
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

**Quarterly Report Pursuant to Section 13 or 15(d) of the
Securities Exchange Act of 1934**

**For the Quarterly Period Ended
March 31, 2002**

**Commission File
No. 1-7361**

AMERICAN FINANCIAL CORPORATION

**Incorporated under
the Laws of Ohio**

**IRS Employer I.D.
No. 31-0624874**

**One East Fourth Street, Cincinnati, Ohio 45202
(513) 579-2121**

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 X No

As of May 1, 2002, there were 10,593,000 shares of the Registrant's Common Stock outstanding, all of which were owned by American Financial Group, Inc.

AMERICAN FINANCIAL CORPORATION 10-Q
PART I
FINANCIAL INFORMATION

AMERICAN FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEET
(Dollars In Thousands)

	March 31, 2002	December 31, 2001
Assets:		
Cash and short-term investments	\$ 271,532	\$ 543,644
Investments:		
Fixed maturities - at market (amortized cost - \$11,050,249 and \$10,593,205)	11,077,749	10,748,605
Other stocks - at market (cost - \$180,233 and \$187,810)	319,733	313,710
Policy loans	208,430	211,288
Real estate and other investments	259,722	262,801
Total investments	11,865,634	11,536,404
Recoverables from reinsurers and prepaid reinsurance premiums	2,341,013	2,286,509
Agents' balances and premiums receivable	704,928	666,171
Deferred acquisition costs	852,030	818,323
Other receivables	280,797	254,137
Variable annuity assets (separate accounts)	560,821	529,590
Prepaid expenses, deferred charges and other assets	453,547	451,362
Goodwill	312,594	312,134
	<u>\$17,642,896</u>	<u>\$17,398,274</u>
Liabilities and Capital:		
Unpaid losses and loss adjustment expenses	\$ 4,835,895	\$ 4,777,580
Unearned premiums	1,720,065	1,640,955
Annuity benefits accumulated	5,931,565	5,832,120
Life, accident and health reserves	653,458	638,522
Payable to American Financial Group, Inc.	348,100	356,689
Long-term debt:		
Holding companies	249,518	228,252
Subsidiaries	270,412	270,752
Variable annuity liabilities (separate accounts)	560,821	529,590
Accounts payable, accrued expenses and other liabilities	1,153,187	1,185,146
Total liabilities	15,723,021	15,459,606
Minority interest	455,021	460,737
Shareholders' Equity:		
Preferred Stock - at liquidation value	72,154	72,154
Common Stock, no par value		
- 20,000,000 shares authorized		
- 10,593,000 shares outstanding	9,625	9,625
Capital surplus	985,868	984,125
Retained earnings	301,207	255,127
Unrealized gain on marketable securities, net	96,000	156,900
Total shareholders' equity	1,464,854	1,477,931
	<u>\$17,642,896</u>	<u>\$17,398,274</u>

AMERICAN FINANCIAL CORPORATION 10-Q

AMERICAN FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF EARNINGS
(In Thousands)

	Three months ended March 31,	
	<u>2002</u>	<u>2001</u>
Income:		
Property and casualty insurance premiums	\$603,908	\$644,723
Life, accident and health premiums	70,935	69,158
Investment income	220,959	209,790
Realized losses on:		
Securities	(17,800)	(6,881)
Subsidiaries	-	(1,586)
Other income	<u>47,612</u>	<u>58,292</u>
	<u>925,614</u>	<u>973,496</u>
Costs and Expenses:		
Property and casualty insurance:		
Losses and loss adjustment expenses	442,913	496,216
Commissions and other underwriting expenses	170,266	184,974
Annuity benefits	75,525	69,264
Life, accident and health benefits	55,920	54,083
Interest charges on borrowed money	11,094	18,873
Other operating and general expenses	<u>113,311</u>	<u>107,871</u>
	<u>869,029</u>	<u>931,281</u>
Operating earnings before income taxes	56,585	42,215
Provision for income taxes	<u>2,703</u>	<u>14,952</u>
Net operating earnings	53,882	27,263
Minority interest expense, net of tax	(5,068)	(6,919)
Equity in net losses of investees, net of tax	<u>(2,734)</u>	<u>(3,334)</u>
Net Earnings	<u>\$ 46,080</u>	<u>\$ 17,010</u>

AMERICAN FINANCIAL CORPORATION 10-Q

**AMERICAN FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
(Dollars in Thousands)**

	Preferred Stock	Common Stock and Capital Surplus	Retained Earnings	Unrealized Gain on Securities	Total
Balance at January 1, 2002	<u>\$72,154</u>	<u>\$993,750</u>	<u>\$255,127</u>	<u>\$156,900</u>	<u>\$1,477,931</u>
Net earnings	-	-	46,080	-	46,080
Change in unrealized	-	-	-	(60,900)	(60,900)
Comprehensive income (loss)					(14,820)
Capital contribution from parent	-	1,533	-	-	1,533
Other	-	210	-	-	210
Balance at March 31, 2002	<u>\$72,154</u>	<u>\$995,493</u>	<u>\$301,207</u>	<u>\$ 96,000</u>	<u>\$1,464,854</u>
Balance at January 1, 2001	\$72,154	\$984,391	\$258,371	\$139,200	\$1,454,116
Net earnings	-	-	17,010	-	17,010
Change in unrealized	-	-	-	34,400	34,400
Comprehensive income					51,410
Capital contribution from parent	-	3,067	-	-	3,067
Other	-	(174)	-	-	(174)
Balance at March 31, 2001	<u>\$72,154</u>	<u>\$987,284</u>	<u>\$275,381</u>	<u>\$173,600</u>	<u>\$1,508,419</u>

AMERICAN FINANCIAL CORPORATION 10-Q

AMERICAN FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CASH FLOWS
(In Thousands)

	Three months ended March 31,	
	2002	2001
Operating Activities:		
Net earnings	\$ 46,080	\$ 17,010
Adjustments:		
Equity in net losses of investees	2,734	3,334
Depreciation and amortization	44,295	36,485
Annuity benefits	75,525	69,264
Realized (gains) losses on investing activities	17,605	(6,840)
Deferred annuity and life policy acquisition costs	(38,600)	(35,551)
Decrease (increase) in reinsurance and other receivables	(119,921)	4,727
Increase in other assets	(7,997)	(19,369)
Increase in insurance claims and reserves	152,361	74,616
Increase (decrease) in other liabilities	(4,307)	38,419
Increase in minority interest	3,284	4,095
Other, net	321	(434)
	<u>171,380</u>	<u>185,756</u>
Investing Activities:		
Purchases of and additional investments in:		
Fixed maturity investments	(1,499,179)	(544,186)
Equity securities	-	(2,571)
Real estate, property and equipment	(4,518)	(13,278)
Maturities and redemptions of fixed maturity investments	408,962	131,547
Sales of:		
Fixed maturity investments	597,159	194,182
Equity securities	5,164	4,679
Subsidiaries	-	22,000
Real estate, property and equipment	1,669	24,562
Cash and short-term investments of former subsidiaries	-	(132,858)
Decrease (increase) in other investments	3,368	(673)
	<u>(487,375)</u>	<u>(316,596)</u>
Financing Activities:		
Fixed annuity receipts	169,872	126,223
Annuity surrenders, benefits and withdrawals	(135,912)	(186,921)
Net transfers from (to) variable annuity assets	(5,570)	2,929
Additional long-term borrowings	41,000	26,842
Reductions of long-term debt	(20,240)	(47,601)
Borrowings from AFG	4,400	1,000
Payments to AFG	(12,000)	(23,000)
Capital contribution	2,333	4,667
	<u>43,883</u>	<u>(95,861)</u>
Net Decrease in Cash and Short-term Investments	(272,112)	(226,701)
Cash and short-term investments at beginning of period	<u>543,644</u>	<u>437,263</u>
Cash and short-term investments at end of period	<u>\$ 271,532</u>	<u>\$210,562</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A. Accounting Policies

Basis of Presentation The accompanying consolidated financial statements for American Financial Corporation ("AFC") and subsidiaries are unaudited; however, management believes that all adjustments (consisting only of normal recurring accruals unless otherwise disclosed herein) necessary for fair presentation have been made. The results of operations for interim periods are not necessarily indicative of results to be expected for the year. The financial statements have been prepared in accordance with the instructions to Form 10-Q and therefore do not include all information and footnotes necessary to be in conformity with generally accepted accounting principles.

Certain reclassifications have been made to prior years to conform to the current year's presentation. All significant intercompany balances and transactions have been eliminated. All acquisitions have been treated as purchases. The results of operations of companies since their formation or acquisition are included in the consolidated financial statements.

The preparation of the financial statements requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Changes in circumstances could cause actual results to differ materially from those estimates.

Investments All fixed maturity securities are considered "available for sale" and reported at fair value with unrealized gains and losses reported as a separate component of shareholders' equity. Short-term investments are carried at cost; loans receivable are carried primarily at the aggregate unpaid balance. Premiums and discounts on mortgage-backed securities are amortized over a period based on estimated future principal prepayments and adjusted to reflect actual prepayments.

Gains or losses on securities are determined on the specific identification basis. 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 and the cost basis of that investment is reduced.

Emerging Issues Task Force Issue No. 99-20 established a new standard for recognizing interest income and impairment on certain asset-backed investments. Interest income on these investments is recorded at a yield based on projected cash flows. The yield is adjusted prospectively to reflect actual cash flows and changes in projected amounts. Impairment losses on these investments must be recognized when (i) the fair value of the security is less than its cost basis and (ii) there has been an adverse change in the expected cash flows. The new standard became effective on April 1, 2001. Impairment losses on initial application of this rule were recognized as the cumulative effect of an accounting change. Subsequent impairments are recognized as a component of net realized gains and losses.

Goodwill Goodwill represents the excess of cost of subsidiaries over AFC's equity in their underlying net assets. Through December 31, 2001, goodwill was being amortized over periods of 20 to 40 years. Effective January 1, 2002, AFC implemented Statement of Financial Accounting Standards ("SFAS") No. 142, under which goodwill is no longer amortized but is subject to an impairment test at least annually. As required under SFAS No. 142, AFC will complete the transitional test for goodwill impairment (as of January 1, 2002) by the end of 2002. Any resulting write-down will be reported by restating first quarter 2002 results for the cumulative effect of a change in accounting principle.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

Insurance As discussed under "Reinsurance" below, unpaid losses and loss adjustment expenses and unearned premiums have not been reduced for reinsurance recoverable.

Reinsurance In the normal course of business, AFC's insurance subsidiaries cede reinsurance to other companies to diversify risk and limit maximum loss arising from large claims. To the extent that any reinsuring companies are unable to meet obligations under agreements covering reinsurance ceded, AFC's insurance subsidiaries would remain liable. Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured policies. AFC's insurance subsidiaries report as assets (a) the estimated reinsurance recoverable on unpaid losses, including an estimate for losses incurred but not reported, and (b) amounts paid to reinsurers applicable to the unexpired terms of policies in force. AFC's insurance subsidiaries also assume reinsurance from other companies. Income on reinsurance assumed is recognized based on reports received from ceding companies.

Deferred Acquisition Costs ("DPAC") Policy acquisition costs (principally commissions, premium taxes and other marketing and underwriting expenses) related to the production of new business are deferred. For the property and casualty companies, DPAC is limited based upon recoverability without any consideration for anticipated investment income and is charged against income ratably over the terms of the related policies.

DPAC related to annuities and universal life insurance products is amortized, with interest, in relation to the present value of expected gross profits on the policies. To the extent that realized gains and losses result in adjustments to the amortization of DPAC related to annuities, such adjustments are reflected as components of realized gains. DPAC related to annuities is also adjusted, net of tax, for the change in amortization that would have been recorded if the unrealized gains (losses) from securities had actually been realized. This adjustment is included in unrealized gains (losses) on marketable securities.

DPAC related to traditional life and health insurance is amortized over the expected premium paying period of the related policies, in proportion to the ratio of annual premium revenues to total anticipated premium revenues.

Unpaid Losses and Loss Adjustment Expenses The net liabilities stated for unpaid claims and for expenses of investigation and adjustment of unpaid claims are based upon (a) the accumulation of case estimates for losses reported prior to the close of the accounting period on direct business written; (b) estimates received from ceding reinsurers and insurance pools and associations; (c) estimates of unreported losses based on past experience; (d) estimates based on experience of expenses for investigating and adjusting claims and (e) the current state of the law and coverage litigation. These liabilities are subject to the impact of changes in claim amounts and frequency and other factors. Changes in estimates of the liabilities for losses and loss adjustment expenses are reflected in the Statement of Earnings in the period in which determined. In spite of the variability inherent in such estimates, management believes that the liabilities for unpaid losses and loss adjustment expenses are adequate.

Annuity Benefits Accumulated Annuity receipts 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 are charged to expense and decreases for surrender charges are credited to other income.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

Life, Accident and Health Reserves Liabilities for future policy benefits under traditional life, accident and health policies are computed using the net level premium method. Computations are based on anticipated investment yield, mortality, morbidity and surrenders and include provisions for unfavorable deviations. Reserves established for accident and health claims are modified as necessary to reflect actual experience and developing trends.

Variable Annuity Assets and Liabilities Separate accounts related to variable annuities represent deposits invested in underlying investment funds on which Great American Financial Resources, Inc. ("GAFRI"), an 83%-owned subsidiary, earns a fee. Investment funds are selected and may be changed only by the policyholder, who retains all investment risk. Accordingly, GAFRI's liability for these accounts equals the value of the account assets.

Premium Recognition Property and casualty premiums are earned over the terms of the policies on a pro rata basis. Unearned premiums represent that portion of premiums written which is applicable to the unexpired terms of policies in force. On reinsurance assumed from other insurance companies or written through various underwriting organizations, unearned premiums are based on reports received from such companies and organizations. For traditional life, accident and health products, premiums are recognized as revenue when legally collectible from policyholders. For interest-sensitive life and universal life products, premiums are recorded in a policyholder account which is reflected as a liability. Revenue is recognized as amounts are assessed against the policyholder account for mortality coverage and contract expenses.

Policyholder Dividends Dividends payable to policyholders are included in "Accounts payable, accrued expenses and other liabilities" and represent estimates of amounts payable on participating policies which share in favorable underwriting results. Estimates are accrued during the period in which premiums are earned. Changes in estimates are included in income in the period determined. Policyholder dividends do not become legal liabilities unless and until declared by the boards of directors of the insurance companies.

Minority Interest For balance sheet purposes, minority interest represents (i) the interests of noncontrolling shareholders in AFC subsidiaries, including preferred securities issued by trust subsidiaries of GAFRI and (ii) American Financial Group, Inc.'s ("AFG") direct ownership interest in American Premier Underwriters, Inc. ("American Premier" or "APU") and American Financial Enterprises, Inc. For income statement purposes, minority interest expense represents those shareholders' interest in the earnings of AFC subsidiaries as well as accrued distributions on the trust preferred securities.

Income Taxes AFC files consolidated federal income tax returns which include all 80%-owned U.S. subsidiaries, except for certain life insurance subsidiaries and their subsidiaries. Deferred income taxes are calculated using the liability method. Under this method, deferred income tax assets and liabilities are determined based on differences between financial reporting and tax bases and are measured using enacted tax rates. Deferred tax assets are recognized if it is more likely than not that a benefit will be realized.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

Benefit Plans AFC provides retirement benefits to qualified employees of participating companies through contributory and noncontributory defined contribution plans contained in AFG's Retirement and Savings Plan. The Company makes all contributions to the retirement fund and matches a portion of employee contributions to the savings fund. Employees have been permitted to direct the investment of their contributions to independently managed investment funds, while Company contributions have been invested primarily in securities of AFG and affiliates. Employees are being afforded the flexibility to direct the investment of a portion of their vested retirement fund account balances (increasing from 12.5% in July 2002 to 100% in April 2004) from securities of AFG and its affiliates to independently managed investment funds. The Plan owns 12% of AFG's outstanding common stock. Company contributions are charged against earnings in the year for which they are declared.

AFC and many of its subsidiaries provide health care and life insurance benefits to eligible retirees. AFC also provides postemployment benefits to former or inactive employees (primarily those on disability) who were not deemed retired under other company plans. The projected future cost of providing these benefits is expensed over the period employees earn such benefits.

Derivatives Derivatives included in AFC's Balance Sheet consist primarily of investments in common stock warrants (included in other stocks), the equity-based component of certain annuity products (included in annuity benefits accumulated) and call options (included in other investments) used to mitigate the risk embedded in the equity-indexed annuity products. Changes in the fair value of derivatives are included in current earnings.

Statement of Cash Flows For cash flow purposes, "investing activities" are defined as making and collecting loans and acquiring and disposing of debt or equity instruments and property and equipment. "Financing activities" include obtaining resources from owners and providing them with a return on their investments, borrowing money and repaying amounts borrowed. Annuity receipts, benefits and withdrawals are also reflected as financing activities. All other activities are considered "operating". Short-term investments having original maturities of three months or less when purchased are considered to be cash equivalents for purposes of the financial statements.

B. Acquisitions and Sales of Subsidiaries

Manhattan National Life Insurance In March 2002, GAFRI reached an agreement to acquire Manhattan National Life Insurance Company ("MNL") from Conseco, Inc. for \$48.5 million in cash. GAFRI expects to close on this transaction in the second quarter of 2002 and to fund this acquisition with cash on hand and through reinsurance of up to 90% of the business in force. While MNL is not currently writing new policies, the company reported over \$43 million of statutory renewal premiums in 2001. At December 31, 2001, MNL had approximately 90,000 policies in force (primarily term life) representing over \$12 billion in face amount of insurance, statutory assets of \$297.8 million and statutory capital and surplus of \$23.1 million.

Japanese division In December 2000, AFC agreed to sell its Japanese property and casualty division to Mitsui Marine & Fire Insurance Company of America for \$22 million in cash and recorded an estimated \$10.7 million pretax loss. Upon completion of the sale in March 2001, AFC realized an additional pretax loss of \$1.6 million and deferred a gain of approximately \$21 million on ceded insurance; the deferred gain is being recognized over the estimated settlement period (weighted average of 4 years) of the ceded claims.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

- C. Segments of Operations** AFC's property and casualty group is engaged primarily in specialty and private passenger automobile insurance businesses. The Specialty group includes a highly diversified group of specialty business units. Some of the more significant areas are inland and ocean marine, California workers' compensation, agricultural-related coverages, executive and professional liability, fidelity and surety bonds, collateral protection, and umbrella and excess coverages. The Personal group writes nonstandard and preferred/standard private passenger auto and other personal insurance coverage. AFC's annuity, life and health business markets primarily retirement products as well as life and supplemental health insurance.

The following table (in thousands) shows AFC's revenues and operating profit (loss) by significant business segment. Operating profit (loss) represents total revenues less operating expenses.

	Three months ended March 31,	
	<u>2002</u>	<u>2001</u>
Revenues (a)		
Property and casualty insurance:		
Premiums earned:		
Specialty	\$356,415	\$316,307
Personal	247,203	327,632
Other lines (b)	<u>290</u>	<u>784</u>
	603,908	644,723
Investment and other income	<u>100,259</u>	<u>107,335</u>
	704,167	752,058
Annuities, life and health (c)	217,422	217,030
Other	<u>4,025</u>	<u>4,408</u>
	<u>\$925,614</u>	<u>\$973,496</u>
Operating Profit (Loss)		
Property and casualty insurance:		
Underwriting:		
Specialty	\$ 5,294	(\$ 2,230)
Personal	(5,239)	(27,782)
Other lines (b)	<u>(9,326)</u>	<u>(6,455)</u>
	(9,271)	(36,467)
Investment and other income	<u>63,251</u>	<u>75,202</u>
	53,980	38,735
Annuities, life and health	21,981	30,123
Other (d)	<u>(19,376)</u>	<u>(26,643)</u>
	<u>\$ 56,585</u>	<u>\$ 42,215</u>

- (a) Revenues include sales of products and services as well as other income earned by the respective segments.
 (b) Represents lines in "run-off"; AFC has ceased underwriting new business in these operations.
 (c) Represents primarily investment income.
 (d) Includes holding company expenses.

- D. Goodwill** Effective January 1, 2002, goodwill is no longer amortized. If the \$3.5 million of goodwill amortization had not been deducted in the first quarter of 2001, net earnings for that period would have been \$20.5 million.
- E. Payable to American Financial Group** AFC has a reciprocal Master Credit Agreement with various AFG holding companies under which these companies make funds available to each other for general corporate purposes.

AMERICAN FINANCIAL CORPORATION 10-Q

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

- F. Long-Term Debt** The carrying value of long-term debt consisted of the following (in thousands):

	March 31, 2002	December 31, 2001
Holding Companies:		
AFC notes payable under bank line	\$225,000	\$203,000
APU 10-7/8% Subordinated Notes due May 2011	11,542	11,557
Other	<u>12,976</u>	<u>13,695</u>
	<u>\$249,518</u>	<u>\$228,252</u>
Subsidiaries:		
GAFRI 6-7/8% Senior Notes due June 2008	\$100,000	\$100,000
GAFRI notes payable under bank line	121,100	121,100
Notes payable secured by real estate	36,081	36,253
Other	<u>13,231</u>	<u>13,399</u>
	<u>\$270,412</u>	<u>\$270,752</u>

At March 31, 2002, sinking fund and other scheduled principal payments on debt for the balance of 2002 and the subsequent five years were as follows (in millions):

	Holding Companies	Subsidiaries	Total
2002	\$234.9	\$.9	\$235.8
2003	-	1.2	1.2
2004	-	122.4	122.4
2005	-	10.4	10.4
2006	-	19.1	19.1
2007	.1	.6	.7

Debentures purchased in excess of scheduled payments may be applied to satisfy any sinking fund requirement. The scheduled principal payments shown above assume that debentures previously purchased are applied to the earliest scheduled retirements.

AFC and GAFRI each have an unsecured credit agreement with a group of banks under which they can borrow up to \$300 million and \$155 million, respectively. Borrowings bear interest at floating rates based on prime or Eurodollar rates. Loans mature in December 2002 under the AFC credit agreement and in December 2004 under the GAFRI credit agreement.

- G. Minority Interest** Minority interest in AFC's balance sheet is comprised of the following (in thousands):

	March 31, 2002	December 31, 2001
Interest of AFG (parent) and noncontrolling shareholders in subsidiaries' common stock	\$312,108	\$317,824
Preferred securities issued by subsidiary trusts	<u>142,913</u>	<u>142,913</u>
	<u>\$455,021</u>	<u>\$460,737</u>

AMERICAN FINANCIAL CORPORATION 10-Q

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

Trust Issued Preferred Securities Wholly-owned subsidiary trusts of GAFRI have issued preferred securities and, in turn, purchased a like amount of subordinated debt which provides interest and principal payments to fund the respective trusts' obligations. The preferred securities must be redeemed upon maturity or redemption of the subordinated debt. GAFRI effectively provides unconditional guarantees of its trusts' obligations.

The preferred securities consisted of the following (in thousands):

Date of Issuance	Issue (Maturity Date)	March 31, 2002	December 31, 2001	Optional Redemption Dates
November 1996	GAFRI 9-1/4% TOPrS (2026)	\$72,913	\$72,913	Currently redeemable
March 1997	GAFRI 8-7/8% Pfd (2027)	70,000	70,000	On or after 3/1/2007

Minority Interest Expense Minority interest expense is comprised of (in thousands):

	Three months ended March 31,	
	2002	2001
Interest of AFG (parent) and noncontrolling shareholders in earnings of subsidiaries	\$5,479	\$4,005
Effect of basis difference in realized gains (losses) of subsidiaries	(2,517)	-
Accrued distributions by subsidiaries on trust issued preferred securities, net of tax	2,106	2,914
	<u>\$5,068</u>	<u>\$6,919</u>

- H. **Shareholders' Equity** At March 31, 2002, and December 31, 2001, American Financial Group beneficially owned all of the outstanding shares of AFC's Common Stock.

Preferred Stock Under provisions of both the Nonvoting (4.0 million shares authorized) and Voting (4.0 million shares authorized) Cumulative Preferred Stock, the Board of Directors may divide the authorized stock into series and set specific terms and conditions of each series. At March 31, 2002, and December 31, 2001, the outstanding voting shares of AFC's Preferred Stock consisted of the following:

Series J, no par value; \$25.00 liquidating value per share; annual dividends per share \$2.00; redeemable at AFC's option at \$25.75 per share beginning December 2005 declining to \$25.00 at December 2007 and thereafter; 2,886,161 shares (stated value \$72.2 million) outstanding at March 31, 2002, and December 31, 2001.

The change in unrealized gain on marketable securities for the three months ended March 31 included the following (in millions):

	Pretax	Taxes	Minority Interest	Net
<u>2002</u>				
Unrealized holding losses on securities arising during the period	(\$125.1)	\$43.6	\$12.9	(\$68.6)
Realized losses included in net income	<u>17.8</u>	<u>(6.2)</u>	<u>(3.9)</u>	<u>7.7</u>
Change in unrealized gain on marketable securities, net	<u>(\$107.3)</u>	<u>\$37.4</u>	<u>\$ 9.0</u>	<u>(\$60.9)</u>
<u>2001</u>				
Unrealized holding gains on securities arising during the period	\$ 59.0	(\$20.6)	(\$8.2)	\$30.2
Realized losses included in net income	<u>6.9</u>	<u>(2.4)</u>	<u>(.3)</u>	<u>4.2</u>
Change in unrealized gain on marketable securities, net	<u>\$ 65.9</u>	<u>(\$23.0)</u>	<u>(\$8.5)</u>	<u>\$34.4</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

- I. Equity in Losses of Investees Since 1998, AFC subsidiaries have made loans to two start-up manufacturing businesses which were previously owned by unrelated third-parties. During 2000, the former owners chose to forfeit their equity interests to AFC rather than invest additional capital.

During the fourth quarter of 2000, AFC sold the equity interests to a group of employees for nominal cash consideration plus warrants to repurchase a significant ownership interest. Due to the absence of significant financial investment by the buyers relative to the amount of loans (\$61.5 million at December 31, 2000) owed to AFC subsidiaries, the sale was not recognized as a divestiture for accounting purposes. Assets of the businesses transferred (\$56.1 million at March 31, 2002 and \$57.1 million at December 31, 2001) are included in other assets; liabilities of the businesses transferred (\$11.7 million at March 31, 2002 and \$11.8 million at December 31, 2001, after consolidation and elimination of loans from AFC subsidiaries) are included in other liabilities. Investee losses in the Statement of Earnings represents AFC's equity in the losses of these two companies. One of the businesses is involved in litigation impacting its operations; see "Investee Corporations" in Management's Discussion and Analysis.

- J. Commitments and Contingencies There have been no significant changes to the matters discussed and referred to in Note M "Commitments and Contingencies" of AFC's Annual Report on Form 10-K for 2001.

ITEM 2

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

GENERAL

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

IT Initiative In 1999, AFC initiated an enterprise-wide project to study its information technology ("IT") resources, needs and opportunities. The initiative, involving improvements in physical infrastructure and business support systems, entails extensive effort and costs over a period of several years. While the costs precede the expected savings, management believes the benefits will exceed the costs incurred, all of which have been and will be funded through available working capital.

Forward-Looking Statements 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 forward-looking words such as "believes", "expects", "may", "will", "should", "seeks", "intends", "plans", "estimates", "anticipates" or the negative version of those words or other comparable terminology. Examples of such forward-looking statements include statements relating to: expectations concerning market and other conditions and their effect on future premiums, revenues, earnings and investment activities; expected losses and the adequacy of reserves for asbestos, environmental pollution and mass tort claims; rate increases, improved loss experience and expected expense savings resulting from recent initiatives.

Actual results could differ materially from those contained in or implied by such forward-looking statements for a variety of factors including:

- changes in economic conditions, including interest rates, performance of securities markets, and the availability of capital;
- regulatory actions;
- changes in legal environment;
- tax law changes;
- levels of catastrophes and other major losses;
- the ultimate amount of liabilities associated with certain asbestos and environmental-related insurance claims;
- adequacy of loss reserves;
- availability of reinsurance and ability of reinsurers to pay their obligations; and
- competitive pressures, including the ability to obtain rate increases.

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

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

LIQUIDITY AND CAPITAL RESOURCES

Ratios AFC's debt to total capital ratio at the parent holding company level (excluding amounts due AFG) was approximately 15% at March 31, 2002, and 13% at December 31, 2001. Including amounts due AFG, the ratio was 29% at March 31, 2002, and 28% at December 31, 2001.

AFC's ratio of earnings to fixed charges, excluding and including preferred dividends, on a total enterprise basis was 3.86 and 3.57 for the first three months of 2002 and 1.56 and 1.45 for the entire year of 2001.

Sources of Funds Management believes the parent holding companies have sufficient resources to meet their liquidity requirements, primarily through funds generated by their subsidiaries' operations. If funds provided by subsidiaries through dividends and tax payments are insufficient to meet fixed charges in any period, the holding companies would be required to generate cash through borrowings, sales of securities or other assets, or similar transactions.

AFC has a revolving credit agreement with several banks under which it can borrow up to \$300 million until December 31, 2002. At March 31, 2002, three-fourths of the credit line had been used. While management expects to negotiate a replacement bank agreement later this year, market conditions indicate the maximum amount may be smaller and interest costs will likely be greater.

Investments AFC's investment portfolio at March 31, 2002, contained \$11.1 billion in "Fixed maturities" and \$320 million in "Other stocks", all carried at market value with unrealized gains and losses reported as a separate component of shareholders' equity on an after-tax basis. At March 31, 2002, AFC had pretax net unrealized gains of \$27.5 million on fixed maturities and \$139.5 million on other stocks.

Approximately 93% of the fixed maturities held by AFC at March 31, 2002, 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 noninvestment grade. Management believes that a high quality investment portfolio is more likely to generate a stable and predictable investment return.

Individual portfolio securities are sold creating gains or losses as market opportunities exist. Since all of these securities are carried at market value in the balance sheet, there is virtually no effect on liquidity or financial condition upon the sale and ultimate realization of unrealized gains and losses.

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

Summarized information for the unrealized gains and losses recorded in AFC's balance sheet at March 31, 2002, follows (dollars in millions):

	<u>Securities with</u>	
	<u>Gains</u>	<u>Losses</u>
<u>Fixed Maturities</u>		
Market value	\$6,100	\$4,600
Gross unrealized	\$ 228	\$ 201
Number of security positions	1,200	600
Number individually exceeding \$2 million gain or loss	4	11
Concentration of gains or losses by type or industry (exceeding 5% of unrealized):		
Mortgage-backed securities	\$ 75.2	\$ 36.5
U.S. Treasuries	14.2	11.0
Telephone communications	3.2	33.3
Banks	24.0	1.9
Electric services	7.7	12.3
Air transportation	1.5	11.3
Percentage rated investment grade	96%	90%
<u>Other Stocks</u>		
Market value	\$ 264	\$ 19
Gross unrealized	\$ 151	\$ 12
Number individually exceeding \$2 million gain or loss	3	2

AFC's investment in equity securities of Provident Financial Group, a Cincinnati-based commercial banking and financial services company, represents \$137 million of the \$151 million in unrealized gains on other stocks at March 31, 2002.

The table below sets forth the scheduled maturities of fixed maturity securities (by separate gain/loss segments and in total) at March 31, 2002, based on their market values.

<u>Maturity</u>	<u>Unrealized</u>		<u>Total</u>
	<u>Gains</u>	<u>Losses</u>	
One year or less	9%	1%	6%
After one year through five years	27	15	22
After five years through ten years	18	40	27
After ten years	16	14	15
	70	70	70
Mortgage-backed securities	30	30	30
	100%	100%	100%

AFC realized aggregate losses of \$5.9 million during the first three months of 2002 on \$71.1 million in sales of fixed maturity securities (16 issues) that had unrealized losses at December 31, 2001. Market values of ten of the issues improved from year-end to date of sale while the other six deteriorated; overall, there was a slight net improvement. Of the three with unrealized losses greater than \$500,000 at year-end, actual losses on sale were \$1.1 million less than the unrealized loss at year-end. Although AFC had the ability to continue holding these investments, its intent to hold them changed due to a variety of reasons including actual or expected deterioration in the issuer's credit and decisions to lessen exposure to a particular credit or industry.

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

The length of time securities with unrealized losses at March 31, 2002, have been in an unrealized loss position varies by individual security. Of the 96 individual securities at that date with unrealized losses exceeding \$500,000, 78 have been in that position for less than one year, including 68 that have been in that position for less than six months. Of the 111 individual securities at that date with unrealized gains exceeding \$500,000, 48 have been in that position for less than one year, including 9 that have been in that position for less than six months.

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. The determination of whether unrealized losses are "other than temporary" requires judgment based on subjective as well as objective factors. A listing of factors considered and resources used is contained in the discussion of "Investments" under Management's Discussion and Analysis in AFC's 2001 Form 10-K.

Based on its analysis, management believes (i) AFC will recover its cost basis in the securities with unrealized losses and (ii) that AFC has the ability and intent to hold the securities until they mature or recover in value. Should either of these beliefs 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 a future period. Management believes it is not likely that future impairment charges will have a significant effect on AFC's liquidity.

Uncertainties Aside from risks common to most insurance operations, management believes that the areas posing the greatest risk of material loss are Great American's exposure to asbestos, environmental and other mass tort claims and American Premier's exposure to asbestos, environmental and other contingencies arising out of its former operations.

Property and Casualty Insurance Reserves Future costs of claims are projected based on historical trends adjusted for changes in underwriting standards, policy provisions, product mix and other factors. Estimating the liability for unpaid losses and LAE is inherently judgmental and is influenced by factors which are subject to significant variation. Through the use of analytical reserve development techniques, management monitors items such as the effect of inflation on medical, hospitalization, material, repair and replacement costs, general economic trends and the legal environment.

Asbestos and Environmental-related ("A&E") Reserves Establishing reserves for A&E claims is subject to uncertainties that are significantly greater than those presented by other types of claims. Estimating ultimate liability for asbestos claims presents unique and difficult challenges 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, as is AFC, in extensive litigation over these coverage and liability issues as the volume and severity of claims against asbestos defendants continue to increase.

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

While management believes that AFC's reserves for A&E claims are a reasonable estimate of ultimate liability for such claims, actual results may vary materially from the amount currently recorded due to outstanding issues and uncertainties such as whether coverage exists, whether claims are to be allocated among triggered policies and implicated years, whether claimants who exhibit no signs of illness will be successful in pursuing their claims, predicting the number of future claims, and the impact of recent bankruptcy filings.

Further, certain policyholders assert that each bodily injury claim should be treated as a separate occurrence under the policy, and that their claims are not subject to aggregate limits on coverage because either their policies did not contain aggregate limits with respect to products liability coverage or, faced with exhaustion of products coverage limits, their asbestos claims fall within non-products liability coverage which is not subject to any aggregate limit. These claims are now being contested in insurance coverage litigation in various jurisdictions. In rejecting the claims that are the basis of this litigation, AFC believes its coverage defenses are substantial and intends to continue to vigorously defend its position. Nonetheless, the outcome of this litigation is uncertain and such claims may have a material adverse effect upon AFC's future results of operations and financial condition.

For further discussion of uncertainties and litigation involving AFC, see Note M "Commitments and Contingencies" to the financial statements and "Legal Proceedings" in AFC's Annual Report on Form 10-K for 2001.

RESULTS OF OPERATIONS

General Pretax operating earnings for the first quarter of 2002 were \$56.6 million compared to \$42.2 million for the first quarter of 2001. First quarter results reflect significantly improved property and casualty underwriting results, partially offset by a decrease in income from the sale of real estate and higher realized losses.

Property and Casualty Insurance - Underwriting AFC's property and casualty group consists of two major business groups: Specialty and Personal.

The Specialty group includes a highly diversified group of business lines. Some of the more significant areas are inland and ocean marine, California workers' compensation, agricultural-related coverages, executive and professional liability, fidelity and surety bonds, collateral protection, and umbrella and excess coverages.

The Personal group sells nonstandard and preferred/standard private passenger auto insurance and, to a lesser extent, homeowners' insurance. Nonstandard automobile insurance covers risk not typically accepted for standard automobile coverage because of an applicant's driving record, type of vehicle, age or other criteria.

Underwriting profitability is measured by the combined ratio which is a sum of the ratios of underwriting losses, loss adjustment expenses, underwriting expenses and policyholder dividends to premiums. When the combined ratio is under 100%, underwriting results are generally considered profitable; when the ratio is over 100%, underwriting results are generally considered unprofitable. The combined ratio does not reflect investment income, other income or federal income taxes.

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

Net written premiums and combined ratios for AFC's property and casualty insurance subsidiaries were as follows (dollars in millions):

	Three months ended March 31,	
	2002	2001
<u>Net Written Premiums (GAAP)</u>		
Specialty	\$386.7	\$356.6 (a)
Personal	256.4 (b)	370.5
Other lines	.3	-
	<u>\$643.4</u>	<u>\$727.1</u>
<u>Combined Ratios (GAAP)</u>		
Specialty	98.5%	100.6%
Personal	102.1	108.5
Aggregate (including discontinued lines)	101.4	105.6

(a) Before a reduction of \$29.7 million for unearned premium transfer related to the sale of the Japanese division.

(b) Reflects the ceding of \$88.7 million in premiums under a reinsurance agreement (effective April 1, 2001).

Specialty The Specialty group's increase in net written premiums reflects the impact of rate increases and the realization of growth opportunities in certain commercial markets, partially offset by the decision to discontinue certain lines of business (during 2001) that were not achieving adequate returns and by additional reinsurance agreements. Specialty rate increases averaged over 25% during the first quarter of 2002 and are expected to average approximately 20% for the year. The Specialty group reported a solid underwriting profit for the 2002 quarter with a combined ratio of 98.5%. The 2.1 point improvement in the combined ratio compared to 2001 reflects strategic changes in the mix of specialty businesses and the impact of rate increases.

Personal The Personal group's decline in net written premiums reflects a reinsurance agreement, effective April 1, 2001, under which AFC cedes 90% of the automobile physical damage business written by certain of its insurance subsidiaries. This agreement is enabling AFC to reallocate some of its capital to the more profitable specialty operations. Excluding the effect of this agreement, the Personal group's net written premiums declined about 7%, reflecting lower business volume partially offset by the impact of rate increases. Rate increases implemented in the first quarter of 2002 were about 4% and are expected to range between 8% and 10% for the year. As a result of rate increases implemented over the last year, the combined ratio improved by 6.4 points over the first quarter of 2001. Management expects the Personal group to achieve underwriting profitability by the fourth quarter of 2002.

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

Real Estate Operations AFC's subsidiaries are engaged in a variety of real estate operations including hotels, apartments, office buildings and recreational facilities; they also own several parcels of land. Revenues and expenses of these operations, including gains and losses on disposal, are included in AFC's statement of earnings as shown below (in millions).

	Three months ended March 31,	
	2002	2001
Other income	\$15.3	\$32.0
Other operating and general expenses	14.5	15.0
Interest charges on borrowed money	.6	.7
Minority interest expense, net	-	1.9

Other income includes net pretax gains on the sale of real estate assets of \$171,000 in the first quarter of 2002 and \$15.3 million in the first quarter of 2001.

Other Income Excluding gains on sales of real estate assets (discussed above), other income increased \$4.4 million (10%) due primarily to fees earned by certain new specialty insurance operations.

Realized Gains Realized capital gains have been an important part of the return on investments. Individual assets are sold creating gains and losses as market opportunities exist.

Losses on Securities Realized losses on securities include provisions for other than temporary impairment of securities still held of \$18.3 million in the first quarter of 2002 and \$8 million in the first quarter of 2001. Increased impairment charges in recent years reflect a rise in corporate defaults in the marketplace resulting from the weakened economy.

Warrants to purchase common stock of publicly traded companies are generally considered derivatives and marked to market through current earnings as realized gains and losses. Realized losses on securities include losses of \$3 million in the first quarter of 2002 and \$.8 million in the first quarter of 2001 to adjust the carrying value of AFC's investment in warrants to market value (\$26.4 million at March 31, 2002).

Loss on Subsidiaries AFC recognized a \$1.6 million pretax loss in connection with the sale of the Japanese division in 2001.

Annuity Benefits Annuity benefits reflect amounts accrued on annuity policyholders' funds accumulated. The majority of GAFRI's fixed rate annuity products permit GAFRI to change the crediting rate at any time (subject to minimum interest rate guarantees of 3% or 4% per annum). As a result, management has been able to react to changes in market interest rates and maintain a desired interest rate spread.

Interest Expense Interest expense for the first quarter of 2002 decreased compared to 2001 as lower average interest rates on AFC's variable rate debt (including AFC's payable to AFG) more than offset higher average indebtedness.

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

Other Operating and General Expenses Other operating and general expenses for the first quarter of 2001 include goodwill amortization of \$3.5 million. Under SFAS No. 142, which was implemented January 1, 2002, goodwill is no longer amortized. Excluding 2001 goodwill amortization, other operating and general expenses increased \$8.9 million (9%) due primarily to expenses related to certain new specialty insurance operations and increased amortization of annuity and life deferred acquisition costs.

Income Taxes The 2002 provision for income taxes includes a \$16 million tax benefit for the reversal of previously accrued amounts due to the resolution of certain tax matters.

Investee Corporations Equity in losses of investee corporations represents losses of two start-up manufacturing businesses (see Note I). In November 2001, an injunction was issued against one of the companies which would prohibit the company from using equipment subject to litigation alleging the misappropriation of a trade secret and effectively close the plant. The injunction was subsequently modified, pending appeal, to permit operations to continue and require certain escrow payments. If the investee is unsuccessful in its attempt to have the injunction lifted or further modified, or if operating results fail to improve, a substantial portion of AFC's investment (\$32.4 million as of March 31, 2002), may be written off.

Item 3

Quantitative and Qualitative Disclosure of Market Risk

As of March 31, 2002, there were no material changes to the information provided in AFC's Form 10-K for 2001 under the caption "Exposure to Market Risk" in Management's Discussion and Analysis of Financial Condition and Results of Operations.

AMERICAN FINANCIAL CORPORATION 10-Q
PART II
OTHER INFORMATION

Item 6

Exhibits and Reports on Form 8-K

(a) Exhibit 10 - 2002 Annual Bonus Plan

(b) Reports on Form 8-K: none

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934, American Financial Corporation has duly caused this Report to be signed on its behalf by the undersigned duly authorized.

American Financial Corporation

May 13, 2002

BY: Fred J. Runk
Fred J. Runk
Senior Vice President and Treasurer