

AMERICAN FINANCIAL GROUP INC
Form 10-K
February 26, 2019

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, 2018

Commission File No. 1-13653

AMERICAN FINANCIAL GROUP, INC.

Incorporated under the Laws of Ohio IRS Employer I.D. No. 31-1544320

301 East Fourth Street, Cincinnati, Ohio 45202

(513) 579-2121

Securities Registered Pursuant to Section 12(b) of the Act:

| Title of Each Class | Name of Each Exchange on Which Registered |
|---|---|
| Common Stock | New York Stock Exchange |
| 6-1/4% Subordinated Debentures due September 30, 2054 | New York Stock Exchange |
| 6% Subordinated Debentures due November 15, 2055 | New York Stock Exchange |

Securities Registered Pursuant to Section 12(g) of the Act: None

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, and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the Registrant has submitted electronically, every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months. 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, a non-accelerated filer, a smaller reporting company or an emerging growth company. See definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer

Smaller reporting company Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the Registrant's most recently completed second fiscal quarter: \$8.40 billion.

Indicate the number of shares outstanding of each of the Registrant's classes of common stock, as of the latest practicable date: 89,312,398 shares (excluding 14.9 million shares owned by subsidiaries) as of February 1, 2019.

Documents Incorporated by Reference:

Proxy Statement for 2019 Annual Meeting of Stockholders (portions of which are incorporated by reference into Part III hereof).

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FORWARD-LOOKING STATEMENTS

The disclosures in this Form 10-K contain certain forward-looking statements that are subject to numerous assumptions, risks or uncertainties. The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. Some of the forward-looking statements can be identified by the use of words such as “anticipates”, “believes”, “expects”, “projects”, “estimates”, “intends”, “plans”, “seeks”, “could”, “may”, “should”, “will” or the version of those words or other comparable terminology. Such forward-looking statements include statements relating to: expectations concerning market and other conditions and their effect on future premiums, revenues, earnings, investment activities, and the amount and timing of share repurchases; recoverability of asset values; expected losses and the adequacy of reserves for asbestos, environmental pollution and mass tort claims; rate changes; and improved loss experience.

Actual results and/or financial condition could differ materially from those contained in or implied by such forward-looking statements for a variety of reasons including but not limited to the following and those discussed in Item 1A — Risk Factors.

- changes in financial, political and economic conditions, including changes in interest and inflation rates, currency fluctuations and extended economic recessions or expansions in the U.S. and/or abroad;
- performance of securities markets, including the cost of equity index options;
- new legislation or declines in credit quality or credit ratings that could have a material impact on the valuation of securities in AFG’s investment portfolio;
- the availability of capital;
- changes in insurance law or regulation, including changes in statutory accounting rules and changes in regulation of the Lloyd’s market, including modifications to the establishment of capital requirements for and approval of business plans for syndicate participation;
- changes in the legal environment affecting AFG or its customers;
- tax law and accounting changes, including the impact of recent changes in U.S. corporate tax law;
- levels of natural catastrophes and severe weather, terrorist activities (including any nuclear, biological, chemical or radiological events), incidents of war or losses resulting from civil unrest and other major losses;
- disruption caused by cyber-attacks or other technology breaches or failures by AFG or its business partners and service providers, which could negatively impact AFG’s business and/or expose AFG to litigation;
- development of insurance loss reserves and establishment of other reserves, particularly with respect to amounts associated with asbestos and environmental claims;
- availability of reinsurance and ability of reinsurers to pay their obligations;
- trends in persistency and mortality;
- competitive pressures;
- the ability to obtain adequate rates and policy terms;
- changes in AFG’s credit ratings or the financial strength ratings assigned by major ratings agencies to AFG’s operating subsidiaries; and
- the impact of the conditions in the international financial markets and the global economy relating to AFG’s international operations.

The forward-looking statements herein are made only as of the date of this report. The Company assumes no obligation to publicly update any forward-looking statements.

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ITEM 1
Business

Introduction

American Financial Group, Inc. (“AFG” or the “Company”) is an insurance holding company. Through the operations of Great American Insurance Group, AFG is engaged primarily in property and casualty insurance, focusing on specialized commercial products for businesses, and in the sale of traditional fixed, fixed-indexed and variable-indexed annuities in the retail, financial institutions, registered investment advisor and education markets. Its address is 301 East Fourth Street, Cincinnati, Ohio 45202; its phone number is (513) 579-2121. SEC filings, news releases, AFG’s Code of Ethics applicable to directors, officers and employees and other information may be accessed free of charge through AFG’s Internet site at: www.AFGinc.com. (Information on AFG’s Internet site is not part of this Form 10-K.)

See Note C — “Segments of Operations” to the financial statements for information on AFG’s assets, revenues and earnings before income taxes by segment.

Property and Casualty Insurance Segment

General

AFG’s property and casualty insurance operations provide a wide range of commercial coverages through over 30 niche insurance businesses that make up the Great American Insurance Group. AFG’s property and casualty insurance operations ultimately report to a single senior executive and operate under a business model that allows local decision-making for underwriting, claims and policy servicing in each of the niche operations. Each business is managed by experienced professionals in particular lines or customer groups and operates autonomously but with certain central controls and accountability. The decentralized approach allows each unit the autonomy necessary to respond to local and specialty market conditions while capitalizing on the efficiencies of centralized investment and administrative support functions. AFG’s property and casualty insurance operations employed approximately 6,700 people as of December 31, 2018. These operations are conducted through the subsidiaries listed in the following table, which includes independent financial strength ratings and 2018 gross written premiums (in millions) for each major subsidiary. These ratings are generally based on concerns for policyholders and agents and are not directed toward the protection of investors. AFG believes that maintaining a rating in the “A” category by A.M. Best is important to compete successfully in most lines of business.

| | Ratings | | Gross Written Premiums |
|---|---------|-----------|------------------------------|
| | AM Best | S&P | |
| Insurance Group | | | |
| Great American Insurance | A+ | A+ | \$ 4,478 |
| National Interstate | A+ | not rated | 755 |
| Summit (Bridgefield Casualty and Bridgefield Employers) | A | A+ | 605 |
| Republic Indemnity | A | A+ | 219 |
| Neon Lloyd’s Syndicate | A | A+ | 532 |
| Mid-Continent Casualty | A+ | A+ | 143 |
| Other | | | 108 |
| | | | \$ 6,840 |

The primary objectives of AFG's property and casualty insurance operations are to achieve solid underwriting profitability and provide excellent service to its policyholders and agents. Underwriting profitability is measured by the combined ratio, which is a sum of the ratios of losses, loss adjustment expenses ("LAE"), underwriting expenses and policyholder dividends to premiums. A combined ratio under 100% indicates an underwriting profit. The combined ratio does not reflect investment income, other income or federal income taxes.

While many costs included in underwriting are readily determined (commissions, administrative expenses and many of the losses on claims reported), the process of determining overall underwriting results is highly dependent upon the use of estimates in the case of losses incurred or expected but not yet reported or developed. Actuarial procedures and projections are

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used to obtain “point estimates” of ultimate losses. While the process is imprecise and develops amounts which are subject to change over time, management believes that the liabilities for unpaid losses and loss adjustment expenses are adequate.

Financial information is reported in accordance with U.S. generally accepted accounting principles (“GAAP”) for shareholder and other investor-related purposes and reported on a statutory basis for U.S. insurance regulatory purposes. Unless indicated otherwise, the financial information presented in the Form 10-K for AFG’s property and casualty insurance operations is presented based on GAAP. Statutory information is only prepared for AFG’s U.S.-based subsidiaries, which represented approximately 91% of AFG’s direct written premiums in 2018, and is provided for industry comparisons or where comparable GAAP information is not readily available.

Major differences for statutory accounting include charging policy acquisition costs to expense as incurred rather than spreading the costs over the periods covered by the policies; reporting investment grade bonds and redeemable preferred stocks at amortized cost rather than fair value; netting of reinsurance recoverables and prepaid reinsurance premiums against the corresponding liabilities rather than reporting such items separately; and charging to surplus certain GAAP assets, such as furniture and fixtures and agents’ balances over 90 days old.

AFG’s statutory combined ratio averaged 91.7% for the period 2016 to 2018 as compared to 101.8% for the property and casualty industry over the same period (Sources: Conning, Inc.’s Property - Casualty Forecast & Analysis (Fourth Quarter 2018 Edition, used with permission) and A.M. Best’s Review & Preview Report (February 2018 Edition)). AFG believes that its specialty niche focus, product line diversification and underwriting discipline have contributed to the Company’s ability to consistently outperform the industry’s underwriting results. Management’s philosophy is to refrain from writing business that is not expected to produce an underwriting profit even if it is necessary to limit premium growth to do so.

Property and Casualty Results

Performance measures such as underwriting profit or loss and related combined ratios are often used by property and casualty insurers to help users of their financial statements better understand the company’s performance. See Note C — “Segments of Operations” to the financial statements for the reconciliation of AFG’s earnings before income taxes by significant business segment to the statement of earnings.

The following table shows the performance of AFG’s property and casualty insurance operations (dollars in millions):

| | 2018 | 2017 | 2016 |
|--|----------|----------|----------|
| Gross written premiums | \$6,840 | \$6,502 | \$5,981 |
| Ceded reinsurance | (1,817) | (1,751) | (1,595) |
| Net written premiums | \$5,023 | \$4,751 | \$4,386 |
| Net earned premiums | \$4,865 | \$4,579 | \$4,328 |
| Loss and LAE | 2,985 | 2,884 | 2,669 |
| Special asbestos and environmental (“A&E”) charges ¹⁸ | 89 | 89 | 36 |
| Neon exited lines charge | — | (18) | 65 |
| Underwriting expenses | 1,560 | 1,382 | 1,322 |
| Underwriting gain | \$302 | \$242 | \$236 |

GAAP ratios:

| | | | | | | |
|----------------------------|------|---|------|---|------|---|
| Loss and LAE ratio | 61.7 | % | 64.5 | % | 63.8 | % |
| Underwriting expense ratio | 32.1 | % | 30.2 | % | 30.7 | % |
| Combined ratio | 93.8 | % | 94.7 | % | 94.5 | % |

Statutory ratios:

| | | | | | | |
|----------------------------|------|---|------|---|------|---|
| Loss and LAE ratio | 60.2 | % | 63.0 | % | 58.8 | % |
| Underwriting expense ratio | 31.6 | % | 30.1 | % | 31.4 | % |
| Combined ratio | 91.8 | % | 93.1 | % | 90.2 | % |

Industry statutory combined ratio (a)

| | | | | | | |
|------------------|------|---|-------|---|-------|---|
| All lines | 99.4 | % | 105.1 | % | 100.9 | % |
| Commercial lines | 98.7 | % | 103.5 | % | 99.6 | % |

The sources of the industry ratios are Conning, Inc.'s Property - Casualty Forecast & Analysis (Fourth Quarter 2018 (a)Edition, used with permission) for 2018 and A.M. Best's Review & Preview Report (February 2018 Edition) for 2017 and 2016.

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As with other property and casualty insurers, AFG’s operating results can be adversely affected by unpredictable catastrophe losses. Certain natural disasters (hurricanes, severe storms, earthquakes, tornadoes, floods, etc.) and other incidents of major loss (explosions, civil disorder, terrorist events, fires, etc.) are classified as catastrophes by industry associations. Losses from these incidents are usually tracked separately from other business of insurers because of their sizable effects on overall operations. Total net losses to AFG’s insurance operations from current accident year catastrophes were \$103 million in 2018, \$140 million in 2017 and \$55 million in 2016 and are included in the table above.

AFG generally seeks to reduce its exposure to catastrophes through individual risk selection, including minimizing coastal and known fault-line exposures, and the purchase of reinsurance. AFG’s net exposure to a catastrophic earthquake or windstorm that industry models indicate should statistically occur once in every 500 years (a “500-year event”) is expected to be approximately 6% of AFG’s Shareholders’ Equity.

Property and Casualty Insurance Products

AFG is focused on growth opportunities in what it believes to be more profitable specialty businesses where AFG personnel are experts in particular lines of business or customer groups. The following are examples of AFG’s specialty businesses:

Property and
Transportation

Inland and Ocean Marine Provides coverage primarily for builders’ risk, contractors’ equipment, property, motor truck cargo, marine cargo, boat dealers, marina operators/dealers and excursion vessels.

Agricultural-related Provides federally reinsured multi-peril crop (allied lines) insurance covering most perils as well as crop-hail, equine mortality and other coverages for full-time operating farms/ranches and agribusiness operations on a nationwide basis.

Commercial Automobile Provides coverage for vehicles (such as buses and trucks) in a broad range of businesses including the moving and storage and transportation industries, and a specialized physical damage product for the trucking industry.

Specialty Casualty

Executive and Professional Liability Markets coverage for directors and officers of businesses and non-profit organizations; errors and omissions; cyber; and mergers and acquisitions.

Umbrella and Excess Liability Provides liability coverage in excess of primary layers.

Excess and Surplus Provides liability, umbrella and excess coverage for unique, volatile or hard to place risks, using rates and forms that generally do not have to be approved by state insurance regulators.

General Liability Provides coverage for contractor-related businesses, energy development and production risks, and environmental liability risks.

Targeted Programs Includes coverage (primarily liability and property) for social service agencies, leisure, entertainment and non-profit organizations, customized solutions for other targeted markets and alternative risk programs using agency captives.

Workers’ Compensation Provides coverage for prescribed benefits payable to employees who are injured on the job.

Specialty Financial

Fidelity and Surety Provides fidelity and crime coverage for government, mercantile and financial institutions and surety coverage for various types of contractors and public and private corporations.

Provides coverage for insurance risk management programs for lending and leasing
Lease and Loan Services institutions, including equipment leasing and collateral and lender-placed mortgage property
insurance.

Management believes specialization is the key element to the underwriting success of these business units. These specialty businesses are opportunistic and their premium volume will vary based on prevailing market conditions. AFG continually evaluates expansion in existing markets and opportunities in new specialty markets that meet its profitability objectives. Likewise, AFG will withdraw from markets that do not meet its profit objectives or business strategy.

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Premium Distribution

The following table shows the net written premiums by sub-segment for AFG's property and casualty insurance operations for 2018, 2017 and 2016 (in millions):

| | 2018 | 2017 | 2016 |
|-----------------------------|---------|---------|---------|
| Property and transportation | \$1,754 | \$1,765 | \$1,672 |
| Specialty casualty | 2,509 | 2,280 | 2,036 |
| Specialty financial | 602 | 596 | 572 |
| Other | 158 | 110 | 106 |
| | \$5,023 | \$4,751 | \$4,386 |

The geographic distribution of statutory direct written premiums by AFG's U.S.-based insurers for 2018, 2017 and 2016 is shown below. Approximately 9% of AFG's direct written premiums in 2018 were derived from non U.S.-based insurers, primarily Neon, a United Kingdom-based Lloyd's insurer.

| | 2018 | 2017 | 2016 | | 2018 | 2017 | 2016 |
|------------|-------|-------|-------|----------------|--------|--------|--------|
| California | 13.5% | 13.2% | 14.3% | Missouri | 2.5 % | 2.8 % | 2.7 % |
| Florida | 10.0% | 10.0% | 9.6 % | Pennsylvania | 2.5 % | 2.4 % | 2.5 % |
| New York | 6.8 % | 6.6 % | 6.7 % | Iowa | 2.3 % | 2.4 % | 2.3 % |
| Texas | 6.8 % | 6.2 % | 6.1 % | Kansas | 2.3 % | 2.2 % | 2.2 % |
| Illinois | 5.3 % | 5.6 % | 5.3 % | North Carolina | 2.1 % | 2.1 % | 2.4 % |
| Georgia | 3.3 % | 3.2 % | 2.9 % | Arizona | 2.0 % | 2.6 % | 2.1 % |
| New Jersey | 2.6 % | 2.6 % | 2.5 % | Other | 38.0 % | 38.1 % | 38.4 % |
| | | | | | 100.0% | 100.0% | 100.0% |

Reinsurance

Consistent with standard practice of most insurance companies, AFG reinsures a portion of its property and casualty business with other insurance companies and assumes a relatively small amount of business from other insurers. AFG uses reinsurance for two primary purposes: (i) to provide higher limits of coverage than it would otherwise be willing to provide (i.e. large line capacity) and (ii) to protect its business by reducing the impact of catastrophes. The availability and cost of reinsurance are subject to prevailing market conditions, which may affect the volume and profitability of business that is written. AFG is subject to credit risk with respect to its reinsurers, as the ceding of risk to reinsurers does not relieve AFG of its liability to its insureds until claims are fully settled.

Reinsurance is provided on one of two bases, facultative or treaty. Facultative reinsurance is generally provided on a risk-by-risk basis. Individual risks are ceded and assumed based on an offer and acceptance of risk by each party to the transaction. AFG purchases facultative reinsurance, both pro rata and excess of loss, depending on the risk and available reinsurance markets. Treaty reinsurance provides for risks meeting prescribed criteria to be automatically ceded and assumed according to contract provisions.

Catastrophe Reinsurance AFG has taken steps to limit its exposure to wind and earthquake losses through individual risk selection, including minimizing coastal and known fault-line exposures, and purchasing catastrophe reinsurance. Catastrophe reinsurance is purchased separately for AFG's U.S. property and casualty insurance group and for Neon, AFG's Lloyd's insurance business. In addition, AFG purchases catastrophe reinsurance for its workers' compensation businesses. Although the cost of catastrophe reinsurance varies depending on exposure and the level of worldwide loss activity, AFG continues to obtain reinsurance coverage in adequate amounts at acceptable rates.

In June 2017, AFG's property and casualty insurance subsidiaries entered into a reinsurance agreement to obtain supplemental catastrophe protection through a catastrophe bond structure with Riverfront Re Ltd. ("Riverfront"). The

reinsurance agreement provides supplemental reinsurance coverage up to 95% of \$200 million (fully collateralized) for catastrophe losses in excess of \$104 million (per occurrence and annual aggregate) occurring between June 1, 2017 and December 31, 2020. In connection with the reinsurance agreement, Riverfront issued notes to unrelated investors for the full amount of coverage provided under the reinsurance agreement. Riverfront is a variable interest entity in which AFG does not have a variable interest because the variability in Riverfront's results will be absorbed entirely by the investors in Riverfront. Accordingly, Riverfront is not

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consolidated in AFG's financial statements and the reinsurance agreement is accounted for as ceded reinsurance. AFG's cost for this coverage is approximately \$11 million per year.

In January 2018, Neon launched NCM Re (UK PCC) Ltd. ("NCM Re"), the first insurance-linked securities ("ILS") vehicle in the United Kingdom ("UK"). NCM Re utilizes recently approved UK regulations to provide Neon with the ability to further enhance its global reinsurance offering to clients. NCM Re uses a range of catastrophe modeling and pricing techniques to make use of Neon's underwriting and risk selection skills to source business for third-party ILS investors in the capital markets. In early 2019, NCM Re completed its second ILS transaction, which provides \$77 million in collateralized quota share reinsurance that assumed 17.1% of the Neon Lloyd's syndicate's property treaty reinsurance and direct and facultative portfolios. Losses are recovered from NCM Re before Neon's catastrophe excess of loss reinsurance coverage applies. In addition to NCM Re, Neon also placed a 25.5% quota share reinsurance treaty covering its property insurance and a further 7.1% quota share treaty covering its property insurance placed under binding authorities.

Also in January 2019, AFG's property and casualty insurance subsidiaries renewed their catastrophe reinsurance coverages. For AFG's U.S. based operations, the Company continued to place \$85 million of coverage in excess of a \$15 million per event primary retention in the traditional reinsurance markets. Neon placed \$225 million of coverage in excess of a \$25 million per event primary retention. For the catastrophe excess of loss reinsurance coverage, recoveries from NCM Re and Neon's property insurance quota share apply before calculating losses recoverable from the catastrophe excess of loss reinsurance treaty. In addition to Neon's catastrophe excess of loss reinsurance coverage, Neon has placed a quota share treaty which covers 12.8% of Neon's gross property losses with a \$510 million event limit (maximum \$65 million recoverable) which supplements its catastrophe excess of loss reinsurance coverage and property quota share coverages up to the event limit; recoveries from this quota share treaty also apply before calculating losses recoverable from the catastrophe excess of loss reinsurance treaty.

The commercial marketplace requires large policy limits (\$25 million or more) in several of AFG's lines of business, including certain executive and professional liability, umbrella and excess liability, and fidelity and surety coverages. Since these limits exceed management's desired exposure to an individual risk, AFG generally enters into reinsurance agreements to reduce its net exposure under such policies to an acceptable level. Reinsurance continues to be available for this large line capacity exposure with satisfactory pricing and terms.

In addition to the catastrophe and large line capacity reinsurance programs discussed above, AFG purchases reinsurance on a product-by-product basis. AFG regularly reviews the financial strength of its current and potential reinsurers. These reviews include consideration of credit ratings, available capital, claims paying history and expertise. This process periodically results in the transfer of risks to more financially secure reinsurers. Substantially all reinsurance is ceded to companies with investment grade S&P ratings or is secured by "funds withheld" or other collateral. Under "funds withheld" arrangements, AFG retains ceded premiums to fund ceded losses as they become due from the reinsurer. Recoverables from the following companies were individually between 5% and 10% of AFG's total property and casualty reinsurance recoverable (including prepaid reinsurance premiums and net of payables to reinsurers) at December 31, 2018: Hannover Rueck SE, Munich Reinsurance America, Inc. and Swiss Reinsurance America Corporation. In addition, AFG has a reinsurance recoverable from Ohio Casualty Insurance Company of \$149 million related to that company's purchase of AFG's commercial lines business in 1998. No other reinsurers exceeded 5% of AFG's property and casualty reinsurance recoverable.

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The following table presents (by type of coverage) the amount of each loss above the specified retention covered by treaty reinsurance programs in AFG's U.S.-based property and casualty insurance operations (in millions) as of January 1, 2019:

| | Primary Retention | Reinsurance Coverage AFG | | AFG | |
|---|-------------------|--------------------------|-------------------|--------------|--------------|
| | | Coverage Amount | Participation (%) | Maximum Loss | Maximum Loss |
| | | | | | |
| U.S.-based operations: | | | | | |
| California Workers' Compensation | \$ 2 | \$148 | 1 % | \$ 1 | \$ 3 |
| Summit Workers' Compensation | 3 | 37 | — % | — | 3 |
| Other Workers' Compensation | 2 | 48 | — % | — | 2 |
| Commercial Umbrella | 1 | 49 | 14 % | 7 | 8 |
| Property — General | 5 | 45 | 1 % | 1 | 6 |
| Property — Catastrophe | 15 | 85 | — % | — | 15 |
| Neon Lloyd's Syndicate | | | | | |
| Property — Catastrophe (c) | 25 | 225 | — % | — | 25 |
| Riverfront Re Ltd. catastrophe bond (d) | 104 | 200 | 5 % | 10 | N/A |

(a) Includes the participation of AFG's internal reinsurance program.

(b) Maximum loss per event for claims up to reinsurance coverage limit.

Neon's excess of loss catastrophe reinsurance limits the maximum retained loss per event to \$25 million for a U.S. catastrophe and \$15 million for a non-U.S. catastrophe until such coverage is exhausted. During 2019, Neon

(c) intends to evaluate purchasing additional catastrophe reinsurance to reduce its maximum retained loss per event from a U.S. catastrophe to \$15 million.

(d) Includes aggregate coverage. See description above.

In addition to the coverage shown above, AFG reinsures a portion of its crop insurance business through the Federal Crop Insurance Corporation ("FCIC"). The FCIC offers both proportional (or "quota share") and non-proportional coverages. The proportional coverage provides that a fixed percentage of risk is assumed by the FCIC. The non-proportional coverage allows AFG to select desired retention of risk on a state-by-state, county, crop or plan basis. AFG typically reinsures 15% to 25% of gross written premiums with the FCIC. AFG also purchases quota share reinsurance in the private market. This quota share provides for a ceding commission to AFG and a profit sharing provision. During 2018 and 2017, AFG reinsured 50% and 52.5%, respectively, of premiums not reinsured by the FCIC in the private market and purchased stop loss protection coverage for the remaining portion of the business. In 2019, AFG expects to reinsure 50% of the premiums not reinsured by the FCIC in the private market.

The balance sheet caption "recoverables from reinsurers" included approximately \$109 million on paid losses and LAE and \$2.94 billion on unpaid losses and LAE at December 31, 2018. These amounts are net of allowances of approximately \$18 million for doubtful collection of reinsurance recoverables. The collectibility of a reinsurance balance is based upon the financial condition of a reinsurer as well as individual claim considerations.

Reinsurance premiums ceded and assumed are presented in the following table (in millions):

| | 2018 | 2017 | 2016 |
|--|---------|---------|---------|
| Reinsurance ceded | \$1,817 | \$1,751 | \$1,595 |
| Reinsurance ceded, excluding crop | 1,202 | 1,076 | 985 |
| Reinsurance assumed — including involuntary pools and associations | 214 | 192 | 123 |

Loss and Loss Adjustment Expense Reserves

The consolidated financial statements include the estimated liability for unpaid losses and LAE of AFG's insurance subsidiaries. This liability represents estimates of the ultimate net cost of all unpaid losses and LAE and is determined by using case-basis evaluations, actuarial projections and management's judgment. These estimates are subject to the effects of changes in claim amounts and frequency and are periodically reviewed and adjusted as additional information becomes known. In accordance with industry practices, such adjustments are reflected in current year operations. Generally, reserves for reinsurance assumed and involuntary pools and associations are reflected in AFG's results at the amounts reported by those entities. See Note O — "Insurance — Property and Casualty Insurance Reserves" to the financial statements for information

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on the development of AFG's liability for unpaid losses and loss adjustment expenses by accident year as well as a progression of the liability on a GAAP basis over the past three years.

The differences between the liability for losses and LAE reported in the annual statements filed with the state insurance departments in accordance with statutory accounting principles ("SAP") and that reported in the accompanying consolidated financial statements in accordance with GAAP at December 31, 2018 are as follows (in millions):

| | |
|--|---------|
| Liability reported on a SAP basis, net of \$145 million of retroactive reinsurance | \$6,234 |
| Reinsurance recoverables, net of allowance | 2,942 |
| Other, including reserves of foreign insurers | 565 |
| Liability reported on a GAAP basis | \$9,741 |

Asbestos and Environmental ("A&E") Reserves AFG's property and casualty group, like many others in the industry, has A&E claims arising in most cases from general liability policies written more than thirty years ago. The establishment of reserves for such A&E claims presents unique and difficult challenges and is subject to uncertainties significantly greater than those presented by other types of claims. For a discussion of these uncertainties, see Item 7 — Management's Discussion and Analysis — "Uncertainties — Asbestos and Environmental-related ("A&E") Insurance Reserves" and Note M — "Contingencies" to the financial statements.

The following table (in millions) is a progression of the property and casualty group's A&E reserves.

| | 2018 | 2017 | 2016 |
|---|-------|-------|-------|
| Reserves at beginning of year | \$403 | \$337 | \$327 |
| Incurred losses and LAE | 18 | 89 | 36 |
| Paid losses and LAE | (26) | (23) | (26) |
| Reserves at end of year, net of reinsurance recoverable | 395 | 403 | 337 |
| Reinsurance recoverable, net of allowance | 129 | 125 | 106 |
| Gross reserves at end of year | \$524 | \$528 | \$443 |

In addition to its ongoing internal monitoring of asbestos and environmental exposures, AFG has periodically conducted comprehensive external studies of its asbestos and environmental reserves relating to the run-off operations of its property and casualty insurance segment and exposures related to its former railroad and manufacturing operations with the aid of specialty actuarial, engineering and consulting firms and outside counsel, every two years in recent periods, with an in-depth internal review during the intervening years. AFG is currently evaluating the frequency of future external studies.

An in-depth internal review of AFG's A&E reserves was completed in the third quarter of 2018 by AFG's internal A&E claims specialists in consultation with specialty outside counsel and an outside consultant. As a result of the review, AFG's property and casualty insurance segment recorded an \$18 million pretax special charge to increase its asbestos reserves by \$6 million (net of reinsurance) and its environmental reserves by \$12 million (net of reinsurance). Over the past few years, the focus of AFG's asbestos claims litigation has shifted to smaller companies and companies with ancillary exposures. AFG's insureds with these exposures have been the driver of the property and casualty segment's asbestos reserve increases in recent years. AFG is seeing modestly increasing estimates for indemnity and defense compared to prior studies on certain specific open claims.

The increase in property and casualty environmental reserves in 2018 (as well as in 2017 and 2016) was primarily associated with updated estimates of site investigation and remedial costs with respect to existing sites and newly identified sites. AFG has updated its view of legal defense costs on open environmental claims as well as a number of claims and sites where the estimated investigation and remediation costs have increased. As in recent past years, there were no new or emerging broad industry trends that were identified in this review.

As a result of the comprehensive external study completed in the third quarter of 2017, AFG's property and casualty insurance segment recorded an \$89 million pretax special charge to increase its asbestos reserves by \$53 million (net of reinsurance) and its environmental reserves by \$36 million (net of reinsurance).

An in-depth internal review of AFG's A&E reserves was completed in the third quarter of 2016. As a result of the review, AFG's property and casualty insurance segment recorded a \$36 million pretax special charge to increase its asbestos reserves by \$5 million (net of reinsurance) and its environmental reserves by \$31 million (net of reinsurance).

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Marketing

The property and casualty insurance group directs its sales efforts primarily through independent insurance agents and brokers, although small portions are written through employee agents. Independent agents and brokers generally receive a commission on the sale of each policy. Some agents and brokers are eligible for a bonus commission based on the overall profitability of policies placed with AFG by the broker or agent in a particular year. The property and casualty insurance group writes insurance through several thousand agents and brokers.

Competition

AFG's property and casualty insurance businesses compete with other individual insurers, state funds and insurance groups of varying sizes, some of which are mutual insurance companies possessing competitive advantages in that all their profits inure to their policyholders. See Item 1A — Risk Factors. They also compete with self-insurance plans, captive programs and risk retention groups. Due to the specialty nature of these coverages, competition is based primarily on service to policyholders and agents, specific characteristics of products offered and reputation for claims handling. Financial strength ratings, price, commissions and profit sharing terms are also important factors. Management believes that sophisticated data analysis for refinement of risk profiles, extensive specialized knowledge and loss prevention service have helped AFG compete successfully.

Annuity Segment

General

AFG sells 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. The annuity operations employed approximately 600 people at December 31, 2018. These operations are conducted primarily through the subsidiaries listed in the following table, which includes 2018 statutory annuity premiums (in millions), annuity policies in force and independent ratings.

| Company | Annuity | | | |
|--|------------------|-------------------|-----------------|-----|
| | Annuity Premiums | Policies In Force | Ratings AM Best | S&P |
| Great American Life Insurance Company | \$ 5,212 | 423,000 | A | A+ |
| Annuity Investors Life Insurance Company | 195 | 111,000 | A | A+ |

AFG believes that the ratings assigned by independent insurance rating agencies are an important competitive factor because agents, potential policyholders and financial institutions often use a company's rating as an initial screening device in considering annuity products. AFG believes that a rating in the "A" category by at least one rating agency is necessary to successfully compete in its primary annuity markets.

Due to the deposit-type nature of annuities, annuity premiums received and benefit payments are recorded as increases or decreases in the annuity benefits accumulated liability rather than as revenue and expense under GAAP. Statutory premiums of AFG's annuity operations for the last three years were as follows (in millions):

| | Statutory Premiums | | |
|---|--------------------|---------|---------|
| | 2018 | 2017 | 2016 |
| Financial institutions single premium annuities — indexed | \$1,776 | \$1,711 | \$1,950 |
| Financial institutions single premium annuities — fixed | 492 | 622 | 468 |
| Retail single premium annuities — indexed | 1,418 | 990 | 1,056 |
| Retail single premium annuities — fixed | 87 | 70 | 73 |
| Broker-dealer single premium annuities — indexed | 1,271 | 733 | 658 |

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| | | | |
|--|---------|---------|---------|
| Broker-dealer single premium annuities — fixed | 14 | 7 | 9 |
| Pension risk transfer | 132 | 6 | — |
| Education market — fixed and indexed annuities | 192 | 174 | 184 |
| Total fixed annuity premiums | 5,382 | 4,313 | 4,398 |
| Variable annuities | 25 | 28 | 37 |
| Total annuity premiums | \$5,407 | \$4,341 | \$4,435 |

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Annuities are long-term retirement saving instruments that benefit from income accruing on a tax-deferred basis. The issuer of the annuity collects premiums, credits interest or earnings on the policy and pays out a benefit upon death, surrender or annuitization. Single premium annuities are generally issued in exchange for a one-time lump-sum premium payment. Certain annuities, primarily in the education market, have premium payments that are flexible in both amount and timing as determined by the policyholder and are generally made through payroll deductions.

Annuity contracts are generally classified as either fixed rate (including fixed-indexed and variable-indexed) or variable. With a traditional fixed rate annuity, AFG seeks to maintain a desired spread between the yield on its investment portfolio and the rate it credits to policyholders. AFG accomplishes this by: (i) offering crediting rates that it has the option to change after any initial guarantee period (subject to minimum interest rate and other contractual guarantees); (ii) designing annuity products that encourage persistency; and (iii) maintaining an appropriate matching of assets and liabilities.

An indexed annuity provides policyholders with the opportunity to receive a crediting rate tied, in part, to the performance of an existing market index (generally the S&P 500) or other external rate, price, or unit value (an “index”). A fixed-indexed annuity protects against the related downside risk through a guarantee of principal (excluding surrender charges, market value adjustments, and certain benefit charges). In 2018, AFG began offering variable-indexed annuities, which are similar to fixed-indexed annuities except that the product offers greater upside participation in the selected index as compared to a fixed-indexed annuity and replaces the guarantee of principal in a fixed-indexed annuity with a guaranteed maximum loss. AFG purchases and sells call and put options designed to substantially offset the effect of the index participation in the liabilities associated with indexed annuities.

As an accommodation in its education market, AFG offers a limited amount of variable annuities. With a variable annuity, the earnings credited to the policy vary based on the investment results of the underlying investment options chosen by the policyholder, generally without any guarantee of principal except in the case of death of the insured. Premiums directed to the underlying investment options maintained in separate accounts are invested in funds managed by various independent investment managers. AFG earns a fee on amounts deposited into separate accounts. Subject to contractual provisions, policyholders may also choose to direct all or a portion of their premiums to various fixed-rate options, in which case AFG earns a spread on amounts deposited.

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The profitability of a fixed annuity business is largely dependent on the ability of a company to earn income on the assets supporting the business in excess of the amounts credited to policyholder accounts plus expenses incurred (earning a “spread”). Performance measures such as net spread earned are often presented by annuity businesses to help users of their financial statements better understand the company’s performance. The following table shows the earnings before income taxes, as well as the net spread earned on fixed annuities, for the annuity segment both before and after the impact of fair value accounting for derivatives related to fixed-indexed (including variable-indexed) annuities (“FIAs”) (dollars in millions):

| | Year ended December 31, | | |
|---|-------------------------|----------|----------|
| | 2018 | 2017 | 2016 |
| Annuity earnings before income taxes — before unlocking and change in fair value of derivatives related to FIAs | \$425 | \$416 | \$394 |
| Unlocking | (31) | (3) | 1 |
| Impact of derivatives related to FIAs (a): | | | |
| Change in fair value of derivatives | (51) | (70) | (53) |
| Related impact on amortization of DPAC (b) | 18 | 37 | 26 |
| Annuity segment earnings before income taxes | \$361 | \$380 | \$368 |
| Net spread earned on fixed annuities — before impact of unlocking and derivatives related to FIAs | 1.26 % | 1.34 % | 1.38 % |
| Unlocking | (0.09 %) | (0.01 %) | 0.01 % |
| Impact of derivatives related to FIAs: | | | |
| Change in fair value of derivatives | (0.15 %) | (0.22 %) | (0.19 %) |
| Related impact on amortization of DPAC (b) | 0.05 % | 0.12 % | 0.09 % |
| Net spread earned on fixed annuities | 1.07 % | 1.23 % | 1.29 % |

FIAs provide policyholders with a crediting rate tied, in part, to the performance of an existing stock market or other financial index. AFG attempts to mitigate the risk in the index-based component of these products through the purchase and sale of call and put options on the appropriate index. AFG’s strategy is designed so that the change in the fair value of the call option assets and put option liabilities will generally offset the economic change in the policyholder liability from the index participation. Both the index-based component of the annuities (fair value of (a) \$2.72 billion at December 31, 2018) and the related call and put options (net fair value of \$183 million at December 31, 2018) are considered derivatives that must be marked-to-market through earnings each period. Fluctuations in interest rates and the stock market, among other factors, can cause volatility in the periodic measurement of fair value of the embedded derivative that management believes can be inconsistent with the long-term economics of these products.

(b) An estimate of the related acceleration/deceleration of the amortization of deferred policy acquisition costs and deferred sales inducements.

Marketing

AFG sells its single premium annuities, excluding financial institution production (discussed below), primarily through a retail network of approximately 75 national marketing organizations (“NMOs”) and managing general agents (“MGAs”) who, in turn, direct approximately 1,600 actively producing agents.

AFG also sells single premium annuities in financial institutions through direct relationships with certain financial institutions and through independent agents and brokers. The table below highlights the percentage of AFG’s total annuity premiums generated through its top five financial institution relationships (ranked based on 2018 statutory premiums):

| | 2018 | 2017 |
|-----------------------|-------|-------|
| Wells Fargo & Company | 7.4 % | 8.1 % |

| | | |
|--|------|------|
| The PNC Financial Services Group, Inc. | 6.6% | 9.1% |
| Regions Financial Corporation | 4.8% | 6.5% |
| LPL Financial | 4.8% | 5.5% |
| BB&T Corporation | 3.7% | 5.5% |

In the education market, schools may allow employees to save for retirement through contributions made on a before-tax basis. Federal income taxes are not payable on pretax contributions or earnings until amounts are withdrawn. AFG sells its education market annuities through regional and national agencies.

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AFG is licensed to sell its fixed annuity products in all states except New York; it is licensed to sell its variable products in all states except New York and Vermont. At December 31, 2018, AFG had approximately 536,000 annuity policies in force. The states that accounted for 5% or more of AFG's statutory annuity premiums in 2018 and the comparable preceding years are shown below:

| | 2018 | 2017 | 2016 |
|--------------|-------|-------|-------|
| California | 10.2% | 10.0% | 9.8% |
| Florida | 8.1 % | 7.3 % | 8.5 % |
| Pennsylvania | 5.5 % | 6.1 % | 7.2% |
| Ohio | 5.2 % | 5.4 % | 5.2% |
| Texas | 5.1 % | 5.1 % | 4.6% |

Competition

AFG's annuity businesses operate in highly competitive markets. They compete with other insurers and financial institutions based on many factors, including: (i) ratings; (ii) financial strength; (iii) reputation; (iv) service to policyholders and agents; (v) product design (including interest rates credited, bonus features and index participation); and (vi) commissions. Since most policies are marketed and distributed through independent agents, the insurance companies must also compete for agents.

No single insurer dominates the markets in which AFG's annuity businesses compete. See Item 1A — Risk Factors. Competitors include (i) individual insurers and insurance groups, (ii) mutual funds and (iii) other financial institutions. In a broader sense, AFG's annuity businesses compete for retirement savings with a variety of financial institutions offering a full range of financial services. In the financial institution annuity market, AFG's annuities compete directly against competitors' annuities, certificates of deposit and other investment alternatives at the point of sale. In addition, over the last few years, several offshore and/or hedge fund companies have made significant acquisitions of annuity businesses, resulting in annuity groups that are larger in size than AFG's annuity business.

Sales of annuities, including renewal premiums, are affected by many factors, including: (i) competitive annuity products and rates; (ii) the general level and volatility of interest rates, including the slope of the yield curve; (iii) the favorable tax treatment of annuities; (iv) commissions paid to agents; (v) services offered; (vi) ratings from independent insurance rating agencies; (vii) other alternative investments; (viii) performance and volatility of the equity markets; (ix) media coverage of annuities; (x) regulatory developments regarding suitability and the sales process; and (xi) general economic conditions.

Other Operations

AFG ceased new sales of long-term care insurance in January 2010 and sold substantially all of its run-off long-term care business in December 2015. The legal entities sold in 2015, United Teacher Associates Insurance Company and Continental General Insurance Company, contained substantially all of AFG's long-term care insurance reserves (96% as measured by net statutory reserves as of November 30, 2015), as well as smaller blocks of annuity and life insurance business. Renewal premiums on the remaining small block of long-term care policies (which are guaranteed renewable) covering approximately 1,500 lives will be accepted unless those policies lapse. At December 31, 2018, AFG's long-term care insurance reserves were \$45 million, net of reinsurance recoverables and excluding the impact of unrealized gains on securities.

Although AFG no longer actively markets new life insurance products, it continues to service and receive renewal premiums on its in-force block of approximately 97,000 policies and \$10.82 billion gross (\$3.13 billion net of reinsurance) of life insurance in force at December 31, 2018. Renewal premiums, net of reinsurance, were \$21 million

in 2018, \$17 million in 2017 and \$18 million in 2016. At December 31, 2018, AFG's life insurance reserves were \$292 million, net of reinsurance recoverables.

Through subsidiaries, AFG 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). These operations employed approximately 300 full-time employees at December 31, 2018.

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Investment Portfolio

General

A summary of AFG's fixed maturities and equity securities is shown in Note E — "Investments" to the financial statements. For additional information on AFG's investments, see Item 7 — Management's Discussion and Analysis — "Investments." AFG's earned yield (net investment income divided by average invested assets) on fixed maturities was 4.4% for both 2018 and 2017 and 4.5% for 2016.

The table below compares total returns, which include changes in fair value, on AFG's fixed maturities and common stocks and equivalents to comparable public indices. While there are no directly comparable indices to AFG's portfolio, the two shown below are widely used benchmarks in the financial services industry.

| | 2018 | 2017 | 2016 |
|---|---------|-------|-------|
| Total return on AFG's fixed maturities | 1.3 % | 5.9 % | 4.7 % |
| Barclays Capital U.S. Universal Bond Index | (0.3 %) | 4.1 % | 3.9 % |
| Total return on AFG's common stocks and equivalents | (12.0%) | 15.8% | 12.5% |
| Standard & Poor's 500 Index | (4.4 %) | 21.8% | 12.0% |

AFG's bond portfolio is invested primarily in taxable bonds. The following table shows AFG's available for sale fixed maturity investments by Standard & Poor's Corporation or comparable rating as of December 31, 2018 (dollars in millions).

| S&P or comparable rating | Amortized Fair Value | | |
|----------------------------|----------------------|----------|------|
| | Cost | Amount | % |
| AAA, AA, A | \$ 25,999 | \$26,091 | 62 % |
| BBB | 12,195 | 12,042 | 29 % |
| Total investment grade | 38,194 | 38,133 | 91 % |
| BB | 700 | 682 | 2 % |
| B | 261 | 254 | — % |
| CCC, CC, C | 588 | 688 | 2 % |
| D | 202 | 233 | — % |
| Total non-investment grade | 1,751 | 1,857 | 4 % |
| Not rated | 1,892 | 2,007 | 5 % |
| Total | \$ 41,837 | \$41,997 | 100% |

The National Association of Insurance Commissioners ("NAIC") has retained third-party investment management firms to assist in the determination of appropriate NAIC designations for mortgage-backed securities ("MBS") based not only on the probability of loss (which is the primary basis of ratings by the major ratings firms), but also on the severity of loss and statutory carrying value. Approximately 9% of AFG's fixed maturity investments are MBS. At December 31, 2018, 98% (based on statutory carrying value of \$41.81 billion) of AFG's fixed maturity investments held by its insurance companies had an NAIC designation of 1 or 2 (the highest of the six designations).

Regulation

AFG's insurance company subsidiaries are subject to regulation in the jurisdictions where they do business. In general, the insurance laws of the various states establish regulatory agencies with broad administrative powers governing, among other things, premium rates, solvency standards, licensing of insurers, agents and brokers, trade practices, forms of policies, maintenance of specified reserves and capital for the protection of policyholders, deposits of

securities for the benefit of policyholders, investment activities and relationships between insurance subsidiaries and their parents and affiliates. Material transactions between insurance subsidiaries and their parents and affiliates generally must receive prior approval of the applicable insurance regulatory authorities and be disclosed. In addition, while differing from state to state, these regulations typically restrict the maximum amount of dividends that may be paid by an insurer to its shareholders in any twelve-month period without advance regulatory approval. Such limitations are generally based on net earnings or statutory surplus. Under applicable restrictions, the maximum amount of dividends available to AFG in 2019 from its insurance subsidiaries without seeking regulatory approval is approximately \$1.30 billion.

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The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank Act”), among other things, established a Federal Insurance Office (“FIO”) within the U.S. Treasury. Under this law, regulations will need to be created for the FIO to carry out its mandate to focus on systemic risk oversight. Since its formation, the FIO has worked with the NAIC and other stakeholders to explore a hybrid approach to regulation of the insurance industry; however, the state-based system of regulation has largely been retained. AFG cannot predict the future role of the FIO and its role in regulation of the insurance industry and how that might ultimately affect AFG’s operations.

Neon, AFG’s UK-based Lloyd’s insurer, is subject to regulation by Lloyd’s, including the establishment of capital requirements and approval of business plans, and the Prudential Regulation Authority.

Most states have created insurance guaranty associations that assess solvent insurers to pay claims of insurance companies that become insolvent. Annual guaranty assessments for AFG’s insurance companies have not been material.

Disclosure of Certain Activities Under Section 13(r) of the Securities Exchange Act of 1934

Section 13(r) of the Securities Exchange Act of 1934, as amended (“Section 13(r)”), requires a registrant to disclose in its annual or quarterly reports whether it or an affiliate knowingly engaged in certain activities, transactions or dealings related to Iran during the period covered by the report.

Certain of the Company’s subsidiaries located outside the United States subscribe to insurance policies that provide insurance coverage to vessels owned by international shipping and marine entities with vessels that travel worldwide. As a result, the insurance policies may be called upon to respond to claims involving or that have exposure to Iranian petroleum resources, refined petroleum, and petrochemical industries. For example, certain of the Company’s non-U.S. subsidiaries participate in global marine hull and war policies that provide coverage for damage to vessels navigating into and out of ports worldwide, which could include Iran.

For the year ended December 31, 2018, the Company is not aware of any additional premium with respect to underwriting insurance or reinsurance activities reportable under Section 13(r). Should any such risks have entered into the stream of commerce covered by these insurance or reinsurance activities, the Company believes that the premiums associated with such business would be immaterial.

ITEM 1A

Risk Factors

In addition to the other information set forth in this report, particularly information under “Forward-Looking Statements” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” the following factors could materially affect AFG’s business, financial condition, cash flows or future results. Any one of these factors could cause AFG’s actual results to vary materially from recent results or from anticipated future results. The risks described below are not the only risks facing AFG. Additional risks and uncertainties not currently known to management or that management currently deems to be immaterial also may materially adversely affect AFG’s business, financial condition and/or operating results.

Adverse developments in the financial markets and deterioration in global economic conditions could have a material adverse effect on AFG’s results of operations and financial condition.

Worldwide financial markets have, from time to time, experienced significant and unpredictable disruption. A prolonged economic downturn would result in heightened credit risk, reduced valuation of certain investments and decreased economic activity.

Changes in financial markets including fluctuations in interest rates, credit conditions, equity prices and many other factors that are unpredictable and beyond AFG's control can adversely affect the value of investments and the realization of investment income.

A significant majority of AFG's investment portfolio consists of fixed maturity investments, and changes in global economic conditions, including interest rates, could have a material adverse effect on AFG's results of operations and financial condition.

As of December 31, 2018, approximately 87% of AFG's investment portfolio holdings consisted of fixed maturity investments that are sensitive to changes in interest rates. A decline in interest rates may reduce the returns earned on new and floating-rate

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fixed maturity investments, thereby reducing AFG's net investment income, while an increase in interest rates may reduce the value of AFG's existing fixed maturity investments, which primarily have fixed interest rates. The value of AFG's fixed maturity investments is also subject to credit risk as certain investments may default or become impaired due to deterioration in the financial condition of issuers of those investments. If a decline in the fair value of a specific investment (below its amortized cost) is considered to be other-than-temporary, a provision for impairment would be charged to earnings.

Despite modest increases in the past year, long-term interest rates have remained at historical lows for an extended period. In addition, central banks in some countries have pursued largely unprecedented negative interest rate policies in recent years, the consequences of which are uncertain. The continuation of the current low interest rate environment or a deflationary environment with negative interest rates could affect business behavior in ways that are adverse to AFG and could constrict AFG's net investment income.

As of December 31, 2018, mortgage-backed securities constituted approximately 9% of AFG's fixed maturity portfolio. In addition to the risks applicable to the entire fixed maturity investment portfolio, changes in interest rates can expose AFG to prepayment risks on mortgage-backed securities. In periods of declining interest rates, mortgage prepayments generally increase and mortgage-backed securities are paid down more quickly, requiring AFG to reinvest the proceeds at the then current market rates, which may be lower than on the securities repaid.

Changes in interest rates could adversely affect AFG's results of operations.

The profitability of AFG's annuity segment is largely dependent on the spread between what it earns on its investments and the crediting rate it pays on its annuity contracts plus expenses incurred.

Both rising and declining interest rates can negatively affect AFG's annuity results. Most of AFG's annuity products have guaranteed minimum crediting rates. Although AFG could reduce the average crediting rate on a substantial portion of its traditional fixed and fixed-indexed annuities during periods of low or falling interest rates, AFG may not be able to fully offset the decline in investment earnings with lower crediting rates.

During periods of rising interest rates, AFG may experience competitive pressure to increase crediting rates to avoid a decline in sales or increased surrenders, thus resulting in lower spreads. In addition, an increase in surrenders could require the sale of investments at a time when the prices of those assets are lower due to the increase in market rates, which may result in realized investment losses.

Intense competition could adversely affect AFG's results of operations.

The property and casualty insurance segment operates in a highly competitive industry that is affected by many factors that can cause significant fluctuations in its results of operations. The lines of business in this segment compete with other individual insurers, state funds and insurance groups of varying sizes, some of which are mutual insurance companies possessing competitive advantages in that all their profits inure to their policyholders. In addition, certain foreign insurers may be taxed at lower rates, which may result in a competitive advantage over AFG. The property and casualty insurance segment also competes with self-insurance plans, captive programs and risk retention groups. Competition is based on many factors, including service to policyholders and agents, product design, reputation for claims handling, price, commissions, ratings and financial strength. Peer companies and competitors in some or all of AFG's specialty lines include the following companies and/or their subsidiaries: Alleghany Corp., American International Group Inc., American National Insurance Company, AmTrust Financial Services, Inc., Arch Capital Group Ltd., Chubb Ltd., Cincinnati Financial Corp., CNA Financial Corp., Fairfax Financial Holdings Ltd. (Zenith National), The Hartford Financial Services Group, Inc., Lancer Insurance Company, Liberty Mutual, Markel Corp., Munich Re Group (American Modern Insurance), Protective Insurance Company, RLI Corp., The Travelers

Companies, Inc., Tokio Marine Holdings, Inc. (HCC Insurance, Philadelphia Consolidated), W.R. Berkley Corp., AXA (XL Group Ltd.) and Zurich Insurance Group Ltd.

AFG's annuity segment competes with individual insurers and insurance groups, mutual funds and other financial institutions. In addition, in recent years, offshore and/or hedge fund companies have made significant acquisitions of annuity businesses. Competition is based on numerous factors including reputation, product design, interest crediting rates, performance, scope of distribution, price and perceived financial strength and credit ratings. Peer companies and competitors for AFG's annuity segment include the following companies and/or their subsidiaries: Allianz Life Insurance Company of North America, American Equity Investment Life Holding Company (Eagle Life Insurance Company), American International Group Inc., Athene Holding Ltd, Global Atlantic Financial Group Ltd. (Forethought Life Insurance Company), Lincoln National Corp., MetLife, Inc., Nationwide Mutual Insurance Company, Pacific Life Insurance Company, Sumitomo Life Insurance Company (Symetra Financial Corp.) and Voya Financial, Inc.

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Some of AFG's competitors have more capital and greater resources than AFG, and may offer a broader range of products and lower prices than AFG offers. If competition limits AFG's ability to write new or renewal business at adequate rates, its results of operations will be adversely affected.

A significant percentage of AFG's sales of annuity products through financial institutions is concentrated in a small number of institutions.

Annuity premiums generated through financial institutions represented 42% of AFG's annuity premiums in 2018. In 2018, two large financial institutions accounted for 34% of AFG's total sales through financial institutions and 14% of AFG's overall annuity sales. In the financial institutions annuity market, AFG competes directly against competitors' annuities, certificates of deposit and other investment alternatives at the point of sale. Loss of a substantial portion of this business coupled with a failure to replace these financial institutions if they significantly reduce sales of AFG annuities could reduce AFG's future growth.

AFG's revenues could be adversely affected if it is not able to attract and retain independent agents.

AFG's reliance on the independent agency market makes it vulnerable to a reduction in the amount of business written by agents. Many of AFG's competitors also rely significantly on the independent agency market. Some of AFG's competitors offer a wider variety of products, lower prices for insurance coverage or higher commissions. A reduction in the number of independent agencies marketing AFG's products, the failure of agencies to successfully market AFG's products, changes in the strategy or operations of agencies (including agency consolidation) or the choice of agencies to reduce their writings of AFG products could adversely affect AFG's revenues and profitability.

The inability to obtain reinsurance or to collect on ceded reinsurance could adversely affect AFG's results of operations.

AFG purchases reinsurance to limit the amount of risk it retains. Market conditions determine the availability and cost of the reinsurance protection AFG purchases, which affects the level of AFG's business and profitability, as well as the level and types of risk AFG retains. If AFG is unable to obtain sufficient reinsurance at a cost AFG deems acceptable, AFG may opt to reduce the volume of its underwriting. AFG is also subject to credit risk with respect to its reinsurers, as AFG will remain liable to its insureds regardless of whether a reinsurer is able to meet its obligations under agreements covering the reinsurance ceded. The collectability of recoverables from reinsurers is subject to uncertainty arising from a number of factors, including a reinsurers' financial capacity and willingness to make payments under the terms of a reinsurance treaty or contract and changes in market conditions. As of December 31, 2018, AFG has \$3.35 billion of recoverables from reinsurers on its balance sheet.

AFG is subject to comprehensive regulation, and its ability to earn profits may be restricted by these regulations.

AFG is subject to comprehensive regulation by government agencies in the states and countries where its insurance company subsidiaries are domiciled and where these subsidiaries issue policies and handle claims. In addition, the Lloyd's marketplace sets rules under which its members operate, including Neon (AFG's Lloyd's syndicate). Most insurance regulations are designed to protect the interests of AFG's policyholders and third party claimants as opposed to its investors.

The Dodd-Frank Act, enacted in June 2010, mandates changes to the regulation of the financial services industry. Implementation of the Dodd-Frank Act is ongoing. The potential impacts of the Act on the U.S. insurance industry are not clear, but may affect AFG's operations and governance in ways that could adversely affect AFG's financial condition and results of operations.

Changes in domestic or foreign tax laws or interpretations of such laws could increase AFG's corporate taxes and reduce earnings. For example, on December 22, 2017, the U.S. enacted The Tax Cuts and Jobs Act of 2017 ("TCJA"), which significantly reformed the U.S. tax code. Clarifications and interpretations of the TCJA may adversely affect our expected effective tax rate and the realization of deferred taxes.

As a participant in the federal crop insurance program, AFG could also be impacted by regulatory and legislative changes affecting that program. For example, the reinsurance levels that the federal government provides to authorized carriers could be reduced by future legislation. AFG will continue to monitor new and changing federal regulations and their potential impact, if any, on its insurance company subsidiaries.

On April 18, 2018, the U.S. Securities and Exchange Commission released a package of regulatory proposals to enhance standards of conduct owed by broker-dealers to their clients known as Regulation Best Interest. If adopted as proposed,

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Regulation Best Interest would heighten the standards that registered representatives need to meet when making a recommendation by requiring them to act in the best interest of the retail customer at the time of the recommendation. Regulation Best Interest would require a registered representative to (i) disclose to the customer the material facts relating to scope and terms of the relationship, (ii) exercise reasonable diligence, care, skill and prudence in recommending a product that is in the customer's best interest, and (iii) eliminate or, at a minimum, disclose, material conflicts of interests.

Existing insurance-related laws and regulations may become more restrictive in the future or new restrictive laws may be enacted; it is not possible to predict the potential effects of these laws and regulations. The costs of compliance or the failure to comply with existing or future regulations could impose significant burdens on AFG.

A downgrade or potential downgrade in AFG's financial strength and/or credit ratings by one or more rating agencies could adversely affect its business, financial condition, results of operations and/or cash flows.

Financial strength ratings are an important factor in establishing the competitive position of insurance companies and may have an effect on an insurance company's sales. A downgrade out of the "A" category in AFG's insurers' claims-paying and financial strength ratings could significantly reduce AFG's business volumes in certain lines of business, adversely impact AFG's ability to access the capital markets and increase AFG's borrowing costs.

In addition to the financial strength ratings of AFG's principal insurance company subsidiaries, various rating agencies also publish credit ratings for AFG. Credit ratings are indicators of a debt issuer's ability to meet the terms of debt obligations in a timely manner, are part of AFG's overall financial profile and affect AFG's ability to access certain types of capital. A downgrade in AFG's credit ratings could have a material adverse effect on AFG's financial condition and results of operations and cash flows in a number of ways, including adversely limiting access to capital markets, potentially increasing the cost of debt or increasing borrowing costs under AFG's current revolving credit facility.

The continued threat of terrorism and ongoing military and other actions, as well as civil unrest, may adversely affect AFG's results of operations.

The occurrence of one or more terrorist attacks could cause significant losses from insurance claims that could adversely affect AFG's profitability. Private sector catastrophe reinsurance is limited and generally unavailable for terrorism losses caused by attacks with nuclear, biological, chemical or radiological weapons. Reinsurance coverage from the federal government under the Terrorism Risk Insurance Program Reauthorization Act of 2015 ("TRIPRA") is also limited. Although TRIPRA provides benefits for certified acts of terrorism that exceed a certain threshold of industry losses (\$160 million in 2018, increasing by \$20 million annually to \$200 million by 2020), those benefits are subject to a deductible and other limitations. In 2019, AFG would have to sustain losses from terrorism of nearly \$700 million to be eligible for reinsurance under the program. In addition, because the interpretation of this law is untested, there is substantial uncertainty as to how it will be applied to specific circumstances. Finally, the program currently expires at the end of 2020, and the elimination or modification of the program, or a failure to extend the program, could adversely affect AFG's property and casualty insurance business through increased exposure to a catastrophic level of terrorism losses.

AFG may experience difficulties with technology or data security, which could have an adverse effect on its business or reputation.

AFG uses computer systems and services to store, retrieve, evaluate and utilize company and customer data and information. Systems failures or outages could compromise AFG's ability to perform business functions in a timely manner, which could harm its ability to conduct business and hurt its relationships with business partners and customers. In the event of a disaster such as a natural catastrophe, an industrial accident, a blackout, malicious

software, a terrorist attack or war, AFG's systems may be inaccessible to employees, customers or business partners for an extended period of time. Even if AFG's employees are able to report to work, they may be unable to perform their duties for an extended period of time if the Company's data or systems are disabled or destroyed.

AFG's computer systems are vulnerable to security breaches due to the sophistication of cyber-attacks, viruses, malware, hackers and other external hazards, as well as inadvertent errors, equipment and system failures, and employee misconduct. In addition, over time, and particularly recently, the sophistication of these threats continues to increase. AFG's administrative and technical controls as well as other preventative actions used to reduce the risk of cyber incidents and protect AFG's information may be insufficient to detect or prevent unauthorized access, other physical and electronic break-ins, cyber-attacks or other security breaches to AFG's computer systems or those of third parties with whom AFG does business.

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AFG has increasingly outsourced certain technology and business process functions to third parties and may continue to do so in the future. Outsourcing of certain technology and business process functions to third parties may expose AFG to increased risk related to data security or service disruptions. If AFG does not effectively develop, implement and monitor these relationships, third party providers do not perform as anticipated, technological or other problems are incurred with a transition, or outsourcing relationships relevant to AFG's business process functions are terminated, AFG may not realize expected productivity improvements or cost efficiencies and may experience operational difficulties, increased costs and a loss of business.

The increased risks identified above could expose AFG to data loss, disruption of service, monetary and reputational damages, competitive disadvantage and significant increases in compliance costs and costs to improve the security and resiliency of AFG's computer systems. The compromise of personal, confidential or proprietary information could also subject AFG to legal liability or regulatory action under evolving cyber-security, data protection and privacy laws and regulations enacted by the U.S. federal and state governments, Canada, the European Union (the "EU") or other jurisdictions or by various regulatory organizations or exchanges. As a result, AFG's ability to conduct business and its results of operations might be materially and adversely affected.

Any failure to protect the confidentiality of customer information could adversely affect AFG's reputation and have a material adverse effect on AFG's business, financial condition and results of operations.

AFG and certain of its third-party vendors collect and store sensitive data in the ordinary course of AFG's business, including personal identification information of its employees and that of its customers, vendors, investors and other third parties. In connection with AFG's property and casualty insurance operations, data may include medical information. AFG is subject to numerous federal, state and international laws regarding the privacy and security of personal information, which laws vary significantly from jurisdiction to jurisdiction. If any disruption or security breach results in a loss or damage to AFG's data, or inappropriate disclosure of AFG's confidential information or that of others, it could damage AFG's reputation, affect its relationships with customers and clients, lead to claims against AFG, result in regulatory action and harm AFG's business. In addition, AFG may be required to incur significant costs to mitigate the damage caused by any security breach or to protect against future damage.

AFG's property and casualty reserves may be inadequate, which could have a material adverse effect on AFG's results of operations.

Liabilities for unpaid losses and loss adjustment expenses do not represent an exact calculation of liability but instead represent management estimates of what the ultimate settlement and administration of claims will cost, supported by actuarial expertise and projection techniques, at a given accounting date. The process of estimating unpaid losses and loss adjustment expense reserves involves a high degree of judgment and is subject to a number of variables. These variables can be affected by both internal and external events, such as: changes in claims handling procedures, adverse changes in loss cost trends (including inflationary pressures on medical costs), economic conditions (including general inflation), legal trends and legislative changes, and varying judgments and viewpoints of the individuals involved in the estimation process, among others. The impact of many of these items on ultimate costs for unpaid losses and loss adjustment expenses is difficult to estimate. Unpaid losses and loss adjustment expense reserve estimation difficulties also differ significantly by product line due to differences in claim complexity, the volume of claims, the potential severity of individual claims, the determination of an occurrence date for a claim and lags in the time between damage, loss or injury and when a claim is actually reported to the insurer. In addition, the historic development of AFG's liability for unpaid losses and loss adjustment expenses may not necessarily reflect future trends in the development of these amounts. Accordingly, it is not appropriate to extrapolate future redundancies or deficiencies based on historical information. To the extent that reserves are inadequate and are strengthened, AFG's profitability would be adversely affected because the amount of any such increase would be treated as a charge to earnings in the period in which the deficiency is recognized.

AFG's results of operations could be adversely impacted by severe weather conditions or other catastrophes, both natural and man-made.

Catastrophes can be caused by unpredictable natural events such as hurricanes, windstorms, severe storms, tornadoes, floods, hailstorms, severe winter weather, earthquakes, explosions and fire, and by man-made events, such as terrorist attacks. While not considered a catastrophe by insurance industry standards, droughts can have a significant adverse impact on AFG's crop insurance results. In addition, extreme weather events that are linked to rising temperatures, changing global weather patterns and fluctuating rain, snow and sea levels could result in increased occurrence and severity of catastrophes. The extent of gross losses from a catastrophe event is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event, potentially mitigated by any reinsurance coverage purchased by AFG's insurance subsidiaries. In

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addition, certain catastrophes could result in both property and non-property claims from the same event. A severe catastrophe or a series of catastrophes could result in losses exceeding AFG's reinsurance protection and may have a material adverse impact on its results of operations or financial condition.

Volatility in crop prices, as a result of weather conditions or otherwise, could adversely impact AFG's results of operations.

Weather conditions, including too much moisture (flooding or excessive rain) or not enough moisture (droughts), and the level of crop prices in the commodities market heavily impact AFG's crop insurance business. These factors are inherently unpredictable and could result in significant volatility in the results of the crop insurance business from one year to the next. AFG's crop results could also be negatively impacted by pests and plant disease. A large decline in the commodity prices of one or more of the major crops that AFG insures could have a material adverse effect on AFG's results of operations or financial condition.

AFG's international operations exposes it to investment, political and economic risks, including foreign currency and credit risk.

AFG's international operations expose AFG to a number of additional risks. These risks include restrictions such as price controls, capital controls, currency exchange limits, ownership limits and other restrictive or anti-competitive governmental actions or requirements, which could have an adverse effect on AFG's business and reputation. AFG's business activities outside the United States may also be subject to political and economic risks, including foreign currency and credit risk.

AFG's business activities outside the United States subject AFG to additional domestic and foreign laws and regulations, including the Foreign Corrupt Practices Act, the UK Bribery Act and similar laws in other countries that prohibit the making of improper payments to foreign officials. Although AFG has policies and controls in place that are designed to ensure compliance with these laws, if those controls are ineffective and an employee or intermediary fails to comply with applicable laws and regulations, AFG could suffer civil and criminal penalties and AFG's business and reputation could be adversely affected. Some countries have laws and regulations that lack clarity and, even with local expertise and effective controls, it can be difficult to determine the exact requirements of, and potential liability under, the local laws. Failure to comply with local laws in a particular market may result in substantial liability and could have a significant and negative effect not only on AFG's business in that market but also on AFG's reputation generally.

Exposure to asbestos or environmental claims could materially adversely affect AFG's results of operations and financial condition.

AFG has asbestos and environmental ("A&E") exposures arising from its insurance operations and former railroad and manufacturing operations. Uncertainties surrounding the final resolution of these asbestos and environmental liabilities continue, and it is difficult to estimate AFG's ultimate exposure to such liabilities and related litigation. Establishing A&E liabilities is subject to uncertainties that are significantly greater than those presented by other types of liabilities. Uncertainties include the long delays between exposure and manifestation of any bodily injury or property damage, difficulty in identifying the source of the asbestos or environmental contamination, long reporting delays, the risks inherent in complex litigation and difficulty in properly allocating liability for the asbestos or environmental damage. As a result, A&E liabilities are subject to revision as new information becomes available and as claims are made and develop. Claimants continue to assert new and novel theories of recovery, and from time to time, there is proposed state and federal legislation regarding A&E liability, which would also affect AFG's exposure. If AFG has not established adequate reserves to cover future claims, AFG's results of operations and financial condition could be materially adversely affected.

Ineffective use of options in the fixed-indexed and variable-indexed annuity business could affect AFG's results of operations.

AFG's fixed-indexed and variable-indexed annuities provide policyholders with a crediting rate tied, in part, to the performance of an existing stock market or other financial index. AFG attempts to mitigate the risk in the index-based component of these products through the purchase and sale of call and put options on the appropriate index. AFG's strategy is designed so that the change in the fair value of the options will generally offset the economic change in the liabilities from the index participation. However, this strategy may not be fully effective at mitigating risk exposures in all market conditions or against all types of risk. In addition, AFG's use of options may not be sufficient to completely hedge the associated risks or AFG may decide not to hedge all of the risks to which it is exposed.

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Variations from the actuarial assumptions used to establish certain assets and liabilities in AFG's annuity business could adversely affect AFG's results of operations.

The earnings on AFG's annuity products depend significantly upon the extent to which actual experience is consistent with the assumptions used in setting reserves and establishing and amortizing deferred policy acquisition costs. These assumptions relate to investment yields (and spreads over fixed annuity crediting rates), benefit utilization rates, equity market performance, the cost of options used in the fixed-indexed (including variable-indexed) annuity business, mortality, surrenders, annuitizations and other withdrawals. Developing such assumptions is complex and involves information obtained from company-specific and industry-wide data, as well as general economic information. These assumptions, and therefore AFG's results of operations, could be negatively impacted by changes in any of the factors listed above.

The modification or elimination of the London Inter-Bank Offering Rate may adversely affect AFG's results of operations.

The modification or elimination of the London Inter-Bank Offered Rate ("LIBOR"), a long-standing benchmark interest rate for floating-rate financial contracts, may adversely affect the interest rates on and fair value of AFG's floating rate investments, interest rate swaps, Federal Home Loan Bank advances and any other assets or liabilities whose value is tied to LIBOR. In addition, the majority of the assets and liabilities of the collateralized loan obligations that AFG manages and consolidates are tied to LIBOR. On July 27, 2017, the U.K. Financial Conduct Authority announced that it will no longer persuade or compel banks to submit rates for the calculation of LIBOR after 2021. However, it remains unclear if, how and in what form, LIBOR will continue to exist. Proposals for alternative reference rates for dollars and other currencies have been announced or have already begun publication. Markets are slowly developing in response to these new rates but questions around liquidity in these alternative reference rates and how to appropriately adjust these alternative reference rates to eliminate any economic value transfer at the time of transition persist. At this time, AFG cannot predict the overall effect of the modification or elimination of LIBOR or the establishment of alternative benchmark rates.

Changes to existing accounting standards could adversely impact AFG's reported results of operations.

As a U.S.-based SEC registrant, AFG prepares its financial statements in accordance with GAAP, as promulgated by the Financial Accounting Standards Board, subject to the accounting-related rules and interpretations of the SEC. Changes in accounting standards, particularly those that specifically apply to insurance company operations, may impact AFG's reported financial results and could cause increased volatility in reported earnings, resulting in other adverse impacts on AFG's ratings and cost of capital, and decrease the understandability of AFG's financial results as well as the comparability of AFG's reported results with other insurers.

As a holding company, AFG is dependent on the operations of its insurance company subsidiaries to meet its obligations and pay future dividends.

AFG is a holding company and a legal entity separate and distinct from its insurance company subsidiaries. As a holding company without significant operations of its own, AFG's principal sources of funds are dividends and other distributions from its insurance company subsidiaries. State insurance laws differ from state to state but, absent advance regulatory approval, restrict the maximum amount of dividends that may be paid by an insurer to its shareholders in any twelve-month period. AFG's rights to participate in any distribution of assets of its insurance company subsidiaries are subject to prior claims of policyholders and creditors (except to the extent that its rights, if any, as a creditor are recognized). Consequently, AFG's ability to pay its debts, expenses and dividends to its shareholders may be limited.

Statutory capital requirements set by the NAIC and the various state insurance regulatory bodies establish regulations that provide minimum capitalization requirements based on risk-based capital (“RBC”) ratios for insurance companies. Statutory surplus and RBC ratios may change in a given year based on a number of factors, including statutory earnings/losses, reserve changes, excess capital held to support growth, equity market and interest rate changes, the value of investment securities, and changes to the RBC formulas. Increases in the amount of capital or reserves that AFG’s larger insurance subsidiaries are required to hold could reduce the amount of future dividends such subsidiaries are able to distribute to the holding company or require capital contributions. Any reduction in the RBC ratios of AFG’s insurance subsidiaries could also adversely affect their financial strength ratings as determined by rating agencies.

Adverse developments in the financial markets may limit AFG’s access to capital.

Financial markets in the U.S. and elsewhere can experience extreme volatility, which exerts downward pressure on stock prices and limits access to the equity and debt markets for certain issuers, including AFG. AFG can borrow up to \$500 million under

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its revolving credit facility, which expires in June 2021. In addition, AFG's access to funds through this facility is dependent on the ability of its banks to meet their funding commitments. There were no borrowings outstanding under AFG's bank credit line or any other parent company short-term borrowing arrangements during 2018. If AFG cannot obtain adequate capital or sources of credit on favorable terms, or at all, its business, operating results and financial condition would be adversely affected.

AFG may suffer losses from litigation, which could materially and adversely affect AFG's financial condition and business operations.

AFG, primarily in its property and casualty insurance operations and historical operations, is involved in litigation. Litigation by nature is unpredictable, and the outcome of any case is uncertain and could result in liabilities that vary from the amounts AFG has currently recorded. Pervasive or significant changes in the judicial environment relating to matters such as trends in the size of jury awards, developments in the law relating to the liability of insurers or tort defendants, and rulings concerning the availability or amount of certain types of damages could cause AFG's ultimate liabilities to change from current expectations. Changes in federal or state tort litigation laws or other applicable law could have a similar effect. It is not possible to predict changes in the judicial and legislative environment, including in connection with asbestos and environmental claims. AFG's business, financial condition, results of operations and liquidity could also be adversely affected if judicial or legislative developments cause AFG's ultimate liabilities to increase from current expectations.

Certain shareholders exercise substantial control over AFG's affairs, which may impede a change of control transaction.

Carl H. Lindner III and S. Craig Lindner are each Co-Chief Executive Officers and Directors of AFG. Together, Carl H. Lindner III and S. Craig Lindner beneficially own 10.9% of AFG's outstanding Common Stock as of February 1, 2019. Other members of the Lindner family own, directly or through trusts, a significant number of additional shares of AFG Common Stock. As a result, the Lindner family has the ability to exercise significant influence over AFG's management, including over matters requiring shareholder approval. Such concentrated ownership could prevent an acquisition of AFG at a price which other shareholders may find attractive.

The price of AFG Common Stock may fluctuate significantly, which may make it difficult for holders to resell common stock when they want or at a price they find attractive.

The price of AFG's Common Stock, which is listed on the NYSE, constantly changes. During 2018, AFG's Common Stock traded at prices ranging between \$84.18 and \$121.69. AFG's Common Stock price can fluctuate as a result of a variety of factors, many of which are beyond its control. These factors include but are not limited to:

- actual or anticipated variations in quarterly operating results;
- actual or anticipated changes in the dividends paid on AFG Common Stock;
- rating agency actions;
- recommendations by securities analysts;
- significant acquisitions or business combinations, strategic partnerships, joint ventures or capital commitments by or involving AFG or its competitors;
- operating and stock price performance of other companies that investors deem comparable to AFG;
- news reports relating to trends, concerns and other issues in AFG's lines of business;
- general economic conditions, including volatility in the financial markets; and
- geopolitical conditions such as acts or threats of terrorism or military conflicts.

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ITEM 2

Properties

AFG and its insurance subsidiaries lease the majority of their office and storage facilities in numerous cities throughout the United States and internationally, including the Company's headquarters in Cincinnati, Ohio. Subsidiaries of AFG own several other buildings in downtown Cincinnati. AFG and its affiliates occupy approximately half of the aggregate 670,000 square feet of commercial and office space in these buildings. A property and casualty insurance subsidiary occupies approximately 93% of the 281,000 square feet of rentable office space on 17.5 acres of land that it owns in Richfield, Ohio. See Item 1 — Business — “Other Operations” for a discussion of AFG's other commercial real estate operations.

ITEM 3

Legal Proceedings

AFG and its subsidiaries are involved in litigation from time to time, generally arising in the ordinary course of business. This litigation may include, but is not limited to, general commercial disputes, lawsuits brought by policyholders, employment matters, reinsurance collection matters and actions challenging certain business practices of insurance subsidiaries. Except for the following, management believes that none of the litigation meets the threshold for disclosure under this Item.

AFG's insurance company subsidiaries and its 100%-owned subsidiary, American Premier Underwriters (including its subsidiaries, “American Premier”), are parties to litigation and receive claims alleging injuries and damages from asbestos, environmental and other substances and workplace hazards and have established loss accruals for such potential liabilities. None of such litigation or claims is individually material to AFG; however, the ultimate loss for these claims may vary materially from amounts currently recorded as the conditions surrounding resolution of these claims continue to change.

American Premier is a party or named as a potentially responsible party in a number of proceedings and claims by regulatory agencies and private parties under various environmental protection laws, including the Comprehensive Environmental Response, Compensation and Liability Act, seeking to impose responsibility on American Premier for hazardous waste or discharge remediation costs at certain railroad sites formerly owned by its predecessor, Penn Central Transportation Company (“PCTC”), and at certain other sites where hazardous waste or discharge allegedly generated by PCTC's railroad operations and American Premier's former manufacturing operations is present. It is difficult to estimate American Premier's liability for remediation costs at these sites for a number of reasons, including the number and financial resources of other potentially responsible parties involved at a given site, the varying availability of evidence by which to allocate responsibility among such parties, the wide range of costs for possible remediation alternatives, changing technology and the period of time over which these matters develop. Nevertheless, American Premier believes that its accruals for potential environmental liabilities are adequate to cover the probable amount of such liabilities, based on American Premier's estimates of remediation costs and related expenses and its estimates of the portions of such costs that will be borne by other parties. Such estimates are based on information currently available to American Premier and are subject to future change as additional information becomes available.

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PART II

ITEM 5

Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities
AFG Common Stock is listed and traded on the New York Stock Exchange under the symbol AFG. There were approximately 5,500 shareholders of record of AFG Common Stock at February 1, 2019.

Issuer Purchases of Equity Securities AFG repurchased shares of its Common Stock during 2018 as follows:

| | Total Number of Shares Purchased | Average Price Paid Per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Maximum Number of Shares that May Yet be Purchased Under the Plans or Programs (a) |
|-------------------|---|------------------------------------|---|---|
| First Nine Months | — | \$ — | — | 4,132,838 |
| Fourth Quarter: | | | | |
| October | 12,500 | 99.48 | 12,500 | 4,120,338 |
| November | — | — | — | 4,120,338 |
| December | 53,089 | 91.95 | 53,089 | 3,000,000 |
| Total | 65,589 | \$ 93.38 | 65,589 | |

Represents the remaining shares that may be repurchased under the Plans authorized by AFG's Board of Directors in December 2014 and February 2016. On December 31, 2018, 1,067,249 shares that were authorized in (a) December 2014 expired. In February 2019, AFG's Board of Directors authorized the repurchase of two million additional shares.

In addition, AFG acquired 26,520 shares of its Common Stock (at an average of \$111.91 per share) in the first nine months of 2018 in connection with its stock incentive plans.

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Stock Performance Graph The following graph compares performance of AFG Common Stock during the five year period from December 31, 2013 through December 31, 2018 with the performance of (i) the S&P 500 Composite Stock Index (“S&P 500 Index”), (ii) the S&P 500 Property & Casualty Insurance Index and (iii) the S&P 500 Life & Health Index. The graph assumes that an initial investment of \$100 was made on December 31, 2013 and all dividends were reinvested. The stock price performance presented below is not intended to be indicative of future price performance.

| | As of December 31, | | | | | |
|---------------------------------|--------------------|-------|-------|-------|-------|-------|
| | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
| AFG | \$100 | \$109 | \$133 | \$167 | \$216 | \$188 |
| S&P 500 Index | 100 | 114 | 115 | 129 | 157 | 150 |
| S&P 500 P&C Index (b) | 100 | 116 | 127 | 147 | 180 | 171 |
| S&P 500 Life & Health Index (c) | 100 | 102 | 96 | 119 | 139 | 110 |

Cumulative total shareholder return measures the performance of a company’s stock (or an index) over time and is (a) calculated as the change in the stock price plus cumulative dividends (assuming dividends are reinvested) over a specific period of time divided by the stock price at the beginning of the time period.

The S&P 500 Property & Casualty Insurance Index included the following companies at December 31, 2018 (b)(weighted by market capitalization): The Allstate Corporation, Chubb Limited, Cincinnati Financial Corporation, The Progressive Corporation and The Travelers Companies, Inc.

The S&P 500 Life & Health Insurance Index included the following companies at December 31, 2018 (weighted (c) by market capitalization): Aflac Incorporated, Brighthouse Financial Inc., Lincoln National Corporation, MetLife Inc., Principal Financial Group, Inc., Prudential Financial, Inc., Torchmark Corporation and Unum Group.

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ITEM 6

Selected Financial Data

The following table sets forth certain data for the periods indicated (dollars in millions, except per share data).

| | 2018 | 2017 | 2016 | 2015 | 2014 |
|--|----------|----------|----------|----------|----------|
| Earnings Statement Data: | | | | | |
| Total revenues | \$7,150 | \$6,865 | \$6,498 | \$6,145 | \$5,733 |
| Earnings before income taxes | 639 | 724 | 787 | 565 | 626 |
| Net earnings, including noncontrolling interests | 517 | 477 | 668 | 370 | 406 |
| Less: Net earnings (loss) attributable to noncontrolling interests | (13 |) 2 | 19 | 18 | (46 |
| Net earnings attributable to shareholders | 530 | 475 | 649 | 352 | 452 |
| Earnings attributable to shareholders per Common Share: | | | | | |
| Basic — GAAP | \$5.95 | \$5.40 | \$7.47 | \$4.02 | \$5.07 |
| Diluted — GAAP | 5.85 | 5.28 | 7.33 | 3.94 | 4.97 |
| Core net operating earnings per share (diluted) (a) | 8.40 | 6.55 | 6.03 | 5.44 | 4.82 |
| Cash dividends paid per share of Common Stock (b) | \$4.45 | \$4.7875 | \$2.1525 | \$2.03 | \$1.91 |
| Ratio of earnings to fixed charges including annuity benefits (c) | 1.54 | 1.72 | 1.85 | 1.66 | 1.90 |
| Balance Sheet Data: | | | | | |
| Cash and investments | \$48,498 | \$46,048 | \$41,433 | \$37,736 | \$36,210 |
| Total assets | 63,456 | 60,658 | 55,072 | 49,837 | 47,513 |
| Property and casualty insurance reserves: | | | | | |
| Unpaid losses and loss adjustment expenses | 9,741 | 9,678 | 8,563 | 8,127 | 7,872 |
| Unearned premiums | 2,595 | 2,410 | 2,171 | 2,060 | 1,956 |
| Annuity benefits accumulated | 36,616 | 33,316 | 29,907 | 26,622 | 23,764 |
| Life, accident and health reserves | 635 | 658 | 691 | 705 | 2,175 |
| Long-term debt | 1,302 | 1,301 | 1,283 | 998 | 1,039 |
| Shareholders' equity | 4,970 | 5,330 | 4,916 | 4,592 | 4,879 |
| Less: | | | | | |
| Net unrealized gains related to fixed maturities (d) | 72 | 606 | 299 | 279 | 604 |
| Appropriated retained earnings | — | — | — | — | (2 |
| Adjusted shareholders' equity (e) | 4,898 | 4,724 | 4,617 | 4,313 | 4,277 |
| Book value per share | \$55.66 | \$60.38 | \$56.55 | \$52.50 | \$55.62 |
| Adjusted book value per share (e) | 54.86 | 53.51 | 53.11 | 49.32 | 48.76 |

(a) AFG's net earnings per share (diluted), determined in accordance with GAAP, includes certain items that may not be indicative of its ongoing core operations. AFG believes that its core net operating earnings per share provides management, financial analysts, rating agencies and investors with an understanding of the results from the ongoing operations of the Company by excluding the impact of net realized investment gains and losses and other items that are not necessarily indicative of operating trends. AFG's management uses core net operating earnings to evaluate financial performance against historical results because it believes this provides a more comparable measure of its continuing business. Core net operating earnings is also used by AFG's management as a basis for strategic planning and forecasting. Core net operating earnings per share (diluted) is a non-GAAP financial measure. See Item 7 — Management's Discussion and Analysis — "Results of Operations — General" for additional details including a reconciliation of core net operating earnings per share (diluted) to net earnings available to shareholders

(diluted) computed in accordance with GAAP.

(b) AFG increased its quarterly dividend in October of each of the last five years as follows: increased to \$0.40 per share in 2018, \$0.35 per share in 2017, \$0.3125 per share in 2016, \$0.28 per share in 2015, and \$0.25 per share in 2014. In addition, AFG paid special cash dividends of \$3.00 per share in 2018, \$3.50 per share in 2017 and \$1.00 per share in 2016, 2015 and 2014.

(c) Fixed charges are computed on a “total enterprise” basis. For purposes of calculating the ratios, “earnings” have been computed by adding to pretax earnings the fixed charges and the noncontrolling interests in earnings of subsidiaries having fixed charges and the undistributed equity in earnings or losses of investees. Fixed charges include interest (including annuity benefits as indicated), amortization of debt premium/discount and expense, preferred dividend and distribution requirements of subsidiaries and a portion of rental expense deemed to be representative of the interest factor. The ratio of earnings to fixed charges excluding annuity benefits was 7.86, 7.67, 8.62, 6.58 and 7.95 for 2018, 2017, 2016, 2015 and 2014, respectively. Although the ratio of earnings to fixed charges excluding annuity benefits is not required or encouraged to be disclosed under Securities and

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Exchange Commission rules, some investors and lenders may not consider interest credited to annuity policyholders' accounts a borrowing cost for an insurance company, and accordingly, believe this ratio is meaningful.

Net unrealized gains related to fixed maturities, which includes net unrealized gains (losses) on cash flow hedges, (d) is part of accumulated other comprehensive income and is shown net of related adjustments to deferred policy acquisition costs and certain liabilities in the annuity, long-term care and life businesses.

Adjusted shareholders' equity and adjusted book value per share exclude appropriated retained earnings and net unrealized gains related to fixed maturity securities. Management believes that investors find a measurement of shareholders' equity excluding these items to be meaningful as (i) the unrealized gains related to fixed maturities (e) fluctuates with changes in interest rates in a way that is primarily only meaningful to AFG if it sells those investments and (ii) appropriated retained earnings represented amounts that will ultimately inure to the debt holders of the collateralized loan obligations managed by AFG as reported under accounting guidance that was no longer applicable beginning in 2016.

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ITEM 7

Management's Discussion and Analysis of Financial Condition and Results of Operations

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GENERAL

Following is a discussion and analysis of the financial statements and other statistical data that management believes will enhance the understanding of AFG's financial condition and results of operations. This discussion should be read in conjunction with the financial statements beginning on page F-1.

OVERVIEW

Financial Condition

AFG is organized as a holding company with almost all of its operations being conducted by subsidiaries. AFG, however, has continuing cash needs for administrative expenses, the payment of principal and interest on borrowings, shareholder dividends, and taxes. Therefore, certain analyses are most meaningfully presented on a parent only basis while others are best done on a total enterprise basis. In addition, because most of its businesses are financial in nature, AFG does not prepare its consolidated financial statements using a current-noncurrent format. Consequently, certain traditional ratios and financial analysis tests are not meaningful.

At December 31, 2018, AFG (parent) held approximately \$223 million in cash and securities and had \$500 million available under a bank line of credit, which expires in June 2021.

Results of Operations

Through the operations of its subsidiaries, AFG is engaged primarily in property and casualty insurance, focusing on specialized commercial products for businesses, and in the sale of traditional fixed, fixed-indexed and variable-indexed annuities in the retail, financial institutions, broker-dealer and registered investment advisor markets.

AFG reported a fourth quarter 2018 net loss attributable to shareholders of \$29 million (\$0.33 per share, diluted) compared to net earnings attributable to shareholders of \$166 million (\$1.84 per share, diluted) in the fourth quarter of 2017, reflecting:

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net realized losses on securities in the fourth quarter of 2018 compared to net realized gains on securities in the fourth quarter of 2017. The 2018 period reflects the change in the fair value of equity securities that are required to be carried at fair value through net earnings under new accounting guidance adopted on January 1, 2018,

• lower earnings in the annuity segment,

• lower underwriting profit in the property and casualty insurance segment,

• higher net investment income in the property and casualty insurance segment,

• lower interest charges on borrowed money,

• lower holding company expenses,

• a lower corporate income tax rate,

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- the fourth quarter 2017 loss on retirement of debt,
- the fourth quarter 2017 tax benefit related to the Neon Underwriting Ltd. (“Neon”) restructuring, and
- the fourth quarter 2017 tax expense related to the change in the U.S. corporate tax rate.

Full year 2018 net earnings attributable to AFG’s shareholders were \$530 million (\$5.85 per share, diluted) compared to \$475 million (\$5.28 per share, diluted) in 2017, reflecting:

- higher underwriting profit in the property and casualty insurance segment due primarily to lower catastrophe losses and lower special charges to increase asbestos and environmental reserves,
- net realized losses on securities in 2018 compared to net realized gains on securities in 2017,
- higher net investment income in the property and casualty insurance segment,
- lower interest charges on borrowed money,
- lower holding company expenses,
- a lower corporate income tax rate,
- lower earnings in the annuity segment,
- income from the sale of real estate in 2017,
- the 2017 loss on retirement of debt,
- the fourth quarter 2017 tax benefit related to the Neon restructuring, and
- the fourth quarter 2017 tax expense related to the change in the U.S. corporate tax rate.

CRITICAL ACCOUNTING POLICIES

Significant accounting policies are summarized in Note A — “Accounting Policies” to the financial statements. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that can have a significant effect on amounts reported in the financial statements. As more information becomes known, these estimates and assumptions change and, thus, impact amounts reported in the future. The areas where management believes the degree of judgment required to determine amounts recorded in the financial statements is most significant are as follows:

- the establishment of insurance reserves, especially asbestos and environmental-related reserves,
- the recoverability of reinsurance,
- the recoverability of deferred acquisition costs,
- the measurement of the derivatives embedded in fixed-indexed and variable-indexed annuity liabilities,
- the establishment of asbestos and environmental reserves of former railroad and manufacturing operations, and
- the valuation of investments, including the determination of other-than-temporary impairments.

See “Liquidity and Capital Resources — Uncertainties” for a discussion of insurance reserves, recoverables from reinsurers, indexed annuity embedded derivatives and contingencies related to American Premier’s former operations and “Liquidity and Capital Resources — Investments” for a discussion of impairments on investments. Deferred policy acquisition costs (“DPAC”) and certain liabilities related to annuities are amortized in relation to the present value of expected gross profits on the policies. Assumptions considered in determining expected gross profits involve significant judgment and include management’s estimates of interest rates and investment spreads, surrenders, annuitizations, renewal premiums and mortality. Should actual experience require management to change its assumptions (commonly referred to as “unlocking”), a charge or credit would be recorded to adjust DPAC or annuity liabilities to the levels they would have been if the new assumptions had been used from the inception date of each policy.

LIQUIDITY AND CAPITAL RESOURCES

Ratios AFG’s debt to total capital ratio on a consolidated basis is shown below (dollars in millions). Management intends to maintain the ratio of debt to capital at or below 25% and intends to maintain the capital of its significant

insurance subsidiaries at or above levels currently indicated by rating agencies as appropriate for the current ratings.

| | December 31, | | | |
|------------------------------------|--------------|----------|---|--|
| | 2018 | 2017 | | |
| Principal amount of long-term debt | \$ 1,318 | \$ 1,318 | | |
| Total capital | 6,218 | 6,046 | | |
| Ratio of debt to total capital: | | | | |
| Including subordinated debt | 21.2 | % 21.8 | % | |
| Excluding subordinated debt | 16.4 | % 16.8 | % | |

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The ratio of debt to total capital is a non-GAAP measure that management believes is useful for investors, analysts and independent ratings agencies to evaluate AFG's financial strength and liquidity and to provide insight into how AFG finances its operations. In addition, maintaining a ratio of debt, excluding subordinated debt and debt secured by real estate (if any), to total capital of 35% or lower is a financial covenant in AFG's bank credit facility. The ratio is calculated by dividing the principal amount of AFG's long-term debt by its total capital, which includes long-term debt, noncontrolling interests and shareholders' equity (excluding unrealized gains (losses) related to fixed maturity investments).

AFG's ratio of earnings to fixed charges, including annuity benefits as a fixed charge, was 1.54 for the year ended December 31, 2018. Excluding annuity benefits, this ratio was 7.86. The ratio excluding annuity benefits is presented because interest credited to annuity policyholder accounts is not always considered a borrowing cost for an insurance company.

The NAIC's model law for risk based capital ("RBC") applies to both life and property and casualty companies. RBC formulas determine the amount of capital that an insurance company needs so that it has an acceptable expectation of not becoming financially impaired. At December 31, 2018, the capital ratios of all AFG insurance companies exceeded the RBC requirements.

Condensed Consolidated Cash Flows AFG's principal sources of cash include insurance premiums, income from its investment portfolio and proceeds from the maturities, redemptions and sales of investments. Insurance premiums in excess of acquisition expenses and operating costs are invested until they are needed to meet policyholder obligations or made available to the parent company through dividends to cover debt obligations and corporate expenses, and to provide returns to shareholders through share repurchases and dividends. Cash flows from operating, investing and financing activities as detailed in AFG's Consolidated Statement of Cash Flows are shown below (in millions):

| | Year ended December 31, | | |
|---|-------------------------|----------|----------|
| | 2018 | 2017 | 2016 |
| Net cash provided by operating activities | \$2,083 | \$1,804 | \$1,150 |
| Net cash used in investing activities | (5,350) | (3,292) | (2,981) |
| Net cash provided by financing activities | 2,444 | 1,719 | 2,718 |
| Net change in cash and cash equivalents | \$(823) | \$231 | \$887 |

Net Cash Provided by Operating Activities AFG's property and casualty insurance operations typically produce positive net operating cash flows as premiums collected and investment income exceed policy acquisition costs, claims payments and operating expenses. AFG's net cash provided by operating activities is impacted by the level and timing of property and casualty premiums, claim and expense payments and recoveries from reinsurers. AFG's annuity operations typically produce positive net operating cash flows as investment income exceeds acquisition costs and operating expenses. Interest credited on annuity policyholder funds is a non-cash increase in AFG's annuity benefits accumulated liability and annuity premiums, benefits and withdrawals are considered financing activities due to the deposit-type nature of annuities. Cash flows provided by operating activities also include the activity of AFG's managed investment entities (collateralized loan obligations) other than those activities included in investing or financing activities. The changes in the assets and liabilities of the managed investment entities included in operating activities increased cash flows from operating activities by \$148 million in 2018, increased cash flows from operating activities by \$60 million in 2017 and reduced cash flows from operating activities by \$279 million in 2016, accounting for a \$88 million increase in cash flows from operating activities in 2018 compared to 2017 and a \$339 million increase in cash flows from operating activities in 2017 compared to 2016. As discussed in Note A — "Accounting Policies — Managed Investment Entities" to the financial statements, AFG has no right to use the CLO assets and no obligation to pay the CLO liabilities and such assets and liabilities are shown separately in AFG's Balance Sheet. Excluding the impact of the managed investment entities, net cash provided by operating activities was \$1.94 billion, \$1.74 billion and \$1.43 billion in 2018, 2017 and 2016, respectively.

Net Cash Used in Investing Activities AFG's investing activities consist primarily of the investment of funds provided by its property and casualty and annuity businesses. Net cash used in investing activities was \$5.35 billion in 2018 compared to \$3.29 billion in 2017, an increase of \$2.06 billion. As discussed below (under net cash provided by financing activities), AFG's annuity group had net cash flows from annuity policyholders of \$2.76 billion in 2018 and \$1.99 billion in 2017, which is the primary source of AFG's cash used in investing activities. In addition, AFG's cash on hand decreased by \$823 million during 2018 as AFG invested a large portion of its cash on hand at December 31, 2017. In addition to the investment of funds provided by the insurance operations, investing activities also include the purchase and disposal of managed investment entity investments, which are presented separately in AFG's Balance Sheet. Net investment activity in the managed investment entities was a \$169 million use of cash in 2018 compared to a \$205 million use of cash in 2017, accounting for a \$36 million

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decrease in net cash used in investing activities in 2018 compared to 2017. See Note A — “Accounting Policies — Managed Investment Entities” and Note H — “Managed Investment Entities” to the financial statements.

Net cash used in investing activities was \$3.29 billion in 2017 compared to \$2.98 billion in 2016, an increase of \$311 million. Purchases of fixed maturities and equity securities exceeded maturities, redemptions and sales by \$2.95 billion in 2017 compared to \$2.04 billion in 2016, accounting for a \$912 million increase in cash used in investing activities in 2017 compared to 2016. Settlements of equity index call options exceeded purchases by \$285 million in 2017 compared to purchases exceeding settlements by \$110 million in 2016, accounting for a \$395 million decrease in cash used in investing activities. In general, purchases of equity index call options have increased due to growth in the fixed-indexed annuity business while proceeds from settlements of equity options are impacted by the performance of the stock market during the term of the options. Net investment activity in the managed investment entities was a \$205 million use of cash in 2017 compared to a \$364 million use of cash in 2016, accounting for a \$159 million decrease in net cash used in investing activities in 2017 compared to 2016.

Net Cash Provided by Financing Activities AFG’s financing activities consist primarily of transactions with annuity policyholders, issuances and retirements of long-term debt, repurchases of common stock and dividend payments. Net cash provided by financing activities was \$2.44 billion in 2018 compared to \$1.72 billion in 2017, an increase of \$725 million. Annuity receipts exceeded annuity surrenders, benefits, withdrawals and transfers by \$2.76 billion in 2018 compared to \$1.99 billion in 2017, resulting in a \$773 million increase in net cash provided by financing activities in 2018 compared to 2017. During 2018, AFG had no additional long-term borrowings or repayments as compared to \$712 million of additional long-term debt borrowings and \$745 million of debt repayments in 2017. During 2018, AFG repurchased \$6 million of its Common Stock compared to no shares in 2017. In addition to its regular quarterly cash dividends, AFG paid special cash dividends of \$3.00 per share and \$3.50 per share of American Financial Group Common Stock in 2018 and 2017, respectively, which resulted in total cash dividends of \$394 million in 2018 compared to \$417 million in 2017. Financing activities also include issuances and retirements of managed investment entity liabilities, which are nonrecourse to AFG and presented separately in AFG’s Balance Sheet. Issuances of managed investment entity liabilities exceeded retirements by \$48 million in 2018 compared to \$146 million in 2017, accounting for a \$98 million decrease in net cash provided by financing activities in 2018 compared to 2017. See Note A — “Accounting Policies — Managed Investment Entities” and Note H — “Managed Investment Entities” to the financial statements.

Net cash provided by financing activities was \$1.72 billion in 2017 compared to \$2.72 billion in 2016, a decrease of \$999 million. Annuity receipts exceeded annuity surrenders, benefits, withdrawals and transfers by \$1.99 billion in 2017 compared to \$2.35 billion in 2016, resulting in a \$362 million decrease in net cash provided by financing activities in 2017 compared to 2016. In 2017, AFG issued \$590 million of 4.50% Senior Notes due in 2047 and \$125 million of 3.50% Senior Notes due in 2026, the net proceeds of which contributed \$712 million to net cash provided by financing activities in 2017 compared to net proceeds from additional long-term borrowings of \$302 million in 2016, which accounted for a \$410 million increase in cash provided by financing activities in 2017 compared to 2016. Redemptions of long-term debt were a \$745 million use of cash in 2017 and an \$18 million use of cash in 2016, which accounted for a \$727 million decrease in net cash provided by financing activities in 2017 compared to 2016. There were no shares of AFG Common Stock repurchased in 2017 compared to \$133 million repurchased in 2016. In addition to its regular quarterly cash dividends, AFG paid special cash dividends of \$3.50 per share and \$1.00 per share of American Financial Group Common Stock in 2017 and 2016, respectively, which resulted in total cash dividends of \$417 million in 2017 compared to \$185 million in 2016. Additionally, in 2016, \$315 million was used to fund the acquisition of the noncontrolling interest in National Interstate Corporation. Issuances of managed investment entity liabilities exceeded retirements by \$146 million in 2017 compared to \$693 million in 2016, accounting for a \$547 million decrease in net cash provided by financing activities in 2017 compared to 2016.

Parent and Subsidiary Liquidity

Parent Holding Company Liquidity Management believes AFG has sufficient resources to meet its liquidity requirements. If funds generated from operations, including dividends, tax payments and borrowings from subsidiaries, are insufficient to meet fixed charges in any period, AFG would be required to utilize parent company cash and marketable securities or to generate cash through borrowings, sales of other assets, or similar transactions.

AFG can borrow up to \$500 million under its revolving credit facility which expires in June 2021. Amounts borrowed under this agreement bear interest at rates ranging from 1.00% to 1.875% (currently 1.375%) over LIBOR based on AFG's credit rating. There were no borrowings under this agreement, or under any other parent company short-term borrowing arrangements, during 2018.

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In 2018, AFG paid special cash dividends of \$3.00 per share of AFG Common Stock (\$1.50 per share in May and November) totaling approximately \$267 million and repurchased 65,589 shares of its Common Stock for \$6 million.

In June 2017, AFG issued \$350 million of 4.50% Senior Notes due in June 2047. Net proceeds from the offering were used to redeem AFG's \$230 million outstanding principal amount of 6-3/8% Senior Notes due in June 2042, at par value in June 2017 and AFG's \$125 million outstanding principal amount of 5-3/4% Senior Notes due in August 2042 at par value in August 2017.

In November 2017, AFG issued an additional \$240 million of 4.50% Senior Notes due in 2047 and \$125 million of 3.50% Senior Notes due in 2026. The net proceeds of the offering were used to redeem AFG's \$350 million outstanding principal amount of 9-7/8% Senior Notes due in June 2019 for \$388 million (including a make-whole premium of \$38 million) in December 2017.

In 2017, AFG paid special cash dividends of \$3.50 per share of AFG Common Stock (\$1.50 per share in May and \$2.00 per share in November) totaling approximately \$308 million.

In November 2016, AFG acquired the 49% of National Interstate Corporation ("NATL") not previously owned by AFG's wholly-owned subsidiary, Great American Insurance Company ("GAI") for \$315 million (\$32.00 per share) in cash in a merger transaction. In addition, NATL paid a one-time special cash dividend of \$0.50 per share to its shareholders immediately prior to the merger closing (\$5 million was paid to noncontrolling shareholders). See Note B — "Acquisitions and Sale of Businesses" to the financial statements.

In August 2016, AFG issued \$300 million of 3.50% Senior Notes due 2026. AFG used the net proceeds from the offering to fund a portion of the acquisition of NATL mentioned above.

During 2016, AFG repurchased 1.9 million shares of its Common Stock for \$133 million. In December 2016, AFG paid a special cash dividend of \$1.00 per share of AFG Common Stock totaling approximately \$87 million.

All debentures and notes issued by AFG are rated investment grade by two nationally recognized rating agencies. Under a currently effective shelf registration statement, AFG can offer additional equity or debt securities. The shelf registration provides AFG with flexibility to access the capital markets from time to time as market and other conditions permit.

Under a tax allocation agreement with AFG, its 80%-owned U.S. subsidiaries generally pay taxes to (or recover taxes from) AFG based on each subsidiary's contribution to amounts due under AFG's consolidated tax return.

Subsidiary Liquidity Great American Life Insurance Company ("GALIC"), a wholly-owned annuity subsidiary, is a member of the Federal Home Loan Bank of Cincinnati ("FHLB"). The FHLB makes advances and provides other banking services to member institutions, which provides the annuity operations with an additional source of liquidity. At December 31, 2018, GALIC had \$1.1 billion in outstanding advances from the FHLB (included in annuity benefits accumulated), bearing interest at rates ranging from 0.15% to 0.24% over LIBOR (average rate of 2.68% at December 31, 2018). While these advances must be repaid between 2019 and 2021 (\$445 million in 2019, \$40 million in 2020 and \$611 million in 2021), GALIC has the option to prepay all or a portion of the advances. GALIC has invested the proceeds from the advances in fixed maturity securities with similar expected lives as the advances for the purpose of earning a spread over the interest payments due to the FHLB. At December 31, 2018, GALIC estimated that it had additional borrowing capacity of approximately \$300 million from the FHLB.

In the fourth quarter of 2018, GALIC, AFG's primary annuity subsidiary, entered into a reinsurance treaty with Hannover Life Reassurance Company of America that transfers the risk of certain surrender activity in GALIC's

fixed-indexed annuity business. This treaty meets the statutory risk transfer rules and resulted in a \$510 million increase in statutory surplus (through an after-tax reserve credit). The treaty reduces statutory capital and surplus volatility related to GALIC's fixed-indexed annuity policies from stock market fluctuations, which could impact GALIC's risk-based capital and the amount of dividends available in future periods. Under GAAP, this transaction does not meet the GAAP insurance risk transfer criteria and did not have a material impact on AFG's financial statements.

The liquidity requirements of AFG's insurance subsidiaries relate primarily to the liabilities associated with their products as well as operating costs and expenses, payments of dividends and taxes to AFG and contributions of capital to their subsidiaries. Historically, cash flows from premiums and investment income have generally provided more than sufficient funds to meet these requirements. Funds received in excess of cash requirements are generally invested in additional marketable securities. In addition, the insurance subsidiaries generally hold a significant amount of highly liquid, short-term investments.

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The excess cash flow of AFG's property and casualty group allows it to extend the duration of its investment portfolio somewhat beyond that of its claim reserves.

In the annuity business, where profitability is largely dependent on earning a spread between invested assets and annuity liabilities, the duration of investments is generally maintained close to that of liabilities. In a rising interest rate environment, significant protection from withdrawals exists in the form of temporary and permanent surrender charges on AFG's annuity products. With declining rates, AFG receives some protection (from spread compression) due to the ability to lower crediting rates, subject to contractually guaranteed minimum interest rates ("GMIRs"). AFG began selling policies with GMIRs below 2% in 2003; almost all new business since late 2010 has been issued with a 1% GMIR. At December 31, 2018, AFG could reduce the average crediting rate on approximately \$28 billion of traditional fixed, fixed-indexed and variable-indexed annuities without guaranteed withdrawal benefits by approximately 119 basis points (on a weighted average basis). Annuity policies are subject to GMIRs at policy issuance. The table below shows the breakdown of annuity reserves by GMIR. The current interest crediting rates on substantially all of AFG's annuities with a GMIR of 3% or higher are at their minimum.

| GMIR | % of Reserves at December 31, | | |
|-----------------|----------------------------------|------|------|
| | 2018 | 2017 | 2016 |
| 1 — 1.99% | 79% | 76% | 72% |
| 2 — 2.99% | 4% | 5% | 6% |
| 3 — 3.99% | 8% | 10% | 12% |
| 4.00% and above | 9% | 9% | 10% |

Annuity benefits

| | | | |
|---------------------------|----------|----------|----------|
| accumulated (in millions) | \$36,616 | \$33,316 | \$29,907 |
|---------------------------|----------|----------|----------|

For statutory accounting purposes, equity securities of non-affiliates and equity call and put options used in the fixed-indexed annuity business are generally carried at fair value. At December 31, 2018, AFG's insurance companies owned publicly traded equity securities with a fair value of \$1.76 billion and equity index call and put options with a net fair value of \$183 million. Decreases in market prices could adversely affect the insurance group's capital, potentially impacting the amount of dividends available or necessitating a capital contribution. Conversely, increases in market prices could have a favorable impact on the group's dividend-paying capability.

AFG believes its insurance subsidiaries maintain sufficient liquidity to pay claims and benefits and operating expenses. In addition, these subsidiaries have sufficient capital to meet commitments in the event of unforeseen events such as reserve deficiencies, inadequate premium rates or reinsurer insolvencies. Nonetheless, changes in statutory accounting rules, significant declines in the fair value of the insurance subsidiaries' investment portfolios or significant ratings downgrades on these investments, could create a need for additional capital.

Condensed Parent Only Cash Flows AFG's parent holding company only condensed cash flows from operating, investing and financing activities are shown below (in millions):

| | Year ended December 31, | | |
|---|----------------------------|--------|--------|
| | 2018 | 2017 | 2016 |
| Net cash provided by operating activities | \$215 | \$578 | \$555 |
| Net cash provided by (used in) investing activities | 10 | (63) | (560) |
| Net cash provided by (used in) financing activities | (366) | (413) | 13 |
| Net change in cash and cash equivalents | \$(141) | \$102 | \$8 |

Parent Net Cash Provided by Operating Activities Parent holding company cash flows from operating activities consist primarily of dividends and tax payments received from AFG's insurance subsidiaries, reduced by tax payments to the IRS and holding company interest and other expenses. Parent holding company net cash provided by operating activities was \$215 million in 2018 compared to \$578 million in 2017 and \$555 million in 2016. The \$363 million decrease in net cash provided by operating activities in 2018 as compared to 2017 was due to lower dividends received from subsidiaries in 2018 as compared to 2017. The \$23 million increase in net cash provided by operating activities in 2017 as compared to 2016 was due to lower taxes paid, partially offset by lower dividends received from subsidiaries for those comparable periods.

Parent Net Cash Provided by (Used in) Investing Activities Parent holding company investing activities consist of capital contributions to and returns of capital from subsidiaries and, to a much lesser extent, parent company investment activity. Parent holding company net cash provided by investing activities was \$10 million in 2018 compared to net cash used in

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investing activities of \$63 million in 2017 and \$560 million in 2016. The \$10 million in net cash provided by investing activities in 2018 and the \$63 million of net cash used in investing activities in 2017 are significantly lower than the \$560 million in net cash used in investing activities in 2016 due primarily to 2016 capital contributions to a subsidiary to fund the acquisition of the noncontrolling interest in National Interstate Corporation.

Parent Net Cash Provided by (Used in) Financing Activities Parent company financing activities consist primarily of repurchases of AFG Common Stock, dividends to shareholders, the issuance and retirement of long-term debt and, to a lesser extent, proceeds from employee stock option exercises. Significant long-term debt and common stock transactions are discussed above under “Parent Holding Company Liquidity.” Parent holding company net cash used in financing activities was \$366 million in 2018 compared to \$413 million in 2017 and net cash provided by financing activities of \$13 million in 2016. The \$47 million decrease in net cash used in financing activities in 2018 as compared to 2017 reflects lower net redemptions of long-term debt in 2018 and decreased dividends (due primarily to special dividends of \$3.00 per share in 2018 compared to \$3.50 per share in 2017). The \$426 million increase in net cash used in financing activities in 2017 as compared to 2016 reflects higher net redemptions of long-term debt in 2017 and increased dividends (due primarily to special dividends of \$3.50 per share in 2017 compared to \$1.00 per share in 2016), partially offset by the absence of American Financial Group, Inc. Common Stock repurchases in 2017.

Contractual Obligations The following table shows an estimate (based on historical patterns and expected trends) of payments to be made for insurance reserve liabilities, as well as scheduled payments for major contractual obligations (in millions).

| | Total | Within One Year | 2-3 Years | 4-5 Years | More than 5 Years |
|--|----------|--------------------|-----------|-----------|----------------------|
| Annuities (a) | \$43,588 | \$ 3,493 | \$ 8,598 | \$ 9,341 | \$ 22,156 |
| Life, accident and health liabilities (a) | 1,363 | 114 | 195 | 199 | 855 |
| Property and casualty unpaid losses and loss adjustment expenses (b) | 9,741 | 2,630 | 2,572 | 1,101 | 3,438 |
| Long-term debt, including interest | 2,862 | 60 | 120 | 120 | 2,562 |
| Operating leases | 326 | 65 | 107 | 75 | 79 |
| Total | \$57,880 | \$ 6,362 | \$ 11,592 | \$ 10,836 | \$ 29,090 |

Amounts presented in the table represent estimated cash payments under such contracts, based on significant assumptions related to mortality, morbidity, lapse, renewal, retirement and annuitization. These assumptions also include interest and index crediting consistent with assumptions used to amortize DPAC and assess loss recognition. All estimated cash payments are undiscounted for the time value of money. As a result, total outflows (a) for all years exceed the corresponding liabilities of \$36.62 billion for annuity benefits accumulated and \$635 million for life, accident and health reserves included in AFG’s Balance Sheet as of December 31, 2018. Based on the same assumptions, AFG projects reinsurance recoveries related to life, accident and health reserves totaling \$651 million as follows: Within 1 year — \$65 million; 2-3 years — \$113 million; 4-5 years — \$85 million; and thereafter — \$388 million. Actual payments and their timing could differ significantly from these estimates. Dollar amounts and time periods are estimates based on historical net payment patterns applied to the gross reserves and do not represent actual contractual obligations. Based on the same assumptions, AFG projects (b) reinsurance recoveries related to these reserves totaling \$2.94 billion as follows: Within 1 year — \$800 million; 2-3 years — \$800 million; 4-5 years — \$300 million; and thereafter — \$1.04 billion. Actual payments and their timing could differ significantly from these estimates.

AFG has no material contractual purchase obligations or other long-term liabilities at December 31, 2018.

Off-Balance Sheet Arrangements See Note P — “Additional Information — Financial Instruments — Unfunded Commitments” to the financial statements.

Investments AFG attempts to optimize investment income while building the value of its portfolio, placing emphasis upon total long-term performance.

AFG's investment portfolio at December 31, 2018, contained \$42.00 billion in fixed maturity securities classified as available for sale and carried at fair value with unrealized gains and losses included in a separate component of shareholders' equity on an after-tax basis and \$105 million in fixed maturities classified as trading with holding gains and losses included in net investment income. In addition, AFG's investment portfolio includes \$1.63 billion in equity securities carried at fair value with

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holding gains and losses included in realized gains (losses) on securities and \$187 million in equity securities carried at fair value with holding gains and losses included in net investment income.

As detailed in Note E — “Investments — Net Unrealized Gain on Marketable Securities” to the financial statements, unrealized gains and losses on AFG’s fixed maturity securities are included in shareholders’ equity after adjustments for related changes in DPAC and certain liabilities related to annuity, long-term care and life businesses, noncontrolling interests and deferred income taxes. DPAC and certain other balance sheet amounts applicable to annuity, long-term care and life businesses are adjusted for the impact of unrealized gains or losses on investments as if these gains or losses had been realized, with corresponding increases or decreases (net of tax) included in accumulated other comprehensive income in AFG’s Balance Sheet.

Fixed income investment funds are generally invested in securities with intermediate-term maturities with an objective of optimizing total return while allowing flexibility to react to changes in market conditions. At December 31, 2018, the average life of AFG’s fixed maturities was about 6 years.

Fair values for AFG’s portfolio are determined by AFG’s internal investment professionals using data from nationally recognized pricing services as well as non-binding broker quotes. Fair values of equity securities are generally based on published closing prices. For mortgage-backed securities (“MBS”), which comprise approximately 9% of AFG’s fixed maturities, prices for each security are generally obtained from both pricing services and broker quotes. For the remainder of AFG’s fixed maturity portfolio, approximately 74% are priced using pricing services and the balance is priced primarily by using non-binding broker quotes. When prices obtained for the same security vary, AFG’s internal investment professionals select the price they believe is most indicative of an exit price.

The pricing services use a variety of observable inputs to estimate fair value of fixed maturities that do not trade on a daily basis. Based upon information provided by the pricing services, these inputs include, but are not limited to, recent reported trades, benchmark yields, issuer spreads, bids or offers, reference data, and measures of volatility. Included in the pricing of MBS are estimates of the rate of future prepayments and defaults of principal over the remaining life of the underlying collateral. Due to the lack of transparency in the process that brokers use to develop prices, valuations that are based on brokers’ prices are classified as Level 3 in the GAAP hierarchy unless the price can be corroborated, for example, by comparison to similar securities priced using observable inputs.

Valuation techniques utilized by pricing services and prices obtained from external sources are reviewed by AFG’s internal investment professionals who are familiar with the securities being priced and the markets in which they trade to ensure the fair value determination is representative of an exit price. To validate the appropriateness of the prices obtained, these investment managers consider widely published indices (as benchmarks), recent trades, changes in interest rates, general economic conditions and the credit quality of the specific issuers. In addition, AFG communicates directly with pricing services regarding the methods and assumptions used in pricing, including verifying, on a test basis, the inputs used by the services to value specific securities.

In general, the fair value of AFG’s fixed maturity investments is inversely correlated to changes in interest rates. The following table demonstrates the sensitivity of such fair values to reasonably likely changes in interest rates by illustrating the estimated effect on AFG’s fixed maturity portfolio and accumulated other comprehensive income that an immediate increase of 100 basis points in the interest rate yield curve would have at December 31, 2018 (dollars in millions). Effects of increases or decreases from the 100 basis points illustrated would be approximately proportional.

| | |
|---|------------|
| Fair value of fixed maturity portfolio | \$42,102 |
| Percentage impact on fair value of 100 bps increase in interest rates | (4.5 %) |
| Pretax impact on fair value of fixed maturity portfolio | \$(1,895) |
| Offsetting adjustments to deferred policy acquisition costs and other balance sheet amounts | 800 |

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| | |
|--|----------|
| Estimated pretax impact on accumulated other comprehensive income | (1,095) |
| Deferred income tax | 230 |
| Estimated after-tax impact on accumulated other comprehensive income | \$(865) |

Approximately 91% of the fixed maturities held by AFG at December 31, 2018, were rated “investment grade” (credit rating of AAA to BBB) by nationally recognized rating agencies. Investment grade securities generally bear lower yields and lower degrees of risk than those that are unrated and non-investment grade. Management believes that the high quality investment portfolio should generate a stable and predictable investment return.

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MBS are subject to significant prepayment risk due to the fact that, in periods of declining interest rates, mortgages may be repaid more rapidly than scheduled as borrowers refinance higher rate mortgages to take advantage of lower rates. Although interest rates have been low in recent years, tighter lending standards have resulted in fewer buyers being able to refinance the mortgages underlying much of AFG's non-agency residential MBS portfolio.

Summarized information for AFG's MBS (including those classified as trading) at December 31, 2018, is shown in the table below (dollars in millions). Agency-backed securities are those issued by a U.S. government-backed agency; Alt-A mortgages are those with risk profiles between prime and subprime. The average life of both the residential and commercial MBS is approximately 4-1/2 years.

| Collateral type | Amortized Cost | Fair Value | Fair Value as % of Cost | Unrealized Gain (Loss) | % Rated Investment Grade |
|------------------|----------------|------------|-------------------------|------------------------|--------------------------|
| Residential: | | | | | |
| Agency-backed | \$ 170 | \$ 168 | 99 % | \$ (2) | 100 % |
| Non-agency prime | 967 | 1,098 | 114 % | 131 | 28 % |
| Alt-A | 972 | 1,074 | 110 % | 102 | 31 % |
| Subprime | 369 | 406 | 110 % | 37 | 27 % |
| Commercial | 905 | 920 | 102 % | 15 | 94 % |
| | \$ 3,383 | \$ 3,666 | 108 % | \$ 283 | 49 % |

The National Association of Insurance Commissioners ("NAIC") assigns creditworthiness designations on a scale of 1 to 6 with 1 being the highest quality and 6 being the lowest quality. The NAIC retains third-party investment management firms to assist in the determination of appropriate NAIC designations for MBS based not only on the probability of loss (which is the primary basis of ratings by the major ratings firms), but also on the severity of loss and statutory carrying value. At December 31, 2018, 96% (based on statutory carrying value of \$3.33 billion) of AFG's MBS had an NAIC designation of 1.

Municipal bonds represented approximately 17% of AFG's fixed maturity portfolio at December 31, 2018. AFG's municipal bond portfolio is high quality, with 99% of the securities rated investment grade at that date. The portfolio is well diversified across the states of issuance and individual issuers. At December 31, 2018, approximately 78% of the municipal bond portfolio was held in revenue bonds, with the remaining 22% held in general obligation bonds. AFG does not own general obligation bonds issued by Puerto Rico.

Summarized information for the unrealized gains and losses recorded in AFG's Balance Sheet at December 31, 2018, is shown in the following table (dollars in millions). Approximately \$463 million of available for sale fixed maturity securities had no unrealized gains or losses at December 31, 2018.

| | Securities With Unrealized Gains | Securities With Unrealized Losses |
|---|----------------------------------|-----------------------------------|
| Available for Sale Fixed Maturities | | |
| Fair value of securities | \$ 19,866 | \$ 21,668 |
| Amortized cost of securities | \$ 19,103 | \$ 22,271 |
| Gross unrealized gain (loss) | \$ 763 | \$ (603) |
| Fair value as % of amortized cost | 104 % | 97 % |
| Number of security positions | 3,016 | 2,324 |
| Number individually exceeding \$2 million gain or loss | 52 | 25 |
| Concentration of gains (losses) by type or industry (exceeding 5% of unrealized): | | |

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| | | | |
|--|-------|-------|---|
| Mortgage-backed securities | \$294 | \$(11 |) |
| States and municipalities | 169 | (55 |) |
| Asset-backed securities | 130 | (100 |) |
| Banks, savings and credit institutions | 34 | (112 |) |
| Manufacturing | 24 | (80 |) |
| Insurance companies | 19 | (45 |) |
| Percentage rated investment grade | 87 | % 96 | % |

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The table below sets forth the scheduled maturities of AFG's available for sale fixed maturity securities at December 31, 2018, based on their fair values. Securities with sinking funds are reported at average maturity. Actual maturities may differ from contractual maturities because certain securities may be called or prepaid by the issuers.

| | Securities With Unrealized Gains | | Securities With Unrealized Losses | |
|--|---|---|--|---|
| Maturity | | | | |
| One year or less | 5 | % | 1 | % |
| After one year through five years | 25 | % | 16 | % |
| After five years through ten years | 25 | % | 41 | % |
| After ten years | 12 | % | 11 | % |
| | 67 | % | 69 | % |
| Asset-backed securities (average life of approximately 4-1/2 years) | 18 | % | 28 | % |
| Mortgage-backed securities (average life of approximately 4-1/2 years) | 15 | % | 3 | % |
| | 100 | % | 100 | % |

The table below (dollars in millions) summarizes the unrealized gains and losses on fixed maturity securities by dollar amount:

| | Aggregate Fair Value | Aggregate Unrealized Gain (Loss) | Fair Value as % of Cost | |
|---------------------------------------|----------------------------|--|-------------------------------|---|
| Fixed Maturities at December 31, 2018 | | | | |
| Securities with unrealized gains: | | | | |
| Exceeding \$500,000 (395 securities) | \$ 5,180 | \$ 464 | 110 | % |
| \$500,000 or less (2,621 securities) | 14,686 | 299 | 102 | % |
| | \$ 19,866 | \$ 763 | 104 | % |
| Securities with unrealized losses: | | | | |
| Exceeding \$500,000 (342 securities) | \$ 6,392 | \$ (353) | 95 | % |
| \$500,000 or less (1,982 securities) | 15,276 | (250) | 98 | % |
| | \$ 21,668 | \$ (603) | 97 | % |

The following table (dollars in millions) summarizes the unrealized losses for all securities with unrealized losses by issuer quality and the length of time those securities have been in an unrealized loss position:

| | Aggregate Fair Value | Aggregate Unrealized Loss | Fair Value as % of Cost | |
|--|----------------------------|---------------------------------|-------------------------------|---|
| Securities with Unrealized Losses at December 31, 2018 | | | | |
| Investment grade fixed maturities with losses for: | | | | |
| Less than one year (1,571 securities) | \$ 17,103 | \$ (387) | 98 | % |
| One year or longer (567 securities) | 3,648 | (167) | 96 | % |
| | \$ 20,751 | \$ (554) | 97 | % |
| Non-investment grade fixed maturities with losses for: | | | | |
| Less than one year (133 securities) | \$ 663 | \$ (24) | 97 | % |
| One year or longer (53 securities) | 254 | (25) | 91 | % |
| | \$ 917 | \$ (49) | 95 | % |

When a decline in the value of a specific investment is considered to be other-than-temporary, a provision for impairment is charged to earnings (accounted for as a realized loss) and the cost basis of that investment is reduced by

the amount of the charge. The determination of whether unrealized losses are other-than-temporary requires judgment based on subjective as well as objective factors. Factors considered and resources used by management include:

- a) whether the unrealized loss is credit-driven or a result of changes in market interest rates,
- b) the extent to which fair value is less than cost basis,
- c) cash flow projections received from independent sources,
- d) historical operating, balance sheet and cash flow data contained in issuer SEC filings and news releases,
- e) near-term prospects for improvement in the issuer and/or its industry,
- f) third party research and communications with industry specialists,

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- g) financial models and forecasts,
- h) the continuity of interest payments, maintenance of investment grade ratings and hybrid nature of certain investments,
- i) discussions with issuer management, and
- j) ability and intent to hold the investment for a period of time sufficient to allow for anticipated recovery in fair value.

Based on its analysis of the factors listed above, management believes AFG will recover its cost basis in the fixed maturity securities with unrealized losses and that AFG has the ability to hold the securities until they recover in value and had no intent to sell them at December 31, 2018. Although AFG has the ability to continue holding its fixed maturity investments with unrealized losses, its intent to hold them may change due to deterioration in the issuers' creditworthiness, decisions to lessen exposure to a particular issuer or industry, asset/liability management decisions, market movements, changes in views about appropriate asset allocation or the desire to offset taxable realized gains. Should AFG's ability or intent change with regard to a particular security, a charge for impairment would likely be required. While it is not possible to accurately predict if or when a specific security will become impaired, charges for other-than-temporary impairment could be material to results of operations in future periods. Significant declines in the fair value of AFG's investment portfolio could have a significant adverse effect on AFG's liquidity. For information on AFG's realized gains (losses) on securities, including charges for other-than-temporary impairment, see "Results of Operations — Consolidated Realized Gains (Losses) on Securities."

As discussed in Note A — "Accounting Policies — Investments" to the financial statements, effective January 1, 2018, all equity securities previously classified as "available for sale" are now required to be carried at fair value through net earnings instead of accumulated other comprehensive income and will therefore no longer be evaluated for other-than-temporary impairment.

Uncertainties As more fully explained in the following paragraphs, management believes that the areas posing the greatest risk of material loss are the adequacy of its insurance reserves and contingencies arising out of its former railroad and manufacturing operations.

Property and Casualty Insurance Reserves Estimating the liability for unpaid losses and loss adjustment expenses ("LAE") is inherently judgmental and is influenced by factors that are subject to significant variation. Determining the liability is a complex process incorporating input from many areas of the Company including actuarial, underwriting, pricing, claims and operations management.

The estimates of liabilities for unpaid claims and for expenses of investigation and adjustment of unpaid claims are based upon: (i) the accumulation of case estimates for losses reported prior to the close of the accounting periods on direct business written ("case reserves"); (ii) estimates received from ceding reinsurers and insurance pools and associations; (iii) estimates of claims incurred but not reported or "IBNR" (including possible development on known claims); (iv) estimates (based on experience) of expense for investigating and adjusting claims; and (v) the current state of law and coverage litigation.

The process used to determine the total reserve for liabilities involves estimating the ultimate incurred losses and LAE, adjusted for amounts already paid on the claims. The IBNR reserve is derived by first estimating the ultimate unpaid reserve liability and subtracting case reserves for loss and LAE. See Note O — "Insurance — Property and Casualty Insurance Reserves" to the financial statements for a discussion of the factors considered and actuarial methods used in determining management's best estimate of the ultimate liability for unpaid losses and LAE.

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The following table shows (in millions) the breakdown of AFG's property and casualty insurance reserves between case reserves, IBNR reserves and LAE reserves (estimated amounts required to adjust, record and settle claims, other than the claim payments themselves) at December 31, 2018 and gross written premiums for the year ended December 31, 2018.

| | Gross Loss Reserves | | | Total Reserves | Gross Written Premiums |
|--|---------------------|---------|---------|----------------|------------------------|
| | Case | IBNR | LAE | | |
| Statutory Line of Business | | | | | |
| Other liability — occurrence | \$679 | \$1,811 | \$440 | \$2,930 | \$1,000 |
| Workers' compensation | 1,022 | 1,413 | 332 | 2,767 | 1,293 |
| Other liability — claims made | 198 | 320 | 247 | 765 | 474 |
| Commercial auto/truck liability/medical | 236 | 333 | 109 | 678 | 413 |
| Special property (fire, allied lines, inland marine, earthquake) | 379 | 127 | 25 | 531 | 1,369 |
| Products liability — occurrence | 76 | 152 | 141 | 369 | 142 |
| Commercial multi-peril | 153 | 136 | 69 | 358 | 276 |
| Other lines | 191 | 366 | 86 | 643 | 1,091 |
| Total Statutory | 2,934 | 4,658 | 1,449 | 9,041 | 6,058 |
| Adjustments for GAAP: | | | | | |
| Foreign operations | 218 | 441 | 30 | 689 | 759 |
| Deferred gains on retroactive reinsurance | — | 34 | — | 34 | — |
| Loss reserve discounting | (9) | — | — | (9) | — |
| Other | (14) | — | — | (14) | 23 |
| Total Adjustments for GAAP | 195 | 475 | 30 | 700 | 782 |
| Total GAAP Reserves and Premiums | \$3,129 | \$5,133 | \$1,479 | \$9,741 | \$6,840 |

While current factors and reasonably likely changes in variable factors are considered in estimating the liability for unpaid losses, there is no method or system that can eliminate the risk of actual ultimate results differing from such estimates.

Following is a discussion of certain critical variables affecting the estimation of loss reserves of the more significant long-tail lines of business (asbestos and environmental liabilities are separately discussed below). Many other variables may also impact ultimate claim costs.

An important assumption underlying reserve estimates is that the cost trends implicitly built into development patterns will continue into the future. However, future results could vary due to an unexpected change in the underlying cost trends. This unexpected change could arise from a variety of sources including a general increase in economic inflation, inflation from social programs, new medical technologies, or other factors such as those listed below in connection with AFG's largest lines of business. It is not possible to isolate and measure the potential impact of just one of these variables, and future cost trends could be partially impacted by several such variables. However, it is reasonable to address the sensitivity of the reserves to potential impact from changes in these variables by measuring the effect of a possible overall 1% change in future cost trends that may be caused by one or more variables. Utilizing the effect of a 1% change in overall cost trends enables changes greater than 1% to be estimated by extrapolation. Each additional 1% change in the cost trend would increase the effect on net earnings by an amount slightly (about 5%) greater than the effect of the previous 1%. For example, if a 1% change in cost trends in a line of business would change net earnings by \$20 million, a 2% change would change net earnings by approximately \$41 million.

The estimated cumulative impact that a 1% change in cost trends in AFG's more significant lines of property and casualty business (exceeding 5% of total reserves) would have on net earnings is shown below (in millions).

| Line of business | Effect of 1% Change in Cost Trends |
|---|--|
| Other liability — occurrence | \$ 44 |
| Workers' compensation | 75 |
| Other liability — claims made | 12 |
| Commercial auto/truck liability/medical | 10 |

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The judgments and uncertainties surrounding management's reserve estimation process and the potential for reasonably possible variability in management's most recent reserve estimates may also be viewed by looking at how recent historical estimates of reserves have developed. The following table shows (dollars in millions) what the impact on AFG's net earnings would be on the more significant lines of business if the December 31, 2018, reserves (net of reinsurance) developed at the same rate as the average development of the most recent five years.

| | 5-yr. | | Net Reserves (b) | Effect on Net |
|---|---------|-------------|-------------------|---------------|
| | Average | Development | December 31, 2018 | Earnings (b) |
| | (a)(b) | | | |
| Other liability — occurrence | 2.2 | % | \$ 1,223 | \$ (27) |
| Workers' compensation | (2.8 | %) | 2,335 | 65 |
| Other liability — claims made | (2.0 | %) | 556 | 11 |
| Commercial auto/truck liability/medical | 2.0 | % | 478 | (10) |

(a) Adverse (favorable), net of tax effect.

(b) Excludes asbestos and environmental liabilities.

The following discussion describes key assumptions and important variables that affect the estimate of the reserve for loss and loss adjustment expenses of the more significant lines of business and explains what caused them to change from assumptions used in the preceding period.

Other Liability — Occurrence

This long-tail line of business consists of coverages protecting the insured against legal liability resulting from negligence, carelessness, or a failure to act causing property damage or personal injury to others. Some of the important variables affecting estimation of loss reserves for other liability — occurrence include:

- Litigious climate
- Unpredictability of judicial decisions regarding coverage issues
- Magnitude of jury awards
- Outside counsel costs
- Timing of claims reporting

AFG recorded adverse prior year reserve development of \$48 million in 2018 related to its other liability — occurrence coverage due to continued claim severity increases in excess and umbrella liability coverages as well as late emergence of excess workers' compensation and Texas non-subscribers workers' injury claims. AFG recorded adverse prior year reserve development of \$37 million in 2017 due to continued severity increases in New York contractor claims, as well as increased claim severity across other excess and umbrella liability coverages and general liability coverages. AFG recorded adverse prior year reserve development of \$61 million in 2016 due primarily to increased severity in New York contractor claims.

While management applies the actuarial methods mentioned above, more judgment is involved in arriving at the final reserve to be held. For recent accident years, more weight is given to the Bornhuetter-Ferguson method.

Workers' Compensation

This long-tail line of business provides coverage to employees who may be injured in the course of employment. Some of the important variables affecting estimation of loss reserves for workers' compensation include:

- Legislative actions and regulatory and legal interpretations
- Future medical cost inflation
- Economic conditions

- Frequency of reopening claims previously closed
- Advances in medical equipment and processes
- Pace and intensity of employee rehabilitation
- Changes in the use of pharmaceutical drugs
- Changes in longevity trends for permanently injured workers

Approximately 25% and 22% of AFG's workers' compensation reserves at December 31, 2018 relate to policies written in Florida and California, respectively. The *Castellanos v. Next Door Company* decision in Florida and the implementation of Senate Bill 863 in California are two examples of recent changes that impacted the workers' compensation operating environment and added difficulty and uncertainty to the estimation of related liabilities.

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AFG recorded favorable prior year reserve development of \$127 million in 2018 related to its workers' compensation coverage due to lower than anticipated claim severity in the southeastern United States and improving claim closure rates in California. AFG recorded favorable prior year reserve development of \$79 million in 2017 due to lower than anticipated claim severity and improving claim closure rates, particularly in the southeastern United States and California. AFG recorded favorable prior year reserve development of \$85 million in 2016 due to lower than anticipated claim severity and improving claim closure rates.

Other Liability — Claims Made

This long-tail line of business consists mostly of directors' and officers' liability ("D&O"). Some of the important variables affecting estimation of loss reserves for other liability — claims made include:

- Litigious climate
- Economic conditions
- Variability of stock prices
- Magnitude of jury awards

The general state of the economy and the variability of the stock price of the insured can affect the frequency and severity of shareholder class action suits and other situations that trigger coverage under D&O policies. For example, from 2008 to 2010, economic conditions led to higher frequency of claims, particularly in the D&O policies for small account and not-for-profit organizations. Since then, claim frequency has consistently decreased from its peak in 2010, offsetting increased claim severity.

AFG recorded favorable prior year reserve development of \$9 million in 2018, \$5 million in 2017 and \$24 million in 2016 on its D&O business as claim severity was less than expected across several prior accident years.

Commercial Auto/Truck Liability/Medical

This line of business is a mix of coverage protecting the insured against legal liability for property damage or personal injury to others arising from the operation of commercial motor vehicles. The property damage liability exposure is usually short-tail with relatively quick reporting and settlement of claims. The bodily injury and medical payments exposures are longer-tailed; although the claim reporting is relatively quick, the final settlement can take longer to achieve. Some of the important variables affecting estimation of loss reserves for commercial auto/truck liability/medical are similar to other liability — occurrence and include:

- Magnitude of jury awards
- Unpredictability of judicial decisions regarding coverage issues
- Litigious climate and trends
- Change in frequency of severe accidents
- Health care costs and utilization of medical services by injured parties

AFG recorded favorable prior year reserve development of \$26 million in 2018 for this line of business due primarily to lower than expected claim severity. AFG recorded adverse prior year reserve development of \$2 million in 2017 and \$28 million in 2016 for this line of business. Claim severity trends had been significantly higher than expected beginning with accident years 2010, but have more recently stabilized.

Reserves of Foreign Operations

Approximately \$417 million of the \$689 million in gross reserves of foreign operations relate to the operations of Neon Underwriting Limited, AFG's wholly-owned United Kingdom-based Lloyd's insurer. Neon writes cargo, cyber, financial lines, marine and energy liability, marine hull and war, personal accident and health, political and trade risk, professional indemnity, property reinsurance and terrorism and political violence insurance. Significant variables in

estimating Neon's loss reserves include:

- Litigious environment
- Magnitude of court awards
- Trends in claim costs, including medical cost inflation
- Global economic conditions
- Reporting lag from ceding property insurers

Neon recorded favorable prior year reserve development of \$26 million in 2018, due primarily to lower than expected emergence in assumed 2017 property catastrophe losses.

In the fourth quarter of 2017, Neon entered into a reinsurance to close agreement for 2015 and prior years of account, which transfers the responsibility for all of the liabilities that attach to the transferred year of account (gross reserves of \$385 million)

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at December 31, 2017) as well as any income due to the closing year of account in return for a premium. The reinsurance to close agreement eliminates any remaining reserve volatility from years of account 2015 and prior, including all medical malpractice exposure. As a result of the reinsurance to close transaction, Neon recorded favorable reserve development of approximately \$42 million, including \$24 million related to its ongoing lines of business and \$18 million that relates to the exited lines of business discussed below. In addition to the prior year reserve development related to the reinsurance to close transaction, Neon recorded favorable prior year reserve development of \$29 million in 2017 related to the retained loss reserves across all of Neon’s ongoing lines of business, particularly property lines.

During the second quarter of 2016, Neon completed a strategic review of its business under a new leadership team. As part of its strategic review, Neon sold and/or exited certain historical lines of business including its medical malpractice and general liability classes. As a result of Neon’s claims review of its exited lines of business, AFG recorded a charge of approximately \$65 million, including \$57 million to increase loss reserves (adverse development) primarily related to Neon’s medical malpractice and general liability lines. In addition to the prior year reserve development related to the Neon exited lines charge, Neon recorded adverse prior year reserve development of \$21 million in 2016, attributable to reserve strengthening in several lines of business, including political risk and personal accident.

Recoverables from Reinsurers and Availability of Reinsurance AFG is subject to credit risk with respect to its reinsurers, as reinsurance contracts do not relieve AFG of its liability to policyholders. To mitigate this risk, substantially all reinsurance is ceded to companies with investment grade S&P ratings or is secured by “funds withheld” or other collateral.

The availability and cost of reinsurance are subject to prevailing market conditions, which are beyond AFG’s control and which may affect AFG’s level of business and profitability. Although the cost of certain reinsurance programs may increase, management believes that AFG will be able to maintain adequate reinsurance coverage at acceptable rates without a material adverse effect on AFG’s results of operations. AFG’s gross and net combined ratios are shown in the table below.

See Item 1 — Business — “Property and Casualty Insurance Segment — Reinsurance” for more information on AFG’s reinsurance programs. For additional information on the effect of reinsurance on AFG’s historical results of operations see Note O — “Insurance — Reinsurance” to the financial statements.

The following table illustrates the effect that purchasing property and casualty reinsurance has had on AFG’s combined ratio over the last three years.

| | 2018 | 2017 | 2016 |
|-----------------------------|---------|---------|--------|
| Before reinsurance (gross) | 94.1 % | 98.9 % | 92.5 % |
| Effect of reinsurance | (0.3 %) | (4.2 %) | 2.0 % |
| Actual (net of reinsurance) | 93.8 % | 94.7 % | 94.5 % |

Outside of its property and casualty operations, AFG also has reinsurance recoverables totaling \$298 million, including \$247 million related to the run-off life business. These recoverables include \$210 million directly or indirectly from Hannover Life Reassurance Company of America (rated A+ by A.M. Best).

Asbestos and Environmental-related (“A&E”) Insurance Reserves Asbestos and environmental reserves of the property and casualty group consisted of the following (in millions):

December
31,
2018 2017

| | | |
|--|-------|-------|
| Asbestos | \$234 | \$238 |
| Environmental | 161 | 165 |
| A&E reserves, net of reinsurance recoverable | 395 | 403 |
| Reinsurance recoverable, net of allowance | 129 | 125 |
| Gross A&E reserves | \$524 | \$528 |

Asbestos reserves include claims asserting alleged injuries and damages from exposure to asbestos. Environmental reserves include claims relating to polluted sites.

Asbestos claims against manufacturers, distributors or installers of asbestos products were presented under the products liability section of their policies, which typically had aggregate limits that capped an insurer's liability. In recent years, a number of asbestos claims are being presented as "non-products" claims, such as those by installers of asbestos products and by property

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owners or operators who allegedly had asbestos on their property, under the premises or operations section of their policies. Unlike products exposures, these non-products exposures typically had no aggregate limits, creating potentially greater exposure for insurers. Further, in an effort to seek additional insurance coverage, some insureds with installation activities who have substantially eroded their products coverage are presenting new asbestos claims as non-products operations claims or attempting to reclassify previously settled products claims as non-products claims to restore a portion of previously exhausted products aggregate limits. AFG, along with other insurers, is and will be subject to such non-products claims. It is difficult to predict whether insureds will be successful in asserting claims under non-products coverage or whether AFG and other insurers will be successful in asserting additional defenses. Therefore, the future impact of such efforts is uncertain.

Approximately 43% of AFG's net asbestos reserves relate to policies written directly by AFG subsidiaries. Claims from these policies generally are product-oriented claims with only a limited amount of non-products exposures, and are dominated by small to mid-sized commercial entities that are mostly regional policyholders with few national target defendants. The remainder is assumed reinsurance business that includes exposures for the periods 1954 to 1983. The asbestos and environmental assumed claims are ceded by various insurance companies under reinsurance treaties. A majority of the individual assumed claims have exposures of less than \$100,000 to AFG. Asbestos losses assumed include some of the industry known manufacturers, distributors and installers. Pollution losses include industry known insured names and sites.

Establishing reserves for A&E claims relating to policies and participations in reinsurance treaties and former operations is subject to uncertainties that are significantly greater than those presented by other types of claims. For this group of claims, traditional actuarial techniques that rely on historical loss development trends cannot be used and a range of reasonably possible losses cannot be estimated. Case reserves and expense reserves are established by the claims department as specific policies are identified. In addition to the case reserves established for known claims, management establishes additional reserves for claims not yet known or reported and for possible development on known claims. These additional reserves are management's best estimate based on periodic comprehensive studies and internal reviews adjusted for payments and identifiable changes, supplemented by management's review of industry information about such claims, with due consideration to individual claim situations.

Management believes that estimating the ultimate liability for asbestos claims presents a unique and difficult challenge to the insurance industry due to, among other things, inconsistent court decisions, an increase in bankruptcy filings as a result of asbestos-related liabilities, novel theories of coverage, and judicial interpretations that often expand theories of recovery and broaden the scope of coverage. The casualty insurance industry is engaged in extensive litigation over these coverage and liability issues as the volume and severity of claims against asbestos defendants continue to increase. Environmental claims likewise present challenges in prediction, due to uncertainty regarding the interpretation of insurance policies, complexities regarding multi-party involvements at sites, evolving cleanup standards and protracted time periods required to assess the level of cleanup required at contaminated sites.

The following factors could impact AFG's reserves and payments:

There is a growing interest at the state level to attempt to legislatively address asbestos liabilities and the manner in which asbestos claims are resolved. These developments are fluid and could result in piecemeal state-by-state solutions.

The manner by which bankruptcy courts are addressing asbestos liabilities is in flux.

AFG's insureds may make claims alleging significant non-products exposures.

While management believes that AFG's reserves for A&E claims are a reasonable estimate of ultimate liability for such claims, actual results may vary materially from the amounts currently recorded due to the difficulty in predicting the number of future claims, the impact of recent bankruptcy filings, and unresolved issues such as whether coverage exists, whether policies are subject to aggregate limits on coverage, how claims are to be allocated among triggered

policies and implicated years, and whether claimants who exhibit no signs of illness will be successful in pursuing their claims. A 1% variation in loss cost trends, caused by any of the factors previously described, would change net earnings by approximately \$33 million.

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AFG tracks its A&E claims by policyholder. The following table shows, by type of claim, the number of policyholders that did not receive any payments in the calendar year separate from policyholders that did receive a payment. Policyholder counts represent policies written by AFG subsidiaries and do not include assumed reinsurance.

| | 2018 | 2017 | 2016 |
|---|------|------|------|
| Number of policyholders with no indemnity payments: | | | |
| Asbestos | 94 | 81 | 87 |
| Environmental | 112 | 101 | 107 |
| | 206 | 182 | 194 |
| Number of policyholders with indemnity payments: | | | |
| Asbestos | 49 | 74 | 66 |
| Environmental | 32 | 31 | 28 |
| | 81 | 105 | 94 |
| Total | 287 | 287 | 288 |

Amounts paid (net of reinsurance recoveries) for asbestos and environmental claims, including loss adjustment expenses, were as follows (in millions):

| | 2018 | 2017 | 2016 |
|---------------|-------|-------|-------|
| Asbestos | \$ 9 | \$ 11 | \$ 12 |
| Environmental | 17 | 12 | 14 |
| Total | \$ 26 | \$ 23 | \$ 26 |

The survival ratio is a measure often used by industry analysts to compare A&E reserves strength among companies. This ratio is typically calculated by dividing reserves for A&E exposures by the three-year average of paid losses, and therefore measures the number of years that it would take to pay off current reserves based on recent average payments. Because this ratio can be significantly impacted by a number of factors such as loss payout variability, caution should be exercised in attempting to determine reserve adequacy based simply on the survival ratio. At December 31, 2018, the property and casualty insurance segment's three-year survival ratios compare favorably with industry survival ratios derived from data published by A.M. Best (as of December 31, 2017) as detailed in the following table:

| | Property and Casualty Insurance Reserves Three-Year Survival Ratio (% Times Paid Losses) | | |
|-----------------------|---|---------------|--------------|
| | Asbestos | Environmental | Total A&E |
| AFG (12/31/2018) | 21.8 | 11.4 | 15.9 |
| Industry (12/31/2017) | 6.6 | 6.8 | 6.6 |

In addition to its ongoing internal monitoring of asbestos and environmental exposures, AFG has periodically conducted comprehensive external studies of its asbestos and environmental reserves relating to the run-off operations of its property and casualty insurance segment and exposures related to its former railroad and manufacturing operations with the aid of specialty actuarial, engineering and consulting firms and outside counsel, every two years in recent periods, with an in-depth internal review during the intervening years. AFG is currently evaluating the frequency of future external studies.

An in-depth internal review of AFG's A&E reserves was completed in the third quarter of 2018 by AFG's internal A&E claims specialists in consultation with specialty outside counsel and an outside consultant. As a result of the review, AFG's property and casualty insurance segment recorded an \$18 million pretax special charge to increase its asbestos reserves by \$6 million (net of reinsurance) and its environmental reserves by \$12 million (net of reinsurance). Over the past few years, the focus of AFG's asbestos claims litigation has shifted to smaller companies and companies with

ancillary exposures. AFG's insureds with these exposures have been the driver of the property and casualty segment's asbestos reserve increases in recent years. AFG is seeing modestly increasing estimates for indemnity and defense compared to prior studies on certain specific open claims.

The increase in property and casualty environmental reserves was primarily associated with updated estimates of site investigation and remedial costs with respect to existing sites and newly identified sites. AFG has updated its view of legal defense costs on open environmental claims as well as a number of claims and sites where the estimated investigation and remediation costs have increased. As in past years, there were no new or emerging broad industry trends that were identified in this review.

As a result of the comprehensive external study completed in the third quarter of 2017, AFG's property and casualty insurance segment recorded an \$89 million pretax special charge to increase its asbestos reserves by \$53 million (net of reinsurance) and

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its environmental reserves by \$36 million (net of reinsurance). The increase in property and casualty asbestos reserves reflects increasing life expectancies in the U.S., which have allowed more time for the impacts of asbestos exposure to emerge. AFG's comprehensive external study incorporates, among other factors, the increase in projected industry ultimate losses attributable to asbestos exposures, as well as revised estimates for future claims emergence. The increase in property and casualty environmental reserves was attributed primarily to increased legal defense costs and a number of claims and sites where the estimated investigation and remediation costs have increased.

As a result of the in-depth internal review completed in the third quarter of 2016, AFG's property and casualty insurance segment recorded a \$36 million pretax special charge to increase its asbestos reserves by \$5 million (net of reinsurance) and its environmental reserves by \$31 million (net of reinsurance). The increase in property and casualty asbestos reserves was due primarily to increased estimates for indemnity and defense costs. The increase in property and casualty environmental reserves was attributed primarily to increased defense costs and a number of claims and sites where the estimated investigation and remediation costs have increased.

Contingencies related to Subsidiaries' Former Operations The A&E studies and reviews discussed above encompassed reserves for various environmental and occupational injury and disease claims and other contingencies arising out of the railroad operations disposed of by American Premier's predecessor and certain manufacturing operations disposed of by American Premier and its subsidiaries and by Great American Financial Resources, Inc. Charges resulting from the A&E study and reviews were \$9 million in 2018, \$24 million in 2017 and \$5 million in 2016. For a discussion of the charges recorded for those operations, see "Results of Operations — Holding Company, Other and Unallocated." Liabilities for claims and contingencies arising from these former railroad and manufacturing operations totaled \$91 million at December 31, 2018. For a discussion of the uncertainties in determining the ultimate liability, see Note M — "Contingencies" to the financial statements.

Fixed-indexed Annuity Embedded Derivatives As of December 31, 2018, annuity benefits accumulated in AFG's Balance Sheet includes \$2.72 billion for the fair value of the derivatives embedded in its fixed-indexed and variable-indexed annuities. As discussed in Note F — "Derivatives" to the financial statements, AFG's fixed-indexed and variable-indexed annuities provide policyholders with a crediting rate tied, in part, to the performance of an existing stock market or other financial index. Under GAAP, this index participation is considered an embedded derivative that is required to be carried at fair value in the financial statements. AFG attempts to mitigate the risk in the index-based component of these products through the purchase and sale of call and put options on the appropriate index. AFG's strategy is designed so that the change in the fair value of the call and put options will generally offset the economic change in the liabilities from the index participation. The fair value of the embedded derivatives represents an estimate of the present value of projected policyholder benefits from the equity participation in excess of the projected minimum guaranteed contract values based on the estimated present value of certain projected future cash flows. As discussed in Note D — "Fair Value Measurements" to the financial statements, the fair value of the embedded derivatives is impacted by fluctuations in interest rates, the stock market (including the cost of options), policyholder behavior and other factors. Certain of these fluctuations, such as changes in interest rates and the performance of the stock market, are not economic in nature for the current reporting period, but rather impact the timing of reported results.

Run-off Long-term Care Insurance In December 2015, AFG completed the sale of United Teacher Associates Insurance Company and Continental General Insurance Company, the legal entities containing substantially all of its run-off long-term care insurance business, to HC2 Holdings, Inc. ("HC2") for approximately \$13 million in net proceeds. AFG may also receive up to \$13 million of additional proceeds from HC2 in the future contingent upon the release of certain statutory-basis liabilities of the legal entities sold by AFG. In connection with obtaining regulatory approval for the transaction, AFG agreed to provide up to an aggregate of \$35 million of capital support for the insurance companies, on an as-needed basis to maintain specified surplus levels, subject to immediate reimbursement by HC2 through a five-year capital maintenance agreement expiring in 2020. With the completion of this sale, AFG divested substantially all of its long-term care business (96% as measured by net statutory reserves as of

November 30, 2015) and retained only a small block of long-term care insurance (1,500 policies) with approximately \$45 million of reserves at December 31, 2018. AFG will continue to accept renewal premiums on its remaining outstanding policies, which are guaranteed renewable.

MANAGED INVESTMENT ENTITIES

Accounting standards require AFG to consolidate its investments in collateralized loan obligation (“CLO”) entities that it manages and owns an interest in (in the form of debt). See Note A — “Accounting Policies — Managed Investment Entities” and Note H — “Managed Investment Entities” to the financial statements. The effect of consolidating these entities is shown in the tables below (in millions). The “Before CLO Consolidation” columns include AFG’s investment and earnings in the CLOs on an unconsolidated basis.

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CONDENSED CONSOLIDATING BALANCE SHEET

| | Before CLO Consolidation | Managed Investment Entities | Consol. Entries | Consolidated As Reported |
|--|-----------------------------|-----------------------------------|--------------------|-----------------------------|
| December 31, 2018 | | | | |
| Assets: | | | | |
| Cash and investments | \$ 48,685 | \$ — | \$(187) (a) | \$ 48,498 |
| Assets of managed investment entities | — | 4,700 | — | 4,700 |
| Other assets | 10,259 | — | (1) (a) | 10,258 |
| Total assets | \$ 58,944 | \$ 4,700 | \$(188) | \$ 63,456 |
| Liabilities: | | | | |
| Unpaid losses and loss adjustment expenses and unearned premiums | \$ 12,336 | \$ — | \$— | \$ 12,336 |
| Annuity, life, accident and health benefits and reserves | 37,251 | — | — | 37,251 |
| Liabilities of managed investment entities | — | 4,700 | (188) (a) | 4,512 |
| Long-term debt and other liabilities | 4,385 | — | — | 4,385 |
| Total liabilities | 53,972 | 4,700 | (188) | 58,484 |
| Redeemable noncontrolling interests | — | — | — | — |
| Shareholders' equity: | | | | |
| Common Stock and Capital surplus | 1,334 | — | — | 1,334 |
| Retained earnings | 3,588 | — | — | 3,588 |
| Accumulated other comprehensive income, net of tax | 48 | — | — | 48 |
| Total shareholders' equity | 4,970 | — | — | 4,970 |
| Noncontrolling interests | 2 | — | — | 2 |
| Total equity | 4,972 | — | — | 4,972 |
| Total liabilities and equity | \$ 58,944 | \$ 4,700 | \$(188) | \$ 63,456 |
| December 31, 2017 | | | | |
| Assets: | | | | |
| Cash and investments | \$ 46,262 | \$ — | \$(214) (a) | \$ 46,048 |
| Assets of managed investment entities | — | 4,902 | — | 4,902 |
| Other assets | 9,709 | — | (1) (a) | 9,708 |
| Total assets | \$ 55,971 | \$ 4,902 | \$(215) | \$ 60,658 |
| Liabilities: | | | | |
| Unpaid losses and loss adjustment expenses and unearned premiums | \$ 12,088 | \$ — | \$— | \$ 12,088 |
| Annuity, life, accident and health benefits and reserves | 33,974 | — | — | 33,974 |
| Liabilities of managed investment entities | — | 4,902 | (215) (a) | 4,687 |
| Long-term debt and other liabilities | 4,575 | — | — | 4,575 |
| Total liabilities | 50,637 | 4,902 | (215) | 55,324 |
| Redeemable noncontrolling interests | 3 | — | — | 3 |
| Shareholders' equity: | | | | |
| Common Stock and Capital surplus | 1,269 | — | — | 1,269 |
| Retained earnings | 3,248 | — | — | 3,248 |

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| | | | | |
|--|-----------|----------|----------|-----------|
| Accumulated other comprehensive income, net of tax | 813 | — | — | 813 |
| Total shareholders' equity | 5,330 | — | — | 5,330 |
| Noncontrolling interests | 1 | — | — | 1 |
| Total equity | 5,331 | — | — | 5,331 |
| Total liabilities and equity | \$ 55,971 | \$ 4,902 | \$(215) | \$ 60,658 |

(a) Elimination of the fair value of AFG's investment in CLOs and related accrued interest.

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CONDENSED CONSOLIDATING STATEMENT OF EARNINGS

| | Before CLO Consolidation (a) | Managed Investment Entities | Consol. Entries | Consolidated As Reported |
|--|---------------------------------|-----------------------------------|--------------------|-----------------------------|
| Three months ended December 31, 2018 | | | | |
| Revenues: | | | | |
| Insurance net earned premiums | \$ 1,276 | \$ — | \$ — | \$ 1,276 |
| Net investment income | 538 | — | 4 (b) | 542 |
| Realized losses on securities | (238) |) — | — | (238) |
| Income of managed investment entities: | | | | |
| Investment income | — | 68 | — | 68 |
| Gain (loss) on change in fair value of assets/liabilities | — | (1) | (10) (b) | (11) |
| Other income | 57 | — | (4) (c) | 53 |
| Total revenues | 1,633 | 67 | (10) | 1,690 |
| Costs and Expenses: | | | | |
| Insurance benefits and expenses | 1,575 | — | — | 1,575 |
| Expenses of managed investment entities | — | 67 | (10) (b)(c) | 57 |
| Interest charges on borrowed money and other expenses | 97 | — | — | 97 |
| Total costs and expenses | 1,672 | 67 | (10) | 1,729 |
| Earnings (loss) before income taxes | (39) |) — | — | (39) |
| Provision (credit) for income taxes | (4) |) — | — | (4) |
| Net earnings (loss), including noncontrolling interests | (35) |) — | — | (35) |
| Less: Net earnings (losses) attributable to noncontrolling interests | (6) |) — | — | (6) |
| Net earnings (loss) attributable to shareholders | \$ (29) |) \$ — | \$ — | \$ (29) |
| Three months ended December 31, 2017 | | | | |
| Revenues: | | | | |
| Insurance net earned premiums | \$ 1,230 | \$ — | \$ — | \$ 1,230 |
| Net investment income | 472 | — | (7) (b) | 465 |
| Realized gains on securities | 6 | — | — | 6 |
| Income of managed investment entities: | | | | |
| Investment income | — | 55 | — | 55 |
| Gain on change in fair value of assets/liabilities | — | — | — (b) | — |
| Other income | 56 | — | (4) (c) | 52 |
| Total revenues | 1,764 | 55 | (11) | 1,808 |
| Costs and Expenses: | | | | |
| Insurance benefits and expenses | 1,340 | — | — | 1,340 |
| Expenses of managed investment entities | — | 54 | (10) (b)(c) | 44 |
| Interest charges on borrowed money and other expenses | 157 | — | — | 157 |
| Total costs and expenses | 1,497 | 54 | (10) | 1,541 |
| Earnings before income taxes | 267 | 1 | (1) | 267 |
| Provision (credit) for income taxes | 101 | — | — | 101 |
| Net earnings, including noncontrolling interests | 166 | 1 | (1) | 166 |
| Less: Net earnings attributable to noncontrolling interests | — | — | — | — |
| Net earnings attributable to shareholders | \$ 166 | \$ 1 | \$ (1) | \$ 166 |

(a)

Includes a loss of \$4 million in the fourth quarter of 2018 and income of \$7 million in the fourth quarter of 2017 representing the change in fair value of AFG's CLO investments plus \$4 million in both the fourth quarter of 2018 and 2017 in CLO management fees earned.

- (b) Elimination of the change in fair value of AFG's investments in the CLOs, including \$6 million in both the fourth quarter of 2018 and 2017 in distributions recorded as interest expense by the CLOs.
- (c) Elimination of management fees earned by AFG.

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CONDENSED CONSOLIDATING STATEMENT OF EARNINGS - CONTINUED

| | Before CLO Consolidation (a) | Managed Investment Entities | Consol. Entries | Consolidated As Reported |
|--|---------------------------------|-----------------------------------|--------------------|-----------------------------|
| Year ended December 31, 2018 | | | | |
| Revenues: | | | | |
| Insurance net earned premiums | \$ 4,889 | \$ — | \$ — | \$ 4,889 |
| Net investment income | 2,101 | — | (7) (b) | 2,094 |
| Realized losses on securities | (266) | — | — | (266) |
| Income (loss) of managed investment entities: | | | | |
| Investment income | — | 255 | — | 255 |
| Gain (loss) on change in fair value of assets/liabilities | — | (7) | (14) (b) | (21) |
| Other income | 215 | — | (16) (c) | 199 |
| Total revenues | 6,939 | 248 | (37) | 7,150 |
| Costs and Expenses: | | | | |
| Insurance benefits and expenses | 5,885 | — | — | 5,885 |
| Expenses of managed investment entities | — | 248 | (37) (b)(c) | 211 |
| Interest charges on borrowed money and other expenses | 415 | — | — | 415 |
| Total costs and expenses | 6,300 | 248 | (37) | 6,511 |
| Earnings before income taxes | 639 | — | — | 639 |
| Provision for income taxes | 122 | — | — | 122 |
| Net earnings, including noncontrolling interests | 517 | — | — | 517 |
| Less: Net earnings (losses) attributable to noncontrolling interests | (13) | — | — | (13) |
| Net earnings attributable to shareholders | \$ 530 | \$ — | \$ — | \$ 530 |
| Year ended December 31, 2017 | | | | |
| Revenues: | | | | |
| Insurance net earned premiums | \$ 4,601 | \$ — | \$ — | \$ 4,601 |
| Net investment income | 1,854 | — | (23) (b) | 1,831 |
| Realized gains on securities | 5 | — | — | 5 |
| Income of managed investment entities: | | | | |
| Investment income | — | 210 | — | 210 |
| Gain on change in fair value of assets/liabilities | — | 22 | (10) (b) | 12 |
| Other income | 224 | — | (18) (c) | 206 |
| Total revenues | 6,684 | 232 | (51) | 6,865 |
| Costs and Expenses: | | | | |
| Insurance benefits and expenses | 5,453 | — | — | 5,453 |
| Expenses of managed investment entities | — | 231 | (50) (b)(c) | 181 |
| Interest charges on borrowed money and other expenses | 507 | — | — | 507 |
| Total costs and expenses | 5,960 | 231 | (50) | 6,141 |
| Earnings before income taxes | 724 | 1 | (1) | 724 |
| Provision for income taxes | 247 | — | — | 247 |
| Net earnings, including noncontrolling interests | 477 | 1 | (1) | 477 |
| Less: Net earnings attributable to noncontrolling interests | 2 | — | — | 2 |
| Net earnings attributable to shareholders | \$ 475 | \$ 1 | \$ (1) | \$ 475 |

(a)

Includes income of \$7 million and \$23 million in 2018 and 2017, respectively, representing the change in fair value of AFG's CLO investments plus \$16 million and \$18 million in 2018 and 2017, respectively, in CLO management fees earned.

- (b) Elimination of the change in fair value of AFG's investments in the CLOs, including \$21 million and \$32 million in 2018 and 2017, respectively, in distributions recorded as interest expense by the CLOs.
- (c) Elimination of management fees earned by AFG.

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CONDENSED CONSOLIDATING STATEMENT OF EARNINGS - CONTINUED

| | Before CLO Consolidation (a) | Managed Investment Entities | Consol. Entries | Consolidated As Reported |
|---|---------------------------------|-----------------------------------|--------------------|-----------------------------|
| Year ended December 31, 2016 | | | | |
| Revenues: | | | | |
| Insurance net earned premiums | \$ 4,352 | \$ — | \$ — | \$ 4,352 |
| Net investment income | 1,733 | — | (37) (b) | 1,696 |
| Realized gains on: | | | | |
| Securities | 19 | — | — | 19 |
| Subsidiaries | 2 | — | — | 2 |
| Income of managed investment entities: | | | | |
| Investment income | — | 190 | — | 190 |
| Gain on change in fair value of assets/liabilities | — | 8 | 7 (b) | 15 |
| Other income | 241 | — | (17) (c) | 224 |
| Total revenues | 6,347 | 198 | (47) | 6,498 |
| Costs and Expenses: | | | | |
| Insurance benefits and expenses | 5,130 | — | — | 5,130 |
| Expenses of managed investment entities | — | 197 | (46) (b)(c) | 151 |
| Interest charges on borrowed money and other expenses | 430 | — | — | 430 |
| Total costs and expenses | 5,560 | 197 | (46) | 5,711 |
| Earnings before income taxes | 787 | 1 | (1) | 787 |
| Provision for income taxes | 119 | — | — | 119 |
| Net earnings, including noncontrolling interests | 668 | 1 | (1) | 668 |
| Less: Net earnings attributable to noncontrolling interests | 19 | — | — | 19 |
| Net earnings attributable to shareholders | \$ 649 | \$ 1 | \$ (1) | \$ 649 |

(a) Includes income of \$37 million representing the change in fair value of AFG's CLO investments plus \$17 million in CLO management fees earned.

(b) Elimination of the change in fair value of AFG's investments in the CLOs, including \$29 million in distributions recorded as interest expense by the CLOs.

(c) Elimination of management fees earned by AFG.

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RESULTS OF OPERATIONS

General AFG's net earnings attributable to shareholders, determined in accordance with GAAP, include certain items that may not be indicative of its ongoing core operations. For example, core net operating earnings excludes realized gains (losses) on securities because such gains and losses are influenced significantly by financial markets, interest rates and the timing of sales. Similarly, significant gains and losses from the sale of real estate are excluded from core earnings as they are influenced by the timing of sales and realized gains (losses) and significant tax benefits (charges) related to subsidiaries are excluded because such gains and losses are largely the result of the changing business strategy and market opportunities. In addition, special charges related to coverage that AFG no longer writes, such as the Neon exited lines and for asbestos and environmental exposures are excluded from core earnings. The following table (in millions, except per share amounts) identifies non-core items and reconciles net earnings attributable to shareholders to core net operating earnings, a non-GAAP financial measure. AFG believes core net operating earnings is a useful tool for investors and analysts in analyzing ongoing operating trends and for management to evaluate financial performance against historical results because it believes this provides a more comparable measure of its continuing business.

| | Three months ended December 31, | | Year ended December 31, | | |
|--|------------------------------------|--------|----------------------------|--------|--------|
| | 2018 | 2017 | 2018 | 2017 | 2016 |
| Components of net earnings (loss) attributable to shareholders: | | | | | |
| Core operating earnings before income taxes | \$ 199 | \$ 283 | \$ 932 | \$ 865 | \$ 840 |
| Pretax non-core items: | | | | | |
| Realized gains (losses) on securities | (238) | 6 | (266) | 5 | 19 |
| Realized gain on long-term care business | — | — | — | — | 2 |
| Gain on sale of apartment property | — | — | — | — | 32 |
| Special A&E charges | — | — | (27) | (113) | (41) |
| Neon exited lines charge | — | 18 | — | 18 | (65) |
| Loss on retirement of debt | — | (40) | — | (51) | — |
| Earnings (loss) before income taxes | (39) | 267 | 639 | 724 | 787 |
| Provision (credit) for income taxes: | | | | | |
| Core operating earnings | 46 | 86 | 184 | 275 | 290 |
| Non-core items: | | | | | |
| Realized gains (losses) on securities | (50) | 2 | (56) | 2 | 7 |
| Tax benefit related to Neon restructuring | — | (56) | — | (56) | (111) |
| Tax expense related to change in U.S. corporate tax rate | — | 83 | — | 83 | — |
| Tax benefit related to National Interstate merger | — | — | — | — | (66) |
| Other | — | (14) | (6) | (57) | (1) |
| Total provision (credit) for income taxes | (4) | 101 | 122 | 247 | 119 |
| Net earnings (loss), including noncontrolling interests | (35) | 166 | 517 | 477 | 668 |
| Less net earnings (losses) attributable to noncontrolling interests: | | | | | |
| Core operating earnings | (6) | — | (13) | 2 | 16 |
| Non-core items | — | — | — | — | 3 |
| Total net earnings (losses) attributable to noncontrolling interests | (6) | — | (13) | 2 | 19 |
| Net earnings (loss) attributable to shareholders | \$(29) | \$ 166 | \$ 530 | \$ 475 | \$ 649 |
| Net earnings (loss): | | | | | |
| Core net operating earnings | \$ 159 | \$ 197 | \$ 761 | \$ 588 | \$ 534 |
| Non-core items | (188) | (31) | (231) | (113) | 115 |
| Net earnings (loss) attributable to shareholders | \$(29) | \$ 166 | \$ 530 | \$ 475 | \$ 649 |

| | | | | | |
|--|----------|---------|---------|---------|---------|
| Diluted per share amounts: | | | | | |
| Core net operating earnings | \$1.75 | \$2.20 | \$8.40 | \$6.55 | \$6.03 |
| Realized gains (losses) on securities | (2.08) | 0.04 | (2.31) | 0.03 | 0.16 |
| Realized gain on long-term care business | — | — | — | — | 0.01 |
| Gain on sale of apartment property | — | — | — | — | 0.17 |
| Special A&E charges | — | — | (0.24) | (0.82) | (0.30) |
| Neon exited lines charge | — | 0.19 | — | 0.19 | (0.73) |
| Loss on retirement of debt | — | (0.29) | — | (0.37) | — |
| Tax benefit related to Neon restructuring | — | 0.62 | — | 0.62 | 1.25 |
| Tax expense related to change in U.S. corporate tax rate | — | (0.92) | — | (0.92) | — |
| Tax benefit related to National Interstate merger | — | — | — | — | 0.74 |
| Net earnings (loss) attributable to shareholders | \$(0.33) | \$1.84 | \$5.85 | \$5.28 | \$7.33 |

AFG reported a net loss attributable to shareholders of \$29 million in the fourth quarter of 2018 compared to net earnings attributable to shareholders of \$166 million in the fourth quarter of 2017. Results for the fourth quarter of 2018 include \$188 million in non-core net realized losses on securities. Comparatively, net earnings in the 2017 fourth quarter were

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adversely impacted by \$31 million in net non-core items. The change in the U.S. corporate tax rate from 35% to 21%, effective January 1, 2018, contributed to a lower effective tax rate in 2018 as compared to 2017. Core net operating earnings decreased \$38 million in the fourth quarter of 2018 compared to the same period in 2017 reflecting lower earnings in the annuity segment and lower underwriting profit in the property and casualty insurance segment, partially offset by higher net investment income in the property and casualty insurance segment, lower holding company expenses and the lower corporate income tax rate. Realized losses on securities in the fourth quarter of 2018 includes the decline in fair value of equity securities that are required to be carried at fair value through net earnings under new accounting guidance adopted on January 1, 2018. Included in the \$188 million of non-core net realized losses on securities in the fourth quarter of 2018 were \$179 million in net losses on equity securities that AFG continued to own at December 31, 2018.

Net earnings attributable to shareholders increased \$55 million for the full-year of 2018 compared to the same period in 2017 due primarily to higher core net operating earnings, lower special A&E charges recorded in 2018 compared to 2017, losses on the retirement of debt in 2017 and the 2017 tax expense related to the change in the U.S. corporate tax rate, partially offset by net realized losses on securities in 2018 compared to net realized gains on securities in 2017, the 2017 favorable development in the Neon exited lines in connection with a reinsurance to close transaction and the 2017 tax benefit from restructuring at Neon. Core net operating earnings increased \$173 million in 2018 compared to 2017 reflecting higher net investment income in the property and casualty insurance segment, lower interest charges on borrowed money, lower holding company expenses and a lower corporate income tax rate, partially offset by lower earnings in the annuity segment and income from the sale of real estate in 2017. Realized losses on securities in 2018 includes the decline in fair value of equity securities that are required to be carried at fair value through net earnings under new accounting guidance adopted on January 1, 2018. Included in the \$210 million of non-core net realized losses on securities in 2018 were \$214 million in net losses on equity securities that AFG continued to own at December 31, 2018.

Net earnings attributable to shareholders decreased \$174 million for the full-year of 2017 compared to the same period in 2016 due primarily to the 2017 tax expense related to the change in the U.S. corporate tax rate, the 2016 tax benefits related to the National Interstate merger and Neon restructuring, higher special A&E charges recorded in 2017 compared to 2016, lower net realized gains on securities in 2017 compared to 2016, a gain on the sale of an apartment property in 2016 and losses on the retirement of debt in 2017, partially offset by a 2016 charge related to the exit of certain lines of business within Neon and favorable development in 2017 on the Neon exited lines in connection with a reinsurance to close transaction, the 2017 tax benefit from restructuring at Neon and higher core net operating earnings. Core net operating earnings increased \$54 million in 2017 compared to 2016 reflecting higher earnings in the property and casualty insurance and annuity segments.

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RESULTS OF OPERATIONS — QUARTERS ENDED DECEMBER 31, 2018 AND 2017

Segmented Statement of Earnings AFG reports its business as three segments: (i) Property and casualty insurance (“P&C”), (ii) Annuity and (iii) Other, which includes run-off long-term care and life, holding company costs and income and expenses related to the managed investment entities (“MIEs”).

Effective January 1, 2018, the results of AFG’s run-off long-term care and life businesses are included in the “Other” segment instead of as a separate reportable segment based on the immaterial size of the remaining operations. Prior periods amounts were reclassified for consistent presentation.

AFG’s net earnings attributable to shareholders, determined in accordance with GAAP, include certain items that may not be indicative of its ongoing core operations. The following tables for the three months ended December 31, 2018 and 2017 identify such items by segment and reconcile net earnings attributable to shareholders to core net operating earnings, a non-GAAP financial measure that AFG believes is a useful tool for investors and analysts in analyzing ongoing operating trends (in millions):

| | P&C | Annuity | Other MIEs | Holding Company, other and unallocated | Total | Non-core reclass | GAAP Total |
|--|---------|---------|---------------|--|---------|---------------------|---------------|
| Three months ended December 31, 2018 | | | | | | | |
| Revenues: | | | | | | | |
| Property and casualty insurance net earned premiums | \$1,270 | \$ — | \$ — | \$ — | \$1,270 | \$ — | \$1,270 |
| Life, accident and health net earned premiums | — | — | — | 6 | 6 | — | 6 |
| Net investment income | 115 | 419 | 4 | 4 | 542 | — | 542 |
| Realized losses on securities | — | — | — | — | — | (238) | (238) |
| Income (loss) of MIEs: | | | | | | | |
| Investment income | — | — | 68 | — | 68 | — | 68 |
| Gain (loss) on change in fair value of assets/liabilities | — | — | (1) | — | (11) | — | (11) |
| Other income | 2 | 27 | (4) | 28 | 53 | — | 53 |
| Total revenues | 1,387 | 446 | 57 | 38 | 1,928 | (238) | 1,690 |
| Costs and Expenses: | | | | | | | |
| Property and casualty insurance: | | | | | | | |
| Losses and loss adjustment expenses | 797 | — | — | — | 797 | — | 797 |
| Commissions and other underwriting expenses | 372 | — | — | 6 | 378 | — | 378 |
| Annuity benefits | — | 334 | — | — | 334 | — | 334 |
| Life, accident and health benefits | — | — | — | 8 | 8 | — | 8 |
| Annuity and supplemental insurance acquisition expenses | — | 56 | — | 2 | 58 | — | 58 |
| Interest charges on borrowed money | — | — | — | 16 | 16 | — | 16 |
| Expenses of MIEs | — | — | 57 | — | 57 | — | 57 |
| Other expenses | 10 | 36 | — | 35 | 81 | — | 81 |
| Total costs and expenses | 1,179 | 426 | 57 | 67 | 1,729 | — | 1,729 |
| Earnings (loss) before income taxes | 208 | 20 | — | (29) | 199 | (238) | (39) |
| Provision (credit) for income taxes | 49 | 5 | — | (8) | 46 | (50) | (4) |
| Net earnings (loss), including noncontrolling interests | 159 | 15 | — | (21) | 153 | (188) | (35) |
| Less: Net earnings (losses) attributable to noncontrolling interests | (6) | — | — | — | (6) | — | (6) |
| Core Net Operating Earnings | 165 | 15 | — | (21) | 159 | — | 159 |

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Non-core earnings attributable to shareholders (a):

| | | | | | | | |
|--|-------|-------|-----|----------|---------|------|---------|
| Realized losses on securities, net of tax | — | — | — | (188) | (188) | 188 | — |
| Net Earnings (Loss) Attributable to Shareholders | \$165 | \$ 15 | \$— | \$(209) | \$(29) | \$ — | \$(29) |

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| | P&C | Annuity | Other Holding Company MIEs and unallocated | Total | Non-core reclass | GAAP Total |
|---|----------|---------|---|----------|---------------------|---------------|
| Three months ended December 31, 2017 | | | | | | |
| Revenues: | | | | | | |
| Property and casualty insurance net earned premiums | \$ 1,225 | \$ — | \$ — | \$ 1,225 | \$ — | \$ 1,225 |
| Life, accident and health net earned premiums | — | — | 5 | 5 | — | 5 |
| Net investment income | 86 | 376 | (7) 10 | 465 | — | 465 |
| Realized gains on securities | — | — | — | — | 6 | 6 |
| Income of MIEs: | | | | | | |
| Investment income | — | — | 55 | 55 | — | 55 |
| Gain on change in fair value of assets/liabilities | — | — | — | — | — | — |
| Other income | 7 | 24 | (4) 25 | 52 | — | 52 |
| Total revenues | 1,318 | 400 | 44 40 | 1,802 | 6 | 1,808 |
| Costs and Expenses: | | | | | | |
| Property and casualty insurance: | | | | | | |
| Losses and loss adjustment expenses | 734 | — | — | 734 | (18) | 716 |
| Commissions and other underwriting expenses | 336 | — | 9 | 345 | — | 345 |
| Annuity benefits | — | 257 | — | 257 | — | 257 |
| Life, accident and health benefits | — | — | 5 | 5 | — | 5 |
| Annuity and supplemental insurance acquisition expenses | — | 15 | 2 | 17 | — | 17 |
| Interest charges on borrowed money | — | — | 20 | 20 | — | 20 |
| Expenses of MIEs | — | — | 44 | 44 | — | 44 |
| Other expenses | 15 | 31 | 51 | 97 | 40 | 137 |
| Total costs and expenses | 1,085 | 303 | 44 87 | 1,519 | 22 | 1,541 |
| Earnings before income taxes | 233 | 97 | (47) | 283 | (16) | 267 |
| Provision for income taxes | 69 | 32 | (15) | 86 | 15 | 101 |
| Net earnings, including noncontrolling interests | 164 | 65 | (32) | 197 | (31) | 166 |
| Less: Net earnings attributable to noncontrolling interests | — | — | — | — | — | — |
| Core Net Operating Earnings | 164 | 65 | (32) | 197 | | |
| Non-core earnings attributable to shareholders (a): | | | | | | |
| Realized gains on securities, net of tax | — | — | 4 | 4 | (4) | — |
| Neon exited lines charge | 18 | — | — | 18 | (18) | — |
| Loss on retirement of debt, net of tax | — | — | (26) | (26) | 26 | — |
| Tax benefit related to Neon restructuring | 56 | — | — | 56 | (56) | — |
| Tax expense related to change in U.S. corporate tax rate | (88) | 25 | (20) | (83) | 83 | — |
| Net Earnings Attributable to Shareholders | \$ 150 | \$ 90 | \$ — (74) | \$ 166 | \$ — | \$ 166 |

(a) See the reconciliation of core earnings to GAAP net earnings under “Results of Operations — General” for details on the tax and noncontrolling interest impacts of these reconciling items.

Property and Casualty Insurance Segment — Results of Operations Performance measures such as underwriting profit or loss and related combined ratios are often used by property and casualty insurers to help users of their financial statements better understand the company’s performance. Underwriting profitability is measured by the combined ratio, which is a sum of the ratios of losses and loss adjustment expenses, and commissions and other underwriting expenses to premiums. A combined ratio under 100% indicates an underwriting profit. The combined ratio does not

reflect net investment income, other income, other expenses or federal income taxes.

AFG's property and casualty insurance operations contributed \$208 million in GAAP pretax earnings in the fourth quarter of 2018 compared to \$251 million in the fourth quarter of 2017, a decrease of \$43 million (17%). Property and casualty core pretax earnings were \$208 million in the fourth quarter of 2018 compared to \$233 million in the fourth quarter of 2017, a decrease of \$25 million (11%). The decrease in GAAP and core pretax earnings reflects lower underwriting profits in the Property and transportation and Specialty casualty sub-segments, partially offset by higher net investment income due to higher

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earnings from limited partnerships and similar investments. The high returns from limited partnerships and similar investments should not be expected to repeat in future periods. The decrease in GAAP pretax earnings also reflects the impact of favorable development in the fourth quarter of 2017 in the Neon exited lines in connection with a reinsurance to close transaction.

The following table details AFG's earnings before income taxes from its property and casualty insurance operations for the three months ended December 31, 2018 and 2017 (dollars in millions):

| | Three months ended December 31, | | | |
|---|---------------------------------------|---------|----------|----|
| | 2018 | 2017 | % Change | |
| Gross written premiums | \$1,613 | \$1,571 | 3 | % |
| Reinsurance premiums ceded | (405) | (410) | (1 | %) |
| Net written premiums | 1,208 | 1,161 | 4 | % |
| Change in unearned premiums | 62 | 64 | (3 | %) |
| Net earned premiums | 1,270 | 1,225 | 4 | % |
| Loss and loss adjustment expenses (*) | 797 | 734 | 9 | % |
| Commissions and other underwriting expenses | 372 | 336 | 11 | % |
| Core underwriting gain | 101 | 155 | (35 | %) |
| Net investment income | 115 | 86 | 34 | % |
| Other income and expenses, net | (8) | (8) | — | % |
| Core earnings before income taxes | 208 | 233 | (11 | %) |
| Pretax non-core Neon exited lines charge | — | 18 | (100 | %) |
| GAAP earnings before income taxes | \$208 | \$251 | (17 | %) |

(*) Excludes pretax non-core income of \$18 million in the fourth quarter of 2017 representing favorable development related to the Neon exited lines in connection with a reinsurance to close transaction.

Combined Ratios:

| Specialty lines | Change | | | |
|------------------------------------|--------|--------|-------|---|
| Loss and LAE ratio | 62.7 | % 59.8 | % 2.9 | % |
| Underwriting expense ratio | 29.3 | % 27.5 | % 1.8 | % |
| Combined ratio | 92.0 | % 87.3 | % 4.7 | % |
| Aggregate — including exited lines | | | | |
| Loss and LAE ratio | 62.7 | % 58.5 | % 4.2 | % |
| Underwriting expense ratio | 29.3 | % 27.5 | % 1.8 | % |
| Combined ratio | 92.0 | % 86.0 | % 6.0 | % |

AFG's statutory combined ratio has been better than the U.S. industry average for 31 of the last 33 years. Management believes that AFG's insurance operations have performed better than the industry as a result of its specialty niche focus, product line diversification, stringent underwriting discipline and alignment of compensation incentives.

AFG reports the underwriting performance of its Specialty property and casualty insurance business in the following sub-segments: (i) Property and transportation, (ii) Specialty casualty and (iii) Specialty financial.

To understand the overall profitability of particular lines, the timing of claims payments and the related impact of investment income must be considered. Certain “short-tail” lines of business (primarily property coverages) generally have quick loss payouts, which reduce the time funds are held, thereby limiting investment income earned thereon. In contrast, “long-tail” lines of business (primarily liability coverages and workers’ compensation) generally have payouts that are either structured over many years or take many years to settle, thereby significantly increasing investment income earned on related premiums received.

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Gross Written Premiums

Gross written premiums (“GWP”) for AFG’s property and casualty insurance segment were \$1.61 billion for the fourth quarter of 2018 compared to \$1.57 billion for the fourth quarter of 2017, an increase of \$42 million (3%). Detail of AFG’s property and casualty gross written premiums is shown below (dollars in millions):

| | Three months ended December 31, | | | | | |
|-----------------------------|------------------------------------|------|---------|------|----------|--|
| | 2018 | | 2017 | | % Change | |
| | GWP | % | GWP | % | | |
| Property and transportation | \$651 | 40 % | \$626 | 40 % | 4 % | |
| Specialty casualty | 778 | 48 % | 737 | 47 % | 6 % | |
| Specialty financial | 184 | 12 % | 208 | 13 % | (12 %) | |
| | \$1,613 | 100% | \$1,571 | 100% | 3 % | |

Reinsurance Premiums Ceded

Reinsurance premiums ceded (“Ceded”) for AFG’s property and casualty insurance segment were 25% of gross written premiums for the fourth quarter of 2018 compared to 26% for the fourth quarter of 2017, a decrease of 1 percentage point. Detail of AFG’s property and casualty reinsurance premiums ceded is shown below (dollars in millions):

| | Three months ended December 31, | | | | |
|-----------------------------|------------------------------------|-------------|---------|-------------|-------------------|
| | 2018 | | 2017 | | Change in % |
| | Ceded | % of GWP | Ceded | % of GWP | % of GWP |
| Property and transportation | \$(203) | 31 % | \$(202) | 32 % | (1 %) |
| Specialty casualty | (197) | 25 % | (182) | 25 % | — % |
| Specialty financial | (42) | 23 % | (52) | 25 % | (2 %) |
| Other specialty | 37 | | 26 | | |
| | \$(405) | 25 % | \$(410) | 26 % | (1 %) |

Net Written Premiums

Net written premiums (“NWP”) for AFG’s property and casualty insurance segment were \$1.21 billion for the fourth quarter of 2018 compared to \$1.16 billion for the fourth quarter of 2017, an increase of \$47 million (4%). Detail of AFG’s property and casualty net written premiums is shown below (dollars in millions):

| | Three months ended December 31, | | | | | |
|-----------------------------|------------------------------------|------|---------|------|----------|--|
| | 2018 | | 2017 | | % Change | |
| | NWP | % | NWP | % | | |
| Property and transportation | \$448 | 37 % | \$424 | 37 % | 6 % | |
| Specialty casualty | 581 | 48 % | 555 | 48 % | 5 % | |
| Specialty financial | 142 | 12 % | 156 | 13 % | (9 %) | |
| Other specialty | 37 | 3 % | 26 | 2 % | 42 % | |
| | \$1,208 | 100% | \$1,161 | 100% | 4 % | |

Net Earned Premiums

Net earned premiums (“NEP”) for AFG’s property and casualty insurance segment were \$1.27 billion for the fourth quarter of 2018 compared to \$1.23 billion for the fourth quarter of 2017, an increase of \$45 million (4%). Detail of AFG’s property and casualty net earned premiums is shown below (dollars in millions):

| | Three months ended | | | | | |
|-----------------------------|--------------------|------|---------|------|----------|----|
| | December 31, | | | | | |
| | 2018 | | 2017 | | | |
| | NEP | % | NEP | % | % Change | |
| Property and transportation | \$479 | 38 % | \$485 | 40 % | (1 | %) |
| Specialty casualty | 613 | 48 % | 573 | 47 % | 7 | % |
| Specialty financial | 141 | 11 % | 141 | 11 % | — | % |
| Other specialty | 37 | 3 % | 26 | 2 % | 42 | % |
| | \$1,270 | 100% | \$1,225 | 100% | 4 | % |

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The \$42 million (3%) increase in gross written premiums in the fourth quarter of 2018 compared to the fourth quarter of 2017 reflects growth in the Property and transportation and Specialty casualty sub-segments, partially offset by lower gross written premiums in the Specialty financial sub-segment. Excluding the impact of the timing of renewal of two large accounts in the Property and transportation sub-segment, gross written premiums increased approximately 1% in the fourth quarter of 2018 compared to the prior year period. Overall average renewal rates increased approximately 2% in the fourth quarter of 2018. Excluding the workers' compensation business, renewal pricing increased approximately 4%.

Property and transportation Gross written premiums increased \$25 million (4%) in the fourth quarter of 2018 compared to the fourth quarter of 2017. This increase was largely the result of a change in the timing of two large policy renewals in one of the transportation businesses from the third quarter to the fourth quarter of 2018. Excluding the impact of the timing of these policy renewals, gross written premiums increased 1% in the fourth quarter of 2018 compared to the fourth quarter of 2017. Lower year-over-year premiums in the crop insurance business and underwriting actions on under-performing accounts in the Singapore branch also impacted fourth quarter premiums. Average renewal rates increased approximately 3% for this group in the fourth quarter of 2018. Reinsurance premiums ceded as a percentage of gross written premiums decreased 1 percentage point for the fourth quarter of 2018 compared to the fourth quarter of 2017. Lower cessions in the crop insurance business were partially offset by reinstatement premiums in the aviation business.

Specialty casualty Gross written premiums increased \$41 million (6%) in the fourth quarter of 2018 compared to the fourth quarter of 2017. Higher premiums within Neon, resulting from the growth of its portfolio in targeted classes of business, along with growth in several other businesses and the addition of ABA Insurance Services, were partially offset by lower premiums in the workers' compensation businesses. Average renewal rates for this group were flat in the fourth quarter of 2018. Excluding the workers' compensation businesses, renewal rates for this group increased approximately 4%. Reinsurance premiums ceded as a percentage of gross written premiums were comparable between periods. Higher cessions to AFG's internal reinsurance program, which is included in Other specialty and higher cessions in the workers' compensation businesses were offset by lower reinstatement premiums resulting from reinsured hurricane losses in the 2018 period compared to the 2017 period.

Specialty financial Gross written premiums decreased \$24 million (12%) in the fourth quarter of 2018 compared to the fourth quarter of 2017, due primarily to the timing of several new accounts in the lending and leasing businesses in 2017. Average renewal rates for this group increased approximately 5% in the fourth quarter of 2018. Reinsurance premiums ceded as a percentage of gross written premiums decreased 2 percentage points for the fourth quarter of 2018 compared to the fourth quarter of 2017 reflecting lower cessions in the equipment leasing business.

Other specialty The amounts shown as reinsurance premiums ceded represent business assumed by AFG's internal reinsurance program from the operations that make up AFG's other Specialty property and casualty insurance sub-segments. Reinsurance premiums assumed increased \$11 million (42%) in the fourth quarter of 2018 compared to the fourth quarter of 2017, reflecting an increase in premiums retained, primarily from businesses in the Specialty casualty sub-segment.

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Combined Ratio

Performance measures such as the combined ratio are often used by property and casualty insurers to help users of their financial statements better understand the company's performance. The combined ratio is the sum of the loss and loss adjustment expenses ("LAE") and underwriting expense ratios. These ratios are calculated by dividing each of the respective expenses by net earned premiums. The table below (dollars in millions) details the components of the combined ratio for AFG's property and casualty insurance segment:

| | Three months ended December 31, | | | Three months ended December 31, | |
|---|---------------------------------|-------|---------|---------------------------------|-------|
| | 2018 | 2017 | Change | 2018 | 2017 |
| Property and transportation | | | | | |
| Loss and LAE ratio | 68.2% | 67.1% | 1.1 % | | |
| Underwriting expense ratio | 18.3% | 15.5% | 2.8 % | | |
| Combined ratio | 86.5% | 82.6% | 3.9 % | | |
| Underwriting profit | | | | \$64 | \$84 |
| Specialty casualty | | | | | |
| Loss and LAE ratio | 63.5% | 59.1% | 4.4 % | | |
| Underwriting expense ratio | 33.0% | 30.9% | 2.1 % | | |
| Combined ratio | 96.5% | 90.0% | 6.5 % | | |
| Underwriting profit | | | | \$22 | \$58 |
| Specialty financial | | | | | |
| Loss and LAE ratio | 36.4% | 33.1% | 3.3 % | | |
| Underwriting expense ratio | 49.1% | 53.1% | (4.0 %) | | |
| Combined ratio | 85.5% | 86.2% | (0.7 %) | | |
| Underwriting profit | | | | \$20 | \$19 |
| Total Specialty | | | | | |
| Loss and LAE ratio | 62.7% | 59.8% | 2.9 % | | |
| Underwriting expense ratio | 29.3% | 27.5% | 1.8 % | | |
| Combined ratio | 92.0% | 87.3% | 4.7 % | | |
| Underwriting profit | | | | \$102 | \$156 |
| Aggregate — including exited lines | | | | | |
| Loss and LAE ratio | 62.7% | 58.5% | 4.2 % | | |
| Underwriting expense ratio | 29.3% | 27.5% | 1.8 % | | |
| Combined ratio | 92.0% | 86.0% | 6.0 % | | |
| Underwriting profit | | | | \$101 | \$173 |

The Specialty property and casualty insurance operations generated an underwriting profit of \$102 million for the fourth quarter of 2018 compared to \$156 million in the fourth quarter of 2017, a decrease of \$54 million (35%). Lower underwriting profitability in the Specialty casualty sub-segment, due primarily to higher catastrophe losses and lower favorable reserve development at Neon, and lower underwriting profit in the Property and transportation sub-segment, primarily the result of lower crop earnings, contributed to these results. Overall catastrophe losses were \$39 million (3.0 points on the combined ratio) in the fourth quarter of 2018 compared to \$8 million (0.6 points) in the fourth quarter of 2017. Net reinstatement premiums related to catastrophe losses were less than \$1 million in the

fourth quarter of 2018. In connection with catastrophe losses incurred in the fourth quarter of 2017, AFG paid \$4 million in net reinstatement premiums, resulting in a total pretax loss from catastrophes of \$12 million for the quarter. Losses related to third quarter 2018 catastrophes, primarily Hurricane Florence, developed favorably by \$7 million, primarily in the Property and transportation and Specialty financial sub-segments. Losses related to third quarter 2017 catastrophes, specifically Hurricanes Harvey, Irma and Maria, and two earthquakes in Mexico, developed favorably by \$25 million during the fourth quarter of 2017 across all property and casualty sub-segments.

Property and transportation Underwriting profit for this group was \$64 million for the fourth quarter of 2018 compared to \$84 million in the fourth quarter of 2017, a decrease of \$20 million (24%). Improved underwriting results in the transportation, property and inland marine and ocean marine operations were more than offset by lower underwriting profits in the agricultural businesses and the Singapore branch. The crop insurance operations reported strong profitability in the fourth quarter of 2018, albeit at lower levels than the fourth quarter of 2017. Catastrophe losses for this group had a favorable impact of \$2 million in

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the fourth quarter of 2018, compared to a favorable impact of \$3 million in the 2017 fourth quarter, with catastrophe losses reported from the previous quarter developing favorably in the fourth quarters of both years.

Specialty casualty Underwriting profit for this group was \$22 million for the fourth quarter of 2018 compared to \$58 million for the fourth quarter of 2017, a decrease of \$36 million (62%). Lower underwriting profit within Neon, primarily the result of higher 2018 catastrophe losses and lower year-over-year favorable reserve development due to the fourth quarter 2017 Neon reinsurance to close transaction, and to a lesser extent, lower profitability in the workers' compensation businesses contributed to the decrease in underwriting profit in the fourth quarter of 2018 compared to the prior year period. Higher underwriting profits in the excess and surplus lines and targeted markets businesses partially offset these results. Catastrophe losses were \$28 million (4.7 points on the combined ratio) for the fourth quarter of 2018 compared to \$14 million (2.5 points) and related net reinstatement premiums paid of \$4 million for the fourth quarter of 2017. Catastrophe losses for the fourth quarter of 2017 include the impact of the favorable reserve development on third quarter catastrophes discussed above.

Specialty financial Underwriting profit for this group was \$20 million for the fourth quarter of 2018 compared to \$19 million in the fourth quarter of 2017, an increase of \$1 million (5%). Each business within this group achieved profitable underwriting results in both periods. Catastrophe losses were \$10 million (7.1 points on the combined ratio) for the fourth quarter of 2018 compared to the favorable impact of catastrophes of \$5 million (3.7 points) for the fourth quarter of 2017. Catastrophe losses reported from the previous quarter developed favorably in the fourth quarters of both years.

Other specialty This group reported an underwriting loss of \$4 million for the fourth quarter of 2018 compared to \$5 million in the fourth quarter of 2017, an improvement of \$1 million (20%). The underwriting loss in the fourth quarter of 2018 is due primarily to losses in the business assumed by AFG's internal reinsurance program from the operations that make up AFG's other Specialty sub-segments. The underwriting loss in the fourth quarter of 2017 is due primarily to an \$8 million charge to adjust the deferred gain on the retroactive reinsurance transaction entered into in connection with the sale of businesses in 1998.

Aggregate Aggregate underwriting results for AFG's property and casualty insurance segment for the fourth quarter of 2017 includes favorable development in the Neon exited lines discussed in more detail below under "Net prior year reserve development."

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Losses and Loss Adjustment Expenses

AFG's overall loss and LAE ratio was 62.7% for the fourth quarter of 2018 compared to 58.5% for fourth quarter of 2017, an increase of 4.2 percentage points. The components of AFG's property and casualty losses and LAE amounts and ratio are detailed below (dollars in millions):

| | Three months ended December 31, | | | | Change in Ratio |
|--|------------------------------------|-------|---------|---------|-----------------------|
| | Amount | | Ratio | | |
| | 2018 | 2017 | 2018 | 2017 | |
| Property and transportation | | | | | |
| Current year, excluding catastrophe losses | \$335 | \$332 | 69.9% | 68.5% | 1.4 % |
| Prior accident years development | (7) | (4) | (1.5 %) | (0.8 %) | (0.7 %) |
| Current year catastrophe losses | (1) | (3) | (0.2 %) | (0.6 %) | 0.4 % |
| Property and transportation losses and LAE and ratio | \$327 | \$325 | 68.2% | 67.1% | 1.1 % |
| Specialty casualty | | | | | |
| Current year, excluding catastrophe losses | \$413 | \$376 | 67.3% | 65.8% | 1.5 % |
| Prior accident years development | (52) | (52) | (8.5 %) | (9.2 %) | 0.7 % |
| Current year catastrophe losses | 28 | 14 | 4.7 % | 2.5 % | 2.2 % |
| Specialty casualty losses and LAE and ratio | \$389 | \$338 | 63.5% | 59.1% | 4.4 % |
| Specialty financial | | | | | |
| Current year, excluding catastrophe losses | \$48 | \$51 | 34.5% | 36.0% | (1.5 %) |
| Prior accident years development | (7) | 1 | (5.2 %) | 0.8 % | (6.0 %) |
| Current year catastrophe losses | 10 | (5) | 7.1 % | (3.7 %) | 10.8 % |
| Specialty financial losses and LAE and ratio | \$51 | \$47 | 36.4% | 33.1% | 3.3 % |
| Total Specialty | | | | | |
| Current year, excluding catastrophe losses | \$818 | \$774 | 64.4% | 63.3% | 1.1 % |
| Prior accident years development | (61) | (49) | (4.7 %) | (4.1 %) | (0.6 %) |
| Current year catastrophe losses | 39 | 8 | 3.0 % | 0.6 % | 2.4 % |
| Total Specialty losses and LAE and ratio | \$796 | \$733 | 62.7% | 59.8% | 2.9 % |
| Aggregate — including exited lines | | | | | |
| Current year, excluding catastrophe losses | \$819 | \$774 | 64.4% | 63.3% | 1.1 % |
| Prior accident years development | (61) | (66) | (4.7 %) | (5.4 %) | 0.7 % |
| Current year catastrophe losses | 39 | 8 | 3.0 % | 0.6 % | 2.4 % |
| Aggregate losses and LAE and ratio | \$797 | \$716 | 62.7% | 58.5% | 4.2 % |

Current accident year losses and LAE, excluding catastrophe losses

The current accident year loss and LAE ratio, excluding catastrophe losses for AFG's Specialty property and casualty insurance operations was 64.4% for the fourth quarter of 2018 compared to 63.3% for the fourth quarter of 2017, an increase of 1.1 percentage points.

Property and transportation The 1.4 percentage points increase in the loss and LAE ratio for the current year, excluding catastrophe losses reflects an increase in the loss and LAE ratio in the aviation business and the Singapore branch, partially offset by a decrease in the loss and LAE ratio in the trucking business.

Specialty casualty The 1.5 percentage points increase in the loss and LAE ratio for the current year, excluding catastrophe losses reflects an increase in the loss and LAE ratio at Neon.

Specialty financial The 1.5 percentage points decrease in the loss and LAE ratio for the current year, excluding catastrophe losses reflects a decrease in the loss and LAE ratio of the equipment leasing and financial institutions businesses.

Net prior year reserve development

AFG's Specialty property and casualty insurance operations recorded net favorable reserve development related to prior accident years of \$61 million in the fourth quarter of 2018 compared to \$49 million in the fourth quarter of 2017, an increase of \$12 million (24%).

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Property and transportation Net favorable reserve development of \$7 million in the fourth quarter of 2018 reflects lower than expected claim frequency and severity at National Interstate and lower than expected losses in the crop business. Net favorable reserve development of \$4 million in the fourth quarter of 2017 reflects lower than expected losses in the crop business and lower than expected claim severity in the property and inland marine and trucking businesses, partially offset by higher than expected claim severity and frequency in the ocean marine business.

Specialty casualty Net favorable reserve development of \$52 million in the fourth quarter of 2018 reflects lower than anticipated claim severity in the workers' compensation businesses and lower than expected emergence in assumed 2017 property catastrophe losses at Neon. Net favorable reserve development of \$52 million in the fourth quarter of 2017 reflects favorable reserve development on ongoing lines of business within Neon recorded in connection with the reinsurance to close agreement entered into in December 2017 for the 2015 and prior years of account, lower than anticipated claim severity in the workers' compensation businesses and lower than expected losses in the executive liability business, partially offset by higher than anticipated claim severity in the targeted markets businesses and higher than anticipated severity in New York contractor claims.

In the fourth quarter of 2017, Neon entered into a reinsurance to close agreement for its 2015 and prior years of account, which transfers the responsibility for all of the liabilities that attach to the transferred year of account as well as any income due to the closing year of account in return for a premium. As a result of the reinsurance to close agreement, Neon recorded favorable development of \$42 million, of which \$24 million related to its ongoing lines of business (included in Specialty casualty) and \$18 million related to the exited lines of business (treated as non-core). See "Net prior year reserve development" under "Results of Operations — Property and Casualty Insurance Segment" for the years ended 2018, 2017 and 2016.

Specialty financial Net favorable reserve development of \$7 million in the fourth quarter of 2018 reflects lower than expected claim frequency and severity in the surety business and lower than anticipated claim frequency in run-off businesses. Net adverse reserve development of \$1 million in the fourth quarter of 2017 reflects higher than expected claim severity in the financial institutions business, partially offset by lower than anticipated claim frequency and severity in the surety business.

Other specialty In addition to the reserve development discussed above, total Specialty prior year reserve development for the fourth quarter of 2018 includes net adverse reserve development of \$5 million, reflecting adverse development associated with AFG's internal reinsurance program, partially offset by amortization of deferred gains on retroactive reinsurance. Total Specialty prior year reserve development for the fourth quarter of 2017 includes net adverse reserve development of \$6 million, reflecting an \$8 million charge to adjust the deferred gain on the retroactive reinsurance transaction entered into in connection with the sale of businesses in 1998, partially offset by the amortization of deferred gains on retroactive reinsurance.

Aggregate Aggregate net prior accident years reserve development for AFG's property and casualty insurance segment for the fourth quarter of 2017 includes the favorable development on the Neon exited lines discussed above and adverse reserve development of \$1 million related to business outside of the Specialty group that AFG no longer writes.

Catastrophe losses

AFG generally seeks to reduce its exposure to catastrophes through individual risk selection, including minimizing coastal and known fault-line exposures, and the purchase of reinsurance. Based on data available at December 31, 2018, AFG's exposure to a catastrophic earthquake or windstorm that industry models indicate should statistically occur once in every 100, 250 or 500 years as a percentage of AFG's Shareholders' Equity is shown below:

Impact of modeled loss on AFG's

Industry Model Shareholders' Equity

100-year event Less than 1%

250-year event Less than 3%

500-year event Approximately 6%

AFG maintains comprehensive catastrophe reinsurance coverage, including a \$15 million per occurrence net retention for its U.S.-based property and casualty insurance operations for losses up to \$100 million and a separate \$25 million per occurrence retention for Neon for losses up to \$250 million. AFG's property and casualty insurance operations further maintain supplemental fully collateralized reinsurance coverage up to 95% of \$200 million for catastrophe losses in excess of \$104 million of traditional catastrophe reinsurance through a catastrophe bond.

Catastrophe losses of \$39 million in the fourth quarter of 2018 resulted primarily from Hurricane Michael and wildfires in California. Catastrophe losses of \$8 million in the fourth quarter of 2017 resulted primarily from wildfires in California,

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partially offset by favorable development related to third quarter 2017 catastrophe losses, specifically Hurricanes Harvey, Irma and Maria, and two earthquakes in Mexico.

Commissions and Other Underwriting Expenses

AFG's property and casualty commissions and other underwriting expenses ("U/W Exp") were \$372 million in the fourth quarter of 2018 compared to \$336 million for the fourth quarter of 2017, an increase of \$36 million (11%). AFG's underwriting expense ratio, calculated as commissions and other underwriting expenses divided by net premiums earned, was 29.3% for the fourth quarter of 2018 compared to 27.5% for the fourth quarter of 2017, an increase of 1.8 percentage points. Detail of AFG's property and casualty commissions and other underwriting expenses and underwriting expense ratios is shown below (dollars in millions):

| | Three months ended December 31, | | | | Change in % of NEP |
|-----------------------------|------------------------------------|-------------|------------|-------------|-----------------------------|
| | 2018 | | 2017 | | |
| | U/W Exp | % of NEP | U/W Exp | % of NEP | |
| Property and transportation | \$88 | 18.3% | \$76 | 15.5% | 2.8 % |
| Specialty casualty | 202 | 33.0% | 177 | 30.9% | 2.1 % |
| Specialty financial | 70 | 49.1% | 75 | 53.1% | (4.0 %) |
| Other specialty | 12 | 35.8% | 8 | 36.8% | (1.0 %) |
| | \$372 | 29.3% | \$336 | 27.5% | 1.8 % |

Property and transportation Commissions and other underwriting expenses as a percentage of net earned premiums increased 2.8 percentage points in the fourth quarter of 2018 compared to the fourth quarter of 2017 reflecting lower premiums in the crop business, which has a lower expense ratio than AFG's overall Property and transportation group and an increase in the expense ratio in the transportation businesses.

Specialty casualty Commissions and other underwriting expenses as a percentage of net earned premiums increased 2.1 percentage points in the fourth quarter of 2018 compared to the fourth quarter of 2017 reflecting growth at Neon, which has a higher expense ratio than AFG's overall Specialty casualty group, higher dividends paid to policyholders in the workers' compensation businesses and lower underwriting, policy administration and claims services fees collected from unaffiliated insurers in the workers' compensation businesses.

Specialty financial Commissions and other underwriting expenses as a percentage of net earned premiums decreased 4.0 percentage points in the fourth quarter of 2018 compared to the fourth quarter of 2017 reflecting lower profitability-based commissions paid to agents in the financial institutions business and the impact of higher premiums on the ratio in the international operations.

Property and Casualty Net Investment Income

Net investment income in AFG's property and casualty insurance operations was \$115 million in the fourth quarter of 2018 compared to \$86 million in the fourth quarter of 2017, an increase of \$29 million (34%). The average invested assets and overall yield earned on investments held by AFG's property and casualty insurance operations are provided below (dollars in millions):

| | Three months ended December 31, | | | |
|-----------------------|------------------------------------|------|--------|-------------|
| | 2018 | 2017 | Change | % Change |
| Net investment income | \$115 | \$86 | \$29 | 34 % |

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| | | | | | |
|---|----------|----------|--------|---|---|
| Average invested assets (at amortized cost) | \$10,651 | \$10,062 | \$589 | 6 | % |
| Yield (net investment income as a % of average invested assets) | 4.32 | % 3.42 | % 0.90 | | % |
| Tax equivalent yield (*) | 4.49 | % 3.85 | % 0.64 | | % |

(*) Adjusts the yield on equity securities and tax-exempt bonds to the fully taxable equivalent yield.

The increase in net investment income in the property and casualty insurance segment for the fourth quarter of 2018 as compared to the fourth quarter of 2017 reflects growth in the property and casualty insurance segment and strong earnings from limited partnerships and similar investments. The property and casualty insurance segment's overall yield on investments (net investment income as a percentage of average invested assets) was 4.32% for the fourth quarter of 2018 compared to 3.42% for the fourth quarter of 2017, an increase of 0.90 percentage points, reflecting the higher earnings of limited partnerships and

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similar investments. AFG's property and casualty insurance operations recorded \$22 million in earnings from partnerships and similar investments and AFG-managed CLOs in the fourth quarter of 2018 compared to \$6 million in the fourth quarter of 2017, an increase of \$16 million (267%). The annualized yield earned on these investments was 13.8% in the fourth quarter of 2018 compared to 4.1% in the prior year period. The high returns from limited partnerships and similar investments should not be expected to repeat in future periods.

Property and Casualty Other Income and Expenses, Net

Other income and expenses, net for AFG's property and casualty insurance operations was a net expense of \$8 million for both the fourth quarter of 2018 and the fourth quarter of 2017. The table below details the items included in other income and expenses, net for AFG's property and casualty insurance operations (in millions):

| | Three months ended December 31, 2018 2017 | |
|--------------------------------|--|-------|
| Other income | \$2 | \$7 |
| Other expenses | | |
| Amortization of intangibles | 2 | 2 |
| Other | 8 | 13 |
| Total other expenses | 10 | 15 |
| Other income and expenses, net | \$(8) | \$(8) |

Other income for AFG's property and casualty insurance operations for the fourth quarter of 2017 includes a \$3 million death benefit on a life insurance policy.

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Annuity Segment — Results of Operations

AFG's annuity operations contributed \$20 million in pretax earnings in the fourth quarter of 2018 compared to \$97 million in the fourth quarter of 2017, a decrease of \$77 million (79%). This decrease in AFG's annuity segment results for the fourth quarter of 2018 as compared to the fourth quarter of 2017 is due primarily to the unfavorable impact of the significant decline in stock market performance on annuities with guaranteed withdrawal benefits and on the fair value of derivatives related to fixed-indexed annuities ("FIAs") in the fourth quarter of 2018. AFG's periodic detailed review ("unlocking") of the major actuarial assumptions underlying its annuity operations resulted in a net annuity charge of \$4 million in the fourth quarter of 2018 and \$3 million in the fourth quarter of 2017.

The following table details AFG's earnings before income taxes from its annuity operations for the three months ended December 31, 2018 and 2017 (dollars in millions):

| | Three months ended December 31, | | | |
|---|---------------------------------|-------|----------|---|
| | 2018 | 2017 | % Change | |
| Revenues: | | | | |
| Net investment income | \$419 | \$376 | 11 | % |
| Other income: | | | | |
| Guaranteed withdrawal benefit fees | 17 | 17 | — | % |
| Policy charges and other miscellaneous income | 10 | 7 | 43 | % |
| Total revenues | 446 | 400 | 12 | % |
| Costs and Expenses: | | | | |
| Annuity benefits (*) | 334 | 257 | 30 | % |
| Acquisition expenses | 56 | 15 | 273 | % |
| Other expenses | 36 | 31 | 16 | % |
| Total costs and expenses | 426 | 303 | 41 | % |
| Earnings before income taxes | \$20 | \$97 | (79) | % |

(*)Details of the components of annuity benefits provided below.

The following tables provide analysis of AFG's annuity earnings before income taxes (dollars in millions):

| | Three months ended December 31, | | | |
|---|---------------------------------|-------|----------|---|
| | 2018 | 2017 | % Change | |
| Earnings before income taxes — before the impact of unlocking and derivatives related to FIAs (see additional analysis below) | \$71 | \$111 | (36) | % |
| Unlocking | (4) | (3) | 33 | % |
| Impact of derivatives related to FIAs | (47) | (11) | 327 | % |
| Earnings before income taxes | \$20 | \$97 | (79) | % |

The vast majority of AFG's FIAs are indexed to the S&P 500, which decreased 14% in the fourth quarter of 2018. As highlighted in the table below, this poor stock market performance adversely impacted AFG's earnings before income taxes from its annuity operations beyond the impact on derivatives related to FIAs by \$30 million, particularly related to FIAs with guaranteed withdrawal benefits. If the stock market performance reverts back to AFG's long-term expectation over the life of these policies, management expects a substantial portion of this unfavorable impact to

reverse.

| | Three months ended December 31, | | | |
|--|---|-------|------|--------|
| | 2018 | 2017 | % | Change |
| Earnings before income taxes — before the impact of unlocking, derivatives related to FIAs and other impacts of stock market performance on FIAs | \$101 | \$104 | (3 | %) |
| Other impacts of stock market performance on FIAs: | | | | |
| FIAs with guaranteed withdrawal benefits | (22 |) 5 | (540 | %) |
| DPAC associated with FIAs | (8 |) 2 | (500 | %) |
| Earnings before income taxes — before the impact of unlocking and derivatives related to FIAs | \$71 | \$111 | (36 | %) |

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Annuity benefits consisted of the following (dollars in millions):

| | Three months ended December 31, | | |
|--|---------------------------------------|--------|----------|
| | 2018 | 2017 | % Change |
| Interest credited — fixed | \$ 186 | \$ 164 | 13 % |
| Interest credited — fixed component of variable annuities | 1 | 1 | — % |
| Other annuity benefits: | | | |
| Change in expected death and annuitization reserve | 4 | 5 | (20 %) |
| Amortization of sales inducements | 4 | 5 | (20 %) |
| Change in guaranteed withdrawal benefit reserve: | | | |
| Impact of change in the stock market | 22 | (5) | (540 %) |
| Accretion of benefits and other | 24 | 21 | 14 % |
| Change in other benefit reserves | 8 | 9 | (11 %) |
| Total other annuity benefits | 62 | 35 | 77 % |
| Total before impact of unlocking and derivatives related to FIAs | 249 | 200 | 25 % |
| Unlocking | 5 | 35 | (86 %) |
| Derivatives related to fixed-indexed annuities: | | | |
| Embedded derivative mark-to-market | (490) | 178 | (375 %) |
| Equity option mark-to-market | 570 | (156) | (465 %) |
| Impact of derivatives related to FIAs | 80 | 22 | 264 % |
| Total annuity benefits | \$ 334 | \$ 257 | 30 % |

See “Annuity Unlocking” below for a discussion of the impact that the periodic review of actuarial assumptions had on annuity benefit expense.

Net Spread on Fixed Annuities (excludes variable annuity earnings)

The profitability of a fixed annuity business is largely dependent on the ability of a company to earn income on the assets supporting the business in excess of the amounts credited to policyholder accounts plus expenses incurred (earning a “spread”). Performance measures such as net interest spread and net spread earned are often presented by annuity businesses to help users of their financial statements better understand the company’s performance.

The table below (dollars in millions) details the components of these spreads for AFG’s fixed annuity operations (including fixed-indexed and variable-indexed annuities):

| | Three months ended December 31, | | |
|---|------------------------------------|-----------|----------|
| | 2018 | 2017 | % Change |
| Average fixed annuity investments (at amortized cost) | \$ 35,993 | \$ 32,245 | 12 % |
| Average fixed annuity benefits accumulated | 36,103 | 32,680 | 10 % |
| As % of fixed annuity benefits accumulated (except as noted): | | | |
| Net investment income (as % of fixed annuity investments) | 4.64 | % 4.62 | % |
| Interest credited — fixed | (2.06 | %) (2.00 | %) |
| Net interest spread | 2.58 | % 2.62 | % |
| Policy charges and other miscellaneous income | 0.08 | % 0.10 | % |
| Other annuity benefit expenses, net of guaranteed withdrawal benefit fees | (0.51 | %) (0.21 | %) |
| Acquisition expenses | (0.59 | %) (0.60 | %) |

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| | | | | |
|--|-------|----|-------|----|
| Other expenses | (0.38 | %) | (0.37 | %) |
| Change in fair value of derivatives related to fixed-indexed annuities | (0.89 | %) | (0.27 | %) |
| Unlocking | (0.04 | %) | (0.06 | %) |
| Net spread earned on fixed annuities | 0.25 | % | 1.21 | % |

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The table below illustrates the impact of fair value accounting for derivatives related to fixed-indexed annuities on the annuity segment's net spread earned on fixed annuities:

| | Three months ended December 31, | |
|---|---------------------------------------|----------|
| | 2018 | 2017 |
| Net spread earned on fixed annuities — before impact of unlocking and derivatives related to FIAs | 0.81 % | 1.40 % |
| Unlocking | (0.04 %) | (0.06 %) |
| Impact of derivatives related to fixed-indexed annuities: | | |
| Change in fair value of derivatives | (0.89 %) | (0.27 %) |
| Related impact on amortization of DPAC (*) | 0.36 % | 0.14 % |
| Related impact on amortization of deferred sales inducements (*) | 0.01 % | — % |
| Net spread earned on fixed annuities | 0.25 % | 1.21 % |

(*) An estimate of the related acceleration/deceleration of the amortization of deferred policy acquisition costs and deferred sales inducements.

The net spread on fixed annuities before the impact of unlocking and derivatives related to FIAs decreased 0.59 percentage points to 0.81% for the fourth quarter of 2018 from 1.40% for the fourth quarter of 2017 due primarily to the impact of poor stock market performance on annuities with guaranteed withdrawal benefits. As previously noted, if the stock market performance reverts back to AFG's long-term expectation over the life of these policies, a substantial portion of this unfavorable impact would be expected to reverse.

Annuity Net Investment Income

Net investment income for the fourth quarter of 2018 was \$419 million compared to \$376 million for the fourth quarter of 2017, an increase of \$43 million (11%). This increase reflects the growth in AFG's annuity business and higher earnings from limited partnerships and similar investments, partially offset by the impact of lower fixed maturity investment yields. The overall yield earned on investments in AFG's fixed annuity operations, calculated as net investment income divided by average investment balances (at amortized cost), increased by 0.02 percentage points to 4.64% from 4.62% in the fourth quarter of 2018 compared to the fourth quarter of 2017. The net investment yield between periods reflects higher earnings from limited partnerships and similar investments, offset by the impact of the reinvestment of proceeds from maturity and redemption of higher yielding investments at the lower yields available in the financial markets. For the period from October 1, 2017 through December 31, 2018, \$5.8 billion in annuity segment investments with an average yield of approximately 4.9% were redeemed or sold with the proceeds reinvested at an approximately 0.5% lower yield.

Annuity Interest Credited — Fixed

Interest credited — fixed for the fourth quarter of 2018 was \$186 million compared to \$164 million for the fourth quarter of 2017, an increase of \$22 million (13%). This increase reflects the impact of growth in the annuity business. The average interest rate credited to policyholders, calculated as interest credited divided by average fixed annuity benefits accumulated, increased 0.06 percentage points to 2.06% in the fourth quarter of 2018 from 2.00% in the fourth quarter of 2017 due to higher crediting rates on new business.

Annuity Net Interest Spread

AFG's net interest spread decreased 0.04 percentage points to 2.58% from 2.62% in the fourth quarter of 2018 compared to the same period in 2017 due primarily to higher crediting rates on new business and lower fixed maturity investment yields, partially offset by higher earnings from limited partnerships and similar investments. Features included in current annuity product offerings allow AFG to achieve its desired profitability at a lower net interest spread than historical product offerings. As a result, AFG expects its net interest spread to narrow in the future.

Annuity Policy Charges and Other Miscellaneous Income

Annuity policy charges and other miscellaneous income, which consist primarily of surrender charges, amortization of deferred upfront policy charges (unearned revenue) and income from sales of real estate were \$10 million in the fourth quarter of 2018 and \$7 million the fourth quarter of 2017, an increase of \$3 million (43%). Excluding the impact of unlocking charges of \$3 million in the fourth quarter of 2017 related to unearned revenue, annuity policy charges and other miscellaneous income were \$10 million in both the fourth quarter of 2018 and 2017. Excluding the impact of unlocking charges related to unearned revenue, annuity policy charges and other miscellaneous income as a percentage of average fixed annuity benefits accumulated decreased 0.02 percentage points to 0.08% in the fourth quarter of 2018 from 0.10% in the fourth quarter of 2017.

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See “Annuity Unlocking” below for a discussion of the impact that the periodic review of actuarial assumptions had on annuity policy charges and other miscellaneous income.

Other Annuity Benefits, Net of Guaranteed Withdrawal Benefit Fees

Other annuity benefits, net of guaranteed withdrawal benefit fees (excluding the impact of unlocking) for the fourth quarter of 2018 were \$45 million compared to \$18 million for the fourth quarter of 2017, an increase of \$27 million (150%). As a percentage of average fixed annuity benefits accumulated, these net expenses increased 0.30 percentage points to 0.51% from 0.21% in the fourth quarter of 2018 compared to the fourth quarter of 2017. In addition to interest credited to policyholders’ accounts and the change in fair value of derivatives related to fixed-indexed annuities, annuity benefits expense also includes the following expenses (in millions, net of guaranteed withdrawal benefit fees):

| | Three months ended December 31, 2018 2017 | |
|--|--|-------|
| Change in expected death and annuitization reserve | \$4 | \$5 |
| Amortization of sales inducements | 4 | 5 |
| Change in guaranteed withdrawal benefit reserve: | | |
| Impact of change in the stock market | 22 | (5) |
| Accretion of benefits and other | 24 | 21 |
| Change in other benefit reserves | 8 | 9 |
| Other annuity benefits | 62 | 35 |
| Offset guaranteed withdrawal benefit fees | (17) | (17) |
| Other annuity benefits, net | \$45 | \$18 |

As discussed under “Annuity Benefits Accumulated” in Note A — “Accounting Policies” to the financial statements, guaranteed withdrawal benefit reserves are accrued for and modified using assumptions similar to those used in establishing and amortizing deferred policy acquisition costs. The guaranteed withdrawal benefit reserve related to FIAs can be inversely impacted by the calculated FIA embedded derivative reserve as the value to policyholders of the guaranteed withdrawal benefits increases when the benefit of stock market participation decreases. As shown in the table above, the change in the stock market increased AFG’s guaranteed withdrawal benefit reserve by \$22 million in the fourth quarter of 2018 compared to a favorable impact of \$5 million in the fourth quarter of 2017. This \$27 million increase (540%) was the primary cause of the \$27 million overall increase in other annuity benefits, net of guaranteed withdrawal fees in the fourth quarter of 2018 compared to the fourth quarter of 2017.

See “Annuity Unlocking” below for a discussion of the impact that the periodic review of actuarial assumptions had on annuity benefits expense.

Annuity Acquisition Expenses

Annuity acquisition expenses for the fourth quarter of 2018 were \$56 million compared to \$15 million for the fourth quarter of 2017, an increase of \$41 million (273%). Excluding the \$1 million and \$35 million favorable impact on amortization of DPAC from the unlocking recorded in the fourth quarter of 2018 and 2017, respectively, annuity acquisition expenses were \$57 million for the fourth quarter of 2018 compared to \$50 million for the fourth quarter of 2017, an increase of \$7 million (14%), reflecting growth in the business. Excluding the impact of unlocking charges discussed under “Annuity Unlocking” below, AFG’s amortization of DPAC and commission expenses as a percentage of average fixed annuity benefits accumulated was 0.59% for the fourth quarter of 2018 compared to 0.60% for the fourth quarter of 2017 and has generally ranged between 0.75% and 0.85%. Variances from the general range relate

primarily to the impact of (i) material changes in interest rates or the stock market on AFG's FIA business, and (ii) differences in actual experience from actuarially projected estimates and assumptions. For example, the unfavorable impact of the significant decline in stock market performance during the fourth quarter of 2018 and the unfavorable impact of lower than anticipated interest rates in the fourth quarter of 2017 on the fair value of derivatives related to FIAs both resulted in a partially offsetting deceleration in the amortization of DPAC.

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The table below illustrates the estimated impact of fair value accounting for derivatives related to fixed-indexed annuities on annuity acquisition expenses as a percentage of average fixed annuity benefits accumulated (excluding the impact of unlocking):

| | Three months ended December 31, | |
|---|---------------------------------|----------|
| | 2018 | 2017 |
| Before the impact of changes in the fair value of derivatives related to FIAs on the amortization of DPAC | 0.95 % | 0.74 % |
| Impact of changes in fair value of derivatives related to FIAs on the amortization of DPAC (*) | (0.36 %) | (0.14 %) |
| Annuity acquisition expenses as a % of fixed annuity benefits accumulated | 0.59 % | 0.60 % |

(*) An estimate of the acceleration/deceleration in the amortization of deferred policy acquisition costs resulting from fair value accounting for derivatives related to fixed-indexed annuities.

As illustrated in the table above, changes in the fair value of derivatives related to FIAs decreased annuity acquisition expenses as a percentage of average fixed annuity benefits accumulated by 0.36% in the fourth quarter of 2018 compared to 0.14% in the fourth quarter of 2017. In the fourth quarter of 2018, the favorable impact of the deceleration in the amortization of DPAC related to changes in the fair value of derivatives related to FIAs on annuity acquisition expenses as a percentage of average fixed annuity benefits accumulated was substantially offset by the unfavorable impact of poor stock market performance on projected future investment income generated by the investment of the projected net proceeds from the call and put options used in the FIA business. Depending on the timing and extent of a recovery in the stock market, a portion of this unfavorable impact would be expected to reverse.

See “Annuity Unlocking” below for a discussion of the impact that the periodic review of actuarial assumptions had on annuity and supplemental insurance acquisition expenses. Unanticipated spread compression, decreases in the stock market, adverse mortality experience, and higher than expected lapse rates could lead to future write-offs of DPAC or the present value of future profits on business in force of companies acquired (“PVFP”).

Annuity Other Expenses

Annuity other expenses were \$36 million for the fourth quarter of 2018 compared to \$31 million for the fourth quarter of 2017, an increase of \$5 million (16%). Annuity other expenses represent primarily general and administrative expenses, as well as selling and issuance expenses that are not deferred. The increase in annuity other expenses reflects primarily growth in the business and an increase in the number of sales personnel focused on new initiatives and increased market share within existing financial institutions and retail marketing organizations in the fourth quarter of 2018 compared to the fourth quarter of 2017. As a percentage of average fixed annuity benefits accumulated, these expenses increased 0.01 percentage points to 0.38% from 0.37% for the fourth quarter of 2018 as compared to the fourth quarter of 2017 due primarily to growth in the business.

Change in Fair Value of Derivatives Related to Fixed-Indexed (Including Variable-Indexed) Annuities

AFG’s fixed-indexed (including variable-indexed) annuities provide policyholders with a crediting rate tied, in part, to the performance of an existing stock market or other financial index. AFG attempts to mitigate the risk in the index-based component of these products through the purchase and sale of call and put options on the appropriate index. AFG’s strategy is designed so that the change in the fair value of the call option assets and put option liabilities will generally offset the economic change in the net liability from the index participation. Both the index-based component of the annuities (an embedded derivative) and the related call and put options are considered derivatives that must be adjusted for changes in fair value through earnings each period. The fair values of these derivatives are impacted by actual and expected stock market performance and interest rates as well as other factors. For a list of other factors impacting the fair value of the embedded derivative component of AFG’s annuity benefits accumulated, see Note D — “Fair Value Measurements” to the financial statements. Fluctuations in certain of these factors, such as

changes in interest rates and the performance of the stock market, are not economic in nature for the current reporting period, but rather impact the timing of reported results.

Excluding the impact of unlocking charges, the net change in fair value of derivatives related to fixed-indexed annuities increased annuity benefits by \$80 million in the fourth quarter of 2018 and \$22 million in the fourth quarter of 2017. The change in the fair value of these derivatives includes \$11 million in the fourth quarter of 2018 and \$5 million in the fourth quarter of 2017 in interest accreted on the embedded derivative (before DPAC amortization), an increase of \$6 million (120%). AFG expects both the size of the embedded derivative and interest rates to rise, resulting in continued increases in interest on the embedded derivative. The \$80 million increase in annuity benefits in the fourth quarter of 2018 reflects the negative impact of the significant decline in the stock market on the fair value of these derivatives. The \$22 million increase in annuity benefits in the fourth quarter of 2017 reflects the negative impact of lower than anticipated interest rates on the fair value of these derivatives, partially offset by the positive impact of strong stock market performance. As a percentage of average fixed annuity benefits accumulated, this net expense increased 0.62 percentage points to 0.89% in the fourth quarter of 2018 from 0.27% in

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the fourth quarter of 2017.

Fluctuations in interest rates and the stock market, among other factors, can cause volatility in the periodic measurement of fair value of the embedded derivative that management believes can be inconsistent with the long-term economics of these products. The table below illustrates the impact of fair value accounting for derivatives related to fixed-indexed annuities on the annuity segment's earnings before income taxes (dollars in millions):

| | Three months ended December 31, 2018 2017 % Change | | |
|---|---|-------|--------|
| Earnings before income taxes — before unlocking and change in fair value of derivatives related to FIAs | \$71 | \$111 | (36 %) |
| Unlocking | (4) | (3) | 33 % |
| Impact of derivatives related to fixed-indexed annuities: | | | |
| Change in fair value of derivatives related to FIAs | (80) | (22) | 264 % |
| Related impact on amortization of DPAC (*) | 33 | 11 | 200 % |
| Earnings before income taxes | \$20 | \$97 | (79 %) |

(*) An estimate of the related acceleration/deceleration of amortization of deferred sales inducements and deferred policy acquisition costs.

As illustrated in the table above, the change in fair value of derivatives related to fixed-indexed annuities, including the related impact on amortization of DPAC, decreased the annuity segment's earnings before income taxes by \$47 million in the fourth quarter of 2018 and \$11 million in the fourth quarter of 2017.

The following table provides analysis of the primary factors impacting the change in the fair value of derivatives related to FIAs. Each factor is presented net of the estimated related impact on amortization of DPAC (dollars in millions).

| | Three months ended December 31, 2018 2017 % Change | | |
|--|---|--------|---------|
| Interest on the embedded derivative liability | \$(11) | \$(5) | 120 % |
| Change in the stock market, including volatility | (27) | 9 | (400 %) |
| Changes in interest rates higher (lower) than expected | (4) | (12) | (67 %) |
| Renewal option costs lower (higher) than expected | 1 | — | — % |
| Other, including the impact of actual versus expected lapses | (6) | (3) | 100 % |
| Impact of derivatives related to FIAs | \$(47) | \$(11) | 327 % |

The change in the fair value of derivatives related to FIAs includes an ongoing expense for annuity interest accreted on the embedded derivative reserve. The amount of interest accreted in any period is generally based on the size of the embedded derivative and current interest rates. AFG expects both the size of the embedded derivative and interest rates to rise, resulting in continued increases in interest on the embedded derivative liability.

In the fourth quarter of 2018, the 14% decline in the S&P 500 Index had a \$27 million unfavorable impact on the derivatives related to FIAs compared to a \$9 million favorable impact of strong stock market performance on these derivatives in the fourth quarter of 2017. The derivatives related to FIAs were unfavorably impacted by lower than expected interest rates in the fourth quarter of both 2018 and 2017. Management believes that the majority of this impact is non-economic and is expected to reverse over time, even in the absence of a stock market recovery.

See “Annuity Unlocking” below for a discussion of the impact that the periodic review of actuarial assumptions had on the change in the fair value of the embedded derivative liability.

Annuity Net Spread Earned on Fixed Annuities

AFG’s net spread earned on fixed annuities decreased 0.96 percentage points to 0.25% from 1.21% in the fourth quarter of 2018 compared to the same period in 2017 due primarily to the net impact of poor stock market performance on annuities with guaranteed withdrawal benefits, changes in the fair value of derivatives and related DPAC amortization offset discussed above and the 0.04 percentage points decrease in AFG’s net interest spread.

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Annuity Benefits Accumulated

Annuity premiums received and benefit payments are recorded as increases or decreases in annuity benefits accumulated rather than as revenue and expense. Increases in this liability for interest credited and other benefits are charged to expense and decreases for surrender and other policy charges are credited to other income.

For certain products, annuity benefits accumulated also includes reserves for accrued persistency and premium bonuses, excess benefits expected to be paid on future deaths and annuitizations (“EDAR”) and guaranteed withdrawal benefits. Annuity benefits accumulated also includes amounts advanced from the Federal Home Loan Bank of Cincinnati. The following table is a progression of AFG’s annuity benefits accumulated liability for the three months ended December 31, 2018 and 2017 (in millions):

| | Three months ended December 31, | |
|---|---------------------------------------|----------|
| | 2018 | 2017 |
| Beginning fixed annuity reserves | \$35,774 | \$32,354 |
| Fixed annuity premiums (receipts) | 1,476 | 903 |
| Federal Home Loan Bank advances and repayments | 225 | (64) |
| Surrenders, benefits and other withdrawals | (796) | (596) |
| Interest and other annuity benefit expenses: | | |
| Interest credited | 186 | 164 |
| Embedded derivative mark-to-market | (490) | 178 |
| Change in other benefit reserves | 52 | 25 |
| Unlocking | 4 | 41 |
| Ending fixed annuity reserves | \$36,431 | \$33,005 |
| Reconciliation to annuity benefits accumulated per balance sheet: | | |
| Ending fixed annuity reserves (from above) | \$36,431 | \$33,005 |
| Impact of unrealized investment gains | 10 | 133 |
| Fixed component of variable annuities | 175 | 178 |
| Annuity benefits accumulated per balance sheet | \$36,616 | \$33,316 |

Statutory Annuity Premiums

AFG’s annuity operations generated statutory premiums of \$1.48 billion in the fourth quarter of 2018 compared to \$909 million in the fourth quarter of 2017, an increase of \$573 million (63%). The following table summarizes AFG’s annuity sales (dollars in millions):

| | Three months ended December 31, | | | |
|---|---|-------|----------|---|
| | 2018 | 2017 | % Change | |
| Financial institutions single premium annuities — indexed | \$455 | \$364 | 25 | % |
| Financial institutions single premium annuities — fixed | 142 | 63 | 125 | % |
| Retail single premium annuities — indexed | 392 | 239 | 64 | % |
| Retail single premium annuities — fixed | 27 | 15 | 80 | % |
| Broker dealer single premium annuities — indexed | 335 | 174 | 93 | % |
| Broker dealer single premium annuities — fixed | 4 | 1 | 300 | % |
| Pension risk transfer | 75 | 6 | 1,150 | % |
| Education market — fixed and indexed annuities | 46 | 41 | 12 | % |

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| | | | | |
|------------------------------|---------|-------|----|---|
| Total fixed annuity premiums | 1,476 | 903 | 63 | % |
| Variable annuities | 6 | 6 | — | % |
| Total annuity premiums | \$1,482 | \$909 | 63 | % |

Management attributes the 63% increase in annuity premiums in the fourth quarter of 2018 compared to the fourth quarter of 2017 to the introduction of new products, efforts to expand in the retail and broker dealer markets and an overall improving interest rate environment during 2018.

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Annuity Unlocking

In the fourth quarters of 2018 and 2017, AFG conducted a detailed review (“unlocking”) of the major actuarial assumptions underlying its annuity operations. As a result of these reviews, AFG recorded a net charge related to its annuity business of \$4 million in 2018 and \$3 million in 2017, which impacted AFG’s financial statements as follows (in millions):

| | Three months ended December 31, 2018 2017 | |
|--|--|-------|
| Policy charges and other miscellaneous income: | | |
| Unearned revenue | \$— | \$(3) |
| Total revenues | — | (3) |
| Annuity benefits: | | |
| Fixed-indexed annuity embedded derivative | — | 25 |
| Sales inducements | 1 | (6) |
| Other reserves | 4 | 16 |
| Total annuity benefits | 5 | 35 |
| Annuity and supplemental insurance acquisition expenses: | | |
| Deferred policy acquisition costs | (1) | (35) |
| Total costs and expenses | 4 | — |
| Net charge | \$(4) | \$(3) |

The net charge from unlocking annuity assumptions in the fourth quarter of 2018 reflects the favorable impact of an increase in projected net interest spreads on in-force business (due primarily to higher actual yields than previously anticipated), more than offset by a slight increase in projected expenses and the unfavorable impact of changes in projected policyholder annuitization and lapse behavior. Reinvestment rate assumptions are based primarily on 7-year and 10-year corporate bond yields. For the fourth quarter 2018 unlocking, AFG assumed a net reinvestment rate (net of default and expense assumptions) of 4.68% in 2019, grading up ratably to an ultimate net reinvestment rate of 5.54% in 2025 and beyond.

The table below compares the reinvestment rate assumed on assets purchased to directly support “fixed annuity benefits accumulated” in AFG’s fourth quarter unlockings for the next calendar year to the actual reinvestment rate achieved in that period (both net of investment expenses):

| Unlocking Year | First Investment Period | Reinvestment Rate | |
|-------------------|-------------------------------|----------------------|----------|
| | | Assumed (*) | Achieved |
| 2015 | 2016 | 4.05% | 4.27% |
| 2016 | 2017 | 4.42% | 3.95% |
| 2017 | 2018 | 4.17% | 4.57% |
| 2018 | 2019 | 4.86% | n/a |

(*) Assumed reinvestment rates exclude default rates of 0.18% in each period.

Management believes that these results over the last several years demonstrate that AFG’s investment rate assumptions are reasonable and prudent. During 2018, credit spreads widened resulting in a higher achieved reinvestment rate than assumed in the 2017 unlocking. During 2017, long-term interest rates were lower than anticipated and credit spreads

narrowed, resulting in a lower achieved reinvestment rate than assumed in the 2016 unlocking. In addition to the reinvestment rates above, actual default rates in 2018, 2017 and 2016 were lower than the long-term default rates of 0.18% assumed in the unlocking in each of the periods above.

The 2017 net charge reflects the unfavorable impacts of a decrease in projected net interest spreads on in-force business (due primarily to lower than previously anticipated reinvestment rates), a slight increase in projected expenses (due primarily to an increase in projected trailer commissions) and slightly higher projected option costs in the near term, substantially offset by the favorable impact of changes in projected policyholder annuitization and lapse behavior. For the 2017 unlocking, AFG assumed a net reinvestment rate (net of default and expense assumptions) of 3.99% in 2018, grading up ratably to an ultimate net reinvestment rate of 5.55% in 2023 and beyond.

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Annuity Earnings before Income Taxes Reconciliation

The following table reconciles the net spread earned on AFG's fixed annuities to overall annuity pretax earnings for the three months ended December 31, 2018 and 2017 (in millions):

| | Three months ended December 31, 2018 2017 | |
|--|--|------|
| Earnings on fixed annuity benefits accumulated | \$22 | \$99 |
| Earnings impact of investments in excess of fixed annuity benefits accumulated (*) | (1) | (5) |
| Variable annuity earnings (loss) | (1) | 3 |
| Earnings before income taxes | \$20 | \$97 |

Net investment income (as a % of investments) of 4.64% and 4.62% for the three months ended December 31, (*)2018 and 2017, respectively, multiplied by the difference between average fixed annuity investments (at amortized cost) and average fixed annuity benefits accumulated in each period.

Holding Company, Other and Unallocated — Results of Operations AFG's net GAAP pretax loss outside of its property and casualty insurance and annuity operations (excluding realized gains and losses) totaled \$29 million for the fourth quarter of 2018 compared to \$87 million for the fourth quarter of 2017, a decrease of \$58 million (67%). AFG's net core pretax loss outside of its property and casualty insurance and annuity operations (excluding realized gains and losses) totaled \$29 million in the fourth quarter of 2018 compared to \$47 million in the fourth quarter of 2017, a decrease of \$18 million (38%).

The following table details AFG's GAAP and core loss before income taxes from operations outside of its property and casualty insurance and annuity operations for the three months ended December 31, 2018 and 2017 (dollars in millions):

| | Three months ended December 31, 2018 2017 % Change | | |
|---|---|-------|--------|
| Revenues: | | | |
| Life, accident and health net earned premiums | \$6 | \$5 | 20 % |
| Net investment income | 4 | 10 | (60 %) |
| Other income — P&C fees | 19 | 20 | (5 %) |
| Other income | 9 | 5 | 80 % |
| Total revenues | 38 | 40 | (5 %) |
| Costs and Expenses: | | | |
| Property and casualty insurance — commissions and other underwriting expenses | 6 | 9 | (33 %) |
| Life, accident and health benefits | 8 | 5 | 60 % |
| Life, accident and health acquisition expenses | 2 | 2 | — % |
| Other expense — expenses associated with P&C fees | 13 | 11 | 18 % |
| Other expenses (*) | 22 | 40 | (45 %) |
| Costs and expenses, excluding interest charges on borrowed money | 51 | 67 | (24 %) |
| Core loss before income taxes, excluding realized gains and losses and interest charges on borrowed money | (13) | (27) | (52 %) |

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| | | | | | | |
|--|--------|--------|-----|------|-----|----|
| Interest charges on borrowed money | 16 | 20 | (20 | %) | | |
| Core loss before income taxes, excluding realized gains and losses | (29 |) | (47 |) | (38 | %) |
| Pretax non-core loss on retirement of debt | — | (40 |) | (100 | %) | |
| GAAP loss before income taxes, excluding realized gains and losses | \$(29) | \$(87) | (67 | %) | | |

(*)Excludes a pretax non-core loss on retirement of debt of \$40 million in the fourth quarter of 2017.

Holding Company and Other — Life, Accident and Health Premiums, Benefits and Acquisition Expenses

AFG's run-off long-term care and life insurance operations recorded net earned premiums of \$6 million and related benefits and acquisition expenses of \$10 million in the fourth quarter of 2018 compared to net earned premiums of \$5 million and related benefits and acquisition expenses of \$7 million in the fourth quarter of 2017. The \$3 million (60%) increase in life, accident and health benefits reflects higher claims in the run-off long-term care business.

Holding Company and Other — Net Investment Income

AFG recorded net investment income on investments held outside of its property and casualty insurance and annuity operations of \$4 million in the fourth quarter of 2018 compared to \$10 million in the fourth quarter of 2017, a decrease of \$6 million

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(60%). The parent company holds a small portfolio of securities that are carried at fair value through net investment income. These securities decreased in value by \$5 million in the fourth quarter of 2018 compared to an increase of \$2 million in the fourth quarter of 2017.

Holding Company and Other — P&C Fees and Related Expenses

Summit, a workers' compensation insurance subsidiary, collects fees from a small group of unaffiliated insurers for providing underwriting, policy administration and claims services. In addition, certain of AFG's property and casualty insurance businesses collect fees from customers for ancillary services such as workplace safety programs and premium financing. In the fourth quarter of 2018, AFG collected \$19 million in fees for these services compared to \$20 million in the fourth quarter of 2017. Management views this fee income, net of the \$13 million in the fourth quarter of 2018 and \$11 million in the fourth quarter of 2017, in expenses incurred to generate such fees, as a reduction in the cost of underwriting its property and casualty insurance policies. Consistent with internal management reporting, these fees and the related expenses are netted and recorded as a reduction of commissions and other underwriting expenses in AFG's segmented results.

Holding Company and Other — Other Income

Other income in the table above includes \$4 million in both the fourth quarter of 2018 and 2017, in management fees paid to AFG by the AFG-managed CLOs (AFG's consolidated managed investment entities). The management fees are eliminated in consolidation — see the other income line in the Consolidate MIEs column under "Results of Operations — Segmented Statement of Earnings." Excluding amounts eliminated in consolidation, AFG recorded \$5 million in other income outside of its property and casualty insurance and annuity operations in the fourth quarter of 2018 compared to \$1 million in the fourth quarter of 2017. The increase in other income is due primarily to the impact of a loss recorded on the disposal of equipment in the fourth quarter of 2017.

Holding Company and Other — Other Expenses

Excluding the non-core loss on retirement of debt discussed below, AFG's holding companies and other operations outside of its property and casualty insurance and annuity operations recorded other expenses of \$22 million in the fourth quarter of 2018 compared to \$40 million in the fourth quarter of 2017, a decrease of \$18 million (45%). This decrease is due primarily to the impact of lower holding company expenses related to employee benefit plans that are tied to stock market performance in the fourth quarter of 2018 compared to the fourth quarter of 2017.

Holding Company and Other — Interest Charges on Borrowed Money

AFG's holding companies and other operations outside of its insurance operations recorded interest expense of \$16 million in the fourth quarter of 2018 compared to \$20 million in the fourth quarter of 2017, a decrease of \$4 million (20%). This decrease is due primarily to a lower weighted average interest rate on AFG's outstanding debt. The following table details the principal amount of AFG's long-term debt balances as of October 1, 2018 compared to October 1, 2017 (dollars in millions):

| | October 1, 2018 | October 1, 2017 | | |
|---|--------------------|--------------------|---|--|
| Direct obligations of AFG: | | | | |
| 4.50% Senior Notes due June 2047 | \$ 590 | \$ 350 | | |
| 3.50% Senior Notes due August 2026 | 425 | 300 | | |
| 9-7/8% Senior Notes due June 2019 | — | 350 | | |
| 6-1/4% Subordinated Debentures due September 2054 | 150 | 150 | | |
| 6% Subordinated Debentures due November 2055 | 150 | 150 | | |
| Other | 3 | 3 | | |
| Total principal amount of Holding Company Debt | \$ 1,318 | \$ 1,303 | | |
| Weighted Average Interest Rate | 4.6 | % 6.1 | % | |

The decrease in the weighted average interest rate for the fourth quarter of 2018 as compared to the fourth quarter of 2017 reflects the following financing transactions completed by AFG between October 1, 2017 and December 31, 2017:

Issued an additional \$125 million of 3.50% Senior Notes on November 9, 2017

Issued an additional \$240 million of 4.50% Senior Notes on November 9, 2017

Redeemed \$350 million of 9-7/8% Senior Notes on December 11, 2017

Holding Company and Other — Loss on Retirement of Debt

On December 11, 2017, AFG redeemed its \$350 million outstanding principal amount of 9-7/8% Senior Notes due 2019 and recorded a pretax loss on retirement of debt of \$40 million, primarily a \$38 million make-whole premium.

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Consolidated Realized Gains (Losses) on Securities AFG's consolidated realized gains (losses) on securities, which are not allocated to segments, were net losses of \$238 million in the fourth quarter of 2018 compared to net gains of \$6 million in the fourth quarter of 2017, a decrease of \$244 million (4,067%). Realized gains (losses) on securities consisted of the following (in millions):

| | Three months ended December 31, 2018 | | 2017 | |
|--|--------------------------------------|--|-------|--|
| Realized gains (losses) before impairments: | | | | |
| Disposals | \$(2) | | \$26 | |
| Change in the fair value of equity securities (*) | (223) | | — | |
| Change in the fair value of derivatives | 3 | | (2) | |
| Adjustments to annuity deferred policy acquisition costs and related items | — | | 2 | |
| | (222) | | 26 | |
| Impairment charges: | | | | |
| Securities | (23) | | (23) | |
| Adjustments to annuity deferred policy acquisition costs and related items | 7 | | 3 | |
| | (16) | | (20) | |
| Realized gains (losses) on securities | \$(238) | | \$6 | |

As discussed in Note A — “Accounting Policies — Investments,” beginning in January 2018, all equity securities other (*) than those accounted for under the equity method are carried at fair value through net earnings. This amount includes a \$228 million net loss on securities that were still held at December 31, 2018.

The \$223 million net realized loss from the change in the fair value of equity securities in the fourth quarter of 2018 includes losses of \$65 million on banks and financing companies, \$23 million on asset management companies, \$22 million on energy exploration and production companies and \$21 million on technology companies. AFG's impairment charges on securities for the fourth quarter of 2018 consist of \$23 million on fixed maturities compared to \$14 million on equity securities, \$5 million on fixed maturities and \$4 million on other investments in the fourth quarter of 2017. The 2018 fourth quarter impairment charges consisted of \$17 million on corporate bonds and \$6 million on residential MBS. Approximately \$11 million in impairment charges in the fourth quarter of 2017 related to financial institutions and \$4 million related to investments in pharmaceutical companies.

Consolidated Income Taxes AFG's consolidated provision (credit) for income taxes was a credit of \$4 million for the fourth quarter of 2018 compared to an expense of \$101 million in the fourth quarter of 2017. The following is a reconciliation of income taxes at the statutory rate (21% in 2018 and 35% in 2017) to the provision (credit) for income taxes as shown in the segmented statement of earnings (dollars in millions):

| | Three months ended December 31, 2018 | | 2017 | |
|---|--------------------------------------|----------|--------|----------|
| | Amount | % of EBT | Amount | % of EBT |
| Earnings (loss) before income taxes (“EBT”) | \$(39) | | \$267 | |
| Income taxes at statutory rate | \$(8) | 21 % | \$93 | 35 % |
| Effect of: | | | | |
| Tax exempt interest | (3) | 8 % | (6) | (2 %) |
| Adjustment to prior year taxes | 1 | (3 %) | (2) | (1 %) |

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| | | | | |
|--|--------|--------|-------|--------|
| Stock-based compensation | (1) | 3 % | (2) | (1 %) |
| Dividend received deduction | (1) | 3 % | (2) | (1 %) |
| Employee stock ownership plan dividend paid deduction | (1) | 3 % | (3) | (1 %) |
| Foreign operations | (5) | 13 % | 14 | 5 % |
| Change in valuation allowance (excluding change in tax rate) | 8 | (21 %) | (23) | (9 %) |
| Nondeductible expenses | 2 | (5 %) | 1 | — % |
| Neon restructuring | — | — % | (56) | (21 %) |
| Change in U.S. corporate tax rate | — | — % | 83 | 31 % |
| Other | 4 | (12 %) | 4 | 3 % |
| Provision (credit) for income taxes | \$(4) | 10 % | \$101 | 38 % |

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The impact of “foreign operations” for the fourth quarter of 2017 in the table above relates to a reduction in the “foreign underwriting losses” deferred tax asset as a result of the sale of the noncontrolling interest in Neon. Since AFG maintains a full valuation allowance against the deferred tax assets related to Neon, this reduction in deferred tax assets was offset by a corresponding reduction in the valuation allowance and had no overall impact on AFG’s income tax expense or results of operations.

The changes in valuation allowance in the table above are primarily related to the cumulative losses in the Neon Lloyd’s insurance business. Due to the uncertainty concerning the realization of the deferred tax benefits associated with these losses, AFG maintains a full valuation allowance against these deferred tax assets. The \$61 million decrease in the valuation allowance in the fourth quarter of 2017 related to the change in the U.S. corporate tax rate is included in “Change in U.S. corporate tax rate” in the table above.

In connection with the reorganization of AFG’s Neon Lloyd’s business, in December 2016, AFG undertook a restructuring that included the liquidation for tax purposes of the foreign subsidiary that is the parent of the Neon Lloyd’s operations, resulting in a taxable loss on the liquidation on which AFG reported a \$111 million tax benefit in the fourth quarter of 2016. An additional loss associated with the 2016 restructuring was deferred under U.S. tax laws, resulting in an unrecognized potential tax benefit of \$48 million at December 31, 2016. On December 29, 2017, AFG entered into agreements under which certain Neon executives acquired an indirect noncontrolling interest in Neon. The sale of the noncontrolling interest in Neon resulted in the recognition for U.S. tax purposes of the loss deferred from the 2016 restructuring. AFG recorded a tax benefit of \$56 million in the fourth quarter of 2017 related to the sale of the noncontrolling interest in Neon and the recognition of the previously deferred loss. See Note L — “Income Taxes” to the financial statements.

The Tax Cuts and Jobs Act of 2017 (“TCJA”), which lowered the U.S. corporate tax rate to 21% and made other widespread changes to the U.S. tax code beginning in 2018, was enacted on December 22, 2017. Because the TCJA was enacted in December 2017, AFG recorded the \$83 million decrease in its net deferred tax asset resulting from the changes in the tax code (primarily the lower corporate tax rate applicable to 2018 and future years) in the fourth quarter of 2017. See Note L — “Income Taxes” to the financial statements. Although accounting for the TCJA reduced AFG’s net deferred tax asset, AFG’s effective tax rate and net earnings attributable to shareholders for the full-year 2018 were favorably impacted by the lower corporate income tax rate.

Excluding the tax benefits related to the Neon restructuring and the impact of the change in the U.S. corporate tax rate, AFG’s effective tax rate was 28% for the three months ended December 31, 2017.

Consolidated Noncontrolling Interests AFG’s consolidated net earnings (losses) attributable to noncontrolling interests was a net loss of \$6 million for the fourth quarter of 2018 related to losses at Neon, AFG’s United Kingdom-based Lloyd’s insurer, compared to earnings of less than \$1 million for the fourth quarter of 2017.

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RESULTS OF OPERATIONS — YEARS ENDED DECEMBER 31, 2018, 2017 AND 2016

Segmented Statement of Earnings AFG reports its business as three segments: (i) Property and casualty insurance (“P&C”), (ii) Annuity and (iii) Other, which includes run-off long-term care and life, holding company costs and income and expenses related to the managed investment entities (“MIEs”).

Effective January 1, 2018, the results of AFG’s run-off long-term care and life businesses are included in the “Other” segment instead of as a separate reportable segment based on the immaterial size of the remaining operations. Prior periods amounts were reclassified for consistent presentation.

AFG’s net earnings attributable to shareholders, determined in accordance with GAAP, include certain items that may not be indicative of its ongoing core operations. The following tables for the years ended December 31, 2018, 2017 and 2016 identify such items by segment and reconcile net earnings attributable to shareholders to core net operating earnings, a non-GAAP financial measure that AFG believes is a useful tool for investors and analysts in analyzing ongoing operating trends (in millions):

| | P&C | Annuity | Other Holding Company, Consolidated, and other MIEs and unallocated | Total | Non-core reclass | GAAP Total |
|--|---------|---------|---|---------|---------------------|---------------|
| Year ended December 31, 2018 | | | | | | |
| Revenues: | | | | | | |
| Property and casualty insurance net earned premiums | \$4,865 | \$ — | \$ — | \$4,865 | \$ — | \$4,865 |
| Life, accident and health net earned premiums | — | — | 24 | 24 | — | 24 |
| Net investment income | 438 | 1,638 | (7) 25 | 2,094 | — | 2,094 |
| Realized losses on securities | — | — | — | — | (266) | (266) |
| Income (loss) of MIEs: | | | | | | |
| Investment income | — | — | 255 | 255 | — | 255 |
| Gain (loss) on change in fair value of assets/liabilities | — | — | (21) | (21) | — | (21) |
| Other income | 10 | 107 | (16) 98 | 199 | — | 199 |
| Total revenues | 5,313 | 1,745 | 211 | 7,416 | (266) | 7,150 |
| Costs and Expenses: | | | | | | |
| Property and casualty insurance: | | | | | | |
| Losses and loss adjustment expenses | 2,985 | — | — | 2,985 | 18 | 3,003 |
| Commissions and other underwriting expenses | 1,560 | — | 23 | 1,583 | — | 1,583 |
| Annuity benefits | — | 998 | — | 998 | — | 998 |
| Life, accident and health benefits | — | — | 40 | 40 | — | 40 |
| Annuity and supplemental insurance acquisition expenses | — | 255 | 6 | 261 | — | 261 |
| Interest charges on borrowed money | — | — | 62 | 62 | — | 62 |
| Expenses of MIEs | — | — | 211 | 211 | — | 211 |
| Other expenses | 41 | 131 | 172 | 344 | 9 | 353 |
| Total costs and expenses | 4,586 | 1,384 | 211 | 6,484 | 27 | 6,511 |
| Earnings before income taxes | 727 | 361 | (156) | 932 | (293) | 639 |
| Provision for income taxes | 149 | 70 | (35) | 184 | (62) | 122 |
| Net earnings, including noncontrolling interests | 578 | 291 | (121) | 748 | (231) | 517 |
| Less: Net earnings (losses) attributable to noncontrolling interests | (13) | — | — | (13) | — | (13) |
| Core Net Operating Earnings | 591 | 291 | (121) | 761 | — | 761 |
| Non-core earnings attributable to shareholders (a): | | | | | | |
| Realized losses on securities, net of tax | — | — | (210) | (210) | 210 | — |

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| | | | | | | | |
|---|-------|--------|-----|----------|-------|----|---------|
| Special A&E charges, net of tax | (14) | — | — | (7) | (21) | 21 | — |
| Net Earnings Attributable to Shareholders | \$577 | \$ 291 | \$— | \$(338) | \$530 | \$ | — \$530 |

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| | P&C | Annuity | Other Holding Company MIEs and unallocated | Total | Non-core reclass | GAAP Total |
|---|---------|---------|---|---------|---------------------|---------------|
| Year ended December 31, 2017 | | | | | | |
| Revenues: | | | | | | |
| Property and casualty insurance net earned premiums | \$4,579 | \$ — | \$—\$ — | \$4,579 | \$ — | \$4,579 |
| Life, accident and health net earned premiums | — | — | — 22 | 22 | — | 22 |
| Net investment income | 362 | 1,458 | (2) 34 | 1,831 | — | 1,831 |
| Realized gains on securities | — | — | — — | — | 5 | 5 |
| Income of MIEs: | | | | | | |
| Investment income | — | — | 210— | 210 | — | 210 |
| Gain on change in fair value of assets/liabilities | — | — | 12 — | 12 | — | 12 |
| Other income | 28 | 103 | (1) 93 | 206 | — | 206 |
| Total revenues | 4,969 | 1,561 | 181149 | 6,860 | 5 | 6,865 |
| Costs and Expenses: | | | | | | |
| Property and casualty insurance: | | | | | | |
| Losses and loss adjustment expenses | 2,884 | — | — — | 2,884 | 71 | 2,955 |
| Commissions and other underwriting expenses | 1,382 | — | — 25 | 1,407 | — | 1,407 |
| Annuity benefits | — | 892 | — — | 892 | — | 892 |
| Life, accident and health benefits | — | — | — 26 | 26 | — | 26 |
| Annuity and supplemental insurance acquisition expenses | — | 168 | — 5 | 173 | — | 173 |
| Interest charges on borrowed money | — | — | — 85 | 85 | — | 85 |
| Expenses of MIEs | — | — | 181— | 181 | — | 181 |
| Other expenses | 41 | 121 | — 185 | 347 | 75 | 422 |
| Total costs and expenses | 4,307 | 1,181 | 181326 | 5,995 | 146 | 6,141 |
| Earnings before income taxes | 662 | 380 | — (177) | 865 | (141) | 724 |
| Provision for income taxes | 219 | 128 | — (72) | 275 | (28) | 247 |
| Net earnings, including noncontrolling interests | 443 | 252 | — (105) | 590 | (113) | 477 |
| Less: Net earnings attributable to noncontrolling interests | 2 | — | — — | 2 | — | 2 |
| Core Net Operating Earnings | 441 | 252 | — (105) | 588 | | |
| Non-core earnings attributable to shareholders (a): | | | | | | |
| Realized gains on securities, net of tax | — | — | — 3 | 3 | (3) | — |
| Special A&E charges, net of tax | (58) | — | — (16) | (74) | 74 | — |
| Neon exited lines charge | 18 | — | — — | 18 | (18) | — |
| Loss on retirement of debt, net of tax | — | — | — (33) | (33) | 33 | — |
| Tax benefit related to Neon restructuring | 56 | — | — — | 56 | (56) | — |
| Tax expense related to change in U.S. corporate tax rate | (88) | 25 | — (20) | (83) | 83 | — |
| Net Earnings Attributable to Shareholders | \$369 | \$ 277 | \$—\$ (171) | \$475 | \$ — | \$475 |

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| | P&C | Annuity | Other Holding Co. Consol' other MIEs and unallocated | Total | Non-core reclass | GAAP Total |
|---|---------|---------|---|---------|---------------------|---------------|
| Year ended December 31, 2016 | | | | | | |
| Revenues: | | | | | | |
| Property and casualty insurance net earned premiums | \$4,328 | \$ — | \$ — | \$4,328 | \$ — | \$4,328 |
| Life, accident and health net earned premiums | — | — | 24 | 24 | — | 24 |
| Net investment income | 350 | 1,356 | (37) | 1,696 | — | 1,696 |
| Realized gains on: | | | | | | |
| Securities | — | — | — | — | 19 | 19 |
| Subsidiaries | — | — | — | — | 2 | 2 |
| Income of MIEs: | | | | | | |
| Investment income | — | — | 190 | 190 | — | 190 |
| Gain on change in fair value of assets/liabilities | — | — | 15 | 15 | — | 15 |
| Other income | 19 | 103 | (17) | 192 | 32 | 224 |
| Total revenues | 4,697 | 1,459 | 151 | 6,445 | 53 | 6,498 |
| Costs and Expenses: | | | | | | |
| Property and casualty insurance: | | | | | | |
| Losses and loss adjustment expenses | 2,669 | — | — | 2,669 | 93 | 2,762 |
| Commissions and other underwriting expenses | 1,322 | — | 19 | 1,341 | 8 | 1,349 |
| Annuity benefits | — | 800 | — | 800 | — | 800 |
| Life, accident and health benefits | — | — | 33 | 33 | — | 33 |
| Annuity and supplemental insurance acquisition expenses | — | 181 | 5 | 186 | — | 186 |
| Interest charges on borrowed money | — | — | 77 | 77 | — | 77 |
| Expenses of MIEs | — | — | 151 | 151 | — | 151 |
| Other expenses | 60 | 110 | 178 | 348 | 5 | 353 |
| Total costs and expenses | 4,051 | 1,091 | 151 | 5,605 | 106 | 5,711 |
| Earnings before income taxes | 646 | 368 | (174) | 840 | (53) | 787 |
| Provision for income taxes | 229 | 127 | (66) | 290 | (17) | 119 |
| Net earnings, including noncontrolling interests | 417 | 241 | (108) | 550 | 118 | 668 |
| Less: Net earnings attributable to noncontrolling interests | 16 | — | — | 16 | 3 | 19 |
| Core Net Operating Earnings | 401 | 241 | (108) | 534 | | |
| Non-core earnings attributable to shareholders (a): | | | | | | |
| Realized gains on securities, net of tax and noncontrolling interests | — | — | 13 | 13 | (13) | — |
| Realized gain on subsidiaries, net of tax | — | — | 1 | 1 | (1) | — |
| Gain on sale of apartment property, net of tax and noncontrolling interests | 15 | — | — | 15 | (15) | — |
| Special A&E charges, net of tax | (23) | — | (3) | (26) | 26 | — |
| Neon exited lines charge | (65) | — | — | (65) | 65 | — |
| Tax benefit related to Neon restructuring | 111 | — | — | 111 | (11) | — |
| Tax benefit related to National Interstate merger | 66 | — | — | 66 | (66) | — |
| Net Earnings Attributable to Shareholders | \$505 | \$ 241 | \$— | \$ 97 | \$ — | \$649 |

(a)

See the reconciliation of core earnings to GAAP net earnings under “Results of Operations — General” for details on the tax and noncontrolling interest impacts of these reconciling items.

Property and Casualty Insurance Segment — Results of Operations AFG’s property and casualty insurance operations contributed \$709 million in GAAP pretax earnings in 2018 compared to \$591 million in 2017, an increase of \$118 million (20%). Property and casualty core pretax earnings were \$727 million in 2018 compared to \$662 million in 2017, an increase of \$65 million (10%). The increase in GAAP and core pretax earnings reflects higher underwriting profit in 2018 compared to 2017 due primarily to higher favorable prior year reserve development and lower catastrophe losses, higher net investment income, due primarily to higher earnings from limited partnerships and similar investments and growth in the business, partially offset by the impact of income from the sale of real estate in 2017. The high returns on limited partnerships and similar

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investments should not be expected to repeat in future periods. The increase in GAAP pretax earnings also reflects lower special A&E charges in 2018 compared to 2017, partially offset by the impact of favorable reserve development of \$18 million in the fourth quarter of 2017 in the Neon exited lines in connection with a reinsurance to close transaction.

AFG's property and casualty insurance operations contributed \$591 million in GAAP pretax earnings in 2017 compared to \$577 million in 2016, an increase of \$14 million (2%). Property and casualty core pretax earnings were \$662 million in 2017 compared to \$646 million in 2016, an increase of \$16 million (2%). The increase in GAAP and core pretax earnings reflects higher underwriting profit in the Specialty casualty sub-segment, higher net investment income and lower other expenses, partially offset by lower underwriting profits in the Property and transportation and Specialty financial sub-segments. The increase in GAAP pretax earnings also reflects the impact of a pretax non-core charge of \$65 million in the second quarter of 2016 related to the exit of certain lines of business within Neon and favorable development of \$18 million in the fourth quarter of 2017 in the Neon exited lines in connection with a reinsurance to close transaction, partially offset by the impact of a \$32 million pretax non-core gain on the sale of an apartment property in the second quarter of 2016 and special A&E charges of \$89 million in 2017 compared to \$36 million in 2016.

The following table details AFG's GAAP and core earnings before income taxes from its property and casualty insurance operations for the years ended December 31, 2018, 2017 and 2016 (dollars in millions):

| | Year ended December 31, | | | % Change | |
|---|-------------------------|----------|----------|-------------|-------------|
| | 2018 | 2017 | 2016 | 2018 - 2017 | 2017 - 2016 |
| Gross written premiums | \$6,840 | \$6,502 | \$5,981 | 5 % | 9 % |
| Reinsurance premiums ceded | (1,817) | (1,751) | (1,595) | 4 % | 10 % |
| Net written premiums | 5,023 | 4,751 | 4,386 | 6 % | 8 % |
| Change in unearned premiums | (158) | (172) | (58) | (8 %) | 197 % |
| Net earned premiums | 4,865 | 4,579 | 4,328 | 6 % | 6 % |
| Loss and loss adjustment expenses (a) | 2,985 | 2,884 | 2,669 | 4 % | 8 % |
| Commissions and other underwriting expenses (b) | 1,560 | 1,382 | 1,322 | 13 % | 5 % |
| Core underwriting gain | 320 | 313 | 337 | 2 % | (7 %) |
| Net investment income | 438 | 362 | 350 | 21 % | 3 % |
| Other income and expenses, net (c) | (31) | (13) | (41) | 138 % | (68 %) |
| Core earnings before income taxes | 727 | 662 | 646 | 10 % | 2 % |
| Pretax non-core special A&E charges | (18) | (89) | (36) | (80 %) | 147 % |
| Pretax non-core Neon exited lines charge | — | 18 | (65) | (100%) | (128%) |
| Pretax non-core gain on sale of an apartment property | — | — | 32 | — % | (100%) |
| GAAP earnings before income taxes | \$709 | \$591 | \$577 | 20 % | 2 % |

(a) Excludes pretax non-core special A&E charges of \$18 million, \$89 million and \$36 million in 2018, 2017 and 2016, respectively, a non-core charge of \$57 million related to the exit of certain lines of business within Neon in 2016 and income of \$18 million in 2017 representing favorable development related to the Neon exited lines in connection with a reinsurance to close transaction.

(b) Excludes a non-core charge of \$8 million related to the exit of certain lines of business within Neon in 2016.

(c) Excludes a pretax non-core gain of \$32 million on the sale of an apartment property in 2016.

Change
2018 - 2017 -
2017 2016

Combined Ratios:

Specialty lines

| | | | | | | | | | |
|----------------------------|------|---|------|---|------|---|---------|---------|---|
| Loss and LAE ratio | 61.3 | % | 62.9 | % | 61.7 | % | (1.6 %) | 1.2 | % |
| Underwriting expense ratio | 32.1 | % | 30.2 | % | 30.6 | % | 1.9 % | (0.4 %) | |
| Combined ratio | 93.4 | % | 93.1 | % | 92.3 | % | 0.3 % | 0.8 | % |

Aggregate — including exited lines

| | | | | | | | | | |
|----------------------------|------|---|------|---|------|---|---------|---------|---|
| Loss and LAE ratio | 61.7 | % | 64.5 | % | 63.8 | % | (2.8 %) | 0.7 | % |
| Underwriting expense ratio | 32.1 | % | 30.2 | % | 30.7 | % | 1.9 % | (0.5 %) | |
| Combined ratio | 93.8 | % | 94.7 | % | 94.5 | % | (0.9 %) | 0.2 | % |

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AFG reports the underwriting performance of its Specialty property and casualty insurance business in the following sub-segments: (i) Property and transportation, (ii) Specialty casualty and (iii) Specialty financial.

Gross Written Premiums

Gross written premiums (“GWP”) for AFG’s property and casualty insurance segment were \$6.84 billion in 2018 compared to \$6.50 billion in 2017, an increase of \$338 million (5%). GWP increased \$521 million (9%) in 2017 compared to 2016. Detail of AFG’s property and casualty gross written premiums is shown below (dollars in millions):

| | Year ended December 31, | | | | | | % Change | |
|-----------------------------|-------------------------|------|---------|------|---------|------|----------|------|
| | 2018 | | 2017 | | 2016 | | 2018 | 2017 |
| | GWP | % | GWP | % | GWP | % | 2017 | 2016 |
| Property and transportation | \$2,645 | 39 % | \$2,688 | 41 % | \$2,504 | 42 % | (2 %) | 7 % |
| Specialty casualty | 3,445 | 50 % | 3,087 | 48 % | 2,792 | 47 % | 12 % | 11 % |
| Specialty financial | 750 | 11 % | 727 | 11 % | 685 | 11 % | 3 % | 6 % |
| | \$6,840 | 100% | \$6,502 | 100% | \$5,981 | 100% | 5 % | 9 % |

Reinsurance Premiums Ceded

Reinsurance premiums ceded (“Ceded”) for AFG’s property and casualty insurance segment were 27% of gross written premiums for each of the years ended December 31, 2018, 2017 and 2016. Detail of AFG’s property and casualty reinsurance premiums ceded is shown below (dollars in millions):

| | Year ended December 31, | | | | | | Change in | |
|-----------------------------|-------------------------|----------|-----------|----------|-----------|----------|-----------|-------|
| | 2018 | | 2017 | | 2016 | | 2018 | 2017 |
| | Ceded | % of GWP | Ceded | % of GWP | Ceded | % of GWP | 2017 | 2016 |
| Property and transportation | \$(891) | 34 % | \$(923) | 34 % | \$(832) | 33 % | —% | 1 % |
| Specialty casualty | (936) | 27 % | (807) | 26 % | (756) | 27 % | 1 % | (1 %) |
| Specialty financial | (148) | 20 % | (131) | 18 % | (113) | 16 % | 2 % | 2 % |
| Other specialty | 158 | | 110 | | 106 | | | |
| | \$(1,817) | 27 % | \$(1,751) | 27 % | \$(1,595) | 27 % | —% | —% |

Net Written Premiums

Net written premiums (“NWP”) for AFG’s property and casualty insurance segment were \$5.02 billion in 2018 compared to \$4.75 billion in 2017, an increase of \$272 million (6%). NWP increased \$365 million (8%) in 2017 compared to 2016. Detail of AFG’s property and casualty net written premiums is shown below (dollars in millions):

| | Year ended December 31, | | | | | | % Change | |
|-----------------------------|-------------------------|------|---------|------|---------|------|----------|------|
| | 2018 | | 2017 | | 2016 | | 2018 | 2017 |
| | NWP | % | NWP | % | NWP | % | 2017 | 2016 |
| Property and transportation | \$1,754 | 35 % | \$1,765 | 37 % | \$1,672 | 38 % | (1 %) | 6 % |
| Specialty casualty | 2,509 | 50 % | 2,280 | 48 % | 2,036 | 46 % | 10 % | 12 % |
| Specialty financial | 602 | 12 % | 596 | 13 % | 572 | 13 % | 1 % | 4 % |
| Other specialty | 158 | 3 % | 110 | 2 % | 106 | 3 % | 44 % | 4 % |
| | \$5,023 | 100% | \$4,751 | 100% | \$4,386 | 100% | 6 % | 8 % |

Net Earned Premiums

Net earned premiums (“NEP”) for AFG’s property and casualty insurance segment were \$4.87 billion in 2018 compared to \$4.58 billion in 2017, an increase of \$286 million (6%). NEP increased \$251 million (6%) in 2017 compared to 2016. Detail of AFG’s property and casualty net earned premiums is shown below (dollars in millions):

| | Year ended December 31, | | | | | | % Change | |
|-----------------------------|-------------------------|------|---------|------|---------|------|----------|------|
| | 2018 | | 2017 | | 2016 | | 2018 | 2017 |
| | NEP | % | NEP | % | NEP | % | 2017 | 2016 |
| Property and transportation | \$1,729 | 36 % | \$1,711 | 37 % | \$1,662 | 38 % | 1 % | 3 % |
| Specialty casualty | 2,403 | 49 % | 2,186 | 48 % | 2,006 | 46 % | 10 % | 9 % |
| Specialty financial | 598 | 12 % | 576 | 13 % | 557 | 13 % | 4 % | 3 % |
| Other specialty | 135 | 3 % | 106 | 2 % | 103 | 3 % | 27 % | 3 % |
| | \$4,865 | 100% | \$4,579 | 100% | \$4,328 | 100% | 6 % | 6 % |

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The \$338 million (5%) increase in gross written premiums in 2018 compared to 2017 reflects growth in the Specialty casualty and Specialty financial sub-segments. Overall average renewal rates increased approximately 1% in 2018. Excluding the workers' compensation business, renewal pricing increased approximately 3%.

The \$521 million (9%) increase in gross written premiums in 2017 compared to 2016 reflects growth in each of the Specialty property and casualty sub-segments. Overall average renewal rates increased approximately 1% in 2017.

Property and transportation Gross written premiums decreased \$43 million (2%) in 2018 compared to 2017. This decrease was largely the result of lower year-over-year premiums in the crop insurance business and underwriting actions on under-performing accounts in the Singapore branch. Average renewal rates increased approximately 3% for this group in 2018. Reinsurance premiums ceded as a percentage of gross written premiums were comparable in 2018 and 2017.

Gross written premiums increased \$184 million (7%) in 2017 compared to 2016. This increase was the result of higher gross written premiums in the crop, transportation and property and inland marine businesses, and the Singapore branch. This growth was partially offset by lower premiums resulting from an exit from the customs bond business, which was part of the ocean marine operations. Average renewal rates increased approximately 3% for this group in 2017. Reinsurance premiums ceded as a percentage of gross written premiums increased 1 percentage point in 2017 compared to 2016, reflecting a change in the mix of business and the impact of reinstatement premiums in 2017 resulting from reinsured hurricane losses.

Specialty casualty Gross written premiums increased \$358 million (12%) in 2018 compared to 2017 due primarily to growth at Neon. Higher gross written premiums in the excess and surplus, targeted markets and executive liability businesses also contributed to the year-over-year growth. Average renewal rates decreased approximately 1% for this group in 2018. Excluding the workers' compensation businesses, renewal rates for this group increased approximately 3% in 2018. Reinsurance premiums ceded as a percentage of gross written premiums increased 1 percentage point in 2018 compared to 2017, reflecting higher cessions to AFG's internal reinsurance program, which is included in Other specialty and higher cessions in the workers' compensation businesses.

Gross written premiums increased \$295 million (11%) in 2017 compared to 2016. New accounts written in the targeted markets businesses and higher gross written premiums at Neon, resulting from the growth of its portfolio in targeted classes of business were the primary drivers of the increase. Additionally, higher gross written premiums in the workers' compensation businesses, primarily the result of rate increases in the state of Florida, coupled with growth in the executive liability and excess and surplus businesses contributed to the growth in gross written premiums in 2017. Average renewal rates were flat for this group in 2017. Reinsurance premiums ceded as a percentage of gross written premiums decreased 1 percentage point in 2017 compared to 2016, reflecting a change in the mix of business.

Specialty financial Gross written premiums increased \$23 million (3%) in 2018 compared to 2017 due primarily to higher premiums in the financial institutions business. Average renewal rates for this group increased approximately 5% in 2018. Reinsurance premiums ceded as a percentage of gross written premiums increased 2 percentage points in 2018 compared to 2017, reflecting higher cessions in the financial institutions and equipment leasing businesses and the impact of a reinstatement premium in 2018 related to a reinsured loss in the fidelity business.

Gross written premiums increased \$42 million (6%) in 2017 compared to 2016 due primarily to higher premiums in the lending and leasing, fidelity and surety businesses. Average renewal rates for this group decreased approximately 2% in 2017. Reinsurance premiums ceded as a percentage of gross written premiums increased 2 percentage points in 2017 compared to 2016, reflecting higher cessions in the lending and leasing businesses.

Other specialty The amounts shown as reinsurance premiums ceded represent business assumed by AFG's internal reinsurance program from the operations that make up AFG's other Specialty property and casualty insurance sub-segments. Reinsurance premiums assumed increased \$48 million (44%) in 2018 compared to 2017, reflecting an increase in premiums retained, primarily from businesses in the Specialty casualty sub-segment.

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Combined Ratio

The table below (dollars in millions) details the components of the combined ratio for AFG's property and casualty insurance segment for 2018, 2017 and 2016:

| | Year ended December 31, | | | Change | | Year ended December 31, | | |
|---|-------------------------|-------|-------|-------------|-------------|-------------------------|-------|-------|
| | 2018 | 2017 | 2016 | 2018 - 2017 | 2017 - 2016 | 2018 | 2017 | 2016 |
| Property and transportation | | | | | | | | |
| Loss and LAE ratio | 69.0% | 68.5% | 67.0% | 0.5 % | 1.5 % | | | |
| Underwriting expense ratio | 24.1% | 22.5% | 23.0% | 1.6 % | (0.5%) | | | |
| Combined ratio | 93.1% | 91.0% | 90.0% | 2.1 % | 1.0 % | | | |
| Underwriting profit | | | | | | \$120 | \$154 | \$166 |
| Specialty casualty | | | | | | | | |
| Loss and LAE ratio | 61.5% | 64.5% | 65.8% | (3.0%) | (1.3%) | | | |
| Underwriting expense ratio | 32.7% | 30.7% | 30.3% | 2.0 % | 0.4 % | | | |
| Combined ratio | 94.2% | 95.2% | 96.1% | (1.0%) | (0.9%) | | | |
| Underwriting profit | | | | | | \$141 | \$104 | \$78 |
| Specialty financial | | | | | | | | |
| Loss and LAE ratio | 37.6% | 39.4% | 32.0% | (1.8%) | 7.4 % | | | |
| Underwriting expense ratio | 51.3% | 50.0% | 52.9% | 1.3 % | (2.9%) | | | |
| Combined ratio | 88.9% | 89.4% | 84.9% | (0.5%) | 4.5 % | | | |
| Underwriting profit | | | | | | \$66 | \$61 | \$84 |
| Total Specialty | | | | | | | | |
| Loss and LAE ratio | 61.3% | 62.9% | 61.7% | (1.6%) | 1.2 % | | | |
| Underwriting expense ratio | 32.1% | 30.2% | 30.6% | 1.9 % | (0.4%) | | | |
| Combined ratio | 93.4% | 93.1% | 92.3% | 0.3 % | 0.8 % | | | |
| Underwriting profit | | | | | | \$322 | \$317 | \$337 |
| Aggregate — including exited lines | | | | | | | | |
| Loss and LAE ratio | 61.7% | 64.5% | 63.8% | (2.8%) | 0.7 % | | | |
| Underwriting expense ratio | 32.1% | 30.2% | 30.7% | 1.9 % | (0.5%) | | | |
| Combined ratio | 93.8% | 94.7% | 94.5% | (0.9%) | 0.2 % | | | |
| Underwriting profit | | | | | | \$302 | \$242 | \$236 |

The Specialty property and casualty insurance operations generated an underwriting profit of \$322 million in 2018 compared to \$317 million in 2017, an increase of \$5 million (2%). Higher underwriting profits in the Specialty casualty and Specialty financial sub-segments were partially offset by lower underwriting profit in the Property and transportation sub-segment. Overall catastrophe losses were \$103 million (2.1 points on the combined ratio) for 2018 compared to \$140 million (3.0 points) for 2017. In connection with catastrophe losses incurred in 2018, AFG paid \$2 million in net reinstatement premiums, resulting in a total pretax loss from catastrophes of \$105 million. In connection with catastrophe losses incurred in 2017, AFG reduced profit-based commissions payable to agents by \$8 million in the Specialty financial sub-segment and paid \$10 million in net reinstatement premiums, resulting in a total pretax loss from catastrophes of \$142 million in 2017.

The Specialty property and casualty insurance operations generated an underwriting profit of \$317 million in 2017 compared to \$337 million in 2016, a decrease of \$20 million (6%). The lower underwriting profit in 2017 as compared

to 2016 reflects lower underwriting profits in the Property and transportation and Specialty financial insurance sub-segments, partially offset by higher underwriting profit in the Specialty casualty insurance sub-segment. Results for each of the Specialty property and casualty insurance sub-segments reflect higher catastrophe losses in 2017 compared to 2016. Overall catastrophe losses were \$140 million (3.0 points on the combined ratio) for 2017 compared to \$55 million (1.3 points) for 2016. In connection with catastrophe losses incurred in 2017, AFG reduced profit-based commissions payable to agents by \$8 million in the Specialty financial sub-segment and paid \$10 million in net reinstatement premiums, resulting in a total pretax loss from catastrophes of \$142 million in 2017.

Property and transportation Underwriting profit for this group was \$120 million in 2018 compared to \$154 million in 2017, a decrease of \$34 million (22%). Lower underwriting profits in the agricultural, property and inland marine and aviation businesses and the Singapore branch were partially offset by higher underwriting profit at National Interstate and improved

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results in the ocean marine operations. Catastrophe losses were \$26 million (1.5 points on the combined ratio) in 2018 compared to catastrophe losses of \$36 million (2.1 points) and related reinstatement premiums of \$2 million in 2017.

Underwriting profit for this group was \$154 million in 2017 compared to \$166 million in 2016, a decrease of \$12 million (7%). Lower underwriting profits in the crop and ocean marine businesses were the primary drivers of these lower results, partially offset by higher underwriting profit in the transportation businesses. The crop insurance operations reported strong underwriting profitability in 2017, albeit at lower levels than in 2016. Catastrophe losses were \$36 million (2.1 points on the combined ratio) and related reinstatement premiums were \$2 million in 2017 compared to catastrophe losses of \$31 million (1.9 points) in 2016.

Specialty casualty Underwriting profit for this group was \$141 million in 2018 compared to \$104 million in 2017, an increase of \$37 million (36%). These results reflect higher underwriting profits in the executive liability and targeted markets businesses and lower adverse prior year reserve development in run-off businesses. Catastrophe losses were \$45 million (1.9 points on the combined ratio) and related net reinstatement premiums were \$1 million in 2018 compared to catastrophe losses of \$71 million (3.3 points) and related net reinstatement premiums of \$6 million in 2017.

Underwriting profit for this group was \$104 million in 2017 compared to \$78 million in 2016, an increase of \$26 million (33%), reflecting favorable reserve development within Neon, including the portion of the 2015 and prior years reinsurance to close transaction attributed to ongoing lines of business, and higher underwriting profits in the excess and surplus lines and workers' compensation businesses. These improved results were partially offset by lower underwriting profit in the executive liability business, due primarily to lower favorable prior year reserve development, adverse prior year reserve development in the targeted markets operations and higher catastrophe losses. Catastrophe losses were \$71 million (3.3 points on the combined ratio) and related net reinstatement premiums were \$6 million in 2017 compared to catastrophe losses of \$10 million (0.5 points) in 2016.

Specialty financial Underwriting profit for this group was \$66 million in 2018 compared to \$61 million in 2017, an increase of \$5 million (8%) due primarily to favorable prior year reserve development in run-off businesses. Catastrophe losses were \$28 million (4.7 points on the combined ratio) in 2018 compared to \$30 million (5.2 points) in 2017. In connection with catastrophe losses incurred in 2018, the Specialty financial sub-segment paid \$1 million in reinstatement premiums compared to a reduction of profit-based commissions payable to agents of \$8 million (1.1 points on the combined ratio) and reinstatement premiums of \$2 million in 2017.

Underwriting profit for this group was \$61 million in 2017 compared to \$84 million in 2016, a decrease of \$23 million (27%), reflecting lower underwriting profitability in the financial institutions business due primarily to higher catastrophe losses and adverse prior year reserve development. Catastrophe losses were \$30 million (5.2 points on the combined ratio) in 2017 compared to \$11 million (2.0 points) in 2016. In connection with catastrophe losses incurred in 2017, the Specialty financial sub-segment reduced profit-based commissions payable to agents by \$8 million (1.1 points on the combined ratio) and paid \$2 million in reinstatement premiums.

Other specialty This group reported an underwriting loss of \$5 million in 2018 compared to \$2 million in 2017, an increase of \$3 million (150%). The lower results are due primarily to losses in the business assumed by AFG's internal reinsurance program from the operations that make up AFG's other Specialty sub-segments in 2018, partially offset by the impact of a \$14 million charge recorded in 2017 to adjust the deferred gain on the retroactive reinsurance transaction entered into in connection with the sale of businesses in 1998.

This group reported an underwriting loss of \$2 million in 2017 compared to an underwriting profit of \$9 million in 2016, a decrease of \$11 million (122%). The decrease is due primarily to the \$14 million charge to adjust the deferred gain on the retroactive reinsurance transaction entered into in connection with the sale of businesses in 1998.

Aggregate Aggregate underwriting results for AFG's property and casualty insurance segment include the asbestos and environmental reserve charges and the Neon exited lines charge and favorable development in the Neon exited lines discussed below under "Net prior year reserve development."

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Losses and Loss Adjustment Expenses

AFG's overall loss and LAE ratio was 61.7%, 64.5% and 63.8% in 2018, 2017 and 2016, respectively. The components of AFG's property and casualty losses and LAE amounts and ratio are detailed below (dollars in millions):

| | Year ended December 31, | | | | | | Change in | |
|--|-------------------------|---------|---------|---------|---------|---------|-------------|-------------|
| | Amount | | | Ratio | | | Ratio | |
| | 2018 | 2017 | 2016 | 2018 | 2017 | 2016 | 2018 - 2017 | 2017 - 2016 |
| Property and transportation | | | | | | | | |
| Current year, excluding catastrophe losses | \$1,216 | \$1,176 | \$1,104 | 70.3% | 68.7% | 66.3% | 1.6 % | 2.4 % |
| Prior accident years development | (50) | (40) | (21) | (2.8 %) | (2.3 %) | (1.2 %) | (0.5 %) | (1.1 %) |
| Current year catastrophe losses | 26 | 36 | 31 | 1.5 % | 2.1 % | 1.9 % | (0.6 %) | 0.2 % |
| Property and transportation losses and LAE and ratio | \$1,192 | \$1,172 | \$1,114 | 69.0% | 68.5% | 67.0% | 0.5 % | 1.5 % |
| Specialty casualty | | | | | | | | |
| Current year, excluding catastrophe losses | \$1,570 | \$1,425 | \$1,323 | 65.4% | 65.2% | 66.0% | 0.2 % | (0.8 %) |
| Prior accident years development | (139) | (86) | (13) | (5.8 %) | (4.0 %) | (0.7 %) | (1.8 %) | (3.3 %) |
| Current year catastrophe losses | 45 | 71 | 10 | 1.9 % | 3.3 % | 0.5 % | (1.4 %) | 2.8 % |
| Specialty casualty losses and LAE and ratio | \$1,476 | \$1,410 | \$1,320 | 61.5% | 64.5% | 65.8% | (3.0 %) | (1.3 %) |
| Specialty financial | | | | | | | | |
| Current year, excluding catastrophe losses | \$223 | \$218 | \$190 | 37.3% | 37.8% | 34.0% | (0.5 %) | 3.8 % |
| Prior accident years development | (26) | (21) | (23) | (4.4 %) | (3.6 %) | (4.0 %) | (0.8 %) | 0.4 % |
| Current year catastrophe losses | 28 | 30 | 11 | 4.7 % | 5.2 % | 2.0 % | (0.5 %) | 3.2 % |
| Specialty financial losses and LAE and ratio | \$225 | \$227 | \$178 | 37.6% | 39.4% | 32.0% | (1.8 %) | 7.4 % |
| Total Specialty | | | | | | | | |
| Current year, excluding catastrophe losses | \$3,092 | \$2,879 | \$2,675 | 63.6% | 62.9% | 61.8% | 0.7 % | 1.1 % |
| Prior accident years development | (212) | (139) | (61) | (4.4 %) | (3.0 %) | (1.4 %) | (1.4 %) | (1.6 %) |
| Current year catastrophe losses | 103 | 140 | 55 | 2.1 % | 3.0 % | 1.3 % | (0.9 %) | 1.7 % |
| Total Specialty losses and LAE and ratio | \$2,983 | \$2,880 | \$2,669 | 61.3% | 62.9% | 61.7% | (1.6 %) | 1.2 % |
| Aggregate — including exited lines | | | | | | | | |
| Current year, excluding catastrophe losses | \$3,092 | \$2,879 | \$2,675 | 63.6% | 62.9% | 61.8% | 0.7 % | 1.1 % |
| Prior accident years development | (192) | (64) | 32 | (4.0 %) | (1.4 %) | 0.7 % | (2.6 %) | (2.1 %) |
| Current year catastrophe losses | 103 | 140 | 55 | 2.1 % | 3.0 % | 1.3 % | (0.9 %) | 1.7 % |
| Aggregate losses and LAE and ratio | \$3,003 | \$2,955 | \$2,762 | 61.7% | 64.5% | 63.8% | (2.8 %) | 0.7 % |

Current accident year losses and LAE, excluding catastrophe losses

The current accident year loss and LAE ratio, excluding catastrophe losses for AFG's Specialty property and casualty insurance operations was 63.6% in 2018, 62.9% in 2017 and 61.8% in 2016.

Property and transportation The 1.6 percentage points increase in the loss and LAE ratio for the current year, excluding catastrophe losses in 2018 compared to 2017 reflects an increase in the loss and LAE ratio of the aviation business and the Singapore branch.

The 2.4 percentage points increase in the loss and LAE ratio for the current year, excluding catastrophe losses in 2017 compared to 2016 reflects an increase in the loss and LAE ratio of the crop and property and inland marine businesses

and the Singapore branch.

Specialty casualty The loss and LAE ratio for the current year, excluding catastrophe losses is comparable in 2018 and 2017.

The 0.8 percentage points improvement in the loss and LAE ratio for the current year, excluding catastrophe losses in 2017 compared to 2016 reflects a decrease in the loss and LAE ratio at Neon.

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Specialty financial The loss and LAE ratio for the current year, excluding catastrophe losses is comparable in 2018 and 2017.

The 3.8 percentage points increase in the loss and LAE ratio for the current year, excluding catastrophe losses in 2017 compared to 2016 reflects an increase in the loss and LAE ratio of the financial institutions business.

Net prior year reserve development

AFG's Specialty property and casualty insurance operations recorded net favorable reserve development related to prior accident years of \$212 million in 2018 compared to \$139 million in 2017 and \$61 million in 2016, an increase of \$73 million (53%) and \$78 million (128%), respectively.

Property and transportation Net favorable reserve development of \$50 million in 2018 reflects lower than expected losses in the crop business and lower than expected claim severity at National Interstate, partially offset by higher than expected claim frequency and severity in the Singapore branch and aviation operations.

Net favorable reserve development of \$40 million in 2017 reflects lower than expected losses in the crop and equine businesses and lower than expected claim severity in the property and inland marine and transportation businesses, partially offset by higher than expected claim frequency and severity in the ocean marine business.

Net favorable reserve development of \$21 million in 2016 reflects lower than expected losses in the crop operations and lower than expected claim severity in the property and inland marine and trucking businesses, partially offset by reserve strengthening at National Interstate and higher than expected claim frequency in the ocean marine business.

Specialty casualty Net favorable reserve development of \$139 million in 2018 reflects lower than anticipated claim severity in the workers' compensation businesses and lower than expected emergence in assumed 2017 property catastrophe losses at Neon, and to a lesser extent, lower than expected claim severity in the executive liability business.

Net favorable reserve development of \$86 million in 2017 includes favorable reserve development on ongoing lines of business within Neon recorded in connection with the reinsurance to close agreement entered into in December 2017 for the 2015 and prior years of account, lower than anticipated claim severity in the workers' compensation businesses and lower than expected losses in the executive liability business, partially offset by higher than anticipated claim severity in the targeted markets and general liability businesses and higher than anticipated severity in New York contractor claims.

In the fourth quarter of 2017, Neon entered into a reinsurance to close agreement for its 2015 and prior years of account, which transfers the responsibility for all of the liabilities that attach to the transferred year of account as well as any income due to the closing year of account in return for a premium. As a result of the reinsurance to close agreement, Neon recorded favorable development of \$42 million, of which \$24 million related to its ongoing lines of business (included in Specialty casualty) and \$18 million related to the exited lines of business (discussed below and included in Neon exited lines charge).

Net favorable reserve development of \$13 million in 2016 reflects lower than anticipated claim frequency and severity in workers' compensation business, lower than expected claim severity in directors and officers liability insurance and lower than expected claim frequency and severity in excess liability business, partially offset by adverse reserve development at Neon, higher than anticipated severity in New York contractor claims, higher than anticipated claim frequency and severity in general liability insurance and higher than expected claim frequency and severity in the targeted markets business.

Specialty financial Net favorable reserve development of \$26 million in 2018 reflects lower than expected claim frequency and severity in the surety business, lower than expected claim severity in the fidelity business and lower than expected claim frequency in run-off businesses.

Net favorable reserve development of \$21 million in 2017 reflects lower than anticipated claim severity in the fidelity business and lower than expected claim frequency and severity in the surety business.

Net favorable reserve development of \$23 million in 2016 reflects lower than anticipated claim severity in the fidelity business, lower than expected claim frequency and severity in the surety business and lower than anticipated claim frequency in the financial institutions business.

Other specialty In addition to the reserve development discussed above, total Specialty prior year reserve development includes net adverse reserve development of \$3 million in 2018, net adverse reserve development of \$8 million in 2017 and net

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favorable reserve development of \$4 million in 2016. The adverse reserve development in 2018 reflects \$10 million of adverse reserve development associated with AFG’s internal reinsurance program, partially offset by amortization of the deferred gains on the retroactive reinsurance transactions entered into in connection with the sale of businesses in 1998 and 2001. The adverse reserve development in 2017 reflects a \$14 million charge to adjust the deferred gain on the retroactive reinsurance transaction entered into in connection with the sale of businesses in 1998, partially offset by the amortization of deferred gains on retroactive reinsurance and favorable reserve development associated with AFG’s internal reinsurance program. Favorable reserve development in 2016 reflects amortization of deferred gains on retroactive reinsurance and reserve development associated with AFG’s internal reinsurance program.

Asbestos and environmental reserve charges As previously discussed under “Uncertainties” — “Asbestos and Environmental-related (“A&E”) Insurance Reserves,” AFG has established property and casualty reserves for claims related to environmental exposures and asbestos claims. Total charges recorded to increase reserves (net of reinsurance recoverable) for A&E exposures of AFG’s property and casualty group (included in loss and loss adjustment expenses) were \$18 million in 2018, \$89 million in 2017 and \$36 million in 2016.

Neon exited lines charge During the second quarter of 2016, AFG’s specialist Lloyd’s market insurer completed a strategic review of its business under a new leadership team and re-launched as Neon Underwriting Ltd. As part of its strategic review, Neon sold and/or exited certain historical lines of business including its UK and international medical malpractice and general liability classes. As a result of Neon’s claims review of its exited lines of business, AFG recorded a charge of approximately \$65 million including \$57 million to increase loss reserves primarily related to its medical malpractice and general liability lines. Consistent with the treatment of other items that are not indicative of AFG’s ongoing operations (both favorable and unfavorable), the 2016 charge was treated as non-core because it resulted from a special strategic review of lines of business that Neon no longer writes. Similarly, the \$18 million in favorable development related to the Neon exited lines recorded in connection with the December 2017 reinsurance to close transaction (discussed above under Specialty casualty) was treated as non-core.

Aggregate Aggregate net prior accident years reserve development for AFG’s property and casualty insurance segment includes the A&E charges, the Neon exited lines charge and the favorable development on the Neon exited lines mentioned above and adverse reserve development of \$2 million in 2018 and \$4 million in 2017 related to business outside the Specialty group that AFG no longer writes.

Catastrophe losses

AFG generally seeks to reduce its exposure to catastrophes through individual risk selection, including minimizing coastal and known fault-line exposures, and the purchase of reinsurance. AFG recorded net catastrophe losses of \$103 million in 2018 primarily from mudslides in California in the first quarter, storms and flooding in several regions of the United States in the second quarter, Hurricane Florence in the third quarter and Hurricane Michael and wildfires in California in the fourth quarter. Catastrophe losses of \$140 million in 2017 resulted primarily from storms and tornadoes in several regions of the United States in the first and second quarters, Hurricanes Harvey, Irma and Maria and earthquakes in Mexico in the third quarter and wildfires in California in the fourth quarter. Catastrophe losses of \$55 million in 2016 resulted primarily from winter storms in the first quarter, storms in Texas in the second quarter, flooding in Louisiana and multiple storms in the southern United States in the third quarter and Hurricane Matthew in the fourth quarter.

Commissions and Other Underwriting Expenses

AFG’s property and casualty commissions and other underwriting expenses (“U/W Exp”) were \$1.56 billion in 2018 compared to \$1.38 billion in 2017, an increase of \$178 million (13%). AFG’s underwriting expense ratio was 32.1% in 2018 compared to 30.2% in 2017, an increase of 1.9 percentage points.

AFG's property and casualty U/W Exp were \$1.38 billion in 2017 compared to \$1.33 billion in 2016, an increase of \$52 million (4%). AFG's underwriting expense ratio was 30.2% in 2017 compared to 30.7% in 2016, a decrease of 0.5 percentage points.

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Detail of AFG's property and casualty commissions and other underwriting expenses and underwriting expense ratios is shown below (dollars in millions):

| | Year ended December 31, | | | | | | Change in % of NEP | |
|-----------------------------|-------------------------|-------------|------------|-------------|------------|-------------|-----------------------|----------------|
| | 2018 | | 2017 | | 2016 | | 2018 - | 2017 - 2016 |
| | U/W Exp | % of NEP | U/W Exp | % of NEP | U/W Exp | % of NEP | | |
| Property and transportation | \$417 | 24.1% | \$385 | 22.5% | \$382 | 23.0% | 1.6% | (0.5%) |
| Specialty casualty | 786 | 32.7% | 672 | 30.7% | 608 | 30.3% | 2.0% | 0.4% |
| Specialty financial | 307 | 51.3% | 288 | 50.0% | 295 | 52.9% | 1.3% | (2.9%) |
| Other specialty | 50 | 37.3% | 37 | 35.8% | 37 | 36.5% | 1.5% | (0.7%) |
| Total Specialty | 1,560 | 32.1% | 1,382 | 30.2% | 1,322 | 30.6% | 1.9% | (0.4%) |
| Neon exited lines charge | — | | — | | 8 | | | |
| Total Aggregate | \$1,560 | 32.1% | \$1,382 | 30.2% | \$1,330 | 30.7% | 1.9% | (0.5%) |

AFG's overall expense ratio increased 1.9% in 2018 as compared to 2017 and decreased 0.5% in 2017 compared to 2016.

Property and transportation Commissions and other underwriting expenses as a percentage of net earned premiums increased 1.6 percentage points in 2018 compared to 2017 reflecting lower premiums in the crop business, which has a lower expense ratio than AFG's overall Property and transportation group and an increase in the expense ratio in the transportation businesses.

Commissions and other underwriting expenses as a percentage of net earned premiums decreased 0.5 percentage points in 2017 compared to 2016 reflecting the impact of higher crop premiums on the ratio.

Specialty casualty Commissions and other underwriting expenses as a percentage of net earned premiums increased 2.0 percentage points in 2018 compared to 2017 reflecting growth at Neon, which has a higher expense ratio than AFG's overall Specialty casualty group, higher dividends paid to policyholders in the workers' compensation businesses and lower underwriting, policy administration and claims services fees collected from unaffiliated insurers in the workers' compensation businesses.

Commissions and other underwriting expenses as a percentage of net earned premiums increased 0.4 percentage points in 2017 compared to 2016 reflecting the impact of reinstatement premiums on the ratio.

Specialty financial Commissions and other underwriting expenses as a percentage of net earned premiums increased 1.3 percentage points in 2018 compared to 2017 reflecting higher profitability-based commissions paid to agents in the financial institutions business compared to 2017, which included an \$8 million commission expense reduction due to hurricane losses in the 2017 period, partially offset by the impact of higher premiums on the ratio in the international operations.

Commissions and other underwriting expenses as a percentage of net earned premiums decreased 2.9 percentage points in 2017 compared to 2016 reflecting lower profitability-based commissions paid to agents in the financial institutions business, including an \$8 million commission expense reduction due to hurricane losses.

Aggregate Aggregate commissions and other underwriting expenses for AFG's property and casualty insurance segment includes \$8 million of restructuring charges recorded as part of the \$65 million non-core charge related to the

exit of certain lines of business within Neon, AFG's Lloyd's insurer, recorded in the second quarter of 2016. See "Net prior year reserve development" under "Results of Operations — Property and Casualty Insurance Segment" for the years ended December 31, 2018, 2017 and 2016.

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Property and Casualty Net Investment Income

Net investment income in AFG's property and casualty insurance operations was \$438 million in 2018 compared to \$362 million in 2017, an increase of \$76 million (21%). Net investment income in AFG's property and casualty operations was \$362 million in 2017 compared to \$350 million in 2016, an increase of \$12 million (3%). In recent years, yields available in the financial markets on fixed maturity securities have generally been lower than yields on maturing investments, placing downward pressure on AFG's investment portfolio yield. The average invested assets and overall yield earned on investments held by AFG's property and casualty insurance operations are provided below (dollars in millions):

| | Year ended December 31, | | | 2018 - 2017 | | 2017 - 2016 | |
|---|-------------------------|---------|---------|-------------|----------|-------------|----------|
| | 2018 | 2017 | 2016 | Change | % Change | Change | % Change |
| Net investment income | \$438 | \$362 | \$350 | \$76 | 21 % | \$12 | 3 % |
| Average invested assets (at amortized cost) | \$10,497 | \$9,948 | \$9,550 | \$549 | 6 % | \$398 | 4 % |
| Yield (net investment income as a % of average invested assets) | 4.17 % | 3.64 % | 3.66 % | 0.53 % | | (0.02 %) | |
| Tax equivalent yield (*) | 4.35 % | 4.10 % | 4.16 % | 0.25 % | | (0.06 %) | |

(*) Adjusts the yield on equity securities and tax-exempt bonds to the fully taxable equivalent yield.

The increase in average invested assets and net investment income in the property and casualty insurance segment in 2018 compared to 2017 reflects growth in the property and casualty insurance segment and very strong earnings from limited partnerships and similar investments. The property and casualty insurance segment's overall yield on investments (net investment income as a percentage of average invested assets) was 4.17% in 2018 compared to 3.64% in 2017, an increase of 0.53 percentage points due primarily to the higher earnings from limited partnerships and similar investments. AFG's property and casualty insurance operations recorded \$80 million in earnings from partnerships and similar investments and AFG-managed CLOs in 2018 compared to \$34 million in 2017, an increase of \$46 million (135%). The yield earned on these investments was 13.9% in 2018 compared to 7.9% in 2017. The high returns from limited partnerships and similar investments should not be expected to repeat in future periods.

The increase in average invested assets and net investment income in the property and casualty insurance segment in 2017 as compared to 2016 is due primarily to growth in the property and casualty insurance segment. The property and casualty segment's overall yield on investments was 3.64% in 2017 compared to 3.66% in 2016, a decrease of 0.02 percentage points reflecting the impact of lower yields available in the financial markets and lower income from certain investments that are required to be carried at fair value through earnings, partially offset by higher earnings from limited partnerships and similar investments.

Property and Casualty Other Income and Expenses, Net

GAAP other income and expenses, net for AFG's property and casualty insurance operations was a net expense of \$31 million in 2018, \$13 million in 2017, and \$9 million in 2016. Core other income and expenses, net for AFG's property and casualty insurance operations was a net expense of \$31 million, \$13 million and \$41 million in 2018, 2017 and 2016, respectively. The table below details the items included in GAAP and core other income and expenses, net for AFG's property and casualty insurance operations (in millions):

| | Year ended | | |
|---|--------------|------|------|
| | December 31, | | |
| | 2018 | 2017 | 2016 |
| Other income | | | |
| Income from the sale of real estate (*) | \$— | \$16 | \$1 |

| | | | |
|---|--------|--------|-------|
| Other | 10 | 12 | 18 |
| Total other income | 10 | 28 | 19 |
| Other expenses | | | |
| Amortization of intangibles | 9 | 8 | 8 |
| NATL merger/tender offer expenses | — | — | 10 |
| Other | 32 | 33 | 42 |
| Total other expense | 41 | 41 | 60 |
| Core other income and expenses, net | (31) | (13) | (41) |
| Pretax non-core gain on sale of an apartment property | — | — | 32 |
| GAAP other income and expenses, net | \$(31) | \$(13) | \$(9) |

(*Excludes a pretax non-core gain of \$32 million on the sale of an apartment property in 2016.

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Other income for AFG's property and casualty insurance operations includes \$3 million in 2017 and \$4 million in 2016 in death benefits from life insurance policies.

AFG and its consolidated subsidiaries incurred \$10 million in transaction expenses in 2016 related to GAI's acquisition of all of the NATL common stock that it did not already own. These expenses consisted primarily of financial advisory and legal services. See Note B — "Acquisitions and Sale of Businesses" to the financial statements.

Annuity Segment — Results of Operations

AFG's annuity operations contributed \$361 million in pretax earnings in 2018 compared to \$380 million in 2017, a decrease of \$19 million (5%). AFG's annuity segment results in 2018 compared to 2017 reflect a 10% increase in average annuity investments (at amortized cost) and higher earnings from limited partnerships and similar investments, more than offset by higher unlocking charges, the impact of lower investment yields due to the run-off of higher yielding investments and the impact from changes in stock market performance and interest rates discussed below. The high returns on limited partnerships and similar investments should not be expected to repeat in future periods.

The fair value of derivatives related to FIAs was favorably impacted by higher than anticipated interest rates in 2018 compared to the negative impact of lower than anticipated interest rates in 2017. The favorable impact of interest rates between periods was offset by the negative impact of higher interest on the embedded derivative (from growth in the FIA business and higher interest rates), higher than expected option costs in 2018 and the impact of lower stock market performance in the 2018 period. AFG monitors the major actuarial assumptions underlying its annuity operations throughout the year and conducts detailed reviews ("unlocking") of its assumptions in the fourth quarter of each year. If changes in the economic environment of actual experience would cause material revisions to future estimates, these assumptions are updated (unlocked) in an interim quarter. In addition to the fourth quarter detailed review, AFG unlocked its assumptions for option costs and interest rates in the second quarter of 2018 due to the continued higher FIA option costs (resulting primarily from higher than expected risk-free rates). AFG's unlocking of the actuarial assumptions underlying its annuity operations resulted in a net charge of \$31 million in 2018 compared to \$3 million in 2017.

AFG's annuity operations contributed \$380 million in pretax earnings in 2017 compared to \$368 million in 2016, an increase of \$12 million (3%). The increase in AFG's annuity segment results in 2017 compared to 2016 reflect an 11% increase in average annuity investments (at amortized cost), partially offset by lower investment yields due to the run-off of higher yielding investments and higher general and administrative expenses. The change in fair value of derivatives related to FIAs had a negative impact of \$33 million in 2017 compared to \$27 million in 2016. Both periods reflect the negative impact of lower than anticipated interest rates, partially offset by the positive impact of a higher stock market on the fair value accounting for FIAs. Operating earnings also included a net unlocking annuity charge of \$3 million in 2017 compared to a net annuity expense reduction of \$1 million in 2016.

The following table details AFG's earnings before income taxes from its annuity operations for 2018, 2017 and 2016 (dollars in millions):

| | Year ended December 31, | | | % Change | |
|-----------------------|-------------------------|---------|---------|-------------|-------------|
| | 2018 | 2017 | 2016 | 2018 - 2017 | 2017 - 2016 |
| Revenues: | | | | | |
| Net investment income | \$1,638 | \$1,458 | \$1,356 | 12% | 8% |
| Other income: | | | | | |

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| | | | | | |
|---|-------|-------|-------|-------|-------|
| Guaranteed withdrawal benefit fees | 65 | 60 | 53 | 8 % | 13 % |
| Policy charges and other miscellaneous income | 42 | 43 | 50 | (2 %) | (14%) |
| Total revenues | 1,745 | 1,561 | 1,459 | 12% | 7 % |
| Costs and Expenses: | | | | | |
| Annuity benefits (*) | 998 | 892 | 800 | 12% | 12 % |
| Acquisition expenses | 255 | 168 | 181 | 52% | (7 %) |
| Other expenses | 131 | 121 | 110 | 8 % | 10 % |
| Total costs and expenses | 1,384 | 1,181 | 1,091 | 17% | 8 % |
| Earnings before income taxes | \$361 | \$380 | \$368 | (5 %) | 3 % |

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Detail of annuity earnings before income taxes (dollars in millions):

| | Year ended December 31, | | | % Change | |
|---|----------------------------|-------|-------|----------------|----------------|
| | 2018 | 2017 | 2016 | 2018 - 2017 | 2017 - 2016 |
| Earnings before income taxes — before the impact of unlocking and derivatives related to FIAs | \$425 | \$416 | \$394 | 2 % | 6 % |
| Unlocking | (31) | (3) | 1 | 933 % | (400 %) |
| Impact of derivatives related to FIAs | (33) | (33) | (27) | — % | 22 % |
| Earnings before income taxes | \$361 | \$380 | \$368 | (5 %) | 3 % |

(*) Annuity benefits consisted of the following (dollars in millions):

| | Year ended December 31, | | | % Change | |
|--|----------------------------|--------|--------|----------------|----------------|
| | 2018 | 2017 | 2016 | 2018 - 2017 | 2017 - 2016 |
| Interest credited — fixed | \$704 | \$633 | \$574 | 11 % | 10 % |
| Interest credited — fixed component of variable annuities | 5 | 5 | 5 | — % | — % |
| Other annuity benefits: | | | | | |
| Change in expected death and annuitization reserve | 17 | 18 | 18 | (6 %) | — % |
| Amortization of sales inducements | 19 | 19 | 24 | — % | (21 %) |
| Change in guaranteed withdrawal benefit reserve: | | | | | |
| Impact of change in the stock market | 14 | (14) | (6) | (200 %) | 133 % |
| Accretion of benefits and other | 92 | 81 | 75 | 14 % | 8 % |
| Change in other benefit reserves | 37 | 45 | 34 | (18 %) | 32 % |
| Total other annuity benefits | 179 | 149 | 145 | 20 % | 3 % |
| Total before impact of unlocking and derivatives related to FIAs | 888 | 787 | 724 | 13 % | 9 % |
| Unlocking | 59 | 35 | 23 | 69 % | 52 % |
| Derivatives related to fixed-indexed annuities: | | | | | |
| Embedded derivative mark-to-market | (248) | 564 | 194 | (144 %) | 191 % |
| Equity option mark-to-market | 299 | (494) | (141) | (161 %) | 250 % |
| Impact of derivatives related to FIAs | 51 | 70 | 53 | (27 %) | 32 % |
| Total annuity benefits | \$998 | \$892 | \$800 | 12 % | 12 % |

See “Annuity Unlocking” below for a discussion of the impact that the unlocking of actuarial assumptions had on annuity benefit expense.

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Net Spread on Fixed Annuities (excludes variable annuity earnings)

The table below (dollars in millions) details the components of the spreads for AFG's fixed annuity operations (including fixed-indexed and variable-indexed annuities):

| | Year ended December 31, | | | % Change | |
|---|-------------------------|----------|----------|----------|------|
| | 2018 | 2017 | 2016 | 2018 | 2017 |
| | | | | - | - |
| | | | | 2017 | 2016 |
| Average fixed annuity investments (at amortized cost) | \$34,471 | \$31,250 | \$28,223 | 10% | 11% |
| Average fixed annuity benefits accumulated | 34,706 | 31,526 | 28,146 | 10% | 12% |
| As % of fixed annuity benefits accumulated (except as noted): | | | | | |
| Net investment income (as % of fixed annuity investments) | 4.73 | % 4.63 | % 4.77 | % | |
| Interest credited — fixed | (2.03 | %) (2.01 | %) (2.04 | %) | |
| Net interest spread | 2.70 | % 2.62 | % 2.73 | % | |
| Policy charges and other miscellaneous income | 0.10 | % 0.11 | % 0.15 | % | |
| Other annuity benefit expenses, net of guaranteed withdrawal benefit fees | (0.33 | %) (0.28 | %) (0.33 | %) | |
| Acquisition expenses | (0.79 | %) (0.62 | %) (0.70 | %) | |
| Other expenses | (0.37 | %) (0.37 | %) (0.38 | %) | |
| Change in fair value of derivatives related to fixed-indexed annuities | (0.15 | %) (0.22 | %) (0.19 | %) | |
| Unlocking | (0.09 | %) (0.01 | %) 0.01 | % | |
| Net spread earned on fixed annuities | 1.07 | % 1.23 | % 1.29 | % | |

The table below illustrates the impact of fair value accounting for derivatives related to fixed-indexed annuities on the annuity segment's net spread earned on fixed annuities:

| | Year ended December 31, | | |
|---|-------------------------|----------|----------|
| | 2018 | 2017 | 2016 |
| Net spread earned on fixed annuities — before impact of unlocking and derivatives related to FIAs | 1.26 % | 1.34 % | 1.38 % |
| Unlocking | (0.09 %) | (0.01 %) | 0.01 % |
| Impact of derivatives related to fixed-indexed annuities: | | | |
| Change in fair value of derivatives | (0.15 %) | (0.22 %) | (0.19 %) |
| Related impact on amortization of DPAC (*) | 0.05 % | 0.12 % | 0.09 % |
| Related impact on amortization of deferred sales inducements (*) | — % | — % | — % |
| Net spread earned on fixed annuities | 1.07 % | 1.23 % | 1.29 % |

(*) An estimate of the related acceleration/deceleration of the amortization of deferred policy acquisition costs and deferred sales inducements.

Annuity Net Investment Income

Net investment income in 2018 was \$1.64 billion compared to \$1.46 billion in 2017, an increase of \$180 million (12%). This increase reflects the growth in AFG's annuity business and higher earnings from limited partnerships and similar investments, partially offset by the impact of lower investment yields. The overall yield earned on investments in AFG's annuity operations, calculated as net investment income divided by average investment balances (at amortized cost), increased by 0.10 percentage points to 4.73% from 4.63% in 2018 compared to 2017. This increase in net investment yield reflects higher earnings from limited partnerships and similar investments, partially offset by (i) the investment of new premium dollars at lower yields as compared to the existing investment portfolio and (ii) the impact of the reinvestment of proceeds from maturity and redemption of higher yielding investments at the lower yields available in the financial markets. AFG's annuity operations recorded \$114 million in earnings from

partnerships and similar investments and AFG-managed CLOs in 2018 compared to \$53 million in 2017, an increase of \$61 million (115%). The yield earned on these investments was 12.4% in 2018 compared to 8.2% in 2017. The high returns from limited partnerships and similar investments should not be expected to repeat in future periods. For the period from October 1, 2017 through December 31, 2018, \$5.8 billion in annuity segment investments with an average yield of approximately 4.9% were redeemed or sold with the proceeds reinvested at an approximately 0.5% lower yield.

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Net investment income in 2017 was \$1.46 billion compared to \$1.36 billion in 2016, an increase of \$102 million (8%). This increase reflects growth in AFG's annuity business, partially offset by the impact of lower investment yields. The overall yield earned on investments in AFG's annuity operations decreased by 0.14 percentage points to 4.63% from 4.77% in 2017 compared to 2016. This decline in net investment yield reflects (i) the investment of new premium dollars at lower yields as compared to the existing investment portfolio and (ii) the impact of the reinvestment of proceeds from maturity and redemption of higher yielding investments at the lower yields available in the financial markets. During 2017, \$4.9 billion in annuity segment investments with an average yield of 5.14% were redeemed or sold while the investments purchased during 2017 (with new premium dollars and the redemption/sale proceeds) had an average yield at purchase of 3.94%.

Annuity Interest Credited — Fixed

Interest credited — fixed in 2018 was \$704 million compared to \$633 million in 2017, an increase of \$71 million (11%), reflecting the impact of growth in the annuity business. The average interest rate credited to policyholders, calculated as interest credited divided by average fixed annuity benefits accumulated, increased 0.02 percentage points to 2.03% in 2018 from 2.01% in 2017 due primarily to higher crediting rates on new business.

Interest credited — fixed in 2017 was \$633 million compared to \$574 million in 2016, an increase of \$59 million (10%). The impact of growth in the annuity business was partially offset by lower interest crediting rates on new premiums as compared to the crediting rates on policyholder funds surrendered or withdrawn. The average interest rate credited to policyholders decreased 0.03 percentage points to 2.01% in 2017 from 2.04% in 2016.

Annuity Net Interest Spread

AFG's net interest spread increased 0.08 percentage points to 2.70% from 2.62% in 2018 compared to 2017 due primarily to higher earnings from limited partnerships and similar investments, partially offset by lower investment yields. Features included in current annuity offerings allow AFG to achieve its desired profitability at a lower net interest spread than historical product offerings. As a result, AFG expects its net interest spread to narrow in the future.

AFG's net interest spread decreased 0.11 percentage points to 2.62% in 2017 from 2.73% in 2016 due primarily to lower fixed maturity investment yields, partially offset by the impact of lower crediting rates.

Annuity Policy Charges and Other Miscellaneous Income

Annuity policy charges and other miscellaneous income, which consist primarily of surrender charges, amortization of deferred upfront policy charges (unearned revenue) and income from sales of real estate, were \$42 million in 2018 compared to \$43 million in 2017, a decrease of \$1 million (2%). Excluding the impact of unlocking charges of \$1 million in 2018 and \$3 million in 2017 related to unearned revenue, annuity policy charges and other miscellaneous income were \$43 million in 2018 compared to \$46 million in 2017, a decrease of \$3 million (7%). Other miscellaneous income includes \$1 million from the sale of real estate in 2017. Excluding the impact of unlocking charges related to unearned revenue, annuity policy charges and other miscellaneous income as a percentage of average fixed annuity benefits accumulated decreased 0.01 percentage points to 0.10% in 2018 from 0.11% in 2017.

Annuity policy charges and other miscellaneous income were \$43 million in 2017 compared to \$50 million in 2016, a decrease of \$7 million (14%). Excluding the impact of unlocking charges of \$3 million in 2017 and \$1 million in 2016 related to unearned revenue, annuity policy charges and other miscellaneous income were \$46 million in 2017 compared to \$51 million in 2016, a decrease of \$5 million (10%). Other miscellaneous income includes \$1 million in income from the sale of real estate in 2017 compared to \$5 million in 2016. Excluding the impact of unlocking charges related to unearned revenue, annuity policy charges and other miscellaneous income as a percentage of

average fixed annuity benefits accumulated decreased 0.04 percentage points to 0.11% in 2017 from 0.15% in 2016.

See “Annuity Unlocking” below for a discussion of the impact that the unlocking of actuarial assumptions had on annuity policy charges and other miscellaneous income.

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Other Annuity Benefits, Net of Guaranteed Withdrawal Benefit Fees

Other annuity benefits, net of guaranteed withdrawal benefit fees (excluding the impact of unlocking) were \$114 million in 2018, \$89 million in 2017 and \$92 million in 2016, representing an increase of \$25 million (28%) in 2018 compared to 2017 and a decrease of \$3 million (3%) in 2017 compared to 2016. As a percentage of average fixed annuity benefits accumulated, these net expenses increased 0.05 percentage points to 0.33% in 2018 from 0.28% in 2017 and decreased 0.05 percentage points to 0.28% in 2017 from 0.33% in 2016. In addition to interest credited to policyholders' accounts and the change in fair value of derivatives related to fixed-indexed annuities, annuity benefits expense also includes the following expenses (in millions, net of guaranteed withdrawal benefit fees):

| | Year ended December 31, | | |
|--|----------------------------|------|------|
| | 2018 | 2017 | 2016 |
| Change in expected death and annuitization reserve | \$17 | \$18 | \$18 |
| Amortization of sales inducements | 19 | 19 | 24 |
| Change in guaranteed withdrawal benefit reserve: | | | |
| Impact of change in the stock market | 14 | (14) | (6) |
| Accretion of benefits and other | 92 | 81 | 75 |
| Change in other benefit reserves | 37 | 45 | 34 |
| Other annuity benefits | 179 | 149 | 145 |
| Offset guaranteed withdrawal benefit fees | (65) | (60) | (53) |
| Other annuity benefits, net | \$114 | \$89 | \$92 |

As discussed under “Annuity Benefits Accumulated” in Note A — “Accounting Policies” to the financial statements, guaranteed withdrawal benefit reserves are accrued for and modified using assumptions similar to those used in establishing and amortizing deferred policy acquisition costs. The guaranteed withdrawal benefit reserve related to FIAs can be inversely impacted by the calculated FIA embedded derivative reserve as the value to policyholders of the guaranteed withdrawal benefits increases when the benefit of stock market participation decreases. As shown in the table above, the change in the stock market increased AFG’s guaranteed withdrawal benefit reserve by \$14 million in 2018 compared to a favorable impact of \$14 million in 2017. This \$28 million increase (200%) was the primary cause of the \$25 million overall increase in other annuity benefits, net of guaranteed withdrawal fees in 2018 compared to 2017.

See “Annuity Unlocking” below for a discussion of the impact that the unlocking of actuarial assumptions had on annuity benefits expense.

Annuity Acquisition Expenses

Annuity acquisition expenses were \$255 million in 2018 compared to \$168 million in 2017, an increase of \$87 million (52%). Excluding the \$29 million and \$35 million favorable impact on amortization of DPAC from the unlocking recorded in 2018 and 2017, respectively, annuity acquisition expenses were \$284 million in 2018 compared to \$203 million in 2017, an increase of \$81 million (40%), reflecting growth in the business and the acceleration (in 2018) and deceleration (in 2017) of DPAC amortization related to changes in the fair value of derivatives related to FIAs. Excluding the impact of unlocking charges (expense reductions) discussed under “Annuity Unlocking” below, AFG’s amortization of DPAC and commission expenses as a percentage of average fixed annuity benefits accumulated was 0.79% in 2018 compared to 0.62% in 2017 and 0.70% in 2016 and has generally ranged between 0.75% and 0.85%. Variances from the general range relate primarily to the impact of (i) material changes in interest rates or the stock market on AFG’s fixed-indexed annuity business, and (ii) differences in actual experience from actuarially projected estimates and assumptions. For example, the positive impact of higher than anticipated interest rates during 2018 on the fair value of derivatives related to FIAs (discussed below) resulted in a partially offsetting acceleration in the amortization of DPAC. In contrast, the negative impact of significantly lower than anticipated interest rates during 2017 and 2016 on the fair value of derivatives related to FIAs resulted in a partially offsetting deceleration of the

amortization of DPAC.

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The table below illustrates the estimated impact of fair value accounting for derivatives related to fixed-indexed annuities on annuity acquisition expenses as a percentage of average fixed annuity benefits accumulated (excluding the impact of unlocking):

| | Year ended December 31, | | |
|---|-------------------------|----------|----------|
| | 2018 | 2017 | 2016 |
| Before the impact of changes in the fair value of derivatives related to FIAs on the amortization of DPAC | 0.84 % | 0.74 % | 0.79 % |
| Impact of changes in fair value of derivatives related to FIAs on the amortization of DPAC (*) | (0.05 %) | (0.12 %) | (0.09 %) |
| Annuity acquisition expenses as a % of fixed annuity benefits accumulated | 0.79 % | 0.62 % | 0.70 % |

(*) An estimate of the acceleration/deceleration in the amortization of deferred policy acquisition costs resulting from fair value accounting for derivatives related to fixed-indexed annuities.

See “Annuity Unlocking” below for a discussion of the impact that the unlocking of actuarial assumptions had on annuity and supplemental insurance acquisition expenses. Unanticipated spread compression, decreases in the stock market, adverse mortality experience, and higher than expected lapse rates could lead to write-offs of DPAC or PVFP in the future.

Annuity Other Expenses

Annuity other expenses were \$131 million in 2018, \$121 million in 2017 and \$110 million in 2016, representing an increase of \$10 million (8%) in 2018 compared to 2017 and an increase of \$11 million (10%) in 2017 compared to 2016. Annuity other expenses represent primarily general and administrative expenses, as well as selling and issuance expenses that are not deferred. As a percentage of average fixed annuity benefits accumulated, these expenses remained unchanged at 0.37% in 2018 and 2017 and decreased 0.01 percentage points to 0.37% in 2017 from 0.38% in 2016. The increase in annuity other expenses in 2017 compared to 2016 reflects primarily growth in the business and an increase in the number of sales personnel focused on new initiatives and increased market share within existing financial institutions and retail marketing organizations.

Change in Fair Value of Derivatives Related to Fixed-Indexed (Including Variable-Indexed) Annuities

AFG’s fixed-indexed (including variable-indexed) annuities provide policyholders with a crediting rate tied, in part, to the performance of an existing stock market or other financial index. AFG attempts to mitigate the risk in the index-based component of these products through the purchase and sale of call and put options on the appropriate index. AFG’s strategy is designed so that the change in the fair value of the call option assets and put option liabilities will generally offset the economic change in the net liability from the index participation. Both the index-based component of the annuities (an embedded derivative) and the related call and put options are considered derivatives that must be adjusted for changes in fair value through earnings each period. The change in the fair value of the embedded derivative includes an ongoing expense for interest accreted on the embedded derivative. The interest accreted in any period is generally based on the size of the embedded derivative and current interest rates. The fair values of these derivatives are impacted by actual and expected stock market performance and interest rates as well as other factors. For a list of other factors impacting the fair value of the embedded derivative component of AFG’s annuity benefits accumulated, see Note D — “Fair Value Measurements” to the financial statements. Fluctuations in certain of these factors, such as changes in interest rates and the performance of the stock market, are not economic in nature for the current reporting period, but rather impact the timing of reported results.

Excluding the impact of unlocking charges, the net change in fair value of derivatives related to fixed-indexed annuities increased annuity benefits by \$51 million in 2018, \$70 million in 2017 and \$53 million in 2016. The change in the fair value of these derivatives includes \$36 million in 2018, \$16 million in 2017 and \$7 million in 2016 in interest accreted on the embedded derivative (before DPAC amortization). AFG expects both the size of the embedded derivative and interest rates to rise, resulting in continued increases in interest on the embedded derivative. During

2018, the positive impact of higher than expected interest rates on the fair value of these derivatives was more than offset by the higher interest on the embedded derivative, the negative impact of higher than expected option costs and significantly lower stock market performance. The increase in 2017 and 2016 reflects the negative impact of significantly lower than anticipated interest rates on the fair value of these derivatives, partially offset by the positive impact of strong stock market performance in both periods. As a percentage of average fixed annuity benefits accumulated, this net expense decreased 0.07 percentage points to 0.15% in 2018 from 0.22% in 2017, and increased 0.03 percentage points to 0.22% in 2017 from 0.19% in 2016.

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Fluctuations in interest rates and the stock market, among other factors, can cause volatility in the periodic measurement of fair value of the embedded derivative that management believes can be inconsistent with the long-term economics of these products. The table below illustrates the impact of fair value accounting for derivatives related to fixed-indexed annuities on the annuity segment's earnings before income taxes (dollars in millions):

| | Year ended December 31, | | | % Change | |
|---|----------------------------|-------|-------|----------------|----------------|
| | 2018 | 2017 | 2016 | 2018 - 2017 | 2017 - 2016 |
| Earnings before income taxes — before unlocking and change in fair value of derivatives related to FIAs | \$425 | \$416 | \$394 | 2 % | 6 % |
| Unlocking | (31) | (3) | 1 | 933 % | (400 %) |
| Impact of derivatives related to FIAs: | | | | | |
| Change in fair value of derivatives related to FIAs | (51) | (70) | (53) | (27 %) | 32 % |
| Related impact on amortization of DPAC (*) | 18 | 37 | 26 | (51 %) | 42 % |
| Earnings before income taxes | \$361 | \$380 | \$368 | (5 %) | 3 % |

(*) An estimate of the related acceleration/deceleration of amortization of deferred sales inducements and deferred policy acquisition costs.

As illustrated in the table above, the change in fair value of derivatives related to fixed-indexed annuities, including the related impact on amortization of DPAC decreased the annuity segment's earnings before income taxes by \$33 million in both 2018 and 2017 and \$27 million in 2016.

| | Year ended December 31, | | | % Change | |
|--|----------------------------|--------|--------|----------------|----------------|
| | 2018 | 2017 | 2016 | 2018 - 2017 | 2017 - 2016 |
| Interest on the embedded derivative liability | \$(36) | \$(16) | \$(7) | 125 % | 129 % |
| Change in the stock market, including volatility | (11) | 29 | 6 | (138 %) | 383 % |
| Changes in interest rates higher (lower) than expected | 33 | (50) | (29) | (166 %) | 72 % |
| Renewal option costs lower (higher) than expected | (6) | 4 | 5 | (250 %) | (20 %) |
| Other, including the impact of actual versus expected lapses | (13) | — | (2) | — % | (100 %) |
| Impact of derivatives related to FIAs | \$(33) | \$(33) | \$(27) | — % | 22 % |

See “Annuity Unlocking” below for a discussion of the impact that the unlocking of actuarial assumptions had on the change in the fair value of the embedded derivative liability.

Annuity Net Spread Earned on Fixed Annuities

AFG's net spread earned on fixed annuities decreased 0.16 percentage points to 1.07% in 2018 from 1.23% in 2017 due primarily to the net impact of changes in the fair value of derivatives and related DPAC amortization offset discussed above and the impact of the unlocking of actuarial assumptions discussed below, partially offset by the 0.08 percentage points increase in AFG's net interest spread.

AFG's net spread earned on fixed annuities decreased 0.06 percentage points to 1.23% in 2017 from 1.29% in 2016 due primarily to the 0.11 percentage points decrease in AFG's net interest spread, partially offset by other small net positive items.

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Annuity Benefits Accumulated

Annuity premiums received and benefit payments are recorded as increases or decreases in annuity benefits accumulated rather than as revenue and expense. Increases in this liability for interest credited and other benefits are charged to expense and decreases for surrender and other policy charges are credited to other income.

For certain products, annuity benefits accumulated also includes reserves for accrued persistency and premium bonuses, excess benefits expected to be paid on future deaths and annuitizations (“EDAR”) and guaranteed withdrawal benefits. Annuity benefits accumulated also includes amounts advanced from the Federal Home Loan Bank of Cincinnati. The following table is a progression of AFG’s annuity benefits accumulated liability for 2018, 2017 and 2016 (in millions):

| | Year ended December 31, | | |
|---|-------------------------|----------|----------|
| | 2018 | 2017 | 2016 |
| Beginning fixed annuity reserves | \$33,005 | \$29,647 | \$26,371 |
| Fixed annuity premiums (receipts) | 5,382 | 4,313 | 4,398 |
| Federal Home Loan Bank advances and repayments | 225 | (64) | 150 |
| Surrenders, benefits and other withdrawals | (2,836) | (2,246) | (2,189) |
| Interest and other annuity benefit expenses: | | | |
| Interest credited | 704 | 633 | 574 |
| Embedded derivative mark-to-market | (248) | 564 | 194 |
| Change in other benefit reserves | 140 | 117 | 122 |
| Unlocking | 59 | 41 | 27 |
| Ending fixed annuity reserves | \$36,431 | \$33,005 | \$29,647 |
| Reconciliation to annuity benefits accumulated per balance sheet: | | | |
| Ending fixed annuity reserves (from above) | \$36,431 | \$33,005 | \$29,647 |
| Impact of unrealized investment gains | 10 | 133 | 76 |
| Fixed component of variable annuities | 175 | 178 | 184 |
| Annuity benefits accumulated per balance sheet | \$36,616 | \$33,316 | \$29,907 |

Statutory Annuity Premiums

AFG’s annuity operations generated statutory premiums of \$5.41 billion in 2018, \$4.34 billion in 2017 and \$4.44 billion in 2016, an increase of \$1.07 billion (25%) in 2018 compared to 2017 and a decrease of \$94 million (2%) in 2017 compared to 2016. The following table summarizes AFG’s annuity sales (dollars in millions):

| | Year ended December 31, | | | % Change | |
|---|-------------------------|---------|---------|-------------|-------------|
| | 2018 | 2017 | 2016 | 2018 - 2017 | 2017 - 2016 |
| Financial institutions single premium annuities — indexed | \$1,776 | \$1,711 | \$1,950 | 4 % | (12) % |
| Financial institutions single premium annuities — fixed | 492 | 622 | 468 | (21) % | 33 % |
| Retail single premium annuities — indexed | 1,418 | 990 | 1,056 | 43 % | (6) % |
| Retail single premium annuities — fixed | 87 | 70 | 73 | 24 % | (4) % |
| Broker dealer single premium annuities — indexed | 1,271 | 733 | 658 | 73 % | 11 % |
| Broker dealer single premium annuities — fixed | 14 | 7 | 9 | 100 % | (22) % |
| Pension risk transfer | 132 | 6 | — | 2,100 % | — % |
| Education market — fixed and indexed annuities | 192 | 174 | 184 | 10 % | (5) % |
| Total fixed annuity premiums | 5,382 | 4,313 | 4,398 | 25 % | (2) % |
| Variable annuities | 25 | 28 | 37 | (11) % | (24) % |
| Total annuity premiums | \$5,407 | \$4,341 | \$4,435 | 25 % | (2) % |

Management believes the 25% increase in annuity premiums in 2018 compared to 2017 is the result of the introduction of new products, efforts to expand in the retail and broker dealer markets and an improving interest rate environment in 2018.

Management attributes the 2% decrease in annuity premiums in 2017 compared to 2016 to AFG's adherence to pricing discipline in a relatively low and decreasing interest rate environment during the year, as well as from aggressive pricing in certain of AFG's competitors.

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Annuity Unlocking

AFG monitors the major actuarial assumptions underlying its annuity operations throughout the year and conducts detailed reviews (“unlocking”) of its assumptions in the fourth quarter of each year. If changes in the economic environment or actual experience would cause material revisions to future estimates, these assumptions are updated (unlocked) in an interim period. AFG recorded net unlocking charges related to its annuity business of \$31 million and \$3 million in 2018 and 2017, respectively, and a net expense reduction of \$1 million in 2016, which impacted AFG’s financial statements as follows (in millions):

| | Year ended December 31, | | |
|--|----------------------------|--------|--------|
| | 2018 | 2017 | 2016 |
| Policy charges and other miscellaneous income: | | | |
| Unearned revenue | \$(1) | \$(3) | \$(1) |
| Total revenues | (1) | (3) | (1) |
| Annuity benefits: | | | |
| Fixed-indexed annuities embedded derivative | 44 | 25 | 17 |
| Sales inducements | — | (6) | (4) |
| Other reserves | 15 | 16 | 10 |
| Total annuity benefits | 59 | 35 | 23 |
| Annuity and supplemental insurance acquisition expenses: | | | |
| Deferred policy acquisition costs | (29) | (35) | (25) |
| Total costs and expenses | 30 | — | (2) |
| Net expense reduction (charge) | \$(31) | \$(3) | \$1 |

See “Annuity Unlocking” under “Annuity Segment — Results of Operations” for the quarters ended December 31, 2018 and 2017 for a discussion of the overall net expense reduction from the periodic review of actuarial assumptions in the fourth quarter of 2018 and 2017.

In addition to the \$4 million net charge from the periodic review of annuity assumptions in the fourth quarter of 2018, AFG recorded a \$27 million net unlocking charge in the second quarter of 2018 due primarily to the unfavorable impact of higher projected option costs, partially offset by the favorable impact of an increase in projected net interest spreads on in-force business (due primarily to higher than previously anticipated reinvestment rates). Reinvestment rate assumptions are based primarily on 7-year and 10-year corporate bond yields.

Annuity Earnings before Income Taxes Reconciliation

The following table reconciles the net spread earned on AFG’s fixed annuities to overall annuity pretax earnings for 2018, 2017 and 2016 (in millions):

| | Year ended December 31, | | |
|--|----------------------------|-------|-------|
| | 2018 | 2017 | 2016 |
| Earnings on fixed annuity benefits accumulated | \$370 | \$387 | \$363 |
| Earnings impact of investments in excess of fixed annuity benefits accumulated (*) | (11) | (13) | 4 |
| Variable annuity earnings | 2 | 6 | 1 |
| Earnings before income taxes | \$361 | \$380 | \$368 |

Net investment income (as a % of investments) of 4.73%, 4.63% and 4.77% in 2018, 2017 and 2016, respectively, (*) multiplied by the difference between average fixed annuity investments (at amortized cost) and average fixed annuity benefits accumulated in each period.

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Holding Company, Other and Unallocated — Results of Operations AFG's net GAAP pretax loss outside of its property and casualty insurance and annuity operations (excluding realized gains and losses) totaled \$165 million in 2018 compared to \$252 million in 2017, a decrease of \$87 million (35%). AFG's net core pretax loss outside of its property and casualty insurance and annuity operations (excluding realized gains and losses) totaled \$156 million in 2018 compared to \$177 million in 2017, a decrease of \$21 million (12%).

AFG's net GAAP pretax loss outside of its property and casualty insurance and annuity operations (excluding realized gains and losses) totaled \$252 million in 2017 compared to \$177 million in 2016, an increase of \$75 million (42%). AFG's net core pretax loss outside of its property and casualty insurance and annuity operations (excluding realized gains and losses) totaled \$177 million in 2017 compared to \$174 million in 2016, an increase of \$3 million (2%).

The following table details AFG's GAAP and core loss before income taxes from operations outside of its insurance operations in 2018, 2017 and 2016 (dollars in millions):

| | Year ended December 31, | | | % Change | |
|---|-------------------------|---------|---------|-------------|-------------|
| | 2018 | 2017 | 2016 | 2018 - 2017 | 2017 - 2016 |
| Revenues: | | | | | |
| Life, accident and health net earned premiums | \$24 | \$22 | \$24 | 9 % | (8 %) |
| Net investment income | 25 | 34 | 27 | (26 %) | 26 % |
| Other income — P&C fees | 69 | 66 | 60 | 5 % | 10 % |
| Other income | 29 | 27 | 27 | 7 % | — % |
| Total revenues | 147 | 149 | 138 | (1 %) | 8 % |
| Costs and Expenses: | | | | | |
| Property and casualty insurance — commissions and other underwriting expenses | 23 | 25 | 19 | (8 %) | 32 % |
| Life, accident and health benefits | 40 | 26 | 33 | 54 % | (21 %) |
| Life, accident and health acquisition expenses | 6 | 5 | 5 | 20 % | — % |
| Other expense — expenses associated with P&C fees | 46 | 41 | 41 | 12 % | — % |
| Other expenses (*) | 126 | 144 | 137 | (13 %) | 5 % |
| Costs and expenses, excluding interest charges on borrowed money | 241 | 241 | 235 | — % | 3 % |
| Core loss before income taxes, excluding realized gains and losses and interest charges on borrowed money | (94) | (92) | (97) | 2 % | (5 %) |
| Interest charges on borrowed money | 62 | 85 | 77 | (27 %) | 10 % |
| Core loss before income taxes, excluding realized gains and losses | (156) | (177) | (174) | (12 %) | 2 % |
| Pretax non-core special A&E charges | (9) | (24) | (5) | (63 %) | 380 % |
| Pretax non-core loss on retirement of debt | — | (51) | — | (100 %) | — % |
| Pretax non-core realized gain on subsidiaries | — | — | 2 | — % | (100 %) |
| GAAP loss before income taxes, excluding realized gains and losses | \$(165) | \$(252) | \$(177) | (35 %) | 42 % |

(*) Excludes pretax non-core special A&E charges of \$9 million, \$24 million and \$5 million in 2018, 2017 and 2016, respectively, and a pretax non-core loss on retirement of debt of \$51 million in 2017.

Holding Company and Other — Life, Accident and Health Premiums, Benefits and Acquisition Expenses

AFG's run-off long-term care and life insurance operations recorded net earned premiums of \$24 million and related benefits and acquisition expenses of \$46 million in 2018 compared to net earned premiums of \$22 million and related benefits and acquisition expenses of \$31 million in 2017. The \$14 million (54%) increase in life, accident and health benefits reflects higher claims in both the run-off long-term care and run-off life insurance businesses in 2018 compared to 2017.

AFG's run-off long-term care and life insurance operations recorded net earned premiums of \$22 million and related benefits and acquisition expenses of \$31 million in 2017 compared to net earned premiums of \$24 million and related benefits and acquisition expenses of \$38 million in 2016. The \$7 million (21%) decrease in life, accident and health benefits reflects the impact of improved life claims experience in 2017 compared to 2016.

Holding Company and Other — Net Investment Income

AFG recorded net investment income on investments held outside of its property and casualty insurance and annuity operations of \$25 million, \$34 million and \$27 million in 2018, 2017 and 2016, respectively. The \$9 million (26%) decrease in 2018 as

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compared to 2017 and the \$7 million (26%) increase in 2017 as compared to 2016 is due primarily to the impact of the market performance on a small portfolio of securities that are carried at fair value through net investment income. These securities decreased in value by \$4 million in 2018 and increased in value by \$6 million in 2017.

Holding Company and Other — P&C Fees and Related Expenses

Summit, a workers' compensation insurance subsidiary, collects fees from a small group of unaffiliated insurers for providing underwriting, policy administration and claims services. In addition, certain of AFG's property and casualty businesses collect fees from customers for ancillary services such as workplace safety programs and premium financing. In 2018, AFG collected \$69 million in fees for these services compared to \$66 million in 2017 and \$60 million in 2016. Management views this fee income, net of the \$46 million in 2018 and \$41 million in both 2017 and 2016, in expenses incurred to generate such fees, as a reduction in the cost of underwriting its property and casualty insurance policies. Consistent with internal management reporting, these fees and the related expenses are netted and recorded as a reduction of commissions and other underwriting expenses in AFG's segmented results.

Holding Company and Other — Other Income

Other income in the table above includes \$16 million, \$18 million and \$17 million in 2018, 2017 and 2016, respectively, in management fees paid to AFG by the AFG-managed CLOs (AFG's consolidated managed investment entities). The management fees are eliminated in consolidation — see the other income line in the Consolidated MIEs column under "Results of Operations — Segmented Statement of Earnings." Excluding amounts eliminated in consolidation, AFG recorded other income outside of its property and casualty insurance and annuity operations of \$13 million in 2018, \$9 million in 2017 and \$10 million in 2016.

Holding Company and Other — Other Expenses

Excluding the non-core special A&E charges and the non-core losses on retirement of debt discussed below, AFG's holding companies and other operations outside of its property and casualty insurance and annuity operations recorded other expenses of \$126 million in 2018 compared to \$144 million in 2017, a decrease of \$18 million (13%). This decrease reflects lower holding company expenses related to employee benefit plans that are tied to stock market performance, partially offset by a \$5 million charge to increase liabilities related to the environmental exposures of AFG's former railroad and manufacturing operations in 2018. AFG's holding companies and other operations outside of its property and casualty insurance and annuity operations recorded other expenses of \$144 million in 2017 compared to \$137 million in 2016, an increase of \$7 million (5%). This increase reflects higher holding company expenses related to employee benefit plans that are tied to stock market performance, partially offset by the impact of a \$5 million donation to the University of Cincinnati College of Business in 2016.

Holding Company and Other — Interest Charges on Borrowed Money

The following table details the principal amount of AFG's long-term debt balances as of January 1, 2018, January 1, 2017 and January 1, 2016 (dollars in millions):

| | January 1, 2018 | January 1, 2017 | January 1, 2016 |
|---|-----------------------|-----------------------|-----------------------|
| Direct obligations of AFG: | | | |
| 4.50% Senior Notes due June 2047 | \$590 | \$— | \$— |
| 3.50% Senior Notes due August 2026 | 425 | 300 | — |
| 9-7/8% Senior Notes due June 2019 | — | 350 | 350 |
| 6-3/8% Senior Notes due June 2042 | — | 230 | 230 |
| 5-3/4% Senior Notes due August 2042 | — | 125 | 125 |
| 6-1/4% Subordinated Debentures due September 2054 | 150 | 150 | 150 |
| 6% Subordinated Debentures due November 2055 | 150 | 150 | 150 |
| Other | 3 | 3 | 3 |

| | | | |
|--|---------|---------|---------|
| Total principal amount of Holding Company Debt | \$1,318 | \$1,308 | \$1,008 |
|--|---------|---------|---------|

| | | | | |
|--------------------------------|-----|-------|-------|---|
| Weighted Average Interest Rate | 4.6 | % 6.5 | % 7.4 | % |
|--------------------------------|-----|-------|-------|---|

AFG's holding companies and other operations outside of its property and casualty insurance and annuity operations recorded interest expense of \$62 million in 2018, \$85 million in 2017 and \$77 million in 2016. The \$23 million (27%) decrease in interest expense in 2018 compared to 2017 is due primarily to a lower weighted average interest rate on AFG's outstanding debt. The \$8 million (10%) increase in interest expense in 2017 compared to 2016 reflects higher average indebtedness during 2017 compared to 2016, partially offset by a lower weighted average interest rate on outstanding debt.

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The decrease in the weighted average interest rate for 2018 compared to 2017 and 2017 compared to 2016 reflects the following financing transactions completed by AFG in 2016 and 2017:

- Issued \$300 million of 3.50% Senior Notes in August 2016
- Issued \$350 million of 4.50% Senior Notes in June 2017
- Redeemed \$230 million of 6-3/8% Senior Notes in June 2017
- Redeemed \$125 million of 5-3/4% Senior Notes in August 2017
- Issued an additional \$125 million of 3.50% Senior Notes in November 2017
- Issued an additional \$240 million of 4.50% Senior Notes in November 2017
- Redeemed \$350 million of 9-7/8% Senior Notes in December 2017

Holding Company and Other — Special A&E Charges

As a result of the comprehensive external studies and internal reviews of A&E exposures discussed under “Uncertainties — Asbestos and Environmental-related (“A&E”) Insurance Reserves,” AFG’s holding companies and other operations outside of its property and casualty insurance and annuity operations recorded non-core special charges of \$9 million in 2018, \$24 million in 2017 and \$5 million in 2016 to increase liabilities related to the A&E exposures of AFG’s former railroad and manufacturing operations. The charges in 2018, 2017 and 2016 are due to relatively small movements across several sites that primarily reflect changes in the scope and costs of investigation. In addition, AFG has seen a small increase in claims arising from exposure to deleterious substances other than asbestos, which has caused it to increase its estimated future liability. Total charges recorded to increase liabilities for A&E exposures of AFG’s former railroad and manufacturing operations (included in other expenses) were \$21 million in 2018, \$31 million in 2017 and \$20 million in 2016.

Holding Company and Other — Loss on Retirement of Debt

In December 2017, AFG redeemed its \$350 million outstanding principal amount of 9-7/8% Senior Notes due 2019 and recorded a pretax loss on retirement of debt of \$40 million, primarily a \$38 million make-whole premium. In addition, AFG wrote off unamortized debt issuance costs of \$7 million related to the redemption of its \$230 million outstanding 6-3/8% Senior Notes due 2042 at par value in June 2017 and \$4 million related to the redemption of its \$125 million outstanding 5-3/4% Senior Notes due 2042 at par value in August 2017.

Consolidated Realized Gains (Losses) on Securities AFG’s consolidated realized gains (losses) on securities, which are not allocated to segments, were net losses of \$266 million in 2018 compared to net gains of \$5 million in 2017, a decrease of \$271 million (5,420%). AFG’s consolidated realized gains (losses) on securities were net gains of \$5 million in 2017 compared to \$19 million in 2016, a decrease of \$14 million (74%). Realized gains (losses) on securities consisted of the following (in millions):

| | Year ended December 31, | | |
|--|----------------------------|-------|--------|
| | 2018 | 2017 | 2016 |
| Realized gains (losses) before impairments: | | | |
| Disposals | \$9 | \$87 | \$151 |
| Change in the fair value of equity securities (*) | (262) | — | — |
| Change in the fair value of derivatives | (5) | (6) | (9) |
| Adjustments to annuity deferred policy acquisition costs and related items | 11 | (3) | (7) |
| | (247) | 78 | 135 |
| Impairment charges: | | | |
| Securities | (26) | (88) | (131) |
| Adjustments to annuity deferred policy acquisition costs and related items | 7 | 15 | 15 |
| | (19) | (73) | (116) |
| Realized gains (losses) on securities | \$(266) | \$5 | \$19 |
| (*) | | | |

As discussed in Note A — “Accounting Policies — Investments,” beginning in January 2018, all equity securities other than those accounted for under the equity method are carried at fair value through net earnings. This amount includes a \$279 million net loss on securities that were still held at December 31, 2018.

The \$262 million net realized loss from the change in the fair value of equity securities in 2018 includes losses of \$92 million on banks and financing companies, \$31 million on real estate investment trusts, \$30 million on energy exploration and production companies and \$27 million on asset management companies. AFG’s impairment charges on securities in 2018 all relate to fixed maturities. Approximately \$19 million of impairment charges were taken on corporate bonds and \$6 million were taken on residential MBS.

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AFG's impairment charges on securities in 2017 consist of \$63 million on equity securities, \$21 million on fixed maturities and \$4 million on other investments. Approximately \$28 million of the impairment charges in 2017 relates to investments in pharmaceutical companies, \$24 million relates to investments in various industrial entities, \$14 million relates to investments in financial institutions and \$12 million relates to investments in media companies.

AFG's impairment charges on securities in 2016 consist of \$93 million on equity securities and \$38 million on fixed maturities. Approximately \$70 million in impairment charges in 2016 are related to financial institutions, \$19 million are on energy related investments and \$7 million relates to a pharmaceutical company.

Consolidated Income Taxes AFG's consolidated provision for income taxes was \$122 million in 2018 compared to \$247 million in 2017, a decrease of \$125 million (51%). AFG's consolidated provision for income taxes was \$247 million in 2017 compared to \$119 million in 2016, an increase of \$128 million (108%). See Note L — "Income Taxes" to the financial statements for an analysis of items affecting AFG's effective tax rate.

Consolidated Noncontrolling Interests AFG's consolidated net earnings (losses) attributable to noncontrolling interests was a net loss of \$13 million in 2018 compared to net earnings of \$2 million in 2017, an increase of \$15 million (750%). AFG's consolidated net earnings (losses) attributable to noncontrolling interests was earnings of \$2 million in 2017 compared to \$19 million in 2016, a decrease of \$17 million (89%). The following table details net earnings (losses) in consolidated subsidiaries attributable to holders other than AFG (dollars in millions):

| | Year ended | | | % Change | |
|--|--------------|------|-------|-------------|-------------|
| | December 31, | | | | |
| | 2018 | 2017 | 2016 | 2018 - 2017 | 2017 - 2016 |
| Neon | \$(13) | \$ — | \$ — | — % | — % |
| National Interstate | — | — | 15 | — % | (100%) |
| Other | — | 2 | 4 | (100%) | (50 %) |
| Earnings (losses) attributable to noncontrolling interests | \$(13) | \$ 2 | \$ 19 | (750%) | (89 %) |

Other noncontrolling interests includes \$2 million related to the gain on the sale of a hotel property in the first quarter of 2017 and \$4 million related to the gain on the sale of an apartment property in the second quarter of 2016. Both properties were owned by an 80%-owned subsidiary of GAI.

RECENTLY ADOPTED ACCOUNTING STANDARDS

In the fourth quarter of 2017, AFG adopted Accounting Standards Update ("ASU") 2017-04, which simplifies the test for goodwill impairment. Under the previous guidance, if the quantitative test for impairment indicated that the carrying value of a reporting unit exceeded its fair value, an entity had to perform procedures to determine the fair value (at the impairment testing date) of its assets and liabilities (including unrecognized assets and liabilities) following the procedure that would be required in determining the fair value of assets acquired and liabilities assumed in a business combination. Under the new guidance, an impairment charge is measured as the excess of the reporting unit's carrying value over its fair value (up to the full amount of the goodwill). Because the annual impairment testing of AFG's goodwill in 2017 did not require quantitative testing, the implementation of the new guidance had no impact on AFG's results of operations or financial position. In addition, AFG does not expect the new guidance to have a material effect on its results of operations or financial position in future periods.

See Note A — "Accounting Policies — Investments" to the financial statements for a discussion of accounting guidance adopted on January 1, 2018, which, among other things, requires equity investments that are not accounted for under the equity method of accounting to be measured at fair value with changes in fair value recognized in net earnings, clarifies that the need for a valuation allowance on a deferred tax asset related to available for sale securities should be

evaluated with other deferred tax assets and modifies disclosure requirements for financial instruments.

See Note A — “Accounting Policies — Income Taxes” to the financial statements for a discussion of accounting guidance adopted effective December 31, 2017, which allows the reclassification of amounts stranded in accumulated other comprehensive income from accounting for the Tax Cuts and Jobs Act of 2017 to retained earnings.

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ACCOUNTING STANDARDS TO BE ADOPTED

See Note A — “Accounting Policies — Lease Accounting Guidance Effective in 2019” to the financial statements for a discussion of accounting guidance adopted on January 1, 2019, which requires entities that lease assets for terms longer than one year to recognize the assets and liabilities for the rights and obligations created by those leases on the balance sheet based on the present value of cash flows.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments – Credit Losses: Measurement of Credit Losses on Financial Instruments, which provides a new credit loss model for determining credit-related impairments for financial instruments measured at amortized cost (e.g. mortgage loans or reinsurance recoverables) and requires an entity to estimate the credit losses expected over the life of an exposure or pool of exposures. The estimate of expected credit losses considers historical information, current information, as well as reasonable and supportable forecasts, including estimates of prepayments. The expected credit losses, and subsequent increases or decreases in such losses, will be recorded immediately through realized gains (losses) as an allowance that is deducted from the amortized cost basis of the financial asset, with the net carrying value of the financial asset presented on the balance sheet at the amount expected to be collected. The updated guidance also amends the current other-than-temporary impairment model for available for sale debt securities by requiring the recognition of impairments relating to credit losses through an allowance account and limits the amount of credit loss to the difference between a security’s amortized cost basis and its fair value. Subsequent increases or decreases in expected credit losses will be recorded immediately in the income statement through realized gains (losses). AFG will be required to adopt this guidance effective January 1, 2020. AFG cannot estimate the impact that the updated guidance will have on its results of operations, financial position or liquidity until the updated guidance is adopted.

In August 2018, the FASB issued ASU 2018-12, Financial Services – Insurance: Targeted Improvements to the Accounting for Long-Duration Contracts, which changes the assumptions used to measure the liability for future policy benefits for traditional and limited pay contracts (e.g. life, accident and health benefits) from being locked in at inception to being updated at least annually and standardizes the liability discount rate to be used and updated each reporting period, requires the measurement of market risk benefits associated with deposit contracts (e.g. annuities) to be recorded at fair value, simplifies the amortization of deferred policy acquisition costs to a constant level basis over the expected life of the related contracts and requires enhanced disclosures. AFG will be required to adopt this guidance effective January 1, 2022. AFG cannot estimate the impact that the updated guidance will have on its results of operations, financial position or liquidity until the updated guidance is adopted.

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ITEM 7A

Quantitative and Qualitative Disclosures about Market Risk

Market risk represents the potential economic loss arising from adverse changes in the fair value of financial instruments. AFG's exposures to market risk relate primarily to its investment portfolio and annuity contracts, which are exposed to interest rate risk and, to a lesser extent, equity price risk. To a much lesser extent, AFG's long-term debt is also exposed to interest rate risk.

Fixed Maturity Portfolio In general, the fair value of AFG's fixed maturity investments is inversely correlated to changes in market interest rates. AFG's fixed maturity portfolio is comprised of primarily fixed-rate investments with intermediate-term maturities. This practice is designed to allow flexibility in reacting to fluctuations of interest rates. The portfolios of AFG's insurance operations are managed with an attempt to achieve an adequate risk-adjusted return while maintaining sufficient liquidity to meet policyholder obligations. AFG's annuity and run-off long-term care and life operations attempt to align the duration of their invested assets to the projected cash flows of policyholder liabilities.

Consistent with the discussion in Item 7 — Management's Discussion and Analysis — "Investments," the following table demonstrates the sensitivity of the fair value of AFG's fixed maturity portfolio to reasonably likely changes in interest rates by illustrating the estimated effect on AFG's fixed maturity portfolio and accumulated other comprehensive income that an immediate increase of 100 basis points in the interest rate yield curve would have at December 31 (based on the duration of the portfolio, dollars in millions). Effects of increases or decreases from the 100 basis points illustrated would be approximately proportional.

| | 2018 | 2017 |
|---|------------|------------|
| Fair value of fixed maturity portfolio | \$42,102 | \$38,727 |
| Percentage impact on fair value of 100 bps increase in interest rates | (4.5 %) | (5.0 %) |
| Pretax impact on fair value of fixed maturity portfolio | \$(1,895) | \$(1,936) |
| Offsetting adjustments to deferred policy acquisition costs and other balance sheet amounts | 800 | 750 |
| Estimated pretax impact on accumulated other comprehensive income | (1,095) | (1,186) |
| Deferred income tax | 230 | 249 |
| Estimated after-tax impact on accumulated other comprehensive income | \$(865) | \$(937) |

Municipal bonds represented approximately 17% of AFG's fixed maturity portfolio at December 31, 2018. AFG's municipal bond portfolio is high quality, with 99% of the securities rated investment-grade at that date. The portfolio is well diversified across the states of issuance and individual issuers. At December 31, 2018, approximately 78% of the municipal bond portfolio was held in revenue bonds, with the remaining 22% held in general obligation bonds. AFG does not own general obligation bonds issued by Puerto Rico.

Annuity Contracts Substantially all of AFG's fixed rate annuity contracts permit AFG to change crediting rates (subject to minimum interest rate guarantees as determined by applicable law) enabling management to react to changes in market interest rates. In 2003, AFG began issuing products with guaranteed minimum interest rates ("GMIRs") of less than 2%; almost all new business since late 2010 has been issued at a 1% GMIR. At December 31, 2018, AFG could reduce the average crediting rate on approximately \$28 billion of traditional fixed and fixed-indexed annuities without guaranteed withdrawal benefits by approximately 119 basis points (on a weighted average basis).

As presented in Item 7 — Management's Discussion and Analysis — "Results of Operations — Annuity Segment — Years ended December 31, 2018, 2017 and 2016 — Net Spread on Fixed Annuities," the interest credited rate as a percent of fixed annuity benefits accumulated on AFG's in-force block of fixed annuities was 2.03% for the year ended December 31, 2018. Management estimates that the interest credited rate on this in-force business will range from 2.10% to 2.20%

over the next five years. This rate reflects actuarial assumptions as to (i) expected investment spreads, (ii) deaths, (iii) annuitizations, (iv) surrenders and other withdrawals and (v) renewal premiums. Actual experience and changes in actuarial assumptions may result in different effective crediting rates than those above.

Actuarial assumptions used to estimate DPAC and certain annuity liabilities, as well as AFG's ability to maintain spread, could be impacted if a low interest rate environment continues for an extended period, or if increases in interest rates cause policyholder behavior to differ significantly from current expectations.

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Projected payments (in millions) in each of the subsequent five years and for all years thereafter on AFG's fixed annuity liabilities at December 31 were as follows.

| | First | Second | Third | Fourth | Fifth | Thereafter | Total | Fair Value (*) |
|------|---------|---------|---------|---------|---------|------------|----------|-------------------|
| 2018 | \$3,493 | \$3,989 | \$4,609 | \$4,701 | \$4,640 | \$ 22,156 | \$43,588 | \$34,765 |
| 2017 | 2,655 | 3,071 | 3,481 | 4,121 | 4,343 | 20,982 | 38,653 | 32,461 |

(*) Fair value of annuity benefits accumulated excluding life contingent annuities in the payout phase (carrying value of \$232 million at December 31, 2018 and \$206 million at December 31, 2017).

AFG's fixed-indexed (including variable-indexed) annuities provide policyholders with a crediting rate tied, in part, to the performance of an existing stock market or other financial index. AFG attempts to mitigate the risk in the index-based component of these products through the purchase and sale of call and put options on the appropriate index. AFG's strategy is designed so that the change in the fair value of the call option assets and put option liabilities will generally offset the economic change in the net liability from the index participation. Both the index-based component of the annuities (an embedded derivative) and the related call and put options are considered derivatives that must be adjusted for changes in fair value through earnings each period. See Note D — "Fair Value Measurements" and Note F — "Derivatives" to the financial statements for a discussion of these derivatives.

Long-Term Debt The following table shows scheduled principal payments on fixed-rate long-term debt of AFG and its subsidiaries and related weighted average interest rates for each of the subsequent five years and for all years thereafter (dollars in millions):

| | December 31, 2018 | | | December 31, 2017 | | |
|------------|------------------------------------|------|------------|------------------------------------|------|---|
| | Scheduled Principal Payments | | | Scheduled Principal Payments | | |
| 2019 | \$— | — | % 2018 | \$— | — | % |
| 2020 | — | — | % 2019 | — | — | % |
| 2021 | — | — | % 2020 | — | — | % |
| 2022 | — | — | % 2021 | — | — | % |
| 2023 | — | — | % 2022 | — | — | % |
| Thereafter | 1,318 | 4.6% | Thereafter | 1,318 | 4.6% | |
| Total | \$1,318 | 4.6% | Total | \$1,318 | 4.6% | |

Fair Value \$1,231 Fair Value \$1,354

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ITEM 8

Financial Statements and Supplementary Data

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