

## American Financial(AFG)

**\$111.28** (As of 01/20/20)

Price Target (6-12 Months): **\$117.00**

Long Term: 6-12 Months

**Zacks Recommendation:**

**Neutral**

(Since: 01/30/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

**Zacks Rank:** (1-5)

**3-Hold**

Zacks Style Scores:

VGM:B

Value: A

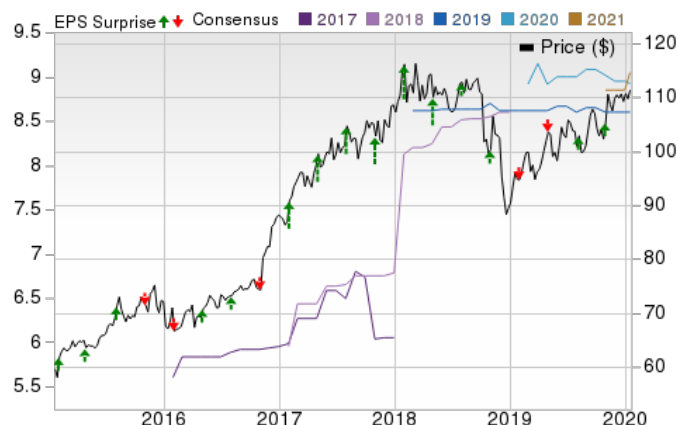
Growth: B

Momentum: D

## Summary

American Financial's shares have outperformed its industry in a year's time. The company is well poised to benefit from impressive inorganic growth and is thus prudently investing in businesses. It is actively involved in startups, small-to-medium sized acquisitions, and product launches. Consistent price increase in property and casualty business should favor results. Better industry fundamentals with strong pricing and a higher renewal ratio should drive growth. A strong balance sheet, low leverage cost and an efficient capital management are tailwinds. However, soft Annuity business continues to weigh on earnings. Also, exposure to weather-related calamities and drought has induced volatility to the earnings of the company.

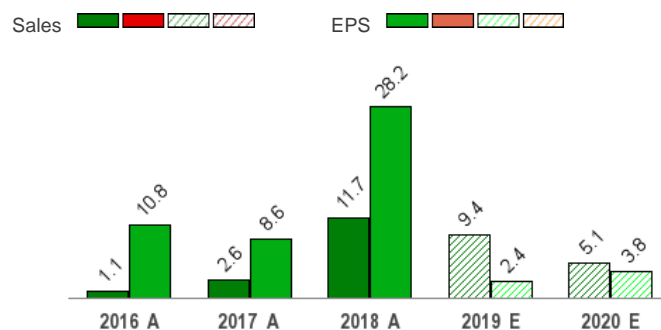
## Price, Consensus & Surprise



## Data Overview

52 Week High-Low	<b>\$111.86 - \$90.20</b>
20 Day Average Volume (sh)	<b>259,493</b>
Market Cap	<b>\$10.0 B</b>
YTD Price Change	<b>1.5%</b>
Beta	<b>0.84</b>
Dividend / Div Yld	<b>\$1.80 / 1.6%</b>
Industry	<b><a href="#">Insurance - Property and Casualty</a></b>
Zacks Industry Rank	<b>Top 22% (57 out of 254)</b>

## Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	<b>15.4%</b>
Last Sales Surprise	<b>NA</b>
EPS F1 Est- 4 week change	<b>0.0%</b>
Expected Report Date	<b>02/03/2020</b>
Earnings ESP	<b>0.0%</b>
P/E TTM	<b>13.7</b>
P/E F1	<b>12.5</b>
PEG F1	<b>2.0</b>
P/S TTM	<b>1.3</b>

## Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020					8,256 E
2019	1,771 A	1,836 A	2,088 A		7,856 E
2018	1,657 A	1,740 A	1,914 A	1,871 A	7,182 A

## EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$2.07 E	\$2.14 E	\$2.09 E	\$2.59 E	\$8.93 E
2019	\$2.02 A	\$2.12 A	\$2.25 A	\$2.21 E	\$8.60 E
2018	\$2.42 A	\$2.04 A	\$2.19 A	\$1.75 A	\$8.40 A

\*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 01/20/2020. The reports text is as of 01/21/2020.

## Overview

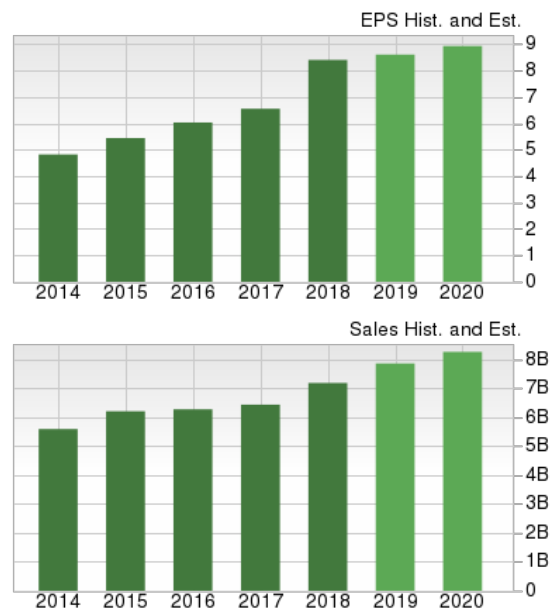
Founded in 1872 and headquartered in Cincinnati, OH, American Financial Group, Inc. is a holding company which, through its subsidiaries, engages primarily in property and casualty insurance, with focus on specialized commercial products for businesses. The company also engages in the sale of traditional fixed, fixed-indexed and variable-indexed annuities in the retail, financial institutions, registered investment advisor and education markets.

American Financial Group reports its earnings in three segments:

**Property and Casualty Insurance Operations** – These operations consist of approximately 30 niche insurance businesses offering a wide range of commercial coverage. The business is conducted through Property and Transportation (consisting Inland and Ocean Marine, Agricultural-related and Commercial Automobile), Specialty Casualty (consisting Executive and Professional Liability, Umbrella and Excess Liability, Excess and Surplus, General Liability, Targeted Programs and Workers' Compensation) and Specialty Financial (consisting Fidelity and Surety and Lease and Loan Services). These operations are conducted through subsidiaries namely Great American Insurance, National Interstate, Summit (Bridgefield Casualty and Bridgefield Employers), Republic Indemnity, Neon Lloyd's Syndicate and Mid-Continent Casualty. These subsidiaries carry strong ratings from AM Best and S&P.

**Annuity Operations** – Annuity operations primarily involve the sale of traditional fixed, fixed-indexed and variable-indexed annuities in the retail, financial institutions, broker-dealer and registered investment advisor markets through independent producers and through direct relationships with certain financial institutions. These operations are conducted primarily through the subsidiaries, Great American Life Insurance Company and Annuity Investors Life Insurance Company.

**Other Operations** – Through subsidiaries, it is engaged in a variety of other operations, including commercial real estate operations in Cincinnati (office buildings), Whitefield, New Hampshire (Mountain View Grand Resort), Chesapeake Bay (Skipjack Cove Yachting Resort and Bay Bridge Marina), Charleston (Charleston Harbor Resort and Marina) and Palm Beach (Sailfish Marina and Resort).



---

## Reasons To Buy:

- ▲ **Share Price Movement:** Shares of American Financial have gained 16% in a year's time, outperforming the industry's increase of 13%. Strategic acquisitions, better pricing, improving industry fundamentals might continue to drive price performance.
- ▲ **Sturdy Growth Profile:** American Financial is actively involved in startups, small-to-medium sized acquisitions, and product launches. It is prudently investing in businesses. The company expects National Interstate to begin issuing policies in the third quarter of 2019 and thus add \$20 million in gross written premium in the second half of 2019.

American Financial, a niche player in the P&C and annuity markets, will benefit from the strategic acquisitions and improved pricing. Improving industry fundamentals will drive overall growth.

Given continued solid operational performance, management now expects Specialty Property and Casualty Group's net written premiums to be up 4-7% compared with the increase of 2-5% guided earlier. Of this, net written premium is expected to increase in the range of 4-8% (up from 3-7% guided earlier) for Property and Transportation Group and 4-7% (compared with 2-6% growth guided earlier) for Specialty Casualty Group. Net written premium is expected to be flat to up 3% compared with the earlier guidance of flat-to-down 4%) for Specialty Financial Group. The company expects 2019 net operating earnings in the range of \$8.50 to \$8.70 per share compared with \$8.40-\$8.80 announced previously.

- ▲ **Consistent Price Increase in Property and Casualty (P&C) Business:** American Financial witnessed renewal pricing increase of more than 3% in the third quarter of 2019 (up from 3% achieved in first half 2019) in Property and Casualty group and 9% in Specialty Casualty Group excluding workers' compensation. The company intends to maintain satisfactory rates in P&C renewal pricing going forward. Management estimates Property and Casualty renewal pricing in 2019 to be up 2% to 4% (up from 1-3% guided earlier). Excluding workers' compensation, the company estimates renewal rate increase to be in the range of 5% to 6%. Along with price increase, projects loss cost trends are expected to remain stable and appear relatively benign across all the P&C lines. These are strong positive trends that should favor the company in the long run.
- ▲ **Improving Investment Income:** The company's net investment income has been improving over the last few quarters and this momentum continued through the first nine months of 2019. Investment income increased 10.2% driven by strong performance of limited partnerships and similar investments. The company expects 2019 investment income to be up 4-7% (up from 2-6% guided earlier).
- ▲ **Favorable Combined Ratio:** American Financial's combined ratio has been better than the industry average over more than two decades. For 2019, the company expects Specialty Property and Casualty Group combined ratio between 93% and 94%, in line with past five-year average. Of this, combined ratio is projected between 93% and 96% for Property and Transportation Group (narrowed down from 93% to 97% guided earlier) and between 92% and 95% (up from 90-94% guided earlier) for Specialty Casualty Group. For Specialty Financial Group, combined ratio is estimated to be in the range of 86% to 89%, a slight improvement from the earlier expectation of 87% to 91%.
- ▲ **Strong Capital Management:** American Financial has traditionally maintained moderate adjusted financial leverage around 20%, with good cash flow and interest coverage ratio. In each of the last 13 years, the company has successfully increased its dividends and paid out special dividend. To this end, in May 2019, the company paid out a special dividend of \$1.50 per share. The robust operating profitability at the P&C segment, a stellar investment performance and an effective capital management have driven the company to deliver five-year total shareholder return, representing growth and share price plus dividends of 88%, outperforming the total return performance of the S&P 500, S&P Property and Casualty Index and the S&P Life & Health Index over the same period. Its dividend strategy reflects its solid financial position.

The company intends to hold back about \$200-\$300 million of the excess capital to maintain flexibility for any opportunity that may arise in the future.

---

## Reasons To Sell:

▼ **Annuity Business:** The company has been witnessing weak performance at this segment over the past quarters. Pre-tax income dropped 14% year over year through the first nine months of 2019. Premiums declined 2.6% year over year in the same time frame. The company implemented several rate decreases to maintain proper returns on annuity sales that have started to affect new sales.

In response to the continued drop in market interest rates in 2019, the company has implemented numerous crediting rate decreases on its products in order to maintain appropriate returns on Annuity sales. The company expects 2019 Annuity sales to be down 9-10% compared with its \$5.4 billion of premiums in 2018. However, pre-tax annuity core operating earnings are expected to increase in the range of \$380 million to \$400 million compared with the earlier guidance range of \$375 million to \$405 million.

▼ **Exposure to Catastrophes:** The company's earnings have traditionally been affected by catastrophes. Even drought, which does not otherwise qualify as a catastrophe, had impacted its earnings, given its exposure to the crop business. In the first nine months of 2019, the company incurred catastrophe loss of \$46 million, down 31.3% year over year. Irrespective of catastrophe mitigation techniques deployed by it, exposure to weather-related calamities makes its earnings volatile.

▼ **Stretched Valuation:** Valuation remains stretched at current level. Price to book value, the multiple for valuing insurers, of 1.59X is higher than the industry average of 1.44X.

---

Underperforming Annuity business weighing on earnings and exposure to cat losses (specifically its exposure to the crop business) inducing volatility to underwriting results pose near-term headwinds.

## Last Earnings Report

### American Financial Q3 Earnings Top Estimates, Rise Y/Y

American Financial Group third-quarter 2019 net operating earnings per share of \$2.25 beat the Zacks Consensus Estimate by 15.3%. Also, the bottom line increased 2.7% year over year.

Higher net premiums written in Specialty Property and Casualty insurance operations were partially offset by lower premiums in Annuity Segment.

#### Behind the Headlines

Total operating revenues of \$2.1 billion rose 9.4% year over year. This top-line improvement can be attributed to higher net investment income and increase in net earned premiums at its Property & Casualty insurance.

Net investment income of \$588 million increased 11.6% year over year.

American Financial's total cost and expenses were \$1.9 billion, up 10.3% year over year. This was due to higher P&C insurance loss and expenses, annuity, life, accident and health benefits, interest charges on borrowed money and expenses plus expenses of managed investment entities as well as other expenses.

#### Segment Results

Specialty Property and Casualty Insurance generated \$1.6 billion in net premiums written, up 11% year over year, driven by increase of 17%, 8% and 6%, respectively, in the Property & Transportation, Specialty Casualty in Specialty Financial.

Core operating earnings were \$194 million in the third quarter, up 22.8% year over year, driven by higher P&C underwriting profit and higher P&C net investment income as a result of higher earnings on limited partnerships and similar investments.

Underwriting profit of \$88 million increased 60% as higher year-over-year underwriting profits in the Property and Transportation and Specialty Financial Groups were partially offset by lower underwriting profit in the Specialty Casualty Group.

The segment's combined ratio improved 170 basis points (bps) year over year to 94%.

Annuity segment's premiums of \$1.1 billion declined 22% year over year, as higher traditional fixed annuity premiums in the financial institutions channel were offset by lower FIA premiums in the retail and broker dealer channels, Pension Risk Transfer, Education Market and Variable Annuities.

Pre-tax income of \$100 million remained unchanged year over year.

#### Financial Update

As of Sep 30, 2019, American Financial had cash and investments of \$54.2 billion, which grew 11.8% from year-end 2018 level.

As of Sep 30, 2019, long-term debt of \$1.4 billion was up 9.3% from 2018 end level.

As of Sep 30, 2019, the company's book value per share (excluding unrealized gains/losses on fixed maturities) was \$59.65, up 8.7% from the figure at 2018 end.

Annualized return on equity was 15.3%, down 50 bps year over year.

#### 2019 Guidance

American Financial expects full-year 2019 pretax Annuity core operating earnings to be in the range of \$380 million to \$400 million. This compares favorably with the previous guidance of \$375 million to \$405 million.

American Financial expects core net operating earnings for 2019 to be in the range of \$8.50 to \$8.70 per share compared with \$8.40-\$8.80 announced previously.

Specialty Casualty net written premiums are expected to grow in the range of 4% to 7%, up from previous guidance of 2-5%. It reported \$5.0 billion in 2018.

Combined ratio for 2019 is expected in the range of 93% to 94% compared with the previous projection of 92-94%.

Quarter Ending **09/2019**

Report Date	<b>Oct 29, 2019</b>
Sales Surprise	<b>NA</b>
EPS Surprise	<b>15.38%</b>
Quarterly EPS	<b>2.25</b>
Annual EPS (TTM)	<b>8.14</b>

## Recent News

### American Financial's Unit to Quit Lloyd's Insurance Market— Jan 6, 2020

American Financial announced that it will no longer be part of the Lloyd's of London insurance market in 2020. To this end, the company commenced the process of putting its Lloyd's subsidiaries including its Lloyd's Managing Agency Neon Underwriting Ltd into a run-off.

### American Financial Announces Quarterly Dividend — Jan 2, 2020

The board of directors of American Financial declared a quarterly dividend of 45 cents per share. The dividend will be paid out on Jan 27 to shareholders of record as of Jan 15.

## Valuation

American Financial shares are up 15.9% over the trailing 12-month period. Over the past year, stocks in the Zacks sub-industry and Zacks Finance sector are up 13% and 11.7%, respectively.

The S&P 500 index is up nearly 23.8% in the past year.

The stock is currently trading at 1.59X trailing 12-month book value, which compares to 1.44X for the Zacks sub-industry, 2.86X for the Zacks sector and 4.55X for the S&P 500 index.

Over the past five years, the stock has traded as high as 2X and as low as 1.01X, with a 5-year median of 1.56X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$117 price target reflects 1.67X trailing 12-month book value.

The table below shows summary valuation data for AFG

Valuation Multiples - AFG					
		Stock	Sub-Industry	Sector	S&P 500
P/B TTM	Current	1.59	1.44	2.86	4.55
	5-Year High	2	1.67	2.89	4.55
	5-Year Low	1.01	1.26	1.83	2.85
	5-Year Median	1.56	1.47	2.51	3.61
P/S F12M	Current	1.86	1.67	6.53	3.57
	5-Year High	2.05	11.26	6.61	3.57
	5-Year Low	1.15	1.55	5.2	2.54
	5-Year Median	1.57	1.92	6.04	3
P/E F12M	Current	12.46	26.9	14.73	19.19
	5-Year High	17.94	31.55	16.21	19.34
	5-Year Low	9.9	22.77	12.01	15.17
	5-Year Median	12.61	25.7	13.98	17.44

As of 01/20/2020

## Industry Analysis Zacks Industry Rank: Top 22% (57 out of 254)



## Top Peers

Market Corporation (MKL)	Outperform
Arch Capital Group Ltd. (ACGL)	Neutral
American International Group, Inc. (AIG)	Neutral
Cincinnati Financial Corporation (CINF)	Neutral
CNA Financial Corporation (CNA)	Neutral
The Hartford Financial Services Group, Inc. (HIG)	Neutral
Everest Re Group, Ltd. (RE)	Neutral
Alleghany Corporation (Y)	Neutral

Industry Comparison Industry: Insurance - Property And Casualty				Industry Peers		
	AFG Neutral	X Industry	S&P 500	MKL Outperform	RE Neutral	Y Neutral
<b>VGM Score</b>	<b>B</b>	-	-	<b>F</b>	<b>B</b>	<b>D</b>
Market Cap	10.03 B	1.99 B	24.65 B	16.47 B	11.42 B	11.75 B
# of Analysts	3	2	13	1	3	2
Dividend Yield	1.62%	0.98%	1.73%	0.00%	2.21%	0.00%
<b>Value Score</b>	<b>A</b>	-	-	<b>D</b>	<b>C</b>	<b>D</b>
Cash/Price	0.28	0.18	0.04	0.30	0.10	0.16
EV/EBITDA	9.50	9.50	14.11	27.25	-65.45	44.95
PEG Ratio	2.03	1.71	2.08	NA	1.17	NA
Price/Book (P/B)	1.58	1.27	3.39	1.55	1.27	1.33
Price/Cash Flow (P/CF)	10.23	13.97	13.81	23.23	51.73	32.72
P/E (F1)	12.41	13.88	19.19	30.29	11.65	17.89
Price/Sales (P/S)	1.29	1.05	2.69	2.06	1.46	1.48
Earnings Yield	8.02%	7.18%	5.21%	3.30%	8.58%	5.59%
Debt/Equity	0.23	0.21	0.72	0.37	0.07	0.19
Cash Flow (\$/share)	10.88	3.05	6.94	51.34	5.41	24.96
<b>Growth Score</b>	<b>B</b>	-	-	<b>F</b>	<b>B</b>	<b>B</b>
Hist. EPS Growth (3-5 yrs)	13.41%	-0.55%	10.56%	-0.95%	-26.70%	-22.88%
Proj. EPS Growth (F1/F0)	3.78%	6.72%	7.57%	-2.17%	5.72%	18.40%
Curr. Cash Flow Growth	39.71%	9.94%	14.73%	174.99%	-47.78%	122.47%
Hist. Cash Flow Growth (3-5 yrs)	13.00%	7.23%	9.00%	10.64%	-27.90%	-13.07%
Current Ratio	0.16	0.44	1.24	0.60	0.35	0.32
Debt/Capital	18.38%	17.79%	42.99%	27.64%	6.59%	17.53%
Net Margin	8.43%	5.34%	11.14%	6.75%	5.30%	1.43%
Return on Equity	12.83%	6.81%	17.16%	5.18%	5.90%	4.36%
Sales/Assets	0.12	0.31	0.55	0.23	0.30	0.31
Proj. Sales Growth (F1/F0)	%	4.75%	4.16%	8.95%	9.80%	NA
<b>Momentum Score</b>	<b>D</b>	-	-	<b>D</b>	<b>B</b>	<b>F</b>
Daily Price Chg	0.53%	0.39%	0.27%	0.86%	0.92%	1.09%
1 Week Price Chg	-0.88%	-0.83%	0.39%	0.07%	-0.87%	-2.07%
4 Week Price Chg	0.52%	1.84%	2.95%	4.47%	1.60%	1.88%
12 Week Price Chg	8.71%	2.52%	7.76%	6.94%	12.14%	6.63%
52 Week Price Chg	16.60%	10.68%	22.29%	12.91%	30.02%	32.29%
20 Day Average Volume	259,493	115,834	1,536,375	31,791	184,314	55,170
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.03%	0.07%	-0.16%
(F1) EPS Est 4 week change	0.00%	0.00%	0.00%	0.03%	-0.21%	-0.16%
(F1) EPS Est 12 week change	-1.47%	-0.42%	-0.40%	2.94%	0.87%	-1.62%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	-7.62%	0.05%	5.44%

---

## Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

### Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

### Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

---

### Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	A
Growth Score	B
Momentum Score	D
VGM Score	B

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

---

### Disclosures

**This report contains independent commentary to be used for informational purposes only. The analysts contributing to this report do not hold any shares of this stock. The analysts contributing to this report do not serve on the board of the company that issued this stock. The EPS and revenue forecasts are the Zacks Consensus estimates, unless indicated otherwise on the reports first page.** Additionally, the analysts contributing to this report certify that the views expressed herein accurately reflect the analysts personal views as to the subject securities and issuers. ZIR certifies that no part of the analysts compensation was, is, or will be, directly or indirectly, related to the specific recommendation or views expressed by the analyst in the report.

Additional information on the securities mentioned in this report is available upon request. This report is based on data obtained from sources we believe to be reliable, but is not guaranteed as to accuracy and does not purport to be complete. Any opinions expressed herein are subject to change.

ZIR is not an investment advisor and the report should not be construed as advice designed to meet the particular investment needs of any investor. Prior to making any investment decision, you are advised to consult with your broker, investment advisor, or other appropriate tax or financial professional to determine the suitability of any investment. This report and others like it are published regularly and not in response to episodic market activity or events affecting the securities industry.

This report is not to be construed as an offer or the solicitation of an offer to buy or sell the securities herein mentioned. ZIR or its officers, employees or customers may have a position long or short in the securities mentioned and buy or sell the securities from time to time. ZIR is not a broker-dealer. ZIR may enter into arms-length agreements with broker-dealers to provide this research to their clients. Zacks and its staff are not involved in investment banking activities for the stock issuer covered in this report.

ZIR uses the following rating system for the securities it covers. **Outperform-** ZIR expects that the subject company will outperform the broader U.S. equities markets over the next six to twelve months. **Neutral-** ZIR expects that the company will perform in line with the broader U.S. equities markets over the next six to twelve months. **Underperform-** ZIR expects the company will underperform the broader U.S. equities markets over the next six to twelve months.

No part of this report can be reprinted, republished or transmitted electronically without the prior written authorization of ZIR.