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Allstate Insurance Group
Combined Management Discussion and Analysis
For the Year Ended December 31, 2007

The Allstate Insurance Group (referred to in this document as "we", "our", "us", "Allstate", the "Group" or the "Company") consists of the Allstate Insurance Company ("AIC"), Allstate Indemnity Company ("AI"), Allstate Texas Lloyd's ("ATL"), Deerbrook Insurance Company ("DIC"), Allstate Property and Casualty Insurance Company ("APC"), Allstate County Mutual Insurance Company ("ACM"), Allstate Fire and Casualty Insurance Company ("AFCIC"), Northbrook Indemnity Company ("NIC"), Allstate North American Insurance Company ("ANAIC"), Encompass Insurance Company ("EIC"), Encompass Indemnity Company ("EI"), Encompass Independent Insurance Company ("EIIC"), Encompass Home and Auto Insurance Company ("EHAIC"), Encompass Insurance Company of America ("EICA"), Encompass Insurance Company of Massachusetts ("EICMA") and Encompass Property and Casualty Company ("EPC"). Since these insurers are part of a consolidated group that utilize 100% intercompany reinsurance agreements, regulatory approval was obtained to prepare a combined Management Discussion and Analysis ("MD&A"). Accordingly, the combined results of the aforementioned companies have been analyzed in this MD&A.

In addition to the affiliated property casualty insurers listed above, Allstate has several unconsolidated subsidiaries, the largest of which is the Allstate Life Insurance Company ("Allstate Life"). Allstate Life and its subsidiaries market a broad line of life insurance and investment products. Allstate also has several unconsolidated property casualty insurers, the two largest being Allstate New Jersey Insurance Company ("ANJ") and Allstate Floridian Insurance Company ("AFIC"). ANJ writes homeowners and auto exclusively in New Jersey, while AFIC writes only homeowners in Florida. Separate MD&A's were filed for Allstate Life, ANJ, AFIC and certain of their subsidiaries.

AIC is an Illinois domiciled insurer licensed to write property and casualty business in 49 states, the District of Columbia, and Puerto Rico and offers a broad range of personal and commercial insurance products. The Allstate Corporation (the "Corporation"), a Delaware Corporation, owns all of AIC's outstanding 42,000 shares of common stock.

Catastrophe losses are an inherent risk of the property-liability insurance industry that have contributed, and will continue to contribute, to potentially material year-to-year fluctuations in our results of operations and financial position. We define a catastrophe as an event that produces pretax losses before reinsurance in excess of $1 million and involves multiple first party policyholders, or an event that produces a number of claims in excess of a preset, per-event threshold of average claims in a specific area, occurring within a certain amount of time following the event. Catastrophes are caused by various natural events including earthquakes, volcanoes, wildfires, tornadoes, hailstorms, hurricanes, tropical storms, high winds and winter storms. We are also exposed to certain human-made catastrophic events, such as certain acts of terrorism or industrial accidents. The nature and level of catastrophes in any period cannot be predicted.

Over time we have limited our aggregate insurance exposure to catastrophe losses in certain regions of the country that are subject to high levels of natural catastrophes. Limitations include our participation in various state facilities, such as the CEA, which provides insurance for California earthquake losses; the FHCF, which provides reimbursements on certain qualifying Florida hurricane losses; and other state facilities, such as wind pools. However, the impact of these actions may be diminished by the growth in insured values, the effect of state insurance laws and regulations and by the effect of competitive considerations. In addition, in various states we are required to participate in assigned risk plans, reinsurance facilities and joint underwriting associations that provide insurance coverage to individuals or entities that otherwise are unable to purchase such coverage from private insurers. Because of our participation in these and other state facilities such as wind pools, we may be exposed to losses that surpass the capitalization of these facilities and/or to assessments from these facilities.

Actions we have taken or are considering to attain an acceptable catastrophe exposure level in our property business include:

- purchasing reinsurance or engaging in other forms of risk transfer arrangements
- limitations on new business writings
- not offering continuing coverage to some existing policyholders
- withdrawing from certain geographic markets

- changes in rates, deductibles and coverage
- changes to underwriting requirements, including limitations in coastal and adjacent counties
- discontinuing coverage for certain types of residences
- removing wind coverage from certain policies and allowing our agencies to help customers apply for wind coverage through state facilities such as wind pools

We are working for changes in the regulatory environment, including fewer restrictions on underwriting, recognizing the need for and improving appropriate risk based pricing and promoting the creation of government sponsored, privately funded solutions for large catastrophes. While the actions that we take will be primarily focused on reducing the catastrophe exposure in our property business, we also consider their impact on our ability to market our auto lines.

We consider the greatest areas of potential catastrophe losses due to hurricanes to generally be major metropolitan centers in counties along the eastern and gulf coasts of the United States. Generally, the average premium on a property policy near these coasts is greater than other areas. However, average premiums are not considered commensurate with the inherent risk of loss.

BUSINESS SEGMENTS

The Company's property-liability operations consist of two business segments: Allstate Protection and Discontinued Lines and Coverages. Allstate Protection is structured around two brands, the Allstate brand and Encompass brand. Allstate Protection is principally engaged in the sale of personal property and casualty insurance, primarily private passenger auto and homeowners insurance, to individuals in the United States and Canada. Discontinued Lines and Coverages includes results from insurance coverage that we no longer write and results for certain commercial and other businesses in run-off. These segments are consistent with the groupings of financial information that management uses to evaluate performance and to determine the allocation of resources.

In our strategy for the Allstate brand, we are seeking, through the utilization of our distribution channels, our sophisticated risk segmentation process ("Tiered Pricing") and consumer marketing, to attract and retain high lifetime value customers who will potentially provide favorable prospects for profitability over the course of their relationship with us.

We maintain a comprehensive marketing approach throughout the U.S. We have aligned agency and management compensation and the overall strategies of the Allstate brand to best serve our customers by basing certain incentives on Allstate brand profitability, PIF growth, retention, and sales of financial products. We differentiate the Allstate brand from competitors by offering a choice of products, including our innovative Allstate® Your Choice Auto ("YCA") with options such as safe driving deductibles and a safe driving bonus, Allstate® Your Choice Homeowners ("YCH") with options such as claims free bonus and greater ability to tailor insurance coverage, Allstate Blue℠, our non-standard auto product with features such as a loyalty bonus and roadside assistance coverage and Allstate Green, our new eco-friendly insurance option that offers consumers a convenient way to help the environment.

Our strategy for the Encompass brand includes enhancing pricing and product sophistication through our Tiered Pricing approach with the Encompass Edge® product, increasing distribution effectiveness and improving agency technology interfaces to support profitable growth. We are positioning the brand to expand product breadth and improve independent agency penetration by leveraging technology and service capabilities.

Tiered Pricing and underwriting are designed to enhance both our competitive position and profit potential, and produce a broader range of premiums that is more refined than the range generated by the standard/non-standard model. Tiered Pricing includes our Strategic Risk Management program, which uses a number of risk evaluation factors including, to the extent legally permissible, insurance scoring based on information that is obtained from credit reports. We continue to expand the number of tiers with successive rating program releases.

Substantially all of new and approximately 86% of renewal business written for Allstate brand auto uses Tiered Pricing. For Allstate brand homeowners, approximately 93% of new and 57% of renewal business written uses Tiered Pricing. For Allstate brand auto and homeowners business, our result indicate that over time, Tiered Pricing, has improved our mix of customers towards those who we consider high lifetime value

that generally have better retention and more favorable loss experience. Usually, standard auto customers are expected to have lower risks of loss than non-standard auto customers.

We are pursuing improvements in the overall customer experience through actions targeted to increase customer satisfaction and retention. These programs are designed around establishing customer service expectations and customer relationship building. Our claims strategy focuses on delivering fast, fair and consistent claim service while achieving loss cost management and customer satisfaction.

We continue to enhance technology to integrate our distribution channels, improve customer service, facilitate the introduction of new products and services and reduce infrastructure costs related to supporting agencies and handling claims. These actions and others are designed to optimize the effectiveness of our distribution and service channels by increasing the productivity of the Allstate brand's exclusive agencies and our direct channels.

Pricing of property products is typically intended to establish returns that we deem acceptable over a long-term period. Losses, including losses from catastrophic events and weather-related losses (such as wind, hail, lightning and freeze losses not meeting our criteria to be declared a catastrophe) are accrued on an occurrence basis within the policy period. Therefore, in any reporting period, loss experience from catastrophic events and weather-related losses may contribute to negative or positive underwriting performance relative to the expectations we incorporated into the products' pricing. Accordingly, property products are more capital intensive than other personal lines products.

The Discontinued Lines and Coverages segment includes results from insurance coverage that we no longer write and results for certain commercial and other businesses in run-off. Our exposure to asbestos, environmental and other discontinued lines claims is reported in this segment. We have assigned management of this segment to a designated group of professionals with expertise in claims handling, policy coverage interpretation, exposure identification and reinsurance collection. As part of its responsibilities, this group is also regularly engaged in policy buybacks, settlements and reinsurance assumed and ceded commutations.

FINANCIAL POSITION

Cash and invested assets

Allstate's investment strategy emphasizes safety of principal and consistent income generation, within a total return framework. This approach, which has produced competitive returns over time, is designed to ensure financial strength and stability for paying claims, while maximizing economic value and surplus growth. We employ a strategic asset allocation model, which considers the nature of the liabilities and risk tolerances, as well as the risk and return parameters of the various asset classes in which we invest. The model's recommended asset allocation, along with duration and liquidity considerations, guides our initial asset allocation. This is further adjusted based on an analysis of other potential market opportunities available. Portfolio performance is measured against benchmarks at target allocation weights.

As a result of tactical decisions, the Company may sell securities during the period in which fair value has declined below amortized cost for fixed income securities or cost for equity securities. Portfolio monitoring, which includes identifying securities that are other-than-temporarily impaired, and recognizing other-than-temporary impairment on securities in an unrealized loss position for which we do not have the intent and ability to hold until recovery, are conducted regularly.

The composition of the investment portfolio at December 31 was:

(in millions)	2007	2006
Bonds	$ 27,981	$ 28,026
Preferred stocks	612	377
Common stocks	8,021	10,116
Mortgage loans on real estate	795	648
Real estate	292	299
Cash and cash equivalents	278	66
Short-term investments	101	34
Other invested assets	1,885	1,651
Total	$ 39,965	$ 41,217

Cash and invested assets decreased 3%, or $1.3 billion, primarily due to dividends paid to the Corporation and unrealized losses on common stock caused by market conditions.

Bonds

The Group's bond portfolio consists of U.S. government bonds, municipal bonds, publically traded corporate bonds, asset-backed securities ("ABS") and mortgage-backed securities ("MBS"). Allstate generally holds its bonds to maturity, but has classified all bonds as available for sale to allow maximum flexibility in portfolio management.

Municipal bonds totaled $16.8 billion at December 31, 2007 compared to $16.8 billion at December 31, 2006. Municipal bonds, including tax-exempt and taxable securities, comprise $16.8 billion, or 60%, of the bond portfolio at December 31, 2007. The municipal bond portfolio at December 31, 2007 consisted of 4,731 issues from 1,978 issuers. The largest exposure to a single issuer was 1% of the municipal bond portfolio. Corporate entities were the ultimate obligors of 9% of the municipal bond portfolio.

Corporate bonds totaled $3.4 billion at December 31, 2007 compared to $3.3 billion at December 31, 2006. As of December 31, 2007, the portfolio also contained $1.6 billion of privately placed corporate obligations, compared with $1.5 billion at December 31, 2006. Privately placed securities primarily consist of corporate issued senior debt securities that are in unregistered form and are directly negotiated with the borrower. All privately placed corporate securities are rated by the National Association of Insurance Commissioners ("NAIC") Securities Valuation Office based on information provided to them and are also internally rated. Additionally, 25.7% of the privately placed corporate securities in our portfolio are rated by an independent rating agency.

ABS totaled $3.0 billion at December 31, 2007 compared to $3.3 billion at December 31, 2006. Credit risk is managed by monitoring the performance of the collateral. In addition, many of the securities in the ABS portfolio are credit enhanced with features such as over-collateralization, subordinated structures, reserve funds, guarantees and/or insurance. A portion of the ABS portfolio is also subject to interest rate risk since, for example, price volatility and ultimate realized yields are affected by the rate of prepayment of the underlying assets.

MBS totaled $2.6 billion at December 31, 2007 compared to $2.7 billion at December 31, 2006, of which 99.9% were investment grade in 2007. The credit risk associated with MBS is mitigated due to the fact that 62% of the portfolio consists of securities that were issued by, or have underlying collateral that is guaranteed by U.S. government agencies or U.S. government sponsored entities. The MBS portfolio is subject to interest rate risk since price volatility and the ultimate realized yield are affected by the rate of prepayment of the underlying mortgages.

At December 31, 2007, 91.3% of the consolidated bond portfolio was rated investment grade, which is defined as a security having a rating from the NAIC Securities Valuation Office of 1 or 2; a rating of Aaa, Aa, A or Baa from Moody's or a rating of AAA, AA, A or BBB from S&P, Fitch or Dominion; or a comparable internal rating if an externally provided rating is not available.

Bonds are carried at amortized cost. The fair value of bonds was $28.5 billion and $28.9 billion at December 31, 2007 and 2006, respectively. At December 31, 2007, unrealized net capital gains on the bond portfolio, which are measured as the difference between statement value and fair value, were $468 million compared to $869 million as of December 31, 2006.

The ratings of securities in the Company's portfolio are influenced by many factors, including the impact of the economic environment on individual securities. The Investment Manager closely monitors the bond portfolio for ratings changes or other declines in value that are other than temporary. Fixed income securities are placed on non-accrual status when they are in default or when the timing or receipt of principal or interest payments are in doubt. Write-downs of bonds are recorded when the decline in value is considered to be other than temporary.

Equity securities

Equity securities include common and non-redeemable preferred stocks, and investments in affiliates. The $2.1 billion decrease in common stocks was attributable to the desire to reposition invested assets based on market conditions and a decrease in subsidiaries' underlying book value.

Mortgage loans on real estate

Allstate's investment in mortgage loans increased from $648 million at December 31, 2006 to $795 million at December 31, 2007. The increase was a result of Allstate investing in 20 new commercial loans. The Company closely monitors the commercial mortgage loan portfolio on a loan-by-loan basis. Loans with an estimated collateral value less than the loan balance, as well as loans with other characteristics indicative of higher than normal credit risks, are reviewed by financial and investment management at least quarterly for purposes of establishing valuation allowances and placing loans on non-accrual status when and if necessary. The underlying collateral values are based upon either discounted property cash flow projections or a commonly used valuation method that utilizes a one-year projection of expected annual income divided by a market based expected rate of return.

Short-term investments

The short-term investment portfolio was $101 million and $34 million at December 31, 2007 and 2006, respectively. We invest available cash balances primarily in taxable short-term securities having a final maturity date or redemption date of less than one year.

Other invested assets

Allstate's other invested asset portfolio increased $234 million, or 14%, from prior year driven primarily by additional investments in limited partnerships due to favorable market conditions and low income housing tax credit property investments.

Other assets

Receivables from parent, subsidiaries and affiliates decreased $414 million mainly due to settlement of the intercompany loan with Allstate Life. Premiums and considerations decreased $109 million mainly due to a change in policyholder payment preference of premiums booked but deferred and not yet due.

Reserves for losses and loss adjustment expenses

Activity in the reserve for losses and loss adjustment expenses, on a net basis, was summarized as follows at December 31:

(in millions)	2007	2006
Balance at January 1	$ 14,346	$ 16,486
Current year	16,326	15,508
Prior years	(82)	(748)
Total incurred	16,244	14,760
Paid related to:		
Current year	10,356	9,697
Prior years	6,002	7,203
Total paid	16,358	16,900
Balance at December 31	$ 14,232	$ 14,346

Incurred losses and loss adjustment expenses attributable to insured events of prior years were $(82) million and $(748) million as a result of the reestimation of unpaid losses and loss adjustment expenses for the years ending December 31, 2007 and 2006, respectively. During 2007, incurred losses and loss adjustment expenses related to prior years were primarily composed of net decreases in auto reserves due to claim severity development that was better than expected, partially offset by increases in environmental reserves of $54 million. During 2006 incurred losses and loss adjustment expenses related to prior years also included favorable catastrophe loss reserve reestimates of $132 million net of recoveries for the 2005 and 2004 hurricanes, primarily related to lower than expected claim severity for Hurricane Katrina and $6 million related to a reduction of the expected assessment from Florida Citizens Property Insurance Corporation.

Other liabilities

Aggregate write-ins for liabilities also decreased $118 million, or 5%, primarily the result of decreased securities lending transactions due to reduced loan activity. A 43%, or $67 million, decrease in the provision for reinsurance was due to strong collections which lowered outstanding recoverables. Borrowed money decreased $53 million, or 100%, due to a change in investment strategy as borrowing was not attractive in the current market.

Capital and surplus
The following table summarizes Allstate's capital resources at the end of the last two years.

(in millions)	2007	2006
Common capital stock	$ 4	$ 4
Gross paid in and contributed surplus	2,358	2,328
Unassigned funds (surplus)	15,656	16,768
Aggregate write-ins for special surplus funds	29	41
Total surplus as regards policyholders	$ 18,047	$ 19,141

Total surplus as regards policyholders decreased 6%, or $1.1 billion. The decrease was primarily due to the combination of dividends paid to the Corporation and increased unrealized losses on common stock, partially offset by net income.

RESULTS OF OPERATIONS

(in millions)	2007	2006
Premiums earned	$ 25,063	$ 25,078
Losses incurred	13,298	11,889
Loss expenses incurred	2,946	2,870
Other underwriting expenses incurred	6,449	6,453
Total underwriting deductions	22,693	21,212
Net underwriting gain (loss)	2,370	3,866
Net investment income earned	2,636	2,535
Net realized capital gains (losses)	989	108
Net investment gain (loss)	3,625	2,643
Total other income	224	245
Net income, after dividends to policyholders but before federal and foreign income taxes	6,219	6,754
Federal and foreign income taxes incurred	1,345	1,814
Net income	$ 4,874	$ 4,940

Net underwriting gain
The decrease in underwriting gain was the result of lower favorable prior year reserve reestimates, higher catastrophe losses, increases in auto and homeowners claim frequency excluding catastrophes, higher current year claim severity and increases in the cost of catastrophe reinsurance.

The Discontinued Lines and Coverages segment generated an underwriting loss of $54 million in 2007 primarily related to a $63 million reestimate of environmental reserves and a $6 million reestimate of asbestos reserves as a result of the annual third quarter 2007 ground up reserves review, partially offset by a $46 million reduction in the reinsurance recoverable valuation allowance.

Net investment income earned
Net investment income earned increased from $2.5 billion in 2006 to $2.6 billion in 2007. The change was primarily due to higher income from limited partnership investments, affiliated common stock and higher bond portfolio balances resulting from positive cash flow from operations and investment activities, partially offset by lower portfolio yields on unaffiliated investments.

CASH FLOW AND LIQUIDITY
The following table summarizes cash flow.

(in millions)	2007	2006
Net cash from operations	$ 3,067	$ 3,277
Net cash from investments	1,651	(1,227)
Net cash from financing and miscellaneous sources	(4,439)	(1,630)
Net change in cash, cash equivalents and short-term investments	$ 279	$ 420

The Company's operations typically generate substantial positive cash flow from operations as most premiums are received in advance of the time when claim payments are made. This positive operating cash flow is expected to continue to meet the liquidity requirements of the Company. Lower operating cash flow in 2007 was mainly due to increased federal income taxes, partially offset by decreased claim payments, commissions and related expenses. Cash provided from investments increased in 2007 primarily as a result of increased proceeds from sales of securities. The change in cash flow from financing was impacted by dividends paid by AIC to the Corporation in 2007.

Financial ratings and strength
Allstate's financial strength was rated Aa2, AA and A+ by Moody's, S&P and A.M. Best, respectively, at December 31, 2007.

Risk based capital
The NAIC has a standard to help assess the solvency of insurance companies, which is referred to as risk based capital ("RBC"). The standard is based on a formula for determining each insurer's RBC and a model law specifying regulatory actions if an insurer's RBC falls below specified levels. The formula for calculating RBC takes into account asset and credit risks, but places more emphasis on underwriting factors for reserving and pricing. At December 31, 2007, the RBC for each of the insurers comprising the Group was significantly above levels that would require regulatory action.

IRIS ratios
The NAIC has also developed a set of financial relationships or tests known as the Insurance Regulatory Information System ("IRIS") to assist state regulators in monitoring the financial condition of insurance companies and identifying companies that require special attention or action by insurance regulatory authorities. The NAIC analyzes financial data provided by insurance companies using prescribed ratios, each with a defined usual range. Additional regulatory scrutiny may occur if a company's ratio results fall outside the usual range for four or more of the ratios. At December 31, 2007, AIC had one ratio result that was out of the usual range.