0014

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Mark R. Thresher
Executive Vice President,
Chief Financial Officer
Nationwide

November 17, 2011

Via E-Mail and UPS Next Day Air

Hon. Michael F. Consedine
Commissioner of Insurance
Pennsylvania Insurance Department
1345 Strawberry Square
Harrisburg, PA 17120

Re: Proposed Merger of Harleysville Mutual Insurance Company into Nationwide Mutual Insurance Company

Dear Commissioner Consedine:

Nationwide Mutual is writing in response to the letter Liberty Mutual sent to your attention on October 12, 2011 (the "Liberty Letter") regarding the proposed merger of Harleysville Mutual with Nationwide Mutual (the "Proposed Merger").[1] At Nationwide, we strongly believe the proposed combination of the two companies benefits all stakeholders, is a fair and compelling transaction, and meets the standards for approval by the Pennsylvania Insurance Department in accordance with the standards set forth in Section 991.1402 of Title 40 of the Pennsylvania Statutes.

In our view, the Liberty Letter is inaccurate in many respects and mistakenly characterizes the Proposed Merger. We note the following:

- The Proposed Merger is a traditional merger of two mutual insurance companies, and the policyholders of Harleysville Mutual will benefit by becoming members and policyholders in a substantially stronger and better diversified company with higher ratings.

- Unlike policyholders, who continue to benefit after completion of the Mergers, the interests of public stockholders are extinguished at the time of the Mergers in exchange for cash consideration.

[1] The Proposed Merger provides for the merger of Harleysville Mutual Insurance Company, a Pennsylvania mutual insurance company ("Harleysville Mutual"), with and into Nationwide Mutual Insurance Company, an Ohio mutual insurance company ("Nationwide Mutual"), and the simultaneous merger (the "Subsidiary Merger") of a subsidiary of Nationwide Mutual, Nationals Sub, Inc., a Delaware corporation ("Merger Sub"), with and into Harleysville Group Inc., a Delaware corporation ("HGI"), with the result that HGI will become a wholly owned subsidiary of Nationwide Mutual (the Proposed Merger and the Subsidiary Merger are hereinafter collectively referred to as the "Mergers").

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- Contrary to Liberty's assertion, it is common for mutual insurance companies to have stock subsidiaries and for control of such subsidiaries to change as a result of a mutual merger.

- The agreed market premium is appropriate and within the range of comparable transactions. Under the most widely used valuation metric for industry transactions, at least 21 comparable precedent transactions since 1995 contemplate Price-to-Book Value ratios in excess of that which is contemplated in the Proposed Merger.

- With respect to the evaluation of acquisition proposals, HGI is governed by the law of Delaware while Harleysville Mutual is governed by the law of Pennsylvania. There are dramatic differences in the laws of these jurisdictions on this point, which Liberty's analysis ignores.

As set forth in more detail below, Nationwide respectfully requests that the Pennsylvania Insurance Department reject both Liberty's incorrect statements and its specific requests and take no further action with respect to the Liberty Letter.

Liberty admits that, as a result of the consummation of the Proposed Merger, the policyholders of Harleysville Mutual will become members of Nationwide Mutual with "ostensibly" the same voting, liquidation and distribution rights with respect to Nationwide Mutual as the other policyholders of Nationwide Mutual. Section 2.2(c) of the Agreement and Plan of Merger (the "Merger Agreement") dated as of September 28, 2011, by and among Nationwide Mutual, Harleysville Mutual, Merger Sub, and HGI, expressly states that the policyholders of Harleysville Mutual will become policyholders of Nationwide Mutual and, as such, will become members of Nationwide Mutual and will have the same voting, liquidation and distribution rights with respect to Nationwide Mutual as the other policyholders of Nationwide Mutual.

Liberty asserts that the Proposed Merger "differs significantly" from traditional mutual to mutual mergers solely because Harleysville Mutual owns approximately 54% of the shares of HGI, a publicly traded insurance holding company. However, contrary to Liberty's assertion, the Proposed Merger <u>is</u> a traditional merger of two mutual insurance companies, and the policyholders of Harleysville Mutual will benefit by becoming members and policyholders in Nationwide Mutual, a substantially stronger company from a financial point of view for several reasons. First, as a result of the Mergers, Nationwide will have a group surplus of approximately $13 billion, or over ten times that of Harleysville. Second, Nationwide Mutual enjoys a higher rating than Harleysville Mutual. Harleysville Mutual's current financial strength rating is 'A' by A.M. Best Company and 'A-' by Standard & Poor's, whereas Nationwide Mutual's current rating is 'A+' by each of A.M. Best Company and Standard & Poor's. Following announcement of the proposed transaction, A.M. Best placed Harleysville Mutual and its affiliates' ratings under review with positive implications, and Standard & Poor's upgraded the outlook on the companies' ratings from "stable" to "positive." Third, Nationwide Mutual is better diversified, including geographically, with a national risk pool with less concentrated catastrophe exposure; from a product perspective, based on Nationwide's diversified financial services model across the property and casualty, life and retirement markets; and from a financial perspective. Furthermore, Harleysville Mutual policyholders will benefit from a more complete line of products and our national service support.

The fact that Harleysville Mutual owns a majority interest in HGI does not make the Proposed Merger contemplated by the Merger Agreement "highly unusual." To the contrary, it is common for mutual insurance companies to have stock subsidiaries and for control of such subsidiaries to change as a result of the mutual merger.

Liberty's statement that there is divergent treatment of the public stockholders of HGI versus the members of Harleysville Mutual compares apples to oranges and finds them to be different. The transactions involve two very different legal entities with two very different constituents: a mutual insurance company incorporated in Pennsylvania with policyholders and members (but no stockholders) and a public company incorporated in Delaware, the stockholders of which, as such, may or may not be policyholders or members of the mutual insurance company. The benefits of the Proposed Merger to the members and policyholders of Harleysville Mutual are significant and traditional for a merger of two mutual insurance companies. Significantly, but ignored by the Liberty Letter, those benefits continue <u>after</u> the Mergers have been completed, but the interests of the public stockholders of HGI, as such, are extinguished at the time of the Mergers in exchange for the cash consideration of $60 per share. In fact, Liberty acknowledges that it is not unusual for no consideration to be paid to members in connection with a "traditional" merger of two mutual insurance companies and there is certainly no legal requirement that a policyholder dividend or other consideration be paid in connection with such a merger.

The Liberty Letter makes much of the premium to the market price to be paid to HGI's public stockholders under the Merger Agreement. The market premium is one valuation metric and captures the price paid to public shareholders relative to the closing price of the stock on any given day but does not take account of intrinsic, or franchise, value. An equally important valuation metric for property and casualty merger and acquisition transactions is the Price-to-Book Value ratio, which equals 2.1x for the Subsidiary Merger based on the latest available book value as of June 30, 2011. Based on a review of comparable precedent transactions, there have been at least 21 transactions since 1995 with Price-to-Book Value ratios in excess of 2.0x.

Liberty also makes inaccurate comparisons regarding the market premium. First, Liberty makes a wholly inappropriate comparison of the market premium against that paid in "going private" transactions in which the majority stockholder was buying out the minority public stockholders. The "precedent transactions" referenced by Liberty are simply not comparable to the transaction proposed by Nationwide, which is not affiliated with Harleysville Mutual and is not a stockholder, majority or otherwise, of HGI.

0014

Second, the Liberty Letter arbitrarily calculates the premium for the HGI shares against the market price on September 22, 2011, but disregards the recent trading history of the stock. Consistent with the broader market and its peers, HGI's common stock traded with significant volatility during the period that Nationwide was engaged in discussions with Harleysville. As a mutual insurer focused on long-term value creation, Nationwide has taken a long-term view of the intrinsic value of HGI that has been consistent regardless of short-term movements in the stock market.

The most relevant time period to evaluate the market premium was from February through April of 2011, when most of the price discussions were held. During this time, Nationwide developed its valuation of HGI that would not change unless new information was discovered in due diligence that would suggest a different intrinsic value. While the stock market turned south in the summer and early fall, due diligence conducted in that time frame revealed no commensurate diminution in fundamental value and, accordingly, no adjustment to the price was made. The acquisition Price-to-Book Value ratio remained virtually unchanged at 2.1x from February through announcement. In contrast, the market premium, which was impacted by heightened volatility in the stock market generally, varied daily and changed considerably during this period. If the market premium was calculated on March 1, when the closing price per share was $36.13, the premium would have been 66%. Two months later, on May 2, the premium would have been 89% based on a closing price of $31.70. Despite these market fluctuations, nothing at Harleysville had fundamentally changed over this time period to affect its intrinsic value.

Similar price-to-book ratios and, in many cases, high market premiums have been paid in precedent transactions in which, as here, there is a strong strategic rationale. Nationwide views the transaction as highly important from a strategic perspective given that the combination with Harleysville (i) significantly expands Nationwide's independent agency ("IA") platform, particularly in the attractive small and middle market commercial segment; (ii) substantially grows Nationwide's IA presence in the Northeast region; and (iii) represents a unique opportunity to join with an organization that shares a strong philosophical and cultural "fit" and mutual heritage.

The Liberty Letter also makes much of the fact that the Merger Agreement provides the Board of Directors of HGI with a so-called "fiduciary out", but does not provide a similar right for the Board of Directors of Harleysville Mutual. The reason for the absence of a "fiduciary out" for the Board of Directors of Harleysville Mutual is simple – it is not required by Pennsylvania law. The Liberty Letter fails to note that "fiduciary outs" are required by the so-called "Revlon duties" imposed by Delaware law on directors of public companies incorporated in Delaware, such as HGI. Harleysville Mutual, on the other hand, is incorporated in Pennsylvania, the law of which expressly disclaims the imposition of "Revlon duties." For this reason, the board of directors of a Pennsylvania corporation, such as a mutual insurance company incorporated in Pennsylvania, is permitted to approve a merger transaction without

03

0014

"fiduciary outs." Simply put, the Liberty Letter ignores the dramatic differences between the law of Delaware, applicable to HGI, and the law of Pennsylvania, applicable to Harleysville Mutual.

Liberty's hypothetical regarding a "Superior Proposal" is fundamentally flawed. The hypothetical references the "same merger consideration" to the public stockholders of HGI but fails to note that a competing offer with even modest additional consideration could become a "Superior Proposal" if HGI and Harleysville Mutual were able to attract such a competing offer. Acceptance of a "Superior Proposal," as defined in the Merger Agreement, allows the Board of Directors of HGI to terminate the Merger Agreement, which terminates the obligations of Harleysville Mutual with respect to the Proposed Merger as well. Liberty also fails to note that if the Board of Directors of HGI terminates the Merger Agreement in accordance with the "fiduciary out" provisions, HGI, but not Harleysville Mutual, is obligated to pay a "break-up" fee of $29,588,535 and reimburse Nationwide Mutual for its expenses, also typical for a public company acquisition.

For the foregoing reasons, Nationwide respectfully requests that the Pennsylvania Insurance Department approve the Proposed Merger in accordance with the standards set forth in Section 991.1402 of Title 40 of the Pennsylvania Statutes and reject Liberty's inaccurate factual and legal objections.

Should you have any questions, please do not hesitate to contact me at 614-249-6950.

Sincerely,

Mark R. Thresher
Chief Financial Officer
Nationwide

cc: Robert A. Kauffman, Harleysville Mutual

03