



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

Quarter Ended March 31, 2009

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 months ended March 31, 2009 and 2008. This Management's Discussion & Analysis of Financial Condition and Results of Operations ("MD&A") should be read in conjunction with the Company's 2008 Annual Report, 2009 Unaudited Consolidated Financial Statements and First Quarter 2009 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 potentially hazardous products or substances, including welding rod, lead paint 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 portfolio, which could suffer reduced returns or losses adversely affecting the Company's profitability, capitalization and liquidity; market conditions that may limit the Company's ability to replace maturing liabilities in a timely manner or that may make it difficult to value the Company's investments; developments in U.S. and global financial and capital markets, including changes in interest rates, rates of inflation, credit spreads, equity prices and foreign exchange rates; losses due to defaults of individual issuers and defaults of the collateral backing certain investments; weakening U.S. and global economic conditions, which could adversely affect the Company's ability to grow its business profitably; the potential effect of legislation and other governmental initiatives taken in response to the current financial crisis; 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; 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, which may be adversely affected by the current financial crisis; the Company's ability to successfully integrate operations, personnel and technology from its acquisitions, including the acquisition of Ohio Casualty Corporation ("Ohio Casualty") and its subsidiaries, and the recent acquisition of Safeco Corporation ("Safeco") 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 hurricanes, hail, tornados, 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, which could adversely affect its business volumes, adversely affect its ability to access the debt markets and increase its borrowing costs; 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 March 31, 2009 - Consolidated Results of Operations

- Revenues for the three months ended March 31, 2009 were \$7.406 billion, an increase of \$521 million or 7.6% over the same period in 2008.
- Net written premium for the three months ended March 31, 2009 was \$7.028 billion, an increase of \$772 million or 12.3% over the same period in 2008.
- Pre-tax operating income before private equity (loss) income for the three months ended was \$404 million, a decrease of \$28 million or 6.5% from the same period in 2008.
- Pre-tax operating income for the three months ended March 31, 2009 was \$31 million, a decrease of \$461 million or 93.7% from the same period in 2008.
- Net income for the three months ended March 31, 2009 was \$28 million, a decrease of \$332 million or 92.2% from the same period in 2008.
- Cash flow from operations for the three months ended March 31, 2009 was \$385 million, a decrease of \$228 million or 37.2% from the same period in 2008.
- The combined ratio before catastrophes¹ and net incurred losses attributable to prior years² for the three months ended March 31, 2009 was 97.3%, a decrease of 1.8 points from the same period in 2008. Including the impact of catastrophes and net incurred losses attributable to prior years, the Company's combined ratio for the three months ended March 31, 2009 decreased 1.2 points to 99.5%.

Financial Condition as of March 31, 2009

- Total assets were \$104.730 billion as of March 31, 2009, an increase of \$414 million over December 31, 2008.
- Policyholders' equity was \$10.387 billion as of March 31, 2009, an increase of \$227 million over December 31, 2008.

¹ Catastrophes include all current and prior year catastrophe losses including assessments from the Texas Windstorm Insurance Association ("TWIA") 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, the 2005 U.S. Hurricanes and the September 2008 Hurricanes. 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.

Other 2009 1st Quarter Highlights

- On January 22, 2009, the Company established Liberty Mutual Middle Market, a new market segment in Commercial Markets that combines the Business Market and Wausau Insurance market segments. As part of this change, the Company eliminated its direct distribution channel to its mid-sized commercial lines customers and retired the Wausau brand. Middle Market provides Liberty Mutual products and services exclusively through independent agents and brokers. As part of this change, on February 27, 2009, the Company completed the sale of the policy renewal rights of the existing Business Market and Wausau Insurance policyholders in various portions to three nationally recognized brokerage firms.
- On March 11, 2009, Liberty Mutual Insurance Company (“LMIC”), an affiliate of the Company, became a member of the Federal Home Loan Bank of Boston. To date, no funds have been borrowed.

Subsequent Events

- On April 9, 2009, A.M. Best affirmed its ‘A’ financial strength rating and revised the outlook for the Company to ‘negative’ from ‘stable’.

CONSOLIDATED RESULTS OF OPERATIONS

The Company has identified consolidated pre-tax operating income (“PTOI”) and net written premium as non-GAAP financial measures. PTOI is defined by the Company as pre-tax income excluding net realized gains (losses), extraordinary items, discontinued operations and cumulative effects of changes in accounting principles. PTOI is considered by the Company to be an appropriate indicator of underwriting and operating results and is consistent with the way the Company internally evaluates performance, except that limited partnership results recognized on the equity method are not included in internal PTOI. Net realized investment gains (losses) and private equity income (loss) 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 and 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. 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:

\$ in Millions	Three Months Ended March 31,		
	2009	2008	Change
Private passenger automobile	\$2,309	\$1,681	37.4%
Workers compensation	1,204	1,433	(16.0)
Commercial multiple peril / Fire	593	471	25.9
International local businesses	479	429	11.7
Homeowners	433	451	(4.0)
Commercial automobile	386	330	17.0
LIU ¹ reinsurance	382	327	16.8
General liability	310	342	(9.4)
LIU inland marine program	163	145	12.4
Bond	160	88	81.8
Group disability and life	147	137	7.3
LIU third party	122	100	22.0
LIU first party	61	63	(3.2)
Individual life	61	53	15.1
Assumed voluntary reinsurance	43	55	(21.8)
Other ²	175	151	15.9
Total net written premium³	\$7,028	\$6,256	12.3%

¹ Liberty International Underwriters (LIU).

² Primarily includes net written premium from domestic inland marine and allied lines.

³ Net written premium associated with internal reinsurance has been re-allocated to the appropriate lines of business.

Consolidated net written premium by SBU was as follows:

\$ in Millions	Three Months Ended March 31,		
	2009	2008	Change
Agency Markets	\$2,709	\$1,577	71.8%
International	1,692	1,577	7.3
Personal Markets	1,423	1,345	5.8
Commercial Markets	1,422	1,729	(17.8)
Corporate and Other ¹	(218)	28	NM
Total net written premium (NWP)	\$7,028	\$6,256	12.3%
Foreign exchange effect on growth			(3.2)
NWP growth excluding foreign exchange			15.5%

¹ Includes internal and external reinsurance.

NM = Not Meaningful

Major drivers of net written premium growth were as follows:

\$ in Millions	Three Months Ended March 31,			
	2009	2008	\$ Change	Pts. Attribution
LMG NWP	\$7,028	\$6,256	\$772	12.3
Components of Growth:				
Safeco	1,244	-	1,244	19.8
International local businesses (excluding foreign exchange)	1,173	1,007	166	2.7
Domestic personal auto ¹	1,134	1,103	31	0.5
Domestic homeowners ¹	491	451	40	0.6
Workers compensation booked as billed adjustment	(45)	(79)	34	0.5
Individual life	61	53	8	0.1
Group disability and life	147	137	10	0.1
Bond ¹	77	88	(11)	(0.1)
Foreign exchange	(198)	-	(198)	(3.2)
Homeowners quota share	(223)	-	(223)	(3.5)
Other commercial lines ¹	3,167	3,496	(329)	(5.2)
Total LMG NWP	\$7,028	\$6,256	\$772	12.3

¹ Excludes Safeco premium.

Net written premium for the three months ended March 31, 2009 was \$7.028 billion, an increase of \$772 million over the same period in 2008. Significant changes by major line of business include:

- Private passenger automobile net written premium increased \$628 million over the same period in 2008. The increase primarily reflects approximately \$615 million of premium related to the Safeco acquisition completed on September 22, 2008, organic growth in International's local businesses primarily in Latin America and strong new business growth in Personal Markets. The increase was partially offset by weaker foreign currencies versus the prior period (approximately \$73 million).
- Workers compensation net written premium decreased \$229 million from the same period in 2008. The decrease primarily reflects lower retention and new business writings in Commercial and Agency Markets reflecting a very competitive market and the impact of an 18.9% state mandated rate decrease in Florida. Partially offsetting the decrease were modest rate increases (excluding Florida) and approximately \$29 million of premium related to the Safeco acquisition.

- Commercial multiple peril/fire new written premium increased \$122 million over the same period in 2008. The increase primarily reflects approximately \$126 million of premium related to the Safeco acquisition.
- International local businesses net written premium (excluding private passenger automobile), increased \$50 million over the same period in 2008. The increase reflects organic growth in International's local businesses, primarily in Latin America, and to a lesser extent, Asia Pacific, partially offset by a decline in Europe as a result of the region's general economic contraction. Partially offsetting the increase was the impact of weaker foreign currencies versus the U.S. dollar (approximately \$61 million).
- Homeowners net written premium decreased \$18 million from the same period in 2008. The decrease reflects the impact of \$223 million related to a homeowners quota share reinsurance treaty entered into in 2008. Partially offsetting the decrease was approximately \$165 million related to the Safeco acquisition and strong customer retention, new business growth and rate increases in Personal Markets.
- Commercial automobile net written premium increased \$56 million over the same period in 2008. The increase reflects approximately \$97 million of premium related to the Safeco acquisition. Partially offsetting the increase was lower retention and reduced new business in Commercial and Agency Markets due to a more competitive environment.
- LIU reinsurance net written premium increased \$55 million over the same period in 2008. The increase was primarily a result of an improved rate environment.
- General liability net written premium decreased \$32 million from the same period in 2008. The decrease reflects a reduction in premium of \$59 million within the National Market segment of Commercial Markets driven by a multi-year construction account written in 2008 that did not recur, and a decline in construction projects. Partially offsetting the decrease was approximately \$41 million of premium related to the Safeco acquisition.
- Bond net written premium increased \$72 million over the same period in 2008. The increase primarily reflects approximately \$83 million of premium related to the Safeco acquisition partially offset by reduced exposures of existing policyholders due to economic conditions.
- LIU third party net written premium increased \$22 million over the same period in 2008. The change reflects a decrease in ceded written premium due to a change in the structure of a reinsurance program, partially offset by the weakening of foreign currencies versus the U.S. dollar.

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 March 31,		
	2009	2008	Change
Revenues	\$7,406	\$6,885	7.6%
PTOI before catastrophes, net incurred losses attributable to prior years and private equity (loss) income	\$547	\$523	4.6
Catastrophes ¹ :			
-September 2008 Hurricanes	(6)	-	NM
-All other ²	(320)	(166)	92.8
Net incurred losses attributable to prior years:			
- Asbestos & environmental	(1)	-	NM
- All other ³	184	75	145.3
Pre-tax operating income before private equity (loss) income	404	432	(6.5)
Private equity (loss) income ⁴	(373)	60	NM
Pre-tax operating income	31	492	(93.7)
Realized gains (losses), net	6	(12)	150.0
Federal and foreign income tax expense	(9)	(120)	(92.5)
Net income	\$28	\$360	(92.2%)
Cash flow from operations	\$385	\$613	(37.2%)

1 Catastrophes include all current and prior year catastrophe losses including assessments from TWIA 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, the 2005 U.S. Hurricanes and the September 2008 Hurricanes. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

2 Catastrophe losses ceded under the homeowners quota share treaty are included to the extent that the ceded combined ratio exceeds 100.0%.

3 Net of earned premium attributable to prior years of zero and \$3 million for the three months ended March 31, 2009 and 2008, respectively. Net of amortization of deferred gains on retroactive reinsurance of \$17 million for the three months ended March 31, 2009 and 2008, respectively.

4 Private equity (loss) income is included in net investment income in the accompanying statements of income.

NM = Not Meaningful

Revenues for the three months ended March 31, 2009 were \$7.406 billion, an increase of \$521 million over the same period in 2008. The major components of revenues are net premium earned, net investment income, net realized gains (losses), and fee and other revenues.

Net premium earned for the three months ended March 31, 2009 was \$6.882 billion, an increase of \$944 million over the same period in 2008. The increase in the quarter primarily reflects approximately \$1.265 billion of premium related to the acquisition of Safeco. Partially offsetting the increase were \$247 million of ceded premium related to the homeowners quota share treaty and approximately \$202 million of negative foreign exchange impact due to a stronger dollar.

Net investment income for the three months ended March 31, 2009 was \$337 million, a decrease of \$420 million from the same period in 2008. The decrease is primarily the result of reduced valuations for investments in limited partnerships and limited liability companies and dividend income as a result of a change in investment strategy to reduce the total equity portfolio exposure. Partially offsetting these decreases were increases in interest income, primarily due to a higher invested asset base resulting from the Safeco acquisition and the continued investment of cash flows from operations.

Net realized gains (losses) for the three months ended March 31, 2009 were \$6 million, compared to losses of (\$12) million in the same period in 2008. Net gains for the three months ended March 31, 2009 reflect gains recognized from sales related to the Company's decision to reduce its exposure to the equity markets, and other gains. In addition, the Company recorded net derivative gains of \$25 million for the three

months ended March 31, 2009 associated with the equity swap derivative contracts the Company entered into in August 2008 and that were terminated in January 2009. Partially offsetting these net gains were higher impairment losses on fixed maturity and equity securities deemed to be other-than-temporarily impaired.

Fee and other revenues for the three months ended March 31, 2009 were \$181 million, a decrease of \$21 million from the same period in 2008. The decrease reflects a reduction in oil and gas revenues due to price declines and 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 months ended March 31, 2009 were \$7.369 billion, an increase of \$964 million over the same period in 2008. The increase in the quarter primarily reflects the acquisition of Safeco, organic business growth, in particular International's Latin America operations, higher catastrophe losses related to winter and Midwest hail storms and higher interest expense as a result of the Company's May 2008 debt offering. Partially offsetting the increase were ceded losses and expenses associated with the homeowners quota share reinsurance treaty, more favorable incurred losses attributable to prior years, primarily related to Agency Markets workers compensation and general liability lines, and the impact of weaker foreign currencies versus the U.S dollar.

	Three Months Ended March 31,		
	2009	2008	Change (Points)
CONSOLIDATED			
Combined ratio before catastrophes and net incurred losses attributable to prior years			
Claims and claim adjustment expense ratio	69.4%	71.2%	(1.8)
Underwriting expense ratio	27.7	27.6	0.1
Dividend ratio	0.2	0.3	(0.1)
Subtotal	97.3	99.1	(1.8)
Catastrophes ¹ :			
-September 2008 Hurricanes	0.1	-	0.1
-All other	4.8	2.9	1.9
Net incurred losses attributable to prior years:			
- Asbestos & environmental	-	-	-
- All other	(2.7)	(1.3)	(1.4)
Total combined ratio²	99.5%	100.7%	(1.2)

- 1 Catastrophes include all current and prior year catastrophe losses including assessments from TWIA 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, the 2005 U.S. Hurricanes and the September 2008 Hurricanes. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.
- 2 The combined 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 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 months ended March 31, 2009 was 97.3%, a decrease of 1.8 points from the same period in 2008. The decrease in the claims and claim adjustment expense ratio reflects the impact of Agency Markets favorable Regional Company results across both property and liability lines and a greater weighting of personal lines results due to lower loss ratios from the acquired Safeco personal lines business. The decrease was partially offset by an increase in the Commercial Markets claims and claim adjustment expense ratio due to increasing loss trends in workers compensation and general liability businesses and higher loss ratios in Summit due to a mandatory rate decrease in the state of Florida. The increase in the underwriting expense ratio reflects the impact of the homeowners quota share reinsurance treaty, partially offset by the greater weighting of personal results mentioned above and reduced compensation costs.

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three months ended March 31, 2009 was 99.5%, a decrease of 1.2 points from the same period in 2008. The decrease in the quarter primarily reflects the change in the combined ratio components previously discussed and the impact of the favorable net incurred loss development attributable to prior years in the workers compensation and general liability lines of business. Partially offsetting the decrease were higher catastrophe losses due primarily to the winter and Midwest hail storms.

PTOI for the three months ended March 31, 2009 was \$31 million, a decrease of \$461 million from the same period in 2008.

Federal and foreign income tax expense for the three months ended March 31, 2009 was \$9 million, a decrease of \$111 million from the same period in 2008. The Company's effective tax rate for the three months ended March 31, 2009 was 24.0%, compared to 25.0% for the same period in 2008. 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 months ended March 31, 2009 was \$28 million, a decrease of \$332 million from the same period in 2008.

Cash flow from operations for the three months ended March 31, 2009 was \$385 million, a decrease of \$228 million from the same period in 2008. The decrease primarily reflects ceded premium payments for the homeowners quota share treaty, other external catastrophe reinsurance payments, and an increase in catastrophe loss payments. Partially offsetting the decrease were lower non-catastrophe losses and reduced general expenses.

AGENCY MARKETS

Overview – Agency Markets

Agency Markets delivers personal and commercial insurance products and services to individuals and businesses through independent agents throughout the United States. Commercial lines products are offered through eight regional insurance companies that combine their local underwriting, market knowledge and service orientation with the cost efficiencies of a national company. Personal lines products are distributed nationally using the Safeco brand, with a focus on product and pricing sophistication. Liberty Mutual Surety is a leading provider of nationwide contract and commercial surety bonds. Summit provides workers compensation in the Southeast (primarily Florida).

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

\$ in Millions	Three Months Ended March 31,		
	2009¹	2008¹	Change
Regional Companies Group	\$1,143	\$894	27.9%
Safeco	1,186	308	NM
Summit	181	253	(28.5%)
Liberty Mutual Surety	160	89	79.8%
Other ²	39	33	18.2%
Total net written premium	\$2,709	\$1,577	71.8%

1 Effective in the first quarter 2009, net written premium of both legacy Safeco and Regional Companies Group have been reclassified as follows: a) commercial lines operations are reflected in the Regional Companies Group segment; this segment also includes excess casualty operations previously reflected in Other, b) personal lines results are reflected in the Safeco segment and c) surety and fidelity operations are reflected in the Liberty Mutual Surety segment. The prior periods have been restated to reflect these changes.

2 Includes run-off operations and internal reinsurance.

NM= Not Meaningful

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

\$ in Millions	Three Months Ended March 31,		
	2009	2008	Change
Commercial Lines			
Workers compensation total:	\$409	\$477	(14.3%)
- Summit	181	253	(28.5%)
- All other	228	224	1.8%
Commercial multiple peril	467	347	34.6%
Commercial automobile	278	205	35.6%
General liability	127	91	39.6%
Bond	160	88	81.8%
Other Commercial	66	55	20.0%
Subtotal	\$1,507	\$1,263	19.3%
Personal Lines			
Private passenger automobile	\$806	\$197	NM
Homeowners	296	97	NM
Other Personal	100	20	NM
Subtotal	\$1,202	\$314	NM
Total net written premium	\$2,709	\$1,577	71.8%

NM = Not Meaningful

Net written premium for the three months ended March 31, 2009 was \$2.709 billion, an increase of \$1.132 billion over the same period in 2008. The increase reflects the impact of the Safeco acquisition which contributed approximately \$1.244 billion of the change. This increase represents additional written premium of approximately \$845 million in personal lines and \$399 million in commercial lines. The increase was partially offset by lower retention and new business across most commercial lines due to a more competitive environment, reductions in exposure due to the contraction of the economy, and state mandated rate decreases of 18.9% in Florida workers compensation.

Results of Operations – Agency Markets

\$ in Millions	Three Months Ended March 31,		
	2009	2008	Change
Revenues	\$3,034	\$1,647	84.2%
PTOI before catastrophes and net incurred losses attributable to prior years	\$329	\$108	NM%
Catastrophes ¹			
-September 2008 Hurricanes	(14)	-	NM
-All other	(192)	(80)	140.0%
Net incurred losses attributable to prior years:			
- Asbestos & environmental	-	-	
- All other ²	151	66	128.8%
Pre-tax operating income	\$274	\$94	191.5%

1 Catastrophes include all current and prior year catastrophe losses including assessments from TWIA. Catastrophe losses, where applicable, include the impact of accelerated earned premiums and earned reinstatement premiums.

2 Net of earned premium attributable to prior years of (\$3) million and (\$4) million for the three months ended March 31, 2009 and 2008 respectively.

NM = Not Meaningful

Revenues for the three months ended March 31, 2009 were \$3.034 billion, an increase of \$1.387 billion over the same period in 2008. The major components of revenues are net premium earned, net investment income, and fee and other revenues.

Net premium earned for the three months ended March 31, 2009 was \$2.786 billion, an increase of \$1.293 billion over the same period in 2008. The increase reflects approximately \$1.265 billion of premium related to the Safeco acquisition in the quarter and earned premium associated with the other changes in net written premium in 2008 and first quarter of 2009 previously discussed.

Net investment income for the three months ended March 31, 2009 was \$218 million, an increase of \$79 million over the same period in 2008. The increase reflects an increase in invested assets due to the Safeco acquisition and the continued investment of cash flow from operations.

Fee and other revenues for the three months ended March 31, 2009 was \$30 million, an increase of \$15 million over the same period in 2008. The increase primarily reflects increased finance and service charges as a result of the Safeco acquisition.

Claims, benefits and expenses for the three months ended March 31, 2009 were \$2.760 billion, an increase of \$1.207 billion over the same period in 2008. The increase primarily reflects the impact of the Safeco acquisition and higher catastrophe losses related to winter and Midwest hail storms partially offset by favorable incurred losses attributable to prior years in liability lines.

	Three Months Ended March 31,		
	2009	2008	Change (Points)
AGENCY MARKETS			
Combined ratio before catastrophes and net incurred losses attributable to prior years			
Claims and claim adjustment expense ratio	64.5%	68.7%	(4.2)
Underwriting expense ratio ¹	30.1	32.2	(2.1)
Dividend ratio	0.3	0.8	(0.5)
Subtotal	94.9	101.7	(6.8)
Catastrophes ² :			
-September 2008 Hurricanes	0.5	-	0.5
-All other	6.9	5.3	1.6
Net incurred losses attributable to prior years:			
- Asbestos & environmental	-	-	-
- All other	(5.4)	(4.4)	(1.0)
Total combined ratio	96.9%	102.6%	(5.7)

1 One-time Safeco integration costs have been excluded from the combined ratio.

2 Catastrophes include all current and prior year catastrophe losses including assessments from TWIA. Catastrophe losses, where applicable, include the impact of accelerated earned premiums and earned reinstatement premiums.

The Agency Markets combined ratio before catastrophes and net incurred losses attributable to prior years for the three months ended March 31, 2009 was 94.9%, a decrease of 6.8 points from the same period in 2008. The decrease in the claims and claim adjustment expense ratio reflects favorable Regional Companies Group results across both property and liability lines (2.1%) and favorable personal lines results due to lower loss ratios from the acquired Safeco personal lines business (2.4%), partially offset by higher loss ratios in Summit due to the state mandated decrease in rates. The decrease in the underwriting expense ratio reflects the impact of writing more personal lines business due to the Safeco acquisition, which typically has a lower expense ratio (2.0%).

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three months ended March 31, 2009 was 96.9%, a decrease of 5.7 points from the same period in 2008. The decrease in the quarter primarily reflects the changes in the combined ratio previously discussed and favorable incurred losses attributable to prior years in liability lines due to moderate frequency and severity trends, partially offset by higher catastrophe losses due to the winter and Midwest hail storms.

PTOI for the three months ended March 31, 2009 was \$274 million, an increase of \$180 million over the same period in 2008.

INTERNATIONAL

Overview – International

International provides insurance products and services through two distinct approaches: local businesses, which sell personal and small commercial lines products, and Liberty International Underwriters (“LIU”) which sells specialty commercial lines worldwide. International's local business operations consist of local insurance operations selling traditional property, casualty, health and life insurance products to individuals and businesses in countries with a large and growing middle class. Automobile insurance is the predominant line of business. In Latin America, International operates in Venezuela, Argentina, Colombia, Brazil and Chile. In Asia, International writes business in Singapore, Thailand, Vietnam and China (including Hong Kong). In Europe, International operates in Spain, Portugal, Turkey and Poland. LIU writes casualty, specialty casualty, marine, energy, construction, aviation and property coverages through offices in Asia, Australia, Europe, the Middle East and North America. LIU, through its Lloyd's Syndicate 4472, also provides multi-line insurance and reinsurance, including property catastrophe reinsurance, on a worldwide basis.

International net written premium by market segment was as follows:

\$ in Millions	Three Months Ended March 31,		
	2009	2008	Change
International Local Businesses Total	\$1,019	\$988	3.1%
- Latin America	679	587	15.7
- Europe	278	344	(19.2)
- Asia	62	57	8.8
Liberty International Underwriters	673	589	14.3
Total net written premium (NWP)	\$1,692	\$1,577	7.3%
Foreign exchange effect on growth			(12.6%)
NWP growth excluding foreign exchange			19.9%

International’s major product lines 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: handset protection coverage for lost or damaged devices;
- (4) LIU third party: includes casualty, excess casualty, D&O, E&O, professional liability, environmental impairment liability, railroad and other;
- (5) LIU first party: includes marine, energy, construction, aviation and property; and
- (6) LIU other: includes workers compensation, commercial automobile, surety, trade credit, crisis management and residual value.

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

\$ in Millions	Three Months Ended March 31,		
	2009	2008	Change
Local businesses – private passenger auto	\$556	\$578	(3.8%)
Local businesses – all other ¹	463	410	12.9
LIU reinsurance	335	285	17.5
LIU inland marine program	163	145	12.4
LIU third party	110	90	22.2
LIU first party	56	58	(3.4)
LIU other	9	11	(18.2)
Total net written premium	\$1,692	\$1,577	7.3%

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

Net written premium for the three months ended March 31, 2009 was \$1.692 billion, an increase of \$115 million over the same period in 2008. This increase reflects organic growth in both LIU and local businesses. LIU's growth was primarily attributable to its reinsurance business which benefited from an improved rate environment. Growth in the period also reflects 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 and the continued expansion of LIU's inland marine program. Organic growth within the local businesses occurred primarily in Latin America, and to a lesser extent, Asia Pacific, partially offset by a decline in Europe as a result of the region's general economic contraction. These increases were partially offset by the weakening of foreign currencies versus the U.S. dollar (approximately \$198 million).

Results of Operations – International

\$ in Millions	Three Months Ended March 31,		
	2009	2008	Change
Revenues	\$1,728	\$1,731	(0.2%)
PTOI before catastrophes and net incurred losses attributable to prior years	\$128	\$125	2.4%
Catastrophes ¹			
-September 2008 Hurricanes	(3)	-	NM
-All other	(1)	-	NM
Net incurred losses attributable to prior years:			
- Asbestos & environmental	-	-	NM
- All other ²	(2)	6	NM
Pre-tax operating income	\$122	\$131	(6.9%)

1 Catastrophes include all current and prior year catastrophe losses including assessments from TWIA 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, the 2005 U.S. Hurricanes and the September 2008 Hurricanes. 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 for the three months ended March 31, 2009 and 2008, respectively.

NM = Not Meaningful

Revenues for the three months ended March 31, 2009 were \$1.728 billion, a decrease of \$3 million from the same period in 2008. The major components of revenues are net premium earned and net investment income.

Net premium earned for the three months ended March 31, 2009 was \$1.536 billion, a decrease of \$3 million from the same period in 2008. The decrease reflects the impact of weaker foreign currencies versus the U.S. dollar (approximately \$202 million), partially offset by growth in net written premium in the latter half of 2008 and in the first quarter of 2009.

Net investment income for the three months ended March 31, 2009 was \$148 million, a decrease of \$4 million from the same period in 2008. The decrease reflects the impact of weaker foreign currencies versus the U.S. dollar (approximately \$182 million), partially offset by a higher invested asset base.

Claims, benefits and expenses for the three months ended March 31, 2009 were \$1.598 million, a decrease of \$5 million from the same period in 2008. The decrease reflects the impact of weaker foreign currencies versus the U.S. dollar, partially offset by the previously mentioned business growth in the local businesses and LIU, as well as the increase in commission expense primarily due to a change in the structure of a reinsurance program in LIU's third party business.

	Three Months Ended March 31,		
	2009	2008	Change (Points)
INTERNATIONAL			
Combined ratio before catastrophes and net incurred losses attributable to prior years			
Claims and claim adjustment expense ratio	69.2%	69.2%	-
Underwriting expense ratio	31.0	31.1	(0.1)
Dividend ratio	-	-	-
Subtotal	100.2	100.3	(0.1)
Catastrophes ¹ :			
-September 2008 Hurricanes	0.2	-	0.2
-All other	0.1	-	0.1
Net incurred losses attributable to prior years:			
- Asbestos & environmental	-	-	-
- All other	0.1	(0.4)	0.5
Total combined ratio	100.6%	99.9%	0.7

¹ Catastrophes include all current and prior year catastrophe losses including assessments from TWIA 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, the 2005 U.S. Hurricanes and the September 2008 Hurricanes. Catastrophe losses, where applicable, include the impact of accelerated earned catastrophe premiums and earned reinstatement premiums.

NM = Not Meaningful

The consolidated combined ratio before catastrophes and net incurred losses attributable to prior years for the three months ended March 31, 2009 was 100.2%, a decrease of 0.1 point from the same period in 2008.

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three months ended March 31, 2009 was 100.6%, an increase of 0.7 points over the same period in 2008. This reflects the impact of unfavorable catastrophe loss development related to the 2004, 2005 and September 2008 Hurricanes in LIU's first party business, and a decrease in the amount of net favorable incurred loss development attributable to the prior years.

PTOI for the three months ended March 31, 2009 was \$122 million, a decrease of \$9 million from the same period in 2008.

PERSONAL MARKETS

Overview – Personal Markets

Personal Markets sells primarily automobile, homeowners and other types of property and casualty insurance coverage, as well as a wide range of life and annuity products, to individuals in the United States. Products are distributed through approximately 1,800 licensed captive sales representatives, approximately 500 licensed telesales counselors, third-party producers and the Internet. Personal Markets' largest source of new business is through its more than 11,850 sponsored affinity groups (including employers, professional associations and alumni associations, credit unions, and other partnerships). Personal Markets' coverages are primarily personal automobile and homeowners.

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

\$ in Millions	Three Months Ended March 31,		
	2009	2008	Change
Private passenger automobile	\$942	\$906	4.0%
Homeowners and other	420	386	8.8
Individual life	61	53	15.1
Total net written premium	\$1,423	\$1,345	5.8%

Net written premium for the three months ended March 31, 2009 was \$1.423 billion, an increase of \$78 million over the same period in 2008. The increase reflects new business growth, strong customer retention in both automobile and homeowners and rate increases on homeowners policies. For individual life, the increase in the quarter reflects higher structured settlement sales.

Private passenger automobile net written premium for the three months ended March 31, 2009 was \$942 million, an increase of \$36 million over the same period in 2008. The increase reflects a 4.9% increase in voluntary policies in-force as compared to March 31, 2008 due to strong customer retention and new business growth, partially offset by lower average premium per policy due primarily to the effect of rate decreases in Massachusetts. The introduction of managed competition in 2008 provided the Company with the opportunity to significantly increase its presence in the Massachusetts automobile insurance market.

Homeowners and other net written premium for the three months ended March 31, 2009 was \$420 million, an increase of \$34 million over the same period in 2008. The increase reflects rate increases and a 4.9% increase in policies in-force (1.6 points related to renters policies) as compared to March 31, 2008 due to strong customer retention and new business growth, primarily in non-coastal areas. In addition, approximately one point of the policies in-force growth is attributable to the relationship established with GEICO in late 2007, which allows GEICO to offer Liberty Mutual homeowners products to its auto prospects and customers through the Internet and call centers.

Individual life net written premium for the three months ended March 31, 2009 was \$61 million, an increase of \$8 million over the same period in 2008. The increase in the quarter reflects higher structured settlement sales.

Results of Operations – Personal Markets

\$ in Millions	Three Months Ended March 31,		
	2009	2008	Change
Revenues	\$1,671	\$1,634	2.3%
PTOI before catastrophes and net incurred losses attributable to prior years and private equity income	\$222	\$204	8.8
Catastrophes ¹ :			
-September 2008 Hurricanes	21	-	NM
-All other	(123)	(64)	92.2
Net incurred losses attributable to prior years:			
- Asbestos & environmental	-	-	-
- All other	18	2	NM
Pre-tax operating income before private equity income	138	142	(2.8)
Private equity income ²	7	-	NM
Pre-tax operating income	\$145	\$142	2.1%

1 Catastrophes include all current and prior year catastrophe losses including assessments from TWIA. Catastrophe losses, where applicable, include the impact of accelerated earned premiums and earned reinstatement premiums.

2 Private equity income is included in net investment income in the accompanying statements of income.

NM = Not Meaningful

Revenues for the three months ended March 31, 2009 were \$1.671 billion, an increase of \$37 million over the same period in 2008. The major components of revenues are net premium earned, net investment income, and fee and other revenues.

Net premium earned for the three months ended March 31, 2009 was \$1.478 billion, an increase of \$48 million over the same period in 2008. The increase reflects the earned premium associated with the changes in net written premium for both the voluntary automobile and homeowners lines of business in 2008 and 2009. For individual life, the increase in the quarter reflects higher structured settlement sales.

Net investment income for the three months ended March 31, 2009 was \$183 million, an increase of \$9 million over the same period in 2008.

Claims, benefits and expenses for the three months ended March 31, 2009 was \$1.546 billion, an increase of \$52 million over the same period in 2008. The increase reflects business growth, general cost increases, and higher catastrophe losses driven by increased severity of winter and hail storms. This was partially offset by lower profit share expense related to business acquired from Prudential Financial, Inc. (“PruPac”), favorable development on the September 2008 hurricanes, and an increase in the amount of favorable prior year loss development on state pools and increased ceded losses on quota share reinsurance.

	Three Months Ended March 31,		
	2009	2008	Change (Points)
PERSONAL MARKETS			
Combined ratio before catastrophes and net incurred losses attributable to prior years			
Claims and claim adjustment expense ratio	65.3%	65.5%	(0.2)
Underwriting expense ratio	24.6	25.7	(1.1)
Dividend ratio	-	-	-
Subtotal	89.9	91.2	(1.3)
Catastrophes ¹ :			
-September 2008 Hurricanes	(1.5)	-	(1.5)
-All other	8.7	4.7	4.0
Net incurred losses attributable to prior years:			
- Asbestos & environmental	-	-	-
- All other	(1.3)	(0.2)	(1.1)
Total combined ratio	95.8%	95.7%	0.1

1 Catastrophes include all current and prior year catastrophe losses including assessments from TWIA. Catastrophe losses, where applicable, include the impact of accelerated earned premiums and earned reinstatement premiums.

The Personal Markets combined ratio before catastrophes and net incurred losses attributable to prior years for the three months ended March 31, 2009 was 89.9%, a decrease of 1.3 points from the same period in 2008. The decrease in the claims and claim adjustment expense ratio is mainly related to favorable loss trends in the automobile physical damage line of business. The decrease in the underwriting expense ratio was primarily due to lower profit share expense related to PruPac.

Including the impact of catastrophes and net incurred losses attributable to prior years, the total combined ratio for the three months ended March 31, 2009 was 95.8%, an increase of 0.1 points over the same period in 2008. The increase reflects the changes in the combined ratio previously discussed and higher catastrophe losses related to increased severity of winter and hail storms. This was partially offset by favorable development on the September 2008 hurricanes and an increase in the amount of favorable net incurred loss development attributable to prior years due to growth in affinity quota share reinsurance agreements and state pool activity.

PTOI for the three months ended March 31, 2009 was \$145 million, representing an increase of \$3 million over the same period in the prior year.

COMMERCIAL MARKETS

Overview – Commercial Markets

Commercial Markets offers a wide array of commercial insurance and reinsurance coverages to U.S. employers and insurance companies, respectively. Products are distributed primarily by agents and brokers, a direct national accounts sales force, employee benefits brokers, and consultants. The Commercial Markets business unit is organized into separate marketing and underwriting groups, each of which focuses on a particular customer base, product grouping or distribution channel to provide tailored products and services that specifically address customers' needs. The Commercial Markets coverages include workers compensation, commercial automobile, general liability (including product liability), group disability and life, commercial multiple peril and fire, assumed voluntary reinsurance, and a variety of other coverages. The Company is also a servicing carrier for state based workers compensation involuntary market pools.

On January 22, 2009, Commercial Markets established Middle Market, a new market segment that combines the Business Market and Wausau Insurance market segments. As part of this change, Commercial Markets eliminated its direct distribution channel to its mid-sized commercial lines customers and retired the Wausau brand. Middle Market provides Liberty Mutual products and services exclusively through independent agents and brokers. As part of this change, the Company completed the sale of the policy renewal rights of the existing Business Market and Wausau Insurance policyholders in various portions to three nationally recognized brokerage firms on February 27, 2009.

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

\$ in Millions	Three Months Ended March 31,		
	2009	2008	Change
Middle Market ^{1,2}	\$581	\$765	(24.1%)
National Market ²	379	485	(21.9)
Group Market	147	137	7.3
Specialty Lines ³	115	126	(8.7)
Liberty Mutual Property	80	89	(10.1)
Other Markets	120	127	(5.5)
Total net written premium	\$1,422	\$1,729	(17.8%)

1 Effective in the fourth quarter 2008, net written premium associated with Business Markets and Wausau Insurance, previously reported separately, is now included in Middle Market. The prior periods have been restated to reflect this change.

2 Effective November 1, 2008, certain accounts with available premium and premium equivalents greater than \$1.5 million, previously reported as part of Middle Market, have been transferred upon renewal to National Market. The first quarter of 2008 included approximately \$100 million of net written premium that met this definition included in Middle Market. The prior periods have been restated to reflect these changes.

3 Effective in the fourth quarter 2008, net written premium associated with Commercial Affinity, previously reported as part of Wausau Insurance, is now included in Specialty Lines. The prior periods have been restated to reflect this change.

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

\$ in Millions	Three Months Ended March 31,		
	2009	2008	Change
Workers compensation	\$832	\$1,022	(18.6%)
General liability	139	236	(41.1)
Group disability and life	147	137	7.3
Commercial automobile	106	124	(14.5)
Commercial multiple peril / Fire	107	119	(10.1)
Assumed voluntary reinsurance	43	39	10.3
Other	48	52	(7.7)
Total net written premium	\$1,422	\$1,729	(17.8%)

Net written premium for the three months ended March 31, 2009 was \$1.422 billion, a decrease of \$307 million from the same period in 2008. The decrease reflects lower retention levels and new business writings across most lines of business and market segments, most pronounced in the Middle Market segment. In addition, general liability premium decreased \$59 million in the National Market segment driven by a multi-year construction account written in 2008 that did not recur, and a decline in construction projects. Partially offsetting the decrease in the quarter was an increase in assumed voluntary reinsurance included in the Other Markets segment, as well as an increase in group disability and life business due to a broader penetration of those markets.

Results of Operations – Commercial Markets

\$ in Millions	Three Months Ended March 31,		
	2009	2008	Change
Revenues	\$1,604	\$1,702	(5.8%)
PTOI before catastrophes and net incurred losses attributable to prior years	110	113	(2.7)
Catastrophes ¹ :			
-September 2008 Hurricanes	-	-	-
-All other	(6)	(15)	(60.0)
Net incurred losses attributable to prior years:			
- Asbestos & environmental	-	-	-
- All other ²	19	10	90.0
Pre-tax operating income	\$123	\$108	13.9%

- 1 Catastrophes include all current and prior year catastrophe losses including assessments from TWIA and exclude losses related to the Company's assumed voluntary reinsurance except for losses related to the events of September 11, 2001, the 2004 U.S. Hurricanes, the 2005 U.S. Hurricanes and the September 2008 Hurricanes. 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 \$3 million and \$8 million for and the three months ended March 31, 2009 and 2008, respectively. Net of amortization of deferred gains on retroactive reinsurance of \$12 million for the three months ended March 31, 2009 and 2008, respectively.

Revenues for the three months ended March 31, 2009 were \$1.604 billion, a decrease of \$98 million from the same period in 2008. The major components of revenues are net premium earned, net investment income and fee and other revenues.

Net premium earned for the three months ended March 31, 2009 was \$1.321 billion, a decrease of \$98 million from the same period in 2008. The decrease in earned premium reflects the decrease in net written premium during 2008 and the first quarter of 2009.

Net investment income for the three months ended March 31, 2009 was \$210 million, an increase of \$7 million over the same period in 2008. The increase primarily reflects a higher invested asset base due to the continued investment of cash flow from operations.

Fee and other revenues for the three months ended March 31, 2009 was \$73 million, a decrease of \$7 million from the same period in 2008. The decrease primarily reflects 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 months ended March 31, 2009 was \$1.481 billion, a decrease of \$113 million from the same period in 2008. The decrease primarily reflects lower non-catastrophe and catastrophe related property losses and lower workers compensation losses due to reserve weakening from the involuntary market workers compensation pools. Compensation related expenses have decreased, primarily as a result of the Middle Market reorganization. In addition, a decline in exposures and net written premium resulted in declining claims and premium tax expense.

	Three Months Ended March 31,		
	2009	2008	Change (Points)
COMMERCIAL MARKETS			
Combined ratio before catastrophes and net incurred losses attributable to prior years			
Claims and claim adjustment expense ratio	84.3%	83.2%	1.1
Underwriting expense ratio	20.7	21.5	(0.8)
Dividend ratio	0.6	0.6	-
Subtotal	105.6	105.3	0.3
Catastrophes ¹ :			
-September 2008 Hurricanes	-	-	-
-All other	0.5	1.1	(0.6)
Net incurred losses attributable to prior years:			
- Asbestos & environmental	-	-	-
- All other	(1.7)	(0.7)	(1.0)
Total combined ratio	104.4%	105.7%	(1.3)

1 Catastrophes include all current and prior year catastrophe losses including assessments from TWIA and exclude losses related to the Company's assumed voluntary reinsurance except for losses related to the events of September 11, 2001, the 2004 U.S. Hurricanes, the 2005 U.S. Hurricanes and the September 2008 Hurricanes. 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 months ended March 31, 2009 was 105.6%, an increase of 0.3 points over the same period in 2008. The increase in the claims and claim adjustment expense ratio primarily reflects a higher claims and claim adjustment expense ratio in the workers compensation and general liability lines of business due to increasing loss trends. Also contributing to the increase are losses related to a 2009 plane crash in Buffalo, New York, partially offset by lower non-catastrophe related property losses. The decrease in the underwriting expense ratio primarily reflects a decrease in the premium tax ratio due to a shift in the mix of premium by state and a decrease in the New York premium tax rate. In addition, the general expense ratio has decreased driven by lower compensation related expenses, primarily as a result of the Middle Market reorganization, partially offset 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 months ended March 31, 2009 was 104.4%, a decrease of 1.3 points from the same period in 2008. The decrease reflects the changes in the combined ratio previously discussed offset by

lower catastrophe losses and favorable net incurred losses attributable to prior years driven by involuntary pool workers compensation reserve weakening in the first quarter of 2009.

PTOI for the three months ended March 31, 2009 was \$123 million, an increase of \$15 million over the same period in 2008.

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, pre-2004 Commercial Markets assumed voluntary reinsurance business and Commercial Markets pre-2005 fully insured workers compensation business.
- Interest expense on the Company's outstanding debt.
- As part of its risk management program, the Company reinsures certain risks of its SBUs.
- The Company reports its written premiums on workers compensation contracts on the "booked as billed" method. Commercial Markets and Agency Markets report workers compensation 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.

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

\$ in Millions	Three Months Ended March 31,		
	2009	2008	Change
Reinsurance, net	(\$173)	\$106	NM
Workers compensation ¹	(45)	(79)	(43.0%)
Other	-	1	(100%)
Total net written premium	(\$218)	\$28	NM

¹ Booked as billed adjustment
 NM = Not Meaningful

Net written premium for the three months ended March 31, 2009 was (\$218) million, a decrease of \$246 million from the same period from 2008. The decrease is primarily driven by an increase in externally ceded reinsurance. In the fourth quarter of 2008, the Company entered into a reinsurance contract where the Company cedes a pro rata portion of consolidated U.S. direct written homeowners premiums. In the quarter, the impact on net written premium was \$223 million. The decrease in the quarter is also driven by a decrease in internal reinsurance of \$56 million, partially offset by an increase in the Company's workers compensation "booked as billed" adjustment of \$34 million.

Results of Operations – Corporate and Other

\$ in Millions	Three Months Ended March 31,		
	2009	2008	Change
Revenues	(\$631)	\$171	NM
PTOI before catastrophes, net incurred losses attributable to prior years and private equity (loss) income	(\$242)	(\$27)	NM
Catastrophes ¹ :			
-September 2008 Hurricanes	(10)	-	NM
-All other ²	2	(7)	NM
Net incurred losses attributable to prior years:			
- Asbestos & environmental	(1)	-	NM
- All other ³	(2)	(9)	(77.8)
Pre-tax operating (loss) income before private equity (loss) income	(253)	(43)	NM
Private equity (loss) income ⁴	(380)	60	NM
Pre-tax operating (loss) income	(\$633)	\$17	NM

1 Catastrophes include all current and prior year catastrophe losses including assessments from TWIA 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 of \$2 million and \$1 million for the three months ended March 31, 2009 and 2008, respectively.

2 Catastrophe losses ceded under the homeowners quota share treaty are included to the extent that the ceded combined ratio exceeds 100.0%.

3 Net of amortization of deferred gains on retroactive reinsurance of \$5 million for the three months ended March 31, 2009 and 2008, respectively.

4 Private equity (loss) income is included in net investment income in the accompanying statements of income.

NM = Not Meaningful

Revenues for the three months ended March 31, 2009 were (\$631) million, a decrease of \$802 million from the same period in 2008. The major components of revenues include net (ceded) premium earned, net investment income (loss), net realized investment losses, and fee and other revenues.

Net (ceded) premium earned for the three months ended March 31, 2009 was (\$239) million, a decrease of \$296 million from the same period in 2008. The decrease is primarily due to ceded premium related to the homeowners quota share treaty.

Net investment income (loss) for the three months ended March 31, 2009 was \$422 million, compared to income of \$89 million in same period in 2008. The decrease is primarily the result of reduced valuations for investments in limited partnerships and limited liability companies and dividend income as a result of a change in investment strategy to reduce the total equity portfolio exposure. Partially offsetting these decreases were increases in interest income, primarily due to a higher invested asset base resulting from the Safeco and the continued investment of cash flows from operations

Net realized investment gains (losses) for the three months ended March 31, 2009 were \$18 million, compared to a loss of (\$7) million in the same period in 2008. Net gains for the three months ended March 31, 2009 reflect gains recognized from sales related to the Company's decision to reduce its exposure to the equity markets, and other gains. In addition, the Company recorded net derivative gains of \$25 million for the three months ended March 31, 2009 associated with the equity swap derivative contracts the Company entered into in August 2008 and that were terminated in January 2009. Partially offsetting these net gains were higher impairment losses on fixed maturity and equity securities deemed to be other-than-temporarily impaired.

Fee and other revenues for the three months ended March 31, 2009 were \$12 million, a decrease of \$20 million from the same period in 2008. Results in the quarter primarily reflect a decrease in oil and gas revenues due to price declines.

Claims, benefits and expenses for the three months ended March 31, 2009 were (\$16) million, a decrease of \$177 million from the same period in 2008. The decrease primarily reflects ceded losses and expenses associated with the homeowners quota share reinsurance treaty, partially offset by higher interest expense as a result of the Company's May 2008 debt offering and an increase in unfavorable variable annuity reserve development.

Pre-tax operating (loss) income for the three months ended March 31, 2009 was (\$633) million, compared to \$17 million in the same period in 2008.

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 March 31, 2009 and December 31, 2008:

\$ in Millions	As of March 31, 2009		As of December 31, 2008	
	Carrying Value	% of Total	Carrying Value	% of Total
Invested Assets by Type				
Fixed maturities, available for sale, at fair value	\$48,444	80.9%	\$47,731	79.9%
Equity securities, available for sale, at fair value	709	1.2	1,184	2.0
Trading securities, at fair value	1	-	1	-
Limited partnerships and limited liability companies	2,299	3.8	2,534	4.2
Commercial mortgage loans	1,082	1.8	1,090	1.8
Short-term investments	1,002	1.7	1,193	2.0
Other investments	149	0.2	194	0.3
Cash and cash equivalents	6,195	10.4	5,848	9.8
Total invested assets	\$59,881	100.0%	\$59,775	100.0%

Total invested assets as of March 31, 2009 were \$59.881 billion, an increase of \$106 million or 0.2% over December 31, 2008. The increase reflects investment of cash from operations and a decrease in unrealized losses primarily due to a decrease in credit spreads. Partially offsetting the increase were sales of common equity securities and a general decline in the valuations of private equity investments.

Fixed maturities as of March 31, 2009 were \$48.444 billion, an increase of \$713 million or 1.5% over December 31, 2008. The increase reflects market value increases and additional purchases of fixed income securities.

Equity securities available for sale as of March 31, 2009 were \$709 million (\$402 million common stock and \$307 million preferred stock versus \$694 million common stock and \$490 million preferred stock as of December 31, 2008), a decrease of \$475 million or 40.1% from December 31, 2008. Of the \$402 million

of common stock at March 31, 2009, \$162 million relates to securities associated with non-guaranteed unit linked products where the policyholder bears the investment risk. The decrease in total equity securities available for sale primarily reflects the execution of a program to reduce the Company's existing and acquired exposure to the common equity markets as well as a decline in the market value of both common and preferred stocks. Additionally, unrealized losses increased in the period related to a general decline in equity market indices.

Investments in limited partnerships and limited liability companies as of March 31, 2009 were \$2.299 billion, a decrease of \$235 million or 9.3% from December 31, 2008. These investments consist of traditional private equity partnerships of \$1.385 billion, other partnerships (primarily energy) of \$472 million, and real estate partnerships of \$442 million. The decrease from December 31, 2008 primarily reflects a decline in market value. 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 March 31, 2009 were \$1.082 billion (net of \$1 million of loss reserve or .09% of the outstanding loan portfolio), a decrease of \$8 million or 0.7% from December 31, 2008. The decrease reflects \$8 million in principal repayments. The entire commercial loan portfolio is U.S. based. As of March 31, 2009, the average total loan size was \$1.5 million and the average loan participation size was \$0.5 million. The number of loans in the portfolio decreased from 2,257 at December 31, 2008 to 2,256 at March 31, 2009. Approximately 90% of the loans are full or partial recourse to borrowers.

Short term investments as of March 31, 2009 were \$1.002 billion, a decrease of \$191 million or 16.0% from December 31, 2008. This decrease primarily reflects a decline in short term assets held as collateral in connection with the Company's security lending program.

Cash and cash equivalents as of March 31, 2009 were \$6.195 billion, an increase of \$347 million or 5.9% over December 31, 2008 due primarily to cash generated from operations, the previously mentioned security sales, deliberately increasing liquidity resources, and an overall reduction in investment opportunities due to lack of new issues, market illiquidity and ongoing volatility in the markets.

In January 2008, the Company adopted FASB Statement of Financial Accounting Standards No. 157, *Fair Value Measurements*, which establishes a fair value hierarchy that prioritizes inputs to valuation techniques used to measure fair value. As of March 31, 2009, excluding separate accounts and other assets, the Company reflected \$1.580 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 March 31, 2009, the Company reported \$47.661 billion as level 2, consisting primarily of various fixed maturity securities. Finally, the Company reported \$1.029 billion as level 3 (unobservable inputs) and this primarily comprised international and privately held securities for which a market price is not readily available.

As of March 31, 2009, the Company had unfunded commitments in traditional private equity partnerships, real estate partnerships, and energy and other of \$1.028 billion, \$420 million and \$476 million respectively. As of March 31, 2009, the Company had commitments to purchase various residential mortgage-backed securities at a cost of \$341 million and fair market value of \$348 million.

As of March 31, 2009, no single issuer, excluding U.S. Treasuries, agency securities and mortgage-backed securities, accounted for more than 1% of invested assets.

The gross unrealized gains and losses and fair values of available for sale investments as of March 31, 2009 and December 31, 2008 are as follows:

March 31, 2009	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. government and agency securities	\$2,093	\$224	(\$2)	\$2,315
Mortgage and asset-backed securities:				
Residential	8,642	388	(247)	8,783
Commercial	2,331	9	(258)	2,082
Other mortgage and ABS securities	1,618	69	(45)	1,642
U.S. state and municipal	14,097	337	(305)	14,129
Corporate and other	18,608	241	(1,953)	16,896
Foreign government securities	2,600	119	(122)	2,597
Total fixed maturities	49,989	1,387	(2,932)	48,444
Total equity securities	1,024	85	(400)	709
Total securities available for sale	\$51,013	\$1,472	(\$3,332)	\$49,153

December 31, 2008	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. government and agency securities	\$2,105	\$272	(\$2)	\$2,375
Mortgage and asset-backed securities:				
Residential	8,422	267	(247)	8,442
Commercial	2,229	6	(256)	1,979
Other mortgage and ABS securities	1,614	27	(62)	1,579
U.S. state and municipal	14,277	143	(702)	13,718
Corporate and other	18,637	236	(1,866)	17,007
Foreign government securities	2,618	123	(110)	2,631
Total fixed maturities	49,902	1,074	(3,245)	47,731
Total equity securities	1,279	215	(310)	1,184
Total securities available for sale	\$51,181	\$1,289	(\$3,555)	\$48,915

The following table summarizes the Company's mortgage and asset-backed fixed maturity portfolio by credit quality as of March 31, 2009:

\$ in Millions	As of March 31, 2009							
	AAA	AA	A	BBB	BB	B or Lower	Total	% of Total
Mortgage & Asset-Backed Fixed Maturities by Credit Quality								
SBA loans	\$1,232	\$-	\$-	\$-	\$-	\$-	\$1,232	9.9%
GNMA residential mortgage	1,332	-	-	-	-	-	1,332	10.7
FNMA residential mortgage	2,684	-	-	-	-	-	2,684	21.5
FHLMC residential mortgage	4,055	-	-	-	-	-	4,055	32.4
Prime residential mortgage	326	24	32	11	75	-	468	3.7
Alt-A residential mortgage	108	-	16	2	7	7	140	1.1
Sub-prime residential mortgage	76	6	5	14	-	3	104	0.8
Commercial mortgage-backed securities	1,988	77	10	7	-	-	2,082	16.6
Other asset-backed securities	289	37	46	25	7	6	410	3.3
Total	\$12,090	\$144	\$109	\$59	\$89	\$16	\$12,507	100%
% of Total	96.6%	1.2%	0.9%	0.5%	0.7%	0.1%	100%	

More than 74% of the Company's securitized portfolio is explicitly backed by the U.S. government (GNMA and SBA) or by government-sponsored entities (FHLMC and FNMA). Over 96% of these holdings remain rated AAA. The commercial mortgage-backed securities portfolio is well diversified and of high quality with 99.2% rated AA or above, approximately 20% of the underlying collateral having been defeased with U.S. Treasuries, and less than 10% of the holdings backed by 2006 to 2008 vintage transactions.

The following table summarizes the Company's allocation of fixed maturities by credit quality as of March 31, 2009 and December 31, 2008:

\$ in Millions	As of March 31, 2009		As of December 31, 2008	
	Market Value	% of Total	Market Value	% of Total
Fixed Maturities by Credit Quality¹				
AAA	\$21,626	44.6%	\$21,786	45.6%
AA+, AA, AA-	9,951	20.5	9,162	19.2
A+, A, A-	9,089	18.8	9,156	19.2
BBB+, BBB, BBB-	4,779	9.9	4,776	10.0
BB+, BB, BB-	1,891	3.9	1,575	3.3
B+, B, B-	739	1.5	897	1.9
CCC or lower	369	0.8	379	0.8
Total fixed maturities	\$48,444	100.0%	\$ 47,731	100.0%

¹For 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 93.8% at March 31, 2009 from 94.0% December 31, 2008. Overall, the average credit quality rating remains at AA-.

The Company had 6.2% of its fixed maturity securities invested in non-investment grade securities at March 31, 2009. The Company's holdings of below investment grade securities primarily consist of an actively managed diversified portfolio of high yield securities and loans within the domestic insurance portfolios and 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 March 31, 2009 and December 31, 2008:

\$ in Millions	As of March 31, 2009		As of December 31, 2008	
	Market Value	% of Total	Market Value	% of Total
Fixed Maturities by Maturity Date				
1 yr or less	\$1,561	3.2%	\$1,669	3.5%
Over 1 yr through 5 yrs	10,036	20.7	9,764	20.5
Over 5 yrs through 10 yrs	9,853	20.3	9,689	20.3
Over 10 years	14,487	30.0	14,609	30.6
Mortgage and asset-backed securities	12,507	25.8	12,000	25.1
Total fixed maturities	\$48,444	100.0%	\$47,731	100.0%

During 2009, after taking into consideration changes in investment opportunities and its view of the current and prospective business and economic environment, the Company made only minor adjustments to the average life of its investment portfolio.

Net Investment Income

The following table summarizes the Company's net investment income for the three months ended March 31, 2009 and 2008:

\$ in Millions	Three Months Ended March 31,	
	2009	2008
Net Investment Income		
Taxable interest income	\$566	\$584
Tax-exempt interest income	153	106
Dividends	9	24
Limited partnerships and limited liability companies	(373)	60
Commercial mortgage loans	17	10
Other investment income	4	2
Gross investment income	376	786
Investment expenses	(39)	(29)
Net investment income	\$337	\$757

Net investment income for the three months ended March 31, 2009 was \$337 million, a decrease of \$420 million from the same period in 2008. The decrease is primarily the result of reduced valuations for investments in limited partnerships and limited liability companies and dividend income as a result of a change in investment strategy to reduce the total equity portfolio exposure. Partially offsetting these decreases were increases in interest income, primarily due to a higher invested asset base resulting from the Safeco acquisition in the third quarter of 2008 and the continued investment of cash flows from operations.

Net Realized Investment Gains (Losses)

The following tables summarize the Company's net realized investment gains (losses) for the three months ended March 31, 2009 and 2008:

\$ in Millions	Sales & Dispositions	Impairments	Change in Derivatives Value	Total
Net Realized Gains (Losses)				
<u>Three Months Ended March 31, 2009:</u>				
Fixed maturities	(\$24)	(\$75)	\$ -	(\$99)
Common and preferred stock	78	(33)	-	45
Other	40	(5)	25	60
Total	\$94	(\$113)	\$25	\$ 6
<u>Three Months Ended March 31, 2008:</u>				
Fixed maturities	(\$4)	(\$15)	\$-	(\$19)
Common and preferred stock	5	(16)	-	(11)
Other	1	-	17	18
Total	\$2	(\$31)	\$17	(\$12)

\$ in Millions	Three Months Ended March 31,	
Components of Net Realized Gains (Losses)	2009	2008
Fixed maturities:		
Gross realized gains	\$24	\$32
Gross realized losses	(123)	(51)
Equities:		
Gross realized gains	95	16
Gross realized losses	(50)	(27)
Other:		
Gross realized gains	66	27
Gross realized losses	(6)	(9)
Total net realized gains (losses)	\$6	(\$12)

Net realized gains for the three months ended March 31, 2009 were \$6 million, compared to losses of (\$12) million in the same period in 2008. Net gains for the three months ended March 31, 2009 reflect gains recognized from sales related to the Company's decision to reduce its exposure to the equity markets, and other gains. In addition, the Company recorded net derivative gains of \$25 million for the three months ended March 31, 2009 associated with the equity swap derivative contracts the Company entered into in August 2008 and that were terminated in January 2009. Partially offsetting these net gains were higher impairment losses on fixed maturity and equity securities deemed to be other-than-temporarily impaired.

The following table summarizes the Company's impairments by issuer for the three months ended March 31, 2009:

\$ in Millions	Three Months Ended March 31, 2009				
	Fixed Maturities	Preferred Stock	Common Stock	Other	Total by Issuer
Bank of America	(\$12)	(\$7)	\$-	\$-	(\$19)
Commonwealth of Puerto Rico	(10)	-	-	-	(10)
MGM Mirage	(9)	-	-	-	(9)
Citigroup	-	(9)	-	-	(9)
International Lease Financing	-	(5)	-	-	(5)
Other	(44)	(3)	(9)	(5)	(61)
Total by Security Type	(\$75)	(\$24)	(\$9)	(\$5)	(\$113)

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 March 31, 2009:

\$ in Millions	Less Than 12 Months		Greater Than 12 Months	
	Unrealized Losses	Fair Value of Investments with Unrealized Losses	Unrealized Losses	Fair Value of Investments with Unrealized Losses
U.S. Government and agency securities	\$-	\$87	(\$2)	\$2
Mortgage and asset-backed securities				
Residential	(61)	233	(186)	367
Commercial	(110)	1,046	(148)	762
Other mortgage and ABS securities	(35)	231	(10)	68
U.S. state and municipal	(128)	2,452	(177)	1,820
Corporate and other	(658)	5,737	(1,295)	4,545
Foreign government securities	(64)	314	(58)	140
Total fixed maturities	(1,056)	10,100	(1,876)	7,704
Common stock	(42)	141	(38)	49
Preferred stock	(52)	104	(268)	177
Total equities	(94)	245	(306)	226
Total	(\$1,150)	\$10,345	(\$2,182)	\$7,930

Unrealized losses decreased from \$3.555 billion as of December 31, 2008 to \$3.332 billion as of March 31, 2009 primarily due to a decrease in credit spreads, and a planned reduction in equity holdings. Unrealized losses less than 12 months decreased from \$1.869 billion at December 31, 2008 to \$1.150 billion as of March 31, 2009 and accounted for \$719 million of the overall decrease in unrealized losses. Unrealized losses greater than 12 months increased from \$1.686 billion to \$2.182 billion at December 31, 2008 and March 31, 2009 respectively, an increase of \$496 million. Included in the \$2.182 billion of unrealized losses were \$809 million of unrealized losses on securities that had been in an unrealized loss position of 10% or greater for more than twelve months. 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 does not currently have the intent to sell these securities and has determined it is not likely that it would be required to sell these fixed income securities before they recover their fair value.

Effective January 1, 2009, the Company adopted FASB Staff Position FAS 115-2 and 124-2 “*Recognition and Presentation of Other-Than-Temporary Impairments.*” See Footnote 1 to the Unaudited Financial Statements as of and for the three months ended March 31, 2009 for details. In the first quarter of 2009, the Company recorded a cumulative effect adjustment, net of US and foreign income taxes, in the amount of \$28 million. The adjustment was an increase to policyholders’ unassigned equity and a corresponding decrease to accumulated other comprehensive income.

If the Company believes a decline in the value of a particular investment is temporary, the decline is recorded as an unrealized loss in policyholders’ equity. If the decline is believed to be “other-than-temporary,” and the Company believes it will be able to collect all cash flows due on its fixed income securities, then the carrying value of the investment is written down to fair value and a non-credit impairment loss is recorded in policyholders’ equity. If the Company believes a decline in value to be other-than-temporary and the Company will not collect all cash flows due from the fixed income security, then the carrying value is written down to the expected cash flow amount and a realized loss is recorded. As a result of this review, the Company recorded a \$75 million impairment loss related to fixed maturities in the first quarter 2009 and has concluded that the remaining gross unrealized losses of fixed maturity securities as of March 31, 2009 are temporary.

For all other investment types, 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. The gross unrealized losses recorded on equity securities at March 31, 2009 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. The Company recorded \$33 million in equity impairment losses in the first quarter 2009 that were deemed to be other-than-temporary.

LIQUIDITY AND CAPITAL RESOURCES
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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. 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 March 31, 2009 (including cash and cash equivalents) totaled \$59.881 billion.

Short-term debt outstanding at March 31, 2009 and December 31, 2008 was as follows:

\$ in Millions	As of March 31, 2009	As of December 31, 2008
Commercial paper	\$-	\$-
Revolving credit facilities	-	-
Current maturities of long-term debt	300	-
Total short-term debt	\$300	\$-

The increase in short-term debt reflects the current maturity of the 4.875% notes due 2010.

Long-term debt outstanding at March 31, 2009 and December 31, 2008 was as follows:

\$ in Millions	As of March 31, 2009	As of December 31, 2008
4.875% Notes, due 2010 ¹	\$-	\$300
7.25% Notes, due 2012 ¹	204	204
8.00% Notes, due 2013	260	260
7.86% Medium term notes, due 2013	25	25
5.75% Notes, due 2014	500	500
7.30% Notes, due 2014 ²	200	200
6.70% Notes, due 2016	250	250
7.00% Subordinated notes, due 2067 ³	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% Notes, due 2034	250	250
6.50% Notes, due 2035	500	500
7.50% Notes, due 2036	500	500
7.80% Subordinated notes, due 2087 ⁴	700	700
10.75% Subordinated notes, due 2088 ⁵	1,250	1,250
7.697% Surplus notes, due 2097	500	500
Subtotal	5,842	6,142
Unamortized discount	(53)	(53)
Total long-term debt excluding current maturities	\$5,789	\$6,089

¹ Reflects debt originally issued by Safeco. On December 29, 2008, \$281 million of the outstanding \$300 million 4.785% notes due 2010 and \$187 million of the outstanding \$204 million 7.25% notes due 2012 were exchanged for a like principal amount of newly issued Liberty Mutual Group Inc ("LMGI") notes.

² Reflects debt originally issued by Ohio Casualty. On December 29, 2008, \$180 million of the outstanding \$200 million 7.30% notes due 2014 were exchanged for a like principal amount of newly issued LMGI notes.

³ The par value call date and final fixed rate interest payment date is March 15, 2017, subject to certain requirements.

⁴ The par value call date and final fixed rate interest payment date is March 15, 2037, subject to certain requirements.

⁵ The par value call date and final fixed rate interest payment date is June 15, 2038, subject to certain requirements.

As part of its overall capital strategy, the Company may issue, repurchase or exchange debt depending on market considerations. Debt repurchases, if any, may be done through open market or other appropriate transactions.

Debt Transactions and In-force Credit Facilities

On March 11, 2009, LMIC became a member of the Federal Home Loan Bank of Boston. To date, no funds have been borrowed.

The Company places commercial paper through a \$1 billion program issued by LMGI and guaranteed by LMIC. The program is backed by two revolving credit facilities totaling \$750 million. On February 24, 2009, LMGI entered into a \$30 million unsecured revolving credit facility which terminates on July 25, 2010. On March 16, 2009, the five-year \$750 million credit facility, which also terminates on July 25, 2010, was amended to remove a lender with a \$30 million commitment in the facility. To date, no funds have been borrowed under either facility.

On December 29, 2008, the following transactions occurred:

- LMGI exchanged \$281 million of the outstanding \$300 million Safeco 4.875% Senior Notes due 2010 for a like principal amount of newly issued LMGI 4.875% Senior Notes due 2010.

- LMGI exchanged \$187 million of the outstanding \$204 million Safeco 7.25% Senior Notes due 2012 for a like principal amount of newly issued LMGI 7.25% Senior Notes due 2012.
- LMGI exchanged \$180 million of the outstanding \$200 million Ohio Casualty 7.30% Senior Notes due 2014 for a like principal amount of newly issued LMGI 7.30% Senior Notes due 2014.

Safeco and Ohio Casualty received and accepted the requisite consents to enable each to execute a supplemental indenture governing the Safeco and Ohio Casualty Senior Notes that remain outstanding. In connection with the consents, LMGI paid approximately \$5.6 million in consideration to the noteholders. These costs were capitalized and will be amortized into income over the remaining term of the respective newly issued LMGI Senior Notes. The supplemental indenture eliminated substantially all restrictive covenants and eliminated or modified certain events of default.

On September 2, 2008, LMIC entered into a \$750 million, 364 - day committed repurchase agreement facility for general corporate purposes. To date, no funds have been borrowed under the facility.

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).

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.

On June 9, 2006, Liberty Mutual Insurance Europe Limited entered into a \$20 million revolving loan facility. The facility is available to provide working capital to the Company's international operations. The revolving loan facility is guaranteed by LMIC. As of March 31, 2009, no borrowings were outstanding under the facility.

Interest Expense

Consolidated interest expense for the three months ended March 31, 2009 was \$122 million, an increase of \$39 million over the same period in 2008. The increase was principally due to the Series C Notes and debt resulting from the Safeco acquisition. As part of its overall capital strategy, the Company may issue, repurchase or exchange debt depending on market considerations. Debt repurchases, if any, may be done through open market or other appropriate transactions.

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 March 31, 2009, the Company, through its downstream subsidiary LMGI, had \$5.183 billion of debt outstanding, excluding discount.

The insurance subsidiaries' ability to pay dividends on preferred or common stock 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, 2008) and 2009 dividend capacity prior to needing regulatory approval for LMIC, LMFIC and EICOW were as follows:

\$ in Millions	RBC Ratio ¹		Dividend Capacity²
	2008	2007	2009
RBC Ratios and Dividend Capacity			
LMIC ³	402%	519%	\$1,501
LMFIC ³	501%	507%	\$97
EICOW ³	362%	516%	\$95

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, 2009, the LMIC pooling percentage decreased from 75.9% to 75.0%, the LMFIC pooling percentage increased from 10.0% to 12.9%, and the EICOW pooling percentage decreased from 10.0% to 8.0%.

NA=Not Available

As of January 1, 2009, LMGI also has access to the following sources of funding:

- A management services agreement with LMIC pursuant to which LMGI is entitled to collect certain costs plus a management fee of approximately \$50 million in 2009 for services rendered by LMGI employees.
- Liberty Corporate Services LLC ("LCS"), which through its subsidiaries, collects fees and other revenues, primarily for claims administration and agency services rendered for affiliated and non-affiliated entities. For the three months ended March 31, 2009, LCS recorded \$56 million in pre-tax income.
- Approximately \$80 million of annual dividends related to non-redeemable perpetual preferred stock issuances by LMIC and LMFIC.

Statutory Surplus

Statutory surplus as regards policyholders for the combined operations of LMIC and its U.S. affiliates including international branches was \$12.155 billion and \$12.330 billion at March 31, 2009, and December 31, 2008, respectively. The decrease in surplus primarily reflects unaffiliated and affiliated unrealized investment losses of \$569 million, partially offset by net income of \$246 million (the sum of earnings from the Company's 64 domestic insurance companies and dividends from subsidiaries) and a \$148 million decrease in non-admitted assets, primarily goodwill from recent acquisitions.

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 2008 tables to conform to the 2009 tables.

Adoption of New Accounting Standards

Effective January 1, 2009, the Company adopted Financial Accounting Standards Board ("FASB") Staff Position ("FSP") No. FAS 115-2 and 124-2, "*Recognition and Presentation of Other-Than-Temporary Impairments*" ("FSP FAS 115-2 and 124-2"). FSP FAS 115-2 and 124-2 amended the accounting for other-than-temporary impairment of debt securities, requires the establishment of a policy for determining when "credit losses" exist and provides guidance on determining the amount of impairment to be recognized in the statement of income. As a result of the adoption, the Company recognized an increase of \$28 million (net of tax) in policyholders' unassigned equity and a corresponding decrease to accumulated comprehensive loss. See Note 1 in the Unaudited Consolidated Financial Statements as of and for the three months ended March 31, 2009 for further detail.

Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standard No. 157, "*Fair Value Measurement*," ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value under accounting principles generally accepted in the United States, and enhances disclosures about fair value measurements. SFAS 157 provides guidance on how to measure fair value when required under existing accounting standards. The statement establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels ("Level 1, 2 and 3"). Level 1 inputs are observable inputs that reflect quoted prices for identical assets or liabilities in active markets the Company has the ability to access at the measurement date. Level 2 inputs are observable inputs, other than quoted prices included in Level 1, for the asset or liability. Level 3 inputs are unobservable inputs reflecting the Company's estimates of the assumptions that market participants would use in pricing the asset or liability (including assumptions about risk). Certain derivatives recorded at fair value based on the requirements of Statement of Financial Accounting Standard No. 133, "*Accounting for Derivative Instruments and Hedging Activities*," ("SFAS 133") are impacted by the application of SFAS 157. The adoption of FAS 157 did not have a material effect on the Company's results of operations,

financial position or liquidity. See Note 11 to the 2008 Audited Consolidated Financial Statements for further detail.

Effective January 1, 2008, the adopted 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 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 policyholders’ equity of \$41 million.

None of the other accounting standards adopted by the Company in the first quarter of 2009 had a material impact on the Company. See Note 1 in the Unaudited Consolidated Financial Statements as of and for the three months ended March 31, 2009 for further detail.

Future Adoption of New Accounting Standards

None of the new accounting standards that will be adopted by the Company in subsequent quarters of 2009 are expected to have a material impact on the Company. See Note 1 in the Unaudited Consolidated Financial Statements as of and for the three months ended March 31, 2009 for further details.

Unpaid Claims and Claim Adjustment Expenses

Reserves for property-casualty unpaid claims and claim adjustment expenses were \$48.842 billion and \$48.727 billion at March 31, 2009 and December 31, 2008, respectively. The increase was primarily due to business growth and current year catastrophe losses, partially offset by 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 litigation, 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 \$1.374 billion and \$1.396 billion at March 31, 2009 and December 31, 2008, respectively, net of reinsurance and including an allowance for uncollectible reinsurance.

In the third quarter of 2007, the Company completed its biennial ground-up asbestos reserve study and increased its asbestos reserves by \$90 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 \$15.452 billion and \$15.309 billion at March 31, 2009 and December 31, 2008, respectively, net of allowance for doubtful accounts. The increase is primarily due to the purchase of additional homeowners quota share protection in 2009.

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. Reinsured's credit risk with respect to any such involuntary pool or association is a function of the creditworthiness of all participants in their respective pools.

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

Approximately 95% of the Company's reinsurance recoverable balance, net of collateral held and including voluntary and involuntary pools and associations, was placed with reinsurers rated A- or better from A.M.

Best at March 31, 2009. Collateral held against outstanding gross reinsurance recoverable balances was \$5.963 billion and \$5.418 billion at March 31, 2009 and December 31, 2008, respectively.

The remaining 5% of the Company's net reinsurance recoverable balance is well diversified. No single reinsurer rated B++ or below by A.M. Best accounts for more than 2% of statutory surplus as regards policyholders. In addition, the average net reinsurance recoverable balance from individual reinsurers rated below A- or not rated by A.M. Best was approximately \$1 million as of March 31, 2009.

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 March 31, 2009, and December 31, 2008, deferred gains related to these reinsurance arrangements were \$721 million and \$725 million, respectively, and are included in other liabilities within the consolidated balance sheets. Interest credited to the funds held balances was \$29 million for the three months ended March 31, 2009, and 2008. Deferred gain amortization was \$17 million and \$16 million for the three months ended March 31, 2009, and 2008, respectively. Reinsurance recoverables related to these transactions, including experience related profit accruals, were \$2.162 billion and \$2.165 billion as of March 31, 2009, and December 31, 2008, 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, any premium and loss activity subsequent to December 31, 2001 is 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. As of December 31, 2008, \$325 million of the original \$525 million of Mystic Re matured. As no events attached to that issue, the respective collateral was released during the fourth quarter of 2008. In the first quarter of 2009, the Company entered into an agreement with Mystic Re II to provide \$225 million of additional reinsurance coverage for the Company in the event of a U.S. hurricane or earthquake event. The Company has not recorded any recoveries under these programs. Neither Mystic Re nor Mystic Re II has any other reinsurance in force.

During the first quarter of 2009, the Company entered into new property catastrophe reinsurance, replacing \$162 million of collateral with \$186 million of new collateral issued at 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 months ended March 31, 2009 were \$113 million, an increase of \$82 million over the same period in 2008. Of the \$113 million of impairments recognized for the three months ended March 31, 2009, \$33 million was recognized as non-credit impairments as required under FSP FAS 115-2.

The Company reviews fixed income and public equity securities for impairment on a quarterly basis and private equity and co-investment securities on a semi-annual basis. Securities are reviewed for both quantitative and qualitative considerations including, but not limited to: (a) the extent of the decline in fair value below book value, (b) the duration of the decline, (c) significant adverse changes in the financial condition or near term prospects of the investment or issuer, (d) significant change in the business climate or credit ratings of the issuer, (e) general market conditions and volatility, (f) industry factors, and (g) the past impairment of the security holding or the issuer. For fixed income securities where the Company does not expect to recover the entire amortized cost basis of the security, the Company will evaluate whether the other-than-temporary is a credit or a non-credit impairment based on the guidance outlined in FSP FAS 115-2. The factors considered in making an evaluation for credit versus non-credit other-than-temporary include the following: (a) failure of the issuer of the security to make scheduled interest or principal payments (including the payment structure of the debt security and the likelihood the issuer will be able to make payments that increase in the future), (b) performance indicators of the underlying assets in the security (including default and delinquency rates), (c) vintage, (d) geographic concentration, (e) industry analyst reports, sector credit ratings, and volatility of the security's fair value. In addition, the Company's accounting policy for other-than-temporary impairment recognition requires an other-than-temporary impairment charge be recorded when it is determined the security will be sold or it is more likely than not that the Company will be required to sell the security before recovery of the security's amortized cost basis (all debt securities and certain preferred equity securities) or the Company's intent and ability to hold certain equity securities for a period of time that is sufficient to allow for any anticipated recovery in market value.

Subsequent to quarter end, the Company has not recognized any additional material other-than-temporary impairments.

Variable Interest Entities

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 those 2 VIEs in its financial statements. In addition, the Company has investments in 62 VIEs for which it is not the primary beneficiary at March 31, 2009 and December 31, 2008. The Company's investments in VIEs were \$521 million and \$623 million at March 31, 2009 and December 31, 2008, respectively. The Company's maximum exposure to losses from VIEs was \$1.152 billion and \$1.267 billion as of March 31, 2009 and December 31, 2008, 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 March 31, 2009 and December 31, 2008, the Company had one

interest rate swap remaining that was acquired with the assets and liabilities of the Genesis life insurance business, with a value of approximately \$0.3 million.

Beginning in January 2008, the Company, as part of its risk management program and diversification strategy, 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 entered into a \$600 million notional equity swap agreement. For the period ending March 31, 2008 the Company incurred a \$9 million loss related to the change in value of this swap contract. The contract expires in January, 2009, however, earlier termination is allowed. The contract was terminated in December 2008 and the Company realized gains of \$187 million on this transaction. In August 2008, the Company entered into two additional equity swap agreements with a total notional amount of \$335 million. These contracts matured in January 2009 resulting in realized gains of \$25 million for the period ended March 31, 2009.

Deferred Acquisition Costs and Acquired In-force Policy Intangibles

Total deferred policy acquisition costs and acquired in-force policy intangibles were \$2.585 billion and \$2.541 billion as of March 31, 2009 and December 31, 2008, 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 Safeco that equal the fair value of in-force insurance contracts at the date of acquisition.

Goodwill

Goodwill assets were \$4.626 billion and \$4.645 billion at March 31, 2009 and December 31, 2008, respectively.

Deferred Income Taxes

The net deferred income tax asset was \$3.120 billion and \$3.166 billion as of March 31, 2009 and December 31, 2008, respectively, net of a valuation allowance of \$130 million and \$131 million, respectively. Management believes it is more likely than not that the Company's net deferred income tax asset will be realized based on the Company's ability and likelihood of generating future taxable income.

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

On October 15, 2008, the Company prevailed in its suit for refund of overpaid federal income tax for the 1990 tax year, based on the treatment of salvage and subrogation. The United States District Court, District of Massachusetts, in *Liberty Mutual Insurance Co. v. United States* and *Liberty Mutual Fire Ins. Co. v. United States*, ruled that the amount of income tax refund due and deficiency interest refund due was \$42 million and \$40 million respectively, plus statutory interest on the income tax and deficiency interest refunds until paid. The Government has filed a notice of appeal.

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 fifth largest property and casualty insurer in the U.S. based on 2008 direct written premium. The Company also ranks 86th on the Fortune 500 list of largest corporations in the United States based on 2008 revenue. As of December 31, 2008, LMG had \$104.316 billion in consolidated assets, \$94.156 billion in consolidated liabilities, and \$28.855 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 substantially all of its business through four strategic business units: 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 more than 45,000 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.