Strong performance in challenging conditions

Elaine Whelan
Group Chief Financial Officer

In 2017, we carried a little bit more of a capital buffer than we typically would – a bit of an insurance policy given the market conditions we were dealing with. That strategy served us well and our balance sheet remains strong.

Lancashire produced a loss for the year. What drove that?
There were a number of significant and costly catastrophe events in 2017 – Hurricanes Harvey, Irma and Maria, two Mexican earthquakes plus the Californian wildfires being the larger events and the ones with the most impact on Lancashire's performance. We have therefore produced a return on equity of negative 5.9 per cent and a comprehensive loss of $66.2 million. Given the nature of our book, and that 2017 could end up being one of the costliest natural catastrophe years on record, we are actually pretty pleased with the way our book performed. Our loss experience across these events was very much in line with expectations. Overall, for these events we have recorded a net loss after recoveries and reinstatement premiums of $189.2 million, with our equity pick-up from our investment in Kinesis also included in that number. Looking forward to 2018 we do expect to benefit from the post-loss improved pricing environment.

How does the Group establish reserves for such significant events?
It's quite an involved process. Our CUOs and Active Underwriters work with our claims and actuarial teams to establish which lines of business are impacted. There is then a detailed review on an account-by-account basis by our underwriting teams, in conjunction with claims, to identify the individual accounts which may be exposed. With a combination of experience, history and feedback from the brokers and clients themselves, they put together a preliminary estimate of loss per client. The gross loss is then fed through our various reinsurance programmes to get to a net loss position. This goes through a rigorous internal review process and we overlay our view of the industry loss size. Lastly, all of this is provided to the Reserve Committee who review and challenge the underlying estimates.

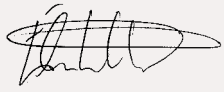
"Given the nature of our book, and that 2017 could end up being one of the costliest natural catastrophe years on record, we are actually pretty pleased with the way our book performed."

What does that mean for Lancashire's capital position?

We always work out the business we want to write and then we work out the capital we need to support that. We add a buffer on top of that and typically any excess is returned to shareholders. In 2017, we carried a little bit more of a capital buffer than we typically would – a bit of an insurance policy given the market conditions we were dealing with. That strategy served us well and our balance sheet remains strong. Given current expectations of post-loss pricing, we expect to fully utilise our current capital base. As a result, we did not declare a special dividend in 2017. Depending on loss activity in 2018, a better rating environment should lead to better returns.

Have the events had any impact on the Group's strategy?

In short, no. Our goal has always been to maximise risk-adjusted returns for our shareholders across the cycle. Our strategy remains to manage the cycle appropriately and match our capital to the underwriting opportunity. Over the last few years we have reduced our top line and bought more reinsurance as the market softened. In 2018 we expect to be able to take advantage of the post-loss pricing environment.



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Group Chief Financial Officer

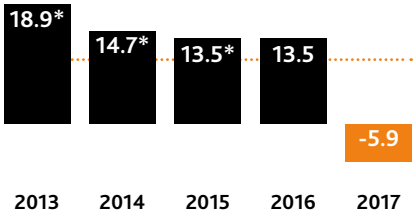
Financial highlights

	2017 $m	2016 $m	2015 $m	2014 $m	2013 $m
Gross premiums written	**591.6**	633.9	641.1	907.6	679.7
Net premiums written	**398.0**	458.7	481.7	742.8	557.6
Net premiums earned	**427.9**	488.1	567.1	715.6	568.1
Net insurance losses	**335.4**	142.5	155.7	226.5	188.1
Net underwriting (loss) income	**(23.1)**	213.5	265.2	335.7	254.2
Net investment income	**30.5**	29.8	29.8	28.6	25.4
Net realised gains (losses) and impairments	**9.1**	(2.4)	(2.8)	(5.9)	12.6
Net operating (loss) profit	**(86.0)**	144.0	173.4	231.9	184.2
(Loss) profit after tax	**(71.1)**	153.8	181.1	229.3	222.5
Net change in unrealised gains/losses on investments	**4.9**	4.1	(11.3)	(2.1)	(32.5)
Comprehensive (loss) income	**(66.2)**	157.9	169.8	227.2	190.0
Dividends[1]	**29.9**	178.9	317.5	321.0	325.6
Diluted (loss) earnings per share	**($0.36)**	$0.76	$0.91	$1.16	$1.17
Diluted operating (loss) earnings per share	**($0.43)**	$0.71	$0.87	$1.17	$0.97
Fully converted book value per share	**$5.48**	$5.98	$6.07	$6.96	$7.50
Return on equity	**(5.9%)**	13.5%	10.9%	13.9%	18.9%
Return on equity excluding warrant adjustments	**(5.9%)**	13.5%	13.5%	14.7%	18.9%
Net loss ratio	**78.4%**	29.2%	27.5%	31.7%	33.1%
Net acquisition cost ratio	**27.0%**	27.1%	25.8%	21.4%	22.1%
Expense ratio	**19.5%**	20.2%	18.8%	15.6%	15.0%
Combined ratio	**124.9%**	76.5%	72.1%	68.7%	70.2%
Accident year loss ratio	**94.2%**	46.2%	46.0%	35.9%	36.1%
Net total return on investments[2]	**2.5%**	2.1%	0.7%	1.0%	0.3%

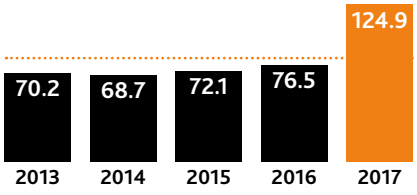
(1) Dividends are included in the financial statement year in which they were recorded.
(2) Net return on investments includes internal foreign exchange hedge.

Key performance indicators

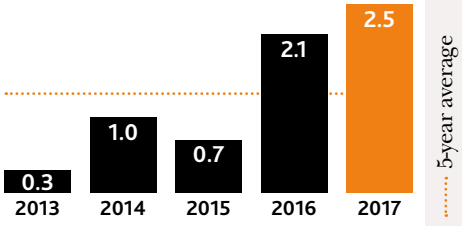
	Return on equity	Combined ratio	Total investment return
Measurement	The return on equity is measured by management as the internal rate of return of the change in fully converted book value per share in the period, adjusted for dividends.	The combined ratio is the ratio of costs to net premiums earned and is a measure of an insurance company's operating performance. It is calculated as the sum of the loss ratio, the acquisition cost ratio and the expense ratio. These ratios are defined in our glossary.	Total investment return measures investment income and net realised and unrealised gains and losses produced by the Group's managed investment portfolio.
Aim	The Group's aim is to provide shareholders with a risk-adjusted return on equity of 13 per cent in excess of the risk-free rate over the longer term.	The Group aims to price its business to ensure that the combined ratio across the cycle is significantly less than 100 per cent.	The Group's primary investment objectives are to preserve capital and provide adequate liquidity to support the Group's payment of claims and other obligations. Within this framework we aim for a degree of investment portfolio return.
Performance	**-5.9%**	**124.9%**	**2.5%**



A significant level of loss activity in 2017 has resulted in a negative RoE for the year for the first time since we began underwriting in 2006.



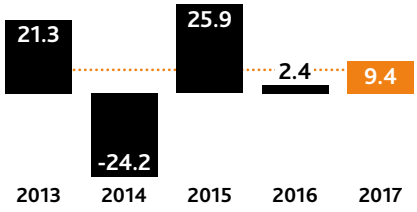
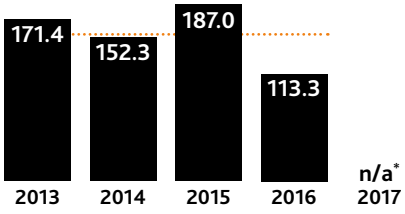
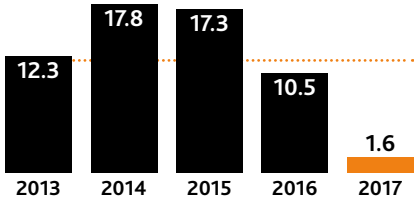
In 2017, we witnessed the occurrence of three major hurricanes (Harvey, Irma and Maria), two earthquakes in Mexico as well as wildfires in California. The high combined ratio in 2017 reflects the impact of these losses. Whilst there was a higher than usual sequence of catastrophe loss events in 2017 the impact of these was not outsize or unexpected for the Group or its stakeholders.



In 2017, Lancashire continued to monitor risk-on/risk-off volatility and maintained the allocation to risk assets in the surplus portfolio as a hedge against the interest rate risk inherent in the significant fixed maturity allocation of the portfolio.

Risk management	The stated aim is a long-term goal, acknowledging that management expects both higher and lower results in the shorter term. The cyclicality and volatility of the insurance market is expected to be the largest driver of this pattern. We seek to align our variable remuneration to shareholders' interests by having a RoE component in this. Please refer to the Directors' Remuneration Report on page 60 for further details.	The Group's underwriters assess likely losses, using models, their experience and knowledge of past loss experience, industry trends and current circumstances. This allows them to estimate the premiums sufficient to meet likely losses and expenses. Peer reviews of risks are conducted through the daily underwriting call or peer review, depending on risk impact, enabling the Group to ensure careful risk selection, limits on concentration and appropriate portfolio diversification. The RRC then monitors performance at a portfolio level.	The investment strategy places an emphasis on the preservation of invested assets and provision of sufficient liquidity for the prompt payment of claims, in conjunction with providing a reasonably stable income stream. These objectives are reflected in the Group's investment guidelines and its conservative asset allocation. Management reviews the composition, duration and asset allocation of the investment portfolio on a regular basis in order to respond to changes in interest rates and other market conditions.

* RoE including the impact of warrants was 10.9% in 2015, 13.9% in 2014 and 18.9% in 2013. The five-year average was 10.3%.

	Total shareholder return $	Percentage of comprehensive income returned to shareholders	Dividend yield
Measurement	Total shareholder return is measured in terms of the internal rate of return of the increase/decrease in share price in the period, measured in U.S. dollars and adjusted for dividends.	The percentage of comprehensive income returned to shareholders equals the total capital returned to shareholders through dividends and share repurchases paid in a given year, divided by the Group's comprehensive income.	Dividend yield is measured by dividing the annual dividends per share by the share price on the last day of the given year.
Aim	The Group's aim is to maximise RoE over the longer term and we would expect that to be reflected in our share price and multiple. This is a long-term goal, recognising that the cyclicality and volatility of both the insurance market and the financial markets in general will impact management's ability to maximise the share multiple in the immediate term.	The Group aims to carry the right level of capital to match attractive underwriting opportunities, utilising an optimal mix of capital tools. Over time, through proactive and flexible capital management across the cycle, we aim to generate optimum returns for shareholders.	The Group aims to maintain a strong balance sheet whilst generating an attractive risk-adjusted return for shareholders. Lancashire's dividend yield demonstrates our ability to operate nimbly through the cycle through the active capital management that underpins our business model. We aim to pay annual ordinary dividends, and when we decide not to retain our profits as additional underwriting capital we return them to shareholders by way of special dividends.
Performance	**9.4%**  The share price benefited from an uptick towards the end of the year due to positive expectations for the (re)insurance market following the run of catastrophe losses.	**n/a***  Following the costly catastrophe events in 2017, Lancashire took the decision not to pay a special dividend in order to retain capital to support potential business opportunities in the post-loss market. * The Group made a comprehensive loss of $66.2 million during 2017. We paid annual ordinary dividends of $0.15 per share. Due to 2017 being n/a, the average is calculated over 4 years.	**1.6%**  During 2017, we paid annual ordinary dividends of $0.15 per share.
Risk management	The Lancashire remuneration structure and RSS ensure that staff are highly motivated and closely aligned to the Group's goals, and therefore with shareholders. Permanent staff are all eligible to receive RSS awards. The participation of employees in the RSS ensures that there is a strong focus on sustainable long-term shareholder value.	Risk tolerances are set at a level that aims to prevent the Group incurring losses that would impair its ability to operate. The Group's key capital measure is its A.M. Best rating, and a minimum rating of A– is considered necessary to attract business. In 2017, Lancashire maintained its A rating.	As capital continues to accumulate in the (re)insurance market, the need to be nimble is more important than ever. This means being ready to deploy capital quickly when it is needed and having the discipline to return it when it is not. The Group has to ensure that all shareholders understand that in harder markets the Group will want to retain, and potentially even raise, capital to take full advantage of underwriting opportunities.

$ *KPI linked to Executive Directors' remuneration. For more information see pages 60 to 79.*

Adapting to the cycle

We have always been very candid about our underwriting approach. Our aim as underwriters has always been to find the appropriate balance between risk and return. This underwriting philosophy has never changed since our formation, however it does mean that at each stage of the market cycle our underwriting tactics change.

In recent years we have been able to ignore the pressure for top-line premium growth, focusing on maintaining a core portfolio of risks and protecting this portfolio with tailored, and increasingly more comprehensive, reinsurance products. When the price you receive for the risk reduces, the amount of risk you take should also reduce.

Rates in almost all of our product lines have been declining year-on-year making it more and more difficult to produce acceptable underwriting margins. We, like all of our peers, have clearly benefited from what has been a benign period over a number of years for natural catastrophe insured loss events. However, in non-natural catastrophe exposed lines we have also been able to continue to deliver underwriting margins, which the broader market has struggled to achieve, through disciplined underwriting and superior risk selection. The benign loss environment in natural catastrophe exposed lines has certainly masked rating deficiency elsewhere. So despite soft market conditions we were still able to achieve sector-leading underwriting results across our underwriting platforms by maintaining underwriting discipline.

The benign natural catastrophe environment was never going to continue forever, and the broader market was able to hide behind the profits generated by catastrophe business throughout this benign period. At some point this was going to end, and in the third quarter of 2017 this benign loss environment came to an abrupt halt with the three land-falling hurricanes, namely Harvey, Irma and Maria, as well as Mexico experiencing two major earthquakes. These losses were promptly followed by a fourth, if rather less significant, hurricane (Nate) and some of the costliest wildfires ever seen in California. In addition to these there were also major flood events in South East Asia and devastating mudslides in Columbia.

Mother Nature has certainly reminded our industry of the devastation and cost she can deliver. Every time there are catastrophe losses there seems to be something 'unique' about the loss or losses. By now we should realise the next loss or run of losses will always be different from the last.

First, these losses are devastating from a human perspective with millions of people's lives impacted by these cruel events. Second, the broader economic impact of these events, particularly in areas such as the Caribbean, are also incredibly damaging with lasting implications for these local economies. Third, the impact to our industry has been significant. It is likely that when the final bill is added up 2017 will be only the third year on record with natural catastrophe insured losses in excess of $100 billion and quite possibly the costliest in history, and in any year this is a true test for the industry.

As a Group we have always had significant exposure to natural catastrophe risk across all of our platforms via a number of our reinsurance and insurance product lines. These events are a real test of our risk management capabilities as they are at the heart of our major product lines. When there are losses of this frequency and magnitude we obviously expect to incur losses across all of our platforms. At our inception one of our strategic objectives was to make an underwriting profit four years in every five, therefore acknowledging that there will be years where we will make an underwriting loss. We have been able to achieve an underwriting profit every year for the past 11 years, so whilst this year will be the first exception to this, in the context of our original target we have performed remarkably well.

Paul Gregory
Group Chief Underwriting Officer

"Mother Nature has certainly reminded our industry of the devastation and cost she can deliver. Every time there are catastrophe losses there seems to be something 'unique' about the loss or losses. By now we should realise the next loss or run of losses will always be different from the last."

Part of our disciplined underwriting strategy over the past few years has been to ensure that when we experience loss events such as those in 2017, we perform in line with our various stakeholders' expectations and remain in a position to be responsive to our clients' and brokers' needs. First, we need to be able to pay our clients' claims expeditiously. Second, we need to be in a position to continue to provide these clients with ongoing support. Third, we want the underwriting platforms to be in a robust position to broaden our underwriting appetite and client base should the market conditions dictate.

I am very pleased that after experiencing these events we have achieved these aims and remain in a position to respond appropriately to our clients' current and future needs. As much as we have been prepared to narrow our portfolio in soft market conditions, we are equally prepared to broaden our portfolio in improving market conditions.

So as we look forward into 2018 we are very well positioned as a Group to service and support our existing clients and portfolio. We have the platforms and the people to ensure we maximise whatever underwriting opportunities manifest themselves.

Property Reinsurance

2017 certainly bucked the recent trend of benign loss years. The market received a stark reminder of the havoc and cost that Mother Nature can deliver. All of the various hurricane, flood, fire and earthquake events of 2017 tested the global reinsurance and retrocession markets. It was not just the quantum of these losses but the frequency. After a number of years of rate reductions and broadening terms and conditions these losses come at a time that really tests the robustness of the market. Thus far it looks like the market will be able to respond to these losses as our customers would expect with claims being paid, however the dynamics of the market are now likely to change, albeit not to the extent we would like to see.

The structure of the reinsurance market in recent years has subtly changed, with the growth of ILS funds in the sector, predominantly into the retrocession space. It is fair to say that the 2017 losses are the first true test for a lot of this 'new' capacity and much like traditional rated paper there will be some that respond better than others. There is no doubt that retrocession pricing is going up, whether that be rated paper or ILS paper. This will flow through to the property reinsurance market as retrocessional costs increase.

There will of course be differentiation, with loss-impacted territories and clients sharing more of the cost burden than those territories and clients that were not loss impacted.

No one can predict exactly how much better the market will be in 2018 for these classes of business but what we do know is the softening has currently stopped and pricing is improving. The extent to which it does is very much dependent upon both the development pattern of the losses, and as always the dynamic between demand and supply.

As a Group we are very well placed to access all sectors of the reinsurance market so will be able to maximise whatever opportunity there is. We have the option of both rated paper, either company market or Lloyd's, and collateralised products via Kinesis, providing our clients with the full suite of reinsurance options. We have an established position and reputation in the property reinsurance market with deep broker and client relationships to benefit from any improved market conditions. As always the Group will look to take risk that is appropriate to the opportunity.

Property Direct & Facultative

Much like the property reinsurance market the story for the direct property market in 2017 was dominated by the significant natural catastrophe events. Years of relatively benign conditions had led to increased competition in this sector, which inevitably had led to rating pressure across all elements of the portfolio, albeit more so for the open market business than the more stable binder business. As in other sectors of the market this pricing pressure had taken the margin from the portfolio. As a result, when events with the frequency and severity of those experienced in 2017 occur, the underwriting results will be in the red.

The D&F portfolio within the Group is primarily written from our Lloyd's platform and much like other lines of business this has shrunk as market conditions softened. The portfolio has de-risked in certain territories as rates and conditions became unsustainable. Given the 2017 industry loss events this has justified the decision as the losses incurred to the Group would have undoubtedly been larger if risk levels had not been reduced.

Following the losses there is likely to be positive rating movement during 2018 on our existing Direct & Facultative portfolio and also the opportunity to grow in areas where in recent years we have shrunk, for example Mexico and the Caribbean. We expect this to be predominantly within the open market D&F sphere as the binder book is traditionally a more stable portfolio although this will also benefit from better rating conditions. The extent of any growth will obviously be dictated by the extent of the opportunity as we look to balance risk and return appropriately.

Energy

The 'perfect storm' of a low oil price and historically high levels of upstream energy market capacity witnessed during 2015 and 2016 continued in 2017, albeit with an oil price that was far more stable and a client base whose necessary cost cutting had largely been achieved. The stabilisation of the oil price meant that the demand side of the equation held up during 2017. Whilst the upstream energy market did not see a huge uptick in demand there were not any further reductions and there are a few early signs of some demand coming back into the system with a small number of construction projects coming to market and a number of our clients gradually increasing activity.

With the supply dynamic unchanged, i.e. historically high levels of market capacity, there was still pressure on rates as competition for a much reduced pot of premium continued amongst markets. The Group's strategy has been to maintain our core portfolio of profitable business as rates are now approaching levels last seen in the late 1990s and, considering that in 2012 rates were not far from historical highs, this shows how steep the fall in energy rates has been in the space of only a few years.

2017, however, was relatively benign for the upstream energy market in terms of significant claims although some prior year major losses did develop negatively, highlighting the volatility of the class. This benign loss year has helped mask the underlying weakness of energy rates and any return to a 'normalised' loss year would likely render the current rating environment unsustainable from a macro-market perspective. Whilst the natural catastrophe events of 2017 have not directly impacted the upstream energy market they are large enough to alter the direction of the energy reinsurance market, which will filter through to the direct market as reinsurance costs increase. With this dynamic in place we fully expect market conditions to improve during 2018. The Group has access to energy business from both the Lancashire Companies and Lloyd's platforms, which primarily will focus on servicing existing clients' needs. However, should market conditions dictate, we have the people and the platforms to grow our energy portfolio further.

"Following the losses there is likely to be positive rating movement during 2018 on our existing Direct & Facultative portfolio and also the opportunity to grow in areas where in recent years we have shrunk, for example Mexico and the Caribbean."

"The Group is able to offer significant capacity across multiple platforms to ensure we are providing both clients and brokers with fully rounded products and services, which allows us to maintain our underwriting principles despite the many challenges the market contains."

Marine

The marine market was relatively stable during 2017 with rates across areas of our marine portfolios remaining reasonably static.

Within the cargo market a number of London market participants exited the class during 2017, which aided this stability. The natural catastrophe events later in the year also impacted the cargo market given the exposure that this portfolio has to these kinds of events. Fortunately for us our portfolio performed admirably given the make-up of the book which has been deliberately designed to try to mitigate natural catastrophe exposures where possible. We expect these loss events to improve the cargo market during 2018 with rates reacting positively.

Outside of cargo, our hull, builders' risk and ancillary marine products portfolio performed steadily and we maintained our position on all our key accounts. This portfolio has been our most stable since our inception with our risk appetite clearly defined, which has allowed us to deliver sector-leading results for what is a notoriously difficult area to generate underwriting returns. Whilst the natural catastrophe events of 2017 have no direct impact on the insurance lines we write it will impact the broader reinsurance market so we expect stability in this market to continue through 2018.

Aviation

The aviation market, much like the marine market, has historically been a difficult place to deliver respectable underwriting returns. Fortunately as a Group we have consistently been able to do this across all of our platforms. In a soft but more stable market in 2017 we continued to deliver underwriting profits. We access both the direct and reinsurance market across the Group's platforms so have excellent visibility of the entire sector.

Throughout the year there were a few green shoots of hope that the market had found a more viable level, particularly in the direct lines such as war. Market capacity has yet to retract, however, so as always until the demand/supply dynamic alters there is unlikely to be any material improvement in market conditions. That said there has been a general recognition within the market, most notably post the natural catastrophe events of the third quarter of 2017, that the softening needs to stop. The rating environment for the broader market has now stabilised, much like other non-catastrophe lines, although it is still not at a level to sustain any quantum of normalised loss levels. We are confident that, at the very least, this stability of market conditions will continue through 2018.

Terrorism, Political Violence & Political Risks

As in recent years the world continued to be a volatile place during 2017. There were numerous terrorist attacks across the globe in cities including London, Manchester, Barcelona, Paris and Stockholm as well as ongoing wars and civil disruption in many countries including Syria, Libya, Afghanistan, Iraq and Yemen. In addition, we have seen political tensions escalate between North Korea and the U.S. with the sabre-rattling intensifying. Despite these terrorism events and wars being horrific from a loss of life perspective, the impact on the insurance market has been minimal as they have created very few actual insured losses.

This global political and socio-economic climate certainly creates challenges for underwriting these classes of business, and risk selection remains absolutely crucial as years of softening rates means that there is little margin to cater for any type of attritional losses. Given this, and as with other classes of business, we have built up a profitable core portfolio of business, which in the softer market we have successfully retained. If the significant loss events of 2017 lead to a broader hard market then our leadership capabilities in these classes would allow us to develop our portfolio quickly and we have the appetite to do so.

The Group is able to offer significant capacity across multiple platforms to ensure we are providing both clients and brokers with fully rounded products and service which allows us to maintain our underwriting principles despite the many challenges the market contains.

Ready to deliver, in all conditions

Hayley Johnson
Chief Underwriting Officer, LUK

Sylvain Perrier
Chief Underwriting Officer, LICL

Jon Barnes
Active Underwriter, Syndicate 2010

John Spence
Active Underwriter, Syndicate 3010

Business environment and outlook

2017 was characterised by a significant level of loss activity. With the occurrence of hurricanes Harvey, Irma and Maria, the Mexican earthquakes and the California wildfires, the industry has incurred substantial losses.

At Lancashire we pride ourselves on understanding the insurance cycle. These events have shown the value of our priorities. Our discipline means that we prioritise the appropriate risk selection for all stages of the cycle.

Our outlook for 2018 is more positive than it has been for some time. We expect to put our capital to work to take advantage of improving market conditions and will be paying our standard ordinary dividend, in line with our stated dividend policy.

Renewal price index (RPI)

Lancashire's RPI is an internal methodology that management uses to track trends in premium rates on a portfolio of insurance and reinsurance contracts. The RPI is calculated on a per contract basis and reflects Lancashire's assessment of relative changes in price, terms, conditions and limits on like-for-like renewals only, and is weighted by premium volume. The RPI does not include new business and only covers business written by LICL and LUK, to offer a consistent basis for analysis. The calculation involves a degree of judgement in relation to the comparability of contracts and the assessment noted above. To enhance the RPI tool, Lancashire may revise the methodology and assumptions underlying the RPI, so the trends in premium rates reflected in the RPI may not be comparable over time. Consideration is only given to renewals of a comparable nature so the RPI does not reflect every contract in LICL and LUK's portfolio. The future profitability of the portfolio of contracts within the RPI is dependent upon many factors besides the trends in premium rates.

The following table summarises the RPI figures for the main business classes, excluding the Lloyd's segment, using 2006 as the base year:

RPI

Class	2017	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007	2006
Aviation (AV52)	**34**	37	41	44	49	55	59	62	68	69	80	100
Gulf of Mexico offshore energy	**103**	111	118	125	136	140	140	139	137	64	80	100
Worldwide offshore energy	**68**	70	81	91	97	100	97	88	84	68	80	100
Marine	**65**	72	82	91	89	86	79	80	82	80	88	100
Property retrocession and reinsurance	**98**	103	117	132	152	157	131	121	127	86	97	100
Terrorism	**36**	38	43	48	52	55	57	60	66	71	86	100
Combined	**57**	61	68	76	81	84	83	81	83	76	86	100

Underwriting results

	2017						2016					
	Property $m	Energy $m	Marine $m	Aviation $m	Lloyd's $m	Total $m	Property $m	Energy $m	Marine $m	Aviation $m	Lloyd's $m	Total $m
Gross premiums written	**198.0**	**101.8**	**67.6**	**16.9**	**207.3**	**591.6**	219.5	126.0	37.2	36.2	215.0	633.9
Net premiums earned	**146.5**	**70.4**	**50.7**	**11.6**	**148.7**	**427.9**	148.5	105.5	35.4	25.5	173.2	488.1
Net loss ratio	**114.4%**	**15.8%**	**32.9%**	**(19.0)%**	**95.6%**	**78.4%**	9.2%	39.3%	41.8%	(4.7)%	42.6%	29.2%
Net acquisition cost ratio	**18.8%**	**44.0%**	**36.3%**	**27.6%**	**23.8%**	**27.0%**	18.9%	45.1%	27.4%	30.6%	22.5%	27.1%
Expense ratio	**—**	**—**	**—**	**—**	**—**	**19.5%**	—	—	—	—	—	20.2%
Combined ratio	**133.2%**	**59.8%**	**69.2%**	**8.6%**	**119.4%**	**124.9%**	28.1%	84.4%	69.2%	25.9%	65.1%	76.5%

Premiums

Gross premiums written decreased by 6.7 per cent in 2017 compared to 2016. Gross premiums earned decreased by 6.9 per cent in 2017 compared to 2016. The Group's five principal segments, and the key market factors impacting them, are discussed below.

Property

Property gross premiums written decreased by 9.8 per cent for the year ended 31 December 2017 compared to the year ended 31 December 2016. The decrease was primarily due to multi-year contracts in the property catastrophe, political risk and terrorism classes which were written in 2016 that are not yet due to renew. This reduction was partly offset by new business written in the political risk book. Business flow in the political risk class is generally less predictable than other classes due to the specific nature of each deal. We also saw some new business written in the property catastrophe book and $7.0 million of reinstatement premiums in connection with hurricanes Harvey, Irma and Maria.

Energy

Energy gross premiums written decreased by 19.2 per cent for the year ended 31 December 2017 compared to the year ended 31 December 2016. The decrease for the year was mainly due to exposure reductions on prior underwriting year risk-attaching business in the worldwide offshore book, which can include exposure such as construction projects that have been delayed or cancelled, plus the timing of renewal of non-annual deals in the worldwide offshore book.

Marine

Marine gross premiums written increased by 81.7 per cent for the year ended 31 December 2017 compared to the year ended 31 December 2016. The majority of the increase was due to new pro-rata business plus the timing of non-annual renewals and an increase in prior underwriting year risk-attaching business due to changes in the underlying exposure.

Aviation

Aviation gross premiums written decreased by 53.3 per cent for the year ended 31 December 2017 compared to the year ended 31 December 2016. This was due to exposure reductions on prior underwriting year risk-attaching business in the AV52 book. In addition, there were premium reductions year on year in the satellite book following the de-risking of this book during 2017.

Lloyd's

In the Lloyd's segment gross premiums written decreased by 3.6 per cent for the year ended 31 December 2017 compared to the year ended 31 December 2016. The decrease was driven primarily by continued rating pressure on the energy book. This decrease was partly offset by an increase in reinstatement premiums in connection with hurricanes Harvey, Irma, and Maria.

Ceded

Ceded reinsurance premiums increased by $18.4 million, or 10.5 per cent, for the year ended 31 December 2017 compared to the year ended 31 December 2016. The increase was due to additional limit purchased plus reinstatement premiums in connection with hurricanes Harvey, Irma, and Maria.

Earned

Net premiums earned as a proportion of net premiums written were 107.5 per cent for the year ended 31 December 2017, compared to 106.4 per cent for the year ended 31 December 2016. The earnings ratios were relatively stable on an annual basis.

Losses

2017 was characterised by significant catastrophe activity, in the form of hurricanes Harvey, Irma and Maria, the two earthquakes in Mexico and the California wildfires. As a result, the Group's net loss ratio was 78.4 per cent for the year ended 31 December 2017 compared to 29.2 per cent for the year ended 31 December 2016. The 2017 accident year loss ratio, including the impact of foreign exchange revaluations, was 94.2 per cent compared to 46.2 per cent for the year ended 31 December 2016.

Our net losses recorded for the year ended 31 December 2017 in relation to the catastrophe events noted above was $181.8 million, excluding the impact of inwards and outwards reinstatement premiums and our share of losses from Kinesis. While reserves have been recorded, significant uncertainty exists on the eventual ultimate losses in relation to the hurricanes, earthquakes and wildfires as loss information after these types of events can take some time to obtain. The Group's reserve estimates were derived from a combination of market data and assumptions, a limited number of provisional loss advices, limited client loss data and modeled loss projections. As additional information emerges, the Group's actual ultimate loss may vary, perhaps materially, from the current reported reserves. The final settlement of all claims is likely to take place over a considerable period of time.

While there were no other significant net losses in either of 2017 and 2016, both years experienced a few small to mid-sized losses, primarily across the property and energy classes.

Prior year favourable development was $65.1 million for the year ended 31 December 2017 compared to $85.8 million for the year ended 31 December 2016. Despite some adverse development on a prior accident year property and energy claims, we saw overall favourable development primarily due to general IBNR releases across most lines of business due to a lack of reported claims. Experience in 2016 was similar in terms of releases, offset partially by some adverse development on prior accident year energy and marine claims.

Excluding the impact of foreign exchange evaluations, the table below shows the impact of current accident year catastrophe events on the Group's loss ratio for the year ended 31 December 2017:

	Losses $m	Loss ratio %
Reported loss ratio at 31 December 2017	**335.4**	**78.4**
Absent hurricane Harvey	**287.6**	**67.7**
Absent hurricane Irma	**281.6**	**66.1**
Absent hurricane Maria	**300.0**	**70.5**
Absent Mexico earthquakes	**325.1**	**76.0**
Absent California wildfires	**300.9**	**70.4**
Absent all catastrophe events	**153.6**	**36.6**

Note: The table does not sum to a total due to the impact of reinstatement premiums.

Excluding the impact of foreign exchange revaluations, previous accident years' ultimate losses developed as follows during 2017 and 2016:

Ultimate loss development by accident year

	2017 $m	2016 $m
2007 accident year and prior	**0.6**	(0.4)
2008 accident year	**(0.5)**	1.6
2009 accident year	**0.1**	(18.0)
2010 accident year	**1.8**	3.2
2011 accident year	**8.8**	9.9
2012 accident year	**5.0**	13.5
2013 accident year	**3.5**	(1.6)
2014 accident year	**9.2**	19.9
2015 accident year	**20.3**	57.7
2016 accident year	**16.3**	—
Total	**65.1**	85.8

Note: Positive numbers denote favourable development.

The ratio of IBNR to total net loss reserves was 44.8 per cent as at 31 December 2017 compared to 34.6 per cent as at 31 December 2016.

The table below provides further detail of the prior years' loss development by class, excluding the impact of foreign exchange revaluations:

Loss development by class

	2017 $m	2016 $m	2015 $m	2014 $m	2013 $m
Property	**14.4**	36.6	26.4	19.8	13.2
Energy	**21.1**	17.3	35.2	5.4	18.4
Marine	**15.2**	1.9	13.8	(9.7)	(23.4)
Aviation	**3.0**	3.9	2.9	0.9	(1.4)
Lloyd's	**11.4**	26.1	29.4	18.0	9.1
Total	**65.1**	85.8	107.7	34.4	15.9

Note: Positive numbers denote favourable development.

Accident year loss ratios

	2017 %	2016 %	2015 %	2014 %	2013 %
Accident year loss ratio	**94.2**	43.5	32.4	25.9	28.1
Initial accident year loss ratio	**n/a**	46.2	46.0	35.9	36.1
Change in loss ratio post accident year	**n/a**	2.7	13.6	10.0	8.0

Note: Adjusted for revaluation of foreign currencies at the exchange rate as at 31 December 2017.

Acquisition costs

The acquisition cost ratio was 27.0 per cent for the year ended 31 December 2017 compared to 27.1 per cent for the year ended 31 December 2016. The acquisition cost ratio is relatively stable on an annual basis.

Investments, liquidity and cash flow

Since inception, the primary objectives for our investment portfolio have been capital preservation and liquidity. Those objectives remain unchanged, and are more important than ever in today's volatile and reactive markets. As market volatility continues, we position our portfolio to limit downside risk in the event of market shocks. In 2017, our focus has been on managing our interest rate risk, the largest risk to our predominantly fixed maturity portfolio. We continue to maintain a short-duration fixed maturity portfolio and have been using our risk budget to add products to our portfolio to help mitigate a rise in rates.

Our portfolio mix illustrates our conservative philosophy, as shown in the table below. With the composition regulated by the Group's investment guidelines, we have three investment portfolio categories: 'core', 'core plus' and 'surplus'. The core portfolio contains at least enough funds required to meet near-term obligations and cash flow needs following an extreme event. Assets in excess of those required to be held in the core portfolio may be held in any of the three categories, which are discussed further on page 110.

As at 31 December 2017 and 2016 the managed portfolio was as follows:

	2017 %	2016 %
Fixed maturity securities	**80.1**	81.4
Cash and cash equivalents	**10.2**	10.4
Hedge funds	**8.4**	7.0
Equity securities	**1.3**	1.2
Total	**100.0**	100.0

Managed investment portfolio allocations

	2017 %	2016 %	2015 %	2014 %	2013 %
Cash	**10.2**	10.4	9.6	10.6	14.7
Short-term investments	**6.0**	0.3	1.1	1.4	9.8
Fixed maturity funds	**1.7**	0.8	0.6	0.7	1.1
Government debt	**17.0**	20.3	23.6	21.4	14.6
Agency debt	**3.8**	4.4	0.2	0.8	4.1
Agency MBS, CMBS	**7.7**	6.4	7.3	7.7	10.9
Non-agency RMBS, ABS, CMBS	**8.5**	7.3	8.4	11.0	8.4
Corporate bonds	**28.2**	32.5	33.2	31.7	29.7
Bank loans	**5.8**	6.6	5.9	5.8	4.5
Fixed maturity – at FVTPL	**1.4**	2.8	1.3	1.4	1.3
Equity securities	**1.3**	1.2	0.8	0.7	0.7
Hedge funds – at FVTPL	**8.4**	7.0	8.0	6.8	—
Other investments	**—**	—	—	—	0.2
Total	**100.0**	100.0	100.0	100.0	100.0

The composition, duration and asset allocation of the investment portfolio are reviewed on a regular basis in order to respond to changes in interest rates and other market conditions. If certain asset classes are anticipated to produce a higher return within management's risk tolerance an adjustment in asset allocation may be made. Conversely, if the risk profile is expected to move outside of tolerance levels, adjustments may be made to reduce the risk in the portfolio. We try to be nimble in our investment strategy while putting our objective of capital preservation first and foremost.

We believe in the application of common sense, and do not place much reliance on 'black box' approaches to investment selection.

Investments are, however, inherently unpredictable and there are risks associated with any investment strategy decisions. Recent market history has been tumultuous and we remain ever watchful. We will continue to monitor the economic environment closely.

Investment performance

Net investment income excluding realised and unrealised gains and losses, was $30.5 million for the year ended 31 December 2017, an increase of 2.3 per cent compared to 2016. Total investment return, including net investment income, net realised gains and losses, impairments and net change in unrealised gains and losses, was a gain of $45.7 million for the year ended 31 December 2017 compared to a gain of $38.4 million for 2016.

Despite the increase in treasury yields in 2017, the investment portfolio produced a return of 2.5 per cent due to the narrowing of credit spreads, coupon income and strong returns in the Group's risk-asset portfolios. In 2016, the investment portfolio returned 2.1 per cent. The fixed maturity portfolios performed reasonably well in 2016, primarily due to the narrowing of credit spreads, which more than offset the slight increase in treasury yields during the year. The 2016 returns were also supported by strong performance from the Group's bank loans, equities and equity-linked notes.

Our average annual total investment return since inception is 2.9 per cent, and we have made a positive investment return in every year since inception, including 2008.

Liquidity

The Group is a short-tail insurance and reinsurance group. As such, the investment portfolio must be liquid, short duration and highly creditworthy. As noted earlier, the Group's investment strategy places an emphasis on the preservation of invested assets and provision of sufficient liquidity for the prompt payment of claims in conjunction with providing a reasonably stable income stream.

Liquid securities will be maintained at an adequate level to more than meet expenses, including unanticipated claims payments. Only once safety, liquidity and investment income requirements are satisfied, may additional growth in the investment portfolio be pursued.

Cash flow

The Group's cash inflows are primarily derived from net premiums received, from losses recovered from reinsurers, from net investment income, including dividends and net income from managed third party capital, and any capital raising activities performed in a given year including the issuance of debt. Excess funds are invested in the investment portfolio, which primarily consists of high-quality, highly liquid fixed maturity securities of short duration. Other cash inflows result from the sale and redemption of investments.

The principal outflows for the Group are the settlement of claims, the payment of premiums for reinsurance cover, payment of general and administrative expenses, the servicing of debt, the purchase of investment products and the distribution of dividends.

Key investment portfolio statistics

	2017	2016	2015	2014	2013
Duration	**1.7 years**	1.8 years	1.5 years	1.5 years	1.0 year
Credit quality	**AA-**	A+	AA-	AA-	AA-
Market yield	**2.1%**	1.9%	1.9%	1.5%	1.2%
Book yield	**2.0%**	1.8%	1.6%	1.5%	1.4%

Lancashire third party capital management

The total contribution from third party capital activities consists of the following items:

	2017 $m	2016 $m
Kinesis underwriting fees	**5.8**	4.4
Kinesis profit commission	**5.9**	6.2
Lloyd's managing agency fees & profit commission	**5.5**	9.9
Total other income	**17.2**	20.5
Share of (loss) profit of associate	**(9.4)**	5.1
Total net third party capital managed income	**7.8**	25.6

The increase in Kinesis underwriting fees during 2017 was due to more limit being placed compared to 2016. The Kinesis profit commission was driven by the timing of loss experience and collateral release and therefore varies from year to year. The share of (loss) profit of associate reflects Lancashire's 10 per cent equity interest in KHL. The overall loss for 2017 was entirely driven by the significant catastrophe activity during the second half of 2017. The reduction in Lloyd's fees and profit commission was driven by the relative profitability of the underwriting years impacting each period.

Other operating expenses

	2017 $m	2016 $m
Employee remuneration costs	**40.2**	61.4
Other operating expenses	**43.4**	37.1
Total	**83.6**	98.5

Employee remuneration costs for the year ended 31 December 2017 were $21.2 million lower than the same period in 2016, primarily driven by lower variable compensation due to the catastrophe activity in the year.

Other operating expenses were $6.3 million higher for the year ended 31 December 2017 compared to the same period in 2016, primarily due to increased software costs, placement fees for the Kinesis vehicle plus higher consulting costs.

The equity-based compensation credit of $0.4 million for the year ended 31 December 2017, compared to an expense of $10.7 million for the year ended 31 December 2016, was due to incorporating losses incurred during the second half of 2017 into performance estimates, combined with the lapsing of awards of former Cathedral employees on their departure from the Group. The equity-based compensation charge was driven by the anticipated vesting level of the active awards based on current performance expectations.

Capital management

Lancashire has built a reputation for being one of the best known and most active proponents of capital management in the industry. Capital management is our most important area of focus after underwriting and it is our firm belief that proactive and flexible capital management is crucial in helping to maximise risk-adjusted return over time. With that focus we will return capital where this offers the best returns for our shareholders. We have returned 108.1 per cent of comprehensive income generated via dividends or share repurchases since inception.

The Group actively reviews the level and composition of capital on an ongoing basis. Internal methods have been developed to review the profitability of classes of business and their estimated capital requirements plus the capital requirements of the combination of a wide range of other risk categories. The key aim of the capital management process is to maintain a strong balance sheet, whilst:

- maintaining sufficient capital for underwriting opportunities and to meet obligations to policyholders;
- maximising the risk-adjusted return to shareholders within predetermined risk tolerances;
- maintaining adequate financial strength ratings; and
- meeting internal, regulatory and rating agency requirements.

The subsidiary operating entities also conduct capital requirement assessments under internal measures and in compliance with local regulatory and Lloyd's requirements.

Capital raising can include debt or equity, and returns of capital may be made through dividends, share repurchases, a redemption of debt or any combination thereof. All capital actions require approval by the Board of Directors. The retention of earnings generated also leads to an increase in capital.

The composition of capital is driven by management's appetite for leverage, amongst other factors, including the cost and availability of different types of capital. Maintaining a strong balance sheet will be the overriding factor in all capital management decisions.

Capital

As at 31 December 2017, total capital available to the Group was $1.433 billion, comprising shareholders' equity of $1.107 billion and $326.3 million of long-term debt. Tangible capital was $1.279 billion. Leverage was 22.8 per cent on total capital and 25.5 per cent on total tangible capital. Total capital and total tangible capital as at 31 December 2016 were $1.528 billion and $1.374 billion respectively.

Dividends

During 2017, the Lancashire Board declared a final dividend of $0.10 per common share in respect of the 2016 financial year and an interim dividend of $0.05 per common share in respect of 2017. With the final dividend in respect of 2017 of $0.10 per common share, total capital returns since inception amount to $2.7 billion, or 277.8 per cent of initial capital raised. The final dividend of $0.10 per common share will be paid on 21 March 2018 to the shareholders of record on 23 February 2018.

Non pre-emptive issue of shares

As part of the Group's flexible approach to capital management the Board has in recent years requested and received from shareholders authority to issue up to 15 per cent of its shares on a non pre-emptive basis. Lancashire believes that this ability to raise capital quickly is important in securing first-mover advantage in the catastrophe insurance and reinsurance business in which it underwrites. The Board proposes to put a similar request for authority to shareholders in a resolution at the 2018 AGM to be held on 2 May 2018.

Letters of credit

Lancashire has a standard syndicated LOC facility which in total amounts to $300.0 million, with a $75.0 million loan sub-limit available for general corporate purposes. Syndicate 2010 has an $80.0 million catastrophe facility in place to assist in paying claims and gross funding of catastrophes. Furthermore, a $130.0 million syndicated uncollateralised facility is available for utilisation by LICL and guaranteed by LHL for Funds at Lloyd's purposes.

There was no outstanding debt under the above facilities at any reporting date. There are no off-balance sheet forms of capital.

Navigating our environment

Consistent Enterprise Risk Management is the key to being ready to respond in all environments.

Louise Wells
Group Chief Risk Officer

Maintaining the balance

The first eight months of 2017 were all about maintaining the balance of the risk we were taking on with the return we were receiving for that risk. It was pleasing therefore, that post hurricanes Harvey, Irma and Maria, the Mexican earthquakes and California wildfires we remained inside our Board-approved risk appetite and tolerances. Following these events our risk management processes did not change; our risk appetite was reviewed with the changing environment in mind, however no adjustments to tolerances were required.

Risk strategy

Our risk strategy is the starting point for the development and evolution of our risk management framework and is therefore refreshed on an annual basis in line with the continuous development of our framework and the annual review of the business and capital strategy. Our risk strategy must be aligned with our business and capital strategy to ensure the capital resources held are matched to the risk profile of the Group and that the balance between risk and return is considered as part of all key business decisions.

The Group is exposed to risks from several sources. These include insurance risk, market risk, liquidity risk, credit risk, operational risk and strategic risk. The primary risk to the Group is insurance risk, which can be subdivided into the core risk of underwriting and non-core risk of reserving.

The Group has formulated, and keeps under review, a risk appetite which is set by the Board of Directors. The Group's appetite for risk will vary marginally from time to time to reflect the potential risks and return that present themselves. However, protecting the Group's capital and maximising risk-adjusted returns for investors over the long term are constants. The risk appetite of the Group is central to how the business is run and permeates into the risk appetites that the individual operating entity boards of directors have adopted. These risk appetites are expressed through detailed risk tolerances at both a Group and an operating entity level. Risk tolerances represent the maximum amount of capital, generally on a modeled basis, that the Group and its entities are prepared to expose to certain risks.

The Board of Directors is responsible for setting and monitoring the Group's risk appetite and tolerances, whereas the individual entity boards of directors are responsible for setting and monitoring entity-level risk tolerances. All risk tolerances are subject to at least an annual review and consideration by the respective boards of directors. The Board and individual entity boards of directors review actual risk levels versus tolerances, emerging risks and any risk learning events at least quarterly. In addition, on at least a monthly basis, management reviews the output from SHARP in order to assess modeled potential losses against risk tolerances and to ensure that risk levels are managed in accordance with them.

ERM framework

The Group subscribes to a 'three lines of defence' model, the front line being risk ownership by business managers. Responsibility for the management of individual risks has been assigned to, and may form part of the performance objectives of, the risk owners within the business. Risk owners ensure that these risks and controls are consistent with their day-to-day processes and the entries made in the Group risk registers, which are a direct input into the subsidiary capital models. The second line comprises the risk management team, which is responsible for risk oversight. Within this, the Group CRO provides regular reports to the business outlining the status of the Group's ERM activities and strategy, as well as formal reports to the Board and the boards of the individual operating entities. The Group CRO ultimately has the right to report directly to the Group and entity regulators if she feels that management is not appropriately addressing areas of concern. Cathedral's CRO provides formal reports to the CUL Board and its Risk, Capital and Compliance Committee. The third line of defence is the internal audit function, which works very closely with the business and the risk management team in providing risk assurance.

We continue to perform a quarterly risk and controls affirmation process whereby the operation of all key controls is affirmed by the control operators and then reviewed and signed off by the risk owners. In addition, the risk owners are required to affirm their risks remain appropriately documented and scored. During 2017 this process was expanded to include all individual operating entities including the syndicates. The output from this process is reported to the RRC and the Group and operating subsidiary audit committees or boards of directors as appropriate.

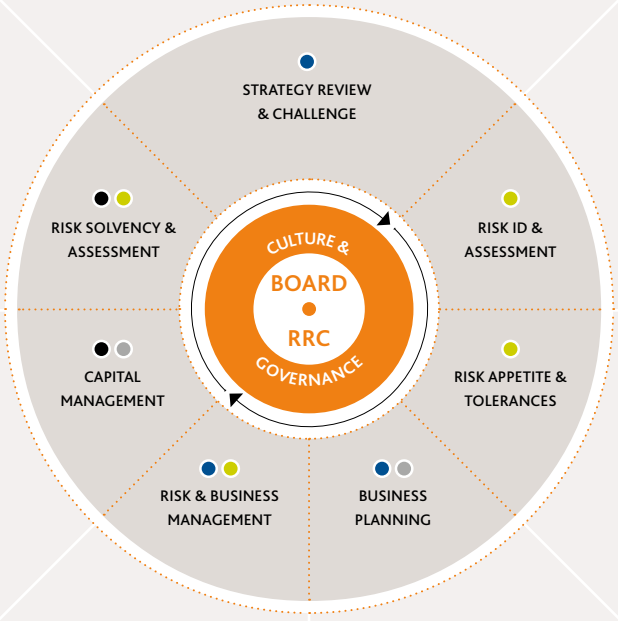
ERM & ORSA

Key Activities

- Review of business strategy with challenge from the Board
- Annual approval of a business strategy paper by the Board

- Group CRO report to Board and Executive Management Committee
- Production of ORSA report and review and approval by the Board

- Risk identification and assessment
- Quarterly risk and control affirmations
- Quarterly internal audit reports to the Audit Committee per a three- and four-year rolling programme
- External audit reports to the Audit Committee
- Audit Committee annual review of the effectiveness of financial controls



- Capital and liquidity management frameworks
- Review of BLAST policies, capital and solvency appetites
- Full/proxy capital assessments
- Rating agency capital assessments
- Stress and scenario testing

- Review of risk strategy and 'attitude to risk'
- Review of risk appetite and limits
- Review of Group risk tolerances
- Management, Board and subsidiary board approval of risk tolerances

- Review of risk management policies
- Assessment of risk management framework maturity
- Integrated assurance assessment
- Emerging risk assessment

- Review and approval of business plan by the Board
- Stress and scenario testing (business plan)
- Assessment of management actions

Key Elements of ORSA

Board sign-off and embedding · Business Strategy · Risks · Capital and Solvency · Stress and Scenario testing

As at 31 December 2017, all Group entities were operating within their board-approved risk tolerances. No significant new risks have been identified and there have not been any material changes in our existing risks.

Our quarterly ORSA reports prepared by the Group CRO to the main Board provide a timely analysis of current and potential risks, compared against risk tolerances, along with their associated capital requirements. The 2018 annual ORSA report will be presented to the Board for review, challenge and approval during Q1 2018 and then submitted to the PRA in line with supervisory requirements.

As a Lloyd's managing agent, CUL falls within the Society of Lloyd's for Solvency II reporting, preparing ORSA reports for each syndicate. Cathedral has its own ERM framework to ensure adherence to Lloyd's minimum standards.

In November 2017, the Group CRO reported to the Remuneration Committee regarding risk and remuneration, recognising the importance of the design of the remuneration structure in driving desired behaviours over both the short-term and the longer-term business planning periods. In addition, a Group Solvency II Staff policy was reviewed, challenged and approved by the Remuneration Committee.

The diagram above illustrates how we balance our ERM and ORSA activities. Our risk culture is driven from the top down via the Board and executive management to the business, with the RRC central to these processes. The primary role of the Group CRO is to facilitate the effective operation of ERM and the ORSA process throughout the Group at all levels. The role includes, but is not limited to, the following responsibilities:

- overall management of the risk management system;
- to drive ERM culture, ownership and execution on three levels: Board, executive management and operational within the business;
- to facilitate the identification, assessment, evaluation and management of existing and emerging risks by management and the Board including the articulation of risk preferences and the adoption of formal risk tolerances;
- to ensure that these risks are given due consideration and are embedded within management's and the Board's oversight and decision-making process;
- to be consulted, and opine, on policy in areas such as, but not limited to, underwriting, claims, investments, operations and capital management; and

- to provide timely, accurate, reliable, factual, objective and accessible information and analysis to guide, coach and support decision making.

RRC

The RRC, under the chairmanship of the Group CEO, is the key management tool for monitoring and challenging the assessment of risk on a continual basis. It seeks to optimise risk-adjusted return and facilitate the appropriate use of BLAST, including considering its effectiveness. It ensures that all key areas of risk are discussed according to a schedule that covers fortnightly, monthly, quarterly, semi-annual and annual reviews. The RRC meets fortnightly and is responsible for co-ordinating and overseeing ERM activities within the risk profile, appetites and tolerances set by the Group and individual entity boards of directors. The RRC includes the Group CEO, members from the finance, actuarial, modeling, operations, treasury and underwriting functions and both the Group CRO and Cathedral CRO. The Group CRO reports on the RRC's activities to the Group and individual entity boards of directors and, via the Cathedral CRO, the Risk, Capital and Compliance Committee of Cathedral. Through the Group CRO the RRC considers recommendations to the Board and its Committees with regard to the adoption of formal risk tolerances.

Capital models

We continue to challenge the assumptions used in the individual capital models and make changes where appropriate.

Emerging risk

The identification and assessment of emerging risk occurs throughout the Group from individual departments to management and executive committees to the boards of directors and sub-committees of the boards. The risk department maintains an emerging risk register, which is provided to the Board and entity boards of directors each quarter, and is therefore subject to an iterative process of review and oversight. Emerging risks, by their nature, are difficult to quantify, however during 2017 the Group strove to foresee potential areas of new risk, or developments in existing risks and to assess how those risks could impact the Group.

Risk universe

We continue to classify risks in three broad classes: (a) Intrinsic Risk: 'Risk that stems from the inherent randomness and uncertainty that exists in the universe in which we operate and that is therefore fundamental to how we manage our business'. This can be core or non-core; (b) Operational Risk: which can be independent or correlated; and (c) Other Risk: the non-financial category of risks which cannot necessarily be mitigated by holding capital since such risks may not have direct balance sheet implications.

The Board evaluated the risks disclosed, alongside other factors, in the assessment of the Group's viability and prospects as set out in the going concern and viability statement in the Directors' Report at page 83.

Risk universe

Type	Category	Description
Intrinsic Core	Underwriting Investment	Intrinsic risks representing the potential to generate a return as well as a loss. In these areas, the Group promotes informed risk-taking that considers the risk and return equation in all major decisions, with the intention of maximising risk-adjusted return on equity. We recognise that by insuring fortuitous events we can suffer losses, and that within our investment portfolio we can see the value of investments fall. We cannot avoid these risks so we focus on the correlated operational risks and seek to mitigate them. For example, we know that by insuring the risk of earthquake we are exposed to the risk that losses exceed our plan. We model our portfolio using stochastic modeling to review actual and planned exposures to ensure they remain within tolerances. The correlated risks are that we might fail to design or maintain effective tolerances and limits, and fail to maintain exposures within such limits; or that we fail to keep accurate and timely records of our exposures. We then devise systems and processes to mitigate these risks, such as PML reconciliations, and RDS sign-offs, with review by the RRC and regular ORSA reports to the Board, which also considers and approves formal risk tolerances.
Intrinsic Non-core	Reserving (Re)Insurance counterparty Liquidity	Intrinsic risks to which we are inevitably exposed as a result of conducting our day-to-day business operations yet offer no direct potential for return. They are quantified insofar as practicable for the purposes of capital and risk management and avoided or minimised insofar as is economically justifiable.
Operational	Operational	These are risks arising as a result of inadequate or failed internal processes, personnel, systems or (non-insurance) external events. They have the potential either to magnify the adverse impacts of intrinsic risks, for example increased reinsurer default losses arising through the use of non-approved counterparties; or to crystallise separately in their own right, for example losses arising through the imposition of fines as a result of a regulatory breach, so unrelated to our core functions.
Other	Strategic Group Emerging	These are risks for which quantitative assessment is difficult but for which a structured approach is still required to ensure that their potential impact is considered and mitigated insofar as is practicable. These are included within the risk register and are assessed and mitigated through scenario and stress testing.

Balancing our risks and opportunities

As described under our review of the Risk Universe, our classification of risks as Intrinsic Core and Intrinsic Non-core, Operational and Other helps us to focus on our management and mitigation of those risks. Further details concerning these risks can be found on pages 100 to 125. Within the capital models, insurance risk accounts for over 80 per cent of the allocated risk capital, so this is clearly the principal area where we stringently apply controls and reviews. For example, we place a large number of controls around monitoring risk levels across the business. However, we understand that even risks that do not generate a capital charge under an economic capital model can pose serious threats to the execution of the business plan and strategy, and therefore need to be monitored and tested. For example, we spend a lot of time looking at the implications of emerging capital and the evolution of the market cycle.

INTRINSIC RISK: CORE

TYPE	MITIGATION
Underwriting: Losses in our classes are hard to predict in particular as to the specifics of timing and quantum of catastrophe loss events. Additionally, we write lines of business that are subject to accumulations, including accumulations of individual risk losses arising from a single event such as several property catastrophe excess of loss programmes being affected by a windstorm or earthquake, and accumulations between business lines such as a 9/11 type event impacting both the terrorism and AV52 portfolios. Losses can also exceed expectations in terms of both frequency and severity. So, although we model losses, for example using the RMS and AIR stochastic models, we know that these projections can and will be wrong in many instances. Movement since 2016: Decreased due to reduced retentions and further contraction to core book reducing aggregate exposure.	Modeling: We apply loads to, and stress test, stochastic models and develop alternative views of losses using exposure damage ratios. RRC: The RRC considers accumulations, clashes and parameterisation of losses and models. Capital: We set our internal capital requirements at a level that allows for buffers above accumulations of extreme events and the Board approves risk tolerances at least annually and considers capital requirements on at least a quarterly basis.
Investment: We need to hold sufficient assets in readiness to pay claims, but the markets and products in which we invest can suffer volatility and losses. As a short-tail insurer, we are able to hold the majority of assets in low-duration securities such as fixed maturities. However, this creates an additional source of risk in the current environment, where there is a considerable risk from changes to interest rates as quantitative easing programmes may begin to taper or be increased. We model our investment portfolios and use various stress scenarios to see what kinds of losses we could expect under a range of outcomes. Movement since 2016: No material change.	Investment strategy: Our strategy is that investment income is not expected to be a significant driver of our returns. Our primary focus remains on underwriting as the engine of profits. Investment strategy, including investment risk tolerances, is approved annually and monitored on a quarterly basis by the Investment Committee and Board. IRRC: The IRRC forms an integral part of our risk management framework, meeting at least quarterly and reporting to the RRC. External advisers: Lancashire's Board and management recognise that the Group's principal expertise lies in underwriting so we use the services of internationally recognised investment managers who are experts in their fields.

INTRINSIC RISK: NON-CORE

TYPE	MITIGATION
Reserving: Because we do not know the amount of losses we are going to incur at the outset of a contract, we have to make estimates of the reserves we need to hold to pay claims. If these reserves are inadequate and claims exceed them, this may have an impact on earnings, or indeed capital. Independent external reviews of our reserves look at the overall levels of expected losses, as well as individual large events, including benchmarking analyses to provide assurance over the level of reserves booked. Movement since 2016: No material change. Our processes and controls remain the same as in previous periods.	Short-tail business: Lancashire's focus is on short-tail lines of business where losses are usually known within, or shortly after, the policy period with a reasonable degree of certainty. Experience data: We have access to a lot of data, both our own and from the industry as a whole, about losses and loss trends. Actuarial and statistical data are used to set estimates of future losses, and these are reviewed by underwriters, claims staff and actuaries to ensure that they reflect the actual experience of the business. External review: Insurers typically facilitate an independent, external review of their loss reserves. Lancashire retains the services of one of the leading industry experts, and our appetite is defined so as to set reserves within a range of reasonable estimates based on both internal and external review. The Audit Committee of the Board reviews reserve adequacy at its quarterly meetings.

INTRINSIC RISK: NON-CORE

TYPE	MITIGATION
(Re)Insurance and intermediary counterparty: Almost all the insurance policies which we write are brought to us by brokers, who act as intermediaries between us and the client, and handle the transaction of payments of claims and premiums on our behalf. This exposes us to the risk of mishandling by, or failure of, the broker concerned. In order to make our portfolio as efficient as possible, we buy reinsurance to protect against severity, frequency and accumulation of losses. Again, this exposes us to the risk that our counterparties may have the inability or unwillingness to pay us in the event of a loss. Movement since 2016: No material change.	Counterparty credit limits: The Broker Vetting Committee is responsible for the broker vetting approval process and monitoring credit risk in relation to brokers. In addition, the Group conducts broker business using non-risk transfer TOBAs. This mitigates the risk due to non-payment by brokers and intermediaries as monies are held in separated client accounts. We use counterparty credit limits, seek to deal with reputable reinsurers that meet our minimum rating standards, and use collateral agreements where appropriate. The operating entities of the Group that contract for reinsurance separately maintain and report their own counterparty credit limits at the entity level. The RSC is responsible for approving counterparties and monitoring aggregate limits.
Liquidity: In order to satisfy claims payments we need to ensure that sufficient assets are held in a readily realisable form. This includes holding cash accounts for the expected level of attritional losses, as well as ensuring that we can meet claims payment requirements in extreme events. Movement since 2016: No material change.	Portfolio management: The Group maintains liquidity in excess of the Board-agreed tolerances. This is achieved through the maintenance of a highly liquid portfolio with short duration and high creditworthiness. We monitor this through the use of stress tests and mitigate risks through the quality of the investments themselves.

OPERATIONAL

TYPE	MITIGATION
These are risks arising as a result of inadequate or failed internal processes, personnel, systems or (non-insurance) external events. They have the potential either to magnify the adverse impacts of intrinsic risks or crystallise separately in their own right. This can encompass IT availability, where the failure of an IT system, such as our underwriting system, could impact our ability to maintain accurate and up-to-date records of our exposures. If correlated with an insurance loss this could cause us to breach insurance risk tolerances. It could also encompass IT integrity, where an unauthorised intruder could alter data in our systems, or introduce a bug that would corrupt the system. Movement since 2016: Increasing as we commence our project to develop our systems to enable us to further improve the functionality of Group IT Finance systems, to enhance management of financial reporting risk and to ensure compliance with IFRS 17 which comes into effect in 2021.	Capacity: We mitigate IT availability risk by adding redundancy to the capacity we need and using backups of data including off-site storage that we test regularly. Testing and access: We mitigate the integrity risk by using independent external penetration tests, and by restricting access to key systems to only those people who are qualified and need to use them. Personnel: We mitigate the risks associated with staff retention and key-man risk through a combination of resource planning processes and controls. Examples include targeted retention packages, documented position descriptions and employment contracts, resource monitoring and the provision of appropriate compensation and training schemes. The Board regularly reviews succession planning arrangements and remuneration structures.

OTHER

TYPE	MITIGATION
These are risks for which quantitative assessment is difficult but for which a structured approach is still required to ensure that their potential impact is considered and mitigated insofar as practicable. They include categories such as Strategic, Group and Emerging Risks. Movement since 2016: On balance no material change. The impact of Brexit is not considered to be a significant risk to the Group given the Group's current operations and trading profile. We will keep U.S. tax reform under review but do not at present consider that it will materially adversely impact the Group's operations.	Qualitative approach: These risks require a qualitative approach, engaging staff in appropriate discussions about sources of risk, and then thinking about possible outcomes. The Group Executive Management Committee and the RRC consider these issues, and the ORSA reports made by the Group CRO to the Board include standing items on Emerging Risk.

Our responsibility to others and the environment

Why corporate responsibility is important to Lancashire

Corporate responsibility is an integral part of Lancashire's approach to its business. We recognise the need to balance our commitment to our shareholders, employees and more immediate stakeholders with a responsibility to support the wider community and the environment, whether within our neighbouring areas or further afield. The work of The Lancashire Foundation is fundamental to the Group's corporate responsibility programme.

Our approach

Lancashire tries to improve society and our environment using such tools as donations by the Foundation and the allocation of staff charity days to work on local improvement projects. We limit the negative impact of our carbon footprint through mitigation strategies and off setting. As well as the direct benefits, we believe that Lancashire reaps indirect benefits in terms of its attraction as an ethical and compassionate employer, and the positive and long-lasting team-building benefits of the activities undertaken. In terms of governance, the Board sets the policy for corporate donations to the Foundation and reviews reports on its activities. For more information about the day-to-day management of the Foundation and how it operates see pages 37 and 38. The Board also sets the policy for the operation of the HR function, and oversees the management of the environmental impact of the business.

Lancashire has a relatively low headcount (204 employees globally), all of whom are remunerated on a basis which comfortably exceeds UK minimum wage requirements. In particular, the Group's UK operation is an accredited Living Wage employer by the Living Wage Foundation. In the ancillary services and limited supply chains used by the Group, Lancashire seeks to receive assurance that its service providers pay a living wage. Concerns over human rights issues with insureds and potential clients are addressed as part of the underwriting process. The Board has recently reviewed and modified the statement on slavery and human trafficking made on behalf of all companies within the Group and considers that it remains fit for purpose. This statement is published on the Company's website. The Chairman's statement on the Group's diversity policy has also been debated by the Board during the year and is posted on the Company's website.

We focus on the following four areas:

Community

$18.5m

donated by the Lancashire Foundation since inception

See page 37

Environment

100%

of our 2017 CO_2 emissions offset

See page 39

Marketplace

100%

of our permanent employees are eligible for RSS awards

See page 39

Workplace

12

different nations represented by our employees

See page 40

The Lancashire Foundation

Committed to supporting communities

The Lancashire Foundation, our charitable grant-making body, is the cornerstone of our support. The channelling of the talents and energy of our staff in helping others in this way helps benefit and build Lancashire's business and a positive culture.

Michael Connor
Chairman of the Trustees of The Lancashire Foundation

Can you explain what The Lancashire Foundation is and define its purpose?
The Foundation is a registered charity in England and Wales (number 1149184) and its purpose is to act as the focal point for the Lancashire Group's corporate social responsibility activities.

These activities can be divided into two main streams: giving money in the form of grants to selected charities and, equally as important, encouraging our staff to give of themselves by supporting the Foundation's work through volunteering. We do this by providing day release programmes for staff to give back to the communities in which they live and around the world. In addition, staff are entitled to up to a week's annual charity leave on completion of three years' permanent employment with the Group.

In 2017, 131 of our staff across the Group participated in charity volunteer days, mentoring opportunities or fundraising events. The Foundation also operates a charity matching scheme to support individual staff members' charitable initiatives. During 2017 matched funds from the Foundation amounted to £16,785 and supported 12 charities.

This sounds simple, but how does it work in practice?
Let's take grant-making first. As a charity closely linked to the Lancashire Group, we strive to ensure that the charities we support reflect the issues and concerns of our staff, whether from personal experience or through the demonstrably positive impact that they have on those in need. We underpin this with a set of objectives to inform our giving with a focus on charities operating in the fields of poverty relief, removing barriers to social exclusion, supporting medical research and humanitarian relief.

The majority of charities we supported in 2017 were as a result of staff suggestions and support. In addition, the Foundation also supported charities suggested by clients and brokers which, for 2017, included Batten Disease Family Association, Skiing with Heroes, Edinburgh Global Partnerships, Starlight Foundation, The Brain Tumour Charity, World Vision – Hurricane Relief and Richard House Children's Hospice.

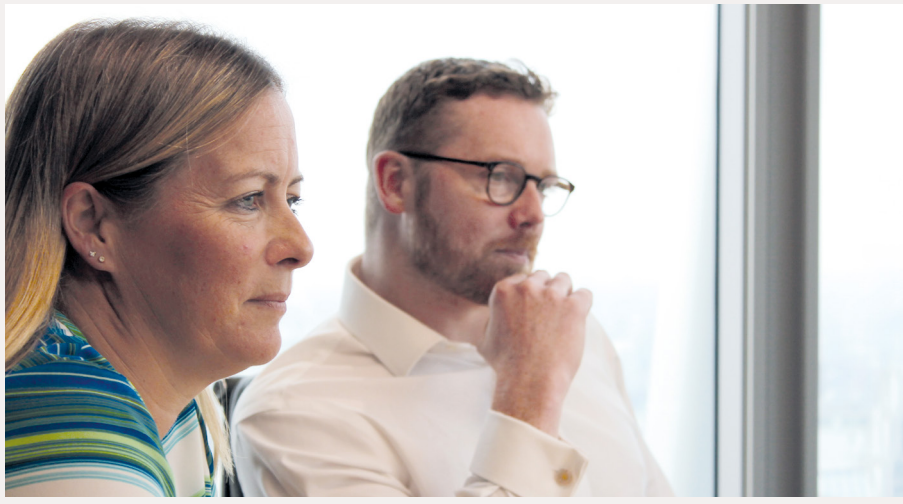
Taking the second aspect of staff giving, we actively encourage support by staff. This takes a number of forms, for example: carrying out volunteering work that directly benefits the charity, like our annual volunteering trip to the Philippines to support the work of ICM with the ultra-poor; providing mentoring support to staff at St Giles Trust, many of whom are ex-offenders; or participating in fundraising events like marathons. During the year the Foundation carried out a number of presentations to remind staff what the Foundation aims to do and how they can support it.

How is the Foundation staffed to support this work?
We don't employ staff; all the work is carried out on a voluntary basis by the existing staff of the Lancashire Group. As I mentioned earlier, a key aspect is ensuring that the Foundation reflects what engages our staff, so funding applications received from charities are analysed and challenged by the Foundation's Donations Committee, which is comprised of staff from across the UK and Bermuda platforms.

The Trustees of the Foundation review the recommendations for funding received from the Donations Committee and release funds as appropriate. As Trustees we also set the strategic direction of the Foundation and ensure it is meeting all of its governance and compliance requirements.

We are lucky with the quality and commitment of the people involved in the Foundation. It does not seem right to highlight certain individuals involved in the Foundation's work as all of them are

The Lancashire Foundation



Clockwise from left: Louise Wells, Chris Wilkinson, Louise Byrne, Derek Stapley and Robert Kennedy

committed and talented, however I am very grateful for the insight and support of my fellow trustees, Derek Stapley and Louise Wells, the Chair of our Donations Committee, Chris Wilkinson, Robert Kennedy, who lends his considerable financial skills to the Foundation's budgeting and forecasting and Louise Byrne, whose organisational skills keep the whole show on the road!

However, it does not stop there. We have a wider pool of advocates to draw upon, namely staff members who act as the Foundation's 'eyes and ears' in relation to specific charities. This really allows both the Donations Committee and the Trustees to obtain comfort that we have close liaison with our charity partners and that questions and issues can typically be resolved quickly.

"It was very pleasing that the Foundation was shortlisted for an award at the 2017 Charity Times Awards in the Corporate Community Local Involvement category."

We've not really talked about charities. Can you give me a flavour of who you support?

Of course. The Foundation looks to support charities around the world but with an emphasis on charities where we can see a demonstrable positive impact on the communities they serve and which operate in effective, transparent and sustainable ways to deliver the programmes they provide.

Through our flagship or cornerstone relationships we can see this: for example, the work of MSF really needs little introduction but they have an ability to react nimbly to multiple international humanitarian crises and to continue to shine a light on issues once the news cycle has moved on. More locally, the Family Centre in Bermuda provides early intervention services for children on the island suffering from family-based problems such as abuse and neglect, and St Giles Trust in the UK looks to break the bleak cycle of re-offending through a variety of means, one of which is its model of using ex-offenders trained to act as peer advisers to support those released from prison.

It was very pleasing that the Foundation was shortlisted for an award at the 2017 Charity Times Awards in the Corporate Community Local Involvement category, which is a tribute to our advocate for St Giles, John Cadman (the Group's General Counsel), and a number of our staff who act as mentors and give up their spare time to support selected St Giles' staff as they develop their careers.

What kind of relationships do you look to cultivate with the charities you support?

Put simply – open and transparent. The advocate system allows us to get close to our charities and foster the deep, multi-year relationships we hope to develop with most of the charities we support.

Annually, where we have multi-year relationships, the advocates are expected to review and reflect on the performance of the charity they advocate with the Donations Committee to ensure that the Committee is happy to recommend a renewal of the grant for the next year to the Trustees. Both quantitative and qualitative data will be reviewed as part of this process.

What is the relationship like between the Foundation and Lancashire Holdings Limited?

A very supportive one. The Foundation has been very lucky to receive an annual donation from LHL to support its activities and at the Foundation's inception it was granted warrants which have been converted into shares. We currently hold 330,713 shares in LHL. In this way we have aligned the Foundation to the Group and can share in its success, and leverage that success to causes and communities that do not often receive such material rewards. Ideally through our work we can develop something approaching a virtuous circle as a grant maker, but this remains a work in progress.

Environment

Despite a small increase in reporting scope, total emissions for 2017 have decreased by 4.3 per cent compared to 2016, with emissions per full-time employee (FTE) falling by 7.0 per cent.

With operations in London and Bermuda, and with clients and brokers around the globe, the Lancashire Group incurs the bulk of its carbon footprint as a result of airline travel, which is offset through an organised programme. The Group operates out of two offices; in London and Bermuda. The Group is also responsible for an apartment in Bermuda which is used for temporary visitor accommodation.

Our approach

The figures in this report are calculated over a 12-month period from 1 January 2017 to 31 December 2017. Emissions are calculated by converting consumption data into tonnes of carbon equivalent (tCO_2e) using the DEFRA 2017 greenhouse gas reporting: conversion factors. Lancashire uses the number of FTE as its intensity metric, which this year shows a decrease of 7.0 per cent to 12.0 tCO_2e per FTE, compared to 12.9 tCO_2e per FTE in 2016.

Where data was not available for 2017, values have been extrapolated by using available data or calculated using industry benchmarks.

Our focus areas

Using an operational control approach, Lancashire assessed its boundaries to identify all the activities and facilities for which it is responsible and reported on all material Greenhouse Gas (GHG) emissions including Scope 1, 2 and 3. Calculations performed follow the ISO-14064-1:2006 standard and give absolute and intensity factors for the Group's emissions.

In 2017, the Group's UK operations achieved BREEAM excellence for its London offices at 20 Fenchurch Street, which has supported an overall improvement in environmental performance.

Therefore, results show that GHG emissions in the year were 2,453.3 tCO_2e, comprised of direct emissions (Scope 1) amounting to 70.9 tCO_2e, and indirect emissions (Scope 2) amounting to 418.0 tCO_2e. The source of other indirect emissions (Scope 3) comprised 1,964.4 tCO_2e. Scope 1 emissions have decreased by 21.7 per cent. Scope 2 emissions have decreased by 14.4 per cent compared with 2016 due to the decarbonisation of the UK power grid. Scope 3 emissions have also decreased compared with 2016 due, in part, to a reduction in airline travel, most notably short haul flights.

Types of Emissions	Activity	2017 tCO_2e	2016 tCO_2e
Direct (Scope 1)	Gas *(measured in kWh)*	**70.9**	90.5
	Refrigerant *(measured in kg)*	**0.0**	0.0
Indirect Energy (Scope 2)	Electricity *(measured in kWh)*	**418.0**	488.5
Indirect Other (Scope 3)	Business Travel *(measured in miles and GBP)*	**1,619.5**	1,624.3
	Additional Upstream Activities[1] *(measured in kWh, litres, miles and spend)*	**299.7**	308.7
	Water *(measured in m^3)*	**7.2**	25.9
	Waste *(measured in kg)*	**4.4**	1.7
	Paper *(measured in reams)*	**6.9**	5.5
	Hotels *(measured in hotel nights)*	**26.7**	17.2
Gross Emissions (tCO_2e)		**2,453.3**	2,562.3
Gross Emissions per FTE (tCO_2e/FTE)		**12.0**	12.9
Carbon Credits		**2,454**	2,563
Total Net Emissions after offset (tCO_2e)		**0.0**	0.0

(1) Additional Upstream Activities include Well-to-Tank and Transmission & Distribution emissions. These are emissions associated with the upstream processes of extracting, refining, and transporting raw fuel to our business.

Emissions from water (Scope 3) have also decreased by 72.2 per cent compared with 2016. This was due to a water leakage at the Bermuda office during 2016, which was subsequently rectified in 2017.

Lancashire has purchased carbon credits to reduce its gross GHG emissions by 2,453.3 tonnes, offsetting its total carbon emissions and remaining carbon neutral.

The Group has chosen to offset its carbon emissions with Carbon Clear by buying credits in the Wind Power Generation Project in India. These offsetting proposals were discussed and agreed with the Group CEO.

Marketplace

We continue to help the development of our marketplace by making employees available to sit on market committees, boards and working groups. During 2017, our employees gave talks at industry conferences, investor days and symposia, and market education programmes. As noted on page 37, we also donate to many of the causes supported by our industry partners through the Foundation.

Our approach

We believe it is important to make our people available to the markets in which we operate, and we do this happily. We also engage actively with our regulators in Bermuda and London, and the Cathedral team is active within the Lloyd's market. With our clients and their brokers, we are happy to welcome them to our offices, but we also travel to see them and their businesses all around the world.

Our focus areas

Clients: we strive to offer clear, fairly priced and useful products that meet their needs across our range of underwriting operations.

Brokers: we are fully committed to supporting a 'broker market' and prize our broker relationships very highly, right across the Group.

Investors: we continue to work hard at investor relations and have an active programme of engagement with investors around the globe.

Regulators: we recognise the need to engage closely with our regulators at the PRA, FCA, BMA and at Lloyd's and seek to be transparent in all our dealings with them.

Corporate responsibility in action

Relay for Life

For the past four years the Bermuda office has participated in the Relay for Life event put on by Bermuda Cancer and Health Centre. This event is part of the Global Relay for Life which is a 24-hour fundraiser that brings communities together in the fight against cancer. We walk to remember those we have lost, celebrate those who have survived, encourage those who are still fighting and give thanks to all caregivers. In 2017, Lancashire's 'Team Tango' was made up of over 100 staff, family and friends. In 2017 our team raised over $25,000 and over the four years we have raised over $75,000. These funds have been used to bring radiation therapy to Bermuda so patients can be treated locally rather than having to travel overseas.

Workplace

We strive to attract and retain excellent employees who drive our appetite to outperform so as to ensure that the talents of our people and our unique culture continue to set us apart from our competitors. Matching the skills, aspirations and values of new recruits to both the role and the values of Lancashire remains a high priority for our business.

Our approach – promoting a positive and diverse culture

The Group promotes an inclusive environment that recognises and values diversity as key to enhancing individual development and maximising business effectiveness. As an equal opportunities employer, we will not tolerate discrimination of any kind in any aspect of employment, including in job advertisements, recruitment, training, promotion, compensation, benefits, advancement and career development. The Group is also committed to a working environment that is free from any form of bullying or harassment.

Our proactive measures to achieve a diverse, vibrant and positive business culture include our 'Respect in the Workplace/ Communications Etiquette' training sessions which are given to all new employees during their induction. The training sessions aim to highlight their responsibilities in preventing discrimination in the workplace and in fostering a positive and productive working environment.

The Group values having a diverse workforce and bases all recruitment decisions on the ability of prospective employees to do the job, without consideration to race, age, gender, sexual orientation, disability, beliefs, background (except as may be pertinent to the requirements of a role, such as educational qualifications or prior employment experience) or nationality.

The Group is currently represented by employees from 12 different nations. The gender split of males to females (see page 56) within the Group is 60/40 per cent respectively.

Lancashire respects, supports and complies with all relevant local Bermudian and UK legal requirements, in particular with respect to rights of freedom of association, collective bargaining and working time regulations.

Staff training and professional development

The Group encourages continuous personal and professional development for all of its employees, whether through individual external training, professional qualifications, performance coaching or 'lunch and learn' sessions.

Individual training and personal development needs are discussed on a regular and ongoing basis by managers and their team members, including as part of the formal performance appraisal process.

Compulsory training is provided to new permanent staff and fixed-term contract staff in relation to a number of topics as follows:

- Tax/Regulatory Operating Guidelines;
- Disclosure (including share dealing);
- Inspections;
- Financial Crime;
- ERM; and
- Respect in the Workplace/ Communications Etiquette.

Other training may be held on an ad hoc, one-off or refresher basis. The training is designed to ensure that all personnel who

are employed by the Group are provided with the skills, knowledge and expertise appropriate to their responsibilities. Quarterly updates regarding attendance at these compulsory training sessions are provided to the Board for information purposes.

Employee turnover and third party contractors

Among the Group's employees, the turnover for 2017 was 16.2 per cent (a decrease from 20.1 per cent in 2016), and as at 31 December 2017, 10.1 per cent of the workforce was composed of third party contractors, a decrease from 11.6 per cent in 2016. The rate of staff turnover and third party contractors was driven principally by changes in our Lloyd's platform, where there continued to be a process of refreshment and renewal implemented during 2017.

Our focus areas

Our focus in 2017 has been to maintain the success of our employees through ongoing training and coaching, provided both internally and externally. During 2017 approximately 67 per cent of our employees undertook formal training supported by the Group. We continue to measure our employees' success through attainment of personal performance metrics as well as performance within the Group's values framework. We can confirm that during 2017 3.4 per cent of our employees were promoted within the Group, supported by the training and development opportunities provided. An area for continuing development during 2018 will be greater standardisation of the appraisal and training frameworks across the Group.

Internship programme – Corporate responsibility in action

Since 2014, the Group and the Foundation have jointly sponsored an internship programme for Bermuda resident college graduates. These graduates are afforded the opportunity to spend two years working and learning about insurance in the Group's London office. The first two-year placement completed during 2016 and one of these graduates is now a permanent employee within Lancashire and the other has obtained a role at another market insurer in Bermuda. The Group has since welcomed two further graduates during 2016 and 2017, respectively.

Corporate responsibility in action

Project Transform

Every year since 2010, six to eight employees from across the Group volunteer to travel to the Philippines and work alongside ICM for a week providing aid and support to those living in ultra-poverty. The 2017 Project Transform volunteers have reflected on their experience and summarised their thoughts:

"The members of the 2017 Project Transform team were very grateful to have been selected to travel to the Philippines and work with ICM.

We each applied to be part of the team due to the positive feedback shared by previous team members. The team were keen to help people less fortunate than ourselves, as well as better understand some of the challenges ICM is trying to overcome locally.

During the project week we had the opportunity to see how ICM are trying to reach and educate as many people as possible. Our work included building projects and delivering educational talks within various communities.

> **"Ultimately ICM gives people hope for the future."**

We loved spending time and interacting with the communities we visited and could see first-hand that lives have clearly been changed by the work of ICM. The week with ICM was a humbling experience which made us all see the world a little differently. Ultimately ICM gives people hope for the future."

The Lancashire 2017 Project Transform team – Steven Hartley, Shirley Donovan, Susan Blasetti, Mathew Churm, Samantha Cobb, Sean Pitcher, Louise Cowin and Harry London.

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members of staff have volunteered to participate in ICM's Project Transform in the Philippines since 2010.