorized share repurchases since 1996. We discuss the board authorization in Item 7, Liquidity and Capital Resources, Uses of Capital, Page 64. In 2007, we repurchased a total of 7,454,637 shares.

Month	Total number of shares purchased <sup>(1)</sup>	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
January 1-31, 2007	0	\$ 0.00	0	6,819,248
February 1-28, 2007	478,267	43.82	478,267	6,340,981
March 1-31, 2007	1,012,808	42.64	1,012,317	5,328,664
April 1-30, 2007	0	0.00	0	5,328,664
May 1-31, 2007	0	0.00	0	5,328,664
June 1-30, 2007	0	0.00	0	5,328,664
July 1-31, 2007	0	0.00	0	5,328,664
August 1-31, 2007	1,522,147	41.42	1,522,147	3,806,517
September 1-30, 2007	405,001	42.18	405,001	3,401,516
October 1-31, 2007	4,000,000	40.02	4,000,000	12,401,516
November 1-30, 2007	55,332	39.99	36,905	12,364,611
December 1-31, 2007	0	0.00	0	12,364,611
Totals	7,473,555	41.02	7,454,637	

(1) Includes 18,918 shares acquired in 2007 primarily in satisfaction of the purchase price due upon exercise of stock options.

On October 24, 2007, we entered into an accelerated share repurchase agreement for 4 million shares. At the same time, the board of directors also expanded the existing repurchase authorization to approximately 13 million shares. 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, pursuant to SEC regulations.

The prior repurchase program for 10 million shares was announced in 2005, replacing a program that had been in effect since 1999. No repurchase program has expired during the period covered by the above table. All of the repurchases reported in the table above were repurchased under our original 2005 program or the expansion announced in October 2007. Neither the 2005 nor 1999 program had an expiration date, but no further repurchases will occur under the 1999 program.

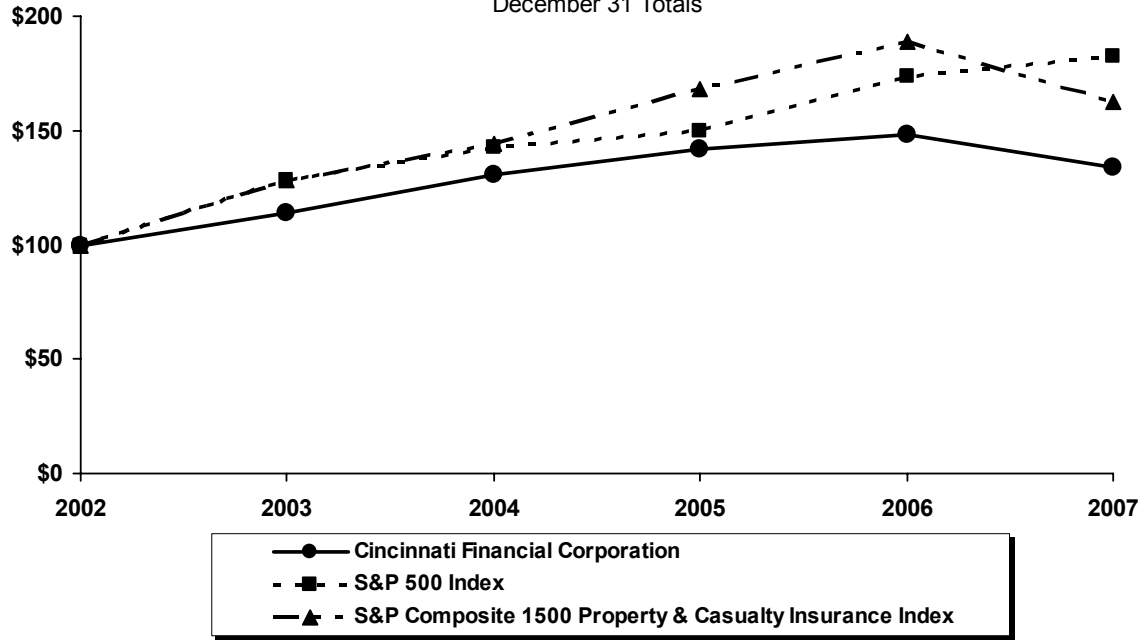
### **Cumulative Total Return**

As depicted in the graph below, the five-year total return on a \$100 investment made December 31, 2002, assuming the reinvestment of all dividends, was 34.0 percent for Cincinnati Financial Corporation's common stock compared with 62.3 percent for the Standard & Poor's Composite 1500 Property & Casualty Insurance Index and 82.9 percent for the Standard & Poor's 500 Index.

The Standard & Poor's Composite 1500 Property & Casualty Insurance Index includes 29 companies: Ace Ltd., Allstate Corporation, AMBAC Financial Group, Berkley (W R) Corporation, Chubb Corporation, Cincinnati Financial Corporation, Commerce Group Inc., Fidelity National Financial Inc., First American Corporation, Hanover Insurance Group Inc., Infinity Property & Casualty Corporation, Landamerica Financial Group, MBIA Inc., Mercury General Corporation, Old Republic International Corporation, Philadelphia Consolidated Holding Corporation, Proassurance Corporation, Progressive Corporation, RLI Corporation, Safeco Corporation, Safety Insurance Group Inc., SCPIE Holdings Inc., Selective Insurance Group Inc., Stewart Information Services, Tower Group Inc., Travelers Companies Inc., United Fire & Casualty Company, XL Capital Ltd. and Zenith National Insurance Corporation.

The Standard & Poor's 500 Index includes a representative sample of 500 leading companies in a cross section of industries of the U.S. economy. Although this index focuses on the large capitalization segment of the market, it is widely viewed as a proxy for the total market.

**Total Return Analysis**  
**CFC vs. Market Indices**  
December 31 Totals



## Item 6. Selected Financial Data

(In millions except per share data)

	Years ended December 31,			
	2007	2006	2005	2004
<b>Consolidated Income Statement Data</b>				
Earned premiums	\$ 3,250	\$ 3,278	\$ 3,164	\$ 3,020
Investment income, net of expenses	608	570	526	492
Realized investment gains and losses	382	684	61	91
Total revenues	4,259	4,550	3,767	3,614
Net income	855	930	602	584
Net income per common share:				
Basic	\$ 5.01	\$ 5.36	\$ 3.44	\$ 3.30
Diluted	4.97	5.30	3.40	3.28
Cash dividends per common share:				
Declared	1.42	1.34	1.205	1.04
Paid	1.40	1.31	1.162	1.02
<b>Shares Outstanding</b>				
Weighted average, diluted	172	175	177	178
<b>Consolidated Balance Sheet Data</b>				
Invested assets	\$ 12,261	\$ 13,759	\$ 12,702	\$ 12,677
Deferred policy acquisition costs	461	453	429	400
Total assets	16,637	17,222	16,003	16,107
Loss and loss expense reserves	3,967	3,896	3,661	3,549
Life policy reserves	1,478	1,409	1,343	1,194
Long-term debt	791	791	791	791
Shareholders' equity	5,929	6,808	6,086	6,249
Book value per share	35.70	39.38	34.88	35.60
<b>Property Casualty Insurance Operations</b>				
Earned premiums	\$ 3,125	\$ 3,164	\$ 3,058	\$ 2,919
Unearned premiums	1,562	1,576	1,557	1,537
Loss and loss expense reserves	3,925	3,860	3,629	3,514
Investment income, net of expenses	393	367	338	289
Loss ratio	46.6 %	51.9 %	49.2 %	49.8 %
Loss expense ratio	12.0	11.6	10.0	10.3
Expense ratio	31.7	30.8	30.0	29.7
Combined ratio	90.3 %	94.3 %	89.2 %	89.8 %

Per share data adjusted to reflect all stock splits and dividends prior to December 31, 2007.

### Significant realized gains and one-time charges or adjustments:

2007 – The company sold 3.8 million shares of its holding in Exxon Mobil Corporation common stock. The sale contributed \$217 million (pretax) to realized investment gains and revenues and \$141 million (after tax), or 81 cents per share, to net income. The company divested the majority of its real estate investment trust holdings. The sales contributed \$73 million (pretax) to realized investment gains and revenues and \$47 million (after tax), or 27 cents per share, to net income.

The company sold 5.5 million shares of its holdings in Fifth Third Bancorp common stock. The sale contributed \$64 million (pretax) to realized investment gains and revenues and \$42 million (after tax), or 24 cents per share, to net income.

The company sold all of its holdings in FirstMerit Corporation common stock. The sale contributed \$59 million (pretax) to realized investment gains and revenues and \$38 million (after tax), or 22 cents per share, to net income.

2006 – The company sold all of its holdings in Alltel Corporation common stock. The sale contributed \$647 million (pretax) to realized investment gains and revenues and \$412 million (after tax), or \$2.35 per share, to net income.

2003 – As the result of a settlement negotiated with a vendor, pretax results included the recovery of \$23 million of the \$39 million one-time, pretax charge incurred in 2000.

2000 – The company recorded a one-time charge of \$39 million, pretax, to write down previously capitalized costs related to the development of software to process property casualty policies. The company earned \$5 million in interest in the first quarter from a \$303 million single-premium bank-owned life insurance (BOLI) policy booked at the end of 1999 that was segregated as a separate account effective April 1, 2000. Investment income and realized investment gains and losses from separate accounts generally accrue directly to the contract holder and, therefore, are not included in the company's consolidated financials.

	2003	2002	2001	2000	1999	1998	1997
\$	2,748	\$ 2,478	\$ 2,152	\$ 1,907	\$ 1,732	\$ 1,613	\$ 1,516
	465	445	421	415	387	368	349
	(41)	(94)	(25)	(2)	0	65	69
	3,181	2,843	2,561	2,331	2,128	2,054	1,942
	374	238	193	118	255	242	299
\$	2.11	\$ 1.33	\$ 1.10	\$ 0.67	\$ 1.40	\$ 1.31	\$ 1.64
	2.10	1.32	1.07	0.67	1.37	1.28	1.61
	0.90	0.81	0.76	0.69	0.62	0.55	0.50
	0.89	0.80	0.74	0.67	0.60	0.54	0.49
	178	180	179	181	186	190	188
\$	12,485	\$ 11,226	\$ 11,534	\$ 11,276	\$ 10,156	\$ 10,296	\$ 8,778
	372	343	286	259	226	143	135
	15,509	14,122	13,964	13,274	11,795	11,484	9,867
	3,415	3,176	2,887	2,473	2,154	2,055	1,937
	1,025	917	724	641	885	536	482
	420	420	426	449	456	472	58
	6,204	5,598	5,998	5,995	5,421	5,621	4,717
	35.10	31.43	33.62	33.80	30.35	30.58	25.71
\$	2,653	\$ 2,391	\$ 2,073	\$ 1,828	\$ 1,658	\$ 1,543	\$ 1,454
	1,444	1,317	1,060	920	835	458	442
	3,386	3,150	2,894	2,416	2,093	1,979	1,889
	245	234	223	223	208	204	199
	56.1 %	61.5 %	66.6 %	71.1 %	61.6 %	65.4 %	58.3 %
	11.6	11.4	10.1	11.3	10.0	9.3	10.1
	27.0	26.8	28.2	30.4	28.6	29.6	30.0
	94.7 %	99.7 %	104.9 %	112.8 %	100.2 %	104.3 %	98.4 %

# Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

## INTRODUCTION

The purpose of Management's Discussion and Analysis is to provide an understanding of Cincinnati Financial Corporation's consolidated results of operations and financial position. Management's Discussion and Analysis should be read in conjunction with Item 6, Selected Financial Data, Pages 30 and 31, and Item 8, Consolidated Financial Statements and related Notes, beginning on Page 80. We present per share data on a diluted basis unless otherwise noted, and we have adjusted those amounts for all stock splits and stock dividends.

We begin with an executive summary of our results of operations and outlook, as well as details on critical accounting policies and estimates. Periodically, we refer to estimated industry data so that we can give information on our performance versus the overall insurance industry. Unless otherwise noted, the industry data is prepared by A.M. Best, 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).

## EXECUTIVE SUMMARY

Through The Cincinnati Insurance Company and its local independent agent representatives, Cincinnati Financial Corporation has become one of the 25 largest property casualty insurer groups in the nation, based on premium volume for the approximate 2,000 U.S. stock and mutual insurer groups. We primarily market standard market property casualty insurance products through a select group of independent insurance agencies in 34 states. As we discussed in the business description in Item 1, we believe three key characteristics distinguish our company and allow us to build shareholder value:

- We cultivate relationships with the independent insurance agents who market our policies and we make our decisions at the local level
- We achieve claims excellence, covering the spectrum from our response to reported claims to our approach to establishing reserves for not-yet-paid claims
- We invest for long-term total return, using available cash flow to purchase equity securities after covering insurance liabilities by purchasing fixed-maturity securities

We provide additional detail on these subjects in the Results of Operations and Liquidity and Capital Resources sections of this discussion.

Among the factors that influence the consolidated results of operations and financial position of the company, we consider our relationships with independent insurance agents to be the most significant. We seek to be an indispensable partner in each agency's success. To continue to achieve our performance targets, we must maintain these strong relationships, write a significant portion of each agency's business and attract new agencies that share our business philosophy.

We believe consistently applying our long-term strategies rather than taking short-term actions will allow us to address these challenges. We seek to meet our agents' needs, with an eye toward solutions and approaches that will give us an advantage for five, 10 or more years. As we appoint new agencies, we are looking to build relationships that lead them to award us a preferred position and a meaningful share of the business they write.

In 2007, we did not achieve some of our objectives for creating shareholder value. For the year, we wrote less new property casualty business than the prior year and market pricing trends led to slightly lower written premiums and put some pressure on our current accident year margins. Nonetheless, we continued to build our company for the long term. Agencies continued to successfully market our products to their better accounts. They gave us \$325 million of new property casualty business and helped us maintain the persistency of renewals at more than 90 percent of our accounts. Our equity-focused investment strategy led to another year of record investment income even as declines in the market values of our financial sector common stocks led to lower invested assets and book value.

We look beyond 2007, recognizing the challenges that will face us and with strategies in place to address those challenges. We remain committed to providing a stable market for our agents' high quality business, underwriting this business carefully and producing steady value for our shareholders, as represented by the board of directors' recent decision to increase our 2008 indicated annual cash dividend by 9.9 percent, which would mark the 48<sup>th</sup> consecutive year of increase in that measure. We believe we can achieve above-industry-average growth in written premiums and industry-leading profitability over the long term by building on our proven strategies: strong agency relationships, local underwriting, quality claims service, solid reserves and total return investing.



Over our 57 year history, our growth largely has been driven by increasing our share of the business written by the agencies that market our products, growth of those agencies, appointment of new agencies and our periodic entry into new states. During 2008, we are targeting 65 new agency appointments.

Over the years, we have been able to increase our share of our agencies' business by making available insurance products that meet the needs of the individuals and businesses in their communities. In recent years, our agents had indicated their interest in having Cincinnati available as a market for commercial accounts that require the flexibility of excess and surplus lines coverage. Preparations that began in early 2007 to initiate excess and surplus lines operations concluded on schedule in December 2007. Our new subsidiary, The Cincinnati Specialty Underwriters Insurance Company, received an A (Excellent) rating from A.M. Best, an independent provider of insurer ratings. As noted in Item 1, Excess and Surplus Lines Operation Further Enhances Agency Relationships, Page 6, our new wholly owned brokerage CSU Producer Resources began marketing excess and surplus lines policies to selected agencies in five states in January 2008.

Below we review highlights of our financial results for the past three years and measures of the success of our efforts to create shareholder value. Detailed discussion of these topics appears in Results of Operations, Page 42, and Liquidity and Capital Resources, Page 60.

## CORPORATE FINANCIAL HIGHLIGHTS

### Income Statement and Per Share Data

(Dollars in millions except share data)	Twelve months ended December 31,			2007-2006	2006-2005
	2007	2006	2005	Change %	Change %
<b>Income statement data</b>					
Earned premiums	\$ 3,250	\$ 3,278	\$ 3,164	(0.9)	3.6
Investment income, net of expenses	608	570	526	6.6	8.4
Realized investment gains and losses (pretax)	382	684	61	(44.1)	1,026.1
Total revenues	4,259	4,550	3,767	(6.4)	20.8
Net income	855	930	602	(8.0)	54.5
<b>Per share data (diluted)</b>					
Net income	\$ 4.97	\$ 5.30	\$ 3.40	(6.2)	55.9
Cash dividends declared	1.42	1.34	1.205	6.0	11.2
Weighted average shares outstanding	172,167,452	175,451,341	177,116,126	(1.9)	(0.9)

Revenues in 2007 and 2006 were significantly higher than in 2005. Both years reflected significant net realized investment gains from sales of common stock holdings. In both years, rising pretax investment income offset the slowing growth rate of consolidated property casualty earned premiums.

Net income and net income per share declined slightly in 2007 from a record level in 2006. The most significant factors contributing to net income are:

- Underwriting profit or loss – The consolidated property casualty underwriting profit rose in 2007 because of lower catastrophe losses and a higher level of savings from favorable development on prior period reserves. In 2006, underwriting profit was below the prior year due to higher catastrophe losses and a lower level savings from favorable development of prior period reserves as well as higher underwriting expenses. These factors are discussed in more detail in the Results of Operations beginning on Page 42.
- Realized investment gains or losses – Realized investment gains and losses are integral to our financial results over the long term. We have substantial discretion in the timing of investment sales and, therefore, the gains or losses that will be recognized in any period. That discretion generally is independent of the insurance underwriting process. Also, applicable accounting standards require us to recognize gains and losses from certain changes in fair values of securities and embedded derivatives without actual realization of those gains and losses. As discussed in Investments Segment Results of Operation, Page 57, security sales led to realized investment gains in the past three years:
  - 2007 – Raised net income by \$245 million, or \$1.43 per share. This amount reflected the sale of 3.8 million shares of Exxon Mobil Corporation, the block sale of 5.5 million shares of Fifth Third Bancorp common stock, the sale of our FirstMerit Corporation common stock holdings and the disposition of the majority of our real estate investment trust holdings.
  - 2006 – Raised net income by \$434 million, or \$2.48 per share. This amount reflected the sale of our Alltel Corporation common stock holding.
  - 2005 – Raised net income by \$40 million, or 23 cents per share.

- Weighted average shares outstanding may fluctuate from period to period because we regularly repurchase shares under board authorizations and we issue shares when associates exercise stock options. Weighted average shares outstanding on a diluted basis declined 3 million in 2007 and 2 million in 2006.

Cash dividends declared per share rose 6.0 percent and 11.2 percent in 2007 and 2006.

## Balance Sheet Data and Performance Measures

(Dollars in millions except share data)	At December 31,		At December 31,		At December 31,	
	2007		2006		2005	
<b>Balance sheet data</b>						
Invested assets	\$	12,261	\$	13,759	\$	12,702
Total assets		16,637		17,222		16,003
Short-term debt		69		49		0
Long-term debt		791		791		791
Shareholders' equity		5,929		6,808		6,086
Book value per share		35.70		39.38		34.88
Debt-to-capital ratio		12.7 %		11.0 %		11.5 %
Years ended December 31,						
		2007		2006		2005
<b>Performance measures</b>						
Comprehensive income	\$	(368)	\$	1,057	\$	99
Return on equity		13.4 %		14.4 %		9.8 %
Return on equity based on comprehensive income		(5.8)		16.4		1.6

Invested assets and total assets declined in 2007, primarily due to lower market values of financial sector equity holdings. Invested assets and total assets rose in 2006 on new investments and appreciation in the equity portfolio.

Comprehensive income is net income plus the year-over-year difference in unrealized gains on investments. Comprehensive income moved in concert with the changes in unrealized investment gains over the three-year period. Unrealized investment gains declined in 2007 because of lower market values of our financial sector holdings, after rising in 2006. Unrealized gains were lower in 2005 primarily due to a decline in the market value of our Fifth Third investment.

Return on equity in 2007 declined slightly due to lower realized gains on investments after rising in 2006 due to higher realized gains on investments. Return on equity based on comprehensive income declined in 2007 because of lower comprehensive income due to lower unrealized investment gains. It rose in 2006 due to the increase in accumulated other comprehensive income.

Our ratio of long-term debt to capital (long-term debt plus shareholders' equity) rose in 2007 after declining in 2006. The increase in 2007 was due to share repurchase and lower unrealized gains, which primarily reflected the lower market values of our financial sector equity holdings.

## Property Casualty Highlights

(Dollars in millions)	Years ended December 31,			2007-2006 Change %	2006-2005 Change %			
	2007	2006	2005					
<b>Property casualty highlights</b>								
Written premiums	\$	3,117	\$	3,178	\$	3,076	(1.9)	3.3
Earned premiums		3,125		3,164		3,058	(1.2)	3.5
Underwriting profit		304		181		330	68.3	(45.2)
GAAP combined ratio		90.3 %		94.3 %		89.2 %		
Statutory combined ratio		90.3		93.9		89.0		

The trend in overall written premium growth reflected the competitive and market factors discussed in Item 1, Commercial Lines and Personal Lines Insurance Results of Operations, Page 44 and Page 51. Our consolidated property casualty insurance underwriting profit rose in 2007 after declining in 2006, matching the trend in our combined ratio. (The combined ratio is the percentage of each premium dollar spent on claims plus all expenses – the lower the ratio, the better the performance.) 2007 performance was bolstered by lower catastrophe losses and higher savings from favorable development on prior period reserves.

We also measure a variety of non-financial metrics for our property casualty operations. For example, we monitor our rank within our reporting agency locations. In 2006, we ranked No. 1 or No. 2 by premium volume in 74.2 percent of the locations that have marketed our products for more than five years. Other measures include subdivision of territories and new agency appointments. We ended 2007 with 106 field territories, subdividing three new territories and merging one into the surrounding regions. As discussed in Item 1, Growing with Our Agencies, Page 9, we made 66 new agency appointments in 2007, 50 of which were new relationships. These new appointments and other changes in agency structures led to a net increase in reporting agency locations of 38 in 2007.

Agent satisfaction with our technology solutions is, and will continue to be, a requirement for maintaining our strong relationships with these agencies. In 2007, we made additional progress in implementing technology solutions that we believe should make it easier for agencies to do business with us. Among other 2007 milestones, we deployed our new commercial lines policy processing system to agencies in 10 states for use in processing new and renewal businessowners policies, bringing the year-end total to 17 states. We also deployed our personal lines policy processing system in four states, bringing the year-end total to 17 states, and continued to make important upgrades and enhancements.

In each of the past three years, our results have compared satisfactorily to estimated industry results. Industry net written premiums were estimated to decline 1.2 percent in 2007. In 2006, industry premiums were estimated to rise 3.9 percent after no change in 2005. In the past three years, industry premium trends have been obscured by the reinsurance sector, where premiums were estimated to have declined 8.5 percent in 2007, risen 28.1 percent in 2006 and declined 28.2 percent in 2005. The estimated industry average statutory combined ratios were 95.6 percent in 2007, 92.4 percent in 2006 as well as 101.2 percent in 2005 when the 144.9 percent estimated reinsurance sector combined ratio obscured the industry combined ratio.

## MEASURING OUR SUCCESS IN 2008 AND BEYOND

Looking into 2008 and beyond, we will continue to measure the success of our strategies:

- Maintaining our strong relationships with our established agencies, writing a significant portion of each agency's business and attracting new agencies – In 2008, we expect to continue to rank No. 1 or No. 2 by premium volume in approximately 75 percent or more of the locations that have marketed our products for more than five years, not taking into account any contribution from our excess and surplus lines business. We expect to improve service to our agencies by subdividing one or two field territories in 2008. We also expect to appoint another 65 agencies.

In 2008, we expect to make further progress in our efforts to improve service to and communication with our agencies through our expanding portfolio of software. In particular, we will continue to deploy our commercial lines and personal lines quoting and policy processing systems that allow our agencies and our field and headquarters associates to collaborate on new and renewal business more efficiently and give our agencies choice and control. We discuss our technology plans for 2008 in Item 1, Technology Solutions, Page 4.

- Achieving above-industry-average growth in property casualty statutory net written premiums and maintaining industry-leading profitability by leveraging our regional franchise and proven agency-centered business strategy – If current commercial lines pricing trends continue into 2008, our net written premiums could decline as much as 5 percent compared with the 1.9 percent decline in 2007.

Overall industry premiums are expected to decline 0.6 percent in 2008, which includes an estimated 5.0 percent decline for the reinsurance sector. Net written premiums for the commercial lines sector are expected to be down 2.3 percent in 2008 while the personal lines sector is expected to grow 1.4 percent. The projected industry average 2008 combined ratio is 98.6 percent.

Our combined ratio estimate for 2008 is 96 percent to 98 percent compared with 90.3 percent in 2007. The year-over-year increase reflects three assumptions:

- Current accident year loss ratio excluding catastrophe losses – We believe the market trends that contributed to an increase in this ratio in 2007 are continuing and may put the ratio under further pressure in 2008.
- Catastrophe loss ratio – We assume catastrophe losses could contribute approximately 4.5 percentage points to the full-year 2008 combined ratio. We are aware of the unpredictability of catastrophic events in any given year. Catastrophe losses have made an average contribution of 3.7 percentage points to our combined ratio in the past 10 years, ranging from 2007's low of 0.8 points to 1998's high of 6.1 points.

In January and February of 2008, storms affecting our policyholders in the Midwest resulted in at least \$36 million of pretax catastrophe losses, which will be included in first-quarter 2008 results.

This estimate does not take into account any catastrophe activity that may occur in the remainder of the first quarter of 2008 or potential development from events in prior periods.

- Savings from favorable development on prior period reserves – To establish this combined ratio estimate, management made the assumption that prior period reserves would develop favorably and that the development would affect the ratio by 4 percentage points. The actual level of development on prior period reserves will be based on sound actuarial analysis.

Economic factors, including Inflation, may increase our claims and settlement expenses related to medical care, litigation and construction. We could see higher than anticipated loss costs related to workers' compensation and lines of business that provide protection against bodily injury claims. Similarly, higher legal expenses could raise the loss expenses we incur to defend our policyholders and settle complex or disputed claims. We would factor any such higher losses and loss expenses into our pricing and reserve

calculations, potentially increasing reserves and adjusting rates. Our ability to meet performance targets would depend on our ability to offset the increased losses and loss expenses by promptly effecting rate adjustments or finding other savings and efficiencies, and on our agents' ability to market at the increased rate.

- Pursuing a total return investment strategy that generates both strong investment income growth and capital appreciation – In 2008, we estimate the growth rate of investment income may be below the 6.6 percent growth rate in 2007 as financial sector holdings in our portfolio evaluate their dividend levels. We continue to focus on portfolio strategies to balance near-term income generation and long-term book value growth. This outlook considers the anticipated level of dividend income from equity holdings, the investment of insurance operations cash flow and the current portfolio attributes.

We do not establish annual capital appreciation targets. Over the long term, our target is to have the equity portfolio outperform the Standard & Poor's 500 Index. In 2007, our compound annual equity portfolio return was a negative 16.3 percent, compared with a compound annual total return of 5.5 percent for the Index. Over the five years ended December 31, 2007, our compound annual equity portfolio return was flat compared with a compound annual total return of 12.8 percent for the Index. Our equity portfolio underperformed the market for the five-year period primarily because of the decline in the market value of our holdings of Fifth Third common stock between 2003 and 2007.

- Increasing the total return to shareholders through a combination of higher earnings per share, growth in book value, increasing dividends and share repurchase – We do not announce annual targets for earnings per share or book value. Over the long term, we look for our earnings per share growth to outpace that of a peer group of national and regional property casualty insurance companies. Long-term book value growth should exceed that of our equity portfolio.

The board of directors is committed to steadily increasing cash dividends, periodically authorizing stock dividends and splits and authorizing share repurchase. In February 2008, the board increased the indicated annual cash dividend rate 9.9 percent, marking the 48<sup>th</sup> consecutive year of increase in the dividend rate. We believe our record of dividend increases is matched by only 11 other publicly traded corporations. Between January 1 and February 22, 2008, we repurchased 1 million shares under the current board authorization.

Over the long-term, we seek to increase earnings per share, book value and dividends at a rate that would allow long-term total return to our shareholders to exceed that of the Standard & Poor's Composite 1500 Property Casualty Insurance Index. Over the past five years, our total return to shareholders of 34.0 percent was below the 62.3 percent return for that Index.

- Maintaining financial strength by keeping the ratio of debt to capital below 15 percent and purchasing reinsurance to provide investment flexibility – Our debt-to-capital ratio rose to 12.7 percent in 2007 because of the decline in shareholders' equity. Based on our present capital requirements, we do not anticipate a material increase in debt levels during 2007. As a result, we believe our debt-to-capital ratio will remain below 13 percent.

In December 2007, we finalized our property casualty reinsurance program for 2008, updating it to maintain the balance between the cost of the program and the level of risk we retain. Under the new program, our 2008 reinsurance costs are expected to decline slightly due to higher retention levels and moderating rates for certain lines of business. We provide more detail on our reinsurance programs in 2008 Reinsurance Programs, Page 70.

Factors supporting our outlook for 2008 are discussed in the Results of Operations for each of the four business segments.

## CRITICAL ACCOUNTING ESTIMATES

Cincinnati Financial Corporation's financial statements are prepared using GAAP. These principles require management to make estimates and assumptions that affect the amounts reported in the Consolidated Financial Statements and accompanying Notes. Actual results could differ materially from those estimates.

The significant accounting policies used in the preparation of the financial statements are discussed in Item 8, Note 1 of the Consolidated Financial Statements, Page 87. In conjunction with that discussion, material implications of uncertainties associated with the methods, assumptions and estimates underlying the company's critical accounting policies are discussed below. The audit committee of the board of directors reviews the annual financial statements with management and the independent registered public accounting firm. These discussions cover the quality of earnings, review of reserves and accruals, reconsideration of the suitability of accounting principles, review of highly judgmental areas including critical accounting policies, audit adjustments and such other inquiries as may be appropriate.

# PROPERTY CASUALTY INSURANCE LOSS AND LOSS EXPENSE RESERVES

## Overview

We establish loss and loss expense reserves for our property casualty insurance business as balance sheet liabilities. These reserves account for unpaid loss and loss expenses as of a financial statement date. Unpaid loss and loss expenses are the estimated amounts necessary to pay for and settle all outstanding insured claims, including incurred but not reported (IBNR) claims, as of that date.

For some lines of business that we write, a considerable and uncertain amount of time can elapse between the occurrence, reporting and payment of insured claims. The amount we will actually have to pay for such claims also can be highly uncertain. This uncertainty, together with the size of our reserves, makes the loss and loss expense reserves our most significant estimate. Gross loss and loss expense reserves were \$3.925 billion, or 36.7 percent of total liabilities, at year-end 2007, compared with \$3.860 billion, or 37.1 percent of total liabilities, at year-end 2006.

## How Reserves Are Established

Our field claims representatives establish case reserves when claims are reported to the company to provide for our unpaid loss and loss expense obligation associated with these claims. Experienced headquarters claims supervisors review individual case reserves greater than \$35,000 that were established by field claims representatives. Headquarters claims managers also review case reserves greater than \$100,000.

Our claims representatives base their case reserve estimates primarily upon case-by-case evaluations that consider:

- type of claim involved
- circumstances surrounding each claim
- policy provisions pertaining to each claim
- potential for subrogation or salvage recoverable
- general insurance reserving practices

Case reserves of all sizes are subject to review on a 90-day cycle or more frequently, if new information regarding a loss becomes available. As part of the review process, we monitor industry trends, cost trends, relevant court cases, legislative activity and other current events in an effort to ascertain new or additional loss exposures.

We also establish incurred but not reported (IBNR) reserves to provide for all unpaid loss and loss expenses not accounted for by case reserves. For other than asbestos and environmental claims, we calculate IBNR reserves quarterly by first deriving an actuarially based estimate of the ultimate cost of total loss and loss expenses incurred as of the financial statement date. We then reduce the estimate by total loss and loss expense payments and total case reserves carried as of the financial statement date.

We calculate IBNR reserves for asbestos and environmental claims by deriving an actuarially based estimate of total unpaid loss and loss expenses as of the financial statement date. We then reduce the estimate by total case reserves as of the financial statement date. We discuss the reserve analysis that applies to claims other than asbestos and environmental claims below. We discuss the reserve analysis that applies to asbestos and environmental reserves in Asbestos and Environmental Reserves, Page 66.

Our actuarial staff applies significant judgment in selecting models and estimating model parameters when preparing reserve analyses. In addition, unpaid loss and loss expenses are inherently uncertain as to timing and amount. Uncertainties relating to model appropriateness, parameter estimates and actual loss and loss expense amounts are referred to as model, parameter and process uncertainty, respectively. Our management and actuarial staff control for these uncertainties in the reserving process in a variety of ways.

Our actuarial staff bases its estimates primarily on the indications of methods and models that analyze accident year data. Accident year is the year in which an insured claim, loss, or loss expense occurred. The specific methods and models that we have used for the past several years are:

- paid and reported loss development methods
- paid and reported loss Bornhuetter-Ferguson methods
- individual and multiple probabilistic trend family models

Our actuarial staff uses diagnostics provided by stochastic reserving software to evaluate the appropriateness of the models and methods listed above. The software's diagnostics have indicated that the appropriateness of these models and methods for estimating IBNR reserves for our lines of business tends to depend on a line's tail. Tail refers to the time interval between a typical claim's occurrence and its settlement. For our long tail lines such as workers' compensation and commercial casualty, models from the probabilistic trend family tend to provide superior fits and to validate well compared with models underlying the loss development and Bornhuetter-Ferguson methods. The loss development and Bornhuetter-Ferguson methods, particularly the reported loss variations, tend to produce the more appropriate IBNR reserve estimates for our short-tail lines

such as homeowner and commercial property. For our mid-tail lines such as personal and commercial auto liability, all models and methods provide useful insights.

Our actuarial staff also devotes significant time and effort to the estimation of model and method parameters. The loss development and Bornhuetter-Ferguson methods require the estimation of numerous loss development factors. The Bornhuetter-Ferguson methods also involve the estimation of numerous ultimate loss ratios by accident year. Models from the probabilistic trend family require the estimation of development trends, calendar year inflation trends and exposure levels. Consequently, our actuarial staff monitors a number of trends and measures to gain key business insights necessary for exercising appropriate judgment when estimating the parameters mentioned.

These trends and measures include:

- company and industry pricing
- company and industry exposure
- company and industry loss frequency and severity
- past large loss events such as hurricanes
- company and industry premium
- company in-force policy count
- average premium per policy

These trends and measures also support the estimation of ultimate accident year loss ratios needed for applying the Bornhuetter-Ferguson methods and for assessing the reasonability of all IBNR reserve estimates computed. Our actuarial staff reviews these trends and measures quarterly and updates them as necessary.

Quarterly, our actuarial staff summarizes its reserve analysis by preparing an actuarial best estimate and a range of reasonable IBNR reserves intended to reflect the uncertainty of the estimate. An inter-departmental committee that includes our actuarial management team reviews the results of each quarterly reserve analysis. The committee establishes management's best estimate of IBNR reserves, which is the amount that is included in each period's financial statements. In addition to the information provided by actuarial staff, the committee also considers factors such as the following:

- large loss activity and trends in large losses
- new business activity
- judicial decisions
- general economic trends such as inflation
- trends in litigiousness and legal expenses
- product and underwriting changes
- changes in claims practices

The determination of management's best estimate, like the preparation of the reserve analysis that supports it, involves considerable judgment. Changes in reserving data or the trends and factors that influence reserving data may signal fundamental shifts or may simply reflect single-period anomalies. Even if a change reflects a fundamental shift, the full extent of the change may not become evident until years later. Moreover, since our methods and models do not explicitly relate many of the factors we consider directly to reserve levels, we typically cannot quantify the precise impact of such factors on the adequacy of reserves prospectively or retrospectively.

Due to the uncertainties described above, our ultimate loss experience could prove better or worse than our carried reserves reflect. To the extent that reserves are inadequate and increased, the amount of the increase is a charge in the period that the deficiency is recognized, raising our loss and loss expense ratio and reducing earnings. To the extent that reserves are redundant and released, the amount of the release is a credit in the period that the redundancy is recognized, reducing our loss and loss expense ratio and increasing earnings.

### **Key Assumptions - Loss Reserving**

Our actuarial staff makes a number of key assumptions when using their methods and models to derive IBNR reserve estimates. Appropriate reliance on these key assumptions essentially entails determinations regarding the likelihood that statistically significant patterns in historical data will extend into the future. The four most significant of the key assumptions used by our actuarial staff and approved by management are:

- Emergence of loss and allocated loss expenses on an accident year basis. Historical paid loss, reported loss and paid allocated loss expense data for the business lines we analyze contain patterns that reflect how unpaid losses, unreported losses and unpaid allocated loss expenses as of a financial statement date will emerge in the future on an accident year basis. Unless our actuarial staff or management identifies reasons or factors that invalidate the extension of historical patterns into the future, these patterns can be

used to make projections necessary for estimating IBNR reserves. Our actuaries significantly rely on this assumption in the application of all methods and models mentioned above.

- Calendar year inflation. For long-tail and mid-tail business lines, calendar year inflation trends for future paid losses and paid allocated loss expenses will not vary significantly from a stable, long-term average. Our actuaries base reserve estimates derived from probabilistic trend family models on this assumption.
- Exposure levels. Historical earned premiums, when adjusted to reflect common levels of product pricing and loss cost inflation, can serve as a proxy for historical exposures. Our actuaries require this assumption to estimate expected loss ratios and expected allocated loss expense ratios used by the Bornhuetter-Ferguson reserving methods. They also use this assumption to establish exposure levels for recent accident years, characterized by “green” or immature data, when working with probabilistic trend family models.
- Claims having atypical emergence patterns. Characteristics of certain subsets of claims, such as high frequency, high severity, or mass tort claims, have the potential to distort patterns contained in historical paid loss, reported loss and paid allocated loss expense data. When testing indicates this to be the case for a particular subset of claims, our actuaries segregate these claims from the data and analyze them separately. Subsets of claims that could fall into this category include hurricane claims, individual large claims and asbestos and environmental claims.

These key assumptions have not changed since 2005, when our actuarial staff began using probabilistic trend family models to estimate IBNR reserves.

Paid losses, reported losses and paid allocated loss expenses are subject to random as well as systematic influences. As a result, actual paid losses, reported losses and paid allocated loss expenses are virtually certain to differ from projections. Such differences are consistent with what specific models for our business lines predict and with the related patterns in the historical data used to develop these models. As a result, management does not closely monitor statistically insignificant differences between actual and projected data.

### Reserve Estimate Variability

Management believes that the standard error of a reserve estimate, a measure of the estimate's variability, provides the most appropriate measure of the estimate's sensitivity. The reserves we establish depend on the models we use and the related parameters we estimate in the course of conducting reserve analyses. However, the actual amount required to settle all outstanding insured claims, including IBNR claims, as of a financial statement date depends on stochastic, or random, elements as well as the systematic elements captured by our models and estimated model parameters. For the lines of business we write, process uncertainty – the inherent variability of loss and loss expense payments – typically contributes more to the imprecision of a reserve estimate than parameter uncertainty.

Consequently, a sensitivity measure that ignores process uncertainty would provide an incomplete picture of the reserve estimate's sensitivity. Since a reserve estimate's standard error accounts for both process and parameter uncertainty, it reflects the estimate's full sensitivity to a range of reasonably likely scenarios.

The table below provides standard errors and reserve ranges for lines of business that account for 91.6 percent of our loss and loss expense reserves as well as the potential effects on our net income assuming a 35 percent federal tax rate. Standard errors and reserve ranges for assorted groupings of these lines of business cannot be computed by simply adding the standard errors and reserve ranges of the component lines of business, since such an approach would ignore the effects of product diversification. See Range of Reasonable Reserves below for a total reserve range. While the table reflects our assessment of the most likely range within which each line's actual unpaid loss and loss expenses will fall, one or more lines' actual unpaid loss and loss expenses could nonetheless fall outside of the indicated ranges.

(In millions)	Net loss and loss expense range of reserves					Net income effect
	Carried reserves	Low point	High point	Standard error		
<b>At December 31, 2007</b>						
Commercial casualty	\$ 1,565	\$ 1,352	\$ 1,634	\$ 141	\$ 92	
Commercial property	121	104	136	16	10	
Commercial auto	383	362	395	17	11	
Workers' compensation	777	726	786	30	20	
Personal auto	189	173	191	9	6	
Homeowners	77	75	88	7	5	
<b>At December 31, 2006</b>						
Commercial casualty	\$ 1,483	\$ 1,269	\$ 1,542	\$ 136	\$ 88	
Commercial property	170	155	181	13	8	
Commercial auto	386	374	387	6	4	
Workers' compensation	713	665	724	30	20	
Personal auto	206	193	203	5	3	
Homeowners	104	100	108	4	3	

If actual unpaid loss and loss expenses fall within these ranges, our cash flow and fixed maturity investments should provide sufficient liquidity to make the subsequent payments. To date, our cash flow has covered our loss and loss expense payments, and we have never had to sell investments to make these payments. If this were to become necessary, however, our fixed maturity investments should provide us with ample liquidity. At year-end 2007, fixed maturity investments exceeded total insurance reserves (including life policy reserves) by more than \$400 million.

## **LIFE INSURANCE POLICY RESERVES**

We establish the reserves for traditional life insurance policies based on expected expenses, mortality, morbidity, withdrawal rates 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. We use our own experience and historical trends for setting our assumptions for expected expenses. We base our assumptions for expected investment income on our own experience adjusted for current economic conditions.

We establish reserves for our universal life, deferred annuity and investment contracts equal to the cumulative account balances, which include premium deposits plus credited interest less charges and withdrawals. Some of our universal life insurance 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.

## **ASSET IMPAIRMENT**

Our fixed-maturity and equity investment portfolios are our largest assets. The company's asset impairment committee continually monitors the holdings in these portfolios and all other assets for signs of other-than-temporary or permanent impairment. The committee monitors significant decreases in the market value of invested assets, changes in legal factors or in the business climate, an accumulation of costs in excess of the amount originally expected to acquire or construct an asset, uncollectability of all receivable assets, or other factors such as bankruptcy, deterioration of creditworthiness, failure to pay interest or dividends or signs indicating that the carrying amount may not be recoverable.

The application of our impairment policy resulted in other-than-temporary impairment charges and realized investment losses that reduced our income before income taxes by \$16 million in 2007 and \$1 million in both 2006 and 2005.

Our portfolio managers monitor the status of their assigned portfolios for indications of potential problems that may be possible impairment issues. If a security is trading below book value, the portfolio managers undertake additional reviews. Such declines often occur in conjunction with events taking place in the overall economy and market, combined with events specific to the industry or operations of the issuing organization.

Management reviews quantitative measurements such as a declining trend in market value, the extent of the market value decline and the length of time the value of the security has been depressed, as well as qualitative measures such as pending events and issuer liquidity. Generally, these declines in valuation are greater than might be anticipated when viewed in the context of overall economic and market conditions. We provide information regarding valuation of our invested assets in Item 8, Note 2 of the Consolidated Financial Statements, Page 93.

Impairment charges are recorded for other-than-temporary declines in value, if, in the asset impairment committee's judgment, there is little expectation that the value will be recouped in the foreseeable future. A security valued between 95 percent and 100 percent of book value will not be monitored separately by the committee. These assets generally are at this value because of interest rate-driven factors. All securities valued below 95 percent of book value are reported to the asset impairment committee for evaluation.

When evaluating for other-than-temporary impairments, the committee considers the company's intent and ability to retain a security for a period adequate to recover its cost. Because of the company's strong capitalization, management may not impair certain securities even though they are trading below cost. The company can make that determination based on its ability to hold until their scheduled redemption securities that have the potential to recover value. In addition to evaluating the security's current valuation, the impairment committee reviews objective evidence that indicates the potential for a recovery in value. Information is evaluated regarding the security, such as financial performance, near-term prospects and the financial condition of the region and industry in which the issuer operates.

Securities that have previously been impaired are evaluated based on their adjusted book value and written down further, if deemed appropriate. The decision to sell or write down a security with impairment indications reflects, at least in part, management's opinion that the security no longer meets the company's investment objectives. We provide detailed information about securities trading in a continuous loss position at year-end 2007 in Item 7A, Unrealized Investment Gains and Losses, Page 77. An other-than-temporary decline in the fair value of a security is recognized in net income as realized investment losses.



Permanent impairment charges (write-offs) are defined as those for which management believes there is little potential for future recovery, for example, following the bankruptcy of the issuer. A permanent decline in the fair value of a security is written off at the time when facts and circumstances indicate such write-down is warranted, and is reflected in realized investment losses.

Other-than-temporary and permanent impairments are distinct from the ordinary fluctuations seen in the value of a security when considered in the context of overall economic and market conditions. Securities considered to have a temporary decline would be expected to recover their market value, which may be at maturity. Under the same accounting treatment as market value gains, temporary declines (changes in the fair value of these securities) are reflected on our balance sheet in accumulated other comprehensive income, net of tax, and have no impact on reported net income.

## **EMPLOYEE BENEFIT PENSION PLAN**

We have a defined benefit pension plan covering substantially all employees. Contributions and pension costs are developed from annual actuarial valuations. These valuations involve key assumptions including discount rates and expected return on plan assets, which are updated each year. Any adjustments to these assumptions are based on considerations of current market conditions. Therefore, changes in the related pension costs or credits may occur in the future due to changes in assumptions.

Key assumptions used in developing the 2007 net pension obligation were a 6.25 percent discount rate and rates of compensation increases ranging from 4 percent to 6 percent. Key assumptions used in developing the 2007 net pension expense were a 5.75 percent discount rate, an 8 percent expected return on plan assets and rates of compensation increases ranging from 4 percent to 6 percent.

In 2007, the net pension expense was \$21 million. In 2008, we expect a net pension expense of \$19 million, primarily as a result of reduced service costs due to a 0.5 percentage point increase in the discount rate.

Holding all other assumptions constant, a 0.5 percentage point decline in the discount rate would lower our 2008 net income before income taxes by \$2 million. Likewise, a 0.5 percentage point decline in the expected return on plan assets would lower our 2008 income before income taxes by \$1 million.

The fair value of the plan assets exceeded the accumulated benefit obligation by \$9 million at year-end 2007 and \$8 million at year-end 2006. The fair value of the plan assets was less than the projected plan benefit obligation by \$54 million at year-end 2007 and \$58 million at year-end 2006. Market conditions and interest rates significantly affect future assets and liabilities of the pension plan.

## **DEFERRED ACQUISITION COSTS**

We establish a deferred asset for costs that vary with, and are primarily related to, acquiring property casualty and life insurance business. These costs are principally agent commissions, premium taxes and certain underwriting costs, which are deferred and amortized into income as premiums are earned. Deferred acquisition costs track with the change in premiums. Underlying assumptions are updated periodically to reflect actual experience. Changes in the amounts or timing of estimated future profits could result in adjustments to the accumulated amortization of these costs.

For property casualty policies, deferred acquisition costs are amortized over the terms of the policies. For life policies, acquisition costs are amortized into income either over the premium-paying period of the policies or the life of the policy, depending on the policy type.

## **CONTINGENT COMMISSION ACCRUAL**

Another significant estimate relates to our accrual for property casualty contingent (profit-sharing) commissions. We base the contingent commission accrual estimates on property casualty underwriting results and on supplemental information. Contingent commissions are paid to agencies using a formula that takes into account agency profitability, premium volume and other factors, such as prompt monthly payment of amounts due to the company. Due to the complexity of the calculation and the variety of factors that can affect contingent commissions for an individual agency, the amount accrued can differ from the actual contingent commissions paid. The contingent commission accrual of \$102 million in 2007 contributed 3.3 percentage points to the property casualty combined ratio. If contingent commissions paid were to vary from that amount by 5 percent, it would affect 2008 net income by \$3 million (after tax), or 2 cents per share, and the combined ratio by approximately 0.2 percentage points.

## **SEPARATE ACCOUNTS**

We issue life contracts, referred to as bank-owned life insurance policies (BOLI). Based on the specific contract provisions, the assets and liabilities for some BOLIs are legally segregated and recorded as assets and liabilities of the separate accounts. Other BOLIs are included in the general account. For separate account BOLIs, minimum investment returns and account values are guaranteed by the company and also include death benefits to beneficiaries of the contract holders.

Separate account assets are carried at fair value. Separate account liabilities primarily represent the contract holders' claims to the related assets and also are carried at the fair value of the assets. Generally, investment income and realized investment gains and losses of the separate accounts accrue directly to the contract holders and, therefore, are not included in our Consolidated Statements of Income. However, each separate account contract includes a negotiated realized gain and loss sharing arrangement with the company. This share is transferred from the separate account to our general account and is recognized as revenue or expense. In the event that the asset value of contract holders' accounts is projected below the value guaranteed by the company, a liability is established through a charge to our earnings.

For our most significant separate account, written in 1999, realized gains and losses are retained in the separate account and are deferred and amortized to the contract holder over a five-year period, subject to certain limitations. Upon termination or maturity of this separate account contract, any unamortized deferred gains and/or losses will revert to the general account. In the event this separate account holder were to exchange the contract for the policy of another carrier in 2008, the account holder would pay a surrender charge equal to 2 percent of the contract's account value. The surrender charge will fall to 1 percent in 2009 and 0 percent in 2010 and beyond.

At year-end 2007, net unamortized realized gains amounted to \$1 million. In accordance with this separate account agreement, the investment assets must meet certain criteria established by the regulatory authorities to whose jurisdiction the group contract holder is subject. Therefore, sales of investments may be mandated to maintain compliance with these regulations, possibly requiring gains or losses to be recorded, and charged to the general account. Potentially, losses could be material; however, unrealized losses in the separate account portfolio were less than \$6 million at year-end 2007.

## RECENT ACCOUNTING PRONOUNCEMENTS

Information regarding recent accounting pronouncements is provided in Item 8, Note 1 of the Consolidated Financial Statements, Page 87. We have determined that recent accounting pronouncements have not had nor are they expected to have any material impact on our consolidated financial statements.

## RESULTS OF OPERATIONS

The consolidated results of operations reflect the operating results of each of our four segments along with the parent company and other non-insurance activities. The four segments are:

- Commercial lines property casualty insurance
- Personal lines property casualty insurance
- Life insurance
- Investments operations

We measure profit or loss for our property casualty and life segments based upon underwriting results (profit or loss), which represent net earned premium less loss and loss expenses and underwriting expenses on a pretax basis. We also frequently evaluate results for our consolidated property casualty insurance operations, which is the total of our commercial lines and personal lines insurance segments. Our consolidated property casualty insurance operations generated an unusually low percent of our total revenues in 2007 and 2006 due to sales of investment assets, which are included in the investments segment results. Underwriting results and segment pretax operating income are not substitutes for net income determined in accordance with GAAP.

For our consolidated property casualty insurance operations as well as the commercial lines and personal lines segments, statutory accounting data and ratios are key performance indicators that we use to assess business trends and to make comparisons to industry results, since GAAP-based industry data generally is not as readily available. We also use statutory accounting data and ratios as key performance indicators for our life insurance operations.

Investments held by the parent company and the investment portfolios for the property casualty and life insurance subsidiaries are managed and reported as the investments segment, separate from the underwriting businesses. Net investment income and net realized investment gains and losses for our investment portfolios are discussed in the Investments Results of Operations.

The calculations of segment data are described in more detail in Item 8, Note 17 of the Consolidated Financial Statements, Page 96. The following sections review results of operations for each of the four segments. Commercial Lines Insurance Results of Operations begins on Page 44, Personal Lines Insurance Results of Operations begins on Page 51, Life Insurance Results of Operations begins on Page 56, and Investments Results of Operations begins on Page 57. We begin with an overview of our consolidated property casualty operations, which is the total of our commercial lines and personal lines segments.

## CONSOLIDATED PROPERTY CASUALTY INSURANCE RESULTS OF OPERATIONS

(Dollars in millions)	Years ended December 31,			2007-2006	2006-2005
	2007	2006	2005	Change %	Change %
Written premiums	\$ <u>3,117</u>	\$ <u>3,178</u>	\$ <u>3,076</u>	(1.9)	3.3
Earned premiums	\$ 3,125	\$ 3,164	\$ 3,058	(1.2)	3.5
Loss and loss expenses excluding catastrophes	1,806	1,833	1,685	(1.5)	8.8
Catastrophe loss and loss expenses	26	175	127	(85.1)	37.9
Commission expenses	599	596	592	0.4	0.7
Underwriting expenses	375	363	319	3.2	13.9
Policyholder dividends	15	16	5	(5.4)	208.1
Underwriting profit	\$ <u>304</u>	\$ <u>181</u>	\$ <u>330</u>	68.3	(45.2)
Ratios as a percent of earned premiums:					
Loss and loss expenses excluding catastrophes	57.8 %	58.0 %	55.1 %		
Catastrophe loss and loss expenses	<u>0.8</u>	<u>5.5</u>	<u>4.1</u>		
Loss and loss expenses	58.6	63.5	59.2		
Commission expenses	19.2	18.8	19.4		
Underwriting expenses	12.0	11.5	10.4		
Policyholder dividends	<u>0.5</u>	<u>0.5</u>	<u>0.2</u>		
Combined ratio	<u>90.3 %</u>	<u>94.3 %</u>	<u>89.2 %</u>		

In addition to the factors discussed in Commercial Lines and Personal Lines Insurance Results of Operations, Page 44 and Page 51, growth and profitability for our consolidated property casualty insurance operations were affected by:

- Changes in written and earned premiums over the past three years, reflecting growing price competition partially offset by consistently high retention rates. New business written directly by agencies was \$325 million, \$357 million and \$314 million in 2007, 2006 and 2005, respectively. New business levels reflected market conditions for commercial and personal lines as well as the advantages of our agency relationship strategy.
- Savings from favorable development on prior period reserves improved the combined ratio by 7.7 percentage points in 2007 compared with 3.7 and 5.2 percentage points in 2006 and 2005. These amounts include development on prior period catastrophe loss reserves as discussed below.
- The adoption of stock option expensing added approximately 0.5 percentage points to the 2007 and 2006 combined ratios.
- Non-catastrophe weather-related losses – Approximately 1 percentage point of the increase in the 2007 accident year loss and loss expense ratio was due to higher losses from weather events not deemed to be catastrophes, including a few unusually large losses.
- Catastrophe losses contributed 0.8 percentage points to the combined ratio in 2007, the lowest catastrophe loss ratio for our company since 1991. The ratio compared with 5.5 percentage points in 2006 and 4.1 percentage points in 2005. The following table shows catastrophe losses incurred, net of reinsurance, for the past three years as well as the effect of loss development on prior period catastrophe events. Our 2005 Hurricane Katrina and Rita losses included significant losses associated with commercial accounts with operations extending into states where we do not actively market, as well as losses under three assumed reinsurance treaties.

## Catastrophe Losses Incurred

(In millions, net of reinsurance)

Dates	Cause of loss	Region	Years ended December 31,		
			Commercial lines	Personal lines	Total
<b>2007</b>					
Mar. 1-2	Wind, hail, flood	South	\$ 6	\$ 2	\$ 8
Jun. 7-9	Wind, hail, flood	Midwest	4	5	9
Sep. 20-21	Wind, hail, flood	Midwest	2	4	6
Other 2007 catastrophes			14	9	23
Development on 2006 and prior catastrophes			(10)	(10)	(20)
Calendar year incurred total			<u>\$ 16</u>	<u>\$ 10</u>	<u>\$ 26</u>
<b>2006</b>					
Mar. 11-13	Wind, hail	Midwest, Mid-Atlantic	\$ 29	\$ 8	\$ 37
Apr. 2-3	Wind, hail	Midwest	12	5	17
Apr. 6-8	Wind, hail	South	13	24	37
Apr. 13-15	Wind, hail	South	4	6	10
Jun. 18-22	Wind, hail, flood	South	3	2	5
Jul. 19-21	Wind, hail, flood	South	4	1	5
Aug. 23-25	Wind, hail, flood	Midwest	5	2	7
Oct. 2-4	Wind, hail, flood	Midwest	7	31	38
Nov. 30-Dec. 3	Wind, hail, ice, snow	Midwest, South	4	4	8
Other 2006 catastrophes			7	3	10
Development on 2005 and prior catastrophes			1	0	1
Calendar year incurred total			<u>\$ 89</u>	<u>\$ 86</u>	<u>\$ 175</u>
<b>2005</b>					
Jan. 4-6	Wind, ice, snow	Midwest, Mid-Atlantic	\$ 0	\$ 1	\$ 1
May 6-12	Wind, hail	Midwest	4	8	12
Jul. 9-11	Hurricane Dennis	South	5	2	7
Aug. 25-26	Hurricane Katrina	South	36	11	47
Sep. 20-24	Hurricane Rita	South	3	0	3
Oct. 24	Hurricane Wilma	South	13	12	25
Nov. 6	Wind, hail	Midwest	2	9	11
Nov. 15-16	Wind	Midwest, South	2	10	12
Other 2005 catastrophes			0	0	0
Development on 2004 and prior catastrophes			11	(2)	9
Calendar year incurred total			<u>\$ 76</u>	<u>\$ 51</u>	<u>\$ 127</u>

The discussions of our property casualty insurance segments provide additional detail regarding these factors.

## COMMERCIAL LINES INSURANCE RESULTS OF OPERATIONS

### Overview – Three-year Highlights

Performance highlights for the commercial lines segment include:

- **Premiums** – As competition in our commercial markets continued to increase, our 2007 commercial lines written premiums declined slightly. Softer pricing offset the benefits of our strong agency relationships, healthy policy retention rates, accurate risk classification, and insurance-to-value initiatives. We continue to make deliberate decisions not to write or renew certain business. In this pricing environment we have been careful to maintain our underwriting discipline for both renewal and new business. We believe that our written premium growth rate compares satisfactorily with the average for the overall commercial lines industry, which was estimated to decline 1.5 percent in 2007, after rising 3.5 percent in 2006 and declining 0.4 percent in 2005. Earned premiums remained relatively steady over the period.
- **Combined ratio** – Our commercial lines combined ratio was a strong 89.2 percent in 2007. This was better than the 91.3 percent reported in 2006 but higher than the 87.4 percent reported in 2005. The 2007 ratio reflected higher current accident year losses excluding catastrophe losses and higher underwriting expenses. These were more than offset by lower catastrophe losses and higher savings from favorable development on prior period reserves. We continue to focus on sound underwriting fundamentals and seek to obtain adequate premiums per policy. We discuss factors affecting the combined ratio and savings from favorable reserve development by commercial line of business below.

Our commercial lines statutory combined ratio was 89.2 percent in 2007 compared with 90.8 percent in 2006 and 87.1 percent in 2005. By comparison, the estimated industry commercial lines combined ratio was 94.0 percent in 2007, 91.2 percent in 2006 and 99.7 percent in 2005. We believe our results trended differently than the overall industry in part because the industry experienced unusually high catastrophe losses in 2005 and unusually low catastrophe losses in 2006.

## Commercial Lines Results

(Dollars in millions)	Years ended December 31,			2007-2006	2006-2005
	2007	2006	2005	Change %	Change %
Written premiums	\$ <u>2,413</u>	\$ <u>2,442</u>	\$ <u>2,290</u>	(1.2)	6.7
Earned premiums	\$ 2,411	\$ 2,402	\$ 2,254	0.4	6.6
Loss and loss expenses excluding catastrophes	1,378	1,377	1,222	0.1	12.7
Catastrophe loss and loss expenses	16	89	76	(81.3)	16.6
Commission expenses	454	444	438	2.0	1.4
Underwriting expenses	287	268	228	7.0	17.8
Policyholder dividends	15	16	5	(5.4)	208.1
Underwriting profit	\$ <u>261</u>	\$ <u>208</u>	\$ <u>285</u>	25.4	(27.0)
Ratios as a percent of earned premiums:					
Loss and loss expenses excluding catastrophes	57.2 %	57.3 %	54.2 %		
Catastrophe loss and loss expenses	<u>0.7</u>	<u>3.7</u>	<u>3.4</u>		
Loss and loss expenses	57.9	61.0	57.6		
Commission expenses	18.8	18.5	19.5		
Underwriting expenses	11.9	11.1	10.1		
Policyholder dividends	0.6	0.7	0.2		
Combined ratio	<u>89.2 %</u>	<u>91.3 %</u>	<u>87.4 %</u>		

### Growth and Profitability

As the commercial markets have grown more competitive over the past several years, we have focused on leveraging our local relationships and the efforts of our agents and the teams that work with them. We believe that we are maintaining appropriate pricing discipline for both new and renewal business as we emphasize the importance of assessing account quality to our agencies and underwriters.

For new business, our field associates are in our agents' offices helping to judge the quality of each account, emphasizing the Cincinnati value proposition, calling on prospects with those agents, carefully evaluating risk exposure and working up their best quotes. At year-end 2007, our field marketing representatives reported pricing down about 15 percent to 20 percent on average to write the same piece of new quality business we would have quoted in 2006, the second consecutive year of significant declines in our new business pricing. We believe this reflects the importance carriers are placing on protecting their renewal portfolios.

For renewal business, our headquarters underwriters talk regularly with agents. Our field teams are available to assist the headquarters underwriters by conducting inspections and holding renewal review meetings with agency staff. These activities can help verify that a commercial account retains the characteristics that caused us to write the business initially. For quality risks, our commercial underwriters are offering policyholders the convenience of policy extensions of one and two additional years.

In these conditions, we have needed to use credits more frequently to retain renewals of quality business – the larger the account, the higher the credits, with variations by geographic region and class of business. At year-end 2007, rate declines of 4 percent to 6 percent seemed typical for our renewal business.

We intend to remain a stable market for our agencies' best business and believe that our case-by-case approach gives us a clear advantage. Our independent agents, field marketing representatives and headquarters underwriters work together to select risks and respond appropriately to local pricing trends. Historically, they have proven capable of balancing risk and price to achieve profitable growth over the longer term.

Staying abreast of evolving market conditions is a critical function, accomplished in both an informal and a formal manner. Informally, our field marketing representatives and underwriters are in constant receipt of market intelligence from the agencies with which they work. Formally, our commercial lines product management group and field marketing associates conduct periodic surveys to obtain competitive intelligence. This market information helps identify the top competitors by line of business or specialty program and also identifies our market strengths and weaknesses. The analysis encompasses pricing, breadth of coverage and underwriting/eligibility issues.

In addition to reviewing our competitive position, our product management group and our underwriting audit group review compliance with our underwriting standards as well as the pricing adequacy of our commercial insurance programs and coverages. Further, our research and development department analyzes opportunities and develops new products, new coverage options and improvements to existing insurance products.

In 2007, competition in our markets continued to intensify, and we view this as the most significant factor in the 1.2 percent decline in commercial lines written premiums. Our largest four commercial lines of business reported lower written premiums, led by commercial auto, which is one of the first lines to experience pricing pressure because it often represents the largest portion of insurance costs for many commercial policyholders. In this environment, we will continue to work with our agents to identify quality risks, lower prices to keep our

best accounts and help our agencies protect their accounts from competition. Agency emphasis on larger accounts, convenience and technology considerations were the primary reasons for a slight decline in the number of our smallest policies.

Other factors contributing to the year-over-year premium differences include the economic slowdown in many regions and higher reinsurance premiums. For commercial accounts, we typically calculate general liability premiums based on sales or payroll volume while we calculate workers' compensation premiums based on payroll volume. A change in sales or payroll volume generally indicates a change in a business's exposure to risk.

Economic factors, such as the housing market slowdown, can cause demand for our policyholders' business services to rise or fall. Changes in demand may cause our policyholders' sales and payroll volumes to fluctuate. Those fluctuations can have a modest effect on our premium trends. Policyholders that experience sales or payroll volume changes due to economic factors may be purchasers of other types of insurance, such as commercial auto or commercial property, in addition to general liability and workers' compensation. Premium levels for these other types of policies generally are not linked directly to sales or payroll volumes. In 2007, we estimated that policyholders with a contractor-related ISO general liability code accounted for approximately 43 percent of our general liability premiums, which are included in the commercial casualty line of business, and that policyholders with a contractor-related NCCI workers' compensation code accounted for approximately 46 percent of our workers' compensation premiums.

In 2006, strong new business activity, steady policy retention rates and higher premiums per policy led to net written premium growth in all of our commercial lines of business, with commercial auto showing the slowest rate of growth.

Primarily because of the heightened competition, new commercial lines business written directly by agencies declined 11.5 percent to \$287 million in 2007 after rising 14.9 percent to a record \$324 million in 2006.

We discuss growth by commercial line of business below. Over the past three years, we continued to focus on seeking and maintaining adequate premium per exposure as well as pursuing non-pricing means of enhancing longer-term profitability. Non-pricing means have included deliberate reviews of each risk, seeking to ensure that we identified relevant exposures and offered appropriate coverages, terms and conditions and limits of insurance. We continue to adhere to our underwriting guidelines, to re-underwrite books of business with selected agencies and to update policy terms and conditions, where necessary. In addition, we continue to leverage our strong local presence. Our field marketing representatives meet with local agencies to reaffirm agreements on the extent of frontline renewal underwriting agents will perform. Loss control, machinery and equipment and field claims representatives continue to conduct on-site inspections. Field claims representatives prepare full risk reports on any account reporting a loss above \$100,000 or on any risk of concern.

We describe the significant cost components for the commercial lines segment below.

### **Loss and Loss Expenses (excluding catastrophe losses)**

Loss and loss expenses include both net paid losses and reserve changes for unpaid losses as well as the associated loss expenses. The trend in the loss and loss expense ratio excluding catastrophe losses over the past three years reflected competitive market conditions and softer pricing that began in 2005 and continued through 2007, as discussed above. This resulted in a steady increase in the accident year loss and loss expense ratio excluding catastrophe losses to 65.2 percent in 2007 from 61.4 percent in 2006 and 60.3 percent in 2005.

Savings from favorable development on prior period reserves reduced the ratio by 8.4, 4.1 and 5.6 percentage points in 2007, 2006 and 2005, respectively. Particularly for our longer-tail lines, our ultimate loss ratio estimates continue to show the benefits of re-classification and re-pricing initiatives undertaken early in this decade. During the same period, we also made changes to our policy terms, conditions and coverages, to help manage limits or exposures. Further, we also continue to see positive payment and reporting pattern changes, attributable to the implementation of a claims management system and to the use of a claims mediation process that promotes earlier liability settlement resolution.

The rise in the loss and loss expense ratio included a higher contribution from new losses and case reserve increases greater than \$250,000. In total, commercial lines new losses and reserve increases greater than \$250,000 rose to 23.3 percent of earned premium from 21.3 percent in 2006 and 16.8 percent in 2005. Our analysis indicated no unexpected concentration of these losses and reserve increases by risk category, geographic region, policy inception, agency or field marketing territory. We believe the increase was due to a number of factors, including changes in retention levels for our per risk reinsurance programs, case reserve practices for our workers' compensation business line, natural volatility and general inflationary trends in loss costs, which we continue to monitor. A single large loss in 2005 was insufficiently covered through our facultative reinsurance programs, which increased that year's loss and loss expenses by \$22 million, net of reinsurance, or 1.0 percentage points.

## Commercial Lines Losses by Size

(Dollars in millions)	Years ended December 31,			2007-2006	2006-2005
	2007	2006	2005	Change %	Change %
New losses greater than \$4,000,000	\$ 4	\$ 0	\$ 23	0.0	nm
New losses \$2,000,000-\$4,000,000	111	111	34	0.3	225.8
New losses \$1,000,000-\$2,000,000	90	67	60	34.2	11.2
New losses \$750,000-\$1,000,000	33	28	20	18.8	36.7
New losses \$500,000-\$750,000	48	40	32	20.9	22.9
New losses \$250,000-\$500,000	74	64	59	14.1	7.5
Case reserve development above \$250,000	201	201	150	0.3	33.9
Total large losses incurred	<u>561</u>	<u>511</u>	<u>378</u>	10.0	34.3
Other losses excluding catastrophes	502	562	596	(10.6)	(5.7)
Catastrophe losses	16	89	76	(82.3)	16.6
Total losses incurred	<u>\$ 1,079</u>	<u>\$ 1,162</u>	<u>\$ 1,050</u>	(7.0)	10.7
Ratios as a percent of earned premiums:					
New losses greater than \$4,000,000	0.2 %	0.0 %	1.1 %		
New losses \$2,000,000-\$4,000,000	4.6	4.6	1.5		
New losses \$1,000,000-\$2,000,000	3.7	2.8	2.7		
New losses \$750,000-\$1,000,000	1.4	1.2	0.9		
New losses \$500,000-\$750,000	2.0	1.7	1.4		
New losses \$250,000-\$500,000	3.0	2.7	2.6		
Case reserve development above \$250,000	8.4	8.3	6.6		
Total large loss ratio	<u>23.3</u>	<u>21.3</u>	<u>16.8</u>		
Other losses excluding catastrophes	20.8	23.4	26.4		
Catastrophe losses	0.7	3.7	3.4		
Total loss ratio	<u>44.8 %</u>	<u>48.4 %</u>	<u>46.6 %</u>		

### Catastrophe Loss and Loss Expenses

Commercial lines catastrophe losses added just 0.7 percentage points to the loss and loss expense ratio in 2007, down from the significantly higher levels of the prior two years.

### Commission Expenses

Commercial lines commission expense as a percent of earned premium was relatively stable in 2007 after declining by 1.0 percentage points in 2006. Commission expenses include our profit-sharing, or contingent, commissions, which are calculated on the profitability of an agency's aggregate property casualty book of Cincinnati business, taking into account longer-term profit and premium volume, with a percentage for prompt payment of premiums and other criteria, and reward the agency's effort. These profit-based commissions generally fluctuate with our loss and loss expense ratio. Our 2007 contingent commission accrual reflected our estimate of the profit-sharing commissions to be paid to our agencies in early 2008 based largely on each agency's performance in 2007.

### Underwriting Expenses

Non-commission underwriting expenses rose to 11.9 percent of earned premiums in 2007 from 11.1 percent in 2006 and 10.1 percent in 2005. In 2007, slower earned premium growth led to an unfavorable deferred acquisition expense comparison. Further, our excess and surplus lines start-up activities contributed slightly to higher staffing and technology expenses. Reallocation of expenses between our commercial lines and personal lines segments as we refined our data also contributed to the increase in non-commission underwriting expenses. In 2006, higher technology and staffing expenses contributed 1.2 percentage points to the increase, with stock option expense accounting for 0.5 percentage points of that amount. These increases were offset partially by savings in taxes, licenses and fees.

### Policyholder Dividends

Policyholder dividend expense was 0.6 percent of earned premium in 2007 compared with 0.7 percent in 2006 and 0.2 percent in 2005.

### Line 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 the commercial lines segment is best measured and evaluated on a segment basis. However, we provide line of business data to summarize growth and profitability trends separately for each line. The accompanying accident year loss data provides current estimates of incurred loss and loss expenses and corresponding ratios over the most recent three accident years. Accident year data classifies losses according to the year in which the corresponding loss event occurs, regardless of when the losses are actually reported, recorded or paid.

## Commercial Casualty

(Dollars in millions)	Years ended December 31,			2007-2006	2006-2005	
	2007	2006	2005	Change %	Change %	
<b>Commercial casualty:</b>						
Written premiums	\$ 830	\$ 838	\$ 779	(1.0)	7.7	
Earned premiums	827	831	759	(0.5)	9.5	
Loss and loss expenses incurred	423	440	302	(4.0)	45.8	
Loss and loss expense ratio	51.1 %	53.0 %	39.8 %			
Loss and loss expense ratio excluding catastrophes	51.1	53.0	39.8			
Reserve development impact on loss and loss expense ratio	(18.1)	(12.0)	(22.5)			
Accident year loss and loss expenses incurred and ratios to earned premiums:						
Accident year:	2007	2006	2005	2007	2006	2005
as of December 31, 2007	\$ 572	\$ 469	\$ 398	69.2 %	56.4 %	52.5 %
as of December 31, 2006		540	420		64.9	55.4
as of December 31, 2005			473			62.3

Commercial casualty is our largest business line. Commercial casualty net written premiums declined slightly in 2007 as competition intensified in the casualty market. In addition, premiums for this business line can reflect economic trends, including changes in underlying exposures.

The commercial casualty loss and loss expense ratio improved slightly in 2007 after rising in 2006 and remains within the range we consider appropriate. In each of the last three calendar years, the level of favorable development on prior period reserves has been the primary reason for the fluctuations in the loss and loss expense ratio. Factors contributing to the level of favorable development are discussed in Commercial Lines Insurance Segment Reserves, Page 67. In addition to the level of favorable development, the ratio was affected by the substantial rise in 2007 and 2006 of the level of \$1 million plus general liability losses compared with the level in 2005. These large losses contributed 6.9 percentage points to the loss and loss expense ratio in 2007, 5.9 percentage points in 2006 and 2.4 percentage points in 2005.

Pricing and normal loss cost inflation accounted for a portion of the deterioration in the accident year loss ratio over the three-year period. In addition, the commercial casualty business line includes some of our longest tail exposures, making initial estimates of accident year loss and loss expenses incurred more uncertain, as we discuss in Critical Accounting Estimates, Property Casualty Insurance Loss and Loss Expense Reserves, Page 37.

## Commercial Property

(Dollars in millions)	Years ended December 31,			2007-2006	2006-2005	
	2007	2006	2005	Change %	Change %	
<b>Commercial property:</b>						
Written premiums	\$ 499	\$ 505	\$ 476	(1.1)	6.1	
Earned premiums	497	491	467	1.2	5.1	
Loss and loss expenses incurred	241	282	300	(14.6)	(5.9)	
Loss and loss expense ratio	48.5 %	57.5 %	64.2 %			
Loss and loss expense ratio excluding catastrophes	46.3	43.6	49.3			
Reserve development impact on loss and loss expense ratio	(3.9)	0.9	3.5			
Accident year loss and loss expenses incurred and ratios to earned premiums:						
Accident year:	2007	2006	2005	2007	2006	2005
as of December 31, 2007	\$ 260	\$ 274	\$ 287	52.4 %	55.7 %	61.4 %
as of December 31, 2006		278	300		56.6	64.2
as of December 31, 2005			283			60.7

Commercial property is our second largest business line. Commercial property net written premiums declined slightly in 2007 in part due to higher reinsurance premiums. The 2006 growth rate benefited by 1.2 percentage points due to the effect of a \$5 million reinsurance reinstatement premium included in 2005 premiums.

The commercial property loss and loss expense ratio excluding catastrophe losses deteriorated in 2007 after improving in 2006. The rise in 2007 reflected the growing impact of softer pricing on our commercial property business line. The improvement in the ratio in 2006 largely was due to the large loss discussed above that added 5.0 percentage points to the 2005 ratio.

Lower catastrophe losses were the primary factor in the decline in the accident year loss ratio over the three-year period.



## Commercial Auto

(Dollars in millions)	Years ended December 31,			2007-2006	2006-2005	
	2007	2006	2005	Change %	Change %	
<b>Commercial auto:</b>						
Written premiums	\$ 429	\$ 450	\$ 448	(4.7)	0.3	
Earned premiums	440	453	457	(2.9)	(0.9)	
Loss and loss expenses incurred	278	278	274	0.2	1.5	
Loss and loss expense ratio	63.5 %	61.5 %	60.1 %			
Loss and loss expense ratio excluding catastrophes	63.5	60.6	60.0			
Reserve development impact on loss and loss expense ratio	(5.8)	(4.6)	(5.0)			
Accident year loss and loss expenses incurred and ratios to earned premiums:						
Accident year:	2007	2006	2005	2007	2006	2005
as of December 31, 2007	\$ 304	\$ 284	\$ 274	69.3 %	62.7 %	60.1 %
as of December 31, 2006		300	281		66.1	61.4
as of December 31, 2005			298			65.1

The decline in commercial auto 2007 written premiums reflected the downward pressure exerted by the market on the pricing of commercial accounts. Commercial auto is one of the business lines that we renew and price annually, so market trends may be reflected here more quickly than in other lines. Commercial auto also is generally one of the larger components of the typical package.

The commercial auto loss and loss expense ratio remained within the range we consider appropriate despite the increasing pricing pressures. New losses greater than \$1 million contributed 16.5 percentage points to the loss and loss expense ratio in 2007, 11.5 percentage points in 2006 and 8.5 percentage points in 2005. We believe the higher number of commercial auto losses greater than \$1 million was due to natural volatility and general inflationary trends in loss costs.

Pricing and normal loss cost inflation were the primary drivers of the deterioration in the accident year loss ratio over the past three years. In each calendar year, the loss and loss expense ratio reflected an increase in the accident-year loss and loss expense ratio that was moderated by favorable development on prior period reserves, a benefit of past re-underwriting efforts, Ohio judicial decisions regarding underinsured/uninsured motorist claims and a favorable frequency trend.

## Workers' Compensation

(Dollars in millions)	Years ended December 31,			2007-2006	2006-2005	
	2007	2006	2005	Change %	Change %	
<b>Workers' compensation:</b>						
Written premiums	\$ 378	\$ 379	\$ 338	(0.3)	12.1	
Earned premiums	373	366	328	1.9	11.4	
Loss and loss expenses incurred	316	313	299	1.0	4.7	
Loss and loss expense ratio	84.6 %	85.4 %	90.9 %			
Loss and loss expense ratio excluding catastrophes	84.6	85.4	90.9			
Reserve development impact on loss and loss expense ratio	(2.7)	2.6	12.9			
Accident year loss and loss expenses incurred and ratios to earned premiums:						
Accident year:	2007	2006	2005	2007	2006	2005
as of December 31, 2007	\$ 326	\$ 284	\$ 254	87.3 %	77.6 %	77.3 %
as of December 31, 2006		300	254		82.8	77.4
as of December 31, 2005			256			78.1

In 2007, workers' compensation written premiums were essentially unchanged after rising significantly in 2006. Workers' compensation premiums partially reflect the general business economy and related payroll levels. Premiums also benefited from initiatives to modestly expand our workers' compensation business in selected states. We cannot offer workers' compensation coverage in Ohio, our highest total property casualty premium volume state, because it is provided solely by the state instead of private insurers.

In 2005, the workers' compensation loss and loss expense ratio rose to 90.9 percent after remaining steady for several years. The 2005 rise largely was due to reserve strengthening on incurred but not reported claims for older accident years to reflect higher trends in medical cost inflation and longer estimated payout periods than originally projected. Since we pay a lower commission rate on workers' compensation business, this line has a higher loss and loss expense breakeven point than our other commercial business lines. Nonetheless, the ratio remained above our target level over the three-year period.

In 2006, we also reviewed each of our established workers' compensation case reserves above \$100,000 in light of current trends in medical cost inflation and estimated payout periods. The review led to an approximate \$60 million increase in case reserves held for specific claims from accident years going back as many as 20 years and the identification of several new losses greater than \$1 million. Since we had raised workers' compensation IBNR reserves in 2005 to reflect trends in medical cost inflation and estimated payout periods, we were able to offset \$44 million of the case reserve increases through IBNR reserve decreases.

Pricing and normal loss cost inflation contributed to the increase in the accident year loss and loss expense ratio in 2007. In addition, the workers' compensation business line includes our longest tail exposures, making initial estimates of accident year loss and loss expenses incurred more uncertain. Favorable development on prior period reserves moderated the effect of the increase in the 2007 accident year loss and loss expense ratio on the corresponding calendar year ratio.

Due to the lengthy payout period of workers' compensation claims, small shifts in medical cost inflation and payout periods could have a significant effect on our potential future liability compared with our current projections.

## Specialty Packages

(Dollars in millions)	Years ended December 31,			2007-2006	2006-2005	
	2007	2006	2005	Change %	Change %	
Specialty packages:						
Written premiums	\$ 146	\$ 144	\$ 138	1.5	4.6	
Earned premiums	146	141	137	3.1	3.2	
Loss and loss expenses incurred	86	94	92	(7.5)	2.1	
Loss and loss expense ratio	59.4 %	66.3 %	67.0 %			
Loss and loss expense ratio excluding catastrophes	55.3	54.9	61.8			
Reserve development impact on loss and loss expense ratio	0.5	1.6	10.9			
Accident year loss and loss expenses incurred and ratios to earned premiums:						
Accident year:	2007	2006	2005	2007	2006	2005
as of December 31, 2007	\$ 86	\$ 92	\$ 81	58.9 %	65.3 %	59.1 %
as of December 31, 2006		91	80		64.7	58.6
as of December 31, 2005			77			56.1

Specialty packages net written premiums rose in 2007 and 2006. The rollout of our commercial lines policy processing system for Businessowners Policies, which are included in this business line, should help us meet changing agency needs and address pricing, technology and service innovations that other carriers have introduced for similar products in recent years.

The loss and loss expense ratio excluding catastrophe losses and the accident year loss and loss expense ratio remained within the ranges we consider appropriate.

## Surety and Executive Risk

(Dollars in millions)	Years ended December 31,			2007-2006	2006-2005	
	2007	2006	2005	Change %	Change %	
Surety and executive risk:						
Written premiums	\$ 102	\$ 97	\$ 85	5.2	15.3	
Earned premiums	100	93	80	7.8	16.3	
Loss and loss expenses incurred	42	47	27	(11.1)	72.2	
Loss and loss expense ratio	41.8 %	50.7 %	34.2 %			
Loss and loss expense ratio excluding catastrophes	41.8	50.7	34.2			
Reserve development impact on loss and loss expense ratio	1.2	6.3	(5.4)			
Accident year loss and loss expenses incurred and ratios to earned premiums:						
Accident year:	2007	2006	2005	2007	2006	2005
as of December 31, 2007	\$ 41	\$ 44	\$ 42	40.6 %	47.3 %	52.5 %
as of December 31, 2006		41	39		44.4	48.3
as of December 31, 2005			32			39.6

Surety and executive risk net written premiums rose in 2007 and 2006. Healthy economic activity in some regions drove the 2006 growth.

Director and officer liability coverage accounted for 62.3 percent of surety and executive risk premiums in 2007 compared with 60.5 percent in 2006 and 57.1 percent in 2005. Our director and officer liability policies are offered primarily to nonprofit organizations, reducing the risk associated with this line of business.

Nonprofit organizations accounted for approximately 80 percent of the director and officer liability policies we wrote in 2007. We manage our loss exposure to director and officer liability coverages by writing on claims-made coverage forms, providing limits up to \$10 million and purchasing reinsurance.

In addition, our independent agencies market our director and officer liability policies to some clients that are for-profit organizations. At year-end 2007, our in-force director and officer liability policies provided coverage to 30 non-financial publicly traded companies, including two Fortune 1000 companies. We also provided this coverage to approximately 500 banks, savings and loans and other financial institutions. The majority of these financial institution policyholders are smaller community banks, and we believe they have no unusual exposure to credit-market concerns, including subprime mortgages. Only 12 of our bank and savings and loan policyholders have assets greater than \$2 billion, including one Fortune 500 company; only 23 have assets between \$1 billion and \$2 billion; and 52 have assets between \$500 million and \$1 billion.

The loss and loss expense ratio and reserve development fluctuated significantly over the three years. We do not believe the changes indicate any new trend or risk.

## Machinery and Equipment

(Dollars in millions)	Years ended December 31,			2007-2006	2006-2005	
	2007	2006	2005	Change %	Change %	
<b>Machinery and equipment:</b>						
Written premiums	\$ 29	\$ 29	\$ 26	0.2	8.7	
Earned premiums	28	27	26	2.4	5.8	
Loss and loss expenses incurred	8	12	6	(32.3)	98.7	
Loss and loss expense ratio	27.8 %	42.0 %	22.4 %			
Loss and loss expense ratio excluding catastrophes	28.1	41.6	22.5			
Reserve development impact on loss and loss expense ratio	(5.8)	2.8	(3.7)			
<b>Accident year loss and loss expenses incurred and ratios to earned premiums:</b>						
Accident year:	2007	2006	2005	2007	2006	2005
as of December 31, 2007	\$ 10	\$ 10	\$ 7	33.6 %	35.9 %	26.1 %
as of December 31, 2006		11	7		39.2	28.6
as of December 31, 2005			7			26.1

Machinery and equipment net written premiums rose slightly in 2007, building on an 8.7 percent increase in 2006. Marketing by machinery and equipment and field marketing representatives contributed to the growth. Conditions in the machinery and equipment insurance marketplace are similar to those of commercial lines overall.

Because of the relatively small size of this business line, the calendar year and accident year loss and loss expense ratio fluctuates. In 2006, a single unusually large loss was responsible for the higher ratio.

### Commercial Lines Insurance Outlook

Industrywide commercial lines written premiums are expected to decline approximately 2.3 percent in 2008 with the industry combined ratio estimated at 97.5 percent. As discussed in Item 1, Commercial Lines Insurance Marketplace, Page 12, over the past several years, agents have reported that renewal and new business pricing have come under steadily increasing pressure, reinforcing the need for more flexibility and careful risk selection. We anticipate that commercial lines pricing trends observed in 2007 will persist into 2008.

We intend to continue to market our products to a broad range of business classes, price our products adequately and take a package approach. We intend to maintain our underwriting selectivity and carefully manage our rate levels as well as our programs that seek to accurately match exposures with appropriate premiums. We will continue to evaluate each risk individually and to make decisions regarding rates, the use of three-year commercial policies, policy term extensions and other policy conditions on a case-by-case basis, even in lines and classes of business that are under competitive pressure. We also expect new marketing territories created over the past several years and new agency appointments will make a growing contribution to commercial lines premiums and underwriting profit in 2008.

We believe our approach should allow us to continue to underwrite commercial lines business profitably in 2008 although we anticipate another year of both lower premiums and a higher commercial lines combined ratio, as ongoing soft market conditions lead to lower premium per exposure. In addition, we do not believe favorable reserve development will continue to contribute to underwriting profits to the extent seen over the past four years. Further, underwriting expenses are rising. We discuss our overall outlook for our property casualty insurance operations in Measuring Our Success in 2008 and Beyond, Page 35.

## PERSONAL LINES INSURANCE RESULTS OF OPERATIONS

### Overview – Three-year Highlights

Performance highlights for the personal lines segment include:

- **Premiums** – As competition in our personal lines markets rose and we continued to work to generate consistent profitability in our personal lines segment, our written premiums declined in both 2007 and 2006, largely due to pricing that led to lower premiums per policy. Industry average written premiums were estimated to be flat in 2007, after rising 2.0 percent in 2006 and 3.7 percent in 2005. Personal lines new business premiums written directly by agencies increased 16.9 percent to \$38 million in 2007 and 1.6 percent to \$33 million in 2006 after declining 33.9 percent to \$32 million in 2005.
- **Combined ratio** – The combined ratio improved 9.7 percentage points in 2007 after rising 9.2 percentage points in 2006. The year-over-year differences largely were due to fluctuations in the level of catastrophe losses and the steady rise in the current accident year loss and loss expense ratio excluding catastrophe losses. Year-over-year comparisons would have been stronger if earned premiums had not declined.

Our personal lines statutory combined ratio was 94.1 percent in 2007, 103.6 percent in 2006 and 94.3 percent in 2005. By comparison, the estimated industry personal lines combined ratio was 97.0 percent in 2007, 92.3 percent in 2006 and 97.6 percent in 2005. We believe our results are trending differently than the overall industry because of the competitive and pricing factors discussed below. In addition, the industry experienced unusually high catastrophe losses in 2005 and unusually low catastrophe losses in 2006.

## Personal Lines Results

(Dollars in millions)	Years ended December 31,			2007-2006	2006-2005
	2007	2006	2005	Change %	Change %
Written premiums	\$ <u>704</u>	\$ <u>736</u>	\$ <u>786</u>	(4.4)	(6.4)
Earned premiums	\$ 714	\$ 762	\$ 804	(6.3)	(5.3)
Loss and loss expenses excluding catastrophes	428	456	463	(6.2)	(1.5)
Catastrophe loss and loss expenses	10	86	51	(89.0)	69.8
Commission expenses	145	152	154	(4.4)	(1.6)
Underwriting expenses	88	95	91	(7.5)	4.2
Underwriting profit (loss)	\$ <u>43</u>	\$ <u>(27)</u>	\$ <u>45</u>	260.9	(160.0)
Ratios as a percent of earned premiums:					
Loss and loss expenses excluding catastrophes	60.0 %	59.9 %	57.6 %		
Catastrophe loss and loss expenses	<u>1.3</u>	<u>11.3</u>	<u>6.3</u>		
Loss and loss expenses	61.3	71.2	63.9		
Commission expenses	20.3	19.9	19.2		
Underwriting expenses	12.3	12.5	11.3		
Combined ratio	<u>93.9 %</u>	<u>103.6 %</u>	<u>94.4 %</u>		

## Growth and Profitability

Personal lines insurance is a strategic component of our overall relationship with many of our agencies and an important component of agency relationships with their clients. We believe agents recommend Cincinnati personal insurance products for their value-oriented clients who seek to balance quality and price and are attracted by Cincinnati's superior claims service and the benefits of our package approach.

In late 2004, price competition returned to the personal lines market as insurers leveraged the higher profitability and stronger financial positions that were the outcome of industrywide increases in homeowner rates and of stricter enforcement of underwriting standards. Through 2006, our growth and profitability were stymied by delays in implementing rate changes needed to respond to the market and delays in deploying new technology initiatives. During this time, other carriers began using segmented pricing models more aggressively, allowing them to develop more accurate prices for each risk.

Policyholder retention and new business levels have remained at higher levels following our July 2006 introduction of a limited program of policy credits for personal auto and homeowner pricing in most of the states in which our Diamond system is in use. These credits incorporate insurance scores and are intended to improve our ability to compete for our agents' highest quality personal lines accounts, increasing the opportunity for our agents to market the advantages of our personal lines products and services to their clients. These changes resulted in credits for eligible new and renewal policyholders identified as above-average risks.

We also have deployed our technology solution, Diamond, to 17 states, which represent 97.5 percent of personal lines premiums. We continue to respond to agency requests for enhancements as we prepare Diamond for additional states.

At year-end 2007, new business premiums had risen for six consecutive quarters after declining for the 14 prior quarters. However, the increased new business did not fully offset the impact of lost business and lower rates on above-average quality renewal business. The number of in-force homeowner and personal auto policies has declined since 2003.

Premium trends by personal line of business and strategies to achieve growth in our personal lines segment are discussed below.

Even though 2007 was a profitable year as a result of low catastrophe activity, the combined ratio excluding catastrophes has risen in each of the past three years and remains above our targeted range. We continue to address pricing, scale, growth and other issues to help restore the financial health of this strategic business segment. In 2006, higher catastrophe losses also contributed to a higher combined ratio.

We describe the significant cost components for the personal lines segment below.

### Loss and Loss Expenses (excluding catastrophe losses)

Loss and loss expenses include both net paid losses and reserve changes for unpaid losses as well as the associated loss expenses. The trend in the loss and loss expense ratio excluding catastrophe losses over the past three years largely was due to the pricing factors discussed above. This resulted in a steady increase in the accident year loss and loss expense ratio excluding catastrophe losses to 64.2 percent in 2007 from

61.9 percent in 2006 and 61.5 percent in 2005. Savings from favorable development on prior period reserves reduced the loss and loss expense ratio by 5.7, 2.4 and 4.3 percentage points in 2007, 2006 and 2005, respectively. We discuss the contribution of changes in prior period reserves by personal line of business below.

The rise in the loss and loss expense ratio included a higher contribution from new losses and case reserve increases greater than \$250,000. In total, personal lines new losses and reserve increases greater than \$250,000 rose to 12.8 percent of earned premium from 11.0 percent in 2006 and 8.2 percent in 2005. Our analysis indicated no unexpected concentration of these losses and reserve increases by risk category, geographic region, policy inception, agency or field marketing territory. We believe the increase largely was due to general inflationary trends in loss costs, which we continue to monitor, as well as natural volatility. We also continue to analyze factors that could contribute to a rise in large losses.

### Personal Lines Losses by Size

(Dollars in millions)	Years ended December 31,			2007-2006	2006-2005
	2007	2006	2005	Change %	Change %
New losses greater than \$4,000,000	\$ 0	\$ 0	\$ 0	0.0	0.0
New losses \$2,000,000-\$4,000,000	13	8	2	72.0	270.4
New losses \$1,000,000-\$2,000,000	15	14	6	3.5	113.2
New losses \$750,000-\$1,000,000	8	9	8	(6.7)	13.8
New losses \$500,000-\$750,000	10	8	9	20.9	(4.4)
New losses \$250,000-\$500,000	26	22	22	15.5	2.3
Case reserve development above \$250,000	19	23	19	(16.4)	21.9
Total large losses incurred	91	84	66	8.1	27.7
Other losses excluding catastrophes	279	309	339	(9.7)	(8.9)
Catastrophe losses	10	86	51	(89.0)	69.8
Total losses incurred	\$ 380	\$ 479	\$ 456	(20.8)	5.1
Ratios as a percent of earned premiums:					
New losses greater than \$4,000,000	0.0 %	0.0 %	0.0 %		
New losses \$2,000,000-\$4,000,000	1.9	1.0	0.3		
New losses \$1,000,000-\$2,000,000	2.0	1.8	0.8		
New losses \$750,000-\$1,000,000	1.1	1.1	0.9		
New losses \$500,000-\$750,000	1.5	1.1	1.1		
New losses \$250,000-\$500,000	3.6	2.9	2.7		
Case reserve development above \$250,000	2.7	3.1	2.4		
Total large losses incurred	12.8	11.0	8.2		
Other losses excluding catastrophes	39.1	40.6	42.2		
Catastrophe losses	1.3	11.3	6.3		
Total loss ratio	53.2 %	62.9 %	56.7 %		

### Catastrophe Loss and Loss Expenses

Personal lines catastrophe losses, net of reinsurance and before taxes, contributed 10 percentage points less to the combined ratio in 2007 primarily because of the lower level of catastrophe activity during the year. In 2006, catastrophe losses, net of reinsurance and before taxes, contributed 5 percentage points more to the combined ratio than in 2005 because of an increase of \$35 million in incurred catastrophe losses and lower earned premium. The majority of these losses related to wind and hail from storms in Indiana and Ohio.

### Commission Expenses

Personal lines commission expense as a percent of earned premium rose by 0.4 and 0.7 percentage points in 2007 and 2006. The increases were primarily due to higher profit-sharing commissions resulting from accrual and allocation adjustments. Commission expenses include our profit-sharing, or contingent, commissions, which are calculated on the profitability of an agency's aggregate property casualty book of Cincinnati business, taking into account longer-term profit and premium volume, with a percentage for prompt payment of premiums and other criteria, and reward the agency's effort. These profit-based commissions generally fluctuate with our loss and loss expense ratio. Our 2007 contingent commission accrual reflected our estimate of the profit-sharing commissions to be paid to our agencies in early 2008 based largely on each agency's performance in 2007.

### Underwriting Expenses

Non-commission underwriting expenses moderated slightly in 2007 after a significant rise in 2006. We continue to invest in our associates and technology, which contributed to an increase in non-commission underwriting expenses in 2006. In that year, higher technology expense contributed 0.8 percentage points and higher staffing expense contributed 0.8 points, with stock option expense accounting for 0.5 percentage points of that amount. Increases in those amounts were offset partially by savings in taxes, licenses and fees. Reallocation of expenses between our commercial lines and personal lines segments as we refined our data also contributed to the 2007 improvement.

## Line of Business Analysis

We prefer to write personal lines coverage on an account basis that includes both auto and homeowner coverages as well as coverages from the other personal business line. As a result, we believe that the personal lines segment is best measured and evaluated on a segment basis. However, we provide the line of business data to summarize growth and profitability trends separately for each line.

The corresponding accident year loss data provides current estimates of incurred loss and loss expenses and corresponding ratios over the most recent three accident years. Accident year data classifies losses according to the year in which the corresponding loss event occurs, regardless of when the losses are actually reported, recorded or paid.

### Personal Auto

(Dollars in millions)	Years ended December 31,			2007-2006	2006-2005	
	2007	2006	2005	Change %	Change %	
Personal auto:						
Written premiums	\$ 332	\$ 359	\$ 409	(7.5)	(12.4)	
Earned premiums	342	385	433	(11.0)	(11.2)	
Loss and loss expenses incurred	228	250	259	(8.6)	(3.5)	
Loss and loss expense ratio	66.8 %	65.0 %	59.9 %			
Loss and loss expense ratio excluding catastrophes	67.4	62.2	59.3			
Reserve development impact on loss and loss expense ratio	0.7	0.6	(1.9)			
Accident year loss and loss expenses incurred and ratios to earned premiums:						
Accident year:	2007	2006	2005	2007	2006	2005
as of December 31, 2007	\$ 226	\$ 251	\$ 276	66.1 %	65.4 %	64.0 %
as of December 31, 2006		248	272		64.5	62.8
as of December 31, 2005			267			61.8

The decline in written and earned premiums over the past three years largely was due to policy credits adopted in mid-2006 that improved our position in the market by lowering premiums for eligible new and renewal policyholders. The new policy credits have had a positive effect on policyholder retention and new business activity. New business, however, has not yet returned to a level that would allow us to replace premiums lost due to price reductions and normal attrition. We continue to monitor and modify selected rates and credits to address our competitive position.

The personal auto loss and loss expense ratio excluding catastrophe losses deteriorated in 2007 after several years of stability. The higher ratio in 2007 largely reflected current pricing and normal loss cost trends. In recent years, we have seen generally higher costs for liability claims, including severe injuries, and we are seeking rate increases for liability coverages that would partially offset price decreases we are seeking for physical damage coverages. Pricing decreases and normal loss cost inflation also are the primary drivers in the rise in the accident year loss and loss expense ratio over the past three years.

### Homeowner

(Dollars in millions)	Years ended December 31,			2007-2006	2006-2005	
	2007	2006	2005	Change %	Change %	
Homeowner:						
Written premiums	\$ 284	\$ 290	\$ 288	(2.1)	0.7	
Earned premiums	285	289	282	(1.6)	2.3	
Loss and loss expenses incurred	168	240	213	(30.0)	12.4	
Loss and loss expense ratio	59.0 %	83.0 %	75.5 %			
Loss and loss expense ratio excluding catastrophes	55.5	59.3	58.6			
Reserve development impact on loss and loss expense ratio	(3.5)	1.5	(0.4)			
Accident year loss and loss expenses incurred and ratios to earned premiums:						
Accident year:	2007	2006	2005	2007	2006	2005
as of December 31, 2007	\$ 178	\$ 229	\$ 220	62.5 %	79.2 %	77.9 %
as of December 31, 2006		235	219		81.5	77.6
as of December 31, 2005			215			76.0

Written and earned premium trends reflected improved new business levels in 2007 that were not sufficient; however, to replace premiums lost due to price reductions, normal attrition and higher reinsurance premiums. Policy credits adopted in mid-2006 improved our competitive position, while lowering rates for eligible new and renewal policyholders. The new policy credits have had a positive effect on policyholder retention and new business activity. We continue to monitor and modify selected rates and credits to address our competitive position. Higher 2007 reinsurance premiums contributed 2.7 percentage points to the decline in written premiums.

The homeowner loss and loss expense ratio excluding catastrophes improved in 2007 after deteriorating in 2006. Although the full benefit of pricing and underwriting actions taken between 2004 and 2006 is reflected in homeowner results, this line has not yet achieved breakeven performance if a normalized level of

catastrophe losses is assumed. Rate changes we made to keep our retention rate and new business at acceptable levels, along with higher reinsurance costs, have interrupted our progress toward consistent breakeven performance for the homeowner business line. Changes in catastrophe loss levels were the primary reason for the fluctuations in the accident year loss ratio over the past three years.

Two other factors also contribute to our ability to achieve satisfactory homeowner results:

- Non-commission expenses – Since we generally do not allocate non-commission expenses to individual business lines, to measure homeowner profitability, we use a personal lines segment commission and underwriting expense ratio of approximately 33 percentage points to determine an estimated homeowner combined ratio. Lower levels of premium growth affected our expense ratio in 2007 and may affect our ability to attain our personal lines segment expense ratio target in the future.
- Catastrophe losses – To measure our progress toward homeowner profitability, we use a normalized catastrophe loss ratio (as a percent of homeowner earned premium) in the range of 17 percent. Between 2005 and 2007, catastrophe losses averaged 14.5 percent of homeowner earned premiums. We have not changed our catastrophe loss assumption because unusually low catastrophe losses in 2007 artificially lowered the average and because the geographic concentration of losses in 2005 and 2006 was unusual.

## Other Personal

(Dollars in millions)	Years ended December 31,			2007-2006	2006-2005	
	2007	2006	2005	Change %	Change %	
Other personal:						
Written premiums	\$ 88	\$ 87	\$ 89	0.4	(2.0)	
Earned premiums	87	88	89	(1.2)	(1.1)	
Loss and loss expenses incurred	41	52	40	(21.7)	31.6	
Loss and loss expense ratio	47.0 %	59.4 %	44.6 %			
Loss and loss expense ratio excluding catastrophes	45.3	52.0	41.6			
Reserve development impact on loss and loss expense ratio	(37.8)	(28.6)	(28.7)			
Accident year loss and loss expenses incurred and ratios to earned premiums:						
Accident year:	2007	2006	2005	2007	2006	2005
as of December 31, 2007	\$ 74	\$ 67	\$ 53	84.8 %	75.7 %	59.3 %
as of December 31, 2006		77	58		88.0	65.4
as of December 31, 2005			64			73.3

Other personal written premiums were essentially unchanged between 2005 and 2007. The decline in the number of homeowner and personal auto policies over the past several years hindered growth in this business line since most of our other personal coverages are endorsed to homeowner or auto policies.

The loss and loss expense ratio for other personal improved in 2007 after deteriorating in 2006. Personal umbrella losses, which are a major component of other personal losses, can fluctuate significantly, and we do not believe that the changes indicated any new trend.

## Personal Lines Insurance Outlook

Industry analysts currently anticipate industrywide personal lines written premiums may rise approximately 1.4 percent in 2008 with the combined ratio estimated at 99.5 percent. While the improvement in our new business levels and policy retention rates over the past 18 months are positive indications for our personal lines business, we believe our growth rate will be below that of the industry as we continue to address our pricing structure. We are aware that our personal lines pricing and loss activity are at levels that could put pressure on our future consolidated property casualty insurance combined ratio, if those trends continue.

We plan to take steps in our personal lines insurance operations to enhance our response to the changing marketplace. These strategies should help us achieve our long-term objectives for this segment:

- Competitive rates – In mid-2006, we introduced insurance scores into our rating program for homeowner and personal auto pricing. In 2007 we began offering a discount on homeowner policies in some states when an auto policy is also purchased. Previously, we discounted only the auto policy when a policyholder had both policies. Rollout of this credit will continue in additional states in 2008. While these pricing refinements reduced premiums for many policies we write, we believe they present an opportunity to attract our agents' more quality-conscious clientele. We are working to build on this success with the introduction of more sophisticated rating during 2008.
- Value-added products – We introduced three new personal lines products in 2007, supporting our agents' ability to create packages with marketable differences: Replacement Cost Coverage for a Total Loss – Auto; Personal Auto Plus Endorsement; and Identify Theft Expense Coverage and Advocacy Services. Another new product will begin rolling out in the second half of 2008: Mechanical Breakdown Coverage adds protection for major home systems to the homeowner policy.
- Diamond – The Diamond system is in use by agencies writing approximately 97.5 percent of personal lines premium volume. The system makes it easier for agents to place personal auto, homeowner and other personal lines business with us, while greatly increasing policy-issuance and policy-renewal efficiencies

and providing direct-bill capabilities. In 2008, we expect to implement upgrades that will further improve user satisfaction.

- **New agencies** – The availability of Diamond should help us increase the number of agencies that offer our personal lines products. During 2007, some agency locations that previously marketed only our commercial lines products added our personal lines products. Expanding into these agencies should provide additional sources of premiums and help geographically diversify our personal lines portfolio. Further, in 2008, we expect to deploy Diamond to agencies in eight additional states. We already market personal lines products in Maryland, Montana, New Hampshire, North Carolina and Vermont, and we expect agencies in these states to respond favorably to its advantages. We also expect to deploy Diamond to agencies in Arizona, South Carolina and Utah, where we currently market only commercial lines products.

We identify several other factors that may affect the personal lines combined ratio in 2008 and beyond. Personal lines underwriters continue to focus on insurance-to-value initiatives to verify that policyholders are buying the correct level of coverage for the value of the insured risk, and we are carefully maintaining underwriting standards. If earned premiums decline more than we expect, the personal lines expense ratio may be higher than the 2007 level because some of our costs are relatively fixed, such as our planned investments in technology. We discuss our overall outlook for our property casualty insurance operations in Measuring Our Success in 2008 and Beyond, Page 35.

## LIFE INSURANCE RESULTS OF OPERATIONS

### Overview – Three-year Highlights

Performance highlights for the life insurance segment include:

- **Revenues** – Driven by higher term life insurance premiums, revenue growth has accelerated over the past three years. Gross in-force policy face amounts increased to \$61.875 billion at year-end 2007 from \$56.971 billion at year-end 2006 and \$51.493 billion at year-end 2005.
- **Profitability** – The life insurance segment frequently reports a small GAAP loss because its investment income is included in investment segment results, except investment income credited to contract holders (interest assumed in life insurance policy reserve calculations). The segment reported a nominal operating profit in 2007.

At the same time, we recognize that assets under management, capital appreciation and investment income are integral to evaluation of the success of the life insurance segment because of the long duration of life products. For that reason, we also evaluate GAAP data, including all investment activities on life insurance-related assets. Including investment income and realized gains on investments, GAAP net income for the life insurance segment grew 3.8 percent in 2007 to \$65 million, 32.6 percent in 2006 to \$63 million and 23.8 percent in 2005 to \$47 million. The life insurance company portfolio had after tax realized investment gains of \$26 million in 2007 compared with \$29 million in 2006 and \$11 million in 2005.

### Life Insurance Results

(In millions)	Years ended December 31,			2007-2006	2006-2005
	2007	2006	2005	Change %	Change %
Written premiums	\$ <u>167</u>	\$ <u>161</u>	\$ <u>205</u>	3.2	(21.3)
Earned premiums	\$ 125	\$ 115	\$ 106	9.0	7.9
Separate account investment management fees	4	3	4	25.1	(0.3)
Total revenues	<u>129</u>	<u>118</u>	<u>110</u>	9.5	7.6
Contract holders benefits incurred	133	122	102	9.2	20.1
Investment interest credited to contract holders	(59)	(54)	(51)	9.8	5.7
Operating expenses incurred	52	51	52	0.8	(1.8)
Total benefits and expenses	<u>126</u>	<u>119</u>	<u>103</u>	5.3	16.1
Life insurance segment profit (loss)	\$ <u>3</u>	\$ <u>(1)</u>	\$ <u>7</u>	446.3	(115.4)

### Growth

We market term, whole and universal life products, fixed annuities and disability income products. In addition, we offer term, whole and universal life and disability insurance to employees at their worksite. These products provide our property casualty agency force with excellent cross-serving opportunities for both commercial and personal accounts.

Total statutory life insurance net written premiums were \$167 million in 2007 compared with \$161 million in 2006 and \$205 million in 2005. Total statutory written premiums for life insurance operations for all periods include life insurance, annuity and accident and health premiums. The change primarily was due to:

- Statutory written premiums for term and other life insurance products rose 10.5 percent to \$141 million for 2007 and 12.7 percent to \$127 million for 2006. In 2006, we began emphasizing products that



generate a higher average premium per policy through enhanced features and higher face amounts while reducing expenses.

- Statutory written annuity premiums declined \$8 million in 2007 and \$58 million in 2006. Since late 2005, we have de-emphasized annuities because of an unfavorable interest rate environment.

Fee income from universal life products increased 35.1 percent in 2007 to \$31 million after declining 14.9 percent to \$23 million in 2006. Our new universal life product with secondary guarantees contributed to the increase in fee income in 2007. Separate account investment management fee income contributed \$4 million, \$3 million and \$4 million to total revenues in 2007, 2006 and 2005.

Over the past several years, we have worked to maintain a portfolio of simple, yet competitive products, primarily under the LifeHorizons banner. Our product development efforts emphasize death benefit protection and guarantees. Distribution expansion within our property casualty insurance agencies remains a high priority. In the past several years, we have added life field marketing representatives for the western, southeastern and northeastern states. Our 29 life field marketing representatives work in partnership with our 106 property casualty field marketing representatives. Approximately 71 percent of our term and other life insurance product premiums were generated through our property casualty insurance agency relationships.

## **Profitability**

Life segment expenses consist principally of:

- Contract holders (policyholders) benefits incurred related to traditional life and interest-sensitive products accounted for 71.9 of 2007 total benefits and expenses, 73.8 percent of 2006 total benefits and expenses and 71.3 percent of 2005 total benefits and expenses.
- Operating expenses incurred, net of deferred acquisition costs, accounted for 28.1 percent of 2007 total benefits and expenses, 29.7 percent of 2006 total benefits and expenses and 34.0 percent of 2005 total benefits and expenses. Operating expenses rose on an absolute and percentage basis principally because of changes in the amortization of universal life deferred acquisition costs.

Life segment profitability depends largely on premium levels, the adequacy of product pricing, underwriting skill and operating efficiencies. Life segment results include only investment interest credited to contract holders (interest assumed in life insurance policy reserve calculations). The remaining investment income is reported in the investment segment results. The life investment portfolio is managed to earn target spreads between earned investment rates on general account assets and rates credited to policyholders. We consider the value of assets under management and investment income for the life investment portfolio as key performance indicators for the life insurance segment.

We seek to maintain a competitive advantage with respect to benefits paid and reserve increases by consistently achieving better than average claims experience due to skilled underwriting. Commissions paid by the life insurance operation are on par with industry averages. During the past several years, we have invested in imaging and workflow technology and have significantly improved application processing. We have achieved process efficiencies while improving our service.

## **Life Insurance Outlook**

Our overall objective is to increase premiums and contain expenses as the life insurance company seeks to improve penetration of our property casualty agencies. Term insurance is our largest life insurance product line. We continue to introduce new term products with features our agents and their clients indicate are important. We also continue to improve our worksite portfolio to help in our cross-selling initiatives.

The life insurance business is considered mature. In our experience, it is not mature within the property casualty distribution system where cross-sell opportunities abound – both to personal lines and commercial lines clients. In particular, there are approximately 41 million under- and uninsured employees of small business in the United States, making the cross-selling of voluntary, worksite products a huge opportunity for Cincinnati Life's worksite marketing and sales strategies.

In 2008 we plan to redesign all our term insurance products. In addition to redesigning our worksite term insurance, we will be updating all of the other products in our worksite life insurance portfolio. These improvements support opportunities to cross-sell life insurance products to clients of the independent agencies that sell Cincinnati's property casualty insurance policies.

## **INVESTMENTS RESULTS OF OPERATIONS**

### **Overview – Three-year Highlights**

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

- Investment income – Pretax investment income reached a new record again in 2007, rising 6.6 percent from the prior record in 2006. Growth in investment income over the past two years has been driven by

strong cash flow for new investments, higher interest income from the growing fixed-maturity portfolio and increased dividend income from the common stock portfolio.

- Realized investment gains and losses – We reported realized investment gains in all three years largely due to investment sales that were discretionary in timing and amount.

## Investment Results

(In millions)	Years ended December 31,			2007-2006	2006-2005
	2007	2006	2005	Change %	Change %
Investment income:					
Interest	\$ 308	\$ 300	\$ 280	2.5	7.1
Dividends	294	262	244	12.1	7.5
Other	15	15	8	(0.5)	90.0
Investment expenses	(9)	(7)	(6)	(18.7)	(19.3)
Total investment income, net of expenses	608	570	526	6.6	8.4
Investment interest credited to contract holders	(59)	(54)	(51)	9.8	5.7
Realized investment gains and losses summary:					
Realized investment gains and losses	409	678	69	(39.6)	883.0
Change in fair value of securities with embedded derivatives	(11)	7	(7)	(263.6)	200.7
Other-than-temporary impairment charges	(16)	(1)	(1)	(1,872.5)	41.7
Total realized investment gains and losses	382	684	61	(44.1)	1,026.0
Investment operations income	\$ 931	\$ 1,200	\$ 536	(22.4)	124.0

## Investment Income

Growth of investment income reflected new investments, higher interest income from the growing fixed-maturity portfolio and increased cash dividend income from the common stock portfolio. The advantages of strong cash flow in the past three years for new investments have been somewhat offset by the challenge of investing in a low interest rate environment. In 2006, proceeds from the sale of the Alltel holding that were later used to make the applicable tax payments during the year were invested in short-term instruments that generated approximately \$5 million in interest income.

Overall, common stock dividends contributed 44.6 percent of pretax investment income compared with 42.4 percent in 2006 and 43.7 percent in 2005. Fifth Third, our largest equity holding, contributed 41.3 percent of total dividend income in 2007. We discuss our Fifth Third investment in Item 7A, Quantitative and Qualitative Disclosures About Market Risk, Page 73. In 2007, 35 of the 42 common stock holdings in the portfolio raised their indicated annual dividend payout, as did 38 of the 50 in 2006 and 36 of 49 in 2005.

## Net Realized Investment Gains and Losses

Net realized investment gains and losses are made up of realized investment gains and losses on the sale of securities, changes in the valuation of embedded derivatives within certain convertible securities and other-than-temporary impairment charges. These three areas are discussed below.

## Realized Investment Gains and Losses

Pretax realized investment gains in the past three years largely were due to the sale of equity holdings. We discuss these sales in Item 1, Investments Segment, Page 15. As appropriate, we buy, hold or sell both fixed-maturity and equity securities on an ongoing basis to help achieve our portfolio objectives.

- 2007 –
  - We sold 3.8 million shares of ExxonMobil common stock, contributing \$217 million to realized investment gains
  - We divested the majority of our real estate investment trust holdings, contributing \$72 million to realized investment gains
  - We sold 5.5 million shares of Fifth Third common stock in a block sale, contributing \$64 million to realized investment gains
  - We sold all of our FirstMerit common stock holdings, contributing \$59 million to realized investment gains
- 2006 – We sold the remainder of our Alltel common stock holdings, contributing \$647 million to realized investment gains.
- 2005 – We had gains from the sale of equity holdings that no longer met our investment parameters or were obtained from convertible securities whose underlying common stock was never intended to be a long-term holding. Included in 2005 were gains from the initial sales of a portion of our Alltel holding.

During the past three years, fixed maturity securities were divested as a result of calls or as outright sales executed to either improve yield prospects or in response to adverse credit concerns. Although we prefer to hold fixed-maturity investments until they mature, a decision to sell reflects our perception of a change in the underlying fundamentals of the security and preference to allocate those funds to investments that more

closely meet our established parameters for long-term stability and growth. Our opinion that a security fundamentally no longer meets our investment parameters may reflect a loss of confidence in the issuer's management, a change in underlying risk factors (such as political risk, regulatory risk, sector risk or credit risk), or a strategic shift in business strategy that is not consistent with our long-term outlook.

Realized gains in the past three years also have included gains from the sale of previously impaired securities.

### Change in the Valuation of Securities with Embedded Derivatives

In 2007, we recorded \$11 million in fair value declines compared with \$7 million in fair value increases in 2006 and \$7 million in fair value declines in 2005. In 2007, these changes in fair value were due to the application of SFAS No. 155, which allows us to account for the entire hybrid financial instrument at fair value, with changes recognized in realized investment gains and losses. In 2006 and 2005, these changes in fair value were due to the application of SFAS No. 133, which required measurement of the fluctuations in the value of the embedded derivative features in selected convertible securities. The changes in fair values are recognized in net income in the period they occur. See the discussion of Derivative Financial Instruments and Hedging Activities in Item 8, Note 1 of the Consolidated Financial Statements, Page 87, for details on the accounting for convertible security embedded options.

### Other-than-temporary Impairment Charges

In 2007, we recorded \$16 million in write-downs of investments that we deemed had experienced an other-than-temporary decline in market value versus \$1 million in both 2006 and 2005. The factors we consider when evaluating impairments are discussed in Critical Accounting Estimates, Asset Impairment, Page 40. The other-than-temporary impairment charges represented less than 0.1 percent of our total invested assets at year-end 2007. Other-than-temporary impairment charges also include unrealized losses of holdings that we have identified for sale but not yet completed a transaction.

The increase in other-than-temporary impairment in 2007 from the negligible level of the prior two years was due to market value declines for 20 securities. Those declines reflected general credit concerns that began in the subprime mortgage market and spread to other areas in the homebuilding and related industries over the course of 2007. While we do not directly own mortgages or mortgage backed securities in our investment portfolio, we do own investments in industries directly affected by this credit environment.

Other-than-temporary impairment charges from the investment portfolio by industry are summarized as follows:

(In millions)	Years ended December 31,		
	2007	2006	2005
Home building	\$ (5)	\$ 0	\$ 0
Financial	(6)	0	0
Automotive	0	(1)	(1)
Other	(5)	0	0
Total	<u>\$ (16)</u>	<u>\$ (1)</u>	<u>\$ (1)</u>

Other-than-temporary impairment charges from the investment portfolio by the asset class we described in Item 1, Investments Segment, Page 15, are summarized below:

(Dollars in millions)	Years ended December 31,		
	2007	2006	2005
Taxable fixed maturities:			
Impairment amount	\$ (14)	\$ (1)	\$ (1)
New book value	\$ 46	\$ 0	\$ 0
Percent to total owned	1 %	0 %	0 %
Number of securities impaired	18	1	2
Percent to total owned	2 %	0 %	0 %
Common equities:			
Impairment amount	\$ (2)	\$ 0	\$ 0
New book value	\$ 2	\$ 0	\$ 0
Percent to total owned	0 %	0 %	0 %
Number of securities impaired	2	0	0
Percent to total owned	4 %	0 %	0 %
Total:			
Impairment amount	<u>\$ (16)</u>	<u>\$ (1)</u>	<u>\$ (1)</u>
New book value	<u>\$ 48</u>	<u>\$ 0</u>	<u>\$ 0</u>
Percent to total owned	<u>1 %</u>	<u>0 %</u>	<u>0 %</u>
Number of securities impaired	<u>20</u>	<u>1</u>	<u>2</u>
Percent to total owned	<u>1 %</u>	<u>0 %</u>	<u>0 %</u>

### Investments Outlook

We believe investment income growth may slow in 2008 as managements of our financial sector holdings evaluate their dividend levels. Our buy-and-hold equity investing strategy has been key to the long-term growth

of our assets and shareholders' equity. Our common stock investments generally are securities with annual dividend yields that meet or exceed that of the overall market and have the potential for future dividend increases. Other criteria we evaluate include increasing sales and earnings, proven management and a favorable outlook. Over the years, these equities have generally offered a steadily increasing flow of dividend income along with the potential for capital appreciation.

We continue to focus on portfolio strategies to balance near-term income generation and long-term book value growth. In 2008, we expect to continue to allocate a proportion of cash available for investment to equity securities, taking into consideration insurance department regulations and ratings agency comments.

We believe a continuation of the current credit environment, if exacerbated by recessionary economic conditions, could lead to further declines in portfolio values and a resulting increase in other-than-temporary impairment charges in 2008. All but three securities in the portfolio were trading at or above 70 percent of book value at year-end 2007. Our asset impairment committee continues to monitor the investment portfolio. The current asset impairment policy is described in Critical Accounting Estimates, Asset Impairment, Page 40.

## **OTHER**

In 2007, other income of the insurance subsidiaries, parent company operations and non-investment operations of CFC Investment Company and CinFin Capital Management Company resulted in \$15 million in revenues compared with \$14 million in 2006 and \$12 million in 2005. Losses before income taxes of \$46 million in 2007 were primarily due to \$49 million in interest expense from debt of the parent company. Losses before income taxes were \$51 million and \$50 million in 2006 and 2005, when interest expense was \$51 million and \$52 million, respectively. An immaterial level of expenses for CSU Producer Resources was included in 2007.

## **TAXES**

Income tax expense was \$337 million in 2007 compared with \$399 million in 2006 and \$221 million in 2005. The effective tax rate for 2007 was 28.3 percent compared with 30.0 percent in 2006 and 26.8 percent in 2005.

The primary reason for the change in the effective tax rate was the level and timing of realized gains as discussed in Investments Results of Operations, Page 57. In 2007, we had pretax realized gains of \$382 million compared with pretax gains of \$684 million in 2006 and \$61 million in 2005. Growth in the tax-exempt municipal bond portfolio, higher investment income from dividends and changes in operating earnings over the periods also contributed to the change in the effective tax rate for 2007.

We pursue 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. For our insurance subsidiaries, approximately 85 percent of income from tax-advantaged fixed-maturity investments is exempt from federal tax. Our non-insurance companies own no tax-advantaged fixed-maturity investments. For our insurance subsidiaries, the dividend received deduction, after the dividend proration of the 1986 Tax Reform Act, exempts approximately 60 percent of dividends from qualified equities from federal tax. The dividend received deduction exempts 70 percent of dividends from qualified equities for our non-insurance companies. Details regarding our effective tax rate are found in Item 8, Note 10 of the Consolidated Financial Statements, Page 98.

## **LIQUIDITY AND CAPITAL RESOURCES**

Liquidity and capital resources represent the overall financial strength of our company and our ability to generate cash flows to meet the short- and long-term cash requirements of business obligations and growth needs. We seek to maintain prudent levels of liquidity and financial strength for the protection of our policyholders, creditors and shareholders. We manage liquidity at two levels. The first is the liquidity of the parent company. The second is the liquidity of our insurance subsidiary. The management of liquidity at both levels is essential because each has different funding needs and sources and each is subject to certain regulatory guidelines and requirements.

The parent company's primary means of meeting liquidity requirements are dividends from our insurance subsidiary and income from investments held at the parent-company level supported by our capital resources. At year-end 2007, we had shareholders' equity of \$5.929 billion and total debt of \$860 million. Our ability to access the capital markets and short-term bank borrowing provide other potential sources of liquidity. One way we seek to maintain financial strength is by keeping our ratio of debt to capital below 15 percent. Our parent company's cash requirements include dividends to shareholders, interest payments on our long-term debt, common stock repurchases and general operating expenses.

Our insurance subsidiary's primary sources of liquidity are collection of premiums and investment income. Its cash needs primarily consist of paying property casualty and life insurance loss and loss expenses as well as

ongoing operating expenses and payments of dividends to the parent company. Although we have never sold investments to pay claims, the sale of investments would provide an additional source of liquidity, if required. After satisfying operating cash requirements, cash flows are invested in fixed-maturity and equity securities, leading to the potential for increases in future investment income and unrealized appreciation.

## SOURCES OF LIQUIDITY AND CAPITAL RESOURCES

### Subsidiary Dividends

Our insurance subsidiary declared dividends to the parent company of \$420 million in 2007 and \$275 million in both 2006 and 2005. State of Ohio regulatory requirements restrict the dividends insurance subsidiaries can pay. During 2008, total dividends that our insurance subsidiary can pay to our parent company without regulatory approval are approximately \$658 million.

### Insurance Underwriting

Our property casualty and life insurance operations provide liquidity because premiums generally are received before losses are paid under the policies purchased with those premiums. After satisfying our cash requirements, we invest excess cash flows, increasing future investment income.

This table shows a summary of operating cash flow of the insurance subsidiary (direct method):

(In millions)	Years ended December 31,		
	2007	2006	2005
Premiums collected	\$ 3,256	\$ 3,285	\$ 3,187
Loss and loss expenses paid	(1,888)	(1,859)	(1,752)
Commissions and other underwriting expenses paid	(1,053)	(1,036)	(995)
Insurance subsidiary cash flow from underwriting	315	390	440
Investment income received	505	471	427
Insurance subsidiary operating cash flow	\$ 820	\$ 861	\$ 867

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. While first-year life insurance expenses normally exceed the premiums, subsequent premiums are used to generate investment income until the time the policy benefits are paid.

We believe that our insurance operations maintain sufficient liquidity to pay claims and operating expenses, as well as meet commitments in the event of unforeseen circumstances such as catastrophe losses, reinsurer insolvencies, changes in the timing of claims payments, increases in claims severity, reserve deficiencies or inadequate premium rates. We believe catastrophic events are the most likely cause of an unexpected rise in claims severity or frequency.

After payment of claims and operating expenses, cash flows from underwriting declined in 2007 and 2006, tracking with the changes in underwriting income discussed in Commercial Lines and Personal Lines Insurance Results of Operations, Pages 44 and 51. We discuss our future obligations for claims payments in Contractual Obligations, Page 63, and our future obligations for underwriting expenses in Other Commitments, Page 64. Insurance subsidiary operating cash flow remained relatively stable over the three years, however, due to rising investment income.

Based on our outlook for commercial lines, personal lines and life insurance, we believe that cash flows from underwriting could continue to decline in 2008. A lower level of cash flow available for investment could lead to lower investment income and reduced potential for future capital gains.

### Investing Activities

Investment income is a primary source of liquidity for both the parent company and insurance subsidiary. As we discuss under Investments Results of Operations, Page 57, investment income rose in each of the past three years. We anticipate slower growth in investment income in 2008 as our financial sector holdings evaluate their dividend levels. We continue to focus on portfolio strategies to balance near-term income generation and long-term book value growth.

Realized gains also can provide liquidity, although we follow a buy-and-hold investment philosophy seeking to compound cash flows over the long-term. When we dispose of investments, we generally reinvest the gains in new investment securities. Disposition of investments may occur for a number of reasons:

- Sales of fixed-maturity investments – The majority of our fixed-maturity securities are held until maturity. Any decision to sell or reduce a holding is executed either to improve long term total return prospects or in response to adverse credit concerns.
- Call or maturity of fixed-maturity investments – Calls and maturities of fixed-maturity investments are a function of the yield curve. The pace of calls of fixed maturities, including U.S. Agency paper, began to rise in 2007 as interest rates shifted lower in the second half of the year.

- Sales of equity securities investments – The decision to divest an equity position generally is reached after careful analysis of the direction the company is headed and its ability to meet our investment parameters. In 2007 and 2006, we sold a portion of our ExxonMobil common stock holding, completed the sale of our Alltel and FirstMerit common stock holdings and made other sales of all or part of smaller holdings, including divesting the majority of our REIT holdings. We sold a portion of our Fifth Third position in 2007 to fund an accelerated share repurchase program.

We generally have substantial discretion in the timing of investment sales and, therefore, the resulting gains or losses to be recognized in any period. That discretion generally is independent of the insurance underwriting process. In 2008, we expect to continue to limit the disposition of investments to those that no longer meet our investment parameters or those that reach maturity or are called by the issuer. The sale of equity investments that no longer meet our investment criteria can provide cash for investment in common stocks that we perceive to have greater potential for dividend growth and capital appreciation.

## **Sources of Capital**

As a long-term investor, we historically have followed a buy-and-hold investing strategy. This policy has generated a significant amount of unrealized appreciation on equity investments. Total unrealized appreciation in the investment portfolio, before deferred income taxes, declined to \$3.339 billion from \$5.244 billion at year-end 2007 and 2006, respectively, because of market value declines of our equity holdings. On an after-tax basis, it constituted 36.6 percent of total shareholders' equity at year-end 2007.

At year-end 2007, our debt-to-capital ratio was 12.7 percent. Based on our present capital requirements, we do not anticipate a material increase in debt levels during 2008. As a result, we believe that changes in our debt-to-capital ratio will be a function of the contribution of unrealized investment gains or losses to shareholders' equity. We estimate that changes in that measure would not be sufficient to increase the debt-to-capital ratio above our target cap of 15 percent.

We had \$791 million of long-term debt and \$69 million in borrowings on our short-term lines of credit at year-end 2007. We generally have minimized our reliance on debt financing although we may utilize lines of credit to fund short-term cash needs.

We provide details of our three long-term notes in Item 8, Note 7 of the Consolidated Financial Statements, Page 96. None of the notes are encumbered by rating triggers.

Four independent credit rating organizations affirmed Cincinnati Financial Corporation's debt ratings in 2007, maintaining stable outlooks on the ratings. On May 21, 2007, A.M. Best affirmed its aa- senior debt ratings and issuer credit rating. On July 26, 2007, Standard & Poor's Ratings Services affirmed its A counterparty credit rating. On September 18, 2007, Moody's Investors Service affirmed its A2 senior debt rating. On October 8, 2007, Fitch Ratings affirmed its AA- issuer default rating and A+ senior debt ratings.

At year-end 2007, we had two lines of credit with commercial banks amounting to \$225 million with an outstanding balance of \$69 million. One line of credit for \$75 million was established more than five years ago and has no financial covenants. This line of credit matures on June 30, 2008, and we expect to renew it under terms and conditions that are essentially unchanged.

The second line of credit is an unsecured \$150 million line of credit from Huntington Bancshares established in 2007 that will mature in 2012. It is available for general corporate purposes and contains customary financial covenants.

## **Off-balance Sheet Arrangements**

We do not utilize 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 AND CAPITAL RESOURCES

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

At December 31, 2007, we estimated our future contractual obligations as follows:

(In millions)	Payment due by period				Total
	Less than 1 year	Years 1-3	Years 4-5	More than 5 years	
Interest on long-term debt	\$ 52	\$ 104	\$ 104	\$ 944	\$ 1,204
Long-term debt	0	0	0	795	795
Short-term debt	69	0	0	0	69
Profit-sharing commissions	102	0	0	0	102
Headquarters building expansion	16	0	0	0	16
Capital lease obligations	5	9	1	0	15
Computer hardware and software	4	4	2	0	10
Other invested assets	12	15	11	4	42
Liability for uncertain tax positions	2	11	1	0	14
Subtotal	<u>262</u>	<u>143</u>	<u>119</u>	<u>1,743</u>	<u>2,267</u>
Gross property casualty loss and loss expense payments (1)	1,193	1,320	582	830	3,925
Gross life policyholder obligations (2)	30	49	92	3,611	3,782
Total	<u>\$ 1,485</u>	<u>\$ 1,512</u>	<u>\$ 793</u>	<u>\$ 6,184</u>	<u>\$ 9,974</u>

(1) Gross property casualty loss and loss expense payments – Our estimate of gross property casualty loss and loss expense payments of \$3.925 billion is lower than loss and loss expense reserves of \$3.967 billion as of year-end 2007. The \$42 million difference is due to life and health losses, as discussed in Item 8, Note 4 of the Consolidated Financial Statements, Page 95.

We believe that our insurance subsidiaries maintain sufficient liquidity to pay claims and operating expenses, as well as meet commitments in the event of unforeseen circumstances such as catastrophe losses, reinsurer insolvencies, changes in the timing of claims payments, increases in claims severity, reserve deficiencies or inadequate premium rates. We believe catastrophic events are the most likely cause of an unexpected rise in claims severity or frequency.

While we believe that historical performance of property casualty and life loss payment patterns is a reasonable source for projecting future claims payments, there is inherent uncertainty in this estimate of contractual obligations. We believe that we could meet our obligations under a significant and unexpected change in the timing of these payments because of the liquidity of our invested assets, strong financial position and access to lines of credit.

Our estimates of gross property casualty loss and loss expense payments also do not include reinsurance receivables or ceded losses. As discussed in 2008 Reinsurance Programs, Page 70, we purchase reinsurance to mitigate our property casualty risk exposure. Ceded property casualty reinsurance receivables of \$528 million at year-end 2007 offset our gross property casualty loss and loss expense obligations. Our reinsurance program mitigates the liquidity risk of a single large loss or an unexpected rise in claims severity or frequency due to a catastrophic event. Reinsurance does not relieve us of our obligation to pay covered claims. The financial strength of our reinsurers is important because our ability to recover for losses under one of our reinsurance agreements depends on the financial viability of the reinsurer.

We direct our associates and agencies to settle claims and pay losses as quickly as practical and made \$1.791 billion in net claim payments during 2007. At year-end 2007, net property casualty reserves reflected \$1.901 billion in unpaid amounts on reported claims (case reserves), \$808 million in loss expense reserves and \$688 million in estimates of incurred but not yet reported claims. The specific amounts and timing of obligations related to case reserves and associated loss expenses are not set contractually. The amounts and timing of obligations for IBNR claims and related loss expenses are unknown. We discuss the adequacy of our loss and loss expense reserves in Critical Accounting Estimates, Property Casualty Insurance Loss and Loss Expense Reserves, Page 37.

The historic pattern of using premium receipts for the payment of loss and loss expenses has enabled us to extend slightly the maturities of our investment portfolio beyond the estimated settlement date of the loss reserves. The effective duration of our fixed-maturity portfolio was 4.84 years at year-end 2007. By contrast, the duration of our loss and loss expense reserves was 3.21 years, and the duration of all liabilities was 2.86 years. We believe this difference in duration does not affect our ability to meet current obligations because cash flow from operations is sufficient to meet these obligations. In addition, our investment strategy has led to substantial unrealized gains from holdings in equity securities. These equity holdings could be liquidated, if necessary, to meet higher than anticipated loss and loss expenses.

(2) Gross life policyholder obligations - Our estimates of life, annuity and disability policyholder obligations reflect future estimated cash payments to be made to policyholders for future policy benefits, policyholders' account balances and separate account liabilities. These estimates include death and disability claims, policy surrenders, policy maturities, annuity payments, minimum guarantees on separate account products, commissions and premium taxes offset by expected future deposits and premiums on in-force contracts.

Our estimates of gross life, annuity and disability obligations do not reflect net recoveries from reinsurance agreements. Ceded life reinsurance receivables were \$208 million at year-end 2007. As discussed in 2008 Reinsurance Programs, Page 70, we purchase reinsurance to mitigate our life insurance risk exposure. At year-end 2007, ceded death benefits represented approximately 53.3 percent of our total policy face amounts in force.

These estimated cash outflows are undiscounted with respect to interest. As a result, the sum of the cash outflows shown for all years of \$3.782 billion (total of life insurance obligations) exceeds the liabilities recorded in life policy reserves and separate accounts for future policy benefits and claims of \$2.037 billion (total of life insurance policy reserves and separate account policy reserves). Separate account policy reserves make up all but \$10 million of separate accounts liabilities.

We have made significant assumptions to determine the estimated undiscounted cash flows of these policies and contracts that include mortality, morbidity, future lapse rates and interest crediting rates. Due to the significance of the assumptions used, the amounts presented could materially differ from actual results.

Factors contributing to our estimation of other future contractual obligations include:

- Interest on long-term debt – Our interest expense remained unchanged in 2007 at an annual rate of approximately \$52 million. We generally have tried to minimize our reliance on debt financing and do not expect a material increase in interest expense from long-term debt in the near future.
- Short-term debt – We plan to renew our \$69 million outstanding note payable drawn on our lines of credit.
- Headquarters building expansion – The construction project is on schedule and on budget. We expect construction to be completed by July 2008.
- Contingent commissions – Contingent, or profit-sharing, commissions are paid to agencies using a formula that takes into account agency profitability and other factors. We estimate 2008 contingent commission payments of approximately \$102 million.
- Computer hardware and software – We expect to need approximately \$10 million over the next five years for current material commitments for computer hardware and software, including maintenance contracts on hardware and other known obligations. We discuss below the non-contractual expenses we anticipate for computer hardware and software in 2008.

## Other Commitments

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

- Commissions – As discussed above, commissions paid rose in each the past two years, reflecting the operating expense trends we discuss in the Commercial Lines and Personal Lines Insurance Results of Operations, Page 44 and Page 51. Commission payments generally track with written premiums.
- Other operating expenses – Many of our operating expenses are not contractual obligations, but reflect the ongoing expenses of our business. Non-commission operating expenses paid rose in the past two years. Staffing is the largest component of our operating expenses and is expected to rise again in 2008, reflecting the 1.7 percent average annual growth in our associate base over the past three years. Our associate base has grown as we focus on enhancing service to our agencies and staffing additional field territories. In 2008, we also anticipate an additional \$9 million of expenses related to associate benefit plan modifications. Our benefit plans help us retain experienced associates, attract new talent and provide a measure of security and stability to associates and their families.

In addition to contractual obligations for hardware and software, we anticipate capitalizing \$8 million in spending for key technology initiatives in 2008. Technology projects for 2008 are discussed in Item 1, Technology Solutions, Page 4. Capitalized development costs related to key technology initiatives totaled \$6 million in 2007. These activities are conducted at our discretion, and we have no material contractual obligations for activities planned as part of these projects.

- Disaster recovery and backup data processing center – We expect to spend approximately \$26 million in 2008 and 2009 to begin renovation of a newly purchased building that will serve as our disaster recovery and backup data processing center.
- Qualified pension plan – We anticipate a cash contribution of \$10 million to pension plan assets in 2008. Our results of operation will reflect an anticipated \$19 million expense related to an increase in accrued pension benefits.

## 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. See Item 1, Investments Segment, Page 15, for a discussion of our investment strategy, portfolio allocation and quality.

## Uses of Capital

Uses of cash to enhance shareholder return include:

- Dividends to shareholders – Over the past 10 years, the company has paid an average of 37 percent of net income as dividends, with the remaining 63 percent available to reinvest for future growth and for share repurchases. The ability of the company to continue paying cash dividends is subject to factors the board of directors may deem relevant.

In February 2008, the board of directors authorized a 9.9 percent increase in the regular quarterly cash dividend to an indicated annual rate of \$1.56 per share. In 2007, 2006 and 2005, we paid cash dividends of \$240 million, \$228 million and \$204 million.

- Common stock repurchase – Our board believes that stock repurchases can help fulfill our commitment to enhancing shareholder value. Consequently, the board has authorized the repurchase of outstanding shares. Common stock repurchases for treasury were a record in 2007, building from the steady pace of the last several years. Repurchases occur when we believe that stock prices on the open market are favorable for such repurchases. Our corporate code of conduct restricts repurchases during certain time



periods. At a minimum, we would expect repurchases to offset dilution from share-based compensation. In 2007, 2006 and 2005, we used \$306 million, \$118 million and \$63 million for share repurchase.

Repurchase activity in 2007 included open market purchases, two private transactions (at market prices) and an ASR agreement under which 4 million shares were purchased at an average price of \$39.20. In conjunction with the authorization for the ASR, the board increased its repurchase authorization to an additional 13 million shares.

The details of the repurchase authorizations and activity are described in Item 5, Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities, Page 27. Between February 1999 and year-end 2007, we have repurchased 24.9 million shares at a total cost to the company of \$967 million. We do not adjust the number of shares repurchased and average price per repurchased share for stock dividends.

## **PROPERTY CASUALTY INSURANCE RESERVES**

### **Range of Reasonable Reserves**

The company established a reasonably likely range for net loss and loss expense reserves of \$3.132 billion to \$3.427 billion at year-end 2007, carrying net reserves of \$3.397 billion. The likely range was \$3.097 billion to \$3.380 billion at year-end 2006, with the company carrying net reserves of \$3.356 billion. Our loss and loss expense reserves are not discounted, but we have reduced the reserves by an estimate of the amount of salvage and subrogation payments we expect to recover. We provide a reconciliation of the property casualty reserves with the loss and loss expense reserve as shown on the balance sheet in Item 8, Note 4 of the Consolidated Financial Statements, Page 95.

The low point of each year's range corresponds to approximately one standard error below each year's mean reserve estimate, while the high point corresponds to approximately one standard error above each year's mean reserve estimate. We discussed management's reasons for basing reasonably likely reserve ranges on standard errors in Reserve Estimate Variability above.

The ranges reflect our assessment of the most likely unpaid loss and loss expenses at year-end 2007 and 2006. However, actual unpaid loss and loss expenses could nonetheless fall outside of the indicated ranges.

Management's best estimate of total loss reserves as of year-end 2007 was consistent with the corresponding actuarial best estimate. Management's best estimate as of year-end 2006 was above the corresponding actuarial best estimate. Our inter-departmental committee, which includes our actuarial management team, chose a higher estimate for two reasons. First, we incurred three unusually large workers' compensation claims in accident year 2006 that totaled \$12 million. The historical reserving data used to derive the actuarial best estimate for this line of business did not fully reflect those three losses. Second, management recognized the potential for a higher level of loss expense inflation for the commercial casualty line than was reflected in the actuarial best estimate. Management chose the higher level because of a rise in loss expense inflation between 2004 and 2006.

### **Development of Loss and Loss Expenses**

We reconcile the beginning and ending balances of our reserves for loss and loss expenses at December 31, 2007, 2006 and 2005, in Item 8, Note 4 of the Consolidated Financial Statements, Page 95. The reconciliation of our year-end 2006 reserve balance to net incurred losses one year later recognizes approximately \$244 million of redundant reserves.

The table below shows the development of the estimated reserves for loss and loss expenses the past 10 years.

- Section A shows our total property casualty loss and loss expense reserves recorded at the balance sheet date for each of the indicated calendar years on a gross and net basis. Those reserves represent the estimated amount of unpaid loss and loss expenses for claims arising in the indicated calendar year and all prior accident years at the balance sheet date, including losses that were incurred but not yet reported to the company.
- Section B shows the cumulative net amount paid with respect to the previously recorded reserve as of the end of each succeeding year. For example, as of December 31, 2007, we had paid \$1.295 billion of loss and loss expenses in calendar years 1998 through 2007 for losses that occurred in accident years 1997 and prior. An estimated \$171 million of losses remained unpaid as of year-end 2007 (net re-estimated reserves of \$1.466 billion from Section C less cumulative paid loss and loss expenses of \$1.295 billion).
- Section C shows the re-estimated amount of the previously reported reserves based on experience as of the end of each succeeding year. The estimate is increased or decreased as we learn more about the frequency and severity of claims.
- Section D, cumulative net redundancy, represents the aggregate change in the estimates for all years subsequent to the year the reserves were initially established. For example, reserves established at

December 31, 1997, had developed a \$311 million redundancy over 10 years, net of reinsurance, which was reflected in income over the 10 years. The table shows favorable development in redundant reserves as a negative number. The effects on income in 2007, 2006 and 2005 of changes in estimates of the reserves for loss and loss expenses for all accident years are shown in the reconciliation below.

In evaluating the development of our estimated reserves for loss and loss expenses for the past 10 years, note that each amount includes the effects of all changes in amounts for prior periods. For example, payments or reserve adjustments related to losses settled in 2007 but incurred in 2001 are included in the cumulative deficiency or redundancy amount for 2001 and each subsequent year. In addition, this table presents calendar year data, not accident or policy year development data, which readers may be more accustomed to analyzing. Conditions and trends that affected development of the reserves in the past may not necessarily occur in the future. Accordingly, it may not be appropriate to extrapolate future redundancies or deficiencies based on this data.

Differences between the property casualty reserves reported in the accompanying consolidated balance sheets (prepared in accordance with GAAP) and those same reserves reported in the annual statements (filed with state insurance departments in accordance with statutory accounting practices – SAP), relate principally to the reporting of reinsurance recoverables, which are recognized as receivables for GAAP and as an offset to reserves for SAP.

(In millions)	Calendar year ended December 31,										
	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
A. Originally reported reserves for unpaid loss and loss expenses:											
Gross of reinsurance	\$ 1,889	\$ 1,978	\$ 2,093	\$ 2,401	\$ 2,865	\$ 3,150	\$ 3,386	\$ 3,514	\$ 3,629	\$ 3,860	\$ 3,925
Reinsurance recoverable	112	138	161	219	513	542	541	537	518	504	528
Net of reinsurance	<u>\$ 1,777</u>	<u>\$ 1,840</u>	<u>\$ 1,932</u>	<u>\$ 2,182</u>	<u>\$ 2,352</u>	<u>\$ 2,608</u>	<u>\$ 2,845</u>	<u>\$ 2,977</u>	<u>\$ 3,111</u>	<u>\$ 3,356</u>	<u>\$ 3,397</u>
B. Cumulative net paid as of:											
One year later	\$ 499	\$ 522	\$ 591	\$ 697	\$ 758	\$ 799	\$ 817	\$ 907	\$ 944	\$ 1,006	
Two years later	761	833	943	1,116	1,194	1,235	1,293	1,426	1,502		
Three years later	965	1,067	1,195	1,378	1,455	1,519	1,626	1,758			
Four years later	1,075	1,207	1,327	1,526	1,614	1,716	1,823				
Five years later	1,152	1,283	1,412	1,623	1,717	1,823					
Six years later	1,205	1,333	1,464	1,680	1,778						
Seven years later	1,239	1,366	1,496	1,717							
Eight years later	1,260	1,390	1,520								
Nine years later	1,279	1,409									
Ten years later	1,295										
C. Net reserves re-estimated as of:											
One year later	\$ 1,623	\$ 1,724	\$ 1,912	\$ 2,120	\$ 2,307	\$ 2,528	\$ 2,649	\$ 2,817	\$ 2,995	\$ 3,112	
Two years later	1,551	1,728	1,833	2,083	2,263	2,377	2,546	2,743	2,871		
Three years later	1,520	1,636	1,802	2,052	2,178	2,336	2,489	2,657			
Four years later	1,465	1,615	1,771	2,010	2,153	2,299	2,452				
Five years later	1,466	1,608	1,757	1,999	2,127	2,276					
Six years later	1,463	1,602	1,733	1,992	2,122						
Seven years later	1,460	1,577	1,739	1,994							
Eight years later	1,435	1,593	1,746								
Nine years later	1,456	1,603									
Ten years later	1,466										
D. Cumulative net redundancy as of:											
One year later	\$ (154)	\$ (116)	\$ (20)	\$ (62)	\$ (45)	\$ (80)	\$ (196)	\$ (160)	\$ (116)	\$ (244)	
Two years later	(226)	(112)	(99)	(99)	(89)	(231)	(299)	(234)	(240)		
Three years later	(257)	(204)	(130)	(130)	(174)	(272)	(356)	(320)			
Four years later	(312)	(225)	(161)	(172)	(199)	(309)	(393)				
Five years later	(311)	(232)	(175)	(183)	(225)	(332)					
Six years later	(314)	(238)	(199)	(190)	(230)						
Seven years later	(317)	(263)	(193)	(188)							
Eight years later	(342)	(247)	(186)								
Nine years later	(321)	(237)									
Ten years later	(311)										
Net reserves re-estimated—latest	\$ 1,466	\$ 1,603	\$ 1,746	\$ 1,994	\$ 2,122	\$ 2,276	\$ 2,452	\$ 2,657	\$ 2,871	\$ 3,112	
Re-estimated recoverable—latest	188	214	223	257	537	591	584	637	641	532	
Gross liability re-estimated—latest	<u>\$ 1,654</u>	<u>\$ 1,817</u>	<u>\$ 1,969</u>	<u>\$ 2,251</u>	<u>\$ 2,659</u>	<u>\$ 2,867</u>	<u>\$ 3,036</u>	<u>\$ 3,294</u>	<u>\$ 3,512</u>	<u>\$ 3,644</u>	
Cumulative gross redundancy	<u>\$ (235)</u>	<u>\$ (161)</u>	<u>\$ (124)</u>	<u>\$ (150)</u>	<u>\$ (206)</u>	<u>\$ (283)</u>	<u>\$ (350)</u>	<u>\$ (220)</u>	<u>\$ (117)</u>	<u>\$ (216)</u>	

### Asbestos and Environmental Reserves

We carried \$123 million of net loss and loss expense reserves for asbestos and environmental claims as of year-end 2007, compared with \$131 million for such claims as of year-end 2006. These amounts constitute 3.6 percent and 3.9 percent of total loss and loss expense reserves as of these year-end dates.

We believe our exposure to asbestos and environmental claims is limited, largely because our reinsurance retention was \$500,000 or below prior to 1987. We also predominantly were a personal lines company in the 1960s and 1970s when asbestos and pollution exclusions were not widely used. During the 1980s and early 1990s, commercial lines grew as a percentage of our overall business and our exposure to asbestos and environmental claims grew accordingly. Over that period, we endorsed to or included in most policies an asbestos and environmental exclusion.

Additionally, since 2002, we have revised policy terms where permitted by state regulation to limit our exposure to mold claims prospectively and further reduce our exposure to other environmental claims generally. Finally, we have not engaged in any mergers or acquisitions through which such a liability could have been assumed. We continue to monitor our claims for evidence of material exposure to other mass tort classes such as silicosis, but we have found no such credible evidence to date.

Reserving data for asbestos and environmental claims has characteristics that limit the usefulness of the methods and models used to analyze loss and loss expense reserves for other claims. Specifically, asbestos and environmental loss and loss expenses for different accident years do not emerge independently of one another as loss development and Bornhuetter-Ferguson methods assume. In addition, asbestos and environmental loss and loss expense data available to date does not reflect a well-defined tail, greatly complicating the identification of an appropriate probabilistic trend family model.

Due to these considerations, our actuarial staff elected to use a paid survival ratio method to estimate reserves for incurred but not yet reported asbestos and environmental claims. Although highly uncertain, reserve estimates obtained via this method have held up reasonably well since 2004. Between 2005 and 2007, total asbestos and environmental reserves decreased 1.3 percent. Our exposure to such claims is limited, therefore, we do not believe that a more detailed reserve analysis would be an appropriate use of resources.

### Commercial Lines Insurance Segment Reserves

For the business lines in the commercial lines insurance segment, the following table shows the breakout of gross reserves among case, IBNR and loss expense reserves. The rise in total gross reserves for our commercial business lines is partially due to normal loss cost inflation and exposure growth in our commercial casualty and workers' compensation business lines. The increase also reflected higher loss expense reserves due to a claims mediation process that promoted earlier liability settlement resolution and to increased legal fees. In addition, commercial casualty gross reserves rose because of the increase in large losses as we discussed in Commercial Lines Insurance Results of Operations, Page 44.

(In millions)	Loss reserves		Loss	Total	Percent
	Case	IBNR	expense	gross	of total
	reserves	reserves	reserves	reserves	
<b>At December 31, 2007</b>					
Commercial casualty	\$ 1,035	\$ 389	\$ 524	\$ 1,948	55.1 %
Commercial property	104	6	29	139	3.9
Commercial auto	276	48	65	389	11.0
Workers' compensation	426	315	119	860	24.3
Specialty packages	67	1	9	77	2.3
Surety and executive risk	68	2	42	112	3.2
Machinery and equipment	4	3	1	8	0.2
Total	<u>\$ 1,980</u>	<u>\$ 764</u>	<u>\$ 789</u>	<u>\$ 3,533</u>	<u>100.0 %</u>
<b>At December 31, 2006</b>					
Commercial casualty	\$ 923	\$ 437	\$ 483	\$ 1,843	54.0 %
Commercial property	132	31	36	199	5.8
Commercial auto	274	52	64	390	11.4
Workers' compensation	411	277	99	787	23.1
Specialty packages	80	1	5	86	2.5
Surety and executive risk	67	1	32	100	2.9
Machinery and equipment	5	3	1	9	0.3
Total	<u>\$ 1,892</u>	<u>\$ 802</u>	<u>\$ 720</u>	<u>\$ 3,414</u>	<u>100.0 %</u>

The following table shows net reserve changes at year-end 2007, 2006 and 2005 by commercial line of business and accident year:

(Dollars in millions)	Commercial casualty	Commercial property	Commercial auto	Workers' compensation	Specialty packages	Surety & executive risk	Machinery & equipment	Totals
<b>As of December 31, 2007</b>								
2006 accident year	\$ (70)	\$ (4)	\$ (15)	\$ (20)	\$ 1	\$ 3	\$ (1)	\$ (106)
2005 accident year	(22)	(13)	(6)	0	2	3	(1)	(37)
2004 accident year	(34)	(1)	1	1	(1)	(1)	0	(35)
2003 accident year	(2)	0	(3)	(1)	0	(3)	0	(9)
2002 accident year	(15)	(1)	1	5	(1)	(3)	0	(14)
2001 accident year	(8)	0	(1)	2	0	1	0	(6)
2000 and prior accident years	2	0	(2)	3	0	1	0	4
Deficiency/(redundancy)	<u>\$ (149)</u>	<u>\$ (19)</u>	<u>\$ (25)</u>	<u>\$ (10)</u>	<u>\$ 1</u>	<u>\$ 1</u>	<u>\$ (2)</u>	<u>\$ (203)</u>
Reserves estimated as of December 31, 2006	\$ 1,483	\$ 170	\$ 386	\$ 713	\$ 84	\$ 83	\$ 9	\$ 2,928
Reserves re-estimated as of December 31, 2007	<u>1,334</u>	<u>151</u>	<u>361</u>	<u>703</u>	<u>85</u>	<u>84</u>	<u>7</u>	<u>2,725</u>
Deficiency/(redundancy)	<u>\$ (149)</u>	<u>\$ (19)</u>	<u>\$ (25)</u>	<u>\$ (10)</u>	<u>\$ 1</u>	<u>\$ 1</u>	<u>\$ (2)</u>	<u>\$ (203)</u>
<b>As of December 31, 2006</b>								
2005 accident year	\$ (52)	\$ 17	\$ (17)	\$ (2)	\$ 3	\$ 7	\$ 1	\$ (43)
2004 accident year	(21)	(3)	1	5	(1)	(3)	0	(22)
2003 accident year	(12)	(3)	1	0	1	(1)	0	(14)
2002 accident year	2	(1)	(2)	(3)	0	1	0	(3)
2001 accident year	(9)	(4)	(2)	(1)	0	1	0	(15)
2000 accident year	(9)	(1)	(1)	1	(1)	0	0	(11)
1999 and prior accident years	2	0	(1)	9	0	0	0	10
Deficiency/(redundancy)	<u>\$ (99)</u>	<u>\$ 5</u>	<u>\$ (21)</u>	<u>\$ 9</u>	<u>\$ 2</u>	<u>\$ 5</u>	<u>\$ 1</u>	<u>\$ (98)</u>
Reserves estimated as of December 31, 2005	\$ 1,359	\$ 160	\$ 386	\$ 634	\$ 73	\$ 63	\$ 6	\$ 2,681
Reserves re-estimated as of December 31, 2006	<u>1,260</u>	<u>165</u>	<u>365</u>	<u>643</u>	<u>75</u>	<u>68</u>	<u>7</u>	<u>2,583</u>
Deficiency/(redundancy)	<u>\$ (99)</u>	<u>\$ 5</u>	<u>\$ (21)</u>	<u>\$ 9</u>	<u>\$ 2</u>	<u>\$ 5</u>	<u>\$ 1</u>	<u>\$ (98)</u>
<b>As of December 31, 2005</b>								
2004 accident year	\$ (78)	\$ 23	\$ (15)	\$ 9	\$ 7	\$ 2	\$ (1)	\$ (53)
2003 accident year	(51)	(3)	(5)	13	3	(4)	0	(47)
2002 accident year	(17)	(3)	(1)	8	2	0	0	(11)
2001 accident year	(7)	(1)	(1)	3	0	(1)	0	(7)
2000 accident year	8	0	0	3	2	0	0	13
1999 accident year	(1)	0	0	3	0	0	0	2
1998 and prior accident years	(25)	1	(1)	2	1	(1)	0	(23)
Deficiency/(redundancy)	<u>\$ (171)</u>	<u>\$ 17</u>	<u>\$ (23)</u>	<u>\$ 41</u>	<u>\$ 15</u>	<u>\$ (4)</u>	<u>\$ (1)</u>	<u>\$ (126)</u>
Reserves estimated as of December 31, 2004	\$ 1,332	\$ 104	\$ 372	\$ 558	\$ 72	\$ 64	\$ 5	\$ 2,507
Reserves re-estimated as of December 31, 2005	<u>1,161</u>	<u>121</u>	<u>349</u>	<u>599</u>	<u>87</u>	<u>60</u>	<u>4</u>	<u>2,381</u>
Deficiency/(redundancy)	<u>\$ (171)</u>	<u>\$ 17</u>	<u>\$ (23)</u>	<u>\$ 41</u>	<u>\$ 15</u>	<u>\$ (4)</u>	<u>\$ (1)</u>	<u>\$ (126)</u>

The overall favorable development recorded for the commercial lines reserves illustrates the potential for revisions inherent in estimating reserves, especially for long-tail lines such as commercial casualty. Commercial lines reserve development over the past three years was consistent with:

- The initiative, begun in 2001 and expanded to other states in 2004, to use a claims mediation process that promotes earlier liability settlement resolution
- Increased loss expenses due to higher legal fees
- Workers' compensation claim reserving practices
- Higher than expected medical inflation affecting the workers' compensation line
- Changes in reinsurance treaty retentions
- Settlements that differed from the established case reserves
- Changes in case reserves based on new information for specific claims or classes of claims
- Differences in the timing of actual settlements compared with the payout patterns assumed in the accident year IBNR reductions
- Lower risk profile after 2001 due to commercial lines underwriting initiatives
- Recognition of favorable case reserve development
- Implementation of Claims Management System in 2003 and 2004

## Personal Lines Insurance Segment Reserves

For the business lines in the personal lines insurance segment, the following table shows the breakout of gross reserves among case, IBNR and loss expense reserves. Total gross reserves were down slightly from year-end 2006 due to the decline in premiums and exposures for this segment. Homeowner gross reserves also reflected a lower level of catastrophe losses in 2007 as we discussed in Personal Lines Insurance Results of Operations, Page 51.

(In millions)	Loss reserves		Loss expense reserves	Total gross reserves	Percent of total
	Case reserves	IBNR reserves			
<b>At December 31, 2007</b>					
Personal auto	\$ 163	\$ (4)	\$ 30	\$ 189	48.2 %
Homeowners	61	8	14	83	21.0
Other personal	54	54	12	120	30.8
Total	<u>\$ 278</u>	<u>\$ 58</u>	<u>\$ 56</u>	<u>\$ 392</u>	<u>100.0 %</u>
<b>At December 31, 2006</b>					
Personal auto	\$ 169	\$ 5	\$ 32	\$ 206	46.2 %
Homeowners	69	24	17	110	24.7
Other personal	55	61	14	130	29.1
Total	<u>\$ 293</u>	<u>\$ 90</u>	<u>\$ 63</u>	<u>\$ 446</u>	<u>100.0 %</u>

The following table shows net reserve changes at year-end 2007, 2006 and 2005 by personal line of business and accident year:

(Dollars in millions)	Personal auto	Homeowner	Other personal	Totals
<b>As of December 31, 2007</b>				
2006 accident year	\$ 3	\$ (7)	\$ (11)	\$ (15)
2005 accident year	5	0	(5)	0
2004 accident year	(2)	(3)	(10)	(15)
2003 accident year	(3)	(1)	(1)	(5)
2002 accident year	(1)	0	(4)	(5)
2001 accident year	0	0	(1)	(1)
2000 and prior accident years	0	1	(1)	0
Deficiency/(redundancy)	<u>\$ 2</u>	<u>\$ (10)</u>	<u>\$ (33)</u>	<u>\$ (41)</u>
Reserves estimated as of December 31, 2006	\$ 206	\$ 104	\$ 118	\$ 428
Reserves re-estimated as of December 31, 2007	208	94	85	387
Deficiency/(redundancy)	<u>\$ 2</u>	<u>\$ (10)</u>	<u>\$ (33)</u>	<u>\$ (41)</u>
<b>As of December 31, 2006</b>				
2005 accident year	\$ 4	\$ 5	\$ (7)	\$ 2
2004 accident year	6	1	(2)	5
2003 accident year	(3)	0	(4)	(7)
2002 accident year	(2)	(1)	(4)	(7)
2001 accident year	(2)	0	(2)	(4)
2000 accident year	(1)	0	(3)	(4)
1999 and prior accident years	0	0	(3)	(3)
Deficiency/(redundancy)	<u>\$ 2</u>	<u>\$ 5</u>	<u>\$ (25)</u>	<u>\$ (18)</u>
Reserves estimated as of December 31, 2005	\$ 213	\$ 99	\$ 118	\$ 430
Reserves re-estimated as of December 31, 2006	215	104	93	412
Deficiency/(redundancy)	<u>\$ 2</u>	<u>\$ 5</u>	<u>\$ (25)</u>	<u>\$ (18)</u>
<b>As of December 31, 2005</b>				
2004 accident year	\$ 0	\$ 0	\$ (5)	\$ (5)
2003 accident year	0	(2)	(11)	(13)
2002 accident year	(3)	0	(3)	(6)
2001 accident year	(4)	0	(3)	(7)
2000 accident year	(1)	0	0	(1)
1999 accident year	0	1	0	1
1998 and prior accident years	0	0	(3)	(3)
Deficiency/(redundancy)	<u>\$ (8)</u>	<u>\$ (1)</u>	<u>\$ (25)</u>	<u>\$ (34)</u>
Reserves estimated as of December 31, 2004	\$ 231	\$ 114	\$ 125	\$ 470
Reserves re-estimated as of December 31, 2005	223	113	100	436
Deficiency/(redundancy)	<u>\$ (8)</u>	<u>\$ (1)</u>	<u>\$ (25)</u>	<u>\$ (34)</u>

The overall favorable development recorded for the personal lines segment reserves illustrates the potential for revisions inherent in estimating reserves. Personal lines reserve development over the past three years was consistent with:

- Settlements that differed from the established case reserves
- Changes in reinsurance treaty retentions

- Changes in case reserves based on new information for specific claims or classes of claims
- Differences in the timing of actual settlements compared with the payout patterns assumed in the accident year IBNR reductions
- Implementation of Claims Management System in 2003 and 2004

## **LIFE INSURANCE RESERVES**

Gross life policy reserves were \$1.478 billion at year-end 2007, compared with \$1.409 billion at year-end 2006. We establish reserves for traditional life insurance policies based on expected expenses, mortality, morbidity, withdrawal rates 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. We use our own experience and historical trends for setting our assumptions for expected expenses. We base our assumptions for expected investment income on our own experience adjusted for current economic conditions.

We establish reserves for our universal life, deferred annuity and investment contracts equal to the cumulative account balances, which include premium deposits plus credited interest less charges and withdrawals. Some of our universal life insurance 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.

We regularly review our life insurance business to ensure that any deferred acquisition cost associated with the business is recoverable and that our actuarial liabilities (life insurance segment reserves) make sufficient provision for future benefits and related expenses.

## **2008 REINSURANCE PROGRAMS**

A single large loss or an unexpected rise in claims severity or frequency due to a catastrophic event could present us with a liquidity risk. In an effort to control such losses, we forego marketing property casualty insurance in specific geographic areas, monitor our exposure in certain coastal regions, review aggregate exposures to huge disasters and purchase reinsurance. We use the Risk Management Solutions (RMS) and Applied Insurance Research (AIR) models to evaluate exposures to a once-in-a-100 year and a once-in-a-250 year event to help determine appropriate reinsurance coverage programs. In conjunction with these activities, we also continue to evaluate information provided by our reinsurance broker. These various sources explore and analyze credible scientific evidence, including the impact of global climate change, which may affect our exposure under insurance policies.

Reinsurance mitigates the risk of highly uncertain exposures and limits the maximum net loss that can arise from large risks or risks concentrated in areas of exposure. Management's decisions regarding 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. Reinsurance does not relieve us of our obligation to pay covered claims. The financial strength of our reinsurers is important because our ability to recover for losses covered under any reinsurance agreement depends on the financial viability of the reinsurer.

Currently participating on our standard market property and casualty per-risk and per-occurrence programs are Hannover Reinsurance Company, Munich Reinsurance America, Partner Reinsurance Company of the U.S. and Swiss Reinsurance America Corporation, all of which have A.M. Best insurer financial strength ratings of A (Excellent) or A+ (Superior). Our property catastrophe program is subscribed through a broker by reinsurers from the United States, Bermuda, London and the European markets.

Primary components of the 2008 property and casualty reinsurance program include:

- Property per risk treaty – The primary purpose of the property treaty is to provide capacity up to \$25 million, adequate for the majority of the risks we write. It also includes protection for extra-contractual liability coverage losses. We retain the first \$4 million of each loss. Losses between \$4 million and \$25 million are reinsured at 100 percent. The ceded premium is estimated at \$38 million for 2008, compared with \$35 million in 2007 and \$29.5 million in 2006.
- Casualty per occurrence treaty – The casualty treaty provides capacity up to \$25 million. Similar to the property treaty, it provides sufficient capacity to cover the vast majority of casualty accounts we insure and also includes protection for extra-contractual liability coverage losses. We retain the first \$5 million of each loss. Losses between \$5 million and \$25 million are reinsured at 100 percent. The ceded premium is estimated at \$45 million in 2008, compared with \$50 million in 2007 and \$44.8 million in 2006.

We have modified our casualty per occurrence treaty for one Fortune 1000 policyholder. Three executive risk policies are written for this insured and the \$5 million casualty retention would apply separately to each policy for a total retention of \$15 million. This aggregation would be applicable only if all three policies were triggered under the same occurrence.

- Casualty excess treaties – We purchase a casualty reinsurance treaty that provides an additional \$25 million in protection for certain casualty losses. This treaty, along with the casualty per occurrence treaty, provides a total of \$50 million of protection for workers' compensation, extra-contractual liability coverage and clash coverage losses, which would apply when a single occurrence involved multiple policyholders of The Cincinnati Insurance Companies or multiple coverages for one insured. The ceded premium is estimated at \$1.8 million in 2008, the same premium we paid in 2007.

We purchase a second casualty excess treaty, which provides an additional \$20 million in casualty loss coverage. This treaty also provides catastrophic coverage for workers' compensation and extra-contractual liability coverage losses. The ceded premium is estimated at less than \$1 million for 2008, the same premium we paid in 2007.

- Property catastrophe treaty – To protect against catastrophic events such as wind and hail, hurricanes or earthquakes, we purchase property catastrophe reinsurance with a limit up to \$500 million. For the 2008 treaty, ceded premiums are estimated at \$43 million compared with \$48 million in 2007 and \$38 million in 2006. Our retention on this program remains at \$45 million and we also retain:
  - 43 percent of losses between \$45 million and \$70 million
  - 5 percent of losses between \$70 million and \$200 million
  - 12 percent of losses between \$200 million and \$300 million
  - 19 percent of losses between \$300 million and \$400 million and
  - 11 percent of losses between \$400 million and \$500 million.

After reinsurance, our maximum exposure to a catastrophic event that caused \$500 million in covered losses would be \$105 million compared with \$103 million in 2007. The largest catastrophe loss in our history was \$87 million before reinsurance. The treaty contains one reinstatement provision.

Individual risks with insured values in excess of \$25 million, as identified in the policy, are handled through a different reinsurance mechanism. We typically reinsure property coverage for individual risks with insured values between \$25 million and \$60 million under an automatic facultative treaty. For risks with property values exceeding \$60 million, we negotiate the purchase of facultative coverage on an individual certificate basis. For casualty coverage on individual risks with limits exceeding \$25 million, facultative reinsurance coverage is placed on an individual certificate basis.

Terrorism coverage at various levels has been secured in all of our reinsurance agreements. The broadest coverage for this peril is found in the property and casualty working treaties, which provide coverage for commercial and personal risks. Our property catastrophe treaty provides coverage for personal risks, and the majority of its reinsurers provide limited coverage for commercial risks with total insured values of \$10 million or less. For insured values between \$10 million and \$25 million, there also may be coverage in the property working treaty.

Reinsurance protection for the company's surety business is covered under separate treaties with many of the same reinsurers that write the property casualty working treaties.

The company's newly formed excess and surplus lines subsidiary has purchased a property and casualty reinsurance treaty for 2008 through Swiss Reinsurance America Corporation. Primary components of the treaty include:

- Property per risk treaty – The property treaty provides limits up to \$5 million, which provides adequate capacity for the risk profile we expect to write in 2008. We retain the first \$1 million of any policy loss. Losses between \$1 million and \$5 million are reinsured at 100 percent.
- Casualty per occurrence treaty - The casualty treaty provides limits up to \$5 million, which provides adequate capacity for the risk profile we expect to write in 2008. We retain the first \$1 million of any policy loss. Losses between \$1 million and \$5 million are reinsured at 100 percent.
- Basket retention – CSU has purchased this coverage to limit our retention to \$1 million in the event that the same occurrence results in both a property and a casualty loss.
- Property catastrophe treaty – As a subsidiary of The Cincinnati Insurance Company, CSU has been added as a named insured under our property catastrophe treaty. All terms and conditions of this treaty apply to policies underwritten by CSU.

For property or casualty risks with limits exceeding \$5 million, underwriters place facultative reinsurance coverage on an individual certificate basis. The combined property and casualty treaty provides protection on a participating basis for extra contractual obligations, as well as exposure to losses in excess of policy limits. The limit is \$5 million for both property and casualty.

Reinsurance protection for our life insurance business is covered under separate treaties with many of the same reinsurers that write the property casualty working treaties. In 2005, we modified our reinsurance protection for our term life insurance business due to changes in the marketplace that affected the cost and availability of reinsurance for term life insurance. We are retaining no more than a \$500,000 exposure, ceding

the balance using excess over retention mortality coverage, and retaining the policy reserve. Retaining the policy reserve has no direct impact on GAAP results. However, because of the conservative nature of statutory reserving principles, retaining the policy reserve unduly depresses our statutory earnings and requires a large commitment of our capital. We also have catastrophe reinsurance coverage on our life insurance operations that reimburses us up to \$40 million for covered net losses in excess of \$10 million. The treaty contains a reinstatement provision, provided the covered losses were not due to terrorism, and contains protection for extra-contractual liability coverage losses. For term life insurance business written prior to 2005, we retain 10 percent to 25 percent of each term policy, not to exceed \$500,000, ceding the balance of mortality risk and policy reserve.

The NAIC has asked for industry comments on proposals to modify statutory accounting procedures to reduce the negative effect on statutory life insurance income. We expect the NAIC proposals will be adopted. If they are not, we believe we will be able to structure a reinsurance program to provide the life insurance company with the ability to continue to grow in the term life insurance marketplace while appropriately managing risk, at a cost that allows us to achieve our life insurance company profit targets.

## 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 Item 1A, Risk Factors, Page 21. Although we often review or update our forward-looking statements when events warrant, we caution our readers that we undertake no obligation to do so.

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
- Inaccurate estimates or assumptions used for critical accounting estimates
- 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
- Changing consumer buying habits and consolidation of independent insurance agencies that could alter our competitive advantages
- 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:
  - Downgrade of the company's financial strength ratings
  - Concerns that doing business with the company is too difficult or
  - Perceptions that the company's level of service, particularly claims service, is no longer a distinguishing characteristic in the marketplace
- Sustained decline in overall stock market values negatively affecting the company's equity portfolio and book value; in particular a sustained decline in the market value of Fifth Third shares, a significant equity holding
- Securities laws that could limit the manner and timing of our investment transactions
- Recession or other economic conditions or regulatory, accounting or tax changes resulting in lower demand for insurance products
- Events, such as the subprime mortgage lending crisis, that lead to a significant decline in the value of a particular security or group of securities, such as our financial sector holdings, and impairment of the asset(s)
- 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
- Delays or inadequacies in the development, implementation, performance and benefits of technology projects and enhancements
- Ability to obtain adequate reinsurance on acceptable terms, amount of reinsurance purchased, financial strength of reinsurers and the potential for non-payment or delay in payment by reinsurers
- Increased competition that could result in a significant reduction in the company's premium growth rate
- Underwriting and pricing methods adopted by competitors that could allow them to identify and flexibly price risks, which could decrease our competitive advantages



- Personal lines pricing and loss trends that lead management to conclude that this segment could not attain sustainable profitability, which could prevent the capitalization of policy acquisition costs
- Actions of insurance departments, state attorneys general or other regulatory agencies that:
  - Restrict our ability to exit or reduce writings of unprofitable coverages or lines of business
  - Place the insurance industry under greater regulatory scrutiny or result in new statutes, rules and regulations
  - Increase our expenses
  - 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
  - Limit our ability to set fair, adequate and reasonable rates
  - Place us at a disadvantage in the marketplace or
  - Restrict our ability to execute our business model, including the way we compensate agents
- Adverse outcomes from litigation or administrative proceedings
- 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.
- Investment activities or market value fluctuations that trigger restrictions applicable to the parent company under the Investment Company Act of 1940
- Events, such as an epidemic, natural catastrophe, terrorism or construction delays, 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, 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 recent measures affecting corporate financial reporting and governance. The ultimate changes and eventual effects, if any, of these initiatives are uncertain.

## **Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

### **INTRODUCTION**

Market risk is the potential for a decrease in securities value resulting from broad yet uncontrollable forces such as: inflation, economic growth, interest rates, world political conditions or other widespread unpredictable events. It is comprised of many individual risks that, when combined, create a macroeconomic impact. The company accepts and manages risks in the investment portfolio as part of the means of achieving portfolio objectives. Some of the risks are:

- Political – the potential for a decrease in market value due to the real or perceived impact of governmental policies or conditions
- Regulatory – the potential for a decrease in market value due to the impact of legislative proposals or changes in laws or regulations
- Economic – the potential for a decrease in value due to changes in general economic factors (recession, inflation, deflation, etc.)
- Revaluation – the potential for a decrease in market value due to a change in relative value (change in market multiple) of the market brought on by general economic factors
- Interest-rate – the potential for a decrease in market value of a security or portfolio due to its sensitivity to changes (increases or decreases) in the general level of interest rates

Company-specific risk is the potential for a particular issuer to experience a decline in valuation due to the impact of sector or market risk on the holding or because of issues specific to the firm:

- Fraud – the potential for a negative impact on an issuer's performance due to actual or alleged illegal or improper activity of individuals it employs
- Credit – the potential for deterioration in an issuer's financial profile due to specific company issues, problems it faces in the course of its operations or industry-related issues

- Default – the possibility that an issuer will not make a required payment (interest payment or return of principal) on its debt. Generally this occurs after its financial profile has deteriorated (credit risk) and it no longer has the means to make its payments

The investment committee of the board of directors monitors the investment risk management process primarily through its executive oversight of our investment activities. We take an active approach to managing market and other investment risks, including the accountabilities and controls over these activities. Actively managing these market risks is integral to our operations and could require us to change the character of future investments purchased or sold or require us to shift the existing asset portfolios to manage exposure to market risk within acceptable ranges.

Sector risk is the potential for a negative impact on a particular industry due to its sensitivity to factors that make up market risk. Market risk affects general supply/demand factors for an industry and will affect companies within that industry to varying degrees.

Risks associated with the five asset classes described in Item 1, Investments Segment, Page 15, can be summarized as follows (H – high, A – average, L – low):

	Taxable fixed maturities	Tax-exempt fixed maturities	Common equities	Preferred equities	Short-term investments
Political	A	H	A	A	L
Regulatory	A	A	A	A	L
Economic	A	A	H	A	L
Revaluation	A	A	H	A	L
Interest rate	H	H	A	H	L
Fraud	A	L	A	A	L
Credit	A	L	A	A	L
Default	A	L	A	A	L

## FIXED-MATURITY INVESTMENTS

For investment-grade corporate bonds, the inverse relationship between interest rates and bond prices leads to falling bond values during periods of increasing interest rates. Although the potential for a worsening financial condition, and ultimately default, does exist with investment-grade corporate bonds, their higher-quality financial profiles make credit risk less of a concern than for lower-quality investments. We address this risk by consistently investing within a particular maturity range, which has, over the years, provided the portfolio with a laddered maturity schedule, which we believe is less subject to large swings in value due to interest rate changes. While a single maturity range may see values drop due to general interest rate levels, other maturity ranges would typically be less affected by those changes. Additionally, purchases are spread across a wide spectrum of industries and companies, diversifying our holdings and minimizing the impact of specific industries or companies with greater sensitivities to interest rate fluctuations.

The primary risk related to high-yield corporate bonds is credit risk or the potential for a deteriorating financial structure. A weak financial profile can lead to rating downgrades from the credit rating agencies, which can put further downward pressure on bond prices. Interest rate risk, while significant, is less of a factor with high-yield corporate bonds, as valuation is related more directly to underlying operating performance than to general interest rates. This puts more emphasis on the financial results achieved by the issuer rather than on general economic trends or statistics within the marketplace. We address this concern by analyzing issuer- and industry-specific financial results and by closely monitoring holdings within this asset class.

The primary risks related to tax-exempt bonds are interest rate risk and political risk associated with the specific economic environment within the political boundaries of the issuing municipal entity. We address these concerns by focusing on municipalities' general-obligation debt and on essential-service bonds.

Essential-service bonds derive a revenue stream from the services provided by the municipality, which are vital to the people living in the area (water service, sewer service, etc.). Another risk related to tax-exempt bonds is regulatory risk or the potential for legislative changes that would negate the benefit of owning tax-exempt bonds. We monitor regulatory activity for situations that may negatively affect current holdings and our ongoing strategy for investing in these securities.

The final, less significant risk is our exposure to credit risk for a portion of the tax-exempt portfolio that has support from corporate entities. Examples are bonds insured by corporate bond insurers or bonds with interest payments made by a corporate entity through a municipal conduit/authority. Our decisions regarding these investments primarily consider the underlying municipal situation. The existence of third-party insurance is intended to reduce risk in the event of default. In circumstances in which the municipality is unable to meet its obligations, risk would be increased if the insuring entity were experiencing financial duress. Because of our diverse exposure and selection of higher-rated entities with strong financial profiles, we do not believe this is a material concern as we discuss in Item 1, Investments Segment, Page 15.

## 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 well positioned if interest rates were to rise. 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 book value, we believe lower fixed-maturity security values due solely to interest rate changes would not signal a decline in credit quality.

A dynamic financial planning model developed during 2002 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 fixed-maturity portfolio:

(In millions)	Fair value of fixed maturity portfolio	Effective duration	
		100 basis point spread decrease	100 basis point spread increase
<b>At December 31, 2007</b>	<b>\$ 5,848</b>	<b>\$ 6,131</b>	<b>\$ 5,565</b>
At December 31, 2006	5,805	6,099	5,511

The effective duration of the fixed maturity portfolio is currently 4.84 years, down slightly from year-end 2006. A 100 basis point movement in interest rates would result in an approximately 4.8 percent change in the market value of the fixed maturity portfolio. Generally speaking, the higher a bond is rated, the more directly correlated movements in its market value will be to changes in the general level of interest rates, exclusive of call features. The market values of average- to lower-rated corporate bonds are additionally influenced by the expansion or contraction of credit spreads.

In the dynamic financial planning model, the selected interest rate change of 100 basis points represents our views 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.

## SHORT-TERM INVESTMENTS

Our short-term investments present minimal risk as we generally purchase the highest quality commercial paper.

## EQUITY INVESTMENTS

Common stocks are subject to a variety of risk factors encompassed under the umbrella of market risk. General economic swings influence the performance of the underlying industries and companies within those industries. A downturn in the economy can have a negative impact on an equity portfolio. Industry- and company-specific risks have the potential to substantially affect the market value of the company's equity portfolio. We address these risks by maintaining investments in a small group of holdings that we can analyze closely, better understanding their business and the related risk factors.

At year-end 2007, we held 15 individual equity positions valued at approximately \$100 million or above, see Item 1, Investments Segment, Page 15, for additional details on these holdings. These equity positions accounted for approximately 93.0 percent of the unrealized appreciation of the entire portfolio.

Our common stock investments generally are securities with annual dividend yields that meet or exceed that of the overall market and have the potential for future dividend increases. 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. We believe that the continued payment of cash dividends by the issuers of the common equities we hold also should provide a floor to their valuation.

Our investments are heavily weighted toward the financial sector, which represented 56.7 percent of the total fair value of the common stock portfolio at year-end 2007. Financial sector investments typically underperform the overall market during periods when interest rates are expected to rise. We historically have seen these types of short-term fluctuations in market value of our holdings as potential buying opportunities but are aware that a prolonged downturn in this sector could create a long-term negative effect on the portfolio.

Over the longer term, our objective is for the performance of our equity portfolio to exceed that of the broader market. Over the five years ended December 31, 2007, our compound annual equity portfolio return was flat compared with a compound annual total return of 12.8 percent for the Standard & Poor's 500 Index,

a common benchmark of market performance. In 2007, our annual equity portfolio return was a negative 16.3 percent, compared with an annual total return of 5.5 percent for that Index. Our equity portfolio underperformed the market for the five-year period primarily because of the decline in the market value of our holdings of Fifth Third common stock between 2003 and 2007.

The primary risks related to preferred stocks are similar to those related to investment grade corporate bonds. Falling interest rates adversely affect market values due to the normal inverse relationship between rates and yields. Credit risk exists due to the subordinate position of preferred stocks in the capital structure. We minimize this risk by primarily purchasing investment grade preferred stocks of issuers with a strong history of paying a common stock dividend.

In 2007, we purchased residual shares in two auction rate pass-through trusts, otherwise known as auction rate securities. Each of the two trusts we purchased contain a single investment grade preferred security (rated A3/A- and Aa3/A+) that provides for the cash flow to be divided between the two types of shares within the Trust. We own both the primary ("A") and residual ("B") shares in one of these investments. Due to recent disruptions within the auction process that sets the rate for payment to the primary shares, there have been no residual cash flows available for payout to our residual shares although the primary shares have performed as expected. We have both the ability and intent to hold these securities. We will continue to monitor the auction process until such time as it normalizes. However, if the auction process fails to normalize in a reasonable period of time, we may deem it necessary to impair these securities. As of year-end 2007, these investments had a fair value of \$13 million and represented unrealized losses of \$4.2 million.

### Fifth Third Bancorp Holding

One of our common stock holdings, Fifth Third, accounted for 28.5 percent of our shareholders' equity at year-end 2007 and dividends earned from our Fifth Third investment were 20.0 percent of our investment income in 2007. In October 2007, we sold 5.5 million shares of our Fifth Third holding to fund an ASR agreement.

(In millions except market price data)	Years ended December 31,	
	2007	2006
Fifth Third Bancorp common stock holding:		
Dividends earned	\$ 121	\$ 115
Percent of total net investment income	20.0 %	20.2 %
	<b>At December 31,</b>	<b>At December 31,</b>
	<b>2007</b>	<b>2006</b>
Shares held	67	73
Closing market price of Fifth Third	\$ 25.13	\$ 40.93
Book value of holding	185	283
Fair value of holding	1,691	2,979
After-tax unrealized gain	979	1,752
Market value as a percent of total equity investments	27.1 %	38.2 %
Market value as a percent of invested assets	13.8	21.7
Market value as a percent of total shareholders' equity	28.5	43.8
After-tax unrealized gain as a percent of total shareholders' equity	16.5	25.7

Based on 2007 results, a 10 percent change in dividends earned from our Fifth Third holding would result in a \$12 million change in pretax investment income and a \$11 million change in after-tax earnings.

Every \$1.00 change in the market price of Fifth Third's common stock has approximately a 26 cent impact on our book value per share. A 20 percent change in the market price of Fifth Third's common stock from its year-end 2007 closing price would result in a \$338 million change in assets and a \$220 million change in after tax unrealized gains.

The market value of Fifth Third, our largest holding, has been affected in recent years by the residual effects of a regulatory review concluded in 2004, and, more recently by a difficult interest rate environment and by challenging economic conditions in certain of its geographic markets. We maintain confidence in its management team's ability to successfully execute its long-term strategic plan. During this challenging period for the bank, we have continued to benefit from its superior dividend growth. Fifth Third paid dividends of \$1.66 per share in 2007 compared with \$1.56 per share in 2006.

### SECURITIES LENDING COLLATERAL INVESTED

We participate in a securities lending program under which certain fixed maturities from our investment portfolio are loaned to other institutions for short periods of time. At year-end 2007, we had fixed maturities with a market value of \$745 million on loan. The \$760 million in offsetting collateral is shown on our balance sheets as securities lending collateral invested.

A portion of the securities lending collateral invested was placed in asset-backed commercial paper (ABCP) programs during 2007 by our lending agent. Due to the ABCP market disruption, maturities on two of our investments were extended beyond their original stated maturity dates. As of the date of this 10-K filing, only one of these investments remained outstanding. The remaining ABCP had an amortized cost of \$73 million at February 22, 2008, compared with \$74 million at year-end 2007. The ABCP manager is continuing to work with investors to allow for an orderly liquidation of the fund. Excluding this remaining ABCP investment, all investments within our securities lending program now are in overnight securities.

We are potentially at risk if our ability to return the collateral is compromised because of a material decline in the market value of the securities in which we have invested the collateral. We discuss the program in Item 8, Note 1 of the Consolidated Financial Statements, Page 87.

## UNREALIZED INVESTMENT GAINS AND LOSSES

At year-end 2007, unrealized investment gains before taxes totaled \$3.527 billion and unrealized investment losses in the investment portfolio amounted to \$188 million.

### Unrealized Investment Gains

The unrealized gains at year-end 2007 largely were due to long-term gains from our holdings of Fifth Third common stock, which contributed 42.7 percent of those gains, and from our other common stock holdings, including AllianceBernstein Holding L.P. (NYSE:AB), ExxonMobil (NYSE:XOM), PNC Financial Services Group, Inc. (NYSE:PNC) and The Procter & Gamble Company (NYSE:PG), which each contributed at least 5 percent of those gains.

### Unrealized Investment Losses – Potential Other-than-temporary Impairments

During 2007, a total of 20 securities were written down as other-than-temporarily impaired because of credit concerns that began with the pressure that the fallout from the subprime mortgage crisis has placed on securities in the housing and related industries. Those declines reflected general credit concerns that began in the subprime mortgage market and spread to other areas in the homebuilding and related industries over the course of 2007. During 2006, one security was written down.

We expect the number of securities trading below 100 percent of book value to fluctuate as interest rates rise or fall and credit spreads expand or contract due to prevailing economic conditions. Further, book values for some securities have been revised due to impairment charges recognized in prior periods. At year-end 2007, 373 of the 2,053 securities we owned were trading below 100 percent of book value compared with 679 of the 1,973 securities we owned at year-end 2006 and 732 of the 1,814 securities we owned at year-end 2005.

The 373 holdings trading below book value at year-end 2007 represented 18.2 percent of invested assets and \$188 million in unrealized losses. We deem the risk related to securities trading between 70 percent and 100 percent of book value to be relatively minor and at least partially offset by the earned income potential of these investments.

- 319 of these holdings were trading between 90 percent and 100 percent of book value. The value of these securities fluctuates primarily because of changes in interest rates. The fair value of these 319 securities was \$1.332 billion at year-end 2007, and they accounted for \$46 million in unrealized losses.
- 54 of these holdings were trading below 90 percent of book value at year-end 2007. The fair value of these holdings was \$562 million, and they accounted for \$142 million in unrealized losses. These securities, which are being closely monitored, have been affected by a combination of factors including the effects of higher interest rates on longer-duration instruments, leveraged buyout activity and the slowdown in the residential construction market. The majority of these securities are in the financial sector.
- Three securities were trading below 70 percent of book value at year-end 2007. The fair value of these holdings was \$12 million, and they accounted for \$6 million in unrealized losses. Our impairment committee evaluated these securities and believes the change in valuation is temporary.

As discussed in Critical Accounting Estimates, Asset Impairment, Page 40, when evaluating other-than-temporary impairments, we consider our intent and ability to retain a security for a period adequate to recover a substantial portion of its cost. Because of our investment philosophy and strong capitalization, we can hold securities until their scheduled redemption that might otherwise be deemed impaired as we evaluate their potential for recovery based on economic, industry or company factors.

The following table summarizes the length of time securities in the investment portfolio have been in a continuous unrealized gain or loss position.

(Dollars in millions)	6 Months or less		> 6 - 12 Months		> 12 - 24 Months		> 24 - 36 Months	
	Number of issues	Gross unrealized gain/loss	Number of issues	Gross unrealized gain/loss	Number of issues	Gross unrealized gain/loss	Number of issues	Gross unrealized gain/loss
<b>At December 31, 2007</b>								
Taxable fixed maturities:								
Trading below 70% of book value	0	\$ 0	0	\$ 0	0	\$ 0	0	\$ 0
Trading at 70% to less than 100% of book value	57	(7)	64	(19)	27	(4)	80	(15)
Trading at 100% and above of book value	241	9	17	1	47	5	203	49
Total	298	2	81	(18)	74	1	283	34
Tax-exempt fixed maturities:								
Trading below 70% of book value	0	0	0	0	0	0	0	0
Trading at 70% to less than 100% of book value	3	0	19	(1)	8	0	69	(1)
Trading at 100% and above of book value	741	17	3	0	89	6	290	25
Total	744	17	22	(1)	97	6	359	24
Common equities:								
Trading below 70% of book value	0	0	0	0	0	0	0	0
Trading at 70% to less than 100% of book value	11	(60)	2	(47)	0	0	0	0
Trading at 100% and above of book value	3	0	2	19	5	237	23	3,156
Total	14	(60)	4	(28)	5	237	23	3,156
Preferred equities:								
Trading below 70% of book value	3	(6)	0	0	0	0	0	0
Trading at 70% to less than 100% of book value	21	(21)	6	(7)	0	0	0	0
Trading at 100% and above of book value	5	1	1	0	2	2	4	0
Total	29	(26)	7	(7)	2	2	4	0
Short-term investments:								
Trading below 70% of book value	0	0	0	0	0	0	0	0
Trading at 70% to less than 100% of book value	0	0	3	0	0	0	0	0
Trading at 100% and above of book value	4	0	0	0	0	0	0	0
Total	4	0	3	0	0	0	0	0
Summary:								
Trading below 70% of book value	3	(6)	0	0	0	0	0	0
Trading at 70% to less than 100% of book value	92	(88)	94	(74)	35	(4)	149	(16)
Trading at 100% and above of book value	994	27	23	20	143	250	520	3,230
Total	1,089	\$ (67)	117	\$ (54)	178	\$ 246	669	\$ 3,214

The following table summarizes the investment portfolio:

(Dollars in millions)	Number of issues	Book value	Fair value	Gross unrealized gain/loss	Gross investment income
<b>At December 31, 2007</b>					
Taxable fixed maturities:					
Trading below 70% of book value	0	\$ 0	\$ 0	\$ 0	0
Trading at 70% to less than 100% of book value	228	936	891	(45)	52
Trading at 100% and above of book value	508	2,329	2,393	64	130
Securities sold in current year	0	0	0	0	22
Total	<u>736</u>	<u>3,265</u>	<u>3,284</u>	<u>19</u>	<u>204</u>
Tax-exempt fixed maturities:					
Trading below 70% of book value	0	0	0	0	0
Trading at 70% to less than 100% of book value	99	246	244	(2)	9
Trading at 100% and above of book value	1,123	2,272	2,320	48	98
Securities sold in current year	0	0	0	0	3
Total	<u>1,222</u>	<u>2,518</u>	<u>2,564</u>	<u>46</u>	<u>110</u>
Common equities:					
Trading below 70% of book value	0	0	0	0	0
Trading at 70% to less than 100% of book value	13	672	565	(107)	21
Trading at 100% and above of book value	33	2,043	5,455	3,412	244
Securities sold in current year	0	0	0	0	6
Total	<u>46</u>	<u>2,715</u>	<u>6,020</u>	<u>3,305</u>	<u>271</u>
Preferred equities:					
Trading below 70% of book value	3	18	12	(6)	0
Trading at 70% to less than 100% of book value	27	180	152	(28)	10
Trading at 100% and above of book value	12	62	65	3	1
Securities sold in current year	0	0	0	0	3
Total	<u>42</u>	<u>260</u>	<u>229</u>	<u>(31)</u>	<u>14</u>
Short-term investments:					
Trading below 70% of book value	0	0	0	0	0
Trading at 70% to less than 100% of book value	3	30	30	0	0
Trading at 100% and above of book value	4	71	71	0	0
Securities sold in current year	0	0	0	0	2
Total	<u>7</u>	<u>101</u>	<u>101</u>	<u>0</u>	<u>2</u>
Portfolio summary:					
Trading below 70% of book value	3	\$ 18	\$ 12	\$ (6)	0
Trading at 70% to less than 100% of book value	370	2,064	1,882	(182)	92
Trading at 100% and above of book value	1,680	6,777	10,304	3,527	473
Investment income on securities sold in current year	0	0	0	0	36
Total	<u>2,053</u>	<u>\$ 8,859</u>	<u>\$ 12,198</u>	<u>\$ 3,339</u>	<u>\$ 601</u>
At December 31, 2006					
Portfolio summary:					
Trading below 70% of book value	0	\$ 0	\$ 0	\$ 0	0
Trading at 70% to less than 100% of book value	679	2,787	2,728	(59)	127
Trading at 100% and above of book value	1,294	5,668	10,971	5,303	416
Investment income on securities sold in current year	0	0	0	0	19
Total	<u>1,973</u>	<u>\$ 8,455</u>	<u>\$ 13,699</u>	<u>\$ 5,244</u>	<u>\$ 562</u>

## **Item 8. Financial Statements and Supplementary Data**

### **RESPONSIBILITY FOR FINANCIAL STATEMENTS**

We have prepared the consolidated financial statements of Cincinnati Financial Corporation and our subsidiaries for the year ended December 31, 2007, in accordance with accounting principles generally accepted in the United States of America (GAAP).

We are responsible for the integrity and objectivity of these financial statements. The amounts, presented on an accrual basis, reflect our best estimates and judgment. These statements are consistent in all material aspects with other financial information in the Annual Report on Form 10-K. Our accounting system and related internal controls are designed to assure that our books and records accurately reflect the company's transactions in accordance with established policies and procedures as implemented by qualified personnel.

Our board of directors has established an audit committee of independent outside directors. We believe these directors are free from any relationships that could interfere with their independent judgment as audit committee members.

The audit committee meets periodically with management, our independent registered public accounting firm and our internal auditors to discuss how each is handling responsibilities. The audit committee reports their findings to the board of directors. The audit committee recommends to the board the annual appointment of the independent registered public accounting firm. The audit committee reviews with this firm the scope of the audit assignment and the adequacy of internal controls and procedures.

Deloitte & Touche LLP, our independent registered public accounting firm, audited the consolidated financial statements of Cincinnati Financial Corporation and subsidiaries for the year ended December 31, 2007. Their report is on Page 82. Deloitte's auditors met with our audit committee to discuss the results of their examination. They have the opportunity to present their opinions about the adequacy of internal controls and the quality of financial reporting without management present.



## MANAGEMENT'S ANNUAL REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of Cincinnati Financial Corporation and its subsidiaries is responsible for establishing and maintaining adequate internal controls, designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America (GAAP). The company's internal control over financial reporting includes those policies and procedures that:

1. Pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company;
2. Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP and that receipts and expenditures of the company are being made only in accordance with authorizations of management and the directors of the company; and
3. Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

All internal control systems, no matter how well designed, have inherent limitations, including the possibility of human error and the circumvention of overriding controls. Accordingly, even effective internal control can provide only reasonable assurance with respect to financial statement preparation and presentation. Further, because of changes in conditions, the effectiveness of internal control may vary over time.

The company's management assessed the effectiveness of the company's internal control over financial reporting as of December 31, 2007, as required by Section 404 of the Sarbanes Oxley Act of 2002. Management's assessment is based on the criteria established in the Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and was designed to provide reasonable assurance that the company maintained effective internal control over financial reporting as of December 31, 2007. The assessment led management to conclude that, as of December 31, 2007, the company's internal control over financial reporting was effective based on those criteria.

The company's independent registered public accounting firm has issued an attestation report on our internal control over financial reporting as of December 31, 2007. This report appears below.

/S/ John J. Schiff, Jr.

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John J. Schiff, Jr., CPCU  
Chairman and Chief Executive Officer

/S/ Kenneth W. Stecher

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Kenneth W. Stecher  
Chief Financial Officer, Executive Vice President, Secretary and Treasurer  
(Principal Accounting Officer)

February 28, 2008

# REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Directors of Cincinnati Financial Corporation  
Fairfield, Ohio

We have audited the accompanying consolidated balance sheets of Cincinnati Financial Corporation and subsidiaries (the company) as of December 31, 2007 and 2006, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2007. Our audits also included the financial statement schedules listed in the Index at Item 15(c). We also have audited the company's internal control over financial reporting as of December 31, 2007, based on criteria established in the Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The company's management is responsible for these financial statements and financial schedules, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Annual Report on Internal Control Over Financial Reporting report. Our responsibility is to express an opinion on these financial statements and financial statement schedules and an opinion on the company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audit of financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that: (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the company as of December 31, 2007 and 2006, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2007, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedules, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly, in all material respects, the information set forth therein. Also, in our opinion, the company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on the criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

As discussed in Note 1 of the Consolidated Financial Statements, the company adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 123(R), Share Based Payment, on January 1, 2006; the recognition and related disclosure provisions of SFAS No. 158, Employers' Accounting for Defined Benefit Pension Plans and Other Postretirement Benefit Plans, on December 31, 2006; the provisions of SFAS No. 155, Accounting for Certain Hybrid Financial Instruments, an amendment of SFAS No. 133 and 140, on January 1, 2007; and the provisions of Financial Interpretation No. 48, Accounting for Uncertainty in Income Taxes, an Interpretation of SFAS No. 109, on January 1, 2007.

/S/ Deloitte & Touche LLP  
Cincinnati, Ohio  
February 28, 2008

# CINCINNATI FINANCIAL CORPORATION AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS

(Dollars in millions except per share data)

	December 31, 2007	December 31, 2006
<b>ASSETS</b>		
Investments		
Fixed maturities, at fair value (amortized cost: 2007—\$5,783; 2006—\$5,739) (includes securities pledged to creditors of \$745 at December 31, 2007)	\$ 5,848	\$ 5,805
Equity securities, at fair value (cost: 2007—\$2,975; 2006—\$2,621)	6,249	7,799
Short-term investments, at fair value (amortized cost: 2007—\$101; 2006—\$95)	101	95
Other invested assets	63	60
Total investments	<u>12,261</u>	<u>13,759</u>
Cash and cash equivalents	226	202
Securities lending collateral invested	760	0
Investment income receivable	124	121
Finance receivable	92	108
Premiums receivable	1,107	1,128
Reinsurance receivable	754	683
Prepaid reinsurance premiums	13	13
Deferred policy acquisition costs	461	453
Land, building and equipment, net, for company use (accumulated depreciation: 2007—\$276; 2006—\$261)	239	193
Other assets	72	58
Separate accounts	528	504
Total assets	<u>\$ 16,637</u>	<u>\$ 17,222</u>
<b>LIABILITIES</b>		
Insurance reserves		
Loss and loss expense reserves	\$ 3,967	\$ 3,896
Life policy reserves	1,478	1,409
Unearned premiums	1,564	1,579
Securities lending payable	760	0
Other liabilities	574	533
Deferred income tax	977	1,653
Note payable	69	49
6.125% senior notes due 2034	371	371
6.9% senior debentures due 2028	28	28
6.92% senior debentures due 2028	392	392
Separate accounts	528	504
Total liabilities	<u>10,708</u>	<u>10,414</u>
Commitments and contingent liabilities (Note 15)	—	—
<b>SHAREHOLDERS' EQUITY</b>		
Common stock, par value—\$2 per share; (authorized: 2007—500 million shares, 2006—500 million shares; issued: 2007—196 million shares, 2006—196 million shares)	393	391
Paid-in capital	1,049	1,015
Retained earnings	3,404	2,786
Accumulated other comprehensive income	2,151	3,379
Treasury stock at cost (2007—30 million shares, 2006—23 million shares)	<u>(1,068)</u>	<u>(763)</u>
Total shareholders' equity	<u>5,929</u>	<u>6,808</u>
Total liabilities and shareholders' equity	<u>\$ 16,637</u>	<u>\$ 17,222</u>

Accompanying notes are an integral part of these statements.

# CINCINNATI FINANCIAL CORPORATION AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF INCOME

(In millions except per share data)

	Years ended December 31,		
	2007	2006	2005
<b>REVENUES</b>			
Earned premiums			
Property casualty	\$ 3,125	\$ 3,163	\$ 3,058
Life	125	115	106
Investment income, net of expenses	608	570	526
Realized investment gains and losses	382	684	61
Other income	19	18	16
Total revenues	4,259	4,550	3,767
<b>BENEFITS AND EXPENSES</b>			
Insurance losses and policyholder benefits	1,963	2,128	1,911
Commissions	624	630	627
Other operating expenses	362	354	302
Taxes, licenses and fees	75	77	72
Increase in deferred policy acquisition costs	(9)	(21)	(19)
Interest expense	52	53	51
Total benefits and expenses	3,067	3,221	2,944
<b>INCOME BEFORE INCOME TAXES</b>	<b>1,192</b>	<b>1,329</b>	<b>823</b>
<b>PROVISION (BENEFIT) FOR INCOME TAXES</b>			
Current	325	404	188
Deferred	12	(5)	33
Total provision for income taxes	337	399	221
<b>NET INCOME</b>	<b>\$ 855</b>	<b>\$ 930</b>	<b>\$ 602</b>
<b>PER COMMON SHARE</b>			
Net income—basic	\$ 5.01	\$ 5.36	\$ 3.44
Net income—diluted	4.97	5.30	3.40

Accompanying notes are an integral part of this statement.

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

(In millions)	Years ended December 31,		
	2007	2006	2005
<b>COMMON STOCK</b>			
Beginning of year	\$ 391	\$ 389	\$ 370
5% stock dividend	0	0	18
Stock options exercised	2	2	1
End of year	<u>393</u>	<u>391</u>	<u>389</u>
<b>PAID-IN CAPITAL</b>			
Beginning of year	1,015	969	618
5% stock dividend	0	0	341
Stock options exercised	19	28	9
Share-based compensation	14	17	0
Other	1	1	1
End of year	<u>1,049</u>	<u>1,015</u>	<u>969</u>
<b>RETAINED EARNINGS</b>			
Beginning of year	2,786	2,088	2,057
Cumulative effect of change in accounting for hybrid financial securities	5	0	0
Cumulative effect of change in accounting for uncertain tax positions	(1)	0	0
Adjusted beginning of year	<u>2,790</u>	<u>2,088</u>	<u>2,057</u>
Net income	855	930	602
5% stock dividend	0	0	(359)
Dividends declared	(241)	(232)	(212)
End of year	<u>3,404</u>	<u>2,786</u>	<u>2,088</u>
<b>ACCUMULATED OTHER COMPREHENSIVE INCOME</b>			
Beginning of year	3,379	3,284	3,787
Cumulative effect of change in accounting for hybrid financial securities	(5)	0	0
Adjusted beginning of year	<u>3,374</u>	<u>3,284</u>	<u>3,787</u>
Other comprehensive income (loss), net	(1,223)	127	(503)
Cumulative effect of change in accounting for pension obligations	0	(32)	0
End of year	<u>2,151</u>	<u>3,379</u>	<u>3,284</u>
<b>TREASURY STOCK</b>			
Beginning of year	(763)	(644)	(583)
Purchase	(306)	(120)	(63)
Reissued	1	1	2
End of year	<u>(1,068)</u>	<u>(763)</u>	<u>(644)</u>
Total shareholders' equity	<u>\$ 5,929</u>	<u>\$ 6,808</u>	<u>\$ 6,086</u>
<b>COMMON STOCK - NUMBER OF SHARES OUTSTANDING</b>			
Beginning of year	173	174	167
5% stock dividend	0	0	9
Shares issued	0	1	0
Purchase of treasury shares	(7)	(2)	(2)
End of year	<u>166</u>	<u>173</u>	<u>174</u>
<b>COMPREHENSIVE INCOME</b>			
Net income	\$ 855	\$ 930	\$ 602
Unrealized investment gains and losses during the period	(1,898)	181	(749)
Taxes on other comprehensive income	667	(54)	246
Pension obligations	8	0	0
Total comprehensive income (loss)	<u>\$ (368)</u>	<u>\$ 1,057</u>	<u>\$ 99</u>

Accompanying notes are an integral part of this statement.

# CINCINNATI FINANCIAL CORPORATION AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS

(In millions)	Years ended December 31,		
	2007	2006	2005
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net income	\$ 855	\$ 930	\$ 602
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation, amortization and other non-cash items	36	38	33
Realized gains on investments	(382)	(684)	(61)
Share-based compensation	14	17	0
Interest credited to contract holders	36	31	28
Changes in:			
Investment income receivable	(3)	(3)	(10)
Premiums and reinsurance receivable	(50)	(13)	2
Deferred policy acquisition costs	(8)	(21)	(19)
Other assets	(4)	17	5
Loss and loss expense reserves	71	235	112
Life policy reserves	101	81	84
Unearned premiums	(15)	20	20
Other liabilities	64	(5)	(17)
Deferred income tax	12	(5)	33
Current income tax	(22)	(23)	(7)
Net cash provided by operating activities	<u>705</u>	<u>615</u>	<u>805</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Sale of fixed maturities	321	110	243
Call or maturity of fixed maturities	520	343	466
Sale of equity securities	812	859	104
Collection of finance receivables	37	35	34
Purchase of fixed maturities	(924)	(753)	(1,297)
Purchase of equity securities	(769)	(689)	(219)
Change in short-term investments, net	(5)	(15)	(4)
Investment in buildings and equipment, net	(70)	(52)	(44)
Investment in finance receivables	(23)	(41)	(45)
Change in other invested assets, net	(1)	(11)	(9)
Change in securities lending collateral invested	(760)	0	0
Net cash used in investing activities	<u>(862)</u>	<u>(214)</u>	<u>(771)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Payment of cash dividends to shareholders	(240)	(228)	(204)
Purchase of treasury shares	(307)	(120)	(61)
Increase in notes payable	20	49	0
Proceeds from stock options exercised	19	27	11
Contract holder funds deposited	12	32	87
Contract holder funds withdrawn	(79)	(78)	(54)
Change in securities lending payable	760	0	0
Excess tax benefits on share-based compensation	2	2	0
Other	(6)	(2)	0
Net cash provided by (used in) financing activities	<u>181</u>	<u>(318)</u>	<u>(221)</u>
Net increase (decrease) in cash and cash equivalents	<u>24</u>	<u>83</u>	<u>(187)</u>
Cash and cash equivalents at beginning of year	202	119	306
Cash and cash equivalents at end of period	<u>\$ 226</u>	<u>\$ 202</u>	<u>\$ 119</u>
Supplemental disclosures of cash flow information:			
Interest paid (net of capitalized interest: 2007—\$2; 2006—\$1)	\$ 51	\$ 53	\$ 51
Income taxes paid	346	429	195
Non-cash activities:			
Conversion of securities	\$ 20	\$ 50	\$ 42
Equipment acquired under capital lease obligations	12	12	0

Accompanying notes are an integral part of these statements.

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Nature of Operations

Cincinnati Financial operates through our insurance group and three complementary subsidiary companies: The Cincinnati Insurance Company leads our standard market property casualty insurance group that also includes subsidiaries The Cincinnati Casualty Company and The Cincinnati Indemnity Company. This group markets a broad range of standard market business, homeowner and auto policies in 34 states. The group provides quality customer service to our select group of 1,092 local insurance agencies with 1,327 reporting locations. Other subsidiaries of The Cincinnati Insurance Company include The Cincinnati Life Insurance Company, which markets life insurance policies, disability income policies and annuities, and The Cincinnati Specialty Underwriters Insurance Company, which began offering excess and surplus lines insurance products in 2008.

The three complementary subsidiaries are CSU Producer Resources Inc. which offers insurance brokerage services to our independent agencies so their clients can access our excess and surplus lines insurance products; CFC Investment Company, which offers commercial leasing and financing services to our agents, their clients and other customers; and CinFin Capital Management Company, which provides asset management services to institutions, corporations and individuals.

### Basis of Presentation

Our consolidated financial statements include the accounts of the parent company and our wholly owned subsidiaries. We present our statements in accordance with accounting principles generally accepted in the United States of America (GAAP). In consolidating our accounts, we have eliminated significant intercompany balances and transactions.

In accordance with GAAP, we have made estimates and assumptions that affect the amounts we report and discuss in the consolidated financial statements and accompanying notes. Actual results could differ from our estimates.

### Earnings per Share

Net income per common share is based on the weighted average number of common shares outstanding during each of the respective years. We calculate net income per common share (diluted) assuming the exercise of stock options. We have adjusted shares and earnings per share to reflect all stock splits and dividends prior to December 31, 2007.

### Share-based Compensation

We grant qualified and non-qualified share-based compensation under authorized plans. Until 2007, all stock-based awards were in the form of stock options that had an exercise price equal to the market value of the underlying common stock on the date of grant, vested in equal amounts over the three years following the date of grant and were exercisable over 10 year periods.

The 2006 Stock Compensation Plan, approved in 2006 by shareholders, provides the compensation committee of the board of directors flexibility in the types of available stock-based awards including stock options along with restricted stock, restricted stock units, stock appreciation rights and other stock-based awards. The 2006 Stock Compensation Plan also allowed the grant of performance-based awards.

In 2007, the committee approved a mix of stock options and restricted stock units for stock-based awards. Service-based stock options awarded had similar terms but generally were awarded for fewer shares compared with previous years to accommodate new awards of restricted stock units while keeping the overall cost of stock-based compensation in line with previous years.

Prior to January 1, 2006, we accounted for our stock option plans using the recognition and measurement provisions pursuant to Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations (APB 25), as permitted by the Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation," (SFAS No. 123). No stock-based employee compensation cost was recognized in the Statements of Income for the year ended December 31, 2005.

Effective January 1, 2006, we adopted the fair value recognition provisions of the SFAS No. 123(R), "Share-Based Payment," using the modified-prospective-transition method. We elected to use the alternative method for determining the beginning balance of the additional paid-in capital pool, as described in the Financial Accounting Standards Board (FASB) Staff Position 123(R)-3. Refer to Note 16, Stock-based Associate Compensation Plans, Page 102 for more information regarding our share-based compensation.

### Employee Benefit Pension Plan

We sponsor a defined benefit pension plan covering substantially all employees. Our pension expense is based on certain actuarial assumptions and also is composed of several components that are determined using the projected unit credit actuarial cost method.

## **Property Casualty Insurance**

Property casualty policy written premiums are deferred and recorded as earned premiums on a pro rata basis over the terms of the policies. We record as unearned premium the portion of written premiums that apply to unexpired policy terms. The expenses associated with issuing insurance policies – primarily commissions, premium taxes and underwriting costs – are deferred and amortized over the terms of policies. We update our acquisition cost assumptions periodically to reflect actual experience and we evaluate our deferred acquisition cost for recoverability.

Certain property casualty policies are not booked before the effective date. An actuarial estimate is made to determine the amount of unbooked written premiums. The majority of the estimate is unearned and does not have a material impact on earned premium.

We establish reserves to cover the expected cost of claims – or losses – and our expenses related to investigating, processing and resolving claims. Although determining the appropriate amount of reserves is inherently uncertain, we base our decisions on past experience and current facts. Reserves are based on claims reported prior to the end of the year and estimates of unreported claims. We take into account the fact that we may recover some of our costs through salvage and subrogation. We regularly review and update reserves using the most current information available. Any resulting adjustments are reflected in current year insurance losses and policyholder benefits.

The Cincinnati Insurance Companies actively write standard market property casualty insurance policies in 34 states. Our 10 largest states generated 69.1 percent and 70.0 percent of total property casualty premiums in 2007 and 2006. Ohio, our largest state, accounted for 21.2 percent and 22.0 percent of total earned premiums in 2007 and 2006. Agencies in Georgia, Illinois, Indiana, Michigan, North Carolina, Pennsylvania and Virginia each contributed between 4 percent and 9 percent of premium volume in 2007. The largest single agency relationship accounted for approximately 1.2 percent of the company's total agency direct earned premiums in 2007.

## **Policyholder Dividends**

Certain workers' compensation policies include the possibility of an insured earning a return of a portion of their premium, called a policyholder dividend. The dividend is generally calculated by determining the profitability of a policy year along with the associated premium. We reserve for all probable future policyholder dividend payments.

## **Life and Health Insurance**

We offer several types of life and health insurance and we account for each according to the duration of the contract. Short-duration contracts are written to cover claims that arise during a short, fixed term of coverage. We generally have the right to change the amount of premium charged or cancel the coverage at the end of each contract term. Group life insurance is an example. We record premiums for short-duration contracts similarly to property casualty contracts.

Long-duration contracts are written to provide coverage for an extended period of time. Traditional long-duration contracts require policyholders to pay scheduled gross premiums, generally not less frequently than annually, over the term of the coverage. Premiums for these contracts are recognized as revenue when due. Whole life insurance and disability income insurance are examples. Some traditional long-duration contracts have premium payment periods shorter than the period over which coverage is provided. For these contracts the excess of premium over the amount required to pay expenses and benefits is recognized over the term of the coverage rather than over the premium payment period. Ten-pay whole life insurance is an example.

We establish a liability for traditional long-duration contracts as we receive premiums. The amount of this liability is the present value of future expenses and benefits less the present value of future net premiums. Net premium is the portion of gross premium required to provide for all expenses and benefits. We estimate future expenses and benefits and net premium using assumptions for expected expenses, mortality, morbidity, withdrawal rates and investment income. We include a provision for adverse deviation, meaning we allow for some uncertainty in making our assumptions. We establish our assumptions when the contract is issued and we generally maintain those assumptions for the life of the contract. 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. We use our own experience and historical trends for setting our assumption for expected expenses. We base our assumption for expected investment income on our own experience, adjusted for current economic conditions.

When we issue a traditional long-duration contract, we capitalize acquisition costs. Acquisition costs are costs which vary with, and are primarily related to, the production of new business. We then charge these deferred policy acquisition costs to expenses over the premium paying period of the contract and we use the same assumptions that we use when we establish the liability for the contract. We update our acquisition cost assumptions periodically to reflect actual experience and we evaluate our deferred acquisition cost for recoverability.



Universal life contracts are long-duration contracts for which contractual provisions are not fixed, unlike whole life insurance. Universal life contracts allow policyholders to vary the amount of premium, within limits, without our consent. However we may vary the mortality and expense charges, within limits, and the interest crediting rate used to accumulate policy values. We do not record universal life premiums as revenue. Instead we recognize as revenue the mortality charges, administration charges and surrender charges when received. Some of our universal life contracts assess administration charges in the early years of the contract that are compensation for services we will provide in the later years of the contract. These administration charges are deferred and are recognized over the period when we provide those future services.

For universal life long-duration contracts we maintain a liability equal to the policyholder account value. There is no provision for adverse deviation. 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.

When we issue a universal life long-duration contract we capitalize acquisition costs. We then charge these capitalized costs to expenses over the term of coverage of the contract. When we charge deferred policy acquisition costs to expenses, we use assumptions based on our best estimates of long-term experience. We review and modify these assumptions on a regular basis.

### **Separate Accounts**

We issue life contracts with guaranteed minimum returns, referred to as bank-owned life insurance contracts (BOLIs). We legally segregate and record as separate accounts the assets and liabilities for some of our BOLIs, based on the specific contract provisions. We guarantee minimum investment returns, account values and death benefits for our separate account BOLIs. Our other BOLIs are general account products.

We carry the assets of separate account BOLIs at fair value. The liabilities on separate account BOLIs primarily are the contract holders' claims to the related assets and are carried at the fair value of the assets. If the BOLI asset value is projected below the value we guaranteed, a liability is established by a charge to the company's earnings.

Generally, investment income and realized investment gains and losses of the separate accounts accrue directly to the contract holder and we do not include them in the Consolidated Statements of Income. Revenues and expenses related to separate accounts consist of contractual fees and mortality, surrender and expense risk charges. Also, each separate account BOLI includes a negotiated gain and loss sharing arrangement with the company. A percentage of each separate account's realized gain and loss representing contract fees and assessments accrues to us and is transferred from the separate account to our general account and is recognized as revenue or expense.

### **Reinsurance**

We reduce risk and uncertainty by buying property casualty and life reinsurance. Reinsurance contracts do not relieve us from our duty to policyholders, but rather help protect our financial strength to perform that duty. All of our reinsurance contracts transfer the economic risk of loss.

We also serve in a limited way as a reinsurer for other insurance companies, reinsurers and involuntary state pools. We record our transactions for such assumed reinsurance based on reports provided to us by the ceding reinsurer.

Reinsurance assumed and ceded premiums are deferred and recorded as earned premiums on a pro rata basis over the terms of the contract. We estimate loss amounts recoverable from our reinsurers based on the reinsurance policy terms. Historically, our claims with reinsurers have been paid. We do not have an allowance for uncollectible reinsurance.

### **Cash and Cash Equivalents**

Cash and cash equivalents include commercial paper, money market funds, invested cash and other overnight investments purchased with original maturities of less than three months, which are carried at fair value.

### **Investments**

Our portfolio investments are primarily in publicly traded fixed-maturity, equity and short-term investments, classified as available for sale at fair value in the consolidated financial statements. Fixed-maturity investments (taxable bonds, tax-exempt bonds and redeemable preferred stocks) and equity investments (common and non-redeemable preferred stocks) are classified as available for sale and recorded at fair value in the consolidated financial statements. The number of fixed-maturity securities trading below 100 percent of book value can be expected to fluctuate as interest rates rise or fall. Because of our strong surplus and long-term investment horizon, our intent is to hold fixed-maturity investments until maturity, regardless of short-term fluctuations in fair values.

We include unrealized gains and losses on investments, net of taxes, in shareholders' equity as accumulated other comprehensive income. Realized gains and losses on investments are recognized in net income on a specific identification basis.

Investment income consists mainly of interest and dividends. We record interest on an accrual basis and record dividends at the ex-dividend date. We amortize premiums and discounts on fixed-maturity securities using the effective interest method over the expected life of the security.

Facts and circumstances sometimes warrant investment write-downs. We record such other-than-temporary declines as realized investment losses. When evaluating for other-than-temporary impairments, the committee considers the company's intent and ability to retain a security for a period adequate to recover its cost.

### **Fair Value Disclosures**

We primarily base fair value for investments in equity and fixed-maturity securities (including redeemable preferred stock and assets held in separate accounts) on quoted market prices or on prices from FT Interactive Data, an outside resource that supplies global securities pricing, dividend, corporate action and descriptive information to support fund pricing, securities operations, research and portfolio management. When a price is not available from these sources, as the case of securities that are not publicly traded, we determine the fair value using cash flow projection models or using quotes from independent brokers. The fair value of investments priced by independent brokers is less than 1 percent of the fair value of our total investment portfolio.

We estimate fair value for liabilities under investment-type insurance contracts (annuities) using discounted cash flow calculations. We base the calculations on interest rates offered on contracts of similar nature and maturity. We base fair value for long-term senior notes and notes payable on the quoted market prices for such notes.

### **Derivative Financial Instruments and Hedging Activities**

We account for derivative financial instruments as defined by SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended by SFAS No. 137, "Deferral of the Effective Date of FASB Statement No. 133" and SFAS No. 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities" (collectively referred to as SFAS No. 133).

The hedging definitions included in SFAS No. 133 guide our recognition of the changes in the fair value of derivative financial instruments as realized gains or losses in the consolidated statements of income or as a component of accumulated other comprehensive income in shareholder's equity in the period for which they occur.

In 2006, CFC Investment Company (CFC-I) replaced \$49 million of intercompany debt owed to CFC with a short-term line of credit issued by PNC bank. CFC-I entered into an interest-rate swap contract to hedge against fluctuations of interest payments for certain variable-rate debt obligations (\$49 million notional amount). Under the interest-rate swap contract, CFC-I agreed to pay a fixed rate of interest of 5.66 percent for a three-year period ending August 29, 2009. In October 2006, we completed necessary requirements for the interest-rate swap to qualify for hedge accounting treatment under the provisions of SFAS No. 133. At December 31, 2007 and 2006, the fair value of the interest rate swap was \$1.2 million and \$430,000, respectively. We do not expect any significant reclassification into consolidated net income for the year ending December 31, 2008.

### **Securities Lending Program**

In 2006, we began actively participating in a securities lending program under which certain fixed-maturity securities from our investment portfolio are loaned to other institutions for short periods of time. We require cash collateral in excess of the market value of the loaned securities. The collateral received is invested in accordance with our guidelines in high-quality, short-duration instruments to generate additional investment income. The market value of the loaned securities is monitored on a daily basis and additional collateral is added or refunded as the market value of the loaned securities changes. As this program is accounted for as a secured borrowing, the collateral is recognized as an asset, and classified as securities lending collateral invested, with a corresponding liability for the obligation to return the collateral.

We maintain the right and ability to redeem the securities loaned on short notice and continue to earn interest on the collateral securities. Although the securities loaned have been pledged and effectively secure the cash collateral we receive, we maintain effective control over our securities, which we continue to classify as invested assets on our consolidated balance sheets. At year-end 2007, we had \$745 million in securities on loan and \$760 million of collateral. At year-end 2006, we had no securities on loan and held no collateral because we recalled our securities on loan prior to year-end. Interest income on collateral, net of fees, was \$1.5 million in 2007 and \$697,000 in 2006.

A portion of the securities lending collateral invested was placed in asset-backed commercial paper (ABCP) programs during 2007 by our lending agent. Due to the ABCP market disruption, maturities on two of our investments were extended beyond their original stated maturity dates. Only one of these investments remains outstanding. That ABCP had an amortized cost of \$73 million at February 22, 2008, compared with \$74 million at year-end 2007. The ABCP manager is continuing to work with investors to allow for an orderly liquidation of the fund. Excluding this remaining ABCP investment, all investments within our securities lending program now are in overnight securities.

## **Lease/Finance**

Our CFC Investment Company subsidiary provides auto and equipment direct financing (leases and loans) to commercial and individual clients. We generally transfer ownership of the property to the client as the terms of the leases expire. Our lease contracts contain bargain purchase options. We record income over the financing term using the effective interest method.

We capitalize and amortize lease or loan origination costs over the life of the financing using the effective interest method. These costs may include, but are not limited to: finder fees, broker fees, filing fees and the cost of credit reports. We account for these leases and loans as direct financing-type leases.

## **Asset Management**

Our CinFin Capital Management subsidiary generates revenue from management fees. We set those fees based on the market value of assets under management, and we record our revenue as it is earned.

## **Land, Building and Equipment**

We record building and equipment at cost less accumulated depreciation. Certain equipment held under capital leases also is classified as property and equipment with the related lease obligations recorded as liabilities. Our depreciation is based on estimated useful lives (ranging from three years to 39½ years) using straight-line and accelerated methods. Depreciation expense was \$38 million in both 2007 and 2006 and \$33 million in 2005. We monitor land, building and equipment for potential impairments. Potential impairments may include a significant decrease in the market values of the assets, considerable cost overruns on projects or a change in legal factors or business climate, or other factors that indicate that the carrying amount may not be recoverable.

We capitalize costs for internally developed computer software during the application development stage. These costs generally consist of external consulting, payroll and payroll-related costs.

## **Income Taxes**

We calculate deferred income tax liabilities and assets using tax rates in effect for the time when temporary differences in book and taxable income are estimated to reverse. We recognize deferred income taxes for numerous temporary differences between our taxable income and book-basis income and other changes in shareholders' equity. Such temporary differences relate primarily to unrealized gains on investments and differences in the recognition of deferred acquisition costs and insurance reserves. We charge deferred income taxes associated with unrealized appreciation (except the amounts related to the effect of income tax rate changes) to shareholders' equity in accumulated other comprehensive income. We charge deferred taxes associated with other differences to income.

## **Pending Accounting Standards**

- SFAS No. 157, Fair Value Measurements – In September 2006, FASB issued SFAS No. 157, "Fair Value Measurements." SFAS No. 157 defines fair value, establishes a framework for measuring fair value and expands disclosures of fair value measurements. The provisions of SFAS No. 157 are effective for financial statements issued for fiscal years beginning after November 15, 2007, and for interim periods within those fiscal years. Management currently is evaluating the effect SFAS No. 157 will have on our results of operations and financial position in 2008.
- SFAS No. 159, Fair Value Option for Financial Assets and Financial Liabilities – including an amendment of FASB Statement No. 115 – In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities - Including an Amendment of FASB Statement No. 115." SFAS No. 159, which is effective for fiscal years beginning after November 15, 2007, permits an entity to choose to measure many financial instruments and certain other items at fair value (on an instrument-by-instrument basis) at specified election dates. The objective is to improve financial reporting by providing an entity with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. We have not yet determined whether we will elect the fair value option for certain financial assets or liabilities; and therefore, we do not know the impact, if any, SFAS No. 159 may have on our results of operations and financial position in 2008.
- SFAS No. 160, Noncontrolling Interests In Consolidated Financial Statements – an amendment of Accounting Research Bulletin (ARB) No. 51 – In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests In Consolidated Financial Statements – an amendment of Accounting ARB No. 51. SFAS No. 160 establishes accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. The provisions of SFAS No. 160 are effective for financial statements issued for fiscal years beginning after December 15, 2008. Management currently is evaluating the effect SFAS No. 160 will have on our results of operations and financial position.

## **Adopted Accounting Standards**

- FIN No. 48, Accounting For Uncertainty in Income Taxes, an interpretation of SFAS No. 109 – In July 2006, the FASB issued FIN 48. We adopted the provisions of FIN 48 on January 1, 2007.

As a result, we recorded a charge of approximately \$300,000 to the January 1, 2007, retained earnings. As of the adoption date, we had a gross unrecognized tax benefit of \$24.8 million. See Note 10, Income Taxes, Page 98, for additional information.

- SFAS No. 155, Accounting for Certain Hybrid Financial Instruments, an amendment of SFAS Nos. 133 and 140 – In February 2006, the FASB issued SFAS No. 155, “Accounting for Certain Hybrid Financial Instruments - an amendment of FASB Statements No. 133 and 140.” SFAS No. 155 amends SFAS No. 133, “Accounting for Derivative Instruments and Hedging Activities,” and SFAS No. 140, “Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities” and resolves issues addressed in SFAS No. 133 Implementation Issue No. D1, “Application of Statement 133 to Beneficial Interest in Securitized Financial Assets.”

SFAS No. 155: (a) permits fair value re-measurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation; (b) clarifies which interest-only strips and principal-only strips are not subject to the requirements of SFAS No. 133; (c) establishes a requirement to evaluate beneficial interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation; (d) clarifies that concentrations of credit risk in the form of subordination is not embedded derivatives; and (e) eliminates restrictions on a qualifying special-purpose entity's ability to hold passive derivative financial instruments that pertain to beneficial interests that are or contain a derivative financial instrument. SFAS No. 155 was effective for all financial instruments acquired or issued in a fiscal year that begins after September 15, 2006.

On January 1, 2007, we adopted SFAS No. 155, which allows us to account for the entire hybrid financial instrument at fair value, with changes in the fair value recognized in realized investment gains and losses rather than unrealized investment gains and losses. We elected the fair value option for hybrid financial instruments to simplify our reporting, to address cost-benefit considerations and to have a consistent and reliable fair value. The transition adjustment was comprised of \$12 million of gross realized investment gains and \$4 million of gross realized investment losses, before tax. Our transition adjustment increased retained earnings by \$5 million, reducing accumulated other comprehensive income by the same amount.

- SOP 05-1, Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchange of Insurance Contracts – In September 2005, the Accounting Standards Executive Committee issued Statement of Position 05-1, “Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection With Modifications or Exchanges of Insurance Contracts.” This statement provides guidance on accounting for deferred acquisition costs on an internal replacement, which is defined broadly as a modification in product benefits, features, rights, or coverages that occurs by the exchange of an existing contract for a new contract, or by amendment, endorsement, or rider to an existing contract, or by the election of a benefit, feature, right, or coverage within an existing contract. An internal replacement that is determined to result in a replacement contract that is substantially unchanged from the replaced contract should be accounted for as a continuation of the replaced contract. Contract modifications resulting in a replacement contract that is substantially changed from the replaced contract should be accounted for as an extinguishment of the replaced contract and any unamortized deferred acquisition costs, unearned revenue liabilities, and deferred sales inducement assets from the replaced contract should not be deferred in connection with the replacement contract. The provisions of SOP 05-1 were effective for internal replacements beginning January 1, 2007. The initial adoption of SOP 05-1 did not have a material impact on our results of operations or financial position.
- SFAS No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of SFAS Nos. 87, 88, 106, and 132(R) – In September 2006, the FASB issued SFAS No. 158, “Employers Accounting for Defined Benefit and Other Retirement Plans - an amendment of FASB Statements No. 87, 88, 106 and 132(R).” SFAS No. 158 requires employers to recognize the overfunded or underfunded status of defined benefit pension and other postretirement benefit plans as an asset or liability in its statement of financial position, measured as the difference between the fair value of plan assets and the projected benefit obligation as of the end of our fiscal year-end. In addition, SFAS No. 158 requires employers to recognize changes in the funded status of defined benefit pension and other postretirement plans in the year in which the changes occur through other accumulated comprehensive income. The company adopted SFAS No. 158 effective December 31, 2006. The adoption of SFAS No. 158 resulted in an increase in liabilities of \$32 million on an after-tax basis with a corresponding reduction in accumulated other comprehensive income and shareholders' equity. SFAS No. 158 did not change the amount of net periodic benefit expense recognized in an entity's results of operations.

## 2. INVESTMENTS

The following table analyzes investment income, realized investment gains and losses and the change in unrealized investment gains and losses:

(In millions)	Years ended December 31,		
	2007	2006	2005
<b>Investment income summarized by investment category:</b>			
Interest on fixed maturities	\$ 308	\$ 300	\$ 280
Dividends on equity securities	294	262	244
Other investment income	15	15	8
Total	<u>617</u>	<u>577</u>	<u>532</u>
Less investment expenses	9	7	6
Total	<u>\$ 608</u>	<u>\$ 570</u>	<u>\$ 526</u>
<b>Realized investment gains and losses summary:</b>			
Fixed maturities:			
Gross realized gains	\$ 8	\$ 27	\$ 36
Gross realized losses	(18)	(2)	(1)
Other-than-temporary impairments	(14)	(1)	(1)
Equity securities:			
Gross realized gains	438	656	40
Gross realized losses	(24)	(5)	(6)
Other-than-temporary impairments	(2)	0	0
Securities with embedded derivatives	(11)	7	(7)
Other	5	2	0
Total	<u>\$ 382</u>	<u>\$ 684</u>	<u>\$ 61</u>
<b>Change in unrealized investment gains and losses and other summary:</b>			
Fixed maturities	\$ 7	\$ (23)	\$ (198)
Equity securities	(1,904)	200	(575)
Adjustment to deferred acquisition costs and life policy reserves	(1)	2	6
Pension obligations	12	0	0
Other	0	2	18
Income taxes on above	663	(54)	246
Total	<u>\$ (1,223)</u>	<u>\$ 127</u>	<u>\$ (503)</u>

At December 31, 2007, contractual maturity dates for fixed-maturity and short-term investments were:

(In millions)	Amortized cost	Fair value	% of Fair value
<b>Maturity dates occurring:</b>			
Less than one year	\$ 201	\$ 202	3.4 %
One year through five years	880	911	15.3
After five years through ten years	3,000	3,008	50.6
After ten years through twenty years	1,641	1,680	28.2
Over twenty years	162	148	2.5
Total	<u>\$ 5,884</u>	<u>\$ 5,949</u>	<u>100.0 %</u>

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

At December 31, 2007, investments with book value of \$52 million and fair value of \$53 million were on deposit with various states in compliance with regulatory requirements.

The following table analyzes cost or amortized cost, gross unrealized gains, gross unrealized losses and fair value for our investments:

(In millions)	Cost or amortized cost		Gross unrealized gains losses		Fair value			
<b>At December 31,</b>								
<b>2007</b>								
Fixed maturities:								
States, municipalities and political subdivisions	\$	2,518	\$	48	\$	2	\$	2,564
Convertibles and bonds with warrants attached		238		2		14		226
Public utilities		163		5		1		167
United States government		4		0		0		4
Government-sponsored enterprises		894		2		0		896
Foreign government		3		0		0		3
All other corporate bonds and short-term investments		2,064		56		31		2,089
Total	\$	<u>5,884</u>	\$	<u>113</u>	\$	<u>48</u>	\$	<u>5,949</u>
Equity securities	\$	<u>2,975</u>	\$	<u>3,414</u>	\$	<u>140</u>	\$	<u>6,249</u>
<b>2006</b>								
Fixed maturities:								
States, municipalities and political subdivisions	\$	2,382	\$	40	\$	6	\$	2,416
Convertibles and bonds with warrants attached		264		17		3		278
Public utilities		140		4		2		142
United States government		5		0		0		5
Government-sponsored enterprises		995		0		23		972
Foreign government		3		0		0		3
All other corporate bonds and short-term investments		2,045		61		22		2,084
Total	\$	<u>5,834</u>	\$	<u>122</u>	\$	<u>56</u>	\$	<u>5,900</u>
Equity securities	\$	<u>2,621</u>	\$	<u>5,181</u>	\$	<u>3</u>	\$	<u>7,799</u>

At year-end 2007, our Fifth Third Bancorp common stock holding, with fair value of \$1.691 billion and a cost of \$185 million, was our only investment for which the fair value exceeded 10 percent of shareholders' equity. At year-end 2006, our Fifth Third common stock holding, with fair value of \$2.979 billion and a cost of \$283 million, and our Exxon Mobil Corporation common stock holding, with a fair value of \$687 million and a cost of \$133 million, exceeded 10 percent of shareholders' equity.

We sold 5.5 million shares of our holdings of Fifth Third common stock in 2007. The sale contributed \$64 million to our 2007 pretax realized gains and \$42 million to net income. We sold 3.8 million shares of our holdings of ExxonMobil common stock in 2007. The sale contributed \$217 million to our 2007 pretax realized gains and \$141 million to net income.

We sold 12.7 million shares of our holdings of Alltel Corporation common stock in 2006. The sale contributed \$647 million to our 2006 pretax realized gains and \$412 million to net income.

This table reviews unrealized losses and fair values by investment category and by the duration of the securities' continuous unrealized loss position:

(In millions)	Less than 12 months		12 months or more		Total			
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses		
<b>At December 31,</b>								
<b>2007</b>								
Fixed maturities:								
States, municipalities and political subdivisions	\$	39	\$	1	\$	244	\$	2
Convertibles and bonds with warrants attached		70		14		70		14
Public utilities		13		0		41		1
Government-sponsored enterprises		0		0		20		0
All other corporate bonds and short-term investments		384		13		393		18
Total		<u>506</u>		<u>28</u>		<u>659</u>		<u>20</u>
Equity securities		<u>729</u>		<u>140</u>		<u>0</u>		<u>0</u>
Total	\$	<u>1,235</u>	\$	<u>168</u>	\$	<u>659</u>	\$	<u>20</u>
<b>2006</b>								
Fixed maturities:								
States, municipalities and political subdivisions	\$	190	\$	1	\$	589	\$	5
Convertibles and bonds with warrants attached		6		0		43		3
Public utilities		4		0		54		2
United States government		3		0		1		0
Government-sponsored enterprises		1		0		970		23
Foreign government		3		0		0		3
All other corporate bonds and short-term investments		88		2		726		20
Total		<u>295</u>		<u>3</u>		<u>2,383</u>		<u>53</u>
Equity securities		<u>39</u>		<u>2</u>		<u>11</u>		<u>1</u>
Total	\$	<u>334</u>	\$	<u>5</u>	\$	<u>2,394</u>	\$	<u>54</u>
								<u>50</u>
								<u>3</u>
								<u>59</u>

When evaluating for other-than-temporary impairments, our asset impairment committee considers the company's intent and ability to retain a security for a period adequate to recover its cost.

At December 31, 2007, 184 fixed-maturity investments with a total unrealized loss of \$20 million had been in an unrealized position for 12 months or more. Three securities were trading below 70 percent of book value with a total unrealized loss of \$6 million. The remainder were trading between 70 percent to less than 100 percent of book value.

At December 31, 2006, 482 fixed-maturity investments with a total unrealized loss of \$53 million and three equity securities with a total unrealized loss of \$1 million had been in an unrealized position for 12 months or more. All were trading between 70 percent to less than 100 percent of book value.

### 3. DEFERRED ACQUISITION COSTS

This table summarizes components of our deferred policy acquisition costs asset:

(In millions)	Years ended December 31,		
	2007	2006	2005
Deferred policy acquisition costs asset at beginning of year	\$ 453	\$ 429	\$ 400
Capitalized deferred policy acquisition costs	666	706	683
Amortized deferred policy acquisition costs	(657)	(685)	(664)
Amortized shadow deferred policy acquisition costs	(1)	3	10
Deferred policy acquisition costs asset at end of year	<u>\$ 461</u>	<u>\$ 453</u>	<u>\$ 429</u>

### 4. PROPERTY CASUALTY LOSS AND LOSS EXPENSES

This table summarizes activity loss and loss expense reserves:

(In millions)	Years ended December 31,		
	2007	2006	2005
Gross loss and loss expense reserves, January 1,	\$ 3,860	\$ 3,629	\$ 3,514
Less reinsurance receivable	504	518	537
Net loss and loss expense reserves, January 1,	<u>3,356</u>	<u>3,111</u>	<u>2,977</u>
Net incurred loss and loss expenses related to:			
Current accident year	2,076	2,124	1,972
Prior accident years	(244)	(116)	(160)
Total incurred	<u>1,832</u>	<u>2,008</u>	<u>1,812</u>
Net paid loss and loss expenses related to:			
Current accident year	785	819	772
Prior accident years	1,006	944	906
Total paid	<u>1,791</u>	<u>1,763</u>	<u>1,678</u>
Net loss and loss expense reserves, December 31,	3,397	3,356	3,111
Plus reinsurance receivable	528	504	518
Gross loss and loss expense reserves, December 31,	<u>\$ 3,925</u>	<u>\$ 3,860</u>	<u>\$ 3,629</u>

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 and 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.

Because of changes in estimates of insured events in prior years, we decreased the provision for loss and loss expenses by \$244 million, \$116 million and \$160 million in calendar years 2007, 2006 and 2005. These decreases are partly due to the effects of settling reported (case) and unreported (IBNR) reserves established in prior years for amounts less than expected. The reserve for loss and loss expenses in the consolidated balance sheets also includes \$42 million, \$36 million and \$32 million at December 31, 2007, 2006 and 2005, respectively, for certain life and health losses.

### 5. LIFE POLICY RESERVES

We establish the reserves for traditional life insurance policies based on expected expenses, mortality, morbidity, withdrawal rates 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 investment contracts 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.

Here is a summary of our life policy reserves:

(In millions)	At December 31,	
	2007	2006
Ordinary/traditional life	\$ 505	\$ 453
Universal life	410	396
Annuities	541	537
Other	22	23
Total	\$ 1,478	\$ 1,409

At both December 31, 2007 and 2006, the fair value associated with the annuities shown above was approximately \$564 million and \$563 million, respectively.

## 6. NOTES PAYABLE

At December 31, 2007, we had two lines of credit with commercial banks amounting to \$225 million with an outstanding balance of \$69 million. We had two lines of credit with commercial banks amounting to \$125 million with an outstanding balance of \$49 million at year-end 2006. The company had no compensating balance requirement on short-term debt for either 2007 or 2006. Interest rates charged on borrowings ranged from 5.4 percent to 8.3 percent during 2007.

The company's subsidiary, CFC Investment Company, entered into an interest-rate swap agreement during 2006, which expires August 29, 2009. The purpose of the interest-rate swap contract is to hedge against fluctuations of interest payments for certain variable-rate debt obligations (\$49 million notional amount). Under the interest-rate swap contract, CFC-I agreed to pay a fixed rate of interest of 5.66 percent. This swap is reflected at fair value in the consolidated balance sheets as a component of shareholders' equity in accumulated other comprehensive income. The unrealized loss, net of tax, was \$594,000 at year-end 2007 compared with \$69,000 at year-end 2006. Management does not expect any significant amounts to be reclassified into earnings as a result of interest rate changes in the next 12 months.

## 7. SENIOR DEBT

This table summarizes the principal amounts of our long-term debt excluding unamortized discounts:

(In millions)			At December 31,	
Interest rate	Year of issue		2007	2006
6.900%	1998	Senior debentures, due 2028	\$ 28	\$ 28
6.920%	2005	Senior debentures, due 2028	392	392
6.125%	2004	Senior notes, due 2034	375	375
		Total	\$ 795	\$ 795

The fair value of our senior debt approximated \$802 million at year-end 2007 and \$850 million at year-end 2006. None of the notes are encumbered by rating triggers.

## 8. SHAREHOLDERS' EQUITY AND DIVIDEND RESTRICTIONS

Our insurance subsidiary declared dividends to the parent company of \$420 million in 2007 and \$275 million in both 2006 and 2005. State regulatory requirements restrict the dividends insurance subsidiaries can pay. Generally, the most our insurance subsidiaries can pay without prior regulatory approval is the greater of 10 percent of policyholder surplus or 100 percent of statutory net income for the prior calendar year. Dividends exceeding these limitations may be paid only with approval of the insurance department of the domiciliary state. During 2008, the total dividends that our lead insurance subsidiary may pay to our parent company without regulatory approval will be approximately \$658 million.

As of December 31, 2007, 10.6 million shares of common stock were available for future stock option grants.

Declared cash dividends per share were \$1.42, \$1.34 and \$1.21 for the years ended December 31, 2007, 2006 and 2005, respectively.



## Accumulated Other Comprehensive Income

The change in unrealized gains and losses on investments, pension obligations and derivatives included:

(In millions)	Years ended December 31,								
	2007			2006			2005		
	Before tax	Income tax	Net	Before tax	Income tax	Net	Before tax	Income tax	Net
Accumulated unrealized gains (losses) on securities available for sale at January 1,	\$ 5,241	\$ 1,830	\$ 3,411	\$ 5,060	\$ 1,776	\$ 3,284	\$ 5,809	\$ 2,022	\$ 3,787
Net unrealized gains (losses)	(1,515)	(530)	(985)	880	298	582	(692)	(226)	(466)
Reclassification adjustment for (gains) losses included in net income	(382)	(137)	(245)	(701)	(245)	(456)	(61)	(21)	(40)
Adjustment to deferred acquisition costs and life policy reserves	(1)	-	(1)	2	1	1	4	1	3
Effect on other comprehensive income	(1,898)	(667)	(1,231)	181	54	127	(749)	(246)	(503)
Accumulated unrealized gains (losses) on securities available for sale at December 31,	\$ 3,343	\$ 1,163	\$ 2,180	\$ 5,241	\$ 1,830	\$ 3,411	\$ 5,060	\$ 1,776	\$ 3,284
Accumulated unrealized gains (losses) on hybrid financial securities at January 1,	\$ (7)	\$ (2)	\$ (5)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Net unrealized gains (losses)	-	-	-	-	-	-	-	-	-
Reclassification adjustment for (gains) losses included in net income	-	-	-	-	-	-	-	-	-
Effect on other comprehensive income	-	-	-	-	-	-	-	-	-
Accumulated unrealized gains (losses) on hybrid financial securities at December 31,	\$ (7)	\$ (2)	\$ (5)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Accumulated unrealized losses for pension obligations at January 1,	\$ (49)	\$ (17)	\$ (32)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Cumulative effect of change in accounting for pension obligations	-	-	-	(49)	(17)	(32)	-	-	-
Current year change in accounting for pension obligations	12	4	8	-	-	-	-	-	-
Accumulated unrealized losses for pension obligations at December 31,	\$ (37)	\$ (13)	\$ (24)	\$ (49)	\$ (17)	\$ (32)	\$ -	\$ -	\$ -
Accumulated other comprehensive income at January 1,	\$ 5,185	\$ 1,811	\$ 3,374	\$ 5,060	\$ 1,776	\$ 3,284	\$ 5,809	\$ 2,022	\$ 3,787
Other comprehensive income (loss)	(1,898)	(667)	(1,231)	181	54	127	(749)	(246)	(503)
Effect of change in accounting for pension obligations and hybrid financial securities	12	4	8	(49)	(17)	(32)	-	-	-
Accumulated other comprehensive income at December 31,	\$ 3,299	\$ 1,148	\$ 2,151	\$ 5,192	\$ 1,813	\$ 3,379	\$ 5,060	\$ 1,776	\$ 3,284

## 9. REINSURANCE

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

(In millions)	Years ended December 31,		
	2007	2006	2005
Direct earned premiums	\$ 3,278	\$ 3,296	\$ 3,209
Assumed earned premiums	22	26	28
Ceded earned premiums	(175)	(158)	(179)
Net earned premiums	\$ 3,125	\$ 3,164	\$ 3,058

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

(In millions)	Years ended December 31,		
	2007	2006	2005
Direct incurred loss and loss expenses	\$ 1,922	\$ 2,072	\$ 1,898
Assumed incurred loss and loss expenses	17	13	40
Ceded incurred loss and loss expenses	(107)	(77)	(126)
Net incurred loss and loss expenses	<u>\$ 1,832</u>	<u>\$ 2,008</u>	<u>\$ 1,812</u>

Our statements of income include earned life insurance premiums on assumed and ceded business:

(In millions)	Years ended December 31,		
	2007	2006	2005
Direct earned premiums	\$ 178	\$ 159	\$ 150
Assumed earned premiums	0	0	0
Ceded earned premiums	(53)	(44)	(44)
Net earned premiums	<u>\$ 125</u>	<u>\$ 115</u>	<u>\$ 106</u>

Our statements of income include life insurance contract holder benefits incurred on assumed and ceded business:

(In millions)	Years ended December 31,		
	2007	2006	2005
Direct contract holders benefits incurred	\$ 173	\$ 162	\$ 141
Assumed contract holders benefits incurred	0	0	0
Ceded contract holders benefits incurred	(40)	(40)	(39)
Net incurred loss and loss expenses	<u>\$ 133</u>	<u>\$ 122</u>	<u>\$ 102</u>

## 10. INCOME TAXES

Deferred tax assets and liabilities reflect temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amount recognized for tax purposes. The significant components of deferred tax assets and liabilities included in the balance sheet at December 31 were as follows:

(In millions)	At December 31,	
	2007	2006
Deferred tax liabilities:		
Unrealized gains on investments and derivatives	\$ 1,158	\$ 1,824
Deferred acquisition costs	145	142
Other	35	36
Total	<u>1,338</u>	<u>2,002</u>
Deferred tax assets:		
Loss and loss expense reserves	200	190
Unearned premiums	108	109
Life policy reserves	13	22
Other	40	28
Total	<u>361</u>	<u>349</u>
Net deferred tax liability	<u>\$ 977</u>	<u>\$ 1,653</u>

The provision for federal income taxes is based upon filing a consolidated income tax return for the company and subsidiaries. As of December 31, 2007, we had no operating or capital loss carry forwards.

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

	Years ended December 31,		
	2007	2006	2005
Tax at statutory rate	35.0 %	35.0 %	35.0 %
Increase (decrease) resulting from:			
Tax-exempt municipal bonds	(2.7)	(2.2)	(3.2)
Dividend exclusion	(4.7)	(3.9)	(5.7)
Other	0.7	1.1	0.7
Effective rate	<u>28.3 %</u>	<u>30.0 %</u>	<u>26.8 %</u>

### Interpretation No. 48, Accounting for Uncertainty in Income Taxes, an Interpretation of SFAS No. 109

We adopted the provisions of FIN 48 on January 1, 2007. As a result of the adoption, we recorded a charge of approximately \$300,000 to retained earnings. As of the adoption date, we had a gross unrecognized tax benefit (FIN 48 liability) of \$25 million.

We reconcile the unrecognized tax benefit between January 1, 2007, and December 31, 2007, as follows:

(In millions)

	2007
Gross unrecognized tax benefits at January 1,	\$ 24.8
Gross increase in prior year positions	0
Gross decrease in prior year positions	(12.0)
Gross increase in current year positions	1.4
Gross decrease in current year positions	0
Settlements with tax authorities	0
Decrease for lapse in applicable statute of limitations	0
Gross unrecognized tax benefits at December 31,	<u>\$ 14.2</u>

The FIN 48 liability is carried in other liabilities in the condensed consolidated balance sheets as of December 31, 2007. Included in the FIN 48 liability is an immaterial amount that would change the effective tax rate, if recognized. Although no penalties currently are accrued, if incurred, they would be recognized as a component of income tax expense. Accrued interest expense is recognized as other operating expense in the condensed consolidated statements of income. The accrued interest liability was \$2.5 million and \$1.8 million as of January 1, 2007, and December 31, 2007, respectively. The consolidated statements of income for the current year reflected net Internal Revenue Service interest income of \$1.5 million from a reduction in the accrued interest liability and interest received on refund claims.

The IRS has concluded the examination phase of its audit of our 2002 through 2004 tax years. In November 2007, we met with IRS appeals personnel in an attempt to settle the unresolved issues related to those tax years. As a result of the appeals process, we reached a preliminary agreement with the IRS settling those unresolved issues. Until an IRS administrative review for the appeals settlement has been performed, the issues for which preliminary agreement have been reached cannot be considered effectively settled under FIN 48. However, as a result of the preliminary agreement, the FIN 48 liability associated with the 2002 to 2004 tax years have been adjusted and certain assumptions made for our FIN 48 liability associated with the tax years 2005 through 2007 tax years have been adjusted. We anticipate that the 2002 through 2004 tax years will be effectively settled in the next 12 months, resulting in a settlement of the FIN 48 liability of approximately \$2 million, primarily related to the valuation of our loss reserves.

The IRS has begun the examination phase of its audit for our 2005 and 2006 tax years. It is reasonably possible that a change in the unrecognized tax benefits may occur once the examination phase has concluded. At this time, we can neither estimate the settlement date of, nor quantify an estimated range for any potential change to, the unrecognized tax benefits relating to these years.

In addition to our Internal Revenue Service filings, we file income tax returns in various state jurisdictions. Material amounts of income tax are paid to Ohio, Illinois and Florida. Of the state jurisdictions, Illinois has concluded an audit of tax years 2004 and 2005 resulting in an immaterial change to tax. No other audits are currently under way, nor is the company aware of any pending audits.

## 11. NET INCOME PER COMMON SHARE

Basic earnings per share are computed based on the weighted average number of shares outstanding. Diluted earnings per share are computed based on the weighted average number of common and dilutive potential common shares outstanding. We have adjusted shares and earnings per share to reflect all stock splits and dividends prior to December 31, 2007.

Here are calculations for basic and diluted earnings per share:

(In millions)	Years ended December 31,		
	2007	2006	2005
Numerator:			
Net income—basic and diluted	\$ <u>855</u>	\$ <u>930</u>	\$ <u>602</u>
Denominator:			
Weighted-average common shares outstanding	170,595,204	173,423,395	175,062,669
Effect of stock options and non-vested shares	1,572,248	2,027,946	2,053,457
Adjusted weighted-average shares	<u>172,167,452</u>	<u>175,451,341</u>	<u>177,116,126</u>
Earnings per share:			
Basic	\$ 5.01	\$ 5.36	\$ 3.44
Diluted	4.97	5.30	3.40
Number of anti-dilutive option shares	1,870,579	1,336,150	-
Exercise price of anti-dilutive option shares	\$ 44.79-45.26	\$ 45.26	-

The only current sources of dilution of our common shares are outstanding stock options to purchase shares of common stock and non-vested shares. The above table shows the number of anti-dilutive options shares at year-end 2007, 2006 and 2005. We did not include these options in the computation of net income per common share (diluted) because their exercise would have an anti-dilutive effect.

## 12. EMPLOYEE BENEFIT PENSION PLAN

We sponsor a defined contribution plan (401(k) savings plan) and a defined benefit pension plan covering substantially all employees. We do not contribute to the 401(k) plan but we do pay all operating expenses. Benefits for the defined benefit pension plan are based on years of credited service and compensation level. Contributions are based on the frozen entry age actuarial cost method. We also maintain a supplemental retirement plan (SERP) with liabilities of approximately \$6 million and \$5 million at year-end 2007 and 2006. The SERP is included in the obligation and expense amounts. Our pension expense is based on certain actuarial assumptions and also is composed of several components that are determined using the projected unit credit actuarial cost method.

Key assumptions used in developing the 2007 net pension obligation were a 6.25 percent discount rate and rates of compensation increases ranging from 4 percent to 6 percent. To determine the discount rate, the plan's particular liability characteristics – the amounts, timing and interest sensitivity of expected benefit payments – were evaluated and then matched to a yield curve based on actual high-quality corporate bonds across a full maturity spectrum. Once the plan's projected cash flows matched the yield curve, a present value was developed, which was then calibrated to a single-equivalent discount rate. That discount rate, when applied to a single sum, would generate the necessary cash flows to pay benefits when due. We increased the rate by 0.5 percentage points in 2007 due to market interest rates conditions. We based the rates of compensation increase on the company's historical data, which led us to lower the range from the 5 percent to 7 percent used in previous years.

Key assumptions used in developing the 2007 net pension expense were a 5.75 percent discount rate, an 8 percent expected return on plan assets and rates of compensation increases ranging from 4 percent to 6 percent. The 8 percent return on plan assets assumption is based partially on the fact that substantially all of the investments held by the pension plan are common stocks that pay dividends. We believe this rate is representative of the expected long-term rate of return on these assets. These assumptions were consistent with the prior year, except that the discount rate was increased by 0.25 percentage points due to market interest rate conditions.

Benefit obligation activity using an actuarial measurement date at December 31 follows:

(In millions)	Qualified Pension Plan		Supplemental Pension Plan		Totals	
	2007	2006	2007	2006	2007	2006
Change in projected benefit obligation:						
Benefit obligation at beginning of year	\$ 266	\$ 235	\$ 5	\$ 9	\$ 271	\$ 244
Service cost	17	16	0	0	17	16
Interest cost	16	14	0	0	16	14
Plan amendments	0	0	0	0	0	0
Actuarial loss/(gain)	(30)	11	1	0	(29)	11
Benefits paid	(5)	(10)	0	(4)	(5)	(14)
Projected benefit obligation at end of year	<u>\$ 264</u>	<u>\$ 266</u>	<u>\$ 6</u>	<u>\$ 5</u>	<u>\$ 270</u>	<u>\$ 271</u>
Accumulated benefit obligation	<u>\$ 201</u>	<u>\$ 200</u>	<u>\$ 5</u>	<u>\$ 4</u>	<u>\$ 206</u>	<u>\$ 204</u>
Change in plan assets:						
Fair value of plan assets at beginning of year	\$ 208	\$ 173	\$ 0	\$ 0	\$ 208	\$ 173
Actual return on plan assets	(4)	35	0	0	(4)	35
Employer contributions	11	10	0	4	11	14
Benefits paid	(5)	(10)	0	(4)	(5)	(14)
Fair value of plan assets at end of year	<u>\$ 210</u>	<u>\$ 208</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 210</u>	<u>\$ 208</u>
Funded (unfunded) status:						
Funded (unfunded) status at end of year	<u>\$ (54)</u>	<u>\$ (58)</u>	<u>\$ (6)</u>	<u>\$ (5)</u>	<u>\$ (60)</u>	<u>\$ (63)</u>

The accumulated benefit obligation was \$206 million and \$204 million at December 31, 2007 and 2006, respectively. The fair value of our stock comprised \$25 million (12 percent of total plan assets) at December 31, 2007, and \$29 million (14 percent of total plan assets) at December 31, 2006.

A reconciliation follows of the funded status at the end of the measurement period to the amounts recognized in the balance sheet at December 31, 2007:

(In millions)	Qualified Pension Plan			Supplemental Pension Plan		
	2007	2007	Total 2007	2006	2006	Total 2006
Amounts recognized in the balance sheet consists of:						
Noncurrent liability	\$ (54)	\$ (6)	\$ (60)	\$ (58)	\$ (5)	\$ (63)
Total	\$ (54)	\$ (6)	\$ (60)	\$ (58)	\$ (5)	\$ (63)
Amounts recognized in accumulated other comprehensive income not yet recognized as a component of net periodic benefit costs consist of:						
Net actuarial loss/(gain)	\$ 27	\$ 1	\$ 28	\$ 40	\$ (1)	\$ 39
Prior service cost	6	3	9	6	4	10
Total	\$ 33	\$ 4	\$ 37	\$ 46	\$ 3	\$ 49

The projected benefit obligation and fair value of plan assets for pension plans with a projected benefit obligation in excess of plan assets at December 31 follows:

(In millions)	Qualified Pension Plan		Supplemental Pension Plan		Total	
	2007	2006	2007	2006	2007	2006
Projected benefit obligation in excess of plan assets:						
Projected benefit obligation at end of year	\$ 264	\$ 266	\$ 6	\$ 5	\$ 270	\$ 271
Fair value of plan assets at end of year	210	208	0	0	210	208

The projected benefit obligation, accumulated benefit obligation and fair value of plan assets for pension plans with an accumulated benefit obligation in excess of plan assets at December 31 follows:

(In millions)	Supplemental Pension Plan	
	2007	2006
Accumulated benefit obligation in excess of plan assets:		
Projected benefit obligation at end of year	\$ 6	\$ 5
Accumulated benefit obligation at end of year	5	4
Fair value of plan assets at end of year	0	0

The weighted-average assumptions used to determine benefit obligations at December 31 follows:

(In millions)	2007	2006
	Discount rate	6.25 %
Rate of compensation increase	4-6	4-6

We evaluate our pension plan assumptions annually and update them as necessary. The discount rate assumptions for our benefit obligation track with Moody's Aa bond yield and yearly adjustments reflect any changes to those bond yields. Compensation increase assumptions reflect historical calendar year compensation increases.

Here are the components of our net periodic benefit cost at December 31:

(In millions)	Qualified Pension Plan			Supplemental Pension Plan			Total		
	2007	2006	2005	2007	2006	2005	2007	2006	2005
Service cost	\$ 17	\$ 16	\$ 13	\$ 0	\$ 0	\$ 0	\$ 17	\$ 16	\$ 13
Interest cost	16	14	12	0	0	1	16	14	13
Expected return on plan assets	(15)	(14)	(13)	0	0	0	(15)	(14)	(13)
Amortization of actuarial gain, prior service cost and transition asset	2	2	1	1	1	0	3	3	1
Net periodic benefit cost	\$ 20	\$ 18	\$ 13	\$ 1	\$ 1	\$ 1	\$ 21	\$ 19	\$ 14

Here is a summary of the weighted-average assumptions we use to determine our net expense for the plan:

	Qualified Pension Plan			Supplemental Pension Plan		
	2007	2006	2005	2007	2006	2005
Discount rate	5.75 %	5.50 %	5.75 %	5.75 %	5.50 %	5.75 %
Expected return on plan assets	8.00	8.00	8.00	NA	NA	NA
Rate of compensation increase	4-6	5-7	5-7	4-6	5-7	5-7

Our pension plan asset allocations by category are:

Asset category:	At December 31,	
	2007	2006
Equity securities	94 %	94 %
Fixed maturities	3	4
Cash and cash equivalents	3	2
Total	100 %	100 %

We expect to contribute approximately \$10 million to our pension plan in 2008 with a target allocation of 90 percent equity securities and 10 percent fixed maturities and cash.

We expect to make the following benefit payments, which reflect expected future service:

(In millions)	Qualified Pension Plan	Supplemental Pension Plan	Total
For the years ended December 31,			
2008	\$ 9	\$ 0	\$ 9
2009	12	0	12
2010	13	6	19
2011	10	0	10
2012	15	0	15
Years 2013-2017	108	3	111

The estimated costs to be amortized from accumulated other comprehensive income into net periodic benefit cost over the next year are as follows:

(In millions)	Qualified Pension Plan	Supplemental Pension Plan	Total
Actuarial loss/ (gain)	\$ 0	\$ 1	\$ 1
Prior service cost	1	0	1
Total	<u>\$ 1</u>	<u>\$ 1</u>	<u>\$ 2</u>

### 13. STATUTORY ACCOUNTING INFORMATION (UNAUDITED)

Insurance companies use statutory accounting practices (SAP) as prescribed by regulatory authorities. The three primary differences between SAP and GAAP are:

- policy acquisition costs are expensed when incurred,
- life insurance reserves are based upon different actuarial assumptions and
- deferred income taxes are valued and established using a different basis.

Statutory net income and capital and surplus as determined in accordance with SAP prescribed or permitted by insurance regulatory authorities for four legal entities, our insurance subsidiary and its three insurance subsidiaries, are as follows:

(In millions)	SAP Net Income			Capital and Surplus	
	Years ended December 31,			At December 31,	
	2007	2006	2005	2007	2006
The Cincinnati Insurance Company	\$ 658	\$ 572	\$ 517	\$ 4,307	\$ 4,750
The Cincinnati Casualty Company	12	15	13	278	282
The Cincinnati Indemnity Company	1	2	2	66	62
The Cincinnati Specialty Underwriters Insurance Company	0	0	0	196	0
The Cincinnati Life Insurance Company	39	28	21	477	479

Statutory capital and surplus for our insurance subsidiary, The Cincinnati Insurance Company, includes capital and surplus of its four insurance subsidiaries.

### 14. TRANSACTIONS WITH AFFILIATED PARTIES

We paid certain officers and directors, or insurance agencies of which they are shareholders, commissions of approximately \$7 million, \$7 million and \$6 million on premium volume of approximately \$37 million, \$40 million and \$41 million for 2007, 2006 and 2005, respectively.

### 15. COMMITMENTS AND CONTINGENT LIABILITIES

Legal issues are part of the normal course of business for all companies. As such, we have various litigation and claims against us in process and pending. Having analyzed those claims with our legal counsel, we believe the outcomes of normal insurance matters will not have a material effect on our consolidated financial position, results of operations or cash flows. We further believe that the outcomes of non insurance matters will be covered by insurance coverage or will not have a material effect on our consolidated financial position, results of operations or cash flows.

### 16. STOCK-BASED ASSOCIATE COMPENSATION PLANS

The adoption of SFAS No. 123(R) on January 1, 2006, reduced our income before income taxes by \$14 million and \$17 million in the years ended December 31, 2007 and 2006, and reduced our net income by \$11 million and \$14 million in the years ended December 31, 2007 and 2006.

The weighted-average grant-date fair value of options granted during 2007 and 2006 was \$9.43 and \$10.09 per share, respectively. The total intrinsic value of options exercised during the years ended December 31, 2007, 2006 and 2005, was \$8 million, \$22 million and \$9 million, respectively. In total, options vested during the year ended December 31, 2007, had no intrinsic value. The total intrinsic value of options vested during the years ended December 31, 2006 and 2005, was \$10 million and \$12 million. (Intrinsic value is the market price less the exercise price.)

Under the modified-prospective-transition method, we recognized:

- Compensation cost for all stock options granted subsequent to January 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of SFAS No. 123(R)
- Compensation cost for all non-vested stock options granted prior to January 1, 2006, that vested during 2007, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123 and
- Compensation cost for all non-vested stock options that have nonsubstantive vesting requirements, such as those to associates who are eligible for retirement.

Results for prior periods have not been retrospectively adjusted for SFAS No. 123(R). As of December 31, 2007, we had \$13 million of unrecognized total compensation cost related to non-vested stock options. That cost will be recognized over a weighted-average period of 1.7 years. SFAS No. 123(R) also requires us to classify certain tax benefits related to share-based compensation deductions as cash from financing activities. For the year ended December 31, 2007, these tax benefits totaled \$2 million.

In determining the share-based compensation amounts for 2007, the fair value of each option granted in 2007 was estimated on the date of grant using the binomial option-pricing model with the following weighted average assumptions used for grants in 2007: dividend yield of 3.33 percent; expected volatility ranging from 18.29 percent to 24.14 percent; risk-free interest rates ranging from 4.80 percent to 4.81 percent; and expected lives of five to seven years.

In determining the share-based compensation amounts for 2006, the fair value of each option granted in 2006 was estimated on the date of grant using the binomial option-pricing model with the following weighted average assumptions used for grants in 2006: dividend yield of 3.22 percent; expected volatility ranging from 20.25 to 27.12 percent; risk-free interest rates ranging from 4.5 to 4.61 percent; and expected lives of five to seven years.

The following table illustrates the effect on net income and earnings per share if we had applied the fair value recognition provisions of SFAS No. 123 to options granted under our stock option plans prior to our adoption of SFAS No. 123(R) on January 1, 2006. For purposes of this pro forma disclosure, the fair value of each option was estimated on the date of grant using the binomial option-pricing model. In 2005, the weighted-average assumptions used for grants were a dividend yield of 2.66 percent; expected volatility of 25.61 percent; risk-free interest rate of 4.62 percent; and expected lives of 10 years.

(In millions except per share data)		Year ended December 31, 2005
Net income	As reported	\$ 602
Stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects		13
	Pro forma	<u>\$ 589</u>
Net income per common share—basic	As reported	\$ 3.44
	Pro forma	3.36
Net income per common share—diluted	As reported	\$ 3.40
	Pro forma	3.32

Here is a summary of options information:

(Dollars in millions, shares in thousands)	Shares	Weighted- average exercise	Aggregate intrinsic value
<b>2007</b>			
Outstanding at beginning of year	10,667	\$ 36.03	
Granted/reinstated	582	44.79	
Exercised	(634)	29.56	
Forfeited/revoked	(135)	38.86	
Outstanding at end of period	<u>10,480</u>	36.86	\$ 42
Options exercisable at end of period	8,597	\$ 35.25	\$ 42
Weighted-average fair value of options granted during the period		9.43	
<b>2006</b>			
Outstanding at beginning of year	10,589	\$ 33.70	
Granted/reinstated	1,372	45.26	
Exercised	(1,084)	24.93	
Forfeited/revoked	(210)	36.16	
Outstanding at end of period	<u>10,667</u>	36.03	\$ 99
Options exercisable at end of period	7,985	\$ 33.70	\$ 93
Weighted-average fair value of options granted during the period		10.09	
<b>2005</b>			
Outstanding at beginning of year	9,698	\$ 32.05	
Granted/reinstated	1,504	41.62	
Exercised	(467)	24.18	
Forfeited/revoked	(146)	35.89	
Outstanding at end of period	<u>10,589</u>	33.70	\$ 116
Options exercisable at end of period	7,794	\$ 31.69	\$ 101
Weighted-average fair value of options granted during the period		12.49	

Cash received from the exercise of options was \$19 million, \$27 million and \$11 million for the years ended December 31, 2007, 2006 and 2005, respectively. The tax benefit realized on options exercised was \$2 million for the year ended December 31, 2007, \$3 million for the year ended December 31, 2006, and \$1 million for the year ended December 31, 2005.

Options outstanding and exercisable consisted of the following at December 31, 2007:

(Shares in thousands)	Options outstanding			Options exercisable	
	Shares	Weighted-average remaining contractual life	Weighted- average exercise price	Shares	Weighted- average exercise price
Range of exercise prices					
\$25.00 to \$29.99	831	2.08 yrs	\$ 26.97	831	\$ 26.97
\$30.00 to \$34.99	4,293	3.24 yrs	32.70	4,293	32.70
\$35.00 to \$39.99	1,836	4.45 yrs	38.45	1,836	38.45
\$40.00 to \$44.99	2,220	6.71 yrs	42.38	1,195	41.51
\$45.00 to \$49.99	1,300	8.05 yrs	45.26	442	45.26
Total	<u>10,480</u>	4.69 yrs	36.86	<u>8,597</u>	35.25

The weighted-average remaining contractual life for exercisable awards as of December 31, 2007, was 4.20 years. As of December 31, 2007, 10.6 million shares of common stock were available for future stock option grants. We currently issue new shares for option exercises.

### Restricted Stock Units

In January 2007, the compensation committee granted service-based and performance-based restricted stock units. The service-based restricted stock units vest at the end of a three-year vesting period. The performance based restricted stock units granted in 2007 will vest on March 1, 2010, if certain performance targets are attained. As of December 31, 2007, management assumed for accounting purposes that performance targets used for the 2007 awards would be met, which resulted in the inclusion of costs for these awards in share-based compensation for 2007.

The fair value of the restricted stock unit awards was determined based on the fair value on the date of grant less the present value of the dividends that holders of restricted stock units do not receive on the restricted stock units during the vesting period.



Restricted stock unit awards in 2007 were:

(Shares in thousands)	Service - based nonvested shares	Weighted - average grant- date fair value	Performance - based nonvested shares	Weighted - average grant- date fair value
Nonvested at January 1, 2007	0	\$ 0.00	0	\$ 0.00
Granted	168	40.74	35	40.74
Vested	0	0.00	0	0.00
Forfeited	(6)	40.74	0	0.00
Nonvested at December 31, 2007	<u>162</u>	40.74	<u>35</u>	40.74

## 17. SEGMENT INFORMATION

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

- Commercial lines property casualty insurance
- Personal lines property casualty insurance
- Life insurance
- Investment operations

We report as "Other" the non-investment operations of the parent company, CFC Investment Company and CinFin Capital Management Company (excluding client investment activities), as well as other income of our insurance subsidiary. In 2007, an immaterial level of expenses from The Cincinnati Specialty Underwriters Insurance Company was included in the commercial lines property casualty insurance segment while an immaterial level of expenses for CSU Producer Resources was included in Other.

**Revenues** come primarily from unaffiliated customers:

- All three insurance segments record revenues from insurance premiums earned. Life insurance segment revenues also include separate account investment management fees.
- Our investment operations' revenues are pretax net investment income plus realized investment gains and losses.
- Other revenues are primarily finance/lease income.

**Income or loss before income taxes** for each segment is reported based on the nature of that business area's operations:

- Income before income taxes for the insurance segments is defined as underwriting income or loss.
  - For commercial lines and personal lines insurance segments, we calculate underwriting income or loss by recording premiums earned minus loss and loss expenses and underwriting expenses incurred.
  - For the life insurance segment, we calculate underwriting income or loss by recording premiums earned and separate account investment management fees, minus contract holder benefits and expenses incurred, plus investment interest credited to contract holders.
- Income before income taxes for the investment operations segment is net investment income plus realized investment gains and losses for investments of the entire company, minus investment interest credited to contract holders of the life insurance segment.
- Loss before income taxes for the Other category is primarily due to interest expense from debt of the parent company and operating expenses of our headquarters.

**Identifiable assets** are used by each segment in its operations. We do not separately report the identifiable assets for the commercial or personal lines segments because we do not use that measure to analyze the segments. We include all fixed-maturity and equity security investment assets, regardless of ownership, in the investment operations segment.

This table summarizes segment information:

(In millions)	Years ended December 31,		
	2007	2006	2005
<b>Revenues:</b>			
Commercial lines insurance			
Commercial casualty	\$ 827	\$ 831	\$ 759
Commercial property	497	491	467
Commercial auto	440	453	457
Workers' compensation	373	366	328
Specialty packages	146	141	137
Surety and executive risk	100	93	80
Machinery and equipment	28	27	26
Total commercial lines insurance	<u>2,411</u>	<u>2,402</u>	<u>2,254</u>
Personal lines insurance			
Personal auto	342	385	433
Homeowner	285	289	282
Other personal lines	87	88	89
Total personal lines insurance	<u>714</u>	<u>762</u>	<u>804</u>
Life insurance	129	118	110
Investment operations	990	1,254	587
Other	15	15	12
Consolidated eliminations	0	(1)	0
Total	<u>\$ 4,259</u>	<u>\$ 4,550</u>	<u>\$ 3,767</u>
<b>Income (loss) before income taxes:</b>			
Insurance underwriting results:			
Commercial lines insurance	\$ 261	\$ 208	\$ 285
Personal lines insurance	43	(27)	45
Life insurance	3	(1)	7
Investment operations	931	1,200	536
Other	(46)	(51)	(50)
Total	<u>\$ 1,192</u>	<u>\$ 1,329</u>	<u>\$ 823</u>
<b>Identifiable assets:</b>			
Property casualty insurance	\$ 2,281	\$ 2,220	
Life insurance	938	886	
Investment operations	12,322	13,820	
Other	1,096	296	
Total	<u>\$ 16,637</u>	<u>\$ 17,222</u>	

## 18. QUARTERLY SUPPLEMENTARY DATA (UNAUDITED)

This table includes unaudited quarterly financial information for the years ended December 31, 2007 and 2006:

(Dollars in millions except per share data)	Quarter					Full year
	1 <sup>st</sup>	2 <sup>nd</sup>	3 <sup>rd</sup>	4 <sup>th</sup>		
<b>2007</b>						
Revenues	\$ 1,029	\$ 1,267	\$ 980	\$ 983	\$ 4,259	
Income before income taxes	271	508	160	254	1,192	
Net income	194	351	124	187	855	
Net income per common share—basic	1.12	2.04	0.72	1.12	5.01	
Net income per common share—diluted	1.11	2.02	0.72	1.11	4.97	
<b>2006</b>						
Revenues	\$ 1,607	\$ 981	\$ 967	\$ 995	\$ 4,550	
Income before income taxes	834	175	148	172	1,329	
Net income	552	132	115	130	930	
Net income per common share—basic	3.17	0.77	0.67	0.75	5.36	
Net income per common share—diluted	3.13	0.76	0.66	0.75	5.30	

Note: The sum of the quarterly reported amounts may not equal the full year as each is computed independently.

### Significant realized gains:

Over the course of 2007, we sold 3.8 million shares of Exxon Mobil Corporation, 5.5 million shares of Fifth Third Bancorp common stock, all of our FirstMerit Corporation common stock holdings and disposed of the majority of our real estate investment trust holdings.

In the first quarter of 2006, we sold our Alltel Corporation common stock holding.

## **Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

We had no disagreements with the independent registered public accounting firm on accounting and financial disclosure during the last two fiscal years.

### **Item 9A. 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 December 31, 2007. 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
- 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 December 31, 2007, 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. Management's Annual Report on Internal Control Over Financial Reporting and the Attestation Report of the Independent Registered Public Accounting Firm are set forth in Item 8, Pages 81 and 82.

### **Item 9B. Other Information**

None

## **Part III**

Our Proxy Statement will be filed with the SEC in preparation for the 2008 Annual Meeting of Shareholders no later than April 4, 2008. As permitted in Paragraph G(3) of the General Instructions for Form 10-K, we are incorporating by reference to that statement portions of the information required by Part III as noted in Item 10 through Item 14 below.

### **Item 10. Directors and Executive Officers of the Registrant**

- a) Information about our directors and executive officers is in the Proxy Statement under "Security Ownership of Principal Shareholders and Management," "Information Regarding Nondirector Executive Officers" and "Information regarding the Board of Directors."
- b) Information about Section 16(a) beneficial ownership reporting compliance appears in the Proxy Statement under "Section 16(a) Beneficial Ownership Reporting Compliance."
- c) Information about the "Code of Ethics for Senior Financial Officers" appeared in the 2004 Proxy Statement as an appendix and is available in the Investors section of our Web site, [www.cinfin.com](http://www.cinfin.com). Our code of ethics applies to those who are responsible for preparing and disclosing our financial information. This includes our chief executive officer, chief financial officer, chief investment officer and others performing similar functions or reporting directly to these officers.
- d) Information about our audit committee membership and our financial expert compliance appears in the Proxy Statement under "Information Regarding the Board of Directors" and "Report of the Audit Committee."
- e) The procedures under which shareholders may recommend director nominees have not changed during the reporting period. Information on the nominating committee processes appears in the Proxy Statement under "Information Regarding the Board of Directors."

### **Item 11. Executive Compensation**

Information on executive compensation appears in the Proxy Statement under "Compensation of Named Executive Officers and Directors," which includes the "Report of the Compensation Committee" and the "Compensation Discussion and Analysis."

## **Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

- a) Information on the security ownership of certain beneficial owners and management appears in the Proxy Statement under "Security Ownership of Principal Shareholders and Management."
- b) Information on securities authorized for issuance under equity compensation plans appears in Part II, Item 5, Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities, Page 27, as securities authorized for issuance under equity compensation plans. Additional information on share-based compensation under our equity compensation plans is available in Item 8, Note 16 of the Consolidated Financial Statements, Page 102.

## **Item 13. Certain Relationships and Related Transactions**

Information about certain relationships and related transactions appears in the Proxy Statement under "Certain Relationships and Transactions" and "Compensation Committee Interlocks and Insider Participation."

## **Item 14. Principal Accountant Fees and Services**

Information about independent registered public accounting firm fees and services and audit committee pre-approval policies and procedures appears in the Proxy Statement under "Audit-related Matters," which includes the "Report of the Audit Committee," "Fees Billed by the Independent Registered Public Accounting Firm" and "Services Provided by the Independent Registered Public Accounting Firm."

# **Part IV**

## **Item 15. Exhibits and Financial Statement Schedules**

- a) Financial Statements – information contained in Part II, Item 8, of this report, Page 83 to Page 87
- b) Exhibits – see Index of Exhibits, Page 120
- c) Financial Statement Schedules
  - Schedule I – Summary of Investments – Other than Investments in Related Parties, Page 109
  - Schedule II – Condensed Financial Statements of Registrant, Page 111
  - Schedule III – Supplementary Insurance Information, Page 114
  - Schedule IV – Reinsurance, Page 116
  - Schedule V – Valuation and Qualifying Accounts, Page 117
  - Schedule VI – Supplementary Information Concerning Property Casualty Insurance Operations, Page 118

# SCHEDULE I

## Cincinnati Financial Corporation and Subsidiaries Summary of Investments - Other than Investments in Related Parties

(In millions)	At December 31, 2007		
Type of investment	Cost or amortized	Fair value	Balance sheet
Fixed maturities:			
United States government:			
The Cincinnati Insurance Company	\$ 1	\$ 1	\$ 1
The Cincinnati Life Insurance Company	3	4	3
Total	<u>4</u>	<u>5</u>	<u>4</u>
Government-sponsored enterprises:			
The Cincinnati Insurance Company	547	548	548
The Cincinnati Casualty Company	4	4	4
The Cincinnati Indemnity Company	2	2	2
The Cincinnati Life Insurance Company	341	341	342
Total	<u>894</u>	<u>895</u>	<u>896</u>
Foreign government:			
The Cincinnati Insurance Company	3	3	3
Total	<u>3</u>	<u>3</u>	<u>3</u>
States, municipalities and political subdivisions:			
The Cincinnati Insurance Company	2,318	2,360	2,360
The Cincinnati Casualty Company	138	141	141
The Cincinnati Indemnity Company	33	33	33
The Cincinnati Specialty Underwriters Insurance Company	23	24	24
The Cincinnati Life Insurance Company	6	6	6
Total	<u>2,518</u>	<u>2,564</u>	<u>2,564</u>
Public utilities:			
The Cincinnati Insurance Company	63	65	65
The Cincinnati Casualty Company	4	4	4
The Cincinnati Indemnity Company	1	1	1
The Cincinnati Specialty Underwriters Insurance Company	2	2	2
The Cincinnati Life Insurance Company	91	93	93
Cincinnati Financial Corporation	2	2	2
Total	<u>163</u>	<u>167</u>	<u>167</u>
Convertibles and bonds with warrants attached:			
The Cincinnati Insurance Company	139	141	141
The Cincinnati Life Insurance Company	90	76	76
Cincinnati Financial Corporation	9	9	9
Total	<u>238</u>	<u>226</u>	<u>226</u>
All other corporate bonds:			
The Cincinnati Insurance Company	893	900	900
The Cincinnati Casualty Company	23	24	24
The Cincinnati Indemnity Company	8	9	9
The Cincinnati Specialty Underwriters Insurance Company	32	32	32
The Cincinnati Life Insurance Company	929	945	945
Cincinnati Financial Corporation	78	78	78
Total	<u>1,963</u>	<u>1,988</u>	<u>1,988</u>
Total fixed maturities	<u>\$ 5,783</u>	<u>\$ 5,848</u>	<u>\$ 5,848</u>

# SCHEDULE I (CONTINUED)

## Cincinnati Financial Corporation and Subsidiaries Summary of Investments - Other than Investments in Related Parties

(In millions)	At December 31, 2007		
Type of investment	Cost or amortized	Fair value	Balance sheet
Equity securities:			
Common stocks:			
Public utilities:			
The Cincinnati Insurance Company	\$ 84	\$ 144	\$ 144
The Cincinnati Casualty Company	2	7	7
The Cincinnati Life Insurance Company	11	28	28
CinFin Capital Management Company	1	1	1
Cincinnati Financial Corporation	55	110	110
Total	<u>153</u>	<u>290</u>	<u>290</u>
Banks, trust and insurance companies:			
The Cincinnati Insurance Company	620	1,649	1,649
The Cincinnati Casualty Company	16	53	53
The Cincinnati Specialty Underwriters Insurance Company	15	42	42
The Cincinnati Life Insurance Company	57	119	119
CinFin Capital Management Company	1	2	2
Cincinnati Financial Corporation	515	1,178	1,178
Total	<u>1,224</u>	<u>3,043</u>	<u>3,043</u>
Industrial, miscellaneous and all other:			
The Cincinnati Insurance Company	683	1,695	1,695
The Cincinnati Casualty Company	17	71	71
The Cincinnati Indemnity Company	7	21	21
The Cincinnati Specialty Underwriters Insurance Company	19	21	21
The Cincinnati Life Insurance Company	124	210	210
CinFin Capital Management Company	5	5	5
Cincinnati Financial Corporation	483	664	664
Total	<u>1,338</u>	<u>2,687</u>	<u>2,687</u>
Nonredeemable preferred stocks:			
The Cincinnati Insurance Company	235	207	207
The Cincinnati Life Insurance Company	16	13	13
Cincinnati Financial Corporation	9	9	9
Total	<u>260</u>	<u>229</u>	<u>229</u>
Total equity securities	<u>\$ 2,975</u>	<u>\$ 6,249</u>	<u>\$ 6,249</u>
Short-term investments:			
The Cincinnati Insurance Company	\$ 50	\$ 50	\$ 50
The Cincinnati Life Insurance Company	51	51	51
Total short-term investments	<u>\$ 101</u>	<u>\$ 101</u>	<u>\$ 101</u>
Other invested assets:			
Policy loans:			
The Cincinnati Life Insurance Company	\$ 32	—	\$ 32
Limited partnerships:			
Cincinnati Financial Corporation	31	—	31
Total other invested assets	<u>\$ 63</u>	<u>—</u>	<u>\$ 63</u>
Total investments	<u>\$ 8,922</u>	<u>—</u>	<u>\$ 12,261</u>

# SCHEDULE II

## Cincinnati Financial Corporation (parent company only) Condensed Balance Sheets

(In millions)	At December 31,	
	2007	2006
<b>ASSETS</b>		
Investments		
Fixed maturities, at fair value	\$ 88	\$ 128
Equity securities, at fair value	1,961	2,484
Other invested assets	31	25
Cash and cash equivalents	16	38
Securities lending collateral invested	9	0
Equity in net assets of subsidiaries	4,831	5,303
Investment income receivable	18	16
Land, building and equipment, net, for company use (accumulated depreciation: 2007—\$67; 2006—\$64)	169	121
Prepaid federal income tax	5	0
Other assets	14	19
Due from subsidiaries	66	150
Total assets	<u>\$ 7,208</u>	<u>\$ 8,284</u>
<b>LIABILITIES</b>		
Dividends declared but unpaid	\$ 59	\$ 58
Securities lending payable	9	0
Deferred federal income tax	296	526
6.92% senior debentures due 2028	392	392
6.9% senior debentures due 2028	28	28
6.125% senior notes due 2034	371	371
Other liabilities	124	101
Total liabilities	<u>1,279</u>	<u>1,476</u>
<b>SHAREHOLDERS' EQUITY</b>		
Common stock	393	391
Paid-in capital	1,049	1,015
Retained earnings	3,404	2,786
Accumulated other comprehensive income	2,151	3,379
Treasury stock at cost	(1,068)	(763)
Total shareholders' equity	<u>5,929</u>	<u>6,808</u>
Total liabilities and shareholders' equity	<u>\$ 7,208</u>	<u>\$ 8,284</u>

This condensed financial information should be read in conjunction with the Consolidated Financial Statements and Notes included in Part II, Item 8, Page 80.

## SCHEDULE II (CONTINUED)

### Cincinnati Financial Corporation (parent company only)

#### Condensed Statements of Income

(In millions)	Years ended December 31,		
	2007	2006	2005
<b>REVENUES</b>			
Dividends from subsidiaries	\$ 420	\$ 275	\$ 275
Investment income, net of expenses	100	98	89
Realized gains on investments	97	410	2
Other revenue	10	10	10
Total revenues	<u>627</u>	<u>793</u>	<u>376</u>
<b>EXPENSES</b>			
Interest expense	49	51	52
Depreciation expense	3	3	3
Other expenses	15	18	16
Total expenses	<u>67</u>	<u>72</u>	<u>71</u>
INCOME BEFORE INCOME TAXES AND EARNINGS OF SUBSIDIARIES	<u>560</u>	<u>721</u>	<u>305</u>
<b>PROVISION (BENEFIT) FOR INCOME TAXES</b>			
Current	34	153	(27)
Deferred	(2)	(11)	20
Total provision for income taxes	<u>32</u>	<u>142</u>	<u>(7)</u>
NET INCOME BEFORE EARNINGS OF SUBSIDIARIES	<u>528</u>	<u>579</u>	<u>312</u>
Increase in undistributed earnings of subsidiaries	<u>327</u>	<u>351</u>	<u>290</u>
NET INCOME	<u>\$ 855</u>	<u>\$ 930</u>	<u>\$ 602</u>

This condensed financial information should be read in conjunction with the Consolidated Financial Statements and Notes included in Part II, Item 8, Page 80.



# SCHEDULE II (CONTINUED)

## Cincinnati Financial Corporation (parent company only) Condensed Statements of Cash Flows

(In millions)	Years ended December 31,		
	2007	2006	2005
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net income	\$ 855	\$ 930	\$ 602
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	2	1	3
Realized (gains) on investments	(97)	(410)	(2)
Changes in:			
Investment income receivable	(2)	1	0
Current federal income taxes	(21)	48	(12)
Deferred income taxes	(2)	(11)	19
Other assets	0	2	(3)
Other liabilities	12	16	0
Undistributed earnings of subsidiaries	(327)	(351)	(290)
Net cash provided by operating activities	<u>420</u>	<u>226</u>	<u>317</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Sale of fixed-maturities	9	4	8
Call or maturity of fixed-maturities	37	36	2
Sale of equity securities	186	511	18
Purchase of fixed-maturities	(1)	(42)	(9)
Purchase of equity securities	(231)	(351)	(12)
Change in short-term investments, net	0	3	21
Investment in buildings and equipment, net	(49)	(26)	(24)
Change in other invested assets, net	(6)	(8)	(8)
Change in securities lending collateral, net	(9)	0	0
Net cash (used in) provided by investing activities	<u>(64)</u>	<u>127</u>	<u>(4)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Increase in notes payable	20	0	0
Payment of cash dividends to shareholders	(240)	(228)	(204)
Purchase/issuance of treasury shares	(307)	(119)	(61)
Proceeds from stock options exercised	20	30	11
Net transfers to subsidiaries	120	(5)	(80)
Change in securities lending payable, net	9	0	0
Net cash used in financing activities	<u>(378)</u>	<u>(322)</u>	<u>(334)</u>
Net increase (decrease) in cash and cash equivalents	(22)	31	(21)
Cash and cash equivalents at beginning of year	38	7	28
Cash and cash equivalents at end of year	<u>\$ 16</u>	<u>\$ 38</u>	<u>\$ 7</u>

This condensed financial information should be read in conjunction with the Consolidated Financial Statements and Notes included in Part II, Item 8, Page 80.

# SCHEDULE III

## Cincinnati Financial Corporation and Subsidiaries Supplementary Insurance Information

(In millions)	Years ended December 31,		
	2007	2006	2005
<b>Deferred policy acquisition costs:</b>			
Commercial lines insurance	\$ 234	\$ 235	\$ 226
Personal lines insurance	<u>78</u>	<u>80</u>	<u>85</u>
Total property casualty insurance	<u>312</u>	<u>315</u>	<u>311</u>
Life insurance	<u>149</u>	<u>138</u>	<u>118</u>
Total	<u>\$ 461</u>	<u>\$ 453</u>	<u>\$ 429</u>
<b>Future policy benefits, losses, claims and expense losses:</b>			
Commercial lines insurance	\$ 3,533	\$ 3,414	\$ 3,173
Personal lines insurance	<u>392</u>	<u>446</u>	<u>456</u>
Total property casualty insurance	<u>3,925</u>	<u>3,860</u>	<u>3,629</u>
Life insurance	<u>1,505</u>	<u>1,430</u>	<u>1,362</u>
Total (1)	<u>\$ 5,430</u>	<u>\$ 5,290</u>	<u>\$ 4,991</u>
<b>Unearned premiums:</b>			
Commercial lines insurance	\$ 1,191	\$ 1,195	\$ 1,150
Personal lines insurance	<u>371</u>	<u>382</u>	<u>407</u>
Total property casualty insurance	<u>1,562</u>	<u>1,577</u>	<u>1,557</u>
Life insurance	<u>2</u>	<u>2</u>	<u>2</u>
Total (1)	<u>\$ 1,564</u>	<u>\$ 1,579</u>	<u>\$ 1,559</u>
<b>Other policy claims and benefits payable:</b>			
Commercial lines insurance	\$ 0	\$ 0	\$ 0
Personal lines insurance	<u>0</u>	<u>0</u>	<u>0</u>
Total property casualty insurance	<u>0</u>	<u>0</u>	<u>0</u>
Life insurance	<u>15</u>	<u>15</u>	<u>13</u>
Total (1)	<u>\$ 15</u>	<u>\$ 15</u>	<u>\$ 13</u>
<b>Premium revenues:</b>			
Commercial lines insurance	\$ 2,411	\$ 2,402	\$ 2,254
Personal lines insurance	<u>714</u>	<u>762</u>	<u>804</u>
Total property casualty insurance	<u>3,125</u>	<u>3,164</u>	<u>3,058</u>
Life insurance	<u>125</u>	<u>115</u>	<u>106</u>
Consolidated eliminations	<u>0</u>	<u>(1)</u>	<u>0</u>
Total	<u>\$ 3,250</u>	<u>\$ 3,278</u>	<u>\$ 3,164</u>

# SCHEDULE III (CONTINUED)

## Cincinnati Financial Corporation and Subsidiaries Supplementary Insurance Information

(In millions)	Years ended December 31,		
	2007	2006	2005
<b>Investment income, net of expenses:</b>			
Commercial lines insurance	\$ 0	\$ 0	\$ 0
Personal lines insurance	<u>0</u>	<u>0</u>	<u>0</u>
Total property casualty insurance (3)	<u>393</u>	<u>367</u>	<u>338</u>
Life insurance	<u>114</u>	<u>108</u>	<u>99</u>
Total	<u>\$ 507</u>	<u>\$ 475</u>	<u>\$ 437</u>
<b>Benefits, claims losses and settlement expenses:</b>			
Commercial lines insurance	\$ 1,395	\$ 1,466	\$ 1,298
Personal lines insurance	<u>437</u>	<u>542</u>	<u>514</u>
Total property casualty insurance	<u>1,832</u>	<u>2,008</u>	<u>1,812</u>
Life insurance	<u>133</u>	<u>122</u>	<u>102</u>
Total	<u>\$ 1,965</u>	<u>\$ 2,130</u>	<u>\$ 1,914</u>
<b>Amortization of deferred policy acquisition costs:</b>			
Commercial lines insurance	\$ 477	\$ 504	\$ 473
Personal lines insurance	<u>150</u>	<u>160</u>	<u>168</u>
Total property casualty insurance	<u>627</u>	<u>664</u>	<u>641</u>
Life insurance	<u>30</u>	<u>21</u>	<u>23</u>
Total (2)	<u>\$ 657</u>	<u>\$ 685</u>	<u>\$ 664</u>
<b>Other operating expenses:</b>			
Commercial lines insurance	\$ 248	\$ 224	\$ 198
Personal lines insurance	<u>83</u>	<u>87</u>	<u>77</u>
Total property casualty insurance	<u>331</u>	<u>311</u>	<u>275</u>
Life insurance	<u>22</u>	<u>30</u>	<u>29</u>
Total (2)	<u>\$ 353</u>	<u>\$ 341</u>	<u>\$ 304</u>
<b>Written premiums:</b>			
Commercial lines insurance	\$ 2,413	\$ 2,442	\$ 2,290
Personal lines insurance	<u>704</u>	<u>736</u>	<u>786</u>
Total property casualty insurance	<u>3,117</u>	<u>3,178</u>	<u>3,076</u>
Accident health insurance	<u>3</u>	<u>3</u>	<u>3</u>
Consolidated eliminations	<u>0</u>	<u>(1)</u>	<u>0</u>
Total	<u>\$ 3,120</u>	<u>\$ 3,180</u>	<u>\$ 3,079</u>

### Notes to Schedule III:

(1) The sum of future policy benefits, losses, claims and expense losses, unearned premium and other policy claims and other policy claims and benefits payable is equal to the sum of loss and loss expense, life policy reserves and unearned premiums reported in the company's consolidated balance sheets.

(2) The sum of amortization of deferred policy acquisition costs and other operating expenses is equal to the sum of Commissions; Other operating expenses; Taxes, licenses and fees; and Increase in deferred acquisition costs expenses shown in the consolidated statements of income, less other expenses not applicable to the above insurance segments.

(3) This segment information is not regularly allocated to segments and reviewed by company management in making decisions about resources to be allocated to the segments or to assess their performance.

# SCHEDULE IV

## Cincinnati Financial Corporation and Subsidiaries Reinsurance

(Dollars in millions)	Years ended December 31,		
	2007	2006	2005
<b>Gross amounts:</b>			
Life insurance in force	\$ <u>61,873</u>	\$ <u>56,968</u>	\$ <u>51,488</u>
Earned premiums			
Commercial lines insurance	\$ <u>2,536</u>	\$ <u>2,513</u>	\$ <u>2,386</u>
Personal lines insurance	<u>742</u>	<u>783</u>	<u>823</u>
Total property casualty insurance	<u>3,278</u>	<u>3,296</u>	<u>3,209</u>
Life insurance	<u>178</u>	<u>159</u>	<u>150</u>
Consolidated eliminations	<u>0</u>	<u>(1)</u>	<u>0</u>
Total	\$ <u>3,456</u>	\$ <u>3,454</u>	\$ <u>3,359</u>
<b>Ceded amounts to other companies:</b>			
Life insurance in force	\$ <u>32,959</u>	\$ <u>31,744</u>	\$ <u>30,705</u>
Earned premiums			
Commercial lines insurance	\$ <u>144</u>	\$ <u>134</u>	\$ <u>157</u>
Personal lines insurance	<u>31</u>	<u>24</u>	<u>22</u>
Total	<u>175</u>	<u>158</u>	<u>179</u>
Life insurance	<u>53</u>	<u>44</u>	<u>44</u>
Total	\$ <u>228</u>	\$ <u>202</u>	\$ <u>223</u>
<b>Assumed amounts from other companies:</b>			
Life insurance in force	\$ <u>2</u>	\$ <u>3</u>	\$ <u>5</u>
Earned premiums			
Commercial lines insurance	\$ <u>20</u>	\$ <u>24</u>	\$ <u>25</u>
Personal lines insurance	<u>2</u>	<u>2</u>	<u>3</u>
Total property casualty insurance	<u>22</u>	<u>26</u>	<u>28</u>
Life insurance	<u>0</u>	<u>0</u>	<u>0</u>
Total	\$ <u>22</u>	\$ <u>26</u>	\$ <u>28</u>
<b>Net amounts:</b>			
Life insurance in force	\$ <u>28,916</u>	\$ <u>25,227</u>	\$ <u>20,788</u>
Earned premiums			
Commercial lines insurance	\$ <u>2,411</u>	\$ <u>2,402</u>	\$ <u>2,254</u>
Personal lines insurance	<u>714</u>	<u>762</u>	<u>804</u>
Total property casualty insurance	<u>3,125</u>	<u>3,164</u>	<u>3,058</u>
Life insurance	<u>125</u>	<u>115</u>	<u>106</u>
Consolidated eliminations	<u>0</u>	<u>(1)</u>	<u>0</u>
Total	\$ <u>3,250</u>	\$ <u>3,278</u>	\$ <u>3,164</u>
<b>Percentage of amounts assumed to net:</b>			
Life insurance in force	0.0 %	0.0 %	0.0 %
Earned premiums			
Commercial lines insurance	0.8 %	1.1 %	1.1 %
Personal lines insurance	0.3	0.4	0.4
Total property casualty insurance	0.7	0.9	0.9
Life insurance	0.0	0.0	0.0
Total	0.7	0.9	0.9

# SCHEDULE V

## Cincinnati Financial Corporation and Subsidiaries Valuation and Qualifying Accounts

(In millions)	At December 31,		
	2007	2006	2005
Allowance for doubtful receivables:			
Balance at beginning of period	\$ 3	\$ 3	\$ 3
Additions charged to costs and expenses	3	3	6
Other additions	0	0	0
Deductions	(2)	(3)	(6)
Balance at end of period	<u>\$ 4</u>	<u>\$ 3</u>	<u>\$ 3</u>

# SCHEDULE VI

## Cincinnati Financial Corporation and Subsidiaries Supplementary Information Concerning Property Casualty Insurance Operations

(In millions)	Years ended December 31,		
	2007	2006	2005
Deferred policy acquisition costs:			
Commercial lines insurance	\$ 234	\$ 235	\$ 226
Personal lines insurance	78	80	85
Total	<u>\$ 312</u>	<u>\$ 315</u>	<u>\$ 311</u>
Reserves for unpaid claims and claim adjustment expenses:			
Commercial lines insurance	\$ 3,533	\$ 3,414	\$ 3,173
Personal lines insurance	392	446	456
Total	<u>\$ 3,925</u>	<u>\$ 3,860</u>	<u>\$ 3,629</u>
Reserve discount deducted	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
Unearned premiums:			
Commercial lines insurance	\$ 1,191	\$ 1,195	\$ 1,150
Personal lines insurance	371	382	407
Total	<u>\$ 1,562</u>	<u>\$ 1,577</u>	<u>\$ 1,557</u>
Earned premiums:			
Commercial lines insurance	\$ 2,411	\$ 2,402	\$ 2,254
Personal lines insurance	714	762	804
Total	<u>\$ 3,125</u>	<u>\$ 3,164</u>	<u>\$ 3,058</u>
Investment income:			
Commercial lines insurance (1)	\$ 0	\$ 0	\$ 0
Personal lines insurance (1)	0	0	0
Total	<u>\$ 393</u>	<u>\$ 367</u>	<u>\$ 338</u>
Loss and loss expenses incurred related to current accident year:			
Commercial lines insurance	\$ 1,598	\$ 1,564	\$ 1,424
Personal lines insurance	478	560	548
Total	<u>\$ 2,076</u>	<u>\$ 2,124</u>	<u>\$ 1,972</u>
Loss and loss expenses incurred related to prior accident years:			
Commercial lines insurance	\$ (204)	\$ (98)	\$ (126)
Personal lines insurance	(40)	(18)	(34)
Total	<u>\$ (244)</u>	<u>\$ (116)</u>	<u>\$ (160)</u>
Amortization of deferred policy acquisition costs:			
Commercial lines insurance	\$ 477	\$ 504	\$ 473
Personal lines insurance	150	160	168
Total	<u>\$ 627</u>	<u>\$ 664</u>	<u>\$ 641</u>
Paid loss and loss expenses:			
Commercial lines insurance	\$ 1,299	\$ 1,218	\$ 1,126
Personal lines insurance	492	545	552
Total	<u>\$ 1,791</u>	<u>\$ 1,763</u>	<u>\$ 1,678</u>
Written premiums:			
Commercial lines insurance	\$ 2,413	\$ 2,442	\$ 2,290
Personal lines insurance	704	736	786
Total	<u>\$ 3,117</u>	<u>\$ 3,178</u>	<u>\$ 3,076</u>

### Note to Schedule VI:

(1) This segment information is not regularly allocated to segments and not reviewed by company management in making decisions about resources to be allocated to the segments or to assess their performance.

## SIGNATURES

Pursuant to the requirements of Section 13 or 15 (d) 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

/S/ Kenneth W. Stecher

By: Kenneth W. Stecher  
 Title: Chief Financial Officer, Executive Vice President, Secretary and Treasurer  
 Date: February 29, 2008

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been duly signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/S/ John J. Schiff, Jr.	Chairman, Chief Executive Officer and Director	February 29, 2008
John J. Schiff, Jr.		
/S/ Kenneth W. Stecher	Chief Financial Officer, Executive Vice President, Secretary and Treasurer (Principal Accounting Officer)	February 29, 2008
Kenneth W. Stecher		
/S/ William F. Bahl	Director	February 29, 2008
William F. Bahl		
/S/ James E. Benoski	Vice Chairman, President, Chief Operating Officer, Chief Insurance Officer and Director	February 29, 2008
James E. Benoski		
/S/ Gregory T. Bier	Director	February 29, 2008
Gregory T. Bier		
/S/ Dirk J. Debbink	Director	February 29, 2008
Dirk J. Debbink		
/S/ Kenneth C. Lichtendahl	Director	February 29, 2008
Kenneth C. Lichtendahl		
/S/ W. Rodney McMullen	Director	February 29, 2008
W. Rodney McMullen		
/S/ Gretchen W. Price	Director	February 29, 2008
Gretchen W. Price		
/S/ Thomas R. Schiff	Director	February 29, 2008
Thomas R. Schiff		
/S/ Douglas S. Skidmore	Director	February 29, 2008
Douglas S. Skidmore		
/S/ John F. Steele, Jr.	Director	February 29, 2008
John F. Steele, Jr.		
/S/ Larry R. Webb	Director	February 29, 2008
Larry R. Webb		
/S/ E. Anthony Woods	Director	February 29, 2008
E. Anthony Woods		

## INDEX OF EXHIBITS

Exhibit No.	Exhibit Description
3.1A	Amended Articles of Incorporation of Cincinnati Financial Corporation <sup>(1)</sup>
3.1B	Amendment to Article Fourth of Amended Articles of Incorporation of Cincinnati Financial Corporation <sup>(2)</sup>
3.2	Regulations of Cincinnati Financial Corporation <sup>(3)</sup>
4.1	Indenture with The Bank of New York Trust Company <sup>(4)</sup>
4.2	Supplemental Indenture with The Bank of New York Trust Company <sup>(4)</sup>
4.3	Second Supplemental Indenture with The Bank of New York Trust Company <sup>(5)</sup>
4.4	Form of 6.125% Exchange Note Due 2034 (included in Exhibit 4.2)
4.5	Form of 6.92% Debentures Due 2028 (included in Exhibit 4.3)
4.6	Indenture with the First National Bank of Chicago (subsequently assigned to The Bank of New York Trust Company) <sup>(6)</sup>
4.7	Form of 6.90% Debentures Due 2028 (included in Exhibit 4.6)
10.1	Agreement with Messer Construction <sup>(7)</sup>
10.2	2003 Non-Employee Directors' Stock Plan <sup>(8)</sup>
10.3	Cincinnati Financial Corporation Stock Option Plan No. VI <sup>(9)</sup>
10.4	Cincinnati Financial Corporation Stock Option Plan No. VII <sup>(10)</sup>
10.5	Standard Form of Nonqualified and Incentive Option Agreements for Stock Option Plan No. VI <sup>(7)</sup>
10.6	Cincinnati Financial Corporation Incentive Compensation Plan <sup>(11)</sup>
10.7	Cincinnati Financial Corporation 2006 Stock Compensation Plan <sup>(11)</sup>
10.8	Standard Form of Combined Incentive/Nonqualified Stock Option for Stock Option Plan VI <sup>(12)</sup>
10.9	364-Day Credit Agreement by and among Cincinnati Financial Corporation and CFC Investment Company, as Borrowers, and Fifth Third Bank, as Lender <sup>(13)</sup>
10.10	Director and Named Executive Officer Compensation Summary <sup>(11)</sup>
10.11	Executive Compensation Arrangements November 2007 <sup>(14)</sup>
10.12	Executive Compensation Arrangements November 2006 <sup>(15)</sup>
10.13	Amendment No. 1 to Credit Agreement by and among Cincinnati Financial Corporation and CFC investment Company, as Borrower, and Fifth Third Bank, as lender. <sup>(16)</sup>
10.14	Cincinnati Financial Corporation Supplemental Retirement Plan <sup>(17)</sup>
10.15	Standard Form of Incentive Stock Option Agreement for Stock Option Plan VII <sup>(18)</sup>
10.16	Standard Form of Nonqualified Stock Option Agreement for Stock Option Plan VII <sup>(19)</sup>
10.17	Standard Form of Incentive Stock Option Agreement for the 2006 Stock Compensation Plan <sup>(20)</sup>
10.18	Standard Form of Nonqualified Stock Option Agreement for the 2006 Stock Compensation Plan <sup>(21)</sup>
10.19	Restricted Stock Unit Agreement for John J. Schiff, Jr., dated January 31, 2007 <sup>(22)</sup>
10.20	Restricted Stock Unit Agreement for James E. Benoski, dated January 31, 2007 <sup>(23)</sup>
10.21	Restricted Stock Unit Agreement for Jacob F. Scherer, Jr., dated January 31, 2007 <sup>(24)</sup>
10.22	Restricted Stock Unit Agreement for Kenneth W. Stecher, dated January 31, 2007 <sup>(25)</sup>

<sup>(1)</sup> Incorporated by reference to the company's 1999 Annual Report on Form 10-K dated March 23, 2000 (File No. 000-04604).

<sup>(2)</sup> Incorporated by reference to Exhibit 3(i) filed with the company's Current Report on Form 8-K dated July 15, 2005.

<sup>(3)</sup> Incorporated by reference to the company's Definitive Proxy Statement dated March 2, 1992, Exhibit 2 (File No. 000-04604).

<sup>(4)</sup> Incorporated by reference to the company's Current Report on Form 8-K dated November 2, 2004, filed with respect to the issuance of the company's 6.125% Senior Notes due November 1, 2034.

<sup>(5)</sup> Incorporated by reference to the company's Current Report on Form 8-K dated May 9, 2005, filed with respect to the completion of the company's exchange offer and rescission offer for its 6.90% senior debentures due 2028.

<sup>(6)</sup> Incorporated by reference to the company's registration statement on Form S-3 effective May 22, 1998 (File No. 333-51677).

<sup>(7)</sup> Incorporated by reference to the company's 2004 Annual Report on Form 10-K dated March 11, 2005.

<sup>(8)</sup> Incorporated by reference to the company's Definitive Proxy Statement dated March 21, 2005. (File No. 000-04604)

<sup>(9)</sup> Incorporated by reference to the company's Definitive Proxy Statement dated March 1, 1999 (File No. 000-04604).

<sup>(10)</sup> Incorporated by reference to the company's Definitive Proxy Statement dated March 8, 2002 (File No. 000-04604).

<sup>(11)</sup> Incorporated by reference to the company's Definitive Proxy Statement dated March 30, 2007 (File No. 000-04604).

<sup>(12)</sup> Incorporated by reference to Exhibit 10.3 filed with the company's Current Report on Form 8-K dated July 15, 2005.

<sup>(13)</sup> Incorporated by reference to Exhibit 10.1 filed with the company's Current Report on Form 8-K dated May 31, 2005.

<sup>(14)</sup> Incorporated by reference to Item 5.02 of the company's Current Report on Form 8-K dated November 14, 2007.

<sup>(15)</sup> Incorporated by reference to Item 5.02 of the company's Current Report on Form 8-K dated November 24, 2006.

<sup>(16)</sup> Incorporated by reference to Exhibit 10.01 filed with the company's Current Report on Form 8-K dated May 26, 2006.



Exhibit No.	Exhibit Description
10.23	Restricted Stock Unit Agreement for Thomas A. Joseph, dated January 31, 2007 <sup>(26)</sup>
10.24	Form of Restricted Stock Unit Agreement for use under the Cincinnati Financial Corporation 2006 Stock Purchase Incentive Plan (service-based) <sup>(27)</sup>
10.25	Form of Restricted Stock Unit Agreement for use under the Cincinnati Financial Corporation 2006 Stock Purchase Incentive Plan (performance-based) <sup>(28)</sup>
10.26	Form of Incentive Compensation Agreement for use under the Cincinnati Financial Corporation 2006 Incentive Compensation Plan (performance-based) <sup>(29)</sup>
10.27	Credit Agreement by and among Cincinnati Financial Corporation, CFC Investment Company, The Huntington National Bank and LaSalle Bank National Association, among others, dated July 2, 2007 <sup>(30)</sup>
10.28	Second Amended and Restated Discretionary Line of Credit Note with PNC Bank, National Association dated July 12, 2007 <sup>(31)</sup>
10.29	Secondary Block Trade Agreement between The Cincinnati Insurance Company and UBS Securities LLC, dated October 23, 2007 <sup>(32)</sup>
10.30	Purchase Agreement (Tranche 1 of 4) between Cincinnati Financial Corporation and UBS AG, London Branch, acting through UBS Securities LLC as agent, dated October 24, 2007 <sup>(33)</sup>
10.31	Purchase Agreement (Tranche 2 of 4) between Cincinnati Financial Corporation and UBS AG, London Branch, acting through UBS Securities LLC as agent, dated October 24, 2007 <sup>(34)</sup>
10.32	Purchase Agreement (Tranche 3 of 4) between Cincinnati Financial Corporation and UBS AG, London Branch, acting through UBS Securities LLC as agent, dated October 24, 2007 <sup>(35)</sup>
10.33	Purchase Agreement (Tranche 4 of 4) between Cincinnati Financial Corporation and UBS AG, London Branch, acting through UBS Securities LLC as agent, dated October 24, 2007 <sup>(36)</sup>
10.34	Stock Purchase Agreement between Cincinnati Financial Corporation and the E. Perry Webb Marital Trust, dated September 5, 2007 <sup>(37)</sup>

- <sup>(17)</sup> Incorporated by reference to Exhibit 10.17 filed with the company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2006.
- <sup>(18)</sup> Incorporated by reference to Exhibit 10.1 filed with the company's Current Report on Form 8-K dated October 20, 2006.
- <sup>(19)</sup> Incorporated by reference to Exhibit 10.2 filed with the company's Current Report on Form 8-K dated October 20, 2006.
- <sup>(20)</sup> Incorporated by reference to Exhibit 10.3 filed with the company's Current Report on Form 8-K dated October 20, 2006.
- <sup>(21)</sup> Incorporated by reference to Exhibit 10.4 filed with the company's Current Report on Form 8-K dated October 20, 2006.
- <sup>(22)</sup> Incorporated by reference to Exhibit 10.1 filed with the company's Current Report on Form 8-K dated January 31, 2007.
- <sup>(23)</sup> Incorporated by reference to Exhibit 10.2 filed with the company's Current Report on Form 8-K dated January 31, 2007.
- <sup>(24)</sup> Incorporated by reference to Exhibit 10.3 filed with the company's Current Report on Form 8-K dated January 31, 2007.
- <sup>(25)</sup> Incorporated by reference to Exhibit 10.4 filed with the company's Current Report on Form 8-K dated January 31, 2007.
- <sup>(26)</sup> Incorporated by reference to Exhibit 10.5 filed with the company's Current Report on Form 8-K dated January 31, 2007.
- <sup>(27)</sup> Incorporated by reference to Exhibit 10.6 filed with the company's Current Report on Form 8-K dated January 31, 2007, as amended.
- <sup>(28)</sup> Incorporated by reference to Exhibit 10.1 filed with the company's Current Report on Form 8-K dated November 14, 2007.
- <sup>(29)</sup> Incorporated by reference to Exhibit 10.1 filed with the company's Current Report on Form 8-K dated March 19, 2007.
- <sup>(30)</sup> Incorporated by reference to Exhibit 10.01 filed with the company's Current Report on Form 8-K dated June 30, 2007.
- <sup>(31)</sup> Incorporated by reference to Exhibit 10.27 filed with the company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2007.
- <sup>(32)</sup> Incorporated by reference to Exhibit 10.29 filed with the company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2007.
- <sup>(33)</sup> Incorporated by reference to Exhibit 10.30 filed with the company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2007.
- <sup>(34)</sup> Incorporated by reference to Exhibit 10.31 filed with the company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2007.
- <sup>(35)</sup> Incorporated by reference to Exhibit 10.32 filed with the company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2007.
- <sup>(36)</sup> Incorporated by reference to Exhibit 10.33 filed with the company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2007.
- <sup>(37)</sup> Incorporated by reference to Exhibit 10.34 filed with the company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2007.

Exhibit No.	Exhibit Description
10.35	Restricted Stock Unit Agreement for John J. Schiff, Jr. dated February 18, 2008 <sup>(38)</sup>
10.36	Restricted Stock Unit Agreement for James E. Benoski dated February 18, 2008 <sup>(39)</sup>
10.37	Restricted Stock Unit Agreement for Jacob F. Scherer, Jr. dated February 18, 2008 <sup>(40)</sup>
10.38	Restricted Stock Unit Agreement for Kenneth W. Stecher dated February 18, 2008 <sup>(41)</sup>
10.39	Restricted Stock Unit Agreement for Thomas A. Joseph dated February 18, 2008 <sup>(42)</sup>
10.40	Standard Form of Performance-based Restricted Stock Unit Agreement <sup>(43)</sup>
11	Statement re: Computation of per share earnings for the years ended December 31, 2007, 2006 and 2005, contained in Note 11 of the Consolidated Financial Statements included in Part II, Item 8 of this report, Page 99
14	Cincinnati Financial Corporation Code of Ethics for Senior Financial Officers <sup>(44)</sup>
21	Cincinnati Financial Corporation Subsidiaries contained in Part I, Item 1, Page 1
23	Consent of Independent Registered Public Accounting Firm, Page 123
31A	Certification pursuant to Section 302 of the Sarbanes Oxley Act of 2002 – Chief Executive Officer, Page 124
31B	Certification pursuant to Section 302 of the Sarbanes Oxley Act of 2002 – Chief Financial Officer, Page 125
32	Certification pursuant to Section 906 of the Sarbanes Oxley Act of 2002, Page 126

<sup>(38)</sup> Incorporated by reference to Exhibit 10.1 filed with the company's Current Report on Form 8-K dated February 20, 2008.

<sup>(39)</sup> Incorporated by reference to Exhibit 10.2 filed with the company's Current Report on Form 8-K dated February 20, 2008.

<sup>(40)</sup> Incorporated by reference to Exhibit 10.3 filed with the company's Current Report on Form 8-K dated February 20, 2008.

<sup>(41)</sup> Incorporated by reference to Exhibit 10.4 filed with the company's Current Report on Form 8-K dated February 20, 2008.

<sup>(42)</sup> Incorporated by reference to Exhibit 10.5 filed with the company's Current Report on Form 8-K dated February 20, 2008.

<sup>(43)</sup> Incorporated by reference to Exhibit 10.6 filed with the company's Current Report on Form 8-K dated February 20, 2008.

<sup>(44)</sup> Incorporated by reference to the company's Definitive Proxy Statement dated March 18, 2004 (File No. 000-04604).

## EXHIBIT 23

### CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in Registration Statement No. 333-85953 (on Form S-8), No. 333-24815 (on Form S-8), No. 333-24817 (on Form S-8), No. 333-49981 (on Form S-8), No. 333-103509 (on Form S-8), No. 333-103511 (on Form S-8), No. 333-121429 (on Form S-4), No. 333-123471 (on Form S-4), and No. 333-126714 (on Form S-8), as amended, of Cincinnati Financial Corporation of our report dated February 29, 2008, relating to the consolidated financial statements and financial statement schedules of Cincinnati Financial Corporation and subsidiaries and the effectiveness of internal control over financial reporting (which report expresses an unqualified opinion and includes an explanatory paragraph relating to the company's adoption of Statement of Financial Accounting Standards (SFAS) No. 123(R), Share Based Payment, on January 1, 2006; the recognition and related disclosure provisions of SFAS No. 158, Employers' Accounting for Defined Benefit Pension Plans and Other Postretirement Benefit Plans, on December 31, 2006; the provisions of SFAS No. 155, Accounting for Certain Hybrid Financial Instruments, an amendment of SFAS No. 133 and 140, on January 1, 2007; and the provisions of Financial Interpretation No. 48, Accounting for Uncertainty in Income Taxes, an Interpretation of SFAS No. 109, on January 1, 2007) appearing in this Annual Report on Form 10-K of Cincinnati Financial Corporation for the year ended December 31, 2007.

/S/ Deloitte & Touche LLP

Cincinnati, Ohio  
February 28, 2008

# EXHIBIT 31A

## Certification pursuant to Section 302 of the Sarbanes Oxley Act of 2002

I, John J. Schiff, Jr., certify that:

1. I have reviewed this Annual Report on Form 10-K of Cincinnati Financial Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principals;
  - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 29, 2008

/S/ John J. Schiff, Jr.

John J. Schiff, Jr., CPCU  
Chairman and Chief Executive Officer

# EXHIBIT 31B

## Certification pursuant to Section 302 of the Sarbanes Oxley Act of 2002

I, Kenneth W. Stecher, certify that:

1. I have reviewed this Annual Report on Form 10-K of Cincinnati Financial Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principals;
  - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
  - a) all significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 29, 2008

/S/ Kenneth W. Stecher

Kenneth W. Stecher  
Chief Financial Officer, Executive Vice President, Secretary and Treasurer  
(Principal Accounting Officer)

## EXHIBIT 32

### Certification pursuant to Section 906 of the Sarbanes Oxley Act of 2002

The certification set forth below is being submitted in connection with this report on Form 10-K for the purpose of complying with Rule 13a-14(b) or Rule 15d-14(b) of the Securities Exchange Act of 1934 and Section 1350 of Chapter 63 of Title 18 of the United States Code.

John J. Schiff, Jr., the chief executive officer, and Kenneth W. Stecher, the chief financial officer, of Cincinnati Financial Corporation each certifies that, to the best of his knowledge:

1. the report fully complies with the requirements of Section 13(a) or 15(d) of the Exchange Act; and
2. the information contained in the report fairly presents, in all material respects, the financial condition and results of operations of Cincinnati Financial Corporation.

Date: February 29, 2008

/S/ John J. Schiff, Jr.

John J. Schiff, Jr., CPCU  
Chairman and Chief Executive Officer

/S/ Kenneth W. Stecher

Kenneth W. Stecher  
Chief Financial Officer, Executive Vice President, Secretary and Treasurer  
(Principal Accounting Officer)

# Cincinnati Financial Corporation Officers and Directors

(as of February 28, 2008)

## Directors

### William F. Bahl, CFA, CIC

Chairman  
Bahl & Gaynor Investment Counsel Inc.  
Director since 1995 (1)(3)(4)(5\*)

### James E. Benoski

Vice Chairman, President, Chief Operating Officer and Chief Insurance Officer  
Cincinnati Financial Corporation  
Director since 2000 (3)(4)

### Gregory T. Bier, CPA (Ret.)

Managing Partner (Ret.), Cincinnati Office  
Deloitte & Touche LLP  
Director since 2006 (1)(4)

### Dirk J. Debbink

Chairman  
MSI General Corporation  
(design/build/construction)  
Director since 2004 (1)(3)

### Kenneth C. Lichtendahl

President and Chief Executive Officer  
Tradewinds Beverage Company  
Director since 1988 (1\*)(2)(5)

### W. Rodney McMullen

Vice Chairman  
The Kroger Co.  
Director since 2001 (2\*)(3)(4)

### Gretchen W. Price

Chief Financial Officer  
philosophy inc.  
Director since 2002 (1)(2)(5)

### John J. Schiff, Jr., CPCU

Chairman and Chief Executive Officer  
Cincinnati Financial Corporation  
Director since 1968 (3\*)(4\*)

### Thomas R. Schiff

Chairman and Chief Executive Officer  
John J. & Thomas R. Schiff & Co. Inc.  
(insurance agency)  
Director since 1975 (4)

### Douglas S. Skidmore

President and Chief Executive Officer  
Skidmore Sales & Distributing Company Inc.  
(food distribution)  
Director since 2004 (1)(5)

### John F. Steele, Jr.

Chairman and Chief Executive Officer  
Hilltop Basic Resources Inc.  
(aggregates/concrete supplier)  
Director since 2005 (1)

### Larry R. Webb, CPCU

President  
Webb Insurance Agency Inc.  
Director since 1979 (3)

### E. Anthony Woods

Chairman and Chief Executive Officer  
SupportSource LLC  
(health care consulting)  
Director since 1998 (2)(3)(4)

- (1) Audit Committee
- (2) Compensation Committee
- (3) Executive Committee
- (4) Investment Committee; also  
Richard M. Burrige, CFA, adviser
- (5) Nominating Committee
- \* Committee Chair



W.F. Bahl



J.E. Benoski



G.T. Bier



Dirk J. Debbink



K.C. Lichtendahl



W.R. McMullen



G.W. Price



J.J. Schiff, Jr.



T.R. Schiff



D.S. Skidmore



J.F. Steele, Jr.



L.R. Webb



E.A. Woods

## Officers

### John J. Schiff, Jr., CPCU

Chairman and Chief Executive Officer

### James E. Benoski

Vice Chairman, President, Chief Operating Officer and Chief Insurance Officer

### Kenneth W. Stecher

Chief Financial Officer, Executive Vice President, Secretary and Treasurer

### Eric N. Mathews, CPCU, AIAF

Vice President, Assistant Secretary and Assistant Treasurer

## Directors Emeriti

Vincent H. Beckman  
Michael Brown  
Robert J. Driehaus  
John E. Field, CPCU  
Jackson H. Randolph  
Lawrence H. Rogers II  
John Sawyer

Robert C. Schiff  
Frank J. Schultheis  
David B. Sharrock  
John M. Shepherd  
Thomas J. Smart  
Alan R. Weiler, CPCU  
William H. Zimmer

# Shareholder Information

Cincinnati Financial Corporation had approximately 12,000 shareholders of record and approximately 46,000 beneficial shareholders as of December 31, 2007. Many of the company's independent agent representatives and most of the 4,087 associates of its subsidiaries own the company's common stock.

## Common Stock Price and Dividend Data

Common shares are traded under the symbol CINF on the NASDAQ Global Select Market.

Quarter:	2007				2006			
	1 <sup>st</sup>	2 <sup>nd</sup>	3 <sup>rd</sup>	4 <sup>th</sup>	1 <sup>st</sup>	2 <sup>nd</sup>	3 <sup>rd</sup>	4 <sup>th</sup>
High	\$ 45.92	\$ 47.62	\$ 44.79	\$ 44.84	\$ 45.56	\$ 47.01	\$ 48.44	\$ 49.07
Low	42.24	42.57	36.91	38.37	42.07	41.43	45.93	44.25
Period-end close	42.40	43.40	43.31	39.54	42.07	47.01	48.12	45.31
Cash dividends declared	0.355	0.355	0.355	0.355	0.335	0.335	0.335	0.335

## Annual Meeting

Shareholders are invited to attend the Annual Meeting of Shareholders of Cincinnati Financial Corporation at 9:30 a.m. on Saturday, May 3, 2008, at the Cincinnati Art Museum in Eden Park, Cincinnati, Ohio. You may listen to an audio webcast of the event by visiting the Investors section of the company's Web site, [www.cinfin.com](http://www.cinfin.com).

## Independent Registered Public Accounting Firm

Deloitte & Touche LLP  
250 East Fifth Street  
Cincinnati, Ohio 45202-5109

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# Contact Information

Communications directed to the company's secretary, Kenneth W. Stecher, chief financial officer and executive vice president, are shared with the appropriate individual(s). Or, you may directly access services:

**Investors:** Investor Relations responds to investor inquiries about Cincinnati Financial Corporation and its performance.

Heather J. Wietzel – Vice President, Investor Relations  
513-870-2768 or [investor\\_inquiries@cinfin.com](mailto:investor_inquiries@cinfin.com)

**Shareholders:** Shareholder Services provides stock transfer services, fulfills requests for shareholder materials and assists registered shareholders who wish to update account information or enroll in shareholder plans.

Jerry L. Litton – Assistant Vice President, Shareholder Services  
513-870-2639 or [shareholder\\_inquiries@cinfin.com](mailto:shareholder_inquiries@cinfin.com)

**Media:** Corporate Communications assists media representatives seeking information or comment from Cincinnati Financial Corporation or its subsidiaries.

Joan O. Shevchik, CPCU, CLU – Senior Vice President, Corporate Communications  
513-603-5323 or [media\\_inquiries@cinfin.com](mailto:media_inquiries@cinfin.com)

## Cincinnati Financial Corporation

The Cincinnati Insurance Company  
The Cincinnati Casualty Company  
The Cincinnati Indemnity Company  
The Cincinnati Specialty Underwriters Insurance Company

The Cincinnati Life Insurance Company  
CSU Producer Resources Inc.  
CFC Investment Company  
CinFin Capital Management Company

### Mailing Address:

P.O. Box 145496  
Cincinnati, Ohio 45250-5496

Phone: 513-870-2000

Fax: 513-870-2066

[www.cinfin.com](http://www.cinfin.com)

### Street Address:

6200 South Gilmore Road  
Fairfield, Ohio 45014-5141





Cincinnati Financial Corporation

# The Cincinnati Experience

February 2008

In 2008, we are offering shareholders the same types of information about our company as in prior years, but on a different schedule. As each item is published, it appears online in an integrated annual report format. Many items will be available to you earlier than you received them in the past, because you no longer have to wait until all sections of our annual report are printed. Items available now are titled in color, and those coming soon are titled in gray.

## About the Company

Cincinnati Financial meets the needs of agencies and policyholders through our insurance group and three complementary subsidiaries:

**The Cincinnati Insurance Company** leads our A++ A.M. Best-rated standard market property casualty insurance group, which includes **The Cincinnati Casualty Company** and **The Cincinnati Indemnity Company**. This group markets a broad range of business, homeowner and auto policies through our select group of local independent insurance agencies in 34 states. These companies support each agency's ability to provide exceptional value and service to the people and businesses in its community. Our local field representatives work out of their homes, customizing products to meet policyholder needs, responding personally and promptly to claims and strengthening relationships.

Two other subsidiaries of The Cincinnati Insurance Company also market insurance products. **The Cincinnati Life Insurance Company**, rated A+ by A.M. Best, markets life insurance policies, disability income policies and annuities. **The Cincinnati Specialty Underwriters Insurance Company**, rated A by A.M. Best, began offering excess and surplus lines insurance products in 2008.

Three subsidiaries of Cincinnati Financial support our insurance operations. **CSU Producer Resources Inc.**, offers insurance brokerage services to our independent agencies to support their access to Cincinnati Specialty Underwriters. **CFC Investment Company** offers commercial leasing and financing services to our agents and their clients. **CinFin Capital Management Company** provides asset management services to institutions, corporations and individuals.

## 2007 Fourth-quarter and Full-year Letter to Shareholders – mid-February 2008

This message from our chairman and our president includes recent news releases about financial results announced February 6 and actions taken by the board of directors at its February 1 meeting. *The Cincinnati Experience*, a profile of our operating philosophy, accompanies this letter.

## The Cincinnati Experience – mid-February 2008

The Cincinnati Insurance Company, Cincinnati Financial Corporation's lead subsidiary, ranks among the top 25 U.S. property casualty insurer groups based on net written premiums. In *The Cincinnati Experience*, you'll read about how our relationship-based approach creates value and loyalty, supporting premium growth.

## 2007 Annual Report on Form 10-K – late-February 2008

The *Annual Report on Form 10-K* is a detailed document published by every publicly traded company as required by the U.S. Securities and Exchange Commission. In our report, we describe your company's operations, its results and trends, along with supporting data, discussions, audited financial statements and accompanying notes.

## 2008 Shareholder Meeting Notice and Proxy Statement – mid-March 2008

This statement informs you of items requiring shareholder action at the 2008 Annual Meeting of Shareholders on May 3, 2008. It identifies board members, detailing director and executive officer compensation and board activities. Notice cards, mailed in March, tell how to easily obtain the *Proxy Statement* and vote.

## Chairman and President's Letter – late-March 2008

Accompanying the Proxy Statement are the 2007 condensed balance sheets and income statements, six years of financial data and an annual message from our chairman and our president. Their letter presents management's perspectives on your company's 2007 performance and trends that may affect performance in 2008 and beyond.

## First-quarter 2008 Letter to Shareholders – mid-May 2008

This message from our chairman and our president includes recent news releases about financial results announced April 30, results of shareholder votes at the 2008 Annual Meeting of Shareholders and actions of the board at its May meeting. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by May 12, 2008.

## Second-quarter 2008 Letter to Shareholders – mid-August 2008

This message from our chairman and our president includes our August 6 news release with financial results. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by August 11, 2008.

## Third-quarter 2008 Letter to Shareholders – mid-November 2008

This message from our chairman and our president includes our October 29 news release with financial results. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by November 10, 2008.

# To Our Shareholders:

Property casualty insurance is your company's main business. Our distinctive approaches to underwriting and investing have made it a consistently profitable business for Cincinnati Financial Corporation and produced steadily increasing dividends for you, our shareholders.

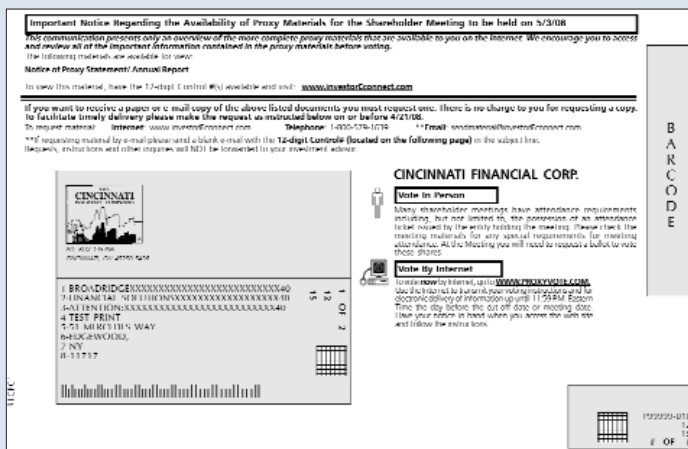
We are one of more than 2,000 U.S. stock and mutual insurer groups that offer individuals and businesses various types of property and casualty coverages. That number makes for a truly competitive marketplace. Competition has been intensifying due to cyclical pressure in our industry, leaving every insurer scrambling for ways to grow in a lower-pricing environment. Broader financial and economic trends also suggest that near-term opportunities may shrink for companies in our industry.

We see the challenges. Yet we believe the operating philosophy your company has in place will continue to be effective now, as in the past. That philosophy determines and

directs the responses and initiatives that help us stand out in any environment or any part of an economic or industry cycle.

Through The Cincinnati Insurance Company and its local independent agent representatives, your company has become one of the 25 largest, based on

## Notice Card



Notice cards mailed by March 24 tell how to easily obtain the *Proxy Statement* and vote online, by phone or through the mail. In early April, a second Notice mailing includes a proxy card to simplify voting by mail.

premium volume, among the 2,000 insurer groups. We have successfully responded to our customers' needs, and we have worked to earn their business. By identifying and

deepening the strategic commitments that allowed us to achieve that rank, we can find opportunities to grow and prosper in any environment.

You'll read more about the philosophy behind those commitments in the following pages. In summary, that philosophy leads us to differentiate ourselves by helping agents and policyholders experience relationships based on knowledge and trust – not mere transactions.

The same principle applies to shareholder relationships. We're pleased with new regulations that allow us to post online rather than mail thousands of bulky paper documents, including the full Annual Report on Form 10-K. However, our pleasure goes beyond the potential to reduce costs and environmental impacts. The real benefit is that we can reallocate some effort and savings to mailing several smaller, more digestible messages to you in 2008, giving you an easier way to gain insight into your company and consider how we can prosper together in the future.

Respectfully,

/S/ John J. Schiff, Jr.

John J. Schiff, Jr., CPCU  
Chairman and Chief Executive Officer

/S/ James E. Benoski

James E. Benoski  
Vice Chairman, President,  
Chief Operating Officer  
and Chief Insurance Officer

# The Cincinnati Experience

Cincinnati Financial Corporation recently reached a new milestone when we began writing excess and surplus lines insurance through two new companies, The Cincinnati Specialty Underwriters Insurance Company and CSU Producer Resources Inc. Donald J. Doyle, Jr., CPCU, AIM, senior vice president leading our new E&S operations, notes, “We tell our independent agents that CSU’s mission is ‘bringing the *Cincinnati experience* to your E&S clients.’ Their response is immediate and positive. Our agents welcome Cincinnati’s relationship-based approach, appropriately applied to aspects of this new venture.”

What is this Cincinnati experience? How does it build the strong relationships that open the door to new opportunities, taking us forward to find new solutions and create more value? Here, some company associates and leaders share their perspectives on how we make the Cincinnati experience special for agents and policyholders:

*“Our research and planning activities affirm our shared belief that partnering with independent agencies is the best way to sell insurance.* Our company’s founding



principle is to be a primary contributor to the success of each agency, regardless of size, location, ownership or length of time appointed. Our strategic plan keeps that principle at the center of our agents’ experience – past, present and future. We listen and act, adapt and improve, in response to these customers. We’ve grown and will continue to grow by meeting their needs for local field representatives to serve their clients; by helping train their new staff members; by deploying Web-based services to support their agency efficiency; and by improving our own internal efficiency and service standards.”

*–Teresa C. Cracas, Counsel and Vice President, Planning & Risk Management*

*“Our company and each subsidiary emphasize strong capitalization, low debt leverage, adequate reserves and appropriate reinsurance programs.* That’s how we build strength, stability and flexibility over the long term. Agents and policyholders experience our strength when they seek an insurer with outstanding ratings from A.M. Best, Fitch, Moody’s and



Standard & Poor's. They experience our stability when we are able to avoid pricing extremes and keep coverage available when the market is disrupted for classes or lines of business. And they experience flexibility when we are able to meet their changing needs by making forward-looking investments in new products, technology or infrastructure."

*–David T. Groff, FCAS, MAAA, CPCU, Vice President, Staff Underwriting*

*"Agencies that receive Cincinnati appointments are the select few – top-notch professional organizations with a strong community presence, sales culture and solid financials.* To become and stay their carrier of choice, we structure our field staff to complement the strengths of our agents as knowledgeable, responsive and trusted advisors. Field



team members are local, working out of their homes in the agencies' communities. They bring our company into our agents' offices with local decision-making authority. Agents can quickly enlist their field marketing representative to help present an insurance program to their prospect. They can reach their field claims representative to guide emergency repairs, or call on their loss control or premium audit representatives to provide client services. The team delivers on the promises agents make to their clients, and we grow together."

*–William M. Clevidence, CIC, Secretary, Sales & Marketing*

*"Agents want the Cincinnati claims experience for their valued clients, including the businesses and people who are centers of influence in their communities.* Our claims service is different. It starts with the way we assign our multi-line claims representatives – to specific agencies, rather than to types of claims. When a policyholder or claimant reports a loss, the agent knows and trusts the local claims representative who will respond. Our representatives make personal contact in most cases within 24 hours, inspect damage, review the policy to find coverage for the claim and provide service with a human touch. They have the authority and

technology to write most checks on the spot. The result is claims service that sells insurance.”

–Charles P. Stoneburner II, CPCU, AIM, Senior Vice President, Field Claims

“As Cincinnati introduces or improves our automation, we preserve and support the agency’s client relationships, choice and control. Technology tools free our agents and associates to do what they do best – sales and service. Our major systems present options that respect agency differences, so agents can experience efficiency gains while managing their client relationships and interactions the way they prefer. Our priorities mirror those of the agencies: we streamline processing and share data between their systems and ours. We mutually benefit from improved data quality, which supports a deeper understanding of the book of business and ensures the right rates, terms and conditions for our products.”

–Robyn C. Muhlberg, Vice President, Information Technology

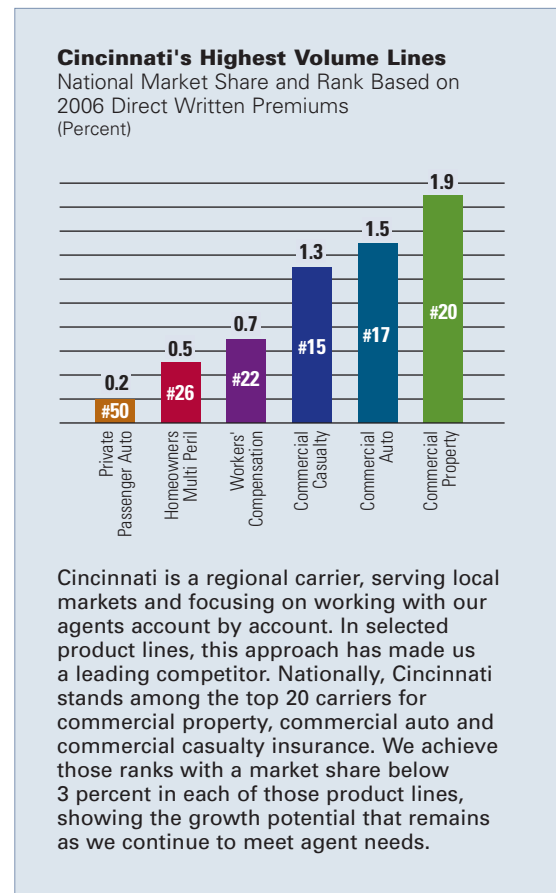
“Policyholders and agents benefit from an underwriting approach that encourages loyalty. They renew more than 90 percent of our expiring policies eligible for renewal. They experience our willingness to write many commercial coverages over a multi-year policy term with pricing that stays the same for the same exposure. In addition to price stability, availability of these



multi-year terms and policy term extensions save everyone from annual paperwork and expenses. We’re also willing to cover our agents’ best-of-class accounts with few exceptions, using versatile products to protect a wide variety of businesses, even as they grow and change. Our underwriters and agents have the skill to tailor comprehensive business insurance packages.

When a loss happens, policyholders are glad their package comes from one agent and one carrier, so it’s clear who will respond.”

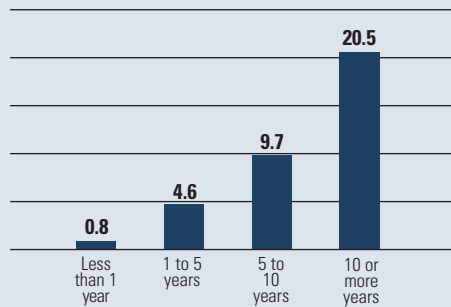
–Stephen A. Ventre, CPCU, Vice President, Commercial Lines



*“Our commitment to personal lines grows from a conviction that insurance is first and foremost a people business. We believe our agents’ home and auto insurance clients deserve a Cincinnati experience with comparable value to the experience of business insurance clients. In fact, a policyholder’s experience with our home or auto policy and service often leads to the decision to become our business policyholder, and vice versa. The same Cincinnati claims representative responds to business and personal claims. The same attention applies to service and product quality, tailored insurance packages and processing systems and efficiencies. We also recognize that different trends and events affect the personal and commercial lines marketplaces to different degrees. Marketing both business and personal insurance can help stabilize the overall book of business.”*

*–John C. DuBois, Assistant Vice President, Personal Lines*

**Cincinnati Market Share Within Reporting Agency Location**  
Based on 2006 Direct Written Premiums (Percent)



As agents learn about Cincinnati, they develop an appreciation for our approach and reward us with a steadily increasing share of their business. We rank No. 1 or No. 2, based on premium volume, in 75 percent of the reporting agency locations that we have served for more than five years. Cincinnati has tremendous potential in the 283 reporting agency locations that have marketed our products for less than five years, even as we continue to grow with the 1,044 more established reporting locations.

*“Cincinnati’s property casualty agencies have easy access to Cincinnati Life products. Our agents can count on Cincinnati Life to help protect their clients’ families, their businesses and their futures. We are a resource for agents whose valuable business clients may need insurance to fund business perpetuation or key employee replacement or who want to offer voluntary benefits to employees. Our term, whole life, universal life and disability income policies and annuities flexibly meet individual and business policyholders’ needs. With the professional advice of our agents, policyholders can select optional features like the accelerated benefit rider. It provides early benefits to terminally ill policyholders, helping preserve their dignity and choices in the last months of life.”*

*–Ann S. Binzer, FLHC, CLU, ChFC, FALU, FLMI, Secretary,  
The Cincinnati Life Insurance Company*



*“Cincinnati has never had to sell an investment security to pay a claim.*

Policyholders, agents, associates and shareholders expect and receive consistent, predictable

performance. We manage insurance operations to achieve a profit, paying all claims and expenses from cash flow. After we buy bonds to cover our insurance



liabilities, we invest in equities. The equities we select and hold offer a current stream of dividends, plus the potential for asset appreciation farther along the horizon. Although financial stocks are a good fit, like any other sector, they periodically fall out of favor. We believe careful selection

and monitoring of well-managed companies, rather than market timing, leads to

higher ultimate returns. This strategy helps us pay steadily increasing dividends

to our shareholders. At the insurance company level, it protects policyholders

by contributing to strong surplus positions.”

*–Martin F. Hollenbeck, CFA, CPCU, Vice President, Investments*

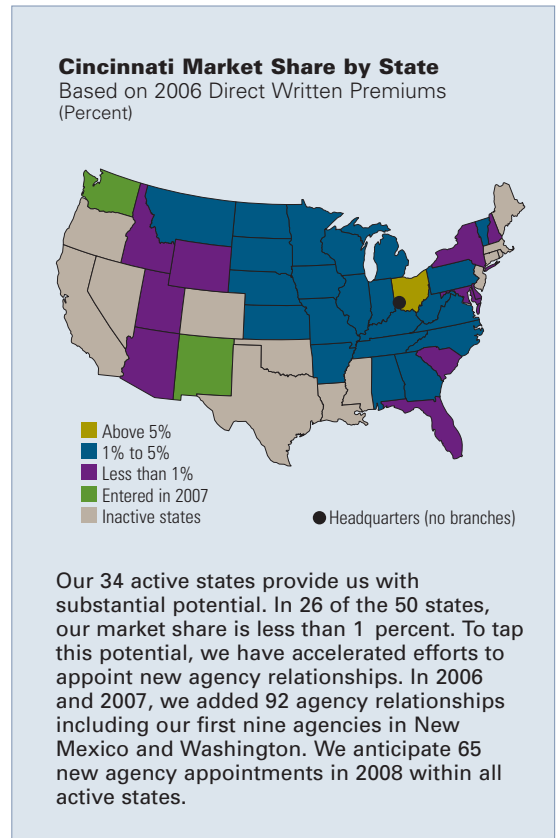
We make deliberate choices about the quality experience we provide for

agents and policyholders. Those experiences create strong relationships that differentiate your

company, giving us a superior ability to prosper in any environment. Relationships are the

centerpiece of our strategies as we move into 2008 and beyond, finding new solutions and creating

long-term value for our shareholders, agents and associates.



Shareholders can experience Cincinnati and support your company's goals by giving us the opportunity to serve your insurance needs. Local independent insurance agencies offer our business policies in 34 states, our personal auto policies in 22 states, homeowner policies in 25 states and life insurance in 49 states. To check availability in your area, please select [Find An Agent](#) on [www.cinfin.com](http://www.cinfin.com) or call us at 1-800-769-0548.

# Condensed Balance Sheets and Income Statements

Cincinnati Financial Corporation and Subsidiaries

(Dollars in millions)

	At December 31,	
	2007 (unaudited)	2006
<b>Assets</b>		
Investments .....	\$ 12,261	\$ 13,759
Cash and cash equivalents .....	226	202
Premiums receivable .....	1,107	1,128
Reinsurance receivable .....	754	683
Other assets .....	2,289	1,450
Total assets .....	<u>\$ 16,637</u>	<u>\$ 17,222</u>
<b>Liabilities</b>		
Insurance reserves .....	\$ 5,445	\$ 5,305
Unearned premiums .....	1,564	1,579
Deferred income tax .....	977	1,653
6.125% senior notes due 2034 .....	371	371
6.9% senior debentures due 2028 .....	28	28
6.92% senior debentures due 2028 .....	392	392
Other liabilities .....	1,931	1,086
Total liabilities .....	<u>10,708</u>	<u>10,414</u>
<b>Shareholders' Equity</b>		
Common stock and paid-in capital .....	1,442	1,406
Retained earnings .....	3,404	2,786
Accumulated other comprehensive income .....	2,151	3,379
Treasury stock .....	(1,068)	(763)
Total shareholders' equity .....	<u>5,929</u>	<u>6,808</u>
Total liabilities and shareholders' equity .....	<u>\$ 16,637</u>	<u>\$ 17,222</u>

(Dollars in millions except per share data)

	Years ended December 31,		
	2007 (unaudited)	2006	2005
<b>Revenues</b>			
Earned premiums .....	\$ 3,250	\$ 3,270	\$ 3,153
Investment income, net of expenses .....	608	570	526
Realized investment gains and losses .....	382	684	61
Other income .....	19	18	16
Total revenues .....	<u>4,259</u>	<u>4,542</u>	<u>3,756</u>
<b>Benefits and Expenses</b>			
Insurance losses and policyholder benefits .....	1,963	2,128	1,911
Commissions .....	624	622	616
Other operating expenses .....	480	463	406
Total benefits and expenses .....	<u>3,067</u>	<u>3,213</u>	<u>2,933</u>
<b>Income Before Income Taxes</b> .....	<b>1,192</b>	1,329	823
<b>Provision for Income Taxes</b> .....	<b>337</b>	399	221
<b>Net Income</b> .....	<u><b>\$ 855</b></u>	<u>\$ 930</u>	<u>\$ 602</u>
<b>Per Common Share</b>			
Net income—basic .....	\$ 5.01	\$ 5.36	\$ 3.44
Net income—diluted .....	\$ 4.97	\$ 5.30	\$ 3.40

# Safe Harbor

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 2006 Annual Report on Form 10-K, Item 1A, Risk Factors, Page 20. Although we often review or update our forward-looking statements when events warrant, we caution our readers that we undertake no obligation to do so. 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
  - Inaccurate estimates or assumptions used for critical accounting estimates
  - 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
  - Changing consumer buying habits and consolidation of independent insurance agencies that could alter our competitive advantages
  - 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:
    - Downgrade of the company's financial strength ratings
    - Concerns that doing business with the company is too difficult or
    - Perceptions that the company's level of service, particularly claims service, is no longer a distinguishing characteristic in the marketplace
  - Sustained decline in overall stock market values negatively affecting the company's equity portfolio and book value; in particular a sustained decline in the market value of Fifth Third shares, a significant equity holding
  - Securities laws that could limit the manner and timing of our investment transactions
  - Recession or other economic conditions or regulatory, accounting or tax changes resulting in lower demand for insurance products
  - Events, such as the sub-prime mortgage lending crisis, that lead to a significant decline in the value of a particular security or group of securities, such as our financial sector holdings, and impairment of the asset(s)
  - 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
  - Delays or inadequacies in the development, implementation, performance and benefits of technology projects and enhancements
  - Ability to obtain adequate reinsurance on acceptable terms, amount of reinsurance purchased, financial strength of reinsurers and the potential for non-payment or delay in payment by reinsurers
  - Increased competition that could result in a significant reduction in the company's premium growth rate
  - Underwriting and pricing methods adopted by competitors that could allow them to identify and flexibly price risks, which could decrease our competitive advantages
  - Personal lines pricing and loss trends that lead management to conclude that this segment could not attain sustainable profitability, which could prevent the capitalization of policy acquisition costs
  - Actions of insurance departments, state attorneys general or other regulatory agencies that:
    - Restrict our ability to exit or reduce writings of unprofitable coverages or lines of business
    - Place the insurance industry under greater regulatory scrutiny or result in new statutes, rules and regulations
    - Increase our expenses
    - 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
    - Limit our ability to set fair, adequate and reasonable rates
    - Place us at a disadvantage in the marketplace or
    - Restrict our ability to execute our business model, including the way we compensate agents
  - Adverse outcomes from litigation or administrative proceedings
  - Investment activities or market value fluctuations that trigger restrictions applicable to the parent company under the Investment Company Act of 1940
  - Events, such as an epidemic, natural catastrophe, terrorism or construction delays, 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, 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 recent measures affecting corporate financial reporting and governance. The ultimate changes and eventual effects, if any, of these initiatives are uncertain.

# Shareholder Information

Cincinnati Financial Corporation had approximately 12,000 shareholders of record and approximately 46,000 beneficial shareholders as of December 31, 2007. Many of the company's independent agent representatives and most of the 4,087 associates of its subsidiaries own the company's common stock.

## Common Stock Price and Dividend Data

Common shares are traded under the symbol CINF on the NASDAQ Global Select Market.

Quarter:	2007				2006			
	1 <sup>st</sup>	2 <sup>nd</sup>	3 <sup>rd</sup>	4 <sup>th</sup>	1 <sup>st</sup>	2 <sup>nd</sup>	3 <sup>rd</sup>	4 <sup>th</sup>
High .....	\$ 45.92	\$ 47.62	\$ 44.79	\$ 44.84	\$ 45.56	\$ 47.01	\$ 48.44	\$ 49.07
Low .....	42.24	42.57	36.91	38.37	42.07	41.43	45.93	44.25
Period-end close .....	42.40	43.40	43.31	39.54	42.07	47.01	48.12	45.31
Cash dividends declared .....	0.355	0.355	0.355	0.355	0.335	0.335	0.335	0.335

## Annual Meeting

Shareholders are invited to attend the Annual Meeting of Shareholders of Cincinnati Financial Corporation at 9:30 a.m. on Saturday, May 3, 2008, at the Cincinnati Art Museum in Eden Park, Cincinnati, Ohio. You may listen to an audio webcast of the event by visiting the Investors section of the company's Web site, [www.cinfin.com](http://www.cinfin.com).

## Independent Registered Public Accounting Firm

Deloitte & Touche LLP  
250 East Fifth Street  
Cincinnati, Ohio 45202-5109

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# Contact Information

Communications directed to the company's secretary, Kenneth W. Stecher, chief financial officer and executive vice president, are shared with the appropriate individual(s). Or, you may directly access services:

**Investors:** Investor Relations responds to investor inquiries about Cincinnati Financial Corporation and its performance.

Heather J. Wietzel – Vice President, Investor Relations  
513-870-2768 or [investor\\_inquiries@cinfin.com](mailto:investor_inquiries@cinfin.com)

**Shareholders:** Shareholder Services provides stock transfer services, fulfills requests for shareholder materials and assists registered shareholders who wish to update account information or enroll in shareholder plans.

Jerry L. Litton – Assistant Vice President, Shareholder Services  
513-870-2639 or [shareholder\\_inquiries@cinfin.com](mailto:shareholder_inquiries@cinfin.com)

**Media:** Corporate Communications assists media representatives seeking information or comment from Cincinnati Financial Corporation or its subsidiaries.

Joan O. Shevchik, CPCU, CLU – Senior Vice President, Corporate Communications  
513-603-5323 or [media\\_inquiries@cinfin.com](mailto:media_inquiries@cinfin.com)

## Cincinnati Financial Corporation

The Cincinnati Insurance Company  
The Cincinnati Casualty Company  
The Cincinnati Indemnity Company  
The Cincinnati Specialty Underwriters Insurance Company

The Cincinnati Life Insurance Company  
CSU Producer Resources Inc.  
CFC Investment Company  
CinFin Capital Management Company

### Mailing Address:

P.O. Box 145496  
Cincinnati, Ohio 45250-5496

Phone: 513-870-2000

Fax: 513-870-2066

[www.cinfin.com](http://www.cinfin.com)

### Street Address:

6200 South Gilmore Road  
Fairfield, Ohio 45014-5141



# Cincinnati Financial Corporation

## 2007 Fourth-quarter and Full-year Letter to Shareholders

February 13, 2008

### To Our Shareholders, Friends and Associates:

Exceptionally strong underwriting and investment income in the fourth quarter helped your company close 2007 with \$610 million of operating income, setting a new record. Our independent agents and associates continue to focus on underwriting fundamentals, including the risk selection and pricing that are key to success in a competitive environment. In addition, nature gave your company a break, hitting us with no significant catastrophe losses in the fourth quarter and only \$26 million for the entire year. What a change this was from last year, when we reported \$44 million of catastrophe losses for the fourth quarter and \$175 million for the full year.

How did we move from record high catastrophe losses one year to record low catastrophe losses the next? To some extent, we can accept credit for managing our catastrophe losses by controlling our coastal exposures, addressing our geographic concentrations, managing policy deductibles and taking other underwriting actions. To a greater extent, the contrast between 2007 and 2006 simply shows that weather is not very predictable. We were lucky in 2007, but cannot predict which way our luck will run in the future. Already in 2008, severe weather across our operating territories has led to catastrophe losses for our policyholders. Our field associates and agents are working hard to assess the damage and develop initial estimates.

That's okay. We are in the business of managing risk. We believe your company is in good shape and has proven strategies to offset the inherent low predictability of weather and the potential it brings for volatile results. We pay attention to the basics, including these three "Rs" of insurance.

**First, reinsurance:** We transfer some of the risk by buying reinsurance. We negotiate prices and contract terms with our high quality reinsurers during the fourth quarter each year. You'll find details of our program in the attached February 6 news release. This program has tremendous benefits in addition to increasing predictability by limiting our potential catastrophe losses. It supports our flexibility in serving our agents and their communities, allowing us to write policies covering higher limits on a case-by-case basis.

**Second, reserves:** We set aside adequate amounts to pay claims, including those already reported as well as those not yet reported. Our reserves for prior years have developed favorably in each of the past 16 years, adding modestly to underwriting profits. You'll read inside that this contribution was higher in 2007 than in the past, and we expect it to return to a more typical level in 2008. Sound reserving policies help assure the accuracy of the prices we charge for our products and the amounts we allocate to pay claims, minimizing the need for reserve charges that would add volatility to our financial results in future years.

**The third "R" is readiness.** We believe catastrophes bring opportunities as we respond effectively. Teams of our own field claims representatives are organized, trained and equipped to move quickly when a storm hits. They are authorized to evaluate and pay claims on the spot, and even our agencies can write checks for smaller claims. They work together to give service with a human touch. Afterwards, policyholders spread the word about their claims satisfaction, increasing sales.

These three "Rs" are part of a fourth you've heard from us before – relationships. Your company aims to conduct business in a way that creates long-term relationships, bringing a measure of stability to shareholders, policyholders, agents and associates. As we consider the challenging market conditions and the severe weather already occurring in early 2008, we think relationships and stability are the right way to weather all storms.

Respectfully,

/S/ John J. Schiff, Jr.

John J. Schiff, Jr., CPCU  
Chairman and Chief Executive Officer

/S/ James E. Benoski

James E. Benoski  
Vice Chairman, President, Chief Operating Officer,  
and Chief Insurance Officer



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This message from our chairman and our president includes recent news releases about financial results announced February 6 and actions taken by the board of directors at its February 1 meeting. *The Cincinnati Experience*, a profile of our operating philosophy, accompanies this letter.

### *The Cincinnati Experience – mid-February 2008*

The Cincinnati Insurance Company, Cincinnati Financial Corporation's lead subsidiary, ranks among the top 25 U.S. property casualty insurer groups based on net written premiums. In *The Cincinnati Experience*, you'll read about how our relationship-based approach creates value and loyalty, supporting premium growth.

### 2007 Annual Report on Form 10-K – late-February 2008

The *Annual Report on Form 10-K* is a detailed document published by every publicly traded company as required by the U.S. Securities and Exchange Commission. In our report, we describe your company's operations, its results and trends, along with supporting data, discussions, audited financial statements and accompanying notes.

### 2008 Shareholder Meeting Notice and Proxy Statement – mid-March 2008

This statement informs you of items requiring shareholder action at the 2008 Annual Meeting of Shareholders on May 3, 2008. It identifies board members, detailing director and executive officer compensation and board activities. Notice cards, mailed in March, tell how to easily obtain the *Proxy Statement* and vote.

### *Chairman and President's Letter – late-March 2008*

Accompanying the Proxy Statement are the 2007 condensed balance sheets and income statements, six years of financial data and an annual message from our chairman and our president. Their letter presents management's perspectives on your company's 2007 performance and trends that may affect performance in 2008 and beyond.

### First-quarter 2008 Letter to Shareholders – mid-May 2008

This message from our chairman and our president includes recent news releases about financial results announced April 30, results of shareholder votes at the 2008 Annual Meeting of Shareholders and actions of the board at its May meeting. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by May 12, 2008.

### Second-quarter 2008 Letter to Shareholders – mid-August 2008

This message from our chairman and our president includes our August 6 news release with financial results. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by August 11, 2008.

### Third-quarter 2008 Letter to Shareholders – mid-November 2008

This message from our chairman and our president includes our October 29 news release with financial results. For additional details, see our *Quarterly Report on Form 10-Q*, filed with the SEC by November 10, 2008.

# Recent News Releases

## Cincinnati Financial Reports Fourth-quarter and Full-year 2007 Results

Cincinnati, February 6, 2008 – Cincinnati Financial Corporation (Nasdaq: CINF) today reported:

- Fourth-quarter net income of \$187 million, or \$1.11 per share, compared with \$130 million, or 75 cents, in the 2006 fourth quarter. Operating income\* of \$179 million, or \$1.07 per share, compared with \$122 million, or 70 cents.
- Full-year 2007 net income of \$855 million, or \$4.97 per share, compared with \$930 million, or \$5.30, in 2006. Operating income a record \$610 million, or \$3.54 per share, compared with \$496 million, or \$2.82.
- Full-year 2007 property casualty underwriting profits of \$304 million compared with \$181 million in 2006.

### Financial Highlights\*

(Dollars in millions except share data)	Three months ended December 31,			Twelve months ended December 31,		
	2007	2006	Change %	2007	2006	Change %
<b>Revenue Highlights</b>						
Earned premiums	\$ 809	\$ 830	(2.5)	\$ 3,250	\$ 3,270	(0.6)
Investment income	157	145	8.5	608	570	6.6
Total revenues	983	992	(0.9)	4,259	4,542	(6.2)
<b>Income Statement Data</b>						
Net income	\$ 187	\$ 130	43.2	\$ 855	\$ 930	(8.0)
Net realized investment gains and losses	8	8	(4.7)	245	434	(43.5)
Operating income*	\$ 179	\$ 122	46.4	\$ 610	\$ 496	23.1
<b>Per Share Data (diluted)</b>						
Net income	\$ 1.11	\$ 0.75	48.0	\$ 4.97	\$ 5.30	(6.2)
Net realized investment gains and losses	0.04	0.05	(20.0)	1.43	2.48	(42.3)
Operating income*	\$ 1.07	\$ 0.70	52.9	\$ 3.54	\$ 2.82	25.5
Book value				\$ 35.70	\$ 39.38	(9.3)
Cash dividend declared	\$ 0.355	\$ 0.335	6.0	\$ 1.42	\$ 1.34	6.0
Weighted average shares outstanding	168,163,752	174,988,162	(3.9)	172,167,452	175,451,341	(1.9)

### Insurance Operations Highlights

- 85.6 percent fourth-quarter 2007 property casualty combined ratio with 4.1 percent decrease in net written premiums; 90.3 percent full-year 2007 property casualty combined ratio with 1.9 percent decrease in net written premiums.
- Profitability improved from prior year periods because of lowest catastrophe loss ratio in over 15 years and \$244 million in full-year savings from favorable development on prior period reserves compared with \$116 million in 2006.
- Continuing new business activity and policyholder retention levels illustrate value of the company's relationships with independent insurance agents in a competitive market.
- 23 cent per share contribution from life insurance operating income to full-year results, up from 19 cents in 2006.

### Investment and Balance Sheet Highlights

- 8.5 percent growth in fourth-quarter 2007 pretax investment income with 6.6 percent full-year increase. Investment income benefited from strong dividend increases in the equity portfolio.
- Book value of \$35.70 per share compared with \$39.38 at year-end 2006. Invested assets and book value declined

primarily on lower market values of financial sector equity holdings.

- \$245 million in full-year 2007 net realized investment gains and losses compared with \$434 million in full-year 2006. 2006 gains included the sale of the company's second largest common stock holding.
- 3.3 million reduction in weighted-average shares outstanding in 2007. Repurchases of the company's common stock totaled 7.5 million shares at a cost of \$306 million, including fourth-quarter accelerated share repurchase.

### Full-year 2008 Outlook\*\*

- Property casualty insurance operations – Management anticipates lower net written premiums due to competitive pricing, with upward pressure on the combined ratio for 2008.
- Investment operations – Management anticipates slower growth in investment income as financial sector holdings evaluate dividend levels. Portfolio strategies to balance near-term income generation and long-term book value growth continue to be our focus.

\* The Definitions of Non-GAAP Information and Reconciliation to Comparable GAAP Measures on www.cinfin.com defines and reconciles measures presented in this release that are not based on Generally Accepted Accounting Principles or Statutory Accounting Principles.

\*\* Forward-looking statements and related assumptions are subject to the risks outlined in the company's safe-harbor statement (see Page 13).

## **Challenging Property Casualty Insurance Environment**

Chairman and Chief Executive Officer John J. Schiff, Jr., CPCU, commented, "We continue to see the benefits of our agency-centered approach, with local market decision making that creates agent and policyholder loyalty through all stages of the insurance pricing cycle. We credit those relationships with contributing to 2007's strong results. Further, our policyholders' catastrophe losses were at the lowest level since 1997 and our savings from favorable development on prior period reserves was above our guidance. We expect these measures to return to more normal levels in the future."

Schiff added, "Our commercial lines premiums continue to reflect reduced pricing due to increased competition. As well, we are seeing economic pressure in some regions and on some types of business, which affects our policyholders' revenues or payrolls and is a factor in the premiums calculated for certain business policies. We have performed well under these types of tough commercial lines market conditions in the past. Our approach – supporting our agents' strong local advantages through our team of field representatives and headquarters associates – gives us unique strengths to succeed. The local knowledge of our agents and field associates helps us carefully underwrite accounts, selecting only the commercial business that appears to be appropriately priced relative to the risk we would assume."

Schiff noted, "Likewise, the marketplace is competitive for personal lines in many regions. Lower new and renewal premiums per policy have reduced our personal lines net written premiums. We are addressing our competitive position so we can resume growing in personal lines. We continue to refine our rates, building on the changes we made in mid-2006 to the structure of our premium credits. Those changes better positioned our agencies to sell the value of our homeowner and personal auto policies. As a result, policy retention rates remain above 90 percent and new personal lines business continues to grow. Another way in which we hope to grow is by making our personal lines products available over the next two years in states where agents currently market only our commercial lines products."

## **Long-term Investment in Property Casualty Business**

James E. Benoski, vice chairman, chief insurance officer and president, said, "2007 marked our first agency appointments and first commercial lines policies in Washington and New Mexico, the 33<sup>rd</sup> and 34<sup>th</sup> states where we actively market property casualty insurance."

Benoski added, "Across our established states, Cincinnati has earned a generous share of each agency's business over the years by offering the products and services agents need to protect their local businesses and families. Our agents have indicated their desire to have Cincinnati available as a market for commercial accounts that require the flexibility of excess and surplus lines coverage. Preparations that began in early 2007 for our excess and surplus lines operations concluded on schedule in December. Our new subsidiary, The Cincinnati Specialty Underwriters Insurance Company, received an A (Excellent) rating from A.M. Best Co., an independent provider of insurer ratings. They began 2008 by successfully issuing the first surplus lines policies from the new policy administration system.

"In addition to growing with our current agencies, we also continue to build new relationships, making agency appointments within our current marketing territories and recently opened states. In total, we completed 66 agency appointments in 2007, including 50 that were new relationships. With many more in the pipeline, we are targeting another 65 appointments in 2008. New appointments, net of other changes in our agency relationships, brought total reporting agency locations to 1,327 at year-end 2007, compared with 1,289 at year-end 2006."

## **2007 Property Casualty Combined Ratio**

Kenneth W. Stecher, chief financial officer and executive vice president, said, "Cincinnati's overall profitability for the fourth quarter and full year was excellent and improved from last year's levels. Results for both the quarter and year benefited from very low catastrophe losses and savings from favorable development on prior period reserves above our guidance. In contrast, the industry's full-year 2007 combined ratio is expected to rise to approximately 95.6 percent, including 1.7 percentage points from catastrophe losses, from 92.4 percent, including 2.1 percentage points from catastrophe losses, in 2006.

Stecher noted, "We did experience a rise in the current accident year loss ratio excluding catastrophe losses. We believe two factors were largely responsible. First, current market conditions and softer pricing are hampering profitability. Second, there are instances when losses from weather events can be significant for some carriers, but not rise to the level where Property Claims Services tracks industrywide losses and designates the events as insurance catastrophes. We believe that was the case for us in 2007, with non-catastrophe weather-related losses adding about 1 percentage point more to our loss ratio than in 2006."

## **2008 Property Casualty Outlook Update**

Stecher commented, "If current commercial lines pricing trends continue into 2008, our net written premiums could decline as much as 5 percent. We believe our GAAP combined ratio could be between 96 percent and 98 percent, as we meet the needs of our agencies while managing for long-term profitability. Industry full-year 2008 net written premiums are expected to decline 0.6 percent with the combined ratio rising to 98.6 percent."

Stecher observed that the combined ratio target relies on three assumptions:

- Current accident year loss ratio excluding catastrophe losses – The company believes the market trends that contributed to an increase in this ratio in 2007 are continuing and may put the ratio under further pressure in 2008.
- Catastrophe loss ratio – The company assumes catastrophe losses would contribute approximately 4.5 percentage points to the full-year 2008 combined ratio. Stecher noted the unpredictability of catastrophic events in any given year. Catastrophe losses have made an average contribution of 3.7 percentage points to the company's combined ratio in the past 10 years, ranging from 2007's low of 0.8 points to 1998's high of 6.1 points.



- Savings from favorable development on prior period reserves – The company assumes savings from favorable development would reduce the full-year 2008 combined ratio by approximately 4 percentage points. Stecher indicated that management will continue to rely on sound actuarial analysis in the determination of loss and loss expense reserves, even as market conditions soften.

Stecher added, “We believe the level of performance we have targeted will allow us to sustain our industry leading position in the commercial lines insurance marketplace. We plan to take steps in our personal lines insurance operations to enhance our response to the changing marketplace. And finally, we look for our life insurance business to continue to make a solid and growing contribution to our earnings.

“Our strong position gives us opportunities to be a market for our agents’ best business, giving them market stability and contributing to their success. Further, we believe we can expect a positive contribution from our new excess and surplus lines operations, although our 2008 targets do not take into account any contribution from excess and surplus lines. We are mindful that it will take some time before our excess and surplus lines operation is of sufficient size to materially influence our overall corporate results,” Stecher said.

#### Investment Performance Affected by Recent Market Activity

Schiff commented, “Our buy-and-hold equity investing strategy has been key to the long-term growth of our assets and shareholders’ equity. We identify companies with the potential for sales, earnings and dividend growth, a strong management team and favorable outlook. Over the years, these equities have generally offered a steadily increasing flow of dividend income along with the potential for capital appreciation.

“Since mid-2007, the success of this strategy has been interrupted as the financial markets have reflected broad

concerns about credit quality, liquidity and the general health of the economy. As we noted in September 2007, uncertainty about the duration and the impact of these issues could significantly influence valuations and the volatility of the markets,” Schiff continued.

“Five months later, our book value has declined due to the significant drop in market value of our financial sector common stocks, which represent approximately 35 percent of our investment portfolio. To varying degrees, these companies are addressing a challenging credit quality environment and related issues. As a result, they may evaluate their dividend levels in light of their own capital requirements and earnings outlook, potentially slowing our investment income growth.

“Providing balance to the challenges of our equity portfolio, our bond portfolio continued to hold steady in the fourth quarter as widening credit spreads were offset by the strong demand in the market for low-risk securities. We believe our investment strategy will continue to allow us to maximize both income and capital appreciation over the long term. We are committed to sustaining the strong capitalization that supports our high insurer financial strength ratings, giving our agents a distinct marketing advantage for their value-oriented clients.”

Schiff added, “Your company returned \$546 million to shareholders in 2007 through cash dividends and a record level of repurchase activity, including the accelerated share repurchase agreement announced in October. At that time, the board of directors expanded its repurchase authorization to communicate to shareholders its confidence in our business and our long-term outlook. The board acted last week to raise the indicated annual dividend rate by 9.9 percent, to \$1.56 per share. We expect the board to continue to take actions supporting increased shareholder value over the long term.”

### Property Casualty Insurance Operations

(Dollars in millions)	Three months ended December 31,			Twelve months ended December 31,		
	2007	2006	Change %	2007	2006	Change %
Written premiums . . . . .	<u>\$ 724</u>	<u>\$ 755</u>	(4.1)	<u>\$ 3,117</u>	<u>\$ 3,178</u>	(1.9)
Earned premiums . . . . .	<u>\$ 777</u>	<u>\$ 802</u>	(3.1)	<u>\$ 3,125</u>	<u>\$ 3,164</u>	(1.2)
Loss and loss expenses excluding catastrophes	<u>397</u>	<u>458</u>	(13.3)	<u>1,806</u>	<u>1,833</u>	(1.5)
Catastrophe loss and loss expenses . . . . .	<u>(2)</u>	<u>44</u>	(104.0)	<u>26</u>	<u>175</u>	(85.1)
Commission expenses . . . . .	<u>159</u>	<u>144</u>	10.3	<u>599</u>	<u>596</u>	0.4
Underwriting expenses . . . . .	<u>105</u>	<u>108</u>	(2.3)	<u>375</u>	<u>363</u>	3.2
Policyholder dividends . . . . .	<u>6</u>	<u>4</u>	41.6	<u>15</u>	<u>16</u>	(5.4)
Underwriting profit . . . . .	<u>\$ 112</u>	<u>\$ 44</u>	153.4	<u>\$ 304</u>	<u>\$ 181</u>	68.3
Ratios as a percent of earned premiums:						
Loss and loss expenses excluding catastrophes	<u>51.1%</u>	<u>57.1%</u>		<u>57.8%</u>	<u>58.0%</u>	
Catastrophe loss and loss expenses . . . . .	<u>(0.2)</u>	<u>5.5</u>		<u>0.8</u>	<u>5.5</u>	
Loss and loss expenses . . . . .	<u>50.9%</u>	<u>62.6%</u>		<u>58.6%</u>	<u>63.5%</u>	
Commission expenses . . . . .	<u>20.5</u>	<u>18.0</u>		<u>19.2</u>	<u>18.8</u>	
Underwriting expenses . . . . .	<u>13.4</u>	<u>13.3</u>		<u>12.0</u>	<u>11.5</u>	
Policyholder dividends . . . . .	<u>0.8</u>	<u>0.6</u>		<u>0.5</u>	<u>0.5</u>	
Combined ratio . . . . .	<u>85.6%</u>	<u>94.5%</u>		<u>90.3%</u>	<u>94.3%</u>	

- \$81 million in fourth-quarter 2007 new business written directly by agencies compared with \$88 million in last year's fourth quarter. Full-year new business was \$325 million in 2007 compared with \$357 million in 2006.
- 1,092 agency relationships with 1,327 reporting locations marketed our insurance products at year-end 2007, up from 1,066 agency relationships with 1,289 reporting locations at year-end 2006.
- Contributions to premiums and underwriting income from excess and surplus lines will begin in 2008.
- 2008 property casualty reinsurance program finalized. Program updated to maintain balance between the cost of the program and the level of risk retained. Reinsurance costs expected to decline slightly due to slightly higher retention levels and moderating rates for certain lines of business.

## 2008 Reinsurance Program

Treaties	Retention Summary	Comments
Property catastrophe	For any one event, retain losses of: <ul style="list-style-type: none"> <li>• 100% of first \$45 million</li> <li>• 43% between \$45 million and \$70 million</li> <li>• 5% between \$70 million and \$200 million</li> <li>• 11% to 19% for layers between \$200 million and \$500 million</li> </ul>	<ul style="list-style-type: none"> <li>• After reinsurance, our maximum exposure to a catastrophic event that caused \$500 million in covered losses would be \$105 million compared with \$103 million in 2007. The largest catastrophe loss in our history was \$87 million before reinsurance.</li> </ul>
Casualty per risk	For a single loss, retain: <ul style="list-style-type: none"> <li>• 100% of first \$5 million</li> <li>• 0% between \$5 million and \$25 million</li> <li>• Obtain facultative reinsurance above \$25 million</li> </ul>	<ul style="list-style-type: none"> <li>• Increased casualty treaty retention to \$5 million from \$4 million</li> </ul>
Property per risk	For a single loss, retain: <ul style="list-style-type: none"> <li>• 100% of first \$4 million</li> <li>• 0% between \$4 million and \$25 million</li> <li>• Obtain facultative reinsurance above \$25 million</li> </ul>	<ul style="list-style-type: none"> <li>• No changes in 2008</li> </ul>
Casualty third excess	• \$25 million excess of \$25 million	• No changes in 2008
Casualty fourth excess	• \$20 million excess of \$50 million	• No changes in 2008

## Insurance Segment Highlights

### Commercial Lines Insurance Operations

(Dollars in millions)	Three months ended December 31,			Twelve months ended December 31,		
	2007	2006	Change %	2007	2006	Change %
Written premiums . . . . .	\$ 562	\$ 589	(4.6)	\$ 2,413	\$ 2,442	(1.2)
Earned premiums . . . . .	\$ 601	\$ 619	(3.0)	\$ 2,411	\$ 2,402	0.4
Loss and loss expenses excluding catastrophes	310	357	(13.2)	1,378	1,377	0.1
Catastrophe loss and loss expenses . . . . .	0	11	nm	16	89	(81.3)
Commission expenses . . . . .	123	113	9.2	454	444	2.0
Underwriting expenses . . . . .	86	79	8.7	287	268	7.0
Policyholder dividends . . . . .	6	4	41.6	15	16	(5.4)
Underwriting profit . . . . .	\$ 76	\$ 55	38.1	\$ 261	\$ 208	25.4
Ratios as a percent of earned premiums:						
Loss and loss expenses excluding catastrophes	51.5%	57.6%		57.2%	57.3%	
Catastrophe loss and loss expenses . . . . .	0.0	1.9		0.7	3.7	
Loss and loss expenses . . . . .	51.5%	59.5%		57.9%	61.0%	
Commission expenses . . . . .	20.6	18.3		18.8	18.5	
Underwriting expenses . . . . .	14.1	12.6		11.9	11.1	
Policyholder dividends . . . . .	1.1	0.7		0.6	0.7	
Combined ratio . . . . .	87.3%	91.1%		89.2%	91.3%	

- \$562 million of commercial lines net written premiums for the three months ended December 31, 2007. \$71 million of new fourth-quarter commercial lines business written directly by agencies, down 10.5 percent from \$80 million in the comparable 2006 quarter.
- \$2.413 billion of commercial lines net written premiums for full-year 2007. \$287 million of new 2007 commercial lines business written directly by agencies, down 11.5 percent from \$324 million for full-year 2006.
- Direct bill payment option now available for businessowners policies issued through e-CLAS policy processing system. Selected agencies received this capability in 2007, with first-quarter 2008 rollout planned for all agencies currently using e-CLAS. By the end of 2008, development of a direct bill payment option for commercial policies not issued through e-CLAS is anticipated.
- 89.2 percent full-year 2007 commercial lines combined ratio, improved 2.1 percentage points over 91.3 percent in full year 2006. This result included higher current accident year losses excluding catastrophe losses and higher expenses. These increases were more than offset by lower catastrophe losses and higher savings from favorable development on prior period reserves.
- 3.8 percentage point increase in full-year 2007 current accident year loss ratio excluding catastrophe losses, due to non-catastrophe weather-related losses and softening market conditions.
- Commercial lines insurance industry combined ratio for full-year 2007 estimated at 94.0 percent with decline in net written premiums estimated at 1.5 percent.

## Personal Lines Insurance Operations

(Dollars in millions)	Three months ended December 31,			Twelve months ended December 31,		
	2007	2006	Change %	2007	2006	Change %
Written premiums	\$ 162	\$ 166	(2.3)	\$ 704	\$ 736	(4.4)
Earned premiums	\$ 176	\$ 183	(3.7)	\$ 714	\$ 762	(6.3)
Loss and loss expenses excluding catastrophes	87	101	(13.9)	428	456	(6.2)
Catastrophe loss and loss expenses	(2)	33	(105.3)	10	86	(89.0)
Commission expenses	36	31	14.1	145	152	(4.4)
Underwriting expenses	19	29	(32.5)	88	95	(7.5)
Underwriting profit (loss)	\$ 36	\$ (11)	426.3	\$ 43	\$ (27)	260.9
Ratios as a percent of earned premiums:						
Loss and loss expenses excluding catastrophes	49.6%	55.5%		60.0%	59.9%	
Catastrophe loss and loss expenses	(1.0)	17.9		1.3	11.3	
Loss and loss expenses	48.6%	73.4%		61.3%	71.2%	
Commission expenses	20.1	16.9		20.3	19.9	
Underwriting expenses	11.0	15.7		12.3	12.5	
Combined ratio	79.7%	106.0%		93.9%	103.6%	

- \$162 million of personal lines net written premiums for the three months ended December 31, 2007. \$10 million of new fourth-quarter personal lines business written directly by agencies, up 12.1 percent from \$9 million in the comparable 2006 quarter.
- \$704 million of personal lines net written premiums for full-year 2007. \$38 million of new 2007 personal lines business written directly by agencies, up 16.9 percent from \$33 million in full-year 2006.
- This was the sixth consecutive quarter of new business growth following July 2006 introduction of a limited program of policy credits for homeowner and personal auto pricing in most states where the company's Diamond personal lines policy processing system is in use. Lower premiums per policy continue to constrain new and renewal premium growth.
- 93.9 percent full-year 2007 personal lines combined ratio, an improvement of 9.7 percentage points over 103.6 percent in full-year 2006. This result included higher current accident year losses excluding catastrophe losses. That increase was more than offset by lower catastrophe losses and higher savings from favorable development on prior period reserves.
- 2.3 percentage point increase in full-year 2007 current accident year loss ratio excluding catastrophe losses, due to non-catastrophe weather-related losses and lower personal auto pricing.
- Personal lines insurance industry combined ratio for full-year 2007 estimated at 97.0 percent on flat net written premiums.

## Life Insurance Operations

(In millions)	Three months ended December 31,			Twelve months ended December 31,		
	2007	2006	Change %	2007	2006	Change %
Written premiums . . . . .	\$ <b>41</b>	\$ 41	(0.1)	\$ <b>167</b>	\$ 161	3.2
Earned premiums . . . . .	\$ <b>32</b>	\$ 29	11.0	\$ <b>125</b>	\$ 107	17.4
Investment income, net of expenses . . . . .	<b>30</b>	27	10.2	<b>115</b>	108	6.3
Other income . . . . .	<b>1</b>	1	(1.0)	<b>4</b>	3	25.1
Total revenues, excluding realized investment gains and losses . . . . .	<b>63</b>	57	10.4	<b>244</b>	218	12.0
Policyholder benefits . . . . .	<b>35</b>	30	15.0	<b>133</b>	122	9.2
Expenses . . . . .	<b>15</b>	16	(6.8)	<b>52</b>	43	20.1
Total benefits and expenses . . . . .	<b>50</b>	46	7.6	<b>185</b>	165	12.0
Net income before income tax and realized investment gains and losses . . . . .	<b>13</b>	11	22.8	<b>59</b>	53	12.1
Income tax . . . . .	<b>4</b>	4	17.9	<b>20</b>	19	5.2
Net income before realized investment gains and losses . . . . .	\$ <b>9</b>	\$ 7	25.3	\$ <b>39</b>	\$ 34	15.9

- \$167 million in total 2007 life insurance segment net written premiums. Written premiums include life insurance, annuity and accident and health premiums.
- 10.5 percent increase to \$141 million in 2007 in written premiums for life insurance products.
- 21.6 percent rise in full-year term life insurance written premiums, reflecting marketing advantages of competitive, up-to-date products, providing close personal attention and exhibiting financial strength and stability. Statutory written annuity premiums decreased to \$22 million in 2007 from \$30 million in 2006. Since late 2005, the company has de-emphasized annuity sales due to unfavorable market conditions.

- 8.6 percent rise in face amount of life policies in force to \$61.875 billion at year-end 2007, from \$56.971 billion at year-end 2006.
- \$5 million increase in 2007 operating profit due to favorable mortality experience and persistency as well as healthy earned premium and investment income growth.
- 2008 plans include redesign of all life term insurance products. In addition to redesigning the worksite term product, we will update the full worksite life portfolio. These improvements support opportunities to cross-sell life insurance products to clients of the independent agencies that sell Cincinnati's property casualty insurance policies.

## Investment and Balance Sheet Highlights

### Investment Operations

(In millions)	Three months ended December 31,			Twelve months ended December 31,		
	2007	2006	Change %	2007	2006	Change %
Investment income:						
Interest . . . . .	\$ <b>79</b>	\$ 75	4.4	\$ <b>308</b>	\$ 300	2.5
Dividends . . . . .	<b>75</b>	68	10.4	<b>294</b>	262	12.1
Other . . . . .	<b>4</b>	4	0.8	<b>15</b>	15	(0.5)
Investment expenses . . . . .	<b>(1)</b>	(2)	96.9	<b>(9)</b>	(7)	(18.7)
Total investment income, net of expenses	<b>157</b>	145	8.5	<b>608</b>	570	6.6
Investment interest credited to contract holders	<b>(14)</b>	(14)	(5.6)	<b>(57)</b>	(54)	(5.1)
Realized investment gains and losses summary:						
Realized investment gains and losses . . . . .	<b>38</b>	11	254.0	<b>409</b>	678	(39.6)
Change in fair value of securities with embedded derivatives . . . . .	<b>(12)</b>	2	(933.2)	<b>(11)</b>	7	(263.6)
Other-than-temporary impairment charges . . . . .	<b>(14)</b>	0	nm	<b>(16)</b>	(1)	(1,872.5)
Total realized investment gains and losses	<b>12</b>	13	(2.0)	<b>382</b>	684	(44.1)
Investment operations income . . . . .	\$ <b>155</b>	\$ 144	7.9	\$ <b>933</b>	\$ 1,200	(22.2)

(Dollars in millions except share data)

	At December 31, 2007	At December 31, 2006
<b>Balance sheet data</b>		
Invested assets .....	\$ 12,261	\$ 13,759
Total assets .....	16,637	17,222
Short-term debt .....	69	49
Long-term debt .....	791	791
Shareholders' equity .....	5,929	6,808
Book value per share .....	35.70	39.38
Debt-to-capital ratio .....	12.7%	11.0%

	Three months ended December 31,		Twelve months ended December 31,	
	2007	2006	2007	2006
<b>Performance measures</b>				
Comprehensive income .....	\$ (404)	\$ 449	\$ (376)	\$ 1,057
Return on equity, annualized .....	12.0%	7.9%	13.4%	14.4%
Return on equity, annualized, based on comprehensive income .....	(25.9)	27.0	(5.9)	16.4

- 8.5 percent growth in fourth-quarter net investment income to \$157 million pretax. Full-year 2007 investment income up 6.6 percent to \$608 million.
- 12.1 percent growth in full-year 2007 dividend income, which contributed \$294 million to investment income. Increase reflected higher dividend payout by 35 of the company's 41 common stock holdings. Dividend income growth rate expected to moderate in 2008 as financial sector holdings evaluate dividend levels.
- Repurchases of the company's common stock totaled 4.0 million shares at a cost of \$162 million in the fourth quarter and 7.5 million shares at a cost of \$306 million for the year. 2007 repurchases represented 4.3 percent of shares outstanding. Approximately 13 million shares remain authorized for repurchase.
- Fourth-quarter repurchases largely due to accelerated share repurchase agreement announced in October. Completed in January 2008, ASR totaled 4,071,000 shares at an average price of \$39.18.
- Sales of equity securities were the primary reason for \$382 million in 2007 pre-tax realized investment gains. Equity sales in 2007 included the sale of approximately 3.8 million shares of Exxon Mobil Corporation common stock as well as the block sale of 5.5 million shares of Fifth Third Bancorp common stock. Sale of our large Alltel Corporation common stock holding was the primary reason for the \$684 million in 2006 pre-tax realized investment gains.
- Fifth Third remains the company's largest equity holding and Cincinnati Financial remains Fifth Third's largest shareholder.
- \$12.198 billion in investment portfolio assets market value at year-end 2007 compared with \$13.699 billion at year-end 2006. Lower market valuations of equity holdings due to broad concerns about credit quality, liquidity and the general health of the economy accounted for the majority of the decline.
- Shareholders' equity at \$5.929 billion, or \$35.70 per share, at year-end 2007, down from \$6.808 billion, or \$39.38, at year-end 2006. Decline caused by lower market values for equity holdings and record level of repurchase activity.
- \$4.306 billion in statutory surplus for the property casualty insurance group at year-end 2007, compared with \$4.750 billion at year-end 2006. The ratio of common stock to statutory surplus for the property casualty insurance group portfolio was 84.5 percent at year-end 2007, compared with 96.7 percent at year-end 2006.
- 28.4 percent ratio of investment securities held at the holding-company level to total holding-company-only assets at year-end 2007, comfortably within management's below-40 percent target.

For additional information or to hear a replay of the February 6 conference call webcast, please visit [www.cinfin.com/investors](http://www.cinfin.com/investors).

## Cincinnati Financial Corporation Consolidated Balance Sheets

(Dollars in millions except per share data)

	December 31, 2007 (unaudited)	December 31, 2006
<b>Assets</b>		
Investments		
Fixed maturities, at fair value (amortized cost: 2007-\$5,783; 2006-\$5,739) . . . . .	\$ 5,848	\$ 5,805
(includes securities pledged to creditors of \$745 at December 31, 2007)		
Equity securities, at fair value (cost: 2007-\$2,975; 2006-\$2,621) . . . . .	6,249	7,799
Short-term investments, at fair value (amortized cost: 2007-\$101; 2006-\$95) . . . . .	101	95
Other invested assets . . . . .	63	60
Total investments . . . . .	<u>12,261</u>	<u>13,759</u>
Cash and cash equivalents . . . . .	226	202
Securities lending collateral invested . . . . .	760	0
Investment income receivable . . . . .	124	121
Finance receivable . . . . .	92	108
Premiums receivable . . . . .	1,107	1,128
Reinsurance receivable . . . . .	754	683
Prepaid reinsurance premiums . . . . .	13	13
Deferred policy acquisition costs . . . . .	461	453
Land, building and equipment, net, for company use (accumulated depreciation: 2007-\$276; 2006-\$261) . . . . .	239	193
Other assets . . . . .	72	58
Separate accounts . . . . .	528	504
Total assets . . . . .	<u>\$ 16,637</u>	<u>\$ 17,222</u>
<b>Liabilities</b>		
Insurance reserves		
Loss and loss expense reserves . . . . .	\$ 3,967	\$ 3,896
Life policy reserves . . . . .	1,478	1,409
Unearned premiums . . . . .	1,564	1,579
Securities lending payable . . . . .	760	0
Other liabilities . . . . .	574	533
Deferred income tax . . . . .	977	1,653
Note payable . . . . .	69	49
6.125% senior notes due 2034 . . . . .	371	371
6.9% senior debentures due 2028 . . . . .	28	28
6.92% senior debentures due 2028 . . . . .	392	392
Separate accounts . . . . .	528	504
Total liabilities . . . . .	<u>10,708</u>	<u>10,414</u>
<b>Shareholders' Equity</b>		
Common stock, par value-\$2 per share; (authorized: 2007-500 million shares, 2006-500 million shares; issued: 2007-196 million shares, 2006-196 million shares) . . . . .	393	391
Paid-in capital . . . . .	1,049	1,015
Retained earnings . . . . .	3,404	2,786
Accumulated other comprehensive income . . . . .	2,151	3,379
Treasury stock at cost (2007-30 million shares, 2006-23 million shares) . . . . .	<u>(1,068)</u>	<u>(763)</u>
Total shareholders' equity . . . . .	<u>5,929</u>	<u>6,808</u>
Total liabilities and shareholders' equity . . . . .	<u>\$ 16,637</u>	<u>\$ 17,222</u>



## Cincinnati Financial Corporation Consolidated Statements of Income

(In millions except per share data)	Three months ended December 31,		Twelve months ended December 31,	
	<b>2007</b>	2006	<b>2007</b>	2006
	(unaudited)		(unaudited)	
<b>Revenues</b>				
Earned premiums				
Property casualty .....	\$ 777	\$ 802	\$ 3,125	\$ 3,163
Life .....	32	29	125	107
Investment income, net of expenses .....	157	145	608	570
Realized investment gains and losses .....	12	12	382	684
Other income .....	5	4	19	18
Total revenues .....	<u>983</u>	<u>992</u>	<u>4,259</u>	<u>4,542</u>
<b>Benefits and Expenses</b>				
Insurance losses and policyholder benefits .....	430	532	1,963	2,128
Commissions .....	164	150	624	622
Other operating expenses .....	96	100	362	354
Taxes, licenses and fees .....	18	19	75	77
Increase in deferred policy acquisition costs .....	8	5	(9)	(21)
Interest expense .....	13	14	52	53
Total benefits and expenses .....	<u>729</u>	<u>820</u>	<u>3,067</u>	<u>3,213</u>
<b>Income Before Income Taxes</b> .....	<u>254</u>	<u>172</u>	<u>1,192</u>	<u>1,329</u>
<b>Provision (Benefit) for Income Taxes</b>				
Current .....	71	41	336	404
Deferred .....	(4)	1	1	(5)
Total provision for income taxes .....	<u>67</u>	<u>42</u>	<u>337</u>	<u>399</u>
<b>Net Income</b> .....	<u>\$ 187</u>	<u>\$ 130</u>	<u>\$ 855</u>	<u>\$ 930</u>
<b>Per Common Share</b>				
Net income-basic .....	\$ 1.12	\$ 0.75	\$ 5.01	\$ 5.36
Net income-diluted .....	\$ 1.11	\$ 0.75	\$ 4.97	\$ 5.30

## Other News Releases

### Cincinnati Financial Corporation Increases Cash Dividend

- Sets stage for 48<sup>th</sup> consecutive year of higher dividends with 9.9% increase in indicated annual dividend rate

Cincinnati, February 4, 2008 – Cincinnati Financial Corporation (Nasdaq: CINF) today announced that the board of directors voted at its regular meeting on February 1, 2008, to increase the regular quarterly cash dividend 9.9 percent to 39 cents per share, payable April 15, 2008, to shareholders of record on March 21, 2008. At the new level, the indicated annual dividend is \$1.56 per share. Cash dividends declared in 2007 were \$1.42 per share.

Chairman and Chief Executive Officer John J. Schiff, Jr., CPCU, commented, “For 48 consecutive years, the board has rewarded our shareholders by increasing the cash dividend. This consistency places Cincinnati Financial in the top tier of U.S. dividend-paying companies, with a long, uninterrupted history of increases that can be claimed by only 10 other companies. We are thankful for the loyalty of our shareholders and policyholders and the efforts of our agents and associates, which together have supported our mutual prosperity.”

# Cincinnati Financial Corporation and Subsidiaries Announce Appointments

## • *Subsidiary Director, Officers and Counsel*

**Cincinnati, February 4, 2008 - Cincinnati Financial Corporation (Nasdaq:CINF)** announced today that its board and boards of its subsidiary companies appointed officers, counsel and a subsidiary director at their regular meetings on February 1, 2008.

For the company and its three standard market property casualty insurance subsidiaries, Donald J. Doyle, Jr., Martin F. Hollenbeck and Charles P. Stoneburner II were named executive officers. For the standard market subsidiaries, Stoneburner additionally was promoted to senior vice president. For the excess and surplus lines subsidiary, Doyle additionally was named executive officer. Hollenbeck additionally was named executive officer for The Cincinnati Life Insurance Company; president and chief operating officer of CFC Investment Company; and president and member of the board of directors of CinFin Capital Management Company.

Boards of subsidiary companies made the following promotions and new or additional appointments of officers and counsel:

### **Property Casualty Insurance – Standard Market Subsidiaries:**

#### **The Cincinnati Insurance Company**

#### **The Cincinnati Casualty Company**

#### **The Cincinnati Indemnity Company**

Charles P. Stoneburner II, CPCU, AIM, Senior Vice President –  
Field Claims

Teresa C. Cracas, Counsel and Vice President – Planning & Risk  
Management

Martin F. Hollenbeck, CFA, CPCU, Vice President and Manager  
– Investments

David E. McKinney, CPCU, AIM, Vice President –  
Commercial Lines

Michael K. O'Connor, CFA, CPCU, AFSB, Vice President –  
Investments

Paul W. Wells, Vice President – Bond & Executive Risk

Ted W. Doughman, CPCU, AFSB, RPLU, Assistant Vice  
President – Bond & Executive Risk

Anthony W. Dunn, CPA, CPCU, CIA, Assistant Vice President –  
Internal Audit

Philip T. Kramer, CIC, Assistant Vice President – Sales &  
Marketing

Jerry L. Litton, Assistant Vice President – Corporate Accounting

Gregory J. Schloemer, Assistant Vice President – Bond &  
Executive Risk

Charlotte A. Tungate, CPCU, AIC, Assistant Vice President –  
Headquarters Claims

Matthew A. Zimmerman, Assistant Vice President – Commercial  
Lines

C. Duane Cantrell, CPCU, AIC, Secretary – Machinery &  
Equipment Specialties

Karen L. Hock, Secretary – Meetings & Travel

Jack D. Kelley, CPCU, AIC, Secretary – Field Claims

Michelle L. Kyle, Secretary – Information Technology

Dennis E. McDaniel, CPA, CMA, CFM, CPCU, Secretary –  
Planning & Risk Management

David V. Neville, CPCU, AIM, API, ARe, Secretary –  
Personal Lines

Janet L. Partin, Secretary – Premium Audit

David A. Rice, SCLA, Secretary – Field Claims

Henry C. Schmidt III, AIM, Secretary – Personal Lines

Blake D. Slater, Secretary – Corporate Accounting

Stephen M. Spray, Secretary – Excess & Surplus Lines

Brent A. Hardesty III, CPCU, CISA, CIA, AIAF, Assistant  
Secretary – Internal Audit

Michael D. Hingsbergen, PMP, Assistant Secretary – Information  
Technology

Troy M. Reichers, Assistant Secretary – Headquarters Claims

James R. Richards, CPCU, AIC, Assistant Secretary –  
Headquarters Claims

Brett J. Starr, CISA, Assistant Treasurer – Financial Reporting &  
Systems Development

Keith W. Collett, Associate Counsel

### **Property Casualty Insurance – Excess & Surplus Lines Subsidiary:**

#### **The Cincinnati Specialty Underwriters Insurance Company:**

Stephen M. Spray\*

Scott E. Hintze, CPCU, AIM, CIC, AU, Assistant Secretary –  
Excess & Surplus Lines

Marc J. Schambow, CPCU, AIM, Assistant Secretary –  
Excess & Surplus Lines

#### **The Cincinnati Life Insurance Company:**

Martin F. Hollenbeck\*

Teresa C. Cracas\*

Michael K. O'Connor\*

Anthony W. Dunn\*

Ann S. Binzer, FLHC, CLU, ChFC, FALU, FLMI, Secretary –  
Life & Health Claims

Michelle L. Kyle\*

Dennis E. McDaniel\*

Kevin C. Smith, Secretary – Corporate Accounting

Brent A. Hardesty III\*

Michael D. Hingsbergen\*

Keith W. Collett\*

#### **Financial Services Subsidiaries:**

##### **CinFin Capital Management Company**

Martin F. Hollenbeck, CFA, CPCU, President

##### **CFC Investment Company**

Martin F. Hollenbeck, CFA, CPCU, President and Chief  
Operating Officer

Blake D. Slater\*

\* Title as listed in first reference



## Cincinnati Specialty Underwriters Issues Its First Excess and Surplus Lines Policies

- Expands business insurance product portfolio for agencies of The Cincinnati Insurance Company
- Earns initial financial strength rating of A (Excellent) from A.M. Best Co.

**CINCINNATI, January 21, 2008** – The Cincinnati Insurance Company today announced that its newest subsidiary, The Cincinnati Specialty Underwriters Insurance Company, now is accepting excess and surplus lines business. Executives highlighted Cincinnati's entry into the E&S market at a sales meeting with its independent agents in Charlottesville, Virginia, the first stop in their annual tour of 25 cities across Cincinnati's operating territories.

Cincinnati's independent agencies in Georgia, Illinois, Indiana, Ohio and Wisconsin now have access to CSU's product line through CSU Producer Resources, Inc., the new, wholly owned insurance brokerage subsidiary of parent-company Cincinnati Financial Corporation. CSU and C-SUPR will expand into additional states where Cincinnati currently offers standard market property casualty policies, including Virginia, as the new companies obtain the necessary state regulatory approvals.

Preparations for E&S operations concluded on schedule in December, when CSU received an A (Excellent) rating from A.M. Best Co., an independent provider of insurer ratings, and successfully issued its first policies from its new policy administration system.

James E. Benoski, president and chief executive officer of The Cincinnati Insurance Company, commented, "Our mission is to help our independent insurance agencies protect the businesses and people in their communities with quality insurance programs. The decision to offer E&S coverage grows from that mission. We specifically structured our E&S operations to serve the needs of the independent agencies that currently market our standard market insurance policies. When part of

their client's insurance program requires E&S coverages, those agencies now can write the whole account with Cincinnati, gaining benefits not often found in the broader E&S market."

Don J. Doyle, Jr., CPCU, AIM, senior vice president, noted, "Producers can submit risks to C-SUPR from a variety of classes, reflecting the mix of accounts Cincinnati agencies currently write. They have direct access to our dedicated E&S underwriters, and they also can tap into their agencies' broader Cincinnati relationships to bring their policyholders services such as experienced and responsive loss control and claims handling.

"We're making it easy to do business. Our new policy administration system delivers electronic copies of policies to producers within minutes of underwriting approval and policy issue. C-SUPR gives extra support to our producers by remitting surplus lines taxes and stamping fees and retaining admitted market declinations."

Benoski added, "We capitalized CSU with \$200 million from its parent company, Cincinnati Insurance. That high level of funding underscores our commitment to help our independent agencies grow by partnering with a carrier they can depend on. Everything we do to increase their competitive advantages and success also helps us achieve our own long term growth and profitability goals."

CSU and C-SUPR were both incorporated in August 2007 to expand Cincinnati's property casualty group's products to include E&S insurance. Generally, E&S provides coverage for businesses that do not find it in the standard market due to market conditions, the nature of the insured business or its specific characteristics and history.

## Inside Cincinnati

In addition to the officer promotions and appointments, these associates merited promotions since our last *Letter to Shareholders*:

Carrie Albanese – Chief Underwriting Specialist  
Brian Archdeacon – P&C Actuary  
Aaron Austin – Senior Underwriter  
Mark Averitt – Senior Claims Representative  
Brent Bailey – Claims Specialist  
Jennifer Baker, CPCU, AIM, ARM, AU – Senior Underwriting Manager  
Jeff Ball – Senior Underwriting Superintendent Field  
John Barnett, CPCU, CIC – Field Director  
Robert Beamon – Senior Claims Representative  
Regina Bobie – Underwriting Superintendent  
Jesse Boehnen, AIC – Senior Claims Specialist  
Gary Boyer, CSP – Loss Control Field Director  
Chris Broglin – Claims Specialist  
Jennifer Byrne – Underwriting Superintendent  
Mindy Carter – Specialist, IT Project & Request Management  
Al Cartwright – Supervisor, Headquarters Claims

Kelly Childress – Claims Specialist  
Vicky Clough – Associate Programmer  
Teresa Cogar – Senior Internal Auditor  
Mickey Cox – Supervisor, Special Investigations Field  
Mike Cozad – Underwriting Specialist  
Linda Craine – Claims Specialist  
Brian Crawford, AIC – Claims Specialist  
Charles Cutter – Senior Field Underwriter  
Michele Defossett – Associate Programmer  
Melissa Donovan – Claims Specialist  
Gary Douty – Senior Claims Representative  
Jason Engel, API – Senior Underwriter  
Andrea Fitzharris – Senior Underwriter  
Greg Foster – Senior Group Manager  
Heather Gabriel, CPCU, AIS, API – Underwriting Specialist  
Cindy Gallaher – Claims Specialist  
Sarah Girten, API – Senior Underwriter

Diana Godsey, AIS, API – Underwriting Specialist  
 Jon Golding, AIC – Field Claims Superintendent  
 Tim Gottsch – Senior Machinery & Equipment Specialist  
 Bill Gregory, SCLA – Assistant Property Claims Manager  
 Joseph Haas, CPCU, AIM, API – Underwriting Specialist  
 Curtis Harrop, AIC – Claims Specialist  
 Joe Harter, AIS – Senior Analyst  
 Ed Hehn, AFSB – Underwriting Director, Bond Field  
 Mark Hertzfeldt, ARM – Loss Control Field Director  
 Tara Hibbard, API – Senior Underwriter  
 John Homan, AIC – Senior Claims Specialist  
 Phil Howard – Senior Regional Director  
 Jeff Kirk, CPCU – Underwriting Manager  
 Jim Knapp – Senior Tax Accountant  
 Denise Kovac – Systems Quality Assurance Manager  
 Tom Krieghoff – Underwriting Specialist  
 John Kucia – Underwriting Specialist  
 Wes Lewis – Underwriting Superintendent  
 Connie Mangrum – Chief Underwriting Specialist  
 Robert Markham – Division Manager  
 Diane Martin, AIC AIS – Senior Claims Specialist  
 Morris Mayo – Claims Specialist  
 David McDaniel, AIC, AIM – Regional Field Claims Manager  
 Kim Meinberg, CPCU – Underwriting Specialist  
 Stephanie Miller – Senior Underwriter  
 Nathan Miller – P&C Actuarial Analyst  
 Doug Mundt, AIC, AIM, ARM – Senior Loss Control Consultant  
 Brian Nagel – Senior Group Manager  
 Tracey Nagle – Senior Systems Analyst  
 Sarah Nally – Underwriting Specialist  
 Kevin Niswonger, AIC – Claims Specialist  
 Cindy Noll – Senior Systems Analyst  
 John O'Brien – P&C Actuarial Analyst

Marc Olsen – Senior Programmer Analyst  
 Patty Patrick – Business Analyst  
 Pat Peters, CSP – Loss Control Field Director  
 Karen Power, API – Requirements Specialist  
 Clint Puskarich, AIC, CPCU – Senior Claims Specialist  
 Tedd Ritchie, CPCU, AIC, AIM, CLU, SCLA – Regional Field  
 Claims Manager  
 Jeffrey Roberts, AIC – Senior Group Manager  
 Ryan Rooks – Group Manager  
 Angie Rose – Senior Underwriter  
 Teresa Rose, FLMI – Underwriter  
 Karl Runkle, AIM, CPCU – Underwriting Director  
 Tom Ryder, CIC – Senior Regional Director  
 Bob Schneider, AIT – Programmer Analyst  
 Brent Showalter, AIC – Senior Claims Specialist  
 Chris Sliga, AIC, AIM – Field Claims Manager  
 Sharon Snow, AIM – Senior Underwriter  
 Lynn Stahr, PMP – Senior Project Manager  
 Leslie Stephens – Senior Underwriter  
 Susanne Stewart, CPCU, API – Manager, Personal Lines  
 Craig Stutzman, AIC – Senior Claims Specialist  
 Tim Taylor – Senior Claims Specialist  
 Nancy Tebbe, CPCU, API – Manager, Personal Lines  
 Ryan Thomas – Lead Network Analyst  
 Brian Toohig – Senior Claims Specialist  
 Julie Urich, AIC – Claims Specialist  
 Jim Vermeesch, CFE – Associate Superintendent, Special  
 Investigations Field  
 David Webb – Senior Claims Specialist  
 Tina Williams – Associate Project Manager  
 Danielle Willman – Senior Underwriter  
 Jennifer Zepf – Senior Analyst  
 Shelly Zorb – Manager, Accounting & Agency Services

## Professional Development

Cincinnati offers independent agents many benefits for doing business with our company. One of those advantages is the opportunity for agents and their staff to attend classroom courses, online training and interactive Web conferences. They may enroll through our Agency Learning Center to study topics ranging from software skills to customer service and Cincinnati product advantages. We work with agencies to develop curricula for their customer services representatives and producers and maintain transcripts that help track each individual's progress. Reducing the agency's training burden is a valuable service. To ensure that agencies are fully aware of the broad range of support available to them, we are showcasing the Agency

Learning Center at this year's annual sales meetings in 25 cities.

We encourage and reward associates who continue their professional insurance education, earning credentials by meeting high academic, ethical and length-of-experience standards. Congratulations to Laura Gibson, Sean Givler and William Ray, who recently completed a series of courses to earn the Certified Insurance Counselor (CIC) designation.

The ABC Award recognizes exemplary productivity, service and quality in exceptional associates. The ABC Award committee recently granted the quarterly Above and Beyond the Call (ABC) award to Jeff Becraft, Printing, and Holly Crowley, AIS, CPCU, Commercial Lines. Congratulations to these quarterly winners!

## Financial Services

The company's two financial services subsidiaries continue to successfully leverage our insurance relationships and broaden our offerings. As of December 31, 2007, CFC Investment Company, which offers equipment and vehicle leases and loans, reported 2,590 accounts representing \$92 million of contract

receivables. CinFin Capital Management Company, which offers asset management services, reported \$944 million under management in 62 accounts.

# Safe Harbor

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 2006 Annual Report on Form 10-K, Item 1A, Risk Factors, Page 20. Although we often review or update our forward-looking statements when events warrant, we caution our readers that we undertake no obligation to do so. 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
  - Inaccurate estimates or assumptions used for critical accounting estimates
  - 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
  - Changing consumer buying habits and consolidation of independent insurance agencies that could alter our competitive advantages
  - 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:
    - Downgrade of the company’s financial strength ratings
    - Concerns that doing business with the company is too difficult or
    - Perceptions that the company’s level of service, particularly claims service, is no longer a distinguishing characteristic in the marketplace
  - Sustained decline in overall stock market values negatively affecting the company’s equity portfolio and book value; in particular a sustained decline in the market value of Fifth Third shares, a significant equity holding
  - Securities laws that could limit the manner and timing of our investment transactions
  - Recession or other economic conditions or regulatory, accounting or tax changes resulting in lower demand for insurance products
  - Events, such as the sub-prime mortgage lending crisis, that lead to a significant decline in the value of a particular security or group of securities, such as our financial sector holdings, and impairment of the asset(s)
  - 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
  - Delays or inadequacies in the development, implementation, performance and benefits of technology projects and enhancements
  - Ability to obtain adequate reinsurance on acceptable terms, amount of reinsurance purchased, financial strength of reinsurers and the potential for non-payment or delay in payment by reinsurers
  - Increased competition that could result in a significant reduction in the company’s premium growth rate
  - Underwriting and pricing methods adopted by competitors that could allow them to identify and flexibly price risks, which could decrease our competitive advantages
  - Personal lines pricing and loss trends that lead management to conclude that this segment could not attain sustainable profitability, which could prevent the capitalization of policy acquisition costs
  - Actions of insurance departments, state attorneys general or other regulatory agencies that:
    - Restrict our ability to exit or reduce writings of unprofitable coverages or lines of business
    - Place the insurance industry under greater regulatory scrutiny or result in new statutes, rules and regulations
    - Increase our expenses
    - 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
    - Limit our ability to set fair, adequate and reasonable rates
    - Place us at a disadvantage in the marketplace or
    - Restrict our ability to execute our business model, including the way we compensate agents
  - Adverse outcomes from litigation or administrative proceedings
  - Investment activities or market value fluctuations that trigger restrictions applicable to the parent company under the Investment Company Act of 1940
  - Events, such as an epidemic, natural catastrophe, terrorism or construction delays, 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, 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 recent measures affecting corporate financial reporting and governance. The ultimate changes and eventual effects, if any, of these initiatives are uncertain.

## Electronic Delivery

Cincinnati Financial Corporation is pleased to offer the convenience of electronic delivery of shareholder communication, including annual reports, interim letters to shareholders and proxy statements – even proxy voting online. With your consent and at no cost to you, we can notify you by e-mail when these materials become available on the Internet at [www.cinfin.com](http://www.cinfin.com).

### Electronic delivery benefits you and your company:

- **Immediate availability** – Immediate availability of important information – no more waiting for the mail to arrive.
- **Less clutter** – The average consumer is receiving more mail today than ever, making it easy to miss important information.
- **Cost savings** – Electronic delivery saves money for Cincinnati Financial – your company.

### Plus, it's better for the environment.

You can benefit from electronic delivery whether you directly hold registered shares or hold your investments through a participating brokerage/financial institution. You will need to provide an e-mail address, account number(s) and the last four digits of the Social Security number of the account holder. If you provide this information, you can give your consent for electronic delivery immediately. While you may cancel your consent for electronic delivery at any time, we are confident that you will find this option an efficient and effective way to receive important information about your investment.

To enroll, select Electronic Delivery from the Investors page of [www.cinfin.com](http://www.cinfin.com). If you hold multiple accounts directly or through a broker, you will need to enroll each account separately – including joint tenant and custodial accounts – to stop paper mailings.

**Enroll Today**

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## Contact Information

Communications directed to the company's secretary, Kenneth W. Stecher, chief financial officer and executive vice president, are shared with the appropriate individual(s). Or, you may directly access services:

**Investors:** Investor Relations responds to investor inquiries about Cincinnati Financial Corporation and its performance.  
Heather J. Wietzel – Vice President, Investor Relations  
513-870-2768 or [investor\\_inquiries@cinfin.com](mailto:investor_inquiries@cinfin.com)

**Shareholders:** Shareholder Services provides stock transfer services, fulfills requests for shareholder materials and assists registered shareholders who wish to update account information or enroll in shareholder plans.  
Jerry L. Litton – Assistant Vice President, Shareholder Services  
513-870-2639 or [shareholder\\_inquiries@cinfin.com](mailto:shareholder_inquiries@cinfin.com)

**Media:** Corporate Communications assists media representatives seeking information or comment from Cincinnati Financial Corporation or its subsidiaries.  
Joan O. Shevchik, CPCU, CLU – Senior Vice President, Corporate Communications  
513-603-5323 or [media\\_inquiries@cinfin.com](mailto:media_inquiries@cinfin.com)

### Cincinnati Financial Corporation

The Cincinnati Insurance Company  
The Cincinnati Casualty Company  
The Cincinnati Indemnity Company  
The Cincinnati Specialty Underwriters Insurance Company

The Cincinnati Life Insurance Company  
CSU Producer Resources Inc.  
CFC Investment Company  
CinFin Capital Management Company

### Mailing Address:

P.O. Box 145496  
Cincinnati, Ohio 45250-5496

Phone: 513-870-2000  
Fax: 513-870-2066  
[www.cinfin.com](http://www.cinfin.com)

### Street Address:

6200 South Gilmore Road  
Fairfield, Ohio 45014-5141