

Message from the Chairman and President

We are pleased to report an earnings recovery in 1988 as compared with our 1987 loss. Income before a change in accounting for income taxes was \$23,733,000 in 1988 (\$1.80 per common share or \$1.75 per fully diluted share) compared to a loss of \$18,144,000 (\$1.32 per common share) in 1987. This past year securities gains were a major factor with recorded net pre-tax gains of \$21,099,000 from securities transactions compared to net losses of \$3,848,000 in 1987. The increased earnings also reflect the effects of our additional investments in PHLCORP, Inc. ("Phlcorp") and BRAE Corporation ("Brae") which in 1988 became consolidated subsidiaries. At December 31, 1988 consolidated assets exceeded \$2 billion.

During 1988 many significant transactions occurred. In February we completed a tender offer for additional Phlcorp common shares and Leucadia's interest in Phlcorp increased from 39% at December 31, 1987 to 64% at December 31, 1988. We invested additional funds in Brae and increased our ownership from 49% at December 31, 1987 to 74% (79% if certain warrants are exercised) at December 31, 1988. As a result of the conversion of the Empire Insurance Company ("Empire") from a mutual company to a stock company and other transactions, Leucadia had an effective interest in Empire of 58% at the end of 1988. During 1988 Leucadia also sold at a profit all or a portion of its interests in the common stock of Minstar, Inc., Oxford First Corp. and several of the companies we had interests in as a result of our association with The Jordan Company. We also entered into an agreement to sell our interest in certain properties located in San Luis Obispo County, California for \$22,000,000; we expect the sale to close in the second quarter of 1989 for a pre-tax gain in excess of \$16,000,000.

During 1989 we acquired additional shares in Cambrian & General Securities p.l.c. ("Cambrian") which, when added to our holdings at December 31, 1988 represent approximately 74% of Cambrian's voting interest. Funding for this

investment was through a special purpose bank facility. We believe that our investment in Cambrian will prove to be profitable.

The Annual Report on Form 10-K filed with the SEC is a part of this report. You are referred there for additional information. However, certain comments on each of our operating divisions follows.

Life Insurance:

Our life insurance operations are principally conducted through Charter National Life Insurance Company of St. Louis ("Charter"), which sells a variety of tax advantaged life insurance products. The tax treatment of Charter's most successful product was changed during the year on a prospective basis. In anticipation of such change, we emphasized the sale of another product which was not subject to this tax uncertainty. The net result was a small decrease in premium revenues from 1987 levels. We account for our insurance products on a very conservative basis and will continue to do so when new accounting principles, which are required for 1989, are implemented. Including a subsidiary, Charter now writes business in all 50 states. In 1989 Charter expects to market a tax advantaged policy which will meet the requirements of the new tax law.

Property And Casualty Insurance:

During 1988 Empire became a consolidated subsidiary. Empire writes personal and commercial lines of insurance almost exclusively in New York. Empire is an unusual casualty company in that it does not sacrifice profitability for market share; in addition, it has been very successful at controlling operating costs. While earnings in 1988 were excellent, the casualty insurance business has historically been very cyclical. Nevertheless, we are cautiously optimistic about the future.

Manufacturing:

The Manufacturing Division produces a variety of products including bathroom vanities, bonded fiber products, plastic netting products, insulation

products, electrical cord sets, bulk wood fiber, office divider panels and electronic signs. Brae's subsidiary, American Sign & Indicator Corporation, joined the group in 1988. Although the Manufacturing Division had lower profits in 1988 (due to higher raw material costs and start up costs of new equipment and facilities resulting in manufacturing inefficiencies) we remain encouraged by the division's excellent return on investment and this year's prospects.

Banking, Real Estate and Leasing:

This division includes our Salt Lake City based national bank and thrift operations, the railcar leasing business, principally conducted through Brae, and computer leasing. The national bank had a higher average investment in loans during 1988 and also opened a new branch and several loan production offices. During 1989 the bank intends to expand by making automobile financing loans to individuals with prior credit problems. We believe this business, properly controlled, can be successful. We also invested additional funds in owned railcars and, as a result of the additional investment in Brae, increased our interest in its railcars.

Trading Stamps:

The trading stamps business is conducted by The Sperry and Hutchinson Company, Inc. ("S&H"), a subsidiary of Phlcorp. Although the trading stamps industry has been in a declining trend for a number of years, and S&H has reduced its operations in response, 1988 operating results were good. In 1989 S&H was informed that its largest customer would discontinue the distribution of trading stamps in the second quarter. S&H believes it will

be able to develop plans which will reduce, but not eliminate, the effect of this lost business.

Motivation Services:

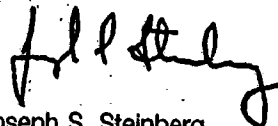
The motivation services business is conducted through S&H Motivation, Inc., a subsidiary of Phlcorp. This segment operated at a break-even in 1988 after instituting a cost cutting program. New management has implemented plans which we believe will lead to future growth and profitability.

A frequent comment concerning Leucadia is that our financial statements and reports are complicated and difficult to understand. We agree, but unfortunately this complexity follows from our business strategy. We tend to be buyers of companies that are troubled or out of favor and as a result are selling substantially below the values which we believe are there. We then work at improving the acquired operations with a view to increasing cash flow and profitability. From time to time we sell parts of these operations when prices available in the market reach what we believe to be advantageous levels. While we are not perfect in executing this strategy, we are proud of our long term track record. We are not income statement driven and do not run your Company with an undue emphasis on either quarterly or annual earnings. We believe that we are conservative in our accounting practices and policies and that our balance sheet is conservatively stated.

The accomplishments of this year required great effort on the part of many. We thank our employees and advisors for the work they have done on behalf of our shareholders. We also thank our bank lenders for their continuing support. We continue to be optimistic about the future of your Company.



Ian M. Cumming
Chairman



Joseph S. Steinberg
President