

# Risk: Our business

2016 saw a number of significant economic and geo-political developments across the globe, most notably the historic Brexit decision and the recent US federal elections. These developments point to a continuation of the uncertain political and economic environment in which we operate, and highlight the increasing importance of a robust approach to the identification, measurement and management of risk.

QBE is fully committed to ensuring that we apply a disciplined approach to risk management and that our risk management practices and systems are robust, independent and aligned with global best practice. QBE's Enterprise Risk Management (ERM) framework is outlined in QBE's Risk Management Strategy and is supported by frameworks for each risk class, including strategic, insurance, operational, credit, market and liquidity risks. All risk categories are managed through Board governance, an approved risk appetite set by the Board, scenario analysis and stress testing and robust capital management. The ERM framework is applied across the Group and provides a sound foundation for reducing uncertainty and volatility in business performance.

## Risk appetite

Our risk appetite forms the basis of QBE's ERM framework and represents the level of risk that the Board and management are prepared to accept in pursuit of the organisation's objectives. Risk appetite is aligned to, and is considered in, all strategic and business planning decisions QBE makes and we monitor our exposures against the risk appetite on an ongoing basis.

## Governance

The Board plays a significant role in the ERM framework. The Board is responsible for ensuring that an effective risk management strategy is implemented and for defining

the risk appetite boundaries within which risk must be managed. The Board is supported by the Board Risk and Capital Committee which meets at least quarterly and is responsible for overseeing active and appropriate management of risks according to the stated risk appetite, strategy and business plans.

QBE manages risk in accordance with the "three lines of defence" governance model. The first line is responsible for managing the risk that arises as a result of activities undertaken in our risk-taking businesses. The second line includes the risk management and compliance functions which are responsible for the maintenance and monitoring of risk management frameworks, as well as the measurement and reporting of risk performance and compliance. The third line is provided by the internal audit function, which is responsible for providing independent assurance to the Board and its various audit and risk committees that risk management and internal control frameworks are working as designed. Having defined responsibilities across all three lines of defence ensures that QBE adopts a coordinated approach to risk management and that accountabilities are clear for our staff.

## Stress and scenario testing

We use stress and scenario testing to better understand our risk profile under a range of different scenarios. Assessing the impact of extreme but plausible events

helps us to better prepare for such situations and ensures that our risk exposure is acceptable to the Board.

QBE also uses sophisticated modelling techniques to estimate potential losses, manage exposure and assist in making decisions regarding risk management and coverage. This capability is critical to managing our exposure to possible events, such as natural catastrophes and economic shocks.

### Emerging risks

We recognise that the risk environment changes and evolves over time. Existing risks develop in new or unexpected ways and new risks, which are usually characterised by incomplete but developing knowledge, materialise. QBE operates emerging risk forums across the Group to identify and monitor these emerging risks, analyse their potential impact and develop strategies to mitigate or exploit opportunities.

### Capital management

Capital management is another key component of the ERM framework and aims to achieve the appropriate balance between our risk appetite and the amount of capital required to support each of our businesses. QBE uses a number of capital management tools to support the assessment of risk and allocation of capital including:

- QBE's Economic Capital Model – QBE's internal model, developed to measure overall exposure to risk as well as exposure to each of our main categories of risk, provides a quantitative base for us to understand, monitor and manage our exposures. We also use the model to make better business decisions, assess economic capital requirements and measure performance on a risk-adjusted basis.
- Analysis of regulatory and rating agency capital models – to better understand how regulatory and rating agencies assess the impact of our strategic decisions on our risk profile and capital requirements, we conduct financial modelling analysis with reference to the requirements of the various capital environments in which QBE operates.
- A number of bespoke risk assessment tools – we use catastrophe models, scenario analysis, stress tests and reverse stress tests to evaluate business plans and support our capital plan.

Another key capital management tool is QBE's Internal Capital Adequacy Assessment Process (ICAAP). The ICAAP is supported by both the Economic Capital Model and scenario analysis, and is used to:

- manage the capital held by QBE;
- monitor the risk profile against appetite;
- ensure the risks taken by QBE are commensurate with required returns;
- allocate capital to operating entities for planning and performance monitoring purposes; and
- analyse alternative reinsurance options and regulatory and rating agency submissions.

Several actions were completed during 2016 as part of our proactive management of QBE's risk profile. These included reinsurance of long-tail run-off reserves in our European and North American divisions to reduce potential future volatility in our result and balance sheet; full assessment and modelling of the Group's reinsurance arrangements to support the 2017 placements; and restructuring of our borrowings to achieve greater capital efficiency.

### Business performance oversight

As well as proactive and formalised engagement of the risk function in the review and oversight of the strategic and business planning process, we continue to apply stress and scenario testing to our performance against plan, incorporating scenario analysis to identify and quantify the risks to our business. This allows us to proactively consider the various exposures we may face as an organisation and determine what additional mitigation or remediation activities may be required.

### Risk culture

QBE defines risk culture as observable patterns of behaviour in the way employees perform their work and the judgements they take, as it relates to risk. Risk culture is an integral component of QBE's ERM framework and, like other components of the framework, we continuously enhance our risk culture approach. We are currently focusing on achieving greater alignment between risk culture, the wider organisational culture and conduct risk, as well as further embedding first line accountability for risk culture, including through remuneration and reward. This is in addition to our ongoing initiatives to maintain a strong risk culture across the Group.

### Investment, market, credit and liquidity risk

QBE actively manages its exposures to investment, market and credit risks that arise inherently from the management of a global insurance operation, including risks generated through:

- the management of a global investment portfolio;
- regular insurance activities and exposure to reinsurance counterparties; and
- global treasury operations, including exposures to foreign exchange movements, collateral management and bank counterparty risks.

Risks to earnings due to material market movements, risk concentrations and changes to credit quality are identified, measured and controlled. These are subject to risk management frameworks and oversight within defined Board-approved risk appetites that are monitored via limits structures and specific delegated authorities.

In 2016, we have made further improvements to our risk systems that will lead to an improved risk analytics capability which will further inform our decision-making process and enable improved risk-return decisions.

QBE's liquidity risk framework is designed to ensure that QBE has sufficient high-quality liquid assets at all times, including at times of severe stress, to meet our liabilities as they fall due. Liquidity risk is monitored against specified limits within the Board-approved risk appetite and supporting processes ensure that contingency plans are in place to address crisis situations.

### Regulatory risk

As a global insurance group, QBE is subject to oversight by approximately 30 prudential regulatory regimes around the world, as well as extensive legal and regulatory requirements and obligations, industry codes and business and ethical standards across its business activities. To manage the regulatory and compliance risk we face as a global organisation, we combine local expertise with a globally consistent compliance framework.