

**City Investing Company
and Subsidiaries**

Financial Highlights

In Thousands

	1977	1976
Revenues	\$3,070,597	\$2,535,093
Net Income	82,523	44,253
Per Primary Share	3.01	1.37
Per Share—Assuming Full Dilution	2.29	1.29
Average Primary Shares	22,097	20,642
Average Shares—Assuming Full Dilution	36,543	35,091
Book Value Per Share of Common Stock	19.66	18.74
Total Assets	4,720,994	4,221,914
Common Stock Dividends	17,636	13,606
Preferred Stock Dividends	16,028	16,109
Total Dividends	33,664	29,715
Employees	44,000	37,500
Shareholders	70,100	70,100

The Company City Investing Company's principal businesses are insurance, housing and worldwide manufacturing. City is the world's leading manufacturer of water heaters and steel shipping containers and the nation's foremost magazine printer. City ranks among the country's leading property and casualty insurers, is one of the largest homebuilders in the U.S., is a major producer of residential heating and air conditioning equipment, and operates the nation's largest chain of budget motels.

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City is now ahead of the planning made just over ten years ago when our major acquisition program was undertaken. In this period, City's diverse businesses have grown considerably and have been integrated with appropriate management control and accountability. Today, having met the test of two serious recessions, City's operations are among the leaders in their respective industries.

We believe that the economy continues to be healthy at the outset of 1978. In these circumstances, City Investing is well positioned for continuing earnings growth. Our backlog of orders in manufacturing and housing is encouraging, as is the current favorable trend in insurance underwriting results and the large and growing income stream from the insurance investment portfolio.

In the interest of further developing our management resources and experience, we have recently provided for an interchange of certain responsibilities among corporate management. Peter C.R. Huang, one of City's two presidents, has now assumed responsibility for our insurance and housing operations, while Stephen E. O'Neil, also president, now directs City's domestic

and international manufacturing and energy activities. Edward P. Sheridan, who has been senior vice president and treasurer of City, now, as senior vice president, assumes operational responsibilities in the further development of City's manufacturing businesses. John J. Quirk was elected vice president and treasurer and Lester J. Mantell, director of taxes, was elected a vice president.

G. H. Walker, Jr., a director of City since 1954, died in 1977. We greatly valued his friendship and good counsel. John L. Gibbons, a City director since 1964, retired at year-end 1977. We continue to have the benefit of his contributions to the Company, as Mr. Gibbons has agreed to serve as a member of the Advisory Committee to City's board.

On the threshold of City's second decade in its present form, we are mindful of the following objectives:

- To improve our market leadership through innovation in our principal products and services.
- To provide for additional productive facilities—as we are doing currently—and to seek compatible opportunities for further expansion of our basic businesses.
- To increase the return on shareholders' equity.
- To provide to shareholders cash dividends in proportion to increasing earnings.

Geo. T. Scharffenberger
Chairman & Chief Executive Officer

February 22, 1978





sation, general liability, automobile liability, specifically commercial automobile liability, and commercial multi-peril.

The Home has not sought to expand its participation in personal lines in view of adverse experience with personal automobile business, particularly in states where it has not been possible to obtain rate relief, and with assigned participation in involuntary pools.

The Home is active abroad through its 18.6% participation in AFIA Worldwide Insurance, which maintains 230 branches in 80 countries. The Home's participation in AFIA's premiums in 1977 was \$68 million, versus \$60 million in 1976.

In 1977, total property and casualty earned premiums increased \$197.7 million, 18.3%, to \$1.28 billion. On a weighted basis, company-wide manual rates were 8% higher than those in effect at year-end 1976. These increases, and those of prior years, are estimated to have contributed \$122 million to premiums in 1977.

The average property and casualty insurance claim paid by The Home increased by 12.8% from 1976 to 1977, having declined by .5% in the previous year. The number of new reported claims decreased by 3.6%, versus an increase of 4% the previous year, and the average dollar amount of new reported claims rose by 17.2%, as compared with a negligible change in 1976. Reserves for loss and loss expenses increased by \$215.0 million, or 29.5%, to total \$943.4 million at year-end 1977. During the last two years, reserves have increased by a total of \$365.7 million.

Pretax investment income from The Home's property and casualty insurance investment portfolio increased by 17.0% to \$82.4 million in 1977. At year-end 1977, the market value of the investment portfolio was \$1.5 billion, \$291.0 million, or 24.1%, higher than at the previous year-end. Cash flow to the portfolio was a record \$301.5 million, as compared with \$146.8 million in 1976 and \$3.9 million in 1975.

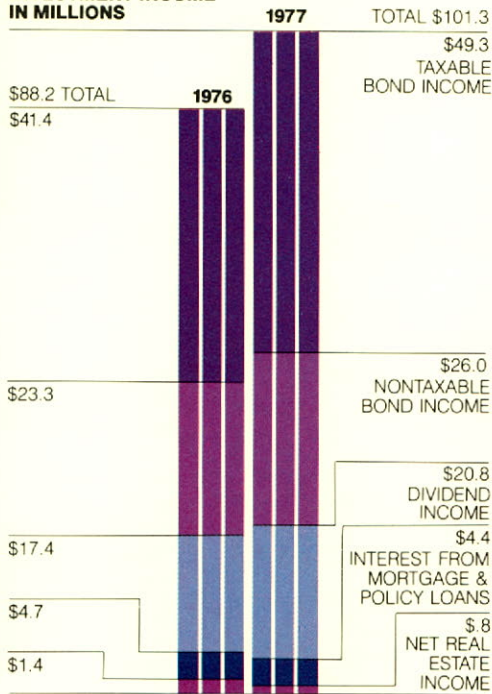
In view of the continued favorable trend of underwriting results, The Home emphasized tax-exempt bonds in its 1977 investment strategy. New investments were allocated approximately 45% to tax-exempts, 35% to taxable bonds and 20% to equities.

The Home's adjusted policyholders' surplus at year-end 1977 was \$365.2 million, representing an increase of 8.2% from the prior year, and resulting in a ratio of written premiums to surplus of 3.4 to 1, as compared with 3.1 to 1 at the end of the previous year.

Life and Health Insurance The Home's principal life and health insurance subsidiaries, Federal Life and Casualty Company and Peoples-Home Life Insurance Company of Indiana, continued to write life and accident and health insurance on a national basis. These companies reported record written premiums in 1977 of \$95.3 million, up 8.9% from the previous year. Earned premiums, also a record at \$92.1 million, represented an increase of 11.4%. At



INSURANCE INVESTMENT INCOME IN MILLIONS



INSURANCE INVESTMENTS IN MILLIONS



year-end 1977, insurance in force for the life companies exceeded \$3.6 billion.

Income from operations in 1977 was \$8.2 million, compared with \$9.1 million the previous year. While income from life insurance business improved, the year-to-year comparison was affected by 1976 having benefited from interest income derived from bond discounts.

Indicative of the rate of growth of the life insurance business was first-year premium volume of \$6.7 million in 1977, up from \$5.1 million the previous year. While volume in individual life and health insurance has been expanded, the company has deliberately reduced its participation in group accident and health business in view of unfavorable experience in this line in prior years.

At year-end 1977, The Home's two major life companies were merged into a single company, Federal Home Life Insurance Company. This merger will provide operating economies and improved service to policyowners and agents.

Other Insurance Operations Included in "Other operations" on page 35 are earnings from The Home's unconsolidated subsidiaries. Among these, Thico Plan, Inc., which is believed to be the second-largest premium financing company in the industry, continued to progress in 1977. Thico's net receivables totaled \$91 million, up 203% from 1976, and income from operations increased 49.7%, to \$1.7 million. Also included are Sterling Forest, a 22,000-acre tract intended for residential development near New York City and Scott Wetzel Services, Inc., which provides risk management services in the growing area of self-insurance.

In 1978, The Home Insurance Company observes its 125th anniversary as one of America's leading property and casualty insurance companies. The Home writes a complete line of property and casualty and life and health insurance.



City's international manufacturing operations comprise sixty-three plants in eighteen countries, mainly producing steel and plastic containers and water heaters.

International Manufacturing

City conducts manufacturing operations in 63 plants in 18 countries abroad. Summary results for the past five years are shown in the accompanying table. The international group, whose products include containers, water heaters, leaf springs and plastics, achieved record revenues and income from operations in 1977. Revenues increased 18.1% to \$393.2 million, and income from operations increased 44.8%, to \$35.9 million. There was no material overall effect on earnings from currency exchange rate changes in 1977. City's participation in certain growing economies, the diversity of its operations abroad and continuing development internally and by acquisition provide a favorable outlook for further growth in 1978.

Brazil City's Rheem Metalurgica is a leading manufacturer of steel drums, pails and food and beverage containers in Brazil. While in prior years profits

were constant on increasing revenues as a result of inflation-related cost increases, exchange rate changes and costs of plant expansion, in 1977 the company's profits improved substantially in consequence of higher unit shipments, improved efficiencies based on full-capacity operation and timely price increases. A new beverage-can line became fully operational in the year and contributed to earnings. The company is now a uniquely integrated manufacturing and marketing operation for a complete range of large and small containers and is investigating opportunities for further expansion of its manufacturing operations.

Mexico City's Rassini Rheem is owned jointly with Altos Hornos, Mexico's largest steel company. A significant portion of the company's revenues are derived from export sales of automotive leaf springs. In 1976, the company's results were adversely affected by the devaluation of the Mexican peso. During 1977, the company began production of steel containers for the petroleum and chemical industries, and expanded production of cold-drawn steel bars in a facility acquired in late 1976.

International Manufacturing In Millions

Revenues	1973	1974	1975	1976	1977
Brazil	\$ 26.6	\$ 46.4	\$ 56.9	\$ 74.2	\$ 94.3
Mexico*	.5	25.0	38.4	56.6	52.0
Belgium	33.0	49.0	50.8	58.1	67.5
Italy	34.3	51.8	51.9	53.3	61.4
United Kingdom*	1.0	1.7	1.4	43.4	52.6
Other International Operations*	52.1	50.6	42.8	47.3	65.4
Total revenues	\$147.5	\$224.5	\$242.2	\$332.9	\$393.2

Income from Operations	1973	1974	1975	1976	1977
Brazil	\$ 3.4	\$ 6.2	\$ 6.0	\$ 6.5	\$ 13.1
Mexico*	.5	2.2	4.6	4.8	8.0
Belgium	3.6	8.2	6.4	9.7	9.6
Italy	.7	1.4	(4.4)	1.6	(.9)
United Kingdom*	1.0	1.7	1.4	3.3	6.5
Other International Operations*	8.6	4.8	3.0	(1.1)	(.4)
Total income from operations	\$ 17.8	\$ 24.5	\$ 17.0	\$ 24.8	\$ 35.9

*The following operations were consolidated in the years indicated, having been previously carried as equity investments: Mexico—1974; United Kingdom—1976; Singapore (included under "Other")—1977.

Belgium City's TMT Group comprises steel container manufacturing operations in Belgium, the Netherlands and France, as well as plastic containers, extruded plastic building materials, beer barrels, drum reconditioning and steel radiators in Belgium. By virtue of its geographic and product diversity, the company has been able to maintain relatively high earnings despite sluggish economic conditions and overcapacity and severe price competition in the European radiator industry. Results for 1977 and 1976 have benefited from favorable translation adjustments. TMT is investigating possibilities for the acquisition of compatible manufacturing operations.

Italy Because of continuing high inflation and generally depressed markets, City's Italian operations showed a loss for the year as compared with a positive result in 1976. The 1976 result, however, benefited from currency translation gains, while in 1977 there were moderate exchange losses. The principal product line, steel drums, showed an increase in unit volume and operated

profitably. Offsetting this were losses in steel structures and water heaters, where concerted efforts are being made to expand into export markets.

United Kingdom Rheem Blagden, which is jointly owned with Blagden & Noakes, Ltd., maintained in 1977 its strong position in steel containers, while improving earnings in drum reconditioning and plastics molding operations. Earnings benefited from the appreciation of the pound sterling relative to the dollar in 1977 versus depreciation of the pound in 1976. In November, 1977, Rheem Blagden acquired W.W. Ball, a manufacturer of molded plastic industrial and consumer products. W.W. Ball revenues are expected to exceed \$10 million in 1978.

Other International Operations Included under this heading in the accompanying table are City's consoli-

dated operations in Canada, South Africa and Singapore, as well as non-consolidated operations and International corporate expense items. Earnings in Canada were adversely affected by depressed business conditions and costs associated with the relocation and expansion of production facilities. The South African container operation, jointly owned with Anglo-American Corporation, reported continued progress in revenues and income from operations. The Singapore operation was consolidated for the first time. This company, Rheem Hume, has container plants in Singapore, Malaysia and Hong Kong, where a plant was acquired in 1977, and is investigating opportunities for further growth in its market areas.

The net loss shown under this heading in 1976 and 1977 is attributed to International corporate expense items, including increased interest costs related to expansion, losses on currency translations pertaining to International corporate borrowings, provision for changes in asset valuations, and increased operating expenses.



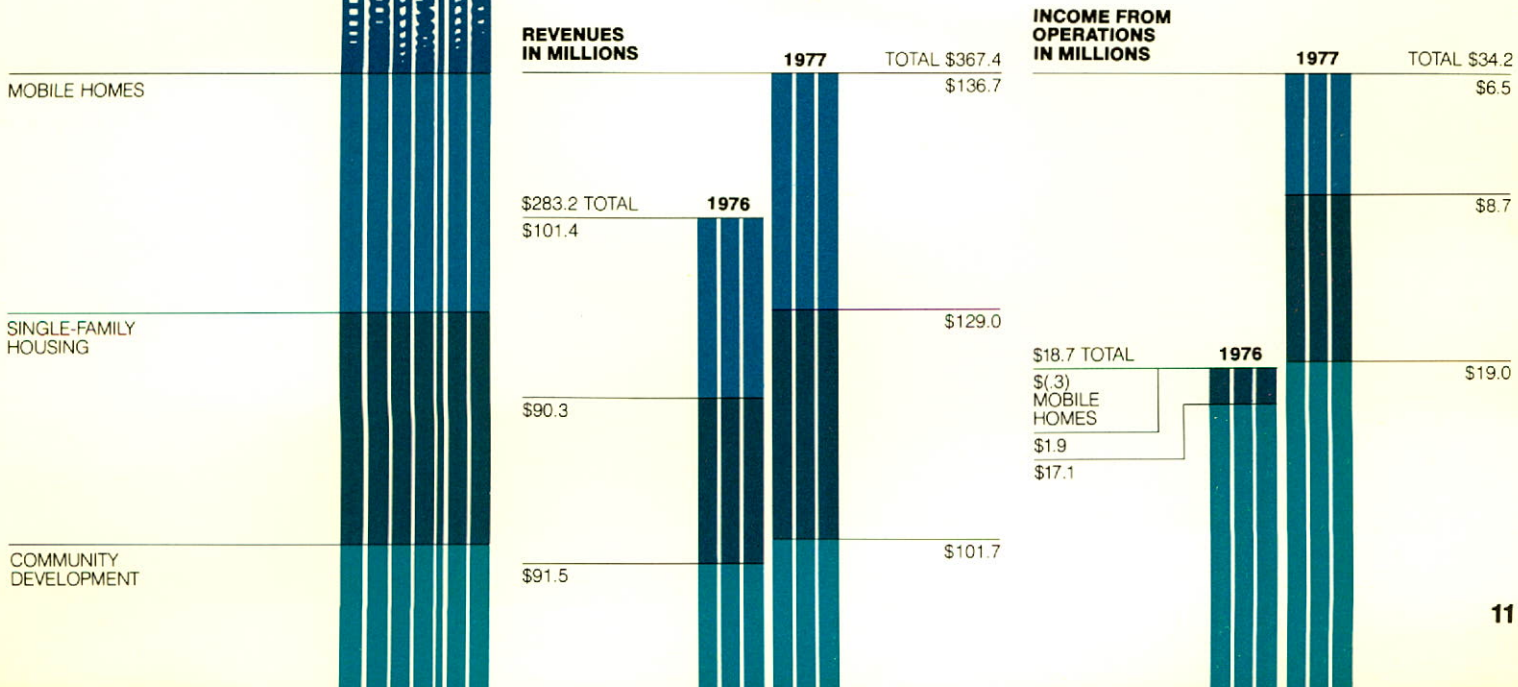
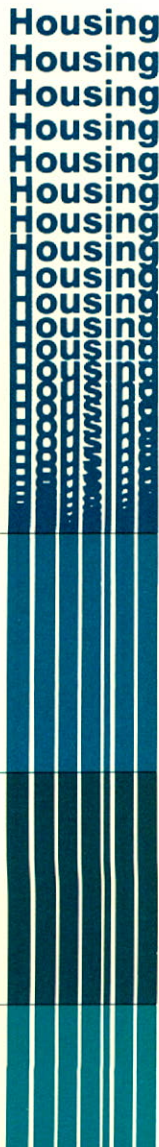
Housing and Community Development

City's housing operations comprise single-family homebuilding, community development and mobile and modular manufactured housing. In 1977, total revenues of these operations increased 29.7% to \$367.4 million, ranking City among the nation's leading participants in the housing industry, while income from operations improved 82.6%, to \$34.2 million.

Single-Family Homebuilding

Wood Bros. Homes, a leading single-family homebuilder in Denver, Dallas, Phoenix, Tucson, Houston and Albuquerque, achieved record sales and earnings in 1977, reflecting the improved trend in the housing market. Revenues increased 42.9%, to \$129.0 million, and income from operations more than quadrupled, to \$8.7 million. The company sold 3,438 homes in 1977, compared with 2,113 units in 1976. The average selling price of a Wood Bros. house, typically 1,570 square feet, was \$45,000 in 1977. During the year, Wood Bros. expanded its operations in existing market areas, added new single-family product lines and opened new operations in El Paso, Texas, and Cheyenne, Wyoming. In November, 1977, Wood Bros. acquired Raldon Corporation of Dallas, Texas, with a product line and price range similar to Wood Bros. Raldon, whose 1977 sales were

Wood Bros. Homes, Inc., is a major builder of single-family homes in the Mountain and Southwestern states.





\$25 million on 570 homes delivered, provides Wood Bros. a leading position in the Dallas market.

Wood Bros. held a record backlog of orders at year end and anticipates further earnings growth in 1978.

Community Development GDV, Inc., 59% owned by City, was formed in 1977 as a holding company to expand and diversify the activities of General Development Corporation, which is wholly-owned by GDV, Inc. In 1977, General Development represented the principal business of GDV.

General Development has been engaged since 1956 in the development of planned communities in Florida in which it offers for sale homesite lots, housing, commercial and special-purpose sites, and typically owns and operates utilities and recreational facilities. General Development's principal communities are Port Charlotte on the

west coast of Florida, Port St. Lucie and Port Malabar on the east coast and Port LaBelle in south central Florida. These communities, together with three smaller communities on the east coast of Florida, comprise approximately 236,000 acres.

In 1977, the company's revenues increased 11.2%, to \$101.7 million, and income from operations improved 11.4%, to \$19.0 million. This improvement reflected a turnaround in housing operations. In 1977, General Development delivered 760 homes, compared with 310 units in 1976. Housing revenues increased to \$29.9 million from \$12.3 million.

After a four-year decline, revenues from sales of homesite lots, accounted for on the instalment basis, improved to \$31.2 million in 1977, versus \$30.6 million in 1976.

In January, 1978, the Board of Directors of GDV approved the proposed acquisition of Wood Bros. Homes, Inc., from

City Investing, for a \$25 million 10% senior promissory note, which approximates City's investment in Wood Bros. The transaction is subject to approval by a majority of the non-City stockholders voting at the GDV annual meeting. GDV's acquisition of Wood Bros. is considered to be an important first step in the planned expansion and diversification of the company. As a result, GDV would rank among the nation's largest homebuilders, with combined assets at December 31, 1977, of \$430 million.

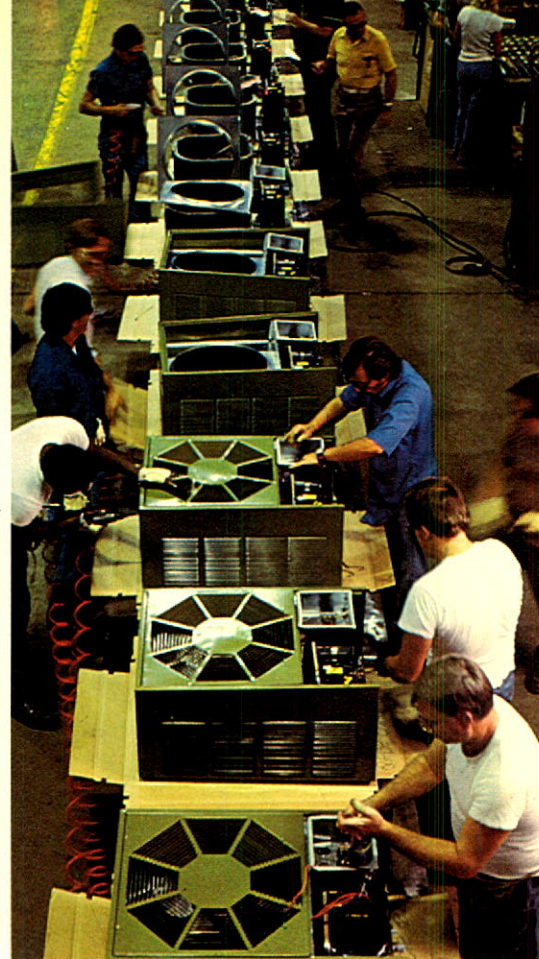
Mobile Homes City's Guerdon Industries, the nation's fourth-largest manufacturer of mobile homes, produces a full line of single-wide and double-wide mobile homes and modular homes. New manufacturing facilities at Boise, Idaho, and at Eupora, Mississippi, were added late in 1977, so that



Guerdon has nineteen plants currently in operation. In 1977, Guerdon's revenues and earnings continued their strong improvement trend with revenues increasing 34.8% to \$136.7 million and income from operations to \$6.5 million, net of \$1.5 million of amortization of parent company intangibles. Estimated total industry shipments of mobile homes increased 13%, to 277,000, while Guerdon's shipments increased 21%. Guerdon's mobile homes vary in size from 600 to 2,100 square feet, and in price from \$4,000 for smaller units to \$30,000 for luxury units and sectional models. Sales in 1977 included exports of mobile homes to the Middle East and to South America. Responding to the dramatic increase in the cost of energy, Guerdon has begun marketing in certain areas an energy-saving home. This program will be expanded in 1978. Based on the need for "affordable" housing which can be supplied by the manufactured housing industry, Guerdon's outlook is for further improvement in sales and earnings in 1978.

City Investing Company, through its Wood Bros. Homes, Guerdon Industries and GDV, Inc., operations, is one of the nation's leading homebuilders.





City is one of the nation's leading air conditioner manufacturers, and is the world's largest producer of water heaters and steel shipping containers.

The division operated in 1977 at its production capacity. To provide for increasing demand for its residential central heating and air conditioning products, the division is currently building a 520,000-square-foot plant at Milledgeville, Georgia, which will double its manufacturing capability, currently based on its Fort Smith, Arkansas, facility. The plant is scheduled to begin operations in late 1978.

In view of continued strength in the housing market and increasing add-on and replacement business, the outlook appears encouraging for 1978.

City's Rheem Water Heater Division, the country's leading manufacturer of residential and commercial water heaters, achieved a 23.2% increase in revenues in 1977, to \$122.5 million, and a 16.4% increase in income from operations, to \$13.0 million, representing the eighth consecutive year of record earnings.

Unit volume in residential water heaters rose 16.7% in 1977. Factors contributing to the division's improved results and increased market share included continuing growth of replacement business,

the strong housing market, a nationwide distribution system comprising Rheem and Ruud wholesaler-distributors and plumbers and continuing improvements in product technology. The current expansion of the Montgomery, Alabama, plant, which will ultimately add one-third to the division's manufacturing capacity, and such new products as the "Sun Set" solar water heating system, introduced late in 1977, contribute to a favorable outlook for further growth in sales and earnings.

Magazine Printing The nation's leading magazine printer, with principal plants at Sparta, Effingham and Salem, Illinois, City's World Color Press for the eighth consecutive year achieved record results. In 1977, revenues increased 25.2%, to \$193.9 million, and income from operations was up 18.3%, to \$15.0 million, reflecting increased production and improved prices.

In June, 1977, World Color signed a ten-year printing contract valued at more



than \$300 million in estimated revenues with The Hearst Corporation to print *Cosmopolitan*, *Good Housekeeping*, *Sports Afield* and *Popular Mechanics* magazines. This contract provides important additional volume to the company's Salem, Illinois, gravure facility, which became operational in 1976 and which is now being expanded.

The trend for the magazine industry generally has been favorable, with advertising revenues and size of publications increasing. In 1977, World Color experienced growth both in printing volume under existing contracts and in new business, which includes *Forbes* and *Boy's Life*, the official publication of The Boy Scouts of America.

World Color continues to investigate new opportunities for expanding print-

ing volume, and further earnings growth is expected in 1978.

Containers The rebound in the container industry which began in 1976 continued in 1977, and City's container division recorded a 15.4% gain in revenues, to \$128.0 million, and a 30.3% increase in income from operations, to \$14.7 million, despite competitive pricing pressures. This improvement reflected the favorable trend of steel drum sales to the chemical, food and petroleum industries. Container shipments are expected to show further, although more moderate gains in 1978, consistent with the trend forecast for the economy. The division will face challenges in 1978 from expected steel price increases and continuing price competition. The division is the nation's largest manufacturer of steel shipping containers, principally 55-gallon drums and smaller containers ranging in size down to 3½-gallon pails. It also makes plastic containers as well as metal closures and processing equipment for flexible packaging systems used by the meat, poultry, dairy and chemical industries.

Other Business Segments

Budget Motels In 1977, City's budget motel operation, Motel 6, Inc., achieved record income from operations of \$11.5 million. This result compares with \$6.6 million in 1976, restated to provide for application of FASB Statement No. 13 requiring the capitalization and amortization of certain leaseholds. Revenues increased 19.2%, to \$75.1 million. The average occupancy rate for the chain in 1977 was 75.3%, up from 66.6% in the previous year. Average room charges increased 1.9% in 1977, to \$11.27.

At year-end 1977, Motel 6 had 239 motels in operation, as compared with 235 at the start of the year. Present plans are to add twenty-five locations annually in the next several years. The company is the leading nationwide economy motel operation and uniquely offers standardized room rates across the country, starting at \$9.45 for a single room.

Alma Plastics Company produces plastic products mainly for the automotive, appliance and building industries.

Motel 6, Inc., is the nation's leading budget motel operation, with 239 locations at year-end 1977.



Savings and Loan City's Southern California Savings and Loan Association nearly doubled income from operations, to a record \$10.1 million in 1977, reflecting advantageous yield spreads between savings deposits and lending rates and increased income from single-family home building operations. The Association is somewhat unusual in its industry in that a significant portion of its income derives from homebuilding. In 1977, the Association participated in the sale of 411 single-family homes in Southern California.

With seventeen offices, the Association ended the year with record deposits of \$307 million, as compared with \$267 million at year-end 1976, and its assets rose to \$379 million from \$335 million.

In February, 1978, the Association agreed to purchase, for \$26.2 million, the assets of First Surety Corp., including Surety Savings and Loan Association, with seven branches in Southern California. Surety Savings and Loan had

deposits of \$142 million and assets of \$171 million at year-end 1977. Assuming completion of the transaction, the Association's resulting approximate ranking will be thirtieth among California savings and loan institutions.

Energy City's energy activities, conducted by City Exploration Company, comprise oil and gas exploration and development activities in the southern United States, the British North Sea, Ecuador, Colombia and Egypt.

As discussed in Financial Report on page 20, in 1977, City elected to adopt Financial Accounting Standards Board Statement No. 19, "Financial Accounting and Reporting for Oil and Gas Producing Companies." Application of this Statement had the effect of reducing earnings for prior years and of reducing the loss previously reported for the first nine months of 1977. City's results have accordingly been restated, and the carrying amount of energy investments at year-end 1977 was reduced to \$7.8 million, net of related indebtedness.

In 1977, City's pretax loss from energy activities amounted to \$21.9 million,

compared with a loss of \$20.2 million, as restated, in 1976. The 1977 result included oil and gas losses in Egypt, Ecuador and the United States, and a \$7.7 million provision for the discontinuance of the Company's domestic coal mining operation.

Watson Oil Corporation continued its domestic production and exploration program during the year. Proved reserves at year-end 1977 amounted to 9.7 billion cubic feet of gas and 428,000 barrels of oil.

On June 30, City concluded an agreement with British Petroleum on the Buchan Field in the British North Sea. BP will develop the field and receive City's 28% interest, subject to a 50% net profits interest retained by City. The Company has received from BP an amount equal to City's past expenditures. That amount will be repaid out of City's share of the future net profits of the field.



BP will also be entitled to one-half of City's remaining interest in the balance of its North Sea license (covering portions of blocks 21-1 and -6). BP will pay City's share of the cost of two additional exploratory wells, one of which was drilled as a dry hole in 1977. The second is being drilled.

In Ecuador, City has nearly completed construction of a feeder pipeline to carry oil from City's producing wells in Oriente Province. This system will provide for initial production of 5,000 barrels of oil per day commencing about mid-1978, from City's concession, which now comprises 118,748 acres.

City's interest in worldwide proved reserves at year-end 1977 totaled 17.2 million barrels of oil and 9.8 billion cubic feet of gas. City's energy policy is to provide for further development and production to the extent that cash flow from present energy operations permits.

Other Operations Included under this heading in the summary of revenues and income from operations on page 35 are the results of City's smaller domestic operations.

City's Refrigeration Division manufactures home food freezers and ultra-low-temperature freezers for scientific use under the Revco label as well as private brands. Shipments of freezers, including a newly-introduced refrigerator with a bottom-mount freezer, increased substantially in 1977. Revenues for the year rose 68.9%, to \$27.3 million, and income from operations was \$1.4 million, compared with a loss in 1976. Expected increased volume, including sales to new customers obtained in 1977, should provide further improvement in 1978.

City's Alma Plastics Company manufactures injection-molded, vacuum-formed and extruded plastic components for the automobile, appliance, building and other industries. In 1977, Alma acquired three additional manufacturing facili-

ties, bringing the total number of plants to eleven and annualized revenues to approximately \$70.0 million.

Hayes International Corporation is principally engaged in maintenance and modification of military and commercial aircraft, primarily for the U.S. Government. 1977 results were adversely affected by start-up costs early in the year on new Air Force contracts and by a month-long strike at the principal operating facility in the second quarter. While revenues increased 37.8% to \$50.1 million, income from operations declined to \$1.1 million from \$2.7 million in 1976. Results improved in the second half of 1977 and are expected to be substantially better in 1978.

City's other operations include C.I. Planning Corporation, the advisor to two real estate investment trusts, C I Mortgage Group and C I Realty Investors. In 1977, C.I. Planning recorded a pretax loss of \$4.7 million in connection with these activities.

Financial Report

Summary Results Revenues during 1977 totaled \$3.07 billion, compared with \$2.54 billion in 1976, a 21% improvement. Net income was \$82.5 million, versus \$44.3 million last year, an 86% improvement. Primary earnings per share increased 120%, to \$3.01, and earnings per share, assuming full dilution, increased 78%, to \$2.29.

Refinancings City's financial structure continued to improve during 1977. In the second quarter, City completed a \$30 million, 8¾% Eurodollar note issue, representing the Company's first public financing in the European market. In the third quarter, City completed a unit offering comprising \$100 million of 9½% sinking fund debentures due 1997 with 800,000 shares of common stock. As a result of these financings, City has repaid all short- and intermediate-term bank debt at the parent company level.

Restructuring of Financial Statements and Retroactive Restatements

During 1977, City adopted three Statements of the Financial Accounting Standards Board. Statement No. 13, "Accounting for Leases," requires that leases transferring substantially all the benefits and risks incident to ownership of property be considered capital leases and reflected in the balance sheet. As a result, \$77.4 million of leases, principally those of City's budget motel operation, were added to the net property, plant and equipment

account, and \$87.9 million has been reflected in the balance sheet as "Obligations under capital leases." Net income for 1976 was retroactively reduced \$1.4 million.

Statement No. 19, "Financial Accounting and Reporting for Oil and Gas Producing Companies," requires the use of a form of the successful efforts method of accounting for oil and gas investments. City had previously capitalized all costs incurred in searching for oil and gas reserves, subject to the limitation that the total amount capitalized not exceed the fair value of the reserves in the country. Under successful efforts, only direct costs incurred in individual successful acquisitions and activities are capitalized. City's energy investments, as reflected on its December 31, 1976, balance sheet, were retroactively reduced \$59.9 million to \$21.9 million, net of related indebtedness. Net income for 1976 was retroactively reduced \$7.5 million.

Statement No. 14, "Financial Reporting for Segments of a Business Enterprise," requires inclusion in the financial statements of certain information including operations in different industries and foreign operations. Since 1972, City has presented in its annual reports to shareholders detailed summaries of revenues and profits by major operating activities for five years. In accordance with Statement No. 14, these operating activities have been grouped into ten business segments on page 35 of this report. The application of this Statement had no effect on the Company's balance sheet or on current or prior years' net income.

City's statement of consolidated income has been restructured from last year's presentation to more meaningfully present consolidated results of operations.

New Investments Major new investments in 1977 include the acquisition of a plastics plant in Milan, Michigan, and

two in Edinburg, Indiana, totaling over 300,000 square feet. Construction is progressing on the new 520,000-square-foot air conditioning plant in Milledgeville, Georgia, the 250,000-square-foot expansion of the Montgomery, Alabama, water heater plant and the 234,000-square-foot expansion of the Salem, Illinois, printing facility, all of which are scheduled for completion by year-end 1978. An additional plastic container plant is also being planned. These investments in 1977 and 1978 will increase our manufacturing facilities by approximately 1,400,000 square feet, and represent the investment of approximately \$83 million to provide for the continued growth of our domestic manufacturing businesses.

Dividend Policy City's dividend policy is to provide shareholders a return on their investment consistent with the Company's internal cash needs for future growth and for servicing debt. In the five years ended 1977, the Company has paid dividends of \$150.4 million on all classes of stock representing 57.7% of the \$260.8 million of cumulative net income, as restated, earned during that period. It is the Company's intention to maintain an approximate 50% relationship of total dividends to net income over five-year periods. Dividends declared during 1977 approximated 41% of 1977 net income.

Financial Position Information in the paragraphs that follow relates mainly to City's financial position, and comments focus primarily on changes in City's balance sheet from 1976 to 1977.

Working capital, at \$228.1 million, increased \$73.3 million from the prior-year level, and the ratio of current assets to current liabilities at year-end was 1.6 to 1, compared with 1.5 to 1 last year. Increases of \$35.4 million in cash, \$48.5

million in accounts receivable and \$63.7 million in inventories contributed to a \$152.8 million increase in current assets, while current liabilities were up \$79.5 million.

Translation of Foreign Accounts Foreign currency assets and liabilities are translated at year-end rates of exchange, except for inventories, plant assets and related depreciation, which are translated at rates in effect at the times of acquisition. Income and expense items are translated at average rates of exchange prevailing during the year, except for inventories charged to cost of sales and depreciation, which are translated at historical rates. Realized profits and losses on exchange transactions and charges and credits arising in consolidation as a result of translating balance sheet accounts are reflected in income. The translation of foreign accounts did not significantly affect 1977 or 1976 consolidated net income.

Inventories classified as current assets were \$299.2 million at the close of 1977, an increase of \$63.7 million, reflecting increases in manufacturing and housing inventories, particularly subdivision land and houses.

Bond investments of insurance and financial companies at the end of 1977 and 1976 are summarized below:

In Millions	1977	1976	Increase
Property and casualty operations			
Taxable bonds	\$ 463.0	\$278.1	\$184.9
Nontaxable bonds	539.7	425.2	114.5
Total property and casualty	1,002.7	703.3	299.4
Life insurance operations	149.5	117.6	31.9
Savings and loan	12.5	12.5	—
Total	\$1,164.7	\$833.4	\$331.3

In accordance with current accounting practices, bonds are carried in the investment account at amortized cost.

Property, plant, equipment and capital leases, net, increased \$53.7 million from last year. Gross additions during 1977, excluding capital leases, totaled \$104.5 million, including \$23.2 million in international manufacturing operations; \$24.9 million in magazine printing facilities and equipment; \$27.0 million in budget motels; and \$9.1 million at GDV, Inc.

Other investments and long-term receivables were \$10.0 million lower than a year ago. As presented on the balance sheet, the \$138.8 million of contracts receivable from homesite sales is net of \$83.4 million of deferred profit related to the sales. Reduced levels of homesite sales in recent years have resulted in a \$15.2 million reduction in the net receivable, which is reported as \$24.0 million current and \$114.8 million long-term.

Reserves and liabilities of insurance and financial companies rose \$269.0 million during 1977, including increases of \$218.0 million in unpaid losses and loss expenses, attributable to higher costs per insurance claim, and \$40.0 million in savings accounts. Unearned insurance premiums were reduced \$24.4 million, due primarily to shorter property and casualty policy terms.

Long-term debt increased a net amount of \$108.3 million, reflecting a decrease of \$1.8 million in current maturities and an increase of \$110.1 million in the long-term portion of the obligations. Approximately two-thirds of the increase was incurred by subsidiaries in connection with expanded operations.

Deferred income taxes of \$166.9 million consist principally of \$101.3 million arising from City's insurance operations, primarily deferral of prepaid insurance acquisition costs for book purposes, and \$65.3 million related to GDV, Inc., principally due to income from homesite sales being reported on a basis for tax purposes which differs from the method used for financial reporting purposes.

Estimated homesite improvement costs represent the estimated future cost to GDV, Inc. to complete land improvements on specific homesites covered by outstanding sales contracts. The liability is carried on the balance sheet as \$17.4 million current and \$27.5 million long-term, the total of which is down \$12.1 million from the prior year.

Shareholders' equity and preferred stock of subsidiary was \$806.0 million at year-end 1977, an increase of \$36.4 million from 1976. Of this amount, \$10.9 million is applicable to the issuance of treasury shares and \$48.9 million reflects 1977 income retained for use in the business after \$33.7 million in cash dividends, offset by an increase of \$23.4 million in unrealized depreciation of stock investments. At year end the book value of common stock was \$19.66 per share, compared with a restated \$18.74 a year earlier.

PEAT, MARWICK, MITCHELL & CO.

CERTIFIED PUBLIC ACCOUNTANTS

555 SOUTH FLOWER STREET

LOS ANGELES, CALIFORNIA 90071

The Board of Directors and Shareholders
City Investing Company:

We have examined the consolidated balance sheet of City Investing Company and subsidiaries as of December 31, 1977 and 1976 and the related consolidated statements of income, retained earnings, unrealized depreciation of stocks held by insurance companies, and changes in financial position for the respective years then ended. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned consolidated financial statements present fairly the financial position of City Investing Company and subsidiaries at December 31, 1977 and 1976, the results of their operations, the changes in retained earnings, unrealized depreciation of stocks held by insurance companies, and the changes in financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis after restatement for the changes, with which we concur, in accounting for oil and gas investments and leases as more fully explained in the Summary of Accounting Policies and Financial Review.

Peat, Marwick, Mitchell & Co.

February 14, 1978

**City Investing Company
and Subsidiaries**

**Years Ended December 31,
1977 and 1976**

Statement of Consolidated Income

In Thousands of Dollars

	1977	1976
Revenues		
Insurance and financial	\$1,509,368	\$1,280,220
Manufacturing and housing	1,561,229	1,254,873
Total revenues	<u>3,070,597</u>	<u>2,535,093</u>
Expenses		
Insurance and financial		
Incurred losses and loss expenses	951,825	848,619
Underwriting expenses	421,530	351,602
Other expenses	27,882	25,085
Total insurance and financial	<u>1,401,237</u>	<u>1,225,306</u>
Manufacturing and housing		
Operating costs	1,183,648	948,551
Selling and general expenses	159,049	133,143
Depreciation and amortization	41,241	36,835
Interest and debt expense, net of amounts capitalized of \$4,252 and \$4,041	41,994	41,742
Total manufacturing and housing	<u>1,425,932</u>	<u>1,160,271</u>
Energy investments	21,865	20,221
Total expenses	<u>2,849,034</u>	<u>2,405,798</u>
Combined income from operations	221,563	129,295
Corporate administrative expense	13,368	11,958
Corporate interest and debt expense, net	48,238	39,344
Income taxes	61,065	22,434
Net (gains) losses on sales of securities,* net of income taxes of \$(126) and \$2,332	71	(6,486)
Minority interest and preferred dividends of subsidiary	16,298	12,845
Income from continuing operations	82,523	49,200
Loss from discontinued operations, net of income taxes of \$(3,267) (\$.24 per primary share; \$.14, diluted)	—	(4,947)
Net income	<u>\$ 82,523</u>	<u>\$ 44,253</u>
Primary net income per share	<u>\$ 3.01</u>	<u>\$ 1.37</u>
Net income per share—assuming full dilution	<u>\$ 2.29</u>	<u>\$ 1.29</u>

*Excludes unrealized appreciation (depreciation) of stocks of insurance companies of \$(23,406) and \$36,783.

See Summary of Accounting Policies and Financial Review.

**City Investing Company
and Subsidiaries**

December 31, 1977 and 1976

Consolidated Balance Sheet

In Thousands of Dollars

Assets	1977	1976
Current assets, excluding insurance and financial companies		
Cash and marketable securities	\$ 62,250	\$ 26,870
Accounts receivable, less allowances	200,340	151,880
Contracts receivable from homesite sales, net	24,035	24,638
Inventories	299,240	235,499
Other	31,572	25,741
	<hr/> 617,437	<hr/> 464,628
Investments of insurance and financial companies		
Bonds at amortized cost (quoted market \$1,138,841 and \$788,085)	1,164,671	833,425
Stocks at quoted market value (cost \$450,385 and \$395,866)	377,778	354,621
Mortgage loans	393,126	344,174
Cash and commercial paper	102,976	165,202
Real estate, less accumulated depreciation	89,596	89,766
Other	19,724	15,197
	<hr/> 2,147,871	<hr/> 1,802,385
Insurance premiums receivable	248,627	330,341
Prepaid insurance acquisition costs	211,493	228,823
Property, plant, equipment and capital leases, net	482,260	428,520
Other investments and long-term receivables		
Contracts receivable from homesite sales, net	114,750	129,394
Homesite land and improvements	69,682	67,899
Other	79,619	76,750
	<hr/> 264,051	<hr/> 274,043
Carrying amount over the equity in net assets of subsidiaries	451,020	449,404
Other assets	298,235	243,770
	<hr/>	<hr/>
Total assets	<hr/> \$4,720,994	<hr/> \$4,221,914

Liabilities and Shareholders' Equity	1977	1976
Current liabilities, excluding insurance and financial companies		
Notes payable	\$ 98,902	\$ 71,069
Accounts payable and accruals	193,449	155,130
Current maturities of long-term debt	42,703	44,522
Obligations under capital leases	3,261	2,759
Dividends payable	8,500	7,579
Estimated homesite improvement costs	17,355	14,445
Income taxes payable	25,197	14,346
	<hr/> 389,367	<hr/> 309,850
Reserves and liabilities of insurance and financial companies		
Unpaid losses and loss expenses	970,534	752,578
Unearned premiums	623,745	648,187
Savings accounts	307,259	267,309
Aggregate life reserves	135,490	122,774
Loans payable	32,040	33,200
Other	227,453	203,476
	<hr/> 2,296,521	<hr/> 2,027,524
Long-term debt	790,270	680,111
Obligations under capital leases	84,682	87,865
Deferred income taxes	166,906	160,679
Other liabilities and deferred income	38,412	34,295
Estimated homesite improvement costs	27,562	42,595
Minority interest	81,296	69,405
Convertible subordinated debentures	39,974	39,974
Preferred stock of subsidiary	50,000	50,000
Shareholders' equity		
Cumulative preference stocks	12,909	12,996
Common stock	29,134	29,042
Capital surplus	542,131	541,268
Unrealized depreciation of stocks held by insurance companies	(53,999)	(30,593)
Retained earnings	236,463	187,604
Cost of common stock in treasury	(10,634)	(20,701)
Total shareholders' equity	<hr/> 756,004	<hr/> 719,616
Total shareholders' equity and preferred stock of subsidiary	<hr/> 806,004	<hr/> 769,616
Total liabilities and shareholders' equity	<hr/> \$4,720,994	<hr/> \$4,221,914

Statement of Consolidated Retained Earnings	1977	1976
Balance at beginning of year, as originally reported		\$204,562
Prior years' restatement for changes in accounting practices		
Oil and gas investments		(23,626)
Leases		(3,658)
Adjustment for change in accounting for warranty costs		(4,212)
Balance at beginning of year, as restated and adjusted	\$187,604	173,066
Net income	82,523	44,253
	270,127	217,319
Dividends declared		
Cumulative preference stocks	16,028	16,109
Common stock, \$.80 and \$.66 per share	17,636	13,606
	33,664	29,715
Balance at end of year	\$236,463	\$187,604

Statement of Unrealized Depreciation of Stocks Held by Insurance Companies	1977	1976
Balance at beginning of year		
Depreciation based on quoted market prices	\$(41,245)	\$(87,416)
Income tax benefit resulting from excess of book basis of certain securities over tax basis	10,652	20,040
Net balance at beginning of year	(30,593)	(67,376)
Appreciation (depreciation) based on end of year quoted market, net of income taxes of \$8,548 and \$(8,822)	(19,976)	35,860
Effect of sale transactions during the year		
Appreciation (depreciation) at beginning of year	(2,838)	1,489
Income tax effect of book basis over tax basis	(592)	(566)
Net change during the year	(23,406)	36,783
Balance at end of year		
Depreciation based on quoted market prices	(72,607)	(41,245)
Income tax benefit resulting from excess of book basis of certain securities over tax basis	18,608	10,652
Net balance at end of year	\$(53,999)	\$(30,593)

**City Investing Company
and Subsidiaries**

**Years Ended December 31,
1977 and 1976**

In Thousands of Dollars

Statement of Changes in Consolidated Financial Position	1977	1976
Source of Funds		
Net income	\$ 82,523	\$ 44,253
Non-fund charges to income		
Increase in insurance reserves and change in premiums receivable and prepaid acquisition costs	305,274	174,497
Depreciation and amortization	41,241	36,835
Other	27,454	26,285
Funds provided from operations	456,492	281,870
Issuance of debentures (with common stock, \$10,910 and \$19,475)	100,000	125,000
Bank and other borrowings	139,434	37,614
Net increase in savings accounts and loans payable	24,746	18,717
Issuance of preference stock	—	5,000
Other, net	1,139	6,623
	<u>\$721,811</u>	<u>\$474,824</u>
Application of Funds		
Reduction of long-term debt	\$133,552	\$177,116
Cash dividends	33,664	29,715
Increase in investments of insurance and financial companies		
Bonds	331,246	78,756
Stocks	23,157	103,813
Mortgage loans	48,952	24,220
Other	(57,869)	62,095
	<u>345,486</u>	<u>268,884</u>
Unrealized (appreciation) depreciation of stocks held by insurance companies	31,362	(46,171)
Additions to property, plant and equipment	104,455	57,261
Energy investments	—	5,235
Increase (decrease) in working capital, excluding insurance and financial companies	73,292	(17,216)
	<u>\$721,811</u>	<u>\$474,824</u>
Working capital increase (decrease) by component		
Cash and marketable securities	\$ 35,380	\$ (24,862)
Inventories	63,741	29,567
Other current assets	53,688	23,960
Notes payable	(27,833)	(8,043)
Current maturities of long-term debt	1,819	(3,027)
Accounts payable and other current liabilities	(53,503)	(34,811)
	<u>\$ 73,292</u>	<u>\$ (17,216)</u>

City Investing Company and Subsidiaries

Summary of Accounting Policies and Financial Review

Principles of Consolidation. The consolidated financial statements include the accounts of all significant subsidiaries. The accounts of insurance subsidiaries and the savings and loan subsidiary are included as insurance and financial companies.

Amounts for 1976 have been restated to give effect to adoption of Statements of Financial Accounting Standards Nos. 13 and 19, "Accounting for Leases" and "Financial Accounting and Reporting by Oil and Gas Producing Companies," which require the capitalization of certain lease obligations and the use of a form of successful efforts accounting for oil and gas investments. As a result, net income, primary net income per share and net income per share—assuming full dilution, were restated and retroactively reduced by \$8,892,000, \$.43 and \$.25, respectively, for the year ended December 31, 1976.

The carrying amount over the equity in net assets of subsidiaries is not being amortized except where there is an indication of diminution in value or for amounts arising after October 31, 1970, which are being amortized over periods of 40 years or less. The amount being amortized at December 31, 1977 and 1976 was \$96,428,000 and \$95,693,000, respectively. Amortization amounted to \$3,083,000 in 1977 and \$3,390,000 in 1976.

All significant intercompany items are eliminated in consolidation. Amounts for 1976 have been reclassified to conform to the 1977 presentation.

Interest Capitalization. The Company follows the practice of capitalizing interest which constitutes an actual cost of certain properties. The amount capitalized represents the cost of borrowed funds utilized in acquiring and carrying real estate; in the construction of houses; and in the construction of motels. Charging such interest to expense would not have significantly affected net income.

Insurance Accounting. The insurance operations of the Company are conducted through its subsidiary, CityHome Corporation. Total revenues of CityHome were \$1,476,434,000 in 1977 and \$1,254,139,000 in 1976. Net income was \$75,038,000 and \$51,645,000 during the same respective periods. Net assets of CityHome were \$676,944,000 at December 31, 1977.

Unearned premiums and prepaid insurance acquisition costs are recognized in the statement of income ratably over the terms of the policies. The method followed in computing prepaid acquisition costs limits the amount of such capitalized costs to their estimated realizable value by giving effect to the losses and loss expenses expected to be incurred as the premium is earned.

Unpaid losses and loss expenses are based on case basis estimates for reported claims, and estimates, based on past experience, for unreported claims and loss expense. The provision for unpaid losses and loss expenses at December 31, 1977 and 1976, has been established to cover the net cost of insured losses. The amounts are necessarily based on estimates of future rates of inflation and other factors, and accordingly there can be no assurance that the ultimate liability will not exceed such estimates.

Investments in stocks are carried at quoted market value. Unrealized appreciation or depreciation is not reflected on the Company's income statement, but is shown as a separate component of shareholders' equity. Unrealized depreciation at December 31, 1977, before income tax benefit, reflects unrealized gains of \$8,913,000 and unrealized losses of \$81,520,000. Investments in bonds are carried at amortized cost. An identified certificate basis is used to determine cost of securities sold.

Real Estate Accounting. Homesite sales are made by the Company's 59% owned subsidiary, GDV, Inc., under nonrecourse instalment contracts which require payments over an average period of ten years. A sale is recorded when aggregate payments equivalent to 10% of the contract price have been received. The gross profit on recorded sales is deferred and recognized in income on a pro rata basis as payments of principal are received. Deferred profit amounted to \$83,413,000 and \$96,342,000 at December 31, 1977 and 1976, respectively. Costs and direct selling expenses are recorded at the time the sale is recognized. Sales of homesites are generally made in advance of the completion of land improvements. The costs of such improvements are accrued when the sale is recorded.

The Company has entered into an agreement with GDV, Inc. which provides for the purchase by GDV of the Company's wholly owned home building subsidiary, Wood Bros. Homes, Inc. Under terms of the agreement, the Company will receive a \$25,000,000 10% senior promissory note, which amount approximates its investment in Wood Bros. The transaction is subject to approval by the public stockholders of GDV, the Company having agreed to vote its shares in the same proportion as the shares voted by the public stockholders of GDV.

Inventories and Product Warranties. Inventories are stated at the lower of cost (generally first-in, first-out and average) or market. Year-end balances are summarized as follows:

In Thousands of Dollars	1977	1976
Raw materials and work in process	\$166,842	\$143,601
Finished goods	42,661	32,032
Subdivision land and houses	78,897	53,232
Homesite land, improvements and houses	10,840	6,634
	<u>\$299,240</u>	<u>\$235,499</u>

During 1976, the Company adopted the policy of accruing for costs expected to be incurred under product warranties. In prior periods such costs were charged to expense as incurred. Because the effect of this change was not material to prior periods, the amount of reserve necessary at December 31, 1975, after related income tax effect, was charged to retained earnings.

Property, Plant, Equipment and Capital Leases. Additions and major renewals and betterments which have the effect of extending the useful lives of property are carried at cost. Excluding capital leases and the effect of the consolidation of the Company's Singapore and English container operations in 1977 and 1976, respectively, gross additions amounted to \$104,455,000 in 1977 and \$57,261,000 in 1976. The Company follows the practice of amortizing investment tax credits. Depreciation is recorded principally on a straight-line basis over the estimated useful lives of the assets. Depreciation and amortization provisions, including amortization of capital leases, were \$38,006,000 and \$33,060,000. Year-end balances follow:

In Thousands of Dollars	1977	1976
Land and improvements	\$ 27,945	\$ 21,228
Buildings and leasehold improvements	313,167	287,337
Machinery and equipment	378,897	320,812
Accumulated depreciation and amortization	(237,749)	(200,857)
	<u>\$482,260</u>	<u>\$428,520</u>

In accordance with Financial Accounting Standards Board Statement No. 13, leases that transfer substantially all the benefits and risks incident to the ownership of property are considered capital leases and are now reflected as assets and liabilities in the balance sheet. Assets recorded under capital leases, primarily buildings and leasehold improvements of the Company's budget motel subsidiary, amounted to \$102,279,000 and \$101,678,000 at December 31, 1977 and 1976, respectively. Related accumulated amortization was \$24,885,000 and \$19,672,000. Minimum payments due under capital leases at December 31, 1977, are as follows:

In Thousands of Dollars	
Year ending December 31:	
1978	\$ 11,358
1979	11,329
1980	10,788
1981	10,434
1982	10,294
Thereafter	141,730
Total	<u>195,933</u>
Less imputed interest	107,990
	<u>\$ 87,943</u>

Other Investments. Energy investments are represented by participations in leases and concessions both within the United States and elsewhere (principally in Ecuador, Colombia, Egypt and the North Sea). In accordance with Financial Accounting Standards Board Statement No. 19 issued in December 1977, the Company adopted the successful efforts method of accounting for costs incurred in searching for and developing oil and gas reserves. The principal difference between the successful efforts method and the full cost method previously followed by the Company is in the accounting treatment of costs that cannot be directly related to the discovery of specific oil and gas reserves, and in the selection of the reserve base or cost center within which capitalized costs are grouped for amortization. Under the method previously followed by the Company, all costs incurred in searching for oil and gas reserves within a country were capitalized subject to the limitation that the total amount capitalized not exceed the fair value of the reserves in the country. Under the successful efforts method of accounting, only direct costs incurred in individual successful acquisitions and activities are capitalized. Other costs are expensed as incurred.

During 1977 and 1976, the Company incurred pretax losses of \$14,165,000 and \$19,471,000, respectively, in its oil and gas operations. During 1977, a pretax loss of \$7,700,000 was recognized in connection with the Company's discontinuance of its domestic coal operation. In 1976, a pretax loss of \$750,000 was recognized. The Company's interest in domestic proved developed gas reserves was 9,845 million cubic feet at December 31, 1977, and 11,501 million cubic feet at December 31, 1976. The Company's interest in proved developed oil reserves, principally foreign, was 17,162,000 barrels and 29,994,000 barrels. The carrying amount of energy investments was \$7,825,000 at December 31, 1977, net of long-term debt of \$18,275,000.

During 1974, the Company decided to discontinue and dispose of its real estate joint venture and bulk land sales operations. During 1976, as a result of increased estimates of disposal and carrying costs and the write-off of a mortgage note receivable, it was determined that an additional net of tax loss of \$4,947,000 should be recognized. The carrying amount of discontinued operations, \$37,585,000 at December 31, 1977, consists primarily of mortgages receivable and real estate, net of long-term debt of \$23,659,000.

Long-term Debt. Year-end summaries of long-term debt, exclusive of amounts due within one year, are as follows:

In Thousands of Dollars	Interest rate	1977	1976
Notes payable to banks under revolving credit agreement	6.75%	\$ —	\$ 51,000
Other bank borrowings	9.20%	114,143	81,000
Notes payable to institutional lenders	8.14%	215,869	230,362
Sinking fund debentures	9.04%	247,500	148,800
Notes secured by property and equipment, subdivision land and houses, and real estate	8.31%	59,346	59,545
Other	8.39%	93,567	40,730
		730,425	611,437
Subordinated debentures	8.07%	108,415	108,384
		838,840	719,821
Less unamortized discount		48,570	39,710
		<u>\$790,270</u>	<u>\$680,111</u>

The aggregate maturities of long-term debt during the five years subsequent to December 31, 1977, are as follows:

Year	1978	1979	1980	1981	1982
Amount	\$42,703	\$47,765	\$44,486	\$60,088	\$43,319
Unamortized discount	3,059	3,159	3,261	3,361	3,507

Interest rates represent average stated rates, except for the December 31, 1976, borrowing rate in effect under the parent company's revolving credit agreement, which was based on the prime lending rate. Unamortized discount is substantially attributable to subordinated and sinking fund debentures and the stated interest rates on those debentures are effectively increased by the amortization to interest expense of the discount as shown in the tabulation above.

The Company has complied with the customary restrictions and limitations required under terms of various loan agreements. Retained earnings not subject to restrictions at December 31, 1977, approximated \$75 million. Substantially all City's income consists of earnings of subsidiaries. Since the earnings of most subsidiaries are subject to restrictions imposed by debt instruments or applicable law on the amount of dividends that may be paid, these earnings are not necessarily immediately available to City.

Capital Stock. Authorized capital stock consists of 15,000,000 shares of \$1.00 par value cumulative preference stock issuable in series and 60,000,000 shares of \$1.25 par value common stock. Capital stock information as of December 31, 1977 and 1976, is summarized as follows:

	1977 Annual Dividend	Liquidation Preference	Common Stock Conversion Privilege	Dollars in Thousands			
				1977		1976	
				Shares	Amount	Shares	Amount
Common stock	\$.80	NA	NA	23,306,887	\$29,134	23,233,621	\$29,042
Preference Stock							
Series A	\$ 1.31	\$ 14.70	2.08 shs	80,978	\$ 202	114,655	\$ 287
Series B	2.00	40.00	1.56 shs	7,706,657	7,707	7,708,729	7,709
Series D	100.00	1,000.00	NA	5,000	5,000	5,000	5,000
					<u>\$12,909</u>		<u>\$12,996</u>

Common stock issued includes 847,081 and 1,648,981 treasury shares at December 31, 1977 and 1976, respectively. During 1977 and 1976, primarily in connection with the issuance of debentures, 801,900 and 1,504,562 shares carried at \$10,067,000 and \$19,626,000, were reissued. During 1976, 230,035 shares were reacquired at a cost of \$2,125,000.

Each share of cumulative preference stock is entitled to one vote. Series A and B are convertible into common stock, subject to customary anti-dilution adjustments. All preference shares are redeemable at the option of the Company as follows: series A, \$49.00; series B, \$40.50, declining to \$40.00 in 1978; series D, \$1,000.00. The series A shares are carried at their stated value of \$2.50 per share and the series D shares are carried at their liquidation value of \$1,000.00 per share. The preference in involuntary liquidation on all issued preference shares amounted to \$314,456,000 at December 31, 1977.

At December 31, 1977, there were 12,190,819 shares of common stock reserved for the conversion of preference stock, 2,914,938 shares reserved for issuance upon the conversion of outstanding debentures and warrants and 1,200,000 shares reserved for issuance under the Company's share unit plan.

A subsidiary of the Company, CityHome Corporation, is authorized to issue up to 10,000,000 shares of cumulative preferred stock, \$1.00 par value, of which 5,000,000 shares were outstanding at December 31, 1977 and 1976. This preferred stock is entitled to a sinking fund commencing December 1, 1986, sufficient to retire the preferred stock by December 1, 2005, has a stated annual dividend of \$1.10 per share, is redeemable for sinking fund purposes at \$10.00 per share plus accrued dividends and is currently redeemable at \$10.99 per share. Dividends on the CityHome preferred stock are reflected as minority interest in the statement of consolidated income.

Convertible Debentures and Warrants. The convertible subordinated debentures bear interest at 7½% and are convertible into common stock at \$16.50 per share. The debentures mature \$3,000,000 annually, 1980 to 1989, and are currently callable at 104½%. Warrants which expire on March 1, 1984, are outstanding to purchase 492,270 shares of common stock at \$27.30 per share. Warrants, which expire on July 15, 1983, are outstanding to purchase 2,040,000 shares of GDV, Inc. common stock from the Company at \$27.70 per share.

Share Unit Plan. The Company's share unit plan provides that participants receive, for each unit awarded, either common stock of the Company or cash equivalent to the increase in market value per share of the Company's common stock over an initial five-year period commencing on date of award. In addition, each participant's account is credited with dividend units equivalent to cash dividends on total units in their account on dividend payment dates. Compensation is recorded based on the increase in value of initial units awarded and the market value of accumulated dividend units. During 1977 and 1976, 187,643 and 305,373 units, respectively, were awarded, 107,259 and 118,544 dividend units were accumulated, and 124,291 and 215,489 units were cancelled or matured. At December 31, 1977, 1,964,580 units were outstanding.

Earnings Per Share. Primary earnings per share are calculated by dividing income, after deducting dividends on the series B and D preference stocks, by the weighted average of common and common equivalent shares outstanding during the year, 22,097,000 in 1977 and 20,642,000 in 1976. The cumulative preference stock convertible series A is included as a common stock equivalent.

Fully diluted earnings per share are calculated by dividing income, after adding back interest net of the income tax effect on debentures assumed converted and after deducting dividends on the series D preference stock, by the weighted average common and common equivalent shares outstanding during the year, with the assumption that outstanding convertible debentures and the series B preference stock were converted at the beginning of the year. Such shares averaged 36,543,000 in 1977 and 35,091,000 in 1976.

Investment Income. Components of investment income reflected in revenues of insurance and financial companies were as follows:

In Thousands of Dollars	1977	1976
Interest income		
Taxable bond income	\$ 52,178	\$ 44,022
Nontaxable bond income	26,028	23,330
Mortgage income	33,225	28,689
	<hr/> 111,431	<hr/> 96,041
Dividend income	20,802	17,391
Net real estate income	3,493	2,027
Other	1,352	(415)
	<hr/> \$137,078	<hr/> \$115,044

Taxable bond income and mortgage income include \$47,917,000 in 1977 and \$41,789,000 in 1976 from life insurance and savings and loan subsidiaries, and the tax rate on these amounts is effectively reduced from the normal tax rate as a result of allocations of income to policyholders' surplus and general reserves.

Income Taxes. Provisions for income taxes applicable to income from continuing operations, exclusive of net (gains) losses on sales of securities, amounted to \$61,065,000 in 1977 and \$22,434,000 in 1976. Such provisions include state income taxes of \$7,268,000 and \$4,998,000 and foreign taxes of \$22,261,000 and \$14,678,000. Income tax expense would have been \$76,779,000 in 1977 and \$37,437,000 in 1976 if the statutory ordinary Federal rate of 48% had been required. Reductions from those amounts were \$20,844,000 and \$18,186,000 attributable to tax-free interest and 85% dividends received deduction; offset by \$3,779,000 and \$2,599,000 attributable to state income taxes, net of Federal benefit, and \$1,351,000 and \$584,000 of miscellaneous items.

The source and income tax effects, primarily Federal, of timing differences between book and taxable income were as follows:

In Thousands of Dollars	1977	1976
Statutory voluntary reserve adjusted for inclusion in the financial statements	\$ (2,000)	\$ (7,900)
Reduction of prepaid insurance acquisition costs for book purposes	(8,300)	(4,800)
Community development subsidiary, primarily from use of instalment accounting practices	(1,000)	(3,800)
Recoverable amounts accrued in the financial statements on insurance claims paid	6,400	(100)
Deferred investment tax credits	9,200	(1,000)
Tax depreciation in excess of book depreciation	4,000	1,300
Statutory reinsurance contracts adjusted for inclusion in the financial statements	—	5,400
Miscellaneous items, net	3,000	700
Tax effect of timing differences	\$ 11,300	\$ (10,200)

Pension Plans. Pension plans are in effect which cover substantially all employees who meet eligibility requirements. Actuarial assumptions of the respective plans are generally standardized and equity securities of the joint trust are valued at a three-year average of quoted market.

Provisions charged against income include normal cost plus interest on unfunded past service costs and include amortization of prior service costs over 30 years. Total expense under pension plans was \$15,358,000 in 1977 and \$12,250,000 in 1976. Subsequent to the inception of the plans, it has been the policy of the Company generally to fund amounts provided. As of December 31, 1977, the unfunded past service liability based on actuarial estimates was approximately \$72 million and the present value of unfunded vested benefits was approximately \$28 million.

Information About Segments of the Company's Operations. Information about the Company's operations in different industries as of and for the year ended December 31, 1977, follows:

In Thousands of Dollars	Revenues	Operating profit	Income from operations	Depreciation and amortization	Assets	Capital expenditures
Insurance	\$1,473,611	\$ 97,715	\$ 97,715	\$ —	\$2,715,961	\$ —
International manufacturing	393,223	44,854	35,922	8,772	285,570	23,212
Housing and community development	367,363	40,396	34,151	6,315	566,986	13,078
Air conditioners and water heaters	269,934	30,876	24,444	2,269	171,171	4,730
Magazine printing	193,851	18,485	15,032	7,600	118,527	24,935
Containers	128,031	17,131	14,657	3,100	82,098	3,483
Budget motels	75,111	23,907	11,467	9,425	187,837	27,035
Savings and loan	34,405	10,140	10,140	—	381,879	—
Energy investments	—	(21,865)	(21,865)	—	7,825	—
Other operations	135,068	1,918	(100)	3,760	134,779	7,982
Combined	\$3,070,597	\$263,557	\$221,563	\$41,241	\$4,652,633	\$104,455

Operating profit represents revenues less all operating expenses except interest expense. Income from operations represents revenues less all operating expenses including interest expense. Additional items included in the determination of consolidated net income are reflected in the Statement of Consolidated Income. Depreciation and amortization included in the determination of operating profit reflects, where applicable, the amortization of carrying amount over equity in net assets.

Assets reflected for the respective segments include, where applicable, the carrying amount over equity in net assets. A reconciliation of combined total assets and consolidated assets appearing in the accompanying balance sheet as of December 31, 1977, follows:

In Thousands of Dollars

Combined total assets	\$4,652,633
Corporate assets	30,776
Discontinued operations	37,585
Consolidated assets	<u>\$4,720,994</u>

Information about the Company's operations in different geographic areas as of and for the year ended December 31, 1977, follows:

In Thousands of Dollars	Revenues	Operating Profit	Income from Operations	Assets
United States	\$2,552,168	\$216,531	\$183,469	\$4,196,708
Foreign countries				
Insurance	125,206	12,715	12,715	151,137
Energy investments	—	(10,543)	(10,543)	19,218
International manufacturing	393,223	44,854	35,922	285,570
Combined	<u>\$3,070,597</u>	<u>\$263,557</u>	<u>\$221,563</u>	<u>\$4,652,633</u>

International manufacturing operations are conducted principally in Western Europe, Brazil and Mexico. Principal products include containers, water heaters, leaf springs and plastic products.

Contingent Liabilities and Other Matters. Various lawsuits are pending against the Company including five lawsuits alleged to be class actions brought against the Company in its capacity as advisor to two real estate investment trusts alleging violations of the Federal securities laws. In the opinion of counsel such lawsuits will not result in a material liability to the Company.

Unaudited summaries of replacement cost data and quarterly results of operations are contained in Management's Discussion and Analysis of Summary of Operations.

**City Investing Company
and Subsidiaries**

**Five Years Ended
December 31, 1977**

**Revenues and Income
from Operations
by Major Product and Service
Group—Unaudited**

In Millions of Dollars

Revenues	1973	1974	1975	1976	1977
Insurance	\$ 922.0	\$ 973.2	\$1,013.8	\$1,253.4	\$1,473.6
International manufacturing (2)	147.5	224.5	242.2	332.9	393.2
Housing and community development	437.3	356.5	264.1	283.2	367.4
Air conditioners and water heaters	147.7	163.4	160.9	220.4	269.9
Magazine printing	94.1	122.8	138.4	154.8	193.9
Containers	83.9	111.1	101.6	110.9	128.0
Budget motels	27.0	39.6	53.7	63.0	75.1
Savings & loan	18.6	20.9	23.9	27.3	34.4
Energy investments	—	—	—	—	—
Other operations	113.0	120.6	106.2	89.2	135.1
Total Revenues	<u>\$1,991.1</u>	<u>\$2,132.6</u>	<u>\$2,104.8</u>	<u>\$2,535.1</u>	<u>\$3,070.6</u>
Combined Income from Operations (3)	1973	1974	1975	1976	1977
Insurance	\$ 78.6	\$ 29.9	\$ 25.7	\$ 51.0	\$ 97.7
International manufacturing (2)	17.8	24.5	17.0	24.8	35.9
Housing and community development	17.7	13.3	10.1	18.7	34.2
Air conditioners and water heaters	14.2	15.6	15.1	20.2	24.4
Magazine printing	6.0	8.9	10.5	12.7	15.0
Containers	8.7	20.1	8.9	11.2	14.7
Budget motels	1.2	(.1)	1.2	6.6	11.5
Savings & loan	3.1	2.3	3.7	5.3	10.1
Energy investments	(14.9)	(10.7)	(21.3)	(20.2)	(21.9)
Other operations	3.7	7.2	7.7	(1.0)	—
Combined Income from Operations (4)	<u>\$ 136.1</u>	<u>\$ 111.0</u>	<u>\$ 78.6</u>	<u>\$ 129.3</u>	<u>\$ 221.6</u>

(1) Revenues and income from operations for 1976 and prior periods have been restated and reclassified to conform to the 1977 presentation. Insurance includes the Company's property and casualty and life insurance operations. The Company's mobile home, community development (GDV, Inc.) and conventional housing operations are included in housing and community development. International manufacturing, whose products include containers, water heaters, leaf springs and plastics, are conducted principally in Western Europe, Brazil and Mexico. Other operations include City's refrigeration, plastics and aircraft modification activities, as well as C.I. Planning Corporation, the advisor to two real estate investment trusts.

(2) During the years indicated, the following International manufacturing operations were consolidated (prior to consolidation, these operations were carried as equity investments): 1974, Mexico; 1976, England; 1977, Singapore. The consolidation of these operations added \$23.9 million, \$42.0 million and \$15.8 million to revenues, and \$1.1 million, \$1.9 million and \$1.3 million to income from operations in the years indicated.

(3) Income from operations represents revenues less all operating expenses including interest expense. See information about segments of the Company's operations on page 33 herein for 1977 amounts exclusive of interest expense and for additional 1977 data (depreciation and amortization, assets and capital expenditures) by major product and service group.

(4) See Summary of Operations on page 36 herein for additional items included in the determination of net income.

**City Investing Company
and Subsidiaries**

**Five Years Ended
December 31, 1977**

Summary of Operations

In Millions of Dollars

	1973	1974	1975	1976	1977
Revenues					
Insurance and financial	\$ 940.7	\$ 993.0	\$1,038.1	\$1,280.2	\$1,509.4
Manufacturing and housing	1,050.4	1,139.6	1,066.7	1,254.9	1,561.2
Total revenues	1,991.1	2,132.6	2,104.8	2,535.1	3,070.6
Expenses					
Insurance and financial	861.6	962.8	1,009.0	1,225.3	1,401.2
Manufacturing and housing					
Operating costs	796.6	848.3	797.2	948.6	1,183.6
Interest and debt expense, net of amounts capitalized of \$8.0, \$7.3, \$4.6, \$4.0 and \$4.3	26.0	44.1	43.5	41.7	42.0
Other expenses	155.9	155.8	155.2	170.0	200.3
Total manufacturing and housing	978.5	1,048.2	995.9	1,160.3	1,425.9
Energy investments	14.9	10.6	21.3	20.2	21.9
Total expenses	1,855.0	2,021.6	2,026.2	2,405.8	2,849.0
Combined income from operations	136.1	111.0	78.6	129.3	221.6
Corporate administrative expense	9.2	10.9	9.1	12.0	13.4
Corporate interest and debt expense, net	35.1	42.8	42.7	39.3	48.2
Income taxes	28.1	7.9	(3.9)	22.4	61.1
Net (gains) losses on sales of securities* (B)	(13.4)	7.9	(4.7)	(6.5)	.1
Minority interest and, in 1976 and 1977, preferred dividends of subsidiary	6.6	7.7	7.2	12.9	16.3
Income from continuing operations	70.5	33.8	28.2	49.2	82.5
Discontinued operations (B)	.5	(4.5)	(3.3)	(4.9)	—
Cumulative effect of change in accounting for catastrophe reserve (B)	—	—	8.8	—	—
Net income	71.0	29.3	33.7	44.3	82.5
Dividends on preferred stock, other than common equivalent shares	(15.4)	(15.4)	(15.4)	(16.0)	(15.9)
Net income applicable to common and common equivalent shares	\$ 55.6	\$ 13.9	\$ 18.3	\$ 28.3	\$ 66.6

	1973	1974	1975	1976	1977
Net income per share (C)					
Primary	\$ 2.40	\$.66	\$.89	\$ 1.37	\$ 3.01
Fully diluted	\$ 1.93	\$.87	\$ 1.01	\$ 1.29	\$ 2.29
Average shares (in thousands)					
Primary	23,136	21,036	20,549	20,642	22,097
Fully diluted	37,585	35,485	34,997	35,091	36,543
Common stock cash dividends	\$.58½	\$.66	\$.66	\$.66	\$.80

* Excludes unrealized appreciation (depreciation) of stocks of \$(63.1), \$(74.9), \$53.7, \$36.8 and \$(23.4) for the five years ended December 31, 1977.

(A) The accounting policies followed by the Company are described in the Summary of Accounting Policies and Financial Review beginning on page 28.

(B) Income taxes applicable to net (gains) losses on sales of securities were \$(5.8), \$3.6, \$(1.9), \$(2.3) and \$.1 for the five years ended December 31, 1977. Income taxes applicable to discontinued operations were \$11.0, \$(2.6), \$(3.1) and \$(3.3) for the four years ended December 31, 1976, and those applicable to the 1975 accounting change were \$8.2.

(C) Earnings per share related to discontinued operations were:

	1973	1974	1975	1976	1977
Primary	\$.02	\$ (.21)	\$ (.16)	\$ (.24)	—
Fully diluted	\$.01	\$ (.13)	\$ (.09)	\$ (.14)	—

Primary earnings per share applicable to the 1975 accounting change were \$.43 and fully diluted earnings per share were \$.25.

Management's Discussion and Analysis of Summary of Operations

This discussion and analysis is limited to a general review of material changes in the various revenue and expense items appearing on the Summary of Operations beginning with the years 1975 and 1976. Generally, a change in a revenue or expense item is commented on if it involves a change of more than 10% as compared with the prior period and a change of more than 2% of the average net income for the three most recent years presented.

The relative contributions to total revenues and combined income from operations of major product and service groups for the five years ended December 31, 1977, are set forth on page 35.

Accounting Changes. Results of operations for the four years ended December 31, 1976, have been restated and retroactively reduced to give effect to adoption of Statements of Financial Accounting Standards Nos. 13 and 19, "Accounting for Leases" and "Financial Accounting and Reporting by Oil and Gas Producing Companies," which require the capitalization of certain lease obligations and the use of a form of successful efforts method of accounting for oil and gas investments. The effect of the restatement is summarized as follows:

	1973	1974	1975	1976
Net income (in millions)	\$ (3.8)	\$ (5.4)	\$ (11.8)	\$ (8.9)
Primary net income per share	\$ (.17)	\$ (.26)	\$ (.58)	\$ (.43)
Net income per share assuming full dilution	\$ (.10)	\$ (.15)	\$ (.34)	\$ (.25)

In March 1975, the Financial Accounting Standards Board issued Statement No. 5, which provides that insurance companies may no longer maintain reserves for catastrophes. The Company's catastrophe reserve was discontinued as of January 1, 1975, and the cumulative effect, \$8.8 million, was included in 1975 net income. The effect on net income of periods prior to 1975, assuming retroactive application of the change, is not significant.

Total Revenues. For the years ended December 31, 1976 and 1977, respectively, total revenues increased \$430.3 million (20%) and \$535.5 million (21%). Insurance and financial revenue increases of 23% in 1976 and 18% in 1977 were primarily attributable to premium rate increases and, in 1977, increased writings in the Company's property and casualty insurance operations. Manufacturing and housing revenues increased 18% in 1976 and 24% in 1977, attributable to increased housing starts, increased unit shipments in City's major domestic manufacturing businesses, particularly in its heating and air conditioning operations, and, in 1977, increased production from new printing contracts in City's magazine printing operation. Total revenues in 1976 also increased as a result of the consolidation of City's English container operation, which previously had been carried as an equity investment. The consolidation added \$42.0 million to revenues and had no effect on net income.

Total Expenses. For the years ended December 31, 1976 and 1977, respectively, total expenses increased \$379.6 million (19%) and \$443.2 million (18%). Insurance and financial expenses increased 21% in 1976 and 14% in 1977 primarily as a result of increases of 24% and 12% in incurred losses and loss expenses reflecting a higher cost per claim, primarily attributable to inflation. Underwriting expenses increased 16% in 1976 and 20% in 1977 attributable to increased premium volume. Manufacturing and housing expenses increased 17% in 1976 and 23% in 1977 including increases in operating costs of 19% and 25%, respectively, reflecting increased unit shipments and production, and increased cost of materials and labor resulting from inflation. Other manufacturing and housing expenses increased 10% in 1976 and 18% in 1977 reflecting increased selling and general expenses resulting from increased sales.

Corporate Administrative Expense. Corporate administrative expense increased \$2.9 million (31%) in 1976 primarily as a result of higher charges under City's share unit program, reflecting increased market value of City's common stock. During 1977, corporate administrative expense increased \$1.4 million (12%) reflecting increased employee costs.

Corporate Interest and Debt Expense. During 1977, corporate interest and debt expense increased \$8.9 million (23%) reflecting the higher effective levels of recent long-term borrowings and increased borrowing levels.

Income Taxes. For the years ended December 31, 1976, and 1977, respectively, the effective income tax rate applicable to income from continuing operations, exclusive of net (gains) losses on sales of securities, was 28.8% and 38.2%. The increase in the effective income tax rate reflects significant increases in pretax income, while the level of tax-free interest and dividend income did not increase proportionately.

Net (Gains) Losses on Sales of Securities. Principally as a result of recovery in stock market conditions, 1976 sales of securities resulted in net capital gains of \$6.5 million. During 1977, sales of securities resulted in net capital losses of \$.1 million as unrealized depreciation increased \$23.4 million. Unrealized appreciation or depreciation of stocks is shown as a separate component of shareholders' equity and is not included in the determination of net income. Realization of income or loss on sales of securities is, to a certain extent, within the control of management, which determines the timing and selection of securities sold.

Minority Interest and Preferred Dividends of Subsidiary. Minority interest increased \$5.7 million in 1976 as a result of the inclusion of dividends on CityHome Corporation preferred stock issued in December, 1975. Preferred dividends of CityHome represent a minority interest in the net income of CityHome and are deducted in arriving at consolidated net income of City. In 1977, minority interest increased \$3.4 million (27%) reflecting the consolidation of City's partially-owned Singapore operation, which previously had been carried as an equity investment, and increased net income of partially-owned consolidated operations, particularly Mexico and the United Kingdom.

Discontinued Operations. During 1975, an after-tax charge of \$3.3 million was made as a result of an increase in estimated disposal and carrying costs related to City's real estate joint venture and bulk land sales operations, which previously had been discontinued. During 1976, it was determined that an additional after-tax loss of \$4.9 million should be recognized as a result of a further increase in estimated disposal and carrying costs and the write-off of a mortgage note receivable.

Unaudited Quarterly Summary of Operations. The following Summary of Operations for the four quarters of 1977 and 1976 is unaudited but, in the opinion of City's management, all adjustments, consisting only of normal recurring accruals, necessary for a fair presentation of the interim periods presented have been included.

1977 (In Thousands of Dollars)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Revenues				
Insurance and financial	\$345,724	\$366,989	\$389,714	\$406,941
Manufacturing and housing	342,079	378,563	424,628	415,959
Total revenues	687,803	745,552	814,342	822,900
Expenses				
Insurance and financial	329,558	345,320	359,992	366,367
Manufacturing and housing				
Operating costs	260,832	286,021	322,813	313,982
Interest and debt expense, net	10,317	10,815	10,481	10,381
Other expenses	45,378	48,323	53,773	52,816
Total manufacturing and housing	316,527	345,159	387,067	377,179
Energy investments	2,330	4,384	4,420	10,731
Total expenses	648,415	694,863	751,479	754,277
Combined income from operations	\$ 39,388	\$ 50,689	\$ 62,863	\$ 68,623
Net income	\$ 11,976	\$ 18,294	\$ 23,928	\$ 28,325
Primary net income per share	\$.37	\$.65	\$.91	\$ 1.08
Net income per share—assuming full dilution	\$.34	\$.51	\$.66	\$.78

Unaudited Quarterly Summary of Operations (continued)

1976 (In Thousands of Dollars)

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Revenues				
Insurance and financial	\$292,984	\$313,872	\$332,907	\$340,457
Manufacturing and housing	274,601	303,788	316,805	359,679
Total revenues	567,585	617,660	649,712	700,136
Expenses				
Insurance and financial	290,889	306,940	316,514	310,963
Manufacturing and housing				
Operating costs	206,212	228,407	240,654	273,278
Interest and debt expense, net	9,769	10,388	10,317	11,268
Other expenses	38,323	40,003	41,055	50,597
Total manufacturing and housing	254,304	278,798	292,026	335,143
Energy investments	3,287	3,277	7,598	6,059
Total expenses	548,480	589,015	616,138	652,165
Combined income from operations	\$ 19,105	\$ 28,645	\$ 33,574	\$ 47,971
Net income	\$ 6,931	\$ 6,460	\$ 10,927	\$ 19,935
Primary net income per share	\$.14	\$.12	\$.34	\$.77
Net income per share—assuming full dilution	\$.21	\$.19	\$.31	\$.58

Amounts for the first three quarters of 1977 and for the 1976 quarters have been restated to give retroactive effect to changes in accounting for oil and gas investments and leases. As a result of these changes, net income for the first three quarters of 1977 was restated and retroactively increased by \$476,000, \$2,324,000 and \$916,000, respectively. For the respective quarters, primary net income per share increased by \$.03, \$.10 and \$.04 and net income per share—assuming full dilution increased by \$.02, \$.06 and \$.02. For the 1976 quarters, net income was restated and retroactively reduced by \$2,077,000, \$1,534,000, \$4,169,000 and \$1,112,000; primary net income per share was reduced by \$.10, \$.08, \$.20 and \$.05; and net income per share—assuming full dilution was reduced by \$.05, \$.05, \$.13 and \$.02.

Included in 1977 net income are net gains (losses) on sales of securities of \$550,000, \$-0-, \$(635,000) and \$14,000 during the four respective quarters. Amounts for 1976 were \$4,709,000, \$1,887,000, \$(478,000) and \$368,000. Second quarter 1976 results reflect a net of tax loss of \$4,947,000 from discontinued operations. During 1977 and 1976, the Company consolidated its Singapore and English container operations which previously had been carried as equity investments. The consolidation of Singapore in 1977 and England in 1976 added \$15,768,000 and \$42,016,000 to revenues and \$1,262,000 and \$1,971,000 to combined income from operations, respectively, and had no effect on net income.

Caution should be exercised in comparing the results of consecutive interim periods since many of City's businesses are seasonal. Absent unusual circumstances, City's manufacturing group, particularly its air conditioning and container operations, typically report higher second and third quarter revenues and income than first and fourth quarter results. Mobile home shipments, conventional house closings and motel occupancy levels are also strongest during the second and third calendar quarters. Generally, with the absence of severe storms and the normal high level of premiums earned compared with premiums written, third and fourth quarter underwriting results are more favorable than during the first two quarters.

Unaudited Replacement Cost Information. The manufacturing and housing operations of the Company have generally been able to compensate for cost increases by increasing sales prices in an amount sufficient to maintain an approximately constant gross profit percentage on sales.

Although the cumulative impact of inflation over a number of years has resulted in higher costs for replacement of existing plant and equipment, such inflationary increases have partially been offset by technological improvements and design changes which often result in increasing the productivity of the newer asset additions.

The Company's annual report on Form 10-K (a copy of which is available upon request) contains specific information with respect to years 1977 and 1976 replacement cost of inventories and productive capacity (generally buildings, machinery, and equipment), and the approximate effect which replacement cost would have had on operating costs and depreciation expense for those years.

**City Investing Company
Operating Groups**

Insurance

The Home Insurance Company, New York, New York
President: Robert H. Tullis, Jr.

Federal Home Life Insurance Company, Battle Creek, Michigan
President: Albert C. Trussell

International Manufacturing

Rheem International, Inc., New York, New York
President: James V. Risk

Housing & Community Development

GDV, Inc., Miami, Florida
President: Peter C. R. Huang

Wood Bros. Homes, Inc., Denver, Colorado
President: William H. Tucker

General Development Corporation, Miami, Florida
President: Louis E. Fischer

Guerdon Industries, Inc., Louisville, Kentucky
President: William S. Goodfellow

U.S. Manufacturing and Printing

Rheem Air Conditioning Division, Fort Smith, Arkansas
President: Robert B. Gilbert

Rheem Water Heater Division, Chicago, Illinois
President: Albert F. Hurley, Jr.

World Color Press, Inc., Effingham, Illinois
President: N. Clyde Oberlin

Rheem Container Division, Linden, New Jersey
President: Carl W. Dinger

Revco, Inc., West Columbia, South Carolina
President: Daniel B. Dawley

Alma Plastics Company, Alma, Michigan
President: Leo Fleming

Hayes International Corporation, Birmingham, Alabama
President: Willis C. Hagan, Jr.

Budget Motels

Motel 6, Inc., Santa Barbara, California
President: Daniel R. Shaughnessy

Savings and Loan

Southern California Savings and Loan Association, Los Angeles, California
President: Kenneth D. Childs, Jr.

Energy

City Exploration Company, Houston, Texas
Executive Vice President: Victor R. Williams

Corporate Data

Corporate Offices

767 Fifth Avenue, New York, New York 10022
9100 Wilshire Boulevard, Beverly Hills, California 90212

European Office

Stockerstrasse 38, 8002 Zurich, Switzerland

Independent Auditors

Peat, Marwick, Mitchell & Co.

Transfer Agents

Common Stock and Series A Preference Stock:
Chemical Bank, 55 Water Street, New York, New York 10041

Common Stock and Series B Preference Stock:
Bank of America, N.T. & S.A.
P.O. Box 3415, San Francisco, California 94120
Continental Illinois National Bank & Trust Co. of Chicago
231 S. LaSalle Street, Chicago, Illinois 60690

Series B Preference Stock:
Citibank, N.A.
111 Wall Street, New York, New York 10015

7½% Convertible Subordinated Debentures:
Marine Midland Bank
250 Park Avenue, New York, New York 10017

8% and 8½% Subordinated Debentures:
Citibank, N.A.
111 Wall Street, New York, New York 10015

8⅞% Sinking Fund Debentures:
First National Bank of Boston
P.O. Box 1897, Boston, Massachusetts 02105

9% and 9⅞% Sinking Fund Debentures:
Manufacturers Hanover Trust Company
Corporate Trust Department
40 Wall Street, New York, New York 10015

Securities Listed

New York Stock Exchange (Common, Series A & B Preference,
7½% Convertible Subordinated Debentures, 8%, 8½%
Subordinated Debentures, 8⅞%, 9% and 9⅞% Sinking Fund Debentures)

Midwest Stock Exchange (Common, Series B Preference)
Pacific Stock Exchange (Common, Series B Preference)
Amsterdam Stock Exchange (Common)
Brussels and Antwerp Stock Exchanges (Common)
London Stock Exchange (Common, Series B Preference)
Zurich, Geneva, Lausanne and Basle Stock Exchanges (Common)

Shareholder Information

Dividend Investment Plan City Investing Company provides a plan which allows shareholders to invest their cash dividends in City's Common Stock without paying brokerage commissions, bank service charges or termination charges. Additional shares may also be purchased by plan participants with the same savings in outside charges. For information about the plan, shareholders of Common and Series A and B Preference Stock are encouraged to write City Investing Company, Shareholder Services Department, P.O. Box 3192, Church Street Station, New York, New York 10008.

Additional Information Shareholders may obtain additional information about City investing, including the Company's annual report on Form 10-K, which includes separate financial statements of CityHome Corporation, as filed with the Securities and Exchange Commission, by communicating with the nearest City office:

Thomas E. Fuszard
Assistant Vice President
City Investing Company
9100 Wilshire Blvd.
Beverly Hills, Ca. 90212
(213) 278-2690

Jerome Hanan
Vice President
City Investing, S.A.
Stockerstrasse 38
8002 Zurich, Switzerland
(01) 36-40-90

Thomas E. McDonnell
Assistant Vice President
City Investing Company
767 Fifth Avenue
New York, N.Y. 10022
(212) 759-5300

Summary of Dividends and Stock Prices

Common Stock: Quarterly cash dividends of 1976 were paid at a rate of 16½ cents per share a total of 66 cents per share for the year. In 1977, dividends paid were 16½ cents in the first quarter and 20 cents a share in the last three quarters, for a total of 76½ cents for the year.

Preference Stocks: Series A and Series B Preference Stock dividends paid for each quarter of both 1976 and 1977 were 32¾ cents and 50 cents per share, respectively, for totals of \$1.31 and \$2.00 per share in both years.

Class of Stock	First Quarter		Second Quarter		Third Quarter		Fourth Quarter	
	High	Low	High	Low	High	Low	High	Low
1976								
Common	11⅝	7	11⅝	8⅞	11⅜	9¼	14¼	10⅞
Series A	23	15	21½	18⅞	23¾	19¾	27¾	21½
Series B	22	16½	21½	19½	23¼	20⅞	26¼	21⅝
1977								
Common	15⅞	12½	16¼	13½	16⅞	12¼	14¼	11⅞
Series A	29¾	28	31½	28¾	31½	27	26½	26¼
Series B	28¼	24⅜	27¾	24⅝	27⅞	24	26	23⅞

1978 Annual Meeting The annual meeting of shareholders of City Investing Company will be held at The Home Insurance Company, 3000 Goffs Falls Road, Manchester, New Hampshire at 11:00 a.m. on Friday, May 19, 1978. Commencing at 10:00 a.m., the Company will hold a shareholder information session, including a review of Company operations and a question and answer period.

Officers and Directors

Officers

Geo. T. Scharffenberger, Chairman & Chief Executive Officer
Peter C. R. Huang, President
Stephen E. O'Neil, President
Daniel E. Lyons, Executive Vice President & Chief Financial Officer
Edward P. Sheridan, Senior Vice President
David Fain Brown, Vice President & General Counsel
Joseph L. DeMieri, Vice President & Controller
John C. Herndon, Vice President—Corporate Communications
John J. McHugh, Vice President & Secretary
Lester J. Mantell, Vice President & Director of Taxes
Frank R. Moothart, Vice President
John J. Quirk, Vice President & Treasurer
Miles P. Shanahan, Vice President
Thomas E. Fuszard, Assistant Vice President & Director—Investor Relations
Joseph C. Kaminski, Assistant Vice President
Thomas E. McDonnell, Assistant Vice President & Director—Advertising & Public Relations
Timothy P. Reames, Assistant Vice President & Assistant General Counsel
Richard A. Williamson, Assistant Vice President
Virginia R. Ortleb, Assistant to the Chairman
Wendell H. Bautz, Assistant Secretary
James N. Castleberry, Assistant Controller
Mauno Rydell, Assistant Treasurer
Catherine A. Wahl, Assistant Secretary

Directors

Arthur C. Babson, Vice President, Babson's Reports, Inc., Investment advisors(1)(3)
Kenneth E. Black, Director & former Chairman, The Home Insurance Company
F. L. Cappaert, Cappaert Enterprises, Private investment company
Edwin I. Hatch, Chairman, Georgia Power Company(3)
Peter C. R. Huang, President
Daniel E. Lyons, Executive Vice President & Chief Financial Officer
Stephen E. O'Neil, President
Eben W. Pyne, Senior Vice President, Citibank, N.A.(1)(2)(3)
Geo. T. Scharffenberger, Chairman & Chief Executive Officer(1)
Elliot H. Stein, President, Scherck, Stein & Franc, Inc., Investment banking(1)(2)
Fred R. Sullivan, Chairman, President & Chief Executive Officer, Walter Kidde & Company, Inc.(2)
A. Lightfoot Walker, Chairman of the Executive Committee(1)
John H. Washburn, Chairman of the Executive Committee, The Home Insurance Company(1)

Advisory Committee to the Board

Sir David Barran, Director & former Chairman, Shell Transport & Trading Company
John L. Gibbons, former Advisor to Fiduciary Division, Chemical Bank
Lewis F. Jeffers, Chairman, Hayes International Corporation
Earle M. Jorgensen, Chairman of the Board, Earle M. Jorgensen Company
Roswell Messing, Jr., Chairman of the Executive Committee, World Color Press, Inc.

(1) Member of the Executive Committee

(2) Member of the Accounting and Audit Committee

(3) Member of the Compensation and Retirement Committee

