To Our Stockholders

Alleghany's common stockholders' equity per share at year-end 2007 was $305.72, an increase of 15.5 percent over common stockholders' equity per share of $264.80 at year-end 2006, adjusted for stock dividends. Underwriting results were excellent at our insurance operating units, and investment performance was also strong. For the five years ended December 31, 2007, Alleghany's common stockholders' equity per share increased at a compound annual rate of 11.7 percent, compared with a compound annual rate of return of 12.8 percent for the S&P 500 over the same time period.

Alleghany's principal financial objective is to grow book value per share at double-digit rates without employing excessive amounts of financial leverage or taking undue amounts of operating risk. By consistently growing book value per share, we believe that we can better compound the value of the company and create attractive long-term returns for our shareholders. This approach stands in contrast to that of many other companies that assume significant risk in the hope of outsized returns in any one year. Although such an approach can at times produce spectacular gains, it can also produce large losses, sometimes more than offsetting these gains.

Management is aligned with Alleghany's principal financial objective in two important ways. First, we are all stockholders, and our personal balance sheets rise and fall with Alleghany's stock price. Second and more importantly, we have no management stock options. Instead, each year our senior management team is awarded performance shares, the value of which depends on both our success in growing book value per share over rolling four-year periods, as well as the stock price movement over that time frame. Management stock options, although sometimes appropriate for entrepreneurial, early-stage growth companies, are less effective in providing management with motivation to consistently compound value into the future. Instead, management stock options can result in management choosing to take outsized risks, reaping the rewards when things go right and losing nothing when they don't.

At the end of 2001, Alleghany had consolidated cash and invested assets of $1,348 million and no insurance operations. At the end of 2007, Alleghany had consolidated cash and invested assets of $4,873 million. Consolidated cash and invested assets per diluted common share have increased from $165 at the end of 2001 to $533 at the end of 2007, a compound annual growth rate of 22 percent. All of this growth has occurred without taking on any meaningful amount of debt.

In 2007, the property and casualty insurance industry had a record year of underwriting profits. In fact, looking at the industry's history, this is the first time in recent history that the industry has had two back-to-back years of underwriting profits since 1977-1978. Given this extraordinarily unusual occurrence, it should be no surprise to investors that industry competition began to increase in 2007, and by the end of 2007 insurance prices were falling, in some cases at double-digit rates. Although it is difficult for anyone to predict the future of the property and casualty insurance industry, we believe that it is likely the competition will continue to intensify in 2008.

Our insurance operating units performed well in 2007, as we enjoyed another year without any significant catastrophe losses. Additionally, the emergence of claims on certain liability insurance lines written over the past several years has been modest, allowing our subsidiaries to reduce reserves for prior years' business. The combination of these two factors resulted in very strong underwriting results for each of our insurance operating units.

RSUI produced underwriting profits of over $220 million in 2007. Although there were no significant catastrophe losses for RSUI in 2007, the company did have to increase its reserves for Hurricane Katrina, as the cost of settling the remaining outstanding claims looked to be larger than previously estimated. For the year, RSUI incurred net losses related to Hurricane Katrina of $43.2 million. These losses were partially offset by reductions in casualty reserves, particularly in professional liability and directors and officers liability, for prior accident years.

RSUI's strategy is to remain focused on providing excellent service to its wholesale brokers and their customers and to maintain prices that are sufficient to generate reasonable underwriting profits. As the market gets more competitive, it is likely that RSUI will lose some business to other markets that are either volume driven or less concerned with profitability. The objective of RSUI's management is to maximize underwriting profitability over a full cycle, which usually means writing more business when prices are high and less business when prices are low. Surprisingly, many insurance companies choose to do the opposite.

We formed RSUI in July of 2003 with a total investment of $628 million. In 2005, we contributed an additional $151 million to the company to offset the impact of Hurricane Katrina. RSUI has returned $100 million in dividends since inception, resulting in a net investment by Alleghany in RSUI of about $679 million. From July 2003 through the end of 2007, RSUI has earned $437 million after taxes, and has produced underwriting profits — after all catastrophe losses — of $460 million.

Capitol Transamerica had another solid year in 2007, producing a 16 percent increase in net premiums earned and a combined ratio of 90.2 percent. The company has significantly improved its information technology platform and continues to make progress in improving its expense efficiency. Also, Capitol Transamerica has shifted its business mix toward specialty lines and has grown its commercial surety business at attractive rates. Although competition is increasing in Capitol Transamerica's markets as well, we believe that it is positioned to continue to produce modest growth and attractive underwriting margins in 2008.

Darwin Professional Underwriters, our 55 percent-owned insurance affiliate, had an excellent year in 2007, increasing net premiums earned by 37 percent and producing underwriting profits of almost $29 million. Although Darwin's markets are increasingly competitive, the company continues to expand its presence in the specialty marketplace through new distribution relationships and new product introductions. At year-end 2007, our holdings of Darwin Professional Underwriters had a market value of $227 million, but were carried at approximately $182 million on our financial statements.

In July 2007, we acquired Employers Direct Corporation, a workers' compensation specialist based in Agoura Hills, California. The purchase price was $198 million including transaction costs. Subsequent to the acquisition, we contributed an additional $50 million to the company and it received a credit rating of A- (Excellent) from A.M. Best Company.

Employers Direct Insurance Company, the principal operating subsidiary of Employers Direct Corporation, markets workers' compensation insurance on a direct basis principally in the state of California. The direct distribution model provides the company with a number of competitive advantages, including the ability to target specific employer groups with favorable risk and pricing characteristics, a lower distribution cost structure than many of its competitors, and the ability to add value to the customer relationship through a strong claims department. We believe that Employers Direct has a very bright long-term future as part of the Alleghany group of insurance companies, although it too must navigate a highly competitive environment in 2008.

Alleghany Properties had a good year in 2007. Despite difficult real estate conditions, Alleghany Properties was able to complete several land sales that produced net earnings of $7.4 million. Recent developments in Sacramento, however, make the intermediate-term outlook extremely challenging for the company. In addition to depressed real estate conditions in California, recent developments concerning flood control designations in North Natomas, the site of the vast majority of Alleghany Properties' land, are likely to preclude any development near-term and thus limit Alleghany Properties' opportunities for land sales.

Alleghany's investment portfolio performed quite well in 2007. On a consolidated basis, our equity securities returned 19.2 percent for the year ended December 31, 2007, and for the four years ended December 31, 2007, the equity portfolio has returned 141.2 percent. Our fixed income portfolio returned 6.1 percent in 2007.

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Recent developments in the U.S. economy have made it clear that the environment of the past five years is changing. Global financial imbalances, which appear to have contributed to low U.S. interest rates, in turn have encouraged excessive consumer sector borrowing that is now in the process of retrenching. This situation has been exacerbated by stubbornly high energy costs, in turn reflecting stagnant global production since 2005 and increasing demand for oil and coal from China. Rising global energy costs have also contributed to increased food costs, both here and abroad, and in the case of China a troubling increase in the rate of inflation. At the same time, Europe, which has until recently has been economically stable, now appears to be seeing a significant slowdown, reflecting unfavorable demographics, an overvalued currency, and persistent fiscal problems. All-in-all, it looks like the robust financial markets of the early 2000s are likely to be considerably more challenging in the years ahead.

We enter this period with a balanced investment portfolio. Although we are not immune to a sell-off in equity prices, our large, high quality bond portfolio can act as a counterbalance to the cyclical exposure of our equity portfolio. Longer-term, we believe that having exposure to the equity market is an important element to the compounding of our invested asset base. Thus, we continue to look for investments in durable business franchises at reasonable prices where we see the potential for significant upside that is a multiple of the potential downside.

Over the past five years, we have avoided competing for acquisitions offered to us in an auction format, seeing that the likely winner was the company or financial investor willing to pay the highest price and employ the most financial leverage. As credit spreads widen and asset values decline, we expect that we will have more opportunities to make attractive acquisitions. We enter 2008 with well capitalized operating subsidiaries and over $800 million of invested assets outside of our regulated insurance subsidiaries.

Yours sincerely,

Weston M. Hicks
President

February 26, 2008