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**Allstate Insurance Group
 Combined Management Discussion and Analysis
 For the Year Ended December 31, 2014**

OVERVIEW

The Allstate Insurance Group (referred to as the "Group") consists of Allstate Insurance Company ("AIC"), Allstate Indemnity Company, Allstate Texas Lloyd's, Allstate Vehicle and Property Insurance Company, Allstate Property and Casualty Insurance Company, Allstate County Mutual Insurance Company, Allstate Fire and Casualty Insurance Company, Allstate Northbrook Indemnity Company, Allstate North American Insurance Company, Encompass Insurance Company, Encompass Indemnity Company, Encompass Independent Insurance Company, Encompass Home and Auto Insurance Company, Encompass Insurance Company of America, Encompass Insurance Company of Massachusetts, Encompass Property and Casualty Company, North Light Specialty Insurance Company, Esurance Insurance Company and Esurance Property and Casualty Insurance Company ("ESPC"). 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-liability insurers listed above, the Group 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. There are also several unconsolidated property and casualty insurers, the two largest being Allstate New Jersey Insurance Company ("ANJ") and Castle Key Insurance Company ("CKIC"). ANJ writes auto and homeowners exclusively in New Jersey, while CKIC writes only homeowners in Florida. The Group also has an affiliated foreign insurer, Allstate Insurance Company of Canada, which has three subsidiary insurance companies. Separate MD&As were filed for Allstate Life and certain of its subsidiaries, ANJ and CKIC.

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. Allstate Insurance Holdings, LLC ("Allstate Holdings"), a Delaware Corporation, owns all of AIC's outstanding shares of common stock and is wholly-owned by The Allstate Corporation ("Corporation").

BUSINESS SEGMENTS

The Group's Property-Liability operations consist of two reporting segments: Allstate Protection and Discontinued Lines and Coverages. Allstate Protection comprises three brands where the Group accepts underwriting risk: Allstate, Esurance and Encompass. 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 property-liability insurance coverage that the Group no longer writes 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.

The Allstate brand utilizes marketing delivered to target customers to promote the Group's strategic priorities, with messaging that communicates the value of the Group's "Good Hands[®]", the importance of having proper coverage by highlighting the comprehensive product and coverage options, and the ease of doing business with Allstate and Allstate Agencies.

The Allstate brand differentiates itself from competitors by offering a comprehensive range of innovative product options and features through a network of agencies that provide local advice and service. Product features include Allstate Your Choice Auto[®] with options such as accident forgiveness, safe driving deductible rewards and a safe driving bonus, and Allstate House and Home[®] that provides options of coverage for roof damage including graduated coverage and pricing based on roof type and age. In addition, the Group offers a Claim Satisfaction GuaranteeSM that promises a return of premium to Allstate brand auto insurance customers dissatisfied with their claims experience. The Group's Drivewise[®] program, available in 46 states and the District of Columbia as of December 31, 2014, uses an in-car device or a

mobile application to capture driving behaviors and reward customers for driving safely. The Group is also testing additional features which extend the benefits of being connected beyond auto insurance pricing. The recently introduced Star Driver[®] program encourages an ongoing conversation about safe driving through an easy-to-use application to develop teens' confidence behind the wheel. The Group will continue to focus on developing and introducing products and services that benefit today's consumers and further differentiate the Group and enhance the customer experience. The Group will deepen customer relationships through value-added customer interactions and expanding its presence in households with multiple products by providing financial protection for customer needs. In certain areas with higher risk of catastrophes, the Group offers a homeowners product from an affiliated excess and surplus lines carrier. When an Allstate product is not available, the Group may make available non-proprietary products for customers through brokering arrangements. For example, in hurricane exposed areas, Allstate agencies sell non-proprietary property insurance products to customers who prefer to use a single agent for all their insurance needs.

The Group is undergoing a focused effort to enhance effectiveness and efficiency by implementing processes and standards to elevate the level and consistency of the Group's customer experience. The Group continues to enhance technology to 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 its distribution and service channels by increasing the productivity of the Allstate brand's exclusive agencies.

Other personal lines sold under the Allstate brand include renter, condominium, landlord, boat, umbrella and manufactured home insurance policies. Commercial lines include insurance products for small business owners. Other business lines include Allstate Roadside Services that provides roadside assistance products, including Good Hands Roadside[®]; Allstate Dealer Services that provides service contracts and other products sold in conjunction with auto lending and vehicle sales transactions, and Ivantage that is a general agency for Allstate exclusive agencies.

The Group's strategy for the Esurance brand focuses on self-directed consumers. To best serve these customers, Esurance develops its technology, website and mobile capabilities to continuously improve its hassle-free purchase and claims experience and offer innovative product options and features. Esurance continues to develop additional products to complement its auto line of business and provide a more comprehensive solution to its customers. Esurance also continues to invest in geographic expansion of its products. Esurance expanded its renter product in 2014 from 16 to 19 states, motorcycle from 6 to 11 states, homeowners from 3 to 14 states and auto from 41 to 43 states. Esurance continues to focus on increasing its preferred driver mix, while raising advertising expenditures and marketing effectiveness to support growth. Esurance's DriveSense[®] program, available in 28 states as of December 31, 2014, enables participating customers to be eligible for discounts based on driving performance as measured by a device installed in the vehicle. Esurance's DriveSafe[®] program is designed to help parents coach teens on safe driving by providing customizable driving statistics and the ability to limit cell phone use while the car is in motion, all controlled by a device installed in the vehicle.

The Group's strategy for the Encompass brand centers around a highly differentiated offering which simplifies the insurance experience by packaging a product with broader coverage and higher limits into a single annual household ("package") policy with one premium, one bill, one policy deductible, one renewal date and one advisor – an independent insurance agent. It especially appeals to the approximately 35 million mass affluent households in the U.S., with their higher average premiums and preference for professional advice regarding coverage needs and risk solutions. Package policies represent over 80% of the Encompass portfolio of business, with concentrations in suburban and urban areas throughout the country. Package policies currently are not offered in Massachusetts, North Carolina and Texas. In pursuit of this strategy and to achieve its financial objectives, Encompass is seeking to diversify through new business writings in states where the risk return opportunities meet its requirements, while aggressively executing pricing, underwriting, and other actions to manage risk and ensure adequate profitability.

The Group's pricing and underwriting strategies and decisions for all of its brands are primarily designed to achieve appropriate returns along with enhancing our competitive position. Sophisticated pricing methodology allows the Group to attract and retain multiple risk segments. A combination of underwriting information, pricing and discounts are used to achieve a more competitive position. The Group's pricing uses a number of risk evaluation factors including insurance scoring, to the extent permissible by applicable law, based on information that is obtained from credit reports, and other factors. A pricing strategy involves marketplace pricing and underwriting decisions that are based on these risk evaluation models and an evaluation of competitors.

Pricing of property products is typically intended to establish returns that are deemed 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 the 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 that were incorporated into the products' pricing. The Group pursues rate increases where indicated, taking into consideration potential customer disruption, the impact on its ability to market auto lines, regulatory limitations, competitive position and profitability, using a methodology that appropriately addresses the changing costs of losses from catastrophes such as severe weather and the net cost of reinsurance.

CATASTROPHE MANAGEMENT

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 the Group's results of operations and financial position. The Group defines a "catastrophe" as an event that produces pre-tax 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 high winds, winter storms, tornadoes, hailstorms, wildfires, tropical storms, hurricanes, earthquakes and volcanoes. The Group is also exposed to man-made catastrophic events, such as certain types of terrorism or industrial accidents. The nature and level of catastrophes in any period cannot be predicted.

The Group considers the greatest areas of potential catastrophe losses due to hurricanes generally to be major metropolitan centers in counties along the eastern and gulf coasts of the United States. Usually, the average premium on a property policy near these coasts is greater than in other areas. However, average premiums are often not considered commensurate with the inherent risk of loss. In addition, in various states the Group is subject to assessments from assigned risk plans, reinsurance facilities and joint underwriting associations providing insurance for wind related property losses.

Over time the Group has limited its aggregate insurance exposure to catastrophe losses in certain regions of the country that are subject to high levels of natural catastrophes. Limitations include participation in various state facilities, such as the California Earthquake Authority, which provides insurance for California earthquake losses; and other state facilities, such as wind pools. However, the impact of these actions may be diminished by the growth in insured values, and the effect of state insurance laws and regulations. In addition, in various states the Group is 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 the Group's participation in these and other state facilities such as wind pools, it may be exposed to losses that surpass the capitalization of these facilities and to assessments from these facilities.

Property catastrophe exposure management includes purchasing reinsurance to provide coverage for known exposure to hurricanes, earthquakes, wildfires, fires following earthquakes and other catastrophes. The Group is also working to promote measures to prevent and mitigate losses and make homes and communities more resilient, including enactment of stronger building codes and effective enforcement of those codes, adoption of sensible land use policies, and development of effective and affordable methods of improving the resilience of existing structures.

The Group continues to take actions to maintain an appropriate level of exposure to catastrophic events while continuing to meet customer's needs, including the following:

- Continuing to not offer new homeowners business in certain coastal states.
- Increased capacity in the brokerage platform for customers not offered a renewal.
- Expanded the Group's excess and surplus carrier to 9 new states in 2014, bringing the total number of active states to 42.
- In Texas, wind exposure related to insured property located in wind pool eligible areas along the coast including the Galveston Islands is being ceded.
- No writing of new homeowners business in California since 2007. The Group continues to renew current policyholders.

- Tropical cyclone deductibles are in place for a large portion of coastal insured properties though contract language varies across states and companies, allowing for these higher deductibles to be triggered differently across our customer base.
- The Group has additional catastrophe exposure, beyond the property lines, for auto customers who have purchased physical damage coverage. Auto physical damage coverage generally includes coverage for flood-related loss. The Group manages this additional exposure through inclusion of auto losses in our nationwide reinsurance program (which excludes New Jersey and Florida). New Jersey auto losses are included in the Group's New Jersey reinsurance program.
- Redesigning the Group's homeowners new business offering, Allstate House and Home[®], that provides options of coverage for roof damage including graduated coverage and pricing based on roof type and age. Allstate House and Home[®] is currently available in 34 states.

The Group continues to seek appropriate returns for its risks. This may require further actions, similar to those already taken, in geographies where the Group is not getting appropriate returns. However, the Group may maintain or opportunistically increase its presence in areas where it achieves adequate returns and does not materially increase its hurricane risk.

FINANCIAL POSITION

Cash and invested assets

The Group's investment strategy emphasizes safety of principal and consistent income generation, within a total return framework. This approach, which has produced competitive returns over the long term, is designed to ensure financial strength and stability for paying claims, while maximizing economic value and surplus growth. A strategic asset allocation model is employed, 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 the Group invests. The model's recommended asset allocation, along with duration and liquidity considerations, guides the Group's initial asset allocation. This is further adjusted based on an analysis of other potential market opportunities available. Portfolio performance is measured against income targets, with absolute and relative returns a secondary consideration.

The Group has a comprehensive portfolio monitoring process to identify and evaluate each security whose carrying value may be other than temporally impaired. The Group's portfolio monitoring process includes a quarterly review of all securities to identify instances where the fair value of a security compared to its amortized cost (for bonds, including loan-backed and structured securities) or cost (for stocks) is below established thresholds. The process also includes the monitoring of other impairment indicators such as ratings, ratings downgrades and payment defaults.

The composition of the investment portfolio at December 31 was:

(in millions)	<u>2014</u>	<u>2013</u>
Bonds	\$ 26,880	\$ 25,316
Preferred stocks	81	61
Common stocks	6,898	8,349
Mortgage loans on real estate	370	429
Real estate	299	296
Cash and cash equivalents	(206)	203
Short-term investments	168	115
Other invested assets	3,264	3,770
Total	<u>\$ 37,754</u>	<u>\$ 38,539</u>

Total invested assets decreased \$785 million, or 2%, compared to prior year. Explanations for the more significant items follow.

Bonds

The Group's bond portfolio consists of publicly traded and privately placed corporate obligations, municipal bonds, asset-backed securities ("ABS"), U.S. government bonds, mortgage-backed securities ("MBS") and foreign government bonds.

At December 31, 2014, 85.6% of the consolidated bond portfolio was rated investment grade, which is defined as having a National Association of Insurance Commissioners ("NAIC") Securities Valuation Office designation of 1 or 2, a Moody's rating of Aaa, Aa, A or Baa, a rating of AAA, AA, A or BBB from

S&P, Fitch, Dominion, Kroll, Realpoint or Egan Jones, a rating of aaa, aa, a or bbb from A.M. Best, or a comparable internal rating if an externally provided rating is not available. The investment grade percentage for each individual bond category ranged from 61.2% to 100%. The most significant change in the bond portfolio mix from the prior year occurred in the corporate public bond portfolio which increased \$1.07 billion. There was no significant change in the bond portfolio quality distribution from the prior year.

Bonds with an NAIC designation 1 or 2, including loan-backed and structured securities, are reported at amortized cost. Bonds with an NAIC designation 3 through 6 are reported at the lower of amortized cost or fair value, with the difference reflected in unassigned surplus.

Publicly traded corporate bonds totaled \$12.88 billion at December 31, 2014 compared to \$11.81 billion at December 31, 2013. As of December 31, 2014, the portfolio also contained \$4.71 billion of privately placed corporate obligations, compared with \$4.00 billion at December 31, 2013. Privately placed securities primarily consist of corporate issued senior debt securities that are directly negotiated with the borrower or are in unregistered form. Privately placed corporate obligations contain structural security features such as financial covenant and call protections that provide investors greater protection against credit deterioration, reinvestment risk or fluctuations in interest rates than those typically found in publicly registered debt securities. At December 31, 2014, 61% of the privately placed securities were rated investment grade.

Municipal bonds including tax-exempt and taxable securities totaled \$3.48 billion at December 31, 2014 compared to \$4.03 billion at December 31, 2013. The municipal bond portfolio at December 31, 2014 consisted of 1,087 issues from 524 issuers. The largest exposure to a single issuer was 2% of the municipal bond portfolio. Corporate entities were the ultimate obligors of 2% of the municipal bond portfolio.

ABS totaled \$3.47 billion at December 31, 2014 compared to \$3.65 billion at December 31, 2013. Credit risk is managed by monitoring the performance of the underlying collateral. Many of the securities in the ABS portfolio have credit enhancement with features such as overcollateralization, subordinated structures, reserve funds, guarantees and/or insurance.

MBS totaled \$475 million at December 31, 2014 compared to \$568 million at December 31, 2013. The MBS portfolio is subject to interest rate risk, but unlike other fixed income securities, is additionally subject to prepayment risk from the underlying mortgages.

The fair value of all bonds was \$27.31 billion and \$25.86 billion at December 31, 2014 and 2013, respectively. At December 31, 2014, unrealized net capital gains on the bond portfolio, which are calculated as the difference between statement value and fair value, were \$428 million compared to \$541 million as of December 31, 2013.

Equity securities

Equity securities include common and non-redeemable preferred stocks, and investments in affiliates. The \$1.43 billion decrease in common and preferred stocks was due to the shift of the investment portfolio from common stocks to bonds.

Cash and cash equivalents

The \$409M decrease in cash and cash equivalents was primarily due to an increase in outstanding claim checks.

Limited partnership interests

Limited partnership interests consist of investments in private equity/debt, real estate and other funds. The limited partnership interests portfolio is diversified across a number of characteristics including fund managers, vintage years, strategies, geography (including international), and company/property types.

Reserves for losses and loss adjustment expenses

Incurred losses and loss adjustment expenses represent the sum of paid losses and reserve changes in the calendar year. This expense included net losses from catastrophes of \$1.95 billion and \$1.25 billion for the years ended December 31, 2014 and 2013, respectively. Activity in the reserve for losses and loss adjustment expenses is summarized as follows:

(in millions)	2014	2013
Balance at January 1	\$ 14,553	\$ 14,499
Incurred related to		
Current year	17,682	16,392
Prior years	(12)	28
Total incurred	<u>17,670</u>	<u>16,420</u>
Paid related to:		
Current year	11,777	10,735
Prior years	5,781	5,631
Total paid	<u>17,558</u>	<u>16,366</u>
Balance at December 31	\$ <u>14,665</u>	\$ <u>14,553</u>

Incurred losses and loss adjustment expenses attributable to insured events of prior years were \$(12) million and \$28 million as a result of the reestimation of unpaid losses and loss adjustment expenses for years ended December 31, 2014 and 2013, respectively. These changes were generally the result of ongoing analyses of recent loss development trends. Initial estimates were revised as additional information regarding claims became known.

Unsecured reinsurance recoverables

The Group has unsecured reinsurance recoverables that exceeded 3% of policyholder surplus at December 31, 2014, of \$4.42 billion, all of which is receivable from the Michigan Catastrophic Claim Association ("MCCA")

The MCCA is a mandatory insurance coverage and reinsurance indemnification mechanism for personal injury protection losses that provides indemnification for losses over a retention level that increases every other MCCA fiscal year. The MCCA operates similar to a reinsurance program and is funded by participating companies through a per vehicle annual assessment. This assessment is included in the premiums charged to the Group's customers and when collected, assessments are remitted to the MCCA. The MCCA is required to assess an amount each year sufficient to cover lifetime claims of all persons catastrophically injured in that year, its operating expenses, and adjustments for the amount for excesses or deficiencies in prior assessments. The MCCA prepares statutory-basis financial statements in conformity with accounting practices prescribed or permitted by the State of Michigan Department of Insurance and Financial Services ("MI DOI"). The MI DOI has granted the MCCA a statutory permitted practice that expires in 2016 to discount its liabilities for loss and loss adjustment expense. As of June 30, 2014, the date of its most recent annual financial report, the permitted practice reduced the MCCA's accumulated deficit by \$51.24 billion to \$411 million.

The collectibility of reinsurance recoverables is subject to uncertainty arising from a number of factors, including changes in market conditions, whether insured losses meet the qualifying conditions of the reinsurance contract and whether reinsurers, or their affiliates, have the financial capacity and willingness to make payments under the terms of a reinsurance treaty or contract. The Group also has credit risk exposure associated with the MCCA. There have been no significant uncollectible balances from the MCCA.

Capital and surplus

The following table summarizes the Group's capital position at December 31:

(in millions)	<u>2014</u>	<u>2013</u>
Common capital stock	\$ 22	\$ 22
Gross paid in and contributed surplus	3,922	5,074
Unassigned funds (surplus)	12,979	12,795
Aggregate write-ins for special surplus funds	<u>54</u>	<u>59</u>
Total surplus as regards policyholders	<u>\$ 16,977</u>	<u>\$ 17,950</u>

Total surplus as regards policyholders decreased 5%, or \$973 million, and was mainly comprised of the following items:

- \$2.47 billion - Dividends paid to Allstate Holdings in 2014 compared to 1.97 billion in 2013
- \$2.32 billion - Net income in 2014 compared to \$2.49 billion in 2013
- \$1.15 billion - Surplus paid in 2014
- \$470 million - Change in net unrealized capital gains in 2014 compared to \$595 million in 2013

RESULTS OF OPERATIONS

(in millions)	<u>2014</u>	<u>2013</u>
Premiums earned	\$ 25,976	\$ 24,736
Losses incurred	14,831	13,412
Loss expenses incurred	2,839	3,008
Other underwriting expenses incurred	<u>7,009</u>	<u>6,938</u>
Total underwriting deductions	<u>24,679</u>	<u>23,358</u>
Net underwriting gain (loss)	<u>1,297</u>	<u>1,378</u>
Net investment income earned	1,233	1,145
Net realized capital gains (losses)	<u>426</u>	<u>422</u>
Net investment gain	1,659	1,567
Total other income	<u>139</u>	<u>204</u>
Net income, after dividends to policyholders but before	3,095	3,149
Federal and foreign income taxes incurred	<u>772</u>	<u>662</u>
Net income	<u>\$ 2,323</u>	<u>\$ 2,487</u>

Net underwriting gain

The \$81 million decrease in underwriting gain was primarily due to lower underwriting income in homeowners in 2014 compared to 2013 due to increased catastrophe losses, partially offset by increased premiums earned.

Net investment gains

Net investment gain increased \$92 million, primarily due to higher net investment income. Net investment income earned increased \$88 million to \$1,233 million in 2014 from \$1,145 million in 2013, mostly as a result of increases in unaffiliated common stocks. Net realized capital gains were relatively flat year-over-year.

CASH FLOW AND LIQUIDITY

The following table summarizes cash flow.

(in millions)	2014	2013
Net cash from operations	\$ 2,169	\$ 2,604
Net cash from investments	1,153	(621)
Net cash from financing and miscellaneous sources	(3,678)	(1,793)
Net change in cash, cash equivalents and short-term investments	\$ (356)	\$ 190

The Group's operations typically generate substantial cash flows from operations as most premiums are received in advance of the time claim payments are made. Cash provided from operations decreased in 2014 as a result of a decrease in net underwriting income. Cash from investments increased in 2014 due to purchase and sale activity during the year. Negative cash flows from financing increased mainly due to increased dividends paid to the stockholder in 2014.

Financial strength ratings and outlook

The Company's most recent financial strength ratings and outlook were A+ (exceptional), Aa3 (excellent) and AA- (excellent) from A.M. Best, Moodys and Standard & Poors, respectively; all with a stable outlook.

Risk-based capital

The NAIC has a uniform capital adequacy standard, referred to as the risk-based capital ("RBC"), that serves as one of the solvency monitoring regulatory tools to measure and assess the amount of capital that is appropriate for an insurance company to support its overall business operations in consideration of its size and risk profile. The standard utilizes a formula to calculate a company's minimum capital requirement ("company action level RBC") based on the insurance, business, asset, interest rate, market, credit, underwriting and reserving risk associated with its business. There is no regulatory action required if a company maintains an actual capital level greater than the company action level RBC. A RBC model law does, however, mandate four levels of regulatory action based on a company's degree of capital impairment. At December 31, 2014, the total adjusted capital of each insurer comprising the Group was significantly above the company action level RBC.

IRIS ratios

The NAIC has also developed a set of financial relationships or tests known as the Insurance Regulatory Information System to assist state regulators in monitoring the financial condition of insurance companies and identifying companies that require special attention or action. 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 thirteen ratios. At December 31, 2014, no insurer comprising the Group had more than three ratio results outside the usual range.