

Understanding risk.  
Seeing the opportunity.



## OUR PURPOSE IS TO...

- Deliver bespoke risk solutions that protect our clients and support economies, businesses and communities in the face of uncertain loss events;
- Manage our risk exposures and capital resources to generate returns for our investors; and
- Support our people and work with our stakeholders; fostering a positive, sustainable and open business culture to the benefit of society.

### STRATEGIC REPORT

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## FROM OUR BEGINNING

### 2005: Inception

**\$1bn**

LHL was incorporated in Bermuda on 12 October 2005 and raised over \$1 billion via an initial public offering on AIM on 16 December 2005.

Our focus has always been that 'underwriting comes first' as we seek to capitalise on the opportunities of the market.

### 2008: LHL profitable in a year of significant market losses

In 2008 there were very substantial losses to the (re)insurance markets, both from insured events and the impact of the financial crisis, testing Lancashire on both sides of the balance sheet. Even in such challenging circumstances we delivered a combined ratio of 86.3% and a positive total investment return of 3.1%.

### 2009: Listing on the LSE

Our listing on the main market of the LSE was built on four years of strong performance and the indication of pricing improvements across our business lines. With opportunities and capital, we began to grow, and others withdrew from the market.

### 2011: Resilience in the face of volatility

With the insurance sector reeling from record breaking, \$100 billion losses, Lancashire's focus on fundamentals over diversification paid off, with superior combined ratios compared to competitors reflecting our exceptional risk management. Our nimble approach to capital allowed us to take advantage of this post-loss market. We launched the Accordion third-party capital reinsurance facility.

### 2012: Focusing our core portfolio

In a year of flat demand and ample industry capacity, Lancashire optimised its portfolio, in order to better balance our exposure and focus on more profitable areas. We launched the client-facing third-party capital reinsurance facility, Saltire, and issued \$130m of senior debt.

## WE HAVE UNDERSTOOD THE CYCLE

**2014: Returning capital to shareholders**

**\$346.0m**

returned to shareholders

With low rates making investment of capital into the market unattractive, the Group delivered on its commitment to instead return excess capital to our shareholders. Over time we have a proven record of doing so, actively managing our capital to adjust to conditions.

**2013: Broadening capital base**

Against a backdrop of capital oversupply and market softening, Lancashire broadened its base to access different kinds of capital through the purchase of Cathedral (now Lancashire Syndicates) and the establishment of Kinesis (now LCM).

**2018: Lloyd's review**

An overdue review by Lloyd's of underperforming classes leads to a number of (re) insurance businesses leaving the market, reducing the supply of risk capital and contributing to the improvement in rates.

**2017: Loss events stress test Lancashire**

2017 saw three major hurricanes, Harvey, Irma and Maria, two earthquakes in Mexico, and wildfires in California. Lancashire's careful balancing of risk and return managed its exposures, where others with higher exposure were forced to leave the market.

## WE CAPTURE OUR OPPORTUNITIES

KPI  
Combined  
ratio  
**80.9%**  
2018: 92.2%

KPI  
Total  
investment  
return  
**4.9%**  
2018: 0.8%

KPI  
Total  
shareholder  
return  
**34.3%**  
2018: -12.7%

KPI  
Dividend  
yield  
**1.5%**  
2018: 4.5%

KPI  
Return  
on equity  
**14.1%**  
2018: 2.4%

Profit  
after tax  
**\$117.9m**  
2018: \$37.5m

For APMs refer to page 176



TO DELIVER BESPOKE RISK SOLUTIONS

# Protecting against uncertainty



## Five business segments

Our focus is on short-tail, specialty (re)insurance risks within five general segments: Property, Energy, Marine, Aviation and Lancashire Syndicates.

### 2019 gross premium written by segment:

#### ■ Property

Lancashire covers property catastrophe excess of loss, terrorism, property political risk, property risk excess of loss, property retrocession and other property.

#### ■ Energy

Lancashire covers worldwide offshore energy, Gulf of Mexico offshore energy, onshore energy, energy liabilities, construction energy and other energy.

#### ■ Marine

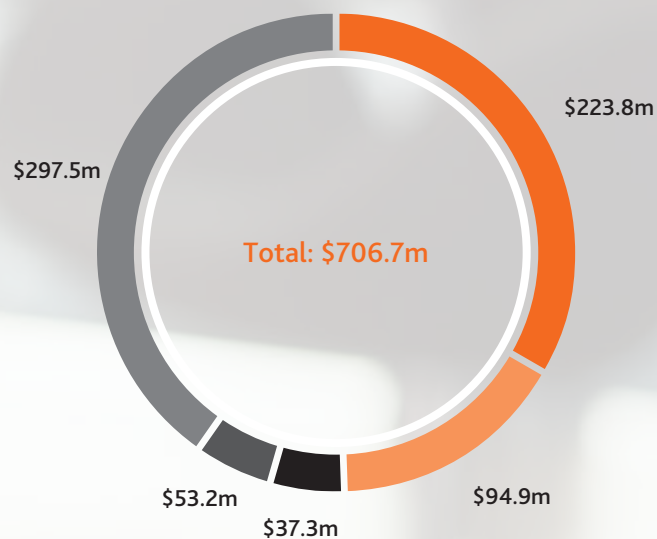
Lancashire covers marine hull and total loss, marine builders' risk, marine excess of loss, marine P&I clubs, marine hull war and other marine.

#### ■ Aviation

Lancashire covers AV52, aviation deductible and other aviation.

#### ■ Lancashire Syndicates

Syndicates 2010 and 3010 cover property reinsurance, property direct and facultative, aviation deductible, other aviation and satellite, marine cargo, energy and terrorism.



A close-up photograph of a person's hand holding an orange pen, poised to write on a white document. The person is wearing a grey suit jacket. The background is blurred, showing more of the suit and a dark chair.

MANAGING OUR CAPITAL

# Focusing on managing risk and generating investor returns



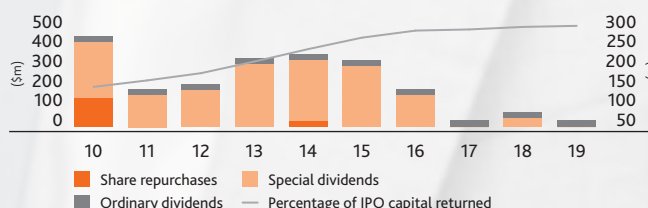
## Our investment case

To generate meaningful returns for our investors across the insurance cycle.

### Producing a solid performance across the insurance cycle

Lancashire has a proven record of returning excess capital to shareholders over time.

### Proven record of capital management



### Delivering across the cycle

Since our inception, we have a history of delivering shareholder returns across the cycle.

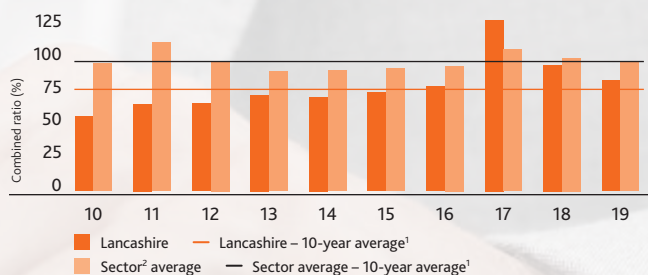
### Total shareholder return



### Experienced underwriters producing higher returns

Group management and our underwriters have decades of experience in rated companies, Lloyd's and collateralised markets.

### Combined ratio



1. Ten-year average based on 2010-2019 reporting periods. Sector ratios are weighted by net premiums earned.

2. Sector includes Arch, Argo, Axis, Beazley, Everest, Greenlight, Hanover, Hiscox, Renaissance Re and Third Point Re.

The 2019 results for Argo, Greenlight, Hiscox and Third Point Re are not available at the time of the report.

Source: Company reports



ENGAGING WITH STAKEHOLDERS

There for those  
who rely on us

## Our core stakeholders

The Group values its relations with, and works to support, its stakeholders to ensure the success of the business. We engage constructively with our people, our stakeholders and in society.

Since its foundation in 2005, the Group has focused on fostering relations with a broad range of stakeholders.

### Our people

Our employees are the lifeblood of the organisation and the Group therefore strives to attract and retain excellent individuals who share our drive and appetite to outperform.

See page 42 for further details.

### Our policyholders

Policyholders are central to our business, so understanding and serving their commercial requirements is at the forefront of everything we do. Through our range of underwriting platforms, we strive to offer clear, fairly priced and useful products.

See page 43 for further details.

### Our shareholders

As a premium-listed company on the LSE, LHL understands the importance of its obligations to shareholders. We work hard to foster good investor relations and pride ourselves on having an active programme of engagement with our diverse shareholder community.

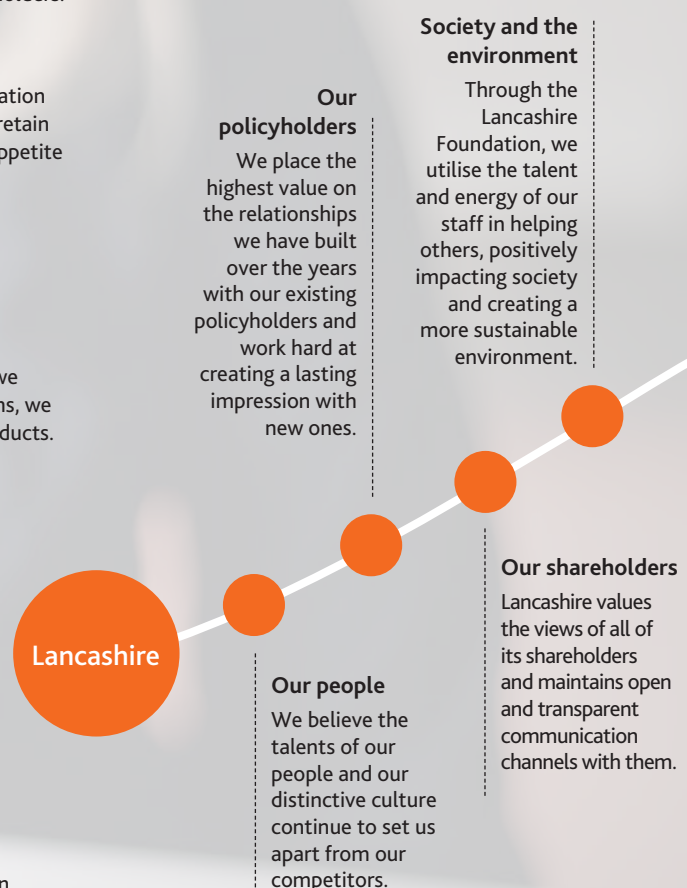
See page 44 for further details.

### Society and the environment

Our insurance products deliver social benefits in helping businesses and communities manage and mitigate the risks they face.

Lancashire is strongly committed to giving back to the communities within which it operates and also further afield. The business seeks to help those who are in distress or at a disadvantage, through continued support of local initiatives and activities, volunteering days, mentoring opportunities and fundraising events.

See page 44 for further details.





# A strategic approach to risk, capital and returns

**Peter Clarke**  
Non-Executive Chairman



The Board pays particular attention to the Group's purpose of delivering insurance solutions for our clients and managing our risk and capital resources across the insurance cycle. We aim to generate meaningful returns for our investors whilst fostering a positive, sustainable and socially beneficial business and culture.

## How did the business perform during 2019?

Lancashire has generated a strong return on equity of 14.1% for 2019 and an impressive combined ratio of 80.9% which, in view of the challenge of another year impacted by catastrophe and risk losses, are a tribute to the Group's underwriting and risk management expertise.

## How does the Board expect strategy to develop in 2020?

The Board regularly monitors business performance to ensure that we maintain Lancashire's record of nimble risk monitoring and capital management. This has meant that over several recent years the Board has returned some of our capital to shareholders in circumstances where it has not been required to meet the risk capital requirements of our business. As Alex notes in his introductory comments (see page 12), after many years of a downward pricing trend across those property catastrophe and specialty classes in which we underwrite, there is currently an expectation of an improved pricing environment during 2020, which may afford the Group the opportunity to assume more underwriting risk.

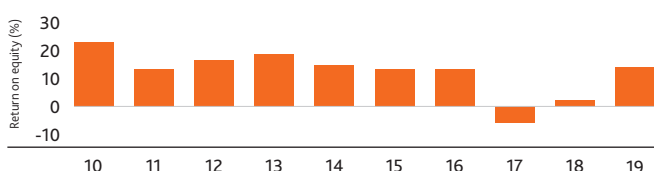
## How does the Board view the capital requirements of the business?

The Board regularly considers the balance of risk and return when setting our capital levels, using capital for underwriting when the opportunity presents itself and returning capital to shareholders when it is not needed. As we enter 2020, we believe that our capital resources are appropriate for the current market opportunity, but the Board will continue to adopt a flexible approach to capital management.

An important tool within Lancashire's active capital management strategy is the flexibility afforded to us by shareholders during the last eight years to issue up to 15% of Lancashire's shares on a non pre-emptive basis. The best opportunities in the insurance and reinsurance sectors typically arise following major loss events, and the flexibility to issue shares and raise capital quickly is a central pillar of our business strategy and will help the Group maximise underwriting opportunities for the business. Once again, the Group is seeking shareholder support for resolutions at the 2020 AGM, allowing this capital management flexibility, and I would encourage all shareholders to vote in favour.

**"As we enter 2020, we believe that our capital resources are appropriate for the current market opportunity, but the Board will continue to adopt a flexible approach to capital management."**

### Return on equity



### How has the Board developed its dividend strategy?

Our dividend and capital management strategy has not changed and in view of the anticipation of an improving underwriting environment the Board has decided not to declare a special dividend in respect of the 2019 financial year. In addition, for the first time, we propose to make our final ordinary dividend subject to a shareholder vote of approval at the April 2020 AGM which will be held in Bermuda, with a live shareholder video link from our London office. Details are set out in the Notice of the AGM.

Assuming such shareholder approval, the aggregate of all dividends for the 2019 year will amount to \$0.15 per common share. Lancashire's nimble capital management and dividend strategy is well understood by our shareholders and the dividend policy is set out on page 96 of this Annual Report and Accounts.

### What risk factors have most affected the Board's thinking in 2019?

The fundamental risk which we consider as a Board is the underwriting risk which we assume as a Group. In this regard, readers will be interested in the work which we carry out in setting capital risk tolerances for underwriting risk and in monitoring those risks, which are described in more detail in the risk section of this Annual Report and Accounts (see pages 30 to 39) and in the summary of the Group's probable maximum losses (PMLs), which are monitored by the Board on at least a quarterly basis. In his report on page 13, Alex mentions how we think about climate change risk within the business. This is increasingly a topic of debate within the Board and its various Committees (see the Risk and Governance sections of this report commencing respectively on pages 30 and 48 for further discussion of these issues).

The Board has also monitored the risk arising from the UK's Brexit process during the year. We are satisfied that measures are in place to mitigate some of the adverse effects on the Group's business, although this matter will be kept under review during the coming year. For a further discussion please see the Risk section at page 38.

Other areas of focus for the Board during the year have included oversight of business culture within the Group as well as issues of staff development, retention and succession. Please see my introduction to the Governance section of this report on page 48 for an account of the work of the Board in these and other areas and our governance arrangements for the 2019 year.

**Peter Clarke**  
Non-Executive Chairman

The Board announced the appointment of Natalie Kershaw as an Executive Director and Group CFO on 5 December 2019. Natalie will assume her new roles on 1 March 2020.

"I look forward to welcoming Natalie to our Board and to the fresh insights that she will bring to her role."  
– Peter Clarke

"Natalie has been an insightful and dedicated team member for nearly 10 years. Her appointment is testimony to the strength of our management team and our succession planning."  
– Alex Maloney



# A model for success

We leverage our deep underwriting expertise with efficient management of risk and capital and resources across our three platforms to provide our clients and brokers with bespoke solutions for their insurance and reinsurance needs.

We always focus on the risk-adjusted return.

## Our strengths

### Customer focus

- Long-term established relationships with clients and brokers
- Continuous support across the cycle
- Prompt payment of valid claims

### Expert people

- Experienced management team with proven ability
- A lean business operation allows us to remain nimble and make decisions efficiently
- Highly specialised multi-class products with barriers to entry in terms of data and modelling expertise

### Disciplined risk and capital management

- Rigorous systems for risk monitoring and management
- Strong record of capital management
- Manage volatility by optimising capital and the underwriting portfolio through the market cycles

### A diverse offering

- Three established platforms: Lancashire, Lancashire Syndicates and Lancashire Capital Management
- Access to multiple markets providing clients with versatility and ourselves with underwriting opportunities
- A stable core book of business and disciplined underwriting

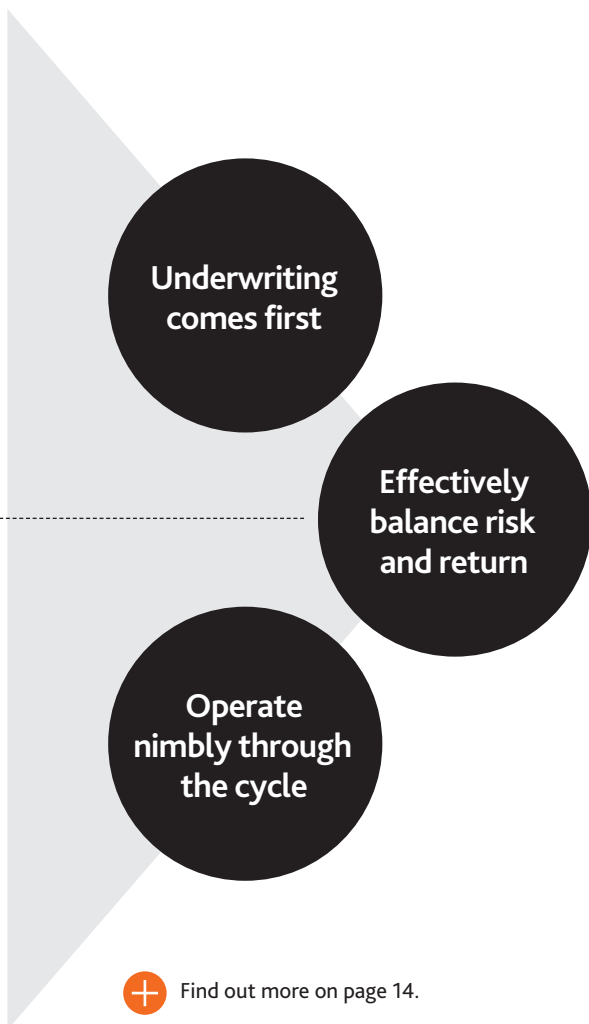




## Our responsibility

We recognise that our responsibility as a company and as individuals reaches wider than our shareholders and our clients. We strive to be a good employer, a good corporate citizen and a responsible preserver of resources. Through the Lancashire Foundation, we make financial contributions and provide human support to a number of good causes in the places we operate around the world (for further details see pages 45 to 47).

## Our strategy



## The value we create for

### Our people

**85%**

of our employees felt positively engaged with the business based on a recent staff survey

### Our policyholders

**\$310.3m**

gross paid losses

### Our shareholders

**34.3%**

Total shareholder return

### Society and the environment

**46%**

of staff volunteering time to the Lancashire Foundation

# Providing risk solutions in a changing world

**Alex Maloney**  
Group Chief Executive Officer



Our purpose as a business is to deliver bespoke risk solutions which help protect our clients in the face of uncertain loss events. It is therefore central to our strategy to develop and retain underwriters and other experts in risk management with the expertise to appraise and price risk properly and to ensure that we use our capital to support our business whilst delivering sustainable returns to our investors.

## Did Lancashire perform as you expected in 2019?

We have generated a strong return on equity of 14.1% and a combined ratio of 80.9%. The return comes from a combination of underwriting and investment returns and represents a good outcome for our shareholders. For me, one of the most pleasing outcomes of these results is that they illustrate that the Lancashire Group has not been materially impacted by the catastrophe reserve deterioration on prior year losses, which has affected some in our industry.

Lancashire has the expertise, the capital, the commercial long-term relationships and the nimble business culture to succeed, and the results for 2019 are testament to the open, honest and sustainable approach we take to underwriting and risk management across the insurance cycle.

## How was the Group impacted by the catastrophe losses which occurred in 2019?

With the occurrence during 2019 of typhoons Faxai and Hagibis in Japan and hurricane Dorian in the Caribbean and along the U.S. south-east coastline, we saw the tragic results of catastrophe loss activity. These events once again caused disruption to lives and livelihoods. There were also significant large aviation, energy and political risk losses during the year which have impacted those specialty lines which form a major part of our underwriting portfolio.

As a Group we established aggregate net loss reserves in respect of typhoons Faxai and Hagibis, and hurricane Dorian of \$52.1 million. But the 2019 losses must be viewed within the context of the catastrophe losses of 2017 and 2018, which taken together produced the largest aggregate losses to the global insurance market in recent memory.

So, while in economic terms the 2019 losses should be considered relatively unremarkable, the fact that they amount to another sequence of mid-sized catastrophe losses serves to demonstrate the continuing need within the insurance industry for a re-rating of pricing in many traditional property and specialty lines.

## What challenges and opportunities do you see over the coming year?

The pressure on insurance risk capital has been further heightened by the recent industry reappraisal of many of the reserving assumptions within the longer-tail casualty classes, and the need to strengthen reserves. Whilst Lancashire has not traditionally operated in the casualty space in any meaningful way, the combination of reserving and pricing pressure across international (re)insurance markets in short-tail catastrophe and specialty lines and in the longer-tail casualty classes has produced an appreciation across our sector that the products we sell need to be sufficiently priced to attract the risk capital on which our industry relies.

**"During 2019, I was pleased to see controlled top-line growth in our premium income, which was a measured response to an improving market environment. As things stand, we believe the positive pricing trend is likely to continue in many of our core specialty and catastrophe lines in a move towards better pricing."**

Although we are still in the early stages of a necessary market correction, developments over the past year or so have illustrated once again that our industry is cyclical in nature and that the key to long-term sustainable success is to show underwriting discipline across that market cycle.

At Lancashire we have taken the difficult decision over the recent years of the soft market phase of the cycle to shrink our top-line income, which reflected the challenging pricing environment. During 2019, I was pleased to see controlled top-line growth in our premium income, which was a measured response to an improving market environment. As things stand, we believe the positive pricing trend is likely to continue in many of our core specialty and catastrophe lines in a move towards better pricing. However, this cautious optimism should be tempered by the knowledge that in many insurance and reinsurance classes pricing still sits below a level which we consider to be sustainable. So, in what remains a competitively priced market, there will be some opportunities for organic growth. It is central to our strategy to develop and retain underwriters and other experts in risk management with the expertise to appraise and price risk properly, to structure and manage our outwards reinsurance protections and to ensure that we use our capital to support our business whilst delivering sustainable returns to our investors.

Paul Gregory discusses the underwriting environment in more detail in his underwriting review on page 20.

### **How does climate change affect the longer-term prospects of the Group's business?**

As a business we have a relatively small headcount of a little over 200 people and our own carbon footprint (which we offset through the purchase of carbon credits) is small relative to many listed businesses of our market capitalisation (see page 44). Perhaps even more important is the trend over the last three years of the increased frequency and severity of weather-related loss events, which I mentioned above. Such a trend will ultimately be understood and managed over longer time frames. What this illustrates is the value of our insurance and reinsurance products to our clients in managing their climate change risks and exposures, in particular through the catastrophe-exposed property insurance and reinsurance products which we underwrite. Our purpose as a business is to deliver bespoke risk solutions which help our clients manage the threats they face from unpredictable perils. It follows as a central pillar of our strategy and its operation that we monitor and manage our own risk exposures

to both weather-related and other catastrophic loss events.

Our investment portfolio is conservative in nature and has limited exposure to climate-related risk. As a business, we are a long-term partner of many clients operating in the oil and gas exploration and development sectors and within power generation and distribution. We recognise the potential environmental effects of carbon emissions, and in a global commercial and political environment, which currently remains reliant on carbon-based forms of energy production, we will work with our clients through a period of global energy transition to help manage their operational and catastrophe-exposure risks in a controlled and responsible way. We also insure many clients in the renewable energy sector, and in this regard please see Paul Gregory's introduction to the underwriting review on page 20. We have also decided to become signatories to the UN Principles for Sustainable Insurance (see pages 52 to 54). Our strategy is to respond nimbly to the demands of a changing world, and we believe this flexibility will help guarantee viability over the longer term.

### **How has the Group developed the Lancashire brand recently?**

We have made a few name changes to our Lloyd's and reinsurance third-party capital management platforms. Our Lloyd's managing agent, Cathedral Underwriting Limited, has changed its name to Lancashire Syndicates Limited (LSL), and our third-party capital management operation, Kinesis Capital Management Limited, has changed its name to Lancashire Capital Management (LCM). There has been no change to the ownership or operation of these businesses. This helps clearly align the 'Lancashire' name and brand across all platforms within the Lancashire Group of companies.

### **Can you tell us about the developments in the Group executive team and business over the last year?**

We announced in May 2019 that, after slightly more than 13 years of service at Lancashire, Elaine Whelan decided to retire from the Group and will step down as our Group CFO and from the LHL Board at the end of February 2020. Personally, I would like to thank Elaine for her years of support and advice to me and to our business. Elaine has been one of the architects of our successful strategy over many years, in particular in the area of our nimble capital management and the delivery of strong cross-cycle returns to our shareholders.

As we say farewell to Elaine, I am pleased to welcome Natalie Kershaw as Elaine's successor to the role of Group CFO and a member of the LHL Board (see page 49 for more details). During the year we have also seen the progression of other colleagues within the Group. Emma Woolley became CEO at LSL, John Cadman (our Group General Counsel) became CEO at LUK, and Hayley Johnston will become our Bermuda CEO at LICL, replacing Elaine in that role. James Flude will assume the role of our LUK CUO, replacing Hayley, subject to regulatory approval.

I would like to thank these and all our staff across our businesses in London and Bermuda, for having contributed to a strong performance for the year. I look forward to leading our excellent team in meeting the challenges and developing the opportunities in the year ahead, which has the potential to be a more interesting phase of the insurance and reinsurance market cycle.



**Alex Maloney**  
Group Chief Executive Officer



# Our strategy

## Our goal

Maximising risk-adjusted returns for shareholders



## Our strategic priorities

### Underwriting comes first

Maintaining the right balance between discipline and creativity is key for success, coupled with a strong focus on profitability and risk selection.

**Delivering bespoke risk solutions in a sustainable framework**

### Effectively balance risk and return

Not seeking top-line growth for the sake of it in markets where we do not believe the right opportunities exist and rigorously monitoring and managing our risk exposures.

**Peak-zone PML limits of 25% of capital**

### Operate nimbly through the cycle

Our speed and agility in the way we manage volatility helps us underwrite our core portfolio profitably through the challenges of the cycle, yet seize opportunities when they present themselves.

**Maximise risk-adjusted returns**



## How we serve clients and brokers

Significant capacity across the cycle allowing us to provide consistent support

A lean structure allowing resources to be refocused quickly when needed

Strong processes and structures supply challenge and assurance

## Our culture

The bedrock of our strategy is a culture of co-operation and respect based on open challenge

## Underwriting comes first

### Description

We focus on maintaining our portfolio structure and our core clients, with the bulk of our exposures balanced towards significant events. We will grow in existing and new classes where favourable and improving market conditions exist. We use the principle of peer review throughout the Group, usually prior to underwriting business for LICL, LUK and LCM, the platforms that accept larger net exposures, and post-underwriting at LSL, with its smaller net exposures.

### Achievements

Successfully embedded the new underwriting teams in downstream energy, power & utilities and aviation, which we hired during 2018. We have grown the funds raised and capital deployed from LCM investors and grown LCM's client base for the second consecutive year. LUK has decided to re-enter the D&F class of business.

### Performance

#### Combined ratio

# 80.9%

A strong combined ratio, even in a loss-impacted year, evidences our continued focus on underwriting, our general appetite for less attritional exposures, our superior risk selection and our portfolio construction.

#### Gross premiums written

# \$706.7m

With an improving rating environment in the majority of our classes, plus business generated by new teams hired in 2018, premiums have grown year on year. We maintain the discipline to decline or restructure our participation on under-priced or poorly-performing business but are willing to accept more risk if the market opportunity allows.

### Associated strategic risk

The key risk in the current market phase is the potential loss of relevance to brokers and clients. While there is still some surplus capacity in the market, insurers need to have a unique selling point. For the Group, that is found in its mixture of underwriting capacity, leadership capability, claims service and multiple balance sheet options.

## Effectively balance risk and return

By bringing together all our disciplines – underwriting, actuarial, modelling, finance, treasury, risk and operations – at our fortnightly RRC meetings, we are able to look at how different parts of our operations are working together. We tailor our reinsurance programmes to manage our exposures and we stress test our business plans and gauge where we can be most effective without undue volatility. Management reports our risk exposures and management to the Board.

We have increased our underwriting footprint and optimised our portfolios in areas where rating has improved whilst adding new complementary classes of business as the market conditions are now improving.

#### Return on equity

# 14.1%

A good result in the light of a challenging market and the incidence of natural catastrophe and risk losses in our major portfolios of business, helped by our improved outwards reinsurance programme and investments.

#### Probable maximum loss

# \$152.0m\*

We continued to match our exposure to key catastrophe perils to the market opportunity, demonstrating our discipline and nimbleness.

\* 1 in 100-year Gulf of Mexico hurricane expected net loss at 1 January 2020.

The key issue for Lancashire is to continue to serve our clients and brokers with significant capacity, whilst ensuring that the portfolio is balanced. This means constantly reassessing our business mix and testing key risk assumptions.

## Operate nimbly through the cycle

As capital supply fluctuates 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.

Profits for 2019 have largely been retained for 2020 underwriting opportunities. Lancashire renewed its 15% disapplication of pre-emption rights at the 2019 AGM to assist potential future capital raises.

#### Percentage of comprehensive income returned to shareholders

# 20.7%

Lancashire continues to exercise the discipline of maintaining sufficient capital headroom to support underwriting operations and take advantage of new opportunities as they emerge or returning capital to shareholders it cannot profitably use.

#### Dividend yield

# 1.5%

Current opportunities exist in the short-tail specialty insurance classes that, in general, require less capital than catastrophe exposed classes, so we grow in these areas but still provide modest capital returns. If opportunities exist in capital-intensive product lines then capital will be retained to take advantage of these opportunities.

Lancashire has developed an expectation among its shareholders that it will produce a consistent return and pay ordinary dividends with supplementary special dividends only when it makes sense to do so. We believe our shareholders understand that in harder markets Lancashire will retain, and potentially even raise, capital to take full advantage of underwriting opportunities.

# A solid underwriting performance combined with positive investment returns

**Elaine Whelan**  
Group Chief Financial Officer



While Lancashire has clearly picked up losses from the 2019 events, our share was very manageable and well within our expectations. Our predominantly fixed maturity investment portfolio also performed well in a declining yield environment, supported by strong performance from our risk asset allocation. All that has meant a welcome change to the relative battering of the last two years and a return to strong profitability.

## How has the Group performed in 2019 within the market environment?

Compared to 2017 and 2018, 2019 saw much lower annual global insured losses. While insured losses from man-made and natural catastrophes were below the 10-year average, it wasn't a benign year by any stretch of the imagination with the significant windstorms Dorian, Faxai and Hagibis occurring and wreaking havoc in their respective regions. There was also significant adverse development for the industry as a whole on the 2018 typhoon Jebi. There have been some meaningful industry risk losses as well and we also saw a general uptick in attritional losses across the industry this year. That all sounds a bit bleak, but I think what we have seen is a reaction by the industry to the losses of the last few years and the recognition that pricing had to move. While that's not where it needs to be yet, Lancashire has been adding new teams to the business over the last few years, positioning ourselves for the improving market that we hoped to see. Our patience has paid off in that regard and we have, for the first time in a long time, been able to add a meaningful amount of new business to our top line. While we have yet to see that factor through to the bottom line – it takes a little while for the timing impacts of the new business to flow through to earnings – that has been all about putting ourselves in the best possible position for the pricing improvement we are expecting. While Lancashire has clearly picked up losses from the 2019 events I have mentioned, our share was very manageable and well within our expectations. Our predominantly fixed maturity investment portfolio also performed well in a declining yield environment, supported by strong performance from our risk asset allocation. All that has meant a welcome change to the relative battering of the last two years and a return to strong profitability. We are pleased to have produced an RoE of 14.1% and a combined ratio of 80.9%.

## Do you anticipate needing to raise more capital in 2020 to take advantage of an improving market?

The short answer is no. Or not yet. While it's great to finally see the market turning, it's from a low base and still has some way to go before we get too excited about it. We're probably back to around 2014/2015 pricing levels now and we'd like to see that move more before we think the economics make sense to raise more capital. We have enough existing capital to take advantage of what we are seeing in terms of opportunities, and also remember that many of the new lines of business we have added are in specialty lines and not too capital intensive. I think we would say the current market is "interesting". Which means we will be watching how it develops closely rather than jumping in. If there are more opportunities,

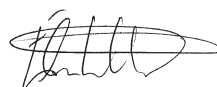
with the right economics, then we will certainly be ready to go to market. Our shareholders remain supportive of our capital management approach. That is greatly appreciated, and also comforting to know that they are ready to support a capital raise if there are good reasons to do so.

### What does that mean for special dividend expectations?

Given my comments above on an improving market, we chose not to declare a special dividend with our November 2019 trading statement. There was also a fair amount of uncertainty heading into the January renewals, particularly around the retro markets. It seemed prudent for us to keep the capital while we see how that develops. With the 1 January 2020 renewal season behind us now, we do expect the market to continue to improve through 2020 and we have therefore again chosen to retain our capital. We have always said our special dividends are indeed special, and most of our shareholders understand that and see it as good news in the context of improved future returns.

### How does the U.S. Federal Reserve's recent pivot impact Lancashire's investment portfolio?

We are back in a lower yielding environment. Although we hadn't actually really left it! But rates will be lower going forward across the majority of our portfolio. We have already had the initial benefit of rate reductions on the valuation of the fixed income portfolio. We don't expect to see any significant benefit there going forward and there isn't much more benefit to be had from future spread compression either. We do continue to look for ways to add yield to the portfolio, without adding too much risk, and we will continue to do that. We have recently decided to redeem about half of our hedge fund portfolio in 2020. While the volatility remained low and it acted as a good diversifier to the rest of the portfolio, we weren't seeing the returns we had hoped for there. Those funds will be redeployed and hopefully produce a better risk-adjusted return.



**Elaine Whelan**  
Group Chief Financial Officer

## Financial highlights

	2019 \$m	2018 \$m	2017 \$m	2016 \$m	2015 \$m
Gross premiums written	<b>706.7</b>	638.5	591.6	633.9	641.1
Net premiums written	<b>424.7</b>	417.7	398.0	458.7	481.7
Net premiums earned	<b>421.7</b>	413.5	427.9	488.1	567.1
Net insurance losses	<b>129.8</b>	165.4	335.4	142.5	155.7
Net underwriting profit (loss)	<b>186.5</b>	121.7	(23.1)	213.5	265.2
Net investment income	<b>37.7</b>	34.7	30.5	29.8	29.8
Net realised gains (losses) and impairments	<b>8.9</b>	(5.1)	9.1	(2.4)	(2.8)
Profit (loss) after tax <sup>1</sup>	<b>117.9</b>	37.5	(71.1)	153.8	181.1
Net change in unrealised gains/losses on investments	<b>27.8</b>	(12.8)	4.9	4.1	(11.3)
Comprehensive income (loss) <sup>1</sup>	<b>145.7</b>	24.7	(66.2)	157.9	169.8
Dividends <sup>2</sup>	<b>30.2</b>	70.2	29.9	178.9	317.5
Diluted earnings (loss) per share	<b>\$0.58</b>	\$0.19	(\$0.36)	\$0.76	\$0.91
Fully converted book value per share	<b>\$5.84</b>	\$5.26	\$5.48	\$5.98	\$6.07
Return on equity	<b>14.1%</b>	2.4%	(5.9%)	13.5%	10.9%
Return on equity excluding warrant adjustments	<b>14.1%</b>	2.4%	(5.9%)	13.5%	13.5%
Net loss ratio	<b>30.8%</b>	40.0%	78.4%	29.2%	27.5%
Net acquisition cost ratio	<b>25.0%</b>	30.6%	27.0%	27.1%	25.8%
Expense ratio	<b>25.1%</b>	21.6%	19.5%	20.2%	18.8%
Combined ratio	<b>80.9%</b>	92.2%	124.9%	76.5%	72.1%
Accident year loss ratio	<b>51.3%</b>	70.0%	94.2%	46.2%	46.0%
Net total return on investments <sup>3</sup>	<b>4.9%</b>	0.8%	2.5%	2.1%	0.7%

1. Amounts are attributable to Lancashire and exclude non-controlling interest.

2. Dividends are included in the financial statement year in which they were recorded.

3. Net return on investments includes internal foreign exchange hedging.



## KEY PERFORMANCE INDICATORS

### Return on equity

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#### 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.

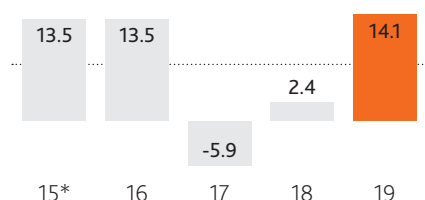
#### Aim

The Group's aim is to maximise risk-adjusted returns for our shareholders across the cycle.

#### Performance

14.1%

Given the sequence of mid-sized catastrophe and risk losses during the year we were pleased to generate a strong RoE for the year, reflecting a solid underwriting performance combined with positive investment returns.



#### Risk management

The stated aim is a long-term goal, acknowledging that management expects both high and low results in the shorter term. The cyclical nature 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 an RoE component in this.

Please refer to the Directors' Remuneration Report on page 74 for further details.

\* RoE including the impact of warrants was 10.9% in 2015. The five-year average was 7.0%.

### Combined ratio

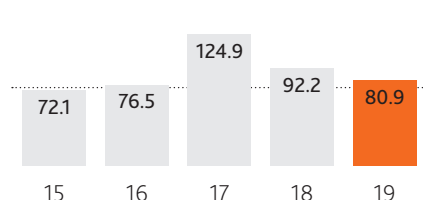
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The combined ratio is the ratio of costs to net premiums earned and is a measure of an insurance company's operating performance. It is calculated as the sum of the net loss ratio, the net acquisition cost ratio and the expense ratio. These ratios are defined in our glossary.

The Group aims to price its business to ensure that the combined ratio across the cycle is significantly less than 100%.

80.9%

The combined ratio reflects the impact of hurricane Dorian and typhoons Faxai and Hagibis. Despite these events our focus on high quality underwriting allowed us to generate an underwriting profit for the year.



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.

### Total investment return

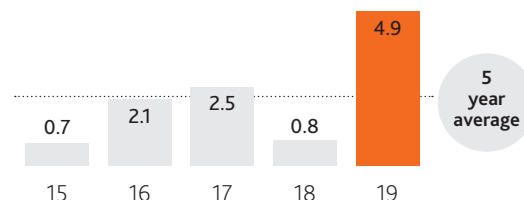
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Total investment return measures investment income and net realised and unrealised gains and losses produced by the Group's managed investment portfolio.

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.

4.9%

In 2019, the Group continued to manage its most significant investment risk, interest rate risk, via floating rate assets and risk assets. This helped to manage the risk on/risk off volatility in the rising rate environment in the first half of 2019.



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 relatively 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.

## Total shareholder return

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### 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.

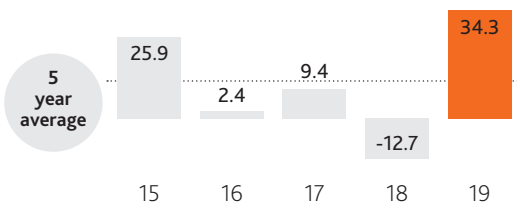
### Aim

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 cyclical nature and volatility of both the insurance market and the financial markets in general will impact management's ability to maximise the RoE in the immediate term.

### Performance

34.3%

Our shares traded well through 2019, reflecting some investor optimism around the improvement in pricing in the insurance market. Towards the end of the year, our shares also benefited from a modest relief rally of all UK assets. In addition, our regular ordinary dividend supplemented the overall TSR.



### 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.

## Comprehensive income returned to shareholders

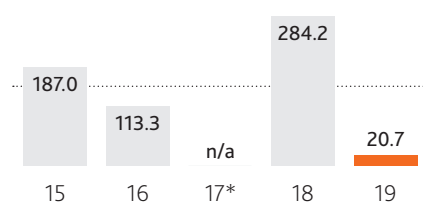
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The percentage of comprehensive income returned to shareholders equals the total capital returned to shareholders through dividends and share repurchases paid in a given year, divided by the Group's comprehensive income.

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 maximise risk-adjusted returns for shareholders.

20.7%

In view of the current market outlook the Group took the decision not to return surplus capital to shareholders in 2019 by way of a special dividend as we position ourselves for the improving market that we hope to see in 2020. Our ordinary dividend payments were unchanged.



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 2019, Lancashire maintained its A rating.

\* 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 four years.

## Dividend yield

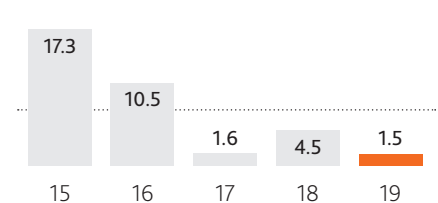
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Dividend yield is measured by dividing the annual dividends per share by the share price on the last day of the given year.

The Group aims to maintain a strong balance sheet whilst maximising risk-adjusted return for shareholders across the cycle. 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.

1.5%

We declared annual ordinary dividends of \$0.15 per share in respect of 2019. The final payment of \$0.10 is subject to shareholder approval at the 2020 AGM.



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.

# Seeing the opportunity

**Paul Gregory**

Group Chief Underwriting Officer



Insurance is an often-underestimated product in the global economy and its value is rarely appreciated until such time as there are losses. Our job is to pay our clients' valid claims promptly whilst also ensuring the premium we receive is adequate to pay these claims and provide appropriate shareholder returns over the long term.

## Introduction

The dynamics of our market are very simple. The basic concepts of demand and supply are the principal drivers of the pricing in the marketplace. From 2013 to 2017, the market for almost all our products experienced a period of oversupply and as such the pricing of those products reduced. This reduction in pricing varied by product line as the dynamics of each area are always slightly different, but the downward trend was consistent. Our response to this environment was to take less risk, by reducing our inwards risk and protecting our portfolio with more reinsurance. Our goal has always been to match risk and return as best we can and ignore pressures to simply grow the top line irrespective of pricing adequacy. We took this approach most importantly because we think this is the right way to manage a business that doesn't sell widgets but sells units of risk protection; and secondly to ensure that when better times did arrive, we were well positioned to maximise the opportunity.

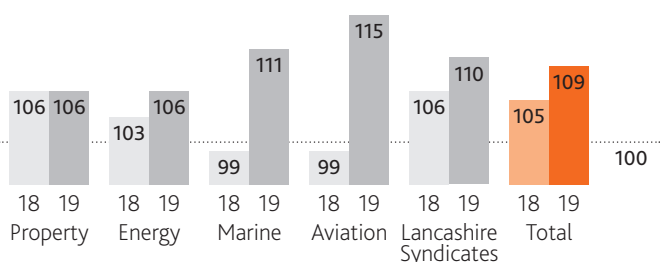
In 2018, we started to see the demand and supply balance begin to tip in our favour, albeit slowly. It was the first year since 2012 that we saw a positive rate movement across our portfolio as a whole. In line with our underwriting philosophy, we grew our premium and added new underwriting teams and products to the Group.

2019 saw a continuation of this trend across most of our product lines, as the demand and supply shift continued to move in our favour. Supply across the market was restricted by various factors including: large carriers reducing risk appetite in underperforming classes; the ILS sector of the property retrocessional reinsurance market wrestling with consecutive years of natural catastrophe losses and significant loss creep on certain catastrophe events; a number of large risk losses; and the Lloyd's performance review starting to take effect. Running adjacent to this, throughout 2019, was the developing story of a creaking casualty market, with several carriers having to bolster reserves on historic underwriting years. As a predominantly short-tail underwriter this casualty development does not directly impact us, but could help further improve broader market conditions should this trend continue, as it may require additional insurance risk capital, which will further restrict supply.

Given these improved market conditions it should come as no surprise that our gross premiums written increased again in 2019. Most of our product lines saw rate increases of varying degrees. As rates improved, we grew our core portfolio and wrote new business in these product lines. Our new teams, added in 2018, have continued to build out and mature whilst also benefiting from the improved rating environments. Our disciplined approach in the softer part of the cycle has meant that our focus for the past two years has been on growing existing and new

"2018 was the first year that we started to see the demand and supply balance begin to tip in our favour, albeit slowly. 2019 has seen a continuation of this trend across most of our product lines, as the demand and supply shift has continued to move in our favour."

Renewal price index (%)



classes and we have not had to shut down or cut back in poor performing product lines, as a number of our peers have had to do.

2019 again had several mid-sized natural catastrophe losses and several large risk losses in areas in which we specialise such as aviation, marine and political risk. It is therefore pleasing to be able to produce a combined ratio of 80.9%. Our clients buy our products for exactly these types of events and this shows the value of the (re)insurance that we provide. Our products help support economies and communities to rebuild after natural catastrophe events, and companies to continue to operate safely and profitably after major loss incidents. Our partnership with our clients helps encourage a good risk management culture, which aids prevention of future major loss incidents. Insurance is an often-underestimated product in the global economy and its value is rarely appreciated until such time as there are losses. Our job is to pay our clients' valid claims promptly, whilst also ensuring that the premium we receive is adequate to pay these claims and provide appropriate shareholder returns over the long term.

For all our natural catastrophe lines of business we are acutely aware of the impact of climate change. The vendor models we use to both assess and price risk are regularly updated to include changing patterns and data. We use this information alongside our own view of risk to measure the frequency and severity of natural catastrophe events across the world. Clearly over the past three years we have seen an increase in frequency as compared to the previous five years. Our role is to assess how the risks we underwrite are changing over time and if we are getting sufficiently well paid for the risks we take onto our balance sheet.

Our outlook for 2020 is more of the same. We anticipate an improving market across most of our product lines. As ever, the dynamics of each market will be subtly different, but the positive pricing trend looks to continue.

Whilst this is pleasing, we are always aware of where we sit in the pricing cycle and the soft market conditions between 2013 and 2017 took a lot of rate and premium out of the system. Although increases in rating in the last two years move us in the right direction, we would not classify the current market as a 'hard market'; it is an improving market.

With this improving underwriting environment in mind, we have chosen not to declare a special dividend to give us maximum flexibility with our capital in order to allow us to grow and take more risk. This aligns fully with our historic capital management philosophy. When there are limited opportunities to deploy excess capital, we will return this to shareholders. When the opportunities improve, and we feel we can deploy it, we retain capital and aim to produce an improved return for shareholders. If the market were to become markedly dislocated, we would seek to raise more capital from our shareholders. Our approach to underwriting and capital management are fully aligned and simply linked with the market environment we see before us. Our actions during each part of the cycle will change, but our philosophy remains constant.



## Property

Our property offering across the Group is split into four principal classes of business: retrocession, property reinsurance, property D&F insurance, and terrorism and political risks. The demand and supply dynamics of each of these classes were very different throughout the course of 2019.

The retrocession market faced two challenging years in 2017 and 2018 with the worst consecutive insured loss years on record. To further add to that challenge, large losses such as hurricane Irma (2017), hurricane Michael (2018) and typhoon Jebi (2018) experienced significant loss creep.

2019 continued to increase pressure on this market with more typhoons in Japan (Faxai and Hagibis) as well as hurricane Dorian impacting the Caribbean and U.S. The losses in 2019, in aggregate, were not of the same magnitude as the previous two years but once again impacted the market, causing billions of dollars of insured loss.

Over recent years the retrocession market has been dominated by the growing ILS market and after years of a benign loss environment the past three years have been a real challenge for this sector. 2019 was the first year that we started to witness supply in the ILS market coming under downward pressure as capital providers started to question the risk-reward metrics they had historically received, given they now understand the potential volatility of the product sold. As supply tightened, pricing firmed as the year progressed.

The Group offers retrocession capacity from all three of our platforms, albeit the majority is sold via our ILS vehicle, LCM. During the softer part of the cycle we deliberately kept LCM relatively small as we were not able to find enough products to sell at the required return metrics of our capital providers. We also did our best to be as transparent as possible with our capital providers, particularly regarding the volatility of the portfolio being underwritten.

Whilst the LCM underwriting result was negatively impacted by the natural catastrophe losses of 2017 and 2018, we were still able to grow LCM in both 2018 and 2019, which is the opposite direction of travel to most ILS vehicles in the market. We believe this is because of our underwriting discipline and transparency. The most important thing is that when the opportunity has improved, we have been able to grow with that opportunity. Our expectation for 2020 is that this market will continue to improve, and we aim to maximise this opportunity across our platforms.

The property reinsurance market has experienced the same natural catastrophe losses as the retrocession market. However, the demand and supply dynamics of this market have not shifted to the same extent. As a result, the pricing environment (whilst still positive) has not moved as much as the retrocession market. Prior to the start of 2019, our expectation was that outside of loss impacted territories such as Japan and Florida, rates would be broadly static with only those loss-impacted territories seeing positive rate movement. The reason for this is that supply of capacity into this sector of the reinsurance market remained relatively stable, so the only drivers of rate movement were the increased cost of retrocession and market sentiment. The market reacted in line with our expectations. Our response was to grow in those areas getting rate increases. We broadened our core relationships with Japanese cedants and started to write a Florida property catastrophe portfolio via our Bermuda office. Moving into 2020 we expect positive pricing in the property catastrophe market, but once again it is unlikely to be to the same extent as we expect to see in the retrocession market. Albeit the more dislocated the retrocession market becomes, the more impact on the property catastrophe market we would anticipate seeing. Dependent upon market conditions, it is likely we will look to grow in certain territories where there is the opportunity to do so.

The property D&F insurance market developed as the year progressed. Similarly impacted by the natural catastrophe events of recent years, the market had seen several capacity withdrawals through the course of the year. The Lloyd's Decile 10 performance review included D&F and as such some markets withdrew from the class and others cut back on their exposure. Just as significantly, some of the larger carriers in this market made substantial reductions to the capacity they offered in the product line. As the effect of this was felt, the pricing began to increase as the year progressed. The Group writes the vast majority of D&F via Lancashire Syndicates and has benefitted from these pricing improvements. The Group also decided to re-enter this class of business through LUK as the market continued to harden into 2020.

The only part of our property offering that did not experience rate increases in 2019 was our terrorism and political risk portfolio. The reason for this is simple. There remained an ample supply of capacity, which outstripped the demand. The world remains a volatile place with incidents of terrorism and political unrest across the globe. However, ultimately, the pricing of our products is driven by demand and supply and unlike our other lines this has not tipped in the underwriters' favour. The product line remains profitable for most carriers and, as such, no one has cut back. Our view is that pricing remains adequate for our risk profile and the product line continues to be profitable for us, so we continue to support our core clients. Absent any shift in demand/supply dynamics, our view is that market conditions for 2020 will be broadly like 2019.

## Energy

Our energy portfolio has a number of components: upstream (offshore) energy, downstream (onshore) energy, renewable energy and power. It is underwritten across our company and Lloyd's platforms. Much like our other classes of business we are seeing different dynamics across the sub-classes.

Downstream energy and power saw supply continue to retract in 2019. Large carriers have reduced their risk appetite following several large losses and increasing attrition. Additionally, these classes fell under the Lloyd's performance review microscope. As a result pricing accelerated through 2019, albeit coming from a historically low base. We entered both these sub-classes during 2018, so our timing had been favourable with the market moving in the right direction. As others retract from these sub-classes we look to grow (whilst always mindful of rating adequacy). We expect pricing to continue to improve in 2020 which will provide us with the opportunity to further build out these portfolios.

Within our power and energy portfolios we support a range of renewable projects around the world. As this industry continues to develop during this period of a global transition to a lower-carbon future, the insurance community helps to provide valuable insurance products that allow such projects to be viable. Renewable energy rates increased during 2019 and we expect this trend to continue into 2020.

Our upstream portfolio saw no supply of capital restrictions. This was primarily because the loss environment, driven by low levels of activity due to oil price levels, has been very benign over the past few years. Therefore, this sector has delivered good underwriting profits and, as such, no one is exiting the class. That said, there is a broad acknowledgement that rating levels are relatively low, so market sentiment had seen pricing improve slowly in both 2018 and 2019, but not to the levels where we would want to broaden our portfolio too much. Our belief is that this market is finely balanced, and it will not take too much loss activity to see rates start to improve more materially. We will remain patient until such time and maintain our core portfolio of risk that has historically performed very well.

## Aviation

The Group underwrites both an aviation insurance and reinsurance portfolio across our company and Lloyd's platforms.

The aviation insurance market saw some historically large losses in 2019. Capacity withdrew from the market due to historical unprofitability and the Lloyd's performance management initiative. Therefore, rates improved throughout the year in all parts of our aviation insurance portfolio.

Our aviation insurance offering was broadened at the end of 2018, with a new team specialising in a niche area of the aviation market. This complemented our existing aviation offering to clients and brokers, and as a result our aviation premium grew in 2019 from both rate improvement and new business.

There remain areas of the aviation insurance market where we still do not have a significant market share given current pricing levels. Should rates change, we have the team and the platforms to increase our market share quickly.

The aviation reinsurance market also improved during 2019, albeit to a lesser extent than the insurance market. The simple reason for this is that less capacity exited this sector. Our portfolio shrank during the soft cycle to a core portfolio of risk, and 2019 was the first year where we have been able to cautiously grow as rates started to improve.

Our general outlook for 2020 is for continued pricing momentum in aviation insurance, allowing us the opportunity to continue to increase our footprint in this class.

## Marine

We underwrite various sub-classes of marine across our company and through Lancashire Syndicates. All our marine classes saw pricing improvement throughout 2019.

Like many of the specialty lines of business we write, marine has been under scrutiny from the Lloyd's performance review which has seen numerous syndicates exit or significantly reduce their marine portfolios. Consequently, market conditions have improved.

Cargo has seen the greatest degree of dislocation. Withdrawal of capacity started in 2018 and continued into 2019 and underwriting conditions have continued to improve. Most of our cargo portfolio is written by Lancashire Syndicates and we have grown with the market opportunity – with the discipline shown in the soft cycle allowing us the platform to grow into the better market.

Most of our remaining marine sub-classes such as hull, builders' risks and liability are underwritten from our company platform. Whilst not at the same level as cargo, these sub-classes have also seen pricing improvement during 2019 as supply restrictions manifest themselves.

Our outlook for marine in 2020 is for continued rating improvement. Depending upon the extent of this improvement we will look to develop our marine portfolio further.

## Overall

In summary, the rating environment seen in 2019 played out broadly as we predicted at the start of the year. We have been able to grow into the improving market and our new teams have benefited from an improved rating environment, allowing them to develop their portfolios. We are very pleased to produce a combined ratio of 80.9% in a year with several mid-sized natural catastrophe losses as well as some large risk losses. This demonstrates our rigorous approach to risk selection and portfolio management. If the market continues to improve in 2020, as we expect it will, then our aim would be to maximise the underwriting opportunity and deliver appropriate risk-adjusted returns.

# Protecting our clients, balancing risk, and generating returns



**Hayley Johnston**  
Chief Underwriting Officer,  
LUK



**James Irvine**  
Chief Underwriting Officer,  
LICL



**Jon Barnes**  
Active Underwriter,  
Syndicate 2010



**John Spence**  
Active Underwriter,  
Syndicate 3010

## Underwriting results

	2019						2018					
	Property \$m	Energy \$m	Marine \$m	Aviation \$m	Lancashire Syndicates \$m	Total \$m	Property \$m	Energy \$m	Marine \$m	Aviation \$m	Lancashire Syndicates \$m	Total \$m
Gross premiums written	223.8	94.9	37.3	53.2	297.5	706.7	214.6	103.0	31.1	33.0	256.8	638.5
Net premiums earned	121.7	66.5	28.4	23.6	181.5	421.7	131.9	75.9	21.5	17.8	166.4	413.5
Net loss ratio	8.8%	14.1%	13.0%	36.4%	53.7%	30.8%	34.0%	(27.1%)	102.3%	2.2%	71.4%	40.0%
Net acquisition cost ratio	18.6%	33.1%	30.6%	23.3%	25.7%	25.0%	23.9%	44.3%	55.8%	47.2%	24.6%	30.6%
Expense ratio	–	–	–	–	–	25.1%	–	–	–	–	–	21.6%
Combined ratio	27.4%	47.2%	43.6%	59.7%	79.4%	80.9%	57.9%	17.2%	158.1%	49.4%	96.0%	92.2%

### Premiums

Gross premiums written increased by 10.7% in 2019 compared to 2018. The Group's five principal segments, and the key market factors impacting them, are discussed below.

### Property

Property gross premiums written increased by 4.3% for the year ended 31 December 2019 compared to the year ended 31 December 2018. The property segment experienced new business growth along with rate and exposure-related premium increases across all classes of business, particularly in the property catastrophe and political risk classes. Business flow in the political risk class is generally less predictable than other classes of business due to the lead time and specific nature of each deal. The new business was partially offset by the impact of multi-year contracts written in the prior year that were not yet due to renew.

### Energy

Energy gross premiums written decreased by 7.9% for the year ended 31 December 2019 compared to the year ended 31 December 2018. While there was more new business in the worldwide offshore and onshore energy classes in 2019 compared to 2018, the prior year

benefited from the restructuring of an existing Gulf of Mexico multi-year deal in addition to premium adjustments that were made to prior underwriting year risk-attaching business in the worldwide offshore energy class.

### Marine

Marine gross premiums written increased by 19.9% for the year ended 31 December 2019 compared to the year ended 31 December 2018. The growth reflects rate and exposure increases and favourable prior underwriting year premium adjustments in the marine builders' risk class. In the prior year there was a reduction in exposure on prior underwriting year risk-attaching business in the other marine class and less pro-rata business.

### Aviation

Aviation gross premiums written increased by 61.2% for the year ended 31 December 2019 compared to the year ended 31 December 2018. The growth was primarily driven by new and renewal business in the aviation deductible and other aviation classes of business as that underwriting team continues to build their book. The increase was only partially offset by exposure decreases in the AV52 and satellite classes.

## Lancashire Syndicates

In our Lancashire Syndicates segment, our Lloyd's platform, gross premiums written increased by 15.8% for the year ended 31 December 2019 compared to the year ended 31 December 2018. The increase was primarily due to new business in the energy, aviation, marine and terrorism classes of business, offset slightly by lower premiums in the property classes.

## Ceded

Ceded premiums increased by \$61.2 million, or 27.7%, for the year ended 31 December 2019 compared to the year ended 31 December 2018. The increase was primarily due to a combination of additional cover purchased, including some quota share cover for some of the new lines of business we have entered into, and the timing of renewals.

## Earned

Net premiums earned as a proportion of net premiums written were 99.3% for the year ended 31 December 2019, compared to 99.0% for the year ended 31 December 2018.

## Losses

The Group's net loss ratio for 2019 was 30.8% compared to 40.0% for the same period in 2018. The accident year loss ratio for 2019, including the impact of foreign exchange revaluations, was 51.3% compared to 70.0% for the same period in 2018.

2019 was impacted by catastrophe activity in the form of hurricane Dorian and typhoons Faxai and Hagibis. Our net losses recorded for these events, excluding the impact of inwards and outwards reinstatement premiums, was \$52.1 million. In 2018, our net losses from marine and natural catastrophe events, excluding the impact of inwards and outwards reinstatement premiums, was \$104.9 million.

While reserves have been recorded, uncertainty exists on the eventual ultimate net loss estimates in relation to hurricanes, typhoons and wildfires as loss information after these types of events can take some time to obtain. The Group's ultimate net loss estimates for these natural catastrophe events were derived from a combination of market data and assumptions, a limited number of provisional loss advices, limited client loss data and modelled loss projections. As additional information emerges, the Group's actual ultimate net losses may vary, perhaps materially, from the current estimates. The final settlement of all claims is likely to take place over a considerable period of time.

Excluding the impact of foreign exchange revaluations, the table below shows the impact of current accident year catastrophe events on the Group's loss ratio for the year ended 31 December 2019:

	Losses \$m	Loss ratio %
Reported at 31 December 2019	129.8	30.8
Absent all catastrophe events	77.7	18.5

As reported in the Group's results for the year ended 31 December 2018 and excluding the impact of foreign exchange revaluations, the impact of marine and natural catastrophe loss events on the Group's 2018 loss ratio was as follows:

	Losses \$m	Loss ratio %
Reported at 31 December 2018	165.4	40.0
Absent natural catastrophe events	78.6	19.2
Absent large marine losses	147.3	34.7
Absent the combined events	60.5	14.4

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

The total estimated ultimate net loss, excluding the impacts of inwards and outwards reinstatement premiums for the 2018 reported marine and natural catastrophe losses were as follows:

	As at 31 December 2019 \$m	As at 31 December 2018 \$m
2018 loss events <sup>1</sup>	100.6	104.9

1. The 2018 loss events include hurricanes Florence and Michael, typhoons Jebi, Mangkhut and Trami and the California wildfires, plus loss events within our marine portfolio.

Prior year favourable development for 2019 was \$88.0 million, compared to \$126.9 million of favourable development for the same period in 2018. The favourable development in both periods was primarily due to general IBNR releases across most lines of business due to a lack of reported claims. In 2019, the Group also benefited from favourable development on the 2017 catastrophe loss events partially offset by 2018 accident year claims in the energy and Lancashire Syndicates' segments. In the prior period, the Group benefited from a reduction on prior accident year property and energy claims.

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

	2019 \$m	2018 \$m	2017 \$m	2016 \$m	2015 \$m
Property	37.3	46.5	14.4	36.6	26.4
Energy	20.2	55.0	21.1	17.3	35.2
Marine	11.1	12.1	15.2	1.9	13.8
Aviation	1.1	1.4	3.0	3.9	2.9
Lancashire Syndicates	18.3	11.9	11.4	26.1	29.4
<b>Total</b>	<b>88.0</b>	<b>126.9</b>	<b>65.1</b>	<b>85.8</b>	<b>107.7</b>

Note: Positive numbers denote favourable development.



Excluding the impact of foreign exchange revaluations, previous accident years' ultimate losses developed as follows during 2019 and 2018:

### Ultimate loss development by accident year

	2019 \$m	2018 \$m
2009 accident year and prior	3.3	27.0
2010 accident year	(0.9)	1.6
2011 accident year	1.4	4.7
2012 accident year	6.6	8.8
2013 accident year	4.2	3.5
2014 accident year	(1.3)	3.4
2015 accident year	5.7	6.6
2016 accident year	19.3	33.3
2017 accident year	30.8	38.0
2018 accident year	18.9	–
<b>Total</b>	<b>88.0</b>	<b>126.9</b>

Note: Positive numbers denote favourable development.

The ratio of IBNR to total net loss reserves was 30.9% as at 31 December 2019 compared to 39.3% as at 31 December 2018.

### Accident year loss ratios

	2019 %	2018 %	2017 %	2016 %	2015 %
Current accident year loss ratio	51.3	65.6	77.6	32.5	30.2
Initial accident year loss ratio	n/a	70.0	94.2	46.2	46.0
Change in loss ratio post-accident year	n/a	4.4	16.6	13.7	15.8

Note: Adjusted for revaluation of foreign currencies at the exchange rate as at 31 December 2019.

### Other operating expenses

Other operating expenses were \$106.0 million in 2019 compared to \$89.2 million in the same period last year. The increase was driven primarily by the underlying performance of the Group which has resulted in a higher variable compensation element of employee remuneration costs compared to 2018. Employment costs have also increased due to general salary increases. This was only partially offset by the impact of the depreciation in Sterling relative to the prior period.

The equity-based compensation expense was \$9.6 million in 2019 compared to \$7.9 million in the same period last year. The equity-based compensation charge was driven by anticipated vesting levels of active awards based on current performance expectations. Lower equity-based compensation charges were recorded in 2018 as required return thresholds for performance award vesting were not met.

### Third-party capital management

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

	2019 \$m	2018 \$m
LCM underwriting fees	7.9	6.6
LCM profit commission	1.0	–
LSL fees & profit commission	2.5	5.8
<b>Total other income</b>	<b>11.4</b>	<b>12.4</b>
Share of profit (loss) of associate	5.9	(7.1)
<b>Total third-party capital management income</b>	<b>17.3</b>	<b>5.3</b>

The LCM profit commission is driven by the timing of loss experience, settlement of claims and collateral release and therefore varies year on year. Following the significant catastrophe loss activity during 2017 and 2018, and the resulting loss experience, there was no profit commission for any of the 2017 or 2018 underwriting cycles.

The higher underwriting fees in 2019 reflect the increased level of premiums under management compared to 2018.

The LSL fees and profit commission were driven by the relative profitability of the underwriting years impacting the profit commission in each period.

The share of profit (loss) of associate reflects Lancashire's 10% equity interest in the LCM managed vehicle.

**Denise O'Donoghue**  
Group Chief Investment Officer



## 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 the first half of 2019, our focus was on managing our interest rate risk, and as such we continued to hold short duration high quality assets. With the Federal Reserve's pivot in June, interest rates declined, however with the very flat yield curve, we did not see a large benefit from increasing duration much. 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 diversify from interest rate volatility.

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 and core plus portfolios contain 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 and core plus portfolios may be held in any of the three categories, which are discussed further on page 127.

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 \$37.7 million for the year ended 31 December 2019, an increase of 8.6% compared to 2018. Total investment return, including net investment income, net realised gains and losses, impairments and net change in unrealised gains and losses, was \$83.2 million for the year ended 31 December 2019 compared to \$12.5 million for 2018.

The Group's investment portfolio generated a strong total return of 4.9% in 2019 with positive returns from all asset classes, driven primarily by the three 25 basis point rate cuts by the Federal Reserve. Credit spreads also tightened during the year. This was in contrast to 2018 which saw an increase in treasury yields and the widening of credit spreads, resulting in an annual return of 0.8%.

## Managed investment portfolio allocations

	2019 %	2018 %	2017 %	2016 %	2015 %
Cash	11.4	4.8	10.2	10.4	9.6
Short-term investments	4.9	12.9	6.0	0.3	1.1
Fixed maturity funds	0.7	0.7	1.7	0.8	0.6
Government debt	12.7	14.4	17.0	20.3	23.6
Agency debt	3.5	5.1	3.8	4.4	0.2
Agency MBS, CMBS	5.8	4.9	7.7	6.4	7.3
Non-agency RMBS, ABS, CMBS	8.2	8.6	8.5	7.3	8.4
Corporate bonds	34.4	29.9	28.2	32.5	33.2
Bank loans	5.9	6.3	5.8	6.6	5.9
Fixed maturity – at FVTPL	2.9	2.6	1.4	2.8	1.3
Equity securities	–	1.3	1.3	1.2	0.8
Private debt fund – at FVTPL	0.9	–	–	–	–
Hedge funds – at FVTPL	8.7	8.5	8.4	7.0	8.0
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>

## 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 yield 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 other returns from its associates, 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 (including LCM), the distribution of dividends and the repurchasing of shares.

## 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 generate a superior risk-adjusted return over time. With our focus on maximising risk-adjusted shareholder return over the long-term we will return capital where this offers the best returns for our shareholders. We have returned 105.0% 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 2019, total capital available to the Group was \$1.517 billion, comprising shareholders' equity of \$1.193 billion and \$323.5 million of long-term debt. Tangible capital was \$1.363 billion. Leverage was 21.3% on total capital and 23.7% on total tangible capital. Total capital and total tangible capital as at 31 December 2018 were \$1.391 billion and \$1.238 billion respectively.

## Dividends

During 2019, the Lancashire Board declared a final dividend of \$0.10 per common share in respect of the 2018 financial year and an interim dividend of \$0.05 per common share in respect of 2019. The Board of Directors has declared a final dividend for 2019 of \$0.10 per common share, subject to a shareholder vote of approval at the AGM to be held on 29 April 2020. On the basis that the final dividend of \$0.10 per common share is approved by the shareholders at the 2020 AGM the total capital returns since inception amount to \$2.8 billion or 288% of initial capital raised. The final dividend will be paid on 5 June 2020 to shareholders of record on 11 May 2020.

## 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% 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 which it underwrites. The Board proposes to put a similar request for authority to shareholders in a resolution at the 2020 AGM to be held on 29 April 2020.

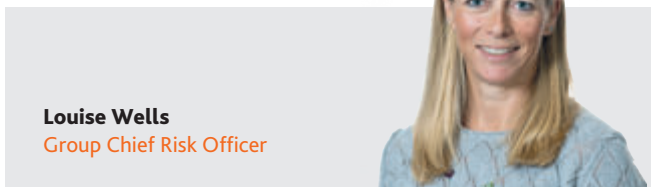
## Letters of credit

Lancashire has a 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 a catastrophe facility in place to assist in paying claims and the gross funding of catastrophes. Up to \$80.0 million can be utilised by way of an LOC or a RCF to assist Syndicate 2010's gross funding requirements. With effect from 1 January 2020, while up to \$80.0 million in aggregate can be utilised by way of an LOC or an RCF to assist Syndicate 2010's gross funding requirements, only \$40.0 million of this amount can be utilised by way of an RCF. Furthermore, a \$44.0 million uncollateralised facility is available for utilisation by LICL and guaranteed by LHL for FAL purposes.

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



# Continuous and consistent risk management



As a short-tail, specialty (re)insurer risk management is key to our success; balancing the risk we take on with the return we receive for that risk is critical. Understanding the risk and seeing the opportunity enables us to deliver for our clients; additionally, balancing the risk and managing our volatility enables us to maximise the return to our shareholders over the cycle. As a result, ensuring we have continuous and consistent risk management embedded across the Group through the Risk Management Framework is a key focus.

## 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 regular 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's financial performance is exposed to risks from several sources. These include insurance risk, strategic risk, market risk, liquidity risk, credit risk, operational risk, group risk and regulatory and legal risk. The primary risk to the Group is insurance risk, which can be subdivided into the core risk of underwriting and the non-core risk of reserving and includes the Group's risk exposures to natural catastrophes including wind storms, wildfires and other loss events linked to climate change trends.

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 returns 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 modelled 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 assesses our modelled potential losses against risk tolerances to ensure that risk levels are managed in accordance with them.

## Risk Management 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 the controls that mitigate against these risks are consistent with their day-to-day processes and the entries made in the respective 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. LSL's CRO provides formal reports to the LSL Board and its RCCC. The third

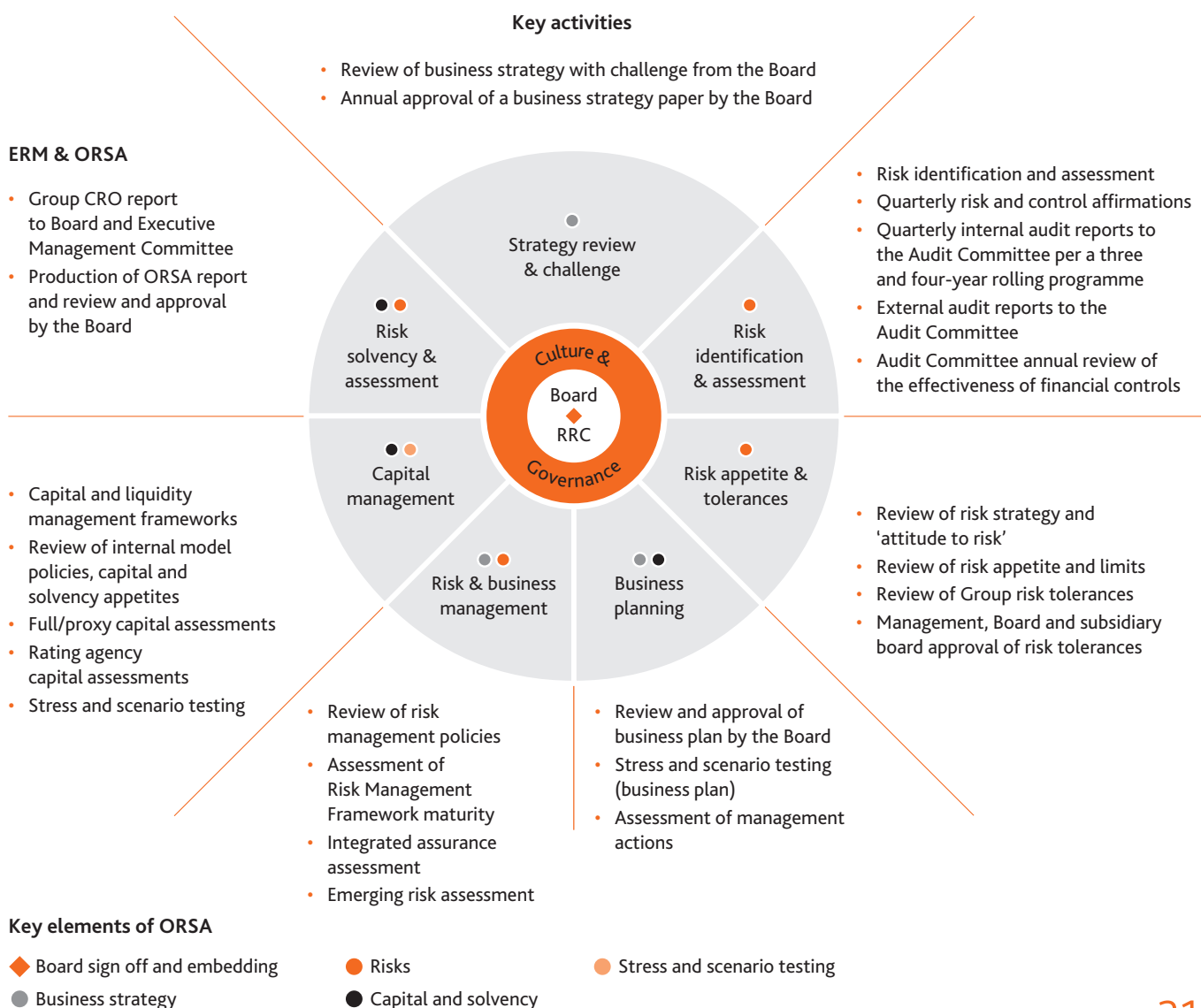
line of defence is the internal audit function, which works closely with the risk management team in providing risk assurance by assessing the operating effectiveness of the controls and the culture.

We continue to perform a quarterly risk and control 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 that their risks remain appropriately documented and scored. The risks are scored on both a gross basis (i.e. inherent risk pre-controls) and a net basis (i.e. residual risk post the application of controls). The output from this process is reported to the RRC and the Group and operating subsidiary audit and risk committees or boards of directors as appropriate.

As at 31 December 2019, all Group entities were operating within their board-approved risk tolerances.

The quarterly ORSA reports prepared by the Group CRO to the main Board provide a timely analysis of current and potential or emerging

## ERM & ORSA



risks, compared against risk tolerances, along with their associated capital requirements.

Our annual ORSA report is now prepared under the requirements of the BMA's regulatory regime which has been recognised as being Solvency II equivalent. The 2020 ORSA will be presented to the Board for review, challenge and approval at the Q1 2020 Board meeting.

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

The diagram on the previous page 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. Culture is also driven from the 'bottom up' through the risk and control affirmation process. The primary role of the Group CRO is to facilitate the effective operation of ERM and the ORSA processes 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; and
- 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 regular basis. It seeks to optimise risk-adjusted returns and facilitate the appropriate use of the Group's internal models, including considering their 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 coordinating 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, modelling, operations, treasury and underwriting functions and both the Group CRO and LSL CRO. The Group CRO reports on the RRC's activities to the Group and individual entity boards of directors and via the LSL CRO to the RCCC of LSL. Through the Group CRO the RRC considers recommendations to the Board and its Committees with regard to the adoption of formal risk tolerances.

Examples of specific items considered by the RRC during 2019 include: the Group strategy and business plan, risk appetite statements, capital and solvency appetite, ERM framework, stress and scenario tests (including the addition of a climate change scenario covering

transitional and physical risk factors) and the results of the quarterly affirmation process and related controls testing.

## Capital models

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

## Changes in risk

From an insurance risk perspective, the business has written just over 10% more Gross Written Premium (GWP) than in 2018. This increase reflects an increased appetite to write business as we have seen improving rates across most of our classes of business and increases in business in downstream energy, power and aviation deductible following recruitment of new underwriting teams in these areas in 2018. In addition, as is the case every year, our underwriters have reviewed and refined our purchasing of reinsurance cover. This is designed to ensure our reinsurance buying is aligned to our latest strategy and is targeted to be as responsive as possible, thereby helping to reduce net insurance risk exposures or enabling additional risk taking.

From an operational risk perspective, there have also been a number of important risk and control changes during the year, for example the change of regulatory and tax domicile of the Group from the UK to Bermuda in January 2019. Following this change, the business has documented related controls to help ensure that there is a good understanding of how and where key decisions are to be taken in order to mitigate associated corporate governance and tax risks arising from this change.

## 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 executive committees, 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 2019 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. Much of the focus in 2019 was on the continued development of previously reported emerging risks including Brexit, climate change risks (physical, financial, transitional and liability), global tax reform and geopolitical instability. Climate change risk has risen to the top of many political agendas internationally over the last year and has remained an area of risk monitoring and management for us at both management and Board level. The threat which catastrophic weather events poses to individuals, communities and businesses illustrates the social and economic value which our risk management products generate. This is therefore a key area both of strategic opportunity for our business and one of the key drivers of our underwriting risk exposure management. In particular, management and the Board set tolerances for, and monitor, the Group's probable maximum losses for major catastrophe events and in particular weather-related exposures. Please see page 120 for a list of the Group's current PML risk exposures. Climate change risk also informs the way we manage our investment portfolio and associated risk. During 2019, the Group once again participated in the Carbon Disclosure Project, which is aligned with the recommendations of the Task Force on Climate-

related Financial Disclosures, which are promoted by the Financial Stability Board and the Bank of England.

## 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 (represents the potential to generate a return as well as a loss) or non-core (offers no direct potential for return); (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 99.

## 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 modelling 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.
	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 on page 33, 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 119 to 142. Within the capital models, insurance risk accounts for over 80% 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. In addition, the Group continues to consider and adapt to the risks and opportunities arising from climate change through the analysis of the associated physical, transitional and liability risks. As part of our overall risk mitigation strategy we perform detailed stress and scenario testing to stress the financial stability of the Group. This process is aligned to our business planning, ORSA processes and time horizons. The selected tests are aligned to our key risk areas and include capital (rating agency and regulatory), underwriting and investment-related stress tests, at a minimum.




Type	Mitigation
<b>Intrinsic risk: Core</b>	
<p><b>Underwriting:</b> 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. We recognise that through climate change trends, and other influencing factors, weather-related incidences or other actual catastrophe loss events may increase losses in frequency, severity and clustering 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.</p>	<p><b>Modelling:</b> We apply loads to, and stress test, stochastic models and develop alternative views of losses using exposure damage ratios. We review our assumptions periodically to ensure they remain appropriate. We also back test our portfolio against historic events to assess potential losses.</p> <p><b>RRC:</b> The RRC considers accumulations, clashes and parameterisation of losses and models.</p> <p><b>Governance: Board and capital management:</b> We set our internal capital requirements at a level that allows for buffers above accumulations of extreme events and, further to recommendations, the Board approves risk tolerances at least annually and considers capital requirements on at least a quarterly basis.</p> <p><b>Reinsurance:</b> We buy reinsurance to manage our exposure and protect our balance sheet. The structure of our programme was reviewed for 2020 to ensure it remained aligned to our strategy and risk profile.</p>






#### Risk trend key:




Increased	
Stable	
Decreased	

#### Risk impact key:









High	
Moderate	
Low	

#### Risk appetite key:

Acceptable	
Reassess	
Unacceptable	

Trend	Impact	Appetite	Link to strategy	Opportunities	How the Board reviews this risk
			<b>Underwriting comes first</b>	As market dynamics change so too do the opportunities available to the Group. We remain creative in being able to provide tailored insurance and reinsurance products and solutions to our core clients across the three platforms of our business. 2019 saw some opportunity for organic growth and there are signs that 2020 will provide further opportunities.	Unsurprisingly, the Board views underwriting as the Group's key risk. As such, the Board continues to focus on underwriting expertise and discipline to effectively balance the equation of risk and return, and operate nimbly through the cycle. The Board is actively engaged in the development and implementation of the Group's underwriting strategy, plus the articulation of, and adherence to, formal underwriting risk tolerances. Quarterly risk data on this is both received and reviewed by the Board's Underwriting and Underwriting Risk Committee (UURC) to ensure that good risk selection and disciplined underwriting remain at the core of the Group's underwriting strategy. The UURC and Board also review and approve the structure of the Group's outwards reinsurance programme.

Type	Mitigation
<b>Intrinsic risk: Core (continued)</b>	
<p><b>Investment:</b> 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 an interest rate risk as a result of Federal Reserve policy, such as the pivot in the Federal Reserve's outlook in June 2019. We model our investment portfolios and use various stress scenarios to see what kinds of losses we could expect under a range of outcomes. The Investment Committee adopts a strategy which has a low exposure to the effects of climate change transitional risk over the various asset classes.</p>	<p><b>Governance: Board and investment strategy:</b> 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. A detailed strategic asset allocation study is performed biannually.</p> <p><b>IRRC:</b> The IRRC forms an integral part of our risk management framework, meeting at least quarterly and reporting to the RRC.</p> <p><b>External advisers:</b> 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. The Group's principal investment managers are signatories to the Principles for Responsible Investment.</p>
<b>Intrinsic risk: Non-core</b>	
<p><b>Reserving:</b> 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 reserve reviews by external actuaries 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.</p>	<p><b>Short-tail business:</b> 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.</p> <p><b>Experience data:</b> 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.</p> <p><b>Governance:</b> Reserves are reviewed and approved by the Reserve Committee whose members include representation from finance, actuarial and claims; there are additional attendees from finance, actuarial, underwriting, legal and risk. A reserve report is presented and reviewed on a quarterly basis by the Audit Committee.</p> <p><b>External review:</b> Insurers typically facilitate an independent review by external actuaries 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 receives and considers quarterly reports from management and the Group Chief Actuary. In addition, the Audit Committee receives and considers reports on reserve adequacy from the external actuary six monthly.</p>
<p><b>(Re)Insurance and intermediary counterparty:</b> 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.</p>	<p><b>Counterparty credit limits:</b> 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.</p>

Trend	Impact	Appetite	Link to strategy	Opportunities	How the Board reviews this risk
			<b>Effectively balance risk and return</b>	The primary objectives for our investment portfolio remain capital preservation and liquidity. Our conservative approach limits our downside risk but means we are unlikely to equal the returns of peers taking on more investment risk.	The Investment Committee receives and reviews investment strategies, guidelines and policies, risk appetite and associated risk tolerances, and makes recommendations to the Board in this regard. The Committee also monitors performance of the investment strategies within the risk framework and compliance with investment operating guidelines. In addition, the quarterly ORSA report from the Group CRO includes statements regarding performance against investment risk tolerances.
			<b>Effectively balance risk and return</b>	Whilst our focus is on short-tail lines of business uncertainty still exists on the eventual ultimate losses as loss information can take some time to obtain. As additional information emerges, the Group's actual ultimate loss may vary, perhaps materially, from those initially reported. This may result in reserve releases or a required strengthening of reserves.	The Board reviews this risk in detail on a six-monthly basis through the Audit Committee, which focuses on the appropriateness of the overall reserve levels, informed by the external actuary's independent review of reserve adequacy and the UURC, which receives updates from management on individual large losses.
			<b>Underwriting comes first and Effectively balance risk and return</b>	As both a purchaser and seller of reinsurance, opportunities exist throughout the insurance cycle. In recent years, with rates suppressed, the quantum of reinsurance coverage purchased has increased and therefore so has counterparty exposure. This is mitigated through established governance processes to manage the aggregate exposure and credit control processes to ensure monies due are received. As always, it is the case of balancing the risk we are taking with the expected return; reinsurance purchasing is one way of balancing this.	The quarterly ORSA report to the Board includes the top five reinsurance counterparty exposures versus the Board-agreed tolerances. These tolerances are reviewed and approved on an annual basis by the Board and considered as part of the annual strategy review. Amounts owed to intermediary counterparties are included in the underwriting information provided to the UURC on a quarterly basis.

Type

Mitigation

## Intrinsic risk: Non-core (continued)

**Liquidity:** In order to satisfy claims payments we need to ensure that sufficient assets are held in a readily realisable form. This includes holding liquid assets for the modelled payout of loss reserves, as well as ensuring that we can meet claims payments in relatively extreme events.

**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

These are risks arising as a result of inadequate or failed internal processes, personnel, systems or (non-insurance) external events. The Group is also subject to regulatory supervision and oversight, as well as legislation and tax requirements across a number of jurisdictions (see page 46 for more information). Operational risks 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. Furthermore, unauthorised access to IT systems as a result of a breach or failure could result in data loss, including personal data, which may have regulatory and/or reputational risk implications.

**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. Additionally, the Group has both Disaster Recovery and Business Continuity Plans in place that are tested annually and which are designed, in particular, to help minimise the risk posed by Bermuda hurricane events or disruptive political or terrorism events in London. The business follows strict tax and regulatory operating guidelines, which are periodically reviewed and approved by the Board.










**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. In addition, the Group has core values, which all employees subscribe to and which reflect the culture described in our recent staff engagement survey. The Board regularly reviews succession planning arrangements and remuneration structures. Although the Group holds limited personal data, it has a suite of policies and processes, including penetration testing procedures, around data protection which facilitate compliance with the EU General Data Protection Regulation (GDPR) and the Bermuda equivalent of the GDPR, the Personal Information Protection Act (PIPA).

## Other – Brexit and climate change

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, regulatory and emerging risks. Brexit has been a continued focus of the Group during 2019. With the UK having left the EU at the end of January 2020, our focus for 2020 will be on monitoring what the UK's ongoing trading relationship with the EU will be at the end of the transition period (currently due to end on 31 December 2020), in particular on the financial services industry. We maintain our view that the impact of Brexit is not a significant risk to the Group given our trading profile and the solutions that have been put in place. Whilst we view climate change as a factor relevant principally to our underwriting and investment risks (see above), the Board and business continue to monitor the effects of climate change risk perceptions as a driver of global economic, political and regulatory change.

**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 quarterly ORSA reports made by the Group CRO to the Board include standing items on these risk areas. Brexit updates were included throughout the year.

Trend	Impact	Appetite	Link to strategy	Opportunities	How the Board reviews this risk
			<b>Effectively balance risk and return</b>	As previously noted, liquidity is a primary objective of our investment portfolio. It is important we balance the need for liquidity and being able to pay our clients' claims on a timely basis with the opportunity for return from our investments. We do this through different investment portfolio categories.	Liquidity risk is reviewed by the Investment Committee which regularly receives and reviews reports detailing asset allocation and compliance with pre-defined guidelines and tolerances.
			<b>Operate nimbly through the cycle and Effectively balance risk and return</b>	A risk-based approach is followed to determine which areas require strongly controlled processes and procedures (i.e. the key risk areas) and those areas where a more proportionate approach is appropriate (those areas assessed as low risk).	The Audit Committee receives quarterly reports from the Group CRO summarising the results from the quarterly risk and control affirmation process. The Audit Committee reviews this alongside the quarterly updates from internal audit regarding their programme of work and opinion on the effectiveness of controls. In addition, the quarterly ORSA report from the Group CRO to the Board includes details of any operational loss events and changes to the risk register and the drivers for such change. The focus on operational resilience and culture has increased in 2019, with the Audit Committee receiving an internal audit report on IT strategy and the Board receiving the results of the staff engagement survey.
			<b>Effectively balance risk and return</b>	<p>Brexit and climate change risk factors are examples of other risks the Group considers and monitors.</p> <p>As reported last year, to mitigate the impact of Brexit, the Group considers that a significant proportion of LUK's existing EU27 business could be written via Lloyd's Brussels, utilising LSL, which has Lloyd's approval for this arrangement, subject to ongoing approval from Lloyd's and any additional approvals required in relation to the operation of Lloyd's Brussels.</p> <p>Climate change, as Alex Maloney discussed in his report on page 13, and the trend of increased frequency and severity of weather-related loss events illustrate the value of our insurance and reinsurance products to our clients. Whilst we already insure many clients in the renewable energy sector, as the world transitions to non-carbon forms of energy the opportunities within this sector will grow.</p>	As Peter Clarke and Alex Maloney noted in their introductory statements (see page 9 and page 13), climate change is increasingly a topic of debate at the Board and its various Committee meetings. In addition, the stress and scenario testing performed as part of the annual business planning process and regulatory reporting process includes a climate change related scenario looking at both transitional and physical risks, and the Board concluded that the results of this scenario testing did not represent a material risk to the Group.



# Delivering our purpose

We are committed to engaging with our people, our stakeholders and society, and creating a healthy and sustainable corporate culture.

## The Board and Section 172 responsibilities

At the beginning of 2019, the 2018 UK Corporate Governance Code introduced more formal requirements around the interests of and engagement with stakeholders, and the duties falling upon boards under Section 172 of the UK Companies Act 2006. Although the Company is incorporated in Bermuda and therefore not subject to the UK Companies Act requirements, the Board continues to pay close attention to developments in English law and governance best practice.

In this 2019 Annual Report and Accounts, we give an overview of how both the Board and the business have factored in the needs of its stakeholders in their discussions and decision making. To that end, this engagement and sustainability segment should be considered together with the rest of this report as the Company's comprehensive account of its Directors' compliance with their Section 172 duties. The table below directs readers to some illustrative examples of where the Board and business have addressed these duties:



Section 172(1): Duty to promote the success of the company, with regard to:	For further details, see:
a) The likely consequences of any decision in <b>the long term</b> ;	<ul style="list-style-type: none"> <li>The Group's statement of purpose – inside cover</li> <li>The Group's business model for success – pages 10 to 11</li> <li>The Group's strategic goal and three priorities: that underwriting comes first; to effectively balance risk and return; and to operate nimbly through the cycle – pages 14 to 15</li> </ul>
b) The interests of the company's <b>employees</b> ;	<ul style="list-style-type: none"> <li>The importance of our people, and the business's focus on Lancashire's values, culture, diversity &amp; inclusion, training &amp; development and workforce engagement (for example, our 'Engagement in action') – pages 41 to 43 and 74 to 76</li> </ul>
c) The need to foster the company's <b>business relationships with suppliers, customers and others</b> ;	<ul style="list-style-type: none"> <li>Our business depends upon the strong business relationships that we build and maintain with our core and broader stakeholders. All Board members attend the quarterly Underwriting and Underwriting Risk Committee and, during 2019, gave close consideration to business development opportunities as summarised in the Committee's report – pages 43 and 70 to 71</li> </ul>
d) The impact of the company's operations on the <b>community and the environment</b> ;	<ul style="list-style-type: none"> <li>Society and the environment form part of our 'core' set of stakeholders. The Board is engaged with the impact of the Company's operations through its oversight of the Lancashire Foundation, the Group's submission to the Carbon Disclosure Project, the annual offsetting of our GHG emissions, and more recently the commitment to report against the UNEP FI Principles for Sustainable Insurance – pages 44 to 45 and 52 to 54</li> </ul>
e) The desirability of the company maintaining a reputation for <b>high standards of business conduct</b> ; and	<ul style="list-style-type: none"> <li>Through its compliance with the FRC's UK Corporate Governance Code, the Company strives to operate in line with high standards of governance expectation and business conduct. A healthy and sustainable corporate culture is embedded throughout the business, which is assessed by the Board through various channels – pages 40 to 47, 48 to 49 and 64 to 67</li> <li>The Audit Committee oversees the Group's implementation of whistleblowing arrangements, and other systems and controls for the prevention of fraud, bribery and money laundering – page 62</li> </ul>
f) The need to act fairly as between <b>members of the company</b> .	<ul style="list-style-type: none"> <li>The Board is committed to treating the Company's shareholders fairly, and engaging with them through a broad programme of investor relation activities, meetings (including the AGM), and targeted consultations; be that with our substantial shareholders, the Company's own employees, private individuals, or via shareholder advisory groups – pages 28 to 29, 40 to 47 and 76</li> <li>Capital management/actions and dividend policy – in particular, the Board's consideration of the balance between underwriting opportunities and the payment of special dividends – pages 8 to 9, 29 and 96</li> </ul>

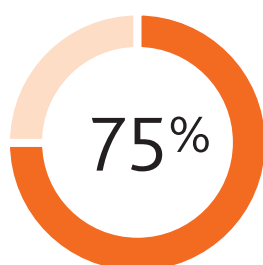
## Our approach to stakeholder engagement

The Group has always positively engaged with a broad range of stakeholders. Our 'core' stakeholders are shown at the heart of the diagram, namely our shareholders and our people (who support our business), as well as our policyholders who rely on the (re)insurance products we sell. Through our purpose as a business we aim to benefit society and the environment. The value of these relationships and the responsibilities they entail are recognised throughout the Group, ranging from Board-level decision making through to the day-to-day business activities of our workforce.

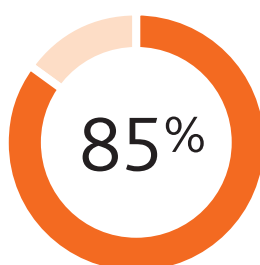
The Group's relationship with its broader stakeholders can, of course, at any one time also be of key importance. The Board and the business prioritise underwriting excellence and nimble capital management to serve the best interests of core stakeholders, and ultimately benefit a broader group of stakeholders. It is the fluidity of these relationships which enables the business to deliver on its purpose and strategy.

### Key findings and feedback:

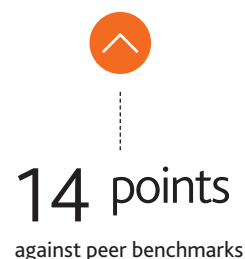
#### Employee participation



#### Employees responding positively as engaged with the business



#### Versus benchmark



#### Employee Engagement



#### Company Alignment



#### Leadership



#### My Manager



#### My Colleagues



#### Empowerment



#### Personal Growth



#### Recognition



#### Wellbeing



#### Satisfaction



## Engagement in action:

### The 'Lancashire values' working group

During 2019, a small working group of employee volunteers was assigned the task of devising a new set of 'Lancashire values', based on what they consider to be representative of the business's culture. The values form part of the year-end employee appraisal process and reflect a standard of conduct expected from everyone working within the Group. Following a series of constructive meetings, the working group settled upon the following new values, which were approved by the Group Executive and will be rolled out to the business during 2020:

- **Leadership**, exhibiting passion and commitment in all aspects of Lancashire life and inspiring others to do the same, we are...
- **Aspirational**, aspiring to deliver a superior service for our clients, ourselves and our business partners, we are...
- **Nimble** in our decisions, actions and business processes, we are...
- **Collaborative**, valuing teamwork and a diversity of skills and experience and sharing in our success, and we are...
- **Straightforward** in conducting our business in an accountable, open, honest and sustainable way.

## Our people

### Culture

Our employees are the lifeblood of the organisation and the Group therefore strives to attract and retain excellent individuals who share our drive and appetite to outperform. Matching the skills, aspirations and values of new recruits to those of the business remains a key priority. We believe the talents of our people and our distinctive culture continue to set us apart from our competitors.

Lancashire offers a rewarding environment within which to work, both in terms of the support and opportunities given to employees to enable them to excel in their role and the competitive and attractive compensation and reward structures. To further enhance the link between our people and the performance of the business, all of our permanent employees are eligible to receive RSS awards, therefore giving them the opportunity to share in the growth and success of the Group and ultimately to become shareholders.

### Diversity and inclusion

The Group promotes an inclusive, collegiate and positive environment that recognises and values diversity as key to enhancing individual development and maximising business effectiveness (see in this regard the Nomination and Corporate Governance Committee report on pages 64 to 67). As an equal opportunities employer, we do not tolerate discrimination of any kind in any aspect of employment. For example, all decisions relating to recruitment, assessment and promotion are based on the ability of the individual 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. Our workforce is represented by employees from 12 different nations and the gender split of males to females (see page 67) is 61.5%/38.5% respectively. The Group is also committed to providing a working environment that is free from any form of bullying or harassment.

We expect our staff to conduct themselves in a professional manner which is reflective of the Group's core values (see page 41 for further details). All new employees are required to attend our Communications Etiquette/Equality, Diversity & Inclusion training sessions as part of their induction. The training sessions aim to highlight employees' responsibilities in ensuring that there is no

discrimination in the workplace and in fostering a positive and productive working environment.

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

### Training and development

The Group encourages continuous personal and professional development for all of its employees, through internal and external training, professional qualifications, internships and secondments, performance coaching, and 'lunch and learn' sessions. During 2019, approximately 69.3% of our employees undertook some form of training supported by the Group. As ever, we encourage all our employees to take advantage of the training opportunities offered. Individual training and personal development needs are discussed on a regular and ongoing basis by managers and their team members, and are assessed as part of the formal appraisal process, where principally each employee's success is measured through the attainment of personal performance metrics as well as performance within the Group's values framework. We can confirm that during 2019 9.2% of our employees were promoted within the Group, supported by the training and development opportunities afforded to them.

The Group also delivers compulsory training to all new permanent staff and fixed-term contract staff which covers a range of important topics, including: Tax/Regulatory Operating Guidelines, Disclosure (including the requirements of the Market Abuse Regulation 2016), Inspections, Financial Crime, ERM, Communications Etiquette/Equality, Diversity & Inclusion, GDPR and Conduct Rules. Other training may be held on an ad hoc, one-off or refresher basis according to an individual's requirements. 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 role and responsibilities within the business. There is an expectation that all new staff members will have completed their compulsory training during the first six months of joining the business. Quarterly updates regarding attendance at these compulsory training sessions are provided to the Board for information purposes.

	2019*	2018*
Number of employees (UK and Bermuda)	➡ 218	218
Percentage of female employees	⬇ 38.5%	39.0%
Percentage of women on the LHL Board	⬆ 37.5%	28.6%
Percentage of women on the Group executive committee	⬆ 50.0%	37.5%
Percentage of women in senior management positions	⬆ 38.1%	29.4%
Number of different nations represented by our employees	⬇ 12	13
Percentage of the workforce composed of third-party contractors	⬆ 8.0%	6.9%
Group employee turnover (annual)	➡ 13.8%	13.8%
Percentage of employees who undertook training during the year	⬆ 69.3%	65.6%
Percentage of permanent employees eligible for RSS awards	➡ 100.0%	100.0%
Accredited London Living Wage employer	➡ Yes	Yes

\* Unless otherwise stated above all figures are as at 31 December.

**"The Group promotes an inclusive, collegiate and positive environment that recognises and values diversity as key to enhancing individual development and maximising business effectiveness."**

**Number of employees**

**218**

**Percentage of women on the Group executive committee**

**50.0%**

### Engagement

The Group benefits from having a relatively small headcount, 218 employees globally, which allows its staff members to interact easily between departments and to access members of the senior management team, including the CEOs at both Group and subsidiary level. Lancashire also encourages a high level of engagement between its workforce and the Board. There are regular opportunities for each of the Directors and staff members to interact at all levels across the organisation in a particular year, and such engagement is encouraged both at the level of the Group's subsidiary boards and the main Board of the Company. This occurs at board dinners (to which UK and Bermuda staff members are routinely invited), interaction with senior employees as part of quarterly activities, semi-formal lunches, 'town hall' quarterly update meetings, periodic attendance at the daily underwriting call and annual attendance at the AGM. Furthermore, both Simon Fraser and Samantha Hoe-Richardson are Non-Executive Directors on the subsidiary boards of LSL and LUK, respectively, and in that capacity each has the opportunity to meet and engage with a range of staff members within those businesses. Please see page 49 of the Chairman's introduction for an account of the Board's engagement with the workforce in 2019 and its plans for 2020.

Our new programme of employee engagement surveys (as conducted in 2019) gives our staff members the opportunity to provide their feedback to peers, senior management, departmental heads and the Board on their experience working for the Lancashire Group. For a fuller account, see our 'Engagement in action' section on page 41.

Our employees also continue to contribute towards the development of our marketplace through their involvement with market committees, boards and working groups. During 2019, our employees actively participated in industry conferences, investor days and symposia, and market education programmes. We also donate to many of the causes supported by our industry partners through the Lancashire Foundation.

### Our policyholders

Policyholders are central to our business, so understanding and serving their commercial requirements is at the forefront of everything we do. Through our range of underwriting platforms, we strive to offer clear, fairly-priced and useful products that continue to meet our policyholders' insurance and reinsurance needs across the cycle. In the event of a loss occurring, we remain responsive in order to provide our policyholders with ongoing support and seek to pay their claims as expeditiously as possible, knowing the importance of providing an excellent service. We place the highest value on the relationships we have built over the years with our existing policyholders and work hard at creating a lasting impression with new ones. To this end, we are happy to welcome both our policyholders and their brokers to our offices, but we also travel to see them and their businesses around the world.

A more detailed account of the work we do in meeting the needs of our policyholders can be found in the underwriting review and business review sections of this Annual Report and Accounts on pages 20 to 23 and pages 24 to 29, respectively.

### Brokers

We are fully committed to supporting a 'broker market' and to maintaining a strong working relationship with the largest global broking firms, as well as independent brokers. The Group depends on brokers to distribute its products and actively assesses these relationships to ensure that it continues to be viewed as a trusted partner and provider of solutions for their clients' (re)insurance needs.

## Our shareholders

As a premium-listed company on the LSE, Lancashire understands the importance of its obligations to shareholders. We work hard to foster good investor relations and pride ourselves on having an active programme of engagement with our diverse shareholder community around the world.

Lancashire values the views of all of its shareholders and maintains open and transparent communication channels with them and certain of the leading shareholder advisory services. This is led by our Group Head of Investor Relations, in collaboration with members of the Board and the executive team, and is achieved through a structured programme of meetings, presentations and periodic consultation initiatives (with both shareholders and industry analysts). These can cover a range of topics including the Group's financial performance and business strategy; ESG matters; and the executive remuneration policy.

The Board meets regularly with the Group's corporate brokers to seek their feedback on investor priorities as well as Lancashire's performance and perception amongst investors within the broader insurance sector. To learn more about the Board's engagement and relationship with its shareholders, please see page 57 of this Annual Report and Accounts.

## Society and the environment

### Environmental impact and offsetting

The Group is committed to managing the environmental impact of its business. We continue to measure our carbon footprint with a view to minimising its negative impact through mitigation strategies and by offsetting 100% of our greenhouse gas (GHG) emissions, as reported in the table below, to remain carbon neutral. The Group also recognises the challenges posed by climate change and considers its impact as part of the risk management and strategic planning process (please refer to the Group CEO's review on page 13 and the section on principal risks from pages 33 to 39 for further details). The Group CRO and the Board oversee the Company's annual submission to the Carbon Disclosure Project. The information which is requested as part of the reporting process is aligned with the recommendations of the Task Force on Climate-related Financial Disclosures.

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.

Emissions are collated over a 12-month period from 1 January 2019 to 31 December 2019 and are calculated by converting consumption data into tonnes of carbon equivalent (tCO<sub>2</sub>e) using the BEIS 2019 factors (note: this annual publication was previously managed by the UK's Department for Environment, Food and Rural Affairs (DEFRA), though is now published by the Department for Business, Energy and Industrial Strategy (BEIS)).

Using an operational control approach, Lancashire has assessed its boundaries to identify all the activities and facilities for which it is responsible. Subsequently, we have reported 100% of our Scope 1 and 2 footprint, along with areas of our Scope 3 footprint with high levels of operational control, as detailed below. Calculations performed follow the ISO 14064-1:2018 standard, giving absolute and intensity factors for the Group's emissions. Lancashire uses the number of full-time employees (FTE) as its intensity metric. Where data was not available for 2019, values have been extrapolated by using available data or calculated using industry benchmarks.

\* The Group's UK operations have been awarded BREEAM excellence for their London offices at 20 Fenchurch Street

Types of Emissions	Activity	2019 tCO <sub>2</sub> e	2018 tCO <sub>2</sub> e
Direct (Scope 1)	Gas ( <i>measured in kWh</i> )	126.9	60.1
	Refrigerant ( <i>measured in kg</i> )	0.0	0.0
Indirect Energy (Scope 2)	Electricity ( <i>measured in kWh</i> )	294.1	319.9
Indirect Other (Scope 3)	Business Travel ( <i>measured in miles and spend</i> )	1,925.9	1,457.2
	Additional Upstream Activities ( <i>measured in kWh, litres, miles and spend</i> )	297.1	246.4
	Water ( <i>measured in m<sup>3</sup></i> )	14.2	12.9
	Waste ( <i>measured in kg</i> )	6.1	3.7
	Paper ( <i>measured in reams</i> )	4.4	5.6
	Hotels ( <i>measured in hotel nights</i> )	26.8	24.0
<b>Gross Emissions (tCO<sub>2</sub>e)</b>		<b>2,695.5</b>	<b>2,129.8</b>
<b>Gross Emissions per FTE (tCO<sub>2</sub>e/FTE)</b>		<b>12.4</b>	<b>9.8</b>
<b>Carbon Credits</b>		<b>2,696</b>	<b>2,130</b>
<b>Total Net Emissions after offset (tCO<sub>2</sub>e)</b>		<b>0.0</b>	<b>0.0</b>

Please note: all numbers quoted have been rounded to one decimal place.

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 and the emissions associated with the electrical energy lost during transmission to our business.



**"Family Centre is an internationally accredited Bermuda registered charity that provides early intervention services to children and families at risk in Bermuda. Our mandate is to strengthen families to create a healthier Bermuda for our children. Family Centre is proud to call Lancashire Foundation a 'Champion of Children'. They have partnered with Family Centre since 2007 and have provided \$1,309,407 in vital funding to sustain the delivery of critical intervention and counselling services to children and families in crisis – free of charge. Thanks to the Lancashire Foundation we have many children and families who have successfully turned their crisis into an opportunity to have a positive outcome and brighter future."**

**Family Centre**

The table on page 44 sets out the Group's carbon footprint for the current and prior reporting period, broken down by emission source.

Total emissions for 2019 have increased by 26.6% compared to 2018. As FTEs have remained constant year on year, emissions per FTE have also increased by 26.6%.

Results show that GHG emissions in the year were 2,695.5 tCO<sub>2</sub>e, comprised of direct emissions (Scope 1) amounting to 126.9 tCO<sub>2</sub>e, and indirect emissions (Scope 2) amounting to 294.1 tCO<sub>2</sub>e. The source of other indirect emissions (Scope 3) comprised 2,274.5 tCO<sub>2</sub>e. Scope 1 emissions have increased by 111.2% due to improving data quality for natural gas. Scope 2 emissions have decreased by 8.1% compared with 2018 due to the continuing decarbonisation of the UK grid mix. Scope 3 emissions have also increased compared with 2018 due, primarily, to increasing air mileage year-on-year. This is in part a result of the Board's decision to re-establish Group regulatory supervision to Bermuda with effect from 1 January 2019. The Board will continue to monitor and offset the Group's emissions, mindful of the Group's strategic and business operational requirements.

The Group has fully offset its 2019 GHG emissions through an organised programme with EcoAct by purchasing credits in the Wind Power Generation project in India. These offsetting proposals were discussed and agreed with the Group CEO.

#### **Communities, including the Lancashire Foundation**

Lancashire is strongly committed to giving back to the communities within which it operates, both locally in the UK and Bermuda and also further afield. The business seeks to help those who are in distress or at a disadvantage, through continued support of local initiatives and activities, volunteering days, mentoring opportunities and fundraising events, to name a few. We utilise the talent and energy of our staff in helping others, positively impacting society and creating a more sustainable environment. In turn, this stimulates a positive culture amongst staff and promotes Lancashire as an ethical and compassionate employer. These goals are primarily achieved through the work of the Lancashire Foundation. Read further on to learn more about the Lancashire Foundation and the charities it supports.

The Group and the Foundation have jointly sponsored an internship programme for Bermuda resident college graduates since 2014. These

graduates are afforded the opportunity to work and learn about insurance in the Group's London office.

The Board keeps itself informed of the activities of the Lancashire Foundation through regular reporting and meetings with the Foundation's Trustees. The Board also sets the policy for donations to the Lancashire Foundation.

#### **The Lancashire Foundation**

The Lancashire Foundation, our charitable grant-making body, is the cornerstone of our community activity and support, and a key component of our corporate persona.

The Foundation is funded by regular donations from the Company and also retains a shareholding in the Company, therefore benefitting from any dividends paid. This creates a direct link between the success of the Company and the resources available to the Foundation, serving as an additional motivation for our people, as the Foundation is able to support more of the causes that are suggested by employees. In this way we have aligned the Foundation to the Lancashire Group and can share in its success, and leverage that success to causes and communities that do not often receive such material rewards.

Major donations, such as those made to MSF, which operates in crisis relief around the world, and ICM, which works with the poorest of the poor in the Philippines, complement Lancashire's own insurance and reinsurance business by seeking to provide support to those afflicted by unexpected events and extreme poverty in areas where there is no insurance to protect people and their property. Our donation to St Giles Trust seeks to break the cycle of reoffending that blights many of our most vulnerable communities.

Other charities supported by the Lancashire Foundation during 2019 include:

- London Air Ambulance
- Cancer Research UK
- Child Bereavement UK
- Kiva Microfunds
- Knowledge Quest
- Medical Detection Dogs
- Mission Aviation Fellowship

- St Giles Trust
- Family Centre
- Tomorrow's Voices
- Victor Scott (Fruit for Schools)
- Warwick Academy
- Windreach Bermuda
- Team-Up
- The Poppy Factory
- Care for Children
- Vauxhall City Farm

## Our broader stakeholders

### Government and regulators

In an industry that is subject to strict regulatory supervision and oversight, we recognise the need to work closely and openly with all relevant regulatory bodies. We place great importance on the relationships we have with our regulators and engage actively with them, whether that is through meetings, reporting or routine regulatory reviews. The Board is also kept apprised of communications with regulators and supervisors and, together with management, monitors changes in regulatory and supervisory requirements closely.

In addition, the Group maintains proactive relationships with relevant tax authorities in order to achieve compliance with all its tax obligations. This requires us to keep abreast of developments in tax legislation and to work with the tax authorities to manage our tax risk.

### Rating agencies

Lancashire maintains a positive relationship with three major rating agencies: A.M. Best, S&P and Moody's. These rating agencies assess and rate the creditworthiness and claims-paying ability of the Group's insurance subsidiaries, LICL and LUK, based upon established criteria. The syndicates benefit from Lloyd's current ratings. We are proud of the ratings which we have been assigned by each of these rating agencies and we engage with them on the following bases: annually, for our rating review; quarterly, to discuss our results for the period; and on an ad hoc basis as events dictate including after significant industry loss events or a series of loss events. These ratings allow the Group to write business successfully in all major global insurance markets and to comply with reinsurance contracts under which the Group is reinsured, as well as its credit facilities which support underwriting obligations.



The 2019 Project Transform team

### The Foundation in action: Project Transform

"Seven members of staff from across the Group were chosen to join the 2019 Project Transform trip. We all volunteered after listening to the stories and feedback from the previous year's team and wanted to experience for ourselves the amazing work that ICM does with Project Transform. Whilst we had a good idea what the trip involved it wasn't until we were on the ground that we could fully appreciate the extraordinary work that ICM does to help the ultra-poor.

The week involved building toilets for two families, a basic need that we all take for granted. We visited communities for house to house visits with the local pastor and provided health and livelihood lessons to help provide the skills to recognise illness and to provide guidance on starting a small business. We also visited the family academy where local volunteers help mothers to become their children's first teachers and prepare their children for school.

The poverty we saw in the Philippines was heart breaking. To see how these ultra-poor communities live and survive was devastating, but with ICM's help there is hope for these people. We thank Lancashire for giving us this amazing opportunity, anyone can give money to a charity but being able to volunteer and give our time to help was so much more rewarding. For the 2019 team this was something we'll never forget."

### Service providers, including suppliers and contractors

The Group contracts with a number of third parties for the provision of important services to help run its business. Having developed excellent relationships with its service providers, Lancashire is able to work collaboratively with them. This helps us to respond to technological advances and to develop internal systems and infrastructure to operate efficiently.

For all employers within the ancillary services and limited supply chains used by the Group, Lancashire seeks to receive assurance that its service providers pay a living wage. In particular, the Group's UK operation is an accredited Living Wage employer by the Living Wage Foundation.

The Group operates a policy of paying its service providers in accordance with the individual payment terms agreed. The Group's UK subsidiary, LUK, complies with its statutory reporting duty for payment practices and performance in relation to qualifying contracts on a half-yearly basis.

As a service provider in our own right, Lancashire has its own responsibilities to those within its limited supply chain. Any concerns arising over the human rights records of insureds and potential clients would be considered as part of the underwriting process.

### Lenders

The Group has in place a number of long-term debt and financing arrangements with lenders which help to support and fund its underwriting operations and to comply with regulatory capital requirements. The Group's solid relationships with its lenders allow it the flexibility to respond to changing business and economic conditions and to raise capital, when required, to execute its strategy. We routinely publish financial information for the benefit of all our capital providers, including our lenders.

Further details of our long-term debt and financing arrangements are set out in note 18 to the consolidated financial statements from page 162 to 164.



**Team Tango – Bermuda**

### The Foundation in action: Relay for Life

"The Bermuda Relay for Life cancer fundraiser took place on May 17-18 and we had a huge team of almost 100 staff, family and friends participating in the 24-hour event. Team Tango (the LICL team) raised \$24,274 through its participation in 2019's event, which raised some \$707,804 in total.

Bermuda Cancer and Health Centre is a registered charity engaged in the prevention, detection, treatment and support of cancer and other health concerns in the local community. Their vision is to serve the community by building healthier lives free of cancer and disease. Since 2017, residents no longer have to uproot their lives and travel overseas for radiation treatment. The radiation therapy unit at BCHC can treat 95% of all cancers enabling patients to undergo treatment surrounded by family and friends and to participate in their regular daily activities such as work. Funds raised support Bermuda Cancer and Health Centre's Equal Access Fund; ensuring that everyone can utilise the Centre's services (mammography, ultrasound, breast and prostate biopsies and radiation therapy) without a health insurance co-pay, regardless of their level of health insurance or ability to pay."