

NAIC Group Code 0008
NAIC Company Code 60186
Employer's ID Number 36-2554642

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

The Allstate Life Insurance Group ("Company") consists of Allstate Life Insurance Company ("ALIC"), Allstate Life Insurance Company of New York ("ALNY"), Lincoln Benefit Life Company ("LBL"), Surety Life Insurance Company ("Surety"), Charter National Life Insurance Company ("CNLIC"), Intramerica Life Insurance Company ("ILIC"), Allstate Assurance Company ("AAC") and ALIC Reinsurance Company ("ALIC Re"). Regulatory approval was received 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.

ALIC, the lead company, is a wholly-owned subsidiary of Allstate Insurance Company ("AIC") and an Illinois domiciled insurer. AIC is a wholly-owned subsidiary of The Allstate Corporation ("Corporation"). The Company is licensed to conduct business in all states, the District of Columbia, Guam, Puerto Rico and the U.S. Virgin Islands. The Company provides life insurance, retirement and investment products, and voluntary accident and health insurance to individuals and institutional customers. Its products include fixed annuities, including deferred, immediate and indexed; interest-sensitive, traditional and variable life insurance; voluntary accident and health insurance; and funding agreements backing medium-term notes ("MTNs").

Individual products are sold through multiple intermediary distribution channels, including Allstate exclusive agencies and exclusive financial specialists, independent agents (including master brokerage agencies), and financial service firms such as banks, broker-dealers, and specialized structured settlement brokers. The Company's funding agreements are sold to unaffiliated trusts that issue MTNs to institutional and individual investors.

The Company's mission is to reinvent retirement and protection of the middle market consumer. To achieve its mission and reach its financial goals, the Company's primary objectives are to deepen financial services relationships with its customers and build consumer-driven innovation capabilities and culture. The Company will continue to drive scale through non-proprietary distribution channel relationships and leverage future innovations across those channels. The Company will also enhance our operational excellence. In addition to focusing on higher return markets, products, and distribution channels, the Company will improve its financial performance through capital efficiency and enterprise risk and return management capabilities and practices.

On June 1, 2006, the Corporation, ALIC, and ALNY entered into a definitive agreement ("Agreement") with Prudential Financial, Inc. and its subsidiary, The Prudential Insurance Company of America (collectively, "Prudential"), for the sale pursuant to a combination of coinsurance and modified coinsurance reinsurance of substantially all of its variable annuity business.

The terms of the Agreement gave Prudential the right to be the exclusive provider of its variable annuity products through the Allstate proprietary agency force for three years and a non-exclusive preferred provider for the following two years. During a transition period, ALIC and ALNY will continue to issue new variable annuity contracts, accept additional deposits on existing business from existing contractholders on behalf of Prudential and, for a period of twenty-four months or less, service the reinsured business while Prudential prepares for the migration of the business onto its servicing platform. ALIC and ALNY have also agreed to continue to issue variable annuity contracts in the financial institutions channel for a period of at least thirty-three months and cede the financial results to Prudential.

FINANCIAL POSITION

Cash and invested assets

An important component of our financial results is the return on our investment portfolio. The investment portfolio is managed based upon the nature of the business and its corresponding liability structure.

Our investment strategy has historically focused on the need for risk-adjusted spread to support the underlying liabilities to achieve return on capital and profitable growth. We believe investment spread is maximized by selecting assets that perform favorably on a long-term basis and by disposing of certain assets to minimize the

effect of downgrades and defaults. We believe this strategy maintains the investment spread necessary to sustain income over time. The portfolio management approach employs a combination of recognized market, analytical and proprietary modeling, including a strategic asset allocation model, as the primary basis for the allocation of interest sensitive, illiquid and credit assets as well as for determining overall below investment grade exposure and diversification requirements. Within the ranges set by the strategic asset allocation model, tactical investment decisions are made in consideration of prevailing market conditions. We will be adding a total return framework to the management of our assets to further enhance long-term returns and leverage our active management capabilities.

In conjunction with our priority of optimizing the returns we realize for the risks we accept, we will be undertaking selected new investment strategies. We are forming an investment subsidiary to pursue investment opportunities not efficiently held within our insurance operations. The creation of this subsidiary improves our capital management by enabling higher return investment strategies. As a result of this strategy, there may be a different mix in the reporting of returns between investment income, realized capital gains and losses, unrealized capital gains and losses and higher investment expenses. Additionally, this strategy may result in increased leverage from investing activities.

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 impairment on securities in an unrealized loss position for which the Company does 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	\$ 49,748	\$ 51,513
Preferred stocks	2,458	1,796
Common stocks	101	63
Mortgage loans on real estate	8,145	7,124
Cash and cash equivalents	159	708
Short-term investments	189	31
Contract loans	772	753
Other invested assets	1,125	469
Other	592	314
Total	\$ 63,289	\$ 62,771

Total invested assets increased \$0.5 billion, or 1%, at December 31, 2007 and was primarily due to positive cash flows generated from operating activities.

Bonds

The bond portfolio consists of privately placed securities, publicly traded corporate bonds, mortgage-backed securities ("MBS"), asset-backed securities ("ABS"), tax-exempt and taxable municipal bonds, U.S. government bonds and foreign government bonds. The Company generally holds its bond portfolio to maturity, but has classified all bonds as available for sale to allow maximum flexibility in portfolio management.

At December 31, 2007, 93.6% of the consolidated bond portfolio was rated investment grade, which is defined as a security having a National Association of Insurance Commissioners ("NAIC") Securities Valuation Office rating of 1 or 2; a Moody's rating of Aaa, Aa, A, or Baa, a S&P, Fitch or Dominion rating of AAA, AA, A or BBB; an A.M. Best rating of aaa, aa, a or bbb; or a comparable internal rating if an externally provided rating is not available. There were no material changes in the invested asset mix or quality distribution from the prior year.

Bonds are carried at amortized cost. The fair value of bonds was \$50.8 billion and \$53.1 billion at December 31, 2007 and 2006, respectively. At December 31, 2007, unrealized net capital gains on the bond portfolio, which are calculated as the difference between statement value and fair value, were \$1.0 billion compared to \$1.6 billion as of December 31, 2006.

Corporate bonds totaled \$26.3 billion and \$26.5 billion at December 31, 2007 and 2006, respectively. As of December 31, 2007, the portfolio also contained \$13.5 billion of privately placed corporate obligations

compared with \$12.4 billion at December 31, 2006. The benefits of privately placed securities as compared to public securities are generally higher yields, improved cash flow predictability through pro-rata sinking funds on many bonds, and a combination of covenant and call protection features designed to better protect the holder against losses resulting from credit deterioration, reinvestment risk and fluctuations in interest rates. A potential disadvantage of privately placed securities as compared to public securities is reduced liquidity. 86.9% of the privately placed securities were rated investment grade by either the NAIC or internal ratings.

At December 31, 2007 and 2006, \$9.8 billion and \$10.5 billion, respectively, of the bond portfolio were invested in MBS. The MBS portfolio consists primarily of securities which were issued by or have underlying collateral that is guaranteed by U.S. government agencies or sponsored entities, thus minimizing credit risk. The MBS portfolio, however, is subject to interest rate risk since price volatility and ultimate realized yield are affected by the rate of repayment of the underlying mortgages. The Company attempts to limit interest rate risk on these securities by investing a portion of the portfolio in securities that provide prepayment protection. At December 31, 2007, 99.8% of the MBS portfolio was rated investment grade.

The bond portfolio also contained \$5.2 billion and \$4.9 billion of ABS at December 31, 2007 and 2006, respectively. The ABS portfolio is subject to credit and interest rate risks. Credit risk is mitigated 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 debt, reserve funds, guarantees and/or insurance. 97% of the ABS securities were rated investment grade by either the NAIC or internal ratings. Interest rate risk is similar to the risk posed by MBS, but to a lesser degree due to the nature of the underlying assets. The portfolio is primarily backed by securitized home equity, collateralized debt obligations and collateralized loan obligations.

Municipal bonds, including tax-exempt and taxable securities, totaled \$4.0 billion at December 31, 2007 compared to \$4.3 billion at December 31, 2006. 99.7% of these securities were rated investment grade at December 31, 2007.

Fixed income securities issued by the U.S. government and agencies of the U.S. government totaled \$3.9 billion at December 31, 2007 compared to \$3.7 billion at December 31, 2006. 99.9% of these securities were rated investment grade at December 31, 2007.

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 Company closely monitors its bond portfolio for rating 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.

Preferred stocks

Preferred stocks increased by \$0.7 billion to \$2.5 billion at December 31, 2007. The reclassification of hybrid securities from bonds to preferred stocks based on a new NAIC definition totaling \$0.7 billion accounted for most of the change.

Mortgage loans on real estate

Mortgage loans on real estate increased \$1.0 billion to \$8.1 billion at December 31, 2007 due to the purchase of commercial mortgages to take advantage of favorable spreads. The Company's mortgage loans are collateralized by a variety of commercial real estate property types located throughout the United States.

The Company closely monitors its 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 risk, are reviewed by management at least quarterly for purposes of establishing valuation allowances and placing loans on non-accrual status. 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 an expected rate of return.

Short-term investments

The short-term investment portfolio was \$189 million and \$31 million at December 31, 2007 and 2006, respectively. The Company invests all available cash balances primarily in taxable and tax-exempt short-term securities having a final maturity date or redemption date of less than one year.

Transfers from Separate Accounts

Separate Accounts balances decreased by \$2.1 billion, or 8%, to \$23.3 billion at December 31, 2007 due in large part to the decline in the equity market performance.

The assets of the Separate Accounts are carried at fair value. Separate Accounts liabilities represent the contractholders' claim to the related assets and are carried at the fair value of the assets. Investment income and realized capital gains and losses of the Separate Accounts accrue directly to the contractholders, and therefore, are not included in the consolidated Statement of Operations. Revenues from the Separate Accounts consist of contract maintenance and administration fees, and mortality, surrender and expense charges.

The Company issues deferred variable annuities, variable life contracts and certain guaranteed investment contracts, the assets and liabilities of which are legally segregated and recorded as assets and liabilities of the Separate Accounts. Absent any contract provision wherein the Company guarantees either a minimum return or account value upon death or annuitization, variable annuity and variable life contractholders bear the investment risk that the Separate Accounts funds may not meet their stated investment objectives. The Company's variable annuity business was sold to Prudential in 2006.

Aggregate reserve for life contracts

(in millions)	<u>2007</u>	<u>2006</u>
Fixed annuities	\$ 19,690	\$ 20,422
Interest sensitive life	8,372	7,810
Structured settlements	6,269	6,072
Indexed annuities	3,564	3,092
Annuity buy outs	1,061	1,102
Traditional	1,318	1,195
Single premium immediate annuities	659	681
Payout annuities	426	403
Other	148	161
Total	<u>\$ 41,507</u>	<u>\$ 40,938</u>

Aggregate reserves increased \$569 million to \$41.5 billion as of December 31, 2007 compared to \$40.9 billion as of December 31, 2006. Reserves for interest sensitive life increased \$562 million primarily due to an increase in account value. Indexed annuity reserves increased \$471 million due to strong sales performance. The overall increase was partially offset by a \$731 million decrease in fixed annuity reserves due to higher surrenders.

Liability for deposit-type contracts

Liability for deposit type contracts increased \$736 million to \$16.7 billion. The majority of the increase was due to credited interest payable to institutional investors for MTNs.

Transfers to Separate Accounts

Transfers to Separate Accounts was \$219 million as of December 31, 2007 compared to transfers from Separate Accounts of \$76 million at December 31, 2006. The increase of \$295 million was primarily attributed to the change in market value adjustments.

Net adjustments in assets and liabilities due to foreign exchange rates

This account balance increased 100% to \$373 million as of December 31, 2007. The increase was due to a change in reporting presentation beginning in 2007 to show the receivables and liabilities associated with swaps on MTNs separately. The receivables and liabilities were previously reported net on the liability for deposit-type contracts line. Currently, the receivables and the liabilities are reported on the aggregate write-ins for invested assets line and the net adjustments in assets and liabilities due to foreign exchange rates line, respectively.

Borrowed money

Borrowed money decreased \$142 million, or 99%, to \$1 million as of December 31, 2007. The decrease was due to the temporary suspension of the mortgage dollar roll program while the implications of proposed new guidance based on Generally Accepted Accounting Principles can be evaluated.

Capital and surplus

Capital and surplus decreased \$758 million to \$2.8 billion. In 2007, net income of \$167 million was more than offset by \$725 million of dividends paid and a \$119 million increase in the asset valuation reserve.

RESULTS OF OPERATIONS

(in millions)	<u>2007</u>	<u>2006</u>
Premiums and annuity considerations	\$ 5,249	\$ 7,027
Net investment income including IMR amortization	3,604	3,535
Commissions and expense allowances	311	439
Reserve adjustments on reinsurance ceded	(1,917)	(949)
Income from fees	76	182
Other income	19	46
Total revenue	<u>7,342</u>	<u>10,280</u>
Provision for benefits	8,868	9,473
Commissions and general insurance expenses	1,021	1,263
Insurance taxes, licenses and fees	71	75
Net transfers to or (from) Separate Accounts	(2,786)	(1,160)
Maturities and other scheduled payments	30	163
Transfer of IMR due to reinsurance agreement	-	21
Total expense	<u>7,204</u>	<u>9,835</u>
Net gain from operations before dividends to policyholders and federal income taxes	138	445
Federal and foreign income taxes incurred	<u>(52)</u>	<u>256</u>
Net gain from operations after dividends to policyholders and federal income taxes and before realized capital gains or (losses)	190	189
Realized gains or (losses), net of IMR and federal income taxes	<u>(23)</u>	<u>63</u>
Net income	<u>\$ 167</u>	<u>\$ 252</u>

Net income

Net income decreased by \$85 million to \$167 million. A substantial decrease in premiums and annuity considerations along with higher reserve adjustments on reinsurance ceded more than offset the effects of higher investment income and lower benefits.

Premiums and annuity considerations

Premiums and annuity considerations decreased \$1.8 billion, or 25%, due in large part to a decline in sales of fixed annuities, partially offset by an increase in variable annuities. Fixed annuity considerations decreased \$2.0 billion primarily driven by lower sales of the Preferred Performance, Sure Horizon and T-Link products. The Company had almost no variable annuity consideration in 2007 compared to a negative amount of \$626 million for 2006 that was attributable to the transfer of reserves to Prudential related to the initial cession.

Net investment income

Net investment income, including interest maintenance reserve ("IMR") amortization, increased \$69million, or 2%. The increase, excluding IMR amortization, was due to a higher invested assets base due to positive cash flow from operations.

Commissions and expense allowances

Commissions and expense allowances decreased \$128 million mainly due to the sale of variable annuity business to Prudential.

Reserve adjustments on reinsurance ceded

Reserve adjustments on reinsurance ceded decreased \$968 million due to an increase in the reserve adjustment on variable annuity business ceded to Prudential under modified coinsurance.

Provision for benefits

Provision for benefits decreased \$0.6 billion, or 6%, and was largely driven by surrender benefits and aggregate life reserves, partially offset by an increase in death benefits.

Surrender benefits decreased \$0.4 billion, or 8%, primarily due to the cession of the variable annuity business to Prudential, partially offset by the increases in fixed annuities and MVAA annuities.

Increase in aggregate reserves decreased \$0.3 billion, or 35%, in large part due to a decrease on fixed annuities attributable to the decrease in account value. The decrease was partially offset by an increase in the variable annuities reserves mainly due to the cession of the variable annuity business in the second quarter of 2006.

Net transfers from Separate Accounts

The transfers increased \$1.6 billion in 2007 due to higher fund transfers from Separate Accounts and premiums, partially offset by lower MVAA effect and the continuing effect of the sale of the variable annuity business to Prudential. Fund transfers from Separate Accounts increased \$1,531 million as customers moved more money to fixed funds. A decrease of \$1,273 million in transfer activity due to premiums mostly driven by the sale of variable annuity business to Prudential also contributed to the increase in the overall net transfers. The increases in the transfers were partially offset by the decrease of MVAA of \$598 million primarily attributed to reserves for VA with MVA features ceded to Prudential. The decrease in surrenders further decreased the net transfers by \$421 million.

Maturities and other scheduled payments

The decrease of \$133 million, or 82%, over the prior year was primarily due to lower scheduled distributions for guaranteed investment contracts (“GICs”). The total number of contracts along with the reserve balance continues to decrease since GICs are essentially in run-off given the Company’s current strategic product focus.

CASH FLOW AND LIQUIDITY

The following table summarizes cash flow.

(in millions)	2007	2006
Net cash from operations	\$ 2,129	\$ 2,151
Net cash from investments	(995)	(2,042)
Net cash from financing and miscellaneous sources	<u>(1,525)</u>	<u>(243)</u>
Net change in cash and short-term investments	\$ <u>(391)</u>	\$ <u>(134)</u>

The principal sources of positive cash flow from operations were premiums, investment income and net transfers from Separate Accounts. The principal uses were the payment of claims and related expenses, and commissions and operating expenses. The most significant components of the negative cash flow from financing and miscellaneous sources were dividends of \$725 million and other cash applied of \$447 million. Other cash applied was mainly comprised of a \$286 million decrease in swap collateral and a \$164 million decrease in net payable to parent, subsidiaries and affiliates.

The maturity structure of the Company’s bonds, which represent 79% of the Company’s total investments, is managed to meet the anticipated cash flow requirements of the underlying liabilities. A portion of the diversified product portfolio, primarily fixed deferred annuities and universal life insurance policies, is subject to discretionary surrender and withdrawal by customers. Management believes its assets are sufficiently liquid to meet future obligations to its life and annuity policyholders, under various interest rate scenarios.

Liquidity for life insurance companies is measured by the ability to pay contractual benefits and operating expenses, and fund investment commitments. Annuity reserves at December 31, 2007, excluding Separate Accounts, comprise 83% of total reserves in-force. Of the total annuity reserves, \$25.3 billion, or 52%, are not subject to discretionary withdrawal. The Company maintains a strong liquidity position and is well positioned to meet its policyholders’ obligations.

Financial rating and strength

At December 31, 2007, ALIC’s financial strength ratings from A.M. Best, Moody’s, and Standard & Poor’s were A+, Aa2, and AA, respectively.

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. RBC is calculated by applying factors to various asset, premium, claim, expense and reserve items. At December 31, 2007, RBC for the Company 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 that require special attention or action by insurance regulatory authorities. The NAIC analyzes financial data provided by insurance companies using prescribed ratios, each with defined usual range. Additional regulatory scrutiny may occur if a company's ratio results fall outside the usual range for four or more ratios. At December 31, 2007, ALIC had four ratios that were out of the usual range. ALIC is not currently under regulatory scrutiny based on these ratios.

OTHER

Reinsurance

The Company's reinsurance ceded on life insurance increased 4% to \$244.8 billion at December 31, 2007 from \$236.3 billion at December 31, 2006. The increase was consistent with the growth in life insurance policies in-force at the end of the year. The Company purchases reinsurance to limit aggregate and single losses on large risks, while retaining primary liability as a direct insurer for all risks ceded to reinsurers.

ALIC's domestic insurance subsidiaries are domiciled in Illinois, Nebraska, New York and South Carolina. Except for those domiciled in New York and South Carolina, ALIC has 100% intercompany reinsurance agreements in place with its domestic insurance subsidiaries.

As of December 31, 2007 and 2006, 49% and 50%, respectively, of the Company's face amount of life insurance in-force was reinsured. As of December 31, 2007 and 2006, for certain term life insurance policies, the Company ceded up to 90% of the mortality risk depending on the length of the term, policy premium guarantees and the date of policy issuance. The Company also cedes substantially all of the risk associated with variable annuity contracts and 100% of the morbidity risk on substantially all of the long-term care contracts. Beginning in July 2007, for new life insurance contracts, the Company ceded mortality risk associated with coverage in excess of \$3 million per life for contracts issued to individuals age 70 and over, and ceded the mortality risk associated with coverage in excess of \$5 million per life for most other contracts. Also beginning in July 2007, the Company increased its mortality risk retention to \$10 million per individual life for insurance policies meeting specific criteria. From October 1998 through July 2007, the Company ceded the mortality risk on new life contracts that exceed \$2 million per individual, except in 2006 for certain instances when specific criteria were met, the Company ceded the mortality risk associated with coverage in excess of \$5 million per life.

The credit worthiness of external reinsurers is continuously monitored. As of December 31, 2007, approximately 95% of ceded premiums under uncollateralized non-affiliate reinsurance treaties were ceded to parties with financial strength ratings above investment grade level, as measured by at least one of the major rating agencies. In certain cases, these ratings refer to the financial strength of the affiliated group or parent company of the reinsurer.