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

Quarter Ended June 30, 2007

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

The following discussion highlights significant factors influencing results of operations and changes in financial position of Liberty Mutual Holding Company Inc., the parent corporation of the Liberty Mutual Group of companies (the "Company" or "LMG"), for the three and six months ended June 30, 2007 and 2006. This Management's Discussion & Analysis of Financial Condition and Results of Operations ("MD&A") should be read in conjunction with the Company's 2006 Annual Report, Second Quarter 2007 Consolidated Financial Statements (unaudited), Second Quarter 2007 Financial Supplement and First Quarter MD&A, located on the Company's Investor Relations website at www.libertymutual.com/investors. The Company's discussions related to net income are presented on an after-tax GAAP basis. All other discussions are presented on a pre-tax GAAP basis, unless otherwise noted.

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Cautionary Statement Regarding Forward-Looking Statements

This report contains forward-looking statements that are intended to enhance the reader's ability to assess the Company's future financial and business performance. 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.

In particular, the sufficiency of the Company's reserves for (i) asbestos, (ii) environmental ((i) and (ii) together "A&E"), and (iii) toxic tort (i.e., claims that arise primarily from exposure to chemical or other hazardous substances, including welding rod and silica related claims), as well as its results of operations, financial condition and liquidity, to the extent impacted by the sufficiency of the Company's A&E and toxic tort reserves, are subject to a number of potential adverse developments including adverse developments involving A&E and toxic tort claims and the related level and outcome of litigation, the willingness of parties, including the Company, to settle disputes, the interpretation of aggregate policy coverage limits, the Company's ability to recover reinsurance for A&E, toxic tort and other claims, the legal, economic, regulatory, and legislative environments, and their impact on the future development of A&E and toxic tort claims, and the impact of bankruptcies of various asbestos producers and related peripheral businesses.

Some of the other factors that could cause actual results to differ include, but are not limited to, the following: the Company's inability to obtain price increases due to competition or otherwise; the performance of the Company's investment portfolios, which could be adversely impacted by unanticipated developments in U.S. and global financial markets, interest rates and rates of inflation; weakening U.S. and global economic conditions; insufficiency of, or changes in, loss reserves; the occurrence of catastrophic events, both natural and man-made, including terrorist acts, with a severity or frequency exceeding the Company's expectations; exposure to, and adverse developments involving, environmental claims and related litigation; the impact of claims related to exposure to potentially harmful products or substances, including, but not limited to, lead paint, silica and other potentially harmful substances; adverse changes in loss cost trends, including inflationary pressures in medical costs and auto and home repair costs; developments relating to coverage and liability for mold claims; the effects of corporate bankruptcies on surety bond claims; adverse developments in the cost, availability and/or ability to collect reinsurance; the ability of the Company's subsidiaries to pay dividends to the Company; adverse results or other consequences from legal proceedings; the impact of regulatory investigations or reforms, including governmental actions regarding the compensation of brokers and agents and the purchase and sale of nontraditional products and related disclosures; unusual loss activity resulting from adverse weather conditions, including storms, hurricanes, hail, snowfall and winter conditions; repatriation of foreign earnings; judicial expansion of policy coverage and the impact of new theories of liability; the impact of legislative actions, including Federal and state legislation related to asbestos liability reform; larger than expected assessments for guaranty funds and mandatory pooling arrangements; a downgrade in the Company's claims-paying and financial strength ratings; the loss or significant restriction on the Company's ability to use credit scoring in the pricing and underwriting of Personal Lines policies; and amendments and changes to the risk-based capital requirements. The Company's forward-looking statements speak only as of the date of this report or as of the date they are made and should be regarded solely as the Company's current plans, estimates and beliefs. For a detailed discussion of these and other cautionary statements, visit the Company's Investor Relations web site at www.libertymutual.com/investors. The Company undertakes no obligation to update these forward-looking statements.

EXECUTIVE SUMMARY

The following highlights do not address all of the matters covered in the other sections of Management's Discussion & Analysis of Financial Condition and Results of Operations or contain all of the information that may be important to the investing public. This summary should be read in conjunction with the other sections of Management's Discussion & Analysis of Financial Condition and Results of Operations and the Company's unaudited financial statements.

Three Months Ended June 30, 2007 - Consolidated Results of Operations

- Revenues for the three months ended June 30, 2007 were $6.295 billion, an increase of $245 million or 4.0% over the same period in 2006.
- Pre-tax income for the three months ended June 30, 2007 was $498 million, an increase of $15 million or 3.1% over the same period in 2006.
- Net income for the three months ended June 30, 2007 was $339 million, an increase of $16 million or 5.0% over the same period in 2006.
- Cash flow from operations for the three months ended June 30, 2007 was $787 million, a decrease of $339 million or 30.1% from the same period in 2006. Results in the period primarily reflect a $290 million decrease in immediate annuity sales from the same period in 2006.
- The combined ratio before catastrophes[1] and net incurred losses attributable to prior years[2] for the three months ended June 30, 2007 was 96.5%, an increase of 1.4 points over the same period in 2006. Including the impact of catastrophes and net incurred losses attributable to prior years, the Company's combined ratio for the three months ended June 30, 2007 decreased 0.9 points to 100.1%.

Six Months Ended June 30, 2007 - Consolidated Results of Operations

- Revenues for the six months ended June 30, 2007 were $12.438 billion, an increase of $940 million or 8.2% over the same period in 2006.
- Pre-tax income for the six months ended June 30, 2007 was $998 million, an increase of $111 million or 12.5% over the same period in 2006. Results in the period reflect an increase in realized capital gains of $56 million.
- Net income for the six months ended June 30, 2007 was $689 million, an increase of $74 million or 12.0% over the same period in 2006.
- Cash flow from operations for the six months ended June 30, 2007 was $1.796 billion, an increase of $172 million or 10.6% over the same period in 2006.
- The combined ratio before catastrophes and net incurred losses attributable to prior years for the six months ended June 30, 2007 was 97.8%, an increase of 1.9 points over the same period in 2006. Including the impact of catastrophes and net incurred losses attributable to prior years, the Company's combined ratio for the six months ended June 30, 2007 increased 0.1 points to 100.6%.

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[1] Catastrophes include all current and prior year catastrophe losses related to the Company's insurance lines and exclude losses related to the Company's external reinsurance assumed lines (assumed voluntary reinsurance and reinsurance assumed through Lloyd's Syndicate 4472) except for losses related to the events of September 11, 2001, the 2004 U.S. hurricanes and the 2005 U.S. hurricanes. In addition, losses related to the 2005 U.S. hurricanes and the 2004 U.S. hurricanes for assumed external reinsurance are reported net of the Company's reasonable assumption of expected catastrophe activity (defined as "net catastrophe reinsurance premium earned"). Internally reinsured catastrophe losses are not reported net of net catastrophe reinsurance premium earned. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums and losses related to June 2007 California wildfires.

[2] Net incurred losses attributable to prior years is defined as incurred losses attributable to prior years (excluding prior year losses related to natural catastrophes and the events of September 11, 2001) including both earned premium attributable to prior years and amortization of retroactive reinsurance gains.

Financial Condition as of June 30, 2007

- Total assets were $88.472 billion as of June 30, 2007, an increase of $2.974 billion or 3.5% over December 31, 2006.

- Policyholders' equity was $11.228 billion as of June 30, 2007, an increase of $333 million or 3.1% over December 31, 2006.

- Statutory surplus as regards policyholders for the combined operations of Liberty Mutual Insurance Company ("LMIC") and its U.S. affiliates was $13.547 billion as of June 30, 2007, an increase of $1.416 billion or 11.7% over December 31, 2006.

Other 2007 2nd Quarter Highlights

Acquisitions

- On May 7, 2007, LMG and Ohio Casualty Corporation announced that they have entered into a definitive agreement pursuant to which LMG, through its subsidiaries, will acquire with cash all outstanding shares of common stock of Ohio Casualty for $44.00 per share or approximately $2.7 billion. The proposed transaction, which has been approved by the Boards of Directors of both companies, is subject to approval by Ohio Casualty shareholders and customary regulatory approvals and conditions, and is expected to close in the third quarter of 2007.

Rating Actions

- On May 7, 2007, Moody's Investors Service upgraded the debt ratings of Liberty Mutual Group Inc. ("LMGI"), including its non-guaranteed unsecured debt (to Baa2 from Baa3) and junior subordinated debt (to Baa3 from Ba1). In the same action, Moody's confirmed its Baa2 rating on the surplus notes of LMIC, as well as LMIC's Baa1 long-term issuer rating and the Baa1 rating on the medium term notes of LMGI (originally issued by Liberty Mutual Capital Corporation), based on a guarantee provided by LMIC. The A2 insurance financial strength ratings of LMIC and its inter-company reinsurance pool members were affirmed, as was LMGI's Prime-2 short-term rating for commercial paper. The outlook for all ratings is stable.

- On May 7, 2007, Standard & Poor's Ratings Services affirmed its ratings on LMGI and all of its operating insurance companies. The outlook for all ratings is stable.

Changes in Debt/Credit Facilities

- The Company recently entered into certain debt facilities to further improve its liquidity profile. On April 5, 2007, LMGI entered into a $250 million 3-year unsecured revolving credit facility for general corporate purposes.
- On June 15, 2007, LMIC and certain insurance affiliates entered into a $1.25 billion short-term revolving credit facility, guaranteed by LMIC, to facilitate the pending acquisition of Ohio Casualty Corporation by allowing for an optimal liquidation of investment assets.
- On June 25, 2007 LMGI increased its commercial paper program, guaranteed by LMIC, from $600 million to $1.0 billion

CONSOLIDATED RESULTS OF OPERATIONS

The Company has identified consolidated pre-tax operating income ("PTOI") and net written premium as non-GAAP financial measures. PTOI is defined by the Company as pre-tax income excluding net realized gains (losses), extraordinary items, discontinued operations and cumulative effects of changes in accounting principles. PTOI is considered by the Company to be an appropriate indicator of underwriting and operating results and is consistent with the way the Company internally evaluates performance, except that limited partnership results recognized on the equity method are not included in internal PTOI. Net realized investment gains (losses) are significantly impacted by both discretionary and economic factors and are not necessarily indicative of operating results. Federal and foreign income taxes are significantly impacted by permanent differences and valuation allowances. References to "direct written premium" represent the amount of premium recorded for policies issued during a fiscal period excluding assumed reinsurance and ignoring the effects of ceded reinsurance. References to "net written premium" represent the amount of premium recorded for policies issued during a fiscal period including audits, retrospectively rated premium related to loss sensitive policies, and assumed premium, less ceded premium. Assumed and ceded reinsurance premiums include premium adjustments for reinstatement of coverage when a loss has used some portion of the reinsurance provided, generally under catastrophe treaties ("reinstatement premium"). In addition, the majority of workers compensation premium is adjusted to the "booked as billed" method through the Corporate & Other segment. "Premium earned," which is the portion of premium that applies to the expired part of the policy period, is a GAAP measure. The Company believes that net written premium is a performance measure useful to investors as it generally reflects current trends in the Company's sale of its insurance products.

The Company's discussions related to net income are presented on an after-tax GAAP basis. All other discussions are presented on a pre-tax GAAP basis, unless otherwise noted.

Overview – Consolidated

Consolidated net written premium (NWP) by significant line of business was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2007**	**2006**	**Change**	**2007**	**2006**	**Change**
Private passenger automobile	$1,592	$1,453	9.6%	$3,038	$2,770	9.7%
Workers compensation	1,119	1,013	10.5	2,604	2,453	6.2
Homeowners	502	465	8.0	896	817	9.7
Commercial multiple peril / Fire	412	384	7.3	804	776	3.6
International local businesses[2]	326	270	20.7	679	555	22.3
LIU[3] reinsurance	237	303	(21.8)	581	687	(15.4)
Commercial automobile	275	272	1.1	563	557	1.1
General liability	210	235	(10.6)	466	431	8.1
LIU inland marine program[4]	133	67	98.5	264	129	104.7
LIU third party	138	122	13.1	263	232	13.4
Group disability and life	117	100	17.0	233	198	17.7
LIU first party[4]	76	84	(9.5)	147	147	-
Individual life	80	370	(78.4)	144	504	(71.4)
Surety	78	64	21.9	144	122	18.0
Assumed voluntary reinsurance	28	27	3.7	59	46	28.3
Other	154	115	33.9	279	230	21.3
Total net written premium[1]	$5,477	$5,344	2.5%	$11,164	$10,654	4.8%

1 Net written premium associated with internal reinsurance has been re-allocated to the appropriate lines of business in the above table.
2 Local international businesses, selling small commercial and other personal lines products locally, excluding private passenger automobile.
3 Liberty International Underwriters (LIU).
4 Effective in the first quarter of 2007, the LIU inland marine program has been reported separately from LIU first party. The prior period has been restated to reflect this change.

Consolidated net written premium by SBU was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2007**	**2006**	**Change**	**2007**	**2006**	**Change**
Personal Markets	$1,438	$1,404	2.4%	$2,693	$2,599	3.6%
Commercial Markets	1,015	924	9.8	2,295	2,101	9.2
Agency Markets	1,544	1,467	5.2	3,198	3,069	4.2
International	1,384	1,217	13.7	2,807	2,491	12.7
Corporate and Other[1]	96	332	(71.1)	171	394	(56.6)
Total net written premium (NWP)	$5,477	$5,344	2.5%	$11,164	$10,654	4.8%
Foreign exchange effect on growth			1.0			1.0
NWP growth excluding foreign exchange			1.5%			3.8%

1 Includes Individual life operations and internal reinsurance.
NM = Not Meaningful

Net written premium for the three and six months ended June 30, 2007 was $5.477 billion and $11.164 billion, respectively, increases of $133 million and $510 million over the same periods in 2006. Significant changes by major line of business include:

- Private passenger automobile net written premium increased $139 million and $268 million in the quarter and year-to-date, respectively. The increases in both periods primarily reflect organic growth in International's local businesses of Latin America and Europe, primarily Venezuela, Portugal and Spain, the acquisition of Seker Sigorta A.S., a property and casualty insurer located in Turkey, and the strengthening of foreign currencies versus the U.S. dollar. The increases in both periods also reflect strong customer retention and new business growth in both Personal Markets and Agency Markets.
- Workers compensation net written premium increased $106 million and $151 million in the quarter and year-to-date, respectively. The increases in both periods primarily reflect new business writings, increased audit and retrospective premium of $25 million and $103 million in the quarter and year-to-date, respectively, higher customer retention at the Regional Companies and Wausau, and a $20 million and $35 million adjustment to the Corporate and Other segment for the "booked as billed" method of accounting for net written premium in the quarter and year-to-date, respectively. Partially offsetting these increases in both periods was a decrease in Summit's premium due to mandated rate decreases in Florida.
- Homeowners net written premium increased $37 million and $79 million in the quarter and year-to-date, respectively. The increases in both periods primarily reflect the impact of rate increases, strong customer retention and new business growth, primarily in non-coastal areas, in both Personal Markets and Agency Markets.
- Commercial multiple peril / Fire increased $28 million in the quarter and year-to-date. The increases in both periods reflect strong retention, new business growth and rate increases in Commercial Markets' Liberty Mutual Property segment as well as strong customer retention and new business writings in Commercial Markets' other segments and Agency Markets.
- International local businesses net written premium (excluding private passenger automobile) increased $56 million and $124 million in the quarter and year-to-date, respectively. The increases in both periods reflect organic growth in Latin America and Europe and the strengthening of foreign currencies versus the U.S. dollar.
- LIU reinsurance net written premium decreased $66 million and $106 million in the quarter and year-to-date, respectively. The decreases in both periods primarily reflect management's decision to significantly reduce its catastrophe exposure in the U.S. and Europe, partially offset by property-related growth outside of the major catastrophe exposed areas.

- General liability net written premium decreased $25 million in the quarter and increased $35 million year-to-date. The decrease in the quarter is primarily driven by premium recognized on a large Commercial Markets account with a multi-year policy in June of 2006, which did not recur this quarter, partially offset by new business writings and higher year-to-date audit and retrospective premium.
- LIU inland marine program net written premium increased $66 million and $135 million in the quarter and year-to-date, respectively. The program provides replacement coverage for lost or damaged cell phones.
- LIU third party net written premium increased $16 million and $31 million in the quarter and year-to-date, respectively. The increases in both periods were primarily due to a reduction in the utilization of reinsurance as compared to prior periods, partially offset by a modest decline in rates as a result of more competitive market conditions.
- Group disability and life net written premium increased $17 million and $35 million in the quarter and year-to-date, respectively, due primarily to the impact of an expanded sales force and broader market penetration.
- LIU first party net written premium decreased $8 million in the quarter. The change reflects a more competitive rate environment and a change in the timing of recording ceded written premium for certain excess of loss contracts.
- Individual life net written premium decreased $290 million and $360 million in the quarter and year-to-date, respectively, due to the decline in immediate annuity sales.
- Surety net written premium increased $14 million and $22 million in the quarter and year-to-date, respectively, due to new business writings and the non-renewal of a 2006 reinsurance program in Agency Markets.
- Other net written premium increased $39 million and $49 million in the quarter and year-to-date, respectively, due to increases in internal reinsurance.

More detailed explanations of the changes in net written premium by line of business are included in the related discussion of financial results for each segment.

For a more complete description of the Company's business operations, products and distribution channels, please visit the Company's Investor Relations web site at www.libertymutual.com/investors.

Results of Operations – Consolidated

	Three Months Ended June 30,			**Six Months Ended June 30,**		
$ in Millions	**2007**	**2006**	**Change**	**2007**	**2006**	**Change**
Revenues	$6,295	$6,050	4.0%	$12,438	$11,498	8.2%
PTOI before catastrophes and net incurred losses attributable to prior years	$638	$713	(10.5%)	$1,152	$1,239	(7.0%)
Catastrophes[1]	(122)	(187)	(34.8)	(181)	(286)	(36.7)
Net incurred losses attributable to prior years:						
- Asbestos & environmental[2]	(1)	(1)	-	(1)	(3)	(66.7)
- All other[3]	(62)	(86)	(27.9)	(97)	(132)	(26.5)
Pre-tax operating income	453	439	3.2	873	818	6.7
Realized investment gains, net	45	44	2.3	125	69	81.2
Federal and foreign income tax expense	(159)	(160)	(0.6)	(309)	(272)	13.6
Net income	$339	$323	5.0%	$689	$615	12.0%
Cash flow from operations	$787	$1,126	(30.1%)	$1,796	$1,624	10.6%

1 Catastrophes include all current and prior year catastrophe losses related to the Company's insurance lines and exclude losses related to the Company's external reinsurance assumed lines (assumed voluntary reinsurance and reinsurance assumed through Lloyd's Syndicate 4472) except for losses related to the events of September 11, 2001, the 2004 U.S. hurricanes and the 2005 U.S. hurricanes. In addition, losses related to the 2005 U.S. hurricanes and the 2004 U.S. hurricanes for assumed external reinsurance are reported net of the Company's reasonable assumption of expected catastrophe activity (defined as "net catastrophe reinsurance premium earned"). Internally reinsured catastrophe losses are not reported net of net catastrophe reinsurance premium earned. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums and losses related to June 2007 California wildfires.

2 Net of allowance for uncollectible reinsurance reduction of zero and $3 million for the three and six months ended June 30, 2007, respectively, and zero for the comparable periods of 2006.

3 Net of earned premium attributable to prior years of $16 million and $35 million for the three and six months ended June 30, 2007, respectively, and $18 million and $34 million for the comparable periods of 2006. Net of amortization of deferred gains on retroactive reinsurance of $32 million and $48 million for the three and six months ended June 30, 2007, respectively, and $15 million and $31 million for the comparable periods of 2006.

NM = Not Meaningful

Revenues for the three and six months ended June 30, 2007 were $6.295 billion and $12.438 billion, respectively, increases of $245 million and $940 million over the same periods in 2006. The major components of revenues are net premium earned, net investment income, net realized investment gains and losses, and fee and other revenues.

Net premium earned for the three and six months ended June 30, 2007 was $5.356 billion and $10.567 billion, respectively, increases of $176 million and $721 million over the same periods in 2006. The increases in both periods primarily reflect the earned premium associated with the changes in net written premium in 2006 and the first half of 2007.

Net investment income for the three and six months ended June 30, 2007 was $710 million and $1.383 billion, respectively, increases of $76 million and $189 million over the same periods in 2006. The increases in both periods reflect an increase in interest income due primarily to higher invested assets driven by strong cash flow from operations and the proceeds received from the Company's August 2006 and March 2007 debt offerings. Year-to-date results also reflect an increase in limited partnership and limited liability company income. Year-to-date dividend income relates to the increased investment in equity securities. These increases in net investment income, however, were constrained by lower yields on the fixed maturity portfolio, due primarily to the Company's increased investment in tax-exempt securities.

Net realized investment gains for the three and six months ended June 30, 2007 were $45 million and $125 million, respectively, increases of $1 million and $56 million over the same periods in 2006. The increase year-to-date was primarily driven by a $34 million increase in net gains on equities, primarily by gains on foreign equities, and lower impairment losses.

Fee and other revenues for the three and six months ended June 30, 2007 were $184 million and $363 million, respectively, decreases of $8 million and $26 million from the same periods in 2006. The decreases reflect lower revenues from the sale and production of oil and gas from the subsidiary operations of Liberty Energy Holdings, LLC (“Liberty Energy”) and lower fee revenues associated with the Company’s involuntary market servicing carrier operations due to lower involuntary market premium volume. As a servicing carrier, the Company receives fee income for performing certain underwriting, claims and administrative services for all participating involuntary pool members.

Claims, benefits and expenses for the three and six months ended June 30, 2007 were $5.797 billion and $11.440 billion, respectively, increases of $230 million and $829 million over the same periods in 2006. The increases in both periods are primarily due to business growth and general cost increases in each of the Company’s SBU’s, higher interest expense, and foreign exchange gains in 2006 that did not recur in 2007, primarily from the strengthening of the Colombian peso versus the U.S. dollar as respects U.S. dollar denominated investments of foreign subsidiaries. The increases to claims, benefits and expenses related to foreign exchange losses were $24 million and $28 million in the quarter and year-to-date, respectively. In addition, International’s net commission expense increased in both periods due to the reduction in ceding commission recognized by LIU’s third party business as a result of the reduction in reinsurance utilization, higher acquisition costs in the local businesses, primarily Europe, and lower ceding commission recognized on LIU’s inland marine program due to a change in the terms of the program. The increase year-to-date also reflects higher non-catastrophe related property losses, including losses from the floods in the United Kingdom in both periods and year-to-date losses from the European storm Kyrill, and higher acquisition costs related to the Personal Markets’ advertising program. The increases in both periods were partially offset by lower catastrophe losses and a decrease in policyholder benefits due to the decline in immediate annuity sales. The decrease in year-to-date incurred losses attributable to prior years primarily reflects favorable development in automobile, property and liability lines, partially offset by an increase in workers compensation.

CONSOLIDATED	Three Months Ended June 30, 2007	2006	Change (Points)	Six Months Ended June 30, 2007	2006	Change (Points)
Combined ratio before catastrophes and net incurred losses attributable to prior years						
Claims and claim adjustment expense ratio	68.7%	67.7%	1.0	69.6%	68.8%	0.8
Underwriting expense ratio	27.5	27.1	0.4	27.9	26.8	1.1
Dividend ratio	0.3	0.3	-	0.3	0.3	-
Subtotal	96.5	95.1	1.4	97.8	95.9	1.9
Catastrophes[1]	2.4	4.0	(1.6)	1.8	3.2	(1.4)
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other	1.2	1.9	(0.7)	1.0	1.4	(0.4)
Total combined ratio[2]	100.1%	101.0%	(0.9)	100.6%	100.5%	0.1

1 Catastrophes include all current and prior year catastrophe losses related to the Company's insurance lines and exclude losses related to the Company's external reinsurance assumed lines (assumed voluntary reinsurance and reinsurance assumed through Lloyd's Syndicate 4472) except for losses related to the events of September 11, 2001, the 2004 U.S. hurricanes and the 2005 U.S. hurricanes. In addition, losses related to the 2005 U.S. hurricanes and the 2004 U.S. hurricanes for assumed external reinsurance are reported net of the Company's reasonable assumption of expected catastrophe activity (defined as "net catastrophe reinsurance premium earned"). Internally reinsured catastrophe losses are not reported net of net catastrophe reinsurance premium earned. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums and losses related to June 2007 California wildfires.

2 The combined claim and expense ratio, expressed as a percentage, is a measure of underwriting profitability. This measure should only be used in conjunction with, and not in lieu of, underwriting income and may not be comparable to other performance measures used by the Company's competitors. The combined claim and expense ratio is computed as the sum of the following property and casualty ratios: the ratio of claims and claim adjustment expense to earned premium; the ratio to earned premium of insurance operating costs plus amortization of deferred policy acquisition costs less fee income (primarily related to the Company's involuntary market servicing carrier operations and managed care income) and less installment charges; and the ratio of policyholder dividends to earned premium. Provisions for uncollectible premium and reinsurance are not included in the combined ratio unless related to an asbestos & environmental commutation.

The consolidated combined ratio before catastrophes and net incurred losses attributable to prior years for the three and six months ended June 30, 2007 was 96.5% and 97.8%, respectively, increases of 1.4 points and 1.9 points over the comparable periods in 2006. The increases in both periods reflect a higher underwriting expense ratio due to an increase in International's net commission expense resulting from a reduction in the utilization of reinsurance on LIU's third party business which resulted in a lower amount of ceding commission received, higher acquisition costs in International's Local Businesses, primarily Europe, and lower ceding commission recognized on LIU's inland marine program due to a change in the terms of the program, partially offset by higher earned premium growth. The year-to-date underwriting expense ratio also reflects an increase in variable incentive compensation and other corporate expenses, partially offset by higher premium growth. In addition, the claims and claim adjustment expense ratio increased in both periods as the Personal Markets' current accident year loss ratios in both periods were recorded at levels higher than 2006, reflective of the uncertainty associated with the continuation of favorable auto liability loss trends and lower premium rates. The increases in the claims and claim adjustment expense ratio in both periods also reflect an increase in non-catastrophe related property losses and more competitive margins in most commercial lines, partially offset by higher earned premium primarily associated with internal property catastrophe reinsurance which had no corresponding losses and improved loss experience on LIU's first party, third party and reinsurance businesses.

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three and six months ended June 30, 2007 was 100.1% and 100.6%, respectively, a decrease of 0.9 points in the quarter and an increase of 0.1 points year-to-date versus the same periods in 2006. The changes in both periods reflect lower catastrophe losses of 1.6 points and 1.4 points in the quarter and year-to-date, respectively as the prior periods included additional losses attributable to the 2005 U.S. hurricanes and more significant storm activity.

PTOI for the three and six months ended June 30, 2007 was $453 million and $873 million, respectively, increases of $14 million and $55 million over the same periods in 2006.

Federal and foreign income tax expense for the three and six months ended June 30, 2007 was $159 million and $309 million, respectively, a decrease of $1 million and an increase of $37 million versus the same periods in 2006. The Company's effective tax rates for the three and six months ended June 30, 2007 were 32% and 31%, respectively, compared to 33% and 31% for the same periods in 2006. The Company's effective rate differs from the Federal statutory rate of 35% principally due to tax-preferenced investment income.

Net income for the three and six months ended June 30, 2007 was $339 million and $689 million, respectively, increases of $16 million and $74 million over the same periods in 2006.

PERSONAL MARKETS

Overview – Personal Markets

Personal Markets net written premium by line of business was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2007**	**2006**	**Change**	**2007**	**2006**	**Change**
Private passenger automobile	$981	$974	0.7%	$1,881	$1,839	2.3%
Homeowners and other	457	430	6.3	812	760	6.8
Total net written premium	$1,438	$1,404	2.4%	$2,693	$2,599	3.6%

Net written premium for the three and six months ended June 30, 2007 was $1.438 billion and $2.693 billion, respectively, increases of $34 million and $94 million over the same periods in 2006. The increases in both periods reflect new business growth and strong customer retention in both auto and homeowners and rate increases on homeowners policies.

Private passenger automobile net written premium for the three and six months ended June 30, 2007 was $981 million and $1.881 billion, respectively, increases of $7 million and $42 million over the same periods in 2006. The increases in both periods are driven by a 2.9% increase in voluntary policies in force as compared to June 30, 2006, due to strong customer retention and new business growth, partially offset by lower average premium per policy. The lower average premium per policy is primarily driven by mandatory rate decreases in Massachusetts, effective in April of 2007.

Homeowners and other net written premium for the three and six months ended June 30, 2007 was $457 million and $812 million, respectively, increases of $27 million and $52 million over the same periods in 2006. The increases in both periods are due to rate increases and a 3.7% increase in policies in force as compared to June 30, 2006 due to strong customer retention and new business growth, primarily in non-coastal areas.

Results of Operations – Personal Markets

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2007**	**2006**	**Change**	**2007**	**2006**	**Change**
Revenues	$1,439	$1,394	3.2%	$2,850	$2,756	3.4%
PTOI before catastrophes and net incurred losses attributable to prior years	$207	$228	(9.2)	$363	$404	(10.1)
Catastrophes[1]	(92)	(81)	13.6	(128)	(140)	(8.6)
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other[2]	34	-	NM	74	-	NM
Pre-tax operating income	149	147	1.4	309	264	17.0
Realized investment gains, net	-	-	-	-	-	-
Federal and foreign income tax expense	(45)	(50)	(10.0)	(93)	(91)	2.2
Net income	$104	$97	7.2%	$216	$173	24.9%

1 Catastrophes include all current and prior year catastrophe losses related to the Company's insurance lines and exclude losses related to the Company’s external reinsurance assumed lines (assumed voluntary reinsurance and reinsurance assumed through Lloyd’s Syndicate 4472) except for losses related to the events of September 11, 2001, the 2004 U.S. hurricanes and the 2005 U.S. hurricanes. In addition, losses related to the 2005 U.S. hurricanes and the 2004 U.S. hurricanes for assumed external reinsurance are reported net of the Company’s reasonable assumption of expected catastrophe activity (defined as “net catastrophe reinsurance premium earned”). Internally reinsured catastrophe losses are not reported net of net catastrophe reinsurance premium earned. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums and losses related to June 2007 California wildfires.

2 Net of earned premium attributable to prior years of zero for the three and six months ended June 30, 2007, respectively, and zero for the comparable periods of 2006.

NM = Not Meaningful

Revenues for the three and six months ended June 30, 2007 were $1.439 billion and $2.850 billion, respectively, increases of $45 million and $94 million over the same periods in 2006. The major components of revenues are net premium earned and net investment income.

Net premium earned for the three and six months ended June 30, 2007 was $1.341 billion and $2.657 billion, respectively, increases of $33 million and $73 million over the same periods in 2006. The increases in both periods reflect the earned premium associated with growth in net written premium for both the voluntary auto and homeowners lines of business in 2006 and the first half of 2007, partially offset by a reduction in involuntary market policies.

Net investment income for the three and six months ended June 30, 2007 was $84 million and $165 million, respectively, increases of $11 million and $21 million over the same periods in 2006. The increases in both periods primarily reflect higher invested assets due to strong cash flow from operations.

Claims, benefits and expenses for the three and six months ended June 30, 2007 were $1.290 billion and $2.541 billion, respectively, increases of $43 million and $49 million over the same periods in 2006. The increases in both periods reflect business growth and higher acquisition costs related to the Company’s advertising program. These increases were partially offset by lower year-to-date catastrophe losses and favorable incurred loss development attributable to prior years in both periods compared to 2006.

PERSONAL MARKETS	Three Months Ended June 30, 2007	2006	Change (Points)	Six Months Ended June 30, 2007	2006	Change (Points)
Combined ratio before catastrophes and net incurred losses attributable to prior years						
Claims and claim adjustment expense ratio	65.4%	62.2%	3.2	67.0%	64.6%	2.4
Underwriting expense ratio	24.8	25.4	(0.6)	25.1	24.9	0.2
Dividend ratio	-	-	-	-	-	-
Subtotal	90.2	87.6	2.6	92.1	89.5	2.6
Catastrophes[1]	6.9	6.2	0.7	4.8	5.4	(0.6)
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other	(2.5)	-	(2.5)	(2.8)	-	(2.8)
Total combined ratio	94.6%	93.8%	0.8	94.1%	94.9%	(0.8)

1 Catastrophes include all current and prior year catastrophe losses related to the Company's insurance lines and exclude losses related to the Company’s external reinsurance assumed lines (assumed voluntary reinsurance and reinsurance assumed through Lloyd’s Syndicate 4472) except for losses related to the events of September 11, 2001, the 2004 U.S. hurricanes and the 2005 U.S. hurricanes. In addition, losses related to the 2005 U.S. hurricanes and the 2004 U.S. hurricanes for assumed external reinsurance are reported net of the Company’s reasonable assumption of expected catastrophe activity (defined as “net catastrophe reinsurance premium earned”). Internally reinsured catastrophe losses are not reported net of net catastrophe reinsurance premium earned. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums and losses related to June 2007 California wildfires.

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three and six months ended June 30, 2007 was 94.6% and 94.1%, an increase of 0.8 points and a decrease of 0.8 points over the same periods in 2006. Both periods reflect higher current accident year losses, as the current accident year has been recorded at a loss ratio reflective of the uncertainty associated with the continuation of favorable auto liability loss trends and lower premium rates. This is offset by favorable net incurred losses attributable to prior years primarily related to the auto line of business, as prior year auto liability loss and loss adjustment expense reserves continued to develop favorably, resulting in 2.5 points and 2.8 points of favorable development in the three and six months ended June 30, 2007, respectively. The increase in the quarter reflects higher catastrophe losses in 2007, offset by lower underwriting expense ratio due to a decrease in acquisition costs related to lower profit share expense related to operations acquired from Prudential Financial, Inc. (“PruPac”). The decrease in the six months ended June 30, 2007 reflects lower catastrophe losses, offset by higher underwriting expense ratio due to an increase in advertising costs.

PTOI for the three and six months ended June 30, 2007 was $149 million and $309 million, respectively, increases of $2 million and $45 million over the same periods in 2006.

Federal and foreign income tax expense for the three and six months ended June 30, 2007 was $45 million and $93 million, respectively, a decrease of $5 million and an increase of $2 million versus the same periods in 2006, as a result of higher pre-tax income offset by a lower effective tax rate in 2007. The effective rate differs from the Federal statutory rate of 35% principally due to tax-preferenced investment income.

Net income for the three and six months ended June 30, 2007 was $104 million and $216 million, respectively, increases of $7 million and $43 million over the same periods in 2006.

COMMERCIAL MARKETS

Overview – Commercial Markets

Commercial Markets net written premium by market segment was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2007**	**2006**	**Change**	**2007**	**2006**	**Change**
Business Market	$375	$349	7.4%	$923	$886	4.2%
National Market	315	308	2.3	752	683	10.1
Group Market	117	100	17.0	233	198	17.7
Liberty Mutual Property	108	74	45.9	188	159	18.2
Other Markets[1]	100	93	7.5	199	175	13.7
Total net written premium	$1,015	$924	9.8%	$2,295	$2,101	9.2%

1 Effective January 1, 2007, net written premium associated with the involuntary pools for Wausau, previously included in Commercial Markets, is included in Agency Markets. The prior period has been restated to reflect this change.

Commercial Markets net written premium by line of business was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2007**	**2006**	**Change**	**2007**	**2006**	**Change**
Workers compensation	$512	$443	15.6%	$1,250	$1,165	7.3%
General liability	114	147	(22.4)	281	256	9.8
Group disability and life	117	100	17.0	233	198	17.7
Commercial automobile	96	93	3.2	209	206	1.5
Commercial multiple peril / Fire	91	70	30.0	161	147	9.5
Assumed voluntary reinsurance	26	27	(3.7)	56	46	21.7
Other	59	44	34.1	105	83	26.5
Total net written premium	$1,015	$924	9.8%	$2,295	$2,101	9.2%

Net written premium for the three and six months ended June 30, 2007 was $1.015 billion and $2.295 billion, respectively, increases of $91 million and $194 million over the same periods in 2006. The increases in both periods primarily reflect new business writings across all market segments and lines of business. In addition audit and retrospective premium increased approximately $47 million and $113 million in the quarter and year-to-date, respectively, over the same periods in 2006. The increases in Group disability and life premium for both periods reflect the impact of an expanded sales force and broader market penetration. Commercial multiple peril/fire and other lines premium growth in both periods reflects new business growth in the Liberty Mutual Property segment as well as strong retention and rate increases. Partially offsetting these increases were modest rate decreases and lower retention levels across most lines of business reflective of the competitive market environment. The decrease in general liability premium in the quarter primarily reflects premium recognized on a large account with a multi-year policy in June of 2006, which did not recur this quarter.

Results of Operations – Commercial Markets

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2007**	**2006[3]**	**Change**	**2007**	**2006[3]**	**Change**
Revenues	$1,255	$1,160	8.2%	$2,510	$2,250	11.6%
PTOI before catastrophes and net incurred losses attributable to prior years	$98	$117	(16.2%)	$194	$202	(4.0%)
Catastrophes[1]	(3)	(39)	(92.3)	(8)	(51)	(84.3)
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other[2]	(19)	(2)	NM	(28)	(23)	21.7
Pre-tax operating income	76	76	-	158	128	23.4
Realized investment gains, net	-	-	-	-	-	-
Federal and foreign income tax expense	(22)	(27)	(18.5)	(47)	(44)	6.8
Net income	$54	$49	10.2%	$111	$84	32.1%

1 Catastrophes include all current and prior year catastrophe losses related to the Company's insurance lines and exclude losses related to assumed voluntary reinsurance except for losses related to the events of September 11, 2001, the 2004 U.S. hurricanes and the 2005 U.S. hurricanes. In addition, losses related to the 2005 U.S. hurricanes and the 2004 U.S. hurricanes for assumed external reinsurance are reported net of the Company's reasonable assumption of expected catastrophe activity (defined as "net catastrophe reinsurance premium earned"). Internally reinsured catastrophe losses are not reported net of net catastrophe reinsurance premium earned. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

2 Net of earned premium attributable to prior years of $5 million and $10 million for the three and six months ended June 30, 2007, respectively, and $1 million and ($5) million for the comparable periods of 2006. Net of amortization of deferred gains on retroactive reinsurance of $24 million and $34 million for the three and six months ended June 30, 2007, respectively, and $8 million and $15 million for the comparable periods of 2006.

3 Effective January 1, 2007, the results associated with the involuntary pools for Wausau, previously included in Commercial Markets, are included in Agency Markets. In 2006, the net result was allocated to Agency Markets. The prior period has been restated to reflect this change.

NM = Not Meaningful.

Revenues for the three and six months ended June 30, 2007 were $1.255 billion and $2.510 billion, respectively, increases of $95 million and $260 million over the same periods in 2006. The major components of revenues are net premium earned, net investment income, and fee and other revenues.

Net premium earned for the three and six months ended June 30, 2007 was $1.026 billion and $2.052 billion, respectively, increases of $88 million and $246 million over the same periods in 2006. The increases in both periods primarily reflect the earned premium associated with the changes in net written premium in 2006 and the first half of 2007.

Net investment income for the three and six months ended June 30, 2007 was $151 million and $299 million, respectively, increases of $15 million and $31 million over the same periods in 2006. The increases in both periods primarily reflect higher invested assets due to strong cash flow from operations.

Fee and other revenues for the three and six months ended June 30, 2007 were $78 million and $159 million, respectively, decreases of $8 million and $17 million from the same periods in 2006. The decreases in both periods primarily reflect lower fee revenues associated with the Company's involuntary market servicing carrier operations due to lower involuntary market premium volume. As a servicing carrier, the Company receives fee income for performing certain underwriting, claims and administrative services for all participating involuntary pool members.

Claims, benefits and expenses for the three and six months ended June 30, 2007 were $1.179 billion and $2.352 billion, respectively, increases of $95 million and $230 million over the same periods in 2006. The increases in both periods primarily reflect business growth, general cost increases, higher non-catastrophe related property losses and an increase in incurred losses attributable to prior years. These increases are partially offset by lower catastrophes.

COMMERCIAL MARKETS	Three Months Ended June 30, 2007	2006[2]	Change (Points)	Six Months Ended June 30, 2007	2006[2]	Change (Points)
Combined ratio before catastrophes and net incurred losses attributable to prior years						
Claims and claim adjustment expense ratio	82.5%	79.6%	2.9	82.9%	81.1%	1.8
Underwriting expense ratio	20.1	20.4	(0.3)	19.4	20.2	(0.8)
Dividend ratio	0.3	0.2	0.1	0.3	0.2	0.1
Subtotal	102.9	100.2	2.7	102.6	101.5	1.1
Catastrophes[1]	0.2	4.7	(4.5)	0.4	3.1	(2.7)
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other	2.2	0.2	2.0	1.5	1.5	-
Total combined ratio	105.3%	105.1%	0.2	104.5%	106.1%	(1.6)

1 Catastrophes include all current and prior year catastrophe losses related to the Company's insurance lines and exclude losses related to assumed voluntary reinsurance except for losses related to the events of September 11, 2001, the 2004 U.S. hurricanes and the 2005 U.S. hurricanes. In addition, losses related to the 2005 U.S. hurricanes and the 2004 U.S. hurricanes for assumed external reinsurance are reported net of the Company's reasonable assumption of expected catastrophe activity (defined as "net catastrophe reinsurance premium earned"). Internally reinsured catastrophe losses are not reported net of net catastrophe reinsurance premium earned. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

2 Effective January 1, 2007, the results associated with the involuntary pools for Wausau, previously included in Commercial Markets, are included in Agency Markets. In 2006, the net result was allocated to Agency Markets. The prior period has been restated to reflect this change.

The Commercial Markets combined ratio before catastrophes and net incurred losses attributable to prior years for the three and six months ended June 30, 2007 was 102.9% and 102.6%, respectively, increases of 2.7 points and 1.1 points over the comparable periods in 2006. The increases in the claims and claim adjustment expense ratio in both periods primarily reflect higher non-catastrophe related property losses compared to the same periods in 2006 and the impact of a more competitive rate environment. The decrease in the underwriting expense ratio in both periods is a result of earned premium growth greater than the rate of general expense growth, partially offset by the lower expense reimbursement received from the Company's servicing carrier operations.

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three and six months ended June 30, 2007 was 105.3% and 104.5%, respectively, an increase of 0.2 points and a decrease of 1.6 points versus the same periods in 2006. Results in both periods reflect lower catastrophe losses as 2006 included additional losses attributable to the 2005 U.S. hurricanes related to assumed voluntary reinsurance lines. In addition, net incurred losses attributable to prior years increased in the quarter but were unchanged on a year-to-date basis.

PTOI for the three and six months ended June 30, 2007 was $76 million and $158 million, respectively, unchanged in the quarter and an increase of $30 million over the six month period in 2006.

Federal and foreign income tax expense for the three and six months ended June 30, 2007 was $22 million and $47 million, respectively, a decrease of $5 million and an increase of $3 million versus the same periods in 2006. The decrease in the quarter reflects a lower effective tax rate in 2007 vs. 2006. The increase year-to-date reflects higher pre-tax income. The effective rate differs from the Federal statutory rate of 35% principally due to tax-preferenced investment income.

Net income for the three and six months ended June 30, 2007 was $54 million and $111 million, respectively, increases of $5 million and $27 million over the same periods in 2006.

AGENCY MARKETS

Overview – Agency Markets

Agency Markets net written premium by market segment was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2007**	**2006[1]**	**Change**	**2007**	**2006[1]**	**Change**
Regional Companies[2]	$912	$863	5.7%	$1,767	$1,674	5.6%
Wausau	288	242	19.0	721	667	8.1
Summit	240	280	(14.3)	520	571	(8.9)
Surety	78	61	27.9	144	118	22.0
Other[2]	26	21	23.8	46	39	17.9
Total net written premium	$1,544	$1,467	5.2%	$3,198	$3,069	4.2%

[1] Effective January 1, 2007, net written premium associated with the involuntary pools for Wausau, previously included in Commercial Markets, is included in Agency Markets. The prior period has been restated to reflect this change.
[2] Effective January 1, 2007, the results associated with the National Council on Compensation Insurance involuntary business, which were previously included in Other, are included in Regional Companies. Reclassifications have been made to the prior period to reflect this change, with no overall impact to Agency Markets.

Agency Markets net written premium by line of business was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2007**	**2006[1]**	**Change**	**2007**	**2006[1]**	**Change**
Commercial Lines						
Workers compensation total:	$649	$630	3.0%	$1,475	$1,443	2.2%
- Wausau	230	184	25.0	588	531	10.7
- Summit	240	280	(14.3)	520	571	(8.9)
- All other	179	166	7.8	367	341	7.6
Commercial multiple peril	300	290	3.4	595	575	3.5
Commercial automobile	178	178	-	351	350	0.3
General liability	71	68	4.4	139	138	0.7
Surety	78	64	21.9	144	122	18.0
Other	51	45	13.3	103	90	14.4
Subtotal	$1,327	$1,275	4.1%	$2,807	$2,718	3.3%
Personal Lines						
Private passenger automobile	$128	$113	13.3%	$235	$210	11.9%
Homeowners	79	70	12.9	137	123	11.4
Other	10	9	11.1	19	18	5.6
Subtotal	$217	$192	13.0%	$391	$351	11.4%
Total net written premium	$1,544	$1,467	5.2%	$3,198	$3,069	4.2%

Net written premium for the three and six months ended June 30, 2007 were $1.544 billion and $3.198 billion, increases of $77 million and $129 million over the same periods in 2006. The growth in the quarter and year-to-date primarily reflects stable to higher retention levels and new business writings in most commercial lines of business, partially offset by modest rate decreases in most states due to competitive market conditions and significant rate decreases in California due to workers compensation reform. In addition, surety premium increased due to new business writings and the non-renewal of a reinsurance program. Personal auto premium, excluding the impact of the non-standard runoff business (GoAmerica), increased 21.0% and 19.4% in the quarter and year-to-date, respectively. This reflects the impact of new business, personal auto multivariate pricing models and an increase in distribution focus and resources, which also had a favorable impact on homeowners growth. These increases were partially offset by a decrease in Summit's workers compensation premium due to mandated rate decreases in Florida.

Results of Operations – Agency Markets

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2007**	**2006[3]**	**Change**	**2007**	**2006[3]**	**Change**
Revenues	$1,643	$1,550	6.0%	$3,259	$3,043	7.1%
PTOI before catastrophes and net incurred losses attributable to prior years	$144	$173	(16.8%)	$269	$297	(9.4%)
Catastrophes[1]	(27)	(62)	(56.5)	(45)	(84)	(46.4)
Net incurred losses attributable to prior years:						
- Asbestos & environmental	(1)	-	NM	(1)	-	NM
- All other[2]	57	7	NM	78	33	136.4
Pre-tax operating income	173	118	46.6	301	246	22.4
Realized investment gains, net	-	-	-	-	-	-
Federal and foreign income tax expense	(52)	(41)	26.8	(90)	(86)	4.7
Net income	$121	$77	57.1%	$211	$160	31.9%

1 Catastrophes include all current and prior year catastrophe losses related to the Company's insurance lines and exclude losses related to the Company's external reinsurance assumed lines (assumed voluntary reinsurance and reinsurance assumed through Lloyd's Syndicate 4472) except for losses related to the events of September 11, 2001, the 2004 U.S. hurricanes and the 2005 U.S. hurricanes. In addition, losses related to the 2005 U.S. hurricanes and the 2004 U.S. hurricanes for assumed external reinsurance are reported net of the Company's reasonable assumption of expected catastrophe activity (defined as "net catastrophe reinsurance premium earned"). Internally reinsured catastrophe losses are not reported net of net catastrophe reinsurance premium earned. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

2 Net of earned premium attributable to prior years of $6 million and $19 million for the three and six months ended June 30, 2007, respectively, and $16 million and $33 million for the comparable periods of 2006. Net of amortization of deferred gains on retroactive reinsurance of $2 million and $3 million for the three and six months ended June 30, 2007, respectively, and $2 million and $5 million for the comparable periods of 2006.

3 Effective January 1, 2007, the results associated with the involuntary pools for Wausau, previously included in Commercial Markets, are included in Agency Markets. In 2006, the net result was allocated to Agency Markets. The prior period has been restated to reflect this change.

NM = Not Meaningful

Revenues for the three and six months ended June 30, 2007 were $1.643 billion and $3.259 billion, respectively, increases of $93 million and $216 million over the same periods in 2006. The major components of revenues are net premium earned and net investment income.

Net premium earned for the three and six months ended June 30, 2007 were $1.487 billion and $2.949 billion, respectively, increases of $77 million and $180 million over the same periods in 2006. The increases in both periods primarily reflect the earned premium associated with the changes in net written premium in 2006 and the first half of 2007.

Net investment income for the three and six months ended June 30, 2007 was $136 million and $268 million, respectively, increases of $20 million and $40 million over the same periods in 2006. The increases in both periods primarily reflect higher invested assets due to strong cash flow from operations.

Claims, benefits and expenses for the three and six months ended June 30, 2007 were $1.470 billion and $2.958 billion, increases of $38 million and $161 million over the same periods in 2006. The increases in both periods are primarily due to business growth, an increase in non-catastrophe related property losses, and general cost increases, partially offset primarily by an increase in the amount of favorable incurred loss development attributable to prior years related to workers compensation and general liability lines and lower catastrophe losses.

AGENCY MARKETS	Three Months Ended June 30, 2007	2006[2]	Change (Points)	Six Months Ended June 30, 2007	2006[2]	Change (Points)
Combined ratio before catastrophes and net incurred losses attributable to prior years						
Claims and claim adjustment expense ratio	67.4%	65.3%	2.1	68.3%	65.7%	2.6
Underwriting expense ratio	30.7	30.7	-	30.6	30.9	(0.3)
Dividend ratio	1.0	0.9	0.1	0.9	1.1	(0.2)
Subtotal	99.1	96.9	2.2	99.8	97.7	2.1
Catastrophes[1]	1.9	4.4	(2.5)	1.6	3.0	(1.4)
Net incurred losses attributable to prior years:						
- Asbestos & environmental	0.1	-	0.1	-	-	-
- All other	(3.9)	(0.5)	(3.4)	(2.7)	(1.2)	(1.5)
Total combined ratio	97.2%	100.8%	(3.6)	98.7%	99.5%	(0.8)

1 Catastrophes include all current and prior year catastrophe losses related to the Company's insurance lines and exclude losses related to the Company's external reinsurance assumed lines (assumed voluntary reinsurance and reinsurance assumed through Lloyd's Syndicate 4472) except for losses related to the events of September 11, 2001, the 2004 U.S. hurricanes and the 2005 U.S. hurricanes. In addition, losses related to the 2005 U.S. hurricanes and the 2004 U.S. hurricanes for assumed external reinsurance are reported net of the Company's reasonable assumption of expected catastrophe activity (defined as "net catastrophe reinsurance premium earned"). Internally reinsured catastrophe losses are not reported net of net catastrophe reinsurance premium earned. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

2 Effective January 1, 2007, the results associated with the involuntary pools for Wausau, previously included in Commercial Markets, are included in Agency Markets. In 2006, the net result was allocated to Agency Markets. The prior period has been restated to reflect this change.

The Agency Markets combined ratio before catastrophes and net incurred losses attributable to prior years for the three and six months ended June 30, 2007 was 99.1% and 99.8%, respectively, increases of 2.2 points and 2.1 points over the comparable periods in 2006. The increases in both periods primarily reflect a higher claims and claim adjustment expense ratio due primarily to higher non-catastrophe related property losses. The underwriting expense ratio in both periods was essentially unchanged while the decrease in the year-to-date dividend ratio reflects lower dividends incurred at Summit as a result of the state mandated rate decrease in Florida.

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio was 97.2% and 98.7%, respectively, decreases of 3.6 points and 0.8 points over the same periods in 2006. The decreases in both periods primarily reflect lower catastrophe losses as compared to the same periods in 2006 and an increase in the amount of favorable net incurred losses attributable to prior years related to workers compensation and general liability lines.

PTOI for the three and six months ended June 30, 2007 was $173 million and $301 million, respectively, increases of $55 million over both periods in 2006.

Federal and foreign income tax expense for the three and six months ended June 30, 2007 was $52 million and $90 million, respectively, increases of $11 million and $4 million over the same periods in 2006, as a result of higher pre-tax income offset by a lower effective tax rate in 2007. The effective rate differs from the Federal statutory rate of 35% principally due to tax-preferenced investment income.

Net income for the three and six months ended June 30, 2007 was $121 million and $211 million, respectively, increases of $44 million and $51 million over the same periods in 2006.

INTERNATIONAL

Overview – International

International net written premium by market segment was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2007**	**2006**	**Change**	**2007**	**2006**	**Change**
International Local Businesses Total	$802	$635	26.3%	$1,594	$1,275	25.0%
- Latin America	389	312	24.7	791	656	20.6
- Europe	371	292	27.1	718	553	29.8
- Asia Pacific	42	31	35.5	85	66	28.8
Liberty International Underwriters	582	582	-	1,213	1,216	(0.2)
Total net written premium (NWP)	$1,384	$1,217	13.7%	$2,807	$2,491	12.7%
Foreign exchange effect on growth			4.2			4.3
NWP growth excluding foreign exchange			9.5%			8.4%

The Company's International operations provide insurance products and services through 1) Local Businesses, selling personal and small commercial lines products locally and 2) Liberty International Underwriters ("LIU") which sells specialty commercial lines insurance and reinsurance products worldwide.

International's six major lines of business are as follows:

(1) Local businesses: personal and small commercial insurance;
(2) LIU reinsurance: includes multi-line insurance and reinsurance with an emphasis on property, treaty casualty, personal accident, aviation and reinsurance through Lloyd's Syndicate 4472;
(3) LIU inland marine program: cell phone replacement coverage for lost or damaged devices;
(4) LIU third party: includes casualty, excess casualty, D&O, E&O, professional liability and other;
(5) LIU first party: includes marine, energy, engineering, aviation, and property; and
(6) LIU other: includes workers compensation, commercial auto, and residual value.

International net written premium by line of business was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2007**	**2006[1]**	**Change**	**2007**	**2006[1]**	**Change**
Local businesses – private passenger auto	$482	$365	32.1%	$921	$720	27.9%
Local businesses – all other	320	270	18.5	673	555	21.3
LIU reinsurance	240	303	(20.8)	531	687	(22.7)
LIU inland marine program[1]	133	67	98.5	264	129	104.7
LIU third party	135	122	10.7	260	232	12.1
LIU first party[1]	68	84	(19.0)	139	147	(5.4)
LIU other	6	6	-	19	21	(9.5)
Total net written premium	$1,384	$1,217	13.7%	$2,807	$2,491	12.7%

1 Effective in the first quarter of 2007, LIU inland marine program has been reported separately from LIU first party. The prior period has been restated to reflect this change.

Net written premium for the three and six months ended June 30, 2007 was $1.384 billion and $2.807 billion, respectively, increases of $167 million and $316 million over the same periods in 2006. The increases in both periods reflect organic growth in the local businesses of Latin America and Europe, primarily Venezuela, Portugal and Spain, the acquisition of Seker Sigorta A.S., a property and casualty insurer located in Turkey, and the strengthening of foreign currencies versus the U.S. dollar. Growth in both periods also reflects the continued expansion of LIU's inland marine program business and a change in the terms of the program, which provides replacement coverage for lost or damaged cell phones. The increases in LIU's third party business in both periods were primarily due to a reduction in the utilization of reinsurance as compared to prior periods, partially offset by a modest decline in rates as a result of more competitive market conditions. Similarly, the slight decline in year-to-date net written premium for LIU's first party business is largely the result of a more competitive rate environment. LIU's first party net written premium for the quarter was also impacted by a change in the timing of recording ceded written premium for certain excess of loss contracts. The decrease in LIU's reinsurance business reflects management's decision to significantly reduce its catastrophe exposure in the U.S. and Europe, partially offset by growth in the Lloyd's property business outside of the major catastrophe exposed areas.

Results of Operations – International

	Three Months Ended June 30,			**Six Months Ended June 30,**		
$ in Millions	**2007**	**2006**	**Change**	**2007**	**2006**	**Change**
Revenues	$1,513	$1,249	21.1%	$2,946	$2,364	24.6%
PTOI before catastrophes and net incurred losses attributable to prior years	$144	$134	7.5%	$279	$248	12.5%
Catastrophes[1]	-	(6)	(100.0)	-	(6)	(100.0)
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other[2]	13	(39)	NM	22	(57)	NM
Pre-tax operating income	157	89	76.4	301	185	62.7
Realized investment (losses) gains, net	(1)	9	NM	11	24	(54.2)
Federal and foreign income tax expense	(47)	(32)	46.9	(91)	(66)	37.9
Net income	$109	$66	65.2%	$221	$143	54.5%

1 Catastrophes include all current and prior year catastrophe losses related to the Company's insurance lines and exclude losses related to external reinsurance assumed through Lloyd's Syndicate 4472 except for losses related to the events of September 11, 2001, the 2004 U.S. hurricanes and the 2005 U.S. hurricanes. In addition, losses related to the 2005 U.S. hurricanes and the 2004 U.S. hurricanes for assumed external reinsurance are reported net of the Company's reasonable assumption of expected catastrophe activity (defined as "net catastrophe reinsurance premium earned"). Internally reinsured catastrophe losses are not reported net of net catastrophe reinsurance premium earned. Catastrophe losses, where applicable, include the impact of reinstatement premiums.

2 Net of earned premium attributable to prior years of $5 million and $6 million for the three and six months ended June 30, 2007, respectively, and $1 million and $6 million for the comparable periods of 2006.

NM = Not Meaningful

Revenues for the three and six months ended June 30, 2007 were $1.513 billion and $2.946 billion, respectively, increases of $264 million and $582 million over the same periods in 2006. The major components of revenues are net premium earned, net investment income and net realized investment gains and losses.

Net premium earned for the three and six months ended June 30, 2007 was $1.365 billion and $2.648 billion, respectively, increases of $241 million and $525 million over the same periods in 2006. The increases in both periods reflect the impact of business growth, consistent with the increase in net written premium from local businesses, LIU's inland marine program and LIU's third party business. Earned premium from LIU's reinsurance business increased primarily as a result of a higher level of written premium in 2006 primarily due to rate increases on property business.

Net investment income for the three and six months ended June 30, 2007 was $130 million and $253 million, respectively, increases of $31 million and $65 million over the same periods in 2006. The increases are driven by higher invested assets due to very strong cash flows from operations, higher yields and the impact of foreign exchange.

Net realized investment (losses) gains for the three and six months ended June 30, 2007 were $(1) million and $11 million, respectively, decreases of $10 million and $13 million over the same periods in 2006. The decline in both periods is primarily attributable to losses realized on investment transactions in Venezuela.

Claims, benefits and expenses for the three and six months ended June 30, 2007 were $1.357 billion and $2.634 billion, respectively, increases of $206 million and $479 million over the same periods in 2006. The increases in both periods primarily reflect business growth, losses related to European storm Kyrill, the floods in the United Kingdom and higher commission expense. Additionally, claims, benefits and expenses increased due to foreign exchange gains in 2006 that did not recur in 2007, primarily from the strengthening of the Colombian peso versus the U.S. dollar as respects U.S. dollar denominated investments of foreign subsidiaries. The increase to claims, benefits and expenses related to foreign exchange losses was $24 million and $28 million in the quarter and year-to-date, respectively. The increase in net commission expense primarily reflects the reduction in ceding commission recognized by LIU's third party business as a result of the aforementioned reduction in reinsurance utilization, higher acquisition costs in the local businesses, primarily Europe, and lower ceding commission recognized on LIU's inland marine program due to a change in the terms of the program. These increases in both periods were partially offset by a decrease in incurred losses attributable to prior years reflecting favorable loss development in local business operations, primarily auto business in Spain, and LIU third party, partially offset by adverse development on prior years within LIU's reinsurance business.

	Three Months Ended June 30,			**Six Months Ended June 30,**		
INTERNATIONAL	**2007**	**2006**	**Change (Points)**	**2007**	**2006**	**Change (Points)**
Combined ratio before catastrophes and net incurred losses attributable to prior years						
Claims and claim adjustment expense ratio	65.4%	68.7%	(3.3)	66.5%	67.5%	(1.0)
Underwriting expense ratio	31.3	27.5	3.8	31.1	28.3	2.8
Dividend ratio	-	-	-	-	-	-
Subtotal	96.7	96.2	0.5	97.6	95.8	1.8
Catastrophes[1]	-	0.5	(0.5)	-	0.3	(0.3)
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other	(1.0)	3.6	(4.6)	(0.9)	2.8	(3.7)
Total combined ratio	95.7%	100.3%	(4.6)	96.7%	98.9%	(2.2)

1 Catastrophes include all current and prior year catastrophe losses related to the Company's insurance lines and exclude losses related to external reinsurance assumed through Lloyd's Syndicate 4472 except for losses related to the events of September 11, 2001, the 2004 U.S. hurricanes and the 2005 U.S. hurricanes. In addition, losses related to the 2005 U.S. hurricanes and the 2004 U.S. hurricanes for assumed external reinsurance are reported net of the Company's reasonable assumption of expected catastrophe activity (defined as "net catastrophe reinsurance premium earned"). Internally reinsured catastrophe losses are not reported net of net catastrophe reinsurance premium earned. Catastrophe losses, where applicable, include the impact of reinstatement premiums.

The consolidated combined ratio before catastrophes and net incurred losses attributable to prior years for the three and six months ended June 30, 2007 was 96.7% and 97.6%, respectively, increases of 0.5 points and 1.8 points over the comparable periods in 2006. The increases in both periods reflect a higher underwriting expense ratio resulting from the aforementioned increase in net commission expense. The decreases in claim and claim adjustment expense ratio in both periods reflect the aforementioned change in the terms of the program related to LIU's inland marine program and improved loss experience on LIU's first party, third party and reinsurance businesses. These improvements in the claim and claim adjustment expense ratio in both periods were partially offset by higher loss trends from the auto business in Latin America and Europe, particularly Venezuela, Brazil and Spain.

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three and six months ended June 30, 2007 was 95.7% and 96.7%, respectively, decreases of 4.6 points and 2.2 points over the same periods in 2006. The decreases in both periods reflect lower catastrophe losses and a decrease in net incurred losses attributable to prior years reflecting favorable loss development in local business operations, primarily in Spain, and LIU third party, partially offset by LIU reinsurance, in 2007 versus unfavorable development in 2006.

PTOI for the three and six months ended June 30, 2007 was $157 million and $301 million, respectively, increases of $68 million and $116 million over the same periods in 2006.

Federal and foreign income tax expense for the three and six months ended June 30, 2007 was $47 million and $91 million, respectively, increases of $15 million and $25 million over the same periods in 2006, as a result of higher pre-tax income offset by a lower effective tax rate in 2007. The effective tax rates for the three and six months ended June 30, 2007 were 30% and 29%, respectively, compared to 33% and 32% for the same periods in 2006. Federal and foreign income taxes reflect the different tax structures within the countries where International operates.

Net income for the three and six months ended June 30, 2007 was $109 million and $221 million, respectively, increases of $43 million and $78 million over the same periods in 2006.

CORPORATE and OTHER

Overview – Corporate and Other

Corporate and Other includes the following significant items:

- Individual life, which provides life insurance and annuities for individuals and also issues structured settlement contracts and administers separate account contracts. Individual life is licensed and sells its products in all 50 states, the District of Columbia and Canada.

- Certain internal discontinued operations, composed of: asbestos, environmental, toxic tort exposures, the run-off of the California workers compensation business of Golden Eagle Insurance Corporation, and certain distribution channels related to PruPac's business.

- Interest expense on the Company's outstanding domestic debt.

- Internal reinsurance programs, primarily catastrophe treaties where the SBUs choose to purchase more reinsurance coverage than the Company purchases for the consolidated group and, effective in 2007, loss development associated with Commercial Market pre-2005 fully insured workers compensation business.

- The Company reports its written premiums on workers compensation contracts on the "booked as billed" method. Commercial Markets and Agency Markets report these same written premiums on the "booked at inception" method. Corporate and Other results reflect the difference between these two methods.

- Costs associated with certain long-term compensation plans and other corporate costs not allocated to the SBUs. For presentation in this MD&A, domestic property and casualty operations' investment income was allocated based on planned ordinary investment income returns by investment category allocated to the business units. Investments are allocated as follows: fixed income equal to liabilities net of insurance assets (reinsurance, premiums receivable, etc.) and a combination of fixed income, equity and nontraditional investments supporting allocated statutory policyholders' surplus. For internal reporting purposes, the Company allocates expected long-term returns on invested assets, including realized investment gains.

- Federal and foreign income taxes represent the difference between the consolidated projected income tax expense and the amounts recognized by the Personal, Commercial, and Agency Markets and International business units. In 2007, the Company changed its allocation methodology to allocate federal taxes at an initial expected tax rate (30%) to the domestic operations, while International reflects the actual tax expense of each country including changes in the international valuation allowance. The difference between the initial rate and the actual rate allocated to the SBUs is included in Corporate and Other. In 2006, domestic operations included in the business units reflect income tax at the 35% marginal U.S. Federal tax rate, while International reflects the actual tax expense of each country including changes in the international valuation allowance.

- Income (loss) related to limited partnership and limited liability company investments.

- Realized gains (losses) from the domestic property-casualty investment portfolio.

- Fee and other revenues include revenues from the Company's wholly owned subsidiary, Liberty Energy, and lease and other income on investment properties. Liberty Energy generates revenue from the production and sale of oil and gas.

Corporate and Other net written premium by line of business was as follows:

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2007**	**2006**	**Change**	**2007**	**2006**	**Change**
Internal Reinsurance	$64	$30	113.3%	$162	$60	170.0%
Individual life	80	370	(78.4)	144	504	(71.4)
Workers compensation[1]	(48)	(68)	29.4	(135)	(170)	20.6
Total net written premium	$96	$332	(71.1%)	$171	$394	(56.6%)

1 Booked as billed adjustment.

Net written premium for the three and six months ended June 30, 2007 was $96 million and $171 million, respectively, decreases of $236 million and $223 million from the same periods in 2006. The decreases in both periods are due to a decline in Individual life, principally immediate annuity sales, partially offset by an increase in internal reinsurance and a decrease in the workers compensation "booked as billed" adjustment.

Results of Operations – Corporate and Other

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2007**	**2006**	**Change**	**2007**	**2006**	**Change**
Revenues	$445	$697	(36.2%)	$873	$1,085	(19.5%)
PTOI before catastrophes and net incurred losses attributable to prior years	$45	$61	(26.2%)	$47	$88	(46.6%)
Catastrophes[1]	-	1	(100.0)	-	(5)	(100.0)
Net incurred losses attributable to prior years:						
- Asbestos & environmental[2]	-	(1)	(100.0)	-	(3)	(100.0)
- All other[3]	(147)	(52)	182.7	(243)	(85)	185.9
Pre-tax operating income (loss)	(102)	9	NM	(196)	(5)	NM
Realized investment gains, net	46	35	31.4	114	45	153.3
Federal and foreign income tax benefit (expense)	7	(10)	NM	12	15	(20.0)
Net income (loss)	($49)	$34	NM	($70)	$55	NM

1 Catastrophes include all current and prior year catastrophe losses related to the Company's insurance lines and exclude losses related to the Company's external reinsurance assumed lines (assumed voluntary reinsurance and reinsurance assumed through Lloyd's Syndicate 4472) except for losses related to the events of September 11, 2001, the 2004 U.S. hurricanes and the 2005 U.S. hurricanes. In addition, losses related to the 2005 U.S. hurricanes and the 2004 U.S. hurricanes for assumed external reinsurance are reported net of the Company's reasonable assumption of expected catastrophe activity (defined as "net catastrophe reinsurance premium earned"). Internally reinsured catastrophe losses are not reported net of net catastrophe reinsurance premium earned. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

2 Net of allowance for uncollectible reinsurance reduction of zero and $3 million for the three and six months ended June 30, 2007, respectively, and zero for the comparable periods of 2006.

3 Net of amortization of deferred gains on retroactive reinsurance of $6 million and $11 million for the three and six months ended June 30, 2007, respectively, and $5 million and $11 million for the comparable periods of 2006.

NM = Not Meaningful

Revenues for the three and six months ended June 30, 2007 were $445 million and $873 million, respectively, decreases of $252 million and $212 million from the same periods in 2006. The major components of revenues include net premium earned, net investment income, net realized investment gains and losses, and fee and other revenues.

Net premium earned for the three and six months ended June 30, 2007 was $137 million and $261 million, respectively, decreases of $263 million and $303 million from the same periods in 2006. The decreases in both periods primarily reflect lower sales of immediate annuities partially offset by an increase in internal reinsurance earned premium.

Net investment income for the three and six months ended June 30, 2007 was $209 million and $398 million, respectively, a decrease of $1 million and an increase of $32 million versus the same periods in 2006. The increase year-to-date reflects an increase in interest income due primarily to higher invested assets driven by strong cash flow from operations and the proceeds received from the Company's August 2006 and March 2007 debt offerings. The increase also reflects an increase in limited partnership and limited liability company income. These increases in net investment income, however, were constrained by lower yields on the fixed maturity portfolio, due primarily to the Company's increased investment in tax-exempt securities.

Net realized investment gains for the three and six months ended June 30, 2007 were $46 million and $114 million, respectively, increases of $11 million and $69 million over the same periods in 2006. The increase in year-to-date net realized investment gains was primarily driven by gains on foreign equities and lower impairment losses.

Fee and other revenues for the three and six months ended June 30, 2007 were $53 million and $100 million, respectively, an increase of $1 million and a decrease of $10 million from the same periods in 2006. The decrease in year–to-date fee and other revenues is due to a decline in the sale and production of oil and gas from the Liberty Energy subsidiary operation.

Claims, benefits and expenses for the three and six months ended June 30, 2007 were $501 million and $955 million, respectively, decreases of $152 million and $90 million from the same periods in 2006. The decreases in both periods reflect a decrease in policyholder benefits due to the reduction of immediate annuity sales. This decrease was partially offset by an increase in variable incentive compensation and other corporate expenses, an increase in incurred losses attributable to prior years primarily related to workers compensation and higher interest expense related to the Company's March 2007 and August 2006 debt offerings.

Pre-tax operating loss for the three and six months ended June 30, 2007 was $102 million and $196 million, respectively, increases of $111 million and $191 million over the same periods in 2006.

Federal and foreign income tax benefit for the three and six months ended June 30, 2007 was $7 million and $12 million, respectively, an increase of $17 million and a decrease of $3 million from the same periods in 2006. See the Consolidated section for a discussion of taxes.

Net loss for the three and six months ended June 30, 2007 was $49 million and $70 million, respectively, increases of $83 million and $125 million over the same periods in 2006.

INVESTMENTS

General

The Company's investment strategy seeks long-term returns through disciplined security selection, portfolio diversity and an integrated approach to risk management. The Company selects and monitors investments to balance the goals of safety, stability, liquidity, growth and after-tax total return with its need to comply with regulatory investment requirements. A relatively safe and stable income stream is achieved by maintaining a broadly based portfolio of investment grade bonds. These holdings are supplemented by investments in additional asset types with the objective of further enhancing the portfolio's diversification and expected returns. These additional asset types include commercial mortgages and other real estate financing investments, non-investment grade bonds, including syndicated bank loans, common and preferred stock, private equity and direct investments in energy ventures. Risk management is accomplished through asset liability management (including both interest rate risk and foreign currency risk), diversification, credit limits and a careful analytic review of each investment decision.

The Company's investment policy and strategy are reviewed and approved by the Investment Committee of its Board of Directors, which meets on a regular basis to review and consider investment activities, tactics and new investment classes. In addition, the Company has an experienced team of investment personnel responsible for managing and administering the investment portfolios of its domestic and foreign insurance operations.

Invested Assets

The following table summarizes the Company's invested assets by asset category as of June 30, 2007 and December 31, 2006:

$ in Millions	**As of June 30, 2007**		**As of December 31, 2006**	
Invested Assets by Type	**Carrying Value**	**% of Total**	**Carrying Value**	**% of Total**
Fixed maturities, available for sale, at fair value	$42,406	86.8%	$41,102	87.0%
Equity securities, available for sale, at fair value	3,104	6.4	2,619	5.6
Trading securities, at fair value	23	-	22	-
Limited partnerships and limited liability companies	1,704	3.5	1,435	3.0
Commercial mortgage loans	466	1.0	322	0.7
Short-term investments	920	1.9	1,550	3.3
Other investments	209	0.4	211	0.4
Total invested assets	$48,832	100.0%	$47,261	100.0%

Total invested assets as of June 30, 2007 were $48.832 billion, an increase of $1.571 billion or 3.3% over December 31, 2006. This increase reflects strong cash flow from operations, continued growth in investment income, and a portion of the proceeds received from the Company's March 2007 junior subordinated notes offering.

Fixed maturities as of June 30, 2007 were $42.406 billion, an increase of $1.304 billion or 3.2% over December 31, 2006. The increase reflects the aforementioned change in the amount of cash available to invest.

Equity securities, available for sale, as of June 30, 2007 were $3.104 billion, an increase of $485 million ($436 million common stock and $49 million preferred stock) or 18.5% over December 31, 2006. The common stock increase reflects approximately $200 million in additional funding for new investments, the reinvestment of gains and changes in market value.

Limited partnerships and limited liability companies as of June 30, 2007 were $1.704 billion, an increase of $269 million or 18.7% over December 31, 2006. These investments consist of traditional private equity partnerships of $1.159 billion, real estate partnerships of $242 million, and other partnerships (primarily energy) of $303 million. The increase over December 31, 2006 was driven primarily by new investments in real estate limited partnerships as the Company continues to diversify its private equity portfolio. The Company's investments in private equity limited partnerships and limited liability companies are long-term in nature and highly illiquid. The Company believes these investments offer the potential for superior long-term returns and are appropriate in the overall context of a diversified portfolio.

Commercial mortgage loans as of June 30, 2007 were $466 million, an increase of $144 million or 44.7% over December 31, 2006. The increase reflects new investments and is consistent with the Company's diversification strategy.

Short term investments as of June 30, 2007 were $920 million, a decrease of $630 million or 40.6% from December 31, 2006. This decrease from December 31, 2006 was driven by other previously mentioned investment opportunities and liquidity requirements.

As of June 30, 2007, the Company had unfunded commitments in traditional private equity partnerships, real estate partnerships, energy, and commercial mortgage loans of $858 million, $378 million, $451 million, and $183 million, respectively. As of June 30, 2007, the Company had commitments to purchase various residential mortgage-backed securities at a cost and fair market value of $121 million and various corporate and municipal securities at a cost of $50 million (fair market value of $51 million).

As of June 30, 2007, no single issuer, excluding U.S. Treasuries, agency securities and mortgage-backed securities, accounted for more than 1.0% of invested assets.

The following tables summarize the Company's fixed maturity portfolio by security type, credit quality and maturity as of June 30, 2007 and December 31, 2006:

$ in Millions	**As of June 30, 2007**		**As of December 31, 2006**	
Fixed Maturities by Security Type	**Market Value**	**% of Total**	**Market Value**	**% of Total**
U.S. Government and agency securities	$4,423	10.4%	$4,658	11.3%
Mortgage and asset-backed securities	12,409	29.3	12,267	29.8
U.S. state and municipal	7,715	18.2	6,612	16.1
Corporate and other	15,584	36.7	15,354	37.4
Foreign government securities	2,275	5.4	2,211	5.4
Total fixed maturities	$42,406	100.0%	$41,102	100.0%

During the first quarter of 2007, the Company, after consideration of investment opportunities, its tax status, and the current and prospective business environment, continued to increase its tactical allocation to U.S. state and municipal securities. As of June 30, 2007, U.S. state and municipal securities were $7.715 billion, an increase of $1.103 billion or 16.7% over December 31, 2006. This was partially offset by a decline in U.S. Government and agency securities, which totaled $4.423 billion as of June 30, 2007, a decrease of $235 million or 5.0% from December 31, 2006.

$ in Millions	As of June 30, 2007		As of December 31, 2006	
Fixed Maturities by Credit Quality*	**Market Value**	**% of Total**	**Market Value**	**% of Total**
AAA	$22,704	53.6%	$21,954	53.4%
AA+, AA, AA-	6,492	15.3	5,706	13.9
A+, A, A-	6,278	14.8	6,631	16.1
BBB+, BBB, BBB-	3,998	9.4	3,995	9.7
BB+, BB, BB-	1,481	3.5	1,699	4.1
B+, B, B-	1,204	2.8	1,047	2.6
CCC or lower	249	0.6	70	0.2
Total fixed maturities	$42,406	100.0%	$41,102	100.0%

For purposes of this disclosure, credit quality is primarily based upon Standard & Poor's ratings.

The Company's allocation to investment grade securities in total remained unchanged from December 31, 2006.

The Company had 6.9% of its fixed maturity securities invested in non-investment grade securities at June 30, 2007. The Company's holdings of below investment grade securities primarily consist of: (1) an actively managed diversified portfolio of high yield securities and loans within the domestic insurance portfolios; and (2) investments in emerging market sovereign debt primarily in support of the Company's international insurance companies.

$ in Millions	As of June 30, 2007		As of December 31, 2006	
Fixed Maturities by Maturity Date	**Market Value**	**% of Total**	**Market Value**	**% of Total**
1 yr or less	$1,781	4.2%	$1,946	4.7%
Over 1 yr through 5 yrs	8,040	18.9	7,679	18.7
Over 5 yrs through 10 yrs	8,167	19.3	7,937	19.3
Over 10 years	12,009	28.3	11,273	27.5
Mortgage and asset-backed securities	12,409	29.3	12,267	29.8
Total fixed maturities	$42,406	100.0%	$41,102	100.0%

During the first half of 2007, after taking into consideration changes in investment opportunities and its view of the current and prospective business and economic environment, the Company made only minor adjustments to the average life of its investment portfolio.

Net Investment Income

The following table summarizes the Company's net investment income for the three and six months ended June 30, 2007 and 2006:

$ in Millions	Three Months Ended June 30,		Six Months Ended June 30,	
Net Investment Income	**2007**	**2006**	**2007**	**2006**
Taxable interest income	$540	$510	$1,086	$1,008
Tax-exempt interest income	80	46	152	87
Dividends	25	17	42	24
Limited partnerships and limited liability companies[1]	85	87	150	129
Commercial mortgage loans[1]	6	-	11	-
Other investment income	2	2	3	5
Gross investment income	738	662	1,444	1,253
Investment expenses	(28)	(28)	(61)	(59)
Net investment income	$710	$634	$1,383	$1,194

1. *Commercial mortgage loan income previously reported as limited liability income in 2006.*

Net investment income for the three and six months ended June 30, 2007 was $710 million and $1.383 billion, respectively, increases of $76 million and $189 million over the same periods in 2006. The increases in both periods reflect an increase in interest income due primarily to higher invested assets driven by strong cash flow from operations and the proceeds received from the Company's August 2006 and March 2007 debt offerings. Year-to-date results also reflect an increase in limited partnership and limited liability company income. Year-to-date dividend income relates to the increased investment in equity securities. These increases in net investment income, however, were constrained by lower yields on the fixed maturity portfolio, due primarily to the Company's increased investment in tax-exempt securities.

Net Realized Investment Gains (Losses)

The following tables summarize the Company's net realized investment gains (losses) for the three and six months ended June 30, 2007 and 2006:

$ in Millions **Net Realized Investment Gains (Losses)**	**Sales & Dispositions**	**Impairments**	**Change in Trading Security Unrealized**	**Total**
Three Months Ended June 30, 2007:				
Fixed maturities	$3	$-	$ -	$3
Common and preferred stock	29	-	-	29
Other	22	(9)	-	13
Total	$54	($9)	$ -	$45
Three Months Ended June 30, 2006:				
Fixed maturities	$8	($17)	$ -	($9)
Common and preferred stock	32	-	-	32
Other	21	-	-	21
Total	$61	($17)	$ -	$44
Six Months Ended June 30, 2007:				
Fixed maturities	$18	$-	$ -	$18
Common and preferred stock	88	(2)	-	86
Other	36	(15)	-	21
Total	$142	($17)	$ -	$125
Six Months Ended June 30, 2006:				
Fixed maturities	$18	($30)	$ -	($12)
Common and preferred stock	54	(2)	-	52
Other	29	-	-	29
Total	$101	($32)	$ -	$69

$ in Millions	**Three Months Ended June 30,**		**Six Months Ended June 30,**	
Components of Net Realized Investment Gains (Losses)	**2007**	**2006**	**2007**	**2006**
Fixed maturities:				
Gross realized gains	$22	$18	$54	$46
Gross realized losses	(19)	(27)	(36)	(58)
Equities:				
Gross realized gains	30	34	91	60
Gross realized losses	(1)	(2)	(5)	(8)
Other:				
Gross realized gains	22	21	36	30
Gross realized losses	(9)	-	(15)	(1)
Total net realized investment gains (losses)	$45	$44	$125	$69

Net realized investment gains for the three and six months ended June 30, 2007 were $45 million and $125 million, respectively, increases of $1 million and $56 million over the same periods in 2006. The increase year-to-date was primarily driven by a $34 million increase in net gains on equities, primarily by gains on foreign equities, and lower impairment losses.

The following table shows a schedule of the Company's unrealized losses and fair value by security type by duration of potential impairment as of June 30, 2007:

$ in Millions	**Less Than 12 Months**		**Greater Than 12 Months**	
Unrealized Losses & Fair Value by Security Type	**Unrealized Losses**	**Fair Value of Investments with Unrealized Losses**	**Unrealized Losses**	**Fair Value of Investments with Unrealized Losses**
U.S. Government and agency securities	($15)	$1,326	($81)	$2,047
Mortgage and asset-backed securities	(115)	5,574	(293)	4,927
U.S. state and municipal	(182)	6,212	(21)	182
Corporate and other	(180)	6,330	(303)	4,701
Foreign government securities	(32)	1,137	(17)	474
Equities	(16)	332	(4)	35
Total	($540)	$20,911	($719)	$12,366

Unrealized losses increased from $636 million as of December 31, 2006 to $1.259 billion as of June 30, 2007 primarily due to an increase in interest rates. Approximately 93.5% of the unrealized losses ($1.178 billion) exist on holdings where the fair value as of June 30, 2007 was less than 10% below amortized cost. The Company monitors the difference between the amortized cost and estimated fair value of investments to ascertain whether declines in value are temporary in nature. The Company employs a systematic methodology utilizing a quantitative and qualitative process ensuring that available evidence concerning the declines in fair value below amortized cost is evaluated in a disciplined manner.

If the Company believes a decline in the value of a particular investment is temporary, the decline is recorded as an unrealized loss in shareholders' equity. If the decline is believed to be "other-than-temporary," the carrying value of the investment is written down to fair value and a realized loss is recorded. As a result of this review, the Company has concluded that the gross unrealized losses of fixed maturity securities as of June 30, 2007 are temporary.

The gross unrealized losses recorded on common equity securities and other investments at June 30, 2007 resulted primarily from decreases in quoted market values from the dates that certain investment securities were acquired as opposed to fundamental changes in the issuer's financial performance and near-term financial prospects. Therefore, these decreases are also viewed as temporary in accordance with the Company's policy with respect to recognizing impairments in the investment portfolio.

LIQUIDITY AND CAPITAL RESOURCES

General

The liquidity requirements of the insurance subsidiaries are met primarily by funds generated from operations, asset maturities and income received on investments. Cash provided from these sources is used primarily for claims, claim adjustment expenses and operating expenses (underwriting and corporate benefit costs). There are certain cash outflows such as catastrophes and continued settlements of asbestos reserves that are unpredictable in nature and could create increased liquidity needs. The Company believes that the insurance subsidiaries' future business liquidity needs will be met from all the above sources.

Net cash flows are generally invested in marketable securities. The Company invests its net cash flows in fixed income securities and equities while keeping a certain amount in cash and short-term investments to meet unpredictable cash obligations. For ongoing business, the Company monitors the duration of these investments, and purchases and sales are executed with the objective of having adequate cash available to satisfy its maturing liabilities. As the Company's investment strategy focuses on overall asset and liability durations, and not specific cash flows, asset sales may be required to satisfy obligations or rebalance asset portfolios. The Company's invested assets as of June 30, 2007 totaled $48.832 billion.

Short-term debt outstanding at June 30, 2007 and December 31, 2006 was as follows:

$ in Millions	**As of June 30, 2007**	**As of December 31, 2006**
Commercial paper	$ -	$ -
Revolving credit facilities	65	50
Current maturities of long-term debt	2	121
Total short-term debt	$67	$171

Long-term debt outstanding at June 30, 2007 and December 31, 2006 was as follows:

$ in Millions	**As of June 30, 2007**	**As of December 31, 2006**
6.75% Notes, due 2008	$15	$15
5.00% Prudential notes, due 2008	4	4
8.00% Prudential notes—series B due 2013	260	260
5.75% Senior notes, due 2014	500	500
6.70% Senior notes, due 2016	250	250
7.00% Junior subordinated notes due 2067[1]	300	-
8.50% Surplus notes, due 2025	150	150
7.875% Surplus notes, due 2026	250	250
7.63% Notes, due 2028	3	3
7.00% Senior notes, due 2034	250	250
6.50% Senior notes, due 2035	500	500
7.50% Senior notes, due 2036	500	500
7.80% Junior subordinated notes due 2087[2]	700	-
7.697% Surplus notes, due 2097	500	500
7.10% – 7.86% Medium term notes, with various maturities	25	27
Subtotal	4,207	3,209
Unamortized discount	(36)	(34)
Total long-term debt excluding current maturities	$4,171	$3,175

[1] The par value call date and final fixed rate interest payment date is March 15, 2017, subject to certain requirements (see discussion in Liquidity and Capital Resources section).
[2] The par value call date and final fixed rate interest payment date is March 15, 2037, subject to certain requirements (see discussion in Liquidity and Capital Resources section).

The Company issues commercial paper through LMGI. On June 25, 2007, LMGI increased its commercial paper program, guaranteed by LMIC, from $600 million to $1 billion. The program is backed by a $750 million five-year revolving credit facility. To date, no funds have been borrowed under the facility.

On June 15, 2007, LMIC and certain insurance affiliates entered into a $1.25 billion short-term revolving credit facility, guaranteed by LMIC, to facilitate the pending acquisition of Ohio Casualty Corporation by allowing for an optimal liquidation of investment assets. To date, no funds have been borrowed under the facility.

On April 5, 2007, LMGI entered into a $250 million 3-year unsecured revolving credit facility for general corporate purposes. To date, no funds have been borrowed under the facility.

Liberty Corporate Capital Limited entered into a $100 million / €85 million / £65 million 364 day revolving credit facility, which became effective July 31, 2006. The facility is available to provide working capital to the Company's Lloyd's Syndicate business. The 364 day credit facility is guaranteed by LMIC. To date, no funds have been borrowed under the facility.

Liberty Mutual Insurance Europe Limited entered into a $20 million revolving loan facility, which became effective June 9, 2006. The facility is available to provide working capital to the Company's international operations. The revolving loan facility is guaranteed by LMIC. As of June 30, 2007, no borrowings were outstanding under the facility.

The Company also has a Venezuelan subsidiary, Inversora Segucar, C.A., which has entered into a $90 million revolving credit facility to provide liquidity for working capital purposes. Inversora Segucar also has short-term loans outstanding. As of June 30, 2007, total short-term loans and borrowings under the Venezuelan credit facility were approximately $65 million.

The $104 million decrease in short-term debt outstanding is due to the $121 million redemption of the Company's 8.2% Surplus Notes on May 4, 2007. This decrease was partially offset by an increase of $15 million in outstanding borrowings under the Venezuelan credit facility.

On March 7, 2007, LMGI issued junior subordinated notes (the "Notes") with a face amount of $1 billion, consisting of $700 million Series A junior subordinated notes (the "Series A Notes") and $300 million Series B junior subordinated notes (the "Series B Notes"). The Notes are scheduled for redemption on March 15, 2037; the final maturity of the Series A Notes is March 7, 2087; and the final maturity of the Series B Notes is March 7, 2067. LMGI may redeem (a) the Series B Notes in whole or in part, on March 15, 2017 and on each interest payment date thereafter at their principal amount plus accrued and unpaid interest to the date of redemption, or (b) prior to March 15, 2037 for the Series A Notes or March 15, 2017 for the Series B Notes, (i) in whole or in part at any time at their principal amount or, if greater, a make-whole price, or (ii) in certain circumstances, in whole at their principal amount plus accrued and unpaid interest to the date of redemption or, if greater, a special event make-whole price. Interest is payable semi-annually at a fixed rate of 7.800% for the Series A Notes and 7.000% for the Series B Notes up to, but excluding, the final fixed rate interest payment date. In the event the Notes are not redeemed on or before the final fixed rate interest payment date, interest will accrue at an annual rate of three-month LIBOR plus 3.576% for the Series A Notes and three-month LIBOR plus 2.905% for the Series B Notes, payable quarterly in arrears. LMGI has the right to defer interest payments on the Notes for a period up to ten years. Interest compounds during periods of deferral. In connection with the issuance of the Notes, LMGI entered into a replacement capital covenant ("RCC"). As part of the RCC, LMGI agreed that it will not repay, redeem, defease or purchase the Notes on or before the relevant RCC termination date unless, subject to certain limitations, it has received proceeds from the sale of specified capital securities. The RCC will terminate upon the occurrence of certain events, including an acceleration of the Notes, and may not be enforced by the holders of the Series A Notes or the Series B Notes. The RCC is for the benefit of holders of the specified series of LMGI's indebtedness (initially LMGI's 7.50% senior notes due 2036). The $996 million increase in long-term debt outstanding is primarily the result of this offering.

Consolidated interest expense for the six months ended June 30, 2007 was $145 million, representing an increase of $48 million over the same period in 2006.

Holding Company Liquidity and Capital Resources

The Company conducts substantially all of its operations through its wholly owned insurance and service company subsidiaries, and therefore is primarily dependent on dividends, distributions, loans or other payments of funds from these entities to meet its current and future obligations. However, the subsidiaries are separate and distinct legal entities and have no obligation to make funds available to the Company, whether in the form of loans, dividends or other distributions. As of June 30, 2007, the Company, through its downstream subsidiary LMGI, had $3.291 billion of debt outstanding.

The insurance subsidiaries' ability to pay dividends is restricted under applicable insurance laws and regulations. Under the insurance laws of the domiciliary states of the insurance subsidiaries, an insurer may make an ordinary dividend payment if its surplus as regards to policyholders, following such dividend, is reasonable in relation to its outstanding liabilities and adequate to its financial needs. However, no insurer may pay an extraordinary dividend without the approval or non-disapproval of the domiciliary insurance regulatory authority. Under the insurance laws of Massachusetts, the domiciliary state of LMIC, an extraordinary dividend is defined as a dividend whose fair market value, together with other dividends made within the preceding 12 months, exceeds the greater of 10% of the insurer's surplus as regards policyholders as of the preceding December 31, or the insurer's net income for the 12-month period ending on the preceding December 31. Under the insurance laws of Wisconsin, the domiciliary state of Liberty Mutual Fire Insurance Company ("LMFIC") and Employers Insurance Company of Wausau ("EICOW"), an extraordinary dividend is defined as a dividend whose fair market value, together with other dividends paid within the preceding 12 months, exceeds the lesser of (a) 10% of the insurer's surplus as regards policyholders as of the preceding December 31, or (b) the greater of (1) the insurer's net income for the preceding calendar year, minus realized capital gains for that calendar year, or (2) the aggregate of the insurer's net income for the three preceding calendar years minus realized capital gains for those calendar years and minus dividends paid within the first two of the preceding three calendar years. Changes in the extraordinary dividend regulation of the domiciliary states of LMIC, LMFIC and EICOW could negatively affect LMGI's ability to pay principal and interest on the Notes, as could a redomestication, merger or consolidation of LMIC, LMFIC or EICOW to a different domiciliary state.

As of December 31, 2006, the authorized control level risk-based capital and 2007 dividend capacity prior to needing regulatory approval for LMIC, LMFIC and EICOW were as follows:

$ in Millions	**RBC Ratio [1]**			**Dividend Capacity[2]**
RBC Ratios and Dividend Capacity	**2006**	**2005**	**Change**	**2007**
LMIC [3]	554%	495%	59 points	$1,007
LMFIC	579%	596%	(17 points)	$69
EICOW [3]	395%	370%	25 points	$121

[1] Authorized control level risk-based capital as defined by the NAIC.
[2] Represents maximum allowable dividend without prior regulatory approval in the state of domicile.
[3] Any reallocation of surplus between insurance subsidiaries could change the dividend capacity of individual companies within the group. Effective January 1, 2007, the EICOW pooling percentage decreased from 16.0% to 10.0% and LMIC's pooling percentage increased accordingly.

LMGI also has access to funds at Liberty Corporate Services LLC ("Corporate Services"). Through its subsidiaries, Corporate Services collects fees and other revenues, primarily for claims administration and agency services rendered for affiliated and non-affiliated entities. For the six months ended June 30, 2007, Corporate Services recorded $144 million in pre-tax income.

Statutory Surplus

Statutory surplus as regards policyholders for the combined operations of LMIC and its U.S. affiliates including international branches was $13.547 billion and $12.131 billion at June 30, 2007, and December 31, 2006, respectively. The increase in surplus reflects net income of $221 million (the sum of earnings from the Company's 43 domestic insurance companies and dividends from subsidiaries), capital contributions from the parent, LMGI, of $951 million, affiliated unrealized gains of $206 million, and unaffiliated unrealized gains of $150 million, partially offset by the redemption of surplus notes of $121 million. The balance of the increase in statutory surplus primarily reflects changes in deferred taxes, foreign exchange, and non-admitted assets.

CRITICAL ACCOUNTING POLICIES

Critical Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. The Company's principal estimates include:

- unpaid claims and claim adjustment expense reserves, including asbestos and environmental liability reserves and loss sensitive premium attributable to prior years;
- reinsurance recoverables and associated uncollectible reserves;
- impairments to the fair value of the investment portfolio;
- variable interest entities;
- deferred acquisition costs;
- valuation of goodwill; and
- deferred income tax valuation allowance.

While the Company believes the amounts included in the consolidated financial statements reflect best estimates and appropriate assumptions, these amounts could ultimately be materially different from the amounts currently provided for in the consolidated financial statements.

Certain reclassifications have been made to the 2006 tables to conform to the 2007 tables.

Adoption of New Accounting Standards

In June 2006, the FASB issued Interpretation No. 48, "*Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement No. 109*" ("FIN 48"). FIN 48 requires companies to recognize the tax benefits of uncertain tax positions only where the position is "more likely than not" to be sustained assuming examination by tax authorities. The amount recognized is the amount that represents the largest amount of tax benefit that is greater than 50% likely of being ultimately realized. A liability is recognized for any benefit claimed, or expected to be claimed, in a tax return in excess of the benefit recorded in the financial statements, along with any interest and penalty (if applicable) on the excess. FIN 48 requires a tabular reconciliation of the change in the aggregate unrecognized tax benefits claimed, or expected to be claimed, in tax returns and disclosure relating to accrued interest and penalties for unrecognized tax benefits. Discussion is also required for those uncertain tax positions where it is reasonably possible that the estimate of the tax benefit will change significantly in the next 12 months.

The Company adopted the provisions of FIN 48 on January 1, 2007. As a result of the adoption, the Company recognized a decrease of approximately $11 million in the liability for unrecognized tax benefits, which was accounted for as an increase to retained earnings.

As of the date of adoption of FIN 48, the total amount of unrecognized tax benefits was approximately $107 million, including approximately $85 million related to tax positions that would impact the annual effective rate. The Company recognizes interest and penalties related to unrecognized tax benefits in Federal and foreign income tax expense and had approximately $39 million accrued as of January 1, 2007. The Company does not expect any material changes to the unrecognized benefits within 12 months of the reporting date.

The IRS is currently reviewing the Company's federal tax returns for the 1999 through 2003 tax years. Any adjustments that may result from the IRS examination of these income tax returns are not expected to have a material impact on the financial position, liquidity or results of operations of the Company.

In September 2005, the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants ("AcSEC") issued Statement of Position No. 05-1, "*Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts*" ("SOP 05-1"). This SOP provides guidance on accounting by insurance enterprises for deferred acquisition costs on internal replacements of insurance and investment contracts other than those specifically described in FASB Statement No. 97, "*Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments*" ("FAS 97"). As defined by the SOP, an internal replacement is a modification in product benefits, features, rights, or coverage that occurs by exchange of a contract for a new contract, or by amendment, endorsement, rider, or by election of a feature or coverage within an existing contract. The Company adopted SOP 05-1 on January 1, 2007. The adoption of SOP 05-1 did not have a material impact the Company's consolidated financial statements.

In February 2006, the FASB released Statement of Financial Accounting Standards No. 155, "*Accounting for Certain Hybrid Financial Instruments - an Amendment of FASB Statements No. 133 and 140*" ("SFAS 155"). SFAS 155 nullifies the guidance in the FASB's Derivatives Implementation Group Issue D1 "*Application of Statement 133 to Beneficial Interests in Securitized Assets*," which had deferred the bifurcation requirements of Statement of Financial Accounting Standards No. 133, "*Accounting for Derivative Instruments and Hedging Activities*" ("SFAS 133"), for certain beneficial interests in securitized financial assets. SFAS 155 requires beneficial interests in securitized financial assets be analyzed to determine whether they are freestanding derivatives or hybrid instruments that contain an embedded derivative requiring bifurcation. SFAS 155 is effective for all financial instruments acquired, issued or subject to a re-measurement (new basis) event occurring after the beginning of an entity's fiscal year that begins after September 15, 2006. In January 2007, the FASB issued Derivative Implementation Group Issue No. B40, "*Embedded Derivatives: Application of Paragraph 13(b) to Securitized Interests in Prepayable Financial Assets*" ("DIG B40"). DIG B40 provided limited exemption from bifurcation of embedded derivatives as required by paragraph 13(b) of SFAS 133. The Company adopted SFAS 155 on January 1, 2007. Management has concluded the exemption applies for the Company's investment in its mortgage backed securities and as a result, adoption of SFAS 155 did not have a material impact to the Company's consolidated financial statements.

Future Adoption of New Accounting Standards

In September 2006, the FASB issued SFAS No. 157, "*Fair Value Measurements*" ("SFAS 157"). This statement defines fair value, establishes a framework for measuring fair value under accounting principles generally accepted in the United States, and enhances disclosures about fair value measurements. SFAS 157 provides guidance on how to measure fair value when required under existing accounting standards. The statement establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels ("Level 1, 2 and 3"). Level 1 inputs are observable inputs that reflect quoted prices for identical assets or liabilities in active markets the Company has the ability to access at the measurement date. Level 2 inputs are observable inputs, other than quoted prices included in Level 1, for the asset or liability. Level 3 inputs are unobservable inputs reflecting the reporting entity's estimates of the assumptions that market participants would use in pricing the asset or liability (including assumptions about risk). Quantitative and qualitative disclosures will focus on the inputs used to measure fair value for both recurring and non-recurring fair value measurements and the effects of the measurements in the financial statements. The Company is required to adopt SFAS 157 effective January 1, 2008. The Company is in the process of evaluating the impact of adoption.

In September 2006, the FASB issued SFAS No. 158, "*Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an Amendment of FASB Statements No. 87, 88, 106 and 132(R)*" ("SFAS

158”). This statement requires an entity to: (a) recognize an asset for the funded status of defined benefit plans that are over-funded and a liability for plans that are under-funded, measured as of the employer’s fiscal year end; and (b) recognize changes in the funded status of defined benefit plans, other than for the net periodic benefit cost included in net income, in accumulated other comprehensive income. For pension plans the funded status must be based on the projected benefit obligation, which includes an assumption for future salary increases. For postretirement plans the funded status is based on the accumulated postretirement benefit obligation. The Company is required to adopt SFAS 158 effective December 31, 2007. The actual impact to the Company will depend on the discount rate, other valuation assumptions, and the actual value of plan assets as of December 31, 2007. The impact is expected to be less than 5% of equity.

In February 2007, the FASB issued SFAS No. 159, “*The Fair Value Option for Financial Assets and Financial Liabilities, Including an Amendment of SFAS 115*” (“SFAS 159”). SFAS 159 permits all entities to choose, at specified election dates, to measure eligible items at fair value (the “fair value option”). An entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date eliminating complex hedge accounting provisions. The decision about whether to elect the fair value option is applied on an instrument by instrument basis and is irrevocable unless a new election date occurs and is applied only to an entire instrument. SFAS 159 also provides guidance on disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. SFAS 159 is effective for the Company January 1, 2008. The Company is in the process of evaluating the impact of adoption.

In September 2006, the Emerging Issues Task Force (EITF) released, issue No. 06-4, “*Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements”* (“EITF 06-4”). This issue requires a company to recognize a liability for future life insurance benefits in accordance with SFAS 106 or Opinion 12. EITF 06-4 is effective for the Company for fiscal years beginning after December 15, 2007. The Company is in the process of evaluating the impact of adoption but it is not expected to be material.

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. The effects of these changes are reflected in current operating results.

Unpaid Claims and Claim Adjustment Expenses

Reserves for property-casualty unpaid claims and claim adjustment expenses were $39.495 billion and $38.606 billion at June 30, 2007 and December 31, 2006, respectively. The increase was primarily due to business growth less the on-going settlement of claims.

Property-casualty insurance unpaid claims and claim adjustment expenses 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 development patterns. Consideration is given to such historical patterns as field reserving trends and claims settlement practices, loss payments, pending levels of unpaid claims and product mix, as well as court decisions, economic conditions and public attitudes. All of these factors can affect the estimation of reserves.

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 litigated cases, medical costs, and cost of repair materials and labor rates can all affect ultimate claim costs. In addition, the span of time between the incidence of a loss and the payment or settlement of the claim can be a critical part of reserving determinations and will cause more variability in the ultimate claim cost. 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.

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. The effects of these changes are reflected in current operating results.

Asbestos and Environmental

The Company’s asbestos and environmental (A&E) reserves for unpaid claims and claim adjustment expenses net of reinsurance and including an allowance for uncollectible accounts were $1.243 billion and $1.386 billion at June 30, 2007 and December 31, 2006, respectively. The decline in reserves is primarily due to the ongoing settlement of asbestos and environmental claims.

All A&E claims against policies issued prior to 1986 by EICOW and its affiliates are 100% ceded to Nationwide Indemnity Company and guaranteed by Nationwide Mutual Insurance Company. In addition, the Company’s 2003 acquisition of PruPac included $190 million and $130 million of gross and net A&E reserves, respectively. Any increase in A&E reserves related to PruPac is reinsured by Vantage Casualty Insurance Company and guaranteed by Prudential Financial Inc. The Company had paid losses associated with these reserves of $30 million for the six months ended June 30, 2007 and $61 million for the year ended December 31, 2006.

The estimation of asbestos claims and associated liabilities and the analysis of environmental claims considered prevailing applicable law and certain inconsistencies of court decisions as to coverage, plaintiffs’ expanded theories of liability, and the risks inherent in major litigation and other uncertainties; the Company believes that in future periods it is possible that the outcome of the continued uncertainties regarding asbestos and environmental related claims could result in liability that differs from current reserves by an amount that could be material to the Company’s future operating results and financial condition.

Reinsurance Recoverables

The Company reported reinsurance recoverables of $15.258 billion and $15.564 billion at June 30, 2007 and December 31, 2006, respectively, net of allowance for doubtful accounts. The decrease is primarily due to the ongoing settlement of 2005 hurricane claims and the continued payout of losses and expenses related to Nationwide’s discontinued operations.

The reinsurance recoverables from Nationwide Indemnity Co. have been fully guaranteed by its parent, Nationwide Mutual Insurance Co., which has a financial strength rating of A+ from Standard & Poor’s and A+ from A.M. Best. The reinsurance recoverables from state mandated involuntary pools and associations represent the Company’s servicing carrier business. As a servicing carrier, the Company retains no direct underwriting risk but instead cedes 100% of the involuntary market premium and losses back to the pool. Payment of losses is shared by the pool participants in proportion to their pool participation. Credit risk with respect to this servicing carrier business is the composite of the cumulative creditworthiness of all participants in their respective pools.

As part of its reinsurance security oversight, the Company has established a Reinsurance Credit Committee that meets quarterly to monitor and review the credit quality of the existing reinsurance portfolio, discuss emerging trends in the reinsurance marketplace, and ensure that the current portfolio of reinsurance is in compliance with the committee’s security standards. The committee is directly responsible for establishing the rating, collateral, and diversification requirements governing the Company’s purchase and use of reinsurance.

Approximately 95% of the Company's reinsurance recoverable balance, net of collateral held and including voluntary and involuntary pools and associations, was placed with reinsurers rated A- or better from A.M. Best at June 30, 2007. Collateral held against outstanding gross reinsurance recoverable balances was $4.997 billion and $4.802 billion at June 30, 2007 and December 31, 2006, respectively.

The remaining 5% of the Company's net reinsurance recoverable balance is well diversified. No single reinsurer rated B++ or below by A.M. Best accounts for more than 2% of statutory surplus as regards policyholders. In addition, the average net reinsurance recoverable balance from individual reinsurers rated below A- or not rated by A.M. Best was approximately $1 million as of June 30, 2007.

The Company evaluates and monitors the financial condition of its reinsurers under voluntary reinsurance arrangements to minimize its exposure to significant losses from reinsurer insolvencies. The Company reports its reinsurance recoverables net of an allowance for estimated uncollectible reinsurance recoverables. The allowance is based upon the Company's ongoing review of amounts outstanding, length of collection periods, changes in reinsurer credit standing and other relevant factors. Accordingly, the establishment of reinsurance recoverables and the related allowance for uncollectible reinsurance recoverables is also an inherently uncertain process involving estimates. Changes in these estimates could result in additional income statement charges.

The Company is party to retroactive reinsurance arrangements where a significant portion of the consideration was retained on a "funds held" basis and interest is credited on the balance at a weighted average rate of approximately 7.7% annually. These contracts resulted in deferred gains (including experience related profit accruals of $195 million as of June 30, 2007 and December 31, 2006) that are amortized into income using the effective interest method over the estimated settlement periods. At June 30, 2007 and December 31, 2006, deferred gains related to these reinsurance arrangements were $817 million and $839 million, respectively, and are included in other liabilities within the consolidated balance sheets. Interest credited to the funds held balances for the three and six months ended June 30, 2007 was $29 million and $57 million, respectively, as compared to $27 million and $52 million, for the three and six months ended June 30, 2006, respectively. Amortization of the deferred gain for the three and six months ended June 30, 2007 was $13 million and $29 million, respectively, as compared to $14 million and $30 million, for the three and six months ended June 30, 2006, respectively. Reinsurance recoverables related to these transactions, including experience related profit accruals, were $2.250 billion and $2.258 billion as of June 30, 2007 and December 31, 2006, respectively.

Additionally, the Company has an aggregate stop loss program covering substantially all of Commercial Markets and the Wausau market segment voluntary workers compensation business from the fourth quarter 2000 through the fourth quarter 2002 accident year periods. Under these contracts, losses in excess of a specified loss ratio are reinsured up to a maximum loss ratio and were accounted for as prospective reinsurance at inception. However, due to a material contract change at the January 1, 2002 renewal, premium and loss activity subsequent to December 31, 2001 is now accounted for as retroactive reinsurance for coverage provided from the fourth quarter 2000 through the fourth quarter 2001 covered accident year periods. The retroactive portion of the aggregate stop loss program is included in the preceding paragraph.

In 2006, LMIC entered into multi-year property catastrophe reinsurance agreements with Mystic Re Ltd. ("Mystic Re"), a Cayman Islands domiciled reinsurer, to provide $525 million of additional reinsurance coverage for LMIC and its affiliates in the event of a Northeast hurricane. The reinsurance agreements are fully collateralized by proceeds received by Mystic Re from the issuance of catastrophe bonds and provide coverage for hurricane-related losses from Washington, D.C. to Maine based on industry-insured losses as reported by Property Claim Services. In 2007, LMIC supplemented this reinsurance in a similar transaction with Mystic Re II Ltd. ("Mystic Re II"); a Cayman Islands domiciled reinsurer, to provide $150 million of additional reinsurance coverage for LMIC and its affiliates in the event of a Northeast and/or Florida hurricane event. The Company has not recorded any recoveries under these programs. Neither Mystic Re nor Mystic Re II has any other reinsurance in force.

Impairment Losses on Investments

The total impairment losses on investments for the three and six months ended June 30, 2007 were $9 million and $17 million, respectively, decreases of $8 million and $15 million over the same periods in 2006. Unrealized losses that are other-than-temporary are recognized as realized losses. The Company's accounting policy for other-than-temporary impairment recognition requires other-than-temporary impairment charges to be recorded when it is determined that the Company is unlikely to recover its cost basis in an investment in the near-term. Factors considered in evaluating whether a decline in value is other-than-temporary include: (a) the length of time and extent to which the fair value has been below cost; (b) the financial condition and near-term prospects of the issuer; and (c) the intent and ability of the Company to retain the investment for a period of time sufficient to allow for any anticipated recovery. In addition, for securities expected to be sold, an other-than-temporary impairment charge is recognized if the Company does not expect the fair value of a security to recover to cost or amortized cost prior to the expected date of sale.

The Company employs a systematic methodology to evaluate declines in fair value below the book value for equity securities and other investments. The methodology utilizes a quantitative and qualitative process ensuring that available evidence concerning the declines in fair value below carrying value is evaluated in a disciplined manner. Based on that evaluation and the Company's ability and intent to hold these investments for a reasonable period of time sufficient for a recovery of fair value, the Company views the decline in market value of these investments as being temporary in accordance with the Company's impairment policy. However, the Company reserves the flexibility to trade any investment as deemed appropriate based on changes in credit or other market factors in managing the invested assets positions of the Company.

Variable Interest Entities

In January 2003, the FASB issued Interpretation No. 46, *"Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51"* ("FIN 46"). The Company's exposure to investment structures subject to analysis under FIN 46(R), relate primarily to investments in energy, private equity, and real estate limited partnerships that are accounted for under the equity method. The Company consolidates 2 VIEs in the energy investment sector in its 2007 and 2006 financial statements; the Company has been deemed to be the primary beneficiary. In addition, the Company has investments in 35 VIEs for which it is not the primary beneficiary at June 30, 2007. The Company's investments in VIEs were $255 million and $208 million at June 30, 2007 and December 31, 2006, respectively. The Company's maximum exposure to losses from VIEs is $598 million and $481 million as of June 30, 2007 and December 31, 2006, respectively, and there is no recourse provision to the general credit of the Company beyond the full amount of the Company's loss exposure.

Derivatives

The Company has a Derivative Use Policy, which has been approved by the Investment Committee. Pursuant to the policy, the Company may enter into derivative transactions. As of June 30, 2007, the Company had several embedded derivative instruments in its portfolio, warrants and two interest rate swaps acquired with the assets and liabilities of the Genesis life insurance business. As of June 30, 2007, the value of these instruments was $12 million. The Company recognized approximately $6 million in net realized investment gains through June 30, 2007 driven by changes in fair value of derivative instruments, primarily warrants.

Deferred Policy Acquisition Costs

Total deferred policy acquisition costs were $1.785 billion and $1.662 billion as of June 30, 2007 and December 31, 2006, respectively. Deferred policy acquisition costs are costs that vary with, and are primarily related to, the acquisition of new and renewal insurance and investment contracts that are deferred and amortized over the respective policy terms. Deferred acquisition costs are reviewed annually for recoverability. Investment income is considered in the recoverability assessment. For short-duration insurance contracts, acquisition costs include commissions, underwriting expenses, and premium taxes and assessments. For long-duration insurance contracts, these costs include first year commissions in excess of annual renewal commissions and variable sales, underwriting and administrative expenses.

Goodwill and Intangibles

Goodwill and intangible assets were $937 million and $907 million at June 30, 2007 and December 31, 2006, respectively.

Deferred Income Taxes

The net deferred income tax asset was $1.602 billion and $1.490 billion as of June 30, 2007 and December 31, 2006, respectively, net of a valuation allowance of $107 million and $101 million, respectively. Management believes it is more likely than not that the Company's net deferred income tax asset will be realized based on the Company's ability and likelihood of generating future taxable income.

The income tax provision is calculated under the liability method. Deferred tax assets and liabilities are recorded based on the difference between the financial statement and tax bases of assets and liabilities at the enacted tax rates. The principal assets and liabilities giving rise to such differences are unrealized capital gains and losses on certain investments, insurance loss reserves, unearned premiums, deferred policy acquisition costs, employee benefits, net operating losses, and alternative minimum tax credits.

The IRS is currently reviewing the Company's federal tax returns for the 1999 through 2003 tax years. Any adjustments that may result from the IRS examination of these income tax returns are not expected to have a material impact on the financial position, liquidity or results of operations of the Company.

About the Company

Boston-based Liberty Mutual Holding Company Inc., the parent corporation of the Liberty Mutual Group of entities ("LMG" or the "Company"), is a diversified global insurer and sixth largest property and casualty insurer in the U.S. based on 2006 direct written premium. The Company also ranks 95th on the Fortune 500 list of largest corporations in the United States based on 2006 revenue. As of December 31, 2006, LMG had $85.498 billion in consolidated assets, $74.603 billion in consolidated liabilities, and $23.520 billion in annual consolidated revenue.

LMG, through its subsidiaries and affiliated companies, offers a wide range of property-casualty insurance products and services to individuals and businesses alike. In 2001 and 2002, the Company formed a mutual holding company structure, whereby the three principal mutual insurance companies, LMIC, LMFIC and EICOW, each became separate stock insurance companies under the ownership of Liberty Mutual Holding Company Inc.

Functionally, the Company conducts its business through four SBUs: Personal Markets, Commercial Markets, Agency Markets and International. Each business unit operates independently of the others and has dedicated sales, underwriting, claims, actuarial, financial and certain information technology resources. Management believes this structure allows each business unit to execute its business strategy and/or to make acquisitions without impacting or disrupting the operations of the Company's other business units.

LMG employs over 39,000 people in more than 900 offices throughout the world. For a full description of the Company's business operations, products and distribution channels, please visit Liberty Mutual's Investor Relations web site at www.libertymutual.com/investors.