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

Quarter Ended June 30, 2008

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, 2008 and 2007. This Management's Discussion & Analysis of Financial Condition and Results of Operations ("MD&A") should be read in conjunction with the Company's 2007 Annual Report, Second Quarter 2008 Consolidated Financial Statements (unaudited) and Second Quarter 2008 Financial Supplement 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 or maintain market share 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 automobile 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 Company's ability to successfully integrate operations, personnel and technology from its acquisitions, including the recent acquisition of Ohio Casualty Corporation and its subsidiaries, and the proposed acquisition of Safeco Corporation and its subsidiaries, in accordance with its business strategy; 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 2008 - Consolidated Results of Operations

- Revenues for the three months ended June 30, 2008 were $6.948 billion, an increase of $653 million or 10.4% over the same period in 2007.
- Net written premium for the three months ended June 30, 2008 was $6.279 billion, an increase of $802 million or 14.6% over the same period in 2007.
- Pre-tax income for the three months ended June 30, 2008 was $412 million, a decrease of $86 million or 17.3% from the same period in 2007. Results in the period reflect a decrease in realized investment gains of $40 million.
- Net income for the three months ended June 30, 2008 was $300 million, a decrease of $39 million or 11.5% from the same period in 2007.
- Cash flow from operations for the three months ended June 30, 2008 was $1.079 billion, an increase of $292 million or 37.1% over the same period in 2007.
- The combined ratio before catastrophes[1] and net incurred losses attributable to prior years[2] for the three months ended June 30, 2008 was 98.0%, an increase of 1.5 points over the same period in 2007. 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, 2008 increased 1.8 points to 101.9%.

Six Months Ended June 30, 2008 - Consolidated Results of Operations

- Revenues for the six months ended June 30, 2008 were $13.833 billion, an increase of $1.395 billion or 11.2% over the same period in 2007.
- Pre-tax income for the six months ended June 30, 2008 was $892 million, a decrease of $106 million or 10.6% from the same period in 2007. Results in the period reflect a decrease in realized investment gains of $132 million.
- Net income for the six months ended June 30, 2008 was $660 million, a decrease of $29 million or 4.2% from the same period in 2007.
- Cash flow from operations for the six months ended June 30, 2008 was $1.692 billion, a decrease of $104 million or 5.8% from the same period in 2007.
- The combined ratio before catastrophes and net incurred losses attributable to prior years for the six months ended June 30, 2008 was 98.5%, an increase of 0.7 points over the same period in 2007. 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, 2008 increased 0.7 points to 101.3%.

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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.

[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, 2008

- Total assets were $99.877 billion as of June 30, 2008, an increase of $5.135 billion over December 31, 2007.

- Policyholders' equity was $12.265 billion as of June 30, 2008, a decrease of $101 million from December 31, 2007.

- Statutory surplus as regards policyholders for the combined operations of Liberty Mutual Insurance Company ("LMIC") and its U.S. affiliates was $15.371 billion as of June 30, 2008, an increase of $1.216 billion from December 31, 2007.

Other 2008 2nd Quarter Highlights

Acquisitions and New Markets

- On April 23, 2008, LMG and Safeco Corporation ("Safeco") announced that they entered into a definitive agreement pursuant to which LMG, through its subsidiaries, will acquire all outstanding shares of common stock of Safeco for $68.25 per share or approximately $6.2 billion. The proposed transaction, which has been approved by the Boards of Directors of both companies, is subject to approval by Safeco's shareholders and customary regulatory approvals and conditions. The transaction is targeted to close in the third quarter of 2008. On July 14, 2008, LMG reaffirmed its commitment to consummate the acquisition.

- On June 29, 2008, Liberty Insurance Company Limited ("LICL"), a wholly owned subsidiary of LMG, was granted approval to establish a branch in Beijing by the China Insurance Regulatory Commission. Beijing is the first branch established by LICL in China and will offer various personal lines products, including auto and a wide range of commercial lines products with a focus on small-to-medium enterprises.

Rating Actions

- On April 23, 2008, A.M. Best Co. affirmed the A (Excellent) financial strength rating of LMIC and its related property/casualty companies following the announcement that LMG had reached a definitive agreement to acquire all outstanding shares of Safeco's common stock. The outlook was stable.

- On April 23, 2008, Moody's Investors Service affirmed the debt and insurance financial strength ratings of Liberty Mutual Group Inc. ("LMGI") and its subsidiaries following the announcement that LMG had reached a definitive agreement to acquire all outstanding shares of Safeco's common stock. The outlook for all of LMG's long-term ratings was changed to negative, from stable.

- On April 23, 2008, Standard & Poor's Rating Service placed LMGI's 'A' counterparty credit and financial strength ratings on CreditWatch negative following the announcement that LMG had reached a definitive agreement to acquire all outstanding shares of Safeco's common stock. The Company expects to meet with Standard & Poor's to discuss in more detail its plans for integrating Safeco into Agency Markets and the anticipated impact on LMG's capital position.

Debt Transactions

- On May 29, 2008, LMGI issued $1.25 billion of 10.75% Series C junior subordinated notes having a final maturity of 2088 and a final fixed rate interest payment date of 2038. This security receives high levels of equity treatment by the rating agencies. The proceeds from the offering are being used to finance the Safeco transaction.

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 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. 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	**2008**	**2007**	**Change**	**2008**	**2007**	**Change**
Private passenger automobile	$1,887	$1,592	18.5%	$3,568	$3,038	17.4%
Workers compensation	1,183	1,119	5.7	2,616	2,604	0.5
Homeowners	557	501	11.2	1,008	896	12.5
Commercial multiple peril / Fire	477	405	17.8	948	804	17.9
International local businesses	404	325	24.3	833	679	22.7
Commercial automobile	351	275	27.6	681	563	21.0
General liability	277	210	31.9	619	466	32.8
LIU[1] reinsurance	206	238	(13.4)	533	581	(8.3)
LIU third party	230	138	66.7	330	263	25.5
LIU inland marine program	157	133	18.0	302	264	14.4
Group disability and life	140	117	19.7	277	233	18.9
Bond	94	78	20.5	182	144	26.4
LIU first party	70	76	(7.9)	133	147	(9.5)
Individual Life	66	80	(17.5)	119	144	(17.4)
Assumed voluntary reinsurance	20	28	(28.6)	75	59	27.1
Other	160	162	(1.2)	311	279	11.5
Total net written premium[2]	$6,279	$5,477	14.6%	$12,535	$11,164	12.3%

1 Liberty International Underwriters (LIU).
2 Net written premium associated with internal reinsurance has been re-allocated to the appropriate lines of business in the above table.

Consolidated net written premium by SBU was as follows:

$ in Millions	Three Months Ended June 30, 2008	2007	Change	Six Months Ended June 30, 2008	2007	Change
Personal Markets[1]	$1,539	$1,518	1.4%	$2,884	$2,837	1.7%
Commercial Markets	1,410	1,303	8.2	3,139	3,016	4.1
Agency Markets	1,600	1,256	27.4	3,177	2,477	28.3
International	1,705	1,384	23.2	3,282	2,807	16.9
Corporate and Other[2]	25	16	56.3	53	27	96.3
Total net written premium (NWP)	$6,279	$5,477	14.6%	$12,535	$11,164	12.3%
Foreign exchange effect on growth			2.1			2.0
NWP growth excluding foreign exchange			12.5%			10.3%

1 Effective January 1, 2008, individual life, previously included in Corporate and Other, is now included with the Personal Markets segment. All prior periods have been restated.

2 Includes internal reinsurance.

Net written premium for the three and six months ended June 30, 2008 was $6.279 billion and $12.535 billion, respectively, increases of $802 million and $1.371 billion over the same periods in 2007. Significant changes by major line of business include:

- Private passenger automobile net written premium, including internal reinsurance premium, increased $295 million and $530 million in the quarter and year-to-date, respectively. The increases in both periods primarily reflect organic growth in all of International's local businesses in Latin America, the acquisitions of Ohio Casualty Corporation ("Ohio Casualty"), approximately $59 million and $123 million of premium in the quarter and year-to-date, respectively, and Brazilian insurer Indiana Seguros, approximately $49 million and $84 million of premium in the quarter and year-to-date, respectively, and the strengthening of foreign currencies versus the U.S. dollar ($69 million and $133 million in the quarter and year-to-date, respectively). The increase also reflects strong customer retention and new business growth in both Personal Markets and Agency Markets. These increases were partially offset by lower average premium per policy in Personal Markets due primarily to mandatory rate decreases in Massachusetts, which became effective in April 2007.
- Workers compensation net written premium, including internal reinsurance premium, increased $64 million and $12 million in the quarter and year-to-date, respectively. The increase in the quarter primarily reflects new business premium of $48 million related to a construction account with a multi-year exposure written in Commercial Markets' National Market segment. Both periods were also impacted by approximately $31 million and $62 million of premium related to the Ohio Casualty acquisition in the quarter and year-to-date, respectively. Partially offsetting the increases in both periods were rate decreases in both Agency Markets and Commercial Markets and lower retention in Commercial Markets due to a more competitive environment, a decrease in Summit's premium due to both mandated rate decreases in Florida and lower audit and retrospectively rated premium. Both periods also include an adjustment to the Corporate and Other segment for the "booked as billed" method of accounting for net written premium.
- Homeowners net written premium, including internal reinsurance premium, increased $56 million and $112 million in the quarter and year-to-date, respectively. The increases in both periods primarily reflect approximately $36 million and $65 million of premium related to the Ohio Casualty acquisition in the quarter and year-to-date, respectively, and strong customer retention and new business growth, primarily in non-coastal areas, in both Personal Markets and Agency Markets. The increase in both periods also reflects the impact of rate increases in Personal Markets.
- Commercial multiple peril / fire, including internal reinsurance premium, increased $72 million and $144 million in the quarter and year-to-date, respectively. The increases in both periods

primarily reflect approximately $85 million and $169 million of premium related to the Ohio Casualty acquisition in the quarter and year-to-date, respectively, improved retention in Commercial Markets and a reduction in the utilization of ceded reinsurance in Commercial Markets' Liberty Mutual Property segment as compared to 2007. These increases were offset by rate decreases in both Commercial Markets and Agency Markets due to a more competitive environment and lower retention in Agency Markets.

- International local businesses net written premium (excluding private passenger automobile), including internal reinsurance premium, increased $79 million and $154 million in the quarter and year-to-date, respectively. The increases in both periods primarily reflect organic growth in International's local businesses in Latin America and the strengthening of foreign currencies versus the U.S. dollar ($32 million and $58 million in the quarter and year-to-date, respectively).
- Commercial automobile net written premium, including internal reinsurance premium, increased $76 million and $118 million in the quarter and year-to-date, respectively. The increases in both periods primarily reflect approximately $68 million and $130 million of premium related to the Ohio Casualty acquisition in the quarter and year-to-date, respectively, and a higher amount of audit and retrospective premium in Commercial Markets' National Market segment, partially offset by modest rate decreases and lower retention in both Commercial Markets and Agency Markets.
- General liability net written premium, including internal reinsurance premium, increased $67 million and $153 million in the quarter and year-to-date, respectively. The increases in both periods reflect approximately $27 million and $52 million of premium related to the Ohio Casualty acquisition in the quarter and year-to-date, respectively, partially offset by modest rate decreases due to a more competitive environment. Also impacting the year-to-date increase was a new business premium of approximately $43 million related to a construction account with a multi-year exposure written in Commercial Markets' National Market segment in the first quarter of 2008.
- LIU reinsurance net written premium, including internal reinsurance premium, decreased $32 million and $48 million in the quarter and year-to-date, respectively. The decreases in both periods primarily reflect a decline in rates as a result of a more competitive environment.
- LIU third party net written premium, including internal reinsurance premium, increased $92 million and $67 million in the quarter and year-to-date, respectively. The increases in both periods primarily reflect a decrease in ceded written premium due to a change in the structure of a reinsurance program, partially offset by a decline in rates as a result of a more competitive environment.
- LIU inland marine program net written premium increased $24 million and $38 million in the quarter and year-to-date, respectively. The increases in both periods are primarily due to International's continued expansion in this line of business.
- Group disability and life net written premium increased $23 million and $44 million in the quarter and year-to-date, respectively, due primarily to the impact of broader market penetration.
- Bond net written premium, including internal reinsurance premium, increased $16 million and $38 million in the quarter and year-to-date respectively, primarily due to approximately $17 million and $31 million of premium related to the Ohio Casualty acquisition in the quarter and year-to-date, respectively.
- LIU first party net written premium, including internal reinsurance premium, decreased $6 million and $14 million in the quarter and year-to-date, respectively. The decreases in both periods are primarily due to a decline in rates and lower retention as a result of more a competitive environment.
- Individual life net written premium decreased $14 million and $25 million in the quarter and year-to-date, respectively, primarily due to lower immediate annuity and structured settlement sales.

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

$ in Millions	Three Months Ended June 30, 2008	2007	Change	Six Months Ended June 30, 2008	2007	Change
Revenues	$6,948	$6,295	10.4%	$13,833	$12,438	11.2%
PTOI before catastrophes and net incurred losses attributable to prior years	$632	$638	(0.9)	$1,215	$1,152	5.5
Catastrophes[1]	(313)	(122)	156.6	(479)	(181)	164.6
Net incurred losses attributable to prior years:						
- Asbestos & environmental[2]	(4)	(1)	NM	(4)	(1)	NM
- All other[3]	92	(62)	NM	167	(97)	NM
Pre-tax operating income	407	453	(10.2)	899	873	3.0
Realized investment gains (losses), net	5	45	(88.9)	(7)	125	NM
Federal and foreign income tax expense	(112)	(159)	(29.6)	(232)	(309)	(24.9)
Net income	$300	$339	(11.5%)	$660	$689	(4.2%)
Cash flow from operations	$1,079	$787	37.1%	$1,692	$1,796	(5.8%)

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 Net of allowance for uncollectible reinsurance $3 million for the three and six months ended June 30, 2008, and zero and $3 million for the comparable periods of 2007.

3 Net of earned premium attributable to prior years of $(6) million and $(3) million for the three and six months ended June 30, 2008, and $16 million and $35 million for the comparable periods of 2007. Net of amortization of deferred gains on retroactive reinsurance of $19 million and $36 million for the three and six months ended June 30, 2008, and $32 and $48 million for the comparable periods of 2007.

NM = Not Meaningful

Revenues for the three and six months ended June 30, 2008 were $6.948 billion and $13.833 billion respectively, increases of $653 million and $1.395 billion over the same periods in 2007. The major components of revenues are net premium earned, net investment income, net realized investment gains, and fee and other revenues.

Net premium earned for the three and six months ended June 30, 2008 was $6.004 billion and $11.942 billion, respectively, increases of $648 million and $1.375 billion over the same periods in 2007. The increases primarily reflect premium related to the acquisitions of Ohio Casualty, approximately $339 million and $689 million in the quarter and year-to-date, respectively, and Brazilian insurer Indiana Seguros, approximately $53 million and $105 million in the quarter and year-to-date, respectively, foreign exchange, approximately $108 million and $213 million in the quarter and year-to-date, respectively, and higher earned premium associated with the changes in net written premium in 2007 and the first half of 2008.

Net investment income for the three and six months ended June 30, 2008 was $754 million and $1.511 billion, respectively, increases of $44 million and $128 million over the same periods in 2007. The increases in both periods primarily reflect a higher invested asset base resulting from the continued investment of cash flow from operations, proceeds from the May 2008 debt issuance and the impact of foreign exchange, approximately $8 million and $20 million in the quarter and year-to-date, respectively. Partially offsetting these increases were lower investment yields, a shift to tax exempt securities, and a decrease in limited partnerships and limited liability companies income due to reduced valuations and IPO/takeover activities as compared to prior periods in 2007.

Net realized investment gains (losses) for the three and six months ended June 30, 2008 were $5 million and ($7) million, decreases of $40 million and $132 million from the same periods in 2007. The decreases for both periods reflect higher impairment losses on fixed maturity and equity investments related to securities subsequently sold in conjunction with funding for the acquisition of Safeco. The year-to-date decrease also reflects significant foreign equity gains in 2007 that did not recur in 2008. Partially offsetting these losses were $17 million and $33 million respectively, in net gains related to derivative contracts the Company used to partially hedge its equity exposure for the three and six months ended June 30, 2008.

Fee and other revenues for the three and six months ended June 30, 2008 were $185 million and $387 million, respectively, increases of $1 million and $24 million over the same periods in 2007. The increases in both periods primarily reflect the reclassification of contractholder charges and assessments related to SFAS 97 business within Spain and Portugal from earned premium to fee and other revenue, partially offset by lower fee revenues from the Company's 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, 2008 were $6.536 billion and $12.941 billion, respectively, increases of $739 million and $1.501 billion over the same periods in 2007. The increases in both periods primarily reflect the acquisitions of Ohio Casualty and Brazilian insurer Indiana Seguros, business growth across all strategic business units, in particular International's Latin America operations, higher catastrophe losses, general cost increases including higher interest expense and an increase in non-catastrophe property losses in both Agency Markets and Commercial Markets. Partially offsetting these increases were a decrease in incurred losses attributable to prior years, primarily related to the workers compensation and general liability lines, and lower variable incentive compensation.

CONSOLIDATED	Three Months Ended June 30, 2008	2007	Change (Points)	Six Months Ended June 30, 2008	2007	Change (Points)
Combined ratio before catastrophes and net incurred losses attributable to prior years						
Claims and claim adjustment expense ratio	70.0%	68.7%	1.3	70.5%	69.6%	0.9
Underwriting expense ratio	27.7	27.5	0.2	27.7	27.9	(0.2)
Dividend ratio	0.3	0.3	-	0.3	0.3	-
Subtotal	98.0	96.5	1.5	98.5	97.8	0.7
Catastrophes[1]	5.4	2.4	3.0	4.2	1.8	2.4
Net incurred losses attributable to prior years:						
- Asbestos & environmental	0.1	-	0.1	0.1	-	0.1
- All other	(1.6)	1.2	(2.8)	(1.5)	1.0	(2.5)
Total combined ratio[2]	101.9%	100.1%	1.8	101.3%	100.6%	0.7

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 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 and 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, 2008 was 98.0% and 98.5% respectively, increases of 1.5 points and 0.7 points over the same periods in 2007. The increases in both periods primarily reflect a higher claims and claim adjustment expense ratio due to start-up costs associated with the Company's operations in Poland and the effects of a more competitive rate environment across all SBUs and lines of business. Both periods were also impacted by higher non-catastrophe property related losses in both Agency Markets and Commercial Markets, higher auto physical damage losses due to an increase in frequency in Agency Markets and losses related to internal reinsurance. The year-to-date increase in the claims and claim adjustment expense ratio also reflects increased loss activity within LIU's first party business. Partially offsetting these increases was a lower claims and claim adjustment ratio in Personal Markets mainly related to the auto liability line of business. In 2008, Personal Markets began recording an accident year loss ratio at a level which was consistent with market trends for the period ending December 31, 2007. The underwriting expense ratio in both periods was essentially unchanged at 27.7%.

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three months and six months ended June 30, 2008 was 101.9% and 101.3% respectively, increases of 1.8 points and 0.7 points over the same periods in 2007. The increases in both periods primarily reflect the changes in the combined ratio components discussed previously and higher catastrophe losses due mainly to tornados and Midwestern storms. Partially offsetting the increases in both periods was the impact of favorable net incurred loss development attributable to prior years.

PTOI for the three months six months ended June 30, 2008 was $407 million and $899 million, respectively, a decrease of $46 million and an increase of $26 million versus the same periods in 2007.

Federal and foreign income tax expense for the three and six months ended June 30, 2008 was $112 million and $232 million, respectively, decreases of $47 million and $77 million from the same periods in 2007. The Company's effective tax rate for the three and six months ended June 30, 2008 was 27% and $26%, respectively, compared to 32% and 31% for the same periods in 2007. The effective tax rate for the three months ended June 30, 2008, reflects a net increase in the foreign valuation allowance and an increase in statutory tax rates of foreign locations. The Company's effective tax rate differs from the Federal statutory rate of 35% principally due to tax-preferenced investment income, goodwill and foreign taxes.

Net income for the three and six months ended June 30, 2008 was $300 million and $660 million, respectively, decreases of $39 million and $29 million from the same periods in 2007.

Cash flow from operations for the three and six months ended June 30, 2008 was $1.079 billion and $1.692 billion, respectively, an increase of $292 million and a decrease of $104 million versus the same periods in 2007. The increase in the quarter reflects lower Corporate expenses due to corporate benefit payments made in 2007 that did not recur in 2008 and higher investment income collections due to a higher invested asset base, partially offset by higher catastrophe payments. The year-to-date decrease reflects higher loss payments related to catastrophes and large property losses and also higher auto physical damage losses resulting from a more severe northeast winter.

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	**2008**	**2007**	**Change**	**2008**	**2007**	**Change**
Private passenger automobile	$995	$981	1.4%	$1,901	$1,881	1.1%
Homeowners and other	478	457	4.6	864	812	6.4
Individual Life[1]	66	80	(17.5)	119	144	(17.4)
Total net written premium	$1,539	$1,518	1.4%	$2,884	$2,837	1.7%

1 Effective January 1, 2008, individual life, previously included in Corporate and Other, is now included with the Personal Markets segment. All prior periods have been restated.

Net written premium for the three and six months ended June 30, 2008 was $1.539 billion and $2.884 billion, respectively, increases of $21 million and $47 million over the same periods in 2007. The increases in both periods reflect new business growth, strong customer retention in both automobile and homeowners and rate increases on homeowners policies, partially offset by a decrease in sales of immediate annuity and structured settlement products.

Private passenger automobile net written premium for the three and six months ended June 30, 2008 was $995 million and $1.901 billion, respectively, increases of $14 million and $20 million over the same periods in 2007. The increases in both periods reflect a 3.6% increase in voluntary policies in force as compared to June 30, 2007 due to strong customer retention and new business growth, partially offset by lower average premium per policy which includes the mandatory rate decreases in Massachusetts.

Homeowners and other net written premium for the three and six months ended June 30, 2008 was $478 million and $864 million, respectively, increases of $21 million and $52 million over the same periods in 2007. The increases in both periods reflect rate increases and a 4.1% increase in policies in force as compared to June 30, 2007 due to strong customer retention and new business growth, primarily in non-coastal areas.

Individual life net written premium for the three and six months ended June 30, 2008 was $66 million and $119 million, respectively, decreases of $14 million and $25 million from the same periods in 2007. The decreases in both periods reflect lower immediate annuity and structured settlement sales.

Results of Operations – Personal Markets

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2008**	**2007**	**Change**	**2008**	**2007**	**Change**
Revenues	$1,652	$1,625	1.7%	$3,286	$3,203	2.6%
PTOI before catastrophes and net incurred losses attributable to prior years	$231	$215	7.4	$435	$379	14.8
Catastrophes[2]	(191)	(92)	107.6	(255)	(128)	99.2
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other	11	34	(67.6)	13	74	(82.4)
Pre-tax operating income	$51	$157	(67.5%)	$193	$325	(40.6%)

1 Effective January 1, 2008, individual life, previously included in Corporate and Other, is now included with the Personal Markets segment. All prior periods have been restated.

2 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. Internally reinsured cat losses are not reported net of net catastrophe reinsurance premium earned.

NM = Not Meaningful

Revenues for the three and six months ended June 30, 2008 were $1.652 billion and $3.286 billion, respectively, increases of $27 million and $83 million over the same periods in 2007. 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, 2008 was $1.448 billion and $2.878 billion, respectively, increases of $27 million and $77 million over the same periods in 2007. The increases in both periods reflect the earned premium associated with the changes in net written premium for both the voluntary automobile and homeowners lines of business in 2007 and the first half of 2008, partially offset by a decrease in sales of immediate annuity and structured settlement products.

Net investment income for the three and six months ended June 30, 2008 was $176 million and $350 million, respectively, increases of $5 million and $11 million over the same periods in 2007. The increases in both periods primarily reflect a higher invested asset base due to the continued investment of cash flow from operations, partially offset by lower investment yields.

Claims, benefits and expenses for the three and six months ended June 30, 2008 was $1.608 billion and $3.102 billion, respectively, increases of $142 million and $228 million over the same periods in 2007. The increases in both periods reflect business growth, general cost increases, higher catastrophe losses driven primarily by wind and hail storms in Midwestern and Southwestern states, an increase in acquisition expenses mainly due to higher advertising costs as compared to the same periods in 2007 and a decrease in the amount of favorable prior year loss development on auto liability business, partially offset by a lower current accident year auto liability loss ratio.

	Three Months Ended June 30,			Six Months Ended June 30,		
			Change			**Change**
PERSONAL MARKETS	**2008**	**2007**	**(Points)**	**2008**	**2007**	**(Points)**
Combined ratio before catastrophes and net incurred losses attributable to prior years						
Claims and claim adjustment expense ratio	62.5%	65.4%	(2.9)	64.0%	67.0%	(3.0)
Underwriting expense ratio	26.8	24.8	2.0	26.2	25.1	1.1
Dividend ratio	-	-	-	-	-	-
Subtotal	89.3	90.2	(0.9)	90.2	92.1	(1.9)
Catastrophes[1]	13.8	6.9	6.9	9.3	4.8	4.5
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other	(0.8)	(2.5)	1.7	(0.5)	(2.8)	2.3
Total combined ratio	102.3%	94.6%	7.7	99.0%	94.1%	4.9

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. Internally reinsured cat losses are not reported net of net catastrophe reinsurance premium earned.

The Personal Markets combined ratio before catastrophes and net incurred losses attributable to prior years for the three and six months ended June 30, 2008 was 89.3% and 90.2%, respectively, decreases of 0.9 points and 1.9 points from the same periods in 2007. The decreases in both periods reflect a lower claim and claim adjustment ratio mainly related to the auto liability line of business. In 2008, Personal Markets began recording an accident year loss ratio on its auto liability business at a level which was consistent with market trends for the period ending December 31, 2007. The higher underwriting expense ratio in both periods was primarily due to an increase in advertising costs.

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, 2008 was 102.3% and 99.0%, respectively, increases of 7.7 points and 4.9 points over the same periods in 2007. The increases in both periods reflect the changes in the combined ratio previously discussed, higher catastrophe losses related to wind and hail storms and a decrease in the amount of favorable net incurred loss development attributable to prior years as compared to the same period in 2007.

PTOI for the three and six months ended June 30, 2008 was $51 million and $193 million, respectively, decreases of $106 million and $132 million from the same periods in 2007.

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	**2008**	**2007**	**Change**	**2008**	**2007**	**Change**
Business Market	$352	$ 375	(6.1%)	$834	$ 923	(9.6%)
Wausau Insurance	293	281	4.3	732	696	5.2
National Market	345	277	24.5	721	640	12.7
Group Market	140	117	19.7	277	233	18.9
Liberty Mutual Property	119	108	10.2	208	188	10.6
Other Markets	161	145	11.0	367	336	9.2
Total net written premium	$1,410	$ 1,303	8.2%	$3,139	$ 3,016	4.1%

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

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2008**	**2007**	**Change**	**2008**	**2007**	**Change**
Workers compensation	$786	$742	5.9%	$1,808	$1,838	(1.6%)
General liability	138	134	3.0	374	324	15.4
Group disability and life	140	117	19.7	277	233	18.9
Commercial automobile	136	119	14.3	260	257	1.2
Commercial multiple peril / Fire	115	107	7.5	234	202	15.8
Assumed voluntary reinsurance	33	26	26.9	72	56	28.6
Other	62	58	6.9	114	106	7.5
Total net written premium	$1,410	$1,303	8.2%	$3,139	$3,016	4.1%

Net written premium for the three and six months ended June 30, 2008 was $1.410 billion and $3.139 billion, respectively, increases of $107 million and $123 million over the same periods in 2007. The increases in both periods primarily reflect an increase in group disability and assumed voluntary reinsurance business due to a broader penetration of those markets and new business premium of approximately $48 million related to a construction account with a multi-year exposure written in the National Market segment during the second quarter. Also impacting both periods were an increase in commercial multiple peril/fire premium as a result of a reduction in the utilization of ceded reinsurance as compared to 2007, and a higher amount of audit and retrospective commercial auto premium in the National Market segment, partially offset by lower customer retention levels and rate decreases across most lines of business due to the competitive environment. Both periods were also impacted by a decrease in audit and retrospective workers compensation premium recorded in Business Market. Year-to-date results also reflect new business premium of approximately $43 million related to a construction account with a multi-year exposure written in the National Market segment in the first quarter of 2008.

Results of Operations – Commercial Markets

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2008**	**2007**	**Change**	**2008**	**2007**	**Change**
Revenues	$1,684	$1,642	2.6%	$3,386	$3,278	3.3%
PTOI before catastrophes and net incurred losses attributable to prior years	119	123	(3.3)	232	239	(2.9)
Catastrophes[1]	(44)	(4)	NM	(59)	(9)	NM
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other[2]	12	(15)	NM	22	(21)	NM
Pre-tax operating income	$87	$104	(16.3%)	$195	$209	(6.7%)

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 hurricanes and the 2005 hurricanes. In addition, losses related to the 2005 hurricanes and the 2004 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"). Catastrophe losses 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 $2 million for the three and six months ended June 30, 2008, and $7 million and $21 million for the comparable period of 2007. Net of amortization of deferred gains on retroactive reinsurance of $14 million and $26 million for the three and six months ended June 30, 2008, and $26 million and $37 million for the comparable period of 2007.

Revenue for the three and six months ended June 30, 2008 was $1.684 billion and $3.386 billion, respectively, increases of $42 million and $108 million over the same periods in 2007. 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, 2008 was $1.402 billion and $2.821 billion, respectively, increases of $33 million and $90 million over the same periods in 2007. The increases reflect the earned premium associated with the changes in net written premium in 2007 and the first half of 2008.

Net investment income for the three and six months ended June 30, 2008 was $208 million and $411 million, respectively, increases of $17 million and $33 million over the same periods in 2007. The increases primarily reflect a higher invested asset base due to the continued investment of cash flow from operations.

Fee and other revenues for the three and six months ended June 30, 2008 was $74 million and $154 million, respectively, decreases of $8 million and $15 million from the same periods in 2007. The decreases primarily reflect lower fee revenues from the Company's 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, 2008 was $1.597 billion and $3.191 billion, respectively, increases of $59 million and $122 million over the same periods in 2007. The increases primarily reflect business growth, general cost increases and higher non-catastrophe and catastrophe related property losses. Partially offsetting these increases was a decrease in the amount of incurred losses attributable to prior years, primarily in the workers compensation line of business, and a reduction in premium taxes.

COMMERCIAL MARKETS	Three Months Ended June 30, 2008	2007	Change (Points)	Six Months Ended June 30, 2008	2007	Change (Points)
Combined ratio before catastrophes and net incurred losses attributable to prior years						
Claims and claim adjustment expense ratio	82.7%	80.6%	2.1%	83.0%	81.4%	1.6%
Underwriting expense ratio	20.8	21.8	(1.0)	21.2	21.2	-
Dividend ratio	0.7	0.5	0.2	0.6	0.5	0.1
Subtotal	104.2	102.9	1.3	104.8	103.1	1.7
Catastrophes[1]	3.5	0.3	3.2	2.3	0.3	2.0
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other	(1.0)	1.3	(2.3)	(0.9)	0.9	(1.8)
Total combined ratio	106.7%	104.5%	2.2%	106.2%	104.3%	1.9%

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.

The Commercial Markets combined ratio before catastrophes and net incurred losses attributable to prior years for the three and six months ended June 30, 2008 was 104.2% and 104.8%, respectively, increases of 1.3 and 1.7 points over the comparable periods in 2007. The increases in the claims and claim adjustment expense ratio in both periods primarily reflect the impact of large property losses and a more competitive rate environment. The underwriting expense ratio in both periods was impacted by a reduction in premium taxes partially offset in the quarter and fully offset on a year-to-date basis by a decrease in the amount of expense reimbursement received from the Company's servicing carrier operations due to the depopulation of the involuntary pools.

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, 2008 was 106.7% and 106.2%, respectively, increases of 2.2 and 1.9 points over the same periods in 2007. The increases reflect the change in the combined ratio previously discussed and higher catastrophe losses attributable to Georgia tornados and Midwest flooding, partially offset by a decrease in net incurred losses attributable to prior years as a result of less workers compensation strengthening in 2008 versus the comparable period in 2007.

PTOI for the three and six months ended June 30, 2008 was $87 million and $195 million, respectively, decreases of $17 million and $14 million from the same periods in 2007.

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	**2008**	**2007[1]**	**Change**	**2008**	**2007[1]**	**Change**
Regional Companies Commercial Lines	$915	$697	31.3%	$1,792	$1,380	29.9%
Regional Companies Personal Lines	369	213	73.2	677	381	77.7
Summit	175	240	(27.1)	428	520	(17.7)
Bond	94	78	20.5	183	144	27.1
Other[2]	47	28	67.9	97	52	86.5
Total net written premium	$1,600	$1,256	27.4%	$3,177	$2,477	28.3%

1 Tables exclude the results of Ohio Casualty prior to August 24, 2007.

2 Effective in the first quarter 2008, net written premium associated with the run-off operations of GoAmerica, previously included in Regional Companies Personal Lines, is included in Other. The prior period has been restated to reflect this change.

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

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2008**	**2007**	**Change**	**2008**	**2007**	**Change**
Commercial Lines						
Workers compensation total:	$407	$419	(2.9%)	$884	$887	(0.3%)
- Summit	175	240	(27.1)	428	520	(17.7)
- All other	232	179	29.6	456	367	24.3
Commercial multiple peril	354	281	26.0	701	554	26.5
Commercial automobile	212	155	36.8	417	303	37.6
General liability	99	51	94.1	190	96	97.9
Bond	95	78	21.8	183	144	27.1
Other	57	55	3.6	112	101	10.9
Subtotal	$1,224	$1,039	17.8%	$2,487	$2,085	19.3%
Personal Lines						
Private passenger automobile	$224	$128	75.0%	$421	$235	79.1%
Homeowners	129	78	65.4	226	137	65.0
Other	23	11	109.1	43	20	115.0
Subtotal	$376	$217	73.3%	$690	$392	76.0%
Total net written premium	$1,600	$1,256	27.4%	$3,177	$2,477	28.3%

Net written premium for the three and six months ended June 30, 2008 was $1.600 billion and $3.177 billion, respectively, increases of $344 million and $700 million over the same periods in 2007. The increases in both periods primarily reflect the impact of the Ohio Casualty acquisition (approximately $358 million and $703 million of premium in the quarter and year-to-date, respectively) and organic growth in personal lines due to improved retention and an increase in new business. These increases were partially offset by modest rate decreases in most states and lines of business due to a more competitive market environment and a decrease in Summit's premium due to both mandated rate decreases in Florida and lower audit and retrospectively rated premium.

Results of Operations – Agency Markets

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2008**	**2007**	**Change**	**2008**	**2007**	**Change**
Revenues	$1,670	$1,256	33.0%	$3,317	$2,491	33.2%
PTOI before catastrophes and net incurred losses attributable to prior years	$127	$119	6.7%	$235	$224	4.9%
Catastrophes[1]	(75)	(26)	188.5	(155)	(44)	NM
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	(1)	(100.0)	-	(1)	(100.0)
- All other[2]	47	53	(11.3)	113	71	59.2
Pre-tax operating income	$99	$145	(31.7%)	$193	$250	(22.8%)

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. 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 ($1) million and ($5) million for the three and 6 months ended June 30, 2008, respectively, and $4 million and $8 million for the comparable periods of 2007.

NM = Not Meaningful

Revenues for the three and six months ended June 30, 2008 were $1.670 billion and $3.317 billion, respectively, increases of $414 million and $826 million over the same periods in 2007. 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, 2008 were $1.515 billion and $3.008 billion, respectively, increases of $371 million and $738 million over the same periods in 2007. The increase in both periods reflect approximately $339 million and $689 million of premium related to the Ohio Casualty acquisition in the quarter and year-to-date, respectively, and earned premium associated with the changes in net written premium in 2007 and the first half of 2008.

Net investment income for the three and six months ended June 30, 2008 was $139 million and $278 million, respectively, increases of $43 million and $89 million over the same periods in 2007. The increases in both periods reflect an increase in invested assets due to the continued investment of cash flow from operations and assets assumed from the Ohio Casualty acquisition.

Claims, benefits and expenses for the three and six months ended June 30, 2008 were $1.571 billion and $3.124 billion, respectively, increases of $460 million and $883 million over the same periods in 2007. The increases in both periods primarily reflect the impact of the Ohio Casualty acquisition and higher catastrophe losses, which includes losses related to tornados mainly in Tennessee and Midwestern storms. In addition, the increase in both periods reflects an increase in non-catastrophe property losses due in part to adverse weather conditions, higher auto physical damage losses due to an increase in frequency and general cost increases. Partially offsetting the year-to-date increase was an increase in favorable incurred loss development attributable to prior years primarily related to liability lines.

	Three Months Ended June 30,			Six Months Ended June 30,		
AGENCY MARKETS	**2008**	**2007**	**Change (Points)**	**2008**	**2007**	**Change (Points)**
Combined ratio before catastrophes and net incurred losses attributable to prior years						
Claims and claim adjustment expense ratio	66.5%	65.0%	1.5	67.6%	65.7%	1.9
Underwriting expense ratio	33.0	31.9	1.1	32.6	31.8	0.8
Dividend ratio	0.7	1.0	(0.3)	0.7	0.9	(0.2)
Subtotal	100.2	97.9	2.3	100.9	98.4	2.5
Catastrophes[1]	5.0	2.3	2.7	5.1	2.0	3.1
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	0.1	(0.1)	-	-	-
- All other	(3.1)	(4.6)	1.5	(3.7)	(3.1)	(0.6)
Total combined ratio	102.1%	95.7%	6.4	102.3%	97.3%	5.0

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.

The Agency Markets combined ratio before catastrophes and net incurred losses attributable to prior years for the three and six months ended June 30, 2008 was 100.2% and 100.9%, respectively, increases of 2.3 points and 2.5 points over the same periods in 2007. The increases in both periods primarily reflect a higher claims and claim adjustment expense ratio due primarily to an increase in non-catastrophe property losses and higher auto physical damage losses due to an increase in frequency. The increase in the underwriting expense ratio in both periods reflects the impact of one-time integration costs associated with the Ohio Casualty acquisition primarily related to systems integration, partially offset by a decrease in premium taxes mainly related to Summit's operations. A more competitive rate environment also impacted results in both periods.

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, 2008 was 102.1% and 102.3%, respectively, an increase of 6.4 points and 5.0 points over the same periods in 2007. The increases in both periods primarily reflect the changes in the combined ratio previously discussed and higher catastrophe losses. The increase in the quarter also reflects a decrease in net incurred loss development attributable to prior years related to a reduction in prior year audit and retrospectively rated premium earned. On a year-to-date basis, the increase in net incurred losses attributable to prior years primarily reflects favorable development in casualty lines.

PTOI for the three and six months ended June 30, 2008 was $99 million and $193 million, respectively, decreases of $46 million and $57 million over the same periods in 2007.

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	**2008**	**2007**	**Change**	**2008**	**2007**	**Change**
International Local Businesses Total	$1,065	$802	32.8%	$2,053	$1,594	28.8%
- Latin America	615	389	58.1	1,202	791	52.0
- Europe	397	371	7.0	741	718	3.2
- Asia Pacific	53	42	26.2	110	85	29.4
Liberty International Underwriters	640	582	10.0	1,229	1,213	1.3
Total net written premium (NWP)	$1,705	$1,384	23.2%	$3,282	$2,807	16.9%
Foreign exchange effect on growth			8.2%			8.1%
NWP growth excluding foreign exchange			15.0%			8.8%

The Company's International operations provide insurance products and services through 1) Local Businesses, selling personal and 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, primarily private passenger automobile, and 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, construction, aviation, and property; and
(6) LIU other: includes workers compensation, commercial automobile, 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	**2008**	**2007**	**Change**	**2008**	**2007**	**Change**
Local businesses – private passenger auto	$662	$482	37.3%	$1,240	$921	34.6%
Local businesses – all other[1]	403	320	25.9	813	673	20.8
LIU reinsurance	201	240	(16.3)	486	531	(8.5)
LIU inland marine program	157	133	18.0	302	264	14.4
LIU third party	216	135	60.0	306	260	17.7
LIU first party	51	68	(25.0)	109	139	(21.6)
LIU other	15	6	150.0	26	19	36.8
Total net written premium	$1,705	$1,384	23.2%	$3,282	$2,807	16.9%

1 Premium related to commercial and other personal lines insurance products sold by local business operations.

Net written premium for the three and six months ended June 30, 2008 was $1.705 billion and $3.282 billion, respectively, increases of $321 million and $475 million over the same periods in 2007. The increases in both periods reflect organic growth in the local businesses, primarily in Latin America, the acquisition of Brazilian insurer Indiana Seguros, approximately $57 million and $102 million in the quarter and year-to-date, respectively, start-up operations in Poland and the strengthening of foreign currencies versus the U.S. dollar, approximately $114 million and $228 million in the quarter and year-to-date, respectively. Growth in both periods also reflects the continued expansion of LIU's inland marine program business and a decrease in the amount of ceded written premium in LIU's third party business due to a change in the structure of a reinsurance program. These increases were partially offset by rate decreases in LIU's reinsurance, third and first party businesses due to a more competitive environment.

Results of Operations – International

	Three Months Ended June 30,			Six Months Ended June 30,		
$ in Millions	**2008**	**2007**	**Change**	**2008**	**2007**	**Change**
Revenues	$1,767	$1,513	16.8%	$3,498	$2,946	18.7%
PTOI before catastrophes and net incurred losses attributable to prior years	$137	$144	(4.9%)	$262	$279	(6.1%)
Catastrophes[1]	-	-	-	-	-	-
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other[2]	33	13	153.8	39	22	77.3
Pre-tax operating income	$170	$157	8.3%	$301	$301	-

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. Internally reinsured catastrophe losses are not reported net of net catastrophe reinsurance premium earned, the Company's reasonable assumption of expected catastrophe activity. Catastrophe losses, where applicable, include the impact of reinstatement premiums.

2 Net of earned premium attributable to prior years of $1 million and zero for the three and six months ended June 30, 2008, respectively, and $5 million and $6 million for the comparable periods of 2007.

Revenues for the three and six months ended June 30, 2008 were $1.767 billion and $3.498 billion, respectively, increases of $254 million and $552 million over the same periods in 2007. 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, 2008 was $1.606 billion and $3.145 billion, respectively, increases of $241 million and $497 million over the same periods in 2007. The increases in both periods primarily reflect the impact of foreign exchange, approximately $108 million and $213 million in the quarter and year-to-date, respectively, and business growth consistent with the increase in net written premium from the local businesses and LIU's inland marine program and third party business in 2007 and the first half of 2008.

Net investment income for the three and six months ended June 30, 2008 was $147 million and $299 million, respectively, increases of $17 million and $46 million over the same periods in 2007. The increases in both periods reflect a higher invested asset base, higher yields in many of the local businesses, primarily Latin America and Europe, and the impact of foreign exchange, approximately $8 million and $20 million in the quarter and year-to-date, respectively.

Claims, benefits and expenses for the three and six months ended June 30, 2008 were $1.611 billion and $3.214 billion, respectively, increases of $254 million and $580 million over the same periods in 2007. The increases in both periods primarily reflect business growth in the local businesses, primarily in Latin America, including the acquisition of Indiana Seguros in Brazil, the overall strengthening of foreign currencies versus the U.S. dollar and the continued expansion of LIU's inland marine program business. Also impacting both periods was an increase in net commission expense due to higher acquisition costs in the local businesses, primarily Latin America, and a change in the structure of a reinsurance program in LIU's third party business, partially offset by an increase in ceding commissions in LIU's inland marine program due to a change in the terms of the program. Partially offsetting these increases was an increase in the amount of favorable incurred loss development attributable to prior years primarily from automobile business in Spain and a decline in the amount of unfavorable incurred loss development attributable to prior years within LIU reinsurance. The year-to-date increase in the amount of favorable prior-year development was partially offset by unfavorable loss development associated with automobile business in Turkey.

	Three Months Ended June 30,			**Six Months Ended June 30,**		
INTERNATIONAL	**2008**	**2007**	**Change (Points)**	**2008**	**2007**	**Change (Points)**
Combined ratio before catastrophes and net incurred losses attributable to prior years						
Claims and claim adjustment expense ratio	68.6%	65.4%	3.2	68.9%	66.5%	2.4
Underwriting expense ratio	32.3	31.3	1.0	31.7	31.1	0.6
Dividend ratio	-	-	-	-	-	-
Subtotal	100.9	96.7	4.2	100.6	97.6	3.0
Catastrophes[1]	-	-	-	-	-	-
Net incurred losses attributable to prior years:						
- Asbestos & environmental	-	-	-	-	-	-
- All other	(2.1)	(1.0)	(1.1)	(1.2)	(0.9)	(0.3)
Total combined ratio	98.8%	95.7	3.1	99.4%	96.7%	2.7

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. Internally reinsured catastrophe losses are not reported net of net catastrophe reinsurance premium earned, the Company's reasonable assumption of expected catastrophe activity. 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, 2008 was 100.9% and 100.6%, respectively, increases of 4.2 points and 3.0 points over the comparable periods in 2007. The increases in the claims and claim adjustment expense ratio in both periods reflect unfavorable current accident year loss experience on automobile business written in Turkey, start-up costs associated with the Company's operations in Poland and the effects of a more competitive rate environment on LIU's reinsurance, third and first party business. The year-to-date increase in the claims and claim adjustment expense ratio also reflects increased loss activity within LIU's first party business**.** The increase in the combined ratio in both periods also reflects a higher underwriting expense ratio due to higher acquisition costs in Latin America and Europe, including start-up operations in Poland, and a change in the structure of a reinsurance program in LIU's third party business which reduced the amount of ceded commissions received versus 2007.

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, 2008 was 98.8% and 99.4%, respectively, increases of 3.1 points and 2.7 points over the comparable periods in 2007. These increases reflect the aforementioned changes in the combined ratio components, as well as an increase in the amount of favorable incurred loss development attributable to prior years.

PTOI for the three and six months ended June 30, 2008 was $170 million and $301 million, respectively, increases of $13 million and zero from the same periods in 2007.

CORPORATE and OTHER

Overview – Corporate and Other

Corporate and Other includes the following significant items:

- 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, certain distribution channels related to PruPac, and Commercial Markets assumed voluntary reinsurance 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 Markets 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 is allocated to the business units based on planned ordinary investment income returns by investment category. Investments are allocated to the business units in an amount equal to their respective liabilities net of insurance assets (reinsurance, premiums receivable, etc.) plus allocated statutory policyholders' surplus. The difference between allocated net investment income and actual net investment income is included in Corporate and Other.

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

- 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.

- Effective January 1, 2008, individual life, previously included in Corporate and Other, is now included with the Personal Markets segment. All prior periods have been restated.

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

$ in Millions	Three Months Ended June 30, 2008	2007	Change	Six Months Ended June 30, 2008	2007	Change
Internal reinsurance[1]	$34	$63	(46.0%)	$140	$160	(12.5%)
Workers compensation[2]	(10)	(48)	79.2	(89)	(135)	34.1
Other	1	1	-	2	2	-
Total net written premium	$25	$16	56.3%	$53	$27	96.3%

[1] Net of external cessions
[2] Booked as billed adjustment

Net written premium for the three and six months ended June 30, 2008 was $25 million and $53 million, respectively, increases of $9 million and $26 million over the same periods in 2007. The increases in both periods reflect a decrease in the Company's workers compensation "booked as billed" adjustment, partially offset by a decrease in internal reinsurance premium due to an increase in external ceded reinsurance as a result of the Company purchasing additional catastrophe reinsurance.

Results of Operations – Corporate and Other

$ in Millions	Three Months Ended June 30, 2008	2007	Change	Six Months Ended June 30, 2008	2007	Change
Revenues	$175	$259	(32.4%)	$346	$520	(33.5%)
PTOI before catastrophes and net incurred losses attributable to prior years	$18	$37	51.4%	$51	$31	64.5%
Catastrophes[1]	(3)	-	NM	(10)	-	NM
Net incurred losses attributable to prior years:						
- Asbestos & environmental[2]	(4)	-	NM	(4)	-	NM
- All other[3]	(11)	(147)	(92.5)	(20)	(243)	(91.8)
Pre-tax operating income (loss)	$-	($110)	(100.0%)	$17	($212)	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). 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 $3 million for the three and six months ended June 30, 2008, and zero and $3 million for the comparable periods of 2007.

3 Net of amortization of deferred gains on retroactive reinsurance of $5 million and $10 million for the three and six months ended June 30, 2008, and $6 million and $11 million for the comparable periods of 2007.

4 NM = Not Meaningful

Revenues for the three and six months ended June 30, 2008 were $175 million and $346 million, respectively, decreases of $84 million and $174 million from the same periods in 2007. 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, 2008 was $33 million and $90 million, respectively, decreases of $24 million and $27 million from the same periods in 2007. The decreases in both periods reflect an increase in external ceded reinsurance.

Net investment income for the three and six months ended June 30, 2008 was $84 million and $173 million, respectively, decreases of $38 million and $51 million from the same periods in 2007. The decreases reflect a decrease in investment income related to limited partnerships and limited liability companies.

Net realized investment gains (losses) for the three and six months ended June 30, 2008 were $26 million and $19 million, respectively, decreases of $18 million and $91 million from the same periods in 2007. The decreases for both periods reflect higher impairment losses on fixed maturity and equity investments related to securities subsequently sold to raise funds for the acquisition of Safeco. The year-to-date decrease also reflects significant foreign equity gains in 2007 that did not recur in 2008. Partially offsetting these losses were $17 million and $33 million respectively, in net gains related to derivative contracts the Company used to partially hedge its equity exposure for the three and six months ended June 30, 2008.

Fee and other revenues for the three and six months ended June 30, 2008 were $32 million and $64 million, respectively, decreases of $4 million and $5 million from the same periods in 2007. The decreases in both periods primarily reflect the loss of revenue associated with the sale of a Company owned property in 2007, partially offset by an increase in oil and gas revenues.

Claims, benefits and expenses for the three and six months ended June 30, 2008 were $149 million and $310 million, respectively, decreases of $176 million and $312 million from the same periods in 2007. The decreases in both periods primarily reflect a decrease in the amount of unfavorable incurred losses attributable to prior years primarily related to pre-2005 fully insured workers compensation business and assumed voluntary reinsurance business. In addition, variable incentive compensation and other corporate expenses decreased in both periods, partially offset by an increase in catastrophe losses related to internal reinsurance programs and higher interest expense as a result of the Company's March 2007 and May 2008 debt offerings.

Pre-tax operating income for the three and six months ended June 30, 2008 was zero and $17 million, respectively, increases of $110 million and $229 million over the same periods in 2007.

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 (including cash and cash equivalents)

The following table summarizes the Company's invested assets by asset category as of June 30, 2008 and December 31, 2007:

$ in Millions	**As of June 30, 2008**		**As of December 31, 2007**	
Invested Assets by Type	**Carrying Value**	**% of Total**	**Carrying Value**	**% of Total**
Fixed maturities, available for sale, at fair value	$44,145	73.3%	$46,934	82.1%
Equity securities, available for sale, at fair value	2,394	4.0	3,285	5.7
Trading securities, at fair value	17	-	16	-
Limited partnerships and limited liability companies	2,475	4.1	2,134	3.7
Commercial mortgage loans	912	1.5	657	1.2
Short-term investments	901	1.5	764	1.3
Other investments	228	0.4	214	0.4
Cash and cash equivalents	9,127	15.2	3,199	5.6
Total invested assets	$60,199	100.0%	$57,203	100.0%

Total invested assets as of June 30, 2008 were $60.199 billion, an increase of $2.996 billion or 5.2% from December 31, 2007. The increase in invested assets primarily reflects the investment of cash flows from operations, proceeds from the May 2008 debt issuance and continued growth in investment income. Partially offsetting these increases was an increase in unrealized losses primarily due to an increase in credit spreads and a general decline in market values related to both fixed income and equity markets.

Separately, the Company's cash balances grew significantly in the second quarter due to the planned liquidation of securities to fund the Safeco acquisition.

Fixed maturities as of June 30, 2008 were $44.145 billion, a decrease of $2.789 billion or 5.9% from December 31, 2007. The decrease reflects the liquidation of securities in the second quarter to help fund the acquisition of Safeco and market value declines in fixed income securities, partially offset by the investment of cash flows from operations.

Equity securities, available for sale, as of June 30, 2008 were $2.394 billion ($1.870 billion common stock and $524 million preferred stock), a decrease of $891 million or 27.1% from December 31, 2007. The decrease primarily reflects the liquidation of securities in the second quarter to help fund the acquisition of Safeco and to reduce the Company's exposure to the equity markets. The decrease also reflects a decrease in unrealized gains due in part to a general decline in equity market indices.

Limited partnerships and limited liability companies as of June 30, 2008 were $2.475 billion, an increase of $341 million or 16.0% over December 31, 2007. These investments consist of traditional private equity partnerships of $1.561 billion, other partnerships (primarily energy) of $471 million, and real estate partnerships of $443 million. The increase over December 31, 2007 reflects new investments across all three categories as the Company continues to diversify its private equity portfolio. The Company's investments in 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, 2008 were $912 million, net of $0.8 million of loss reserve or 0.09% of the outstanding loan portfolio, an increase of $255 million or 38.8% over December 31, 2007. The increase reflects $267 million of new capital loaned, net of $12 million in principal repayments. The entire commercial loan portfolio is U.S. based. The average total loan size was $1.4 million and the average loan participation size was $0.5 million. The number of loans in the portfolio increased from 1,406 at December 31, 2007 to 1,883 at June 30, 2008.

Short term investments as of June 30, 2008 were $901 million, an increase of $137 million or 17.9% over December 31, 2007. This increase reflects assets assumed from the acquisition of Indiana Seguros S.A., a Brazilian insurer, and short term assets received as collateral from the Company's security lending program.

In January 2008, the Company adopted SFAS 157, which establishes a fair value hierarchy that prioritizes inputs to valuation techniques used to measure fair value. As of June 30, 2008, the Company reflected $3.063 billion as level 1 (quoted prices in active markets) and this primarily comprised U.S. Treasuries and common equity securities. The majority of the Company's invested assets are reported as level 2 (quoted prices from other observable inputs). As of June 30, 2008, the Company reported $43.648 billion as level 2, consisting primarily of various fixed maturity securities. Finally, the Company reported $1.799 billion as level 3 (unobservable inputs) and this primarily comprised international and privately held securities for which a market price is not readily available and commercial mortgage loans which are carried at amortized cost.

As of June 30, 2008, the Company had unfunded commitments in traditional private equity partnerships, real estate, energy and other, and commercial mortgage loans of $1.073 billion, $487 million, $442 million and $195 million, respectively. As of June 30, 2008, the Company had commitments to purchase various residential mortgage-backed securities at a cost and fair market value of $10 million.

As of June 30, 2008, no single issuer, excluding U.S. Treasuries, agency securities and mortgage-backed securities, accounted for more than 1% of invested assets.

The following table summarizes the Company's fixed maturity portfolio by security type as of June 30, 2008 and December 31, 2007:

$ in Millions	**As of June 30, 2008**		**As of December 31, 2007**	
Fixed Maturities by Security Type	**Market Value**	**% of Total**	**Market Value**	**% of Total**
U.S. Government and agency securities	$2,569	5.8%	$3,318	7.1%
Mortgage and asset-backed securities	11,789	26.7	13,491	28.7
U.S. state and municipal	9,482	21.5	10,001	21.3
Corporate and other	17,513	39.7	17,438	37.2
Foreign government securities	2,792	6.3	2,686	5.7
Total fixed maturities	$44,145	100.0%	$46,934	100.0%

During the second quarter of 2008, as previously mentioned, the decrease in U.S. government and agency securities, mortgage and asset-backed securities, and U.S. state and municipal securities, reflects the liquidation of these securities for the pending acquisition of Safeco.

The following table summarizes the Company's exposure to alt-A and sub-prime mortgage collateral as of June 30, 2008:

$ in Millions	As of June 30, 2008		
	Alt-A	Sub-prime	Total
Liberty Mutual Group (excluding Ohio Casualty)	$133	$12	$145
Ohio Casualty	37	62	99
Consolidated	$170	$74	$244

The following table summarizes the Company's exposure to alt-A and sub-prime mortgage collateral as of December 31, 2007:

$ in Millions	As of December 31, 2007		
	Alt-A	Sub-prime	Total
Liberty Mutual Group (excluding Ohio Casualty)	$161	$16	$177
Ohio Casualty	44	80	124
Consolidated	$205	$96	$301

As of June 30, 2008, the Company's exposure to sub-prime ($74 million or 0.12% of invested assets) and alt-A mortgage collateral ($170 million or 0.28% of invested assets) was primarily AAA rated.

The following table summarizes the Company's exposure to mortgage-backed securities (both pass-throughs and CMOs), debt and equity issued by FNMA and FHLMC:

$ in Millions	As of June 30, 2008				
	MBS	Fixed	Preferred	Common	Total
FNMA	$2,805	$171	$73	$4	$3,053
FHLMC	3,967	114	83	1	4,165
Total	$6,772	$285	$156	$5	$7,218

The following table summarizes the Company's allocation of fixed maturities by credit quality as of June 30, 2008 and December 31, 2007:

$ in Millions	As of June 30, 2008		As of December 31, 2007	
Fixed Maturities by Credit Quality*	Market Value	% of Total	Market Value	% of Total
AAA	$20,423	46.2%	$24,576	52.4%
AA+, AA, AA-	8,345	18.9	7,586	16.2
A+, A, A-	7,575	17.2	7,196	15.3
BBB+, BBB, BBB-	4,635	10.5	4,405	9.4
BB+, BB, BB-	1,844	4.2	1,797	3.8
B+, B, B-	1,051	2.4	1,165	2.5
CCC or lower	272	0.6	209	0.4
Total fixed maturities	$44,145	100.0%	$ 46,934	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 decreased slightly to 92.8% at June 30, 2008 from 93.3% December 31, 2007. This decrease reflects the liquidation of securities in the second quarter in anticipation of funding for the Safeco acquisition.

The Company had 7.2% of its fixed maturity securities invested in non-investment grade securities at June 30, 2008. 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 and corporate debt primarily in support of the Company's international insurance companies.

The following table summarizes the Company's allocation of fixed maturities by maturity date as of June 30, 2008 and December 31, 2007:

$ in Millions	**As of June 30, 2008**		**As of December 31, 2007**	
Fixed Maturities by Maturity Date	**Market Value**	**% of Total**	**Market Value**	**% of Total**
1 yr or less	$1,646	3.7%	$1,376	3.0%
Over 1 yr through 5 yrs	9,175	20.8	9,295	19.8
Over 5 yrs through 10 yrs	9,524	21.6	9,567	20.4
Over 10 years	12,011	27.2	13,205	28.1
Mortgage and asset-backed securities	11,789	26.7	13,491	28.7
Total fixed maturities	$44,145	100.0%	$46,934	100.0%

During 2008, 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. The planned sale of securities in the second quarter consisted primarily of longer term maturities and mortgage and asset-backed securities.

Net Investment Income

The following table summarizes the Company's net investment income for the three and six months ended June 30, 2008 and 2007:

$ in Millions	**Three Months Ended June 30,**		**Six Months Ended June 30,**	
Net Investment Income	**2008**	**2007**	**2008**	**2007**
Taxable interest income	$565	$540	$1,149	$1,086
Tax-exempt interest income	106	80	212	152
Dividends	31	25	55	42
Limited partnerships and limited liability companies	58	85	118	150
Commercial mortgage loans	12	6	22	11
Other investment income	9	2	11	3
Gross investment income	781	738	1,567	1,444
Investment expenses	(27)	(28)	(56)	(61)
Net investment income	$754	$710	$1,511	$1,383

Net investment income for the three and six months ended June 30, 2008 was $754 million and $1.511 billion, respectively, increases of $44 million and $128 million over the same periods in 2007. The increases in both periods primarily reflect a higher invested asset base resulting from the continued investment of cash flow from operations, proceeds from the May 2008 debt issuance, and the impact of foreign exchange, approximately $8 million and $20 million in the quarter and year-to-date, respectively. Partially offsetting these increases were lower investment yields, a shift to tax exempt securities, and a decrease in limited partnerships and limited liability companies income due to reduced valuations and IPO/takeover activities as compared to prior periods in 2007.

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, 2008 and 2007:

$ in Millions **Net Realized Investment Gains (Losses)**	**Sales & Dispositions**	**Impairments**	**Change in Derivatives Value**	**Total**
Three Months Ended June 30, 2008:				
Fixed maturities	($16)	($21)	$-	($37)
Common and preferred stock	69	(43)	-	26
Other	(10)	-	26	16
Total	$43	($64)	26	$5
Three Months Ended June 30, 2007:				
Fixed maturities	$3	$-	$-	$3
Common and preferred stock	29	-	-	29
Other	22	(9)	-	13
Total	$54	($9)	$-	$45
Six Months Ended June 30, 2008:				
Fixed maturities	($20)	($36)	$-	($56)
Common and preferred stock	74	(59)	-	15
Other	17	-	17	34
Total	$71	($95)	$17	($7)
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

$ in Millions	**Three Months Ended June 30,**		**Six Months Ended June 30,**	
Components of Net Realized Investment Gains (Losses)	**2008**	**2007**	**2008**	**2007**
Fixed maturities:				
Gross realized gains	$23	$22	$55	$54
Gross realized losses	(60)	(19)	(111)	(36)
Equities:				
Gross realized gains	95	30	111	91
Gross realized losses	(69)	(1)	(96)	(5)
Other:				
Gross realized gains	18	22	36	36
Gross realized losses	(2)	(9)	(2)	(15)
Total net realized investment gains (losses)	$5	$45	($7)	$125

Net realized investment gains (losses) for the three and six months ended June 30, 2008 were $5 million and ($7) million, decreases of $40 million and $132 million from the same periods in 2007. The decreases for both periods reflect higher impairment losses on fixed maturity and equity investments related to securities subsequently sold to raise funds for the acquisition of Safeco. The year-to-date decrease also reflects significant foreign equity gains in 2007 that did not recur in 2008. Partially offsetting these losses were $17 million and $33 million respectively, in net gains related to derivative contracts the Company used to partially hedge its equity exposure for the three and six months ended June 30, 2008.

Equities and Hedging Program

Beginning in January 2008, the Company, as part of its risk management, diversification strategy, and economic hedging strategies, entered into several futures contracts related to the equities market. The contracts were terminated in March 2008 and the Company realized gains of $26 million on these transactions. Subsequent to the futures program, the Company has entered into an equity swap agreement. For the period ended June 30, 2008 the Company recorded a $7 million net gain from the swap agreement. This contract expires in January 2009 with earlier termination allowed.

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, 2008:

$ 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	($6)	$491	($5)	$11
Mortgage and asset-backed securities	(152)	5,448	(105)	1,269
U.S. state and municipal	(114)	5,012	(85)	1,215
Corporate and other	(305)	7,420	(516)	4,666
Foreign government securities	(70)	1,542	(12)	230
Equities	(312)	1,003	(48)	62
Total	($959)	$20,916	($771)	$7,453

Unrealized losses increased from $934 million as of December 31, 2007 to $1.730 billion as of June 30, 2008 primarily due to an increase in credit spreads and a general decline in market values related to both fixed income and equity markets. Unrealized losses less than 12 months increased from $510 million to $959 million and accounted for $449 million, or 56.4%, of the overall increase in unrealized losses. 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, 2008 are temporary.

The gross unrealized losses recorded on equity securities at June 30, 2008 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, 2008 totaled $51.072 billion.

Short-term debt outstanding at June 30, 2008 and December 31, 2007 was as follows:

$ in Millions	**As of June 30, 2008**	**As of December 31, 2007**
Commercial paper	$-	$-
Revolving credit facilities	-	70
Current maturities of long-term debt	18	21
Total short-term debt	$18	$91

Long-term debt outstanding at June 30, 2008 and December 31, 2007 was as follows:

$ in Millions	**As of June 30, 2008**	**As of December 31, 2007**
8.00% Prudential notes—series B, due 2013	$260	$260
7.86% Medium term notes, due 2013	25	25
5.75% Senior notes, due 2014	500	500
7.30% Senior notes, due 2014[1]	200	200
6.70% Senior notes, due 2016	250	250
7.00% Junior subordinated notes, due 2067[2]	300	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[3]	700	700
10.75% Junior subordinated notes, due 2088[4]	1,250	-
7.697% Surplus notes, due 2097	500	500
Subtotal	5,638	4,388
Unamortized discount[5]	(55)	(28)
Total long-term debt excluding current maturities	$5,583	$4,360

[1] Reflects debt issued by Ohio Casualty.
[2] The par value call date and final fixed rate interest payment date is March 15, 2017, subject to certain requirements.
[3] The par value call date and final fixed rate interest payment date is March 15, 2037, subject to certain requirements.
[4] The par value call date and final fixed rate interest payment date is June 15, 2038, subject to certain requirements.
[5] Reflects purchase accounting adjustment related to Ohio Casualty $200 million senior notes, due 2014.

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 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 364 day revolving credit facility, which became effective October 26, 2007. 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. As of June 30, 2008, no borrowings were outstanding 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, 2008, no borrowings were outstanding under the facility.

The Company's Venezuelan subsidiary, Inversora Segucar, C.A., maintains a $115 million revolving credit facility to provide liquidity for working capital purposes. As of June 30, 2008, no borrowings were outstanding under the facility.

The $73 million decrease in short-term debt outstanding is due to a decrease of $70 million in outstanding borrowings under the Venezuelan credit facility, redemption of the Company's 7.10% Medium Term notes on May 15, 2008 for $2 million, and $1 million partial redemption of the 5.0% Prudential notes due 2008.

On May 29, 2008, LMGI issued Series C junior subordinated notes (the "Series C Notes") with a face amount of $1.25 billion. The Series C Notes are scheduled for redemption on June 15, 2058 with a final maturity of June 15, 2088. LMGI may redeem the Series C Notes in whole or in part, on June 15, 2038 and on each interest payment date thereafter at their principal amount plus accrued and unpaid interest to the date of redemption, or prior to June 15, 2038, (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 10.75% up to, but excluding, the final fixed rate interest payment date. In the event the Series C 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 7.12%, payable quarterly in arrears. LMGI has the right to defer interest payments on the Series C Notes for a period up to ten years. Interest compounds during periods of deferral. In connection with the issuance of the Series C 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 Series C 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 Series C Notes, and may not be enforced by the holders of the Series C 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).

Consolidated interest expense for the three and six months ended June 30, 2008 was $93 million and $176 million, respectively, increases of $14 million and $31 million over the same periods in 2007.

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, 2008, the Company, through its downstream subsidiary LMGI, had $4.538 billion of debt outstanding, excluding discount.

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 its debt, as could a redomestication, merger or consolidation of LMIC, LMFIC or EICOW to a different domiciliary state.

The authorized control level risk-based capital (as of December 31, 2007) and 2008 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	**2007**	**2006**	**Change**	**2008**
LMIC [3]	519%	554%	(35 points)	$1,182
LMFIC	507%	579%	(72 points)	$87
EICOW [3]	516%	395%	121 points	$130

[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 three and six months ended June 30, 2008, Corporate Services recorded $66 million and $132 million in pre-tax income, respectively.

Statutory Surplus

Statutory surplus as regards policyholders for the combined operations of LMIC and its U.S. affiliates including international branches was $15.371 billion and $14.155 billion at June 30, 2008, and December 31, 2007, respectively. The increase in surplus primarily reflects a capital contribution associated with the Company’s May 2008 debt offering, an increase in net income and a decrease in non-admitted goodwill, offset by unrealized losses.

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;
- deferred acquisition costs;
- valuation of goodwill and intangible assets; 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 2007 tables to conform to the 2008 tables.

Adoption of New Accounting Standards

Effective January 1, 2008, the Company had the option to adopt Statement of Financial Accounting Standards No. 159, "*The Fair Value Option for Financial Assets and Financial Liabilities, Including an Amendment of SFAS 115*" ("SFAS 159"). The Company has not made any fair value elections as allowed under SFAS 159.

Effective January 1, 2008, the Company adopted Emerging Issues Task Force ("EITF") issue No. 06-4, "*Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*" ("EITF 06-4"). This issue provides guidance on the recognition and measurement of assets related to collateral assignment split-dollar life insurance arrangements. The adoption of EITF 06-4 resulted in a decrease to equity of $41 million.

Effective January 1, 2008, the Company adopted EITF issue No. 06-10, "*Accounting for Deferred Compensation and Postretirement Benefit Aspects of Collateral Assignment Split-Dollar Life Insurance Arrangements* ("EITF 06-10"). This issue requires a company to recognize a liability for future life insurance benefits in accordance with SFAS 106 or Opinion 12. The adoption of EITF 06-10 had no impact on the Company's financial statements.

Future Adoption of New Accounting Standards

In December 2007, the FASB issued SFAS No. 141(R), "*Applying the Acquisition Method*" ("SFAS 141(R)"). This issue will result in significant changes to accounting for business combinations. Prospective adoption is required and early adoption is not permitted. The Company is required to adopt SFAS 141(R) effective January 1, 2009.

In December 2007, the FASB issued SFAS No. 160, "*Accounting for Noncontrolling Interests*" ("SFAS 160"). SFAS 160 will result in the consolidation of all non-controlling interests within the income statement and balance sheet of the Company for all consolidated subsidiaries. SFAS 160 is required to be adopted on January 1, 2009. Prospective adoption is required, except for the required reclassifications which are to be applied retrospectively. Early adoption is not permitted. The Company is in the process of evaluating the impact of adoption.

In March 2008, FASB issued SFAS No. 161, "*Disclosures about Derivative Instruments and Hedging Activities*" ("SFAS 161"). SFAS 161 is intended to improve financial reporting about derivative instruments and hedging activities by requiring enhanced disclosures to enable investors to better understand their effects on an entity's financial position, financial performance, and cash flows. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008.

In May 2008, the FASB issued SFAS No. 162, "*The Hierarchy of Generally Accepted Accounting Principles*" ("SFAS 162"). SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of entities that are presented in conformity with generally accepted accounting principles in the United States. This Statement is effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board amendments to AU Section 411, *The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles*. The Company is in the process of evaluating the impact of adoption.

In May 2008, the FASB issued SFAS No. 163, "*Accounting for Financial Guarantee Insurance Contracts – an interpretation of FASB Statement No. 60,*" ("SFAS 163"). SFAS 163 is intended to increase comparability in financial reporting of financial guarantee insurance contracts by insurance companies. SFAS 163 requires that an insurance enterprise recognize a claim liability prior to an event of default when there is evidence that credit deterioration has occurred in an insured financial obligation. This Statement also clarifies how Statement 60 applies to financial guarantee insurance contracts, including the recognition and measurement to be used to account for premium revenue and claim liabilities. SFAS 163 is effective for fiscal years beginning after December 15, 2008. As the Company does not write financial guarantee insurance contracts, SFAS 163 will have no impact.

Unpaid Claims and Claim Adjustment Expenses

Reserves for property-casualty unpaid claims and claim adjustment expenses were $44.005 billion and $42.992 billion at June 30, 2008 and December 31, 2007, 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 A&E reserves for unpaid claims and claim adjustment expenses were $1.255 billion and $1.334 billion at June 30, 2008 and December 31, 2007, respectively, net of reinsurance and including an allowance for uncollectible reinsurance. The year-to-date decrease was due primarily to ongoing settlement activity of asbestos and environmental claims.

In the third quarter of 2007, the Company completed its biennial ground-up asbestos reserve study and increased its asbestos reserves by $95 million. The study was completed by a multi-disciplined team of internal claims, legal, reinsurance and actuarial personnel, and it included all major segments of the Company's direct, assumed, and ceded asbestos claims. In addition, an internationally known actuarial consulting firm performed its own independent review of the Company's asbestos reserves and confirmed the reasonableness of the reserve increase.

As part of the internal review, potential exposures of large policyholders were individually evaluated using the Company's proprietary stochastic model, which is consistent with the latest published actuarial paper on asbestos reserving. Among the factors reviewed in depth by the team specialists were the type of business, level of exposure, coverage limits, geographic distribution of products, types of injury, state jurisdictions, legal defenses, and reinsurance potential. Small policyholders were evaluated using aggregate methods that utilized information developed from the large policyholders. Additionally, a provision of pure IBNR was established for the potential emergence of first-time filers of future asbestos 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 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 $15.272 billion and $15.518 billion at June 30, 2008 and December 31, 2007, respectively, net of allowance for doubtful accounts. The decrease is primarily due to the ongoing settlement of 2005 hurricane claims.

The reinsurance recoverables from Nationwide Indemnity Company have been fully guaranteed by its parent, Nationwide Mutual Insurance Company, 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 96% 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, 2008. Collateral held against outstanding gross reinsurance recoverable balances was $4.663 billion and $4.584 billion at June 30, 2008 and December 31, 2007, respectively.

The remaining 4% 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 1% 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, 2008.

Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured business. 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) that are amortized into income using the effective interest method over the estimated settlement periods. At June 30, 2008, and December 31, 2007, deferred gains related to these reinsurance arrangements were $761 million and $786 million, respectively, and are included in other liabilities within the consolidated balance sheets. Interest credited to the "funds held" balances for the three months and six months ended June 30, 2008, was $30 million and $59 million, respectively, as compared to $29 million and $57 million, for the three months and six months ended June 30, 2007, respectively. Deferred gain amortization for the three months and six months ended June 30, 2008, was $17 million and $33 million, respectively, as compared to $13 million and $29 million for the three months and six months ended June 30, 2007, respectively. Reinsurance recoverables related to these transactions, including experience related profit accruals, were $2.192 billion and $2.222 billion as of June 30, 2008, and December 31, 2007, respectively.

Additionally, the Company has an aggregate stop loss program covering substantially all of Commercial Markets 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.

In 2006, the Company 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 the Company in the event of a Northeast hurricane. The reinsurance agreements are collateralized through a trust and guarantee 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, the Company 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 the Company 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.

In 2008, the Company purchased property catastrophe reinsurance of which $426 million of limits are collateralized from the inception of the contracts. The Company has not recorded any recoveries under these programs.

Impairment Losses on Investments

The total impairment losses on investments for the three and six months ended June 30, 2008 were $64 million and $95 million, respectively, an increase of $55 million and $78 million compared to the same periods in 2007. Impairments in 2008 were related primarily to high yield, fixed income and foreign and domestic equity securities. 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 has been deemed to be the primary beneficiary for 2 VIEs in the energy investment sector, therefore it consolidates these 2 VIEs in its financial statements. In addition, the Company has investments in 48 and 40 VIEs for which it is not the primary beneficiary at June 30, 2008 and December 31, 2007, respectively. The Company's investments in VIEs were $480 million and $386 million at June 30, 2008 and December 31, 2007, respectively. The Company's maximum exposure to losses from VIEs was $1.098 billion and $786 million as of June 30, 2008 and December 31, 2007, 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 of each insurance subsidiary that has entered into derivative transactions. Pursuant to the policy, the Company may enter into derivative transactions. As of June 30, 2008 and December 31, 2007, the Company had two interest rate swaps acquired with the assets and liabilities of the Genesis life insurance business. As of both June 30, 2008 and December 31, 2007, the value of these instruments was approximately ($5) million.

Beginning in January 2008, the Company, as part of its risk management program, diversification, and economic hedging strategies, entered into several futures contracts related to the equities market with notional amounts totaling $599 million. All futures contracts concluded in March 2008 and the Company realized gains of $26 million on these transactions. Subsequent to the above transactions, the Company has entered into a $600 million notional equity swap agreement. For the period ending June 30, 2008 the Company incurred a $7 million net gain related to the swap contract. This contract expires in January 2009; however, earlier termination is allowed.

Deferred Acquisition Costs and Acquired In-force Policy Intangibles

Total deferred policy acquisition costs and acquired in-force policy intangibles were $2.222 billion and $2.045 billion as of June 30, 2008 and December 31, 2007, 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. Acquired in-force policy intangibles are costs associated with the acquisition of Ohio Casualty that equal the fair value of in-force insurance contracts at the date of acquisition.

Goodwill and Intangibles

Goodwill and intangible assets were $2.403 billion and $2.292 billion at June 30, 2008 and December 31, 2007, respectively. The increase was primarily due to the acquisition of Indiana Seguros, S.A..

Deferred Income Taxes

The net deferred income tax asset was $1.955 billion and $1.469 billion as of June 30, 2008 and December 31, 2007, respectively, net of a valuation allowance of $155 million and $117 million, respectively. The net increase in the Company's valuation allowance is primarily due to increases in the uncertainty of the realization of certain foreign net operating losses, foreign currency translation adjustments and changes in foreign statutory tax rates, offset by decreases due to positive expectations for future realization of certain foreign net operating losses. 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 and net operating losses.

The liability for unrecognized tax benefits at January 1, 2008 was $175 million. A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

($ in millions)	
Balance at January 1, 2008	$175
Additions based on tax positions related to current year	-
Additions for tax positions of prior years	33
Reductions for tax positions of prior years	-
Settlements	(14)
Increases in unrecognized tax benefits acquired or assumed in a business combination	11
Balance at June 30, 2008	$205

Included in the balance at June 30, 2008, are $83 million related tax positions that would impact the effective tax rate.

The IRS is currently reviewing the Company's federal tax returns for the 1999 through 2005 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 94th on the Fortune 500 list of largest corporations in the United States based on 2007 revenue. As of December 31, 2007, LMG had $94.742 billion in consolidated assets, $82.376 billion in consolidated liabilities, and $25.961 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 41,000 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.