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The Progressive Corporation 2008 Annual Report

the unimaginable

The Progressive Group of Insurance Companies, in business since 1937, is one of the country's largest auto insurance groups, the largest seller of motorcycle policies and a market leader in commercial auto insurance based on premiums written. Progressive is committed to becoming consumers' #1 choice for auto insurance by providing competitive rates and innovative products and services that meet drivers' needs throughout their lifetimes, including superior online and in-person customer service, and best-in-class, 24-hour claims service, such as its concierge level of claims service available at service centers located in major metropolitan areas throughout the United States.

Progressive companies offer consumers choices in how to shop for, buy and manage their auto insurance policies. Progressive offers its products, including personal and commercial auto, motorcycle, boat and recreational vehicle insurance, through more than 30,000 independent insurance agencies throughout the U.S. and online and by phone directly from the Company.

By definition, innovation is Progressive. For the theme of this year's annual report, Progressive explores innovation through the eyes of artist Caleb Charland, whose work incorporates everyday objects and fundamental forces to illustrate our shared experience of wonder. Charland's work will join Progressive's growing collection of contemporary art.

Imagine a world where you could name your price for car insurance. That concept is now a reality for people who shop on progressive.com. Name Your Price® is an easy-to-use tool that gives consumers control over the cost of their car insurance. If you tell us that you want to pay $90 per month, we'll search for coverage options that fit your budget.

Five-Year Financial Highlights

(billions—except per share amounts)

	2008	2007	2006	2005	2004
For the Year					
Net premiums written	$ 13.6	$ 13.8	$ 14.1	$ 14.0	$ 13.4
Growth over prior year	(1)%	(3)%	1%	5%	12%
Net premiums earned	$ 13.6	$ 13.9	$ 14.1	$ 13.8	$ 13.2
Growth over prior year	(2)%	(2)%	3%	5%	16%
Total revenues	$ 12.8	$ 14.7	$ 14.8	$ 14.3	$ 13.8
Net income (loss)	$ (.07)	$ 1.18	$ 1.65	$ 1.39	$ 1.65
Per share[1]	$ (.10)	$ 1.65	$ 2.10	$ 1.74	$ 1.91
Underwriting margin	5.4%	7.4%	13.3%	11.9%	14.9%

(billions – except shares outstanding, per share amounts, and policies in force)

	2008	2007	2006	2005	2004
At Year-End					
Common shares outstanding (millions)	676.5	680.2	748.0	789.3	801.6
Book value per share	$ 6.23	$ 7.26	$ 9.15	$ 7.74	$ 6.43
Consolidated shareholders' equity	$ 4.2	$ 4.9	$ 6.8	$ 6.1	$ 5.2
Market capitalization	$ 10.0	$ 13.0	$ 18.1	$ 23.0	$ 17.0
Return on average shareholders' equity	(1.5)%	19.5%	25.3%	25.0%	30.0%
Policies in Force (thousands)					
Personal Lines					
Agency–Auto	4,288.6	4,396.8	4,433.1	4,491.4	4,244.9
Direct–Auto	2,824.0	2,598.5	2,428.5	2,327.7	2,084.1
Special Lines	3,352.3	3,120.3	2,879.5	2,674.9	2,351.3
Total Personal Lines	10,464.9	10,115.6	9,741.1	9,494.0	8,680.3
Growth over prior year	3%	4%	3%	9%	11%
Commercial Auto	539.4	539.2	503.2	468.2	420.2
Growth over prior year	—%	7%	7%	11%	15%
Market share[2]	7.2%	7.3%	7.4%	7.5%	7.3%
Industry net premiums written[3]	$ 159.9	$ 159.1	$ 160.2	$ 159.6	$ 157.3

	1-Year	3-Year	5-Year
Stock Price Depreciation[4]			
Progressive	(21.9)%	(17.3)%	(4.6)%
S&P 500	(36.5)%	(8.3)%	(2.2)%

[1]Since we reported a net loss for 2008, the calculated diluted earnings per share was antidilutive; therefore, basic earnings per share is disclosed. For all other periods, diluted earnings per share is disclosed.

[2]Represents Progressive's personal auto business as a percent of the personal auto insurance market; 2008 is estimated.

[3]Represents personal auto insurance market net premiums written as reported by A.M. Best Company, Inc.; 2008 is estimated.

[4]Represents average annual compounded rate of decrease and assumes dividend reinvestment.

All share and per share amounts were adjusted for the May 18, 2006, 4-for-1 stock split.

Communicating a clear picture of Progressive by stating what we try to achieve (Vision), how we interact with customers (Customer Value Proposition), and what guides our behavior (Core Values) permits all people associated with us to understand what we expect of ourselves and each other and how we conduct our business.

Vision

We seek to be an excellent, innovative, growing, and enduring business by cost-effectively and profitably reducing the human trauma and economic costs of auto accidents and other mishaps, and by building a recognized, trusted, admired, business-generating brand. We seek to maximize shareholder value and to provide a positive environment that attracts quality people who develop and achieve ambitious growth plans.

Customer Value Proposition

Our Customer Value Proposition provides a litmus test for customer interactions and relationships and innovation.

Fast, Fair, Better That's what you can expect from Progressive. Everything we do recognizes the needs of busy consumers, who are cost-conscious, increasingly savvy about insurance, and ready for new, easy ways to quote, buy, and manage their policies, including claims service that respects their time and reduces the trauma and inconvenience of loss.

Core Values

Progressive's Core Values serve as the foundation for our corporate culture. They govern our decisions and define the manner in which we conduct our business and how we interact with all interested parties. We want them understood and embraced by all Progressive people. Growth and change provide new perspective, requiring regular refinement of Core Values.

Integrity We revere honesty. We adhere to the highest ethical standards, provide timely, accurate, and complete financial reporting, encourage disclosing bad news, and welcome disagreement.

Golden Rule We respect all people, value the differences among them, and deal with them in the way we want to be dealt with. This requires us to know ourselves and to try to understand others.

Objectives We strive to communicate clearly Progressive's ambitious objectives and our people's personal and team objectives. We evaluate performance against all these objectives.

Excellence We strive constantly to improve in order to meet and exceed the highest expectations of our customers, agents, shareholders, and people. We teach and encourage our people to improve performance and to reduce the costs of what they do for customers. We base their rewards on results and promotion on ability.

Profit The opportunity to earn a profit is how the competitive free-enterprise system motivates investment to enhance human health and happiness. Profits reflect our customers' and claimants' increasingly positive view of Progressive.

“Good ideas and innovations

must be driven into existence

by courage and patience.”

Admiral Hyman George Rickover

“Creativity
is thinking up
new things.

Innovation
is

doing

new

things.”

Theodore Levitt

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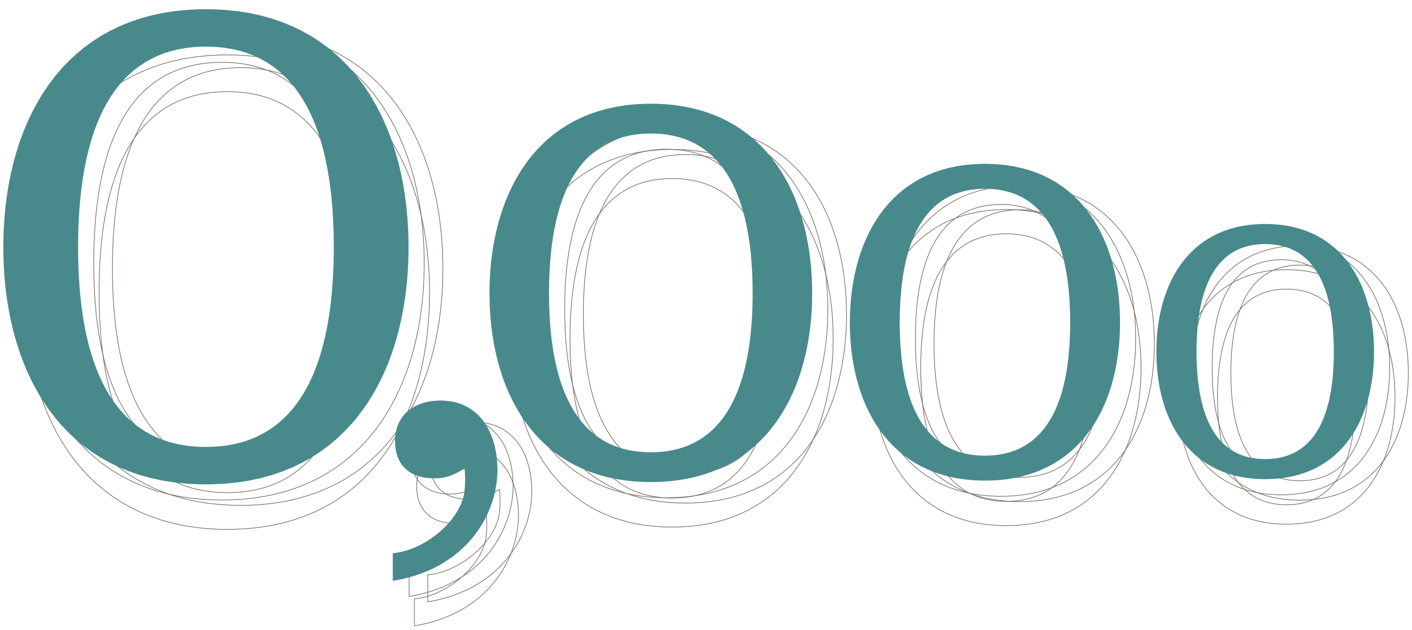
Thanks to the one million Progressive customers who took us up on our offer to go "paperless" and receive their policy documents online. For each one of you, a tree will be planted in a U.S. National Forest. Progressive is funding the planting of these trees through the Arbor Day Foundation.



Wow! Followed by the claim, "I say it louder," was an effective interjection in the debut television commercial of our revamped 2008 advertising efforts, but might equally be used with a less positive tone as a descriptor for the business year in the U.S. 2008 for Progressive had plenty of Wow!, some very positive and encouraging, and some just flat out disappointing.

Reporting a net loss, the first in 26 years, is unquestionably a tough pill to swallow and calls for a clear, open, and objective diagnostic. My tendency is to focus on the actions we most directly control and as such I'll lead off with a high level review of operating results and environment before getting to our investment and capital story which, this year, takes on unprecedented importance.

Writing this time last year, I summarized a prospective view of the auto insurance rate environment as becoming more "normal." A view formed after observing, and participating in, the prior year and a half of widespread rate reductions and the emergence of an increasing rate need to match inflation in claims cost.

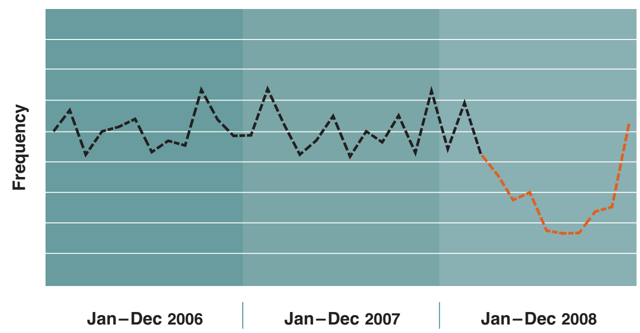
The year started off essentially true to that script. By June the nation was focused on many issues, gas prices being high on the list for most. The implication for our business was a sudden and dramatic reduction in claims frequency. While the change in consumer behavior, which led to fewer miles driven, fewer exposures, and fewer accidents, was a societal positive, it added a level of complexity to those who must price for future conditions, with little precedent for guidance.

Falling frequency and explanatory theories have been a topic in these pages and for many industry commentators throughout the current decade, but the sudden turn in 2008 was an entirely different event. The graph makes the point better than my words.

By later in the year, gas prices were less than half their peaks and one might assume with perfect elasticity of demand all would be as it once was. But, the country was now in an economic tailspin and, at a minimum, consumer uncertainty prevailed. Consumer behavior did not show perfect elasticity and the return to frequency levels of even the first quarter was dampened.

Modeling certain response variables important to us against external data, such as unemployment rates, is critical, but challenging statistically. Rates of uninsured drivers, changes in valuation of vehicles and parts, fleet aging dynamics, bad debt propensity, medical treatment patterns, and the like are all subject to change in the current environment. Our models, while interesting, will never substitute for our ability to observe and respond quickly. Our internal response is to assume change is at an all-time high, be nimble in responding, reduce the time to implement rate change, and assume that with any change we may need to iterate quickly to match the environment.

Progressive: Auto Claim Frequency



Profit

Our 94.6 combined ratio for the year is testament to our responsiveness and respect for the conditions. The result is well in-line with our target of a 96, and needs no qualifying statements regarding prior year development or storm adjustments. 42 of our established 50 states, which includes the District of Columbia, were profitable for the year as were 8 of our largest 10 states, including New York auto, which was a definite concern in 2007. Duplicating this profit margin next year will be very pleasing, but will take incredible vigilance. In my view, that's Progressive at its best.

I distinguish established states to make special mention of our entry into Massachusetts, which occurred on May 1st. Progressive is now available in every state of the nation. Additional commentary on Massachusetts is included in the Operations Summary.

Growth

Growth, by our standards, has been stalled for some time. Measured by premiums written that statement is undeniable; our 1, 3, and 5 year written premium growth has been (1)%, (1)%, and 3%, respectively. Corresponding industry growth has been less than 1% for the three year period, 1% for five, and an estimated .5% for the past year. As noted earlier a prolonged period of negative price adjustments is part of the explanation. In 2008 we saw our average auto premiums on our new Agency business applications increase slightly over the prior year for the first time in 2 years, while the similar measure in our Direct business still lags the prior year by 6%.

A healthier measure and our preferred one is the number of customers served. Unfortunately there is no consistently reliable comparative measure for the industry. Our results here are considerably more encouraging with continuous increases in numbers of policies in force. We ended the year up 3%, which translates to 350,000 additional policies spread across our product offerings. A closer look will show these additions have come in our Direct auto offering, which has been and continues to be a referendum on changing consumer shopping behavior. Our 9% growth in policies, and 4% increase in written premiums, coupled with attractive improvements in expected customer tenure, are top echelon results in this environment and forecast to me even better days ahead.

Our industry leading special lines group, serving motorcyclists, motor home and small boat owners, also gained a disproportionate share of our new customers in 2008. Some of these products represent more discretionary consumer spending and, in the near term, we may struggle to see significant market growth in units.

Similarly our Commercial Auto business group turned in a very respectable year, but ended the year with about the same number of policies as it started the year. The more recent trends in growth and retention reflect the depressed outlook for contractors and tradesmen.

Our biggest challenge continues to be growing our agent business. While increasing our acceptance for agents more preferred and commercial customers, we have lost some momentum in our traditional strength niche for agents—nonstandard auto. Agents are critical to our success and our focus is, as it should be, on providing products that continuously allow them to "win" with Progressive. The Operations Summary in this report will provide more details on specifics of new product and service developments for agents. Our goal is a constant and always worth reinforcing—To grow as quickly as possible, constrained only by our profitability objective and ability to provide high-quality customer service. That said, we must aggressively meet all competitive challenges through increased segmentation and innovation.

Investment and Capital

A pretax underwriting income of some $735 million was, with the above qualifications, an acceptable result and highlights the quality of earnings we are capable of even in times when more draconian changes may be inflicted on other parts of the economy. This very premise is the basis for our long-standing investment and capital management policy to maintain a liquid, diversified, and high-quality investment portfolio. In short, our primary investment goal is to ensure we never constrain our ability to write as much insurance as we can. 2008 has exposed us to market conditions that require us to do some additional soul searching on our investment philosophy. Our intent remains unchanged. However our accepted views of liquidity, quality, and diversification have all been severely challenged.

The accounting for invested assets in 2008 was, for me, an academic version of water torture. Assessments of impairment done in one quarter may require further impairment in the next. Reliable market pricing, in times of high volatility, added a new level of challenge and diligence. We have handled our accounting obligations with the openness and transparency we believe characterizes Progressive. Many years ago a colleague said, "Embarrassment is just a timing difference," an expression for which I and others maintain great affinity, and believe reflects in all our disclosures.

Our monthly reporting made our capital position consistently available, however balance sheet versus income statement presentation depended on the timing of impairment assessments. Experience gives rise to knowledge and in this case we believe we can provide additional benefit to readers by adding comprehensive income and derived comprehensive income per share to our monthly disclosure. Without reducing the importance of net income, it should provide our owners an additional, and at times more consistent, "all-in" economic data point. During the year we recognized net realized losses, including other-than-temporary impairment losses on the portfolio, of some $1.4 billion (I had trouble typing that), or about 10% of invested assets, all culminating in a net loss of $70 million for the year.

So, what do we know now? And, what can we take away from this experience? This may well be an unrepeated event, but the lessons for many should be invaluable and the tuition has been paid.

We have codified lessons learned based on what we thought were our intents and expected outcomes versus what we now know was actually possible. For example I reported last year that our direct exposure to sub-prime related instruments was small. However we also had exposure to the largest banks and financial institutions that had such risk. It is clearer to us now that our indirect risk was far greater than the direct risk we avoided, and yet we fell short in anticipating the impact in the same way we normally expect of ourselves.

Similarly, we allowed our concentration guidelines to permit us to favor Government Sponsored Entities, such as Fannie Mae and Freddie Mac, operating under failed expectations of just what Government Sponsorship would mean. Detailing the specifics is perhaps less important than the recognition that, regardless of the environment, there are opportunities to improve what we do. The extremes of outcomes that were far beyond those seen or imagined in the economy forced us to adopt a mantra of "Imagine the Unimaginable." Only then could we break with thinking constrained by norms that no longer applied. Breaking with thinking that defines the norm is, in large part, what characterizes Progressive and has been the spirit that has given rise to innovations such as concierge claims service, comparative rating, pet injury coverage, and usage-based insurance. So, for our 2008 report, it seemed apropos for the art to reflect the notion of "Imagine the Unimaginable."

The investment results and market valuations clearly eroded our capital position, raising reasonable questions about the need for replacement capital. I used the third quarter letter accompanying the 10-Q to provide insight into how we think about capital and, in effect, constructed our capital position using a regulatory required layer, extreme contingency reserve layer, and an excess layer. While the construct was for illustrative purposes, it is in fact an excellent model of our capital husbandry.

While the loss of capital was clear, for some it was less clear that the loss was contained at the excess layer, a layer largely held at the holding company and outside the insurance subsidiaries. Dividends are made out of and, as necessary, into the insurance subsidiaries to ensure they meet appropriate capital requirements. We ended the year in a similar position to my summary comments in the third quarter letter—several hundred million dollars above the sum of the regulatory and extreme contingency layer. While some return in investment valuations would be welcome, we are not depending on any in the short term. We have taken significant steps to restructure the portfolio and, more specifically, the deployment of any new money to considerably lower risk investments for now. While yields will match the risk, our ability to generate operating income is the protected asset and drives our prioritization. The prioritization is accentuated when one considers that our operating cash flow has now been positive for 100 consecutive quarters.

An Update

I said in my opening that there were some positive and encouraging Wows! And if you're ready for a change of pace I would like to share a few.

In closing this letter last year I said, "Our opportunities are clear and exciting and include…" and listed five bullet points. I repeat them here as my sub-headings along with some illustrative examples of meaningful progress made during the year. A broad-based agenda such as this is never done, but I think you will see we had some very real progress.

Building a stronger brand and communicating it well We let "Flo" loose on consumers in 2008 as part of our television advertising, in a campaign that by all accounts has trumped our prior efforts. I report that much less based upon feelings and anecdotes and more from the measurement analytics that support all our actions.

I reported last year that we challenged ourselves to produce advertising that has thematic continuity, makes a real breakthrough in interest, and has a strong call to action. The consumer-familiar setting of a "superstore" provides a constancy of identity and foundation for delivery of our many messages. While auto insurance doesn't come in a box or service in a can, building on the store-based metaphor provides tangibility over mystery, enhances approachability, and invites trial for many consumers. Less analytical assessments can be derived by consumer requests for their policy to in fact be delivered in a box—a request we were initially not well equipped to handle.

A key objective is to have our efforts in marketing and brand-building match our assessed competency in other technical skills—and sooner is always better. Adding the experience that Larry Bloomenkranz brings as our Chief Marketing Officer during the year is just one step of many that we have taken to make this happen.

Advertising, however, is but a part of our marketing and branding efforts. Our mid-year Investor Relations meeting used multiple consumer profiles to highlight internal marketing constructs that segment consumer behaviors. Simply stated, "Know your Target—Act with Purpose," while not a breakthrough in marketing thought process, it is a very powerful notion when implemented well in our product and service organizations.

Early in 2008 we announced we would be the title sponsor for the Automotive X PRIZE, now known as the Progressive Automotive X PRIZE. This worldwide competition, with a prize purse of $10 million, is designed to inspire a new generation of viable, super fuel-efficient vehicles that are affordable and meet market needs for capability, safety, and performance.

Following in the footsteps of the British Government's Longitude prize in 1714 and the Orteig prize won by Charles Lindbergh in 1927, the X PRIZE Foundation has already changed the world's views of what is possible in space flight, and has active plans to do similar things in genetics. There can be little question that our fossil fuel dependence is an issue that needs meaningful leadership. Employees and I are proud to associate the Progressive brand with a relevant and bold effort to help move innovations forward even faster on this challenge—we think it fits perfectly.

We measure effectiveness of all such actions in economic terms as best we can and we will have little to report until 2010, the year the contestants will offer their solutions. If media interest and consumer response to date are indicative, these will be dollars well spent on something that also feels very right. For updates on this effort and worldwide entries see progressiveautoxprize.org.

Building on our retention gains and providing continuity of coverage throughout a customer's lifetime Retention of customers has been a significant focus for some years now, and at times the slow speed of change in certain measures has posed doubt in our belief that we could effect more dramatic change. 2008 confirmed our confidence in the magnitude of change that is possible.

In a moderately increasing rate climate, we continued to see an increase in customer retention with both our Agency and Direct auto policy life expectancy measures increasing 11%. Improvement in our special lines products was numerically less at around 1% but, as a group, they remain our longest-tenured customers. Commercial customer measures ended the year slightly lower than where they started, after some initial gains, reflecting the somewhat shocking numbers of trucks being taken out of service and the general economic pull back.

Good luck or hard work? Either way when the sensitivity of one month of policy life extension is easily valued at over one billion dollars of lifetime premium, the result is bankable. The answer, without doubt, is in fact hard work over a prolonged period of time.

We have used this report and other forums to highlight our intensity into what we have called friendly fire incidents, or rough product edges, along with our actions to address them. We have continuously embraced the concepts and analytics of total quality management, and of more recent times adopted, and now have become somewhat recognized for, the depth of application of the Net Promoter® Score. What has really happened is that we have matured from tactically addressing just retention measures or customer experience improvements on multiple fronts into a more deliberate customer care culture that is embraced, managed, and advanced at every level of the organization by those who correctly see themselves as brand ambassadors and disciples.

My words likely don't do justice to the degree of change this represents and, while not an objective, it is of some note to see favorable positioning or improvement in external measures of customer satisfaction. To be fair, our self assessment is that we still have many opportunities to further improve customer experiences and permanently eliminate all too frequent lapses in quality. I suggest with some satisfaction and confidence that our momentum here is contagious and our objective of making Progressive what we call a "destination" auto insurer is very real.

Maintaining a focus on operating at a lower cost than competitors, while providing remarkable service Creating expense advantages that are sustainable generally require doing things differently, not just better. In 2008, our Claims and IT organizations made substantial progress on redesigning how they do what they do while operating at lower costs.

For many years we have been able to report each year as "our best ever" in claims quality. This year is no different. The preservation of claims quality is a must, along with the equally encouraging progress on customer satisfaction. However, skills and tasks can be rearranged to optimize even a well-performing process and, while our guiding principles remain unchanged, we see opportunities. Our concierge centers have provided invaluable insights and surfaced opportunities to apply those insights more broadly, and as such are central to the redesigned process architecture. Proof will be in our future loss adjustment expenses.

Reduced claims frequency, while at first a welcome sign, poses significant challenges in maintaining the balance between appropriately sizing the claims organization, and preserving the talent and experience required to support growth and any return to prior frequency levels. Claims management has met that challenge with creative solutions that are economically satisfactory, consistent with our workplace culture objectives, and advance the redesign process even faster. The supply and demand of claims and claims response will likely remain a significant management challenge throughout 2009.

Our dependence on, and self-assessed strength in, technology has been reported on frequently by me and remains true. The challenge imposed and actively accepted in 2008 within our technology organization is the age-old desire to do more with current resource levels, while doing the right things well: "Smart choices, well executed."

In a vibrant business culture, demand for technology resources may well outstrip supply. In 2008 our business and technology groups have reassessed just about every aspect of what we do and how we do it—to make the "smart choices, well executed" by line more operationally reflect business priority and intensity. I have every expectation these efforts will result in increased leverage of technology costs and greater accountability to market priorities.

Creating more responsive product and service offerings for the consumers we currently do not reach Progressive Home Advantage, our offering which combines a Progressive auto policy with a homeowner's or renter's policy underwritten by Homesite Insurance, expanded consistent with our expectations in 2008 and now serves a growing number of our customers, many of whom have added the offering to their existing auto policy. We provide this important option to customers in 46 states for Direct buyers and in 33 states for Agency customers. The objective is simple: reach new customers who we might not have been reaching and retain them and existing customers longer. So far, so good, and in 2009 we will make it available through additional agents.

We have placed additional emphasis on understanding the needs of our multi-policy households, especially those with special lines products in addition to their auto. We clearly have more opportunity and have set challenging internal goals for multi-policy penetration in 2009 based on achieved results to date.

Our usage-based insurance offering, now called MyRate℠, expanded within and across states in 2008. Notwithstanding the continuous challenges posed by such a new concept, the opportunity to reach a set of customers that have significantly different usage patterns than traditionally underwritten products would recognize is clear, and welcomed. Consumer acceptance is good. For us MyRate is slowly moving from feeling like a new and different product to becoming a very viable consumer option that speaks to a specific consumer segment.

Continuing to be innovative in all we do
The depth of this notion is not easily captured by a single example, but one may serve well to amplify the thought and share a recent product introduction.

Price is a clear factor in a consumer's purchasing decision and many efforts, including our own, have focused on providing consumers with increased access to price comparisons between providers. This year we introduced a new concept we call Name Your Price®, which invites the consumer to participate in the quoting process by telling us just how much they would like to spend on car insurance.

We start the quoting "conversation" in a place determined by the customer. Then we use combinations of coverages, limits, and deductibles to meet or approximate their needs. Involving the consumer in this way is both respectful of their preferences and involves them more actively in the process.

Early results are very encouraging, but even more important is the opportunity to use technology to engage the consumer in a meaningful and different way ensuring they get what they want, at a price they can manage.

Looking Forward

We remain continuously motivated by our aspiration of becoming Consumers' #1 Choice for Auto Insurance and, while our numerical progress in 2008 did not match our aspirations, some of our actions set an interesting stage for the future.

Nothing we have achieved has been without the efforts of so many and, our single most important initiative especially in current times, is ensuring Progressive is a Great Place to Work. Creating an environment where our people enjoy working hard, are motivated to do their best, can grow constantly, and that others want to join is a never-ending challenge. Our people and culture are what makes us special.

Equally important is our appreciation for the customers we are privileged to serve, the agents and brokers who choose to represent us, and shareholders who support what we are doing.

Glenn M. Renwick
President and Chief Executive Officer

What if you got into an accident and only had to spend about 15 minutes on the repair process? Customers who choose one of Progressive's 54 concierge service centers throughout the country can do that. Drivers drop off their car and we do the rest, including finding a quality body shop. A process so unique it's patented!

Consistent achievement of superior results requires that our people understand Progressive's objectives and their specific roles, and that their personal objectives dovetail with Progressive's. Our objectives are ambitious, yet realistic. We recognize that the dynamics of each distribution channel are very different and, therefore, have established a product management system responsible for achieving stated financial objectives over rolling five-year periods. Progressive monitors its financial policies continuously and strives to meet these targets annually. Experience always clarifies objectives and illuminates better policies. We constantly evolve as we monitor the execution of our policies and progress toward achieving our objectives.

Objectives

Profitability Progressive's most important goal is for our insurance subsidiaries to produce an aggregate calendar-year underwriting profit of at least 4%. Our business is a composite of many product offerings defined in part by product type, distribution channel, geography, customer tenure, and underwriting grouping. Each of these products has targeted operating parameters based on level of maturity, underlying cost structures, customer mix, and policy life expectancy. Our aggregate goal is the balanced blend of these individual performance targets in any calendar year.

Growth Our goal is to grow as fast as possible, constrained only by our profitability objective and our ability to provide high-quality customer service. Progressive is a growth-oriented company and management incentives are tied to profitable growth.

We report Personal Lines and Commercial Auto results separately. We further break down our Personal Lines' results by channel (Agency and Direct) to give shareholders a clearer picture of the business dynamics of each distribution method and their respective rates of growth. Aggregate expense ratios and aggregate growth rates disguise the true nature and performance of each business.

Financial Policies

Progressive balances operating risk with risk of investing and financing activities in order to have sufficient capital to support all the insurance we can profitably underwrite and service. Risks arise in all operational and functional areas, and therefore must be assessed holistically, accounting for the offsetting and compounding effects of the separate sources of risk within Progressive.

We use risk management tools to quantify the amount of capital needed, in addition to surplus, to absorb consequences of foreseeable events such as unfavorable loss reserve development, litigation, weather-related catastrophes, and investment-market corrections. Our financial policies define our allocation of risk and we measure our performance against them. If, in our view, future opportunities meet our financial objectives and policies, we will invest capital in expanding business operations. Underleveraged capital will be returned to investors. We expect to earn a return on equity greater than its cost. Presented is an overview of Progressive's Operating, Investing, and Financing policies.

Operating

Monitor pricing and reserving discipline

- Manage profitability targets and operational performance at our lowest level of product definition
- Sustain premiums-to-surplus ratios at efficient levels, and below applicable state regulations, for each insurance subsidiary
- Ensure loss reserves are adequate and develop with minimal variance

Investing

Maintain a liquid, diversified, high-quality investment portfolio

- Manage on a total return basis
- Target an allocation of 75% to 100% for fixed-income securities with the balance in common equities
- Manage interest rate, credit, prepayment, extension, and concentration risk

Financing

Maintain sufficient capital to support insurance operations

- Maintain debt below 30% of total capital at book value
- Neutralize dilution from equity-based compensation in the year of issuance through share repurchases
- Return underleveraged capital through share repurchases and a variable dividend program based on annual underwriting results

Objectives and Policies Scorecard

Financial Results	Target	2008	2007	2006	5 Years[1]	10 Years[1]
Underwriting margin–Progressive	4%	5.4%	7.4%	13.3%	10.6%	8.8%
–Industry[2]	na	1.5%	2.5%	4.5%	3.6%	—%
Net premiums written growth	(a)	(1)%	(3)%	1%	3%	10%
Policies in force growth–Personal Auto	(a)	2%	2%	1%	4%	9%
–Special Lines	(a)	7%	8%	8%	11%	14%
–Commercial Auto	(a)	—%	7%	7%	8%	18%
Companywide premiums-to-surplus ratio	(b)	3.0	3.0	2.8	na	na
Investment allocation–fixed:equity	(c)	94%:6%	83%:17%	84%:16%	na	na
Debt-to-total capital ratio	< 30%	34.0%	30.6%	14.8%	na	na
Return on average shareholders' equity (ROE)[3]	(d)	(1.5)%	19.5%	25.3%	20.5%	19.0%
Comprehensive ROE[4]	(d)	(13.3)%	17.7%	28.4%	18.8%	18.7%

(a) Grow as fast as possible, constrained only by our profitability objective and our ability to provide high-quality customer service.

(b) Determined separately for each insurance subsidiary.

(c) Allocate 75% to 100% in fixed-income securities with the balance in common equities.

(d) Progressive does not have a predetermined target for ROE.

na = not applicable

[1] Represents results over the respective time period; growth represents average annual compounded rate of increase.

[2] Represents the personal auto insurance industry; 2008 is estimated.

[3] Based on net income (loss).

[4] Based on comprehensive income (loss). Comprehensive ROE is consistent with Progressive's policy to manage on a total return basis and better reflects growth in shareholder value. For a reconciliation of net income (loss) to comprehensive income (loss) and for the components of comprehensive income (loss), see Progressive's *Consolidated Statements of Changes in Shareholders' Equity* and *Note 11–Other Comprehensive Income (Loss)*, respectively, which can be found in the complete Consolidated Financial Statements and Notes included in Progressive's 2008 Annual Report to Shareholders, which is attached as an Appendix to Progressive's 2009 Proxy Statement.

Achievements

We are convinced that the best way to maximize shareholder value is to achieve these financial objectives and policies consistently. A shareholder who purchased 100 shares of Progressive for $1,800 in our first public stock offering on April 15, 1971, owned 92,264 shares on December 31, 2008, with a market value of $1,366,430, for a 19.7% compounded annual return, compared to the 6.0% return achieved by investors in the Standard & Poor's 500 during the same period. In addition, the shareholder received their 2007 dividends of $13,378 in 2008, bringing total dividends received to $235,224 since the shares were purchased.

In the ten years since December 31, 1998, Progressive shareholders have realized compounded annual returns, including dividend reinvestment, of 1.7%, compared to (1.4)% for the S&P 500. In the five years since December 31, 2003, Progressive shareholders' returns were (4.6)%, compared to (2.2)% for the S&P 500. In 2008, the returns were (21.9)% on Progressive shares and (36.5)% for the S&P 500.

Over the years, when we have had adequate capital and believed it to be appropriate, we have repurchased our shares. In addition, as our Financial Policies state, we will repurchase shares to neutralize the dilution from equity-based compensation programs and return any underleveraged capital to investors. During 2008, we repurchased 9,918,818 common shares. The total cost to repurchase these shares was $179 million, with an average cost of $18.09 per share. Since 1971, we have spent $6.3 billion repurchasing our shares, at an average cost of $5.84 per share.

Operations Summary

Personal Lines While monthly profitability results for Personal Lines fluctuated through the year due to shifts in gas consumption, an active storm season, and a more severe than normal winter, the full year combined ratio for Personal Lines was 94.6. This is inclusive of 95.1 for Agency and 93.9 for Direct, and was almost 1.5 points better than our target underwriting margin.

Total net premiums written were relatively flat versus 2007. Average premium per policy increased slightly for new Agency-written auto business, and decreased 6% in both our Direct auto and special lines businesses. Our weighted average filed rate level change for the year was +2.8% for Agency auto and +1.6% for Direct auto. The lower average premium results relative to the filed rate increases is a function of a shift in the mix of business toward more preferred customers whose average rates are lower, but who stay with us longer. We are encouraged by the trend. In special lines, filed rate changes were about +3.5% and the lower average premium resulted from a shift towards more motorcycle business, demand for which increased significantly with the increase in gas prices.

Our underwriting expense ratio for Personal Lines was 21.1 for the year, a tenth of a point better than 2007. Average cost per policy in force dropped more than 4%, partially offset by the decrease in average premium per policy. Improved customer retention is at the core of this improvement along with attention to expenses and process improvements. Moving our customers to a paperless environment is one example of efforts to decrease costs and improve the customer experience. We now have over a million customers signed up for paperless interaction with Progressive and our enrollment rate is accelerating.

Personal Lines policies in force grew by 3% for the year. Direct auto led the way at 9%. Special lines was close behind at 7%. Agency auto unfortunately continued a several year trend, shrinking 2%. Policy growth is a function of new business growth and in-force policyholder retention. New business change was positive 2% for Direct auto and 3% for special lines, and negative 13% for Agency auto. Customer retention improved across all of our personal product lines with notable gains in the auto programs and a slight increase in special lines.

While there are some indications that auto insurance shopping has declined, we are at a minimum confident that the trend toward online shopping continues, albeit likely at a slower pace than in previous years. New Direct auto quotes increased modestly for the year, with effectively all of that growth coming online. We attribute this growth to an increase in advertising spend of 7% and what we believe to be far better creative content. The mix of our advertising spend continued to shift online as well with online spending for 2008 23% higher than 2007.

During the year, we introduced a new online quoting application in 16 states and also introduced our Name Your Price® quoting experience in 7 states. Results of both of these efforts have been positive in terms of increasing the percentage of consumers who purchase after receiving a quote. While conversion of online quotes into policies for Direct auto improved for the year, aggregate conversion decreased slightly due to the shift towards Internet purchasing versus the phone.

Another significant factor in our Direct auto new business growth was our entry into the Commonwealth of Massachusetts on May 1. We are pleased with Massachusetts consumers' response to our offering there, but have acknowledged uncharacteristic quality problems with our rate comparison process that have our full attention.

Agency new business volume was very challenging in 2008. The shift towards quoting on vendor-supplied multi-carrier quoting platforms (comparative rating systems) continued similar to 2007.

	2008	2007	Change
Net premiums written (in billions)	$ 11.9	$ 11.9	—%
Net premiums earned (in billions)	$ 11.8	$ 12.0	(1)%
Loss and loss adjustment expense ratio	73.5	71.8	1.7 pts.
Underwriting expense ratio	21.1	21.2	(.1) pts.
Combined ratio	94.6	93.0	1.6 pts.
Policies in force (in thousands)	10,464.9	10,115.6	3%

While agents again quoted a Progressive rate about 10% more often than the previous year, the conversion of those quotes to policies dropped from prior year levels.

We are responding to this challenge in several ways.

First is to ensure we are positioned in agencies such that we are considered for more preferred customers in addition to our historically strong nonstandard appeal. We have done this by introducing more competitive auto product offerings for these segments and by beginning to provide the breadth of other products necessary to meet this segment's needs. During 2008, we introduced our new 7.0 auto program in 13 states and have seen benefits in preferred volume as a result of doing so. This auto program features significant tenure-based benefits and other features that appeal to preferred drivers.

Second is to ensure we have our most competitive rate displayed on the comparative rating systems by ensuring agents see our rates with all applicable discounts applied. This effort is in its infancy and will roll out in early 2009.

Third is to ensure that we employ market leading rating segmentation at the state level. We have made significant headway and have recently elevated new programs in key states including New York, a state in which we restricted Agency business significantly in 2008. While total Agency new business for the year was disappointing, we are somewhat encouraged by the fact that we grew our Agency preferred new business in the low single digits.

Policyholder retention gains have come as a result of continued close assessment and modification of customer-facing processes, a shift toward more preferred customers who retain longer, and a continued focus on improving service levels, which we measure via the Net Promoter® Score (NPS). We have also begun to focus more on the needs of our customers' households in aggregate versus our historical approach of focusing on individual policies. We fully intend that doing so and offering more cohesive bundles of products and services will lead to continued retention gains. A growing percentage of our customers have more than one Progressive policy in their household. We are also now able to meet customers' property insurance needs and are pleased with the success here, especially for our Direct customers. Almost 4% of our Direct auto customers also have a Progressive Home Advantage policy.

A key ongoing tactic for our business is to lead the market in rating segmentation. In addition to progress such as the 7.0 program roll out, we also made considerable progress on what we perceive to be a transformational approach to rating for auto insurance in our patented MyRate℠ program. We added this program in 6 states during 2008, bringing the total to 9, and also made significant improvements in the customer experience. Customers now simply plug a device into a port in their vehicle and the device transmits driving behavior to Progressive virtually real-time via a cellular connection. We expect to continue to broaden the availability of this program in 2009.

Our priorities for 2009 are clear: continue to improve customer retention; continue to reduce non-claims costs; ensure we maximize new business sales across all distribution points; and ensure we improve the breadth and competitiveness of the products we and our agents offer consumers.

Commercial Lines Progressive's Commercial Auto business encountered strong headwinds throughout 2008 as the general economy stumbled into recession. Spending on residential construction, a key customer segment, was significantly lower than any of the previous four years, lowering demand for both our business auto and truck products.

Short-haul trucking was adversely affected by increases in diesel fuel prices, the overall reduction in economic activity, and a decline in goods shipped. Our customers are primarily small business owners and the tightening of the credit markets has left many of them vulnerable, which is reflected in the increasing small business bankruptcy rate.

Our efforts in 2008 were directed at ensuring profitable underwriting results, retaining current customers, enhancing our processes and skills for handling high exposure commercial claims, and building out the product portfolio. For the year, Commercial Auto net premiums written declined 7%, primarily due to a decline in new business applications versus the prior year. The balance of the decline can be attributed to declines in average policy premiums as prior year rate decreases earned in and customers bought less coverage.

Policies in force remained relatively unchanged for the year, as new business production slowed and we experienced an increase in policy cancellations due to business failures. The 2008 combined ratio was 94.7, an increase of 4.8 points versus the prior year but more in line with our profit target. The combined ratio included 1.6 points of adverse development and reserve strengthening on prior accident years. The Commercial Auto expense ratio came in at 21.5, an increase of 1.3 points from 2007, largely a function of reduced premium levels.

During 2008 we increased rates in most markets in response to increasing loss costs. These increases have begun to stabilize average premiums which, for business auto, began to trend positive by year end. We finished the year confident in the overall adequacy of our rates and will remain vigilant in responding to changes in loss cost trends. An area of concern at the end of 2008 was California business auto where we put new business restrictions in place in October. We have since received approval on two rate increases there and continue to work closely with the California Department of Insurance to secure an adequate rate level before any restrictions are lifted.

We continued the deployment of our enhanced truck and tow coverages throughout the year and they are now available in 29 states. The sale of enhanced coverages is designed to attract higher retaining customers, increase average policy premiums, and contribute to profitability and growth of the business. We will complete this deployment in 2009.

Our focus on the foundational issues of claims handling, pricing accuracy, and products that respond to customer needs keeps us well positioned as a top four commercial auto insurer able to respond as the economy recovers and expansion resumes.

	2008	2007	Change
Net premiums written (in billions)	$ 1.7	$ 1.8	(7)%
Net premiums earned (in billions)	$ 1.8	$ 1.8	(5)%
Loss and loss adjustment expense ratio	73.2	69.7	3.5 pts.
Underwriting expense ratio	21.5	20.2	1.3 pts.
Combined ratio	94.7	89.9	4.8 pts.
Policies in force (in thousands)	539.4	539.2	— %

"Innovation is not the product of logical thought, although the result is tied to logical structure."

Albert Einstein

“The challenge isn’t to keep your eye on big competitors.

It’s to pay attention to

the innovators.”

Dave Duffield

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The current standard is 27.5. The government wants 35. Progressive aims higher. The Progressive Insurance Automotive X PRIZE is an international competition designed to inspire a new generation of viable, super fuel-efficient vehicles that get 100 miles per gallon or the energy equivalent. We're not talking about science experiments, either. We're offering a $10 million prize purse for the development of safe, affordable vehicles that people actually want to buy.

Consolidated Financial Statements

Basis of Presentation

The accompanying consolidated financial statements include the accounts of The Progressive Corporation, its subsidiaries and affiliate. These financial statements should be read in conjunction with the complete Consolidated Financial Statements, including the complete Notes to the Consolidated Financial Statements, as well as Management's Discussion and Analysis of Financial Condition and Results of Operations and Supplemental Information, which are included in Progressive's 2008 Annual Report to Shareholders, which is attached as an Appendix to Progressive's 2009 Proxy Statement.

Consolidated Statements of Income

(millions—except per share amounts)

For the years ended December 31,	2008	2007	2006
Revenues			
Net premiums earned	$ 13,631.4	$ 13,877.4	$ 14,117.9
Investment income	637.7	680.8	647.8
Net realized gains (losses) on securities	(1,445.1)	106.3	(9.7)
Service revenues	16.1	22.3	30.4
Total revenues	12,840.1	14,686.8	14,786.4
Expenses			
Losses and loss adjustment expenses	10,015.0	9,926.2	9,394.9
Policy acquisition costs	1,358.1	1,399.9	1,441.9
Other underwriting expenses	1,523.4	1,526.2	1,402.8
Investment expenses	8.8	12.4	11.9
Service expenses	20.4	20.5	24.4
Interest expense	136.7	108.6	77.3
Total expenses	13,062.4	12,993.8	12,353.2
Net Income (Loss)			
Income (loss) before income taxes	(222.3)	1,693.0	2,433.2
Provision (benefit) for income taxes	(152.3)	510.5	785.7
Net income (loss)	$ (70.0)	$ 1,182.5	$ 1,647.5
Computation of Earnings Per Share			
Basic:			
Average shares outstanding	668.0	710.4	774.3
Per share	$ (.10)	$ 1.66	$ 2.13
Diluted:			
Average shares outstanding	668.0	710.4	774.3
Net effect of dilutive stock-based compensation	5.9	8.1	9.5
Total equivalent shares	673.9	718.5	783.8
Per share[1]	$ (.10)	$ 1.65	$ 2.10

[1]For 2008, amount represents basic earnings per share since diluted earnings per share was antidilutive due to the net loss for the year.

See Notes to the complete Consolidated Financial Statements included in Progressive's 2008 Annual Report to Shareholders, which is attached as an Appendix to Progressive's 2009 Proxy Statement.

Consolidated Balance Sheets

(millions)

December 31,	2008	2007
Assets		
Investments – Available-for-sale, at fair value:		
Fixed maturities (amortized cost: $10,295.3 and $9,135.6)	$ 9,946.7	$ 9,184.9
Equity securities:		
Nonredeemable preferred stocks (cost: $1,131.3 and $2,578.1)	1,150.0	2,270.3
Common equities (cost: $553.6 and $1,361.0)	727.8	2,327.5
Short-term investments (amortized cost: $1,153.6 and $382.4)	1,153.6	382.4
Total investments	12,978.1	14,165.1
Cash	2.9	5.8
Accrued investment income	125.7	142.1
Premiums receivable, net of allowance for doubtful accounts of $113.7 and $118.1	2,408.6	2,395.1
Reinsurance recoverables, including $44.0 and $47.6 on paid losses	288.5	335.1
Prepaid reinsurance premiums	62.4	69.8
Deferred acquisition costs	414.0	426.3
Income taxes	821.6	106.0
Property and equipment, net of accumulated depreciation of $653.6 and $605.7	997.1	1,000.4
Other assets	151.6	197.4
Total assets	$ 18,250.5	$ 18,843.1
Liabilities and Shareholders' Equity		
Unearned premiums	$ 4,175.9	$ 4,210.4
Loss and loss adjustment expense reserves	6,177.4	5,942.7
Accounts payable, accrued expenses, and other liabilities[1]	1,506.4	1,580.6
Debt[2]	2,175.5	2,173.9
Total liabilities	14,035.2	13,907.6
Common Shares, $1.00 par value (authorized 900.0; issued 797.9 and 798.1, including treasury shares of 121.4 and 117.9)	676.5	680.2
Paid-in capital	892.9	834.8
Accumulated other comprehensive income (loss):		
Net unrealized gains (losses) on securities	(76.8)	465.0
Net unrealized gains on forecasted transactions	24.9	27.8
Retained earnings	2,697.8	2,927.7
Total shareholders' equity	4,215.3	4,935.5
Total liabilities and shareholders' equity	$ 18,250.5	$ 18,843.1

[1]See *Note 12 — Litigation* and *Note 13 — Commitments and Contingencies*, in Progressive's 2008 Annual Report to Shareholders, for further discussion.

[2]Consists of long-term debt. See *Note 4 — Debt*, in Progressive's 2008 Annual Report to Shareholders, for further discussion.

See Notes to the complete Consolidated Financial Statements included in Progressive's 2008 Annual Report to Shareholders, which is attached as an Appendix to Progressive's 2009 Proxy Statement.

Consolidated Statements of Changes in Shareholders' Equity

(millions—except per share amounts)

For the years ended December 31,	2008		2007		2006	
Retained Earnings						
Balance, Beginning of year	$ 2,927.7		$ 4,646.9		$ 4,726.0	
Net income (loss)	(70.0)	$ (70.0)	1,182.5	$ 1,182.5	1,647.5	$ 1,647.5
Cash dividends declared on common shares ($0, $2.145, and $.0325 per share)	—		(1,507.6)		(25.0)	
Treasury shares purchased[1]	(157.1)		(1,388.4)		(1,111.6)	
Capitalization of stock spilt	—		—		(585.9)	
Other, net[2]	(2.8)		(5.7)		(4.1)	
Balance, End of year	$ 2,697.8		$ 2,927.7		$ 4,646.9	
Accumulated Other Comprehensive Income (Loss), Net of Tax						
Balance, Beginning of year	$ 492.8		$ 604.3		$ 398.7	
Changes in:						
Net unrealized gains (losses) on securities		(541.8)		(131.8)		206.7
Net unrealized gains on forecasted transactions		(2.9)		20.3		(1.1)
Other comprehensive income (loss)	(544.7)	(544.7)	(111.5)	(111.5)	205.6	205.6
Balance, End of year	$ (51.9)		$ 492.8		$ 604.3	
Comprehensive Income (Loss)		$ (614.7)		$ 1,071.0		$ 1,853.1
Common Shares, $1.00 Par Value						
Balance, Beginning of year	$ 680.2		$ 748.0		$ 197.3	
Stock options exercised	3.5		3.4		3.7	
Treasury shares purchased[1]	(9.9)		(72.9)		(39.1)	
Restricted stock issued, net of forfeitures	2.7		1.7		.2	
Capitalization of stock split	—		—		585.9	
Balance, End of year	$ 676.5		$ 680.2		$ 748.0	
Paid-in Capital						
Balance, Beginning of year	$ 834.8		$ 847.4		$ 848.2	
Stock options exercised	23.5		27.4		39.6	
Tax benefits from exercise/vesting of stock-based compensation	11.1		15.5		38.8	
Treasury shares purchased[1]	(12.4)		(87.1)		(63.8)	
Restricted stock issued, net of forfeitures	(2.7)		(1.7)		(.2)	
Amortization of stock-based compensation	35.1		28.0		27.8	
SFAS 123(R) reclass[3]	—		—		(51.5)	
Other[2]	3.5		5.3		8.5	
Balance, End of year	$ 892.9		$ 834.8		$ 847.4	
Unamortized Restricted Stock						
Balance, Beginning of year	$ —		$ —		$ (62.7)	
SFAS 123(R) reclass[3]	—		—		62.7	
Balance, End of year	$ —		$ —		$ —	
Total Shareholders' Equity	$ 4,215.3		$ 4,935.5		$ 6,846.6	

[1]Progressive did not split its treasury shares in conjunction with the May 18, 2006, 4-for-1 stock split. In 2006, we repurchased 3,182,497 common shares prior to the stock split and 35,887,246 common shares subsequent to the stock split.

[2]Primarily reflects activity associated with our deferred compensation and incentive plans.

[3]Upon adoption of SFAS 123(R), companies were required to eliminate any unearned compensation (i.e., contra-equity) accounts against the appropriate equity accounts. As a result, as of January 1, 2006, we were required to reclassify $62.7 million of "Unamortized restricted stock," of which $51.5 million related to equity awards and $11.2 million related to liability awards.

There are 20.0 million Serial Preferred Shares authorized; no such shares are issued or outstanding.

There are 5.0 million Voting Preference Shares authorized; no such shares have been issued.

See Notes to the complete Consolidated Financial Statements included in Progressive's 2008 Annual Report to Shareholders, which is attached as an Appendix to Progressive's 2009 Proxy Statement.

Consolidated Statements of Cash Flows

(millions)

For the years ended December 31,	2008	2007	2006
Cash Flows from Operating Activities			
Net income (loss)	$ (70.0)	$ 1,182.5	$ 1,647.5
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation	99.1	106.9	103.4
Amortization of fixed-income securities	249.6	284.1	225.6
Amortization of stock-based compensation	34.5	26.5	27.6
Net realized (gains) losses on securities	1,445.1	(106.3)	9.7
Net loss on disposition of property and equipment	1.6	.4	.9
Changes in:			
Premiums receivable	(13.5)	103.1	2.5
Reinsurance recoverables	46.6	98.7	(28.1)
Prepaid reinsurance premiums	7.4	19.7	14.2
Deferred acquisition costs	12.3	14.7	3.8
Income taxes	(423.8)	(30.3)	10.1
Unearned premiums	(34.5)	(124.6)	(.1)
Loss and loss adjustment expense reserves	234.7	217.7	64.7
Accounts payable, accrued expenses, and other liabilities	(101.2)	2.4	7.1
Other, net	61.3	(4.5)	(64.3)
Net cash provided by operating activities	1,549.2	1,791.0	2,024.6
Cash Flows from Investing Activities			
Purchases:			
Fixed maturities	(7,593.9)	(8,184.6)	(6,294.9)
Equity securities	(598.3)	(1,490.3)	(1,131.6)
Short-term investments — auction rate securities	(631.5)	(7,156.6)	(2,999.3)
Sales:			
Fixed maturities	5,629.5	8,327.6	5,668.2
Equity securities	1,401.0	775.2	323.1
Short-term investments — auction rate securities	631.5	7,325.4	3,215.5
Maturities, paydowns, calls, and other:			
Fixed maturities	505.5	557.9	686.1
Equity securities	34.9	10.7	223.5
Net sales (purchases) of short-term investments — other	(771.0)	30.0	(22.3)
Net unsettled security transactions	177.2	35.1	(116.6)
Purchases of property and equipment	(98.5)	(136.3)	(334.3)
Sale of property and equipment	1.1	2.0	15.4
Net cash provided by (used in) investing activities	(1,312.5)	96.1	(767.2)
Cash Flows from Financing Activities			
Proceeds from exercise of stock options	27.0	30.8	43.3
Tax benefits from exercise/vesting of stock-based compensation	11.1	15.5	38.8
Proceeds from debt[1]	—	1,021.7	—
Payment of debt	—	—	(100.0)
Dividends paid to shareholders	(98.3)	(1,406.5)	(25.0)
Acquisition of treasury shares	(179.4)	(1,548.4)	(1,214.5)
Net cash used in financing activities	(239.6)	(1,886.9)	(1,257.4)
Increase (decrease) in cash	(2.9)	.2	—
Cash, Beginning of year	5.8	5.6	5.6
Cash, End of year	$ 2.9	$ 5.8	$ 5.6

[1]Includes a $34.4 million pretax gain received upon closing a forecasted debt issuance hedge. See *Note 4 — Debt* in Progressive's 2008 Annual Report to Shareholders, for further discussion.

See Notes to the complete Consolidated Financial Statements included in Progressive's 2008 Annual Report to Shareholders, which is attached as an Appendix to Progressive's 2009 Proxy Statement.

CEO and CFO Certifications

Glenn M. Renwick, President and Chief Executive Officer of The Progressive Corporation, and Brian C. Domeck, Vice President and Chief Financial Officer of The Progressive Corporation, have issued the certifications required by Sections 302 and 906 of The Sarbanes-Oxley Act of 2002 and applicable SEC regulations with respect to Progressive's 2008 Annual Report on Form 10-K, including the financial statements provided in this Report and in the 2008 Annual Report to Shareholders, which is attached as an Appendix to Progressive's 2009 Proxy Statement. Among other matters required to be included in those certifications, Mr. Renwick and Mr. Domeck have each certified that, to the best of his knowledge, the financial statements, and other financial information included in the Annual Report on Form 10-K, fairly present in all material respects the financial condition, results of operations, and cash flows of Progressive as of, and for, the periods presented. See Exhibits 31 and 32 to Progressive's Annual Report on Form 10-K for the complete Section 302 and 906 Certifications, respectively.

In addition, Mr. Renwick submitted his annual certification to the New York Stock Exchange (NYSE) on May 16, 2008, stating that he was not aware of any violation by Progressive of the NYSE corporate governance listing standards, as required by Section 303A.12(a) of the NYSE Listed Company Manual.

Internal Control over Financial Reporting

Progressive's management is responsible for establishing and maintaining adequate internal control over financial reporting. Based on Progressive's evaluation under the framework in *Internal Control–Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), management concluded that Progressive's internal control over financial reporting was effective as of December 31, 2008. The complete "Management's Report on Internal Control over Financial Reporting," as required by Section 404 of The Sarbanes-Oxley Act of 2002 and applicable SEC regulations, along with the related report of PricewaterhouseCoopers LLP, is presented in the 2008 Annual Report to Shareholders, which is attached as an Appendix to Progressive's 2009 Proxy Statement.

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of The Progressive Corporation:

We have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of The Progressive Corporation and its subsidiaries as of December 31, 2008 and 2007, and the related consolidated statements of income, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2008 (not presented herein) appearing in The Progressive Corporation's 2008 Annual Report to Shareholders, which is attached as an Appendix to The Progressive Corporation's 2009 Proxy Statement; and in our report dated February 25, 2009, we expressed an unqualified opinion on those consolidated financial statements.

In our opinion, the information set forth in the accompanying condensed consolidated financial statements is fairly stated, in all material respects, in relation to the consolidated financial statements from which it has been derived.

PricewaterhouseCoopers LLP

Cleveland, Ohio
February 25, 2009

Safe Harbor Statement Under the Private Securities Litigation Reform Act of 1995

Statements in this report that are not historical fact are forward-looking statements that are subject to certain risks and uncertainties that could cause actual events and results to differ materially from those discussed herein. These risks and uncertainties include, without limitation, uncertainties related to estimates, assumptions, and projections generally; inflation and changes in economic conditions (including changes in interest rates and financial markets); the financial condition of, and other issues relating to the strength of and liquidity available to, issuers of securities held in our investment portfolios and other companies with which we have ongoing business relationships, including counterparties to certain financial transactions; the accuracy and adequacy of our pricing and loss reserving methodologies; the competitiveness of our pricing and the effectiveness of our initiatives to retain more customers; initiatives by competitors and the effectiveness of our response; our ability to obtain regulatory approval for requested rate changes and the timing thereof; the effectiveness of our brand strategy and advertising campaigns relative to those of competitors; legislative and regulatory developments; disputes relating to intellectual property rights; the outcome of litigation pending or that may be filed against us; weather conditions (including the severity and frequency of storms, hurricanes, snowfalls, hail, and winter conditions); changes in driving patterns and loss trends; acts of war and terrorist activities; our ability to maintain the uninterrupted operation of our facilities, systems (including information technology systems), and business functions; court decisions and trends in litigation and health care and auto repair costs; and other matters described from time to time in our releases and publications, and in our periodic reports and other documents filed with the United States Securities and Exchange Commission. In addition, investors should be aware that generally accepted accounting principles prescribe when a company may reserve for particular risks, including litigation exposures. Accordingly, results for a given reporting period could be significantly affected if and when a reserve is established for one or more contingencies. Also, our regular reserve reviews may result in adjustments of varying magnitude as additional information regarding pending loss and loss adjustment expense reserves becomes known. Reported results, therefore, may be volatile in certain accounting periods.

Common Shares

The Progressive Corporation's common shares (symbol PGR) are traded on the New York Stock Exchange. Progressive currently has an annual variable dividend policy. We expect the Board to declare the next annual variable dividend, subject to policy limitations, in December 2009, with a record date in January 2010 and payment shortly thereafter. A complete description of our annual variable dividend policy can be found at: progressive.com/dividend.

Quarter	Stock Price High	Low	Close	Rate of Return	Dividends Declared per Share
2008					
1	$ 19.84	$ 15.00	$ 16.07		$ —
2	21.31	16.11	18.72		—
3	20.71	15.70	17.40		—
4	17.59	10.29	14.81		—
	$ 21.31	$ 10.29	$ 14.81	(21.9)%	$ —
2007					
1	$ 24.75	$ 20.91	$ 21.82		$ —
2	25.16	21.55	23.93		2.000
3	24.10	18.88	19.41		—
4	20.50	17.26	19.16		.145
	$ 25.16	$ 17.26	$ 19.16	(12.6)%	$ 2.145

Corporate Information

Principal Office
The Progressive Corporation
6300 Wilson Mills Road
Mayfield Village, Ohio 44143
440-461-5000
progressive.com

Annual Meeting The Annual Meeting of Shareholders will be held at the offices of The Progressive Corporation, 6671 Beta Drive, Mayfield Village, Ohio 44143 on April 24, 2009, at 10 a.m. eastern time. There were 3,847 shareholders of record on December 31, 2008.

Shareholder/Investor Relations Progressive does not maintain a mailing list for distribution of shareholders' reports. To view Progressive's publicly filed documents, shareholders can access our Web site: progressive.com/sec. To view our earnings and other releases, access progressive.com/investors.

To request copies of Progressive's publicly filed documents free of charge, write to: The Progressive Corporation, Investor Relations, 6300 Wilson Mills Road, Box W33, Mayfield Village, Ohio 44143, e-mail: investor_relations@progressive. com or call: 440-395-2258.

For financial-related information, call: 440-395-2222 or e-mail: investor_relations @progressive.com.

For all other Company information, call: 440-461-5000 or e-mail: webmaster@ progressive.com.

Counsel Baker & Hostetler LLP, Cleveland, Ohio

Corporate Governance Progressive's Corporate Governance Guidelines and Board committee charters are available at: progressive.com/governance, or may be requested in print by writing to: The Progressive Corporation, Investor Relations, 6300 Wilson Mills Road, Box W33, Mayfield Village, Ohio 44143.

Transfer Agent and Registrar
REGISTERED SHAREHOLDERS If your Progressive shares are registered in your name, contact National City Bank regarding questions or changes to your account: National City Bank, Shareholder Services Operations Dept. 5352, P.O. Box 92301, Cleveland, Ohio 44193-0900. Phone: 1-800-622-6757 or e-mail: shareholder.inquiries@nationalcity.com.

BENEFICIAL SHAREHOLDERS If your Progressive shares are held in a brokerage or other financial institution account, contact your broker or financial institution directly regarding questions or changes to your account.

Contact Non-Management Directors Interested parties have the ability to contact the non-management directors as a group by sending a written communication clearly addressed to the non-management directors and sent to any of the following:

Peter B. Lewis, Chairman of the Board, The Progressive Corporation, 6300 Wilson Mills Road, Mayfield Village, Ohio 44143 or e-mail: peter_lewis@progressive.com.

Charles E. Jarrett, Corporate Secretary, The Progressive Corporation, 6300 Wilson Mills Road, Mayfield Village, Ohio 44143 or e-mail: chuck_ jarrett@progressive.com.

The recipient will forward communications so received to the non-management directors.

Accounting Complaint Procedure Any employee or other interested party with a complaint or concern regarding accounting, internal accounting controls, or auditing matters relating to Progressive may report such complaint or concern directly to the Chairman of the Audit Committee, as follows:

Stephen R. Hardis, Chairman of the Audit Committee, stephen_ hardis@progressive.com.

Any such complaint or concern also may be reported anonymously over the following toll-free Alert Line: 1-800-683-3604 or online at www.progressivealertline.com. Progressive will not retaliate against any individual by reason of his or her having made such a complaint or reported such a concern in good faith. View the complete procedures at progressive.com/governance.

Whistleblower Protections Progressive will not retaliate against any officer or employee of Progressive because of any lawful act done by the employee to provide information or otherwise assist in investigations regarding conduct that the employee reasonably believes to be a violation of Federal Securities Laws or of any rule or regulation of the Securities and Exchange Commission or Federal Securities Laws relating to fraud against shareholders. View the complete Whistleblower Protections at progressive.com/governance.

Charitable Contributions Progressive contributes annually to The Progressive Insurance Foundation, which provides: (i) financial support to the Insurance Institute for Highway Safety to further its work in reducing the human trauma and economic costs of auto accidents, and (ii) matching funds to eligible 501(c)(3) charitable organizations to which Progressive employees contribute.

Registered Trademarks Net Promoter® is a registered trademark of Satmetrix Systems, Inc. All other registered trademarks used within this report are registered to The Progressive Corporation or its subsidiaries.

Online Annual Report and Proxy Statement Our 2008 Annual Report to Shareholders, in an interactive format, can be found at: progressive.com/annualreport.

We have also posted copies of our 2009 Proxy Statement and 2008 Annual Report to Shareholders, in a "PDF" format, at: progressiveproxy.com.

Directors and Officers

Directors

Charles A. Davis[4,5,6]
Chief Executive Officer,
Stone Point Capital LLC
(private equity investing)

Roger N. Farah[3,6]
President and Chief Operating Officer,
Polo Ralph Lauren Corporation
(lifestyle products)

Stephen R. Hardis[1,2,5,6]
Non-Executive Chairman of the Board,
Marsh & McLennan Companies, Inc.
(financial services)

Bernadine P. Healy, M.D.[1,6]
Health Editor and Medical Columnist,
U.S. News & World Report
(publishing)

Jeffrey D. Kelly[2,4,6]
Former Chief Financial Officer,
National City Corporation
(commercial banking)

Abby F. Kohnstamm[1,6]
President and Chief Executive Officer,
Abby F. Kohnstamm & Associates, Inc.
(marketing consulting)

Peter B. Lewis[2,4,6,7]
Chairman of the Board

Norman S. Matthews[3,5,6]
Consultant,
former President,
Federated Department Stores, Inc.
(retailing)

Patrick H. Nettles, Ph.D.[1,6]
Executive Chairman,
Ciena Corporation
(telecommunications)

Glenn M. Renwick[2]
President and
Chief Executive Officer

Donald B. Shackelford[4,6]
Retired, former Chairman,
Fifth Third Bank, Central Ohio
(commercial banking)

Bradley T. Sheares, Ph.D.[3,6]
Former Chief Executive Officer,
Reliant Pharmaceuticals, Inc.
(pharmaceuticals)

[1]Audit Committee member
[2]Executive Committee member
[3]Compensation Committee member
[4]Investment and Capital Committee member
[5]Nominating and Governance Committee member
[6]Independent director
[7]Non-executive chairman

Corporate Officers

Glenn M. Renwick
President and
Chief Executive Officer

Brian C. Domeck
Vice President and
Chief Financial Officer

Charles E. Jarrett
Vice President, Secretary,
and Chief Legal Officer

Thomas A. King
Vice President and Treasurer

Jeffrey W. Basch
Vice President and
Chief Accounting Officer

Mariann Wojtkun Marshall
Assistant Secretary

Peter B. Lewis
Chairman of the Board
(non-executive)

24-Hour Insurance Quotes, Claims Reporting, and Customer Service

	Private passenger autos, motorcycles, and recreational vehicles	**Commercial autos/trucks**
To Receive a Quote	1-800-PROGRESSIVE (1-800-776-4737) progressive.com	1-888-806-9598 progressivecommercial.com
To Report a Claim	1-800-274-4499 progressive.com[1]	1-800-274-4499
For Customer Service If you bought your policy through an independent agent or broker	1-800-925-2886 (1-800-300-3693 in California) progressiveagent.com	1-800-444-4487 progressivecommercial.com
If you bought your policy directly through Progressive online or by phone	1-800-PROGRESSIVE (1-800-776-4737) progressive.com	1-800-895-2886 progressivecommercial.com
If you have a complaint or concern regarding any claim handling or other claims-related issue[2]	1-800-274-4641 e-mail: claims@email.progressive.com	1-800-274-4641 e-mail: claims@email.progressive.com

[1]Claims reporting via the Web site is currently only available for private passenger auto policies.

[2]Any policyholder, claimant, or other interested party who has any complaint or concern regarding any claim handling or other claims-related issue may report such claim using the contact information above. The complaint or concern will be promptly forwarded to the appropriate management personnel in our claims organization for review and response.

expect the unexpected

Photography
All images are gelatin silver prints,
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Design
Nesnadny + Schwartz,
Cleveland + New York + Toronto

Printing
AGS Custom Graphics

This publication was printed at an FSC-certified printer (Certification No. SW-COC-001530). The FSC Label identifies products that contain wood from well-managed forests certified in accordance with the rules of the Forest Stewardship Council. Acid-Free, recycled and recyclable papers were employed throughout this publication.

"Innovation
is the ability
to see
change

as an
opportunity

not a threat."

anonymous