

2001

Letter from the Chairman and President

To Our Shareholders

In 2001, Leucadia lost \$7.5 million, the third loss in the 24 years we have been managing this enterprise. We have an explanation, which does not excuse the loss. It involves the arcane intricacies invented by the accounting profession to supposedly make financial reporting more realistic. In 2001, the fruits of their efforts resulted in our only picking up as income a small portion of the \$60 million in cash we received from the FINOVA transaction (described in our SEC filings) and requiring us to write off \$94.4 million of investment in FINOVA stock we got for free and never thought was worth much to begin with. To further complicate matters (which are not the accountants' doing) we wrote off our remaining investment in Empire Insurance Group, about which more later. Empire resulted in an after-tax loss of \$72.7 million. On the plus side was the release of \$36.2 million of previously accrued tax contingencies that are no longer necessary. Happily the \$60 million and the \$94.4 million from the FINOVA transaction are being recognized in income as FINOVA repays its loan. The detailed footnotes are on pages F-12 through F-14. The chart below attempts to explain the P & L in greater detail.

Here is what happened.

(In millions)	
Revenues ^(a) ^(b)	\$375.3
Expenses	(321.6)
Income	53.7
Taxes, net ^(c)	16.6
Income after tax	70.3
Other:	
Minority expense	(5.5)
Empire losses ^(d)	(72.7)
Accounting changes	.4
Net Loss as reported (GAAP)	\$(7.5)
Earnings to be reported in future periods as the Berkadia loan is repaid:	
FINOVA stock loss	\$82.1
Accrued FINOVA cash fees	52.2
Taxes at 35%	(47.0)
After-tax future earnings	\$87.3

(a) Includes a loss of \$94.4 million on 25% of FINOVA's common stock, acquired for no additional consideration in connection with Berkadia's loan to FINOVA, which will be amortized back into income as the Berkadia loan is paid down by FINOVA. \$12.3 million of this amount was amortized into income in 2001.

(b) Includes just \$7.8 million of the \$60 million of cash fee (points) paid to Leucadia for Berkadia's loan to FINOVA. The balance was deferred and will be amortized into income as the FINOVA loan is repaid.

(c) Includes \$36.2 million release of previously accrued tax contingencies.

(d) This is all related to Empire, which is being discontinued. See Empire below.

Empire

First, a mercifully short history of the rise and fall of the Empire Insurance Group. We obtained control of Empire in early 1988, it had a statutory net worth of \$63.2 million. By December 31, 1997, its statutory net worth peaked at \$180 million. A good portion of the increase in net worth resulted from redundant reserves (which means we paid less in claims than we had originally expected to pay). The redundancies began to evaporate in 1995, but we did not realize the importance of this fact at the time. A couple of years earlier we had made what became the fatal decision. We dramatically expanded our private passenger auto book of business in New York City, the Bermuda Triangle for insurance companies. We believed we could underwrite bad drivers at high prices and make money. We were wrong. Looking through the rear view mirror, our prices were not high enough to overcome bad drivers, endemic medical fraud, poor systems and equally overconfident competitors. At December 31, 2001, the statutory net worth was \$23.2 million and shrinking. Our decision to discontinue Empire's operations and Empire's operating loss resulted in a total loss of \$72.7 million for the year. If there is a recovery at the end of this saga, it will be a tiny one and a miracle. The best thing about this unfortunate journey is that it is over.

This difficult job has been accomplished under the leadership of Bud Scruggs and a remarkable group of young executives he has recruited and mentored. Bud has been heard to muse: "This job feels like following elephants in a parade!"

Bermuda

You are being asked at the shareholders' meeting to consider changes to allow Leucadia to move its domicile to Bermuda. The proxy statement has a detailed description of what needs to be done to accomplish this. There is also an explanation of how the move will affect shareholders.

Why are we advocating this? Over the years, we have made successful investments not only in the United States, but also in England, France, Argentina, Barbados, Bolivia and El Salvador. We currently have ongoing investments in Barbados, France, Spain and Russia; in Russia we have lost money so far. When the successful investments were realized, we would have paid tax on the gain, were it not for our net operating loss carryforwards. Those loss carryforwards are gone now and are irreplaceable. As a Bermuda company, Leucadia would be able to reinvest these profits without an intervening U.S. corporate level tax. This resulting benefit is at the heart of what we are paid to do—increase shareholder value. The United States is almost alone in taxing corporate worldwide income even if earned outside the United States. Putting this in dollars and cents means that if we make a good investment from Bermuda and sell the investment at a gain, there will be no corporate level tax due on the profit. If, for example, as a Bermuda company we were to make a profit of \$500 million on the sale of a particularly successful investment, Leucadia would save more than \$175 million in corporate level taxes (at current U.S. rates), or over \$3.00 per share. Shareholders will continue to be liable for taxes on dividends and capital gains. Leucadia will continue to pay taxes on its U.S. operations.

If approved at our shareholders meeting in May, the move to Bermuda may not take place immediately. There is a U.S. tax to be paid by the Company at the time of the move to Bermuda that is dependent on the price of our stock versus the value of our assets. We do not intend to implement the move unless the tax cost is reasonable. Furthermore, the move to Bermuda will also impose some additional restrictions on stockholders owning more than 1% of the shares of the Company (currently 553,000 shares equals one percent). Existing shareholders will not be required to sell any stock. The purpose of these additional restrictions also has to do with taxes. The proxy statement goes into this in greater detail. Please read it carefully before voting. We're voting "yes".

Recently, there has been much sound and fury about Bermuda from several politicians, both Republican and Democrat. They claim that such moves are in some way nefarious and even un-American. We strenuously disagree.

The United States is a nation of laws. Our elected representatives make the laws and we obey them. We don't make laws, they do, and we don't interpret laws, judges do. In 1947, Judge Learned Hand wrote, "Over and over again courts have said that there is nothing sinister in so arranging one's affairs as to keep taxes as low as possible. Everybody does so, rich and poor, and all do right, for nobody owes any public duty to pay more than the law demands: taxes are enforced exactions, not voluntary contributions."¹

Even before Judge Hand's learned opinion, Justice George Sutherland delivered an opinion of the U.S. Supreme Court which in part read, "The legal right of a taxpayer to decrease the amount of what otherwise would be his taxes, or altogether avoid them, by means which the law permits, cannot be doubted."²

Banking and Lending

Leucadia's banking and lending operations are principally conducted through American Investment Bank, N.A. (AIB), a national bank subsidiary, and American Investment Financial (AIF), an industrial loan corporation. AIB and AIF deposits are insured by the FDIC. Together AIB and AIF had deposits of \$476.5 million at December 31, 2001. Consolidated loans of the two entities at December 31, 2001, were \$521.2 million. AIB's largest market segment is sub-prime auto loans, consisting of loans to individuals who have difficulty obtaining credit, with the principal secured by used and moderately priced automobiles. For taking this risk, AIB charges higher rates of interest. In 2001 the average initial loan balance was \$12,250 and the yield was 21.5%; in an earlier day competition allowed 24%.

AIF is a small lender to non-prime boat and recreational vehicle buyers and also, until recently, made loans guaranteed by the Small Business Administration.

Beginning in the second half of 2000, we noticed an increase in losses and delinquencies in the auto portfolio. This increase, we thought, could be explained by the deteriorating economic conditions in the United States. Customers who are at the bottom of the economic ladder have little protection in the face of a slowing economy and their behavior represents a leading indicator of things to come. In response, we reduced loan originations significantly by tightening underwriting standards and eliminated marginal auto dealer relationships and territories. We managed the business so that AIB's assets would be flat in 2001, after growing 55% to \$544 million in 2000. Caution was in order.

However, the adverse trends continued during 2001, and despite our efforts of cutting costs and being more selective in underwriting loans, profitability continued to deteriorate.

As a result, in September 2001, AIB stopped originating new sub-prime automobile loans. At year-end 2001, additional reserves were added to account for the closing of the Indianapolis collection office. This has not been a bad business, just not good enough for the current risks versus the rewards.

We continue to service our existing loan portfolios. We will also seek to acquire loan portfolios that meet our credit criteria. If over the next several years these institutions cannot find profitable lending niches, or portfolio purchases, the invested capital should be repatriated to Leucadia.

¹ COMMISSIONER V. NEWMAN, 159 F2D 848, 850-851 (CA2 1947)

² GREGORY V. HELVERING, Commissioner of Internal Revenue, 293 U.S. 465, 468 (1935)

Manufacturing

Conwed Plastics is a leading manufacturer of proprietary lightweight plastic netting used for a variety of purposes including construction, agriculture, packaging, carpet padding, filtration and consumer products. The products are primarily used to add strength to other materials as in carpet padding, or to act as a barrier as in warning fences, or as crop protection from birds. This is a business where Conwed's netting is engineered into 1000's of other manufacturers' products.

Conwed markets its products both domestically and internationally, with approximately 13% of its 2001 sales exported to Europe, Latin America, Japan and Australia. The Company primarily sells its products through an employee sales force, which is located in the United States and Europe.

Results are as follows.

(In millions)	1997	1998	1999	2000	2001
Sales	\$50.9	\$56.6	\$64.0	\$65.0	\$53.7
Pre-tax profits	8.9	10.1	11.9	11.3	7.8
Return on net invested assets	32.5%	29.5%	31.9%	23.3%	13.8%
Return on average equity	37.8%	39.7%	42.2%	28.7%	16.5%

Conwed is our old economy thermometer. As you can see from the chart above, it tracks what is going on in the real economy, not to be confused with the enthusiast's economy, which resides on Wall Street.

Conwed continues to be profitable and is working on being more so—dedicated to the proposition that being a low cost producer is great in good times and bad. Some of the erosion in the return on average equity and return on net invested assets is the result of our increased investment in the Belgium plant. We decided, probably prematurely, to build a European plant in 1999. It is up and running, but does not yet have enough business to be profitable. We think it was the right decision, which will eventually pay off.

There is a recent small but measurable increase in our sales to carpet cushion manufacturers over same period sales to this segment last year. This might indicate a slight uptick in the old economy or might indicate that new carpeting is an affordable luxury in a down economy.

Kudos to Conwed for leading the way in the fight to keep as many costs variable and to exact more productivity from the costs that are not!

Winery

Leucadia owns two wineries: Pine Ridge in Napa Valley, California and Archery Summit in the Willamette Valley, Oregon. Pine Ridge was acquired in 1991 and Archery Summit was started from scratch in 1993. The wineries produce and sell ultra-premium and luxury wines, \$25–\$135 per bottle. Archery Summit's case sales are less than its production capacity. To date, Archery Summit has been able to sell all its production at very high prices. The challenge will be to continue to do so as production continues to increase.

In 2001, Gary and Nancy Andrus, our partners and founders of Pine Ridge, decided they wanted to sell out. Leucadia agreed to buy their interest and now owns 100%. Gary is going to pursue other interests and we wish him well. Nancy will continue on at Pine Ridge in marketing.

During 2000, these wineries sold 79,300 9-liter equivalent cases for \$14.4 million. During 2001, 68,900 9-liter equivalent cases were sold for \$12.8 million. The fourth quarter is usually a large revenue period for our wineries, and the events of 9/11 certainly resulted in lower wine sales, which has continued in 2002.

George Scheppler has joined us as the new President and CEO of the wineries. George's entire career has been spent in the wine business. For sixteen years, George has been working for the wine interests of the Baron Philippe de Rothschild, with the last 10 of those years as co-CEO of Opus One, a French/American joint venture winery and preeminent luxury goods wine brand. We welcome him and look forward to the implementation of his exciting plans for the future. In the meantime, wines of both Pine Ridge Winery and Archery Summit Winery continue to receive great reviews by the wine press.

Remember—wine is food; it has biblical antecedents. One glass each day of Pine Ridge or Archery Summit wine extends life and makes your fellow shareholders happy.

Depending upon your state liquor laws, you may order wine through the mail or on the Internet at www.pineridgewinery.com or www.archerysummit.com. Both wineries are quite beautiful from spring through the fall grape crush. Come visit and taste! Call Pine Ridge at (800) 575-9777 or Archery Summit at (800) 732-8822 and tell them you are a shareholder and ask for a tour.

MK Gold

MK Gold is traded on the NASD OTC Bulletin Board; Leucadia owns 72.8%. MK Gold owns Cobre Las Cruces, S.A., a Spanish company that owns the Las Cruces copper deposit in the Pyrite Belt of Spain. As a result of approximately 280 drill holes totaling over 82,000 meters, proven and probable reserves are estimated at 15.8 million metric tonnes grading 5.94% copper. A feasibility study completed by Bechtel International, Inc., estimates the capital cost will be approximately \$290 million to bring the mine into production. Operating costs are estimated at \$.33/lb of copper. Mining will be subject to permitting and obtaining both debt and equity financing for the project. A mining concession application, accompanied by the feasibility study and an environmental impact study, was submitted to the applicable governmental agencies during the first quarter of 2001. As of this writing at the end of March 2002, the process of obtaining the permits continues. There is no reason to believe it will not be issued, but we knoweth not when. Prayers for high copper prices are also in order.

FINOVA

FINOVA, a financial services holding company that emerged from bankruptcy in August 2001, is 50% owned by Berkadia, a joint company owned by Berkshire Hathaway Inc. and Leucadia. Berkadia made FINOVA a \$5.6 billion loan to finance FINOVA's chapter 11 plan. Leucadia has guaranteed 10% of Berkadia's borrowings to fund the FINOVA loan. Leucadia has a ten-year management agreement with FINOVA and Larry Hershfield, a Leucadia employee, is the chief executive of FINOVA.

Leucadia owns, through Berkadia, 25% of FINOVA's common stock, receives \$4 million of the management fee yearly, plus interest received on 10% of the Berkadia loan, less 10% of Berkadia's cost of funds. Leucadia also received \$60 million of the \$120 million in fees charged to FINOVA for the loan.

Since its chapter 11 restructuring, FINOVA's business activities have been limited to the orderly collection and liquidation of its assets and is not engaged in any new lending activities. Cash generated by these activities is used to pay operating expenses and interest on all the FINOVA debt and then the principal of the Berkadia loan. As of this writing, the loan is paid down to \$3.9 billion.

The bulk of FINOVA's loans were to less than prime credits. After 9/11, significant additional reserves for impairment were taken, mainly on the hospitality and transportation portfolios. It is Leucadia's belief that the Berkadia loan will be paid in full, but FINOVA's other outstanding debt is substantially impaired and there will be nothing left for FINOVA's shareholders.³

Real Estate

FIDEI is a 100%-owned French subsidiary headquartered in Paris. When acquired, the Company had over 150 properties:

1999: 62 properties sold for pretax gain of \$37.9 million

2000: 38 properties sold for pretax gain of \$27.1 million

2001: 26 properties sold for pretax gain of \$8.2 million

At December 31, 2001, 27 properties aggregating 858,000 square feet remain, with a book value of \$28.7 million. These remaining properties should be sold during 2002. While the real estate is being liquidated, we are investigating selling the company, which has some French tax attributes. So far we have enjoyed a return of 19.7% on our original investment of \$67 million. Our thanks to Zalmie Jacobs, Luis Medeiros, Jean-François Delepouille and Jean-Frédéric Lambert.

At December 31, 2001, the Company's domestic real estate had a book value of \$146 million. The most significant real estate investments are:

- A loan to and a residual equity interest in a master-planned community in San Diego County with 3,400 entitled residential units that are being developed by HomeFed Corporation. We also have a loan to HomeFed and a preferred equity interest in one of their projects.
- A 719-room hotel located on Waikiki Beach, called the Aston Waikiki Beach Hotel, which is being renovated. Rooms are available from \$65 to \$95 per night on Expedia.com and are selling briskly.
- Several small shopping centers that we are in the process of selling.
- Partial interest in the Brooklyn Marriott Hotel and an adjoining office building and parking structure. Empire profitably sublet its space in the office building to the United States Secret Service, who needed the space subsequent to 9/11, and to the New York City Board of Education.

We believe that these properties are worth something more than their carrying value.

Money and Other Things

At December 31, 2001, excluding amounts held by regulated subsidiaries, Leucadia has cash, cash equivalents and marketable securities of \$805 million, plus \$163.8 million in cash and securities collateralizing letters of credit. At December 31, 2001, Leucadia had credit facilities of \$152.5 million, of which none was drawn. Total parent company debt, which excludes non-recourse debt of subsidiaries, was \$194.5 million. Except for our investment in Berkadia described above, we are not responsible for the indebtedness of any of the partnerships and other companies in which we have investments.

During 2001, we repurchased none of our common stock.

³ The stock is on our books for zero.

In 2000, Leucadia invested \$100 million in JPOF II, a limited liability company that is a registered broker-dealer. JPOF II is managed and controlled by Jefferies & Company, and makes markets in high yield bonds. For the year ended December 31, 2001, Leucadia recorded \$27.1 million of pretax income from this investment. Our thanks to the team.

In 2001, we invested \$75 million in White Mountains Insurance Group, Ltd. (WTM-NYSE), for 375,000 common shares or about 4% of this Bermuda-domiciled financial services holding company. At December 31, 2001, these shares had a market value of \$130.5 million.

In 2001, the Company invested \$127.5 million for approximately 25% of the common stock in Olympus Re Holdings, Ltd., a newly formed Bermuda reinsurance company, primarily engaged in property excess, marine and aviation reinsurance. Joe Steinberg is its Chairman. This company was formed with the intention of benefiting from the expected increase in reinsurance pricing subsequent to 9/11. At the end of two years each shareholder has an option to withdraw if the shareholder believes prices for reinsurance are headed south as they seemingly always do. Though prices are definitely up, this investment is exposed to the usual risks reinsurance companies subject themselves to. Olympus' reinsurance contracts generally do not cover losses resulting from terrorist attacks, except for certain personal lines contracts. We will be carefully watching the Weather Channel beginning in late August.

Since 1982, we have invested an aggregate of \$105 million in various entities owned or controlled by Jay Jordan and David Zalaznick. As of December 31, 2001, we have received \$166.1 million back. Also at December 31, 2001, we hold interests in 45 Jordan/Zalaznick companies, carried at \$59 million on our books, of which \$43.8 million relates to public companies carried at market value.

The Future

2001 was a confusing year. It began with equity prices in the markets falling toward their historical means. We do better when markets are below their historical means, but we do little when they are far above. To our surprise, earlier this year there was a reversal of the downward trend towards the mean. Prices in the markets strengthened and the Federal Reserve and others announced the recession to be over. Time will tell whether this turns out to be true.

Our personal view is that there is a disconnect. The real economy is still in a period of readjustment whereby the ebullient speculative economy, i.e., the stock markets, are struggling mightily to maintain prices that suggest continued high growth rates that we do not think are sustainable.

Meanwhile, we continue to forage for undervalued or underappreciated investments. For what it is worth, we are busier this year than last, and although we usually are not high bidders, recently we have been closer to winning than losing and have bought a few small investments. We started at Leucadia together in 1978, with \$53,000 which we borrowed on our credit cards. We have been enormously fortunate for which we are grateful beyond words. But we are 24 years older, richer and probably a bit lazier (at least one of us) and undoubtedly more conservative. We hope our shareholders find themselves in the same situation.

In the past Leucadia has occasionally invested a large percentage of its net worth in the purchase of a single investment. (For example, Avco in 1984, Baldwin United in 1986 and Colonial Penn in 1991.) It is hard to imagine investing the same percentage again in a single investment with our net worth today of \$1.2 billion. We are intuitively most comfortable with investments in the \$100-\$200 million range. What that means is that we must not only find and manage good investments, but also multiples of them. To this end we are developing, successfully we think, several executives and teams who have the talent for sniffing out the extraordinary investment opportunity. If we cannot invest in compelling values, we prefer to leave Leucadia's money in the bank.

Complicating our efforts is the fact that there is more competition for the good deal than ever before. Traditional private equity funds have veered into our areas of expertise as well as hedge funds. An enormous amount of money has been raised for investing in distressed assets. All of this continues to make our job harder.

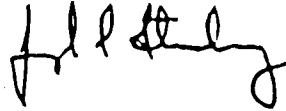
The "when are you going to slow down" bell has rung several times this year in one of our households! For the time being we are ignoring the peal.

We and our able staff and advisors will continue the search for attractive, safe investments that, over time, will return higher yields than those generally available in the market. If we are unsuccessful in our search, we and our fellow shareholders ought to give the money to someone else to manage.

After 24 years, this is still fun!



Ian M. Cumming
Chairman



Joseph S. Steinberg
President