

CAUTIONARY NOTICE REGARDING FORWARD-LOOKING INFORMATION

This web site may contain forward-looking statements that are intended to enhance the reader's ability to assess the future financial and business performance of Liberty Mutual Group ("LMG" or the "Company"). Forward-looking statements include, but are not limited to, statements that represent the Company's beliefs concerning future operations, strategies, financial results or other developments, and contain words and phrases such as "may," "expects," "should," "believes," "anticipates," "estimates," "intends" or similar expressions. Because these forward-looking statements are based on estimates and assumptions that are subject to significant business, economic and competitive uncertainties, many of which are beyond the Company's control or are subject to change, actual results could be materially different.

Such forward-looking statements should be regarded solely as the Company's current plans, estimates and beliefs. The Company does not intend, and does not undertake, any obligation to update any forward-looking statements to reflect future events or circumstances after the date of such statements.

Please refer to Risk Factors below for a discussion of the various factors that could cause an adverse effect on the business, operations and financial condition of the Company.

RISK FACTORS

The Company's business, operations and financial condition are subject to various risks. Some of these risks are described below. This section does not describe all risks applicable to the Company, the Company's industry or its business and it is intended only as a summary of certain material factors.

The Company's business could be harmed because its potential exposure to asbestos and environmental ("A&E") claims and related litigation is very difficult to predict.

The Company has exposure to A&E related claims that emanate principally from general liability policies written prior to the mid-1980's. Asbestos claims relate primarily to injuries asserted by those who allegedly came in contact with asbestos or products containing asbestos. Environmental claims relate primarily to pollution and related clean-up cost obligations, particularly as mandated by federal and state environmental protection agencies. The process of establishing reserves for A&E claims is subject to greater uncertainty than the establishment of reserves for liabilities relating to other types of insurance claims. The uncertainties surrounding the resolution of all of these claims continue, and it is presently not possible to estimate the ultimate exposure for A&E claims and related litigation. As a result, the reserves are subject to revision as new information becomes available. The continuing uncertainties include the lack of available and reliable historical claims data as an indicator of future loss development, the long waiting periods between exposure and manifestation of bodily injury or property damage, the difficulty in identifying the source of A&E contamination, the risks and lack of predictability inherent in major litigation, any impact from the bankruptcy protection sought by various asbestos producers and other asbestos litigation defendants, a further increase or decrease in the nature and volume of asbestos claims which cannot now be anticipated, the application and exhaustion of coverage limits, the resolution or adjudication of some disputes pertaining to the amount of available coverage for A&E claims in a manner inconsistent with the Company's previous assessment of these claims, the number and outcome of direct actions against the Company, and future developments pertaining to the Company's ability to recover reinsurance for A&E claims. It is also not possible to predict changes in the legal, economic, regulatory and legislative environments, and their impact on the future development of A&E claims. This development also will be affected by future court decisions and interpretations.

The uncertainties associated with establishing reserves for A&E claims and claim adjustment expenses are compounded by the differing, and at times inconsistent, court rulings on A&E coverage issues involving: (i) the differing interpretations of various insurance policy provisions and whether A&E losses are, or were ever intended to be, covered; (ii) when the loss occurred and what policies provide coverage; (iii) whether there is an insured obligation to defend; (iv) whether a compensable loss or injury has occurred; (v) how policy limits are determined; (vi) how policy exclusions are applied and interpreted; (vii) the impact of entities seeking bankruptcy protection as a result of asbestos-related liabilities; (viii) whether clean-up costs are covered as insured property damage and (ix) applicable coverage defenses or determinations, if any, including the determination as to whether or not an asbestos claim is a products or completed operation claim subject to an aggregate limit and the available coverage, if any, for that claim.

The Company estimates its net A&E reserves based upon numerous factors, including the facts surrounding reported cases and exposures to claims, such as policy limits and deductibles, current law, past and projected claim activity and past settlement values for similar claims, reinsurance coverage as well as analysis of industry studies and events, such as recent settlements and asbestos-related bankruptcies.

As a result of the significant uncertainty inherent in determining the Company's A&E liabilities, the amount of reserves required to adequately fund the Company's A&E claims cannot be accurately estimated using conventional reserving methodologies based upon historical data and trends and, as a result, the use of conventional reserving methodologies frequently has to be supplemented by subjective considerations, including management judgment. Thus, the ultimate amount of the Company's A&E exposures may vary materially from the reserves currently recorded and could have a material adverse effect on the Company's business, financial condition and results of operations.

Unpredictable catastrophic events could have a material adverse effect on the Company's financial condition or results of operations.

The Company writes insurance policies that cover catastrophic events. The Company's policies cover unpredictable natural and other disasters, such as hurricanes, windstorms, earthquakes, floods, fires, terrorist attacks and explosions. In addition, climate conditions, primarily global temperatures, may be changing, which may in the future increase the frequency and severity of natural catastrophes and the losses resulting there from. Although the Company carries reinsurance to mitigate its exposure to certain catastrophic events, claims from catastrophic events could reduce the Company's earnings and cause substantial volatility in its financial results for any fiscal quarter or year and have a material adverse effect on its financial condition.

The Terrorism Risk Insurance Act of 2002, as amended by the Terrorism Risk Insurance Program Reauthorization Act of 2007 (as amended, the "Terrorism Act") requires all commercial property and casualty insurers writing business in the U.S. to make terrorism coverage available to commercial policyholders and provides a Federal backstop for certified terrorist acts which result in losses above individual insurance company deductible amounts. The Terrorism Act directly applies to the Company's U.S. property and casualty insurance business. In 2008, on eligible lines of business, participating insurers will receive reimbursement from the Federal government for 85% of paid losses in excess of the insurer's deductible, provided the aggregate industry losses exceed \$100 million, to a maximum industry loss of \$100 billion. The Company estimates its deductible for commercial policies subject to the Terrorism Act (the amount the Company will have to pay before the Federal backstop becomes available) to be \$1.659 billion in 2008. This amounts to 20% of the Company's direct earned premium from commercial lines of business subject to the Terrorism Act and approximately 8.7% (on a net of tax basis) of policyholders' equity of the Company at December 31, 2007, prior to consideration of terrorism reinsurance that the Company has purchased for 2008. As of December 26, 2007, the U.S. government may "certify," and the Terrorism Act will cover, losses caused by a terrorist attack conducted by any individual, foreign or domestic. Damage outside the U.S. is not covered except in limited circumstances, such as damage to a U.S. air carrier. In addition, the Terrorism Act will remain in effect until December 31, 2014. There can be no assurance that it will be

extended beyond that date. Therefore, future losses from terrorist attacks could prove to be material to the Company's business, financial condition, and results of operations.

The Company's business could be harmed if its reserves are inadequate to cover actual claims and claim adjustment expenses.

Unpaid claims and claim adjustment expenses with respect to property-casualty insurance represent the Company's best estimate of amounts necessary to settle all outstanding claims, including claims that are incurred but not reported as of the reporting date. The Company's reserve projections are based primarily on detailed analysis of the facts in each case, experience with similar cases and various historical patterns. Consideration is given to such historical patterns as field reserving trends and claims settlement practices, loss payments, medical inflation, reinsurance program changes, pending levels of unpaid claims and product mix, as well as court decisions, economic conditions and public attitudes. The process of establishing loss reserves is complex and imprecise because it is subject to variables that are influenced by significant judgmental factors. Establishing loss reserves, including loss reserves for catastrophic events that have occurred, is an estimation process. Many factors can ultimately affect the final settlement of a claim and, therefore, the necessary reserve. Changes in the law, results of litigation, medical costs, the costs of repair materials and labor rates can all affect ultimate claim costs. In addition, time can be a critical part of reserving determinations since the longer the span between the incidence of a loss and the payment or settlement of the claim, the more variable the ultimate settlement can be. Accordingly, "short-tail" claims, such as property damage claims, tend to be easier to estimate than "long-tail" claims, such as workers compensation or general liability claims. Judicial decisions and legislative actions continue to broaden liability and policy definitions and to increase the cost of settling claims ("severity"). As a result of this and other societal and economic developments, the uncertainties inherent in estimating ultimate claim costs on the basis of past experience have been exacerbated, further complicating the already complex loss reserving process. Because of the inherent uncertainties that surround estimating loss reserves, the Company cannot be certain that its reserves are adequate and actual claims and claim adjustment expenses paid might exceed its reserves. As information develops that varies from past experience, provides additional data, or in some cases, augments data that previously was not considered sufficient for use in determining reserves, changes in the Company's estimate of ultimate liabilities may be required. These changes could have a material adverse effect on the Company's business, financial condition or results of operations.

Industry investigations and regulatory activity could adversely affect the Company's business.

In 2004, a number of companies engaged in the insurance business, including the Company, received subpoenas and other requests from the Attorneys General for the States of Connecticut, New York and Illinois and other insurance, governmental and enforcement authorities requesting information regarding broker sales practices, contingent commissions and improper quotations. In 2006, the Company was named in three separate civil actions filed by the Attorneys General for the States of Connecticut, Illinois and New York. The complaints contain allegations concerning broker sales practices, contingent commissions and improper quotations. The New York complaint alleges claims for fraudulent business

practices, anti-competitive behavior, common law fraud, unjust enrichment and inducement of breach of fiduciary duty. The Connecticut complaint alleges claims for breach of the Connecticut antitrust act and unfair trade practices act. The Illinois complaint alleged Consumer Fraud Act violations, inducement of a breach of fiduciary duty and unjust enrichment. Investigations revealed that two employees of the Company engaged in violations of Company policies to serve their personal interests by providing Marsh Inc.'s Global Broking Excess Casualty unit with a small number of false quotes. Both are no longer employees. The Company cooperated with the investigation into these matters and engaged in a dialogue to resolve the claims. Management concluded that the states' settlement demands were excessive and unreasonable. In the lawsuits, the states seek disgorgement of alleged illegal profits, restitution and damages, including punitive and treble damages. Illinois voluntarily dismissed the action without prejudice in June 2007. The Company continues to pursue the dismissal of the Connecticut and New York matters. Discovery has not yet begun in any of the cases.

In 2004 and 2005, a number of companies engaged in the insurance business, including the Company, received subpoenas and other requests from the SEC, the Justice Department and the New York Attorney General with respect to its purchase and sale of "non-traditional" or loss-mitigation products, including the purchase of retroactive reinsurance and its accounting for such products. In 2004, the Company also received a subpoena and request for information from the New York Attorney General regarding its underwriting practices in the sale of legal malpractice insurance. The Company believes that the investigations regarding "non-traditional" or loss-mitigation/retroactive reinsurance and the legal malpractice insurance have concluded without further action.

The Company cannot predict the impact, if any, that these matters may have on its business, financial condition or results of operations or the property and casualty insurance industry.

A significant ratings downgrade may have a material adverse effect on the Company's business.

Financial strength ratings issued by major rating organizations such as A.M. Best, Standard & Poor's and Moody's have become an increasingly important factor in establishing the competitive position of insurance companies. Rating agencies assign ratings based upon their evaluations of an insurance company's ability to meet its financial obligations.

The insurance entities that participate in the "Liberty Mutual Insurance Companies" pool, including Liberty Mutual Insurance Company, Liberty Mutual Fire Insurance Company and Employers Insurance Company of Wausau, have a current interactive financial strength rating and outlook as a group as set forth in the chart below:

Rating Agency	Rating	Rank of Rating	Outlook
A.M. Best	A (Excellent)	(3 rd highest of 16 ratings)	Stable
Standard & Poor's.....	A- (Strong)	(7 th highest of 21 ratings)	Stable
Moody's.....	A2 (Good)	(6 th highest of 21 ratings)	Negative

Following the April 23, 2008 announcement of the proposed acquisition of Safeco Corporation (“Safeco”), the Company’s financial strength ratings were affirmed with a Stable outlook by A.M. Best, affirmed by Moody’s with the outlook changed to Negative from Stable and placed on CreditWatch with negative implications by Standard & Poor’s pending their further review of the Safeco acquisition’s strategic and financial implications. On September 23, 2008, Moody’s affirmed the debt and insurance financial strength ratings of the Company and its subsidiaries following the Company’s announcement that it completed the acquisition of Safeco. The outlook for all of the Company’s long-term ratings remains negative. On September 25, 2008, Standard & Poor’s removed from CreditWatch and lowered to A- from A its counterparty credit and financial strength ratings of the Company’s insurance subsidiaries following the close of the Safeco acquisition on September 22, 2008. The outlook on all of these companies is Stable. If the Company’s ratings were lowered significantly relative to those of its competitors, the Company’s ability to market products to new customers could be harmed and existing policyholders might cancel or not renew their policies. In addition, downgrades could adversely affect the Company’s ability to access the debt markets and increase its borrowing costs. These events, in turn, could have a material adverse effect on the Company’s business, financial condition or results of operations.

The Company’s business could be harmed if it fails to adequately address the risks or any other problems encountered in connection with business combinations and acquisitions.

As a part of its business strategy, the Company intends to grow through business combinations and acquisitions. In particular, the Company is continuing to integrate Ohio Casualty Corporation and has begun to integrate Safeco. Acquisitions are typically accompanied by a number of risks, including:

- the difficulty of integrating the operations and personnel of the acquired companies;
- the difficulty of implementing and maintaining uniform standards, controls, procedures and policies;
- the potential disruption of the Company’s ongoing business and distraction of management;
- the impairment of relationships with employees and desirable policyholders; and
- potential unknown liabilities associated with acquired businesses.

The Company may not succeed in addressing these risks or any other problems encountered in connection with business combinations and acquisitions, including the Safeco acquisition, potentially having a material adverse effect on the Company’s business, financial condition or results of operations.

Reinsurance may not be adequate to protect the Company against losses, and reinsurers may not pay in a timely manner or at all.

The Company attempts to limit its risk of loss through reinsurance. The availability and cost of reinsurance protection is subject to market conditions, which are outside of the Company's control. As a result, the Company may not be able to successfully alleviate risk through these arrangements. In addition, the Company is subject to credit risk with respect to its reinsurance because the ceding of risk to reinsurers does not relieve the Company of its obligation to its policyholders. The Company also may experience difficulties in the future in recovering material reinsurance receivables under its reinsurance if one or more of the Company's reinsurers suffers financial deterioration. One or more of the Company's reinsurers could be significantly adversely affected by future significant loss events, including events related to the current financial crisis.

The effects of emerging claim and coverage issues on the Company's business are uncertain.

As industry practices and legal, judicial, social and other environmental conditions change, unexpected and unpredictable issues related to claims and coverage may emerge. These issues can have a negative effect on the Company's business by either extending coverage beyond the Company's underwriting intent or by increasing the number or size of claims. Examples of emerging claims and coverage issues include:

- court rulings that homeowners policy language excluding flood coverage is ambiguous;
- increases in the number and size of water damage claims related to expenses for testing and remediation of mold conditions;
- increases in the number and size of claims relating to construction defects, which often present complex coverage and damage valuation questions; and
- a trend of plaintiffs targeting property and casualty insurers, including the Company's insurance subsidiaries and affiliates authorized to transact business in one or more jurisdictions within the United States ("Insurance Subsidiaries"), in putative class action litigation related to claims handling and underwriting practices.

The effects of these and other unforeseen emerging claims and coverage issues are extremely hard to predict and could have a material adverse effect on the Company's business, financial condition or results of operations.

The Insurance Subsidiaries are highly regulated, and changes in these regulations could negatively affect the Company's business.

The Insurance Subsidiaries are subject to government regulation in their states of domicile and also in each of the jurisdictions in which they are licensed or authorized to do business. Governmental agencies have broad administrative power to regulate many aspects of the insurance business, including trade and claim practices, accounting methods, premium rates,

marketing practices, advertising, policy forms and capital adequacy. These agencies are concerned primarily with the protection of policyholders rather than shareholders or creditors. Moreover, insurance laws and regulations, among other things:

- establish solvency requirements, including minimum capital and surplus requirements and risk-based capital requirements;
- limit the amount of dividends, intercompany loans and other payments the Insurance Subsidiaries can make without prior regulatory approval;
- impose restrictions on the amounts and types of investments the Company may hold; and
- require assessments to pay claims of insolvent insurance companies.

The National Association of Insurance Commissioners (“NAIC”) continually examines existing laws and regulations. The Company cannot predict the effect that any NAIC recommendations or proposed or future legislation or rulemaking in the United States or elsewhere may have on the Company’s business, financial condition or results of operations.

The Company is also subject to the application of GAAP and statutory accounting practices, which are periodically revised. As a result, the Company may be required to adopt new or revised accounting standards issued by regulatory bodies. Any such changes to the Company’s current accounting treatment could result in material adverse effects on its reported net income or surplus/equity.

The Company has engaged in significant acquisitions of insurance companies and may do so in the future. Any such transactions will likely require regulatory approval which could result in limitations on the conduct of the Company’s business and financial activities.

A redomestication, merger or consolidation involving an Insurance Subsidiary could change its domiciliary state, resulting in materially different regulations becoming applicable to its business and operations.

The laws regarding redomestication, merger and consolidation, as applicable to the Insurance Subsidiaries, allow for the possibility that any of the Insurance Subsidiaries could change its domiciliary state, subject to regulatory approval. In the event of such a change, the regulations applicable to that Insurance Subsidiary, including restrictions on its ability to pay shareholder dividends, could be materially different from the currently applicable regulations.

Weak performance in the fixed income, equity and other markets has and could continue to negatively affect the Company’s profitability, capitalization and liquidity.

Investment returns are an important part of the Company’s overall profitability, and fluctuations in the fixed income, equity and other markets, or the continuation of the current weakness in those markets, has and could continue to negatively affect the Company’s profitability and/or financial condition. Historical performance of the equity markets has

exhibited significant volatility. In particular, the three-year period from March 2000 to March 2003 was characterized by significant negative returns. In addition, corporate downgrades and default rates were also at very high levels during this period. During the last 16 months, disruption in the global credit markets coupled with the re-pricing of credit risk created and continues to create extremely difficult market conditions and volatility in the financial markets. Initially, the concerns on the part of market participants were focused on the subprime segment of the mortgage-backed securities market. However, these concerns have since expanded to include a broad range of mortgage-and asset-backed and other fixed income securities, including those rated investment grade, the U.S. and international credit and interbank money markets generally, and a wide range of financial institutions and markets, asset classes and sectors. In recent weeks, disruptions and volatility in the fixed income, equity and other markets have reached unprecedented levels. Some of the largest companies in the financial sector have received government support, been acquired by stronger firms or been allowed to fail. These unprecedented events have been accompanied by extremely poor performance in fixed income, equity and other markets. These conditions resulted in greater volatility, less liquidity and widening of credit spreads.

In addition to occasionally issuing debt securities, the Company maintains a commercial paper facility that provides liquidity and allows for the orderly administration of its investment portfolio. The disruption in the credit markets negatively impacts the Company's ability to access these facilities at favorable rates or at all. Such market conditions may also limit our ability to replace, in a timely manner, maturing liabilities. It is difficult to predict how long these conditions will exist and how they will affect the Company in the future.

To the extent that the Company has portfolio exposure to fixed income, equity and other investments, it is subject to the following risks:

Interest rate changes. The market value of the Company's fixed income portfolio is dependent on market interest rates, which are primarily predicated on the market yield of United States Treasury bonds. As the Company holds its fixed income securities as available for sale, GAAP accounting requires the Company to mark to market the value of fixed income securities. In addition, market volatility, including significantly rising interest rates, rapidly widening credit spreads and illiquidity, has made it difficult to value certain of our securities if trading becomes less frequent. As such, valuations may include assumptions or estimates that may have significant period to period changes which could have a material adverse effect on our consolidated results of operations or financial condition. On the one hand, rising interest rates will result in a corresponding decline in the market value of the Company's fixed income portfolio, which could have a material adverse impact on the Company's GAAP equity. On the other hand, declining interest rates could lead to an increase in calls and prepayments and result in reinvestment at lower yields. This will lead to a decline in future net investment income.

Bond defaults and impairments. Increasing credit downgrades and defaults may result in write-downs in the value of bonds and preferred stock the Company holds or in losses on bonds that the Company liquidates. Additionally, credit rating agencies have downgraded, and may in the future downgrade, certain issuers and fixed income securities. In addition, the Company could incur write-downs due to the interest rate or credit spread environment or to defaults of the collateral backing certain securities. Recent events have led to increases in unrealized losses in certain securities in the Company's portfolio, including securities issued

by Federal National Mortgage Association (“FNMA”), Federal Home Loan Mortgage Corporation (“FHLMC”), Lehman Brothers Holdings Inc. (“Lehman Brothers”) and Washington Mutual, Inc. (“Washington Mutual”). For the nine months ended September 30, 2008, we had \$169 million of impairments related to fixed maturity securities of these and other issuers. There can be no assurance that our management has accurately assessed the level of impairments taken and allowances reflected in our financial statements. Furthermore, additional impairments may need to be taken or allowances provided for in the future.

Losses in the Company’s equity portfolio. The Company invests in the common and preferred stock of publicly traded companies. The performance of these investments is subject to a variety of domestic and international macroeconomic factors. A decline in the value of the Company’s equity portfolio could have an adverse effect on its financial condition and, to the extent the Company realizes write-downs or losses on these holdings, on its results of operation. On September 7, 2008, the United States Treasury announced that FNMA and FHLMC had been placed into conservatorship. On September 14, 2008, Lehman Brothers declared bankruptcy. On September 25, 2008, Washington Mutual was placed in federal receivership, and later declared bankruptcy. On October 3, 2008, Wachovia Corporation announced its intention to sell itself to Wells Fargo & Co., after previously disclosing its intention to sell itself to Citigroup Inc. Each of these events resulted in an impairment of the Company’s holdings of these companies’ common and/or preferred stock. For the nine months ended September 30, 2008, we had \$349 million of impairments related to the common and/or preferred stock of these and other issuers. The Company can make no assurance that these or any other assets in its equity portfolio will not continue to lose value.

Private equity. The Company invests in traditional private equity (primarily venture capital and buy out) and other forms of private equity (primarily energy) sectors through limited partnerships, as well as directly in various forms of equity, oil and gas working interests and debt. The Company’s investments in partnerships are generally accounted for using the equity method of accounting. The performance of these investments is subject to a wide variety of factors, including domestic economic growth levels, public stock market performance, initial public offering activity and energy prices. These investments are long-term in nature, highly illiquid and can be subject to significant underlying volatility. The Company has material unfunded commitments in its portfolio.

Real Estate. The Company invests in real estate through limited partnerships, limited liability corporations and participation agreements. The Company also holds participation certificates in commercial mortgage loans. Negative developments in the real estate market could adversely affect the value and the rental income of the Company’s properties as well as the delinquency and default rate of the Company’s participation certificates in commercial mortgage loans. These investments are long-term in nature and are highly illiquid. The Company has material unfunded commitments in its portfolio.

Foreign Currency. The Company invests in assets denominated in foreign currencies. A strengthening of the U.S. dollar against such foreign currencies will reduce the value of these assets. This will adversely impact the Company’s GAAP equity and result in a decline in future net investment income.

Pension Accounts. The Company maintains a defined benefit pension plan for a significant portion of its employees. A decline in the value of the assets in the plan caused by adverse

investment performance or an increase in the value of the liabilities caused by a decline in the discount rate could require the Company to provide additional funding for the plan or incur an equity charge. In 2007, the Company contributed \$205 million to the pension plan.

There can be no assurance that actions of the U.S. government, Federal Reserve and other governmental and regulatory bodies for the purpose of stabilizing the financial markets will achieve the intended effect.

In response to the financial crises affecting the banking system and financial markets and going concern threats to investment banks and other financial institutions, on October 3, 2008, President Bush signed the Emergency Economic Stabilization Act of 2008 (the “EESA”) into law. Pursuant to the EESA, the U.S. Treasury has the authority to, among other things, make equity investments in certain financial institutions and purchase mortgage-backed and other securities from financial institutions for a combined total amount of up to \$700 billion for the purpose of stabilizing the financial markets.

On October 7, 2008, the U.S. Federal Reserve announced that it would buy U.S. commercial paper through a special funding facility designed to provide liquidity to term-funding markets and backstop U.S. issuers of commercial paper. The facility will buy unsecured and asset-backed three-month commercial paper directly from eligible issuers, and the U.S. Federal Reserve will lend funds to the funding vehicle at the target federal funds rate. On October 14, 2008, the U.S. Treasury announced that the U.S. government would acquire preferred shares of nine of the largest financial institutions in the U.S., and up to a total of \$250 billion of equity stakes in financial institutions throughout the U.S.

The U.S. federal government, Federal Reserve and other governmental and regulatory bodies have taken or are considering taking other actions to address the financial crisis, including future investments in other financial institutions. There can be no assurance as to what impact such actions will have on the financial markets, including the extreme levels of volatility currently being experienced. Such continued volatility could materially and adversely affect our business, financial condition and results of operations, or the trading price of our debt securities.

Existing difficult economic conditions may materially adversely affect our business and results of operations and we do not expect these conditions to improve in the near future.

Our results of operations are materially affected by general economic conditions, both in the U.S. and elsewhere around the world. Beginning in the second half of 2007 and continuing in 2008, global financial, equity and other markets experienced significant stress, which has reached unprecedented levels in recent weeks. Recently, concerns over the availability and cost of credit, the U.S. mortgage market, a declining real estate market in the U.S., inflation, energy costs, extreme volatility in fixed income and equity markets and geopolitical issues have contributed to increased volatility and diminished expectations for the economy and the markets going forward. These factors, combined with volatile oil prices, declining business and consumer confidence and increased unemployment, have precipitated an economic slowdown and fears of a recession, which continue to challenge the U.S. and global fixed income, equity and other markets and overall economies. These events and the continuing market upheavals may have an adverse effect on us, in part because we are dependent upon customer behavior, and we have a large investment portfolio. Our revenues

are likely to decline in such circumstances and our profit margins could erode. Factors such as consumer spending, business investment, government spending, the volatility and strength of the capital markets and inflation all affect the business and economic environment and, ultimately, the amount of funds generated from our operations and the profitability of our business. In an economic downturn characterized by higher unemployment, lower family income, lower corporate earnings, lower business investment and lower consumer spending, the demand for our insurance products could be adversely affected. In addition, we may experience an elevated incidence of claims and lapses of policies. Our policyholders may choose to defer paying insurance premiums or stop paying insurance premiums altogether. Any such developments would adversely affect the amount of funds generated from operations, and we may not be able to replace those funds from other sources such as income or investments or borrowing, in particular during the current environment in the fixed income, equity and other markets. Fixed income and equity market volatility also reduces market liquidity which, in turn, negatively impacts the value of our investment portfolio. In these market conditions, fixed income instruments may also experience increased credit downgrading events and incremental probabilities of default. These adverse changes in the economy could have a material adverse effect on our business, results of operations and financial condition.

Inflation, including medical inflation, could have a material adverse effect on the Company's results.

The Company is a leading writer of workers compensation insurance, which is a line of business with reserves that are sensitive to medical inflation and medical utilization. In the last several years, medical inflation has increased by a greater rate than other types of inflation and its rate of increase has been difficult to predict. Because workers compensation involves long-tail liability for which premiums are calculated based partly on assumed rates of future medical inflation, if medical inflation increases significantly more than such assumptions, the Company may be required to increase its loss reserves with a corresponding reduction in its net income in the period in which the deficiency is identified.

The effects of inflation could also cause the severity of claims from catastrophes or other events to rise in the future. The Company's reserve for claims and claim adjustment expenses includes assumptions about future payments for settlement of claims and claims handling expenses, such as litigation costs. To the extent that actual inflation increases significantly more than such assumptions, the Company may be required to increase its loss reserves with a corresponding reduction in its net income in the period in which the deficiency is identified.

Competition in the Company's core businesses is intense.

Each of the Company's business segments faces strong competition from other insurers. The Company competes for sales of all its products against many competitors including some that are better capitalized or more specialized. In workers compensation insurance, the Company also competes against state insurance funds. The ability to compete effectively in the insurance industry is affected by various factors, including financial strength ratings, size and strength of the agency force, distribution capabilities, commission structure, range of product lines and product quality, price and features, customer service and general reputation. The level of competition may also increase as a result of further consolidation in

the insurance industry as companies seek to improve their competitive position through increased market share, economies of scale and diversification of products and services.

Inadequate premium rates for property and casualty insurance could have a material adverse effect on the Company's results.

Premium rates for property and casualty insurance are influenced by factors that are outside of the Company's control, including market and competitive conditions, regulatory issues and claims inflation. Any significant decrease in the rates the Company can charge for property and casualty insurance without a corresponding decrease in losses and expenses would adversely affect its results. Until 2001, the property and casualty insurance industry had experienced a prolonged period of downward pressure on prices caused by excess underwriting capacity and intense competition.

Despite the fact that the premium rates the Company has achieved since 2001 are significantly improved over those achieved in prior years, increasing competition resulting from increased capital in the property and casualty insurance industry has adversely impacted pricing trends. Competitive pressures have resulted in rates moderating, which could affect the Company's ability to attract or retain business or to write business at premium rates sufficient to cover costs.

Cyclical nature of the property and casualty insurance industry may cause the Company's results to fluctuate.

The property and casualty insurance industry is cyclical in nature and has historically been characterized by periods of relatively high levels of price competition, less restrictive underwriting standards and relatively low premium rates, followed by periods of capital shortages resulting in a lack of insurance availability, relatively low levels of competition, more selective underwriting of risks and relatively high premium rates. These factors could have a material adverse effect on the Company's business, financial condition or results of operations.

The Company's international business faces political, legal, operational and other risks that could adversely affect its results of operations.

The Company's international operations face political, legal, operational and other risks not encountered in the Company's U.S. operations. The Company faces the risk of discriminatory regulation, nationalization or expropriation of assets, price controls and exchange controls or other restrictions that could prevent the Company from transferring funds from these operations out of the countries in which they operate or converting local currencies it holds into U.S. dollars or other currencies. For example, in Venezuela, where the Company operates, the government has nationalized a number of key industries. In addition, the Company relies on local sales forces in these countries and may encounter labor problems resulting from workers associations and trade unions in some countries.

The Company's foreign insurance operations generally write policies denominated in local currencies and in large part invest in local currencies. Although investing in local currencies limits the effect of currency exchange rate fluctuation on local operating results, fluctuations in such rates affect the translation of these results into the Company's financial statements

and could have a material adverse effect on the Company's business, financial condition or results of operations.

Furthermore, the Company's international businesses are focused on emerging markets, which can be subject to severe economic and financial disruptions, including significant devaluations of their currencies and low or negative growth rates in economies.

The Company's surety products expose it to potentially high severity losses.

The Company provides surety products through its Liberty Mutual Surety operating unit, a part of Agency Markets. The majority of its surety obligations are performance based guarantees. This business exposes the Company to infrequent, but potentially high severity losses. The Company has accounts with bonded exposure in excess of \$100 million. The deterioration of one or more of these large accounts could have a material adverse effect on the Company's business, financial condition or results of operations.

The Company's results of operations are vulnerable to the credit risk presented by policyholders issued certain types of commercial policies.

A significant portion of the Company's commercial business is written with large deductible insurance policies. Under some commercial insurance contracts with deductible features, the Company is obligated to pay the claimant the full amount of the claim. The Company is subsequently reimbursed by the contract holder for the deductible amount, and is subject to credit risk until such reimbursement is made. Additionally, retrospectively rated policies are also used, primarily for workers compensation coverage, whereby the ultimate premium is determined based on actual loss activity. Although the retrospectively rated feature of the policy substantially reduces insurance risk for the Company, it does introduce credit risk to the Company. The Company's results of operations could be adversely affected if a significant portion of such contract holders failed to reimburse the Company for the deductible amount or the retrospectively rated policyholders failed to pay additional premiums owed.

Loss or significant restriction of the use of credit scoring, education and occupation in the pricing and underwriting of personal lines products could reduce the Company's future profitability.

The Company uses credit scoring, education and occupation data in various states in making risk selection and pricing decisions. Some consumer groups and regulators have questioned whether the use of credit scoring, education and occupation unfairly discriminates against lower-income and minority consumers and are calling for the prohibition of or restriction on the use of such factors in underwriting and pricing. Enactment in a large number of states of laws or regulations that significantly curtail the use of credit scoring, education and occupation in the underwriting process could reduce the Company's future profitability and thus could have a material adverse effect on the Company's business, financial condition or results of operations.