

## Cincinnati Financial Corp.

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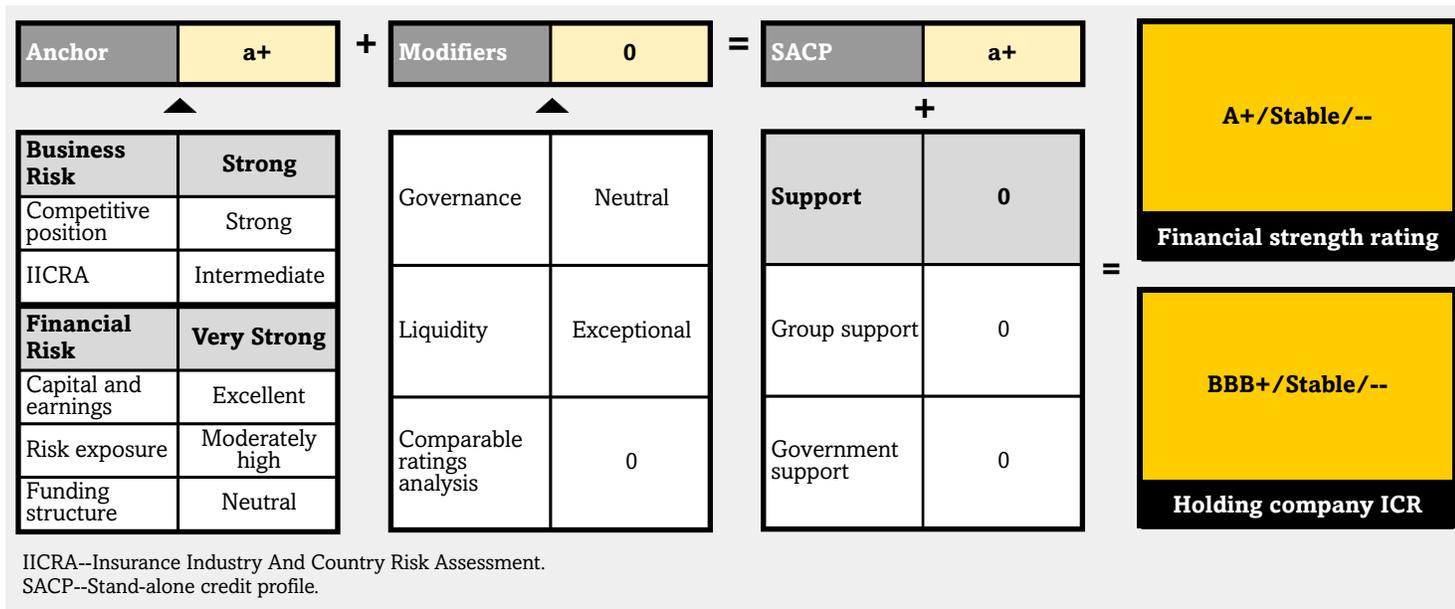
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# Cincinnati Financial Corp.



## Credit Highlights

Overview	
Key strengths	Key risks
Extremely strong capital adequacy with a significant buffer at the 'AAA' level, low financial leverage, and exceptional liquidity	Susceptible to earnings volatility due to high allocation of investment portfolio to equity investments
Strong and consistent underwriting margins	Geographic concentration, though shrinking, in the Midwest
Agent-centric business model and profit-driven commission structure	

**Cincinnati Financial continues to diversify risk geographically and by product line.** Cincinnati Re, Cincinnati Global, and its excess and surplus (E&S) lines businesses are gradually representing more of the consolidated results. Additionally, the group continues to diversify risk, which has reduced geographic concentration in the Midwest and Southeast regions, thus lessening volatility from weather-related losses.

**The group has robust capital to absorb asset-risk shock amid rising interest rates and stock market volatility.**

Cincinnati Financial Corp. (CFC) and its subsidiaries' (collectively, Cincinnati Financial) capital position has historically been a strength to the rating. While unrealized losses from rising interest rates and stock market volatility pressure capital in the near term, we expect Cincinnati Financial to maintain a strong buffer at the 'AAA' level through our three-year forecast horizon. The group is subject to earnings volatility because of the higher allocation to equity investments than peers, but we expect Cincinnati Financial's operating earnings generation will continue to support the company's maintenance of capital adequacy commensurate with the rating.

**The combination of a strong business risk profile and very strong financial risk profile leads to a split anchor of 'a+'/'a'.** We select the higher anchor based on CFC's commitment to 'AAA' capital, strong operating performance that is in line with 'A+' rated peers, and strength of distribution.

**Outlook: Stable**

The stable outlook reflects our expectation that Cincinnati Financial will maintain excellent capital per our risk-based capital model, produce stable and profitable operating results, and improve risk diversification.

**Downside scenario**

Although it is unlikely, we could lower our ratings over the next 24 months if capital adequacy deteriorates below the excellent level and we believe the company will not be able to improve its capital position. We could also lower the ratings if operating performance weakens significantly and we expect that improvement is unlikely.

**Upside scenario**

We could raise our ratings if the group demonstrates consistent profitability while continuing with product and geographic diversification through Cincinnati Global, reinsurance, life, and E&S businesses and maintaining excellent capital adequacy.

**Assumptions**

- Real U.S. GDP growth of 1.7% in 2023 and 1.3% in 2024
- 10-year Treasury rate of about 3.7% in 2023 and 3.6% 2024
- Core Consumer Price Index increase of 5.0% in 2023 and 3.3% in 2024
- Unemployment rate at 3.5% in 2023 and 4.0% in 2024
- Negative sector outlook for property/casualty (P/C) insurers

Source: "Economic Outlook U.S. Q3 2023: A Sticky Slowdown Means Higher For Longer," June 26, 2023

**Key metrics**

<b>Cincinnati Financial key metrics</b>						
<b>(Mil. \$)</b>	<b>2024f</b>	<b>2023f</b>	<b>2022</b>	<b>2021</b>	<b>2020</b>	<b>2019</b>
Net premiums earned	8,000-8,500	7,750-8,000	7,219.0	6,482.0	5,980.0	5,604.0
EBITDA fixed-charge coverage (x)	18-20	18-20	17.81	26.23	14.17	17.87
Financial leverage (%)	6-8	6-8	7.82	6.41	7.89	7.74
Return on equity (%)	5-10	0-2	-4.11	24.66	11.78	22.57
P/C: Net combined ratio (%)	94-96	96-98	98.12	88.34	98.07	93.81
Return on revenue excluding investment gains/losses (%)	12-14	10-12	10.31	18.21	10.32	13.95
S&P Global Ratings' capital adequacy	AAA	AAA	AA	AAA	AAA	AAA

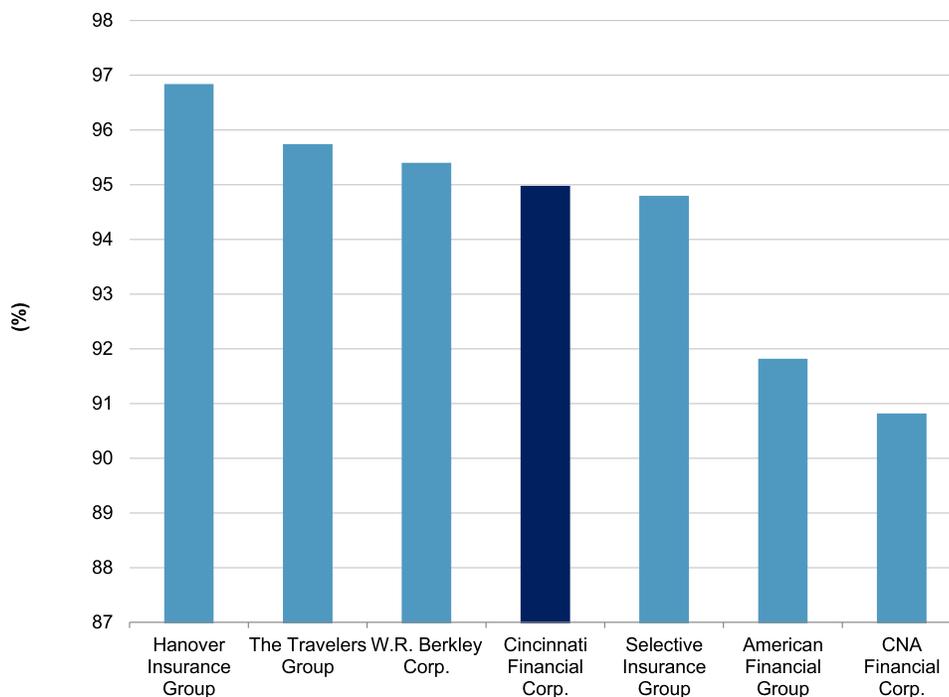
f--Forecast.

## Business Risk Profile: Strong

Cincinnati Financial has built its business around a low fixed-cost expense structure and a competitive, profit-driven agent commission structure, with 1,984 P/C agency relationships as of year-end 2022. The group has a strong and growing network of independent agents who are supported by local field representatives to help with underwriting, claims, production, and loss control. The independent agents are carefully selected to ensure business growth is profitable and in line with the company's expectations and objectives.

### Chart 1

#### Combined ratio peer comparison (2018-2022)



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At year-end 2022, net premiums written (NPW) totaled \$7.6 billion, represented by:

- Commercial lines (54% of NPW),
- Personal lines (24% of NPW),
- Reinsurance via Cincinnati Re (8% of NPW),
- E&S lines (7% of NPW),
- Life insurance (4% of NPW), and

- Cincinnati Global (3% of NPW).

The company continues to steadily diversify the P/C business, but concentrations in the Midwest and Southeast remain and expose the company to both catastrophe and noncatastrophe convective storm losses, as evidenced by a consolidated P/C combined ratio of 100.7% with 13.8 points owing to catastrophes through the first quarter of 2023. However, the group has proved it can manage these risks without significant volatility in underwriting performance, with a five-year average (2018-2022) combined ratio of 94.9%.

The group's \$4.2 billion commercial lines book has historically produced strong underwriting margins and has anchored underwriting performance with a five-year average combined ratio of 93.9%. The book has an emphasis on small to midsize businesses and continues to grow. We expect management to maintain adept risk selection and exposure management in this segment.

Cincinnati Financial's \$1.8 billion personal lines book finished year-end 2022 with a combined ratio of 99.2%, despite industrywide pressures on the segment from rising severity, catastrophe losses, and persistent inflation. Management has focused on the use of technology to improve risk selection and geographic diversification in recent years, which has proved successful. The group has also earned its spot as one of the top players in the high-net-worth space and continues to grow, with \$919 million of high-net-worth NPW in 2022.

Earnings are further diversified through the E&S, reinsurance, Cincinnati Global, and life insurance businesses:

- The growing E&S book focuses on casualty business and has been a strong source of earnings, with a five-year average combined ratio of 85.0%.
- Cincinnati Re began in 2015 and continues to grow, finishing 2022 with \$585 million of NPW.
- Cincinnati Global, acquired in February 2019, underwrites insurance in the Lloyd's of London marketplace and generated \$230 million of NPW in 2022.
- The Cincinnati Life Insurance Co. offers primarily term life and annuity products and remains a steady source of operating income for the group.

These segments continue to expand, represent more of the consolidated results, and diversify earnings.

## **Financial Risk Profile: Very Strong**

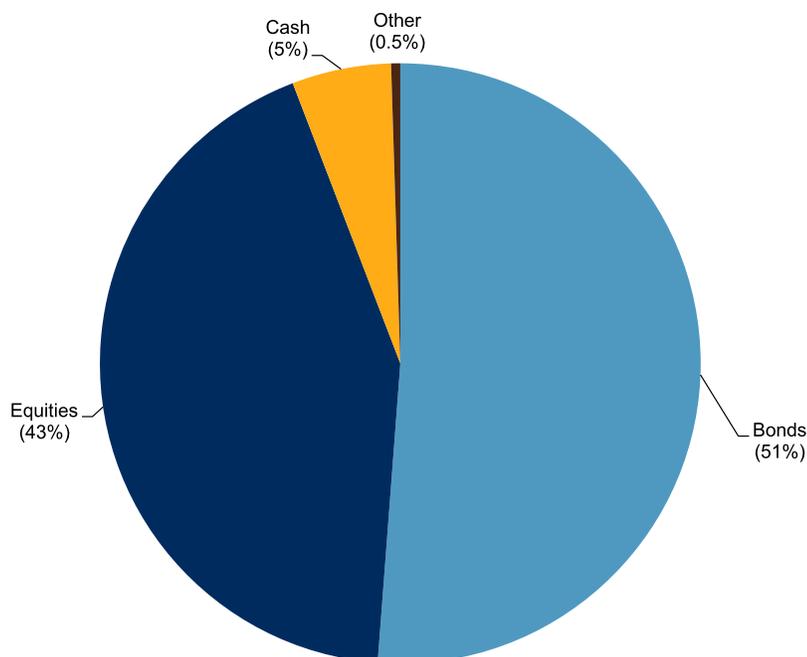
Cincinnati Financial's strong underwriting margins and consistent investment income support its capital and earnings. The group also has historically maintained relatively low leverage and excellent liquidity. CFC's shareholders' equity in 2022 declined to \$10.5 billion from \$13.1 billion, primarily due to significant unrealized and realized losses from its investment portfolio on account of increasing interest rates.

As of year-end 2022, CFC's \$23.7 billion investment portfolio had material exposure to common equities, at about 42% of invested assets. The portfolio is 51% bonds, 5% cash and short-term investments, and about 2.0% real estate, loans, and other investments. While the equity portfolio consists of high-quality, dividend-paying stocks, we recognize the

potential for earnings volatility due to equity market swings. Volatile market conditions and increasing rates in 2022 led CFC's fixed-income and equity portfolios to report net unrealized losses of about \$1.64 billion and \$1.51 billion, respectively. In the first quarter of 2023, however, total investment gains were \$269 million, reflecting a reversal of some of the losses on equity and fixed-income securities. We think the group is able to comfortably withstand the risk associated with its investment allocation due to the sizable buffer at the 'AAA' level per our capital model.

## Chart 2

### Cincinnati Financial investment portfolio



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## Other Key Credit Considerations

### Governance

Management enhances financial and operational performance by focusing on capital stability, agency relationships, small-to-midsize accounts, underwriting discipline, and an investment strategy aligned to support earnings in a soft market cycle. The group has a record of achieving its operational and strategic goals.

Its business model depends on a strong network of carefully selected independent agents to serve local businesses and customers. Management enhances operational performance by providing resources to and remaining engaged with agents. It maintains a low fixed expense ratio, which enables the group to offer higher commissions and attract more profitable business than competitors.

## Liquidity

We consider CFC's liquidity to be exceptional because of its strong operating cash flow and liquid investment portfolio. CFC finished 2022 with \$2.052 billion in operating cash flow, and it had \$250 million through the first quarter of 2023.

## Factors specific to the holding company

Our rating on the holding company reflects its structural subordination to its regulated operating subsidiaries. CFC's operating performance and debt service needs depend on the operating subsidiaries' ability to pay dividends.

## Environmental, social, and governance

### ESG Credit Indicators

E-1	E-2	<b>E-3</b>	E-4	E-5	S-1	<b>S-2</b>	S-3	S-4	S-5	G-1	<b>G-2</b>	G-3	G-4	G-5
- Physical risks					- N/A					- N/A				

N/A—Not applicable. ESG credit indicators provide additional disclosure and transparency at the entity level and reflect S&P Global Ratings' opinion of the influence that environmental, social, and governance factors have on our credit rating analysis. They are not a sustainability rating or an S&P Global Ratings ESG Evaluation. The extent of the influence of these factors is reflected on an alphanumerical 1-5 scale where 1 = positive, 2 = neutral, 3 = moderately negative, 4 = negative, and 5 = very negative. For more information, see our commentary "ESG Credit Indicator Definitions And Applications," published Oct. 13, 2021.

Environmental factors are a moderately negative consideration in our credit rating analysis of Cincinnati Financial. The majority of catastrophe losses in recent years were attributable to convective storms in the Midwest, but despite a higher frequency of catastrophe losses, the company had lower loss severity than its peers with more coastal exposure. While historically, catastrophe losses have been relatively material to earnings, the company has established a culture focused on risk management and improved its ability to quantify exposures and tolerances.

## Accounting considerations

Cincinnati Financial is a publicly traded company and timely prepares its financial statements under both generally accepted accounting principles (GAAP) and statutory accounting principles. We consider GAAP statements when examining the capital, earnings, and other financial metrics relative to peers'.

## Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010

### Business And Financial Risk Matrix

Business risk profile	Financial risk profile							
	Excellent	Very Strong	Strong	Satisfactory	Fair	Marginal	Weak	Vulnerable
Excellent	aa+	aa	aa-	a+	a-	bbb	bb+	b+
Very Strong	aa	aa/aa-	aa-/a+	a+/a	a-/bbb+	bbb/bbb-	bb+/bb	b+
<b>Strong</b>	aa-/a+	<b>a+/a</b>	a/a-	a-/bbb+	bbb+/bbb	bbb-/bbb	bb-/bb+	b+/b
Satisfactory	a	a/a-	a-/bbb+	bbb+/bbb	bbb-/bbb-	bb+/bb	bb-/b+	b/b-
Fair	a-	a-/bbb+	bbb+/bbb	bbb/bbb-	bbb-/bb+	bb/bb-	b+/b	b-
Weak	bbb+/bbb	bbb/bbb-	bbb-/bb+	bb+/bb	bb/bb-	bb-/b+	b/b-	b-
Vulnerable	bbb-/bb+	bb+/bb	bb/bb-	bb-/b+	b+/b	b/b-	b-	b-

**Note:** Where table indicates two possible outcomes, we determine the anchor as follows: For financial risk profiles that we assess as satisfactory or stronger, we consider the relative strength of both the business risk and financial risk profiles within the cell. This is based on a holistic assessment of the relative strengths of the rating factors of the business risk profile and financial risk profile. For financial risk profiles that we assess as fair or weaker, we typically place more weight on the relative strength of the rating factors of the financial risk profile.

### Ratings Detail (As Of June 29, 2023)\*

#### Cincinnati Financial Corp.

Issuer Credit Rating

*Local Currency*

BBB+/Stable/--

Senior Unsecured

BBB+

#### Related Entities

##### Cincinnati Casualty Co.

Financial Strength Rating

*Local Currency*

A+/Stable/--

Issuer Credit Rating

*Local Currency*

A+/Stable/--

##### Cincinnati Indemnity Co.

Financial Strength Rating

*Local Currency*

A+/Stable/--

Issuer Credit Rating

*Local Currency*

A+/Stable/--

##### Cincinnati Insurance Co.

Financial Strength Rating

*Local Currency*

A+/Stable/--

Issuer Credit Rating

*Local Currency*

A+/Stable/--

##### Cincinnati Life Insurance Co.

Financial Strength Rating

*Local Currency*

A+/Stable/--

Issuer Credit Rating

*Local Currency*

A+/Stable/--

#### Domicile

Ohio

\*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and

**Ratings Detail (As Of June 29, 2023)\*(cont.)**

debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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