Baldwin & Lyons, Inc. has, since its founding in 1930, been engaged in marketing and underwriting casualty insurance. Specialty markets are served by the Company's subsidiaries.

Protective Insurance Company, with licenses in all 50 states, the District of Columbia and all Canadian provinces, provides coverage for large trucking fleets which retain substantial amounts of self-insurance, medium-sized trucking companies on a first dollar or small deductible basis and for independent contractors of such trucking companies. These trucking products are marketed primarily by the Baldwin & Lyons agency organization directly to trucking clients without broker or agent intermediaries. The agency operations also provide claims handling, loss prevention and other insurance-related services to trucking insureds. In addition, Protective accepts retrocessions from reinsurance companies, principally reinsuring against catastrophes.

Sagamore Insurance Company, licensed in 47 states, markets private passenger automobile insurance products to individuals and commercial automobile coverage to small trucking fleets.

A subsidiary is also maintained in Bermuda to provide captive insurance company benefits to trucking insureds.

Financial Highlights

	Year Ended December 31		
	2008	2007	2006
	(dollars in thousands, except per share data)		
Operating revenue[1]	**$ 204,679**	$ 203,667	$ 196,005
Revenue	**156,930**	243,763	213,069
Operating income[1]	**23,324**	29,069	27,093
Net income (loss)	**(7,713)**	55,131	38,185
Per share data - diluted:			
Operating income	**$ 1.55**	$ 1.91	$ 1.80
Net gains (losses) on investments	**(2.06)**	1.72	.74
Net income (loss)	**(0.51)**	3.63	2.54
Book value	**22.32**	24.98	23.60
Dividends paid to shareholders	**1.00**	1.65	2.55
Return on average shareholders' equity:[2]			
Operating income	**7.1%**	8.9%	8.8%
Net income (loss)	**-2.3%**	16.9%	12.4%
Combined ratio of insurance subsidiaries (GAAP basis)	**94.4%**	91.1%	92.9%

[1] Operating revenue and operating income exclude net gains or losses on investments.

[2] Average shareholders' equity excludes unrealized gains or losses on investments.

There is no need for me to tell our shareholders, investors or other readers of this report that the year 2008 was a horrible year for those whose financial fortunes depend wholly or partially from the investment of funds, and the pain continues as this letter is written in the second week of March, 2009. As a property/casualty insurance company, the funds we hold are placed in a variety of investments. Historically, we have invested a portion of our portfolio in equity securities. In 2008 equities were not the place to be invested. As a result, although our operating income was good, the company reported a net loss and a decrease in book value. I'll comment further on what happened in 2008, what is happening in 2009 as this letter is written, and how, though investment results have recently been adverse, your company remains strong, stable and a most secure investment.

At year end 2008, the company had $50.5 million in cash, cash equivalents and highly rated short term money market funds. We further had $364 million invested in a high quality, short duration bond portfolio the value of which slightly exceeded the actual cost of the portfolio. Your management has long felt that property/casualty companies should maintain highly secure, highly liquid investments in an amount that exceeds the company's claim reserves. Our cash and highly liquid bond portfolio total $415 million dollars and compares most favorably to our net claims reserves of $232 million; and our claim reserves have always proven to be more than adequate. Emphasizing our liquidity, that $415 million is easily more than all of our net liabilities of $290 million. Our total fixed income portfolio, of which 73% is invested in high rated municipals, is of a short duration of 2.3 years. We have experienced no discernable deterioration or quality concerns in any of the fixed income or money market holdings since year end. The company had and has no "exotic" type investments that have fared so poorly through these difficult financial times. We have no losses due to derivatives or other toxic holdings buried in our balance sheet. We have "marked to market" and recognized "other than temporary impairment' in our investments for years. We have very little in the way of hard to value instruments. In short, all holdings are fairly and correctly valued on the balance sheet. While we had no losses due to exotic instruments, we did have investment losses in 2008. We lost money the old fashioned way - by holding equity investments that declined in value as the entire equity market declined.

As we have discussed numerous times throughout the years, the company invests a higher percentage of its investable assets in equity securities than the average property/casualty insurance company. With the highly liquid position explained above and a non-leveraged premium to surplus ratio of less than 1 to 1, a more aggressive investment philosophy has been followed with approximately 23% of invested assets placed in equities (primarily common stocks of publicly traded companies, both domestic and foreign) through direct holdings or via the company's investment in limited partnerships. The company's direct holdings are managed by selected portfolio managers. Investments in limited partnerships, whose investments are primarily in publicly traded common stocks, provide a similar, but a more indirect method of owning equities.

Like the overwhelming majority of investors in 2008, our equity investments fared poorly. We were bruised as we were swept along with the 34% reduction in the DJIA for 2008. Those poor results were reflected in both our net income for the year and by a reduction in shareholders' equity and the company's book value. As we have before explained, accounting for the company's investment in limited partnerships is different than for the company's direct equity holdings. While gains and losses upon disposal of all securities are recognized and go through the income statement for both direct and limited partnership investments, the change in value of securities held by limited partnerships during an accounting period must also be recognized as realized gains or losses for our income statement, and therefore are included in our net income calculation. That has, and may in the future, cause significant volatility to our earnings, as happened positively in 2007 and negatively in 2008. In 2008, our limited partnership investments lost $33.6 million pre-tax both realized and unrealized as to them, but because of accounting requirements, entirely realized as to us. In our direct equity holdings, we had pre-tax realized losses of $5.2 million and a negative change in the impairment allowance, which also goes through the income statement, of $9.0 million. All of which totaled $47.7 million pre-tax or $2.06 per share after tax. Good results in operating income of $1.55 per share could not offset those investment losses, and we reported a net loss for the year of $.51 per share. We also recorded unrealized losses of $26.9 million, pre-tax, in the company's direct holdings for the year. Those did not go through the income statement but were a reduction to equity.

And we are suffering more bruising so far this year. As this is written, the DJIA has declined another 25%. Assuming our direct equity holdings and limited partnership results are similar, the company's expected operating income will not offset such a decline, and we will see a further net loss for the quarter with a further reduction in book value.

For the year 2008, the company's book value declined by $2.66 or 10.6%. In addition to the discussed investment losses, both realized and unrealized, the company's surplus declined due to dividend payments of $15.1 million ($1.00 per common share) and by $8.9 million used to repurchase 456,000 shares of the company's stock. With all purchases at less than book value, the effect of the repurchase was to increase the company's book value by 16 cents per share.

In spite of its investment losses, your company stands strong and safe. Year end bank debt stood at only $9 million at the holding company level. Those funds borrowed were used in the repurchase of treasury stock, and that debt can easily be extinguished with surplus funds available from the parent's subsidiary companies. Cash and fixed income investments handily cover net claim reserves and all other liabilities. The company's year end net worth of $330 million allows the company to most favorably compare to any accepted safe leverage ratio with a ratio of premium written to surplus of less than 1 to 1. And, keep in mind, that the book value of the company has always been fairly presented. Assets have been properly valued and liabilities properly estimated, as proven year after year. The company has a history of strong operating results that continued in 2008 with a consolidated combined ratio of 94.4%, the 8th consecutive year the company's combined ratio has been less than 100%. Your company's strength is recognized by the industry and the rating agencies. Baldwin and Lyons and its subsidiary companies were again rated A+ by A.M. Best Co. Only 24% of the country's property/casualty companies achieve a Best's A+ or better rating. The Street.Com (formerly Weiss Rating Service) rated Protective Insurance Company as an A+ company, one of only five of all the p/c companies in the country so rated. Ward's Rating Service again designated Protective Insurance Company as one of the top 50 p/c insurance companies in the U.S.

Underwriting profit and lower investment income due to declining short term yields available through the year produced operating earnings per share of $1.55 in 2008 compared to $1.91 per share in 2007. The 2008 profitable combined ratio of 94.4% was good, but was 3.3% higher than 2007's 91.1%. 2008 results were influenced by Hurricane Ike which hit the Texas coast, but continued north through the country with an unusual sustained force. We incurred significant Hurricane Ike losses in Texas, but also in other states north to Ohio, which is something not usually expected. Even with the catastrophe losses, our assumed reinsurance business performed well with a combined ratio of 81% on volume that was up year over year by 23% to $35 million. For 2009, we have increased our participation in certain programs while decreasing participation in some for which we were less optimistic. In general, catastrophe reinsurance is a part of the insurance industry that is probably an exception to the soft market conditions that have compressed margins. It is a small segment of the industry where we are actually seeing generally higher rates caused by loss experience and the somewhat limited capacity available. As we have before stated, our risk management technique is to decide on our tolerance for loss, and then to write coverage that models for various possible events to that level. Overall, we expect premium volume to increase slightly for this segment in 2009. Losses depend on whether, where and when natural disasters occur.

Total premium written and assumed for the year 2008 was up 7% over the prior year. Net premiums earned increased 2%. Besides the healthy increase in reinsurance assumed premium, the other product group contributing heavily to the overall increase in premium was our offerings to independent contractors. Expansion within existing sponsored programs by the addition of coverages to a larger number of contractors and the addition of new accounts with our IC2 product, which we discussed in last year's letter, produced an 18% increase in premiums earned. We continue to be satisfied with the performance of this product group.

All other trucking products suffered a decline in premium volume. The soft market continues both influencing pricing of existing accounts and making the addition of accounts difficult. In addition for larger customers, as rates are based on the miles driven or revenue earned by their fleets, a contraction in business activity immediately causes a reduction in the premiums we earn. That contraction occurred in 2008 and continues to date in 2009 with double digit mileage and revenue reductions seen in our accounts' recent premium reports. As no general sentiment for increasing insurance rates has yet been seen, flat to lower premium rates combined with lower business activity causes less premium from the same stable of clients. Our smaller accounts similarly suffer when economic activity declines. Here, many operators not able to secure an adequate number of loads or volume of freight to haul cease business by parking or selling their truck(s) or losing the truck(s) to the secured lender. The need for insurance then no longer exists. Our volume reflects those discontinuances of business and also heavy insurance rate competition, both causing a reduction in premiums earned.

Our personal auto product has seen volume reductions for the past few years as the marketplace changed with the non-standard auto segment blurred as more companies adopted more sophisticated and granular rating plans that allowed their writing of those risks previously designated non-standard. We too adopted a new rating system called "Scorecard" rating that made our Sagamore subsidiary more of an auto writer as opposed to a non-standard auto writer. With "Scorecard" rating and perhaps some change in competitive conditions caused by small industry increases in rates, we began to see modest volume improvements in the latter half of 2008. Those hopeful signs continue to date. The personal auto product differs from other company offerings in that it requires many more touches per dollar of premium. As a result, non-variable expenses consume a higher portion of the premium dollar, especially as volume is reduced. But the opposite is also true, and as volume expands underwriting expenses do not expand by the same percentage allowing margins to improve. That principal fosters optimism for seeing improved results from this part of our business.

Towards the end of 2008, we completed the acquisition of a smaller independent insurance agency. The agency, a trucking specialist, writes about $20 million in trucking insurance. Much of that is independent contractor coverage. This purchase fits into one of our long range strategic options of buying agencies with books of business, some of which might ultimately be moved to our subsidiary companies. This is the first such purchase, and while a small acquisition, it should aid us in determining the feasibility of future, similar purchases. It is too soon with only a few months of ownership to yet gauge success or the concept's viability.

Last year we advised we had expanded our transportation writings to include public transportation risks (primarily buses.) That expansion has gone according to plan with many new risks added. It seems that a service oriented company such as ours has been well received by this new (to us) sector of the transportation business aiding us in writing new accounts. As our marketing efforts continue and as our reputation spreads, we foresee more possible expansion.

We continue working on new ventures and possible combinations or acquisitions. If and as deals come to fruition, we will report throughout the year.

I'll conclude this letter by observing that in the past year we have seen chaos in the financial services industry that we could never have imagined. One of our biggest competitors now exists on government handouts – a situation where we as a taxpayer are subsidizing the low prices with which we must compete. Previously mighty financial firms are at death's door propped up by the government's apparently unending support. We observe in wonderment never before believing that such could happen. That such respected firms could be brought down by wholly improper assessments of the risks they undertook is astonishing. Assessing risk is our business. It was also their business and they obviously did it very wrong. I assure the reader that we have not assessed the risks we take in any such improper manner. We do not do the unfamiliar or the exotic. Our past assessment of risks has consistently produced operating results that are superior. Future operating results will fluctuate based on loss frequency and severity, especially in the catastrophe insurance we write and also due to market softness or competitiveness, but history will indicate that shareholders have not seen big disappointments or surprises. This past year, continuing to date, we suffered bad investment results, as did many, wiping out much of the benefit of the good investment results we enjoyed in prior years. However, you can be assured the company's Balance Sheet is accurately presented and allows the conclusion that Baldwin and Lyons, Inc. is a strong, safe and secure company.

So while we are less than optimistic about the country's near term economic recovery and wonder about the severity and fallout of the continuing difficulties seen in the financial services industry, we are optimistic that your company will give a good account of itself. We are equipped financially and operationally to take advantage of the future as it unfolds.

With Joe DeVito, our President and Chief Operating Officer joining me, we both thank our employees for performing very well in a difficult year adding to our strengths as we look to the future. To our shareholders, we thank you for your support. We will strive not to disappoint.

Gary W. Miller
Chairman & CEO

Selected Financial Data

	Year Ended December 31				
	2008	2007	2006	2005	2004
	(Dollars in thousands, except per share data)				
Direct and assumed premiums written	**$ 221,942**	$ 207,367	$ 197,064	$ 222,445	$ 247,099
Net premiums earned	**182,299**	179,065	169,766	186,165	172,145
Net investment income	**17,063**	19,595	19,548	14,840	12,287
Net gains (losses) on investments	**(47,749)**	40,096	17,064	22,981	9,770
Losses and loss expenses incurred	**115,752**	107,781	112,604	140,622[5]	126,298
Net income (loss)	**(7,713)**	55,131	38,185	34,223	30,306
Earnings per share -- net income (loss)[1]	**(.51)**	3.63	2.54	2.30	2.05
Cash dividends per share[2]	**1.00**	1.65	2.55	.95	2.05
Investment portfolio[3]	**545,491**	650,538	626,753	622,920	577,428
Total assets	**777,743**	842,833	853,719	862,081	866,914
Shareholders' equity	**330,067**	380,718	357,627	346,685	326,548
Cost of treasury shares purchased	**8,908**	—	401	—	—
Book value per share[1]	**22.32**	24.98	23.60	23.31	22.04
Underwriting ratios[4]					
Losses and loss expenses	**63.5%**	60.2%	66.3%	75.5%	73.4%
Underwriting expenses	**30.9%**	30.9%	26.6%	22.0%	24.0%
Combined	**94.4%**	91.1%	92.9%	97.5%	97.4%

[1] Earnings and book value per share are adjusted for the dilutive effect of stock options outstanding.

[2] Includes extra dividends of $0, $.65, $1.70, $.55, and $1.65 per share for 2008, 2007, 2006, 2005 and 2004, respectively.

[3] Includes money market instruments classified with cash in the Consolidated Balance Sheets.

[4] Data is for all coverages combined, does not include fee income and is presented based upon generally accepted accounting principles.

[5] Includes $17,595 relating to Hurricanes Katrina, Rita and Wilma.

Liquidity and Capital Resources

The primary sources of the Company's liquidity are (1) funds generated from insurance operations including net investment income, (2) proceeds from the sale of investments and (3) proceeds from maturing investments. The Company generally experiences positive cash flow from operations resulting from the fact that premiums are collected on insurance policies in advance of the disbursement of funds in payment of claims. Operating costs of the insurance subsidiaries, other than loss and loss expense payments, generally average less than 30% of premiums earned on a consolidated basis and the remaining amount is available for investment for varying periods of time depending on the type of insurance coverage provided. Because losses are often settled in periods subsequent to when they are incurred, operating cash flows may, at times, turn negative as loss settlements on claim reserves established in prior years exceed net premium revenue and receipts of investment income. During 2008, negative cash flow from operations totaled $3.5 million compared to a positive $27.3 million in 2007. This comparative decrease in operating cash flow resulted from increases in loss settlements of $24 million and increases in ceded premiums reflecting changes in reinsurance treaties.

For several years, the Company's investment philosophy has emphasized the purchase of short-term bonds with maximum quality and liquidity. As interest rates and yield curves have not provided a strong incentive to lengthen maturities in recent years, the Company has continued to maintain its fixed maturity portfolio at very conservative levels. The average contractual life of the Company's bond and short-term investment portfolio decreased from 3.7 to 3.0 years during 2008. The average duration of the Company's fixed maturity portfolio is shorter than the contractual maturity average and much shorter than the duration of the Company's liabilities. The Company also remains an active participant in the equity securities market using capital which is in excess of amounts considered necessary to fund current operations. The long-term horizon for the Company's equity investments allows it to invest in positions where ultimate value, and not short-term market fluctuation, is the primary focus. Investments made by the Company's domestic insurance subsidiaries are regulated by guidelines promulgated by the National Association of Insurance Commissioners which are designed to provide protection for both policyholders and shareholders.

The Company's assets at December 31, 2008 included $58.1 million in short-term and cash equivalent investments which are readily convertible to cash without market penalty and an additional $128.1 million of fixed maturity investments (at par) maturing in less than one year. The Company believes that these liquid investments, plus the expected cash flow from current operations, are more than sufficient to provide for projected claim payments and operating cost demands. In the event competitive conditions produce inadequate premium rates and the Company chooses to further restrict volume, the liquidity of its investment portfolio would permit management to continue to pay claims as settlements are reached without requiring the disposal of investments at a loss, regardless of interest rates in effect at the time. In addition, the Company's reinsurance program is structured to avoid serious cash drains that accompany large losses.

Net premiums written by the Company's U.S. insurance subsidiaries for 2008 equaled approximately 41% of the combined statutory surplus of these subsidiaries. Premium writings of 100% to 200% of surplus are generally considered acceptable by regulatory authorities. Further, the statutory capital of each of the insurance subsidiaries substantially exceeds minimum risk based capital requirements set by the National Association of Insurance Commissioners. Accordingly, the Company has the ability to significantly increase its business without seeking additional capital to meet regulatory guidelines.

As more fully discussed in Note R to the consolidated financial statements, at December 31, 2008, $86.7 million, or 26% of shareholders' equity, represented net assets of the Company's insurance subsidiaries which, at that time, could not be transferred in the form of dividends, loans or advances to the parent company because of minimum statutory capital requirements. However, management believes that these restrictions pose no material liquidity concerns for the Company. The financial strength and stability of the subsidiaries permit ready access by the parent company to short-term and long-term sources of credit. The Company maintains a $20 million unsecured line of credit and has $9.0 million of drawings outstanding on this line at December 31, 2008, the proceeds of which were used to purchase treasury stock.

Results of Operations

2008 Compared to 2007

Direct premiums written for 2008 totaled $182.8 million, an increase of $6.6 million (4%) from 2007. The increase is primarily attributable to an increase in the Company's fleet transportation business of $8.3 million (6%). The higher premium volume from the fleet transportation program resulted from the addition of contractors by existing accounts and from modifications to the program whereby workers' compensation coverages were offered to employees of the independent contractors. This increase was partially offset by a decrease in the Company's private passenger automobile program of $3.1 million (13.0%) due to ongoing rate competition and the resultant loss of business.

Premiums assumed from other insurers and reinsurers totaled $39.1 million during 2008, an increase of $8.0 million (26%) from 2007. The property reinsurance increase resulted from increased premiums generated by most of the Company's programs reflecting increased exposure and, to a lesser extent, higher premium rates. As was the case in 2007, slightly less than half of the net premium volume for this segment is produced through an exclusive marketing arrangement for property catastrophe business produced by Paladin Catastrophe Management, a non-affiliated firm which focuses on soliciting coverage from insurance companies with risks throughout the U.S. Midwest and limited coastal regions excluding Florida and California as well as Canadian exposures. This business complements other property reinsurance by Protective in different geographic regions. Premium volume from property reinsurance will often fluctuate depending on the favorability of pricing for the coverages provided. Further, premium volume for this segment is limited by the Company's self-imposed limitation to loss from a single catastrophic event.

Premiums ceded to reinsurers on direct business increased $6.8 million (21%) during 2008 to $39.8 million as the consolidated percentage of premiums ceded to direct premiums written increased to 21.8% for 2008 from 18.7% for 2007. This increase is reflective of the Company's decreased retention under reinsurance treaties effective June, 2007, and June, 2008, covering fleet transportation risks, resulting in a higher percentage of the direct premiums ceded to reinsurers.

After giving effect to changes in unearned premiums, net premiums earned increased 2% to $182.3 million for 2008 from $179.1 million for 2007. Net premiums earned from fleet transportation insurance products increased by $2.7 million (2%). Additionally, net premiums earned from property reinsurance increased by $6.7 million (23%). Net premiums earned from the Company's private passenger automobile product decreased by $7.2 million (25%).

Pre-tax investment income of $17.1 million reflects a decrease during 2008 compared to 2007 as pre-tax yields were down 12% on average reflecting worldwide lower available rates, principally on short-term investments. After tax investment income decreased by 8% during 2008, compared to the prior year, and is lower than the pre-tax change due to the utilization of municipal bonds at a higher level during 2008.

Net losses on investments, before taxes, totaled $47.7 million in 2008 compared to a net gain on investments of $40.1 million last year. These totals include gains and losses from both direct securities trading and investments in limited partnerships. The losses in 2008 are attributable to $11.9 million in fixed maturity and equity security net direct trading losses, $33.6 million in limited partnerships net losses and $2.2 in derivative security net losses. Limited partnership ventures utilized by the Company are primarily engaged in the trading of public and private securities, including foreign securities and small venture capital activities and, to a lesser extent, real estate development. The estimated market value of limited partnership ventures investments was

$59.9 million at December 31, 2008 compared to a cost basis of $47.0 million. The aggregate of the Company's share of earnings in these entities represented a loss of 43% for 2008 versus a positive return of over 40% for 2007. The Company follows the equity method of accounting for its investments in limited partnerships. To the extent that accounting rules require the limited partnerships to include realized and unrealized gains or losses in their net income, the Company's proportionate share of net income will include unrealized as well as realized gains or losses. The current year limited partnership total is composed of estimated realized gains of $3.4 million and estimated unrealized losses of $37.0 million, as reported to the Company by the general partners. Inception to date unrealized losses included in the December 31, 2008 asset valuation total $6.9 million. Adjustments attributable to "other-than-temporary impairment," of $9.0 million during 2008 are reflected in fixed maturity and equity security net losses as stated above. Further explanation of "other-than-temporary impairment" can be found in Note B to the consolidated financial statements.

Losses and loss expenses incurred during 2008 increased $8.0 million (7%) to $115.8 million. The increase in losses incurred is due to increased current year loss activity, including $5.5 million in losses attributable to hurricanes, and lower savings on prior accident year losses, primarily from property reinsurance. Partially offsetting increases in loss and loss expenses was a $5.5 million decrease in losses from the Company's private passenger automobile product corresponding to the decline in premium volume for that product. The 2008 consolidated loss and loss expense ratio was 63.5% compared to 60.2% for 2007. The Company's loss and loss expense ratios for major product lines are summarized in the following table.

Loss and loss expense ratios:

	2008	2007
Fleet transportation	**63.6%**	58.4%
Private passenger automobile	**64.5**	67.7
Property reinsurance	**63.7**	60.8
All lines	**63.5**	60.2

The fleet transportation loss ratio for 2008 was adversely impacted by increases in reported loss amounts on a handful of severe claims. Also, the loss ratio for the independent contractor product is higher in 2008 as a significant number of insured contractors altered their business structure and therefore transitioned from accident and health to workers' compensation coverage. Factors such as fluctuations in premium volume, the levels of self-insured retentions and the Company's higher net retention under reinsurance treaties in recent years allow for more volatility in losses. The decrease in the private passenger automobile loss ratio is due primarily to increased savings on prior years' losses. The property reinsurance loss ratio was higher in 2008 as the result of hurricane losses, principally Hurricane Ike, which added almost 16 points to the loss ratio for this segment for the year end more than offset a decline in the unusually large amount of tornado and hail losses experienced during 2007.

The Company produced an overall savings on the handling of prior year claims during 2008 of $17.1 million. This net savings is included in the computation of loss ratios shown in the previous table, as is the $21.3 million savings produced during 2007 on prior year claims. This savings was distributed among all of the Company's products, with the majority attributable to the Company's large fleet transportation business, and is generally consistent with recent prior years before consideration of savings related to retrospectively-rated contracts. Because of the high limits provided by the Company to its fleet transportation insureds, the length of time necessary to settle larger, more complex claims and the volatility of the fleet transportation liability insurance business, the Company believes it is important to take a conservative posture in its reserving process. As claims are settled in years subsequent to their occurrence, the Company's claim handling process has, historically, tended to produce savings from the reserves provided. Changes in both gross premium volumes and the Company's reinsurance structure for its fleet transportation business can have a significant impact on future loss developments and, as a result, loss and loss expense ratios and prior year reserve development may not be consistent year to year.

Other operating expenses for 2008, before credits for allowances from reinsurers, increased $3.4 million (6%) to $61.7 million. This increase is due primarily to a $2.4 million increase in commission expense and an

$.8 million investment in new product development. The higher commissions reflect expansion of the Company's distribution channels to include non-affiliated agents. It should be noted that much of the Company's expense structure is fixed, that is, expenses do not vary directly with revenue, as revenue consists principally of net premiums earned by the insurance subsidiaries. In general, only commissions to non-affiliated agents, premium taxes and other acquisition costs vary directly with premium volume and each of these factors is considered in the pricing of insurance products.

Reinsurance ceded credits were $1.2 million (62%) higher in 2008, resulting from the Company ceding a higher percentage of the gross premium to other companies under reinsurance treaties. After consideration of these expense offsets, operating expenses increased $2.2 million, or 4% from the prior year.

A portion of the Company's fleet transportation business is produced by direct sales efforts of Baldwin & Lyons, Inc. employees and, accordingly, this business does not incur commission expense on a consolidated basis. Instead, the expenses of the agency operations, including salaries and bonuses of salesmen, travel expenses, etc. are included in operating expenses. In general, commissions paid by the insurance subsidiaries to the parent company exceed related acquisition costs incurred in the production of the property and casualty insurance business. The ratio of net operating expenses of the insurance subsidiaries to net premiums earned was 30.9% during 2008, level with the prior year. Including the agency operations, and after elimination of inter-company commissions, the ratio of operating expenses to operating revenue (defined as total revenue less gains (losses) on investments) was 28.6% for 2008 compared with 27.7% for 2007.

The effective federal tax rate on the consolidated loss for 2008 was a benefit of 60.8%. The effective rate differs from the normal statutory rate as a result of tax-exempt investment income.

As a result of the factors mentioned above, and primarily the change in net gains and losses on investments, the Company experienced a net loss for 2008 of $7.7 million compared to net income of $55.1 million for 2007. Diluted earnings per share were a loss of $(.51) in 2008 compared to income of $3.63 in 2007. Earnings per share from operations, defined as income before gains or losses on investments, were $1.55 compared to $1.91 in 2007.

2007 Compared to 2006

Direct premiums written for 2007 totaled $176.1 million, a decrease of $8.0 million (4%) from 2006. This decrease is primarily attributable to a decrease in the Company's private passenger automobile business of $10.4 million (31%), partially offset by an increase in the Company's fleet transportation business of $1.4 million (1%) The overall net decrease in direct premiums written volume was a result of ongoing rate competition and the resultant loss of business.

Premiums assumed from other insurers and reinsurers totaled $26.4 million during 2007, an increase of $13.5 million (105%) from 2006. The property reinsurance increase resulted primarily from new business generated by the Company's affiliation with Paladin Catastrophe Management. Protective is the exclusive market for property catastrophe business produced by Paladin which focused on soliciting coverage from insurance companies with risks throughout the U.S. Midwest and limited coastal regions excluding Florida and California in 2007.

Premiums ceded to reinsurers on direct business increased $8.1 million (32.8%) during 2007 to $33.0 million as the consolidated percentage of premiums ceded to direct premiums written increased to 19% for 2007 from 14% for 2006. This increase is reflective of the Company's decreased retention under reinsurance treaties effective June 2007 covering large fleet transportation risks, resulting in a higher percentage of the direct premiums ceded to reinsurers.

After giving effect to changes in unearned premiums, net premiums earned increased 5% to $179.1 million for 2007 from $169.8 million for 2006. Net premiums earned from all fleet transportation products increased by $1.8 million (2%). Additionally, net premiums earned from non-affiliated property reinsurance increased by

$13.4 million (102%). Net premiums earned from the Company's private passenger automobile decreased by $6.8 million (19%).

Pre-tax investment income of $19.6 million was essentially flat during 2007 compared to 2006 as pre-tax yields were up 4% on average and were largely offset by a 3% decrease in average invested assets. Average invested assets decreased primarily due to the payment of over $25 million in cash dividends to shareholders during the year partially offset by increased cash flow from operations. After tax investment income increased by 7% during 2007, compared to the prior year. The after-tax investment income yield increased by 10% from 2006 reflecting a significantly higher proportion of the Company's bond portfolio allocated to municipal bonds in 2007.

Net gains on investments totaled $40.1 million in 2007 compared to $17.1 million last year. These totals include gains from both direct securities trading and investments in limited partnerships. The gains in 2007 are attributable to $16.8 million in equity security net gains, $23.2 million in limited partnerships net gains and $.1 in debt security net gains. During 2007, the Company disposed of numerous equity securities primarily to provide funds for a new investment program initiated after year end which will be managed by a consolidated entity in 2008. The Company's investments in limited partnership ventures, consists primarily of securities trading which include foreign securities and small venture capital activities and, to a lesser extent, real estate development. The estimated market value of limited partnership ventures investments was $80.9 million at December 31, 2007 and the aggregate of the Company's share of earnings in these entities represented a return of over 40% for 2007 and 25% for 2006. The Company follows the equity method of accounting for its investments in limited partnerships. To the extent that the limited partnerships include realized and unrealized gains or losses in their net income, the Company's proportionate share of net income will include unrealized as well as realized gains or losses. The current year limited partnership total is composed of estimated realized income of $7.9 million and estimated unrealized income of $15.3 million, as reported to the Company by the general partners. Inception to date unrealized gains included in the December 31, 2007 asset valuation total $30.4 million. The final component of investment gains, consisting of adjustments attributable to "other-than-temporary impairment," was not significant during 2007 or 2006 and is more fully explained in Note B to the consolidated financial statements.

Losses and loss expenses incurred during 2007 decreased $4.8 million (4%) to $107.8 million. The decrease in losses incurred is due to increased savings on prior accident year losses, primarily from fleet transportation and property reinsurance, continued low frequency of large trucking claims, and premium volume declines in the Company's private passenger automobile product. These decreases were largely offset by $12.2 million in losses from the Company's expansion of its property catastrophe business during 2007. The 2007 consolidated loss and loss expense ratio was 60.2% compared to 66.3% for 2006. The Company's loss and loss expense ratios for individual product lines are summarized in the following table.

Loss and loss expense ratios:	**2007**	2006
Fleet transportation	**58.4%**	70.5%
Private passenger automobile	**67.7**	64.8
Property reinsurance	**60.8**	35.9
All lines	**60.2**	66.3

The fleet transportation loss ratio for 2007 was favorably impacted by an increase in savings on prior year losses and a continued low frequency of extremely severe accidents. Factors such as fluctuations in premium volume, the levels of self-insured retentions and the Company's higher net retention under reinsurance treaties in recent years tend to allow for more volatility in losses. The increase in the private passenger automobile loss ratio is associated with product modifications as competitive market conditions are ongoing. The loss ratio for property reinsurance increased as the result of the Company's expansion of catastrophe coverages to the U.S. Midwest during 2007. An unusually large number of tornado and hail losses were incurred resulting in a loss ratio of 94.5% on this book of business. The property reinsurance loss ratio for the year was 33.0%, or slightly lower than 2006 on the remainder of our property reinsurance book of business.

The Company produced an overall savings on the handling of prior year claims during 2007 of $21.3 million. This net savings is included in the computation of loss ratios shown in the table insert, as is the $16.9 million savings produced during 2006 on prior year claims. The savings is generally consistent with recent prior years before consideration of savings related to retrospectively-rated contracts. Because of the high limits provided by the Company to its large trucking fleet insureds, the length of time necessary to settle larger, more complex claims and the volatility of the fleet transportation liability insurance business, the Company believes it is important to take a conservative posture in its reserving process. As claims are settled in years subsequent to their occurrence, the Company's claim handling process has, historically, tended to produce savings from the reserves provided. Changes in both gross premium volumes and the Company's reinsurance structure for its fleet transportation business can have a significant impact on future loss developments and, as a result, loss and loss expense ratios and prior year reserve development may not be consistent year to year.

Other operating expenses for 2007, before credits for allowances from reinsurers, increased $9.7 million (19.9%) to $58.4 million. This increase is due primarily to a $5.2 million increase in commission expense related to increased business produced through non-affiliated agents and brokers including commissions relating to higher property reinsurance premium volume. Additionally, 2006 operating expenses were favorably impacted by a recovery of nearly $1 million previously written off related to bankrupt reinsurers. After consideration for these three items, expenses before ceding allowances increased $.6 million, or 1.2% from 2006.

Reinsurance ceded credits were $.8 million (69%) higher in 2007, resulting from changes related to recent reinsurance treaties.

A portion of fleet transportation business is produced by direct sales efforts of Baldwin & Lyons, Inc. employees and, accordingly, this business does not incur commission expense on a consolidated basis. Instead, the expenses of the agency operations, including salaries and bonuses of salesmen, travel expenses, etc. are included in operating expenses. In general, commissions paid by the insurance subsidiaries to the parent company exceed related acquisition costs incurred in the production of fleet transportation business. The ratio of net operating expenses of the insurance subsidiaries to net premiums earned was 30.9% during 2007 compared to 26.6% for 2006. Including the agency operations, and after elimination of inter-company commissions, the ratio of other operating expenses to operating revenue (defined as total revenue less gains on investments) was 27.7% for 2007 compared with 24.2% for 2006, reflective of the increase in commission expense, as discussed above.

The effective federal tax rate for consolidated operations for 2007 was 30.8%. This rate is lower than the statutory rate primarily because of tax-exempt investment income.

As a result of the factors mentioned above, net income for 2007 was $55.1 million compared to $38.2 million for 2006. Diluted earnings per share increased to $3.63 in 2007 from $2.54 in 2006. Earnings per share from operations, before gains on investments, was $1.91 compared to $1.80 in 2006.

Critical Accounting Policies

The Company's significant accounting policies are discussed in Note A to the consolidated financial statements. The following discussion is provided to highlight areas of the Company's accounting policies which are material and/or subject to significant degrees of judgment.

Investment Valuation

All marketable securities are included in the Company's balance sheet at current fair market value.

Approximately 70% of the Company's assets are composed of investments at December 31, 2008. Approximately 89% of these investments are publicly-traded, owned directly and have readily-ascertainable market values. The remaining 11% of investments are composed primarily of minority interests in several limited partnerships. These limited partnerships are engaged in the trading of public and non-public equity securities and debt, hedging transactions, real estate development and venture capital investment. These partnerships, themselves, do not have readily-determinable market values. Rather, the fair values recorded are those provided to the Company by the respective partnerships based on the underlying assets of the partnerships. While the majority of the underlying assets at December 31, 2008 are publicly-traded securities, some have been valued by the respective partnerships using their experience and judgment.

Approximately $4.1 million of fixed maturity investments (.7% of total invested assets) consists of bonds rated as less than investment grade at year end. These investments are primarily composed of shares in two widely diversified high yield bond funds where exposure to default by any single issuer is likely to be limited. These funds carry a Morningstar rating of three and five stars. We have included the investments in these funds in the total of non-investment grade bonds since, under the investment guidelines of the funds, the average bond quality rating could fall below BBB. At December 31, 2008, the market value of these bond funds, as recorded in the financial statements, was 17.6% less than cost.

In determining if and when a decline in market value below cost is other-than-temporary, we first make an objective analysis of each individual security where current market value is less than cost. For any security where the unrealized loss exceeds 20% of original or adjusted cost, and where that decline has existed for a period of at least six months, the decline is treated as an other-than-temporary impairment, without any subjective evaluation as to possible future recovery. For individual issues where the decline in value is less than 20% but the amount of the decline is considered significant, we will also evaluate the market conditions, trends of earnings, price multiples and other key measures for the securities to determine if it appears that the decline is other-than-temporary. In those instances, the Company also considers its intent and ability to hold investments until recovery or maturity. For any decline which is considered to be other-than-temporary, we recognize an impairment loss in the current period earnings as an investment loss. Declines which are considered to be temporary are recorded as a reduction in shareholders' equity, net of related federal income tax credits.

It is important to note that all investments included in the Company's financial statements are valued at current fair market values. The evaluation process for determination of other-than-temporary decline in value of investments does not change these valuations but, rather, determines when a decline in value will be recognized in the income statement (other-than-temporary decline) as opposed to a charge to shareholders' equity (temporary decline). Subsequent recoveries in value of investments which have incurred other-than-temporary impairment adjustments are accounted for as unrealized gains until the security is actually disposed of or sold. At December 31, 2008, unrealized gains include $7.2 million of appreciation on investments previously adjusted for other-than-temporary impairment, compared to $11.7 million of impairment write-downs at that date. See Note B to the consolidated financial statements for additional detail with respect to this process. This evaluation process is subject to risks and uncertainties since it is not always clear what has caused a decline in value of an individual security or since some declines may be associated with general market conditions or economic factors which relate to an industry, in general, but not necessarily to an individual issue. The Company has attempted to minimize many of these uncertainties by adopting a largely objective evaluation process which results in income statement recognition of any investment which, over a six month period, is unable to recover from a 20% decline in value from our cost basis. However, to the extent that certain declines in value are reported as unrealized at December 31, 2008, it is possible that future earnings charges will result should the declines in value increase or persist or should the security actually be disposed of while market values are less than cost. At December 31, 2008, the total gross unrealized loss included in the Company's investment portfolio was approximately $7.0 million. No individual issue constituted a material amount of this total. Had this entire amount been considered other-than-temporary at December 31, 2008, investment losses would have increased by $.30 per share for the year, after tax. There would, however, have been no impact on total shareholders' equity or book value per share since the decline in value of these securities was already recognized as a reduction to shareholders' equity at December 31, 2008.

Reinsurance Recoverable

Reinsurance ceded transactions were as follows for the years ended December 31 (dollars in thousands):

	2008	2007	2006
Premium ceded (reduction to premium earned)	**$41,219**	$32,974	$24,841
Losses ceded (reduction to losses incurred)	**53,398**	4,981	14,026
Commissions from reinsurers (reduction to operating expenses)	**3,084**	2,044	1,205

Amounts recoverable under the terms of reinsurance contracts comprise approximately 21% of total Company assets as of December 31, 2008. In order to be able to provide the high limits required by the Company's fleet transportation company insureds, we share a significant amount of the insurance risk of the underlying contracts with various insurance entities through the use of reinsurance contracts. Some reinsurance contracts provide that a loss be shared among the Company and its reinsurers on a predetermined pro-rata basis ("quota-share") while other contracts provide that the Company keep a fixed amount of the loss, similar to a deductible, with reinsurers taking all losses above this fixed amount ("excess of loss"). Some risks are covered by a combination of quota-share and excess of loss contracts. The computation of amounts due from reinsurers is based upon the terms of the various contracts and follows the underlying estimation process for loss and loss expense reserves, as described below. Accordingly, the uncertainties inherent in the loss and loss expense reserving process also affect the amounts recorded as recoverable from reinsurers. Estimation uncertainties are greatest for claims which have occurred but which have not yet been reported to the Company. Further, the high limits provided by the Company's insurance policies for fleet transportation liability and workers' compensation, provide more variability in the estimation process than lines of business with lower coverage limits.

It should be noted, however, that a change in the estimate of amounts due from reinsurers on unpaid claims will not, in itself, result in charges or credits to losses incurred. This is because any change in estimated recovery follows the estimate of the underlying loss. Thus, it is the computation of the underlying loss that is critical.

As with any receivable, credit risk exists in the recoverability of reinsurance. This is even more pronounced than in normal receivable situations since recoverable amounts are not generally due until the loss is settled which, in some cases, may be many years after the contract was written. If a reinsurer is unable, in the future, to meet its financial commitments under the terms of the contracts, the Company would be responsible for the reinsurer's portion of the loss. The financial condition of each of the Company's reinsurers is initially determined upon the execution of a given treaty and only reinsurers with the superior credit ratings available are utilized. However, as noted above, reinsurers are often not called upon to satisfy their obligations for several years and changes in credit worthiness can occur in the interim period. Reviews of the current financial strength of each reinsurer are made continually and, should impairment in the ability of a reinsurer be determined to exist, current year operations would be charged in amounts sufficient to provide for the Company's additional liability. Such charges are included in other operating expenses, rather than losses and loss expenses incurred, since the inability of the Company to collect from reinsurers is a credit risk rather than a deficiency associated with the loss reserving process. See Notes D and L to the consolidated financial statements, for further discussion of reinsurance and concentrations of credit risk with respect to reinsurance recoverable.

Loss and Loss Expense Reserves

The Company's loss and loss expense reserves for each significant product group are shown in the following table for direct and assumed and on a net of reinsurance basis at December 31, 2008 and 2007 (dollars in thousands). Those product groups individually comprising less than three percent of the Company's total reserves are shown in the aggregate as "All other".

	Direct and Assumed		Net	
Line of Business	**2008**	2007	**2008**	2007
Fleet transportation	**$ 325,765**	$ 316,480	**$ 173,320**	$ 186,644
Property reinsurance	**37,489**	33,252	**37,489**	33,252
Private passenger automobile	**9,802**	11,701	**9,802**	11,701
All other	**16,502**	17,184	**11,022**	12,903
	$ 389,558	$ 378,616	**$ 231,633**	$ 244,500

The Company's reserves for losses and loss expenses ("reserves") are determined based on complex estimation processes using historical experience, current economic information and, when necessary, available industry statistics. Reserves are evaluated in three basic categories (1) "case basis", (2) "incurred but not reported" and (3) "loss adjustment expense" reserves. Case basis reserves are established for specific known loss occurrences at amounts dependent upon various criteria such as type of coverage, severity and the underlying policy limits, as examples. Case basis reserves are generally estimated by experienced claims adjusters using established Company guidelines and are subject to review by claims management. Incurred but not reported reserves, which are established for those losses which have occurred, but have not yet been reported to the Company, are not linked to specific claims but are computed on a "bulk" basis. Common actuarial methods are employed in the establishment of incurred but not reported loss reserves using company historical loss data, consideration of changes in the Company's business and study of current economic trends affecting ultimate claims costs. Loss adjustment expense reserves, or reserves for the costs associated with the investigation and settlement of a claim, are also bulk reserves representing the Company's estimate of the costs associated with the claims handling process. Loss adjustment expense reserves include amounts ultimately allocable to individual claims as well as amounts required for the general overhead of the claims handling operation that are not specifically allocable to individual claims. Historical analyses of the ratio of loss adjusting expenses to losses paid on prior closed claims and study of current economic trends affecting loss settlement costs are used to estimate the loss adjustment reserve needs related to the established loss reserves. Each of these reserve categories contain elements of uncertainty which assure variability when compared to the ultimate costs to settle the underlying claims for which the reserves are established. The reserving process requires management to continuously monitor and evaluate the life cycle of claims based on the class of business and the nature of claims. The Company's claims range from the very routine private passenger automobile "fender bender" to the highly complex and costly third party bodily injury claim involving large tractor-trailer rigs. Reserving for each class of claims requires a set of assumptions based upon historical experience, knowledge of current industry trends and seasoned judgment. The high limits provided in the Company's fleet transportation liability policies provide for greater volatility in the reserving process for more serious claims. Court rulings, legislative actions and trends in jury awards also play a significant role in the estimation process of larger claims. The Company continuously reviews and evaluates loss developments subsequent to each measurement date and adjusts its reserve estimation assumptions, as necessary, in an effort to achieve the best possible estimate of the ultimate remaining loss costs at any point in time. Changes to previously established reserve amounts are charged or credited to losses and loss expenses incurred in the accounting periods in which they are determined. Note C to the consolidated financial statements includes additional information relating to loss and LAE reserve development.

The Company's methods for determining loss and loss expense reserves are essentially identical for interim and annual reporting.

A detailed analysis and discussion for each of the above basic reserve categories follows.

Reserves for known losses (Case reserves)

The Company's reserves for known claims are determined on an individual case basis and can range from the routine private passenger "fender bender" valued at a few hundred dollars to the very complex long-haul trucking claim involving multiple vehicles, severe injuries and extensive property damage costing several millions of dollars to settle. Each known claim, regardless of complexity, is handled by a claims adjuster experienced with claims of this nature and a "case" reserve, appropriate for the individual loss occurrence, is established. For very routine "short-tail" claims such as private passenger physical damage, the Company initially records a minimum reserve that is based upon historical loss settlements adjusted for current trends. As information regarding the loss occurrence is gathered in the claim handling process, the reserve is adjusted to reflect the anticipated ultimate cost to settle the claim. For more complex claims which can tend toward being "long-tail" in nature, an experienced claims adjuster will review the facts and circumstances surrounding the loss occurrence to make a determination of the reserve to be established. Many of the more complex claims involve litigation and necessitate an evaluation of potential jury awards in addition to the factual information to determine the value of each claim. Each claim is continually monitored and the recorded reserve is increased or decreased relative to information gathered during the settlement life cycle.

Reserves for incurred but not reported losses

The Company uses both standard actuarial techniques common to most insurance companies as well as techniques developed by the Company in consideration of its specialty business products. For its short-tail lines of business, the Company uses predominantly the incurred or paid loss development factor methods. The Company has found that the use of accident quarter loss development triangles, rather than those based upon accident year, are most responsive to claim settlement trends and fluctuations in premium exposures for its short-tail lines. A minimum of 12 running accident quarters is used to project the reserve necessary for incurred but not reported losses for its short-tail lines.

The Company also uses the loss development factor approach for its long-tail lines of business. A minimum of 15 accident years is included in the loss development triangles used to calculate link ratios and the selected loss development factors used to determine the reserves for incurred but not reported losses. A minimum of 20 accident years is used for long-tail workers' compensation reserve projections. More emphasis is placed on the use of tail factors for the Company's long-tail lines of business.

For the Company's large fleet trucking risks, which are covered by annually-changing reinsurance agreements and which contain wide-ranging self-insured retentions ("SIR") as low as $25,000 per loss occurrence and as high as several million dollars per occurrence, traditional actuarial methods are supplemented by other methods in consideration of the Company's exposures to loss. In situations where the Company's reinsurance structure, the insured's SIR selections, policy volume, and other factors are changing, current accident period loss exposures may not be homogenous with historical loss data to allow for reliable projection of future developed losses. Therefore, the Company supplements the above-described actuarial methods with loss ratio reserving techniques developed from our databases to arrive at the reserve for losses incurred but not reported for the calendar/accident period under review. Management relies on its extensive historical pricing and loss history databases to produce reserve factors unique to this specialty business. As losses for a given calendar/accident period develop with the passage of time, management evaluates such development on a quarterly basis and will adjust reserve factors, as necessary, to reflect current judgment with regard to the anticipated ultimate incurred losses. This process continues until all losses are settled for each period subject to this method.

Reserves for loss adjustment expenses

The Company uses historical analysis of the ratios of allocated loss adjustment expenses paid to losses paid on closed claims to arrive at the expected ultimate incurred loss adjustment expense factors for each of its major products. Once developed, the factors are applied to the expected ultimate incurred losses, including IBNR, on all open claims. The resulting ultimate incurred allocated loss adjustment expense is then reduced by amounts paid to date on all open claims to arrive at the reserve for allocated loss adjustment expenses to be incurred in the future for the handling of specific claims.

For those loss adjustment expenses not specific to individual claims (general claims handling expenses referred to as unallocated LAE) the Company uses standard industry loss adjustment expenses paid to losses paid (net of reinsurance) ratio analysis to establish the necessary reserves. The selected factors are applied to 100% of IBNR reserves and to case reserves with consideration given for that portion of loss adjustment expense already paid at the reserve measurement date. Such factors are monitored and revised, as necessary, on a quarterly basis.

The reserving process requires management to continuously monitor and evaluate the life cycle of claims based on the class of business and the nature of claims. As previously noted, our claims range from the very routine private passenger automobile "fender bender" to the highly complex and costly third party bodily injury claim involving large tractor-trailer rigs. Reserving for each class of claims requires a set of assumptions based upon historical experience, knowledge of current industry trends and seasoned judgment. The high limits provided in the Company's fleet transportation liability policies provide for greater volatility in the reserving process for more serious claims. Court rulings, legislative actions and trends in jury awards also play a significant role in the estimation process of larger claims. The Company continuously reviews and evaluates loss developments subsequent to each measurement date and adjusts its reserve estimation assumptions, as necessary, in an effort to achieve the best possible estimate of the ultimate remaining loss costs at any point in time. Changes to previously established reserve amounts are charged or credited to losses and loss expenses incurred in the accounting periods in which they are determined. Note C to the consolidated financial statements includes additional information relating to loss and loss adjustment expense reserve development.

The Company's methods for determining loss and loss expense reserves are essentially identical for interim and annual reporting.

Sensitivity Analysis - Potential impact on reserve volatility from changes in key assumptions

Management is aware of the potential for variation from the reserves established at any particular point in time. Redundancies or deficiencies could develop in future valuations of the currently established loss and loss expense reserve estimates under a variety of reasonably possible scenarios. The Company's reserve selections are developed to be a "best estimate" of unpaid loss at a point in time and, due to the unique nature of our exposures, particularly in the large fleet transportation excess product where insured's policies of insurance combine large self-insured retentions with high policy limits, ranges of reserve estimates are not established during the reserving process. However, basic assumptions that could potentially impact future volatility of our valuations of current loss and loss expense reserve estimates include, but are not limited to, the following:

- Consistency in the individual case reserving processes
- The selection of loss development factors in the establishment of bulk reserves for incurred but reported losses and loss expenses
- Projected future loss trend
- Expected loss ratios for the current book of business, particularly the Company's large fleet excess product, where the number of accounts insured, selected self-insured retentions, policy limits and reinsurance structure may vary widely period to period

Under reasonably possible scenarios, it is conceivable that the Company's selected loss reserve estimates could be 10%, or more, redundant or deficient. The majority of the Company's reserves for losses and loss expenses, on either a gross or a net of reinsurance basis, relates to the fleet transportation product. Perhaps the most significant example of sensitivity to variation in the key assumptions is the loss ratio selection for the Company's large fleet excess product for policies subject to certain recent major reinsurance treaties (approximately $84.9 million, or approximately 27% of, carried direct reserves for fleet transportation).

Federal Income Tax Considerations

The liability method is used in accounting for federal income taxes. Using this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The provision for deferred federal income tax was based on items of income and expense that were reported in different years in the financial statements and tax returns and were measured at the tax rate in effect in the year the difference originated. Net deferred tax liabilities reported at December 31, 2008 and 2007 consisted of (dollars in thousands):

	2008	2007
Total deferred tax liabilities	**$ 13,155**	$ 33,168
Total deferred tax assets	**23,745**	22,050
Net deferred tax liabilities	**$ 10,590**	$ (11,118)

Deferred tax assets at December 31, 2008, include approximately $15.6 million related to loss and loss expense reserves of which, $9.6 million relates to policy liability discounts required by the Internal Revenue Code which are perpetual in nature and, in the absence of the termination of business, will not reverse to a material degree in the foreseeable future. An additional $4.1 million relates to impairment adjustments made to investments, as required by accounting regulations. The sizable unrealized gains in the Company's investment portfolios would allow for the recovery of this deferred tax at any time. Limited partnership investments represent $2.4 million of deferred tax assets. The balance of deferred tax assets, approximately $1.6 million, consists of various normal operating expense accruals and is not considered to be material. As a result of its analysis, management has determined that no valuation allowance is necessary at December 31, 2008.

Financial Accounting Standards Board Interpretation (FIN) No. 48, *Accounting for Uncertainty in Income Taxes — an Interpretation of FASB Statement No. 109,* provides guidance for recognizing and measuring uncertain tax positions, as defined in SFAS No. 109, *Accounting for Income Taxes*. FIN 48 prescribes a threshold condition that a tax position must meet for any of the benefit of the uncertain tax position to be recognized in the financial statements. Based on this guidance, we regularly analyze tax positions taken or expected to be taken in a tax return based on the threshold condition prescribed under FIN 48. Tax positions that do not meet or exceed this threshold condition are considered uncertain tax positions. We accrue interest related to these uncertain tax positions which is recognized in income tax expense. Penalties, if any, related to uncertain tax positions would be recorded in income tax expenses.

Forward-Looking Information

Any forward-looking statements in this report including, without limitation, statements relating to the Company's plans, strategies, objectives, expectations, intentions and adequacy of resources, are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Investors are cautioned that such forward-looking statements involve risks and uncertainties including, without limitation, the following: (i) the

Company's plans, strategies, objectives, expectations and intentions are subject to change at any time at the discretion of the Company; (ii) the Company's business is highly competitive and the entrance of new competitors into or the expansion of the operations by existing competitors in the Company's markets and other changes in the market for insurance products could adversely affect the Company's plans and results of operations; and (iii) other risks and uncertainties indicated from time to time in the Company's filings with the Securities and Exchange Commission.

Impact of Inflation

To the extent possible, the Company attempts to recover the costs of inflation by increasing the premiums it charges. Within the fleet transportation business, a majority of the Company's premiums are charged as a percentage of an insured's gross revenue or payroll. As these charging bases increase with inflation, premium revenues are immediately increased. The remaining premium rates charged are adjustable only at periodic intervals and often require state regulatory approval. Such periodic increases in premium rates may lag far behind cost increases.

To the extent inflation influences yields on investments, the Company is also affected. The Company's short-term and fixed investment portfolios are structured in direct response to available interest rates over the yield curve. As available market interest rates fluctuate in response to the presence or absence of inflation, the yields on the Company's investments are impacted. Further, as inflation affects current market rates of return, previously committed investments might increase or decline in value depending on the type and maturity of investment (see comments under Market Risk, following).

Inflation must also be considered by the Company in the creation and review of loss and loss adjustment expense reserves since portions of these reserves are expected to be paid over extended periods of time. The anticipated effect of inflation is implicitly considered when estimating liabilities for losses and loss adjustment expenses.

Market Risk

The Company operates solely within the property and casualty insurance industry and, accordingly, has significant invested assets which are exposed to various market risks. These market risks relate to interest rate fluctuations, equities market prices and, to a far lesser extent, foreign currency rate fluctuations. All of the Company's invested assets, with the exception of investments in limited partnerships, are classified as available for sale and are listed as such in Note B to the consolidated financial statements.

The most significant of the three identified market risks relates to prices in the equities market. Though not the largest category of the Company's invested assets, equity securities have a high potential for short-term price fluctuation. The market value of the Company's equity positions at December 31, 2008 was $63.2 million or approximately 12% of invested assets. This market valuation includes $23.1 million of appreciation over the cost basis of the equity security investments. Funds invested in the equities market are not considered to be assets necessary for the Company to conduct its daily operations and, therefore, can be committed for extended periods of time. The long-term nature of the Company's equity investments allows it to invest in positions where ultimate value, and not short-term market fluctuations, is the primary focus.

Reference is made to the discussion of limited partnership investments in the Critical Accounting Policies portion of this report. All of the market risks, attendant to equity securities, apply to the underlying assets in these partnerships, and to a greater degree because of the generally more aggressive investment philosophies utilized by the partnerships. In addition, these investments are illiquid. There is no primary or secondary market on which these limited partnerships trade and, in most cases, the Company is prohibited from disposing of its limited partnership interests for some period of time and must seek approval from the general partner for any such disposal. Distributions of earnings from these partnerships are largely at the sole discretion of the general partners and distributions are generally not received by the Company for many years after the earnings have been reported. Finally, through the application of the equity method of accounting, the Company's share of net income reported by the limited partnerships may include significant amounts of unrealized appreciation on the underlying investments. As such, the likelihood that reported income from limited partnership investments will be ultimately returned to the Company in the form of cash is markedly lower than the Company's other investments, where income is reported only when a security is actually sold.

The Company's fixed maturity portfolio totaled $364.3 million at December 31, 2008. Approximately 83% of this portfolio is made up of U.S. Government and government agency obligations and state and municipal debt securities; 85.6% of the portfolio matures within 5 years; and the average life of the Company's fixed maturity investments is approximately 3.0 years. Although the Company is exposed to interest rate risk on its fixed maturity investments, given the anticipated duration of the Company's liabilities (principally insurance loss and loss expense reserves) relative to investment maturities, even a 100 to 200 basis point increase in interest rates would not have even a moderate impact on the Company's ability to conduct daily operations or to meet its obligations.

There is an inverse relationship between interest rate fluctuations and the fair value of the Company's fixed maturity investments. Additionally, the fair value of interest rate sensitive instruments may be affected by the financial strength of the issuer, prepayment options, relative values of alternative investments, liquidity of the investment and other general market conditions. The Company monitors its sensitivity to interest rate risk by measuring the change in fair value of its fixed maturity investments relative to hypothetical changes in interest rates. As previously indicated, several other factors can impact the fair values of fixed maturity investments and, therefore, significant variations in market interest rates could produce quite different results from the hypothetical estimates presented in the next paragraph.

A 10 percentage point increase or decrease in the loss factors actually utilized in the Company's reserve determination at December 31, 2008 would increase or decrease gross loss reserves by approximately $17.2 million. On a net basis, a 10 percentage point increase in loss ratio would increase net loss reserves by approximately $7.8 million whereas a 10 percentage point decrease would decrease net loss reserves by approximately $9.4 million. Similarly, a 20 percentage point increase or decrease would increase or decrease gross loss reserves by approximately $34.3 million. On a net basis, a 20 percentage point increase in loss ratio would increase net loss reserves by approximately $15.5 million whereas a 20 percentage point decrease would decrease net loss reserves by approximately $20.4 million with the difference attributable to minimums and maximums included in the various reinsurance contracts.

The Company's exposure to foreign currency risk is not material.

Common Stock Market Prices and Dividends

The Company's Class A and Class B common stocks are traded on The NASDAQ Stock Market® under the symbols BWINA and BWINB, respectively.

The Class A and Class B common shares have identical rights and privileges except that Class B shares have no voting rights other than on matters for which Indiana law requires class voting.

As of December 31, 2008, there were approximately 400 record holders of Class A Common Stock and approximately 1,000 record holders of Class B Common Stock.

The table below sets forth the range of high and low sale prices for the Class A and Class B Common Stock for 2008 and 2007, as reported by NASDAQ and published in the financial press. The quotations reflect interdealer prices without retail markup, markdown or commission and do not necessarily represent actual transactions.

	Class A		Class B		Cash Dividends Declared
	High	Low	High	Low	
2008:					
Fourth Quarter	**$ 23.00**	**$ 13.50**	**$ 25.75**	**$ 14.01**	**$ .25**
Third Quarter	**23.74**	**17.97**	**27.90**	**17.01**	**.25**
Second Quarter	**23.22**	**20.19**	**25.99**	**17.36**	**.25**
First Quarter	**26.40**	**22.60**	**27.95**	**23.51**	**.25**
2007:					
Fourth Quarter	28.00	22.83	29.00	25.10	.35
Third Quarter	28.77	25.01	29.61	25.10	.60
Second Quarter	27.85	23.42	26.79	24.25	.25
First Quarter	29.25	24.03	26.55	23.48	.45

The Company has paid quarterly cash dividends continuously since 1974. The current regular quarterly dividend rate is $.25 per share. The Company expects to continue its policy of paying regular cash dividends although there is no assurance as to future dividends because they are dependent on future earnings, capital requirements and financial conditions and are subject to regulatory restrictions as described in Note F to the consolidated financial statements. At times, the Company has paid an extra cash dividend in recognition of the Company's more than adequate capitalization, the favorable income tax rates available to individuals on dividends as well as the Company's excellent earnings over the past four years. The Board intends to address the subject of dividends at each of its future meetings considering the Company's earnings, returns on investments and its capital needs; however, shareholders should not expect extra dividends, if any, in the future to follow any predetermined pattern.

Contractual Obligations

The table below sets forth the amounts of the Company's contractual obligations at December 31, 2008.

	Payments Due by Period				
	Total	Less than 1 year	1 - 3 Years	3 - 5 Years	More Than 5 Years
			(dollars in millions)		
Loss and loss expense reserves	$ 389.6	$ 114.1	$ 103.6	$ 43.3	$ 128.6
Investment commitments	2.5	2.5	—	—	—
Operating leases	6.7	1.4	2.9	2.4	—
Borrowings	9.0	—	9.0	—	—
Total	$ 407.8	$ 118.0	$ 115.5	$ 45.7	$ 128.6

The Company's loss and loss expense reserves do not have contractual maturity dates and the exact timing of the payment of claims cannot be predicted with certainty. However, based upon historical payment patterns, we have included an estimate of when we might expect our direct loss and loss expense reserves (without the benefit of reinsurance recoveries) to be paid in the preceding table. Timing of the collection of the related reinsurance recoverable, estimated to be $160.0 million at December 31, 2008, would approximate that of the above projected direct reserve payout.

The investment commitments in the above table relate to maximum unfunded capital obligations for limited partnership investments at December 31, 2008.

Borrowings are made under a line of credit with a current expiration of May, 2011.

Management's Responsibility For Financial Statements

Management is responsible for the preparation of the Company's consolidated financial statements and related information appearing in this report. Management believes that the consolidated financial statements fairly reflect the form and substance of transactions and that the financial statements reasonably present the Company's financial position and results of operations in conformity with generally accepted accounting principles. Management has included in the Company's financial statements amounts that are based upon estimates and judgments which it believes are reasonable under the circumstances.

Ernst & Young LLP, an independent registered public accounting firm, audits the Company's consolidated financial statements in accordance with the standards of the Public Company Accounting Oversight Board and provides an objective, independent review of the fairness of reported operating results and financial position.

The Board of Directors of the Company has an Audit Committee composed of three non-management Directors. The committee meets periodically with financial management, the internal auditors and the independent registered public accounting firm to review accounting, control, auditing and financial reporting matters.

Management's Report on Internal Control Over Financial Reporting

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f) and 15d-15(f). Under the supervision and with the participation of management, including the chief executive officer and the chief financial officer, the Company conducted an evaluation of the effectiveness of its internal control over financial reporting based on the framework in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation under this framework, management concluded that the Company's internal control over financial reporting was effective as of December 31, 2008. The effectiveness of the Company's internal control over financial reporting as of December 31, 2008 has been audited by Ernst & Young LLP, an independent registered public accounting firm, as stated in their report which is included herein.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders of
Baldwin & Lyons, Inc.

We have audited Baldwin & Lyons, Inc. and subsidiaries internal control over financial reporting as of December 31, 2008, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the "COSO criteria"). Baldwin & Lyons, Inc. and subsidiaries management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Baldwin & Lyons, Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2008, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Baldwin & Lyons, Inc. and subsidiaries as of December 31, 2008 and 2007, and the related consolidated statements of operations, changes in equity other than capital, and cash flows for each of the three years in the period ended December 31, 2008, and our report dated March 16, 2009 expressed an unqualified opinion thereon.

Ernst & Young LLP

Indianapolis, Indiana
March 16, 2009

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders of
Baldwin & Lyons, Inc.

We have audited the accompanying consolidated balance sheets of Baldwin & Lyons, Inc. and subsidiaries as of December 31, 2008 and 2007, and the related consolidated statements of operations, changes in equity other than capital, and cash flows for each of the three years in the period ended December 31, 2008. Our audits also included the financial statement schedules listed in the Index at Item 15(a). These financial statements and schedules are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedules based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Baldwin & Lyons, Inc. and subsidiaries at December 31, 2008 and 2007, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2008, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedules, when considered in relation to the basic financial statements taken as a whole, present fairly in all material respects the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Baldwin & Lyons, Inc. and subsidiaries internal control over financial reporting as of December 31, 2008, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 16, 2009 expressed an unqualified opinion thereon.

Ernst + Young LLP

Indianapolis, Indiana
March 16, 2009

Consolidated Balance Sheets

Baldwin & Lyons, Inc. and Subsidiaries

	December 31	
	2008	2007
	(dollars in thousands)	
Assets		
Investments:		
Fixed maturities	**$ 364,280**	$ 338,011
Equity securities	**63,200**	99,736
Limited partnerships	**59,864**	80,884
Short-term and other	**33,820**	44,768
	521,164	563,399
Cash and cash equivalents	**16,657**	82,137
Accounts receivable--less allowance (2008, $650; 2007, $820)	**29,701**	33,412
Accrued investment income	**5,019**	4,762
Reinsurance recoverable	**159,989**	132,811
Prepaid reinsurance premiums	**4,914**	5,844
Deferred policy acquisition costs	**2,326**	3,193
Property and equipment--less accumulated depreciation (2008, $9,003; 2007, $7,676)	**11,582**	9,265
Notes receivable from employees	**2,199**	2,228
Other assets	**13,602**	5,782
Deferred federal income taxes	**10,590**	—
	$ 777,743	$ 842,833
Liabilities and Shareholders' Equity		
Reserves:		
Losses and loss expenses	**$ 389,558**	$ 378,616
Unearned premiums	**17,183**	22,678
	406,741	401,294
Reinsurance payable	**2,862**	7,261
Short-term borrowings	**9,000**	—
Accounts payable and other liabilities	**27,076**	31,874
Current federal income taxes	**1,997**	10,568
Deferred federal income taxes	**—**	11,118
	447,676	462,115
Shareholders' equity:		
Common stock, no par value:		
Class A voting -- authorized 3,000,000 shares; outstanding -- 2008, 2,623,109; 2007, 2,650,059 shares	**112**	113
Class B non-voting -- authorized 20,000,000 shares; outstanding -- 2008, 12,163,251; 2007, 12,592,555	**519**	537
Additional paid-in capital	**46,312**	47,899
Unrealized net gains on investments	**19,410**	36,876
Retained earnings	**263,714**	295,293
	330,067	380,718
	$ 777,743	$ 842,833

Consolidated Statements of Operations

Baldwin & Lyons, Inc. and Subsidiaries

	Year Ended December 31		
	2008	2007	2006
	(dollars in thousands, except per share data)		
Revenue:			
Net premiums earned	**$ 182,299**	$ 179,065	$ 169,766
Net investment income	**17,063**	19,595	19,548
Net realized gains (losses) on investments	**(47,749)**	40,096	17,064
Commissions and other income	**5,317**	5,007	6,691
	156,930	243,763	213,069
Expenses:			
Losses and loss expenses incurred	**115,752**	107,781	112,604
Other operating expenses	**58,577**	56,330	47,455
	174,329	164,111	160,059
Income (loss) before federal income taxes	**(17,399)**	79,652	53,010
Federal income taxes (benefits)	**(9,686)**	24,521	14,825
Net income (loss)	**$ (7,713)**	$ 55,131	$ 38,185
Per share data:			
Diluted earnings	**$ (.51)**	$ 3.63	$ 2.54
Basic earnings	**$ (.51)**	$ 3.63	$ 2.54
Dividends	**$ 1.00**	$ 1.65	$ 2.55

Consolidated Statements of Changes in Equity Other Than Capital

Baldwin & Lyons, Inc. and Subsidiaries

	2008	2007	2006
		(dollars in thousands)	
Balances at beginning of year:			
Retained earnings	**$ 295,293**	$ 264,060	$ 264,719
Unrealized gains on investments	**36,876**	47,229	42,440
	332,169	311,289	307,159
Changes arising from income-producing activities:			
Net income (loss)	**(7,713)**	55,131	38,185
Gains (losses) on investments:			
Pre-tax holding gains (losses) on debt and equity securities arising during period	**(41,058)**	1,027	13,241
Federal income taxes	**(14,370)**	359	4,634
	(26,688)	668	8,607
Pre-tax gains (losses) on debt and equity securities included in net income (loss) during period	**(14,188)**	16,955	5,874
Federal income taxes	**(4,966)**	5,934	2,056
	(9,222)	11,021	3,818
Change in unrealized gains (losses) on investments	**(17,466)**	(10,353)	4,789
Foreign exchange adjustment	**(1,468)**	1,164	(20)
Comprehensive income - total realized and unrealized income (loss)	**(26,647)**	45,942	42,954
Other changes affecting retained earnings:			
Cash dividends paid to shareholders	**(15,096)**	(25,062)	(38,435)
Cost of treasury shares in excess of original issue proceeds	**(7,302)**	—	(389)
	(22,398)	(25,062)	(38,824)
Total changes	**(49,045)**	20,880	4,130
Balances at end of year:			
Retained earnings	**263,714**	295,293	264,060
Unrealized gains on investments	**19,410**	36,876	47,229
	$ 283,124	$ 332,169	$ 311,289

Consolidated Statements of Cash Flows

Baldwin & Lyons, Inc. and Subsidiaries

	2008	2007	2006
	(dollars in thousands)		
Operating activities			
Net income (loss)	**$ (7,713)**	$ 55,131	$ 38,185
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Change in accounts receivable and unearned premium	**(165)**	(4,891)	(5,262)
Change in accrued investment income	**(257)**	247	(1,496)
Change in reinsurance recoverable on paid losses	**(3,453)**	4,921	(619)
Change in losses and loss expenses reserves net of reinsurance	**(12,786)**	(5,097)	7,767
Change in other assets, other liabilities and current income taxes	**(20,011)**	5,376	(10,458)
Amortization of net policy acquisition costs	**20,353**	18,941	12,950
Net policy acquisition costs deferred	**(19,485)**	(17,392)	(13,316)
Provision for deferred income taxes	**(14,129)**	5,620	2,222
Bond amortization	**3,427**	2,453	2,295
(Gain) loss on sale of property	**(17)**	35	(20)
Depreciation	**2,976**	2,337	1,953
Net (gain) loss on investments	**47,749**	(40,096)	(17,064)
Excess tax benefit related to stock options	**—**	(253)	(604)
Compensation expense related to discounted stock options	**—**	—	20
Net cash provided by (used in) operating activities	**(3,511)**	27,332	16,553
Investing activities			
Purchases of fixed maturities and equity securities	**(276,737)**	(232,147)	(246,679)
Purchases of limited partnership interests	**(16,199)**	(5,995)	(4,957)
Proceeds from maturities	**31,623**	164,739	112,095
Proceeds from sales of fixed maturities	**161,814**	44,508	37,774
Proceeds from sales of equity securities	**45,813**	55,866	33,153
Net sales (purchases) of short-term investments	**10,972**	14,557	(8,265)
Distributions from limited partnerships	**3,657**	5,565	3,562
Purchase of Transport Insurance Agency	**(2,661)**	—	—
Decrease in principal of notes receivable from employees	**29**	110	15
Purchases of property and equipment	**(5,348)**	(6,225)	(3,000)
Proceeds from disposals of property and equipment	**72**	935	116
Net cash provided by (used in) investing activities	**(46,965)**	41,913	(76,186)
Financing activities			
Dividends paid to shareholders	**(15,096)**	(25,062)	(38,435)
Proceeds from sale of common stock	**—**	2,211	6,804
Excess tax benefit related to stock options	**—**	253	604
Drawings on line of credit	**9,000**	—	—
Cost of treasury shares	**(8,908)**	—	(401)
Net cash used in financing activities	**(15,004)**	(22,598)	(31,428)
Increase (decrease) in cash and cash equivalents	**(65,480)**	46,647	(91,061)
Cash and cash equivalents at beginning of year	**82,137**	35,490	126,551
Cash and cash equivalents at end of year	**$ 16,657**	$ 82,137	$ 35,490

Baldwin & Lyons, Inc. and Subsidiaries
(Dollars in thousands, except per share data)

Note A - Summary of Significant Accounting Policies

Basis of Presentation: The consolidated financial statements include the accounts of Baldwin & Lyons, Inc. and its wholly owned subsidiaries (the "Company"). All significant inter-company transactions and accounts have been eliminated in consolidation.

Use of Estimates: Preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

Cash and Cash Equivalents: The Company considers investments in money market funds to be cash equivalents. Carrying amounts for these instruments approximate their fair values.

Investments: Carrying amounts for fixed maturity securities (bonds and notes) represent fair value and are based on quoted market prices, where available, or broker/dealer quotes for specific securities where quoted market prices are not available. Equity securities (common stocks) are carried at quoted market prices (fair value). Limited partnerships are accounted for using the equity method with the corresponding change in value recorded as a component of net gains or losses on investments. Other investments are carried at either market value or cost, depending on the nature of the investment. All fixed maturity and equity securities are considered to be available for sale; the related unrealized net gains or losses (net of applicable tax effect) are reflected directly in shareholders' equity unless a decline in value is determined to be other-than-temporary, in which case, the loss is charged to income. In determining if and when a decline in market value below cost is other-than-temporary, an objective analysis is made of each individual security where current market value is less than cost. For any security where the unrealized loss exceeds 20% of original or adjusted cost, and where that decline has existed for a period of at least six months, the decline is treated as an other-than-temporary impairment, without subjective evaluation as to possible future recovery. Additionally, the Company takes into account any known subjective information in evaluating for impairment without consideration to the Company's 20% threshold. Although the Company has classified fixed maturity investments as available for sale, it has the ability to, and generally does, hold its fixed maturity investments to maturity. Short-term investments are carried at cost which approximates their fair values. Realized gains and losses on disposals of investments are determined by specific identification of cost of investments sold and are included in income.

Property and Equipment: Property and equipment is carried at cost. Depreciation is computed principally by the straight-line method.

Goodwill and Other Intangible Assets: Goodwill is not amortized. It is instead tested for impairment in accordance with Statement of Financial Accounting Standards No. 142 *Goodwill and Other Intangible Assets*, at the reporting-unit level. Goodwill is tested annually (during the fourth quarter) or more often if events or circumstances, such as adverse changes in the business climate, indicate there may be impairment. Intangible assets determined to have indefinite lives are not amortized but instead are tested for impairment at least annually, or more frequently if events or changes in circumstances indicate that the asset might be impaired. The impairment test compares the fair value of the indefinite-lived intangible asset to its carrying amount. Other acquired intangible assets determined to have finite lives, such as customer relationships and employment agreements, are amortized over their estimated useful lives in a manner that best reflects the economic benefits of the intangible asset. In addition, impairment testing is performed on these amortizing intangible assets if impairment indicators are noted.

Reserves for Losses and Loss Expenses: The reserves for losses and loss expenses, minor portions of which are discounted, are determined using case basis evaluations and statistical analyses and represent estimates of the ultimate cost of all reported and unreported losses which are unpaid at year end. These reserves include estimates of future trends in claim severity and frequency and other factors which could vary as the losses are ultimately settled. Although it is not possible to measure the degree of variability inherent in such estimates, management believes that the reserves for losses and loss expenses are adequate. The estimates are continually reviewed and as adjustments to these reserves become necessary, such adjustments are reflected in current operations.

Recognition of Revenue and Costs: Premiums are earned over the period for which insurance protection is provided. A reserve for unearned premiums, computed by the daily pro-rata method, is established to reflect amounts applicable to subsequent accounting periods. Commissions to unaffiliated companies and premium taxes applicable to unearned premiums are deferred and expensed as the related premiums are earned. The Company does not defer acquisition costs which are not directly variable with the production of premium. If it is determined that expected losses and deferred expenses will likely exceed the related unearned premiums, the asset representing deferred policy acquisition costs is reduced and an expense is charged against current operations to reflect any such premium deficiency. In the event that the expected premium deficiency exceeds deferred policy acquisition costs, an additional liability would be recorded with a corresponding expense to current operations for the amount of the excess premium deficiency. Anticipated investment income is considered in determining recoverability of deferred acquisition costs.

Reinsurance: Reinsurance premiums, commissions, expense reimbursements and reserves related to reinsured business are accounted for on bases consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts. Premiums ceded to other insurers have been reported as a reduction of premium earned. Amounts applicable to reinsurance ceded for unearned premium and claim loss reserves have been reported as reinsurance recoverable assets. Certain reinsurance contracts provide for additional or return premiums and commissions based upon profits or losses to the reinsurer over prescribed periods. Estimates of additional or return premiums and commissions are adjusted quarterly to recognize actual loss experience to date as well as projected loss experience applicable to the various contract periods. Estimates of reinstatement premiums on property reinsurance contracts covering catastrophic events are recorded concurrently with the related loss.

Should impairment in the ability of a reinsurer to satisfy its obligations to the Company be determined to exist, current year operations would be charged in amounts sufficient to provide for the Company’s additional liability. Such charges, when incurred, are included in other operating expenses, rather than losses and loss expenses incurred, since the inability of the Company to collect from reinsurers is a credit risk rather than a deficiency associated with the loss reserving process.

The Company accounts for foreign and domestic property reinsurance using the periodic method. Under the periodic method, premiums from foreign property reinsurance are recognized as revenue ratably over the contract term, and claims, including an estimate of claims incurred but not reported, are recognized as they occur.

Federal Income Taxes: A consolidated federal income tax return is filed by the Company and includes all wholly owned subsidiaries.

Deferred income tax assets and liabilities are recognized for temporary differences between the financial statement and tax return bases of assets and liabilities based on enacted tax rates and laws. The deferred tax benefits of the deferred tax assets are recognized to the extent realization of such benefits is more likely than not. Deferred income tax expense or benefit generally represents the net change in deferred income tax assets and liabilities during the year. Current income tax expense represents the tax consequences of revenues and expenses currently taxable or deductible on various income tax returns for the year reported.

In the ordinary course of business, the Company’s federal income tax returns are audited by the Internal Revenue Service.

Share-Based Payments: The Company uses a “Black-Scholes” option pricing model to value options granted to employees and non-employee directors in accordance with Statement of Financial Accounting Standards No. 123R, *Share-Based Payment*, adopted January 1, 2006 with no material effect. Compensation costs for all share-based awards to employees and non-employee directors are measured based on the grant date fair value of the award and are recognized over the period(s) during which the employee or non-employee director is required to perform service in exchange for the award (the vesting period).

Earnings Per Share: Diluted earnings per share of common stock are based on the average number of shares of Class A and Class B common stock outstanding during the year, adjusted for the dilutive effect, if any, of options outstanding. Basic earnings per share are presented exclusive of the effect of options outstanding. See *Note K - Earnings Per Share*.

Comprehensive Income: The Company records accumulated other comprehensive income from unrealized gains and losses on available-for-sale securities as a separate component of shareholders’ equity. Foreign exchange adjustments are generally not material and the Company has no defined benefit pension plan.

The enclosed *Statement of Changes in Equity Other Than Capital* refers to items of other comprehensive income as *Change in unrealized gains (losses) on investments* and *Foreign exchange adjustment*. A reclassification adjustment to other comprehensive income is made for *Gains during period included in net income*.

Reclassification: Certain prior year balances have been reclassified to conform to the current year presentation.

Note B - Investments

The following is a summary of investments at December 31:

	Fair Value	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Net Unrealized Gains (Losses)
2008:					
U.S. government obligations	**$ 26,560**	**$ 26,050**	**$ 510**	**$ —**	**$ 510**
Mortgage-backed securities	**13,490**	**13,813**	**157**	**(480)**	**(323)**
Obligations of states and political subdivisions	**267,152**	**263,026**	**5,132**	**(1,006)**	**4,126**
Corporate securities	**51,103**	**48,793**	**3,520**	**(1,210)**	**2,310**
Foreign government obligations	**5,975**	**5,867**	**108**	**—**	**108**
Total fixed maturities	**364,280**	**357,549**	**9,427**	**(2,696)**	**6,731**
Equity securities	**63,200**	**40,071**	**27,415**	**(4,286)**	**23,129**
Limited partnerships	**59,864**	**59,864**	**—**	**—**	**—**
Short-term	**33,820**	**33,820**	**—**	**—**	**—**
Total available-for-sale securities	**$ 521,164**	**$ 491,304**	**$ 36,842**	**$ (6,982)**	**29,860**
				Applicable federal income taxes	**(10,450)**
				Net unrealized gains - net of tax	**$ 19,410**
2007:					
U.S. government obligations	$ 27,484	$ 27,222	$ 267	$ (5)	$ 262
Mortgage-backed securities	16,153	16,226	58	(131)	(73)
Obligations of states and political subdivisions	280,665	278,752	2,337	(424)	1,913
Corporate securities	5,791	5,696	105	(10)	95
Foreign government obligations	7,918	7,868	50	—	50
Total fixed maturities	338,011	335,764	2,817	(570)	2,247
Equity securities	99,736	45,251	55,885	(1,400)	54,485
Limited partnerships	80,884	80,884	—	—	—
Short-term	44,768	44,768	—	—	—
Total available-for-sale securities	$ 563,399	$ 506,667	$ 58,702	$ (1,970)	56,732
				Applicable federal income taxes	(19,856)
				Net unrealized gains - net of tax	$ 36,876

The following table summarizes, for fixed maturity and equity security investments in an unrealized loss position at December 31, the aggregate fair value and gross unrealized loss categorized by the duration those securities have been continuously in an unrealized loss position.

	2008			2007		
	Number of Securities	Fair Value	Gross Unrealized Loss	Number of Securities	Fair Value	Gross Unrealized Loss
Fixed maturity securities:						
12 months of less	**47**	**$ 80,993**	**$ (2,675)**	15	$ 22,051	$ (476)
Greater than 12 months	**6**	**1,812**	**(21)**	9	7,551	(94)
Total fixed maturities	**53**	**82,805**	**(2,696)**	24	29,602	(570)
Equity securities:						
12 months of less	**33**	**$ 11,362**	**(3,085)**	15	9,194	(1,230)
Greater than 12 months	**14**	**5,845**	**(1,201)**	3	1,165	(170)
Total equity securities	**47**	**17,207**	**(4,286)**	18	10,359	(1,400)
Total fixed maturity and equity securities	**100**	**$ 100,012**	**$ (6,982)**	42	$ 39,961	$ (1,970)

Note B - Investments (continued)

Unrealized losses in the Company's fixed maturity portfolio are generally the result of interest rate fluctuations as well as the disruption of credit markets occasioned by recent financial market turmoil. The largest unrealized loss for any individual issue is approximately 12% of original or adjusted cost and the average unrealized loss for all fixed maturity securities in a loss position at December 31, 2008 is approximately 3% of original or adjusted cost. The Company has the ability and intent to hold these fixed maturity securities until their full cost can be recovered. Therefore, the Company does not believe the unrealized losses represent an other-than-temporary impairment as of December 31, 2008.

The fair value and the cost or amortized cost of fixed maturity investments, at December 31, 2008, by contractual maturity, are shown below. Actual maturities may differ from contractual maturities because borrowers have, in some cases, the right to call or prepay obligations with or without call or prepayment penalties. Pre-refunded municipal bonds are classified based on their pre-refunded call dates.

	Fair Value	Cost or Amortized Cost
One year or less	$ 121,850	$ 118,399
Excess of one year to five years	179,253	176,005
Excess of five years to ten years	30,148	29,731
Excess of ten years	19,539	19,601
Total maturities	350,790	343,736
Mortgage-backed securities	13,490	13,813
	$ 364,280	$ 357,549

Major categories of investment income for the years ended December 31 are summarized as follows:

	2008	2007	2006
Fixed maturities	**$ 14,417**	$ 14,329	$ 12,511
Equity securities	**1,712**	1,866	1,719
Money market funds	**1,332**	2,613	3,882
Short-term and other	**1,649**	2,602	3,087
	19,110	21,410	21,199
Investment expenses	**(2,047)**	(1,815)	(1,651)
Net investment income	**$ 17,063**	$ 19,595	$ 19,548

The summarized financial information of the significant limited partnership investment as of and for the years ended December 31 is as follows:

	2008	2007	2006
Fixed maturities:			
Gross gains	**$ 3,333**	$ 536	$ 157
Gross losses	**(6,806)**	(680)	(714)
Net gains (losses)	**(3,473)**	(144)	(557)
Equity securities:			
Gross gains	**4,463**	19,293	10,226
Gross losses	**(12,943)**	(2,483)	(3,795)
Net gains (losses)	**(8,480)**	16,810	6,431
Limited partnerships - net gain (loss)	**(33,562)**	23,141	11,190
Other - net gain (loss)	**(2,234)**	289	—
Total net gains (losses)	**$ (47,749)**	$ 40,096	$ 17,064

Note B - Investments (continued)

The 2008 net losses from limited partnerships, as shown in the previous table, include approximately $37,000 of unrealized losses as reported in the net loss of the various partnerships. Shareholders' equity includes approximately $8,000, net of deferred federal income taxes, of earnings yet undistributed by limited partnerships as of December 31, 2008.

Gain and loss activity for fixed maturity and equity security investments, as shown in the previous table, include adjustments for other-than-temporary impairment for the years ended December 31 and is summarized as follows:

	2008	2007	2006
Cumulative charges to income at beginning of year	**$ 2,734**	$ 3,717	$ 5,070
Writedowns based on objective criteria	**11,881**	593	1,423
Recovery of prior writedowns upon sale or disposal	**(2,917)**	(1,576)	(2,776)
Cumulative charges to income at end of year	**$ 11,698**	$ 2,734	$ 3,717
Net pre-tax realized gain (loss)	**($ 8,964)**	$ 983	$ 1,353
Addition (reduction) to earnings per share from net pre-tax realized gain (loss)	**($ .39)**	$ .04	$ .06
Unrealized gain on investments previously written down at end of the year - see note below	**$ 7,211**	$ 4,878	$ 6,428

Note: Recovery in market value of an investment which has previously been adjusted for other-than-temporary impairment is treated as an unrealized gain until the investment is disposed of.

There is no primary or secondary market for the Company's investments in limited partnerships and, in most cases, the Company is prohibited from disposing of its limited partnership interests for some period of time and must seek approval from the general partner for any such disposal. Distributions of earnings from these partnerships are largely at the sole discretion of the general partners and distributions are generally not received by the Company for many years after the earnings have been reported. The Company has commitments to contribute an additional $2,500 to various limited partnerships as of December 31, 2008.

The Company has invested a total of $24,000 in three limited partnerships, with an aggregate estimated market value of $29,878 at December 31, 2008, that are managed by organizations in which two directors of the Company are executive officers, directors and owners. The Company's ownership interest in these limited partnerships ranges from 3% to 24%. These limited partnerships added $28,502, net of fees, to investment losses in 2008, and $19,177 and $7,942, net of fees, to investment gains in 2007 and 2006, respectively. During 2008, 2007 and 2006, the Company has recorded management fees of $781, $765 and $604, respectively, and performance-based fees of $0, $4,902 and $1,587, respectively, to these organizations for management of these limited partnerships. The Company has been informed that the fee rates applied to its investments in these limited partnerships are the same as, or lower than, the fee rates charged to unaffiliated customers for similar investments.

The Company utilized the services of a broker-dealer firm of which a director of the Company is an executive officer and owner. This broker-dealer serves as agent for purchases and sales of securities and manages an equity securities portfolio and fixed maturity portfolio with market values of approximately $1,865 and $17,467, respectively, at December 31, 2008. The Company has been informed that commission and management rates charged by this broker-dealer to the Company are commensurate with rates charged to non-affiliated customers for similar investments. Total commissions and fees earned by the broker-dealer and affiliates on these transactions and for advice and consulting were approximately $171, $170 and $148 during 2008, 2007 and 2006, respectively.

The fair value of regulatory deposits with various insurance departments in the United States and Canada totaled $26,023 at December 31, 2008.

Short-term investments at December 31, 2008 include $3,000 in foreign time certificates of deposit.

The Company's limited partnerships include one significant investment accounted for using the equity method. This limited partnership investment's value as of December 31, 2008 and 2007 was $18,761 and $44,716, respectively. At December 31, 2008, the Company's estimated ownership interest in this limited partnership investment was less than 4%.

Note B - Investments (continued)

The Company's share of earnings from this limited partnership investment was as follows for the years ended December 31:

	2008	2007	2006
Estimated realized income	**$ 670**	$ 4,241	$ 971
Estimated unrealized income (loss)	**(26,625)**	12,983	5,566
Net earnings (losses)	**$ (25,955)**	$ 17,224	$ 6,537

The summarized financial information of the significant limited partnership investment as of and for the years ended December 31 is as follows:

	2008	2007
Total assets	**$ 582,920**	$1,466,882
Total partners' capital	**550,840**	1,389,232
Net increase (decrease) in partners' capital resulting from operations	**(858,680)**	666,966

Note C - Loss and Loss Expense Reserves

Activity in the reserves for losses and loss expenses is summarized as follows. All amounts are shown net of reinsurance, unless otherwise indicated for the years ended December 31:

	2008	2007	2006
Reserves at the beginning of the year	**$ 244,500**	$249,495	$242,130
Provision for losses and loss expenses:			
Claims occurring during the current year	**132,829**	129,065	129,551
Claims occurring during prior years	**(17,077)**	(21,284)	(16,947)
Total incurred	**115,752**	107,781	112,604
Loss and loss expense payments:			
Claims occurring during the current year	**51,649**	53,820	45,658
Claims occurring during prior years	**76,970**	58,956	59,581
Total paid	**128,619**	112,776	105,239
Reserves at the end of the year	**231,633**	244,500	249,495
Reinsurance recoverable on unpaid losses at the end of the year	**157,925**	134,116	159,917
Reserves, gross of reinsurance recoverable, at the end of the year	**$389,558**	$378,616	$409,412

The table above shows that a savings of $17,077 developed during 2008 in the settlement of claims occurring on or before December 31, 2007, with similar savings developed during the prior two calendar years on losses occurring on or before years ended December 31, 2006 and 2005. These savings are the result of the settlement of claims at amounts lower than previously reserved and changes in estimates of losses incurred but not reported as part of the normal reserving process.

Note C - Loss and Loss Expense Reserves (continued)

The major components of the developments shown in the previous table are as follows for the years ended December 31:

	2008	2007	2006
Retrospectively-rated direct business	**$ 336**	$ (1,078)	$ (7,171)
Other direct business	**(17,177)**	(16,038)	(7,955)
Reinsurance assumed	**(205)**	(4,112)	(1,288)
Involuntary residual markets	**(31)**	(56)	(533)
Totals	**$ (17,077)**	$ (21,284)	$ (16,947)

Favorable loss development is influenced by the Company's long-standing policy of reserving for losses realistically and a willingness to settle claims based upon a seasoned evaluation of its exposures. Reserve savings developed related to retrospectively-rated business resulted in the concurrent recording of return premiums of approximately $662 and $4,738 for the years ended December 31, 2007 and 2006, respectively. Conversely, the deficiency on retrospectively-rated business recorded in 2008 related to approximately $100 of additional premium. As more fully discussed in Note D, the Company increased its per occurrence retention of risk related to transportation liability business during the period 2001 to 2006. The increased net retention per occurrence is reflected in the increasingly favorable developments on other direct business during 2008, 2007 and 2006. These trends were considered in the establishment of the Company's reserves at December 31, 2008 and 2007.

The Company has not changed its original estimate for the loss sustained as a result of the terrorist attacks of September 11, 2001. Therefore, there is no impact on the loss developments shown in the above table except for payments against the original established reserves. The Company has paid $11.1 million to date and carries a remaining reserve of $8.9 million at December 31, 2008.

The Company participates in mandatory residual market pools in various states. The Company records the results from participation in these pools as the information is reported to the Company and also records an additional provision in the financial statements for operating periods unreported by the pools.

Loss reserves on certain permanent total disability workers' compensation reserves have been discounted to present value at pre-tax rates not exceeding 3.5%. At December 31, 2008 and 2007, loss reserves have been reduced by approximately $5,342 and $5,591, respectively. Discounting is applied to these claims since the amount of periodic payments to be made during the lifetime of claimants is fixed and determinable.

Loss reserves have been reduced by estimated salvage and subrogation recoverable of approximately $5,119 and $4,069 at December 31, 2008 and 2007, respectively.

Note D – Reinsurance

The insurance subsidiaries cede portions of their gross premiums written to certain other insurers under excess and quota share treaties and by facultative placements. Risks are reinsured with other companies to permit the recovery of a portion of related direct losses. Management determines the amount of net exposure it is willing to accept generally on a product line basis. Certain treaties covering fleet transportation include annual deductibles which must be exceeded before the Company can recover under the terms of the treaty. In these cases, the Company retains a higher percentage of the direct premium in consideration of the deductible provisions. The Company remains liable to the extent the reinsuring companies are unable to meet their obligations under reinsurance contracts.

The Company also serves as an assuming reinsurer on treaties with direct writing insurance companies for catastrophic property coverages as well as under retrocessions from certain other reinsurers. The retrocessions include individual risks but are comprised primarily of high layer catastrophe treaties. Accordingly, the occurrence of catastrophic events can have a significant impact on the Company's operations. In addition, the insurance subsidiaries participate in certain involuntary reinsurance pools which require insurance companies to provide coverages on assigned risks. The assigned risk pools allocate participation to all insurers based upon each insurer's portion of premium writings on a state or national level. Historically, the operation of these assigned risk pools have resulted in net losses allocated to the Company although such losses have generally not been material in relation to the Company's direct and voluntary assumed operations.

Note D - Reinsurance (continued)

The following table summarizes the magnitude of reinsurance ceded and assumed on the Company's net premium written and earned for the most recent three years:

	Premiums Written			Premiums Earned		
	2008	2007	2006	**2008**	2007	2006
Direct	**$ 182,810**	$ 176,233	$ 184,538	**$ 188,285**	$ 185,781	$ 182,077
Ceded on direct	**(39,828)**	(32,980)	(24,836)	**(41,214)**	(35,294)	(27,320)
Net on direct	**142,982**	143,253	159,702	**147,071**	150,487	154,757
Assumed	**39,132**	31,134	12,526	**40,528**	33,378	15,009
Ceded on assumed	**(5,300)**	(4,800)	—	**(5,300)**	(4,800)	—
Net on assumed	**33,832**	26,334	12,526	**35,228**	28,578	15,009
Net	**$ 176,814**	$ 169,587	$ 172,228	**$ 182,299**	$ 179,065	$ 169,766

Net losses and loss expenses incurred for 2008, 2007 and 2006 have been reduced by ceded reinsurance recoveries of approximately $53,398, $4,981 and $14,026, respectively. The increase in 2008 recoveries is a result of the Company having reached its annual aggregate deductible on one of its reinsurance treaties. Ceded reinsurance premiums and loss recoveries for catastrophe reinsurance contracts were not material.

Net losses and loss expenses incurred for 2008, 2007 and 2006 include approximately $22,003, $14,638 and $2,623, respectively, relating to property reinsurance from non-affiliated insurance or reinsurance companies, including involuntary residual market pools. The assumed reinsurance losses in 2008 and 2007 reflect an overall increase in the Company's reinsurance assumed portfolio.

Components of reinsurance recoverable at December 31 are as follows:

	2008	2007
Unpaid losses and loss expenses, net of valuation allowance	**$ 155,455**	$ 131,727
Paid losses and loss expenses	**4,531**	1,079
Unearned premiums	**3**	5
	$ 159,989	$ 132,811

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Note E - Income Taxes

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred tax assets and liabilities as of December 31 are as follows:

	2008	2007
Deferred tax liabilities:		
Unrealized gain on fixed income and equity security investments	**$ 10,450**	$ 19,856
Limited partnership investments	**—**	10,632
Deferred acquisition costs	**814**	1,118
Other	**1,891**	1,562
Total deferred tax liabilities	**13,155**	33,168
Deferred tax assets:		
Loss and loss expense reserves	**15,575**	17,755
Limited partnership investments	**2,420**	—
Unearned premiums discount	**1,203**	1,587
Other-than-temporary investment declines	**4,094**	957
Deferred compensation	**228**	1,540
Other	**225**	211
Total deferred tax assets	**23,745**	22,050
Net deferred tax assets (liabilities)	**$ 10,590**	$ (11,118)

A summary of the difference between federal income tax expense computed at the statutory rate and that reported in the consolidated financial statements is as follows:

	2008	2007	2006
Statutory federal income rate applied to pretax income (loss)	**$ (6,090)**	$ 27,878	$ 18,553
Tax effect of (deduction):			
Tax-exempt investment income	**(3,649)**	(3,298)	(2,313)
Net addition to (reduction of) tax positions	**(192)**	125	(1,617)
Other	**245**	(184)	202
Federal income tax expense (benefit)	**$ (9,686)**	$ 24,521	$ 14,825

Federal income tax expense consists of the following:

	2008	2007	2006
Taxes (credits) on pre-tax income (loss):			
Current	**$ 4,443**	$ 18,901	$ 12,603
Deferred	**(14,129)**	5,620	2,222
	$ (9,686)	$ 24,521	$ 14,825

Note E - Income Taxes (continued)

The components of the provision for deferred federal income taxes (credits) are as follows:

	2008	2007	2006
Limited partnerships	**$ (13,052)**	$ 5,354	$ 1,871
Discounts of loss and loss expense reserves	**354**	32	92
Unearned premium discount	**384**	663	(172)
Deferred compensation	**1,310**	(508)	(149)
Other-than-temporary investment declines	**(3,137)**	344	474
Other	**12**	(265)	106
Provision for deferred federal income tax	**$ (14,129)**	$ 5,620	$ 2,222

Cash flows related to federal income taxes paid, net of refunds received, for 2008, 2007 and 2006 were $11,186, $14,502 and $16,097, respectively.

The Company is required to establish a valuation allowance for any portion of the gross deferred tax asset that management believes will not be realized. Management has determined that no such valuation allowance is necessary at December 31, 2008. As of December 31, 2008, the Internal Revenue Service had completed examinations and settled all audits through the Company's 2004 tax year.

Financial Accounting Standards Board Interpretation (FIN) No. 48, *Accounting for Uncertainty in Income Taxes — an Interpretation of FASB Statement No. 109,* provides guidance for recognizing and measuring uncertain tax positions, as defined in SFAS No. 109, *Accounting for Income Taxes*. The Company adopted FIN 48 on January 1, 2007 with no adjustment necessary to beginning retained earnings. The total amount of unrecognized tax benefits from uncertain tax positions at January 1, 2007 was $10,301. The tax positions are uncertain as to the timing of deductibility and therefore, if recognized would have no impact on the Company's effective tax rate.

The Company recognizes accrued interest and penalties, if any, related to unrecognized tax benefits in income tax expense and changes in such accruals would impact the Company's effective tax rate. Amounts accrued for the payment of interest at December 31, 2008 and December 31, 2007 were not material.

A reconciliation of the beginning and ending amounts of unrecognized federal income taxes (credits) are as follows:

	2008	2007
Balance at January 1	**$ 7,781**	$ 10,301
Reductions for tax positions of the current year	**(271)**	(142)
Reductions for tax positions of prior years	**(1,441)**	(2,378)
Settlements with tax authorities	**(114)**	—
Balance at December 31	**$ 5,955**	$ 7,781

Note F - Shareholders' Equity

Changes in common stock outstanding and additional paid-in capital are as follows:

	Class A		Class B		Additional Paid-in Capital
	Shares	Amount	Shares	Amount	
Balance at January 1, 2006	2,666,666	$ 114	12,135,671	$ 518	$ 38,894
Stock options issued	—	—	—	—	20
Stock options exercised	—	—	349,534	15	6,789
Treasury shares purchased	(16,607)	(1)	—	—	(11)
Balance at December 31, 2006	2,650,059	113	12,485,205	533	45,692
Stock options exercised	—	—	107,350	4	2,207
Balance at December 31, 2007	2,650,059	113	12,592,555	537	47,899
Treasury shares purchased	(26,950)	(1)	(429,304)	(18)	(1,587)
Balance at December 31, 2008	2,623,109	$ 112	12,163,251	$ 519	$ 46,312

The Company's Class A and Class B common stock has a stated value of approximately $.04 per share.

Shareholders' equity at December 31, 2008 includes $330,677 representing GAAP shareholder's equity of insurance subsidiaries, of which $39,803 may be transferred by dividend or loan to the parent company during calendar year 2009 with proper notification to, but without approval from, regulatory authorities. An additional $204,135 of shareholder's equity of such insurance subsidiaries may be advanced or loaned to the parent company with prior notification to and approval from regulatory authorities.

Note G - Other Operating Expenses

Details of other operating expenses for the years ended December 31:

	2008	2007	2006
Amortization of deferred policy acquisition costs	**$ 23,437**	$ 20,985	$ 14,155
Other underwriting expenses	**19,745**	21,688	18,789
Expense allowances from reinsurers	**(3,084)**	(2,044)	(1,205)
Total underwriting expenses	**40,098**	40,629	31,739
Operating expenses of non-insurance companies	**18,479**	15,701	15,716
Total other operating expenses	**$ 58,577**	$ 56,330	$ 47,455

Note H - Employee Benefit Plans

The Company maintains a defined contribution 401(k) Employee Savings and Profit Sharing Plan ("the Plan") which covers nearly all employees who have completed one year of service. The Company's contributions to the Plan for 2008, 2007 and 2006 were $1,183, $1,132, and $1,137, respectively.

Note I - Stock Purchase and Option Plans

In accordance with the terms of the 1981 Stock Purchase Plan (1981 Plan), the Company is obligated to repurchase shares issued under the 1981 Plan, at a price equal to 90% of the book value of the shares at the end of the quarter immediately preceding the date of repurchase. No shares have ever been repurchased under the 1981 Plan. At December 31, 2008 there were 124,379 shares (Class A) and 380,833 shares (Class B) outstanding which are eligible for repurchase by the Company.

Note I - Stock Purchase and Option Plans (continued)

The Company maintains two stock option plans which are described below. Compensation cost charged against income for those plans was $0, $0, and $20, for 2008, 2007, and 2006, respectively.

Director Option Plan:

Under the Director Option Plan (the Director Plan), which is shareholder approved, the Company has reserved 300,000 shares of Class B common stock for the granting of discounted and market value options to non-employee directors. Approximately 167,000 shares of Class B common stock are available for future grants. No options were granted to directors during 2008 and 2007. Additionally, no discounted options were outstanding at December 31, 2008 and 2007. Prior to May, 2005, discounted options were granted to non-employee directors in lieu of cash directors' fees. During 2006, all market value options were terminated, without compensation to the directors, and all subsequent directors' fees have been paid in cash. The total intrinsic value of options exercised during 2006 was $484. No options were outstanding or exercised during 2007 or 2008.

Employee Option Plan:

Under the Employee Option Plan (the Employee Plan), which is shareholder approved, the Company has reserved 1,125,000 shares of Class B common stock for the granting of discounted and market value options to employees. Approximately 259,000 shares of Class B common stock are available for future grants. No options were granted to employees during the three year period ended December 31, 2008 and no options remained outstanding at December 31, 2008 and 2007. Additionally, there were no option exercises during 2008. During 2007 and 2006, all options were exercised at $20.60 per share. The total intrinsic value of options exercised during 2007 and 2006 was $722 and $1,684, respectively. No options were outstanding or exercised during 2008.

Cash received from option exercise under all share-based payment arrangements for the years ended December 31, 2007 and 2006 was $2,211, and 6,804, respectively. The federal tax benefit realized for the tax deductions from option exercise of the share-based payment arrangements totaled $253 and $759, respectively, for the years ended December 31, 2007 and 2006. Under the terms of the Employee Plan, $253 and $589, respectively, of tax benefits realized were passed on to employees in the form of cash for the years ended December 31, 2007 and 2006.

The Company's policy is to issue new shares to satisfy share option exercises.

During 2002 and 2001, the Company offered loans to certain employees for the sole purpose of purchasing the Company's Class B common stock in the open market. Principal and interest totaling $2,199 and $2,228 relating to such loans was outstanding at December 31, 2008 and 2007, respectively. Loans carry interest rates ranging from 4.75% to 6%, payable annually. The underlying securities, with value in excess of the related debt, serve as collateral for these full-recourse loans, which must be repaid no later than 10 years from the date of issue. This loan program was terminated in 2002.

Note J - Reportable Segments

The Company has two reportable business segments in its operations: property and casualty insurance and property reinsurance. Previously, the Company had four reportable business segments: fleet trucking, small fleet trucking, private passenger automobile and reinsurance assumed. As of July 1, 2008, the Company completed a restructuring of internal product management whereby divisions, which constituted the previously reported segments other than reinsurance assumed, were eliminated and all functional operations of the Company were vertically integrated. As such, the management of all directly produced property and casualty insurance business is managed as a single segment. Accordingly, the Company has revised its operating segments to reflect the new management structure for all periods presented. Management believes this segment structure better reflects the current operations and future business plan of the Company. Amounts applicable to the historical fleet trucking, small fleet trucking, private passenger automobile segments as well as the all other category, consisting of residual market assignments and discontinued products, for the current and prior periods have been reclassified into the property and casualty insurance segment. The property and casualty insurance segment provides multiple line insurance coverage primarily to fleet transportation companies as well as to independent contractors who contract with fleet transportation companies. In addition, personal automobile products are provided to individuals. The property reinsurance segment, formerly known as reinsurance assumed accepts cessions from other insurance companies as well as retrocessions from selected reinsurance companies, principally reinsuring against catastrophes.

Note J - Reportable Segments (continued)

The Company evaluates performance and allocates resources based on past or expected results from insurance underwriting operations before income taxes. Underwriting gain or loss does not include net investment income or gains or losses on the Company's investment portfolio. All investment-related revenues are managed at the corporate level. Underwriting gain or loss for the property and casualty insurance segment includes revenue and expense from the Company's agency operations since the agency operations serve as a primary direct marketing facility for this segment. Management does not identify or allocate assets to reportable segments when evaluating segment performance and depreciation expense is not material for any of the reportable segments. The accounting policies of each reportable segment are the same as those described in the summary of significant accounting policies.

The following table provides certain profit and loss information for each reportable segment for the years ended December 31:

	2008	2007	2006
Direct and assumed premium written:			
Property and casualty insurance	**$ 182,810**	$ 176,233	$ 184,338
Property reinsurance	**39,132**	31,134	12,726
Totals	**$ 221,942**	$ 207,367	$ 197,064
Net premium earned:			
Property and casualty insurance	**$147,071**	$ 150,487	$ 154,757
Property reinsurance	**35,228**	28,578	15,009
Totals	**$ 182,299**	$ 179,065	$ 169,766
Underwriting gain (loss)			
Property and casualty insurance	**$20,022**	$ 26,654	$ 19,452
Property reinsurance	**6,718**	5,554	6,933
Totals	**$ 26,740**	$ 32,208	$ 26,385

The following table reconciles reportable segment profits to the Company's consolidated income (loss) before federal income taxes:

	2008	2007	2006
Profit:			
Underwriting gain	**$ 26,740**	$ 32,208	$ 26,385
Net investment income	**17,063**	19,595	19,548
Net realized gains (losses) on investments	**(47,749)**	40,096	17,064
Corporate expenses	**(13,453)**	(12,247)	(9,987)
Income before federal income taxes	**$ (17,399)**	$ 79,652	$ 53,010

The Company, through its subsidiaries, is licensed to do business in all 50 states of the United States, all Canadian provinces and Bermuda. Canadian and Bermuda operations are currently not significant.

One customer of the property and casualty insurance segment represents approximately $13,773, $13,772 and $69,636 of the Company's consolidated direct and assumed premium written in 2008, 2007 and 2006, respectively. An additional $99,589, $80,080 and $0 for 2008, 2007 and 2006, respectively, is placed with the Company by a non-affiliated broker on behalf of this same customer.

Note K - Earnings Per Share

The following is a reconciliation of the denominators used in the calculation of basic and diluted earnings per share for the years ended December 31:

	2008	2007	2006
Average share outstanding for basic earnings per share	**15,080,149**	15,175,074	15,004,377
Dilutive effect of options	**—**	14,269	43,094
Average shares outstanding for diluted earnings per share	**15,080,149**	15,189,343	15,047,471

Note L - Concentrations of Credit Risk

The Company writes policies of excess insurance attaching above a self-insured retention ("SIR") and also writes policies that contain large, per-claim deductibles. Those losses and claims that fall within the SIR or deductible are obligations of the insured. The Company also writes surety bonds in favor of various regulatory agencies guaranteeing the insured's payment of claims within the SIR. Losses and claims under a large deductible policy are payable by the Company with reimbursement due the Company from the insured. The Company requires collateral from its insureds to serve as a source of reimbursement if the Company is obligated to pay claims within the SIR by reason of an insured's default or if the insured fails to reimburse the Company for deductible amounts paid by the Company.

Acceptable collateral may be provided in the form of letters of credit on Company approved banks, Company approved marketable securities or cash. At December 31, 2008, the Company held collateral in the aggregate amount of $214,264.

The amount of collateral required of an insured is determined by the financial condition of the insured, the type of obligations guaranteed by the Company, estimated reserves for incurred losses within the SIR or deductible that have been reported to the insured or the Company, estimated incurred but not reported losses, and estimates for losses that are expected to occur, within the SIR or deductible, prior to the next collateral adjustment date. In general, the Company attempts to hold collateral equal to 100% of the ultimate losses that would be paid by or due the Company in the event of the insured's default. Periodic audits are conducted by the Company to evaluate its exposure and the collateral required. If a deficiency in collateral is noted as the result of an audit, additional collateral is requested immediately. Because collateral amounts contain numerous estimates of the Company's exposure, are adjusted only periodically and are sometimes adjusted based on the financial condition of the insured, the amount of collateral held by the Company at a given point in time may not be sufficient to fully reimburse the Company for all of its guarantees or amounts due in the event of an insured's default. Further, the Company is not fully collateralized for the guarantees made for, or the deductible amounts that may be due from, the Company's largest customer, and in the event of that customer's default, such default may have a material adverse impact on the Company. The Company estimates its uncollateralized exposure related to this Fortune 500 company to be as much as 32% of shareholders' equity at December 31, 2008.

In addition, the Company's balance sheet includes paid and unpaid amounts recoverable from reinsurers under various agreements totaling $159,989 at December 31, 2008, as more fully discussed in Note D - Reinsurance. With minor exception, these recoverables are uncollateralized. The three largest estimated amounts due from individual reinsurers were $23,773, $18,631 and $18,083 at December 31, 2008. Included in the total recoverable amount are case basis and estimated IBNR losses of approximately $6,907 due from Converium Insurance (North America) Inc., which reported substantial reserve strengthening and/or impairment of assets in 2005 which have negatively affected their reported financial position. All amounts due from this reinsurer on paid claims as of December 31, 2008 are current and the Company has no information at this time to indicate that all obligations of this reinsurer will not be met.

Investments in limited partnerships include an aggregate of $29,878 invested in three related partnerships, New Vernon India Fund, New Vernon Global Opportunity Fund and New Vernon North American Opportunity Fund.

Note M – Acquisition and related Goodwill and Intangibles

On October 31, 2008, the Company purchased Transportation Specialty Insurance Agency, Inc., ("TIA") of Toledo, Ohio for a cash purchase price of $3,500 which includes a post closing purchase price adjustment related to minimum working capital requirements. TIA is a commercial lines specialty insurance agency primarily focusing on the needs of the transportation industry including trucking independent contractors as well as fleet trucking companies. TIA is part of the Company's property and casualty insurance segment and is not expected to have any material effect on results of operations, liquidity or capital resources. As part of the purchase, the Company recorded goodwill of $3,221 and intangible assets related to customer relationships and employment agreements of $179 with are included in Other Assets in the consolidated balance sheet. During 2008, the Company had amortization of intangible assets of $8. The Company had no goodwill, intangible assets and related amortization prior to 2008.

Note N – Debt

The Company has $9,000 outstanding as of December 31, 2008 under the Company's revolving line of credit at variable interest rates detailed below. No borrowings were outstanding against this line at December 31, 2007. The Company has $11,000 remaining unused under the revolving line of credit. The $9,000 of borrowings was used principally for treasury stock repurchases.

Description	Maturity	2008	2007	Interest Rate
Revolving line of credit	June 23, 2011	$ 5,000,000	$ —	0.97%
Revolving line of credit	June 23, 2011	4,000,000	—	4.03%
	Total Debt	$ 9,000,000	$ —	

Note O – Fair Value

In September 2006, the Financial Accounting Standards Board issued Statement No. 157, *Fair Value Measurements* ("SFAS No. 157"), which provides a common definition of fair value and establishes a framework to make the measurement of fair value more consistent and comparable. SFAS No. 157 also requires expanded disclosures about (1) the extent to which companies measure assets and liabilities at fair value, (2) the methods and assumptions used to measure fair value and (3) the effect of fair value measures on earnings. The Company adopted SFAS 157, effective January 1, 2008 for financial assets and liabilities. The FASB has deferred the implementation of the provisions of SFAS 157 relating to certain nonfinancial assets and liabilities until January 1, 2009. SFAS 157 did not have a significant impact on the Company's consolidated financial condition or results of operations.

Beginning January 1, 2008, assets and liabilities recorded at fair value in the consolidated balance sheets are categorized based upon the level of judgment associated with the inputs used to measure their fair value.

The following table summarizes fair value measurements by level at December 31, 2008 for assets measured at fair value on a recurring basis:

Description	Total	Level 1	Level 2	Level 3
Fixed maturities	$ 364,280	$ —	$ 364,280	$ —
Equity securities	63,200	63,200	—	—
Short term	33,820	2,964	30,856	—
Cash equivalents	24,327	—	24,327	—
	$ 485,627	$ 66,164	$ 419,463	$ —

Note O - Fair Value (continued)

Level inputs, as defined by SFAS No. 157, are as follows:

Level Input:	Input Definition:
Level 1	Inputs are unadjusted, quoted prices for identical assets or liabilities in active markets at the measurement date.
Level 2	Inputs other than quoted prices included in Level 1 that are observable for the asset or liability through corroboration with market data at the measurement date.
Level 3	Unobservable inputs that reflect management's best estimate of what market participants would use in pricing the asset or liability at the measurement date.

A reconciliation of the beginning and ending balances of assets measured at fair value on a recurring basis using Level 3 inputs is as follows for the year ended December 31:

	2008
Beginning of period	$ —
Total gain or losses (realized or unrealized)	
Included in earnings (or changes in net assets)	(2,234)
Included in other comprehensive income	—
Purchases, issuances, and settlements	2,234
Transfers in and/or out of Level 3	—
End of period	$ —

In February 2007, the Financial Accounting Standards Board issued Statement No. 159, *The Fair Value Option for Financial Assets and Liabilities — Including an Amendment of FASB Statement No. 115*, to permit an entity to choose to measure many financial instruments and certain other items at fair value. Most of the provisions in SFAS No. 159 are elective; however the amendment to SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities," applies to all entities with available-for-sale and trading securities. The fair value option permits all entities to choose to measure eligible items at fair value at specified election dates. The fair value option may be applied on an instrument-by-instrument basis, is irrevocable and is to be applied to entire instruments and not portions thereof. The Company did not elect the fair value option. SFAS No. 159 did not have a significant impact on the Company's consolidated financial condition or results of operations.

Note P - New Accounting Pronouncements

In December 2007, Financial Accounting Standards Board issued Statement No. 141 (revised 2007), *Business Combinations* ("SFAS No. 141(R)"). SFAS No. 141(R) changes the requirements for an acquirer's recognition and measurement of the assets acquired and the liabilities assumed in a business combination. SFAS No. 141(R) is effective for annual periods beginning after December 15, 2008 and should be applied prospectively for all business combinations entered into after the date of adoption. SFAS 141(R) is not expected to have a significant impact on the Company's consolidated financial condition or results of operations.

Note Q - Quarterly Results of Operations (Unaudited)

Quarterly results of operations are as follows:

	Results by Quarter							
	2008				2007			
	1st	**2nd**	**3rd**	**4th**	1st	2nd	3rd	4th
Net premiums earned	**$ 45,087**	**$ 46,902**	**$ 43,579**	**$ 46,730**	$ 44,175	$ 44,817	$ 44,601	$ 45,472
Net investment income	**4,200**	**4,195**	**4,372**	**4,296**	4,846	4,882	5,040	4,827
Net gains (losses) on investments	**(13,575)**	**(2,960)**	**(15,965)**	**(15,249)**	474	8,772	6,421	24,429
Losses and loss expenses incurred	**29,461**	**26,462**	**30,427**	**29,402**	26,892	24,493	24,949	31,447
Net income (loss)	**(4,608)**	**6,307**	**(7,270)**	**(2,142)**	8,211	14,792	11,714	20,414
Per share - diluted:								
Income before net gains (losses) on investments	**$ .28**	**$ .54**	**$ .21**	**$ .52**	$ .52	$ .60	$ .50	$ .30
Net gains (losses) on investments	**(.58)**	**(.13)**	**(.69)**	**(.66)**	.02	.38	.27	1.04
Net income (loss)	**$ (.30)**	**$ .41**	**$ (.48)**	**$ (.14)**	$ .54	$ .98	$ .77	$ 1.34

Note R - Statutory (Unaudited)

Net income of the insurance subsidiaries, as determined in accordance with statutory accounting practices, was $19,064, $35,605 and $26,632 for 2008, 2007 and 2006, respectively. Consolidated statutory surplus for these subsidiaries was $315,529 and $360,965 at December 31, 2008 and 2007, respectively.

Minimum statutory surplus necessary for the insurance subsidiaries to satisfy statutory risk based capital requirements was $86,739 at December 31, 2008.

Directors

Stuart D. Bilton
Chairman
Aston Asset Management LLC
Chicago, Illinois

Joseph J. DeVito
President & COO
Baldwin & Lyons, Inc.
President
Protective and Sagamore Insurance Companies

Otto N. Frenzel IV
Chairman
The Symphony Bank
Indianapolis, Indiana

Gary W. Miller
Chairman & CEO
Baldwin & Lyons, Inc.

John M. O'Mara
Business Consultant & Private Investor
Greenwich, Connecticut

Thomas H. Patrick
Principal & Co-owner
New Vernon Capital LLC
Chicago, Illinois

John A. Pigott
Vice Chairman (retired)
Anixter, Inc.
Winnetka, Illinois

Kenneth D. Sacks
Chairman & Executive Vice President
JMB Insurance, Inc.
Chicago, Illinois

Nathan Shapiro
President
S F Investments, Inc.
Chicago, Illinois

Norton Shapiro
Personal Investments
Chicago, Illinois

Robert Shapiro
President & CEO
Emlin Cosmetics
Chicago, Illinois

Steven A. Shapiro
Investment Manager
S F Investments, Inc.
Chicago, Illinois

John D. Weil
President
Clayton Management Co.
St. Louis, Missouri

Officers

Gary W. Miller
Chairman & CEO

Joseph J. DeVito
President & COO

G. Patrick Corydon
Executive Vice President & CFO

Mark L. Bonini
Vice President (Sales)

James D. Isham
Vice President (Administration)

Jennie L. LaReau
Vice President (Underwriting)

John E. Mitchell
Vice President (Reinsurance & Actuarial Services)

Craig C. Morfas
Vice President (Claims)
General Counsel & Secretary

Walter D. Osborne
Treasurer

Corporate Data

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Subsidiaries
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1099 N. Meridian Street
Indianapolis, Indiana 46204

Sagamore Insurance Company
1099 N. Meridian Street
Indianapolis, Indiana 46204
Internet: www.sagamoreinsurance.com

B & L Insurance, Ltd.
Windsor Place
18 Queen Street
Hamilton, Bermuda

Availability of Form 10-K
The Company's 2008 annual report filed with the Securities and Exchange Commission on Form 10-K and the Company's Code of Conduct will be sent to shareholders without charge upon written request to the Investor Contact at the corporate address. These documents, along with all other filings with the Securities and Exchange Commission, are available for review, download or printing from the Company's web site.

Notice of Annual Meeting
10:00 a.m. May 5, 2009
Landmark Center
Lower Level
1099 N. Meridian Street
Indianapolis, Indiana 46204

Transfer Agent and Registrar
National City Bank
Cleveland, Ohio

Investor Contact
G. Patrick Corydon
corydon@baldwinandlyons.com
Fax (317) 715-9610

Common Stock Structure
The Class A and Class B common shares have identical rights and privileges except that Class B shares have no voting rights other than on matters for which Indiana law requires class voting.

Dividends
Cash dividends have been paid quarterly since 1974. The two classes of common stock have identical dividend rights. The current regular quarterly dividend rate is $.25 per share.

Independent Auditors
Ernst & Young LLP
Indianapolis, Indiana